Chapter-2 :- Amalgamation Of Companies (AS-14)

Meaning of Amalagmation

→ Amalgamation refers to the process of merger of two or more companies into a single entity or where one company takes over the other by outright purchase.

- The term amalgamation contemplates two kinds of activities:
  (i) Two or more companies join to form a new company
  (ii) Absorption and blending of one by the other
- In amalgamation we have generally two companies called as
  (a) vendor / transferor company (Seller Co.)
  (b) vendee / transferee company (Buyer Co.)

- Example 1 → Company A and company B amalgamate to form Company C. Company A and Company B are called transferor Companies and Company C is called as the transferee Co. → This Strategy is called as Amalgamation.

- Example-2 → Company A is taken over by company B (purchased) Here company A is called as transferor company and Co. B is transferee Company, This Strategy is Called as absorption

- Example 2 → Company A has been suffering from losses for past 5 years, a new company B is floated to take over the Existing Company A. Here Company A is the transfor Company and company B is transferee company. This Strategy is called as External reconstruction

Understanding the terms

Amalgamation | Absorption | Acquisition | Reconstruction

a. **Amalgamations:-** When businesses of two or more companies are being taken over by a newly formed company the way of merger is called as amalgamation.

* Example- Weak ltd and Strong ltd merged together by way of formation of new company Giant ltd.

Weak ltd → Giant ltd ← Strong ltd

b. **Absorption:-** When businesses of one or more companies are take over by another Existing company the way of merger is called absorption.

* Example- Weak ltd is merged into Strong ltd.

Weak ltd → transferor Co. (Seller)

↓

Strong ltd → transferee Co. (Buyer)

C. **Acquisition:-** If one company acquires (purchase) the controlling interest in another Company, it is acquisition or take over

* Example- Strong ltd takes over 60% Shares of weak ltd.

Strong ltd

↓ 60% Equity Share

Weak ltd

Note:- Evolution of relationship between Companies

① A $\xrightarrow{100\%}$ B Holding & Subsidery relation/ absorption AS-21

② A $\xrightarrow{50\%^{+}}$ B Acquisition AS-21

③ A $\xrightarrow{20\%-50\%}$ B Association AS-23

④ A $\xrightarrow{\text{less than } 20\%}$ B Investment AS-13

⑤ A $\xleftrightarrow{\text{No Sh}}$ B joint venture (particular parmership) AS-27

* Amalgamation → Mergers & acquisitions - takeover
(coperate marriage)

Reasons of Amalgamation

Synergy Benifit
To do something with good intention

To do something with bed intention

બળજબરી ← Hostile takeover, to kill competetion

d. Reconstruction → Substantially same business is carreid on by the same person.

(a) External reconstruction → It means when a company is reconstructed to form new company. old Co. ~~with~~ wound to up

(b) Internal reconstruction → It means the right of investers as well as of creditors are altered, this Co. does not go into liquidation.

Internal	Example	External

Internal	Example	External
Weak ltd.		Sunset ltd
↓		↓
Reconstructed / restructured		wound up by way of formation
↓		↓
Weak ltd.		Starling ltd
(Shareholder and creditors interests are altered).		(Sunset ltd. is wound up)

Calculation of Purchases Consideration

⇒ As per para 3(g) of AS-14, purchase consideration means the "aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company".

- In simple words, it is the price payable by the transferee company to the transferor company for taking over the business of the transferor company.
- Important note- The amount paid towards the equity shareholder and preference shareholders is only considered as part of the purchase consideration
- Any consideration paid to debenture-holders or creditors shall not form part of the purchase consideration

Transferee Co to transfe

"Purchase Consideration"

↓

Something in return

(Seller)

↑

Transferor Co.

liquidated/ Dissolved

PC = para 3(g) of AS-14

Assets & liabilities

Transferee Co.

↓

(Buyer)

* Explaintion of para 3(g) of AS-14

→ The aggregate of shares, and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholder of the transferor company

क्या दिया है, उससे फर्क नहीं पड़ता है किसको दिया है उस से फर्क पड़ता है।

Methods adopted for computation of purchase Consideration

[A] Lumpsum / fixed payment method

→ under this method purchase consideration is agreed upon in totality without attaching individual valuation to assets or liabilities taken over. It is a total value of the Business take over.

[B] Net payments Method

→ under this methods the transferee company makes individual payments to the equity Shareholders and preference Shareholder either by way of cash, issue of Shares and debentures.

