

# **Pick The Correct Statement Related To Stock Dividend From Below. Multiple Choicea Large Stock Dividend**

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Understanding stock dividends is fundamental for investors and financial professionals alike. As companies navigate their growth strategies and investor relations, they often resort to distributing profits in the form of dividends. Among these, stock dividends—especially large stock dividends—are a common mechanism to reward shareholders without disbursing cash. Grasping the nuances of stock dividends, including their implications, accounting treatment, and effects on share value, is crucial for making informed investment decisions.

This article aims to clarify the concept of stock dividends, with a focus on large stock dividends, and help you identify the correct statements related to them through multiple-choice questions. We will explore the definition, types, accounting treatment, and effects of large stock dividends, providing comprehensive insights to enhance your understanding.

## **What Is a Stock Dividend?**

A stock dividend refers to the distribution of additional shares of a company's stock to its shareholders instead of cash. When a company declares a stock dividend, shareholders receive a proportional number of additional shares based on their existing holdings. This is often expressed as a percentage—such as a 10% stock dividend—or in terms of the number of shares issued.

Key features of stock dividends:

- They increase the number of shares outstanding.
- They do not directly change the company's overall market capitalization.
- They are usually issued when the company wants to reward shareholders without affecting cash reserves.
- They can be classified as small or large stock dividends based on the percentage of shares issued.

# Types of Stock Dividends: Small vs. Large

Stock dividends are generally categorized into two types based on the percentage of shares issued relative to the existing shares:

## Small Stock Dividends

- Typically less than 20-25% of the existing shares.
- Usually recorded at market value.
- Accounts involve a debit to retained earnings and a credit to common stock and additional paid-in capital if applicable.
- The impact on per-share metrics is minimal.

## Large Stock Dividends

- Usually 25% or more of the existing shares.
- Recorded at par value or stated value.
- Accounts involve a debit to retained earnings and a credit to common stock at par value.
- Lead to a significant change in the number of shares outstanding.

This article primarily focuses on large stock dividends, which have distinct accounting treatments and implications compared to small stock dividends.

## Understanding Large Stock Dividends

Large stock dividends are issued in substantial proportions—generally 25% or more—of the existing shares outstanding. They are often used by companies to distribute profits in a way that preserves cash flow, reward shareholders, and signal financial strength.

Characteristics of large stock dividends include:

- They increase the total number of shares outstanding significantly.
- They are typically issued at par value or stated value.
- They reduce the retained earnings account proportionally.
- They do not alter the company's total assets or equity in terms of value but reallocate retained earnings into share capital.

## Accounting for Large Stock Dividends

The accounting treatment of large stock dividends involves specific journal entries, reflecting the transfer from retained earnings to share capital.

Basic journal entry:

- Debit: Retained Earnings
- Credit: Common Stock (at par or stated value)

Example:

Suppose a company declares a 25% stock dividend on 1,000,000 shares outstanding, with a par value of \$1 per share.

- Number of shares issued as dividend:  $25\% \times 1,000,000 = 250,000$  shares
- Total value transferred from retained earnings:  $250,000 \text{ shares} \times \$1 \text{ par} = \$250,000$

Journal entry:

| Account           | Debit     | Credit    |
|-------------------|-----------|-----------|
| Retained Earnings | \$250,000 |           |
| Common Stock      |           | \$250,000 |

This process reduces retained earnings by the total value of the stock dividend and increases share capital accordingly.

Impact on Financial Statements:

- Balance Sheet: No change in total assets or total liabilities; only equity accounts are affected.
- Retained Earnings: Decreases by the total value of the dividend.
- Share Capital: Increases by the total par value of the new shares issued.

## Implications of Large Stock Dividends on Shareholders and the Company

Understanding the effects of large stock dividends is crucial for investors and management. Here are some key implications:

### For Shareholders:

- Shareholders receive additional shares, which may dilute earnings per share (EPS) but maintain proportional ownership.
- The market price per share typically decreases proportionally to the stock dividend, reflecting the increased number of shares.
- Stock dividends are viewed as a non-cash distribution, signaling confidence but not providing immediate cash income.

