CHAPTER 25
Mergers and Acquisitions

I. DEFINITIONS

MERGER

a 1. The complete absorption of one company by another, wherein the acquiring firm retains its identity and the acquired firm ceases to exist as a separate entity, is called a:
- a. merger.
- b. consolidation.
- c. tender offer.
- d. spinoff.
- e. divestiture.

CONSOLIDATION

b 2. A merger in which an entirely new firm is created and both the acquired and acquiring firms cease to exist is called a:
- a. divestiture.
- b. consolidation.
- c. tender offer.
- d. spinoff.
- e. conglomeration.

TENDER OFFER

c 3. A public offer by one firm to directly buy the shares of another firm is called a:
- a. merger.
- b. consolidation.
- c. tender offer.
- d. spinoff.
- e. divestiture.

HORIZONTAL ACQUISITION

d 4. The acquisition of a firm in the same industry as the bidder is called a _____ acquisition.
- a. conglomerate
- b. forward
- c. backward
- d. horizontal
- e. vertical

VERTICAL ACQUISITION

e 5. The acquisition of a firm involved with a different production process stage than the bidder is called a _____ acquisition.
- a. conglomerate
- b. forward
- c. backward
- d. horizontal
- e. vertical

CONGLOMERATE ACQUISITION

a 6. The acquisition of a firm whose business is not related to that of the bidder is called a _____ acquisition.
- a. conglomerate
- b. forward
- c. backward
- d. horizontal
- e. vertical

PROXY CONTEST

b 7. An attempt to gain control of a firm by soliciting a sufficient number of stockholder votes to replace the current board of directors is called a:
- a. tender offer.
- b. proxy contest.
- c. going-private transaction.
- d. leveraged buyout.
- e. consolidation.

GOING-PRIVATE TRANSACTION

c 8. A business deal in which all publicly owned stock in a firm is replaced with complete equity ownership by a private group is called a:
- a. tender offer.
- b. proxy contest.
- c. going-private transaction.
- d. leveraged buyout.
- e. consolidation.

LEVERAGED BUYOUT

d 9. Going-private transactions in which a large percentage of the money used to buy the outstanding stock is borrowed is called a:
- a. tender offer.
- b. proxy contest.
- c. merger.
- d. leveraged buyout.
- e. consolidation.

STRATEGIC ALLIANCE

e 10. An agreement between firms to cooperate in pursuit of a joint goal is called a:
- a. consolidation.
- b. merged alliance.
- c. joint venture.
- d. takeover project.
- e. strategic alliance.

JOINT VENTURE

c 11. An agreement between firms to create a separate, co-owned entity established to pursue a joint goal is called a:
a. consolidation.
b. strategic alliance.
c. joint venture.
d. merged alliance.
e. takeover project.

SYNERGY

e 12. The positive incremental net gain associated with the combination of two firms through a merger or acquisition is called:
a. the agency conflict.
b. goodwill.
c. the merger cost.
d. the consolidation effect.
e. synergy.

SUPERMAJORITY AMENDMENT

a 13. A change in the corporate charter making it more difficult for the firm to be acquired by increasing the percentage of shareholders that must approve a merger offer is called a:
a. supermajority amendment.
b. standstill agreement.
c. greenmail provision.
d. poison pill amendment.
e. white knight provision.

STANDSTILL AGREEMENT

b 14. A contract wherein the bidding firm agrees to limit its holdings in the target firm is called a:
a. supermajority amendment.
b. standstill agreement.
c. greenmail provision.
d. poison pill amendment.
e. white knight provision.

GREENMAIL

c 15. The payments made by a firm to repurchase shares of its outstanding stock from an individual investor in an attempt to eliminate a potential unfriendly takeover attempt are referred to as:
a. a golden parachute.
b. standstill payments.
c. greenmail.
d. a poison pill.
e. a white knight.

POISON PILLS

d 16. A financial device designed to make unfriendly takeover attempts financially unappealing, if not impossible, is called:
  a. a golden parachute.
  b. a standstill agreement.
  c. greenmail.
  d. a poison pill.
  e. a white knight.

SHARE RIGHTS PLANS

e 17. Corporate charter provisions allowing existing stockholders to purchase stock at some fixed price in the event of a hostile outside takeover attempt are called:
  a. pac-man defenses.
  b. shark repellent plans.
  c. golden parachute provisions.
  d. greenmail provisions.
  e. share rights plans.

