Student name:\_\_\_\_\_\_\_\_\_\_

**MULTIPLE CHOICE - Choose the one alternative that best completes the statement or answers the question.  
1)** Ultimately, it is the \_\_\_\_\_\_\_\_ who has (have) control over a corporation.

1) \_\_\_\_\_\_

A) bondholders   
 B) classified board  
 C) shareholders  
 D) board of directors  
 E) chief executive officer

**2)** A classified board is one which has:

2) \_\_\_\_\_\_

A) representation from various classes of stock.   
 B) terms that expire at different times.  
 C) both employee and non-employee directors.  
 D) directors elected solely by one class of shareholders.  
 E) directors that have been assigned differing numbers of votes per seat.

**3)** Preferred stock dividends:

3) \_\_\_\_\_\_

A) become a debt of the firm if unpaid.   
 B) can be deferred indefinitely.  
 C) are paid only if common stock dividends are also paid.  
 D) have priority over debt interest payments but not over common stock dividends.  
 E) are a tax-deductible business expense.

**4)** Why might a firm prefer to issue cumulative preferred stock rather than?

4) \_\_\_\_\_\_

A) If there is no current taxable income, preferred stock dividends are automatically voided.   
 B) Preferred stock has no voting rights but debt does.  
 C) Preferred dividends provide a tax shield but debt does not.  
 D) Corporate investors can receive a tax break on dividends received.  
 E) Dividend payments are tax deductible, interest on debt is not.

**5)** Of the following statements about preferred stock, which one is correct?

5) \_\_\_\_\_\_

A) Unlike dividends paid on common stock, dividends paid on preferred stock are a tax-deductible expense.   
 B) Dividends on preferred stock payable during the next twelve months are considered to be a corporate liability.  
 C) If preferred dividends are non-cumulative, then preferred dividends not paid in a particular year will be carried forward to the next year.  
 D) There is no significant difference in the voting rights granted to preferred and common shareholders.  
 E) Preferred stock usually has a stated liquidating value of $100 per share.

**6)** A \_\_\_\_\_\_\_\_ grants authority to someone other than the shareholder to vote shares of stock.

6) \_\_\_\_\_\_

A) power-of-share authorization   
 B) proxy  
 C) share authority grant (SAG)  
 D) restricted conveyance  
 E) general right of execution

**7)** Assume a firm has issued cumulative preferred stock but has not paid any of the dividends. This situation may result in:

7) \_\_\_\_\_\_

A) preferred dividend arrearages that can be eliminated only after all common dividends are paid.   
 B) increased taxes based on the amount of the dividend arrearage.  
 C) the permanent forfeiture of all unpaid past dividends but the resumption of future dividends.  
 D) the issuer being forced into repaying all preferred shareholders the stated value of their shares.  
 E) voting rights being granted to preferred shareholders.

**8)** Alpha owns 15 percent of Omega Corporation. What tax benefit does ALPHA derive from this situation?

8) \_\_\_\_\_\_

A) Alpha receives no tax benefit but Omega is taxed on only 30 percent of its net income.   
 B) Alpha is able to treat any Omega dividends it receives as interest income.  
 C) Fifty percent of the dividends paid by Omega to Alpha is exempt from income taxes.  
 D) Alpha can exclude 30 percent of any Omega dividends received from its taxable income.  
 E) All dividend income Alpha receives from Omega is tax-exempt.

**9)** Assume you own 1,000 shares of stock in a firm for which four directors’ seats are up for election. If you have been granted a total of 4,000 votes to cast in a single election, then the firm uses \_\_\_\_\_\_\_\_ voting.

9) \_\_\_\_\_\_

A) cumulative   
 B) absolute priority  
 C) sequential  
 D) straight  
 E) market share

**10)** Assume you own 1,000 shares of stock in a firm for which four directors’ seats are up for election. If you can cast 1,000 votes in each of the four elections, then the firm uses \_\_\_\_\_\_\_\_ voting.

