basic education

Department:
Basic Education
REPUBLIC OF SOUTH AFRICA

ACCOUNTING

NO PAR VALUE SHARES AND BUYBACK OF SHARES GRADE 12

NO PAR VALUE SHARES AND BUYBACK OF SHARES

CAPS GRADE 12

TERM 1: WEEKS 1 – 2:

1. Companies

A company is a legal entity, separate and distinct from its individual owners, created under the laws of a state, i.e. in terms of company Act 71 of 2008. As a result, the company has an unlimited life, owners have limited legal liability, and ownership interests (shares) of some companies (Public Companies (Limited- Ltd) and State-owned Companies (SOC Ltd) are easily transferable. The purpose of the company and the rights and powers granted by the state to the company to engage in certain legal activities and business transactions related to those activities are stipulated in a written contract called the Memorandum of Incorporation (MOI). Companies may be classified as:

1. Categories of Profit Companies
   - Private Companies: to be reflected as Proprietary Limited or (Pty) Ltd
   - Personal Liability Companies: to be reflected as Incorporated or Inc
   - Public Companies: to be reflected as Limited or Ltd
   - State-owned Companies: to be reflected as SOC Ltd
2. Non-profit companies: to be reflected as "NPC"

2. Shareholders

The individual owners are called shareholders whose ownership in the company is evidenced by a share certificate. Each shareholder has various shareholders' rights that include:

1. the right to share in profits when a dividend is declared,
2. the right to elect directors and to establish corporate policies,
3. the preemptive right to maintain a proportionate interest in the ownership of the company by purchasing a proportionate share of additional share capital, if such share is issued, and
4. the right to share in the distribution of the assets of the company if it is liquidated. Ordinary share has all of these rights; preferred share does not, but has certain other privileges.

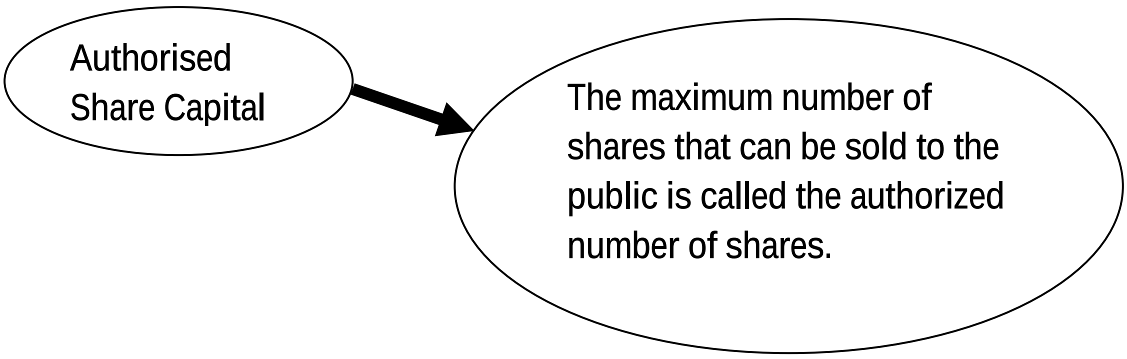
3. Equity

Equity is defined as the residual interest in the assets of a company that remains after deducting its liabilities. In other words, equity is the ownership interest in the company and may be calculated as the difference between assets and liabilities. Equity in a company is first created by owners' investments in the company. Subsequently, the value of the equity is changed by net income (loss), additional investments by owners, and distributions to owners.

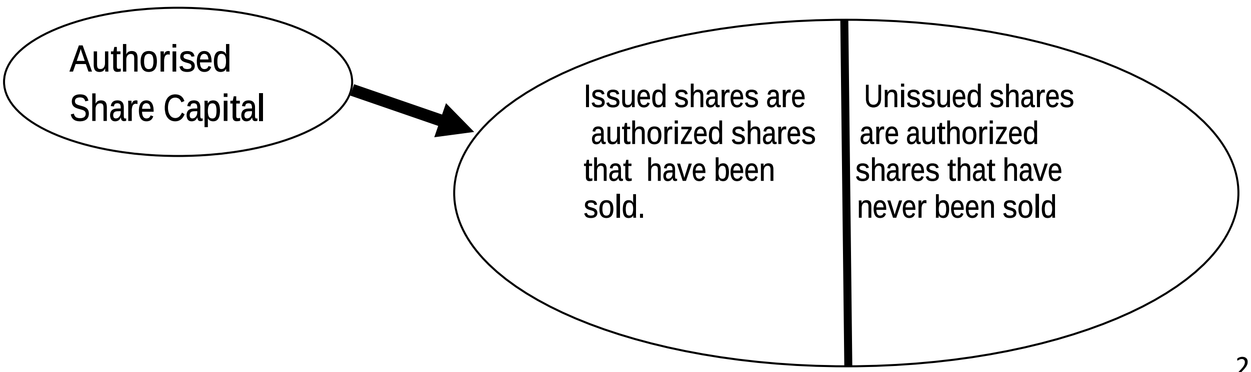
4. Company Capital Structure

Authorized share capital

Authorized share capital is the number of shares of capital stock that may be issued as stated in the company MOI. The maximum number of shares that can be sold to the public is called the authorized number of shares.