GOLDEN PARACHUTES

a 18. Generous compensation packages paid to a firm’s top management in the event of a takeover are referred to as:
  a. golden parachutes.
  b. poison puts.
  c. white knights.
  d. shark repellents.
  e. bear hugs.

POISON PUTS

b 19. Corporate charter provisions that force the firm to buy back its securities at a set and usually quite high price are called:
  a. golden parachutes.
  b. poison puts.
  c. white knights.
  d. shark repellents.
  e. bear hugs.

WHITE KNIGHTS

c 20. A friendly suitor that a target firm turns to as an alternative to a hostile bidder is called a:
  a. golden suitor.
  b. poison put.
  c. white knight.
  d. shark repellent.
  e. crown jewel.

SHARK REPELLENT

d 21. Any tactic employed by a target firm to discourage unwanted merger offers is referred to as a:
a. golden parachute.
b. poison put.
c. white knight.
d. shark repellent.
e. bear hug.

EQUITY CARVE-OUT

b 22. The sale of stock in a wholly owned subsidiary via an initial public offering is referred to as a(n):
a. split-up.
b. equity carve-out.
c. countertender offer.
d. white knight transaction.
e. lockup transaction.

SPIN-OFF

d 23. The distribution of shares in a subsidiary to existing parent company stockholders is called a(n):
a. lockup transaction.
b. bear hug.
c. equity carve-out.
d. spin-off.
e. split-up.

II. CONCEPTS

ACQUISITIONS

a 24. Which of the following statements concerning acquisitions are correct?
I. Being acquired by another firm is an effective method of replacing senior management.
II. The net present value of an acquisition should have no bearing on whether or not the acquisition occurs.
III. Acquisitions are often relatively complex from an accounting and tax point of view.
IV. The value of a strategic fit is easy to estimate using discounted cash flow analysis.
a. I and III only
b. II and IV only
c. I and IV only
d. I, III, and IV only
e. I, II, III, and IV

MERGER

b 25. In a merger the:

a. legal status of both the acquiring firm and the target firm is terminated.
b. acquiring firm retains its name and legal status.
c. acquiring firm acquires the assets but not the liabilities of the target firm.
d. stockholders of the target firm have little, if any, say as to whether or not the merger occurs.
e. target firm continues to exist as a subsidiary of the acquiring firm.

ACQUISITION OF STOCK

e 26. An acquisition of a firm through the purchase of shares of the outstanding stock:

I. is frequently more expensive than if the two firms had just merged.
II. can be accomplished without the involvement of the target firm's board of directors.
III. can be accomplished without having the shareholders vote on the acquisition.
IV. may be dependent upon the maximum amount of shares made available for sale to the acquiring firm.

a. I and III only
b. II and IV only
c. I, III, and IV only
d. I, II, and III only
e. I, II, III, and IV

VERTICAL ACQUISITION

d 27. When a building supply store acquires a lumber mill they are doing a ______ acquisition.

a. horizontal
b. longitudinal
c. conglomerate
d. vertical
e. complementary resources

STOCK ACQUISITION

c 28. If Microsoft were to acquire U.S. Airways, the acquisition would be classified as a _____ acquisition.

a. horizontal
b. longitudinal
c. conglomerate
d. vertical
e. complementary resources

TAKEOVERS

a 29. Assume that both firm A and firm B formally agree to each put up $10 million to form firm C. The operations of firm C are restricted to conducting research and development activities for the benefit of firms A and B. Firm C is a _____ of firms A and B.

a. joint venture
b. going-private transaction
c. conglomerate
d. subsidiary
e. leveraged buyout

TAKEOVERS

e 30. Which of the following activities are commonly associated with takeovers?

I. the acquisition of assets
II. proxy contests
III. management buyouts
IV. leveraged buyouts

a. I and III only
b. II and IV only
c. I, III, and IV only
d. I, II, and IV only
e. I, II, III, and IV

TAXES AND ACQUISITIONS

c 31. In a tax-free acquisition, the shareholders of the target firm:

a. receive income that is considered to be tax-exempt.
b. gift their shares to a tax-exempt organization and therefore have no taxable gain.
c. are viewed as having exchanged their shares.
d. sell their shares to a qualifying entity thereby avoiding both income and capital gains taxes.
e. sell their shares at cost thereby avoiding the capital gains tax.

