

6.5: End-of-Chapter Exercises

Questions

1. Define “common stock.”
2. List three rights normally held by common stockholders.
3. Define “authorized” number of shares of common stock.
4. Define “issued” number of shares of common stock.
5. Define “outstanding” shares of common stock.
6. Explain the meaning of “par value” of a share of stock.
7. Why is preferred stock called “preferred”?
8. What is treasury stock?
9. Give three reasons a corporation might want to buy back its own stock.
10. What is a dividend?
11. What is a cumulative dividend?
12. What is a stock dividend?
13. What is the difference in accounting between a small stock dividend and a large stock dividend?
14. Why do corporations issue stock dividends?
15. How is return on equity calculated?
16. How is a company’s price-earnings ratio calculated?
17. How is basic earnings per share determined?
18. Why would a company be required to report diluted earnings per share?

True or False

1. ____ Common stockholders are usually permitted to vote for a corporation’s board of directors, but preferred stockholders are not.
2. ____ Earnings per share is one of the most watched metrics of a corporation.
3. ____ Preferred dividends must be paid annually.
4. ____ A corporation with stock options had to report diluted earnings per share.
5. ____ A small stock dividend will typically result in a smaller debit to retained earnings than a large stock dividend.
6. ____ It is not possible for a corporation to have more outstanding shares of stock than authorized shares of stock.
7. ____ Most companies choose a relatively large par value for their stock.
8. ____ Preferred stockholder dividends are paid before common stockholder dividends.
9. ____ One reason a company might repurchase its own stock is to protect against a hostile takeover.
10. ____ Anyone not a stockholder on the date of declaration of a dividend will not be eligible to participate in that dividend.
11. ____ When referring to dividends, the term “in arrears” refers to the fact that the date of declaration and the date of payment are not the same.
12. ____ A company’s price-earnings ratio can help predict changes in its stock price based on movement in its EPS.

Multiple Choice

1. Yancey Corporation issues 50,000 shares of common stock for \$30 per share. The stock has a par value of \$2 per share. By what amount would Yancey credit capital in excess of par?
 1. \$1,500,000
 2. \$1,400,000
 3. \$100,000
 4. \$50,000
2. Landon Corporation sold 16,000 shares of \$0.50 par value common stock for \$17 per share. Which of the following is the journal entry Landon should make?
 1. Debit Cash \$272,000 Credit Common Stock \$8,000 and Credit Capital in Excess of Par Value \$264,000.

2. Debit Cash \$272,000 Credit Common Stock \$272,000.
 3. Debit Capital in Excess of Par Value \$264,000 Credit Common Stock \$264,000
 4. Debit Cash \$8,000 and Credit Common Stock \$8,000
3. Jackson Company is authorized to issue 20,000 shares of \$0.50 par value stock. On February 1, it issues 4,000 shares. On April 20, an additional 6,000 shares are issued. On September 23, Jackson repurchases 2,000 shares. On November 3, it reissues half of the shares it repurchased in September. How many outstanding shares does Jackson have on December 31?
1. 20,000
 2. 10,000
 3. 9,000
 4. 8,000
4. Paul Mitchell purchased a licensing agreement for \$40,000 prior to going to work for Traylor Corporation. Traylor agreed to issue 2,000 shares of common stock to Mitchell in exchange for his licensing agreement, which now has a value of \$30,000. At the time of the stock exchange, Traylor's \$2 par value stock was selling for \$14 per share. For what amount should Traylor debit the licensing agreement?
1. \$40,000
 2. \$30,000
 3. \$28,000
 4. \$4,000
5. Kramer Company is authorized to issue 45,000 shares of its 7 percent, \$100 par value preferred stock. On March 15, Kramer issues 5,000 shares for \$200 per share. On November 1, Kramer declares the dividend and pays it on December 1. What amount of cash was paid to the preferred shareholders?
1. \$70,000
 2. \$315,000
 3. \$630,000
 4. \$35,000
6. Portor Corporation is authorized to sell 150,000 shares of its \$0.25 par value common stock. It currently has 90,000 shares issued and outstanding. Portor would like to declare a stock dividend and is curious about the effect this will have on retained earnings. Portor's stock has a current market value per share of \$26. Portor is trying to decide between a 5 percent stock dividend and a 40 percent stock dividend. Which of the following accurately shows the effect of each on retained earnings?