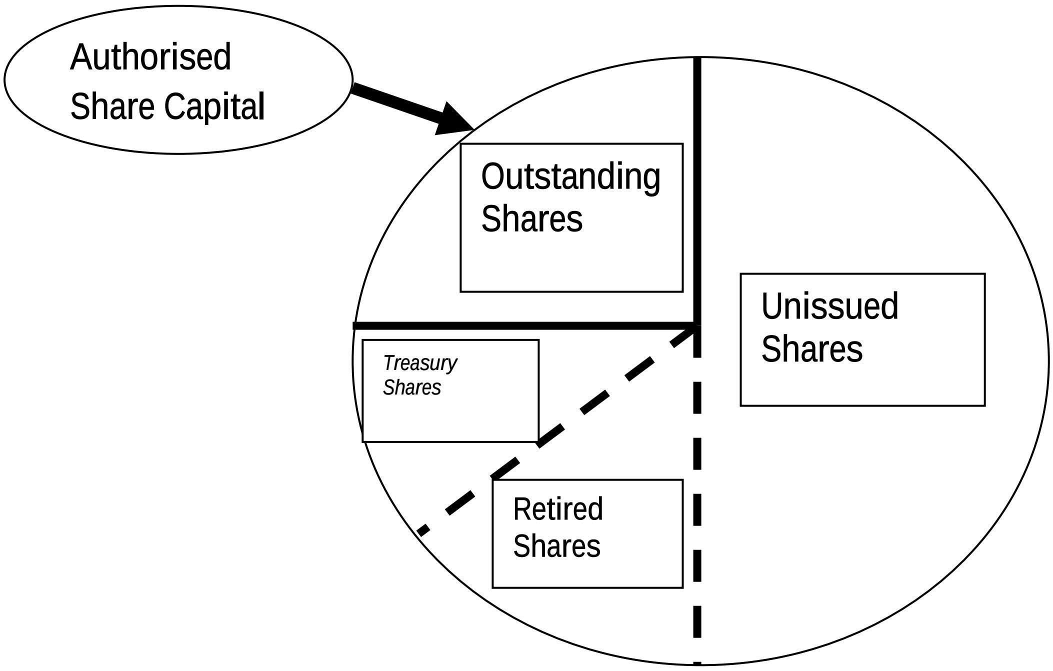
Issued share capital is the number of shares actually issued as of a specific date, i.e. the aggregate number of shares sold to the public. Not all authorized shares are always issued.



Outstanding share capital is the number of shares issued to shareholders that are still being held by them. Shares in the hands of shareholders - Equal to issued shares less retired shares or treasury share

Treasury share is the number of shares of share capital that were issued to shareholders and were later reacquired by the company but not retired. Issued shares less outstanding shares equals treasury share.

Retired share is the number of shares that a company has issued to shareholders and that has subsequently been repurchased by the company and retired or cancelled. *Note, When a company retires its reacquired shares, those shares assume the same status as authorized but unissued shares, just as if they had never been issued. Refer to section 35 of the Act 71 of 2008.*

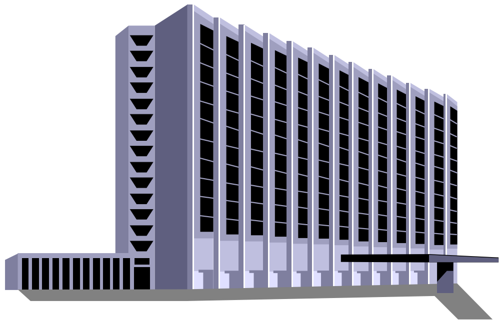


According to section 35 of the Act 71 of 2008 when a company retires its reacquired shares, those shares assume the same status as authorized but unissued shares, just as if they had never been issued. According to the Act, reacquired shares are generally retired and cancelled. *Note, the Accounting for retired shares is prescribed for Grade 12 syllabus.*

In certain restricted circumstances - South African treasury shares are those bought by subsidiaries and trusts (trust not a legal entity), and these shares are not retired, but are held as treasury shares for later reissue. *Note, Accounting for Subsidiaries are not prescribed by CAPS, hence we are only dealing with RETIRED SHARES.*

5. Stockholders' Equity

Sources or components of Shareholders' Equity



Amounts invested by shareholders

Amounts earned by the company

SHAREHOLDERS' EQUITY

1. Contributed Capital / Paid in capital

2. Retained Earnings

3. Accumulated Other Comprehensive Income

Other gains and losses not included in net income

The shareholders' equity is a portion of the balance sheet that discloses the company's capital structure in three sections:

1. Contributed Capital, the total amount invested by stockholders as a result of all company share transactions,
2. Retained Earnings, company net income reinvested in the company, and
3. Accumulated Other Comprehensive Income. Other gains not included in net income.

Note: The basic framework of this shareholders' equity section is as follows:

Shareholders' Equity

Contributed capital Ordinary Share Capital	XXX
Earned capital Retained Income	XXX
Accumulated other comprehensive income	XXX
Total shareholders' equity	RXXX

6. Definitions

What is a Capital Contribution / Paid-in Capital?

A capital contribution is an owner's contribution of assets (usually cash) into a business. When you start a business, you will have to put in money to get it going. This money is your capital contribution. You might also contribute other assets, like a computer, some equipment, or a vehicle that will be owned by the business. This is the portion of shareholders' equity contributed by investors through the issuance of shares.

What is Stated Capital

Amount of capital contributed by shareholders of a company. It is a component of the contributed capital and refers to the actual value of the shares issued. It may also refer to the method of valuating no-par-value shares where the portion of the amount contributed is credited to the share capital account and the balance is credited to contributed capital / paid-in capital.

Issuance of Share Capital

When only one class of share capital is issued, it is called ordinary share. Although most share capital is ordinary share, transactions involving different classes of shares are all recorded in a similar manner with different names.

The authorization to issue share capital of **"no-par value"** is made in the form of a cash journal entry. When the share is issued for cash, Bank is debited, the share capital account (e.g., Ordinary Share) is credited with the entire proceeds.

NO PAR VALUE SHARES

7. The Companies Act 71 of 2008

Section 35 of the Act – Legal nature of company shares and requirement to have shareholders

- According to the Act, a share does NOT have a nominal / par value, i.e. "No-par value shares" are issued.
  - Par value shares in existence retain description and rights attached
  - These shares are to be "converted" into no par value shares, but the process still to be confirmed (S35 par 6).
- A company may NOT issue shares to itself
- Authorized shares have no value until issued
- Shares bought back / surrendered to the company are deemed to be authorized but not issued

No par value shares Section 35 of the Act:

- Shares are most commonly issued for cash. When no par value ordinary shares are issued, the entire proceeds from the issue become share capital. The entire proceeds are credited to Ordinary Share Capital.
- No par value shares are not assigned a nominal value on foundation of the company and are issued at NO premium.
- No assigned legal capital value
- Share capital equals issue price (proceeds)
- Must retain share capital (legal capital).
- No-par value has NO relationship to market value once issued.

