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FOR

CA INTERMEDIATE

2024

MARATHON / ONE SHOT / SUPER REVISION

Advanced Accounting PART 1

By – Nitin Goel

CA INTER MARATHON (SUPER REVISION/ONE SHOT)	
ADVANCED ACCOUNTING	
S.NO.	CHAPTER NAME
1	Financial Statement of Companies
2	Cash Flow Statement (AS 3)
3	BuyBack of Securities
4	Internal Reconstruction
5	Amalgamation (incl. AS 14)
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CA INTERMEDIATE

2024

Financial Statement of Companies

Advanced Accounting | Lecture - 01

By – Nitin Goel

FINANCIAL STATEMENTS OF COMPANIES

"Stop being afraid of what could go wrong and focus on what could go right"

MAINTENANCE OF BOOKS OF ACCOUNTS

Every company shall prepare book on *accrual basis* and according to the *double entry system* of accounting.

PREPARATION OF FINANCIAL STATEMENTS

The Board of Directors of the company shall lay *financial statements* at every annual general meeting of a company which include:

a) Balance Sheet as at the end of the period, and
b) Profit and Loss Account for that period.
[Note: For a Company not carrying on business for profit, an Income and Expenditure Account shall be laid at that AGM, instead of the P & L Account.]
c) Cash flow statement for the financial year
d) Statement of changes in equity, if applicable; and
e) Any explanatory note annexed to, or forming part of, any document referred above

Provisions Applicable

(1) Specific Act is Applicable

For instance any

a) Insurance company
b) Banking company or
c) Any company engaged in generation or supply of electricity or
d) Any other class of company for which a Form of balance sheet or Profit and loss account has been prescribed under the Act governing such class of company

(2) In case of all other companies

Balance Sheet as per Form set out in Part I of Schedule III and Statement of Profit and Loss as per Part II of Schedule III

Division	Applicable to
Division I	Companies that are required to apply Accounting Standards notified under Section 133 of the Companies Act, 2013.
Division II	Companies that are required to apply Indian Accounting Standards notified under Section 133 of the Companies Act, 2013.
Division III	Non-Banking Finance Companies (NBFCs) that are required to apply Indian Accounting Standards notified under Section 133 of the Companies Act, 2013.

Depending upon the Total Income of the company, the figures appearing in the Financial Statements shall be rounded off as given below:

Total Income	Rounding Off
(a) Less than 100 crore rupees	To the nearest hundreds, thousands, lakhs or millions, or decimals thereof
(b) 100 crore rupees or more	To the nearest lakhs, millions or crores, or decimals thereof.

Schedule III of the Companies Act, 2013

PART I – BALANCE SHEET

Name of the Company……………………
Balance Sheet as at ………………………

	PARTICULARS	Note No.	Figures as at the end of current Reporting period	Figures as at the end of previous reporting period
A.	EQUITY AND LIABILITIES			
1.	Shareholder's funds		(Calledup - call in Arr.)	
a	Share capital (Authorised, Issued & Subsc)		Paid up capital	Other than cash, Bonus shares, Buyback
b	Reserves and surplus		Sec. Prem., CRR, Gen. Res., P&L / Surplus	
c	Money received against share warrants			
2.	Share application money pending allotment			
3.	Non-Current Liabilities			
a	Long-term borrowings		Debentures, Bonds, Loans, Public deposits	(Sec. & unsecured)
b	Deferred tax liabilities (Net)			
c	Other long term liabilities			
d	Long-term provisions		Prov. for Gratuity	
4.	Current Liabilities			
a	Short-term borrowings		Current maturities of LTB, Short term loan, Bank overdraft	
b	Trade payables		Creditors, Bills Payable	
c	Other current liabilities		O/s Expenses, Calls in Advance, Dividend Payable	
d	Short-term provisions		Provision for Tax	
	TOTAL			
B.	ASSETS			
1.	Non-Current Assets			
a	Property, Plant & Equipment & Intangible Assets			
i.	Property, Plant & Equipment		Plant & Mach., Furniture, Office Equipment, Land & Building	
ii.	Intangible assets		Patent, Copyright, Trademark, Software, Goodwill	
iii.	Capital work-in-Progress		Building under construction	
iv.	Intangible assets under development			
b	Non-current investments			
c	Deferred tax assets (net)			
d	Long-term loans and advances		Loan to 3rd Party (Long Period)	
e	Other non-current assets		Security Deposits	
2.	Current Assets			
a	Current investments			
b	Inventories	Mftr: R/M, WIP, Finished Goods; Trader: Stock in Trade		Loose Tools, Stock of Consumables
c	Trade receivables		B/R, Debtors Less: Prov. for Doubtful debts	
d	Cash and cash equivalents		Cash, Bank, Deposits (upto 1 year)	
e	Short-term loans and advances		Loan to staff, 3rd Party, Advance tax	
f	Other current assets		Accrued Interest	
	TOTAL			

Important Disclosures in Notes to Accounts

1) Share Capital: For each class of share capital (different classes of preference shares to be treated separately):
   a) the number and amount of shares authorised;
   b) the number of shares issued, subscribed & fully paid, and subscribed but not fully paid;
   c) par value per share;
   d) a reconciliation of the number of shares o/s at the beginning & at the end of the period;
   e) for the period of 5 years immediately preceding the date as at which the Balance Sheet is prepared:
      - Aggregate number & class of shares allotted as fully paid-up pursuant to contract(s) without payment being received in cash.
      - Aggregate number & class of shares allotted as fully paidup by way of bonus shares
      - Aggregate number and class of shares bought back.
   f) List of Shareholders holding more than 5% shares
   g) Shareholding of Promoter's

Shares held by Promoter at the end of the year				% change during the year
S.No.	Promoter Name	No. of Shares	% of total Shares	
Total				

2) Reserves and Surplus: Debit balance of statement of profit and loss shall be shown as negative figure under the head "Surplus". Similarly, balance of "Reserves & 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.

3) Current maturities of Long term borrowings shall be disclosed separately under Short term borrowings & not under Other Current Liabilities

4) Trade Payables ageing Schedule:

Particulars	O/s for following periods from due date of payment				
	Less than 1 year	1-2 years	2-3 years	More than 3 years	Total
MSME					
Others					
Disputed dues-MSME					
Disputed dues-Others					

5) Trade Receivables ageing Schedule:

Particulars	O/s for following periods from due date of payment					
	Less than 6 months	6 months – 1 year	1-2 years	2-3 years	More than 3 years	Total
Undisputed -considered good						
Undisputed -considered doubtful						
Disputed - considered good						
Disputed - considered doubtful						

PART II – STATEMENT OF PROFIT AND LOSS

Name of the Company……………………

Profit and loss statement for the year ended ……………………

	PARTICULARS	Note No.	Figures for the current Reporting period	Figures for the previous reporting period
I.	Revenue from operations (Principal Revenue Gen. Act & Ancilliary) Sale of Goods, services			
II.	Other income Interest, Dividend, Rental Income, Profit on sale of assets			
III.	Total Income (I + II)			
IV.	Expenses:			
	Cost of materials consumed (Mfr.) Raw Material: op. stock + Purchases - clos. stock			
	Purchases of Stock-in-Trade (Trader) Purchases net of Returns			
	Changes in inventories of finished goods, work-in-progress and Stock-in-Trade Opening stock - closing stock			
	Employee benefits expense			
	Finance costs Int. on Loan, Deb., Loan Processing fees, etc.			
	Depreciation and amortization expense Dep on PPE & Amortisation of Intangible Ast			
	Other expenses Rent, carriage, Advertising, Preliminary Exp., Bad debts, Auditor fees, Bank charges, Director fees, Commission, PDD, Loss on sale of Assets.			
	Total Expenses			
V.	Profit before exceptional and extraordinary items and tax (III-IV)			
VI.	Exceptional items Eg: Litigation settlement, Retrospective Law			
VII.	Profit before extraordinary items & tax (V - VI)			
VIII.	Extraordinary Items Loss by Earthquake, flood, fire ; Insurance claim			
IX.	Profit before tax (VII- VIII)			
X	Tax expense:			
	(1) Current tax			
	(2) Deferred tax			
XI.	Profit (Loss) for the period from continuing operations (VII-VIII)			
XII.	Profit/(loss) from discontinuing operations			
XIII.	Tax expense of discontinuing operations			
XIV.	Profit/(loss) from Discontinuing operations (after tax) (XII-XIII)			
XV	Profit (Loss) for the period (XI + XIV)			
XVI.	Earnings per equity share:			
	(1) Basic			
	(2) Diluted			

Additional Information:

A Company shall disclose by way of notes additional information regarding aggregate expenditure and income on the following items:

(a) Employee Benefits Expense [showing separately
   - (i) salaries and wages,
   - (ii) contribution to provident and other funds,
   - (iii) expense on Employee Stock Option Scheme (ESOP) and Employee Stock Purchase Plan (ESPP),
   - (iv) staff welfare expenses].

(b) Any item of income or expenditure which exceeds 1% of the revenue from operations or ₹ 1,00,000, whichever is higher;

(c) 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;

(d) In case of companies covered u/s 135, amount of expenditure incurred on corporate social responsibility activities.

Other Disclosures:

1) Corporate Social Responsibility (CSR):

Where the company covered under section 135 of the companies act, the following shall be disclosed with regard to CSR activities.

(a) amount required to be spent by the company during the year,
(b) amount of expenditure incurred,
(c) shortfall at the end of the year,
(d) total of previous years shortfall,
(e) reason for shortfall,
(f) nature of CSR activities,
(g) details of related party transactions, e.g., contribution to a trust controlled by the company in relation to CSR expenditure as per relevant Accounting Standard,
(h) where provision is made with respect to liability incurred by entering into a contractual obligation, movements in provision during year should be shown separately

2) Details of Crypto Currency or Virtual Currency

Where the Company has traded or invested in Crypto currency or Virtual Currency during the financial year, the following shall be disclosed:

a) profit or loss on transactions involving Crypto currency or Virtual Currency.
b) amount of currency held as at the reporting date,
c) deposits or advances from any person for the purpose of trading or investing in Crypto Currency/ virtual currency.

3) Details as wilful defaulter (where company declared wilful defaulter by bank or financial institution , details to be given like: date, amount & nature of defaults)

4) Relationship with struck off companies

CONTINGENT LIABILITIES and COMMITMENTS (to the extent not provided for)

a. Claims against the company not acknowledged as debt
b. Guarantees
c. Arrears of fixed cumulative dividends on preference shares
d. Estimated amount of contracts remaining to be executed on capital account & not provided
e. Uncalled liability on shares and other investments partly paid
f. Bills discounted not yet matured
g. Other money for which the company is contingently liable & other commitments.

Question 1 *(ICAI Study Material) / (RTP May 2023) (Similar)* *Pg no._____*

From the following particulars furnished by Pioneer Ltd., prepare the Balance Sheet as at 31st March, 2022 as required by Schedule III of the Companies Act. Give notes at the foot of the Balance Sheet as may be found necessary –

	Dr. (₹)	Cr. (₹)
Equity Capital (Face value of ₹ 100)		10,00,000
Calls in Arrears	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	
Dividend Payable		60,000
Profit and Loss Account		86,700
Cash Balance	30,000	
Cash at Bank	2,47,000	
Loans (Unsecured)		1,21,000
Sundry Creditors (For Goods and Expenses)		2,00,000
	18,95,700	18,95,700

The following additional information is also provided:

(1) 2,000 equity shares were issued for consideration other than cash.

(2) Debtors of ₹ 52,000 are due for more than six months.

(3) The cost of assets:

- a. Building ₹ 4,00,000
- b. Plant and Machinery ₹ 7,00,000
- c. Furniture ₹ 62,500

(4) The balance of ₹ 1,50,000 in the loan account with State Finance Corporation is inclusive of ₹ 7,500 for interest accrued but not due. The loan is secured by hypothecation of Plant and Machinery.

(5) Balance at Bank includes ₹ 2,000 with Perfect Bank Ltd., which is not a Scheduled Bank.

(6) Bills receivable for ₹ 2,75,000 maturing on 30th June, 2022 have been discounted.

(7) The company had contract for the erection of machinery at ₹ 1,50,000 which is still incomplete.

Solution

Pioneer Ltd.
Balance Sheet as on 31st March, 2022

	Particulars	Note	₹
	Equity and Liabilities		
1.	Shareholders' funds		
	(a) Share capital	1	9,99,000
	(b) Reserves and Surplus	2	2,96,700
2.	Non-Current liabilities		
	(a) Long-term borrowings	3	2,63,500
3.	Current liabilities		
	(a) Trade Payables		2,00,000
	(b) Other current liabilities	4	67,500
	(c) Short-term provisions	5	68,000
	Total		**18,94,700**
	Assets		
1.	Non-current assets		
	(a) Property, Plant & Equipment & Intangible Assets		
	Property, Plant & Equipment	6	11,25,000
2.	Current assets		
	(a) Inventories	7	2,50,000
	(b) Trade receivables	8	2,00,000
	(c) Cash and cash equivalents	9	2,77,000
	(d) Short-term loans and advances		42,700
	Total		**18,94,700**

Notes to accounts

			₹
1.	**Share Capital**		
	Equity share capital		
	Issued & subscribed & called up		
	10,000 Equity Shares of ₹100 each (Of the above 2,000 shares have been issued for consideration other than cash)	10,00,000	
	Less: Calls in arrears	(1,000)	9,99,000
	Total		**9,99,000**
2.	**Reserves and Surplus**		
	General Reserve		2,10,000
	Surplus (Profit & Loss A/c)		86,700
	Total		**2,96,700**
3.	**Long-term borrowings**		
	Secured		
	Term Loans		
	Loan from State Financial Corporation (1,50,000-7,500) (Secured by hypothecation of Plant and Machinery)		1,42,500
	Unsecured		1,21,000
	Total		**2,63,500**
4.	**Other current liabilities**		
	Interest accrued but not due on loans (SFC)		7,500
	Dividend Payable		60,000
	Total		**67,500**

5.	**Short-term provisions**		
	Provision for taxation		68,000
	Total		**68,000**
6.	**Property, Plant & Equipment**		
	Land		2,00,000
	Buildings	4,00,000	
	Less: Depreciation	(50,000)	3,50,000
	Plant & Machinery	7,00,000	
	Less: Depreciation	(1,75,000)	5,25,000
	Furniture & Fittings	62,500	
	Less: Depreciation	(12,500)	50,000
	Total		**11,25,000**
7.	**Inventories**		
	Raw Material		50,000
	Finished goods		2,00,000
	Total		**2,50,000**
8.	**Trade receivables**		
	Debtors Outstanding for period exceeding 6 months		52,000
	Other Debts		1,48,000
	Total		**2,00,000**
9.	**Cash and cash equivalents**		
	Cash at bank		
	with Scheduled Banks	2,45,000	
	with others (Perfect Bank Ltd.)	2,000	2,47,000
	Cash in hand		30,000
	Total		**2,77,000**

Notes:
There is a contingent liability for bills discounted but not yet matured amounting ₹ 2,75,000.
Estimated amount of contract remaining to be executed on capital account & not provided for 1,50,000*
*It has been assumed that the company had given this contract for purchase of machinery.

Question 2 *(Inter July 2021) (20 Marks)* *Pg no._____*

The following is the Trial Balance of H Ltd., as on 31st March, 2021:

	Dr.	Cr.
Equity Capital (Shares of ₹ 100 each)		8,05,000
5,000, 6% preference shares of ₹ 100 each		5,00,000
9% Debentures		4,00,000
General Reserve		40,00,000
Profit & Loss A/c (of previous year)		72,000
Sales		60,00,000
Trade Payables		10,40,000
Provision for Depreciation on Plant & Machinery		1,72,000
Suspense Account		40,000
Land at cost	24,00,000	
Plant & Machinery at cost	7,70,000	
Trade Receivables	19,60,000	
Inventories (31-03-2021)	9,50,000	
Bank	2,30,900	
Adjusted Purchases	22,32,100	
Factory Expenses	15,00,000	
Administration Expenses	3,00,000	
Selling Expenses	14,00,000	
Debenture Interest	36,000	
Goodwill	12,50,000	
	1,30,29,000	1,30,29,000

Additional Information:

(i) The authorised share capital of the company is :
5,000, 6% preference shares of ₹ 100 each 5,00,000
10,000, equity shares of ₹ 100 each 10,00,000
Issued equity capital as on 1st April 2020 stood at ₹ 7,20,000, that is 6,000 shares fully paid and 2,000 shares ₹ 60 paid. Directors made call of ₹ 40 per share on 1st October 2020. A shareholder could not pay the call on 100 shares and his shares were then forfeited and reissued @ ₹ 90 per share as fully paid.

(ii) On 31st March 2021, the Directors declared a dividend of 5% on equity shares, transferring any amount that may be required from General Reserve. Ignore Taxation.

(iii) The company on the advice of independent valuer wishes to revalue land at ₹ 36,00,000.

(iv) Suspense account of ₹ 40,000 represents amount received for the sale of some of the machinery on 1-4-2020. The cost of the machinery was ₹ 1,00,000 and the accumulated depreciation thereon being ₹ 30,000

(v) Depreciation is to be provided on plant and machinery at 10% on cost.

(vi) Amortize 1/5th of Goodwill.

You are required to prepare H Limited's Balance Sheet as on 31-3-2021 and Statement of Profit and Loss with notes to accounts for the year ended 31-3-2021 as per Schedule III of the Companies Act, 2013. Ignore previous years' figures & taxation.

Solution

H Ltd
Balance Sheet as at 31st March 2021

Particulars	Note No.	Amount in (₹)
Equity and Liabilities		
I. Shareholders' Funds		
a. Share Capital	1	13,00,000
b. Reserves and Surplus	2	53,91,900
II. Non-Current Liabilities		
a. Long Term Borrowings	3	4,00,000
III. Current Liabilities		
a. Trade Payables	4	10,40,000
b. Other Current Liabilities	5	70,000
Total		**82,01,900**
Assets		
I. Non-Current Assets		
(i) PPE & Intangible Assets		
a. Property, Plant and Equipment	6	40,61,000
b. Intangible Assets	7	10,00,000
II. Current Assets		
a. Inventories		9,50,000
b. Trade Receivables		19,60,000
c. Cash and Cash equivalents		2,30,900
Total		**82,01,900**

Statement of Profit and Loss for the year ended 31st March 2021

Particulars	Note No	Amount in (₹)
I. Revenue from operations		60,00,000
Total Income		**60,00,000**
II. Expenses		
Purchases (adjusted)		22,32,100
Finance Costs	8	36,000
Depreciation and Amortization	9	3,17,000
Other Expenses	10	32,30,000
Total Expenses		**58,15,100**
Profit/(Loss) for the period		**1,84,900**

Notes to Accounts **(Amount in ₹)**

1	**Share Capital**		
	Authorized Capital		
	5,000, 6% Preference shares of ₹ 100/- each		5,00,000
	10,000 Equity Shares of ₹100/- each		10,00,000
			15,00,000
	Issued & Subscribed Capital		
	5,000, 6% Preference shares of ₹100/- each		5,00,000
	8,000, Equity shares of ₹100/- each		8,00,000
	Total		**13,00,000**
2	**Reserves & Surplus**		
	Capital Reserve (100 X (90-40))		5,000
	Revaluation Reserve (36,00,000-24,00,000)		12,00,000

	General Reserve		40,00,000
	Surplus	1,84,900	
	Add: Balance from previous year	72,000	
	Less: Dividends declared	(70,000)	
	Profit/(Loss) carried forward to Balance Sheet		1,86,900
	Total		**53,91,900**
3	**Long-Term Borrowings**		
	Secured		
	9% Debentures		4,00,000
4	Trade Payables		10,40,000
5	**Other Current Liabilities**		
	Dividend Payable		
	Preference Dividend		30,000
	Equity Dividend		40,000
	Total		**70,000**
6	**Property, Plant and Equipment**		
	Land		
	Opening balance	24,00,000	
	Add: Revaluation Adjustment	12,00,000	
	Closing Balance		36,00,000
	Plant and Machinery		
	Opening Balance	7,70,000	
	Less: Disposed off	(1,00,000)	
	Depreciation	(2,09,000)	
	Closing Balance		4,61,000
	Total		**40,61,000**
7	**Intangible Assets**		
	Goodwill		12,50,000
	Less: Amortized (1/5th)		(2,50,000)
	Total		**10,00,000**
8	**Finance Costs**		
	Debenture Interest		36,000
9	Depreciation and Amortization		
	Plant and Machinery		67,000
	Goodwill		2,50,000
	Total		**3,17,000**
10	**Other Expenses**		
	Factory Expenses		15,00,000
	Selling Expenses		14,00,000
	Administrative Expenses		3,00,000
	Loss on sale of Plant and Machinery		
	Book Value (1,00,000-30,000) 70,000		
	Less: Sale Value (40,000)		30,000
	Total		**32,30,000**

Question 3 - *(Inter Nov 2022) (20 Marks)* Pg no.______

The following is the Trial Balance of Anmol Limited as on 31st March, 2022:

Debit Balance	Amount(₹)	Credit Balances	Amount(₹)
Purchases	82,95,000	Sales	1,25,87,000
Wages and Salaries	12,72,000	Commission	72,500
Rent	2,20,000	Equity Share Capital	10,00,000
Rates and Taxes	50,000	General Reserve	10,00,000
Selling & Distribution Expenses	4,36,000	Surplus (P&L A/c) 01.04.2021	8,75,500
Directors Fees	32,000	Securities Premium	2,50,000
Bad Debts	38,500	Term Loan from Public Sector Bank	1,02,00,000
Interest on Term Loan	8,05,000	Trade Payables	55,08,875
Land	24,00,000	Provision for Depreciation:	
Factory Building	36,80,000	On Plant & Machinery	9,37,500
Plant and Machinery	62,50,000	On Furniture and Fittings	82,500
Furniture and Fittings	8,25,000	On Factory Building	1,84,000
Trade Receivables	64,75,000	Provision for Doubtful Debts	25,000
Advance Income Tax Paid	37,500	Bills Payable	1,25,000
Stock (1st April,2021)	9,25,000		
Bank Balances	9,75,000		
Cash on Hand	1,31,875		
Total	3,28,47,875	Total	3,28,47,875

Following information is provided:

1. The Authorized Share Capital of the Company is 2,00,000 Equity Shares of ₹ 10 each. The Company has issued 1,00,000 Equity Shares of ₹ 10 each.
2. Rent of ₹ 20,000 and Wages of ₹ 1,56,500 are outstanding as on 31st March, 2022.
3. Provide Depreciation @ 10% per annum on Plant and Machinery, 10% on Furniture and Fittings and 5% on Factory Building on written down value basis.
4. Closing Stock as on 31st March, 2022 is ₹ 11,37,500.
5. Make a provision for Doubtful Debt @ 5% on Debtors.
6. Make a provision of 25% for Corporate Income Tax.
7. Transfer ₹ 1,00,000 to General Reserve.
8. Term Loan from Public Sector Bank is secured against Hypothecation of Plant and Machinery. Installment of Term Loan falling due within one year is ₹ 17,00,000.
9. Trade Receivables of ₹ 85,600 are outstanding for more than six months.
10. The Board declared a dividend @10% on Paid up Share Capital on 5th April, 2022.

You are required to prepare Balance Sheet as on 31st March 2022 and Statement of Profit and Loss with Note to Accounts for the year ending 31st March, 2022 as per Schedule III of the Companies Act, 2013. Ignore previous years' figures.

Solution

Balance Sheet of Anmol Ltd. as at 31st March, 2022

Particulars	Note No	₹
Equity and Liabilities		
1. Shareholders' funds		
a. Share capital	1	10,00,000
b. Reserves and Surplus	2	24,76,462
2. Non-current liabilities		
a. Long-term borrowings	3	85,00,000
3 Current liabilities		
a. Short term borrowings (Installment of term loan falling due in one year)		17,00,000
b. Trade Payables	4	56,33,875
c. Other current liabilities	5	1,76,500
d. Short term provisions (provision for tax)		1,16,988
Total		**1,96,03,825**
ASSETS		
1. Non-current assets		
a. PPE	6	1,11,70,700
2. Current assets		
a. Inventories		11,37,500
b. Trade receivables	7	61,51,250
c. Cash and bank balances	8	11,06,875
d. Short term loans & advances (Advance tax paid)		37,500
Total		**1,96,03,825**

Statement of Profit and Loss of Anmol Ltd. for the year ended 31st March, 2022

	Particulars	Notes	Amount
I.	Revenue from operations		1,25,87,000
II.	Other income (Commission income)		72,500
III.	Total Income (I + II)		**1,26,59,500**
IV.	Expenses:		
	Purchases of Inventory-in-Trade		82,95,000
	Changes in inventories of finished goods work-in-progress and Inventory-in-Trade	9	(2,12,500)
	Employee benefits expense	10	14,28,500
	Finance costs (interest on term loan)		8,05,000
	Depreciation		7,80,300
	Other operating expenses	11	10,95,250
	Total expenses		**1,21,91,550**
V.	Profit (Loss) for the period (III - IV)		4,67,950
VI.	(-) Tax (25%)		(1,16,988)
VII.	PAT		3,50,962

Notes to accounts

1	**Share Capital**		
	Equity share capital		
	Authorized: 2,00,000 equity shares of ₹ 10 each		20,00,000
	Issued & subscribed: 1,00,000 equity shares of ₹ 10 each		**10,00,000**

2	**Reserves and Surplus**		
	General Reserve	10,00,000	
	Add: current year transfer	1,00,000	11,00,000
	Profit & Loss balance		
	Opening balance: Surplus P & L A/c	8,75,500	
	Profit for the year	3,50,962	
	Less: Appropriations:		
	Transfer to General reserve	(1,00,000)	11,26,462
	Securities premium		2,50,000
3	**Long-term borrowings**		**24,76,462**
	Term loan from public sector bank (Sec. by hypothecation)		1,02,00,000
	Less: Installment of Term loan falling due within one year		(17,00,000)
	Total		**85,00,000**
4	**Trade payables**		
	Trade payables	55,08,875	
	Bills payable	1,25,000	56,33,875
5	**Other current liabilities**		
	Rent outstanding	20,000	
	Wages and Salaries Outstanding	1,56,500	1,76,500
6	**PPE (Note 2)**		
	Land		24,00,000
	Factory Buildings		33,21,200
	Plant & Machinery		47,81,250
	Furniture & Fittings		6,68,250
	Total		**1,11,70,700**
7	**Trade receivables**		
	Debtors Outstanding for period exceeding 6 months	85,600	
	Other debts	63,89,400	
	Less: Provision for doubtful debt	(3,23,750)	61,51,250
8	**Cash and bank balances**		
	Cash and cash equivalents		
	Bank balance	9,75,000	
	Cash on hand	1,31,875	11,06,875
9	**Changes in Inventories**		
	Opening Inventory	9,25,000	
	Less: Closing Inventory	(11,37,500)	
	Change		(2,12,500)
10	**Employee benefit expense**		
	Wages and Salaries	12,72,000	
	Add: Wages and Salaries Outstanding	1,56,500	14,28,500
11	**Other operating expenses**		
	Rent	2,20,000	
	Add: outstanding	20,000	2,40,000
	Rates and Taxes		50,000
	Selling & Distribution expenses		4,36,000
	Bad debts		38,500
	Provision for Doubtful Debts (3,23,750-25,000)		2,98,750
	Director's fee		32,000
	Total		**10,95,250**

Note:

1) The final dividend will not be recognized as a liability at the balance sheet date (even if it is declared after reporting date but before approval of the financial statements) as per Accounting Standards. Hence, it has not been recognized in the financial statements for the year ended 31 March, 2022. Such dividends will be disclosed in notes only.

2) **Calculation of depreciation:**

	Book value	**Accumulated depreciation**	**WDV**	**Current year Depreciation**	**Current year WDV**
Land	24,00,000	-	24,00,000	-	24,00,000
Factory building	36,80,000	1,84,000	34,96,000	1,74,800	33,21,200
Plant & Machinery	62,50,000	9,37,500	53,12,500	5,31,250	47,81,250
Furniture & Fittings	8,25,000	82,500	7,42,500	74,250	6,68,250
			Total	**7,80,300**	**1,11,70,700**

DIVIDEND (Sec 123 of Companies Act, 2013)

Dividend	Dividend to be declared / paid out of a) Profits of the company for that year or previous years but after providing depreciation as per Schedule II or b) Money provided by Central Govt. or State Govt. in pursuance of guarantee given by Govt.
General Provisions	➢ Dividend cannot be declared except out of profits. ➢ Dividend to be declared/paid out of free reserves. ➢ Capital cannot be returned to the shareholders by way of dividend. ➢ Dividend is paid to Shareholders; Preference shareholders being paid first. ➢ It is generally calculated on paid up capital i.e., Called up Capital <u>Less</u> Calls in Arrears ➢ No dividend on Calls in Advance ➢ Company cannot declare dividend unless previous year losses & depreciation not provided are set off against profits of current year.
Interim Dividend	The Board of Directors of a company may declare interim dividend during any financial year or at any time during the period from closure of financial year till holding of the AGM out of the surplus in the profit and loss account or out of profits of the financial year for which such interim dividend is sought to be declared or out of profits generated in the financial year till the quarter preceding the date of declaration of the interim dividend: Provided that in case the company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of interim dividend, <u>*such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding three financial years.*</u>
Declaration of Dividend out of Reserves	<u>Withdrawal from Reserves : Conditions</u> 1) Dividend Rate cannot exceed average of previous 3 years 2) Maximum Amount that can be withdrawn from reserves $\leq$ 10% of (Paid up capital + Free Reserves) 3) Minimum Amount left in reserves after withdrawal $\geq$ 15% of (Paid up capital) The amount so drawn shall first be utilised to set off the losses incurred in the financial year in which dividend is declared before any dividend in respect of equity shares is declared.

Question 4 *(RTP May 2021)* *Pg no.____*

XYZ Ltd. is having inadequacy of profits in the year ending 31-03-2022 and it proposes to declare 10% dividend out of General Reserves.

From the following particulars ascertain the amount that can be utilized from general reserves, according to the Companies (Declaration of Dividend out of Reserves) Rules, 2014:

	₹
5,00,000 Equity shares of ₹ 10 each, fully paid up	50,00,000
General Reserves	25,00,000
Revaluation Reserves	6,50,000
Net profit for the year	1,42,500

Average rate of dividend during the last five years has been 12%.

Solution

Amount that can be drawn from reserves for (10% dividend on ₹ 50,00,000 i.e. ₹ 5,00,000)

Profits available

Current year profit	₹ 1,42,500
Amount which can be utilized from reserves (₹ 5,00,000 – 1,42,500)	₹ 3,57,500

Conditions as per Companies (Declaration of dividend out of Reserves) Rules 2014:

Condition I

Since 10% is lower than the average rate of dividend (12%), 10% dividend can be declared.

Condition II

Maximum amount that can be drawn from the accumulated profits and reserves should not exceed 10% of paid up capital plus free reserves ie. ₹ 7,50,000 [10% of (50,00,000 + 25,00,000)]

Condition III

The balance of reserves after withdrawal ₹ 21,42,500 (₹ 25,00,000 - ₹ 3,57,500) should not fall below 15 % of its paid up capital ie. ₹ 7,50,000 (15% of ₹ 50,00,000]

Since all the three conditions are satisfied, the company can withdraw ₹ 3,57,500 from accumulated reserve (as per Declaration and Payment of Dividend Rules, 2014).

Dividend Adjustment

1/4/20 — 31/3/21 — 15/6 — 12/9

15/6: Dividend Proposed by BOD

12/9: Dividend Declared at AGM

FY 2020-21

No Accounting Entry.

Disclosure in Notes of Proposed D/D

FY 2021-22

Declared:

P&L A/c - Dr

To Dividend Payable A/c

Paid:

Dividend Payable A/c - Dr

To Bank A/c

Example:

Profit for the year = 2000000 Opening P&L : 300000

Equity share capital = 5000000

Dividend Declared = 10%. Transfer to General Reserve 5% of Profits

Note to Reserve & Surplus :

1) P&L / Surplus:

Opening	300000	
+ Current Year	2000000	
- Transfer to General Reserve	(100000)	[2000000 x 5%]
- Dividend Payable	(500000)	[5000000 x 10%]
	1700000	

2) General Reserve 100000

Adjustments:

① Trial Balance

	Dr.	Cr.
Salary	50000	

Salary payable 20000

P&L: Employee Benefit Exp.

Salary = 50000 + 20000 = 70000

B/S: Current Liabilities

Other current Liabilities

O/s salary : 20000

② Trial Balance

	Dr.	Cr.
Salary	100000	
O/s Salary		30000

P&L: Employee Benefit Exp.

Salary : 100000

B/S: Current Liabilities

Other current Liabilities

O/s salary : 30000

③

Trial Balance

	Dr.	Cr.
Machinery	100000	

Depreciation @ 10%

P&L: Depreciation

$\Rightarrow 100000 \times 10\% = 10000$

B|S: Property, Plant & Equipment

Machinery 90000

(100000 - 10000)

④

Trial Balance

	Dr.	Cr.
Machinery	150000	
Depreciation	20000	

P&L: Depreciation = 20000

B|S: Property, Plant & Equipment

Machinery = 150000

(5) Trial Balance

	Dr.	Cr.
Machinery	200000	
Acc. Dep. / Provision for Dep.		50000

Depreciation @ 10% on Cost (a) / 10% on WDV (b)

P&L: Depreciation

(a) $200000 \times 10\%$ $\Rightarrow 20000$

(b) $(200000 - 50000) \times 10\%$ $\Rightarrow 15000$

B/S: Property, Plant & Equipment

(a)

Machinery	200000
− Acc. Dep. (50000 + 20000)	(70000)
	130000

(b)

Machinery	200000
− Acc. Dep. (50000 + 15000)	(65000)
	135000

(6)

Trial Balance

	Dr.	Cr.
Machinery	200000	
Acc. Dep. / Provision for Dep.		50000
Depreciation	10000	

P&L: Depreciation = 10000

B/S: Property, Plant & Equipment

Machinery	200000
− Acc. Dep.	(50000)
	150000

(7)

Trial Balance

	Dr.	Cr.
Opening Stock	50000	
Purchases	400000	

Closing Stock 30000

P&L: Purchases 400000

Change in Inventory 20000
(50000 − 30000)

B/S: Current Assets

Inventories 30000

⑧

Trial Balance

	Dr.	Cr.
Closing stock	50000	
Adjusted Purchases	300000	

Op. stock
+ Purchases
- closing stock

P&L: ~~Purchases~~ ~~Change in Inventory~~ Adjusted Purchases 300000

B|S: Current Assets

Inventories 50000

⑨ If written

Closing stock is 20000 more than Opening stock

Then

Opening stock = 30000

Purchases = 320000

P&L: Purchases 320000

Change in Inventory (20000)

B|S: Current Assets

Inventories 50000

(10) Dividend Related

Case 1: Appearing in Trial Balance

(a) Trial Balance

	Dr.	Cr.
Dividend Payable		50000

Entry Passed:

P&L A/c – Dr 50000
To Dividend Payable A/c 50000

B/S: Current Liabilities

Other current Liabilities

Dividend Payable 50000

(b) Trial Balance

	Dr.	Cr.
Dividend / Interim D/D Paid	30000	

Entry Passed:

Dividend A/c – Dr. 30000
To Bank A/c 30000

B/S: Note to Reserve & Surplus

P&L / Surplus xx
– Dividend paid (30000)

Case 2: Appearing Outside Trial Balance

a) Dividend Proposed : No Accounting Entry.

