

A Corporation Issued 1,200 Shares Of Common Stock At \$10 Per Share. If The Stock Has A Par Value Of \$7

A Corporation Issued 1,200 Shares Of Common Stock At \$10 Per Share. If The Stock Has A Par Value Of \$7, understanding the nuances of stock issuance, par value, and related financial implications is essential for investors, accountants, and business owners alike. This article provides a comprehensive overview of what this scenario entails, covering key concepts such as common stock, par value, additional paid-in capital, and the overall impact on a corporation's financial statements.

Understanding the Basic Terms

What Is Common Stock?

Common stock represents ownership in a corporation. Shareholders of common stock typically have voting rights on corporate matters and may receive dividends, which are a portion of the company's profits. The issuance of common stock is a primary method for companies to raise capital.

What Is Par Value?

Par value (also known as face value) is a nominal value assigned to each share of stock in the corporate charter. It is a legal concept that establishes the minimum price at which shares can be issued and often bears little relation to the stock's market value. In this scenario, the stock has a par value of \$7 per share.

Stock Issuance at a Price Above Par

When a company issues stock at a price exceeding its par value, the excess amount is considered additional paid-in capital (also called share premium). This is a crucial accounting concept that impacts the company's equity section on the balance sheet.

Breakdown of the Stock Issuance

Details of the Transaction

- Number of Shares Issued: 1,200
- Issue Price Per Share: \$10
- Par Value Per Share: \$7

Calculating the Total Proceeds

Total proceeds from the issue are calculated as:

- $1,200 \text{ shares} \times \$10 \text{ per share} = \$12,000$

Determining the Par Value Portion

The total par value of all shares issued:

- $1,200 \text{ shares} \times \$7 \text{ par value} = \$8,400$

Calculating Additional Paid-in Capital

The amount received over the par value (also known as share premium) is:

- $\text{Total proceeds} - \text{Total par value} = \$12,000 - \$8,400 = \$3,600$

This \$3,600 is recorded as additional paid-in capital in the equity section of the balance sheet.

Accounting Entries for the Stock Issuance

When a company issues stock, proper journal entries are necessary to accurately reflect the transaction in the books.

Journal Entry Example

The typical journal entry would be:

Account	Debit (\$)	Credit (\$)
Cash	12,000	
Common Stock (at par value)		8,400
Additional Paid-in Capital		3,600

Explanation:

- Debit to Cash increases the company's cash assets.
- Credit to Common Stock reflects the total par value of shares issued.
- Credit to Additional Paid-in Capital captures the amount received above the par value.

Implications of the Stock Issuance

Impact on Shareholders' Equity

The issuance increases the company's total shareholders' equity by the total proceeds of \$12,000. This is divided into:

- Par value component: \$8,400
- Additional paid-in capital: \$3,600

Legal and Regulatory Considerations

- Many jurisdictions require that the par value be disclosed in the articles of incorporation.
- The par value is often set at a minimal amount to avoid legal issues related to issuing stock below certain thresholds.
- The excess over par value is considered a capital surplus, which is part of the company's contributed capital.

Market Perception and Stock Valuation

While the par value is largely a legal and accounting concept, the market value of the stock may be significantly higher or lower based on the company's performance, industry trends, and investor sentiment.

Why Par Value Matters

Historical Significance

Historically, par value served as a safeguard against the issuance of stock below a certain minimum price, protecting creditors and shareholders.

Modern Relevance

In contemporary accounting, par value holds less practical significance as stock is often issued at prices well above par. Many companies issue no-par stock, simplifying the accounting process.

Legal and Financial Implications

- Issuing stock below par value can lead to legal penalties.
- The par value influences the minimum legal capital, which can affect the company's ability to distribute dividends or repurchase shares.

Additional Considerations in Stock Issuance

Authorized vs. Issued Shares

- Authorized Shares: The maximum number of shares a corporation can issue, as specified in its articles of incorporation.
- Issued Shares: The shares actually sold or distributed to shareholders.

- In this scenario, 1,200 shares are issued, but the company may have authority for more shares.