10) \_\_\_\_\_\_

A) cumulative   
 B) absolute priority  
 C) sequential  
 D) straight  
 E) market share

**11)** A \_\_\_\_\_\_\_\_ is when a group other than the current management team solicits the authority to vote shares as part of an effort to replace the current management team.

11) \_\_\_\_\_\_

A) proxy fight   
 B) stockholder derivative action  
 C) tender offer  
 D) vote of confidence  
 E) seniority turnover

**12)** Shareholders obtain the right \_\_\_\_\_\_\_\_ when they are granted preemptive rights.

12) \_\_\_\_\_\_

A) to elect members to the board of directors   
 B) to share proportionally in regular and liquidating dividends  
 C) of first refusal for their proportionate percentage of new shares offered  
 D) to receive dividends prior to any preferred shareholders  
 E) to resell their shares to the issuer at any time at a predetermined price

**13)** Why might a firm issue different classes of stock? In order to:

13) \_\_\_\_\_\_

A) allow a certain group to maintain ownership control while reducing that group’s equity position.   
 B) reduce the firm’s dividend obligation.  
 C) fool investors.  
 D) extract perquisites from one class of shareholders without the other class of shareholders knowing.  
 E) distinguish the time periods in which the various shares were issued.

**14)** Taking control of a corporation would be hardest to do if the corporation uses:

14) \_\_\_\_\_\_

A) cumulative voting with annual elections for each seat.   
 B) cumulative voting with an annual board.  
 C) straight voting with a staggered board.  
 D) cumulative voting with a staggered board.  
 E) straight voting with annual elections for each seat.

**15)** Shareholders are *not* generally granted the:

15) \_\_\_\_\_\_

A) right to elect individuals to the board of directors.   
 B) right to purchase shares of any new stock issue.  
 C) right to receive proportional dividends.  
 D) right to vote to approve or reject a merger offer.  
 E) first right to liquidation proceeds.

**16)** Which one of the following statements is true?

16) \_\_\_\_\_\_

A) Bondholders are generally granted voting rights equal to those of common shareholders.   
 B) Payments of both interest and dividends are tax deductible as business expenses.  
 C) Unpaid common stock dividends can force a firm into liquidation.  
 D) Debt increases the possibility of financial distress.  
 E) Debt holders have a residual claim on a firm’s assets.

**17)** Unsecured corporate debt is commonly referred to as:

17) \_\_\_\_\_\_

A) an indenture.   
 B) a debenture.  
 C) deferred debt.  
 D) protected debt.  
 E) collateralized debt.

**18)** \_\_\_\_\_\_\_\_ grant the issuer the right to extinguish the debt prior to maturity.

18) \_\_\_\_\_\_

A) Put bonds   
 B) Debentures  
 C) Callable bonds  
 D) Subordinated bonds  
 E) Covenant bonds

**19)** The \_\_\_\_\_\_\_\_ is the written agreement between a corporation and its bondholders.

19) \_\_\_\_\_\_

A) collateral agreement   
 B) note  
 C) indenture  
 D) conveyance  
 E) legal understanding

**20)** Ideally, corporations try to create securities that have the tax benefits:

20) \_\_\_\_\_\_

A) of equity but the bankruptcy benefits of debt.   
 B) and bankruptcy benefits of debt.  
 C) and bankruptcy benefits of equity.  
 D) of debt and the equity benefits of dividends.  
 E) of debt but the bankruptcy benefits of equity.

**21)** If an issuer retires a debt issue before its maturity, the amount paid to do so is called the:

21) \_\_\_\_\_\_

A) amortized payoff.   
 B) call price.  
 C) sinking fund amount.  
 D) the discount.  
 E) par or face amount.

**22)** A subordinated debt:

22) \_\_\_\_\_\_

A) has a higher priority status than secured creditors.   
 B) is secondary to equity.  
 C) must give preference to the secured creditors in the event of default.  
 D) has been issued because the company is in default.  
 E) is treated as an equity security.