Disclosure in Notes to A/cs of Dividend Proposed.

b) Dividend Declared :

Entry :

P&L A/c - Dr

To Dividend Payable

1. B/S : Note to Reserve & Surplus

P&L / Surplus	xx
- Dividend Payable	(xx)

2. B/S : Current Liabilities

Other current Liabilities

Dividend Payable	xx

(11) Share Forfeiture & Reissue

Example: 20000 equity shares of 10 each fully called up.
Calls in Arrears on 3000 shares @ 2/share

(1)

Calls in Arrears ✓
Share Forfeiture X

Share capital

20000 sh. of 10 each	200000
- Calls in Arrears (3000 X 2)	(6000)
	194000

Dividend on : 194000

(2)

Calls in Arrears ✓
Share Forfeiture ✓
Share Reissue X

Entry:

Share capital A/c - Dr	3000X10
To Share F.F. A/c	3000X8
To Calls in Arrears A/c	3000X2

Share capital

17000 Sh. of 10 each	170000
+ Share F.F.	24000
	194000

Dividend on : 170000

(3)

Share Reissue ✓
Reissued at 5/share

Entry:

Bank A/c - Dr	3000 X 5
Share F.F. A/c - Dr.	3000 X 5
To Share capital	3000 X 10
Share F.F. A/c - Dr	3000 X 3
To Capital Reserve	3000 X 3

Share capital

20000 shares of 10 each	200000

Res. & Surplus

Capital Reserve	3000X3

Dividend on : 200000

CASH FLOW STATEMENT (AS-3)

"Winners aren't who Never fail, But People who Never quit…"

It is an additional information provided to the users of accounts in the form of a statement, which reflects the various sources from where cash was generated (inflow of cash) by an enterprise during the relevant accounting year and how these inflows were utilized (outflow of cash) by the enterprise.
Financial statements with respect to one person company, small company, dormant company and private company (if such a private company is a startup), may not include the cash flow statement.

'CASH & CASH EQUIVALENTS'

Cash	Cash in hand, Cash at Bank
Cash Equivalents	Short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value. *It has a short maturity of, say, 3 months or less* from the date of acquisition. Investments in shares are not normally taken as cash equivalent

TRANSACTIONS NOT CONSIDERED AS CASH FLOWS

Meaning	Transactions which represent movements between items of Cash or Cash Equivalents are not considered as Cash Flows.
Examples	a) Cash deposited into Bank; b) Cash withdrawn from Bank; c) Purchase/Sale of Short-term Marketable Securities (neither held as Current Investments nor held as Non-current Investments). d) It is important to note that a change in cash does not necessarily imply cash flow. For example: Suppose an enterprise has a bank balance of USD 10,000, stated in books at 4,90,000 using the rate of exchange 49/USD prevailing on date of receipt of dollars. If the closing rate of exchange is 50/USD, the bank balance will be restated at 5,00,000 on the balance sheet date. The increase is, however, not a cash flow because neither there is any cash inflow nor there is any cash outflow.

'CASH FLOWS'

Cash Flows	Cash Flows are inflows and outflows of Cash and Cash equivalents.
Cash Inflows	Cash Inflow arises when the net effect of transaction is increase in the amount of Cash or Cash Equivalents.
Cash Outflows	Cash Outflow arises when the net effect of transaction is to decrease in the amount of Cash or Cash Equivalents.

EXAMPLES OF CASH FLOWS

CASH INFLOWS	CASH OUTFLOWS
1) Cash Sales of Goods	1) Cash Purchases of Goods
2) Cash received from Trade Debtors	2) Cash paid to Trade Creditors
3) Cash received from commission & Royalty	3) Operating Expenses paid (e.g. Salaries & Wages, Administration Exp. Selling Exp.)
4) Sale of Fixed Assets for Cash	4) Income Tax paid
5) Sale of Investments (whether Current or Non-Current) for Cash	5) Purchase of Fixed Assets for Cash
6) Loans & Advances repayment received (whether Short term or Long term)	6) Purchase of Investments (whether Short term or Long term) for Cash
7) Income received on Investments (whether Current or Non-Current)	7) Loans & Advances granted (whether Short term or Long term)
8) Issue of Equity Shares for Cash	8) Buy-back of Equity Shares for Cash
9) Issue of Preference Shares for Cash	9) Redemption of Preference Shares for Cash
10) Issue of Debentures for Cash	10) Redemption of Debentures for Cash
11) Loans taken (whether Short/Long term)	11) Loans repaid (whether Short/Long term)
	12) Interest on Debentures & Loans paid.
	13) Final Dividend on Equity Shares paid.
	14) Dividend on Preference Shares paid.
	15) Interim Dividend on Equity Shares paid.

ACTIVITIES

Operating Activities
Principal Revenue producing activities

Investing Activities
Acquisition & disposal of Long Term Assets & Investments

Financing Activities
Activities that result in change in size & composition of Owner's capital & borrowings

Interest & Dividend Received

Normal / Non Financial Enterprise → Investing Activity

Financial Enterprise → Operating Activity

Dividend Paid → Financing Activity (Always)

In case of *Financial Enterprises* the following activities are classified as Operating Activities since they relate to the main revenue-producing activity of that enterprise:

- *Purchases and Sales of Shares & Debentures of other companies for Cash*
- *Dividend received on Shares of other companies*
- *Interest received on Debentures of other companies*
- *Loans & Advances granted*
- *Interest received on Loans & Advances granted*

Other Examples: Cash receipts and cash payments of an insurance entity for premiums and claims, annuities, and other policy benefits.
Cash receipts & payments relating to futures contracts, forward contracts, option contracts & swap contracts when the contracts are held for dealing or trading purposes.
Cash flows arising from the purchase and sale of dealing or trading securities

NON-CASH TRANSACTIONS

Meaning	Those transactions which do not involve Cash
Examples (Verification by Journal Entry)	Issue of Equity Shares or Debentures against the purchase of an Asset Asset A/c Dr To Equity Share Capital A/c / Debentures A/c
	Issue of Equity Shares on conversion of Convertible Debentures Convertible Debentures A/c Dr To Equity Share Capital A/c
Why ignored in CFS?	Non-Cash transactions are ignored while preparing Cash Flow Statement because these do not involve Cash.

STEPS INVOLVED IN THE PREPARATION OF CASH FLOW STATEMENT

Step 1: Calculate the Cash flow from Operating activities.
Step 2: Calculate the Cash flow from Investing activities
Step 3: Calculate the Cash flow from Financing activitites
Step 4: Calculate Net Increase/(Decrease) in cash & cash equivalents [Step (1 + 2 + 3)]
Step 5: Calculate the Cash and Cash Equivalents at the beginning of period
Step 6: Calculate the Cash and Cash Equivalents at the end of period [Step (4 + 5)]

HOW TO COMPUTE NET CASH FLOW FROM OPERATING ACTIVITIES (UNDER DIRECT METHOD)

Particulars	₹	₹
A. Operating Receipts in Cash (e.g.)		
Cash Sales	xxx	
Cash receipts from Debtors	xxx	
Trading Commission received	xxx	xxx
B. Opening Payments in cash (e.g.)		
Cash Purchases	xxx	
Cash paid to Suppliers	xxx	
Wages & Salaries Paid	xxx	
Office and Administration Expenses paid	xxx	
Manufacturing overheads paid	xxx	
Selling and Distribution expenses paid	xxx	xxx
C. Cash Generated from Operations before taxes (A-B)		xxx
D. Income tax paid (Net of refund of Tax)		xxx
E. Cash flow before extraordinary item (C-D)		xxx
F. Extraordinary item		xxx
G. Net cash from (used in) Operating Activities		xxx

Question 1 *(Inter July 2021) (5 Marks)* *Pg no.____*

Prepare cash flow statement of Gama Limited for the year ended 31st March, 2021 in accordance with AS-3(Revised) from the following cash account summary:

Cash summary Account

Inflows	₹ ('000)	Outflows	₹ ('000)
Opening Balance	945	Payment to suppliers	54,918
Receipts from Customers	74,682	Purchase of Investments	351
Sale of Investments (Cost 4,05,000)	459	Property, plant & equipment acquired	6,210
Issue of Shares	8,100	Wages and salaries	1,863
Sale of Property, Plant & equipment	3,456	Payment of Overheads	3,105
		Taxation	6,561
		Dividends	2,160
		Repayment of Bank Overdraft	6,750
		Interest paid on Bank Overdraft	1,350
		Closing Balance	4,374
	87,642		87,642

Solution

Gama Limited

Cash Flow Statement for the Year Ended 31st March 2021

Particulars	**Amount (₹'000)**	**Amount (₹'000)**
Cash flow from Operating Activities:		
Cash receipts from customers	74,682	
Cash payments to suppliers	(54,918)	
Cash payments for wages & salaries	(1,863)	
Cash payments of overheads	(3,105)	
Cash Generated from Operations	14,796	
Payment of Taxation	(6,561)	
Net Cash from Operating Activities		8,235
Cash Flow from Investing Activities:		
Proceeds from sale of investments	459	
Proceeds from sale of Property, Plant and Equipment	3,456	
Purchase of Investments	(351)	
Purchase of Property, Plant and Equipment	(6,210)	
Net Cash Used in Investing Activities		(2,646)
Cash Flow from Financing Activities:		
Proceeds from issue of shares	8,100	
Payment of Dividend	(2,160)	
Repayment of Bank Overdraft	(6,750)	
Interest paid on Bank Overdraft	(1,350)	
Net Cash Used in Financing Activities		(2,160)
Net Increase in Cash & Cash Equivalent		3,429
Cash and Cash Equivalent in the Beginning of the year		945
Cash and Cash Equivalent in the end of the year		4374

Question 2 *(RTP May 2018) / (RTP Nov 2021)* *Pg no._____*

Prepare a Cash Flow Statement for the year ended 31st March, 2022 (Using direct method):

a) Total sales for year were ₹ 398 crores out of which cash sales amounted to ₹ 262 crores.
b) Receipts from credit customers during the year, totaled ₹ 134 crores.
c) Purchases for the year amounted to ₹ 220 crores out of which credit purchase was 80%.
d) Balance in creditors as on
   1.4.2021 ₹ 84 crores
   31.3.2022 ₹ 92 crores
e) Suppliers of other consumables and services were paid ₹ 19 crores in cash.
f) Employees of the enterprises were paid 20 crores in cash.
g) Fully paid preference share of the face value of ₹32 crores were redeemed. Equity shares of the face value of ₹20 crores were allotted as fully paid up at premium of 20%.
h) Debentures of ₹ 20 crores at a premium of 10% were redeemed. Debenture holders were issued equity shares in lieu of their debentures.
i) ₹26 crores were paid by way of income tax.
j) A new machinery costing ₹ 25 crores was purchased in part exchange of an old machinery. The book value of the old machinery was ₹13 crores. Through the negotiations, the vendor agreed to take over the old machinery at a higher value of ₹15 crores. The balance was paid in cash to the vendor.
k) Investment costing ₹ 18 cores were sold at a loss of ₹2 crores.
l) Dividends totalling ₹ 15 crores was also paid.
m) Debenture interest amounting ₹ 2 crore was paid.
n) On 31st March 2021, Balance with Bank and Cash on hand totaled ₹ 2 crores

Solution

Cash flow statement (using Direct Method) for the year ended 31st March, 2022

	₹ (in crore)	₹ (in crore)
Cash flow from operating activities		
Cash sales	262	
Cash collected from credit customers	134	
Less: Cash Purchases	(44)	
Less: Payment to Creditors (84+176-92)	(168)	
Less: Paid to Suppliers of Consumables & services	(19)	
Less: Payment to Employees	(20)	
Cash from operations	145	
Less: Income tax paid	(26)	
Net cash generated from operating activities		119
Cash flow from investing activities		
Payment for purchase of Machine (25-15)	(10)	
Proceeds from sale of Investments	16	
Net cash generated from investing activities		6
Cash flow from financing activities		
Redemption of Preference shares	(32)	
Proceeds from issue of Equity shares	24	
Debenture interest paid	(2)	
Dividend Paid	(15)	
Net cash used in financing activities		(25)
Net increase in cash and cash equivalent		100
Add: Cash and cash equivalents as on 1.04.2021		2
Cash and cash equivalents as on 31.3.2022		**102**

HOW TO COMPUTE NET CASH FLOW FROM OPERATING ACTIVITIES (UNDER INDIRECT METHOD)

Particulars	₹	₹
Step 1: Calculate Net Profit before Taxation & Extraordinary item:		
Closing Balance of P & L A/c		xxx
Less: Opening Balance of P&L A/c (or Add: Opening Bal. of P&L A/c (Dr.)		xxx
Add: Dividend declared for the current year		xxx
Add: Interim Dividend paid during the current year		xxx
Add: Transfer to Reserve (or Less : Transfer from Reserve)		xxx
Add: Provision for Tax made during the Current Year		xxx
Less: Refund of Tax credited to P&L A/c		(xxx)
Less: Extraordinary Item, if any, credited to P&L A/c (e.g. Insurance proceeds from earthquake disaster settlement)		(xxx)
Add: Extraordinary Debit Items (e.g. Loss due to earthquake)		xxx
Net Profit before Taxation and Extraordinary Item		xxx
Step 2: Calculate Operating Profit before Working Capital Changes:		
Net Profit before Taxation and Extraordinary Item		xxx
Adjustments for Non-Cash and Non-Operating Items: (For Example)		
Depreciation	xxx	
Interest on Debentures & Loans (whether Short term or Long Term)	xxx	
Preliminary Expenses/Underwriting Commission	xxx	
Discount on Issue of Debentures written off	xxx	
Goodwill/Patents/Trade Marks/Copyright amortized	xxx	
Loss on Sale of Investments (whether Current or Non Current)	xxx	
Interest income from Investments (whether current or non-current)	(xxx)	
Dividend income	(xxx)	
Rental income	(xxx)	
Profit on sale of Investments (whether current or non-current)	(xxx)	xxx
Operating profit before working capital changes		xxx
Step 3: Calculate Cash from Operations before tax & Extraordinary item:		
A. Operating profit before working capital changes		xxx
B. Changes in current assets & Current Liabilities		
Decrease in Inventories, Trade Receivables etc.	xxx	
Increase in Trade Payables, O/s exp. Etc.	xxx	
Increase in Inventories, Trade Receivables etc.	(xxx)	
Decrease in trade Payables, O/s Exp. etc.	(xxx)	xxx
Cash Generated from Operations		xxx
Step 4: Calculate Cash generated from Operations after tax but before extraordinary item:		
A. Cash generated from Operations		xxx
B. Less: Income taxes paid		(xxx)
(Note: Income tax should be related to operating activities only)		
C. Cash flow before extraordinary item		xxx
Step 5 : Calculate Net Cash from (used in) Operating Activities :		
Cash Flow before Extraordinary Items		xxx
Add : Extraordinary Items (e.g. Insurance proceeds from earthquake disaster settlement, Govt. Grant)		xxx
Net Cash Flow from (used in) Operating Activities		xxx

Question 3

Pg no._____

The following are the summarized Balance Sheets of 'X' Ltd. as on March 31, 2021 and 2022:

Liabilities	As on 31.03.2021	As on 31.03.2022
Equity share capital	10,00,000	12,50,000
Capital Reserve	-	10,000
General Reserve	2,50,000	3,00,000
Profit and Loss A/c	1,50,000	1,80,000
Long term loan from the bank	5,00,000	4,00,000
Trade Payables	5,00,000	4,00,000
Provision for Taxation	50,000	60,000
Dividend payable	1,00,000	1,25,000
	25,50,000	27,25,000
Assets	**As on 31.03.2021**	**As on 31.03.2022**
Land and Building	5,00,000	4,80,000
Machinery	7,50,000	9,20,000
Investment	1,00,000	50,000
Inventory	3,00,000	2,80,000
Trade Receivables	4,00,000	4,20,000
Cash in Hand	2,00,000	1,65,000
Cash at Bank	3,00,000	4,10,000
	25,50,000	27,25,000

Additional Information:

a) Dividend of ₹ 1,00,000 was paid during the year ended March 31, 2022.

b) Machinery during the year purchased for ₹ 1,25,000.

c) Machinery of another company was purchased for a consideration of ₹ 1,00,000 payable in equity shares.

d) Income-tax provided during the year ₹ 55,000.

e) Company sold some investment at profit of ₹ 10,000, which was credited to Capital reserve.

f) There was no sale of machinery during the year.

g) Depreciation written off on Land and Building ₹ 20,000.

From the above particulars, prepare a cash flow statement for the year ended March, 2022 as per AS 3 (Indirect method).

Solution

Cash Flow Statement for the year ending on March 31, 2022

		₹	₹
I	**Cash flows from Operating Activities**		
	Net profit made during the year (W.N.1) Adjustment for depreciation on Machinery (W.N.2) Adjustment for depreciation on Land & Building	2,60,000 55,000 20,000	
	Operating profit before change in Working Capital Decrease in inventory Increase in trade receivables Decrease in trade payables Income-tax paid	3,35,000 20,000 (20,000) (1,00,000) (45,000)	
	Net cash from operating activities		1,90,000
II.	**Cash flows from Investing Activities**		
	Purchase on Machinery Sale of Investments	(1,25,000) 60,000	(65,000)

III.	**Cash flows from Financing Activities**		
	Issue of equity shares (2,50,000-1,00,000) Repayment of Long Term Loan from Bank (5,00,000-4,00,000) Dividend paid	1,50,000 (1,00,000) (1,00,000)	(50,000)
	Net increase in cash and cash equivalent		75,000
	Cash and cash equivalents at the beginning of the period		5,00,000
	Cash and cash equivalents at the end of the period		5,75,000

Working Notes:

(i) **Net Profit made during the year ended 31.3.2022**

	₹
Increase in P & L (Cr.) Balance Add: Transfer to general reserve Add: Provision for taxation made during the year Add: Dividend payable during the year	30,000 50,000 55,000 1,25,000
	2,60,000

(ii) **Machinery Account**

	₹		₹
To Balance b/d To Bank To Equity share capital	7,50,000 1,25,000 1,00,000	By Depreciation (Bal. Fig.) By Balance c/d	55,000 9,20,000
	9,75,000		**9,75,000**

(iii) **Provision for Taxation Account**

	₹		₹
To Cash (Bal. Fig.) To Balance c/d	45,000 60,000	By Balance b/d By P & L A/cd	50,000 55,000
	1,05,000		**1,05,000**

(iv) **Dividend Payable Account**

	₹		₹
To Bank To Balance c/d	1,00,000 1,25,000	By Balance b/d By P & L A/c (Bal. Fig.)	1,00,000 1,25,000
	2,25,000		**2,25,000**

(v) **Investment Account**

	₹		₹
To Balance b/d To Capital Reserve A/c (Profit on sale of investment)	1,00,000 10,000	By Bank A/c (Bal. fig. for investment sold) By Balance c/d	60,000 50,000
	1,10,000		**1,10,000**

Question 4 *(Inter Jan 2021) (12 Marks)* *Pg no.____*

Following information was extracted from books of S Ltd. for the year ended 31st March, 2022:

(1) Net profit before taking into account income tax and after talking into account the following items was ₹ 30 lakhs;
   (i) Depreciation on Property, Plant & Equipment ₹ 7,00,000
   (ii) Discount on issue of debentures written off ₹ 45,000.
   (iii) Interest on debentures paid ₹ 4,35,000
   (iv) Investment of Book value ₹3,50,000 sold for ₹3,75,000.
   (v) Interest received on Investments ₹70,000

(2) Income tax paid during the year ₹ 12,80,000

(3) Company issued 60,000 Equity Shares of ₹ 10 each at premium of 20% on 10th April, 2021.

(4) 20,000,9% Preference Shares of ₹ 100 each were redeemed on 31st March, 2022 at a premium of 5%

(5) Dividend paid during the year amounted to ₹ 11 Lakhs

(6) A new Plant costing ₹ 7 Lakhs was purchased in part exchange of an old plant on 1st January,2022. The book value of the old plant was ₹ 8 Lakhs but the vendor took over the old plant at a value of ₹ 6 Lakhs only. The balance amount was paid to vendor through cheque on 30th March, 2022.

(7) Company decided to value inventory at cost, whereas previously the practice was to value inventory at cost less 10%. The inventory according to books on 31.03.2022 was ₹ 14,76,000. The inventory on 31.03.2021 was correctly valued at ₹ 13,50,000.

(8) Current Assets & Current Liabilities in the beginning & at the end of year 21-22 were as:

	As on 01.04.2021	As on 31.03.2022
Inventory	13,50,000	14,76,000
Trade receivables	3,27,000	3,13,200
Cash & Bank	2,40,700	3,70,500
Trade payables	2,84,700	2,87,300
Outstanding expenses	97,000	1,01,400

You are required to prepare a Cash Flow Statement for the year ended 31st March, 2022 as per AS 3 (revised) using the indirect method.

Solution

Cash Flow Statement for the year ended 31st March, 2022

	Amount	Amount
Cash flow from Operating Activities		
Net profit before income tax and extraordinary items:		30,00,000
Depreciation on Property, plant and equipment	7,00,000	
Discount on issue of debentures	45,000	
Interest on debentures paid	4,35,000	
Interest on investments received	(70,000)	
Profit on sale of investments	(25,000)	
Stock adjustment {14,76,000 less16,40,000(14,76,000/90X100)}	1,64,000	12,49,000
Operating profit before working capital changes		42,49,000
Increase in inventory {16,40,000(14,76,000/90X100) less 13,50,000}	(2,90,000)	
Decrease in trade receivable	13,800	
Increase in trade payables	2,600	
Increase in outstanding expenses	4,400	(2,69,200)
Cash generated from operations		39,79,800
Income tax paid		(12,80,000)
Net cash flow from operating activities		26,99,800

Cash flow from Investing Activities;		
Sale proceeds of investments	3,75,000	
Interest received on investments	70,000	
Purchase of Fixed Assets (7,00,000 less 6,00,000)	(1,00,000)	
Net cash flow from investing activities		3,45,000
Cash flow from Financing Activities		
Proceeds of issue of equity shares	7,20,000	
Redemption of preference shares	(21,00,000)	
Dividend paid	(11,00,000)	
Interest on debentures paid	(4,35,000)	
Net cash used in financing activities		(29,15,000)
Net increase in cash and cash equivalents during theyear		1,29,800
Add: Cash and cash equivalents as on 31.3.2021		2,40,700
Cash and cash equivalents as on 31.3.2022		3,70,500

*Net profit given in the question is after considering only the items listed as information point (1) of the question; hence amount of loss on plant not added back

Question 5 *(Inter Dec 2021) (5 Marks)* Pg no._____

Following are the extracts from the Balance Sheet of ABC Ltd.

Liabilities	31.3.2020	31.3.2021
	(₹)	(₹)
Equity Share Capital	25,00,000	35,60,000
10% Preference Share Capital	7,00,000	6,00,000
Securities Premium Account	5,00,000	5,50,000
Profit & Loss A/c	20,00,000	28,00,000

Equity Share Capital for the year ended 31st March, 2021 includes ₹ 60,000 of equity shares issued to Grey Ltd. at par for supply of Machinery of ₹ 60,000.
Profit & Loss account on 31st March, 2021 includes ₹ 50,000 of dividend received on Equity shares invested in X Ltd.
Show how the related items will appear in the Cash Flow Statement of ABC Ltd. as per AS-3

Solution

The related items given in the question will appear in the Cash Flow Statement as follows:

		₹	₹
Cash flows from operating activities			
Closing Balance as per Profit and Loss Account		28,00,000	
Less: Opening Balance as per Profit and Loss Account		(20,00,000)	
		8,00,000	
Less: Dividend received		(50,000)	7,50,000
Cash flows from investing activities			
Dividend received			50,000
Cash flows from financing activities			
Proceeds from issuance of share capital			
Equity shares issued for cash	10,00,000		
Securities premium (₹ 5,50,000 – 5,00,000)	50,000	10,50,000	
Redemption of Preference shares (₹ 7,00,000 – ₹ 6,00,000)		(1,00,000)	9,50,000

Note:

a) Machinery acquired by issue of shares does not amount to cash outflow, hence also not considered in the cash flow statement.

IMPORTANT POINTS:

Loans/Advances given and Interests earned

For Financial enterprises	Operating cash flows
For Non-Financial enterprises	Investing cash flows
Given to Subsidiaries	Investing cash flows for all enterprises
Given to Employees	Operating cash flows for all enterprises.
Advance Payments to Suppliers	Operating cash flows for all enterprises.

Interests earned from customers for late payments are operating cash flows for non-financial enterprises.

Loans/Advances taken and interests paid

For Financial enterprises	Operating cash flows
For Non-Financial enterprises	Financing cash flows
Advance Taken from Customers	Operating cash flows

Interests paid to suppliers for late payments are operating cash flows for all enterprises.
Interests taken as part of inventory costs in accordance with AS 16 are operating cash flows

Investments made and Dividend earned

For Financial enterprises	Operating cash flows
For Non-Financial enterprises	Investing cash flows
Given to Subsidiaries	Investing cash flows for all enterprises

Tax Deducted at Source

If concerned incomes are Operating Incomes	Operating cash Outflow
If concerned incomes are Investment Incomes	Investing cash Outflow
If concerned expenses are Operating Expenses	Operating cash Inflow
If concerned expenses are Financing Expenses	Financing cash Inflow

Insurance claims received

Against loss of stock or loss of profits	Extraordinary operating cash inflows
Against loss of fixed assets	Extraordinary investing cash inflows

Question 6 *(Inter Nov 2019) (5 Marks)* Pg no._____

Prepare cash flow from investing activities as per AS 3 of M/s Subham Creative Limited for year ended 31.3.2022.

Particulars	Amount
Machinery acquired by issue of shares at face value	2,00,000
Claim received for loss of machinery in earthquake	55,000
Unsecured loans given to associates	5,00,000
Interest on loan received from associate company	70,000
Pre-acquisition dividend received on investment made	52,600
Debenture interest paid	1,45,200
Term loan repaid	4,50,000
Interest received on investment (TDS of ₹ 8,200 was deducted on the above interest)	73,800
Purchased debentures of X Ltd., on. 1st December, 2021 which are redeemable within 3 months	3,00,000
Book value of plant & machinery sold (loss incurred ₹ 9,600)	90,000

Solution

Cash Flow Statement from Investing Activities

Cash generated from investing activities		
Interest on loan received	70,000	
Pre-acquisition dividend received on investment made	52,600	
Unsecured loans given to subsidiaries	(5,00,000)	
Interest received on investments (gross value)	82,000	
TDS deducted on interest	(8,200)	
Sale of Plant & Machinery (90,000 – 9,600)	80,400	
Cash used in investing activities (before extra-ordinary item)		(2,23,200)
Extraordinary claim received for loss of machinery		55,000
Net cash used in investing activities (after extra-ordinary item)		**(1,68,200)**

Note:

a. Debenture interest paid and Term Loan repaid are financing activities and therefore not considered for preparing cash flow from investing activities.

b. Machinery acquired by issue of shares does not amount to cash outflow, hence also not considered in the above cash flow statement.

c. The investments made in debentures are for short-term, it will be treated as 'cash equivalent' and will not be considered as outflow in cash flow statement.

Question 7 *(ICAI Study Material)* Pg no._____

How would the following cash flows be classified in accordance with AS 3?

a) Corporate Income Tax paid amounting to ₹ 70 lakhs during the reporting period.

b) Payment of advance tax ₹ 8,75,000 out of which ₹ 75,000 was towards capital gains arising on account of sale of assets during the reporting period.

c) Fixed Deposits withdrawn by customers of State Bank of India ₹ 3 crores.

Solution

a) ₹ 70 lakhs: Operating Cash Flows

b) ₹ 8,00,000: Operating Cash Flows ₹ 75,000: Investing Cash Flows

c) ₹ 3 crores: Operating Cash Flows for State Bank of India.

Question 8 – *(Inter Nov 2022) (5 Marks)* Pg no._____

Ridgeway Limited, a Non-Financial company has the following activities:

a) Dividend paid for the year.
b) TDS on interest income earned on investments made.
c) Loans and advances given to suppliers and interest earned from them.
d) Deposit with bank for a term of two years.
e) Highly liquid Marketable Securities (without risk of change in value).
f) Investments made and dividends earned on them.
g) Insurance claims received against loss of stock or loss of profits.
h) Loans and advances given to subsidiaries and interest earned from them.
i) Issue of Bonus Shares.
j) Term loan repaid.

You are required to classify the above activities in Cash Flow Statement as per 'AS-3'.

Solution

No.	Particulars	Activities
(i)	Dividend paid for the year	Financing
(ii)	TDS on interest income earned on investments made	Investing
(iii)	Loans and advances given to suppliers and interest earned from them	Operating
(iv)	Deposit with bank for a term of two years	Investing
(v)	Highly liquid Marketable Securities (without risk of change in value)	Cash Equivalent
(vi)	Investments made and dividends earned on them	Investing
(vii)	Insurance claims received against loss of stock or loss of profits	Operating
(viii)	Loans and advances given to subsidiaries and interest earned from them	Investing
(ix)	Issue of Bonus Shares	No Cash Inflow /Cash outflow
(x)	Term Loan repaid	Financing

REPORTING ON NET BASIS

As per AS 3, Cash Flow Statements, an enterprise should report separately major classes of gross cash receipts and gross cash payments arising from investing and financing activities, *except* in the case of:

- cash receipts and payments on behalf of customers when the cash flows reflect the activities of the customer rather than those of the enterprise; and
- cash receipts and payments for items in which the turnover is quick, the amounts are large, and the maturities are short.

Cash flows arising from each of the following activities of a financial enterprise may be reported on a net basis:

(a) cash receipts & payments for acceptance & repayment of deposits with fixed maturity date
(b) placement of deposits with and withdrawal of deposits from other financial enterprises
(c) cash advances & loans made to customers and the repayment of those advances & loans

BUSINESS PURCHASE

Aggregate cash flows arising from acquisitions & disposals of subsidiaries or other business units should be presented separately and classified as cash flow from investing activities.

(a) The cash flows from disposal and acquisition should not be netted off.

(b) An enterprise should disclose, in aggregate, in respect of both acquisition and disposal of subsidiaries or other business units during the period each of the following:
 (i) The total purchase or disposal consideration; and
 (ii) The portion of the purchase or disposal consideration discharged by means of cash and cash equivalents.

EXCHANGE GAINS AND LOSSES

The exchange gains/losses in respect of cash and cash equivalents in foreign currency (e.g. balance in foreign currency bank account) are restated in the balance sheet in reporting currency at rate of exchange on balance sheet date. The change in cash or cash equivalents due to exchange gains and losses are however not cash flows. This being so, the net increases/decreases in cash or cash equivalents in the cash flow statements are stated exclusive of exchange gains and losses.
The resultant difference between cash and cash equivalents as per the cash flow statement and that recognised in the balance sheet is reconciled in the note on cash flow statement.

Question 9

Pg no._____

Ruby Exports had a bank balance of USD 25,000, stated in books at ₹ 16,76,250 using the rate of exchange ₹ 67.05 per USD prevailing on the date of receipt of dollars. However, on the balance sheet date, the closing rate of exchange was ₹ 67.80, and the bank balance had to be restated at ₹ 16,95,000. Comment on the effect of change in bank balance due to exchange rate fluctuation and also discuss how it will be disclosed in Cash Flow Statement of Ruby Exports with reference to AS-3.

Solution

Cash flows are inflows (i.e. receipts) and outflows (i.e. payments) of cash and cash equivalents. Any transaction, which does not result in cash flow, should not be reported in the cash flow statement. Movements within cash or cash equivalents are not cash flows because they do not change cash as defined by AS 3 “Cash Flow Statements” which is sum of cash, bank and cash equivalents.

In the given case, due to increase in rate of foreign exchange by 75 paise, there is increase (change) in bank balance. This increase of ₹ 18,750 (25,000 x 0.75) is not a cash flow because neither there is any cash inflow nor there is any cash outflow. Therefore, this change in bank balance amounting ₹ 18,750 need not be disclosed in Cash Flow Statement of Ruby exports.

The net increase/decrease in Cash/Cash equivalents in the Cash Flow Statements are stated exclusive of exchange gains and losses. The resultant difference between Cash and Cash Equivalents as per the Cash flow statement and that recognized in the balance sheet is reconciled in the note on cash flow statements.

BUYBACK OF SECURITIES

"You can't go back and change the beginning, but you can start where you are and change the ending."

Meaning:

Buyback means purchase of its own shares by a company. When shares are bought back by a company they have to be cancelled by the company. Thus shares bought back results in decrease in share capital of the company. A company having sufficient cash may decide to buyback its own shares.

Objectives/Advantages of Buyback:

a) To increase Earning per share if there is no dilution in company's earnings as the buyback of shares reduces the outstanding number of shares.
b) To increase promoters holding as the shares bought back are cancelled & also discourage others to make hostile bid to takeover the company (i.e. to eliminate threats by shareholders who are looking for a controlling stake)
c) To support the share price on the stock exchange when the share price in the opinion of company management is less than its worth, especially in depressed market (i.e to take the advantage of undervaluation. For instance, if a company is undervalued due to any microeconomic & macroeconomic reason, it buys its shares back at the current market price & issues those later when the prices go up)
d) To pay surplus cash to the shareholders when the company does not need it for the business.

Basic Conditions:

Section 68 (2) further states that no company shall purchase its own shares or other specified securities unless—

(i) the buy-back is authorised by its articles
(ii) a special resolution has been passed in general meeting of the company authorizing the buy-back
Exception: In case the buy back is upto 10% of paid up equity + free reserves, the same may be done with the authorization of the Board Resolution
(iii) There shall be a minimum gap of 1 year in buyback offer from the date of closure of the previous buy back
(iv) All the shares or other specified securities for buy-back are fully paid-up
(v) Every buy-back shall be completed within 12 months from the date of passing the special resolution, or the resolution passed by the board of directors.

As per Section 68 (1) of the Companies Act 2013, buy back of shares can be made out of: its free reserves; or the securities premium account; or the proceeds of any shares or other specified securities.

Provided that no buyback 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 other specified securities

Three Test Conditions

(i) Maximum Limit of number of equity shares to be bought back must not exceed 25% of total paid up equity capital.