## For the Company:

- Preserves cash while rewarding shareholders.
- Adjusts share structure without affecting total assets.
- May influence stock price and investor perception.

## Multiple Choice Questions on Large Stock Dividends

To test your understanding, here are some multiple-choice statements related to large stock dividends. Select the correct statement from the options provided.

Question 1:

A large stock dividend is generally declared when the dividend is more than what percentage of the existing shares?

- a) 10%
- b) 20%
- c) 25%
- d) 50%

Correct answer: c) 25%

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Question 2:

When a company declares a large stock dividend, what is the typical journal entry?

- a) Debit Cash; Credit Revenue
- b) Debit Retained Earnings; Credit Common Stock
- c) Debit Common Stock; Credit Retained Earnings
- d) Debit Paid-in Capital; Credit Cash

Correct answer: b) Debit Retained Earnings; Credit Common Stock

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Question 3:

Which of the following statements is true regarding the effect of large stock dividends on the company's total assets?

- a) Total assets increase
- b) Total assets decrease
- c) Total assets remain unchanged
- d) Total assets fluctuate unpredictably

Correct answer: c) Total assets remain unchanged

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Question 4:

Large stock dividends are usually issued at:

- a) Market value
- b) Par or stated value
- c) Book value
- d) Premium value

Correct answer: b) Par or stated value

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Question 5:

One of the primary reasons a company might issue a large stock dividend is to:

- a) Increase the company's cash reserves
- b) Reward shareholders without reducing cash
- c) Decrease the number of shares outstanding
- d) Improve short-term liquidity

Correct answer: b) Reward shareholders without reducing cash

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Question 6:

How does a large stock dividend affect earnings per share (EPS)?

- a) EPS increases
- b) EPS decreases proportionally
- c) EPS remains unchanged
- d) EPS becomes zero

Correct answer: b) EPS decreases proportionally

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## **Common Misconceptions About Large Stock Dividends**

Understanding what large stock dividends are and are not is vital to avoid misconceptions:

- Misconception 1: Large stock dividends increase the company's assets.

Correction: They do not; assets remain unchanged as the distribution is in shares, not cash.

- Misconception 2: Large stock dividends are taxable income for shareholders.  
Correction: Generally, stock dividends are not taxable until shares are sold.

- Misconception 3: Issuing large stock dividends dilutes the company's total value.

Correction: Total value remains the same; only the number of shares increases.

- Misconception 4: Large stock dividends are equivalent to cash dividends.  
Correction: They are different; cash dividends provide cash income, whereas stock dividends increase share count.

## Conclusion

Large stock dividends are a strategic tool used by companies to reward shareholders while conserving cash. They involve issuing a significant number of additional shares, typically at par value, and result in proportional adjustments to share capital and retained earnings. The accounting treatment is straightforward, involving transferring the dividend value from retained earnings to share capital, and the overall assets and liabilities of the company remain unaffected.

For investors, understanding the implications of large stock dividends—such as dilution of EPS and changes in share price—is essential for making informed investment decisions. Recognizing the correct statements related to stock dividends, especially large ones, enhances financial literacy and aids in analyzing a company's financial health and strategic direction.

By mastering these concepts and reviewing multiple-choice questions, you can confidently identify the accurate statements and deepen your understanding of stock dividends. Whether you're a student, investor, or financial professional, knowledge about large stock dividends equips you to interpret company actions accurately and plan your investment strategies effectively.

## Frequently Asked Questions

**What is a large stock dividend typically considered as?**

A stock dividend exceeding 25% of the existing shares outstanding.

## **How does a large stock dividend affect a company's earnings per share (EPS)?**

It generally decreases EPS because the number of shares outstanding increases significantly.

## **Which statement is correct regarding the distribution of a large stock dividend?**

It involves issuing additional shares to shareholders instead of cash, diluting the share value.

## **Does a large stock dividend impact the company's total equity? If so, how?**

No, it does not impact total equity; it merely redistributes equity from retained earnings to share capital.