PURCHASE ACCOUNTING METHOD

d 32. The purchase accounting method requires that:

a. the excess of the purchase price over the fair market value of the target firm be recorded as a one-time expense on the income statement of the acquiring firm.
b. goodwill be amortized on a yearly basis.
c. the equity of the acquiring firm be reduced by the excess of the purchase price over the fair market value of the target firm.
d. the assets of the target firm be recorded at their fair market value on the balance sheet of the acquiring firm.
e. the excess amount paid for the target firm be recorded as a tangible asset on the books of the acquiring firm.

PURCHASE ACCOUNTING METHOD

b 33. Goodwill created by an acquisition:

a. affects the cash flows of the acquiring firm on an annual basis for a period of years.
b. must be reviewed each year to determine its current value to the firm.
c. reduces the taxable income of the firm as it is expensed.
d. has no effect on the reported earnings of a firm when it is expensed.
e. is recorded in an amount equal to the fair market value of the assets of the target firm.

POOLING OF INTERESTS

d 34. The pooling of interests method of accounting:

I. creates an account called goodwill which is recorded on the balance sheet of the merged firm.
II. consists of simply combining the balance sheets of the acquiring and the target firms.
III. is no longer permitted by FASB.
IV. acknowledges the excess of the purchase price over the fair market value and records this amount on the balance sheet of the acquiring firm.

a. I and III only
b. I and IV only
c. II and IV only
d. II and III only
e. I, II, and IV only

INCREMENTAL CASH FLOWS

c 35. The incremental cash flows of a merger can relate to changes in which of the following?

I. revenues
II. number of authorized shares of stock
III. taxes
IV. capital requirements

a. I and II only
b. II, III, and IV only
c. I, III, and IV only
d. I, II, and III only
e. I, II, III, and IV

SYNERGY

e 36. Which one of the following statements illustrates a synergistic effect of a merger?

a. The revenue of the combined firm is equal to the revenue of the acquiring firm plus the revenue of the target firm.
b. The costs of the combined firm exceeds the costs of the acquiring firm plus the costs of the target firm.
c. The tax liability of the combined firm is greater than the summation of the tax liabilities of each separate firm.
d. The depreciation expense of the combined firm is equivalent to the depreciation expense of the acquiring firm plus the depreciation expense of the target firm.
e. The capital requirements of the combined firm are less than the summation of the capital requirements of each separate firm.

SYNERGY

d 37. A potential merger that has synergy:

a. should be rejected due to the projected negative cash flows.
b. should be rejected because synergy destroys firm value.
c. has a net present value of zero and thus returns the minimal required rate of return.
d. creates value and therefore should be pursued.
e. reduces the anticipated net income of the acquiring firm.

SYNERGY

d 38. A proposed acquisition may create synergy by:
I. increasing the market power of the combined firm.
II. improving the distribution network of the acquiring firm.
III. providing the combined firm with a strategic advantage.
IV. reducing the utilization of the acquiring firm's assets.
a. I and III only
b. II and III only
c. I and IV only
d. I, II, and III only
e. I, II, III, and IV

ACQUISITION GAINS

c 39. Which of the following represent potential tax gains from an acquisition?
I. a reduction in the level of debt
II. an increase in surplus funds
III. the use of net operating losses
IV. an increased use of leverage
a. I and IV only
b. II and III only
c. III and IV only
d. I and III only
e. II, III, and IV only

ACQUISTION CONSIDERATIONS

c 40. When evaluating an acquisition you should:
a. concentrate on book values and ignore market values.
b. focus on the total cash flows of the merged firm.
c. apply the rate of return that is relevant to the incremental cash flows.
d. ignore any one-time acquisition fees or transaction costs.
e. ignore any potential changes in management.

ACQUISITIONS AND EARNINGS PER SHARE

b 41. If an acquisition does not create value, then the:
a. earnings per share of the acquiring firm must be the same both before and after the acquisition.
b. earnings per share can change but the stock price of the acquiring firm should remain constant.
c. price per share of the acquiring firm should increase because of the growth of the firm.
d. earnings per share will most likely increase while the price-earnings ratio remains constant.
e. price-earnings ratio should remain constant regardless of any changes in the earnings per share.

