

# Peregrine Foundations of Business Finance Practice Test (Sample)

## Study Guide



**Everything you need from our exam experts!**

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# Table of Contents

<b>Copyright</b> .....	<b>1</b>
<b>Table of Contents</b> .....	<b>2</b>
<b>Introduction</b> .....	<b>3</b>
<b>How to Use This Guide</b> .....	<b>4</b>
<b>Questions</b> .....	<b>5</b>
<b>Answers</b> .....	<b>8</b>
<b>Explanations</b> .....	<b>10</b>
<b>Next Steps</b> .....	<b>16</b>

# 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

- 1. Which metric illustrates how effectively a firm uses all its assets to generate sales?**
  - A. Debt-to-equity ratio**
  - B. Total asset turnover ratio**
  - C. Coverage ratio**
  - D. Average payment period**
- 2. The required interest rate on any security is composed of what plus a risk premium?**
  - A. Expected future cash flow**
  - B. Market demand rate**
  - C. Risk-free rate of interest**
  - D. Premium market rate**
- 3. Which of the following is NOT a common method for evaluating capital budgeting projects?**
  - A. Net present value**
  - B. Market share analysis**
  - C. Internal rate of return**
  - D. Payback period**
- 4. What is the formula for calculating operating income?**
  - A. Revenue - Operating Expenses**
  - B. Gross Profit - Operating Expenses**
  - C. Net Income + Operating Expenses**
  - D. Gross Profit + Revenue**
- 5. What does liquidity refer to in financial terms?**
  - A. The ability to produce cash flow**
  - B. The ability to invest in fixed assets**
  - C. The ability to convert an asset into cash quickly**
  - D. The ability to manage a budget effectively**

- 6. What is the relationship between equity financing and ownership?**
- A. Equity financing involves limited ownership**
  - B. Equity financing affects shareholder dividends**
  - C. Equity financing grants ownership in the company**
  - D. Equity financing eliminates ownership risks**
- 7. What characterizes convertible securities?**
- A. They have fixed income and cannot be exchanged**
  - B. They can be converted into another asset**
  - C. They are typically high-risk investments**
  - D. They do not have a conversion price**
- 8. The efficiency with which a firm uses all its assets can be determined by analyzing what ratio?**
- A. Debt-to-equity ratio**
  - B. Average payment period**
  - C. Total asset turnover ratio**
  - D. Coverage ratio**
- 9. Which of the following best describes notes payable?**
- A. Long-term investments**
  - B. Outstanding short-term loans**
  - C. Accrued liabilities**
  - D. Deferred revenue**
- 10. Which type of account represents the additional paid-in capital over the par value of stock?**
- A. Retained earnings**
  - B. Paid-in-capital excess of par**
  - C. Common stock**
  - D. Accrued expenses**



## **Answers**

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

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## **Explanations**

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**1. Which metric illustrates how effectively a firm uses all its assets to generate sales?**

- A. Debt-to-equity ratio**
- B. Total asset turnover ratio**
- C. Coverage ratio**
- D. Average payment period**

The total asset turnover ratio is the correct metric to illustrate how effectively a firm uses all its assets to generate sales. This ratio is calculated by dividing the company's total sales or revenue by its total assets. It provides insight into how efficiently a company is utilizing its assets to generate sales; a higher ratio indicates that the company is effectively using its assets to create revenue, while a lower ratio suggests that the company may not be utilizing its resources as efficiently as it could be. This ratio is particularly valuable because it highlights the relationship between a firm's asset base and its sales performance. Companies with high asset turnover are typically able to generate more revenue per dollar of assets, which can indicate strong operational efficiency, effective management of resources, and high demand for their products or services. In contrast, the other options relate to different aspects of financial performance or different liabilities. The debt-to-equity ratio focuses on the capital structure and financial leverage of a firm, the coverage ratio assesses the ability to meet debt obligations, and the average payment period measures how quickly a firm pays its suppliers. While all are important financial metrics, they do not directly relate to how well a company utilizes its assets to generate sales, which is the primary focus of the total asset turnover ratio.

