FINANCE (FINC) TEST 1 PRACTICE (SAMPLE)

STUDY GUIDE



SAMPLE STUDY GUIDE WITH LIMITED QUESTIONS

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Introduction

Preparing for a certification exam can feel overwhelming, but with the right tools, it becomes an opportunity to build confidence, sharpen your skills, and move one step closer to your goals. At Examzify, we believe that effective exam preparation isn't just about memorization, it's about understanding the material, identifying knowledge gaps, and building the test-taking strategies that lead to success.

This guide was designed to help you do exactly that.

Whether you're preparing for a licensing exam, professional certification, or entry-level qualification, this book offers structured practice to reinforce key concepts. You'll find a wide range of multiple-choice questions, each followed by clear explanations to help you understand not just the right answer, but why it's correct.

The content in this guide is based on real-world exam objectives and aligned with the types of questions and topics commonly found on official tests. It's ideal for learners who want to:

- Practice answering questions under realistic conditions,
- Improve accuracy and speed,
- Review explanations to strengthen weak areas, and
- Approach the exam with greater confidence.

We recommend using this book not as a stand-alone study tool, but alongside other resources like flashcards, textbooks, or hands-on training. For best results, we recommend working through each question, reflecting on the explanation provided, and revisiting the topics that challenge you most.

Remember: successful test preparation isn't about getting every question right the first time, it's about learning from your mistakes and improving over time. Stay focused, trust the process, and know that every page you turn brings you closer to success.

Let's begin.

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How to Use This Guide

This guide is designed to help you study more effectively and approach your exam with confidence. Whether you're reviewing for the first time or doing a final refresh, here's how to get the most out of your Examzify study guide:

1. Start with a Diagnostic Review

Skim through the questions to get a sense of what you know and what you need to focus on. Your goal is to identify knowledge gaps early.

2. Study in Short, Focused Sessions

Break your study time into manageable blocks (e.g. 30 – 45 minutes). Review a handful of questions, reflect on the explanations.

3. Learn from the Explanations

After answering a question, always read the explanation, even if you got it right. It reinforces key points, corrects misunderstandings, and teaches subtle distinctions between similar answers.

4. Track Your Progress

Use bookmarks or notes (if reading digitally) to mark difficult questions. Revisit these regularly and track improvements over time.

5. Simulate the Real Exam

Once you're comfortable, try taking a full set of questions without pausing. Set a timer and simulate test-day conditions to build confidence and time management skills.

6. Repeat and Review

Don't just study once, repetition builds retention. Re-attempt questions after a few days and revisit explanations to reinforce learning. Pair this guide with other Examzify tools like flashcards, and digital practice tests to strengthen your preparation across formats.

There's no single right way to study, but consistent, thoughtful effort always wins. Use this guide flexibly, adapt the tips above to fit your pace and learning style. You've got this!

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Questions

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1. Which entity carries unlimited liability for all partners?

A. Sole Proprietorship

B. General Partnership

C. Corporation

D. Limited Partnership

2. DuPont Identity: Which components does ROE break into?

A. Operating efficiency, asset use efficiency, and financial leverage

B. Revenue growth, cost control, and tax rate

C. Profit margin, asset turnover, and leverage ratio

D. Liquidity, solvency, and profitability

3. If total assets increase, what must happen on the right-hand side to keep the balance?

A. A matching asset

B. A matching expense

C. A reduction in cash

D. A corresponding increase on the right-hand side (liabilities or equity)

4. The Tax Cuts and Jobs Act of 2017 made federal corporate taxes become a flat rate of:

A. 21%

B. 18%

C. 28%

D. 25%

5. The net working capital to total assets ratio measures the proportion of total assets available to cover short-term obligations.

A. Proportion of Total Assets Available to Cover Short-Term Obligations

B. Proportion of Total Assets Funded by Equity

C. Proportion of Current Assets to Total Assets

D. Net Income Relative to Total Assets

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6. Which statement about beta is true in CAPM?

A. Beta measures unsystematic risk; Ke = Rf + β × RM.

B. Beta measures systematic risk; Ke = Rf + β × (RM − Rf).

C. Beta measures dividend risk; Ke = Rf + β × RM.

D. Beta is irrelevant to expected return; Ke = Rf.

7. Which two methods are commonly used to estimate the cost of equity?

A. Internal Rate of Return and Payback Period

B. CAPM and Dividend Discount Model

C. Net Present Value and Terminal Value

D. Price-to-Earnings and Earnings Growth

8. Which of the following is an example of capital budgeting?

A. Deciding whether to build a new production facility

B. Deciding on daily cash collections

C. Issuing new shares

D. Negotiating loan terms

9. Net working capital is defined as

A. Fixed assets minus current assets

B. Current liabilities minus current assets

C. Total assets minus total liabilities

D. Current assets minus current liabilities

10. If the discount rate r increases, what happens to the present value of an ordinary annuity?

A. Increase

B. Decrease

C. Remains unchanged

D. Becomes negative

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Answers

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1. B
2. A
3. D
4. A
5. A
6. B
7. B
8. A
9. D
10. B

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Explanations

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1. Which entity carries unlimited liability for all partners?

