

Solutions to Practice Quiz

Chapter 11 – Equity Financing and Shareholders' Equity

Multiple Choice Questions. Identify the answer that BEST completes the statement or answers the question.

1. During the year, Smith & Sons issued 1,000 shares of its \$1.00 par value common stock for \$15 per share, and declared and paid cash dividends totaling \$0.50 per share.

By what amount does contributed capital increase as a result of these events?

- a. \$15,000
- b. \$ 500
- c. \$14,500
- d. \$14,750

Answer: a

Rationale: (1,000 shares x \$15.00)

2. The Claremont Company began the year with a balance in retained earnings of \$60,000 and 40,000 shares of \$1 par common stock outstanding. During the year, the company reported sales of \$240,000, expenses of \$200,000, and declared and paid a \$0.40 per share cash dividend.

How much is the balance in the Retained Earnings account at the end of the year?

- a. \$ 80,000
- b. \$104,000
- c. \$ 84,000
- d. \$ 23,000

Answer: c

Rationale: [\$60,000 + (\$240,000 - \$200,000) – (40,000 shares x \$0.40)]

3. Keck Enterprises reported the following information at December 31:

Preferred Stock, \$5 par, 10,000 shares authorized	\$ 7,500
Additional paid-in capital – preferred stock	9,900
Common stock, \$1.00 par, 6,000 shares authorized	3,300
Additional paid-in capital – common stock	8,700
Retained earnings	17,000
Treasury stock, at cost of \$4 per share	<u>(2,000)</u>
Total	\$44,400

How many shares of common stock are outstanding?

- a. 2,200
- b. 3,300
- c. 2,800
- d. 5,600

Answer: c

Rationale: [$\$3,300 / \1 par value] – [$\$2,000 / \4 par value]

4. Keck Enterprises reported the following information at December 31:

Preferred Stock, \$5 par, 10,000 shares authorized	\$ 7,500
Additional paid-in capital – preferred stock	9,900
Common stock, \$1.00 par, 6,000 shares authorized	3,300
Additional paid-in capital – common stock	8,700
Retained earnings	17,000
Treasury stock, at cost of \$4 per share	<u>(2,000)</u>
Total	\$44,400

What is the average selling price for each share of preferred stock?

- a. \$5.00
- b. \$0.75
- c. \$2,500
- d. \$11.60

Answer: d

Rationale: $(\$7,500 + \$9,900) / [\$7,500 / \$5]$

5. Keck Enterprises reported the following information at December 31:

Preferred Stock, \$5 par, 10,000 shares authorized	\$ 7,500
Additional paid-in capital – preferred stock	9,900
Common stock, \$1.00 par, 6,000 shares authorized	3,300
Additional paid-in capital – common stock	8,700
Retained earnings	17,000
Treasury stock, at cost of \$4 per share	<u>(2,000)</u>
Total	\$44,400

Keck's stock was selling for \$22 per share at year-end.

If the company declares a 10% common stock dividend, what will be the amount of total shareholders' equity at year-end?

- a. \$44,400
- b. \$27,400
- c. \$10,800
- d. \$28,600

Answer: a

6. Pomona Enterprises has 1,000,000 authorized shares of \$1 par value common stock, with 100,000 shares issued and outstanding with a total current market value of \$150,000. You are the owner of 12% of the stock.

Which statement describes what happens when the company executes a 3-for-1 forward stock split?

- a. You will own 36% of the company's stock after the split
- b. Your ownership is worth \$450,000 after the split
- c. You return your original shares to the company, and receive 36,000 new shares in exchange
- d. You receive 36,000 additional shares of stock

Answer: c

7. Upon submitting its corporate charter to the state, Drucker Corporation was granted permission to issue 5,000 shares of \$1.00 par value common stock. Net income for the year was \$300,000. In addition, the following transactions took place during the year:

January 2: Investors paid the company \$14 each for 2,000 shares of common stock

March 12: Drucker purchased 300 shares of its own common stock for \$13 per share

October 31: Drucker declared a 2-for-1 forward stock split

As of December 31, how many shares are issued, and how many shares are outstanding?

- a. Issued, 4,000; Outstanding, 3,400
- b. Issued, 3,200; Outstanding, 3,400
- c. Issued, 3,800; Outstanding, 1,600
- d. Issued, 3,400; Outstanding, 3,400

Answer: a

Rationale:

Issue: (2,000 shares x 2)

Outstanding: (2,000 shares – 300 shares) x 2

The following information applies to Questions 8 and 9:

Office Supply Corporation purchased 8,000 shares of treasury stock at \$14 per share. The stock had a par value of \$5 and had been issued at an average price of \$8.

8. To record the acquisition of the treasury stock would require:
- a. An increase to Treasury Stock for \$112,000
 - b. A decrease to Common Stock for \$40,000
 - c. A decrease to Additional Paid-In Capital, Common Stock for \$32,000
 - d. An increase to Treasury Stock for \$64,000

Answer: a

Rationale: (8,000 shares x \$14 per share)

9. A few months later, 3,000 shares of the treasury stock were reissued at \$20 per share. To record this transaction requires an increase to:
- a. Additional Paid-in Capital, Treasury Stock for \$45,000
 - b. Common Stock for \$15,000
 - c. Treasury Stock for \$60,000
 - d. Additional Paid-in Capital, Treasury Stock for \$18,000

Answer: d

Rationale: $[3,000 \text{ shares} \times (\$20 - \$14)]$

10. Dividends in arrears (unpaid in prior years) on cumulative preferred stock:
- a. Are considered to be a non-current liability
 - b. Are considered to be a current liability
 - c. Only occur when preferred dividends have been declared
 - d. Should be disclosed in the notes to the financial statements

Answer: d