Outstanding Shares

- Shares held by shareholders, excluding treasury stock (if any).
- The number of outstanding shares affects earnings per share (EPS) and voting rights.

Treasury Stock

- Shares that the company has repurchased and holds in its treasury.
- These do not confer voting rights or dividends until reissued.

Tax and Financial Reporting Implications

Tax Treatment

- The proceeds from issuing stock are generally not taxable income.
- However, the issuance may impact the company's capital structure and future tax liabilities.

Financial Statement Presentation

- The common stock account is presented in the shareholders' equity section.
- Additional paid-in capital is also part of shareholders' equity.
- The total increase in equity reflects the cash inflow from the stock issuance.

Conclusion

Issuing 1,200 shares of common stock at \$10 per share with a par value of \$7 involves several important accounting and legal considerations. The total proceeds of \$12,000 are split between the par value and additional paid-in capital, impacting the company's shareholders' equity structure. Understanding these concepts helps stakeholders evaluate the financial health of the company, its capital structure, and its potential for future growth.

By grasping the significance of par value, the mechanics of stock issuance, and the associated accounting entries, investors, business owners, and accountants can better navigate the complexities of corporate finance. Whether for raising capital, complying with regulations, or analyzing financial statements, these fundamentals serve as the foundation for sound financial management and strategic decision-making.

Frequently Asked Questions

What is the total amount of capital raised from issuing 1,200 shares at \$10 per share?

The total capital raised is $1,200 \text{ shares} \times \$10 = \$12,000$.

What is the total par value of the issued shares?

The total par value is $1,200 \text{ shares} \times \$7 = \$8,400$.

How much is recorded as additional paid-in capital in this transaction?

Additional paid-in capital is the difference between the total proceeds and total par value: $\$12,000 - \$8,400 = \$3,600$.

What journal entry would a company record for this stock issuance?

Debit Cash \$12,000; Credit Common Stock \$8,400; Credit Additional Paid-in Capital \$3,600.

Why is it important to know the par value when issuing common stock?

Par value helps determine the legal capital and the minimum amount that must be maintained per share, affecting accounting and legal considerations.

Additional Resources

A Corporation Issued 1,200 Shares Of Common Stock At \$10 Per Share. If The Stock Has A Par Value Of \$7

In the complex world of corporate finance, understanding the nuances of stock issuance is fundamental for investors, accountants, and business owners alike. When a corporation issues shares, several key details—such as the number of shares, their issue price, and par value—play a pivotal role in shaping the company's financial statements and legal responsibilities. Consider a scenario where a company issues 1,200 shares of common stock at a price of \$10 per share, with a par value of \$7. While this might seem straightforward at first glance, it involves intricate accounting principles and legal considerations that merit a comprehensive exploration.

This article delves into the mechanics behind such a stock issuance, dissecting the significance of par value, the accounting entries involved, the impact on shareholders' equity, and the broader financial implications for the corporation. By the end, readers will gain a clearer understanding of how these transactions are recorded and what they mean for the company's financial health.

Understanding the Key Terms: Common Stock, Par Value, and Issue Price

Common Stock: The Foundation of Ownership

Common stock represents ownership shares in a corporation, conferring voting rights and a residual claim on assets and earnings. When investors purchase common stock, they become partial owners and potentially participate in the company's growth through dividends and capital appreciation.

Par Value: The Legal Nominal Value

Par value (also known as face value) is a nominal value assigned to each share, often set at a minimal amount like \$0.01 or \$1.00, though it can vary. Legally, the par value establishes the minimum legal capital that must be maintained and can serve as a safeguard against issuing shares below a certain threshold.

In our scenario, the stock has a par value of \$7, meaning each share cannot be issued at a price below this amount legally, although in practice, companies often issue shares at prices above par.

Issue Price: The Market or Offering Price

The issue price is the actual price at which the shares are sold to investors—in this case, \$10 per share. When the issue price exceeds the par value, the difference is termed "additional paid-in capital" or "share premium."

