FORMS OF DIVIDENDS DISTRIBUTION PRACTICED BY FIRMS

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Abstract: Subject of real interest both academic world and practice world, the study of the dividend decision offer us a large field of research. In this paper, I try to explore only a little part of this, namelly the presentation of the forms of dividends distribution practiced by firms. So, after a short introduction I present at length the main forms of dividends distribution: payment of dividends cash or in kind; payment of dividends in shares; distributing dividends through stock operations; collateral forms of distribution, with clear presentation of the similitudes and differents that exist between them. Finally, I present some conclusions concerning this subject.

1. Introduction

Both the financial theory and practice consider the dividend decision a very interesting field of study due to the challenges that this subject offers to the scientific research. With a simple approach, in an economic environment less complex, in the framework of the decision of dividend, appears the problem of choosing from distribution of dividends or capitalization of a greater part of the net profit. Gradually according to the development of the economic environment, new questions connected to this type of decision appear, for which the financial management must fiind an answer:

- Which are the forms of dividends distributing?
- Which are more important higher earnings growth or the payments in dividends?
- How can the interests of the different capital contributors be hramonised?

The evolution of the studies regarding the dividend decision has shown the fact that there is a permanent preoccupation for dividend distribution depending on what is more important for the company. So, for attaining a top position on the market, the companies must make their shareholders devoted and keep them, for preventing difficulties in the way to the top.

According to our legislation in force, **the dividend** is any distribution in money or in kind, made by a legal entity to a participant to the legal entity, as a consequence of the possession of some participation titles to that legal entity, except the following situations:

- a distribution of supplementary participation titles which does not modify the percent of participation title possession of any participant to the legal entity;
- a distribution in money or in kind, made in connection to the reinvestment of the participating titles to the legal entity, other than the reinvestment that is a part of the reinvestment plan, that does not modify the percent of title possession of any participant to the legal entity;
- a distribution in money or in kind, made in connection with the liquidation of a legal entity;

▪ a distribution in money or in kind, made with the occasion of registered capital reducing constituted by the participants.

If the amount paid by a legal entity for the goods or services provided for a participant to the legal entity outruns the market price for this kind of goods or services, than the difference is treated as a dividend.

A very sinthetic definition would be: o quota of the profit that is paid to each shareholder (partner) represents a dividend.

We consider to be a very *precise, clear and concise* definition the following: the **dividend** represents any distribution made by a legal entity, in cash and/or in kind, in favour of its shareholders or partners, from the net profit established on the basis of annual financial statement, proportionally with the participation quota of these to the registered capital, if in the constitutive document hasn't been scheduled in this way.

So, any shareholder has the right to receive dividends form the company. What we have to keep in mind, is the fact that dividends distribution **is submitted to the following** conditions:

- existence of real profits, determined in terms of the accomplished activity volume, recognized by beneficiaries, by respecting fiscal rules and bookkeeping rules, so that the distribution of dividends shouldn't affect the substance of the company and the permanent stock exchange capitalization of this;
- approval of results from the profit and loss account by the general Board of Directors after their approval by the managing board and the auditing commission;
- establishing the dividend amount in accordance with proposals of the Managing Board, by the Shareholders' General Assembly (SGA), and the sum of dividends shouldn't outrun the total net profit for this destination;
- distribution of dividends shouldn't affect the liquidities of the company and shouldn't endanger the safety of its creditors whose assets become falling due.

2. Forms of dividends distribution

In conclusion, the net result, obtained after deducting the fiscal obligation of the economic agent regarding the income tax, rightful to the shareholders as cost of their own stock brought in the company, may be distributed to them, having the following forms:

A. **Payment of dividends cash or in kind;**
B. **Payment of dividends in shares;**
C. **Distributing dividends through stock operations;**
D. **Collateral forms of distribution.**

A. ***Dividends***, there are, generally paid cash, after the conclusion of the financial exercise and approval of the annual financial statements by the Shareholders' General Assembly.

