Revised Syllabus at T.Y.B.Com.

With Effect from the Academic Year 2015-2016 for

IDOL Students

Financial Accounting and Auditing Paper-III

Financial Accounting

SECTION I
Modules at a Glance

Sr. No.	Modules	No. of Lectures
1	Amalgamation of Companies (w.r.t AS-14, Excluding inter Company holdings)	18
2	Capital Reduction & Internal Reconstruction	10
3	Investment Accounting w.r.t. AS 13	12
4	Preparation of Final Accounts of Companies.	15
5	Introduction to IFRS	05
Total		**60**

Note: Final accounts of limited companies wherever applicable should be as per the format prescribed by Revised Schedule VI of Companies Act 1956 as per NOTIFICATION NO. S.0.447 (E), DATED 28-2-2011 [AS AMENDED BY NOTIFICATION NO. F.NO. 2/6/2008-CL-V, DATED 30-3-2011]

Sr. No.	Modules / Units	
1	**Amalgamation of Companies (w.r.t. AS 14) (Excluding Intercompany Holdings)**	
	(i)	In the nature of merger and purchase with corresponding accounting treatments of pooling of interests and purchase methods respectively
	(ii)	Computation and meaning of purchase consideration
	(iii)	Problems based on purchase method of accounting only

2	**Capital Reduction and Internal Reconstruction**	
	(i)	Need for reconstruction and Company Law provisions
	(ii)	Distinction between internal and external reconstructions
	(iii)	Methods including alteration of share capital, variation of share holder rights, sub division, consolidation, surrender and reissue/cancellation, reduction of share capital, with relevant legal provisions and accounting treatments for same
3	**Investment Accounting w.r.t. AS -13**	
3.1	(a)	For Shares (Variable income bearing securities)
	(b)	For Debentures, bonds etc. (Fixed Income bearing securities)
3.2		Accounting for transactions of purchase and sales of investments with ex and cum interest prices and finding cost of investment sold and carrying cost as per weighted average method
3.3		Columnar format for investment account
4	**Preparation of Final Accounts of Companies**	
	(i)	Relevant provisions of Companies Act related Final Account (excluding cash flow statement)
	(ii)	Preparation of profit and loss a/c and balance sheet as per revised schedule VI of - Companies act 1956
	(iii)	AS 1 in relation to final accounts of companies (disclosure of accounting policies)
5	**Introduction to IFRS**	
	(i)	Purpose and objectives of Financial statements – Its framework – Its Assumptions, characteristics, elements, recognition and measurement
	(ii)	Convergence and first time adoption of IFRS [IFRS – 1]

SECTION II

Modules at a Glance

Sr. No.	Modules	No. of Lectures
1	Final accounts of Co-operative Housing Society	16
2	Ascertainment and Treatment of Profit Prior to Incorporation	10
3	Valuation of Goodwill and Shares	12
4	Accounting for Translation of Foreign Currency Transactions. Vide AS-11 (Excluding foreign Branches & forward Exchange Contracts & Headings Contracts)	12
5	Buy Back of Equity Shares	10
Total		**60**

Note: Final accounts of limited companies wherever applicable should be as per the format prescribed by Revised Schedule VI of Companies Act 1956 as per NOTIFICATION NO. S.0.447 (E), DATED 28-2-2011 [AS AMENDED BY NOTIFICATION NO. F.NO. 2/6/2008-CL-V, DATED 30-3-2011]

Sr. No.	Modules / Units
1	**Final accounts of Co-operative Housing Society**
	(i) Provisions of Maharashtra State Co-operative Societies Act & Rules (ii) Accounting provisions including appropriations to various fund (ii) Format of final accounts – Form N (iii) Simple Practical problems on preparation of final accounts of Co-operative Housing Society

2	**Ascertainment and Treatment of Profit Prior to Incorporation with** :
	(i) Principles for ascertainment (ii) Preparation of separate, combined and columnar profit and loss a/c including different basis of allocation of expenses/ incomes
3	**Valuation of goodwill and Shares**
3.1 3.2	Valuation of goodwill i. Maintainable Profit method ii Super Profit Method- based on simple average method iii Capitalisation Method- based on simple average method Valuation of shares i. Intrinsic value method ii Yield Method
4	**Accounting for translation of foreign currency transactions vide AS 11 (excluding foreign branches and forward exchange contracts and hedging contracts**)
4.1	"In relation to purchase and sale of goods, services and assets and loan and credit transactions."
4.2	Computation and treatment of exchange differences
5	**Buy Back of Equity Shares**
	(i) Company Law/ Legal Provisions (including related restrictions, power, transfer to capital redemption reserve account and prohibitions) (ii) Compliance of conditions including sources, maximum limits and debt equity ratio

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AMALGAMATION OF LIMITED COMPANIES-I

Unit Structure

8.0 OBJECTIVES:

After studying this unit the students will be able to:

- Understand the Concept of Amalgamation
- Calculate the amount of Purchase Consideration
- Know the Various methods of ascertaining Purchase Consideration.
- Make the Accounting Procedure for Amalgamation.

8.1 INTRODUCTION:

Amalgamation means coming together of two or more limited companies for betterment of the business. It includes dissolution of one or more limited companies and formation of one new company. There can be three situations as below:

a) Amalgamation- Here one or more than one existing limited companies come together and form a new limited company to take over their business.

b) Absorption- Here one existing limited company takes over the business of another existing limited company

c) External reconstruction - Here one limited company is newly formed to take over the business of another existing limited company which is a loss making company.

The I.C.A.I has issued Accounting Standard 14 governing the procedure and accounting of Amalgamation of companies.

8.2 ACCOUNTING STANDARD 14 ISSUED BY INSTITUTE OF CHARTERED ACCOUNTS OF INDIA:

i. **Scope:** Accounting Standard 14 [Accounting for Amalgamation], prescribed by the Institute of Chartered Accounts of India, deals with accounting for amalgamations. The meaning and types of amalgamation, according to AS 14 are explained below.

ii. **Amalgamation:** Amalgamation means an amalgamation pursuant to the provision of the Companies Act, 1956 or any other statute which may be applicable to the Companies, Amalgamation involves acquisition of one company by another. After Amalgamation, the acquired company is dissolved and ceases to exist.

iii. **Transferor Company:** Transferor Company means the Company which a transferor another Company (vendor company).

iv. **Transferee Company:** Transferee Company means the Company into which a transferor Company is amalgamated (purchasing company).

v. **Types of Amalgamations :** (discussed in detail below)

8.3 TYPES OF AMALGAMATION:

The Companies Act 1956 has not specifically defined the term ‘Amalgamation’. However from several legal decisions, the definition of Amalgamation may be inferred. The Institute of Chartered Accountants has introduced Accounting Standard no.14 (AS-14) on Accounting for Amalgamations. The standard recognizes two types of Amalgamations.

(a) Amalgamation in the nature of merger.
(b) Amalgamation in the nature of purchase.

(a) Amalgamation in the nature of merger means which satisfies all the following conditions:

i. All the assets and liabilities of the transferor company are taken over by the transferee company.

ii. Shareholders holding not less than 90% of the face value of equity shares of the transferor company (other than the equity shares already held therein, immediately before the amalgamation, by the transferee company or its subsidiaries of their nominees) become equity shareholders of the transferee company by virtue of the amalgamation.

iii. The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.

iv. The business of the transferor company is intended to be carried on after the amalgamation, by the transferee company.

v. No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies.

(b) Amalgamation in the nature of purchase If Amalgamation does not satisfy any one of the above five conditions then it will be regarded as Amalgamation in the nature of purchase

8.4 DISTINCTION BETWEEN MERGER AND PURCHASE:

Merger	Purchase
1. Shareholders of the transferor company holding 90% of the face value of equity shares become shareholders of transferee company.	1. Shareholders of the transferor company may not become shareholders of transferee company.
2. There is a genuine polling of assets and liabilities of the amalgamating companies.	2. There is no genuine polling of assets and liabilities of the amalgamation companies.
3. There is poling of interest of shareholders also.	3. There may not be pooling of interest of shareholders
4. Values of assets and liabilities, reserves represent the same values of amalgamating companies.	4. The values of assets and liabilities may be different than the amalgamating companies.

In the syllabus of T.Y.B.Com of Mumbai University Amalgamation in the nature of merger is excluded, it is not discussed henceforth in this book.

8.5 PURCHASE CONSIDERATION:

8.5.1 MEANING

Purchase Consideration is the sale price of the business agreed mutually between the two parties, the transferor company (selling company) and the transferee company (purchasing company). The AS 14 defines the Purchase Consideration as " the aggregate of the shares and other securities issue and payment made in the form of cash or otherwise by the transferee company to the "SHAREHOLDERS OF THE TRANSFEROR COMPANY". In other words any payment made to or in satisfaction of other liabilities should not be included in the amount of purchase consideration. If any payment is made to the creditors, debenture holders or any other liabilities, then it should be assumed that such liability is taken over by the transferee company and then it is settled by the transferee company. It should also be noted that liquidation expenses of the transferor company should not be included in the purchase consideration.

8.5.2 METHODS OF PURCHASE CONSIDERATION:

a. **Lump-sum method**: The problem may give the amount of purchase consideration directly and hence there will not be any need to calculate the purchase consideration.
e.g. Alka techno Ltd. agrees to take over business of WLC Ltd for a sum of Rs.10 lakhs.

b. **Net Payment Method**: If the purchase consideration is not given Lum-sum then this method should be adopted. Here the purchase consideration is arrived at by adding up cash paid and the agreed values of shares, securities issued by the transferee company to share holders of transferor Company in discharge of the purchase consideration.
e.g. Reena Engineers Ltd. takes over business of Ramesh Kashyap Ltd. and agrees to pay the purchase consideration as follows:

Issue of 10,000 equity shares of Rs.10 each at Rs. 12 each and cash Rs. 50,000.

Hence the purchase consideration would be	Rs
10,000 equity shares of Rs.10 each at Rs. 12 each	1,20,000
Cash	50,000
Purchase consideration	**1,70,000**

c. **Net Assets Method** : If the purchase consideration can not be calculated by above two methods then this methods should be adopted. It is the aggregate of the assets taken over at agreed values less liabilities taken over at agreed values.

Assets taken over at agreed values,(excluding ficitious assets)	Rs.	Rs.
Goodwill	xx	
Land & Buildings	xx	
Plant & Machinery	xx	
Furniture & Fittings	xx	
Motor vehicles	xx	
Investments	xx	
Stock	xx	
Debtors	xx	
Cash & bank balances	xx	xxx
Less : Liabilities taken over at agreed value		
Creditors	xx	
Bills payables	xx	
Bank over draft	xx	
Debentures	xx	(xxx)
Purchase consideration		xxx

d. **Exchange of shares Method / Intrinsic value Method:** Under this method the intrinsic value of the shares of both the companies is calculated and then the transferor company issues the shares to the transferee company on the basis of these values.

8.6 ACCOUNTING PROCEDURE IN THE BOOKS OF TRANSFEROR COMPANY:

Step 1. Open following Ledger Accounts

1. Realisation A/c
2. Equity Shareholders A/c
3. Preference Shareholders A/c
4. Cash/ Bank A/c
5. Liabilities not taken over A/c
6. Transferee company’s A/c
7. Equity Shares in transferee company A/c
8. Preference Shares in transferee company A/c

Step2. Pass following journal entries

Sr. no	Particulars	Dr. Rs	Cr. Rs
1.	Transfer all assets to realization A/c Whether taken over or not , at their book values.		
	Realisation A/c Dr.	xx	
	To Sundry assets A/c		Xx
	Note: 1.Fictitious assets should not be transferred to realization A/c		
	2. Cash & bank balance should be transferred to realization A/c only if it taken over by the transferee company		
	3. Debtors and R.D.D should be treated as separate A/c. Debtors should be transferred at their gross value on debit side and R.D.D should be transferred on the credit side of realisation A/c		
	4. This entry closes all Assets A/c		
2.	Transfer all liabilities which are taken over by the transferee company to realization A/c, credit side		
	Sundry liabilities A/c Dr.	xx	
	To Realisation A/c		xx
3.	Open separate A/c for Each liability not taken over and bring down the balance on the credit side.		
4.	Transfer Equity Share Capital and Reserves to Equity share holders A/c		
	Equity share Capital A/c Dr.	x	
	Securities Premium A/c Dr.	x	
	Capital Reserve A/c Dr.	x	
	Capital Redemption Reserve A/c Dr.	x	
	General Reserve A/c Dr.	x	
	Profit & Loss A/c Dr.	x	
	To Equity Shareholders A/c		x
5.	Transfer Preference Share Capital to Preference Shareholders A/c		
	Preference Share Capital A/c Dr.	x	
	To Preference Shareholders A/c		x

6.	Record the sale of business		
	Transferee Company A/c Dr.	x	
	To Realisation A/c		x
	(with the amount of purchase Consideration)		
7.	Receive the amount of purchase consideration		
	Equity shares in transferee company A/c Dr	x	
	Preference shares in transferee company A/c Dr.	x	
	Cash/ Bank A/c Dr.	x	
	To Transferee Company A/c		x
8.	Dispose off assets not taken over by the transferee company		
	Cash / Bank A/c Dr.	Xx	
	To Realisation A/c		Xx
	(No separate entry is required for profit/ loss on this transaction it is automatically adjusted in realization A/c)		
9.	Discharge the liabilities not taken over by the Transferee company.		
	Liability A/c Dr.	Xx	
	Realisation A/c (if loss) Dr.	Xx	
	To Cash / Bank A/c		xx
	To Realisation A/c (if Profit)		xx
10.	Payment of realization Expenses		
	Realisation A/c Dr.	Xx	
	To Cash/ Bank A/c.		Xx
11.	Settle the claim of preference shareholders		
	Preference shareholders A/c. Dr.	Xx	
	Realisation A/c. (if paid at premium) Dr.	Xx	
	To preference Shares in transferee Co. A/c		Xx
	To Cash/ Bank A/c.		Xx
	To Realisation A/c. (if paid at discount)		Xx

12.	Balance the Realisation A/c. and transfer the profit / loss on Realisation to Equity Shareholders A/c.		
	a. If Profit		
	Realisation A/c Dr.	Xx	
	To Equity shareholders A/c.		Xx
	OR		
	b. If loss		
	Equity shareholders A/c. Dr.	Xx	
	To Realisation A/c.		Xx
13.	Close the Equity shareholders A/c.		
	Equity shareholders A/c. Dr.	Xx	
	To Enquity shares in transferee Co. A/c		Xx
	To Cash/ bank A/c		Xx

8.7 ACCOUNTING PROCEDURE IN THE BOOKS OF TRANSFEREE COMPANY:

Following Journal Entries are passed in the books of Transferee Company.

8.7.1 PURCHASE METHOD

Sr.no	Particulars	Dr. Rs	Cr.Rs.
1.	Recording Purchase of Business		
	Business Purchase A/c Dr.	xx	
	To Liquidator of transferor company		X
	(The entry should be passed at purchase consideration amount.)		
2.	Recording of assets and liabilities taken over		
	Sundry assets A/c Dr.	xx	
	(With Agreed values)		
	Goodwill A/c (if any) Dr.	xx	
	To Sundry Liabilities A/c		X
	To Business Purchase A/c		Xx
	To Capital Reserve A/c		Xx

3.	Recording Discharge of purchase consideration		
	Liquidator of transferor company A/c Dr.	Xx	
	Discount on issue of shares A/c Dr.	Xx	
	To Equity Share Capital A/c.		XX
	To Preference Share Capital A/c.		XX
	To Securities Premium A/c.		Xx
4.	Discharge of Liabilities of Transferor Company		
	Debentures of Transferor Company A/c Dr.	Xx	
	Discount on issue of Debentures A/c Dr.	Xx	
	To new Debentures A/c.		XX
	To Securities Premium A/c.		Xx
5.	Recording of payment of liquidation expenses		
	Capital Reserve/ Goodwill A/c. Dr.	Xx	
	To Cash/Bank A/c.		Xx
6.	Recording of Expenses incurred by the transferee company for its own formation.		
	Preliminary Expenses A/c. Dr.	Xx	
	To Cash / Bank A/c		Xx
7.	Recoding of Statutory Reserve of transferor company		
	Amalgamation adjustment A/c Dr.	Xx	
	To Statutory Reserve A/c.		XX
8.	Adjusting of mutual indebtedness of transferor & transferee company		
	Sundry Creditors A/c. Dr.	Xx	
	To Sundry Debtors A/c.		Xx

8.7.2 MERGER METHOD

Problems based on merger method are excluded from the syllabus hence not discussed here.

8.8 ILLUSTRATIONS:

Illustration: 1

Balance Sheet of Mihir Ltd as on 31st March 2015 is as follows:

Liabilities	Rs	Assets	Rs
Share Capital 10,000 Equity share of Rs 100	10,00,000	Goodwill	1,00,000
2,000 7% Preference Shares of Rs.100 each fully paid	2,00,000	Land & Building	5,00,000
Securities Premium	1,00,000	Furniture	80,000
Revenue Reserves	1,25,000	Sundry Debtors	4,50,000
Sundry Creditors	1,75,000	Stock	3,80,000
		Bank	90,000
	16,00,000		16,00,000

Mihir Ltd received the following offers:

1. Nishith Ltd. agrees to pay Rs.18,00,000 cash.
2. Waridhi Ltd agrees to take over on the following terms:
   a) Equity shareholders to given 25 Equity shares fully paid of Rs.10 each in Waridhi Ltd for every 2 Equity shares of Mihir Ltd.
   b) 7% Preference shareholders of Mihir Ltd to be issued 9% Preferance shares of Rs.100 each fully paid on 1:1 basis.
   c) Sundry Creditors to be paid in cash.
3. Roohi Ltd. Offers to take over business of Mihir Ltd.as follows:
   a) Assets to be revalued as follows:

Goodwill Land & Building Furniture	2,00,000 7,00,000 50,000

Sundry Debtors	4,00,000
Stock	3,40,000
Bank	90,000

b) Sundry creditors to be taken over subject to 5% discount.

c) 7% Preferance shareholders to be issued 10% Preferance shares of Rs. 100 each of same amount. Balance of purchase consideration to be discharged by issue of Equity shares of Rs.10 each at par.

4 Aashna Ltd. Agreed to take over Mihir Ltd. on the basis of intrinsic value of Equity share of Mihir Ltd., revaluing Goodwill at Rs.2,00,000.the entire purchase price to be paid by issue of 2,000 9% Preferance shares of Rs. 100 each at par and balance in Equity shares of Rs.10 each to be considered worth Rs. 12.50.each.

Calculate:

a) Purchase consideration
b) Statement of net assets taken over in each of the above cases

Solution:

1. Offer of Nishith Ltd.
   a) Purchase consideration: Rs.18,00,000
   b) Statement of net assets taken over

All assets taken over at agreed values:

Goodwill	1,00,000	
Land&Building	5,00,000	
Furniture	80,000	
SundryDebtors	4,50,000	
Stock	3,80,000	
Bank	90,000	1600000
Less : Liabilities taken over		
Sundry Creditors		(1,75,000)
Net assets taken over		14,25,000
Purchase consideration		18,00,000
Capital Reserve		3,75,000

2. Offer of Waridhi Ltd.

a) Purchase consideration

(10,000/2 x25) equity shares of Rs.10	12,50,000
9% Preference shares of Rs. 100 each	2,00,000
	14,50,000

b) Statement of net assets taken over

All assets taken over at agreed values:

Goodwill	1,00,000	
Land&Building	5,00,000	
Furniture	80,000	
SundryDebtors	4,50,000	
Stock	3,80,000	
Bank	90,000	1600000
Less : Liabilities taken over		
Sundry Creditors		(1,75,000)
Net assets taken over		14,25,000
Purchase consideration		14,50,000
Capital Reserve		25,000

3. Offer of Roohi Ltd.

a) Purchase consideration (Net assets method)

All assets taken over at agreed values:

Goodwill	2,00,000	
Land&Building	7,00,000	
Furniture	50,000	
SundryDebtors	4,00,000	
Stock	3,40,000	
Bank	90,000	17,80,000
Less : Liabilities taken over		
Sundry Creditors		(1,66,250)
Net assets taken over		14,33,750
Purchase consideration		14,33,750

b) Discharge of purchase consideration

10% Preferance shares of Rs. 100 each	2,00,000
1,23,375 Equity shares of Rs. 10 each	12,33,750
Total	**14,33,750**

4. Offer of Aashna Ltd.
   a) Purchase consideration Intrinsic value of equity shares method)
   All assets taken over at agreed values:

Goodwill Land&Building Furniture SundryDebtors Stock Bank	2,00,000 5,00,000 80,000 4,50,000 3,80,000 90,000	1700000
Less : Liabilities taken over Sundry Creditors 7% Preferance share capital Net amount payable to equity shareholders	 1,75,000 2,00,000	 (3,75,000) 13,25,000

b) Discharge of purchase consideration

2,000 9% Preference shares of Rs. 100 each at par	2,00,000
1,06,000 equity shares of Rs. 10 each at Rs. 12.50	13,25,000

Illustration: 2

The following is the Balance Sheet of Bad Dream Ltd as on 30th September, 2014

Balance Sheet as on 30th September, 2014

Liabilities	Rs	Assets	Rs
Authorised Share Capital		Land & Buildings	200000
10000 Equity Shares of Rs100	1000000	Plant & Equipments	300000
1000 6% Preference Shares of Rs 100 each	100000	Furnitures	65000
Total	1100000	Patents	45000
Issued capital		Sundry Debtors	149450
6,000 Equity Shares	600000	Inventory	68950
1000 6% Preference Shares of Rs 100 each	100000	Cash	3700
10% Debentures	100000	Profit & loss A/C	307900
Sundry Creditors	100000		
Bank Overdraft	240000		
	1140000		**1140000**

A new Company Good Morning Ltd was formed to take over this company. The Authorized capital of the new company was Rs 1500000 divided into 100000 Equity shares of Rs 10 each and 5000 7% Preference shares of Rs 100 each.

The terms and conditions agreed for this were as follows:

a) 10% debenture holders agreed to take new 9%Debentures of Rs.95000 in full satisfaction.

b) 6% Preference shareholders were to receive 3 new 7% Preference shares of Rs.100 each for every 4 old preference shares.

c) The equity shareholders to receive 30,000 Equity shares of Rs.10 each, credited as Rs.8 paid up

d) Good Morning Ltd. to issue 20,000 equity shares of Rs.10 each at par for cash

e) Good morning Ltd to make a call of Rs.2 per share on shares issued to Bad Dream Ltd.

You are required to give necessary Ledger A/c s to close the books of Bad Dream ltd and Journal entries in the books of Good Morning Ltd and Balance Sheet of Good Morning Ltd.

Solution:

Statement of Purchase consideration: (Net Payment method)

a) 750 7% Perferance shares of Rs.100 each	75000
b) 30,000 Equity shares of Rs.10 each Rs. 8 paid up	240000
	315000

Goodwill/Capital reserve (Net Assets taken over)

Land & Buildings	200000	
Plant & Equipments	300000	

Furnitures	65000	
Patents	45000	
Sundry Debtors	149450	
Inventory	68950	
Cash	3700	832100
Less: Liabilities taken over at agreed values		
10% Debentures	100000	
Sundry Creditors	100000	
Bank Overdraft	240000	440000
Net Assets taken over		392100
Purchase consideration		315000
Capital Reserve		77100

In the books of Bad Dream Ltd

Realization A/c

To Land & Buildings	200000	By 10% Debentures	100000
To Plant & Equipments	300000	By Sundry Creditors	100000
To Furnitures	65000	By Bank Overdraft	240000
To Patents	45000	By Good Morning	315000
To Sundry Debtors	149450	By Pref Shareholders A/c	25000
To Inventory	68950	By Equity Share holders A/c	52100
To Cash	3700		
	832100		832100

Equity Shareholders A/c

To Profit and Loss	307900	By Equity Share Capital A/c	600000
To Realisation A/c	52100		
To Equity Shares in Good Morning Ltd	240000		
	600000		600000

Good morning Ltd A/c

To Realisation A/c	315000	By Pref Shares in Good Mor A/c	75000
		By Equity Shares in Good mor	240000
	315000		315000

Preference Share Holders A/c

To Preference Shares in Good Morning Ltd	75000	By Preference Share capital A/c	100000
To Realisation A/c	25000		
	100000		100000

Equity Shares in Good morning Ltd

To Good morning Ltd	240000	By Equity Share Holders A/c	240000
	240000		240000

Preference Shares in Good Morning Ltd

To Good morning Ltd	75000	By Preference Share Holders A	75000
	75000		75000

Journal Entries in the Books of Good morning Ltd.

1	Business Purchase A/c Dr	315000	
	To Liquidator of Bad dream Ltd		315000
	(Being Business Purchased)		
2	Land and Buildings Dr	200000	
	Plant and Equipments Dr	300000	
	Furnitures Dr	65000	
	Patents Dr	45000	
	Sundry Debtors Dr	149450	
	Inventry A/c Dr	68950	
	Cash Dr	3700	
	To Business Purchase A/c		315000
	To Sundry Creditors		100000
	To Debentures		100000
	To Bank Overdraft		240000
	To Capital Reserve		77100
	(Being Sundry Assets and Liabilities taken over recorded)		
3	Liquidator of Bad dream Ltd Dr	315000	
	To Equity Share Capital A/c		240000
	To 7%Preference Share Capital A/c		75000
	(Being Purchase Consideration Discharged.)		
4	Bank A/c Dr	200000	
	To Equity Share Capital A/c		200000
	(Being 20000 Equity shares of Rs 10 each issued for cash.)		
5	Equity Share Call A/c Dr	60000	
	To Equity Share Capital A/c		60000
	(Being call made at Rs 2 per share on 30000 equity shares)		
6	Bank A/c Dr	60000	
	To Equity Share Call A/c		60000
	(Being Call amount received.)		

Balance Sheet of Good Morning Ltd.
as on 30th September, 2014

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholder's Funds			
a. Share Capital	1	5,75,000	

b. Reserves and Surplus	2	77,100	6,52,100
2. Non-Current Liabilities			
Long Term Borrowings			1,00,000
3. Current Liabilities			
Trade Payables			1,00,000
Total			**8,52,100**
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
- Tangible Assets			5,65,000
- Intangible Assets			45,000
2. Current Assets			
a. Cash and cash equivalents		23,700	
b. Trade Receivables		1,49,450	2,42,100
c. Inventory		68,950	
Total			**8,52,100**

Good Morning Ltd.
Notes to Financial Statements for the year ended ______

	As at ___________	
	Number	**Rs**
Note "1" : SHARE CAPITAL		
Authorised Shares		
Equity Shares of `10 each	100000	10,00,000
7% Preference Share	5000	5,00,000
Issued, Subscribed & Fully Paid up Shares		
Equity Shares of `10 each	50000	5,00,000
7% Preference Share	750	75,000
Total	**50,750**	**5,75,000**

Good Morning Ltd.
Notes to Financial Statements for the year ended ______

	As at ___________	
		Rs
Note "2" : RESERVES & SURPLUS Capital Reserves		77,100
Total		**77,100**

Illustration: 3

The following are the Balance Sheets of P Ltd and S Ltd as on 31st March, 2015
Balance Sheet as on 31st March, 2015

Liabilities	P Ltd	S Ltd	Assets	P Ltd	S Ltd
Equity Share Capital (Rs 10 each)	500,000	300,000	Land and Building	250,000	155000
14% Preference Share Capital (Rs 100 each)	220,000	170,000	Plant and Machinery	325,000	170000
General Reserve	50,000	25,000	Furniture and Fittings	57,500	35000
Export Profit Reserve	30,000	30,000	Investments	125,000	95000
Profit and Loss A/c	75,000	50,000	Stock	90,000	103000
13% Debentures	50,000	35,000	Debtors	72,500	52000
Sundry Creditors	65,000	50,000	Cash and Bank	70,000	50000
	990,000	**660,000**		**990,000**	**660000**

P Ltd takes over S Ltd on 1st April, 2015. P Ltd discharges the Purchase Consideration as below:

a) Issued 35000 Equity Shares of Rs 10 each at par to the equity shareholders of S Ltd.

b) Issued 15% Preference Shares of Rs 100 each

to discharge the Preference share holders of S Ltd at 10% premium.

c) The Debentures of S Ltd will be converted into equivalent numbers of debentures of P Ltd.

You are required to give necessary ledger accounts to close the books of S Ltd and Journal entries in t the books of P Ltd and Balance sheet of P Ltd after absorption.

Solution:

Statement of Purchase consideration: (Net Payment method)

a) 35000 equity shares of Rs 10 each		350000
1870 15%Preference Shares of Rs 100 each		187000
(Old Preference Share Capital	170000	
Add : 10%Premium	17000)	
		537000

In the books of S Ltd
Realization A/c

To Land and Buildings	155000	By 13% Debentures	35000
To Plant and Equipments	170000	By Current Liabilities	50000
To Furnitures	35000	By P Ltd	537000
To Investment	95000	By Equity Share holders A/c	55000
To Inventory	103000		
To Sundry Debtors	52000		
To Cash	50000		
To Preference Share holders	17000		
	677000		677000

Equity Shareholders A/c

To Realisation A/c	55000	By Equity Share Capital A/c	300000
To Equity Shares in P Ltd	350000	By General Reserve	25000
		By Profit and Loss A/c	50000
		By Export Profit Rerve	30000
	405000		405000

P Ltd A/c

To Realisation A/c	537000	By Equity Shares in P Ltd	350000
		By Preference Shares in P Ltd	187000
	537000		537000

Preference Share Holders A/c

To Preference Shares in P Ltd	187000	By Preference Share capital A/c	170000
		By Realisation A/c	17000
	187000		187000

Equity Shares in P Ltd

To P Ltd A/c	350000	By Equity Share Holders A/c	350000
	350000		350000

Preference Shares in P Ltd

To P Ltd A/c	187000	By Equity Share Holders A/c	187000
	187000		187000

Journal Entries in the books of P Ltd

Sr.No	Particulars		Dr. Rs.	Cr. Rs.
i.	Business Purchase A/c	Dr.	5,37,000	
	To Liquidator of Q Ltd.			5,37,000
	(Being Business of Q Ltd. Purchased)			
ii.	Building A/c	Dr.	155000	
	Machinery A/c.	Dr.	170000	
	Furniture and Fittings	Dr	35000	
	Investment	Dr	95000	
	Stock	Dr.	103000	
	Debtors	Dr.	52000	
	Cash and Bank A/c.	Dr.	50000	
	To 13 % Debentures			35000
	To Current Liabilities			50000
	To Business Purchase			537000
	To Capital Reserve			38000
	(Being sundry assets & liabilities taken over)			
iv.	Liquidator of P Ltd. A/c	Dr.	1875000	
	To Equity share capital A/c			1250000
	To securities Premium A/c			625000
	(Being Purchase consideration discharge)			
v.	Liquidator of Q Ltd. A/c.	Dr.	537000	
	To Equity Share Capital A/c.			350000
	To 15% Preference Share Capital A/c.			187000
	(Being purchase consideration discharged)			
vi.	Amalgamation Adjustment A/c.	Dr.	30000	
	To Export profit reserve			30000
	(Being statutory reserve maintained)			
vii.	13% Debentures in Q Ltd. A/c.	Dr	35000	
	To 13% Debentures			35000

Balance Sheet as on 31st March, 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholder's Funds			
a.Share Capital	1	12,57,000	
b.Reserves and Surplus	2	2,23,000	14,80,000
2. Non-Current Liabilities			
Long Term Borrowings			85,000
3.Current Liabilities			
Trade Payables			1,15,000
Total			**16,80,000**
ASSETS			
4.Non Current Assets			
a. Fixed Assets			
- Tangible Assets			9,92,500
5. Non Current Investments			2,20,000
6.Current Assets			
a. Cash and cash equivalents		1,20,000	
b. Trade Receivables		1,24,500	
c. Inventory		1,93,000	4,67,500
d. Short Term Current Assets		30,000	
Total			**16,80,000**

Notes to Financial Statements for the year ended _______

	As at ____________	
	Number	**Rs**
Note "1" : SHARE CAPITAL		
Authorised Shares		
Equity Shares of `10 each	85000	8,50,000
14% Preference Share	2200	2,20,000
15% Pref. Shares	1870	1,87,000

Issued, Subscribed & Fully Paid up Shares		
Equity Shares of `10 each	85000	8,50,000
14% Preference Share	2200	2,20,000
15% Pref. Shares	1870	1,87,000
Total	**89,070**	**12,57,000**

Notes to Financial Statements for the year ended ______		
	As at ___________	
		Rs
Note "2" : RESERVES & SURPLUS		
Capital Reserves		38,000
General Reserve		50,000
Export Profit Reserve		60,000
Profit & Loss A/c.		75,000
Total		**2,23,000**

Illustration: 4

The following is the Balance Sheet of Time Pass Ltd as on 30th September, 2014

Balance Sheet as on 30th September, 2014

Liabilities	Rs	Assets	Rs
Issued capital		Land & Buildings	85000
18000 Equity Shares of Rs10	180000	Plant & Equipments	45000
General Reserve	24000	Furnitures	15000
Profit & loss A/C	10400	Trademarks	7000
12% Debentures	80000	Investments	23000
Sundry Creditors	63720	Sundry Debtors	60000
		Stock	112000
		Bank	11120
	358120		**358120**

Time Pass Ltd was absorbed by Busy Ltd., on the following terms and conditions:

All liabilities and all assets are to be taken over except Investments which were sold by Time Pass Ltd. at 90% of book value.

Debentures of Time Pass Ltd, to be discharged at a discount of 10% by the issue of 14% debentures of Rs 100 each in Busy Ltd.

Trademarks were found useless.

Issue of one equity share of Rs 10 each in Busy Ltd., issued at Rs 12 and a cash payment of Rs 3 for every share in Time Pass Ltd.

a) Cost of absorption paid : Rs 1160
b) Time Pass Ltd. sold half the shares received from Busy Ltd. at Rs 15 per share.

You are required to give necessary Ledger A/c s to close the books of Time Pass Ltd. and Journal entries in the books of Busy Ltd.

Solution:

Statement of Purchase consideration: (Net Payment method)

a) 18000 Equity shares of Rs.10 each at Rs.12 per share	216000
b) Cash at Rs. 3 per share on 18000 Equity shares	54000
	270000

Goodwill/Capital reserve (Net Assets taken over)

Land & Buildings	85000	
Plant & Equipments	45000	
Furnitures	15000	
Sundry Debtors	60000	
Stock	112000	
Bank	11120	
		328120
Less :		
Liabilities taken over		
Debentures	80000	
Creditors	63720	143720
Net assets taken over		184400
Less :		
Purchase consideration		270000
Goodwill		85600

In the books of Time Pass Ltd
Realization A/c

To Land & Buildings	85000	By 10% Debentures	80000
To Plant & Equipments	45000	By Sundry Creditors	63720
To Furnitures	15000	By Busy Ltd.	270000
To Trademarks	7000	By Bank (Investment sold)	20700
To Sundry Debtors	60000	By Bank (shares sold)	27000
To Bank	11120		
To Investments	23000		
To Stock	112000		
To Equity Share holders A/c	103300		
	461420		461420

Equity Shareholders A/c

To Bank	209700	By Equity Share Capital A/c	180000
		By Profit and Loss A/c	10400
		By General Reserve	24000
To Equity Shares in Busy Ltd	108000	By Realisation A/c	103300
	317700		317700

Busy td A/c

To Realisation A/c	270000	By Equity Shares in Busy Ltd	216000
		By Bank	54000
	270000		270000

Bank A/c

To Equity shares in busy Ltd	135000		
To Realisation A/c	20700	By Equity Shareholders A/c	209700
To Busy Ltd.	54000		
	209700		209700

Equity Shares in Busy Ltd

To Busy Ltd.	216000	BY Bank	135000
To Realisation A/c	27000	By Equity Share Holders A/c	108000
	243000		243000

Journal Entries in the Books of Busy Ltd.

1	Business Purchase A/c	Dr	270000	
	To Liquidator of Bad dream Ltd			270000
	(Being Business Purchased)			
2	Land and Buildings	Dr	85000	
	Plant and Equipments	Dr	45000	
	Furnitures	Dr	15000	
	Sundry Debtors	Dr	60000	
	Stock		112000	
	Bank		11120	
	Goodwill		77600	
	To Business Purchase A/c			270000
	To Sundry Creditors			63720
	To Debentures			72000
	(Being Sundry Assets and Liabilities taken over recorded)			
3	Liquidator of Time Pass Ltd	Dr	270000	
	To Equity Share Capital A/c			180000
	To Securities Premium A/c			36000
	To Bank			54000
	(Being Purchase Consideration Discharged.)			
4	Goodwill A/c	Dr.	1160	
	To Bank			1160
	(Being amalgamation expenses paid)			
5	Debentures in Time Pass A/c	Dr.	72000	
	To Debentures A/c			72000
	(Being new debentures issued in satisfaction of old Debentures)			

Illustration 5

A Ltd and B Ltd agreed to amalgamate and form a new company C Ltd. which will take over all the assets and liabilities of the two companies.

The assets and liabilities of A Ltd. Are to be taken over at a book value for shares in C Ltd. At the rate of 5 shares in C Ltd. at 10% premium (i.e. Rs 11 per share) for every four shares in A Ltd.

In the case of B Ltd.

a) The debentures of B Ltd. would be paid off by the issue of an equal no. of debentures in C Ltd.

b) The 11.5% Preference Shareholders of B Ltd. would be allotted four 12% Preferences of Rs 100 each in C Ltd. for every five Preference shares in B Ltd.

c) Sufficient shares of C Ltd would be allotted to the equity share holders to cover the balance on their account after adjusting asset values by reducing Plant and Machinery by 10% and providing 5% on sundry debtors.

The summarized Balance Sheets of the two companies just prior to amalgamation were as follows:

12% Debentures		200000	Sundry Debtors	95000	50000
Profit & loss A/C	500000		Bank	65000	40000
Sundry Creditors	75000	90000			
Contingency Reserve	50000				
	1,025,000	**1090000**		**1025000**	**1090000**

Show the Journal entries in the books of both the companies.

Solution:

Statement of Purchase consideration for A Ltd.

5 Equity Shares of Rs 10 each at 10% premium for every four shares in A Ltd.	550000

Statement of Purchase Consideration for B Ltd / Net Assets taken over of A Ltd.

	A Ltd.	B Ltd.
Plant and Equipments	800000	720000
Stock	65000	60000
Sundry Debtors	95000	47500
Bank	65000	40000
	1025000	**867500**
Less: Liabilities taken over		
Debentures		200000
Sundry Creditors	75000	90000
	-75000	**-290000**
Net Assets taken Over	**950000**	**577500**
Less: Purchase Consideration	-550000	
Capital Reserve	400000	
Purchase Consideration		577500

In the books of A Ltd and B Ltd
Realization A/c

To Plant & Equipments A/c	800000	800000	By Debentures A/c		200000
To Stock A/c	65000	60000	By Creditors A/c	75000	90000
To Sundry Debtors A/c	95000	50000	By C Ltd A/c	550000	577500
To Bank A/c	65000	40000	By Preference Shareholders A/c		60000
			By Equity Share holders A/c	400000	22500
	1025000	950000		1025000	950000

C Ltd A/c

To Realisation A/c	550000	577500	By Equity Shares in C Ltd	550000	337500
			By Preference Shares in C Ltd		240000
	550000	577500		550000	577500

Equity Shareholders A/c

To Profit and Loss A/c		140000	By General Reserve A/c	50000	
To Equity Shares in Good Morning Ltd A/c	550000	337500	By Profit and Loss A/c	500000	
To Realisation A/c	400000	22500	By Equity Share Capital A/c	400000	500000
	950000	500000		950000	500000

Preference Share Holders A/c

To Preference Shares in C Ltd		240000	By Preference Share capital A/c		300000
To Realisation A/c		60000			
		300000			300000

Equity Shares in C Ltd

To C Ltd	550000	337500	By Equity Share Holders A/c	550000	377500
	550000	337500		550000	377500

Preference Shares in C Ltd

To C Ltd	240000	By Preference Share Holders A/c	240000
	240000		240000

Journal Entries in the Books of C Ltd.

1	Business Purchase A/c Dr	1127500	
	To Liquidator of A Ltd A/c		550000
	To Liquidator of B Ltd A/c		577500
	(Being Business Purchased)		
2	Plant and Equipments A/c Dr	800000	
	Stock A/c	65000	
	Debtors A/c	95000	
	Bank A/c	65000	
	To Business Purchase A/c		550000
	To Sundry Creditors		75000
	To Capital Reserve A/c		400000
	(Being Sundry Assets and Liabilities taken over recorded)		
3	Plant and Equipments A/c Dr	720000	
	Stock A/c	60000	
	Debtors A/c	47500	
	Bank A/c	40000	
	To Business Purchase A/c		577500
	To Sundry Creditors		90000
	To Debentures		200000
	(Being Sundry Assets and Liabilities taken over recorded)		
4	Liquidator of A Ltd Dr	550000	
	To Equity Share Capital A/c		500000
	To Secuity Premium A/c		50000
	(Being Purchase Consideration Discharged.)		
5	Liquidator of B Ltd Dr	577500	
	To Equity Share Capital A/c		337500
	To Preference Share Capital A/c		240000
	(Being Purchase Consideration Discharged.)		
6	Old Debentures A/c Dr	200000	
	To New Debenture A/c		180000
	To Capital Reserve A/c		20000
	(Being old Debentures settled at 10% discount.)		

Balance Sheet of C Ltd.

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholder's Funds			
a.Share Capital	1	10,77,500	
b. Reserves and Surplus	2	4,70,000	15,47,500
2. Non-Current Liabilities			
Long Term Borrowings			1,80,000
3. Current Liabilities			
Trade Payables			1,65,000
Total			**18,92,500**

ASSETS			
4. Non Current Assets			
a. Fixed Assets			
- Tangible Assets			15,20,000
5. Current Assets			
a. Cash and cash equivalents			
b. Trade Receivables		1,05,000	3,72,500
c. Inventory		1,42,500	
		1,25,000	
Total			**18,92,500**

C Ltd. **Notes to Financial Statements for the year ended ______**		
	As at ___________	
	Number	**Rs**
Note "1" : SHARE CAPITAL		
Authorised Shares		
Equity Shares of `10 each	83750	8,37,500
11.5% Preference Share	2400	2,40,000
Issued, Subscribed & Fully Paid up Shares		
Equity Shares of `10 each		
11.5% Preference Share	83750	8,37,500
	2400	2,40,000
Total	**86150**	**10,77,500**

	Rs
Note "2" : RESERVES & SURPLUS	
Capital Reserves	4,20,000
Security Premium	50,000
Total	**4,70,000**

❖❖❖❖

2

AMALGAMATION OF LIMITED COMPANIES-II

Unit Structure

9.1 Solved problems

9.1 SOLVED PROBLEMS:

Illustration 1

On 31st March, 2015, Thin Ltd. was absorbed by thick Ltd., the latter taking over all the assets and liabilities of the former at book values. The consideration of the business was fixed at Rs 400000 to be discharged by the transferee company in the form of its fully paid equity shares of Rs 10 each, to be distributed among the shareholders of the transferor company, each shareholder getting two shares for every share held in the transferor company. The balance sheet of the two companies as on the 31st March, 2015 stood as under:

Liabilities	Thick Ltd	Thin Ltd	Assets	Thick Ltd	Thin Ltd
Equity Shares of Rs 10 each, fully paid	900000	200000	Plant & Equipments	412000	100000
			Stock	265500	60000
Profit & loss A/C	20502	12900	Cash at Bank	14000	8300
Workmen Compensation Fund	12000	9000	Sundry Debtors	221200	46000
General Reserve	180000	50000	Cash in Hand	869	356
Sundry Creditors	58567	30456	Goodwill	200000	60000
Staff Provident Fund	10200	4000	Prepaid Insurance		700
Provision for taxation	12300	5000	Income Tax Refund claim		6000
			Furniture	80000	30000
	1193569	311356		1193569	311356

Amalgamation expenses amounting to Rs 1000 were paid by Thick ltd. You are required to:

a) Show the necessary ledger accounts in the books of Thin Ltd.,
b) Show the necessary journal entries in the books of thick Ltd., and

c) Prepare the Balance Sheet of Thick Ltd. in vertical form after amalgamation.

Solution:

In the books of Thin Ltd.'s.

Realization A/c

To Goodwill A/c	60000	By Sundry Creditors A/c	30456
To Plant and Machinery A/c	100000	By Staff Provident Fund A/c	4000
To Furniture A/c	30000	By Provision for taxation A/c	5000
To Stock - in - Trade A/c	60000	By Thick Ltd. A/c	400000
To Sundry Debtors A/c	46000		
To Prepaid Insurance A/c	700		
To Income Tax Refund Claim A/c	6000		
To Cash in hand A/c	356		
To Cash at Bank A/c	8300		
To Equity Share holders A/c	128100		
	439456		439456

Equity Shareholders A/c

To Equity Shares in Thick Ltd A/c	400000	By Profit and Loss A/c	12900
		By General Reserve A/c	50000
		By Workmen Compensation Fund A/c	9000
		By Equity Share Capital A/c	200000
		By Realisation A/c	128100
	400000		400000

Thick Ltd A/c

To Realisation A/c	400000	By Equity Shares in Thick Ltd A/c	400000
	400000		400000

Equity Shares in Thick Ltd

To Thick Ltd	400000	By Equity Share Holders A/c	400000
	400000		400000

Journal Entries in the books of Thick Ltd.

1	Business Purchase A/c Dr	400000	
	To Liquidator of Thin Ltd A/c		400000
	(Being Business Purchased)		
2	Plant and Equipments A/c Dr	100000	
	Stock A/c	60000	
	Debtors A/c	46000	
	Goodwill A/c	197100	
	Furniture A/c	30000	
	Prepaid Insurance A/c	700	
	Income Tax Re-fund Claim A/c	6000	
	Cash in hand	356	
	Cash in Bank A/c	8300	
	To Business Purchase A/c		400000
	To Provision for Taxation A/c		5000
	To Staff Provident Fund A/c		4000
	To Sundry Creditors		30456
	To Workmen Compensation Fund A/c		9000
	(Being Sundry Assets and Liabilities taken over recorded)		
3	Liquidator of Thin Ltd A/c Dr	400000	
	To Equity Share Capital A/c		400000
	(Being Purchase Consideration Discharged.)		
4	Goodwill A/c Dr	1000	
	To Bank A/c		1000
	(Being amalgamation Expenses paid.)		

Balance Sheet of Thick ltd

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1		13,00,000
b. Reserves & Surplus			62,402
2. Non Current Liabilities			
Staff Provident fund			14,200
3. Current Liabilities			
Trade Payables		89023	
Other Current Liabilities	2	21000	1,27,323
Short Term Provisions		17300	
Total			**15,03,925**

ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			6,22,000
Intangible			2,60,000
2. Current Assets			
a. Cash and cash equivalents		22525	
b. Trade Receivables		267200	
c. Inventory		325500	6,15,225
3. Other Current Assets			6,700
Total			**15,03,925**

Thin Ltd.

Notes to Financial Statements for the year ended ______

	As at ___________	
	Number	**Rs**
Note "1" : SHARE CAPITAL		
Authorised Shares		
Equity Shares of `10 each	130000	13,00,000
Issued, Subscribed & Fully Paid up Shares		
Equity Shares of `10 each	130000	13,00,000
Total	130000	13,00,000

Thin Ltd.

Notes to Financial Statements for the year ended ______

	As at ___________	
		Rs
Note "2" : OTHER CURRENT LIABILITIES		
Workmen Compensation Fund	21000	21,000

Illustration : 2

On 31st March, 2015, Sky dud Ltd. was absorbed by Hidud Ltd.,

The balance sheet of the two companies as on the 31st March, 2015 stood as under:

Liabilities	Hidud Ltd	Skydud Ltd	Assets	Hidud Ltd	Skydud Ltd.
Equity Shares of Rs 10 each, fully paid	800000	500000	Plant & Equipments	1600000	830000
General Reserve	1000000	360000	Goodwill		20000
Profit & loss A/C		100000	Investments		170000
Loans	400000		Current Assets	1680000	690000
Bills Payable	100000	220000			
Sundry Creditors	460000	420000			
Provision for taxation	520000	110000			
	3280000	1710000		3280000	1710000

For the purpose of absorption the goodwill of Skydud was considered valueless. Plant and Equipments Are to be depreciated by Rs. 40000. The shareholders of Skydud Ltd are to be allotted sufficient number of Equity shares in Hidud Ltd, based on intrinsic value of equity shares of both the companies.

You are required to:

a) Show the necessary ledger accounts in the books of Skydud Ltd.,
b) Show the necessary journal entries in the books of Hijack Ltd., and
c) Prepare the Balance Sheet of Hijack Ltd. after amalgamation.

Solution:

In the books of Skydud Ltd.

Realization A/c

To Goodwill A/c	20000	By Sundry Creditors A/c	420000
To Plant and equipm. A/c	830000	By Bills Payable A/c	220000
To Investments	170000	By Provision for taxation A/c	110000
To Current Assets	690000	By Hidud Ltd. A/c	900000
		By Equity Share holders A/c	60000
	1710000		1710000

Equity Shareholders A/c

To Equity Shares in Hidud Ltd A/c	900000	By Equity Share capital A/c	500000
To Realisation A/c	60000	By General Reserve A/c	360000
		By Capital Reserve A/c	100000
	960000		960000

Hidud Ltd A/c

To Realisation A/c	900000	By Equity Shares in Hidud Ltd A/c	900000
	900000		900000

Equity Shares in Hidud Ltd

To Hidud Ltd	900000	By Equity Share Holders A/c	900000
	900000		900000

Journal Entries in the books of Hidud Ltd.

1	Business Purchase A/c Dr	900000	
	To Liquidator of Skydud Ltd A/c		900000
	(Being Business Purchased)		
2	Plant and Equipments A/c Dr	790000	
	Investments A/c Dr.	170000	
	Current Assets A/c Dr.	690000	
	To Business Purchase A/c		900000
	To Sundry Creditors		420000
	To Provision for Taxation A/c		110000
	To Bills Payable A/c		220000
	(Being Sundry Assets and Liabilities taken over recorded)		
3	Liquidator of Thin Ltd A/c Dr	900000	
	To Equity Share Capital A/c		400000
	To Securities Premium		500000
	(Being Purchase Consideration Discharged.)		

Balance Sheet of Hidud Ltd. as on 1st April 2015
Balance Sheet of Hidud ltd

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1		12,00,000
b. Reserves & Surplus	2		15,00,000
2. Non Current Liabilities			
Long Term Borrowings			--
3. Current Liabilities			
Short Term Borrowings			4,00,000
Trade Payables			12,00,000
Other Current Liabilities			
Short Term Provisions			6,30,000
Total			**49,30,000**

ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			23,90,000
2. Non Current Investments			1,70,000
3. Current Assets			
a. Trade Receivables			23,70,000
Total			**49,30,000**

Hidud Ltd.

Notes to Financial Statements for the year ended ______

	As at ___________	
	Number	**Rs**
Note "1" : SHARE CAPITAL **Authorised ,Issued, Subscribed & Fully Paid up Shares** Equity Shares of `10 each	120000	12,00,000
Total	120000	12,00,000

Hidud Ltd.

Notes to Financial Statements for the year ended ______

	As at ___________	
		Rs
Note "2" : Reserves and Surplus		
General Reserve		10,00,000
Security Premium		5,00,000
		15,00,000

Working Notes:

1.Calculation of Intrinsic Value of Equity shares:

	Hidud Ltd. Rs.		Skydud Ltd. Rs.
Equity share capital	800000		500000
General Reserve	1000000		360000
Profit and Loss A/c			100000
	-----------		----------
	1800000		960000
Less:			
Depreciation of Plant	40000		
Goodwill	20000		60000
	----------	-------	---------
Equity Shareholders Funds	1800000		900000
	------------		---------
Number of Equity shares	80000		50000
Intrinsic value per equity share	22.50		18.00

2. Value of 4 shares of Hidud Ltd. = Value of 5 shares of Skydud Ltd.

3. Purchase consideration Rs. 900000 to be discharged by issue of 40000 Equity shares of Rs. 10 each at a premium of Rs.12.50 per share.

Illustration : 3

Eno Ltd. and Fanta .Ltd. agreed to amalgamate by transferring their undertakings to a new company, Fantino Ltd. formed for that purpose. On the date of transfer, Balance sheets of the two companies as on 31 March 2015 were as under:

Liabilities	**Eno Ltd. (Rs.)**	**Fanta Ltd (Rs.)**	**Assets**	**Eno Ltd. (Rs.)**	**Fanta Ltd. (Rs.)**
Authorized and Issued Capital:			Leasehold premises	60,000	31,000
Ordinary Shares of			Freehold Property	3,000	
			Debtors	18,000	5,000
Rs. 10 each	75,000	25,000	Investments	13,000	3,000
18% Debentures		3,000	Bank	10,000	2,000
Reserve		2,000			
Mortgage Loan (Secured on freehold Property)					
Sundry Creditors	4,000	10,000			
Profit & Loss A/c	20,000	1,000			
	1,04,000	**41,000**		**1,04,000**	**41,000**

The purchase consideration consisted of:

(a) The assumption of the liabilities of the both companies:
(b) The discharge of the Debentures in Fanta Ltd., by the issue of Rs. 3500, 18.5% Debentures in Fantino Ltd.
(c) Issue at a premium of Rs. 5 per share of ordinary shares of Rs. 10 each in Fantino Ltd. for the purpose of transfer, the assets are to be revalued as under:

	Eno Ltd. Rs.	Fanta Ltd. Rs.
Leasehold premises	65,000	35,000
Freehold Property	5,000	
Debtors	17,100	4,500
Investments	14,900	4,000
Goodwill	11,000	4,000

You are required to:

i) Prepare necessary ledger accounts in the books of Eno Ltd.
ii) Pass Journal Entries in the books Fantino Ltd. under Purchase Method.
iii) Indicate the basis on which the shares of Fantino Ltd. will be distributed among the shareholders of Eno Ltd. and Fanta Ltd. respectively

Purchase Consideration:

	Eno. Ltd. Rs.	Fanto Ltd Rs.
Assets taken over:		
Leasehold premises	65,000	
Freehold Property	5,000	35,000
Debtors	17,100	
Investments	14,900	4,500
Goodwill	11,000	4,000
Bank	10,000	2,000
(A)	**1,23,000**	**49,500**
Less: Liabilities taken over:		
Mortgage Loan	5,000	
18% Debentures		3,500
creditors	4,000	10,000
(B)	9,000	13,500
Net Assets	**1,14,000**	**36,000**

No. of Shares	=	1,14,000/15	36,000/15
	=	7,600	2,400
Ratio of distribution	=	7600 : 7500	2400:2500
	=	76:75	24:25

In the books of Eno Ltd.
Realization A/c

	Rs.		Rs.
To Leasehold premises	60,000	By Mortgage Loan	5,000
To Freehold Property	3,000	By Sundry Creditors	4,000
To Debtors	18,000	By Fantino Ltd.-	
To Investments	13,000	(Purchase	1,14,000
To Bank	10,000	Consideration)	
To Equity Shareholders' A/c (Profit on Realization)	19,000		
	1,23,000		**1,23,000**

Fantino Ltd. A/c

	Rs.		Rs.
To Realization A/c	1,14,000	By Equity Shares in Fantino ltd	1,14,000
	1,14,000		**1,14,000**

Equity Shares in Fantino A/c

	Rs.		Rs.
To Fantino Ltd	1,14,000	By Equity Shareholders A/c	1,14,000
	1,14,000		**1,14,000**

Equity Shareholders A/c

	Rs.		Rs.
		By Share Capital	75,000
To Shares in Fantino Ltd. A/c	1,14,000	By Profit and Loss A/c	20,000
		By Realization A/c	19,000
	1,14,000		**1,14,000**

In the Book of Fanta Ltd.
Realization A/c

	Rs.		Rs.
	31,000	By Creditors	
To Leasehold premises	5,000	By 18% Debentures	10,000
To Debtors	3,000	By Fantino Ltd. A/c	
To Investment	2,000	(Purchase Consideration)	3,000
To Bank			
To Equity Shareholders	8,000		36,000
(Profit on Realization)			
	49,000		49,000

Equity Shareholders A/c

	Rs.		Rs.
To Equity Shares in Fantino Ltd.	36,000	By Share Capital A/c	25,000
		By Reserve A/c	2,000
		By Profit and Loss A/c	1,000
		By Realisation A/c	8,000
	36,000		**36,000**

Fantino Ltd. A/c

	Rs.		Rs.
To Realisation A/c	36,000	By Shares in Fantino Ltd.A/c	36,000
	36,000		**36,000**

Equity Shares in Fantino A/c

	Rs.		Rs.
To Fantino Ltd		By Equity Shareholders	36,000
	36,000	A/c	
	36,000		36,000

Illustration: 4

The following are the Balance Sheets of Prabha Ltd. and Surya Ltd. as on 31st March 2015.

Balance Sheet as on 31st March 2015

Liabilities	Prabha Ltd Rs.	Surya Ltd. Rs.	Assets	Prabha Ltd Rs.	Surya Ltd. Rs.
Equity Share			Land & Buildings	50,000	46,500
capital (Rs.10each)	1,00,000	90,000	Plant & Machinery	65,000	51,000
15 % Preference			Furniture & Fittings	11,500	10,500
Share Capital			Investments	25,000	28,500
(Rs, 100 each)	44,000	51,000	stock	18,000	30,900
General Reserve	10,000	7500	Debtors	14,500	15,600
Export Profit			Cash and Bank	14,000	15,000
Reserve	6,000	6,000			
Investment					
Allowance					
Reserve		3,000			
Profit & Loss A/c	15,000	15,000			
13 % Debentures	10,000	10,500			
(Rs. 100 each)					
Current Liabilities	13,000	15,000			
	198,000	198,000		198,000	198,000

Prabha Ltd. takes over Surya: Ltd. on 1st April 2015. Prabha Ltd. discharges the purchase consideration as below:

a) Issued 10,500 equity shares of Rs.10 each at par to the equity shareholders of Surya Ltd.

b) Issued 15% preference shares of Rs.100 each to discharge the preference share holders of Surya Ltd. at 10% premium the debentures of Surya Ltd. will be converted into equivalent no. of debentures of Prabha Ltd.

The Statutory reserves of Surya Lts. (export profit Reserve and investment allowance reserve are to be maintain for 3 more years.)

Debtors of Prabha Ltd. include Rs.5000 due from Surya Ltd.

You are required to prepare necessary ledger accounts in the books of Surya Ltd. and the Balance Sheet of Prabha Ltd. after absorption

Solution: In The books of Surya Ltd.

Realization Account

To land & building	46,500	By 13% Debentures	10,500
To plant & Machinery	51,000	By current Liabilities	15,000
To furniture	10,500	By Prabha Ltd.	1,61,100
To Investment	28,500	By Equity share holders	16,500
To stock	30,900		
	15,600		
	15,000		
	5,100		
	203,100		203,100

Equity Share holder A/c

To Equity shares in Prabha Ltd.	105,000	By Equity share Capital	90,000
		By General Reserve	7,500
		By Export profit Reserve	6,000
To Realisation A/c	16,500	By Investment allowence reserve	3,000
		By Profit & Loss A/c	15,000
	1,21,500		1,21,500

Preference Shareholders A/c

To prefernce shares in prabha Ltd.	56,100	By preference Share Capital	51,000
		By Realisation	5,100
	56,100		56,100

Prabha Ltd. A/c

To Realisation A/c	1,61,100	By Equity shares in Prbha Ltd	1,05,000
		By preference shares in Prabha Ltd.	56,100
	1,61,100		1,61,100

Equity shares in Prabha Ltd.

To Prabha Ltd	1,05,000	By Equity share holders	1,05,000
	1,05,000		**1,05,000**

Preference shares in Prabha Ltd.

To Prabha Ltd	56,100	By Preference share holders	56100
	56100		56100

Statement of purchase consideration (Net Payment Method)

1. 10,500 Equity shares of Rs. 10 each		1,05000
2. To Preference shareholders	51000	
10% premium	5100	56100
		161100

i.e. 561 preference shares of Rs. 100 each

Prabha Ltd.

Balance Sheet as on 31st March 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1		3,05,100
b. Reserves & Surplus			51,400
2. Non Current Liabilities			
Long Term Borrowing			
13% Debentures			20,500
3. Current Liabilities			
Trade Payables			23,000
Total			**4,00,000**
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			2,34,500
2. Non Current Investments			53,500
2. Current Assets			
a. Cash and cash equivalents		29,000	
b. Trade Receivables		25,100	
c. Inventory		48,900	
d. Other Current Assets		9,000	1,12,000
Total			**4,00,000**

Prabha Ltd. Notes to Financial Statements for the year ended ______		
	As at ___________	
	Number	Rs
Note "1" : SHARE CAPITAL		
Authorised Shares		
Equity Shares of `10 each		
15% Preference Share of Rs.100 each		
Issued, Subscribed & Fully Paid up Shares		
Equity Shares of `10 each		
15% Preference Shares of Rs.100 each	20,500	2,05,000
	1,001	1,00,100
Total	**21,501**	**3,05,100**

Calculation of capital reserve on amalgamation

		Rs.
Assets of Surya Ltd. Taken over		1,98,000
Loss: 13 % Debentures	10,500	
Current Liabilities	15,000	25,500
Net assets taken over		1,72,500
Less: Purchase Consideration		1,61,100
Capital Reserve		**11,400**

Illustration: 5

The Balance sheets of Alpha Ltd. and beets Ltd. as on 31st March, 2015 were as Follow

Liabilities	Alpha Ltd. Rs.	Beeta Ltd. Rs.	Assets	Alpha Ltd. Rs.	Beeta Ltd. Rs.
Equity Share Capital			Building	4,00,00	70000
(Rs.10 Each)	8,00,000	3,00,000	Machinery	4,00,000	150000
Export profit reserve	2,00,000	30000	Debtors	6,00,000	2,00,000
Profit & Loss A/c	2,65,000	2,37,000	Cash at Bank	2,50,000	37000
12%Debetores	5,00,000	3,00,000	Preliminary	50,000	20,000
(Rs. 100 each)			expenses		
	1,12,000	63000			
Bills payable	23,000	70,000			
	2200,000	**12,50,000**		**2200,000**	**12,50,000**

A new company Zinta Ltd. was formed to acquire all the assets and liabilities of Alpha Ltd. and Beeta Ltd.

a) Zinta Ltd. to have an authorized capital of Rs. 25,00,000 divided in 2,50,000 shares of Rs.10 each

b) Business of both the companies taken over for a total price of rs.30 Lakh to be discharged by Zinta Ltd. by issue of equity Shares of Rs. 10 each at a premium of 50%

c) The shareholders of Alpha Ltd. and Beeta Ltd. to get shares in Zinta Ltd. in the ratio of net asset valuation of their respective business.

d) The debentures of both the companies to be converted into equivalent number of 14 % Debentures in Zinta Ltd.

e) Export Profit reserve is to be maintained for two more years

f) The assets of the companies to be revalued at

	Alpha Ltd.	**Beeta Ltd.**
Building	10,00,000	11,50,000
Debtors	3,00,000	1,13,000

g) Liquidation expenses of Alpha Ltd & Beeta Ltd. amounting to Rs. 20,000 were paid by Zinta Ltd. you are required to give Journal Entries in the books of Zinta Ltd. and also prepare Balance sheet of Zinta Ltd. after amalgamation

1. Statement of purchase consideration total purchase consideration
   Lakh equity shares of Rs. 10 each issued
   At Rs.15 each 30,00,000
2. Statement of Net Assets

Building	10,00,000	1150,000
Machinery	3,00,000	1,13,000
Stock	5,00,000	1,43,000
Debtors	6,00,000	2,00,000
Cash at bank	2,50,000	37,000
	26,50,000	1643000
Less: Liabilities		
12% Debentures	500,000	300,000
Current Liabilities	1,12,000	63000
Bills Payable	23000	70000
R.D.D	1500	10000
	6,50,000	4,43,000
Net Assets	20,00,000	12,00,000

No. of shares to issued

Alpha Ltd. $\frac{200000}{3200000}$ X 2000000 = 125000 Shares

Beeta Ltd. $\frac{200000}{3200000}$ X 1200000 = 75000 Shares

Journal of Zinta Ltd.

Sr.No	Particulars	Dr. Rs.	Cr. Rs.
i.	Business Purchase A/c Dr.	3000000	
	To Liquidator of Alpha Ltd.		1875000
	To Liquidator of Beeta Ltd.		1125000
	(Being Business of Alpha Ltd. & Beeta Ltd. Purchase)		
ii.	Building A/c Dr.	1000000	
	Machinery A/c. Dr.	300000	
	Stock Dr.	500000	
	Debtors Dr.	600000	
	Cash and Bank A/c. Dr.	250000	
	To 12 % Debentures		500000
	To Sundry Creditors		112000
	To Bills Payable		23000
	To R.D.D.		15000
	To Business Purchase		1875000
	To Capital Reserve		125000
	(Being sundry assets & liabilities taken over of (Alpha Ltd. Recordable)		
iii.	Building A/c	1150000	
	Machinery A/c	113000	
	Stock A/c	143000	
	Debtors A/c.	200000	
	Cash and bank A/c	37000	
	To 12% Debentures		300000
	To Sundry Creditors		63000
	To Bills Payable		70000
	To R.D.D		10000
	To Business Purchase		1125000
	To Capital Reserve		75000
	(Being Sundry assets & liabilities taken over to Beeta Ltd. recorded)		

iv.	Liquidator of Alpha Ltd. A/c Dr. To Equity share capital A/c To securities Premium A/c (Being Purchase consideration discharge)	1875000	 1250000 625000
v.	Liquidator of Beeta Ltd. A/c. Dr. To Equity share Capital A/c. To Securities premium A/c. (Being purchase consideration discharge)	1125000	 750000 375000
vi.	Amalgamation Adjustment A/c. Dr. To Export profit reserve (Being statutory reserve maintained)	230000	 230000
vii.	12% Debentures in Alpha Ltd. A/c. Dr. 12% Debentures in Beeta Ltd. A/c. Dr To 14% Debentures	5,00,000 3,00,000	 800000
viii.	Capital Reserve A/c. Dr. To Bank A/c. (Being liquidation expenses of Alpha Ltd. and Beeta Ltd. Paid)	20000	 20000

Balance sheet of Zinta Ltd. as on 1st April 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1		20,00,000
b. Reserves & Surplus			14,10,000
2. Non Current Liabilities			
Long Term Borrowing			
14 % Debentures			80,000
3. Current Liabilities			
Trade Payables			268,000
Total			**44,78,000**
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			25,63,000
2. Current Assets			
a. Cash and cash equivalents		2,67000	
b. Trade Receivables		7,75,000	
c. Inventory		6,43,000	
d. Other Current Assets		2,30,000	
			19,15,000
Total			**44,78,000**

Zinta Ltd. Notes to Financial Statements for the year ended ______		
	As at ___________	
	Number	Rs
Note "1" : SHARE CAPITAL		
Authorised Shares		
Equity Shares of `10 each	2,50,000	**25,00,000**
Issued, Subscribed & Fully Paid up Shares		
Equity Shares of `10 each	2,00,000	20,00,000
Total	**2,00,000**	**20,00,000**

Zinta Ltd. Notes to Financial Statements for the year ended ______		
	As at ___________	
		Rs
Note "2" : Reserves and Surplus		
Capital Reserve		10,00,000
Security Premium		1,80,000
Export Profit Reserve		2,30,000
		14,10,000

Illustration No.6

The Balance sheet of Priti Ltd. as on 31st March 2015 was as follows:

Liabilities	Rs.	Assets	Rs.
Capital :		Goodwill	40,000
50,000 Equity Shares of		Plant and Machinery	3,00,000
Rs. 10 each fully paid	5,00,000	Stocks	1,60,000
20000 6 % Cumulative Preference Shares of Rs. 10 each fully paid	2,00,000	Sundry Debtors	2,40,000
5% Debentures of Rs.100 each	1,00,000	Cash at Bank	17,800
Bank Overdraft	40,000	Profit & Loss A/c.	2,80,200
Bills payable	28,000	Preliminary Expenses	10,000
Sundry Creditors	1,83,000	Commission & Brokerage on issue of Shares	8,000
Interest Accrued on Debentures	5,000		
	10,56,000		10,56,000

The Following scheme of reconstration was approved by all the concern parties and Sanctioned by the court.

1. The Company to go in liquidation and a new company, Priya Ltd, with an authorized Capital of Rs. 5,00,000 be formed to

take over the business of Priti Ltd

2. Preferential creditors of Rs. 33000 included in the above balance sheet are to be paid in full.
3. Balance creditors to receive 60% of their claim in cash.
4. Preference shareholders to receive 5000 equity shares of Rs. 10 each at par in full satisfaction their claim
5. Equity share holders to allotted one share of Rs.10 each, credited as Rs. 4 paid up for every share held by them. They have also agreed to pay the balance Rs.6/- share immediately
6. Debentures holders to receive equal no of 12 % debentures of Rs.75 each in the new company. Interest due to them being waived.
7. Reconstruction Cost amounting to Rs.10000 paid by Priya L
8. Your required to give necessary ledger accounts in the books of Priti Ltd. and Balance sheet of Priya Ltd. After reconstructions.

Solution: 1. Purchase consideration(net payment Method)

To Preference share holders 5000 equity shares of Rs. 10 each fully paid	50,000
To Equity share holders 50000 equity shares Rs. 4 paid up	2,00,000
Total Purchase consideration	**2,50,000**

2.Goodwill/ Capital reserve

Assets taken over		
Plant & machinery	3,00,000	
Stock	1,60,000	
Debtors	2,40,000	
Cash Bank	17,800	
		7,17,800
Less liabilities taken over		
Debentures	75,000	
Bank overdraft	40,000	
Bills payable	28,000	
Creditors	1,23,000	
		2,66,000
Net assets taken over		4,51,800
Purchase consideration		2,50,000
Capital reserve		**2,01,800**

In the books of Priti Ltd.
Realisation Account

To Goodwill	40000	By debentures	100000
To Plant & Machinery	300000	By bank over draft	40000
To Stock	160000	By bills payable	28000
To Debentures	240000	By creditors	1,83000
To cash Bank	17800	By interest on debenture	5000
		By Priya Ltd.	250000
		By preference share holders	150000
		By Equity share holders	1800
	757800		**757800**

Equity shareholders account

To profit & loss A/c	280200	By equity share capital	500000
To Preliminary expences	10000		
To share issue expence	8000		
To Realisation A/c	1800		
To Equity share in Priya Ltd.	200000		
	500000		**500000**

Preference shareholders account

To Equity shares in Priya Ltd.	50000	By preference Capital	200000
To realization A/c	150000		
	200000		**200000**

Priya Ltd. A/c

To Realisation A/c	250000	By Equity shares in Priya Ltd	250000
	250000		**250000**

Equity share in Priya Ltd A/c

To Priya Ltd.	250000	By Equity share holders A/c	200000
		By Preference shareholders A/c	50000
	250000		**250000**

Journal Entries in the books of Priya Ltd.

Sr.No.	Particulars	Dr. Rs.	Cr. Rs.
1	Business purchase A/c. Dr.	250000	
	To Liquidator of Priti Ltd.		250000
	(Being business purchase recorded)		

2	Plant and Machinery A/c. Dr.	300000	
	Stock A/c. Dr.	160000	
	Debtors A/c. Dr.	240000	
	Cash Bank A/c. Dr.	17800	
	To Debentures A/c.		75000
	To Bank Overdraft A/c.		40000
	To Bills payable		28000
	To Creditors		123000
	To Business purchase		250000
	To Capital Reserve		201800
	(Being sundry assets and liabilities taken over recorded)		
3	Liquidator of Priti Ltd. A/c. Dr.	250000	
	To Equity Share Capital(fully paid)		50000
	To Equity Share Capital (partly paid)		200000
	(Being purchase consideration discharged.)		
4	Equity Share Call A/c Dr.	300000	
	To Equity Share Capital A/c		300000
	(Being call made on 50000 Equity shares at Rs. 6/ share)		
5	Bank A/c Dr.	300000	
	To Equity Share Call A/c		300000
	(Being Call amount received)		
6	Creditors A/c Dr.	123000	
	To Bank A/c		123000
	(being Creditors Paid)		
7	Debenture holders of Priti Ltd. A/c Dr.	75000	
	To 12% Debentures A/c		75000
	(Being new debentures issued)		
8	Capital reserve A/c Dr.	10000	
	To Bank		10000
	(Being cost of reconstruction paid)		

Balance sheet of Priya Ltd. as on 1st April, 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital			5,50,000

b. Reserves & Surplus			1,91,800
2. Non Current Liabilities			
Long Term Borrowings			
12% Debentures			75,000
3. Current Liabilities			
Trade Payables			28,000
Total			**8,44,800**
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			3,00,000
2. Current Assets			
a. Cash and cash equivalents		144800	
b. Trade Receivables		240000	
c. Inventory		160000	5,44,800
Total			**8,44,800**

Priya Ltd.
Notes to Financial Statements for the year ended _______

	As at ___________	
	Number	**Rs**
Note "1" : SHARE CAPITAL		
Authorised Shares		
Equity Shares of `10 each	1,00,000	**10,00,000**
Issued, Subscribed & Fully Paid up Shares		
Equity Shares of `10 each	55,000	550,000
Total	**55,000**	**5,50,000**

Illustration 7 (Adjustment of rights of shareholders)

Chaitanya Limited is absorbed by New wave limited. Following are the Balance sheets of the above companies as on 31st March 2015

Capital and Liabilities	Chaitanya Ltd. Rs.	New Wave Ltd. Rs.	Assets	Chaitanya Ltd. Rs.	New Wave Ltd. Rs.

Share Capital : Paid up Share Capital : 10,000 Equity Share of Rs. 100 each of 70 paid up	7,00,000	75,00,000	Sundry Assets	20,30,000	98,10,000
1,00,000 Equity Shares of Rs. 100 each Rs 75 per Share paid up	8,50,000	22,00,000	Cash in hand	20,000	2,70,000
Reserve Fund P & L A/c	3,00,000	2,00,000			
Sundry Creditors	2,00,000	1,80,000			
	20,50,000	**1,00,80,000**		**20,50,000**	**1,00,80,000**

It was decided that the holder of every three shares in Chaityanya Limited was to receive five shares in New Wave Limited, plus as much cash as is necessary to adjust the rights of Shareholders of both companies in accordance with the intrinsic value of shares as per respective balance sheets.

Pass the necessary journal entries in the books of New Wave Limited and prepare the balance sheet giving effect to the above scheme of absorption (T.Y.B.com April 1996)

Solution

In the Books of New Wave Ltd.
Calculation of the Intrinsic Value of Shares

Particulars	**Chaitanya Ltd. Rs.**	**New WaveLtd. Rs.**
Sundry Assets	20,30,000	98,10,000
Cash in hand	20,000	2,70,000
Total Assets	20,50,000	1,00,80,000
Less : Sundry Creditors	2,00,000	1,80,000
Net Assets	18,50,000	99,00,000

Intrinsic Value $= \dfrac{\text{Net Assets Available to Equity Shareholders}}{\text{No. of Equity Shares}}$

$= \dfrac{18,50,000}{10,000}$ $= \dfrac{99,00,000}{1,00,000}$

= Rs/ 185/- = Rs. 99/-

Calculation of amount to be paid in cash :

Intrinsic values of 3 shares in Chaitanya Ltd.	185 x 3 =	555
Intrinsic values of 5 shares in New Wave Ltd.	99 x 5=	495
Difference for every 3 shares Payable in Cash		60

Calculation of Purchase Consideration:(Net Payment Method)

1. Shares to be allotted :16,666 Shares x Rs. 99		=	16,49,934
2. Cash	10,000 x Rs. 60	=	2,00,000
3. Cash for Fraction of Shares (0.666 x 99)		=	66
			18,50,000

Journal of New Wave Ltd.
(Purchase Method)

		Debit Rs.	Credit Rs.
Business Purchase A/c	Dr.	18,50,000	
To Liquidators of Chaitanya Ltd. A/c			18,50,000
(Being Purchase Consideration due)			
Sundary Assets	Dr.	20,30,000	
Cash A/c	Dr.	20,000	
To Sundry Creditors A/c			2,00,000
To Business Pruchase A/c			18,50,000
(Being Assets and Liabilities taken over)			
Liquidators of Chaitanya Ltd. A/c	Dr.	18,50,000	
To Equity Share Capital A/c (16,666 x 75)			12,49,950
To Cash A/c			2,00,066
To Securities Permium A/c			3.99,984
(Being the Purchase Consideration settled)			

New Wave Ltd.

Balance Sheet as on 31st March, 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			

1. Shareholders' Funds			
a. Share Capital			87,49,950
b. Reserves & Surplus			27,99,984
3. Current Liabilities			
Trade Payables			3,80,000
Total			1,19,29,934
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			1,18,40,000
2. Current Assets			
a. Cash and cash equivalents			89,934
Total			1,19,29,934

New Wave Ltd.
Notes to Financial Statements for the year ended ______

	As at ___________	
	Number	**Rs**
Note "1" : SHARE CAPITAL		
Authorised Shares		
Equity Shares of `100 each		
Issued, Subscribed & Partly Paid up Shares		
Equity Shares of `100 each, Rs.75 Paid Up	1,16,666	87,49,950
Total	**1,16,666**	**87,49,950**

Illustration 8 (Absorption – Net Payment Method)

Premier Ltd. Agreed to acquire the business of Modern Auto Ltd. as on 31st March,2015. The Balance Sheet of Modern Auto Ltd. as on that date was as under.

Liabilities	Rs.		Assets	Rs.

Share Capital : 6000 Equity Shares of Rs. 10 each fully paid	60,000		Goodwill	10,000
			Building	30,000
			Machinery	34,000
			Stock	16,800
General Reserve	17,000		Book Debts	3,600
Profit and Loss Account	11,000		U.T.I. Bank Account	5,600
6% Debentures	10,000			
Sundry Creditors	2,000			
	1,00,000			**1,00,000**

The Consideration payable by Premier Ltd. was agreed as follows:

a) Cash payment equal to Rs. 2.50 per share in Modern Auto Ltd.

b) Issue of 9,000 Equity shares of Rs. 10 each of Premier Ltd. having as agreed value of Rs. 15 per share.

c) Issue of such an amount of fully paid 8% Debentures of Premier Ltd. at Rs. 96 each as is sufficient to discharge 6% Debentures, of Modern Auto Ltd. at 20% premium.

While computing purchase consideration. Premier Ltd. valued building and machinery at Rs. 60,000 each, stock at Rs. 14,200 and Book debts subject to 5% provision for discount. The cost of liquidation of Modern Auto Ltd. was Rs. 500.

Prepare:

(i) Necessary ledger Accounts in the books of Modern Auto Ltd.

(ii) Journalise the transaction in the books of Premier Ltd. Under Purchase Method

(T.Y.B.Com. 1997)

Solution:

Determination of Purchase Consideration:

To Whom	Amt	Mode of Discharge
Equity Shareholders	15,000	Cash (6,000 Equity Shares @ 2.5)
Equity Shareholders	1,35,000	9,000 equity shares of Rs. 10 each at Rs. 15
	1,50,000	

In the Book of Modern Auto Ltd. Realisation A/c

	Rs.		Rs.

To Sundry Assets : Goodwill 10,000 Building 30,000 Machinery 34,000 Stock 16,800 Debtors 3,600 Bank 5,600	1,00,000	By Creditors	2,000
To Bank (Expenses)	500	By 6% Debentures	10,000
To Equity Shareholders (Profit)	61,500	By Premier Ltd.	1,50,000
	1,62,000		**1,62,000**

Premier Ltd. A/c

	Rs.		Rs.
To Realisation A/c	1,50,000	By Cash	15,000
		By Equity Shares in P. Ltd.	1,35,000
	1,50,000		**1,52,000**

Journal of Premier Ltd.