**23)** The written agreement between a corporation and its bondholders might contain a prohibition against paying dividends in excess of current earnings. This prohibition is an example of a(n):

23) \_\_\_\_\_\_

A) maintenance of security provision.   
 B) collateral restriction.  
 C) affirmative indenture.  
 D) negative covenant.  
 E) put provision.

**24)** Which one of these is *not* included in the indenture?

24) \_\_\_\_\_\_

A) Bond seniority   
 B) Registered owner  
 C) Protective covenant  
 D) Call provision  
 E) Repayment arrangements

**25)** If a bond issue is callable, the call price generally is:

25) \_\_\_\_\_\_

A) less than par value.   
 B) variable based on the market rate of interest.  
 C) equal to par value.  
 D) constant over the life of the debt.  
 E) set so it decreases as the bond approaches maturity.

**26)** Historically in the U.S., corporate bonds have generally been issued with a par value of:

26) \_\_\_\_\_\_

A) $100.   
 B) $5,000.  
 C) $500.  
 D) $10,000.  
 E) $1,000.

**27)** A blanket mortgage is securitized by:

27) \_\_\_\_\_\_

A) the sinking fund.   
 B) the borrower’s inventory.  
 C) all the borrower’s real property.  
 D) the good faith and credit of the borrower.  
 E) the borrower’s inventories and accounts receivables.

**28)** Sinking fund arrangements are *least* likely to include which one of the following requirements?

28) \_\_\_\_\_\_

A) A deferred provision for the first few years   
 B) A one-time repayment of the entire principal and interest at maturity  
 C) A balloon payment  
 D) Equal payments of principal over the life of the bond  
 E) Sufficient payments over the bonds’ life to retire the entire bond issue

**29)** If a bond has a make-whole call provision, the:

29) \_\_\_\_\_\_

A) call premium can be either positive or negative.   
 B) bond’s market price will always equal its face value.  
 C) bondholder will receive the face value amount plus interest if the bond is called.  
 D) bondholder will receive the face value amount minus any interest paid to date if the bond is called.  
 E) call price will increase as interest rates decrease.

**30)** Which one of thefollowing statements is a positive covenant?

30) \_\_\_\_\_\_

A) The firm must maintain a current ratio of 1.2 or better.   
 B) The firm will not issue any debt with higher seniority.  
 C) The firm cannot be acquired in a friendly takeover.  
 D) No dividend increases will be allowed.  
 E) The market debt-equity ratio cannot exceed .60.

**31)** Which one of the following statements applies to floating-rate bonds?

31) \_\_\_\_\_\_

A) Bondholders can generally redeem their bonds at par at any time.   
 B) Coupon payments are variable while the par value is fixed.  
 C) Interest adjustments are accrued and paid on the maturity date.  
 D) Coupon payments are fixed but the par value is variable.  
 E) Bondholders frequently are granted a put provision at the current market price.

**32)** Which type of bond grants the bondholder the right to force the bond’s issuer to repay the bond at a stated price given that a certain situation(s) occurs?

32) \_\_\_\_\_\_

A) Put bond   
 B) Cat bond  
 C) NoNo bond  
 D) Income bond  
 E) Warrant bond

**33)** Bonds with attached warrants are frequently issued:

33) \_\_\_\_\_\_

A) with very low coupons.   
 B) at a greatly discounted price.  
 C) with an attached share of preferred stock.  
 D) with a share purchase price set equal to the market price at time of share purchase.  
 E) with an attached share of common stock.

**34)** A(n) \_\_\_\_\_\_\_\_ bond pays coupon payments only if it can do so from the income earned by the firm.

34) \_\_\_\_\_\_

A) interest-only bond   
 B) sustainability bond  
 C) floater bond  
 D) LIBOR-based bond  
 E) income bond

**35)** Which type of bond is a city or state most likely to use as a means of offsetting its cost of damages caused by a hurricane?