Example 1

On 30 January 2014 5 000 ordinary shares with No par value of R20 were issued and allotted.

Required:

Prepare the journal entries to record the share issue by Brandon Enterprises Ltd.

Solution

Date		Details	Ref	Debit	Credit
2014 Jan	30	Bank		R100 000	
		Ordinary share Capital			R100 000

Note: When no par value ordinary shares are issued, the **entire proceeds** from the issue become **stated capital.** The entire proceeds are credited to Share Capital – ordinary.

Examples 2

1. Aloe Company Ltd issues 6 000 ordinary shares for R144 000 cash on 20 February. The shares have NO PAR VALUE (neither par nor stated value).

   Required:

   Prepare journal entries and ledger to record this event.

Solution

Bank	R144 000	
Ordinary shares Capital		R144 000
Issued ordinary shares for cash		

Dr ORDINARY SHARE CAPITAL Cr

Feb	20	Balance	c/d	R144 000	Feb	20	Bank		R144 000

Dr BANK Cr

Feb	20	Ordinary share capital		R144 000	Feb	20	Balance	c/d	R144 000

Example 3

On Feb 23 AB Company issues 100 000 ordinary shares for R10 per share: the proceeds from the issuance of ordinary shares are R1 000 000.

Required:

Prepare a journal entry and ledger account for the company.

Details	Debit	Credit
Bank	1 000 000	
Ordinary Shares Capital		1 000 000

Dr ORDINARY SHARE CAPITAL Cr

Feb	23	Balance	c/d	1 000 000	Feb	23	Bank		1 000 000

Dr BANK Cr

Feb	23	Ordinary share capital		1 000 000	Feb	23	Balance	c/d	1 000 000

Example 4

A.

Goode Company Ltd issued 4 000 shares of no par value ordinary shares on 1 April 20014 for R45 000 cash

Required:

1. Calculate the average price per share issued
2. Prepare the journal entry of Goode Company Ltd.

Solution:

1.

Average price per share issued / the number of shares = average price per share
R48 000 / 4000 = R12

2.

Date	Details	RF	Debit	Credit
1 April	Bank		48 000	
	Ordinary share capital			48 000

B.

ABC Company Ltd issues 10 000 ordinary shares no par value and received cash of R75 000.

Required:

1. Calculate the average book value per share
2. Prepare the journal entry of ABC Ltd.

Solution

1.

Average book value per share / the number of shares = average price per share
= R750 000 / 10 000 = R75

2.

Date	Details	RF	Debit	Credit
	Bank		R750 000	
	Ordinary share capital			R750 000

SHARE BUYBACK (REPURCHASE / RE-ACQUISITION)

8. Definition of Buyback of shares

A buyback of shares, also known as a "share repurchase", is a company's buying back its own shares from the marketplace. You can think of a buyback as *a company investing in itself*, or using its cash to buy its own shares.

Reacquired shares are a company's own shares that have been issued, fully paid for, and then reacquired by the company.

9. Why would a company choose to reacquire its shares?

Companies will buy back shares:

- Reacquired shares are a company's own shares that have been issued, fully paid for, and then reacquired by the company.
- Reacquired shares are generally retired and cancelled.
- In certain restricted circumstances (SA treasury shares are those bought by subsidiaries and Trusts), these shares are not retired, but are held as treasury shares for later reissue.
- Companies repurchase shares because they:
    - Want to retire the stock(shares)
    - Think the shares are undervalued by the market
    - Want to change the proportion of debt to equity in the company
- Repurchased shares also increases Earnings Per Share (EPS)

10. Accounting treatment when a company buys its own shares: (STEPS)

- The company must calculate the average book value or cost of the shares being repurchased
- The share capital account for the shares must be reduced by the book value of the shares reacquired.
- Any difference between the cash paid to reacquire the shares and the book value of the shares CANNOT ever be reported as a gain or loss on the Income Statement. According to SA GAAP, AC 416 / Standing Interpretation Committee (SIC 16) / International Accounting Standard: IAS 32(AC 125). The effect of these rules is to ensure that a corporation records no income effect (i.e. no gain or loss on the income statement) on buying back its own shares
- If the buyback cost is lower than the average price per share issued to date, Contributed Capital / paid-in capital is created and the cost should be charged:

- to share capital at the average price per issued share
- any remaining amount to contributed capital

- If the buyback cost is **higher** than the average price per share issued to date, Contributed Capital is reduced, if it exists and the cost should be charged in this sequence:
  - to **share capital** at the average price per issued share
  - to any **contributed capital** that was created by earlier transactions in the shares
  - any remaining amount to **retained income**

Summary:

1. The corporation may repurchase shares of its outstanding share capital.
2. Shares may then be retired or cancelled.
3. No gain is ever reported on a share repurchase; however, Contributed Capital from the buy-back and retirement of Ordinary Shares may remain if shares are retired for less than the average issue price.
4. Contributed Capital from the buy-back and retirement of Ordinary Shares is **reported as a separate line in the contributed capital section of shareholders' equity.**
5. When shares are retired for more than the average issue price, Retained Earnings is debited for the excess paid over the issue price.
6. IF THERE IS A BALANCE IN CONTRIBUTED CAPITAL FROM THE BUY-BACK (RETIREMENT) OF ORDINARY SHARES, THIS ACCOUNT IS DEBITED FIRST TO THE EXTENT OF ITS BALANCE.

An extract from the Balance Sheet XYZ Company Limited 28 February 2012			
Shareholders' Equity			
Authorized Ordinary shares Capital			
Ordinary share capital (issued and outstanding)		xxx	
Contributed capital – (*buyback of shares and retired*)		xxx	
Total Contributed capital		xxx	
Retained earnings		xxx	
Total shareholders' equity		xxx	

Example 1:

In December 2013 Cooke Ltd. Sold 11 000 shares. The company repurchased and retired 500 shares at R8 per share. There were 11 000 shares issued and outstanding, with total share capital of R88 000.