(ii) Maximum Limit of amount of equity shares to be bought back must not exceed 25% of (Paid up capital & Free reserves)

(iii) Debt Equity ratio must not be > 2:1 after buyback
where Debt = Secured + Unsecured Debt (both long term & short term)
Equity = Capital + Free Reserves

JOURNAL ENTRIES

S.No	Particulars	Journal Entry
1.	To make partly paid equity shares fully paid up	Equity Share Final Call A/c Dr. To Equity Share Capital A/c Bank A/c Dr. To Equity Share Final Call A/c
2.	To realize investments to provide cash for buyback	Bank A/c Dr. P&L A/c (Loss) Dr. To Investments A/c To P&L A/c (Profit)
3.	To issue Preference shares	Bank A/c Dr. To Preference Share Capital A/c To Securities Premium A/c
4.	To cancel the shares bought back	Equity Share Capital A/c Dr. Premium on Buyback A/c Dr. To Equity Share Buyback A/c Equity Share Buyback A/c Dr. To Bank A/c
5.	For closing the premium on buyback account	Securities Premium A/c Dr. General (Revenue) Reserve/ P&L A/c Dr. To Premium on Buyback A/c
6.	Transfer to CRR (Capital Redemption Reserve)*	General (Revenue) Reserve A/c Dr. P&L A/c Dr. Free Reserve (any) A/c Dr. To CRR A/c

*Note: CRR can be utilized for issuing fully paid bonus shares to its members.

Face Value of Equity Shares bought back	XX
Less: Face Value of shares issued	(XX)
Amount to be transferred to CRR	XX

CREATION OF CRR

Case 1:

Balance sheet

Liabilities	Lakhs	Assets	Lakhs
Share capital	10	Sundry Assets	30
P&L A/c	10		
Creditors	10		
	30		30

Case 2 : Buyback of 2 Lacs: No CRR

Balance sheet

Liabilities	Lakhs	Assets	Lakhs
Share capital	~~10~~ 8	Sundry Assets	~~30~~ 28
P&L A/c	10		
Creditors	10		
	~~30~~ 28		~~30~~ 28

Case 3 : Buyback of 2 Lacs: CRR Created

Balance sheet

Liabilities	Lakhs	Assets	Lakhs
Share capital	~~10~~ 8	Sundry Assets	~~30~~ 28
P&L A/c	10		
CRR			
Creditors	10		
	~~30~~ 28		~~30~~ 28

Question 1 *(Inter Jan 2021) (5 Marks)* *Pg no._____*

The Directors of Umang Ltd. passed a resolution to buyback 5,00,000 of its fully paid equity shares of ₹ 10 each at ₹ 15 per share. This buyback is in compliance with the provisions of the Companies Act, 2013. For this purpose, the company

(i) Sold its investments of ₹ 30,00,000 for ₹ 25,00,000.

(ii) Issued 20,000, 12% preference shares of ₹ 100 each at par, the entire amount being payable with application.

(iii) Used ₹ 15,00,000 of its Securities Premium Account apart from its adequate balance in General Reserve to fulfill the legal requirements regarding buy-back.

(iv) The company has necessary cash balance for the payment to shareholders.

You are required to pass necessary Journal Entries (including narration) regarding buyback of shares in the books of Umang Ltd.

Solution

Journal Entries

S.No.	Particulars		L.F.	Dr.	Cr.
1.	Bank A/c	Dr.		25,00,000	
	Profit & Loss A/c	Dr.		5,00,000	
	To Investments A/c				30,00,000
	(Being investment sold for the purpose of buy-back)				
2.	Bank A/c	Dr.		20,00,000	
	To 12% Preference Share Capital A/c				20,00,000
	(Being 12% Pref. Shares issued for 20,00,000)				
3.	Equity Share Capital A/c	Dr.		50,00,000	
	Premium on buyback	Dr.		25,00,000	
	To Equity Shares buy-back A/c				75,00,000
	(Being Equity Share bought back, Share Capital cancelled, and Premium on Buyback accounted for)				
4.	Securities Premium A/c	Dr.		15,00,000	
	General Reserve A/c	Dr.		10,00,000	
	To Premium on Buyback A/c				25,00,000
	(Being premium on buyback provided out of securities premium)				
5.	Equity Shares buy-back A/c	Dr.		75,00,000	
	To Bank A/c				75,00,000
	(Being payment made to equity shareholders)				
6.	General Reserve Account	Dr.		30,00,000	
	To Capital Redemption Reserve Account				30,00,000
	(Being amount transferred to capital redemption reserve account towards face value of equity shares bought back after deducting nominal value of preference shares redeemed)				

Question 2 *(Inter May 2018) (10 Marks)* *Pg no.____*

Alpha Ltd. furnishes the following summarized Balance Sheet as at 31st March, 2021:

	₹ In Lakhs	₹ In Lakhs
Equity & Liabilities		
Shareholders' Funds		
Equity share capital (fully paid up shares of ₹ 10 each)		2,400
Reserves and Surplus		
Securities Premium	350	
General Reserve	530	
Capital Redemption Reserve	400	
Profit & Loss Account	340	1,620
Non-current Liabilities		
12% Debentures		1,500
Current Liabilities		
Trade Payables'	1,490	
Other Current Liabilities	390	1,880
Total		7,400
Assets		
Non-current Assets		
Property, Plant & Equipment		4,052
Current Assets		
Current Investments	148	
Inventories	1,200	
Trade Receivables	520	
Cash and Bank	1,480	3,348
Total		7,400

(i) On 1st April, 2021, the company announced buy-back of 25% of its equity shares @ ₹ 15 per share. For this purpose, it sold all its investment for ₹ 150 lakhs.

(ii) On 10th April, 2021 the company achieved the target of buy-back.

(iii) On 30th April, 2021, the company issued one fully paid up equity share of ₹ 10 each by way of bonus for every four equity shares held by the equity shareholders by capitalization of Capital Redemption Reserve.

Pass necessary journal entries and prepare the Balance Sheet of Alpha Ltd. after bonus issue.

Solution

Journal Entries in the books of Alpha Ltd. **(Amt. in Lakhs)**

Date	Particulars	L.F.	Dr.	Cr.
April 1	Bank A/c Dr.		150	
	To Investments A/c			148
	To Profit & Loss A/c			2
	(Being investment sold on profit for the purpose of buyback)			
April 10	Equity Share Capital A/c Dr.		600	
	Premium on buyback Dr.		300	
	To Equity Shares buy-back A/c			900
	(Being Equity Share bought back, Share Capital cancelled, and Premium on Buyback accounted for)			
April 10	Securities Premium A/c Dr.		300	
	To Premium on Buyback A/c			300
	(Being premium on buyback provided out of sec.prem.)			

April 10	Equity Shares buy-back A/c Dr.		900	
	To Bank A/c			900
	(Being payment made to equity shareholders)			
April 10	General Reserve Account Dr.		530	
	Profit & Loss Account Dr.		70	
	To Capital Redemption Reserve Account			600
	(Being transfer to CRR towards face value of equity shares)			
April 30	Capital Redemption Reserve A/c Dr.		450	
	To Bonus to Shareholders A/c			450
	(Being the utilization of CRR to issue bonus shares)			
April 30	Bonus to Shareholders A/c Dr.		450	
	To Equity Share Capital A/c			450
	(Being issue of 1 bonus equity share for every 4 shares held)			

Balance Sheet of Alpha Ltd. (after Buyback)

Amount (In Lakhs)

	Note	Amount
A. Equity and Liabilities		
1. Shareholders' Fund		
(a) Share Capital	1	2,250
(b) Reserves & Surplus	2	872
2. Non-current Liabilities		
(a) Long Term Borrowings	3	1,500
3. Current Liabilities		
(a) Trade Payables		1,490
(b) Other Current Liabilities		390
Total		**6,502**
B. Assets		
1. Non-current assets		
(a) Property, Plant & Equipment & Intangible Assets		
(i) Property, Plant & Equipment		4,052
2. Current Assets		
(a) Inventory		1,200
(b) Trade Receivables		520
(c) Cash & Cash Equivalents	4	730
Total		**6,502**

Notes to Accounts

		Amount	Amount
1.	Share Capital		
	225 Lakh Equity shares of ₹ 10 each		2,250
	(Out of above 45 lakh equity shares were issued by way of bonus) (60 lakh equity shares bought back)		
2.	Reserves and Surplus		
	General Reserve (530 – 530)	-	
	CRR (400 + 600 - 450)	550	
	Securities Premium (350 – 300)	50	
	Profit and Loss Account (340 + 2 - 70)	272	872
3.	Long Term borrowings		
	12% Debentures		1,500
4.	Cash & Cash Equivalents		
	Cash at Bank (1,480 + 150 - 900)		730

Question 3 *(Inter Nov 2019) (15 Marks) / (RTP Nov 2021)* *Pg no._____*

X Ltd. furnishes the following summarized Balance Sheet as at 31-03-2021.

	Amount (in ₹)	
Equity & Liabilities		
Share Capital:		
Equity Shares of ₹ 20 each fully paid up	50,00,000	
10,000, 10% Preference Shares of ₹ 100 each fully paid up	10,00,000	60,00,000
Reserves and surplus:		
Capital Reserve	1,00,000	
Securities premium	12,00,000	
Revenue Reserve	5,00,000	
Profit and loss account	20,00,000	
Dividend Equalization Fund	5,50,000	43,50,000
Non-Current Liabilities		
12% Debentures		12,50,000
Current Liabilities and Provisions		5,50,000
		1,21,50,000
Assets		
Non Current Assets		
Property, Plant & Equipment & Intangible Assets		
Property, Plant & Equipment		1,00,75,000
Current assets		
Investment	3,00,000	
Inventory	2,00,000	
Cash & Bank	15,75,000	20,75,000
		1,21,50,000

The shareholders adopted the resolution on the date of above mentioned Balance Sheet to:

(1) Buy back 25% of the paid up capital and it was decided to offer a price of 20% over market price. The prevailing market value of the company's share is ₹ 30 per share.

(2) To finance the buy-back of shares, company:
   (a) Issues 3000, 14% debentures of ₹ 100 each at a premium of 20%.
   (b) Issues 2500, 10% preference shares of ₹ 100 each.

(3) Sell investment worth ₹ 1,00,000 for ₹ 1,50,000.

(4) Maintain a balance of ₹ 2,00,000 in Revenue Reserve.

(5) Later the company issue three fully paid up equity share of ₹ 20 each by way of bonus share for every 15 equity share held by the equity shareholders.

You are required to pass the necessary journal entries to record the above transactions and prepare Balance Sheet after buy back.

Solution

In the books of X Limited
Journal Entries

S.No.	Particulars	L.F.	Debit	Credit
1.	Bank A/c Dr.		3,60,000	
	To 14 % Debenture A/c			3,00,000
	To Securities Premium A/c			60,000
	(Being 14 % debentures issued to finance buy back)			
2.	Bank A/c Dr.		2,50,000	
	To 10% Preference share capital A/c			2,50,000
	(Being 10% preference share issued to finance buy back)			
3.	Bank A/c Dr.		1,50,000	
	To Investment A/c			1,00,000
	To Profit on sale of investment			50,000
	(Being investment sold on profit)			
4.	Equity share capital A/c (62,500 x 20) Dr.		12,50,000	
	Securities premium A/c (62,500 x 16) Dr.		10,00,000	
	To Equity shares buy back A/c (62,500 x 36)			22,50,000
	(Being the amount due to equity shareholders)			
5.	Equity shares buy back A/c Dr.		22,50,000	
	To Bank A/c			22,50,000
	(Being the payment made on account of buy back of 62,500 Equity Shares as per the Companies Act)			
6.	Revenue Reserve Dr.		3,00,000	
	Profit and Loss A/c Dr.		7,00,000	
	To Capital redemption reserve A/c*			10,00,000
	(Being amount equal to nominal value of buy back shares from free reserves transferred to CRR) [12,50,000 less 2,50,000]			
7.	Capital redemption reserve A/c Dr.		7,50,000	
	To Bonus to shareholder A/c (W.N.1)			7,50,000
	(Being the utilization of capital redemption reserve to issue 37,500 bonus shares)			
8.	Bonus to shareholder A/c Dr.		7,50,000	
	To Equity share capital A/c			7,50,000
	(Being issue of 3 bonus equity share for every 15 equity shares held)			

Balance Sheet (After buy back and issue of bonus shares)

Particulars	Notes	Amount
Equity and Liabilities		
1 Shareholders' funds		
Share capital	1	57,50,000
Reserves and Surplus	2	27,10,000
2 Non-Current liabilities		
Long-term borrowings	3	15,50,000
3 Current liabilities		
Trade Payables		-
Current Liabilities & Provisions		5,50,000
Total		**1,05,60,000**

Assets		
1 Non-current assets		
Property, Plant and Equipment & Intangible Asset Property, Plant & Equipment		1,00,75,000
2 Current assets		
Investments		2,00,000
Inventory		2,00,000
Cash and cash equivalent		85,000
Total		**1,05,60,000**

Notes to accounts

			Amount
1	Share Capital		
	Equity share capital (Fully paid up shares of 20 Each) (2,50,000-62,500+37,500 shares) (62,500 equity shares bought back) (37,500 shares issued by way of bonus)		45,00,000
	10% preference shares @ 100 each(10,00,000 + 2,50,000)		12,50,000
			57,50,000
2	Reserves and Surplus		
	Capital Reserve		1,00,000
	Revenue reserve		2,00,000
	Securities premium	12,00,000	
	Add: Premium on debenture	60,000	
	Less: Adjustment for premium paid on buy back	(10,00,000)	2,60,000
	Capital Redemption Reserve		
	Transfer due to buy-back of shares from P&L	10,00,000	
	Less: Utilisation for issue of bonus shares	(7,50,000)	2,50,000
	Profit & Loss A/c	20,00,000	
	Add: Profit on sale of investment	50,000	
	Less: Transfer to CRR	(7,00,000)	13,50,000
	Dividend equalization reserve		5,50,000
			27,10,000
3	Long-term borrowings - 12% Debentures	12,50,000	
	- 14% Debentures	3,00,000	15,50,000

Working Notes:

1. Amount of bonus shares = [(2,50,000 -25%)*3/15] x 20 = 37,500 x 20=7,50,000
2. Cash at bank after issue of bonus shares

Particulars	**Amount**
Cash balance as on 31.3.2021	15,75,000
Add: Issue of debenture	3,60,000
Add: issue of preference shares	2,50,000
Add: Sale of investments	1,50,000
	23,35,000
Less: Buyback of Equity Shares	(22,50,000)
	85,000

Question 4 *(Inter May 2019) (10 Marks)* Pg no.______

Following is the summarized Balance Sheet of Super Ltd. as on 31st March, 2021.

	Amount (in ₹)	
Equity & Liabilities		
Share Capital:		
Equity Shares of ₹ 10 each fully paid up		17,00,000
Reserves and surplus:		
Revenue reserves		23,50,000
Securities premium		2,50,000
Profit and loss account		2,00,000
Infrastructure Development Reserve		1,50,000
Secured Loan		
9% Debentures		22,50,000
Unsecured Loan		8,50,000
Current Maturities of Long term borrowings		15,50,000
		93,00,000
Assets		
Non Current Assets		
Property, Plant & Equipment & Intangible Assets		
Property, Plant & Equipment		58,50,000
Current assets		
Current assets		34,50,000
		93,00,000

Super Limited wants to buy back 35,000 equity shares of ₹ 10 each fully paid up on 1st April, 2021 at ₹ 30 per share. Buy Back of shares is fully authorised by its articles and necessary resolutions have been passed by the company towards this. The payment for buy back of shares will be made by the company out of sufficient bank balance available as part of the Current Assets. Comment with calculations, whether the Buy Back of shares by the company is within the provisions of the Companies Act, 2013

Solution

Determination of Buy back of maximum no. of shares as per the Companies Act, 2013

1. Shares Outstanding Test

Particulars	Shares
Number of shares outstanding	1,70,000
25% of the shares outstanding	42,500

2. Resources Test:

Maximum permitted limit 25% of Equity paid up capital + Free Reserves

Particulars	
Paid up capital (₹)	17,00,000
Free reserves (₹) (23,50,000 + 2,50,000 + 2,00,000)	28,00,000
	45,00,000
25% of Shareholders fund	11,25,000
Buyback Price	₹ 30
Number of shares that can be bought back (shares)	37,500

3. Debt Equity Ratio Test:

Loans cannot be in excess of twice the Equity Funds post Buy Back

Particulars	Amount
Loan funds (₹) (22,50,000+8,50,000+15,50,000)	46,50,000
Minimum equity to be maintained after buy back in the ratio of 2:1 (₹)	23,25,000
Present equity/shareholders fund	45,00,000
Future equity/shareholders fund (₹) (see W.N.) (45,00,000 – 5,43,750)	39,56,250
Maximum permitted buy back of Equity (39,56,250 – 23,25,000)	16,31,250
Maximum number of shares that can be bought back @ ₹ 20 per share	54,375 shares

Summary statement determining the maximum number of shares to be bought back

Particulars	No. of Shares
Shares Outstanding Test	42,500
Resources Test	37,500
Debt Equity Ratio Test	54,375
Maximum number of shares that can be bought back [least of above]	37,500

Company qualifies all tests for buy-back of shares and conclusion is that it can buy maximum 37,500 shares on 1st April, 2021.
However, company wants to buy-back only 35,000 equity shares @ ₹ 30. Therefore, buy-back of 35,000 shares, as desired by the company is within the provisions of the Companies Act, 2013.

Working Note:
Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.
Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.
Then

1. (₹ 45,00,000 – x) – ₹ 23,25,000 = y
2. (y/30)x10 = x
   Or 3x = y

by solving the above equation we get x = ₹ 5,43,750 and y = ₹ 16,31,250

Question 5 *(Inter July 2021) (15 Marks)* Pg no._____

A company provides the following 2 possible Capital Structures as on 31st March, 2021:

Particulars	Situation 1 (₹)	Situation 2 (₹)
Equity Share Capital (Shares of ₹ 10 each, fully paid up)	30,00,000	30,00,000
Reserves & Surplus:		
General Reserve	12,00,000	12,00,000
Securities Premium	6,00,000	6,00,000
Profit & Loss	2,10,000	2,10,000
Statutory Reserve	4,20,000	4,20,000
Loan Funds	25,00,000	1,20,00,000

The company is planning to offer buy back of Equity Share at a price of ₹ 30 per equity share. You are required to calculate maximum permissible number of equity shares that can be bought back in both the situations as per Companies Act, 2013 and are also required to pass necessary Journal Entries in the situation where the buyback is possible.

Solution

Statement determining the maximum number of shares to be bought back

Particulars	When loan fund is	
	₹ 25,00,000	**₹ 1,20,00,000**
Shares Outstanding Test (W.N.1)	75,000	75,000
Resources Test (W.N.2)	41,750	41,750
Debt Equity Ratio Test (W.N.3)	94,000	Nil
Maximum number of shares that can be bought back [least of the above]	41,750	Nil

Journal Entries for the Buy-Back (applicable only when loan fund is ₹ 25,00,000)

	Particulars		Debit	Credit
(a)	Equity shares buy-back account	Dr.	12,52,500	
	To Bank account			12,52,500
	(Being payment for buy-back of 41,750 equity shares of ₹ 10 each @ ₹ 30 per share)			
(b)	Equity share capital account	Dr.	4,17,500	
	Premium on buy-back account	Dr.	8,35,000	
	To Equity share buy-back account			12,52,500
	(Being cancellation of shares bought back)			
(c)	Securities Premium account	Dr.	6,00,000	
	General Reserve / Profit & Loss A/c	Dr.	2,35,000	
	To Premium on buy-back account			8,35,000
	(Being Premium Payable on buy-back account charged to securities premium and general reserve/Profit & Loss A/c)			
(c)	General Reserve*	Dr.	4,17,500	
	To Capital redemption reserve A/c			4,17,500
	(Being transfer of free reserves to CRR to the extent of nominal value of share capital bought back out of redeemed through free reserves)			

*Profit and Loss account balance amounting ₹ 2,10,000 may also be used and General Reserve may be debited for the balance amount.

Working Notes:

1. Shares Outstanding Test

Particulars	(Shares in crores)
Number of shares outstanding	3,00,000
25% of the shares outstanding	75,000

2. Resources Test

Particulars	
Paid up capital (₹)	30,00,000
Free reserves (₹) (12,00,000+6,00,000+2,10,000)	20,10,000
Shareholders' funds (₹)	50,10,000
25% of Shareholders fund (₹)	₹ 12,52,500
Buy-back price per share	₹ 30
Number of shares that can be bought back	41,750 shares

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back

	Particulars	When loan fund is	
(a)	Loan funds (₹)	₹ 25,00,000	₹ 1,20,00,000
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (₹) (a/2)	12,50,000	60,00,000
(c)	Present equity shareholders fund (₹)	50,10,000	50,10,000

Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method. Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y' Then

Equation 1: (Present Equity- Transfer to CRR)- Minimum Equity to be maintained = Maximum Permitted Buy-Back

= (50,10,000 – x) – 12,50,000 = y

= 37,60,000 – x =y (1)

Equation 2: Maximum Permitted Buy-Back X Nominal Value Per Share/Offer Price Per Share

y/30 x 10 = x or

3x = y (2)

by solving the above two equations we get

x = ₹ 9,40,000 and y = ₹28,20,000

In situation 2, first equation will be negative. Buy back not possible in this situation.

Question 6 *(Inter Dec 2021) (10 Marks)* *Pg no._____*

Mohan Ltd. furnishes the following summarised Balance Sheet as on 31st March 2021,

	Amount (₹ in Lakhs)
Equity & Liabilities:	
Shareholder's Fund	
Share Capital	
Equity Shares of 10 each fully paid up	780
6% Redeemable Preference shares of 50 each fully paid up	240
Reserve & Surplus	
Capital Reserve	58
General Reserve	625
Security Premium	52
Profit & Loss	148
Revaluation Reserve	34
Infrastructure Development Reserve	16
Non Current Liabilities	
7% Debentures	268
Unsecured Loans	36
Current Liabilities	395
Total	2652
Assets :	
Non Current Assets	
Plant and Equipment less depreciation	725
Investment at cost	720
Current Assets	1207
Total	2652

Other Information :

a) The Company redeemed Preference shares at a premium of 10% on 1st April, 2021.
b) It is also offered buyback the maximum permissible number of Equity shares of ₹10 each at ₹30 per share an 2nd April, 2021.
c) The payment for the above was made out of available account balance, which appeared as a part of the current assets.
d) The company had investment in own Debentures costing ₹60 lakhs (face value ₹75 lakhs). These Debenture were cancelled on 2nd April, 2021.
e) On 4th April 2021 company issued one fully paid up equity share of ₹10 each by way of bonus for every five equity shares held by the shareholders.

You are required to :

(i) Calculate maximum possible number of equity shares that can be bought back as per the Companies Act, 2013 and
(ii) Record the Journal Entries for the above mentioned information.

<u>Solution</u>

(i) Statement determining the maximum number of shares to be bought back

Number of shares (in lakhs)

Particulars	**When loan fund is ₹ 304 lakhs**
Shares Outstanding Test (W.N.1)	19.5
Resources Test (W.N.2)	11.175
Debt Equity Ratio Test (W.N.3)	29.725
Maximum number of shares that can be bought back [least of the above]	11.175

Thus, the company can buy 11,17,500 Equity shares at ₹ 30 each.

<u>Working Notes:</u>

1. **Shares Outstanding Test**

Particulars	**(Shares in lakh)**
Number of shares outstanding	78
25% of the shares outstanding	19.5

2. **Resources Test**

Particulars	
Paid up capital (₹ in lakh)	780
Free reserves (₹ in lakh) (625+52+148-24-240*)	561
Shareholders' funds (₹ in lakh)	1341
25% of Shareholders fund (₹ in lakh)	335.25
Buy-back price per share	30
Number of shares that can be bought back	11.175

*Amount transferred to CRR is excluded from free reserves. Premium on redemption also reduced.

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back

	Particulars	**₹ In lakh**
(a)	Loan funds (₹)	304
(b)	Minimum equity to be maintained after buy- back in the ratio of 2:1 (₹) (a/2)	152

(c)	Present equity shareholders fund (₹)	1341
(d)	Future equity shareholders fund (₹) (see W.N.4)	1043.75 (1341-297.25)
(e)	Maximum permitted buy-back of Equity (₹) [(d) – (b)]	891.75
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share	29.725
	As per the provisions of the Companies Act, 2013, company	Qualifies

Alternatively, when current liabilities are considered as part of loan funds, in that case Debt Equity Ratio Test will be done as follows:

	Particulars	**₹ in lakh**
(a)	Loan funds (₹)	699
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (₹) (a/2)	349.5
(c)	Present equity shareholders fund (₹)	1341
(d)	Future equity shareholders fund (₹) (see W.N.4)	1093.125 (1341-247.875)
(e)	Maximum permitted buy-back of Equity (₹) [(d) – (b)]	743.625
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share	24.7875
	As per the provisions of the Companies Act, 2013, company	Qualifies

Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method
Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y' Then

Equation 1: (Present Equity- Transfer to CRR) - Minimum Equity to be maintained = Maximum Permitted Buy-Back
= (1341 – x) – 152 = y
= 1189 – x =y(1)
Equation 2: Maximum Permitted Buy-Back x Nominal Value Per Share/Offer Price Per Share
y/30 x 10 = x or 3x = y (2)
by solving the above two equations we get x = ₹ 297.25 and y = ₹ 891.75

Alternatively, when current liabilities are considered as part of loan fund, in that case
Equation 1: (Present Equity- Transfer to CRR)- Minimum Equity to be maintained = Maximum Permitted Buy-Back
= (1341 – x) – 349.5 = y
= 991.5 – x =y (1)
Equation 2: Maximum Permitted Buy-Back X Nominal Value Per Share/Offer Price Per Share
y/30 x 10 = x or 3x = y (2)
by solving the above two equations we get x = 247.875 and y = 743.625

*Loan funds have been taken without considering current liabilities. Alternatively, If current liabilities are considered, then the maximum number of shares that can be bought back as per debt equity ratio test will be 24.7875 lakhs.

(ii) Journal Entries for Buy Back (₹ in lakhs)

Date	Particulars	Debit	Credit
2021 1st April	6% Redeemable preference share capital A/c Dr.	240	
	Premium on redemption of preference shares A/c Dr	24	
	To Preference shareholders A/c		264
	(Being preference share capital transferred to share holders account)		
1st April	Preference shareholders A/c Dr.	264	
	To Bank A/c		264
	(Being payment made to shareholders)		
1st April	General Reserve or P&L A/c* Dr.	24	
	To Premium on redemption of preference shares A/c		24
	(Being premium on redemption of preference shares adjusted through securities premium)		
2nd April	Equity shares buy-back A/c Dr.	335.25	
	To Bank A/c		335.25
	(Being 11.175 lakhs equity shares of ₹ 10 each bought back @ ₹ 30 per share)		
2nd April	Equity share capital A/c Dr.	111.75	
	Securities Premium A/c Dr.	52	
	General Reserve or P&L A/c Dr.	171.50	
	To Equity Shares buy-back A/c		335.25
	(Being cancellation of shares bought back)		
2nd April	General reserve A/c Dr.	351.75	
	To Capital redemption reserve A/c		351.75
	(Being creation of capital redemption reserve account to the extent of the face value of preference shares redeemed and equity shares bought back as per the law ie. 240+111.75 lakhs)		
2nd April	7% Debentures A/c Dr.	75	
	To Investment (own debentures) A/c		60
	To Profit on cancellation of own debentures A/c		15
	(Being cancellation of own debentures costing ₹ 60 lakhs, face value being ₹ 75 lakhs and the balance being profit on cancellation of debentures)		
4th April	Capital Redemption Reserve Dr.	133.65	
	To Bonus Shares A/c		133.65
	(Being issue of one bonus equity share for every five equity shares held)		
4th April	Bonus shares A/c Dr. Dr.	133.65	
	To Equity share capital A/c		133.65
	(Being bonus shares issued)		

Working Note: Bonus Share to be issued =66.825 (78 - 11.175) lakh shares divided by 5 = 13.365 lakh shares.

Note: *Securities premium has not been utilized for the purpose of premium payable on redemption of preference shares assuming that the company referred in the question is governed by Section 133 of the Companies Act, 2013 and complies with the Accounting Standards prescribed for them. Alternative entry considering otherwise is also possible by utilizing securities premium amount.

Bonus Issue (Sec 63)

(Issuing shares free of cost to existing shareholders)

(Fully paid Bonus shares to be given to fully paid existing shareholders)

I

~~Bonus~~ Reserves & surplus A/c - Dr
To share capital

II

* Reserves & surplus A/c - Dr
To Bonus to shareholders A/c

&

Bonus to shareholders A/c - Dr
To share capital

* **Reserves & surplus :**

✓ 1) CRR

✓ 2) Securities Premium

✓ 3) Free Reserve (General Res. / P&L A/c)

Redemption of Preference Shares (Sec 55)

Due

1) Preference Share capital A/c - Dr
Premium on Redemption A/c - Dr
To Preference shareholders A/c

Payment

2) Preference shareholders A/c - Dr
To Bank A/c

Write off

3) * Securities Premium A/c - Dr
P&L A/c / General Res. A/c - Dr
To Premium on Redemption A/c

Tfr. to CRR

4) General Res. / P&L A/c - Dr
To CRR A/c

→ Securities Premium cannot be used as per law.

Face value of Pref. Shares redeemed	xx
- Face value of Shares issued	(xx)
	xx

* For Entry No. 3: Write off of Premium on Redemption

<u>Case 1:</u> If Prescribed co. of Financial Statements comply with AS u/s 133.

Securities Premium cannot be used

Use General Res./ P&L A/c

<u>Case 2:</u> Other than Case 1

Securities Premium can be used.

INTERNAL RECONSTRUCTION

> *"Don't downgrade your dream just to fit your reality. Upgrade your conviction to match your destiny."*

TOPIC1: INTRODUCTION

When a company has been making losses for several years, the financial position does not present a true & fair view of the state of the affairs of the company. In such a company the assets are generally overvalued, as the balance sheet consists of fictitious assets, unrepresented intangible assets & debit balance in profit & loss account.

Reconstruction is a process by which affairs of a company are reorganized by revaluation of assets, reassessment of liabilities and by writing off the losses already suffered by reducing the paid up value of shares and/or varying the rights attached to different classes of shares. Such a process is called internal reconstruction which is carried out without liquidating the company and forming a new one.

Process of Internal Reconstruction

1) Scheme Framed
2) Approval of scheme by concerned parties
3) Sanction of scheme by Court
4) Implementation of scheme
   * Passing Entries in Books
   * Writing off Losses
   * Revised values to appear in B/S

TOPIC 1A: JOURNAL ENTRIES

1.	For increase or reduction in value of assets	
	a) Increase	Asset A/c Dr. To Capital Reduction A/c
	b) Decrease	Capital Reduction A/c Dr. To Asset A/c
2.	For increase or reduction in liabilities:	
	a) Increase	Capital Reduction A/c Dr. To Liability A/c
	b) Decrease	Liability A/c Dr. To Capital Reduction A/c
3.	For payment of reconstruction expenses	
	a) At the time of payment	Capital Reduction A/c Dr. To Bank A/c
4.	Settlement of contingent liability *Example*: Preference dividend in arrears, Capital commitments, etc.	
	a) If waived	No Entry
	b) If paid	Capital Reduction A/c Dr. To Bank A/c To Share Capital A/c
5.	If any losses or deferred revenue expenditure are appearing then such amount should be written off even if question is silent. *Example of deferred revenue expenditure*: Underwriting commission, Discount on issue of debentures, Preliminary expenses, Advertisement suspense, etc.	
	a) At the time of write off	Capital Reduction A/c Dr. To P&L A/c To Deferred Revenue Expenditure A/c
6.	If any intangible assets appear in the balance sheet it may be written off by giving a note. *Example*: Patents, Trademarks, Goodwill, Copyrights etc.	
	a) At the time of write off	Capital Reduction A/c Dr. To Intangible Asset A/c
7.	Closing of Capital Reduction Account	
	a) Credit Balance	Capital Reduction A/c Dr. To Capital Reserve A/c
	b) Debit Balance	Capital Reserve A/c Dr. Securities Premium A/c Dr. General Reserve A/c Dr. To Capital Reduction A/c

Notes:

1) In case of fixed assets, the amount written off under the scheme of reconstruction must be shown for 5 years.
2) After the name of company, the words “and reduced” should be added only if the court so orders.

TOPIC 2: METHODS OF INTERNAL RECONSTRUCTION

Methods of Internal Reconstruction:

Alteration of share capital	Variation of shareholder's rights	Compromise/ arrangement	Reduction of share capital	Surrenders of shares

TOPIC 2A: Alteration of Share Capital, Variation of Shareholder Rights, Compromise/Arrangements & Reduction of Share Capital

ALTERATION OF SHARE CAPITAL

1. For Increase in Share Capital

Example:

X Ltd. issued 10,000 equity shares of ₹10 each at par.	Bank A/c Dr. 1,00,000 To Equity Share Capital A/c 1,00,000

2. For Consolidation of Shares

Example:

X Ltd. having 10,000 equity shares of ₹10 each decides to convert share capital into equity shares of 100 each.	Equity Share Capital A/c (10) Dr. 1,00,000 To Equity Share Capital A/c (100) 1,00,000 (10,000 x 10 = 1,000 x 100)

3. For Sub-division of Shares

Example:

X Ltd. having 1,000 equity shares of ₹100 each decides to convert share capital into equity shares of 10 each.	Equity Share Capital A/c (100) Dr. 1,00,000 To Equity Share Capital A/c (10) 1,00,000 (1,000 x 100 = 10,000 x 10)

4. For Conversion of shares into stock

Stock is a bundle of fully paid shares put together for convenience so that it may be divided into any amount & transferred into any fractions & subdivisions without regard to the original face value of the shares.

Example:

X Ltd. having 10,000 equity shares of 10 each decides to convert the share capital into equity stock	Equity Share Capital A/c Dr. 1,00,000 To Equity Stock A/c 1,00,000

5. For Conversion of stock into shares

Example:

X Ltd. having equity stock of ₹1,00,000 decides to convert the equity stock into equity share capital of ₹ 10 each.	Equity Stock A/c Dr. 1,00,000 To Equity Share Capital A/c 1,00,000

6. For Cancelling the unissued shares

   In this case no accounting entry is passed. The authorized share capital gets reduced by the amount of unissued shares now cancelled.

VARIATION OF SHAREHOLDERS RIGHTS

Only the specific rights are changed. There is no change in the amount of capital. For example, the company may change rate of (a) dividend on preference shares or (b) convert cumulative preference shares into non-cumulative preference shares without changing the amount of share capital.

Example:

X Ltd. has 1,000 10% preference shares of 100 each. At a meeting of preference shareholders, it was decided that the rate of dividend be reduced to 9%.	10% Preference Share Capital A/c Dr. 1,00,000 To 9% Preference Share Capital A/c 1,00,000

COMPROMISE/ARRANGEMENT

A scheme of compromise and arrangement is an agreement between a company and its members and outside liabilities when the company faces financial problems. Such an arrangement therefore also involves sacrifices by shareholders, or creditors and debenture holders or by all.