**2. The required interest rate on any security is composed of what plus a risk premium?**

- A. Expected future cash flow**
- B. Market demand rate**
- C. Risk-free rate of interest**
- D. Premium market rate**

The required interest rate on any security is fundamentally based on the risk-free rate of interest, which represents the return on an investment with no risk of financial loss. This serves as the baseline rate for all securities, taking into account that investors will generally expect to earn at least this minimum return to compensate for the time value of money. The risk premium is then added to the risk-free rate to account for the additional risk associated with the specific security. Different securities carry varying degrees of risk, influenced by factors such as credit risk, market volatility, and potential liquidity issues. The risk premium effectively compensates investors for taking on this extra risk above what they would receive from a risk-free investment. In summary, the composition of the required interest rate includes the risk-free rate as a foundational element, with a subsequent risk premium adding to it in accordance with the particular risks associated with the investment.

**3. Which of the following is NOT a common method for evaluating capital budgeting projects?**

- A. Net present value
- B. Market share analysis**
- C. Internal rate of return
- D. Payback period

The method that is NOT commonly used for evaluating capital budgeting projects is market share analysis. Capital budgeting primarily focuses on assessing the potential profitability and financial viability of investment projects. Techniques such as net present value, internal rate of return, and payback period are specifically designed to analyze cash flows, account for the time value of money, and assess the risks and returns of investments. Net present value calculates the difference between the present value of cash inflows generated by a project and the present value of cash outflows, providing a clear measure of the expected financial return. The internal rate of return determines the discount rate at which the net present value of a project becomes zero, indicating the project's potential profitability. The payback period focuses on the time it takes to recoup the initial investment, assessing liquidity and risk. Market share analysis, on the other hand, is more focused on assessing a company's competitiveness in its industry and does not directly evaluate the financial return of capital projects. Therefore, it is not a standard method used in capital budgeting evaluations.

**4. What is the formula for calculating operating income?**

- A. Revenue - Operating Expenses
- B. Gross Profit - Operating Expenses**
- C. Net Income + Operating Expenses
- D. Gross Profit + Revenue

The formula for calculating operating income is based on the relationship between revenue, operating expenses, and gross profit. Operating income represents the profit earned from the core business operations, excluding any income derived from non-operational activities or expenses like taxes and interests. The correct approach to find operating income is to start with gross profit, which is derived from total revenue minus the cost of goods sold (COGS). From gross profit, you subtract operating expenses, which include wages, rent, and other costs related to running the business (excluding COGS). The resulting figure is operating income, which reflects the profitability of the company's primary activities. Therefore, the formula correctly represented is gross profit minus operating expenses, indicating that operating income captures the performance of ongoing core operations effectively. This measure is crucial for understanding how well a company is performing in its main business activities.

**5. What does liquidity refer to in financial terms?**

- A. The ability to produce cash flow**
- B. The ability to invest in fixed assets**
- C. The ability to convert an asset into cash quickly**
- D. The ability to manage a budget effectively**

Liquidity, in financial terms, refers to the ability to convert an asset into cash quickly without significantly affecting its price. This is crucial for individuals or businesses when they need to access cash to meet immediate obligations, such as paying bills or making investments. Highly liquid assets, like cash itself or marketable securities, can be quickly sold or utilized, providing instant resources. In contrast, other options do not capture the essence of liquidity. While producing cash flow relates to the generation of funds, it does not specifically address the ease of accessing cash from assets. Investing in fixed assets, such as property or equipment, typically involves long-term commitments and does not emphasize the quick cash conversion required in liquidity concepts. Managing a budget effectively pertains more to financial planning and control than to the immediate availability of cash from assets.

**6. What is the relationship between equity financing and ownership?**

- A. Equity financing involves limited ownership**
- B. Equity financing affects shareholder dividends**
- C. Equity financing grants ownership in the company**
- D. Equity financing eliminates ownership risks**

Equity financing grants ownership in the company because when a business raises funds through the sale of equity, it offers shares of its ownership to investors. These investors become shareholders and, as a result, have a claim on a portion of the company's assets and earnings, proportionate to their ownership stake. Issuing shares allows a company to raise capital without incurring debt, but it also means that the original owners will now share control and profits with the new shareholders. Equity financing is a fundamental mechanism for enabling individuals and institutions to invest in a company, thereby aligning their interests with the company's success. Shareholders typically participate in decisions through voting rights and may receive dividends based on company performance. Ownership is a key aspect of equity financing, as it differentiates it from other forms of funding like debt financing, where lenders do not receive any ownership rights in exchange for their loan. By understanding this relationship, one can appreciate how equity financing influences the dynamics of business ownership and governance.