ACQUISITION EFFECTS

c 42. Which one of the following statements is correct?
- a. Acquiring firms tend to avoid firms with large net operating losses when they are seeking a target firm to acquire.
- b. If an acquisition increases the debt level of a firm the tax liability of the firm tends to increase as a result.
- c. If either an increase or a decrease in the level of production causes the average cost per unit to increase the firm is currently operating at its optimal size.
- d. Firms can always benefit from economies of scale if they increase the size of their firm through acquisitions.
- e. If a firm uses its surplus cash to acquire another firm the shareholders of the acquiring firm immediately incur a tax liability related to the transaction.

COMPLEMENTARY RESOURCES

b 43. Which one of the following combinations of firms would benefit the most through the use of complementary resources?
- a. a ski resort and a travel trailer sales outlet
- b. a golf resort and a ski resort
- c. a hotel and a home improvement center
- d. a swimming pool distributor and a kitchen designer
- e. a fast food restaurant and a dry cleaner

COMPLEMENTARY RESOURCES

a 44. Which one of the following is most likely a good candidate for an acquisition that could benefit from the use of complementary resources?
- a. a sports arena that is home only to an indoor hockey team
- b. a hotel in a busy downtown business district of a major city
- c. a day care center located near a major route into the main business district of a large city
- d. an amusement park located in a centralized Florida location
- e. a fast food restaurant located near a major transportation hub

INEFFICIENT MANAGEMENT

a 45. The shareholders of a target firm benefit the most when:
- a. an acquiring firm has the better management team and replaces the target firm’s managers.
- b. the management of the target firm is more efficient than the management of the acquiring firm which replaces them.
- c. the management of both the acquiring firm and the target firm are as equivalent as possible.
- d. their current management team is kept in place even though the managers of the acquiring firm are more suited to manage the target firm’s situation.
- e. their management team is technologically knowledgeable yet ineffective.

ACQUISITION GAINS

c 46. Which of the following represent potential gains from an acquisition?

I. the replacement of ineffective managers
II. lower costs per unit produced
III. an increase in firm size so that diseconomies of scale are realized
IV. spreading of overhead costs

a. II and III only
b. I and IV only
c. I, II, and IV only
d. I, III, and IV only
e. I, II, III, and IV

EFFECTS OF ACQUISITIONS

d 47. Which one of the following statements is correct?

a. A firm must realize some synergy as a result of a merger if the earnings per share of the acquiring firm increase.
b. Any diversification achieved through a merger is valued by investors.
c. Any increase in earnings per share due to a merger provides financial reasoning for an increase in the stock price per share.
d. Firms with surplus cash need to justify an acquisition as having a business purpose other than the avoidance of a dividend distribution.
e. Diversification is one of the greatest benefits derived from an acquisition.

COST OF AN ACQUISITION

a 48. The value of a target firm to the acquiring firm is equal to:

a. the value of the target firm as a separate entity plus the incremental value derived from the acquisition.
b. the purchase cost of the target firm.
c. the value of the merged firm minus the value of the target firm as a separate entity.
d. the purchase cost plus the incremental value derived from the acquisition.
e. the incremental value derived from the acquisition.

CASH VERSUS STOCK ACQUISITION

c 49. Which one of the following statements is correct?

a. If an acquisition is made with cash then the cost of that acquisition is dependent upon the acquisition gains.
b. Acquisitions made by exchanging shares of stock are normally taxable transactions.
c. The management of an acquiring firm may put itself at risk of losing control of the firm if they do acquisitions using shares of stock.
d. The stockholders of the acquiring firm will be better off when an acquisition results in losses if the acquisition was made with cash rather than with stock.
e. Acquisitions based on legitimate business purposes are not taxable transactions regardless of the means of financing used.

DEFENSIVE TACTICS

b 50. The primary purpose of a flip-in provision is to:

a. increase the number of shares outstanding while also increasing the value per share.
b. dilute a corporate raider's ownership position thereby increasing the cost of a takeover.
c. reduce the market value of each share of stock.
d. give the existing corporate directors the sole right to remove a poison pill.
e. provide additional compensation to any senior manager who loses their job as a result of a corporate takeover.

DEFENSIVE TACTICS

c 51. If a firm wants to take over another firm but feels the attempt to do so will be viewed as unfriendly they could decide to take a _____ approach to the acquisition.

a. crown jewel
b. shark repellent
c. bear hug
d. countertender offer
e. lockup

ACQUISITION EFFECTS ON STOCKHOLDERS

d 52. Which of the following have been suggested as reasons why the stockholders in acquiring firms may not benefit to any significant degree from an acquisition?