Example:

In the balance sheet, sundry creditors are appearing at ₹ 4,50,000. They agreed to reduce their claims to 20% and half the balance to be satisfied by issue of equity shares of ₹10 each.	Creditors A/c Dr. 3,60,000 To Capital Reduction A/c 3,60,000 Creditors A/c Dr. 45,000 To Equity Share Capital A/c 45,000

REDUCTION OF SHARE CAPITAL

a) Liability of the shareholders is extinguished or reduced in respect of unpaid amount on the shares held by them.

Number of Shares = 10,000
Face Value = 10
Paid up Value = 8
Reduce 10 per share into 8 per share fully paid up
So Cancel the unpaid amount of 2 per share

Equity Share Capital A/c (10) Dr.	80,000	
To Equity Share Capital A/c (8)		80,000

b) Paying off excess paid-up share capital

Number of Shares = 10,000
Face & Paid up Value = 10
Pay off 2 per share to make it 8 per share fully paid up

Equity Share Capital A/c (10) Dr.	1,00,000	
To Equity Share Capital A/c (8)		80,000
To Bank A/c		20,000

c) Writing off the lost paid up capital

Number of shares = 1,000
Face Value = 100
Paid up Value = 100

	(a)	(b)
Write off	80	80
Face Value	20	100
Paid up	20	20

		Dr.	Cr.
(a)	Equity Share Capital A/c (100) Dr.	1,00,000	
	To Equity Share Capital A/c (20)		20,000
	To Capital Reduction A/c		80,000
(b)	Equity Share Capital A/c Dr.	80,000	
	To Capital Reduction A/c		80,000

__Note__: If question does not specify reduction in Face value or paid up value, then assume change in Face value and paid up value.

TOPIC 2B: SHARE SURRENDER

At the time of internal reconstruction, some people may voluntarily surrender their shares to the company. Alternatively, there can be concept of compulsorily surrender in the reconstruction scheme.

__Entries:__

At the time of surrender	Equity Share Capital A/c Dr. To Share Surrender A/c
If the surrendered shares are cancelled	Share Surrender A/c Dr. To Capital Reduction A/c
If the surrendered shares are utilized for the payment of an obligation	Share Surrender A/c Dr. To Share Capital A/c Liability A/c Dr. To Capital Reduction A/c

Question 1 *(IPCC May 2018) (4 Marks)* Pg no._____

Pass Journal Entries in the following conditions:

1) Super Ltd. had 62,000 equity shares of ₹ 50 each on which ₹ 45 is paid up. In September, 2020 company decided to sub-divide each share into 5 shares of ₹ 10 with ₹ 9 paid up.
2) Top Ltd. had 1,05,000 equity shares of ₹ 10 each fully paid up. In November 2019 company decided to convert the issued shares into stock. But in January 2020 the company re-converted the stock into equity shares of ₹ 100 each fully paid up.
3) New Ltd. had capital of ₹ 15,00,000 divided into 1,50,000 equity shares of ₹ 10 each on which ₹ 6 is paid up. During the year, company decided to reorganize its capital by consolidating 5 shares into one share of ₹ 50 each, ₹ 30 paid up.

Solution

Journal Entries

	Particulars	Debit (₹)	Credit (₹)
Sep 2020 Super Ltd.	Equity Share Capital A/c (₹ 50) Dr.	27,90,000	
	To Equity Share Capital A/c (₹10)		27,90,000
	(Being subdivision of 62,000 equity shares of ₹ 50 (₹ 45 paid up) each into 3,10,000 shares of ₹ 10 each (₹ 9 paid up) as per resolution dated…)		
Nov 2019 Top Ltd.	Equity Share Capital A/c (₹10) Dr.	10,50,000	
	To Equity Stock A/c		10,50,000
	(Being conversion of 1,05,000 lakh equity shares of ₹ 10 each into stock of 10,50,000 as per resolution dated…)		
Jan 2020 Top Ltd.	Equity Stock A/c Dr.	10,50,000	
	To Equity Share Capital A/c (₹100)		10,50,000
	(Being conversion of 10,50,000 stock into 10,500 equity shares of ₹ 100 each)		
New Ltd.	Equity Share Capital A/c (₹10) Dr.	9,00,000	
	To Equity Share Capital A/c (₹50)		9,00,000
	(Being consolidation of 1,50,000 shares of ₹ 10, ₹ 6 paid up each into 30,000 shares of ₹ 50 each (₹ 30 paid up) as per resolution dated…)		

Question 2 *(Inter July 2021) (5 Marks)* Pg no._____

Sapra Limited has laid down the following terms upon the sanction of reconstruction scheme by court.

(i) The shareholders to receive in lieu of their present holding at 7,50,000 shares of ₹10 each, the following:
  a. New fully paid ₹ 10 Equity Shares equal to 3/5th of their holding.
  b. Fully paid ₹ 10, 6% Preference Shares to the extent of 2/5th of the above new equity shares.
  c. 7% Debentures of ₹ 250,000.

(ii) Goodwill which stood at ₹ 2,70,000 is to be completely written off.

(iii) Plant & Machinery to be reduced by ₹ 1,00,000, Furniture to be reduced by ₹ 88,000 and Building to be appreciated by ₹ 1,50,000.

(iv) Investment of ₹ 6,00,000 to be brought down to its existing market price of ₹ 1,80,000.

(v) Write off Profit & Loss Account debit balance of ₹ 2,25,000.

In case of any shortfall, the balance of General Reserve of ₹ 42,000 can be utilized to write off the losses under reconstruction scheme.

You are required to show the necessary Journal Entries in the books of Sapra Limited of the above reconstruction scheme considering that balance in General Reserve is utilized to write off the losses.

Solution

Journal Entries

		₹	₹
Equity Share Capital (old) A/c	Dr.	75,00,000	
To Equity Share Capital (₹ 10) A/c			45,00,000
To 6% Preference Share Capital (₹ 10) A/c			18,00,000
To 7% Debentures A/c			2,50,000
To Capital Reduction A/c			9,50,000
(Being new equity shares, 6% Preference Shares, 7% Debentures issued and the balance transferred to Capital reduction account as per the Scheme)			
Building A/c	Dr.	1,50,000	
To Capital Reduction A/c			1,50,000
(Beig value of Building appreciated)			
Capital Reduction A/c	Dr.	11,03,000	
To Goodwill Account			2,70,000
To Plant and Machinery Account			1,00,000
To Furniture Account			88,000
To Investment A/c			4,20,000
To Profit & Loss A/c			2,25,000
(Being Capital Reduction utilized for writing off of Goodwill, Plant & Machinery, furniture, investment and Profit & Loss)			
General reserve A/c	Dr.	3,000	
To Capital Reduction A/c			3,000
(Being general reserve utilized to write off the balance in Capital reduction A/c)			

Question 3

Pg no.______

The Balance Sheet of Suresh Ltd. as on 31-03-2023 is given below:

Liabilities	₹	Assets	₹
80,000, Equity shares of Rs.10 each fully paid	8,00,000	Freehold property	5,00,000
5,000, 6% Cumulative preference shares of Rs.100 each fully paid	5,00,000	Plant and machinery	5,80,000
6% Debentures 3,75,000 (secured by freehold property)		Trade investment (at cost)	1,70,000
Arrear interest 22,500	3,97,500	Sundry debtors	4,50,000
Sundry creditors	17,500	Stock-in trade	2,00,000
Director's loan (Mr. A)	3,00,000	Deferred Revenue Expenditure	1,50,000
Director's loan (Mr. B)	2,00,000	Profit & Loss Account	3,65,000
Provision for Income Tax	2,00,000		
	24,15,000		24,15,000

The Court approved a scheme of re-organisation to take effect on 1.4.2023 & terms are given below:

a) Preference shares are to be written down to ₹ 75 each and equity shares to ₹ 2 each.
b) Preference dividend in arrear for 4 years to be waived by 75% and for the balance equity shares of ₹ 2 each to be allotted.
c) Arrear of debenture interest to be paid in cash.
d) Debentureholders agreed to take one freehold property (Book value ₹ 2,80,000) at a valuation of ₹ 3,00,000 in part payment of their holding. Rate of interest of balance debentures increased to 8%.
e) Remaining freehold property (after takeover by debentureholders) to be valued at 3,50,000.
f) Investment sold out for ₹ 2,00,000.
g) 80% of A's Director's loan to be waived & for balance, equity shares of ₹ 2 each to be issued.
h) The Income Tax Liability of the company is settled at ₹ 3,20,000. Provision for Income Tax will be raised accordingly.
i) 1/5 of creditors decided to forgo their claim & the balance creditors are allotted equity shares of ₹ 2 each in full settlement of their claim.
j) Contingent Liability of ₹ 2,00,000 is payable which has been created by wrong action of Director Mr. B. He has agreed to compensate this loss out of the loan given by the Director to the Company.
k) The Directors refund ₹ 50,000 of the fees previously received by them.
l) Company's contractual commitments amounting to ₹ 5,00,000 to be cancelled by paying penalty at 3% of contract value.
m) 50,000 new Equity Shares of ₹ 2 each are to be issued at par payable in full on application. The issue was underwritten for a commission of 4%. Shares were fully taken up.
n) Total expenses incurred by the Company in connection with the Scheme excluding underwriting Commission amounted to ₹ 20,000.
o) Deferred advertisement expenditure to be written off.
p) Stock value to be written off fully in the books.
q) 20% of the Sundry Debtors to be written off as bad debt.

Show the Journal entries to be passed for giving effect to the above transactions.

Solution

Journal Entries in the books of Suresh Limited

	Particulars	L.F.	Dr. (₹)	Cr. (₹)
1	6% Preference share capital A/c (₹100) Dr.		5,00,000	
	To 6% Preference share capital A/c (₹ 75)			3,75,000
	To Capital reduction A/c			1,25,000
	(Reduction of preference share of ₹100 each to shares of ₹ 75 each as per the reconstruction scheme)			
2	Equity share capital A/c (₹ 10) Dr.		8,00,000	
	To Equity share capital A/c (₹ 2)			1,60,000
	To Capital reduction A/c			6,40,000
	(Reduction of equity share of ₹ 10 each to shares of ₹ 2 each as per the reconstruction scheme)			
3	Capital reduction A/c Dr.		30,000	
	To Equity share capital A/c (₹ 2 each)			30,000
	(Being 1/4th arrears of preference share dividend of 4 years to be satisfied by issue of 15,000 lakhs equity shares of ₹ 2 each)			
4	Accrued debenture interest A/c Dr.		22,500	
	To Bank A/c			22,500
	(Being debenture interest paid)			

5	6% Debentures A/c Dr.		3,00,000	
	To Freehold property A/c			2,80,000
	To Capital Reduction A/c			20,000
	(Being claim of Debenture holders settled in part by transfer of freehold property)			
6	6% Debentures A/c Dr.		75,000	
	To 8% Debentures A/c			75,000
	(Being rate of balance debentures increased to 8%)			
7	Freehold property A/c Dr.		1,30,000	
	To Capital Reduction A/c			1,30,000
	(Being appreciation in the value of freehold property)			
8	Bank A/c Dr.		2,00,000	
	To Investments A/c			1,70,000
	To Capital Reduction A/c			30,000
	(Being investment sold at profit)			
9	Director's loan A/c Dr.		3,00,000	
	To Equity share capital A/c (₹ 2 each)			60,000
	To Capital Reduction A/c			2,40,000
	(Being director's loan waived by 80% and balance being discharged by issue of 30,000 equity shares of ₹ 2 each)			
10	Capital Reduction A/c Dr.		1,20,000	
	To Provision for Tax A/c			1,20,000
	(Being provision for tax increased)			
11.	Creditors A/c Dr.		17,500	
	To Capital Reduction A/c			3,500
	To Equity Share Capital A/c			14,000
	(1/5 of creditors decided to forgo their claim & balance allotted shares)			
12	Loan from Director A/c Dr.		2,00,000	
	To Provision for contingent liability A/c			2,00,000
	(Being contingent liability of ₹ 2,00,000 is payable and adjusted against loan from Director A/c)			
13	Bank A/c Dr.		50,000	
	To Capital Reduction A/c			50,000
	(Being fees refunded by directors)			
14	Capital Reduction A/c Dr.		15,000	
	To Bank A/c			15,000
	(Being penalty for capital commitments paid 5,00,000*3%)			
15	Bank A/c Dr.		1,00,000	
	To Equity share application & Allotment A/c			1,00,000
	(Being application money received on 50,000 Equity share @ ₹ 2 each)			
16	Equity share application & allotment A/c Dr.		1,00,000	
	To Equity share capital A/c			1,00,000
	(Being application money transferred to capital A/c)			
17	Underwriting Commission A/c Dr.		4,000	
	To Bank A/c			4,000
	(Being underwriting commission paid)			
18	Capital Reduction A/c Dr.		20,000	
	To Bank A/c			20,000
	(Being payment of expenses on reconstruction)			

19	Capital Reduction A/c Dr.		8,09,000	
	To Deferred Revenue Expenditure A/c			1,50,000
	To Stock A/c			2,00,000
	To Debtors A/c			90,000
	To Underwriting Commission A/c			4,000
	To Profit & Loss A/c			3,65,000
	(Written off deferred revenue exp., loss, stock, debtors, and underwriting commission written off)			
20	Capital Reduction A/c Dr.		2,44,500	
	To Capital Reserve A/c			2,44,500
	(Being balance transferred to capital reserve)			

Capital Reduction Account

	Amount		Amount
To Equity share capital	30,000	By 6% Preference share capital	1,25,000
To Provision for Tax	1,20,000	By Equity share capital	6,40,000
To Bank A/c	15,000	By 6% Debentures	20,000
To Bank A/c	20,000	By Freehold Property	1,30,000
To Deferred Revenue Exp.	1,50,000	By Bank	30,000
To Stock	2,00,000	By Director's Loan	2,40,000
To Sundry Debtors	90,000	By Creditors	3,500
To Underwriting Commission	4,000	By Bank	50,000
To Profit & Loss A/c	3,65,000		
To Capital Reserve (Bal.Fig.)	2,44,500		
	12,38,500		**12,38,500**

Question 4 *(Inter Nov 2019) (15 Marks) / (RTP May 2023)* **Pg no._____**

Following is the summarized Balance Sheet of Fortunate Ltd. as on 31st March, 2023.

Particulars	Amount
Liabilities	
Authorized and Issued Share Capital	
(a) 15,000 8% Preference shares of ₹ 50 each	7,50,000
(b) 18,750 Equity shares of ₹ 50 each	9,37,500
Profit and Loss Account	(5,63,750)
Loan	7,16,250
Trade Payables	2,58,750
Other Liabilities	43,750
Total	21,42,500
Assets	
Building at cost less depreciation	5,00,000
Plant at cost less depreciation	3,35,000
Trademarks and goodwill at cost	3,97,500
Inventory	5,00,000
Trade Receivables	4,10,000
Total	21,42,500

(Note: Preference shares dividend is in arrear for last five years).

The Company is running with the shortage of working capital and not earnings profits. A scheme of reconstruction has been approved by both the classes of shareholders. The summarized scheme of reconstruction is as follows:

(i) The equity shareholders have agreed that their ₹ 50 shares should be reduced to ₹ 5 by cancellation of ₹ 45.00 per share. They have also agreed to subscribe for three new equity shares of ₹ 5.00 each for each equity share held.

(ii) The preference shareholders have agreed to forego the arrears of dividends and to accept for each ₹ 50 preference share, 4 new 6% preference shares of ₹ 10 each, plus 3 new equity shares of ₹ 5.00 each, all credited as fully paid.

(iii) Lenders to the company for ₹ 1,87,500 have agreed to convert their loan into shares and for this purpose they will be allotted 15,000 new preference shares of ₹ 10 each and 7,500 new equity shares of ₹ 5.00 each.

(iv) The directors have agreed to subscribe in cash for 25,000 new equity shares of ₹ 5.00 each in addition to any shares to be subscribed by them under (i) above.

(v) Of the cash received by the issue of new shares, ₹ 2,50,000 is to be used to reduce the loan due by the company.

(vi) The equity share capital cancelled is to be applied:
   a. To write off the debit balance in the Profit and Loss A/c, and
   b. To write off ₹ 43,750 from the value of plant.

Any balance remaining is to be used to write down the value of trademarks and goodwill. The nominal capital, as reduced, is to be increased to ₹ 8,12,500 for preference share capital and ₹ 9,37,500 for equity share capital.

You are required to pass journal entries to show the effect of above scheme and prepare the Balance Sheet of the Company after reconstruction.

Solution

Journal Entries in the books of Fortunate Ltd

S.No.	Particulars	L.F	Debit	Credit
1.	Equity share capital A/c (₹50) Dr.		9,37,500	
	To Equity share capital A/c (₹5)			93,750
	To Capital reduction A/c*			8,43,750
	(Being equity cap. reduced to nominal value of ₹5 each)			
2.	Bank A/c Dr.		2,81,250	
	To Equity share capital			2,81,250
	(Being 3 right shares against each share was issued and subscribed)			
3.	8% Preference share capital A/c (₹50) Dr.		7,50,000	
	Capital reduction A/c Dr.		75,000	
	To 6% Preference share capital (₹10)			6,00,000
	To Equity share capital (₹5)			2,25,000
	(Being 8% preference shares of ₹50 each converted to 6% preference shares of ₹10 each and also given to them 3 equity shares for every share held)			
4.	Loan A/c Dr.		1,87,500	
	To 6% Preference share capital A/c(15,000 x ₹10)			1,50,000
	To Equity share capital A/c (7,500 x ₹5)			37,500
	(Being loan of 1,50,000 converted into share capital)			
5.	Bank A/c (25,000 x ₹5) Dr.		1,25,000	
	To Equity share application A/c			1,25,000
	(Being shares subscribed by the directors)			

6.	Equity share application A/c Dr.		1,25,000	
	To Equity share capital A/c			1,25,000
	(Being application money transferred to capital A/c)			
7.	Loan A/c Dr.		2,50,000	
	To Bank A/c			2,50,000
	(Being loan repaid)			
8.	Capital reduction A/c		7,68,750	
	To Profit and loss A/c			5,63,750
	To Plant A/c			43,750
	To Trademarks and Goodwill A/c (Bal. fig.)			1,61,250
	(Being losses & assets written off to the extent required)			

Balance sheet of Fortunate Ltd. (and reduced) as on 31.3.2023

Particulars	Notes	Amount
Equity and Liabilities		
1 Shareholders' funds		
a) Share capital	1	15,12,500
2 Non-current liabilities		
a) Long-term borrowings (7,16,250 – 1,87,500 – 2,50,000)		2,78,750
3 Current liabilities		
a) Trade Payables		2,58,750
b) Other current liabilities		43,750
Total		**20,93,750**
Assets		
1 Non-current assets		
a) PPE & Intangible Assets		
(i) Property, Plant & Equipment	2	7,91,250
(ii) Intangible Asset	3	2,36,250
2 Current assets		
a) Inventories		5,00,000
b) Trade receivables		4,10,000
c) Cash and cash equivalent	4	1,56,250
Total		**20,93,750**

Notes to Accounts

	Amount
1 Share Capital	
Authorized capital:	
81,250 Preference shares of ₹10 each	8,12,500
1,87,500 Equity shares of ₹5 each	9,37,500
Issued, subscribed and paid up:	
1,52,500 equity shares of ₹5 each (Out of above 7,500 equity shares issued for consideration other than cash)	7,62,500
75,000, 6% Preference shares of ₹10 each (Out of above 15,000 preference shares issued for consideration other than cash)	7,50,000
	15,12,500

2. **Property, Plant & Equipment**		
Building at cost less depreciation		5,00,000
Plant at cost less depreciation	3,35,000	
Less: Written off under scheme of reconstruction	(43,750)	2,91,250
		7,91,250
3. **Intangible assets**		
Trademarks and goodwill	3,97,500	
Less: Written off under scheme of reconstruction	(1,61,250)	2,36,250
4. **Cash and cash equivalents**		
Bank (2,81,250+1,25,000-2,50,000)		1,56,250

Note: *In place of Capital Reduction Account, Reconstruction Account may also be used.

SPECIAL CASES

Case 1:

Equity Share Capital Appearing in Balance Sheet = 60,00,000
(1,20,000 shares of ₹ 50 each)
Question mentions that:
The equity shareholders agreed to receive in lieu of their present holding of 1,20,000 shares of ₹ 50 each as under:

1. New fully paid equity shares of ₹ 10 each equal to 2/3rd of their holding.
2. 9% preference shares of ₹ 8 each to the extent of 25% of the above new equity share capital.
3. ₹ 6,00,000, 12% debentures of ₹ 80 each.

Solution

Journal Entries

		Dr.	Cr.
(i)	Equity share capital A/c Dr.		
	To Equity share capital A/c		
	To 9% preference share capital A/c		
	To 12% debentures A/c		
	To Capital Reduction A/c		
	(Being payment made in lieu of equity share capital of ₹50 each by issue of equity shares of ₹10 each, 9% Preference share capital &12% debentures as per reconstruction scheme)		

Case 2:

Balance Sheet (Extract)

Liabilities	₹
Share Capital	
50,000 shares of ₹ 50 each fully paid up	25,00,000
1,00,000 shares of ₹ 50 each, ₹ 40 paid up	40,00,000
8% Debentures of ₹ 100 each	4,00,000
12% Debentures of ₹ 100 each	6,00,000
O/s Debenture Interest (1 year)	1,04,000
Trade Creditors	10,00,000

The following scheme of internal reconstruction was framed and implemented, as approved by the court and concerned parties:

Following is the interest of Mr. Ravi and Mr. Suresh:

	Mr. Ravi	Mr. Suresh
8% Debentures	3,00,000	1,00,000
12% Debentures	4,00,000	2,00,000
Trade Creditors	1,00,000	2,00,000
	8,00,000	5,00,000
Fully paid up ₹ 50 shares	4,00,000	3,00,000
Partly paid up shares (₹ 40 paid up)	5,00,000	2,00,000

(1) Uncalled capital is to be called up in full and then all the shares to be converted into Equity Shares of ₹ 20 each.

(2) Mr. Ravi is to cancel ₹ 5,00,000 of his total debt including O/s interest (other than equity shares) and to pay ₹ 2 lakhs to the company and to receive new 10% First Debentures for the balance amount.

(3) Mr. Suresh is to cancel ₹ 3,00,000 of his total debt including O/s interest (other than equity shares) and to accept new 14% First Debentures for the balance.

(4) Trade Creditors (other than Ravi & Suresh) are given option of either to accept fully paid equity shares of ₹ 20 each for the amount due to them or to accept 70% of the amount due to them in cash in full settlement of their claim. Trade Creditors for ₹ 5,00,000 accept equity shares & rest of them opted for cash towards full and final settlement of their claim.

Solution

Journal Entries

		L.F.	Dr. (₹)	Cr. (₹)
1a	Bank A/c (1,00,000 x ₹10) Dr.		10,00,000	
	To Equity share capital A/c			10,00,000
1b	Equity share capital (₹50) A/c Dr.		75,00,000	
	To Equity share capital (₹20) A/c			30,00,000
	To Capital Reduction A/c			45,00,000
2a	8% Debentures A/c Dr.		3,00,000	
	12% Debentures A/c Dr.		4,00,000	
	O/s Debenture Interest A/c Dr.		72,000	
	Trade Creditors A/c Dr.		1,00,000	
	To Ravi A/c			8,72,000
2b	Ravi A/c Dr.		5,00,000	
	To Capital Reduction A/c			5,00,000
2c	Bank A/c Dr.		2,00,000	
	To Ravi A/c			2,00,000
2d	Ravi A/c Dr.		5,72,000	
	To 10% Debentures A/c			5,72,000
3a	8% Debentures A/c Dr.		1,00,000	
	12% Debentures A/c Dr.		2,00,000	
	O/s Debenture Interest A/c Dr.		32,000	
	Trade Creditors A/c Dr.		2,00,000	
	To Suresh A/c			5,32,000
3b	Suresh A/c Dr.		5,32,000	
	To Capital Reduction A/c			3,00,000
	To 14% Debentures A/c			2,32,000
4	Trade payables A/c Dr.		7,00,000	
	To Equity share capital A/c			5,00,000
	To Bank A/c (2,00,000 x 70%)			1,40,000
	To Capital Reduction A/c			60,000

Case 3:

6% Preference Share Capital Appearing in Balance Sheet = 6,00,000
Question mentions that:
The preference shares are converted from 6% to 8% but revalued in a manner in which the total return on them remains unaffected.

Solution

Journal Entry

	Particulars		Debit	Credit
			(₹)	(₹)
1.	6% Preference share capital A/c	Dr.	6,00,000	
	To 8% Preference share capital A/c			4,50,000
	To Capital reduction A/c			1,50,000
	(Being 6% preference shares converted to 8% preference shares so that return to pref. shareholders remains unaffected)			

Calculation of new Preference Shares

Rate of return	6% on Preference Shares	
Dividend :	(6/100) x ₹ 6,00,000	₹ 36,000
Rate of return:	8% on Preference Shares	
Dividend :	(8/100) x X	₹ 36,000
	X = (36,000/8) x 100	₹ 4,50,000
New Preference Share Capital		₹ 4,50,000
Old Preference Share Capital		₹ 6,00,000
(6,00,000 – 4,50,000)		₹ 1,50,000 Amount taken to Capital Reduction A/c.

Question 5

Pg no._____

The summarised Balance Sheet of Preet Limited as on 31st March 2023, was as follows:

Liabilities	₹	Assets	₹
Authorised and subscribed capital:		Property, Plant & Equipment:	
20,000 Equity shares of ₹ 100 each	20,00,000	Machineries	7,00,000
Unsecured loan:		Current Assets:	
15% Debentures	6,00,000	Inventory	5,06,000
Accrued interest	90,000	Trade Receivables	4,60,000
Current Liabilities:		Bank	40,000
Trade Payables	1,04,000	Profit & loss A/c	11,60,000
Provision for income tax	72,000		
	28,66,000		28,66,000

It was decided to reconstruct the company for which necessary resolution was passed and sanctions were obtained from the appropriate authorities. Accordingly, it was decided that:

a) Each share be sub-divided into 10 fully paid up equity share of ₹ 10 each.

b) After sub-division, each shareholder shall surrender to the company 50% of his holding for the purpose of reissue to debentureholders and trade payables as necessary.

c) Out of shares surrendered 20,000 shares of ₹ 10 each shall be converted into 10% Preference shares of ₹ 10 each fully paid up.

d) The claims of debentureholders shall be reduced by 50%. In consideration of the reduction, the debenture-holder shall receive Preference Shares of ₹ 2,00,000 which are converted out of shares surrendered.

e) Trade Payables claim shall be reduced by 25%. Remaining Trade Payables are to be settled by the issue of equity shares of ₹ 10 each of out of shares surrendered.

f) Balance of Profit and Loss account to be written off.

g) The shares surrendered and not re-issued shall be cancelled.

Pass Journal Entries giving effect to the above and the resultant Balance Sheet.

Solution

Journal Entries in the books of Preet Limited

			₹	₹
(i)	Equity Share capital (₹100) A/c Dr.		20,00,000	
	To Equity share capital (₹10) A/c			20,00,000
(ii)	Equity Share capital (₹10) A/c Dr.		10,00,000	
	To Share surrender A/c			10,00,000
(iii)	15% Debentures A/c Dr.		3,00,000	
	Accrued interest A/c Dr.		45,000	
	To Capital Reduction A/c			3,45,000
(iv)	Share Surrender A/c Dr.		2,00,000	
	To 10% Preference share capital A/c			2,00,000
(v)	Trade Payables A/c Dr.		1,04,000	
	To Capital Reduction A/c			1,04,000
(vi)	Share Surrender A/c Dr.		78,000	
	To Equity share capital A/c			78,000

(vii)	Share Surrender A/c	Dr.		7,22,000	
	To Capital Reduction A/c				7,22,000
(viii)	Capital Reduction A/c	Dr.		11,71,000	
	To Profit & Loss A/c				11,60,000
	To Capital Reserve A/c				11,000

Balance Sheet of Preet Limited (and reduced)

	Particulars	**Notes No.**	**₹**
	Equity and Liabilities		
1	Shareholders' funds		
	a) Share capital	1	12,78,000
	b) Reserves and Surplus	2	11,000
2	Non-current liabilities		
	a) Long-term borrowings	3	3,00,000
3	Current liabilities		
	a) Other current liabilities	4	45,000
	b) Short term provisions	5	72,000
	Total		**17,06,000**
	Assets		
1	Non-current assets		
	a) Property, Plant & Equipment & Intangible Assets		
	i) Property, Plant & Equipment	6	7,00,000
2	Current assets		
	a) Inventories		5,06,000
	b) Trade receivables		4,60,000
	c) Cash and cash equivalents	7	40,000
	Total		17,06,000

Notes to Accounts

1	Share Capital	
	1,07,800 Equity shares of ₹10 each (Out of above 7,800 equity shares issued for consideration other than cash)	10,78,000
	20,000 10% Preference share of ₹10 each	2,00,000
	(all the above shares are allotted as fully paid up for consideration other than cash)	
		12,78,000
2	Reserves and Surplus	
	Capital Reserves	11,000
3.	Long-term borrowings	
	Unsecured	
	15% Debentures	3,00,000
4.	Other current liabilities	
	Accrued interest on 15% Debentures	45,000
5.	Short-term provisions	
	Provision for income tax	72,000
6.	Property, Plant & Equipment	
	Machineries	7,00,000
7.	Cash and cash equivalents	
	Balances with banks	40,000

Question 6 – *(Inter Nov 2023) (20 Marks)* *Pg no._____*

Following is the Balance Sheet of Tourma Limited as at 31st March, 2023:

Particulars	Notes	₹ in Lakhs
Equity and Liabilities:		
1. Shareholders funds		
A. Share Capital	1	24.00
B. Reserves and Surplus	2	(9.10)
2. Non-current liabilities		
A. Long-term borrowings	3	3.20
3. Current liabilities		
A. Trade Payables		1.15
B. Short Term Borrowings – Bank Overdraft		1.40
C. Other current liabilities	4	0.32
D. Short term provisions	5	0.42
Total		21.39
Assets:		
1. Non-current assets		
A. Property, Plant and Equipment	6	7.80
B. Intangible Assets	7	1.70
C. Non-Current Investments	8	1.80
2. Current Assets		
A. Inventory		5.12
B. Trade Receivables		4.32
C. Cash & Cash Equivalents		0.65
Total		21.39

Notes to Accounts:

		₹ in Lakhs
1	Share Capital	
	16,000 Equity Shares of ₹ 100 each	16.00
	8,000 6% Preference Shares of ₹ 100 each	8.00
		24.00
2	Reserves and Surplus	
	Debit balance of profit & loss account	(9.10)
		(9.10)
3	Long-term borrowings	
	3,200 10% Debentures	3.20
		3.20
4	Other current liabilities	
	Interest payable on debentures	0.32
		0.32
5	Short term provisions	
	Provision for taxation	0.42
		0.42
6	Property, Plant and Equipment	
	Plant & Machinery	5.00
	Furniture & Fixture	2.80
		7.80

7	Intangible Assets	
	Patents & Copyrights	1.70
		1.70
8	Non-Current Investments	
	Investments (Market Value ₹ 1,10,000)	1.80
		1.80

As on 1st April, 2023, the following scheme of reconstruction was finalized for which necessary resolution was passed and approvals were obtained from appropriate authorities. Accordingly, it was decided that:

a) Each equity share is to be sub-divided into ten fully paid-up equity shares of ₹ 10 each. After sub-division, each shareholder shall surrender to the company 40% of his holding, for the purpose of reissue to trade payables as necessary.
b) Preference shareholders would give up 30% of their capital and 12% Debentures (face value ₹ 100 each) shall be issued to them for balance holdings.
c) The company would issue additional 12% Debentures (face value ₹ 100 each) for ₹ 4,00,000 for meeting its working capital requirement and final settlement of Bank Overdraft at 90% of the amount.
d) Existing debenture holders would accept Furniture & Fixture in full settlement of their dues.
e) Trade payables claim shall be reduced to 70%, it is to be settled by the issue of equity shares of ₹ 10 each out of shares surrendered.
f) The shares surrendered and not re-issued shall be cancelled.
g) The taxation liability is to be settled at 50,000.
h) Investments value to be reduced to market price.
i) Balance of profit and loss account is to be written off.
j) The value of inventories is to be increased by ₹ 32,000 and Provision for Doubtful Debts is to be created at 5% of Trade Receivables.

You are required to:
1. Pass necessary journal entries in the books of account of Tourma Limited.
2. Prepare Reconstruction Account, and
3. Prepare Balance Sheet of the company after internal reconstruction.

Solution

Journal Entries in the books of Tourma Ltd.