## 7. What characterizes convertible securities?

- A. They have fixed income and cannot be exchanged
- B. They can be converted into another asset**
- C. They are typically high-risk investments
- D. They do not have a conversion price

Convertible securities are characterized by their ability to be converted into another form of asset, typically common stock, at a predetermined conversion ratio. This feature makes them an attractive option for investors, as they provide the benefits of fixed income investment—such as interest payments—while also offering the opportunity to participate in the potential appreciation of the underlying equity. When an investor converts a convertible security into common stock, they can benefit from any increase in the stock's value, which can enhance overall returns. This capacity for conversion allows investors to have the upside potential of equity while still receiving the downside protection typically associated with fixed-income securities. For this reason, the distinguishing feature of convertible securities is their convertibility into other assets, such as shares of the issuing company.

## 8. The efficiency with which a firm uses all its assets can be determined by analyzing what ratio?

- A. Debt-to-equity ratio
- B. Average payment period
- C. Total asset turnover ratio**
- D. Coverage ratio

The total asset turnover ratio is a key indicator of the efficiency with which a firm utilizes its assets to generate sales. This ratio measures how effectively the firm converts its total assets into revenue, reflecting the firm's operational efficiency. A higher total asset turnover ratio suggests that the company is using its assets more efficiently to produce sales, which can lead to stronger financial performance. The calculation of this ratio involves dividing the company's total sales or revenue by its average total assets. This gives insight into how well the firm is leveraging its asset base to drive sales growth. Firms with a high total asset turnover ratio are typically able to generate more revenue per dollar invested in assets, signaling good management and effective asset utilization. In contrast, ratios such as the debt-to-equity ratio primarily assess financial leverage and capital structure, the average payment period focuses on a firm's short-term liquidity and payment practices, and the coverage ratio evaluates a company's ability to meet its debt obligations, none of which directly address asset utilization effectiveness. Thus, the total asset turnover ratio is specifically designed to gauge the efficiency of asset usage, making it the correct choice for this question.

**9. Which of the following best describes notes payable?**

- A. Long-term investments
- B. Outstanding short-term loans**
- C. Accrued liabilities
- D. Deferred revenue

Notes payable refers to written promissory notes where one party agrees to pay a specified amount of money to another party at a future date. These are typically categorized as short-term liabilities, meaning they are payments that are due within a year. In this context, they represent outstanding short-term loans that a business has taken on, and the company is obligated to repay them on or before their maturity date. This categorization aligns perfectly with how notes payable function in a business's financial statements and its cash flow management. The other options provided do not accurately capture the essence of notes payable. Long-term investments pertain to assets the company intends to hold for more than a year, which does not include notes payable. Accrued liabilities are expenses that have been incurred but not yet paid, which are distinct from notes payable that are formalized loans. Deferred revenue pertains to money received before services are performed or goods are delivered, representing a liability at that point but also different from the nature of notes payable.

**10. Which type of account represents the additional paid-in capital over the par value of stock?**

- A. Retained earnings
- B. Paid-in-capital excess of par**
- C. Common stock
- D. Accrued expenses

The correct choice represents the amount of capital that shareholders have invested in the company beyond the nominal or par value of the stock. When shares are issued at a price higher than their par value, the difference between the issuing price and the par value is recorded in a separate account known as "paid-in-capital excess of par." This account captures the additional funds that the company has received from shareholders, which represents their confidence in the company's future potential. For example, if a company issues shares with a par value of \$1 for \$10 each, the additional \$9 per share would be recorded in the paid-in-capital excess of par account. This is important for reflecting the true investment made by the shareholders and plays a role in the equity section of the balance sheet. Other options, such as retained earnings, common stock, or accrued expenses, do not specifically address the capital contributed over the par value of stock. Retained earnings relate to the profits retained in the business rather than distributed as dividends, common stock refers only to the par value itself, and accrued expenses pertain to liabilities rather than equity. Thus, the choice regarding paid-in-capital excess of par accurately captures the additional investments over the stock's par value.



## 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](mailto:hello@examzify.com).**

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

**<https://peregrinefoundationsbusfinance.examzify.com>**

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