I. the price paid for the target firm might equal that firm's total value
II. management may have priorities other than the interest of the stockholders
III. the target firms tend to be much larger than the acquiring firms
IV. the merger benefits may have been underestimated

a. I and III only
b. II and IV only
c. III and IV only
d. I and II only
e. I and IV only

DIVESTITURES AND RESTRUCTURINGS

e 53. Which of the following are reasons why a firm may want to divest itself of some of its assets?

I. to raise cash
II. to get rid of unprofitable operations
III. to get rid of some assets received in an acquisition
IV. to cash in on some profitable operations

a. I and II only
b. I, II, and III only
c. I, III, and IV only
d. II, III, and IV only
e. I, II, III, and IV

DIVESTITURES AND RESTRUCTURINGS

a 54. Which one of the following statements is correct?
- a. A spin-off frequently follows an equity carve-out.
- b. A split-up frequently follows a spin-off.
- c. An equity carve-out is a specific type of acquisition.
- d. A spin-off involves an initial public offering.
- e. A divestiture means that the original firm ceases to exist.

III. PROBLEMS

GOODWILL

b 55. Turner, Inc. has $4.2 million in net working capital. The firm has fixed assets with a book value of $48.6 million and a market value of $53.4 million. Martin & Sons is buying Turner, Inc. for $60 million in cash. The acquisition will be recorded using the purchase accounting method. What is the amount of goodwill that Martin & Sons will record on their balance sheet as a result of this acquisition?
- a. $0
- b. $2.4 million
- c. $6.6 million
- d. $7.2 million
- e. $11.4 million

MERGER PREMIUM

a 56. Rudy's, Inc. and Blackstone, Inc. are all-equity firms. Rudy's has 1,500 shares outstanding at a market price of $22 a share. Blackstone has 2,500 shares outstanding at a price of $38 a share. Blackstone is acquiring Rudy's for $36,000 in cash. What is the merger premium per share?
- a. $2.00
- b. $4.25
- c. $6.50
- d. $8.00
- e. $14.00

MERGER PREMIUM

b 57. Jennifer's Boutique has 2,100 shares outstanding at a market price per share of $26. Sally's has 3,000 shares outstanding at a market price of $41 a share. Neither firm has any debt. Sally's is acquiring Jennifer's for $58,000 in cash. What is the merger premium per share?
- a. $1.43
- b. $1.62
- c. $1.81
- d. $2.04
- e. $2.07

VALUE OF FIRM B TO A

c 58. Jennifer's Boutique has 2,100 shares outstanding at a market price per share of $26. Sally's has 3,000 shares outstanding at a market price of $41 a share. Neither firm has any debt. Sally's is acquiring Jennifer's for $58,000 in cash. The incremental value of the acquisition is $2,500. What is the value of Jennifer's Boutique to Sally's?

a. $26,000
b. $27,600
c. $57,100
d. $58,200
e. $60,500

VALUE OF FIRM B TO A

d 59. Rudy's, Inc. and Blackstone, Inc. are all-equity firms. Rudy's has 1,500 shares outstanding at a market price of $22 a share. Blackstone has 2,500 shares outstanding at a price of $38 a share. Blackstone is acquiring Rudy's for $36,000 in cash. The incremental value of the acquisition is $3,500. What is the value of Rudy's Inc. to Blackstone?

a. $30,000
b. $32,500
c. $33,000
d. $36,500
e. $39,500

CASH ACQUISITION

b 60. ABC and XYZ are all-equity firms. ABC has 1,750 shares outstanding at a market price of $20 a share. XYZ has 2,500 shares outstanding at a price of $28 a share. XYZ is acquiring ABC for $36,000 in cash. The incremental value of the acquisition is $3,000. What is the net present value of acquiring ABC to XYZ?

a. $1,000
b. $2,000
c. $3,000
d. $4,000
e. $5,000

CASH ACQUISITION

d 61. Firm A is acquiring Firm B for $40,000 in cash. Firm A has 2,500 shares of stock outstanding at a market value of $18 a share. Firm B has 1,500 shares of stock outstanding at a market price of $25 a share. Neither firm has any debt. The net present value of the acquisition is $2,500. What is the value of Firm A after the acquisition?

a. $40,000
b. $42,500
c. $45,000
d. $47,500
e. $50,000

CASH ACQUISITION

c 62. Firm A is acquiring Firm B for $25,000 in cash. Firm A has 2,000 shares of stock outstanding at a market value of $21 a share. Firm B has 1,200 shares of stock outstanding at a market price of $17 a share. Neither firm has any debt. The net present value of the acquisition is $1,500. What is the price per share of Firm A after the acquisition?

