Quiz – Chapter 14

1. Hawkeye Cleaners has been considering the purchase of an industrial dry-cleaning machine. The existing machine is operable for three more years and will have a zero disposal price. If the machine is disposed of now, it may be sold for $60,000. The new machine will cost $200,000 and an additional cash investment in working capital of $60,000 will be required. The new machine will reduce the average amount of time required to wash clothing and will decrease labor costs. The investment is expected to net $50,000 in additional cash inflows during the year of acquisition and $150,000 each additional year of use. The new machine has a three-year life. These cash flows will generally occur throughout the year and are recognized at the end of each year. Income taxes are not considered in this problem. The working capital investment will not be recovered at the end of the asset's life.

   What is the net present value of the investment, assuming the required rate of return is 24%? Would the company want to purchase the new machine?
   a. $(32,800); yes
   b. $(16,400); no
   c. $16,400; yes
   d. $32,800; no

2. If the net present value for a project is zero or positive, this means
   a. the project should be accepted.
   b. the project should not be accepted.
   c. the expected rate of return is below the required rate of return.
   d. both (a) and (c).

3. The method that measures the time it will take to recoup, in the form of future cash inflows, the total dollars invested in a project is called
   a. the simple rate-of-return method.
   b. payback method.
   c. internal rate-of-return method.
   d. the book-value method.

4. The approach to capital budgeting which divides an accounting measure of income by an accounting measure of investment is
   a. net present value.
   b. internal rate of return.
   c. payback method.
   d. simple rate of return.

5. The Alpha Beta Corporation disposes of a capital asset with an original cost of $85,000 and accumulated depreciation of $54,500 for $25,000. Alpha Beta's tax rate is 40%. Calculate the after-tax cash inflow from the disposal of the capital asset.
   a. $2,200
   b. ($2,200)
   c. $27,200
   d. $31,500

6. The Phenom Corporation has an annual cash inflow from operations from its investment in a capital asset of $50,000 for five years. The corporation's income tax rate is 40%. Calculate the five years total after-tax cash inflow from operations.
   a. $250,000
   b. $175,000
   c. $150,000
   d. $50,000

Answer Key – Quiz – Chapter 14

1. c
2. a
3. b
4. d
5. c
6. c