At the time of the effective distribution, the company, using the method of the source retaining, must retain and transfer to the State budget the *dividend tax*. In accordance with the modified Law no. 571/2003 regarding Fiscal Code, incomes represented by dividends, including the amounts received for the possession of titles of participation at the closed investments funds, are imposed with a quota of minimum 10% form the gross amount of these, if the shareholders are legal entities and 16% if the shareholders are physical persons, *in the case of residents,* and respectively with a quota of 16%, regardless if they are physical persons or legal entities, *in the case of non-residents* (if it is applied a convention of avoiding a double imposing, a more favourable quota may be applied). It is also important to remember, the fact that beginning with 01.01.2007, there will be a dividend income exemption in the case of dividends paid by a Romanian legal entity to another legal entity, Romanian or resident in UE Member States, on condition that the beneficiary of dividends should own minimum 15% from the shares of the company that distributes the dividends, respectively 10%, beginning with 2009, on an uninterrupted minimum period of 2 years until payment date of these.

The obligation of calculation and retain of the income tax under the form of dividends belongs to the legal entities at the same time with the payment of the dividends to the shareholders or partners. The deadline for income tax payment is until 25^{th} day of the next month to the one in which the payment is made. In the case of distributed dividends,which haven't been paid to shareholders or partners until the end of the year in which the annual financial statements have been approved, dividends income tax is paid until 31^{st} of December of the respective year.

Generally, in Western countries, the dividend income tax is paid together with the other incomes, divided in parts according to size.

If it is foreseen in the company statute, and especially if the company achieves products which the shareholderes are interested in, that the dividend payment can be made in kind,obviously after the payment of fiscal obligations. This type of payment is possible only if the activity field allows it, that is if the shareholders may receive an entire number of goods.

Regardless of the payment way, the dividend at his turn can have two formes: **the first dividend** and **super dividend**

The first dividend also named **statutary or regular dividend** is established under the form of the *minimum guaranteed* (a percent of the net profit) anticipated in the company statute and it is compulsory to pay if the net profit allows it. This indicates the fact that the company management is expecting to maintain the payments in the future. Generally, it can't be cumulative, meaning that it can't be totalized to the dividend of the current year, the statutary dvidends unpaid for different reasons entirely or partially, in the previous years.

If the net result allows it, the general board of the shareholders may decide the payment of a **super dividend** above the value of the statutary dividend.

The legislation in some countries stipulates the obligativity of the distribution of a certain percent from the net profits.

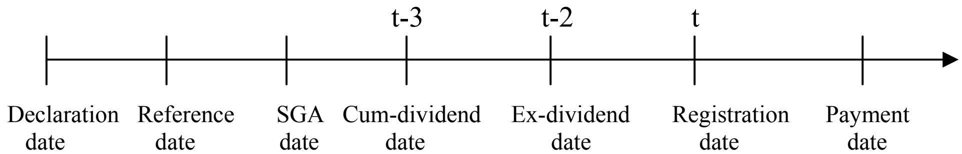
It is to consider the fact that some shareholders prefer cash, and other the reinvestment of the dividends in the company. To support them some companies automatically offer a *dividend reinvestment plan*. This means that the shareholders who agree with this plan will use the dividends to buy additonal shares that are usually issued with a small discount (5-10%) given the fact that the company saves money comparatively with normal issuing of shares.