## **What is a common reason a company might issue a large stock dividend?**

To distribute accumulated earnings to shareholders without reducing cash reserves.

## **How is a large stock dividend reported in the financial statements?**

It is recorded by transferring an amount from retained earnings to share capital and share premium.

## **Which statement best describes the impact of a large stock dividend on the company's market price per share?**

The market price per share usually decreases proportionally to the dividend issued.

## **Is a large stock dividend considered a taxable event for shareholders?**

Generally, no, as it is a non-cash distribution of additional shares, but tax laws may vary by jurisdiction.

# How does issuing a large stock dividend differ from issuing a small stock dividend?

A large stock dividend (over 25%) significantly increases the number of shares outstanding and often affects per-share metrics more noticeably than a small dividend.

## Additional Resources

Understanding Stock Dividends: A Comprehensive Review

Stock dividends are a significant aspect of corporate financial strategies and investor relations. They influence a company's share structure, investor perceptions, and overall market valuation. Among the various types of stock dividends, large stock dividends are particularly noteworthy due to their unique implications and accounting treatments. This review delves deep into the concept of stock dividends, focusing specifically on the statement related to large stock dividends, and aims to clarify common misconceptions while providing a thorough understanding of the subject.

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## What Is a Stock Dividend?

A stock dividend is a dividend payment made by a corporation to its shareholders in the form of additional shares rather than cash. When a company declares a stock dividend, existing shareholders receive additional shares proportional to their current holdings, effectively increasing the number of shares they own.

Key Features of Stock Dividends:

- **Distribution in Shares:** Unlike cash dividends, stock dividends are paid in the form of additional shares.
- **No Immediate Cash Outflow:** The company's cash reserves are unaffected, as no cash is paid to shareholders.
- **Dilution of Equity:** Since the total number of shares increases, each share's proportional ownership might decrease unless adjusted.
- **Impact on Share Price:** Typically, the market adjusts the share price downward to reflect the increased number of shares outstanding.

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# Types of Stock Dividends

Stock dividends are categorized based on their size and the impact they have on the company's share structure.

## Small Stock Dividends

- Usually less than 25% of the existing shares.
- Treated similar to a stock split.
- The market value per share remains relatively stable.

## Large Stock Dividends

- Typically 25% or more of the existing shares.
- Often considered a distribution of earnings in the form of a significant increase in share capital.
- They are distinguished by their accounting treatment and the way they impact the company's financial statements.

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# Large Stock Dividends: Key Characteristics and Accounting Treatment

A large stock dividend involves issuing a substantial number of additional shares to shareholders, often equal to or exceeding 25% of the existing shares. This type of dividend has specific implications.

## Significance of Large Stock Dividends

- Distribution of Retained Earnings: Large stock dividends are generally viewed as a way for companies to distribute accumulated earnings without paying cash.
- Adjustment of Share Capital: They result in a significant increase in the number of outstanding shares.
- Reflects Company's Earnings: Usually declared when a company prefers to conserve cash but still wishes to reward shareholders.

## Accounting Treatment

The accounting for large stock dividends involves specific steps:

- Transfer from Retained Earnings to Share Capital: The total value of the dividend is transferred from retained earnings to share capital (and possibly share premium if applicable).
- No Impact on Total Assets or Equity: The total assets and total equity of the company remain unchanged; only the composition shifts.

- Measurement at Par or Market Value: The value assigned to the dividend is typically based on the par value of shares issued; sometimes, market value might be considered, but standard practice favors par value.

Example:

Suppose a company declares a 50% stock dividend on 1,000,000 shares outstanding with a par value of \$1 per share.

- Shares to be issued: 50% of 1,000,000 = 500,000 shares.
- Value transferred from retained earnings: 500,000 shares x \$1 par = \$500,000.
- Journal Entry:
  - Debit Retained Earnings: \$500,000
  - Credit Share Capital: \$500,000

This process increases the share capital and decreases retained earnings, with no effect on total assets or total equity.

