

CA INTER

ADVANCED ACCOUNTING (MODULE - 1)

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1. PREPARATION OF FINANCIAL STATEMENTS

ILLUSTRATIONS

Illustration 1

Due to inadequacy of profits during the year ended 31st March, 20X2, XYZ Ltd. proposes to declare 10% dividend out of general reserves. From the following particulars, ascertain the amount that can be utilised from general reserves, according to the Companies (Declaration of dividend out of Reserves) Rules, 2014:

	Rs.
17,500 9% Preference shares of Rs.100 each, fully paid up	17,50,000
8,00,000 Equity shares of Rs.10 each, fully paid up	80,00,000
General Reserves as on 1.4.20X1	25,00,000
Capital Reserves as on 1.4.20X1	3,00,000
Revaluation Reserves as on 1.4.20X1	3,50,000
Net profit for the year ended 31 st March, 20X2	3,00,000
Average rate of dividend during the last three years has been 12%.	

Solution:

Amount that can be drawn from reserves for 10% dividend		Rs.8,00,000
10% dividend on Rs.80,00,000		
Profits available		
Current year profit	3,00,000	
Less: Preference dividend	(1,57,500)	(1,42,500)
Amount which can be utilised from reserves		6,57,500

Conditions as per Companies (Declaration of dividend out of Reserves) Rules, 20X1:

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. Rs.12,25,000 [10% of (80,00,000+17,50,000+25,00,000)]

Condition III

The balance of reserves after drawl Rs.18,42,500 (Rs.25,00,000 - Rs.6,57,500) should not fall below 15 % of its paid up capital ie. Rs.14,62,500 (15% of Rs.97,50,000)

Since all the three conditions are satisfied, the company can withdraw Rs.6,57,500 from accumulated reserves (as per Declaration and Payment of Dividend Rules, 2014.)

Illustration 2

The following is the Trial Balance of Omega Limited as on 31.3.20X2:

(Figures in Rs.'000)

	Debit		Credit
Land at cost	220	Equity Capital (Shares of Rs.10 each)	300
Plant & Machinery at cost	770	10% Debentures	200
Trade Receivables	96	General Reserve	130
Inventories (31.3.X2)	86	Profit & Loss A/c	72
Bank	20	Securities Premium	40
Adjusted Purchases	320	Sales	700
Factory Expenses	60	Trade Payables	52
Administration Expenses	30	Provision for Depreciation	172
Selling Expenses	30	Suspense Account	4
Debenture Interest	20		
Interim Dividend Paid	18		
	1670		1670

Additional Information:

- (i) The authorised share capital of the company is 40,000 shares of Rs.10 each.
- (ii) The company on the advice of independent valuer wish to revalue the land at Rs.3,60,000.
- (iii) Declared final dividend @ 10% on 2nd April, 20X2.
- (iv) Suspense account of Rs.4,000 represents cash received for the sale of some of the machinery on 1.4.20X1. The cost of the machinery was Rs.10,000 and the accumulated depreciation thereon being Rs.8,000.
- (v) Depreciation is to be provided on plant and machinery at 10% on cost.

You are required to prepare Omega Limited's Balance Sheet as on 31.3.20X2 and Statement of Profit and Loss with notes to accounts for the year ended 31.3.20X2 as per Schedule III. Ignore previous years' figures & taxation.

Solution:

Omega Limited

Balance Sheet as at 31st March, 20X2

Particulars	Note No.	(Rs.in 000)
Equity and Liabilities		
1. Shareholders' funds		
A Share capital	1	300
B Reserves and Surplus	2	530

2. Non-Current liabilities		
A Long term borrowings		
3. Current liabilities	3	200
A Trade Payables		
Total		<u>52</u>
Assets		<u>1082</u>
1. Non-current assets		
A PPE (Property, Plant & Equipment)		
2. Current assets	4	880
A Inventories		
B Trade receivables		86
C Cash and bank balances		96
Total		<u>20</u>
		<u>1082</u>

Omega Limited

Statement of Profit and Loss for the year ended 31st March, 20X2

Particulars	Notes	(Rs.in 000)
I. Revenue from operations		700
II. Other Income	5	<u>2</u>
III Total Income		<u>702</u>
IV Expenses:		
Purchases		320
Finance costs	6	20
Depreciation (10% of 760*)		76
Other expenses	7	<u>120</u>
Total Expenses		<u>536</u>
V. Profit (Loss) for the period (III – IV)		166

Notes to accounts

		(Rs.in 000)
1.	Share Capital	
	Equity share capital	
	Authorised	
	40,000 shares of Rs.10 each	<u>400</u>
	Issued & subscribed & called up	
	30,000 shares of Rs.10 each	300
2.	Reserves and Surplus	

	Securities Premium Account			40
	Revaluation reserve (360 – 220)			140
	General reserve			130
	Profit & loss Balance			
	Opening balance	72		
	Profit for the period	<u>166</u>	238	
	Less: Appropriations			
	Interim Dividend		<u>(18)</u>	<u>220</u>
				<u>530</u>
3.	Long term borrowing			
	10% Debentures			200
4.	PPE			
	Land			
	Opening balance		220	
	Add: Revaluation adjustment		<u>140</u>	
	Closing balance			360
	Plant and Machinery			
	Opening balance		770	
	Less: Disposed off		<u>(10)</u>	
			760	
	Less: Depreciation (172-8+76)		<u>(240)</u>	
	Closing balance			520
	Total			880
5.	Other Income			
	Profit on sale of machinery:			
	Sale value of machinery		4	
	Less: Book value of machinery (10-8)		<u>(2)</u>	2
6.	Finance costs			
	Debenture interest			20
7.	Other expenses:			
	Factory expenses		60	
	Selling expenses		30	
	Administrative expenses		<u>30</u>	120

Note: 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, 20X2. Such dividends will be disclosed in notes only.

Illustration 3

You are required to prepare Balance sheet and statement of Profit and Loss from the following trial balance of Haria Chemicals Ltd. for the year ended 31st March, 20X1.

Haria Chemicals Ltd.

Trial Balance as at 31st March, 20X1

Particulars	Rs.	Particulars	Rs.
Inventory	6,80,000	Equity Shares	
Furniture	2,00,000	Capital (Shares of Rs.10 each)	25,00,000
Discount	40,000	11% Debentures	5,00,000
Loan to Directors	80,000	Bank loans	6,45,000
Advertisement	20,000	Trade payables	2,81,000
Bad debts	35,000	Sales	42,68,000
Commission	1,20,000	Rent received	46,000
Materials consumed	23,19,000	Transfer fees	10,000
Plant and Machinery	8,60,000	Profit & Loss account	1,39,000
Rentals	25,000	Depreciation provision:	
Current account	45,000	Machinery	1,46,000
Cash	8,000		
Interest on bank loans	1,16,000		
Preliminary expenses	10,000		
Fixtures	3,00,000		
Wages	9,00,000		
Consumables	84,000		
Freehold land	15,46,000		
Tools & Equipment	2,45,000		
Goodwill	2,65,000		
Trade receivables	4,40,000		
Dealer aids	21,000		
Transit insurance	30,000		
Trade expenses	37,000		
Distribution freight	54,000		
Debenture interest	55,000		
	85,35,000		85,35,000

Additional information: Closing Inventory on 31-3-20X1: Rs.8,23,000.

Solution:

Haria Chemicals Ltd.

Balance Sheet as at 31st March, 20X1

	Schedule	Rupees as at the
	No. (1)	end of 31st March 20X1 (2)
Equity and Liabilities		
(1) Shareholders' funds :		
(a) Share Capital	1	25,00,000
(b) Reserves and Surplus	2	7,40,000
(2) Non Current Liabilities		
(a) Long term borrowings	3	11,45,000
(3) Current Liabilities		
(a) Trade payables		2,81,000
Total		46,66,000

Assets

(1) Non current assets		
(a) PPE	4	30,05,000
(b) Intangible assets (goodwill)		2,65,000
(2) Current assets		
(a) Inventories		8,23,000
(b) Trade receivables		4,40,000
(c) Cash and bank balances	5	53,000
(d) Short term loans and advances	6	80,000
Total		46,66,000

Haria Chemicals Ltd.

Statement of Profit and Loss for the year ended 31st March, 20X1

	Schedule	Figures	
Revenue from operations		42,68,000	
Other income	7	<u>56,000</u>	
	(A)	43,24,000	
Expenses			
Cost of materials consumed		23,19,000	
Change in inventory of finished goods	8	(1,43,000)	
Employee benefit expenses	9	9,00,000	
Finance cost	10	1,71,000	

Other expenses		11	<u>4,76,000</u>	
	(B)		<u>37,23,000</u>	
Profit before tax (A – B)				6,01,000
Provision for tax				—
Profit for the period				6,01,000

Notes to Accounts

1. Share capital		Rs.
Authorised:		
Equity share capital of Rs.10 each		<u>25,00,000</u>
Issued and Subscribed:		
Equity share capital of Rs.10 each		25,00,000
2. Reserves and Surplus		
Balance as per last balance sheet		1,39,000
Balance in profit and loss account		<u>6,01,000</u>
		<u>7,40,000</u>
3. Long term Borrowings		
11% Debentures		5,00,000
Bank loans (assumed long-term)		<u>6,45,000</u>
		<u>11,45,000</u>
4. PPE		
Gross block Depreciation Net Block		
Freehold land 15,46,000		15,46,000
Furniture 2,00,000		2,00,000
Fixtures 3,00,000		3,00,000
Plant & Machinery 8,60,000	1,46,000	7,14,000
Tools & Equipment <u>2,45,000</u>		<u>2,45,000</u>
Total 31,51,000	1,46,000	30,05,000
5. Cash and bank balances		
Cash and cash equivalents		
Current account balance		45,000
Cash		8,000
Other bank balances		<u>Nil</u>
		<u>53,000</u>

6. Short-term loans and Advances		
Loan to directors		80,000

7. Other Income		
Rent received		46,000
Transfer fees		<u>10,000</u>
		<u>56,000</u>
8. Changes in inventory of finished goods, WIP & Stock in trade		
Opening inventory	6,80,000	
Closing inventory	<u>(8,23,000)</u>	<u>(1,43,000)</u>
9. Employee benefit expense		
Wages		9,00,000
10. Finance cost		
Interest on bank loans		1,16,000
Debenture interest		<u>55,000</u>
		<u>1,71,000</u>
11. Other Expenses		
Consumables		84,000
Preliminary expenses		10,000
Bad debts		35,000
Discount		40,000
Rentals		25,000
Commission		1,20,000
Advertisement		20,000
Dealers' aids		21,000
Transit insurance		30,000
Trade expenses		37,000
Distribution freight		<u>54,000</u>
		<u>4,76,000</u>

Illustration 4

You are required to prepare a Statement of Profit and Loss and Balance Sheet from the following Trial Balance extracted from the books of the International Hotels Ltd., on 31st March, 20X2:

	Dr.	Cr.
	Rs.	Rs.
Authorised Capital-divided into 5,000 6% Preference Shares of Rs.100 each and 10,000 equity Shares of Rs.100 each		<u>15,00,000</u>
Subscribed Capital -		
5,000 6% Preference Shares of Rs.100 each		5,00,000

Equity Capital		8,05,000
Purchases - Wines, Cigarettes, Cigars, etc.	45,800	
- Foodstuffs	36,200	
Wages and Salaries	28,300	
Rent, Rates and Taxes	8,900	
Laundry	750	
Sales - Wines, Cigarettes, Cigars, etc.		68,400
- Food		57,600
Coal and Firewood	3,290	
Carriage and Cooliage	810	
Sundry Expenses	5,840	
Advertising	8,360	
Repairs	4,250	
Rent of Rooms		48,000
Billiard		5,700
Miscellaneous Receipts		2,800
Discount received		3,300
Transfer fees		700
Freehold Land and Building	8,50,000	
Furniture and Fittings	86,300	
Inventory on hand, 1st April, 20X1		
Wines, Cigarettes. Cigars, etc.	12,800	
Foodstuffs	5,260	
Cash in hand	2,200	
Cash with Bankers	76,380	
Preliminary and formation expenses	8,000	
2,000 Debentures of Rs.100 each (6%)		2,00,000
Profit and Loss Account		41,500
Trade payables		42,000
Trade receivables	19,260	
Investments	2,72,300	
Goodwill at cost	5,00,000	
General Reserve		<u>2,00,000</u>
	<u>19,75,000</u>	<u>19,75,000</u>
Wages and Salaries Outstanding	1,280	

Inventory on 31st March, 20X2			
Wines, Cigarettes and Cigars, etc.	22,500		
Foodstuffs	16,400		

Depreciation: Furniture and Fittings @ 5% p.a.: Land and Building @ 2% p.a.

The Equity capital on 1st April, 20X1 stood at Rs.7,20,000, that is 6,000 shares fully paid and 2,000 shares Rs.60 paid. The directors made a call of Rs.40 per share on 1st October 20X1. A shareholder could not pay the call on 100 shares and his shares were then forfeited and reissued @ Rs.90 per share as fully paid. The Directors declared a dividend of 8% on equity shares on 2nd April, 20X2, transferring any amount that may be required from General Reserve. Ignore Taxation.

Solution:

Balance Sheet of International Hotels Ltd. as at 31st March, 20X2

Particulars	Note No	Rs.
Equity and Liabilities		
1 Shareholders' funds		
a Share capital	1	13,00,000
b Reserves and Surplus	2	2,68,745
2 Non-current liabilities		
a Long-term borrowings	3	2,00,000
3 Current liabilities		
a Trade Payables	4	42,000
b Other current liabilities	5	13,280
Total		18,24,025
ASSETS		
1 Non-current assets		
i PPE	6	9,14,985
ii Intangible assets (Goodwill)		5,00,000
iii Non-current investments		2,72,300
2 Current assets		
i Inventories	7	38,900
ii Trade receivables		19,260
iii Cash and bank balances	8	78,580
Total		18,24,025

Statement of Profit and Loss of International Hotels Ltd. for the year ended 31st March, 20X2

	Particulars	Notes	Amount
I.	Revenue from operations	9	1,79,700
II.	Other income	10	6,800

III.	Total Income (I + II)		1,86,500
IV.	Expenses:		
	Cost of materials consumed	11	25,060
	Purchases of Inventory-in-Trade	12	45,800
	Changes in inventories of finished goods work-	13	(9,700)
	in-progress and Inventory-in-Trade		
	Employee benefits expense	14	29,580
	Finance costs	15	12,000
	Other expenses	16	40,200
	Depreciation and amortisation expense	17	21,315
	Total expenses		1,64,255
V.	Profit (Loss) for the period (III - IV)		22,245

Notes to accounts

		Rs.
1 Share Capital		
Equity share capital		
Authorised		
10,000 Equity shares of Rs.100 each		
Issued & subscribed		10,00,000
8,000 Equity Shares of Rs.100 each (A)		
Preference share capital		8,00,000
Authorised		
5,000 6% Preference shares of Rs.100 each		5,00,000
Issued & subscribed		
5,000 6% Preference shares of Rs.100 each (B)		5,00,000
Total (A + B)		13,00,000
Reserves and Surplus		
2 Capital reserve [100 x (90 – 40)] General reserve		5,000
Surplus (Profit & Loss A/c)		2,00,000
Add: Balance from previous year	22,245	
Total	<u>41,500</u>	<u>63,745</u>
3 Long-term borrowings		2,68,745
Secured		
6% Debentures		2,00,000
Total		2,00,000
4 Trade Payables		42,000

5 Other current liabilities		
Wages and Salaries Outstanding	1,280	
Interest on debentures	12,000	13,280
Total		13,280
6 PPE		
Freehold land & Buildings	8,50,000	
Less: Depreciation	(17,000)	8,33,000
Furniture and Fittings	86,300	
Less: Depreciation	(4,315)	81,985
Total		9,14,985
7 Inventories		
Wines, Cigarettes & Cigars, etc.		22,500
Foodstuffs		16,400
		38,900
8 Cash and bank balances	Total	
Cash and cash equivalents		
Cash at bank		76,380
Cash in hand		2,200
Other bank balances		Nil
		78,580
9 Revenue from operations	Total	
Sale of products		
Wines, Cigarettes, Cigars etc.	68,400	
Food	<u>57,600</u>	1,26,000
Sale of services		
Room Rent	48,000	
Billiards	<u>5,700</u>	53,700
	Total	1,79,700
10 Other Income		
Transfer fees	700	
Miscellaneous Receipts	2,800	
Discount received	<u>3,300</u>	
	Total	6,800
11 Cost of materials consumed		
Opening Inventory	5,260	
Add: Purchases during the year	36,200	



Less: Closing Inventory	(16,400)	25,060
Total		25,060
12 Purchases of Inventory-in-Trade		
Wines, Cigarettes etc.		45,800
Total		45,800
13 Changes in inventories of finished goods work-in-progress and Inventory-in-Trade Wines, Cigarettes etc.		
Opening Inventory	12,800	
Less: Closing Inventory Total	(22,500)	(9,700)
Total		(9,700)
14 Employee benefits expense		
Wages and Salaries	28,300	
Add: Wages and Salaries Outstanding	1,280	29,580
Total		29,580
15 Finance costs		
Interest on Debentures (2,00,000 x 6%)		12,000
16 Other expenses operating expenses		
Rent, Rates and Taxes	8,900	
Coal and Firewood	3,290	
Laundry	750	
Carriage and Cooliage	810	
Repairs	4,250	18,000
Selling and administrative expenses		
Advertising	8,360	
Sundry Expenses	5,840	14,200
Preliminary expenses written off		8,000
Total		40,200
17 Depreciation and amortisation expense		
Land and Buildings (8,50,000 x 2%)	17,000	
Furniture & Fittings (86,300 x 5%)	4,315	21,315
Total		21,315

Note: 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, 20X2. Such dividends will be disclosed in notes only.

Illustration 5

From the following particulars furnished by Pioneer Ltd., prepare the Balance Sheet as at 31st March, 20X1 as required by Schedule III of the Companies Act. Give notes at the foot of the Balance Sheet as may be found necessary -

	Debit Rs.	Credit Rs.
Equity Capital (Face value of Rs.100)		10,00,000
Calls in 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
Inventory:		
Finished Goods	2,00,000	
Raw Materials	<u>50,000</u>	2,50,000
Provision for Taxation		68,000
Trade receivables	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
Trade payables (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) Trade receivables of Rs.52,000 are due for more than six months.
- (3) The cost of assets:

Building	Rs.4,00,000
Plant and Machinery	Rs.7,00,000
Furniture	Rs.62,500

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

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

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

Solution:

Pioneer Ltd.

Balance Sheet as at 31st March, 20X1

Particulars		Notes	Rs.
Equity and Liabilities Shareholders' funds			
1	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
	Assets		18,94,700
1	Non-current assets		
	a PPE	6	11,25,000
2	Current assets		
	a Inventories	7	2,50,000
	b Trade receivables	8	2,00,000
	c Cash and bank balances	9	2,77,000
	d Short-term loans and advances		42,700
	Total		18,94,700

Notes to accounts

	Rs.
1 Share Capital	
Equity share capital	
Issued & subscribed & called up	
10,000 Equity Shares of Rs.100 each (Of the above 2,000 shares have been issued for consideration other than cash)	10,00,000
Less: Calls in arrears	<u>(1,000)</u>
Total	9,99,000
2 Reserves and Surplus	
General Reserve	2,10,000
Surplus (Profit & Loss A/c)	<u>86,700</u>

	Total		<u>2,96,700</u>
3 Long-term borrowings			
Secured- Term Loans			
Loan from State Financial Corporation (1,50,000 – 7,500)			1,42,500
(Secured by hypothecation of Plant and Machinery)			
Unsecured loan			<u>1,21,000</u>
	Total		<u>2,63,500</u>
4 Other current liabilities			
Interest accrued but not due on loans (SFC)			7,500
Dividend Payable			<u>60,000</u>
	Total		<u>67,500</u>
5 Short-term provisions			
Provision for taxation			<u>68,000</u>
	Total		<u>68,000</u>
6 PPE			
Land			2,00,000
Buildings		4,00,000	
Less: Depreciation		<u>(50,000) (b.f.)</u>	3,50,000
Plant & Machinery		7,00,000	
Less: Depreciation		<u>(1,75,000) (b.f.)</u>	5,25,000
Furniture & Fittings		62,500	
Less: Depreciation		<u>(12,500) (b.f.)</u>	<u>50,000</u>
	Total		<u>11,25,000</u>
7 Inventories			
Raw Material			50,000
Finished goods			<u>2,00,000</u>
	Total		<u>2,50,000</u>
8 Trade receivables			
Debts outstanding for a period exceeding six months			52,000
Other Debts			<u>1,48,000</u>
	Total		<u>2,00,000</u>
9 Cash and bank balances			
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

Other bank balances		Nil
Total		2,77,000

Note: Estimated amount of contract remaining to be executed on capital account and not provided for Rs.1,50,000. It has been assumed that the company had given this contract for purchase of machinery.

Illustration 6

Following is the trial balance of Delta limited as on 31.3.20X2.

(Figures in Rs.'000)

Particulars	Debit	Particulars	Credit
Land at cost	800	Equity share capital	500
		(shares of Rs.10 each)	
Calls in arrears	5	10% Debentures	300
Cash in hand	2	General reserve	150
Plant & Machinery at cost	824	Profit & Loss A/c (balance on 1.4.X1)	75
Trade receivables	120	Securities premium	40
Inventories (31-3-X2)	96	Sales	1200
Cash at Bank	28	Trade payables	30
Adjusted Purchases	400	Provision for depreciation	150
Factory expenses	80	Suspense Account	10
Administrative expenses	45		
Selling expenses	25		
Debenture Interest	30		
	2455		2455

Additional Information:

- The authorized share capital of the company is 80,000 shares of Rs.10 each.
- The company revalued the land at Rs.9,60,000.
- Equity share capital includes shares of Rs.50,000 issued for consideration other than cash.
- Suspense account of Rs.10,000 represents cash received from the sale of some of the machinery on 1.4.20X1. The cost of the machinery was Rs.24,000 and the accumulated depreciation thereon being Rs.20,000. The balance of Plant & Machinery given in trial balance is before adjustment of sale of machinery.
- Depreciation is to be provided on plant and machinery at 10% on cost.
- Balance at bank includes Rs.5,000 with ABC Bank Ltd., which is not a Scheduled Bank.
- Make provision for income tax @30%.
- Trade receivables of Rs.50,000 are due for more than six months.

You are required to prepare Delta Limited's Balance Sheet as at 31.3.20X2 and Statement of Profit
CA Inter | P1 Advanced Accounting | Question Bank(M1) | CA Sai Babu

and Loss with notes to accounts for the year ended 31.3.20X2 as per Schedule III. Ignore previous year's figures & taxation.

Solution:

Delta Limited
Balance Sheet as at 31st March 20X2

Particulars	Note No.	(Rs.in '000)
A. Equity and Liabilities		
1. Shareholders' funds		
(a) Share Capital	1	495.00
(b) Reserves and Surplus	2	807.20
2. Non-Current Liabilities		
(a) Long Term Borrowings	3	300.00
3. Current Liabilities		
(a) Trade Payables		30.00
(b) Short- term provision	4	<u>163.80</u>
Total		<u>1,796.00</u>
B. Assets		
1. Non-Current Assets		
(a) Property, Plant and Equipment	5	1,550.00
2. Current Assets		
(a) Inventories		96.00
(b) Trade Receivables	6	120.00
(c) Cash and Cash equivalents	7	<u>30.00</u>
Total		<u>1,796.00</u>

Statement of Profit and Loss for the year ended 31st March 20X2

Particulars	Note No.	(Rs.in '000)
I. Revenue from Operations		1200.00
II. Other Income	8	<u>6.00</u>
III. Total Income (I +II)		<u>1,206.00</u>
IV. Expenses:		
Purchases (adjusted)		400.00
Finance Costs	9	30.00
Depreciation (10% of 800)		80.00
Other expenses	10	<u>150.00</u>
Total Expenses		<u>660.00</u>
V. Profit / (Loss) for the period before tax (III – IV)		546.00

VI. Tax expenses @30%		<u>163.80</u>
VII Profit for the period		<u>382.20</u>

Notes to Accounts

	Particulars		(Rs.in '000)
1	Share Capital		
	Equity Share Capital		
	Authorised		
	80,000 Shares of Rs.10/- each		<u>800</u>
	Issued, Subscribed and Called-up		
	50,000 Shares of Rs.10/- each	500	
	(Out of the above 5,000 shares have been issued for consideration other than cash)		
	Less: Calls in arrears	<u>(5)</u>	495
2	Reserves and Surplus		
	Securities Premium		
	Revaluation Reserve Rs.(960 – 800)		40.00
	General Reserve		160.00
	Surplus i.e. Profit & Loss Account Balance		150.00
	Opening Balance	75.00	
	Add: Profit for the period	<u>382.20</u>	<u>457.20</u>
			<u>807.20</u>
3	Long-Term Borrowings		
	10% Debentures		300
4.	Short – term provision		
	Provision for tax		163.80
5	Property, plant & equipment		
	Land		
	Opening Balance	800	
	Add: Revaluation adjustment	<u>160</u>	960
	Closing Balance		
	Plant and Machinery		
	Opening Balance	824	
	Less: Disposed off	<u>(24)</u>	
		800	
	Less: Depreciation Rs.(150 – 20 + 80)	<u>(210)</u>	
	Closing Balance		<u>590</u>
	Total		<u>1,550</u>

6	Trade receivables		
	Debits outstanding for a period exceeding six months	50	
	Other debts	<u>70</u>	120
7	Cash and Cash Equivalents		
	Cash at Bank With scheduled banks	23	
	With others (ABC Bank Limited)	5	
	Cash in hand	<u>2</u>	30
8	Other Income		
	Profit on sale of machinery		
	Sale value of machinery	10	
	Less: Book value of machinery (24 – 20)	<u>(4)</u>	6
9	Finance Costs		
	Debenture Interest		30
10	Other Expenses:		
	Factory expenses	80	
	Selling expenses	25	
	Administrative expenses	<u>45</u>	150



TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. Trade payables as per Schedule III will include:
 - (a) Dues payable in respect to statutory obligation
 - (b) Interest accrued on trade payables
 - (c) Bills payables.
 - (d) Bills receivables

2. Securities Premium Account is shown on the liabilities side in the Balance Sheet under the heading:
 - (a) Reserves and Surplus.
 - (b) Current Liabilities.
 - (c) Share Capital.
 - (d) Share application money pending allotment

3. "Fixed assets held for sale" will be classified in the company's balance sheet as
 - (a) Current asset
 - (b) Non-current asset
 - (c) Capital work- in- progress
 - (d) Deferred tax assets

4. Current maturities of long- term debt will come under
 - (a) Current Liabilities.
 - (b) Short term borrowings.
 - (c) Long term borrowings.
 - (d) Short term provisions

5. Declaration of dividends for current year is made after providing for
 - (a) Depreciation of past years only.
 - (b) Depreciation on assets for the current year and arrears of depreciation of past years (if any).
 - (c) Depreciation on current year only and by forgoing arrears of depreciation of past years.
 - (d) Excluding current year depreciation



Answer to the Multiple Choice Questions

1.	(c)	2.	(a)	3.	(a)	4.	(b)	5.	(b)

THEORETICAL QUESTIONS

6. State under which head these accounts should be classified in Balance Sheet, as per Schedule III of the Companies Act, 2013:
- i) Share application money received in excess of issued share capital.
 - ii) Share option outstanding account.
 - iii) Unpaid matured debenture and interest accrued thereon.
 - iv) Uncalled liability on shares and other partly paid investments.
 - v) Calls unpaid.
 - vi) Money received against share warrant.

Answer:

- i) Current Liabilities/ Other Current Liabilities
- ii) Shareholders' Fund / Reserve & Surplus
- iii) Current liabilities/Other Current Liabilities
- iv) Contingent Liabilities and Commitments
- v) Shareholders' Fund / Share Capital
- vi) Shareholders' Fund / Money received against share warrants



SCENARIO BASED QUESTIONS

7. On 31st March, 20X1 Bose and Sen Ltd. provides to you the following ledger balances after preparing its Profit and Loss Account for the year ended 31st March, 20X1:

Credit Balances:

	Rs.
Equity shares capital, fully paid shares of Rs.10 each	70,00,000
General Reserve	15,49,100
Loan from State Finance Corporation (Secured by hypothecation of Plant & Machinery Repayable within one year Rs.2,00,000)	10,50,000
Loans: Unsecured (Long term)	8,47,000
Sundry Creditors for goods & expenses (Payable within 6 months)	14,00,000
Profit & Loss Account	7,00,000
Provision for Taxation	8,16,900
	1,33,63,000

Debit Balances:

	Rs.
Calls in arrear	7,000
Land	14,00,000
Buildings	20,50,000
Plant and Machinery	36,75,000
Furniture & Fixture	3,50,000
Inventories: Finished goods	14,00,000
Raw Materials	3,50,000
Trade Receivables	14,00,000
Advances: Short-term	2,98,900
Cash in hand	2,10,000
Balances with banks	17,29,000
Preliminary Expenses	93,100
Patents & Trademarks	4,00,000
	1,33,63,000

The following additional information is also provided in respect of the above balances:

- (i) 4,20,000 fully paid equity shares were allotted as consideration for land & buildings.
- (ii) Cost of Building Rs.28,00,000
- (iii) Cost of Plant & Machinery Rs.49,00,000 Cost of Furniture & Fixture Rs.4,37,500

- (iv) Trade receivables for Rs.3,80,000 are due for more than 6 months.
- (v) The amount of Balances with Bank includes Rs.18,000 with a bank which is not a scheduled Bank and the deposits of Rs.5 lakhs are for a period of 9 months.
- (vi) Unsecured loan includes Rs.2,00,000 from a Bank and Rs.1,00,000 from related parties.
- (vii) Entire amount of Preliminary expenses to be written off, by adjusting from opening balance of General Reserve.

You are not required to give previous year's figures. You are required to prepare the Balance Sheet of the Company as on 31st March, 20X1 as required under Schedule III to the Companies Act, 2013.

Answer:

Bose and Sen Ltd.

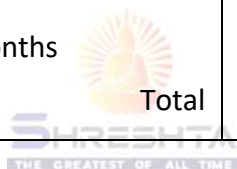
Balance Sheet as at 31st March, 20X1

Particulars		Notes	Figures at the end of current reporting period (Rs.)
Equity and Liabilities			
1	Shareholders' funds		
a	Share capital	1	69,93,000
b	Reserves and Surplus	2	21,56,000
2	Non-current liabilities		
a	Long-term borrowings	3	16,97,000
3	Current liabilities		
a	Trade Payables		14,00,000
b	Short term borrowings Short-term provisions	4	2,00,000
c	Total	5	8,16,900
			1,32,62,900
Assets			
1	Non-current assets		
a	PPE	6	74,75,000
b	Intangible assets (Patents & Trade Marks)		4,00,000
2	Current assets		
a	Inventories	7	17,50,000
b	Trade receivables	8	14,00,000
c	Cash and bank balances	9	19,39,000
d	Short-term loans and advances		2,98,900
	Total		1,32,62,900

Notes to accounts

			Rs.
1	Share Capital Equity share capital Issued, subscribed and called up 7,00,000 Equity Shares of Rs.10 each (Out of the above 4,20,000 shares have been issued for consideration other than cash) Less: Calls in arrears Total	70,00,000 (7,000)	 <u>69,93,000</u> 69,93,000
2	Reserves and Surplus General Reserve Less: Preliminary expenses Surplus (Profit & Loss A/c) Total	15,49,100 (93,100)	 <u>7,00,000</u> <u>21,56,000</u>
3	Long-term borrowings Secured Term Loans Loan from State Finance Corporation (Rs.10,50,000 - Rs.2,00,000) (Secured by hypothecation of Plant and Machinery) Unsecured Bank Loan Loan from related parties Others Total	 2,00,000 1,00,000 <u>5,47,000</u>	 <u>8,47,000</u> <u>16,97,000</u>
4	Short term borrowings Current maturities of long-term debt- loan Instalment repayable within one year		 2,00,000
5	Short-term provisions Provision for taxation		 8,16,900
6	Property, plant and equipment Land Buildings Less: Depreciation Plant & Machinery Less: Depreciation Furniture & Fittings	 28,00,000 (7,50,000) (b.f.) 49,00,000 (12,25,000)(b.f.) 4,37,500	 14,00,000 20,50,000 36,75,000

	Less: Depreciation	(87,500) (b.f.)	3,50,000
	Total		74,75,000
7	Inventories		
	Raw Material		3,50,000
	Finished goods		14,00,000
	Total		17,50,000
8	Trade receivables		
	Debts outstanding for a period exceeding six months		3,80,000
	Other Debts		10,20,000
	Total		14,00,000
9	Cash and bank balances		
	Cash and cash equivalents		
	Cash at bank with Scheduled Banks	12,11,000	
	with others	18,000	12,29,000
	Cash in hand		2,10,000
	Other bank balances		
	Bank deposits for period of 9 months		5,00,000
	Total		19,39,000



8. From the following particulars furnished by Alpha Ltd., prepare the Balance Sheet as on 31st March 20X1 as required by Part I, Schedule III to the Companies Act, 2013.

Particulars		Debit Rs.	Credit Rs.
Equity Share Capital (Face value of Rs. 100 each)			50,00,000
Call in Arrears		5,000	
Land & Building		27,50,000	
Plant & Machinery		26,25,000	
Furniture		2,50,000	
General Reserve			10,50,000
Loan from State Financial Corporation			7,50,000
Inventory:			
Raw Materials	2,50,000		
Finished Goods	<u>10,00,000</u>	12,50,000	
Provision for Taxation			6,40,000

Trade receivables		10,00,000	
Short term Advances		2,13,500	
Profit & Loss Account			4,33,500
Cash in Hand		1,50,000	
Cash at Bank		12,35,000	
Unsecured Loan			6,05,000
Trade payables (for Goods and Expenses)			8,00,000
Loans & advances from related parties			2,00,000
		94,78,500	94,78,500

The following additional information is also provided:

- i) 10,000 Equity shares were issued for consideration other than cash.
- ii) Trade receivables of Rs.2,60,000 are due for more than 6 months.
- iii) The cost of the Assets were:
Building Rs.30,00,000, Plant & Machinery Rs.35,00,000 and Furniture Rs.3,12,500
- iv) The balance of Rs.7,50,000 in the Loan Account with State Finance Corporation is inclusive of Rs.37,500 for Interest Accrued but not Due. The loan is secured by hypothecation of Plant & Machinery.
- v) Balance at Bank includes Rs.10,000 with Omega Bank Ltd., which is not a Scheduled Bank.
- vi) Transfer Rs.20,000 to general reserve is proposed by Board of directors.
- vii) Board of directors declared dividend of 5% on the paid up capital on 2nd April, 20X1.

Answer:

Alpha Ltd.

Balance Sheet as at 31st March, 20X1

		Particulars	Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	a	Share capital	1	49,95,000
	b	Reserves and Surplus	2	14,83,500
2		Non-current liabilities		
		Long-term borrowings	3	13,17,500
3		Current liabilities		
	a	Trade Payables		8,00,000
	b	Short-term provisions	5	6,40,000
	c	Short-term borrowings	4	2,00,000
	d	Other Current Liabilities: Interest accrued but not due on loans (SFC)		<u>37,500</u>

		Total		<u>94,73,500</u>
1	Assets			
	Non-current assets			
	PPE	6		56,25,000
2	Current assets			
a	Inventories	7		12,50,000
b	Trade receivables	8		10,00,000
c	Cash and bank balances	9		13,85,000
d	Short-term loans and advances			<u>2,13,500</u>
	Total			<u>94,73,500</u>

Notes to accounts

		Rs.
1 Share Capital		
Equity share capital		
Issued & subscribed & called up 50,000 Equity Shares of Rs.100 each		
(of the above 10,000 shares have been issued for consideration other than cash)	50,00,000	
Less: Calls in arrears	<u>(5,000)</u>	<u>49,95,000</u>
Total		<u>49,95,000</u>
2 Reserves and Surplus		
General Reserve	10,50,000	
Add: current year transfer	<u>20,000</u>	10,70,000
Profit & Loss balance		
Profit for the year	4,33,500	
Less: Appropriations:	<u>(20,000)</u>	4,13,500
Transfer to General reserve		
Total		<u>14,83,500</u>
3 Long-term borrowings		
Secured Term Loan		
State Financial Corporation Loan (7,50,000-37,500)		7,12,500
(Secured by hypothecation of Plant and Machinery)		
Unsecured Loan		6,05,000
Total		<u>13,17,500</u>
4 Short term Borrowings		
Loans and advances		<u>2,00,000</u>

5 Short-term provisions		
Provision for taxation		6,40,000
6 Property, plant and equipment		
Land and Building	30,00,000	
Less: Depreciation	<u>(2,50,000) (b.f.)</u>	
Plant & Machinery	35,00,000	
Less: Depreciation	<u>(8,75,000) (b.f.)</u>	
Furniture & Fittings	3,12,500	
Less: Depreciation	<u>(62,500) (b.f.)</u>	
Total		56,25,000
7 Inventories		
Raw Materials		2,50,000
Finished goods		10,00,000
Total		12,50,000
8 Trade receivables		
Outstanding for a period exceeding six months		2,60,000
Other Amounts		7,40,000
Total		10,00,000
9 Cash and bank balances		
Cash and cash equivalents		
Cash at bank		
with Scheduled Banks	12,50,000	
with others (Omega Bank Ltd.)	10,000	12,35,000
Cash in hand		1,50,000
Other bank balances		Nil
Total		13,85,000

Note: 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, 20X1. Such dividends will be disclosed in notes only.

9. Ring Ltd. was registered with a nominal capital of Rs.10,00,000 divided into shares of Rs.100 each. The following Trial Balance is extracted from the books on 31st March, 20X2:

Particulars	Rs.	Particulars	Rs.
Buildings Machinery	5,80,000	Sales	10,40,000
Closing Stock	2,00,000	Outstanding Expenses Provision for	4,000

Loose Tools	1,80,000	Doubtful Debts (1-4-20X1)	6,000
	46,000		
Purchases (finished goods)	4,20,000	Equity Share Capital	4,00,000
Salaries	1,20,000	General Reserve	80,000
Directors' Fees	20,000	Profit and Loss A/c (1-4-20X1)	50,000
Rent	52,000		
Depreciation	40,000	Creditors	1,84,000
Bad Debts	12,000	Provision for depreciation:	
Investment	2,40,000	On Building 1,00,000	
Interest accrued on investment	4,000	On Machinery <u>1,10,000</u>	2,10,000
Debenture Interest	56,000	14% Debentures	4,00,000
Advance Tax	1,20,000	Interest on Debentures accrued but not due	28,000
Sundry expenses	36,000		
Debtors	2,50,000	Interest on Investments	24,000
Bank	60,000	Unclaimed dividend	10,000
	24,36,000		24,36,000

You are required to prepare statement of Profit and Loss for the year ending 31st March, 20X2 and Balance sheet as at that date after taking into consideration the following information:

- Closing stock is more than opening stock by Rs.1,60,000.
- Provide to doubtful debts @ 4% on Debtors.
- Make a provision for income tax @30%.
- Depreciation expense included depreciation of Rs.16,000 on Building and that of Rs.24,000 on Machinery.
- The directors declared a dividend @ 25% on 2nd April, 20X2 and transfer to General Reserve @ 10%.
- Bills Discounted but not yet matured Rs.20,000.

Answer:

Ring Ltd.

Profit and Loss Statement for the year ended 31st March, 20X2

	Particulars	Note No.	(Rs.In lacs)
I	Revenue from operations		10,40,000
II	Other income (interest on investment)		<u>24,000</u>
III	Total income [I + II]		<u>10,64,000</u>
IV	Expenses:		
	Cost of purchase [4,20,000+ 1,60,000]		5,80,000
	Changes in inventories [20,000-1,80,000]		(1,60,000)

	Employee Benefits Expense		1,20,000
	Finance Costs (debenture interest)		56,000
	Depreciation and Amortisation Expenses		40,000
	Other Expenses	8	<u>1,24,000</u>
	Total Expenses		<u>7,60,000</u>
V	Profit before Tax (III-IV)		3,04,000
VI	Tax Expenses @ 30%		(91,200)
VII	Profit for the period		2,12,800

Balance Sheet of Ring Ltd. as at 31ST March, 20X2

	Particulars	Note No.	Rs.
I	EQUITY AND LIABILITIES		
	(1) Shareholders' Funds		
	(a) Share Capital	1	4,00,000
	(b) Reserves and Surplus	2	3,42,800
	(2) Non-Current Liabilities		
	(a) Long-term Borrowings (14% debentures)		4,00,000
	(3) Current Liabilities		
	(a) Trade Payable (Sundry Creditors)		1,84,000
	(b) Other Current Liabilities	3	42,000
	(c) Short-Term Provisions	4	91,200
	Total		<u>14,60,000</u>
II	ASSETS		
	(1) Non-Current Assets		
	(a) PPE	5	5,70,000
	(b) Non-current Investments		2,40,000
	(2) Current Assets		
	(a) Inventories	6	2,26,000
	(b) Trade Receivables	7	2,40,000
	(c) Cash and bank balances		60,000
	(d) Short Term Loans and Advances (Advance Payment of Tax)		1,20,000
	(e) Other Current Assets (Interest accrued on investments)		4,000
	Total		<u>14,60,000</u>

Note: There is a Contingent Liability for bills discounted but not yet matured amounting to Rs. 20,000.

Notes to Accounts:

1.	Share Capital Authorised Capital 10,000 Equity Shares of Rs.100 each Issued Capital 4,000 Equity Shares of Rs.100 each Subscribed Capital and fully paid 4,000 Equity Shares of Rs.100 each		<u>10,00,000</u> 4,00,000 4,00,000
2.	Reserve and Surplus General Reserve [Rs.80,000 + Rs.21,280] Balance of Statement of Profit & Loss Account Opening Balance Add: Profit for the period Appropriations Transfer to General Reserve @ 10%	50,000 <u>2,12,800</u> 2,62,800 <u>(21,280)</u>	1,01,280 <u>2,41,520</u> <u>3,42,800</u>
3.	Other Current Liabilities Unclaimed Dividend Outstanding Expenses Interest accrued on Debentures		10,000 4,000 <u>28,000</u> <u>42,000</u>
4.	Short-Term Provision Provision for Tax		91,200
5	Property, plant and equipment Buildings Less: Provision for Depreciation Plant and Equipment Less: Provision for Depreciation	5,80,000 <u>1,00,000</u> 2,00,000 <u>1,10,000</u>	4,80,000 <u>90,000</u> <u>5,70,000</u>
6	Inventories Closing Stock of Finished Goods Loose Tools	1,80,000 <u>46,000</u>	<u>2,26,000</u>
7	Trade Receivables Sundry Debtors Less: Provision for Doubtful Debts	2,50,000 <u>(10,000)</u>	<u>2,40,000</u>
8.	Other Expenses Rent		52,000

Directors' Fees	20,000
Bad Debts	12,000
Provision for Doubtful Debts (4% of Rs.2,50,000 less Rs.6,000)	4,000
Sundry Expenses	36,000
	1,24,000

Note: 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, 20X2. Such dividends will be disclosed in notes only.

10. On 31st March, 20X1, SR Ltd. provides the following ledger balances after preparing its Profit & Loss Account for the year ended 31st March, 20X1.

Particulars	Amount (Rs.)	
	Debit	Credit
Equity Share Capital, fully paid shares of Rs.50 each		80,00,000
Calls in arrear	15,000	
Land	25,00,000	
Buildings	30,00,000	
Plant & Machinery	24,00,000	
Furniture & Fixture	13,00,000	
Securities Premium		15,00,000
General Reserve		9,41,000
Profit & Loss Account		5,80,000
Loan from Public Finance Corporation (Secured by Hypothecation of Land)		26,30,000
Other Long Term Loans		22,50,000
Short Term Borrowings		4,60,000
Inventories: Finished goods	45,00,000	
Raw materials	13,00,000	
Trade Receivables	17,50,000	
Advances: Short Term	3,75,000	
Trade Payables		8,13,000
Provision for Taxation		3,80,000
Unpaid Dividend		70,000
Cash in Hand	70,000	
Balances with Banks	4,14,000	
Total	1,76,24,000	1,76,24,000

The following additional information was also provided in respect of the above balances:

(1) 50,000 fully paid equity shares were allotted as consideration for land.

(2) The cost of assets were:

Building	Rs.32,00,000
Plant and Machinery	Rs.30,00,000
Furniture and Fixture	Rs.16,50,000

(3) Trade Receivables for Rs.4,86,000 due for more than 6 months.

(4) Balances with banks include Rs.56,000, the Naya bank, which is not a scheduled bank.

(5) Loan from Public Finance Corporation repayable after 3 years.

(6) The balance of Rs.26,30,000 in the loan account with Public Finance Corporation is inclusive of Rs.1,34,000 for interest accrued but not due. The loan is secured by hypothecation of land.

(7) Other long term loans (unsecured) includes:

Loan taken from Nixes Bank	Rs.13,80,000
(Amount repayable within one year	Rs.4,80,000)
Loan taken from Directors	Rs.8,50,000

(8) Bills Receivable for Rs.1,60,000 maturing on 15th June, 20X1 has been discounted.

(9) Short term borrowings includes:

Loan from Naya bank	Rs.1,16,000 (Secured)
Loan from directors	Rs.48,000

(10) Transfer of Rs.35,000 to general reserve has been proposed by the Board of directors out of the profits for the year.

(11) Inventory of finished goods includes loose tools costing Rs.5 lakhs (which do not meet definition of property, plant & equipment as per AS 10)

You are required to prepare the Balance Sheet of the Company as on March 31st 20X1 as required under Part - I of Schedule III of the Companies Act, 2013.

You are not required to give previous year figures.

Answer:

SR Ltd.

Balance Sheet as at 31st March, 20X1

Particulars	Notes	Figures at the end of current reporting period (Rs.)
Equity and Liabilities		
1 Shareholders' funds		
a Share capital	1	79,85,000
b Reserves and Surplus	2	30,21,000

2 Non-current liabilities		
a Long-term borrowings	3	42,66,000
3 Current liabilities		
a Short-term borrowings	4	9,40,000
b Trade Payables		8,13,000
c Other current liabilities	5	2,04,000
d Short-term provisions	6	3,80,000
Total		1,76,09,000
Assets		
1 Non-current assets		
a PPE	7	92,00,000
2 Current assets		58,00,000
a Inventories	8	
b Trade receivables	9	17,50,000
c Cash and cash equivalents	10	4,84,000
d Short-term loans and advances		3,75,000
Total		1,76,09,000

Notes to accounts

			Rs.
1.	Share Capital		
	Equity share capital		
	Issued, subscribed and called up 1,60,000 Equity Shares of Rs. 50 each	80,00,000	
	(Out of the above 50,000 shares have been issued for consideration other than cash)		
	Less: Calls in arrears	<u>(15,000)</u>	79,85,000
2.	Reserves and Surplus		
	General Reserve	9,41,000	
	Add: Transferred from Profit and loss account Securities premium	<u>35,000</u>	9,76,000
			15,00,000
	Surplus (Profit & Loss A/c)	5,80,000	
	Less: Appropriation to General Reserve (proposed)	<u>(35,000)</u>	<u>5,45,000</u>
			<u>30,21,000</u>
3.	Long-term borrowings		
	Secured: Term Loans		

	Loan from Public Finance Corporation [repayable after 3 years (Rs.26,30,000 - Rs.1,34,000 for interest accrued but not due)] (secured by hypothecation of land) Unsecured Bank Loan (Nixes bank) 9,00,000 (Rs.13,80,000 - Rs.4,80,000 repayable within 1 year) Loan from Directors 8,50,000 Others <u>20,000</u> Total <u>42,66,000</u>		24,96,000
4. Short-term borrowings			
	Loan from Naya bank (Secured)	1,16,000	
	Loan from Nixes bank repayable within one year (Current maturity of Long term borrowing)	4,80,000	
	Loan from Directors	48,000	
	Others	<u>2,96,000</u>	9,40,000
5. Other current liabilities			
	Unpaid dividend	70,000	
	Interest accrued but not due on borrowings	<u>1,34,000</u>	2,04,000
6. Short-term provisions			
	Provision for taxation		3,80,000
7. PPE			
	Land		25,00,000
	Buildings	32,00,000	
	Less: Depreciation	<u>(2,00,000)</u>	30,00,000
	Plant & Machinery	30,00,000	
	Less: Depreciation	<u>(6,00,000)</u>	24,00,000
	Furniture & Fittings	16,50,000	
	Less: Depreciation	<u>(3,50,000)</u>	<u>13,00,000</u>
	Total		<u>92,00,000</u>
8. Inventories			
	Raw Material	13,00,000	
	Finished goods	40,00,000	
	Loose tools	<u>5,00,000</u>	58,00,000
9. Trade receivables			
	Outstanding for a period exceeding six months		4,86,000

	Others		<u>12,64,000</u>
	Total		<u>17,50,000</u>
10.	Cash and cash equivalents		
	Balances with banks		
	with Scheduled Banks	3,58,000	
	with others banks	<u>56,000</u>	4,14,000
	Cash in hand		<u>70,000</u>
	Total		<u>4,84,000</u>

Note: There is a contingent liability amounting to Rs.1,60,000



QUESTIONS FROM RTP'S, MTP'S, QP'S

Question 1

You are required to prepare a Balance Sheet as at 31st March 2020, as per Schedule III of the Companies Act, 2013, from the following information of Mehar Ltd.:

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
Term Loans (Secured)	40,00,000	Investments (non-current)	9,00,000
Trade payables	45,80,000	Profit for the year	32,00,000
Cash and Bank Balances	38,40,000	Trade receivables	49,00,000
Staff Advances	2,20,000	Miscellaneous Expenses	2,32,000
Other advances (given by Co.)	14,88,000	Loan from other parties	8,00,000
Provision for Taxation	10,20,000	Provision for Doubtful Debts	80,000
Securities Premium	19,00,000	Stores	16,00,000
Loose Tools	2,00,000	Finished Goods	30,00,000
General Reserve	62,00,000	Plant and Machinery (WDV)	2,14,00,000

Additional Information: -

- Share Capital consists of-
 - 1,20,000 Equity Shares of Rs. 100 each fully paid up.
 - 40,000, 10% Redeemable Preference Shares of Rs. 100 each fully paid up.
- Write off the amount of Miscellaneous Expenses in full, amounting Rs. 2,32,000.

(MTP April 22 & Oct 23)

Answer :

Balance Sheet of Mehar Ltd. as at 31st March, 2020

		Note	₹
I	EQUITY AND LIABILITIES:		
(1)	(a) Share Capital	1	1,60,00,000
	(b) Reserves and Surplus	2	110,68,000
(2)	Non-current Liabilities		
	Long term Borrowings- Terms Loans (Secured)		40,00,000
(3)	Current Liabilities		
	(a) Trade Payables		45,80,000
	(b) Other current liabilities	3	8,00,000
	(c) Short-term Provisions (Provision for taxation)		10,20,000
	Total		3,74,68,000
II	ASSETS		
(1)	Non-current Assets		

	(a)	Property, Plant and Equipment	4	214,00,000
	(b)	Non– current Investments		9,00,000
(2)	Current Assets:			
	(a)	Inventories	5	48,00,000
	(b)	Trade Receivables	6	48,20,000
	(c)	Cash and Cash Equivalents		38,40,000
	(d)	Short–term Loans and Advances	7	17,08,000
		Total		3,74,68,000

Notes to accounts

			(₹)
1.	Share Capital		
	Authorized, issued, subscribed & called up		
	1,20,000, Equity Shares of ₹ 100 each	1,20,00,000	
	40,000 10% Redeemable Preference Shares of 100 each	40,00,000	1,60,00,000
2.	Reserves and Surplus		
	Securities Premium Account	19,00,000	
	General reserve	62,00,000	
	Profit & Loss Balance		
	Opening balance –		
	Profit for the period 32,00,000		
	Less: Miscellaneous Expenditure written off (2,32,000)	29,68,000	110,68,000
3.	Other current liabilities		
	Loan from other parties		8,00,000
4.	Property, plant and equipment		
	Plant and Machinery (WDV)		214,00,000
5.	Inventories		
	Finished Goods	30,00,000	
	Stores	16,00,000	
	Loose Tools	2,00,000	48,00,000
6.	Trade Receivables		
	Trade receivables	49,00,000	
	Less: Provision for Doubtful Debts	(80,000)	48,20,000
7.	Short term loans & Advances		
	Staff Advances*	2,20,000	
	Other Advances*	14,88,000	17,08,000

*Considered to be short term.

Question 2

From the following information, prepare extract of Balance Sheet of A Limited along with notes making necessary compliance of Schedule III to the Companies Act, 2013:

	Amount (₹)
Loan Funds	
(a) Secured Loans	18,12,000
(b) Unsecured Loan - Short term from bank	2,25,000
Other information is as under:	
Secured Loans	
Term Loans from:	
Banks	8,95,000
Others	9,17,000
	18,12,000
Current Maturities of long-term loan from Bank	1,24,000
Current Maturities of long- term loan from Others	85,000

There was no interest accrued / due as at the end of the year. Current maturities of long-term loans amounting ₹ 2,09,000 is included in the value of secured loans of ₹ 18,12,000. (MTP April 23)

Answer :

Extract of Balance Sheet of A Ltd

Particulars	Note No.	Amount
Non - Current Liabilities		
Long term borrowings	1	16,03,000
Current Liabilities		
Short term borrowings	2	4,34,000

Notes to Accounts

1. Long-Term Borrowings	
Term loans — Secured	
– From banks	8,95,000
– From other parties	9,17,000
	18,12,000
Less: Current maturities of long-term debt (Refer Note 3)	(2,09,000)
	16,03,000
2. Short-Term Borrowings	
(Unsecured loan)	
– from bank	2,25,000
Current maturities of long-term debt	

	– From banks	1,24,000
	– From others	85,000
		4,34,000

Question 3

The following balance appeared in the books of Oliva Ltd. as on 31-03-2022.

Particulars		₹	Particulars		₹
Inventory 01-04-2021			Sales		17,10,000
–Raw Material	30,000		Interest		3,900
–Finished goods	46,500	76,500	Profit and Loss A/c		21,000
Purchases of raw material		12,60,000	Share Capital		3,15,000
Manufacturing Expenses		2,70,000	Secured Loans:		
			Short-term	4,500	
			Long-term	21,000	25,500
			Fixed Deposits (unsecured)		
Salaries and wages		40,200	Short –term	1,500	
General Charges		16,500	Long – term	3,300	4,800
Building		1,01,000	Trade payables		3,27,000
Plant and Machinery		70,400			
Furniture		10,200			
Motor Vehicles		40,800			
Investments: Current	4,500				
Non-Current	7,500	12,000			
Trade receivables		2,38,500			
Cash in Bank		2,71,100			
		24,07,200			24,07,200

From the above balance and the following information, prepare the company's statement of Profit and Loss for the year ended 31st March, 2022 and company's Balance Sheet as on that date:

1. Inventory on 31st March, 2022– Raw material ₹ 25,800 and finished goods ₹ 60,000.
2. Outstanding Expenses: Manufacturing Expenses ₹ 67,500 & Salaries & Wages ₹ 4,500.
3. Interest accrued on Securities ₹ 300.
4. General Charges prepaid ₹ 2,490.

5. Provide depreciation: Building @ 2% p.a., Machinery @ 10% p.a., Furniture @ 10% p.a. & Motor Vehicles @ 20% p.a.

6. Current maturity of long-term loan is ₹ 1,000.

7. The Taxation provision of 40% on net profit is considered.

(RTP Nov 22)

Answer :

Oliva Ltd.

Balance Sheet as at 31.03.2022

	Particulars	Note	Amount
(1)	Equity and Liabilities		
	(i) Shareholders' funds		
	(a) Share Capital		3,15,000
	(b) Reserves and surplus	1	50,430
(2)	Non-current liabilities		
	(a) Long-term borrowings	2	23,300
(3)	Current Liabilities		
	(a) Short-term borrowings	3	7,000
	(b) Trade payables		3,27,000
	(c) Other current liability	4	72,000
	(d) Short term provision	5	19,620
II	ASSETS		8,14,350
(1)	Non-current assets		
	(a) Property, Plant & equipment	6	2,04,160
	(b) Non-current investments		7,500
(2)	Current assets		
	(a) Current investments		4,500
	(b) Inventories	7	85,800
	(c) Trade receivables		2,38,500
	(d) Cash and cash equivalents		2,71,100
	(e) Short-term loans and advances	8	2,490
	(f) Other current assets	9	300
			8,14,350

Oliva Ltd.

Statement of Profit and loss for the year ended 31.03.2022

(₹)

	Particulars	Note	Amount
I	Revenue from operations		17,10,000

II	Other income (3,900 +300)		4,200
III	Total income (I +II)		17,14,200
IV	Expenses:		
	Cost of materials consumed	10	12,64,200
	Purchases of inventory-in-trade		--
	Changes in inventories of finished goods, work-in-progress and inventory-in-Trade	11	(13,500)
	Employee benefit expenses	12	44,700
	Finance costs		--
	Depreciation and amortization expenses		18,240
	Other expenses	13	3,51,510
	Total Expenses		16,65,150
V	Profit before exceptional and extraordinary items and tax		49,050
VI	Exceptional items		--
VII	Profit before extraordinary items and tax		49,050
VIII	Extraordinary items		--
IX	Profit before tax		49,050
X	Tax expense (40% of 49,050)		19,620
XI	Profit/Loss for the period from continuing operations		29,430

Notes to accounts

No.	Particulars		Amount	Amount
1.	Reserve & Surplus			
	Profit & Loss Account: Balance b/f		21,000	
	Net Profit for the year		29,430	50,430
2.	Long term borrowings			
	Secured loans (21,000 less current maturities 1,000)		20,000	
	Fixed Deposits: Unsecured		3,300	23,300
3.	Short term borrowings			
	Secured loans		4,500	
	Fixed Deposits –Unsecured		1,500	
	Current maturities of long term borrowings		1,000	7,000
4.	Other current liabilities			
	Expenses Payable (67,500 + 4,500)		72,000	72,000
5.	Short term provisions			
	Provision for Income tax			19,620
6.	Property, plant and equipment			

	Building	1,01,000		
	Less: Depreciation @ 2%	(2,020)	98,980	
	Plant & Machinery	70,400		
	Less: Depreciation @10%	(7,040)	63,360	
	Furniture	10,200		
	Less: Depreciation @10%	(1,020)	9,180	
	Motor vehicles	40,800		
	Less: Depreciation @20%	(8,160)	32,640	2,04,160
7	Inventory			
	Raw Material		25,800	
	Finished goods		60,000	85,800
8.	Short term Loans & Advances			
	General Charges prepaid			2,490
9.	Other Current Assets			
	Interest accrued			300
10.	Cost of material consumed			
	Opening inventory of raw Material	30,000		
	Add: Purchases	12,60,000	12,90,000	
	Less: Closing inventory		(25,800)	12,64,200
11.	Changes in inventory of Finished Goods & WIP			
	Closing Inventory of Finished Goods		60,000	
	Less: Opening Inventory of Finished Goods		(46,500)	13,500
12.	Employee Benefit expenses			
	Salary & Wages (40,200 + 4,500)			44,700
13.	Other Expenses:			
	Manufacturing Expenses (2,70,000 + 67,500)		3,37,500	
	General Charges (16,500 – 2,490)		14,010	3,51,510

Question 4

The following balances are extracted from the books of Travesse Limited as on 31st March 2023:

Particulars	Amount (₹)	
	Debit	Credit
7% Debentures		48,45,000
Plant & Machinery (at cost)	37,43,400	
Trade Receivable	35,70,000	
Land	97,37,000	

Debenture Interest	3,39,150	
Bank Interest	13,260	
Sales		47,22,600
Transfer Fees		38,250
Discount received		66,300
Purchases	28,86,600	
Inventories 1.04.2022	4,97,250	
Factory Expenses	2,58,060	
Rates, Taxes and Insurance	65,025	
Repairs	1,49,685	
Sundry Expenses	1,27,500	
Selling Expenses	26,520	
Directors Fees	38,250	
Interest on Investment for the year 2022-2023		55,000
Provision for depreciation		5,96,700
Miscellaneous receipts		1,42,800

Additional information:

- (i) Closing inventory on 31.03.2023 is ₹ 4,76,850,
- (ii) Miscellaneous receipts represent cash received from the sale of the Plant on 01.04.2022. The cost of the Plant was ₹ 1,65,750 and the accumulated depreciation thereon is ₹ 24865.
- (iii) The Land is re-valued at 1,08,63,000.
- (iv) Depreciation is to be provided on Plant & Machinery at 10% p.a. on cost.
- (v) Make a provision for income tax @ 25%.
- (vi) The Board of Directors declared a dividend of 10% on Equity shares on 4th April, 2023.

You are required to prepare a Statement of Profit and Loss as per Schedule III of the Companies Act, 2013 for the year ended 31.03.2023. (Ignore previous year figures) (PYP May 23)

Answer :

Statement of Profit and Loss of Travesse Limited. for the year ended 31st March, 2023

	Particulars	Notes	Amount
I.	Revenue from operations	1	47,22,600
II.	Other income Total	2	1,61,465
III.	Income (I + II)		
IV.	Expenses:		48,84,065
	Purchases of Inventory-in-Trade		28,86,600
	Changes in inventories of finished goods, work-in progress and Inventory-in-Trade	3	20,400

	Finance costs	4	3,52,410
	Depreciation and amortization expenses	5	3,57,765
	Other expenses	6	6,65,040
	Total expenses		42,82,215
V.	Profit (Loss) for the period (III – IV) before tax		6,01,850
VI	Provision for tax		(1,50,463)
VII	Profit for the period		4,51,387

Notes to accounts

			₹
1	Revenue from operations Sale		47,22,600
2	Other Income		
	Transfer fees		38,250
	Discount received		66,300
	Interest on Investment		55,000
	Profit on sale of plant		1,915
	Total		1,61,465
3	Changes in inventories of finished goods, Work-In Progress and Inventory-in-Trade Opening Inventory	4,97,250	
	Less: Closing Inventory	(4,76,850)	20,400
	Total		20,400
	Finance costs		3,39,150
4	Interest on Debentures		
	Bank Interest		13,260
	Total		3,52,410
5	Depreciation and Amortization expenses		
	Depreciation on Plant & Machinery (10% x 37,43,400 – 1,65,750)		3,57,765
6	Other expenses		2,58,060
	Factory expense		
	Rent, Taxes and Insurance		65,025
	Repairs		1,49,685
	Sundry expenses		1,27,500
	Selling expenses		26,520
	Directors fees		38,250
Total			6,65,040

Note:

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 financial statements) as per accounting standards. Hence, it is not recognized in the financial statement for the year ending 31st March 2023. Such dividend will be disclosed in notes only.



2: CASH FLOW STATEMENTS (AS 3)

ILLUSTRATIONS

Illustration 1

Intelligent Ltd., a non-financial company has the following entries in its Bank Account. It has sought your advice on the treatment of the same for preparing Cash Flow Statement.

(i) Loans and Advances given to the following and interest earned on them:

(1) to suppliers

(2) to employees

(3) to its subsidiaries companies

(ii) Investment made in subsidiary Smart Ltd. and dividend received

(iii) Dividend paid for the year

(iv) TDS on interest income earned on investments made

(v) TDS on interest earned on advance given to suppliers

(vi) Insurance claim received against loss of fixed asset by fire Discuss in the context of AS 3 Cash Flow Statement.

Solution:

(i) Loans and advances given and interest earned

1. to suppliers

Operating Cash flow

2. to employees

Operating Cash flow

3. to its subsidiary companies

Investing Cash flow

(ii) Investment made in subsidiary company and dividend received

Investing Cash flow

(iii) Dividend paid for the year

Financing Cash Outflow

(iv) TDS on interest income earned on investments made

Investing Cash Outflow

(v) TDS on interest earned on advance given to suppliers

Operating Cash Outflow

(vi) Insurance claim received of amount loss of fixed asset by fire

Extraordinary item to be shown under a separate heading as 'Cash inflow from investing activities'.

Illustration 2

Following are extracts of the Balance Sheets of Ajay Ltd.:

	Particulars	Notes	31.3.20X1 Rs.	31.3.20X2 Rs.
	Equity and Liabilities			

	Shareholder's funds			
(a)	Share capital	1	5,00,000	5,00,000
(b)	Reserve & surplus	2	50,000	90,000
	Non-current liabilities			
(a)	Long-term borrowings	3	5,00,000	7,50,000
	Current liabilities			
(a)	Other current liabilities	4	---	5,000
	Assets			
	Non-current assets			
(a)	Intangible assets	5	2,05,000	1,80,000

Notes to accounts

		31.3.20X1 Rs.	31.3.20X2 Rs.
1	Share Capital 50,000 Equity Shares of Rs.10 each	5,00,000	5,00,000
2	Reserve & surplus Profit & Loss A/c	50,000	90,000
3	Long-term borrowings 10% Debentures	5,00,000	7,50,000
4	Other current liabilities Unpaid interest	---	5,000
5	Intangible assets Goodwill	2,05,000	1,80,000

You are required to show the related items in Cash Flow Statement.

Solution:

An Extract of Cash Flow Statement for the year ending 31.3.20X2

	Rs.
Cash flows from operating activities:	
Closing balance as per Profit & Loss A/c	90,000
Less: Opening balance as per Profit & Loss Alc	(50,000)
Add: Goodwill amortisation	25,000
Add: Interest on Debentures (Refer Note 1)	75,000
Net Cash from Operating Activities	1,40,000

Note 1: Interest has been computed on the closing balance of debentures as on 31.3.20X2 assuming that all the additions/ deletions were made, if any, at the beginning of the year.

Cash flows from financing activities:

Proceeds from debentures (Refer Working Note)	2,50,000
Interest paid on Debentures [less unpaid]	(70,000)
Net Cash from Financing Activities	1,80,000

Working Note:

10% Debentures Account

Particulars	Rs.	Particular	Rs.
To Balance c/d	7,50,000	By Balance b/d	5,00,000
		By Bank A/c (Bal. fig.)	2,50,000
	7,50,000		7,50,000

Illustration 3

From the following information, calculate cash flow from operating activities:

**Summary of Cash Account
for the year ended March 31, 20X1**

Particulars	Rs.	Particulars	Rs.
To Balance b/d	1,00,000	By Cash Purchases	1,20,000
To Cash sales	1,40,000	By Trade payables	1,57,000
To Trade receivables	1,75,000	By Office & Selling Expenses	75,000
To Trade Commission	50,000	By Income Tax	30,000
To Sale of Investment	30,000	By Investment	25,000
To Loan from Bank	1,00,000	By Repayment of Loan	75,000
To Interest & Dividend	1,000	By Interest on loan	10,000
		By Balance c/d	1,04,000
	5,96,000		5,96,000

Solution:

**Cash Flow Statement of
for the year ended March 31, 20X1(Direct Method)**

Particulars	Rs.	Rs.
Operating Activities:		
Cash received from sale of goods	1,40,000	
Cash received from Trade receivables	1,75,000	
Trade Commission received	50,000	3,65,000
Less: Payment for Cash Purchases	1,20,000	
Payment to Trade payables	1,57,000	
Office and Selling Expenses	75,000	
Payment for Income Tax	30,000	(3,82,000)

Net Cash Flow used in Operating Activities		(17,000)

Illustration 4.

The following summary cash account has been extracted from the company's accounting records:

Summary Cash Account

		(Rs. '000)
Balance at 1.3.20X1		35
Receipts from customers		2,783
Issue of shares		300
Sale of fixed assets		128
		3,246
Payments to suppliers	2,047	
Payments for property, plant & equipment	230	
Payments for overheads	115	
Wages and salaries	69	
Taxation	243	
Dividends	80	
Repayments of bank loan	250	(3,034)
Balance at 31.3.20X2		212

Prepare Cash Flow Statement of this company Hills Ltd. for the year ended 31st March, 20X2 in accordance with AS-3 (Revised).

The company does not have any cash equivalents.

Solution:

Hills Ltd.

Cash Flow Statement for the year ended 31st March, 20X2

(Using direct method)

		(Rs. '000)
Cash flows from operating activities		
Cash receipts from customers	2,783	
Cash payments to suppliers	(2,047)	
Cash paid to employees	(69)	
Other cash payments (for overheads)	(115)	
Cash generated from operations	552	
Income taxes paid	(243)	
Net cash from operating activities		309
Cash flows from investing activities		

Payments for purchase of fixed assets	(230)	
Proceeds from sale of fixed assets	128	
Net cash used in investing activities		(102)
Cash flows from financing activities		
Proceeds from issuance of share capital	300	
Bank loan repaid	(250)	
Dividend paid	(80)	
Net cash used in financing activities		(30)
Net increase in cash and cash equivalents		177
Cash and cash equivalents at beginning of period		35
Cash and cash equivalents at end of period		212

Illustration 5

Prepare cash flow statement of M/s MNT Ltd. for the year ended 31st March, 20X1 with the help of the following information:

1. Company sold goods for cash only.
2. Gross Profit Ratio was 30% for the year, gross profit amounts to Rs. 3,82,500.
3. Opening inventory was lesser than closing inventory by Rs. 35,000.
4. Wages paid during the year Rs. 4,92,500.
5. Office and selling expenses paid during the year Rs. 75,000.
6. Dividend paid during the year Rs. 30,000.
7. Bank loan repaid during the year Rs. 2,15,000 (included interest Rs. 15,000).
8. Trade payables on 31st March, 20X0 exceed the balance on 31st March, 20X1 by Rs. 25,000.
9. Amount paid to trade payables during the year Rs. 4,60,000.
10. Tax paid during the year amounts to Rs. 65,000 (Provision for taxation as on 31.03.20X1 Rs.45,000).
11. Investments of Rs. 7,00,000 sold during the year at a profit of Rs. 20,000.
12. Depreciation on fixed assets amounts to Rs. 85,000.
13. Plant and machinery purchased on 15th November, 20X0 for Rs. 2,50,000.
14. Cash and Cash Equivalents on 31st March, 20X0Rs. 2,00,000.
15. Cash and Cash Equivalents on 31st March, 20X1Rs. 6,07,500.