Given the fact that the shares are transactioned constantly, is interesting to know the key facts that occur in the dividend distribution:

- *Declaration date,* it is the date when the Managing Board announces the intention of distributing dividends and convokes the Shareholders' General Assembly;
- *Reference date* is the day when the shareholders entitled to participate and to vote in SGA are identified;
- *Registration date* (t moment), according to the Law no.297/2004 regarding the capital market, is the date that serves to identify the shareholders that shall benefit from

dividends or other rights and upon whom are reflected the effects of the decisions made by the general meeting of the shareholders. This date shall be established by SGA and will be subsequent to SGA date;

- *Cum-dividend data* is the last day when there can be bought the shares for benefitting from dividends.Taking into consideration the registration date, this is the t-3 moment. We mention that only lucrative days are taken into consideration;
- *Ex-dividend data* is the first day when the transactioned shares don't include the dividend, meaning the right to the dividend is separated from the share, practically the t-2 moment. Not taking into consideration the normal fluctuation on the capital market, the price of the shares generally registrates a decrease equal to the value of the dividend approved by SGA;
- *Payment date.* The dividends are paid within the term established by SGA, depending on the situation, established by special laws, but not later than six months from the date of the apporval of annual financial statements, afferent to the concluded financial exercise. Otherwise the company will pay damages-interests for the period of delay, at the level of legal interest, if through the constitutive document or by the SGA decision, which has approved the financial statements afferent to the concluded financial exercise, hasn't been established a greater interest.



In table 1 it can be seen the gross value of dividends distributed in cash by some important companies listed at BVB and the main key data.

Table 1

The gross value of dividends distributed in cash by some important companies listed at BVB and the main key data

Symbol	Gross Dividend value (lei)	Reference date	SGA date	Cum-dividend date	Registration date
ALR	0,3891	27/03/07	25/04/07	09/05/07	14/05/07
ALU	0,3600	23/04/07	17/05/07	14/05/07	01/06/07
ATB	0,0231	16/04/07	27/04/07	11/05/07	16/05/07
BRD	0,3672	10/04/07	19/04/07	27/04/07	04/05/07
DUCL	0,0462	10/04/07	26/04/07	10/05/07	15/05/07
OIL	0,0012	02/04/07	27/04/07	10/05/07	15/05/07
SIF1	0,0600	09/03/07	28/03/07	14/05/07	17/05/07
SIF2	0,0630	01/03/07	28/03/07	10/05/07	17/05/07
SIF4	0,0700	21/03/07	28/04/07	10/05/07	15/05/07
SIF5	0,0700	14/03/07	28/04/07	10/05/07	15/05/07
SNO	0,4000	23/03/07	14/04/07	25/04/07	30/04/07
SNP	0,0179	30/03/07	18/04/07	27/04/07	04/05/07
TBM	0,0300	19/04/07	26/04/07	10/05/07	15/05/07
TEL	1,4700	06/04/07	26/04/07	09/05/07	14/05/07

Source: BSE

B. ***Payment of dividends in stocks (stock dividend)***

The way of distributing stock dividends is assimilated, from a legal point of view, to an increase of registered capital in cash. This can be done by joint-stock companies, for the entire or partial amount of dvidends, the payment proportion in stock shares being established by the SGA with the condition that this possibility should be stipulated in the statute.For example, a company can declare a dividend distribution in stocks of 10%. In this case, the shareholder of 100 stocks receives 10 extra stock shares without paying for them. The effect, is that the increasing number of shares makes the profit the dividend and the share price, to decrease. Also, an increase of the registered capital of this type has as effect the exemption of the company of an liquidity payment like when the distribution is made in cash), contributing at the same time, at the improvement of the financial indebted degree through the increase of the proper capitals.

Sometimes, the payment offer in cash or in shares is made by all the shareholders who have to communicate their preferrence at a determined date. The idea of this distribution form has as basis both the investment development and protection of population savings and also the maintenance of the share price within certain limits. The problem that occurs is that of the price (exchange) of corresponding shares which under no circumstances, shouldn't be under the nominal value of the titles.

It is interesting to see to what extent the *payment procedure* draws a wealth transfer towards the shareholders, given the fact that some shareholders prefer cash and others shares.

Thus, we note:

P_1 = price after the detaching of the payment coupon of the dividend (date ex-dividend);

P_0 = previous selling price (cum-dividend date);

D = dividend per share;

P_E = issuing price of the new shares in order to cover the dividend payment with this purpose;

p = distributing percent of free shares;

n = shares number that must be detained in order to have the right of a free share, $\frac{1}{p}$.