A. Sole Proprietorship

B. General Partnership

C. Corporation

D. Limited Partnership

Unlimited liability means personal assets can be used to satisfy business debts. In a general partnership, all partners share this risk and are personally liable for the partnership's debts, with creditors able to pursue any partner for the full amount. This joint and several liability is what makes unlimited liability apply to all partners. By contrast, corporations limit liability to the amount invested, and limited partnerships restrict the unlimited liability to general partners while limited partners are protected; a sole proprietorship involves a single owner (not multiple partners). So, the structure where every partner has unlimited liability is the general partnership.

2. DuPont Identity: Which components does ROE break into?

A. Operating efficiency, asset use efficiency, and financial leverage

B. Revenue growth, cost control, and tax rate

C. Profit margin, asset turnover, and leverage ratio

D. Liquidity, solvency, and profitability

The main idea being tested is that return on equity can be broken into three driving forces: operating efficiency, asset use efficiency, and financial leverage. In the DuPont view, ROE = (net income / sales) × (sales / total assets) × (total assets / equity). Each factor corresponds to a specific area: operating efficiency reflects how well a company turns sales into profit (profit margin), asset use efficiency shows how effectively assets generate sales (asset turnover), and financial leverage measures how much debt is used relative to equity (the equity multiplier, i.e., financial leverage). So the components are operating efficiency, asset use efficiency, and financial leverage, which is why this option is the best match. The first term captures profitability per dollar of sales, the second shows how efficiently assets are worked to produce sales, and the third gauges the degree of leverage financing the assets, all combining to ROE. Other options mix in elements that aren't the standard three-factor decomposition—revenue growth, cost control, and tax rate describe operating outcomes but aren't the three ROE drivers; liquidity and solvency describe liquidity positions and long-term viability rather than ROE decomposition; and while a version with profit margin, asset turnover, and leverage ratio is similar, the conventional phrasing uses financial leverage for the third component, avoiding ambiguity in what the leverage ratio refers to.

3. If total assets increase, what must happen on the right-hand side to keep the balance?

A. A matching asset

B. A matching expense

C. A reduction in cash

D. A corresponding increase on the right-hand side (liabilities or equity)

In double-entry accounting, the accounting equation must stay in balance: assets equal liabilities plus equity. So when total assets rise, there has to be a matching increase on the right-hand side. That means either liabilities or equity grows to offset the asset increase. For example, borrowing to buy an asset increases cash (an asset) and creates a corresponding liability, or issuing stock or earning revenue increases equity, keeping the equation balanced. The other options don't fit because they don't produce the required offset on the right side or they reduce assets rather than increase them.

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4. The Tax Cuts and Jobs Act of 2017 made federal corporate taxes become a flat rate of:

A. 21%

B. 18%

C. 28%

D. 25%

The key idea is that the Tax Cuts and Jobs Act of 2017 created a single, uniform rate for corporate income tax. It reduced the corporate tax rate from the previous 35% and replaced the graduated/tiered structure with one flat rate applied to all corporate taxable income. This means every dollar of taxable income is taxed at the same percentage, though the actual tax paid can still vary due to credits, deductions, and other provisions in the code. The chosen rate is 21%, which is why this option is correct. The other percentages were not the rate established by the act.

5. The net working capital to total assets ratio measures the proportion of total assets available to cover short-term obligations.

A. Proportion of Total Assets Available to Cover Short-Term Obligations

B. Proportion of Total Assets Funded by Equity

C. Proportion of Current Assets to Total Assets

D. Net Income Relative to Total Assets

This item tests liquidity—how much of a company's resources are available to meet near-term obligations. Net working capital is current assets minus current liabilities, representing the short-term liquidity buffer. When you divide that by total assets, you get the fraction of all assets that are tied up in this short-term buffer: (current assets − current liabilities) / total assets. Interpreting this ratio, a larger value means the firm has a bigger cushion to cover short-term obligations, indicating stronger liquidity; a smaller value signals tighter liquidity. This concept is not about how much of assets are funded by equity (that would be an equity-financing measure), nor about the portion of assets that are current assets (which would be current assets divided by total assets), nor about net income relative to assets (which is return on assets). Therefore, the description that matches is the proportion of total assets available to cover short-term obligations.