	Debit Rs.	Credit Rs.
Building A/c Dr.	60,000	
Machinery A/c Dr.	60,000	
Stock A/c Dr.	14,200	
Book Debts A/c Dr.	3,600	
U.T.I. Bank A/c Dr.	5,600	
Goodwill A/c (Balance Figure)	20,780	
To Reserve for Discount on Debtors		180
To Creditors A/c		2,000
To Liquidators of Modern Auto Ltd. A/c		1,50,000
To 6 % Debentures (Modern Auto)		12,000
(Being Assets and Liabilities taken over)		
Liquidator of Moderyn Auto Ltd A/c Dr.	1,50,000	
To Cash A/c		15,000

To Equity Share Capital A/c To Securities Premium A/c (Being discharged Purchase Consideration)		90,000 45,000
6% Debentures (Modern Auto) Dr. Discount on issue of Debentures Dr To 8% Debentures . (Being 8% Debentures issued in settlement of 6% Debentures)	12,000 500	 12,500

Illustration 9 (Purchase Consideration Nil)

The following are the Balance Sheets of Bada Ltd. and Choota Ltd. as on 31.03.2015:

		Bada Ltd. Rs.		Chotta Ltd. Rs
1. Sources of Funds				
Authorised Share Capital		500		25
a) Issued Share Capital				
for Cash fully paid Equity Share of Rs 10/- each or consideration other than cash		100		10
as Bonus share fully paid Equity share of Rs 10/- each out of General Reserve		400		15
		500		25
b) Reserve and Surplus :				
Capital Reserves		100		5
Revenue Reserve		1,900		70
		2,000		75
Owner's Fund		2,500		100
c) Loan Funds :				
Unsecured Debentures		500		100
Total Fund Rs.		3,000		200
d) **Fund Employed in**				
Fixed assets : Cost	600		5	
Less Depreciation	500	100	4	1
2. Investments :				
a) 2.5 Crore Shares of Chotta Ltd. fully paid at cost	20			
b) 1 Crore Unsecured Debentures of Chotta Ltd. of RS 100 each fully paid at cost	98			

c) 1 Crore fully paid Equity Shares of Rs 10/- each of Madhyam Ltd. at cost (Market Value Rs. 30 crores)	____	118	10	10
3. Current Assets , Loans and Advances :				
Current Assets	2,100	____	150	____
Loans and Advances	3,000	____	100	____
	5,100		250	
Less : Current Liabilities	1,500		50	
Provisions	818		15	
	2,318	2,782	65	185
4. Miscellaneous Expenditure to the extent not written of adjusted..	____		____	4
	____	3,000	____	200

On the day Bada Ltd. absorbed Chotta Ltd. taking over all the assets and liabilities. The consideration was Rs. Nil. You are asked to pass the journal entries in the books of Bada Ltd. and prepare the balance sheet of Bada Ltd in vertical form after absorption under purchase method, showing corresponding figures before absorption.

(T.Y.B.Com October 1999)

Solution:

Journal Entries
In the Books of Bada Ltd.

No.		Debit Rs.	Credit Rs.
	Fixed Assets A/c	1	
	Investment A/c	10	
	Current Assets A/c	250	
	To Investments in Shares of Chhota Ltd		20
	To Current Liabilities		65
	To Investment in Debentures of Chhota Ltd.		98
	To Capital Reserve (Balance Figure)		78
	(Being Premises of Chhota Ltd. taken over)		

Bada Ltd
Balance Sheet
(After Absorption)

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1		500
b. Reserves & Surplus	2		2078
2. Current Liabilities			
Short Term Borrowings			
Trades Payable	3		2050
3. Short Term Provisions	4		833
Total			5461
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			101
2. Non Current Investments			10
3. Current Assets			2250
4. Short Term Current Assets			3100
Total			5461

Notes to Accounts

	Rs.	**Rs**	**Rs.**
			500
1. Authorised Share Capital			
a) Issued Share Capital			
for Cash fully paid Equity			
Share of Rs 10/- each	100		
For consideration other than			
cash as Bonus share fully paid			
Equity share of Rs 10/- each	400	500	
out of General Reserve			
2) Reserve and Surplus :			
Capital Reserves			
Revenue Reserve	178		
	1,900	2,078	
3. Current Liabilities			
a) Unsecured Debentures			
b) Current Liabilities		500	
		1550	2050
4. Provisions			
			833
5. Fixed Assets : cost			
Less : Depreciation	601		
6.Investments	500		101
1 crore fully paid Equity Shares of Rs. 10 each of Madhyam Ltd. at cost (Market value Rs. 30 crore)			10

Illustration 10 (Amalgamation – Valuation of Goodwill)

The Balance sheets of Bill Ltd. and Mona Ltd. as on 1st January 2015 were as under.

Liabilities	Bill Ltd Rs.	Mona Ltd Rs.	Assets	Bill Ltd. Rs.	Mona Ltd. Rs.
Equity Capital (of Rs 1/- each full paid)	31,000	33,500	Fixed Assets	45,000	29,000
			Current Assets	25,000	61,000
Profit and Loss A/c	19,000	1,500			
Current Liabilities	20,000	55,000			
	70,000	**90,000**		**70,000**	**90,000**

Oral Ltd. was formed to amalgamate the business of the two companies. The authorized capital of Oral Ltd. being Rs. 1,00,000 divided into Equity Shares of Re 1/- each of which 20,000 shares were issued for each at a premium of 25 paise per share and are fully paid.

The amalgamation took place on 1st January 2002 on the following terms:

a) All the assets and liabilities of Bill Ltd. and Mona Ltd. to be assured by Oral Ltd. for a total consideration of 80,000 shares of Oral Ltd.

b) The Fixed and Current Assets and Liabilities are taken over at book value.

c) Goodwill to be valued on the basis of 2.5 years purchase of past 3 years Average profit after deducting Normal Profit of 10% on Capital employed as on 1st January 2015 of each company

d) The trading profits for the year ending:

	Bill Ltd.	Mona Ltd.
	Rs.	Rs.
31.12.2012	7,050	5,500
31.12.2013	8,800	6,400
31.12.2014	8,900	6,850

e) Ignore taxation

You are required to ascertain and prepare :

a) number of shares to be issued by Oral Ltd. to share holders of Bill Ltd. and Mona Ltd. Stating the ratio thereof to their former holding

b) Balance sheet of Oral Ltd. amalgamation of Bill/Mona Ltd. Under Purchase Method.

(T.Y.B.Com October 1999)

Solution:

Valuation of Goodwill

	Bill Ltd Rs	Mona Ltd. Rs.
1. Capital Employed	50,000	35,000
2. Normal Rate of Return (NRR)	10%	10%
3. Standard Profit	5,000	3,500
4. Average Past Profit	8,250	6,250
5. Super Profit = Average profit – standard profit	3,250	2,750
6. Goodwill = no. of year purchased x Super profit	x 2.5 Yrs	x 2.5 Yrs
	8,125	6,875
Denomination of Purchase Consideration		
Fixed Assets	45,000	29,000
Current Assets	25,000	61,000
Goodwill	8,125	6,875
	78,125	**96,875**
Less : Current Liabilities	(20,000)	(55,000)
	58,125	41,875

Issue Price of One Equity Share in Oral Ltd $\frac{58.125 + 41,875}{80,000}$

= Rs. 1.25

Oral Ltd.
Balance Sheet

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital			1,00,000
b. Reserves & Surplus			25,000
2. Current Liabilities			
Trades Payable			75,000
Total			2,00,000
ASSETS			
1. Non Current Assets			

a. Fixed Assets			
Tangible Assets			74,000
Intangible Assets			15,000
2. Current Assets			
Cash Equivalents			25,000
Trade Receivables			86,000
Total			2,00,000

Oral Ltd. **Notes to Financial Statements for the year ended ______**		
	As at ___________	
	Number	**Rs**
Note "1" : SHARE CAPITAL **Authorised Issued, Subscribed & Fully Paid Shares** Equity Shares of `1 each (of the above 80,000 shares are issued to Vendors of business and consideration other than cash)	1,00,000	1,00,000
Total	**100000**	**1,00,000**

Number of Shares to be issued to Bill Ltd and Mona Ltd by Oral Ltd.

	Bill Ltd.	Mona Ltd
Purchase Consideration	58,125	41,875
Issue Price per Share	1.25	1.25
No. of Shares	= 46,500	33,500

The ratio of Shares in Oral Ltd. to be issued to Shareholders of old Companies

=	$\frac{46,500}{31,000}$	$\frac{33,500}{33,500}$
	1.5 : 1	1 : 1

For every 2 shares in Bill Ltd., new 3 shares in Oral Ltd.

For every one share in Mona Ltd., one new share in Oral Ltd.

Illustration 11 (Dissented Shareholders)
Balance Sheet of useless Ltd. As on 31st March 2015

Liabilities	Rs.	Assets	Rs.
Share Capital 2,500 Equity Shares RS. 100 each fully paid	2,50,000	**Fixed Assets** Land and Building 1,30,000 Plant and	
Sundry Creditors	1,10,000	Machinery 75,000	2,05,000
		Current Assets	
Preferential Creditors	15,000	Stock 50,000 Debtors 57,000 Cash 1,000	1,08,000
		Preliminary Expenses	5,500
		Profit and Loss A/c	56,500
	3,75,000		**3,75,000**

The shareholders of the company resolved to take the company into voluntary liquidation and to form M/s Useful Limited, a new company with an authorized share capital of Rs. 10 lakh to take over the business on the following terms:

a) Preferential creditors of Rs. 15,000 are to be paid in full.

b) Unsecured creditors to receive 50 paise in a rupee in full settlement of their claims or par value of their claim in 7% Debentures of useful limited.

c) 2,500 Equity Shares of RS 100 each Rs. 60 paid to be distributed prorata to existing shareholders.

Five shareholders holding 200 shares dissented and their interest was purchased at Rs 50 per share by an assenting shareholder to whom the shares were transferred Half the unsecured creditors opted to be paid in cash, and the fund for this purpose were procured by calling up the balance of RS. 40 per share. Cost of liquidation amounting to Rs. 3,500 paid by Useful Ltd. as part of purchase consideration.

Journalise the above transaction in the books of Useful Limited and prepare the balance sheet in vertical form thereafter assuming the Plant and Machinery, Stock and Debtors were acquired at their book values and Land and Building is to be taken at Rs. 68000.

(T.Y.B.Com April 2000)

Solution

In the Book of Useful Ltd.
Calculation of Purchase Consideration

To Whom	What	How	Amount Rs.
1. Equity Shareholders	Equity Shares Capital	2,500 x 60	1,50,000

No effect of settlement of dissenting shareholders and transfer to shares in Balance Sheets.

Journal Entries
In the Book of Useful Ltd.

		Rs.	Rs,
1. Business Purchase A/c	Dr	1,50,000	
To Liquidator of Useless Ltd.			1,50,000
(Being taken over business of Useless Ltd)			
2. Land and Building A/c	Dr.	68,000	
Plant and Machinery A/c	Dr.	75,000	
Stock A/c	Dr.	50,000	
Debtors A/c	Dr.	57,000	
Cash A/c	Dr.	1,000	
To Preferential Creditors			15,000
To Unsecured Creditors			27,500
To Unsecured Creditors			55,000
To Business Purchase A/c			1,50,000
To Capital Reserve A/c			3,500
(Being Assets & Liabilities brought into the Books)			
3. Liquidator of Useless Ltd A/c	Dr	1,50,000	1,50,000
To Equity Share Capital A/c			
(Being Purchase Consideration discharged)			
4. Preferential Creditors A/c	Dr.	15,000	
Unsecured Creditors A/c	Dr.	27,500	
To Cash A/c			42,500
(Being Preferential & Unsecured Creditors paid off)			
5. Unsecured Creditors A/c	Dr.	55,000	
To 7% Debentures A/c			55,000
(Being Unsecured Creditors settled on issue of 7% Debentures)			
6. Goodwill A/c	Dr.	3,500	
To Cash A/c			3,500
(Being paid for cost of Liquidation)			

7. Bank A/c Dr. To Equity Share Capital (2,500 x 40) A/c (Being collected a call of Rs. 40 per share)	1,00,000	1,00,000

Useful Ltd.
Balance Sheet as on 31st March 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1		2,50,000
b. Reserves & Surplus	2		3,500
2. Non-Current Liabilities			
Long Term Borrowings	3		55,000
Total			3,08,500
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			1,43,000
Intangible Assets			3,500
2. Current Assets			
Cash Equivalents		55,000	
Trade Receivables		57,000	
Inventories		50,000	1,62,000
Total			3,08,500

Notes to Accounts:

Note 1

Share Capital	Rs.
Authorised :	
10,000 Equity Shares of Rs 100 each	10,00,000
Issued and Subscribed :	
2,500 Equity Shares of RS. 100 Each	2,50,000
	2,50,000

Note 2

Reserve and Surplus	Rs.
Capital Reserve	3,500
	3,500

Note 3

Secured Loans	Rs.
7% Debentures	55,000
	55,000

Working

	Rs.
Cash Balance	1,000
Received From Useless Ltd	1,00,000
Share Capital (2,500 x 40)	1,01,000
Less: Paid on preferential creditors	15,000
Paid to unsecured creditors	27,500
Liquidation Expenses	3,500
Balance	**55,000**

Illustration 12 (External – Reconstruction – Net Payment Method)

The following was the Balance Sheet of DT. Ltd. as on 30th June 2015

Liabilities	Rs.	Assets	Rs.
Share Capital		Goodwill	25,000
2,500 8% Cumulative Preference Shares of Rs. 100 each	2,50,000	Fixed Assets	12,85,000
		Stock	3,03,000
		Debtors	2,50,000
		Bank Balance	7,000
12,000 Equity Shares of Rs 100 each	12,00,000	Preliminary Expenses	25,000
9% Debentures	5,00,000	Profit and Loss A/c	6,00,000
Interest Accrued thereon	45,000		
Creditors	5,00,000		
	24,95,000		**24,95,000**

Note: Preference dividend was in arrears RS. 40,000

The following scheme of Reconstruction is duly sanctioned:

a) A new company TD Ltd. is formed with Rs. 15,00,000 as Authorised share capital divided into 15,00,000 Equity Shares of Rs. 10 each.

b) The Company will acquire DT Ltd. on the following conditions :

i) Old Companies Debentures will be paid by similar debentures in the new company. For the arrears of interest, equivalent amount of equity shares will be issued.

ii) The creditors will be paid for every Rs. 100 for their claim, Rs sixteen cash and ten equity shares in the new company.

iii) Preference shareholders are paid ten Equity shares in the new company for each shares held by them in the old company. They will not press for their dividend arrears.

iv) Equity Shareholders will be given ten equity shares in the new company for three shares held in the old company

v) Expenses of Rs. 20,000 will be borne by the new company, as a part of purchase consideration.

c) The new company will take the current assets at their book value except stock which will be reduced by Rs. 15,000 Intangible, assets are not to appear in the new balance sheet, appropriate adjustment being made in the values of fixed assets

d) Remaining equity shares in the new company are issued to the public and are fully paid.

You are required to prepare :

a) In the book of DT Ltd. (i) Realisation Account (ii) DT Equity Shareholders account

b) In the Book of DT. Ltd. i) Journal Entries (ii) Balance Sheet

Solution

Calculation of Purchase Consideration

	Rs.
To Preference Shareholders: 25,000 Equity Shares of Rs. 10/- each To Equity Shareholders $\frac{10}{3}$x12,000 = 40,000 shares of Rs. 10/- each	 2,50,000 4,00,000 6,50,000

Note: As per AS – 14 expenses are not covered by purchase consideration

	Rs.		Rs.
To Sundry Assets	18,70,000	By Liabilities 9% Debentures Interest on Debentures **Creditors :** By T.D. Ltd. By Equity Shareholders A/c (Loss)	5,00,000 45,000 5,00,000 6,50,000 1,75,000
	18,70,000		**18,70,000**

DT Equity Shareholders A/c

	Rs		Rs.
To Preliminary Expenses	25,000	By Equity Share Capital	12,00,000
To Profit & Loss A/c	6,00,000		
To Realisation (Loss)	1,75,000		
To Equity Shares in TD Ltd.	4,00,000		
	12,00,000		**12,00,000**

Journal of TD. Ltd.

	Dr Rs.	Cr Rs,
1. Business Purchase A/c Dr	6,50,000	
To Liquidator of DT Ltd.		6,50,000
(Being Purchase Consideration Due)		
2. Stock A/c Dr.	2,88,000	
Debetors A/c Dr.	2,50,000	
Bank A/c Dr.	7,000	
Fixed Assets Dr.	12,30,000	
To 9% Debenture A/c		
To Creditors A/c		5,45,000
To Business Purchase A/c		5,80,000
(Being Assets & Liabilities taken over, balance being Fixed Assets)		6,50,000
3. Liquidator of DT.Ltd A/c Dr	6,50,000	
To Equity Share Capital A/c		6,50,000
(Being Purchase Consideration discharged)		

4. Bank A/c Dr. To Equity Share Capital A/c (Being amount received for issue of remaining shae to Public)	3,05,000	 3,05,000
5. 9% Debent holder of DT Ltd A/c Dr. To 9% Debentures A/c To Equity Shares Capital A/c (Being Debentures holder's claim settled)	 5,45,000	 5,00,000 45,000
6. Creditors A/c Dr. To Cash A/c To Equity Share CApital A/c (Being Creditors A/c Settled)	 5,80,000	 80,000 5,00,000
7. Goodwill A/c Dr. To Cash A/c (Being paid for Realisation Expenses)	 20,000	 20,000

TD Ltd.
Balance Sheet As on 1st July, 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital			15,00,000
2. Non- Current Liabilities			
Long Term Borrowings			
9% Debentures			5,00,000
Total			20,00,000
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			12,50,000
2. Current Assets			
Cash Equivalents		2,12,000	
Trade Receivables		2,50,000	
Inventories		2,88,000	7,50,000
Total			20,00,000

Working note:

Cash A/c

	Rs.		Rs
To Sundry Liabilities	7,000	By Goodwill A/c	20,000
		By Creditors :	80,000
To Equity Share Capital	3,05,000	By Balance c/d	2,12,000
	3,12,000		**3,12,000**

Illustration13

The following were the Balance sheets of Amar Ltd and Akbar Ltd as at 31st March 15

Liabilities	Amar Ltd Rs.	Akbar Ltd Rs.	Assets	Amar Ltd. Rs.	Akbar Ltd. Rs.
Equity Share Capital (fully paid share of Rs 10/- each)	15,00,000	6,00,000	Land & Building	8,00,000	
Securities Premium	3,00,000	-	Plant & Machinery	12,00,000	5,00,000
Foreign Projects Reserve	-	31,000	Furnitures, Fixtures and Fittings	2,50,000	1,60,000
General Reserve	9,50,000	3,20,000	Stock in Trade	7,70,000	4,10,000
Profit and Loss A/c	2,87,000	82,500	Sundry Debtors	2,20,000	1,10,000
12% Debentures	-	1,00,000	Cash at Bank	1,00,000	62,000
Bills Payable	12,000	-	Bills Receivable	-	8,000
Sundry Creditors	1,30,000	45,000			
Sundry Provisions	1,61,000	71,500		-	-
	33,40,000	12,50,000		33,40,000	12,50,000

At the bill receivable held by Akbar Ltd. were Amar Lts's acceptances. On 1st April 2015. Amar Ltd. took over Akbar Ltd. in an amalgamation in the nature of merger.

It was agreed that in discharge of consideration for the business, Amar Ltd. would allot three fully paid equity shares of Rs. 10 each at par for every two shares held in Akbar Ltd.

It was also agreed that 12% Debentures in Akbar Ltd. would be converted into 13% Debentures in Amar Ltd. of the same amount and denomination. Expenses of amalgamation amounting to Rs. 1,000 were borne by Amar Ltd.

You are required to

a) Pass Journal entries in the books of Amar Ltd. and

(T.Y.B.Com. March 2003)

Solution :

Purchase Consideration :

	Rs.
Equity Shares in Amar Ltd. $\left(\frac{3}{2} x 60{,}000\right)$ 90,000 Equity Shares of Rs. 10 each	<u>9,00,000</u>
	<u>9,00,000</u>

Journal of Amar Ltd.

	Dr. Rs.	**Dr. Rs**
Business Purchase A/c Dr.	9,00,000	
To Liquidator of Akbar Ltd.		9,00,000
(Being Pruchase of Akbar Ltd.)		
Plant and Machinery A/c Dr.	5,00,000	
Furniture, Fixtures & Fittings A/c Dr.	1,60,000	
Stock in Trade A/c Dr.	4,10,000	
Sundry Debtors A/c Dr.	1,10,000	
Cash at Bank A/c Dr.	62,000	
Bills Receivable A/c Dr.	8,000	
To Foreign Project Reserve A/c		31,000
To General Reserve A/c (Balance Figure)		20,000
To Profit & Loss A/c		82,500
To 12% Debentures A/c		1,00,000
To Sundry Creditors A/c		45,000
To Sundry Provisions A/c		71,500
To Business Purchase A/c		9,00,000
(Being brought into books the Assets and Liabilities taken over)		
Liquidator of Akbar Ltd. A/c	9,00,000	
To Equity Share Capital A/c Dr.		9,00,000
(Being issued 90,000 Equity Shares of Rs. 10 each in Settlement of Purchase Consideration)		

Bills Payable A/c Dr. To Bills Receivable A/c (Being inter company Bills Receivable adjusted)	8,000	 8,000
12% Debentures A/c Dr. To 13% Debentures A/c (Being 12% Debentures in Akbar Ltd. converted into 13% Debentures)	1,00,000	 1,00,000
General Reserve A/c Dr. To Bank A/c (Being paid for expenses of amalgamation)	1,000	 1,000

Illustration 14

On 31st March 2015, B Ltd. was absorbed by A Ltd. the latter taking over all the assets and liabilities of the former at book values. The consideration for the business was fixed at Rs. 80,000 to be discharged by the transfer company in the form of its fully paid equity shares of Rs. 10 each, to be distributed among the shareholders of the transferor company, each shareholder getting two shares for every share held in the transferor company.

The Balance sheet of the two companies as at 31st March 2015 were as under:

Balance Sheets on 31st March 2015

Liabilities	A Ltd Rs.	B Ltd Rs.	Assets	A Ltd. Rs.	B Ltd. Rs.
Share Capital:			Goodwill	40,000	12,000
Authorised	3,00,000	1,00,000	Plant & Machinery	82,400	20,000
Issued and Subscribed Equity Shares of Rs. 10 each fully paid up	1,80,000	40,000	Furniture Stock in Trade Sundry Debtors Prepaid Insurance	16,000 53,100 44,240 -	6,000 12,000 9,200 140
General Reserve	36,000	10,000			
Profit & Loss A/c	4,100	2,580	Income Tax Refund Claim	-	1,200
Sundry Creditors	14,114	7,890	Cash in Hand	174	70
Bills Payable	2,040	800	Cash in Bank	2,8000	1,660
Provision for	2,460	1,000			
	2,38,714	**62,270**		**2,38,714**	**62,270**

Amalgamation expenses amounting to Rs. 200 were paid by A Ltd. You are required to:

1. Show the necessary Journal Entries in the book of A Ltd. assuming amalgamation in the nature of merger and prepare the balance Sheet of A Ltd. after the amalgamation

(T.Y.B.Com. Oct 2003)

Date	Particulars	L.F.	Dr. Rs.	Cr. Rs
1	Business Purchase A/c Dr.		90,000	
	To Liquidators of B Ltd. A/c			90,000
	(Being purchased business)			
2	Goodwill A/c Dr.		12,000	
	Plant & Machinery A/c Dr.		20,000	
	Furniture A/c Dr.		6,000	
	Stock in Trade A/c Dr.		12,000	
	Sundry Debtors A/c Dr.		9,200	
	Prepaid Insurance A/c Dr.		140	
	Income Tax Refund Claim A/c Dr.		1,200	
	Cash in Hand A/c Dr.		70	
	Cash in Bank A/c Dr.		1,660	
	General Reserve A/c Dr.		27,420	
	To Sundry Creditors A/c			7,890
	To Bills Payable A/c			800
	To Provision for Taxation			1,000
	To Business Purchase A/c			80,000
	(Being Assets and Liabilities taken over)			
3	Liquidator of B Ltd. A/c Dr		80,000	
	To Equity Share Capital A/c			80,000
	(Being settled purchase consideration)			
4.	General Reserve A/c Dr.		200	
	To Bank A/c			200
	(Being paid for expenses)			

Balance Sheet of A Ltd. as at 31st March, 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1	2,60,000	
b.Reserves & surplus		12,480	2,72,480
2. Current Liabilities			24,844
3.Short Term Provisons			3,460
Total			**3,00,784**
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			1,24,400
Intangible Assets			52,000
2. Current Assets			
Trade Receivables		53,440	
Inventories		65,100	
Cash and cash equivalents		4,504	1,23,044
3.Other current Assets			1,340
Total			**3,00,784**

Notes to Accounts

	Rs.
1. Authorised 3000 Equity Shares of Rs. 10 each fully paid	**3,00,000**
Issued and Subscribed : 26,000 Equity Shares of Rs. 10 each fully paid up (Out of the above 8,000 for consideration Equity Shares of Rs 10 each fully paid up have been issued other than cash)	2,60,000

Working Notes:

		Rs.
1.	Statement of Purchase Consideration:	
	8,000 Equity Shares of A Ltd. at RS. 10 at par	80,000
2.	General Reserve:	
	Equity Shares Capital of A Ltd.	40,000
	General Reserve	10,000
	Profit and Loss A/c	2,580
	Net Assets Taken over	52,580

Less : Amalgamation Expenses	80,000
∴ General Reserve	27,420
Less : Amalgamation Expenses	200
General Reserve of A Ltd.	27,620

3.

General Reserve of B Ltd	36,000
Add : General Reserve of A Ltd.	27,620
Balance c/f	8,380

Illustration 15 (Issue of Shares in fraction, unrealised profit in stock)

Following are the balance sheets of Galaxy Ltd. and Gemini Ltd., as on 31st March 2015

Balance Sheet
As on 31st March 2015

Liabilities	A Ltd Rs.	B Ltd Rs.	Assets	A Ltd. Rs.	B Ltd. Rs.
Share Capital:			Fixed Assets	60,000	1,25,000
(Rs. 10 each)			Loan to Gemini	5,000	-
Reserve Fund	50,000	1,00,000	Ltd.		
Foreign	20,000	30,000	Debtors	15,000	10,000
projects			Stock	10,000	15,000
Reserve	5,000	-	Cash at Bank	-	5,000
Creditors	15,000	20,000			
Loan from	-	5,000			
Galaxy Ltd.					
	90,000	**1,55,000**		**90,000**	**1,55,000**

Gemini Ltd. agreed to absorb Galaxy Ltd. on the following terms:

Gemini Ltd. shall give one share of Rs. 10 each at RS 35 per share for every 3 shares held in Galaxy Ltd. the amount for the fraction of shares shall be paid in cash calculated as per the market price of the share of Gemini Ltd.

Stock of Galaxy Ltd. includes goods worth Rs. 7,500 purchased from Gemini Ltd. which has a profit margin of 20% on cost.

Debtors of Gemini Ltd. includes Rs. 2,500 being amount due from Galaxy Ltd. but the Creditors of Galaxy Ltd. include Rs. 2,000 only being the amount due to Gemini Ltd.

The Difference between the Debtors and Creditors is due to cash in transit.

The shares of Gemini Ltd. are quoted in the market at Rs. 45 per share.

You are requested to pass the journal Entries in the books of Gemini Ltd. and the Balance Sheet after the absorption, assuming that the Foreign Projects Reserve is still to be maintained for 3 years.

Assume that the amalgamation is in the nature of Purchase.
(T.Y.B.Com April 2004)

Solution:

Purchase Consideration

Rs.

One Share in Gemini Ltd. for every 3 shares of Galaxy Ltd.

$\frac{5,000}{3}$ = 1,666 Equity Shares of Rs. 10 each @ Rs. 35 each full paid up 58,310 Cash – 0.67 share x Market value of share of Gemini Ltd (Rs 45) 30

Purchase Consideration **58,340**

Journal of Gemini Ltd.
(Amalgamation is in the nature of purchase)

	Dr. Rs.	Dr. Rs
Business Purchase A/c Dr. To Liquidator of Galaxy Ltd. A/c *(Being business of Galaxy Ltd. taken over)*	58,340	 58,340
Fixed Assets A/c Dr. Loan to Gemini Ltd. A/c Dr. Debtors A/c Dr. Stock A/c Dr. To Creditors A/c To Business Purchse A/c To Capital Reserve A/c (Bal Figure) (Being various assets and liabilities of Galaxy Ltd. taken over at agreed values)	60,000 5,000 15,000 10,000	 15,000 58,340 16,660
Liquidator of Galaxy Ltd. A/c Dr. To Equity Share Capital A/c (1.666 x 10)	 58,340	 16,660

To Securities Premium A/c (1.666 x 25) To Cash/Bank A/c (Being Payment to purchase Consideration to liquidators of Galaxy Ltd.)		 41,650 30
Goodwill A/c Dr. To Stock Reserve A/c (Being profit element in stock of Galaxy Ltd)	1,250	 1,250
Loan from Galaxy Ltd A/c Dr. To Loan to Gemini LTd A/c (Being inter – company loan set off)	5000	 5,000
Creditors A/c Dr. Cash to Transit A/c Dr. To Debtors Bank A/c (Being inter – company debts set off)	2,000 500	 2,500
Amalgamation Adjustment A/c Dr. To Foreign Projects Reserve A/c (Being Foreign Projects Reserve maintained	5,000	 5,000

Balance Sheet of Gemini Ltd.
As at 31st March 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1	1,16,660	
b.Reserves & surplus		93,310	2,09,970
2. Current Liabilities			33,000
Total			**2,42,970**
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			1,85,000
Intangible Asset			1,250
2. Current Assets		22,500	
Trade Receivables		23,750	
Inventories		4,970	
Cash and cash equivalents		5,500	56,720
3.Other Current Assets			
Total			**2,42,970**

Notes to Accounts

	Rs.

1. Authorised Issued and Subscribed 11,666 Equity Shares of Rs. 10 each fully paid up (of the above, 1,666 share have been Issued for consideration other than cash)	**1,16,660**

Illustration 16 (Statutory Reserve to be maintained)

The Following is the Balance Sheet of Vikrant Ltd.

Liabilities	Rs.	Assets	Rs.
Issued and Paid up Equity Share Capital	5,00,000	Intangible Assets	50,000
		Fixed Assets	4,20,000
		Current Assets	1,10,000
Statutory Reserve (to be maintained for 3 more years)	10,000	Profit and Loss A/c	80,000
Debentures	1,00,000		
Creditors	50,000		
	6,60,000		**6,60,000**

Virat Ltd. agreed to absorb Vikrant Ltd. on the following terms:

1. Virat Ltd. agreed to take over all the assets and liabilities
2. The assets of Vikrant Ltd. are to be considered to be worth Rs. 5,00,000
3. The Purchase price is to be paid one – quarter in ash and the balance in shares which are issued at the market price.
4. Liquidation expenses amounted to Rs. 300 agreed to be paid by Vikrant Ltd.
5. Market value of shares of RS. 10 each of Virat Ltd. is Rs. 12 per share.
6. Debentures of Vikrant Ltd. were paid.
7. The amalgamation is in the nature of purchase

You are required to show:

a) Purchase consideration

b) Ledger accounts in the books of Vikrant Ltd.

c) Opening entries in the book of Virat Ltd.

(T.Y.B.Com Oct 2004)

Solution:

Purchase Consideration

	Rs.
Market value of assets taken over	5,00,000

Less: Liabilities taken over	50,000	
Debentures	1,00,000	1,50,000
		3,50,000

Discharge of Purchase Consideration:

	Rs.
In Cash $\frac{1}{4}$ x Rs. 3,50,000	87,500
In Shares $\frac{3}{4}$ x Rs. 3,50,000	2,62,500
	3,50,000

In the Book of Vikrant LTd.
Realisation A/c

Dr. **Cr.**

Liabilities	Rs.	Assets	Rs.
To Intangible Assets A/c	50,000	By Debentures A/c	1,00,000
		By Creditors A/c	50,000
To Fixed Assets A/c	4,20,000	By Virat Ltd. A/c (Purchase Price)	3,50,000
To Current Assets A/c	1,10,000	By Shareholders A/c (Loss on Realisation)	80,300
To Bank A/c (Expenses)	300		
	5,80,300		**5,80,300**

Equity Shareholders A/c

Dr. **Cr.**

	Rs		Rs
To Realisation A/c	80,300	By Share Capital A/c	5,00,000
To Profit and Loss A/c	80,000	By Statutory Reserve A/c	10,000
To Bank A/c	87,200		
To Equity Shares in Virat Ltd	2,62,500		
	5,10,000		**5,10,000**

Virat Ltd A/c

Dr. **Cr.**

	Rs		Rs

To Realisation A/c	3,50,000	By Bank A/c	87,500
		By Equity Share in Virat	2,62,500
	3,50,000		**3,50,000**

Bank A/c

Dr. **Cr.**

	Rs.		Rs.
To Virat Ltd. A/c	87,500	By Realisation A/c	300
		By Shareholders A/c	87,200
	87,500		87,500

Equity Share in Virat Ltd. A/c

Dr. **Cr.**

	Rs.		Rs.
To Virat Ltd. A/c	2,62,500	By Equity Shareholders A/c	2,62,500
	2,62,500		**2,62,500**

Journal of Virat Ltd.

Date	Particulars	L.F.	Dr. Rs.	Cr. Rs
1	Business Purchase A/c Dr.		3,50,000	
	To Liquidators of Vikarant Ltd. A/c			3,50,000
	(Being purchased business of Vikrant Ltd)			
2	Sundry Assets A/c Dr.		5,00,000	
	To Trade Creditors A/c			50,000
	To Debentures A/c			1,00,000
	To Business Purchase A/c			3,50,000
	(Being Assets and Liabilities taken over)			
3	Liquidator of Vikran Ltd. A/c Dr		3,50,000	
	To Share Capital A/c			2,18,750
	To Securities Premium A/c			43,750
	To Bank A/c			87,500
	(Being purchase consideration settled)			
4.	Amalgamation Adjustment A/c Dr.		10,000	
	To Statutory Reserve A/c			10,000

	(Being statutory reserve maintained)			
5	Debentures A/c Dr. To Bank A/c (Being payment to debenture holders of Vikrant Ltd.)		1,00,000	1,00,000

Working Notes:

Number of shares to be issued to Vikrant Ltd.
Amount to be paid in form of equity share capital Rs. 2,62,500
Agreed value of one equity Share Rs. 12

Number of equity shares to be issued = $\frac{2,62,500}{12}$ i.e. 21,875 shares

Share Capital = 21,875 x 10
= 2,18,750
Securities Provision = 21,875 x 2
= 43,750

Illustration 17

The following are the Balance sheets as on 31.12.2014 of Nisha Ltd. and Usha Ltd.

Liabilities	A Ltd Rs.	B Ltd Rs.	Assets	A Ltd. Rs.	B Ltd. Rs.
Equity Share Capital: (Rs. 10 per share)	2,00,000	1,20,000	Land & Building	70,000	-
15% Debentures	40,000	-	Plant and Machinery	2,20,000	1,00,000
Reserve Fund	76,000	5,000	Stock	35,000	18,000
Employee's Provident Fund	6,000	-	Debtors	25,000	16,000
Sundry Creditors	30,000	16,000	Bank	6,000	2,000
Profit & Loss A/c	4,000	-	Misc Exp.not W/o	-	-
			Advertisement Expenses		5,000
	3,56,000	**1,41,000**		**3,56,000**	**1,41,000**

The two companies agreed to amalgamation and form a new company M/s Ujala Ltd/ which takes over the assets and liabilities of both the companies.

The authorized capital of Ujala Ltd. is Rs. 20,00,000 consisting of 2,00,000 Equity Shares of Rs. 10 each. The assets of Nisha Ltd. are taken over at 90% of the book value with the exception of land and building which are accepted to book value.

Both the companies are to receive 10% of the net valuation of their respective business as Goodwill.

The purchase consideration is to be satisfied by Ujala Ltd. in its fully paid shares at 10% premium. In return of Debentures of Nisha Ltd. Debentures of the same amount and denomination are to be issued by Ujala Ltd.

Close the books of Nisha Ltd. and Usha Ltd. and show the Opening Balance sheet of Ujala Ltd. under Purchase Method.

(T.Y.B.Com. March 2005)

Solution:

Computation at Purchase Consideration

	Nisha Ltd		Usha Ltd		Total	
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
Assets Taken over						
Land and Building	70,000				70,000	
Plant and Machinery	1,98,000		1,00,000		2,98,000	
Stock	31,500		18,000		49,500	
Debtors	22,500		16,000		38,500	
Bank	6,000	3,28,000	2,000	1,36,000	8,000	4,64,000
Less : Liabilities						
15% Debentures	40,000				40,000	
Sundry Creditors	30,000		16,000		46,000	
Employees Provident Fund	6,000	76,000		16,000	8,000	92,000
Net Assets Before Goodwill		2,52,000		1,20,000		3,72,000
Add : Goodwill (10% of Net Assets)		25,200		12,000		37,200
Purchase Consideration		2,77,200		1,32,000		4,09,200
No. of Shares		25,200		12,000		37,200

(N.V. Security Premium	2,52,000 + 25,200	2,77,200	1,20,000 +12,000	1,32,000	3,72,000 +37,200	4,09,200
P.C. Satisfied as Under			Nisha Ltd		Usha Ltd	
25,200 Eq. Shares of Ujala Ltd. at Rs. 11 each 12,000 Eq. Shares of Ujala Ltd. at Rs. 11 each			2,77,200		1,32,000	

In the Books of Nisha Ltd. and Usha Ltd.
Realisation A/c

	Nisha Ltd. Rs	Usha Ltd. Rs		Nisha Ltd. Rs	Usha Ltd. Rs
To Sundry Assets :			By Sundry Liabilities		
Land & Building	70,000		15% Debentures	40,000	-
Plant & Machinery	2,20,000	1,00,000	Sundry Creditors	30,000	16,000
Stock	35,000	18,000	Employee's		
Debtors	25,000	16,000	Provident Fund	6,000	
Bank	6,000	2,000	By Usha Ltd.		
To Equity			(P.C.)	2,77,200	1,32,000
Share holders (Realisation Profit)	-	12,000	By Equity Shareholders (Realisation Loan)	2,800	
	3,56,000	1,48,000		3,56,000	1,48,000

Ujala Ltd. A/c

	Nisha Ltd. Rs	Usha Ltd. Rs		Nisha Ltd. Rs	Usha Ltd. Rs
To Realisation A/c (P.C.)	2,77,000	1,32,000	By Eq. Shares in Ujala Ltd.	2,77,200	1,32,000
	2,77,200	1,32,000		2,77,200	1,32,000

Equity Shareholders A/c

	Nisha Ltd. Rs	Usha Ltd. Rs		Nisha Ltd. Rs	Usha Ltd. Rs

To Advertisement Expenses		5,000	By Eq. Share Capital	2,00,000	1,20,000
To Realisation A/c (Loan)	2,800		By Reserve Fund	76,000	5,000
To Equity Shares in Ujala Ltd.	2,77,200	1,32,000	By P & L A/c	4,000	12,000
			By Realisation A/c (Profit)		
	2,80,000	1,37,000		2,80,000	1,37,000

Balance Sheet of Ujala Ltd.
As on 31.12.2014

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1	3,72,000	
b.Reserves & surplus		37,200	4,09 ,200
2. Non-Current Liabilities			
Long Term Borrowings			46,000
3. Current Liabilities			46,000
Total			**5,01,200**
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets			3,68,000
Intangible Assets			37,200
2. Current Assets			
Trade Receivables		38,500	
Inventories		49,500	
Cash and cash equivalents		8,000	96,000
Total			**5,01,200**

Notes to Accounts

	Rs.
1. Authorised Share Capital 2,00,000 Equity Shares of Rs. 10 each	**20,00,000**
Issued and Subscribed : Issued, Subscribed & Paid up 37,200 Equity Shares of Rs. 10 each	3,72,000

10.3 EXERCISES:

10.3.1 OBJECTIVE TYPE QUESTIONS

1. Which of the following statements is true with amalgamation?
   a. Amalgamation signifies the merging of two or more companies into one.
   b. Two or more companies form a new company.
   c. Refers to an arrangement, whereby a previously unprofitable of weak Company, is reconstructed.
   d. **Both (a) and (b) above**
   e. All of the above (a),(b)and (c) above.

2. Reconstruction refers to an arrangement, whereby:
   a. A Previously unprofitable or weak company is reconstructed by certain measures
   b. It is a blend of two or more undertakings into one undertaking
   c. Reconstruction includes absorption
   d. In reconstruction the assets and liabilities are not valued
   e. None of the above.

3. The assets Which is not taken under the net assets method of calculation purchase consideration is
   a. Furniture
   b. Preliminary expenses
   c. Stock
   d. Cash
   e. Debtors

4. Pooling of Interest Method of
   a. Valuation of Inventory
   b. Calculation of purchase consideration
   c. Accounting of amalgamation
   d. Method of valuing good will
   e. Method of valuing shares

5. In which of the following methods the purchase consideration is calculated on the basis of the agreed value of the shares of the transferor company?
   a. Lump sum Method
   b. Net assets Method
   c. Net Payment Method
   d. Intrinsic value Method
   e. Purchase Method

6. The Adjustment entry passes to eliminate the inter-company Owings is
   a. Debit Amalgamation Adjustment a/c, Credit Statutory reserve account
   b. Debit sundry Creditors a/c,Credit Sundry Debtors a/c
   c. Debit sundry Creditors a/c, Credit Statutory reserve a/c

d. Debit Amalgamation adjustment a/c, Credit sundry debtors
e. Debit sundry debtors, Credit Sundry Creditors

7. Under purchase Method, any excess of the amount of purchase consideration over the acquired assets of the transferor company should be recognized as-
   a. **Statuory Reserve**
   b. Amalgamation Adjustment
   c. Equity shares
   d. Good will

8. When there is goodwill arising in amalgamation in the financial statement of the transferee company such good will should be amortized to income and such amortization period should not exceed.
   a. 12 years
   b. 10 years
   c. 5 Years
   d. 7 years
   e. 6 years
9. If there is a provision against an asset, such an asset is transferred to the Realization account at-
   a. **Gross figure**
   b. Net figure
   c. Historical Values
   d. Current market value
   e. Net realizable value.

10. The Method of calculation of purchase consideration is

   a. Net Assets Method
   b. Net Payment Method
   c. Lump-sum Method
   d. Exchange of shares Method

PRACTICAL PROBLEMS

Exercises: 1

The following Balance Sheet are given as on 31st March, 2015:

Liabilities	**Lock Ltd**	**Key Ltd.**	**Assets**	**Lock Ltd.**	**Key Ltd.**
Share Capital			Fixed Assets	25000	15000
Shares of Rs.100 each			Investments	5000	----
Fully paid	20000	10000	Current Assets	20000	5000
Reserves	10000	8000			

Other liabilities	20000	2000		
	--------	--------	-------	--------
	50000	**20000**	**50000**	**20000**
	======	=====	=====	======

The following further information is given –

a) Investments of Lock Ltd. include Rs. 3000 representing shares in Key Ltd. having a face value of Rs.2000

b) Key Limited issued bonus shares on 1st April, 2015 in the ratio of one share for every two held out of Reserves and Surplus.

c) It was agreed that Lock Ltd. will take over the business of Key Ltd. on the basis of the latter's Balance Sheet, the consideration taking the form of allotment of shares in Key Ltd

d) The value of shares in Lock Ltd. was considered to be Rs. 150 and the shares in Key Ltd. were valued at Rs.100 after the issue of the bonus shares. The allotment of shares is to be made on the basis of these values.

e) Liabilities of Key Ltd. includes Rs.1000 due to Lock Ltd. for purchases from it on which Lock Ltd. made profit of 25% of the cost. The goods of Rs. 500 out of the said purchases Remained in stock on the date of the above Balance Sheet.

Make the closing ledger in the Books of Key Ltd. and the opening journal entries in the Books Of Lock Ltd. and prepare the Balance Sheet as at 1st April, 2015 after the takeover.

3

INTERNAL RECONSTRUCTION

Unit Structure

11.0 OBJECTIVES:

After studying the unit the students will be able to:

- Understand the types of reconstruction.
- Know the alternation of share capital.
- Explain the procedure of reconstruction.
- Understand the Accounting entries for reconstruction.
- Solve the practical problems on the unit.

11.1 INTRODUCTION:

The term reconstruction means reorganizing the capital structure of a company including the reduction of the claim of both the classes of shareholders & the creditors against the company. Sick companies (loss making companies) may be taken over by the profit making companies however in case of c/f of huge losses, assets are overvalued or undervalued, in such cases company may go for reconstruction. It may be external or internal reconstruction.

11.2 TYPES OF RECONSTRUCTION:

The Company can be reconstructed internally or externally. It means two types of reconstruction is possible:

11.2.1 External Reconstruction:

In case of external reconstruction a new company is formed to take over the business of an existing company which has suffered huge losses & which is in bad financial position. The vendor company goes into liquidation & its business is taken over by the new company.

11.2.2 Internal Reconstruction:

In case of internal reconstruction, the capital structure of the company is reorganized to infuse new life in the company. It includes alteration, reduction and reorganization of share capital of the company.

11.3 ALTERATION OF SHARE CAPITAL:

A limited company if authorized by its Articles of Association can alter the capital clause of its Memorandum of Association. As per Sec. 61 of the Companies Act 2013 a company can alter its share capital. The alteration of share capital may be in following different ways: -

a] Increase in share capital by the issue of new shares.

b] Consolidation of shares:

Consilidation refers to conversion of shares of the smaller denomination into shares of larger denomination e.g: 5000 equity shares of Rs. 10 each can be consolidated into 500 shares of Rs. 100 each.

c] Subdivision of shares:

Sub division refers to conversion of shares of the larger denomination into shares of small denomination e.g: 5000 equity shares of Rs. 100 each can be subdivided into 50000 shares of Rs. 10 each.

d] Conversion of shares into stock:

A company may convert its shares into stock. Stocks may be in fractions which is not possible in case of shares. Conversion of shares into stock requires sanction of the Central Government.

e] Surrender of shares:

In a reconstruction scheme the shareholders may be required to surrender a part of their shareholdings. Such a surrender may be either before immediate cancellation or for issue to some of the creditors of the company in satisfaction of their claim.

f] Cancellation of Unissued shares:

In case a company cancels its unissued shares it does not require any accounting entry to be passed. The authorized shares capital of the company will stand reduced by the amount of unissued shares now cancelled.

11.4 LEGAL ASPECTS:

Internal reconstruction scheme should be framed by careful study and proper valuation of assets and liabilities. It involves a compromise or arrangement between the company and its members or/and its creditors. However following aspects should be carefully taken care of while framing the scheme of internal reconstruction –

a] For change in share capital in any form, it should be considered as per provisions of the M/A & A/A, and in case if required the company should alter the provisions in the M/A & A/A.

b] Company is required to give a notice to the Register of Companies within 30 days of its passing resolution.

c] Sanction of SEBI is necessary in certain cases.

d] Board Resolution is necessary to effect the alteration.

11.5 CAPITAL REDUCTION: (Section 66)

Internal reconstruction means the reduction of capital to cancel any paid-up share capital which is lost during the course of business i.e. not represented by the real value of the assets.

A company can reduce its share capital in the followings ways:

a] Writing off lost capital

b] Refunding surplus paid-up capital.

c] Reducing the liability of the members for uncalled capital.

A company can reduce its share capital only when each of the following condition is satisfied

a] The A/A of the company must permit such reduction.

b] The company passes special resolution for reducing its share capital.

c] The company obtains the confirmation of the court.

Reduction of capital will be effective only when it is sanctioned by the court and registered with Registrar of Companies. Court may at its discretion order the words “And Reduced” to be added to the name of the company for the period prescribed.

11.6 ACCOUNTING ENTRIES:

Capital Reduction Account is opened in the ledger to give effect of sacrifice made by shareholders & others as well as to write off accumulated losses, fictitious assets, & change in values of assets/liabilities.

1] **When the face value of share is changed:**
Share capital A/c (o/d) Dr.
(With paid up value of old shares)
To Share Capital A/c (new)
(With paid up value of new shares)
To Capital Reduction A/c
(With difference)

2] **When any sacrifice is made by the creditors:**
Creditors A/c (with sacrifice) Dr.
To Capital Reduction A/c

3] **When there is reduction in share capital (face value of share is not changed)**
Share Capital A/c Dr.
To Capital Reduction A/c
(With the amount of reduction).

4] **When the value of any asset is appreciated:**
Asset A/c (increase in value) Dr.
To Capital Reduction A/c

5] **When any sacrifice is made by the Debenture Holders**
Debentures A/c (increase in value) Dr.
To Capital Reduction A/c

6] **When shares are consolidated:**
Share Capital A/c (say Rs. 10) Dr.
To Share Capital A/c (say Rs. 100)

7] **When Shares are subdivided:**
Share Capital A/c (say Rs. 100) Dr.
To Share Capital A/c (say Rs. 10)

8] When capital reduction is utilised for writing off fictitious assets, losses and excess value of other assets:

Capital Reduction A/c Dr.
To P/L A/c
To Goodwill A/c
To Preliminary Expenses A/c
To Discount on Shares/Debentures A/c
To Other Assets A/c
To Capital Reserve A/c (if any balance is left)

9] When shares are converted into stock:

Share Capital A/c Dr.
To Share Stock A/c

10] When shares are surrendered:

Share Capital A/c Dr.
To Share Surrendered A/c

11] When surrendered shares are converted into preference shares:

Share Surrendered A/c Dr.
To Preference Share Capital A/c

12] When contingent liability/unrecorded liability is paid for:

Capital Reduction A/c Dr.
To Bank A/c

(**Note:** No entry is required for amount foregone against such liability.)

13] When recorded liability is paid for:

Liability A/c Dr.
To Bank A/c

(**Note:** Any profit or loss should be transferred to Capital Reduction A/c)

14] When recorded assets are disposed off:

Bank A/c Dr.
To Assets A/c

(**Note:** Any profit or loss on sale should be transferred to Capital Reduction A/c)

15] When Reconstruction expenses are paid

Capital Reduction A/c Dr.
To Bank A/c

16] When an unrecorded assets is sold off:

Bank A/c Dr.

To Capital Reduction A/c

17] When finance is raised by issue of shares

Bank A/c Dr.

To Share Capital A/c

18] When arrears of preference dividend are cancelled:

No Entry

19] When new debentures are exchanged for old debentures:

Old Debentures A/c Dr.

To New Debentures A/c

20] When arrears of preference dividend are settled by issue of deposit certificates cash/shares:

Capital Reduction A/c Dr.

To Deposit Certificates/Cash/Share Certificate A/c

21] When the rate of preference dividend is changed:

Preference Share Capital (old) A/c Dr.

To Preference Share Capital A/c (new)

22] When surrendered shares are issued to creditors:

(a) Surrendered A/c Dr.

To Share Capital A/c

(b) Creditors A/c Dr.

To Capital Reduction A/c

Note: Profit or Loss on scheme to be transferred to capital Reduction A/c.

23] When provision for taxation, Capital Reserve,Securities Premium is utilised:

Provision for Taxation A/c Dr.

Capital Reserve A/c Dr.

Securities Premium A/c Dr.

To Capital Reduction A/c

Proforma:

Capital Reduction A/c

Particulars	Rs.	Particulars	Rs.
To P & L A/c (Loss written off) To Goodwill A/c (Written off) To Preliminary expenses A/c (Written off) To Discount on Shares/Debentures (Written off) To Assets A/c (Decrease in value) To Bank A/c (payment of unrecorded liability) To Bank A/c (payment of Reconstruction Expenses) To Bank A/c (Refund of Directors Fees) To Capital Reserve (Balancing figure)	XX XX XX XX XX XX XX XX XX	By Share Capital A/c (Amount of reduction) By Debentures A/c (Amount of Reduction) By Creditors A/c (Amount of Sacrifice) By Assets A/c (Increase in value) By Bank A/c (sate of unrecorded assets)	XX XX XX XX XX
	XXX		**XXX**

11.7 SOLVED PROBLEMS:

Illustration– 1

Following is the Balance sheet of M/s. Life Care Ltd. as on 31st March, 2015.

Balance Sheet as on 31st March, 2015.

Liabilities	Rs.	Assets	Rs.
50,000 – 8% Cumulative Preference Shares of Rs.10/- each.	5,00,000	Goodwill	1,00,000
40,000 – Equity Shares of Rs.10/- each.	4,00,000	Freehold Property	1,50,000
Security Premium	8,000	Leasehold Property	2,40,000
9% Debentures	1,00,000	Plant & Machinery	3,00,000
Accrued Debenture interest	6,000	Furniture	1,00,000
Sundry Creditors	1,00,000	Stock	50,000
Bank Overdraft	1,42,000	Debtors	1,00,000
		Preliminary Exp.	9,000
		Profit & Loss A/c	2,07,000
	12,56,000		12,56,000

Note –

1) Preference dividend was in arrears for 3 years.
2) There was a contingent liability of Rs.30,000/- for workmen compensation.

   Following scheme of reconstruction was approved & implemented.

   a) The Preference shares were reduced to Rs.8/- per share fully paid & Equity Shares to Rs.3/- per share fully paid.
   b) One new Equity share of Rs.10/- each was issued of every Rs.50/- gross preference dividend in arrears.
   c) After reduction, both classes of shares were consolidated into Rs.10/- shares.
   d) The balance of Securities Premium was utilized.
   e) Plant & Machinery was written of down to Rs.2,50,000/-.
   f) Furniture was sold to Rs.75,000/-
   g) Preliminary expenses debit balance in Profit & Loss A/c, debt of Rs.25,000/- & obsolete stock Rs.18,000/- were to be written off.
   h) Contingent liability for which no provision has been made was settled at Rs.15,000/-. However, the amount of Rs.11,000/- was recovered from insurance company.
   i) Debenture holders agreed to Forgo principal amount by Rs.50,000/- & accrued debenture interest in full.

Pass journal entries. Prepare capital reduction account & Balance sheet after reconstruction.

Solution :

Journal of Life Care Ltd.

Date	Particulars	Debit (Rs.)	Credit (Rs.)
1.	8% Preference Share Cap. A/c …………Dr. (50,000X10) To 8% Preference Share Capital A/c (50,000X8) To Capital Reduction A/c (50,000X2) (Being reduction in 8% Preference Capital.)	5,00,000	 4,00,000 1,00,000

2.	8% Preference Share Capital A/c……..…Dr. (40,000X8) To 8% Preference Share Capital A/c (32,000X10) (Being consolidation of 8% Preference Shares.)	3,20,000	3,20,000
3.	Equity Share Capital A/c ………………….Dr. (40,000X10) To Equity Share Capital A/c (40,000X3) To Capital Reduction A/c (40,000X7) (Being reduction in Equity Share Capital)	4,00,000	1,20,000 2,80,000
4.	Equity Share Capital A/c ……..………….. Dr. (40,000X3) To Equity Share Capital A/c (12,000X10) (Being consolidation of Equity Shares.)	1,20,000	1,20,000
5.	Capital Reduction A/c ……………………. Dr. To Equity Share Capital A/c $(8\%\text{X}5,00,000\text{X}\frac{3}{50}\text{X}10)$ (Being arrears of Preference dividend paid by issue of Equity shares.)	24,000	24,000
6.	Security Premium A/c ……………………. Dr. To Capital Reduction A/c (Being Security Premium used.)	8,000	8,000
7.	Bank A/c ……………………………………Dr. Capital Reduction A/c …………………… Dr. To Furniture A/c (Being sale of Furniture at a loss of Rs.25,000/-)	75,000 25,000	1,00,000
8.	Capital Reduction A/c ……………………Dr. To Bank A/c (Being payment of contingent liability.)	15,000	15,000
9.	Bank A/c ………………………………….. Dr. To Capital Reduction A/c (Being recovery of claim from insurance company.)	11,000	11,000
10.	9% Debentures A/c ……………………… Dr. Accrued Debenture interest A/c ……….. Dr. To Capital Reduction A/c	50,000 6,000	56,000

11.	Capital Reduction A/c …………………… Dr.	3,91,000	
	To Plant & Machinery A/c		50,000
	(3,00,000 – 2,50,000)		
	To Preliminary Expenses A/c		9,000
	To Profit & Loss A/c		2,07,000
	To Sundry Debtors A/c		25,000
	To Stock A/c		18,000
	To Capital Reserve A/c		82,000
	(Being losses & Assets written off.)		

Capital Reduction Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Equity Share Cap. A/c (Preference Dividend)	24,000	By 8% Pref. Share Cap. A/c	1,00,000
To Furniture	25,000	By Equity Share Capital A/c	2,50,000
To Plant & Machinery A/c	50,000		
To Preliminary Expenses	9,000	By Security Premium	8,000
To Profit & Loss A/c	2,07,000	By 9% Debentures	50,000
To Sundry Debtors A/c	25,000	By Accrued interest on debentures	6,000
To Stock	18,000		
To Bank (Contingent liability)	15,000	By Bank (Insurance)	11,000
To Capital Reserve	82,000		
	4,55,000		4,55,000

M/s. Life Care Ltd (And Reduced)
Balance Sheet as on 1st April 2015

Particulars	Notes	Rs.	Rs.
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1	5,44,000	
b. Reserves & Surplus	2	82,000	6,22,000
2. Non-Current Liabilities			
Long Term Borrowings			
a. 9% Non-Convertible Debn.			50,000
3. Current Liabilities			
a. Trade Payables			1,00,000
b. Short Term Borrowings(Bank Overdraft)			71,000
Total			**8,47,000**

II. ASSETS			
1. Non current Assets			
a. Fixed Assets	3		6,40,000
- i. Tangible Assets			
ii. Intangible Assets (Goodwill)			1,00,000
2. Current Assets			
a. Inventories		32,000	
b. Trade Receivables		75,000	1,07,000
Total			**8,47,000**

Notes to Accounts

Note – 1 Share Capital	Number	Rs.
Authorised Share Capital		
Issued, Paid Up Share Capital		
Equity Share Capital		
Equity Shares of Rs. 10/- each	14,400	1,44,000
Preference Share Capital		
8% Pref. Share of Rs. 10/- each	40,000	4,00,000
		5,44,000

Note – 2 Reserves & Surplus	Rs.	Rs.
Capital Reserve (transf. from Capital Reduction A/c)		82,000

Note – 3 Tangible Assets	Rs.	Rs.
Free hold Property	1,50,000	
Leasehold Property	2,40,000	
Plant & Machinery	2,50,000	6,40,000

Illustration – 2

Following is the Balance Sheet of Satya Ltd. as on 31st March, 2015.

Balance Sheet as on 31st March 2015

Liabilities	Amt.	Assets	Amt.
Share Capital		Goodwill	3,00,000
1,50,000 Equity Shares of Rs.5/- each fully paid	7,50,000	Land & Building	2,40,000
		Equipment	2,10,000
		Sundry Debtors	2,00,970
5,000 6% Preference Shares of Rs.100/- each fully paid	5,00,000	Stock	3,32,440
		Investment	44,000
		Cash at Bank	21,000
8% Debentures	3,00,000	Profit & Loss A/c	7,51,590
Bank Overdraft	1,70,000		
Sundry Creditors (including Rs.22,000 int. on Bank Overdraft)	3,80,000		
	21,00,000		21,00,000

Preference dividend is in arrears for Five years.

Following scheme of reconstruction was approved by the court.

1) Equity Shares be reduced to Rs.150/- each of then to be consolidated into shares of Rs.10/- each.
2) 6% Preference shares be reduced to Rs.50/- each & then to be subdivided into shares of Rs.10/- each.
3) Interest accrued but not due on 8% debentures. For half year ended 31st March 2015 has not been provided in the above Balance Sheet. The debenture holders have agreed to received 30% of this interest in cash immediately & provision for the balance be made in the books of account.
4) Rs.20,000/- be paid to Preference shareholders in lieu of arrears of Preference dividend.
5) The debenture holders have also agreed to accept equal number of 9% debentures of Rs.60/- each in exchange of 8% debentures of Rs.100/- each.
6) Bank has agreed to take over 50% stock in full satisfaction of its claim including interest. The remaining stock be revalued at Rs.80,000/-.
7) Investment be sold for Rs.39,000/-.

8) Tangible Fixed assets be appreciated by 15% & provision be made for doubtful debts of Rs.18,000/-.

Give journal entries for the above scheme of reconstruction. Prepare Capital Reduction Account in the books of Satya Ltd. & Balance sheet of the company after reconstruction.

Solution :

Journal of Satya Ltd.

Date	Particulars	Debit (Rs.)	Credit (Rs.)
1.	Equity Shares Capital A/c (5) ……………Dr. To Equity Share Capital A/c (1.50) To Capital Reduction A/c (3.5) (Being 1,50,000 Equity Shares of Rs.5/- each reduced to Rs.1.50 each.)	7,50,000	 2,25,000 5,25,000
2.	Equity Share Capital A/c (1.50) …………Dr. To Equity Share Capital (10) (Being 1,50,000 Equity shares of Rs.1.50 consolidated into shares of Rs.10/- each.)	2,25,000	 2,25,000
3.	6% Preference Share Capital A/c (100) .. Dr. To 6% Preference Share Capital A/c (50) To Capital Reduction A/c (Being 6% Preference shares of Rs.100/- each reduced to shares of Rs.50/- each.)	5,00,000	 2,50,000 2,50,000
4.	6% Preference Share Capital A/c ……….Dr. To 6% Preference Shares Capital A/c (Being 6% Preference shares of Rs.50/- each subdivided into shares of Rs.10/- each.)	2,50,000	 2,50,000
5.	Capital Reduction A/c …………………….Dr. To Bank A/c To Interest on Debentures A/c (Being payment of accrued interest on debentures to the extent of 30% & provided for the balance.)	12,000	 3,600 8,400
6.	Capital Reduction A/c …………………… Dr. To Bank A/c (Being paid to preference share holders in lieu of arrears of dividend.)	20,000	 20,000

7.	8% Preferences A/c (100) ……………….Dr. To 9% Debentures A/c (60) To Capital Reduction A/c (Being exchanged 8% debentures by 9% debentures.)	3,00,000	 1,80,000 1,20,000
8.	Bank Overdraft A/c ………………………. Dr. Sundry Creditors A/c …………………….. Dr. (Interest on Bank Overdraft) To Stock A/c To Capital Reduction A/c (Being taken over 50% of the Stock by the bank in satisfaction of bank overdraft.)	1,70,000 22,000	 1,66,220 25,780
9.	Capital Reduction A/c …………………….Dr. To Stock A/c (Being reduction in Stock.)	86,220	 86,220
10.	Bank A/c ………………………………….Dr. Capital Reduction A/c …………………… Dr. To Investment A/c (Being sale of investment at a loss.)	39,000 5,000	 44,000
11.	Capital Reduction A/c …………………… Dr. To Profit & Loss A/c To Provision for doubtful debts A/c To Capital Reserve A/c (Being written off profit & loss account debit balance, provided for reduction redemption reserve & transferred the remaining amount to Capital Reserve Account.)	8,65,040	 7,51,590 18,000 95,470
12.	Land & Building A/c ………………………Dr. Equipment A/c …………………………… Dr. To Capital Reduction A/c (Being appreciation in Land & Building & Equipment.)	36,000 31,500	 67,500

Capital Reduction Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Bank A/c	3,600	By Equity Share Capital A/c	5,25,000
To Int. on debentures	8,400	By 6% Preference Share Capital A/c	2,50,000
To Bank A/c	20,000	By 8% Debentures A/c	1,20,000
To Stock A/c	86,220	By Bank Overdraft & Creditors A/c	25,780
To Investment A/c	5,000	By Land & Building A/c	36,000
To Profit & Loss A/c	7,51,590	By Equipments A/c	31,500
To Provision for doubtful debts.	18,000		
To Capital Reserve	95,470		
	9,88,280		9,88,280

Satya Ltd. (And Reduced)
Balance Sheet as on 1st April 2015

Particulars	Notes	Rs.	Rs.
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1	4,75,000	
b. Reserves & Surplus	2	95,470	5,70,470
2. Non-Current Liabilities			
Long Term Borrowings			1,80,000
3. Current Liabilities			
a. Trade Payables			3,58,000
b. Other Current Liabilities	3		8,400
Total			**11,16,870**
II. ASSETS			
1. Non current Assets			
a. Fixed Assets	4		
- i. Tangible Assets			5,17,500
ii. Intangible Assets (Goodwill)			3,00,000
2. Current Assets			
a. Inventories	5	80,000	
b. Trade Receivables		1,82,970	
c. Cash & Cash Equivalents		36,400	2,99,370
Total			**11,16,870**

Notes to Accounts

Note – 1 Share Capital	Number	Rs.
Authorised Share Capital		
Issued, Paid Up Share Capital		
Equity Share Capital		
Equity Shares of Rs. 10/- each	22,500	2,25,000
Preference Share Capital		
6% Pref. Share of Rs. 10/- each	25,000	2,50,000
		4,75,000

Note – 2 Reserves & Surplus	Rs.	Rs.
Capital Reserve (transf. from Capital Reduction A/c)		95,470

Note – 3 Other Current Liabilities	Rs.	Rs.
Interest payable on Debentures		8,400

Note – 4 Tangible Assets	Rs.	Rs.
Land & Building	2,76,000	
Equipments	2,41,500	5,17,500

Note – 5 Trade Receivables	Rs.	Rs.
S. Debtors	2,00,970	
Less: Prov.for doubtful debts.	18,000	1,82,970

Illustration – 3

Following is the Balance sheet of Damyanti Ltd. as on 31st March, 2015.

Liabilities	Amt.	Assets	Amt.
16,000 12% Preference Shares of Rs.10/- each fully paid up	1,60,000	Goodwill	90,000
		Patents	50,000
		Land & Building	1,50,000
		Plant & Machinery	3,00,000
1,40,000 10% Preference shares of Rs.10/-, Rs.5/- per share paid up	70,000	Furniture	35,000
		Investment	85,000
		Sundry Debtors	3,00,000
		Bills Receivables	1,20,000

18,000 Equity Share of Rs.10/- each fully paid up	1,80,000	Bank	30,000
		Profit & Loss A/c	71,500
12% Debenture of Rs.100/- each	1,70,000		
11% Debentures of Rs.100/- each	2,80,000		
Interest due on debenture	21,500		
Sundry Creditors	3,50,000		
	12,31,500		12,31,500

The following scheme of reconstruction was submitted & approved by the court.

1) 12% Preference Shares of the Rs.10/- each fully paid were reduced to 13% Preference Shares of Rs.10/- each, Rs.6/- per share paid up.
2) 10% Preference share of Rs.10/- each, Rs.5/- per share paid up were reduced to 13% Preference shares of Rs.10/- each, Rs.4/- per share paid up.
3) Equity Shares of Rs.10/- each fully paid were reduced to the denomination of Rs.7/- each fully paid.
4) 11% Debenture holders agreed to accept 44,800 Equity Shares of Rs.5/- each in full settlement of their claims.
5) Debentures holders agreed to Forgo the interest due on debentures.
6) Sundry Creditors agreed to Forgo 20% of their claims.
7) The company recovered as damages as sum of Rs.60,000/- which was not recorded in the books.
8) Cost of reconstruction was paid Rs.3,000/-.
9) Assets are to be revalued as under : Land & Buildings Rs.2,05,000/-, Plant & Machinery Rs.2,50,000/-, Furniture Rs.10,000/-, Investment Rs.1,05,000/-, Sundry Debtors Rs.2,77,000/-.
10) All intangible assets & accumulated losses are to be written off.

You are required to –

i) Pass journal entries in the books of Damyanti Ltd.

ii) Prepare Capital Reduction Account & Balance Sheet after reconstruction.

Solution:

Journal of Damyanti Ltd.

Date	Particulars	Debit (Rs.)	Credit (Rs.)
1.	12% Preference Share Capital A/c ……..Dr.	1,60,000	
	To 13% Preference Share Capital A/c		96,000
	To Capital Reduction A/c		64,000
	(Being reduction in 12% Preference Capital.)		
2.	10% Preference Share Capital A/c ……..Dr.	70,000	
	To 13% Preference Share Capital A/c		56,000
	To Capital Reduction A/c		14,000
	(Being reduction in 13% Preference Capital.)		
3.	Equity Share Capital A/c …………………Dr.	1,80,000	
	To Equity Share Capital A/c		1,26,000
	To Capital Reduction A/c		54,000
	(Being reduction in Equity Share Capital.)		
4.	11% Debenture A/c ………………………Dr.	2,80,000	
	To Equity Share Capital A/c		2,24,000
	To Capital Reduction A/c		56,000
	(Being reduction in debentures.)		
5.	Interest due on Debenture A/c …………. Dr.	21,500	
	To Capital Reduction A/c		21,500
	(Being interest dues on debentures cancelled.)		
6.	Creditors A/c …………………………….. Dr.	70,000	
	To Capital Reduction A/c		70,000
	(Being Creditors dues reduced.)		
7.	Bank A/c ………………………………….. Dr.	60,000	
	To Capital Reduction A/c		60,000
	(Being damages recovered.)		
8.	Capital Reduction A/c …………………… Dr.	3,000	
	To Bank A/c		3,000
	(Being costs of reconstruction paid.)		
9.	Land & Building A/c ………………………Dr.	55,000	
	Investment A/c …………………………… Dr.	20,000	
	To Capital Reduction A/c		75,000
	(Being increase in valuations.)		
10.	Capital Reduction A/c …………………… Dr.	5,01,500	
	To Plant & Machinery A/c		50,000
	To Furniture A/c		25,000
	To Sundry Debtors A/c		23,000

	To Goodwill A/c		90,000
	To Patents A/c		50,000
	To Profit & Loss A/c		71,500
	To Capital Reserve A/c		1,02,000

Capital Reduction Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Bank A/c	3,000	By 12% Preference	
To Plant & Machinery	50,000	Share Capital A/c	64,000
To Furniture A/c	25,000	By 10% Preference	
To Sundry Debtors A/c	23,000	Share Capital A/c	14,000
To Goodwill A/c	90,000	By Equity Share Capital	
To Patents A/c	50,000	A/c	54,000
To Profit & Loss A/c	71,500	By 11% Debenture A/c	56,000
To Capital Reserve A/c	10,200	By Interest due on	
		debentures	21,500
		By Sundry Creditors	70,000
		By Bank A/c	60,000
		By Land & Building A/c	55,000
		By Investment A/c	20,000
	4,14,500		4,14,500

Balance Sheet of Damyanti Ltd. (And Reduced) as on 1st April, 2015

Particulars	Notes	Rs.	Rs.
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1	5,02,000	
b. Reserves & Surplus	2	1,02,000	6,04,000
2. Non-Current Liabilities			
Long Term Borrowings			
	3		1,70,000
3. Current Liabilities			
a. Trade Payables			2,80,000
Total			**10,54,000**

II. ASSETS			
1. Non current Assets			
a. Fixed Assets	4		
- i. Tangible Assets			
b. Non -current Investments	5		4,65,000
3. Current Assets			1,05,000
a. Trade Receivables			
b. Cash & Cash Equivalents			
		3,97,000	
		87,000	4,84,000
Total			**10,54,000**

Notes to Accounts

Note – 1 Share Capital	**Number**	**Rs.**
Authorised Share Capital		
Issued, Paid Up Share Capital		
Equity Share Capital		
Equity Shares of Rs. 7/- each	18,000	1,26,000
Equity Shares of Rs. 5/- each	44,800	2,24,000
Preference Share Capital		
13 % Pref. Share of Rs. 10/- each Rs.6/- paid up	16,000	96,000
13 % Pref. Share of Rs. 10/- each Rs.4/- paid up	14,000	56,000
		5,02,000

Note – 2 Reserves & Surplus	**Rs.**	**Rs.**
Capital Reserve (transf. from Capital Reduction A/c)		1,02,000

Note – 3 Long Term Borrowings	**Rs.**	**Rs.**
12% Debentures of Rs.100/- each		1,70,000

Note – 4 Tangible Assets	Rs.	Rs.
Land & Building	2,05,000	
Plant & Machinery	2,50,000	
Furniture	10,000	4,65,000

Note – 5 Non -current Investments	Rs.	Rs.
Balance:	85,000	
Add: Increase in valuations	20,000	1,05,000

Illustration– 4

M/s. Katrina Ltd. whose Balance Sheet as at 31st March 2015 is as given below.

Liabilities	Rs.	Assets	Rs.
Sources of Funds		Application of Sources	
2,00,000 Equity Shares of Rs.20/- each Rs.10/- paid up	20,00,000	Fixed assets 15,50,000 Goodwill 50,000	16,00,000
10% Preference Shares Capital		Investment at cost (Market value 1,00,000)	1,10,000
10,000 Shares of Rs.100/- each, Rs.50/- paid up	5,00,000	Current Assets & Loans & Advances Current Assets	
Secured Loan 9% Deb. 7,00,000 (+) O/s int. 1,00,000	8,00,000	Stock 3,00,000 Debtors 5,00,000 B.R. 8,00,000 16,00,000	
Loan from ICICI Ltd. 1,80,000 (+) O/s Int. 30,000	2,10,000	Less : Liab. S. Creditors 2,00,000	14,00,000
		Profit & Loss A/c	4,00,000
	35,10,000		35,10,000

Preference dividend is in arrears for 1 year. Following scheme of reconstruction is approved & agreed upon

1) Preference Shareholders to give up their claims, inclusive of dividends to the extent of 50% & balance to be paid off.
2) Debenture holders agree to give up their claims to receive interest in consideration of their rate of interest being enhanced to 12% henceforth.

3) ICICI Ltd. agree to give up 80% of their interest outstanding in consideration of their claim being paid off at once.
4) Sundry Creditors would like to grant a discount 20% if they were to be paid off immediately.
5) Balance of Profit & Loss A/c, Goodwill & 50% of the total sundry debtors to by written off.
6) Fixed Assets to be written down by Rs.50,000/-.
7) Investment to be reflected at their market value.
8) Cost of reconstruction is Rs.50,000/-.
9) To the extent required Equity Shareholders suffers on reduction of their rights.
10) The Equity shareholder bring in necessary as against their partly paid shares to leave working capital at Rs.30,000/-.

Pass necessary journal entries in the books of the company assuming that scheme has been put through fully & prepare the Balance Sheet after reconstruction. Ignore narration.

Solution:

In the books of Ms. Katrina Ltd.

Date	Particulars	Debit (Rs.)	Credit (Rs.)
Dec. 31 1.	Preference Share Capital A/c ………..Dr. To Preference Shareholders A/c To Capital Reduction A/c	5,00,000	 2,50,000 2,50,000
2.	Capital Reduction A/c …………………Dr. To Preference Shareholders A/c	50,000	 50,000
3.	9% Debenture A/c ……………………. Dr. Interest o/s on debenture A/c ……….. Dr. To 12% Debentures A/c To Capital Reduction A/c	7,00,000 1,00,000	 7,00,000 1,00,000
4.	ICICI Loan A/c …………………………Dr. Outstanding interest A/c …………….. Dr. To Bank A/c To Capital Reduction A/c	1,80,000 30,000	 1,86,000 24,000
5.	Capital Reduction A/c …………………Dr. To Profit & Loss A/c To Goodwill A/c To Investment A/c To Debtors A/c To Fixed Assets A/c	7,65,000	 4,00,000 50,000 10,000 2,50,000 50,000

	To Bank (Expenses) A/c		5,000
6.	Creditors A/c ……………………………Dr. To Bank A/c To Capital Reduction A/c	2,00,000	 1,60,000 40,000
7.	Preference Shareholders A/c ……….. Dr. To Bank A/c	3,00,000	 3,00,000
8.	Equity Share Capital A/c …………….. Dr. To Capital Reduction A/c	4,01,000	 4,01,000
9.	Bank A/c ……………………………… Dr. To Equity Share Capital A/c	6,81,000	 6,81,000

Working Note:

Bank Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Equity Share Capital A/c (Bal Figure)	6,81,000	By Creditors A/c By Expenses A/c By Loan Interest A/c By Preference Share Capital A/c By Closing Balance	1,60,000 5,000 1,86,000 3,00,000 30,000
	6,81,000		6,81,000

Capital Reduction Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Preference Dividend A/c To Sundries A/c	50,000 7,65,000	By Preference Shareholders A/c By Debenture Interest A/c By Interest A/c By Creditors A/c By Equity Share Capital A/c	2,50,000 1,00,000 24,000 40,000 4,01,000
	8,15,000		8,15,000

Balance Sheet as on 1st April, 2015

Particulars	Notes	Rs.	Rs.
I. Equity and Liabilities			
1. Shareholders' Funds			
Share Capital	1		22,80,000
2. Non-Current Liabilities			

Long Term Borrowings 12% Debentures			7,00,000
Total			**29,80,000**
II. Assets **1. Non current Assets** a. Tangible Assets b. Non Current Investments **2. Current Assets** Inventories Trade Receivables Cash & Cash equivalents	2	3,00,000 10,50,000 30,000	15,00,000 1,00,000 13,80,000
Total			**29,80,000**

Notes to Accounts

Note – 1 Share Capital	**Number**	**Rs.**
Authorised Share Capital *Issued, Paid Up Share Capital* Equity Share Capital 200000 Equity Shares of Rs. 20, Rs.11.4 paid up	200000	22,80,000 22,80,000

Note – 2 Trade Receivables	**Rs.**	**Rs.**
Debtors Bills Receivables	2,50,000 8,00,000	10,50,000 10,50,000

Illustration 5

The summarized Balance Sheet of Vipul Ltd. as at 31st March, 2015 was as under:

Liabilities	**Rs.**	**Assets**	**Rs.**
Redeemable Preference shares of Rs.100/- each fully paid	15,00,000	Fixed assets	60,00,000
Equity Shares of Rs.100/- each fully paid	40,00,000	Cash on hand	10,00,000
Reserve	30,00,000	Cash at IDBI Bank	30,00,000
Creditors	50,00,000	Other Current Assets	40,00,000
Loans	10,00,000	Preliminary Expenses	5,00,000
	1,45,00,000		1,45,00,000

The company proposed to make a fresh issue of Capital to the public in June 2015. However, before doing so the directors desire to carry out the following scheme of reconstruction.

1) The fictitious assets shall be written off.
2) The fixed assets to be appreciated by 50%.
3) The goodwill of the company valued at Rs.28,00,000/- shall be brought into the books.
4) A provision of 20% shall be made against the other current assets for likely shortfall in its realization by ear – marking the requisite amount from the existing reserves.
5) The Preference shares shall be redeemed at 20% Premium.
6) The company to issue bonus shares in the ratio of one share for every two existing Equity Shares.
7) The Equity Capital thereafter to be sub-divided into shares of Rs.50/- each.

You are required to prepare Capital Reduction Account.

Solution:

In the books of Vipul Ltd.
Capital Reduction Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Preliminary Expenses A/c	5,00,000	By Fixed Assets A/c	3,00,000
To preliminary Redemption of Preference Share A/c	3,00,000	By Goodwill A/c	28,00,000
To Capital Reserve A/c	30,00,000	By Reserve A/c	7,00,000
	38,00,000		38,00,000

Reserve Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Other Current Assets A/c	8,00,000	By Balance b/d	30,00,000
To Capital Redemption Reserve A/c	15,00,000		
To Capital Redemption A/c	7,00,000		
	30,00,000		30,00,000

Illustration 6

The Balance Sheet of Three Idiots Ltd. as at 31st March 2015 was as under –

Liabilities	Rs.	Assets	Rs.
10,000 Equity Shares of Rs.50/- each fully paid	5,00,000	Goodwill	1,00,000
10%, 50,000 Debentures of Rs.10/- each	5,00,000	Other Assets	8,00,000
Interest on debenture	20,000	Profit & Loss A/c	3,00,000
Sundry Creditors	1,80,000		
	12,00,000		12,00,000

For the purpose of reconstruction of the company, necessary resolutions are passed on the following lines.

1) The Equity Shares are to be sub divided into Share of Re.1/- each & each shareholder shall re-surrender 80% of his holding.
2) Out of the surrendered shares, 1,00,000 shares will be converted to 8% Preference Shares of Rs.10/- each.
3) Debentures holders will reduced their claims by Rs.2,20,000/- & in consideration they are to get the entire Preference Shares Capital converted from Shares Surrendered.
4) Creditors claims are to be reduced to the extent of Rs.80,000/- & in consideration they are to received Equity Shares of Re.1/- each, amounting to Rs.50,000/- from the Shares surrendered.
5) Goodwill & profit & loss A/c (Dr.) are to be written off fully.
6) The remaining surrendered shares shall be cancelled.

You are required to give the journal entries for the above & prepare Balance sheet of the company after reconstruction.