35) \_\_\_\_\_\_

A) Convertible bond   
 B) Sustainability bond  
 C) Cat bond  
 D) Put bond  
 E) CoCo bond

**36)** Which set of circumstances would best ensure that the price of a bond with attached warrants will increase given no change in the bond’s credit quality or terms?

36) \_\_\_\_\_\_

A) An increase in both the market rate of interest and the underlying stock price   
 B) A decrease in the market rate of interest and an increase in the underlying stock price  
 C) An increase in the market rate of interest and a decrease in the underlying stock price  
 D) A decrease in both the market rate of interest and the underlying stock price  
 E) A decrease in the market rate of interest with no change in the underlying stock price

**37)** A revolving bank line of credit:

37) \_\_\_\_\_\_

A) generally requires the borrower to borrow the entire credit line amount at some point in time.   
 B) generally involves a fee charged to the borrower on the unused portion of the revolver.  
 C) may only be offered for periods of one year or less.  
 D) generally is free of charge until money is actually borrowed.  
 E) allows the borrower to determine the amount of credit to be granted.

**38)** Which one of these statements correctly applies to either a leveraged or an unleveraged syndicated loan?

38) \_\_\_\_\_\_

A) The loan will always be rated as investment grade.   
 B) The loan may not be publicly traded.  
 C) The loan arranger is not involved with the actual lending.  
 D) Each bank that participates negotiates the terms for its portion of the overall loan.  
 E) Each bank has its own loan agreement with the borrowers.

**39)** Which of the following characteristics does *not* apply to Eurobonds?

39) \_\_\_\_\_\_

A) Commonly traded from London   
 B) Always denominated in euros  
 C) Always denominated in a single currency  
 D) Generally denominated in the issuer’s home currency  
 E) Issued in multiple countries

**40)** Bulldog bonds are associated with:

40) \_\_\_\_\_\_

A) Spain.   
 B) Great Britain.  
 C) France.  
 D) Germany.  
 E) Morocco.

**41)** Rembrandt bonds are associated with:

41) \_\_\_\_\_\_

A) the Netherlands.   
 B) Switzerland.  
 C) Germany.  
 D) Belgium.  
 E) Austria and Hungary.

**42)** The term *financial deficit* is defined as the:

42) \_\_\_\_\_\_

A) loss realized on bonds that are sold for less than their purchase price.   
 B) amount needed to fund all interest payments on currently outstanding debt.  
 C) total amount of cash flow required from all sources to meet the needs of the uses of cash.  
 D) amount of cash flow that must be funded internally.  
 E) uses of cash flow minus the cash flow available from internal sources.

**43)** What is the predominant source of financing for positive NPV projects by U.S. nonfinancial corporations?

43) \_\_\_\_\_\_

A) Preferred stock   
 B) Internally generated funds  
 C) Common stock  
 D) Publicly issued debt  
 E) Privately issued debt

**44)** Recently, U.S. nonfinancial corporations have been:

44) \_\_\_\_\_\_

A) net repurchasers of stock.   
 B) issuing new shares of stock in record numbers.  
 C) primarily relying on external debt.  
 D) paying off external debt at a record pace.  
 E) net issuers of stock.

**45)** Since 1975, U.S. nonfinancial corporations have tended to have debt-equity ratios that are:

45) \_\_\_\_\_\_

A) steadily rising due to the low interest rate environment.   
 B) less than 1.0.  
 C) averaging in the .8 to .9 range.  
 D) relatively stable over time.  
 E) relatively unaffected by stock market movements.

**46)** Financial economists prefer to use market values rather than book values when measuring debt ratios because market values are:

46) \_\_\_\_\_\_

A) more stable than book values.   
 B) a better reflection of current information.  
 C) net of taxes.  
 D) used by Standard & Poor’s to measure credit worthiness.  
 E) most commonly required by bond covenants.