Date	Details	Ref.	Debit	Credit
Jan. 10	Ordinary Share Capital		R4 000	
	Bank			R4 000

Dr ORDINARY SHARE CAPITAL B Cr

2011 Dec	31	Bank		4 000	2013 Dec	31	Balance	b/d	xxxxxx

Dr BANK ACCOUNT B Cr

2011 Jan	01	Balance	b/d	xxxxxx	2013 Dec	31	Ord. share capital		4 000

Example 2

In January 2014, Cooke Ltd. repurchased and retired 500 shares at R5 per share. There were 10 500 shares issued and outstanding, with total share capital of R84 000

Solution

- Acquisition cost = per share price/cost = R5.00
- Assigned share value = R84 000/10 500 = R8.00

Value below assigned value (R3.00)

Date	Details	Ref.	Debit	Credit
	Ordinary Shares Capital		R4 000	
	Contributed Capital			R1 500
	Bank			R2 500

(500 @ R8.00 [R84 000/10 500] = R4 000)

(500 @ R3.0 = R1 500)

(500 shares@ R5.00 = R2 500)

Dr ORDINARY SHARE CAPITAL B Cr

2012 Dec	31	Bank		4 000	2014 Jan	01	Balance	b/d	xxxxxx

Dr CONTRIBUTED CAPITAL B Cr

					2014 Dec	31	Ord. share capital		1 500

Dr BANK ACCOUNT B Cr

2014 Jan	01	Balance	b/d	xxxx	2014 Dec	31	Ord share capital		2 500

Example 3

- In December 2014 Cooke Ltd. repurchased and retired 1 000 shares at R10 per share. There were 10 000 shares issued and outstanding, with total share capital of R80 000.

Solution

- Acquisition cost = per share price/cost = R10.00
- Assigned share value = R80 000/10 000 = R8.00
- Value over assigned value R2.00

Date	Details	Ref.	Debit	Credit
	Ordinary Shares Capital		R8 000	
	Contributed Capital		1 500	
	Retained Income		500	
	Bank			10 000

(1000 @ R8.00 [R80 000/10 000] = R8 000)

(1000 @ R2.00 = R2 000): 10 000-8 000-1 500 = 500.

(1000 shares@ R10.00 = R10 000)

GENERAL LEDGER OF FRESCO COMPANY

Dr ORDINARY SHARE CAPITAL B Cr

		Bank		8 000			Balance	c/d	8 000
				8 000					8 000

Dr CONTRIBUTED CAPITAL B Cr

		Bank		1 500			Balance	b/d	1 500

Dr RETAINED INCOME B Cr

		Bank		500			Balance	c/d	500
		Balance	b/d	500					

Dr BANK ACCOUNT B Cr

		Balance	c/d	10 000			Ord share capital		8 000
							Contr. Capital		1 500
							Retained Income		500
				10 000					10 000
							Balance	b/d	10 000

Self-Evaluation Exercises

Exercise 1

Item	Questions	Answer
Give the definition, explanation or the relevant concept.		
1.	Share that has not been assigned a value in the company MOI.	
2,	The amount of shares that a company is authorized to sell as indicated in its MOI	
3.	Shares that has been issued and is being held by shareholders.	
4.	The difference between ordinary shares issued (1200) and outstanding (1000) is equal to	
5.	Paid in Capital is sometimes called	
6.	Net income that is retained in the corporation for future use.	
7.	Occurs when a corporation repurchases and cancels its own shares.	
8.	If no-par stock is issued without a stated value, then	
State whether the following are True or False		
9.	A company can issue more shares than it is authorized in its MOI, if the board of directors approves of an increase in the number of authorized shares.	
10.	As soon as a company is authorized to issue shares, an accounting journal entry should be made recording the total value of the shares authorized.	
11.	Shares that are retired are the same as authorized and unissued shares.	
12.	Company purchases and retirements of shares are made at a company's discretion.	
13.	No-par value share must always have a stated value so it can be recorded properly.	

14.	The shareholders' equity section of the balance sheet may contain three elements, Contributed Capital, Accumulated Other Comprehensive Income, and Retained Earnings.	

Multiple choice

Choose the answer and write only the letter next to the question number

15. Retirement of shares:

a) Reduces the number of issued shares.

b) Is permissible under law if the interest of the shareholders is not jeopardized.

c) Is accounted for like treasury shares.

d) Reduces the number of issued shares and is permissible under law if the interest of the shareholders is not jeopardized.

e) All of these answers are correct.

16. Shares are reacquired by a company for all of the following reasons except:

Shares are reacquired by a company for all of the following reasons except:

(a) to maintain the market price of its shares.

(b) to increase the earnings per share.

(c) Reacquired shares are generally retired and cancelled.

(d) to reduce dividends to others and increase dividends to itself.

17. Athens, Ltd., has 9 000 ordinary shares outstanding of which the following data has been collected:

Ordinary shares, 20 000 shares	
authorized and 10 000 issued	R150 000
Retained earnings	25 000
Retired shares	11 500

The cost per share of the retired shares is:

a) R1.15.

b) R1.28.

c) R11.

d) R10.50.

e) None of these answers is correct.

18. A company purchased 30 000 shares of its own R20 no par ordinary shares for R35 per

	share, recording it at cost. What will be the effect on total shareholders' equity? a) Increase by R1 050 000 b) Decrease by R600 000 c) Decrease by R1 050 000 d) Increase by R600 000	
19.	Elton Manufacturing Corporation purchased 4 000 shares of its own previously issued R10 no par ordinary shares for R92 000. As a result of this event, a) Elton's Ordinary shares account decreased R40 000. b) Elton's total shareholders' equity decreased R92 000. c) Elton's Paid-in Capital in Excess of Par Value account decreased R52 000. d) All of the above.	

Exercise 2

A

Video Electronics Company is organized with 10 000 shares authorized without par value. On 3 May Video Electronics issues 500 shares for at R10 per share.

You are required to prepare the journal entry and ledger of Video Electronics Company

B

On 1 December a company received R30 000 for issuing 10 000 shares of common stock of R3 No par value. Pass the journal entry to record the issuance of shares and post to the ledger.

C

On 1 June, ABC International sells 1 000 shares of no par value shares to investors for R10 per share. It records the transaction in the journal and ledger.

