

P13-1

a.

April 1:

Cash	16,000,000
Common stock	
4,000,000	
Additional paid in capital	
12,000,000	

May 1:

Beginning balance	200,000	shares
Additional shares issued	400,000	shares
Total shares outstanding	600,000	
Percent of stock dividend	10%	
Shares issued in stock dividend	60,000	
Market price per share	\$42	
Retained earnings capitalized:	\$2,520,000	
Retained earnings	2,520,000	
Common stock (60,000 × \$10)		600,000
Capital in excess of par		1,920,000

Sept 1: No entry required. The description of the stock will change. The number of shares outstanding will increase to 2,640,000 (660,000 × 4). The par value will decrease to \$2.50. (\$10/4)

October 1:

Treasury stock	2,250,000	
Cash		2,250,000

b.	TRANSACTION	ASSETS	LIABILITIES	EQUITY
	April 1	I	NE	I
	May 1	NE	NE	NE
	September 1	NE	NE	NE
	October 1	D	NE	D

c.	Transaction	Change in Number of shares	Shares outstanding
	Beginning balance	—	200,000
	April 1	400,000	600,000
	May 1	60,000	660,000
	Sept 1	1,980,000	2,640,000
	Oct 1	(50,000)	2,590,000

P13-2

a.

Annual dividend requirement on cumulative preferred:
 $\$30,000,000 \times .08 =$ $\$2,400,000$

<u>Dividends declared in 2004</u>	<u>2,000,000</u>
Dividends in arrears at 12/31/04	\$ 400,000
2000 Dividend requirement:	
Cumulative preferred arrears	\$ 400,000
Cumulative preferred current	2,400,000
Cumulative preferred requirement	\$2,800,000
<u>Dividend for common: 1,200,000 × \$2</u>	<u>2,400,000</u>
Total dividend needed	\$5,200,000

Note: Treasury stock does not participate in the dividend.

b. A 25% stock dividend will result in a transfer of \$18,000,000 from Retained earnings to common stock and Additional paid in capital.

Shares currently outstanding	1,200,000
Percent of stock dividend	25%
New shares issued	300,000
Market price per share	\$60
Total retained earnings capitalized	\$18,000,000

Entry:

Retained earnings (300,000 × 60)	18,000,000	
Common stock (300,000 × 10)		3,000,000
Additional paid-in capital		15,000,000

Since this is a transfer from one stockholders' equity account into other stockholders' equity accounts, the transaction will have no effect on total stockholders' equity.

c. All shares authorized, issued, and outstanding will double as the result of a 2 for 1 stock split. The par value of the shares will decrease to \$5 per share. Shares authorized will increase to 4,000,000; shares issued to 3,000,000, treasury shares to 600,000. There will be no change in the dollar amounts of any stockholders' equity account.

P13-4

a.

Basic earnings per share:
 Net income – Preferred dividends = \$5,000,000 – 600,000
 / Weighted average shares outstanding 400,000
 = \$11.00

b.

Diluted earnings per share:
 Numerator $\$5,000,000 + 48,000 =$ $\$5,048,000$
 \ Denominator $400,000 + 100,000 + 4,000 + 1,000 =$ $505,000$
 = \$10.00

P13-5

- a. Total selling price of preferred:
 Preferred stock \$4,000,000
Paid in capital 480,000
 Total \$4,480,000
 Number of shares of preferred issued: 40,000
 Average issue price: \$4,480,000/40,000 = \$112.00
- b. Common shares issued: 600,000
Treasury stock (50,000)
 Common shares outstanding 550,000
- c. Cash 2,010,000
 Common stock 600,000
 Additional paid in capital 1,410,000
- d. Cash 400,000
 Treasury stock 300,000
 Paid in capital—Treasury stock 100,000
- e. $\$4,000,000 \times .07 = \$280,000$ or $\$7$ per share $\times 40,000 = \$280,000$
- f. Preferred dividend = $\$280,000/40,000 = \7.00 per share
 Total dividend: \$580,000
 Preferred dividend (280,000)
 Common dividend $\$300,000/550,000$ shares outstanding = \$0.5455 per share
- g. Common shares outstanding: 550,000
 Percent of stock dividend 10%
 Common stock dividend 55,000
 Market price per share \$80
 Retained earnings capitalized \$4,400,000
- Retained earnings 4,400,000
 Common stock (55,000 \times \$1) 55,000
 Additional paid in capital—Common 4,345,000
- h. Net income – Preferred dividends = $\$1,560,000 - 280,000$
 \ Common shares outstanding = 550,000
 = \$2.33
- i. Shares outstanding before split: $550,000/2 = 275,000 \times 3 = 825,000$ shares
- j. The stock split has no effect on net income. Total assets, liabilities, and

equity remain unchanged. To accommodate the additional shares, the par value will be reduced to \$0.67 per share (rounded).

Before split: $600,000$ shares issued \times \$1 = \$600,000

After split: $(600,000/2) \times 3 = 900,000$

$\$600,000/900,000 = \0.67 per share

A stock split has no effect on cash flows.