Solution:

M/s MNT Ltd.

Cash Flow Statement for the year ended 31st March, 20X1 (Using direct method)

Particulars	Rs.	Rs.
Cash flows from Operating Activities		
Cash sales (Rs. 3,82,500/.30)		12,75,000

Less: Cash payments for trade payables	(4,60,000)	
Wages Paid	(4,92,500)	
Office and selling expenses	(75,000)	(10,27,500)
Cash generated from operations before taxes		2,47,500
Income tax paid		(65,000)
Net cash generated from operating activities (A)		1,82,500
Cash flows from investing activities		
Sale of investments (7,00,000 + 20,000)	7,20,000	
Payments for purchase of Plant & machinery	(2,50,000)	
Net cash used in investing activities (B)		4,70,000
Cash flows from financing activities		
Bank loan repayment (including interest)	(2,15,000)	
Dividend paid	(30,000)	
Net cash used in financing activities (C)		(2,45,000)
Net increase in cash (A+B+C)		4,07,500
Cash and cash equivalents at beginning of the period		2,00,000
Cash and cash equivalents at end of the period		6,07,500

Illustration 6

Ryan Ltd provides you the following information at the year-end, March 31, 20X1:

	Rs.	Rs.
Sales		6,98,000
Cost of Goods Sold		(5,20,000)
		1,78,000
Operating Expenses		
(including Depreciation Expense of Rs. 37,000)		(1,47,000)
		31,000
Other Income / (Expenses):		
Interest Expense paid	(23,000)	
Interest Income received	6,000	
Gain on Sale of Investments	12,000	
Loss on Sale of Plant	(3,000)	
		(8,000)
		23,000
Income tax		(7,000)
		16,000

Information available:

	31st March 20X1	31st March 20X0
	Rs.	Rs.
Plant	7,15,000	5,05,000
Less: Accumulated Depreciation	(1,03,000)	(68,000)
	6,12,000	4,37,000
Investments (Long term)	1,15,000	1,27,000
Inventory	1,44,000	1,10,000
Trade receivables	47,000	55,000
Cash	46,000	15,000
Prepaid expenses	1,000	5,000
Share Capital	4,65,000	3,15,000
Reserves and surplus	1,40,000	1,32,000
Bonds	2,95,000	2,45,000
Trade payables	50,000	43,000
Outstanding liabilities	12,000	9,000
Income taxes payable	3,000	5,000

Analysis of selected accounts and transactions during 20X0-X1

1. Purchased investments for Rs. 78,000.
2. Sold investments for Rs. 1,02,000. These investments cost Rs. 90,000.
3. Purchased plant assets for Rs. 1,20,000.
4. Sold plant assets that cost Rs.10,000 with accumulated depreciation of Rs. 2,000 for Rs. 5,000.
5. Issued Rs. 1,00,000 of bonds at face value in an exchange for plant assets on 31st March, 20X1.
6. Repaid Rs. 50,000 of bonds at face value at maturity.
7. Issued 15,000 shares of Rs. 10 each.
8. Paid cash dividends Rs. 8,000.

Prepare Cash Flow Statement as per AS-3 (Revised), using indirect method.

Solution:

Ryan Ltd.

Cash Flow Statement for the year ending 31st March, 20X1

	Rs.	Rs.
Cash flows from operating activities		
Net profit before taxation	23,000	
Adjustments for:		
Depreciation	37,000	

Gain on sale of investments	(12,000)	47,000
Loss on sale of plant assets	3,000	
Interest expense	23,000	
Interest income	(6,000)	
Operating profit before working capital changes	68,000	
Decrease in trade receivables	8,000	
Increase in inventory	(34,000)	
Decrease in prepaid expenses	4,000	
Increase in trade payables	7,000	
Increase in outstanding liabilities	3,000	
Cash generated from operations	56,000	
Income taxes paid*	(9,000)	
Net cash generated from operating activities		
Cash flows from investing activities		
Purchase of plant	(1,20,000)	
Sale of plant	5,000	
Purchase of investments	(78,000)	
Sale of investments	1,02,000	
Interest received	6,000	
Net cash used in investing activities		(85,000)
Cash flows from financing activities		
Proceeds from issuance of share capital	1,50,000	
Repayment of bonds	(50,000)	
Interest paid	(23,000)	
Dividends paid	(8,000)	
Net cash from financing activities		<u>69,000</u>
Net increase in cash and cash equivalents		31,000
Cash and cash equivalents at the beginning of the period		15,000
Cash and cash equivalents at the end of the period		<u>46,000</u>

Note: Significant non-cash adjustments: Issued ₹ 1,00,000 of bonds at face value for acquisition of plant on 31st March, 20X1.

***Working Note:**

Rs.

Income taxes paid:

Income tax expense for the year

7,000

Add: Income tax liability at the beginning of the year

5,000

12,000

Less: Income tax liability at the end of the year

(3,000)

9,000

Illustration 7

The balance sheets of Sun Ltd. as at 31st March 20X1 and 20X0 were as:

Particulars	Notes	20X1 Rs.	20X0 Rs.
Equity and Liabilities			
1 Shareholder's funds			
(a) Share capital	1	60,000	50,000
(b) Reserve & surplus	2	5,000	4,000
2 Current liabilities			
(a) Trade Payables		4,000	2,500
(b) Other current liabilities	3	-	1,000
(c) Short term provision (provision for tax)		1,500	1,000
Total		70,500	58,500
Assets			
1 Non-current assets			
(a) Property, Plant & Equipment	4	39,500	29,000
2 Current assets			
(a) Current investments		2,000	1,000
(b) Inventories		17,000	14,000
(c) Trade receivables		8,000	6,000
(d) Cash & cash equivalents	5	4,000	8,500
		70,500	58,500

Notes to accounts

		20X1 Rs.	20X0 Rs.
1	Share Capital		
	Equity Shares of Rs.10 each	<u>60,000</u>	<u>50,000</u>
2	Reserve & surplus		
	Profit and Loss Account	<u>5,000</u>	<u>4,000</u>
3	Other current liabilities		
	Dividend Payable	-	<u>1,000</u>
4	Property, plant and equipment (at WDV)		
	Building	10,000	10,000
	Fixtures	17,000	11,000
	Vehicles	<u>12,500</u>	<u>8,000</u>
	Total	<u>39,500</u>	<u>29,000</u>

5	Cash and cash equivalents		
	Cash and Bank	<u>4,000</u>	<u>8,500</u>

The profit and loss statement for the year ended 31st March, 20X1 disclosed:

Particulars	Rs.
Profit before tax	4,500
Tax expense: Current tax	<u>(1,500)</u>
Profit for the year	3,000
Declared dividend	<u>(2,000)</u>
Retained Profit	1,000

Further information is available:

	Fixtures	Vehicles
	Rs.	Rs.
Depreciation for the year	1,000	2,500
Disposals:		
Proceeds on disposal of vehicles	—	1,700
Written down value	—	<u>(1,000)</u>
Profit on disposal		<u>700</u>

Prepare a Cash Flow Statement for the year ended 31st March, 20X1.

Solution:



Cash Flow Statement
for the year ended 31st March, 20X1

	Rs.	Rs.
Cash flows from operating activities		
Net Profit before taxation	4,500	
Adjustments for:		
Depreciation	3,500	
Profit on sale of vehicles (1,700 – 1,000)	(700)	
Operating profit before working capital changes	7,300	
Increase in Trade receivables	(2,000)	
Increase in inventories	(3,000)	
Increase in Trade payables	1,500	
Cash generated from operations	3,800	
Income taxes paid (W.N.1)	(1,000)	
Net cash generated from operating activities		2,800
Cash flows from investing activities		

Sale of vehicles	1,700	
Purchase of current investments	(1,000)	
Purchase of vehicles (W.N.3)	(8,000)	
Purchase of fixtures (W.N.3)	(7,000)	
Net cash used in investing activities		(14,300)
Cash flows from financing activities		
Issue of shares for cash	10,000	
Dividends paid (W.N.2)	(3,000)	
Net cash generated from financing activities		<u>7,000</u>
Net decrease in cash and cash equivalents		(4,500)
Cash and cash equivalents at beginning of period (See Note)		8,500
Cash and cash equivalents at end of period (See Note)		4,000
Note to the Cash Flow Statement		
Cash and Cash Equivalents	31.3.20X1	31.3.20X0
Bank and Cash	4,000	8,500
Cash and cash equivalents	4,000	8,500

Working Notes:

			Rs.
1. Income taxes paid			
Income tax expense for the year			1,500
Add: Income tax liability at the beginning of the year			1,000
			2,500
Less: Income tax liability at the end of the year			(1,500)
			1,000
2. Dividend paid			
Declared dividend for the year			2,000
Add: Amount payable at the beginning of the year			1,000
			3,000
Less: Amount payable at the end of the year			-
			3,000
3. Property, plant and equipment acquisitions	Fixtures	Vehicles	
	Rs.	Rs.	
W.D.V. at 31.3.20X1	17,000	12,500	
Add back:			
Depreciation for the year	1,000	2,500	
Disposals	—	1,000	

		18,000	16,000
	Less: W.D.V. at 31.12.20X0	(11,000)	(8,000)
	Acquisitions during 20X0-20X1	7,000	8,000

Note: Current investments may not be readily convertible to a known amount of cash and may not be subject to an insignificant risk of changes in value as per the requirements of AS 3 and hence those have been considered as investing activities.

Illustration 8

Ms. Jyoti of Star Oils Limited has collected the following information for the preparation of cash flow statement for the year ended 31st March, 20X1:

	(Rs. in lakhs)
Net Profit	25,000
Dividend paid	8,535
Provision for Income tax	5,000
Income tax paid during the year	4,248
Loss on sale of assets (net)	40
Book value of the assets sold	185
Depreciation charged to the Statement of Profit and Loss	20,000
Profit on sale of Investments	100
Carrying amount of Investment sold	27,765
Interest income received on investments	2,506
Interest expenses of the year	10,000
Interest paid during the year	10,520
Increase in Working Capital (excluding Cash & Bank Balance)	56,081
Purchase of Fixed assets	14,560
Investment in joint venture	3,850
Expenditure on construction work in progress	34,740
Proceeds from calls in arrear	2
Receipt of grant for capital projects	12
Proceeds from long-term borrowings	25,980
Proceeds from short-term borrowings	20,575
Opening cash and bank balance	5,003
Closing cash and bank balance	6,988

Prepare the Cash Flow Statement for the year ended 31 March 20X1 in accordance with AS 3.

(Make necessary assumptions)

Solution:

Star Oils Limited Cash Flow Statement
for the year ended 31st March, 20X1

		(Rs. in lakhs)
Cash flows from operating activities		
Net profit before taxation (25,000 + 5,000)	30,000	
Adjustments for :		
Depreciation	20,000	
Loss on sale of assets (Net)	40	
Profit on sale of investments	(100)	
Interest income on investments	(2,506)	
Interest expenses	10,000	
Operating profit before working capital changes	57,434	
Changes in working capital (Excluding cash and bank balance)	(56,081)	
Cash generated from operations	1,353	
Income taxes paid	(4,248)	
Net cash used in operating activities		(2,895)
Cash flows from investing activities		
Sale of assets (W.N.1)	145	
Sale of investments (27,765 + 100)	27,865	
Receipt of grant for capital projects	12	
Interest income on investments	2,506	
Purchase of fixed assets	(14,560)	
Investment in joint venture	(3,850)	
Expenditure on construction work-in progress	(34,740)	
Net cash used in investing activities		(22,622)
Cash flows from financing activities		
Proceeds from calls in arrear	2	
Proceeds from long-term borrowings	25,980	
Proceed from short-term borrowings	20,575	
Interest paid	(10,520)	
Dividend (including dividend tax) paid	(8,535)	27,502
Net increase in cash and cash equivalents		1,985
Cash and cash equivalents at the beginning of the period		5,003
Cash and cash equivalents at the end of the period		6,988

Working note:

1. Book value of the assets sold	185
Less : Loss on sale of assets	<u>(40)</u>
Proceeds on sale	<u>145</u>

Illustration 9

From the following Summary Cash Account of X Ltd. prepare Cash Flow Statement for the year ended 31st March, 20X1 in accordance with AS 3 (Revised) using the direct method. The company does not have any cash equivalents.

Summary Cash Account for the year ended 31.3.20X1

	Rs.'000		Rs.'000
Balance on 1.4.20X0	50	Payment to Suppliers	2,000
Issue of Equity Shares	300	Purchase of Fixed Asset	200
Receipts from Customers	2,800	Overhead expense	200
Sale of Fixed Assets	100	Wages and Salaries	100
		Taxation	250
		Dividend	50
		Repayment of Bank Loan	300
		Balance on 31.3.20X1	150
	3,250		3,250

Solution:**X Ltd.****Cash Flow Statement for the year ended 31st March, 20X1 (Using direct method)**

	Rs. '000	Rs. '000
Cash flows from operating activities		
Cash receipts from customers	2,800	
Cash payments to suppliers	(2,000)	
Cash paid to employees	(100)	
Cash payments for overheads	(200)	
Cash generated from operations	500	
Income tax paid	(250)	
Net cash generated from operating activities		250
Cash flows from investing activities		
Payments for purchase of fixed assets	(200)	
Proceeds from sale of fixed assets	100	
Net cash used in investing activities		(100)

Cash flows from financing activities		
Proceeds from issuance of equity shares	300	
Bank loan repaid	(300)	
Dividend paid	(50)	
Net cash used in financing activities		(50)
Net increase in cash		100
Cash at the beginning of the year		50
Cash at the end of the year		150

Illustration 10

Given below are the relevant extracts of the Balance Sheet and the Statement of Profit and Loss of ABC Ltd. along with additional information:

Extract of Balance sheet

		Particulars	Notes	31.3.20X1 (Rs. in lakhs)	31.3.20X0 (Rs. in lakhs)
1		Equity and Liabilities Current liabilities			
	(a)	Trade Payables		250	230
	(b)	Short term Provisions Other	1	200	180
	(c)	current liabilities	2	70	50
1		Assets Current assets			
	(a)	Inventories		200	180
	(b)	Trade Receivables Other		400	250
	(c)	current assets	3	195	180

Statement of Profit and Loss of ABC Ltd. for the year ended 31st March, 20X1

	Particulars	Notes	Rs. in lakhs
I	Revenue from operations		4,150
II	Other income	4	100
III	Total income (I + II)		4,250
	Expenses:		
	Purchases of Stock-in-Trade		2,400
	Change in inventories of finished goods		(20)
	Employee benefits expense		800
	Depreciation expense		100
	Finance cost	5	60
	Other expenses		200

IV	Total expenses		<u>3,540</u>
V	Profit before tax (III – IV)		710
VI	Tax expense: Current tax		200
VII	Profit for the year from continuing operations		510

Appropriations

Balance of Profit and Loss account brought forward	50
Transfer to general reserve	200
Dividend paid	330

Notes to accounts:

		20X1 (Rs. in lakhs)	20X0 (Rs. in lakhs)
1	Short term Provisions: Provision for Tax	<u>200</u>	<u>180</u>
2	Other current liabilities: Outstanding wages Outstanding expenses Total	50 <u>20</u> <u>70</u>	40 <u>10</u> <u>50</u>
3	Other current assets: Advance tax	<u>195</u>	<u>180</u>
4	Other income: Interest and dividend	<u>100</u>	
5	Finance cost: Interest	<u>60</u>	

Compute cash flow from operating activities using both direct and indirect method.

Solution:

Cash Flows from Operating Activities

	Rs. in lakhs	Rs. in lakhs
Using Direct Method		
Cash Receipts:		
Cash sales and collection from Trade receivables		
Sales + Opening Trade receivables – Closing Trade receivables (A)	4,150 + 250 - 400	<u>4,000</u>
Cash payments:		
Cash purchases & payment to Trade payables		
Purchases + Opening Trade payables – Closing Trade	2,400 + 230 - 250	2,380

payables		
Wages and salaries paid	800 + 40 - 50	790
Cash expenses	200 + 10 - 20	190
Taxes paid – Advance tax		195
(B)		3,555
Cash flow from operating activities (A – B)		445
Using Indirect Method		
Profit before tax		710
Add: Non-cash items : Depreciation		100
Add: Interest : Financing cash inflow		60
Less: Interest and Dividend : Investment cash outflow		(100)
Less: Tax paid		(195)
Working capital adjustments		
Trade receivables	250 - 400 (150)	(130)
Inventories	180 - 200 (20)	
Trade payables	250 - 230 20	
Outstanding wages	50 - 40 10	
Outstanding expenses	20 - 10 10	
Cash flow from operating activities		<u>445</u>

Illustration 11

Prepare Cash flow for Gamma Ltd., for the year ending 31.3.20X1 from the following information:

- (1) Sales for the year amounted to Rs. 135 crores out of which 60% was cash sales.
- (2) Purchases for the year amounted to Rs. 55 crores out of which credit purchase was 80%.
- (3) Administrative and selling expenses amounted to Rs. 18 crores and salary paid amounted to Rs. 22 crores.
- (4) The Company redeemed debentures of Rs. 20 crores at a premium of 10%. Debenture holders were issued equity shares of Rs. 15 crores towards redemption and the balance was paid in cash. Debenture interest paid during the year was Rs. 1.5 crores.
- (5) Dividend paid during the year amounted to Rs. 11.7 crores.
- (6) Investment costing Rs. 12 crores were sold at a profit of Rs. 2.4 crores.
- (7) Rs. 8 crores was paid towards income tax during the year.
- (8) A new plant costing Rs. 21 crores was purchased in part exchange of an old plant. The book value of the old plant was Rs. 12 crores but the vendor took over the old plant at a value of Rs. 10 crores only. The balance was paid in cash to the vendor.
- (9) The following balances are also provided:

	Rs. in crores 1.4.20X0	Rs. in crores 31.3.20X1
Debtors	45	50
Creditors	21	23
Bank	6	18.2

Solution:

Gamma Ltd.

Cash Flow Statement for the year ended 31st March, 20X1 (Using direct method)

Particulars	Rs. in crores	Rs. in crores
Cash flows from operating activities		
Cash sales (60% of 135)	81	
Cash receipts from Debtors [45+ (135x40%) - 50]	49	
Cash purchases (20% of 55)	(11)	
Cash payments to suppliers [21+ (55x80%) - 23]	(42)	
Cash paid to employees	(22)	
Cash payments for overheads (Adm. and selling)	(18)	
Cash generated from operations	37	
Income tax paid	(8)	
Net cash generated from operating activities		29
Cash flows from investing activities		
Sale of investments (12+ 2.40)	14.4	
Payments for purchase of fixed assets (21 - 10)	(11)	
Net cash generated from investing activities		3.4
Cash flows from financing activities		
Redemption of debentures (22-15)	(7)	
Interest paid	(1.5)	
Dividend paid	(11.7)	
Net cash used in financing activities		(20.2)
Net increase in cash		12.2
Cash at beginning of the period		6.0
Cash at end of the period		18.2

Significant non-cash items:

- (a) Debenture-holders received equity shares of ₹ 15 crores on redemption of the debentures.
- (b) Plant having book value of ₹ 12 crores was given in exchange of an asset costing ₹ 21 crores. The said plant was transferred at a value of ₹ 10 crores only, and ₹ 11 crores was paid for the balance dues towards the plant.

Illustration 12

From the following information of Mr. Zen, prepare a Cash flow statement as per AS-3 for the year ended 31.3.20X1:

Ledger balances of Mr. Zen as of 20X0 and 20X1

	As on 1.4.20X0 Rs.	As on 1.4.20X1 Rs.
Zen's Capital A/c	10,00,000	12,24,000
Trade payables	3,20,000	3,52,000
Mrs. Zen's loan	2,00,000	--
Loan from Bank	3,20,000	4,00,000
Land	6,00,000	8,80,000
Plant and Machinery (net block)	6,40,000	4,40,000
Inventories	2,80,000	2,00,000
Trade receivables	2,40,000	4,00,000
Cash	80,000	56,000

Additional information:

A machine costing Rs. 80,000 (accumulated depreciation there on Rs.24,000) was sold for Rs.40,000. The provision for depreciation on 1.4.20X0 was Rs. 2,00,000 and 31.3.20X1 was Rs.3,20,000. The net profit for the year ended on 31.3.20X1 was Rs. 3,60,000.

Solution:

Cash Flow Statement of Mr. Zen as per AS 3 for the year ended 31.3.20X1

	Rs.
(i) Cash flow from operating activities	
Net Profit (given)	3,60,000
Adjustments for	
Depreciation on Plant & Machinery (W.N.2)	1,44,000
Loss on Sale of Machinery (W.N.1)	16,000
Operating Profit before working capital changes	5,20,000
Decrease in inventories	80,000
Increase in trade receivables	(1,60,000)
Increase in trade payables	32,000
Net cash generated from operating activities	4,72,000
(ii) Cash flow from investing activities	
Sale of Machinery (W.N.1)	40,000
Purchase of Land (8,80,000 – 6,00,000)	(2,80,000)
Net cash used in investing activities	(2,40,000)

(iii) Cash flow from financing activities		
Repayment of Mrs. Zen's Loan	(2,00,000)	
Drawings (W.N.3)	(1,36,000)	
Loan from Bank	80,000	
Net cash used in financing activities		(2,56,000)
Net decrease in cash		(24,000)
Opening balance as on 1.4.20X0		80,000
Cash balance as on 31.3.20X1		56,000

Working Notes:

Plant & Machinery A/c

	Rs.		Rs.
To Balance b/d	8,40,000	By Cash – Sales	40,000
(6,40,000 + 2,00,000)		By Provision for Depreciation A/c	24,000
		By Profit & Loss A/c – Loss on Sale (80,000 – 64,000)	16,000
		By Balance c/d (4,40,000+3,20,000)	7,60,000
	8,40,000		8,40,000

Provision for depreciation on Plant and Machinery A/c

	Rs.		Rs.
To Plant and Machinery A/c	24,000	By Balance b/d	2,00,000
To Balance c/d	3,20,000	By Profit & Loss A/c (Bal. fig.)	1,44,000
	<u>3,44,000</u>		<u>3,44,000</u>

To find out Mr. Zen's drawings:

	Rs.
Opening Capital	10,00,000
Add: Net Profit	<u>3,60,000</u>
	13,60,000
Less: Closing Capital	<u>(12,24,000)</u>
Drawings	<u>1,36,000</u>

Note: Students may note that in case there is an increase in the amount of debentures/ loans during the year and the interest is required to be computed, then in such a case, students may choose either to compute interest on the closing balance of the debentures or may compute interest on opening balance for full year (in case of no repayment) and proportionate interest on additions. Suitable note for assumption may be given in the Solution: for this.

Illustration 13

Classify the following activities as (a) Operating Activities, (b) Investing Activities, (c) Financing Activities (d) Cash Equivalents.

- (a) Purchase of Machinery.**
- (b) Proceeds from issuance of equity share capital**
- (c) Cash Sales.**
- (d) Proceeds from long-term borrowings.**
- (e) Cheques collected from Trade receivables.**
- (f) Cash receipts from Trade receivables.**
- (g) Trading Commission received.**
- (h) Purchase of investment.**
- (i) Redemption of Preference Shares.**
- (j) Cash Purchases.**
- (k) Proceeds from sale of investment**
- (l) Purchase of goodwill.**
- (m) Cash paid to suppliers.**
- (n) Interim Dividend paid on equity shares.**
- (o) Wages and salaries paid.**
- (p) Proceed from sale of patents.**
- (q) Interest received on debentures held as investment.**
- (r) Interest paid on Long-term borrowings.**
- (s) Office and Administration Expenses paid**
- (t) Manufacturing Overheads paid.**
- (u) Dividend received on shares held as investments.**
- (v) Rent Received on property held as investment.**
- (w) Selling and distribution expense paid.**
- (x) Income tax paid**
- (y) Dividend paid on Preference shares.**
- (z) Underwritings Commission paid.**
- (aa) Rent paid.**
- (bb) Brokerage paid on purchase of investments.**
- (cc) Bank Overdraft**
- (dd) Cash Credit**
- (ee) Short-term Deposits**
- (ff) Highly liquid Marketable Securities (without risk of change in value)**
- (gg) Refund of Income Tax received.**



Solution:

- (a) Operating Activities: c, e, f, g, j, m, o, s, t, w, x, aa & gg.
- (b) Investing Activities: a, h, k, l, p, q, u, v, bb & ee.
- (c) Financing Activities: b, d, i, n, r, y, z, cc & dd.
- (d) Cash Equivalent: ff.

Illustration 14

X Ltd. purchased debentures of Rs.10 lacs of Y Ltd., which are redeemable within three months. How will you show this item as per AS 3 while preparing cash flow statement for the year ended on 31st March, 20X1?

Solution:

As per AS 3 on 'Cash flow Statement', cash and cash equivalents consists of cash in hand, balance with banks and short-term, highly liquid investments. If investment, of Rs.10 lacs, made in debentures is for short-term period then it is an item of 'cash equivalents'.

However, if investment of Rs.10 lacs made in debentures is for long-term period then as per AS 3, it should be shown as cash flow from investing activities.

Illustration 15

Classify the following activities as per AS 3 Cash Flow Statement:

- (i) Interest paid by financial enterprise
- (ii) Tax deducted at source on interest received from subsidiary company
- (iii) Deposit with Bank for a term of two years
- (iv) Insurance claim received towards loss of machinery by fire
- (v) Bad debts written off

Solution:

- (i) Interest paid by financial enterprise
Cash flows from operating activities
- (ii) TDS on interest received from subsidiary company
Cash flows from investing activities
- (iii) Deposit with bank for a term of two years
Cash flows from investing activities
- (iv) Insurance claim received against loss of fixed asset by fire
Extraordinary item to be shown as a separate heading under 'Cash flow from investing activities'
- (v) Bad debts written off
It is a non-cash item which is adjusted from net profit/loss under indirect method, to arrive at net cash flow from operating activity.

Illustration 16

Following is the cash flow abstract of Alpha Ltd. for the year ended 31st March, 20X1:

Cash Flow (Abstract)

Inflows	Rs.	Outflows	Rs.
Opening balance:			
Cash	10,000	Payment for Account Payables	90,000
Bank	70,000	Salaries and wages	25,000
Share capital – shares issued	5,00,000	Payment of overheads	15,000
Collection on account of Trade Receivables	3,50,000	Property, plant and equipment acquired 4,00,000	
		Debentures redeemed	50,000
Sale of Property, plant and equipment	70,000	Bank loan repaid	2,50,000
		Taxation	55,000
		Dividends	1,00,000
		Closing balance:	
		Cash	5,000
		bank	10,000
	10,00,000		10,00,000

Prepare Cash Flow Statement for the year ended 31st March, 20X1 in accordance with Accounting Standard 3.

Solution:**Cash Flow Statement for the year ended 31.3.20X1**

	Rs.	Rs.
Cash flow from operating activities		
Cash received on account of trade receivables	3,50,000	
Cash paid on account of trade payables	(90,000)	
Cash paid to employees (salaries and wages)	(25,000)	
Other cash payments (overheads)	(15,000)	
Cash generated from operations	2,20,000	
Income tax paid	(55,000)	
Net cash generated from operating activities		
Cash flow from investing activities		
Payment for purchase of Property, plant and equipment		
Proceeds from sale of Property, plant and equipment	(4,00,000)	
Net cash used in investment activities		
Cash flow from financing activities		
Proceeds from issue of share capital		

Bank loan repaid	(2,50,000)	
Debentures redeemed	(50,000)	
Dividends paid	(1,00,000)	
Net cash used in financing activities		
Net decrease in cash and cash equivalents		(65,000)
Cash and cash equivalents at the beginning of the year		80,000
Cash and cash equivalents at the end of the year		15,000

Illustration 17

Prepare Cash Flow from Investing Activities of M/s. Creative Furnishings Limited for the year ended 31-3-20X1.

Particulars	Rs.
Plant acquired by the issue of 8% Debentures	1,56,000
Claim received for loss of plant in fire	49,600
Unsecured loans given to subsidiaries	4,85,000
Interest on loan received from subsidiary companies	82,500
Pre-acquisition dividend received on investment made	62,400
Debenture interest paid	1,16,000
Term loan repaid	4,25,000
Interest received on investment	68,000
(TDS of Rs. 8,200 was deducted on the above interest)	
Book value of plant sold (loss incurred Rs. 9,600)	84,000

Solution:

Cash Flow Statement from Investing Activities of M/s Creative Furnishings Limited for the year ended 31-03-20X1

Cash generated from investing activities	Rs.	Rs.
Interest on loan received	82,500	
Pre-acquisition dividend received on investment made	62,400	
Unsecured loans given to subsidiaries	(4,85,000)	
Interest received on investments (gross value)	76,200	
TDS deducted on interest	(8,200)	
Sale of plant	74,400	
Cash used in investing activities (before extra ordinary item)		(1,97,700)
Extraordinary claim received for loss of plant		49,600
Net cash used in investing activities (after extra-ordinary item)		(1,48,100)

Note:

1. Debenture interest paid and Term Loan repaid are financing activities and, therefore, not considered for preparing cash flow from investing activities.
2. Plant acquired by issue of 8% debentures does not amount to cash outflow, hence also not considered in the above cash flow statement.

Note: For details regarding preparation of Cash Flow Statement and Problems based on practical application of AS 3, students are advised to refer unit 2 of Chapter 11.

Reference: The students are advised to refer the full text of AS 3 "Cash Flow Statement."



TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. While preparing cash flow statement, conversion of debt to equity
 - (a) Should be shown as a financing activity.
 - (b) Should be shown as an investing activity.
 - (c) Should not be shown as it is a non-cash transaction
 - (d) Should not be shown as operating activity.

2. Which of the following would be considered a 'cash-flow item from an "investing" activity'?
 - (a) Cash outflow to the government for payment of taxes.
 - (b) Cash outflow to purchase bonds issued by another company.
 - (c) Cash outflow to shareholders as dividends
 - (d) Cash outflow to make payment to trade payables.

3. All of the following would be included in a company's operating activities except:
 - (a) Income tax payments
 - (b) Collections from customers or Cash payments to suppliers
 - (c) Dividend payments
 - (d) Office and selling expenses.

4. Hari Uttam, a stock broking firm, received Rs. 1,50,000 as premium for forward contracts entered for purchase of equity shares. How will you classify this amount in the cash flow statement of the firm?
 - (a) Operating Activities.
 - (b) Investing Activities.
 - (c) Financing Activities.
 - (d) Non-cash transaction

5. As per AS 3 on Cash Flow Statements, cash received by a manufacturing company from sale of shares of ABC Company Ltd. should be classified as
 - (a) Operating activity.
 - (b) Financing activity.
 - (c) Investing activity.
 - (d) Non-cash transaction

6. Crown Ltd. wants to prepare its cash flow statement. It sold equipment of book value of Rs. 60,000 at a gain of Rs. 8,000. The amount to be reported in its cash flow statement under operating activities is

- (a) Nil
- (b) Rs. 8,000
- (c) Rs. 68,000
- (d) Rs. 60,000

7. While preparing cash flows statement, an entity (other than a financial institution) should disclose the dividends received from its investment in shares as
- (a) operating cash inflow
 - (b) investing cash inflow
 - (c) financing cash inflow
 - (d) cash & cash equivalent
8. XYZ Co. is a financial enterprise. In its cash flow statement, interest paid and dividends received should be
- (a) classified as operating cash flows.
 - (b) classified as financing cash flows.
 - (c) Not shown in cash flow statement.
 - (d) classified as investing cash flows.
9. In the cash flow statement, 'cash and cash equivalents' donot include
- (a) Bank balances .
 - (b) Short-term investments readily convertible into Cash are subject to an insignificant risk of changes in value.
 - (c) Cash balances.
 - (d) Loan from bank.
10. While preparing a Cash Flow Statement using the Indirect method as required under AS 3, which of the following will not be deducted from/added to the Net Profit to arrive at the "Cash flow from Operating activities"?
- (a) Interest income
 - (b) Gain on sale of a fixed asset.
 - (c) Depreciation.
 - (d) Gain on sale of inventory

Answer to the Multiple Choice Questions

1.	(c)	2.	(b)	3.	(c)	4.	(a)	5.	(c)
6.	(a)	7.	(b)	8.	(a)	9.	(d)	10.	(d)

THEORETICAL QUESTIONS

11. What is the significance of cash flow statement? Explain in brief.

Answer:

Cash flow statement provides information about the changes in cash and cash equivalents of an enterprise. It identifies cash generated from trading operations and is very useful tool of planning.

12. Explain the difference between direct and indirect methods of reporting cash flows from operating activities with reference to AS 3.

Answer:

As per Para 18 of AS 3 (Revised) on Cash Flow Statements, an enterprise should report cash flows from operating activities using either:

- (a)** The direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed; or
- (b)** the indirect method, whereby net profit or loss is adjusted for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash flows.

13. What are the main features of the Cash Flow Statement?

Answer:

According to AS 3 on "Cash Flow Statement", cash flow statement deals with the provision of information about the historical changes in cash and cash equivalents of an enterprise during the given period from operating, investing and financing activities. Cash flows from operating activities can be reported using either (a) the direct method, or (b) the indirect method. A cash flow statement when used in conjunction with the other financial statements, provides information that enables users to evaluate the changes in net assets of an enterprise, its financial structure (including its liquidity and solvency), and its ability to affect the amount and timing of cash flows in order to adapt to changing circumstances and opportunities.

14. Mayuri Ltd. acquired Plant and Machinery for Rs. 25 lakhs. During the same year, it also sold Furniture and Fixtures for Rs. 4 lakhs. Can the company disclose, Net Cash Outflow towards purchase of Fixed Assets Rs. 21 lakhs (i.e., 25 lakhs – 4 lakhs) in the Cash Flow Statement?

Answer:

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.

In the given case, since the purchase of Plant and Machinery and disposal of Furniture and Fixtures do not fall in the criteria of exception mentioned above, the same should be presented on a gross basis as an outflow of Rs. 25 lakhs and an inflow of Rs. 4 lakhs. Presentation of net cash outflow of Rs. 21 lakhs is not permitted as per AS 3.



SCENARIO BASED QUESTIONS

15. Classify the following activities as (a) Operating activities, (b) Investing activities (c) Financing activities (d) Cash equivalents with reference to AS 3 (Revised).

- (a) Brokerage paid on purchase of investments
- (b) Underwriting commission paid
- (c) Trading commission received
- (d) Proceeds from sale of investment
- (e) Purchase of goodwill
- (f) Redemption of preference shares
- (g) Rent received from property held as investment
- (h) Interest paid on long-term borrowings
- (i) Marketable securities (having risk of change in value)
- (j) Refund of income tax received

Answer:

Classification of activities with reference to AS 3

a.	Brokerage paid on purchased of investments	Investing Activities
b.	Underwriting Commission paid	Financing Activities
c.	Trading Commission received	Operating Activities
d.	Proceeds from sale of investment	Investing Activities
e.	Purchase of goodwill	Investing Activities
f.	Redemption of Preference shares	Financing Activities
g.	Rent received from property held as investment	Investing Activities
h.	Interest paid on long term borrowings	Financing Activities
i.	Marketable securities	Not a Cash equivalent
j.	Refund of Income tax received	Operating activities

16. How will you disclose following items while preparing Cash Flow Statement of Gagan Ltd. as per AS-3 for the year ended 31st March, 20X2?

- (i) 10% Debentures issued: As on 01-04-20X1 Rs. 1,10,000 As on 31-03-20X2 Rs. 77,000
- (ii) Debentures were redeemed at 5% premium at the end of the year. Premium was charged to the Profit & Loss Account for the year.
- (iii) Unpaid Interest on Debentures:
As on 01-04-20X1 Rs. 275
As on 31-03-20X2 Rs. 1,175
- (iv) Debtors of Rs. 36,000 were written off against the Provision for Doubtful Debts A/c during the year.
- (v) 10% Bonds (Investments): As on 01-04-20X1 Rs. 3,50,000 As on 31-03-20X2 Rs. 3,50,000

(vi) **Accrued Interest on Investments: As on 31-03-20X2 Rs. 10,500**

Answer:

Cash Flow Statement of M/s Gagan Ltd. for the year ended March 31, 20X2

A	Cash Flow from Operating Activities	
	Net Profit as per Profit & Loss A/c	xxxxx
	Add: Premium on Redemption of Debentures	1,650
	Add: Interest on 10% Debentures	11,000
	Less: Interest on 10% Investments	(35,000)
B	Cash Flow from Investing Activities	
	Interest on Investments [35,000-10,500]	24,500
C	Cash Flow from Financing Activities	
	Interest on Debentures paid [11,000 - (1,175 - 275)] - outflow	(10,100)
	Redemption of Debentures [(1,10,000 - 77,000) at 5% premium] - outflow	(34,650)

17. From the following Balance sheet of Grow More Ltd., prepare Cash Flow Statement for the year ended 31st March, 20X1 :

Particulars			Notes	31 st March, 20X1	31 st March, 20X0
1	Equity and Liabilities				
	Shareholders' funds				
A	Share capital			10,00,000	8,00,000
B	Reserves and Surplus	1		3,00,000	2,10,000
2	Non-current liabilities				
	Long term borrowings	2		2,00,000	-
3	Current liabilities				
A	Trade Payables			7,00,000	8,20,000
B	Other current liabilities	3		-	1,00,000
C	Short term provision (provision for tax)			1,00,000	70,000
	Total			23,00,000	20,00,000
	Assets				
1	Non-current assets				
A	Property, plant and Equipment	4		13,00,000	9,00,000
B	Non-Current Investments			1,00,000	-
2	Current assets				
A	Inventories			4,00,000	2,00,000

B	Trade receivables	5,00,000	7,00,000
C	Cash and Cash equivalents	-	2,00,000
	Total	23,00,000	20,00,000

Notes to accounts

No.	Particulars	31 st March, 20X1	31 st March, 20X0
1	Reserves and Surplus		
	General reserve	2,00,000	1,50,000
	Profit and Loss account	1,00,000	60,000
	Total	3,00,000	2,10,000
2	Long term borrowings		
	Debentures (issued at end of year)	2,00,000	==
3.	Other current liabilities		
	Dividend payable	-	1,00,000
4	Property, plant and equipment		
	Plant and machinery	7,00,000	5,00,000
	Land and building	6,00,000	4,00,000
	Net carrying value	13,00,000	9,00,000

- (i) Depreciation @ 25% was charged on the opening value of Plant and Machinery.
- (ii) At the year end, one old machine costing Rs. 50,000 (WDV Rs. 20,000) was sold for Rs. 35,000. Purchase was also made at the year end.
- (iii) Rs. 50,000 was paid towards Income tax during the year.
- (iv) Construction of the building got completed on 31.03.20X1 and hence no depreciation may be charged on the same.

Prepare Cash flow Statement.

Answer:

Cash Flow Statement of Grow More Ltd. for the year ended 31st March, 20X1 Cash Flow from Operating Activities

		Rs.
Increase in balance of Profit and Loss Account (1,00,000 – 60,000)	40,000	
Provision for taxation (W.N.1)	80,000	
Transfer to General Reserve (2,00,000 – 1,50,000)	50,000	
Depreciation (W.N.2)	1,25,000	
Profit on sale of Plant and Machinery	(15,000)	

Operating Profit before Working Capital changes	2,80,000	1,10,000
Increase in Inventories	(2,00,000)	
Decrease in Trade receivables	2,00,000	
Decrease in Trade payables	(1,20,000)	
Cash generated from operations	1,60,000	
Income tax paid	(50,000)	
Net Cash generated from operating activities		

Cash Flow from Investing Activities

Purchase of fixed assets	(3,45,000)	(6,10,000)
Expenses on building (6,00,000 – 4,00,000)	(2,00,000)	
Increase in investments	(1,00,000)	
Sale of old machine	35,000	
Net Cash used in investing activities		

Cash Flow from Financing activities

Proceeds from issue of shares (10,00,000 – 8,00,000)	2,00,000	3,00,000 (2,00,000) 2,00,000 <u>Nil</u>
Proceeds from issue of debentures	2,00,000	
Dividend paid	<u>(1,00,000)</u>	
Net cash generated from financing activities		
Net decrease in cash and cash equivalents		
Cash and Cash equivalents at the beginning of the year		
Cash and Cash equivalents at the end of the year		

Working Notes:

1. Provision for taxation account

	Rs.		Rs.
To Cash (Paid)	50,000	By Balance b/d	70,000
To Balance c/d	1,00,000	By Profit and Loss A/c	80,000
		(Balancing figure)	
	<u>1,50,000</u>		<u>1,50,000</u>

2. Plant and Machinery account

	Rs.		Rs.
To Balance b/d	5,00,000	By Depreciation	1,25,000
To Profit and Loss A/c	15,000		
(profit on sale of machine)			
To Cash (Balancing figure)	3,45,000	By Cash (sale of machine)	35,000

			By	Balance c/d	<u>7,00,000</u>
		<u>8,60,000</u>			<u>8,60,000</u>

18. From the following Balance Sheets and information, prepare Cash Flow Statement of Ryan Ltd. by Indirect method for the year ended 31st March, 20X1:

Particulars			Notes	31 st March 20X1Rs.	31 st March 20X0 Rs.
1		Equity and Liabilities			
		Shareholders' funds			
	A	Share capital	1	6,00,000	7,00,000
	B	Reserves and Surplus	2	4,20,000	3,00,000
2		Non-current liabilities			
		Long term borrowings	3	2,00,000	-
3		Current liabilities			
	A	Trade Payables		1,15,000	1,10,000
	B	Other current liabilities	4	30,000	80,000
	C	Short term provision (provision for tax)		95,000	60,000
		Total		14,60,000	12,50,000
		Assets			
1		Non-current assets			
	A	Property, plant and Equipment	5	9,15,000	7,00,000
	B	Non-Current Investments		50,000	80,000
2		Current assets			
	A	Inventories		95,000	90,000
	B	Trade receivables		2,50,000	2,25,000
	C	Cash and Cash equivalents		50,000	90,000
	D	Other Current assets		1,00,000	65,000
		Total		14,60,000	12,50,000

Notes to accounts

No.			31 st March, 20X1	31 st March, 20X0
1.	Share capital			
	Equity share capital		6,00,000	5,00,000
	10% Redeemable Preference share capital		--	<u>2,00,000</u>
	Total		<u>6,00,000</u>	<u>7,00,000</u>

2	Reserves and Surplus			
	Capital redemption reserve		1,00,000	-
	Capital reserve		70,000	-
	General reserve		1,50,000	2,50,000
	Profit and Loss account		<u>1,00,000</u>	<u>50,000</u>
	Total		<u>4,20,000</u>	<u>3,00,000</u>
3	Long term borrowings			
	9% Debentures		<u>2,00,000</u>	--
4.	Other current liabilities			
	Dividend payable		-	60,000
	Liabilities for expenses		<u>30,000</u>	<u>20,000</u>
	Total		<u>30,000</u>	<u>80,000</u>
5	Property, plant and equipment			
	Plant and machinery		7,65,000	5,00,000
	Land and building		<u>1,50,000</u>	<u>2,00,000</u>
	Net carrying value		<u>9,15,000</u>	<u>7,00,000</u>

Additional Information:

- A piece of land has been sold out for Rs.1,50,000 (Cost – Rs.1,20,000) and the balance land was revalued. Capital Reserve consisted of profit on revaluation of land.
- On 1st April, 20X0 a plant was sold for Rs.90,000 (Original Cost – Rs.70,000 and W.D.V. – Rs. 50,000) and Debentures worth Rs.1 lakh were issued at par as part consideration for plant of Rs.4.5 lakhs acquired.
- Part of the investments (Cost – Rs.50,000) was sold for Rs.70,000.
- Pre-acquisition dividend received Rs.5,000 was adjusted against cost of investment.
- Interim dividend was declared and paid @ 15% during the current year.
- Income-tax liability for the current year was estimated at Rs.1,35,000.
- Depreciation @ 15% has been charged on Plant and Machinery but no depreciation has been charged on Building.

Answer:

Cash Flow Statement of Ryan Limited For the year ended 31st March, 20X1

	Rs.	Rs.
Cash flow from operating activities		
Net Profit before taxation (W.N.1)	2,75,000	
Adjustment for		
Depreciation (W.N.3)	1,35,000	
Profit on sale of land	(30,000)	

Profit on sale of plant (W.N.3)	(40,000)	
Profit on sale of investments (W.N.4)	(20,000)	
Interest on debentures (2,00,000 X 9%)	18,000	
Operating profit before working capital changes	3,38,000	
Increase in inventory	(5,000)	
Increase in trade receivables	(25,000)	
Increase in Other current assets (W.N.9)	(35,000)	
Increase in Trade payables	5,000	
Increase in liabilities for expenses	10,000	
Cash generated from operations	2,88,000	
Income taxes paid (W.N.8)	(1,00,000)	
Net cash generated from operating activities		1,88,000
Cash flow from investing activities		
Proceeds from sale of land (W.N.2)	1,50,000	
Proceeds from sale of plant (W.N.3)	90,000	
Proceeds from sale of investments (W.N.4)	70,000	
Purchase of plant (W.N.3)	(3,50,000)	
Purchase of investments (W.N.4)	(25,000)	
Pre-acquisition dividend received (W.N.4)	5,000	
Net cash used in investing activities		(60,000)
Cash flow from financing activities		
Proceeds from issue of equity shares (6,00,000 – 5,00,000)	1,00,000	
Proceeds from issue of debentures (2,00,000 – 1,00,000)	1,00,000	
Redemption of preference shares	(2,00,000)	
Dividends paid	(1,50,000)	
Interest paid on debentures	(18,000)	
Net cash used in financing activities		(1,68,000)
Net decrease in cash and cash equivalents		(40,000)
Cash and cash equivalents at the beginning of the year		90,000
Cash and Cash equivalents at the end of the year		50,000

Significant Non-cash Items:

Debentures amounting to Rs. 1,00,000 have been issued as part consideration for acquisition of plant of Rs. 4,50,000.

Working Notes:**1.**

	Rs.
Net profit before taxation	
Retained profit	1,00,000
Less: Balance as on 31.3.20X0	(50,000)
	50,000
Provision for taxation	1,35,000
Dividend	90,000
	2,75,000

2.**Land and Building Account**

	Rs.		Rs.
To	Balance b/d	By	Cash (Sale)
	2,00,000		1,50,000
To	Profit and Loss A/c (Profit on sale)	By	Balance c/d
	30,000		1,50,000
To	Capital reserve (Revaluation profit)		
	70,000		
	3,00,000		3,00,000

3.**Plant and Machinery Account**

	Rs.		Rs.
To	Balance b/d	By	Cash (Sale)
	5,00,000		90,000
To	Profit and loss account	By	Depreciation
	40,000		1,35,000
To	Debentures	By	Balance c/d
	1,00,000		7,65,000
To	Bank		
	3,50,000		
	9,90,000		9,90,000

4.**Investments Account**

	Rs.		Rs.
To	Balance b/d	By	Cash (Sale)
	80,000		70,000
To	Profit and loss account	By	Dividend (Pre- acquisition)
	20,000		5,000
To	Bank (Balancing figure)	By	Balance c/d
	25,000		50,000
	1,25,000		1,25,000

5.**Capital Reserve Account**

	Rs.		Rs.
To	Balance c/d	By	Profit on revaluation of land
	70,000		70,000
	<u>70,000</u>		70,000

6. General Reserve Account

		Rs.			Rs.
To	Capital redemption reserve	1,00,000	By	Balance b/d	2,50,000
To	Balance c/d	1,50,000			
		2,50,000			2,50,000

7. Dividend payable Account

		Rs.			Rs.
To	Bank (Balancing figure)	1,50,000	By	Balance b/d	60,000
To	Balance c/d	-	By	Profit and loss account	90,000
		1,50,000			1,50,000

8. Provision for Taxation Account

		Rs.			Rs.
To	Bank (Balancing figure)	1,00,000	By	Balance b/d	60,000
To	Balance c/d	95,000	By	Profit and loss account	1,35,000
		1,95,000			1,95,000

9. Other Current Assets Account

		Rs.			Rs.
To	Balance b/d	65,000	By	Balance c/d	1,00,000
To	Bank (Balancing figure)	35,000			
		1,00,000			1,00,000

19. The Balance Sheet of New Light Ltd. as at 31st March, 20X1 and 20X0 (for the years ended) are as follows:

			Notes	Rs. 31 st March 20X0	Rs. 31 st March 20X1
		Equity and Liabilities			
1		Shareholders' funds			
	A	Share capital	1	16,00,000	18,80,000
	B	Reserves and Surplus	2	8,40,000	11,00,000
2		Non-current liabilities			
		Long term borrowings	3	4,00,000	2,80,000
3		Current liabilities			
	A	Other current liabilities	4	6,00,000	5,20,000

	B	Short term provision (provision for tax)		3,60,000	3,40,000
		Total		38,00,000	41,20,000
		Assets			
1		Non-current assets			
	A	Property, plant and Equipment	5	22,80,000	26,40,000
	B	Non-Current Investments		4,00,000	3,20,000
2		Current assets			
	A	Cash and Cash equivalents		10,000	10,000
	B	Other Current assets		11,10,000	11,50,000
		Total		38,00,000	41,20,000

Notes to accounts

No.	Particulars		31 st March, 20X0	31 st March, 20X1
1.	Share capital			
	Equity share capital		12,00,000	16,00,000
	10% Preference share capital		<u>4,00,000</u>	<u>2,80,000</u>
	Total		<u>16,00,000</u>	<u>18,80,000</u>
2	Reserves and Surplus			
	General reserve		6,00,000	7,60,000
	Profit and Loss account		<u>2,40,000</u>	<u>3,40,000</u>
	Total		<u>8,40,000</u>	<u>11,00,000</u>
3	Long term borrowings			
	9% Debentures		<u>4,00,000</u>	<u>2,80,000</u>
	Total		<u>4,00,000</u>	<u>2,80,000</u>
4.	Other current liabilities			
	Dividend payable		1,20,000	-
	Current Liabilities		<u>4,80,000</u>	<u>5,20,000</u>
	Total		<u>6,00,000</u>	<u>5,20,000</u>
5	Property, plant and equipment			
	Property, plant and equipment		32,00,000	38,00,000
	Less: Depreciation		<u>(9,20,000)</u>	<u>(11,60,000)</u>
	Net carrying value		<u>22,80,000</u>	<u>26,40,000</u>

Additional information:

- i) The company sold one property, plant and equipment for Rs. 1,00,000, the cost of which was Rs. 2,00,000 and the depreciation provided on it was Rs.80,000.

- ii) The company also decided to write off another item of property, plant and equipment costing Rs. 56,000 on which depreciation amounting to Rs. 40,000 has been provided.
- iii) Depreciation on property, plant and equipment provided Rs. 3,60,000.
- iv) Company sold some investment at a profit of Rs. 40,000.
- v) Debentures and preference share capital redeemed at 5% premium. Debentures were redeemed at the year end.
- vi) 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 31.3.20X0 was Rs. 2,16,000. The inventory on 31.3.20X1 was correctly valued at Rs. 3,00,000.

Prepare Cash Flow Statement as per revised Accounting Standard 3 by indirect method.

Answer:

New Light Ltd.

Cash Flow Statement for the year ended 31st March, 20X1

A.	Cash Flow from operating activities	Rs.	Rs.
	Profit after appropriation		
	Increase in profit and loss A/c after inventory adjustment [Rs.3,40,000 – (Rs.2,40,000 + Rs.24,000)]	76,000	
	Transfer to general reserve	1,60,000	
	Provision for tax	3,40,000	
	Net profit before taxation and extraordinary item	5,76,000	
	Adjustments for:		
	Depreciation	3,60,000	
	Loss on sale of property, plant and equipment	20,000	
	Decrease in value of property, plant and equipment	16,000	
	Profit on sale of investment	(40,000)	
	Premium on redemption of preference share capital	6,000	
	Interest on debentures	36,000	
	Premium on redemption of debentures	6,000	
	Operating profit before working capital changes	9,80,000	
	Increase in current liabilities (Rs.5,20,000 –Rs.4,80,000)	40,000	
	Increase in other current assets [Rs.11,50,000 – (Rs. 11,10,000 + Rs.24,000)]	(16,000)	
	Cash generated from operations	10,04,000	
	Income taxes paid	(3,60,000)	
	Net Cash generated from operating activities		44,000
B.	Cash Flow from investing activities		

	Purchase of property, plant and equipment (W.N.3)	(8,56,000)	
	Proceeds from sale of property, plant and equipment (W.N.3)	1,00,000	
	Proceeds from sale of investments (W.N.2)	1,20,000	
	Net Cash used in investing activities		(6,36,000)
C.	Cash Flow from financing activities		
	Proceeds from issuance of share capital	4,00,000	
	Redemption of preference share capital (Rs.1,20,000 + Rs.6,000)	(1,26,000)	
	Redemption of debentures (Rs. 1,20,000 +Rs. 6,000)	(1,26,000)	
	Dividend paid	(1,20,000)	
	Interest on debentures	(36,000)	
	Net Cash generated from financing activities		(8,000)
	Net increase/decrease in cash and cash equivalent during the year		Nil
	Cash and cash equivalent at the beginning of the year		10,000
	Cash and cash equivalent at the end of the year		10,000

Working Notes:

1. Revaluation of inventory will increase opening inventory by Rs. 24,000. $2,16,000/90 \times 10 = \text{Rs. } 24,000$

Therefore, opening balance of other current assets would be as follows:

$$\text{Rs. } 11,10,000 + \text{Rs. } 24,000 = \text{Rs. } 11,34,000$$

Due to under valuation of inventory, the opening balance of profit and loss account be increased by Rs. 24,000.

The opening balance of profit and loss account after revaluation of inventory will be Rs. 2,40,000 + Rs. 24,000 = Rs. 2,64,000

2. Investment Account

	Rs.		Rs.
To Balance b/d	4,00,000	By Bank A/c	1,20,000
To Profit and Loss A/c (Profit on sale of investment)	40,000	(balancing figure being investment sold)	
	4,40,000	By Balance c/d	3,20,000
			4,40,000

3. Property, Plant and Equipment Account

	Rs.		Rs.	Rs.
To Balance b/d	32,00,000	By Bank A/c (sale of assets)	1,00,000	
To Bank A/c (balancing figure being assets purchased)	8,56,000	By Accumulated depreciation A/c	80,000	
		By Profit and loss A/c (loss on sale of assets)	20,000	2,00,000
		By Accumulated depreciation A/c	40,000	
		By Profit and loss A/c (assets written off)	<u>16,000</u>	56,000
		By Balance c/d		<u>38,00,000</u>
	<u>40,56,000</u>			<u>40,56,000</u>

4. Accumulated Depreciation Account

	Rs.		Rs.
To Property, plant and equipment A/c	80,000	By Balance b/d	9,20,000
To Property, plant and equipment A/c	40,000	By Profit and loss A/c (depreciation for the year)	3,60,000
To Balance c/d	11,60,000		
	<u>12,80,000</u>		<u>12,80,000</u>

20. ABC Ltd. gives you the Balance sheets as at 31st March 20X0 and 31st March 20X1. You are required to prepare Cash Flow Statement by using indirect method as per AS 3 for the year ended 31st March 20X1:

Particulars	Notes	Rs. 31 st March 20X0	Rs. 31 st March 20X1
1 Equity and Liabilities			
Shareholders' funds			
A Share capital		50,00,000	50,00,000
B Reserves and Surplus		26,50,000	36,90,000
Non-current liabilities			
2 Long term borrowings	1	-	9,00,000

3		Current liabilities			
	A	Short-term borrowings		1,50,000	3,00,000
		(Bank loan)			
	B	Trade payables		8,80,000	8,20,000
	C	Other current liabilities	2	4,80,000	2,70,000
		Total		91,60,000	1,09,80,000
		Assets			
1		Non-current assets			
	A	Property, plant and Equipment	3	21,20,000	32,80,000
2		Current assets			
	A	Current Investments		11,80,000	15,00,000
	B	Inventory		20,10,000	19,20,000
	C	Trade receivables	4	22,40,000	26,40,000
	D	Cash and Cash equivalents		15,20,000	15,20,000
	E	Other Current assets (Prepaid expenses)		90,000	1,20,000
		Total		91,60,000	1,09,80,000

Notes to accounts

No.	Particulars		Rs.20X0	20X1
1	Long term borrowings			
	9% Debentures (issued at the end of year)		-	<u>9,00,000</u>
	Total		-	<u>9,00,000</u>
2.	Other current liabilities			
	Dividend payable		1,50,000	-
	Liabilities for expenses		<u>3,30,000</u>	<u>2,70,000</u>
	Total		<u>4,80,000</u>	<u>2,70,000</u>
3	Property, plant and equipment			
	Plant and machinery Less:		27,30,000	40,70,000
	Depreciation		<u>(6,10,000)</u>	<u>(7,90,000)</u>
	Net carrying value		<u>21,20,000</u>	<u>32,80,000</u>
4	Trade receivables			
	Gross amount		23,90,000	28,30,000
	Less: Provision for doubtful debts		<u>(1,50,000)</u>	<u>(1,90,000)</u>
	Total		<u>22,40,000</u>	<u>26,40,000</u>

Additional Information:

- (i) Net profit for the year ended 31st March, 20X1, after charging depreciation Rs. 1,80,000 is Rs. 10,40,000.

- (ii) Trade receivables of Rs. 2,30,000 were determined to be worthless and were written off against the provisions for doubtful debts account during the year.

Answer:

Cash Flow Statement of ABC Ltd. for the year ended 31.3.20X1

Cash flows from Operating Activities	Rs.	Rs.
Net Profit	10,40,000	
Add: Adjustment For Depreciation (Rs.7,90,000 – Rs.6,10,000)	1,80,000	
Add: Adjustment for Provision for Doubtful Debts (Rs. 4,20,000 – Rs.1,50,000)	2,70,000	
Operating Profit Before Working Capital Changes	14,90,000	
Add: Decrease in Inventories (Rs. 20,10,000 – Rs. 19,20,000)	90,000	
	15,80,000	
Less: Increase in Current Assets		
Trade Receivables (Rs. 30,60,000 – Rs.23,90,000)	6,70,000	
Prepaid Expenses (Rs. 1,20,000 – Rs.90,000)	30,000	
Decrease in Current Liabilities:		
Trade Payables (Rs. 8,80,000 – Rs. 8,20,000)	60,000	
Expenses Outstanding (Rs. 3,30,000 – Rs. 2,70,000)	<u>60,000</u>	(8,20,000)
Net Cash generated from Operating Activities		7,60,000
Cash Flows from Investing Activities		
Investment in Current Investments	(3,20,000)	
Purchase of Plant & Machinery (Rs. 40,70,000 – Rs. 27,30,000)	(13,40,000)	
Net Cash Used in Investing Activities		(16,60,000)
Cash Flows from Financing Activities		
Bank Loan Raised (Rs. 3,00,000 – Rs. 1,50,000)	1,50,000	
Issue of Debentures	9,00,000	
Payment of Dividend	<u>(1,50,000)</u>	
Net Cash Used in Financing Activities		9,00,000
Net Increase in Cash During the Year		-
Add: Cash and Cash Equivalents as on 1.4.20X0		15,20,000
Cash and Cash Equivalents as on 31.3.20X1		15,20,000

Note:

1. Bad debts amounting Rs.2,30,000 were written off against provision for doubtful debts account during the year. In the above Solution:, Bad debts have been added back in the balances of provision for doubtful debts and trade receivables as on 31.3.20X1. Alternatively, the adjustment of writing off bad debts may be ignored and the Solution: can be given on the basis of figures of trade receivables and provision for doubtful debts as appearing in the balance sheet on 31.3.20X1.
2. Current investments (i.e. Marketable securities) may not be readily convertible to a known amount of cash and be subject to an insignificant risk of changes in value as per the requirements of AS 3 and hence those have been considered as investing activities.

21. Following is the Balance Sheet of Fox Ltd. You are required to prepare cash flow statement using Indirect Method.

Particulars	Note No.	31st March,20X2 (Rs.)	31st March,20X1 (Rs.)
(I) Equity and Liabilities			
1. Shareholders' Funds			
(a) Share capital	1	5,60,000	3,00,000
(b) Reserve and Surplus	2	35,000	25,000
2. Current Liabilities			
(a) Trade payables		1,50,000	60,000
(b) Short-term provisions (Provision for taxation)		8,000	5,000
Total		7,53,000	3,90,000
(II) Assets			
1. Non-current assets			
(a) Property, Plant and Equipment		3,50,000	1,80,000
2. Current assets			
(a) Inventories		1,20,000	50,000
(b) Trade receivables		1,00,000	25,000
(c) Cash and cash equivalents		1,05,000	90,000
(d) Other current assets		78,000	45,000
Total		7,53,000	3,90,000

Notes to Accounts

Particulars	31st March,20X2 (Rs.)	31st March,20X1 (Rs.)
1. Share capital		
(a) Equity share capital	4,10,000	2,00,000
(b) Preference share capital	<u>1,50,000</u>	<u>1,00,000</u>
	<u>5,60,000</u>	<u>3,00,000</u>
2. Reserve and surplus		
Surplus in statement of profit and loss at the beginning of the year	25,000	
Add: Profit of the year	20,000	
Less: Dividend	<u>(10,000)</u>	
Surplus in statement of profit and loss at the end of the year	35,000	25,000

Additional Information:

- Dividend paid during the year Rs. 10,000
- Depreciation charges during the year Rs. 40,000.

Answer:

Fox Ltd.

Cash Flow Statement for the year ended 31st March, 20X2

	Rs.	Rs.
<u>Cash flows from operating activities</u>		
Net Profit (35,000 less 25,000)	10,000	
Add: Dividend	10,000	
Provision for tax	<u>8,000</u>	
Net profit before taxation and extraordinary items	28,000	
Adjustments for:		
Depreciation	40,000	
Operating profit before working capital changes		68,000
Increase in trade receivables	(75,000)	
Increase in inventories	(70,000)	
Increase in other current assets	(33,000)	
Increase in trade payables	90,000	(88,000)
Cash used in operating activities		(20,000)
Less: Tax paid*		(5,000)
Net cash used in operating activities		(25,000)

<u>Cash flows from investing activities</u>		
Purchase of PPE	(2,10,000)	
Net cash used in investing activities		(2,10,000)
<u>Cash flows from financing activities</u>		
Issue of equity shares for cash	2,10,000	
Issue of preference shares	50,000	
Dividends paid	(10,000)	
Net cash generated from financing activities		2,50,000
Net increase in cash and cash equivalents		15,000
Cash and cash equivalents at beginning of period		90,000
Cash and cash equivalents at end of period		1,05,000

*Provision for tax of last year considered to be paid in the current year.

Working Note:

	Rs.
Property, plant and equipment acquisitions	
W.D.V. at 31.3.20X2	3,50,000
Add back:	
Depreciation for the year	40,000
	3,90,000
Less: W.D.V. at 31.12.20X1	1,80,000
Acquisitions during 20X1-20X2	2,10,000

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

- ◆ Corporate Income Tax paid amounting to Rs. 70 lakhs during the reporting period.
- ◆ Payment of advance tax Rs. 8,75,000 out of which Rs. 75,000 was towards capital gains arising on account of sale of assets during the reporting period.
- ◆ Fixed Deposits withdrawn by customers of State Bank of India Rs. 3 crores.

Answer:

As per AS 3, the given cash flows shall be recorded as under:

Corporate Income Tax paid amounting to Rs. 70 lakhs during the reporting period.	Rs. 70 lakhs: Operating Cash Flows
Payment of advance tax Rs. 8,75,000 out of which Rs. 75,000 was towards capital gains arising on account of sale of assets during the reporting period.	Rs. 8,00,000: Operating Cash Flows Rs. 75,000: Investing Cash Flows
Fixed Deposits withdrawn by customers of State Bank of India Rs. 3 crores.	Rs. 3 crores: Operating Cash Flows for State Bank of India.

23. Money Ltd., a non-financial company has the following entries in its Bank Account. It has sought your advice on the treatment of the same for preparing Cash Flow Statement.

(i) Loans and Advances given to the following and interest earned on them:

- (1) to suppliers**
- (2) to employees**
- (3) to its subsidiaries companies**

(ii) Investment made in subsidiary Smart Ltd. and dividend received

(iii) Dividend paid for the year

Discuss in the context of AS 3 Cash Flow Statement.

Answer:

Treatment as per AS 3 'Cash Flow Statement'

(i) Loans and advances given and interest earned

- (1) to suppliers - Cash flows from operating activities**
- (2) to employees - Cash flows from operating activities**
- (3) to its subsidiary companies - Cash flows from investing activities**

(ii) Investment made in subsidiary company and dividend received

Cash flows from investing activities

(iii) Dividend paid for the year

Cash flows from financing activities



24. From the following information of XYZ Limited, calculate cash and cash equivalent as on 31-03-20X2 as per AS 3.

Particulars	Amount (Rs.)
Balance as per the Bank Statement	25,000
Cheque issued but not presented in the Bank	15,000
Short Term Investment in liquid equity shares of ABC Limited	50,000
Fixed Deposit created on 01-11-20X1 and maturing on 15-04-20X2	75,000
Short Term Investment in highly liquid Sovereign Debt Mutual fund on 01-03-20X2 (having maturity period of less than 3 months)	1,00,000
Bank Balance in a Foreign Currency Account in India (Conversion Rate: On the day of deposit Rs. 69/USD as on 31-03-20X2 Rs. 70/USD)	\$ 1,000

Answer:

Computation of Cash and Cash Equivalents as on 31st March, 20X2

	Rs.
Cash balance with bank (Rs.25,000 less Rs.15,000)	10,000

Short term investment in highly liquid sovereign debt mutual fund on 1.3.20X2	1,00,000
Bank balance in foreign currency account (\$1,000 x Rs.70)	70,000
	1,80,000

Note: Short term investment in liquid equity shares and fixed deposit will not be considered as cash and cash equivalents.

25. Z Ltd. has no Foreign Currency Cash Flow during the reporting period. It held a deposit in a bank in France. The balances as at the beginning of the year and at the end of the year were € 100,000 and € 105,000 respectively. The exchange rate at the beginning of the year was € 1 = Rs. 82, and at the end of the year was € 1 = Rs. 85. The increase in the deposit balance of € 5,000 was on account of interest credited on the last day of the reporting period. The deposit was reported at Rs. 82,00,000 in the opening balance sheet and at Rs. 89,25,000 in the closing balance sheet. You are required to show how these transactions would be presented in the Cash Flow Statement as per AS 3.

Answer:

The Statement of Profit and Loss was credited on account of:

Interest Income: € 5,000 x Rs. 85 = Rs. 4,25,000

Exchange difference = € 100,000 x (Rs. 85 – Rs. 82) = Rs. 3,00,000

In preparing the Cash Flow Statement, the exchange difference of Rs. 3,00,000 should be deducted from the Net Profit before taxes, since it is a non-cash item. However, in order to reconcile the opening balance of the Cash and Cash Equivalents with its closing balance, the Exchange Difference of Rs. 3,00,000 should be added to the opening balance in a Note to the Cash Flow Statement., Cash Flows arising from transactions in a Foreign Currency shall be recorded in Z Ltd.'s reporting currency by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the cash flow.

26. Following is the Balance Sheet of Fox Ltd. You are required to prepare cash flow statement using Indirect Method.

Particulars	Note No.	31 st March,20X2 (Rs.)	31 st March,20X1 (Rs.)
(I) Equity and Liabilities			
1. Shareholders' Funds			
(a) Share capital	1	5,60,000	3,00,000
(b) Reserve and Surplus	2	35,000	25,000
2. Current Liabilities			
(a) Trade payables		1,50,000	60,000
(b) Short-term provisions		8,000	5,000

(Provision for taxation)			
Total		7,53,000	3,90,000
(II) Assets			
1. Non-current assets			
(a) Property, Plant and Equipment		3,50,000	1,80,000
2. Current assets			
(a) Inventories		1,20,000	50,000
(b) Trade receivables		1,00,000	25,000
(c) Cash and cash equivalents		1,05,000	90,000
(d) Other current assets		78,000	45,000
Total		7,53,000	3,90,000

Notes to Accounts

Particulars	31st March, 20X2 (Rs.)	31st March, 20X1 (Rs.)
1. Share capital		
(a) Equity share capital	4,10,000	2,00,000
(b) Preference share capital	1,50,000	1,00,000
	5,60,000	3,00,000
2. Reserve and surplus		
Surplus in statement of profit and loss at the beginning of the year	25,000	
Add: Profit of the year	20,000	
Less: Dividend	(10,000)	
Surplus in statement of profit and loss at the end of the year	35,000	25,000

Additional Information:

- Dividend paid during the year Rs. 10,000
- Depreciation charges during the year Rs. 40,000.

Answer:

Fox Ltd.

Cash Flow Statement for the year ended 31st March, 20X2

	Rs.	Rs.
Cash flows from operating activities		
Net Profit (35,000 less 25,000)	10,000	
Add: Dividend	10,000	
Provision for tax	8,000	
Net profit before taxation and extraordinary items	28,000	

Adjustments for:		
Depreciation	40,000	
Operating profit before working capital changes		68,000
Increase in trade receivables	(75,000)	
Increase in inventories	(70,000)	
Increase in other current assets	(33,000)	
Increase in trade payables	90,000	(88,000)
Cash used in operating activities		(20,000)
Less: Tax paid*		(5,000)
Net cash used in operating activities		(25,000)
Cash flows from investing activities		
Purchase of PPE	(2,10,000)	
Net cash used in investing activities		(2,10,000)
Cash flows from financing activities		
Issue of equity shares for cash	2,10,000	
Issue of preference shares	50,000	
Dividends paid	(10,000)	
Net cash generated from financing activities		2,50,000
Net increase in cash and cash equivalents		15,000
Cash and cash equivalents at beginning of period		90,000
Cash and cash equivalents at end of period		1,05,000

*Provision for tax of last year considered to be paid in the current year.