D

The board of directors of Armadillo Industries authorizes the repurchase of 100 000 shares of its shares, which has a no par value. The company originally sold the shares for R12 each, or R1 200 000 in total. Armadillo pays R1 500 000 to repurchase the shares. Record the transaction in the journal entry.

E

Company XYZ currently has 2 million shares outstanding, and ordinary shares account balance of R4 million. The company decides to buy back a million shares.

The company repurchases 500 000 shares at a price of R1.50/share and later it buys back the remaining 500 000 shares for R2.75/share. You are required to prepare the journal entries of Company XYZ.

Exercise 3

Average Price per share = R12

May 1 repurchase 1 000 shares at R12

June 1 repurchase 500 shares at R11

July 5 repurchase 2 000 shares at R15

Required:

Prepare the journal entries to record the above share transactions.

Date	Detail	Dr	Cr

Date	Detail	Dr	Cr

Date	Detail	Dr	Cr

Exercise 4

The Norseman Company Ltd issued ordinary shares for R45. Two years later, on June 10, 1 000 shares were repurchased and retired at a cost of R40. Use the journal entry to record this transaction and post to the general ledger.

Date	Details	Ref.	Debit	Credit

Dr BANK ACCOUNT Cr

Dr ORDINARY SHARE CAPITAL Cr

Dr CONTRIBUTED CAPITAL Cr

Exercise 5

Blue Jean Company Ltd originally issued its ordinary shares at R25 per share.

1. Prepare a journal entry to record the purchase and retirement of 500 shares if Blue Jean Company Ltd paid R30 per share and post to the ledger. The company has a retained income balance of R60 000.

2. Prepare a journal entry to record the purchase and retirement of 500 shares if Blue Jean Corporation paid R20 per share and post to the ledger.

1.

Date	Details	Ref.	Debit	Credit

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

Dr ORDINARY SHARE CAPITAL Cr

Dr RETAINED INCOME Cr

2.

Date	Details	Ref.	Debit	Credit

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

Dr ORDINARY SHARE CAPITAL Cr

Dr CONTRIBUTED CAPITAL Cr

Exercise 6

Beta, Company Ltd had the following shareholders' equity as of December 31 of Year 1:

Ordinary shares, 1 000 000 shares authorized,	
200 000 shares issued	R2 400 000
Retained Income	1 600 000

The following transactions related to the company's shares took place during Year 2:

Aug. 1 Purchased and retired 6 000 shares at R13 per share.

Dec. 3 Purchased and retired 5 000 shares at R11 per share.

Prepare the journal entries to record the transactions and post to the ledger.

A

Date	Details	Ref.	Debit	Credit

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

Dr ORDINARY SHARE CAPITAL Cr

Dr RETAINED INCOME Cr

B

Date	Details	Ref.	Debit	Credit

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

Dr ORDINARY SHARE CAPITAL Cr

Dr CONTRIBUTED CAPITAL Cr

Exercise 7

Fresco Company has 200 000 **no-par** ordinary shares outstanding, and that there is R1 million in the ordinary share capital account, which yields an average issuance price per share of R5. The Company acquired and retired 10 000 shares for R4.25 per share. The shareholder who sold these shares back to Fresco Company had originally paid R4 per share.

Required:

Prepare the journal entries and Ledger accounts to record the share transactions of Fresco Company.

Answer sheet:

Workings:

Date	Details	Ref.	Debit	Credit

GENERAL LEDGER OF FRESCO COMPANY

Dr ORDINARY SHARE CAPITAL Cr

Dr CONTRIBUTED CAPITAL Cr

Dr BANK ACCOUNT Cr

Exercise 7 ... continues

Fresco company has 190 000 no par ordinary shares outstanding. There is R950 000 in the ordinary share capital account which yields an average issuance price per share of R5. The contributed capital account / paid-in capital from previous acquisition transactions of ordinary shares have a R7 500 credit balance. The company acquired and retired 10 000 shares at a price of R6.25 per share. The shareholder who sold these shares back to Fresco Company had originally paid R4 per share.

Required:

- Prepare journal entries and Ledger accounts to record the share transactions of Fresco Company.

ANSWER SHEET:

Date	Details	Ref.	Debit	Credit

GENERAL LEDGER ACCOUNTS

Dr ORDINARY SHARE CAPITAL Cr

Dr CONTRIBUTED CAPITAL Cr

Dr RETAINED INCOME Cr

Dr BANK ACCOUNT Cr

Date	Details	Ref.	Debit	Credit

Dr CONTRIBUTED CAPITAL Cr

Dr RETAINED INCOME Cr

Dr BANK ACCOUNT Cr

Exercise 8

Thomas Cook Company Limited reported the following information on its Balance Sheet as of December 31, 2011:

Ordinary shares of no par value, 200 000 issued…..……………………R1 800 000

During March 2012, Thomas Cook repurchased 2 000 ordinary shares at a total cost of R12 000.
During July 2012, Thomas Cook repurchased 1 000 ordinary shares at a total cost of R22 000.

Required:
Prepare the journal entries to record the share transactions on Thomas Cook's books during 2012.

ANSWER SHEET

Workings:

Date	Details	Dr	Cr

Workings:

Date	Details	Dr	Cr

Exercise 9

Cattrall Company Ltd is authorized to issue an unlimited number of **no par value** ordinary shares. On 1 February 2011, the general ledger contained the following:

Shareholders' equity accounts:	
Ordinary shares (78 000 shares issued)	R1 490 000
Contributed capital—reacquisition of ordinary shares	75 000
Retained earnings	1 000 000
Accumulated other comprehensive income	65 000

The following equity transactions occurred during the year ended 31January 2012:

Feb. 28	Issued 2 400 ordinary shares for	R150 000.
Apr. 12	Issued 200 000 ordinary shares for	R3.2 million.
May 25	Issued 5,000 ordinary shares in cash................................	R80 000
Sept. 12	Repurchased 75 000 ordinary shares for	R1 275 000.
2012		
Jan. 1	Paid dividend of R2.50 per share to ordinary shareholders	

Required:

a) Prepare the journal entries to record the share transactions of Cattrall Company Ltd's for the year ended 31 January 2012.

b) Post the journal entries to the ledger.