a. $21.00
b. $21.25
c. $21.75
d. $22.00
e. $22.50

CASH ACQUISITION

a 63. Alto and Solo are all-equity firms. Alto has 2,400 shares outstanding at a market price of $24 a share. Solo has 4,000 shares outstanding at a price of $17 a share. Solo is acquiring Alto for $63,000 in cash. The incremental value of the acquisition is $5,500. What is the net present value of acquiring Alto to Solo?

a. $100
b. $400
c. $1,200
d. $2,400
e. $5,500

CASH ACQUISITION

c 64. Principal, Inc. is acquiring Secondary Companies for $29,000 in cash. Principal has 2,500 shares of stock outstanding at a market price of $30 a share. Secondary has 1,600 shares of stock outstanding at a market price of $15 a share. Neither firm has any debt. The net present value of the acquisition is $4,500. What is the price per share of Principal after the acquisition?

a. $30.00
b. $30.70
c. $31.80
d. $32.10
e. $32.50

STOCK ACQUISITION

c 65. Winslow Co. has agreed to be acquired by Ferrier, Inc. for $25,000 worth of Ferrier stock. Ferrier currently has 1,500 shares of stock outstanding at a price of $21 a share. Winslow has 1,000 shares outstanding at a price of $22. The incremental value of the acquisition is $4,000. What is the merger premium per share?

a. $1
b. $2
c. $3
d. $4
e. $5

STOCK ACQUISITION

c 66. Winslow Co. has agreed to be acquired by Ferrier, Inc. for $25,000 worth of Ferrier stock. Ferrier currently has 1,500 shares of stock outstanding at a price of $21 a share. Winslow has 1,000 shares outstanding at a price of $22. The incremental value of the acquisition is $4,000. What is the value of Winslow Co. to Ferrier, Inc.?

a. $24,000
b. $25,000
c. $26,000
d. $28,000
e. $29,000

STOCK ACQUISITION

e 67. Brite Industries has agreed to merge with Nu-Day, Inc. for $20,000 worth of Nu-Day stock. Brite has 1,200 shares of stock outstanding at a price of $15 a share. Nu-Day has 2,000 shares outstanding with a market value of $19 a share. The incremental value of the acquisition is $3,500. What is the value of Nu-Day after the merger?

a. $53,000
b. $54,250
c. $56,000
d. $57,750
e. $59,500

STOCK ACQUISITION

a 68. Goodday & Sons is being acquired by Baker, Inc. for $19,000 worth of Baker stock. Baker has 1,500 shares of stock outstanding at a price of $25 a share. Goodday has 1,000 shares outstanding with a market value of $16 a share. The incremental value of the acquisition is $2,000. How many new shares of stock will be issued to complete this acquisition?

a. 760.0 shares
b. 840.0 shares
c. 960.0 shares
d. 1,187.5 shares
e. 1,312.5 shares

STOCK ACQUISITION

e 69. Holiday & Sons is being acquired by Miller's, Inc. for $20,000 worth of Miller's stock. Miller has 1,300 shares of stock outstanding at a price of $20 a share. Holiday has 1,000 shares outstanding with a market value of $18 a share. The incremental value of the acquisition is $2,000. What is the total number of shares in the new firm?

a. 1,000 shares
b. 1,300 shares
c. 1,500 shares
d. 2,000 shares
e. 2,300 shares

STOCK ACQUISITION

d 70. Firm A is being acquired by Firm B for $24,000 worth of Firm B stock. The incremental value of the acquisition is $3,500. Firm A has 1,500 shares of stock outstanding at a price of $15 a share. Firm B has 1,200 shares of stock outstanding at a price of $30 a share. What is the value per share of Firm B after the acquisition?

a. $17.50
b. $24.00
c. $30.00
d. $31.00
e. $35.00

STOCK ACQUISITION

b 71. Firm X is being acquired by Firm Y for $35,000 worth of Firm Y stock. The incremental value of the acquisition is $2,500. Firm X has 2,000 shares of stock outstanding at a price of $16 a share. Firm Y has 1,200 shares of stock outstanding at a price of $40 a share. What is the actual cost of the acquisition using company stock?