	5% Stock Dividend	40% Stock Dividend
a.	\$117,000	\$936,000
b.	\$117,000	\$9,000
c.	\$1,125	\$9,000
d.	\$1,125	\$936,000

7. Falls Church Corporation ended the year with revenues of \$45,000 and expenses of \$33,000. Its stockholders' equity accounts total \$490,000. Which of the following is Falls Church's return on equity for the year?
1. 9.18%
 2. 6.73%
 3. 73.33%
 4. 2.45%

8. Fleming Corporation began and ended the year with 50,000 outstanding shares of common stock net income for the year totaled \$480,000. Preferred dividends amounted to \$30,000. Which of the following would be Fleming's basic earnings per share?
1. \$9.60 per share
 2. \$16.00 per share
 3. \$6.00 per share
 4. \$9.00 per share
9. Which of the following would not force a company to compute diluted earnings per share in addition to basic earnings per share?
1. Convertible preferred stock
 2. Stock warrants
 3. Nonconvertible preferred stock
 4. Stock options
10. Friar Inc. had a net income for 20X5 of \$1,870,000. It had 600,000 shares of common stock outstanding on 1/1/X5 and repurchased 150,000 of those shares on 8/31/X5. It has no preferred stock. On 12/31/X5, Friar's stock was selling for \$26 per share. Which of the following is Friar's price-earnings ratio on 12/31/X5?
1. 7.65
 2. 8.33
 3. 6.25
 4. 7.00

Problems

1. Cutlass Corporation is authorized to issue 40,000 shares of \$.25 par value common stock. On March 15, it issues 1,000 shares for \$7 per share. Record this transaction for Cutlass.
2. McNair Corporation is authorized to issue 105,000 shares of 5 percent, \$100 par value preferred stock. On May 22, McNair issues 32,000 shares of preferred stock for \$125 per share. McNair declares the preferred dividend on September 1 and pays it on October 1.
 1. Record the issuance of the preferred stock.
 2. Record the declaration of the dividend on September 1.
 3. Record the payment of the preferred dividend on October 1.
3. Douglas Company's board of directors approves a plan to buy back shares of its common stock. Prepare journal entries for each of the following transactions. Assume that the transactions occur in the order given. At the beginning of 2023, Douglas has 80,000 shares issued and outstanding. All the transactions happen during 2023.
 1. Douglas buys back 3,500 shares of its \$1 common stock for \$32 per share.
 2. Douglas resells 1,500 shares for \$36.
 3. Douglas resells 500 shares for \$32.
 4. Douglas resells 600 shares for \$29.
 5. How many shares does Douglas have issued and outstanding at the end of 2023?
4. Grayson Corporation is authorized to sell 2,000,000 shares of its \$1 par value common stock to the public. Before 2024, it had issued 60,000 shares with a market value of \$15 per share. During 2024, Grishom issued another 14,000 shares when the market value per share was \$20.

On 1/1/24, Grishom had retained earnings of \$1,950,000. During 2024, Grishom earned net income of \$80,000 and paid dividends to common stockholders of \$19,000. Also during 2024, Grishom repurchased 11,000 shares of its own stock when the market price was \$18.

 1. Record the issuance of the common stock during 2024.
 2. Determine retained earnings on 12/31/24.
 3. Record the purchase of the treasury stock.
 4. Prepare the stockholders' equity section of the balance sheet on 12/31/24.

5. In late 2022, the Pickins Corporation was formed. The articles of incorporation authorize 5,000,000 shares of common stock carrying a \$1 par value, and 1,000,000 shares of \$100 par value preferred stock. On January 1, 2023, 2,000,000 shares of common stock are issued for \$20 per share. Also on January 1, 50,000 shares of preferred stock are issued at \$100 per share.

1. Prepare journal entries to record these transactions on January 1.

During March 2023, the Pickins Corporation repurchased 100,000 common shares for the treasury at a price of \$18 per share. During August 2023, all 100,000 treasury shares are reissued at \$19 per share.

2. Prepare journal entries to record these transactions.

During November 2023, Pickins issues a 25 percent stock dividend on all outstanding shares when its stock was selling for \$30 per share. On December 1, 2023, Pickins declares a \$0.75 per share cash dividend on common stock and a \$2.00 per share cash dividend on preferred stock. Payment is scheduled for December 20, 2023, to shareholders of record on December 10, 2023.

3. Prepare journal entries to record the declaration and payment of these stock and cash dividends.

6. On March 1, St. George Company declares a stock dividend on its \$1 par value stock. It had 1,000 shares outstanding and the market value was \$13 per share.

1. What would be the debit to retained earnings for a 10 percent stock dividend?

2. What would be the debit to retained earnings for a 30 percent stock dividend?

7. Rawlings Company has the following equity accounts at the beginning and end of 2023:

	1/1/2023	12/31/2023
Common Stock, \$1 Par Value	\$160,000	\$200,000
Capital in Excess of Par, Common	\$12,000,000	\$16,000,000
Retained Earnings	\$1,100,000	\$1,800,000

The additional 40,000 shares of common stock were issued on September 1, 2023. Net income for the year was \$1,200,000.

Determine Rawlings' basic EPS on December 31, 2023.