[C] Net Assets method

→ under this method the purchase consideration is determined by calculating the NET ASSETS / NETWORTH of the transferor company. The Consideration is arrived at by adding the value of Assets taken over (at Agreed Value or Book Value) minus value of liabilities taken over (at Agreed Value or Book value) by the transferee Company (outside liabilities Excluding Share capital and reserves and Surplus).

* purchase consideration = Assets taken over at an agreed value xxx

(-) liabilities taken over at an agreed value (xxx)

[D] Intrinsic Value / Share Exchange method

→ The word intrinsic means inherent under this method the transferee company determines the purchase consideration payable to the transferor company on the basis of intrinsic value of their share by calculating total number of share to be issued on the basis of share exchange ratio.

Note:- Consideration for equity shareholder may be agreed upon the basis of book value or intrinsic value or agreed value per share.

$$\text{Book value per Eq. Share} \Rightarrow \frac{\text{Net Assets} - \text{Sum due to preference Shareholders}}{\text{total number of Equity Shares}}$$

Or

$$\frac{\text{Eq. Share Capital} + \text{Reserves \& Surplus} - \text{Miss Exp.}}{\text{total number of Eq. Share}}$$

Intrinsic Value per Share -

$$= \frac{\text{Market value of Net Assets} - \text{Sum due to pref Sharehold}}{\text{Total number of Eq. Shares}}$$

1:38:00
L-21

5 Conditions of AS-14

> To decide wearther it is amalgamation in the nature of merger or purchases.

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

• Explaination - If transferee Co. becomes selective while taken over assets and liabilities of transferor Co., it will become amalgamation in the nature of ~~merger~~ purchase

ii) Shareholder holding not less then 90% of face value of equity shares of transferor Co. agrees to become shareholder of transferee Co., Except, the share held by transferee Co. itself or though its nominees or though its subsidiaries.

• Explaination - AS-14 requires consent of independand shareholder i.e, those who are directly or indirectly not related to transferor Co.

• If less than 90% shareholder agrees for amalgation it become amalgamation in the nature purchase.

iii) The transferee co. discharges entire PC to the shareholders of transferor Co. only by way of issue of Equity Shares (of transferee Co.) Except the fractional part that can be paid in cash.

Explaination - The transferee Co. should issue only and only Equity Share to transferor Co. because by giving Equity Share transfree Co. shares ownership to the shareholder of transferor Co. and also entitles them for voting rights.

If PC includes preferance shares or debentures or cash (Except for fractional part) then it will be become amalgamation in the nature of purchase.

Example:-

Inrinsic value/ES of transferor Co. Rs 150/ES

Intrinsic value/ES of transferee Co. Rs 60/ES

- This means that transferee Co will give 2.5 ES for (150/60) for every 1 ES of transfor Co. but they cannot issue shares in fraction i,e 0.5. Hence, for 0.5 Share, they will pay Cash ₹30 (60×0.5).