Journal entries in the books of Three Idiots Ltd.

Date	Particulars	Debit (Rs.)	Credit (Rs.)
1.	Equity Share Capital A/c (50) ………….Dr. To Equity Share Capital A/c (1) (Being 10,000 Equity Shares of Rs.50/- each sub-dividend into shares of Re.1/- each.)	5,00,000	 5,00,000
2.	Equity Share Capital A/c ……………….Dr. To Share Surrendered A/c (Being surrender of 80% of shares.)	4,00,000	 4,00,000
3.	Shares Surrendered A/c ………………. Dr.	1,00,000	

	To 8% Preference Share Capital A/c (Being converted Rs.1,00,000/- shares surrendered into 80% Preference Shares Capital.)		1,00,000
4.	10% Debentures A/c ……………………Dr. Interest Debenture A/c ………………… Dr. To Capital Reduction A/c (Being reduction in the claim of debenture holders.)	2,00,000 20,000	 2,20,000
5.	Share Surrendered A/c ………………...Dr. To Equity Share Capital A/c (Being issued to Creditors out of surrendered Shares.)	50,000	 50,000
6.	Creditors A/c ……………………………Dr. To Capital Reduction A/c (Being reduced the claim of creditors.)	80,000	 80,000
7.	Capital Reduction A/c …………………..Dr. To Goodwill A/c To Profit & Loss A/c (Being written off Goodwill & Profit & Loss Account debit balance.)	4,00,000	 1,00,000 3,00,000
8.	Shares Surrendered A/c ………………. Dr. To Capital Reduction A/c (Being cancelled remaining Surrendered Shares.)	2,50,000	 2,50,000
9.	Capital Reduction A/c …………………..Dr. To Capital Reserve A/c (Being the balance on Capital Reduction transferred to Capital Reserve.)	1,50,000	 1,50,000

Capital Reduction Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Goodwill A/c To Profit & Loss A/c To Capital Reserve A/c	1,00,000 3,00,000 1,50,000	By 10% Debentures A/c By Interest A/c By Share Surrendered A/c By Creditors A/c	2,00,000 20,000 2,50,000 80,000
	5,50,000		5,50,000

Three Idiots Ltd. (And reduced)
Balance sheet as on 1st April , 2015

Particulars	Notes	Rs.	Rs.
I. Equity and Liabilities			
1. Shareholders' Funds			
a. Share Capital	1	2,50,000	
b. Reserves and Surplus	2	1,50,000	4,00,000
2. Non-Current Liabilities			
Long Term Borrowings			
10% Debentures			3,00,000
3. Current Liabilities			
Trade Payables			1,00,000
Total			**8,00,000**
II. Assets			
1. Non current Assets			
Tangible Assets			8,00,000
Total			**8,00,000**

Notes to Accounts

Note – 1 Share Capital	Number	Rs.
Authorised Share Capital	-	-
Issued, Paid Up Share Capital		
Equity Share Capital		
Equity Shares of Re. 1 each	150000	1,50,000
Preference Shares of Rs. 10 each	10000	1,00,000
		2,50,000

Note – 2 Reserves & Surplus	Rs.	Rs.
Capital Reserve:		
(transf. from Capital Reduction A/c)		1,50,000

Illustration 7

Following is the balance sheet of Veer Ltd. as on 31st March 2015.

Liabilities	Rs.	Assets		Rs.
10,000 8% Cumulative Preference Shares of Rs.100/- each	10,00,000	Goodwill		90,000
		Patents		30,000
8,000 Equity Shares of Rs.100/- each	8,00,000	Land & Building		10,00,000
		Pant & Machinery		4,80,000
9% Debentures of Rs.100/- each (Secured on Land / Building)	7,00,000	Investment (at cost)		50,000
		Stock		4,80,000
		Debtors :		
Interest payable to debenture holders	20,000	Considered Goods	3,00,000	
Loan from Directors	2,00,000	Considered Doubtful	70,000	3,70,000
Creditors	3,00,000	Cash		5,000

UTI Bank Overdraft	2,80,000	Preliminary Expenses Profit & Loss A/c	95,000 7,00,000
	33,00,000		33,00,000

Contingent Liabilities:

1) Claims for damages pending in the court totaling Rs.1,00,000/-
2) Arrears of Preference dividend Rs.30,000/-.

The board of directors agreed to present the realistic picture of the state of affairs of the company's position & the following scheme of reconstruction was duly approved.

1) The Preference shares were to be reduced to an equal number of fully paid Preference Shares of Rs.50/- each. Equity Share to an equal number of fully paid Equity Shares of Rs.30/- each.
2) All intangible assets, including patents to be written off.
3) Stock to be revalued at Rs.4,00,000/- & debtors considered doubtful to be written off.
4) Preference Shareholders agreed to waive half of the arrears of dividends & to receive Equity Shares in lieu of the balance.
5) Debenture holder agreed to take over part of the security of the book value of Rs.2,00,000/- for Rs.2,00,000/- in satisfaction of part of their claim & to provide further cash of Rs.1,00,000/- after deducting arrears of interest due to them on floating charge of the rest of the assets.
6) The contingent liability for claims for damage pending in the court of law materialized to the full extent. However, the company could recover Rs.80,000/- from those who were responsible for such damages & settled the rest by issuing Equity Shares.
7) The Directors agreed to convert the loan into Equity Shares.

You are required to prepare –

i) Capital Reduction Account
ii) The Balance sheet after reconstruction

Solution:

In the books of Veer Ltd.

Capital Reduction Account

Dr. **Cr.**

Particulars	**Amt.**	**Particulars**	**Amt.**
To Goodwill A/c	90,000	By Preference Share	
To Patents	30,000	Capital A/c	5,00,000
To Preliminary		By Equity Share	
Expenses A/c	95,000	Capital A/c	5,60,000

To Profit & Loss A/c	7,00,000	By Cash A/c (claim recovery)	80,000
To Stock (4,80,000 - 4,00,000)	80,000	By Land & Building A/c (3,00,000 - 2,00,000)	1,00,000
To Debtors	70,000		
To Preference Dividend A/c	1,50,000		
To Cash A/c (damages)	80,000		
To Damages A/c	20,000		
To Capital Reserve A/c	60,000		
	12,40,000		12,40,000

Working Note:

1) Equity Shares @ Rs.30/- each

	Nos.	Amount
Original (at Reduced Value)	8,000	2,40,000
Issued against arrears of Preference Dividend	500	15,000
Issued against claim for Damages	666.67	20,000
Loan from Directors converted	6,666.67	2,00,000
Closing Balance	15,833	4,75,000

2) **Cash Account**

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Balance b/d	5,000	By Debenture interest A/c	20,000
To Damages Claim A/c	80,000	By Recovery A/c	80,000
To Debenture holders A/c	1,00,000	By Balance c/d	85,000
	1,85,000		1,85,000

3) It is assumed that the debenture holder brought in gross Rs.1,00,000/- without deducting Rs.20,000/- for arrears of interest.

4) 9% debenture holders

	Amount
Balance	7,00,000
Less : Land / Building taken over	3,00,000

Add : Further Cash brought in	4,00,000 1,00,000
Closing Balance	5,00,000

Veer Ltd. (And reduced)
Balance Sheet as on 1st April 2015

Particulars	Notes	Rs.	Rs.
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1	9,75,000	
b. Reserves & Surplus	2	60,000	10,35,000
2. Non-Current Liabilities			
Long Term Borrowings			5,00,000
(Secured 9% Debentures)			
3. Current Liabilities			
a. Trade Payables			
b. Short -Term Liabilities		3,00,000	
(UTI Bank Overdraft)		2,80,000	5,80,000
Total			**21,15,000**
II. ASSETS			
1. Non current Assets			
a. Fixed Assets			
- i. Tangible Assets	3		12,80,000
b. Non Current Investment			50,000
2. Current Assets			
a. Inventories		4,00,000	
b. Trade Receivables	4	3,00,000	
c. Cash & Cash Equivalents		85,000	7,85,000
Total			**21,15,000**

Notes to Accounts

Note – 1 Share Capital	**Number**	**Rs.**
Authorised Share Capital		
Issued, Paid Up Share Capital		
Equity Share Capital		
Equity Shares of Rs. 30/- each	15,833	4,75,000
Preference Share Capital		
8 % Pref. Share of Rs. 50/- each	10,000	5,00,000
		9,75,000

Note – 2 Reserves & Surplus	**Rs.**	**Rs.**

Capital Reserve: Balance (transf. from Capital Reduction A/c)		60,000

Note – 3 Tangible Assets	Rs.	Rs.
Land & Building Less: Given to Debenture holders	10,00,000 2,00,000	8,00,000
Plant & Machinery		4,80,000
		12,80,000

Note – 4 Trade Receivables	Rs.	Rs.
Balance (Unsecured, Considered Good)		3,00,000

Illustration 8

Monaco Ltd. had adverse trading for past few years resulting in accumulated losses & over valued assets. It's Balance Sheet as on 31st March 2015 is as follows.

Liabilities	Rs.	Assets	Rs.
Share Capital (in shares of Rs.10/- each)		Goodwill	60,000
50,000 Equity Share Capital	5,00,000	Freehold Property	70,000
40,000 Preference Share Capital	4,00,000	Leasehold Property	1,50,000
Securities Premium	30,000	Plant	1,40,000
12% Debenture	1,20,000	Investment	80,000
Accrued Interest	10,000	Stock	1,00,000
Creditors	1,10,000	Debtors	5,00,000
Overdraft	1,30,000	Profit & Loss A/c	2,00,000
	13,00,000		13,00,000

Note : Preference dividend is unpaid for past three years.

The shareholders & the court approved the following scheme of reconstruction.

1) The paid – up value of preference shares and Equity shares was to be reduced by 50% & 85% respectively. The face value will remain unchanged.

2) The Preference dividend for one years is to be paid by allotment of Equity shares credited Rs.2/- per share. The remaining amount to be cancelled.
3) The debenture holders took over Freehold property which was mortgaged in their favour. This property realized Rs.1,40,000/-. The balance amount after adjusting principal & interest was handed over to the company.
4) The investments are sold for Rs.1,00,000/-.
5) Obsolete Stock worth Rs.25,000/- & irrecoverable debt worth Rs.15,000/- are to be written off along with goodwill & profit & loss A/c.
6) There was a claim against company not provided to the extent of Rs.1,00,000/-. This was settled for Rs.83,000/-.
7) A call @ Rs.3/- per share on revised Equity & Preference shares was made. This was paid by all shareholders.
8) The authorized capital was suitably revised from Rs.8,00,000/- to Rs.12,00,000/- which was equally divided between Equity & 8% Preference shares.
9) Remaining bank balance to be utilized to pay bank overdraft.

You are required to show journal entries & balance sheet after implementation of the scheme.

Solution:

Journal in the books of Monaco Ltd.

Sr. No.	Particulars	Debit (Rs.)	Credit (Rs.)
1.	8% Preference Share Capital A/c ……Dr. To Capital Reduction A/c (Being reduced Preference share by 50%.)	2,00,000	 2,00,000
2.	Equity Share Capital A/c …………….. Dr. To Capital Reduction A/c (Being 50,000 Equity shares of Rs.10/- each reduced by 75%.)	4,25,000	 4,25,000
3.	Capital Reduction A/c ……………….. Dr. To Equity Share Capital A/c (Being 10,667 Equity shares of Rs.3/- each allotted to satisfy the arrears of preference dividend for 1 year.)	32,000	 32,000
4.	12% Debenture A/c ………………….. Dr. Accrued Interest on Debenture A/c … Dr. Bank A/c ………………………………. Dr. To Freehold Property A/c To Capital Reduction A/c	1,20,000 10,000 10,000	 70,000 70,000

	(Being Freehold property of Rs.70,000/- taken by debenture holders, remaining amount paid by the debenture holders.)		
5.	Bank A/c ………………………………. Dr. To Investment A/c To Capital Reduction A/c (Being sold out investments at a profit of Rs.20,000/-.)	1,00,000	 80,000 20,000
6.	Capital Reduction A/c …………………Dr. To Stock A/c To Debtors A/c To Goodwill A/c To Profit & Loss A/c (Being written off Stock, Debtors, Goodwill & Profit and Loss debit balance as agreed upon.)	3,00,000	 25,000 15,000 60,000 2,00,000
7.	Capital Reduction A/c …………………Dr. To Bank A/c (Being settled the claim.)	83,000	 83,000
8.	Preference Share Call A/c ……………Dr. To 8% Preference Share Capital A/c (Being made a call on 40,000 Preference Share @ Rs.3/- each.)	1,20,000	 1,20,000
9.	Equity Share Call A/c …………………Dr. To Equity Share Capital A/c (Being made a call on 66,000 Equity shares @ Rs.3/- each.)	1,98,000	 1,98,000
10.	Bank A/c ………………………………. Dr. To Preference Share Call A/c To Equity Share Call A/c (Being collected call money.)	3,18,000	 1,20,000 1,98,000
11.	Bank A/c ………………………………. Dr. To Bank A/c (Being cleared Bank overdraft.)	1,30,000	 1,30,000
12.	Capital Reduction A/c…………………Dr. To Capital Reserve A/c (Being Capital Reserve account closed)	3,00,000	 3,00,000

Capital Reduction Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Equity Share Capital A/c	32,000	By Preference Capital A/c	2,00,000
To Stock A/c	25,000	By Equity Share Capital	

To Debtors A/c	15,000	A/c	4,25,000
To Goodwill A/c	60,000	By 12% Debenture A/c	70,000
To Profit & Loss A/c	2,00,000	By Bank A/c	20,000
To Bank A/c	83,000		
To Capital Reserve A/c	3,00,000		
	7,15,000		7,15,000

Bank Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Freehold Property A/c	10,000	By Capital Reduction A/c	83,000
To Investment A/c	80,000	By Bank overdraft A/c	1,30,000
To Capital Reduction A/c	20,000	By Balance c/d	2,15,000
To Preference Share Capital A/c	1,20,000		
To Equity Share Capital A/c	1,98,000		
	4,28,000		4,28,000

Monaco Ltd. (And reduced)
Balance Sheet as on 1st April, 2015

Particulars	Notes	Rs.	Rs.
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
a. Share Capital	1	6,25,000	
b. Reserves & Surplus	2	3,30,000	9,55,000
2. Current Liabilities			
a. Trade Payables			1,10,000
Total			**10,65,000**
II. ASSETS			
1. Non current Assets			
a. Fixed Assets			
- i. Tangible Assets	3		2,90,000
2. Current Assets			
a. Inventories	4	75,000	
b. Trade Receivables	5	4,85,000	

c. Cash & Cash Equivalents		2,15,000	7,75,000
Total			**10,65,000**

Note – 1 Share Capital	**Number**	**Rs.**
Authorised Share Capital		
Equity Share of Rs.10/- each	60,000	6,00,000
8% Preference share of Rs.10/- each	60,000	6,00,000
	1,20,000	**12,00,000**
Issued, Paid Up Share Capital		
Equity Share Capital		
Equity Shares of Rs. 10/- each Rs.5/- paid up	61,000	3,05,000
Preference Share Capital		
8 % Pref. Share of Rs. 10/- each	32,000	3,20,000
		6,25,000

Note – 2 Reserves & Surplus	**Rs.**	**Rs.**
Security Premium: Balance	30,000	
Capital Reserve: (transf. from Capital Reduction A/c)	3,00,000	3,30,000

Note – 3 Tangible Assets	**Rs.**	**Rs.**
Leasehold Property	1,50,000	
Plant & Machinery	1,40,000	2,90,000

Note – 4 Inventories	**Rs.**	**Rs.**
Balance	1,00,000	
Less : written off	-25,000	
		75,000

Note – 5 Trade Receivables	**Rs.**	**Rs.**
Balance	5,00,000	
Less : written off	-15,000	
		4,85,000

Illustration 9

The paid – up Capital of Fast traler Ltd. amounted to Rs.12,00,000/- consisting of 6,000 – 5% Cumulative Shares of Rs.100/- each and 60,000 Equity Shares of Rs.10/- each. The Preference dividend was in arrears for Rs.80,000/- (Contingent Liability)

The company incurred heavy losses continuously. Therefore, the Directors recommended to the shareholders the following scheme of reconstruction to provide a sum sufficient for the following purpose :

1) To write down the book value of Patents by Rs.2,00,000/-, Plant & Machinery by Rs.24,000/- and Tools & Equipments by Rs.8,000/-.
2) To write off the debit balance of Profit & Loss Account of Rs.2,96,000/-.
3) Any balance made available by the reduction of capital is to be utilized to write off "Experiment & research expenses"
4) The scheme duly approved & authorized provided the following.
   i) For every 15, 5% Preference Shares, 8 – 4% Cumulative Preference Shares of Rs.100/- each & 40 Equity shares of Rs.2/- each are to be issued.
   ii) For every Rs.20/- of Cumulative Preference Divided; 2 Equity shares of Rs.3/- each are to be issued.
   iii) For every 10 old Equity shares, 2 new Equity shares of Rs.2/- each are to be issued.

You are required to:

Pass journal entries in the books of the company to record the above transactions. Prepare Capital Reduction Account.

Solution:

Journal of Fast Traler Ltd.

Date	Particulars	Debit (Rs.)	Credit (Rs.)
1.	5% Preference Share Capital A/c ………Dr.	6,00,000	
	To 4% Cumulative Preference Share Capital A/c		3,20,000
	To Equity Share Capital A/c		48,000
	To Capital Reduction A/c		2,32,000
	(Being issued 3200, 4% Preference shares of Rs.100/- each & 24,000 Equity Shares of 5% Preference shares Capital.		
2.	Capital Reduction A/c ………………………Dr.	18,000	
	To Equity Share Capital A/c		18,000
	(Being issued 6,000 Equity shares of Rs.3/- each in settlement of arrears of Preference		

	dividend.)		
3.	Equity Share Capital A/c ……………………Dr.	6,00,000	
	To Equity Share Capital A/c		24,000
	To Capital Reduction A/c		5,76,000
	(Being issued 12,000 Equity share of Rs.2/- each to the existing Equity shareholders.)		
4.	Capital Reduction A/c ………………………Dr.	7,96,000	
	To Patents A/c		2,00,000
	To Plant & Machinery A/c		24,000
	To Tools & Equipment A/c		8,000
	To Profit & Loss A/c		2,96,000
	To Experiment & Research Expenses A/c		2,68,000
	(Being written off Patents, Plant & Machinery, Tools & Equipments, Profit & Loss A/c, Debit balance & Experiment & Research Expenses as agreed upon.)		

Capital Reduction Account

Dr. **Cr.**

Particulars	Amt.	Particulars	Amt.
To Equity Share Capital A/c	18,000	By 5% Preference Share Capital A/c	2,32,000
To Patents A/c	2,00,000	By Equity Share Capital A/c	5,76,000
To Plant & Machinery A/c	24,000		
To Tools & Equipment A/c	8,000		
To Profit & Loss A/c	2,96,000		
To Experiment & Research Expenses A/c	2,62,000		
	8,08,000		8,08,000

12.2 EXERCISES:

12.2.1 OBJECTIVES QUESTIONS

- **Filling the blanks.**

1) Capital Reduction is implemented per section ____________ of Companies Act.

2) The scheme of Capital reduction is to be approved by ____________ .
3) Fictitious assets are to be transferred to ____________ .
4) Balance in Capital Reduction should be transferred to ____________ .
5) The payment for contingent liability should be debited to ____________ .
6) And reduced words are to be shown as in Balance sheet as per ____________ required.
7) XYZ Ltd. has on 31st March, 2015 1,00,000 Equity shares at Rs.10/- each. It was decided to reduced share to Rs.8/- each. The reduction is ____________ .
8) The Preference shareholders agree to Forgo arrears of Preference dividend Rs.80,000/-. The amount transferred to Capital Reduction Account is ____________ .
9) Investment costing of Rs.36,000/- given to Bank for bank overdraft Rs.19,800/-. The Capital reduction is debited by Rs. ____________ .
10) Provision for taxation is Rs.1,62,000/-. The tax liability of the company is settled at Rs.1,40,000/- & it is paid immediately. Amount credited to Capital Reduction is ____________ .

(Ans – 1) 100, 2) High court, 3) Internal Reconstruction, 4) Capital Reserve, 5) Capital Reduction, 6) Company law, 7) 2,00,000, 8) Nil, 9) 16,200, 10) 22,000.)

1) The capital reduction means reduction in ____________ value of shares.
2) The sub division of shares does not result in ____________ of capital.
3) The shareholders can surrender shares for ____________ or ____________ .
4) The internal reconstruction results in proper valuation of ____________ & ____________ of company.
5) ____________ resolution is to be passed by shareholders for approval of scheme or reconstruction.
6) The Fictitious debit balances are to be transferred to ____________ Account.
7) The full balance of Capital is to be debited, if ____________ value is reduced.
8) Shareholders not approving scheme is called ____________ shareholders.
9) The expenses for forming & implementing scheme should be debited to ____________ .

10) The scheme of internal reconstruction can be utilized to provide ____________ for the company.

(Ans – 1) Paid-up Value, 2) Reduction, 3) Re-issue, cancellation, 4) Assets & Liability, 5) Special, 6) Capital Reduction, 7) Face, 8) dissenting, 9) Capital Reduction, 10) Funds.

- **Match the following.**

1)

Group "A"	Group "B"
1) Capital Reduction	a) Transfer to Capital Reduction
2) Fictitious Balance	b) Section 100
3) Capital Reduction Scheme	c) No reduction of Capital
4) Consolidation of Share	d) Internal Reconstruction
5) Subdivision of Share	e) No Change in Capital

(Ans : 1 – b, 2 – a, 3 – d, 4 – e, 5 – c.)

2)

Group "A"	Group "B"
1) Surrender of share	a) Credit – Capital reduction
2) Cancellation of surrendered shares	b) Unchanged Capital
3) Surplus on revaluation of assets	c) Transfer to Capital Reserve
4) Loss on revaluation of assets	d) Transfer to Capital Reduction
5) Credit balance in Capital Reduction	e) Debit Capital Reduction

(Ans : 1 – b, 2 – a, 3 – c, 4 – e, 5 – d.)

3)

Group "A"	Group "B"

1) Balance sheet after reduction 2) Statutory Reserve 3) Expenses of Scheme 4) Reduction in paid up value of shares 5) Reduction in face value of debenture	a) Not transferable to Capital Reduction b) Transfer difference to Capital Reserve c) Cancel present capital, raise new capital & difference to reduction d) Indicate, & reduced E) Debit capital reduction account

(Ans – 1 – d, 2 – a, 3 – e, 4 – b, 5 – c.)

- **True or False.**

1) Capital Reduction & Internal reconstruction is synonym. – True
2) Consolidation of shares result in profit for a company. – False
3) Sub – division of shares result in gain for a company. – False
4) Provision for unrecorded liability indicates loss to a company. – True
5) Accounting for Internal & External reconstruction is in identical manner. – False
6) Authorised Share Capital is to be reduced to the extent of Capital Reduction. – False
7) Cancellation of contingent liability is treated as profit to the company. – False
8) Re – classification of surrendered shares should not be accounted. – True
9) The requirements of schedule VI is to be complied while preparing account after internal reconstruction. – True
10) Internal reconstruction scheme cannot be prepared to cover capital reconstruction. – False

12.2.2 PROBLEMS FOR PRACTICE

1) Following is the balance sheet of Harshal Ltd. as on 31st March, 2015.

Liabilities	Rs.	Assets	Rs.
6,000 10% Cumulative Preference Share of Rs.100/- each fully paid up	6,00,000	Goodwill	2,00,000
		Land & Building	19,50,000
		Plant & Machinery	70,000
		Stock	4,00,000
15,000 Equity share		Trade Debtors	2,88,000

of Rs.100/- each, fully paid up Loans Creditors	15,00,000 2,22,000 7,50,000	Bank Balance Profit & Loss A/c	1,26,000 38,000
	30,72,000		30,72,000

Note: Preference dividend was in arrears Rs.1,20,000/-. The Board of Directors of the company decided upon the following scheme of reconstruction, which was approved by all concerned.

1) Paid up value of Equity shares shall be reduced to Rs.50/- per share, face value being Rs.100/-.
2) Preference shares are to be converted into 13% debentures of Rs.100/- each with regard to their 80% of dues (including arrears of Preference dividend) & for the balance (including dividend arrears) Equity, shares of Rs.100/- each (Rs.50/- paid up shall be issued.)
3) All Equity shareholders agreed to pay the balance amount, making shares full paid up.
4) The Plant & Machinery was revalue at Rs.90,000/-.
5) The value of Stock was reduced by Rs.1,00,000/-.
6) Land & Building shall be written down to Rs.15,50,000/-.
7) Creditors agreed to Forgo their claims by 10%.
8) Loans was fully settled for Rs.2,00,000/-.
9) Goodwill, debit balance of profit & loss Account shall be written off.
10) Cost of reconstruction of Rs.5,000/- was paid.

Above resolution was carried out

You are required to:

i) Pass journal entries in the books of the company.
ii) Prepare Capital Reduction Account
iii) Prepare Balance sheet after reconstruction

(Ans : Capital Reserve – Rs.4,000/-, Tally – 30,43,000/-)

2) The ledger balance of ZEE TV Ltd. include Building Rs.6,10,000/-, Furniture Rs.2,00,000/-, Computer Rs.3,00,000/-, Debtors Rs.3,00,000/-, Preliminary Expenses Rs.20,000/-, Cash at Bank Rs.80,000/-, Bills Receivable Rs.2,50,000/-, Stock Rs.40,000/-, 8% Preference Share Capital – 2,000 shares Rs.100/- each, Equity Share Capital – 80,000 shares of Rs.10/- each, 'A' 10% Debentures Rs.4,00,000/-, 'B' 12% Debenture Rs.5,00,000/-, Outstanding Interest for one year on Debentures Rs.1,00,000/-.

Creditors Rs.4,00,000/-, Bills Payable Rs.50,000/-, Outstanding Audit Fees Rs.50,000/-, Profit & Loss Account

The company has incurred heavy losses. The following scheme of reconstruction is agreed upon.

1) 8% Preference shares are to be reduced by Rs.20/- per share, Equity shares be reduced by Rs.5/- per share.
2) To settle the claim of holders of 'A' 10% Debenture by issue of new 11% Debenture of Rs.2,00,000/-, 'A' Debenture holders agree to forgo their interest.
3) To settle the claim of holders of 'B' 12% Debenture by issue of new 13% Debenture of Rs.5,00,000/- outstanding Debenture interest on 'B' 12% Debenture holders be paid.
4) To write off Fictitious assets & debit balance of Profit & Loss Account.
5) Director refund Rs.60,000/- fees previously received by them.
6) Computer was to be written down by Rs.20,000/-.

You are required to show :

a) Journal entries to record the above transactions in books of ZEE Ltd.
b) Balance sheet before reconstruction
c) Balance sheet after reconstruction.

Assume that all the formalities are duly complied.

(Ans : Balance sheet before reconstruction Tally – Rs.25,00,000/-, Balance sheet after reconstruction Tally – Rs.17,60,000/-, Capital Reduction – Rs.7,40,000/-.)

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5

FINAL ACCOUNTS OF LIMITED COMPANIES-I

Unit Structure

15.0 OBJECTIVES:

After studying the unit the students will be able to:

- Understand the methods of preparation of Final Accounts.
- Understand Revised Schedule VI of companies Act
- Know the Requirements to Balance Sheet.
- Know the Requirements to Profit and Loss Account.
- Know the Account Standard I
- Understand the various adjustments
- Solve the practical Problems.

15.1 INTRODUCTION

Every Organization or entity which maintains the books of accounts day to day transactions needs to prepare the Final Accounts at the end of Interval - normally one year.

15.1.1 THE FINAL ACCOUNTS COMPRISES:

I. Profit and Loss Account showing Income, expenses, gains and losses pertaining to the period.

II. Balance sheet enlisting assets, receivables, payables and capital on the specific date.

These accounts or statement has to be prepared in accordance with the requirements of provisions of the law; applicable to it.

In addition to these, these accounts also need to comply with the statements and standard issued by The Institute of Chartered Accountants of India to the extent these are relevant on applicable.

The preparation and presentation of final accounts is essential for all entity irrespective of the form of organization and nature and volume of transactions.

The Objective of preparation of Final Accounts is to satisfy or ensure that these represent a true and fair view of affairs and profits of the entity.

15.2 THE METHOD OF PREPARATION OF FINAL ACCOUNTS:

Irrespective of the form of organization and nature of activity, some of the steps involved for this purpose are commonly applicable to all.

These Steps are: -

15.2.1 PREPARATION OF TRIAL BALANCE

Enlisting all balances extracted from books of accounts maintained during the specified period. This step is to satisfy that the arithmetic accuracy of accounting process is ensured.

15.2.2 SCRUTINISE THE ACCOUNTS

To ensure that the proper accounting effect is made for the following-

i. Provision is made for all unpaid expenses and outstanding income.
ii. Advance receipts of income, pre - payment of expenses is properly segregated.
iii. Accounting Errors - particularly affecting capital and revenue items are identified and rectified.
iv. Provision for all known losses, such as loss by fire or accident, depreciation, devaluation of investments, profit or

loss on sale of investments or assets is shown in the accounts.

v. Statutory Provisions as required under applicable laws e.g. Transfer to Reserve, Dividend, Tax.

15.2.3 Compliance with Accounting Standards (AS) and Statements issued by the Institute of Chartered Accountants of India (ICAI)

The ICAI has issued several Standards and Statements to ensure the uniformity in prepare at and presentation of Final Accounts. In many cases, it is mandatory or compulsory to comply with these, Statements and Standards. The ICAI while issuing such Statements and Standards, specify the type of entity and accounting period covered by the same and also extent to which it is mandatory.

These Standards can he categorized as: -

a) Basic subject matters for preparation and presentation of Final Accounts which has general application eg.

i. Disclosure of Accounting Policies (AS 1)
ii. Valuation of inventories (AS 2)
iii. Depreciation (AS 6)
iv. Revenue Recognition (AS 9)
v. Fixed Assets (AS 10)
vi. Investments (AS 13)
vii. Prior Period - items (AS 5)
viii. Income Tax (AS 22)
ix. Intangible Assets (AS 26)
x. Contingencies & events after Balance Sheet (AS 4)

b) Special Transaction or Items

i. Construction Contracts (AS 7)
ii. Research & Development (AS 8)
iii. Foreign Exchange Translation (AS 11)
iv. Government Grants (AS 12)
v. Retirement Benefit Scheme (AS 15)
vi. Borrowing Costs (AS 16)
vii. Segment Reporting (AS 17)
viii. Related Party (AS 18)
ix. Leases (AS 19)

x. Earnings per share (AS 20)
xi. Amalgamation (AS 14)
xii. Consolidated Statements (AS 21)
xiii. Investments in Associates etc (AS 23)
xiv. Cash Flow Statements (AS 3)
xv. Discontinuing Operation (AS 24)
xvi. Interim Financial Reporting (AS 25)
xvii. Impairment of Assets (AS 28)
xviii. Financial Reporting of interest in Joint Venture (AS 27)

Till Date, 28 AS have been issued. Of these AS enlisted as basic are Mandatory and should complied by every enterprise to whom these AS apply. The remaining AS, should be complied if there are transactions or events effected by the enterprise.

c) Statutory Requirements

Certain categories of enterprises are governed or represented by specific laws. These laws specify the provision relating to certain transactions or contracts as also form and requirements for the preparation and presentation of Final Accounts. Some such institutions are -

- Companies Act - for Companies
- Partnership Act - for Partnership Firm
- Bombay Public Trust Act - for Trusts, Associations & Societies.
- Maharashtra State Co-operative Societies Act - for Co-operative Societies
- Banking Regulation Act - for Banks
- Each of these laws require that the final Accounts prepared under these laws should
    i. Be in form prescribed under law.
    ii. Disclose the information required.

d) Forms of Presentation of Final Accounts

The final Accounts can be presented in vertical form form. - Only a vertical form of Balance Sheet is permitted.

The present syllabus requires the study of preparation and presentation of Final accounts of Companies governed under Companies Act as per revised Schedule VI. The notes have been compiled from Supplement on Revised Schedule VI issued by ICSI and guidance notes issued by ICAI

15.3 REVISED SCHEDULE VI OF COMPANIES ACT

15.3.1 Introduction to Revised Schedule VI:[1]

Every company registered under the Act shall prepare its Balance Sheet, Statement of Profit and Loss and notes thereto in accordance with the manner prescribed in Schedule VI to the Companies Act, 1956. To harmonise the disclosure requirements with the Accounting Standards and to converge with the new reforms, the Ministry of Corporate Affairs vide Notification No. S.O. 447(E), dated 28thFebruary 2011 replaced the existing Schedule VI of the Companies Act, 1956 with the revised one. Government vide Notification No. F.N. 2/6/2008 – C.L-V dated 30th March 2011 made the revised Schedule VI applicable to all companies for the financial year commencing from 01st April 2011. The requirements of the Revised Schedule VI however, do not apply to companies as referred to in the proviso to Section 211 (1) and Section 211 (2) of the Act, i.e., any insurance or banking company, or any company engaged in the generation or supply of electricity or to any other class of company for which a form of Balance Sheet and Profit and Loss account has been specified in or under any other Act governing such class of company. The pre-revised Schedule VI was introduced in 1976.

15.3.2 Need of Revised Schedule VI

As mentioned in the Foreword of the ICAI Guidance Note on Revised Schedule VI to the Companies Act, 1956 (ICAI GN), “to make Indian business and companies competitive and globally recognizable, a need was felt that format of Financial Statements of Indian corporations should be comparable with international format. Since most of the Indian Accounting Standards are being made at par with the international Accounting Standards, the changes to format of Financial Statements to align with the Accounting Standards will make Indian companies competitive on the global financial world. Taking cognizance of imperative situation and need, the Ministry of Corporate Affairs revised the existing Schedule VI to the Companies Act, 1956”

.15.3.2 Applicability of the Revised Schedule VI

As mentioned in the Notification dated 30th March 2011, financial statements for all companies have to be prepared using the format given by Revised Schedule VI for financial years commencing on or after 1st April 2011.

A company having its financial year ending on, say, **30th June 2011, 30th September 2011 or 31st December 2011**

cannot adopt the new format since their financial years have not commenced on or after 1st April 2011. Since the format of Revised Schedule VI is a statutory format, a company cannot decide to follow the same even on a voluntary basis. However, if a company decides to prepare its financial statements from 1st April 2011 to 31st December 2011 (i.e., for a period of 9 months), it will have to prepare the same using the format of Revised Schedule VI.

All companies registered under the Companies Act, 1956 have to prepare their financial statements using Revised Schedule VI. However, proviso to section 211 exempts banking companies, insurance companies and companies engaged in generation or supply of electricity from following the said format since these are governed by their respective statutes. However, since the Electricity Act 2003 and the Rules there under do not prescribe any format for preparing financial statements, such companies will have to follow the format laid down by the Revised Schedule VI till a separate format is prescribed.

Listed companies require to publish information on quarterly and annual basis in the prescribed format in terms of clauses 41(I)(ea) and 41(I)(eaa) of the Listing Agreement. These formats are inconsistent with formats under the Revised Schedule VI. However, since the formats are statutory formats as per the Listing Agreement, the same will have to be followed till the time a new format is prescribed under Clause 41 of the Listing Agreement.

Companies which are in the process of making an issue of shares (IPO/FPO) have to file ‘offer documents’ containing among other details, financial information of the last 5 years. The formats of Balance Sheet and Statement of Profit and Loss prescribed under the SEBI (Issue of Capital & Disclosure Requirements) Regulations, 2009 (‘ICDR Regulations’) are inconsistent with the format of the Balance Sheet/Statement of Profit and Loss in the Revised Schedule VI. However, since the formats of Balance Sheet and Statement of Profit and Loss under ICDR Regulations are only illustrative, to make the data comparable and meaningful for users, companies will be required to use the Revised Schedule VI format to present the restated financial information for inclusion in the offer document.

It may also be noted that the MCA had vide General Circular No. 62/2011, dated 5th September 2011 has clarified that ‘the presentation of Financial Statements for the limited purpose of IPO/FPO during the financial year 2011-12 may be made in the format of the pre-revised Schedule VI under the Companies Act, 1956. However, for period beyond 31st March 2012, they would prepare only in the new format as prescribed by the present Schedule VI of the Companies Act, 1956’.

Revised Schedule VI requires that except in the case of the first financial statements (i.e., for the first year after incorporation), the corresponding amounts for the immediately preceding period are to be disclosed in the Financial Statements including the Notes to Accounts. Accordingly, corresponding information will have to be presented starting from the first year of application of the Revised Schedule VI.

All companies whether private or public, whether listed or unlisted, and irrespective of their size in terms of turnover, assets, etc. (other than those mentioned in para 9 above) will have to adhere to the new format of financial statements from 2011-12 onwards.

15.3.3 Key Features of Revised Schedule VI –Balance Sheet

• The revised schedule contains General Instructions, Part I – Form of Balance Sheet; General instructions for Preparation of Balance Sheet, Part II – Form of Statement of Profit and Loss; General Instructions for Preparation of Statement of Profit and Loss.

• The Revised Schedule VI has eliminated the concept of 'schedule' and such information is now to be furnished in the notes to accounts.

• The revised schedule gives prominence to Accounting Standards (AS) i.e. in case of any conflict between the AS and the Schedule, AS shall prevail.

• The revised schedule prescribes a vertical format for presentation of balance sheet therefore, no option to prepare the financial statement in horizontal format. It ensures application of uniform format.

• All Assets and liabilities classified into current and non-current and presented separately on the face of the Balance Sheet.

• Number of shares held by each shareholder holding more than 5% shares now needs to be disclosed.

• Details pertaining to aggregate number and class of shares allotted for consideration other than cash, bonus shares and shares bought back will need to be disclosed only for a period of five years immediately preceding the Balance Sheet date.

• Any debit balance in the Statement of Profit and Loss will be disclosed under the head "Reserves and surplus." Earlier, any debit balance in Profit and Loss Account carried forward after deduction from uncommitted reserves was required to be shown as the last item on the asset side of the Balance Sheet.

• Specific disclosures are prescribed for Share Application money. The application money not exceeding the capital offered for issuance and to the extent not refundable will be shown separately on the face of the Balance Sheet. The amount in excess of subscription or if the requirements of minimum subscription are not met will be shown under “Other current liabilities.”

• The term “sundry debtors” has been replaced with the term “trade receivables.” ‘Trade receivables’ are defined as dues arising only from goods sold or services rendered in the normal course of business. Hence, amounts due on account of other contractual obligations can no longer be included in the trade receivables.

• The Old Schedule VI required separate presentation of debtors outstanding for a period exceeding six months based on date on which the bill/invoice was raised whereas, the Revised Schedule VI requires separate disclosure of “trade receivables outstanding for a period exceeding six months from the date the bill/invoice is due for payment.”

• “Capital advances” are specifically required to be presented separately under the head “Loans & advances” rather than including elsewhere.

• Tangible assets under lease are required to be separately specified under each class of asset. In the absence of any further clarification, the term “under lease” should be taken to mean assets given on operating lease in the case of lessor and assets held under finance lease in the case of lessee.

• In the Old Schedule VI, details of only capital commitments were required to be disclosed. Under the Revised Schedule VI, other commitments also need to be disclosed.

15.3.4 Key Features of Revised Schedule VI – Statement of Profit and Loss

• The name has been changed to “Statement of Profit and Loss” as against ‘Profit and Loss Account’ as contained in the Old Schedule VI.

• Unlike the Old Schedule VI, the Revised Schedule VI lays down a format for the presentation of Statement of Profit and Loss. This format of Statement of Profit and Loss does not mention any appropriation item on its face. Further, the Revised Schedule VI format prescribes such ‘below the line’ adjustments to be presented under “Reserves and Surplus” in the Balance Sheet.

• As per revised schedule VI, any item of income or expense which exceeds one per cent of the revenue from operations or Rs.100,000 (earlier 1 % of total revenue or Rs.5,000), whichever is higher, needs to be disclosed separately.

• In respect of companies other than finance companies, revenue from operations need to be disclosed separately as revenue from (a) sale of products, (b) sale of services and (c) other operating revenues.

• Net exchange gain/loss on foreign currency borrowings to the extent considered as an adjustment to interest cost needs to be disclosed separately as finance cost.

• Break-up in terms of quantitative disclosures for significant items of Statement of Profit and Loss, such as raw material consumption, stocks, purchases and sales have been simplified and replaced with the disclosure of "broad heads" only. The broad heads need to be decided based on materiality and presentation of true and fair view of the financial statements.

15.3.5 Major principles as per Revised Schedule VI

Revised Schedule VI has eliminated the concept of 'Schedules'. Such information will now have to be provided in the 'Notes to accounts'. Accordingly, the manner of cross-referencing to various other information contained in financial statements will also be changed to 'Note number' as against 'Schedule number' in pre-revised Schedule VI.

As per general instructions contained in the Revised Schedule VI, the terms used shall carry the meanings as per the applicable Accounting Standards (AS). As per ICAI GN, the applicable AS for this purpose shall mean the AS notified by the Companies (Accounting Standards) Rules, 2006.

Revised Schedule VI requires that if compliance with the requirements of the Companies Act, 1956 (Act) and/or AS requires a change in the treatment or disclosure in the financial statements, the requirements of the Act and/or AS will prevail over Revised Schedule VI.

As per preface to the AS issued by ICAI, if a particular AS is not in conformity with law, the provisions of the said law or statute will prevail. Using this principle, disclosure requirements of existing Schedule VI were considered to prevail over AS. However, since the Revised Schedule VI gives specific overriding status to the requirements of AS notified by the Companies (Accounting Standards) Rules, 2006, the same would prevail over the Revised Schedule VI.

There are several instances of conflict between provisions of the Revised Schedule VI and the notified AS e.g., definition of Current Investments as per the Revised Schedule VI and AS-11, definition of Cash and Cash Equivalents as per the Revised Schedule VI and AS-3, treatment of proposed dividend as per the Revised Schedule VI and AS-4, etc. In all such cases, provisions of the AS will prevail over the Revised Schedule VI.

The nomenclature for the Profit and Loss account is now changed to 'Statement of Profit and Loss'. Also, only the vertical format is prescribed for both Balance Sheet and the Statement of Profit and Loss.

The format of the Statement of Profit and Loss as per the Revised Schedule VI does not contain disclosure of appropriations like transfer to reserves, proposed dividend, etc. These are now to be disclosed in the Balance Sheet as part of adjustments in 'Surplus in Statement of Profit and Loss' contained in 'Reserves and Surplus'. Further, debit balance of 'profit and loss account', if any, is to be disclosed as a reduction from 'Reserves and Surplus' (even if the final figure of Reserves and Surplus becomes negative).

It is clarified by the Revised Schedule VI that the requirements mentioned therein are minimum requirements. Thus, additional line items, sub-line items and sub-totals can be presented as an addition or substitution on the face of the financial statements if the company finds them necessary or relevant for understanding of the company's financial position. Also, in preparing the financial statements, a balance will have to be maintained between providing excessive detail that may not assist users of the financial statements and not providing important information as a result of too much aggregation.

Revised Schedule VI requires use of the same unit of measurement uniformly throughout the financial statements and 'Notes to Accounts'. Rounding off requirements, if opted, are to be followed uniformly throughout the financial statements and 'Notes to Accounts'. The rounding off requirements as per prerevised Schedule VI and as per the Revised Schedule VI are summarized in the following table:

Pre-revised Schedule VI	Revised Schedule VI
Turnover less than Rs.100 crore Round off to the nearest hundreds, thousands or decimal there of	Turnover < Rs.100 crore Round off to the nearest hundreds, thousands, lakhs or millions or decimal thereof.

Turnover Rs.100 to 500 crore Round off to the nearest hundreds, thousands, lakhs or millions or decimal thereof	Turnover over Rs.100 crore Round off to the earest lakhs, millions or crores, or decimal thereof.
Turnover over Rs.500 crore Round off to the nearest hundreds, thousands, lakhs, millions or crores, or decimal thereof.	

15.3.6 Disclosures not required in the Revised Schedule VI

The disclosure requirements as per the Revised Schedule VI do not contain several disclosures which were required by pre-revised Schedule VI. Some of these are:

(a) Disclosures relating to managerial remuneration and computation of net profits for calculation of commission;

(b) Information relating to licensed capacity, installed capacity and production;

(c) Information on investments purchased and sold during the year;

(d) Investments, sundry debtors and loans & advances pertaining to companies under the same management;

(e) Maximum amounts due on account of loans and advances from directors or officers of the company;

(f) Commission, brokerage and non-trade discounts; and

(g) Information as required under Part IV of pre-revised Schedule VI.

15.3.7 Disclosures required as per Revised Schedule VI

It should be noted that besides the format for preparation of Balance Sheet and Profit and Loss statement as notified by the Revised Schedule VI, there are other disclosure requirements also. These disclosures are:

(a) Disclosures as per the notified Accounting Standards i.e., as per the Companies (Accounting Standards) Rules, 2006;

(b) Disclosures under the Companies Act, 1956 (e.g., on buyback of shares — section 77, political contributions — section 293, etc.);

(c) Disclosures under Statutes (e.g., as per the Micro, Small and Medium Enterprises Development Act, 2006);

(d) Disclosures as per other ICAI pronouncements (e.g., disclosure on MTM exposure for derivatives);

(e) In case of listed companies, disclosures under Clause 32 of the Listing Agreement (e.g., Loans to associate companies, etc.)

15.3.8 COMPARITIVE ANALYSIS BETWEEN OLD SCHEDULE VI AND REVISED SCHEDULE VI

POINTS	OLD SCHEDULE VI	REVISED SCHEDULE VI
Parts	Part I (Balance Sheet), Part II (Profit and Loss Account), Part III (Interpretation) and Part IV (Balance sheet Abstract of company's general business)	Only two parts- Part I(Balance Sheet) and Part II (Statement of Profit and Loss) Part III (Interpretation) and Part IV (Balance sheet Abstract of company's general business profile) omitted
Format of Balance Sheet	Horizontal and Vertical formats are prescribed.	Only vertical format is prescribed.
Rounding off (R/off) of Figures appearing in financial statement	(a) Turnover of less than Rs. 100 Crs - R/off to the nearest Hundreds, thousands or decimal thereof (b) Turnover of Rs. 100 Crs or more but less than Rs. 500 Crs - R/off to the nearest Hundreds, thousands, lakhs or millions or decimal there of (c)Turnover of Rs. 500 Crs or more - R/off to the nearest Hundreds, thousands, lakhs, millions or crores, or decimal thereof	(a)Turnover of less than Rs. 100 Crs - R/off to the nearest Hundreds, thousands, lakhs or millions or decimal thereof (b)Turnover of Rs. 100 Crs or more - R/off to the nearest lakhs, millions or crores, or decimal thereof
Net Working Capital	Current assets & Liabilities are shown together under application of funds. The net working capital appears on balance sheet.	Assets & Liabilities are to be bifurcated into current & Non-current and to be shown separately. Hence, net working capital will not be appearing on Balance sheet.

Fixed Assets	There was no bifurcation required into tangible & intangible assets.	Fixed assets to be shown under noncurrent assets and it has to be bifurcated into Tangible & intangible Assets.
Borrowings	Short term & long term borrowings are grouped together under the head Loan funds subhead Secured / Unsecured	Long term borrowings to be shown under non-current liabilities and short term borrowings to be shown under current liabilities with separate disclosure of secured / unsecured loans. Period and amount of continuing default as on the balance sheet date in repayment of loans and interest to be separately specified
Finance lease Obligation	Finance lease obligations are included in current liabilities	Finance lease obligations are to be grouped under the head non-current liabilities
Deposits	Lease deposits are part of loans & advances	Lease deposits to be disclosed as long term loans & advances under the head non-current assets
Investments	Both current & non-current investments to be disclosed under the head investments	Current and non-current investments are to be disclosed separately under Current assets & non-current assets respectively.
Loans & Advances	Loans & Advance are disclosed along with current assets	Loans & Advances to be broken up in long term & short term and to be disclosed under non-current & current assets respectively.
Cash & Bank Balances	Bank balance to be bifurcated in scheduled banks & others	Bank balances in relation to earmarked balances, held as margin money against borrowings, deposits with more than 12 months maturity, each of these to be shown separately.
Profit & Loss (Dr Balance)	P&L debit balance to be shown under the head Miscellaneous expenditure & losses.	Debit balance of Profit and Loss Account to be shown as negative figure under the head Surplus. Therefore, reserve & surplus balance can be negative.

Sundry Creditors	Creditors to be broken up in to micro & small suppliers and other creditors	It is named as Trade payables and there is no mention of micro & small enterprise discl.
Other current liabilities	No specific mention for separate disclosure of Current maturities of long term debt. No specific mention for separate disclosure of Current maturities of finance lease obligation	Current maturities of long term debt to be disclosed under other current liabilities. Current maturities of finance lease obligation to be disclosed.
Separate line item Disclosure criteria	any item under which expense exceeds one per cent of the total revenue of the company or Rs.5,000 whichever is higher; shall be disclosed separately	any item of income / expense which exceeds one per cent of the revenue from operations or Rs. 1,00,000, whichever is higher; to be disclosed separately
Expense classification	Function wise & nature wise	Expenses in Statement of Profit and Loss to be classified based on nature of expenses
Finance Cost	Finance cost to be classified in fixed loans & other loans	Finance cost shall be classified as interest expense, other borrowing costs & Gain / Loss on foreign currency transaction & translation.

15.4 FORMAT OF REVISED SCHEDULE VI

The Ministry of Corporate Affairs specified the format of Schedule VI vide Notification No. S.O. 447(E), dated 28th February 2011 as follows:
A. General Instructions
B. Part I – Form of Balance Sheet
C. General Instructions for Preparation of Balance Sheet
D. Part II – Form of Statement of Profit and Loss
E.General Instructions for Preparation of Statement of Profit and Loss

15.4.1 A. General Instructions

1. Where compliance with the requirements of the Act, including the Accounting Standards as applicable to companies, requires any change in treatment or disclosure including addition, amendment,

substitution or deletion in the head / sub-head or any changes inter se, in the financial statements or statements forming part thereof, the same shall be made and the requirements of the Schedule VI shall stand modified accordingly.

2. The disclosure requirements specified in Parts I and II of this Schedule are in addition to and not in substitution of the disclosure requirements specified in the Accounting Standards prescribed under the Companies Act, 2013. Additional disclosures specified in the Accounting Standards shall be made in the notes to accounts or by way of additional statement unless required to be disclosed on the face of the Financial Statements. Similarly, all other disclosures as required by the Companies Act, 2013 shall be made in the notes to accounts in addition to the requirements set out in this Schedule.

3. Notes to accounts shall contain information in addition to that presented in the Financial Statements and shall provide where required:

(a) Narrative descriptions or disaggregation of items recognized in those statements and

(b) Information about items that do not qualify for recognition in those statements.

Each item on the face of the Balance Sheet and the Statement of Profit and Loss shall be cross-referenced to any related information in the notes to accounts. In preparing the Financial Statements including the notes to accounts, a balance shall be maintained between providing excessive detail that may not assist users of financial statements and not providing important information as a result of too much aggregation.

4. Depending upon the turnover of the company, the figures appearing in the Financial Statements may be rounded off as below:

Turnover	Rounding off
(i) less than one hundred crore rupees	To the nearest hundreds, thousands, lakhs or millions, or decimals thereof.
(ii) one hundred crore rupees or more	To the nearest lakhs, millions or crores, or decimals thereof
Once a unit of measurement is used, it should be used uniformly in the Financial Statements.	

5. Except in the case of the first Financial Statements laid before the Company (after its incorporation), the corresponding amounts (comparatives) for the immediately preceding reporting period for all items shown in the Financial Statements including notes shall also be given.

6. For the purpose of this Schedule, the terms used herein shall be as per the applicable Accounting Standards. This part of Schedule sets out the minimum requirements for disclosure on the face of the Balance Sheet and the Statement of Profit and Loss (hereinafter referred to as "Financial Statements" for the purpose of this Schedule) and Notes. Line items, sub-line items and sub-totals shall be presented as an addition or substitution on the face of the Financial Statements when such presentation is relevant to an understanding of the Company's financial position or performance or to cater to industry / sector specific disclosure requirements or when required for compliance with the amendments to the Companies Act, 2013 or under the Accounting Standards

15.5 B. FORMAT OF BALANCE SHEET AS PER REVISED SCHEDULE VI

Name of the Company

Balance Sheet as at 31 March,20X2				
	Particulars	Note No.	Figures for the current period	Figures for the previous period
A	**EQUITY AND LIABILITIES**			
1	Shareholders' funds			
	(a) Share capital	A		
	(b) Reserves and surplus	B		
	(c) Money received against share warrants			
2	Share application money pending allotment			
3	Non-current liabilities			
	(a) Long-term borrowings	C		
	(b) Deferred tax liabilities (net)			
	(c) Other long-term liabilities	D		
	(d) Long-term provisions	E		

4	Current liabilities			
	(a) Short-term borrowings	F		
	(b) Trade payables			
	(c) Other current liabilities	G		
	(d) Short-term provisions	H		
	TOTAL			
B	**ASSETS**			
1	Non-current assets			
	(a) Fixed assets			
	(i) Tangible assets	I		
	(ii) Intangible assets	J		
	(iii) Capital work-in-progress			
	(iv) Intangible assets under development			
	(v) Fixed assets held for sale			
	(b) Non-current investments	K		
	(c) Deferred tax assets (net)			
	(d) Long-term loans and advances	L		
	(e) Other non-current assets	M		
2	Current assets			
	(a) Current investments	N		
	(b) Inventories	O		
	(c) Trade receivables	P		
	(d) Cash and cash equivalents	Q		
	(e) Short-term loans and advances	R		
	(f) Other current assets	S		
	TOTAL			
	See accompanying notes forming part of the financial statements			

15.6. GENERAL INSTRUCTIONS FORPREPARATION of BALANCE SHEET AS PER REVISED SCHEDULE VI

1. An asset shall be classified as current when it satisfies any of the following criteria:

(a) it is expected to be realized in, or is intended for sale or consumption in, the company's normal operating cycle;

(b) it is held primarily for the purpose of being traded;

(c) it is expected to be realized within twelve months after the reporting date; or

(d) it is cash or cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date.

All other assets shall be classified as non-current.

2. An operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents. Where the normal operating cycle cannot be identified, it is assumed to have duration of 12 months.

3. A liability shall be classified as current when it satisfies any of the following criteria:

(a) it is expected to be settled in the company's normal operating cycle;

(b) it is held primarily for the purpose of being traded;

(c) it is due to be settled within twelve months after the reporting date; or

(d) the company does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification. All other liabilities shall be classified as non-current.

4. A receivable shall be classified as a 'trade receivable' if it is in respect of the amount due on account of goods sold or services rendered in the normal course of business.

5. A payable shall be classified as a 'trade payable' if it is in respect of the amount due on account of goods purchased or services received in the normal course of business.

6. A company shall disclose the following in notes to accounts:

6A. Share capital: Clauses (a) to (l) of Notes 6 A deal with disclosures for Share Capital and such disclosures are required for each class of share capital (different classes of preference shares to be treated separately).

a. The number and amount of shares authorized

b. The number of shares issued, subscribed and fully paid, and subscribed but not fully paid

c. Par value per share

d. A reconciliation of the number of shares outstanding at the beginning and at the end of the reporting period

e. The rights, preferences and restrictions attaching to each class of shares including restrictions on the distribution of dividends and the repayment of capital

f. Shares in respect of each class in the company held by its holding capacity or its ultimate holding company including shares held by or by subsidiaries or associates of the holding company or the ultimate holding company in aggregate.

g Shares in the company held by each Shareholder holding more than 5 per cent shares specifying the number of shares held

h.Shares reserved for issue under options and contracts/commitments for the sale of shares/disinvestment, including the terms and amounts

j. For the period of five years immediately preceding the date as at which the balance sheet is prepared :

- aggregate number and class of shares allotted as fully paid up pursuant to contract(s) without payment being received in cash.
- aggregate number and class of shares allotted as fully paid up by way of bonus shares.
- aggregate number and class of shares bought back.

j. Terms of any securities convertible into equity/preference shares issued along with the earliest date of conversion in descending order starting from the farthest such date

k. Calls unpaid (showing aggregate value of calls unpaid by directors and officers)

6B. Reserves and Surplus

(i) Reserve and surplus shall classified as follows

a) Capital Reserves
b) Capital Redemption Reserve
c) Securities Premium Reserve
d) Debenture Redemption Reserve
e) Revaluation Reserve
f) Share Options Outstanding Account
g) Other Reserves (specify the nature and purpose of reserve and the amount in respect thereof)
h) Surplus i.e. balance in Statement of Profit & Loss disclosing allocations and appropriations, such as dividend, bonus shares and transfer to/from reserves, etc(Additions and deductions since the last Balance Sheet to be shown under each of the specified head)

- A reserve specifically represented by earmarked investments shall be termed as a 'fund'.
- Debit balance of statement of profit and loss shall be shown as a negative figure under the head 'Surplus'. Similarly, the balance of 'Reserves and Surplus', after adjusting negative balance of surplus, if any, shall be shown under the head 'Reserves and Surplus' even if the resulting figure is in the negative.

6C. Non-Current Liabilities

a. Long-term borrowings:
• Long-term borrowings shall be classified as:
(a) Bonds/debentures;
(b) Term loans;
• from banks;
• from other parties;
(c) Deferred payment liabilities;
(d) Deposits;
(e) Loans and advances from related parties;
(f) Long term maturities of finance lease obligations;
(g) Other loans and advances (specify nature).

- Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.
- Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall be disclosed. The word "others" used in the phrase "directors or others" would mean any person or entity other than a director.

- Bonds/debentures (along with the rate of interest and particulars of redemption or conversion, as the case may be) shall be stated in descending order of maturity or conversion, starting from farthest redemption or conversion date, as the case may be. Where bonds/debentures are redeemable by installments, the date of maturity for this purpose must be reckoned as the date on which the first installment becomes due.
- Particulars of any redeemed bonds/ debentures which the company has power to reissue shall be disclosed.
- Period and amount of continuing default as on the Balance Sheet date in repayment of loans and interest shall be specified separately in each case.

b. Other Long-term liabilities
This should be classified into:
a) Trade payables; and
b) Others

c. Long-Term Provisions
This should be classified into
a) provision for employee benefits and
b) others specifying the nature.

6D. Current Liabilities
a. Short-term borrowings;

(i) (a) Loans repayable on demand
- from banks;
- from other parties.

(b) Loans and advances from related parties;
(c) Deposits;
(d) Other loans and advances (specify nature).
- Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.
- Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall be disclosed.
- Period and amount of default as on the Balance Sheet date in repayment of loans and interest shall be specified separately in each case.

b. Other current liabilities

The amounts shall be classified as:
(a) Current maturities of long-term debt;
(b) Current maturities of finance lease obligations;

(c) Interest accrued but not due on borrowings;
(d) Interest accrued and due on borrowings;
(e) Income received in advance;
(f) Unpaid dividends;
(g) Application money received for allotment of securities and due for refund and interest accrued thereon;
(h) Unpaid matured deposits and interest accrued thereon;
(i) Unpaid matured debentures and interest accrued thereon;
(j) Other payables (specify nature).

The portion of long term debts / lease obligations, which is due for payments within twelve months of the reporting date is required to be classified under "Other Current liabilities" while the balance amount should be classified under Long-term Borrowings. Other Payables would include amounts in the nature of statutory dues such as Withholding taxes, Service Tax, VAT, Excise Duty etc.

c. Short-term provisions

The amounts shall be classified as:
(a) Provision for employee benefits;
(b) Others (specify nature).

6E. Non-Current Assets

a. Tangible assets

(i) Classification shall be given as:

a. Land.
b. Buildings.
c. Plant and Equipment.
d. Furniture and Fixtures.
e. Vehicles.
f. Office equipment.
g. Others (specify nature).

(ii) Assets under lease shall be separately specified under each class of asset.

(iii) A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations and other adjustments and the related depreciation and impairment losses/reversals shall be disclosed separately.

(iv) Where sums have been written off on a reduction of capital or revaluation of assets or where sums have been added on revaluation of assets, every balance sheet subsequent to date of such write-off, or addition shall show the reduced or increased figures as applicable and shall by way of a note also show the amount of the reduction or increase as applicable together with the date thereof for the first five years subsequent to the date of such reduction or increase.

b. Intangible Assets

(i) Classification shall be given as:

a. Goodwill.
b. Brands /trademarks.
c. Computer software.
d. Mastheads and publishing titles.
e. Mining rights.
f. Copyrights, and patents and other intellectual property rights, services and operating rights.
g. Recipes, formulae, models, designs and prototypes.
h. Licenses and franchise.
i. Others (specify nature).

(ii) A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations and other adjustments and the related amortization and impairment losses/reversals shall be disclosed separately.

(iii) Where sums have been written off on a reduction of capital or revaluation of assets or where sums have been added on revaluation of assets, every balance sheet subsequent to date of such write-off, or addition shall show the reduced or increased figures as applicable and shall by way of a note also show the amount of the reduction or increase as applicable together with the date thereof for the first five years subsequent to the date of such reduction or increase.

c. Non-current investments

(i) Non-current investments shall be classified as trade investments and other investments and further classified as:

a. Investment property;
b. Investments in Equity Instruments;
c. Investments in preference shares
d. Investments in Government or trust securities;
e. Investments in debentures or bonds;
f. Investments in Mutual Funds;
g. Investments in partnership firms
h. Other non-current investments (specify nature)

Under each classification, details shall be given of names of the bodies corporate (indicating separately whether such bodies are

- subsidiaries,
- associates,
- joint ventures, or

- controlled special purpose entities) in whom investments have been made and the nature and extent of the investment so made in each such body corporate (showing separately investments which are partly paid).In regard to investments in the capital of partnership firms, the names of the firms (with the names of all their partners, total capital and the shares of each partner) shall be given.

(ii) Investments carried at other than at cost should be separately stated specifying the basis for valuation thereof.

(iii) The following shall also be disclosed:

a. Aggregate amount of quoted investments and market value thereof;
b. Aggregate amount of unquoted investments;
c. Aggregate provision for diminution in value of investments
d. Long-term loans and advances

(i) Long-term loans and advances shall be classified as:

a. Capital Advances;
b. Security Deposits;
c. Loans and advances to related parties (giving details thereof);
d. Other loans and advances (specify nature).

(ii) The above shall also be separately sub-classified as:

a. Secured, considered good;
b. Unsecured, considered good;
c. Doubtful.

(iii) Allowance for bad and doubtful loans and advances shall be disclosed under the relevant heads separately.

(iv) Loans and advances due by directors or other officers of the company or any of them either severally or jointly with any other persons or amounts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

e. Other non-current assets

Other non-current assets shall be classified as:

(i) Long Term Trade Receivables (including trade receivables on deferred credit terms);

(ii) Others (specify nature)

(iii) Long term Trade Receivables, shall be sub-classified as:

a. Secured, considered good;
b. Unsecured considered good;
c. Doubtful

(ii) Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.

(iii) Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

6F. Current Investment

a. Current Investments

(i) Current investments shall be classified as:

a. Investments in Equity Instruments;
b. Investment in Preference Shares
c. Investments in government or trust securities;
d. Investments in debentures or bonds;
e. Investments in Mutual Funds;
f. Investments in partnership firms
g. Other investments (specify nature).

Under each classification, details shall be given of names of the bodies corporate (indicating separately whether such bodies are (i) subsidiaries, (ii) associates, (iii) joint ventures, or (iv)controlled special purpose entities) in whom investments have been made and the nature and extent of the investment so made in each such body corporate (showing separately investments which are partly paid).

In regard to investments in the capital of partnership firms, the names of the firms (with the names of all their partners, total capital and the shares of each partner) shall be given.

(ii) The following shall also be disclosed:

a. The basis of valuation of individual investments
b. Aggregate amount of quoted investments and market value thereof;
c. Aggregate amount of unquoted investments;
d. Aggregate provision made for diminution in value of investments.

b. Inventories

(i) Inventories shall be classified as:

a. Raw materials;
b. Work-in-progress;
c. Finished goods;
d. Stock-in-trade (in respect of goods acquired for trading);
e. Stores and spares;
f. Loose tools;
g. Others (specify nature).

(ii) **Goods-in-transit** shall be disclosed under the relevant sub-head of inventories. Mode of valuation shall be stated.

c. Trade Receivables

(i) Aggregate amount of Trade Receivables outstanding for a period exceeding six months from the date they are due for payment should be separately stated.

(ii) Trade receivables shall be sub-classified as:

a. Secured, considered good;
b. Unsecured considered good;
c. Doubtful.

(iii) Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.

(iv) Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

d. Cash and cash equivalents

(i) Cash and cash equivalents shall be classified as:

a. Balances with banks;
b. Cheques, drafts on hand;
c. Cash on hand;
d. Others (specify nature).

(ii) Earmarked balances with banks (for example, for unpaid dividend) shall be separately stated.

(iii) Balances with banks to the extent held as margin money or security against the borrowings, guarantees, other commitments shall be disclosed separately.

(iv) Repatriation restrictions, if any, in respect of cash and bank balances shall be separately stated.

(v) Bank deposits with more than 12 months maturity shall be disclosed separately.

e. Short-term loans and advances

(i) Short-term loans and advances shall be classified as:

(a) Loans and advances to related parties (giving details thereof);

(b) Others (specify nature).

(ii) The above shall also be sub-classified as:

a. Secured, considered good;
b. Unsecured, considered good;
c. Doubtful.

(iii) Allowance for bad and doubtful loans and advances shall be disclosed under the relevant heads separately.

(iv) Loans and advances due by directors or other officers of the company or any of them either severally or jointly with any other person or amounts due by firms or private companies respectively n which any director is a partner or a director or a member shall be separately stated.

f. Other current assets (specify nature). This is an all-inclusive heading, which incorporates current assets that do not fit into any other asset categories.

6G. Contingent liabilities and commitments (to the extent not provided for)

(i) Contingent liabilities shall be classified as:

a. Claims against the company not acknowledged as debt;
b. Guarantees;
c. Other money for which the company is contingently liable

(ii) Commitments shall be classified as:

a. Estimated amount of contracts remaining to be executed on capital account and not provided for;
b. Uncalled liability on shares and other investments partly paid
c. Other commitments (specify nature).

6H. The amount of dividends proposed to be distributed to equity and preference shareholders for the period and the related amount per share shall be disclosed separately. Arrears of fixed cumulative dividends on preference shares shall also be disclosed separately.

6I. where in respect of an issue of securities made for a specific purpose, the whole or part of the amount has not been used for the specific purpose at the balance sheet date, there shall be indicated by way of note how such unutilized amounts have been used or invested.

6J. If, in the opinion of the Board, any of the assets other than fixed assets and non-current investments do not have a value on realization in the ordinary course of business at least equal to the amount at which they are stated, the fact that the Board is of that opinion, shall be stated

15.6 A PART II – FORM OF STATEMENT OF PROFIT AND LOSS

Name of the Company …………
Profit and loss statement for the year ended ……………….

Particulars	Note no.	Figures for the current period	Figures for the previous period
i. Revenue from Operations	T		
ii. Other incomes	U		
iii. Total Revenue (i+ii)			
iv. Expenses Cost of Material consumed Purchases of Stock in Trade Changes in inventories of finished goods Work in Progress and Stock in Trade Employee Benefits expenses Finance expenses Depreciation and amortization expenses Other expenses Total Expenses	 V W X Y Z		
v. Profit Before Exceptional and Extraordinary items ant Tax (iii – iv)			
vi. Exceptional items			
Profit before extraordinary items and tax (v – vi)			
vii. Extraordinary items			
viii. Profit before tax (vii – viii)			
ix. Tax Expenses (1) Current Tax (2) Deferred Tax			
x. Profit/Loss for the period from continuing operations (ix – x)			

xi. Profit/Loss from discontinuing operations			
xii. Tax expenses of discontinuing operations			
xiii. Profit/Loss from Discontinuing operations (after tax)			
xiv. Profit/Loss for the period			
xv. Earning per equity share: (1) Basic (2) Diluted			

15.6. B. General Instructions for Preparation of Statement of Profit and Loss

1. The provisions of this Part shall apply to the income and expenditure account referred to in subsection (2) of Section 210 of the Act, in like manner as they apply to a statement of profit and loss.

2. (A) In respect of a company other than finance company revenue from operations shall disclose separately in the notes revenue from

(a) sale of products;
(b) sale of services;
(c) other operating revenues;
Less:
(d) Excise duty.

(B) In respect of a finance company, revenue from operations shall include revenue from
(a) Interest; and
(b) Other financial services

Revenue under each of the above heads shall be disclosed separately by way of notes to accounts to the extent applicable.

3. Finance Costs: Finance costs shall be classified as:

a. Interest expense;
b. Other borrowing costs;
c. Applicable net gain/loss on foreign currency transactions and translation.

4. Other income: Other income shall be classified as:
a. Interest Income (in case of a company other than a finance company);

b. Dividend Income;
c. Net gain/loss on sale of investments
d. Other non-operating income (net of expenses directly attributable to such income).

5. Additional Information: A Company shall disclose by way of notes additional information regarding aggregate expenditure and income on the following items:-

(i) (a) Employee Benefits Expense [showing separately

a. salaries and wages,
b. contribution to provident and other funds,
c. expense on Employee Stock Option Scheme (ESOP) and Employee Stock Purchase Plan (ESPP),
d. staff welfare expenses].

(b) Depreciation and amortization expense;

(c) Any item of income or expenditure which exceeds one per cent of the revenue from operations or Rs.1,00,000, whichever is higher;

(d) Interest Income;

(e) Interest Expense;

(f) Dividend Income;

(g) Net gain/ loss on sale of investments;

(h) Adjustments to the carrying amount of investments;

(i) Net gain or loss on foreign currency transaction and translation (other than considered as finance cost);

(j) Payments to the auditor as

a. auditor,
b. for taxation matters,
c. for company law matters,
d. for management services,
e. for other services,
f. for reimbursement of expenses;
g. Details of items of exceptional and extraordinary nature
h. Prior period items;

(ii) (a) In the case of manufacturing companies,-

a. Raw materials under broad heads.
b. Goods purchased under broad heads.

(b) In the case of trading companies, purchases in respect of goods traded in by the company under broad heads.

(c) In the case of companies rendering or supplying services, gross income derived form services rendered or supplied under broad heads.

(d) In the case of a company, which falls under more than one of the categories mentioned in (a), (b) and (c) above, it shall be sufficient compliance with the requirements herein if purchases, sales and consumption of raw material and the gross income from services rendered is shown under broad heads.

(e) In the case of other companies, gross income derived under broad heads.

(iii) In the case of all concerns having works in progress, works-in progress under broad heads.

(iv) (a) The aggregate, if material, of any amounts set aside or proposed to be set aside, to reserve, but not including provisions made to meet any specific liability, contingency or commitment known to exist at the date as to which the balance-sheet is made up.

(b) The aggregate, if material, of any amounts withdrawn from such reserves.

(v) (a) The aggregate, if material, of the amounts set aside to provisions made for meeting specific liabilities, contingencies or commitments.

(b) The aggregate, if material, of the amounts withdrawn from such provisions, as no longer required.

(vi) Expenditure incurred on each of the following items, separately for each item:-

a. Consumption of stores and spare parts.
b. Power and fuel.
c. Rent.
d. Repairs to buildings.
e. Repairs to machinery.
f. Insurance.
g. Rates and taxes, excluding, taxes on income.
h. Miscellaneous expenses

(vii) (a) Dividends from subsidiary companies.

(b) Provisions for losses of subsidiary companies.

(viii) The profit and loss account shall also contain by way of a note the following information, namely:-
a) Value of imports calculated on C.I.F basis by the company during the financial year in
Respect of –

a. Raw materials;
b. Components and spare parts;
c. Capital goods;

b) Expenditure in foreign currency during the financial year on account of royalty, know-how, Professional and consultation fees, interest, and other matters;

c) Total value if all imported raw materials, spare parts and components consumed during the financial year and the total value of all indigenous raw materials, spare parts and components similarly consumed and the percentage of each to the total consumption;

d) The amount remitted during the year in foreign currencies on account of dividends with a specific mention of the total number of non-resident shareholders, the total number of shares held by them on which the dividends were due and the year to which the dividends related;
e) Earnings in foreign exchange classified under the following heads, namely:-

a. Export of goods calculated on F.O.B. basis;
b. Royalty, know-how, professional and consultation fees;
c. Interest and dividend;
d. Other income, indicating the nature thereof

15.7 IMPLICATIONS OF REVISED FORMAT

The changes brought in revised format have been segregated in the following manner: -

1. Balance Sheet
2. Profit & Loss A/c

15.7.1General Changes

1. While both Vertical and horizontal forms of presentation were allowed under old schedule VI, only vertical form is allowed under revised Schedule VI.

2. Once a unit measurement is used, it should be used uniformly in the Financial Statements.

15.7.2 Changes in Balance Sheet

Liabilities

1. Change in nomenclature – “Sources of Funds” has been replaced with “Equity & Liabilities”

2. Share Capital – Company would need to show in sub-head à Shares held more than 5% in company along with number of shares

3. Debit Balance of P&L A/c shall now be shown as negative figure under head Surplus

4. Liabilities will now broadly be classified as

- Current Liabilities &
- Non Current Liabilities

5. Deferred payment liabilities and loans & advances from related parties to be shown separately under head “Long term Borrowings”.

6. Provisions to be classified as Short Term Provisions & Long Term Provisions

Assets

1. Change in nomenclature – “Application of Funds” has been replaced with “Assets”

2. Fixed Assets to be further classified as

- Tangible
- Non-Tangible

3. Current Assets are to be shown under separate head.

4. “Sundry Debtors” have now been named “Trade Receivables”

5. “Cash and Bank Balances” have now been termed as “Cash and Cash Equivalents”. Classification under this head has been completely revamped.

6. Inventories – Goods in transit shall be disclosed under the relevant sub-head of inventories

7. Misc expenditure (to the extent not written off or adjusted) shall now not be shown separately under head “Other Current Assets”

8. The amount of dividend proposed to be distributed to shareholders (equity and preference) for the period and amount per share to be disclosed separately

15.7.3 Changes in Profit & Loss A/c

1. Under head *“Other Income”* - Net gain/loss on foreign currency translation and transaction (other than finance cost) shall be disclosed separately.

2. Employee benefit expense shall disclose additionally expense on account of Employee stock option scheme (ESOP)

3. Following shall now be disclosed separately –

- Provision for loss of Subsidiary companies
- Net loss on sale of Investments
- Details of exceptional and extraordinary items
- Prior Period items
- Adjustment to carrying amount of investments

4. A new format has been issued for face reporting of Profit & Loss A/c.

15.7.4 Impact of Revision in Schedule VI

1. The revised schedule VI intends to familiarize companies with Ind-AS/IFRS by using certain concepts such as current/non-current classification.

2. The revised Schedule VI has e*liminated the concept of schedule*s and such information will now be provided in the notes to accounts. This is as done when applying IFRS.

3. From now on, the compliance requirements of Act and/or Accounting standards will prevail over schedule VI.

4. Better presentation, disclosures intended to facilitate better organised data for users of financial statement.

15.8 ADJUSTMENT SPECIFICALLY APPLICABLE TO COMPANIES:

As stated earlier the final accounts of Companies, should be in compliance with the statutory provision of the Companies Act.

Such adjustments are: -

1. Provision for income tax (incl. minimum alternate tax)
2. Accounting for assessment of income tax.
3. Transfer to reserve, out of current year profit
4. Proposal of dividend-
5. Dividend distribution tax.
6. Issue of shares without consideration i.e. Capitalization of Reserve and issue of bonus shares.
7. Issue of shares, for non cash consideration

1. **Advance Tax / Tax deducted at source as income**

a) **Tax deducted at source:** Payer of certain amount is required to deduct amount as income tax from payment to be made. The amount so deducted is to be treated as tax paid. The receiver receives net amount. The entry should be passed in the books of receiver as:

Bank A/c Dr.
Tax Deducted at source (TDS) to income.Dr.
To Interest Earned A/c.

b Advance tax is the tax paid on the current year during the current year itself. It is required to estimate the tax payable on current income and pay the amount is through installments before end of financial year. The entry to be passed is.

Tax Paid A/c Dr.
To bank A/c

2. Provision for income tax (incl. minimum alternative Tax).

Income tax payable as percentage on profit currently for year ending 31-3-2003, income tax is payable @ 35 on taxable income.

The provision is made at lower percentage and Assessed tax is more than provision or other information may be given. The entry would be: -

Profit & loss A/c Dr.
To provision for income tax

NOTE: As per accounting standard 22, deducting with income tax, advance tax, TDS and provision for income tax should be shown as net balance. If net amount is debit, then show under heading loan & advance. And if it is credit show it as current liabilities.

This is to be disclosed on the face of the Statement to Profit and Loss and bifurcated into:
(1) Current tax and
(2) Deferred tax

Current tax: The term 'Current tax' has been defined under AS-22 "Accounting for Taxes" on Income as the amount of income tax determined to be payable (recoverable) in respect of the taxable income (tax loss) for a period. Hence, details of all taxes on income payable under the applicable taxation laws should be disclosed here.

Presentation for Minimum Alternate Tax (MAT) credit should be made as prescribed by the ICAI Guidance Note on "Accounting for Credit Available in Respect of Minimum Alternative tax under the Income-tax Act, 1961'. The relevant portion is as under:

Profit and Loss Account:

According to paragraph 6 of Accounting Standards Interpretation (ASI) 6, 'Accounting for Taxes on Income in the context of Section 115JB of the Income-tax Act, 1961', issued by the Institute of Chartered Accountants of India, MAT is the current tax. Accordingly, the tax expense arising on account of payment of MAT should be charged at the gross amount, in the normal way, to the profit and loss account in the year of payment of MAT. In the year in which the MAT credit becomes eligible to be recognized as an asset in accordance with the recommendations contained in this Guidance Note, the said asset should be created by way of a credit to the profit and loss account and presented as a separate line item therein."

The Disclosure in this regard should be made as under:

Current tax (MAT)	XX
Less : MAT credit entitlement	(XX)
Net Current tax	XX

Any interest on shortfall in payment of advance income-tax is in the nature of finance cost and hence should not be clubbed with the Current tax.The same should be classified as Interest expense under finance costs. However, such amount should be separately disclosed.

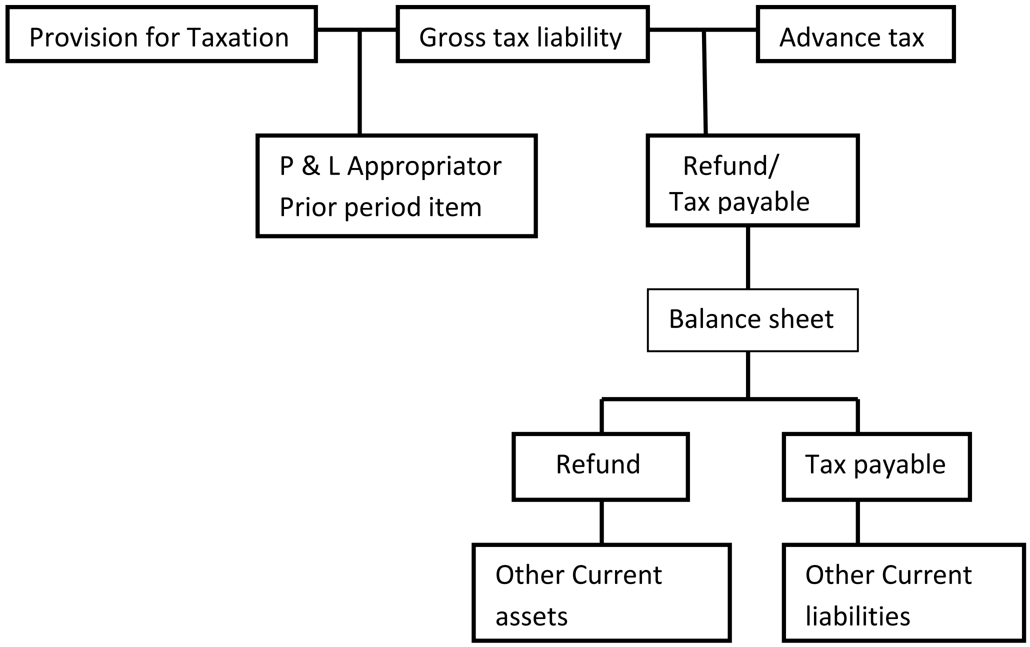
Any penalties levied under Income tax laws should not be classified as Current tax. Penalties which are compensatory in nature should be treated as interest and disclosed in the manner explained above. Other tax penalties should be classified under other expenses.

