1. Answer: D – Limited liability and transferability of ownership are advantages, not disadvantages, of a corporate form of business. Corporations are subject to more, not less regulation.
2. Answer: A – Companies may issue shares and later buy those share back from the stockholders. The repurchased shares are called treasury stock. The amount of outstanding shares is equal to the amount of shares issued minus the treasury stock. As a result, if a company has treasury stock the number of shares issued will be greater than the number of shares outstanding.
3. Answer: A – Normally, the right to vote on the membership of the board of directors and major policies and practices of operating the corporation are limited to common stockholders. However, even certain classes of common stock may be issued without voting rights.
4. Answer: A – Preferred shareholders are entitled to a $50,000 ($50 par value x .05 dividend x 20,000 shares) per year dividend. At the end of 2015, because no dividend was paid, there were $50,000 of preferred dividends in arrears. At the end of 2016, all $40,000 in dividends were paid to the preferred shareholders, leaving $60,000 in arrears ($50,000 from 2015 and $10,000 from 2016). At the end of 2017, all $90,000 in dividends were paid to the preferred shareholders ($60,000 in arrears, plus $30,000 of the 2017 dividend), leaving $20,000 in arrears.
5. Answer: C – Preferred shareholders are entitled to a $50,000 ($50 par value x .05 dividend x 20,000 shares) per year dividend. Because the preferred stock is non-cumulative, the preferred dividends that were owed but not paid in 2015 and 2016 are disregarded. In 2017, $50,000 of the dividend will be paid to the preferred stockholders, with the remaining $40,000 paid to the common stockholders.
6. Answer: C – When Gleason issues the stock, assets (cash) increase and two stockholders’ equity accounts increase. Debit entries increase asset accounts and credit entries increase stockholders’ equity accounts. In this case the asset account (cash) is debited, the stockholders’ equity accounts (common stock and additional paid-in capital in excess of par value) are credited.
7. Answer: B – Normally par value, stated value and no-par value accounts are shown first. Any associated paid-in excess accounts are shown next. The total of all of these accounts is shown under the title “Total Paid-in Capital”. The balance in retained earnings is then shown after the Total Paid-in Capital.
8. Answer: B – Purchasing treasury stock has the opposite effect on the financial statements as issuing stock. When treasury stock is purchased, assets (cash) decrease and treasury stock increases. Note that treasury stock is a contra equity account. As a result, increasing the treasury stock account decreases total stockholders’ equity. Purchasing treasury stock does not affect the income statement. Treasury stock transactions are transactions between a corporation and its investors and therefore, are financing activities.
9. Answer: D – When treasury stock is sold, assets (cash) increase and treasury stock decreases. Note that treasury stock is a contra equity account. As a result, decreasing the treasury stock account increases total stockholders’ equity. Since the treasury stock was sold for $2 ($18 sales price - $20 acquisition price) less than it cost, the company must use $800 of retained earnings to make up the difference. Treasury stock transactions are transactions between a corporation and its investors and therefore, are financing activities.
10. Answer: C – When treasury stock is sold, assets (cash) increase and treasury stock decreases. Note that treasury stock is a contra equity account. As a result, decreasing the treasury stock account increases total stockholders’ equity. Since the treasury stock was sold for $2 ($22 sales price - $20 acquisition price) more than it cost, the company must recognize $800 ($2 x 400 shares) of additional paid-in capital from treasury stock transactions. Debit entries increase asset accounts and credit entries increase equity accounts. In this case, the asset account (cash) is debited and the stockholders’ equity accounts (treasury stock and paid-in capital from treasury stock transactions) are credited.
11. Answer: A – October is the declaration date. The declaration of a cash dividend is a claims exchange event. A liability account (dividends payable) increases and a stockholders’ equity account (retained earnings) decreases. Since dividends are not sacrifices incurred to generate revenue, there is no impact on the income statement. Since cash was not collected or paid, there is no impact on the statement of cash flows
12. Answer: B – Number of shares: 30,000 shares x .05 dividend = 1,500 shares

Amount to transfer from retained earnings: 1,500 shares x $40 per share = $60,000

Par value of stock issue: 1,500 shares x $10 par value = $15,000

Additional paid-in capital in excess of par: 1,500 shares x ($40 market value - $10 par) = $45,000

A stock dividend is a claims exchange event. The retained earnings account decreases by $60,000, the common stock account increases by $15,000 (1,500 shares x $10 par value) and the additional paid-in capital in excess of par value increases by $45,000 ($60,000 - $15,000). Since dividends do not affect the determination of net income, the income statement is not affected. Since cash was not collected or spent, the statement of cash flows is not affected

1. Answer: A – A two for one stock split will double the number of shares of stock outstanding but will have no effect to the total amount of assets, liabilities, or stockholders’ equity. Since the account balances do not change there is no need to record a journal entry