**47)** There are three seats on the board of directors of MMT, Incorporated, up for election. The firm has 175,000 shares of stock outstanding and uses cumulative voting. Each share is granted one vote per open seat. You currently own 10,000 shares that have a market value of $23 each. How much must you spend, if anything, to acquire sufficient shares to guarantee your election to the board? Assume no one else votes for you.

47) \_\_\_\_\_\_

A) $1,111,690   
 B) $776,273  
 C) $830,814  
 D) $1,006,273  
 E) $688,230

**48)** There are five seats on the board of directors of Serbone Equity that are up for election. The firm has 320,400 shares of stock outstanding and uses straight voting. Each share is granted one vote for each open seat. How many shares must you control if you want to guarantee your election to the board and no one else votes for you?

48) \_\_\_\_\_\_

A) 53,334   
 B) 64,000  
 C) 160,200  
 D) 160,201  
 E) 64,001

**49)** There are four seats on the board of directors of Heritch Global that up for election. The firm has 160,000 shares of stock outstanding and uses cumulative voting. Each share is granted one vote per open seat. How many shares must you control if you want to guarantee your election to the board and assuming no one else votes for you?

49) \_\_\_\_\_\_

A) 40,000   
 B) 40,001  
 C) 36,001  
 D) 32,000  
 E) 32,001

**50)** Arevalos, Incorporated, has cumulative preferred stock outstanding that calls for quarterly dividend payments of $2.25 per share. Unfortunately, the firm has not paid these preferred dividends for the past three quarters. What amount per share must be paid to the preferred shareholders this quarter if the firm also wants to pay a dividend on its common stock?

50) \_\_\_\_\_\_

A) $9.00   
 B) $6.75  
 C) $4.50  
 D) $11.25  
 E) $13.50

**51)** Analysts estimate that one year from today, a bond has a probability of 40 percent of being priced at $950 and a probability of 60 percent of being priced at $1,050. The bond is also callable at any time at $1,010. What is the expected value of this bond in one year?

51) \_\_\_\_\_\_

A) $995   
 B) $980  
 C) $1,000  
 D) $1,010  
 E) $986

**52)** Analysts estimate that a bond has an equal probability of being priced at either $940 or $1,050 one year from today. The bond is also callable at any time at $1,020. What is the expected value of this bond in one year?

52) \_\_\_\_\_\_

A) $995   
 B) $980  
 C) $1,000  
 D) $1,020  
 E) $940

**53)** You want a seat on the board of directors of Four Keys, Incorporated The company has 275,000 shares of stock outstanding and the stock sells for $58 per share. There are currently 5 seats up for election. The company uses straight voting. How many shares do you need to guarantee that you will be elected to the board?

53) \_\_\_\_\_\_

A) 91,668 shares   
 B) 123,751 shares  
 C) 55,000 shares  
 D) 137,501 shares  
 E) 45,834 shares

**54)** You want a seat on the board of directors of Red Cow, Incorporated The company has 310,000 shares of stock outstanding and the stock sells for $55 per share. There are currently 3 seats up for election. The company uses straight voting. How much will it cost you to guarantee that you will be elected to the board?

54) \_\_\_\_\_\_

A) $5,683,333   
 B) $8,525,055  
 C) $6,393,805  
 D) $7,672,550  
 E) $4,262,555

**55)** You want a seat on the board of directors of Four Keys, Incorporated The company has 230,000 shares of stock outstanding and the stock sells for $63 per share. There are currently 4 seats up for election. If the company uses cumulative voting, how many shares do you need to guarantee that you will be elected to the board?

55) \_\_\_\_\_\_

A) 80,501 shares   
 B) 41,401 shares  
 C) 46,001 shares  
 D) 115,001 shares  
 E) 57,500 shares

**56)** You want a seat on the board of directors of Zeph, Incorporated The company has 300,000 shares of stock outstanding and the stock sells for $55 per share. There are currently 3 seats up for election. If the company uses cumulative voting, how much will it cost you to guarantee that you will be elected to the board?