Wealth tax payable by a company on assets liable for wealth tax should not be included within current tax since the same is not a tax on income. Accordingly, wealth tax should be included in Rates and taxes under other expenses.

Excess/Short provision of tax relating to earlier years should be separately disclosed.

3. Completion of assessment.

The liability for income tax is determined by income tax officer after completion of assessment. On receipt of assessment order gross amount liability should be composed with (i) Advance tax & TDS difference would be refund or tax payable. This should be shown as current asset or current liability. And (II) provision for income tax- the difference should be shown as profit & loss appropriation account as prior period items.



4. Assessment under dispute.

After receipt of assessment order, the company has right to file an appeal and challenge the order. If the assessment is disputed the balance sheet should disclose advance tax and provision for that year till the disposal of the matter. The information of amount of tax subject to appeal should be shown as contingent liability.

Illustration 1:

Show necessary journal entries and disclosure of relevant items in final account.

Trial Balance
As at 31st March, 2015

	Dr (Rs.)	Cr (Rs.)
Advance income tax A.Y. 2014-2015	2, 00,000	
Advance income tax A.Y.2015-2016	1, 30,000	
Provision for income tax 2014-2015		1, 80,000

Adjustments: -

a) The income tax assessment for 2014-15 has been completed during the year and tax liability has been fixed at Rs. 2, 20,000. No effect has been given to this in the accounts.

b) Provision for income tax to be made for the A.Y. 2015-16 is for Rs. 1, 20,000

Solution:

Journal

	Dr (Rs.)	Cr (Rs.)
Profit & Loss A/c Dr.	1, 20,000	
To provision for income tax A/c		1, 20,000
(being provided for taxation for the year 2013-14)		
P & L A/c Dr.	40,000	
To Provision for tax A/c		40,000
(being entry to record completion of tax assessment and resulting deemed / provision)		

Provision for Income Tax A/c
A.Y.2014-2015

To advance income tax	2, 00,000	By balance b/d	1, 80,000
To Liability for taxation	20,000 (Bat. Fig)	By profit & Loss	40,000
	2, 20,000		2, 20,000

Provision for Income Tax A/c
A.Y.2013-2014

To balance c/d	1,30,000	By profit & Loss	1, 30,000
	1, 30,000		1, 30,000

Advance Payment of Income Tax A/c

To balance c/d	1,20,000	By Provision for Income Tax(2012-2013)	2, 00,000
To balance c/d	80,000		
	2,00,000		2,00,000

Liability for taxation A/c

To balance c/d	40,000	By Provision for Income Tax(2012-2013)	40,000
	40,000		40,000

Statement of Profit & Loss A/c for the year ended 31st March, 2015(extract)

Particulars	Rs.	Rs.
Profit before Tax		xxxxxx
Less Tax Expense-Current year	1,30,000	
Short Provision for Previous year	40,000	2,70,000
		xxxxxxx

Balance sheet as on 31st March, 2015(extract)

Particulars	Rs.	Rs.
1. EQUITY AND LIABILITIES		xxxxxx
A. Other Current Liabilities		
Liability for taxation(2012-2013)		40,000
B. Short term Provisions		
Provision for Income tax(2013-2014)	1,20,000	
Less Advance Tax	1,30,000	(10,000)

5. Corporate dividend tax

The Finance Act, 2003 introduced the tax on dividends, tax is levied on the dividend paid by the company or what is termed as Corporate Dividend tax.(CDT).

- Corporate dividend tax is in addition to the corporate tax paid by the company on its profits.
- Such taxes are levied on any amount declared, distributed or paid by the domestic company (in India by way of dividends in cash).
- The dividend may be declared out of current or accumulated profits.
- Corporate dividend tax is payable even if no corporate tax is payable by a company or its income.
- The principal officer of the domestic company and the company shall be liable to pay the tax on distributed profits to the credit of the central government within 14 days from the date of declaration, distribution or payment of any dividend whichever is the earliest.
- The rate of CDT is 15% of the dividend (plus surcharge at 1.5% on tax and cess on 3%)
- Provision for CDT should be debited to profit and loss account of the same year in which CDT liability is recognized
- Provision for CDT' should be disclosed separately under 'Short Term Provisions'.

- Provision for CDT should be shown separately in the P&L A/c as follows :
  Dividend xxxx
  Corporate Dividend Tax xxxx

6. Provision for the dividend

Dividends refer to the amount of the profit distributed among the shareholder. Preference shareholders are entitled to get dividend at the fixed rate. Preference dividend is paid before payment of the equity dividend.

If proposed dividend on equity capital is specified, the dividend on preference share capital at a given rate should be added to the amount proposed dividend.

Interim dividend: -

It is declared between two annual general meetings. It does not require approval of the shareholder. The amount of interim dividend is shown as debit profit & loss appropriation A/c Final dividend:

It is the dividend proposed by the directors and declared by the shareholders in the annual general meeting. Companies are required to pay dividend within 42 days from the date of declaration. After expiry of the period, the unpaid dividend is transferred to unpaid dividend bank A/c which is to be transferred to "Investors education & protection fund A/c".

Illustration 2: -

	Rs.
13.5% preference share capital	4, 00,000
Fully paid equity share capital	5, 00,000
The board of Directors declared a dividend of 15%	
Dividend distribution Tax @ 10.2%	

Solution: -

Preference dividend	
13.5% of 4, 00,000	54,000
Equity dividend	75,000
	1, 29,000
Dividend distribution tax 10.2%	13,158

Journal entry

Particulars	Dr.(Rs.)	Cr.(Rs.)
Profit and loss Appropriation A/c Dr.		1, 42,158
To proposed preference dividend A/c	75,000	
To proposed equity dividend A/c		75,000
To dividend distribution tax		13,158

7. Transfer to reserves

As per the rules framed under the companies Act, companies are required to transfer certain percentages of their profit after tax to reserves to declare dividend out of current year's profit which is arrived at after making necessary provision for depreciation as required by the section 123I of the Companies Act, 2013. The various rates of transfer based on the rate of dividend are as follows:

Rate of dividend	Transfer to reserves
Exceeds 10% but not 12½% of the paid capital.	2½% of the current profit
Exceeds 12.5% but not 15% of the paid up capital.	5% of the current profit
Exceeds 15% but not 20% of the paid up capital.	7½% of the current profit
Exceeds 20%	10% of the current profit

8. Managerial remuneration.

The remuneration to managerial personnel is payable as per term by the company and approved by the company law/registrar of companies.

This consists of (1) Salary, (2) Perquisites and (3) Commission as a percentage on profit or turnover.

Where the remuneration is stated as percentage on profit or turnover the care should be taken too uncertain whether percentage is before or after applying the limit. The amount so calculated, should be provided for to the extent not included in trial balance. Corresponding the same should be shown as current liability as Short -Term Provisions. The Revised Schedule VI has removed disclosures relating to managerial remuneration and computation of net profits as it is not considered relevant in the present day.

9. Discount or Loss on Issue of Debentures shall be written off either

(i) from Securities Premium Reserve (permitted u/s 78 of the Companies Act, 1956); or

(ii) from the Statement of Profit and Loss over the period of the loan i.e. Debenture.

Revised Schedule VI requires that all assets shown in the Balance Sheet should be classified into Non – current Assets and Current Assets. Accordingly, Discount on Issue of Shares or Share Issue Expenses not yet written off are to be classified as Non – current Assets and Current Assets.

Discount or Loss on Issue of Debentures that shall be written off after 12 months of the date of Balance Sheet shall be shown as ***Other Non – current Assets under Non – current Assets*** and the amount to be written off within 12 months from the date of Balance Sheet shall be shown as ***Other Current Asset under Current Assets***

10. Operating Cycle: Operating Cycle means the time between the acquisition of assets for processing and their realization in cash or cash or cash equivalent. Current Assets required to be classified into the following categories on the face of the balance sheet:

a. Current investments
b. Inventories
c. Trade receivables
d. Cash and cash equivalents.
e. Short-term loans and advances
f. Other current assets

Current Assets: All assets are divided into Non-Current Assets and Current Assets. According to the Revised Schedule VI an asset shall be classified as current if it satisfies any one of the following criteria;

a. it is expected to be realised in, or is intended for sale or consumption in, the company's normal operating cycle.
b. It is held primarily for the purpose of being traded
c. It is expected to be realised within 12 months after the reporting date or
d. It is cash or cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least 12 months after the reporting date.

Non – Current Assets: All other assets shall be classified as non-current assets

Illustration 3:

X Ltd. declared 15% dividend on equity share capital. The net profit of the company after tax is Rs. 4, 00,000. How much amount will be transferred to reserve? Pass journal entry for transfer to reserve.

Solution:

As the rate of dividend is 15%, the board should transfer 5% of the net profit to reserve i.e. 5% of Rs. 4, 00,000 = Rs. 20,000.

Journal Entry

Particulars	Dr.(Rs.)	Cr.(Rs.)
Profit and loss A/c Dr.	20,000	
To General reserve		20,000
(being transfer to general reserve)		

Illustration 4:

Share capital 2, 00,000 equity share of Rs. 10 each	20, 00,000
Securities premium	4, 00,000
General reserve	10, 00,000
Profit and loss A/c	8, 00,000

The company decided to issue bonus share at the rate of 3 shares for every four share held and decided to utilize securities premium. General reserve and profit and loss A/c show the effect on financial statements.

Solution:

No. of bonus share = $\frac{2,00,000}{4} \times 3 = 1,50,000$

Share of Rs. 10 each i.e. Rs. 15, 00,000

Journal

Particulars	Dr.(Rs.)	Cr.(Rs.)
Securities premium A/c Dr.	4, 00,000	
General reserve A/c Dr.	10, 00,000	
Profit and loss A/c Dr.	1, 00,000	
To bonus to equity shareholder A/c		15, 00,000
(being capitalization of profit for issue of bonus share)		
Bonus to equity shareholder A/c	15, 00,000	
To equity share capital A/c		15, 00,000
(being issue of bonus shares to existing equity shareholder)		

Balance sheet (extract) as on --------------

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholder's Funds			
a. Share Capital	1	35,00,000	
b. Reserves and Surplus	2	7,00,000	
Total			42,00,000

Notes to Accounts:

Particulars	Dr.(Rs.)	Cr.(Rs.)
1.Share Capital		
Equity share capital		
Issued and subscribed		
3, 50,000 equity shares of Rs. 10 each		
(Of the above shares 1, 50,000 shares are		
Issued as bonus shares out of securities premium)		35,00,000
2. **Reserves and Surpluses**		
Profit & loss A/c		7, 00,000

Illustration 5:

A company has opening debit balance in Statement of Profit and Loss of Rs. 1, 00,000. During the year, it earned a profit of Rs. 5, 00,000. It decided to transfer Rs. 1, 50,000 to Debenture Redemption Reserve (DRR) and also proposed to pay dividend of Rs. 25,000? How will you show them in financial statement?

Reserves and Surplus

Statement of Profit and Loss	**Rs.**	**Rs.**
Statement of Profit and Loss		(1,00,000)
Add: Profit (Loss) for the Period		5,00,000
Balance		**4,00,000**
Less: Appropriations (Debentures Redemption Reserve) **Debentures Redemption Reserve**	1,50,000	
Proposed Dividend	25,000	1,75,000
Balance – Statement of Profit and Loss		**2,25,000**

Debentures Redemption Reserve (DRR)	
Opening Balance	Nil
Transfer from Statement of Profit and Loss	1,50,000
	1,50,000
Balance – Reserves and Surplus	3,75,000

Current Liabilities

Current Liabilities	Rs.
Short – Term Provisions	25,000

Illustration 6:

Ricoh Ltd. is registered with the capital: 1,00,000, Equity Shares of Rs.10 each; and 60,000, 9% Preference Shares of Rs.10 each. It issued 90,000 Equity Shares and 50,000, 9% Preference Shares for subscription.

85,000 Equity Shares were subscribed on which the company had called Rs. 8. It did not receive first call of Rs. 2 on 3,000 shares, out of which 2,000 allotted to Atul were forfeited. Out of the forfeited shares 1,500 shares were reissued at Rs. 6,Rs. 8 paid up.9% Preference Shares were fully paid up. How will it be shown in balance sheet as per Revised Schedule VI

Solution:

Balance sheet (extract) as on --------------

Particulars		Note No.	Rs.
1. Equity and Liabilities Shareholders Fund		1.	11,77,000
Notes to Accounts Note 1:			
Share Capital		Rs.	Rs.
Authorised Share Capital		10,00,000	
Preference Share Capital	1 0	6,00,000	16,00,000
Issued Capital		9,00,000	
50,000, 9% Preference Shares of ~	1	5,00,000	14,00,000
Subscribed Capital **Subscribed and Fully Paid up**	1 0		5,00,000

Subscribed and not Fully Paid up		6,76,000	
Less: Calls in Arrears (1,000 Share × ~ 2)		2,000	
		6,74,000	
Add: Forfeited Share Account		3,000	6,77,000
			11,77,000

15.9 ACCOUNTING STANDARD-I:

Disclosure of Accounting Policies

This AS deals with different accounting policies to be adopted by the concern in the preparation and presentation of financial statements and its disclosure in such statement. In view of diverse according policies; disclosure of policies adopted is necessary for proper appreciation of statements. The purpose of AS is to promote better understanding of statements by establishing the disclosure of significant accounting policies.

For this AS:

I] **Fundamental accounting assumptions**: are the assumptions used for the preparation and presentation of statements If these are followed, no disclosure is required. These assumptions are.

a. Going concern: An enterprise will continue in operation for foreseeable future. The liquidation or material curtailment of operation is neither necessary nor intended.

b. Consistency in policies from one period to another period - particularly where the different alternatives are generally accepted in given situation.

c. Accrual of revenue and costs is the basis of recognition thereof.

II] **Considerations in selection of accounting policies**.

Prime consideration is to enable representation of true and fair view of statement of affairs and profit or loss. Major considerations for them are:

a. Prudence - i.e. conservatism concept
b. Substance over legal term of transaction & events.

c. Materiality - Material item are those items the knowledge of which might influence the decisions of user of statements.
d. Statutory or legal requirements, as applicable to the entity.

III] The AS gives illustrative list of areas where different policies might be adopted by different enterprises. Some areas are:

i) Depreciation & amortization - re: method, period, rate
ii) Expenditure during construction.
iii) Translation of foreign currency item.
iv) Valuation of inventories.
v) Valuation of investments / Goodwill / Fixed assets.
vi) Profits on long-term contracts.
vii) Contingent liabilities.
viii) Retirement benefits.
ix) Method of accounting - accrual / cash

The ASB had issued separate AS for these items.

Disclosure:

- All significant accounting policies adopted should be disclosed so as to form part of financial statements.
- Any change in policy, which has a material effect, should be disclosed together with monetary effect of such change (AS 5)
- If fundamental assumptions are not followed or applicable, the fact should be disclosed.

❖❖❖❖

6

FINAL ACCOUNTS OF LIMITED COMPANY-II

Unit Structure

16.1 Solved Problems
Exercise

16.1 SOLVED PROBLEMS:

Problems (Balance Sheet)
Illustration no.1
Following is the trial balance of Rahul Ltd. as on 31st March, 2015

Debit Balance	Rs.	Credit Balances	Rs.
Fixed Assets (at cost)	9,50,000	Equity share capital	
Investments	2,50,000	(Rs. 10/- each fully paid)	5,00,000
Closing Stock	4,05,000	11% Preference Share Capital	
Sundry Debtors	1,32,500	(Rs. 100/- each fully paid)	3,00,000
Preliminary Expenses	20,000	Profit for the year	1,65,000
Staff Advance	1,20,000	Securities Premium	30,000
Advance Tax	60,000	Dividend Equalisation Reserve	20,000
Interim Dividend paid	60,000	Debenture Redemption R	1,00,000
Bills Receivables	45,000	General Reserves	75,000
Advance to Suppliers	27,500	9% Debentures	5,30,000
Cash in Hand	12,500	Loan from Director Mr. Mani	10,000
Bank Balance	2,30,000	Loan from Bank	70,000
		Sundry Creditors	58,500
		Bills Payable	21,500
		Provision for Taxation	1,62,500
		Surplus brought forward from last year	1,50,000
		Provision for Depreciation	1,20,000

	23,12,500		**23,12,500**

Additional Information

(a) Transfer to dividend equalization reserve Rs. 10,000/- and General, Reserves Rs. 75,000/-.and debenture redemption reserve Rs. 25,000/-

(b) The Company declared dividend on Equity share capital at 12% after declaring preference dividend. The dividend declared was excluding Interim dividend

(c) Entire authorised share capital has been issued and subscribed.

(d) 9% Debentures and Loan from bank are secured against all fixed assets. The figure in trial balance for 9% Debentures includes interest accrued and due Rs. 30,000/-.

(e) Loan from Director is unsecured.

(f) Stock comprises of Raw-materials Rs. 1,30,000/-, work in progress Rs. 1,00,000/- and Finished goods Rs. 1,75,000/-.

(h) Of the debtors, debts due for more than 6 months is Rs. 32,500/-. All debts are unsecured and considered to be good.

(j) Ignore Previous Year's figures. After considering the above adjustments, prepare Balance Sheet of the company as at that date in the vertical form as per schedule VI requirements

Solution:

Rahul Ltd.
Balance Sheet as at 31st March 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
2. Shareholder's Funds			
c. Share Capital	1	8,00,000	
d. Reserves and Surplus	2	3,87,000	11,87,000
3. Non-Current Liabilities	3		5,70,000
Long Term	4	10,000	
Borrowings	5	80,000	
4. Current Liabilities	6	30,000	
a. Short term			
Borrowings	7	1,95,500	
b. Trade Payables			
c. Other Current Liabilities			3,15,500
			20,72,500

d. Short term Provisions			
Total			
ASSETS			
1. Non Current Assets	8	8,30,000	11,00,000
a. Fixed Assets		2,50,000	
- Tangible Assets		20,000	
b. Non Current Investments			
c. Other non current assets			
2. Current Assets	9	4,05,000	
a. Inventories	10	1,32,500	
b. Trade receivables	11	2,42,500	
c. Cash and cash equivalents	12	1,92,500	9,72,500
			20,72,500
d. Short term loans and advances.			
Total			

Notes to Accounts

Note	Particulars	Amount	Amount	Amount
1.	**Share Capital**			
	Equity share capital			
	Authorised, Issued, Subscribed and fully paid shares (Rs.10)			5,00,000
	Preference Share Capital			
	11% Pref. Shares			
	Authorised, Issued, Subscribed and fully paid shares (Rs.100)			3,00,000
	Total			8,00,000
2.	**Reserves and Surpluses**			
	a. Securities Premium			30,000
	b. Debenture Redemption Reserve			
	Opening Balance		1,00,000	
	Additions during year		25,000	1,25,000
	c. General Reserves			
	Balance b/d		75,000	
	Transferred from Profit & Loss a/c		75,000	1,50,000
	d. Dividend equalization Reserve			
	Balance b/d		20,000	
	Transferred from Profit & Loss a/c		10,000	
	e. Surplus / (Deficit)			30,000

	Balance in Statement of	1,50,000		
	P & L	1,65,000		
	Surplus for the year		3,15,000	
	Available for			
	Appropriations	60,000		
	Less: Allocations	33,000		
	Dividend-Interim	60,000		
	Dividend – Preference	25,000		
	Dividend- Equity	10,000		
	Transfer to Debenture	75,000	2,63,000	
	Redemption Res.			
				52,000
3.	Transfer to Dividend			3,87,000
	equalization res.			
	Transfer to General			
	Reserve			5,00,000
	Appropriations			
	Total			70,000
				5,70,000
4.	Long Term Borrowings			
	a. 9% Debentures (Secured by charge of fixed asset)			
	b. Loan from Bank(Secured by charge of fixed asset)			10,000
	Total			
				58,500
				21,500
5.	Short Term Borrowings			80,000
	Loans and advances from related parties			30,000
	- From Directors			
6.	Trade Payables			
	a. Sundry creditors			
	b. Bills Payable			
	Total			
			1,62,500	
7.	Other Current Liabilities		60,000	
	Interest accrued and due on Debentures			1,02,500
				93,000
				1,95,500
	Short term provisions			
8.	a. Provision for tax			
	Less: Advance Tax			
	b. Proposed Dividends			20,000
	Total			
9.	Other non current assets			1,30,000

	Share issue expenses (assumed for 12 months)			1,00,000 1,75,000 4,05,000
10.	Inventories a. Raw Material b. Work in Progress c. Finished Goods Total			32,500 1,00,000 1,32,500
11.	Trade Receivables Unsecured, considered good - More than 6 months - Other Total			2,30,000 12,500 2,42,500
12.	Cash and Cash Equivalents a. Balance with Banks b. Cash in Hand Total Short term loans and advances Unsecured, Considered good a. Bills Receivable b. Staff advances c. Advance to suppliers .			45,000 1,20,000 27,500 1,92,000

Note: Excess of Tax provision after deducting advance tax is shown under short term provision.

Illustration 2 (Balance Sheet)

1. Following is the trial balance of KKK Ltd. as on 31st March, 2015

Debit Balance	Rs.	Credit Balances	Rs.
Fixed Assets (Net Block)	7,50,000	Equity share capital	
Investments	2,50,000	(Rs. 10/- each fully paid)	4,40,000
Closing Stock	3,75,000	9% Preference Share Capital	
Sundry Debtors	1,22,500	(Rs. 100/- each fully paid)	1,00,000

Preliminary Expenses	20,000	Profit and Loss Account	2,80,000
Staff Advance	1,00,000	Securities Premium	30,000
Advance Tax	60,000	Debenture Redemption Reserves	2,00,000
Bills Receivables	45,000	General Reserves	75,000
Advance to Suppliers	27,500	8% Debentures	5,25,000
Cash in Hand	12,500	Loan from Director Mr. D	10,000
Bank Balance	1,10,000	Loan from Subsidiary Co.	70,000
		Sundry Creditors	58,500
		Bills Payable	21,500
		Provision for Taxation	62,500
	18,72,500		**18,72,500**

Additional Information

(a) Transfer to debenture redemption reserves Rs. 50,000/- and Genera, Reserves Rs. 25,000/-.

(b) The Company declared dividend on Equity share capital at 15% after declaring preference dividend.

(c) Entire authorised share capital has been issued and subscribed.

(d) 8% Debentures are secured against all fixed assets. The figure in trial balance includes interest accrued and due Rs. 25,000/-.

(e) Loan from Director and subsidiary Co. are unsecured.

(f) Creditors include Creditors for goods Rs. 40,000/- while for expenses Rs. 18,500/-.

(g) Stock comprises of Raw-materials Rs. 2,50,000/-, work in progress Rs. 50,000/- and Finished goods Rs. 75,000/-.

(h) Of the debtors, debts due for more than 6 months is Rs. 22.500/-. All debit are unsecured and considered to be good.

(i) Profit and Loss Account figure in Trial Balance is arrived at as under

	Rs.

Previous Year's Balance b/d	1,48,500
Net Profit for the Year	1,31,500
	2,80,000

(j) Ignore Previous Year's figures. After considering the above adjustments, prepare Balance Sheet of the company as at that date in the vertical form as per schedule VI requirements

(MU. Mar. 08)

Solution:

KKK Ltd.
Balance Sheet as at 31st March 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholder's Funds			
a. Share Capital	1	5,40,000	
b. Reserves and Surplus	2	5,10,000	10,50,000
2. Non-Current Liabilities			
Long Term Borrowings	3		
3. Current Liabilities			5,00,000
a. Short term Borrowings			
b. Trade Payables	4	80,000	
c. Other Current	5	80,000	
Liabilities	6	25,000	2,62,500
d. Short term Provisions	7	77,500	18,12,500
Total			
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
Tangible Assets	8	7,50,000	
b. Non Current Investments		2,50,000	10,20,000
		20,000	
c. Other non current assets			
2. Current Assets			
a. Inventories	9	3,75,000	
b. Trade receivables	10	1,22,500	
c. Cash and cash	11	1,22,500	7,92,500
equivalents	12	1,72,500	18,12,500
d. Short term loans and advances.			
Total			

Notes to Accounts

Note	Particulars	Amount	Amount	Amount
1.	**Share Capital**			
	Equity share capital			
	Authorised, Issued, Subscribed and fully paid shares (Rs.10)			4,40,000
	Preference Share Capital			
	9% Pref. Shares			
	Authorised, Issued, Subscribed and fully paid shares (Rs.100)			1,00,000
	Total			5,40,000
	Reserves and Surpluses			
2.	a. Securities Premium			
	b. Debenture Redemption			30,000
	Reserve		2,00,000	
	Opening Balance		50,000	2,50,000
	Additions during year		75,000	
	c. General Reserves		25,000	1,00,000
	Balance b/d			
	Transferred from Profit & Loss a/c			
	d. Surplus / (Deficit)			
	Balance in	1,48,500	2,80,000	
	Statement of P & L	1,31,500		
	Surplus for the year			
	Available for Appropriations	9,000		
	Less: Allocations	66,000		
	Dividend –	50,000	1,50,000	
	Preference	25,000		
	Dividend- Equity			
	Transfer to Debenture			

	Redemption Res.			
	Transfer to General Reserve			1,30,000
	Appropriations			5,10,000
	Total			
	Long Term Borrowings			
3.	8% Debentures (Secured by charge of fixed asset)			5,00,000
	Short Term Borrowings			
4.	Loans and advances from related parties			
	- From Directors			10,000
	- From Subsidiaries			70,000
	Total			80,000
	Trade Payables			
5.	a. Sundry creditors for goods			40,000
	b. Sundry creditors for expenses			18,500
	c. Bills Payable			21,500
	Total			80,000
	Other Current Liabilities			
6.	Interest accrued and due on Debentures			25,000
	Short term provisions			
7.	a. Provision for tax		62,500	
	b. Less: Advance Tax		60,000	2,500
	Proposed Dividends			75,000
	Total			77,500
	Other non current assets			
8.	Share issue expenses (assumed for more than 12 months)			20,000
	Inventories			
9.	a. Raw Material			2,50,000
	b. Work in Progress			50,000
	c. Finished Goods			75,000
	Total			3,75,000
	Trade Receivables			
	Unsecured, considered			

10.	good - More than 6 months - Other Total			22,500 1,00,000 1,22,500
11.	**Cash and Cash Equivalents** a. Balance with Banks b. Cash in Hand Total			1,10,000 12,500 1,22,500
12.	**Short term loans and advances** Unsecured, Considered good a. Pre-paid expenses b. Staff advances c. Advance to suppliers .			45,000 1,00,000 27,500 1,72,000

Note: Excess of Tax provision after deducting advance tax is shown under short term provision.

Illustration 3

Following balances are extracted from the books of SURE SUCCESS CO. LTD. as on 31st March 2015

	Rs.		Rs.	Rs.
Freehold Factory Premises	6,00,000	2,00,000 Equity Shares of Rs. 10 each		20,00,000
Leasehold Office Premises	5,00,000	5,000 6% Debentures of Rs. 100 each		5,00,000
Bank Balance	60,500	General Reserves		75,000
Vehicles	3,15,000	Sinking Fund for Leasehold Premises		15,000
Plant & machinery	8,30,000	**Profit & loss Account**		
Sundry Debtors	2,40,000	Balance B/d	47,450	
Computer	30,000	+ Net Profit after tax	2,90,000	
Goodwill	2,00,000		3,37,450	
Stock	1,30,000	- Debenture Interest	30,000	3,07,450
Cash in Hand	1,950	Provision for tax [Accounting Year 2003]		1,50,000
Advance Income Tax :		Provision for tax [Accounting Year 2004]		1,80,000
- [Accounting Year 2011]	1,45,000			
- [Accounting Year 2012]	1,75,000			
	32,27,450			**32,27,450**

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ADJUSTMENTS :-

During the current year Income Tax assessment for the accounting year is completed with a gross demand of Rs. 1,35,000 but no effect of the same is given in the accounts of the current year.

(2) The Board of Directors decided to provide :-

(i) 20% Bonus on the year's salary of Rs. 1,00,000

(ii) 10% Sinking fund on leasehold premises

(iii) Rs. 5,000 as Director's fees

(iv) 5% Dividend for the year to the shareholders

(v) Transfer Rs. 50,000 to General Reserves.

Considering the above Trial Balance and the adjustments and assuming that there will be no change in the provision for tax of the accounting year 31st March 2015 on account of changes if any, prepare Profit and Loss Account for the year ended 31st March 2015 and the Balance Sheet as on that date in a vertical form keeping in mind the prescribed formats and applicable accounting standards. Ignore previous year's figures

(MU 2005):

Sure Success Co. Ltd.

Balance Sheet as at 31st March 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholder's Funds			
a. Share Capital	1	20,00,000	
b. Reserves and	2	2,22,450	22,22,450
Surplus			
2. Non-Current Liabilities	3		5,00,000
Long Term Borrowings			
3. Current Liabilities	4	25,000	
a. Trade Payables	5	1,05,000	1,30,000
b. Short term			28,52,450
Provisions			
Total			
ASSETS			
1. Non Current Assets	6	22,10,000	
Fixed Assets		2,00,000	24,10,000
- Tangible Assets			
- Intangible Assets	7	1,30,000	
(Goodwill)	8	2,40,000	
2. Current Assets	9	62,450	4,42,450
a. Inventories	10	10,000	28,52,450
b. Trade receivables			
c. Cash and cash equivalents			
d. Other current assets			
Total			

Profit and Loss Statement for the year ended 31st March 2015

Particulars	Amount	Amount
1. Revenue from operations (NPBT 2,90,000 + 1,80,000)		4,70,000
		4,70,000
I. Total Revenue		
Expenses	20,000	
1. Employee Benefits expenses (Bonus)	30,000	
2. Finance Costs (Interest on Debenture)	50,000	
3. Depreciation and Amortization Exps	5,000	
(Leasehold)		1,05,000
4. Other Expenses (Directors Fees)		3,65,000
II. Total Expenses	1,80,000	
III. Profit Before Tax	(15,000)	(1,65,000)
Provision for tax current year		2,00,000
Excess Provision for Tax L.Y. Written back		
IV. Profit / Loss for the period		

Notes to Accounts

Note	Particulars	Amount	Amount	Amount
1.	**Share Capital**			
	Equity share capital			
	Authorized, Issued,			
	Subscribed and fully paid			20,00,000
	shares (Rs.10)			
2.	**Reserves and Surpluses**			
	a. General Reserves		75,000	
	Balance b/d		50,000	1,25,000
	Transferred from			
	Profit & Loss a/c	47,450		
	b. Surplus / (Deficit)	2,00,000		
	Balance in		2,47,450	
	Statement of P & L			
	Surplus for the year	1,00,000		
	Available for	50,000		
	Appropriations		1,50,000	
	Less: Allocations			
	Dividend- Equity			
	Transfer to General Reserve			
	Appropriations			
	Total			
3.	**Long Term Borrowings**			97,450
	5,000 6%Debentures of			2,22,450
	Rs.100			
				5,00,000
4.	**Trade Payables**			
	a. Bonus payable			20,000
	b. Directors fees			5,000
	payable			25,000
	Total			
5.	**Short term provisions**			5,000
	a. Provision for tax			1,00,000
	(1,80,000 – Adv			1,05,000
	Tax 1,75,000)			
	b. Proposed			
	Dividends			**22,10,000**
	Total			
6.	**Fixed Assets** (see table below)			1,30,000
7.	**Inventories**			
	Stock in trade			
8.	**Trade Receivables**			2,40,000
	Unsecured, considered good			
9.	**Cash and Cash Equivalent**			60,500 1,950

	a. Balance with banks b. Cash on hand c. Total			62,450
10.	**Other Current Assets** Tax Refund Receivables			10,000

Fixed Assets

Assets	Gross Block			Provision for Depreciation			Net Block	
	Opening	Additions	Closing	Opening	Additions	Closing	Opening	closing
Tangible Assets								6,00,000
Free hold premises			5,00,000	15,000	50,000	65,000	4,85,000	4,35,000
Leashold premises								8,30,000
Plant & Machinery								30,000
Computers								3,15,000
Vehicles								
								22,10,000

Calculation of Refund due from Tax A/C

Provision for Tax A/c

Particulars	Amount	Particulars	Amount
To Advance Tax To Profit and Loss Account	1,45,000 15,000	By Balance b/d By Refund due	1,50,000 10,000
	1,60,000		1,60,000

Illustration 4:

The following balances relate to Himalaya Co. Ltd. as on 31st March, 2015:

	Dr. Rs.		Cr. Rs.
Motor car	8,000	Share forfeiture Account	500
(Cost less Depreciation)	60,000	Share Capital	1, 00,000
Sundry Debtors		Profit & Loss (31.3.2008)	1,500
Furniture		Gross profit	54,150
(Cost less Depreciation)	4,000	Development rebate	1,350

Plant (Cost less Depreciation)	15,000	reserve	
		Bank overdraft 0 UCO	25,000
Compensation to employees	2,000	Sundry creditors	11,000
Closing stock	35,000	Liabilities for expenses	3,500
Rent and Taxes	8,000		
Selling Expenses	10,000		
Office expenses, etc.	12,000		
Security deposit	4,000		
Advance income tax	9,000		
Cash in hand	2,500		
Cash at bank	27,500		
	1, 97,000		**1, 97,000**

The following additional information is also available:

a) Share capital consists of:
   i) 15,000 10% cumulative preference shares of Rs. 100 each, out of which 500 shares are fully called up and paid-up.
   ii) 15,000 equity shares of Rs. 10 each, out of which5,000 shares are fully called up and paid-up.

b) Transfer Rs. 900 to be development rebate reserve account on 31st March 2015.

c) Bank overdraft secured by the hypothecation of stock.

d) The manager is entitled to 5% commission on the net profit of the company.

e) Addition made to plant during the year ended 31st March, 2015 was Rs. 8,000.

f) Depreciation written off up to 31st March, 2014 and rates against each are as under:

	Amount (Rs.)	**Rate (%)**
Plant	2,000	15
Furniture	10,000	10
Motor Car	10,000	20

g) Provision for taxation to be made at Rs. 9,600.

h) The amount shown against shares forfeited account represents unadjusted profit on reissue of forfeited shares made during the year.

i) Sundry debtors include outstanding Rs. 1,000 for more than six months.

j) Office expenses include Rs. 1,500 as audit fee and Rs. 500 as audit expenses.

You are required to draw:

i) The profit & loss account for the year ended on 31st March, 2015, and

ii) The Balance Sheet (in revised schedule VI) as on that date.

	Himalaya Co. Ltd. **BALANCE SHEET AS AT 31ST MARCH 2015**		**(Amount in Rs.)**
	Particulars	**Notes**	
I	**EQUITY AND LIABILITIES**		
1	**Shareholders' funds**		
	(a) Share capital	1	100,000
	(b) Reserves and surplus	2	12,850
4	**Current liabilities**		
	(a) Short-term borrowings	3	25,000
	(b) Trade Payables	4	11,000
	(c) Other current liabilities	5	3,500
	(d) Short-term provisions	6	9,600
	TOTAL		**161,950**

II	**ASSETS**		
1	**Non-current assets**		
	(a) Fixed assets		
	Tangible assets		
	Motor Car		6,400
	Furniture		3,600
	Plant		13,950
2	**Current assets**		
	(a) Inventories	7	35,000
	(b) Trade receivables	8	60,000
	(c) Cash and cash equivalents	9	30,000
	(e) Other current assets	10	13,000
	TOTAL		**161,950**

Profit and Loss statement for the year ended 31st March 2015

Particulars		Notes	
I.	Revenue from operations	11	54,150
II.	**Total Revenue**		**54,150**
III.	Expenses:		
	Employee Benefit Expenses	12	2,000
	Depreciation and amortization expense	13	3,050
	Other Expenses	15	30,000
	Total expenses		**35,050**
IV.	**Profit before tax (II- III)**		**19,100**
V	Tax expense:		
	(1) Current tax		9,600
VI	**Profit (Loss) for the period from continuing operations**		**9,500**

Himalaya Co. Ltd.

Notes to Financial Statements for the year ended 31 March, 2015

	Number	`
Note "1" : SHARE CAPITAL		
Authorised Shares		
Equity Shares of `10 each	15,000	150,000
10% Cum Pref Shares of `100 each	15,000	1,500,000
Issued, Subscribed & Fully Paid up Shares		
Equity Shares of `10 each	5,000	50,000
10% Cum Pref Shares of `100 each	500	50,000
Total	**5,500**	**100,000**

Note "2" : RESERVES & SURPLUS	
Surplus	
Reserves & Surplus	
Opening balance	1,500
(+) Net Profit/(Net Loss) For the current year	9,500
(-) Transfer to Development Reserve	(900)
Closing Balance	**10,100**
Capital Reserve	**500**
Development Rebate Reserve	**1,350**
(+) Additions for the current year	**900**
Closing Balance	**2,250**
Total	**12,850**

Note "3" : SHORT-TERM BORROWINGS	
Secured	
Loans repayable on demand	
Bank Od	
(Secured by Hypothecation of Stock)	25,000
Total	**25,000**

Note "4" : TRADE PAYABLES	
(a) Trade Payables	
Acceptances	-
Other than Acceptances	11,000
Total	**11,000**
Note "5" : OTHER CURRENT LIABILITIES	
(a) Current maturities of long-term debt	-
(b) Others	
Creditors for Expenses & Others	3,500
Statutory Liabilities	
Total	**3,500**
Note "6" : SHORT-TERM PROVISIONS	
(a) Others	
Provision for Tax	9,600
Total	**9,600**
Note "7" : INVENTORIES	
Stock - in - Trade	35,000
Total	**35,000**
Note "8" : TRADE RECEIVABLES	
Trade receivables outstanding for a period less than six months	59,000
Unsecured, considered good	
Trade receivables outstanding for a period exceeding six months	
Unsecured, considered good	1,000
Less: Provision for doubtful debts	-
Total	**60,000**

Note "9" : CASH & BANK BALANCES	
a. Balances with banks	27,500
b. Cash on hand	2,500
Total	**30,000**
Note "10" : OTHER CURRENT ASSETS	
Advance Tax	9,000
Security Deposit	4,000
Total	**13,000**
Note "11" : REVENUE FROM OPERATIONS	
Sale of products	54,150
Total	**54,150**
Note "12" : EMPLOYEE BENEFIT EXPENSES	
Employee Benefits Expense	
(a) Salaries	2,000
Total	**2,000**
Note "13" : DEPRECIATION & AMORTIZATION EXPENSES	
Depreciation on Tangible Assets	
Motor Car	1,600
Furniture	400
Plant	1,050
Total	**3,050**
Note "14" : OTHER EXPENSES	
Rent Sales & tax	8,000
Selling Expenses	10,000
Audit Fees	1,500
Audit Expenses	500
Office Expenses	10,000
Total	**30,000**

Illustration 4

The following is the Trial Balance of Bee Ltd. as on 31st March, 2015

Debits	Rs.	Credits	Rs.
Stock as on 1.4.2014	75,000	Prov. for Dep.on Plant & Machinery	10,000
Purchases	2,45,000	Sales	3,70,000
Wages	30,000	Discount	3,000
Carriage	950	Profit and Loss Account	15,000
Furniture	17,000	Share Capital(Rs. 10 fully paid)	1,00,000
Bad Debts	7,500	Creditors	17,500
Rent	4,000	General Reserve	15,500
Sundry trade expenses	7,050	Bills payable	7,000
Dividend paid	12,500	Bank Loan	64,500
Debtors	39,000	10% Debentures	90,000
Plant and Machinery	79,000		
Cash at bank	46,200		
Patents	4,800		
Bill Receivable	20,000		
Interest on Bank Loan	11,600		
Deb. Interest	4,000		
Freehold Land	88,900		
	6,92,500		**6,92,500**

Prepare the Profit and Loss Account for the year ended 31st March, 2015 and a Balance Sheet as on that date after considering the following adjustments:

I. Stock as on 31st March, 2015: Rs. 88,000.

II. Provide for income tax at 50%.

III. Depreciate plant and machinery at 15%; furniture at 10%; and patents at 5%.

IV. On 31st March, 2015 outstanding rent amounted to Rs.800

V. The Board recommends payment of a dividend @ 15% per annum. Transfer the minimum required amount from General Reserve.

Solution:

This problem has been solved considering Corporate Dividend Tax @17%.

Bee Ltd.
Profit and Loss Statement for the year ended 31st March, 2015

Particulars	Note	Amount	Amount
2. Revenue from operations (Sales)		3,70,000	
3. Other Receipts (Discount)		3,000	
V. Total Revenue			3,73,000
Expenses			
1. Purchase of stock in trade		2,45,000	
2.Change in Inventories in trade		(13,000)	
3. Employee Benefits expenses		30,000	
4. Other Operating Expenses	7	20,300	
5. Finance Costs	8	15,600	
6. Depreciation and Amortization Exps	9	9,840	
VI. Total Expenses		3,07,740	
VII. Profit Before Tax		65,260	
Provision for tax current year @ 50%		32,630	32,630
Profit / Loss for the period			
Provision for corporate dividend tax			2,550
			30,080

Balance Sheet as at 31st March, 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholder's Funds			
c. Share Capital	1	1,00,000	
d. Reserves and Surplus	2	45,580	1,45,580
2. Non-Current Liabilities			
Long Term Borrowings	3		1,54,500
3. Current Liabilities			
c. Trade Payables	4	24,500	
d. Other Current Liabilities		800	
e. Short term Provisions	5	37,680	62,980
Total			**3,63,060**
ASSETS			
3. Non Current Assets			
Fixed Assets			
- Tangible Assets	6	1,65,300	
- Intangible Assets		4,560	1,69,860

4. Current Assets			
e. Inventories		88,000	
f. Trade receivables		59,000	
g. Cash and cash equivalents		46,200	1,93,200
Total			**3,63,060**

Notes to Accounts

Note	Particulars	Amount	Amount	Amount
1.	**Share Capital**			
	Equity share capital			
	Authorised, Issued, Subscribed and fully paid shares (Rs.10)			1,00,000
2.	**Reserves and Surpluses**			
	c. General Reserves		15,500	
	Balance b/d		1,631	17,131
	Transferred from Profit & Loss a/c	32,630		
	d. Surplus / (Deficit)	15,000		
	Balance in Statement of P & L			
	Surplus for the year Available for Appropriations		47,630	
	Less: Allocations		15,000	
	Dividend- Equity			
	Transfer to General Reserve(Statutory		1631	
	5%)		2550	28,449
	Less : Provision for Corporate Dividend Tax			45,580
	Total			
3.	Long Term Borrowings		90,000	1,54,500
	900, 10 %Debentures of Rs.100		64,500	
	Bank Loan			
4.	Trade Payables		17,500	
	c. Creditors		7,000	
	d. Bills payable			24,500
	Total			

5.	Short term provisions c. Provision for tax d. Provision for CDT Proposed Dividends Total		32,630 2,550 2,500	37,680
6.	Fixed Assets (see table below)			
7.	Other Operating Expenses Carriage Bad debts Rent Add: Outstanding Sundry Trade Expenses	4000 800	950 7500 4800 7050	20,300
8.	Finance Cost Interest on Bank Charges Debenture Interest		11,600 4000	15600
9.	Depreciation & Amortization Expenses Plant and machinery @10%; Furniture at 10%; Patents at 5%.		7900 1700 240	9840

Fixed Assets

Assets	Gross Block			Provision for Depreciation			Net Block	
	Opening	Additions	Closing	Opening	Additions	Closing	Opening	closing
Tangible Assets								
Free hold premises	88,900		88,900				88,900	88900
Plant & Machinery	79000		79000	10,000	7,900	17,900	69,000	61,100
Furniture	17000		17000		1,700	1,700	17,000	15,300
								1,65,300

Notes:

1. Dividend of Rs.12,500 appearing in the Trial Balance is treated as interim, dividend. The Board recommends payment of dividend @ 15% p.a. It means that interim dividend is also a part of 15% dividend per annum. Therefore Rs.2,500 (Rs. 15,000 - Rs. 12,500) is to be provided as proposed Dividend.

2. Where proposed dividend exceeds 12.5% but does not exceed 15% of the paid-up capital, the amount to be transferred to Reserve should not be less than 5% of the current profit.

Therefore, amount to be transferred to Reserve = 5% of Rs. 19,630= Rs. 982.

3. Corporate dividend tax is payable on Rs. 15,000 (Rs. 9,000 paid + Rs. 6,000 proposed) @ 17% = Rs. 2,550.

Illustration 5: Premier Ltd has Authorized share capital as follows:

Equity share capital	
30,000 Equity Shares Rs. 100/- each fully paid	**30,00,000**
Preference Share Capital	
8,000, 8% Preference Shares Rs. 100/- each fully paid	**8,00,000**

Following is the trial balance of Premier Ltd. as on 31st March, 2015.

Debit Balance	Rs.	Credit Balances	Rs.
Land & Building	9,00,000	Discount Received	3,800
Purchases	1,00,000	Transfer Fees	1,700
Wages	20,300	Equity share capital	
Investments	2,46,000	(Rs. 100/- each fully paid)	7,00,000
Rent	9,800	8% Preference Share Capital	
Sundry Debtors	90,320	(Rs. 100/- each fully paid)	6,00,000
Consumables	3,290	Profit and Loss Account	1,21,500
Sundry Expenses	6,840	Sales	1,26,300
Advertising	15,000	Capital Reserve	25,000
Bills Receivables	45,000	General Reserves	1,50,000
Stock(1-4-2011)	20,000	10% Debentures	1,00,000
Cash in Hand	85,000	Rent	73,700
Preliminary Expenses	18,000	Miscellaneous Receipts	10,800
Repair	6,250	Sundry Creditors	48,000
Furniture	40,000		
	19,60,800		**19,60,800**

Additional Information

(Wages and Salaries outstanding 5,900

— Stock as on 31st March, 2015 40,200

— Provide 10 % depreciation on Furniture and 5 % on Land and Building.

The equity capital on 1st April, 2014 stood at `7,00,000, that is 7,000 shares fully paid.The director proposes a dividend of 9 % on equity shares, transferring any amount that may be required from general reserve. Ignore taxation. Ignore Previous Year's figures. After considering the above adjustments, prepare Balance Sheet of the company as at that date as per revised schedule VI requirements

Solution:

Premier Ltd.

Profit and Loss Statement for the year ended 31st March 2015

Particulars	Note	Amount	Amount
4. Revenue from operations			2,00,000
Other Receipts	9		16,300
VIII. Total Revenue			2,16,300
Expenses			
1. Purchases of Stock in trade		1,00,000	
2. Changes in inventories of Finished Goods		(20,200)	
3. Employee Benefits expenses	10	26,200	
4. Finance Costs (Interest on Debenture)		10,000	
5. Depreciation and Amortisation Exps	11	49,000	
6. Selling & Admn. Exps		15,000	
7. Other Expenses	12	26,180	
IX. Total Expenses		2,06,180	
X. Profit Before Tax			10,120
XI. Bal from previous year			1,21,500
Less Proposed Divided			1,31,620
Preference Share Capital @ 8%			48,000
Equity Share Capital @ 9 %			63,000
XII. Profit / Loss for the period			20,620

Balance Sheet as at 31st March 2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
5. Shareholder's Funds			
e. Share Capital	1	13,00,000	
f. Reserves and Surplus	2	1,95,620	14,95,620
6. Non-Current Liabilities	3		1,00,000
Long Term Borrowings	4	53,900	
7. Current Liabilities	5	1,21,000	1,74,900
e. Trade Payables			**17,70,520**
f. Short term Provisions			
Total			
ASSETS			
3. Non Current Assets	6	8,91,000	
d. Fixed Assets		4,00,000	
- Tangible Assets			
- Intangible Assets (Goodwill)		2,46,000	15,37,000
e. Non Current Investments		40,200	
		90,320	
4. Current Assets	7		
e. Inventories		85,000	
f. Trade receivables	8	18,000	2,33,520
g. Cash and cash equivalents			**17,70,520**
h. Other Current Assets			
Total			

Notes to Accounts

Note	Particulars	Amount	Amount	Amount
1.	**Share Capital**			
	Authorised			
	Equity share capital			
	30,000 Equity Shares Rs. 100/- each fully paid			30,00,000
	Preference Share Capital			
	8,000 Preference Shares Rs. 100/- each fully paid			<u>8,00,000</u> <u>38,00,000</u>
	Issued, Subscribed and fully paid shares (Rs.100)			
	Equity share capital			
	7000 Equity Shares Rs. 100/- each fully paid		7,00,000	
	Preference Share Capital			
	6,000 Preference Shares Rs. 100/- each fully paid		<u>6,00,000</u>	13,00,000
	Total			
2.	**Reserves and Surpluses**			
	e. Capital Reserve			
	f. General Reserve			
	Balance in Statement of P & L			25,000 1,50,000
	Surplus for the year	1,21,500		
	Available for Appropriations	10,120		
	Less: Allocations	1,31,620		
	Dividend – Preference			
	Dividend- Equity			
	Total			
3.	Long Term Borrowings	48,000		<u>20,620</u>
	2000, 10% Debentures of Rs.100 each	<u>63,000</u>		1,95,620
	Trade Payables			1,00,000
4.	d. Sundry creditors			
	e. Wages Outstanding			
	Total			

	Short term provisions			
5.	c. Interest due on Debentures		48,000	
			5,900	
	d. Proposed Dividends			53,900
	i. Equity			
	ii Preference			
	Total		10,000	
	Tangible Assets			
6.	Free hold Land & Building			
	Less :Depreciation @ 5%		63,000	
	Furniture		48,000	
	Less :Depreciation @ 10%			1,21,000
	Cash and Cash Equivalents	9,00,000		
7.	c. Cash in Hand	45,000		
			8,55,000	
	Other Current Assets	40,000		8,91,000
8.	Preliminary expenses(assumed to be amortised in 12 months)	4,000	36,000	
				85,000
	Other Receipts			
9.	Miscellaneous Receipts		10,800	18,000
	Discount Received		3,800	
	Transfer Fee		1,700	
	Employee Benefits expenses			16,300
			20,300	
10.	Wages		5,900	
	Add: Outstanding			26,200
	Depreciation and Amortisation Exps		45,000	
11.			4,000	
	Land & Building			49,000
	Furniture			
			9,800	
	Other Operating Expenses		3,290	
12.	Rent		6,250	
	Consumables		6,840	
	Repair			26,180
	Sundry Expenses			

Illustration No. 6

The Trial balance of Alpha Ltd. as on 31st March, 2015 is given below:

Debit Balances	Rs.	Credit Balances	Rs.
Calls in Arrears	5,000	Authorized Capital	
Freehold buildings	2, 00,000	60,000 equity shares of	
Plant & Machinery	2, 20,000	Rs. 10 each	6, 00,000
Interim dividend paid	25,000	Issued & Subscribed	
Opening stock	1, 90,000	Capital	4, 00,000
Furniture	5,000	8% Debentures	
Patterns	51,500	(Secured)	2, 00,000
Patents	40,000	Profit & Loss A/c	21,400
Sundry Debtors	2, 77,000	Bill payable	90,000
Cash in hand	4,500	Sundry Creditors	1, 77,000
Cash at bank	88,000	Sales	12, 35,000
Purchases	6, 36,550	Discount received	11,800
Preliminary Expenses	8,000	Sinking fund	
Sinking Fund Investment	50,000	Redemption of	
Wages	2, 95,000	Debentures	50,000
Repairs & Renewals	12,000	Provision for	
Factory power	25,000	Doubtful debts	12,500
Rates & Taxes	13,500	Royalties received	3,250
Salaries	11,250	Interest on Sinking fund	
Travelling Expenses	10,750	Investment	2,000
Discount allowed	20,200		
Directors Fees	4,200		
Bad debts	2,500		
Debentures interest	8,000		
	22,02,950		22, 02,950

Additional Information:

1. Depreciate plant & machinery, furniture, pattern and patents at 10%.
2. Write of Rs. 2,000 from preliminary expenses.
3. Transfer Rs. 10,000 to sinking fund for redemption of debentures.
4. Maintain bad & doubtful debts provision at 5% on sundry debtors.
5. Stock was valued at Rs.80,750 (at cost).

You are required to prepare profit & loss account showing gross profit and net profit for the year ended 31st March, 2015 and a balance Sheet (in prescribed from) as on that date.

Alpha Ltd.
Balance Sheet as at 31st March, 2015

Particulars	Note	Amount	Amount

EQUITY AND LIABILITIES			
1. Shareholder's Funds			
e. Share Capital	1	3,95,000	
f. Reserves and Surplus	2	1,07,250	5,02,250
2. Non-Current Liabilities			
a. Secured Loans (8% Debentures)			2,00,000
3. Current Liabilities			
f. Trade Payables			2,67,000
g. Other Current Liabilities	3		8,000
Total			**9,77,250**
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
- Tangible Assets	4	4,48,850	
- Intangible Assets (Patents)		36,000	4,84,850
b. Non-Current Investments	5		50,000
2. Non Current Assets	6		6,000
3. Current Assets			
h. Inventories		80,750	
i. Trade receivables		2,63,150	
j. Cash and cash equivalents		92,500	4,36,400
Total			**9,77,250**

Profit and Loss Statement for the year ended 31st March 2015

Particulars	Note	Amount	Amount
5. Revenue from operations			12,35,000
Other Receipts	7		15,050
I. Total Revenue			12,50,050
Expenses			
5. Purchases of Stock in trade		6,36,550	
6. Changes in inventories of Finished Goods	8	1,09,250	
7. Employee Benefits expenses	9	3,06,250	
8. Depreciation and	10	31,650	

	Amortisation Exps			
	9. Admn., Selling &Other Exps	11	89,500	
	10. Finance Cost (Int. on Deb.)		16000	
			11,89,200	
II.	Total Expenses			
				60,850
III.	Profit Before Tax			
IV.	Less Miscellaneous Expenses w/off			2,000
				58,850
V.	Profit / Loss for the period			21,400
VI.	Bal from previous year			80,250
				25,000
	Less :Interim Dividend			
	Transfer to Sinking fund for Debenture redemption			10,000
VII.	Profit / Loss for the period			
				45,250

Notes to Accounts

Note	Particulars	Amount	Amount	Amount

1.	**Share Capital** **Authorised** **Equity share capital** 60,000 Equity Shares Rs. 10/- each fully paid			**6,00,000**
	Issued, Subscribed and fully paid shares (Rs.10) Equity share capital 4000 Equity Shares Rs. 10/- each fully paid		4,00,000	
	Less: Unpaid calls		5,000	3,95,000
	Total			**3,95,000**
2.	**Reserves and Surpluses** a. Sinking fund for Debenture redemption Balance		50,000	
	Additions for the year		10,000	
	Add: Interest		2,000	62,000
	b. Balance in Statement of P & L Surplus for the year		80,250	
	Available for Appropriations Less: Allocations Dividend- Interim		25,000	
	Transfer to Sinking fund for Debenture		10,000	45,250
	redemption			1,07,250
3.	Other Current Liabilities Interest accrued on debentures			8,000
4.	Tangible Assets		2,00,000	
	Freehold Building	2,20,000		
	Plant & Machinery(Balance)	22,000	1,98,000	
	Less :Depreciation @ 10%	5,000		
	Furniture	500	4,500	
	Less :Depreciation @ 10%	51,500		
	Patterns	5,150	46,350	4,48,850
	Less :Depreciation @ 10%			

Note	Particulars	Amount	Amount	Amount
6.	Non Current Assets Preliminary expenses(			

	assumed not to be amortised in 12 months)			6,000
7	Other Receipts			
	Discount Received		11,800	
	Royalties		3,250	15050
8	Changes in inventories of Finished Goods			
	Opening		1,90,000	
	Less: Closing		80,750	1,09,250
9	Employee Benefits			
	expenses		2,95,000	
	Wages		11,250	3,06,250
	Salaries			
10				
	Depreciation and			
	Amortisation Exps		22,000	
	Plant & Machinery		500	
	Furniture		5,150	
	Patterns		4,000	31,650
	Patents			
11				
	Other Operating Expenses		12,000	
	Repairs & Renewals		25,000	
	Factory power		13,500	
	Rates & Taxes		10,750	
	Travelling Expenses		20,200	
	Discount allowed		4,200	
	Directors Fees		3,850	89,500
	R.D.D			

EXERCISES:

A. OBJECTIVE QUESTIONS:

- **Multiple Choice Questions**

1. Accounting Standard 1 is
   (a) Recommendatory (b) Mandatory
   (c) Optional (d) No longer valid

2. Purpose of Accounting Standard 1 is to establish a standard as to

(a) The desirable accounting policies
(b) The fundamental accounting assumptions
(c) Disclosure of accounting policies
(d) Preparation of final accounts

3. Vide Accounting Standard 1, fundamental accounting assumptions should
(a) Always be disclosed
(b) Be disclosed if not allowed
(c) Be disclosed in notes to accounts
(d) Be disclosed in auditor's report

4. Following is an example of an accounting policy
(a) Going concern
(b) Accrual
(c) Treatment of retirement benefits
(d) Disclosure

5. A concern should select an accounting policy which enables it to
(a) Show good profits
(b) Present a true and fair view of its state of affairs and profit or loss
(c) Calculate the correct amount of cash in hand
(d) Pay the proper amount of income-tax

6. According to AS 1, Disclosure should be made of
(a) Fundamental accounting assumptions
(b) All accounting principles
(c) All significant accounting policies
(d) All Accounting policies

7. According to AS 1, Disclosure should form part of
(a) The final accounts (b) The Auditor's report
(c) The Directors Report (d) The Books of Accounts

8. According to AS 1, any change in accounting policy
(a) Should never be made
(b) Is not possible
(c) Should be disclosed
(d) Requires permission of the Institute of Chartered Accountants of India

9. Which of the following should be deducted from the share capital to find out paid-up capital?
(a) Calls-in-advance (b) Calls-in-arrears
(c) Securities Premium (d) Bonus

10. Dividends are usually paid on
    - (a) Authorized capital (b) Issued capital
    - (c) Paid up capital (d) reserve capital

11. Which of the following is not shown under the head 'Share Capital' in the balance sheet of a company?
    - (a) Preference Share Capital
    - (b) Calls-in-arrears
    - (c) Forfeited Shares
    - (d) Preference Dividend

12. Which of the following items is not taken in Profit and Loss Appropriation Account
    - (a) Proposed Dividend
    - (b) Provision for Taxation
    - (c) Transfer to general reserve
    - (d) Transfer to dividend equalization reserve

13. Which of the following items cannot be shown as reserves?
    - (a) Securities premium
    - (b) Capital Reserve
    - (c) Capital Redemption Reserve
    - (d) None of the above

14. As per schedule VI, to the companies Act, 1956 'unclaimed dividends' are to be shown as
    - (a) Current Assets (b) Current Liability
    - (c) Reserves and Surplus (d) None of the above

15. Interim dividend of a company can be declared by
    - (a) Only by shareholders
    - (b) Board of directors after approval of stock exchange
    - (c) Board of directors
    - (d) None of the above

16. Which of the following is not an example of contingent liability?
    - (a) Liability in respect of bills discounted
    - (b) Interim dividend
    - (c) Liability under guarantee
    - (d) All (a), (b) and (c) of the above

17. Which of the following items cannot be shown under the heading 'Provision' with respect to balance sheet under the Companies Act, 1956?
    - (a) Provision for taxation
    - (b) Proposed dividends
    - (c) Provision for doubtful debt
    - (d) Unclaimed dividend

18. Which of the following is not an item under Current Assets, Loans and Advances under Part I of Schedule VI of the Companies Act, 1956?
    (a) Interest accrued on investment
    (b) Bills receivable
    (c) Closing Stock
    (d) Preliminary expenditure not written off

19. Which of the following is not a secured loan?
    (a) Debentures (b) Fixed Deposits
    (c) Term loan from banks (d) None of the above

20. Advance tax that appears in the trial balance is shown
    (a) As a current liability in the balance sheet
    (b) As an expense in the profit and loss account
    (c) Under the head 'loans and advances' in the balance sheet
    (d) Only in cash flow statement as an outflow of cash from operations

Answer: 1. b, 2. c, 3. b, 4. c, 5. b, 6.c, 7. a, 8. c, 9. b,10. c, 11. d, 12. b, 13. d, 14. b, 15. c ,16. b, 17. d, 18. d, 19. b, 20. c

- **Fill in the blanks.**

1. The revised Schedule VI will apply to all the companies uniformly for the financial statements to be prepared for the financial year **2010-11 and onwards**

2. The revised Schedule VI has **eliminated the concept of schedule** and such information will now be provided in **the notes to accounts**.

3. There is an explicit requirement to use the **same unit of measurement uniformly** throughout the financial statements.

4. The revised Schedule VI prescribes a **vertical format for presentation** of balance sheet.

5. "Capital advances" are now required to be presented separately under the head **"Loans & advances"** rather than as part of "capital work-in-progress" or "fixed assets.

6. The term "sundry debtors" has been replaced with the term **"trade receivables."**

7. In addition to specific disclosures prescribed in the P&L account, any item of income or expense which exceeds **1% of the revenue from operations or `100,000,** whichever is higher, needs to be disclosed separately.

8. AS 4 still requires that "dividends stated to be in respect of the period covered by the financial statements, which are proposed or declared by the enterprise after the balance sheet date but before approval of the financial statements, should be **adjusted**". So companies will have to continue to create a provision for dividends in respect of the period covered by the financial statements and disclose the same as a provision in the balance sheet.

9. Revised Schedule VI requires presentation of **trade receivables** as against sundry debtors required by pre-Revised Schedule VI

10. As per Revised Schedule VI of para 6.A.b of General Instructions, details of shares subscribed and fully paid up and details of shares subscribed, but not fully paid up,**should be shown separately.**

11. The schedule does not apply to **Insurance or banking** company, and company engaged in the generation or supply of electricity and any other class of company for which a form of Balance Sheet and Profit and Loss account has been specified in or under any other Act governing such class of company.

12. **Accounting Standards** requires a change in the treatment or disclosure in the Financial Statements as compared to that provided in the Revised Schedule VI, the requirements of the Act and / or the notified Accounting Standards will prevail over the Schedule.

13. Statement of Profit and Loss does not mention any appropriation item **on its face** as against the old schedule

14. Below the line adjustments to be shown under '**reserves and surplus'.**

15. **Disclosure requirements** of the revised schedule VI are in addition to and not in substitution to the notified

16. Separate disclosure required by **<u>Section 293A</u> of the** Act for donations made to political parties.

17. **<u>Dissimilar items</u>** must be presented separately.

18. A company needs to present **<u>comparative information</u>** for disclosures required under Revised Schedule VI even if their current period amount is Nil.

19. **<u>Interest Cost</u>** needs to be disclosed separately as finance cost

20. Amortization of issue expenses and discounts as per AS-16 are to be included under '**<u>Borrowing costs</u>**

21. loan processing charges, guarantee charges, loan facilitation charges, discounts/premium on borrowings, other ancillary costs incurred in connection with borrowings, or amortization of such costs to be included under '**<u>Borrowing costs".</u>**

22. "An asset shall be classified as **<u>current</u>** when it satisfies any ofthe following criteria:

    (a) it is expected to be realized in, or is intended for sale or consumption in, the company's normal operating cycle;

    (b) it is held primarily for the purpose of being traded;

    (c) it is expected to be realized within twelve months after the reporting date; or

    (d) it is Cash or cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date

23. "A liability shall be classified as **<u>current</u>** when it satisfies any of the following criteria

    (a) it is expected to be settled in the company's normal operating cycle;

    (b) it is held primarily for the purpose of being traded;

    c) it is due to be settled within twelve months after the reporting date; or

(d) the company does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date.

24. **Inventories** are the assets held primarily for the purpose of being traded are to be classified as current assets.

25. on the basis of estimated billing schedule, the portion of advance which is projected to be adjusted within 12 months after the reporting date is classified as current and balance is classified as **non current**

26. Numbers of shares held by each shareholder holding more than 5% of shares on balance sheet date to be **disclosed.**

27. Calls unpaid on shares are to be disclosed separately as per the **Revised Schedule VI**

28. Reconciliation of the number of shares outstanding at the beginning and at the end of the reporting period is to be disclosed separately for both **Equity and Preference** Shares and for each class of share capital within Equity and Preference Shares

29. '**Share warrants'** are financial instruments which give the holder the right to acquire equity shares.

30. Calls in advance is not part of the share capital and need to be reflected under '**other current liabilities'**

31. Deferred payment liability would include any liability for which payment is to be made on **deferred credit terms.**

32. Long term borrowings to be classified as **secured and unsecured** and nature of security to be specified.

33. **Current maturities of all long term borrowings** will be disclosed under "other current liabilities".

34. Contractual obligations include dues payables in respect of statutory obligations like **contribution to provident fund**

35. **Unclaimed dividend** is payable on demand and is therefore to be classified as current liability.

36. **Provision for proposed dividend** needs to be disclosed only in the notes as per the revised schedule.

37. **Contingent liability** would include Claims against the company not acknowledged as debts.

38. **Capital advances** should be included under Long-term loans and advances.

39. Term **sundry debtors** have been replaced with "trade receivables".

40. **Trade receivables'** are defined as dues arising only from goods sold or services rendered in the normal course of business.

41. **Bank deposits** with original maturity of more than 12 months needs to be disclosed separately

42. **Earmarked bank balances** example for unpaid dividend to be disclosed separately.

43. **Allowance for bad and doubtful loans** and advances shall be disclosed under the relevant heads separately.

44. **Miscellaneous expenditure** class of asset has been deleted from revised Schedule VI

45. Revised Schedule VI does not mention any disclosure for the unamortized portion of expense items such as **share issue expenses**

46. "**Revenue** includes only the gross inflows of economic benefits received/receivable by the entity.

47. To comply with the disclosure requirements of AS-9 Revenue recognition, **excise duty** has to be disclosed on the face of Statement of Profit and Loss.

48. As per revised schedule VI, dividends should be recognized as income only when the **right to receive dividends** is established as on the Balance Sheet date.

49. Income and net gain on sale of investments should be disclosed separately for **Current as well as Long-term**

50. Finance charges on finance lease to be included under **interest cost.**

51. Interest on shortfall in payment of advance tax should be classified under **finance cost**

52. **<u>Extraordinary items’</u>** are items of income or expenses that arise from events or transactions that are clearly distinct from the ordinary activities of the enterprise and, therefore, are not expected to recur frequently or regularly.

- **Fill in the blanks**

1) A financial year a company may be for a period less or more than ____________ year.

2) Interest accrued on investments is required to be shown under ____________ in the balance sheet of a company.

3) Unutilised Monies from share issues is required to be shown under ____________ in the Balance Sheet of a company.

4) Livestock is required to be shown under ____________ in the Balance sheet of a company.

5) Interest accrued but not due on a Secured Loan is required to be shown under ____________ in the balance sheet of a company.

6) Uncalled amount of partly paid shares is required to be shown under ____________ in the balance sheet of a company.

7) Option on Unissued Shares is required to be shown under ____________ in the balance sheet of a company.

8) Arrears of Fixed cumulative Preference Dividends are required to be shown under ____________ in the balance sheet of a company.

9) According to Schedule VI, in case any addition is made to any asset during the financial year, depreciation should be calculated on a ____________ basis from the date of such addition.

10) Interest from Sinking Fund Investments is required under Schedule VI to be credited to the ____________ .

Answer: (1) a calendar, (2) Current Assets, (3) Investments, (4) Fixed Assets, (5) Current Liabilities, (6) Contingent Liabilities, (7) Share Capital, (8) Contingent Liabilities, (9) (10) pro-data, (11) P&L Account,

- **Match the following columns:**

Column A	Column B
1. Debentures 2. Fixed Deposits 3. Acceptances 4. Proposed Dividends 5. Interest out of capital during construction 6. Due for more / less than 6 months 7. Tax Demand Letter Received 8. Disputed Tax Demand 9. Tax Demand Accepted Exceeds Provision for Tax 10. Provision for Tax More than Tax Demand Accepted 11. Tax Paid Exceeds Accepted Tax Demand	a) Provisions b) Unsecured Loans c) Misc. Expenditure not written off d) Sundry Creditors e) Sundry Debtors f) Secured Loans g) Profit and Loss Account h) Current Liabilities i) Debit P&L Appropriation Account j) Show as Current Assets k) No Entry l) Credit P&L Appropriation Account m) Show as Contingent Liability

Answer: (1) – (f), (2) – (b), (3) – (h), (4) – (a), (5) – (c), (6) – (e), (7) – (k), (8) – (n), (9) – (i), (10) – (m), (11) – (j).

- **State whether True or False.**

1. Schedule XIV specifies the rates of depreciation for various categories of assets on the written down value basis.
2. Calls unpaid are added back to Authorised Share Capital in the Balance Sheet.
3. Any dividend remaining unpaid after 3 year from its due date can be transferred to capital reserve.
4. The brokerage and discount on sales, including the trade discount, related to turnover is to be disclosed separately in the Profit and Loss Account.
5. If the dividend is not claimed within 7 years from the date of its transfer to a special bank account, the amount is distributed to the remaining shareholders.
6. Capital profit realized in cash can be used for paying dividend.

7. Dividend can be paid out of capital, but interest cannot be paid out of capital.

8. One of the few assets that is usually not depreciated is Goodwill.

9. Amount paid on Forfeited Shares is added to Paid-up Capital in the Balance Sheet.

10. Sundry Debtors are to be classified as (i) Small Scale Industries; and (ii) others.

11. Unclaimed dividends are shown under Provisions in the Balance Sheet.

12. Under Secured Loans; Short Term Loans and Other Loans are to be shown separately.

13. Current liabilities are deducted from Current assets so as to show the amount of Net Current Assets in the Horizontal format of balance sheet.

14. The titles – 'Sources of Funds' and 'Application of Funds' appear in the horizontal format of balance sheet.

15. In Fixed Assets schedule, Closing WDV + Depreciation for the year = Opening Gross Block

16. Provision for bad debts is shown under Provisions in the Balance Sheet.

17. If the dividend is not claimed within 7 years from the date of its transfer to a special bank account, the company retains it.

18. Calls in advance are shown under Current Liabilities in the Balance Sheet.

True : 6, 8, 9, 18.

False : 1, 2, 3, 4, 5, 7, 10, 11, 12,13,14, 15, 16, 17.

B. PRACTICAL PROBLEMS

1. **F**rom the following particulars furnished by Pioneer Ltd. prepare the balance sheet as at 31st March, 2015 as required by part I, Schedule VI of the companies Act. Give notes at the foot of the balance sheet as may be found necessary:-

	Debit Rs.	Credit Rs.

Equity capital (Face value of Rs.100)		10, 00,000
Calls in arrear	1,000	
Land	2, 00,000	
Building	3, 50,000	
Plant and Machinery	5, 25,000	
Furniture	50,000	
General reserve		2, 10,000
Loan from State Financial Corporation		1, 50,000
Stock: Finished goods 2, 00,000 Raw Materials 50,000	2, 50,000	
Provision for taxation		68,000
Sundry debtors	2, 00,000	
Advances	42,700	
Proposed dividend		60,000
Profit and loss Account		1, 00,000
Cash balance	30,000	
Cash at bank	2, 47,000	
Preliminary expenses	13,300	
Loans (Unsecured)		1, 21,000
Sundry creditors (For goods and expenses)		2, 00,000
Total	**19, 09,000**	**19, 09,000**

The following additional information is also provided:

1. Miscellaneous expenses included Rs. 5,000 audit fees and Rs.700 for out-of-pocket expenses paid to the auditors.
2. 2,000 equity shares were issued for consideration other than cash.
3. Debtors of Rs. 52,000 are due for more than six months.
4. The cost of assets:

Building	4, 00,000
Plant & Machinery	7, 00,000
Furniture	62,500

5. The balance of Rs. 1, 50,000 on the loan account with State Finance Corporation is inclusive of Rs. 7,500 for interest accrued but not due. The loan is secured by hypothecation of the plant and machinery.
6. Balance at bank includes Rs. 2,000 with Perfect Bank Ltd. which is not a scheduled bank.
7. Bills receivable for Rs. 2,75,000 maturing on 30th June, 2015, have been discounted.

8. The company had contract for the erection of machinery at Rs. 1, 50,000 which is still incomplete.

Notes: (i) Estimated amount of contract remaining to be executed on capital account and not provided for Rs. 1,50,000. The company had given this contract for purchase of machinery.
(ii) Bills receivable discounted maturing on 31st June, 2015 amount to Rs. 2, 75,000.

(Answer: Balance Total Rs.19, 08,000)

2. The Auto Paris Manufacturing Co. Ltd. was registered with an authorized capital of Rs. 10, 00,000 divided into shares of Rs. 10 each, of which 40,000 shares had been issued and fully paid.

The following is the Trial Balance extracted on 31st March 2015.

	Debit Rs.	Credit Rs.
Stock (1st April 2008)	1, 86,420	
Purchases and sales	7, 18,210	11, 69,900
Returns	12,680	9,850
Manufacturing wages	1, 09,740	--
Sundry Manufacturing expenses	19,240	--
Carriage inwards	4,910	--
18% Bank loan (Secured)	--	50,000
Interest on bank loan	4,500	--
Office salaries and expenses	17,870	--
Auditors' fees	8,600	--
Director's remuneration	26,250	--
Preliminary expenses	6,000	--
Freehold premises	1, 64,210	--
Plant and machinery	1, 28,400	--
Furniture	5,000	--
Loose Tools	12,500	--
Debtors and Creditors	1, 05,400	62,220
Cash in hand	19,530	--
Cash at bank	96,860	--
Advance payment of tax	84,290	
P & L A/c on 1st April 2008	--	38,640
Share Capital	--	4, 00,000
	17, 30,610	**17, 30,610**

You are required to prepare Trading and profit & Loss Account for the year ended 31st March, 2015 and a balance sheet as at that date after taking into consideration the following adjustments.

i. On 31st March, 2015 outstanding Manufacturing Wages and outstanding Office salaries stood at Rs. 1,890 and Rs. 1,200 respectively. On the same date stock was valued at

Rs. 1, 24,840 and loose tools at Rs. 10,000.

ii. Provide for interest on Bank Loan for 6 months.

iii. Depreciation on plant and machinery is to be provided @ 15%p.a. while on office furniture it is to be @ 10%p.a.

iv. Write off one-third of balance of preliminary expenses.

v. Make a provision for income tax @ 50%.

vi. The directors recommended a maiden (first) dividend @ 15% for the year ending 31st March 2015 after a transfer of 5% of net profits to General Reserve.

❖❖❖❖

7

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

Unit Structure

OBJECTIVES

After studying the unit the students will be able to:

- Understand the Meaning of IFRS.
- Know the objectives of IFRS
- Explain the Scope of IFRS
-

INTRODUCTION

Accounting is the art and science of recording business transactions in best possible manner with proper selection and adoption of accounting policies and principles. Over the time it was felt necessary to ensure easy comparability the enterprises should follow uniform accounting methods. In India the Institute of Chartered Accountants of India governs the profession of accountancy. The institute ensures professionalism and prudence in preparation and presentation of financial statements by issuing guidelines, accounting standardsfrom time to time. In today's world of globalization business enterprises have become more dependent on each other, across the nation and across the world. The globalization has forced more and more countries to open their doors for business expansion across borders and to foreign investments.Traditionally companies raised funds from domestic capital markets and financial institutions. The business was restricted to very few countries. The rapid expansion of international trade and internationalization of firms, the development of new communication technologies, and the 514emergence of international competitive forces has made it extremely necessary to have uniform and internationally acceptable accounting standards. Now it has been realized that under this global business scenario the business community is badly in need of a common accounting language that should be spoken by all of them across the world. A financial reporting systemsupported by a strong governance, high quality standardsand firm regulatory framework is the key to economic development. Indeed, sound financial reporting standards underline the trust that investors place in financial reporting information and thusplay an important role in contributing to the economic development of a country. Different countries have local accounting standards which spell out the accounting treatment and disclose your requirements for preparing of financial statements, some sort of compatibility or convergence is necessary to enable all the stake holders to take appropriate economic decisions. This is sought to be ensured through the International Financial Reporting Systems (IFRS) adopted by International Accounting Standards Board (IASB). Most of the countries have started adopting IFRS or making their local GAAP convergent with IFRS. Major stock exchanges across the world today accept IFRS.

MEANING OF IFRS:

IFRSs are principle-based standards.

- The principle-based standards have distinct advantage that the transactions cannot be manipulated easily to achieve a particular accounting.
- The Financial Accounting Standards Board (FASB), USA, is having a convergence project with the IASB and is broadly adopting the principle-based approach instead of rule-based approach.
- IFRSs lay down treatments based on the economic substance of various events and transactions rather than their legal form.
- The application of this approach may result into events and transactions being presented in a manner different from their legal form.
- To illustrate, as per IAS 32, preference shares that provide for mandatory redemption by the issuer are presented as a liability.

OBJECTIVES OF IFRS:

WHY IFRS?

A single set of accounting standards would enable internationally to standardize training and assure better quality on a global screen, it would also permit international capital to flow more freely, enabling companies to develop consistent global practices on accounting problems. It would be beneficial to regulators too, as a complexity associated with needing to understand various reporting regimes would be reduced.

OBJECTIVES OF IFRS:

1. The main objective of IFRS is to develop in the public the interest of a single set of high quality, understandable and enforceable global accounting standards that require high quality, transparent and comparable information in financial statements and other financial reporting to help participants in the world's capital markets and other users make economic decisions.
2. To promote the use and rigorous application of those standards; in fulfilling the objectives associated with it.
3. To take account of, as appropriate, the special needs of small and medium-sized entities and emerging economies.
4. To bring about convergence of national accounting standards and International Accounting standards and IFRS to high quality solutions.

SCOPE OF IFRS

All International Accounting Standards (IASs) and Interpretations issued by the former IASC (International Accounting Standard Committee) and SIC (Standard Interpretation Committee) continue to be applicable unless and until they are amended or withdrawn. IFRSs apply to the general purpose financial statements and other financial reporting by profit-oriented entities -- those engaged in commercial, industrial, financial, and similar activities, regardless of their legal form. Entities other than profit-oriented business entities may alsofind IFRSs appropriate. General purpose financial statements are intended to meet the common needs of shareholders, creditors, employees, and the public at large for information aboutan entity's financial

position, performance, and cash flows. Otherfinancial reporting includes information provided outside financialstatements that assists in the interpretation of a complete set offinancial statements or improves users' ability to make efficient economic decisions. IFRS apply to individual company and consolidated financial statements. A complete set of financial statements includes a balance sheet, an income statement, a cash flow statement, a statement showing either all changes in equity or changes in equity other than those arising from investments by and distributions to owners, a summary of accounting policies, and explanatory notes.
If an IFRS allows both a 'benchmark' and an 'allowed alternative' treatment, financial statements may be described as conforming to IFRS whichever treatment is followed. In developing Standards, IASB intends not to permit choices in accounting treatment. Further, IASB intends toreconsider the choices in existing IASs with a view to reducing the number of those choices. IFRS will present fundamental principles in bold face type and other guidance in non-bold type (the 'black-letter'/'grey-letter' distinction). Paragraphs of both types have equalauthority. The provision of IAS 1 that conformity with IAS requires compliance with every applicable IAS and Interpretation requires compliance with all IFRSs as well.

CONVERGENCE WITH IFRSS: INDIAN PERSPECTIVE

- Indian Accounting Standards (ASs) are formulated on the basis of the IFRSs.
- While formulating ASs, the endeavor of the ICAI remains to converge with the IFRSs.
- The ICAI has till date issued 29 ASs corresponding to IFRSs.
- Some recent ASs, issued by the ICAI, are totally at par with the corresponding IFRSs, e.g., the Standards on ‘Impairment of Assets’ and ‘Construction Contracts’.
- While formulating Indian Accounting Standards, changes from the corresponding IAS/ IFRS are made only in those cases where these are unavoidable considering:
- Legal and/ or regulatory framework prevailing in the country.

- To reduce or eliminate the alternatives so as to ensure comparability.
- State of economic environment in the country
- Level of preparedness of various interest groups involved in implementing the accounting standards.