Working Note:

	Rs.
Property, plant and equipment acquisitions	
W.D.V. at 31.3.20X2	3,50,000
Add back:	
Depreciation for the year	40,000
	3,90,000
Less: W.D.V. at 31.12.20X1	1,80,000
Acquisitions during 20X1-20X2	2,10,000

QUESTIONS FROM RTP'S, MTP'S, QP'S

Question 1

The Balance Sheet of Harry Ltd. for the year ending 31st March, 2018 and 31st March, 2017 were summarised as follows:

	2018 (₹)	2017 (₹)
Equity share capital	1,20,000	1,00,000
Reserves:		
Profit and Loss Account	9,000	8,000
Current Liabilities:		
Trade Payables	8,000	5,000
Income tax payable	3,000	2,000
Declared Dividends	4,000	2,000
	1,44,000	1,17,000
Property, Plant & Equipment (at W.D.V) :		
Building	19,000	20,000
Furniture & Fixture	34,000	22,000
Cars	25,000	16,000
Long Term Investments	32,000	28,000
Current Assets:		
Inventory	14,000	8,000
Trade Receivables	8,000	6,000
Cash & Bank	12,000	17,000
	1,44,000	1,17,000

The Profit and Loss account for the year ended 31st March, 2018 disclosed:

	₹
Profit before tax	8,000
Income Tax	(3,000)
Profit after tax	5,000
Declared Dividends	(4,000)
Retained Profit	1,000

Further Information is available:

1. Depreciation on Building ₹ 1,000.
2. Depreciation on Furniture & Fixtures for the year ₹ 2,000.
3. Depreciation on Cars for the year ₹ 5,000. One car was disposed during the year for ₹ 3,400 whose written down value was ₹ 2,000.
4. Purchase investments for ₹ 6,000.

5. Sold investments for ₹ 10,000, these investments cost ₹ 2,000.

6. You are required to prepare Cash Flow Statement as per AS-3 (revised) using indirect method.

(MTP March '23, RTP Nov'22)

Answer :

Harry Ltd.

Cash Flow Statement for the year ended 31st March, 2018

	₹	₹
Cash flows from operating activities		
Net Profit before taxation	8,000	
Adjustments for:		
Depreciation (1,000 + 2,000 +5,000)	8,000	
Profit on sale of Investment	(8,000)	
Profit on sale of car	(1,400)	
Operating profit before working capital changes	6,600	
Increase in Trade receivables	(2,000)	
Increase in inventories	(6,000)	
Increase in Trade payables	3,000	
Cash generated from operations	1,600	
Income taxes paid	(2,000)	
Net cash generated from operating activities (A)		(400)
Cash flows from investing activities		
Sale of car	3,400	
Purchase of car	(16,000)	
Sale of Investment	10,000	
Purchase of Investment	(6,000)	
Purchase of Furniture & fixtures	(14,000)	
Net cash used in investing activities (B)		(22,600)
Cash flows from financing activities		
Issue of shares for cash	20,000	
Dividends paid*	(2,000)	
Net cash from financing activities(C)		18,000
Net decrease in cash and cash equivalents (A + B +C)		(5,000)
Cash and cash equivalents at beginning of period		17,000
Cash and cash equivalents at end of period		12,000

* Dividend declared for the year ended 31st March, 2017 amounting ₹ 2,000 must have been paid in the year 2017-18. Hence, it has been considered as cash outflow for preparation of cash flow statement of 2017-18.

Working Notes:**1. Calculation of Income taxes paid**

	₹
Income tax expense for the year	3,000
Add: Income tax liability at the beginning of the year	2,000
	5,000
Less: Income tax liability at the end of the year	(3,000)
	2,000

2. Calculation of Fixed assets acquisitions

	Furniture & Fixtures (₹)	Car (₹)
W.D.V. at 31.3.2018	34,000	25,000
Add back: Depreciation for the year	2,000	5,000
Disposals	—	2,000
	36,000	32,000
Less: W.D.V. at 31. 3. 2017	(22,000)	(16,000)
Acquisitions during 2016–2018	14,000	16,000

Question 2

The following figures have been extracted from the books of Manan Limited for the year ended on 31.3.2022. You are required to prepare the Cash Flow statement as per AS 3 using indirect method.

- i) Net profit before taking into account income tax and income from law suits but after taking into account the following items was ₹ 30 lakhs:
 - (a) Depreciation on Property, Plant & Equipment ₹ 7,50 lakhs;
 - (b) Discount on issue of Debentures written off ₹ 45,000;
 - (c) Interest on Debentures paid ₹ 5,25,000;
 - (d) Book value of investments ₹ 4,50 lakhs (Sale of Investments for ₹ 4,80,000);
 - (e) Interest received on investments ₹ 90,000;
 - ii) Compensation received ₹ 1,35,000 by the company in a suit filed;
 - iii) Income tax paid during the year ₹ 15,75,000;
 - iv) 22,500, 10% preference shares of ₹ 100 each were redeemed on 02-04-2021 at a premium of 5%.
 - v) Further the company issued 75,000 equity shares of ₹ 10 each at a premium of 20% on 30.3.2022
(Out of 75,000 equity shares, 25,000 equity shares were issued to a supplier of machinery)
 - vi) Dividend for FY 2020-21 on preference shares were paid at the time of redemption.
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vii) Dividend on Equity shares paid on 31.01.2022 for the year 2020-2021 ₹ 7;50 lakhs and interim dividend paid ₹ 2;50 lakhs for the year 2021-2022.

viii) Land was purchased on 02;4;2021 for ₹ 3,00,000 for which the company issued 22,000 equity shares of ₹ 10 each at a premium of 20% to the land owner and balance in cash as consideration;

ix) Current assets and current liabilities in the beginning and at the end of the years were as detailed below:

	As on 01.04.2021	As on 31.3.2022
	₹	₹
Inventory	18,00,000	19,77,000
Trade receivables	3,87,000	3,79,650
Cash in hand	3,94,450	16,950
Trade payables	3,16,500	3,16,950
Outstanding expenses	1,12,500	1,22,700

(MTP April 23 & Sep '23)

Answer :

Manan Ltd.

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

	Rs.	Rs.
Cash flow from Operating Activities		
Net profit before income tax and extraordinary items:		30,00,000
Adjustments for:		
Depreciation on Property, plant and equipment	7,50,000	
Discount on issue of debentures	45,000	
Interest on debentures paid	5,25,000	
Interest on investments received	(90,000)	
Profit on sale of investments		12,00,000
Operating profit before working capital changes		42,00,000
Adjustments for:		
Increase in inventory	(1,77,000)	
Decrease in trade receivable	7,350	
Increase in trade payables	450	
Increase in outstanding expenses	10,200	(1,59,000)
Cash generated from operations		40,41,000
Income tax paid		(15,75,000)
Cash flow from ordinary items		24,66,000

Cash flow from extraordinary items:		
Compensation received in a suit filed		1,35,000
Net cash flow from operating activities		26,01,000
Cash flow from Investing Activities;		
Sale proceeds of investments	4,80,000	
Interest received on investments	90,000	
Purchase of land (3,00,000 less 2,64,000)	36,000	
Net cash flow from investing activities		5,34,000
Cash flow from Financing Activities		
Proceeds of issue of equity shares at 20% premium	6,00,000	
Redemption of preference shares at 5% premium	(23,62,500)	
Preference dividend paid	(2,25,000)	
Interest on debentures paid	(5,25,000)	
Dividend paid (7,50,000 + 2,50,000)	(10,00,000)	
Net cash used in financing activities		(35,12,500)
Net decrease in cash and cash equivalents during the year		(3,77,500)
Add: Cash and cash equivalents as on 31.3.2021		3,94,450
Cash and cash equivalents as on 31.3.2022		16,950



Question 3

From the following details relating to the accounts of Omega Ltd. prepare Cash Flow Statement for the year ended 31st March, 2021:

	31;03;2021(₹)	31;03;2020 (₹)
Share Capital	14,00,000	11,20,000
General Reserve	5,60,000	3,50,000
Profit and Loss Account	1,40,000	84,000
Debentures	2,80,000	-
Provision for taxation	1,40,000	98,000
Trade payables	9,80,000	11,48,000
Plant and Machinery	9,80,000	7,00,000
Land and Building	8,40,000	5,60,000
Investments	1,40,000	-
Trade receivables	7,00,000	9,80,000
Inventories	5,60,000	2,80,000
Cash in hand and at Bank	2,80,000	2,80,000

(i) Depreciation @ 20% was charged on the opening value of Plant and Machinery.

(ii) At the year end, one old machine costing 70,000 (WDV 28,000) was sold for ₹ 49,000; Purchase of machinery was also made at the year end.

(iii) ₹ 70,000 was paid towards Income tax during the year.

(iv) Land & Building is not subject to any depreciation; Expenses on renovation of building amount ₹ 2,80,000 were incurred during the year. Prepare Cash Flow Statement. (RTP May '22)

Answer :

Omega Ltd.

Cash Flow Statement for the year ended 31st March, 2021

Cash Flow from Operating Activities		
Increase in balance of Profit and Loss Account	56,000	
Provision for taxation	1,12,000	
Transfer to General Reserve	2,10,000	
Depreciation	1,40,000	
Profit on sale of Plant and Machinery	(21,000)	
Operating Profit before Working Capital changes	4,97,000	
Increase in Inventories	(2,80,000)	
Decrease in Trade receivables	2,80,000	
Decrease in Trade payables	(1,68,000)	
Cash generated from operations	3,29,000	
Income tax paid	(70,000)	
Net Cash from operating activities		2,59,000
Cash Flow from Investing Activities		
Purchase of plant & machinery	(4,48,000)	
Expenses on building	(2,80,000)	
Increase in investments	(1,40,000)	
Sale of old machine	49,000	
Net Cash used in investing activities		(8,19,000)
Cash Flow from Financing activities		
Proceeds from issue of shares	2,80,000	
Proceeds from issue of debentures	2,80,000	
Net cash from financing activities		5,60,000
Net increase in cash or cash equivalents		NIL
Cash and Cash equivalents at the beginning of the year		2,80,000
Cash and Cash equivalents at the end of the year		2,80,000

Working Notes: Provision for taxation account

	₹		₹
To Cash (Tax Paid)	70,000	By Balance b/d	98,000
To Balance c/d	1,40,000	By Profit and Loss A/c	1,12,000
		(Balancing figure)	
	2,10,000		2,10,000

Plant and Machinery account

	₹		₹
To Balance b/d	7,00,000	By Depreciation	1,40,000
To Profit and Loss A/c (profit on sale of machine)	21,000	By Cash (sale of machine)	49,000
		By Balance c/d	9,80,000
To Cash (Balancing figure)	4,48,000		
	11,69,000		11,69,000

Question 4

Following is the Balance Sheet of Fox Ltd. You are required to prepare cash flow statement using Indirect Method.

Particulars	Note No.	31st March,2021 (Rs.)	31st March,2020 (Rs.)
(I) Equity and Liabilities			
1. Shareholders' Funds			
(a) Share capital	1	5,60,000	3,00,000
(b) Reserve and Surplus	2	35,000	25,000
2. Current Liabilities			
(a) Trade payables		1,50,000	60,000
(b) Short-term provisions (Provision for taxation)		8,000	5,000
Total		7,53,000	3,90,000
(II) Assets			
1. Non-current assets			
(a) Property, Plant and Equipment		3,50,000	1,80,000
2. Current assets			
(a) Inventories		1,20,000	50,000
(b) Trade receivables		1,00,000	25,000
(c) Cash and cash equivalents		1,05,000	90,000

(d) Other current assets		78,000	45,000
Total		7,53,000	3,90,000

Notes to Accounts

Particulars	31st March,2021 (₹)	31st March,2020 (₹)
1. Share capital		
(a) Equity share capital	4,10,000	2,00,000
(b) Preference share capital	1,50,000	1,00,000
	5,60,000	3,00,000
2. Reserve and surplus		
Surplus in statement of profit and loss at the beginning of the year	25,000	
Add: Profit of the year	20,000	
Less: Dividend	(10,000)	
Surplus in statement of profit and loss at the end of the year	35,000	25,000

Additional Information:

1. Dividend paid during the year ₹ 10,000

2. Depreciation charges during the year ₹ 40,000;

(RTP May 23)

Answer :

Fox Ltd.

Cash Flow Statement for the year ended 31st March 2021

	₹	₹
Cash flows from operating activities		
Net Profit (35,000 less 25,000)	10,000	
Add: Dividend	10,000	
Provision for tax	8,000	
Net profit before taxation and extraordinary items	28,000	
Adjustments for:		
Depreciation	40,000	
Operating profit before working capital changes		68,000
Increase in trade receivables	(75,000)	
Increase in inventories	(70,000)	
Increase in other current assets	(33,000)	
Increase in trade payables	90,000	(88,000)
Cash used in operating activities		(20,000)

Less: Tax paid*		(5,000)
Net cash used in operating activities	(2,10,000)	(25,000)
Cash flows from investing activities		
Purchase of PPE		
Net cash used in investing activities		(2,10,000)
Cash flows from financing activities		
Issue of equity shares for cash	2,10,000	
Issue of preference shares	50,000	
Dividends paid	(10,000)	
Net cash generated from financing activities		2,50,000
Net increase in cash and cash equivalents		15,000
Cash and cash equivalents at beginning of period		90,000
Cash and cash equivalents at end of period		1,05,000

*Provision for tax of last year considered to be paid in the current year.

Working Note:

	₹
Property, plant and equipment acquisitions	
W.D.V. at 31.3.2021	3,50,000
Add back:	
Depreciation for the year	40,000
	3,90,000
Less: W.D.V. at 31.12.2020	1,80,000
Acquisitions during 2020–2021	2,10,000

3. BUY-BACK OF SECURITIES

ILLUSTRATIONS

Illustration 1

M Ltd. furnishes the following Balance Sheet as at 31st March, 20X1:

Particulars			Notes	Rs.(in 000)
1		Equity and Liabilities		
		Shareholders' funds		
	A	Share capital	1	5,000
	B	Reserves and Surplus	2	6,310
2		Non-current liabilities		
		Long term borrowings	3	400
3		Current liabilities		
	A	Trade Payables		40
		Total		11,750
1		Assets		
		Non-current assets		
	A	Property, plant and Equipment	4	2,750
	B	Non-Current Investments (at cost)		5,000
2		Current assets		
	A	Inventories		1,000
	B	Trade receivables		2,000
	C	Cash and Cash equivalents		1,000
		Total		11,750

Notes to accounts

No.	Particulars		Rs.in ('000)
1	Share Capital		
	Authorized, Issued and Subscribed Capital:		
	3,00,000 Equity shares of Rs.10 each fully paid up		3,000
	20,000 9% Preference Shares of 100 each		2,000
	Total		5,000
2	Reserves and Surplus		
	Capital reserve		10
	Revenue reserve		4,000
	Securities premium		500
	Profit and Loss account		1,800

	Total		<u>6,310</u>
3	Long term borrowings		
	10% Debentures		<u>400</u>
4	Property, Plant and Equipment (PPE)		
	PPE: Cost		<u>3,000</u>
	Less: Provision for depreciation		<u>(250)</u>
	Net carrying value		<u>2,750</u>

The company passed a reSolution: to buy-back 20% of its equity capital @ Rs.15 per share. For this purpose, it sold its investments of Rs.30 lakhs for Rs.25 lakhs.

You are required to pass necessary Journal entries.

Solution:

Journal Entries in the books of M Ltd.

Rs.in '000

	Particulars		Dr.	Cr.
1.	Bank A/c	Dr.	2,500	3,000
	Profit and Loss A/c	Dr.	500	
	To Investment A/c			
	(Being investment sold for the purpose of buy- back of Equity Shares)			
2.	Equity share capital A/c	Dr.	600	
	Premium payable on buy-back	Dr.	300	
	To Equity shares buy-back A/c			900
	(Being the amount due on buy-back of equity shares)			
3.	Equity shares buy-back A/c	Dr.	900	
	To Bank A/c			900
	(Being payment made for buy-back of equity shares)			
4.	Securities Premium A/c	Dr.	300	
	To Premium payable on buy-back			300
	(Being premium payable on buy-back charged from Securities premium)			
5.	Revenue reserve A/c	Dr.	600	
	To Capital Redemption Reserve A/c			600
	(Being creation of capital redemption reserve to the extent of the equity shares bought back)			

Illustration 2

Anu Ltd. (a non-listed company) furnishes you with the following balance sheet as at 31st March, 20X1: (in crores Rs.)

Particulars			Notes	Rs.
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	100
	B	Reserves and Surplus	2	300
2		Current liabilities		
	A	Trade Payables		40
		Total		440
		Assets		
1		Non-current assets		
	A	Property, plant and equipment	3	-
	B	Non-Current Investments	4	100
2		Current assets		
	A	Trade receivables		140
	B	Cash and Cash equivalents		200
		Total		440

Notes to accounts

No.	Particulars	Rs.
1	Share Capital	
	Authorized, issued and subscribed share capital:	
	12% Redeemable preference shares of Rs.100 each, fully paid up	75
	Equity shares of Rs.10 each, fully paid up	<u>25</u>
	Total	<u>100</u>
2	Reserves and Surplus	
	Capital reserve	15
	Securities premium	25
	Revenue reserves	<u>260</u>
	Total	<u>300</u>
3	Property, Plant and Equipment	
	PPE Cost	100
	Less: Provision for depreciation	<u>(100)</u>
	Net carrying value	<u>NIL</u>
4	Non-Current Investments	
	Non-current investments at cost (Market value Rs.400 Cr.)	<u>100</u>

The company redeemed preference shares on 1st April, 20X1. It also bought back 50 lakhs equity shares of Rs.10 each at Rs.50 per share. The payments for the above were made out of the huge bank balances, which appeared as a part of current assets.

You are asked to:

(i) Pass journal entries to record the above.

(ii) Prepare balance sheet as at 1.4.20X1.

Solution:

(i) Journal entries in the books of Anu Ltd.

		Rs.in crores		
	Particulars		Dr.	Cr.
1 st	12% Preference share capital A/c	Dr.	75	
April, 20X1	To Preference shareholders A/c (Being preference share capital account transferred to shareholders account)			75
	Preference shareholders A/c	Dr.	75	
	To Bank A/c (Being payment made to shareholders)			75
	Shares buy-back A/c	Dr.	25	
	To Bank A/c (Being 50 lakhs equity shares bought back @ Rs.50 per share)			25
	Equity share capital A/c (50 lakhs x Rs.10)	Dr.	5	
	Securities premium A/c (50 lakhs x Rs.40)	Dr.	20	
	To Shares buy-back A/c (Being cancellation of shares bought back)			25
	Revenue Reserve A/c	Dr.	80	
	To Capital Redemption Reserve A/c (75+5)			80
	(Being creation of capital redemption reserve to the extent of the face value of preference shares redeemed and equity shares bought back)			

(ii) Balance Sheet of Anu Ltd as at 1.4.20X1

(in crores Rs.)

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	20

	B	Reserves and Surplus	2	280
2		Current liabilities		
	A	Trade Payables		40
		Total		340
		Assets		
1		Non-current assets		
	A	Property, plant and equipment	3	-
	B	Non-Current Investments	4	100
2		Current assets		
	A	Trade receivables		140
	B	Cash and Cash equivalents	5	100
		Total		340

Notes to accounts

No.	Particulars		Rs.
1	Share Capital		
	Authorized, issued and subscribed share capital		
	200 lakhs Equity shares of Rs.10 each fully paid		<u>20</u>
	Total		<u>20</u>
2	Reserves and Surplus		
	Capital reserve		15
	Capital redemption reserve		80
	Securities premium	25	
	Less: Utilization for buy-back of shares	<u>(20)</u>	5
	Revenue Reserve	260	
	Less: transfer to Capital redemption reserve	<u>(80)</u>	<u>180</u>
	Total		<u>280</u>
3	Property, plant and Equipment		
	PPE: cost		100
	Less: Provision for depreciation		<u>(100)</u>
	Net carrying value		-
4	Non-Current Investments		
	Non-current investments at cost		<u>100</u>
	(Market value Rs.400 Crores)		
5	Cash and Cash Equivalents		
	Cash and Cash Equivalents as on 31.3.20X1		200
	Less: Bank payment for redemption and buy-back		<u>(100)</u>
	Total		<u>100</u>

Illustration 3

Dee Limited (a non-listed company) furnishes the following Balance Sheet as at 31st March, 20X1:
(in thousand Rs.)

Particulars			Notes	Rs.
1		Equity and Liabilities		
2	A	Shareholders' funds		
		Share capital	1	2,700
	B	Reserves and Surplus	2	9,700
		Current liabilities		
	A	Trade Payables		<u>1,400</u>
		Total		<u>13,800</u>
1		Assets		
		Non-current assets		9,300
	A	Property, plant and Equipment		3,000
	B	Non-Current Investments		
2		Current assets		
	A	Inventories		500
	B	Trade receivables		200
	C	Cash and Cash equivalents		800
		Total		13,800

Notes to accounts

No.	Particulars	Rs.
1	Share Capital	
	Authorized, issued and subscribed capital:	
	2,50,000 Equity shares of Rs.10 each fully paid up	2,500
	2,000, 10% Preference shares of Rs.100 each	200
	(Issued two months back for the purpose of buy-back)	
	Total	<u>2,700</u>
2	Reserves and Surplus	
	Capital reserve	1,000
	Revenue reserve	3,000
	Securities premium	2,200
	Profit and loss account	<u>3,500</u>
	Total	<u>9,700</u>

The company passed a reSolution: to buy-back 20% of its equity capital @ Rs.50 per share. For this purpose, it sold all of its investment for Rs.22,00,000.

You are required to pass necessary journal entries and prepare the Balance Sheet.

Solution:

Journal Entries in the books of Dee Limited

(in thousand Rs.)

	Particulars		Dr.	Cr.
(i)	Bank Account	Dr.	2,200	
	Profit and Loss Account	Dr.	800	
	To Investment Account			3,000
	(Being the investments sold at loss for the purpose of buy-back)			
(ii)	Equity Share buy-back Account	Dr.	2,500	
	To Bank Account			2,500
	(Being the payment made on buy-back)			
(iii)	Equity Share Capital Account	Dr.	500	
	Premium Payable on Buy-Back Account	Dr.	2,000	
	To Equity Shares Buy-Back Account			2,500
	(Being the buy-back amount allocated to equity share capital)			
(iv)	Securities premium Account	Dr.	2,000	
	To Premium payable on buy-back Account			2,000
	(Being the premium payable on buy-back adjusted against securities premium account)			
(v)	Revenue reserve Account	Dr.	300	
	To Capital Redemption Reserve Account			300
	(Being the amount equal to nominal value of equity shares bought back out of free reserves transferred to capital redemption reserve account)			

Balance Sheet of Dee Limited as at 1st April, 20X1 (After buy-back of shares)

(in thousand Rs.)

	Particulars	Notes	Rs.
	Equity and Liabilities		
1	Shareholders' funds		
	A Share capital	1	2,200
	B Reserves and Surplus	2	6,900
2	Current liabilities		
	A Trade Payables		1,400
	Total		10,500
	Assets		
1	Non-current assets		

	A	Property, plant and Equipment		9,300
2		Current assets		
	A	Inventories		500
	B	Trade receivables		200
	C	Cash and Cash equivalents		500
		Total		10,500

Notes to accounts

No.	Particulars		Rs.
1	Share Capital		
	Authorized, issued and subscribed capital:		
	2,50,000 Equity shares of Rs.10 each fully paid up		2,000
	2,000, 10% Preference shares of Rs.100 each		200
	(Issued two months back for the purpose of buy- back)		—
	Total		<u>2,200</u>
2	Reserves and Surplus		
	Capital reserve		1,000
	Capital redemption reserve		300
	Securities Premium	2,200	
	Less: Premium payable on buy-back of shares	<u>(2,000)</u>	200
	Revenue reserve	3,000	
	Less: Transfer to Capital redemption reserve	<u>(300)</u>	2,700
	Profit and loss A/c	3,500	
	Less: Loss on investment	<u>(800)</u>	<u>2,700</u>
	Total		<u>6,900</u>

Illustration 4

Extra Ltd. (a non-listed company) furnishes you with the following Balance Sheet as at 31st March, 20X1:

(in lakhs Rs.)

	Particulars	Notes	Rs.
	Equity and Liabilities		
1	Shareholders' funds		
	A Share capital	1	120
	B Reserves and Surplus	2	118
2	Non-current liabilities		
	Long term borrowings	3	4

3		Current liabilities		
	A	Trade Payables		70
		Total		312
		Assets		
1		Non-current assets		
	A	Property, plant and Equipment		50
	B	Non-current Investments		120
2		Current assets		
	A	Cash and Cash equivalents		142
		Total		312

Notes to accounts

No.	Particulars		Rs.
1	Share Capital Authorized, issued and subscribed capital: Equity shares of Rs.10 each fully paid 9% Redeemable preference shares of Rs.100 each fully paid Total		100 <u>20</u> 120
2	Reserves and Surplus Capital reserves Revenue reserves Securities premium Total		8 50 <u>60</u> 118
3	Long term borrowings 10% Debentures		<u>4</u>

- (i) The company redeemed the preference shares at a premium of 10% on 1st April, 20X1.
- (ii) It also bought back 3 lakhs equity shares of Rs.10 each at Rs.30 per share. The payment for the above was made out of huge bank balances.
- (iii) Included in its investment were “investments in own debentures” costing Rs.2 lakhs (face value Rs.2.20 lakhs). These debentures were cancelled on 1st April, 20X1.
- (iv) The company had 1,00,000 equity stock options outstanding on the above- mentioned date, to the employees at Rs.20 when the market price was Rs.30 (This was included under current liabilities) On 1.04.20X1 employees exercised their options for 50,000 shares.
- (v) Pass the journal entries to record the above.
- (vi) Prepare Balance Sheet as at 01.04.20X1.

Solution:
(Rs.in lakhs)

Date	Particulars		Debit	Credit
20X1				
1 st April	9% Redeemable preference share capital A/c	Dr.	20.00	
	Premium on redemption of preference shares A/c	Dr.	2.00	
	To Preference shareholders A/c			22.00
	(Being preference share capital transferred to shareholders account)			
	Preference shareholders A/c	Dr.	22.00	
	To Bank A/c			22.00
	(Being payment made to shareholders)			
	Equity shares buy-back A/c	Dr.	90.00	
	To Bank A/c			90.00
	(Being 3 lakhs equity shares of Rs.10 each bought back @ Rs.30 per share)			
	Equity share capital A/c	Dr.	30.00	
	Securities premium A/c	Dr.	60.00	
	To Equity Shares buy-back A/c			90.00
	(Being cancellation of shares bought back)			
	Revenue reserve A/c	Dr.	50.00	
	To Capital redemption reserve A/c			50.00
	(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)			
	10% Debentures A/c	Dr.	2.20	
	To Investment (own debentures) A/c			2.00
	To Profit on cancellation of own debentures A/c			0.20
	(Being cancellation of own debentures costing Rs.2 lakhs, face value being Rs.2.20 lakhs and the balance being profit on cancellation of debentures)			
	Bank A/c	Dr.	10.00	
	Employees stock option outstanding (Current liabilities) A/c	Dr.	5.00	
	To Equity share capital A/c			5.00

	To Securities premium A/c			10.00
	(Being the allotment to employees, of 50,000 shares of Rs.10 each at a premium of 20 per share in exercise of stock options by employees)			
	Securities premium A/c	Dr.	2.00	
	To Premium on redemption of preference shares A/c			2.00
	(Being premium on redemption of preference shares adjusted through securities premium)			

Balance Sheet of Extra Ltd. as at 01.04.20X1

(in lakhs Rs.)

Particulars			Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	A	Share capital	1	75.00
	B	Reserves and Surplus	2	66.20
2		Non-current liabilities		
		Long term borrowings	3	1.80
3		Current liabilities		
	A	Other Current Liabilities	4	65.00
		Total		208
1		Assets		
		Non-current assets		
	A	Property, plant and Equipment		50.00
	B	Non-current Investments	5	118.00
2		Current assets		
	A	Cash and Cash equivalents	6	40.00
		Total		208

Notes to accounts

No.	Particulars		Rs.
1	Share Capital		
	Equity shares of Rs.10 each fully paid		100
	Less: Cancellation of bought back shares		(30)
	Add: Shares issued against ESOP		5
	Total		75
2	Reserves and Surplus		
	Capital Reserve		

	Opening balance	8.00	
	Add: Profit on cancellation of debentures	<u>0.20</u>	8.20
	Revenue reserves		
	Opening balance	50.00	
	Less: Creation of Capital Redemption Reserve	<u>(50.00)</u>	-
	Securities Premium		
	Opening balance	60.00	
	Less: Adjustment for cancellation of equity shares	<u>(60.00)</u>	
	Less: Adjustment for premium on redemption of preference shares	<u>(2.00)</u>	
	Add: Shares issued against ESOP at premium	<u>10.00</u>	8.00
	Capital Redemption Reserve		<u>50.00</u>
	Total		<u>66.20</u>
3	Long term borrowings		
	10% Debentures		4.00
	Less: Cancellation of own debentures		<u>(2.20)</u>
	Total		<u>1.80</u>
4.	Other Current liabilities		
	Opening balance		70.00
	Less: Adjustment for ESOP outstanding		<u>(5.00)</u>
	Total		<u>65.00</u>
5.	Non-current investments		
	Opening balance		120.00
	Less: Investment in own debentures		<u>(2.00)</u>
	Total		<u>118.00</u>
6.	Cash and Cash Equivalents		
	Opening balance		142.00
	Less: Payment to preference shareholders		<u>(22.00)</u>
	Less: Payment to equity shareholders		<u>(90.00)</u>
	Add: Share price received against ESOP		<u>10.00</u>
	Total		<u>40.00</u>

Illustration 5

Pratham Ltd. (a non-listed company) has the following Capital structure as on 31st March, 20X1:

Particulars	Rs.	Rs.
Equity Share Capital (shares of Rs.10 each fully paid)		30,00,000

Reserves & Surplus		
General Reserve	32,50,000	
Security Premium Account	6,00,000	
Profit & Loss Account	4,30,000	
Revaluation Reserve	<u>6,20,000</u>	49,00,000
Loan Funds		42,00,000

You are required to compute by Debt Equity Ratio Test, the maximum number of shares that can be bought back in the light of above information, when the offer price for buy-back is Rs.30 per share.

Solution:

Debt Equity Ratio Test

	Particulars	Rs.
(a)	Loan funds	42,00,000
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (Rs.in crores)	21,00,000
(c)	Present equity shareholders fund (Rs.in crores)	72,80,000
(d)	Future equity shareholder fund (Rs.in crores) (See Note 2)	59,85,000 (72,80,000-12,95,000)
(e)	Maximum permitted buy-back of Equity (Rs.in crores) [(d) – (b)] (See Note 2)	38,85,000 (by simultaneous equation)
(f)	Maximum number of shares that can be bought back @ Rs.30 per share (shares in crores) (See Note 2)	1,29,500 (by simultaneous equation)

Working Note:

1. Shareholders' funds

Particulars	Rs.
Paid up capital	30,00,000
Free reserves (32,50,000 + 6,00,000 + 4,30,000)	<u>42,80,000</u>
	<u>72,80,000</u>

2. As per section 68 of the Companies Act, 2013, amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

Suppose amount equivalent to nominal value of bought back shares transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.

Equation 1 : (Present equity – Nominal value of buy-back transfer to CRR) – Minimum equity to be maintained = Maximum permissible buy-back of equity.

$$(72,80,000 - x) - 21,00,000 = y \quad (1)$$

$$\text{Since } 51,80,000 - x = y$$

$$\text{Equation 2: } \left(\frac{\text{Maximum buy - back}}{\text{Offer price for buy - back}} \times \text{Nominal Value} \right)$$

= Nominal value of the shares bought –back to be transferred to CRR

$$= \left(\frac{y}{30} \times 10 \right) = x$$

$$3x = y \quad (2)$$

x = Rs.12,95,000 crores and

y = Rs.38,85,000 crores

Illustration 6

Perrotte Ltd. (a non-listed company) has the following Capital Structure as on 31.03.20X1:

	Particulars	(Rs.in crores)	
(1)	Equity Share Capital (Shares of Rs.10 each fully paid)	-	330
(2)	Reserves and Surplus		
	General Reserve	240	-
	Securities Premium Account	90	-
	Profit & Loss Account	90	-
	Infrastructure Development Reserve	180	600
(3)	Loan Funds		1,800

The Shareholders of Perrotte Ltd., on the recommendation of their Board of Directors, have approved on 12.09.20X1 a proposal to buy-back the maximum permissible number of Equity shares considering the large surplus funds available at the disposal of the company.

The prevailing market value of the company's shares is Rs.25 per share and in order to induce the existing shareholders to offer their shares for buy-back, it was decided to offer a price of 20% over market.

You are also informed that the Infrastructure Development Reserve is created to satisfy Income-tax Act requirements.

You are required to compute the maximum number of shares that can be bought back in the light of the above information and also under a situation where the loan funds of the company were either Rs.1,200 crores or Rs.1,500 crores.

Assuming that the entire buy-back is completed by 09.12.20X1, show the accounting entries in the company's books in each situation.

Solution:**Statement determining the maximum number of shares to be bought back****Number of shares**

Particulars	When loan fund is		
	Rs.1,800 crores	Rs.1,200 crores	Rs.1,500 crores
Shares Outstanding Test(W.N.1)	8.25	8.25	8.25
Resources Test (W.N.2)	6.25	6.25	6.25
Debt Equity Ratio Test (W.N.3)	Nil	3.75	Nil
Maximum number of shares that can be bought back [least of the above]	Nil	3.75	Nil

Journal Entries for the Buy-Back (applicable only when loan fund is Rs.1,200 crores)**Rs.in crores**

	Particulars		Debit	Credit
(a)	Equity share buy-back account	Dr.	112.5	
	To Bank account			112.5
	(Being buy-back of 3.75 crores equity shares of Rs. 10 each @ Rs.30 per share)			
(b)	Equity share capital account	Dr.	37.5	
	Securities premium account	Dr.	75	
	To Equity share buy-back account			112.5
	(Being cancellation of shares bought back)			
(c)	General reserve account	Dr.	37.5	
	To Capital redemption reserve account			37.5
	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out of redeemed through free reserves)			

Working Notes:**1. Shares Outstanding Test**

Particulars	(Shares in crores)
Number of shares outstanding	33
25% of the shares outstanding	8.25

2. Resources Test

Particulars	
Paid up capital (Rs.in crores)	330
Free reserves (Rs.in crores)	<u>420</u>

Shareholders' funds (Rs.in crores)	750
25% of Shareholders fund (Rs.in crores)	Rs.187.5 crores
Buy-back price per share	Rs.30
Number of shares that can be bought back (shares in crores)	6.25 crores shares

3. Debt Equity Ratio Test

	Particulars	When loan fund is		
		Rs. 1,800 crores	Rs.1,200 crores	Rs.1,500 crores
(a)	Loan funds (Rs.in crores)	1,800	1,200	1,500
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (Rs.in crores)	900	600	750
(c)	Present equity shareholders fund (Rs.in crores)	750	750	750
(d)	Future equity shareholder fund (Rs.in crores) (See Note 2)	N.A.	712.5 (750-37.5)	N.A.
(e)	Maximum permitted buy-back of Equity (Rs.in crores) [(d) (b)] (See Note 2)	Nil	112.5 (by simultaneous equation)	Nil
(f)	Maximum number of shares that can be bought back @ Rs.30 per share (shares in crores) (See Note 2)	Nil	3.75 (by simultaneous equation)	Nil

Note:

- Under Situations 1 & 3 the company does not qualify for buy-back of shares as per the provisions of the Companies Act, 2013.
- As per section 68 of the Companies Act, 2013, the ratio of debt owed by the company should not be more than twice the capital and its free reserve after such buy-back. In the question, it is stated that the company has surplus funds to dispose of therefore, it is presumed that buy-back is out of free reserves or securities premium and hence a sum equal to the nominal value of the share bought back shall be transferred to Capital Redemption Reserve (CRR). Utilization of CRR is restricted to issuance of fully paid-up bonus shares only. It means CRR is not available for distribution as dividend. Hence, CRR is not a free reserve. Therefore, for calculation of future equity i.e. share capital and free reserves, amount transferred to CRR on buy-back has to be excluded from present equity.
Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

Suppose amount equivalent to nominal value of bought back shares transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.

Then

Equation 1 : (Present equity – Nominal value of buy-back transfer to CRR) – Minimum equity to be maintained = Maximum permissible buy-back of equity

$$(750 - x) - 600 = y \quad (1)$$

$$\text{Since } 150 - x = y$$

$$\text{Equation 2: } \left(\frac{\text{Maximum buy-back}}{\text{Offer price for buy-back}} \times \text{Nominal Value} \right)$$

= Nominal value of the shares bought –back to be transferred to CRR

$$= \left(\frac{y}{30} \times 10 \right) = x$$

[here (30 = 25% x 120)]

$$\text{Or } 3x = y \quad (2)$$

by solving the above two equations we get

x = Rs.37.5 crores

y = Rs.112.5 crores



TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. As per section 68(1) of the Companies Act, buy-back of own shares by the company, shall not exceed
 - (a) 25% of the total paid-up capital and free reserves of the company.
 - (b) 20% of the total paid-up capital and free reserves of the company.
 - (c) 15% of the total paid-up capital and free reserves of the company.
 - (d) 10% of the total paid-up capital and free reserves of the company.
2. The companies are permitted to buy-back their own shares out of
 - (a) Free reserves and Securities premium
 - (b) Proceeds of the issue of any shares.
 - (c) Both (a) and (b)
 - (d) Neither (a) nor (b).
3. When a company purchases its own shares out of free reserves; a sum equal to nominal value of shares so purchased shall be transferred to
 - (a) Revenue redemption reserve.
 - (b) Capital redemption reserve.
 - (c) Buy-back reserve
 - (d) Special reserve
4. State which of the following statements is true?
 - (a) Buy-back is for more than twenty-five per cent of the total paid-up capital and free reserves of the company.
 - (b) Partly paid shares cannot be bought back by a company.
 - (c) Buy-back of equity shares in any financial year shall exceed twenty-five per cent of its total paid-up equity capital in that financial year.
 - (d) Partly paid shares can be bought back by a company.
5. Premium (excess of buy-back price over the par value) paid on buy-back should be adjusted against
 - (a) Free reserves.
 - (b) Securities premium.
 - (c) Both (a) and (b).
 - (d) Neither (a) nor (b).



6. Advantages of Buy-back of shares include to
- (a) Encourage others to make hostile bid to take over the company.
 - (b) Decrease promoters holding as the shares which are bought back are cancelled.
 - (c) Discourage others to make hostile bid to take over the company as the buy-back will increase the promoters holding.
 - (d) All of the above.

Answer to the Multiple Choice Questions

1.	(a)	2.	(c)	3.	(b)	4.	(b)	5.	(c)	6.	(c)

7. What are the conditions to be fulfilled by a Joint Stock Company to buy-back its equity shares as per Companies Act, 2013? Explain in brief.

Answer:

Section 68 to 70 of the Companies Act, 2013 lays down the provisions for a company to buy-back its own equity shares. For details, refer Para 1.1 and 1.2 of the chapter.



SCENARIO BASED QUESTIONS

8. SMM Ltd. has the following capital structure as on 31st March, 20X1:

Rs.in crore

	Particulars	Situation I	Situation II
(i)	Equity share capital (shares of Rs.10 each)	1,200	1,200
(ii)	Reserves:		
	General Reserves	1,080	1,080
	Securities Premium	400	400
	Profit & Loss	200	200
	Infrastructure Development Reserve (Statutory Reserve)	320	320
(iii)	Loan Funds	3,200	6,000

The company has offered buy-back price of Rs.30 per equity share. You are required to calculate maximum permissible number of equity shares that can be bought back in both situations and also required to pass necessary Journal Entries.

Answer:

Statement determining the maximum number of shares to be bought back

Number of shares (in crores)

Particulars	When loan fund is	
	Rs.3,200 crores	Rs.6,000 crores
Shares Outstanding Test (W.N.1)	30	30
Resources Test (W.N.2)	24	24
Debt Equity Ratio Test (W.N.3)	32	Nil
Maximum number of shares that can be bought back [least of the above]	24	Nil

Journal Entries for the Buy-Back (applicable only when loan fund is Rs.3,200 crores)

Rs.in crores				
	Particulars		Debit	Credit
(a)	Equity shares buy-back account	Dr.	720	720
	To Bank account			
	(Being payment for buy-back of 24 crores equity shares of Rs.10 each @ Rs.30 per share)			
(b)	Equity share capital account	Dr.	240	
	Premium Payable on buy-back account	Dr.	480	
	To Equity share buy-back account			720
	(Being cancellation of shares bought back)			
	Securities Premium account General Reserve / Profit & Loss A/c	Dr.	400	

	To Premium Payable on buy-back account (Being Premium Payable on buy-back account charged to securities premium and general reserve/Profit & Loss A/c)	Dr.	80	480
(c)	General Reserve / Profit & Loss A/c	Dr.	240	240
	To Capital redemption reserve account			
	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out of redeemed through free reserves)			

Working Notes:

1. Shares Outstanding Test

Particulars	(Shares in crores)
Number of shares outstanding	120
25% of the shares outstanding	30

2. Resources Test

Particulars	
Paid up capital (Rs.in crores)	1,200
Free reserves (Rs.in crores) (1,080 + 400 +200)	<u>1,680</u>
Shareholders' funds (Rs.in crores)	<u>2,880</u>
25% of Shareholders fund (Rs.in crores)	Rs.720 crores
Buy-back price per share	Rs.30
Number of shares that can be bought back	24 crores shares

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

Particulars		When loan fund is	
		Rs.3,200 crores	Rs.6,000 crores
(a)	Loan funds (Rs.)	3,200	6,000
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (Rs.) (a/2)	1,600	3,000
(c)	Present equity shareholders fund (Rs.)	2,880	2,880
(d)	Future equity shareholders fund (Rs.) (see W.N.4)	2,560 (2,880-320)	N.A.
(e)	Maximum permitted buy- back of Equity (Rs.) [(d) – (b)]	960	Nil
(f)	Maximum number of shares that can be bought back @ Rs.30 per share	32 crore shares	Nil
	As per the provisions of the Companies Act, 2013, company	Qualifies	Does not Qualify

4. 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

$$= (2,880 - x) - 1,600 = y$$

$$= 1280 - x = y \quad (1)$$

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

$$y/30 \times 10 = x \text{ or}$$

$$3x = y \quad (2)$$

by solving the above two equations we get $x = \text{Rs.}320$

$$y = \text{Rs.}960$$

9. KG Limited furnishes the following Balance Sheet as at 31st March, 20X1:

Particulars			Notes	Rs.
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	1,200
	B	Reserves and Surplus	2	810
2		Non-current liabilities		
		Long term borrowings		750
			3	
3		Current liabilities		
	A	Trade Payables		745
	B	Other Current Liabilities		195
		Total		3,700
		Assets		
1		Non-current assets		
	A	Property, plant and equipment	4	2,026
	B	Non-current Investments		74
2		Current assets		
	A	Inventories		600
	B	Trade receivables		260
	C	Cash and Cash equivalents		740
		Total		3,700

Notes to accounts

No.	Particulars	Rs.
1	Share Capital	
	Authorized, issued and subscribed capital	
	Equity share capital (fully paid up shares of Rs.10 each)	<u>1,200</u>
2	Reserves and Surplus	
	Securities premium	175
	General reserve	265
	Capital redemption reserve	200
	Profit & loss A/c	<u>170</u>
	Total	<u>810</u>
3	Long term borrowings	
	12% Debentures	<u>750</u>
4	Property, plant and equipment	
	Land and Building	1,800
	Plant and machinery	<u>226</u>
	Net carrying value	2,026

On 1st April, 20X1, the company announced the buy-back of 25% of its equity shares @ Rs.15 per share. For this purpose, it sold all of its investments for Rs.75 lakhs.

On 5th April, 20X1, the company achieved the target of buy-back. On 30th April, 20X1 the company issued one fully paid up equity share of Rs.10 by way of bonus for every four equity shares held by the equity shareholders.

You are required to:

- (1) Pass necessary journal entries for the above transactions.
- (2) Prepare Balance Sheet of KG Limited after bonus issue of the shares.

Answer:

In the books of KG Limited Journal Entries

Date 20X1	Particulars	Dr. (Rs.in lakhs)	Cr.
April 1	Bank A/c Dr. To Investment A/c To Profit on sale of investment (Being investment sold on profit)	75	74 1
April 5	Equity share capital A/c Dr. Securities premium A/c Dr. To Equity shares buy-back A/c	300 150	450

April 5	(Being the amount due to equity shareholders on buy-back)	450	450
	Equity shares buy-back A/c Dr. To Bank A/c (Being the payment made on account of buy- back of 30 Lakh Equity Shares)		
	General reserve A/c Dr. Profit and Loss A/c Dr. To Capital redemption reserve A/c (Being amount equal to nominal value of buy- back shares from free reserves transferred to capital redemption reserve account as per the law)	265 35	300
April 30	Capital redemption reserve A/c Dr. To Bonus shares A/c (W.N.1) (Being the utilization of capital redemption reserve to issue bonus shares)	225	225
	Bonus shares A/c Dr. To Equity share capital A/c (Being issue of one bonus equity share for every four equity shares held)	225	225

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

Particulars			Notes	Rs.
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	1,125
	B	Reserves and Surplus	2	436
2		Non-current liabilities		
		Long term borrowings	3	750
3		Current liabilities		
	A	Trade Payables		745
	B	Other Current Liabilities		195
		Total		3,251
		Assets		
1		Non-current assets		
	A	Property, plant and equipment	4	2,026
2		Current assets		
	A	Inventories		600

B	Trade receivables		260
C	Cash and Cash equivalents		365
	Total		3,251

Notes to accounts

No.	Particulars		Rs.
1	Share Capital		
	Authorized, issued and subscribed capital:		
	Equity share capital (fully paid up shares of Rs. 10 each)		<u>1,125</u>
2	Reserves and Surplus		
	General Reserve	265	
	Less: Transfer to CR	<u>(265)</u>	-
	Capital Redemption Reserve	200	
	Add: Transfer due to buy-back of shares from P/L	35	
	Add; Transfer due to buy-back of shares from General Reserve	265	
	Less: Utilisation for issue of bonus shares	<u>(225)</u>	275
	Securities premium	175	
	Less: Adjustment for premium paid on buy- back	<u>(150)</u>	25
	Profit & Loss A/c	170	
	Add: Profit on sale of investment	1	
	Less: Transfer to CRR	<u>(35)</u>	<u>136</u>
	Total		<u>436</u>
3	Long term borrowings		
	12% Debentures		<u>750</u>
4	Property, Plant and Equipment		
	Land and Building		1,800
	Plant and machinery		<u>226</u>
	Net carrying value		2,026

Working Notes:

- Amount of bonus shares = 25% of (1,200 – 300) lakhs = Rs.225 lakhs
- Cash at bank after issue of bonus shares

Particulars	Rs.in lakhs
Cash balance as on 1 st April, 20X1	740
Add: Sale of investments	<u>75</u>
	815
Less: Payment for buy-back of shares	<u>(450)</u>
	<u>365</u>

Note: In the given Solution:, it is possible to adjust transfer to capital redemption reserve account or capitalization of bonus shares from any other free reserves or securities premium (to the extent available) also.

10. Following is the Balance Sheet of Competent Limited as at 31st March, 20X1:

Particulars			Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	A	Share capital	1	12,50,000
	B	Reserves and Surplus	2	18,75,000
2		Non-current liabilities		
		Long term borrowings	3	28,75,000
3		Current liabilities		
	A	Other Current Liabilities		16,50,000
		Total		76,50,000
		Assets		
1		Non-current assets		
	A	Property, plant and Equipment	4	46,50,000
2		Current assets		
	A	Other Current Assets		30,00,000
		Total		76,50,000

Notes to accounts

No.	Particulars	Rs.
1	Share Capital	
	Authorized, issued and subscribed capital:	
	Equity share capital (fully paid up shares of Rs.10 each)	<u>12,50,000</u>
2	Reserves and Surplus	
	Securities premium	2,50,000
	Profit and loss account	1,25,000
	Revenue reserve	<u>15,00,000</u>
	Total	<u>18,75,000</u>
3	Long term borrowings	
	14% Debentures	18,75,000
	Unsecured Loans	<u>10,00,000</u>
	Total	<u>28,75,000</u>
4	Property, plant and equipment	
	Land and Building	19,30,000

	Plant and machinery		18,00,000
	Furniture and fitting		<u>9,20,000</u>
	Net carrying value		<u>46,50,000</u>

The company wants to buy-back 25,000 equity shares of Rs.10 each, on 1st April, 20X1 at Rs.20 per share. Buy-back of shares is duly authorized by its articles and necessary reSolution: has 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 shown as part of Current Assets.

Comment with your calculations, whether buy-back of shares by company is within the provisions of the Companies Act, 2013. If yes, pass necessary journal entries towards buy-back of shares and prepare the Balance Sheet after buy-back of shares.

Answer:

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	1,25,000
25% of the shares outstanding	31,250

2. Resources Test: Maximum permitted limit 25% of Equity paid up capital + Free Reserves

Particulars	
Paid up capital (Rs.)	12,50,000
Free reserves (Rs.) (15,00,000 + 2,50,000 + 1,25,000)	<u>18,75,000</u>
Shareholders' funds (Rs.)	<u>31,25,000</u>
25% of Shareholders fund (Rs.)	7,81,250
Buy-back price per share	Rs.20
Number of shares that can be bought back (shares) Actual Number of	39,062
shares for buy-back	25,000

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

	Particulars	Rs.
(a)	Loan funds (Rs.) (18,75,000 + 10,00,000 + 16,50,000)	45,25,000
(b)	Minimum equity to be maintained after buy- back in the ratio of 2:1 (Rs.) (a/2)	22,62,500
(c)	Present equity/shareholders fund (Rs.)	31,25,000
(d)	Future equity/shareholders fund (Rs.) (see W.N.) (31,25,000 – 2,87,500)	28,37,500 *
(e)	Maximum permitted buy-back of Equity (Rs.) [(d) – (b)]	5,75,000
(f)	Maximum number of shares that can be bought back @ Rs.20 per share	28,750 shares
(g)	Actual Buy-Back Proposed	25,000 Shares

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

Particulars	Number of shares
Shares Outstanding Test	31,250
Resources Test	39,062
Debt Equity Ratio Test	28,750
Maximum number of shares that can be bought back [least of the above]	28,750

Company qualifies all tests for buy-back of shares and came to the conclusion that it can buy maximum 28,750 shares on 1st April, 20X1.

However, company wants to buy-back only 25,000 equity shares @ Rs.20. Therefore, buy-back of 25,000 shares, as desired by the company is within the provisions of the Companies Act, 2013.

Journal Entries for buy-back of shares

	Particulars	Debit (Rs.)	Credit (Rs.)
(a)	Equity shares buy-back account Dr. To Bank account (Being buy-back of 25,000 equity shares of Rs.10 each @ Rs.20 per share)	5,00,000	5,00,000
(b)	Equity share capital account Dr. Securities premium account Dr. To Equity shares buy-back account (Being cancellation of shares bought back)	2,50,000 2,50,000	5,00,000
(c)	Revenue reserve account Dr. To Capital redemption reserve account (Being transfer of free reserves to capital redemption reserve to the extent of nominal value of capital bought back through free reserves)	2,50,000	2,50,000

Balance Sheet of M/s. Competent Ltd. as at 31st March, 20X1

	Particulars	Notes	Rs.
1	Equity and Liabilities		
	Shareholders' funds		
A	Share capital	1	10,00,000
B	Reserves and Surplus	2	16,25,000
2	Non-current liabilities		
	Long term borrowings	3	28,75,000
3	Current liabilities		
A	Other Current Liabilities		16,50,000
	Total		71,50,000

1		Assets		
		Non-current assets		
	A	Property, plant and equipment	4	46,50,000
2		Current assets		
	A	Other Current Assets (30,00,000 – 5,00,000)		25,00,000
		Total		71,50,000

Notes to accounts

No.	Particulars		Rs.
1	Share Capital		
	Authorized, issued and subscribed capital:		
	Equity share capital (fully paid up shares of Rs.10 each)		<u>10,00,000</u>
2	Reserves and Surplus		
	Profit and Loss A/c		1,25,000
	Revenue reserves	15,00,000	
	Less: Transfer to CRR	<u>(2,50,000)</u>	12,50,000
	Securities premium	2,50,000	
	Less: Utilization for share buy-back	<u>(2,50,000)</u>	-
	Capital Redemption Reserves		<u>2,50,000</u>
	Total		<u>16,25,000</u>
3	Long term borrowings		
	14% Debentures		18,75,000
	Unsecured Loans		<u>10,00,000</u>
	Total		<u>28,75,000</u>
4	Property, plant and equipment		
	Land and Building		19,30,000
	Plant and machinery		18,00,000
	Furniture and fitting		<u>9,20,000</u>
	Net carrying value		<u>46,50,000</u>

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

$$(31,25,000 - x) - 22,62,500 = y \quad (1)$$

$$= \left(\frac{y}{20} \times 10 \right) = x \text{ or } 2x = y$$

by solving the above equation, we get

$$x = \text{Rs. } 2,87,500$$

$$y = \text{Rs. } 5,75,000$$

11. The following information from Balance Sheet of Z Ltd. as on 31st March ,20X1:

Share Capital:	
Equity shares of Rs.10 each Fully Paid Up	16,000
10% Redeemable Pref. Shares of Rs.10 each Fully Paid Up	5,000
Reserves & Surplus	
Capital Redemption Reserve	2,000
Securities Premium	1,600
General Reserve	12,000
Profit & Loss Account	600
Secured Loans:	
9% Debentures	10,000
Current Liabilities:	
Trade payables	4,600
Sundry Provisions	<u>2,000</u>
Fixed Assets	28,000
Investments	4,700
Cash at Bank	4,600
Other Current Assets	16,500

On 1st April, 20X1 the Company redeemed all its Preference Shares at a Premium of 10% and bought back 10% of its Equity Shares at Rs.20 per Share. In order to make cash available, the Company sold all the Investments for Rs.5,000 lakhs.

You are required to pass journal entries for the above and prepare the Company's Balance sheet immediately after buyback of equity shares and redemption of preference shares.

Answer:

(i) Journal Entries in the books of Z Ltd. (Rs.in lakhs)

	Particulars			
1	Bank A/c To Investments A/c To Profit and Loss A/c (Being investment sold on profit for the purpose of buy-back)	Dr.	5,000	4,700 300
2	10% Redeemable Preference Share Capital A/c	Dr.	5,000	

	Premium on Redemption of Preference Shares A/c To Preference Shareholders A/c (Being redemption of preference share capital at premium of 10%)	Dr.	500	5,500
3	Profit and Loss A/c To Premium on Redemption of Preference Shares A/c (Being premium on redemption of preference shares adjusted through securities premium)	Dr.	500	500
4	Equity Share Capital A/c Premium on buyback To Equity buy-back A/c (Being Equity Share bought back, Share Capital cancelled, and Premium on Buyback accounted for)	Dr. Dr.	1,600 1,600	3,200
5	Securities Premium A/c (1,600) To Premium on Buyback A/c (Being premium on buyback provided out of securities premium)	Dr.	1,600	1,600
6	Preference Shareholders A/c Equity buy-back A/c To Bank A/c (Being payment made to preference shareholders and equity shareholders)		5,500 3,200	8,700
7	General Reserve Account To Capital Redemption Reserve Account (Being amount transferred to capital redemption reserve account towards face value of preference shares redeemed and equity shares bought back)		6,600	6,600

(ii) Balance Sheet of C Ltd. (after Redemption and Buyback)

(Rs.Lakhs)

	Particulars	Note No	Amount
	EQUITY AND LIABILITIES		Rs.
(I)	Shareholders' Funds:		
	(a) Share Capital	1	14,400
	(b) Reserves and Surplus	2	14,400
(2)	Non-Current Liabilities:		
	(a) Long Term Borrowings	3	10,000
(3)	Current Liabilities:		
	(a) Trade payables		4,600
	(b) Short Term Provisions		<u>2,000</u>
	Total		<u>45,400</u>

(II)	ASSETS		
	Non-Current Assets		
(1)			
	PPE		28,000
	Current Assets:		
	(a) Cash and Cash equivalents (W N)		900
	(b) Other Current Assets		<u>16,500</u>
			<u>45,400</u>

Notes to Accounts

		Rs.in Lakhs		
1.	Share Capital 1,440 lakh Equity Shares of Rs.10 each Fully Paid up (160 lakh Equity Shares bought back)			14,400
2.	Reserves and Surplus General Reserve Less: Transfer to CRR Capital Redemption Reserve Add: Transfer due to buy-back of shares from Gen. res. Securities premium Less: Adjustment for premium paid on buy back Profit & Loss A/c Add: Profit on sale of investment Less: Adjustment for premium paid on redemption of preference shares	12,000 (6,600) 2,000 6,600 1,600 (1,600) 600 300 (500)	5,400 8,600 400	14,400
3.	Long-term borrowings Secured 9 % Debentures			10,000

Working Note:

Bank Account

	Amount		Amount
	(Rs.Lakhs)		(Rs.Lakhs)
To balance b/d	4,600	By Preference Shareholders A/c	5,500
To Investment A/c (sale Proceeds)	5,000	By Equity buy back A/c	3,200
		By Balance c/d (Balancing figure)	<u>900</u>
	<u>9,600</u>		<u>9,600</u>

QUESTIONS FROM RTP'S, MTP'S, QP'S

Question 1

Following is the summarized Balance Sheet of Complicated Ltd. as on 31st March, 2016:

Liabilities	Amount (Rs.)
Equity shares of Rs. 10 each, fully paid up	12,50,000
Bonus shares of Rs. 10 each, fully paid up	1,00,000
Share option outstanding Account	4,00,000
Revenue Reserve	15,00,000
Securities Premium	2,50,000
Profit & Loss Account	1,25,000
Capital Reserve	2,00,000
Unpaid dividends	1,00,000
12% Debentures (Secured)	18,75,000
Advance from related parties (Unsecured)	10,00,000
Current maturities of long term borrowings	16,50,000
Application money received for allotment due for refund	2,00,000
	86,50,000
Property, Plant & Equipment	46,50,000
Current Assets	40,00,000
	86,50,000

The Company wants to buy back 25,000 equity shares of Rs. 10 each, on 1st April, 2016 at Rs. 20 per share. Buy back of shares is duly authorized by its Articles and necessary resolution has been passed by the Company towards this. The buy-back of shares by the Company is also within the provisions of the Companies Act, 2013. The payment for buy back of shares will be made by the Company out of sufficient bank balance available shown as part of Current Assets. You are required to prepare the necessary journal entries towards buy back of shares and prepare the Balance Sheet after buy back of shares. (MTP May'22)

Answer :

As per the information given in the Question, buy-back of 25,000 shares @ Rs. 20, as desired by the company, is within the provisions of the Companies Act, 2013.

Journal Entries for buy-back of shares

		Debit	Credit
(a) Equity Share buyback account	Dr.	5,00,000	
To Bank Account			5,00,000
(Being buy back of 25,000 equity shares of Rs. 10 each @ Rs. 20)			

20 per share)			
(b) Equity shares capital account	Dr.	2,50,000	
Securities premium account		2,50,000	
To Equity shares buy-back account (Being cancellation of shares bought back)			5,00,000
(c) Revenue reserve account		2,50,000	
To Capital redemption reserve account (Being transfer of free reserves to capital redemption reserve to the extent of nominal value of capital bought back through free reserves)			2,50,000

Balance Sheet of Complicated Ltd.as on 1st April, 2016

Particulars	Note No	Amount Rs.
EQUITY AND LIABILITIES		
1 Shareholders' funds		
(a) Share capital	1	11,00,000
(b) Reserves and Surplus	2	22,25,000
2 Non-current liabilities		
(a) Long-term borrowings	3	28,75,000
3 Current liabilities		
(a) Other current liabilities	4	19,50,000
Total		81,50,000
ASSETS		
1 Non-current assets		
(a) Property, Plant & Equipment		46,50,000
2 Current assets (40,00,000–5,00,000)		35,00,000
Total		81,50,000

Notes to Accounts

			Rs.	Rs.
1.	Share Capital			
	Equity share capital			
	1,10,000 Equity shares of Rs.10 each			11,00,000
2.	Reserves and Surplus			
	Profit and Loss A/c		1,25,000	
	Revenue reserves	15,00,000		
	Less: Transfer to CRR	(2,50,000)	12,50,000	

	Securities premium	2,50,000		
	Less: Utilization for share buy-back	(2,50,000)	–	
	Share Option Outstanding Account		4,00,000	
	Capital Reserve		2,00,000	
	Capital Redemption Reserve		2,50,000	22,25,000
3.	Long-term borrowings			
	Secured			
	12% Debentures		18,75,000	
	Unsecured loans		10,00,000	28,75,000
4.	Other Current Liabilities			
	Current maturities of long term borrowings		16,50,000	
	Unpaid dividend		1,00,000	
	Application money received for allotment due for refund		2,00,000	19,50,000

Question 2

Alpha Ltd. furnishes the following information as at 31st March, 2021:

	Rs In lakhs	Rs In lakhs
Shareholders' Funds		
Equity share capital (fully paid up shares of Rs 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
Non-current Assets		
Property, plant and equipment		4,052
Current Assets		
Current Investments	148	
Inventories	1,200	
Trade Receivables	520	
Cash and Bank	1,480	3,348

- (i) On 1st April, 2021, the company announced buy-back of 25% of its equity shares @ Rs 15 per share. For this purpose, it sold all its investment for Rs 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 Rs 10 each by way of bonus for every four equity shares held by the equity shareholders by capitalization of Capital Redemption Reserve. Premium (excess of buy-back price over the par value) paid on buy-back should be adjusted against securities premium account. You are required to pass necessary journal entries and prepare the Balance Sheet of Alpha Ltd. after bonus issue.

(MTP Mar'22, PYP Nov'22)

Answer :

In the books of Alpha Limited Journal Entries

Date	Particulars		Dr.	Cr.
2021			(Rs in lakhs)	
April 1	Bank A/c	Dr.	150	
	To Investment A/c			148
	To Profit on sale of investment			2
	(Being investment sold on profit)			
April 10	Equity share capital A/c	Dr.	600	
	Securities premium A/c	Dr.	300	
	To Equity shares buy back A/c			900
	(Being the amount due to equity shareholders on buy back)			
	Equity shares buy back A/c	Dr.	900	
	To Bank A/c			900
	(Being the payment made on account of buy back of Rs 60 Lakh Equity Shares)			
April 10	General reserve A/c	Dr.	530	
	Profit and Loss A/c	Dr.	70	
	To Capital redemption reserve (CRR) A/c			600
	(Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law)			
April 30	Capital redemption reserve A/c	Dr.	450	
	To Bonus shares A/c (W.N.1)			450
	(Being the utilization of capital redemption reserve to issue bonus shares)			

	Bonus shares A/c	Dr.	450	
	To Equity share capital A/c			450
	(Being issue of one bonus equity share for every four equity shares held)			
	Profit on sale of Investment	Dr.	2	
	To Profit and Loss A/c			2
	(Profit on sale transfer to Profit and Loss A/c)			

Note: For transferring amount equal to nominal value of buy back shares from free reserves to capital redemption reserve account, the amount of Rs 340 lakhs from P & L A/c and the balance from general reserve may also be utilized. The combination of different set of amounts (from General Reserve and Profit and Loss Account) aggregating Rs 600 lakhs may also be considered for the purpose of transfer to CRR.

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

Particulars	Note No	Amount (Rs in Lakhs)
I. Equity and Liabilities		
(1) Shareholder's Funds	1	2,250
(a) Share Capital		
(b) Reserves and Surplus	2	872
(2) Non-Current Liabilities		
(a) Long-term borrowings – 12% Debentures		1,500
(3) Current Liabilities		
(a) Trade payables		1,490
(b) Other current liabilities		390
Total		6,502
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment		4,052
(2) Current assets		
(a) Current investments		
(b) Inventory		1,200
(c) Trade receivables		520
(d) Cash and cash equivalents (W.N. 2)		730
Total		6,502

Notes to Accounts

				Rs In lakhs
1.	Share Capital			
	Equity share capital (225 lakh fully paid up shares of Rs 10 each)			2,250
2.	Reserves and Surplus			
	General Reserve	530		
	Less: Transfer to CRR	(530)	–	
	Capital Redemption Reserve	400		
	Add: Transfer due to buy-back of shares from P/L	70		
	Add: Transfer due to buy-back of shares from Gen. res. 530			
	Less: Utilisation for issue of bonus shares	(450)	550	
	Securities premium	350		
	Less: Adjustment for premium paid on buy back	(300)	50	
	Profit & Loss A/c	340		
	Add: Profit on sale of investment	2		
	Less: Transfer to CRR	(70)	272	872

Working Notes:

- Amount of equity share capital = 2,400 – 600 (buyback) + 450 (Bonus shares) = 2,250
- Cash at bank after issue of bonus shares

	Rs in lakhs
Cash balance as on 1st April, 2021	1480
Add: Sale of investments	150
	1630
Less: Payment for buy back of shares	(900)
	730

Question 3

Super Ltd. gives the following information as on 31st March, 2022.

Liabilities	In ₹
Equity Shares of ₹ 10 each fully paid up	17,00,000
Revenue Reserve	23,50,000
Securities Premium	2,50,000
Profit & Loss Account	2,00,000
Infrastructure Development Reserve	1,50,000

9% Debentures	38,00,000
Unsecured Loan	8,50,000
Property, plant & equipment	58,50,000
Current Assets	34,50,000

Super Limited wants to buy back 35,000 equity shares of ₹ 10 each fully paid up on 1st April, 2022 at ₹ 30 per share;

Buy Back of shares is fully authorised by its articles and necessary reSolution:s 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. (MTP Oct'22)

Answer :

Determination of maximum no. of shares that can be bought back 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
Shareholders' funds (₹)	45,00,000
25% of Shareholders fund (₹)	11,25,000
Buy back price per share	₹ 30
Number of shares that can be bought back (shares)	37,500
Actual Number of shares proposed for buy back	35,000

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

	Particulars	₹
(a)	Loan funds (₹) (38,00,000+8,50,000)	46,50,000
(b)	Minimum equity to be maintained after buy back in the ratio of 2:1 (₹) (a/2)	23,25,000
(c)	Present equity/shareholders fund (₹)	45,00,000
(d)	Future equity/shareholders fund (₹) (see W;N;) (45,00,000 – 5,43,750)	39,56,250
(e)	Maximum permitted buy back of Equity (₹) [(d) – (b)]	16,31,250

(f)	Maximum number of shares that can be bought back @ ₹ 30 per share	54,375 shares
(g)	Actual Buy Back Proposed	35,000 Shares

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

Particulars	Number 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 the above]	37,500

Company qualifies all tests for buy-back of shares and it can buy back maximum 37,500 shares on 1st April, 2022.

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

$$(45,00,000 - x) - 23,25,000 = y \quad (1)$$

$$\left(\frac{y}{30} \times 10 \right) = x \text{ Or } 3x = y \quad (2)$$

by solving the above equation, we get

$$x = ₹ 5,43,750$$

$$y = ₹ 16,31,250$$

Question 4

Quick Ltd. has the following capital structure as on 31st March, 2021:

		₹ in Crores	
(1)	Share Capital:		462
	(Equity Shares of ₹ 10 each, fully paid)		
(2)	Reserves and Surplus:		
	General Reserve	336	
	Securities Premium Account	126	
	Profit and Loss Account	126	
	Statutory Reserve	180	

	Capital Redemption Reserve	87	
	Plant Revaluation Reserve	33	888
(3)	Loan Funds:		
	Secured	2,200	
	Unsecured	320	2,520

On the recommendations of the Board of Directors, on 16th September, 2021, the shareholders of the company have approved a proposal to buy-back of equity shares. The prevailing market value of the company's share is ₹ 20 per share and in order to induce the existing shareholders to offer their shares for buy-back, it was decided to offer a price of 50% over market value. The company had sufficient balance in its bank account for the buy-back of shares.

You are required to compute the maximum number of shares that can be bought back in the light of the above information and also under a situation where the loan funds of the company were either ₹ 1,680 Crores or ₹ 2,100 Crores;

Assuming that the entire buy-back is completed by 31st December, 2021, Pass the necessary accounting entries (narrations not required) in the books of the company in each situation (PYP May'22)

Answer :

Statement determining the maximum number of shares to be bought back Number of shares

Particulars	When loan fund is		
	₹ 2,520 crores	₹ 1,680 crores	₹ 2,100 crores
Shares Outstanding Test (W.N.1)	11.55	11.55	11.55
Resources Test (W.N.2)	8.75	8.75	8.75
Debt Equity Ratio Test (W.N.3)	Nil	5.25	Nil
Maximum number of shares that can be bought back [least of the above]	Nil	5.25	Nil

Journal Entries for the Buy-Back (applicable only when loan fund is ₹ 1,680 crores)

₹ in crores

	Particulars		Debit	Credit
(a)	Equity share buy-back account	Dr.	157.5	
	To Bank account			157.5
(b)	Equity share capital account (5;25 x ₹ 10)	Dr.	52.5	
	Securities premium account (5;25 x ₹ 20)	Dr.	105	
	To Equity share buy-back account			157.5
(c)	General reserve account	Dr.	52.5	
	To Capital redemption reserve account			52.5

Working Notes:**1. Shares Outstanding Test**

Particulars	(Shares in crores)
Number of shares outstanding	46.2
25% of the shares outstanding	11.55

2. Resources Test

Particulars	
Paid up capital (₹ in crores)	462
Free reserves (₹ in crores) (336+126+126)	588
Shareholders' funds (₹ in crores)	1,050
25% of Shareholders fund (₹ in crores)	₹ 262.5 crores
Buy-back price per share	₹ 30
Number of shares that can be bought back (shares in crores)	8.75 crores shares

3. Debt Equity Ratio Test

	Particulars	When loan fund is		
		₹ 2,520 crores	₹ 1,680 crores	₹ 2,100 crores
(a)	Loan funds (₹ in crores)	2,520	1,680	2,100
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (₹ in crores)	1,260	840	1,050
(c)	Present equity shareholders fund (₹ in crores)	1,050	1,050	1,050
(d)	Future equity shareholder fund (₹ in crores) (See Note 2)	N.A.	997.5 (1,050-52.5)	N.A.
(e)	Maximum permitted buy-back of Equity (₹ in crores) [(d) - (b)] (See Note 2)	Nil	157.5 (by simultaneous equation)	Nil
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share (shares in crores) (See Note 2)	Nil	5.25 (by simultaneous equation)	Nil

Note:

- Under Situations 1 & 3 the company does not qualify for buy-back of shares as per the provisions of the Companies Act, 2013.
- As per section 68 of the Companies Act, 2013, the ratio of debt owed by the company should not be more than twice the capital and its free reserve after such buy-back.
Amount transferred to CRR and maximum equity to be bought back will be calculated by

simultaneous equation method.