ANSWER SHEET

Date	Details	Ref.	Debit	Credit

Workings:

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

Dr ORDINARY SHARE CAPITAL Cr

Dr RETAINED INCOME Cr

Dr DIVIDENDS ACCOUNT Cr

Solutions

Exercise 1

Item	Questions	Answer
Definitions		
1.	Share that has not been assigned a value in the company MOI.	No-par value share
2,	The amount of shares that a company is authorized to sell as indicated in its MOI	Authorized shares
3.	Shares that has been issued and is being held by shareholders.	Outstanding shares
4.	The difference between ordinary shares issued (1200) and outstanding (1000) is equal to	Retired shares (200)
5.	Paid in Capital is sometimes called	Contributed capital
6.	Net income that is retained in the corporation for future use.	Retained Income
7.	Occurs when a corporation repurchases and cancels its own shares.	Cancelling of shares Or Retirement of shares
8.	If no-par stock is issued without a stated value, then	the entire proceeds are considered to be legal capital
True or False		
9.	A company can issue more shares than it is authorized in its MOI, if the board of directors approves of an increase in the number of authorized shares.	False The **authorised capital** of a company is the maximum amount of share capital that the company is authorised to issue (allocate) to shareholder.
10.	As soon as a company is authorized to issue shares, an accounting journal entry should be made recording the total value of the shares authorized.	False Authorised share capital in only stated in the MOI of the company. An accounting journal entry only comes when the shares are issued.
11.	Shares that are retired are the same as authorized and unissued shares.	True

<table>
<tr><td>12.</td><td>Company purchases and retirements of shares are made at a company's discretion.</td><td>False
Prescribed by the companies Act 71 of 2008.</td></tr>
<tr><td>13.</td><td>No-par value share must always have a stated value so it can be recorded properly.</td><td>False
There is no requirement for share to have a par or stated value.</td></tr>
<tr><td>14.</td><td>The shareholders' equity section of the balance sheet may contain three elements, Contributed Capital, Accumulated Other Comprehensive Income, and Retained Earnings.</td><td>True
The shareholders' equity section of the balance sheet will always contain a contributed capital section. If a company has retained earnings or any of the four items that comprise other comprehensive income, these two sections will also be included.</td></tr>
<tr><td colspan="3">Multiple choice</td></tr>
<tr><td>15.</td><td>Retirement of shares:
f) Reduces the number of issued shares.
a) Is permissible under law if the interest of the shareholders is not jeopardized.
b) Is accounted for like treasury shares.
c) Reduces the number of issued shares and is permissible under law if the interest of the shareholders is not jeopardized.
d) All of these answers are correct.</td><td>D</td></tr>
<tr><td>16.</td><td>Shares are reacquired by a company for all of the following reasons except:
Shares are reacquired by a company for all of the following reasons except:
(a) to maintain the market price of its shares.
(b) to increase the earnings per share.
(c) Reacquired shares are generally retired and cancelled.
(d) to reduce dividends to others and increase dividends to itself.</td><td>D</td></tr>
<tr><td>17.</td><td>Athens, Ltd., has 9 000 ordinary shares outstanding of which the following data has been collected:
<table>
<tr><td>Ordinary shares, 20 000 shares</td><td></td></tr>
<tr><td>authorized and 10 000 issued</td><td>R150 000</td></tr>
<tr><td>Retained earnings</td><td>25 000</td></tr>
<tr><td>Retired shares</td><td>11 500</td></tr>
</table></td><td>C</td></tr>
</table>

	The cost per share of the retired shares is: a) R1.15. b) R1.28. c) R11. d) R10.50. e) None of these answers is correct.	
18.	A company purchases 30 000 shares of its own R20 no par ordinary shares for R35 per share, recording it at cost. What will be the effect on total shareholders' equity? e) Increase by R1 050 000 a) Decrease by R600 000 b) Decrease by R1 050 000 c) Increase by R600 000	C
19.	Elton Manufacturing Corporation purchased 4 000 shares of its own previously issued R10 no par ordinary shares for R92 000. As a result of this event, a) Elton's Ordinary shares account decreased R40 000. b) Elton's total shareholders' equity decreased R92 000. c) Elton's Paid-in Capital in Excess of Par Value account decreased R52 000. d) All of the above.	B

Exercise 2

A

Video Electronics Company is organized with 10 000 shares authorized without par value. On 3 May Video Electronics issues 500 shares for at R10 per share.

You are required to prepare the journal entry and ledger of Video Electronics Company

Date	Details	Dr	Cr
May 03	Bank	5 000	
	Ordinary shares		5 000
	No par value shares issued		

Dr BANK ACCOUNT Cr

May	03	Ordinary shares		5 000					

Dr ORDINARY SHARE CAPITAL Cr

					May	03	Bank		5 000

B

On 1 December a company received R30 000 for issuing 10 000 shares of common stock of R3 No par value. Pass the journal entry to record the issuance of shares and post to the ledger.

Date	Details	Dr	Cr
Dec. 1	Bank	30 000	
	Ordinary Shares Capital		30 000
	No par value shares issued		

Dr BANK ACCOUNT Cr

Dec.	1	Ordinary Shares Capital		30 000					

Dr ORDINARY SHARE CAPITAL Cr

					Dec.	1	Bank		30 000

C

On 1June, ABC International sells 1 000 shares of no par value shares to investors for R10 per share. It records the transaction in the journal and ledger.

Date	Details	Dr	Cr
June 1	Bank	10 000	
	Ordinary Share Capital		10 000
	No par value shares issued		

Dr BANK ACCOUNT Cr

June	1	Ordinary Share Capital		10 000					

Dr ORDINARY SHARE CAPITAL Cr

					June	1	Bank		10 000

C

Company XYZ currently has 2 million shares outstanding, and ordinary shares account balance of R4 million. The company decides to buy back a million shares.

The company repurchases 500 000 shares at a price of R1.50/share and later it buys back the remaining 500 000 shares for R2.75/share. You are required to prepare the journal entries of Company XYZ.

