

Chapter 11 Study Guide: Stockholders' Equity

1. Introduction to Stockholders' Equity

- **Stockholders' Equity** represents the ownership interest in a corporation, consisting of two primary components:
 1. **Contributed Capital** (or Paid-In Capital): Money invested by stockholders, primarily through the issuance of stock.
 2. **Retained Earnings**: Cumulative net income or loss that has been retained in the company and not paid out as dividends.
- **Formula for Stockholders' Equity:**

$$\text{Stockholders' Equity} = \text{Contributed Capital} + \text{Retained Earnings}$$

2. Components of Stockholders' Equity

- **Contributed Capital (Paid-In Capital):**
 - Represents the funds raised through the issuance of stock.
 - Includes:
 - **Common Stock**: Represents ownership interest in the company and is the most basic type of stock.
 - **Preferred Stock**: A type of stock that gives stockholders priority in dividends and liquidation, but typically does not carry voting rights.
 - **Additional Paid-In Capital**: The amount received from stock issuance that is above the par value of the stock.
 - **Retained Earnings:**
 - Cumulative amount of net income retained in the company after dividends are paid.
 - **Retained Earnings** = Previous Retained Earnings + Net Income - Dividends.
 - **Dividends:**
 - A distribution of a portion of the company's earnings to stockholders.
 - Types of dividends include:
 - **Cash Dividends**: Cash payments to stockholders.
 - **Stock Dividends**: Additional shares of stock given to stockholders instead of cash.
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3. Issuance of Stock

- **Common Stock Issuance:**
 - The company issues stock to raise funds, usually through an **Initial Public Offering (IPO)** or secondary offering.
 - **Journal Entry for Common Stock Issuance:**
 - **Debit:** Cash (amount received)
 - **Credit:** Common Stock (par value)
 - **Credit:** Additional Paid-In Capital (amount above par value)
 - **Preferred Stock Issuance:**
 - Preferred stock is issued similarly to common stock but typically has a fixed dividend and preference over common stock in case of liquidation.
 - **Journal Entry for Preferred Stock Issuance:**
 - **Debit:** Cash (amount received)
 - **Credit:** Preferred Stock (par value)
 - **Credit:** Additional Paid-In Capital (above par value)
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4. Dividends

- **Cash Dividends:**
 - **Declaration Date:** The date the board of directors announces a dividend.
 - **Record Date:** The date on which stockholders must own shares to receive the dividend.
 - **Payment Date:** The date on which the dividend is actually paid to stockholders.
 - **Journal Entries for Cash Dividends:**
 - **Declaration Date:**
 - **Debit:** Retained Earnings (amount of the dividend)
 - **Credit:** Dividends Payable (amount of the dividend)
 - **Payment Date:**
 - **Debit:** Dividends Payable (amount of the dividend)
 - **Credit:** Cash (amount paid)
 - **Stock Dividends:**
 - Stock dividends are distributions of additional shares of stock instead of cash.
 - **Journal Entry for Stock Dividends:**
 - **Debit:** Retained Earnings (value of stock dividends)
 - **Credit:** Common Stock (par value of the additional shares issued)
 - **Credit:** Additional Paid-In Capital (value above par)
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5. Stockholders' Equity on the Balance Sheet

- **Format:** The stockholders' equity section typically appears below the liabilities section on the balance sheet. It includes:
 - Common Stock
 - Preferred Stock
 - Additional Paid-In Capital
 - Retained Earnings
 - Less: Treasury Stock (if applicable)
 - **Treasury Stock:**
 - Represents shares of the company's stock that have been repurchased but not retired. Treasury stock reduces stockholders' equity.
 - **Journal Entry for Treasury Stock:**
 - **Debit:** Treasury Stock (cost of repurchased shares)
 - **Credit:** Cash (amount paid for repurchase)
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6. Key Terms to Know

- Common Stock
 - Preferred Stock
 - Additional Paid-In Capital
 - Retained Earnings
 - Dividends
 - Cash Dividends
 - Stock Dividends
 - Treasury Stock
 - Stockholder's Equity
 - Paid-In Capital
 - Stock Issuance
 - Par Value
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Practice Questions for Chapter 11: Stockholders' Equity

1. Issuance of Common Stock

Problem 1.1: Common Stock Issuance

ABC Corp. issues 1,000 shares of common stock with a par value of \$1 per share for \$10 per share. What is the journal entry to record the issuance?

2. Issuance of Preferred Stock

Problem 2.1: Preferred Stock Issuance

XYZ Corp. issues 500 shares of preferred stock with a par value of \$100 per share for \$120 per share. What is the journal entry to record the issuance?

3. Cash Dividend Declaration and Payment

Problem 3.1: Cash Dividend

ABC Corp. declares a \$2,000 dividend to be paid to stockholders on the record date. The dividend will be paid on March 31. What are the journal entries for the declaration date and payment date?

4. Stock Dividend Declaration

Problem 4.1: Stock Dividend

XYZ Corp. declares a 10% stock dividend on its 1,000 shares of common stock, with a par value of \$1 per share. The market price of the stock is \$15 per share. What is the journal entry to record the stock dividend?

5. Treasury Stock Transactions

Problem 5.1: Treasury Stock

ABC Corp. repurchases 200 shares of its own stock for \$30 per share. What is the journal entry to record the repurchase?

6. Stockholders' Equity Calculation

Problem 6.1: Stockholders' Equity

The following information is provided for XYZ Corp. at the end of the year:

- Common Stock (1,000 shares, \$1 par value): \$1,000
- Additional Paid-In Capital: \$4,000
- Retained Earnings: \$10,000
- Treasury Stock (50 shares at \$10 per share): \$(500)

What is the total stockholders' equity?

Answers to Practice Questions

Problem 1.1: Common Stock Issuance

- **Journal Entry:**
 - **Debit:** Cash \$10,000 (1,000 shares × \$10)
 - **Credit:** Common Stock \$1,000 (1,000 shares × \$1 par value)
 - **Credit:** Additional Paid-In Capital \$9,000 (the difference)
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Problem 2.1: Preferred Stock Issuance

- **Journal Entry:**
 - **Debit:** Cash \$60,000 (500 shares × \$120)
 - **Credit:** Preferred Stock \$50,000 (500 shares × \$100 par value)
 - **Credit:** Additional Paid-In Capital \$10,000 (the difference)
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Problem 3.1: Cash Dividend Declaration and Payment

- **Journal Entry on Declaration Date:**
 - **Debit:** Retained Earnings \$2,000
 - **Credit:** Dividends Payable \$2,000
 - **Journal Entry on Payment Date:**
 - **Debit:** Dividends Payable \$2,000
 - **Credit:** Cash \$2,000
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Problem 4.1: Stock Dividend Declaration

- **Journal Entry:**
 - **Debit:** Retained Earnings \$15,000 (1,000 shares × 10% × \$15 market price)
 - **Credit:** Common Stock \$1,000 (1,000 shares × 10% × \$1 par value)
 - **Credit:** Additional Paid-In Capital \$14,000 (the difference)
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Problem 5.1: Treasury Stock

- **Journal Entry:**
 - **Debit:** Treasury Stock \$6,000 (200 shares × \$30)
 - **Credit:** Cash \$6,000
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Problem 6.1: Stockholders' Equity

- **Stockholders' Equity Calculation:**
 - Common Stock: \$1,000
 - Additional Paid-In Capital: \$4,000
 - Retained Earnings: \$10,000
 - Treasury Stock: \$(500)
 - **Total Stockholders' Equity** = \$1,000 + \$4,000 + \$10,000 - \$500 = **\$14,500**