Suppose amount equivalent to nominal value of bought back shares transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y';

Then

Equation 1: (Present equity – Nominal value of buy-back transfer to CRR) – Minimum equity to be maintained = Maximum permissible buy-back of equity

$$(1,050 - x) - 840 = y$$

$$\text{Since } 210 - x = y$$

Maximum buy-back

$$\text{Equation 2} = \left(\frac{\text{Maximum buy - back}}{\text{Offer price for buy - back}} \times \text{Nominal Value} \right)$$

= Nominal value of the shares bought –back to be transferred to CRR

$$\frac{y}{30} \times 10$$

$$\text{Or } 3x = y \quad (2)$$

by solving the above two equations we get

$$x = ₹ 52;5 \text{ crores } y = ₹ 157;5 \text{ crores}$$

3. Statutory reserves, capital redemption reserve and plant revaluation reserves are not free reserves.
4. For calculation of debt –equity ratio both secured and unsecured loans have been considered.



4. AMALGAMATION OF COMPANIES (AS – 14)

ILLUSTRATIONS

Illustration 1

S. Ltd. is absorbed by P. Ltd. S Ltd. gives the following information on the date of absorption:

Rs.

Sundry Assets	13,00,000
Share capital:	
2,000 7% Preference shares of Rs.100 each (fully paid-up)	2,00,000
5,000 Equity shares of Rs.100 each (fully paid-up)	5,00,000
Reserves	3,00,000
6% Debentures	2,00,000
Trade payables	1,00,000

Additional information:

P. Ltd. has agreed:

- (i) to issue 9% Preference shares of Rs.100 each, in the ratio of 3 shares of P. Ltd. for 4 preference shares in S. Ltd.
- (ii) to issue to the debenture-holders in S Ltd. 8% Mortgage Debentures at Rs.96 in lieu of 6% Debentures in S. Ltd. which are to be redeemed at a premium of 20%;
- (iii) to pay Rs.20 per share in cash and to issue six equity shares of Rs.100 each issued at the market value Rs.125 in lieu of every five shares held in S. Ltd.; and
- (iv) to assume the liability to trade payables.

You are required to calculate the purchase consideration.

Solution:

The purchase consideration will be

	Rs.	Form
Preference shareholders: $2,000 \times \frac{3}{4} \times 100$	1,50,000	9% Pref. shares
Equity shareholders: $5,000 \times 20$	1,00,000	Cash
$5,000 \times \frac{6}{5} \times 125$	<u>7,50,000</u>	Equity shares
	<u>10,00,000</u>	

Note:

- According to AS 14, 'consideration' excludes the any amount payable to debenture-holders. The liability in respect of debentures of S Ltd. will be taken by P Ltd., which will then be settled by issuing new 8% debentures.
- The issue of the equity shares is done at Rs. 125 (market value) as it has been mentioned in the question. The face value shall not be considered for this purpose.

Illustration 2

Following is the balance sheet of A Ltd. as on 31st March, 20X1

		Particulars	Notes	Rs.(000)
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	22,50
	B	Reserves and Surplus	2	9,00
2		Non-current liabilities		
	A	Long-term borrowings	3	7,00
3		Current liabilities		
	A	Trade Payables		<u>5,00</u>
		Total		<u>43,50</u>
		Assets		
1		Non-current assets		
	A	Property, Plant and Equipment	4	32,50
	B	Non-current investments	5	6,00
2		Current assets		
	a	Inventories		2,00
	b	Trade receivables		2,00
	c	Cash and Cash equivalents		<u>1,00</u>
		Total		<u>43,50</u>

Notes to accounts

1	Share Capital	Rs.in ('000)
	Equity share capital	
	1,50,000 Equity Shares of Rs.10 each	15,00
	7,500 14% Preference Shares of Rs.100 each	<u>7,50</u>
		<u>22,50</u>
2	Reserves and Surplus	
	General reserve	<u>9,00</u>
3	Long-term borrowings	
	Secured	
	15% Debentures	<u>7,00</u>
4	Property, plant and Equipment	
	Land and Building	<u>32,50</u>
5	Non-current investments	
	Investments at cost	<u>6,00</u>

B Ltd agreed to take over the assets and liabilities on the following terms and conditions:

- (a) Discharge 15% debentures at a premium of 10% by issuing 15% debentures of X Ltd.
- (b) PPE at 10% above the book value and investments at par value.
- (c) Current assets at a discount of 10% and Current liabilities at book value.
- (d) Preference shareholders are discharged at a premium of 10% by issuing 15% preference shares of Rs.100 each.
- (e) Issue 3 equity shares of Rs.10 each for every 2 equity shares in B Ltd. and pay the balance in cash.

Calculate Purchase consideration.

Solution:

Calculation of Purchase Consideration (Net Asset value Method)

Particulars	(Rs.in '000's)
Value of assets taken over:	
Property, Plant and Equipment	35,75
Non-Current Investments	6,00
Current Assets	<u>4,50</u>
Total Assets (A)	<u>46,25</u>
Less: Liabilities taken over:	
15% Debentures	7,70
Current Liabilities	<u>5,00</u>
Total Liabilities (B)	<u>12,70</u>
Purchase consideration (A -B)	<u>33,55</u>
Mode of Purchase Consideration	
In the form of 15% Preference shares	8,25
In the form of Equity shares	22,50
In the form of Cash (Balance)	<u>2,80</u>
Total	33,55

Illustration 3

Let us consider the Balance Sheet of X Ltd. as at 31st March, 20X1:

	Particulars	Notes	Rs.(000)
1	Equity and Liabilities		
	Shareholders' funds		
A	Share capital	1	100,00
B	Reserves and Surplus	2	12,50
2	Non-current liabilities		
A	Long-term borrowings	3	40,00

3		Current liabilities		
	A	Trade Payables		<u>20,00</u>
		Total		<u>172,50</u>
1		Assets		
		Non-current assets		
	A	Property, Plant and Equipment	4	105,50
	B	Non-current investments	5	5,00
2		Current assets		
	a	Inventories		23,00
	b	Trade receivables		24,00
	c	Cash and Cash equivalents		<u>15,00</u>
		Total		<u>172,50</u>

Notes to accounts

			Rs.in (‘000)
1	Share Capital		
	Equity share capital		
	7,50,000 Equity Shares of Rs.10 each		75,00
	25,000 14% Preference Shares of Rs.100 each		<u>25,00</u>
			<u>100,00</u>
2	Reserves and Surplus		
	General reserve		<u>12,50</u>
			<u>12,50</u>
3	Long-term borrowings		
	Secured		
	14% Debentures		<u>40,00</u>
			<u>40,00</u>
4	Property, plant and Equipment		
	Land and Building		50,00
	Plant and machinery		45,00
	Furniture		<u>10,50</u>
			<u>105,50</u>
5	Non-current investments		
	Investments at cost		<u>5,00</u>
			<u>5,00</u>

Other Information:

- (i) Y Ltd. takes over X Ltd. on 10th April, 20X1.
- (ii) Debenture holders of X Ltd. are discharged by Y Ltd. at 10% premium by issuing 15% own debentures of Y Ltd.
- (iii) 14% Preference Shareholders of X Ltd. are discharged at a premium of 20% by issuing necessary number of 15% Preference Shares of Y Ltd. (Face value Rs.100 each).
- (iv) Intrinsic value per share of X Ltd. is Rs.20 and that of Y Ltd. Rs.30. Y Ltd. will issue equity shares to satisfy the equity shareholders of X Ltd. on the basis of intrinsic value. However, the entry should be made at par value only. The nominal value of each equity share of Y Ltd. is Rs.10.

Compute the purchase consideration.

Solution:

Computation of Purchase consideration	(Rs.in '000)	Form
For Preference Shareholders of X Ltd.	3,000	30,000 15% Preference shares in Y Ltd.
For equity shareholders of X Ltd. (20/30 × 7,50,000) × Rs.10 of Rs.10 each	5,000	5,00,000 Equity shares of Y Ltd.
Total Purchase consideration	<u>8,000</u>	

Note: According to AS 14, amount paid to the debenture holders should not be included in the purchase consideration calculation. Such debentures will be taken over by Y Ltd. and then discharged by them later.

Illustration 4

Neel Ltd. and Gagan Ltd. amalgamated to form a new company on 1.04.20X1. Following is the Balance Sheet of Neel Ltd. and Gagan Ltd. as at 31.3.20X1:

		Particulars	Notes	Neel	Gagan
1		Equity and Liabilities			
		Shareholders' funds			
	A	Share capital		7,75,000	8,55,000
2		Current liabilities		<u>6,23,500</u>	<u>5,57,600</u>
		Total		<u>13,98,500</u>	<u>14,12,600</u>
		Assets			
1		Non-current assets			
	A	Property, Plant and Equipment		12,35,000	12,54,000

2	Current assets	1	<u>1,63,500</u>	<u>1,58,600</u>
	Total		<u>13,98,500</u>	<u>14,12,600</u>

Notes to accounts:

1	Property, plant and Equipment			
	Land and Building		7,50,000	6,40,000
	Plant and machinery		<u>4,85,000</u>	<u>6,14,000</u>
			<u>12,35,000</u>	<u>12,54,000</u>

Following is the additional information:

(i) The assets of Neel Ltd. and Gagan Ltd. are to be revalued as under:

	Neel	Gagan
	Rs.	Rs.
Plant and machinery	5,25,000	6,75,000
Building	7,75,000	6,48,000

(ii) The purchase consideration is to be discharged as under:

(a) Issue 24,000 equity shares of Rs.25 each fully paid up in the proportion of their profitability in the preceding 2 years.

(b) Profits for the preceding 2 years are given below:

	Neel	Gagan
	Rs.	Rs.
1 st year	2,62,800	2,75,125
2 nd year	<u>2,12,200</u>	<u>2,49,875</u>
Total	<u>4,75,000</u>	<u>5,25,000</u>

(c) Issue 12% preference shares of Rs.10 each fully paid up at par to provide income equivalent to 8% return on net assets in the business as on 31.3.20X1 after revaluation of assets of Neel Ltd. and Gagan Ltd. respectively.

You are required to compute the

(i) Equity and preference shares issued to Neel Ltd. and Gagan Ltd.,

(ii) Purchase consideration.

Solution:

Calculation of equity shares to be issued to Neel Ltd. and Gagan Ltd.

Profits of	Neel	Gagan
	Rs.	Rs.
I year	2,62,800	2,75,125
II year	<u>2,12,200</u>	<u>2,49,875</u>
Total	<u>4,75,000</u>	<u>5,25,000</u>

The total profits- Rs.4,75,000+ Rs.5,25,000= Rs.10,00,000

No. of shares to be issued = 24,000 equity shares in the proportion of the preceding 2 years' profits.

	Neel	Gagan
24,000 x 475/1000	11,400 equity shares	
24,000 x 525/1000		12,600 equity shares

Calculation of 12% Preference shares to be issued to Neel Ltd. and Gagan Ltd.

	Neel	Gagan
	Rs.	Rs.
Net assets (Refer working note)	8,40,000	9,24,000
8% return on Net assets	67,200	73,920
12% Preference shares to be issued		
$\left[67,200 \times \frac{100}{12} \right]$ 5,60,000 @ Rs.10 each	56,000 shares	
$\left[73,920 \times \frac{100}{12} \right]$ 6,16,000 @ Rs.10 each		61,600 shares

Total Purchase Consideration

	Neel	Gagan
	Rs.	Rs.
Equity shares @ of Rs.25 each	2,85,000	3,15,000
12% Preference shares @ of Rs.10 each	<u>5,60,000</u>	<u>6,16,000</u>
Total	<u>8,45,000</u>	<u>9,31,000</u>

Working Note:

Calculation of Net assets as on 31.3.20X1

	Neel	Gagan
	Rs.	Rs.
Plant and machinery	5,25,000	6,75,000
Building	7,75,000	6,48,000
Current assets	1,63,500	1,58,600
Less: Current liabilities	<u>(6,23,500)</u>	<u>(5,57,600)</u>
	<u>8,40,000</u>	<u>9,24,000</u>

Note: Since the income from the preference shares shall be equal to the 8% return on assets, the shares are computed in such way that 12% dividend on them shall be equal to 8% of the return on Net assets.

Illustration 5

Wye Ltd. acquires the business of Zed Ltd. whose balance sheet as at 31st March, 20X1 is as under:

		Particulars	Notes	Rs.
		Equity and Liabilities		
		Shareholders' funds		
1	A	Share capital	1	12,00,000
	B	Reserves and Surplus	2	1,58,000
2		Non-current liabilities		
	A	Long-term borrowings	3	2,00,000
3		Current liabilities		
	A	Trade Payables		1,20,000
	B	Other current liabilities		<u>12,000</u>
		(Interest payable on debentures)		
		Total		<u>16,90,000</u>
		Assets		
1		Non-current assets		
	A	Property, Plant and Equipment	4	10,00,000
	B	Intangible assets	5	2,90,000
2		Current assets		
	A	Inventories		1,50,000
	B	Trade receivables		1,80,000
	C	Cash and Cash equivalents		<u>70,000</u>
		Total		<u>16,90,000</u>

Notes to accounts:

		Rs.
1	Share Capital	
	Equity Share capital (Rs.100 each)	8,00,000
	6% Preference Share capital (Rs.100 each)	<u>4,00,000</u>
		<u>12,00,000</u>
2	Reserves and Surplus	
	Capital reserve	1,00,000
	Profit and loss A/c	50,000
	Workmen compensation reserve (Expected liability Rs.5,000)	<u>8,000</u>
		<u>1,58,000</u>
3	Long-term borrowings	
	6% Debentures	<u>2,00,000</u>

		<u>2,00,000</u>
4	Property, Plant and Equipment	
	Land and Building	<u>4,00,000</u>
	Plant and machinery	<u>6,00,000</u>
		<u>10,00,000</u>
5	Intangible assets	
	Goodwill	<u>2,40,000</u>
	Patents	<u>50,000</u>
		<u>2,90,000</u>

Wye Ltd. was to take over all assets (except cash) and liabilities (except for interest due on debentures) and to pay following amounts:

- (i) Rs.2,00,000 7% Debentures (Rs.100 each) in Wye Ltd. for the existing debentures in Zed Ltd.; for the purpose, each debenture of Wye Ltd. is to be treated as worth Rs.105.
- (ii) For each preference share in Zed Ltd. Rs.10 in cash and one 9% preference share of Rs.100 each in Wye Ltd.
- (iii) For each equity share in Zed Ltd. Rs.20 in cash and one equity share in Wye Ltd. of Rs.100 each having the market value of Rs.140.
- (iv) Expense of liquidation of Zed Ltd. are to be reimbursed by Wye Ltd. to the extent of Rs.10,000. Actual expenses amounted to Rs.12,500.

Wye Ltd. valued Land and building at Rs.5,50,000 Plant and Machinery at Rs.6,50,000 and patents at Rs.20,000 of Zed Ltd for the purpose of amalgamation.

Solution:

Purchase Consideration

		Rs.	Form
(i) Preference Shares: Rs.10 per share	40,000		Cash
Preference shares	<u>4,00,000</u>	4,40,000	Preference shares
(ii) Equity shares: Rs.20 per share	1,60,000		Cash
8,000 equity shares in			
Wye Ltd. @ Rs.140	<u>11,20,000</u>	<u>12,80,000</u>	Equity shares
	<u>17,20,000</u>		

Steps to close the Books of the Vendor Company

1. Open Realization Account and transfer all assets at book value.

Exception: If cash is not taken over by the purchasing company, it should not be transferred.

Note: Profit and Loss Account (Dr.) and expenses not written off are not assets and should not be transferred to the Realization Account.

The journal entry in the above case is:

Rs. Rs.

Realization A/c Dr.	16,20,000	
To Sundries —		
Goodwill		2,40,000
Land & Building		4,00,000
Plant & Machinery	6,00,000	
Patents	50,000	
Inventory	1,50,000	
Trade receivables	1,80,000	

(Transfer of assets to Realization Account on sale of business to Wye Ltd.)

2. Transfer to the Realization Account the liabilities which the purchasing company is to take over. In case of the provisions, the portion which represents liability expected to arise in future should be so transferred and the portion which is not required (i.e., the reserve portion) should be treated as profit. Accordingly, the following entry will be recorded:

		Rs.	Rs.
6% Debentures in Wye Ltd.	Dr.	2,00,000	
Workmen's Compensation Reserve	Dr.	5,000	
Trade payables	Dr.	1,20,000	
To Realization A/c			3,25,000

(Transfer of liabilities taken over by Wye Ltd. to Realization A/c)

For liabilities not take over by the purchasing company, the profit or loss on discharge of such liabilities shall be transferred to Realization Account.

3. Debit purchasing company and credit Realization Account with the purchase consideration.

Wye Ltd.-	Dr.	17,20,000	
To Realization A/c			17,20,000

(Amount receivable from Wye Ltd. for sale of business)

4. On receipt of the purchase consideration debit what is received (cash, debentures, shares etc.) and credit the purchasing company. Thus —

Cash	Dr.	2,00,000	
9% Preference shares in Wye Ltd.	Dr.	4,00,000	
Equity shares in Wye Ltd.	Dr.	11,20,000	
To Wye Ltd.			17,20,000

(Receipt of purchase consideration from the purchase company)

5. Expenses of liquidation have to be dealt with according to the circumstances of each case.

(a) If the vendor company has to bear and pay them:

Realization Account should be debited and Cash Account credited.

(b) If the expenses are to be borne by the purchasing company, the question may be dealt within one of the two ways mentioned below:

- (i) It may be ignored in the books of the vendor company.
- (ii) If the expenses are to be paid first by the vendor company and afterwards reimbursed by the purchasing company, the following two entries will be passed:
 - (a) Debit Purchasing company and credit Cash Account when expenses are paid by the vendor company; and
 - (b) Debit Cash Account and credit purchasing company (on the expenses being reimbursed).

In the above mentioned case Wye Ltd. has to pay maximum of Rs.10,000 only whereas, the amount spent is Rs.12,500. Hence Rs.2,500 is to be borne by Zed Ltd.; the entries required will be :

		Rs.	Rs.
Wye Ltd.	Dr.	10,000	
Realization A/c	Dr.	2,500	
To Cash A/c			12,500
(Liquidation expenses out of which Rs.10,000 is payable by Wye Ltd.)			
Cash A/c	Dr.	10,000	
To Wye Ltd.		10,000	
(Account reimbursed by Wye Ltd. for expense)			

6. Liabilities not assumed by the purchasing company, have to be paid off. On payment, debit the liability concerned and credit cash. Any difference between the amount actually paid and the book figure must be transferred to the Realization Account. Zed Ltd. shall pass the following entries in this respect:

		Rs.	Rs.
Interest Outstanding	Dr.	12,000	
To Debenture holders A/c			12,000
(Amount due to debenture holders for debentures interest)			
Debenture holders	Dr.	12,000	
To Cash A/c			12,000
(Debenture holders paid cash Rs.12,000 for outstanding interest)			

7. Credit the preference shareholders with the amount payable to them, debiting Preference Share Capital with the amount shown in the books, transferring the difference between the two, if any, to the Realization Account. Thus —

6% Pref. Share Capital A/c	Dr.	4,00,000
Realization A/c	Dr.	40,000

To Preference Shareholders A/c 4,40,000

(The amount due to preference shareholders for capital and the extra amount payable under the scheme of absorption)

Note: In the absence of any indication to the contrary, preference shareholders will be entitled only to the capital contributed by them. But if funds available after paying off creditors are not sufficient to satisfy the claim of preference shareholders fully, they will have to suffer a loss to the extent of the deficit.

8. Pay off preference shareholders by debiting them and crediting whatever is given to them. The entry in the above case is :

		Rs.	Rs.
Preference shareholders A/c	Dr.	4,40,000	
To Cash A/c			40,000
To 9% Preference shares in Wye Ltd.			4,00,000

(Cash and preference shares in Wye Ltd. given to preference shareholders)

9. Transfer equity share capital and account representing profit or loss (including the balance in Realization Account) to Equity Shareholders Account. This will determine the amount receivable by the equity shareholders. Zed Ltd. shall pass the following entries in this regard :

		Rs.	Rs.
Equity Share Capital A/c	Dr.	8,00,000	
Capital Reserve A/c	Dr.	1,00,000	
Profit and Loss A/c	Dr.	50,000	
Workmen's Compensation Reserve A/c	Dr.	3,000	
Realization A/c	Dr.	3,82,500	
To Equity Shareholders A/c			13,35,500

(Various accounts representing capital and profit transferred to Equity Shareholders Account)

10. On satisfaction of the claims of the equity shareholders, debit their account and credit whatever is given to them. Hence:

Equity Shareholders A/c	Dr.	13,35,500	
To Equity Shares in Wye Ltd.			11,20,000
To Cash A/c (W.N.2)			2,15,500

Working Notes

1. Realization Account

		Rs.		Rs.
To	Sundry Assets	16,20,000	By Sundry Liabilities	3,25,000
To	Cash (excess expenses of liquidation)	2,500	By Wye Ltd.	17,20,000
To	Preference Shareholders	40,000		

To	Equity Shareholders A/c - profit transferred	<u>3,82,500</u>		
		<u>20,45,000</u>		<u>20,45,000</u>

2. Cash Account

	Rs.			Rs.
To Balance b/d	70,000	By	Realization	2,500
To Wye Ltd.	2,00,000	By	Wye Ltd.	10,000
(consideration for amalgamation)				
To Wye Ltd.	10,000	By	Debenture-holders	12000
(liquidation expenses reimbursed)		By	Preference shareholder	40000
		By	Equity Shareholder (B/F)	<u>215500</u>
	<u>280000</u>			<u>280000</u>

Illustration 6

The following Balance Sheets are given as at 31st March, 20X1:

		Particulars	Rs. Best Ltd. (in lakhs)	Rs. Better Ltd. (in lakhs)
1		Equity and Liabilities		
	A	Shareholders' funds		
	B	Share capital	20	10
		(shares of Rs.100 each, fully paid)		
		Reserves and Surplus	10	8
2		Current liabilities	20	2
		Total	50	20
		Assets		
1		Non-current assets		
	A	Property, Plant and Equipment	25	15
	B	Non-current investments	5	-
2		Current assets	20	5
		Total	50	20

The following further information is given:

- Better Limited issued bonus shares on 1st April, 20X1, in the ratio of one share for every two held, out of Reserves and Surplus.
- It was agreed that Best Ltd. will take over the business of Better Ltd., on the basis of the latter's Balance Sheet, the consideration taking the form of allotment of shares in Best Ltd.
- The value of shares in Best Ltd. was considered to be Rs.150 and the shares in Better Ltd. were valued at Rs.100 after the issue of the bonus shares. The allotment of shares is to be made on

the basis of these values.

- (d) Liabilities of Better Ltd., included Rs.1 lakh due to Best Ltd., for purchases from it, on which Best Ltd., made profit of 25% of the cost. The goods of Rs.50,000 out of the said purchases, remained in stock on the date of the above Balance Sheet.

Make the closing ledger in the Books of Better Ltd. and the opening journal entries in the Books of Best Ltd., and prepare the Balance Sheet as at 1st April, 20X1 after the takeover.

Solution:

LEDGER OF BETTER LIMITED

Property, Plant and Equipment (PPE) Account

	Rs.		Rs.
To Balance b/d	<u>15,00,000</u>	By Realization A/c (transfer)	<u>15,00,000</u>

Current Assets Account

	Rs.		Rs.
To Balance b/d	<u>5,00,000</u>	By Realization A/c (transfer)	<u>5,00,000</u>

Liabilities Account

	Rs.		Rs.
To Realization A/c	<u>2,00,000</u>	By Balance b/d	<u>2,00,000</u>

Realization Account

	Rs.		Rs.
To PPE A/c	15,00,000	By Liabilities A/c	2,00,000
" Current Assets A/c	5,00,000 "	Best Limited	15,00,000
		(Purchase Consideration)	
		" Shareholders' A/c	3,00,000
		(Loss on Realization)	
	20,00,000		20,00,000

Share Capital Account

	Rs.		Rs.
To Sundry shareholders		By Balance b/d	10,00,000
A/c - (transfer)	15,00,000	" Reserves & Surplus A/c	
		(Bonus issue)	5,00,000
	15,00,000		15,00,000

Reserves & Surplus Account

	Rs.		Rs.
To Share Capital (Bonus issue)	5,00,000	By Balance b/d	8,00,000
" Sundry Shareholders	<u>3,00,000</u>		
	<u>8,00,000</u>		<u>8,00,000</u>

Best Ltd.

	Rs.			Rs.
To Realization A/c – Purchase Consideration	<u>15,00,000</u>	By	Shares in Best Ltd	15,00,000
	<u>15,00,000</u>			<u>15,00,000</u>

Shares in Best Ltd.

	Rs.		Rs.
To Best Ltd.	15,00,000	By Sundry Shareholders A/c	15,00,000

Sundry Shareholders Account

	Rs.		Rs.
To Realization A/c	3,00,000	By Share Capital A/c	15,00,000
(Loss)		" Reserves & Surplus A/c	3,00,000
" Share in Best Ltd.	<u>15,00,000</u>		
	<u>18,00,000</u>		<u>18,00,000</u>

Journal of Best Ltd.

	Dr.	Cr.
20X1	Rs.	Rs.
Apr. 1 Property, Plant and Equipment A/c Dr.	15,00,000	
Current Assets A/c Dr. 5,00,000		
To Liabilities A/c		2,00,000
To Liquidator of Better Ltd.		15,00,000
To Capital Reserve A/c		3,00,000
<u>(Assets & Liabilities of Better Ltd. taken over for an agreed purchase consideration of Rs.15,00,000 as per agreement dated)</u>		
Liquidator of Better Ltd.	Dr. 15,00,000	
To Share Capital A/c		10,00,000
To Securities Premium A/c		5,00,000
<u>(Discharge of Purchase consideration by the issue of equity shares of Rs.10,00,000 at a premium of Rs.50 per share as per agreement)</u>		
Trade payables A/c	Dr. 1,00,000	
To Trade receivables A/c		1,00,000
<u>(Amount due from Better Ltd., and included in its creditors taken over, cancelled against own Trade receivables)</u>		
Capital Reserve A/c	Dr. 10,000	

To Current Asset (Stock) A/c			10,000
(Unrealized profit on stock included in current assets of Better Ltd. written off to Reserve Account. 20% on sale value of Rs.50,000 shall be eliminated as unrealized profit)			

Working Note :

Calculation of Purchase consideration:

Issued Capital of Better Ltd. (after bonus issue) at Rs.100 per share Rs.15,00,000

Purchase consideration has been discharged by Best Ltd. by the issue of shares for Rs.10,00,000 at a premium of Rs.5,00,000. This gives the value of Rs.150 per share.

Balance Sheet of Best Ltd. (After absorption)

		Particulars	Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	a	Share capital	1	30,00,000
	b	Reserves and Surplus	2	17,90,000
2		Current liabilities		21,00,000
		Total		68,90,000
1		Assets		
		Non-current assets		
	a	Property, Plant and Equipment	3	40,00,000
	b	Non-current investments		5,00,000
2		Current assets		23,90,000
		Total		68,90,000

Notes to accounts

		Rs.
1	Share Capital	
	Equity share capital	
	Issued & Subscribed	
	30,000 shares of Rs.100 (of the above 10,000 shares have been issued for consideration other than cash)	30,00,000
	Total	30,00,000
2	Reserves and Surplus	
	Capital Reserve (3,00,000 – 10,000)	2,90,000
	Securities Premium	5,00,000
	Other reserves and surplus	10,00,000
	Total	17,90,000

3	Property, Plant and Equipment		
	PPE	25,00,000	
	Acquired during the year	15,00,000	40,00,000
	Total		40,00,000

Illustration 7

K Ltd. and L Ltd. amalgamate to form a new company LK Ltd. The financial position of these two companies as at the date of amalgamation was as under:

		Particulars	Notes	Rs.K Ltd.	Rs.L Ltd.
1		Equity and Liabilities			
		Shareholders' funds			
	A	Share capital	1	12,00,000	6,00,000
	B	Reserves and Surplus	2	3,71,375	1,97,175
2		Non-current liabilities			
	A	Long-term borrowings	3	2,00,000	2,00,000
3		Current liabilities			
	A	Trade Payables		<u>1,00,000</u>	<u>2,10,000</u>
		Total		<u>18,71,375</u>	<u>12,07,175</u>
		Assets			
1		Non-current assets			
	A	Property, Plant and Equipment	4	11,30,000	8,20,000
	B	Intangible assets	5	80,000	-
2		Current assets			
	A	Inventories		2,25,000	1,40,000
	B	Trade receivables		2,75,000	1,75,000
	C	Cash and Cash equivalents	6	<u>1,61,375</u>	<u>72,175</u>
		Total		<u>18,71,375</u>	<u>12,07,175</u>

Notes to accounts

1	Share Capital		K Ltd.	L Ltd.
	Equity shares of Rs.100 each		8,00,000	3,00,000
	7% Preference Shares of Rs.100 each		<u>4,00,000</u>	<u>3,00,000</u>
			<u>12,00,000</u>	<u>6,00,000</u>
2	Reserves and Surplus			
	General reserve		-	1,00,000
	Profit and loss account		<u>3,71,375</u>	<u>97,175</u>
			<u>3,71,375</u>	<u>1,97,175</u>

3	Long-term borrowings			
	5% Debentures		2,00,000	-
	Secured loan		-	<u>2,00,000</u>
			<u>2,00,000</u>	<u>2,00,000</u>
4	Property, plant and Equipment			
	Land and Building		4,50,000	3,00,000
	Plant and machinery		6,20,000	5,00,000
	Furniture and fittings		<u>60,000</u>	<u>20,000</u>
			<u>11,30,000</u>	<u>8,20,000</u>
5	Intangible assets			
	Goodwill		<u>80,000</u>	-
			<u>80,000</u>	-
6	Cash and Cash Equivalents			
	Cash at Bank		1,20,000	55,000
	Cash in hand		<u>41,375</u>	<u>17,175</u>
			<u>1,61,375</u>	<u>72,175</u>

The terms of amalgamation are as under:

(A) (1) The assumption of liabilities of both the Companies.

(2) Issue of 5 Preference shares of Rs.20 each in LK Ltd. @ Rs.18 paid up at premium of Rs.4 per share for each preference share held in both the Companies.

(3) Issue of 6 Equity shares of Rs.20 each in LK Ltd. @ Rs.18 paid up at a premium of Rs.4 per share for each equity share held in both the Companies. In addition, necessary cash should be paid to the Equity Shareholders of both the Companies as is required to adjust the rights of shareholders of both the Companies in accordance with the intrinsic value of the shares of both the Companies.

(4) Issue of such amount of fully paid 6% debentures in LK Ltd. as is sufficient to discharge the 5% debentures in K Ltd. at a discount of 5% after takeover.

(B) (1) The assets and liabilities are to be taken at book values inventory and trade receivables for which provisions at 2% and 2 ½ % respectively to be raised.

(2) The trade receivables of K Ltd. include Rs.20,000 due from L Ltd.

(C) The LK Ltd. is to issue 15,000 new equity shares of Rs.20 each, Rs.18 paid up at premium of Rs.4 per share so as to have sufficient working capital. Prepare ledger accounts in the books of K Ltd. and L Ltd. to close their books.

Solution:

Books of K Ltd.
Realization Account

	Rs.			Rs.
To Goodwill	80,000	By	5% Debentures	2,00,000
To Land & Building	4,50,000	By	Trade payables	1,00,000
To Plant & Machinery	6,20,000	By	LK Ltd.	15,60,000
To Furniture & Fitting	60,000		(Purchase consideration)	
To Trade receivables	2,75,000	By	Equity shareholders A/c	51,375
To Stores & inventory	2,25,000		(loss)	
To Cash at Bank	1,20,000			
To Cash in hand	41,375			
To Preference shareholders (excess payment)	<u>40,000</u>			
	<u>19,11,375</u>			<u>19,11,375</u>

Equity Shareholders Account

	Rs.		Rs.
To Realization A/c (loss)	51,375	By Share capital	8,00,000
To Equity Shares in LK Ltd.	10,56,000	By Profit & Loss A/c	3,71,375
To Cash	<u>64,000</u>		
	<u>11,71,375</u>		<u>11,71,375</u>

7% Preference Shareholders Account

	Rs.		Rs.
To Preference Shares in LK Ltd.	4,40,000	By Share capital	4,00,000
		By Realization A/c	<u>40,000</u>
	<u>4,40,000</u>		<u>4,40,000</u>

LK Ltd. Account

	Rs.		Rs.
To Realization A/c	15,60,000	By Equity Shares in LK Ltd.	
		For Equity	10,56,000
		Pref.	<u>4,40,000</u>
		By Cash	<u>64,000</u>
	<u>15,60,000</u>		<u>15,60,000</u>

Books of L Ltd.
Realization Account

		Rs.			Rs.
To	Land & Building	3,00,000	By	Trade payables	2,10,000
To	Plant & Machinery	5,00,000	By	Secured loan	2,00,000
To	Furniture & Fittings	20,000	By	LK Ltd. (Purchase	
To	Trade receivables	1,75,000		consideration)	7,90,000
To	Inventory of stores	1,40,000	By	Equity shareholders A/c	37,175
				Loss	
To	Cash at bank	55,000			
To	Cash in hand	17,175			
To	Pref. shareholders	<u>30,000</u>			
		<u>12,37,175</u>			<u>12,37,175</u>

Equity Shareholders Account

	Rs.		Rs.
To Equity shares in LK Ltd.	3,96,000	By Share Capital	3,00,000
To Realization	37,175	By Profit & Loss A/c	97,175
To Cash	<u>64,000</u>	By Reserve	<u>1,00,000</u>
	<u>4,97,175</u>		<u>4,97,175</u>

7% Preference Shareholders Account

	Rs.		Rs.
To Preference Shares in LK Ltd.	3,30,000	By	Share capital
		By	Realization A/c
	<u>3,30,000</u>		<u>30,000</u>
			<u>3,30,000</u>

LK Ltd. Account

	Rs.		Rs.
To Realization A/c	7,90,000	By Equity shares in LK Ltd.	
		For Equity	3,96,000
		Preference	<u>3,30,000</u>
		By Cash	<u>64,000</u>
	<u>7,90,000</u>		<u>7,90,000</u>

Working Notes:

(i) Purchase consideration

	K Ltd.	L Ltd.
	Rs.	Rs.
Payable to preference shareholders:		

Preference shares at Rs.22 per share	4,40,000	3,30,000
Equity Shares at Rs.22 per share	10,56,000	3,96,000
Cash [See W.N. (ii)]	<u>64,000</u>	<u>64,000</u>
	<u>15,60,000</u>	<u>7,90,000</u>

(ii) Value of Net Assets

	K Ltd.	L Ltd.
	Rs.	Rs.
Goodwill	80,000	
Land & Building	4,50,000	3,00,000
Plant & Machinery	6,20,000	5,00,000
Furniture & Fittings	60,000	20,000
Trade receivables less 2.5%	2,68,125	1,70,625
Inventory less 2%	2,20,500	1,37,200
Cash at Bank	1,20,000	55,000
Cash in hand	<u>41,375</u>	<u>17,175</u>
	18,60,000	12,00,000

Less : Debentures	2,00,000		–	
Trade payables	1,00,000		2,10,000	
Secured Loans	–	(3,00,000)	<u>2,00,000</u>	(4,10,000)
		15,60,000		7,90,000
Payable in shares		<u>14,96,000</u>		<u>7,26,000</u>
Payable in cash		<u>64,000</u>		<u>64,000</u>

Illustration 8

Consider the following balance sheets of X Ltd. and Y Ltd. as at 31st March, 20X1:

		Particulars	Notes	Rs.X Ltd (‘000)	Rs.Y Ltd. (‘000)
		Equity and Liabilities			
1		Shareholders’ funds			
	A	Share capital	1	72,00	47,00
	B	Reserves and Surplus	2	15,50	10,50
2		Non-current liabilities			
	A	Long-term borrowings	3	5,00	3,50

3		Current liabilities			
	A	Trade Payables		4,50	3,50
	B	Other current liabilities		<u>2,00</u>	<u>1,50</u>
		Total		<u>99,00</u>	<u>66,00</u>
		Assets			
1	A	Non-current assets			
	A	Property, Plant and Equipment	4	63,25	36,00
	B	Non-current investments	5	7,00	5,00
2		Current assets			
	A	Inventories		12,50	9,50
	B	Trade receivables		9,00	10,30
	C	Cash and Cash equivalents		<u>7,25</u>	<u>5,20</u>
		Total		<u>99,00</u>	<u>66,00</u>

Notes to accounts

		X Ltd ('000)	Y Ltd ('000)
1	Share Capital		
	Equity share capital (Rs.10 each)	50,00	30,00
	14% Preference Shares capital Rs.100 each	<u>22,00</u>	<u>17,00</u>
		<u>72,00</u>	<u>47,00</u>
2	Reserves and Surplus		
	General reserve	5,00	2,50
	Export profit reserve	3,00	2,00
	Investment allowance reserve	-	1,00
	Profit and loss account	<u>7,50</u>	<u>5,00</u>
		<u>15,50</u>	<u>10,50</u>
3	Long-term borrowings		
	13% Debentures of Rs.100 each	<u>5,00</u>	<u>3,50</u>
		<u>5,00</u>	<u>3,50</u>
4	Property, Plant and Equipment		
	Land and Building	25,00	15,50
	Plant and machinery	32,50	17,00
	Furniture	<u>5,75</u>	<u>3,50</u>
		<u>63,25</u>	<u>36,00</u>
5	Non-current investments		
	Investments at cost	<u>7,00</u>	<u>5,00</u>
		<u>7,00</u>	<u>5,00</u>

X Ltd. takes over Y Ltd. on 1st April, 20X1. X Ltd. discharges the purchase consideration as below:

- (i) Issued 3,50,000 equity shares of Rs.10 each at par to the equity shareholders of Y Ltd.
- (ii) Issued 15% preference shares of Rs.100 each to discharge the preference shareholders of Y Ltd. at 10% premium.

The debentures of Y Ltd. will be converted into equivalent number of debentures of X Ltd. The statutory reserves of Y Ltd. are to be maintained for 2 more years.

Show the (i) Journal entries and (ii) Balance sheet of X Ltd. after amalgamation on the assumption that:

- (a) the amalgamation is in the nature of merger.
- (b) the amalgamation is in the nature of purchase.

Solution:

Amalgamation in the nature of merger:

Journal Entries in the Books of X Ltd.

		Rs.'000	Rs.' 000
Business Purchase	Dr.	53,70	
To Liquidator of Y Ltd.			53,70
(Consideration payable for business taken over from Y Ltd)			
Sundry Assets of Y Ltd	Dr.	66,00	
General Reserve (Related to X Ltd)		4,20	
To Sundry Liabilities of Y Ltd			8,50
To Export profit Reserve			2,00
To Investment allowance Reserve			1,00
To Profit & Loss			5,00
To Business Purchase			53,70
(Incorporation of various assets and liabilities taken over from Y Ltd. at book values and difference of share capital and purchase consideration being adjusted with free Reserves)			
Liquidator of Y Ltd.	Dr.	53,70	
To Equity Share Capital			35,00
To 15% Preference Share Capital			18,70
(Discharge of consideration for Y Ltd.' s business)			
Sundry Liabilities in Y Ltd (13% Debentures in Y Ltd.)	Dr.	3,50	
To 13% Debentures			3,50
(Allotment of 13% Debentures to debenture holders of Y Ltd. at Par)			

Balance Sheet of X Ltd.

		Particulars	Notes	Rs.in '000
1		Equity and Liabilities		
		Shareholders' funds		
	a	Share capital	1	12,570
	b	Reserves and Surplus	2	1,930
2		Non-current liabilities		
	a	Long-term borrowings	3	850
3		Current liabilities		
	a	Trade Payables		800
	b	Other current liabilities		350
		Total		16,500
		Assets		
1		Non-current assets		
	a	Property, Plant and Equipment	4	9,925
	b	Non-current investments		1,200
2		Current assets		
	a	Inventories		2,200
	b	Trade receivables		1,930
	c	Cash and cash equivalents		1,245
		Total		16,500

Notes to accounts

		Rs.in ' 000
1 Share Capital		
Equity share capital		
8,50,000 Equity Shares of Rs.10 each		8,500
Preference share capital		
18,700, 15% Preference Shares of Rs.100 each		1,870
22,000, 14% Preference Shares of Rs.100 each		2,200
Total		12,570
2 Reserves and Surplus		
General Reserve of X Ltd. 500		
Add: General reserve of Y Ltd. <u>250</u>	750	
Less: Adjustment for amalgamation*	(670)	80
Export Profit Reserve of X Ltd.	300	
Add: Export Profit Reserve of Y Ltd.	<u>200</u>	500
Investment Allowance Reserve		100

Profit & Loss A/c of X Ltd.	750	
Add: Profit & Loss A/c of Y Ltd.	<u>500</u>	1,250
Total		1,930
3 Long-term borrowings		
Secured		
8,500 13% Debentures of Rs.100 each		850
Total		850
4 Property, Plant and Equipment		
Land & Buildings		4,050
Plant & Machinery		4,950
Furniture & Fittings		925
Total		9,925

*The difference between the amount recorded as share capital issued and the amount of share capital of transferor-company should be adjusted in reserves.

Thus, Adjustment for amalgamation = Rs.'000 (53,70 – 47,00) = Rs.('000) 670

Amalgamation in the nature of purchase:

Journal Entries in the Books of X Ltd.

		Dr. Rs.	Cr. Rs.
Business Purchase To Liquidator of Y Ltd. (Consideration payable for business taken over from Y Ltd)	Dr.	53,70,000	53,70,000
Sundry Assets of Y Ltd To Sundry Liabilities of Y Ltd To Capital Reserve To Business Purchase (Incorporation of various assets and liabilities taken over from Y Ltd. at book values and difference of Net assets and purchase consideration being credited to Capital reserve)	Dr.	66,00,000	8,50,000 3,80,000 53,70,000
Liquidator of Y Ltd. To Equity Share Capital To 15% Preference Share Capital (Discharge of consideration for Y Ltd.' s business)	Dr.	53,70,000	35,00,000 18,70,000
13% Debentures in Y Ltd. To 13% Debentures (Allotment of 13% Debentures to debenture holders of Y Ltd. at Par)	Dr.	3,50,000	3,50,000

Balance Sheet of X Ltd.

		Particulars	Notes	Rs.in'000
1		Equity and Liabilities		
		Shareholders' funds		
	a	Share capital	1	12,570
	b	Reserves and Surplus	2	1,930
2		Non-current liabilities		
	a	Long-term borrowings	3	850
3		Current liabilities		
	a	Trade Payables		800
	b	Other current liabilities		350
		Total		16,500
1		Assets		
		Non-current assets		
	a	Property, Plant and Equipment	4	9,925
	b	Non-current investments		1,200
2		Current assets		
	a	Inventories		2,200
	b	Trade receivables		1,930
	c	Cash and cash equivalents		1,245
		Total		16,500

Notes to accounts

		Rs.in'000
1	Share Capital	
	Equity share capital	
	8,50,000 Equity Shares of Rs.10 each	8,500
	Preference share capital	
	18,700, 15% Preference Shares of Rs.100 each	1,870
	22,000, 14% Preference Shares of Rs.100 each	2,200
	Total	12,570
2	Reserves and Surplus	
	Capital Reserve	380
	General Reserve	500
	Amalgamation adjustment reserve	(300)
	Export Profit Reserve	500
	Investment Allowance Reserve	100

	Surplus (Profit & Loss A/c)		750
	Total		1,930
3	Long-term borrowings		
	Secured		
	8,500 13% Debentures of Rs.100 each		850
	Total		850
4	Property, Plant and Equipment		
	Land & Buildings		4,050
	Plant & Machinery		4,950
	Furniture & Fittings		925
	Total		9,925

Workings Notes:

Capital Reserve arising on Amalgamation:

(A) Net Assets taken over:	Rs.('000)	Rs.('000)
Sundry Assets		66,00
Less: 13% Debentures	3,50	
Trade payables	3,50	
Other current liabilities	<u>1,50</u>	<u>(8,50)</u>
		<u>57,50</u>
(B) Purchase consideration:		
To Equity Shareholders of Y Ltd.		35,00
To Preference Shareholders of Y Ltd.		<u>18,70</u>
		<u>53,70</u>
(C) Capital Reserve (A – B)		<u>3,80</u>

Illustration 9

The following are the Balance Sheets of P Ltd. and Q Ltd. as at 31st March, 20X1:

		Particulars	Notes	Rs.P Ltd	Rs.Q Ltd
1		Equity and Liabilities			
		Shareholders' funds			
	A	Share capital	1	8,00,000	4,00,000
	B	Reserves and Surplus		3,00,000	2,00,000
2		Non-current liabilities			
	A	Long-term borrowings	2	2,00,000	1,50,000
3		Current liabilities			
	A	Trade Payables		<u>2,50,000</u>	<u>1,50,000</u>

1	A	Total Assets		<u>15,50,000</u>	<u>9,00,000</u>
		Non-current assets			
		Property, Plant and Equipment		7,00,000	2,50,000
2	B	Non-current investments		80,000	80,000
	A	Current assets			
		Inventories		2,40,000	3,20,000
		Trade receivables		4,20,000	2,10,000
		Cash and Cash equivalents		<u>1,10,000</u>	<u>40,000</u>
		Total		<u>15,50,000</u>	<u>9,00,000</u>

Notes to accounts

			P Ltd.	Q Ltd.
1	Share Capital			
	Equity shares of Rs.10 each		6,00,000	3,00,000
	10% Preference Shares of Rs.100 each		<u>2,00,000</u>	<u>1,00,000</u>
			<u>8,00,000</u>	<u>4,00,000</u>
2	Long term borrowings			
	12% Debentures		<u>2,00,000</u>	<u>1,50,000</u>
			<u>2,00,000</u>	<u>1,50,000</u>

Details of Trade receivables and trade payables are as under:

	P Ltd. (Rs.)	Q Ltd. (Rs.)
Trade receivables		
Debtors	3,60,000	1,90,000
Bills Receivable	<u>60,000</u>	<u>20,000</u>
	<u>4,20,000</u>	<u>2,10,000</u>
Trade payables		
Sundry Creditors	2,20,000	1,25,000
Bills Payable	<u>30,000</u>	<u>25,000</u>
	<u>2,50,000</u>	<u>1,50,000</u>

Property, plant and equipment of both the companies are to be revalued at 15% above book value. Both the companies are to pay 10% Equity dividend, but Preference dividend having been already paid.

After the above transactions are given effect to, P Ltd. will absorb Q Ltd. on the following terms:

- 8 Equity Shares of Rs.10 each will be issued by P Ltd. at par against 6 shares of Q Ltd.
- 10% Preference Shareholders of Q Ltd. will be paid at 10% discount by issue of 10% Preference Shares of Rs.100 each at par in P Ltd.
- 12% Debenture holders of Q Ltd. are to be paid at 8% premium by 12% Debentures in P Ltd.

issued at a discount of 10%.

(iv) Rs.30,000 is to be paid by P Ltd. to Q Ltd. for Liquidation expenses. Sundry Creditors of Q Ltd. include Rs.10,000 due to P Ltd.

(v) Inventory in Trade and Debtors are taken over at 5% lesser than their book value by P Ltd.

Prepare:

(a) Journal entries in the books of P Ltd.

(b) Statement of consideration payable by P Ltd.

Solution:

(a) Journal Entries in the Books of P Ltd.

		Dr. Rs.	Cr. Rs.
Property, Plant and Equipment To Revaluation Reserve (Revaluation of PPE at 15% above book value)	Dr.	1,05,000	1,05,000
Reserve and Surplus To Equity Dividend (Declaration of equity dividend @ 10%)	Dr.	60,000	60,000
Equity Dividend To Bank Account (Payment of equity dividend)	Dr.	60,000	60,000
Business Purchase Account To Liquidator of Q Ltd. (Consideration payable for the business taken over from Q Ltd.)	Dr.	4,90,000	4,90,000
Property, Plant and Equipment (115% of Rs.2,50,000)	Dr.	2,87,500	
Inventory (95% of Rs.3,20,000)	Dr.	3,04,000	
Debtors	Dr.	1,90,000	
Bills Receivable	Dr.	20,000	
Investment	Dr.	80,000	
Cash at Bank	Dr.	10,000	
(Rs.40,000 –Rs.30,000 dividend paid)			
To Provision for Bad Debts (5% of Rs.1,90,000)			9,500
To Sundry Creditors			1,25,000
To 12% Debentures in Q Ltd.			1,62,000
To Bills Payable			25,000
To Business Purchase Account			4,90,000
To Capital Reserve (Balancing figure)			80,000
(Incorporation of various assets and liabilities taken over from Q Ltd.)			

at agreed values and difference of net assets and purchase consideration being credited to capital reserve)			
Liquidator of Q Ltd. To Equity Share Capital To 10% Preference Share Capital (Discharge of consideration for Q Ltd.'s business)	Dr.	4,90,000	4,00,000 90,000
12% Debentures in Q Ltd. (Rs.1,50,000 × 108%) Discount on Issue of Debentures To 12% Debentures (Allotment of 12% Debentures to debenture holders of Q Ltd. at a discount of 10%)	Dr. Dr.	1,62,000 18,000	1,80,000
Sundry Creditors of Q Ltd. To Sundry Debtors of P Ltd. (Cancellation of mutual owing)	Dr.	10,000	10,000
Goodwill To Bank (Being liquidation expenses reimbursed to Q Ltd.)	Dr.	30,000	30,000
Capital Reserve To Goodwill (Being goodwill set off)	Dr.	30,000	30,000

(b) Statement of Consideration payable by P Ltd. for 30,000 shares (payment method)

Shares to be allotted $\frac{30,000}{6} \times 8 = 40,000$ shares of P Ltd.

Issued 40,000 shares of Rs.10 each i.e. Rs.4,00,000 (i)

For 10% preference shares, to be paid at 10% discount

Rs. $\frac{1,00,000 \times 90}{100}$ Rs.90,000 (ii)

Consideration amount [(i) + (ii)] Rs.4,90,000

Illustration 10

The financial position of two companies Hari Ltd. and Vayu Ltd. as at 31st March, 20X1 was as under:

		Particulars	Notes	Hari Ltd.	Vayu Ltd.
1	A	Equity and Liabilities Shareholders' funds Share capital	1	11,00,000	4,00,000

2	B	Reserves and Surplus	2	70,000	70,000
		Non-current liabilities			
3	A	Long term provisions	3	50,000	20,000
		Current liabilities			
	A	Trade Payables		<u>1,30,000</u>	<u>80,000</u>
		Total		<u>13,50,000</u>	<u>5,70,000</u>
1		Assets			
		Non-current assets			
	A	Property, Plant and Equipment	4	8,00,000	2,50,000
	B	Intangible assets	5	50,000	25,000
2		Current assets			
	A	Inventories		2,50,000	1,75,000
	B	Trade receivables		2,00,000	1,00,000
	C	Cash and Cash equivalents		<u>50,000</u>	<u>20,000</u>
		Total		<u>13,50,000</u>	<u>5,70,000</u>

Notes to accounts

			Hari Ltd.	Vayu Ltd.
1	Share Capital			
	Equity shares of Rs.10 each		10,00,000	3,00,000
	9% Preference Shares of Rs.100 each		1,00,000	--
	10% Preference Shares of Rs.100 each		--	<u>1,00,000</u>
			<u>11,00,000</u>	<u>4,00,000</u>
2	Reserves and Surplus			
	General reserve		<u>70,000</u>	<u>70,000</u>
			<u>70,000</u>	<u>70,000</u>
3	Long term Provisions			
	Retirement gratuity fund		<u>50,000</u>	<u>20,000</u>
			<u>50,000</u>	<u>20,000</u>
4	Property, plant and Equipment			
	Land and Building		3,00,000	1,00,000
	Plant and machinery		<u>5,00,000</u>	<u>1,50,000</u>
			<u>8,00,000</u>	<u>2,50,000</u>
5	Intangible assets			
	Goodwill		<u>50,000</u>	<u>25,000</u>
			<u>50,000</u>	<u>25,000</u>

Hari Ltd. absorbs Vayu Ltd. on the following terms:

- (a) 10% Preference Shareholders are to be paid at 10% premium by issue of 9% Preference Shares of Hari Ltd.
- (b) Goodwill of Vayu Ltd. is valued at Rs.50,000, Buildings are valued at Rs.1,50,000 and the Machinery at Rs.1,60,000.
- (c) Inventory to be taken over at 10% less value and Provision for Doubtful Debts to be created @ 7.5%.
- (d) Equity Shareholders of Vayu Ltd. will be issued necessary Equity Shares @ 5% premium.

Prepare necessary Ledger Accounts to close the books of Vayu Ltd. and show the acquisition entries in the books of Hari Ltd. Also draft the Balance Sheet after absorption as at 31st March, 20X1.

Solution:

In the Books of Vayu Ltd.

Realization Account

	Rs.		Rs.
To Sundry Assets	5,70,000	By Retirement Gratuity Fund	20,000
To Preference Shareholders (Premium on Redemption)	10,000	By Trade payables	80,000
To Equity Shareholders (Profit on Realization)	<u>50,000</u>	By Hari Ltd. (Purchase Consideration)	5,30,000
	<u>6,30,000</u>		<u>6,30,000</u>

Equity Shareholders Account

	Rs.		Rs.
To Equity Shares of Hari Ltd.	4,20,000	By Share Capital	3,00,000
		By General Reserve	70,000
		By Realization Account (Profit on realization)	<u>50,000</u>
	<u>4,20,000</u>		<u>4,20,000</u>

Preference Shareholders Account

	Rs.		Rs.
To 9% Preference Shares of Hari Ltd.	1,10,000	By Preference Share Capital	1,00,000
		By Realization Account	

		(Premium on Redemption of Preference Shares)	<u>10,000</u>
	<u>1,10,000</u>		<u>1,10,000</u>

Hari Ltd. Account

	Rs.		Rs.
To Realization Account	5,30,000	By 9% Preference Shares	1,10,000
	<u>5,30,000</u>	By Equity Shares	<u>4,20,000</u>
			<u>5,30,000</u>

In the Books of Hari Ltd.

Journal Entries

		Dr.	Cr.
		Rs.	Rs.
Business Purchase A/c To Liquidators of Vayu Ltd. Account (Being business of Vayu Ltd. taken over)	Dr.	5,30,000	5,30,000
Goodwill Account	Dr.	50,000	
Building Account	Dr.	1,50,000	
Machinery Account	Dr.	1,60,000	
Inventory Account	Dr.	1,57,500	
Trade receivables Account	Dr.	1,00,000	
Bank Account	Dr.	20,000	
To Retirement Gratuity Fund Account			20,000
To Trade payables Account			80,000
To Provision for Doubtful Debts Account			7,500
To Business Purchase A/c (Being Assets and Liabilities taken over as per agreed valuation).			5,30,000
Liquidators of Vayu Ltd. A/c To 9% Preference Share Capital A/c To Equity Share Capital A/c To Securities Premium A/c (Being Purchase Consideration satisfied as above).	Dr.	5,30,000	1,10,000 4,00,000 20,000

Balance Sheet of Hari Ltd. (after absorption) as at 31st March, 20X1

Particulars	Notes	Rs.
Equity and Liabilities		
1 Shareholders' funds		
A Share capital	1	16,10,000
B Reserves and Surplus	2	90,000
2 Non-current liabilities		
A Long-term provisions	3	70,000
3 Current liabilities		
A Trade Payables		2,10,000
Total		19,80,000
Assets		
1 Non-current assets		
A Property, Plant and Equipment	4	11,10,000
B Intangible assets	5	1,00,000
2 Current assets		
A Inventories		4,07,500
B Trade receivables	6	2,92,500
C Cash and cash equivalents		<u>70,000</u>
Total		<u>19,80,000</u>

Notes to accounts

		Rs.
1 Share Capital		
Equity share capital		
1,40,000 Equity Shares of Rs.10 each fully paid (Out of above 40,000 Equity Shares were issued in consideration other than for cash)		14,00,000
Preference share capital		
2,100 9% Preference Shares of Rs.100 each (Out of above 1,100 Preference Shares were issued in consideration other than for cash)		2,10,000
Total		16,10,000
2 Reserves and Surplus		
Securities Premium		20,000
General Reserve		70,000
Total		90,000
3 Long-term provisions		
Retirement Gratuity fund		70,000

	Total		70,000
4	Property, Plant and Equipment		
	Buildings		4,50,000
	Machinery		6,60,000
	Total		11,10,000
5	Intangible assets		
	Goodwill		1,00,000
6	Trade receivables		3,00,000
	Less: Provision for Doubtful Debts		7,500
			2,92,500

Working Notes:

Purchase Consideration:	Rs.
Goodwill	50,000
Building	1,50,000
Machinery	1,60,000
Inventory	1,57,500
Trade receivables	92,500
Cash at Bank	<u>20,000</u>
	6,30,000
Less: Liabilities:	
Retirement Gratuity Fund	(20,000)
Trade payables	<u>(80,000)</u>
Net Assets/ Purchase Consideration	<u>5,30,000</u>
To be satisfied as under:	
10% Preference Shareholders of Vayu Ltd.	1,00,000
Add: 10% Premium	<u>10,000</u>
1,100 9% Preference Shares of Hari Ltd.	1,10,000
Equity Shareholders of Vayu Ltd. to be satisfied by issue of 40,000 Equity Shares of Hari Ltd. at 5% Premium	<u>4,20,000</u>
Total	<u>5,30,000</u>

Illustration 11

The following are the Balance Sheets of A Ltd. and B Ltd. as at 31.3.20X1:

	Particulars	Notes	Rs.A Ltd (in'000)	Rs.B Ltd (in'000)
	Equity and Liabilities			

1		Shareholders' funds			
	A	Share capital	1	2,000	1,000
	B	Reserves and Surplus	2	1,000	(800)
2		Non-current liabilities			
	A	Long-term borrowings	3	750	450
3		Current liabilities			
	A	Trade Payables		300	300
	B	Short term Borrowings – Bank overdraft		--	50
		Total		4,050	1,000
1		Assets			
		Non-current assets			
	A	Property, Plant and Equipment Non-		2,700	850
	B	current investments		700	--
2		Current assets			
	A	Trade receivables		400	150
	B	Cash and Cash equivalents (cash at bank)		250	--
		Total		4050	1000

Notes to accounts

1	Share capital	A Ltd. ('000)	B Ltd. ('000)
	Equity shares of Rs.100 each	2000	1000
		2000	1000
2	Reserves and Surplus		
	General reserve	1000	--
	Profit and loss A/c (debit balance)	--	(800)
		1000	(800)
3	Long term borrowings		
	10% debentures	500	--
	Loan from banks	250	450
		750	450

B Ltd. has acquired the business of A Ltd. The following scheme of merger was approved:

(i) Banks agreed to waive off the loan of Rs.60 thousands of B Ltd.

(ii) B Ltd. will reduce its shares to Rs.10 per share and then consolidate 10 such shares into one share of Rs.100 each (new share).

(iii) Shareholders of A Ltd. will be given one share (new) of B Ltd. in exchange of every share held in A Ltd.

(iv) Trade payables of B Ltd. includes Rs.100 thousands payable to A Ltd.

Pass necessary entries in the books of B Ltd. and prepare Balance Sheet after merger.

Solution:

Calculation of purchase consideration

One share of B Ltd. will be issued in exchange of every share of A Ltd. (i.e. 20,000 equity shares of B Ltd. will be issued against 20,000 equity shares of A Ltd.)	20,000 shares

Journal Entries in the books of B Ltd.

Date		(Rs.in thousands)	
		Dr.	Cr.
20X1			
	March,31		
	Loan from bank A/c Dr.	60	
	To Capital reduction A/c (Being loan from bank waived off to the extent of Rs.60 thousand)		60
	Equity share capital A/c (Rs.100) Dr.	1,000	
	To Equity share capital A/c (Rs.10)		100
	To Capital reduction A/c (Being equity shares of Rs.100 each reduced to Rs.10 each)		900
	Equity share capital A/c (Rs.10) Dr.	100	
	To Equity share capital A/c (Rs.100 each) (Being 10 equity shares of Rs.10 each consolidated to one share of Rs.100 each)		100
	Capital reduction A/c Dr.	960	
	To Profit and loss A/c		800
	To Capital reserve A/c (Being accumulated losses set off against reconstruction A/c and balance transferred to capital reserve account)		160
	Property, plant and equipment A/c Dr.	2,700	
	Investment A/c Dr.	700	
	Trade receivables A/c Dr.	400	
	Cash at bank A/c Dr.	250	
	To Trade payables A/c		300
	To Loans from bank A/c		250
	To 10% Debentures A/c		500
	To Liquidator of A Ltd. A/c		2,000
	To Reserves A/c		1,000

(Being assets, liabilities and reserves taken over under pooling of interest method and amount due to Liquidator)			
Liquidator of A Ltd. A/c	Dr.	2,000	
To Equity share capital A/c			2,000
(Being payment made to liquidators of A Ltd. by allotment of 20,000 new equity shares)			
Trade payables A/c	Dr.	100	
To Trade receivables A/c			100
(Being mutual owing cancelled)			

Balance Sheet of B Ltd. after merger as at 31.3.20X1

		Particulars	Notes	Rs.in '000
1		Equity and Liabilities		
		Shareholders' funds		
	a	Share capital	1	2,100
	b	Reserves and Surplus	2	1,160
2		Non-current liabilities		
	a	Long term borrowings	3	1,140
3		Current liabilities		
	a	Trade payables		500
	b	Short term borrowings	4	50
			Total	4,950
1		Assets		
		Non-current assets		
	a	Property, Plant and Equipment		3,550
	b	Non-current investments		700
2		Current assets		
	a	Trade receivables		450
	b	Cash and cash equivalents		250
			Total	4,950

Notes to accounts

		Rs.in '000
1	Share Capital	
	21,000, Equity shares of Rs.100 each fully paid	2,100
	(Out of the above, 20,000 shares have been issued for consideration other than cash)	

2	Reserves and Surplus		
	Capital reserve	160	
	General reserve	1,000	
	Total		1,160
3	Long Term Borrowings		
	10% Debentures	500	
	Loan from Bank (250+450-60)	640	1,140
4	Short term borrowings		
	Bank overdraft		50

Illustration 12

A Ltd. take over B Ltd. on April 01, 20X1 and discharges consideration for the business as follows:

- (i) Issued 42,000 fully paid equity shares of Rs.10 each at par to the equity shareholders of B Ltd.
- (ii) Issued fully paid up 15% preference shares of Rs.100 each to discharge the preference shareholders (Rs.1,70,000) of B Ltd. at a premium of 10%.
- (iii) It is agreed that the debentures of B Ltd. (Rs.50,000) will be converted into equal number and amount of 13% debentures of A Ltd.

Determine the amount of purchase consideration as per AS 14.

Solution:

Particulars	Rs.
Equity Shares (42,000 x 10)	4,20,000
15% Preference Share Capital	1,70,000
Add: Premium on Redemption	<u>17,000</u>
Purchase Consideration	<u>6,07,000</u>

Note: As per AS 14, 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. Thus, payment to debenture holders are not covered by the term 'consideration'.

Illustration 13

A Ltd. and B Ltd. were amalgamated on and from 1st April, 20X1. A new company C Ltd. was formed to take over the business of the existing companies. A Ltd. and B Ltd. have the following ledger balances as on 31st March, 20X1:

	A Ltd. (Rs.in lakhs)	B Ltd. (Rs.in lakhs)
Land and Building	550	400
Plant and Machinery	350	250
Investments (Non-current)	150	50
Inventory	350	250
Trade Receivables	300	350
Cash and Bank	300	200
Share Capital:		
Equity Shares of Rs.100 each	800	750
12% Preference shares of Rs.100 each	300	200
Reserves and Surplus:		
Revaluation Reserve	150	100
General Reserve	170	150
Investment Allowance Reserve	50	50
Profit and Loss Account	50	30
Secured Loans:		
10% Debentures (Rs.100 each)	60	30
Trade Payables	420	190

Additional Information:

- (1) 10% Debenture holders of A Ltd. and B Ltd. are discharged by C Ltd. issuing such number of its 15% Debentures of Rs.100 each so as to maintain the same amount of interest.
- (2) Preference shareholders of the two companies are issued equivalent number of 15% preference shares of C Ltd. at a price of Rs.150 per share (face value of Rs.100).
- (3) C Ltd. will issue 5 equity shares for each equity share of A Ltd. and 4 equity shares for each equity share of B Ltd. The shares are to be issued @ Rs.30 each, having a face value of Rs.10 per share.
- (4) Investment allowance reserve is to be maintained for 4 more years.

Prepare the Balance Sheet of C Ltd. as on 1st April, 20X1 after the amalgamation has been carried out on the basis of Amalgamation in the nature of purchase.

Solution:**Balance Sheet of C Ltd. as at 1st April, 20X1**

Particulars	Note No.	(Rs.in lakhs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1,200
(b) Reserves and Surplus	2	1,650
(2) Non-Current Liabilities		
Long-term borrowings	3	60
(3) Current Liabilities		
Trade payables	8	610
Total		3,520
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment	4	1,550
(b) Intangible assets	5	20
(c) Non-current investments	6	200
(2) Current assets		
(a) Inventory (350 + 250)		600
(b) Trade receivables	7	650
(c) Cash and bank balances (300 + 200)		500
Total		3,520

Notes to Accounts

		(Rs.in lakhs)	(Rs.in lakhs)
1.	Share Capital		
	Equity share capital (W.N.1)		
	70,00,000 ¹ Equity shares of Rs.10 each	700	
	5,00,000 ² Preferenceshares of Rs.100 each	500	
	(all the above shares are allotted as fully paid-up pursuant to contracts without payment being received in cash)		1,200
2.	Reserves and surplus		
	Securities Premium Account (W.N.3) (950 + 700)	1,650	
	Investment Allowance Reserve (50 + 50)	100	
	Amalgamation Adjustment Reserve (50 + 50)	(100)	
3.	Long-term borrowings		1,650

4.	15% Debentures		60
	Property, Plant and Equipment		
	Land and Building (550 + 400)	950	
5.	Plant and Machinery (350 + 250)	600	1,550
	Intangible assets		
	Goodwill [W.N. 2] (110 – 90)		20
6.	Non-current Investments		
	Investments (150 + 50)		200
7.	Trade receivables (300 + 350)		650
8.	Trade payables (420 + 190)		610

Working Notes:

		(Rs.in lakhs)	
		A Ltd.	B Ltd.
(1)	Computation of Purchase consideration		
	(a) Preference shareholders:		
	$\left(\frac{3,00,00,000}{100} \text{ i.e. } 3,00,0000 \text{ shares} \right) \times \text{Rs. } 150 \text{ each}$	450	
	$\left(\frac{2,00,00,000}{100} \text{ i.e. } 2,00,0000 \text{ shares} \right) \times \text{Rs. } 150 \text{ each}$		300
	(b) Equity shareholders:		
	$\left(\frac{8,00,00,000 \times 5}{100} \text{ i.e. } 40,00,0000 \text{ shares} \right) \times \text{Rs. } 30 \text{ each}$	1,200	
	$\left(\frac{7,50,00,000 \times 4}{100} \text{ i.e. } 30,00,0000 \text{ shares} \right) \times \text{Rs. } 30 \text{ each}$	—	900
	Amount of Purchase Consideration	<u>1,650</u>	<u>1,200</u>
(2)	Net Assets Taken Over		
	Assets taken over:		
	Land and Building	550	400
	Plant and Machinery	350	250
	Investments	150	50
	Inventory	350	250
	Trade receivables	300	350
	Cash and bank	<u>300</u>	<u>200</u>
		2,000	1,500
	Less: Liabilities taken over:		
	Debentures 40		20

	Trade payables	<u>420</u>		<u>190</u>
			<u>460</u>	<u>210</u>
	Net assets taken over		1,540	1,290
	Purchase consideration		<u>1,650</u>	1,200
	Goodwill		<u>110</u>	
	Capital reserve			<u>90</u>
(3)	Computation of securities premium			
	On preference share capital			
	A Ltd.- 3,00,000 x 50		150	
	B Ltd.- 2,00,000 x 50			100
	On equity share capital			
	A Ltd.- 40,00,000 x 20		800	
	B Ltd.- 30,00,000 x 20		--	<u>600</u>
	Total		<u>950</u>	<u>700</u>



TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. In case of amalgamation, the entry for elimination of unrealized profit or loss on stock is made
 - (a) By the vendor company
 - (b) By the purchasing company
 - (c) By the third party
 - (d) By the court

2. If expenses of liquidation of the vendor company are paid by the purchasing company then, in purchasing company's book, the account debited is
 - (a) Goodwill account.
 - (b) Liquidation expense account.
 - (c) Vendor company account.
 - (d) General reserve.