Date	Details	Dr	Cr
June 1	Ordinary Share Capital	1 000 000	
	Contributed capital		250 000
	Bank		750 000
	No par value shares issued		

*The average price/share on the books is R2 (4 000 000/2 000 000) 500 000 x R2

**Since the purchase price is below the average price by R0.50 (R2 - R1.50). 500,000 x R0.50

D

The board of directors of Armadillo Industries authorizes the repurchase of 100 000 shares of its shares, which has a no par value. The company originally sold the shares for R12 each, or R1 200 000 in total. Armadillo pays R1 500 000 to repurchase the shares. Record the transaction in the journal entry.

Date	Details	Dr	Cr
	Ordinary Shares Capital	1 000 000	
	Contributed capital	250 000	
	Retained Income	125 000	
	Bank		1 375 000

Exercise 3

Average Price per share = R12

May 1 repurchase 1 000 shares at R12

June 1 repurchase 500 shares at R11

July 5 repurchase 2 000 shares at R15

Required:

Prepare the journal entries to record the above share transactions.

Date	Detail	Dr	Cr
May 1	Ordinary Share capital	12 000	
	Bank		12 000
	Purchased and retired 1 000 ordinary shares at R12 per share.		

Date	Detail	Dr	Cr
Jun. 1	Ordinary Share capital	6 000	
	Bank		5 500
	Contributed Capital		500
	Purchased and retired 500 ordinary shares at R11.00		

Date	Detail	Dr	Cr
Jul. 5	Ordinary share capital	24 000	
	Contributed Capital	500	
	Retained Earnings	5 500	
	Bank		30 000
	Purchased and retired 2 000 ordinary shares at R15.00		

Exercise 4

The Norseman Company Ltd issued ordinary shares for R45. Two years later, on June 10, 1 000 shares were repurchased and retired at a cost of R40. Present the general journal entry to record the June 10 transaction and post to he ledger.

Date	Details	Ref.	Debit	Credit
June 10	Ordinary Share Capital		45 000	
	Contributed capital			5 000
	Bank			40 000
	Retirement of ordinary shares bought at a R40			

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

					June	10	Ordinary Share Capital		40 000

Dr ORDINARY SHARE CAPITAL Cr

June	10	Bank		40 000			Balance	c/d	45 000
		Contributed capital		5 000					
				45 000					45 000
		Balance	b/d	45 000					

Dr CONTRIBUTED CAPITAL Cr

					June	10	Ordinary Share Capital		5 000

Exercise 5

Blue Jean Company Ltd originally issued its ordinary shares at R25 per share.

1. Prepare a journal entry to record the purchase and retirement of 500 shares if Blue Jean Company Ltd paid R30 per share. The company has a retained income balance of R60 000.

2. Prepare a journal entry to record the purchase and retirement of 500 shares if Blue Jean Corporation paid R20 per share and post to the ledger.

1

Date	Details	Ref.	Debit	Credit
	Ordinary share capital (500 x R25)		12 500	
	Retain Earnings		2 500	
	Bank (500 x R30)			15 000
	Purchase and retire 500 shares at R30			

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

									15 000

Dr ORDINARY SHARE CAPITAL Cr

		Bank		12 500					

Dr RETAINED INCOME Cr

		Bank		2 500					

2

Date	Details	Ref.	Debit	Credit
	Ordinary Share Capital		12 500	
	Contributed capital			2 500
	Bank			10 000
	Retirement of ordinary shares bought at R20			

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

							Ordinary Share Capital		10 000

Dr ORDINARY SHARE CAPITAL Cr

		Bank		10 000			Balance	c/d	12 500
		Contributed capital		2 500					
				12 500					12 500
		Balance	b/d	12 500					

Dr CONTRIBUTED CAPITAL Cr

							Ordinary Share Capital		2 500

Exercise 6

Beta, Company Ltd had the following shareholders' equity as of December 31 of Year 1:

Ordinary shares, 1 000 000 shares authorized,	
200 000 shares issued	R2 400 000
Retained Income	1 600 000

The following transactions related to the company's shares took place during Year 2:

Aug. 1 Purchased and retired 6 000 shares at R13 per share.

Dec. 3 Purchased and retired 5 000 shares at R11 per share.

Prepare the journal entries to record the transactions and post to the ledger.

August:

Date	Details	Ref.	Debit	Credit
	Ordinary share capital		72 000	
	Retain Income		6 000	
	Bank			78 000
	Purchase and retire 6 000 shares at R13			

Workings:

6 000 x R13 = R78 000

6 000 x R12 = R72 000

Retain income R6 000

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

Aug.	31	Balance	c/d	78 000	Aug.	1	Ordinary share capital		72 000
							Retain Income		6 000
				78 000					78 000
					Sept.	1	Balance	b/d	

Dr ORDINARY SHARE CAPITAL Cr

Aug.	1	Bank		72 000					

Dr RETAINED INCOME Cr

Aug.	1	Bank		6 000					

December

Date	Details	Ref.	Debit	Credit
Dec. 3	Ordinary Share Capital		60 000	
	Contributed Capital			55 000
	Bank			5 000
	Retirement of ordinary shares bought at R11			

Workings:

5 000 x R12 = R60 000

5 000 x R11 = R55 000

Bank R5 000

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

					Dec.	3	Ordinary Share Capital		5 000

Dr ORDINARY SHARE CAPITAL Cr

Dec.	3	Bank		5 000	Dec.	31	Balance	c/d	60 000
		Contributed Capital		55 000					
				60 000					60 000
Jan.	1	Balance	b/b	60 000					

Dr CONTRIBUTED CAPITAL Cr

					Dec.	3	Ordinary Share Capital		55 000

Exercise 7

Workings:

Book value of outstanding Ordinary Shares {R1 000 000 / R200 000 = R5} X 10 000 shares = R50 000

Cost of shares buy back (10 000 X R4.25) = R42 500

Contributed capital, ordinary share required (R50 000 - R42 500) = R7 500

Date	Details	Ref.	Debit	Credit
Jan. 10	Dr. Ordinary Share Capital		R50 000	
	Cr. Contributed Capital			R 7 500
	Cr. Bank			R42 500

GENERAL LEDGER OF FRESCO COMPANY

Dr ORDINARY SHARE CAPITAL Cr

		Contr. capital		7 500					
		Bank		42 500					
				50 000					

Dr CONTRIBUTED CAPITAL Cr

							Ord share capital		7 500
									7 500

Dr BANK ACCOUNT Cr

		Balance	b/d	xxxxx			Ord share capital		42 500
							Balance	c/d	Xxxxx
		Balance	b/d	xxxxx					

Exercise 7 - cont.