- k. Total market capitalization before split: $550,000 \times \$80 = \$44,000,000$
 Total market capitalization: \$44,000,000
 / Shares outstanding after split 825,000
 = \$2.33

P13-6

- a. Beginning shares: 400,000
April 1 shares 600,000
 Balance before stock dividend 1,000,000
Shares issued in stock dividend 100,000
 Shares outstanding before split 1,100,000
Stock split 1,100,000
 Shares outstanding 2,200,000
Treasury stock acquired (100,000)
 Shares outstanding at year end 2,100,000

b. The weighted average number of shares must be restated retroactively for the stock dividend and stock split. These shares are assumed to have been outstanding at the beginning of the year. Restatement is not necessary for treasury shares, since they were acquired after the stock dividend and stock split.

	Number of shares	Restatement	Fraction of year	Weighted shares
Jan 1–April 1	$400,000 \times 1.1 \times 2$	880,000	3/12	220,000
April 1–Oct 1	$1,000,000 \times 1.1 \times 2$	2,220,000	6/12	1,100,000
<u>Oct 1–Dec 31</u>		<u>2,100,000</u>	<u>3/12</u>	<u>525,000</u>
Weighted average shares				1,845,000

P13-7

- . The par value is \$0.01 per share: Common stock: \$3,732
 Shares issued and outstanding at 12/31/00 373,218
 = .01

b. The company uses the same number of shares because the convertible shares are anti-dilutive. If the company used the increased number of shares in

its computation of earnings per share, the loss per share would decrease. In this circumstance anti-dilutive securities are excluded from the calculation of earnings per share.

c. Shares issued and outstanding at December 31, 2000:	357,140,000
<u>Shares issued and outstanding at December 31, 2001:</u>	<u>373,218,000</u>
Additional shares issued during 2001:	16,078,000

d. Increase in common stock account	\$ 119,000
<u>Increase in additional paid-in-capital account</u>	<u>143,934,000</u>
Total consideration received:	\$144,053,000

Cash	144,053,000	
Common stock		119,000
Additional paid-in-capital		143,934,000

e. The net loss increased the accumulated deficit:	
Balance at 12/31/2000	\$(2,293,301,000)
<u>Net loss in 2001</u>	<u>(567,277,000)</u>
Balance at 12/31/2001	\$(2,860,578,000)

f. It is highly unlikely that Amazon.com will pay a dividend. The company has negative total stockholders' equity. A dividend payment would likely violate state laws as well as numerous loan covenants on Amazon.com's enormous debt. The company needs to conserve all cash to pay down debt levels.

P13-8

a.		2000	2001
Cash and short-term investments:	\$23,798	\$31,600	
Total current assets	30,308	39,637	
Percentage of current assets:	78.5%	79.7%	
Cash and short-term investments:	\$23,798	\$31,600	
Total assets	52,150	59,257	
Percentage of total assets:	45.6%	53.3%	

The amount of cash and cash equivalents has increased, both as a percentage of current assets and as a percentage of total assets. The company has nearly 80% of current assets and more than 50% of total assets in cash and highly liquid investments.

b. While the amount of cash and cash equivalents represents an extremely liquid and low risk position, it does not show the use of assets that investors in growth stocks would like to see. Generally, the return on these assets is very low. In order to generate sufficient returns to its stockholders, the company must invest in projects that earn higher returns.

- c. Arguments in favor of Microsoft paying a dividend:
- The company has sufficient resources to continue to invest in Research and Development to be able to pay a dividend.
 - Attractive dividend yields shorten an investor's break-even period in a stock purchase.
 - Companies that pay dividends are viewed as financially sound.
 - Dividends cannot be manipulated or restated after the fact. They are not ambiguous.
 - Microsoft is no longer the super growth company that it was. If it cannot find investments with higher returns, it should return the cash to the stockholders, who can invest it on their own.

Arguments against Microsoft paying a dividend:

- Dividends are unfavorably taxed. The company pays dividends from after-tax dollars. The dividend is then taxed as income to the recipient. Stockholders may favor returns resulting from capital gains, which are taxed favorably in the United States tax code.
- Stockholders who have invested in Microsoft have not sought out a dividend-paying stock. They are paying for growth and would like to see the company reinvest all earnings to achieve maximum growth.
- Other comprehensive income could include unrealized gains or losses on available-for-sale securities, foreign currency gains and losses and other "income" type transactions that currently bypass the income statement according to GAAP regulations.
- Shares issued and outstanding at June 30, 2000: 5,283,000,000
Shares issued and outstanding at June 30, 2001: 5,383,000,000
Increase in shares issued: 100,000,000
- Shares authorized at June 30, 2001: 12,000,000,000
Shares issued and outstanding at June 30, 2001: 5,383,000,000
Additional shares that could be issued: 6,617,000,000
- It is highly unlikely at this time that Microsoft would have a secondary offering of its common stock. The company is highly liquid; a secondary offering would dilute the holdings of current shareholders. Such an offering would probably have a negative impact on Microsoft's stock price.

P13-9

a.	There were 69,300,000 shares issued at 12/31/01.
	Common stock \$34,650,000

f.	Cash	20,000,000	
	Treasury stock		17,167,000
	Additional paid-in-capital		2,833,000

g. There would be no impact on the income statement. Assets would increase by \$20 million and stockholders' equity would increase by \$20 million. Cash flows from financing activities would increase by \$20 million.

h.	Retained earnings	106,000	
	Dividends payable		106,000
	Dividends payable	106,000	
	Cash		106,000