Shareholders who prefer *dividends payment in cash s*hall have at the ex-dividend date a share with the value P_1 and waits for a dividend D, taht is a value (P_1+D).

Shareholders who prefer *dividend payment in shares* shall have a value $P_1 \cdot (1+p)$.

As a consequence, there will take place a wealth transfer in favour of the ones who prefer dividend payment in shares in the detriment of those who prefer cash payment, when:

$$P_1 \cdot (1+p) > P_1+D \quad (1)$$

$$P_1 \cdot p > D \ (2)$$

Taking into account the fact that, generally,

$$P_1 = P_0 - D, \text{ we obtain: } (3)$$

$$(P_0 - D) \cdot p > D \ (4)$$

$$P_0 \cdot p > D \cdot (1+p) \ (5)$$

$$P_0 > \frac{D}{p} + D \quad (6)$$

$$P_0 > n \cdot D + D \quad (7)$$

$$P_0 > P_E + D \quad (8)$$

Therefore, shareholders who prefer dividends in cash are disadvantaged if the exchange value before the decision for distributing is higher than the price of issuing of the new shares increased with the value of the dividend. In the opposite situation, the wealth transfer is in their favour.

C. ***Distributing through capital operations***.

In this category we have, especially:

- Reduction of registered capital (repurchase and annulment of shares);
- Distribution of free shares.

Reduction of registered capital may be a purely bookkeeping opration if it is motivated by the loss registrated by the company. But, the reduction of the registered capital can be realized through **repurchase and annulment of a number of shares**. *This operation is assimilated with the dividend payment in cash to the extent in which it draws a funds transfer towards the shareholders of the company.* However it is distinguished by the dividend payment in cash through its optional character and through the liberty that the shareholder has to decline this kind of offer totally or partially. At the same time, this operation is also a mea nod selecting the shareholders. Reduction of registered capital can be realized only with the vote of the majority of the shareholders gathered in an extraordinary general meeting that leads to the modification of the statute of the company. The buying offer is presented at the same time to all the shareholders. If the number of the titles offered by the shareholders is higher than the number of the ones the company wishes to ransom, all the offers are reduced, in the same proportion, according to the rate, depending on the quota of the number of the ransom titles per number of offered titles.

From the reasons that can lead to the reducing of the registered capital, we remember:

- The attempt to consolidate the control of the management team, in order to avoid a hostile taking over;
- The management team considers that the shares of the company are underrated;
- The company disposes of funds in excess;
- The management team believes that the shareholders will benefit more if the company will ransom a part of the shares than if the funds in excess are paid as dividends in cash.

In order to show why the ransom is similarly to the dividend payment in cash we shall staudy table no.2.

In the basic scenario (original balance sheet), the shareholders own 100.000 shares with a total value on the market of 1.000.000 lei. This means that the value on the market of one share is 10 lei.

We start from the idea that the company recommends to give a dividend of 1 leu per share. This means that the total amount the company has to pay in dividends is of 100.000 lei. Thus, the financial availability will decline with 100.000 lei and, implicitly, the value of the company on the market will reach the value of 900.000 lei. Being given the fact that 100.000 shares are still in circulation, the price of a share will decline at 9 lei/share. We assume that in the basic script somebody owned 1% from the total of shares, meaning 1.000 shares. After the dividends payment in cash he will receive *1.000 lei cash and he would still have 1.000 shares with the market value of 9.000 lei.*