BENEFITS OF IFRS

The forces of globalization prompt more and more countries to open their doors to foreign investment and as businesses expand across borders the need arises to recognize the benefits of having commonly accepted and understood financial reporting standards. Following are some of the benefits of adopting IFRS -

- Transparency and comparability
- Low cost of capital
- Eliminates need for multiple reporting
- True value of acquisition
- Cross border transaction
- Sets a benchmark
- Improvement in planning and forecasting

IFRS -1: FIRST TIME ADOPTION OF IFRS

1. An entity shall prepare and present an opening IFRS statement of financial position at the date of transition to IFRSs. This is the starting point for its accounting under IFRSs.
2. An entity shall prepare an opening IFRS balance sheet at the date of transition to IFRSs. This is the starting point for its accounting under IFRSs.
3. An entity need not present its opening IFRS balance sheet in its first IFRS financial statements. In general, the IFRS requires an entity to comply with each IFRS effective at the end of its first IFRS reporting period. In particular, the IFRS requires an entity to do the following in the opening IFRSstatement of financial position that it prepares as a starting point for its accounting under IFRSs:

- Recognize all assets and liabilities whose recognition is required by IFRSs.
- Not to recognize items as assets or liabilities if IFRSs do not permit such recognition; IFRS-1.
- IFRS-1 reclassify items that it recognized under previous GAAP as one type of asset, liability or component of equity, butare different type of asset, liability or component of equityunder IFRSs. Apply IFRSs in measuring all recognized assets and liabilities.

The IFRS grants limited exemptions from these requirements in specified areas where the cost of complying with them would be likely to exceed the benefits to users of financialstatements. The IFRS also prohibits retrospective application of IFRSs in some areas; particularly where retrospective application would require judgments by management about past conditions after the outcome of a particular transaction is already known. The IFRS requires disclosures that explain how the transition from previous GAAP to IFRSs affected the entities reported financial position, financial performance and cash flows.

EXERCISE

1. Explain the meaning and scope of IFRS.
2. What are the objectives of IFRS?

8

FINAL ACCOUNTS OF CO-OPERATIVE HOUSING SOCIETIES

Unit Structure:

1.1 INTRODUCTION

A co-operative society is a voluntary and autonomous organization formed for the purpose of promoting and protecting interests of its members. The main objective of the Co-operative society is to provide service to its members. It may or may not earn profit. The profits earned are partly distributed among members and partly kept as reserves.

A co-operative society can be defined as a voluntary association of persons making equitable contribution to the required capital and expecting a share and risks and benefits of the organization. Normally a co-operative society is a service oriented organization and is not interested in making profit.

A co-operative society is most important form of organization in Indian economic scene. The Co-operative Societies Act, 1912 governs formation and working of co-operative Societies. Also most of the states have enacted their own Co-operative Societies Acts, the basic framework remaining the same as central Act. In the state of Maharashtra, co-operative societies are governed by the "The Maharashtra co-operative Societies Act 1960" and the "The Maharashtra co-operative Societies Rules 1961"

1.2 FEATURES OF CO-OPERATIVE SOCIETY

a. Voluntary membership
b. Equal Rights
c. Corporate body
d. Perpetual succession
e. Democratic management: one member one vote
f. Co-operation
g. Mutual trust
h. Common welfare
i. Economy
j. Self management
k. Distribution of profit

1.3 TYPES OF CO-OPERATIVE SOCIETIES

There are various types of co-operative societies like

a. Agricultural co-operative society
b. Credit co-operative society
c. Consumer co-operative society
d. Co-operative sugar factories
e. Co-operative Banks
f. Manufacturing co-operative society
g. Marketing co-operative society

1.4 SUITABILITY OF CO-OPERATIVE FOR HOUSING

A housing society or apartment associations is a situation popular in India with a group of house owners within a residential complex, usually one consisting of buildings that each have flats. A housing society's apartments or premises are formed as per relevant laws for smooth functioning of utilities and other amenities provided to them. The housing society formed must be formally registered with registrar of co-operatives. Each building in same premise may have separate housing society or one. Many housing societies form one federation. Housing societies run on the service charges levied by them on house or flat owners for various services provided by the society. Some of the housing societies have other sources of income also like advertisement hoardings, Mobile cell phone antennas, shops or commercial organizations etc. The society provides basic amenities like security, lighting cleaning as well as luxuries like health club swimming pool, community hall etc.

The principal of co-operation and democratic control ensures that co-operative form is best for such services to the members.

The Managing Committee takes care of the affairs of the Housing Society like appointment of service providers, maintenance of Society premises, solving member's grievances, maintenance of books of accounts and taking care of safety and security.

1.5 TYPES OF CO-OPERATIVE HOUSING SOCIETIES

Housing Society means a society, the object of which is to provide its members with open plots for housing, dwelling or flats; or if open plots, the dwelling houses or flats are already acquired, to provide its members common amenities and service." Based on the above definition rule 10 classifies housing societies into:

TENANT OWNERSHIP HOUSING SOCIETIES These are housing societies where land is held either on leasehold or freehold basis by societies and houses are owned or are to be owned by members. In such societies, the societies are the owners or lessees of land, plots are carved out and given on a long term lease to construct their dwelling houses thereon as per the terms of the lease deed. The society is thus an owner of the land only either on leasehold or freehold basis and the ownership of building vests in the individual members.

TENANT CO-PARTNERSHIP HOUSING SOCIETIES These are societies which hold land on ownership or on lease and construct flats thereon which are allotted to members who occupy them. The societies, thus, hold both the land and buildings and its members are allot tees therein having the right of occupancy which right is transferable by transfer of shares to other members in accordance with the provisions of the Act. The right of occupancy of the flat is transferable and inheritable under MCS Act and by the byelaws of the society.

OTHER HOUSING SOCIETIES These are house mortgage societies and house construction societies. House mortgage has the object of advancing loans to the members and to the societies on the security of land and houses. House construction deals in purchase and sale of constructed houses or dwellings to members or other societies

1.6 IMPORTANT DEFINITIONS UNDER MAHARASHTRA CO-OPERATIVE SOCIETIES ACT

a. Co-operative Society: under section 2 (27) of the Act society means a co-operative society registered or deemed to be registered under this Act. Co-operative society is corporate body distinct from its members. Section 167of the Act states that provisions and companies Act are not applicable to co-operatives.

b. Working Capital: under section 2 (31) of the Act working capital means funds at the disposal of the society inclusive of paid up share capital, funds built up out of profits and money raised by borrowing and other means.

c. Auditor: Rule No. 69 of co-operative Societies Rules states that the audit of co-operative society shall be conducted by departmental auditor or certified auditors.

   The term certified auditors includes following:

   - Chartered Accountant
   - A person who holds government diploma in Co-operative department of Accounts & Audits
   - A person who has served as an auditor in the Co-operative department of the state government

d. Bye-laws: under section 2(5) Bye-laws means bye laws registered under this Act and for the time being in force and includes registered amendments of such Bye-laws. Bye-laws of a co-operative society may be compared to articles of association of a Ltd company. The provisions of bye-laws cannot be contrary to the provisions of co-operative societies Act. These are rules for internal and day to day management and smooth running of the society. Generally these include clauses for:

   1. Name
   2. Address
   3. Area of operation
   4. Objects of the society
   5. The manner in which and the limits up to which the funds of the society should be raised and utilized.
   6. Rules regarding share capital
   7. Terms and qualifications for admission of membership.

8. Rights duties and liabilities of members
9. Rules regarding non occupancy or renting out of flat
10. Transfer fees
11. Disposal of net profit

e. Member: under section 2(19), a member of a co-operative society means a person joining in an application for the registration of a co-operative society which is subsequently registered or a person duly admitted to the membership of existing society and includes associate member or nominal member.

1.7 MANAGEMENT AND ADMINISTRATION

General Body:

Every co-operative society forms a general body from its members. It is the final authority of the society. It exercises various powers like:

a. Expulsion of a member by $3/4^{th}$ majority.

b. Amendment of Bye-laws of the society by $2/3^{rd}$ majority, subject to approval from Registrar.

c. Adoption of accounts, appropriation of profits as per Act and Bye –laws

Managing Committee:

The day today affairs of the society are managed by the managing committee, which consists of at least 4 members. The committee performs various functions such as:

a. Proper custody and maintenance of movable and immovable property belonging to the society.

b. Proper maintenance of books of accounts relating to financial transactions of the society.

c. To call and conduct all the meetings and to record the minutes of all such meetings.

d. To maintain all the registers as required by the act and rules and bye –laws.

Secretary:

The managing committee elects one of them to act as secretary of the society. He is responsible for filing of various returns with the registrar.

Chairman:

The managing committee elects one of them to act as chairman of the society.

7.8 ACCOUNTING AND FINANCE

Accounting year:

The Act has fixed 30th day of June of every year as the day of balancing of accounts of the society, however any other day can be fixed by the society with prior approval of the Registrar. Normally most of the societies opt for 31st day of March as yearend date so as to confirm with government year end.

Books of Accounts and Records:

Books of accounts should be so maintained as to give the necessary financial statistical and other information as regards money received and expended, sales and purchases, assets and liabilities, dues from various members etc.

Normally following books of accounts are maintained by the society.

1. Cash book
2. General Ledger
3. Members Register
4. Stock Register
5. Property Register
6. Register of audit objections and their clarification etc.

Financial Statements: according to Maharashtra co-operative societies Rules the society will have to prepare within 45 days of close of accounting year financial statements disclosing the following:

1. Receipts and Payments Account for the year
2. Income and Expenditure Account for the year in the prescribed N Form
3. Balance Sheet as on that date in the prescribed N Form

Some important aspects of accounts:

1. **Ascertainment and appropriation of profit:** Surplus/Deficit of a co-operative is calculated on the basis of income and Expenditure for the year. The members contribute money to the society on regular basis (monthly/quarterly/or otherwise) for

various expenses the society incurs. The contribution may be lump sum or itemized. Contributions from members can be for following:

i) Property Taxes
ii) Water charges
iii) Electricity charges
iv) Repairs and maintenance fund
v) Service charges
vi) Lift maintenance charges
vii) Contribution to sinking fund
viii) Parking charges
ix) Interest and penalty for delayed payments
x) Non occupancy charges
xi) Lease rent
xii) Swimming pool and other amenities charges

2. The society has to pay lot many other expenses in addition to charges received for various expenses as mentioned above. These are:

i) Printing & Stationery, postage
ii) Office Expenses, sundry Expenses
iii) Account writing charges, Audit fees, legal expanses
iv) Cleaning expenses
v) Security charges
vi) Subscription to Education fund
vii) Affiliation fees to Housing federation
viii) Office bearers remuneration
ix) Meeting expenses

3. The society may have other incomes apart from contribution from members. These are as follows

i) Interest received on investments
ii) Interest received on F.D. with banks
iii) Rent received from commercial premises let out
iv) Rent received from Advertising Hoardings
v) Rent received from antennas of mobile companies

vi) Transfer fees received

vii) Admission fees

4. Every society shall transfer 25% of its net profit to statutory reserve every year.

5. A society can maintain cash balance for petty expenses not exceeding Rs. 5000.

6. Profit and Loss Appropriation Account; all appropriations of profit must be approved at the General body meeting and therefore if in the examination appropriations are given Profit and loss appropriation account should be prepared on memorandum basis but transfer of 25% of profit to reserve fund should be made.

1.9 STATUTORY FORMATS OF FINAL ACCOUNTS

Format for Income and Expenditure Account and Balance Sheet: the Act does not specify any Format of Income & Expenditure Account but the Balance Sheet must be Prepared in the “N” form

PERFORMA OF INCOME AND EXPENDITURE ACCOUNT

EXPENDITURE	Rs.	INCOME	Rs.
To Property taxes	X	By Contributions received from members for	X
To Water Charges	X	-property Tax	X
To Security expenses	X	-lift maintenance	X
To Repairs and maintenance	X	-electricity	X
To Cleaning charges	X	-security	X
To Electricity Charges	X	-parking’s	X
To Office Expenses	X	-lift maintenance	X
To Printing & Stationery	X	-garden/gym/swimming pool. maintenance	X
To Meeting Expenses	X	-misc.	X
To Meeting fees	X	By Interest received	X
To Account writing charges	X	By Rent received	X
To Audit Fees	X	By Transfer fees received	X
To Insurance	X	By Miscellaneous Income	X
To subscription to	X	By Deficit	X

Education fund			
To Affiliation fees	X		
To Postage	X		
To Service tax	X		
To Income tax provision	X		
To Depreciation	X		
To Sinking fund	X		
To Reserve fund	X		
To Surplus	X		
	XX		xx

PROFORMA OF BALANCE SHEET (N FORM)

	LIABILITIES	RS.		ASSETS	RS.
I	**SHARE CAPITAL**		I	**CASH AND BANK BALANCES**	
	Authorised			Cash on hand	
	Issued & paid up			Cash at bank	
	Less : Calls in arrears			Current A/c	
				Saving A/c	
II	**RESERVE AND OTHER FUNDS**			Call A/c	
	Reserve Fund				
	Sinking Fund		II	**INVESTMENTS**	
	Development Fund			Government Securities	
	Building Fund			Other securities	
	Depreciation Fund			Shares of other co-operative societies	
	Dividend Equalization Fund			Shares, Debentures of companies	
				F.D. With banks	
III	**STAFF PROVIDENT FUND**		III	**INVESTMENTS OF STAFF P.F.**	
				Advances against PF	
IV	**SECURED LOANS**		IV	**LOANS AND ADVANSES**	
	Cash Credit			Loans	
	Bank overdraft			Cash Credits	
	Loans			Dues from members	

	Loan from MCHFS			Dues from employees	
	Other secured loans			Dues from office bearers	
V	**UNSECURED LOANS**		V	**SUNDRY DEBTORS**	
	From Bank			Advances	
	From Government			Others	
	Others				
VI	**DEPOSITS**		VI	**CURRENT ASSETS**	
	Fixed Deposits			Stores and Spare Parts	
	Recurring Deposits			Loose Tools	
	Current Deposits			Stock in trade	
	Call Deposits			Work in Progress	
VII	**CURRENT LIABILITIES AND PROVISIONS**		VII	**FIXED ASSETS**	
	Outstanding Expenses			Land & Buildings	
	Advances			Gym Equipments	
				Furniture	
				Live Stock	
				Motor vehicles	
VIII	**INTEREST DUE BUT NOT PAID**		VIII	**MISC EXPENSES AND LOSSES**	
IX	**OTHER LIABILITIES**			Goodwill	
				Preliminary Expenses	
X	**PROFIT AND LOSS ACCOUNTS**			Deferred Revenue Expenses	
	Profit for last Year		IX	**OTHER ITEMS**	
	Less: appropriations of last year			Prepaid Expenses	
	Add : surplus for the current year			Interest accrued but not due	
			X	**PROFIT & LOSS ACCOUNT**	
	TOTAL			**TOTAL**	

1.10 SOLVED POBLEMS

Illustrations 1

Priya Darshan Co.Op Hsg. Society

Trial Balance as on 31st March, 2015

	RS.		Rs.
Bank Balance with MSC bank	85,241	Contribution from Members	
Cash at Hand	759	Property Tax	18,000
Furniture	14,500	Water Charges	85,000
Water Pump	15,500	Life Maintenance	40,000
Accounting Charges	16,000	Service Charges	135,000
Audit Fees	3,500	Insurance	11,000
Bank Charges	400	Sinking Fund	12,500
Investment of Sinking fund	27,900	Repairs Fund	15,000
Investment of Reserve Fund	20,000	Misc Income	27,500
Investment of Repairs Fund	70,800	Interest from members	125,700
Deposit with Reliance	9,500	Share Capital	75,000
Dues from members	12,500	Sinking Fund	39,500
Electricity Charges	12,200	Reserve Fund	10,200
Rent, Rates & Tax	15,550	Repairs Fund	99,000
Water Charges	79,000	Income & Expenditure A/c.	100,000
Salary	25,500	Building Fund	4000,000
Printing & Stationery	11,000		
Conveyance	550		
Building	4000000		
Postage	2,000		
Sundry Expenses	900		
Security Charges	20,900		
Lift Maintenance	25,200		
Fire Insurance	24,000		
F.D. with Union Bank	300,000		
	4,793,400		4793,400

Adjustments

1) Provide for depreciation: Furniture 10%, Water Pump 20%
2) Interest accrued on: Sinking fund Investment Rs.1,300, Repairs fund Investment Rs.1,000, Reserve fund Investments Rs.500
3) Expenses Payable: Salary Rs. 2,800, Printing bill Rs.500
4) Insurance paid in advance Rs. 2,500
5) Education fund payable Rs.150

Prepare Income & Expenditure A/c. for the year ended 31st March 2015 and Balance sheet as on that date.

SOLUTION:

Priya Darshan Co. Op Hsg. Society ltd.

INCOME AND EXPENDITURE ACCOUNT for the Year Ended 31st March 2015

EXPENDITURE	Rs.	INCOME	Rs.
To Electricity Charges	12,200	By Contribution from Members	
To Rent, Rates & Tax	15,550	Property Tax	18,000
To Water Charges	79,000	Water Charges	85,000
To Salary 25500		Life Maintenance	40,000
Add: O/s 2800	28300	Service Charges	135,000
To Printing & Stationery 11000		Insurance	11,000
Add: O/s 500	11500	By Misc. Income	27,500
To Conveyance	550	Interest from members	125700
To Postage	2,000		
To Sundry Expenses	900		
To Security Charges	20,900		
To Lift Maintenance	25,200		
To Fire Insurance 24000			
Less prepaid 2500	21500		
To Accounting Charges	16,000		
To Audit Fees	3,500		

To Bank Charges	400		
To Education fund payable	150		
To Depreciation			
Furniture 1450			
Water Pump 3100	4550		
To Reserve Fund	50000		
To Surplus	150000		
	442,200		442200

BALANCE SHEET as on 31st March 2015

LIABILITIES	RS.	ASSETS	RS.
SHARE CAPITAL		**CASH AND BANK BALANCES**	
Authorised		Cash on hand	759
Issued & paid up	75000	Cash at MSC bank	85241
RESERVE AND OTHER FUNDS		**INVESTMENTS**	
Reserve Fund 10200		Reserve fund Invest 20000	
Add: current year Transfer 50000		Add : accrued Int. 500	20500
Add : accrued Int. 500	60700	Sinking fund Invest 27900	
Sinking Fund 39500		Add : accrued Int. 1300	29200
Add: Contribution 12500		Repairs Fund Invest 70800	
Add : accrued Int. 1300	53300	Add : accrued Int. 1000	71800
Repairs Fund 99000		F.D. With Union Bank	300000
Add: Contribution 15000			
Add : accrued Int. 1000	115000	**LOANS AND ADVANCES**	
Building Fund	4000000	Dues from members	12500
CURRENT LIABILITIES AND		**FIXED ASSETS**	

PROVISIONS			
Outstanding Expenses		Buildings	4000000
Salaries 2800		Furniture 14500	
Printing 500	3300	Less: Depreciation 1450	13050
Education fund payable	150	Water Pump 15500	
		Less: Depreciation 3100	12400
PROFIT AND LOSS ACCOUNTS			
Profit for last Year 100000		**OTHER ITEMS**	
Add : surplus 150000	250000	Prepaid Insurance	2500
		Deposit with Reliance	9500
	4557450		4557450

2. From the following Trial Balance of Rutuja Co-operative Housing Society ltd, Parel., prepare Income and Expenditure Account for the year ended 31st March 2015 and the Balance Sheet as on that date:

Particulars	Debit Rs.	Credit Rs.
Share Capital		285000
Water pump	175000	
Furniture	250000	
Buiding	3450000	
Sinking fund		43500
Property Tax	52800	
Members contribution		494600
Security charges	85800	
Lift maintenance	34600	
Building fund		3550000
Reserve fund		112800
Meeting fees paid	24600	
Annual general body meeting expenses	12500	
Audit Fees	8500	
Salaries	32100	
Honorarium to secretary	5000	

Insurance	16300	
Legal and professional charges	24500	
General expenses	28300	
Fixed deposit with bank	500000	
Cash at bank	40000	
Interest on fixed deposit		45000
Transfer fees received		5000
Parking charges received		60000
Income and Expenditure (Cr balance)		152000
Cash in hand	2900	
Subscription to housing Federation	5000	
	4747900	4747900

Adjustments:

1) Depreciate water pump at 20% p. a., Furniture at 20 % p.a. and Building at 5 %.
2) Salaries outstanding Rs.5,100.
3) One member has not paid parking charges of Rs. 1000
4) Transfer Rs. 2000 to Sinking Fund

Solution

Rutuja Co-operative Housing Society ltd, Parel.
Income and Expenditure Account
for the year ended 31st March 2015

Expenditure	**Rs.**	**Income**	**Rs.**
To Property tax	52800	By Members contribution	494600
To Security charges	85800	By Interest on fixed deposit	45000
To Lift maintenance	34600	By Transfer fees received	5000
To Meeting fees paid	24600	By Parking charges received 60000	
To Annual general body meeting expenses	12500	Add : Receivable 1000	61000
To Audit Fees	8500		605600
To Salaries 32100			
Add : Outstanding 5100	37200		

To Honorarium to secretary	5000		
To Insurance	16300		
To Legal and professional charges	24500		
To General expenses	28300		
To Subscription to housing Federation	5000		
To Depreciation			
Building 172500			
Water pump 35000			
Furniture 50000	257500		
To Sinking fund	5000		
To Reserve Fund (25 %)	2000		
To surplus c/f	6000		
	6,05,600		6,05,600

BALANCE SHEET as on 31st March 2015

	LIABILITIES	RS.		ASSETS	RS.
I	**SHARE CAPITAL**		**I**	**CASH AND BANK BALANCES**	
	Authorised			Cash on hand	2900
	Issued & paid up	285000		Cash at bank	40000
II	**RESERVE AND OTHER FUNDS**		**II**	**INVESTMENTS**	
	Sinking Fund 43500			F.D. With banks	500000
	Add: Transfer 5000	48500			
	Building Fund	3550000	**III**	**INVESTMENTS OF STAFF P.F.**	
	Reserve Fund 112800				
	Add: Transfer 2000	114800	**IV**	**LOANS AND ADVANSES**	

III	**STAFF PROVIDENT FUND**		**V**	**SUNDRY DEBTORS**	
				Parking charges receivable	1000
IV	**SECURED LOANS**				
			VI	**CURRENT ASSETS**	
V	**UNSECURED LOANS**				
			VII	**FIXED ASSETS**	
VI	**DEPOSITS**			Buildings 3450000	
				Less: dep @ 5% 172500	3277500
VII	**CURRENT LIABILITIES AND PROVISIONS**			Furniture 250000	
	O/s Expenses salaries	5100		Less: Dep @ 20% 50000	200000
				Water Pump 175000	
VIII	**INTEREST DUE BUT NOT PAID**			Less: Dep @ 20% 35000	140000
IX	**OTHER LIABILITIES**		**VIII**	**MISC EXPENSES AND LOSSES**	
X	**PROFIT AND LOSS ACCOUNTS** Income & Expe b/f 152000 Add : surplus 6000	158000			
	TOTAL	4161400		**TOTAL**	4161400

3. Yashodhan co-operative housing society ltd. has prepared following Trial Balance as on 31st March 2015

PARTICULARS	Dr. Rs.	Cr Rs.
Share Capital		7500
Land	300000	
Building	6500000	
Sinking fund		250000
Repairs Fund		500000
Sinking fund Investments	250000	
Repairs Fund investments	500000	
Contribution from members towards Land & Building		6800000
Contributions received from members		270000
Reserve fund		125000
Salaries	48000	
Municipal Taxes	45500	
Water Charges	12600	
Printing and Stationery	6800	
Audit fees	5000	
Bank interest		25000
Cash on hand	3800	
Cash at bank	68700	
Office expenses	12700	
Honorarium to secretary	6000	
Security charges	26000	
Electricity Expenses	7500	
Furniture and Fixtures	50000	
Parking charges received		60000
Repairs and Maintenance	12900	
Income & Expenditure account		68000
Fixed Deposit with Indian Bank	250000	
Total Rs.	8105500	8105500

Additional information:

1. The society has 30 members. Every member has purchased 5 shares of Rs. 50 each.
2. Every member pays Rs. 800/- as monthly contribution. One member has paid 3months contribution in advance.

3. The society transfers every year 0.25% of cost of building to sinking fund and 0.75%of cost of building to repairs fund. On the same day equal amount is transferred from bank account to respective fund investment account.

Prepare Income & Expenditure A/c. for the year ended 31st March 2015 and Balance sheet as on that date.

Solution :

Yashodhan Co-operative Housing Society Ltd
INCOME AND EXPENDITURE ACCOUNT
for the year ended 31st March 2015

EXPENDITURE	Rs.	INCOME	Rs.
To Salaries	48000	By Contributions 270000	
To Municipal Taxes	45500	Add: outstanding 20400	
To Water Charges	12600	Less; advance 2400	288000
To Printing and Stationery	6800	By Interest received	25000
To Audit fees	5000	By Parking Charges received	60000
To Office expenses	12700		
To Honorarium to secretary	6000		
To Security charges	26000		
To Electricity Expenses	7500		
To Repairs and Maintenance	12900		
To transfer to repairs fund	48750		
To Transfer to Sinking fund	16250		
To Transfer to reserve fund	31250		
To Surplus	93750		
	373000		373000

BALANCE SHEET as on 31st March 2015

	LIABILITIES	RS.		ASSETS	RS.
I	**SHARE CAPITAL**		I	**CASH AND BANK BALANCES**	
	Authorised			Cash on hand	3800
	Issued & paid up	7500		Cash at bank 68700 - trf to rep. fund inv 48750	
II	**RESERVE AND OTHER FUNDS**			-trf to sink fund inv 16250	3700
	Repairs Fund 500000				
	Add; current year trf 48750	548750	II	**INVESTMENTS**	
	Sinking Fund 250000			Repairs Fund Inv 500000	
	Add; current year trf 16250	266250		Add; current year trf 48750	548750
	Reserve Fund 125000			Sinking Fund Inv 250000	
	Add; current year trf 31250	156250		Add; current year trf 6250	266250
	Building fund	6800000		F.D. With banks	250000
III	**CURRENT LIABILITIES AND PROVISIONS**		III	**LOANS AND ADVANSES**	
	Advance contribution	2400		Dues from members	20400
IV	**PROFIT AND LOSS ACCOUNTS**		IV	**FIXED ASSETS**	
	Profit for last Year 68000			Land	300000
	Add : surplus 93750	161750		Buildings	6500000
				Furniture	50000
	TOTAL	7942900		**TOTAL**	7942900

4. Trial balance of Hill View Co-operative Housing society Ltd. As on 31st March 2015 was as follows

PARTICULARS	Dr. Rs.	Cr Rs.
Share Capital		15000
Reserve Fund		117000
Shares of Maharashtra Co-op Housing Finance Society	75000	
Loan from Maharashtra Co-op Housing Finance Society		425000
Members Contribution for		
Land		1500000
Construction of building		4000000
Shares of Maharashtra Co-op Housing Finance Society		75000
Monthly contribution for expenses		236000
Parking Charges		11400
Repayment of loan from Maha. Co-op ho.fin. so.	50000	
Cash on Hand	1900	
Current A/c with Saraswat Co-op Bank	15700	
F.D. with Saraswat co-op bank	500000	
Saving a/c with Indian Bank	12400	
Land	1500000	
Building	4000000	
Housing Finance loan to members	425000	
Salaries	44700	
Printing & Stationery	12700	
Security charges	24000	
Municipal taxes	57300	
Water charges	5600	
Lease rent	2400	
Legal & professional charges	12000	
Repairs	16300	
Rent received from Mobile Antenna		120000
Collection of installments of loan to members		50000
Income & Expenditure Account		205600
	6755000	6755000

Additional Expenses

1. There are 50 members in the society each has taken 20 Shares of Rs. 15 each. Each member pays Rs. 400 as monthly charges. There are 10members who are paying Rs. 100 p.m. as parking charges. Two of them have not paid parking charges for last quarter and five of them have not paid monthly charges for two months.
2. Out of current year installments of Rs. 50000 paid to Maharashtra Co-op Housing Finance Society Rs.35000 is towards interest and balance is towards repayment of loan.
3. Audit Fees Rs. 5000 is for the current year is outstanding.
4. Secretary is to be paid honorarium of Rs. 2000.

From the above trial Balance and additional information you are required to prepare Income and Expenditure account for the year ended 31st March 2015 and balance sheet as on that date in prescribed format.

SOLUTION:

Hill View Co-operative Housing society Ltd
Income and Expenditure Account
for the year ended 31st March 2015

Expenditure	Rs.	Income	Rs.
To Salaries	44700	By Contri. from members 236000	
To Printing & Stationery	12700	Add: o/s 4000	240000
To Security charges	24000	By Parking Charges 11400	
To Municipal taxes	57300	Add: O/s 600	12000
To Water charges	5600	By Rent recd from Mobile Antenna	120000
To Lease rent	2400		
To Legal & professional charges	12000		
To Repairs	16300		
To O/s audit Fees	5000		
To secretary's remuneration payable	2000		
To Reserve Fund	47500		
To Surplus	142500		
	382000		372000

BALANCE SHEET as on 31st March 2015

LIABILITIES	RS.	ASSETS	RS.
SHARE CAPITAL		**CASH AND BANK BALANCES**	
Authorised		Cash on hand	1900
Issued & paid up	15000	Cash at bank current A/c Saraswat	15700
(1000 shares of Rs. 15 each)		Saving a/c with Indian Bank	12400
RESERVE AND OTHER FUNDS		**INVESTMENTS**	
Reserve Fund 117000		Shares in maha.co. Hsg Fin	75000
Add: C/y Trf 47500	164500	F.D. with Saraswat co-op bank	500000
Members contribution for			
Land	1500000	**LOANS AND ADVANSES**	
Construction of Building	4000000	MCHFS Loan to members 425000	
Shares of Maha.co.Hsg. Fin. So.	75000	Add :interest 35000	
		Less: collections 50000	410000
SECURED LOANS		Dues from members	
Loan from MCHFS 425000		Monthly Exp 4000	
Add: interest 35000		Parking Charges 600	4600
Less: repayment 50000	410000		
		FIXED ASSETS	
CURRENT LIABILITIES AND PROVISIONS		Land	1500000
Outstanding Expenses		Buildings	4000000
Audit Fees	5000		

Secretary's remuneration	2000		
PROFIT AND LOSS ACCOUNTS			
Profit for last Year 205600			
Add : surplus for the c/y 142500	348100		
	6519600		6519600

5. Following is the Trial Balance of Usha Kiran Co.Op Hsg. Society

Trial Balance as on 31st March, 2015

	RS.		Rs.
Balance with Dena Bank current a/c	142150	Contribution from Members	
Cash at Hand	2780	Property Tax	62420
Furniture	64500	Water Charges	14560
Water Pump	46500	Life Maintenance	22420
Computer	62000	Service Charges	54000
Gym equipment	85000	Insurance	3600
Land & Building	8000000	Rent received from hoarding	120000
Investment of Repairs Fund	242500	Rent recd from mobile towers	340000
Investment in Govt Securities	100000	Misc income	12560
Investment of Sinking Fund	132500	Interest from Govt Securities	6000
Shares of MCHFC	75000	Share Capital	30000
Dues from members (01.04.2014)	22430	Repairs Fund	242500
Electricity Charges	16480	Reserve Fund	342500
Municipal Taxes	65780	Sinking Fund	132500
Water Charges	13540	Income & Expenditure A/c.	212500
Salary	63510	Building Fund	8000000
Printing & Stationery	12420		9595560
Conveyance	3820		
Accounting Charges	15300		

Audit Fees	6300		
Bank Charges	420		
Security charges	48620		
Postage	3450		
Sundry Expenses	23560		
Honorarium to secretary	18000		
Lift Maintenance	24500		
Fire Insurance	4500		
F.D. with Union Bank	300000		
	9595260		

Adjustments

1. Provide for depreciation

   Furniture 10%, Computer 25%,Water Pump 20% Gym Equipments25%

2. Interest accrued on: Sinking fund Investment Rs.20,300, Repairs fund Investment Rs.13,400
3. The society transfers every year 0.25% of cost of building to sinking fund and 0.75%of cost of building to repairs fund. On the same day equal amount is transferred from bank account to respective fund investment account.
4. Members contribution receivable Rs.24620
5. Interest on F.D. with union bank is accrued @ 9%p.a.for the entire year.
6. Expenses Payable: Salary Rs. 2,800, Printing bill Rs.500
7. Insurance paid in advance Rs. 500
8. Education fund payable Rs.250

Prepare Income & Expenditure A/c. for the year ended 31st March 2015 and Balance sheet as on that date.

SOLUTION:

Usha Kiran Co.Op Hsg. Society ltd.

INCOME AND EXPENDITURE ACCOUNT for the Year Ended 31st March 2015

EXPENDITURE	Rs.	INCOME	Rs.
To Electricity Charges	16480	By Contribution from Members	
To Municipal Taxes	65780	Property Tax 62420	
To Water Charges	13540	Water Charges 14560	
To Salaries 63510		Life Maintenance 22420	
Add: O/s 2800	66310	Service Charges 54000	
To Printing & Stationery 12420		Insurance 3600	
Add: O/s 500	12920	157000	
To Conveyance	3820	Add: Closing o/s 24620	
To Accounting Charges	15300	Less Op O/s 22430	159190
To Audit Fees	6300	By Rent received from hoarding	120000
To Bank Charges	420	By Rent received from mobile towers	340000
To Security charges	48620	By Misc income	12560
To Postage	3450	By Interest from Govt Securities	6000
To Sundry Expenses	23560	By Accrued interest on FD	27000
To Honorarium to secretary	18000		
To Lift Maintenance	24500		
To Fire Insurance 4500			
Less: Prepaid 500	4000		
To Depreciation			
Furniture 6450			
Water pump			

9300 Computer 15500 Gym Equipment 21250	52500		
To transfer to Sinking Fund	20000		
To transfer to Repairs Fund	60000		
To Education fund payable	250		
To Reserve Fund	52250		
To Surplus	156750		
	664750		664750

BALANCE SHEET as on 31st March 2015

LIABILITIES	RS.	ASSETS	RS.
SHARE CAPITAL		**CASH AND BANK BALANCES**	
Authorised		Cash on hand	2780
Issued & paid up	30000	Cash at MSC bank 142150 Less: Trf to SF inv 20000	
RESERVE AND OTHER FUNDS		: trf to Rep F Inv 60000	78150
Reserve Fund 342500 Add: current year Transfer 52250	394750	**INVESTMENTS**	
Repairs Fund 242500 Add: current year Transfer 60000 Add : accrued Interest 20300	322800	Repairs Fund Invest 242500 Add : accrued Int. 20300 Add: current year Transfer 60000	322800
Sinking Fund 132500 Add: current year Transfer 20000 Add : accrued Int. 13400	165900	Sinking Fund Invest 132500 Add : accrued Int. 13400 Add: current year Transfer 20000	165900

Building Fund	8000000	F.D. With Union Bank	300000
		Shares in MCHFC	75000
CURRENT LIABILITIES AND PROVISIONS		Investments in Government securities.	100000
Outstanding Expenses		**LOANS AND ADVANCES**	
Salaries 2800		Dues from members	24620
Printing 500	3300		
Education fund payable	250	**FIXED ASSETS**	
		Buildings	8000000
PROFIT AND LOSS ACCOUNTS		Furniture 64500	
Profit for last Year 212500		Less: Depreciation 6450	58050
Add : surplus 156750	369250	Water Pump 46500	
		Less: Depreciation 9300	37200
		Computer 62000	
		Less: Depreciation 15500	46500
		Gym Equipment 85000	
		Less: Depreciation 21250	63750
		OTHER ITEMS	
		Prepaid Insurance	500
		Interest receivable on FD	27000
	9286250		9286250

1.11 EXERCISES

A. THEORY QUESTIONS:

1. What is Co-operative Housing Society? How it is formed?
2. What are special features of housing society?
3. What are different types of co-op Housing societies?

4. How the affairs of co-op. Housing society are managed?
5. What do you understand by “Bye-Laws”?
6. What are different provisions of MCS Act regarding maintaining of accounts by a co-op. Housing Society?

B. OBJECTIVE TYPE QUESTIONS

A. Fill in the blanks

1. A co-operative society is a -----------association of individuals who come together to achieve common objectives.
2. Co-operative society follows -----------management
3. The first item on asset side of the balance sheet of a co-operative society is ---------------------
4. A co-operative form of organization is based on the principle of ----------------------.
5. The Maharashtra co-op societies act was passed in the year----.
6. Register of members must be maintained in --------form.
7. ---------- means a person appointed to be the registrar of co-operative societies act.
8. In a co-operative society capital is contributed by all the ----------.
9. The society has a separate -------------under co-operative societies act.
10. The books of accounts of the society are audited by ---------- auditors.
11. Every co-operative has its own --------laws.

Answers: voluntary, democratic, Cash balance, democracy, 1960, I, Registrar, members, legal entity, government, bye.

B. True or false

1. The Maharashtra co-op societies act was passed in 1961. **True**
2. Education fund is shown in the balance sheet of a co-operative society under asset side. **False**
3. Balance sheet of a co-op society should be prepared in form B. **False**
4. Apex society is the society where the area of operation extends to the whole of Maharashtra. **True**
5. Every member of a society shall be entitled to inspect, free of cost, at the society’s office during office hours or any time fixed for the purpose by the society. **True**
6. Every society not necessarily contributes to education fund. **False**

7. Co-operative society is an involuntary association of members. **False**
8. In a co-operative society capital is contributed by outsiders. **False**
9. The main motive of a co-operative society is profit making. **False**
10. The society has a separate legal entity with limited liability of its members. **True**
11. The society is managed by one person only. **False**
12. Co-operative societies are formed to provide service rather than maximizing profit. **True**
13. Minimum 10 members are required to form a co-operative society. **True**
14. Co-operative society thrives on the principle of mutual help. **True**
15. Co-operative society works on the principle of one share one vote. **False**

C. Multiple Choice Questions:

1. Final Accounts of a Co-operative Society should be made within------ days of close of accounting year
   a. 90 Days
   b. 45 Days
   c. 60 Days
   d. 120 Days
2. The Maharashtra Co-operative Societies Act was passed in
   a. 1948
   b. 1952
   c. 1961
   d. 1675
3. A Co-operative society should nor pay dividend exceeding
   a. 5%
   b. 10%
   c. 15%
   d. 25%
4. Following is not a principle of co-operative society
   a. Democratic control
   b. Easy formation
   c. Social welfare
   d. Compulsory membership

5. Register of member should be maintained in form
    a. C
    b. F
    c. I
    d. N
6. Balance Sheet and profit and Loss Account of a co-operative society must be prepared in
    a. B form
    b. D form
    c. N form
    d. V form
7. Reserve fund created by a co-operative society can be utilized for
    a. Payment of dividend
    b. Payment of interest
    c. Repairs & Maintenance
    d. All of the above
8. Honorarium to office bearer should not exceed
    a. 15% of net Profit
    b. Rs. 2000
    c. 15% of net Profit Rs. 2000 whichever is less
    d. 15% of net Profit Rs. 2000 whichever is more
9. Contribution to repairs &maintenance Fund is
    a. .75% of construction cost of each flat
    b. .25% of construction cost of each flat
    c. .50% of construction cost of each flat
    d. 1.00% of construction cost of each flat
10. Contribution to repairs &maintenance Fund is
    a. .75% of construction cost of each flat
    b. .25% of construction cost of each flat
    c. .50% of construction cost of each flat
    d. 1.00% of construction cost of each flat
11. Staff Provident fund should be disclosed in the balance sheet under
    a. Separately on the liability side
    b. Current Liabilities
    c. Reserves
    d. Contingent Liability

12. Staff Provident fund investments should be disclosed in the balance sheet under
    a. Under Investments
    b. Under current assets
    c. Under loans & Advances
    d. **Separately on the asset side**.
13. A cooperative housing society is
    a. Sole proprietary business organization.
    b. Limited Liability Partnership
    c. Democratic organization
    d. Government organization
14. Every co-operative housing society must transfer ---- of its profit to reserve fund every year
    a. 10%
    b. 20%
    c. 30%
    d. 40%
15. A co-operative housing society should contribute Rs.--------- towards Education Fund
    a. Rs3
    b. Rs. 5
    c. Rs. 10
    d. Rs 100
16. Transfer fees should not Exceed Rs.
    a. Rs. 5000
    b. Rs. 10000
    c. Rs 25000
    d. Rs 50000
17. All expenses of the co-operative housing society are paid by
    a. The Government
    b. Secretary of the society
    c. Contributed by the members
    d. Office bearer of the society
18. Basic Document governing day to day activities of the society is called
    a. Bye -Laws
    b. Articles of Association
    c. Memorandum of Association
    d. Formation Deed.

19. Embers of Co-operative housing society contribute for
    a. Municipal taxes
    b. Security charges
    c. Parking charges
    d. All of the above
20. Co-operative housing society gets income from
    a. Monthly contributions from members
    b. Interest on investments
    c. Interest on loans to members
    d. All of the above
21. Following are called as office bearers
    a. Secretary
    b. Chairman
    c. Treasurer
    d. All of the above
22. Following is not called as office bearers
    a. Secretary
    b. Chairman
    c. Treasurer
    d. Auditor

❖❖❖❖

9

PROFIT PRIOR TO INCORPORATION-I

Unit Structure

13.0 OBJECTIVES:

After Studying this unit the students will be able to:

- Know the Concept of Profit / Loss Prior to Incorporation
- Calculate the Various Ratios
- Understand the Methods of ascertain pre-incorporation Profit or Loss
- Solve the practical problems.
- Understand the Treatment of Profit or Loss Prior / Post Incorporation

13.1 INTRODUCTION:

In the present scenario, corporate form of organization is preferred. Many existing Non – Corporate concerns get themselves converted into a corporate one, Company is a separate legal entity and enjoy certain tax benefits. Hence existing Propriority / Partnership concern may get converted into a limited company. Therefore they decide to form a Ltd. Co. to take over their business. Formation of a limited co. requires number of formalities and is a time consuming task, such as name approval of proposed company, preparation of Memorandum of Association, Articles of Association etc. In such a situation the promoters who acquire running business, may continue business on behalf of company prior to its incorporation. Therefore for first year; profit earned upto incorporation is considered as profits prior to incorporation.

13.2 MEANING:

Profits prior to incorporation means profits earned between the date of acquisition of business & the date of incorporation. Such situation arises in the first year of operation of the co; when same books of A/c's of the Vender are continued by promoters. The Profit / Loss Prior to Incorporation is determined nationally by allocating various Income & Expenses, Profit or Losses for the entire period (i.e. pre & post incorporation) between two time periods an appropriate logical basis.

13.3 CALCULATION OF VARIOUS RATIOS:

13.3.1 TIME RATIO:

Time Ratio is used for dividing fixed expenses which arise evenly spread within entire period. Pre Incorporation period consist from business acquired up date of Incorporation. Post Incorporation starts from date of Incorporation till accounting period end. The entire period is normally of a year (12 months). But it can be longer or shorter period also depending upon situation.

Illustration 1 : Calculation & various Time Ratio

	Date of Business Acquired	Date of Incorporation	Accounting End	Time Ratio
a)	1st April 14	31st May 14	31st March 15	= 12 mths
	Pre Incorporation 2 Months		Post Incorporation 10 Months	= 1 : 5
b)	1st Jan 14	31st March 148	31st Dec 14	= 12 mths
	Pre Incorporation 3 Months		Post Incorporation 9 Months	= 1 : 3
c)	1st May 14	30th Sept 14	31st Dec 14	= 8 mths
	Pre Incorporation 5 Months		Post Incorporation 3 Months	= 5 : 3
d)	1st Jan. 14	1st April 14	31st March 15	= 15 mths
	Pre Incorporation 3 Months		Post Incorporation 12 Months	= 1 : 4

13.3.2 SALES RATIO / TURNOVER RATIO

Sales Ratio is used for dividing gross Profit, variable expenses etc. Sales Ratio is calculated by comparing sales of pre & post Incorporation period. However if sales are not even / uniform per month, then Weighted Average Sales ratio should be calculated.

Illustration: 2 (Various Sales Ratio)

a) Net Sales Rs.16,00,000/-
Pre Incorporation Sales Rs.5,00,000/-

Post Incorporation Sales = Net Sales (–) Pre Incorporation Sales
= 16,00,000 (–) 5,00,000
= Rs.11,00,000/-

Sales Ratio = 5:11

b) A Ltd. was incorporated on 1st May 14 to take over A & Co. business w.e.f. Feb. 14, period ended 31st Dec 14 monthly sales were doubled from 1st July.

Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1	1	1	1	1	2	2	2	2	2	2
Pre – Incorporation			Post – Incorporation							
3			14							

Sales Ratio = 3:14

c) B Ltd. was incorporated on 1st May 14 to take over B & Co. business w.e.f. 1st Feb.14, period ending 31st Dec. 14. Monthly Sales were doubled from 1st Sept. 14.

Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1	1	1	1	1	1	1	2	2	2	2
Pre – Incorporation			Post – Incorporation							
3			12							

Sales Ratio = 3:12 = 1:4

d) C Ltd. was incorporated on 1st June 14 to take over business from 1st Jan 14 Accounting year ends 31st December 2014. Monthly sales for each month of July to December was thrice the monthly sales of January to June 14.

Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1	1	1	1	1	1	3	3	3	3	3	3
Pre – Incorporation					Post – Incorporation						
5					19						

Sales Ratio: 5:19

e) D Ltd. was incorporated on 1st May 14 to take over business from 1st March 14 for period ending 31st Dec.14. Trend of Sales were as under. Monthly Sales were doubled from 1st July & again from 1st Nov. monthly sales were double that of Oct. Month.

Mar	Apr	May	Jun	July	Aug	Sep	Oct	Nov	Dec
1	1	1	1	2	2	2	2	4	4
2		18							

Sales Ratio = 2:18 = 1:9

13.3.3 WEIGHTED AVERAGE RATIO

This ratio is calculated when Sales / Incomes expenses are not uniform throughout the period.

Illustration: 3 (Calculated various Weight Average Ratio)

A) There are 5 employees up to Incorporation (3 months) and then 8 employees in post Incorporation period (9 months)

Salary Ratio: No. of employees X no. of months

Pre = 5 X 3 = 15

Post = 8 X 9 = 72

Salary Ratio = 5:24

B) X Ltd. was incorporated on 01/08/14 to take over business from 1st April 14 closes accounts on 31st March 15 due to decrease selling price by 20% from 1st Nov. 14 sales in terms of volume (quantities) were doubled from 1st Nov. 14. Ascertain Sales Ratio.

	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar
A	1	1	1	1	1	1	1	2	2	2	2	2
x B	100	100	100	100	100	100	100	80	80	80	80	80
=Sales	100	100	100	100	100	100	100	160	160	160	160	160
Pre 400					Post 1100							

Sales Ratio = 4:11

A **B**

Note : Quality Sold X Selling Price

(Assuming Selling Price = Rs.100/-)

13.3.4 SPECIFIC RATIO

Some expenses may be incurred during specific part of accounting period. This needs to be allocated on basic given data.

a) Interest to vendors paid for period up to date of payment. A company incorporated on 31/07/14. The business taken over on 01/04/14. Interest paid on 31/10/14. This interest is paid upto 31/10/14. This is to be allocated as time ratio as follows.

Apr	May	Jun	July	Aug	Sep	Oct
1	1	1	1	1	1	1
4				3		

Ratio = 4:3

b) Expenses incurred for specific period or on specific date.
E.g. Profit or Loss an sale of Asset on a given date.
Bad Debt pertaining to specific period.
Depreciation an asset acquired during year.

13.3.5 SPECIFIC FOR FORM OF ORGANIZATION

The expenses or Income related to particular form or organization is not to be allocated. These are to be pre – Incorporation or post – Incorporation as case may be.

e.g. a) Directors Remuneration paid by company – Post Incorporation
b) Interest on Debenture Issued by company – Post Incorporation
c) Preliminary Expenses – Post Incorporation (Written off by company)
d) Remuneration or Salary to Partner – Pre Incorporation

13.4 METHODS OF ASCERTAINING PRE-INCORPORATION PROFIT / LOSS:

The pre – Incorporation Profit / Loss can be ascertained in three ways as follows:

i) By preparing separate Profit & Loss A/c for the period up to date of incorporation.

ii) By preparing usual Profit & Loss A/c for entire period and then dividing net Profit / Loss on appropriate basis between two periods.

iii) Combined or Equitable basis – as per available information

13.4.1 SEPARATE PROFIT & LOSS A/C

In this method books of A/c's are balanced and trial balance as on date of Incorporation is prepared. The Profit & Loss A/c, Balance Sheet can also be prepared. However this method, being inconvenient & is practically unnecessary as number of adjustment like depreciation, stock valuation, outstanding expenses prepaid expenses are usually carried out for preparing Final Accounts.

13.4.2 PREPARING PROFIT & LOSS A/C FOR ENTIRE PERIOD AND DIVIDING NET PROFIT / LOSS ON SALE BASIS OR TIME BASIS

Under this method, net Profit for both the period is estimated expenses as well as Incomes are not uniform, some expense or Income may relate to either pre or post Incorporation period. Similarly all expenses or Incomes may not be in same proportion of Time or Sales basis. Therefore this method is not suitable for ascertainment of pre Incorporation Profit / Loss.

Normally Trading Account is prepared for full period as combined Account to ascertain Gross Profit. The Gross Profit is to be transferred to Profit & Loss A/c on ratio of sales.

However, if information of Sales & Purchase for pre – post period & stock an date of incorporation is available then Trading Account can also be prepaid for pre & post period separately in columnar format.

13.4.3 COMBINED OR EQUITABLE BASIS

Under this method Trading Account is prepared for the entire period and gross Profit is ascertained. However if division of purchase, sales direct expenses, stock as on date of Incorporation & year end are available, then Trading Account can be prepared in two parts i.e. pre & post Incorporation, Gross Profit for pre & post Incorporation automatically is ascertained.

13.4.4 FOLLOWING PROCEDURE SHOULD BE FOLLOWED

a) Profit & Loss Account Credit side
b) Profit & Loss Account Debit side

a) Profit & Loss Account Credit Side

i) Gross Profit:

Gross Profit is generally divided into sales ratio. In case there is a change in sales price or cost price between two periods then actual Gross Profit is worked out by considering change in turn over and / or cost. In case details of sales are not available, then it is assumed that sales are spread over equally / evenly in the entire period. So Gross Profit is divided in time ratio.

ii) Other Incomes:

1. Specific Income for a particular period is credited to that period e.g. share transfer fees should be credited in post Incorporation.
2. Discount received is on purchase basis, otherwise sales ratio.
3. Income received on time basis should be divided into time basis e.g. Income from investment, Rent received.

b) Profit & Loss Account Debit Side

i) Time Ratio:

Fixed Expenses / Period Expenses which are incurred with reference to time should be allocated on time basis e.g. Salaries, Audit Fees, Postage, and Depreciation on Fixed Assets, Rates and taxes.

ii) Sales Ratio:

Variable Expenses / Fluctuating Expenses which are related to turnover should be allocated in sales ratio e.g. Bad Debts w/off Advertisement, Sales Commission, Carriage outward. However if any specific information is given in the problem, then expense should be allocated accordingly e.g. Rent paid for pre Incorporation period.

iii) Specific Expenses / Income:

Corporate expenses incurred are charged to post incorporation period e.g. Director Fees, M.D. Fees, Debenture Interest etc.

Expenses incurred by vendor are charged to pre Incorporation period.

Expenses for which specific information is available are allocated accordingly.

Illustration: 4 (Division on basis of information given)

4.1 Bad debts w/off in respects of debts taken from vendor should be debited to Pre-Incorporation & remaining bad debts, should be charged to Post-Incorporation.

4.2 Interest paid to vendor on purchase consideration should be allocated according to the ratio calculated with reference to actual period covered. E.g. A Ltd. was incorporated on 1st March 14 to take over business on 1st Jan 14 purchase consideration was discharged on 31st May 14. Interest paid to vendor Rs.20,000/-.

In above example interest is paid for the period 1st Jan 14 to 31st May 14 (5 months.)

Pre –Incorporation interest = (20000/5)x2=8000
(1st Jan 2014 to 1st March 14 = 2 months)

Post-Incorporation Interest = $\frac{20,000}{5}\times 3 = 12000$
(1st March to 31st May 14 = 3 months)

4.3 Gross Profit is usually divided in Sales Ratio. However if there is change S.P. or C.P. or both, ratio should be worked out accordingly. Z Ltd. increased its sales price by 20% in post incorporation period. However, cost of production remained same. If pre –incorporation sales Rs.3,00,000/- & post-incorporation period sales Rs.15,00,000/- pre-incorporation G.P. was 20% on sales. Find Gross Profit for pre & post incorporation separately.

Pre	S.P.	G.P.	C.P.	G.P. = 3,00,000 x 20%
Let	100	20	80	(Pre) = 60,000
Revised (Post)	120	40	80	(cost remains same)

Post Incorporation G.P. = 15,00,000 X $\frac{40}{120}$ = Rs.5,00,000/-

4.4 Depreciation on Fixed Assets is usually divided in Time Ratio. However if Addition / Sale of fixed assets is given in the problem, then for division of depreciation should be after considering period for which it refers e.g. Y Ltd. was incorporated on 1st May 14 to take over business from 1st Jan 14, Y Ltd. closes its Books of Accounts on 31st Dec. 14.

Depreciation decided to Profit & Loss A/c amounted Rs.30,000/- includes depreciation @ 10% p.a. plant costing Rs.3,00,000/- which was purchased 1st Oct. 08.

	Depreciation	Pre	Post
a)	Dep. on plant purchased on 01/10/14 to 31/12/14 for Post-Incp. 3,00,000 X 10% X $\frac{3}{12}$	-	7,500
b)	Remaining Depreciation in Time Ratio (30,000 – 7,500) = 22,500 in 1:2	7,500	15,000
	Total Depreciation	7,500	22,500

4.5 Provision for Income Tax

Income Tax is payable at a specified percentage of Profit. Provision for Income Tax should be calculated at specified percentage net Profit for each period (pre/post) separately. However, if Income Tax provision is specified for a specific amount, same should be allocated an ratio of net tax net profit for pre & post period.

Pre-Incorporation Profit	Post-Incorporation Profit
75,000	1,25,000

1. Provision for Income Tax @ 30% of Profit.
   75,000 @ 30% = 22,500, 1,25,000 @ 30% = 37,500
2. Provision for Income Tax Rs.36,000/-
   Ratio of Profit 75:125 or 3:5
   Rs.13,500 Rs.22,500

13.5 ACCOUNTING TREATMENT:

i) Profit prior to Incorporation is a capital Profit & hence it should be transferred to Capital Reserve. Capital Reserve may be used to write off Goodwill, Share Issue Expenses, Discount on issue of Debenture etc.

ii) Loss prior to Incorporation should be debited to Goodwill Account.

iii) Post Incorporation Profit / Loss should be transferred to Profit & Loss Appropriation Account, being revenue profit.

The Final Account

The Final Account of companies includes Profit & Loss Account & Balance sheet. After preparing Profit & Loss Account as explained above, Balance Sheet is should beprepared.

13.6 PROFORMA OF PROFIT AND LOSS ACCOUNT UNDER EQUITABLE BASIS

Trading Accounts for the year / period

Dr. Cr.

Particulars	Pre	Post	Particulars	Pre	Post
To Stock A/c			By Sales A/c		
To Purchase A/c			By Stock A/c		
To Direct Expenses A/c					
To Gross Profit c/d					

Note: If the period wise data of purchases, sales and direct expenses, stock on date of Incorporation is not available, columnar presentation is not possible.

Profit & Loss Account

Dr. **Cr.**

Particulars	Basis	Pre	Post	Particulars	Basis	Pre	Post
To Salaries A/c	Time			By Gross Profit c/d	Sales		
To Rent A/c	Time			By Commission on purchase	Purch. or sales		
To Electricity A/c	Time						
To Pre-Incorporation Specific Exp. A/c	Pre			By Investment Income	Specific		
To Post-Incorp. Specific Exp. A/c	Post			By Share Transfer Fee	Post		
To Administration Expenses A/c	Time			By Goodwill A/c	(BF)	x	
To Interest on Deb. vendor A/c	Post-Specific			By Loss A/c	(BF)		x
To Bad debts A/c	Sales						
To Advertisement A/c	Sales						
To Audit Fees A/c	Time						
To Provision for Income Tax A/c	Net Profit						
To Capital Reserve A/c	(BF)	x					
To Net Profit c/d	(BF)		x				

Note: The above basis would need to be changed as per specific data given.

13.7 SOLVED PROBLEMS:

Illustration: 1 (Simple problem)

Jai Ltd. was incorporated on 1st June 2014 to take over running business of JR & Co. with effects from 1st April 2014. The same books of accounts continued and following Profit & Loss Accounts for the year ended 31st March 2015, was prepared.

Profit & Loss Accounts for the year ended 31st March 2015

Dr. Cr.

Particulars	Rs.	Particulars	Rs.
To Salaries A/c	48,000	By Gross Profit b/d	3,72,000

To Office Rent A/c	12,000	By Discount earned	5,400
To Printing & Stationery A/c	6,000	By Share Transfer Fees	600
To Directors Fees A/c	7,250		
To Sundry Expenses A/c	3,000		
To Depreciation A/c	9,000		
To Advertisement Expenses A/c	24,000		
To Preliminary Exp. w/off	2,500		
To Sales Commission A/c	42,000		
To Loss on sale of old Furniture A/c	3,000		
To Audit Fees A/c	9,000		
To M.D. Remuneration A/c	6,250		
To Partner Salaries A/c	1,750		
To Interest paid to vendor A/c (upto 30/04/08)	6,000		
To Debenture Interest A/c	14,250		
To Discount on issue of Debentures A/c	4,000		
To Net Profit c/d	1,80,00		
	3,78,000		3,78,000

Other information:

1) Furniture was sold on 31st March 2015.
2) Monthly average sale were doubled from 1st January 2015.
3) 50% of Advertising Expenses were related with sales and balance expenses for outdoor advertising were paid on monthly basis.
4) Purchase consideration was settled on 31st July 2014 along with interest due upto that date.

Prepare Profit & Loss Account for the year 31st March 2015 appropriating between the pre and post Incorporation period.

Solution:

Jai Ltd.
Profit & Loss Account for the year ended 31st March 2015

Dr. **Cr.**

Particulars	Basis	Pre	Post	Particulars	Basis	Pre	Post
To Salaries A/c	TR	8,000	40,000	By Gross Profit c/d	SR	49,600	3,22,400
To Office Rent A/c	TR	2,000	10,000			720	4,680
To Preliminary Exp.				By Discount		-	600

A/c	TR	1,000	5,000	earned	SR		
To Directors Fees	Post	-	7,250	By Share			
To Sundry Exp. A/c	TR	500	2,500	Transfer Fee	Post		
To Depreciation A/c	TR	3,000	6,000				
To Advertising Exp.							
A/c	W/N	3,600	20,400				
To Preliminary Exp.							
A/c	Post	-	2,500				
To Sales							
Commission A/c	SR	5,600	36,400				
To Loss on Sale of							
Furniture A/c	Post	-	3,000				
To Audit Fees A/c	TR	1,500	7,500				
To M.D.							
Remuneration A/c	Post	-	6,250				
To Partner's							
Salaries A/c	Pre	1,750	-				
To Interest paid to							
vendor A/c	W/N	3,000	3,000				
To Debenture Int.A/c	Post	-	14,250				
To Discount on							
issue Debentures	Post	-	4,000				
To Capital Reserve							
A/c	Pre	20,370	-				
To Net Profit c/d		-	1,59,630				
		50,320	3,27,680			50,320	3,27,680

Working Note:

1) Time Ratio = 1:5

Date of Acquisition	Date of Incorporation	Date of year end
1st April 2015	1st June 2014	31st March 2015

Pre Incorporation 2 Months

Post Incorporation 10 Months

Time Ratio = 2:10 = 1:5

b) Sales Ratio = 2:13

Monthly average sales were doubled from 1st January 2015

Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	March
1	1	1	1	1	1	1	1	1	2	2	2
Pre-		Post Incorporation Period									

Incop	
2	13

∴ Sales Ratio = 2:13

c) Advertisement Expenses = Rs.24,000

	Pre	Post
a) Sales promotion Exp. in Sales Ratio (24,000 X 50% = 12,000 in 2:13)	1,600	10,400
b) Balance 50% in Time Ratio (12,000 in Time Ratio = 1:5)	2,000	10,000
	3600	**20400**

d) Interest paid to vendor Rs.6, 000/- for the period from 1st April 2014 to 31st July 2014 (4 months)

∴ Pre (2 months) = 6,000 X $\frac{2}{4}$ = 3,000

∴ Post (2 months) = 6,000 X $\frac{2}{4}$ = 3,000

6,000

Illustration 2: (Calculation of Depreciation, Commission on Actual basis)

H Ltd. was incorporated on 1st September 2014 to take over a business from 1st April 2014. The accounts were made up to 31st March 2015 as usual and Profit & Loss Accounts showed the following results.

Profit and Loss A/c for the year on ended 31st March2015

Dr. Cr.

Particulars	Rs.	Particulars	Rs.
To Salaries A/c	24,000	By Gross Profit b/d	2,10,000
To Rent A/c	6,400	By Interest (from	
To Directors Fees A/c	7,000	Bank F.D. made	12,000
To Bad debts	9,000	on 1st Octo2014)	
To Travellers			
commission A/c	18,900		
To Audit Fees A/c	4,000		
To Office Expenses A/c	10,000		
To Discount A/c	6,000		
To Depreciation A/c	25,000		

To Debenture Interest A/c	9,000		
To Goodwill w/off	4,000		
To Advertisement A/c	7,200		
To Interest on purchase consideration (31/7/08)	35,000		
To Printing & Stationery A/c	6,600		
To Net Profit c/d	49,900		
	2,22,000		2,22,000

Additional Information:

1) It is ascertained that sales for May, November, January 2015, February and March were only half the average sales, April were one and half the times of the average of the year end those for October twice the average. Annual net sales amounted Rs.6,00,000/-.
2) Bad debts written off were:
   a) A debt of Rs.4,000/- taken over from vendor
   b) A debt of Rs.5,000/- in respect of Goods sold in November 2014.
3) Travellers commission was 2.5 of sales upto 31/12/2014 then it is increased to 4% on Sales.
4) Office Rent was Rs.6,000/-p.a. upto 31st November 2014, then it was increased by 20%.
5) Depreciation on Furniture amounted to Rs.1,000/- which was discarded on 31st August 2014 sold at Book value. Depreciation @ 10% on New Furniture costing Rs.60,000/- purchased on 01/01/2015.
6) Allocate expenses in an appropriate manner.

Solution:

Profit & Loss A/c for the year ended 31st March 2015

Dr. Cr.

Particulars	Basis	Pre	Post	Particulars	Basis	Pre	Post
To Salaries A/c	TR	10,000	14,000	By Gross Profit c/d	SR	98,000	1,12,000
To Rent A/c	WN4	2,500	3,900	By Interest A/c	-	-	12,000
To Directors Fees A/c	Post	-	7,000				
To Bad debts A/c	Act	4,000	5,000				
To Travellers Commission A/c	WN3	7,000	11,900				
To Audit Fees A/c	TR	1,667	2,333				
To Office Expenses A/c	TR	4,167	5,823				
To Discount A/c	SR	2,800	3,200				
To Depreciation A/c	WN5	10,375	14,625				

To Debenture Interest A/c	Post	-	9,000				
To Goodwill w/off	Post	-	4,000				
To Advertisement A/c	SR	3,360	3,840				
To Interest on purchase consideration A/c	WN	25,000	10,000				
To Printing & Stationery A/c	TR	2,750	3,850				
To Capital Reserve A/c	-	24,381	-				
To Net Profit c/d	-	-	25,519				
		98,000	1,24,000			98,000	1,24,000

Working Note :

1) Time Ratio = 5:7

Date of Acquisition 01/04/2014 — Date of Incorporation 01/09/2014 — Year end 31/03/2015

Pre Incorporation 5 months — Post Incorporation 7 months

Time Ratio = 5:7

2) Sales Ratio = 7:8

Total Sales = Rs.6,00,000

$\therefore$ Average Monthly Sales = $\frac{6,00,000}{12}$ = 50,000

Pre		Post	
April	75,000	September	60,000
May	25,000	October	1,00,000
June	60,000	November	25,000
July	60,000	December	60,000
August	60,000	January	25,000
		February	25,000
		March	25,000
	2,80,000		3,20,000

$\therefore$ Remaining 5 months Sales

= Total Sales (-) Specific Sales Noted

= 6,00,000 (-) 3,00,000 = 3,00,000

$\therefore$ Remaining Monthly Sales = $\frac{300000}{5}$ = 60,000/- p.m.

3) Travellers commission 2.5% of sales upto 30/09/2014, then increase to 4% of sales.

Pre = 2,80,000 X 2.5%		7,000
Post = September 60,000 X 2.5%	1,500	
October to March 2,60,000 X 4%	10,400	11,900
Total Commission		18,900

4) Office Rent was Rs.6,000/- p.a.
= Rs.500/- p.m. upto 30th November 2014.

After 1st December,2014, it was increased by 20%
= 500 + 20% = Rs.600/- p.m.

Pre (upto 31st August2014) 500 X 5		2,500
Post SeptemberOctober ,November,= 500 X 3	1,500	
December14 to March 15 = 600 X 4	2,400	3,900
		6,400

5) Depreciation

	Pre	Post
a) On Furniture discarded on 30/05/08 b) New purchase on 01/10/08 in post 60,000 X 10% X $\frac{3}{12}$ Balance Depreciation = 25,000 – (1,000+1,500) = 22,500 in Time Ratio i.e. 5:7	1,000 9,375	1,500 13,125
	10,375	14,625

Total Depreciation = Rs.25,000/-

6) Interest on purchase consideration Rs.35,000/- paid for the period from 1st April 2014 to 31st October 2014 = 7 months

Pre = 1st April 2014to 31st August 2014 = 5 months = $\frac{35000}{7} \times 5$
= 25,000

Post = Septem. & October, 2 months = $\frac{35000}{7} \times 2$ = 10,000

Total Rs. = 35,000

Illustration: 3

Cho. Chang Ltd. was Incorporation on 1st July 2014 to acquire the business of KT & Co. as on 1st April, 2014. The purchase price of Goodwill was agreed to the sum equal to 75% of the Profit of the business for five years commencing from 1st April 2014, payment to be made at the end of 5th year on ascertainment of the sum due.

The following is the trial balance of Cho. Chang Ltd as on 31st March 2015.

Particulars	Debit	Credit
Equity Share Capital (Rs.10/- each)	-	2,00,000
Sundry Debtors	80,000	-
Stock (on 31.03.09)	1,55,000	-
Director's fees	20,000	-
Bills Receivable	18,000	-
Preliminary Expenses	20,000	-
Sundry Creditors	-	15,000
Net Profit for the year (as per agreement)	-	60,000
	2,75,000	2,75,000

Prepare –

a) Statement of Appropriation of Profit writing of 1/5th of the preliminary expenses.

b) Amount of Goodwill due for the year

Solution:

a) Statement of Appropriation Profit

	Pre-Incorporation		Post-incorporation	
	Rs.	Rs.	Rs.	Rs.
Net Profit for year Time Ratio Pre = $60,000 \times \frac{3}{12}$ Post = $60,000 \times \frac{9}{12}$		15,000		45,000
Less : : i) Directors Fees			2,000	
ii) Preliminary Exp $20,000 \times \frac{1}{5}$		-	4,000	(6,000)
		15,000		39,000

b) Goodwill = 60,000 X 75%
= Rs.45,000/-

Rs.45,000/- due for Goodwill base on Net Profit of year 07 – 08, however amount will be payable along with subsequent years value of Goodwill, at end of 5th year.

Illustration: 4 (Typical Sales Ratio, Rent & Taxes, Salaries, Travelling Expenses allocation)

R. Rice Ltd. was registered on 1st July. 14 to acquire the business of **Dalal** Co. as on 1st May 2014. The accounts of the company for the period ended 31st March 15 disclosed the following expenses / Income:

Particulars	Rs.	Particulars	Rs.
Office Expenses	5,500	Formation Exp. (1/5 to be written off)	15,000
Rent & Taxes	6,900	Depreciation	4,400
Audit Fees	4,400	Printing & Stationery	1,650
Bad debts (of which Rs.1,000/- debts created before 31.12.14)	1,600	Commission	7,200
		Traveling Expenses	16,600
Salaries	44,800	Interest to vendors	6,000
Debenture Interest	5,000	Discount on Debentures (1/10 to be written off)	10,000
Discount Received	9,000		
Bad debts realized	1,500	Carriage Outwards	9,000

Additional Information:

a) Net Sales for the entire period amounted to Rs.5,00,000/- of which Rs.50,000/- related to the period from 1st May 14 to 30th June 14.

b) Cost of goods sold for the above period amounted to Rs.3,20,000/-.

c) There three employs upto 30th July. 14, four employees from August 14 to 31st December 14 and there are 7 employees after wards.

d) Bad debts realized related to sales effected prior to Incorporation.

e) Purchase consideration was discharged on 30th July14.

f) Rent was paid Rs.2,400/- p.a. up to 30th September 14, afterwards it is increased by 25%.

g) Travelling expenses includes to Rs.10,000/- towards sales promotion, balance expenses were season railway passes to office staff.

Show pre and post Incorporation results

Solution:

R. Rice Ltd.

Profit & Loss A/c for the year ended as on 31st March 15

Dr. Cr.

Particulars	Basis	Pre	Post	Particulars	Basis	Pre	Post
To Office Salaries A/c	WN4	5,376	39,424	By Gross Profit c/d	SR	18,000	1,62,000
To Office Expenses A/c	TR	1,000	4,500	By Discount A/c	SR	900	8,100
To Rent & Taxes A/c	WN6	1,200	5,700	By Bad debts realized A/c	Pre	1,500	-
To Audit fees A/c	TR	800	3,600				
To Bad debts A/c	Act	1,000	600				
To Debenture Interest A/c	Post	-	5,000				
To Formation Expenses w/off	Post	-	3,000				
To Depreciation A/c	TR	800	3,600				
To Printing & Stationery A/c	TR	300	1,350				
To Commission A/c	SR	720	6,480				
To Travelling Expenses A/c	WN7	2,200	14,400				
To Interest to Vendor A/c	WN5	4,000	2,000				
To Discount on issue of Debenture A/c	Post	-	1,000				
To Carriage outwards A/c	SR	900	8,100				
To Capital Reserve A/c	-	2,104	-				
To Net Profit c/d	-	-	71,346				
		20,400	1,70,100			20,400	1,70,100

Working Note :

1) Time Ratio = 2:9

Date of Acquisition Date of Incorporation Year end

$$\underbrace{01/05/14 \quad\quad\quad\quad}_{\text{Pre Incorporation 2 months}} 01/07/14 \underbrace{\quad\quad\quad\quad 31/03/15}_{\text{Post Incorporation 9 months}}$$

Time Ratio = 2:9

2) Sales Ratio = 1:9
Pre = 50,000
Post = 5,00,000 (-) 50,000 = 4,50,000
50:450 i.e. 1:9

3) Gross Profit = Net Sales Less Cost of Goods sold
= 5,00,000 (-) 3,20,000 = Rs.1,80,000

4) Salaries

May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar
3	3	3	4	4	4	4	4	7	7	7
Pre		Post								
6		44								

Ratio = 3:22

Pre = 44,800 X $\frac{3}{25}$ = 5,376

Post = 44,800 X $\frac{22}{25}$ = 39,424

5) Interest paid to vendor Rs.6,000/- for the period From 1st May14 to 31st July 14 (3 months)

Pre (May June) = $\frac{6000}{3} \times 2$ = Rs.4,000

Post = 6,000 (-) 4,000 = Rs.2,000 (1 month)

6) Rent & Taxes Rs.6,900/-

<u>Rent</u>

Pre = May June = 200 X 2		400
Post = July, August & September = 200 X 3	600	
October 14 to Mar 15 = 250 X 6	1,500	2,100
(200 + 25% increase)		
Total Rent		2,500

<u>Taxes</u> (6,900 – 2,500) = 4,400 in Time Ratio i.e. 2:9

Pre = 4,400 X $\frac{2}{11}$ = 800

Post = 4,400 X $\frac{9}{11}$ = 3,600

Rent and Taxes	Pre	Post
Rent Taxes	400 800	2,100 3,600
Total	1,200	5,700

7) Travelling Expenses

	Pre	Post
Sales promotion exp. In Sales Ratio Rs.10,000/- in 1:9	1,000	9,000
Bal. Season passes in Time Ratio 16,600 (-) 10,000 = 6,600 in 2:9	1,200	5,400
Total	2,200	14,400

Illustration: 5 (Calculation of sales from G.P., Audit Fees typical adjustment)

Hari Ltd. was incorporated on 1st June 14, to take over the running business of JR & Sons with effects from 1st April 14.
The following Profit & Loss A/c was prepaid for the year ended 31st March 2015.

Particulars	Rs.	Particulars	Rs.
To Office Rent A/c	10,000	By Gross Profit b/d	2,00,000
To Printing & Stationery A/c	2,000	By Income from Investment A/c	6,000
To Office Expenses A/c	9,000	By Rent Received A/c	25,000
To Advertisement A/c	8,000		
To Travelling Exp. A/c	7,500		
To Debenture Interest A/c	10,000		
To Auditor Fees A/c	6,000		
To Directors Fees A/c	12,000		
To Bad debts A/c	4,700		
To Interest on Capital A/c	4,000		
To Electricity Charges A/c	3,000		
To Commission A/c	19,000		
To Depreciation A/c	24,000		
To Net Profit c/d	1,11,800		
	2,31,000		2,31,000

Additional Information:

1) Gross Profit upto 30th May 14 amounted to Rs.50,000/- @ Rate of 20% on Sales; however, it was increased to 25% from 1st June 14.
2) Office Rent was paid upto 31st July 14, there after Hari Ltd. purchased Own Building costing Rs.6,00,000/- on 1st August14, depreciation charge on Building 2.5% p.a., part of Building was let out by company.
3) In lieu of interest on purchase consideration, the vendors would get 40% of the profit earned prior to Incorporation.
4) Investment was purchased on 1st October 14.
5) Board of Directors appointed Auditor on remuneration of 3,000/- p.a. to audit books of accounts from 1st April, 14, however, he resigned on 31st July after auditing upto 30th June14. He was paid upto 30/06/14. The price Home & Co. accepted to audit from 1st July 14, they were paid accordingly.
6) Commission on sales was paid @ 2% on sales upto 31st May 14, after 1st June 14 it was increased by 1%.

Find out the Profit prior to Incorporation and subsequent to Incorporation.

Solution:

Hari Ltd.

Profit & Loss A/c for the year ended as on 31st March 15

Dr. Cr.

Particulars	Basis	Pre	Post	Particulars	Basis	Pre	Post
To Office Rent A/c	WN3	5,000	5,000	By Gross Profit c/d	WN2	50,000	1,50,000
To Printing & Stationery A/c	TR	333	1,667	By Income from invest. A/c	Post	-	6,000
To Office Expenses A/c	TR	1,500	7,500	By Rent recd	Post	-	25,000
To Advertisement A/c	SR	2,353	5,647				
To Travelling Exp. A/c	SR	2,206	5,294				
To Debenture Interest A/c	Post	-	10,000				
To Audit Fees A/c	WN4	500	5,500				
To Director's Fees A/c	Post	-	12,000				
To Bad Debts A/c	SR	1382	3,318				
To Interest on Capital A/c	Pre	4,000	-				
To Electricity Charges A/c	TR	500	2,500				
To Commission A/c	WN5	1,000	18,000				
To Depreciation A/c	WN6	1,000	23,000				

To Profit to Vendor A/c	WN7	12,090	-				
To Capital Reserve A/c		18,136	-				
To Net Profit c/d		-	81,574				
		50,000	1,81,000			50,000	1,81,000

Working Note :

1) Time Ratio = 1:5

Date of Acquisition 01/04/14 — Date of Incorporation 01/06/14 — Year end 31/03/15

$\underbrace{01/04/14 \quad\quad 01/06/14}_{\text{Pre Incorporation 2 months}} \quad \underbrace{01/06/14 \quad\quad 31/03/15}_{\text{Post Incorporation 10 months}}$

Time Ratio = 1:5

2) Sales Ratio = 5:12

Gross Profit for pre-incorporation @ 20% was Rs.50,000/-

$\therefore$ Pre-sales = $\frac{\text{Gross Profit}}{\text{G.P.}} = \frac{50,000}{20\%}$ = Rs.2,50,000/-

$\therefore$ Post Gross Profit = 2,00,000 (-) Pre G.P. 50,000
= 1,50,000

Gross Profit ratio for post-Incorporation = 25%

$\therefore$ Post Sales = $\frac{\text{Gross Profit}}{\text{G.P.}} = \frac{1,50,000}{25\%}$ = Rs.6,00,000/-

Sale
Pre = 2,50,000/-
Post = 6,00,000/-
Sales Ratio = 5:12

3) Office Rent : Rs.10,000/- paid from 1st April 14 to 31st July 14 (4 months)

Pre = (April, May) $\frac{10,000}{4}$ X 2 = 5,000

Post = (June, July) $\frac{10,000}{4}$ X 2 = 5,000

4) Audit Fees

	Pre	Post
First Auditors Fees $\frac{3,000}{12}$ = 250/- p.m.	250 X 2 = 500	250 X 1 = 250

Audited April, May, June Months Price – Home & Co. Bal. fees in post period (6,000 – 750)	 - 	 5,250
Audit Fees	500	5,500

5) Commission on Sales

	Pre	Post
a) 2% on Sales upto 31/05/14 = 50,000 X 2%	 1,000	 -
b) 3% on Rs.6,00,000/- post sales	-	18,000
	1,000	18,000

6) Depreciation

	Pre	Post
a) On Building on Rs.6,00,000/- @ 2.5% p.a. from 1st August 14 to 31st March 25 = 8 months **6,00,000 X 2.5% X $\frac{8}{12}$ (post)**	-	**18,000**
b) Balance Depreciation = 24,000 (-) 18,000 Rs.6,000/- in Time Ratio = 1:5	1,000	5,000
Total Rs.	1,000	23,000

7) Profit to vendor = 40% of Pre-Incorporation
= 30,226 X 40%
= Rs.12,090/-

Illustration: 6 (Typical and having different selling price)

Murali Ltd. was incorporated to take over running business of TR & Co. from 1st Jan 14. The following Profit & Loss A/c is prepared for the period ended 31st March 2015.

Profit & Loss A/c for the period ended 31st March 15

Dr. Cr.

Particulars	Rs.	Rs.	Particulars	Rs.	Rs.
To Cost of goods			By Sales		
sold A/c		10,00,000	Cash	3,40,000	
To Administrative			Retailers	2,40,000	
Expenses A/c		78,000	Wholesalers	6,40,000	
To Selling Expenses			Exports	6,00,000	18,20,000

A/c		10,000	By Share Transfer Fees A/c		10,000
To Office Rent A/c		3,20,000	By Interest on Fixed Deposit A/c		42,000
To Depreciation A/c		95,000			
To Interest paid to Vendor (purchase consideration paid (01/08/14)		35,000			
To Debenture Interest A/c		6,000			
To Preliminary Exp. A/c		4,000			
To Net Profit c/d		3,24,000			
		18,72,000			18,72,000

Additional Information:

1) Goods are sold on the following terms and conditions.

   a) At catalogue price at cash counter which is cost plus 100%.

   b) At catalogue price less 6.25% to retailers.

   c) At catalogue price less 20% to wholesalers.

   d) At catalogue price less 25% for exports.

2) TR & Co. sold goods through following channels only.

   a) At cash counter and retailers. However, Murali Ltd. discontinued the cash counter sale and retail, sale from the date of its Incorporation and decided to expand the Market through wholesalers and exports sales only.

3) Office Rent was Rs.10,000/- p.m. upto 31/08/14 and thereafter it increased by 20%. Balance Rent was for additional space acquired by the directors.

4) Average monthly administrative expenses doubted from date of Incorporation.

5) Depreciation includes Rs.5,000/- on the plant acquired in the post Incorporation period and Rs.15,000/- on plant which was transferred on 31st May 14 sister company.

6) Selling Expenses relates to export sales only.

7) Interest received on Fixed Deposits was from 1st April, 14.

Apportion the Profit between pre-Incorporation and post Incorporation period.

