

ACCOUNTING in the headlines

How would Crocs account for the conversion of its preferred stock into common stock?

At the end of December 2013, Crocs Inc. announced that Blackstone Group is investing \$200 million into the footwear company in the form of a preferred stock purchase. In three years, the preferred stock shares owned by Blackstone Group will convert into common shares if the Crocs common stock market price rises to a certain level. Crocs' preferred stock has a par value of \$0.001 per share, as does its common stock. Over the next three years, Blackstone Groups expects Crocs to replace its CEO, close some stores, expand into Asia, and offer new products in an effort to increase its stock price.

Assume that Blackstone Group purchases 4 million preferred shares with its \$200 million investment in the first quarter of 2014.

Questions

1. Assume that in three years, the market price for one share of Crocs common stock is \$75 and this market price meets the original conversion criteria when Blackstone Group made its original investment. Also assume that one share of preferred stock converts into one share of common stock. Write the journal entry that Crocs would prepare to convert the preferred stock shares into common stock shares.
2. What is the impact of this conversion of preferred stock into common stock on Crocs' assets, liabilities, and stockholders' equity?
3. Why would preferred stock shares have been attractive to Blackstone Group when it made the initial investment in Crocs?
4. Why would Blackstone Group have wanted the conversion feature on the Crocs preferred stock that it purchased?