Table 2

Assets		Liabilities and shareholders' equity	
|Cash, (lei)	150.000	Debt, (lei)	0
Other assets, (lei)	850.000	Equity, (lei)	1.000.000
Value of the company, (lei)	1.000.000	Value of the company, (lei)	1.000.000
Total number of shares	100.000		
Price per share, (lei)	1.000.000/100.000 =10		
Cash, (lei)	50.000	Debt, (lei)	0
Other assets, (lei)	850.000	Equity, (lei)	900.000
Value of the company, (lei)	900.000	Value of the company, (lei)	900.000
Total number of shares	100.000		
Price per share, (lei)	900.000/100.000 =9		
Cash, (lei)	50.000	Debt, (lei)	0
Other assets, (lei)	850.000	Equity, (lei)	900.000
Value of the company, (lei)	900.000	Value of the company, (lei)	900.000
Total number of shares	90.000		
Price per share, (lei)	900.000/90.000 =10		

If the company will ransom 10% of his shares with a price of 10 lei/share, this will have to decrease it money disponibilities with 100.000 lei and thus the company assets will decline at 900.000 lei.The number of the shares still in circulation will be of 90.000 and thus the price will be of 10 lei/share. The owner of the 1.000 shares will sell 100 shares and he will receive *1.000 lei in cash, and the other 900 shares which remain will still value 9.000 lei.*

Therefore from the shareholder's point of view the situation is similar.

Free shares distribution are frequently assimilated to the distribution of dividends under the form of titles. This kind of operation permits the company to offer new shares to its shareholders, as a consequence of:

- the increase of the registered capital through the incorporation of reserve, the undistributed proffits or issuing bonus,
- Share division.

The increase of registered capital through the incorporation of reserves, undistributed proffits and issuing bonus, assumes only the modification of the equity structure (the increase of registered capital and the decrease of the same sum of money of the reserves, undistributed proffits or issuing bonus) and of the number of shares which will increase, which means a possitive influence upon the treasury of the company.

This kind of operation is not reflected in any flux of funds, its impact consisting in a reinforcement of trust to a third part, towards this engagement of the shareholders of keeping their funds in the company.

The interest of the increase of the registered capital in this manner is, more often, that of harmonizing the registered capital with the activity volume of the company and it can be realized only with the approval of the extraordinary board meeting.

As an example we have the announcement of Transilvania S.A Bank, from 14.03.2008, through which the Management Board convokes SGA At point no 1 from daily order of the extraordinary board meeting we can see the proposal of registered capital increase with the amount of 448.616.412,8 lei, through the issuing of 4.486.164.128 new shares with the nominal value of 0,1 lei/share. The increment of the registered capital will be realized through the use of three major sources, respectively:

a) the capitalization of reserves constituted from the net profit, already existing in the balance account according to the balance sheet from 31.12.2007, having the value of 319.460.775 lei, respective the issuing of a number 3.194.607.750 new shares with a nominal value of 0,1 lei/share, in the benefit of the shareholders registered at the Shareholders Register of the Central Deposit at the date of the registration (proposal 16 may 2008);

b) utilization of issuing bonus entirely cashed in, having the value of 98.601.649 lei, respective the issuing of a number of 986.016.490 new shares with a nominal value of 0,1 lei/share, in the benefit of the shareholders registered at the Shareholders Register of the Central Deposit at the date of the registration;

c) new contributions from the shareholders registred at the Shareholders Register of the Central Deposit at the date of the registration, the amount of 30.553.988,80 lei, respective the issuing of a number of 305.539.888 new shares with the nominal value of 0,1 lei/share. The issuing price per share afferent to this majority source is of 0,35 lei/share.

Regarding the fact that at this moment, the company has a total number of 6.110.797.702 shares with a nominal value of 0,1 lei/share, meaning a registered capital of 611.079.770,2 lei means that the following will be offered free:

- from reserves: $\frac{319.460.775}{611.079.770,2} = 52,27\%$
- from bonus: $\frac{98.601.649}{611.079.770,2} = 16,13\%$,

which means a total of 68,40%, that is 1.000 shares owned, every shareholder will receive free 684 shares.