	Dr. ₹ In lakhs	Cr. ₹ In lakhs
Equity Share Capital (₹ 100) A/c Dr.	16.00	
To Share Surrender A/c		6.40
To Equity Share Capital (₹ 10) A/c		9.60
(Subdivision of 16,000 equity shares of ₹ 100 each into 1,60,000 equity shares of ₹ 10 each and surrender of 64,000 of such subdivided shares as per capital reduction scheme)		
Preference Share Capital (₹ 100) A/c Dr.	8.00	
To 12% Debentures A/c		5.60
To Reconstruction (₹ 100) A/c		2.40
(12% Debenture issued to Preference Shareholders and 30% of the capital foregone by them)		
Bank A/c Dr.	4.00	
To 12% Debentures (₹ 100) A/c		4.00
(Being 12% debentures issued)		

Bank Overdraft A/c Dr.	1.40	
To Bank A/c		1.26
To Reconstruction A/c		0.14
(Being bank overdraft amount paid)		
10% Debentures A/c Dr.	3.20	
Interest payable A/c Dr.	0.32	
To Debenture holders A/c		3.52
(Being Interest payable on the 10% debentures credited to debenture holders A/c)		
Debentureholders A/c Dr.	3.52	
To Furniture & fixtures A/c		2.80
To Reconstruction A/c		0.72
Trade payables A/c Dr.	1.15	
To Reconstruction A/c		1.15
(Transferred claims of the trade payables to reconstruction account, 70% of which is being clear reduction and equity shares are being issued in consideration of the balance)		
Share Surrender A/c Dr.	6.40	
To Equity Share Capital A/c		0.805
To Reconstruction A/c		5.595
(Issued equity shares to discharge the claims of the trade payables respectively as per scheme and the balance in share surrender account is being transferred to reconstruction account)		
Provision for Taxation A/c Dr.	0.42	
Reconstruction A/c Dr.	0.08	
To Liability for taxation A/c		0.50
(Being conversion of the provision for taxation into liability for taxation.)		
Liability for taxation A/c Dr.	0.50	
To Cash/Bank A/c		0.50
(Being taxation liability settled)		
Reconstruction A/c Dr.	0.70	
To Investment A/c		0.70
(Being investments' value reduce to market price)		
Inventory A/c Dr.	0.32	
To Reconstruction A/c		0.104
To Provision for doubtful debts (4,32,000 x 5%)		0.216
(Being inventory revalued and provision for doubtful debts created)		
Reconstruction A/c Dr.	9.329	
To Profit and Loss A/c		9.10
To Capital Reserve A/c		0.229
(Adjusted debit balance of profit and loss account against the reconstruction account and the balance in the latter is being transferred to capital reserve)		

Balance Sheet of Tourma Limited (and reduced) as at…

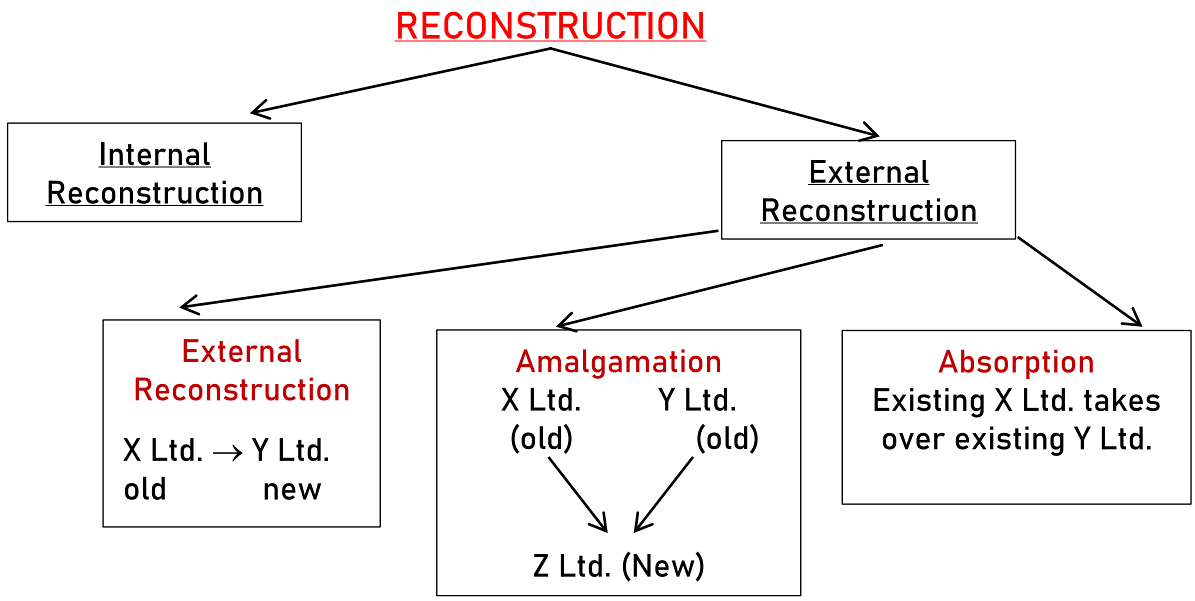
Particulars	Note No.	₹ In lakhs
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	10.405
(b) Reserves and Surplus	2	0.229
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	9.60
(3) Current Liabilities		
Total		**20.234**
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment	4	5.00
(b) Intangible assets	5	1.70
(c) Non-current investments	6	1.10
(2) Current assets		
(a) Inventories	7	5.44
(b) Trade receivables	8	4.104
(c) Cash and cash equivalents (W.N)		2.89
Total		**20.234**

Notes to Accounts

			₹ In lakhs
1.	**Share Capital**		
	Equity Share Capital		
	Issued Capital: 10.405 Equity Shares of ₹ 10 each (9.6 + 0.805)		10.405
	(Of the above shares all are allotted as fully paid up pursuant to capital reduction scheme by conversion of equity shares without payment being received in cash)		
2.	**Reserve and Surplus**		
	Capital Reserve		0.229
3.	**Long-term borrowings**		
	Unsecured Loans:		
	12% Debentures (5.60 + 4)		9.60
4.	**Property, Plant and Equipment**		
	Plant & Machinery		5.00
5.	**Intangible assets**		
	Patents & copyrights		1.70
6.	**Non-Current Investments**		
	Investments		1.10
7.	**Inventory**	5.12	
	Add: Appreciation under scheme of Reconstruction	0.32	5.44
8.	**Trade Receivables**	4.32	
	Less: Provision for doubtful debts	(0.216)	4.104

AMALGAMATION (AS 14)

"Go confidently in the direction of your dreams, Live the life you've imagined".



Basis	Internal Reconstruction	External Reconstruction
Liquidation	The existing company is not liquidated	The existing company is liquidated
Formation	No new company is formed but only the rights of shareholders and creditors are changed	A new company is formed to take over the liquidated company
Reduction of Capital	There is certain reduction of capital & sometimes outside liabilities like debenture holders may have to reduce their claims	There is no reduction of capital. In fact there is fresh share capital of the company

Basis	Amalgamation	Absorption	External Reconstruction
Meaning	2 or more companies are wound up and a new company is formed to take over their business	An existing company takes over the business of one or more existing companies	A newly formed company takes over the business of an existing company
Minimum no. of companies involved	Atleast 3	Atleast 2	Only 2
No. of new resultant company	Only 1	No new resultant company is formed	Only 1
Objective	To cut competition & reap the economies in the larger scale	To cut competition & reap the economies in the larger scale	To reorganize the financial structure of the company

TOPIC 2A: PURCHASE CONSIDERATION (AS -14)

Purchase Consideration

[Value at which business is purchased]

Shares & other securities issued — AND/OR — Cash/ other Assets given — BY — Purchasing Company — TO — Shareholders of Transferor Company

Shares & other securities issued ↓
Equity shares
Preference shares
Debentures

Cash/ other Assets given ↓
Cash
Other Assets

Shareholders of Transferor Company:
Equity Shareholders
Preference Shareholders

METHODS OF COMPUTATION OF PURCHASE CONSIDERATION:

Net Payment Method

To Shareholders of Old / Transferor co.

Net Assets Method

Net Assets = Assets
(-) Outsider Liabilities
(At taken over values)

Does not include capital, Reserves & surplus, losses, etc.

TOPIC 2B: TYPES OF AMALGAMATION

Amalgamation in the Nature of Merger (Pooling of interest method)

As per AS-14 the following 5 conditions are to be fulfilled: -

1. All assets and liabilities are transferred.
2. Assets and liabilities are transferred at same value i.e. book value.
   Exception – 'Purchasing co.' can change value of assets or liabilities to follow same accounting policy.
3. Purchase consideration is discharged by issue of equity shares only to the equity shareholders of transferor company.
   Exception – 'Purchasing company' can pay cash for fractional part of the shares.
4. Same business is intended to be carried on by the purchasing company
5. Shareholders holding atleast 90% of face value of shares in the 'vendor company' becomes the shareholders in the purchasing company.

Amalgamation in the Nature of Purchase (Purchase method)

If any of the 5 conditions discussed above (in merger) is violated, then it is called amalgamation in the nature of purchase.

TOPIC 3: BOOKS OF PURCHASING / TRANSFEREE COMPANY

1. Record the acquisition of business from Vendor Company

Business Purchase A/c	Dr.	(with the Purchase Consideration)
To Liquidator of Vendor Company A/c		

2. Taking over Assets & Liabilities of Vendor Company

A. Nature of Purchase		
Assets A/c	Dr.	(Individually at taken over value)
Goodwill A/c	Dr.	(Difference)
To Liabilities A/c		(Individually at taken over value)
To Business Purchase A/c		(with the Purchase Consideration)
To Capital Reserve A/c		(Difference)
B. Nature of Merger		
Assets A/c	Dr.	(Individually at book value)
To Liabilities A/c		(Individually at book value)
To Reserves A/c		(All at book value & adjustment to be made in it)
To Business Purchase A/c		(with the Purchase Consideration)

3. Making Payment to Vendor Company

Liquidator of Vendor Company A/c	Dr.
To Equity share capital	
To Preference share capital	
To Debentures	
To Securities Premium	
To Bank A/c	
(Only for Equity Shareholders and Preference shareholders)	

4. Record Issue of Debentures to discharge existing Debenture holders of Vendor Company

Debentures of Vendor Company A/c	Dr.
Discount on Issue of Debentures A/c	Dr.
To Debentures	
To Securities Premium	

5. Record Reimbursement of Liquidation expenses of the Vendor Company

A. Nature of Purchase	
Goodwill/Capital Reserve A/c	Dr.
To Bank A/c	
B. Nature of Merger	
P&L /General Reserve A/c	Dr.
To Bank A/c	

6. <u>Eliminate unrealized profit included in the unsold stock/ stock reserve</u>

A. Nature of Purchase
Goodwill/Capital Reserve A/c Dr. To Stock A/c
B. Nature of Merger
P&L /General Reserve A/c Dr. To Stock A/c

7. <u>Elimination of Inter-company owing</u>

Liability A/c Dr. To Asset A/c i.e. Creditors A/c Dr. To Debtors A/c Bills Payable A/c Dr. To Bills Receivable A/c

8. <u>Record the Statutory Reserves of Vendor Company</u> *<u>(Only in case of Purchase Method)</u>*

Amalgamation Adjustment Reserve A/c Dr. To Statutory Reserve A/c

Note:
Statutory reserves are those reserves which are required to be maintained for specific number of years in the balance sheet as per requirements of any statute like Income Tax Act, Custom Act, Excise Act etc.

<u>Examples of Statutory Reserves are:</u>

- Investment Allowance Reserve
- Export Profit Reserve
- Foreign Project Reserve
- Shipping Reserve

<u>Disclosure:</u>
To be disclosed under the head 'Reserves & Surplus' on the Equity & Liabilities Side of the Balance Sheet.

AMALGAMATION

Nature of Purchase (Adjustment Cases)

B/S (Y Ltd.)

Share Capital	500	Fixed Assets	700
Reserves & Surplus	100	Current Assets	300
Creditors	400		
	1000		1000

Fixed Assets valued at 680

Purchase Consideration (Net Payment Method)

Case 1: $\boxed{750}$

Fixed Assets A/c - Dr	680
Current Assets A/c - Dr	300
Goodwill A/c [B.f.]	170
To Creditors A/c	400
To Bus. Purchase	750

Case 2: $\boxed{550}$

	680
	300
To Cap. Res. (B.f.)	30
	400
	550

B/S (Y Ltd.)

Share capital	500	Fixed Assets	700
Reserves & Surplus	100	Current Assets	300
Creditors	400		
	1000		1000

Purchase Consideration (Net Assets Method)

Fixed Assets	=	800
Current Assets	=	400
Creditors	=	(300)
		900

Fixed Ass. A/c - Dr 800

Curr. Ass. A/c - Dr 400

To creditors 300

To Bus. Purch. 900

Nature of Merger (Adjustment Cases)

B/S (Y Ltd.)

Share capital	500	Fixed Assets	700
Reserves & Surplus	100	Current Assets	300
Creditors	400		
	1000		1000

Merger

Purchase Consideration

	Case 1: 540	Case 2: 620	Case 3: 470
FA	700	700	700
CA	300	300	300
		Res. A/c 20	
To Cred.	400	400	400
To Res.	(100 − 40) 60	(100 − 100) −	(100 + 30) 130
To Bus. Purch.	540	620	470

Dr: 1000 Cr: 1040

Diff: $\boxed{40 \text{ Dr.}}$

OR

Sh. cap. vs Purch. cons.
500 vs 540
Diff: 40

500 vs 620
Diff: 120

500 vs 470
Diff: 30

B/S (Y Ltd.)

Share Capital	500	Fixed Assets	700
Res. & surplus		Current Assets	300
Revenue Res.	40		
Capital Res.	35		
Statutory Res.	25		
Creditors	400		
	1000		1000

Purchase Consideration

Case 1: 580

	FA	700
	CA	300
	Rev. Res. (B.S.)	5
	To Cred.	400
(40 − 40)	To Rev. Res.	–
(35 − 35)	To Cap. Res.	–
(25 − ~~25~~)	To Stat. Res.	$\boxed{25}$
	To Bus. Purch.	580

Diff: 500 vs 580

$= \boxed{80}$

Cases: (Debentures Takeover & New Issue)

Old co. 10% Debentures 100000 (FV = 100 each)

Case 1: Redeem/Discharge 10% Des. of old co. at par by issue of 12% Des. of New co.

Entry 2: Takeover

To Des. of old co. A/c 100000

$\frac{100000}{100} = 1000$ Des.

Entry 4: Des. of old co. A/c -Dr 100000

To 12% Debentures A/c 100000

Case 2: Redeem at 5% discount by issue of 12% Des. of New co. at par.

Entry 2: Takeover

To Des. of old co. A/c 95000 (100000 - 5%)

Entry 4: Des. of old co. A/c -Dr 95000

To 12% Debentures A/c 95000

$\frac{95000}{100} = 950$ Des.

Case 3: Redeem at 10% premium by issue of 12% Deb. of New co. at par.

Entry 2: Takeover

To Deb. of old co. A/c — ₹110000
(100000 + 10%)

Entry 4: ₹Deb. of old co. A/c —Dr — ₹110000
To 12% Debentures A/c — ₹110000

No. = $\frac{110000}{100}$ = 1100 Deb.

Case 4: Redeem at 10% premium by issue of 12% Deb. of New co. at 10% premium

Entry 2: Takeover

To Deb. of Old Co. A/c — ₹110000
(100000 + 10%)

Entry 4: ₹Deb. of old co. A/c —Dr — 110000
To 12% Debentures A/c — ₹100000 (1000 X 100)
To Securities Premium A — ₹10000 (1000 X 10)

No: $\frac{₹110000}{₹110}$ = 1000 Deb.

Case 5: Redeem at 20% premium by issue of 12% Deb. of New co. at 96 (4 Discount)

Entry 2: Takeover

To Deb. of old co. A/c 120000

(100000 + 20%)

Entry 4:

Deb. of old co. A/c -Dr 120000

Discount on Issue A/c -Dr 5000 (1250 × 4)

To 12% Debentures A/c 125000 (1250 × 100)

No: $= \left[\frac{120000}{96}\right] = 1250$ Deb.

Question 1 *(Inter Nov 2022) (5 Marks)* Pg no._____

Star Limited agreed to take over Moon Limited on 1st April,2022. The terms and conditions of takeover were as follows:

a) Star Limited issued 70,000 Equity shares of ₹ 100 each at a premium of ₹ 10 per share to the equity shareholders of Moon Limited.
b) Cash payment of ₹ 1,25,000 was made to the equity shareholders of Moon Limited.
c) 25,000 fully paid Preference shares of ₹ 70 each issued at par to discharge the preference shareholders of Moon Limited.

You are required:

i. to give the meaning of "consideration for the amalgamation' as per AS-14, and
ii. Calculate the amount of purchase consideration.

Solution

Consideration for the amalgamation 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.

Computation of Purchase consideration	(₹)	Form
For Preference Shareholders of Moon Ltd. (25,000 × ₹ 70)	17,50,000	25,000 Preference Shares
For equity shareholders of Moon Ltd. (70,000 × ₹ 110)	77,00,000	70,000 Equity shares of Star Ltd.
	1,25,000	Cash
Total Purchase consideration	**95,75,000**	

Question 2 *(Inter Dec 2021) (5 Marks)* Pg no._____

Moon Limited is absorbed by Sun Limited.; the consideration being the takeover of liabilities, the payment of cost of absorption not exceeding ₹ 10,000 (actual cost ₹ 9,000); the payment of 9% debentures of ₹ 50,000 at a premium of 20% through 8% debentures issued at a premium of 25% of face value; the payment of ₹18 per share in cash; allotment of two 11% preference shares of ₹ 10 each and one equity share of ₹10 each at a premium of 30% fully paid for every three shares in Moon Ltd. respectively. The number of shares of the vendor company is 1,50,000 of ₹ 10 each fully paid. Calculate purchase consideration as per AS 14.

Solution

As per AS 14 on Accounting for Amalgamations, the term 'consideration' has been defined as 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. The payment made by transferee company to discharge the Debenture holders and outside liabilities and cost of winding up of transferor company shall not be considered as part of purchase consideration

Computation of Purchase Consideration

Cash payment [₹18 x 1,50,000]	27,00,000
11% Preference Shares of ₹ 10 each [(1,50,000 x 2/3) x ₹ 10]	10,00,000
Equity shares of ₹ 10 each @ 30% premium [(1,50,000 x 1/3) x ₹ 13]	6,50,000
	43,50,000

Question 3

Pg no._____

Following are the summarized Balance Sheet of VT Ltd. and MG Ltd. as on 31st March, 2020:

Particulars	VT Ltd.	MG Ltd.
Equity & Liabilities		
Equity share of ₹ 10 each	12,00,000	6,00,000
10% Pref. Shares of ₹ 100 each	4,00,000	2,00,000
Reserves and Surplus	6,00,000	4,00,000
12% Debentures	4,00,000	3,00,000
Trade Payables	5,00,000	3,00,000
	31,00,000	18,00,000
Assets	VT Ltd.	MG Ltd.
Property, Plant & Equipment	14,00,000	5,00,000
Investment	1,60,000	1,60,000
Inventory	4,80,000	6,40,000
Trade Receivables	8,40,000	4,20,000
Cash at Bank	2,20,000	80,000
	31,00,000	18,00,000

Details of Trade receivables and trade payables are as under:

	VT Ltd.	MG Ltd.
Trade receivables		
Debtors	7,20,000	3,80,000
Bills Receivable	1,20,000	40,000
	8,40,000	4,20,000
Trade payables		
Sundry Creditors	4,40,000	2,50,000
Bills Payable	60,000	50,000
	5,00,000	3,00,000

Property, Plant & Equipment of both companies are to be revalued at 15% above book value. Both companies are to pay 10% equity dividend, Preference dividend having been already paid. After the above transactions are given effect to, VT Ltd. will absorb MG Ltd. on following terms:

(i) VT Ltd. will issue 16 Equity Shares of ₹ 10 each at par against 12 Shares of MG Ltd.

(ii) 10% Preference Shareholders of MG Ltd. will be paid at 10% discount by issue of 10% Preference Shares of ₹ 100 each, at par, in VT. Ltd.

(iii) 12% Debenture holders of MG Ltd. are to be paid at 8% premium, by 12% Debentures in VT Ltd., issued at a discount of 10%.

(iv) Inventory in Trade taken over at 5% lesser than their book value.

(v) ₹ 60,000 is to be paid by VT Ltd. to MG Ltd. for Liquidation expenses.

(vi) Sundry Debtors of MG Ltd. includes ₹ 20,000 due from VT Ltd.

You are required to prepare:

(1) Journal entries in the books of VT Ltd.

(2) Statement of consideration payable by VT Ltd.

Solution

Journal Entries in the books of VT Ltd.

		Dr.	Cr.
1	Property, Plant & Equipment A/c Dr.	2,10,000	
	To Revaluation Reserve A/c		2,10,000
	(Revaluation of fixed assets at 15% above book value)		

2	Reserves & Surplus A/c Dr.	1,20,000	
	To Equity Dividend		1,20,000
	(Declaration of equity dividend @ 10%)		
3	Equity Dividend A/c Dr.	1,20,000	
	To Bank A/c		1,20,000
	(Payment of equity dividend)		
4	Business Purchase A/c Dr.	9,80,000	
	To Liquidator of MG Ltd.		9,80,000
	(Being purchase of business of MG Ltd.)		
5	Property, Plant & Equipment A/c Dr.	5,75,000	
	Inventory A/c Dr.	6,08,000	
	Debtors A/c Dr.	3,80,000	
	Investment A/c Dr.	1,60,000	
	Bills receivables A/c Dr.	40,000	
	Cash at bank A/c (80000-60000) Dr.	20,000	
	To Creditors A/c		2,50,000
	To Bills Payable A/c		50,000
	To 12% Debentures of MG Ltd. A/c		3,24,000
	To Business purchase A/c		9,80,000
	To Capital Reserves A/c (Bal Fig.)		1,79,000
	(Assets & liabilities taken over from MG Ltd. at agreed values & difference of net assets &purchase consideration being credited to capital reserve)		
6	Liquidator of MG Ltd. A/c Dr.	9,80,000	
	To Equity share capital A/c		8,00,000
	To 10% Preference Share Capital A/c		1,80,000
	(Discharge of consideration for MG Ltd.'s)		
7	Creditors A/c Dr.	20,000	
	To Debtors A/c		20,000
	(Being mutual owing cancelled)		
8	12% Debentures of MG Ltd. A/c Dr.	3,24,000	
	Discount on Issue of Debentures Dr.	36,000	
	To 12% Debentures A/c		3,60,000
	(Allotment of 12% Debentures to debenture holders of MG Ltd. at a discount of 10%)		
9	Capital Reserve A/c Dr.	60,000	
	To Bank A/c		60,000
	(Being liquidation expenses reimbursed)		

<u>Statement of Consideration payable by VT Ltd. for 60,000 shares (payment method)</u>

Shares to be allotted 60,000/12 x 16 = 80,000 shares of VT Ltd.

Issued 80,000 shares of ₹ 10 each i.e.		₹ 8,00,000	(i)
For 10% preference shares, to be paid at 10% discount	₹ 2,00,000x 90/100	₹ 1,80,000	(ii)
Consideration amount [(i) + (ii)]		**₹ 9,80,000**	

Question 4 *(Inter Nov 2020) (15 Marks)* *Pg no.______*

High Ltd. and Low Ltd. were amalgamated on and from, 1st April, 2020. A new company Little Ltd. was formed to take over the business of the existing Companies. The summarized Balance sheets of High Ltd. and Low Ltd. as on 31st March, 2020 are as under:

Liabilities	(₹ In Lakhs) High Ltd.	Low Ltd.	Assets	(₹ In Lakhs) High Ltd.	Low Ltd.
Share Capital:			PPE:		
Equity Shares of ₹ 100 each	1000	850	Land and Building	670	385
14% Pref. shares of 100 each	320	175	Plant & Machinery	475	355
Reserves and Surplus			Investments	95	80
Revaluation Reserve	225	110	Current Assets, Loans & Advances		
General Reserve	360	240	Stock	415	389
Investment Allowance Reserve	80	40	Sundry Debtors	322	213
Profit and Loss Account	85	82	Bills Receivable	35	-
Secured Loans			Cash and Bank	303	166
13% Debentures (₹ 100 each)	100	56			
Unsecured Loans (Public Deposits)	50	-			
Current Liabilities & Provisions					
Sundry Creditors	65	35			
Bills Payable	30	-			
	2315	1588		2315	1588

Other Information:

(1) 13% Debenture holders of High Ltd. & Low Ltd. are discharged by Little Ltd. by issuing such number of its 15% Debentures of 100 each so as to maintain same amount of interest.

(2) Preference Shareholders of the two companies are issued equivalent number of 15% Preference shares of Little Ltd. at a price of ₹ 125 per share (Face Value ₹ 100)

(3) Little Ltd. will issue 4 Equity Shares for each Equity Share of High Ltd. & 3 equity shares for each Equity Share of Low Ltd. The shares are to be issued at ₹ 35 each having a face value of ₹ 10 per share.

(4) Investment Allowance Reserve is to be maintained for two more years.

Prepare the Balance sheet of Little Ltd. as on 1st April, 2020 after the amalgamation has been carried out in basis of in the nature of Purchase.

Solution

Balance Sheet of Little Ltd. as at 1st April, 2020

Particulars	Note No.	(₹ in lakhs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1150.00
(b) Reserves and Surplus	2	2437.80
(2) Non-Current Liabilities		
Long-term borrowings	3	185.20
(3) Current Liabilities		
Trade payables	4	130
Total		**3903**

II. Assets		
(1) Non-current assets		
(a) Property, Plant & Equipment & Intangible Assets		
(i) Property, Plant & Equipment	5	1885
(ii) Intangible assets		
(b) Non-current investments (95+80)		175
(2) Current assets		
(a) Inventories (415+389)		804
(b) Trade receivables	6	570
(c) Cash and cash equivalents (303+166)		469
Total		**3903**

Notes to Accounts

		(₹ in lakhs)	**(₹ in lakhs)**
1.	Share Capital		
	Equity share capital		
	65.50 Lakhs equity shares of ₹10 each	655	
	4.95 Lakhs preference shares of ₹100 each	495	
	(all the above shares are allotted as fully paid up pursuant to contracts without payment being received in cash)		1,150
2.	Reserves and surplus		
	Securities premium account		
	On equity shares – 65.50 lakh shares X ₹ 25 = 1,637.50		
	On preference shares – 4.95 lakh shares X ₹ 25 = 123.75	1761.25	
	Capital Reserve (283.33+393.22)	676.55	
	Investment allowance reserve	120	
	Amalgamation Adjustment reserve	(120)	2437.80
3.	Long-term borrowings		
	15% Debentures	135.20	
	Unsecured Loans (Public Deposits)	50	185.20
4.	Trade payables		
	Sundry creditors (65+35)	100	
	Bills Payables	30	130
5.	Property, Plant & Equipment		
	Land and building (670+385)	1055	
	Plant and Machinery (475+355)	830	1885
6.	Trade receivables		
	Sundry Debtors (322+213)	535	
	Bills receivables	35	570

Working Notes:

		(₹ in lakhs)	
(1)	**Computation of Purchase Consideration**		
	(a) Preference shareholders: $\left(\frac{3,20,00,000}{100}\right)$ i.e. 3,20,000 shares x 125 each	400	
	$\left(\frac{1,75,00,000}{100}\right)$ i.e. 1,75,000 shares x 125 each		218.75

	(b) Equity shareholders: $\left(\frac{10,00,00,000 \times 4}{100}\right)$ i.e. 40,00,000 shares x 35 each	1,400	
	$\left(\frac{8,50,00,000 \times 3}{100}\right)$ i.e. 25,50,000 shares x 35 each		892.50
	Amount of Purchase consideration	**1,800**	**1,111.25**
(2)	**Net Assets Taken Over**		
	Assets taken over:		
	Land and building	670	385
	Plant and Machinery	475	355
	Investments	95	80
	Inventories	415	389
	Sundry Debtors	322	213
	Bills receivable	35	-
	Cash and bank	303	166
		2,315	***1,588***
	Less: Liabilities taken over:		
	Debentures	86.67	48.53
	Unsecured Loan (Public Deposits)	50	-
	Sundry Creditors	65	35
	Bills payable	30	-
		(231.67)	***(83.53)***
	Net assets taken over	2083.33	1504.47
	Purchase consideration	1800	1111.25
	Capital reserve	**283.33**	**393.22**
3	**Issue of Debentures** (₹ In Lakhs) High Ltd.- 15% fresh issue of debenture for 13% old debentures = 100 X 13% /15% = 86.67(rounded off) Low Ltd.- 15% fresh issue of debenture for 13% old debentures = 56 X 13% /15% = 48.53 (rounded off) Total debentures issued = 86.67 + 48.53 = 135.20 Lakhs		

Question 5 (Inter Jan 2021) (20 Marks) Pg no.______

Galaxy Ltd. and Glory Ltd., are two companies engaged in the same business of chemicals. To mitigate competition, a new company Glorious Ltd, is to be formed to which the assets and liabilities of the existing companies, with certain exception, are to be transferred. The summarized Balance Sheet of Galaxy Ltd. and Glory Ltd. as at 31st March, 2020 are as follows:

			Galaxy Ltd.	Glory Ltd.
(I)		Equity & Liabilities		
	(1)	Shareholders' fund		
		Share Capital		
		Equity shares of ₹ 10 each	8,40,000	4,55,000
		Reserves & Surplus		
		General Reserve	4,48,000	40,000
		Profit & Loss A/c	1,12,000	72,000

	(2)	Non-current Liabilities		
		Secured Loan		
		6% Debentures	-	3,30,000
	(3)	Current Liabilities		
		Trade Payables	4,20,000	1,83,000
		Total	18,20,000	10,80,000
(II)		Assets		
	(1)	Non-current assets		
		Property, Plant & Equipment		
		Freehold property, at cost	5,88,000	3,36,000
		Plant & Machinery, at cost less depreciation	1,40,000	84,000
		Motor vehicles, at cost less depreciation	56,000	
	(2)	Current Assets		
		Inventories	3,36,000	4,38,000
		Trade Receivables	4,62,000	1,18,000
		Cash at Bank	2,38,000	1,04,000
		Total	18,20,000	10,80,000

Assets and Liabilities are to be taken at book value, with the following exceptions:

(i) The Debentures of Glory Ltd. are to be discharged, by the issue of 8% Debentures of Glorious Ltd. at a premium of 10%.

(ii) Plant and Machinery of Galaxy Ltd. are to be valued at ₹ 2,52,000.

(iii) Goodwill is to be valued at: Galaxy Ltd. ₹ 4,48,000 Glory Ltd. ₹ 1,68,000

(iv) Liquidator of Glory Ltd. is appointed for collection from trade debtors and payment to trade creditors. He retained the cash balance and collected ₹ 1,10,000 from debtors and paid ₹ 1,80,000 to trade creditors. Liquidator is entitled to receive 5% commission for collection and 2.5% for payments. The balance cash will be taken over by new company.

You are required to:

(1) Compute the number of shares to be issued to the shareholders of Galaxy Ltd. and Glory Ltd, assuming the nominal value of each share in Glorious Ltd. is ₹ 10.

(2) Prepare Balance Sheet of Glorious Ltd., as on 1st April, 2020 and also prepare notes to the accounts as per Schedule III of the Companies Act, 2013.

Solution

Calculation of Purchase consideration

	Galaxy Ltd.	Glory Ltd.
Purchase Consideration	₹	₹
Goodwill	4,48,000	1,68,000
Freehold property	5,88,000	3,36,000
Plant and Machinery	2,52,000	84,000
Motor vehicles	56,000	--
Inventory	3,36,000	4,38,000
Trade receivables	4,62,000	--
Cash at Bank	2,38,000	24,000
	23,80,000	**10,50,000**
Less: Liabilities:		
6% Debentures (3,00,000 x 110%)	-	(3,30,000)
Trade payables	(4,20,000)	--
Net Assets taken over	**19,60,000**	**7,20,000**
To be satisfied by issue of shares of Glorious Ltd. @ ₹10 each	**1,96,000**	**72,000**

Balance Sheet Glorious Ltd. as at 1st April, 2020

	Particulars	Note No.	Amount
	Equity and Liabilities		
1	Shareholders funds		
	a) Share capital	1	26,80,000
	b) Reserves and Surplus	2	30,000
2	Non-current liabilities		
	a) Long-term borrowings	3	3,00,000
3	Current liabilities		
	a) Trade payables		4,20,000
	Total		**34,30,000**
	Assets		
1	Non-current assets		
	a) Property, Plant & Equipment & Intangible Assets		
	(i) Property, Plant & Equipment	4	13,16,000
	(ii) Intangible assets	5	6,16,000
2	Current assets		
	a) Inventories	6	7,74,000
	b) Trade receivables		4,62,000
	c) Cash and cash equivalents	7	2,62,000
	Total		**34,30,000**

Notes to accounts

		₹	₹
1	Share Capital		
	Equity share capital		
	2,68,000 shares of ₹10 each (All the above shares are issued for consideration other than cash)		26,80,000
2	Reserves and Surplus		
	Securities Premium A/c (W.N.)		30,000
3	Long-term borrowings		
	Secured		
	8% 3,000 Debentures of 100 each		3,00,000
4	Property, Plant & Equipment		
	Freehold property		
	Galaxy Ltd.	5,88,000	
	Glory Ltd.	3,36,000	9,24,000
	Plant and Machinery		
	Galaxy Ltd.	2,52,000	
	Glory Ltd.	84,000	3,36,000
	Motor vehicles Galaxy Ltd.		56,000
			13,16,000
5	Intangible assets		
	Goodwill		
	Galaxy Ltd.	4,48,000	
	Glory Ltd.	1,68,000	6,16,000
6	Inventories		
	Galaxy Ltd.	3,36,000	
	Glory Ltd.	4,38,000	7,74,000
7	Cash & Cash Equivalents		
	Galaxy Ltd.	2,38,000	
	Glory Ltd.	24,000	2,62,000

Working Note:

Calculation of cash balance of Glory Limited to be taken over by Glorious Limited

Cash balance as at 31st March,2020		1,04,000
Add: Received from debtors		1,10,000
		2,14,000
Less: Paid to Creditors		(1,80,000)
		34,000
Less: Commission to liquidators		
On Debtors @ 5%	5,500	
On Creditors @ 2.5%	4,500	(10,000)
		24,000

Note:

1. It is assumed that the nominal value of debentures of Glory Ltd. is ₹ 100 each.
2. As per the information given in the question, debentures of Glory Ltd. are to be discharged by the issue of debentures of Glorious Ltd. at premium of 10%. It is assumed in the above solution that the debentures are issued at premium of ₹ 10 for discharge of debentures of ₹ 3,30,000. Alternative answer considering other reasonable assumption is also possible.

TOPIC 4: BOOKS OF TRANSFEROR /VENDOR /OLD COMPANY

While closing the books, the general principles of closures shall apply. AS-14 does not deal with the books of vendor company. Also the accounting treatment in the books of vendor is exactly same whether it is in nature of merger or purchase.

1. Transfer of Assets to Realisation Account

Realisation A/c	Dr.
To Sundry Assets A/c	

- By Name of Individual Assets
- To be transferred at BOOK VALUE
- Do not transfer the following.
  - Miscellaneous expenditure
  - P & L debit balance
- Cash to be transferred only if taken over. If written 'Purchasing company takes over vendor company', assume that cash and all assets are taken over.
- Asset not taken over shall also be transferred here.
- If any asset is such which is having corresponding provision, then gross value is to be transferred.

2. Transfer of Outsider's Liabilities to Realisation Account

Liabilities A/c	Dr.
To Realisation A/c	

- By Name of Individual Liabilities
- To be transferred at BOOK VALUE
- Do not transfer the following
  - Equity share capital
  - Preference share capital
  - Reserves and surplus
- Liabilities not taken over shall also be transferred
- Any provision appearing on asset side is to be debited in this entry

3. Making Purchase Consideration Due

Purchasing Company A/c	Dr.
To Realisation A/c	
(With amount of Purchase Consideration)	

4. Receiving Purchase Consideration (Discharge of Purchase Consideration)

Cash/Bank A/c	Dr.
Equity Shares of 'P' Co. A/c	Dr.
Preference Shares of 'P' Co. A/c	Dr.
Debentures of 'P' Co. A/c	Dr.
To Purchasing Company Account	

5. Realize those assets which have not been taken over by Purchasing Company

Cash/Bank A/c	Dr.
To Realisation A/c	

6. Paying off the liabilities which have not been taken over by Purchasing Company

Realisation A/c Dr. To Cash/Bank A/c

7. Liquidation/Realisation Expenses:

Case 1: If expenses borne and paid by vendor company
Realisation A/c Dr. To Cash/Bank A/c
Case 2: If expenses are to be reimbursed by the purchasing company
a) On Payment by Vendor Company: Purchasing Company A/c Dr. (With Agreed Amount) Realisation A/c Dr. (With Excess) To Cash/Bank A/c (With the total) b) On Reimbursement Cash/Bank A/c Dr. To Purchasing Company A/c

8. Discharge the Claims of Preference Shareholders

A: Making Claim Due
Preference Share Capital A/c Dr. (With Book Value) Realisation A/c Dr. (With Difference) To Preference Shareholders A/c (With amount actually payable) To Realisation A/c (With Difference)
B: Making Payment
Preference Shareholders A/c Dr. To Cash/Bank A/c To Equity Shares of 'P' Co. To Preference Shares of 'P' Co. To Debentures of 'P' Co.