Accounting for the Stock Issuance: Journal Entries and Financial Impact

Step 1: Calculating the Total Proceeds and the Par Value

- Number of shares issued: 1,200
- Issue price per share: \$10
- Total proceeds from issuance: $1,200 \text{ shares} \times \$10 = \$12,000$
- Par value per share: \$7
- Total par value: $1,200 \text{ shares} \times \$7 = \$8,400$

Step 2: Recognizing the Par Value and Additional Paid-in Capital

The proceeds are allocated between the par value (legal capital) and the amount exceeding it:

- Par value portion: \$8,400
- Excess over par (additional paid-in capital): $\$12,000 - \$8,400 = \$3,600$

Step 3: Recording the Journal Entry

The typical journal entry to record this stock issuance would be:

Debit:

- Cash: \$12,000

Credit:

- Common Stock (at par value): \$8,400

- Additional Paid-in Capital (share premium): \$3,600

This entry reflects that the company received \$12,000 in cash, with \$8,400 allocated to common stock at par value and \$3,600 as additional paid-in capital.

Accounting Journal Entry:

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Dr. Cash ..... \$12,000

Cr. Common Stock (1,200 shares × \$7) ..... \$8,400

Cr. Additional Paid-in Capital ..... \$3,600

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Legal and Financial Significance of the Par Value and Excess

The Role of Par Value in Corporate Law

While par value has historical significance—serving as a legal minimum to protect creditors—it has become largely symbolic in modern practice.

Nonetheless, issuing shares at a price below par value can lead to legal complications, such as accusations of issuing stock below legal capital, which could jeopardize the company's legal standing.

In this scenario, issuing at \$10 when the par value is \$7 ensures compliance, as the issue price exceeds the par value.

Implications of Excess Paid-in Capital

The difference between the issue price and the par value (\$3,600) is recorded in the "Additional Paid-in Capital" account, which is part of shareholders' equity. This account reflects the amount investors are willing to pay over the nominal value, often representing premium received for the company's growth prospects or brand value.

Impact on Shareholders' Equity:

- Increase in total shareholders' equity by \$12,000

- Composition:

- Common Stock: \$8,400

- Additional Paid-in Capital: \$3,600

This structure provides flexibility for the company to capitalize on favorable market conditions and signals strong investor confidence.

Broader Financial and Strategic Considerations

Impact on the Company's Financial Statements

- Balance Sheet: The cash account increases by \$12,000, while shareholders' equity increases correspondingly, with allocations to common stock and additional paid-in capital.
- Income Statement: No immediate effect, as stock issuance is a financing activity, not operational.

Implications for Future Financing and Stock Management

Issuing shares at a premium can bolster the company's capital reserves, enabling future expansion, debt reduction, or acquisitions. It also signals market confidence, potentially attracting more investors.

Legal and Regulatory Compliance

Companies must adhere to state laws governing par value and share issuance. Issuing stock below par value can lead to legal liabilities or the need to reissue or restate financials. Proper documentation and adherence to corporate bylaws are essential to avoid legal pitfalls.

Summary and Takeaways

Issuing 1,200 shares of common stock at \$10 per share with a par value of \$7 involves a series of accounting and legal considerations that are vital for transparent financial reporting and legal compliance. The transaction increases the company's cash and shareholders' equity, split between common stock at par value and additional paid-in capital, reflecting the premium investors are willing to pay above the legal minimum.

Key points to remember:

- The total proceeds from the issuance are \$12,000.
- The par value total is \$8,400, which is the legal minimum capital.
- The excess over par (\$3,600) is recorded as additional paid-in capital.
- Proper journal entries are essential for accurate financial reporting.
- The issuance strengthens the company's equity base, supporting future growth.

In conclusion, understanding the intricacies of stock issuance, especially the relationship between issue price, par value, and paid-in capital, is crucial for sound financial management and legal compliance. As markets evolve and companies seek to raise capital, mastering these accounting principles ensures transparency and reinforces investor confidence.

A Corporation Issued 1 200 Shares Of Common Stock At 10 Per Share If The Stock Has A Par Value Of 7

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