The subscription in cash: $\frac{30.553.988,8}{611.079.770,2} = 5,00\%$, that is at 1.000owned shares, 50 shares can be preferentially subscribed at a price of 0,35 lei/share.

Other companies that have distributed free shares in the last period, are presented in table.3

Table 3

Symbol	Quantity	Reference Date	SGA Date	Cum- dividend Date	Registration Date
ALBZ	0,4426	25/07/07	22/08/07	12/09/07	15/09/07
ARCV	0,7500	13/04/07	28/04/07	11/05/07	16/05/07
CEON	0,5471	20/08/07	13/09/07	29/10/07	01/11/07
PREB	0,5000	06/04/07	25/04/07	08/05/07	11/05/07
TSND	1,4022	03/12/07	10/12/07	01/02/08	29/01/08

Source:BSE

Shares Division consists in the increase of the number of the shares and the decrease of their nominal value, the amount of the registered capital remaining constant.

Both operational categories require the emission of new shares, these being different from juridicial and accounting point of view.

Shares division (stock split) is strongly connected with the payment of dividends in shares, because in both cases the shareholder receives an invariable number of new shares for every owned share. For example at a division of 2 to 1, every shareholder will receive an extra share for every owned share.

Thus, a division of 2 to 1 is like a dividend payment in shares of 100%. Both have as a result the doubling of the number of total shares but do not affect the total assets, total profits or total value of the company.

The reason for the shares division is that, even though there are many empirical proves in this sense, still there is one shared opinion in financial circles, in the sense of the existence of an optimum price interval for the real estate values. "Optimum " must be understood here in the sense that if the price is inside this interval, PER and thus the value of the company will be maximized. Thus the majority of divisions have as motivation the desire of bringing the share price in this optimum interval of tranzaction.

Shares division, is generally used when a massive discount of price after this had increased very much, is desired. Dividends payed in shares are frequently used in order to mentain the share price between certain ranges. For example if the profits and dividends of a company increase with a installment of 20% anually, the price of a share will tend to increase with approximately the same installment and very soon it will be placed outside the optimum interval of tranzaction.

The new shares from dividends, generated annualy of 20%, will mentained share price inside the optimum interval of tranzaction.

The difference between dividends in shares and shares division is a technical one. Therefore, the dividends payment in shares is shown in the balance sheet as a transfer of the undistributed profits and reserves at the registered capital, while the shares divisions appears as a proportional discount of the nominal value of every share. In none of the situations the entire equity is not affected.

D. ***Collateral aspects of distribution***

Besides the different legal aspects of result distribution a section of the shareholders, more precisely the main shareholders, can benefit of different advantages: a higher wage than that of a wage earner manager for the same ability, different advantages in kind, greater rents for buidings rented to the company by real estate companies controlled by the main shareholders. These financial or material advantages are seen financially as real dividends, but they mostly infringe the juridical, moral principles of equality among shareholders. The existence of these false dividends is characteristic, especially, for medium and small size entreprises, for which even the statistical observations certify a lower rate of dividends distribution, exactly because this "different" type of compensation of which they benefit. In addition these "**false dividends**" are also a source of conflict between the shareholders of the companies that use them.

3. Conclusions

An optimum decision regarding the dividend involves the assurance of an optimum between the part from the net profit distributed as dividends and the remaining part for the self- financing that will assure the future growth of the company, and so the premises of the increase of the share price.

When the SGA decides not to be distribute entirely the net profit, a part of the shareholders is deprived of its right to accomplish an immediate income in the exchange of the hope of achieving a future income. This stays at the basis of the *selection of the shareholder for the company*.

We must specify that the singular interest of the problems of dividend made the object of numerous theoretical achievements and empirical studies of testing of these theories and thesis, but without reaching any common points of view and that is why, as we can't speak about an unitary dividend decision but rather *of methods and applications which stand at the basis of the decision of dividends distribution, in the same way we can't make a final statement about which is the best modality to distribute dividends*.

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