Corporations: Paid-in Capital and the Balance Sheet

Learning Objective 1 Identify the distinguishing characteristics of a corporation

Advantages and Disadvantages of a Corporation

ADVANTAGES	DISADVANTAGES
• Ability to raise money • Continuous life • Easy to transfer ownership • No mutual agency • Limited liability	• Separation of ownership and management • Double taxation • Expensive government regulation

Capital Stock

- State authorizes how many shares of stock a corporation may issue through corporate bylaws
- Corporation issues stock certificates when stockholders buy stock
    - Basic unit of stock is a share
- Stock held by stockholders is outstanding

Learning Objective 2:

- Describe the two sources of stockholders' equity and the classes of stock

Stockholders' Equity

Paid-in capital	Retained earnings
• Amounts received from stockholders • Common stock is main source • Externally generated • Resulting from transactions with outsiders	• Earned Internally generated • y profitable operations • Results from internal corporate decisions and earnings

Classes of Stock

Common stock	**Preferred stock**
Basic form of capital stock	Owners have certain advantages over common • Receive dividends before common • Upon liquidation, receive assets before common • Right to vote sometimes withheld

Learning Objective 3: Journalize the issuance of stock and prepare the stockholders' equity section of a corporation balance sheet

Issue stock at par

Date		Debit	Credit
	Cash		
	Common stock		

Issue stock at a premium

Date		Debit	Credit
	Cash		
	Common stock		
	Paid-in capital in excess of par		

Accounting for Stock Issuances

- Issuing stock for noncash assets
  - Asset is debited for its fair value
- Issuing preferred stock
  - Similar to issuing common stock, except "Preferred stock" is credited at par value
  - Preferred stock usually is not issued above par

Stockholders' Equity on the Balance Sheet

- Equity accounts are listed in the following order on the balance sheet
  - Preferred stock
  - Paid-in capital in excess of par – preferred
  - Common stock
  - Paid-in capital in excess of par – common
  - Retained earnings

Any Company Balance Sheet December 30, 2010		
Stockholders' Equity		
Preferred stock, 6%, $50 par, 2000 shares authorized and issued	$	100,000
Paid-in capital in excess of par - preferred		5,000
Common stock, $1 par, 1,000,000 shares authorized, 500,000 issued		500,000
Paid-in capital in excess of par - common		750,000
Total paid-in captial		1,355,000
Retained earnings		715,000
Total stockholders' equity	$	2,070,000

Learning Objective 4 Illustrate Retained earnings transactions

Retained Earnings

Date		Debit	Credit
	Income summary		
	Retained earnings		

Deficit Balance

- If a company incurs a loss, Retained earnings is decreased
- A debit balance in Retained earnings is called a deficit

Learning Objective 5: Account for cash dividends

- Preferred dividends expressed as either:
  - A percent of par value

    2000 shares of $1000 par 8% = > Preferred dividends= $16000
  - Or a flat dollar amount per share

    2000 shares of no-par $3 = > Preferred dividends= $6000
  - Common dividends expressed as a dollar amount per share

Accounting for Dividends

Date		Debit	Credit
	Retained earnings		
	Dividends payable		
	Declaration of cash dividend		

	Dividends payable		
	Cash		
	Payment of cash dividend		

Dividing Dividends Between Preferred and Common

- Preferred stockholders receive dividends before common
- Common stockholders will only receive dividends if total declared is large enough

Cumulative and Noncumulative Preferred Stock

- Cumulative preferred stock
  - Accumulates dividends each year until the dividends are paid
  - Dividends in arrears - dividends passed or not paid
- Noncumulative preferred stock
  - Dividends not paid do not accumulated from one year to the next

Q1) The following information is from the balance sheet of Tudor Corporation as of December 31, 2010.

Preferred stock, $100 par	$ 500,000
Paid-in capital in excess of par-preferred	35,000
Common stock, $1 par	190,000
Paid-in capital in excess of par -common	380,000
Retained earnings	131,500
Total stockholders' equity	$1,236,500

What was the average issue price of the **common stock shares**?

Calculations: ($190,000/$1 par)= 190,000 shares issued

(190,000 + 380,000)/190,000 shares = $3

What is the average issue price of the **preferred stock shares**?

Calculations: $500,000/$100 par =5,000 shares issued.