3. Amalgamation adjustment reserve is opened in the books of the amalgamated company to incorporate
 - (a) Assets of the amalgamating company.
 - (b) Non- Statutory reserves of the amalgamating company.
 - (c) Statutory reserves of the amalgamating company.
 - (d) General reserve of the amalgamating company.

4. Amalgamation Adjustment Reserve is presented in the financial statements of the transferee company as
 - (a) Other current asset.
 - (b) Separate line item with a negative sign under the head 'Reserves and Surplus'.
 - (c) Other non-current assets.
 - (d) Investment of the company

5. A company into which the vendor company is merged is called
 - (a) Transferee company.
 - (b) Transferor company.
 - (c) Selling company.
 - (d) Acquiree company.

6. If the purchase consideration is more than net assets (at agreed values) of the transferor company, difference shall be recorded as _____ in the books of the transferee company.

- (a) Goodwill.
- (b) Capital Reserve.
- (c) Profit.
- (d) Loss.

7. Which of the following statement is correct:

- (a) In case of merger – ESH can be issued only equity shares as a part of Purchase consideration.
- (b) In case of purchase – ESH can be issued Preference shares also as a part of Purchase consideration.
- (c) Both (a) and (b) are correct.
- (d) Both (a) and (b) are incorrect.

8. State which statement is correct:

- (a) In case of merger – assets and liabilities can only be taken over at book values.
- (b) In case of purchase – assets and liabilities can be taken over at book values or agreed values.
- (c) Both (a) and (b) are correct.
- (d) Both (a) and (b) are incorrect.

9. State which statement is correct:

- (a) In case of merger – All Reserves and surplus of vendor company are taken over by Purchasing company.
- (b) In case of Purchase – None of the Reserves and surplus of vendor company are taken over by Purchasing company.
- (c) Both (a) and (b) are correct.
- (d) Only (a) is correct.

10. State which statement is correct:

- (a) In case of merger – We use pooling of interest method for accounting.
- (b) In case of Purchase We use purchase method or pooling of interest method depending upon whether it is take over at agreed values or book values.
- (c) Both (a) and (b) are correct.
- (d) Only (a) is correct.

11. State which statement is incorrect:

- (a) In case of merger – We can issue either preference shares or equity shares to PSH.
- (b) In case of Purchase – We can issue either preference shares or equity shares to PSH.
- (c) In case of merger – We can issue only preference shares to PSH.
- (d) none of the above.

Answer to the Multiple Choice Questions

1.	(b)	2.	(a)	3.	(c)	4.	(b)	5.	(a)	6.	(a)
7.	(b)	8.	(c)	9.	(d)	10.	(d)	11.	(c)		

THEORETICAL QUESTIONS

12. What are the conditions, which, according to AS 14 on Accounting for Amalgamations, must be satisfied for an amalgamation in the nature of merger?

Answer:

Amalgamation in the nature of merger is an amalgamation, as per para 3(e) of

AS-14, which satisfies all the following conditions:

- i) All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.
- ii) Shareholders holding not less than 90% of the face value of the equity shares of the transferor company (other than the equity shares already held therein, immediately before the amalgamation, by the transferee company or its subsidiaries or their nominees) become equity shareholders of the transferee company by virtue of the amalgamation.
- iii) The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.
- iv) The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company.
- v) No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies. For example, if transferor company is following weighted average method for inventory valuation, the book value of the inventory of the transferor company will be revised by applying the FIFO method (if the transferee company follows FIFO method for inventory valuation).

If any one or more of the above conditions are not satisfied in an amalgamation, such amalgamation is called **amalgamation in the nature of purchase**.

13. Distinguish between (i) the pooling of interests method and (ii) the purchase method of recording transactions relating to amalgamation.

Answer:

i) Pooling of Interest Method

Under pooling of interests method, the assets, liabilities and reserves of the Transferor Company will be taken over by Transferee Company at existing carrying amounts unless any adjustment is

required due to different accounting policies followed by these companies.

As a result the difference between the amount recorded as share capital issued (plus any additional consideration in the form of cash or other assets) and the amount of share capital of Transferor Company should be adjusted in the reserves of the financial statements of Transferee company (recorded as deduction from the reserves where the capital issued is more than the capital of the transferor company).

In simple terms, where in case of pooling method- the amount to be adjusted against the reserves- can be computed in the following 3 steps-

Step I- Equity Share capital + Preference share capital issued+ any other additional consideration in form of cash and other assets by the Transferee Company.

Step II- Existing Equity share capital + Existing Preference share capital in the books of Transferor Company.

Step III- Step I- Step II= amount to be adjusted from the reserves of Transferee company.

ii) Purchase Method

Assets and Liabilities: the assets and liabilities of the transferor company should be incorporated at their existing carrying amounts or the purchase consideration should be allocated to individual identifiable assets and liabilities on the basis of their fair values at the date of amalgamation.



14. Briefly describe the disclosure requirements for amalgamation including additional disclosure, if any, for different methods of amalgamation as per AS 14 (Revised).

Answer:

The disclosure requirements for amalgamations have been prescribed in paragraphs 43 to 46 of AS 14 (Revised) on Accounting for Amalgamation. Refer Para 2.5 for details.

15. List the conditions to be fulfilled as per AS 14 (Revised) for an amalgamation to be in the nature of merger, in the case of companies.

Answer:

According to AS 14 "Accounting for Amalgamations", Amalgamation in the nature of merger is an amalgamation which satisfies all the following conditions:

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

- (iii) The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.
- (iv) The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company.
- (v) No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies.

16. Briefly explain the methods of accounting for amalgamation as per Accounting Standard-14.

Answer:

As per AS 14 on 'Accounting for Amalgamations', there are two main methods of accounting for amalgamations:

The Pooling of Interest Method

Under this method, the assets, liabilities and reserves of the transferor company are recorded by the transferee company at their existing carrying amounts (after making the necessary adjustments).

If at the time of amalgamation, the transferor and the transferee companies have conflicting accounting policies, a uniform set of accounting policies is adopted following the amalgamation. The effects on the financial statements of any changes in accounting policies are reported in accordance with AS 5 on 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies'.

The Purchase Method

Under the purchase method, the transferee company accounts for the amalgamation either by incorporating the assets and liabilities at their existing carrying amounts or by allocating the consideration to individual identifiable assets and liabilities of the transferor company on the basis of their fair values at the date of amalgamation. The identifiable assets and liabilities may include assets and liabilities not recorded in the financial statements of the transferor company.

SCENARIO BASED QUESTIONS

17. The following are the Balance Sheets of Yes Ltd. and No Ltd. as at 31st March, 20X1:

		Particulars	Notes	Rs.Yes Ltd (in crores)	Rs.No Ltd (in crores)
1		Equity and Liabilities			
		Shareholders' funds			
	A	Share capital	1	12	5
	B	Reserves and Surplus		88	10
2		Non-current liabilities			
	A	Long term borrowings	2	--	10
3		Current liabilities		<u>33</u>	<u>15</u>
		Total		<u>133</u>	<u>40</u>
		Assets			
1		Non-current assets			
	A	Property, Plant and Equipment	3	20	6
	B	Non-current investments	4	13	--
2		Current assets		<u>100</u>	<u>34</u>
		Total		<u>133</u>	<u>40</u>

Notes of accounts

		Yes Ltd.	No Ltd.
1	Share Capital Equity share capital		
	Authorized share capital		
	Issued and subscribed:	<u>25</u>	<u>5</u>
	Equity shares of Rs.10 each fully paid	<u>12</u>	<u>5</u>
		<u>12</u>	<u>5</u>
2	Long term borrowings		
	Unsecured loan from Yes Ltd.	--	<u>10</u>
		--	<u>10</u>
3	Property, Plant and Equipment		
	Gross value	70	30
	Depreciation	<u>(50)</u>	<u>(24)</u>
		<u>20</u>	<u>6</u>
4	Non-current investments		
	30 lakhs equity shares of Rs.10 each	3	--
	Long term loan to No Ltd.	<u>10</u>	--
		<u>13</u>	--

On that day Yes Ltd. absorbed No Ltd. The members of No Ltd. are to get one equity share of Yes Ltd. issued at a premium of Rs.2 per share for every five equity shares held by them in No Ltd. The necessary approvals are obtained.

You are asked to pass journal entries in the books of the two companies to give effect to the above if the amalgamation is in the nature of merger.

Answer:

Journal Entries in the books of No Ltd.

(Rupees in crores)

	Dr.	Cr.
Realization Account	Dr. 64.00	
To Property, plant and equipment Account		30.00
To Current Assets Account		34.00
(Being the assets taken over by Yes Ltd. transferred to Realization Account)		
Provision for depreciation Account	Dr. 24.00	
Current Liabilities Account	Dr. 15.00	
Unsecured Loan from Yes Ltd. Account	Dr. 10.00	
To Realization Account		49.00
(Being the transfer of liabilities and provision to Realization Account)		
Yes Ltd.	Dr. 1.2	
To Realization Account		1.2
(Being the amount of consideration due from Yes Ltd. credited to Realization Account)		
Equity Shareholders Account	Dr. 13.80	
To Realization Account	13.80	
(Being the loss on Realization transferred to equity share- holders account)		
Equity Share Capital Account	Dr. 5.00	
Reserves and Surplus Account	Dr. 10.00	
To Equity Shareholders Account		15.00
(Being the amount of share capital, reserves and surplus credited to equity shareholders account)		
Equity shares of Yes Ltd.	Dr. 1.20	
To Yes Ltd.	1.20	
(Being the receipt of 10 lakhs equity shares of Rs.10 each at Rs.12 per share for allotment to shareholders)		
Equity shareholders Account	Dr. 1.20	
To Equity shares of Yes Ltd.	1.20	
(Being the distribution of equity shares received from Yes Ltd. to shareholders)		

Journal Entries in the books of Yes Ltd.

(Rupees in crores)

		Dr.	Cr.
Business Purchase Account	Dr.	1.2	
To Liquidator of No Ltd. Account			1.2

(Being the amount of purchase consideration agreed under approved scheme of amalgamation- W.N. 1)

Property, plant and equipment	Dr.	6.00	
Current Assets	Dr.	34.00	
To Current Liabilities			15.00
To Unsecured Loan (from Yes Ltd.)			10.00
To Business Purchase Account			1.20
To Reserve & Surplus A/c			10.00
To Profit & loss A/c*			3.80

(Being the assets and liabilities taken over and the surplus transferred to Profit and loss account)

Liquidator of No Ltd.	Dr.	1.20	
To Equity Share Capital Account		1.00	
To Securities Premium Account		0.20	

(Being the allotment to shareholders of No Ltd.

10 lakhs equity shares of Rs.10 each at a premium of Rs.2 per share)

Unsecured Loan (from Yes Ltd.)	Dr.	10.00	
To Loan to No. Ltd.		10.00	

(Being the cancellation of unsecured loan given to No Ltd.)

Working Note:

Purchase Consideration Rs.in crores

$$\frac{50 \text{ lakhs}}{5} \times \text{Rs.12} \quad \text{i.e., 10 lakhs equity shares at Rs.12 per share 1.20}$$

$$\text{Number of equity shares of Rs.10 each to be issued} \left[\frac{1.20 \text{ crores}}{12} \right] = 10 \text{ lakhs.}$$

*As amalgamation in the nature of merger so balancing figure will be transferred to Profit & Loss account.

18. The following are the Balance Sheets of X Ltd. and Y Ltd :

		Particulars	Notes	Rs.X Ltd.	Rs.Y Ltd.
1	A	Equity and Liabilities			
		Shareholders' funds			
		Share capital	1	1,00,000	50,000

2	B	Reserves and Surplus	2	10,000	(10,000)
		Non-current liabilities			
	A	Long term borrowings	3	--	15,000
3		Current liabilities			
	A	Trade Payables		<u>25,000</u>	<u>5,000</u>
		Total		<u>135,000</u>	<u>60,000</u>
1		Assets			
		Non-current assets		1,20,000	60,000
	A	Property, Plant and Equipment			
	B	Non-current investments	4	15,000	--
		Total		<u>135,000</u>	<u>60,000</u>

Notes to accounts

1	Share Capital		X Ltd.	Y Ltd.
	Equity share capital		<u>1,00,000</u>	<u>50,000</u>
			<u>1,00,000</u>	<u>50,000</u>
2	Reserves and Surplus			
	Profit and loss A/c		10,000	--
	Profit and loss A/c (debit balance)		--	<u>(10,000)</u>
			<u>10,000</u>	<u>(10,000)</u>
3	Long term borrowings			
	Loan from X Ltd.		--	<u>15,000</u>
4	Non-current investments			
	Loan to Y Ltd.		<u>15,000</u>	--
			<u>15,000</u>	--

A new company XY Ltd. is formed to acquire the sundry assets and trade payables of X Ltd. and Y Ltd. and for this purpose, the sundry assets of X Ltd. are revalued at Rs.1,00,000. The debt due to X Ltd. is also to be discharged in shares of XY Ltd.

Show the Ledger Accounts to close the books of X Ltd.

Answer:

Books of X Ltd.

Realization Account

	Rs.		Rs.
To Sundry Assets	1,20,000	By Trade payables	25,000
		By XY Ltd. (Purchase consideration)	75,000
		By Shareholders (Loss on realization)	<u>20,000</u>
	1,20,000		1,20,000

Shareholders Account

	Rs.		Rs.
To Realization Account (Loss)	20,000	By Equity Share Capital	1,00,000
To Shares in XY Ltd.	<u>90,000</u>	By Profit and Loss Account	<u>10,000</u>
	1,10,000		1,10,000

Loan Y Ltd.

	Rs.		Rs.
To Balance b/d	<u>15,000</u>	By Shares in XY Ltd.	<u>15,000</u>

Shares in XY Ltd.

	Rs.		Rs.
To XY Ltd.	75,000	By Shareholders	90,000
To Loan Y Ltd.	<u>15,000</u>		
	90,000		90,000

XY Ltd.

	Rs.		Rs.
To Realization Account	<u>75,000</u>	By Shares in XY Ltd.	<u>75,000</u>

19. Super Express Ltd. and Fast Express Ltd. were in competing business. They decided to form a new company named Super Fast Express Ltd. The balance sheets of both the companies were as under:

		Particulars	Notes	Super Express Ltd. Rs.	Fast Express Ltd. Rs.
1		Equity and Liabilities			
		Shareholders' funds			
	A	Share capital	1	20,00,000	10,00,000
	B	Reserves and Surplus	2	1,00,000	2,60,000
2		Non-current liabilities			
	A	Long term provisions	3	1,00,000	---
2		Current liabilities			
	A	Trade Payables		<u>60,000</u>	<u>40,000</u>
		Total		<u>22,60,000</u>	<u>13,00,000</u>
		Assets			
1		Non-current assets			
	A	Property, Plant and Equipment	4	14,00,000	11,00,000
	B	Intangible assets		--	1,00,000

		Current assets	5		
2	A	Inventories		3,00,000	40,000
	B	Trade receivables		2,40,000	40,000
	C	Cash and Cash equivalents		<u>3,20,000</u>	<u>20,000</u>
		Total	6	<u>22,60,000</u>	<u>13,00,000</u>

Notes to accounts

		Super Express Ltd. Rs.	Fast Express Ltd.Rs.
1	Share Capital		
	Equity shares of Rs.100 each	<u>20,00,000</u>	<u>10,00,000</u>
2	Reserves and Surplus		
	Insurance reserve	1,00,000	--
	Employee profit sharing reserve	--	60,000
	Reserve account	--	1,00,000
	Surplus	--	1,00,000
		1,00,000	2,60,000
3	Long term provisions		
	Provident fund	<u>1,00,000</u>	--
	Total	<u>1,00,000</u>	--
4	Property, Plant and Equipment		
	Land and Building	10,00,000	6,00,000
	Plant and machinery	<u>4,00,000</u>	<u>5,00,000</u>
		<u>14,00,000</u>	<u>11,00,000</u>
5	Intangible assets		
	Goodwill	--	<u>1,00,000</u>
		--	<u>1,00,000</u>
6.	Cash and Cash Equivalents		
	Cash at Bank	2,20,000	10,000
	Cash in hand	<u>1,00,000</u>	<u>10,000</u>
		<u>3,20,000</u>	<u>20,000</u>

The assets and liabilities of both the companies were taken over by the new company at their book values. The companies were allotted equity shares of Rs.100 each in lieu of purchase consideration amounting to Rs.30,000 (20,000 for Super-Fast Express Ltd and 10,000 for Fast Express Ltd.).

Prepare opening balance sheet of Super Fast Express Ltd. considering pooling method.

Answer:

Balance Sheet of Super Fast Express Ltd.

Particulars		Notes	Rs.
	Equity and Liabilities		
1	Shareholders' funds		
a	Share capital	1	30,00,000
b	Reserves and Surplus	2	3,60,000
2	Non-current liabilities		
a	Long-term provisions	3	1,00,000
3	Current liabilities		
a	Trade Payables		1,00,000
	Total		35,60,000
	Assets		
1	Non-current assets		
a	Property, Plant and Equipment	4	25,00,000
b	Intangible assets	5	1,00,000
2	Current assets		
	Inventories		3,40,000
	Trade receivables		2,80,000
	Cash and cash equivalents	6	3,40,000
	Total		35,60,000

Notes to Accounts

		Rs.
1	Share Capital	
	Equity share capital	
	Issued, subscribed and paid up	
	30,000 Equity shares of Rs.100 each	30,00,000
	Total	30,00,000
2	Reserves and Surplus	
	Reserve account	1,00,000
	Surplus	1,00,000
	Insurance reserve	1,00,000
	Employees profit sharing account	60,000
	Total	3,60,000
3	Long-term provisions	
	Provident fund	1,00,000

	Total		1,00,000
4	Property, Plant and Equipment		
	Buildings		16,00,000
	Machinery		9,00,000
	Total		25,00,000
5	Intangible assets		
	Goodwill		1,00,000
	Total		1,00,000
6	Cash and cash equivalents		
	Balances with banks		2,30,000
	Cash on hand		1,10,000
	Total		3,40,000

20. The following were the Balance Sheets of P Ltd. and V Ltd. as at 31st March, 20X1:

		Particulars	Notes	Rs.P Ltd (Rs.in Lakhs)	Rs.V Ltd (Rs.in Lakhs)
1		Equity and Liabilities			
		Shareholders' funds			
	A	Share capital	1	15,000	6,000
	B	Reserves and Surplus	2	15,370	4,335
2		Non-current liabilities			
		Long term borrowings	3	--	1,000
3		Current liabilities			
	A	Trade Payables		1,200	463
	B	Short term provisions		<u>1,830</u>	<u>702</u>
		Total		<u>33,400</u>	<u>12,500</u>
		Assets			
1		Non-current assets			
	A	Property, Plant and Equipment	4	22,304	6,750
2		Current assets			
		Inventories		7,862	4,041
	A	Trade receivables		2,120	1,100
	B	Cash and Cash equivalents		<u>1,114</u>	<u>609</u>
	C	Total		<u>33,400</u>	<u>12,500</u>

Notes to accounts

			Rs.P Ltd (Rs.in Lakhs)	Rs.V Ltd (Rs.in Lakhs)
1	Share Capital		<u>15,000</u>	<u>6,000</u>
2	Reserves and Surplus			
	Securities premium		3,000	--
	Foreign project reserve		--	310
	General reserve		9,500	3,200
	Profit and loss account		<u>2,870</u>	<u>825</u>
			<u>15,370</u>	<u>4,335</u>
3	Long term borrowings			
	12% debentures		--	<u>1,000</u>
			--	<u>1,000</u>
4	Property, Plant and			
	Equipment			
	Land and Building		6,000	--
	Plant and machinery		14,000	5,000
	Furniture and fixtures		<u>2,304</u>	<u>1,750</u>
			<u>22,304</u>	<u>6,750</u>

All the bills receivable held by V Ltd. were P Ltd.'s acceptances.

On 1st April 20X1, P Ltd. took over V Ltd in an amalgamation in the nature of merger. It was agreed that in discharge of consideration for the business P Ltd. would allot three fully paid equity shares of Rs.10 each at par for every two shares held in V Ltd. It was also agreed that 12% debentures in V Ltd. would be converted into 13% debentures in P Ltd. of the same amount and denomination.

Details of trade receivables and trade payables as under:

	P Ltd. (Rs.in lakhs)	V Ltd. (Rs.in lakhs)
Trade payables		
Bills Payable	120	-
Trade Creditors	<u>1,080</u>	<u>463</u>
	<u>1,200</u>	<u>463</u>
Trade receivables		
Trade debtors	2,120	1,020
Bills Receivable	--	<u>80</u>
	<u>2,120</u>	<u>1,100</u>

Expenses of amalgamation amounting to Rs.1 lakh were borne by P Ltd.

You are required to: (i) pass journal entries in the books of P Ltd. and (ii) prepare P Ltd.'s Balance Sheet immediately after the merger.

Answer:

Books of P Ltd.

Journal Entries

	Dr.	Cr.
	(Rs.in Lacs)	(Rs.in Lacs)
Business Purchase A/c	Dr. 9,000	
To Liquidator of V Ltd.		9,000

(Being business of V Ltd. taken over for Consideration settled as per agreement)

Plant and Machinery	Dr.	5,000
Furniture & Fittings	Dr.	1750
Inventory	Dr.	4,041
Debtors	Dr.	1,020
Cash at Bank	Dr.	609
Bills Receivable	Dr.	80
To Foreign Project Reserve		310
To General Reserve (3,200 - 3,000)		200
To Profit and Loss A/c (825)		825
To Liability for 12% Debentures		1,000
To Creditors		463
To Provisions		702
To Business Purchase		9,000

(Being assets & liabilities taken over from V Ltd.)

Liquidator of V Ltd. A/c	Dr.	9,000
To Equity Share Capital A/c		9,000

(Purchase consideration discharged in the form of equity shares)

Goodwill A/c	Dr.	1
To Bank A/c		1

(Liquidation expenses paid by P Ltd debited to Goodwill A/c)

Profit and loss A/c	Dr.	1
To Goodwill A/c		1

(being the Goodwill charged to Profit and loss account)

Liability for 12% Debentures A/c	Dr.	1,000
To 13% Debentures A/c		1,000

(12% debentures discharged by issue of 13% debentures)

Bills Payable A/c

Dr.

80

To Bills Receivable A/c

80

(Cancellation of mutual owing on account of bills)

Balance Sheet of P Ltd. as at 1st April, 20X1 (after merger)

Particulars		Notes	Rs.(in lakhs)
	Equity and Liabilities		
1	Shareholders' funds		
A	Share capital	1	24,000
B	Reserves and Surplus	2	16,704
2	Non-current liabilities		
A	Long-term borrowings	3	1,000
3	Current liabilities		
A	Trade Payables (1,543 + 40)		1,583
B	Short-term provisions		2,532
	Total		45,819
	Assets		
1	Non-current assets		
A	Property, Plant and Equipment	4	29,054
2	Current assets		
A	Inventories		11,903
B	Trade receivables		3,140
C	Cash and cash equivalents		1,722
	Total		45,819

Notes to accounts

		Rs.
1.	Share Capital	
	Equity share capital	
	Authorized, issued, subscribed and paid up	
	24 crores equity shares of Rs.10 each	<u>24,000</u>
	(Of the above shares, 9 crores shares have been issued for consideration other than cash)	
	Total	<u>24,000</u>
2.	Reserves and Surplus	
	General Reserve	9,700
	Securities Premium	3,000
	Foreign Project Reserve	310
	Profit and Loss Account	<u>3,694</u>

	Total	<u>16,704</u>
3.	Long-term borrowings	
	Secured	
	13% Debentures	<u>1,000</u>
4.	Property, Plant and Equipment	
	Land & Buildings	6,000
	Plant & Machinery	19,000
	Furniture & Fittings	<u>4,054</u>
	Total	<u>29,054</u>

Working Note:

Computation of purchase consideration

The purchase consideration was discharged in the form of three equity shares of P Ltd. for every two equity shares held in V Ltd.

Purchase consideration = Rs.6,000 lacs $\times$ 3 / 2 = Rs.9,000 lacs.

21. Sun and Neptune had been carrying on business independently. They agreed to amalgamate and form a new company Jupiter Ltd. with an authorised share capital of Rs.4,00,000 divided into 80,000 equity shares of Rs.5 each. On 31st March, 20X3 the respective information of Sun and Neptune were as follows:

	Sun (Rs.)	Neptune (Rs.)
Share capital	3,65,000	3,52,500
Current liabilities	5,97,000	1,80,250
Property, Plant and Equipment	6,35,000	3,65,000
Current assets	3,27,000	1,67,750

Additional Information:

(a) Revalued figures of non-current and Current assets were as follows:

	Sun (Rs.)	Neptune (Rs.)
Property, Plant and Equipment	7,10,000	3,90,000
Current Assets	2,99,500	1,57,750

(b) The debtors and creditors include Rs.43,350 owed by Sun to Neptune.

The purchase consideration is satisfied by issue of the following shares and debentures.

(i) 60,000 equity shares of Jupiter Ltd. to Sun and Neptune in the proportion to the profitability of their respective business based on the average net profit during the last three years which were as follows:

	Sun (Rs.)	Neptune (Rs.)
20X1 Profit	4,49,576	2,73,900

20X2 (Loss)/Profit	(2,500)	3,42,100
20X3 Profit	3,77,924	3,59,000

- (ii) 15% debenture in Jupiter Ltd. at par to provide an income equivalent to 8% return business as on capital employed in their respective business as on 31st March, 20X3 after revaluation of assets.

You are required to:

- (1) Compute the amount of debentures and shares to be issued to Sun and Neptune.
- (2) A Balance sheet of Jupiter Ltd. showing the position immediately after amalgamation.

Answer:

(1) Computation of Amount of Debentures and Shares to be issued:

	Sun	Neptune
(i) Average Net Profit		
Rs. $(4,49,576 - 2,500 + 3,77,924) / 3 =$	2,75,000	
Rs. $(2,73,900 + 3,42,100 + 3,59,000) / 3 =$		3,25,000
(ii) Equity Shares Issued		
(a) Ratio of distribution		
Sun: Neptune		
275 325		
(b) Number		
Sun : 27,500		
Neptune: <u>32,500</u>		
<u>60,000</u>		
(c) Amount		
27,500 shares of Rs.5 each =	1,37,500	
32,500 shares of Rs.5 each =		1,62,500
(iii) Capital Employed (after revaluation of assets)	Rs.	Rs.
Property, plant and equipment	7,10,000	3,90,000
Current Assets	<u>2,99,500</u>	<u>1,57,750</u>
	10,09,500	5,47,750
Less: Current Liabilities	<u>(5,97,000)</u>	<u>(1,80,250)</u>
	<u>4,12,500</u>	<u>3,67,500</u>
(iv) Debentures Issued		
8% Return on capital employed	33,000	29,400
15% Debentures to be issued to provide equivalent income:		
Sun: $33,000 \times 100 / 15 = 2,20,000$		
Neptune: $29,400 \times 100 / 15 = 1,96,000$		

(2) Balance Sheet of Jupiter Ltd.**As at 31st March 20X3 (after amalgamation)**

Particulars	Note No	Rs.
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Share Capital	1	3,00,000
(b) Reserves and Surplus	2	64,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	4,16,000
(3) Current Liabilities		
(a) Other current liabilities		7,33,900
Total		15,13,900
II. Assets		
(1) Non-current assets		
(a) PPE		11,00,000
(2) Current assets		
(a) Other current assets		4,13,900
Total		15,13,900

Notes to Accounts

		Rs.
1	Share Capital	
	Authorized	
	80,000 Equity Shares of Rs.5 each	4,00,000
	Issued and Subscribed	
	60,000 Equity Shares of Rs.5 each	<u>3,00,000</u>
	(all the above shares are allotted as fully paid-up pursuant to a contract without payment being received in cash)	
2	Reserve and Surplus	
	Capital Reserve	<u>64,000</u>
3	Long-term borrowings	
	Secured Loans	
	15% Debentures	<u>4,16,000</u>

Working Notes:

	Sun	Neptune	Total
	Rs.	Rs.	Rs.
(1)			
Purchase Consideration			
Equity Shares Issued	1,37,500	1,62,500	3,00,000

	15% Debentures Issued	2,20,000	1,96,000	4,16,000
		3,57,500	3,58,500	7,16,000
(2)	Capital Reserve			
(a)	Net Assets taken over			
	Property, plant & equipment	7,10,000	3,90,000	11,00,000
	Current Assets	2,99,500	1,14,400*	4,13,900
		10,09,500	5,04,400	15,13,900
	Less: Current Liabilities	(5,53,650**)	(1,80,250)	(7,33,900)
		4,55,850	3,24,150	7,80,000
(b)	Purchase Consideration	3,57,500	3,58,500	7,16,000
(c)	Capital Reserve [(a) - (b)]	<u>98,350</u>		
(d)	Goodwill [(b) - (a)]		<u>34,350</u>	
(e)	Capital Reserve [Final Figure(c) -(d)]			64,000

* 1,57,750–43,350= 1,14,400

** 5,97,000–43,350= 5,53,650

22. The following information from Balance Sheet of X Ltd. as at 31st March, 20X1:

	Rs.
4,000 Equity shares of Rs.100 each	4,00,000
10% Debentures	2,00,000
Loans	80,000
Trade payables	1,60,000
General Reserve	40,000
Building	1,70,000
Machinery	3,20,000
Inventory	1,10,000
Trade receivables	1,30,000
Bank	68,000
Patent	65,000
Share issue Expenses	17,000

Y Ltd. agreed to absorb X Ltd. on the following terms and conditions:

- (1) Y Ltd. would take over all assets, except bank balance and Patent at their book values less 10%. Goodwill is to be valued at 4 year's purchase of super profits, assuming that the normal rate of return be 8% on the combined amount of share capital and general reserve.
- (2) Y Ltd. is to take over trade payables at book value.
- (3) The purchase consideration is to be paid in cash to the extent of Rs.3,00,000 and the balance in fully paid equity shares of Rs.100 each at Rs.125 per share.

The average profit is Rs.62,200. The liquidation expenses amounted to Rs.8,000. Y Ltd. sold prior to 31st March, 20X1 goods costing Rs.60,000 to X Ltd. for Rs.80,000. Rs.50,000 worth of goods are still in Inventory of X Ltd. on 31st March, 20X1. Trade payables of X Ltd. include Rs.20,000 still due to Y Ltd.

Show the necessary Ledger Accounts to close the books of X Ltd. and prepare the Balance Sheet of Y Ltd. as at 1st April, 20X1 after the takeover.

Answer:

Books of X Limited

Realisation Account

		Rs.			Rs.
To	Building	1,70,000	By	Trade payables	1,60,000
To	Machinery	3,20,000	By	Y Ltd.	6,05,000
To	Inventory	1,10,000	By	Equity Shareholders (Loss)	38,000
To	Trade receivables	1,30,000			
To	Patent	65,000			
To	Bank (Exp.)	<u>8,000</u>			
		<u>8,03,000</u>			<u>8,03,000</u>

Bank Account

To	Balance b/d	68,000	By	Realisation (Exp.)	8,000
To	Y Ltd.	3,00,000	By	10% Debentures	2,00,000
			By	Loan	80,000
			By	Equity shareholders	<u>80,000</u>
		<u>3,68,000</u>			<u>3,68,000</u>

10% Debentures Account

To	Bank	<u>2,00,000</u>	By	Balance b/d	<u>2,00,000</u>
		<u>2,00,000</u>			<u>2,00,000</u>

Loan Account

To	Bank	<u>80,000</u>	By	Balance b/d	<u>80,000</u>
		<u>80,000</u>			<u>80,000</u>

Share Issue Expenses Account

To	Balance b/d	<u>17,000</u>	By	Equity shareholders	<u>17,000</u>
		<u>17,000</u>			<u>17,000</u>

General Reserve Account

To	Equity shareholders	<u>40,000</u>	By	Balance b/d	<u>40,000</u>
		<u>40,000</u>			<u>40,000</u>

Y Ltd. Account

To	Realisation A/c	6,05,000	By	Bank	3,00,000
			By	Equity share in Y Ltd. (2,440 shares at Rs.125 each)	<u>3,05,000</u>
		<u>6,05,000</u>			<u>6,05,000</u>

Equity Shares in Y Ltd. Account

To	Y Ltd.	<u>3,05,000</u>	By	Equity shareholders	<u>3,05,000</u>
		<u>3,05,000</u>			<u>3,05,000</u>

Equity Share Holders Account

To	Realisation	38,000	By	Equity share capital	4,00,000
To	Share issue Expenses	17,000	By	General reserve	40,000
To	Equity shares in B Ltd.	3,05,000			
To	Bank	<u>80,000</u>			
		<u>4,40,000</u>			<u>4,40,000</u>

Y Ltd

Balance Sheet as on 1st April, 20X1 (An extract)¶

	Particulars	Notes	Rs.
1	Equity and Liabilities		
a	Shareholders' funds		
	Share capital	1	2,44,000
b	Reserves and Surplus	2	53,500
2	Current liabilities		
a	Trade Payables	3	1,40,000
b	Bank overdraft		3,00,000
	Total		7,37,500
	Assets		
1	Non-current assets		
a	Property, Plant and Equipment	4	4,41,000
	Intangible assets	5	1,08,000
2	Current assets		
a	Inventories	6	91,500
b	Trade receivables	7	97,000
			7,37,500

Notes to Accounts

			Rs.
1	Share Capital		
	Equity share capital		
	2,440 Equity shares of Rs.100 each (Shares have been issued for consideration other than cash)		2,44,000
	Total		2,44,000
2	Reserves and Surplus (an extract)		
	Securities Premium		61,000
	Profit and loss account		
	Less: Unrealised profit	(7,500)	(7,500)
	Total		53,500
3	Trade payables		
	Opening balance	1,60,000	
	Less: Inter-company transaction cancelled upon amalgamation	(20,000)	1,40,000
4	Property, Plant and Equipments		
	Buildings		1,53,000
	Machinery		2,88,000
	Total		4,41,000
5	Intangible assets		
	Goodwill		1,08,000
6	Inventories		
	Opening balance	99,000	
	Less: Cancellation of profit upon amalgamation	(7,500)	91,500
7	Trade receivables		
	Opening balance	1,17,000	
	Less: Intercompany transaction cancelled upon amalgamation	(20,000)	97,000

Working Notes:

1. Valuation of Goodwill	Rs.
Average profit	62,200
Less: 8% of Rs.4,40,000	(35,200)
Super profit	27,000
Value of Goodwill = 27,000 x 4	1,08,000
2. Net Assets for purchase consideration	
Goodwill as valued in W.N.1	1,08,000
Building	1,53,000

Machinery	2,88,000
Inventory	99,000
Trade receivables (1,30,000-13,000)	<u>1,17,000</u>
Total Assets	7,65,000
Less: Trade payables	<u>(1,60,000)</u>
Net Assets	<u>6,05,000</u>
Out of this Rs.3,00,000 is to be paid in cash and remaining i.e., (6,05,000 – 3,00,000) Rs.3,05,000 in shares of Rs.125. Thus, the number of shares to be allotted $3,05,000/125 = 2,440$ shares.	
3. Unrealised Profit on Inventory	Rs.
The Inventory of X Ltd. includes goods worth Rs.50,000 which was sold by Y Ltd. on profit. Unrealized profit on this Inventory will be $[20,000/80,000 \times 50,000]$	12,500
As Y Ltd purchased assets of X Ltd. at a price 10% less than the book value, 10% need to be adjusted from the Inventory i.e., 10% of Rs.50,000.	<u>(5,000)</u>
Amount of unrealized profit	<u>7,500</u>

23. X Co. Ltd. having share capital of Rs.50 lakhs divided into equity shares of Rs.10 each was taken over by Y Co. Ltd. Y Co. Ltd. issued 11 equity shares of Rs.10 each for every 10 shares of X Co. Ltd.



Explain how the difference will be adjusted in the books of Y Co. Ltd. for the shares issued under the 'Pooling of interests method' of amalgamation as per AS 14.

Answer:

Particulars	Rs.
Purchase consideration = $5,00,000 \times 11/10 = 55,000$ shares of Rs.10 each	55,00,000
Less: Share capital of X Co. Ltd.	50,00,000
Difference Adjusted through General Reserve	5,00,000

24. On 1st April, 2018, Tina Ltd. take over the business of Rina Ltd. and discharged purchase consideration as follows:

- Issued 50,000 fully paid Equity shares of Rs.10 each at a premium of Rs.5 per share to the equity shareholders of Rina Ltd.
- Cash payment of Rs.50,000 was made to equity shareholders of Rina Ltd.
- Issued 2,000 fully paid 12% Preference shares of Rs.100 each at par to discharge the preference shareholders of Rina Ltd.
- Debentures of Rina Ltd. 20,000) will be converted into equal number and amount of 10% debentures of Tina Ltd.

Calculate the amount of Purchase consideration as per AS-14 and pass Journal Entry relating to discharge of purchase consideration in the books of Tina Ltd.

Answer:

As per AS 14, 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

Particulars	Rs.
Equity Shares (50,000x 15)	7,50,000
Cash payment	50,000
12% Preference Share Capital	2,00,000
Purchase Consideration	10,00,000

Note: Payment to debenture holders are not covered by the term 'consideration'.

Journal entry

Particulars	Rs.	Rs.
Liquidation of Rina Ltd. A/c	10,00,000	
To Equity share capital A/c		5,00,000
To 12% Preference share capital A/c		2,00,000
To Securities premium A/c		2,50,000
To Bank/Cash A/c		50,000
(Being payment of cash and issue of shares for discharge of purchase consideration)		

QUESTIONS FROM RTP'S, MTP'S, QP'S

Question 1

Robert Ltd. and Diamond Ltd. give the following information as at 31.03.2020:

	Robert Ltd. (Rs. in lakhs)	Diamond Ltd. (Rs. in lakhs)
Equity Share Capital (Fully paid shares of Rs. 10 each)	22,500	9,000
Securities Premium	4,500	-
Foreign Project Reserve	-	465
General Reserve	14,250	4,800
Profit and Loss Account	4,305	1,162.5
12% Debentures	-	1,500
Trade payables	1,800	694.5
Provisions	2,745	1,053
Land and Buildings	9,000	-
Plant and Machinery	21,000	7,500
Furniture, Fixtures and Fittings	3,456	2,550
Inventory	11,793	6,061.5
Trade receivables	3,180	1,650
Cash at Bank	1,671	913.5

All the bills receivable held by Diamond Ltd. were Robert Ltd.'s acceptances.

On 1st April 2020, Robert Ltd. took over Diamond Ltd. in an amalgamation in the nature of merger. It was agreed that in discharge of consideration for the business, Robert Ltd. would allot three fully paid equity shares of Rs. 10 each at par for every two shares held in Diamond Ltd. It was also agreed that 12% debentures in Diamond Ltd. would be converted into 13% debentures in Robert Ltd. of the same amount and denomination.

Details of trade receivables and trade payables are as under:

Particulars	Robert Ltd.	Diamond Ltd.
	(Rs. in lakhs)	
Trade Payables:		
Creditors	1,620	694.5
Bills Payable	180	-
	1,800	694.5
Trade receivables:		
Debtors	3,180	1,530
Bills Receivables	-	120
	3,180	1,650

Expenses of amalgamation amounting to Rs. 1.5 lakhs were borne by Robert Ltd. You are required to:

- (i) Pass journal entries in the books of Robert Ltd. and
- (ii) Prepare Robert Ltd.'s Balance Sheet immediately after the merger.

(MTP Apr'22)

Answer :

Books of Robert Ltd. Journal Entries

		(Rs. in Lacs)	(Rs. in Lacs)
Business Purchase A/c	Dr.	13,500	
To Liquidator of Diamond Ltd.			13,500
(Being business of Diamond Ltd. taken over for consideration settled as per agreement)			
Plant and Machinery	Dr.	7,500	
Furniture & Fittings	Dr.	2,550	
Inventory	Dr.	6,061.5	
Debtors	Dr.	1,530	
Cash at Bank	Dr.	913.5	
Bills Receivable	Dr.	120	
To Foreign Project Reserve			465
To General Reserve Rs. (4,800 - 4,500)			300
To Profit and Loss A/c			1,162.5
To Liability for 12% Debentures			1,500
To Creditors			694.5
To Provisions			1,053
To Business Purchase A/c			13,500
(Being assets & liabilities taken over from Diamond Ltd.)			
Liquidator of Diamond Ltd. A/c	Dr.	13,500	
To Equity Share Capital A/c			13,500
(Purchase consideration discharged in the form of equity shares)			
Profit & Loss A/c	Dr.	1.5	
To Bank A/c			1.5
(Liquidation expenses paid and charged to P& L A/c)			
Liability for 12% Debentures A/c	Dr.	1,500	
To 13% Debentures A/c			1500
(12% debentures discharged by issue of 13% debentures)			
Bills Payable A/c	Dr.	120	

To Bills Receivable A/c			120
(Cancellation of mutual owing on account of bills)			

Balance Sheet of Robert Ltd. as at 1st April, 2020 (after merger)

	Particulars	Notes	Rs. (in lakhs)
	Equity and Liabilities		
1	Shareholders' funds		
A	Share capital	1	36,000
B	Reserves and Surplus	2	24,981
2	Non-current liabilities		
A	Long-term borrowings	3	1,500
3	Current liabilities		
A	Trade Payables (1,800+694.5-120)		2,374.5
B	Short-term provisions (2,745+1,053)		3,798
	Total		68,653.5
	Assets		
1	Non-current assets		
A	Property, Plant & Equipment	4	43,506
2	Current assets		
A	Inventories (11,793+6,061.5)		17,854.5
B	Trade receivables (3,180+1,650-120)		4,710
C	Cash and cash equivalents (1,671+913.5-1.5)		2,583
	Total		68,653.5

Notes to Accounts

		Rs.
1.	Share Capital	
	Equity share capital	
	Authorized, issued, subscribed and paid-up: 36 crores equity shares of Rs. 10 each (out of these shares, 13.5 crores shares have been issued for consideration other than cash)	36,000
2.	Reserves and Surplus	
	General Reserve	14,550
	Securities Premium	4,500
	Foreign Project Reserve	465
	Profit and Loss Account Rs. (4,305 +1,162.5-1.5)	5,466
	Total	24,981

3.	Long-term borrowings	
	Secured	
	13% Debentures	1,500
4.	PPE	
	Land & Buildings	9,000
	Plant & Machinery	28,500
	Furniture & Fittings	6,006
	Total	43,506

Working Note:

Computation of purchase consideration

Purchase consideration was discharged in the form of three equity shares of Robert Ltd. for every two equity shares held in Diamond Ltd.

Purchase consideration = Rs. 9,000 lacs $\times$ $\frac{3}{2}$ = Rs. 13,500 lacs

Question 2

Sun and Neptune (both companies) had been carrying on business independently. They agreed to amalgamate and form a new company Jupiter Ltd. with an authorised share capital of Rs. 4,00,000 divided into 80,000 equity shares of Rs. 5 each. On 31st March, 2021 Sun and Neptune provide the following information:

	Sun (Rs.)	Neptune (Rs.)
Property, Plant & Equipment	6,35,000	3,65,000
Current Assets	3,27,000	1,67,750
	9,62,000	5,32,750
Less: Current Liabilities	(5,97,000)	(1,80,250)
Representing Capital	3,65,000	3,52,500

Additional Information:

(a) Revalued figures of Property, Plant & Equipment and Current assets were as follows:

	Sun (Rs.)	Neptune (Rs.)
Property, Plant & Equipment	7,10,000	3,90,000
Current Assets	2,99,500	1,57,750

(b) The debtors and creditors include Rs. 43,350 owed by Sun to Neptune.

The purchase consideration is satisfied by issue of the following shares and debentures.

(i) 60,000 equity shares of Jupiter Ltd. to Sun and Neptune in the proportion to the profitability of their respective business based on the average net profit during the last three years which were as follows:

	Sun (Rs.)	Neptune (Rs.)
2019 Profit	4,49,576	2,73,900

2020 (Loss)/Profit	(2,500)	3,42,100
2021 Profit	3,77,924	3,59,000

(ii) 15% debentures in Jupiter Ltd. at par to provide an income equivalent to 8% return business as on capital employed in their respective business as on 31 st March, 2021 after revaluation of assets.

You are required to :

- (1) Compute the amount of debentures and shares to be issued to Sun and Neptune.
- (2) A Balance sheet of Jupiter Ltd. showing the position immediately after amalgamation.

(MTP April '23, PYP May '23)

Answer ;

(1) Computation of Amount of Debentures and Shares to be issued:

		Sun	Neptune
		Rs.	Rs.
(i)	Average Net Profit		
	Rs. (4,49,576-2,500+3,77,924)/3	= 2,75,000	
	Rs. (2,73,900+,3,42,100+3,59,000)/3		= 3,25,000

(ii) Equity Shares Issued

(a) Ratio of distribution

Sun	:	Neptune
275	:	325

(b) Number

Sun	:	27,500
Neptune	:	32,500
		60,000

(c) Amount

	Sun	Neptune
	Rs.	Rs.
27,500 shares of Rs. 5 each	1,37,500	
32,500 shares of Rs. 5 each		1,62,500
(iii) Capital Employed (after revaluation of assets)	Rs.	Rs.
Property, Plant & Equipment	7,10,000	3,90,000
Current Assets	2,99,500	1,57,750
	10,09,500	5,47,750
Less: Current Liabilities	-5,97,000	-1,80,250
	4,12,500	3,67,500
(iv) Debentures Issued		

	8% Return on capital employed	33,000	29,400
	15% Debentures to be issued to provide equivalent income:		
	Sun: $33,000 \times 100/15$	2,20,000	
	Neptune: $29,400 \times 100/15$		1,96,000

(2) Balance Sheet of Jupiter Ltd. As at 31st March 2021 (after amalgamation)

Particulars	Note No	Rs.
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Share Capital	1	3,00,000
(b) Reserves and Surplus	2	64,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	4,16,000
(3) Current Liabilities		
(a) Other current liabilities		7,33,900
Total		15,13,900
II. Assets		
(1) Non-current assets		
(a) Property, Plant & Equipment		11,00,000
(2) Current assets		
(a) Other current assets		4,13,900
Total		15,13,900

Notes to Accounts

		Rs.
1	Share Capital	
	Authorized	
	80,000 Equity Shares of Rs. 5 each	4,00,000
	Issued and Subscribed	
	60,000 Equity Shares of Rs. 5 each	3,00,000
	(all the above shares are allotted as fully paid-up pursuant to a contract without payment being received in cash)	
2	Reserve and Surplus	
	Capital Reserve	64,000
3	Long-term borrowings	
	Secured Loans	
	15% Debentures	4,16,000

Working Notes:

		Sun	Neptune	Total
		Rs.	Rs.	Rs.
(1)	Purchase Consideration			
	Equity Shares Issued	1,37,500	1,62,500	3,00,000
	15% Debentures Issued	2,20,000	1,96,000	4,16,000
		3,57,500	3,58,500	7,16,000
(2)	Capital Reserve			
(a)	Net Assets taken over			
	Property, Plant & Equipment	7,10,000	3,90,000	11,00,000
	Current Assets	2,99,500	1,14,400*	4,13,900
		10,09,500	5,04,400	15,13,900
	Less: Current Liabilities	(5,53,650**)	(1,80,250)	(7,33,900)
		4,55,850	3,24,150	7,80,000
(b)	Purchase Consideration	3,57,500	3,58,500	7,16,000
(c)	Capital Reserve [(a) - (b)]	98,350		
(d)	Goodwill [(b) - (a)]		34,350	
(e)	Capital Reserve [Final Figure(c) -(d)]			64,000

* 1,57,750–43,350= 1,14,400

** 5,97,000–43,350= 5,53,650

**Question 3**

The following are the Balance Sheets of Aakash Limited and Ganga Limited as at March 31, 2021:

Particulars	Note No.	Aakash Limited (Rs.)	Ganga Limited (Rs.)
I. Equity and Liabilities:			
(1) Shareholder's Funds:			
(a) Share Capital	1	80,00,000	20,00,000
(b) Reserves and Surplus	2	(3,24,00,000)	56,00,000
(2) Non-Current Liabilities:			
(a) Secured Loans	3	3,20,00,000	1,60,00,000
(b) Unsecured Loans	4	1,72,00,000	-
(3) Current Liabilities:			
(a) Trade Payables		56,00,000	36,00,000
(b) Other Current Liabilities	5	2,04,00,000	56,00,000
Total		5,08,00,000	3,28,00,000

II. Assets:			
(1) Non-Current Assets:			
Property, Plant & Equipment		68,00,000	1,36,00,000
(2) Current Assets:			
(a) Inventories		3,68,00,000	-
(b) Other Current Assets		72,00,000	1,92,00,000
Total		5,08,00,000	3,28,00,000

Notes to Accounts:

		Aakash Limited (Rs.)	Ganga Limited (Rs.)
1. Share Capital			
Authorized, Issued, Subscribed & Paid up :			
6,00,000 Equity Shares of Rs.10 each		60,00,000	-
20,000 Preference Shares of Rs. 100 each		20,00,000	-
2,00,000 Equity Shares of Rs. 10 each		-	20,00,000
		80,00,000	20,00,000
2. Reserves and Surplus			
General Reserve		8,00,000	56,00,000
Surplus		(3,32,00,000)	-
		(3,24,00,000)	56,00,000
3. Secured Loans (Secured Loans of Aakash Limited are secured against pledge of Inventories)		3,20,00,000	1,60,00,000
4. Unsecured Loans		1,72,00,000	-
5. Other Current Liabilities			
Statutory Liabilities		1,44,00,000	20,00,000
Liability to Employees		60,00,000	36,00,000
		2,04,00,000	56,00,000

Both the companies go into liquidation and a new company 'AakashGanga Limited' is formed to take over their business. The following information is given:

- All Current Assets of two companies, except pledged inventory are taken over by Aakash Ganga Limited. The realizable value of all the Current Assets (including pledged inventory) is 80% of book value in case of Aakash Limited and 70% for Ganga Limited.
- Property, Plant and Equipment of both the companies are taken over at book value by AakashGanga Limited.

- (iii) Secured Loans include Rs. 32,00,000 accrued interest in case of Ganga Limited.
- (iv) 4,00,000 Equity Shares of Rs. 10 each are allotted by AakashGanga Limited at par against cash payment of entire face value to the shareholders of Aakash Limited and Ganga Limited in the ratio of shares held by them in Aakash Limited and Ganga Limited.
- (v) Preference Shareholders in Aakash Limited are issued Equity Shares in AakashGanga Ltd. worth Rs. 4,00,000 in lieu of their present holdings.
- (vi) Secured Loan agree to continue the balance amount of their loans to AakashGanga Limited after adjusting realizable value of pledged asset in case of Aakash Limited and after waiving 50% of interest due in the case of Ganga Limited.
- (vii) Unsecured Loans are taken over by AakashGanga Limited at 25% of loan amounts.
- (viii) Employees are issued fully paid Equity Shares in AakashGanga Limited in full settlement of their dues.
- (ix) Statutory Liabilities are taken over by AakashGanga Limited at full value and Trade Payables are taken over at 80% of the book value.

You are required to prepare the opening Balance Sheet of AakashGanga Limited as at 1.4.2021.

(RTP May 22)

Answer :

Balance sheet of Aakash Ganga Ltd. as at 1st April, 2021

Particulars	Note No.	(Rs.)
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Share Capital	1	1,40,00,000
(2) Non-Current Liabilities		
(a) Long term borrowings	2	2,12,60,000
(3) Current Liabilities		
(a) Trade Payables	3	73,60,000
(b) Other current liabilities	4	1,64,00,000
Total		5,90,20,000
II. Assets		
(1) Non-current assets		
(a) Property, Plant & Equipment	5	2,04,00,000
(b) Intangible assets	6	1,54,20,000
(2) Current assets		
(a) Cash and cash equivalents		40,00,000
(b) Other current assets	7	1,92,00,000
Total		5,90,20,000

Notes to Accounts

			(Rs.)
1.	Share Capital		
	Issued, subscribed & Paid up:		
	14,00,000 equity shares of Rs. 10 each, fully paid up (W.N.4) (of the above 10,00,000 shares have been issued for consideration other than cash)		1,40,00,000
2.	Long Term borrowings		
	Secured Loans		
	Aakash Limited 25,60,000		
	Ganga Limited 1,44,00,000	1,69,60,000	
	Unsecured Loans	43,00,000	2,12,60,000
3.	Trade Payables (W.N.1)		
	Aakash Limited	44,80,000	
	Ganga Limited	28,80,000	73,60,000
4.	Other current liabilities		
	Statutory Liabilities		
	Aakash Limited	1,44,00,000	
	Ganga Limited	20,00,000	1,64,00,000
5.	Property, Plant & Equipment		
	Aakash Limited	68,00,000	
	Ganga Limited	1,36,00,000	2,04,00,000
6.	Intangible assets		
	Goodwill (W.N.3)		1,54,20,000
7.	Other Current Assets		
	Aakash Limited	57,60,000	
	Ganga Limited	1,34,40,000	1,92,00,000

Working Notes:

1. Value of total liabilities taken over by Aakash Ganga Ltd. (Rs.)

	Aakash Limited		Ganga Limited	
Current liabilities				
Statutory liabilities	1,44,00,000		20,00,000	
Liability to employees	60,00,000		36,00,000	
Trade payables @ 80%	44,80,000	2,48,80,000	28,80,000	84,80,000
Secured loans				
Given in Balance Sheet	3,20,00,000		1,60,00,000	

Interest waived	-		16,00,000	1,44,00,000
Value of Inventory (80% of Rs. 3,68,00,000)	2,94,40,000	25,60,000		
Unsecured Loans (25% of Rs.1,72,00,000)		43,00,000		-
		3,17,40,000		2,28,80,000

2. Assets taken over by AakashGanga Ltd. (Rs.)

	Aakash Limited	Ganga Limited
	Rs.	Rs.
Property, Plant & Equipment	68,00,000	1,36,00,000
Current Assets (80% and 70% respectively of book value)	57,60,000	1,34,40,000
	1,25,60,000	2,70,40,000

3. Goodwill / Capital Reserve on amalgamation (Rs.)

Liabilities taken over (W.N. 1)		3,17,40,000	2,28,80,000
Equity shares to be issued to Preference Shareholders		4,00,000	-
	A	3,21,40,000	2,28,80,000
Less: Total assets taken over (W.N. 2)	B	(1,25,60,000)	(2,70,40,000)
	A-B	1,95,80,000	(41,60,000)
		Goodwill	Capital Reserve
Net Goodwill (1,95,80,000- 41,60,000)		1,54,20,000	

4. Equity shares issued by AakashGanga Ltd.

		Rs.	Rs.
(i)	For Cash		40,00,000
	For consideration other than cash		
(ii)	In Discharge of Liabilities to Employees	96,00,000	
(iii)	To Preference shareholders	4,00,000	1,00,00,000
			1,40,00,000
	No. of shares @ Rs. 10		14,00,000

5. Journal Entries in the Books of Z Ltd.

		Rs.	Rs.
(i)	Equity Share Capital (Rs. 10 each) A/c	Dr.	50,00,000
	To Equity Share Capital (Rs. 5 each) A/c		25,00,000
	To Reconstruction A/c		25,00,000
	(Being conversion of 5,00,000 equity shares of Rs. 10 each fully paid into same number of fully paid equity shares of Rs. 5 each as per scheme of reconstruction.)		

(ii)	9% Preference Share Capital (Rs. 100 each) A/c	Dr.	20,00,000	
	To 10% Preference Share Capital (Rs. 50 each) A/c			10,00,000
	To Reconstruction A/c			10,00,000
	(Being conversion of 9% preference share of Rs. 100 each into same number of 10% preference share of Rs. 50 each and claims of preference dividends settled as per scheme of reconstruction.)			
(iii)	10% Secured Debentures A/c	Dr.	9,60,000	
	Trade payables A/c	Dr.	1,00,000	
	Interest on Debentures payable A/c	Dr.	96,000	
	Bank A/c	Dr.	1,00,000	
	To 12% Debentures A/c			6,78,000
	To Reconstruction A/c			5,78,000
	(Being Rs. 11,56,000 due to Y (including trade payables) cancelled and 12% debentures allotted for the amount after waving 50% as per scheme of reconstruction.)			
(iv)	10% Secured Debentures A/c	Dr.	6,40,000	
	Trade Payables		60,000	
	Interest on debentures payable A/c		64,000	
	Bank A/c		60,000	
	To 12% debentures A/c			4,42,000
	To Reconstruction A/c			3,82,000
	(Being Rs. 7,64,000 due to Z (including trade payables) cancelled and 12% debentures allotted for the amount after waving 50% as per scheme of reconstruction.)			
(v)	Trade payables A/c	Dr.	1,70,000	
	To Reconstruction A/c			1,70,000
	(Being remaining trade payables sacrificed 50% of their claim.)			
(vi)	Directors' Loan A/c	Dr.	1,00,000	
	To Equity Share Capital (Rs. 5) A/c			40,000
	To Reconstruction A/c			60,000
	(Being Directors' loan claim settled by issuing 8,000 equity shares of Rs. 5 each as per scheme of reconstruction.)			
(vii)	Reconstruction A/c	Dr.	15,000	
	To Bank A/c			15,000

	(Being payment made towards penalty of 5% for cancellation of capital commitments of Rs. 3 Lakhs.)			
(viii)	Bank A/c	Dr.	1,00,000	
	To Reconstruction A/c			1,00,000
	(Being refund of fees by directors credited to reconstruction A/c.)			
(ix)	Reconstruction A/c	Dr.	15,000	
	To Bank A/c			15,000
	(Being payment of reconstruction expenses.)			
(x)	Provision for Tax A/c	Dr.	1,00,000	
	To Bank A/c			75,000
	To Reconstruction A/c			25,000
	(Being payment of tax liability in full settlement against provision for tax)			
(xi)	Land and Building A/c	Dr.	2,00,000	
	To Reconstruction A/c			2,00,000
	(Being appreciation in value of Land & Building recorded)			
(xii)	Reconstruction A/c	Dr.	49,85,000	
	To Goodwill A/c			11,00,000
	To Patent A/c			5,00,000
	To Profit and Loss A/c			14,60,000
	To Plant and Machinery A/c			6,50,000
	To Furniture & Fixture A/c			1,00,000
	To Trade Investment A/c			50,000
	To Inventory A/c			2,50,000
	To Trade Receivables A/c			1,00,000
	To Capital Reserve (bal. fig.)			7,75,000
	(Being writing off of losses and reduction in the value of assets as per scheme of reconstruction, balance of reconstruction A/c transfer to Capital Reserve.)			

Bank Account

	Rs.		Rs.
To Reconstruction (Y)	1,00,000	By Balance b/d (overdraft)	1,00,000
To Reconstruction(Z)	60,000	By Reconstruction A/c	15,000
To Reconstruction A/c (refund of earlier fees by directors)	1,00,000	(capital commitment penalty paid)	

		By Reconstruction A/c (reconstruction expenses paid)	15,000
		By Provision for tax A/c (tax paid)	75,000
		By Balance c/d	55,000
	2,60,000		2,60,000

Reconstruction Account

	Rs.		Rs.
To Bank (penalty)	15,000	By Equity Share Capital A/c	25,00,000
To Bank (reconstruction expenses)	15,000		
To Goodwill	11,00,000	By 9% Pref. Share Capital A/c	10,00,000
To Patent	5,00,000		
To P & L A/c	14,60,000	By Mr. Y (Settlement)	5,78,000
To P & M	6,50,000	By Mr. Z (Settlement)	3,82,000
To Furniture and Fixtures	1,00,000	By Trade Payables A/c	1,70,000
To Trade investment	50,000	By Director's loan	60,000
To Inventory	2,50,000	By Bank	1,00,000
To Trade Receivables	1,00,000	By Provision for tax	25,000
To Capital Reserve (bal. fig.)	7,75,000	By Land and Building	2,00,000
	50,15,000		50,15,000

Question 4

The balance sheets of Truth Limited and Myth Limited as at 31.03.2021 is given below. Myth Limited is to be amalgamated with Truth Limited from 1.04.2021. The amalgamation is to be carried out in the nature of purchase

Particulars	Note No.	Truth Ltd. (₹)	Myth Ltd. (₹)
(1) Equity and Liabilities			
1. Shareholders' Funds			
(a) Share Capital	1	10,00,000	4,00,000
(b) Reserves and Surplus	2	11,35,000	4,13,000
2. Non -Current Liabilities	3	-	1,50,000
3. Current Liabilities	4	1,40,000	1,82,000
Total		22,75,000	11,45,000
(2) Assets			
1. Non -Current Assets			
(a) Property, Plant & Equipment		15,75,000	6,80,000
(b) Investments		1,87,500	1,00,000

2. Current Assets	5	5,12,500	3,65,000
Total		22,75,000	11,45,000

Note No.	Particulars	Truth Limited (₹)	Myth Limited (₹)
1	Share Capital	10,00,000	4,00,000
	Equity shares of ₹ 10 each		
2	Reserves & Surplus		
	General Reserve	5,05,000	2,30,000
	Profit & Loss A/c	4,45,000	1,58,000
	Export Profit Reserve	1,85,000	25,000
3	Non- Current Liabilities	11,35,000	4,13,000
	14% Debentures	---	1,50,000
4	Current Liabilities		
	Trade Payables	90,000	1,42,000
	Other Current Liabilities	50,000	40,000
5	Current Assets	1,40,000	1,82,000
	Inventory	2,15,000	85,000
	Trade Receivables	2,02,500	1,75,000
	Cash and Cash equivalents	95,000	1,05,000
		5,12,500	3,65,000

Truth Limited would issue 12% debentures to discharge the claim of the debenture holders of Myth Limited so as to maintain their present annual interest income. Non-trade investment, which constitute 80% of their respective total investments yielded income of 20% to Truth Limited and 15% to Myth Limited. This income is to be deducted from profits while computing average profit for the purpose of calculating goodwill. Profit before tax of both the companies during the last 3 years were as follows:

	Truth Limited (₹)	Myth Limited (₹)
2018-2019	8,20,000	2,55,000
2019-2020	7,45,000	2,15,000
2020-2021	6,04,000	2,14,000

Goodwill is to be calculated on the basis of simple average of three years profit by using Capitalization method taking 18% as normal rate of return. Ignore taxation. Purchase consideration is to be discharged by Truth Limited on the basis of intrinsic value per share. Prepare Balance Sheet of Truth Limited after the amalgamation.

(RTP Nov'22)

Answer :

Balance Sheet of Truth Ltd. (after amalgamated with Myth Ltd.) as at 1.4.2021

Particulars	Note No.	(₹)
I. Equity and liabilities		
(1) Shareholder's funds		
(a) Share capital	1	13,13,750
(b) Reserves and surplus	2	20,76,250
(2) Non-current liabilities		
12% Debentures	3	1,75,000
(3) Current liabilities		
(a) Trade payables	4	2,32,000
(b) Other current liabilities	5	90,000
Total		38,87,000
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment	6	22,55,000
(b) Intangible assets (Goodwill) [WN 1]		4,67,000
(c) Non-current investments	7	2,87,500
(2) Current assets		
(a) Inventories (2,15,000 + 85,000)		3,00,000
(b) Trade receivables (2,02,500 + 1,75,000)		3,77,500
(c) Cash & cash equivalents (95,000 + 1,05,000)		2,00,000
Total		38,87,000

Notes to Accounts

		(₹)	(₹)
1.	Share Capital		
	1,31,375 Equity Shares of ₹ 10 each [1,00,000 + 31,375]		13,13,750
	(of the above shares, 31,375 shares were issued to the vendors otherwise than for cash)		
2.	Reserves and surplus		
	General Reserve	5,05,000	
	Profit and Loss A/c	4,45,000	
	Securities Premium [31,375 x 30]	9,41,250	
	Export profit reserve 1,85,000		
	Add: Balance of Myth Ltd. 25,000	2,10,000	

	Amalgamation Adjustment Reserve	(25,000)	20,76,250
3.	Long Term Borrowings		
	12% Debentures issued to Myth Ltd.		1,75,000
4.	Trade payables		
	Trade payables	90,000	
	Add: Taken over	1,42,000	2,32,000
5	Other Current Liabilities		
	Truth Ltd.	50,000	
	Myth Ltd.	40,000	90,000
6.	Property, Plant & Equipment		
	Truth Ltd.	15,75,000	
	Myth Ltd.	6,80,000	22,55,000
7.	Investment		2,87,500
	Truth Ltd.	1,87,500	
	Myth Ltd.	1,00,000	

Working Notes:

(1) Valuation of Goodwill

(i) Capital Employed

	Truth Ltd.		Myth Ltd.	
	₹	₹	₹	₹
Assets as per Balance Sheet		22,75,000		11,45,000
Less: Non-trade Investment		(1,50,000)		(80,000)
		21,25,000		10,65,000
Less: Liabilities:				
14% Debentures	-		1,50,000	
Trade payables	90,000		1,42,000	
Other current liabilities	50,000	(1,40,000)	40,000	(3,32,000)
Capital Employed		19,85,000		7,33,000

(ii) Average Profit before Tax

	Truth Ltd.		Myth Ltd.	
2018-2019		8,20,000		2,55,000
2019-2020		7,45,000		2,15,000
2020- 2021		6,04,000		2,14,000
Total profit of 3 years (a)		21,69,000		6,84,000
Simple Average [(a)/3]		7,23,000		2,28,000
Less: Non-trading income*		(30,000)		(12,000)

(iii) Goodwill		6,93,000		2,16,000
Capitalized value of average profit	$[(6,93,000 / 18) \times 100]$	38,50,000	$[(2,16,000 / 18) \times 100]$	12,00,000
Less: Capital Employed [From (i) above]		(19,85,000)		(7,33,000)
Goodwill		18,65,000		4,67,000

* For Truth Ltd. = $1,87,500 \times 80\% \times 20\% = 30,000$; and

Myth Ltd. = $1,00,000 \times 80\% \times 15\% = 12,000$

(2) Intrinsic Value per Share

	Truth Ltd.		Myth Ltd.	
		₹		₹
Goodwill [W.N. 1]	18,65,000		4,67,000	
Other Assets	22,75,000	41,40,000	11,45,000	16,12,000
Less: Liabilities				
12% Debentures	-		1,75,000**	
Trade payables	90,000		1,42,000	
Provision for Tax	50,000	(1,40,000)	40,000	(3,57,000)
Net Assets		40,00,000		12,55,000
Intrinsic value per share [Net Assets / No. of Shares]		$40,00,000 / 1,00,000$		$12,55,000 / 40,000$
		= ₹ 40		= ₹ 31.375

** $1,50,000 \times 14\% / 12\% = 1,75,000$

(3) Purchase Consideration & manner of its discharge

Intrinsic Value of Myth Ltd. [a]	₹ 31.375 per share
No. of shares [b]	40,000 shares
Purchase Consideration c= [a x b]	₹ 12,55,000
Intrinsic Value of Truth Ltd. [d]	₹ 40 per share
No. of shares to be issued [c / d]	31,375 shares

Question 5

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	7,00,000
Inventories	10,40,000	5,20,000
Trade Receivables	8,20,000	3,00,000
Cash and Bank	3,00,000	
	71,80,000	43,80,000

B Ltd. is to declare and 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.

- The authorized share capital of Z Ltd. is ₹ 60 lakhs divided into ₹ 6 lakhs equity shares of ₹ 10 each.
- As per Registered Valuer the value of equity shares of A Ltd. is ₹ 18 per share and of B Ltd. is ₹ 12 per share respectively and agreed by respective shareholders of the companies.
- 10% Debentures of A Ltd. to be issued 12% Debentures of Z Ltd. at par in consideration of their holdings.
- A contingent liability of A Ltd. of ₹ 2,00,000 is to be treated as actual liability.
- Liquidation expenses including Registered Valuer fees of A Ltd. ₹ 50,000 and B Ltd. ₹ 30,000 respectively to be borne by Z Ltd.
- 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. (PYP May'22)

Answer :

Journal Entries in the books of Z Ltd.

		₹	₹
Business Purchase A/c	Dr.	54,00,000	54,00,000
To Liquidator of A Ltd. A/c			
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 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 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 in the above Solution:

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 and 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 ¹	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) 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
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

¹ 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	
		3,60,000	
	Less: Liquidation Expenses	(80,000)	2,80,000

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



5. INTERNAL RECONSTRUCTION

ILLUSTRATIONS

Illustration 1

On 31-12-20X1, B Ltd. had 20,000, Rs. 10 Equity Shares as authorized capital and the shares were all issued on which Rs. 8 was paid up. In June, 20X2 the company in general meeting decided to sub-divide each share into two shares of Rs. 5 with Rs. 4 paid up. In June, 20X3 the company in general meeting resolved to consolidate 20 shares of Rs. 5, Rs. 4 per share paid up into one share of Rs. 100 each, Rs. 80 paid up.

Pass entries and show how share capital will appear in notes to Balance Sheet as on 31-12-20X1, 31-12-20X2 and 31-12-20X3.

Solution:

Journal Entries

20X2			Rs.	Rs.
June	Equity Share Capital (Rs. 10) A/c Dr. To Equity Share Capital (Rs. 5) A/c (Being the sub-division of 20,000 shares of Rs. 10 each with Rs. 8 paid up into 40,000 shares Rs. 5 each with Rs. 4 paid up by reSolution: in general meeting dated)		1,60,000	1,60,000
20X3	Equity Share Capital (Rs. 5) A/c Dr.		1,60,000	
June	To Equity Share Capital (Rs. 100) A/c (Being consolidation of 40,000 shares of Rs. 5 with Rs. 4 paid up into 2,000 Rs. 100 shares with Rs. 80 paid up)			1,60,000

Notes to Balance Sheet

Liabilities:	Rs.
As on 31-12-20X1	
1. Share Capital	
Authorized:	
20,000 Equity Shares of Rs. 10 each	<u>2,00,000</u>
Issued, Subscribed and Paid up:	
20,000 Equity Shares of Rs. 10 each Rs. 8 per share paid up	1,60,000
As on 31-12-20X2	
1. Share Capital	
Authorized:	
40,000 Equity Shares of Rs. 5 each	<u>2,00,000</u>

Issued, Subscribed and Paid up:	
40,000 Equity Shares of Rs. 5 each Rs. 4 per share paid up	1,60,000
As on 31-12-20X3	Rs.
1. Share Capital	
Authorized:	
2,000 Equity Shares of Rs. 100 each	<u>2,00,000</u>
Issued, Subscribed and Paid up:	
2,000 Equity Shares of Rs. 100 each Rs. 80 per share paid up	1,60,000

Note: Some accountants prefer not to make any entry as the amount remains same. Even when an entry is passed it applies only to the called-up portion, and not to uncalled or unissued portion of share capital.