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## **Implications of Large Stock Dividends for Shareholders and the Company**

Understanding the impact of large stock dividends is crucial for both management and investors.

For Shareholders:

- Dilution of Earnings Per Share (EPS): Since the number of shares increases significantly, EPS tends to decrease.
- No Immediate Cash Benefit: Shareholders do not receive cash, which might be less attractive during cash shortages.
- Potential Signal of Caution: Large stock dividends may sometimes indicate that the company prefers to conserve cash or is unable to pay cash dividends.

For the Company:

- Conservation of Cash: It allows the company to reward shareholders while preserving cash reserves.
- Enhancement of Share Liquidity: Increased number of shares can improve liquidity.
- Market Perception: Depending on context, large stock dividends can be perceived positively (as a sign of confidence) or negatively (as a sign of financial distress).

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# Common Statements Related to Large Stock Dividends

When reviewing multiple-choice questions or statements about stock dividends, certain key points are often emphasized. Here are some statements, with explanations on their correctness:

1. "A large stock dividend results in a transfer from retained earnings to share capital."  
- Correct. This is the fundamental accounting treatment for large stock dividends. It reflects the distribution of earnings in the form of additional shares.
2. "Large stock dividends increase the company's total assets."  
- Incorrect. Since stock dividends involve only reallocation within equity accounts, total assets remain unchanged.
3. "A large stock dividend decreases total shareholders' equity."  
- Incorrect. Total shareholders' equity remains the same; only its composition changes.
4. "Large stock dividends are distributed when a company wants to conserve cash but still provide value to shareholders."  
- Correct. This is a common motive, especially when cash dividends are not feasible.
5. "Stock dividends are always classified as income."  
- Incorrect. Stock dividends are not considered income; they are distributions of retained earnings and do not affect net income.
6. "The market price per share after a large stock dividend generally remains the same."  
- Incorrect. Typically, the market adjusts the share price downward proportionally to the increase in the number of shares issued, assuming no other changes.

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## Common Misconceptions and Clarifications

Misunderstandings regarding stock dividends, especially large ones, are common. Clarifying these can prevent misconceptions.

| Misconception   Clarification                           |                                                                                              |
|---------------------------------------------------------|----------------------------------------------------------------------------------------------|
| ----- -----                                             |                                                                                              |
| Large stock dividends increase the company's net worth. | Incorrect. They do not affect total assets or net worth; they only change the composition of |

equity. |

| Stock dividends are equivalent to stock splits. | Partially correct. They are similar but differ in purpose and accounting; stock splits do not involve transferring amounts from retained earnings. |

| Large stock dividends are taxable income. | Incorrect. Generally, stock dividends are not taxable until shares are sold. |

| Declaring a large stock dividend boosts the company's cash flow. |

Incorrect. No cash inflow occurs; it's a reallocation within equity accounts.

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## Conclusion: Picking the Correct Statement

When evaluating multiple-choice statements related to stock dividends, especially large stock dividends, the correct understanding hinges on recognizing their accounting treatment, impact on financial statements, and implications for shareholders.

The most accurate statement among common options is:

> "A large stock dividend results in a transfer from retained earnings to share capital."

This statement correctly captures the fundamental accounting process involved. It encapsulates the essence of large stock dividends—distribution of earnings in the form of additional shares, leading to an increase in share capital and a corresponding decrease in retained earnings, with no change in total assets or liabilities.

In summary:

- Large stock dividends are a method for companies to reward shareholders without using cash.
- They involve specific accounting entries, primarily transferring amounts from retained earnings to share capital.
- They do not alter total assets, total liabilities, or total shareholders' equity.
- The statement that they result in a transfer from retained earnings to share capital is a key, correct principle that accurately reflects their nature.

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Final thoughts:

Understanding stock dividends, especially large stock dividends, is vital for accurate financial analysis and sound investment decision-making. Recognizing the correct statements helps investors interpret a company's financial health

and management's strategic choices. Always remember that while stock dividends change the number of shares and the composition of equity, they do not affect the company's total value or cash position, which is a fundamental aspect of sound financial knowledge.

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