($500,000 +35,000)/ 5,000= $107

What was the total paid-in capital as of December 31, 2010?

Calculations: 500,000 + 35,000 + 190,000 + 380,000

Q2) Prepare journal entries for each of the following transactions.

a. July 1 The corporation issued 40,000 shares of no-par common stock at $12 per share.

b. July 12 The corporation issued 1,500 shares of $50 par, 10% cumulative preferred stock for $134,000.

c. July 28 The corporation issued 5,000 shares of no-par common stock for a patent valued at $80,000.

	Date		Account	Debit	Credit
a.	July	1	Cash	480,000	
			Common stock		480,000
b.	12		Cash	134,000	
			Preferred stock		75,000
			Paid-in capital in excess of par - preferred		59,000
c.	28		Patent	80,000	
			Common stock		80,000

Q3) On December 31, 2008. Answer the questions below the table.

Account	Amount
Common stock, $10 par value	$300,000
Paid-in capital in excess of par - common	270,000
Preferred stock, $50 par value	125,000
Paid-in capital in excess of par - preferred	30,000
Retained earnings	225,000

a. How many shares of common stock have been issued?

b. What was the average issuance price of the common stock?

c. How many shares of preferred stock have been issued?

d. What was the average issuance price of the preferred stock?

e. What is total paid-in capital?

f. What is total stockholders' equity?

a. $300,000 / $10 = 30,000 shares

b. ($300,000 + $270,000) / 30,000 shares = $19 per share

c. $125,000 / $50 = 2,500 shares

d. ($125,000 + $30,000) / 2,500 shares = $62 per share

e. $300,000 + $270,000 + $125,000 + $30,000 = $725,000

f. $725,000 + $225,000 = $950,000

Q4) Hudson Corporation was organized on January 1, 2010. Information related to the corporation's equity section is listed below. Using this information, **prepare the stockholders' equity section** for the balance sheet of Hudson Corporation on December 31, 2010.

Authorized stock: 90,000 shares of $10 par value common stock

50,000 shares of 5%, $50 par value, noncumulative preferred stock

Issued stock: 50,000 shares of common stock at an average issue price of $15

12,000 shares of preferred stock at an average issue price of $68

Retained earnings as of December 31, 2010: $47,000

Hudson Corporation Stockholders' Equity December 31, 2010

Preferred stock, 5%, $50 par, 50,000 shares authorized,12,000 shares issued	$ 600,000
Common stock, $10 par, 90,000 shares authorized, 50,000 shares issued	500,000
Paid in capital in excess of par	466,000
Total paid in capital	1,566,000
Retained earnings	47,000
Total stockholders' equity	$1,613,000

A corporation has 10,000 shares of 10%, $50 par, **noncumulative** preferred stock outstanding and 20,000 shares of no-par common stock outstanding.

At the end of the current year, the corporation declares a dividend of $120,000.

How is the **dividend allocated** between preferred and common stockholders?

Preferred: $50 x 10% x 10,000 shares = $50,000

Common: $120,000 – $50,000 = $70,000

What is the **dividend per share** for preferred shares and for common shares?

Preferred: $50 x 10% = $5 per share x 10,000 shares = $50,000 total;

Common: $120,000 – $50,000 = $70,000 / 20,000 shares = $3.50

A corporation has 15,000 shares of 10%, $50 par **cumulative** preferred stock outstanding and 25,000 shares of no-par common stock outstanding. Dividends of $37,500 are in arrears.

At the end of the current year, the corporation declares a dividend of $120,000.

What is the divided allocated between preferred and common shareholders?

Preferred: $50 x 10% x 15,000 shares = $75,000 current year + $37,500 in arrears = $112,500

Common: \$120,000 – \$112,500 = \$7,500

What is the dividend per share for preferred shares and for common shares?

Preferred: \$50 x 10% x 15,000 shares = \$75,000 current year + \$37,500 in arrears

= \$112,500 / 15,000 shares = \$7.50

Common: \$120,000 – \$112,500 = \$7,500 / 25,000 shares = \$0.30

A corporation has 15,000 shares of 10%, \$50 par, **noncumulative** preferred stock outstanding and 25,000 shares of no-par common stock outstanding. No dividends were declared in 2008. At the end of 2009, the corporation declares a dividend of \$150,000.

What is the dividend allocated between preferred and common shareholders?