1 ES of transferor Co. = 2 ES of transferee Co.
+
30 Rs in cash

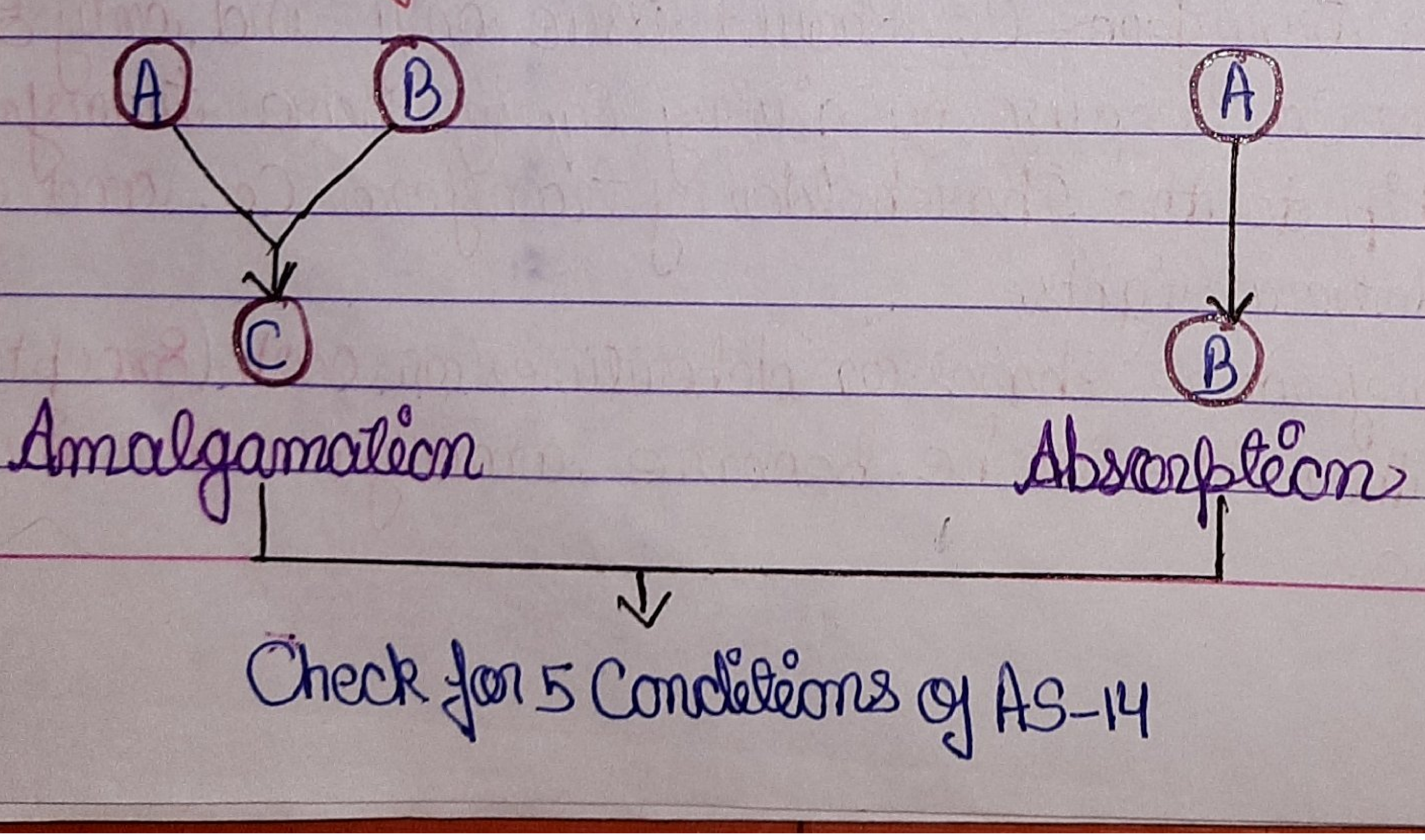
iv) The transferee Co. intends to continue the same line of business which transferor Co. was doing before amalgamation.

- Explaination - कोई प्यार करे तो तुमसे करे, तुम जैसे हो वैसे करे
कोई तुम्हे बदलके प्यार करे, तो वोह प्यार नहीं सौदा करे

प्यार → merger
सौदा → purchase

v) All the assets and liabilities of transferor Co. are taken over by transferee Co. at its book values, Expect for uniformity of accounting policies

- Explaination - If transferee Co. re-assesses the value of any assets or liabilities of transfor Co. then it will be become amalgamation in the nature of purchase



All 5 conditions satisfied	Any of the 5 conditions not satisfied
↓	↓
Amalgamation in the nature of merger	Amalgamation in the nature of purchase
↓	↓
Objective is to grow business	objective is investment
↓	↓
Accounting method pooling of interest method	Accounting method purchase method

Different between :-

Pooling of Interest method	Purchase method
1) This method of Accounting is followed in case of amalgamation in the nature of merger.	1) This method of Accounting is followed in case of amalgamation in the natur of purchase
2) transfree Co. takes over all the A&L at its Book values	2) transferee Co. may/may not take over all A&L, either at Book value or re-assessed.
3) NATO = Assets - liab. - reserves	3) NATO = Assets - liabilities
4) transfree Co. takes overall the reserves of transferor Co.	4) transferee Co. do not take any reserves of transfor Co. (Except statutory reserves)
5) Journal Entry for statutory reserve NO - J.E	5) Journal Entry for statutory reserve :- Amalgamation Adj A/C Dr To Stat. reserve A/C
6) PC > NATO = Dr to Reserves A/C PC < NATO = Cr to reserves A/c	6) PC > NATO = Dr to ~~Capital res.~~ goodwill A/c PC < NATO = Cr to capital res.
7) liq. Exp. (of transferor Co.) = Dr. to reserve A/c	7) liq Exp (of transferor Co.) Dr to Goodwill / C.R A/c

(Net Assets taken over)

PC = NATO — No Extra amount paid (No Gain / loss)