Illustration 2

C Ltd. had Rs. 5,00,000 authorized capital on 31-12-20X1 divided into shares of Rs. 100 each out of which 4,000 shares were issued and fully paid up. In June 20X2 the Company decided to convert the issued shares into stock. But in June, 20X3 the Company re-converted the stock into shares of Rs. 10 each, fully paid up.

Pass entries and show how Share Capital will appear in Notes to Balance Sheet as on 31-12-20X1, 31-12-20X2 and 31-12-20X3.

Solution:



Journal Entries

		Rs.	Rs.
20X2 June	Equity Share Capital A/c Dr. To Equity Stock A/c (Being conversion of 4,000 fully paid Equity Shares of Rs. 100 into Rs. 4,00,000 Equity Stock as per reSolution: in general meeting dated...)	4,00,000	4,00,000
20X3 June	Equity Stock A/c Dr. To Equity Share Capital A/c (Being re-conversion of Rs. 4,00,000 Equity Stock into 40,000 shares of Rs. 10 fully paid Equity Shares as per reSolution: in General Meeting dated...)	4,00,000	4,00,000

Notes to Balance Sheet

	Rs.
As on 31-12-20X1	
Share Capital	
Authorized	
5,000 Equity Shares of Rs. 100 each	<u>5,00,000</u>
Issued and Subscribed	
4,000 Equity Shares of Rs. 100 each fully called up	4,00,000
As on 31-12-20X2	Rs.
Share Capital	
Authorized	
5,000 Equity Shares of Rs. 100 each	<u>5,00,000</u>
Issued and Subscribed	
Equity Stock- 4,000 Equity Shares of Rs. 100 converted into Stock	4,00,000
As on 31-12-20X3	Rs.
Share Capital	
Authorized	
50,000 Equity Shares of Rs. 10 each	<u>5,00,000</u>
Issued and Subscribed	
40,000 Equity Shares of Rs. 10 each fully called up	4,00,000

Illustration 3

The Balance Sheet of A & Co. Ltd. as at 31-3-20X2 is as follows:

		Particulars	Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	A	Share capital	1	11,50,000
	B	Reserves and Surplus	2	(5,35,000)
2		Non-current liabilities		
	A	Long-term borrowings	3	3,75,000
3		Current liabilities		
	A	Trade Payables		3,00,000
	B	Short term borrowings - Bank Overdraft		1,95,000
	C	Other current liabilities	4	<u>1,22,500</u>
		Total		<u>16,07,500</u>
		Assets		
1		Non-current assets		

	A	Property, plant and equipment	5	4,75,000
	B	Intangible assets	6	1,67,500
	C	Non-current investments	7	55,000
2		Current assets		
	A	Inventories		4,25,000
	B	Trade receivables		<u>4,85,000</u>
		Total		<u>16,07,500</u>

Notes to accounts

		Rs.
1	Share Capital Equity share capital: 75,000 Equity Shares of Rs. 10 each Preference share capital: 4,000 6% Cumulative Preference Shares of Rs. 100 each	 7,50,000 <u>4,00,000</u> <u>11,50,000</u>
2	Reserves and Surplus Debit balance of Profit and loss Account	 <u>(5,35,000)</u> <u>(5,35,000)</u>
3	Long-term borrowings Secured 6% Debentures (secured on the freehold property)	 <u>3,75,000</u> <u>3,75,000</u>
4	Other current liabilities Loan from directors Interest payable on 6% debentures	 1,00,000 <u>22,500</u> <u>1,22,500</u>
5	Property plant and Equipment Freehold property Plant	 4,25,000 <u>50,000</u> <u>4,75,000</u>
6	Intangible assets Goodwill Patents	 1,30,000 <u>37,500</u> <u>1,67,500</u>
7	Non-current investments Investments at cost	 <u>55,000</u> <u>55,000</u>

The Court approved a Scheme of re-organization to take effect on 1-4-20X2, whereby:

- (i) The Preference shares to be written down to Rs. 75 each and Equity Shares to Rs. 2 each.
- (ii) Of the Preference Share dividends which are in arrears for four years, three fourths to be waived and Equity Shares of Rs. 2 each to be allotted for the remaining quarter.
- (iii) Interest payable on debentures to be paid in cash.
- (iv) Debenture-holders agreed to take over freehold property, book value Rs. 1,00,000 at a valuation of Rs. 1,20,000 in part repayment of their holdings and to provide additional cash of Rs. 1,30,000 secured by a floating charge on company's assets at an interest rate of 8% p.a.
- (v) Patents and Goodwill to be written off.
- (vi) Inventory to be written off by Rs. 65,000.
- (vii) Amount of Rs. 68,500 to be provided for bad debts.
- (viii) Remaining freehold property after giving to debenture holders, to be re-valued at Rs.3,87,500.
- (ix) Investments be sold for Rs. 1,40,000.
- (x) Directors to accept settlement of their loans as to 90% thereof by allotment of equity shares of Rs. 2 each and as to 5% in cash, and balance 5% being waived.
- (xi) There were capital commitments totalling Rs. 2,50,000. These contracts are to be cancelled on payment of 5% of the contract price as a penalty.
- (xii) Ignore taxation and cost of the scheme.

You are requested to show Journal entries reflecting the above transactions (including cash transactions) and prepare the Balance Sheet of the company after completion of the Scheme.

Solution:

Journal of A & Co. Ltd.

			Dr. Rs.	Cr. Rs.
20X2 April 1	Equity Share Capital A/c (Rs. 10) To Capital Reduction A/c To Equity Share Capital A/c (Rs. 2) (Reduction of equity shares of Rs. 10 each to shares of Rs. 2 each as per Reconstruction Scheme dated...)	Dr.	7,50,000	6,00,000 1,50,000
"	6% Cum. Preference Share Capital A/c (Rs. 100) To Capital Reduction A/c To Pref. Share Capital A/c (Rs. 75) (Reduction of preference shares of Rs. 100 each to shares of Rs. 75 each as per reconstruction scheme)	Dr.	4,00,000	1,00,000 3,00,000
"	Capital Reduction Account To Equity Share Capital Account	Dr.	24,000	24,000

	(Arrears of preference dividends satisfied by the issue of equity shares, 25% of the amount due, Rs. 96,000)															
"	Freehold Property A/c To Capital Reduction A/c (Appreciation in the value of property: <table><tr><td></td><td>Book value</td><td>Revalued Figure</td></tr><tr><td></td><td>Rs. 1,00,000</td><td>Rs. 1,20,000</td></tr><tr><td></td><td><u>Rs. 3,25,000</u></td><td><u>Rs. 3,87,500</u></td></tr><tr><td>Total</td><td>Rs. 4,25,000</td><td>Rs. 5,07,500</td></tr></table> Profit on revaluation: Rs. 82,500)		Book value	Revalued Figure		Rs. 1,00,000	Rs. 1,20,000		<u>Rs. 3,25,000</u>	<u>Rs. 3,87,500</u>	Total	Rs. 4,25,000	Rs. 5,07,500	Dr.	82,500	82,500
	Book value	Revalued Figure														
	Rs. 1,00,000	Rs. 1,20,000														
	<u>Rs. 3,25,000</u>	<u>Rs. 3,87,500</u>														
Total	Rs. 4,25,000	Rs. 5,07,500														
"	6% Debentures A/c To Freehold Property A/c (Claims of debenture-holders, in part, in respect of principal discharged by transfer of freehold property vide Scheme of Reconstruction)	Dr.	1,20,000	1,20,000												
"	Interest payable A/c To Bank A/c (Debenture interest paid)	Dr.	22,500	22,500												
"	Bank A/c To 8% Debentures A/c (8% Debentures issued for cash)	Dr.	1,30,000	1,30,000												
"	Bank A/c To Investment A/c To Capital Reduction A/c (Sale of Investment for Rs. 1,40,000 cost being Rs. 55,000; profit credited to Capital Reduction Account)	Dr.	1,40,000	55,000 85,000												
"	Directors' Loan A/c To Equity Share Capital A/c	Dr.	1,00,000	90,000												
	To Bank A/c			5,000												
	To Capital Reduction A/c			5,000												
	(Directors' loan discharged by issue of equity shares of Rs. 90,000, cash payments of Rs. 5,000 and surrender of Rs. 5,000, vide Scheme of Reconstruction)															

	Capital Reduction A/c	Dr.	8,48,500	
	To Patents			37,500
	To Goodwill			1,30,000
	To Inventory			65,000
	To Provision for Doubtful Debts			68,500
	To Bank			12,500
	To Profit & Loss Account			5,35,000
	(Writing off patents, goodwill, profit and loss account and reducing the value of stock, making the required provision for doubtful debts and payment for cancellation of capital commitments)			

Note: Penalty charges for cancellation of the contract amounts to Rs. 12,500 (2,50,000X5%) being paid in cash.

Balance Sheet of A & Co. Ltd. (And Reduced) as at 1st April, 20X2

		Particulars	Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	A	Share capital	1	5,64,000
2		Non-current liabilities		
	A	Long-term borrowings	2	3,85,000
3		Current liabilities		
	A	Trade Payables		<u>3,00,000</u>
		Total		<u>12,49,000</u>
		Assets		
1		Non-current assets		
	A	Property, plant and equipment	3	4,37,500
	B	Intangible assets	4	-
2		Current assets		
	A	Inventories		3,60,000
	B	Trade receivables	5	4,16,500
	C	Cash and cash equivalents		<u>35,000</u>
		Total		<u>12,49,000</u>

Notes to accounts

1	Share Capital		
	Equity share capital		
	1,32,000 Equity shares of Rs. 2 each (of the above 57,000		2,64,000

	shares have been issued for consideration other than cash)		
	Preference share capital		
	4,000 6% Preference shares of Rs. 75 each		<u>3,00,000</u>
	Total		<u>5,64,000</u>
2	Long-term borrowings		
	Secured		
	6% Debentures		2,55,000
	8% Debentures		<u>1,30,000</u>
	Total		<u>3,85,000</u>
3	Property, plant and equipment		
	Freehold property	4,25,000	
	Add: Appreciation under scheme of Reconstruction	82,500	
	Less: Disposed of	<u>(1,20,000)</u>	3,87,500
	Plant		<u>50,000</u>
	Net carrying value		<u>4,37,500</u>
4	Intangible assets		
	Goodwill	1,30,000	
	Less: Written off under scheme of Reconstruction	<u>(1,30,000)</u>	NIL
	Net carrying value		
	Patents	37,500	
	Less: Written off under scheme of Reconstruction	<u>(37,500)</u>	-
	Net carrying value	-	<u>NIL</u>
5	Trade Receivables	4,85,000	
	Less: Provision for doubtful debts	<u>68,500</u>	
			<u>4,16,500</u>

Illustration 4

Given below is the Balance sheet of Rebuilt Ltd. as at 31.3.20X1:

		Particulars	Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	A	Share capital	1	13,50,000
	B	Reserves and Surplus	2	(4,51,000)
2		Non-current liabilities		
	A	Long-term borrowings (Loan)	3	5,73,000

3		Current liabilities		
	A	Trade Payables		2,07,000
	B	Other current liabilities		<u>35,000</u>
		Total		<u>17,14,000</u>
		Assets		
		Non-current assets		
1	A	Property, plant and equipment		6,68,000
	B	Intangible assets	4	3,18,000
			5	
		Current assets		
	A	Inventories		4,00,000
2	B	Trade receivables		<u>3,28,000</u>
		Total		<u>17,14,000</u>

Notes to accounts

		Rs.
1	Share Capital	
	<u>Equity share capital</u>	7,50,000
	15,000 Equity Shares of Rs. 50 each	
	<u>Preference share capital</u>	
	12,000, 7% Cumulative Preference Shares of Rs. 50 each	
	(Preference dividend is in arrears for five years)	<u>6,00,000</u>
	Total	<u>13,50,000</u>
2	Reserves and Surplus	
	Debit balance of Profit and loss Account	<u>(4,51,000)</u>
		<u>(4,51,000)</u>
3	Long-term borrowings	
	Loan	<u>5,73,000</u>
		<u>5,73,000</u>
4	Property, plant and Equipment	
	Building at cost less depreciation	4,00,000
	Plant at cost less depreciation	<u>2,68,000</u>
		<u>6,68,000</u>
5	Intangible assets	
	Trademarks and Goodwill at cost	<u>3,18,000</u>
		<u>3,18,000</u>

The Company is not earning profits, short of working capital and a scheme of reconstruction has been approved by both the classes of shareholders. A summary of the scheme is as follows:

- (a) The equity shareholders have agreed that their Rs. 50 shares should be reduced to Rs. 2.50 by cancellation of Rs. 47.50 per share. They have also agreed to subscribe for three new equity shares of Rs. 2.50 each for each equity share held.
- (b) The preference shareholders have agreed to cancel the arrears of dividends and to accept for each Rs. 50 share, 4 new 5% preference shares of Rs. 10 each, plus 6 new equity shares of Rs. 2.50 each, all credited as fully paid.
- (c) Lenders to the company for Rs. 1,50,000 have agreed to convert their loan into share and for this purpose they will be allotted 12,000 new preference shares of Rs. 10 each and 12,000 new equity shares of Rs. 2.50 each.
- (d) The directors have agreed to subscribe in cash for 40,000, new equity shares of Rs. 2.50 each in addition to any shares to be subscribed by them under (a) above.
- (e) Of the cash received by the issue of new shares, Rs. 2,00,000 is to be used to reduce the loan due by the company.
- (f) The equity share capital cancelled is to be applied:
 - i. to write off the debit balance in the profit and loss A/c; and
 - ii. to write off Rs. 35,000 from the value of plant.

Any balance remaining is to be used to write down the value of trademarks and goodwill.

Show by journal entries how the financial books are affected by the scheme and prepare the balance sheet of the company after reconstruction. The nominal capital as reduced is to be increased to Rs. 6,50,000 for preference share capital and Rs. 7,50,000 for equity share capital.

Solution:

In the books of Rebuilt Ltd.

Journal Entries

	Particulars		Debit (Rs.)	Credit (Rs.)
1.	Equity share capital A/c (Rs. 50) To Equity share capital A/c (Rs. 2.50) To Capital reduction A/c (Being equity capital reduced to nominal value of Rs. 2.50 each)	Dr.	7,50,000	37,500 7,12,500
2.	Bank A/c To Equity share capital (Being 3 right shares against each share was issued and subscribed)	Dr.	1,12,500	1,12,500
3.	7% Preference share capital A/c (Rs. 50)	Dr.	6,00,000	

	Capital reduction A/c To 5% Preference share capital (Rs. 10) To equity share capital (Rs. 50) (Being 7% preference shares of Rs. 50 each converted to 5% preference shares of Rs. 10 each and also given to them 6 equity shares for every share held)	Dr.	60,000	4,80,000 1,80,000
4.	Loan A/c To 5% Preference share capital A/c To Equity share capital A/c (Being loan to the extent of Rs. 1,50,000 converted into share capital)	Dr.	1,50,000	1,20,000 30,000
5.	Bank A/c To Equity share application money A/c (Being shares subscribed by the directors)	Dr.	1,00,000	1,00,000
6.	Equity share application money A/c To Equity share capital A/c (Being application money transferred to capital A/c)	Dr.	1,00,000	1,00,000
7.	Loan A/c To Bank A/c (Being loan repaid)	Dr.	2,00,000	2,00,000
8.	Capital reduction A/c To Profit and loss A/c To Plant A/c To Trademarks and Goodwill A/c (Bal.fig.) (Being losses and assets written off to the extent required)	Dr.	6,52,500	4,51,000 35,000 1,66,500

Balance sheet of Rebuilt Ltd. (and reduced) as at 31.3.20X1

		Particulars	Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	a	Share capital	1	10,60,000
2		Non-current liabilities		
	a	Long-term borrowings		2,23,000
3		Current liabilities		
	a	Trade Payables		2,07,000
	b	Other current liabilities		<u>35,000</u>
		Total		<u>15,25,000</u>

1	Assets		
	Non-current assets		
a	Property, plant and equipment	2	6,33,000
b	Intangible assets	3	1,51,500
2	Current assets		
a	Inventories		4,00,000
b	Trade receivables		3,28,000
c	Cash and cash equivalents	4	<u>12,500</u>
	Total		<u>15,25,000</u>

Notes to accounts

			Rs.
1.	Share Capital		
	Authorized capital:		
	65,000 Preference shares of Rs. 10 each	6,50,000	
	3,00,000 Equity shares of Rs. 2.50 each	7,50,000	<u>14,00,000</u>
	Issued, subscribed and paid up:		
	1,80,000 equity shares of Rs. 2.5 each	4,60,000	
	60,000, 5% Preference shares of Rs. 10 each	<u>6,00,000</u>	10,60,000
2.	Property plant and equipment		
	Building at cost less depreciation	4,00,000	
	Plant at cost less depreciation	<u>2,33,000</u>	6,33,000
3.	Intangible assets		
	Trademarks and goodwill		1,51,500
4.	Cash and cash equivalents		
	Bank (1,12,500+1,00,000-2,00,000)		12,500

Illustration 5

Vaibhav Ltd. gives the following ledger balances as at 31st March 20X1:

	Rs.
Property, Plant and Equipment	2,50,00,000
Investments (Market-value Rs. 19,00,000)	20,00,000
Current Assets	2,00,00,000
P & L A/c (Dr. balance)	12,00,000
Share Capital: Equity Shares of Rs. 100 each	2,00,00,000
6%, Cumulative Preference Shares of Rs. 100 each	1,00,00,000
5% Debentures of Rs. 100 each	80,00,000
Creditors	1,00,00,000
Provision for taxation	2,00,000

The following scheme of Internal Reconstruction is sanctioned:

- i) All the existing equity shares are reduced to Rs. 40 each.
- ii) All preference shares are reduced to Rs. 60 each.
- iii) The rate of Interest on Debentures increased to 6%. The Debenture holders surrender their existing debentures of Rs. 100 each and exchange the same for fresh debentures of Rs. 70 each for every debenture held by them.
- iv) Property, Plant and Equipment is to be written down by 20%.
- v) Current assets are to be revalued at Rs. 90,00,000.
- vi) Investments are to be brought to their market value.
- vii) One of the creditors of the company to whom the company owes Rs. 40,00,000 decides to forgo 40% of his claim. The creditor is allotted with 60000 equity shares of Rs. 40 each in full and final settlement of his claim.
- viii) The taxation liability is to be settled at Rs. 3,00,000.
- ix) It is decided to write off the debit balance of Profit & Loss A/c.

Pass journal entries and show the Balance Sheet of the company after giving effect to the above.

Solution:

Journal Entries in the books of Vaibhav Ltd.

		Rs.	Rs.
(i)	Equity share capital (Rs. 100) A/c Dr. To Equity Share Capital (Rs. 40) A/c To Capital Reduction A/c (Being conversion of equity share capital of Rs. 100 each into Rs.40 each as per reconstruction scheme)	2,00,00,000	80,00,000 1,20,00,000
(ii)	6% Cumulative Preference Share capital (Rs. 100) A/c Dr. To 6% Cumulative Preference Share Capital (Rs. 60)A/c To Capital Reduction A/c (Being conversion of 6% cumulative preference shares capital of Rs. 100 each into Rs. 60 each as per reconstruction scheme)	1,00,00,000	60,00,000 40,00,000
(iii)	5% Debentures (Rs. 100) A/c Dr. To 6% Debentures (Rs. 70) A/c To Capital Reduction A/c (Being 6% debentures of Rs. 70 each issued to existing 5% debenture holders. The balance transferred to capital reduction account as per reconstruction scheme)	80,00,000	56,00,000 24,00,000
(iv)	Sundry Creditors A/c Dr. To Equity Share Capital (Rs. 40) A/c	40,00,000	24,00,000

	To Capital Reduction A/c (Being a creditor of Rs. 40,00,000 agreed to surrender his claim by 40% and was allotted 60,000 equity shares of Rs. 40 each in full settlement of his dues as per reconstruction scheme)		16,00,000
(v)	Provision for Taxation A/c Dr. Capital Reduction A/c Dr. To Liability for Taxation A/c (Being conversion of the provision for taxation into liability for taxation for settlement of the amount due)	2,00,000 1,00,000	3,00,000
(vi)	Capital Reduction A/c Dr. To P & L A/c To Property, Plant and Equipment A/c To Current Assets A/c To Investments A/c To Capital Reserve A/c (Bal. fig.) (Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) Balance, PPE, Current Assets, Investments and the Balance transferred to Capital Reserve)	199,00,000	12,00,000 50,00,000 110,00,000 1,00,000 26,00,000
(vii)	Liability for Taxation A/c Dr. To Current Assets (Bank A/c) (Being the payment of tax liability)	3,00,000	3,00,000

Balance Sheet of Vaibhav Ltd. (and reduced) as at 31st March, 20X1

Particulars		Notes	Rs.
1	Equity and Liabilities		
a	Shareholders' funds		
a	Share capital	1	164,00,000
b	Reserves and Surplus	2	26,00,000
2	Non-current liabilities		
	Long-term borrowings	3	56,00,000
3	Current liabilities		
	Trade Payables (1,00,00,000 less 40,00,000)		60,00,000
	Total		3,06,00,000
1	Assets		
a	Non-current assets		
a	Property, plant and equipment	4	2,00,00,000

b	Investments	5	19,00,000
2	Current assets	6	87,00,000
	Total		3,06,00,000

Notes to accounts

			Rs.
1.	Share Capital		
	Equity share capital		
	Issued, subscribed and paid up		
	2,60,000 equity shares of Rs. 40 each		
	(of the above 60,000 shares have been issued for consideration other than cash)		1,04,00,000
	Preference share capital		
	Issued, subscribed and paid up		
	1,00,000 6% Cumulative Preference shares of Rs. 60 each		60,00,000
	Total		1,64,00,000
2.	Reserves and Surplus		
	Capital Reserve		<u>26,00,000</u>
3.	Long-term borrowings		
	Secured		
	6% Debentures		<u>56,00,000</u>
4.	Property, Plant and Equipment		
	Carrying value	2,50,00,000	
	Adjustment under scheme of reconstruction	(50,00,000)	<u>2,00,00,000</u>
5.	Investments		
		20,00,000	
	Adjustment under scheme of reconstruction	<u>(1,00,000)</u>	<u>19,00,000</u>
6.	Current assets		
		2,00,00,000	
	Adjustment under scheme of reconstruction	<u>(1,10,00,000)</u>	
		90,00,000	
	Taxation liability paid	<u>(3,00,000)</u>	<u>87,00,000</u>

Working Note:

Capital Reduction Account

To	Liability for taxation A/c	1,00,000	By	Equity share capital	1,20,00,000

To	P & L A/c	12,00,000	By	6% Cumulative preferences	
To	Property, plant and equipment	50,00,000			
To	Current assets	1,10,00,000		Share capital	40,00,000
To	Investment	1,00,000	By	5% Debentures	24,00,000
To	Capital Reserve (Bal. fig.)	<u>26,00,000</u>	By	Sundry creditors	<u>16,00,000</u>
		2,00,00,000			2,00,00,000

Illustration 6

Following is the Balance Sheet of ABC Ltd. as at 31st March, 20X1:

		Particulars	Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	A	Share capital	1	26,00,000
	B	Reserves and Surplus	2	(4,05,000)
2		Non-current liabilities		
	A	Long-term borrowings	3	12,00,000
3		Current liabilities		
	A	Trade Payables		5,92,000
	B	Short term borrowings - Bank overdraft		<u>1,50,000</u>
		Total		<u>41,37,000</u>
1		Assets		
		Non-current assets		
	A	Property, plant and equipment Non-current	4	12,20,000
	B	investment	6	68,000
	C			
2		Current assets		
	A	Inventory		14,00,000
	B	Trade receivables		14,39,000
	C	Cash and cash equivalents		<u>10,000</u>
		Total		<u>41,37,000</u>

Notes to accounts:

		Rs.
1	Share Capital	
	Equity share capital:	
	2,00,000 Equity Shares of Rs. 10 each	20,00,000

	6,000, 8% Preference shares of Rs. 100 each	<u>6,00,000</u>
		<u>26,00,000</u>
2	Reserves and Surplus	
	Debit balance of Profit and loss A/c	<u>(4,05,000)</u>
		<u>(4,05,000)</u>
3	Long-term borrowings	
	9% debentures	<u>12,00,000</u>
		<u>12,00,000</u>
4	Property, Plant and Equipment	
	Plant and machinery	9,00,000
	Furniture and fixtures	<u>3,20,000</u>
		<u>12,20,000</u>
5	Non-current investments	
	Investments (market value of Rs. 55,000)	<u>68,000</u>
		<u>68,000</u>

The following scheme of reconstruction was finalized:

- Preference shareholders would give up 30% of their capital in exchange for allotment of 11% Debentures to them.
- Debenture holders having charge on plant and machinery would accept plant and machinery in full settlement of their dues.
- Inventory equal to Rs. 5,00,000 in book value will be taken over by trade payables in full settlement of their dues.
- Investment value to be reduced to market price.
- The company would issue 11% Debentures for Rs. 3,00,000 and augment its working capital requirement after settlement of bank overdraft.

Pass necessary Journal Entries in the books of the company. Prepare Capital Reduction account and Balance Sheet of the company after internal reconstruction.

Solution:

In the Books of ABC Ltd.

Journal Entries

Particulars	Rs.	Rs.
8% Preference share capital A/c Dr.	6,00,000	
To 11% Debentures A/c		4,20,000
To Capital reduction A/c		1,80,000
[Being 30% reduction in liability of preference share capital and issue of 11% debentures]		

9% Debentures A/c	Dr.	12,00,000	
To Plant & machinery A/c			9,00,000
To Capital reduction A/c			3,00,000
[Settlement of debenture holders by allotment of plant & machinery]			
Trade payables A/c	Dr.	5,92,000	
To Inventory A/c			5,00,000
To Capital reduction A/c			92,000
[Being settlement of creditors by giving Inventories]			
Bank A/c	Dr.	3,00,000	
To 11% Debentures A/c			3,00,000
[Being fresh issue of debentures]			
Bank overdraft A/c	Dr.	1,50,000	
To Bank A/c			1,50,000
[Being settlement of bank overdraft]			
Capital reduction A/c	Dr.	5,72,000	
To Investment A/c			13,000
To Profit and loss A/c			4,05,000
To Capital reserve A/c			1,54,000
[Being decrease in investment and profit and loss account (Dr. bal.); and balance of capital reduction account transferred to capital reserve]			

Capital Reduction Account

	Rs.		Rs.
To Investments A/c	13,000	By Preference share capital A/c	1,80,000
To Profit and loss A/c	4,05,000	By 9% Debenture holders A/c	3,00,000
To Capital reserve A/c	<u>1,54,000</u>	By Trade payables A/c	<u>92,000</u>
	<u>5,72,000</u>		<u>5,72,000</u>

Balance Sheet of ABC Ltd. (And Reduced) As at 31st March 20X1

Particulars	Note No	Rs.
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	20,00,000
(b) Reserves and Surplus	2	1,54,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	7,20,000

Total		28,74,000
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment	4	3,20,000
(b) Non-current investments	5	55,000
(2) Current assets		
(a) Inventories (Rs. 14,00,000 – Rs. 5,00,000)		9,00,000
(b) Trade receivables		14,39,000
(c) Cash and cash equivalents		
Cash at Bank (W. N.)		1,60,000
Total		28,74,000

Notes to Accounts

		Rs.
1.	Share Capital 2,00,000 Equity shares of Rs. 10 each fully paid-up	20,00,000
2.	Reserve and Surplus Capital Reserve	1,54,000
3.	Long Term Borrowings 11% Debentures (Rs. 4,20,000 + Rs. 3,00,000)	7,20,000
4.	Property, Plant and Equipment Plant & machinery 9,00,000 Less: Adjustment on scheme of reconstruction <u>9,00,000</u>	- 3,20,000
5.	Non-Current Investments Investments (Rs. 68,000 – Rs. 13,000)	55,000

Working Note:

Cash at bank = Opening balance + 11% Debentures issued – Bank overdraft paid
= Rs. 10,000 + Rs. 3,00,000 – Rs. 1,50,000 = Rs. 1,60,000

Illustration 7

The Balance Sheet of Revise Limited as at 31st March, 20X1 was as follows :

	Particulars	Notes	Rs.
1	Equity and Liabilities Shareholders' funds		

2	A	Share capital Reserves and surplus	1	10,00,000
	B	Non-current liabilities	2	(6,00,000)
3		Long-term borrowings		
	A	Current liabilities	3	2,00,000
3		Trade Payables		
	A	Other current liabilities Short term		72,000
	B	provisions	4	24,000
	C		5	<u>24,000</u>
		Total		<u>7,20,000</u>
1		Assets		
		Non-current assets		
2	A	Property, Plant and Equipment	6	1,00,000
		Current assets		
	A	Inventory		3,20,000
	B	Trade receivables		2,70,000
	C	Cash and cash equivalents		<u>30,000</u>
		Total		<u>7,20,000</u>

Notes to accounts

			Rs.
1	Share Capital		
	Equity share capital		
	10,000 Equity Shares of Rs. 100 each		<u>10,00,000</u>
			<u>10,00,000</u>
2	Reserves and Surplus		
	Debit balance of Profit and loss Account		<u>(6,00,000)</u>
			<u>(6,00,000)</u>
3	Long-term borrowings		
	12% debentures		<u>2,00,000</u>
			<u>2,00,000</u>
4	Other current liabilities		
	Interest payable on debentures		<u>24,000</u>
			<u>24,000</u>
5	Short term provisions		
	Provision for taxation		<u>24,000</u>
			<u>24,000</u>
6	Property, Plant and Equipment		

	Machinery		<u>1,00,000</u>
			<u>1,00,000</u>

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

- (a) Each share is sub-divided into ten fully paid up equity shares of Rs. 10 each.
- (b) After sub-division, each shareholder shall surrender to the company 50% of his holding, for the purpose of re-issue to debenture holders and trade payables as necessary.
- (c) Out of shares surrendered, 10,000 shares of Rs. 10 each shall be converted into 12% preference shares of Rs. 10 each, fully paid up.
- (d) The claims of the debenture-holders shall be reduced by 75 per cent. In consideration of the reduction, the debenture holders shall receive preference shares of Rs. 1,00,000 which are converted out of shares surrendered.
- (e) Trade payables claim shall be reduced to 50 per cent, it is to be settled by the issue of equity shares of Rs. 10 each 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.

You are required to show the journal entries giving effect to the above and the resultant Balance Sheet

Solution:

		Dr. Rs.	Cr. Rs.
Equity Share Capital (Rs. 100) A/c	Dr.	10,00,000	
To Share Surrender A/c			5,00,000
To Equity Share Capital (Rs. 10) A/c			5,00,000
(Subdivision of 10,000 equity shares of Rs. 100 each into 1,00,000 equity shares of Rs. 10 each and surrender of 50,000 of such subdivided shares as per capital reduction scheme)			
12% Debentures A/c	Dr.	1,50,000	
Interest payable A/c	Dr.	18,000	
To Reconstruction A/c			1,68,000
(Transferred 75% of the claims of the debenture holders to reconstruction account in consideration of which 12% preference shares are being issued out of share surrender account as per capital reduction scheme)			
Trade payables A/c	Dr.	72,000	
To Reconstruction A/c			72,000

(Transferred claims of the trade payables to reconstruction account, 50% of which is being clear reduction and equity shares are being issued in consideration of the balance)			
Share Surrender A/c	Dr.	5,00,000	
To 12% Preference Share Capital A/c			1,00,000
To Equity Share Capital A/c			36,000
To Reconstruction A/c			3,64,000
(Issued preference and equity shares to discharge the claims of the debenture holders and the trade payables respectively as a per scheme and the balance in share surrender account is being transferred to reconstruction account)			
Reconstruction A/c	Dr.	6,04,000	
To Profit and Loss A/c			6,00,000
To Capital Reserve A/c			4,000
(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 Revise Limited (and reduced) as at...

Particulars	Note No.	Rs.
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	6,36,000
(b) Reserves and Surplus	2	4,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	50,000
(3) Current Liabilities		
(a) Other current liabilities	4	6,000
(b) Short-term provisions	5	24,000
Total		7,20,000
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment	6	1,00,000
(2) Current assets		
(a) Inventories		3,20,000
(b) Trade receivables		2,70,000
(c) Cash and cash equivalents		30,000
Total		7,20,000

Notes to Accounts

		Rs.
1.	Share Capital	
	<u>Equity Share Capital</u>	
	Issued Capital: 53,600 Equity Shares of Rs. 10 each	5,36,000
	<u>Preference Share Capital</u>	
	Preference Shares	1,00,000
	(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)	
		6,36,000
2.	Reserve and Surplus	
	Capital Reserve	4,000
3.	Long-term borrowings	
	Unsecured Loans	
	12% Debentures	50,000
4.	Other current liabilities	
	Interest payable on debentures	6,000
5.	Short-term provisions	
	Provision for Income-tax	24,000
6.	Property, plant and Equipment	
	Machinery	1,00,000

Illustration 8

Recover Ltd. decided to reorganize its capital structure owing to accumulated losses and adverse market condition. The Balance Sheet of the company as on 31st March 20X1 is as follows-

		Particulars	Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	A	Share capital	1	3,50,000
	B	Reserves and surplus	2	(70,000)
2		Non-current liabilities		
	A	Long-term borrowings	3	50,000
3		Current liabilities		
	A	Trade Payables		80,000
	B	Short term Borrowings – Bank overdraft		90,000
	C	Other Current Liabilities (Interest payable on Debentures)		5,000

				<u>5,05,000</u>
		Assets		
1		Non-current assets		
	A	Property, Plant Equipment	4	3,35,000
	B	Intangible assets	5	50,000
	C	Non-current investments	6	40,000
2		Current assets		
	A	Inventories		30,000
	B	Trade receivables		<u>50,000</u>
				<u>5,05,000</u>

Notes to accounts:

1	Share Capital Equity share capital: 20,000 Equity Shares of Rs. 10 each Preference share capital: 15,000 8% Cumulative Preference Shares of Rs. 10 each (preference dividend has been in arrears for 4 years)		Rs.
			2,00,000
			<u>1,50,000</u>
			<u>3,50,000</u>
2	Reserves and surplus Profit and loss account (debit balance)		<u>(70,000)</u> (70,000)
3	Long-term borrowings <u>Secured</u> 10% Debentures (secured on the freehold property)		<u>50,000</u> 50,000
4	Property, Plant and Equipment Freehold property Leasehold property Plant and machinery		1,20,000 85,000 <u>1,30,000</u> <u>3,35,000</u>
5	Intangible assets Goodwill		<u>50,000</u> 50,000
6	Non-current investments Non-Trade investments at cost		<u>40,000</u> 40,000

Subsequent to approval by court of a scheme for the reduction of capital, the following steps were taken:

- i. The preference shares were reduced to Rs. 2.5 per share, and the equity shares to Rs. 1 per share.
- ii. One new equity share of Rs. 1 was issued for the arrears of preferred dividend for past 4 years.
- iii. The debenture holders took over the freehold property at an agreed figure of Rs. 75,000 and paid the balance to the company after deducting the amount due to them.
- iv. Plant and Machinery was written down to Rs. 1,00,000.
- v. Non-trade Investments were sold for Rs. 32,000.
- vi. Goodwill and obsolete stock (included in the value of inventories) of Rs. 10,000 were written off.
- vii. A contingent liability of which no provision had been made was settled at Rs. 7,000 and of this amount, Rs. 6,300 was recovered from the insurance.

You are required (a) to show the Journal Entries, necessary to record the above transactions in the company's books and (b) to prepare the Balance Sheet, after completion of the scheme.

Solution:

Journal entries in the books of Recover Ltd

Particulars		Dr. Rs.	Cr. Rs.
8% Cumulative Preference share capital (Rs. 10) A/c To 8% Cumulative Preference share capital (Rs.2.5) A/c To Reconstruction (Rs. 7.5) A/c (Preference shares being reduced to shares of Rs.2.5 per share and remaining transferred to reconstruction account as per internal reconstruction scheme)	Dr.	1,50,000	37,500 1,12,500
Equity share capital A/c (Rs.10) To Equity Share capital A/c (Rs. 1) To Reconstruction A/c (Rs. 9) (Equity shares reduced to Rs. 1 per share with the remaining amount transferred to reconstruction account as a part of the internal reconstruction scheme)	Dr.	2,00,000	20,000 1,80,000
Reconstruction A/c To Equity share capital A/c (Equity shares of Rs. 1 issued in lieu of the arrears of preference dividend for 4 years as a part of the internal reconstruction scheme)	Dr.	48,000	48,000
10% Debentures A/c Interest payable on debentures A/c	Dr. Dr	50,000 5,000	

Bank A/c	Dr.	20,000	
Reconstruction A/c	Dr.	45,000	
To Freehold property A/c			1,20,000
(Debenture holders being paid by the sale of property, which is sold at a loss debited to the reconstruction account. Amount received in excess being refunded to company by debenture holders as a part of the internal reconstruction scheme)			
Reconstruction A/c	Dr.	90,000	
To Plant and Machinery Ac			30,000
To Goodwill A/c			50,000
To Inventory A/c			10,000
(The assets written off as a part of the internal reconstruction scheme)			
Bank A/c	Dr.	32,000	
Reconstruction A/c	Dr.	8,000	
To Investments A/c			40,000
(Investments sold at a loss debited to reconstruction account as a part of the internal reconstruction scheme)			
Contingent Liability A/c	Dr.	7,000	
To Bank A/c			7,000
(Contingent liability paid as a part of the internal reconstruction scheme)			
Bank A/c	Dr.	6,300	
Reconstruction A/c	Dr.	700	
To Contingent Liability A/c			7,000
(The insurance company remitting part of the contingency payment amount)			
Reconstruction A/c	Dr.	70,000	
To Profit and loss A/c			70,000
(Accumulated losses written off to reconstruction account as a part of the internal reconstruction scheme)			
Reconstruction A/c	Dr.	30,800	
To Capital reserve A/c			30,800
(The balance in reconstruction account transferred to capital reserve as a part of the internal reconstruction scheme)			

Balance sheet of Recover Ltd. as at 31st March 20X1 (and reduced)

		Particulars	Notes	Rs.
1		Equity and Liabilities		
		Shareholders' funds		
	A	Share capital	1	1,05,500
	B	Reserves and surplus	2	30,800
2		Non-current liabilities		
	A	Long-term borrowings		-
3		Current liabilities		
	A	Trade Payables		80,000
	B	Short term borrowings - Bank Overdraft		<u>90,000</u>
		Total		<u>3,06,300</u>
		Assets		
1		Non-current assets		
	A	Property, Plant and Equipment	3	1,85,000
2		Current assets		
	A	Inventories		20,000
	B	Trade receivables		50,000
	C	Cash and cash equivalents	4	<u>51,300</u>
		Total		<u>3,06,300</u>

Notes to accounts:

1	Share Capital	Rs.
	Equity share capital	
	68,000 Equity Shares of Rs. 1 each	68,000
	Preference share capital	
	15,000 8% Cumulative Preference Shares of Rs. 2.5 each	<u>37,500</u>
		<u>1,05,500</u>
2	Reserves and surplus	
	Capital reserve	<u>30,800</u>
3	Property, Plant and Equipment	
	Leasehold property	85,000
	Plant and machinery	<u>1,00,000</u>
		<u>1,85,000</u>
4	Cash and cash equivalents	
	Bank A/c (20,000+32,000-7000+6,300)	<u>51,300</u>

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. When the object of reconstruction is usually to re-organise capital or to compound with creditors or to effect economies then such type of reconstruction is called
 - (a) Internal reconstruction with liquidation
 - (b) Internal reconstruction without liquidation of the company
 - (c) External reconstruction
 - (d) None of the above.

2. The accumulated losses under scheme of internal reconstruction are written off against
 - (a) Capital Reduction account
 - (b) Share Capital account
 - (c) Shareholders' account
 - (d) Reserve and surplus.

3. A process of reconstruction, which is carried out without liquidating the company and forming a new one is called
 - (a) Internal reconstruction.
 - (b) External reconstruction.
 - (c) Amalgamation in the nature of merger.
 - (d) Amalgamation in the nature of purchase.

4. Reconstruction is a process by which affairs of a company are reorganized by
 - (a) Revaluation of assets and Reassessment of liabilities.
 - (b) 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.
 - (c) Both (a) and (b).
 - (d) None of the above.

5. For reduction of the share capital, the permission has to be sought from
 - (a) Court.
 - (b) Controller.
 - (c) State government.
 - (d) Shareholders.

6. In case of internal reconstruction
 - (a) Only one company is liquidated.



- (b) Two or more companies are liquidated.
- (c) No company is liquidated.
- (d) Two companies amalgamated.

Answer to Multiple Choice Questions

1.	(b)	2.	(a)	3.	(a)	4.	(c)	5.	(a)	6.	(c)

THEORETICAL QUESTIONS

7. What are the methods of internal reconstruction generally followed by companies?

Answer:

Methods of Internal reconstruction:

- Sub-division or consolidation of shares into smaller or higher Denomination and Conversion of share into stock or vice-versa
- Variation of shareholders' rights
- Reduction of share capital
- Compromise, arrangements etc.
- Surrender of Shares.



SCENARIO BASED QUESTIONS

8. Parth Ltd, had laid down the following terms upon the sanction of the reconstruction plan by the court-
1. Furniture and Fixtures which stood at the books at Rs. 1,50,000 to be written down to Rs. 95,000. The freehold premises which was valued at Rs. 7,00,000 showed an appreciation of Rs. 55,000.
 2. Plant and machinery showed fall in value of Rs. 89,000, to be recorded in the books. Investment at Rs. 2,00,000 was brought down to the existing market value at Rs. 1,05,000.
 3. Debenture holders accepted to receive the following in lieu of their present 9% debentures of Rs. 2,50,000-
 - a. 1/5th of the total to be paid in cash to them.
 - b. To take over the land and buildings of value Rs. 72,000.
 - c. To forgo the remaining unpaid portion as a policy of reconstruction.

Write off the profit and loss A/c debit balance at Rs. 70,000 which had been accumulated over the years. In case of any shortfall, the balance of the General reserve of Rs. 1,50,000 can be utilized to write off the losses under reconstruction scheme.

Show the necessary journal entries as part of the reconstruction process considering that balance in general reserve utilized to write off the losses as per reconstruction scheme.

Answer:

Journal entries in the books of Parth Ltd.

		Dr.	Cr.
		Rs.	Rs.
Reconstruction A/c	Dr	2,39,000	
To Furniture and Fixtures A/c	.		55,000
To Plant and machinery A/c			89,000
To Investment A/c			95,000
(Writing off overvalued assets as per Reconstruction Scheme dated.)			
Freehold premises A/c	Dr	55,000	
To Reconstruction A/c	.		55,000
(Being the increase in the premises credited to reconstruction account as per reconstruction scheme)			
9% Debentures A/c	Dr	2,50,000	
To Bank A/c	.		50,000

To Land and building A/c To Reconstruction A/c (Being the debenture holders claim settled partly and foregone partly as per reconstruction scheme)			72,000 1,28,000
Reconstruction A/c To Profit and loss A/c (Being the loss written off as per reconstruction scheme)	Dr.	70,000	70,000
General reserve A/c To Reconstruction A/c (Being the balance in general reserve utilized to write off the losses as per reconstruction scheme)	Dr.	1,26,000	1,26,000

9. The following scheme of reconstruction has been approved for Win Limited:

- (i) The shareholders to receive in lieu of their present holding at 1,00,000 shares of Rs. 10 each, the following:
 - (a) New fully paid Rs. 10 Equity shares equal to $\frac{3}{5}$ th of their holding.
 - (b) 10% Preference shares fully paid to the extent of $\frac{1}{5}$ th of the above new equity shares.
 - (c) Rs. 40,000, 8% Debentures.
- (ii) An issue of Rs. 1 lakh 10% first debentures was made and allotted, payment for the same being received in cash forthwith.
- (iii) Goodwill which stood at Rs. 1,40,000 was completely written off.
- (iv) Plant and machinery which stood at Rs. 2,00,000 was written down to Rs. 1,50,000.
- (v) Freehold property which stood at Rs. 1,50,000 was written down by Rs.50,000.

You are required to draw up the necessary Journal entries in the Books of Win Limited for the above reconstruction. Suitable narrations to Journal entries should form part of your answer.

Answer:

Journal Entries

		Rs.	Rs.
Equity Share Capital (old) A/c To Equity Share Capital (Rs. 10) A/c To 10% Preference Share Capital A/c To 8% Debentures A/c To Capital Reduction A/c (Being new equity shares, 10% Preference Shares, 8% Debentures issued and the balance transferred to Reconstruction account as per the Scheme)	Dr.	10,00,000	6,00,000 1,20,000 40,000 2,40,000
Bank A/c To 10% First Debentures A/c	Dr.	1,00,000	1,00,000

(Being allotment of 10% first Debentures)			
Capital Reduction A/c	Dr.	2,40,000	
To Goodwill Account			1,40,000
To Plant and Machinery Account			50,000
To Freehold Property Account			50,000
(Being Capital Reduction Account utilized for writing off of Goodwill, Plant and Machinery and Freehold property as per the scheme)			

10. Green Limited had decided to reconstruct the Balance Sheet since it has accumulated huge losses. The following is the Balance Sheet of the Company as at 31.3.20X1 before reconstruction:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	65,00,000
	B	Reserves and Surplus	2	(20,00,000)
2		Non-current liabilities		
	A	Long-term borrowings	3	15,00,000
3		Current liabilities		
	A	Trade Payables		5,00,000
		Total		65,00,000
		Assets		
1		Non-current assets		
	A	Property, plant and equipment	4	45,00,000
	B	Intangible assets	5	20,00,000
2		Current assets		Nil
		Total		65,00,000

Notes to accounts

		Rs.
1	Share Capital	
	Equity share capital	
	<u>Authorized share capital</u>	
	1,50,000 Equity shares of Rs. 50 each	75,00,000
	<u>Issued, subscribed and paid up capital</u>	
	50,000 Equity Shares of Rs. 50 each	25,00,000
	1,00,000 Equity shares of Rs. 50 each, Rs. 40 paid up	40,00,000

2	Reserves and Surplus	<u>65,00,000</u>
	Debit balance of Profit and loss Account	<u>(20,00,000)</u>
		<u>(20,00,000)</u>
3	Long-term borrowings	
	Secured: 12% First debentures	5,00,000
	12% Second debentures	<u>10,00,000</u>
		<u>15,00,000</u>
4	Property, Plant and Equipment	
	Building	10,00,000
	Plant	10,00,000
	Computers	<u>25,00,000</u>
		<u>45,00,000</u>
5	Intangible assets	
	Goodwill	<u>20,00,000</u>
		<u>20,00,000</u>

The following is the interest of Mr. X and Mr. Y in Green Limited:

	Mr. X	Mr. Y
	Rs.	Rs.
12% First Debentures	3,00,000	2,00,000
12% Second Debentures	7,00,000	3,00,000
Trade payables	<u>2,00,000</u>	<u>1,00,000</u>
	<u>12,00,000</u>	<u>6,00,000</u>
Fully paid up Rs. 50 shares	3,00,000	2,00,000
Partly paid up shares (Rs. 40 paid up)	5,00,000	5,00,000

The following Scheme of Reconstruction is approved by all parties interested and also by the Court:

- Uncalled capital is to be called up in full and such shares and the other fully paid up shares be converted into equity shares of Rs. 20 each.
- Mr. X is to cancel Rs. 7,00,000 of his total debt (other than share amount) and to pay Rs. 2 lakhs to the company and to receive new 14% First Debentures for the balance amount.
- Mr. Y is to cancel Rs. 3,00,000 of his total debt (other than equity shares) and to accept new 14% First Debentures for the balance.
- The amount thus rendered available by the scheme shall be utilised in writing off of Goodwill, Profit and Loss A/c Loss and the balance to write off the value of computers.

You are required to draw the Journal Entries to record the same and also show the Balance Sheet of the reconstructed company.

Answer:

Journal Entries in books of Green Limited

		Dr. Rs.	Cr. Rs.
Bank Account	Dr.	10,00,000	
To Equity Share Capital Account			10,00,000
(Balance of Rs. 10 per share on 1,00,000 equity shares <u>called up as per reconstruction scheme</u>)			
Equity Share Capital Account (Rs. 50)	Dr.	75,00,000	
To Equity Share Capital Account (Rs. 20)			30,00,000
To Capital Reduction Account 45,00,000			
(Reduction of equity shares of Rs. 50 each to <u>shares of Rs. 20 each as per reconstruction scheme</u>)			
12% First Debentures Account	Dr.	3,00,000	
12% Second Debentures Account	Dr.	7,00,000	
Trade payables Account	Dr.	2,00,000	
To X			12,00,000
(The total amount due to X, transferred to <u>his account</u>)			
Bank Account	Dr.	2,00,000	
To X			2,00,000
(The amount paid by X under the reconstruction <u>scheme</u>) 12%			
First Debentures Account	Dr.	2,00,000	
12% Second Debentures Account	Dr.	3,00,000	
Trade payables Account	Dr.	1,00,000	
To Y			6,00,000
(The total amount due to Y, transferred to <u>his account</u>)			
Y	Dr.	6,00,000	
To 14% First Debentures Account			3,00,000
To Capital Reduction Account			3,00,000
(The amount due to Y discharged by issue of <u>14% first debentures</u>)			
X	Dr.	14,00,000	
To 14% First Debentures Account			7,00,000
To Capital Reduction Account			7,00,000
(The cancellation of Rs. 7,00,000 out of total debt of Mr. X and issue of 14% first debentures for the balance amount as per reconstruction scheme)			
Capital Reduction Account	Dr.	55,00,000	
To Goodwill Account			20,00,000
To Profit and Loss Account			20,00,000
To Computers Account			15,00,000

(The balance amount of capital reduction account utilised in writing off goodwill, profit and loss account, and computers— Working Note)

Balance Sheet of Green Limited (and reduced) as at 31st March, 20X1

Particulars		Notes	Rs.
	Equity and Liabilities		
1	Shareholders' funds		
a	Share capital	1	30,00,000
2	Non-current liabilities		
a	Long-term borrowings	2	10,00,000
3	Current liabilities		
a	Trade Payables		<u>2,00,000</u>
	Total		<u>42,00,000</u>
	Assets		
1	Non-current assets	3	
a	Property, plant and equipment		30,00,000
2	Current assets		
	Cash and cash equivalents		<u>12,00,000</u>
	Total		<u>42,00,000</u>

Notes to accounts

		Rs.
1.	Share Capital	
	Equity share capital	
	Issued, subscribed and paid up	
	1,50,000 equity shares of Rs. 20 each	30,00,000
	Total	30,00,000
2.	Long-term borrowings	
	Secured	
	14% First Debentures	10,00,000
	Total	10,00,000
3.	Property, Plant and Equipment	
	Building	10,00,000
	Plant	10,00,000
	Computers	10,00,000
	Total	30,00,000

Working Note:**Capital Reduction Account**

	Rs.		Rs.
To Goodwill A/c	20,00,000	By Equity Share Capital A/c	45,00,000
To P & L A/c	20,00,000	By X	7,00,000
To Computers (Bal. Fig.)	15,00,000	By Y	3,00,000
	55,00,000		55,00,000

11. The following is the Balance Sheet of Weak Ltd. as at 31.3.20X1:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	1,50,00,000
	B	Reserves and Surplus	2	(6,00,000)
2		Non-current liabilities		
	A	Long-term borrowings	3	40,00,000
3		Current liabilities		
	A	Trade Payables		50,00,000
	B	Short term provisions	4	<u>1,00,000</u>
		Total		<u>2,35,00,000</u>
		Assets		
1		Non-current assets		
	A	Property, plant and equipment		1,25,00,000
	B	Non-current investment	5	10,00,000
2		Current assets		<u>1,00,00,000</u>
		Total		<u>2,35,00,000</u>

Notes to accounts

		Rs.
1	Share Capital	
	Equity share capital	
	1,00,000 Equity Shares of Rs. 100 each	1,00,00,000
	50,000, 12% Cumulative Preference shares of Rs. 100 each	<u>50,00,000</u>
		<u>1,50,00,000</u>
2	Reserves and Surplus	
	Debit balance of Profit and loss Account	<u>(6,00,000)</u>
		<u>(6,00,000)</u>

3	Long-term borrowings 40,000, 10% debentures of Rs.100 each	<u>40,00,000</u>
		<u>40,00,000</u>
4	Short term provisions Provision for taxation	<u>1,00,000</u>
		<u>1,00,000</u>
5	Non-current investments Investments (market value of Rs. 9,50,000)	<u>10,00,000</u>
		<u>10,00,000</u>

The following scheme of reorganization is sanctioned:

- (i) All the existing equity shares are reduced to Rs. 40 each.
- (ii) All preference shares are reduced to Rs. 60 each.
- (iii) The rate of interest on debentures is increased to 12%. The debenture holders surrender their existing debentures of Rs. 100 each and exchange the same for fresh debentures of Rs. 70 each for every debenture held by them.
- (iv) One of the creditors of the company to whom the company owes Rs. 20,00,000 decides to forgo 40% of his claim. He is allotted 30,000 equity shares of Rs. 40 each in full satisfaction of his claim.
- (v) Property, plant and equipment are to be written down by 30%.
- (vi) Current assets are to be revalued at Rs. 45,00,000.
- (vii) The taxation liability of the company is settled at Rs. 1,50,000.
- (viii) Investments to be brought to their market value.
- (ix) It is decided to write off the debit balance of Profit and Loss account.

Pass Journal entries and show the Balance sheet of the company after giving effect to the above.

Answer:

Journal Entries in the books of Weak Ltd.

			Rs.	Rs.
(i)	Equity share capital (Rs. 100) A/c To Equity Share Capital (Rs. 40) A/c To Capital Reduction A/c (Being conversion of equity share capital of Rs. 100 each into Rs. 40 each as per reconstruction scheme)	Dr.	1,00,00,000	40,00,000 60,00,000
(ii)	12% Cumulative Preference Share capital (Rs. 100) A/c To 12% Cumulative Preference Share Capital (Rs. 60) A/c To Capital Reduction A/c	Dr.	50,00,000	30,00,000

	(Being conversion of 12% cumulative preference share capital of Rs. 100 each into Rs. 60 each as per reconstruction scheme)			20,00,000
(iii)	10% Debentures A/c To 12% Debentures A/c To Capital Reduction A/c (Being 12% debentures issued to 10% debenture-holders for 70% of their claims. The balance transferred to capital reduction account as per reconstruction scheme)	Dr.	40,00,000	28,00,000 12,00,000
(iv)	Trade payables A/c To Equity Share Capital A/c To Capital Reduction A/c (Being a creditor of Rs. 20,00,000 agreed to surrender his claim by 40% and was allotted 30,000 equity shares of Rs. 40 each in full settlement of his dues as per reconstruction scheme)	Dr.	20,00,000	12,00,000 8,00,000
(v)	Provision for Taxation A/c Capital Reduction A/c To current assets(bank A/c) A/c (Being liability for taxation settled)	Dr. Dr.	1,00,000 50,000	1,50,000
(vi)	Capital Reduction A/c To P & L A/c To Property, plant and equipment A/c To Current Assets A/c To Investments A/c (Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) Balance, Property, plant and equipment, Current Assets, Investments through capital reduction account)	Dr.	99,00,000	6,00,000 37,50,000 55,00,000 50,000
(vii)	Capital Reduction A/c To capital Reserve A/c (Being balance in capital reduction account transferred to capital reserve account)	Dr.	50,000	50,000

Balance Sheet of Weak Ltd. (and reduced) as at 31.3.20X1

Particulars		Notes	Rs.
1	Equity and Liabilities		
	Shareholders' funds		
a	Share capital	1	82,00,000
b	Reserves and Surplus	2	50,000
2	Non-current liabilities		
a	Long-term borrowings	3	28,00,000
3	Current liabilities		
a	Trade Payables		30,00,000
	Total		1,40,50,000
	Assets		
1	Non-current assets		
a	Property, plant and equipment	4	87,50,000
b	Investments	5	9,50,000
2	Current assets	6	43,50,000
	Total		1,40,50,000

Notes to accounts

		Rs.	Rs.
1.	Share Capital		
	Equity share capital		
	Issued, subscribed and paid up		
	1,30,000 equity shares of Rs. 40 each		52,00,000
	Preference share capital		
	Issued, subscribed and paid up		
	50,000 12% Cumulative Preference shares of Rs. 60 each		30,00,000
	Total		82,00,000
2.	Reserves and Surplus		
	Capital Reserve		50,000
3.	Long-term borrowings		
	Secured		
	12% Debentures		28,00,000
4.	Property, plant and Equipment		
	Total PPE	1,25,00,000	
	Adjustment under scheme of reconstruction	(37,50,000)	87,50,000
5.	Investments		
	Adjustment under scheme of reconstruction	10,00,000 (50,000)	9,50,000

6.	Current assets	45,00,000	
	Adjustment under scheme of reconstruction	(1,50,000)	43,50,000

Working Note:

Capital Reduction Account

	Rs.		Rs.
To Current Asset	50,000	By Equity share capital	60,00,000
To P & L A/c	6,00,000	By 12% Cumulative	
To Property, plant		preference share capital	20,00,000
and equipment	37,50,000	By 10% Debentures	12,00,000
To Current assets	55,00,000	By Trade payables	8,00,000
To Investment	50,000		
To Capital Reserve (bal. fig.)	50,000		
	1,00,00,000		1,00,00,000

12. The following is the Balance Sheet of X Ltd. as at 31st March, 20X1:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	36,00,000
	B	Reserves and Surplus	2	(14,40,000)
2		Non-current liabilities		
	A	Long-term borrowings	3	6,00,000
3		Current liabilities		
	A	Trade Payables		3,00,000
	B	Short term borrowings - Bank overdraft		6,00,000
		Total		<u>36,60,000</u>
		Assets		
1		Non-current assets		
	A	Property, plant and equipment		30,00,000
	B	Intangible assets	4	90,000
2		Current assets	5	
	a	Inventories		2,60,000
	b	Trade receivables		2,80,000
	c	Cash and cash equivalents		<u>30,000</u>
		Total		<u>36,60,000</u>

Notes to accounts

		Rs.
1	Share capital	
	24,000 Equity Shares of Rs. 100 each	24,00,000
	12,000, 10% Preference Shares of Rs. 100 each	<u>12,00,000</u>
	Total	<u>36,00,000</u>
2	Reserves and Surplus	
	Debit balance of Profit and loss Account	(14,40,000)
		<u>(14,40,000)</u>
3	Long-term borrowings	
	10% debentures	<u>6,00,000</u>
		<u>6,00,000</u>
4.	Property, plant and Equipment	
	Land and Building	12,00,000
	Plant and Machinery	<u>18,00,000</u>
		<u>30,00,000</u>
5	Intangible assets	
	Goodwill	<u>90,000</u>
		<u>90,000</u>

On the above date, the company adopted the following scheme of reconstruction:

- (i) The equity shares are to be reduced to shares of Rs. 40 each fully paid and the preference shares to be reduced to fully paid shares of Rs. 75 each.
- (ii) The debenture holders took over Inventories and Trade receivables in full satisfaction of their claims.
- (iii) The Land and Building to be appreciated by 30% and Plant and machinery to be depreciated by 30%.
- (iv) The debit balance of profit and loss account and intangible assets are to be eliminated.
- (v) Expenses of reconstruction amounted to Rs. 5,000.

Give journal entries incorporating the above scheme of reconstruction and prepare the reconstructed Balance Sheet.

Answer:

In the books of X Ltd. Journal Entries

31 st March, 20X1			Rs.	Rs.
(i)	Equity Share Capital A/c (Rs. 100)	Dr.	24,00,000	
	To Equity Share Capital A/c (Rs. 40)			9,60,000
	To Capital Reduction A/c			14,40,000
	(Being 24,000 equity shares of Rs. 100 each reduced to			

	Rs. 40 each fully paid up)			
(ii)	10% Preference Share Capital A/c (Rs. 100) To 10% Preference Share Capital A/c (Rs. 75) To Capital Reduction A/c (Being 12,000 Preference shares of Rs. 100 each reduced to Rs. 75 each fully paid up)	Dr.	12,00,000	9,00,000 3,00,000
(iii)	10% Debentures A/c To Inventories A/c To Trade receivables A/c To Capital Reduction A/c (Being debenture holders given Inventories and Trade receivables in full settlement of their claims)	Dr.	6,00,000	2,60,000 2,80,000 60,000
(iv)	Land & Building A/c To Capital Reduction A/c (Being Land & Building appreciated by 30%)	Dr.	3,60,000	3,60,000
(v)	Capital reduction A/c To Cash A/c (Being expenses of reconstruction paid)	Dr.	5,000	5,000
(vi)	Capital Reduction A/c To Goodwill A/c To Profit and Loss A/c To Plant & Machinery A/c (Being various losses written off, assets written down through Capital Reserve A/c)	Dr.	20,70,000	90,000 14,40,000 5,40,000
(vii)	Capital Reduction To Capital Reserve A/c (Bal. Fig.) (Being balance in Capital Reduction A/c transferred to Capital Reserve A/c)	Dr.	85,000	85,000

Balance Sheet (And Reduced) of X Ltd. as at 31st March, 20X1

Particulars		Notes No.	Rs.
1	Equity and Liabilities		
	Shareholders' funds		
a	Share capital	1	18,60,000
b	Reserves and Surplus	2	85,000
2	Current liabilities		
a	Trade Payables		3,00,000
b	Short term borrowings		6,00,000

	Total		28,45,000
	Assets		
1	Non-current assets		
a	Property, plant and equipment	3	28,20,000
2	Current assets		
	Cash and cash equivalents (30,000 - 5,000)		25,000
	Total		28,45,000

Notes to accounts

1.	Share Capital		Rs.
	Equity share capital		
	24,000 equity shares of Rs. 40 each fully paid up		9,60,000
	Preference share capital		
	12,000, 10% Preference shares of Rs. 75 each fully paid up		9,00,000
	Total		18,60,000
2.	Reserves and Surplus		
	Capital Reserve		85,000
3.	Property, plant and Equipment		
	Land and Building	15,60,000	
	Plant and Machinery	12,60,000	
	Total		28,20,000



QUESTIONS FROM RTP'S, MTP'S, QP'S

Question 1

The summarized balance sheet of Z Limited as on 31st March, 2017 is as under:

Liabilities Share Capital:	Amount in Rs.
5,00,000 Equity shares of Rs. 10 each fully paid up	50,00,000
9%, 20,000 Preference shares of Rs. 100 each fully paid up	20,00,000
Reserves and Surplus:	
Profit and Loss Account	(14,60,000)
Non-Current Liabilities:	
10% Secured Debentures	16,00,000
Current Liabilities:	
Interest due on Debentures	1,60,000
Trade Payables	5,00,000
Loan from Directors	1,00,000
Bank Overdraft	1,00,000
Provision for Tax	1,00,000
Total	81,00,000
Assets:	
Non-Current Assets:	
Property, Plant & Equipment:	
(a) Tangible Assets:	
Land & Buildings	30,00,000
Plant & Machinery	12,50,000
Furniture & Fixtures	2,50,000
(b) Intangible Assets:	
Goodwill	10,00,000
Patents	5,00,000
Current Assets:	
Trade Investments	5,00,000
Trade Receivables	5,00,000
Inventory	10,00,000
Discount on issue of debentures	1,00,000
Total	81,00,000

Note: Preference dividend is in arrears for last 2 years.

Mr. Y holds 60% of debentures and Mr. Z holds 40% of debentures. Moreover Rs. 1,00,000 and Rs. 60,000 were also payable to Mr. Y and Mr. Z respectively as trade payable.

The following scheme of reconstruction has been agreed upon and duly approved.

- (i) All the equity shares to be converted into fully paid equity shares of Rs. 5.00 each.
- (ii) The Preference shares be reduced to Rs. 50 each and the preference shareholders agreed to forego their arrears of preference dividends, in consideration of which 9% preference shares are to be converted into 10% preference shares.
- (iii) Mr. Y and Mr. Z agreed to cancel 50% each of their respective total debt including interest on debentures. Mr. Y and Mr. Z also agreed to pay Rs. 1,00,000 and Rs. 60,000 respectively in cash and to receive new 12% debentures for the balance amount.
- (iv) Persons relating to trade payables, other than Mr. Y and Mr. Z also agreed to forgo their 50% claims.
- (v) Directors also waived 60% of their loans and accepted equity shares for the balance.
- (vi) Capital commitments of Rs. 3.00 lacs were cancelled on payment of Rs. 15,000 as penalty.
- (vii) Directors refunded Rs. 1,00,000 of the fees previously received by them.
- (viii) Reconstruction expenses paid Rs. 15,000.
- (ix) The taxation liability of the company was settled for Rs 75,000 and was paid immediately.
- (x) The Assets were revalued as under:

Land and Building	32,00,000
Plant and Machinery	6,00,000
Inventory	7,50,000
Trade Receivables	4,00,000
Furniture and Fixtures	1,50,000
Trade Investments	4,50,000

You are required to prepare necessary journal entries for all the above-mentioned transactions including amounts to be written off of Goodwill, Patents, Loss in Profit and Loss account and Discount on issue of debentures. And also, prepare Bank Account and Reconstruction Account.

(RTP May'22)

Answer :

Journal Entries in the Books of Z Ltd.

		Dr. Rs.	Cr. Rs.
(i)	Equity Share Capital (Rs. 10 each) A/c	Dr.	50,00,000
	To Equity Share Capital (Rs. 5 each) A/c		25,00,000
	To Reconstruction A/c		25,00,000
	(Being conversion of 5,00,000 equity shares of Rs. 10 each fully paid into same number of fully paid equity shares of Rs. 5 each as per scheme of reconstruction.)		
(ii)	9% Preference Share Capital (Rs. 100 each) A/c	Dr.	20,00,000

	To 10% Preference Share Capital (Rs. 50 each) A/c			10,00,000
	To Reconstruction A/c			10,00,000
	(Being conversion of 9% preference share of Rs. 100 each into same number of 10% preference share of Rs. 50 each and claims of preference dividends settled as per scheme of reconstruction.)			
(iii)	10% Secured Debentures A/c	Dr.	9,60,000	
	Trade payables A/c	Dr.	1,00,000	
	Interest on Debentures Outstanding A/c	Dr.	96,000	
	Bank A/c	Dr.	1,00,000	
	To 12% Debentures A/c			6,78,000
	To Reconstruction A/c			5,78,000
	(Being Rs. 11,56,000 due to Y (including trade payables) cancelled and 12% debentures allotted for the amount after waving 50% as per scheme of reconstruction.)			
(iv)	10% Secured Debentures A/c	Dr.	6,40,000	
	Trade Payables	Dr.	60,000	
	Interest on debentures outstanding A/c	Dr.	64,000	
	Bank A/c	Dr.	60,000	
	To 12% debentures A/c			4,42,000
	To Reconstruction A/c			3,82,000
	(Being Rs. 7,64,000 due to Z (including trade payables) cancelled and 12% debentures allotted for the amount after waving 50% as per scheme of reconstruction.)			
(v)	Trade payables A/c	Dr.	1,70,000	
	To Reconstruction A/c			1,70,000
	(Being remaining trade payables sacrificed 50% of their claim.)			
(vi)	Directors' Loan A/c	Dr.	1,00,000	
	To Equity Share Capital (Rs. 5) A/c			40,000
	To Reconstruction A/c			60,000
	(Being Directors' loan claim settled by issuing 12,000 equity shares of Rs. 5 each as per scheme of reconstruction.)			
(vii)	Reconstruction A/c	Dr.	15,000	
	To Bank A/c			15,000

	(Being payment made towards penalty of 5% for cancellation of capital commitments of Rs. 3 Lakhs.)			
(viii)	Bank A/c	Dr.	1,00,000	
	To Reconstruction A/c			1,00,000
	(Being refund of fees by directors credited to reconstruction A/c)			
(ix)	Reconstruction A/c	Dr.	15,000	
	To Bank A/c			15,000
	(Being payment of reconstruction expenses)			
(x)	Provision for Tax A/c	Dr.	1,00,000	
	To Bank A/c			75,000
	To Reconstruction A/c			25,000
	(Being payment of tax liability in full settlement against provision for tax)			
(xi)	Land and Building A/c	Dr.	2,00,000	
	To Reconstruction A/c			2,00,000
	(Being appreciation in value of Land & Building recorded)			
(xii)	Reconstruction A/c	Dr.	49,85,000	
	To Goodwill A/c		10,00,000	
	To Patent A/c		5,00,000	
	To Profit and Loss A/c		14,60,000	
	To Discount on issue of Debentures A/c		1,00,000	
	To Plant and Machinery A/c		6,50,000	
	To Furniture & Fixture A/c		1,00,000	
	To Trade Investment A/c		50,000	
	To Inventory A/c		2,50,000	
	To Trade Receivables A/c		1,00,000	
	To Capital Reserve (bal. fig.)		7,75,000	
	(Being writing off of losses and reduction in the value of assets as per scheme of reconstruction, balance of reconstruction A/c transfer to Capital Reserve.)			