Solution:

Murali Ltd.
Profit and Loss Account for the period ended 31st March 15

Dr. Cr.

Particulars	Basis	Pre	Post	Particulars	Basis	Pre	Post
To Administrative Expenses A/c	WN6	12,000	66,000	By Gross Profit c/d	WN4	3,80,000	4,40,000
To Selling Expenses A/c	Post	-	10,000	By Share transfer Fees A/c	Post	-	10,000
To Office Rent A/c	WN5	40,000	2,80,000				
To Depreciation A/c	WN7	32,000	63,000	By Interest on Fixed Deposit A/c	WN9	3,500	38,500
To Interest to vendor A/c	WN8	20,000	15,000				
To Debenture Int.A/c	Post	-	6,000				
To Preliminary Expenses A/c	Post	-	4,000				
To Capital Reserve A/c	-	2,79,500	-				
To Net Profit c/d	-	-	44,500				
		50,000	1,81,000			50,000	1,81,000

Working Notes:

1) Time Ratio = 4:11

Date of Acquisition	Date of Incorporation	Year end
01/01/14	01/05/14	31/03/15

Pre Incorporation 4 months — Post Incorporation 11 months

Time Ratio = 4:11

2) Let the cost price be Rs.100/-
   $\therefore$ Cost counter price = 100 + 100 = Rs.200/- per unit
   a) Catalogue Price = Rs.200/-
   b) Retail Price = 200 – 6.25% = Rs.187.50
   c) Wholesale Price = 200 – 20% = Rs.160/-
   d) Export Price = 200 – 25% = Rs.150/-

3) Gross Profit Ratio = $\dfrac{\text{Gross Profit}}{\text{Sales}}$
   S.P. (–) Cost = Gross Profit

	Gross Profit	G.P. Ratio= $\left(\frac{S.P.}{Sales}\right)$
Cash counter price	200 – 100 = 100	$\frac{100}{200}$
Retail Sales	187.50 – 100 = 87.50	$\frac{87.50}{187.50}$
Wholesale	160 – 100 = 60	$\frac{60}{160}$
Export Sale	150 – 100 = 50	$\frac{50}{150}$

4) Gross Profits

	Pre	Post
a) On case counter sales 3,40,000 X $\frac{100}{200}$	1,70,000	-
b) Retail Sales 2,40,000 X $\frac{87.50}{100}$	2,10,000	-
c) Wholesales 6,40,000 X $\frac{60}{160}$	-	2,40,000
d) Export Sales 6,00,000 X $\frac{50}{150}$	-	2,00,000
Total Gross Profit	3,80,000	4,40,000

Gross Profit = Sales (–) Cost of Goods Sold
= 18,20,000 (–) 10,00,000
= 8,20,000

5) Office Rent Rs.3,20,000/-

	Pre	Post
a) From 01/01/14 to 30/04/14 = 10,000 X 4 =	40,000	-
b) From 01/05/14 to 31/08/14 = 10,000 X 4 =	-	40,000
c) From 01/09/14 to 31/03/15 = 12,000 X 7 =	-	84,000
d) For Addition Space taken by directors = Post Incorporation [3,20,000 – (40,000 + 40,000 + 84,000)] = Rs.1,56,000/-	-	1,56,000
Total Rent	40,000	2,80,000

6)

Monthly Administrative Expenses were doubled from date of incorporation	Pre	Post
No. of Months	4	11
It was doubled from date of Incorporation	X 1	X 2
	4	22

Administrative Expenses Ratio = 4:22

Pre-incorporation = 78,000 X $\frac{4}{26}$ = Rs.12,000

Post-incorporation = 78,000 X $\frac{22}{26}$ = Rs.66,000

Rs.78,000

7) Depreciation: Rs.95,000/-

	Pre	Post
a) On Assets acquired in post period	-	5,000
b) On Assets transferred used 01/01/14 to 31/05/14 (5 months) pre $\frac{15000}{5}\times 4$ post $\frac{15000}{5}\times 1$	12,000	3,000
c) Balance Depreciation (95,000 – 20,000) = 75,000 in Time Ratio 4:11	20,000	55,000
	32,000	63,000

8) Interest paid to vendor Rs.35,000/- (from 01/01/14 to 01/08/14) = 7 months

Pre-Incorporation = $\frac{35,000}{7}\times 4$ Rs.20,000

Post-Incorporation = $\frac{35,000}{7}\times 3$ Rs.15,000

Rs.35,000

9) Interest received on fixed deposit from 1st April 14 to 31st March 15 (12 months)

Pre-Incorporation April 14 only one month $\left(\frac{42,000}{12}\times 1\right)$ 3,500

Post-Incorporation 1st May 14 to 31st March 15 (11 months) 38,500

Total Rs. 42,000

Illustration: 7 (Calculation of Sales commission on a provision for taxations)

The N.C. Ltd. was registered on 1st Julyl 2014 to take over business of C.N. & Sons from 1st April 2014. From the following information calculate the Profit earned by the company in pre and post incorporation period.

1) Sales during year ended 31st March 2015 amounted to Rs.7,20,000/- sales for the month of April, May14, January February and march 15 were half the monthly sales in each of remaining month.
2) Cost of goods sold Rs.2,20,000/-.
3) Rent and Taxes Rs.30,000/-.
4) Bad debts Rs.5,000/-.
5) Salaries (There are four employees in the Pre-Incorporation period and six employees in Post-Incorporation period) Rs.22,000/-.
6) Interest on purchase consideration (purchase consideration was paid on 1st September 14) Rs.30,000/-.
7) Partner's Remuneration Rs.11,000/-.
8) M.D. Remuneration Rs.40,000/-.
9) Commission sales paid 2% of sales upto Incorporation, then after in post-Incorporation 5% on sales.
10) Provision for Taxation @ 30% for entire period.
11) Donation given by the company Rs.11,000/-.
12) Preliminary Expenses amounted to Rs.15,000/-, agreed to be written off over five years.

Solution :

Profit & Loss Account for the year ended 31st March 2015

Dr. Cr.

Particulars	Basis	Pre	Post	Particulars	Basis	Pre	Post
To Rent & Taxes A/c	TR	7,500	22,500	By Gross Profit c/d	SR	1,20,000	4,80,000
To Bad debts A/c	SR	1,000	4,000				
To Salaries A/c	WN4	4,000	18,000				
To Interest to vendors A/c	WN5	18,000	12,000				
To Partners Remuneration A/c	Pre	11,000	-				
To M.D.							

Remuneration A/c	Post	-	40,000				
To Sales Commission A/c	WN6	2,880	28,800				
To Donation A/c	Post	-	11,000				
To Preliminary Expenses w/off	Post	-	2,250				
To Provision for Taxation A/c	WN8	22,686	1,02,435				
To Capital Reserve A/c	-	52934	-				
To Net Profit c/d	-	-	2,39,015				
		1,20,000	4,80,000			1,20,000	4,80,000

Working Note :

1) Time Ratio = 1:3

Date of Purchase 01/04/08 | Date of Incorporation 01/07/08 | Year end 31/03/15

Pre Incorporation 3 months | Post Incorporation 9 months

Time Ratio = 1:3

2) Sales each of month January, February, November and December 2008 were half, for remaining each of monthly sales.

Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar
0.5	0.5	1	1	1	1	1	1	1	1	0.5	0.5
Pre			Post								
2			8								

∴ Sales Ratio = 1:4

3) Gross Profit = Sales (-) Cost of goods sold
= 7,20,000 (-) 2,20,000
= 6,00,000

4) Salaries Rs.22,000/-. There are four employees in Pre-Incorporation period and six employees Post-Incorporation.

	Pre	Post
No. of months X No. of employees	3 X 4	9 X 6
	12	54

$\therefore$ Ratio = 2:9

Pre-Incorporation = 22,000 X $\frac{2}{11}$ = Rs.4,000

Post-Incorporation = 22,000 X $\frac{9}{11}$ = Rs.18,000

Total Salaries Rs.22,000

5) Interest on purchase consideration, Rs.30,000/- paid for the period from 1st January 08 to 1st June 08, for 5 months.

   Pre = April + May + June = 3 months = $\frac{30,000}{5}$ X 3 = Rs.18,000

   Post =July + August = 2 months = $\frac{30,000}{5}$ X 2 = Rs.12,000

6) Commission on sales 2% in Pre-Incorporation and 5% on Post-Incorporation sales
   Pre-Incorporation sales commission
   = 7,20,000 X $\frac{1}{5}$ = Rs.1,44,000 X 2% = 2,880
   Post-Incorporation sales commission
   = 7,20,000 X $\frac{4}{5}$ = Rs.5,76,000 X 5% = 28,800

7) Preliminary Expenses to be w/off over 5 years
   = $\frac{15,000}{5}$ X $\frac{9}{12}$ (post months) = Rs.2,250/-, balance preliminary expenses should shown in Balance sheet.

8) Provision for Taxation @ 30%

	Pre		Post
Gross Profit Less : Total Expenses	1,20,000 (44,380)		4,80,000 (1,38,550)
N.P.B.T. Less : Tax @ 30%	75,620 (22,686)		3,41,450 (1,02,435)
Capital Reserve	52,934	N.P.	2,39,015

Illustration: 8 (Typical – Payment to vendor in installments same books of Accounts continued)

Trial balance of A Ltd. as on 31.03.15

Particulars	Debit (Rs.)	Credit (Rs.)

Opening Stock	50,000	-
Purchase / Sales	6,00,000	7,50,000
Wages	25,000	
Carriage	30,000	
Salaries	24,000	
Rent	18,000	
Capital TR & Co.		5,00,000
10% Bank Loan (1st Jan 15)		1,00,000
Printing & Stationery	6,000	
Debtors / Creditors	50,000	40,000
Bad debts	10,000	
Audit Fees	10,000	
Sundry Expenses	4,000	
Plant & Machinery	2,00,000	
Land & Building	3,00,000	
Bank Balance	5,000	
Furniture & Fixture	58,000	
	13,90,000	13,90,000

Additional Information:

1) A Ltd. was incorporated on 1st Oct 2014 to take over business of TR & Co. as from 01.07.14. No entries relating to transfer of the business were entered in the books which were carried on without a break until 31st March 2015.

2) Purchase consideration agreed Rs.6,00,000/- and discharged as under :

   a) 10,000 9% Preference shares of Rs.10/- each @ Rs.12/-.

   b) Rs.3,00,000/- 12% Debenture issued at 5% discount.

   c) Bal in Equity share of Rs.5/- each, at par. Shares were allotted on 1st October 2014 where as Debentures were allotted on 1st January 2015. Provide interest on Purchase Consideration @ 12% p.a.

3) Monthly sales were doubled from 1st January 2015.

4) Salary includes salary of company's secretary appointed on 1st October2014 Rs.6,000/- & balance salary includes salary of manager Rs.1,000/- per month who resigned on 1st November 14.

5) Bad debts includes Rs.8,000/- written off on 1st October 14.

6) Preliminary Exp. Amounted to Rs.12,000/- paid by directors, yet not accounted is to be written off over period of 5 years.

7) Gross Profit was 20% of sales throughout period.

8) Depreciate Land & Building by 6% p.a. & Plant & Machinery 15% p.a.

Solution:

Trading Account for the period ended on 31st March 2015

Dr. Cr.

Particulars	Rs.	Particulars	Rs.
To Opening Stock	50,000	By Sales	7,50,000
To Purchases	6,00,000	By Closing Stock (Bal. fig)	1,05,000
To Wages	25,000		
To Carriage	30,000		
To Gross Profit (20% on Sales)	1,50,000		
	8,55,000		8,55,000

Profit & Loss Accounts for the year ended 31st March 2015

Dr. Cr.

Particulars	Basis	Pre	Post	Particulars	Basis	Pre	Post
To Salary A/c	WN	7,667	16,000	By Gross Profit			
To Rent A/c	TR	6,000	12,000	b/d	SR	37,500	1,12,500
To Bank Interest A/c		-	2,500	by Goodwill A/c	-	20,833	-
To Printing & Stationery A/c	TR	2,000	4,000				
To Bad Debts (Actual)		8,000	2,000				
To Audit Fees A/c	TR	3,333	6,667				
To Sundry Expenses A/c	TR	1,333	2,667				
To Interest payable vendor A/c	WN	18,000	8,550				
To Debenture Int.A/c		-	9,000				
To Preliminary Exp. w/off A/c	WN	-	1,200				
To Depreciation on Land & Building	TR	4,500	9,000				

A/c To Depreciation on Plant & Machinery A/c To Net Profit c/d	TR	7,500 -	15,000 23,583				
		58,333	1,12,500			58,333	1,12,500

Revised Schedule VI format

A Co. Ltd.
Profit and Loss statement for the year ended 31st March 2015

	Particulars	Notes	Pre	Post
I.	Gross Profit	11	37,500	112,500
	Goodwill		20833	.--
II.	**Total Revenue**		58,333	112,500
III.	<u>Expenses:</u>			
	<u>Purchase of Stock in Trade</u>			
	Employee Benefit Expenses	12	7,667	16,333
	Finance Cost	13	18,000	20,050
	Depreciation and amortization expense	14	12,000	24,000
	Other Expenses	15	20,666	28,534
	Total expenses		**58,333**	**88,917**
IV.	**Profit before tax (II- III)**		-	23,583
V	Provision for tax for current year			
VI	**Profit for the period from the period**		-	23,583

BALANCE SHEET AS AT 31ST MARCH 2015

(Amount in `)

		Particulars	Notes	As on 31 March, 2012
I	**EQUITY AND LIABILITIES**			
1	**Shareholders' funds**			
	(a)	Share capital	1	295,000
	(b)	Reserves and surplus	2	43,583

2	**Non Current liabilities**				
	(a)	Long-term borrowings			
		12% Debentures		3	400,000
3	**Current liabilities**				
	(a)	Trade Payables		4	40,000
	(c)	Other current liabilities		5	11,500
	(d)	Short-term provisions		6	38,550
			TOTAL		**828,633**
II	**ASSETS**				
1	**Non-current assets**				
	(a)	<u>Fixed assets</u>			
		<u>Tangible assets</u>			
		Land and Building			286,500
		Furniture & Fixtures			58,000
		Plant and Machinery			177,500
	(b)	<u>Intangible assets</u>			
		Goodwill			120,833
2	**Current assets**				
	(a)	Inventories		7	105,000
	(b)	Trade receivables		8	50,000
	(c)	Cash and cash equivalents		9	5,000
	(e)	Other current assets		10	25,800
			TOTAL		**828,633**

Notes to Financial Statements for the year ended 31 March, 2015

		As at 31 March 2015	
		Number	`
Note "1" : SHARE CAPITAL	-		
Authorised Shares	-		
39000 Equity Shares of 10 each		39,000	195,000
10000 10% Pref. Shares of Rs.10 each		10,000	100,000
Issued, Subscribed & Fully Paid up Shares	-		
39000 Equity Shares of 10 each		39,000	195,000

10000 10% Pref. Shares of Rs.10 each		10,000	100,000
Total		**49,000**	**295,000**

Note "2" : RESERVES & SURPLUS -	**As at 31 March 2015**
-	`
Surplus	
Reserves & Surplus	
Net Profit For the current year	23,583
Securities Premium	20,000
Total	**43,583**

Note "3" : LONG TERM BORROWINGS	**As at 31 March 2015**
12% Debentures -	300,000
10% Bank Loan	100,000
Total	**400,000**

Note "4" : TRADE PAYABLES	As at 31 March 2015
	`
(a) Trade Payables	
Creditors	40,000
Total	**40,000**
Note "5" : OTHER CURRENT LIABILITIES	**As at 31 March 2015**
Debenture Interest	9,000
Interest on Bank Loan	2,500
Total	**11,500**
Note "6" : SHORT-TERM PROVISIONS	**As at 31 March 2015**
	`
(a) Others	
Interst payable to vendor	26,550
Preliminary Expenses payable	12,000
Total	**38,550**
Note "7" : INVENTORIES	**As at 31 March 2015**
Stock - in - Trade	105,000
Total	**105,000**
Note "8" : TRADE RECEIVABLES	**As at 31 March 2015**
Trade receivables outstanding for a period exceeding six months	
Debtors	50,000
Total	**50,000**
Note "9" : CASH & BANK BALANCES	**As at 31 March 2015**
a. Balances with banks	5,000
Total	**5,000**

Note "10" : OTHER CURRENT ASSETS -	As at 31 March 2015
Preliminary Expenses	15,000
Less- /5th written off	1,200
	10,800
Discount on issue of Debentures	15,000
Total	**25,800**

Note "11" : REVENUE FROM OPERATIONS	Basis	As at 31 March 2015	
		Pre	**Post**
- **Gross Profit**	- SR	37,500	112,500
Total		37,500	112,500

Note "12" : EMPLOYEE BENEFIT EXPENSES	Basis	As at 31 March 2015	
		Pre	**Post**
- Salary	- Post	7,667	16,333
Total		7,667	16,333

Note "13" : FINANCE COST	Basis	As at 31 March 2015	
		Pre	**Post**
Debenture Interest	Post	--	9,000
Bank Interest	Post		2,500
Interest payable vendor		18,000	8,550
Total		18,000	20,050

Note "14" : DEPRECIATION & AMORTIZATION EXPENSES	Basis	As at 31 March 2015	
		Pre	**Post**
Depreciation on Tangible Assets	-		
Land Building	TR	4,500	9,000
Plant & Machinery	TR	7,500	15,000
Total		12,000	24,000

Note "15" : OTHER EXPENSES	Basis	As at 31 March 2015	
		Pre	Post
Rent	TR	6,000	12,000
Printing & Stationery	SR	2000	4000
Audit Fees	TR	3333	6667
Bad Debts		8,000	2,000
Sundry Expenses	TR	1,333	2,667
Preliminary Exps			1,200
Total		20,666	28,534

Working Notes:

1)

TR & Co. Capital A/c

Dr. Cr.

Particulars	Rs.	Particulars	Rs.
To 9% Preference Share Capital A/c	1,00,000	By Bal b/d (as per trial balance)	5,00,000
To Debentures A/c	2,85,000	By Goodwill (Bal fig.)	1,00,000
To Equity Share Capital A/c	1,95,000		
To Securities Premium A/c	20,000		
	6,00,000		6,00,000

2) Time Ratio

Date of take over	Date of Incorporation	Year end
01/07/14	01/10/14	31/03/15

Pre Incorporation 3 months | Post Incorporation 6 months

∴ Time Ratio = 1:2

3) Sales Ratio

July	Aug	Sep	Oct	Nov	Dec	Jan	Feb	March
1	1	1	1	1	1	2	2	2
Pre			Post					
3			9					

∴ Sales Ratio = 1:3

4) Salary Rs.24,000/-

	Pre	Post
Salary to Secretary	-	6,000
Salary to Manager	3,000	1,000
(1,000 per month upto 30th Sep 2014)		
Other Salary (Bal. Rs.14,000/- in TR)	4,667	9,333
	7,667	16,333

5) Purchase Consideration

	Rs.	Rs.
9% Preference share Capital	1,00,000	
(+) Premium @ Rs.2/- per share	20,000	1,20,000
12% Debentures	3,00,000	
(-) 5% Discount on issue	(15,000)	2,85,000
Bal. in Equity shares of Rs.5/- each		1,95,000
$\frac{1,95,000}{5}$ = 39,000 Equity shares of Rs.5 each		
Purchase Consideration		6,00,000

Capital A/c ………………………………..Dr. 6,00,000
Discount on issue of Debentures A/c ….Dr. 15,000
To 9% Preference Share Capital A/c 1,00,000
To Securities Premium A/c 20,000
To Equity Share Capital A/c 1,95,000
To 12% Debentures A/c 3,00,000

Preliminary Expenses w/off
Over 5 years from 1st October 14 onwards

$= 12,000 \times \frac{1}{5} \times \frac{6}{12}$

= Rs.1,200/-

Interest on Purchase Consideration

	Pre	Post
a) On Shares allotted on 1st October 14 from 01.07.14 to 01.10.14 (Pre) $3{,}15{,}000 \text{ X } 12\% \text{ X } \frac{3}{12}$	9,450	-
b) For balance Purchase Consideration, by allotting Debentures on 01.01.15 Pre = From 01.07.14 to 30.09.14 = 3 months Post = From 1st Oct14 to 31st Dec.14 = 3 months $2{,}85{,}000 \text{ X } 12\% \text{ X } \frac{6}{12}$	8,550	8,550
Total Interest	18,000	8,550

Outstanding Interest payable to vendor Rs.26,550/-

Illustration: 9 (Division of Trading Account and P&L A/c)

The Dil Ltd. was incorporated on 1st September 14 to acquire the business of M/s. Top & Son, with effect from 1st April 14. The accounts were maintained as usual up to 31st March, 2015, on which date the following balances were extracted from the books.

Particulars	Debit (Rs.)
Purchase (up to 31st August 14, Rs.45,000/-)	1,35,000
Sales (up to 31st August 14, Rs.1,20,000/-)	4,80,000
Stock as on 1st April 2014	50,000
Carriage Inwards (2% on Purchase)	2,700
Rent	15,000
Formation Expenses	6,000
General Expenses	18,000
Plant & Machinery	60,000
Sundry Debtors	40,000
Sundry Creditors	25,000
Carriage Outwards (2.5% on Sales)	10,000
Bills Receivable	22,000
Bills Payable	5,000
Interest on Purchase Consideration (up to 01/11/14)	21,000
Cash at Bank	9,000
Capital A/c of Top & Sons	90,000
Directors Fees	6,000
Land and Building	2,20,000
General Reserve (31.03.14)	14,700

Additional Addition:

1) Closing stock as on 31st August 14 and 31st March 15 was valued at Rs.60,000/- and Rs.1,10,000/- respectively.
2) Depreciation on Land & Building 5% p.a. and plant and machinery @ 20% p.a.
3) Rent upto 31st January 15 was Rs.1,000/- p.m., it was increased to 1,200 p.m. from 1st February 15, Rent includes advance paid to landlord.
4) Manger Salary at Rs.2,000/- p.m. is payable. The manager became a director on formation of the company. His remuneration as director is included in director's fees.
5) The Purchase Consideration was agreed at Rs.2,14,700/-, was satisfied on 01/11/14, by issue of 1,000 Equity shares of Rs.10/- each @ Rs.15/- per share and balance in 12% Debenture of Rs.100/- each at par.
6) Provide Income tax @ 40%.
7) Director's proposed Equity dividend @ 20%.

Prepare Final Accounts of the DIL Ltd. showing in Profit in the pre and post Incorporation periods after writing off 1/6 of formation expenses.

Solution :

Trading Account for the ended 31st March 2015

Dr. Cr.

Particulars	Pre	Post	Particulars	Pre	Post
To Opening Stock A/c	50,000	60,000	By Sales	1,20,000	3,60,000
To Purchases A/c	45,000	90,000	By Closing Stock A/c	60,000	1,10,000
To Carriage Inward A/c (2% on Purchase)	900	1,800			
To Gross Profit c/d (Bal figure)	84,100	3,18,200			
	1,80,000	4,70,000		1,80,000	4,70,000

Profit & Loss Accounts for the year ended 31st March 2015

Dr. Cr.

Particulars	Basis	Pre	Post	Particulars	Basis	Pre	Post
To Rent A/c	WN3	5,000	7,400	By Gross Profit b/d		84,100	3,18,200
To General Exp. A/c	TR	7,500	10,500				
To Carriage Outwards A/c	WN	3,000	9,000				
To Formation Exp. A/c		-	1,000				
To Interest paid to vendor A/c	WN6	15,000	6,000				
To Director's Fees A/c	Post	-	6,000				
To Depreciation A/c							
On Land & Build.	TR	4,583	6,417				
On Plant & Mach.	TR	5,000	7,000				
To Manager's Salary A/c	Pre	10,000	-				
To Debenture Int.A/c	Post	-	3,235				
To Provision for Taxation A/c	WN8	13,607	1,04,659				
To Capital Reserve A/c		20,410	-				
To Net Profit c/d		-	1,56,989				
		84,100	3,18,200			84,100	3,18,200

Profit & Loss Appropriation A/c

Dr. **Cr.**

Particulars	Rs.	Particulars	Rs.
To Proposed Dividend A/c	20,000	By Net Profit b/d	1,56,984
To Surplus Carried to Balance sheet	1,36,989		
	1,56,989		1,56,989

Revised Schedule VI format

Profit & Loss A/c. of DIL Ltd.

Particulars	Note	Amount	Amount
Income			
Revenue from Operations			4,02,300
Expenditure			
Employee Benefit Expenses	3	16,000	
Finance Cost	4	1,43,501	
Other Expenses	5	65,400	(2,24,901)
			177399

Balance Sheet of DIL Ltd. as on 31-03-2015

Particulars	Note	Amount	Amount
EQUITY AND LIABILITIES			
1. Shareholder's Funds			
a. Share Capital	1		1,00,000
b. Reserves and Surplus	2		2,07,399
2. Non-Current Liabilities			
Long Term Borrowings			
12% Debentures			64,700
3. Current Liabilities			
Trade Payables			30,000
Other Current Liabilities			15,235
Short Term Provisions			1,38,266
Total			**5,55,600**
ASSETS			
1. Non Current Assets			
a. Fixed Assets			
- Tangible Assets			
- Intangible Assets			
4. Current Assets			2,57,000
a. Cash and cash			1,10,000
equivalents		9000	
b. Trade Receivables		62000	
c. Inventory		110000	1,81,000
5. Short Term Loans and Advces			2,600
5. Other Current Assets			5,600
Total			**5,55,600**

Dil Ltd.		
Notes to Financial Statements for the year ended 31-03-2015		
	As at 31-03-2015	
	Number	**Rs**
Note "1" : SHARE CAPITAL		
Authorised Shares		
Equity Shares of `10 each	10000	1,00,000
Issued, Subscribed & Fully Paid up Shares		
Equity Shares of `10 each	10000	1,00,000
Total	**10000**	**1,00,000**

		Rs
Note "2" : RESERVES & SURPLUS		
Capital Reserves		20410
Security Premium		50000
Profit & Loss A/c		136989
Total		**207399**
	As at 31-03-2015	
	Basis	**Rs**
Note "3" : EMPLOYEE BENEFIT EXPS.		
Directors Fees	Post	6000
Managers Salary A/c.	pre	10000
Total		**16000**
	As at 31-03-2015	
	Basis	**Rs**
Note "4" : FINANCE COST		
Formation Exps.		1000
Interest Paid to Vendor		21000
Provision for Tax		118266
Debenture Interest A/c.	Post	3235
Total		**143501**

	As at 31-03-2015	
	Basis	**Rs**
Note "5" : OTHER EXPS.		
Rent A/c.		12400
General Exps.	TR	18000
Carriage Outwards		12000
Depreciation	TR	
Land and Building		11000
Plant and Machinery		12000
Total		**65400**

Working Notes:

1) Time Ratio

Date of take over	Date of Incorporation	Year end
01/04/14	01/09/14	31/03/15

$$\underbrace{01/04/14 \quad 01/09/14}_{\text{Pre Incorporation 5 months}} \quad \underbrace{01/09/14 \quad 31/03/15}_{\text{Post Incorporation 7 months}}$$

∴ Time Ratio = 5:7

2) Sales Ratio

Pre = Rs.1,20,000

Post	Rs.4,80,000
	Rs.1,20,000
	Rs.3,60,000

∴ Sales Ratio = 1:3

3) Rent Rs.15,000/-

	Pre	Post
a) From 01.04.08 to 31.08.08 (1,000X5)	5,000	-
b) The month Sept., Oct, Nov, Dec 14 Jan 15	-	5,000
c) For February, March 15 1200X2	-	2,400
Total Rent	5,000	7,400

Rent Deposit = 15,000 – (5,000 + 7,400) = 2,600

4) Carriage Outwards 2.5% of Sales

Pre = 1,20,000 X 2.5% =	3,000
Post = 3,60,000 X 2.5% =	9,000
Total	12,000
Less : Paid	(10,000)
Outstanding	2,000

5) Interest paid to vendor Rs.21,000/- for period 1st April 14 to 1st November 14 = 7 months out of which 5 months are pre & balance post.

Pre = $\frac{21,000}{7}$ X 5 = Rs.15,000

Post = 21,000 (-) 15,000 = Rs.6,000

6) Debenture Interest = 64,700 X 12% X $\frac{5}{12}$ = Rs.3,235/-

7) Goodwill

	Rs.
Top a son Capital Balance	90,000
Add : General Reserve Balance	14,700
Final Capital Balance	1,04,700
Add : Goodwill (Balancing figure)	1,10,000
Purchase Consideration	2,14,700

8) Provision for Tax

	Pre	Post
Profit & Loss Credit balance	84,100	3,18,200
Less : P&L A/c Dr. Exp.	(50,083)	(56,552)
N.P.B.T.	34,017	2,61,648
Less : Income Tax 40%	13,607	(1,04,659)
Profit after Tax	20,410	1,56,989

9) Closing stock as on 31st September 14 is opening stock for the post period.

14.2 KEY POINTS / KEY TERMS:

1) **Incorporation:** Date of Registration i.e. date on which company comes in existence.
2) **Pre-Incorporation:** Period from date of acquisition to date of Incorporation.
3) **Post-Incorporation:** Period from Incorporation to year end.
4) **Sales Ratio :** Ratio between sales of pre and post Incorporation it is used for dividing Gross Profit and Variable Expenses, Selling and Distribution Expenses.
5) **Time Ratio:** Ratio indication period of pre-Incorporation & post-Incorporation time. It is used to divide Fixed Expenses, Administrative Expenses.
6) **Interest paid to Vendor:** Interest is paid from date of acquisition to payment of purchase consideration, it should be divided considering actual period.
7) **Purchase Consideration:** It is the amount agreed to be paid to vendor for taking over business.
8) **Pre-Incorporation Profit:** Transfer to Capital Reserve
9) **Pre-Acquisition Loss:** Transfer to Goodwill
10) **Goodwill:** Excess of Purchase consideration over net assets taken over (Capital of vendor)

14.3 EXCERCISES:

14.3.1 THEORY QUESTIONS:

1) What is pre-Incorporation Profit?
2) What are different methods of ascertaining Pre-Incorporation Profit?

3) What are different bases of Allocation of Income / Expenses?

4) How would you treat Pre-Incorporation losses in Accounts?

14.3.2 OBJECTIVE TYPE QUESTIONS

- **Fill in the blanks :**

1) Interest on Debentures is ___________ expenditure.
2) Gross Profit are divided in the ratio of ___________ .
3) Interest paid to vendor is ___________ expenditure.
4) Share transferred fees received is ___________ Income.
5) Goodwill written off is charged to ___________ .
6) Audit fees are divided in the ratio of ___________ .
7) Fixed expenses are divided in the ratio of ___________ .
8) Depreciation on asset purchased after incorporation is charged to ___________ .
9) Managing directors renunciation charged to ___________ .
10) Interest on vendor's capital is charged ___________ period.
11) The provision for Income tax is allocated in the ratio of ___________ .
12) The pre-incorporation period loss considered as ___________ .
13) Vendor's salary is charged to ___________ period.
14) The fixed expenditure allocated in the ratio of ___________ .
15) Post-incorporation profit is transferred to ___________ .

- **Multiple Choice Questions :**

1) Profit post incorporation are available for ___________ .
   a) Acquisition of fixed asset b) Debenture interest
   c) Payment of dividend d) For drawing by owner

2) Share issue expenses written off should be charged to ___________ .
   a) Trading Account b) Liabilities
   c) Post incorporation Profit d) None of these

3) Goodwill written off is charged to ___________ .
   a) Current Liabilities b) Floating Assets
   c) Capital Account (share) d) None of these

4) Discount allowed to Customers by a limited company is charged to ___________ .
   a) Pre-incorporation period b) Post-incorporation period
   c) Post acquisition period d) None of these

5) Profit upto date of incorporation is ___________ .
   a) Capital Reserve b) Capital Profit
   c) Security Premium d) Revenue Reserve

6) Expenses exclusively relating to vendor should be charged to ___________ period.
   a) Pre-incorporation b) Post acquisition period
   c) Post-incorporation d) Both

7) The excess of purchased consideration over net assets taken over is debited to ___________ .
   a) Fixed Assets b) Goodwill
   c) Capital Reserve d) None of above

8) The date of taken over 1st January 2008, incorporation 1st June 08 year end – 31st December 2008. Time ratio is ___________ .
   a) 5:1 b) 2:5
   c) 1:6 d) None of these

9) Sales for the year Rs.15 Lakhs pre acquisition sales Rs.3 Lakhs, pre-incorporation Rs.2 Lakhs, Balance post-incorporation. The sales Ratio is ___________ .
   a) 4:1 b) 3:5
   c) 1:6 d) None of these

10) Purchased Consideration Rs.60,000/- net assets taken over Rs.45,000/-. The value of goodwill is ___________ .
   a) Rs.25,000/- b) Rs.45,000/-
   c) Rs.15,000/- d) Rs.60,000/-

- **Match the Column :**

1)

Group "A"	**Group "B"**
i) Pre acquisition Loss	a) Post incorporation
ii) Company related expenses	b) Goodwill
iii) Asset	c) Belongs to vendor
iv) Salaries	d) In Time Ratio
	e) In Sales Ratio

2)

Group "A"	**Group "B"**
i) M. D. Salaries	a) Note to Balance sheet
ii) Contingent Liabilities	b) No Allocations
iii) Share Capital	c) Post incorporation
iv) Purchase Consideration	d) Net Assets taken over

3)

Group "A"	Group "B"
i) Audit Fees ii) Depreciation on Assets Purchased iii) Gross Profit iv) Pre-incorporation Loss	a) Time Ratio b) Sales Ratio c) Post-incorporation d) Goodwill e) Sales Less Cost of Sales

4)

Group "A"	Group "B"
i) Pre-incorporation Profit ii) Net Profit upto pre-incorporation period iii) Dividing point for ascertaining pre / post incorporation period iv) Rent v) Gross Loss	a) Belongs to vendor b) Date of incorporation c) Sales Ratio d) Capital Reserve e) Time Ratio

- **State whether True / False**

1) The Profit made on acquisition is debited to General Reserve.
2) Profit after incorporation is post acquisition.
3) Discount on issue of Debenture is charged to pre acquisition period.
4) Advertisement expense is allocated on the basis of Sales.
5) Depreciation on fixed asset taken over by vendor is charged to post incorporation period.
6) Debenture Interest is debited to post incorporation.
7) Pre acquisition Profit belongs to vendor.
8) Interest paid on purchased consideration is allocated in Sales Ratio of pre incorporation & post incorporation period.
9) Business Commencement Certificate date should be considered for allocation of expenses.
10) Provision for Sales Tax is allocated in the ratio between pre acquisition & pre incorporation period.
11) The partner's salary before acquisition should be allocated to both the period in Sales ratio.
12) Bad debts realized should be debited to pre incorporation period.
13) The corporate expenses should be debited to post acquisition period.

14) The advertisement under the contract Rs.1,000/- month should be divided between pre & post incorporation period in Sales ratio.

15) The Gross Profit should be divided pre & post incorporation period in Sales ratio.

14.3.3 PRACTICAL QUESTIONS:

Example: 1

Sonu Ltd. was incorporated on 01-07-2014 to take over the business of A.K. Enterprises as a going concern with effect from 01-04-2014. Their Profit and Loss Account for the year ended 31-03-2015 is as follows:

Dr. Cr.

Particulars	Rs.	Particulars	Rs.
To Opening Stock	75,000	By Sales (upto30-06-14 Rs.60,000/-)	3,00,000
To Purchases	1,00,000		
To Administration Exp.	12,000	By Closing Stock	46,500
To Director's Fees	4,000		
To Selling Expenses	20,000		
To Audit Fees	6,000		
To Preliminary Expenses	3,000		
To Net Profit	1,26,500		
	3,46,500		3,46,500

Prepare a statement showing the Profit earned prior to and after incorporation.

Example : 2

OT Ltd. was incorporated on 1st July, 2014 to take over the running business of Mr. R with effect from 1st April, 2014.
The following Profit & Loss Account for the year ended 31st March 15 was drawn up

Dr. **Cr.**

Particulars	Rs.	Particulars	Rs.
To Advertisement	10,600	By Gross Profit	2,00,000
To Managing Director's Remuneration	21,000	By Rent	5,000
		By Bad debts Realized	6,000
To Depreciation	4,000	By Income Tax Refund (2013-14)	4,300
To Salaries	18,000		

To Insurance	4,000		
To Preliminary Expenses	1,000		
To Rent and Taxes	6,000		
To Discount	700		
To Debenture Interest	40,000		
To Net Profit	1,10,000		
	2,11,000		2,11,000

The following details are available :

a) Average monthly turnover from October 2014 onwards was double than that of previous months.

b) Rent for the first four months was paid @ Rs.400/- per month and thereafter it is increased by Rs.50/- per month.

c) Bad debts realization of bad debts was in respect of bad debts written off during 2012.

d) Advertisement expenses were directly proportionate to the sales.

You are required to find out the Profit prior to Incorporation.

❖❖❖❖

10

VALUATION OF GOODWILL

Unit Structure:

2.1 Introduction
2.2 Valuation of Goodwill
2.3 Determination of Future Maintainable Profit: [FMP]
2.4 Normal Rate Return (NRR)
2.5 Capital Employed
2.6 Methods of Valuation of Goodwill
2.7 Methods of Valuation under Super Profit
2.8 Capitalization of Future Maintainable Profit (FMP) Method
2.9 Solved Problems
2.10 Exercise

OBJECTIVES

After studying the unit students will be able to:

- Understand the need of valuation of Goodwill.
- Determine the Future Maintainable Profit, Normal Rate Return and Capital Employed for valuation of Goodwill.
- Discuss about the methods of Valuation.
- Solve the related practical problems.

2.1 INTRODUCTION

The term 'Goodwill' is difficult to define and easy to explain. It is intangible fixed asset having a realizable value. It can be converted in to cash at time of Sale / change in the constitutions of earning business. Goodwill is smoothing which enables owners to attract customer towards the organization. It is also consider as "The present value of expected future earnings" in simple words it is the value of reputation of business, the business reputation for quality, punctuality, integrity and honesty. Financial soundness creates Goodwill. The existence of goodwill means the businessman has the excess earning attributable to operating tangible and intangible assets over and above the normal return earned by the firm in the same industry.

Kolher defines goodwill as "Current value of expected future income in excess of normal return on the investment in net tangible assets."

2.2 VALUATION OF GOODWILL

2.2.1 Characteristics of Goodwill

1. It is intangible or invisible assets.
2. It is not fixed. It is subject to fluctuation in value, due to internal as well as external factors.
3. It is not a fictitious asset in case of profitable concerns.
4. It cannot be detached from the other assets of business. Its valuation is attached to total value of the business. It cannot be valued in isolation.
5. It has value only on going concern basis.
6. Because of goodwill, a firm is able to earn excess profits than the other firms in the same class of industry.
7. The value of goodwill may defer due to the different methods of valuations used. No single valuation is arrived at by different velour's on account of complexity.
8. It is either created internally or purchased from outside.

2.2.2 Types of Goodwill

There are four types of goodwill as follows:

a) Local arising from locational advantages of business premises, e.g., chemist shop in or nearer by hospital.

b) Personal reputation of the individual as well as industrial house e.g. Bajaj, Tata's Ambani's etc.

c) Reputation of goods e.g. Brand name.

d) Absence of competition or existence of monopoly.

From the accounting point of view, Goodwill is categorized into two parts:

a) Purchased Goodwill:

Positive goodwill arises when business is acquired, when cost of acquisition exceeds the aggregate fair values of the identifiable net assets taken over.

Goodwill = Purchased Consideration - Net Assets taken over AS10, Accounting Standard 10 'Accounting for Fixed Assets' deals with the treatment of Goodwill. As per AS10, GOODWILL should be recorded in the books only when it is paid for it. As a matter of financial prudence goodwill is to be written off over a period of years at the earliest, as per AS26, not exceeding ten years. AS-14, Accounting for Amalgamations' prescribes the accounting treatment for Goodwill.

b) Inherent Goodwill:

Goodwill can be said to exist because there are many items of benefits to a business and value of it, cannot be included as an assets in the conventional accounts. As per, AS-26, Inherent Goodwill should not be recognized as an asset.

2.2.3 Need of Valuation

In case of partnership firm the necessity of valuing goodwill arises in connection with the following, whenever there is change in the constitution of the business and partnership deed when there is change in the profit-sharing ratio.

1. When a New Partner is Admitted
2. When a Partner Retires or Dies
3. When Firm is amalgamated with Another Firm.

In case of joint Stock Company the necessity of valuation arises in following circumstances:-

1) When the business of the company is taken over by another company, e.g. amalgamation, absorption, mergers.
2) When Stock Exchange Quotations not available, shares are to be valued for taxation purposes.
3) When large stock of shares of the company has to be brought of sold.
4) When management wants to write back goodwill, which was previously written off.
5) When company is taken over by government.

2.2.4 Factors affecting Value of Goodwill

The following are the main factors which affects value of Goodwill / Profitability:

The profitability of a firm is the main factor affecting value of Goodwill of business. The term profitability refers to profit which the business is expected to earn in future.

'Profit' is the most important single factor in respect of valuation of goodwill. One will never pay anything more than the amount which he would pay for purchasing same thing from another source this principle also applicable to Goodwill.

1. Normal Rate of Return: (N.R.R.):

The Term NRR means the rate of return that will satisfy an ordinary investor in the industry concern. NRR differs from industry to industry. It also depends upon business risk as well as financial risk in the business.

2. Capital Employed:

The value of goodwill not only depends upon the amount of F.M.P., but also depends on the amount of capital employed in the business to earn such profit. Other factors which also affect earnings & the value of goodwill:

a) Location
b) Time Factor
c) Nature of business
d) Efficient Management
e) Possibility of Competition
f) Government Policies
g) The Research and Development Efforts and truthful results thereof.
h) Brand Value
i) Competitions from Online Market.

All above factors can be totalize as under:

A firm may earn more profits than other firms in the industry because of numerous factors, some of which are stated below -

Sr. No.	Main Factor	Sub - Factors
1.	Managerial and Human Resource Factors	- Superior Managerial Team - Superb Organisation - Exclusive Training Programmes for Employees - Co-ordinal Labour Relationship - Discovery of Talent - Experienced Work Force

		- Long Standing Experience
2.	Product / Service Factors	- Secret or Patent Manufacturing - Establishing License to Trade - Exclusive know-how - Economies of Scale of Production - Foreign Collaboration - Quality and Reliability
3.	Marketing Factors	- Effective Advertisement - Market Dominance - Favorable attitude of Customers - Adequate Selling Outlets - Adequate Service Centers - Established List of Customers - Exclusive Selling Arrangements
4.	Physical Factors	- Strategic Location - Availability of raw material - Exclusive infrastructural Facilities - Adequate input availability like power, manpower etc.
5.	Fiscal Factors	- Cost Saving - Costs of Financing - Tax Exemptions / Deductions / Benefits - Good Credit Rating
6.	Other Factors	- Good Public Image - Favorable Governmental Regulations - Good Relationship with Suppliers

2.2.5 Limitations of Valuation of Goodwill

a) Valuation is art not science.

b) Valuation is relevant at the point of TIME of valuation.

c) Valuation changes according to various different methods of valuation.

d) Valuation varies from person to person depending on use.

e) Valuation is exercise, which is subjective and based on well-defined assumptions. Assumption may or may not be justifying / acceptable Bayer or Seller of Business.

2.3 DETERMINATION OF FUTURE MAINTAINABLE PROFIT: [FMP]

Determination of future maintainable Trading Profit under normal circumstances is most important & complicated task. FMP is subject to evolution of many factors such as capabilities of management, future Government policies, general & economical trend etc. For determining FMP, non-operating incomes & expenses are not to be considered. It is decided on the basis of average past Trading Profits subject to certain changes that have effect on future earnings of the business concerns.

The following steps are taken to arrive at FMP

1. Calculation of Past Average Earnings:

In Order to calculate FMP the profits of previous year can be considered, if necessary such business profit should be adjusted to make it acceptable for averaging. Such average profit may be simple average profit or weighted average profit.

a) Simple Average Profit = $\frac{\text{Total Profits}}{\text{No. of Years.}}$

Note: When Trading profits shows upward or downwards trend weighted average profits should be preferred.

2. Adjusted Average Profits:

Before finding out average profits, adjustments are to be made from particular year profits to get adjusted profit before Tax.

i) Material non-recurring items of expenses or income should be eliminated e.g. loss due to fire, profit on sale of Fixed assets, lump-sum compensation received for damage in legal action etc.

ii) Elimination of income / profit or loss from non-trading assets.

iii) Elimination of any capital profit or loss included in profits e.g. gain from sale of investments.

iv) Rectification of errors e.g. capital expenditure treated as Revenue expenditure & vice-versa, overvaluation of stock in trade.

After finding out adjusted profit following adjustments to be made from adjusted average profit [before tax]

i) Adjust any expenses or income likely to arise in future.

ii) Adjust past expenses or income not likely to arise in future.

iii) Ensure that adequate depreciation is provided on consistent basis.

Average adjusted profit should be work out, before tax.

Less: Income Tax

Average adjusted profit after Tax. [FMP]

FMP should be always after TAX. (in case tax rate / provision for taxation is given, then Tax should be ignored)

2.4 NORMAL RATE RETURN [NRR]

Normal Rate of Return is the rate of return that the invertors in general expect on their investment in the particular industry. This rate differs from industry to industry, from place to place, from time to time. It also depends upon Government decision, R. B. I. rate etc. NRR is required to be adjusted in certain cases / circumstances .e.g.

i) Risk attached to the business.

ii) Period of investment.

iii) Bank interest rates.

iv)

Boom or Slack Period in the Industry.

Normally NRR, is readily given in the problem, if not, it can be calculated from given information supplied. It can be calculated on the basis of dividend declared in the similar type of industries.

$$\text{N. R. R.} = \frac{\text{Dividend per share in similar type of company}}{\text{Market value per share in similar type of company}} \times 100$$

OR

N. R. R. = Average Rate of Dividend.

2.5 CAPITAL EMPLOYED

Goodwill of business also depends on the amount of capital employed. It is the present value of tangible trading assets minus all external liabilities. Non-trading assets such as investment in share should be excluded. Similarly intangible assets, such as goodwill, useless patents & trademarks should be excluded.

It is consider desirable to use average capital employed in place of capital employed since capital employed as calculated from Balance Sheet will be on certain date i.e. at the end of Year there for average capital employed is calculate.

a) Average Capital Employed (ACE):

Average Capital Employed (ACE) can be calculated as under:

$$\text{A, C. E.} = \frac{1}{2} \times \left[\underline{\text{Opening Capital} + \text{Capital}}\right]$$

OR

$$\text{ACE.} = \text{Opening Capital} + \frac{1}{2} \text{ of the net profit during the year,}$$

OR

ACE. = Closing Capital - $\frac{1}{2}$ of the net profit during the year.

Illustration: 1

A Ltd capital on 31st March,2013 was ₹6,00,000, earned ₹2,00,000 during the year & its closing capital was ₹8,00,000.

$$\text{A,C.E.} = \frac{1}{2} \times \left[\underline{\text{Opening Capital} + \text{Closing Capital}}\right]$$

$$= \frac{1}{2} \times [6{,}00{,}000 + 8{,}00{,}000]$$

$$= ₹7{,}00{,}000$$

OR

$$\text{ACE.} = \text{Opening Capital} + \frac{1}{2} \text{ of the net profit during the year,}$$

$$= 6{,}00{,}000 + \frac{1}{2} \times [2{,}00{,}000]$$

$$= ₹7{,}00{,}000$$

OR

ACE. = Closing Capital + $\frac{1}{2}$ of the net profit during the year,

$= 8{,}00{,}000 - \frac{1}{2}\,[2{,}00{,}000]$

= ₹7,00,000

- **Approaches to Calculate Average Capital Employed:**

Average Capital employed can be calculated from given Balance Sheet on particular date. It is calculated as under:

a. Assets Side Approached:

	₹	₹
All tangible Trading Assets at revised value, Otherwise at Book Value, Recorded as well as unrecorded assets. [Excluding goodwill, Non-Trade Assets, Fictitious Assets, (Differed Revenue Expenditure).]	x	x
Less: Third Party Liabilities Payable, [Recorded or Unrecorded] e.g. Denture, o/s interest, Current Liabilities & Provisions]	x	
Tangible capital employed at the end of year	x	x
Less: half of the profit earned during the year		
Average Capital employed		x

Average Capital employed can be calculated from liabilities side also, it is nothing but Adjusted OWNERS FUNDS employed in the business.

b. Liabilities Side Approached:

	₹	₹
Liabilities side approach may be adopted for deciding average capital employed. It is adjusted owner’s fund [Share - Holder’s Fund] it can be calculated as under:		

Paid up Share Capital [Equity + Preference]	x	xx
Add: Reveres & Surpluses [Accumulated Profits]		
Add: Revaluation Profits		
Less: i) Revaluation Loss	x	
ii) Fictitious Assets	x	
iii) Non-Trading Assets	x	(x x x)
Trading Capital Employed at the end of the year		x x x
Less: Half of the profit earned during the year		(x x)
Average Capital Employed		x x

Note : There is a difference of opinion about deduction of half of the profit for arriving at ACE. During the year if it is assumed that entire profit is withdrawn by the proprietor from business, then half of the profit should not be deducted for arriving at ACE.

2.6 METHODS OF VALUATION OF GOODWILL

a. No. of Years Purchase of Sales or Gross Fees:

Under this method, goodwill is calculated on the basis of turnover and not on net profit. The Buyer pays for goodwill which may be one or two years purchase of Gross receipts or takings. This method is simple & suitable for valuation of goodwill of professionals like Chartered Accountants, Advocates etc. Revenue of practice can be of recurring or non-recurring nature. Valuation of goodwill is based on recurring fees only. After estimating expenses the worth of practice is taken as the value of goodwill. The period of gross fees received or net sales is settled by agreement between Buyer & vendor.

b. No. of Years Purchase of Past Net Profit:

Under this method net profit of past few years is work out. Goodwill is valued either by adding net profit of past three years or as decided no. of years.

Goodwill = Average adjusted net profit x No. of years
Average profit may be simple average or weight average profit.

c. No. of Years Purchase of Future Maintainable Profit:

Under this method the profits which likely to be earned in future over the certain period of time are first estimated. to arrive at FMP. Past profits over the years, after adjusting non-recurring factors as well as expected future events which is not there in the past are also considered. [Refer Para 7, above for calculating FMP]

Goodwill = FMP x No. of years purchase

d. Super Profit Methods:

Under this method the Future Maintainable Profits of the firm are compared with the Normal Profits of the firm. Super Profit is the excess of the profit earned by the firm over the normal profit earned by the concern.

Super Profit = F.M.P. - Normal Profit

e. Normal Profit:

It is average profit earned by similar concern in the industry. It is decided on the basis of Average Capital Employed & Normal Rate of Return expected by the investors on capital employed.

Normal Profit = Average Capital Employed x NRR. (in%)

2.7 METHODS OF VALUATION UNDER SUPER PROFIT

a. Purchase of Super Profit Method:

Goodwill = Super Profit x No. of years of purchase

Under this method the no. of years of purchase will differ from industry & from firm to firm.

b. Capitalization of Super Profit:

Under this method the amount of super profit is capitalized at the normal rate of return. The method tries to find out the amount of capital required for earning the super profit.

$$\text{Goodwill} = \frac{\text{Super Profit}}{\text{N.R.R.}} \times 100$$

c. Sliding Scale Valuation of Super Profit:

This method is the variation of the purchase method. It is on the assumption that the greater amount of super profit, the more difficult it would to be maintained. If the super profit is greater more possibility of competition & therefore is difficult to maintain the same over the many years. In open market economy, it is not possible to maintain super profit for long terms.

In this method the super profit is divided in two or three divisions, each of this is multiplied by different no, of years purchase in descending order from the first division

Illustration : 2

Super profit is estimated ₹90,000/- ₹30,000 is taken as division, value goodwill under sliding scale method.

Solution:

Goodwill will be calculated as under:		₹
First ₹30,000 say three years purchase [30,000 x 3]	=	90,000
Second ₹30,000 two years purchase [30,000 x 2]	=	60,000
Third ₹30,000 one year purchase [30,000 x 1]	=	30,000
Total, Value of Goodwill	₹	1,80,000

d. Annuity Method of Super Profit:

Annuity takes in to consideration time value of money. Payment of Goodwill is made immediately for super profit likely to be earned in future. Goodwill in this case is the discounted value of super value.

Goodwill = Super Profit x Reference to Annuity Table

Note:

If reference to annuity table is not given. It is calculated as follow:

$$\text{Goodwill} = \frac{(1+i)^n}{i} \text{ where } i = \frac{i}{100}$$

The present worth of an annuity of Re.1 for n years at r per cent is calculated by the following formula:

$$Q = 1 - \frac{\left(1+\frac{r}{100}\right)^{n}}{\frac{r}{100}}$$

Q = Present value of an Annuity of Re 1 for n years at r per cent.

r = The Rate Per Cent p.a.

n = Number of Years.

2.8 CAPITALIZATION OF FUTURE MAINTAINABLE PROFIT (FMP) METHOD

Under this method, Goodwill is excess of capitalized value of FMP over net tangible trading assets. Following are the steps to be taken for valuing goodwill under this method

1) Find our FMP
2) Captalised Value of FMP. = $\frac{\text{F.M.P.} \times 100}{\text{N.R.R.}}$
3) Goodwill:

Capitalalised Value of FMP		XXX
LESS: Net tangible Trading Assets		[xxx]
Goodwill	₹	xxxxx

Note:

The value of goodwill remains the same in case of Capitalizations of Super Profit or Capitalization of FMP.

Illustration : 3

Capital Employed = ₹25,00,000 [net tangible trading assets]
N. R. R. = 15%
F. M. P. = ₹5,25,000

Find out value of goodwill under:

i) Capitalizations of Super Profit

ii) Capitalizations of F. M. P.

Solution:

i) Capitalizations of Super Profit

Super Profit = F.M.P. - NORMAL PROFIT
= 5,25,000 - [15% OF 25,00,000]
= 5,25,000 - 3,75,000

$$= 1,50,000$$

$$\text{GOODWILL} = \frac{\text{SUPER PROFIT}}{\text{N.R.R}} \times 100$$

$$= \frac{1,50,000}{15} \times 100$$

$$= ₹10,00,000$$

ii) Capitalization of F.M.P. method

$$\text{Capitalized Value of F.M.P.} = \frac{\text{F.M.P.}}{\text{N.R.R.}} \times 100$$

$$= 5,25,000 \times 100 \div 15$$

$$= ₹35,00,000$$

Value of Goodwill

Capitalalised Value of F.M.P.	35,00,000
LESS: Net tangible trading Assets	25,00,000
Goodwill	₹ 10,00,000

2.9 SOLVED PROBLEMS

Illustration : 1

The net profit of the company after providing for taxation, for the past five years are ₹40,000, ₹42,000, ₹45,000, ₹46,000, ₹47,000. Average capital employed is ₹4,00,000 on which a reasonable rate of return of 10% is expected. It is expected that the company will be able to maintain its super profit for the next five years.

a) Calculate the value of goodwill of business on the basis of the annuity of super profit, taking the present value of annuity of one rupee for five years at 10% interest as ₹3.78.

b) How would your answer differ if the goodwill is calculated by capitalizing the excess of the annual avg. distributable profits over the reasonable return on capital employed on the basis of the seam return of 10%.

c) Calculate goodwill on 5 years purchase of super profit.

Solution:

Super Profit = FMP - Normal Profit

FMP $= \dfrac{40000 + 42000 + 45000 + 46000 + 47000}{5} = \dfrac{2,20,000}{5}$

= ₹44,000

Normal Profit = A.C.E. x N.R.R.%
= 4,00,000 x 10%
= ₹40,000

Super Profit = FMP - Normal Profit
= 44,000 - 40,000
= ₹4,000

a) Goodwill as per annuity method:

Goodwill = Super Profit x Annuity Value
= 4000 x 3.78
= 15,120

b) Goodwill as per capitalization of super profit method:

Goodwill = $\frac{100}{NRR} \times \text{Super Profit}$

= $\frac{100}{10} \times 4000$

= ₹40,000

c) Goodwill as per No. of years purchase of super profit

Goodwill = Super Profit x No. of years of Purchase
= 4000 x 5
= ₹20,000

Illustration : 2

The following is the balance sheet of Mr. Salman as on 30th September 2014.

Liabilities	₹	Assets	₹
Capital	1,64,000	Land & Bldg.	36,000
General Reserves	40,000	Plant	54,000
Creditors	38,040	Investment	30,000
		Stock	26,850
		Bank	75,990
		Debtors	19,200
	2,42,040		2,42,040

The following were the net profits:

For the year ended September 30, 2012 ₹32,280; September 30, 2013 ₹36,870 & September 30, 2014 ₹43,350. (These amounts include income from investment ₹1,800 each year)

You are required to value the goodwill of the above business at 2 year's purchase of the average super profits for 3 Year's, taking the standard rate of return on capital employed in such type of business as 10% & assuming that the year's profit is immediately withdrawn in full by Mr. Salman.

Solution:

Super Profit = FMP - Normal Profit

FMP :

Years	**Profit (`)**	**- Income from Investment**	**= Trading Profits (`)**
2012	32,280	- 1800	30,480
2013	36,870	- 1800	35,070
2014	43,350	- 1800	41,550
Total Trading Profit			₹1,07,100

Average Trading Profit = $\frac{\text{Total Trading Profit}}{\text{No. of Years}}$

= $\frac{1,07,100}{3}$

Therefore **F.M.P.** = `35,700

Normal Profit = $\frac{NRR \times A.C.E.}{100}$

A.C.E. is not given readily therefore we have to find it.

A.C.E. =

Tangible Trading Assets [at market value otherwise B.V.]

	Rs.
Land & Bldg.	36,000
Plant	54,000
Stock	26,850
Bank	75,990

Debtors	19,200
	2,12,040
Less : Liabilities due to outsiders:	
Creditors	(38,040)
Tangible Trading capital	1,74,000

Note: It is mentioned in the problem that each year's profit is immediately in full by the proprietor. Hence, tangible capital at the end of the year is considered equal to average capital employed during the year. In such a case, half of the profit should not be deducted therefore.

A.C.E. = Tangible Trading Capital

Therefore **A.C.E.**= ₹1,74,000

Normal Profit = A.C.E. x N.R.R.%

$$= \frac{10}{100} \times 1,74,000$$

= 1,74,000

Super Profit = FMP - Normal Profit

= 35,700 - 17,400

= 18,300

Therefore, **Goodwill** = Super Profit x No. of yearn of purchase

= 18,300 x 2

= ₹36,600

Note: Income from investment is considered as a non-trading income. That is why we have deducted it from each year's profit while calculating F.M.P. & Investment is not included in A.C.E.

Illustration : 3

Manu & Co. decided to purchase the business Babu & Co. on 31-12-2014. Profits of Babu & Co. for the last 6 year's were :

Year	`
2009	10,000
2010	8,000
2011	12,000
2012	16,000

2013	25,000
2014	31,000

The following additional information about Babu & Co. is also supplied:

a) A casual income of ₹3,000 was included in the profits of 2011 which can never be expected in future.

b) Profit of 2012 was reduced by ₹1000 as a result of an extraordinary loss by fire.

c) After acquisition of the business, Manu & Co. has to pay insurance premium amounting to ₹1,000 which was not paid by Babu & Co.

d) Manu the proprietor of, Manu & Co. was employed in a firm at a monthly salary of ₹1,000 p.m. The business of Babu & Co was managed by a salaries manager who was paid a monthly salary of ₹400. Now, Mr. Manu decides to manage the firm after replacing the manager.

Compute the value of goodwill on the basis of 3 years purchase of the average profit for the last 4 years.

Solution:

Goodwill = Average Profit x 3

Years	**2011 (₹)**	**2012 (₹)**	**2013 (₹)**	**2014 (₹)**
Profits	12,000	16,000	25,000	31,000
Adjustments:				
a) Casual income not likely to be earned	- 3,000			
b) Loss by fire	NIL	- 1,000	NIL	NIL
Trading Profits `	9,000	17,000	25,000	31,000

Average Profit $= \frac{9000 + 17000 + 25000 + 31000}{4}$

= 20,500

	₹
Average Profits	20,500
Less: Insurance Premium Payable in Cuture	(1,000)
Add: Salary of Managers not payable (400 p.m.x12 mths.)	4,800
Less: Cost of Services of Manu (1000 p.m. x 12 mths.)	(12,000)

F.M.P.	`12,300

Therefore, **Adjusted Average Profit** = 12,300

Therefore, **Goodwill** = Average Profit x 3

= 12,300 x 3

= 36,900

Illustration :4

The following is the Balance Sheet of Ashok Ltd. As on 31st December, 2014.

Liabilities	₹	**Assets**	₹
Fully paid up capital 12000 shares of `100 each	12,00,000	Goodwill	40,000
General Reserve	1,60,000	Land & Bldg.	7,80,000
Profit & Loss A/	1,00,000	Plant & Machinery	3,00,000
Creditors	80,000	10% Government Securities (F.V.50000)	60,000
Bills Payable	40,000	Debtors	2,20,000
		Bills Receivable	60,000
		Stock in Trade	1,20,000
	15,80,000		15,80,000

The company earned net profits for the past years as follows: (this amounts include interest received from Government Securities.

Year	**Rs.**
2011	1,00,000

2012	2,00,000
2013	3,00,000
2014	4,00,000

The value of the goodwill should be computed at three years purchase of the average super profit for four years. The normal rate of return on capital employed in a similar business organization is 12%. Also calculate the value goodwill as annually of super profit taking annually outstand of ₹1 = 3.80

A. Valuation of Goodwill as per Super Profit Method:

a) **Average Capital Employed** = Assets at a realizable value o/s Liabilities.

Assets at Realisable Value		₹
Land & Bldg		7,80,000
Plant & Machinery		3,00,000
Debtors		2,20,000
Bills Receivable		60,000
Stock in trade		1,20,000
		14,80,000
Less : o/s Liabilities		
Creditors	80,000	
Bills Payable	40,000	1,20,000
Capital Employed		13,60,000

b) **Normal rate of return** = 12%

c) **Standard Profit** = 1360000 x 12%

= 163200

d) **Average Past Profit** = $\frac{100000 + 200000 + 300000 + 400000}{4}$

= $\frac{1000000}{4}$

= 250000-5000(Interest on investments)

= 245000

e) **Future Maintainable Profit** = Average Past Profit = 245000

f) **Super Profit** = FMP - Normal Profit

= 245000 - 163200

= 81800

g) **Value of Goodwill** = No. of years of purchase x Super Profit

= 3 x 81800

= 245400

B. **Value of Goodwill under annuity of super profit**.

Goodwill = Super Profit x Annuity Value

= 81800 x 3.80

= ₹3,10,840

Illustration: 5

The following is the Balance Sheet of Z & Co. as on 31st December, 2008.

Liabilities	₹	**Assets**	₹
Paid up share capital 1000 shares of `200 each	2,00,000	Goodwill	30,000
Capital Reserve	40,000	Land & Bldg.	1,70,000
General Reserve	60,000	Plant & Machinery	1,60,000
Bank Loan	50,000	Vehicles	70,000
Profit & Loss A/c	20,000	Stock in trade	60,000
Creditors	1,30,000	Debtors	50,000
Bills Payable	40,000	Investments	30,000
Provision for taxation	30,000		
	5,70,000		5,70,000

On December 31 the asses were revalued as follows:

Land & Bldg.	₹ 2,00,000
Plant & Machinery	₹ 1,50,000
Vehicles	₹ 60,000

The company earned profit after depreciation & taxation as follows:

2006	₹ 60,000
2007	₹ 70,000
2008	₹ 80,000

The average of these profits are expected to be earned in future.

The valuation of goodwill should be based on two year's purchase of the annual super profit. It is considered that 10% is a reasonable return on tangible capital.

You are required to value the goodwill.

Solution:

a) **Average Capital Employed** = Assets at a realizable Value - Liabilities

Assets at Realisable value:	₹	
Land & Bldg.	2,00,000	
Plant & Machinery	1,50,000	
Vehicles	60,000	
Stock	60,000	
Debtors	50,000	
Investments	30,000	
		5,50,000
Less : Liabilities		
Creditors	1,30,000	
Bills Payable	40,000	
Tax Provision	30,000	
Bank Loan	50,000	(2,50,000)
Capital Employed		3,00,000

b) **Normal rate of return** = 10%

c) **Standard Profit** = 300000 x 10%
= 30000

d) **Average Past Profit** $= \frac{60000+70000+80000}{3} = \frac{210000}{3}$

= 70000

e) **Future Maintainable Profit** =
Average Past Profit 70000

f) **Super Profit** = F.M.P. - Normal Profit
= 70000 - 30000
= 40000

g) **Value of Goodwill** = No. of years of purchase x Super Profit
= 2 x 40000
= ₹80,000

Illustration: 6

The net profits of a company after providing for taxation for the past five years are ₹20,000, ₹21,000. ₹22,500, ₹23,500. The capital employed in the business is ₹2,00,000 on which a reasonable rate of return of 10% is expected. it is expected that the company will be able to maintain it's super profits for the next five years.

a) Calculate the value of goodwill of business on the basis of an annuity of one rupee for five years at 10% interest as ₹3.78.

b) How would your answer differ if goodwill is calculated by capitalizing the excess of the annual average distributable profits over the reasonable return on capital employed on the basis of the same return of 10%?

c) Calculate goodwill on 5 years purchase of super profit.

Solution:

i) **Average Capital Employed** = ₹2,00,000

ii) **NRR** = 10%

iii) **Standard Profit** = 200000 x 10% = `20,000

iv) **Average Past Profit** $= \frac{20000+21000+22500+23000+23500}{5}$

= 22,000

v) **F.M.P.**

Average Past Profit	22,000
Less: Tax	-

	22,000

vi) **Super Profit** = 22000 - 20000 = 2000

vii) **Valuation of goodwill under annuity value**

Goodwill = Annuity of super Profit = Super Profit x Annuity Value

= 2000 x 3.78

= ₹7,560

viii) **Value of Goodwill** = No. of years of purchase x Super Profit

= 5 x 2000 = 10000

Capital Method:

Capital Value $= \frac{FMP}{NRR} \times 100$

$= \frac{22000}{100} \times 100 =$ ₹2,20,000

Value of Goodwill = Capital Value of FMP. - Capital Employed

= 2, 20,000 - 2, 00,000

= ₹20,000

Illustrations: 7

The following are particulars in respect of R Ltd.

i) Capital employed in the business is ₹10,00,000.

ii) A reasonable rate of return expected in a similar type of business is 7%.

iii) Net profit of the company after providing for depreciation & taxation for the past four years were:

₹1,00,000, ₹1,20,000, ₹1,60,000 & ₹1,80,000

iv) It is expected that the company will be able to maintain it's super profit for the next four years.

You are equired to calculate the value of goodwill.

a) On the basis of annuity of super profit method taking the present value of an annuity of Re. 1 for four years at 7% interest as ₹3.39.

b) By capitalizing the excess of the annual average distributed profits over a reasonable return on capital employed on the basis of the return of 7%.

Solution:

a) i) **Capital Employed** = ₹10,00,000

ii) **NRR** = 7%

iii) **Standard Profit** = 10,00,000 x 7% = 70,000

iv) **Average Past Profit** =
$$\frac{100000+120000+160000+180000}{4}$$
= 1, 40,000

v) **FMP**

Average Past Profit	1,40,000
Less Tax	-

	1,40,000

vi) **Super Profit** = FMP - Normal Profit (Standard Profit)
= 1,40,000 - 70,000
= 70,000

vii) **Value of Goodwill** = 3.39 x 70,000
= ₹2,37,300

viii) **Capitalisation of Super Profit**

Goodwill = $\frac{\text{Super Profit}}{\text{NRR}} \times 100$

$= \frac{70,000}{7} \times 100$

= ₹10,00,000

Illustration: 8

The following is the Balance Sheet of Asha Inc as on 31st March 2012.

Liabilities	₹	Assets		₹
Share Capital		Goodwill		1,25,000
5,000 Shares of `100 each	5,00,000	Land & Building	1,80,000	
Reserve Fund	1,50,000	Less : Depreciation	36,000	1,44,000
Workmen compensation Fund	25,000	Plant & Machinery (at cost)	2,40,000	
Workmen Profit Sharing Fund	45,000	Less : Depreciation	40,000	2,00,000
Profit & Loss Account	1,50,000	Investments (to provide replacement of Plant & Machinery)		1,00,000
Creditors	2,30,000	Book Debts	3,60,000	
Other Liabilities	1,00,000	Less : Provision	30,000	3,30,000
		Stock		2,00,000

		Cash at Bank Preliminary Expenses		75,000 26,000
	12,00,000			12,00,000

Further Information:

1) The profits earned by the company for the three years were as under:
   Year ended 31st March 2010 ₹3,10,000.
   Year ended 31st March 2011 ₹2,73,000.
   Year ended 31st March 2012 ₹2,90,000.

The profits given are profits before tax, which was 40% throughout.

2. Asha Inc had been carrying on business for the past several years. The company is to be taken over by another company. For this purpose you are required to value Goodwill by "Capitalisation of Maintainable Profits Method". For this purpose following additional information is available.

a) The new company expects to carry on business with its own board of directors, without any addition. The fees paid by Asha Inc. to its directors amounted to ₹9,000 per year.
b) The new company expects a large increase in value of business and therefore, will have to take an additional officer for which it will have to pay extra rent of ₹12,000 per year.
c) As on 31st March 2012 Land and Buildings were worth ₹3,00,000 whereas Plant and Machinery were worth only ₹1,80,000. There is sufficient provision for doubtful debts. There is no fluctuation in the values of investments and stocks.
d) Liability under Workmen Compensation Fund was only `5,000.

3) The expected rate of return on similar business may be taken at 12%.

You are required to value Goodwill according to above instructions. All your workings should form part of your answer. Consider average capital employed, the same as closing capital employed for you calculations.

(April 99, Adopted)

Solution:

1) **Future Maintainable Profits**

Year	**Year**	**Profit Before Tax** ₹
1999 - 2000	2009 - 10	3,10,000

2000 - 2001	2010 - 11		2,73,000
2001 - 2002	2011 - 12		2,90,000
			8,75,000
		=	$\frac{8,73,000}{3}$
Average Profit before tax		=	2,91,000
Add : Expenses Not Payable in future (directors fees)			+ 9,000
Less : Additional Expenses (Extra Rent)			- 12,000
Adjusted Profit (before tax)			2,88,000
Less : Tax @ 40%			(1,15,200)
Net Profit after tax, or Future Maintainable Profit			1,72,800

2. Capital Employed (Excluding Goodwill)

Particulars		₹	₹
Assets			
Land & Building (Market Value)		3,00,000	
Plant Machinery (Market Value)		1,80,000	
Investment (cost) (See Note)		1,00,000	
Debtors (Net)		3,30,000	
Stock (Cost)		2,00,000	
Cash		75,000	
`	(A)		11,85,000
Less : Liabilities:			
Creditors		2,30,000	
Other Liabilities		1,00,000	
Workmen's Compensation Fund (actual)		5,000	
Workmen's Profit Sharing Fund		45,000	
	(B)		3,80,000
Closing Capital Employed as on 31-03-2002	(A-B)		8,05,000

3) **Expected Rate of Return** = 12% (given)

4) **Value of business by capitalization of Future Maintainable Profits at 12%**

$$= \text{F.M.P.} \times \frac{100}{\text{NRR}} = \frac{1,72,800}{12} \times 100 = 14,40,000$$

5) **Goodwill** = Value of business Less Capital Employed
= 14,40,000 - 8,05,000 = ₹6,35,000

Working Notes:

1) Investments are included in capital employed because they are trading investments meant for replacement of Plant and Machinery.

2) In the absence of information (regarding rate and method of depreciation) on adjustment is made to Future Maintainable Profit for depreciation on revalued Land & Building and Plant & Machinery.

Illustration: 9

Sandwitch, Pizza a Burger are partners in a firm sharing profits and losses in the ratio of 5:2:1. The partnerships deed provides that in the event of retirement or death of a partner goodwill is to be valued at three years' purchase of Weighted Average of Future Maintainable Profit over a Period of four years, (the weights being four for the immediate year after the event, three for the next year, two for the third year and one for the last year) in excess of 12.5% of Capital Employed in the business at the time of retirement/death. On 31st December, 2014 Pizza retired. The Balance Sheet of the firm was as follows:

Liabilities	₹	**Assets**	₹
Capitals		Fixed Assets	5,00,000
Sandwitch	7,00,000	Net Current Assets	8,00,000
Pizza	3,50,000		
Burgar	2,50,000		
	13,00,000		13,00,000

State during the year ended 31st December 2014 totaled ₹1 crore and were at a gross margin of 10%. The expenses amount to 30% of Gross Profit. It is expected that sales will increase at 20% cumulative rate of growth every year. Gross Profit margin percentage being reduced to 9%. The expenses would continue to be at 30% of Gross Profit. Calculate goodwill which is to be credited to Pizza.

(April 2010, adapted)

Solution:

1) Calculation of Future Maintainable Profits (FMP)

Particulars	**2015 ₹('000)**	**2016 ₹('000)**	**2017 ₹('000)**	**2018 ₹('000)**
Sales (Increase by 20%) Cumulative	12,000	14,400.00	17,280.00	20,736.00
A) Gross Margin (9% on Sale)	1,080	1,296.00	1,555.20	1,866.24
B) Less : Expenses likely to arise in future	324	388.80	466.56	559.87
C) (30% of Gross Profit) D) FMP (B - C)	756 x 4	907.20 x 3	1,088.64 x 2	1,306.37 x 1
E) Weights (given) Weighted FMP (D x E)	3,024	2,721.60	2,177.28	1,306.37

Weighted Average of FMP = $\frac{\text{Weighted FMP}}{\text{Total of Weights}}$

$$= \frac{3,024 + 2,721.60 + 2,177.28 + 1,306.37}{10} = \frac{9,229.25}{10}$$

= ₹922.925 (in '000)

2) **Capital** = ₹13,00,000

3) **Normal Profit**=Capital Employed x NRR (given)
= ₹13,00,000 x 12.5% = ₹1,62,500.

4) **Super Profit** = FMP - Normal Profit.
= 9,22,925 - 1,62,500 = ₹7,60,425

5) **Goodwill** = No. of years of Purchase x Super Profit
= 3 x 7,60,425 = ₹22,81,280

6) **Goodwill to be credited to Pizza's A/c**

= 22,81,280 x $\frac{2}{8}$ = ₹5,70,320

Illustration : 10

Dr. Daroowala is a senior medical practitioner. Due to his old age he invites Dr. Batiwala newly qualified doctor as partner with 60% share in future profits from 1-1-2001. Dr. Daroowala desires to find value of Goodwill to be received from Dr. Batiwala. Goodwill should be valued at two years' purchase of average expected super earning of next three years. He gives following information:-

1) His gross fees for past three years are:

   2008 - ₹12,00,000; 2009 - ₹15,20,000 and 2010 - ₹16,80,000

2) After admission of Dr. Batiwala, Dr. Daroowala will not attend clinic regularly. Due to this the gross fees will be reduced by ₹4,80,000 in 2011. However thereafter increase will be @ ₹1,60,000 per annum for year 2001 onward.

3) Staff salaries in past three years were ₹4,00,000, ₹8,80,000 and ₹6,00,000. In 2001 the expected expenditure for this year will be ₹7,00,000. Thereafter increase will be @ 20% of previous year.

4) Present clinic expenses are ₹80,000 per annum. This will increase by 50% in 2001 and remain unchanged thereafter.

5) Normal net earnings are considered at 2,50,000.

Ascertain amount of goodwill payable by Dr. Batiwala to Dr. Daroowala.

(October 2000, adapted)

Solution:

1) Calculation of Future Maintainable Profits (FMP)

	Particulars	2011 ₹	2012 ₹	2013 ₹
A	**Gross Fees**	12,00,000	13,60,000	15,20,000
B	**Less : <u>Expenses likely to arise in future</u>**			
	Staff Salaries	7,00,000	8,40,000	10,08,000
	Office Expenses	1,20,000	1,20,000	1,20,000
	Adjusted Profits (A - B)	3,80,000	4,00,000	3,92,000

Average Maintainable Profit or FMP

$$= \frac{3,80,000 + 4,00,000+,,92,000}{3} = \frac{11,72,000}{3}$$

= ₹3,90,667

2) **Normal Profit** = 2,50,000 (given)

3) **Super Profit** = FMP - Normal Profit
= 3,90,667 - 2,50,000 = 1,40,667

4) **Goodwill** = No. of years of Purchase x Super Profit
= 2 x 1,40,667 = 2,81,334

5) **Amount of goodwill payable by Mr. Batiwala**
= 60% of 2, 81,334
= ₹1, 68,800

2.10 EXERCISES

1. Explain term 'Goodwill'. State circumstances when Goodwill needs to be valued.
2. Explain various methods for valuation of Goodwill.
3. Elaborate the factors affecting value of Goodwill.
4. Write Short Notes On:
   a. Future Maintainable Profits.
   b. Average Capital Employed.
   c. Normal Rate of Return.
   d. Treatment of Goodwill in Accounts.
   e. Treatment of Non-Operating Income & Assets for Goodwill Valuation.
   f. Super Profit.
5. Objective Type Questions:

A. Fill in the blanks

1. Net tangible assets should exclude **Fictitious assets and non trade Investments** while ascertaining average capital employed.
2. F.M.P. – Normal Profit == **Super Profit**
3. Normal profit = Average Capital employed x **NRR. %**
4. Average Capital employed = Closing capital less ½ **the net profit of the current year.**
5. Goodwill belongs to the category of **Intangible Assets**
6. Weighted Average profit = Total of product of profit **÷ Total Weights.**
7. When Net Profit shows large variations is better to calculate **Weighted** Average profit.
8. Super profits are the profits earned above **Normal profit**.
9. F.M.P. = Adjusted Trading Profits after **abnormal profits/losses.**
10. **Capital Employed** is also called Net Trading Assets
11. Goodwill of professional firm can be valued under **FMP** method
12. Average Capital employed = Opening capital plus ½ **profit for the current Year**

13. Average Capital Employed = ½ **(Opening Capital +Closing Capital)**

B. True or False

1. Goodwill is fictitious asset of business : **False**
2. Goodwill is intangible assets of business **True**
3. Purchased Goodwill must be accounted **True**
4. Goodwill must not be accounted if it is paid privately **True**
5. Goodwill must be valued after valuation of shares : **False**
6. Goodwill is required to be valued when there is change in profit sharing ratio amongst partners of the firm. **True**
7. Goodwill can be purchased / Sold along with business only **True**
8. N. R.R. may differ from industry to industry. **True**
9. Average Capital Employed should be considered for calculation of normal profit. **True**
10. Goodwill of professional firm cannot be valued : **False**
11. Goodwill is capacity of business to retain its customers **True**
12. Goodwill represents excess of book values of the concern over net worth of assets. **True**
13. Any abnormal profits should be deducted from the net profits of that year while calculating F.M.P. **True**
14. Any abnormal loss should be deducted from net profit before asserting F.M.P. : **False**
15. For goodwill valuation F.M.P. should be After Tax **True**

C. Match the Columns:

1]

Column A	Column B
1.Goodwill 2. F.M.P. 3. Normal profit 4. Super Profit 5.Capital employed	a. Average Trading profit b .Excess of normal profit over F.M.P. c. Reputation d. Net tangible trading assets e. Excess of F.M.P. over normal profit f .N.R.R. % X Capital employed

Answer: (1-c, 2-b, 3-a,4-e,5-d)

2]

Column A	**Column B**

1. Capital employed 2. Average capital 3. Weighted average profit 4. No. of year's purchase of super profit 5. Limitation of valuation of Goodwill	a] Goodwill b] Total products÷ Total Weighted c.] Ignores effect of inflation d] Total funds employed e] closing capital- ½ [net profit] f] Total Weights÷ Total Products.

