

FINANCIAL STATEMENT MODELING PRACTICE TEST (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.

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!

Questions

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- 1. A company has a beginning of period cash balance of \$60 million, a minimum cash balance of \$20 million, and its free cash flow for the current period was negative \$80 million. How much does the company need to draw from its revolver?**
 - A. \$30 million
 - B. \$40 million
 - C. \$60 million
 - D. \$20 million

- 2. From the list below, pick the assumption least susceptible to management discretion that could artificially increase profitability?**
 - A. Accounts Payable Supplier Payment Dates
 - B. Inventory Turnover
 - C. Depreciation Methods
 - D. Revenue Recognition Timing

- 3. Which action would, all else equal, likely increase the revolver balance?**
 - A. Increase in minimum cash balance
 - B. Increase in accounts payable
 - C. Higher cash flow from operations
 - D. Increase in inventories

- 4. Which approach best facilitates comparison of scenario results?**
 - A. Present results in a single numeric table without labels.
 - B. Build a chart for each scenario separately without a summary.
 - C. List scenario results in a paragraph in the report.
 - D. Use a summary dashboard comparing key metrics across scenarios.

- 5. When choosing a discount rate for a DCF model, what matters most?**
 - A. Always use the highest possible rate to ensure conservative valuation.
 - B. Use the cost of debt only.
 - C. Use the average inflation rate.
 - D. Choose a rate that reflects risk and capital structure (WACC); an inappropriate rate distorts valuation and decision-making.

6. Let's say a company has purchased a building for \$20m, which will be depreciated under the straight-line approach. If the annual depreciation is equal to 0.5m each year, what is the useful life assumption being used? Assume the salvage value at the end of the useful life is equal to zero, and round your answer to the nearest whole number. Useful Life Assumption = _____ Years
- A. 10
 - B. 20
 - C. 40
 - D. 60
7. Depreciation expense found in the SG&A line of the income statement for a manufacturing firm would most likely be attributable to the wear and tear of which asset?
- A. Computers used by the Accounting Department
 - B. Factory Machinery
 - C. Office Furniture
 - D. Vehicles Used by Sales Force
8. Which statement best defines EBIT margin?
- A. Net income divided by revenue
 - B. EBIT divided by revenue
 - C. Gross profit divided by revenue
 - D. Operating cash flow divided by revenue
9. Suppose a company has acquired a competitor at a \$50m purchase price with a fair market value (FMV) of \$48m. Based on this hypothetical scenario, how much in goodwill is recognized on the acquirer's balance sheet?
- A. 0
 - B. 2
 - C. 4
 - D. 8

10. If a company just initiated a new dividend plan to common shareholders, which of the following would NOT be an example of one of the impacts on the financial statements?

- A. The dividend payout reduces cash in financing activities
- B. Retained earnings are decreased by the dividend
- C. Dividend payable increases liabilities when declared
- D. The dividend payout would appear as an outflow in the non-operating expenses section of the income statement

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Answers

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

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Explanations

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1. A company has a beginning of period cash balance of \$60 million, a minimum cash balance of \$20 million, and its free cash flow for the current period was negative \$80 million. How much does the company need to draw from its revolver?

- A. \$30 million
- B. \$40 million**
- C. \$60 million
- D. \$20 million

The main idea is to figure out how much liquidity is needed to keep the cash balance at or above the minimum, after accounting for the period's cash flow. Start with the opening cash of 60. A negative free cash flow of 80 reduces cash by 80, so cash at the end of the period before any revolver draw would be $60 - 80 = -20$. To meet a minimum cash balance of 20, the company must cover the shortfall of 40. Drawing 40 from the revolver brings ending cash to 20, satisfying the minimum. Drawing more than 40 would leave excess cash beyond the minimum, which isn't necessary, so 40 is the appropriate amount.

2. From the list below, pick the assumption least susceptible to management discretion that could artificially increase profitability?

- A. Accounts Payable Supplier Payment Dates**
- B. Inventory Turnover
- C. Depreciation Methods
- D. Revenue Recognition Timing

The main idea is understanding which accounting choices can actually change reported earnings versus those that mostly affect cash flow. Some policies let management shift when or how much is recognized as revenue or expense, or how assets are valued, thereby altering profitability. The supplier payment dates option, however, mainly affects cash flow timing and the balance sheet, not the amount of expenses recognized in the income statement. Under accrual accounting, expenses are recognized when incurred, not when paid, so extending payment terms does not inflate profits in the period. It may impact cash flow or discount terms, but it doesn't artificially boost earnings. In contrast, revenue recognition timing, depreciation methods, and inventory valuation can directly move reported profitability through timing or measurement changes.

3. Which action would, all else equal, likely increase the revolver balance?

- A. Increase in minimum cash balance**
- B. Increase in accounts payable
- C. Higher cash flow from operations
- D. Increase in inventories

Revolver balance shows how much is drawn on a revolving credit facility to fund short-term liquidity needs. The action that most directly pushes this balance higher is increasing the minimum cash cushion. If you require more cash to be held on hand and other funding sources stay the same, you'd need to borrow more on the revolver to meet that higher cash minimum, raising the revolver balance. The other options either ease liquidity or shift funding in ways that don't force as direct an increase in revolver borrowings: delaying payments through higher accounts payable reduces cash outflows; higher cash flow from operations adds cash to the balance sheet and reduces the need to borrow; increasing inventories ties up cash, but its impact depends on how cash is funded, whereas raising the minimum cash balance directly creates a larger funding gap that the revolver is used to fill.