Transfree Co. Ne Kya diya hai > transfree Co. Ko Kya mila hai — Extra amount paid Dr. to Goodwill A/c (It is a loss / Exp)

Transfree Co. Ne Kya diya hai < transfree Co. Ko Kya mila hai — less Amount paid Cr. to Cap. Res. A/c (It is Gain)

NATO = A - L - R
↓
Amalgamation in the nature of merger
↓
PC > NATO = Dr. to $\boxed{\text{Reseves A/c}}$
PC ≯ NATO = Cr. to $\boxed{\text{Reserves A/c}}$
↓
Revenue receipts In the ordinary course of Business

NATO = A - L
↓
Amalgamation in the nature of purchase
↓
PC > NATO = Dr. to Goodwill A/c
PC < NATO = Cr. to Capital Res A/c

Important point for Calculating purchase Consideration

1. while calculating P.C we require Swap ratio, if Swap ratio is not given we will calculate it by applying the following formula. (eg-4)

$$\text{Swap ratio}^{*} = \frac{\text{Value of old Co. Share}}{\text{Value of new Co. Share}}$$

* Value means → market value
2) Intrinsic Value
3) Paid up value

} order of Preference Same

→ Per Share value for Equity Shareholders assuming that Co. liquidates today

Assets taken over at an agreed value	xxx
(-) liabilities taken over at an agreed value	(xxx)
(-) Preference Share Capital	(xxx)
Balance available for Equity Shareholder	xxx
÷ No. of Equity Share	xxx
Intrinsic Value	xxx

② If question is silent about issue price then -
(a) uses intrinsic value (only if already calculated while calculatin Swap value ratio) i.e do not calculate intrinsic value specially for the purpose of issue price
(b) paid up value or face value

③ When both Swap ratio and intrinsic value are given then we have to calculate -

$$\text{Cash per Share} = \frac{\text{Share Surrendered} \times \text{Value of old Co.} - \text{Shares obtained} \times \text{Value of new Co}}{\text{Share Surrendered}}$$

* Cash per share x number of share of old Co.
* Cash per share is (-)ve then ignore

④ If Question says that Calculate cash per share then -
i. Step 1 → Calculate I.V of both Companies
ii. Step 2 → Calculate Cash per share using point 3

ALWAYS START WITH BELOW EXAMPLES

Eg 1 → X ltd took over Y Ltd and pays
(a) 3 share of X ltd for every 5 shares of Y ltd @ 12 per share
(b) Rs 2 per share in cash
Y ltd has 1,00,000 equity shares.

Sol :-

X Ltd $\xrightarrow{\text{absorption}}$ Y Ltd

New Co.   old Co.

Payment to	Payment in	Workings	Amount
ESH of Y Ltd	Share	60,000 x 12 → issue price (100,000 x 3/5) old co share ← swap ratio	7,20,000
"	Cash	(100,000 x 2)	200,000
		Purchase Consideration	9,20,000

Eg-2 ⇒ A ltd took over B. ltd and pays-
(a) 3 Eq. Share for Every 4 preferance Share of B ltd @ 13 each
(b) 4 preferance for every 5 Equity Share of B ltd @ Rs 17 each
(c) Rs 3 per Share in cash
B ltd has 100,000 equity Shares and 50,000 preferance Shares

Sol

Calculate Purchase Consideration

Payment to	Payment in	Working	Amount
PSH of B Ltd	Equity Share	50,000 x 3/4 x 15 each	562500
ESH of B ltd	preferance Share	60,000 x 17 (100,000 x 4/5 x 17 each	10,20,000
Per Share of B ltd	Cash	1,50,000 x 3	4,50,000
		Purchase Consideration	23,72,500

* further Example are in the practice Copy

Accounting Entries → In the Book of transferee (New) Company

(New Co.) Journal Entries (Purchase Method)

Particular	Accounting Entries
1. On the date of agreement (Purchase of business)	Business purchase A/C Dr XXX (P.C) To liquidator of old Co. A/C XXX
2. On effective date (Recording of assets and liabilities)	Sundry Assets A/C Dr XXX (agreed val) Goodwill A/C (Bala) Dr XXX To Sundry liabilities A/C XXX (agre) To Business purchase A/C XXX (P.C) To Capital reserve A/C (Bala) XXX
3. On payment date (Discharge of purchase Consideration)	Liquidator of old Co A/C Dr XXX P.C To Eq. Share Capital A/C XXX (F.V) To % Pref. Share Capital A/C XXX (F.V) To Securities premium A/C XXX (any) To Cash A/C XXX (any) To % Debenture A/C XXX (F.V)
4. For cancellation of Contra item	Trade payable A/C Dr XXX To trade receivable A/C XXX
5. For payment of Expenses of old Companies (liquidation Exp)	Goodwill A/C Dr XXX To Cash/Bank A/C XXX
6. For payment of liabilities	liabilities A/C Dr XXX To Cash A/C XXX To New liabilities A/C XXX