a. $34,750
b. $34,789
c. $35,000
d. $35,289
e. $35,500

STOCK ACQUISITION

c 72. Firm Q is being acquired by Firm S for $30,000 worth of Firm S stock. The incremental value of the acquisition is $2,000. Firm Q has 1,900 shares of stock outstanding at a price of $15 a share. Firm S has 1,500 shares of stock outstanding at a price of $40 a share. What is the net present value of the acquisition given that the actual cost of the acquisition using company stock is $30,167?

a. $167
b. $225
c. $333
d. $425
e. $433

EARNINGS AND VALUATION

d 73. The Sligo Co. is planning on merging with the Thorton Co. Sligo will pay Thorton's stockholders the current value of their stock in shares of Sligo. Sligo currently has 2,300 shares of stock outstanding at a market price of $20 a share. Thorton has 1,800 shares outstanding at a price of $15 a share. How many shares of stock will be outstanding in the merged firm?

a. 1,800 shares
b. 2,300 shares
c. 2,750 shares
d. 3,650 shares
e. 4,100 shares

EARNINGS AND VALUATION

b 74. Firm A is planning on merging with Firm B. Firm A will pay Firm B's stockholders the current value of their stock in shares of Firm A. Firm A currently has 2,300 shares of stock outstanding at a market price of $20 a share. Firm B has 1,800 shares outstanding at a price of $15 a share. The after-merger earnings will be $6,500. What will the earnings per share be after the merger?

a. $1.67
b. $1.78
c. $1.83
d. $1.87
e. $1.92

EARNINGS AND VALUATION

a 75. Firm A is planning on merging with Firm B. Firm A will pay Firm B's stockholders the current value of their stock in shares of Firm A. Firm A currently has 2,300 shares of stock outstanding at a market price of $20 a share. Firm B has 1,800 shares outstanding at a price of $15 a share. What is the value of the merged firm?

a. $73,000
b. $75,000
c. $76,667
d. $77,778
e. $78,000

EARNINGS AND VALUATION

d 76. Firm A is planning on merging with Firm B. Firm A will pay Firm B's stockholders the current value of their stock in shares of Firm A. Firm A currently has 2,300 shares of stock outstanding at a market price of $20 a share. Firm B has 1,800 shares outstanding at a price of $15 a share. What is the value per share of the merged firm?

a. $19.00
b. $19.18
c. $19.44
d. $20.00
e. $20.33

IV. ESSAYS

MERGER GAINS

77. The empirical evidence strongly indicates that the stockholders of the target firm realize large wealth gains as a result of a takeover bid but the stockholders in the acquiring firm gain little, if anything. Although there exists no definitive answer as to why this is the case, several possible explanations have been proposed. List and explain three of these possible explanations for the minimal returns to the acquiring firm's stockholders.

Size differentials, competition in the takeover market, lack of achieving merger gains, management goals other than the best interests of the shareholders, and early announements of corporate acquisition intent are all presented as possible explanations in the textbook.

FORMS OF ACQUISITION

78. Describe the three basic legal procedures that one firm can use to acquire another and briefly discuss the advantages and disadvantages of each.

    The three forms are merger, acquisition of stock, and acquisition of assets. A merger has the advantage that it is legally simple and therefore low cost but it has the disadvantage that it must be approved by the shareholders of both firms. Acquisition by stock requires no shareholder meetings and management of the target firm can be bypassed. However, it can be a costly form of acquisition and minority shareholders may hold out, thereby raising the cost of the purchase. An acquisition of assets requires the vote of the target firm's shareholders. However, it can become quite costly to transfer title to all of the assets.

MANAGEMENT INTENT

79. Sometimes the management of a target firm fights a takeover attempt even when that attempt appears to be in the best interest of the shareholders. Why would management take this stance?

    Often, the management of the target firm is replaced after an acquisition. If management believes this may be the case, they may fight the takeover attempt in an effort to maintain their current positions. In other cases, management may fight the attempt if they feel that by doing so, they may increase the amount paid by the acquiring firm.

POISON PILLS

80. Defensive merger tactics are designed to thwart unwanted takeovers and mergers. Do such activities work to the advantage of stockholders all of the time? Are these types of activities ethical? Who do you think benefits most from these activities?

    Good answers will acknowledge that defensive tactics "insulate" existing management from the vagaries of the marketplace and may allow ineffective management to remain in charge. Obviously, defensive maneuvers do not always act in the best interest of shareholders and many students will argue that management benefits most from these activities. The ethics debate about these issues is always an interesting one.