9. Ascertainment of Profit/Loss on Realisation Account

A: If Profit
Realisation A/c Dr. To Equity Shareholders A/c
B: If Loss
Equity Shareholders A/c Dr. To Realisation A/c

10. Transferring Equity Share Capital, Accumulated Profits/Reserves & Losses to Equity Shareholders Account

A: For Transfer of Equity Share Capital, Accumulated Profits & Reserves
Equity Share Capital A/c Dr. Reserves and Surplus A/c Dr. (All including Statutory Reserves) To Equity Shareholders A/c
B: For Transfer of Accumulated Losses
Equity Shareholders A/c Dr. To Misc. Expenditure A/c To P & L A/c (Dr. balance)

11. Make Final Payment to Equity Shareholders

Equity Shareholders A/c Dr. To Cash/Bank A/c To Equity Shares of 'P' Co. To Preference Shares of 'P' Co. To Debentures of 'P' Co.

Realisation A/c

To Sundry Assets (Individually at Book value whether taken over or not) X Cash & Bank (To be transferred if taken over) X Losses		By Sundry Liabilities (Outsider) (Individually at Book value whether taken over or not) X Share capital X Reserves & Profits	
To Cash & Bank A/c (Liabilities not taken over : Paid) (Realisation Expenses paid)		By Purchasing Co. Ltd. A/c (Purchase consideration)	
		By Cash & Bank A/c (Assets not taken over : Realised)	
To Pref. shareholders A/c *		By Pref. shareholders A/c *	
To Profit trfd. to ESH A/c (B.f.)		By Loss trfd. to ESH A/c (B.f.)	

* Pref. share capital vs Share in Purchase Consideration for PSH

Question 6

Pg no._____

The Balance Sheet of Reckless Ltd. as on 31st March, 2020 is as follows:

		₹
Assets:		
Freehold premises		2,20,000
Machinery		1,77,000
Furniture & fittings		90,800
Stock		3,87,400
Trade Receivables	95,000	
Less : Provision for doubtful debts	(4,000)	91,000
Cash in hand		2,300
Cash at bank		1,56,500
		11,25,000
Liabilities:		
60,000 Equity shares of ₹ 10 each		6,00,000
Pre-incorporation profit		21,000
Contingency reserve		1,35,000
Profit and loss account		1,26,000
Trade Payables		1,33,000
Provision for income-tax		1,10,000
		11,25,000

Trade receivables consist of debtors amounting ₹ 80,000 and bill receivables worth ₹ 15,000. Trade payables consist of creditors amounting to ₹ 1,13,000 and acceptances worth ₹ 20,000.

Careful Ltd. decided to take over Reckless Ltd. from 31st March, 2020 with the following assets at value noted against them:

	₹
Bills receivable	15,000
Freehold premises	4,00,000
Furniture and fittings	80,000
Machinery	1,60,000
Stock	3,45,000

¼of the consideration was satisfied by the allotment of fully paid preference shares of ₹ 100 each at par which carried 13% dividend on cumulative basis. The balance was paid in the form of Careful Ltd.'s equity shares of ₹ 10 each, ₹ 8 paid up.

Sundry Debtors realised ₹ 79,500. Acceptances were settled for ₹ 19,000. Income-tax authorities fixed the taxation liability at ₹ 1,11,600. Creditors were finally settled with the cash remaining after meeting liquidation expenses amounting to ₹ 4,000.

You are required to :

a) Calculate the number of equity shares and preference shares to be allotted by Careful Ltd. in discharge of consideration.
b) Prepare the important ledger accounts in the books of Reckless Ltd.; and
c) Pass journal entries in the books of Careful Ltd. with narration

Solution

Calculation of the number of equity shares and preference shares to be allotted by Careful Ltd. in discharge of purchase consideration

Calculation of purchase consideration:	**₹**
Agreed value of assets taken over:	
Bills receivable	15,000
Freehold premises	4,00,000
Furniture & fittings	80,000
Machinery	1,60,000
Inventory	3,45,000
	10,00,000
Discharge of purchase consideration:	
1.Amount paid by allotment of 13% preference shares $= ₹10,00,000 \times \frac{1}{4} = ₹2,50,000$	
Number of 13% preference shares of ₹100 each $= \frac{2,50,000}{100}$ = 2,500 preference shares	
2. Amount paid by allotment of equity shares = ₹ 10,00,000 - ₹ 2,50,000 = ₹ 7,50,000 Paid up value of one equity share = ₹8 each Hence, the number of equity shares allotted $= \frac{Rs.7,50,000}{Rs.8}$ = 93,750 equity shares	

Ledger accounts in the books of Reckless Ltd.

Realisation Account

	₹		₹
To Freehold Premises	2,20,000	By Creditors	1,13,000
To Machinery	1,77,000	By Acceptances	20,000
To Furniture & Fittings	90,800	By Provision for tax	1,10,000
To Inventory	3,87,400	By Provision for doubtful debts	4,000
To Sundry Debtors	80,000	By Careful Ltd.	10,00,000
To Bills Receivable	15,000	By Cash/Bank:	
To Cash/Bank:		Sundry Debtors	79,500
Acceptances	19,000		
Provision for tax	1,11,600		
Creditors	1,03,700		
To Cash/Bank:			
Liquidation expenses	4,000		
To Profit	1,18,000		
	13,26,500		**13,26,500**

Cash and Bank Account

	₹		₹
To Balance b/d (cash at bank)	1,56,500	By Realisation A/c (Acceptances)	19,000
To Cash in hand	2,300	By Realisation A/c (Provision for tax)	1,11,600
To Realisation A/c	79,500	By Realisation (Expenses)	4,000
		By Realisation A/c [Creditors (bal fig.)]	1,03,700
	2,38,300		**2,38,300**

Equity Shareholders Account

	₹		₹
To 13% Cumulative preference shares in Careful Ltd.	2,50,000	By Equity Share Capital	6,00,000
To Equity Shares in Careful Ltd.	7,50,000	By Pre-incorporation profit	21,000
		By Contingency reserve	1,35,000
		By Profit &Loss Account	1,26,000
		By Realisation Account	1,18,000
	10,00,000		**10,00,000**

Careful Ltd. Account

	₹		₹
To Realisation Account	10,00,000	By 13% Cumulative preference shares in Careful Ltd.	2,50,000
		By Equity shares in Careful Ltd.	7,50,000
	10,00,000		**10,00,000**

Journal Entries in the books of Careful Ltd.

	Particulars		Dr.	Cr.
1	Business purchase account Dr.		10,00,000	
	To Liquidator of Reckless Ltd. account			10,00,000
	(Being the amount of purchase consideration payable to liquidator of Reckless Ltd. for assets taken over)			
2	Bills receivable account Dr.		15,000	
	Freehold Premises account Dr.		4,00,000	
	Furniture & Fittings account Dr.		80,000	
	Machinery account Dr.		1,60,000	
	Inventory account Dr.		3,45,000	
	To Business purchase account			10,00,000
	(Being assets taken over)			
3	Liquidator of the Reckless Ltd. account Dr.		10,00,000	
	To 13% Preference share capital account			2,50,000
	To Equity share capital account			7,50,000
	(Being in allotment of 13% fully paid up preference shares and equity shares of ₹10 each, ₹8 each paid up)			

Question 7 *(Inter May 2018 (20 Marks) / RTP Nov 2020)* Pg no.______

The financial position of X Ltd. and Y Ltd. as on 31st March, 2020 was as under:

	X Ltd.	Y Ltd.
Equity and Liabilities		
Equity Shares of ₹ 10 each	30,00,000	9,00,000
9% Preference Shares of ₹ 100 each	3,00,000	-
10% Preference Shares of ₹ 100 each	-	3,00,000
General Reserve	2,10,000	2,10,000
Retirement Gratuity Fund (long term)	1,50,000	60,000
Trade Payables	3,90,000	2,40,000
Total	40,50,000	17,10,000
Assets		
Goodwill	1,50,000	75,000
Land & Buildings	9,00,000	3,00,000
Plant & Machinery	15,00,000	4,50,000
Inventories	7,50,000	5,25,000
Trade Receivables	6,00,000	3,00,000
Cash and Bank	1,50,000	60,000
Total	40,50,000	17,10,000

X Ltd. absorbs Y Ltd. on the following terms:

a) 10% Preference Shareholders are to be paid at 10% premium by issue of 9% Preference Shares of X Ltd.

b) Goodwill of Y Ltd. on absorption is to be computed based on two times of average profits of preceding three financial years (2018-19 : ₹ 90,000; 2017-18 : ₹ 78,000 and 2016-17: ₹ 72,000). The profits of 2016 -17 included credit of an insurance claim of ₹ 25,000 (fire occurred in 2015-16 and loss by fire ₹ 30,000 was booked in Profit and Loss Account of that year). In the year 2017 -18, there was an embezzlement of cash by an employee amounting to ₹ 10,000.

c) Land & Buildings are valued at ₹ 5,00,000 and the Plant & Machinery at ₹ 4,00,000.

d) Inventories are to be taken over at 10% less value and Provision for Doubtful Debts is to be created @ 2.5%.

e) There was an unrecorded current asset in the books of Y Ltd. whose fair value amounted to ₹ 15,000 and such asset was also taken over by X Ltd.

f) The trade payables of Y Ltd. included ₹ 20,000 payable to X Ltd.

g) Equity Shareholders of Y Ltd. will be issued Equity Shares @ 5% premium.

You are required to

a) Prepare Realisation A/c in the books of Y Ltd.
b) Show journal entries in the books of X Ltd.
c) Prepare the Balance Sheet of X Ltd. after absorption as at 31st March, 2020.

Solution

In the Books of Y Ltd.
Realisation Account

To Sundry Assets		By Retirement Gratuity Fund	60,000
Goodwill	75,000	By Trade payables	2,40,000
Land & Building	3,00,000	By X Ltd. (Purchase Consideration)	15,90,000
Plant & Machinery	4,50,000		
Inventory	5,25,000		
Trade receivables	3,00,000		
Bank	60,000		
To Preference Shareholders	30,000		
To Equity Shareholders (Profit on Realisation)	1,50,000		
	18,90,000		**18,90,000**

In the Book of X Ltd.
Journal Entries

		Dr.	Cr.
Business Purchase A/c	Dr.	15,90,000	
To Liquidators of Y Ltd. Account			15,90,000
(Being business of Y Ltd. taken over)			
Goodwill Account	Dr.	1,50,000	
Land & Building Account	Dr.	5,00,000	
Plant & Machinery Account	Dr.	4,00,000	
Inventory Account	Dr.	4,72,500	
Trade receivables Account	Dr.	3,00,000	
Bank Account	Dr.	60,000	
Unrecorded Assets Account	Dr.	15,000	
To Retirement Gratuity Fund Account			60,000
To Trade payables Account			2,40,000
To Provision for Doubtful Debts Account			7,500
To Business Purchase A/c			15,90,000
(Being Assets & Liabilities taken over).			
Liquidators of Y Ltd. A/c	Dr.	15,90,000	
To 9% Preference Share Capital A/c			3,30,000
To Equity Share Capital A/c			12,00,000
To Securities Premium A/c			60,000
(Being Purchase Consideration satisfied as above).			

Balance Sheet X Ltd. as at 31st March, 2020

	Particulars	Note No.	Amount
			₹
	Equity and Liabilities		
1	Shareholders funds		
	a) Share capital	1	48,30,000
	b) Reserves and Surplus	2	2,70,000
2	Non-current liabilities		
	a) Long-term Provisions	3	2,10,000
3	Current liabilities		
	a) Trade payables (3,90,000+2,40,000-20,000)		6,10,000
	Total		**59,20,000**

	Assets		
1	Non-current assets		
	a) Property, Plant & Equipment & Intangible Assets		
	(i) Property, Plant & Equipment	4	33,00,000
	(ii) Intangible assets	5	3,00,000
2	Current assets		
	a) Inventories		12,22,500
	b) Trade receivables	6	8,72,500
	c) Cash and cash equivalents	7	2,10,000
	d) Other Current Assets	8	15,000
	Total		**59,20,000**

Notes to accounts

		₹
1. Share Capital		
Equity share capital		
4,20,000 Equity Shares of ₹10 each fully paid (Out of above 1,20,000 Equity shares were issued in consideration other than for cash)		42,00,000
Preference share capital		
6,300 9% Preference Shares of ₹100 each (Out of above 3,300 Preference Shares were issued in consideration other than for cash)		6,30,000
Total		**48,30,000**
2. Reserves and Surplus		
Securities Premium		60,000
General Reserve		2,10,000
Total		**2,70,000**
3. Long-term provisions		
Retirement Gratuity fund		2,10,000
Total		**2,10,000**
4. Property, Plant & Equipment		
Land & Buildings		14,00,000
Plant & Machinery		19,00,000
Total		**33,00,000**
5. Intangible assets		
Goodwill		3,00,000
Total		**3,00,000**
6. Trade receivables (6,00,000+3,00,000-20,000) Less: Provision for Doubtful Debts	8,80,000 (7,500)	**8,72,500**
7. Cash & Cash Equivalents (1,50,000+60,000)		**2,10,000**
8. Other Current Assets (Unrecorded Assets)		**15,000**

Working Notes:

1. **Computation of goodwill**

Profit of 2018-19	90,000
Profit of 2017-18 adjusted (78,000 + 10,000)	88,000
Profit of 2016-17 adjusted (72,000 – 25,000)	47,000
	2,25,000
Average profit	75,000

Goodwill to be valued at 2 times of average profits = ₹ 75,000 x 2 = ₹ 1,50,000

Purchase Consideration	₹
Goodwill	1,50,000
Land & Building	5,00,000
Plant & Machinery	4,00,000
Inventory	4,72,500
Trade receivables	3,00,000
Unrecorded Assets	15,000
Cash at Bank	60,000
	18,97,500
Less: Liabilities:	
Retirement Gratuity Fund	(60,000)
Provision for Doubtful debts	(7,500)
Trade payables	(2,40,000)
Net Assets/Purchase Consideration	**15,90,000**
To be satisfied as under:	
10% Preference Shareholders of Y Ltd.	3,00,000
Add: 10% Premium	30,000
3,300 9% Preference shares of X Ltd.	3,30,000
Equity Shareholders of Y Ltd. to be satisfied by issue of 1,20,000	
Equity Shares of X Ltd. at 5% Premium	12,60,000
Total	**15,90,000**

TOPIC 5: INTRINSIC VALUE METHOD

Intrinsic Value

(Variation of Net Assets Method)

$$\text{No. of shares of New Co.} \times \text{Intrinsic value of New Co.} = \text{No. of shares of Old Co.} \times \text{Intrinsic value of Old Co.}$$

$$\text{No. of shares of New Co.} \Rightarrow \text{No. of Shares of Old Co.} \times \frac{\text{I.V. of Old Co.}}{\text{I.V. of New Co.}}$$

Where

$$\text{Intrinsic Value} = \frac{\text{Net Assets available for ESH}}{\text{No. of Equity shares}}$$

Question 8 Pg no._____

Y Ltd. decides to absorb X Ltd. X Ltd. gives you following information on the date of absorption:

	₹
Net assets	2,90,000
Profit & Loss Account (Dr. Balance)	70,000
Share Capital: 3,000 Equity shares of ₹ 100 each (fully paid)	3,00,000
Preference shares	60,000

Y Ltd. agrees to take over the net assets of X Ltd. The terms of the purchase consideration payable is as follows:

1) An equity share in X Ltd., for purposes of absorption, is valued @ ₹ 70. Y Ltd. shall issue equity shares at value of 120 each for the equity shareholders of X Ltd.
2) Y Ltd. agrees to pay ₹ 60,000 in cash for payment to preference shareholders.

Calculate purchase consideration to be paid by Y Ltd. and how will it be discharged?

Question 9 Pg no._____

Below are summarized balance sheets of Vasudha Ltd. & Vaishali Ltd as at 31st March, 2020

Liabilities	Vasudha Ltd.	Vaishali Ltd.	Assets	Vasudha Ltd.	Vaishali Ltd.
Share capital:			Factory Building	2,10,000	1,60,000
Equity shares of ₹ 10 each	5,40,000	4,03,300	Debtors	2,86,900	1,72,900
General Reserves	86,000	54,990	Stock	91,500	82,500
Profit & Loss A/c	66,000	43,500	Goodwill	50,000	35,000
Sundry Creditors	44,400	58,200	Cash at Bank	98,000	1,09,590
	7,36,400	5,59,990		7,36,400	5,59,990

Goodwill of Vasudha Ltd. and Vaishali Ltd. is to be valued at ₹ 75,000 & ₹ 50,000 respectively. Factory Building of Vasudha Ltd is worth ₹1,95,000 and of Vaishali Ltd ₹ 1,75,000. Stock of Vaishali has been shown at 10% above of its cost. It is decided that Vasudha Ltd will absorb Vaishali Ltd, by taking over its entire business by issue of shares at the Intrinsic Value. Calculate Purchase Consideration and how it is discharged.

Purchase consideration

To	In	Workings	Amount
1) PSH	Cash	-	60000
2) ESH	Equity shares	$\left(3000 \times \frac{70}{120}\right) \times 120$ swap / exchange 1750 equity shares @ 120 each	210000
			270000

No. of shares of New Co. × I.V. of New Co. = No. of shares of old co. × I.V. of old co.

$$x \times 120 = 3000 \times 70 = 210000$$

$$x = \frac{3000 \times 70}{120} = \boxed{1750 \text{ shares}}$$

	Vasudha Ltd.	Vaishali Ltd.
Goodwill	75000	50,000
Factory Building	195000	175000
Debtors	286900	172900
Stock	91500	75000
Bank	98000	109590
Creditors	(44400)	(58200)
Net Assets	702000	524290 → P.C.
No. of Equity Shares	54000	40330
Intrinsic value / share	$\boxed{13}$	13

100
10
110

$\left(82500 \times \frac{100}{110}\right)$

No. of shares of New Co. × I.V. of New Co. = No. of shares of Old Co. × I.V. of Old Co.

No. of shares of New Co. × 13 = 40330 × 13 = 524290

$$\text{No. of shares issued} = \frac{524290}{13}$$

= 40330 eq. shares of 10 each @ 13

Question 10 *(Inter May 2022) (20 Marks)* *Pg no._____*

The summarized Balance Sheet of A Ltd. and B Ltd. as at 31st March,2022 are as under:

	A Ltd. (in ₹)	B Ltd. (in ₹)
Equity shares of ₹10 each, fully paid up	30,00,000	24,00,000
Securities Premium Account	4,00,000	
General Reserve	6,20,000	5,00,000
Profit and Loss Account	3,60,000	3,20,000
Retirement Gratuity Fund Account	1,00,000	
10% Debentures	20,00,000	
Unsecured Loan (including loan from A Ltd.)	6,00,000	8,20,000
Trade Payables	1,00,000	3,40,000
	71,80,000	43,80,000
Land and Buildings	28,00,000	21,00,000
Plant and Machinery	20,00,000	7,60,000
Long term advance to B Ltd.	2,20,000	
Inventories	10,40,000	7,00,000
Trade Receivables	8,20,000	5,20,000
Cash and Bank	3,00,000	3,00,000
	71,80,000	43,80,000

B Ltd. is to declare & pay ₹ 1 per equity share as dividend, before the following amalgamation takes place with Z Ltd.

Z Ltd. was incorporated to take over the business of both A Ltd. and B Ltd.

a) The authorized share capital of Z Ltd. is ₹ 60 lakhs divided into 6 lakhs equity shares of ₹ 10 each.
b) As per Registered Valuer the value of equity shares of A Ltd. is ₹ 18 per share & of B Ltd. is ₹ 12 per share respectively & agreed by respective shareholders of companies.
c) 10% Debentures of A Ltd. to be issued 12% Debentures of Z Ltd. at par in consideration of their holdings.
d) A contingent liability of A Ltd. of ₹ 2,00,000 is to be treated as actual liability.
e) Liquidation expenses including Registered Valuer fees of A Ltd.₹ 50,000 and B Ltd. ₹ 30,000 respectively to be borne by Z Ltd.
f) The shareholders of A Ltd. and B Ltd. is to be paid by issuing sufficient number of fully paid up equity shares of ₹ 10 each at a premium of ₹ 10 per share.

Assuming amalgamation in the nature of purchase, you are required to pass the necessary journal entries (narrations not required) in the books of Z Ltd. and Prepare Balance Sheet of Z Ltd. immediately after amalgamation of both the companies.

Solution

Working Note:

Calculation of amount of Purchase Consideration

	A Ltd.	B Ltd.
Existing shares	3,00,000	2,40,000
Agreed value per share	₹ 18	₹ 12
Purchase consideration	54,00,000	28,80,000
No. of shares to be issued of ₹ 20 each (including ₹ 10 premium)	2,70,000	1,44,000
Face value of shares at ₹ 10	27,00,000	14,40,000
Premium of shares at ₹ 10	27,00,000	14,40,000

Journal Entries in the books of Z Ltd.

	₹	₹
Business Purchase A/c Dr.	54,00,000	
To Liquidator of A Ltd. A/c		54,00,000
Land & Building A/c Dr.	28,00,000	
Plant & Machinery A/c Dr.	20,00,000	
Long term advance to B Ltd. A/c Dr.	2,20,000	
Inventories A/c Dr.	10,40,000	
Trade Receivables A/c Dr.	8,20,000	
Cash and Bank A/c Dr.	3,00,000	
Goodwill A/c Dr.	12,20,000	
To Retirement Gratuity Fund A/c		1,00,000
To 10% Debentures of A Ltd. A/c		20,00,000
To Unsecured Loan A/c		6,00,000
To Trade Payables A/c		1,00,000
To Other liabilities A/c		2,00,000
To Business Purchase A/c		54,00,000
10% Debentures of A Ltd. A/c Dr.	20,00,000	
To 12% Debentures A/c		20,00,000
Liquidator of A Ltd. A/c Dr.	54,00,000	
To Equity Share Capital A/c		27,00,000
To Securities Premium A/c		27,00,000
Business Purchase A/c Dr.	28,80,000	
To Liquidator of B Ltd. A/c		28,80,000
Land and Building A/c Dr.	21,00,000	
Plant & Machinery A/c Dr.	7,60,000	
Inventories A/c Dr.	7,00,000	
Trade Receivables A/c Dr.	5,20,000	
Cash and Bank (less dividend) A/c Dr.	60,000	
To Unsecured Loan A/c		8,20,000
To Trade Payables A/c		3,40,000
To Business Purchase A/c		28,80,000
To Capital Reserve A/c		1,00,000
Liquidators of B Ltd. A/c Dr.	28,80,000	
To Equity Share Capital A/c		14,40,000
To Securities Premium A/c		14,40,000
Unsecured Loans A/c Dr.	2,20,000	
To Long term Advance to B Ltd. A/c		2,20,000
*Capital Reserve A/c Dr.	1,00,000	
To Cash and Bank A/c (Liquidation expenses)		80,000
To Goodwill A/c		20,000

Note:

1. The journal entries for A Ltd. and B Ltd. have been given separately in the above solution. Alternatively, the entries may be given as combined for both companies.
2. *Alternatively, following set of entries may be given in place of the last entry given above:

Goodwill A/c Dr.	50,000	
To Cash & Bank A/c (Liquidation expenses of A Ltd.)		50,000
Capital Reserve A/c Dr.	30,000	
To Cash & Bank A/c (Liquidation expenses of B Ltd.)		30,000
Capital Reserve A/c Dr.	70,000	
To Goodwill A/c		70,000

Balance Sheet of Z Ltd. as at 31st March, 2022

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	41,40,000
(b) Reserves and Surplus	2	41,40,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	20,00,000
(b) Long term provisions	4	1,00,000
(3) Current Liabilities		
(a) Short-term borrowings*	5	12,00,000
(b) Trade payables	6	4,40,000
(a) Other liability		2,00,000
Total		**1,22,20,000**
II. Assets		
(1) Non-current assets		
(a) PPE & Intangible Assets		
i. Property, plant and equipment	7	76,60,000
ii. Intangible Assets (Goodwill 12,20,000-20,000)		12,00,000
(2) Current assets		
(a) Inventories	8	17,40,000
(b) Trade receivables	9	13,40,000
(c) Cash and cash equivalents	10	2,80,000
Total		**1,22,20,000**

*Unsecured loans have been considered as short-term borrowings. Alternatively, it may be considered as long-term borrowings and presented accordingly.

Notes to Accounts

		(₹)	(₹)
1.	**Share Capital**		
	Authorized Share Capital: 6,00,000 Equity shares of ₹ 10 each		60,00,000
	Issued: 4,14,000 Equity shares of ₹ 10 each (all these shares were Issued for consideration other than cash)		41,40,000
2.	**Reserves and surplus**		
	Securities Premium Account (4,14,000 shares × ₹ 10)		41,40,000
3.	**Long-term borrowings**		
	12% Debentures		20,00,000
4	**Long term Provisions**		
	Retirement gratuity fund		1,00,000
5.	**Short-term borrowings**		
	Unsecured loans		
	A Ltd. 6,00,000		
	B Ltd. 8,20,000	14,20,000	
	Less: Mutual	(2,20,000)	12,00,000
6.	**Trade payables**		
	A Ltd.	1,00,000	
	B Ltd.	3,40,000	4,40,000

7.	**Property, plant & equipment**		
	Land and Building		
	A Ltd.	28,00,000	
	B Ltd.	21,00,000	49,00,000
	Plant and Machinery		
	A Ltd.	20,00,000	
	B Ltd.	7,60,000	27,60,000
8.	**Inventories**		76,60,000
	A Ltd.	10,40,000	
	B Ltd.	7,00,000	17,40,000
9	**Trade receivables**		
	A Ltd.	8,20,000	
	B Ltd.	5,20,000	13,40,000
10	**Cash & cash equivalents**		
	A Ltd.	3,00,000	
	B Ltd. [3,00,000-2,40,000(dividend)]	60,000	
	Less: Liquidation Expenses	(80,000)	2,80,000

Question 11 *(Inter Nov 2023) (5 Marks)* Pg no._____

Raman Limited and Naman Limited decided to amalgamate and form a new company Rana Limited as on 31st March, 2023 and provided you the following information :

Particulars	As on 31st March, 2023		Revalued Figures for Amalgamation	
	Raman Limited (₹)	Naman Limited (₹)	Raman Limited (₹)	Naman Limited (₹)
Equity shares of ₹ 10 each	6,72,000	2,52,000	-	-
10% Preference Shares of ₹ 100 Each	3,36,000	1,68,000	-	-
Reserves and Surplus	5,44,240	2,65,480	-	-
Trade Payables	84,000	1,76,000	80,640	1,68,960
Property, Plant and Equipment	7,69,000	4,36,400	10,58,100	5,20,100
Goodwill	1,62,000	-	1,62,000	-
Inventories	1,89,000	1,17,600	2,78,620	2,06,780
Trade Receivables	2,81,000	1,47,000	2,47,140	1,38,180
Cash & Cash Equivalents	2,35,240	1,60,480	-	-

The purchase consideration is to he satisfied as follows:

a) By issue of 4 Preference Shares of ₹ 100 each in Rana Limited @ ₹ 85 paid up and at a premium of ₹ 30 per share for every 3 preference shares held in both the companies.

b) By issue of 5 Equity shares of ₹ 10 each in Rana Limited @ ₹ 7 paid up and at a premium of ₹ 5 per share for every 3 equity shares held in both the companies.

c) In addition, necessary cash should be paid to equity shareholders of both the companies as required to adjust the rights of shareholders of both the companies in accordance with the intrinsic value of the shares of both the companies.

You are required to compute the purchase consideration for both the companies.

Solution

Purchase consideration:

	Raman Ltd. ₹	**Naman Ltd. ₹**
Payable to preference shareholders: Preference shares at ₹ 115 per share	5,15,200 (3,360 x 4)/3	2,57,600 (1,680 x 4)/3
Equity Shares at ₹ 12 per share	13,44,000 (67,200 x 5/3)	5,04,000 (25,200 x 5/3)
Cash [See W.N.]	41,260	94,980
	19,00,460	**8,56,580**

Working note:

	Raman Ltd. ₹	**Naman Ltd. ₹**
Goodwill	1,62,000	-
PPE	10,58,100	5,20,100
Trade receivables	2,47,140	1,38,180
Inventory	2,78,620	2,06,780
Cash & Cash Equivalent	2,35,240	1,60,480
	19,81,100	**10,25,540**
Less: Trade payables	(80,640)	(1,68,960)
	19,00,460	**8,56,580**
Payable in shares	18,59,200	7,61,600
Payable in cash	41,260	94,980

BRANCH ACCOUNTING

- INLAND BRANCH
  - Dependent Branch [Where A/cing Records are Kept at HO]
    - Goods Send at Cost / Invoice Price
      - Debtors Method
      - Final A/cs Method
      - Stock & Debtors Method
    - Goods Send at Wholesale Price
      - Wholesale Price Method
  - Independent Branch [Maintains Independent A/cing Records]
- FOREIGN BRANCH
  - Integral Foreign Operation (IFO)
  - Non Integral Foreign Operation (NIFO)

CONCEPT 1A

DEBTORS METHOD

BRANCH ACCOUNT

Particulars	Amount	Particulars	Amount
To Balance b/d		By Balance b/d	
Stock (At Invoice Price)	xx	Creditors	xx
Debtors	xx	O/s Expenses	xx
Cash in hand	xx	By Stock Reserve (on Opening stock)	xx
Fixed Assets	xx	By Goods sent to branch (Loading)	xx
Prepaid expenses	xx	By Goods Returned to H.O. (At I.P.)	xx
To Goods sent to branch (At I.P.)	xx	By Bank (Remittances to H.O.)	
To Goods returned to H.O. (Loading)	xx	• Cash Sales xx	
To Bank (Cash sent by H.O. to branch for expenses/Purchase of fixed assets)	xx	• Collection from Debtors xx • Recovery from Insurance Co. xx • Expenses paid by branch (xx) • Assets purchased by branch (xx)	xx
To Stock Reserve (on Closing stock)	xx	By Balance c/d	
To Balance c/d		Stock (At I.P.)	xx
Creditors	xx	Debtors	xx
O/s Expenses	xx	Cash in hand	xx
To Net Profit (Bal. Fig.)*	xx	Fixed Assets	xx
		Prepaid expenses	xx
		By Net Loss (Bal. Fig.)*	xx
	XXX		**XXX**

***Any one of these**

Notes:

1) If any figure is missing with respect to stock, debtors, cash etc., we make

Memorandum Stock A/c, Memorandum Debtors A/c, Memorandum Cash A/c

[Eg. closing stock, GSTB, etc.] [Eg. Collection, closing Bal., etc.] [Eg. Remittance, closing Bal, etc.]

2) Discount Allowed, Bad debts, etc.

Branch A/c : No Effect

Memo. Debtors A/c : Shown on Credit side

3) Sales Return by Debtor:

Branch A/c : No Effect

Memo. stock & Memo. Debtors A/c : Shown

4) Normal Loss / Abnormal Loss :

Branch A/c : No Effect

Memo. Stock A/c : Shown

However Insurance claim Received/ Receivable to be shown in Branch A/c

5) Branch stock (Opening & closing) & GSTB (Net) to be shown at Invoice Price & loading reversed always, unless Ques. specifies to show on Cost Basis

6) Goods in Transit

HO $\xrightarrow{\text{Send IP = 600000}}$ Branch

Cost = 500000

Loading (20% on Cost) 100000

Inv. Price 600000

Receive by year end

Amount = 480000 < Sale 420000, Stock 60000

In Transit

Amount = 120000

Branch Stock A/c (IP)

To Bal b/d (Op. Stock)	-	By Cash/Debtors (Sales)	420000
To GSTB	600000	By Bal c/d (incl. GIT) [60000 + 120000]	180000

Question 1

XYZ is having its Branch at Kolkata. Goods are invoiced to the branch at 20% profit on sale. All expenses are paid by head office except petty expenses which are met by the Branch Manager. Prepare branch account in the books of Head Office.