Answer :1-d,2-e,3-f,4-a,5-c

C. MULTIPLE CHOICE QUESTIONS

1. Excess of F.M.P over Normal profit
   a. Net Profit
   b. Surplus profit
   c. Super Profit
   d. Dividend

2. Goodwill is
   a. Reputation of business
   b. Intangible Asset
   c. Brand Name
   d. All the above

3. Excess of Purchase Consideration over net tangible assets
   a. Capital Reserve
   b. Goodwill
   c. Current Assets
   d. None of the above

4. A ltd. having long standing in business , F.M.P. Rs.1,00,000, Normal return expected in same type of business Rs. 65000. Super profit is:

   a. Rs.45,000,
   b. Rs. 75000
   c. Rs. 35000
   d. Rs. 50000

5. B ltd. having long standing in business , F.M.P. Rs.1,50,,000, Normal return expected is same type of business Rs. 50000. VALUE of goodwill at three years purchases of Super profit

   a. Rs. 320,000

b. **Rs. 3,00,000**
c. Rs.2,00,000
d. Rs. 150,000

6. Rate of profit expected on average capital employed

   a. **N.R.R.**
   b. Normal profit
   c. Super profit
   d. F.M.P..

7. Excess of normal profit over super profit:

   a. Goodwill
   b. Machinery
   c. Capital Reserve
   d. **None of the above**

8. Capital Employed in Business is Rs.9,50,000, Average profit Rs.225,000, N.R.R. 15%. Normal profit from the business is

   a. Rs.225000
   b. **Rs.142500**
   c. Rs.82500
   d. None of the above

9. Value of goodwill by capitalization of super profit Rs.32,500, @ N.R.R.16,2/3 % Is

   a. **Rs 195000**
   b. Rs. 194500
   c. Rs. 294500
   d. Rs. None of the above

10. Super profit Rs.120, 000, FMP. Rs.180, 000, NRR. 10.00%, What should be capital Employed

   a. Rs.25,00,000,
   b. Rs.30,00,000
   c. **Rs. 6,00,000**
   d. Rs. 12,00,000

11. Goodwill of the firm valued at four years purchase of super profit Rs.1,80,000, Capital employed Rs.120,000,FMP Rs. 60,000 then rate of NRR is

a. 10.%
b. 12.50%
c. 7.50%
d. None of the above

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11

VALUATION OF SHARES

Unit Structure:

3.1 Introduction
3.2 Valuation of Shares
3.3 Methods of Valuation of Equity Shares
3.4 Valuation of Equity Shares before Bonus and after Bonus
3.5 Valuation of Shares before Right Issue and After Right
3.6 Valuation of Equity Share after Conversion of Preference Shares into Equity Shares
3.7 Valuation of Preference Shares
3.8 Valuation of Shares from the Point of view of Minority/ Majority Shareholders
3.9 Solves Problems
3.10 Exercise

OBJECTIVES

After studying the unit the students will be able to:

- Understand the need of Valuation of Shares.
- Discuss the methods of valuation of shares.
- Solve the practical problems.

3.1 INTRODUCTION

According to Companies Act, 2013, Shares means share in the share capital of a company. A share is one unit into which the total share capital is divided. The shares of the private Ltd. Company cannot quote on stock exchange also not all Public companies shares are quoted on stock exchange. Its value cannot be easily ascertained. Price of such shares depends upon various factors such as demand & supply, market conditions etc. Quoted shares means which are listed on stock exchange. The price prevailing on stock is accepted. However valuation by expert is called for when parties involved in the fails to arrive at a mutually acceptable value.

3.2 VALUATION OF SHARES

3.2.1 Need for Valuation of Shares:

The necessity for valuation of shares arises inter alia in the following circumstances:

1) Share of one class are to be converted into shares of another class.
2) When shareholder wants to take loan by pledging shares with Bank.
3) When shares are to be transferred i.e. bought or sold.
4) When companies are amalgamated, absorbed, merged or reconstructed.
5) When the Government wants to compensate the shareholders on the nationalization.
6) When share are to be distributed among legal heirs on death of share-holder holding the controlling block of shares

The price prevailing on Stock Exchange is accepted for transactions of small block of shares which are quoted on stock Exchange.

3.2.2 Factors affecting Valuation of Shares

a) Nature of business.
b) Market Conditions as Regards The Companies doing the Similar Business & Existing Competition.
c) Demand & Supply of Shares in Stock Exchange.
d) Earning Capacity of Company and Growth Prospects.
e) Goodwill of Company.
f) Reputation of the management.
g) Anticipated legislature measure.
h) General Economics Conditions and Policies of Govt. / R.B.I.

3.3 METHODS OF VALUATION OF EQUITY SHARES

Where there is more than one class of shares i.e. equity shares and preference shares, the Articles of Association must be referred to for the purpose of finding out the respective rights of the shareholders. Preference shareholders may have preferential rights as regards payment of dividend, participating in surplus etc.

Valuation of Equity Share depends upon whether they are quoted or unquoted. In case of quoted shares, the value should be as per quotation in the recognized stock exchanges.

Primarily following are the methods of Valuation of Shares.

1. Assets Based:

a) Intrinsic Value:

2. Yield Based:
a) Yield Value
b) Earning Capacity Method
c) Capitalization of Maintainable Profit Method

3. Other:
a) Fair Value
b) Dividend Capitalization Method

4. Market Price Approaches:
a) Price Earning Multiple
b) Book Value Multiple

1. Assets Based:

Under this type of valuation net assets valuation are considered.

a) Intrinsic Value / Liquidation Value / Break - up Value / or Assets Backing Value:

This method of valuation is based on the assumption of assets. Here it is assumed that the company goes in liquidation in nearby period. All the assets are sold and all the liabilities are paid off, then remaining surplus is distributed among the equity shareholders.

- **Step to Find the Intrinsic Value:**

Step No. I. Find amount available to Equity Shareholders.

All assets at Current Market Value including Goodwill, Non-Trade Investments, but Excluding Fictitious Assets.

	₹	₹
Goodwill	x	
Loan & Buildings	x	
Plant & Machinery	x	
Furniture	x	

Vehicles	x	
Trade & Non-Trade Investments	x	
Stock	x	
Debtors & Bills Receivables	x	
Cash & Bank Balances	x	
Loans, Advances	x	x x
Less: All Liabilities ay Current Values, Excluding Share Capital & Reserves and Surplus.		
Debentures & Accrued Int Thereon	x	
Long Term Loan	x	
Creditors & Bills Payables	x	
Outstanding Expenses	x	
Proposed / Unpaid Dividend	x	
Provision for Taxation	x	
Any other Liabilities Payable [Provided or Not]		(x x)
B) Total Liabilities Payable		
Net Assets (A - B)		
C) Dues to preference share holders:	x	
Paid-up preference share capital	x	
Arrears of Pref. Dividend	x	(x)
Premium payable on redemption of Pref. Share Capital		x x
Amount available to Equity Shareholders [A-B-C]		

Step No. II: Intrinsic Value per Share

A) **If all the share are fully paid-up**

$$= \frac{\text{Amount available to equity sahreholders}}{\text{No.of equity shares}}$$

The Intrinsic value of share is determined as a product of Face Value of Share, in case, Equity Shares having different F.V., then value should be calculated per rupee of share capital.

Intrinsic Value per Rupee

$$= \frac{\text{Amount available to equity shareholders}}{\text{Paid up equity share Capital}}$$

B) If some shares are partly paid-up

[On account of calls in arrears or uncalled capital]

Amount available to equity shareholders [As above]	x
ADD: calls in arrears/uncalled capital assuming that call are	x
Made and received	x
Net amount available to Equity Shareholders [Fully Paid-up]	

Therefore, Intrinsic value per partly paid up share =

$$= \frac{\text{Net amount available as above}}{\text{Total No. of equity shares}} - \text{unpaid amount per equity share =]}$$

- **Key Points to be remembered:**

While calculating the Net Assets Value:

1. Only market value of the assets should be considered. If market value is not given then book value should be considered.
2. All assets recorded as well as unrecorded should be considered.
3. Goodwill also should be considered as per the instruction of the problem.
4. Non-Trade Assets, Non-Trade-Liabilities should be taken into account.
5. If problem is silent, Valuation should be done ex-dividend i.e. proposed dividend should be deducted. If cum-dividend valuation is to be done then, proposed dividend should not be deducted.

- **Merits of Intrinsic Value Method:**

i) It is very useful when the company is being liquidated in near future.

ii) It takes into account both types of assets.

iii) It is simple to use in valuation of different types of Equity Shares

- **Demerits of Intrinsic Value Method:**

i) It is difficult to estimate the realizable Value of Assets.

i) The assumption of liquidation is contradictory with Normal assumption of Going Concern Principle.

iii) The value of the goodwill is very much subjective valuation of the basis of assets is generally not recommended for a going concern, because there, the predominant factor is Yield.

2. Yield Value:

This method is method of valuation is based on the assumption of Going Concern principle. Here it is assumed that the company shall carry on business profitability for many years to come. Therefore, value of share is based on account of profit that would be available to Equity Shareholders as Dividend.

A. Yield Value

Yield value basis valuation may take place in the form of valuation based on rate of return and productivity factor.

Steps to calculate yield value

a) Find out Maintainable Profit [FMP] same as goodwill valuation		x	
Add back-interest on Non-trade income		x	
			xx
Less i) Transfer to reserve as required under Law	x		
ii) Preference dividend	x		
iii) Dividend distribution Tax	x		(xx)
F.M.P. Available to Equity Shareholders			xxx

b) **Find out rate of FMP**

$$= \frac{\text{F.M.P.}}{\text{Paid Equity Capital}} \times 100$$

c) Find out Yield Value

$$= \frac{\text{Rate of F.M.P.}}{\text{N.R.R.}} \times \text{Amount paid up per Equity Share}$$

B. Earning Capacity Method:

Here value of share is decided on the earning capacity of company, earning are different in different contest. Relating to funs employed.

Steps to Calculate Earning Capacity Value of Equity Share:

a) Find out earning: It is the amount of profit before interest loan term loans & preference divided but after tax. It is operating profit on Capital Employed.

b) Calculate Capital Employed: It is Total capital Employed Including Term Loans.

Capital employed = Assets - Short Term Liabilities & Provisions,
= Own Fund + Owed Funds

c) Calculate Rate of Earning = $\frac{\text{Earning / Profit Earned}}{\text{N.R.R.}} \times 100$

d) Value of Equity Share = $\frac{\text{Rate of Earning}}{\text{N.R.R.}} \times \text{Paid up amt. per share}$

C. Capitalization of Maintainable Profit Method:

Under this Method Earning is Capitalized at NRR. Step to Calculate Value of Share:

a) Calculate F.M.P. available to equity shareholders.

b) Capitalized Value of F.M.P = $\frac{\text{F.M.P.}}{\text{N.R.R.}} \times 100$

c) Value Per Equity Share

$$= \frac{\text{Capitalized Value of F.M.P.} \times \text{Amount Paid Per Equity Share}}{\text{Paid up Equity Capital}}$$

3. Other:

A. Fair Value : / Dual Method:

The fair value of a share is the average of the value of shares obtained by the net assets method and the one obtained by yield method. Intrinsic value indicate amount of net assets available to equity shareholder and yield value is based on earning per equity share.

$$\text{Fair value of a equity share} = \frac{\text{Intrinsic Value} + \text{Yield Value}}{2}$$

This method attempts to minimize the demerits of both the methods.

B. Dividend Capitalization Method:

This method is based on dividend paid on equity share i.e. amount of earning made available to shareholders the value of share is determined by capitalizing the dividend per share at N.R.R.

$$\text{Value Per Share} = \frac{\text{Dividend Per Share}}{\text{N.R.R.}} \times \text{Paid Value Per Share}$$

4. Market Price Approaches:

a) Price Earning Multiple

b) Book Value Multiple

Both this methods are to be studied at higher level, therefore not explained here,

5. Shares Having Different Paid-up Value:

Under this type valuation of equity share should be calculated with reference to one rupee of share capital, then such value should be multiplies by paid up amount per share.

3.4 VALUATION OF EQUITY SHARES BEFORE BONUS AND AFTER BONUS

Issue of Bonus Shares is called conversion of profits into share capital or capitalization or profit. Bonus shares are issued to existing shareholders free of cost, net assets available to equity shareholders as well as F.M.P. are remain the same

Illustration : 1

50,000 Equity Shares of `10 each fully paid up	5,00,000
Reversers & Surplus [Including Current Years Retain Earnings]	25,50,000
Net assets available to Equity Shareholders	30,50,000
F.M.P. for the year	9,50,000
N.R.R. 12.5%	

Company declared bonus at rate one share for every two shares held, you are required to find fair value equity share before bonus and after bonus.

	No.	₹ Share Capital
Equity Shares before Bonus	50,000	5,00,000

ADD: Bonus Shares [50,000 x $\frac{1}{2}$]	25,000	2,50,000
Equity Share Capital after Bonus F.M.P. `9,50,000 given, N.R.R. 12.50%	75,000	7,50,000

Net assets available to Equity Shares Holders = 30,50,000 [No Changed as Bonus are Free]

$$\text{Intrinsic Value} = \frac{\text{Net assets available to Equity Shareholders}}{\text{No. of Shares}}$$

		Before Bonus	After Bonus
A] Net assets available to Equity Shareholders		₹30,50,000	₹30,50,000
B] No. of Shares		50,000	75,000
Intrinsic Value = A / B		= ₹61	= ₹40.667
Yield Value			
$\text{Rate of F.M.P.} = \frac{\text{F.M.P.}}{\text{Paid up equity Share Capital}} \times 100$			
A. F.M.P.	₹	9,50,000	9,50,000
B. Equity Share Capital	₹	5,00,000	7,50,000
Rate of F.M.P.=A/B x 100	=	190%	126.667%
$\text{Yield Value} = \frac{\text{Rate of F.M.P.} \times 10}{\text{N.R.R.\%}}$	=	$\frac{190\% \times 10}{12.5\%}$	$\frac{126.667 \times 10}{12.50\%}$
	₹=	152.00	101.33
$\text{Fair Value} = \frac{\text{Intrinsic Value} + \text{Yield Value}}{2}$		$\frac{61+152}{2}$	$\frac{40.67+101.33}{2}$
	=	₹106.50	₹71.00

3.5 VALUATION OF SHARES BEFORE RIGHT ISSUE AND AFTER RIGHT

Rights Shares are issued to existing shareholders for cash, however issue price is always less, therefore there bonus elements included in issue price.

Illustration : 2

40,000 Equity Shares of `10 each fully paid up	4,00,000
Reserves & Surplus [Including Current Years Retain Earnings]	15,50,000
Net assets available to equity shareholders	19,50,000
F.M.P. for the year	₹5,25,000

N.R.R. 10% Company declared Rights at rate one share for every two shares held, at `15, per share payable on application you are required to find fair value equity share before right and after rights.

Solution:

	Before Right	**After Right**
No. Equity Shares =	40,000	60,000
Equity Share Capital ₹10 each	4,00,000	6,00,000
Net assets available to equity shareholders	19,50,000	19,50,000
ADD: Right Issue Amt. [20,000 Share x 15]	--	3,00,000
Net assets available to equity shareholders	₹19,50,000	22,50,000
$\text{Intrinsic Value} = \dfrac{\text{Net assets avialable to Equity Shaareholders}}{\text{No. of Sahres}}$		
Intrinsic Value =	$\dfrac{19,50,000}{40,000}$	$\dfrac{22,50,000}{60,000}$
	=₹48.75	₹37.50
Yield Value		
$\text{Rate of F.M.P.} = \dfrac{\text{F.M.P.}}{\text{Paid up equity share capital}} \times 100$		
A. F.M.P.	₹5,25,000	5,25,000
B. Equity Share Capital	₹4,00,000	6,00,000
Rate of F.M.P. = A/B	= 131.25%	87.50%
$\text{Yield Value} = \dfrac{\text{Rate of F.M.P.} \times 10}{\text{N.R.R.}}$	$\dfrac{131.25\%}{10.\%}$	$\dfrac{87.50\%}{10.00\%}$
	₹131.25	87.50
$\text{Fair Value} = \dfrac{\text{Intrinsic Value} + \text{Yield Value}}{2}$	$\dfrac{48.75 + 131.2}{2}$	$\dfrac{37.50 + 87.50}{2}$
	=₹90.00	₹62.50

3.6 VALUATION OF EQUITY SHARE AFTER CONVERSION OF PREFERENCE SHARES INTO EQUITY SHARES

Preference Shares may be converted into equity share as terms on issue terms:

These Preference Shares may be converted a time of Redemption of Preference Share capital in such case number of equity shares are increased, resulting increase in equity capital. Procedure for valuation is same, only revised calculation of equity shares & equity capital

Illustration : 3

5,75,000 equity shares of ₹10 each fully paid up	57,50,000
25,000 10% Preference Shares of ₹100 each	25,00,000
Reserve & Surplus	2,00,00,000
Net Assets `.	2,82,50,000

Preference Shares are convertible as per terms; three share for every five shares held. You are required to find value of Equity share before & after conversion of pref. assuming all pref. shares holders exercises option in favor of conversion.

Solution:

$$\text{Before Conversion} = \frac{\text{Net assets available to eq. Share-holder}}{\text{No. Equity Shares}}$$

Intrinsic Value = [27,50,000+2,00,00,000]/No. of equity shares

= 2,57,5000,000 / 5,75,000 = ₹44.78

After conversion of preference shares number of equity shares as well as share capital increases

Present No. of Equity Shares before conversion	5,75,000
ADD: Equity Shares Issued to Preference Shareholder [25,000x3/5]	15,000
Total Equity Shares after conversion	5,90,000

$$\text{Intrinsic Value of Eq. Share} = \frac{\text{Net assets available to eq. Share-Holder}}{\text{No.Equity Shares}}$$

$$= \frac{2,82,50,000}{5,90,000}$$

= ₹47.88

Note: Net assets available to equity share holders remain same after conversion if pref. shares.

5,90,000 Equity Share of ₹10 each fully paid	59,00,000

Reserve & Surplus Bal.	2,00,00,000
Security Premium on Conversion [25,00,000-1,50,000]	23,50,000
	2,82,50,000

3.7 VALUATION OF PREFERENCE SHARES

i) If preference shares are non-participating (having priority)

In such a case value of a preference share will be equal to its paid up value:
Intrinsic Value = Paid up Preference Capital + Arrears of dividend, if any / No. of Preference Shares.

ii) If Preference Shares are having no preference over Equity Shares.

In this case, the net assets available should be divided between equity and preference shareholders in the ratio of paid up capital.

$$\text{Intrinsic Value} = \frac{\text{Net Assets Available to Preference Shareholders}}{\text{No. of Preference Shares}}$$

iii) If Preference Shares are Participating:

In this case preference shareholders get a share in surplus assets as per the provisions of Articles of Association:

$$\text{Intrinsic Value} = \frac{\text{Paid up Preference Share Capital + Surplus + Arrears of Dividend if any}}{\text{No. of Preference Shares}}$$

3.8 VALUATION OF SHARES FROM THE POINT OF VIEW OF MINORITY/ MAJORITY SHAREHOLDERS

Shareholders may be classified into two categories namely:

i) Majority Shareholders:
Means those shareholders who are holding larger portion of share capital. Such shareholders are interested in FMP. Therefore, valuation of such share is based on FMP.

ii) Minority Shareholders:

Means those shareholders who are holding smaller portion of share capital of a company. Such shareholders are interested in the rate of dividend declared by the company. Therefore, valuation of such shares is based on the dividend declared by the company. Following formula may be used to decide the value:

$$\frac{\text{Average Rate of Dividend}}{\text{N.R.R.}} \times \text{Amount Paid Per Equity Sahre}$$

3.9 SOLVED PROBLEMS

Illustration: 4

Following is the summarized Balance Sheet of M/s Alpha Paints as on 30-09-2014

Liabilities		₹	Assets	₹
Share Capital			Plant	50,000
30000Equity Shares of ₹10 each		3,00,000	Property	1,20,000
Reserves & Surplus:			Stock	3,10,000
General	1,20,000		Debtors	2,03,000
Capital	40,000		Bank	1,17,000
Profit & Loss A/c	1,20,000	2,80,000	Cash	1,700
Current Liabilities & Provisions:				
Creditors	93,700			
I. T. Payable	11,500			
Proposed Dividend	34,000			
Provision for Taxes	82,500	2,21,700		
		8,01,700		8,01,700

Net Profit before taxation for three years ended 30th September 2012, ₹1,38,000 30th September 2013, ₹1,83,000 & 30th September 2014, ₹1,97,000; freehold property was valued at `1,60,000 Average yield in this type of business is 10% on capital employed. Goodwill to be valued at capitalised value of F.M.P. You are required to find our the value of each equity shares on the basis of above mentioned facts as:

i) Net Assets basis, and ii) Yield basis.

The company has a practice of transferring 20% of it's yearly profit after tax to General Reserve.

Solution:

A) Valuation of Goodwill

a) **Average Capital Employed =** Assets at a Realizable Value - O/s Liabilities.

Assets at Realised Value:

Plant	50,000	
Property	1,60,000	
Stock	3,10,000	
Debtors	2,03,000	
Bank	1,17,000	
Cash	1,700	8,41,700
Less: O/s Liabilities		
Current Liabilities		
Creditors	93,700	
I. T. Payable	11,500	
Proposed Dividend	34,000	
Provision for Taxes	82,500	(2,21,700)
Capital Employed		6,20,000

b) **Normal Rate of Return** = 10%

c) **Average Past Profit**

Net Profit for 30-9-1999 = $\frac{197000+138000+183000}{3}$

= 1,72,667

d) **FMP**

Average Past Profit	1,72,667
Add: Expenses not to be incurred in future	NIL
Less: Expenses to be incurred in future	NIL
FMP before tax	1,72,667
Less: Tax	- 82,500
	90,167
Less: 20% General Reserve	- 18,033
F.M.P.	72,134

e) **Capitalised Value of Maintainable Profit:**

$$= \frac{FMP}{NRR} \times 100$$

$$= \frac{72134}{10} \times 100$$

$$= ₹7,21,340$$

f) **Value of Goodwill**

= Capitalised Value of Maintainable Profit - Actual Cap Employed

= 7,21,340 - 6,20,000

= ₹1,01,340

B**)** **Intrinsic Value Per Equity Share:**

i) **Net Asset Basis:**

Goodwill		1,01,340
Plant		50,000
Property		1,60,000
Stock		3,10,000
Debtors		2,03,000
Cash		1,17,000
Bank		1,700
		9,43,040
Less : O/s Liabilities		
Term Loans	-	
Curr. Liabilities	2,21,700	- 2,21,700
Less: Preference Share Capital		NIL
Net Assets available for eq. shareholders		7,21,340

$$\text{Intrinsic Value} = \frac{\text{Net Assets available for Equity Shareholders}}{\text{No. of eq. Shares}}$$

$$= \frac{721340}{30000}$$

$$= ₹24.04$$

C) Yield Value: Per equity share

	₹
a) Net Profit before tax	1,97,000
Add: Expenses not to be incurred in future	NIL
Less: Expenses to be incurred in future	NIL
F.M.P. before tax	1,97,000
Less: Tax (as per Balance Sheet)	- 82,500
F.M.P. after tax	1,14,500
Less: Appropriation	
transfer to General Reserve	- 18,033
N.P. available to Equity Share workers	96,467

b) **Expected Rate of Dividend =** $\frac{\text{N.P.available for ESH}}{\text{Paid-up Eq.Capital}} \times 100$

$$= \frac{96467}{300000} \times 100$$

= ₹32.15

c) **Yield** $= \frac{\text{Expected rate of dividend} \times \text{Paid up value shares}}{\text{NRR}}$

$$= \frac{32.15 \times 10}{10}$$

= ₹32.15 per share

Illustration: 5

A shareholder of M Private Ltd. requests you to advise him about the fair value of the equity shares of the Company. The Company's financial position as on 31st December, 1997 is as under:

Liabilities	₹	Assets	₹
Shares Capital:		Fixed Assets (at cost)	

20000 6% Cum. Pref. Shares of ₹10 each		2,00,000	Goodwill	1,20,000
12000 Eq. Shares of ₹20 each		2,40,000	Plant & Machinery	2,00,000
Deb. Redemption Fund		40,000	Investment (at cost)	1,20,000
Profit & Loss A/c:			Current Assets	
Bal. As on 1-1-1987	45,000		Stock	1,20,000
Profit for the year (before tax)	1,30,00	1,75,000	Debtors	1,40,000
5% Debentures		2,00,000	Cash at Bank	1,52,000
Creditors		1,67,000	Land & Building	2,00,000
Depreciation Fund (Plant etc.)		30,000		
		10,52,000		10,52,000

The following information is relevant:

1. Goodwill is revalued at ₹1,45,000/-.
2. Normal rate of return expected is 10%.
3. The share of the company are not freely transferable.
4. Investments are part of business assets.
5. Profit for the year as stated above are before annual transfer of ₹12,700 to Debenture Redemption Fund.
6. Income Tax may be taken at 50% of the profit.
7. Dividend record of the company is not stable.

Work out the fair value of Equity as requested.

Solution:

A) Intrinsic Value :

Step - 1:

Fixed Assets:	₹	₹
Goodwill		1,45,000
Land & Building		2,00,000
Plant & Machinery		2,00,000
Investments		1,20,000
Current Assets:		

Stock	1,20,000
Debtors	1,40,000
Cash at bank	1,52,000
	10,77,000

Less: Liabilities:

Debentures	2,00,000	
Creditors	1,67,000	
Depreciation Fund	30,000	
Provision for taxation	65,000	-4,62,000
		6,15,000
Less: Pref. Share Capital		-2,00,000
Net Assets available for Equity Shareholders		4,15,000

Step - 2:

$$\text{Intrinsic Value} = \frac{\text{Net Assets available for ESH}}{\text{No. of eq. Shares}}$$

$$= \frac{415000}{120000}$$

= 34.58 `/Share

B) Yield Value

Step - 1:

F.M.P. before tax	1,30,000
Less: Tax 50%	-65,000
F.M.P. after tax	65,000
Less: Appropriations	
Dividend on Pref. Shares	-12,000
Deb. Redemption Fund	-12,700
Net Profit available for ESH.	40,300

Step - 2:

$$\text{Expected rate of Dividend} = \frac{\text{N.P.available for ESH}}{\text{Paid up Equity Cap}} \times 100$$

$$= \frac{16.79 \times 20}{12}$$

= 27.98

Fair value of Eq. Share $= \dfrac{34.58 + 27.98}{2}$ $\dfrac{\text{Intrinsic Value} + \text{Yield value}}{2}$

$= ₹31.28$

Illustration - 6

The following is the Balance Sheet of Grishma Ltd. as at 31st December, 2014.

Liabilities	₹	Assets	₹
50000 equity share of ₹10 each fully paid	5,00,000	Fixed Assets	11,00,000
50000 equity share of ₹10 each ₹8 paid	4,00,000	Current Assets	5,50,000
5000 eq. shares of ₹10/- each ₹5 paid up	2,50,000	Preliminary Expenses	50,000
Reserves	2,50,000		
Profit & Loss A/c	2,50,000		
Current Liabilities	50,000		
	17,00,000		17,00,000

The normal avg. profit of the company will be maintained at ₹2,30,000. And normal rate of return is 8%.

Calculate the Intrinsic Value & Yield Value for each type of equity shares. Ignore Taxation & Goodwill.

Also comment upon the value of each paid-up share under both the methods.

Solution:

A) Intrinsic Value:

Step - 1:

Net Assets available to equity shareholders=

All assets at market values including goodwill, non-trade investment but, excluding fictitious assets.

	₹	₹
Fixed Assets	11,00,000	
Current Assets	5,50,000	16,50,000
Less:		
All Liabilities at market values excluding Share Capital & Reserves and Surplus Current Liabilities		- 50,000
Net Assets Available to All Shareholders		16,00,000
Add: Un-called Capital, assuming that call is made & is received (1,00,000+2,50,000)		3,50,000
Net Assets Available to All Shareholders, When All the Shares are Fully Paid-up		19,50,000

Step - 2:

a) Intrinsic Value per fully paid equity share = $\frac{\text{Net Assets as above}}{\text{Total no. of Equity Shares}}$

$$= \frac{1950000}{50000}$$

= ₹13 per equity share

b) **Intrinsic Value per ₹8 paid-up share**

= Intrinsic Value per fully paid equity share - Amount unpaid per share

= ₹13 ₹2

= ₹11 per share

c) Intrinsic Value per ₹5 paid-up share

= Intrinsic value per fully paid equity share-Amount unpaid per share

= ₹13 ₹5

= ₹8 per share

B) Yield Value Per Share

Step - 1:

F.M.P. available to equity shareholders = 230000.

Step - 2:

Capitalised Value of F.M.P $= \dfrac{\text{F.M.P}}{\text{N.R.R.}} \times 100$

$$= \frac{230000}{8} \times 100$$

$= ₹28,75,000$

Step - 3:

$$\text{Yield Value Per Share} = \frac{\text{Capitalised Value of F.M.P.} \times \text{Amount Paid-up Per Equity Share}}{\text{Paid-up Equity Share Capital}}$$

a) Fully Equity Share $= \dfrac{28,75,000}{11,50,000} \times 10$

= ₹25 per share

b) ₹8 Paid up Equity Share $= \dfrac{28,75,000}{11,50,000} \times 8$

= ₹20 per share

c) ₹5 paid up equity share $= \dfrac{28,75,000}{11,50,000} \times 5$

= ₹12.50 per share

C) Comparative Study:

Amount paid-up per share	**Intrinsic Value**	**Yield Values**
a) Fully paid (₹10 paid-up)	₹13 per share	₹25 per share
b) ₹8 paid-up	₹11 per share	₹20 per share
c) ₹5 paid-up	₹8 per share	₹12.50 per share
Conclusion:	The difference in paid Up value is maintained	The proportion of paid up value is maintained.

Illustration :7

The Balance Sheet of Rainbow Ltd. as at 31st December, 2014 as follows:

Liabilities	₹	Assets	₹
Subscribed and paid up Capital:		Goodwill at Cost (Net)	70,000
10,000, 10% Cumulative Pref. Shares of ₹10 each	1,00,000	Freehold Land & Bldg. (W.D.V.)	90,000
20,000 Equity Shares of ₹10 each	2,00,000	Plant (W.D.V.)	2,50,000
Profit & Loss A/c	1,00,000	Investment at cost (Market Value `50,000)	20,000
Bank Overdraft	2,00,000	Stock at Cost	1,00,000
Current liabilities	30,000	Debtors	70,000
		Bank Balance	30,000
	6,30,000		6,30,000

i) Net profits (after writing off goodwill each year by ₹10,000) for the years 2012, 2013 and 2014 amounted to ₹28,000, ₹65,000 and ₹1,10,000 respectively.

ii) The company paid dividend on preference shares each year and on equity shares at item (a) above. Preference shareholders have no participating rights.

iii) Recent valuation of land and building and plant amounted to ₹1,00,000 and ₹5,00,000 respectively. Depreciation on buildings and plant will increase by ₹53,000 per annum in future years.

iv) Worthless stock, included above, which are carried forward since 2000 as it is, amounted to ₹90,000. Estimated realizable value thereof is ₹10,000.

What value would you place on each equity share based on

i) Net assets (Excluding Goodwill) and

ii)Capital Value of Maintainable profits, which is agreed to be the weighted average net profits (weight age being 1,2 & 3) of past three years, capitalization rate being 8.1/3%.

Confine to data given only. Ignore Tax.

(T.Y.B.Com. April, 1999)

Solution:

i) Net Asset Value (excluding Goodwill)

a) Amount available to Equity Shareholders**.**

	₹	₹
All Assets at Market Value		
Land and Building		1,00,000
Plant		5,00,000
Investment		50,000
Stock	1,00,000	
Less: Worthless Stock	90,000	
Stock having worth	10,000	
Add: Estimated realizable value of worthless Stock	10,000	20,000
Debtors		70,000
Bank Balance		30,000
Gross Realisation		7,70,000
Less: **Liabilities**		
Current liabilities	30,000	
Bank Overdraft	2,00,000	2,30,000
		5,40,000
Less: Preference Share Capital		1,00,000
Amount available to Equity Shareholders		4,40,000

b) Net assets value $= \dfrac{\text{Amount available to Equity Shareholders}}{\text{No of Equity Shares}}$

$$= \frac{4,40,000}{20,000}$$

= 22 `/share

ii) Capitalised Value of Maintainable Profits

a) F.M.P.

Year	Profit after Goodwill ₹	+Goodwill written off ₹	+Dividend on Equity ₹	=	Trading Profit ₹
2012	28,000	+ 10,000		=	38,000
2013	65,000	+ 10,000	20,000	=	95,000
2014	1,10,000	+ 10,000		=	1,20,000
					2,33,000
	Trading Profit	X	weight assigned	=	Product
	38,000	X	1	=	38,000
	95,000	X	2	=	1,90,000
	1,20,000	X	3	=	3,60,000
					₹5,88,000

Weighted Average Profit = $\frac{\text{Total Product}}{\text{Total Weight}} = \frac{5,88,000}{6} =$ ₹98,000

Weighted Average Profit = 98,000

Less: Increase in Depreciation = 53,000

F.M.P. = 45,000

b) **Capitalised value of F.M.P. at N.R.R.** = $\frac{100}{\text{N.R.R.}} \times \text{F.M.P.}$

$$= \frac{100}{8\frac{1}{3}} \times 45,000$$

$$= 45,000 \times 100 \times \frac{3}{25} = ₹5,40,000$$

c) **Value of a Share** = $\frac{\text{Capitalised Value of F.M.P.}}{\text{No. of Equity Sahres}}$

$$= \frac{5,40,000}{20,000}$$

= ₹27

Illustration : 8

Mr. Kulkarni intends to invest `33,000 in Equity Shares of a Limited Company and seeks your advice as to the maximum numbers of shares he can expect to acquire based on a fair value of the shares to be determined by you. the following information is available.

	₹
Issued and paid up Capital 6% Preference Shares of `100 each	5,50,000
Equity Shares of `10 each.	3,50,000
	9,00,000

Average net profit of the Business is ₹75,000. Expected normal yield is 8% in case of such Equity Shares. It is observed that the net assets on revaluation are worth ₹70,000 more than the amounts at which they are stated in the books. Goodwill is the be calculated at 5 years' purchase of the super profits, if any ignore taxation.

Solution:

i) Goodwill
Super Profit = F.M.P. - Normal Profit

a) F.M.P.: 75,000 (Given)

b) $\text{Normal Profit} = \frac{\text{N.P.R.}}{100} \times \text{Average Capital Employed (A.C.E.)}$

A.C.E.

The net assets at book value at the end of the year are equal to paid up capital of the Co. It is mentioned in the problem that the net assets on revaluation are worth ₹70,000 more than their book value. Therefore the realized value of net assets is 9,00,000 + 70,000 = 9,70,000.

Tangible Capital employed at the end of the year is assumed to be equal to `9,70,000. It is assumed that profit is not withdrawn from business.

	`
A.C.E =	
Capital at the end of the year	9,70,000
Less: 1/2 of the Profit earned $\left(\frac{1}{2}\times 75,000\right)$	(37,500)
A.C.E. during the year	9,32,500

Normal Profit $= \frac{\text{N.R.R.}}{100} \times \text{A.C.E}$

$= \frac{8}{100} \times 9,32,500 = 74,600$

Super Profit = F.M.P. - Normal Profit

= 75,000 - 74,600 = 400

Goodwill = Super Profit x No. of years purchase

= 400 x 5 years

= ₹2,000

ii) Valuation of Shares

a) Intrinsic Value

1. Amount available to Equity Shareholders

	₹
Net Assets at Market Value	9,70,000
Add: Goodwill	+ 2,000
Total Assets available to Equity Shareholder	9,72,000
Less: Claims of Preference Shareholders (Preference Share Capital	(5,50,000)
Amount available to Equity Shareholders	4,22,000

2. Intyrinsic Value $= \frac{\text{Amount available to Equity Shareholders}}{\text{No. of Equity Shares}}$

$= \frac{4,22,000}{35,000}$

= ₹12.06

b) The Yield Value

	₹
1. F.M.P.	
Average Profit	75,000
Less: Preference Dividend $\left(\frac{6}{100}\times 5,50,000\right)$	33,000
F.M.P.	42,000

2. **Rate of F.M.P.** = $\frac{\text{F.M.P.}}{\text{Paid up Equity Capital}} \times 100$

$$= \frac{42,000}{3,50,000} \times = 12\%$$

3. **Yield Value** =

$\frac{\text{Ratio of F.M.P.}}{\text{N.R.R.}} \times \text{Amount paid per Equity Share}$

$$= \frac{12}{8} \times 10$$

= ₹15

c) Fair Value

$\frac{\text{Intrinsic Value + Yield Value}}{2}$

$= \frac{12.06+15}{2} = \frac{27.06}{2}$

= ₹13.53

d) No of Shares to be acquired:

$\frac{\text{Investment}}{\text{Fair Value}} = \frac{33,000}{13.53}$

= 2439 Share. Mr. Kulkarni can acquired 2439 shares @13.53.

Illustration : 9

Below is given the Balance Sheet of Trisure Ltd. as at 31st December 2014.

Liabilities		₹	Assets	₹
Equity Shares of ₹10 each	2,00,000		Goodwill	20,000
Less: Calls in Arrear (₹2 for final call)	(5,000)	1,95,000	Machinery	1,10,000
6% Preference Shares of ₹10 each	1,00,000		Land and Building	1,20,000
Less: Calls in Arrear (₹2 for final call	(1,000)	99,000	Furniture and Fixtures	60,000
General Reserve		80,000	Vehicles	80,000
P & L A/c	16,000		Investments	80,000
Bank Loan		60,000	Stock in Trade	55,000
Sundry Creditors	1,55,000		Sundry Debtors	90,000
Bills Payable			Cash at Bank	10,000
			Preliminary Expenses	10,000
		6,35,000		6,35,000

For the purpose of valuation of shares, Goodwill is to be considered on the basis of 2 years' purchase of the super profits based on average profit of least 4 years. Profits are as follows:

2011: ₹80,000; 2012: ₹90,000; 2013: ₹1,05,000; 2014: ₹1,10,000 In a similar business normal return on capital employed is 5%.

Fixed assets are worth 30% above their actual book value. Stock is over-valued ₹5,000. Debtors are to be reduced by ₹1,000. All trade investments are to be value investments were purchased on 1-1-2012 5% of the non-trade investments were acquire on 1-1-2012 and the rest on 1-1-2013.

A uniform rate of dividend of 10% is earned on all investments.

i) In 2012 a new machinery costing ₹10,000 was purchased but wrongly charged to revenue. (No rectification has yet been made for above).

ii) In 2013, some old furniture (Book value ₹5,000) was disposed of for ₹3,000. You are required to value each fully paid and partly paid equity share. (Depreciation is charged on machinery @ 10% on reducing balance system. Ignore Taxation an Dividend).

(T.Y.B.Com Nov., 1991)

Solution:

	₹
Investments as per B/S	8,00,000
Less: Trade Investment (10% of 80,000)	8,000
Non Trade Investments	72,000
Loss on Valuation of Trade Investment $\left(\frac{10}{100}\times 8,000\right)$	800
Value of Trade Investment (8,000 - 800)	7,200
Non Trade Investment	72,000
Less: 5% of 72,000 acquired on 1-1-2000	3,600
Acquired on 1-1-	68,400

2. Dr. Non-Trade Investment A/c. Cr.

Date	Particulars	₹	Date	Particulars	₹
Jan.1,2012	To Bank	68,400	Dec.31,2012	By Balance c/d	68,400
Jan.1 2013	To Balance c/d	68,400	Dec.13,2013	By Balance c/d	72,000
Jan.1,2013	To Bank	3,600			
		72,000			72,000
Jan.1,2014	To Balance b/d	72,000	Dec.31,2014	By Balance e/d	72,000
		72,000			72,000

Rate of interest on non-trading investment is also 10% interest.

3. Interest on non-trade Investment

Date	Interest	₹
31-12-2012	$\frac{10}{100}\times 68,400$	6,840
31-12-2013	$\frac{10}{100}\times 72,000$	7,200
31-12-2014	$\frac{10}{100}\times 7,200$	7,200

4. Machinery

i) ₹10,000 should be added to profit of 2012.

ii) As machinery was charged to Profit and Loss Account i.e. to revenue, no depreciation on it was provided.

iii) The profits reported in the problem are before providing for depreciation on machinery of `10,000. While calculating F.M.P. the errors is to be rectified and depreciation is to be provided @ 10% p.a. on Reducing Balance Method.

Depreciation on Machinery

		₹
2012	Cost of Machinery	10,000
	Less: Depreciation (10% of 10,000)	1,000
		9,000
2013	Less: Depreciation (10% of 9,000)	900
		8,100
2014	Less: Depreciation (10% of 8,100)	810
	Written down Value to be considered	7,290

5. Loss on Sale of Furniture

(5,000 - 3,000 = 2,000)

₹2,000 loss on sale of furniture is an abnormal loss which should be added to the Profit of 2013 for deciding F.M.P. Super Profit = F.M.P. - Normal Profit.

ii) F.M.P.

	2011 ₹	2012 ₹	2013 ₹	2014 ₹
Reported Profits	80,000	90,000	1,05,000	1,10,000
i) Over Valuation of Stock				- 5,000
ii) Reduction in Debtors				- 1,000
iii) Loss on Revaluation of Trade Investment				- 800
iv) Interest on Non-Trade Investment		- 6,840	- 7,200	- 7,200
v) Machinery Charged to Revenue		+ 10,000		

vi) Depreciation on Machinery		- 1,000	- 900	- 810
vii) Loss on Sale of Furniture	-	-	+ 2,000	-
Trading Profits	80,000	92,160	98,900	95,190

Average Trading Profit = $\frac{80,000+92,160+,98,900+95,190}{4}$

$= \frac{3,66,250}{4}$

= ₹91,563

ii) **Normal Profit** = $\frac{\text{N.R.R.}}{100} \times \text{ACE}$

ACE

	₹	`
Tangible Trading Assets Machinery		1,10,000
Add: w/d/v of Machine charged as Expenses		7,290
		1,17,290
Land & Building		1,20,000
Furniture & Fixture		60,000
Vehicles		80,000
Book Vale of All Fixed Assets		3,77,290
Add: 30% of Book Value		1,13,187
Revised Value		4,90,477
Trade Investment		7,200
Stock in Trade	55,000	
Less: Over Valuation	- 5,000	50,000
Debtors	90,000	
Less: Reduction	1,000	89,000
Bank Balance		10,000
		6,46,677
Less: Liabilities		
Bank Loan	60,000	
Sundry Creditors	1,55,000	
B/P	30,000	2,45,000
Tangible Trading Capital at the end of the year `		4,01,0677

$\therefore$ **A.C.E.** = ₹4,01,677

Normal Profit = $\frac{\text{NRR}}{100} \times \text{A.C.E.}$

$= \frac{5}{100} \times 4,01,677 = 20,083.85 =$ ₹20,084

Super Profit = F.M.P. - Nominal Profit

= 91,563 - 20,084 = ₹71,479

Goodwill = Super Profit x No. of years purchase

= 71,479 x 2 = ₹1,42,958

Net Assets Value (Intrinsic Value)

Amount available to Equity Shareholders

	₹	₹
Net Tangible Trading Assets		4,01,677
Add: Goodwill		1,42,958
Non Trading Investments		72,000
Calls in Arrears: Equity	5,000	
Preference	1,000	6,000
		6,22,635
Less: Preference Share Capital		1,00,000
Amount available to Equity Shareholders		5,22,635

Net Asset Value of a Share = $\frac{\text{Amount available to Equity Shareholders}}{\text{No.of Equity Shares}}$

$= \frac{5,22,635}{20,000} =$ `26.13 P/s

Fully paid eq. share value of fully paid eq. Share = 26.13 less calls in arrears per share 2 value of partly paid equity's share 24.13 [26.13 - 2]

Illustration : 10

From the following Balance Sheet you are required to value the Equity Share assuming that the preference shares are, alternatively (i) non-participating or (ii) participating.

Liabilities	₹	Assets	₹
2,000, 6% Preference Shares of `100 each	2,00,000	Assets at Book Value	6,00,000
30,000 Equity Shares of `10 each	3,00,000		
Liabilities	1,00,000		
	6,00,000		6,00,000

The market value of half of the assets is considered at 10% more than the Book Value, and that of remaining half at 5 per cent less than the Book Value. There was a liability of `5,000 which remained unrecorded.

(April 95, adapted)

Solution:

Valuation of Equity Shares (Net Assets Method)

i) Assuming Pref. Shares to be Non-Participating

Gross Assets:	₹	₹
Book Value of 1/2 assets	3,00,000	
Add: 10% increase	30,000	3,00,000
Book Value of remaining assets	3,00,000	
Less: 5% decrease	- 15,000	+ 2,85,000
		6,15,000
Less: External Liabilities		
Book Value of Liabilities	1,00,000	
Add: Unrecorded Liability	+ 5,000	(1,05,000)
Net Assets (available to all shareholders)		5,10,000
Less: Due to Preference Shareholders		2,00,000
Net Assets available to Equity Shareholders		3,10,000

Note: When pref. shares are not participating Due to Preference should will be equity to it paid capital to arrears of dividend if any.

$$\text{Value Per Equity Share} = \frac{\text{Net Assets for Equity Shareholders}}{\text{No. of Equity Shares}}$$

$$= \frac{3,10,000}{30,000}$$

$$= ₹10.33$$

ii) **Assuming Pref. Shares to be Participating [Surplus assets to be divided in the ratio of pays-up Capital]**

	₹
Net Assets available to Equity Shareholders	3,10,000
Less: Equity Share Capital	3,00,000
Surplus on Liquidation	10,000
Ratio of Pref. & Equity Paid-up Capital = 2:3.	
Surplus divided in above ratio	
Preference Shares (10,000 x 2/5)	4,000
Equity Shares (10,000 x 315)	6,000
Value of Preference Share 2,04,000 / 2,000	102.00
Value of Equity Share 3,06,000/30,000	10.20

Illustration : 11

Rana & Ltd. presents the following Balance Sheet on 31st December, 2014.

Liabilities	₹	Assets	₹
Share Capital (`10/- each)	3,00,000	Assets	4,50,000
Reserves	1,20,000	Current Assets	30,000
Loans	50,000		
Current Liabilities	10,000		
	4,80,000		4,80,000

It is observed that fixed assets are undervalued by ₹30,000.

The current assets are overvalued by ₹2,000. The assets are to be valued properly.

It is proposed to issue fully paid shares by capitalization of General Reserves in ratio of one share for three shares held. Find the value of shares.

i) Before Issue of Bonus Shares; and

ii) After Issue of Bonus Shares.

Solution:

Valuation of Equity Shares (Net Assets Method)

Gross Assets:	₹	₹
Fixed Assets (4,50,000+30,000)		4,80,000
Current Assets (30,000-2,000)		28,000
		5,08,000
Less: Liabilities		
i) Loans	50,000	
ii) Current Liabilities	10,000	60,000
		4,48,000

Net Assets available to Equity Shareholders

Value Per Fully Paid Equity Share (Before Bonus Issue)

$$= \frac{\text{Net Assets for Equity Shareholders}}{\text{No. of Equity Shares}} = \frac{4,48,000}{30,000} = \text{`}14.93$$

Value Per Fully Paid Equity Share (after Bonus Issue)

$$= \frac{\text{Net Assets for Equity Shareholders}}{\text{No. of Equity Shares}} = \frac{4,48,000}{40,000} = \text{`}11.20$$

Note: Number of Bonus Share Issued : 1/3 of 30,000 = 10,000. Equity Shares

$\therefore$ Number of Equity Shares after Bonus

= 30,000 + 10,000 = 40,000 Equity Shares

Illustration : 12

Gem Limited submits the following information as on 31st March, 2015.

		`
i)	Fixed Assets (Tangibles)	15,00,000
ii)	Current Assets	6,00,000
iii)	Patent Rights	2,50,000
iv)	Investments	1,00,000
v)	Capital Issue Expenses	50,000
vi)	Liabilities	4,00,000

Capital comprises of 12,500 shares of ₹100/- each fully paid. It is ascertained that Patent Right are valueless. Ascertain the value of shares on asset backing method.

(Oct. 97, adapted)

Solution:

Valuation of Equity Shares (Net Assets Method)

Gross Tangible Assets	₹
Fixed Assets	15,00,000
Current Assets	6,00,000
Investments	1,00,000
	22,00,000
Less : Liabilities	(4,00,000)
Net Assets available to Equity Shareholders	18,00,000

$$\text{Value Per Fully Paid Equity Share} = \frac{\text{Net Assets for Equity Shareholders}}{\text{No. of Equity Shares}}$$

$$= \frac{18,00,000}{12,500} = ₹144$$

Note: Patents being valueless and Capital Issue Expenses being an intangible asset are ignored while computing gross assets value.

5.10 EXERCISE:

1. Specify the circumstances when valuation of shares in required.
2. Explain the methods for valuation of equity shares for varying circumstances.
3. Specify different classes of shares for purpose of valuation.
4. Write Short Notes.
   a) Valuation when shares have differing paid-up value.
   b) Valuation of Preference Shares.
   c) Fair Value of Shares.
   d) Earning Capacity Method.
   e) Yield value of Shares.
5. Objective Type Questions:

A. Fill in the blanks

a. **Fair value** of Equity share is Average of Intrinsic Value & Yield value

b. Break- up value of Equity share is also known as **Intrinsic Value**.

c. Fictitious assets not considered for ascertaining **Intrinsic Value** of Equity share.

d. Shares are often **Pledged** as security for raising loans.

e. Shares of **Private Ltd.** companies are not listed on the stock exchange.

f. Intrinsic Value of Share = Net Assets available to Equity shareholders / No of shares Equity shares.

g. Net Assets available to Equity shareholders == Equity Shareholders fund

h. Capitalised Value of Share = Capitalised Value of **FMP÷** total No. of equity Shares.

i. **Intrinsic value** aims to find out the possible value of share in at the time Liquidation of the company

j. Dividend Yield Method Value of Share =[Expected Rate of Dividend X Paid UP Value of Share] x **Normal Rate of Dividend.**

k. **Participating** Preference shareholder entitled to share in the surplus arising on Liquidation.

l. The Claim **Preference** Shareholders must also be deducted from the Net Assets to ascertain the value of an Equity Share.

m. Yield Method of valuation of shares is based on **Profitability**

A. Multiple Choice Questions

1. Intrinsic valuation method also known as :

a] Assets backing,
b] Net assets value
c] Break –up value ,
d] **All of the above**

2] The value of share under the Intrinsic Value method is worked out excluding:

a] Net outsider liabilities,

b**] Non trade assets**

c] Equity Shareholder’s fund,

d] Total assets

3] Intrinsic value is calculated after deducting from Net Assets :

a] **Preference share capital**

b] Non trade liabilities

c]Goodwill

d] Equity share capital

4] Intrinsic value of equity share is calculated after adding to net trading assets:

a] Goodwill

b] Preference share capital

c] Gross block

d] Bank overdraft

5] Preference shareholder entitled to share in the surplus arising on liquidation:

a] Non- cumulative preference share

b] Participating preference shares

c] Convertible preference share

d] Reissue of forfeited shares

6] Intrinsic value method ignores:

a] Goodwill,

b] **Earnings,**

c] Going concern concepts,

d] Dividend

7] Intrinsic Value Share is worked out after considering:

a] Authorised share capital

b] Paid up equity share Capital

c] Non Trade Investments

d] Fictitious Assets

8] Fair value method of share valuation considers valuation:

a] No. of equity shares

b] Intrinsic value

c] yield value

d] b & c of above

10] Yield value of Equity share is worked out from:
a]Intrinsic value,
b] Net Profit after Tax
c] **Earnings available to equity share-holders**
d] Fair value

11] Fair value of equity shares is considered when investor's want to have:
a**] Controlling power**
b] Listing shares in share market,
c] Earning capacity
d] None of the above.

12] Consider the following information relating to BSHU Ltd. 20,000 Equity shares of Rs.100 each, 20,00,000, 30,000 Equity shares of Rs.100 , Rs.80 paid up 24,00,000, 25,000, Preference shares of Rs.100 25,00,000
Net Assets available to Equity shareholders 1,20,00,000
Intrinsic value of Rs.80 paid up share,:
a]Rs. 240,
b] Rs.220,
c] Rs.252,
d] Rs. 232

13]Consider the following information relating to ASHOK Ltd.
20,000 Equity shares of Rs.100 each, 20,00,000
NET Assets available to Equity shareholders 1,20,00,000

Ashok ltd. declared bonus shares @ three shares for every two shares.
Intrinsic value of fully paid up share after bonus:
a] Rs.300,
b] Rs.240,
c]Rs. 250,
d] None of the above

14] Consider the following information relating to Z.. Ltd.
40,000 Equity shares of Rs.100 each, 40,00,000
10% Preference shares of Rs. 100 each 5,00,000
NET Assets available to Equity shareholders 1,25,00,000
Z ltd. Declared right @ one for every four shares at Rs.300.

Value of equity share after right:
a] Rs.300
b] Rs.310
c] Rs.290
d] none of the above

15] While calculating Yield value of share, from net profit after tax , amounts to be deducted :
a] Preference Dividend
b] Tax
c] Equity dividend
d] Preference share capital

16] For calculating earning capacity value of equity share, capital employed should be:
a] Owner's fund + Owed fund,
b] **Equity shareholder's fund,**
c] Owed fund
d] Total liabilities

C. **Match the Columns:**

1.

Column : A	Column: B
1.Fair Value of Equity Share 2. Intrinsic Value 3. Yield Value 4. Goodwill 5. Proposed Dividend	A Going concern B . Intangible Asset C. Net Asset Method D Average of intrinsic & yield value E. Current Liabilities F. Current Assets

Answer: 1- D, 2-C,3-A,4-B,5-E

2.

Column : A	Column : B

1. Non-Participating Preference Shares 2. Yield Value 3. Intrinsic Value 4. Dividend basis valuation 5. F.M.P.	A. Basis on Earnings B. Ignores the earning of company C. Earnings available to Equity-shareholders D. Not entitled in surplus on liquidation E. Profitability of business F. Earnings before tax

Answers: 1-D,2-C,3-B,4- A, 5-E

D. True or False

1. Share valuation is must while admitting new partner to firm **False**
2. Fair value = (Intrinsic value + yield Value)/2 **True**
3. Intrinsic valuation of shares is based on the assumption of Liquidity. **True**
4. Calls in arrears are not considered while finding out Intrinsic value of shares **False**
5. Goodwill is not considered in intrinsic value. **False**
6. Yield value of shares is based on the assumption of going Concern. **True**
7. Dividend on preference shares is subtracted from FMP while calculating Yield Value. **True**
8. Intrinsic Value of Partly paid Equity share= Intrinsic value of fully paid equity share- Calls in arrears per share **True**
9. Yield Value of Partly paid Equity share= Yield value of fully paid equity share- Calls in arrears per share **False**
10. Transfer to reserve is not considered while finding Yield value. **False**
11. Future Maintainable profit is considered in finding Intrinsic Value. **False**
12. Income received on non-trade investments is not to be subtracted from FMP in Yield valuation. **True**

13. Premium payable on redemption of preference shares is ignored in finding intrinsic value. **False**
14. Premium payable on redemption of preference shares is ignored in finding Yield value. **True**

❖❖❖❖

12

ACCOUNTING FOR FOREIGN CURRENCY TRANSACTIONS-I

Unit Structure

20.0 OBJECTIVES:

After studying the unit the students will be able to:

- Know the meaning of Foreign currency transactions
- Understand the Need for conversion
- Explain the Recognition of exchange fluctuation
- Know the Translation of foreign currency transactions
- Solve the practical problems on Foreign currency transactions

20.1 INTRODUCTION:

A transaction like sale or purchase of goods involves two parties. Whenever such transaction is entered with another party situated in India, the transaction is in Indian currency, recording of such transaction does not pose any problem. But if the other party is located outside India then the transaction entered might be in foreign currency and then we have to translate this transaction from foreign currency into India currency. This translation is done by applying the foreign exchange rates prevailing at the time of transaction. Accounting Standard 11 deals with recording and translation of such type of foreign currency transactions.

20.2 ACCOUNTING STANDARD NO.11(REVISED) ISSUED BY THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA :

This standard is applicable from 1.04.2004. This standard is mandatory in nature.

20.2.1 OBJECTIVE:

The transactions entered into by an organization in foreign currency must be included in the financial statements of the organization in its reporting currency.

20.2.2 SCOPE:

1. The standard should be applied in accounting for transactions entered in foreign currencies.
2. This standard also deals with accounting for foreign currency transactions in the nature of forward exchange contracts.
3. This standard does not specify the currency of presentation of financial statements. Normally an organisation prepares its financial statements in currency of home country.
4. The standard does not deal with the restatement of an enterprise's financial statements from its reporting currency into another currency for the convenience for user accustomed to that currency of for similar purpose.
5. This standard does not deal with the presentation in a cash flow statement of cash flows arising from transactions in a foreign currency and the transactions of cash flows of a foreign operation.
6. This standard does not deal with the exchange difference arising from foreign currency borrowings to the extent that they are regarded as an adjustment interest cost.

20.2.3 DEFINITIONS:

The following terms are used in this Statement with meanings specified:

(a) **Average rate** is the mean of the exchange rates in force during a period.

(b) **Closing rate** is the exchange rate at the Balance Sheet date.

(c) **Exchange Difference** is the difference resulting from reporting the same number of units of a foreign currency in the reporting currency at different exchange rates.

(d) **Exchange rate** is the ratio for exchange of two currencies.

(e) **Fair value** is the amount for which an asset could be exchanged or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

(f) **Foreign Currency** is a currency other than the reporting currency of an enterprise.

(g) **Monetary items** are money held and assets and liabilities to be received or paid in fixed or determinable amounts of money.e.g. Cash, Receivables, Payables etc.

(h) **Non-monetary items** are assets and liabilities other than monetary items.e.g. Fixed Assets, Inventories, Investments etc.

(i) **Reporting currency** is the currency used in presenting the financial statements.

20.3 ACCOUNTING PROCEDURE:

Record the initial transaction entered in foreign currency by converting in Indian Rs. by multiplying the transaction amount with the foreign exchange rate as on the date of transaction.

Subsequently when the payment is made or is received in the same year it should be recorded at foreign exchange rate on the date of settlement. Any profit or loss arising due to exchange fluctuation should be treated as revenue item, and hence it should be transferred to profit and loss A/c. at the end of the year.

Any balance payable or receivable to or from a foreign party, at the end of year, should be adjusted at the closing foreign exchange rate.

The foreign exchange rate for any payment made or received in the subsequent year should be compared with the closing rate of the earlier year to find the profit or loss on exchange fluctuations.

20.4 PROFORMA JOURNAL ENTRIES:

20.4.1 Transactions which need to be translated:

Following four types of transactions are required to be translated.

I. Import of goods

II. Export of goods

III. Purchase of Fixed Assets

IV. Foreign currency loans

X = Amount of transaction in Foreign Currency

$R_1 =$ Foreign Exchange on the date of transaction

$R_2 =$ Foreign Exchange on the date of settlement

$R_3 =$ Foreign Exchange on the date of Year End

$R_4 =$ Foreign Exchange on the date of settlement in the next year.

20.4.2 Import of goods

Sr. no	Particulars	Dr. Rs	Cr. Rs.
1.	**Purchase of goods/ raw materials**		
	Purchases A/c Dr.	X R_1	
	To Foreign Supplier A/c		X R_1
2.	**Payment to foreign supplier**		
	Foreign Supplier A/c Dr.	X R_1	
	Foreign Exchange Fluctuation A/c (if loss) Dr.	$X(R_{2}- R_{1})$	
	To Foreign exchange Fluctuation A/c (if Profit)		$X(R_{1}- R_2)$
	To Bank A/c		X R_2
3.	Year end adjustments		
A.	**Adjusting closing balance payable to foreign suppliers**		
	A- If closing rate is more than transaction rate(loss i.e. $R_3 > R_1$)		
	Foreign Exchange Fluctuation A/c Dr.	$X(R_3 - R_1)$	
	To Foreign Supplier A/c.		$X(R_3 - R_1)$
	OR B if closing rate is less than the transaction rate (Profit i.e. $R_1 > R_3$)		
	Foreign Supplier A/c. Dr	$X(R_1 – R_3)$	
	To Foreign Exchange Fluctuation A/c		$X(R_1 – R_3)$
B.	Closing of nominal A/c.		
	A- If foreign exchange fluctuation A/c shows credit balance		
	Foreign Exchange Fluctuation A/c Dr.	XX	
	To Profit & Loss A/c		XX
	OR B- If foreign exchange fluctuation A/c shows Debit balance		
	Profit & Loss A/c Dr	XX	
	To Foreign Exchange Fluctuation A/c		XX
4.	Payment to foreign supplier in the next year		
	Foreign Supplier A/c Dr.	XR_3	
	Foreign Exchange Fluctuation A/c (if loss) Dr.	$X(R_4 - R_3)$	
	To exchange Fluctuation A/c(if profit)		$X(R_3 - R_4)$

Sr. no	Particulars	Dr. Rs	Cr. Rs.
1.	**Export of goods**		

	Foreign Customer A/c Dr.	X R_1	
	To Export Sales A/c		X R_1
2.	**Receiving Payment from Foreign Customer**		
	Bank A/c. Dr.	X R_2	
	Foreign Exchange Fluctuation A/c. (If Loss) Dr.	X($R_2 – R_1$)	
	To Foreign Exchange Fluctuation A/c. (If profit)		X($R_1 – R_2$)
	To foreign Customer A/c.		X R_1
3.	Year end Adjustments		
A	Adjusting Closing balance receivable from foreign customer		
	A- If closing rate is more than the transaction rate (Profit $R_3 > R_1$)		
	Foreign customer A/c Dr	X(R_3 - R_1)	
	To Foreign Exchange Fluctuation A/c		X(R_3 - R_1)
	Adjusting Closing balance receivable from foreign customer		
	B- If closing rate is less than the transaction rate (Loss ($R_1 > R_3$)		
	Foreign Exchange Fluctuation A/c Dr.	X($R_1 – R_3$)	
	To Foreign customer A/c		X($R_1 – R_3$)
B	Closing of nominal A/c.		
	A- If foreign exchange fluctuation A/c shows credit balance		
	Foreign Exchange Fluctuation A/c Dr.	XX	
	To Profit & Loss A/c		XX
	B- If foreign exchange fluctuation A/c shows Debit balance		
	Profit & Loss A/c Dr	XX	
	To Foreign Exchange Fluctuation A/c		XX
4.	**Receiving payment from foreign customer in the next Year**		
	Bank A/c. Dr.	X R_4	
	Foreign Exchange Fluctuation A/c. (If Loss) Dr.	X($R_4 – R_3$)	
	To Foreign Exchange Fluctuation A/c. (If profit)		X($R_3 – R_4$)
	To foreign Customer A/c.		X R_3

20.4.3 Purchase of Fixed Assets

Sr.no	**Particulars**	**Dr. Rs**	**Cr. Rs.**
1.	**Purchase of Fixed Assets**		
	Fixed Assets A/c Dr.	X R_1	

	To Foreign Supplier A/c.		X R_1
2.	**Payment To foreign supplier**		
	Foreign Supplier A/c Dr.	X R_1	
	Foreign Exchange Fluctuation A/c (if loss) Dr.	X$(R_2 - R_1)$	
	To exchange Fluctuation A/c		X$(R_1 - R_2)$
	To Bank A/c		X R_2
3.	**Year end adjustments**		
A	Adjusting closing balance payable to foreign suppliers		
	A- If closing rate is more than transaction rate (loss $R_3 > R_1$)		
	Foreign Exchange Fluctuation A/c Dr.	X$(R_3 - R_1)$	
	To Foreign Supplier A/c.		X$(R_3 - R_1)$
	B if closing rates is less than the transaction rate (Profit $R_3 > R_1$)		
	Foreign Supplier A/c. Dr	X$(R_1 – R_3)$	
	To Foreign Exchange Fluctuation A/c		X$(R_1 – R_3)$
B	Providing Depreciation		
	Depreciation A/c. Dr.	XX	
	To Fixed Assets A/c.		XX
	Note: Depreciation should be provided on original amount		
C	Closing of nominal A/c.		
	A- If foreign exchange fluctuation A/c shows credit balance		
	Foreign Exchange Fluctuation A/c Dr.	XX	
	To Profit & Loss A/c		XX
	B- If foreign exchange fluctuation A/c shows Debit balance		
	Profit & Loss A/c Dr	XX	
	To Foreign Exchange Fluctuation A/c		XX
	C- Profit & Loss A/c. Dr.	XX	
	To Depreciation A/c.		XX
4.	**Payment to foreign supplier in the next year**		
	Foreign Supplier A/c Dr.	X R_3	
	Foreign Exchange Fluctuation A/c (if loss) Dr.	X$(R_3 – R_4)$	
	To exchange Fluctuation A/c		X$(R_4 – R_3)$
	To Bank A/c		X R_4

Note: Accounting treatment of profit/loss arising out of fluctuation of foreign currency exchange rate while making payment for purchase of Fixed Assets by a Ltd company

According AS 11 profit/loss arising out of fluctuation of foreign currency exchange rate should be treated as revenue item. This is applicable even in case of fixed assets.

However, as per Schedule VI of Company Act 1956, requirements such exchange difference should be adjusted in the cost of respective fixed assets.

Since the syllabus of T Y B Com specifically states the application of AS 11 student should follow the AS11 and accordingly any such Profit/loss should be treated as revenue item.

20.4.4 Foreign Currency Loan Account

Sr.no	Particulars	Dr. Rs	Cr. Rs.
1.	**Availing the foreign currency loan**		
	Bank A/c Dr.	$X R_1$	
	To Foreign Currency Loan A/c		$X R_1$
2.	**Part Re-payment to foreign currency loan**		
	Foreign Currency Loan A/c Dr.	$X R_1$	
	Foreign Exchange Fluctuation A/c (if loss) Dr.	$X(R_{2-} R_{1)}$	
	To Foreign Exchange Fluctuation A/c		$X(R_{1-} R_2)$
	To Bank A/c		$X R_2$
3.	**Payment of Interest**		
	Interest A/c Dr.	XX	
	To Bank		XX
	(Interest Should be calculated on the loan in foreign currency & then it should be converted into Indian Rupees)		
4.	**Year end adjustments**		
A.	Adjusting closing balance payable to foreign currency loan		
	A- If closing rate is more than transaction rate(loss i.e. $R_3 > R_1$)		
	Foreign Exchange Fluctuation A/c Dr.	$X(R_3 - R_1)$	
	To Foreign currency loan A/c.		$X(R_3 - R_1)$
	Or B if closing rate is less than the transaction rate (Profit i.e. $R_1 > R_3$)		
	Foreign currency loan A/c. Dr	$X(R_1 – R_3)$	
	To Foreign Exchange Fluctuation A/c		$X(R_1 – R_3)$
B.	If the interest payment dates & year end date are different then provide for outstanding interest as follows		

	Interest A/c Dr	XX	
	To Outstanding Interest A/c		XX
	(Interest Should be calculated on the loan in foreign currency & then it should be converted into Indian Rupees)		
C.	Closing of nominal A/c.		
	A- If foreign exchange fluctuation A/c shows credit balance		
	Foreign Exchange Fluctuation A/c Dr.	XX	
	To Profit & Loss A/c		XX
	OR B- If foreign exchange fluctuation A/c shows Debit balance		
	Profit & Loss A/c Dr	XX	
	To Foreign Exchange Fluctuation A/c		XX
	C- Interest A/c		
	Profit & Loss A/c Dr	XX	
	To Interest A/c		XX
5.	**Payment to foreign Currency loan in the next year**		
	Foreign Currency loan A/c Dr.	XR_3	
	Foreign Exchange Fluctuation A/c (if loss) Dr.	$X(R_4 - R_3)$	
	To exchange Fluctuation A/c (if profit)		$X(R_3 - R_4)$
	To Bank		XR_4
6.	**Payment of Outstanding Interest in the Next Year**		
	Outstanding Interest A/c Dr.	$X R_3$	
	Foreign Exchange Fluctuation A/c (if loss) Dr.	$X(R_{4-} R_{3)}$	
	To Foreign exchange Fluctuation A/c		$X(R_{3-} R_4)$
	To Bank A/c		$X R_4$

- Give the Journal Entries for the following transaction
    1. Payment to foreign supplier if there is profit.
    2. Availing the foreign currency loan.

3. Yearend adjustments.

21.3 EXERCISES :

1. Define the following terms
    a. Average rate
    b. Closing Rate
    c. Exchange Rate
    d. Fair Value
    e. Monitory Items
    f. Non-Monitory Items

2. OBJECTIVE TYPE QUESTIONS

A. Multiple Choice Questions :

1. The exchange rate at the balance sheet date is known as
    (a) Average Rate (b) Closing Rate
    (c) Non-monetary Rate (d) Monetary Rate

2. Reporting currency is the currency used
    (a) In recording the financial transactions
    (b) In presenting the financial statements
    (c) In settling the financial transactions
    (d) None of the above

3. Monetary items
    (a) Are assets and liabilities to be received or paid in money
    (b) Are assets to be received in fixed or determinable amounts of money
    (c) Are money held and assets and liabilities to be received or paid in fixed or determinable amounts of money
    (d) None of the above

4. Non-monetary items which are carried in terms of historical cost denominated in a foreign currency should be reported using the exchange rate at the date of the
    (a) Balance Sheet (b) Transaction
    (c) Settlement (d) None of the above

5. The contingent liability denominated in foreign currency at the balance sheet date is disclosed by using the
    (a) Average Rate (b) Closing Rate

(c) Non-monetary Rate (d) Monetary Rate

Answers: 1. b, 2. b, 3. c, 4. b, 5. b.

B. Fill in the blanks.

1. ____________ is the mean of the exchange rates in force during a period.
2. ____________ difference is the difference resulting from reporting the same number of units of a foreign currency in the reporting currency at different exchange rates.
3. ____________ rate is the ratio for exchange of two currencies.
4. ____________ value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.
5. ____________ items are assets and liabilities other than monetary items.
6. ____________ currency is the currency used in presenting the financial statements.
7. Cash, receivable, and payable are examples of ____________ items.
8. Fixed assets, inventories and investments in Equity shares are examples of ____________ items.
9. The contingent liability denominated in foreign currency at the balance sheet date is disclosed by using the ____________ rate.

Answers: (1) Average Rate, (2) Exchange, (3) Exchange, (4) Fair, (5) Non-monetary, (6) Reporting, (7)Monitory, (8) Non-monetary, (9) Closing

C. State whether True or False.

1. Exchange rate is the rate at which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.
2. Inventories is a non-monetary item.
3. A foreign currency transaction should be recorded, on initial recognition in the reporting currency, by applying to the foreign currency amount the exchange rate between the

reporting currency and the foreign currency at the date of the recording.

4. Closing rate is the exchange rate at the close of the date on which a transaction takes place.

5. Foreign Currency is a currency other than the Indian rupee.

6. Monetary items are defined by AS 11 as assets and liabilities other than non-monetary items.

7. Reporting currency is the currency used in recording the financial transactions.

8. Exchange difference is the difference resulting from reporting the same number of units of a foreign currency in the reporting currency at the closing exchange rates.

9. A foreign currency transaction arises when an enterprise buys or sells goods or services whose price is denominated in the reporting currency.

Answers: **True: 2**

False: 1, 3, 4, 5, 6, 7, 8, 9.

❖❖❖❖

13

ACCOUNTING FOR TRANSLATION OF FOREIGN CURRENCY TRANSACTIONS-II

Unit Structure

OBJECTIVES

After studying the unit the students will be able to solve the practical problems.

21.1 SOLVED PROBLEMS

Illustration No. 1

Pass Journal Entries for the following Foreign Exchange transactions in the books of Sonu Ltd. Sonu Ltd. of Pune exported goods worth $1,00,000 on 12th January, 2015 to Universal Traders of USA. The payment for the same was received as follows:

15th February, 2015	$ 50,000
2nd March, 2015	$ 10,000
12th April, 2015	$ 40,000

The company follows financial year as accounting year.
The Exchange Rate for $1 was as follows:

12th January, 2015	Rs. 46
15th February, 2015	Rs. 48
2nd March, 2015	Rs. 45
31st March, 2015	Rs. 49
12th April, 2015	Rs 50

Solution:

In the Books of Sonu Ltd.

Date	Particulars	Dr. Rs.	Cr. Rs
2015 Jan 12.	Universal Traders A/c Dr. To Export Sales A/c (Being goods exported at Exchange Rate being $ 1 = Rs 46)	4,60,000	 4,60,000
Feb 15	Bank A/c Dr. To Universal Traders A/c To Foreign Exchange Fluctuation A/c (Being amount received $ 50000 @ Rs 48, Fluctuation $ 50000 [48-46])	2,40,000	 2,30,000 1,00,000
Mar 2	Bank A/c Dr. Foreign Exchange Fluctuation Dr. To Universal Traders A/c (Being amount received $ 10000 @ Rs 45, Fluctuation $ 10000 [45-46])	4,50,000 10,000	 4,60,000
Mar 31	Universal Traders A/c Dr. To Foreign Exchange Fluctuation A/c (Being difference in Foreign Excahnge accounted for at the end of the year - $40000 [49 - 46])	1,20,000	 1,20,000
Mar 31	Foreign Exchange Fluctuation A/c Dr. To Profit & Loss A/c (Briong profit on Foreign Exchange Fluctuation transferred to Profit & Loss A/c)	2,10,000	 2,10,000
Apr 12	Bank A/c Dr. To Universal Traders A/c To Foreign Exchange Fluctuation A/c (Being amount received $ 50000 @ Rs 48, Fluctuation $ 50000 [48-46])	20,00,000	 19,60,000 40,000

Universal Traders A/c

Date	Particulars	Rs	Date	Particulars	Rs
2015			2015		
Jan. 12	To Export Sales A/c	46,00,000	Feb. 15	By Bank A/c	24,00,000
	(100000 x 46)		Mar. 2	By Bank A/c	4,50,000
Feb. 15	To Foreign Exchange Fluctuation A/c	1,00,000	Mar.31	By Foreign Exchange Fluctuation A/c	10,000
Mar. 31	To Foreign Exchange Fluctuation A/c (40000 x [49-46])	1,20,000	Mar.31	By Bal b/d	19,60,000
		48,20,000			**48,20,000**

Apr. 1 Apr. 12	To bal c/d To Foreign Exchange Fluctuation A/c	19,60,000 40,000	Apr.12	By Bank	20,00,000
		20,00,000			**20,00,000**

Foreign Exchange Fluctuation A/c

Date	Particulars	Rs	Date	Particulars	Rs
2015 Mar. 31 Mar 31	 To Universal Traders To Profit & Loss A/c	 10,000 2,10,000	2015 Feb. 15 Mar.31	 By Universal Traders By Universal Traders	 1,00,000 1,20,000
		2,20,000			**2,20,000**
			Apr.12	By Universal Traders	40,000

Illustration No. 2

Pass necessary Journal Entries in the books of N Ltd. Of Nasik.

A machine was imported on 20th January, 2015 from Jackie Chan of China for US $200000. The payment for the same was made as follows :
US $ 150000 on 27th February, 2015.
US $ 50000 on 15th March, 2015

The exchange rate for $ 1 was as follows :
On 20th January, 2015 Rs. 47.00
On 27th February, 2015 Rs. 46.50
On 15th March, 2015 Rs. 48.00
The company follows financial year as accounting year.

Solution :

In the Books of N Ltd., Nasik

Date	Particulars	Dr. Rs.	Cr. Rs

2015 Jan. 20	Machinery A/c Dr. To Jackie Chan A/c (Being machinery purchased at $ 200000 and Exchange rate of $ 1 was Rs 47)	94,00,000	94,00,000
Feb 20	Jackie Chan A/c Dr. To Bank A/c To Foreign Exchange Fluctuation A/c (Being amount paid $ 150000 @ Rs 46.50, Fluctuation $ 150000 [46.5-47])	70,50,000	69,75,000 75,000
Mar.15	Jackie Chan A/c Dr. Foreign Exchange Fluctuation A/c Dr. To Bank A/c (Being payment made $ 50000 @ Rs 48, Fluctuation $ 50000[48-47])	23,50,000 50,000	24,00,000
Mar.31	Foreign Exchange Fluctuation A/c Dr. To Profit & Loss A/c (Being loss on foreign exchange transferred to Profit & Loss A/c)	25,000	25,000

Jackie Chan A/c

Date 2015	**Particulars**	**Rs**	**Date 2015**	**Particulars**	**Rs**
Feb 20 Feb 20 Mar.15	To Bank A/c To Fluctuation Exchange A/c To Bank A/c	6975000 75000 2400000	Jan. 20 Mar.15	By Machinery By Fluctuation Exchange A/c	9400000 50000
		9450000			**9450000**

Foreign Exchange Fluctuation A/c

Date 2015	**Particulars**	**Rs**	**Date 2015**	**Particulars**	**Rs**
Mar. 15 Mar. 31	To Jackie Chan A/c To Jackie Chan A/c	50000 25000	Feb. 20	By Jackie Chan A/c	75000
		75000			75000

Illustration No. 3

Ashish Ltd. Has entered into the following transactions in foreign currency during the year ended 31st March. 2015.

You are required to pass necessary journal entries for the year ended 31st March, 2015.

Date	**Particulars**
2014	
June 10	Goods worth $ 10000 exported to G of Germany
June 20	Payment received from G of Germany $ 10000
August 16	Raw Material imported worth $ 5000 from S of South Korea
August 31	Payment made to S of South Korea $ 5000
October 10	Payment received from SA of South Africa $ 20000 as advance.
October 15	Goods worth $ 2000 imported to SA of South Africa
November 3	A machine worth $ 12000 imported from UK industries of UK.
November 15	Payment made to UK industries of UK $ 6000
December 15	Payment made to UK industries of UK $ 6000
2015	
January 15	Exported goods to BK Industries of Bangladesh worth $ 2000. Payment was outstanding as on 31st March, **2015**
March 15	Imported machinery worth $ 10000 from GK of Germany. Payment was outstanding as on 31st March, 2015

The exchange rate for $1 was as follows

Date	**Exchange Rate Rs.**
2014	
10th June	46.75
20th June	46.50
16th August	48.00
31st August	48.50
10th October	48.75
15th October	49.00
3rd November	48.60
15th November	48.70
15th December	48.40
2015	
15th January	49.00
15th March	49.50
31st Match	50.00

Solution:

In the Books of Ashish Ltd.

Date	Particulars	Dr. Rs.	Cr. Rs
2014 Jun 10.	G of Germany A/c Dr. To Export Sales A/c (Being goods exported of $ 10000 at exchange Rate $ 1 = Rs 46.75)	467500	467500
Jun 20	Bank A/c Dr. Foreign Exchange Fluctuation Dr. To G of Germany A/c (Being amount received $ 10000 @ Rs 46.5, Fluctuation $ 10000 [46.75-46,5])	465000 2500	467500
Aug.16	Raw Material A/c Dr. To S of South Korea A/c (Being raw material purchased of $ 5000 at exchange rate $ 1 = Rs 48)	240000	240000
Aug.31	S of South Korea A/c Dr. Foreign Exchange Fluctuation A/c Dr. To Bank A/c (Being amount paid $ 5000, Fluctuation $5000 [48.5-48])	240000 2500	242500
Oct. 10	Bank A/c Dr. To SA of South Africa A/c (Being received advance of $ 20000 @ 48.75 from SA of South Africa)	975000	975000
Oct. 15	SA of South Africa A/c Dr. Foreign Exchange Fluctuation A/c Dr. To Export Sales (Being amount received $ 50000 @ Rs 48, Fluctuation $ 50000 [48-46])	975000 5000	980000
Nov. 3	Plant & Machinery A/c Dr. To UK Industries (Being purchased machinery at $ 10000 @ Rs. 48.60)	583200	583200
Nov.15	UK Industries Dr. Foreign Exchange Fluctuation A/c Dr. To Bank A/c (Being amount paid $ 6000, Fluctuation $ 6000[48.70- 48.60])	291600 600	292200
Dec.15	UK Industries A/c Dr To Foreign Exchange Fluctuation A/c To Bank A/c (Being amount paid $ 6000, Fluctuation $ 6000[48.60- 48.40])	291600	1200 290400

2015 Jan. 15	BK Industries A/c Dr. To Export Sales A/c (Being goods exported $2000 @ 49)	98000	98000
Mar.15	Plant & Machinery A/c Dr. To GK of Germany A/c (Being machinery purchased for $ 10000 @ Rs 49.5)	495000	495000
Mar.31	BK Industries A/c Dr. To Foreign Exchange Fluctuation A/c (Being the difference in exchange rate accounted for - $ 2000 [50-49])	2000	2000
Mar.31	Foreign Exchange Fluctuation A/c Dr. To GK of Germany A/c (Being the difference in exchange rate accounted for - $ 10000 [50-49.5])	5000	5000
Mar.31	Profit & Loss A/c Dr. To Foreign Exchange Fluctuation A/c (Being profit on foreign exchange fluctuation recorded)	12400	12400

Illustration. 4

X took a foreign currency loan of US $ 500000 @ 10% p.a. on 1-1-2014. Interest is payable yearly with an installment for principal of US $ 100000. X closes the books of account as on 31st March every year. Exchange rates are as follows:

1-1-2014	32.25	31-12-2009	33.90
31-3-2014	32.50	31-3-2010	33.50

Accounting Year - Financial Year

Show the Ledger Accounts, from 1-1-2014 to 31-3-2014, 1-4-2014 to 31-3-2015.

