Comprehensive Learning Assessment

**Paper details:**

Taxes are costs, and, therefore, changes in tax rates can affect consumer prices, project lives and the value of existing firms. Evaluate the change in taxation on the valuation of the following project: (see materials) Assumptions: Tax depreciation is straight-line over three years. Pre-tax salvage value is 25 in year 3 and 50 if the asset is scrapped in year 2. Tax on salvage value is 40% of the difference between salvage value and book value of the investment. The cost of capital is 20%. Please verify that the information given above yields NPV = 0. If you decide to terminate the project in year two (2) what would be the NPV of the project? Suppose that the government now changes tax depreciation to allow a 100% write-off in year one (1). How does this affect your answers to parts a and b above? Would it now make sense to terminate the project after two rather than three years? How would your answers change if the corporate income tax were abolished entirely? Please explain your answer in detail and provide in-text citations.