Preferred: \$50 x 10% x 15,000 shares = \$75,000

Common: \$150,000 – \$75,000 = \$75,000

Prepare entries for the following transactions.

Dec. 5 The corporation declared the required cash dividend for \$45,000 of \$100 par, 6% cumulative preferred stock, 7,500 shares issued.

Dec. 5 The corporation declared a \$.40 dividend on 130,000 shares of common stock.

Dec. 20 The corporation paid the dividends declared on December 5.

Dec. 31 The corporation sold 5,000 shares of \$10 par value common stock for \$20 per share.

Date	**Account**	**Debit**	**Credit**
Dec. 5	Retained earnings	45,000	
	Dividends payable		45,000
Dec. 5	Retained earnings	52,000	
	Dividends payable (0.4×130000 shares)		52,000
Dec. 20	Dividends payable	97,000	
	Cash (45000+52000)		97,000
Dec. 31	Cash (5000× 20)	100,000	
	Common stock (5000 ×10)		50,000
	Paid in capital in excess of par - common		50,000

The stockholder's equity section for Harris Corporation as of December 31, 2010 is as follows:

Stockholders' Equity December 31, 2010

Preferred stock, 6%, $100 par, cumulative, 10,000 shares authorized, 6,500 shares issued	$ 650,000
Common stock, $10 par, 200,000 shares authorized, 120,000 shares issued	1,200,000
Paid-in capital in excess of par - common	420,000
Total paid-in capital	2,270,000
Retained earnings	467,000
Total stockholders' equity	$2,737,000

For each of the following transactions, indicate the amount of the effect of each transaction on common stock, paid-in capital in excess of par - common, and retained earnings. If appropriate, write "no effect".

Dec. 1 The corporation declared the required cash dividend on the preferred stock and a $1.15 dividend on the common stock.

Dec. 11 The corporation paid the dividends declared on December 1.

Dec. 15 The corporation sold 5,000 shares of common stock for $19 per share.

Date	**Common Stock**	**Paid in capital in excess of par-common**	**Retained earnings**

Date	**Common Stock**	**Paid in capital in excess of par-common**	**Retained earnings**
Dec. 1	No effect	No effect	($177,000)*
Dec. 11	No effect	No effect	No effect
Dec. 15	$50,000	$45,000	No effect

* 6,500 × $100 × .06 =	$ 39,000
$1.15 × 120,000	138,000
Total dividends	$177,000

On January 1, 2010, a corporation issued 25,000 shares of 10%, $50 par, **cumulative preferred stock** and 50,000 shares of $30 par common stock. Cash dividends declared by the board were as follows. Determine the amount of total dividends and dividends per share for preferred stockholders and common stockholders.

2010	none
2011	$100,000
2012	$275,000
2013	$305,000
2014	$355,000

Year	Total Preferred	Per Share Preferred	Total Common	Per Share Common
2010				
2011				
2012				
2013				
2014				

Year	Total Preferred	Per Share Preferred	Total Common	Per Share Common
2010	$0	$0	$0	$0
2011	$100,000	$4.00	$0	$0
2012	$275,000	$11.00	$0	$0
2013	$125,000	$5.00	$180,000	$3.60
2014	$125,000	$5.00	$230,000	$4.60

A corporation reports the following stockholders' equity as of December 31, 2010.

Preferred stock 10%, $50 par, **cumulative**, 100,000 shares authorized, 90,000 shares issued	$ 4,500,000
Paid-in capital in excess of par - preferred	945,000
Common stock, $10 par, 200,000 shares authorized, 200,000 shares issued	2,000,000
Paid-in capital in excess of par - common	800,000
Total paid-in capital	8,245,000
Retained earnings	3,400,000
Total stockholders' equity	$11,645,000

a. What was the average issue price per share of common stock?

b. What was the average issue price per share of preferred stock?

c. The board of directors declares dividends of $1,900,000 in 2010. No dividends were declared in 2011 and there were no dividends in arrears prior to 2011. What is the amount per share each class of stock will receive?

a. ($2,000,000 + $800,000) / 200,000 = $14.00

b. ($4,500,000 + $945,000) / 90,000 = $60.50

c. Preferred - ($4,500,000 × 10% × 2) / 90,000 = $10.00

Common - ($1,900,000 - (90,000 × $10. 00)) / 200,000 = $5.00