

1. A corporate charter is a legal document establishing the corporation under the laws of the jurisdiction of incorporation, which specifies the types of equities, their terms, and the number of shares that may be issued.
2. The three important rights of the owners of a corporation are: 1) the right to control how the corporation uses its assets, what liabilities it incurs, corporate strategies and policies; 2) the right to receive the benefits produced by the corporation after other providers of capital have been paid what they are contractually obligated to receive; and 3) the right to transfer ownership to someone else.
3. Shareholder resolutions are policies voted on by shareholders that mandate or prohibit specific policies or behavior of corporate officers.
4. Preferred shareholders have the right to receive dividends before dividends can be paid to voting common shareholders and they have a senior claim against the assets of the firm relative to common shareholders.
5. The four features that distinguish debt from equity are: 1) debt agreements specify the payments due to their holders, 2) debt agreements determine the maximum amount that a debt holder is entitled to receive, 3) debt holders have the right to payments before equity holders in the event of a default, and 4) debt holders have no control or decision rights.
6. Preferred stock is often described as a hybrid security because, like stock, it has limited equity rights while generally possessing an entitlement to specified dividends. While the dividends are not legally enforceable, they must be paid before any common dividends are paid, making it look like a bond.
7. Redeemable preferred stock can be exchanged with the corporation for cash equal to its par value.
8. Cumulative preferred stock requires that any dividends on the preferred that have been omitted be paid before any dividend is paid on common stock.
9. A stock warrant is the right to buy common stock at a specified price any time up to a specified date.
10. Authorized refers to the number of shares that the corporate charter or stock contract allows to be issued. Issued is the number of shares that were sold to the public. Outstanding refers to the number of shares still publicly owned.
11. Unearned compensation ESOP and Accumulated other comprehensive income represent accounting adjustments that bypass the income statement. While not a component of income, the effects of the transactions leading to these accounts represent equity claims and must appear in the equity section of the balance sheet.
12. Treasury stock represents shares of its own common stock that have been purchased by the company on the open market. It is a contra-equity account.
13. While technically treasury stock represents stock that has been retired, frequently treasury shares are reissued. More often, treasury stock would

- represent shares that are temporarily out of market circulation.
14. Treasury stock is not an asset because companies cannot own themselves.
15. There are no income statement effects from gains or losses on the sale of treasury stock. Such gains or losses would represent increases or decreases to stockholders' equity.
16. Dividends become a liability when they are declared by the board of directors.
17. The company would debit Retained earnings and credit Dividends payable for \$100 when the dividend is declared.
18. The company would debit Dividends payable and credit Cash for \$100 when the dividends are paid.
19. There is no accounting entry for a 3 for 1 stock split; instead the number of shares outstanding and their par value must be adjusted to represent the additional number of shares.
20. Other than the change in the number of shares outstanding and the reduction in the par value of the shares, there is no effect on the income statement and balance sheet from a 3 for 1 stock split.
21. A stock dividend is a small stock split of 20–25% or less of the shares of common stock.
22. There is no effect on the income statement from a 10% stock dividend. On the balance sheet, there would be a reclassification of Retained earnings into Common stock and Additional paid in capital in an amount equal to the number of shares in the dividend times the market price of the stock on the day of the dividend. This is referred to as "capitalizing" retained earnings.
23. Basic earnings per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during the year. Diluted earnings per share is a pro forma number that assumes conversion of all convertible securities. It is a "worst case" scenario that informs investors of the possible dilution that could take place in earnings per share if all of those securities were converted.
24. Since earnings per share refers to earnings per share of common stock, any portion of the earnings that is earmarked for preferred stockholders must be deducted to determine the income available to common shareholders.
25. Dilution is a reduction in the ownership claim of existing shareholders because of the exercise of options, the issuance of more shares of stock, and conversion of bonds and preferred stock into common stock.
26. Anti-dilutive securities are those that would increase diluted earnings per share if converted to common shares. Anti-dilutive securities are excluded from the calculation of diluted earnings per share.