56) \_\_\_\_\_\_

A) $5,670,076   
 B) $9,450,084  
 C) $12,600,084  
 D) $8,400,000  
 E) $4,125,055

**ESSAY. Write your answer in the space provided or on a separate sheet of paper.  
57)** Identify the general rights that are commonly granted to common stock shareholders.

**58)** Explain some of the means by which a select group of shareholders can retain control over a corporation while still raising equity capital outside of their group.

**59)** Explain the main differences between debt and equity.

**60)** Identify three key duties of a bond trustee.

**61)** Bond issuers will call bonds when it is favorable for them to do so. The benefit the issuer receives is a cost to the bondholders. Explain some of the ways in which bondholders are protected from calls.

**Answer Key**Test name: Chapter 15

1) C

2) B

3) B

4) D

5) E

6) B

7) E

8) C

9) A

10) D

11) A

12) C

13) A

14) C

15) E

16) D

17) B

18) C

19) C

20) E

21) B

22) C

23) D

24) B

25) E

26) E

27) C

28) B

29) E

30) A

31) B

32) A

33) A

34) E

35) C

36) B

37) B

38) E

39) B

40) B

41) A

42) E

43) B

44) A

45) B

46) B

47) B

Total shares needed = [1/(3 + 1)](175,000) + 1  
 Total shares needed = 43,751  
   
 Cost to acquire shares = (43,751 − 10,000)($23)  
 Cost to acquire shares = $776,273

48) D

Shares needed = .5(320,400) + 1  
 Shares needed = 160,201

49) E

Shares needed = [1/(4 + 1)](160,000) + 1  
 Shares needed = 32,001

50) A

Preferred dividend requirement = 4($2.25)  
 Preferred dividend requirement = $9.00

51) E

Expected value = .4($950) + .6($1,010)  
 Expected value = $986

52) B

Expected value = ($940 + 1,020)/2  
 Expected value = $980

53) D

Shares necessary = 275,000/2 + 1 = 137,501 shares

54) B

Shares necessary = 310,000/2 + 1 = 155,001 shares  
   
 Cost = 155,001($55) = $8,525,055

55) C

Shares necessary = {[1/(1 + 4)] × 230,000} + 1 = 46,001 shares

56) E

Shares necessary = {[1/(1 + 3)] × 300,000} + 1 = 75,001 shares  
   
 Cost = 75,001($55) = $4,125,055

57) Common stock shareholders generally have the right to:  
 1.share proportionally in dividends.  
 2.share proportionally in assets remaining after liabilities have been paid in a liquidation.  
 3.vote on stockholder matters of great importance, such as a merger or acquisition.  
 4.vote to elect directors to the board.  
 5.share proportionately in any new stock offering.

58) Some of the means include straight voting for the firm’s directors, staggered terms for the directors, and various classes of stock with unequal voting rights.

59) 1.Debt generally does not provide any voting rights nor company ownership; equity does.  
 2.Interest expense is generally at least partially tax deductible, dividends paid are not.  
 3.Unpaid debt is a liability of the firm and can force the firm to liquidate or reorganize. Unpaid dividends are not a liability of the firm unless declared.  
 4.Interest and dividends are often treated differently for tax purposes.  
 5.Dividends paid to corporate shareholders are at least partially tax exempt; interest is not.

60) 1.Ensure the bond indenture provisions are obeyed  
 2.Manage the sinking fund  
 3.Represent the bondholders if the company defaults on its payments

61) The call provision may have a deferral period which prevents the issuer from calling the bonds within the first few years following issuance. The provision may also require the issuer to pay a call premium to help offset the loss to the bondholder. Some provisions are structured as "make-whole" calls which require the issuer to pay the approximate current value of the called bond to the bondholder.