6. Which statement about beta is true in CAPM?

A. Beta measures unsystematic risk; $Ke = Rf + \beta \times RM$.

B. Beta measures systematic risk; $Ke = Rf + \beta \times (RM - Rf)$.

C. Beta measures dividend risk; $Ke = Rf + \beta \times RM$.

D. Beta is irrelevant to expected return; $Ke = Rf$.

In CAPM, beta measures systematic risk—the part of an asset's risk that cannot be diversified away. The expected return is $Ke = Rf + \beta (RM - Rf)$, where RM is the expected market return and $RM - Rf$ is the market risk premium. This shows that the extra return investors demand is proportional to how much the asset moves with the market: a beta of 1 means the asset tends to track the market; above 1 means more volatility and a higher risk premium; below 1 means less volatility and a smaller premium. Unsystematic risk is diversifiable and not priced in, so beta does not measure that. The idea that beta relates to dividend risk or that beta is irrelevant to expected return contradicts CAPM, which ties expected return directly to beta via the market risk premium.

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7. Which two methods are commonly used to estimate the cost of equity?

A. Internal Rate of Return and Payback Period

B. CAPM and Dividend Discount Model

C. Net Present Value and Terminal Value

D. Price-to-Earnings and Earnings Growth

Estimating the cost of equity is about determining the return investors require on a company's equity. The two common approaches are the Capital Asset Pricing Model (CAPM) and the Dividend Discount Model (DDM). CAPM ties the cost of equity to market risk. It says the expected return on equity equals the risk-free rate plus a risk premium that reflects how much the stock's returns move with the overall market. The formula is Ke = Rf + β(Rm − Rf). Here, Rf is the risk-free rate, β measures the stock's sensitivity to market moves, and (Rm − Rf) is the market risk premium. This method is widely used because it links the equity return to observable market data and a measure of systematic risk. Dividend Discount Model estimates the cost of equity from expected dividends. In its Gordon growth form, Ke = D1/P0 + g, where D1 is the next dividend, P0 is the current price, and g is the growth rate of dividends. This approach is intuitive for firms with stable, predictable dividends and directly ties the required return to the income stream investors expect. Other options you might see are more about evaluating projects or valuing entire cash flows rather than directly stating the return investors require on equity, so they aren't the typical methods for estimating the cost of equity.

8. Which of the following is an example of capital budgeting?

A. Deciding whether to build a new production facility

B. Deciding on daily cash collections

C. Issuing new shares

D. Negotiating loan terms

Capital budgeting evaluates long-term investments in assets that will generate cash flows over many years. Building a new production facility fits this idea because it requires a substantial upfront capital outlay and is expected to produce incremental cash inflows over the life of the facility. It's a decision about whether to commit funds now for long-run gains, which is exactly what capital budgeting assesses. Daily cash collections relate to managing liquidity and working capital, not long-term investment appraisal. Issuing new shares and negotiating loan terms are financing decisions, focused on how to raise or obtain funds and how to structure capital, rather than evaluating the profitability of a long-term investment.

9. Net working capital is defined as

A. Fixed assets minus current assets

B. Current liabilities minus current assets

C. Total assets minus total liabilities

D. Current assets minus current liabilities

Net working capital is a measure of a company's short-term liquidity—the cushion available to fund day-to-day operations. It is calculated by taking current assets (such as cash, accounts receivable, and inventory) and subtracting current liabilities (such as accounts payable, short-term debt, and other obligations due within a year). A positive result means the firm has more short-term assets than short-term obligations, signaling it can cover its near-term debts and operate smoothly. A negative result suggests potential liquidity strain. This definition focuses only on the immediately usable resources and obligations, which is why it's distinct from total assets minus total liabilities (that equals equity, not liquidity) and from subtracting current assets from current liabilities (that would invert the sign and misstate the measure). It also avoids including long-term assets like fixed assets, which aren't readily available to meet short-term needs. For illustration, if current assets total 1,200 and current liabilities total 900, net working capital is 300, indicating a healthy short-term liquidity position.

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10. If the discount rate r increases, what happens to the present value of an ordinary annuity?

A. Increase

B. Decrease

C. Remains unchanged

D. Becomes negative

The time value of money means that money today is worth more than the same amount in the future. For an ordinary annuity, where payments occur at the end of each period, the present value sums the discounted value of each payment. If the discount rate rises, each future payment is discounted more heavily, so the total present value falls. This is also shown by the formula PV = PMT × [1 − (1 + r)^−n] / r: as r increases, the fraction becomes smaller, pulling the present value down. Intuitively, a higher rate represents a higher opportunity cost of waiting, so future payments are worth less in today's dollars. Under typical positive payments, the present value decreases, not increases, stays unchanged, or becomes negative.

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Next Steps

Congratulations on reaching the final section of this guide. You've taken a meaningful step toward passing your certification exam and advancing your career.

As you continue preparing, remember that consistent practice, review, and self-reflection are key to success. Make time to revisit difficult topics, simulate exam conditions, and track your progress along the way.

If you need help, have suggestions, or want to share feedback, we'd love to hear from you. Reach out to our team at hello@examzify.com.

Or visit your dedicated course page for more study tools and resources:

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We wish you the very best on your exam journey. You've got this!

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