	Rs.		Rs.
Stock on 1st April 2019 (invoice price) Sundry Debtors on 1st April, 2019 Petty Cash as on 1st April, 2019 Office furniture on 1st April, 2019 O/s Salary as on 1st April 2019 Prepaid Rent as on 1st April 2019	30,000 18,000 800 3,000 200 300	Expenses paid by head office: Rent Salary Stationery & Printing	 1,800 3,200 800
Goods invoiced from the head office (invoice price)	1,60,000	Petty expenses paid by the branch	600
Goods return to Head Office	2,000	Discount allowed to debtors	160
Goods return by debtors	960	Furniture purchased by branch From collections (01.10.2019)	8,000
Cash received from debtors	60,000	Abnormal Loss (Invoice Price)	5,000
Cash Sales	1,00,000	Insurance claim received	3,000
Credit sales	60,000	Depreciation to be provided on branch furniture at 10% p.a.	
		O/s Salary as on 31st March 2020 Prepaid Rent as on 31st March 2020	350 500

Solution

Branch Account

Particulars	Amount	Particulars	Amount
To Balance b/d		By Balance b/d O/s Salary	 200
Stock	30,000	By Stock Reserve (Opening) {30,000 * 20/100}	6,000
Debtors	18,000	By Goods sent to branch (Loading) {1,60,000 * 20/100}	32,000
Petty Cash	800	By Goods Returned to H.O.	2,000
Office furniture	3,000	By Bank (Remittances)	
Prepaid Rent	300	Cash Sales 1,00,000	
To Goods sent to branch	1,60,000	Collection from Debtors 60,000	
To Goods returned to H.O. (Loading) {2,000 * 20/100}	400	Insurance Claim Rec. 3,000 Purchase of Furniture (8,000)	 1,55,000
To Bank:		By Balance c/d	
Rent	1,800	Stock (W.N.-2)	23,960
Salary	3,200	Debtors (WN-1)	16,880
Stationery & Printing	800	Cash in hand (800 - 600)	200
To Stock Reserve (Closing) {23,960 * 20/100}	4,792	Office furniture (3,000-10%)+(8000- 8000*10%*6/12)	10,300
To Balance c/d O/s Salary	 350	Prepaid Rent	500
To Net Profit (Bal. Fig.)	23,598		
	2,47,040		**2,47,040**

WN-1

Memorandum Debtors A/c

To Balance b/d	18,000	By Bank	60,000
To Credit Sales	60,000	By Discount allowed	160
		By Sale Returns	960
		By Balance c/d (Bal. Fig)	16,880
	78,000		**78,000**

WN-2

Memorandum Stock A/c

To Balance b/d	30,000	By Goods returned to HO	2,000
To Goods sent to branch	1,60,000	By Cash Sales	1,00,000
To Sales Returns	960	By Credit sales	60,000
		By Abnormal Loss	5,000
		By Balance c/d (Bal. Fig)	23,960
	1,90,960		**1,90,960**

CONCEPT 1B
FINAL ACCOUNTS METHOD

BRANCH TRADING AND P & L A/C

Particulars	Amount	Particulars	Amount
To Opening stock (at cost)	xx	By Sales	
To Goods sent to branch xx		Cash xx	
(-) Returns (xx)	xx	Credit xx	
To Direct Expenses	xx	(-) Sales Return (xx)	xx
To Gross Profit (Bal. Fig.)	xx	By Abnormal Loss	xx
		By Closing stock (at cost)	xx
	XXX		**XXX**
To Indirect expenses	xx	By Gross Profit	xx
To Abnormal Loss	xx	By discount received	xx
To Net Profit (Bal. Fig.)	xx		
	XXX		**XXX**

Solution of Question 1 by Trading and P&L A/c Method

Branch Trading and P & L A/c

Particulars	Amount	Particulars	Amount
To Opening stock (30,000-6,000)	24,000	By Sales:	
To Goods sent 1,60,000		Cash 1,00,000	
(-) Returns (2,000) (1,58,000-31,600)	1,26,400	Credit 60,000 (-) Sales Return (960)	1,59,040
		By Abnormal Loss (5,000-1,000)	4,000
To Gross Profit (Bal. Fig.)	31,808	By Closing stock (23,960-4,792)	19,168
	1,82,208		**1,82,208**
To Discount Allowed	160	By Gross Profit	31,808
To Abnormal Loss (4,000-3,000)	1,000		

To Rent (1800+300-500)	1,600		
To Salary (3,200-200+350)	3,350		
To Stationary & Printing	800		
To Depreciation on Furniture (300+400)	700		
To Petty expenses	600		
To Net Profit (Bal. Fig.)	23,598		
	31,808		**31,808**

CONCEPT 1C

STOCK & DEBTOR SYSTEM

Branch Stock Account (At Invoice Price)

Particulars	Amount	Particulars	Amount
To Balance b/d	xx	By Goods sent to branch (returns)	xx
To Goods sent to branch	xx	By Bank (Cash Sales)	xx
To Branch Debtors A/c (Returns)	xx	By Branch Debtors A/c (Credit Sale)	xx
To Surplus transferred to Branch adjustment a/c [SP > IP]	xx	By Shortage/Abnormal Loss	xx
		By Branch Adjustment (Normal loss)	xx
		By Balance c/d	Xx
	XXX		**XXX**

Note In case of Branch Stock Account, if Balance figure is on credit side then:
Case 1: Closing stock not given → then balance figure will be considered as Closing Stock.
Case 2: Closing stock is given → then consider the balance figure to be shortage/abnormal loss and separate the same accordingly in Branch adjustment & Branch P&L account.

Branch Adjustment Account

Particulars	Amount	Particulars	Amount
To Goods sent to branch-Returns (Loading)	xx	By Stock Reserve (Opening stock)	xx
To Stock Reserve (Closing stock)	xx	By Goods sent to branch (Loading)	xx
To Abnormal Loss (Loading)	xx	By Surplus transferred from Branch Stock A/c	Xx
To Branch Stock a/c (Normal loss)	xx		
To Branch P&L {Gross Profit}	xx		
	XXX		**XXX**

Branch Expenses Account

Particulars	Amount	Particulars	Amount
To Bank A/c (expenses) [like printing & stationery, salaries, rent & rates, other expense, etc.)	xx	By Branch P & L A/c	xx
	XXX		**XXX**

Branch P & L Account

Particulars	Amount	Particulars	Amount
To Branch Expenses A/c	xx	By Branch Adjustment (G.P.)	xx
To Branch Debtors A/c Discount Bad Debts	xx	By Branch Cash a/c (Claim received from insurance Co.)	xx
To Abnormal Loss (Cost)	xx		
To Net Profit (Bal. Fig.)	xx		
	XXX		**XXX**

Goods Sent to Branch Account

Particulars	Amount	Particulars	Amount
To Branch stock A/c	xx	By Branch stock A/c	xx
To Branch Adjustment A/c	xx	By Branch Adjustment A/c	xx
To Purchases/Trading A/c (Bal. Fig.)	xx		
	XXX		**XXX**

Branch Debtors Account

Particulars	Amount	Particulars	Amount
To Balance b/d	xx	By Branch stock A/c (Returns)	xx
To Branch stock A/c (Credit Sales)	xx	By Branch P&L A/c (Discount, Bad Debts, etc.)	xx
		By Bank A/c (Collection)	xx
		By Balance c/d	xx
	XXX		**XXX**

Question 2

X & Co. invoices goods to its branch at cost plus 33 1/3%. Prepare ledger accounts as per Stock & Debtors System as they would appear in the books of head office.

Stock at commencement at Branch at invoice Price	3,60,000
Branch Debtors as on 1st April 2019	2,00,000
Stock at close at Branch at Invoice Price	2,88,000
Goods sent to Branch during the year at invoice price (including goods invoiced at Rs. 48,000 to Branch on 31.03.2020 but not received by Branch before close of the year).	24,00,000
Return of goods to head office (invoice Price)	1,20,000
Sales return by Debtors to Branch	20,000
Credit Sales at Branch	1,40,000
Invoice value of goods pilfered	24,000
Insurance Claim Received	10,000
Normal loss at Branch due to wastage and deterioration of stock (at invoice price)	36,000
Cash Sales at Branch	21,60,000
Branch Expenses paid by Head Office	20,000
Discount Allowed	5,000
Collection from Debtors	1,80,000

X & Co. closes its books on 31st March, 2020

Solution

Branch Stock Account

Particulars	Amount	Particulars	Amount
To Balance b/d	3,60,000	By Goods sent to branch (returns)	1,20,000
To Goods sent to branch	24,00,000	By Bank (Cash Sales)	21,60,000
To Branch Debtors A/c (Sales Return)	20,000	By Branch Debtors A/c (Credit Sale)	1,40,000
To Surplus (Bal.Fig.)	36,000	By Goods Pilfered (Abnormal loss)	24,000
		By Branch Adjustment (Normal Loss)	36,000
		By Balance c/d In Hand In Transit	 2,88,000 48,000
	28,16,000		**28,16,000**

Branch Adjustment Account

Particulars	Amount	Particulars	Amount
To Goods sent to branch-Returns (Loading) [1,20,000 × 25%]	30,000	By Stock Reserve (Opening stock) [3,60,000 × 25%]	90,000
To Goods Pilfered (Loading on Abnormal Loss) [24,000 × 25%]	6,000	By Goods sent to branch (Loading) [24,00,000 × 25%]	6,00,000
To Branch Stock A/c (Normal Loss)	36,000	By Surplus	36,000
By Stock Reserve (Closing stock) [3,36,000 × 25%]	84,000		
To Branch P&L {G.P} (Bal. Fig)	5,70,000		
	7,26,000		**7,26,000**

Branch Expenses Account

Particulars	Amount	Particulars	Amount
To Bank A/c (expenses)	20,000	By Branch P & L A/c (Bal. Fig.)	20,000
	20,000		**20,000**

Branch P & L Account

Particulars	Amount	Particulars	Amount
To Goods Pilfered (Cost of Abnormal Loss) [24,000 × 75%]	18,000	By Branch Adjustment (G.P.)	5,70,000
To Branch Expenses	20,000	By Bank (Insurance Claim)	10,000
To Branch Debtors (Discount Allowed)	5,000		
To Net Profit (Bal. Fig.)	5,37,000		
	5,80,000		**5,80,000**

Goods Sent to Branch Account

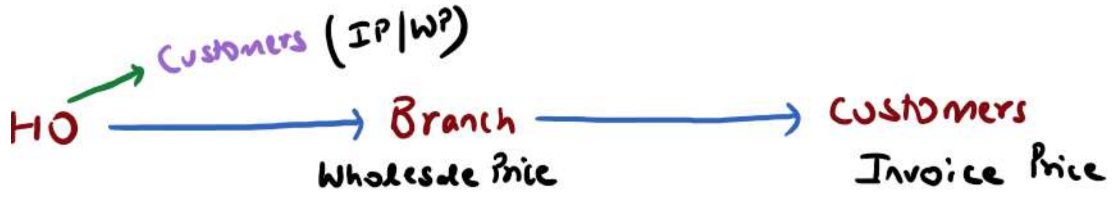
Particulars	Amount	Particulars	Amount
To Branch stock A/c	1,20,000	By Branch stock A/c	24,00,000
To Branch Adjustment A/c	6,00,000	By Branch Adjustment A/c	30,000
To Purchases (Bal. Fig.)	17,10,000		
	24,30,000		**24,30,000**

Branch Debtors Account

Particulars	Amount	Particulars	Amount
To Balance b/d	2,00,000	By Branch stock A/c (Returns)	20,000
To Branch stock A/c (Credit Sales)	1,40,000	By Branch P&L A/c (Discount)	5,000
		By Bank A/c (Collection)	1,80,000
		By Balance c/d (Bal. Fig.)	1,35,000
	3,40,000		**3,40,000**

CONCEPT 1D

WHOLESALE PRICE METHOD



TRADING AND P & L A/C

Particulars	Head Office	Branch	Particulars	Head Office	Branch
To Opening stock	√	√	By Goods sent to Branch	√	×
To Purchases	√	×	By Sales	√	√
To Goods Received from Head Office	×	√	By Closing Stock	√	√
To Gross Profit	√	√		×	
	XXX	**XXX**		**XXX**	**XXX**
To Indirect expenses	√	√	By Gross Profit	√	√
To Stock Reserve	√	×			
To Net Profit	√	√			
	XXX	**XXX**		**XXX**	**XXX**

Question 3

M/s. Ravi having Head Office at Delhi has a Branch at Kolkata. The Head Office does wholesale trade only at cost plus 80%. The Goods are sent to Branch at the wholesale price viz. cost plus 80%. The Branch at Kolkata wholly engaged in retail trade and the goods are sold at cost to Head Office plus 100%.

Following details are furnished for the year ended 31st March, 2020:

	Head Office	Kolkata Branch
Opening Stock (As on 01.04.2019)	1,25,000	36,000
Purchases	21,50,000	-
Goods sent to Branch (cost to H.O. plus 80%)	7,38,000	
Sales	23,79,600	7,30,000
Office Expenses	50,000	4,500
Staff Salary	45,000	8,000

You are required to prepare Trading and Profit & Loss Account of the Head Office and Branch for the Year ended 31st March, 2020.

Solution

Trading and P&L Account

Particulars	H.O	Branch	Particulars	H.O	Branch
To Opening stock	1,25,000	36,000	By Goods sent to branch	7,38,000	-
To Purchases	21,50,000	-	By Sales	23,79,600	7,30,000
To Goods received from HO	-	7,38,000	By Closing Stock (WN-1 & 2)	5,43,000	1,17,000
To Gross Profit	13,85,600	73,000			
	36,60,600	**8,47,000**		**36,60,600**	**8,47,000**
To Office Expenses	50,000	4,500	By Gross Profit	13,85,600	73,000
To Staff Salaries	45,000	8,000	By Stock Reserve (Opening) (WN-3)	16,000	
To Stock Reserve (Closing) (WN3)	52,000	-			
To Net Profit (Bal. Fig.)	12,54,600	60,500			
	14,01,600	**73,000**		**14,01,600**	**73,000**

WN-1 Calculation of closing stock of Head Office

Opening Stock of Head Office	1,25,000
Goods purchased by Head Office	21,50,000
	22,75,000
Less : Cost of goods sold [31,17,600 *100/180]	(17,32,000)
Closing Stock	**5,43,000**

WN-2 Calculation of closing stock of Branch

Opening Stock of Branch	36,000
Goods received from Head Office (At Invoice Value)	7,38,000
Less : Invoice value of goods sold [7,30,000 *180/200]	(6,57,000)
Closing Stock	**1,17,000**

WN-3 Calculation of unrealized profit in branch stock:

	Closing	Opening
Branch stock	1,17,000	36,000
Profit Included	80% of cost	80% of cost
Unrealized Profit	1,17,000 *80/180 = 52,000	36,000 *80/180 = 16,000

CONCEPT 2

INDEPENDENT BRANCH

Features of Accounting System

1. Branch maintains its entire book of accounts under double entry system.
2. Branch opens in its books a Head Office Account to record all the transactions that takes place between Head Office & Branch.
3. Head Office maintains a Branch account to record these transactions.
4. Branch prepares its trial balance, Trading & P & L a/c at the end of accounting period & sends copy of these statements to Head Office for incorporation.
5. After receiving final statement from branch, Head Office reconciles between the two – Branch A/c in Head Office Books & Head Office A/c in Branch Books.
6. Head Office prepares necessary entries to incorporate Branch trial balance in its books.

JOURNAL ENTRIES

S.No.	Transaction	Books of H.O	Books of Branch
1	Goods Dispatched by Head Office	Branch A/c Dr. To Goods Sent to Branch A/c	Goods Rec.from HO A/c Dr. To HO A/c
2	Goods Returned by Branch	Goods Sent to Branch A/c Dr. To Branch A/c	HO A/c Dr. To Goods Rec.from HO A/c
3	Remittance by Branch to Head Office	Cash & Bank A/c Dr. To Branch A/c	HO A/c Dr. To Cash & Bank A/c
4	Head Office sending cash to Branch	Branch A/c Dr. To Cash & Bank A/c	Cash & Bank A/c Dr. To HO A/c
5	Direct purchases by Branch	No Entry	Purchases A/c Dr. To Cash/Creditors A/c
6	Purchases by Branch but payment by HO	Branch A/c Dr. To Cash/Creditors A/c	Purchases A/c Dr. To HO A/c
7	Sales by Branch	No Entry	Cash / Debtors A/c Dr. To Sales A/c
8	Collection from Debtors by branch	No Entry	Cash & Bank A/c Dr. To Debtors A/c
9	Collection from Debtors directly by HO	Cash & Bank A/c Dr. To Branch A/c	HO A/c Dr. To Debtors A/c
10	Expenses incurred at Branch	No Entry	Expenses A/c Dr. To Cash & Bank A/c
11	Expenses of Branch paid by Head Office	Branch A/c Dr. To Cash & Bank A/c	Expenses A/c Dr. To HO A/c
12	Head Office expenses charged to Branch (Allocation to Branch)	Branch A/c Dr. To Expenses A/c	Expenses A/c Dr. To HO A/c
13	Transfer of goods from one branch to another	Receiving Branch A/c Dr. To Sending Branch A/c	<u>Sending Branch</u> HO A/c Dr. To Goods Rec.from HO A/c <u>Receiving Branch</u> Goods Rec.from HO A/c Dr. To HO A/c
14	Fixed Assets A/c maintained at Branch		
a)	Fixed Asset purchased by Branch	No Entry	Fixed Assets A/c Dr. To Cash & Bank A/c
b)	Fixed Asset purchased by Branch paid by Head Office	Branch A/c Dr. To Cash & Bank A/c	Fixed Assets A/c Dr. To HO A/c
c)	Depreciation on the above	No Entry	Depreciation A/c Dr. To Fixed Assets A/c
15	Fixed Asset A/c maintained at Head Office		
a)	Fixed asset purchased at Branch & recorded at Head Office Books	Branch Fixed Assets A/c Dr. To Branch A/c	HO A/c Dr. To Cash & Bank A/c
b)	Branch Fixed Asset recorded in HO books & payment by HO	Branch Fixed Assets A/c Dr. To Cash & Bank A/c	No Entry
c)	Depreciation on the above	Branch A/c Dr. To Branch Fixed Assets A/c	Depreciation A/c Dr. To HO A/c
16	Goods in Transit	No Entry	Goods in Transit A/c Dr. To HO A/c
17	Cash in Transit	Cash in Transit A/c Dr. To Branch A/c	No Entry

Question 4

Pass necessary Journal Entries (with narration) in the books of branch to rectify or adjust the following:

a) Branch Paid Rs. 20,000 as salary to HO Supervisor and the amount was debited to Salaries Account by the branch.
b) Head Office Expenses allocated to branch were Rs. 15,000, but these expenditure were not recorded by the branch.
c) HO collected Rs. 70,000 directly from the customer on branch's behalf.
d) Branch has sent remittance of Rs. 1,50,000 but the same has not yet been received by HO.
e) Branch assets accounts retained at head office, depreciation charged for the year Rs. 15,000 not recorded by Branch.
f) Goods dispatched by the Head office amounting to Rs. 50,000, but not received by the Branch till date of reconciliation.

Solution

Entries in the Books of Branch

S.No.	Particulars	L.F.	Dr. Amount	Cr. Amount
(a)	Head Office A/c Dr.		20,000	
	To Salaries A/c			20,000
	(Being the rectification of salary paid on behalf of H.O.)			
(b)	Expenses A/c Dr.		15,000	
	To Head Office A/c			15,000
	(Being the allocated expenditure by the head office recorded in branch books)			
(c)	Head Office A/c Dr.		70,000	
	To Debtors A/c			70,000
	(Being the adjustment of collection from branch debtors)			
(d)	No entry in the books of branch for remittance sent by branch not received by Head Office till end of year			
(e)	Depreciation A/c Dr.		15,000	
	To Head Office A/c			15,000
	(Being depreciation of assets accounted for)			
(f)	Goods in transit A/c Dr.		50,000	
	To Head Office A/c			50,000
	(Being goods sent by Head Office still in-transit)			

Note: In entry (d) the cash in transit entry will be passed in the Books of the Head Office.

Question 5

Give the journal entries to rectify or adjust the following in the books of the Head Office:

(a) Goods purchased by branch ₹ 7,500 but payment made by Head Office. The Head Office has, wrongly debited this amount to its own purchases account.
(b) Branch paid ₹ 6,500 as salary to a visiting Head Office official. The Branch has debited the amount to salaries account.
(c) Depreciation ₹ 11,250 in respect of Branch Shop whose account is kept in Head Office Books.
(d) Expenses ₹ 5,600 to be charged to the Branch for work done on its behalf by the Head Office.
(e) Goods sent by the Head Office to Branch ₹ 25,000 not yet received by the Branch.

Solution

Entries in the Books of Head Office

S.No.	Particulars	L.F.	Dr. Amount	Cr. Amount
(a)	Branch A/c Dr.		7,500	
	To Purchases A/c			7,500
	(Being rectification of entry for payment for goods purchased by branch wrongly debited to Purchase A/c)			

(b)	Salaries A/c Dr.		6,500	
	To Branch A/c			6,500
	(Being salary paid by the branch for H.O. employee)			
(c)	Branch A/c Dr.		11,250	
	To Branch Fixed Asset (Shop) A/c			11,250
	(Being depreciation of branch fixed assets, whose accounts are kept by head office)			
(d)	Branch A/c Dr.		5,600	
	To Expenses A/c			5,600
	(Being expenses charged to the Branch for work done on its behalf by the Head Office)			
(e)	No entry in the books of head office for goods sent to branch not received by branch till end of year			

Note: In entry (e) the goods in transit entry will be passed in the Books of the Branch.

Question 6

Show adjustment Journal entry alongwith working notes in the books of Head Office at the end of April, 2020 for incorporation of inter-branch transactions assuming that only Head Office maintains different branch account in its books.

A. Delhi Branch:

(1) Received goods from Mumbai – Rs. 1,40,000 and Rs. 60,000 from Kolkata.
(2) Sent goods to Chennai – Rs. 1,00,000, Kolkata – Rs. 80,000.
(3) Bill Receivable received – Rs. 80,000 from Chennai.
(4) Acceptances sent to Mumbai – Rs. 1,00,000, Kolkata – Rs. 40,000.

B. Mumbai Branch (apart from the above):

(5) Received goods from Kolkata – Rs. 60,000, Delhi – Rs. 80,000.
(6) Cash sent to Delhi – Rs. 60,000, Kolkata – Rs. 28,000.

C. Chennai Branch (apart from the above):

(7) Received goods from Kolkata – Rs. 1,20,000.
(8) Acceptances and Cash sent to Kolkata – Rs. 80,000 and Rs.40,000 respectively.

D. Kolkata Branch (apart from the above):

(9) Sent goods, cash & Acceptances to Chennai – Rs. 2,60,000

Solution

Journal Entry in the Books of Head Office

Date	Particulars	L.F.	Dr. Amount	Cr. Amount
30.04.2020	Mumbai Branch A/c Dr.		12,000	
	Chennai Branch A/c Dr.		2,80,000	
	To Delhi Branch A/c			60,000
	To Kolkata Branch A/c			2,32,000
	(Being adjustment entry passed by HO in respect of inter-branch transactions for month of April, 2020)			

Working Note:

Inter – Branch transactions

		Delhi	Mumbai	Chennai	Kolkata
A.	**Delhi Branch**				
(1)	Received goods	2,00,000 (Dr.)	1,40,000 (Cr.)		60,000 (Cr.)
(2)	Sent goods	1,80,000 (Cr.)		1,00,000 (Dr.)	80,000 (Dr.)
(3)	Received B/R	80,000 (Dr.)		80,000 (Cr.)	
(4)	Sent acceptance	1,40,000 (Cr.)	1,00,000 (Dr.)		40,000 (Dr.)
B.	**Mumbai Branch**				
(5)	Received goods	80,000 (Cr.)	1,40,000 (Dr.)		60,000 (Cr.)

(6)	Sent cash	60,000 (Dr.)	88,000 (Cr.)		28,000 (Dr.)
C.	**Chennai Branch**				
(7)	Received goods			1,20,000 (Dr.)	1,20,000 (Cr.)
(8)	Sent cash & acceptances			1,20,000 (Cr.)	1,20,000 (Dr.)
D.	**Kolkata Branch**				
(9)	Sent goods			2,60,000 (Dr.)	2,60,000 (Cr.)
		60,000 (Cr.)	**12,000 (Dr.)**	**2,80,000 (Dr.)**	**2,32,000 (Cr.)**

Incorporation Entries

Example:

TRIAL BALANCE

	Head Office		Branch	
	Dr.	Cr.	Dr.	Cr.
	1000000			
Fixed Assets	1400000		1000000	
Current Assets			800000	
Current Liabilities		800000		700000
P&L A/c		700000		500000
Interunit A/c	600000			600000
Capital A/c		1500000		
	3000000	3000000	1800000	1800000

Entry by HO:

1)	Br. Fixed Assets A/c - Dr	1000000	
	Br. Current Assets A/c - Dr	800000	
	To Branch A/c		1800000
2)	Branch A/c - Dr	1200000	
	To Br. Current Liabilities		700000
	To Br. P&L A/c		500000

Balance Sheet

Liabilities		Assets	
Capital	1500000	Fixed Assets (14L+10L)	2400000
P&L A/c (7L+5L)	1200000	Current Assets (10L+8L)	1800000
Current Liabilities (8L+7L)	1500000		
	4200000		4200000

CONCEPT 3

FOREIGN OPERATIONS

IFO	It is a foreign operation, the activities of which are integral part of those of the reporting enterprise. The business of IFO is carried on as if it were an extension of the reporting enterprises operations.
NIFO	It is a foreign operation that is not an integral foreign operation. The business of NIFO is carried on in substantially independent way by accumulating cash & other monetary items, incurring expenses, generating income & arranging borrowing in its own local currency.

Conversion Rates

	Particulars	IFO	NIFO
1.	Opening Stock	Opening rate	Opening rate
2.	Expenses & Incomes	Average rate	Average rate
3.	Closing Assets & Liabilities (Other than Fixed Assets)	Closing rate	Closing rate
4.	Fixed Assets (& Depreciation)	Actual rate on purchase date	Closing rate
5.	Goods received from Head Office /Remittance to HO and Head Office account balance	Value appearing in HO Trial Balance	Value appearing in HO Trial Balance
6.	Difference in Trial Balance (Exchange Difference)	Transferred to P&L A/c as Exchange Gain/Loss	Transferred to Foreign Currency Translation Reserve A/c in Balance sheet

Points to Note while making converted Trial Balance:

1) O/s Expenses, Prepaid Expenses, Accrued Income, Pre Received Income

↓

Always give both effect while making Trial Balance
(Consider in Trial Balance itself)

2) Depreciation on Fixed Assets: Both the treatments are correct.
i.e. whether in Trial Bal. / P&L A/c & B/s

However if Ques. specifies to consider in Trial Balance then do that.

3) Closing Stock: Never shown in Trial Balance.
Give 2 effects later on 1) Trading A/c 2) B/s.

4) Ques is silent whether IFO or NIFO:

If Fixed Assets Purchase Date: Exchange Rate given: Prefer IFO

Question 7

Omega has a branch at Washington. Its Trial Balance as at 30th September, 2020 is as follows:

	Dr. (US $)	Cr. (US $)
Plant and machinery	1,20,000	-
Furniture and fixtures	8,000	-
Stock, Oct. 1, 2019	56,000	-
Purchases	2,40,000	-

Sales	-	4,16,000
Goods from Omega (H.O.)	80,000	-
Wages	2,000	-
Carriage inward	1,000	-
Office Expenses	10,000	-
Head Office A/c	-	1,14,000
Trade debtors	24,000	-
Trade creditors	-	17,000
Cash at bank	5,000	-
Cash in hand	1,000	-
	5,47,000	**5,47,000**

The following further information is given:

(1) Wages outstanding – $ 1,000.

(2) Depreciate Plant and Machinery and Furniture and Fixtures @ 10 % p.a.

(3) The Head Office sent goods to Branch for Rs. 39,40,000.

(4) The Head Office shows an amount of Rs. 43,00,000 due from Branch.

(5) Stock on 30th September, 2020 – $ 52,000.

(6) There were no in transit items either at the start or at the end of the year.

(7) On September 1, 2018, when fixed assets were purchased, the rate of exchange was Rs. 38 to one $.
On October 1, 2019, the rate was Rs. 39 to one $.
On September 30, 2020, the rate was Rs. 41 to one $.
Average rate during the year was Rs. 40 to one $.

You are asked to prepare:

(a) Trial balance incorporating adjustments given under 1 to 4 above, converting dollars into rupees.

(b) Trading and Profit and Loss Account for the year ended 30th September, 2020 and Balance Sheet as on that date depicting the profitability and net position of the Branch as would appear in India for the purpose of incorporating in the main Balance Sheet

Solution

Washington Branch Trial Balance (in Rupees)
As on 30th September, 2020

Particulars	Dr. (In US $)	Cr. (in US $)	Conversion Rate	Dr. (in Rs.)	Cr. (in Rs.)
Plant & Machinery	1,08,000		38	41,04,000	
Furniture & Fixtures	7,200		38	2,73,600	
Depreciation on P&M =12,000 F&F = <u>800</u>	12,800		38	4,86,400	
Stock (01/10/19)	56,000		39	21,84,000	
Purchases	2,40,000		40	96,00,000	
Sales		4,16,000	40		1,66,40,000
Goods from HO (Omega)	80,000		Actual	39,40,000	
Wages 2,000 (+) O/S <u>1,000</u>	3,000		40	1,20,000	
Carriages inward	1,000		40	40,000	
Office Expenses	10,000		40	4,00,000	
Head Office A/c		1,14,000	Actual		43,00,000
Debtors	24,000		41	9,84,000	
Creditors		17,000	41		6,97,000

Cash at Bank	5,000		41	2,05,000	
Cash in hand	1,000		41	41,000	
O/s Wages		1,000	41		41,000
Exchange gain (Bal. Fig.)					7,00,000
				2,23,78,000	**2,23,78,000**

Trading and P&L A/c

Particulars	Amount	Particulars	Amount
To Opening stock	21,84,000	By Sales	1,66,40,000
To Goods from Head Office	39,40,000	By Closing Stock (52,000 x 41)	21,32,000
To Purchases	96,00,000		
To Carriage inward	40,000		
To Wages	1,20,000		
To Gross Profit (Bal. Fig.)	28,88,000		
	1,87,72,000		**1,87,72,000**
To Depreciation	4,86,400	By Gross Profit	28,88,000
To Office Expenses	4,00,000	By Exchange gain	7,00,000
To Net Profit (Bal. Fig.)	27,01,600		
	35,88,000		**35,88,000**

Balance Sheet

Liabilities	Amount	Assets	Amount
Head Office 43,00,000		Plant & Machinery	41,04,000
(+) NP 27,01,600	70,01,600	Furniture & Fixtures	2,73,600
Creditors	6,97,000	Stock	21,32,000
O/s Wages	41,000	Debtors	9,84,000
		Cash at Bank	2,05,000
		Cash in Hand	41,000
	77,39,600		**77,39,600**

Note: The above solution has been given assuming that the Washington branch is Integral foreign operation of the Omega

EXTRA QUESTION ON STOCK & DEBTORS METHOD:

Question 8 (Inter Nov 2023) (10 Marks)

Jolly Industries of Delhi is a trader in spices. It has a branch at Jalandhar to which Head office invoice goods at 20% on sales. The Jalandhar branch sells spices both on cash and credit. Branch remit all the cash received to Head Office Bank account, thus all expenses of branch are also directly paid from head office.

From the following information given, Prepare Branch Accounts in the Head office ledger using Stock and Debtors Method. Branch does not maintain any books of account, but send fortnightly returns to Head office.

Particulars	₹
Stock at Jalandhar as on 1st April, 2022 (Cost Price)	1,00,000
Sundry Debtors at Jalandhar as on 1st April, 2022	1,10,000
Cash received from Debtors	3,45,000
Bad debts during the year	9,500
Discount allowed to Debtors	5,500
Goods received from Head Office at Invoice Price	6,00,000
Returns to Head office at Invoice Price	60,000
Normal loss of goods during transport (Out of Goods sent by H.O. to Branch)	12,000
Sales returns at Jalandhar Branch	11,000
Salaries and staff welfare expenses at Branch	54,000
Rent and taxes at Branch	9,000
Other Office Expenses	2,500
Sundry Debtors at Branch as at 31st March 2023	1,55,000
Stock at Jalandhar as on 31st March, 2023 (Cost Price)	1,20,000

Credit sales at Branch are four times of the cash Sales at Branch.

Solution

Books of Jolly Industries, Delhi Jalandhar
Branch Stock Account

Particulars	₹	Particulars	₹
To Balance b/d – Op Stock	1,25,000	By Bank A/c – Cash Sales	1,04,000
To Branch Debtors A/c – Sales Return	11,000	By Branch Debtors A/c - Credit Sales	4,16,000
To Goods sent to Branch A/c (6,00,000 +12,000)*	6,12,000	By Goods sent to Branch (Returns to H.O.)	60,000
		By Branch Stock Adjustment A/c (Normal Loss)	12,000
		By Branch Stock Adjustment A/c (Abnormal Loss) (bal. fig.)	6,000
		By Balance c/d - Closing stock	1,50,000
	7,48,000		**7,48,000**

*12,000 added in Goods sent since 6,00,000 is goods received by Branch and this is after loss so to calculate goods sent by HO to branch 12,000 is added.

Jalandhar Branch Stock Adjustment Account

Particulars	₹	Particulars	₹
To Goods sent to Branch A/c (1/5 of ₹60,000) (on returns)	12,000	By Balance b/d (20% of 1,25,000)	25,000
To Branch Stock A/c (Abnormal Loss) (6,000x1/5)	1,200	By Goods sent to Branch A/c (1/5 of ₹ 6,12,000)	1,22,400
To Branch Stock A/c (Normal Loss)	12,000		

To Balance c/d (1/5 of 1,50,000)	30,000		
To Branch P&L A/c (Profit on sale) – B.F.	92,200		
	1,47,400		**1,47,400**

Goods Sent to Branch Account

Particulars	₹	Particulars	₹
To Jalandhar Branch Stock Adjustment A/c	1,22,400	By Jalandhar Branch Stock A/c	6,12,000
To Jalandhar Branch Stock A/c (Returns)	60,000	By Jalandhar Branch Stock Adjustment A/c	12,000
To Purchases A/c	4,41,600		
	6,24,000		**6,24,000**

Branch Debtors Account

Particulars	₹	Particulars	₹
To Balance b/d	1,10,000	By Bank	3,45,000
To Branch Stock A/c	4,16,000	By Branch P&L A/c - Discount	5,500
		By Branch P&L A/c - Bad Debts	9,500
		By Branch Stock - Sales Returns	11,000
		By Balance c/d	1,55,000
	5,26,000		**5,26,000**

Branch Expenses Account

Particulars	₹	Particulars	₹
To Bank A/c (Rent & Taxes)	9,000	By Branch Profit & Loss A/c (Transfer)	65,500
To Bank A/c (Salaries & Staff Welfare expenses)	54,000		
To Bank A/c (office expenses)	2,500		
	65,500		**65,500**

Branch Profit & Loss Account
for the year ending 31st March 2023

Particulars	₹	Particulars	₹
To Branch Expenses A/c	65,500	By Branch Stock Adj. A/c	92,200
To Branch Debtors A/c	5,500		
To Branch Debtors A/c	9,500		
To Abnormal Loss (cost)	4,800		
To Net Profit transferred to Profit & Loss A/c	6,900		
	92,200		**92,200**

FRAMEWORK FOR PREPARATION & PRESENTATION OF FINANCIAL STATEMENTS

The Accounting Standards Board (ASB) of the ICAI issued framework in July, 2000 which provides the fundamental basis for development of new standards as also for review of existing standards.

PURPOSE OF FRAMEWORK

The framework sets out the concepts underlying the preparation and presentation of general purpose financial statements prepared by enterprises for external users. The main purpose of the framework is to assist:

- ❖ Enterprises in preparation of their financial statements in compliance with the accounting standards (AS) and in dealing with the topics not yet covered by any AS.
- ❖ Accounting Standard Board (ASB) in its task of development and review of AS.
- ❖ ASB in promoting harmonization of regulations, accounting standards & procedures relating to preparation & presentation of financial statements by providing basis for reducing the number of alternative accounting treatments permitted by accounting standards.
- ❖ Auditors in forming an opinion as to whether financial statements conform to the AS.
- ❖ Users in interpretation of financial statements.