Bank Account

	Rs.		Rs.
To Reconstruction (Y)	1,00,000	By Balance b/d	1,00,000
To Reconstruction(Z)	60,000	By Reconstruction A/c	15,000
To Reconstruction A/c		(capital commitment penalty paid)	

(refund of earlier fees by directors)	1,00,000	By Reconstruction A/c	
		(reconstruction expenses paid)	15,000
		By Provision for tax A/c(tax paid)	75,000
		By Balance c/d	55,000
	2,60,000		2,60,000

Reconstruction Account

	Rs.		Rs.
To Bank (penalty)	15,000	By Equity Share	
To Bank (reconstruction expenses)	15,000	Capital A/c	25,00,000
To Goodwill	10,00,000	By 9% Pref. Share	
To Patent	5,00,000	Capital A/c	10,00,000
To P & L A/c	14,60,000	By Mr. Y (Settlement)	5,78,000
To Discount on issue of debentures	1,00,000	By Mr. Z (Settlement)	3,82,000
To P & M	6,50,000	By Trade Payables A/c	1,70,000
To Furniture and Fixtures	1,00,000	By Director's loan	60,000
To Trade investment	50,000	By Bank	1,00,000
To Inventory	2,50,000	By Provision for tax	25,000
To Trade Receivables	1,00,000	By Land and Building	2,00,000
To Capital Reserve (bal. fig.)	7,75,000		
	50,15,000		50,15,000

Question 2

Planet Limited has decided to reconstruct the Balance Sheet since it has accumulated huge losses. The following is the balance sheet of the company as on 31 st March, 2022 before reconstruction:

Particulars	Note No.	Amount (₹ In lakh)
Equity & Liabilities		
Shareholders' Funds		
Share Capital	1	2,100
Reserves & Surplus	2	(783)
Non-Current Liabilities		
Long term Borrowings	3	1,050
Current Liabilities		
Trade Payables	4	153
Other Liabilities	5	36
Total		2,556
Assets		

Non-Current Assets:		
PPE	6	1,125
Current Investments	7	300
Inventories	8	450
Trade Receivables	9	675
Cash & Cash Equivalents	10	6
Total		2,556

Notes to Accounts:

		₹ In lakh
(1)	Share capital	
	Authorised:	
	300 lakh Equity shares of ₹ 10 each	3,000
	12 lakh, 8% preference Shares of ₹ 100 each	1,200
	Issued, Subscribed and Paid up:	4,200
	150 Lakh Equity Shares of ₹ 10 each, fully paid up	1,500
	6 lakh 8% Preference Shares of ₹ 100 each, fully paid up	600
(2)	Reserves and Surplus	2,100
	Debit balance of Profit & Loss A/c	(783)
(3)	Long term borrowings	
	6% Debentures (Secured by freehold property)	600
	Director's Loan	450
(4)	Trade payables	1,050
	Trade payables for Goods	153
(5)	Other Liabilities	
	Interest Accrued and Due on 6% Debentures	36
(6)	PPE	
	Freehold Property	825
	Plant & machinery	300
(7)	Current Investment	1,125
	Investment in Equity Instruments	300
(8)	Inventories	
	Finished Goods	450
(9)	Trade Receivables	
	Trade receivables for Goods	675
(10)	Cash and Cash equivalents	
	Balance with bank	6

The Board of Directors of the company decided upon the following scheme of reconstruction with the consent of respective shareholders:

- (1) Preference Shares are to be written down to ₹ 75 each and Equity Shares to ₹ 2 each.
- (2) Preference Shares Dividend in arrears for 3 years to be waived by 2/3rd and for balance 1/3rd, Equity Shares of ₹ 2 each to be allotted.
- (3) Debenture holders agreed to take one Freehold Property at its book value of ₹ 450 lakh in part payment of their holding. Balance Debentures to remain as liability of the company.
- (4) Interest accrued and due on Debentures to be paid in cash.
- (5) Remaining Freehold Property to be valued at ₹ 550 lakh.
- (6) All investments sold out for ₹ 425 lakh.
- (7) 70% of Directors' loan to be waived and for the balance, Equity Shares of ₹ 2 each to be allotted.
- (8) 40% of Trade receivables and 80% of Inventories to be written off.
- (9) Company's contractual commitments amounting to ₹ 900 lakh have been settled by paying penalty of ₹ 72 lakhs.

You are required to:

(a) Pass Journal Entries for all the transactions related to internal reconstruction;

(b) Prepare Capital Reduction Account, Bank Account; and

Prepare Notes to Accounts on Share Capital and PPE, immediately after the implementation of internal reconstruction.



(RTP Nov'22)

Answer :

a) Journal Entries related to internal reconstruction in the books of Planet Ltd.

(₹ in lakhs)

	Particulars		Debit ₹	Credit ₹
i	8% Preference share capital A/c (₹ 100 each)	Dr.	600	
	To 8% Preference share capital A/c (₹ 75 each)			450
	To Capital reduction A/c			150
	(Being the preference shares of ₹ 100 each reduced to ₹ 75 each as per the approved scheme)			
ii	Equity share capital A/c (₹ 10 each)	Dr.	1,500	
	To Equity share capital A/c (₹ 2 each)			300
	To Capital reduction A/c			1,200
	(Being the equity shares of ₹ 10 each reduced to ₹ 2 each)			
iii	Capital reduction A/c	Dr.	48	
	To Equity share capital A/c (₹ 2 each)			48

	(Being 1/3rd of arrears of preference share dividend of three years to be satisfied by issue of 24 lakh equity shares of ₹ 2 each)			
iv	6% Debentures A/c	Dr.	450	
	To Freehold property A/c			450
	(Being claim settled in part by transfer of freehold property)			
v	Accrued debenture interest A/c	Dr.	36	
	To Bank A/c			36
	(Being accrued debenture interest paid)			
vi	Freehold property A/c	Dr.	175	
	To Capital reduction A/c			175
	(Being appreciation (550-375) in the value of freehold property)			
vii	Bank A/c	Dr.	425	
	To Investment A/c			300
	To Capital reduction A/c			125
	(Being investment sold on profit)			
viii	Director's loan A/c	Dr.	450	
	To Equity share capital A/c (₹ 2 each)			135
	To Capital reduction A/c			315
	(Being director's loan waived by 70% and balance being discharged by issue of 67.5 lakh equity shares of ₹ 2 each)			
ix	Capital Reduction A/c	Dr.	1,485	
	To Profit and loss A/c			783
	To Trade receivables A/c (675 x 40%)			270
	To Inventories-in-trade A/c (450 x 80%)			360
	To Bank A/c			72
	(Being various assets, penalty on cancellation of contract, profit and loss account debit balance written off through capital reduction account)			
x	Capital Reduction A/c	Dr.	432	
	To Capital reserve A/c			432
	(Being balance transferred to capital reserve account as per the scheme)			

b) Capital Reduction Account

(₹ in lakhs)

To Equity Share Capital	48	By 8% Pref. Share Capital	150

To P & L A/c	783	By Equity Share Capital	1,200
To Trade Receivables	270	By Freehold property	175
To Inventories	360	By Bank (profit on sale of investment)	125
To Bank	72	By Director's loan	315
To Capital Reserve	432		
	1,965		1,965

Bank Account

(₹ in lakhs)

To Balance b/d	6	By Accrued debenture interest	36
To Investments	300	By Capital Reduction Account (Penalty on cancellation of contract)	72
To Capital reduction	125	By Balance c/d	323
	431		431

c) Note to Accounts on Share Capital and PPE after implementation of internal reconstruction

Share Capital	(₹ in lakhs)
Authorised:	
300 lakh shares of ₹ 2 each	600
12 lakh, 8% Preference shares of ₹ 75 each	900
Issued, subscribed and paid up:	1,500
241.5 lakh Equity shares of ₹ 2 each	483
(out of which 91.5 lakh shares have been issued for consideration other than cash)	450
6 lakh, 8% Preference shares of ₹75 each fully paid up	
Total	933
PPE	
Freehold property 825	
Less: Utilised to pay Debenture holders (450)	
Add: Appreciation 175	550
Plant and machinery	300
Total	850

Working Note:

Calculation of number of equity shares issued	
To equity shareholders	150 Lakh
To Preference shareholders (in lieu of arrear of preference dividend)	24 Lakh
To Directors	67.5 Lakh
	241.5 Lakh

Question 3

The following is the Balance Sheet of Purple Limited as at 31st March, 2022:

Particulars	Notes	Amount in ₹
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Share Capital	1	15,00,000
(b) Reserves & Surplus	2	(3,00,000)
(2) Current Liabilities		
(a) Trade Payables		2,20,000
(b) Short Term Borrowings – Bank Overdraft		2,00,000
Total		16,20,000
II. Assets		
(1) Non-Current Assets		
(a) Property, Plant and Equipment	3	10,20,000
(b) Intangible Assets	4	1,20,600
(2) Current Assets		
(a) Inventories		1,70,000
(b) Trade Receivables		3,01,800
(c) Cash and cash equivalents		7,600
Total		16,20,000

Notes to Accounts

	₹	₹
(1) Share Capital		
90,000 Equity Shares of ₹ 10 each fully paid	9,00,000	
6% Preference Share Capital	6,00,000	15,00,000
(2) Reserves & Surplus		
Profit & Loss account		(3,00,000)
(3) Property, Plant and Equipment		
Land and Building	5,40,000	
Plant and Machinery	4,80,000	10,20,000
(4) Intangible Assets		
Goodwill	84,600	
Patents	36,000	1,20,600

Dividends on preference shares are in arrears for 3 years.

On the above date, the company adopted the following scheme of reconstruction:

- (i) The preference shares are converted from 6% to 8% but revalued in a manner in which the total return on them remains unaffected.

- (ii) The value of equity shares is brought down to ₹ 8 per share;
- (iii) The arrears of dividend on preference shares are cancelled.
- (iv) The debit balance of Goodwill account is written off entirely.
- (v) Land and Building and Plant and Machinery are revalued at 85% and 80% of their respective book values.
- (vi) Book debts amounting to ₹ 14,400 are to be treated as bad and hence to be written off;
- (vii) The company expects to earn a profit at the rate of ₹ 90,000 per annum from the current year which would be utilized entirely for reducing the debit balance of Profit and loss accounts for 3 years. The remaining balance of the said account would be written off at the time of capital reduction process.
- (viii) The balance of total capital reduction is to be utilized in writing down Patents.
- (ix) A secured loan of ₹ 4,80,000 bearing interest at 12% per annum is to be obtained by mortgaging tangible fixed assets for repayment of bank overdraft and for providing additional funds for working capital.

You are required to give journal entries incorporating the above scheme of reconstruction, capital reduction account and prepare the reconstructed Balance Sheet. (PYP Nov '22)

Answer :

	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)			
2.	Equity share capital A/c (₹ 10)	Dr.	9,00,000	
	To Equity share capital A/c (₹ 8)			7,20,000
	To Capital reduction A/c			1,80,000
	(Being equity capital reduced to nominal value of ₹ 8 each)			
3.	Capital Reduction A/c	Dr.	3,30,000	
	To Goodwill A/c			84,600
	To Land and Building A/c			81,000
	To Plant and Machinery A/c			96,000
	To Trade Receivables A/c (Book debts)			14,400
	To Patents A/c (Bal. fig.)			24,000

	To Profit and loss A/c			30,000
	(Being losses and assets written off to the extent required)			
4.	Bank A/c	Dr.	4,80,000	
	To Bank Loan A/c			4,80,000
	(Being Loan taken)			
5.	Bank overdraft A/c	Dr.	2,00,000	
	To Bank A/c			2,00,000
	(Being Bank overdraft repaid)			

Capital Reduction Account

Particulars	₹	Particulars	₹
To Goodwill A/c	84,600	By Equity Share Capital A/c	1,80,000
To Land & Building A/c	81,000	By 6% Preference Share Capital A/c	1,50,000
To Plant and Machinery, A/c	96,000		
To Trade receivables (Book Debts) A/c	14,400		
To Profit & Loss A/c	30,000		
To Patents A/c (Bal. fig.)	24,000		
	3,30,000		3,30,000

Balance Sheet of Purple Ltd. (and reduced) as at 31.3.2022

	Particulars	Notes	₹
	Equity and Liabilities		
1	Shareholders' funds		
a	Share capital	1	11,70,000
b	Reserves and surplus	2	(2,70,000)
2	Current liabilities		
a	Short term borrowings (Secured Bank Loan)		4,80,000
b	Trade Payables		2,20,000
	Total		16,00,000
	Assets		
1	Non-current assets		
a	Property, plant and equipment	3	8,43,000
b	Intangible assets	4	12,000
2	Current Assets		
a	Inventory		1,70,000
b	Trade receivables	5	2,87,400

c	Cash and cash equivalents (7,600+4,80,000–2,00,000)	2,87,600
	Total	16,00,000

Notes to Accounts:

			₹
1.	Share Capital		
	Authorized		
	Issued, subscribed and paid up:		
	90,000 equity shares of ₹ 8 each fully paid	7,20,000	
	8% Preference share capital*	4,50,000	11,70,000
2.	Reserves and Surplus		
	Profit and Loss Account (Dr. balance)		(2,70,000)
3.	Property plant and equipment		
	Land and Building	4,59,000	
	Plant and Machinery	3,84,000	8,43,000
4.	Intangible assets		
	Patent ₹ (36,000 – 24,000)		12,000
5.	Trade Receivables		
	Sundry Debtors	3,01,800	
	Less: Bad debts	(14,400)	2,87,400

Note: *Face value of preference share is not given in the question (pre and post reconstruction) and hence any suitable value of preference share may be assumed.

Working Notes:

1. Calculation of new Preference Shares

Rate of return : 6% on Preference Shares

Dividend	:	$(6/100) \times ₹6,00,000$	= ₹ 36,000
Rate of return	:	8% on Preference Shares	
Dividend :		$(8/100) \times X =$	₹ 36,000
		$X = (36,000/8) \times 100 =$	₹ 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.

2. Since the company expects to earn a profit of ₹ 90,000 p.a; consecutively for three years and it shall be used to write-off debit balance of P & L account, hence ₹ 2,70,000 being loss shall be shown in the Balance Sheet under Reserve & Surplus head and ₹ 30,000 shall be written-off from

Capital Reduction A/c.

3. Calculation of Amount written off on Land & Building and Plant & Machinery

Land & Building	= (85/100) x 5,40,000	= ₹ 4,59,000
Plant & Machinery	= (80/100) x 4,80,000	= ₹ 3,84,000
Reduced by:		
Land & Building	= (5,40,000 – 4,59,000)	= ₹ 81,000
Plant & Machinery	= (4,80,000 – 3,84,000)	= ₹ 96,000

Question 4

X Ltd. had ₹ 1,00,000 equity share capital divided into 1,000 shares of ₹ 100 each out of which ₹ 80 per share was called up and paid up. It has 1,500 cumulative preference shares of ₹ 100 each fully paid up. Intangible assets include Goodwill of ₹ 80,000 and patents of ₹ 27,800. Preference dividends are in arrears of ₹ 33,000.

You are required to show the entries (Ignore dates) under each of the following conditions:

- If X Ltd. resolves to subdivide the equity shares into 10,000 equity shares of ₹ 10 each of which ₹ 8 per share is called up and paid up.
- If X Ltd. resolves to convert its 1,000 equity shares of ₹ 100 each (assume fully - paid) into ₹ 1,00,000 worth of stock.
- The preference shares are to be converted into 11% unsecured debentures of ₹ 100 each (including arrears of dividends).
- Patents and Goodwill to be written-off.

(PYP May '23)

Answer :

Journal Entries in the books of X Ltd.

			₹	₹
(i)	Equity Share Capital (₹ 100) A/c	Dr.	80,000	
	To Equity Share Capital (₹ 10) A/c			80,000
	(Being the sub-division of 1,000 shares of ₹ 100 each with ₹ 80 paid up into 10,000 shares ₹ 10 each with ₹ 8 paid up by reSolution: in general meeting dated)			
(ii)	Equity Share Capital (₹ 100) A/c	Dr.	1,00,000	
	To Equity Stock A/c			1,00,000
	(Being conversion of 1,000 fully paid Equity Shares of ₹ 100 into ₹ 1,00,000 Equity Stock as per reSolution: in general meeting dated<)			
(iii)	Cumulative Preference Share Capital A/c	Dr.	1,50,000	
	Capital Reduction (Reconstruction) A/c	Dr.	33,000	

	To 11% Debentures (Unsecured)			1,83,000
(iv)	(Being 1,500 cumulative preference shares of ₹ 100 each fully paid up converted into 11% debentures of ₹ 100 each (including arrears of dividends amounting ₹ 33,000))			
	Capital Reduction (Reconstruction) A/c	Dr.	1,07,800	
	To Goodwill			80,000
	To Patents (Writing off patents, goodwill)			27,800

Question 5

Following information from Balance Sheet of Ruby Limited as on 31st March, 2023.

	Amount ₹
Authorised and Issued equity share capital:	
60,000 shares of ₹ 100 each fully paid	60,00,000
40,000 7% cumulative preference shares of ₹ 100 each fully paid	40,00,000
General Reserve	12,00,000
Loan from Director	8,80,000
Trade Payables	49,20,000
Outstanding expenses	6,40,000
Bank loan	6,00,000
Patent	8,00,000
Plant & machinery	60,00,000
Building	11,00,000
Trade receivables	47,00,000
Inventory	32,60,000
Cash	2,40,000
Bank Balance	4,60,000
Profit and Loss account	16,80,000

Note: The arrears of preference dividend amount to ₹ 5,60,000;

The company had suffered losses since last 3 years due to bad market conditions and hope for a better position in the future.

The following scheme of reconstruction has been agreed upon and duly approved by all concerned:

- (1) Equity shares to be converted into 6,00,000 shares of ₹ 10 each;
- (2) Equity shareholders to surrender to the company 80 percent of their holdings.

- (3) Preference shareholders agree to forgo their right on arrears of dividends in consideration of which 7% preference shares are to be converted into 8% preference shares.
- (4) Trade payables agree to reduce their claim by one fourth in consideration of their getting shares of ₹ 10,00,000 out of the surrendered equity shares;
- (5) Directors agree to forego the amounts due on account of loan.
- (6) Surrendered shares not otherwise utilized to be cancelled.
- (7) Assets to be reduced as under:

	₹
Patent to	Nil
Plant & Machinery by	8,00,000
Inventory by	6,80,000

- (8) Trade receivables to the extent of ₹ 34,00,000 are considered good;
- (9) Revalued figures for building is accepted at ₹ 14,00,000;
- (10) Bank loan is paid.
- (11) Any surplus after meeting the losses should be utilized in writing down the value of the plant further.
- (12) Expenses of reconstruction amounted to ₹ 1,20,000;
- (13) Further 80,000 equity shares were issued to the existing members for increasing the working capital. The issue was fully subscribed and paid up.

You are required to pass the Journal Entries for giving effect to the above arrangement and also to draw up the resultant Balance Sheet of the Company. (RTP Nov '23)

Answer :

Books of Ruby Ltd.
Journal Entries

Particulars		Debit (₹)	Credit (₹)
Equity Share Capital (₹ 100 each) a/c	Dr	60,00,000	
To Equity share capital (₹ 10 each) A/c			60,00,000
(Sub division of equity share into ₹ 10 each)			
Equity Share Capital (₹ 10) A/c	Dr.	48,00,000	
To Share surrendered A/c			48,00,000
(Surrender of 80% of share holding by equity share holders)			
7% Cumulative preference share capital A/c	Dr.	40,00,000	
To 8% cumulative preference share capital A/c			40,00,000
(Conversion of 7% Cumulative Preference share capital into 8% Cumulative Preference share capital. They also			

forgo their right to arrears of dividends)			
Shares Surrendered A/c	Dr.	10,00,000	
To Equity share capital A/c			10,00,000
(Surrendered share issued against trade payables under reconstruction scheme)			
Bank loan A/c	Dr.	6,00,000	
Expenses of reconstruction A/c	Dr.	1,20,000	
To Bank A/c			7,20,000
(Bank loan and reconstruction expenses paid)			
Share surrendered A/c	Dr.	38,00,000	
To Capital Reduction A/c			38,00,000
(Cancellation of unissued surrendered shares) (48,00,000–10,00,000)			
Loan from Director A/c	Dr.	8,80,000	
Trade Payables A/c	Dr.	12,30,000	
Building A/c	Dr.	3,00,000	
To Capital reduction A/c			24,10,000
(Amount sacrificed by directors and trade payables and appreciation in value of building)			
Capital reduction A/c	Dr.	62,10,000	
To Patent A/c			8,00,000
To Trade receivables A/c			13,00,000
To Inventory A/c			6,80,000
To Profit and Loss A/c			16,80,000
To Expenses on Reconstruction A/c			1,20,000
To Plant A/c (bal. fig) (8,00,000+8,30,000)			16,30,000
(Various assets and expenses written off)			
Bank A/c	Dr.	8,00,000	
To Share application money A/c			8,00,000
(Application money received on full and final payment)			
Share application money A/c	Dr.	8,00,000	
To Share capital A/c			8,00,000
(Being 80,000 equity shares of ₹ 10 each issued and fully paid up)			

Note: Cancellation of preference dividend need not be journalised. On cancellation, it ceases to be contingent liability and hence no further disclosure required.

Balance Sheet of Ruby Ltd. (and Reduced) as at 31st March, 2023

	Particulars	Note	Amount (₹)
I.	EQUITY AND LIABILITIES		
	1. Shareholders' funds		
	a. Share capital	1	70,00,000
	b. General reserve		12,00,000
	2. Current liabilities		
	a. Trade payables (49,20,000–12,30,000)		36,90,000
	b. Other current liabilities (outstanding expenses)		6,40,000
	Total		125,30,000
II.	ASSETS		
	1. Non-current assets		
	i. Property, Plant and Equipments	2	57,70,000
	ii. Intangible assets	3	–
	2. Current assets		
	a. Inventories (32,60,000– 6,80,000)		25,80,000
	b. Trade receivables (47,00,000 – 13,00,000)		34,00,000
	c. Cash and cash equivalents	4	7,80,000
	Total		125,30,000

Notes to the financial statements

(1) Share capital

	Particulars	Amount (₹)
a.	Authorised 6,00,000 equity shares of ₹ 10 each 40,000 8% cumulative preference shares of ₹ 100 each	60,00,000 40,00,000
b.	Issued, subscribed and fully paid up 3,00,000 equity shares of ₹ 10 each (of the above, 1,00,000 shares were issued as fully paid up for consideration other than cash under the scheme of reconstruction) 40,000 8% cumulative preference shares of ₹ 100 each	30,00,000 40,00,000
	Total	70,00,000

(2) Property, Plant and Equipment's

Particulars	₹
Plant (60,00,000–16,30,000)	43,70,000
Building (11,00,000 + 3,00,000)	14,00,000

Total	57,70,000

(3) Intangible assets

Particulars	₹
Patent (8,00,000–8,00,000)	–

(4) Cash and cash equivalents

	Particulars	₹
a.	Balance with bank (4,60,000–6,00,000–1,20,000+8,00,000)	5,40,000
b.	Cash on hand	2,40,000
	Total	7,80,000



6. ACCOUNTING FOR BRANCHES INCLUDING FOREIGN BRANCHES

ILLUSTRATIONS

Illustration 1(a) :

Buckingham Bros, Bombay have a branch at Nagpur. They send goods at cost to their branch at Nagpur. However, direct purchases are also made by the branch for which payments are made at head office. All the daily collections are transferred from the branch to the head office.

From the following, prepare Nagpur branch account in the books of head office by Debtors method:

	Rs.		Rs.
Opening balance (1-1-20X1)		Bad Debts	1,000
Imprest Cash	2,000		
Sundry Debtors	25,000	Discount to Customers	2,000
Stock: Transferred from H.O.	24,000	Remittances to H.O.	
Direct Purchases	16,000	(received by H.O.)	1,65,000
Cash Sales	45,000	Remittances to H.O.	
Credit Sales	1,30,000	(not received by H.O. so far)	5,000
Direct Purchases	45,000	Branch Exp. directly paid by H.O.	30,000
Returns from Customers	3,000	Closing Balance (31-12-20X1)	
Goods sent to branch from H.O.	60,000	Stock: Direct Purchase	10,000
Transfer from H.O. for Petty Cash expenses	4,000	Transfer from H.O.	15,000
		Debtors	?
		Imprest Cash	?
		Petty Cash expenses	4,000

Solution: :

In the Books of Buckingham Bros, Bombay

Nagpur Branch Account

Particulars	Rs.	Particulars		Rs.
To Opening Branch Assets-		By Bank –		
		Remittances received from branch		
Stock (24,000+16,000)	40,000	Cash Sales	45,000	

Debtors	25,000	Cash from Debtors *	1,20,000	
		Cash in transit *	5,000	1,70,000
Imprest Cash	2,000	By Closing Branch Assets		
To Goods sent to Branch A/c	60,000	Stock (15,000 +10,000)		25,000
To Creditors (Direct Purchases)	45,000	Debtors (W.N. 1)		24,000
To Bank (Sundry exp.)	30,000	Imprest Cash (W.N. 2)		2,000
To Bank (Petty cash exp.)	4,000			
To Net Profit transferred to General Profit & Loss A/c	15,000			
	2,21,000			2,21,000

Working Notes:

1. Memorandum Debtors A/c

Particulars	Rs.	Particulars	Rs.
To To Bal b/d	25,000	By By Sales Return	3,000
To To Sales	130,000	By By Bad Debts	1,000
		By By Discount	2,000
		By By Cash *	125,000
		By By Bal c/d	24,000
	155,000		155,000

2. Memorandum Petty Cash

Particulars	Rs.	Particulars	Rs.
To Bal b/d	2,000	By Expenses (met by Branch)	4,000
To Transfer from H.O.	4,000	By Bal c/d	2,000
	6,000		6,000

* Collection from Debtors = Total Remittances (1,65,000+5,000) – Cash Sales (45,000) = Rs. 1,25,000

Illustration 1(b) :

From the information given in the illustration 1(a), prepare Nagpur Branch Trading and Profit and Loss Account in the books of head office.

Solution: :

Buckingham Bros. Bombay
Nagpur Branch-Trading and Profit and Loss Account
for the year ending 31st December, 20X1

Particulars	Rs.	Particulars	Rs.	Rs.
To Opening Stock	40,000	By Sales		
To Goods transferred from Head Office	60,000	Cash	45,000	
To Purchases	45,000	Credit sales	1,30,000	
To Gross Profit c/d	52,000		1,75,000	
		Less: Returns	(3,000)	1,72,000
		By Closing Stock		25,000
	1,97,000			1,97,000
To Expenses	30,000	By Gross Profit b/d		52,000
To Discounts	2,000			
To Bad Debts	1,000			
To Petty Cash Expenses	4,000			
To Net Profit transferred to General P&L A/c	15,000			
	52,000			52,000

The students may note that Gross Profit and Net Profit earned by the branch are ascertainable in this method and also evaluating the performance of the branch is very much easier in this method than in the 'Debtors method'.



Illustration 2 :

The Bombay Traders invoiced goods to its Delhi branch at cost. Head Office paid all the branch expenses from its bank account, except petty cash expenses which were met by the Branch. All the cash collected by the branch was banked on the same day to the credit of the Head Office. The following is a summary of the transactions entered into at the branch during the year ended December 31, 20X1.

	Rs.		Rs.
Balances as on 1.1.20X1:			
Stock	7,000	Bad Debts	600
Debtors	12,600	Goods returned by customers	500
Petty Cash,	200	Salaries & Wages	6,200
Goods sent from H.O.	26,000	Rent & Rates	1,200
Goods returned to H.O.	1,000	Sundry Expenses	800
Cash Sales	17,500	Cash received from Sundry Debtors	28,500
Credit Sales	28,400		
Allowances to customers	200	Balances as on 31.12.20X1:	

Discount to customers	1,400	Stock	6,500
		Debtors	9,800
		Petty Cash	100

Prepare: (a) Branch Account (Debtors Method), (b) Branch Stock Account, Branch Profit & Loss Account, Branch Debtors and Branch Expenses Account by adopting the Stock and Debtors Method and (c) Branch Trading and Profit & Loss Account to prove the results as disclosed by the Branch Account.

Solution: :

a. Debtors Method

Delhi Branch Account

20X1		Rs.	Rs.	20X1		Rs.	Rs.
Jan. 1	To Opening			Dec 31	24 Bank		
	branch assets:						
	Stock	7,000			Cash Sales	17,500	
	Debtors	12,600			Cash from		
	Petty cash	200	19,800		sundry	28,500	46,000
					Debtors		
Dec. 31	To Goods sent to Branch A/c		26,000		By Goods sent to Branch A/c		
	To Bank:				–		
	Salaries & Wages	6,200			Returns to H.O.		1,000
	Rent & Rates	1,200			By Closing branch assets		
	Sundry Exp.	800	8,200		Stock	6,500	
					Debtors	9,800	
					Petty Cash	100	16,400
	To Net profit ts/f to General P&L A/c		9,400				

Jan. 1, 20X2	To	Balance b/d	63,400				63,400
			16,400				

b. Stock and Debtors Method

Branch Stock Account

20X1		Rs.	20X1			Rs.
Jan. 1	To	Balance b/d -	7,000	Dec. 31	By Sales:	
		Opening Stock				
Dec. 31	To	Goods Sent	26,000		Cash	17,500
		to Branch A/c			Credit	28,400
	To	Branch P&L A/c	19,900		Less: Return	(500)
				By	Goods sent to Branch A/c - Return	1,000
				By	Balance c/d - Closing Stock	6,500
			52,900			52,900
20X2 Jan. 1	To	Balance b/d - Opening Stock	6,500			

Delhi Branch Debtors Account

20X1		Rs.	20X1		Rs.
Jan. 1	To	Balance b/d	Dec. 31	By	Cash
Dec. 31	To	Sales		By	Returns
				By	Allowances
				By	Discounts
				By	Bad debts
				By	Balance c/d
		41,000			9,800
20X2 Jan. 1	To	Balance b/d			41,000
		9,800			

Delhi Branch Expenses Account

20X1		Rs.	20X1		Rs.
Dec. 31	To Salaries & Wages	6,200	Dec. 31	By Branch P&L A/c	10,500
	To Rent & Rates	1,200			
	To Sundry Expenses	800			
	To Petty Cash expenses (200-100)	100			
	To Allowance to customers	200			
	To Discount	1,400			
	To Bad Debts	600			
		10,500			10,500

Delhi Branch Profit & Loss Account

20X1		Rs.	20X1		Rs.
Dec. 31	To Branch Exp. A/c	10,500	Dec. 31	By Gross Profit b/d	19,900
	To Net Profit ts/f to General P & L A/c	9,400			
		19,900			19,900

(a) Branch Trading and Profit and Loss Account

	Rs.	Rs.		Rs.	Rs.
To Stock		7,000	By Sales:		
To Goods sent from H.O.	26,000		Cash	17,500	
Less: Returns to H.O.	(1,000)	25,000	Credit	28,400	
			Less: returns	(500)	
				27,900	45,400
To Gross profit c/d		19,900	By Closing Stock		6,500
		51,900			51,900
To Salaries & Wages		6,200	By Gross Profit b/d		19,900
To Rent & Rates		1,200			
To Sundry Exp.		800			
To Petty Cash Exp.		100			
To Allowances to Customers		200			
To Discounts		1,400			

To Bad Debts		600			
To Net Profit		9,400			
		19,900			19,900

Illustration 3 (a) :

Harrison of Chennai has a branch at New Delhi to which goods are sent @ 20% above cost. The branch makes both cash and credit sales. Branch expenses are met partly from H.O. and partly by the branch. The statement of expenses incurred by the branch every month is sent to head office for recording.

Following further details are given for the year ended 31st December, 20X1:

		Rs.
Cost of goods sent to Branch at cost		2,00,000
Goods received by Branch till 31-12-20X1 at invoice price		2,20,000
Credit Sales for the year @ invoice price		1,65,000
Cash Sales for the year @ invoice price		59,000
Cash Remitted to head office		2,22,500
Expenses paid by H.O.		12,000
Bad Debts written off		750
Balances as on		
	1-1-20X1	31-12-20X1
	Rs.	Rs.
Stock	25,000 (Cost)	28,000 (invoice price)
Debtors	32,750	26,000
Cash in Hand	5,000	2,500

Show necessary ledger accounts in the books of the head office and determine the Profit or Loss of the Branch for the year ended 31st December, 20X1.

Solution:

Books of Harrison

Branch Stock Account

	Rs.		Rs.
To Balance b/d – Op Stock	30,000	By Branch Debtors (Sales)	1,65,000
To Goods Sent to Branch A/c	2,40,000	By Branch Cash	59,000
To Branch Adjustment A/c	2,000	By Balance c/d	
(Balancing Figure – Excess of Sale over Invoice Price)		Goods in Transit	
		(Rs. 2,40,000 – Rs. 2,20,000)	20,000
		Closing Stock at Branch	28,000
	2,72,000		2,72,000

Branch Debtors Account

	Rs.		Rs.
To Balance b/d	32,750	By Bad debts written off	750
To Branch Stock A/c (Sales)	1,65,000	By Branch Cash (bal. fig.)	1,71,000
		By Balance c/d	26,000
	1,97,750		1,97,750

Branch Cash Account

	Rs.		Rs.
To Balance b/d	5,000	By Bank Remittance to H.O.	2,22,500
To Branch Stock	59,000	By Branch Expenses	10,000
To Branch Debtors	1,71,000	[met by Branch (Bal. fig.)]	
		By Balance c/d	2,500
	2,35,000		2,35,000

Branch Adjustment Account

	Rs.		Rs.
		By Stock Reserve opening (25,000 × 20%)	5,000
To Branch P & L - Gross Profit (Bal. fig.)	39,000	By Goods sent to Branch A/c	40,000
To Stock Reserve (on closing stock (48,000 × 1/6)	8,000	By Branch Stock A/c	2,000
	47,000		47,000

Branch Expenses

	Rs.		Rs.
To Cash (H.O) To Branch Cash	12,000		
	10,000	By Branch P&L A/c	22,000
	22,000		22,000

Branch Profit and Loss Account

	Rs.		Rs.
To Branch Expenses	22,000	By Gross Profit (from Branch Adjustment A/c)	39,000
To Branch Debtors (bad debts)	750		
To Net Profit	16,250		
	39,000		39,000

Goods Sent to Branch Account

	Rs.		Rs.
To Branch Adjustment A/c To	40,000	By Branch to Stock A/c	2,40,000

Purchase A/c - Transfer	2,00,000		
	2,40,000		2,40,000

Illustration 3 (b) :

Take figures from Illustration 3 (a) and prepare branch account following debtors' method.

Solution: :

Books of Harrison New Delhi Branch Account

	Rs.		Rs.
To Balance B/d			
Stock	30,000	By Stock Reserve	5,000
Debtors	32,750		
Cash	5,000		
To Goods Sent to Branch A/c (2,00,000 + 20%)	2,40,000	By Goods Sent to Branch A/c	40,000
To Cash (Exp. paid by H.O.)	12,000	By Cash – Remittance from branch	2,22,500
To Net Profit ts/f to H.O. Profit & Loss A/c (Balancing Figure)	16,250	By Balance c/d Debtors	26,000
To Stock reserve (48,000X20/120)	8,000	Stock (including Transit – W.N 2)	48,000
		Cash	2,500
	3,44,000		3,44,000

Working Note:

Closing Stock = Stock at branch + Stock in Transit (Goods sent by HO – Goods Received by Branch) =
Rs. 28,000 + (Rs. 2,40,000 - Rs. 2,20,000) = Rs. 48,000.

Illustration 4:

Sell Well who carried on a retail business opened a branch X on January 1st, 20X1 where all sales were on credit basis. All goods required by the branch were supplied from the Head Office and were invoiced to the branch at 10% above cost.

The following were the transactions:

	Jan. 20X1	Feb. 20X1	March 20X1
	Rs.	Rs.	Rs.
Goods sent to Branch (Purchase Price)	40,000	50,000	60,000
Sales as shown by the branch monthly report	38,000	42,000	55,000
Cash received from Debtors and remitted to H.O.	20,000	51,000	35,000
Returns to H.O. (Invoice price to Branch)	1,200	600	2,400

The stock of goods held by the branch on March 31, 20X1 amounted to Rs. 53,400 at invoice to branch.

Record these transactions in the Head Office books, showing balances as on 31st March, 20X1 and the branch gross profit for the three months ended on that date.

All workings should form part of your Solution:.

Solution: :

Books of Sell Well

Branch Account

	Rs.			Rs.
To Goods sent to Branch A/c (1,50,000+10%)	1,65,000	By Goods sent to Branch-Loading		15,000
To Goods sent to Branch A/c (4,200 X 10/110)	382	By Goods sent to Branch-returns		4,200
		By Bank		1,06,000
		By Balance c/d - Closing Branch Assets		
To Stock Reserve (53,400 X 10/110)	4,855	Stock	53,400	
To Net Profit (Bal fig) ts/f to General P&L A/c	37,363	Debtors (Sales-Collection)	<u>29,000</u>	82,400
	2,07,600			2,07,600

Working Note:

Memorandum Branch Debtors Account

	Rs.		Rs.
To Balance b/d	---	By Cash/Bank	1,06,000
To Sales	1,35,000	By Balance c/d	29,000
	1,35,000		1,35,000

Goods Sent to Branch Account

	Rs.		Rs.
To Branch A/c – Loading	15,000	By Branch A/c	1,65,000
To Branch A/c – Returns	4,200	By Branch A/c – Loading on returns	382
To Purchases A/c	1,46,182		
	1,65,382		1,65,382

Illustration 5:

Following is the information of the Jammu branch of Best New Delhi for the year ending 31st March, 20X2 from the following:

- (1) Goods are invoiced to the branch at cost plus 20%.
- (2) The sale price is cost plus 50%.
- (3) Other information:

	Rs.
Stock as on 01.04.20X1(invoice price)	2,20,000
Goods sent during the year (invoice price)	11,00,000
Sales during the year	12,00,000
Expenses incurred at the branch	45,000

Ascertain

- (i) the profit earned by the branch during the year.
- (ii) branch stock reserve in respect of unrealized profit.

Solution: :

- (i) **Calculation of profit earned by the branch**
In the books of Jammu Branch
Trading Account and Profit and Loss Account

Particulars	Amount	Particulars	Amount
	Rs.		Rs.
To Opening stock	2,20,000	By Sales	12,00,000
To Goods received by Head office	11,00,000	By Closing stock (Refer W.N.)	3,60,000
To Expenses	45,000		
To Net profit (Bal fig)	1,95,000		
	15,60,000		15,60,000

- (ii) **Stock reserve in respect of unrealised profit**

$$= \text{Rs. } 3,60,000 \times (20/120) = \text{Rs. } 60,000$$

Working Note:

	Rs.	
Cost Price	100	
Invoice Price	120	
Sale Price	150	
Calculation of closing stock at invoice price	Rs.	
Opening stock at invoice price	2,20,000	

Goods received during the year at invoice price	11,00,000	[12,00,000 x (120/150)]
	13,20,000	
Less: Cost of goods sold at invoice price	(9,60,000)	
Closing stock	3,60,000	

Illustration 6:

Hindustan Industries Mumbai has a branch in Cochin to which office goods are invoiced at cost plus 25%. The branch sells both for cash and on credit. Branch Expenses are paid direct from head office, and the Branch has to remit all cash received into the Head Office Bank Account.

From the following details, relating to calendar year 20X1, prepare the accounts in the Head Office Ledger and ascertain the Branch Profit. Branch does not maintain any books of account, but sends weekly returns to the Head Office:

	Rs.
Goods received from Head Office at invoice price	6,00,000
Returns to Head Office at invoice price	12,000
Stock at Cochin as on 1st Jan., 20X1	60,000
Sales in the year - Cash	2,00,000
Credit	3,60,000
Sundry Debtors at Cochin as on 1st Jan. 20X1	72,000
Cash received from Debtors	3,20,000
Discount allowed to Debtors	6,000
Bad debts in the year	4,000
Sales returns at Cochin Branch	8,000
Rent, Rates, Taxes at Branch	18,000
Salaries, Wages, Bonus at Branch	60,000
Office Expenses	6,000
Stock at Branch on 31st Dec. 20X1 at invoice price	1,20,000

Prepare Branch accounts in books of head office by Stock and debtors method.

Solution :

Books of Hindustan Industries, Mumbai

Cochin Branch Stock Account

	Rs.		Rs.
To Balance b/d – Op Stock	60,000	By Bank A/c – Cash Sales	2,00,000
To Branch Debtors A/c – Sales Return	8,000	By Branch Debtors A/c - Credit Sales	3,60,000
To Goods sent to Branch A/c	6,00,000	By Goods sent to Branch (Returns to H.O.)	12,000

To Branch Adjustment A/c (Excess of Selling Price over Invoice Price)	24,000	By Balance c/d - Closing stock	1,20,000
	6,92,000		6,92,000

Cochin Branch Stock Adjustment Account

	Rs.		Rs.
To Goods sent to Branch A/c (1/5 of Rs. 12,000) (on returns)	2,400	By Balance b/d (1/5 of Rs. 60,000)	12,000
To Branch P & L A/c (Profit on sale) – Bal fig	1,29,600	By Goods sent to Branch A/c (1/5 of Rs. 6,00,000)	1,20,000
To Balance c/d (1/5 of Rs. 1,20,000)	24,000	By Branch Stock	24,000
	1,56,000		1,56,000

Goods Sent to Branch Account

	Rs.		Rs.
To Cochin Branch Stock Adjustment A/c	1,20,000	By Cochin Branch Stock A/c	6,00,000
To Cochin Branch Stock A/c (Returns)	12,000	By Cochin Branch Stock Adj. A/c	2,400
To Purchases A/c	4,70,400		
	6,02,400		6,02,400

Branch Debtors Account

	Rs.		Rs.
To Balance b/d	72,000	By Bank	3,20,000
To Branch Stock A/c	3,60,000	By Branch P&L A/c Discount	6,000
		By Branch P&L A/c - Bad Debts	4,000
		By Branch Stock - Sales Returns	8,000
		By Balance c/d	94,000
	4,32,000		4,32,000

Branch Expenses Account

	Rs.		Rs.
To Bank A/c (Rent, Rates & Taxes)	18,000	By Branch Profit & Loss A/c (Transfer)	84,000

To Bank A/c (Salaries & Wages)	60,000		
To Bank A/c (office exp.)	6,000		
	84,000		84,000

Branch Profit & Loss Account for the year ending 31st Dec. 20X1

	Rs.		Rs.
To Branch Expenses A/c	84,000	By Branch Stock Adj. A/c	1,29,600
To Branch Debtors A/c	6,000		
To Branch Debtors A/c	4,000		
To Net Profit transferred to Profit & Loss A/c	35,600		
	1,29,600		1,29,600

Illustration 7

Arnold of Delhi, trades in Ghee and Oil. It has a branch at Lucknow. He dispatches 25 tins of Oil @ Rs. 1,000 per tin and 15 tins of Ghee @ Rs. 1,500 per tin on 1st of every month. The branch incurs some expenditure which is met out of its collections; this is in addition to expenditure directly paid by Head Office.

Following are the other details:

		Delhi	Lucknow
		Rs.	Rs.
Purchases	Ghee	14,75,000	-
	Oil	29,32,000	-
Direct expenses		3,83,275	-
Expenses paid by H.O.		-	14,250
Sales	Ghee	18,46,350	3,42,750
	Oil	27,41,250	3,15,730
Collection during the year (including Cash Sales)		-	6,47,330
Remittance by Branch to Head Office		-	6,13,250

	(Delhi)	
Balance as on:	1-1-20X1	31-12-20X1
Stock:Ghee	1,50,000	3,12,500
Oil	3,50,000	4,17,250
Debtors	7,32,750	-
Cash on Hand	70,520	55,250

Furniture & Fittings	21,500	19,350
Plant/Machinery	3,07,250	7,73,500

	(Lucknow)	
Balance as on:	1-1-20X1	31-12-20X1
Stock:Ghee	17,000	13,250
Oil	27,000	44,750
Debtors	75,750	?
Cash on Hand	7,540	12,350
Furniture & Fittings	6,250	5,625
Plant/Machinery	-	

Addition to Plant/Machinery on 1-1-20X1 Rs. 6,02,750.

Rate of Depreciation: Furniture / Fittings @ 10% and Plant / Machinery @ 15% (already adjusted in the above figures).

The Branch Manager is entitled to 10% commission after charging such commission whereas, the General Manager is entitled to 10% commission on overall company profits after charging such commission. General Manager is also entitled to a salary of Rs. 2,000 p.m. General expenses incurred by H.O. Rs. 24,000.

Prepare Branch Account in the head office books and also prepare the Arnold's Trading and Profit and Loss A/c (excluding branch transactions).

Solution:

In the books of Arnold
Lucknow Branch Account

	Rs.		Rs.
To Balance b/d		By Bank (Remittance)	6,13,250
-Opening Branch Assets		By Closing Branch Assets	
Opening stock:		Closing stock:	
Ghee	17,000	Ghee	13,250
Oil	27,000	Oil	44,750
Debtors	75,750	Debtors (W.N. 1)	86,900
Cash on hand	7,540	Cash on hand (W.N. 2)	12,350
Furniture & fittings	6,250	Furniture & fittings	5,625
To Goods sent to Branch A/c			
Ghee (15 x 1500 x 12)	2,70,000		
Oil (25 x 1000 x 12)	3,00,000		
To Bank (Expenses paid)	14,250		
To Branch Manager commission			

(Rs. 58,335 × 1/11)	5,303		
To Net Profit transferred to General P & L A/c	53,032		
	7,76,125		7,76,125

Arnold

Trading and Profit and Loss account for the year ended 31st December, 20X1

(Excluding branch transactions)

	Rs.		Rs.
To Opening Stock:		By Sales:	
Ghee	1,50,000	Ghee	18,46,350
Oil	3,50,000	Oil	27,41,250
To Purchases:		By Closing Stock:	
Ghee 14,75,000		Ghee	3,12,500
Less: Goods sent to Branch (2,70,000)	12,05,000	Oil	4,17,250
Oil 29,32,000			
Less: Goods sent to Branch (3,00,000)	26,32,000		
To Direct Expenses	3,83,275		
To Gross Profit c/d	5,97,075		
	53,17,350		53,17,350
To Manager's Salary	24,000	By Gross Profit b/d	5,97,075
To General Expenses	24,000	By Branch Profit transferred	53,032
To Depreciation:			
Furniture @10% 2,150			
Plant & Machinery @ 15% (W.N.3) 1,36,500	1,38,650		
To General Manager's Commission @ 10% (i.e., 4,63,457 × 1/11)	42,132		
To Net profit	4,21,325		
	6,50,107		6,50,107

Working Notes:

(1) Memorandum Branch Debtors Account

	Rs.		Rs.
To Balance b/d	75,750	By Cash Collections (including Cash Sales)	6,47,330

To Sales (including Cash Sales)		By Balance c/d	86,900
Ghee	3,42,750		
Oil	3,15,730		
	7,34,230		7,34,230

(2) Memorandum Branch Cash Account

	Rs.		Rs.
To Balance b/d	7,540	By Remittance	6,13,250
To Collections	6,47,330	By Exp. (Balance fig.)	29,270
		By Balance c/d	12,350
	6,54,870		6,54,870

(3) Depreciation on Plant & Machinery

$$3,07,250 \times 15\% + 6,02,750 \times 15\% = \text{Rs.} 1,36,500$$

Illustration 8

M/s Rahul operates a number of retail outlets to which goods are invoiced at wholesale price which is cost plus 25%. These outlets sell the goods at the retail price which is wholesale price plus 20%.

Following is the information regarding one of the outlets for the year ended 31.3.20X2:

	Rs.
Stock at the outlet 1.4.20X1	30,000
Goods invoiced to the outlet during the year	3,24,000
Gross profit made by the outlet	60,000
Goods lost by fire	?
Expenses of the outlet for the year	20,000
Stock at the outlet 31.3.20X2	36,000

You are required to prepare the following accounts in the books of Rahul Limited for the year ended 31.3.20X2:

- Outlet Stock Account.
- Outlet Profit & Loss Account.
- Stock Reserve Account.

Solution:

Outlet Stock Account

	Rs.		Rs.
To Balance b/d	30,000	By Sales (Working Note 1)	3,60,000

To Goods sent to outlet	3,24,000	By Goods lost by fire (b.f.)	18,000
To Gross Profit c/d	60,000	By Balance c/d	36,000
	4,14,000		4,14,000

Outlet Profit & Loss Account

	Rs.		Rs.
To Expenses	20,000	By Gross Profit b/d	60,000
To Goods lost by fire (W.N.2)	18,000		
To Profit transferred	22,000		
	60,000		60,000

Stock Reserve Account

	Rs.		Rs.
To HO P & L A/c – Transfer	6,000	By Balance b/d	6,000
To Balance c/d (Stock Res. required)	7,200	By HOP&L A/c (W.N. 3)	7,200
	13,200		13,200

Working Notes:

Rs.

(1) Wholesale Price $100+25 = 125$

Retail Price $125 + 20\% = 150$

Gross Profit at the outlet

Wholesale Price – Retail Price $(150 - 125) = 25$

Retail sales value $= 60,000 \times \frac{150}{125} = \text{Rs. } 3,60,000$

(2) Goods lost by fire

Opening Stock + Goods Sent + Gross Profit – Sales – Closing Stock

$30,000 + 3,24,000 + 60,000 - 3,60,000 - 36,000 = \text{Rs. } 18,000$

(3) Stock Reserve

Opening Stock $= 30,000 \times \frac{25}{125} = \text{Rs. } 6,000$

Closing Stock $= 36,000 \times \frac{25}{125} = \text{Rs. } 7,200$

Illustration 9

Give Journal Entries in the books of an independent Branch to rectify or adjust the following:

- Branch paid Rs. 5,000 as salary to H.O supervisor, but the amount paid by branch has been debited to salary account in the books of branch.
- Asset Purchased by branch for Rs. 25,000, but the Asset account was retained in H.O Books.
- A remittance of Rs.8,000 sent by the branch has not been received by H.O.
- H.O collected Rs. 25,000 directly from the customer of Branch but fails to give the intimation to branch.

(v) Remittance of funds by H.O to branch Rs. 5,000 not entered in branch books.

Solution: :

Journal Entries in Books of Branch

	Particulars	Dr. Amount Rs.	Cr. Amount Rs.
(i)	Head office account Dr. To Salaries account (Being the rectification of salary paid on behalf of H.O.)	5,000	5,000
(ii)	Head office account Dr. To Bank / Liability A/c (Being Asset purchased by branch but Asset account retained at head office books)	25,000	25,000
(iii)	No Entry in Branch Books		
(iv)	Head office account Dr. To Debtors account (Being the amount of branch debtors collected by H.O.)	25,000	25,000
(v)	Bank A/c Dr. To Head Office (Remittance of Funds by H.O. to Branch)	5,000	5,000

Illustration 10

The following Trial balances as at 31st December, 20X1 have been extracted from the books of Major Ltd. and its branch at a stage where the only adjustments requiring to be made prior to the preparation of a Balance Sheet for the undertaking as a whole are to be done.

	Head Office		Branch	
	Dr. Rs.	Cr. Rs.	Dr. Rs.	Cr. Rs.
Share Capital		1,50,000		
Fixed Assets	75,125		18,901	
Current Assets	1,21,809		23,715	(Note 3)
Current Liabilities		34,567		9,721
Stock Reserve, 1st Jan., 20X1 (Note 2)		693		
Revenue Account		43,210		10,250

Branch Account	31,536			
Head Office Account				22,645
	2,28,470	2,28,470	42,616	42,616

You are required to record the following in the appropriate ledger accounts in both sets of books.

Note:

1. Goods transferred from Head Office to the Branch are invoiced at cost plus 10% and both Revenue Accounts have been prepared on the basis of the prices charged.
2. Relating to the Head Office goods held by the Branch on 1st January, 20X1.
3. Includes goods received from Head Office at invoice price Rs. 4,565.
4. Goods invoiced by Head Office to Branch at Rs. 3,641 were in transit at 31st December, 20X1, as was also a remittance of Rs. 3,500 from the Branch.
5. At 31st December, 20X1, the following transactions were reflected in the Head Office books but unrecorded in the Branch books.

The purchase price of lorry, Rs. 2,500, which reached the Branch on December 25th; a sum received on December 30, 20X1 from one of the Branch debtors, Rs. 750.

Solution:

H.O. Books
Branch Account

20X1		Rs.	20X1		Rs.
Dec. 31	To Balance b/d	31,536	Dec. 31	By Cash in transit By Balance c/d	3,500 28,036
		31,536			31,536

Cash in transit Account

20X1		Rs.	20X1		Rs.
Dec. 31	To Branch A/c	3,500	Dec. 31	By Balance c/d	3,500

Stock Reserve Account

20X1		Rs.	20X1		Rs.
Dec. 31	To Balance c/d (4,565+3,641) x 10/110	746	Jan. 1	By Balance b/d By Revenue A/c (b.f.)	693 53
		746			746

Revenue Account

20X1		Rs.	20X1		Rs.
Dec. 31	To Stock Reserve To Balance c/d	53 43,157	Dec. 31	By Balance b/d	43,210
		43,210			43,210

Branch Books

Head Office Account

20X1		Rs.	20X1		Rs.
Dec. 31	To Current Assets	750	Dec. 31	By Balance b/d	22,645
	To Balance c/d	28,036		By Goods in transit	3,641
		28,786		By Motor Vehicle	2,500
					28,786

Goods in Transit Account

20X1		Rs.	20X1		Rs.
Dec. 31	To Head Office	3,641	Dec. 31	By Balance c/d	3,641

Motor Vehicle Account

20X1		Rs.	20X1		Rs.
Dec. 31	To Head Office	2,500	Dec. 31	By Balance c/d	2,500

Sundry Current Assets A/c

20X1		Rs.	20X1		Rs.
Dec. 31	To Balance b/d	23,715	Dec. 31	By H.O. (Remittance by Debtor)	750
				By Balance c/d	22,965
		23,715			23,715

Illustration 11

KP manufactures a range of goods which it sells to wholesale customers only from its head office. In addition, the H.O. transfers goods to a newly opened branch at factory cost plus 15%. The branch then sells these goods to the general public on only cash basis.

The selling price to wholesale customers is designed to give a factory profit which amounts to 30% of the sales value. The selling price to the general public is designed to give a gross margin (i.e., selling price less cost of goods from H.O.) of 30% of the sales value.

KP operates from rented premises and leases all other types of fixed assets. The rent and hire charges for these are included in the overhead costs shown in the trial balances.

From the information given below, you are required to prepare for the year ended 31st Dec., 20X1 in columnar form.

- A Profit & Loss account for (i) H.O. (ii) the branch (iii) the entire business.
- Balance Sheet as on 31st Dec., 20X1 for the entire business.

	H.O.		Branch	
	Rs.	Rs.	Rs.	Rs.
Raw materials purchased	35,000			
Direct wages	1,08,500			
Factory overheads	39,000			
Stock on 1-1-20X1				
Raw materials	1,800			
Finished goods	13,000		9,200	
Debtors	37,000			
Cash	22,000		1,000	
Administrative Salaries	13,900		4,000	
Salesmen Salaries	22,500		6,200	
Other administrative & selling overheads	12,500		2,300	
Inter-unit accounts	5,000			2,000
Capital		50,000		
Sundry Creditors		13,000		
Provision for unrealized profit in stock		1,200		
Sales		2,00,000		65,200
Goods sent to Branch		46,000		
Goods received from H.O.			44,500	
	3,10,200	3,10,200	67,200	67,200

Note:

- (1) On 28th Dec., 20X1 the branch remitted Rs. 1,500 to the H.O. and this has not yet been recorded in the H.O. books. Also, on the same date, the H.O. dispatched goods to the branch invoiced at Rs. 1,500 and these too have not yet been entered into the branch books. It is the company's policy to adjust items in transit in the books of the recipient.
- (2) The stock of raw materials held at the H.O. on 31st Dec., 20X1 was valued at Rs. 2,300.
- (3) You are advised that:
 - there were no stock losses incurred at the H.O. or at the branch.
 - it is KP's practice to value finished goods stock at the H.O. at factory cost.
 - there were no opening or closing stock of work-in-progress.
- (4) Branch employees are entitled to a bonus of Rs. 156 under a bilateral agreement.

Solution: :

In the books of KP

Trading and Profit & Loss Account for the year ended 31st Dec., 20X1

	H.O. Rs.	Branch Rs.	Total Rs.		H.O. Rs.	Branch Rs.	Total Rs.
To Opening stock of finished goods	13,000	9,200	22,200	By Sales	2,00,000	65,200	2,65,200
To Material consumed (W.N.1)	34,500	-	34,500				
To Wages	1,08,500	-	1,08,500	By Goods Sent to Branch	46,000	-	-
To Factory Overheads	39,000	-	39,000				
To Goods from H.O.		46,000		By Closing stock including transit (W.N.2)	15,000	9,560	24,560
To Gross Profit c/d (W.N.3)	66,000	19,560	85,560			(Bal Fig)	
	(Bal Fig)						
	2,61,000	74,760	2,89,760		2,61,000	74,760	2,89,760
To Admn. Salaries	13,900	4,000	17,900	By Gross Profit b/d	66,000	19,560	85,560
To Salesmen Salaries	22,500	6,200	28,700				
To Other Admn. & selling Overheads	12,500	2,300	14,800				
To Stock Reserve (W.N.4)	47	-	47				
To Bonus to Staff	-	156	156				
To Net Profit	17,053	6,904	23,957				
	66,000	19,560	85,560		66,000	19,560	85,560

Balance Sheet as on 31st Dec., 20X1

		Rs.	H.O. Rs.	Branh Rs.	Total Rs.		H.O. Rs.	Branh Rs.	Total Rs.
Capital			50,000	-	50,000	Fixed Assets	-	-	-
Profit:	H.O.	17,053				Current			
	Branch	<u>6,904</u>	23,957		23,957	Assets:			
						Raw	2,300		2,300
Trade			13,000		13,000	material			
Creditors				156	156	Finished	15,000	9,560	23,313*
Bonus						Goods			
Payable						(Less Stock			
H.O.				10,404		Res.)			
Account*						Debtors	37,000	-	37,000
Stock						Cash	23,500	1,000	24,500
Reserve			1,247			(includin			
(W.N.4)						g transit			
						item)			
						Branch A/c	10,404**		
			88,204	10,560	87,113		88,204	10,560	87,113

* $9,560 \times 100/115$ i.e., $(8,313 + 15,000) = \text{Rs. } 23,313$ or $(15,000 + 9,560) - 1,247$ (Stock reserve)

** $(5,000 + 6,904) - 1500 = \text{Rs. } 10,404$.



Working Notes:

(1) Material consumed

Opening raw material + Raw Material Purchased – Closing raw material
 $= 1,800 + 35,000 - 2,300 = 34,500$

(2) Closing stock at head office

(a) Calculation of total factor cost = Material consumed + Wages + Factory overhead
 $= 34,500 + 1,08,500 + 39,000 = 1,82,000$

(b) Cost (factory cost) of goods sold = Sales – Gross profit
 $= 2,00,000 - 2,00,000 \times 30\% = 1,40,000$

(c) Stock transferred to branch = $46,000 \times 100/115 = 40,000$

(d) Closing stock = $13,000$ (Opening Stock) + $1,82,000 - 1,40,000 - 40,000$
 $= 15,000$

(3) Gross profit of Branch = Sales x Gross profit ratio

$= 65,200 \times 30\% = 19,560$

(4) Closing stock reserve = $9,560 \times 15/115 = 1,247$

Charge to profit and loss = $1,247 - 1,200$ (existing) = 47

Illustration 12

AFFIX of Kolkata has a branch at Delhi to which the goods are supplied from Kolkata but the cost thereof is not recorded in the Head Office books. On 31st March, 20X1 the Branch Balance Sheet was as follows:

Liabilities	Rs.	Assets	Rs.
Creditors Balance	40,000	Debtors Balance	2,00,000
Head Office	1,68,000	Building Extension A/c closed by transfer to H.O. A/c	—
		Cash at Bank	8,000
	2,08,000		2,08,000

During the six months ending on 30-9-20X1, the following transactions took place at Delhi.

	Rs.		Rs.
Sales	2,40,000	Manager's Salary	4,800
Purchases	48,000	Collections from Debtors	1,60,000
Wages paid	20,000	Discounts allowed	8,000
Salaries (inclusive of advance of Rs. 2,000)	6,400	Discount earned	1,200
General Expenses	1,600	Cash paid to Creditors	60,000
Fire Insurance (paid for one year)	3,200	Building Account (further payment)	4,000
Remittance to H.O.	38,400	Cash in Hand	1,600
		Cash at Bank	28,000

Set out the Head Office Account in Delhi books and the Branch Balance Sheet as on 30-9-20X1.

Also give journal entries in the Delhi books.

Solution: :

Journal Entries

20X1 30 Sept.		Dr. Rs.	Cr. Rs.
Salary Advance A/c	Dr.	2,000	
To Salaries A/c			2,000
(The amount paid as advance adjusted by debit to Salary Advance Account)			
Prepaid Insurance A/c (3,200 x 6/12)	Dr.	1,600	
To Fire Insurance A/c			1,600
(Six months premium transferred to the Prepaid Insurance A/c)			
Head Office Account	Dr.	88,400	
To Purchases A/c			48,000

To Wages A/c			20,000
To Salaries A/c (6,400 – 2,000)			4,400
To General Expenses A/c			1,600
To Fire Insurance A/c (3,200 x 6/12)			1,600
To Manager's Salary A/c			4,800
To Discount Allowed A/c			8,000
(Transfer of various revenue accounts (Dr.) to the H.O. Account for closing the accounts)			
Sales Accounts	Dr.	2,40,000	
Discount Earned A/c	Dr.	1,200	
To Head Office A/c			2,41,200
[Revenue accounts (Cr.) transferred to H.O.]			
Head Office Account	Dr.	4,000	
To Building Account			4,000
(Transfer of amounts spent on building extension to H.O. A/c)			

Head Office Account

20X1		Rs.	20X1		Rs.
Sep. 30	To Cash-remittance	38,400	April 1	By Balance b/d	1,68,000
	To Sundries (Revenue A/cs)	88,400	Sep. 30	By Sundries (Revenue A/cs)	2,41,200
	To Building A/c	4,000			
	To Balanced c/d	2,78,400			
		4,09,200			4,09,200

Balance Sheet of Delhi Branch as on Sept. 30, 20X1

Liabilities	Rs.	Assets	Rs.
Creditors Balances	26,800	Debtors Balances	2,72,000
Head Office Account	2,78,400	Salary Advance	2,000
		Prepaid Insurance	1,600
		Building Extension A/c transferred to H.O.	—
		Cash in Hand	1,600
		Cash at Bank	28,000
	3,05,200		3,05,200

Cash and Bank Account

	Rs.		Rs.
To Balance b/d	8,000	By Wages	20,000

To Collection from Debtors	1,60,000	By Salaries	6,400
		By Insurance	3,200
		By General Exp.	1,600
		By H.O. A/c	38,400
		By Manager's Salary	4,800
		By Creditors	60,000
		By Building A/c	4,000
		By Balance c/d	
		By Cash in Hand 1,600	
		By Cash at Bank <u>28,000</u>	29,600
	1,68,000		1,68,000

Debtors Account

	Rs.		Rs.
To Balance b/d	2,00,000	By Cash Collection	1,60,000
To Sales	2,40,000	By Discount (allowed)	8,000
		By Balance c/d	2,72,000
	4,40,000		4,40,000
To Balance b/d	2,72,000		

Creditors Account

	Rs.		Rs.
To Cash	60,000	By Balance b/d	40,000
To Discount (earned)	1,200	By Purchases	48,000
To Balance c/d	26,800		
	88,000		88,000
		By Balance b/d	26,800

Illustration 13

Ring Bell Ltd. Delhi has a Branch at Bombay where a separate set of books is used. The following is the trial balance extracted on 31st December, 20X1.

Head Office Trial Balance

	Rs.	Rs.
Share Capital (Authorised: 10,000 Equity Shares of Rs. 100 each):		
Issued: 8,000 Equity Shares		8,00,000
Profit & Loss Account - 1-1-20X1		25,310
General Reserve		1,00,000
Fixed Assets	5,30,000	

Stock	2,22,470	
Debtors and Creditors	50,500	21,900
Profit for 20X1		52,200
Cash Balance	62,730	
Branch Current Account	1,33,710	
	9,99,410	9,99,410

Branch Trial Balance

	Rs.	Rs.
Fixed Assets	95,000	
Profit for 20X1		31,700
Stock	50,460	
Debtors and Creditors	19,100	10,400
Cash Balance	6,550	
Head Office Current Account		1,29,010
	1,71,110	1,71,110

The difference between the balances of the Current Account in the two sets of books is accounted for as follows:

- (a) Cash remitted by the Branch on 31st December, 20X1, but received by the Head Office on 1st January 20X2 - Rs. 3,000.
- (b) Stock stolen in transit from Head Office and charged to Branch by the Head Office, but not credited to Head Office in the Branch books as the Branch Manager declined to admit any liability (not covered by insurance) - Rs. 1,700.

Give the Branch Current Account in Head Office books after incorporating Branch Trial Balance through journal.

Solution: :

The Branch Current Account in the Head Office Books and Head Office Current Account in the Branch Books do not show the same balances. Therefore, in order to reconcile them, the following journal entries will be passed in the Head Office books:

Journal Entries

		Dr.	Cr.
		Rs.	Rs.
20X1 Dec., 31	Cash in Transit A/c Dr. To Branch Current A/c (Cash sent by the Branch on 31st Dec., 20X1 but received at H.O. on 1st Jan., 20X2)	3,000	3,000
	Loss by theft A/c Dr.	1,700	

	To Branch Current A/c (Stock lost in transit from H.O. to Branch)		1,700

In order to incorporate, in the H.O. books, the given Branch trial balance which has been drawn up after preparing the Branch Profit & Loss Account, the following journal entries will be necessary:

Journal Entries

20X1			Rs.	Rs.
Dec. 31	Branch Current Account Dr. To Profit & Loss Account (Branch Profit for the year)		31,700	31,700
	Branch Fixed Assets Dr. Branch Stock Dr. Branch Debtors Dr.		95,000 50,460 19,100	
	Branch Cash Dr. To Branch Current Account (Branch assets brought into H.O. Books)		6,550	1,71,110
	Branch Current A/c Dr. To Branch Creditors (Branch creditors brought into H.O. Books)		10,400	10,400

Branch Current Account

	Rs.		Rs.
To Balance b/d	1,33,710	By Cash in transit	3,000
To Profit & Loss A/c	31,700	By Loss of theft	1,700
To Branch Creditors	10,400	By Sundry Branch Assets	1,71,110
	1,75,810		1,75,810

Profit and Loss Account for 20X1

	Rs.		Rs.
To Loss by Theft	1,700	By Balance b/d	25,310
To Balance c/d	1,07,510	By Year's Profit: H.O. Branch	52,200 31,700
	1,09,210		1,09,210

Illustration 14

Messrs Ramchand & Co., Hyderabad has a branch in Delhi. The Delhi Branch deals not only in the goods from Head Office but also buys some auxiliary goods and deals in them. They, however, do not prepare any Profit & Loss Account but close all accounts to the Head Office at the end of the year and open them afresh on the basis of advice from their Head Office. The fixed assets accounts are also maintained at the Head Office.

The goods from the Head Office are invoiced at selling prices to give a profit of 20 per cent on the sale price. The goods sent from the branch to Head Office are at cost. From the following prepare Branch Trading and Profit & Loss Account and Branch fixed Assets Account in the Head Office Books.

Trial Balance of the Delhi Branch as on 31-12-20X1

Debit	Rs.	Credit	Rs.
Head office opening balance on 1-1-20X1	15,000	Sales	1,00,000
Goods from H.O.	50,000	Goods to H.O.	3,000
Purchases	20,000	Head Office Current A/c	15,000
Opening Stock (H.O. supplies goods at invoice prices)	4,000	Sundry Creditors	3,000
Opening Stock of other goods	500		
Salaries	7,000		
Rent	3,000		
Office expenditure	2,000		
Cash on Hand	500		
Cash at Bank	4,000		
Sundry Debtors	15,000		
	1,21,000		1,21,000

The Branch balances as on 1st January, 20X1, were as under: Furniture Rs. 5,000; Sundry Debtors Rs. 9,500; Cash Rs. 1,000, Creditors Rs. 30,000. The closing stock at branch of the head office goods at invoice price is Rs. 3,000 and that of purchased goods at cost is Rs. 1,000. Depreciation is to be provided at 10 per cent on branch assets

Solution: :

Delhi Branch Trading and Profit & Loss Account

for the year ended 31st Dec., 20X1

	Rs.		Rs.
To Opening Stock:		By Sales	1,00,000

Head office Goods (4,000 x 80%)	3,200		By Goods from Branch	2,400	3,000
Others	<u>500</u>	3,700	By Closing Stock:		
To Goods to Branch (50,000 x 80%)		40,000	Head Office goods (3,000 x 80%)	1,000	3,400
To Purchases		20,000	Others		
To Gross Profit c/d		42,700			
		<u>1,06,400</u>			<u>1,06,400</u>
To Salaries		7,000	By Gross profit b/d		42,700
To Rent		3,000			
To Office Expenses		2,000			
To Dep. on furniture @ 10%		500			
To Net profit		30,200			
		<u>42,700</u>			<u>42,700</u>

Branch (Fixed) Assets Account (In Head Office Books)

20X1			Rs.	20X1			Rs.
Jan. 1	To	Balance b/d	5,000	Dec. 31	By	Delhi Branch A/c (Depreciation)	500
					By	Balance c/d	4,500
			<u>5,000</u>				<u>5,000</u>
20X2							
Jan. 1	To	Balance b/d	4,500				

Note: Furniture A/c is maintained in Head office books; it is not a part of either opening or closing balance.

