FIN 516 Week 8 Final Exam

Question 1.**1.** (TCO B) Which of the following statements concerning the MM extension with growth is not correct?
(a) The tax shields should be discounted at the unlevered cost of equity.
(b) The value of a growing tax shield is greater than the value of a constant tax shield.
(c) For a given D/S, the levered cost of equity is greater than the levered cost of equity under MM's original (with tax) assumptions.
(d) For a given D/S, the WACC is greater than the WACC under MM's original (with tax) assumptions.
(e) The total value of the firm is independent of the amount of debt it uses. (Points : 20)

Question 2.**2.** (TCO D) Which of the following statements is most correct?
(a) In a private placement, securities are sold to private (individual) investors rather than to institutions.
(b) Private placements occur most frequently with stocks, but bonds can also be sold in a private placement.
(c) Private placements are convenient for issuers, but the convenience is offset by higher flotation costs.
(d) The SEC requires that all private placements be handled by a registered investment banker.
(e) Private placements can generally bring in funds faster than is the case with public offerings. (Points : 20)

Question 3.**3.** (TCO E) Buster's Beverages is negotiating a lease on a new piece of equipment that would cost $100,000 if purchased. The equipment falls into the MACRS 3-year class, and it would be used for 3 years and then sold, because the firm plans to move to a new facility at that time. The estimated value of the equipment after 3 years is $30,000. If the borrow and purchase option is used, the cash flows would be the following: (Year 1) -2,400; (Year 2) -3,800; (Year 3) -1,400; (Year 4) -79,600; all of these cash outflows would be at the beginning of the respective years. Alternatively, the firm could lease the equipment for 3 years, with annual lease payments of $29,000 per year, payable at the beginning of each year. The firm is in the 20% tax bracket. If it borrows and purchases, it could obtain a 3-year simple interest loan, to purchase the equipment at a before-tax interest rate of 10%. If there is a positive net advantage to leasing, the firm will lease the equipment. Otherwise, it will buy it. What is the NAL?
(a) $5,736
(b) $6,023
(c) $6,324
(d) $6,640
(e) $6,972 (Points : 20)