4. Which approach best facilitates comparison of scenario results?

- A. Present results in a single numeric table without labels.
- B. Build a chart for each scenario separately without a summary.
- C. List scenario results in a paragraph in the report.
- D. Use a summary dashboard comparing key metrics across scenarios.**

To compare scenario results effectively, present a summary dashboard that places the key metrics for every scenario side by side. This setup lets you see differences at a glance, aligns time frames and units, and makes it easy to judge which scenario performs best on each metric. Visual cues like color coding or bar comparisons highlight variances and risks, supporting faster, more confident decisions. Other approaches slow down and confuse comparison. A single numeric table without clear labels can obscure what each figure means. Building a separate chart for each scenario forces you to flip views and mentally line up results. Listing results in a paragraph hides the specific metrics and makes scanning for differences tedious. The dashboard approach keeps everything in one view, enabling quick, apples-to-apples assessment.

5. When choosing a discount rate for a DCF model, what matters most?

- A. Always use the highest possible rate to ensure conservative valuation.
- B. Use the cost of debt only.
- C. Use the average inflation rate.
- D. Choose a rate that reflects risk and capital structure (WACC); an inappropriate rate distorts valuation and decision-making.**

In a DCF, the discount rate should reflect the risk of the cash flows and how the project or firm is financed. That means using the blended cost of capital from all sources—the weighted average cost of capital (WACC)—because it captures the opportunity cost for both debt and equity investors and incorporates the tax shield from debt. If you set the rate too high or too low, you distort present value, leading to systematically faulty valuations and misguided decisions. Using just the cost of debt ignores equity risk and financing structure, while inflation or always choosing the highest rate ignores the actual risk level of the cash flows. The key is to pick a rate that matches the risk of the cash flows and the firm's financing mix, typically expressed as the WACC for unlevered cash flows (or the cost of equity for levered cash flows).

6. Let's say a company has purchased a building for \$20m, which will be depreciated under the straight-line approach. If the annual depreciation is equal to 0.5m each year, what is the useful life assumption being used? Assume the salvage value at the end of the useful life is equal to zero, and round your answer to the nearest whole number. Useful Life Assumption = _____ Years

- A. 10
- B. 20
- C. 40**
- D. 60

Under straight-line depreciation, annual depreciation equals (cost minus salvage value) divided by the useful life. With salvage value assumed zero, the annual depreciation is simply cost divided by the useful life. Here, 0.5 million per year equals 20 million divided by the useful life, so useful life = $20 / 0.5 = 40$ years. The other options would yield annual depreciation totals of 2 million, 1 million, or about 0.333 million respectively, which don't match the given 0.5 million. So the useful life assumption is 40 years.

7. Depreciation expense found in the SG&A line of the income statement for a manufacturing firm would most likely be attributable to the wear and tear of which asset?

A. Computers used by the Accounting Department

B. Factory Machinery

C. Office Furniture

D. Vehicles Used by Sales Force

Depreciation is allocated to the functions those assets support. In a manufacturing firm, depreciation on factory machinery is tied to production costs and would flow into cost of goods sold or manufacturing overhead, not SG&A. Depreciation for assets that support selling, general, and administrative activities belongs in SG&A. A computer used by the accounting department is a classic example of an SG&A asset because it directly supports administrative and financial tasks. While office furniture or a vehicle used by the sales force can also be SG&A items, the accounting computer is the most straightforward and consistently classified as SG&A depreciation.

8. Which statement best defines EBIT margin?

A. Net income divided by revenue

B. EBIT divided by revenue

C. Gross profit divided by revenue

D. Operating cash flow divided by revenue

EBIT margin shows how much operating profit a company makes from each dollar of revenue, before financing and tax effects. It is computed as EBIT divided by revenue, where EBIT is earnings before interest and taxes (often called operating income). This means you're looking at profit generated purely from operating activities, excluding interest expenses and income taxes. This helps you compare how efficiently different companies run their operations, regardless of how they're financed or taxed. The other common measures mix in items that EBIT excludes: net income margin includes interest and taxes, so it reflects financing structure and tax effects; gross profit margin only accounts for cost of goods sold and revenue, omitting operating expenses; operating cash flow margin uses cash flow rather than accounting profit, which can differ due to non-cash items.

9. Suppose a company has acquired a competitor at a \$50m purchase price with a fair market value (FMV) of \$48m. Based on this hypothetical scenario, how much in goodwill is recognized on the acquirer's balance sheet?

A. 0

B. 2

C. 4

D. 8

In a business combination, goodwill is the excess of the purchase price over the fair value of the identifiable net assets acquired. Net identifiable assets are the fair value of assets minus liabilities. Here, the acquirer pays \$50 million for the target, and the fair value of the target's net identifiable assets is \$48 million. The difference is \$2 million, which is recorded as goodwill on the acquirer's balance sheet. (If the purchase price were less than the fair value of net assets, you'd have a negative goodwill situation, handled as a bargain purchase under accounting rules.)

10. If a company just initiated a new dividend plan to common shareholders, which of the following would NOT be an example of one of the impacts on the financial statements?

- A. The dividend payout reduces cash in financing activities
- B. Retained earnings are decreased by the dividend
- C. Dividend payable increases liabilities when declared
- D. The dividend payout would appear as an outflow in the non-operating expenses section of the income statement**

Dividends are distributions of profits to shareholders, not business expenses, so they don't appear on the income statement as any kind of expense, including non-operating expenses. When a dividend is declared, it reduces retained earnings on the balance sheet and creates a dividend payable liability. When the dividend is paid, cash decreases and the liability is settled. On the cash flow statement, the actual dividend payment shows up as a financing activity outflow. Because dividends are not recorded as expenses, displaying the dividend payout as an outflow in the non-operating expenses section of the income statement would be incorrect. That's why this option does not reflect an impact on the financial statements.

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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:

<https://finstatementmodeling.examzify.com>

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

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