Financial Accounting for Undergraduates
3rd Edition by Wallace, Nelson, Christensen, and Ferris

Practice Quiz Solutions

Chapter 13. Analysis and Interpretation of Financial Statements

1. If you wanted to determine whether accounts receivable grew at the same rate as sales, what type of financial statement analysis would you perform?

a. Horizontal analysis of the balance sheet and vertical analysis of the income statement.
b. Vertical analysis of the balance sheet and horizontal analysis of the income statement.
c. Horizontal analysis of both the balance sheet and the income statement.
d. Vertical analysis of both the balance sheet and the income statement.

Answer: *c*

2. Selected balance sheet information is presented for four companies within the same industry (in millions):

	Company 1	Company 2	Company 3	Company 4
Current assets	$927	$2,601	$3,987	$2,201
Current liabilities	$854	$2,887	$3,334	$1,453
Total liabilities	$3,891	$7,011	$6,533	$3,942
Total liabilities and stockholders' equity	$4,843	$13,460	$13,045	$6,566

Based on your calculations of the debt-to-equity ratio for all companies, which company is more solvent?

a. Company 1
b. Company 2
c. Company 3
d. Company 4

Answer: *c*

Rationale:

Company	Debt-to-equity ratio	
Company 1	$3,891 / ($4,843 – $ 3,891)	= 4.09
Company 2	$7,011 / ($13,460 - $7,011)	= 1.09
Company 3	$6,533 / ($13,045 – 6,533)	= 1.00
Company 4	$3,942 / ($6,566 – $3,942)	= 1.50

3. The return on assets ratio can be broken down into two individual ratios, which are:

a. Return on sales and asset turnover
b. Return on sales and return on equity
c. Return on sales and current ratio
d. Asset turnover and return on equity

Answer: *a*

Questions 4 through 10 **were based on the following financial data for Smith & Sons:**

Smith & Sons
Balance Sheet
As of December 31

Cash	$ 80,000	Current liabilities	$ 160,000
Accounts receivable	160,000	Bonds payable	240,000
Inventory	260,000	Common stock	400,000
Plant assets (net)	500,000	Retained earnings	200,000
Total assets	$1,000,000	Total liabilities and stockholders' equity	$1,000,000

Sales revenue for the year was $1,600,000, gross profit was $640,000, and net income was $72,000.

One year ago, accounts receivable were $152,000, inventory was $220,000, total assets were $920,000, and stockholders' equity was $520,000.

4. What the company's inventory turnover for the year?

a. 4.0
b. 0.4
c. 3.0
d. 0.3

Answer: *a*
Rationale: ($1,600,000 - $640,000) / [($260,000 + $220,000) / 2]

5. What was the company's return on common stockholders' equity?

a. 6.0 percent
b. 8.9 percent
c. 11.2 percent
d. 12.9 percent

Answer: *d*
Rationale: $72,000 / [($600,000 + $520,000)/2]

6. What was the company's accounts receivable turnover for the year?

a. 12.0
b. 10.3
c. 8.6
d. 6.6

Answer: *b*
Rationale: $1,600,000 / [($160,000 + $152,000)/2]

7. What was the firm's return on sales for the year?

a. 9.0 percent
b. 6.0 percent
c. 5.0 percent
d. 4.5 percent

Answer: *d*
Rationale: ($72,000 / $1,600,000)

8. What was the firm's return on assets for the year?

a. 9.5 percent
b. 8.5 percent
c. 7.5 percent
d. 5.0 percent

Answer: *c*
Rationale: $72,000 / [($1,000,000 + $920,000) / 2]

9. If the company's interest expense was $24,000 and its income tax expense $20,000, what was the company's times-interest-earned ratio for the year?

a. 5.0
b. 4.8
c. 4.6
d. 4.4

Answer: *b*
Rationale: ($72,000 + $20,000 + $24,000) / $24,000

10. What was the company's current ratio?

a. 3.1
b. 4.0
c. 4.2
d. 5.0

Answer: *a*
Rationale: ($80,000 + $160,000 + $260,000) / $160,000