

# Organizing a Corporation and Paying Dividends

Section 11.1 Starting a Corporation

# Section 11.3

## Calculating and Journalizing Dividends for a Corporation

A new corporation will usually *retain* a portion of net income to finance future expansions & improvements.

Most will try to distribute a portion of earnings to its *stockholders*.

These earnings are called \_\_\_\_\_.

# Declaring a Dividend

*Dividends* – Corporate earnings distributed to stockholders.

*Declaring a dividend* – Action by the board of directors to distribute corporate earnings to stockholders.

- Board determines when and what amount of the *retained earnings* will be distributed.
- A corporation has no obligation to distribute money to stockholders until the board of directors has *declared a dividend*.

# Declaring a Dividend

Three important dates are involved in distributing a dividend:

## 1. Date of declaration

- The date on which a board of directors votes to distribute a dividend.

## 2. Date of record

- The date that determines which stockholders are to receive dividends.
- Stockholders can buy and sell any time; only those listed as stockholders on the *date of record* are eligible to receive dividends.

## 3. Date of payment

- The date on which dividends are actually to be paid to the stockholders.
- Usually occurs several weeks after the date of record.

# Declaring a Dividend

Three important dates are involved in distributing a dividend:

1. Date of declaration
2. Date of record
3. Date of payment

Transactions are recorded in a corporation's accounts on two of the three dates:

1. Date of declaration
2. Date of payment

# Calculating a Dividend

## Declaring a Dividend

- Once a board of declares a dividend, the corporation is obligated to pay it.
- At the *date of declaration* the corporation incurs a *liability* that must be recorded.

# Calculating a Dividend

CompuForm declares an annual dividend of \$24,000.

On the date of record, the corporation has issued 1,000 shares of 8%, \$100 par-value preferred stock & 16,000 shares of \$20 stated-value common stock.

How to calculate the value of preferred and common stock:

<i>Number of shares</i>	<i>X</i>	<i>Par Value</i>	<i>=</i>	<i>Value of</i>
<i>Preferred Stock</i>				
1,000		\$100		\$100,000
<i>Number of shares</i>	<i>X</i>	<i>Par Value</i>	<i>=</i>	<i>Value of</i>
<i>Common Stock</i>				
16,000		\$20		\$320,000

# Calculating a Dividend

CompuForm declares an annual dividend of \$24,000.

How to calculate the value of preferred and common stock:

*Number of shares* X *Par Value* = *Value of Preferred Stock*

1,000                      \$100                      \$100,000

*Number of shares* X *Par Value* = *Value of Common Stock*

16,000                      \$20                      \$320,000

**VERY IMPORTANT:**

The value of preferred stock is used to calculate the dividend on preferred stock.



# Calculating a Dividend

CompuForm declares an annual dividend of \$24,000.

*Value of Preferred Stock - \$100,000*  
\$320,000

*Value of Common Stock -*

*Val. of Pref. Stock* X *Pref. Div. Rate* = *Pref. Div. Amount*

\$100,000

8%

\$8,000

*Total amnt. Avail. For Div. Avail. For Common Div.*      *Pref. Div. Amnt.* = *Amnt.*

\$24,000

\$8,000

\$16,000

The dividend rate for common stock is calculated as follows:

*Com. Div. Amnt.* ÷ *Val. of Com. Stock* = *Com. Div. Rate*

\$16,000

\$320,000

5%

# Summary of CompuForm's dividends

	Amount	Rate
Preferred Stock Dividends	\$ 8,000	8%
Common Stock Dividends	\$16,000	5%

CompuForm may elect to increase its annual dividend.

- The preferred stock dividend rate will never exceed 8%.
- Additional dividends will be distributed to common stock.
- The common stock dividend rate may be less than, equal to, or more than the preferred stock dividend rate.



# Journalizing Payment of a Dividend

January 15. Paid cash for annual dividend declared December 15, \$24,000. Check No. 432.

- Check 432 is deposited in a special dividend checking account.
- A separate check is written to each stockholder from this account.
- Why?
  1. Avoids a large number of entries in the Cash Payment Journal.
  2. Reserves cash specifically for paying the dividends.
- Check is given to the agent who handles preparing and mailing checks to the stockholders.

*Remember: Dividends may be paid in additional capital stock, known as a stock dividend, instead of cash. Dividends Payable is debited and Capital Stock is credited when the stock is issued on the date of payment.*



# Audit your understanding

Who determines when and what amount of retained earnings that a corporation will distribute as dividends?

Answer:

Board determines when and what amount of the *retained earnings* will be distributed.

# Audit your understanding

Why does a corporation record a liability when a dividend is declared?

Answer:

The corporation is obligated to pay the dividend.

# Audit your understanding

What are two reasons for using a special dividend checking account?

Answer:

1. Avoids a large number of entries in the Cash Payment Journal.
2. Reserves cash specifically for paying the dividends.



# Work Together

1. Calculate the value of preferred and common stock:

*Number of shares* X *Par Value* = *Value of Preferred Stock*

*Number of shares* X *Par Value* = *Value of Common Stock*

2. Calculate the amount of dividends for the current year to be paid to preferred & common shareholders.

CompuForm declares an annual dividend of \$24,000.

*Value of Preferred Stock - \$100,000*

*Value of Common Stock - \$320,000*

*Val. of Pref. Stock* X *Pref. Div. Rate* = *Pref. Div. Amount*

\$100,000

8%

\$8,000

*Total amnt. Avail. For Div.*

*Pref. Div. Amnt.*

= *Amnt. Avail. For*

*Common Div.*

\$24,000

\$8,000

\$16,000

# Work Together

1. Calculate the value of preferred and common stock:

$$\text{Number of shares} \times \text{Par Value} = \text{Value of Preferred Stock}$$

$$\text{Number of shares} \times \text{Par Value} = \text{Value of Common Stock}$$

2. Calculate the amount of dividends for the current year to be paid to preferred & common shareholders.

Eagle Express declares an annual dividend of \$

*Value of Preferred Stock - \$*

*Value of Common Stock - \$*

$$\text{Val. of Pref. Stock} \times \text{Pref. Div. Rate} = \text{Pref. Div. Amount}$$

$$\begin{array}{l} \text{Total amnt. Avail. For Div.} \\ \text{Amnt. Avail. For} \\ \text{Common Div.} \end{array} \quad \text{Pref. Div. Amnt.} =$$