7. For Creation of Statutory reserves (even if ques. is silent)	Amalgamation Adjustment A/c Dr xxx → Reserve To Statutory reserve A/c xxx
8. For Cancellation of profit (unrealised on Stock)	
(a) upstream (old co ने New co. को बेचा था)	Goodwill A/c Dr xxx To Stock reserve A/c xxx
(b) Downstream (New ने old co. को बेचा था)	Profit & loss A/c Dr xxx To Stock reserve A/c xxx We are reducing the value of Stock
9. For any other information in Questions	Pass journal Entry as required

Transferee (New Company)

Journal Entries (Pooling of interest method)

Particular	Accounting Entries
1. Purchase of business	Business purchase A/c Dr xxx (P.C) To liquidator of old Co. A/c xxx (P.C)
2. Recording of assets and liabilities	Sundry Assets A/c Dr xxx (B.V) Reserve (may be revenue or Cap) A/c xxx Bal To Sundry liabilities A/c xxx (B.V) To Business purchase A/c xxx (P.C) To General reserve A/c xxx (Bal) To all reserve A/c xxx
3. Discharge of Purchase consideration	liquidator of old Co A/c Dr xxx To Eq. Share Capital A/c xxx To % pref. Share capital A/c xxx To cash A/c (fractional share) A/c xxx
4. Cancellation of Contra item	Trade payables A/c Dr xxx To Trade receivable A/c xxx

5. Payment of Expenses of old Co.	General reserve A/C Dr xxx To Cash A/C xxx
6. Creation of Statutory reserve	No Entry
7. Cancellation of unrea-lised profit on Stock	General reserve Dr xxx To Stock reserve A/C xxx
8. Any other Specific point as per Ques.	Pass J.E as required

∵ If all 5 condition are Satisfied

→ In the Books of Transferor (old) Companies

* Atleast 2 Sincere readings before jumping on Question.

→ Whenever old company is Amalgamated with new company follow the steps only.

1. Step 1:- Transfer all assets and liabilities at book value to the respective account
   - → ESC, Profit, reserves, fictitious assets are transfer to Equity Shareholder of A/C
   - → PSC is transferd to PSH A/C
   - → Cash (if not taken over) is transfered to Cash A/C
   - → Cash (if taken over) is transfer to realisation A/C
   - → All other item is transfered to Realisation.

2. Step 2:- Raise purchase Consideration

New Co. (transferee Co.) A/C Dr xxx
To Realisation A/C xxx] → (P.C)

3. Step 3:- Pay realisation Expenses → Realisation A/C Dr xxx
to Cash / Bank A/C xxx

* If new Company reimbursed (pay) these Expenses:-
Cash / Bank A/C Dr xxx
to realisation A/C xxx

4. Step 4:- Realise (Pay) purchase Consideration
Cash / Bank A/C Dr xxx
Eq. Share in new Co. A/C Dr xxx
Pref. Share in new Co. A/C Dr xxx
other Assets A/C Dr xxx
to transferee (New) Co. A/C xxx → P.C

5. Step 5:- Distribute purchase Consideration
Eq. Shareholder A/C Dr xxx
Pref. Shareholder A/C Dr xxx
to Eq. Shares of New Co. A/C xxx
to pref Shares of New Co. A/C xxx
to Cash A/C xxx

6. Step 6:- Realise assets and pay off liabilities (Not taken over)

(a) Assets realise
Cash / Bank A/C Dr xxx
to realisation A/C xxx
* If question is silent then assets is sold for Nil

(b) liabilities pay
Realisation A/C Dr xxx
to Cash & Bank A/C xxx
* If question is silent then liabilities is paid at Book Value

7. Step 7:- Closing of Accounts
→ The difference in PSH A/C is transferred to realisation A/C
→ The balance of realisation A/C is transfered to ESH A/C
→ Cash A/C
- Positive balance is transfer to ESH A/C
- Negative balance is transfer to Realisation A/C

* ESH A/C will tally