Book value of outstanding ordinary shares {R950 000 / 190 000 = R5} X 10 000 shares = R50 000

Cost of shares buy back (10 000 X R6.25) = R62 500

Excess of cost over book value R62 500 - R50 000 = R12 500

Contributed Capital = R 7 500

Retained earnings (R62 500 - R50 000 - R7 500) = R 5 000

Date	Details	Ref.	Debit	Credit
Jan. 10	Ordinary Shares Capital		R50 000	
	Contributed Capital		7 500	
	Retained income		5 000	
	Bank			R62 500

GENERAL LEDGER OF FRESCO COMPANY

Dr ORDINARY SHARE CAPITAL Cr

		Bank		50 000			Balance	b/d	xxxxxx

Dr CONTRIBUTED CAPITAL Cr

		Bank		7 500			Balance	b/d	7 500

Dr RETAINED INCOME Cr

		Bank		5 000			Balance		xxxxx
		Balance	c/d	xxx					
				xxxxx					xxxxx
									xxx

Dr BANK ACCOUNT Cr

		Balance	b/d	xxxx			Ord share capital		50 000
							Contr. Capital		7 500
							Retained Income		5 000
							Balance	c/d	xxx

Note:

- The first step in constructing this journal entry is to compare the cost to acquire the shares (R62 500) with the average initial issuance price to date (R50 000). The specific issue price of these shares **(R4) is irrelevant**. The company **paid R12 500 more** to acquire these shares than the average original proceeds. Part of the R12 500 (R7 500) is debited first to **contributed or paid-in capital** from prior share acquisitions until that account is exhausted.

- This account may never have a debit balance. Retained income is debited for the balance. The effect of this transaction is to reduce paid-in capital by R57 500, retained earnings by R5 000 and total shareholders' equity by R62 500. Assets are reduced by R62 500.

Date	Details	Ref.	Debit	Credit
Jan. 10	Dr. Contributed Capital		7 500	
	Dr. Retained income		5 000	
	Cr. Bank			R12 500

GENERAL LEDGER ACCOUNTS

Dr CONTRIBUTED CAPITAL Cr

		Bank		7 500			Balance	b/d	7 500

Dr RETAINED INCOME Cr

		Bank		5 000			Balance	b/d	xxxxx

Dr BANK ACCOUNT Cr

		Balance	b/d	xxxx			Contrib. capital		7 500
							Retain. Income		5 000

Exercise 8

Ordinary Share Capital

| 1 800 000

total book value $\underline{1\ 800\ 000}$
total # of shares 200 000

book value/share = R9

March share repurchase

Book value of shares reacquired R9 x 2 000 = R18 000

Cost to reacquire shares $\underline{12\ 000}$

Contributed Capital 6 000

Details		Dr	Cr
Ordinary shares Capital	Dr	R18 000	
Bank	Cr		R12 000
Contributed Capital	Cr		6 000

Note: Contributed capital has a credit balance of R6 000

ORDINARY SHARE CAPITAL

18 000	1 800 000
	1 782 000

total book value 1 782 000

total # of shares 198 000

book value/share = R9

July share repurchase

Book value of shares reacquired R9 x 1,000 =	R 9 000
Cost to reacquire shares	22 000
Excess of cost over book value	13 000
decrease to Contributed Capital	6 000
decrease to Retained Income	7 000

Details	Dr	Cr
Ordinary share Capital	R 9 000	
Contributed capital	6 000	
Retained Income	7 000	
Bank		R22 000

Details	Dr	Cr
Contributed capital	6 000	
Retained Income	7 000	
Bank		R13 000

Exercise 9

Date	Details	Ref	Debit	Credit
Feb 28	Bank		150 000	
	Ordinary Share Capital			150 000
	To record 2 400 ordinary shares issued for R150 000			
Apr 12	Bank		3 200 000	
	Ordinary Share Capital			3 200 000
	To record 200 000 ordinary shares issued for R3.2 million.			
May 25	Bank		80 000	
	Ordinary Share Capital			80 000
	To record 5 000 ordinary shares issued for cash.			
**Sep. 12	Ordinary Share Capital		1 293 000	
	Capital Contribution			18 000
	Bank			1 275 000
	To record 75 000 ordinary shares repurchased for R1 275 000			
Jan. 1	Ordinary share Dividend		526 000	
	Bank			526 000
	Record dividend of R2.50 per share paid to ordinary shareholders.			

Working for 12th September transaction:

Up until the Sept. 12 transaction, the number of shares issued was 78 000 + 200 000 + 5 000 + 2 400 = 285 400 total shares issued.

The amount of these shares was R1 490 000 + R3 200 000 + R80 000 + 150 000 = R4 920 000 total amount. So the average share price is 4 920 000 / 285 400 = R17.24 per share. So the ordinary shares bought back had a total price of 75 000 x R17.24 = R1 293 000. Since the total amount paid for the buyback is R1 275 000 (at R17.00 per share), the difference (R18 000) is charged off to Capital Contributed.

GENERAL LEDGER ACCOUNTS

Dr BANK ACCOUNT Cr

Apr	12	Ordinary shares		3 200 000	Sept	12	Ordinary share		1 179 750
Feb	28	Ordinary share		150 000			Retain Income		95 250

Dr ORDINARY SHARE CAPITAL Cr

Sept	12	Bank		1 293 000	Feb	1	Balance		1 490 000
					Feb	28	Bank		150 000
					Apr.	12	Bank		3 200 000
					May	25	Band		80 000

Dr RETAINED INCOME Cr

		Bank		95 250	Feb	1	Balance	b/d	1 000 000

Dr CONTRIBUTED CAPITAL Cr

							Balance	b/d	75 000
					Sept	12	Ordinary share capital		18 000
									93 000