COMPONENTS OF FIANANCIAL STATEMENTS

Balance sheet	Portrays value of economics resources controlled by an enterprise.
Statement of P&L	Presents the results of operations of an enterprise.
Cash flow statement	Shows the way an enterprise generates cash and uses it.
Notes & other statements	Presents supplementary information explaining different items

USERS OF FINANCIAL STATEMENTS

Investors	Analysis of performance, profitability, financial position of Co.
Employees	Knowledge of stability, continuity, growth
Suppliers, creditors	Determination of credit worthiness
Customers	Analysis of stability, profitability.
Government	Evaluation of entity's performance & contribution to social objectives.
Lenders	Determine whether their loans and interest will be paid when due.
Public	Determine contribution to the local economy and public at large

FUNDAMENTAL ACCOUNTING ASSUMPTIONS

Accrual	Transactions are recognized as and when they occur, without considering receipt /payment of cash.
Going concern	Enterprise will continue in operation in foreseeable future and will not liquidate.
Consistency	Using same accounting policies for similar transactions in all accounting periods.

QUALITATIVE CHARACTERISTICS OF FINANCIAL STATEMENTS

Inter Nov 2020 (5 Marks)

Understandability	Information presented in financial statements should be readily understandable by the users with reasonable knowledge of business and economic activities.
Relevance	Financial statements should contain relevant information only. Information, which is likely to influence the economic decisions by the users, is called relevant.
Reliability	Information must be reliable; that is to say, they must be free from material error and bias.
Comparability	Financial statements should permit both inter-firm and intra-firm comparison.
True and Fair view	Financial statements should show a true and fair view of the performance, financial position and cash flows of an enterprise.

ELEMENTS OF FINANCIAL STATEMENTS

Inter May 2018 (5 Marks)

Asset	Resource controlled by the enterprise as a result of past events from which future economic benefits are expected to flow to the enterprise
Liability*	Present obligation of the enterprise arising from past events, the settlement of which is expected to result i n an outflow of a resource embodying economic benefits.
Equity	Residual interest in assets of an enterprise after deducting all its liabilities.
Income/gain	Increase in economic benefits during accounting period in form of inflows or enhancement of assets or decreases in liabilities that result in increase in equity other than those relating to contributions from equity participants
Expense/loss	Decrease in economic benefits during accounting period in form of outflows or depletions of assets or incurrence of liabilities that result in decrease in equity other than those relating to distributions to equity participants.

* Example: *(RTP May 2020) / (RTP May 2023) / (RTP Nov 2023)*

A Ltd. has entered into a binding agreement with P Ltd. to buy a custom-made machine ₹ 40,000. At the end of 2021-22, before delivery of the machine, A Ltd. had to change its method of production. The new method will not require the machine ordered and it will be scrapped after delivery. The expected scrap value is nil.

Advise the accounting treatment & pass the necessary journal entry.

Solution

A liability is recognised when outflow of economic resources in settlement of a present obligation can be anticipated and the value of outflow can be reliably measured.

In the given case, A Ltd. should recognise a liability of ₹ 40,000 to P Ltd. When flow of economic benefit to the enterprise beyond the current accounting period is considered improbable, the expenditure incurred is recognised as an expense rather than as an asset. In the present case, flow of future economic benefit from the machine to the enterprise is improbable. The entire amount of purchase price of the machine should be recognised as an expense. The accounting entry is suggested below:

P&L A/c Dr. 40,000
To P Ltd. 40,000

(Loss due to change in production method)

(2 separate entries can also be passed instead of 1 entry)

MEASUREMENT BASIS OF ELEMENTS IN FINANCIAL STATEMENTS

Inter Dec 2021 (5 Marks)

Measurement is the process of determining money value at which an element can be recognized in the balance sheet or statement of profit & loss. Framework for Preparation and Presentation of Financial statements recognizes four alternative measurement bases for the purpose of determining the value at which an element can be recognized in the balance sheet or statement of profit & loss.

Historical cost	Acquisition price
Current Cost	Assets are carried out at the amount of cash or cash equivalent that would have to be paid if the same or an equivalent asset was acquired currently. Liabilities are carried at the undiscounted amount of cash or cash equivalents that would be required to settle the obligation currently.
Realisable (Settlement) Value	For assets, amount currently realisable on sale of the asset in an orderly disposal. For liabilities, this is the undiscounted amount expected to be paid on settlement of liability in the normal course of business.
Present Value	Assets are carried at present value of future net cash flows generated by the concerned assets in the normal course of business. Liabilities are carried at present value of future net cash flows that are expected to be required to settle the liability in the normal course of business.

CAPITAL MAINTENANCE

<table>
<tr><td rowspan="2">Financial capital maintenance</td><td>At historical cost</td><td>Opening & closing assets are stated at historical costs.</td></tr>
<tr><td>At current purchasing power</td><td>Restatement at closing prices using average price indices.</td></tr>
<tr><td>Physical capital maintenance</td><td colspan="2">Restatement at closing prices using specific price indices.</td></tr>
</table>

Example 1 **(Financial Capital Maintenance at historical cost)**

A trader commenced business on 01/01/2021 with ₹ 12,000 represented by 6,000 units of a certain product at ₹ 2 per unit. During the year 2021 he sold these units at ₹ 3 per unit and had withdrawn ₹ 6,000. Thus:

Opening Equity = ₹ 12,000 represented by 6,000 units at ₹ 2 per unit.

Closing Equity = ₹ 12,000 (₹ 18,000 – ₹ 6,000) represented entirely by cash.

Retained Profit = ₹ 12,000 – ₹ 12,000 = Nil

The trader can start year 2022 by purchasing 6,000 units at ₹ 2 per unit once again for selling them at ₹ 3 per unit. The whole process can repeat endlessly if there is no change in purchase price of the product.

Example 2 (Financial Capital Maintenance at current purchasing power)

In the previous example (Example 1), suppose that the average price indices at the beginning and at the end of year are 100 and 120 respectively.

Opening Equity = ₹ 12,000 represented by 6,000 units at ₹ 2 per unit.
Opening equity at closing price = (₹ 12,000 / 100) x 120 = ₹ 14,400 (6,000 x ₹ 2.40)
Closing Equity at closing price = ₹ 12,000 (₹ 18,000 – ₹ 6,000) represented entirely by cash.
Retained Profit = ₹ 12,000 – ₹ 14,400 = (-) ₹ 2,400

The negative retained profit indicates that the trader has failed to maintain his capital. The available fund ₹ 12,000 is not sufficient to buy 6,000 units again at increased price ₹ 2.40 per unit. In fact, he should have restricted his drawings to ₹ 3,600 (₹ 6,000 – ₹ 2,400).

Had the trader withdrawn ₹ 3,600 instead of ₹ 6,000, he would have left with ₹ 14,400, the fund required to buy 6,000 units at ₹ 2.40 per unit.

Example 3 (Physical Capital Maintenance)

In the previous example (Example 1) suppose that the price of the product at the end of year is ₹ 2.50 per unit. In other words, the specific price index applicable to the product is 125.

Current cost of opening stock = (₹ 12,000 / 100) x 125 = 6,000 x ₹ 2.50 = ₹ 15,000
Current cost of closing cash = ₹ 12,000 (₹ 18,000 – ₹ 6,000)
Opening equity at closing current costs = ₹ 15,000
Closing equity at closing current costs = ₹ 12,000
Retained Profit = ₹ 12,000 – ₹ 15,000 = (-) ₹ 3,000

The negative retained profit indicates that the trader has failed to maintain his capital. The available fund ₹ 12,000 is not sufficient to buy 6,000 units again at increased price ₹ 2.50 per unit. The drawings should have been restricted to ₹ 3,000 (₹ 6,000 – ₹ 3,000).

Had the trader withdrawn ₹ 3,000 instead of ₹ 6,000, he would have left with ₹ 15,000, the fund required to buy 6,000 units at ₹ 2.50 per unit.

Question 1 *(Inter July 2021) (5 Marks)*

A trader commenced business on April 1, 2020 with ₹ 120,000, represented by 6000 units of a certain product at ₹ 20 per unit. During the year 2020-21 he sold these units at ₹ 30 per unit & had withdrawn ₹ 60,000. The price of the product at end of financial year was ₹ 25 per unit. Compute retained profit of trader under concept of physical capital maintenance at current cost. Also state, whether answer would be different if trader had not withdrawn any amount.

Solution

Physical Capital Maintenance at Current Cost

In the given case, the specific price index applicable to the product is 125 (25/20X100).

Current cost of opening stock = (₹ 1,20,000/100) x 125 Or 6,000 units x ₹ 25	₹ 1,50,000
Current cost of closing cash (₹ 1,80,000 – ₹ 60,000)	₹ 1,20,000
Opening equity at closing current costs	₹ 1,50,000
Closing equity at closing current costs	₹ 1,20,000
Retained Profit = ₹ 1,20,000 – ₹ 1,50,000	(-) ₹ 30,000

The negative retained profit indicates that the trader has failed to maintain his capital. The available fund of ₹ 1,20,000 is not sufficient to buy 6,000 units again at increased price of ₹ 25 per unit. The drawings should have been restricted to ₹ 30,000 (₹ 60,000 – ₹ 30,000).

If the trader had not withdrawn any amount, then the answer would have been as below:

Current cost of opening stock	₹ 1,80,000
Opening equity at closing current costs	₹ 1,50,000
Retained Profit (₹ 1,80,000 – ₹ 1,50,000)	₹ 30,000

If the trader had not withdrawn any amount, then the retained profit would have been₹ 30,000.

Question 2 *(ICAI Study Material)*

Balance sheet of a trader on 31st March, 2021 is given below

Liabilities	Amount	Assets	Amount
Capital	60,000	Property, Plant & Equipment	65,000
Profit and Loss Account	25,000	Stock	30,000
10% Loan	35,000	Trade receivables	20,000
Trade payables	10,000	Deferred costs	10,000
		Bank	5,000
	1,30,000		1,30,000

Additional information:

a) The remaining life of Property, Plant & Equipment is 5 years. The pattern of use of the asset is even. The net realisable value of Property, Plant & Equipment on 31.03.22 was ₹ 60,000.

b) The trader's purchases & sales in 2021-22 amounted to ₹ 4 lakh and ₹ 4.5 lakh respectively.

c) The cost and net realisable value of stock on 31.03.22 were ₹ 32,000 & ₹ 40,000 respectively.

d) Expenses (including interest on loan) for the year amounted to ₹ 14,900.

e) Deferred cost is amortised equally over 4 years.

f) Debtors on 31.03.22 is ₹ 25,000, of which ₹ 2,000 is doubtful. Collection of another ₹ 4,000 depends on successful re-installation of certain product supplied to the customer.

g) Closing trade payable is ₹ 12,000, which is likely to be settled at 5% discount.

h) Cash balance on 31.03.22 is ₹ 37,100.

i) There is an early repayment penalty for the loan ₹ 2,500.

Prepare the Profit and Loss Accounts and Balance Sheets of the trader in two cases

(i) assuming going concern (ii) not assuming going concern

Solution

Profit and Loss Account for the year ended 31st March, 2022

	Case (i)	Case (ii)		Case (i)	Case (ii)
To Opening Stock	30,000	30,000	By Sales	4,50,000	4,50,000
To Purchases	4,00,000	4,00,000	By Closing Stock	32,000	40,000
To Expenses	14,900	14,900	By Trade payables	-	600
To Depreciation	13,000	5,000			
To Provision for doubtful debts	2,000	6,000			
To Deferred cost	2,500	10,000			
To Loan penalty	-	2,500			
To Net Profit (b.f.)	19,600	22,200			
	4,82,000	4,90,600		4,82,000	4,90,600

Balance Sheet as at 31st March, 2022

Liabilities	Case (i)	Case (ii)	Assets	Case (i)	Case (ii)
Capital	60,000	60,000	Property, Plant & Equipment	52,000	60,000
Profit and Loss A/c	44,600	47,200	Stock	32,000	40,000
10% Loan	35,000	37,500	Trade receivables (less provision)	23,000	19,000
Trade payables	12,000	11,400	Deferred costs	7,500	-
			Bank	37,100	37,100
	1,51,600	1,56,100		1,51,600	1,56,100

Question 3 *(Inter Dec 2021) (5 Marks)*

Mrs. A is showing the consolidated aggregate opening balance of equity, liabilities and assets of ₹ 6 lakh, 4 lakh and 10 lakh respectively. During the current year Mrs. A has the following transactions:

1. Received 20% dividend on 10,000 equity shares of ₹ 10 each held as investment.
2. The amount of ₹ 70,000 is paid to creditors for settlement of ₹ 90,000.
3. Salary is pending by ₹ 20,000.
4. Mrs. A's drawing ₹ 20,000 for her personal use.

You are required to prepare the statement of the effect of aforesaid each transaction on closing balance sheet in the form of Assets – Liabilities = Equity after each transaction.

Solution

Effect of each transaction on Balance sheet of Mrs. A is shown below:

Transactions	Assets	–	Liabilities	=	Equity (₹ lakh)
Opening	10.00	–	4.00	=	6.00
(1) Dividend earned	10.20 [10.00+0.20]	–	4.00	=	6.20 [6.00+0.20]
(2) Settlement of Creditors	9.50 [10.20-0.70]	–	3.10 [4.00-0.90]	=	6.40 [6.20+0.20]
(3) Salary Outstanding	9.50	–	3.30 [3.10+0.20]	=	6.20 [6.40-0.20]
(4) Drawings	9.30 [9.50-0.20]	–	3.30	=	6.00 [6.20-0.20]

Question 4 *(Inter May 2019) (5 Marks)/ (RTP May 2022) / (RTP Nov 2022)*

Summarised Balance Sheet of Cloth Trader as on 31.03.2021 is given below

Liabilities	Amount	Assets	Amount
Capital	3,00,000	Property, Plant & Equipment	360,000
Profit and Loss Account	1,25,000	Stock	1,50,000
10% Loan	2,10,000	Debtors	1,00,000
Creditors	50,000	Deferred Expenses	50,000
		Cash & Bank	25,000
	6,85,000		6,85,000

Additional Information is as follows:

(1) The remaining life of Property, Plant & Equipment is 8 years. The pattern of use of asset is even. The net realisable value of Property, Plant & Equipment on 31.03.2022 was 3,25,000

(2) Purchases and Sales in 2021-22 amounted to ₹ 22,50,000 and ₹ 27,50,000 respectively.

(3) Cost & net realizable value of stock on 31.03.2022 were ₹2,00,000 & ₹2,50,000 respectively.

(4) Expenses for the year amounted to ₹ 78,000.

(5) Deferred Expenses are amortized equally over 5 years.

(6) Sundry Debtors on 31.03.22 are 1,50,000 of which 5,000 is doubtful. Collection of another 25,000 depends on successful re-installation of certain product supplied to the customer;

(7) Closing Sundry Creditors are ₹ 75,000, likely to be settled at 10% discount.

(8) Cash balance as on 31.03.2022 is ₹ 4,22,000.

(9) There is an early repayment penalty for the loan of ₹ 25,000.

You are required to prepare: (Not assuming going concern)

(1) Profit & Loss Account for the year 2021-22.

(2) Balance Sheet as on 31st March, 2022.

Solution

Profit and Loss Account for the year ended 31st March, 2022 (not assuming going concern)

	Amount		Amount
To Opening Stock	1,50,000	By Sales	27,50,000
To Purchases	22,50,000	By Closing Stock	2,50,000
To Expenses*	78,000	By Trade payables	7,500
To Depreciation	35,000		
To Provision for doubtful debts	30,000		
To Deferred cost	50,000		
To Loan penalty	25,000		
To Net Profit (b.f.)	3,89,500		
	30,07,500		30,07,500

Balance Sheet as at 31st March, 2022 (not assuming going concern)

Liabilities	Amount	Assets	Amount
Capital	3,00,000	Property, Plant & Equipment	3,25,000
Profit and Loss Account	5,14,500	Stock	2,50,000
10% Loan	2,35,000	Trade receivables (less provision)	1,20,000
Trade payables	67,500	Deferred costs	Nil
		Bank	4,22,000
	11,17,000		11,17,000

*Assumed that ₹ 78,000 includes interest on 10% loan amount for the year.

Question 5 *(Inter Jan 2021) (5 Marks)*

Explain how financial capital is maintained at historical cost?
Kishore started a business on 1st April, 2021 with ₹ 15,00,000 represented by 75,000 units of ₹ 20 each. During the financial year ending on 31st March, 2022, he sold the entire stock for ₹ 30 each. In order to maintain the capital intact, calculate the maximum amount, which can be withdrawn by Kishore in the year 2021-22 if Financial Capital is maintained at historical cost.

Solution

Financial capital maintenance at historical cost: Under this convention, opening and closing assets are stated at respective historical costs to ascertain opening and closing equity. If retained profit is greater than or equals to zero, the capital is said to be maintained at historical costs. This means the business will have enough funds to replace its assets at historical costs. This is quite right as long as prices do not rise.
Maximum amount which can be withdrawn by Kishore in year 2021-22 if Financial capital is maintained at historical cost

Particulars	₹
Closing equity (₹ 30 x 75,000 units)	22,50,000 represented by cash
Opening equity	75,000 units x ₹ 20 = 15,00,000
Permissible drawings to keep Capital intact	7,50,000 (22,50,000 – 15,00,000)

Thus ₹ 7,50,000 is the maximum amount that can be withdrawn by Kishore in year 2021-22 if Financial capital is maintained at historical cost.

Question 6 *(Inter Nov 2020) (5 Marks)*

Following is the Balance Sheet of M/s. S Traders as on 31st March, 2021:

Liabilities	Amount	Assets	Amount
Capital	1,50,000	Fixed Assets	1,05,000
Profit and Loss Account	56,000	Stock	76,000
11% Bank Loan	80,000	Debtors	68,000
Trade Payables	52,000	Deferred Expenses	24,000
		Cash & Bank	65,000
	3,38,000		3,38,000

Additional Information:

(i) Remaining life of Fixed Assets is 6 years with even use. The net realizable value of Fixed Assets as on 31st March, 2022 is ₹ 90,000.

(ii) Firm's Sales & Purchases for the year ending 31st March, 2022 amounted to ₹ 7,80,000 and ₹ 6,25,000 respectively.

(iii) The cost & net realizable value of the stock as on 31st March, 2022 was, ₹ 60,000 and ₹ 66,000 respectively.

(iv) General expenses (including interest on Loan) for the year 2021-22 were ₹ 53,800.

(v) Deferred expenditure is normally amortised equally over 5 years starting from the Financial year 2020-21 i.e. ₹ 6,000 per year.

(vi) Debtors on 31st March, 2022 is ₹ 65,000 of which ₹ 5,000 is doubtful. Collection of another ₹ 10,000 debtors depends on successful re-installation of certain products supplied to the customer.

(vii) Closing Trade payable ₹ 48,000, which is likely to be settled at 5% discount.

(viii) There is a prepayment penalty of ₹ 4,000 for Bank loan outstanding.

(ix) Cash & Bank balances as on 31st March, 2022 is ₹ 1,65,200.

Prepare Profit & Loss Account for the year ended 31st March, 2022 and Balance Sheet as on 31st March, 2022 assuming the firm is not a going concern

Solution

Profit and Loss Account for the year ended 31st March, 2022 (not assuming going concern)

	Amount		Amount
To Opening Stock	76,000	By Sales	7,80,000
To Purchases	6,25,000	By Closing Stock	66,000
To General Expenses	53,800	By Trade payables	2,400
To Depreciation	15,000		
To Provision for doubtful debts	15,000		
To Deferred expenses	24,000		
To Loan penalty	4,000		
To Net Profit (b.f.)	35,600		
	8,48,400		8,48,400

Balance Sheet as at 31st March, 2022 (not assuming going concern)

Liabilities	Amount	Assets	Amount
Capital	1,50,000	Fixed Assets	90,000
Profit and Loss Account 56,000+35,600	91,600	Stock	66,000
11% Loan	84,000	Trade receivables (less provision)	50,000
Trade payables	45,600	Deferred costs	Nil
		Cash & Bank	1,65,200
	3,71,200		3,71,200

Question 7 *(Inter Nov 2022) (5 Marks)*

As on 1st April, 2021 opening Balance Sheet of Mr. Mohanty is showing the aggregate value of Assets, Liabilities and Equity ₹ 12 Lakhs, 3 Lakhs and 9 lakhs respectively.

During the accounting period 01/04/2021 to 31/03/2022, Mr. Mohanty has the following transactions:

(a) A liability of ₹ 50,000 was finally settled at a discount of 2%.
(b) Dividend earned @ 15% on 1,000 (F.V 100 each) Equity shares held @ ₹ 12,000.
(c) Rent of the premises paid ₹ 20,000.
(d) Mr. Mohanty withdrew ₹ 10,000 for personal purposes and also withdrew Goods worth ₹ 5,000 for personal purposes.
(e) ₹ 15,000 were received against Bill Receivables.

You are required to show the effect of the above transactions on Balance Sheet in the form of Assets – Liabilities = Equity equation after each transaction.

Solution

Effects of each transaction on Balance sheet of the trader is shown below:

Transactions	Assets	–	Liabilities	=	Equity
	₹ lakh		₹ lakh		₹ lakh
Opening	12	–	3	=	9
(1) Settlement of	12 – 0.49 = 11.51	–	3 – 0.50 = 2.5	=	9.0 + 0.01 = 9.01

Creditors					
(2) Dividend earned	11.51 + 0.15 = 11.66	–	2.5	=	9.01+0.15 = 9.16
(3) Rent paid	11.66 -0.20 = 11.46	–	2.5	=	9.16 -0.20 = 8.96
(4) Drawings	11.46 -0.15 = 11.31	–	2.5	=	8.96 -0.15 = 8.81
(5) *Money received against B/R	11.31+0.15 -0.15 = 11.31	–	2.5	=	8.81

*No change as cash received from bills receivable will have impact on individual asset only (will reduce bill receivables with corresponding increase in cash)

Question 8 – *(Inter May 2023) (5 Marks)* *Pg no._____*

Mille started a business on 01.04.2022 with a capital of ₹ 15,00,000. She purchased 1,500 units of stock at ₹ 1,000 each. She sold the entire stock for ₹ 1,500 each unit till 31.03.2023.
You are required to calculate the maximum amount which can be withdrawn by Mille in order to keep her capital intact, if Financial Capital is maintained at:

a. Historical Cost
b. Current Purchasing Power (opening index at 100 and closing index at 125)
c. Physical Capital Maintenance (Price per unit at the end of year is ₹ 1,350)

Solution

Financial Capital Maintenance at historical Costs

Sr. No.	Particulars	Computation	₹
(i)	Opening Equity	1,500 x 1,000	15,00,000
(ii)	Closing Equity	1,500 x 1,500	22,50,000
(iii)	Maximum Drawing	(ii)-(i)	7,50,000

Financial Capital Maintenance at current purchasing power

Sr. No.	Particulars	Computation	₹
(i)	Opening Equity	1,500 x 1,000 x 125/100	18,75,000
(ii)	Closing Equity	1,500 x 1,500	22,50,000
(iii)	Maximum Drawing	(ii)-(i)	3,75,000

Financial Capital Maintenance at Physical Capital Maintenance

Sr. No.	Particulars	Computation	₹
(i)	Opening Equity	1,500 x1,350	20,25,000
(ii)	Closing Equity	1,500 x 1,500	22,50,000
(iii)	Maximum Drawing	(ii)-(i)	2,25,000

INTRODUCTION TO ACCOUNTING STANDARDS

Generally Accepted Accounting Principles (GAAP)	• GAAP refer to a common set of accepted accounting principles, standards, and procedures that business reporting entity must follow when it prepares and present its financial statements. • It's a combination of authoritative standards (set by policy boards) & the commonly accepted ways of recording & reporting accounting information • At international level such authoritative standards are known as International Financial Reporting Standards (IFRS) and in India we have authoritative standards named as AS and IND-AS.
Meaning of AS	Accounting standards are written policy documents issued by expert accounting body or by government with the support of other regulatory bodies [*e.g. MCA issuing AS for companies in consultation with NFRA (National Financial Reporting Authority)]* covering the aspects of recognition, measurement, presentation and disclosure of accounting transactions in the financial statements.
Issues dealt by AS	➢ Recognition of events and transactions in the financial statements. ➢ Measurement of these transactions and events. ➢ Presentation of these transactions & events in financial statements in a manner that is meaningful and understandable to the reader. ➢ The disclosure requirements which should be there to enable public at large, the stakeholders and potential investors in particular, to get an insight in to what these financial statements are trying to reflect and thereby facilitating them to take prudent and informed business decisions.
Objectives	➢ The primary objective is to establish standards which have to be complied with to ensure that the financial statements are prepared in accordance with generally accepted accounting principles. ➢ To provide standard for the diverse accounting policies and principles. ➢ To eliminate the non-comparability of financial statements. ➢ To increase/improve the reliability of the financial statements. ➢ To provide standards which are transparent for users.
Benefits	➢ Standardization of alternative accounting treatment (Reduce/ eliminate the confusing variations in the accounting treatments used to prepare the financial statements) ➢ Requirement for additional disclosures. (disclosures which are not statutorily required) ➢ Comparability of financial statements.
Limitations	➢ Difficulties in making choice between different treatments. ➢ Lack of flexibilities ➢ Restricted scope (accounting standards cannot override the statute)

Standards setting process	ICAI has constituted the Accounting Standard Board (ASB) in 1977. ASB is responsible for setting accounting standards. Although ASB is a body constituted by council of ICAI, it is independent in the formulation of accounting standards and council of ICAI is not empowered to make any modifications in the draft AS formulated by ASB without consulting with the ASB.
Process	➢ Identification of area (where standardization is required) ➢ Constitution of study groups (for research) ➢ Preparation of draft and its circulation ➢ Ascertainment of views of different bodies on draft (like SEBI, CBDT, C&AG) ➢ Finalization of exposure draft ➢ Comments reviewed on exposure draft (public comments) ➢ Modification of the draft ➢ Issue of AS • For Non Corporate Entities by ICAI • For Corporate Entities by Ministry of Corporate Affairs in consultation with NFRA

NEED FOR CONVERGENCE TOWARDS GLOBAL STANDARDS

SIGNIFICANCE:

- Global Standards facilitate cross border flow of money, global listing in different stock markets and comparability of financial statements.
- The convergence of financial reporting and Accounting Standards is a valuable process that contributes to the free flow of global investment and achieves substantial benefits for all capital market stakeholders.
- It improves the ability of investors to compare investments on a global basis and, thus, lower their risk of errors of judgment.
- It facilitates accounting and reporting for companies with global operations and eliminates some costly requirements say reinstatement of financial statements.

INTERNATIONAL FINANCIAL REPORTING STANDARDS AS GLOBAL STANDARDS

BECOMING IFRS COMPLIANT

Any country can become IFRS compliant *either* by adoption process or convergence process.
Adoption would mean that the country sets a specific timetable when specific entities would be required to use IFRS as issued by the IASB.
Convergence means that the country will develop high quality, compatible accounting standards over time. Convergence means alignment of the standards of different standard setters with a certain rate of compromise, by adopting the requirements of the standards either fully or partially. Indian Accounting Standards are almost similar to IFRS but with few carve outs so as to make them suitable for Indian Environment.
Convergence with IFRS will result in following benefits:

- Improves investor confidence across the world with transparency and comparability
- Improves inter-unit/ inter-firm/inter-industry comparison
- Group consolidation will be easy with same standard by all companies in group irrespective of their global location.
- Acceptability of financial statements stock exchanges across the globe, which will facilitate entry of any Indian company to any stock exchange.

ISSUE OF IND AS

The Government of India in consultation with the ICAI decided to converge and not to adopt IFRS issued by the IASB. The decision of convergence rather than adoption was taken after the detailed analysis of IFRS requirements and extensive discussion with various stakeholders.

Accordingly, while formulating IFRS converged Indian Accounting Standards (Ind AS), efforts have been made to keep these Standards, as far as possible, in line with the corresponding IAS/IFRS and departures have been made where considered absolutely essential.

Indian Accounting Standards (Ind AS) are IFRS converged standards issued by the Central Government of India under the supervision and control of Accounting Standards Board (ASB) of ICAI and in consultation with NFRA.

CARVE OUTS/INS IN IND AS

- Various terminology related changes have been made to make it consistent with the terminology used in law, e.g., 'statement of profit and loss' in place of 'statement of comprehensive income' and 'balance sheet' in place of 'statement of financial position'.
- Certain changes have been made considering the economic environment of the country, which is different as compared to the economic environment presumed to be in existence by IFRS. These differences are due to differences in economic conditions prevailing in India. These differences which are in deviation to the accounting principles and practices stated in IFRS, are commonly known as 'Carve-outs'.
- Additional guidance given in Ind AS over and above what is given in IFRS, is termed as 'Carve in'

ROADMAP FOR IMPLEMENTATION OF INDAS:

For Companies other than Banks, NBFCs and Insurance Companies

1st April 2016: Mandatory Basis

(a) Companies listed/in process of listing on Stock Exchanges in India or Outside India having net worth of INR 500 crore or more;
(b) Unlisted Companies having net worth of INR 500 crore or more;
(c) Parent, Subsidiary, Associate and JV of above.

Phase II: 1st April 2017: Mandatory Basis

(a) All companies which are listed/or in process of listing on Stock Exchanges in India or outside India not covered in Phase I (other than companies listed on SME Exchanges);
(b) Unlisted companies having net worth of INR 250 crore or more but less than INR 500 crore;
(c) Parent, Subsidiary, Associate and JV of above.

Special Points to Consider:-

- Companies listed on SME exchange are not required to apply Ind AS. Such companies shall continue to apply existing ASs unless they choose otherwise.
- Once Ind AS are applicable, an entity shall be required to follow the Ind AS for all the subsequent financial statements i.e. there is no looking back once the Ind AS are adopted by companies.
- Companies not covered by the above roadmap shall continue to apply Accounting Standards notified in Companies (Accounting Standards) Rules, 2006 (2021 revised)

APPLICABILITY OF ACCOUNTING STANDARDS

Enterprises to which Accounting Standards apply

Accounting Standards apply in respect of any enterprise (whether organized in corporate, cooperative or other forms) engaged in commercial, industrial or business activities, whether or not profit oriented and even if established for charitable or religious purposes.

AS however, do not apply to enterprises solely carrying on the activities, which are not of commercial, industrial or business nature, (e.g., an activity of collecting donations and giving them to flood affected people). Exclusion of an enterprise from the applicability of the AS would be permissible only if no part of the activity of such enterprise is commercial, industrial or business in nature.

Even if a very small proportion of activities of an enterprise were considered to be commercial, industrial or business in nature, the AS would apply to all its activities including those, which are not commercial, industrial or business in nature

Criteria for classification of Non-company entities by ICAI

For the purpose of applicability of Accounting Standards, Non-company entities are classified into four categories, viz., Level I, Level II, Level III and Level IV.

Level I entities are large size entities, Level II entities are medium size entities, Level III entities are small size entities and Level IV entities are micro entities. Level IV, Level III and Level II entities are referred to as Micro, Small and Medium size entities (MSMEs).

Level	Criterion
Level I Entities	Non-company entities which fall in any one or more of the following categories, at the end of the relevant accounting period, are classified as Level I entities: (i) Entities whose securities are listed or are in the process of listing on any stock exchange, whether in India or outside India. (ii) Banks (including co-operative banks), financial institutions or entities carrying on insurance business. (iii) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds ₹ 250 crore in the immediately preceding accounting year. (iv) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of ₹ 50 crore at any time during the immediately preceding accounting year. (v) Holding and subsidiary entities of any one of the above.
Level II Entities	Non-company entities which are not Level I entities but fall in any one or more of the following categories are classified as Level II entities: (i) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds ₹ 50 crore but does not exceed ₹ 250 crore in the immediately preceding accounting year. (ii) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of ₹ 10 crore but not in excess of ₹ 50 crore at any time during the immediately preceding accounting year. (iii) Holding and subsidiary entities of any one of the above.

Level III Entities	Non-company entities which are not Level I and Level II entities but fall in any one or more of the following categories are classified as Level III entities: (i) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds ₹ 10 crore but does not exceed ₹ 50 crore in the immediately preceding accounting year. (ii) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of ₹ 2 crore but not in excess of ₹ 10 crore at any time during the immediately preceding accounting year. (iii) Holding and subsidiary entities of any one of the above.
Level IV Entities	Non-company entities which are not covered under Level I, Level II and Level III are considered as Level IV entities

Note:

Where an entity has been covered in Level I & subsequently, ceases to be so covered and gets covered in Level II or Level III or Level IV, the entity will not qualify for exemption/ relaxation available to that Level, until the entity ceases to be covered in Level I for *2 consecutive years*. Similar is the case in respect of an entity, which has been covered in Level II or Level III and subsequently, gets covered under Level III or Level IV.

EXEMPTIONS or RELAXATIONS FOR NON-COMPANY ENTITIES FALLING IN LEVEL II / LEVEL III AND LEVEL IV

	Level II	Level III	Level IV
AS not Applicable	AS 3, AS 17, AS 20, AS 21, AS 23, AS 25, AS 27	AS 3, AS 17, AS 18, AS 20, AS 21, AS 23, AS 24, AS 25, AS 27	AS 3, AS 14, AS 17, AS 18, AS 20, AS 21, AS 23, AS 24, AS 25, AS 27, AS 28
AS applicable with Disclosure Exemptions	AS 19, AS 28, AS 29	AS 10, AS 11, AS 19, AS 28, AS 29	AS 10, AS 11, AS 13, AS 19, AS 26, AS 29
Applicable with Exemptions	AS 15	AS 15	AS 15, AS 22

AS 21, 23, 25 & 27 is applicable only if a Non-company entity is required or elects to prepare and present consolidated financial statements or interim financial report.

CRITERIA FOR CLASSIFICATION OF COMPANIES AS PER COMPANIES (ACCOUNTING STANDARDS) RULES, 2021

Company	Criterion
SMC *(Inter Nov 2023) (5 Marks)*	Small and Medium-Sized Company (SMC) as defined in Clause 2(e) of the Companies (Accounting Standards) Rules, 2021: "Small and Medium Sized Company" (SMC) means, a company- (i) whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India; (ii) which is not a bank, financial institution or an insurance company; (iii) whose turnover (excluding other income) does not exceed ₹ 250 crore in the immediately preceding accounting year; (iv) which does not have borrowings (including public deposits) in excess of ₹ 50 crore at any time during immediately preceding accounting year; and (v) which is not a holding or subsidiary company of a company which is not a small and medium-sized company. Explanation: For the purposes of clause 2(e), a company shall qualify as a Small and Medium Sized Company, if the conditions mentioned therein are satisfied as at the end of the relevant accounting period
Non-SMCs	Companies not falling within the definition of SMC are considered as Non- SMCs.

Same Additional requirements for Companies as was for non Companies

AS not applicable to SMC's in their entirety
AS 17 Segment Reporting AS 21* Consolidated Financial Statements AS 23* Accounting for Investments in Associates in Consolidated Financial Statements AS 25* Interim Financial Reporting AS 27* Financial Reporting of Interests in Joint Ventures *Applicable to only certain Non SMC's
AS in respect of which relaxations from certain requirements given to SMCs
AS 15 Employee Benefits AS 19 Leases AS 20 Earnings Per Share AS 28 Impairment of Assets AS 29 Provisions, Contingent Liabilities and Contingent Assets