Solution:

LEDGER

Dr. Loan Account Cr.

Date	Particulars	$	Rate	Rs.	Date	Particulars	$	Rate	Rs.
31-3-14	By Balance c/d	500000	32.50	16250000	1-1-14	By Bank	500000	32.25	16125000
					31-3-14	By P &L A/c. (Loss on FE on valuation)	(500000)	0.25	125000
				16250000					**16250000**
31-12-14	To Bank	100000	33.90	3390000	1-4-14	By Balance b/d	500000	32.50	16250000
31-3-	To	400000	33.50	13400000	31-	By P &L A/c.	(100000)	1.40	140000

15	Balance c/d				12-15	(Loss on FE on payment)			
					31-3-15	By P &L A/c. (Loss on FE on valuation)	(400000)	1.00	400000
				16790000					**16790000**

Dr. **Interest Account** **Cr.**

Date	Particulars	$	Rate	Rs.	Date	Particulars	$	Rate	Rs.
31-3-14	To Outstanding Interest A/c	12500	32.50	406250	31-3-14	By P&L A/c.(transfer)	--	--	406250
				406250					**406250**
31-12-14	To Bank	37500	33.90	1271250	31-3-14	By P&L A/c.(ltd)	--	--	1606250
31-3 -15	To Outstanding (400000x 10%x3/12)	10000	33.50	335000					
				1606250					**1606250**

Outstanding Interest Account

Dr. **Cr.**

Date	Particulars	$	Rate	Rs.	Date	Particulars	$	Rate	Rs.
31-3-14	To Balance c/d	12500	32.50	4,06,250	31-3-14	By Interest	12500	32.50	4,06,250
				4,06,250					**4,06,250**
31-12-14	To Bank	12500	33.90	423750	1-4-14	By Balance b/d	12500	32.50	4,06,250
31-3-15	To Balance c/d	10000	33.50	3,35,000	31-12-14	By P & L A/c. (Loss on F.E. On Payment)	(12500)	1.40	17,500
					31-3-15	By Interest	10000	33.50	3,35,000
				7,58,750					**7,58,750**

Illustration 5

From the following details of foreign currency transactions of M/s Fema for the year ended 31st March 2015, prepare the foreign currency fluctuations A/c for the year 1st April 2014 to 31st March 2015.

Import Particulars :

(a) On 15-4-2014 , goods worth \$ 5000 purchased from C of China . The rate of exchange is \$ 1= Rs.48.60. Payment is made on 30-5-2014 when the rate of exchange is \$ 1= Rs. 48.90.

(b) On 12-6-2014 advance amount \$ 1000 paid to F of France. The rate of exchange is \$ 1 = Rs. 48.50 .On 20-6-2014 goods imported worth \$ 10000 from F of France .The rate of exchange is 1\$ =48.00. On 30-6-2014 payment made to F of France \$9000. The rate of exchange is \$1 = Rs. 48.90.

(c) On 10-7-2014 , Machinery purchased from G of Germany for $ 50000. The rate of exchange is $ 1= Rs. 46.80 . On 28-7-2014 payment made to G of Germany $50000. The rate of exchange is $1 = Rs. 47.20.

(d) On 28-1-2015 goods purchased from K of Korea $15000. Rate of exchange is $1= Rs. 47.30. On 20-4-2015 payment made to K of Korea $ 15000. The rate is $1= Rs.47.80.

Export Particulars :

(e) On 28-5-2014,exported goods to C of Canada worth $120000, rate of exchange is $1=Rs.47.35. On 28-6-2014, payment received from C of Canada,$ 40000at exchange rate of $1=Rs.47.60.On 28-8-2014 payment received from C of Canada ,$80000at exchange of rate of 1$= Rs. 47.00.

(f) On 1-10-2014 advanced received from J of Japan $ 10000 exchange rate being $1=Rs. 46.00 On 15-10-2014, exported goods worth $30000 of J of Japan at exchange rate of $1= 46.25. On 28-12-2014, payment received from J of Japan ,$20000 at exchange rate of $1= Rs. 46.25.

(g) On 2-1-2014 exported goods to S of Sri Lanka $40000. Exchange rate is $1=Rs. 45.40 . On 20-3-2015, $ 20000 received from S of Sri Lanka exchange rate being $1= Rs.46.30. On 20-5-2015 $ 20000 received from S of Sri Lanka exchange rate being $ 1= Rs. 48.80

The rate of exchange on 31st March ,2009 was $1=Rs. 45.60.

Solution:

Foreign Exchange Fluctuation Account for The Year Ended 31st March 2015

Dr. Cr.

Date	Particulars	Rs.	Date	Particulars	Rs.
30-5-2014	To C of China {5000x(48.90-48.60)}	1500	28-6-2014	By C of Canada {40000 x (47.60-47.35)}	10000
20-6-2014	To F of France {1000 x (48.50-48.00)}	500	30-6-2014	By F of France {9000 x(48.00-47.90)}	900
28-7-2014	To G of Germany {50000x (47.20-46.80)}	20000	20-3-2014	By S of Sri Lanka {20000x(46.30-45.40)}	18000
28-8-2014	To C of Canada {80000 x (47.35-47.00)}	28000	31-3-2015	By S of Sri Lanka{20000 x(45.60-45.40)}	4000
15-10-2014	To J of Japan {10000x (46.25-46.00)}	2500	31-3-2015	By K of Korea {15000x(47.30-45.60)}	25500
21-3-2015	To Profit & Loss	5900			

	A/c.(Net Tfd)				
		58400			**58400**

Illustration 6

On 1st January-2015 MARINA LTD. an Indian importer purchased $ 250000 worth goods from Gemini Trading Company of USA.

The payment for the import was made as follows:

On 10th February-2015 ---- $ 100000
On 15th March-2015 ---- $ 75000
On 20th April-2015 ---- $ 75000

Marina Limited closes its books on 31st March every year.
The exchange rate for $ 1 was follows :
1st January-2015 ------ Rs. 49.00
10th February-2015 ----- Rs. 49.50
15th March-2015 ---- Rs. 47.60
31st March-2015 ----- Rs. 45.00
20th April-2015 ----- Rs. 46.75

(1) Pass Journal Entries.
(2) Prepare Gemini Trading Company Account and Foreign Exchange Fluctuation Account in the books of Marina Limited.

Solution :

IN THE BOOKS OF MARINA LTD.

JOURNAL

No	Date	Particulars	Dr. Rs.	Cr. Rs.
1	10-1-2015	Purchase A/c. Dr. To Gemini Trading Co. A/c. (Being import of goods from Gemini Trading Co. at the Exchange rate of Rs. 49.00 per $)	12250000	12250000
2	10-02-2015	Gemini Trading Co. A/c. Dr. Foreign Exchange Fluctuation A/c. Dr To Bank A/c.. (Being payment made of $ 100000 at the exchange rate of Rs.49.50 & Loss transferred to Foreign Exchange Fluctuation A/c).	4900000 50000	4950000
3	15-3-2015	Gemini Trading Co. A/c. Dr.	3675000	

		To Bank A/c. To Foreign Exchange Fluctuation A/c.[Being payment made of $ 75000 and exchange gain of Rs. 1.40 (Rs. 49.00-Rs.47.60)]		3570000 105000
4	31-3-2015	Gemini Trading Co. A/c. Dr. To Foreign Exchange Fluctuation A/c. (Being entry for a year and monetary items for $ 75000 payable to suppliers Gain of Rs. 4 [Rs. 49 – Rs.45])	300000	300000
5	31-3-2015	Foreign Exchange Fluctuation A/c Dr. To Profit & Loss A/c. (Being Profit and Foreign Exchange Fluctuation transferred to Profit and Loss A/c.)	355000	355000
6	20-4-2015	Gemini Trading Co. A/c. Dr. Foreign Exchange Fluctuation A/c. To Bank A/c.. (Being payment made $ 75000and exchange loss of Rs. 1.75[Rs. 46.75-45.00])	3375000 131250	3506250
7	31-3-2014	Profit and Loss A/c. Dr. To Foreign Exchange Fluctuation A/c.(Foreign Exchange Fluctuation Account's Balance transferred to Profit and Loss A/c.))	131250	131250

Gemini Traders A/c.

Date	Particulars	U.S.$	Rate	Rs.	Date	Particulars	U.S.$	Rate	Rs.
2015					2015				
Feb.10	To Bank	100000	49.50	4950000	Jan.1	By Purchases A/c.	250000	49	12250000
					Feb.10	By Foreign exc.fluctuation A/c.			50000
Mar.15	To Bank	75000	47.60	3675000					
	To Foreign exc. Fluctuation A/c.			105000					
31	To Foreign exc. Fluctuation A/c.			300000					
31	To Balance c/d	75000	45	3375000					

		250000	**---**	**12300000**			**250000**	**----**	**12300000**
2015					2015				
April 20	To Bank	75000	46.75	3506250	April	By Balance b/d	75000	45	3375000
		-----	---		April 20	By Foreign Exchange Fluctuation A/c.			131250
		75000		**3506250**			**75000**		**3506250**

Foreign Exchange Fluctuation Account

Date	Particulars	Rs.	Date	Particulars	Rs.
2014 April 10	To Gemini trading co A/c	5000	2014 March 15	By Gemini trading co	105000
31-8-14	To Profit & loss A/c [$ 5000x(48.00-48.50)]	355000	31-3-14	By Gemini trading co	300000
		405000			**405000**
2015 April 20	To Gemini Trading Co.A/c	131250	2015 March 31	By Profit & loss A/c	131250
		131250			**131250**

Illustration 7

Jaya Traders purchased a machine for $ 1200000 on 30th September 2013 . Out of this $ 1000000 was financed by a foreign currency loan. The loan carried an interest rate of 10% p.a. On the date of acquisition the exchange rate was 1$= Rs.45.00

The firm closes books on 31st March every year. Depreciation is provided at 10% on WDV basis. The company paid $ 200000(Exchange rate Rs.46.50/$) on 31st March 2014 and 150000 on31st March 2015 (Exchange rate Rs. 47.00/$) alongwith outstanding interest on respective dates.

You are required to prepare Machinery A/c. and Foreign currency loan A/c.for the years 31st March 2014 and March 2015 in the books of Jaya Traders.

Solution:

In the Books of Jaya Traders

Foreign Currency Loan A/c.

Date	Particulars	U.S.$	Rate	Rs.	Date	Particulars	U.S.$	Rate	Rs.
2014					2013				

March. 31	To BAnk	200000	46.50	9300000	September 30	By Machinery	1000000	45.00	45000000
					2014 March 31	By Foreign Exchange fluctuation			300000
March 31	To Balance c/d	800000	46.50	37200000	March1	By Foreign Exchange fluctuation			1200000
				46500000					**46500000**
2014					2014				
					April 1	By Balance b/d.	800000	46.50	37200000
20015 March. 31	To Bank	150000	47.00	7050000	2015 March 31	By Foreign Exchange fluctuation			75000
	To Balance c/d	650000	47.00	30550000	March 31	By Foreign Exchange fluctuation			325000
				37600000					**37600000**
2015					2015				
					April 1	By balance B/d	650000	47.00	30550000

Machinery A/c

Date	Particulars	Rs.	Date	Particulars	Rs.
2013			2014		
Septe30	To Bank	9000000			
	To Foreign currency loan A/c	45000000	March 31	By Depreciation A/c	2700000
			March 31	By Balance C/d	51300000
		54000000			**54000000**
2014			2015		
April 01	To Balance b/d	51300000	March 31	By Depreciation	5130000
			March 31	By balance c/d	46170000
		51300000			**51300000**
2014			2014		
Jan 01	To Balance B/d	46170000			

Illustration 8

On 1st Jan.2015 Suhani Ltd. imported \$ 100000 worth of goods from Jimmy Traders of U.S.A. The payment for the same was made on 15th April 2015.Suhani Ltd. closes it's accounts on

31^{st} March every year. The exchange rates on the relevant dates were :--

1^{st} Jan 2015 1\$=Rs.46
31^{st} March 2015 1\$=Rs.45
15^{th} April 2015 1\$=Rs.48

Journalise the above transactions in the books of Suhani Ltd. in accordance with Accounting Standard 11.

In the books of Suhani Ltd.
Journal entries

Date	**Particulars**	**Dr. Rs.**	**Cr. Rs.**
2015			
1-1	Purchase A/c. Dr. To Jimmy Traders U. S. A. A/c. (Being goods purchased worth U.S.A.100000 at exchange rate Rs.46/\$)	4600000	 4600000
31-3	Jimmy Traders of U.S.A. A/c. Dr. To Foreign Exchange Fluctuation A/c. (Being Exchange rate fluctuation at Rs.{46.00-45.00}per \$ on amount payable to Jimmy Traders of U. S. A. adjusted)	100000	 100000
31-3	Foreign Exchange Fluctuation A/c. Dr. To Profit & Loss A/c. (Being profit on foreign exchange transfer to P& L A/c.)	100000	 100000
15-4	Jimmy Traders of U.S.A. A/c. Dr. Foreign Exchange Fluctuation A/c Dr. To Bank A/c. (Being amount paid to Jimmy Traders,U.S.\$100000 at Rs.48.00/\$)	4500000 300000	 4800000

Illustration 9

Mitul Ltd. an Indian Exporter, sold goods to Charlie Inc. at U.S. \$ 25000 on 1-1-2015. 30 days later Mitul Ltd. received a remittance of U.S. \$ 10000 being part payment. The Foreign Bank deducted \$ 10 as charges while remitting the amount of Mitul Ltd.

The local Bank deducted their charges of Rs.750 while crediting the amount to the account of Mitul Ltd. Mitul Ltd. closes it's account on 31st March every year. The Exchange rates were:-

1st Jan 2015 1$=Rs.46
31st Jan 2015 1$=Rs.45
31st March 2015 1$=Rs.48

Journalise the above transactions in the books of Mitul Ltd. as per According Standard 11.

Solution:

Journal Entries in the books of Mitul Ltd.

Date	Particulars	Dr. Rs.	Cr. Rs.
2015			
1-1	Charlie Inc. U.S. A/c. Dr.	1150000	
	To Export Sales A/c.		1150000
	(Being goods sold worth U.S. $ 25000at Rs. 46/$)		
31-1	Bank A/c. Dr.	448800	
	Bank charges Inc. U. S. A/c. Dr.	1200	
	Foreign Exchange Fluctuation A/c Dr.	10000	
	To Charlie Inc.,USA		460000
	(Being $ 10000 received at rs.45/$ after deducting Bank charges of Rs.10x45 i.e. Rs.450+Rs.750)		
31-3	Charlie Inc. U.S. A/c. Dr.	30000	
	To Foreign Exchange Fluctuation A/c.		30000
	(Being amount receivable from Charlie Inc. U.S. $15000 adjusted at Rs. 2 / $ [48-46])		
31-3	Foreign Exchange Fluctuation A/c. Dr.	20000	
	To Profit& Loss A/c.		20000
	(Being Profit on Foreign exchange fluctuation A/c. transferred to P & L A/c.)		

Illustration 10

Kadambari Food Products purchased food processing machinery from Watson Inc. USA for US $ 20000 on 1st Jan.2011. The price of the machinery was payable as 5000 US $ on 1-1-2011 and balance in 3 annual instalments of 5000 $ on 1st Jan each year. Pass necessary journal entries in the books of the firm for the year 2011,2012, 2013,2014 and 2015. The firm charges depreciation at 20% p.a. on W.D.V. method. The exchange rates per $ were:-

		Rs.
On	01-01-2011	40
	31-12-2011	41
	31-12-2012	42
	31-12-2013	39

The Firm follows Calendar year & Accounting year

Solution:

Journal of Kadambari Food Products

Date	Particulars	Dr. Rs.	Cr. Rs.
1-1-11	Machinery A/c. Dr. To Watson Inc.USA A/c. (Being Machinery purchased exchange rate 1$=40 Rs.)	800000	 800000
1-1-11	Watson Inc. USA A/c Dr. To Bank A/c. (Being amount paid @ exchange rate 1$= 40Rs.)	200000	 200000
31-12-11	Depreciation A/c. Dr. To Machinery A/c. (Being depreciation charged @ 20 % p.a. on W.D.V. Method)	160000	 160000
31-12-11	Watson Inc. USA A/c Dr. Foreign Exchange Fluctuation A/c. Dr. To Bank A/c. (Being 5000 US $ paid to Watson Inc. at exchange rate 1$=41 Rs.)	200000 5000	 205000
31-12-11	Foreign Exchange Fluctuation A/c. Dr. To Watson Inc. USA A/c (Being closing balance payable to Watson Inc. adjusted at exchange rate 1$=41 Rs.)	10000	 10000

31-12-11	Profit & Loss A/c. Dr. To Depreciation A/c. To Foreign Exchange Fluctuation A/c. (Being nominal A/c. transferred to P & L) A/c.)	175000	 160000 15000
31-12-12	Watson Inc.USA A/c Dr. Foreign Exchange Fluctuation A/c. Dr. To Bank A/c. (Being 5000 US $ paid to Watson Inc. at exchange rate 1$=42 Rs.)	205000 5000	 210000
31-12-12	Foreign Exchange Fluctuation A/c. Dr. To Watson Inc.USA A/c (Being closing balance payable to Watson Inc. at exchange rate 1$=42 Rs.)	5000	 5000
31-12-12	Depreciation A/c. Dr. To Machinery A/c. (Being depreciation Provided @ 20%)	128000	 128000
31-12-12	Profit & Loss A/c. Dr. To Depreciation A/c. To Foreign Exchange Fluctuation A/c. (Being nominal A/c. transferred to P & L) A/c.)	138000	 128000 10000
31-12-13	Watson Inc.USA A/c Dr. To Foreign Exchange Fluctuation A/c. To Bank A/c. (Being 5000 US $ paid to Watson Inc. USA at Rs. 39 / $)	210000	 15000 195000
31-12-13	Depreciation A/c. Dr. To Machinery A/c. (Being depreciation provided at 20 % p.a. W.D.V.)	102400	 102400
31-12-13	Profit & Loss A/c. Dr. To Depreciation A/c. (Being depreciation transferred to P & L A/c.)	102400	 102400
31-12-13	Foreign Exchange Fluctuation A/c. Dr. To Profit & Loss A/c (Being nominal A/c transferred to P & L A/c.)	15000	 15000

Working Note: Depreciation

Date	Particulars	Amount
1-1-11 31-12-11	Purchase Depreciation @ 20% W.D.V.	800000 160000
1-1-12	Opening Balance	640000
31-12-12	Depreciation @ 20% p.a. W.D.V.	128000
1-1-13	Opening Balance	512000
31-12-2013	Depreciation @ 20 % p.a. W. D. V.	102400
1-1-14	Opening Balance	409600

Illustration 11

Anand Exports on 10-10-14 goods worth $ 200000 to A Ltd. in New York. The payment was received on 1-1-15. On the date of Export, the exchange rate was $1= Rs. 45. The dollars were actually received when the exchange rate was $1= Rs.48. Record the transactions in the book of Anand in accordance with AS11.

Solution:-

Journal of Anand

Date	No.	Particulars	Dr. Rs.	Cr. Rs.
2014 Oct.10	1	A Ltd. A/c Dr. To Sales A/c. (Being Exports of $200000 to A Ltd. transferred at 1$=Rs.45)	9000000	 9000000
01.01.2015	2	Bank A/c. Dr. To Foreign Exchange Fluctuation A/c To A Ltd. A/c. (Being the receipt of $ 200000 from A Ltd. translated at 1 $= Rs.48)	9600000	 600000 9000000
31.03.2015	3	Foreign Exchange Fluctuation A/c Dr. To Profit & Loss A/c (Being nominal A/c closed)	600000	 600000

Ledger of Anand

A Ltd. Account

Date	Particulars	$	Rate	Rs.	Date	Particulars	$	Rate	Rs.
10-1-14	To Sales	200000	45	9000000	18-1-14	By Bank	200000	48	9600000
18-1-14	To Gain on FE	(200000)	3	600000					
		200000		**9600000**			200000		**9600000**

21.2 KEY TERMS:

- **Average rate:** It is the mean of the Foreign exchange rate.
- **Closing rate:** It is the Foreign Exchange rate as on Balance Sheet date.
- **Exchange rate**: It is the Foreign Exchange rate as given by the RBI
- **Foreign currency:** It is the Currency of the foreign country.
- **Foreign Currency transaction**: It is a transaction entered in a foreign currency.
- **Foreign Exchange Fluctuation Account:** it is an account through which profit or loss due to Foreign Exchange Fluctuation is recorded.
- **Forward rate**: It is the Foreign Exchange rate fixed by the terms of agreement for exchange between two foreign currencies at a specified future date.
- **Reporting currency**: It is the currency of the country in which the financial statements are prepared.
- **Settlement date:** It is the date on which foreign currency transaction is paid or received.

EXERCISE

1. Ceat Ltd. purchased a machine for US $ 1,00,000 on 30th June 2013, from Thompson of USA ,out of which $80,000 was financed by a foreign currency loan and the balance was received by way of Government Grant. The loan carried interest at 9% p.a. On the date of acquisition exchange rate was $1= Rs.50.

   The Foreign currency loan was repaid in two equal annual instalments on 30th June 2014 and 30th June 2015 along with interest due there on.

Ceat Ltd provides depreciation at 20% p.a. WDV. Method on 31st March every year.

The exchange rate were as under:-

31st December 2013	Rs.52/$
31st March 2014	Rs. 54/$
30th June 2014	Rs.53/$
31st March 2015	Rs. 58/$
30th June 2015	Rs. 60/$

You are required to prepare following Ledger Accounts in the books of Ceat Ltd.

a) Machinery A/c.

b) Foreign currency loan A/c.

c) Interest A/c.

d) Depreciation A/c.

e) Outstanding interest A/c.

2. Kailas Ltd. borrowed from Uk , money market a sum of 100000 pounds on 1st January 2014 for a period of 6 months for working capital requirement. The loan was repaid on the due date together with interest at 6 %. The exchange rate for the pound sterling is given below:-

On 1st January 2014	1pound= Rs. 78
31st March 2014	1 Pound= Rs.79
30th June 2014	1 Pound= Rs.80

Pass necessary entries in the books of Kailas Ltd. for the above transactions and show the relevant extract of its balance sheet as on 31st March 2014.

3. Stock at cost to Progressive company ltd. on 31st March 2015 was valued at the cost of £10000 being purchased on 31st December 2014 the currency rate of exchange were:

1£ =Rs.70 (31st March 2015) and Rs.68 (31st December 2014)

The market value on 31st March 2015 of the stock was lower than its cost by 10% thereof when Progressive company ltd. paid half the amount due on the purchases. Show the entries passed by Progressive company ltd. on relevant extract of its balance sheet as on 31st March 2015.

❖❖❖❖

14
BUYBACK OF EQUITY SHARES I

Unit Structure:

14.0 OBJECTIVES

After studying the unit the students will able to:

- Distinguish between Redemption of Preference shares and Buy back of Equity shares.
- Understand the need and objectives of Buy Back.
- Explain the Legal provision for Buy Back.
-

14.1 INTRODUCTION

Buy-Back of securities simply implies purchase of it's own securities by a company. Buy-Back of securities is a important mode of capital restructuring. A buy-back allows companies to invest in them selves. A company can buy-back it's shares under Sec. 68 of companies Act, 2013 which is more or less as per Sec. 77A, 77B of companies Act, 1956.

The modification to existing framework for buy-back through open market purchase have been done by holding the shareholder's interest as paramount consideration. As per companies Act, 2013 there are some more procedural changes. A company doing buy-back of it's own securities is required to comply with the share capital and Debenture Rule, 2014.

14.2 DISTINCTION BETWEEN REDEMPTION OF PREFERENCE SHARES & BUY-BACK OF EQUITY SHARES

Redemption		Buy Back	
1.	Redemption can be only of preference shares.	1.	Buy Back can be of equity as well as preference shares.
2.	The date and terms of Redemption is determined at the time of issue of shares.	2.	Such date and term of buy back is not determined in advance.
3.	Entire preference shares can be subject to redemption	3	The share subject to buy back cannot exceed specified amount.

4.	Redemption of preference shares is subject to provision of sec 42 of Companies Act, 2013.	4	Buy Back of shares is subject to Sec. 68, 69, 70 of the Companies Act, 2013.
5.	Security Premium A/c Cannot be utilized to create Capital Redemption Reserve in case of Redemption.	5.	Security Premium A/c can be utilised for creation of Capital Redemption Reserve.
6.	Fresh issue of same class i.e. preference shares is permissible in case of Redemption.	6.	Fresh issue cannot be of a same class of shares buy back is not permissible.
7.	Redemption is governed under Companies Act.	7.	Buy Back is Governed under Companies Act as well as S.E.B.I. Rules.
8.	Redemption is effected by direct payment by companies or by conversion into share issued to shareholders.	8.	Buy Back of shares can be purchase of shares from market and simultaneous cancellation. This is in addition to direct payment to shareholders.

14.3 NEED AND OBJECTIVES OF BUY-BACK BUY BACK

14.3.1 Need of Buy Back

1. A Company having surplus funds may return to shareholders.
2. A Company required restricting / having excess funds due to change of business whatever may be reason, such as business becoming illegal.
3. Wide fluctuation in market price of Share in Stock Exchange.

14.3.2 Effects of Buy Back

By purchasing its own Shares / Stock, Company reduces the numbers of shares outstanding without affecting its reported earnings, thus increasing the company's earning per Share.

The company's net worth per shares also increases further., even though buy-back may be with premium.

14.3.3 Objectives of Buy Back

Buy-Back of Equity shares may be done with following objectives:

i) To increase the intrinsic value of the share.

ii) To increase Equity Per Share (EPS)

iii) To reduce the outstanding shares in the market.

iv) To effect financial compromise or arrangement.

v) To increase the shareholding of the present management.

14.3.4 Advantages of Buy Back

1. It is an alternative mode of reduction in capital without requiring approval of the Court / CLB.
2. To improve the earnings per share.
3. To improve return on capital, return on net worth and to enhance the long-term shareholders value.
4. To prove an additional exit route to shareholders when shares are undervalued or thinly traded.
5. To enhance consolidation of stake in the company.
6. To prevent unwelcome takeover bids.
7. To return surplus cash to shareholders.
8. To achieve optimum capital structure.
9. To support share price during periods of sluggish market condition.
10. To serve the equity more efficiently.
11. E.P.S. gets improved after Buy-Back.

Particulars	Pre-Buy-Back ₹	Post Buy-Back ₹
A) Profit after Tax, Preference Dividend	1,60,000	1,60,000
B) No of out Standing Shares	1,000	750
E.P.S. (A / B)	160	213.33

After Buy-Back of 250 shares E.P.S. is increased from ₹160 to ₹ 213.33.

14.4 LEGAL PROVISIONS (COMPANIES ACT, 2013)

14.4.1 Following are the provisions made under section 68

1. Purchase can be made out of:

a) Its Free Reserves.

b) The Securities Premium Account or / and

c) The Proceeds of the issue of any shares of other specified securities.

It may any one or any combination of above. No buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities.

2. **Preliminary Conditions:**

a) Must be authorized by its articles;

b) A special resolution has been passed at a general meeting of the company authorizing the buy back, but the same is not required when.
   i. The buy-back is 10% or less of the total paid-up equity capital and free reserves of the company;
   ii. Such buy-back has been authorized by the Board by means of a resolution passed at its meeting;

c) The buy-back is twenty-five per cent or less of the aggregate of paid-up capital and free reserves of the company. But in case of Equity Shares, the same shall be taken as 25% of paid up equity capital only.

d) Debt equity ratio should not exceed 2:1.
Where: Debt is aggregate of secured and unsecured debts owned by the after buy-back, Equity: is aggregate of the paid-up capital and its free reserves:

e) All the shares or other specified securities for buy-back are fully paid-up.

f) If shares or securities are listed, buy back will be in accordance with the regulations made by the Securities and Exchange Board in this behalf; and

g) The buy-back in respect of unlisted shares or other specified securities is in accordance Share Capital and Debentures Rules, 2014.

h) No sub offer of buy-back shall be made within a period of one year from the date of the closure of the preceding offer of buy-back, if any.

3. **Explanatory Statement:**

The notice of the meeting at which the special resolution is proposed to be passed shall be accompanied by an explanatory statement stating -

i) A full and complete disclosure of all material facts.

ii) The necessity for the buy-back.

iii) The class of shares or securities intended to be purchased under the buy-back.

iv) The amount to be invested under the buy-back; and

v) The time-limit for completion of buy-back.

vi) A confirmation that there are no financial defaults subsisting in repayment of deposits, interests etc.

vii) A confirmation required from the board of directors and by the company's Auditors in regards to state of affairs of the company. The amount of buy back within the permissible limits.

4. **Time Limit:**

Every Buy back shall be completed within a period of one year from the date of passing of the special resolution, or as the case may be, the resolution passed by the Board.

5. **Options for Buy Back:**

The Buy Back can be from:

a) From the existing Shareholders or security holders on a proportionate basis.

b) From the open market.

c) By purchasing the securities issued to the employees of the company pursuant to a scheme of stock option or sweat equity.

6. **Solvency Declarations:**

Before making such Buy back, file with the Registrar, a declaration of solvency signed by at least two directors of the company one of whom shall be the managing director.

7. **Extinguishment of Certificate:**

Company shall extinguish and physical destroy the shares or securities so bought back within seven days of the last date of completion of buy back.

8. **No further issue till 6 months:**

Where a company completes a buy back of its shares or other specified securities, it shall not make a further issue of the same kind of shares or other securities including allotment of new shares or other specified securities within a period of six months except by the way of:

a) A bonus issue or

b) In the discharge of subsisting obligations such as conversion of warrants, stock option schemes.

9. **Register to be maintained:**

Company shall maintain a register in Form No. SH.10 of the shares or securities so bought stating

a) Buy back price.

b) Date or Extinguishing and physically destroying the shares or securities.

c) The register of shares or securities bought back shall be maintained at the registered office of the company.

10. Return of Buy Back and Declarations:

A Company shall after the completion of the buy back under this section, file with the registrar a return in Form No. SH.11 containing such particulars relating to the buy back within thirty days of such completion.

11. Punishment for Any Defaults:

If a company makes any default in companying with the provisions of the section, the company shall be punishable with a fine which shall be ₹1 lack to ₹3 lakhs and every officer of the company who is in default shall be punishable with imprisonment for a term with may extend to 3 years and / or with a fine its shall be ₹1 lack to ₹3 lack, ₹1 or both.

12. Capital Redemption Reserve:

Where a company purchases its own shares out of free reserves or securities premium account, a sum equal to the nominal value of the shares so purchased shall be transfer to the capital redemption reserve account and details of such transfer shall be disclosed in the Balance Sheet.

14.4.2 Following are the provisions made under section 69

1. Utilisation of Capital Redemption Reserve:

The Capital redemption reserve account may be utilized by the company for issue of fully paid bonus shares to the existing share holders, to the extent unissued shares of the company.

14.4.3 Following are the provisions made under section 70

1. Restrictions on Buy Back:

No company shall directly or indirectly purchase its own share or other specified securities.

a) Through any subsidy company including its own subsidiary companies.
b) Through any investment companies or any group of companies.
c) If a financial default is made by the company, in repayment of liabilities, including interest thereon before or after commencement of this act.

14.5 SOURCES OF BUY-BACK [SEC. 68(1)]

1. Free Reserve:

Free Reserves means Reserves which are free for distribution by ways of dividend and includes Securities Premium A/c. Free reserve may be in the form of Profit & Loss A/c (Cr. Bal.), General Reserve, Dividend Equalisation Reserve etc.

The following reserves are not free Reserves:

a. Capital Redemption Reserve.
b. Capital Reserve.
c. Statutory Reserves.

For the purpose of Buy-Back, Securities Premium considered as Free Reserve, otherwise it is not considered as free Reserve.

The Free Reserve Balances should be reduced by:

a. The amount included in Miscellaneous Expenditure (to the extent not written off).
b. Unamortized balance of Goodwill or Deferred revenue Expenditure.
c. Impairment or diminution in value of investment and tangible assets.
d. Contingent liabilities likely to be materialized.

2. Securities Premium:

When the company issues shares or debentures at the higher amount than face Value / Nominal Value, the higher amount is considered as Security Premium. It is treated as Capital profit to the company. As per Company Act, 2013 a company can Buy Back its own shares out of the Securities Premium a/c.

3. Statutory Reserve:

Statutory Reserves are the Reserves created to enjoy certain benefits under statue, such as under Income Tax etc. Normally these Statutory Reserves are not free reserves up to 8 years e.g. Investment Allowance Reserve, Export Profit Reserve, Revaluation Reserve etc.

4. Proceeds of an Earlier Issue:

Buy-Back of shares of any kind is not allowed out of fresh issue of shares of the same kind. Buy-Back Equity Shares is allowed by issue of preference shares or by issue of any pure or hybrid debt instruments.

14.6 CONDITIONS AND LIMITS OF BUY-BACK

Following are some of the limitations of Buy Back:

a) Buy-Back cannot be more than 25% of paid up Equity Share Capital in one Financial Year.

b) Buy-Back amount (Fully Paid Equity Shares) can not exceed 25% of Share Capital (Equity + Pref.) + Free Reserves + Securities Premium.

c) After Buy-Back Debt to Equity ratio should not exceed 2:1.

14.7 MODES OF BUY-BACK

a) 10% Buy Back through Tender Offer:

The company may offer to shareholders / members on proportionate basis. In such case shareholders surrender their shares along with application. After Verification Company accepts the offer and pays amount through escrow account to shareholders.

b) Buy-Back through Open Market Operation or Purchase of shares through stock exchange:

In such case, the company purchase shares though stock broker at transaction price, thereafter the shares are cancelled and certificate should be destroyed within the 7 days.

c) Buy-Back Through Book Building Process:

It is an important method of fixation of share price. After passing special resolution, the company should specify the maximum buy back price, company appoints merchant bank and makes public announcement for Buy-Back of shares, the public announcement should specify the step by step procedure of book building process. Buy-Back should short from 7 days from the date of public announcement.

14.8 ACCOUNTING PROCEDURE

14.8.1 Hints for solving problems

1) Only full paid shares can be bought back, in case shares are partly paid, make final call.
2) For Calculating Maximum Buy-Back Price or Maximum No. of shares to be Bought Back or Maximum No. of shares at best possible price: in case of all above following procedure should be followed:

    a. 25% of fully paid Equity Shares / Equity Share Capital.
    b. 25% of Own Fund i.e. 25% of paid up share capital (Including Pref. Shares) + Free Reserve + Securities Premium
    c. Debt to Equity Ratio should not be more than 2:1.
    d. Least of ‘a’ or ‘b’ is the amount available for Buy-Back.

3) Now : Maximum Buy-Back Price = ‘d’ / No. of share to be brought back.

4) Maximum No. of Share to be bought back = ‘a’,
5) Maximum No. of Shares at Best Possible Price = ‘d’ / ‘a’ =
Maximum Amount Available for Buy Back.
Maximum No. of Shares to be Brought Back.

6) C.R.R. = F.V. of share brought less earlier issue [Not of Same Kind]

14.8.2 Journal Entries:

			Dr. ₹	Cr. ₹
1.	**Fresh Issue of Shares:**			
1. a)	At Par:			
	Bank a/c	Dr.	x	
	To Share Capital a/c			x
1. b)	At Premium:			
	Bank a/c	Dr.	x	
	To Share Capital a/c			x
	To Security Premium a/c			x
	Note: the issue cannot be same class of Shares subject to Buy-Back			
2.	**For Sale Investment:**			
2. a)	At Cost:			
	Bank a/c	Dr.	x	
	To Investment a/c			
2. b)	At Profit:			x
	Bank	Dr.	x	
	To Investment a/c			x
	To Profit & Loss a/c			x
2. c)	At Loss:			
	Bank a/c	Dr.	x	
	Profit & Loss a/c	Dr.	x	
	To Investment a/c			x
3.	**For Cancellation of Shares Brought Back:**			
3. a)	Bought back at Face Value:			
	Equity Share Capital a/c [F.V.]	Dr.	x	
	To Equity Shareholders a/c			x

3. b)	Bought Back at Premium		
	Equity Share Capital a/c [F.V.] Dr.	x	
	Premium on Buy-Back of Shares a/c Dr.	x	
	To Equity Shareholders a/c		x
3. c)	Bought Back at Discount:		
	Equity Share Capital a/c [F.V.] Dr.	x	
	To Equity Shareholders a/c		x
	To Capital Reserve a/c		x
4.	**For Providing Premium on Buy-Back of Shares:**		
	Profit & Loss / Divisible Profit a/c Dr.	x	
	Securities Premium a/c [Existing] Dr.	x	
	To Premium on Buy-Back of Shares a/c		x
	Note: Securities Premium can be used only if		
A)	Divisible profits are fully used		
B)	Specifically mentioned in the Problem		
5.	**For Transferring Free Reserves / Security Premium to Capital Redemption Reserve**		
	C.R.R. = F.V. of BUYBACK - Earlier Issue		
	Securities Premium a/c [Existing] Dr.	x	
	Profit & Loss / Divisible profit a/c Dr.	x	
	To Capital Redemption Reserve a/c		x
6.	**For payment to Equity Shareholders:**		
	Equity Shareholders a/c Dr.	x	
	To Bank a/c		x
7.	**Buy-Back Expenses Paid:**		
	Buy-Back Expenses a/c Dr.	x	
	To Bank a/c		x
8.	**For Writing off Buy-Back Exp.**		
	Profit & Loss a/c Dr.	x	
	To Buy-Back Expenses a/c		x
	Note: Buy-Back Expenses can be treated as deferred Revenue expenditure & written off over 3 to 5 years.		

14.9 EXERCISE

1. **Objective Question**

A) Multiple Choice Question

1. The premium paid on the buy-back should be credited to -----.
a) Securities Premium A/c b) Profit & Loss A/c
c) **Equity Shareholders A/**c d) Equity Share Capital A/c

2. For buy-back a company should open an ---- Bank A/c with Bank.
a) Saving Bank b) Current A/c
c) **Escrow A/c** d) Fixed Deposit

3. Board of Directors can approve buy back up to ------.
a) **25%** b) 10%
c) 20% d) 30%

4. The company before buy back has to submit a declaration of --
a) Liquidity b) Insolvency
c) Solvency d) Profitability

5. Time interval between two buy back of shares should not be less than -----.
a) Six Months b) No Time interval
c) 365 Days d) Non of above

6. The shares bought back should be ----- Equity hares.
a) **Cancelled** b) Re-issue
c) Fully paid d) Bonus Shares

7. Extract Balance Sheet Liabilities side

	₹
Equity Share Capital [₹10]	5,00,000
Preference Share Capital	4,00,000
Securities Premium	2,00,000
General Reserve	4,00,000

Maximum no. of Buy Back of. Of Shares = -------.
a) 12500 b) 1500
c) 25,000 d) 5000

8. Extract Balance Sheet Liabilities side

	₹
Equity Share Capital [₹10]	5,00,000
Preference Share Capital	4,00,000
Securities Premium	2,00,000
General Reserve	4,00,000

Maximum no. of Buy Back of. Of Shares at ₹400 = -------.
a) 25000 b) 5,000
c) 10,000 d) None of the above

9. Extract Balance Sheet Liabilities side

	₹
Equity Share Capital [₹10]	10,00,000
Preference Share Capital	5,00,000
Securities Premium	3,00,000
General Reserve	2,00,000

Maximum no. of Shares at best possible price -------.
a) ₹100 b) ₹95
c) ₹125 d) ₹250

10. Buy back shares can be out of ------.
a) Revenue Profits b) Proceeds of fresh issue
c) **Securities Premium** d) Any or all the above

11. The objective of buy back of equity shares is -------.
a) **To increase E.P.S**. b) To bring cash in the business
c) Increase quick ratio d) All of the above

12. Buy-Back shares is governed by ---------.
a) **Section 77A to 77B of the Companies Act, 2013**
b) Section 67 to 70 of The Companies Act, 2013
c) Section 80 of The Companies Act, 2013
d) Section 100 of The Companies Act 2013

13. In case of buy-back at discount, the discount amount is credited to --------.
a) C.R.R b) Securities Premium A/c
c) **Capital Reserve A/c** d) Equity Shareholders A/c

B) State whether the statements are True or False

1. The shares must be cancelled and destroyed after buy-back.
2. A company can buy back any number of equity shares.
3. The class of shares subject to buy-back cannot be issued immediately.
4. The buy back of shares can be effected by purchasing from open market.
5. The fully paid up equity shares can be brought back.
6. The class of shares brought back cannot be issued immediately.
7. Premium paid on buy-back of equity shares can be debited to share capital.

8. The company must buy-back equity shares out of issue of same class of shares.
9. The company must open Escrow a/c on buy-back of Equity Shares.
10. The company going for buy-back must file solvency declaration with SEBI.
11. The company must destroy the share certificate after buy-back within 50 days.
12. As per the Company's Act 2013, buy back of shares amount to Capital Reduction.
13. Capital Redemption Reserve can be used for issue of fully paid Bonus Share.
14. Working Capital / Short term loan must be included in debt for calculating Debit : Equity Ratio.
15. A company can buy-back the shares issued to employees of the company under ESOP.
16. Buy-Back of Equity shares is governed by section 77A to 77B of Companies Act 2013.
17. The uncollected amount must be on buy-back should be added to Share Capital.
18. There is no restriction on frequency of buy-back.
19. Equity shares can be brought back out of fresh issue of Preference Shares.
20. Securities premium can be used for premium on buy-back of Equity Shares.

Answer: TRUE = 1, 3, 4, 5, 6, 9, 10, 13, 15, 19, 20
FALSE = 2, 7, 8, 11, 12, 14, 16, 17, 18

C) Match the columns:

COLUMN A		COLUMN B	
1.	Buy-Back of Shares	a)	Credited to Capital Reserve
2.	Debt equity after buy-back	b)	Article of Association
3.	Discount on buy-back	c)	Must be destroyed within 7 days
		d)	Revenue Reserve
		e)	Section 67 to 70
		f)	Section 77A to 77B
		g)	2 : 1

Ans: 1 = b , 2 = g , 3 = c, 4 = a, 5 = b

D.1 B)

COLUMN A		COLUMN B	
1.	Preference Shares	a)	Own Fund
2.	Debenture	b)	Bonus Share
3.	Board of Directors	c)	Redemption
4.	Capital Redemption Reserve	d)	Loan Fund
5.	Equity	e)	Own Fund
		f)	NOT PREMITED
		g)	SEBI GUIDELINES

15
BUYBACK OF EQUITY SHARES II

Unit Structure

15.0 OBJECTIVES

After studying the unit students will be able to solve the practical problems related to buy back.

15.1 SOLVED PROBLEMS

Illustration - 1

The Balance Sheet of Bharat Ltd. as on 31st March, 2015

Liabilities	₹	Assets	₹
Share Capital		Fixed Assets	38,00,000
Equity (₹10)	10,00,000	Investments	2,00,000
Preference (₹100)	2,00,000	Current Assets	45,00,000
		(including Bank Bal)	
Reserves			
Securities Premium	1,00,000		
General Reserves	25,00,000		
Profit & Loss A/c	3,00,000		
Loans	40,00,000		
Current Liabilities	4,00,000		
	85,00,000		**85,00,000**

Ascertain maximum no. of equity shares can be bought back if:
a) Buy back is at par.
b) Buy back at a premium of ₹ 12 per share.
c) Buy back is at ₹ 51.25 each.

Solution : Option -A

Buy Back is at par.

1. Maximum no. of Equity Shares 25%
   i.e., 25% of ₹10,00,000 = ₹25,000 shares of ₹10 each at par ₹ 2,50,000)

2. Total amount of buy back
   This should not be less then 25% of paid up capital & free reserves

		₹
Equity Share Capital		10,00,000
Preference Share Capital		2,00,000
Free Reserves		
Securities Premium	1,00,000	

General Reserves	25,00,000	
Profit & Loss A/c	3,00,000	29,00,000
		41,00,000

25% of ₹41,00,000 = ₹10,25,000
This is not exceed.

3. Debt equity ratio after buy back
   Total capital+Reserves after buy back= ₹41,00,000 - ₹2,50,000 = ₹38,50,000
   Total Debts = ₹40,00,000

   $$\text{Debt Equity ratio} = \frac{40,00,000}{38,50,000}$$

   = 1.04 : 1
   This is less than 2 : 1
   Thus maximum shares for buy back will be 25000 shares at ₹10 each

Option - B

Buy Back at a premium of ₹12 per share = ₹22 per share.

1. Maximum no. of equity shares 25%
   i.e., 25% of ₹10,00,000 = ₹25,000 shares of ₹10 each at par (₹2,50,000)

2. Total amount of buy back 25,000 shares @ ₹22 i.e., ₹5,50,000 this should not be less then 25% of paid up capital & free reserves.

		₹
Equity Share Capital		10,00,000
Preference Share Capital		2,00,000
Free Reserves		
Securities Premium	1,00,000	
General Reserves	25,00,000	
Profit & Loss A/c	3,00,000	29,00,000
		41,00,000

25% of ₹41,00,000 = ₹10,25,000
Buy back is within limits

3. Debit ratio after buy back
   Total amount after buy back ₹41,00,000 - ₹5,50,000 = ₹35,50,000. Totl Debt ₹40,00,000.

$$\text{Debt Equity ratio} = \frac{41{,}00{,}000}{35{,}50{,}000}$$

= 1.15 : 1
This is less then 2 : 1
Here also maximum shares for buy will be 25000 shares @ ₹22 per share.

Option - C

Buy Back at ₹51.25 per share.

1. Maximum no. of equity shares 25%
   i.e., 25% of ₹10,00,000 = 25,000 shares of ₹10 each at par (₹2,50,000)

2. Total amount of buy back
   25,000 shares @ ₹51.25 = ₹12,81,250.

		₹
Equity Share Capital		10,00,000
Preference Share Capital		2,00,000
Free Reserves		
Securities Premium	1,00,000	
General Reserves	25,00,000	
Profit & Loss A/c	3,00,000	29,00,000
		41,00,000

25% of ₹41,00,000 = ₹10,25,000
Since this is exceed, buy back cannot be done for 25000 shares.

The maximum shares that can be given for buy back @ ₹51.25 be calculated as under :

$$\frac{10{,}25{,}000}{51.25} = 20{,}000 \text{ shares.}$$

3. Debt equity ratio after buy back
   Total capital = ₹41,00, 000 - ₹10,25, 000 = ₹30,75,000
   Total Debt = ₹40,00,000

$$\text{Debt Equity ratio} = \frac{40{,}00{,}000}{30{,}75{,}000}$$

= 1.30 : 1
This is less the 2 : 1
Therefore the maximum shares for Buy Back will be 20000 shares @ ₹ 51.25 per share.

Illustration 2

The Balance Sheet of B.B. Ltd., as on 31st March 2015.

Liabilities	₹	Assets	₹
Share Capital		Fixed Assets	16,00,000
Equity (₹10)	4,50,000	Investments	1,50,000
Preference (₹100)	1,50,000	Current Assets	7,25,000
Reserves			
Securities Premium	2,25,000		
General Reserves	3,00,000		
10% Debentures secured on fixed asset	12,00,000		
Sundry Creditors	1,25,000		
O/s expenses	25,000		
	24,75,000		**24,75,000**

Keeping in view all the requirements of Companies Act, 2013, ascertain the maximum no of equity shares that B.B.Ltd. can buy back at ₹30 per share, being the current market price - Assume that the buy back is carried out actually & give necessary journal entries to record the same.

Solution :

Step - 1

	₹	₹
Calculate Sources for Buy Back:		
a) Free Reserves - General Reserve	3,00,000	
b) Securities Premium	2,25,000	
Total Sources (a + b)		5,25,000

Step - 2

	₹	₹
Calculate limit of 25% of own funds		
a) Sources (free reserves + securities premium as per step-1)	5,25,000	
b) Paid up capital (equity + preference)	6,00,000	
c) Total Own Funds	11,25,000	
d) 25% of Own funds (25% x 11,25,000)		2,81,250

Step - 3

	₹	₹
Calculate minimum own funds remaining after buy back		
a) Calculate minimum own funds = Debt / 2 = 12,00,000 / 2	6,00,000	
b) Calculate required post buy back own funds		
= Own funds before buy back - Minimum own funds		
= 11,25,000 - 6,00,000		5,25000

Step - 4

	₹	₹
Calculate limit of 25% of Equity Capital during the year:		
a) Maximum NV of equity shares which could be bought back during financial year.		
= 25% of total paid up equity share capital		
= 25% x 4,50,000	1,12,500	
b) Maximum no. of equity shares that can be bought back at par		
= Amount as per 4a / face value per share		
= 1,12,500 / 10	11,250	
c) Buy Back amount if equity shares in b) at offer price ₹ 30		
= 11,250 x 30		3,37,500

Conclusion : At the given offer price, the maximum possible buy back will be the least of the above four amounts i.e., ₹2,81,250. Hence the company can buy back (281250 / 30) = 9375 equity shares keeping in view all the legal conditions.

These shares can be bough back at a price of ₹30 each including premium of ₹20 per share.

Journal Entries in the Books of B.B.Ltd.,

			Dr. ₹	**Cr. ₹**
1.	Equity Share Capital A/c	Dr.	93,750	
	Premium on buy back of share A/c	Dr.	1,87,500	
	To Equity shareholders A/c			2,81,250
	(Being amount payable on buy back of 9375 equity shares of 10 each at a premium of 20 per share.)			
2.	General Reserve A/c	Dr.	93,750	

	To Capital Redemption Reserve A/c (Being the amount equal to the face value of share bought back transferred from general rese3rve to CRR)		93,750
3.	Equity shareholders A/c Dr. To Bank A/c (Being the payment made to equity shareholders on buy back.)	2,81,250	2,81,250
4.	Securities Premium A/c Dr. To premium on buy back of share A/c (Being premium on buy back provided)	1,87,500	1,87,500

Illustration : 3

Balance Sheet of Yashshree Ltd. As on 31st March 2015

Liabilities	₹	Assets	₹
Share Capital		**Fixed Assets**	
Equity shares of 10 each	25,00,000	Gross block	55,94,000
7% Preference Shares of ₹100	9,00,000	Less: Depreciation	[12,50,000]
		Net Block	43,44,000
Reserves		Capital Work-in-Prog.	1,50,000
Securities Premium	12,00,000	**Investments:**	
General Reserve	12,50,000	6% R.B.I. Bonds	3,20,000
12% Debentures [100 each]	19,00,000	9% local securities	12,50,000
Fixed deposits [5 years]	7,50,000	Inventories	4,50,000
Sundry Creditors	2,25,000	S. Debtors	11,50,000
Outstanding Expenses	45,500	Cash in Hand	72,000
		Bank Balance	7,58,000
		Short term investments	57,000
		Bill Receivable	2,12,000
		Prepaid exp.	7,500

	87,70,500		**87,70,500**

The Company wants to buy -Back 25% of it's equity capital at 25% premium. For this purpose. The company issued 2000, 9% Preference Shares of ₹100 each at @ 25% premium entire amount payable on application. These shares were duly taken up subsequently the company bought back the Equity Shares. Pass necessary journal entries to record above transaction & prepare Balance Sheet there after.

Solution :

Step - 1

	₹
Calculation of Buy-Back:	
a) Free Reserves-General Reserve	12,50,000
b) Securities Premium	12,00,000
Total Sources:	**24,50,000**
And issue of 2000 preference shares of ₹100 each @ 20% premium	

Step - 2

	₹
Calculate limit of 25% of Own Funds	
a) Sources [Free Reserve + Securities Premium [as per 1)	24,50,000
b) Paid-up capital [equity + pref.]	34,00,000
Total own funds	**58,50,000**
25% of Own Funds after Buy-Back = 58,50, 000 x 25% = ₹14,62,500	

Step - 3

Calculation of minimum Funds after Buy-Back

a) Calculate minimum own funds = Debts / 2

= [Deben. + Fixed deposits] / 2 = 31,50,000 / 2 = ₹15,75,000

= OWN FUNDS BEFORE BUY-BACK - MINIMUM OWN FUNDS

= 58,50,000 - 15,75,000 = ₹42,75,000

Step - 4

Buy - Back :
25% of 2,50,000 Share = 62,500 Equity Shares of ₹10 each
Buy-Back funds required 62,500 x 12.50 per share = ₹7,81,250

As amount of Buy-Back ₹7,81,250 less than amount. Calculated in Step 2 & 3, the Company can buy-back 62500 equity shares of at PREMIUM of ₹2.50.

WORKING FOR C.R.R. =
C.C.R. = 6,25,000 - 2,00,000 = ₹4,25,000

Journal Entries the Books of Yashshree Ltd.

		Dr. ₹	Cr. ₹
1.	Bank A/c Dr.	2,50,000	
	To 9% Preference Capital A/c		2,00,000
	To Securities Premium A/c		50,000
	(Being 2000, 9% Preference shares of 100 each issued at 25% premium)		
2.	Equity Share Capital A/c Dr.	6,25,000	
	Premium on Buy-Back of Share A/c Dr.	1,56,250	
	To Equity Shareholders A/c		7,81,250
	(Being amount due on Buy-Back transferred)		
3.	General Reserve A/c Dr.	4,25,000	
	To Capital redemption Reserve A/c		4,25,000
	(Being amount equal to buy-back of equity shares brought back out of profit transferred to C.R.R.)		
4.	Securities Premium A/c Dr.	1,56,250	
	To Premium on Buy-Back of Share A/c		1,56,250
	(Premium on Buy-Back of Share adjusted)		
5.	Equity Shareholders A/c Dr.	7,81,250	
	To Bank A/c		7,81,250
	(Being Buy-Back amount paid)		

Yashshree Ltd.

Balance Sheet as at 31st March 2015

	Source of Funds		₹	₹
1.	**Shareholder's Fund:**			
	a) Capital	1	29,75,000	
	b) Reserves & Surplus	2	23,43,750	53,18,750
2.	**Loan Funds:**			
	a) Secured Loans	3	19,00,000	
	b) Unsecured Loans	4	7,50,000	26,50,000
	Total ₹			**79,68,750**
	Application of Funds:	5		
1.	**Fixed Assets**			
	a) Gross Block		55,94,000	
	b) Less: Depreciation		[12,50,000]	
	c) Net Block		43,44,000	
	d) Capital Work in-Progress	6	1,50,000	44,94,000
2.	Investment			15,70,000
3.	**Current Assets, Loans & Advances:**			
	a) Inventories		4,50,000	
	b) Sundry Debtors	7	11,50,000	
	c) Cash and Bank Balances	8	2,98,750	
	d) Other Current Assets	9	57,000	
	e) Loans and Advances		2,19,500	
			21,75,250	
	Less: Current Liabilities and Provisions:			
	a) Liabilities	10	[2,70,500]	
	b) Provisions			
	Net Current Assets			19,04,750
4.	a) Miscellaneous Expenditure to the extent not written off or adjusted			
	b) Profit & Loss Account			
	Total ₹			**79,68,750**

Schedule : No. 1	₹
Authorised:	
...... shares of 10 each	
Issued, Subscribed, called up and paid-up:	

1,87,500 Equity Shares of 10 each fully paid-up		18,75,000
9000, 7% Preference Shares of 100 each fully paid-up		9,00,000
2000, 9% Preference Shares of 100 each fully paid-up		2,00,000
		29,75,000
Schedule : No. 2		
Reserves & Surplus		
Securities Premium Bal. b/fd.		12,00,000
Add: recd. On fresh issue		50,000
		12,50,000
Less: Utilised for Premium on Buy-Back of Shares		[1,56,250]
		10,93,750
Capital Redemption Reserve		
General Reserve Bal. b/fd.	12,50,000	
Less: Transferred to C.R.R.	[4,25,000]	8,25,000
		23,43,750
Schedule : No.3		
Secured Loans		
12% Debenture [₹100 each]		19,00,000
Schedule : No. 4		
Unsecured Loans:		
Fixed Deposits [5 years]		7,50,000
Schedule : No. 5		
Fixed Assets:		
Gross Block	55,94,000	
Less: Depreciation	[12,50,000]	
Net Block	43,44,000	
Capital Work-in-Progress	+ 1,50,000	44,94,000

Schedule : No. 6		
Investments		
6% R.B.I. Bonds	3,20,000	
9% Local Govt.,	12,50,000	15,70,000
Schedule : No. 7		

Cash & Bank Balance		
Cash on Hand	72,000	
Bank Balance b/fd.	7,58,000	
+ Issue of Preference Share + Premium	2,50,000	
Less: Buy-Back Payment	[7,81,250]	2,98,750
	2,26,750	
Schedule : No. 10		
Current Liabilities:		
Sundry Creditors	2,25,000	
Outstanding Exp.	45,500	2,70,500

Illustration : 4

Nada Ltd. Furnishes the following information:	₹
80,000 Equity Share of 10 each, 7 per share called-up & paid-up	5,60,000
General Reserve	80,000
Profit & Loss A/c	6,00,000
Securities Premium	1,20,000
Bank Loan [Secured]	3,00,000
Unsecured Loan	1,00,000

Keeping in view Legal requirements, ascertain the maximum number of Equity Shares that can be bought back by the company at a price of ₹40 per share. Also give necessary Journal Entries in the books of Nada Ltd assuming that buy back is actually carried out. (March, 09)

Solution:

In the Journal of Nada Ltd.

		Dr. ₹	Cr. ₹
1.	Shares Final Calls A/c Dr.	2,40,000	
	To Equity Shares Capital A/c		2,40,000
	(Being share final call made on 80000 shares at ₹3 per share)		
2.	Bank A/c Dr.	2,40,000	
	To Shares Final Calls A/c		2,40,000
	(Being share final calls due received)		
3.	Equity Share Capital A/c Dr.	1,00,000	
	Premium on Buy-Back of Equity	3,00,000	

	Shareholders A/c Dr. To Equity Shareholders A/c (Being amount due on buy-back of 10,000 shares of ₹10 at ₹40 per share)		 4,00,000
4.	Securities premium A/c Dr. Profit & Loss A/c Dr. To Premium on Buy-Back of Equity Shares (Being Premium payable on Buy-Back of Equity Shares adjusted)	1,20,000 1,80,000	 3,00,000
5.	Profit & Loss A/c Dr. To Capital Redemption Reserve A/c (Being C.R.R created to the extent buy-back out profit)	1,00,000	 1,00,000
6.	Equity Shareholders A/c Dr. To Bank A/c (Being equity shareholders dues paid)	4,00,000	 4,00,000

The Company can buy-back maximum 25% of fully paid-up equity shares in a financial year. 25% of 80,000 shares = 20,000 @ ₹40 = ₹8,00,000.
However it's is subject to further limits, as under:

1.	**25% of Own Funds:**		
	Equity Share Capital		8,00,000
	General Reserve	80,000	
	Profit & Loss A/c	6,00,000	
	Securities Premium	1,20,000	8,80,000
	Own Funds		16,00,000
	25% of 16,00,000 = 4,00,000		
2.	**Own Funds After buy-back**		
	Own Fund - 50% of Debt [Bank Loan + Unsecured Loan]		
	16,00,000 - 50% [3,00,000 + 1,00,000]		
	16,00,000 - 2,00,000 =		14,00,000
3.	**Amount payable on 20,000 <u>eq.shares@₹40=8,00,000</u>**		
	Amount 1 or 2 or 3, which were less is the amount available for Buy -Back = ₹4,00,000		

	No. of Shares can be brought back @ ₹40 each 4,00,000 ÷40 = 10,000 equity shares of ₹10 each @ ₹40 each		

Illustration : 5

Karmay Ltd. Furnishes the following information:	₹
1,00,000 Equity shares of 10 each, fully paid-up	10,00,000
General Reserve	22,80,000
Profit & Loss A/c	6,00,000
Securities Premium	2,00,000
Bank Loan (secured)	5,00,000
Unsecured Loan	7,00,000

Keeping in view Legal requirements, ascertain the maximum number of Equity shares that ca be bought back by the company at best possible price. Buy-Back Exp. ₹5,000.

Solution:

For Buy Back of Equity Shares, Karmay Ltd. Must comply, various conditions laid down under Companies Act, 2013.

Limits were as under:

1. Maximum number of Shares can be brought back in a Financial Year should not exceed 25% of fully paid-up Equity Shares.

   25% of 1,00,000 shares = 25,000 eq. Shares of ₹10 each.

2. Buy-Back amount should not exceed 25% of own Funds, As per Latest audited Balance Sheet.

Equity Share Capital		10,00,000
Reserves		
General Reserves	22,80,000	
Profit & Loss A/c	6,00,000	
Securities Premium	2,00,000	30,00,000
		40,00,000

25% of 40,00,000 = 10,00,000

3. After buy-back, Debt Equity ratio should not be more than 2:1

Funds available can be ascertained as under
Own funds - 50% of Debts [Long Term Loans]
40,00,000 - 50% [5,00,000 + 7,00,000]
40,00,000 - 6,00,000 = 34,00,000 = ₹34,00,000
Least of 2 and 3, Maximum amount available for Buy-Back = ₹10,00,000.

Best Possible Price = Amount Available / No. of Shares to be bought back = 10,00,000 + 25,000 = ₹40 each.

Illustration - 8

Katha Ltd., furnishes you with the following Balance Sheet as at 31st December, 2015.

Particulars	₹	₹
Sources of Funds:		
Share Capital:		2,00,000
Authorised:		
Issued:		
12% Redeemable Preference Share of 100 each fully paid	75,000	
Equity Shares of ₹10 each fully paid	25,000	1,00,000
Reserves and Surplus:		
Capital Reserve	15,000	
Securities Premium	25,000	
General Reserve	2,60,000	3,00,000
Total ₹		4,00,000

Funds Employed in:		
Fixed Assets (cost)	1,00,000	
Less: Provision for depreciation	1,00,000	NIL
Investment at cost (Market Value ₹4,00,000)		1,00,000
Current Assets	3,40,000	
Less: Current Liabilities	40,000	3,00,000
Net Current Asset Total ₹		**4,00,000**

The company bought back 500 equity shares of ₹10 each at ₹50 per share. The payments for the above made out of the huge bank balances which appeared as part of current assets.

You are asked to pass journal entries to record the above. Also prepare Balance Sheet after buy back.

Solution:

In the Books of Katha Ltd
Journal Entries

Date	Particulars	LF	Dr. ₹	Cr. ₹
1.	Equity Shares Capital A/c Dr.		5,000	
	Premium on Buyback of shares A/c Dr.		20,000	
	To Equity Shareholders A/c			25,000
	(Being the amount payable on buy back)			
2.	Revenue Reserve A/c Dr.		5,000	
	To Capital Redemption Reserve A/c			5,000
	(Being amount equal to nominal value of equity shares bought back transferred to capital redemption reserve)			
3.	Equity Shareholders A/c Dr.		25,000	
	To Bank A/c			25,000
	(Being buy back of equity shares of ₹10 each from the members at a price of ₹50 per share)			
4.	Revenue Reserve A/c Dr.		20,000	
	To Premium Buyback of Shares A/c			20,000
	(Being premium on Buyback adjusted)			

Balance Sheet of Katha Ltd. as at 31st December 2015

I)	SOURCES OF FUNDS:	Schedule No.		
1.	Shareholder's Funds:			
	Share Capital	1	95,000	
	Reserves and Surplus	2	2,80,000	
				3,75,000
2.	Loans Funds:			-
	Total ₹			3,75,000
II)	**APPLICATIONS OF FUNDS:**			
1.	Fixed Assets:			
	Gross Block		1,00,000	
	Less: Depreciation		1,00,000	-
	Net Block			
2.	Investment (Market Value ₹4,00,000)			1,00,000
3.	Current Assets, Loans and Advances		3,15,000	
	Less: Current Liabilities and Provisions		[40,000]	
	Net Current Assets			2,75,000
4.	Miscellaneous Expenditure			-

	(Not written off/adjusted)			
	Total ₹			**3,75,000**

Illustration : 9

Jain Ltd. decided to buy back the maximum number of equity shares that the Company can Buy Back by offering the maximum possible price after complying with all the necessary legal conditions as on March 31st 2015. On that date their position was as under:

Balance Sheet

Liabilities	₹	Assets	₹
Share Capital		Fixed Assets	1,40,000
4000 eq. Share of ₹100 each	4,00,000	Bank Balances	8,60,000
4000 6% redeemable pref shares of ₹50/- each ₹25/- per Share paid up.	1,00,000		
2000 8% redeemable pref shares of ₹100/- each fully paid.	2,00,000		
Reserve & surplus security premium	20,000		
Capital reserve	80,000		
Dividend equalization Reserve	1,10,000		
Current Liabilities	90,000		
	10,00,000		**10,00,000**

To enable the buy back to be carried out the Company decides to issue after carrying out the necessary formalities required under Law, minimum no. of new preference shares of ₹100/- each at par. The buyback is duly carried out. Show Journal entries relating to the buyback and also the balance sheet after redemption and buyback. Along with the buyback company redeemed both the classes of preference shares. By issued of fresh preference shares.

Solution :

When the price for buy back is not given :

To find out the offer price. Following steps must be followed.

1) Find out the sources of buyback.
2) Find out 25% on paid up capital and reserves.

3) Find out the maximum No. of equity shares that can be bought out from the market by using following formula.
   Existing equity shares × 25%.
4) Find out the offered price by using following formula :

$$\frac{\text{Maximum amount available for buyback as per step as per step 2}}{\text{Maximum No. of equal shares that can bought as per step 3.}}$$

I) Redemption Plan :

1) 4000 6% p/s of ₹50/- each 2,00,000 [F.V.]
   2000 8% p/s of ₹100/- each 2,00,000 [F.V.]

   4,00,000

2) F.V. of Pref. Shares redeemed = fresh issue + Free Reserve
   4,00,000 = 4,00,000 + NIL

II)

1) Sources of buy back
   Free reserves
   Dividend equalization Reserve 1,10,000
   Security premium 20,000

   1,30,000

2) Maximum amount available for buyback 25% on paid up capital + Free Reserve
   ₹4,00,000 F.V. + ₹4,00,000 = ₹8,00,000 share capital
   25% (8,00,000 + 1,30,000)
   25% × 9,30,000
   = 2,32,000

3) Maximum No. of Equity shares the co. can bayback
   Existing equity shares × 25%
   4000 × 25% = 1000

4) Offered Price :

$$\frac{\text{Maximum amount available for buyback can be bought back}}{\text{Maximum No. of equity shares}}$$

$$= \frac{2,32,500}{1000}$$

$$= 232.50$$

III) Amount of buyback
(1000 × 100) = 1,00,000 (F.V.)

$$\left(1000\times132.5\right)=\frac{1,32,500}{2,32,500}\left(\text{Prem}\right)$$

$=232.50$

F.V. of buy back = Fresh Issue + Free Reserve
1,00,000 = 1,00,000 + NIL
Premium on buyback = Security Premium + Other Reserve
1,32,500 = 20,000 + 1,12,500

Dividend equalization 1,10,000   Cap. Reserve 2500

Journal Entries in the Books of Jain Ltd.

Date	Particulars	Debit ₹	Credit ₹
1.	6% pref. share final call A/c Dr. To 6% pref. Share Capital A/c [Being final call made on 4000 shares @ ₹25/-]	1,00,000	 1,00,000
2.	Bank A/c Dr. To 6% Pref. Share Final call A/c [Being final call money received]	1,00,000	 1,00,000
3.	Bank A/c Dr. To new pref. Share Capital A/c [Being new pref. Shares issued at par for the purpose of redemption of per share]	4,00,000	 4,00,000
4.	6% pref. Share Capital A/c Dr. 8% pref. Share Capital A/c Dr. To pref. Share holder A/c [Being pref. Shares redeemed at par]	2,00,000 2,00,000	 4,00,000
5.	Pref. Share holder's A/c Dr. To Bank A/c [Being Amount paid to p.s.h.]	4,00,000	 4,00,000
6.	Bank A/c To new pref. Share Capital A/c [Being new pref. Shares issued at par dor the purpose of buy back]	1,00,000	 1,00,000
7.	Equity Share Capital A/c Dr. Premium on buyback A/c Dr. To Eq. Share Holder's A/c [Being eq. Shares bought back by Co.]	1,00,000 1,32,500	 2,32,500
8.	Security Premium A/c Dr. Dividend equalization Reserves A/c Dr. Capital Reserve A/c Dr.	20,000 1,10,000 2,500	
	To premium on buyback A/c [Being Security premium and other Reserves are utilized for canceling premium on buyback]		1,32,500
9.	Eq. Shareholder's A/c Dr.	2,32,500	

	To Bank A/c [Being Amount paid to equity shareholders]		2,32,500

The Balance of Jain Ltd. as on 31st March, 2015

	Particulars	Schedule No.	Amt. as on 31.03.2015	Amt. as on 31.03.15
	Sources of Funds			
1.	Shareholder's Funds :			
	a) Capital	1	8,00,000	
	b) Reserves & Surplus	2	77,500	8,77,500
2.	Loan Funds :			
	a) Secured Loans			
	b) Unsecured Loans			NIL
	Total ₹			8,77,500
	Application of Funds :			
1.	Fixed Assets			1,40,000
2.	Investments			NIL
3.	Current Assets, Loans & Advances :			
	Cash and Bank Balances	3	8,27,500	
	Less : Current Liabilities and Provisions :		[90,000]	
	a) Liabilities		NIL	
	b) Provisions			
	Net Current Assets			7,37,500
4.	a) Miscellaneous Expenditure to the extent not written of or adjusted			
	b) Profit & Loss Account			
	Total ₹			8,77,500

Schedule : 1
Share Capital Authorized Issued,
Sub. Called up, Paid-up

3000, Equity Shares of ₹100 each	3,00,000	
5000 New Preference Shares ₹100 each	5,00,000	8,00,000

Schedule : 2
Reserves & Surplus

Securities Premium	20,000	NIL
Less; Premium on buy-back	[2500]	
	77,500	
Dividend Equalization Reserve	1,10,000	
Less; Premium on buy-back	[1,10,000]	NIL

77,500

Schedule : 3

Bank Balance	8,60,000	
Add Pref. Shares Final call	1,00,000	
+ Issue of New Pref. Shares	4,00,000	
+ Issue of New Pref. Shares	1,00,000	
Less : Redemption of Pref.	[4,00,000]	
Less : Buy-Back of Eq. Shares	[2,32,500]	8,27,500

Illustration : 12

The summarized Balance Sheet of Kumar Ltd. as on 31st March, 2015 was as follows.

Liabilities	₹	Assets	₹
10,000, 8% Pref. Shares of ₹100, each	10,00,000	Fixed Assets	
1,00,000 Equity Shares of ₹10 each	10,00,000	Gross Block	24,45,000
General reserve	8,00,000	Less : Depreciation	[9,21,000]
Profit & Loss A/c	10,00,000	Net Block	15,24,000
10% Debentures	10,00,000	Capital Work-in-Progress	1,25,000
Loan from Directors	2,00,000	Current Assets Inventories	75,000
Current Liabilities Creditors	1,50,000	S. Debtors	14,25,500
Provision for Taxation	2,75,000	Cash & Bank Bal.	22,39,000
		Loan & Advance	31,500
		Discount on issue of Debenture	5,000
	54,25,000		54,25,000

The redemption purpose the Company issued the requisite number of new, 10% Pref. Shares of ₹100 each at par.

On 1st April, 2015 the company decided to Buy-back by offering the maximum no. of Equity shares that can be bought back by offering maximum possible price after complying with all necessary requirement Pass journal entries and prepare Balance Sheet after buy-back as on 1st April 2015.

Solution :

1) Redemption 10,000 8% Preference Shares of ₹100 at par F.V. of Pref. Shares redeemed = Fresh Issue + Free Reserve ₹10,00,000 = 10,00,000 + NIL.

   Therefore no need of transferring free reserve to C.R.R.

2) Buy-Back of Equity Shares at best possible Price limits of Buy-back U/S : 68
a) Maximum 25% of Equity Capital can be bought during any financial year = 25% of 1,00,000 = 25,000 Equity Shares can be brought back of ₹10 each = ₹2,50,000.

A) Maximum 25% of OWN FUNDS can be used for Back : [Sources of buy-back]

Paid up Capital [Eq. + New Pref.]		20,00,000
Free Reserve :		
General Reserve	8,00,000	
Profit & Loss A/c	10,00,000	
	1,00,000	
Less : Discount on issue of Deb.	[5000.] +	17,95,000
	Own Funds :	₹37,95,000

25% OF OWN FUNDS = 37,95,000 × 25% = 9,48,750

OR

B) After the Buy-Back Debts Equity ratio should not exceeds : 2 : 1. It means Debts owed by the company should not exceed twice the amount of Capital and free reserves.

I) Calculate Minimum Own funds reaming after Buy-back
= Debts ÷ 2 = 50% of [secured + unsecured loans]
= 50% of [10,00,000 + 2,00,000] = ₹6,00,000
Calculate required own funds after buyback
= OWN FUNDS before buyback - minimum own funds
= 42,95,000 - 6,00,000 = ₹36,95,000 = ₹36,95,000

Least of a & b is the amount available for buyback = ₹9,48,750

Maximum No. of Equity Shares of BEST POSSIBLE PRICE

$$= \frac{\text{Amount available for buy-back}}{\text{Maximum no. Equity Shares to be brought back}}$$

$$= 9,48,750 \div 25,000 = ₹37.95$$

COMPANY CAN BUYBACK 25,000 EQUITY SHARES AT ₹37.95 per Equity Share.

Journal Entries in the Kumar Inc.

Date	Particulars		Debit ₹	Credit ₹
31.03.15	Bank A/c	Dr.	10,00,000	

	To New 10% Preference Share Capital A/c [Being New 10% Pref. Shares issued at Par]		10,00,000
31.03.15	8% Preference Share Capital A/c Dr. To Preference Shareholders A/c [Being new preference shares issued at par]	10,00,000	10,00,000
31.03.15	Preference Shareholders A/c Dr. To Bank A/c [Being Preference Shareholders paid]	10,00,000	10,00,000
1.04.15	Equity Share Capital A/c Dr. Premium of Buy-Back A/c Dr. To Equity shareholders A/c [Being Equity Share Capital Cancelled due to Buy-Back]	2,50,000 6,98,750	9,48,750
1.04.15	Equity shareholders A/c Dr. To Bank A/c [Being Equity Shareholders paid]	9,48,750	9,48,750
1.04.15	Profit & Loss A/c Dr. To premium on Buy-Back A/c [Being premium on Buy-Back provided]	6,98,750	6,94,750
1.04.15	General Reserve A/c Dr. To Capital Redemption Reserve [Being C.R.R. Created]	2,50,000	2,50,000

Balance of Sheet KUMAR INC as on 1st April 2015 (After Buy-Back)

	Particulars	**Schedule No.**	**₹ 31.03.2015**	**₹ 31.03.2015**
	Sources of Funds			
1.	Shareholder's Funds :			
	a) Capital	1	17,50,000	
	b) Reserves & Surplus	2	11,01,250	28,51,250
2.	Loan Funds :			
	a) Secured Loans	3	10,00,000	
	b) Unsecured Loans	4	2,00,000	12,00,000
	Total ₹			40,51,250
	Application of Funds :			
1.	Non-Current Assets			
	a) Gross Block		24,45,000	
	b) Less : Depreciation		[9,21,000]	

	c) Net Block		15,24,000	
	d) Capital Work-in-Progress	5	1,25,000	16,54,000
	e) Other Non Current assets discount on issue debentures		5,000	
2.	Investments			
3.	Current Assets, Loans & Advances :	6		
	a) Inventories		75,000	
	b) Sundry Debtors		14,25,500	
	c) Cash and Bank Balances		12,90,250	
	d) Other Current Assets		--	
	e) Loans and Advances		28,22,250	
	Less : Current Liabilities and Provisions :			
	a) Liabilities	7	1,50,000	
	b) Provisions	8	2,75,000	
	Net Current Assets		4,25,000	

Schedule : 1
Share Capital

Authorized share Capital Issued,	
Subscribed Called up & Paid-up	
10,000, 10% Pref. Shares of ₹100 each fully paid	10,00,000
7,50,000 Equity Shares of ₹10 each fully paid	7,50,000
	17,50,000

Schedule : 2
Reserves & Surplus

Capital Redemption Reserve		2,50,000
[by Tranf. From Gen. Res]		
General Reserve	8,00,000	
Less : Threaf to C.R.R.	[2,50,000]	5,50,000
Profit & Loss A/c	10,00,000	
Less : Premium on Bay-Back	[6,98,750]	3,01,250
		11,01,250

Schedule : 3

Secured Loans

10% Debentures 10,00,000

Schedule : 4
Unsecured Loans :

Loans from Directors 2,00,000

Schedule : 5
Fixed Assets

Gross Block	24,45,000	
Less : Depreciation	[9,21,000]	
Net Block	15,24,000	
Capital Work in Progress	1,25,000	16,49,000

Schedule : 6
Current Assets, Loans & Advances
A) Current Assets

Inventories	75,000	
Sundry Debtors	14,25,500	
Cash & Bank	12,90,250	27,90,750

Schedule : 7

Loans & Advances		31,500

Schedule : 8
Provisions

Provision from Taxation		2,75,000

Schedule to Balance Sheet

Particulars	Amount ₹	Amount ₹
SCHEDULE 1 : CAPITAL		
Authorised issued, Subscribed and paid up		1,00,000
2,000 Equity shares of ₹10 each fully paid (500 Equity shares of ₹10 each have been bought back out of reserves at ₹50 per share)		20,000
(12% 750 Redeemable Preference Shares of ₹100 each fully paid)		75,000
Total ₹		95,000
SCHEDULE 2 : RESERVE AND SURPLUS		
Capital Reserve		15,000

Capital Redemption Reserve (as per last account)		
Add : Transfer from Revenue Reserve	5,000	5,000
Securities Premium	25,000	
Less : Premium on buy back	[20,000]	5,000
Revenue Reserve (as per last account)	2,60,000	
Less : Transfer to Capital Redemption Reserve	(5,000)	2,55,000
Total ₹		2,80,000

13. EXERCISE

a) Theory Questions :

1) Explain the term "Buy Back of Shares".
2) Difference between Buy Back of Shares & Redemption of Shares.
3) What are the limitations and restrictions on power to Buy Back of Shares of the Company Act 2013.
4) Explain the provision to be complied with by a company before and after Buy Back of Shares.
5) What are the different modes of Buy Back?

b) Practical Questions

Q.1 The following is the Balance Sheet of JPL Ltd. as on 30/09/2015.

Particulars	Amount ₹	Amount ₹
SOURCE OF FUNDS :		
Authorised :		
25,000 Equity Share of ₹10 each		25,00,000
Issue :		
96,000 shares of ₹10 each (₹8 paid up)		7,68,000
Reserves :		
Securities Premium	3,60,000	
Reserve Fund	1,20,000	
Investment Fluctuation Reserve	60,000	
Balance in Profit & Loss A/c	96,000	6,36,000
Loans :		
Loan from IDBI	4,40,000	
Unsecured loan from directors	1,60,000	6,00,000
Total ₹		20,04,000
APPLICATIONS OF FUNDS :		
Fixed Assets (at WDV) - Net Block		12,84,000
Investments		4,80,000
Current Assets	9,00,000	

Less : Current Liabilities	(6,60,000)	
Net Current Assets		2,40,000
Total ₹		20,04,000

The Company bought back 18,000 equity shares at a price of ₹12 per share after completing the necessary legal provisions. Pass the necessary journal entries for same. Assume adequate bank balances.

Also prepare the Balance Sheet after buyback.

❖❖❖❖