Problem 19-11

On December 31, 2020, Dow Steel Corporation had 600,000 shares of common stock and 300,000 shares of 8%, noncumulative, nonconvertible preferred stock issued and outstanding. Dow issued a 4% common stock dividend on May 15, and paid cash dividends of $400,000 and $75,000 to common and preferred shareholders, respectively, on December 15, 2021.

On February 28, 2021, Dow sold 60,000 common shares. In keeping with its long-term share repurchase plan, 2,000 shares were retired on July 1. Dow’s net income for the year ended December 31, 2021, was $2,100,000. The income tax rate is 25%.

Compute Dow’s earnings per share for the year ended December 31, 2021.

Problem 19-11 (continued)

Numerator (Basic EPS): Net income = $2,100,000; Preferred dividends = $75,000 (because the preferred stock is noncumulative, only include the dividends that are actually paid).

Denominator (Basic EPS): Weighted average # shares of common stock outstanding.

\[
\begin{align*}
1/1 - 12/31 & \quad 600,000 \times (12/12) = 600,000 \times 1.04 = 624,000 \\
2/28 - 12/31 & \quad 60,000 \times (10/12) = 50,000 \times 1.04 = 52,000 \\
7/1 - 12/31 & \quad (2,000) \times (6/12) = (1,000) \\
\end{align*}
\]

Weighted average # shares = 675,000

\[
\text{EPS} = \frac{($2,100,000 - $75,000)}{675,000} = $3.00
\]