Illustration 15

On 31st December, 20X2 the following balances appeared in the books of Chennai Branch of an English firm having its HO office in New York:

	Amount in Rs.	Amount in Rs.
Stock on 1st Jan., 20X2	2,34,000	
Purchases and Sales	15,62,500	23,43,750
Debtors and Creditors	7,65,000	5,10,000
Bills Receivable and Payable	2,04,000	1,78,500
Salaries and Wages	1,00,000	-

Rent, Rates and Taxes	1,06,250	-
Furniture	91,000	-
Bank A/c	5,68,650	
New York Account	-	5,99,150
	36,31,400	36,31,400

Stock on 31st December, 20X2 was Rs. 6,37,500.

Branch account in New York books showed a debit balance of \$ 13,400 on 31st December, 20X2 and Furniture appeared in the Head Office books at \$ 1,750.

The rate of exchange for 1 \$ on 31st December, 20X1 was Rs. 52 and on 31st December, 20X2 was Rs. 51. The average rate for the year was Rs. 50.

Prepare in the Head Office books the Profit and Loss a/c and the Balance Sheet of the Branch assuming integral foreign operation.

Solution: :

In the books of English Firm (Head Office in New York)

Chennai Branch Profit and Loss Account

for the year ended 31st December, 20X2

	\$		\$
To Opening stock	4,500	By Sales	46,875
To Purchases	31,250	By Closing stock	12,500
To Gross profit c/d	23,625	(6,37,500 / 51)	
	59,375		59,375
To Salaries	2,000	By Gross profit b/d	23,625
To Rent, rates and taxes	2,125		
To Exchange translation loss	2,000		
To Net Profit c/d	17,500		
	23,625		23,625

Balance Sheet of Chennai Branch

as on 31st December, 20X2

Liabilities	\$	\$	Assets	\$
Head Office A/c	13,400		Furniture	1,750
Add: Net profit	17,500	30,900	Closing Stock	12,500
Trade creditors		10,000	Trade Debtors	15,000
Bills Payable		3,500	Bills Receivable	4,000
			Cash at bank	11,150
		44,400		44,400

Working Note:

Calculation of Exchange Translation Loss
Chennai Branch Trial Balance (converted in \$)
as on 31st December, 20X2

	Dr. Rs.	Cr. Rs.	Conversion Rate	Dr. (\$)	Cr. (\$)
Stock on 1st Jan., 20X2	2,34,000		52	4,500	
Purchases & Sales	15,62,500	23,43,750	50	31,250	46,875
Debtors & creditors	7,65,000	5,10,000	51	15,000	10,000
Bills Receivable and Bills Payable	2,04,000	1,78,500	51	4,000	3,500
Salaries and wages	1,00,000		50	2,000	
Rent, Rates and Taxes	1,06,250		50	2,125	
Furniture	91,000			1,750	
Bank A/c	5,68,650		51	11,150	
New York Account		5,99,150			13,400
Exchange translation loss (bal. fig.)				2,000	
	36,31,400	36,31,400		73,775	73,775

Illustration 16

S & M Ltd., Bombay, have a branch in Sydney, Australia. Sydney branch is an integral foreign operation of S & M Ltd.

At the end of 31st March, 20X2, the following ledger balances have been extracted from the books of the Bombay Office and the Sydney Office:

	Bombay (Rs. thousands)		Sydney (Austr dollars thousands)	
	Debit	Credit	Debit	Credit
Share Capital	—	2,000	—	—
Reserves & Surplus	—	1,000	—	—
Land	500	—	—	—
Buildings (Cost)	1,000	—	—	—
Buildings Dep. Reserve	—	200	—	—
Plant & Machinery (Cost)	2,500	—	200	—
Plant & Machinery Dep. Reserve	—	600	—	130
Debtors / Creditors	280	200	60	30

Stock (1.4.20X1)	100	–	20	–
Branch Stock Reserve	–	4	–	–
Cash & Bank Balances	10	–	10	–
Purchases / Sales	240	520	20	123
Goods sent to Branch	–	100	5	–
Managing Director's salary	30	–	–	–
Wages & Salaries	75	–	45	–
Rent	–	–	12	–
Office Expenses	25	–	18	–
Commission Receipts	–	256	–	100
Branch / H.O. Current A/c	120	–	–	7
	4,880	4,880	390	390

The following information is also available:

(1) Stock as at 31.3.20X2:

Bombay Rs. 1,50,000

Sydney A \$ 3,125

You are required to convert the Sydney Branch Trial Balance into rupees; Use the following rates of exchange :

Opening rate A \$ = Rs. 20

Closing rate A \$ = Rs. 24

Average rate A \$ = Rs. 22

For Fixed Assets A \$ = Rs. 18



Solution: :

Sydney Branch Trial Balance (in Rupees)

As on 31st March, 20X2

(Rs. '000)

Conversion	Rate per A\$	Dr.	Cr.
Plant & Machinery (cost)	Rs. 18	36,00	
Plant & Machinery Dep. Reserve	Rs. 18		23,40
Debtors / Creditors	Rs. 24	14,40	7,20
Stock (1.4.20X1)	Rs. 20	4,00	
Cash & Bank Balances	Rs. 24	2,40	
Purchase / Sales	Rs. 22	4,40	27,06
Goods received from H.O.	–	1,00	
Wages & Salaries	Rs. 22	9,90	
Rent	Rs. 22	2,64	
Office expenses	Rs. 22	3,96	

Commission Receipts	Rs. 22		22,00
H.O. Current A/c			1,20
		78,70	80,86
Exchange loss (balancing figure)		2,16	
		80,86	80,86

Illustration 17

M/s Carlin has head office at New York (U.S.A.) and branch at Mumbai (India). Mumbai branch is an integral foreign operation of Carlin & Co.

Mumbai branch furnishes you with its trial balance as on 31st March, 20X2 and the additional information given thereafter:

	Dr.	Cr.
	Rupees in thousands	
Stock on 1st April, 20X1	300	—
Purchases and sales	800	1,200
Sundry Debtors and creditors	400	300
Bills of exchange	120	240
Wages and salaries	560	—
Rent, rates and taxes	360	—
Sundry charges	160	—
Computers	240	—
Bank balance	420	—
New York office a/c	—	1,620
	3,360	3,360

Additional information:

- Computers were acquired from a remittance of US \$ 6,000 received from New York head office and paid to the suppliers. Depreciate computers at 60% for the year.
- Unsold stock of Mumbai branch was worth Rs. 4,20,000 on 31st March, 20X2.
- The rates of exchange may be taken as follows:
 - on 1.4.20X1 @ Rs. 40 per US \$
 - on 31.3.20X2 @ Rs. 42 per US \$
 - average exchange rate for the year @ Rs. 41 per US \$
 - conversion in \$ shall be made upto two decimal accuracy.

You are asked to prepare in US dollars the revenue statement for the year ended 31st March, 20X2 and the balance sheet as on that date of Mumbai branch as would appear in the books of New York head office of Carlin & Co. You are informed that Mumbai branch account showed a debit balance of US \$ 39609.18 on 31.3.20X2 in New York books and there were no items pending reconciliation.

Solution: :

M/s Carlin
Mumbai Branch Trial Balance in (US \$)
as on 31st March, 20X2

	Conversion	Dr.	Cr.
	rate per US \$ (Rs.)	US \$	US \$
Stock on 1.4.X1	40	7,500.00	—
Purchases and sales	41	19,512.20	29,268.29
Sundry debtors and creditors	42	9,523.81	7,142.86
Bills of exchange	42	2,857.14	5,714.29
Wages and salaries	41	13,658.54	—
Rent, rates and taxes	41	8,780.49	—
Sundry charges	41	3,902.44	—
Computers	—	6,000.00	—
Bank balance	42	10,000.00	—
New York office A/c	—	—	39,609.18
		81,734.62	81,734.62

Trading and Profit & Loss Account for the year ended 31st March, 20X2

	US \$		US \$
To Opening Stock	7,500.00	By Sales	29,268.29
To Purchases	19,512.20	By Closing stock (4,20,000/42)	10,000.00
To Wages and salaries	<u>13,658.54</u>	By Gross Loss c/d	<u>1,402.45</u>
	<u>40,670.74</u>		<u>40,670.74</u>
To Gross Loss b/d	1,402.45	By Net Loss	17,685.38
To Rent, rates and taxes	8,780.49		
To Sundry charges	3,902.44		
To Depreciation on computers (US \$ 6,000 × 0.6)	3,600.00		
	17,685.38		17,685.38

Balance Sheet of Mumbai Branch as on 31st March, 20X2

Liabilities		US \$	Assets	US \$	US \$
New York Office A/c	39,609.18		Computers	6,000.00	

Less: Net Loss	(17,685.38)	21,923.80	Less: Depreciation	(3,600.00)	2,400.00
Sundry creditors		7,142.86	Closing stock		10,000.00
Bills payable		5,714.29	Sundry debtors		9,523.81
			Bank balance		10,000.00
			Bills receivable		2,857.14
		34,780.95			34,780.95



TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. If goods are invoiced to branches at cost, trading results of branch can be ascertained by
 - (a) Debtors method.
 - (b) Stock and debtors method.
 - (c) Either (a) or (b).
 - (d) Both (a) and (b).

2. Under branch trading and profit loss account method
 - (a) H.O prepares profit and loss account.
 - (b) Each branch is treated separate entity.
 - (c) Both (a) and (b).
 - (d) Either (a) or (b).

3. Goods may be invoiced to branch at
 - (a) Cost or Selling price.
 - (b) Wholesale price.
 - (c) Both (a) and (b).
 - (d) Either (a) or (b).

4. Under debtors method, opening balance of debtors is
 - (a) Debited to branch account.
 - (b) Credited to branch account.
 - (c) Debited to H.O account.
 - (d) Credited to H.O account.

5. Cost of goods returned by branch will have the following effect
 - (a) Goods sent to branch account will be debited.
 - (b) Branch stock account will be credited.
 - (c) Both (a) and (b).
 - (d) Either (a) or (b).



ANSWERS

1.	(c)	2.	(c)	3.	(c)	4.	(a)	5.	(c)

THEORETICAL QUESTIONS

6. Why goods are marked on invoice price by the head office while sending goods to the branch?

Answer :

Goods are marked on invoice price to achieve the following objectives:

- (i) To keep secret from the branch manager, the cost price of the goods and profit made, so that the branch manager may not start a rival and competitive business with the concern; and
- (ii) To have effective control on stock i.e. stock at any time must be equal to opening stock plus goods received from head office minus sales made at branch.
- (iii) To dictate pricing policy to its branches, as well as save work at branch because prices have already been decided.

7. Differentiate Branch Accounts with Departmental accounts.

Answer :

Branch accounts may be maintained either at branch or at head office and no allocation problem arises since the expenses in respect of each branch can be identified. However, Departmental accounts are maintained at one place only. Common expenses are distributed among the departments concerned on some equitable basis considered suitable in the case. For details, refer Para 2 of the Chapter to know the differences.



SCENARIO BASED QUESTIONS

8. Goods worth Rs. 50,000 sent by head office but the branch has received till the closing date goods for worth Rs. 40,000 only. Give journal entry in the books of H.O. and branch for goods in transit.

Answer :

Journal entry in the books of Head Office

No entry

Journal entry in the books of Branch

	Rs.	Rs.
Goods-in-transit account Dr.	10,000	
To Head Office account		10,000
(Being goods sent by head office is still in transit)		

9. Alphs having head office in Mumbai has a branch in Nagpur. The branch at Nagpur is an independent branch maintaining separate books of account. On 31.3.20X1, it was found that the goods dispatched by head office for Rs. 2,00,000 was received by the branch only to the extent of Rs. 1,50,000. The balance goods are in transit. What is the accounting entry to be passed by the branch for recording the goods in transit, in its books?

Answer :

Nagpur branch must include the inventory in its books as goods in transit.

The following journal entry must be made by the branch:

Goods in transit A/c Dr. 50,000
To Head office A/c 50,000

[Being Goods sent by Head office is still in transit on the closing date]

10. Show adjustment journal entry in the books of head office at the end of April, 20X1 for incorporation of inter-branch transactions assuming that only head office maintains different branch accounts in its books.

A. Delhi branch:

- (1) Received goods from Mumbai – Rs. 35,000 and Rs. 15,000 from Kolkata.
- (2) Sent goods to Chennai – Rs. 25,000, Kolkata – Rs. 20,000.
- (3) Bill Receivable received – Rs. 20,000 from Chennai.
- (4) Acceptances sent to Mumbai – Rs. 25,000, Kolkata – Rs. 10,000.

B. Mumbai Branch (apart from the above) :

- (5) Received goods from Kolkata – Rs. 15,000, Delhi – Rs. 20,000.
- (6) Cash sent to Delhi – Rs. 15,000, Kolkata – Rs. 7,000.

C. Chennai Branch (apart from the above) :

(7) Received goods from Kolkata – Rs. 30,000.

(8) Acceptances and Cash sent to Kolkata – Rs. 20,000 and Rs.10,000 respectively.

D. Kolkata Branch (apart from the above) :

(9) Sent goods to Chennai – Rs. 35,000.

(10) Paid cash to Chennai – Rs.15,000.

(11) Acceptances sent to Chennai – Rs.15,000.

Answer :

Journal entry in the books of Head Office

Date	Particulars	Dr.	Cr.
		Rs.	Rs.
30th April, 20X1	Mumbai Branch Account Dr.	3,000	
	Chennai Branch Account Dr.	70,000	
	To Delhi Branch Account		15,000
	To Kolkata Branch Account		58,000
	(Being adjustment entry passed by head office in respect of inter-branch transactions for the month of April, 20X1)		

Working Note:

Inter – Branch transactions

	Delhi	Mumbai	Chennai	Kolkata
	Rs.	Rs.	Rs.	Rs.
A. Delhi Branch				
(1) Received goods	50,000 (Dr.)	35,000 (Cr.)		15,000 (Cr.)
(2) Sent goods	45,000 (Cr.)			20,000 (Dr.)
			25,000 (Dr.)	
(3) Received Bills receivable	20,000 (Dr.)		20,000 (Cr.)	
(4) Sent acceptance	35,000 (Cr.)	25,000 (Dr.)		10,000 (Dr.)
B. Mumbai Branch				
(5) Received goods	20,000 (Cr.)	35,000 (Dr.)		15,000 (Cr.)
(6) Sent cash	15,000 (Dr.)	22,000 (Cr.)		7,000 (Dr.)
C. Chennai Branch				
(7) Received goods			30,000 (Dr.)	30,000 (Cr.)
(8) Sent cash and acceptances			30,000 (Cr.)	30,000 (Dr.)

D. Kolkata Branch				
(9)	Sent goods		35,000 (Dr.)	35,000 (Cr.)
(10)	Sent cash		15,000 (Dr.)	15,000 (Cr.)
(11)	Sent acceptances		15,000 (Dr.)	15,000 (Cr.)
		15,000 (Cr.)	3,000 (Dr.)	70,000 (Dr.)
				58,000 (Cr.)

11. Give Journal Entries in the books of Branch A to rectify or adjust the following:

- (i) Head Office expenses Rs. 3,500 allocated to the Branch, but not recorded in the Branch Books.
- (ii) Depreciation of branch assets, whose accounts are kept by the Head Office not provided earlier for Rs. 1,500.
- (iii) Branch paid Rs. 2,000 as salary to a H.O. Inspector, but the amount paid has been debited by the Branch to Salaries account.
- (iv) H.O. collected Rs. 10,000 directly from a customer on behalf of the Branch, but no intimation to this effect has been received by the Branch.
- (v) A remittance of Rs. 15,000 sent by the Branch has not yet been received by the Head Office.
- (vi) Branch A incurred advertisement expenses of Rs. 3,000 on behalf of Branch B.

Answer :

Books of Branch A

Journal Entries

	Particulars	Dr. Amount Rs.	Cr. Amount Rs.
(i)	Expenses account Dr. To Head office account (Being the allocated expenditure by the head office recorded in branch books)	3,500	3,500
(ii)	Depreciation account Dr. To Head office account (Being the depreciation provided)	1,500	1,500
(iii)	Head office account Dr. To Salaries account (Being the rectification of salary paid on behalf of H.O.)	2,000	2,000
(iv)	Head office account Dr. To Debtors account	10,000	10,000

	(Being the adjustment of collection from branch debtors)		
(v)	No entry in branch books		
(vi)	Head Office account	Dr.	3,000
	To Cash account		3,000
	(Being the expenditure on account of Branch B, recorded in books)		

Note: Entry (vi) Inter branch transactions are routed through Head Office.

12. Widespread invoices goods to its branch at cost plus 20%. The branch sells goods for cash as well as on credit. The branch meets its expenses out of cash collected from its debtors and cash sales and remits the balance of cash to head office after withholding Rs. 10,000 necessary for meeting immediate requirements of cash. On 31st March, 20X1 the assets at the branch were as follows:

	Rs. ('000)
Cash in Hand	10
Trade Debtors	384
Stock, at Invoice Price	1,080
Furniture and Fittings	500

During the accounting year ended 31st March, 20X2 the invoice price of goods dispatched by the head office to the branch amounted to Rs. 1 crore 32 lakhs. Out of the goods received by it, the branch sent back to head office goods invoiced at Rs. 72,000. Other transactions at the branch during the year were as follows:

	(Rs. '000)
Cash Sales	9,700
Credit Sales	3,140
Cash collected by Branch from Credit Customers	2,842
Cash Discount allowed to Debtors	58
Returns by Customers	102
Bad Debts written off	37
Expenses paid by Branch	842

On 1st January, 20X2 the branch purchased new furniture for Rs. 1 lakh for which payment was made by head office through a cheque.

On 31st March, 20X2 branch expenses amounting to Rs. 6,000 were outstanding and cash in hand was again Rs. 10,000. Furniture is subject to depreciation @ 16% per annum on diminishing balance method.

Prepare Branch Account in the books of head office for the year ended 31st March, 20X2.

Answer :

In the Head Office Books
Branch Account
for the year ended 31st March, 20X2

	Rs. '000		Rs.'000
To Balance b/d		By Balance b/d	
Cash in hand	10	Stock reserve Rs. 1,080 ×	180
Trade debtors	384	1	
		—	
		6	
Stock	1,080	By Goods sent to branch	72
Furniture and fittings	500	A/c (Returns to H.O.)	
To Goods sent to branch A/c	13,200	By Goods sent to branch A/c	2,188
To Bank A/c (Payment for	100	(Loading on net goods sent to	
furniture)	245	branch —	
To Balance c/d Stock reserve		By (13,128 × 1/6)	
(1,470 × 1/6)		Bank A/c (Remittance from	11,700
		branch to H.O.) (W.N.5)	
To Net profit transferred to		By Balance c/d	
General P/L account	1,096		
		Cash in hand	10
To Balance c/d -		Trade debtors (W.N.3)	485
Outstanding expenses	6	Stock (W.N.1)	1,470
		Furniture and fittings	
		(W.N.4)	516
	16,621		16,621

Working Notes:

1. Invoice price and cost

Let cost be	100
So, invoice price	120
Loading	20
Loading: Invoice price= 20 : 120	= 1 : 6

2. Memorandum Branch Stock Account

	Rs. '000		Rs. '000
To Balance b/d	1,080	By Goods sent to branch	72
To Goods sent to branch	13,200	By Branch Cash	9,700
To Branch debtors	102	By Branch debtors	3,140

		By Balance c/d	1,470
	14,382		14,382

3. Memorandum Branch Debtors Account

	Rs. '000		Rs. '000
To Balance b/d	384	By Branch cash	2,842
To Branch stock	3,140	By Branch expenses discount	58
		By Branch stock (Returns)	102
		By Branch expenses (Bad debts)	37
		By Balance b/d	485
	3,524		3,524

4. Memorandum Branch Furniture and Fittings Account

	Rs. '000		Rs. '000
To Balance b/d	500	By Depreciation [(500x16%) + x 16% x 3/12]	84
To Bank	100	By Balance c/d	516
	600		600
Note: Since the new furniture depreciation will be for 3 months.		was	purchased on 1st Jan 20X2

5. Memorandum Branch Cash Account

	Rs. '000		Rs. '000
To Balance b/d	10	By Branch expenses	842
To Branch stock	9,700	By Remittances to H.O. (b.f)	11,700
To Branch debtors	<u>2,842</u>	By Balance b/d	<u>10</u>
	<u>12,552</u>		<u>12,552</u>

13. On 31st March, 20X2 Kanpur Branch submits the following Trial Balance to its Head Office at Lucknow :

Debit Balances	Rs. in lacs
Furniture and Equipment	18
Depreciation on furniture	2
Salaries	25
Rent	10
Advertising	6

Telephone, Postage and Stationery	3
Sundry Office Expenses	1
Stock on 1st April, 20X1	60
Goods Received from Head Office	288
Debtors	20
Cash at bank and in hand	8
Carriage Inwards	7
	448
Credit Balances	
Outstanding Expenses	3
Goods Returned to Head Office	5
Sales	360
Head Office	80
	448

Additional Information:

Stock on 31st March, 20X2 was valued at Rs. 62 lacs. On 29th March, 20X2 the Head Office dispatched goods costing Rs. 10 lacs to its branch. Branch did not receive these goods before 1st April, 20X2. Hence, the figure of goods received from Head Office does not include these goods. Also, the head office has charged the branch Rs. 1 lac for centralized services for which the branch has not passed the entry.

You are required to:

- Pass Journal Entries in the books of the Branch to make the necessary adjustments
- Prepare Final Accounts of the Branch including Balance Sheet, and
- Pass Journal Entries in the books of the Head Office to incorporate the whole of the Branch Trial Balance.

Answer :

(i) Books of Branch Journal Entries

		(Rs. in lacs)
	Dr.	Cr.
Goods in Transit A/c Dr.	10	
To Head Office A/c		10
(Goods dispatched by head office but not received by branch before 1st April, 20X2)		
Expenses A/c Dr.	1	
To Head Office A/c		1
(Amount charged by head office for centralised services)		

(ii)

Trading and Profit & Loss Account of the Branch
for the year ended 31st March, 20X2

	Rs. in lacs		Rs. in lacs
To Opening Stock	60	By Sales	360
To Goods received from		By Closing Stock	72
Head Office 288+10		including transit	
Less: Returns (5)	293		
To Carriage Inwards	7		
To Gross Profit c/d	72		
	432		432
To Salaries	25	By Gross Profit b/d	72
To Depreciation on Furniture	2		
To Rent	10		
To Advertising	6		
To Telephone, Postage & Stationery	3		
To Sundry Office Expenses	1		
To Head Office Expenses (centralised services)	1		
To Net Profit Transferred to Head Office A/c	24		
	72		72

Balance Sheet as on 31st March, 20X2

Liabilities	Rs. in lacs	Assets	Rs. in lacs
Head Office	80	Furniture & Equipment	20
Add: Goods in	10	Less: Depreciation	(2)
transit		Stock in hand	62
Head Office		Goods in Transit	10
Expenses	1	Debtors	20
Net Profit	24	Cash at bank and in	
Outstanding		hand	8
Expenses	3		
	118		118

(iii)

Books of Head Office

Journal Entries

		Rs. Dr.	Rs. Dr.
Branch Trading Account	Dr.	365	
To Branch Account			365
(The total of the following items in branch trial balance debited to branch trading account:			
	Rs. in lacs		
Opening Stock	60		
Goods received from Head Office	288		
Goods purchased but not received	10		
Carriage Inwards	7		
Branch Account	Dr.	437	
To Branch Trading Account			437
(Total sales, closing stock and goods returned to Head Office credited to branch trading account, individual amount being as follows:			
	Rs. in lacs		
Sales	360		
Closing Stock	62		
Goods in transit	10		
Goods returned to Head Office	5)		
Branch Trading Account	Dr.	72	
To Branch Profit and Loss Account			72
(Gross profit earned by branch credited to Branch Profit and Loss Account)			
Branch Profit and Loss Account	Dr.	48	
To Branch Account			48
(Total of the following branch expenses debited to Branch Profit & Loss Account:			
	Rs. in lacs		
Salaries	25		
Rent	10		
Advertising	6		
Telephone, Postage & Stationery	3		

Sundry Office Expenses	1		
Head Office Expenses	1		
Depreciation on furniture	2)		
Branch Profit & Loss Account	Dr.	24	
To Profit and Loss Account			24
(Net profit at branch credited to general Profit & Loss A/c)			
Branch Furniture & Equipment	Dr.	18	
Branch Stock	Dr.	62	
Branch Debtors	Dr.	20	
Branch Cash at Bank and in Hand	Dr.	8	
Goods in Transit	Dr.	10	
To Branch			118
(Incorporation of different assets at the branch in H.O. books)			
Branch	Dr.	3	
To Branch Outstanding Expenses			3
(Incorporation of Branch Outstanding Expenses in H.O. books)			

14. M/s Marena, Delhi has a branch at Bangalore to which office goods are invoiced at cost plus 25%. The branch sells both for cash and on credit.

Branch Expenses are paid direct from head office and the Branch has to remit all cash received into the Head Office Bank Account.

From the following details, relating to calendar year 20X1, prepare the accounts in the Head Office Ledger and ascertain the Branch Profit under Stock and Debtors Method’.

Branch does not maintain any books of account, but sends weekly returns to the Head Office.

	Rs.
Goods received from Head Office at invoice price	45,00,000
Returns to Heads Office at invoice price	90,000
Stock at Bangalore as on 1st January, 20X1	4,50,000
Sales during the year	
- Cash	15,00,000
- Credit	27,00,000
Sundry Debtors at Bangalore as on 1st January, 20X1	5,40,000
Cash received from Debtors	24,00,000
Discount allowed to Debtors	45,000
Bad Debts in the year	30,000
Sales returns at Bangalore Branch	60,000

Rent, Rates and Taxes at Branch	1,35,000
Salaries, Wages and Bonus at Branch	4,50,000
Office Expenses	45,000
Stock at Branch on 31st December, 20X1 at invoice price	9,00,000

Answer :

Bangalore Branch Stock Account

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Balance b/d Goods sent to branch A/c	4,50,000	By Goods sent to branch A/c (Returns)	90,000
To Branch debtors A/c (Returns)	45,00,000	By Bank A/c (Cash sales)	15,00,000
To Branch adjustment A/c (Surplus over invoice price)*	60,000	By Branch debtors A/c (credit sales)	27,00,000
		By Balance c/d	9,00,000
	<u>1,80,000</u>		
	<u>51,90,000</u>		<u>51,90,000</u>

*Alternatively, this may directly be transferred to Branch P&L A/c without routing it through Branch Adjustment Account.

Bangalore Branch Adjustment Account

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Stock reserve - 20% of Rs. 9,00,000 (closing stock)	1,80,000	By Stock reserve - 20% of Rs. 4,50,000 (Opening stock)	90,000
To Branch profit & loss A/c (Gross profit)	9,72,000	By Goods sent to branch A/c – 20% of Rs. 44,10,000 (45,00,000 – 90,000)	8,82,000
	—	By Branch stock A/c	<u>1,80,000</u>
	<u>11,52,000</u>		<u>11,52,000</u>

Branch Profit & Loss Account

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Branch expenses A/c	6,30,000	By Branch adjustment A/c (Gross Profit)	9,72,000
To Branch debtors A/c (Discount)	45,000		

To Branch Debtors A/c (Bad debts)	30,000		
To Net profit (transferred to Profit & Loss A/c)			
	<u>2,67,000</u>		
	<u>9,72,000</u>		9,72,000

Branch Expenses Account

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Bank A/c (Rent, rates & taxes)	1,35,000	By Branch profit and loss A/c (Transfer)	6,30,000
To Bank A/c (Salaries, wages & bonus)	4,50,000		
To Bank A/c (Office expenses)	<u>45,000</u>		
	<u>6,30,000</u>		<u>6,30,000</u>

Branch Debtors Account

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Balance b/d	5,40,000	By Bank A/c	24,00,000
To Branch stock A/c	27,00,000	By Branch profit and loss A/c (Bad debts and discount)	75,000
		By Branch stock A/c (Sales returns)	60,000
		By Balance c/d fig.) (bal.	
	<u>32,40,000</u>		<u>7,05,000</u>
			<u>32,40,000</u>

Goods sent to Branch Account

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Branch stock A/c	90,000	By Branch stock A/c	45,00,000
To Branch adjustment A/c	8,82,000		
To Purchases A/c	<u>35,28,000</u>		
	<u>45,00,000</u>		<u>45,00,000</u>

15. Beta, having head office at Mumbai has a branch at Nagpur. 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 Nagpur is wholly engaged in retail trade and the goods are sold at cost to H.O. plus 100%.

Following details are furnished for the year ended 31st March, 20X1:

	Head Office (Rs.)	Branch (Rs.)
Opening stock	2,25,000	
Purchases	25,50,000	
Goods sent to branch (Cost to H.O. plus 80%)	9,54,000	
Sales	27,81,000	9,50,000
Office expenses	90,000	8,500
Selling expenses	72,000	6,300
Staff salary	65,000	12,000

You are required to prepare Trading and Profit and Loss Account of the head office and branch for the year ended 31st March, 20X1.

Answer :

Trading and Profit and Loss A/c
For the year ended 31st March 20X1

	Head office Rs.	Branch Rs.		Head office Rs.	Branch Rs.
To Opening stock	2,25,000	-	By Sales	27,81,000	9,50,000
To Purchases	25,50,000	-	By Goods sent to branch	9,54,000	-
To Goods received from head office	-	9,54,000	By Closing stock (W.N.1 & 2)	7,00,000	99,000
To Gross profit c/d	16,60,000	95,000			
	44,35,000	10,49,000		44,35,000	10,49,000
To Office expenses	90,000	8,500	By Gross profit b/d	16,60,000	95,000

To Selling expenses	72,000	6,300			
To Staff salaries	65,000	12,000			
To Branch Stock Reserve (W.N.3)	44,000	—			
To Net Profit	13,89,000	68,200			
	16,60,000	95,000		16,60,000	95,000

Working Notes:

(1)	Calculation of closing stock of head office:	Rs.
	Opening Stock of head office	2,25,000
	Goods purchased by head office	25,50,000
		27,75,000
	Less: Cost of goods sold [37,35,000 x 100/180]	(20,75,000)
		7,00,000
(2)	Calculation of closing stock of branch:	Rs.
	Goods received from head office [At invoice value]	9,54,000
	Less: Invoice value of goods sold [9,50,000 x 180/200]	(8,55,000)
		99,000
(3)	Calculation of unrealized profit in branch stock:	
	Branch stock Rs. 99,000	
	Profit included 80% of cost	
	Hence, unrealized profit would be = Rs. 99,000 x 80/180	Rs. 44,000

16. Pass necessary Journal entries in the books of an independent Branch of a business entity to rectify or adjust the following:

- (i) Income of Rs. 2,800 allocated to the Branch by Head Office but not recorded in the Branch books.**
- (ii) Branch paid Rs.3,000 as salary to a Head Office Manager, but the amount paid has been debited by the Branch to Salaries Account.**
- (iii) Branch incurred travelling expenses of Rs.5,000 on behalf of other Branches, this was not recorded in the books of Branch.**
- (iv) A remittance of Rs. 1,50,000 sent by the Branch has not received by Head Office on the date of reconciliation of Accounts.**
- (v) Head Office allocates Rs.75,000 to the Branch as Head Office expenses, which has not yet been recorded by the Branch.**

(vi) Head Office collected Rs.30,000 directly from a Branch Customer. The intimation of the fact has been received by the Branch only now, not recorded till now.

(vii) Goods dispatched by the Head office amounting to Rs.10,000, but not received by the Branch till date of reconciliation. The Goods have been received subsequently.

Answer :

Books of Branch

Journal Entries

Sr. No	Particulars	Amount in Rs.	
		Dr.	Cr.
(i)	Head Office Account Dr. To Income Account (Being the income allocated by the Head office not recorded earlier, now recorded)	2,800	2,800
(ii)	Head Office Account Dr. To Salaries Account (Being rectification of salary paid on behalf of Head Office)	3,000	3,000
(iii)	Head Office Account Dr. To Cash Account (Being expenditure incurred on account of other branch, now recorded in books)	5,000	5,000
(iv)	No entry in Branch Books is required.		
(v)	Expenses Account Dr. To Head Office Account (Being allocated expenses of Head Office recorded)	75,000	75,000
(vi)	Head Office Account Dr. To Debtors Account (Being adjustment entry for collection from Branch Debtors directly by Head Office)	30,000	30,000
(vii)	Goods -in- transit Account Dr. To Head Office Account (Being goods sent by Head Office still in- transit)	10,000	10,000

17. The Washington branch of XYZ Mumbai sent the following trial balance as on 31st December, 20X1:

	\$	\$
Head office A/c	—	22,800
Sales	—	84,000
Debtors and creditors	4,800	3,400
Machinery	24,000	—
Cash at bank	1,200	—
Stock, 1 January, 20X1	11,200	—
Goods from H.O.	64,000	—
Expenses	5,000	—
	1,10,200	1,10,200

In the books of head office, the Branch A/c stood as follows:

Washington Branch A/c

		Rs.			Rs.
To	Balance b/d	8,10,000	By	Cash	28,76,000
To	Goods sent to branch	<u>29,26,000</u>	By	Balance c/d	<u>8,60,000</u>
		<u>37,36,000</u>			<u>37,36,000</u>

Goods are sent to the branch at cost plus 10% and the branch sells goods at invoice price plus 25%. Machinery was acquired in past, when \$ 1.00 = Rs. 40.

Rates of exchange were:

1 st January, 20X1	\$ 1.00	=	Rs. 46
31 st December, 20X1	\$ 1.00	=	Rs. 48
Average	\$ 1.00	=	Rs. 47

Machinery is depreciated @ 10% and the branch manager is entitled to a commission of 5% on the profits of the branch.

You are required to:

- Prepare the Branch Trading & Profit & Loss A/c in dollars.
- Convert the Trial Balance of branch into Indian currency and prepare Branch Trading & Profit and Loss A/c and the Branch A/c in the books of head office.

Answer :

(i)

In the Books of Head Office

Branch Trading and Profit & Loss A/c (in Dollars)

for the year ended 31st December, 20X1

Particulars	\$	Particulars	\$
To Opening stock	11,200	By Sales	84,000

To	Goods from H.O.	64,000	By	Closing stock (W.N.2)	8,000
To	Gross profit c/d	16,800			
		92,000			92,000
To	Expenses	5,000	By	Gross profit b/d	16,800
To	Depreciation (24,000 x 10%)	2,400			
To	Manager's commission (W.N.1)	470			
To	Net profit c/d	8,930			
		16,800			16,800

(ii) (a) Converted Branch Trial Balance (into Indian Currency)

Particulars	Rate per \$	Dr. (Rs.)	Cr. (Rs.)
Machinery	40	9,60,000	—
Stock January 1, 20X1	46	5,15,200	—
Goods from head office	Actual	29,26,000	—
Sales	47	—	39,48,000
Expenses	47	2,35,000	—
Debtors & creditors	48	2,30,400	1,63,200
Cash at bank	48	57,600	—
Head office A/c	Actual	—	8,60,000
Difference in exchange rate (b.f.)		47,000	—
		49,71,200	49,71,200
Closing stock \$ 8,000 (W.N. 2)	48		Rs. 3,84,000

(b) Branch Trading and Profit & Loss A/c for the year ended 31st December, 20X1

	Rs.		Rs.
To	Opening stock	By	Sales
To	Goods from head office	By	Closing stock (W.N.2)
To	Gross profit c/d		
	43,32,000		43,32,000
To	Expenses	By	Gross profit b/d
To	Depreciation @ 10% on Rs.9,60,000		
To	Exchange difference		
To	Manager's commission (W.N.1)		
	22,560		

To	Net Profit c/d	4,90,240		
		8,90,800		8,90,800

(c) Branch Account

	Rs.			Rs.
To Balance b/d	8,60,000	By Machinery	9,60,000	
To Net profit	4,90,240	Less: Depreciation	(96,000)	
To Creditors	1,63,200			8,64,000
To Outstanding commission		By Closing stock		3,84,000
	22,560	By Debtors		2,30,400
	15,36,000	By Cash at bank		57,600
				15,36,000

Working Notes:

1. Calculation of manager's commission @ 5% on profit

i.e. 5% of \$[16,800 – (5,000 + 2,400)]

Or 5% × \$9,400 = \$ 470

Manager's commission in Rupees = \$ 470 × Rs. 48 = Rs. 22,560

2. Calculation of closing stock

	\$
Opening stock	11,200
Add: Goods from head office	<u>64,000</u>
	75,200
Less: Cost of goods sold (at invoice price)	
i.e. 100 × 84,000	
125	<u>(67,200)</u>
Closing stock	<u>8,000</u>
Closing stock in Rupees = \$8,000 x Rs. 48 = Rs. 3,84,000.	

Note: Manager is entitled to commission on profits earned at the end of the year.

QUESTIONS FROM RTP'S, MTP'S, QP'S

Question 1

L Ltd. has its head office at Mumbai and two branches at Pune and Goa. The branches purchase goods independently. Pune branch makes a profit of one third on cost and Goa branch makes a profit of 20% on sales. Goods are also supplied by one branch to another at the respective sales price. From the following particulars, prepare the Trading and Profit and Loss Account of Pune branch and find out the profit or loss made by it considering the reserve for unrealised profits:

Particulars	Pune Branch ₹	Goa Branch ₹
Opening Stock	40,000	30,000
Purchases (Including Inter Branch transfers)	2,00,000	2,50,000
Sales	2,80,000	2,95,625
Chargeable Expenses	15,000	27,500
Closing Stock	30,000	43,500
Office and Administration Expenses	13,250	7,000
Selling and Distribution Expenses	15,000	10,000

Information:

- (i) Opening stock at Pune Branch includes goods of ₹ 10,000 (invoice price) taken from Goa Branch,
- (ii) Opening stock at Goa Branch includes goods of invoice price ₹ 17,000 taken from Pune Branch,
- (iii) The Pune Branch sales includes transfer of goods to Goa Branch at selling price ₹ 20,000
- (iv) The sales of Goa Branch include transfer of goods to Pune Branch at selling price ₹ 15,000.
- (v) Closing stock at Pune Branch includes goods received from Goa Branch (invoice price ₹ 5,000.
- (vi) Closing stock at Goa Branch includes goods of ₹ 4,000 (invoice price) (MTP Mar 22)

Answer :

Pune Branch Trading and Profit and Loss Account

Particulars	₹	Particulars	₹
To Opening Stock (including ₹10,000 from Goa Branch)	40,000	By Sales (including ₹20,000 to Goa Branch)	2,80,000
To Purchases	2,00,000	By Closing Stock (including ₹5,000 from Goa Branch)	30,000
To Chargeable Expenses	15,000		
To Gross Profit c/d (before making adjustment for unrealised profit)	55,000		
	3,10,000		3,10,000
To Stock Reserve (for unrealised profit in Closing	1,000	By Gross Profit b/d	55,000

Stock lying at Goa Branch) (₹4,000 x 25/100)			
To Office & Adm. Expenses	13,250	By Stock Reserve (for unrealised profit in Opening Stock lying at Goa Branch) (₹ 17,000 x 25/100)	4,250
To Selling & Distribution Expenses	15,000		
To Net Profit	30,000		
	59,250		59,250

Question 2

DM Delhi has a branch in London which is an integral foreign operation of DM. At the end of the year 31st March, 2021, the branch furnishes the following trial balance in U.K. Pound:

Particulars	£	£
	Dr.	Cr.
Property, Plant & Equipment (Acquired on 1st April, 2017)	24,000	
Stock as on 1st April, 2020	11,200	
Goods from head Office	64,000	
Expenses	4,800	
Debtors	4,800	
Creditors		3,200
Cash at bank	1,200	
Head Office Account		22,800
Purchases	12,000	
Sales		96,000
	1,22,000	1,22,000

In head office books, the branch account stood as shown below:

London Branch A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
To Balance b/d	20,10,000	By Bank A/c	52,16,000
To Goods sent to branch	49,26,000	By Balance c/d	17,20,000
	69,36,000		69,36,000

The following further information is given:

- Property, Plant & Equipment are to be depreciated @ 10% p.a. on WDV.
- On 31st March, 2021:

Expenses outstanding	-	£ 400

Prepaid expenses	-	£ 200
Closing stock	-	£ 8,000

(c) Rate of Exchange:

1st April, 2017 - Rs. 70 to £ 1

1st April, 2020 - Rs. 76 to £ 1

31st March, 2021 - Rs. 77 to £ 1

Average - Rs. 75 to £ 1

You are required to prepare: (1) Trial balance, incorporating adjustments of outstanding and prepaid expenses, converting U.K. pound into Indian rupees; and (2) Trading and profit and loss account for the year ended 31st March, 2021 of London branch as would appear in the books of Delhi head office of DM. (MTP April 22)

Answer :

Trial Balance of London Branch as on 31st March, 2021

Particulars	U.K. Pound	Rate Per U.K. Pound	Dr. (Rs.)	Cr. (Rs.)
Property, Plant & Equipment	24,000	70	16,80,000	
Stock (as on 1st April, 2020)	11,200	76	8,51,200	
Goods from Head Office	64,000	-	49,26,000	
Sales	96,000	75		72,00,000
Purchases	12,000	75	9,00,000	
Expenses (4,800 + 400 – 200)	5,000	75	3,75,000	
Debtors	4,800	77	3,69,600	
Creditors	3,200	77		2,46,400
Outstanding Expenses	400	77		30,800
Prepaid expenses	200	77	15,400	
Cash at Bank	1,200	77	92,400	
Head office Account		-		17,20,000
Difference in Exchange				12,400
			92,09,600	92,09,600

Closing stock will be $(8,000 \times 77) = \text{Rs. } 6,16,000$ Trading and Profit & Loss A/c for the year ended 31st March, 2021

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Opening Stock	8,51,200	By Sales	72,00,000
To Purchases	9,00,000	By Closing Stock	6,16,000
To Goods from H.O.	49,26,000		78,16,000

To Gross Profit	11,38,800		
	78,16,000	By Gross Profit	11,38,800
To Expenses	3,75,000	By Profit due to Exchange difference	12,400
To Depreciation	1,68,000		
To Net Profit	6,08,200		
	11,51,200		11,51,200

Working Note:

Since London Branch is an integral foreign operation. Hence, (1) Property, Plant & Equipment (cost and depreciation) are translated using the exchange rate at the date of purchase of the assets. (2) Exchange difference arising on translation of the financial statement is charged to Profit and Loss Account.

Question 3

Moon Star has a branch at Virginia (USA). The Branch is a non-integral foreign operation of the Moon Star. The trial balance of the Branch as at 31st March, 2022 is as follows:

Particulars	US \$	
	Dr.	Cr.
Office Equipment's	48,000	
Furniture and Fixtures	3,200	
Stock (April 1, 2021)	22,400	
Purchases	96,000	
Sales	---	1,66,400
Goods sent from H.O	32,000	
Salaries	3,200	
Carriage inward	400	
Rent, Rates & Taxes	800	
Insurance	400	
Trade Expenses	400	
Head Office Account	---	45,600
Sundry Debtors	9,600	
Sundry Creditors	---	6,800
Cash at Bank	2,000	
Cash in Hand	400	
	2,18,800	2,18,800

The following further information is given:

(1) Salaries outstanding \$ 400.

(2) Depreciate office equipment and furniture & fixtures @10% p.a. at written down value.

- (3) The Head Office sent goods to Branch for ₹15,80,000.
- (4) The Head Office shows an amount of ₹ 20,50,000 due from Branch.
- (5) Stock on 31st March, 2022 - \$21,500.
- (6) There were no transit items either at the start or at the end of the year.
- (7) On April 1, 2020 when the fixed assets were purchased the rate of exchange was ₹ 43 to one \$. On April 1, 2021, the rate was 47 per \$. On March 31, 2022 the rate was ₹ 50 per \$.
- (8) Average rate during the year was ₹ 45 to one \$.

Prepare Trial balance incorporating adjustments given converting dollars into rupees and Trading, Profit and Loss Account for the year ended 31st March, 2022 of the Branch as would appear in the books of Moon Star for the purpose of incorporating in the main Balance Sheet.

(MTP Oct '23, MTP Sep '22)

Answer :

**In the books of Moon Star Trial Balance (in Rupees)
of Virginia (USA) Branch as on 31st March, 2022**

	Dr.	Cr.	Conversion	Dr.	Cr.
	US \$	US \$	rate	₹	₹
Office Equipment	43,200		50	21,60,000	
Depreciation on Office Equipment	4,800		50	2,40,000	
Furniture and fixtures	2,880		50	1,44,000	
Depreciation on furniture and fixtures	320		50	16,000	
Stock (1st April, 2021)	22,400		47	10,52,800	
Purchases	96,000		45	43,20,000	
Sales		1,66,400	45		74,88,000
Goods sent from H.O.	32,000			15,80,000	
Carriage inward	400		45	18,000	
Salaries (3,200+400)	3,600		45	1,62,000	
Outstanding salaries		400	50		20,000
Rent, rates and taxes	800		45	36,000	
Insurance	400		45	18,000	
Trade expenses	400		45	18,000	
Head Office A/c		45,600			20,50,000
Trade debtors	9,600		50	4,80,000	
Trade creditors		6,800	50		3,40,000
Cash at bank	2,000		50	1,00,000	

Cash in hand	400		50	20,000	
Exchange difference (bal. fig.) transferred to foreign currency translation reserve account					4,66,800
	2,19,200	2,19,200		1,03,64,800	1,03,64,800

Trading and Profit and Loss Account of Virginia Branch for the year ended 31st March, 2022

	₹		₹
To Opening stock	10,52,800	By Sales	74,88,000
To Purchases	43,20,000	By Closing stock	10,75,000
To Goods from Head Office	15,80,000	(21,500 US \$ × 50)	
To Carriage inward	18,000		
To Gross profit c/d	15,92,200		
	85,63,000		85,63,000
To Salaries	1,62,000	By Gross profit b/d	15,92,200
To Rent, rates and taxes	36,000		
To Insurance	18,000		
To Trade expenses	18,000		
To Depreciation on office equipment	2,40,000		
To Depreciation on furniture and fixtures	16,000		
To Net Profit c/d	11,02,200		
	15,92,200		15,92,200

Question 4

On 31st March, 2022 Chennai Branch submits the following Trial Balance to its Head Office at Lucknow:

Debit Balances	₹ in lacs
Furniture and Equipment	18
Depreciation on furniture	2
Salaries	25
Rent	10
Advertising	6
Telephone, Postage and Stationery	3
Sundry Office Expenses	1
Stock on 1st April, 2021	60
Goods Received from Head Office	288
Debtors	20

Cash at bank and in hand	8
Carriage Inwards	7
Credit Balances	448
Outstanding Expenses	3
Goods Returned to Head Office	5
Sales	360
Head Office	80
	448

Additional Information:

Stock on 31st March, 2022 was valued at ₹ 62 lacs. On 29th March, 2022 the Head Office dispatched goods costing ₹ 10 lacs to its branch. Branch did not receive these goods before 1st April, 2022. Hence, the figure of goods received from Head Office does not include these goods. Also the head office has charged the branch ₹ 1 lac for centralized services for which the branch has not passed the entry. You are required to

:(i) pass Journal Entries in the books of the Branch to make the necessary adjustments and (ii) prepare Final Accounts of the Branch including Balance Sheet. (MTP March '23)

Answer :

(i) Books of Branch



Journal Entries

		(₹ in lacs)	
		Dr.	Cr.
Goods in Transit A/c	Dr.	10	
To Head Office A/c			10
(Goods dispatched by head office but not received by branch before 1st April, 2022)			
Expenses A/c	Dr.	1	
To Head Office A/c			1
(Amount charged by head office for centralised services)			

(ii) Trading and Profit & Loss Account of the Branch for the year ended 31st March, 2022

	₹ in lacs		₹ in lacs
To Opening Stock	60	By Sales	360
To Goods received from		By Closing Stock	62
Head Office 288			
Less : Returns (5)	283		
To Carriage Inwards	7		
To Gross Profit c/d	72		

	422		422
To Salaries	25	By Gross Profit b/d	72
To Depreciation on Furniture	2		
To Rent	10		
To Advertising	6		
To Telephone, Postage & Stationery	3		
To Sundry Office Expenses	1		
To Head Office Expenses	1		
To Net Profit Transferred to			
Head Office A/c	24		
	72		72

Balance Sheet as on 31st March, 2022

Liabilities	₹ in lacs		Assets	₹ in lacs	
Head Office	80		Furniture & Equipment	20	
Add : Goods in transit	10		Less : Depreciation	(2)	18
Head Office Expenses	1		Stock in hand		62
Net Profit	24		Goods in Transit		10
		115	Debtors		20
Outstanding Expenses		3	Cash at bank and in hand		8
		118			118

Question 5

PQR has a branch at Houston (USA). Business of the Branch is carried out substantially independent by way of accumulating cash and other monetary items, incurring expenses, generating income and arranging borrowing in its local currency. The trial balance of the Branch as at 31st March, 2022 is as follows:

Particulars	US\$	
	Debit	Credit
Office equipment (Cost)	56,400	
Opening Accumulated Depreciation (Office equipment)		5,400
Furniture and Fixtures (Cost)	36,000	
Opening Accumulated Depreciation (Furniture and Fixtures)		6,840
Opening Stock as on 1st April, 2021	24,500	
Purchases	96,500	
Sales		1,76,250

Salaries	4,250	
Carriage inward	256	
Rent, Rates & Taxes	956	
Trade receivables	12,560	
Trade payables		8,650
Cash at bank	2,540	
Cash in hand	500	
Head office Account		37,322
Total	2,34,462	2,34,462

Following further information are given:

- (i) Salaries outstanding as on 31st March, 2022 is US\$ 600.
- (ii) Depreciate office equipment and furniture & fixtures @ 10% at written down value.
- (iii) Closing stock as on 31st March, 2022 is US \$, 24,650.
- (iv) You are informed that the Head office is showing receivable from the Branch as ₹ 23,75,614 as on 31st March, 2022. No transaction in respect of the Branch is pending in Head office.
- (v) Office equipment (cost) includes one office equipment of US \$ 2,400 purchased on 1/04/2021.
- (vi) One furniture of carrying value of US \$ 450 as on 01/04/2021 (cost: US \$ 500 and Accumulated depreciation: US \$ 50) has been sold for US \$ 405 on 31/03/2022 to Mr. M at no profit no loss. Mr. M has not paid the amount till the finalization of branch account. No entry has been passed for this sale of furniture in the above trial balance.
- (vii) The rate of exchange on different dates are:

Date	1 US \$ is equivalent to
1st April, 2021	₹ 64
31st December, 2021	₹ 70
31st March, 2022	₹ 75
Average for the year	₹ 72

You are required to prepare the trial Balance after incorporating adjustments given and converting US \$ into rupees.

(RTP May 23)

Answer :

In the books of PQR

Trial Balance (in Rupees) of Houston (USA) Branch – Non–Integral foreign operation as on 31st March, 2022

	Dr.	Cr.	Conversion	Dr.	Cr.
	US \$	US \$	rate	₹	₹
Office Equipment	56,400		75	42,30,000	
Depreciation on Office Equipment		10,500	75		7,87,500

(Accumulated)					
(5,400+5,100)					
Depreciation	8,016		75	6,01,200	
Furniture and fixtures (36,000–500)	35,500		75	26,62,500	
Depreciation on furniture and fixtures (Accumulated)		9,661	75		7,24,575
(6,840–50–45 +2,916)					
Stock (1st April, 2021)	24,500		64	15,68,000	
Purchases	96,500		72	69,48,000	
Sales		1,76,250	72		126,90,000
Carriage inward	256		72	18,432	
Salaries (4,250+600)	4,850		72	3,49,200	
Rent, rates and taxes	956		72	68,832	
Salaries payable		600	75		45,000
Head Office A/c		37,322			23,75,614
					(given)
Trade receivables	12,560		75	9,42,000	
Trade payables		8,650	75		6,48,750
Cash at bank	2,540		75	1,90,500	
Cash in hand	500		75	37,500	
Mr. M	405		75	30,375	
(Receivable for sale of furniture)					
Exchange gain (bal. fig.)					3,75,100
	2,42,983	2,42,983		176,46,539	176,46,539

Closing stock 24,650 US\$ x ₹ 75 = ₹18,48,750.

Question 6

Manohar of Mohali has a branch at Noida to which the goods are supplied from Mohali but the cost thereof is not recorded in the Head Office books. On 31st March, 2020 the Branch Balance Sheet was as follows:

Liabilities	₹	Assets	₹
Creditors Balance	62,000	Debtors Balance	2,24,000
Head Office	1,88,000	Building Extension A/c	
		Closed by transfer to H.O. A/c	-

		Cash at Bank	26,000
	2,50,000		2,00,000

During the six months ending on 30-09-2020, the following transactions took place at Noida:

	₹		₹
Sales	2,78,000	Manager's salary	16,400
Purchases	64,500	Collections from debtors	2,57,000
Wages Paid	24,000	Discounts allowed	16,000
Salaries (inclusive of advance of 5,000)	15,600	Discount earned	4,600
General Expenses	7,800	Cash paid to creditors	88,500
Fire Insurance (Paid for one year)	11,200	Building Account (further payment)	14,000
Remittance to H.O.	52,900	Cash in Hand	5,600
		Cash at Bank	47,000

Set out the Head Office Account in Noida Books and the Branch Balance Sheet as on 30.09.2020.

Also give journal entries in the Noida books.

(MTP Sep '23)

Answer :

Journal Entries in the Books of Noida Branch

Particulars		Debit (₹)	Credit (₹)
Salary Advance A/c	Dr.	5,000	
To Salaries A/c			5,000
(Being the amount paid as advance adjusted by debit to Salary Advance A/c)			
Prepaid Insurance A/c (11,200 X 6/12)	Dr.	5,600	
To Fire Insurance A/c			5,600
(Being the six months premium transferred to the Prepaid Insurance A/c)			
Head Office A/c	Dr.	1,44,900	
To Purchases A/c			64,500
To Wages A/c			24,000
To Salaries A/c (15,600 – 5000)			10,600
To General Expenses A/c			7,800
To Fire Insurance A/c (11,200 X 6/12)			5,600
To Manager's Salary A/c			16,400
To Discount Allowed A/c			16,000
(Being the transfer of various revenue accounts to the HO A/c for closing the accounts)			

Sales A/c	Dr.	2,78,000	
Discount Earned A/c	Dr.	4,600	
To Head Office A/c			2,82,600
(Being the transfer of various revenue accounts to HO)			
Head Office A/c	Dr.	14,000	
To Building A/c			14,000
(Being the transfer of amounts spent on building extension to HO A/c)			

Head Office Account

2020	Particulars	Amount (₹)	2020	Particulars	Amount (₹)
Sept 30	To Cash Remittance	52,900	April 1	By Balance b/d	1,88,000
	To Sundries* (Revenue)	1,44,900		By Sundries* (Revenue)	2,82,600
	To Building A/c	14,000			
	To Balance c/d	2,58,800			
	Total	4,70,600		Total	4,70,600

* Instead of using Sundries (Revenue) A/c, the concerned revenue accounts can be posted in the ledger.

Balance Sheet of Noida Branch As at 30th Sept 2020

Liabilities	Amt (₹)	Assets	Amt (₹)
Creditors	33,400	Debtors	2,29,000
Head Office A/c	2,58,800	Salary Advance	5,000
		Prepaid Insurance	5,600
		Building Extension A/c transferred to HO	
		Cash in Hand	5,600
		Cash at Bank	47,000
Total	2,92,200	Total	2,92,200

Working Notes

Cash and Bank Account

Particulars	Amt (₹)	Particulars	Amt (₹)
To Balance b/d	26,000	By Wages	24,000
To Collection from debtors	2,57,000	By Salaries	15,600
		By Insurance	11,200
		By General Expenses	7,800

		By HO A/c	52,900
		By Manager's Salary	16,400
		By Creditors	88,500
		By Building A/c	14,000
		By Balance c/d	
Total		– Cash in Hand	5,600
		– Cash at bank	47,000
	2,83,000	Total	2,83,000

Debtors Account

Particulars	Amt (₹)	Particulars	Amt (₹)
To Balance b/d	2,24,000	By Cash Collection	2,57,000
To Sales A/c	2,78,000	By Discount (Allowed)	16,000
		By Balance c/d	2,29,000
Total	5,02,000	Total	5,02,000

Creditors Account

Particulars	Amt (₹)	Particulars	Amt (₹)
To Cash A/c	88,500	By Balance b/d	62,000
To Discount (Earned)	4,600	By Purchases	64,500
To Balance c/d	33,400		
Total	1,26,500	Total	1,26,500

Note:

Since the date of payment of fire insurance has not been mentioned in the Question, it is assumed that it was paid on 01 April 2020. Alternative Answer considering otherwise also possible.

Question 7

Walkaway Footwears has its head office at Nagpur and Branch at Patna. It invoiced goods to its branch at 20% less than the list price which is cost plus 100%, with instruction that cash sales were to be made at invoice price and credit sales at catalogue price (i.e. list price).

The following information was available at the branch for the year ended 31 st March,2022.

(Figures in ₹)

Stock on 1st April,2021 (invoice price)	12,000
Debtors on 1st April, 2021	10,000
Goods received from head office (invoice price)	1,32,000
Sales:	
Cash 46,000	
Credit 1,00,000	1,46,000

Cash received. from debtors	85,000
Expenses at branch	17,500
Debtors on 31st March, 2022	25,000
Stock on 31st March,2022 (invoice price)	17,600
Remittances to head office	1,20,000

You are required to prepare Branch Stock Account, Branch Adjustment Account, Branch Profit & Loss Account and Branch Debtors Account for the year ended 31st March, 2022. (PYP May 22)

Answer :

(a) In the books of walkaway footwears

Patna Branch Stock Account

	Particulars	Amount (₹)		Particulars	Amount (₹)
1.1.21	To Balance b/d Goods sent to	12,000	31.12.21	By Bank A/c (Cash sales)	46,000
31.12.21	To branch A/c	1,32,000		By Branch debtors A/c (credit sales)	1,00,000
	To Branch adjustment A/c (Surplus over invoice price)	20,000	31.12.21	By Shortage in stock A/c	400
				By Balance c/d	17,600
		1,64,000			1,64,000

Patna Branch Adjustment Account

	Particulars	Amount (₹)		Particulars	Amount (₹)
31.12.21	To Stock reserve – ₹17,600x 60/160 (closing stock)	6,600	31.12.21	By Stock reserve – ₹12,000x 60/160 (Opening stock)	4,500
	To Shortage (400x 60/160)	150		By Goods sent to branch A/c	49,500
	To Branch profit & loss A/c (Gross profit)	67,250		(₹1,32,000x 60/160)	
				By Branch stock A/c	20,000
		74,000			74,000

Branch Profit & Loss Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Branch expenses A/c	17,500	By Branch adjustment A/c (Gross Profit)	67,250
To Shortage in stock A/c	250		
To Net profit (transferred to Profit & Loss A/c)			

Loss A/c)	49,500		
	67,250		67,250

Branch Debtors Account

	Particulars	Amount (₹)		Particulars	Amount (₹)
1.1.21	To Balance b/d	10,000	31.12.21	By Bank A/c	85,000
31.12.21	To Branch stock A/c	1,00,000		By Balance c/d (bal. fig.)	25,000
		1,10,000			1,10,000



7. CONSOLIDATED FINANCIAL STATEMENTS (AS 21, 23 & 27)

AS – 21: CONSOLIDATED FINANCIAL STATEMENTS

ILLUSTRATIONS

Illustration 1

From the following data, determine in each case:

- (1) Minority interest at the date of acquisition and at the date of consolidation.
- (2) Goodwill or Capital Reserve.
- (3) Amount of holding company's profit in the consolidated Balance Sheet assuming holding company's own Profit & Loss Account to be Rs.2,00,000 in each case:

Case	Subsidiary Company	% shares owned	Cost Rs.	Date of acquisition		Consolidation Date	
				1.1.20X1		31.12.20X1	
				Share Capital Rs.	Profit & Loss Account Rs.	Share Capital Rs.	Profit & Loss Account Rs.
Case 1	A	90%	1,40,000	1,00,000	50,000	1,00,000	70,000
Case 2	B	85%	1,04,000	1,00,000	30,000	1,00,000	20,000
Case 3	C	80%	56,000	50,000	20,000	50,000	20,000
Case 4	D	100%	1,00,000	50,000	40,000	50,000	55,000

Solution:

(1) Minority Interest = Equity attributable to minorities

Equity is the residual interest in the assets of an enterprise after deducting all its liabilities i.e. in this case it should be equal to Share Capital + Profit & Loss A/c

	Minority % Shares Owned [E]	Minority interest as at the date of acquisition [E] x [A + B] Rs.	Minority interest as at the date of consolidation [E] X [C + D] Rs.
Case 1 [100-90]	10 %	15,000	17,000
Case 2 [100-85]	15 %	19,500	18,000
Case 3 [100-80]	20 %	14,000	14,000
Case 4 [100-100]	NIL	Nil	Nil

A = Share capital on 1.1.20X1

B = Profit & loss account balance on 1.1.20X1 C = Share capital on 31.12.20X1

D = Profit & loss account balance on 31.12.20X1

(2) Calculation of Goodwill or Capital Reserve

	Shareholding % [F]	Cost [G]	Total Equity [A] + [B] = [C]	Parent's Portion of equity [F] x [C] =H	Goodwill Rs.[G] – [H]	Capital Reserve Rs.[H] – [G]
Case 1	90 %	1,40,000	1,50,000	1,35,000	5,000	—
Case 2	85 %	1,04,000	1,30,000	1,10,500	—	6,500
Case 3	80 %	56,000	70,000	56,000	Nil	Nil
Case 4	100 %	1,00,000	90,000	90,000	10,000	—

(3) The balance in the Profit & Loss Account on the date of acquisition (1.1.20X1) is Capital profit, as such the balance of Consolidated Profit & Loss Account shall be equal to Holding Co.'s profit.

On 31.12.20X1 in each case the following amount shall be added or deducted from the balance of holding Co.'s Profit & Loss account.

	% Share holding [K]	P & L as on 1.1.20X1 [L]	P & L as on consolidati on date [M]	P & L post acquisition [N] = [M]-[L]	Amount to be added / (deducted) from holding's P & L [O] = [K] x [N]
1	90 %	50,000	70,000	20,000	18,000
2	85 %	30,000	20,000	(10,000)	(8,500)
3	80 %	20,000	20,000	NIL	NIL
4	100 %	40,000	55,000	15,000	15,000

Illustration 2

XYZ Ltd. purchased 80% shares of ABC Ltd. on 1st January, 20X1 for Rs.1,40,000. The issued capital of ABC Ltd., on 1st January, 20X1 was Rs.1,00,000 and the balance in the Profit & Loss Account was Rs.60,000.

During the year ended 31st December, 20X1, ABC Ltd. earned a profit of Rs.20,000 and at year end, declared and paid a dividend of Rs.15,000.

Show by an entry how the dividend should be recorded in the books of XYZ Ltd.

What is the amount of minority interest as on 1st January, 20X1 and 31st December, 20X1? Also please check whether there should be any goodwill/ capital reserve at the date of acquisition.

Solution:

Total dividend paid is Rs.15,000 (assumed to be out of post-acquisition profits), hence dividend received by XYZ will be credited to P & L.

XYZ Ltd.'s share of dividend = Rs.15,000 X 80% = Rs.12,000

In the books of XYZ Ltd.

	Rs.	Rs.
Bank A/c Dr. To Profit & Loss A/c (Dividend received from ABC Ltd credited to P&L A/c being out of post-acquisition profits – as explained above)	12,000	12,000
Goodwill on consolidation (at the date of acquisition):	Rs.	Rs.
Cost of shares		1,40,000
Less: Face value of capital i.e. 80% of capital	80,000	
Add: Share of capital profits [60,000X 80 %]	<u>48,000</u>	<u>(1,28,000)</u>
Goodwill		<u>12,000</u>
Minority interest on:		
- 1st January, 20X1: 20% of Rs.1,60,000 [1,00,000 + 60,000]		32,000
- 31st December, 20X1: 20% of Rs.1,65,000 [1,00,000 + 60,000 + 20,000 – 15,000]		33,000

Illustration 3

Exe Ltd. acquires 70% of equity shares of Zed Ltd. as on 31st March, 20X1 at a cost of Rs.70 lakhs. The following information is available from the balance sheet of Zed Ltd. as on 31st March, 20X1:

	Rs.in lakhs
Property, plant and equipment	120
Investments	55
Current Assets	70
Loans & Advances	15
15% Debentures	90
Current Liabilities	50

The following revaluations have been agreed upon (not included in the above figures): Property, plant and equipment Up by 20% Investments Down by 10%

Zed Ltd. declared and paid dividend @ 20% on its equity shares as on 31st March, 20X1 (Face value - Rs.10 per share). Exe Ltd. purchased the shares of Zed Ltd. @ Rs.20 per share.

Calculate the amount of goodwill/capital reserve on acquisition of shares of Zed Ltd.

Solution:

Revalued net assets of Zed Ltd. as on 31st March, 20X1

	Rs.in lakhs	Rs.in lakhs
Property, plant and equipment [120 X 120%]		144.0

Investments [55 X 90%]		49.5
Current Assets		70.0
Loans and Advances		<u>15.0</u>
Total Assets after revaluation		278.5
Less: 15% Debentures	90.0	
Current Liabilities	<u>50.0</u>	<u>(140.0)</u>
Equity / Net Worth		<u>138.5</u>
Exe Ltd.'s share of net assets (70% of 138.5)		96.95
Exe Ltd.'s cost of acquisition of shares of Zed Ltd. (Rs.70 lakhs – Rs.7 lakhs*)		<u>63.00</u>
Capital reserve		<u>33.95</u>

* Total Cost of 70 % Equity of Zed Ltd Rs.70 lakhs

Purchase Price of each share Rs.20 Number of shares purchased [70 lakhs /Rs.20] 3.5 lakhs Dividend @ 20 % i.e. Rs.2 per share Rs.7 lakhs

Since dividend received is for pre-acquisition period, it has been reduced from the cost of investment in the subsidiary company.

Illustration 4

A Ltd. acquired 70% of equity shares of B Ltd. on 1.4.20X1 at cost of Rs.10,00,000 when B Ltd. had an equity share capital of Rs.10,00,000 and reserves and surplus of Rs.80,000. In the four consecutive years, B Ltd. fared badly and suffered losses of Rs.2,50,000, Rs.4,00,000, Rs.5,00,000 and Rs.1,20,000 respectively. Thereafter in 20X5- X6, B Ltd. experienced turnaround and registered an annual profit of Rs.50,000. In the next two years i.e. 20X6-X7 and 20X7-X8, B Ltd. recorded annual profits of Rs.1,00,000 and Rs.1,50,000 respectively. Show the minority interests and cost of control at the end of each year for the purpose of consolidation.

Solution:

The losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. In such cases, AS 21 prescribes that the excess, and any further losses applicable to the minority, are adjusted against the majority interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses. If the subsidiary subsequently reports profits, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered.

Where the minority interest has a binding obligation (say by way of a shareholders' agreement), then the share of losses will be attributed to the minority interest even if it exceeds the minority interest in the equity (i.e., debit balance in minority interest). Since information on the existence of a binding obligation is not given in the question, we solve as if such obligation does not exist, and hence the minority interests will be computed as follows:

Year	Profit/(Loss)	Minority Interest (30%)	Additional Consolidated P & L (Dr.) Cr. (for the year ended balance)	Minority's Share of losses borne by A Ltd.		Cost of Control
				Rs.	Balance	
At the time of acquisition in 20X1		3,24,000 - (W.N.)	-			
20X1-X2	(2,50,000)	<u>(75,000)</u>	(1,75,000)			2,44,000 (W.N.)
Balance		2,49,000				
20X2-X3	(4,00,000)	<u>(1,20,000)</u>	(2,80,000)			2,44,000
Balance		1,29,000				
20X3-X4	(5,00,000)	<u>(1,50,000)</u>	(3,50,000)			2,44,000
		(21,000)				
	Loss of minority borne by Holding Co.	<u>21,000</u>	<u>(21,000)</u>	21,000	21,000	
Balance		Nil	<u>(3,71,000)</u>			
20X4-X5	(1,20,000)	<u>(36,000)</u>	(84,000)			2,44,000
	Loss of minority borne by Holding Co.	<u>36,000</u>	<u>(36,000)</u>	36,000	57,000	
Balance		Nil	(1,20,000)			
20X5-X6	50,000	15,000	35,000			2,44,000
	Profit share of minority adjusted against losses of minority absorbed by Holding Co.	<u>(15,000)</u>	<u>15,000</u>	(15,000)	42,000	
Balance		Nil	50,000			
20X6-X7	1,00,000	30,000	70,000			
	Profit share of minority adjusted against losses of minority	<u>(30,000)</u>	<u>30,000</u>	(30,000)	12,000	2,44,000
Balance		Nil	100,000			

	absorbed by Holding Co.					
20X7-X8	1,50,000	45,000 <u>(12,000)</u>	1,05,000 <u>12,000</u>	(12,000)	Nil	2,44,000
Balance		33,000	1,17,000			

Working Note:

Calculation of Minority interest and Cost of control on 1.4.20X1

		Share of Holding Co.	Minority Interest
	100%	70%	30%
	(Rs.)	(Rs.)	(Rs.)
Share Capital	10,00,000	7,00,000	3,00,000
Reserve	80,000	<u>56,000</u>	<u>24,000</u>
		7,56,000	<u>3,24,000</u>
Less: Cost of investment		<u>(10,00,000)</u>	
Goodwill		<u>2,44,000</u>	

Illustration 5

Variety Ltd. holds 46% of the paid-up share capital of VR Ltd. The shares were acquired at a market price of Rs.17 per share. The balance of shares of VR Ltd. are held by a foreign collaborating company. A memorandum of understanding has been entered into with the foreign company providing for the following:

- The shares held by the foreign company will be sold to Variety Ltd. The price per share will be calculated by capitalising the yield at 15%. Yield, for this purpose, would mean 40% of the average of pre-tax profits for the last 3 years, which were Rs.30 lakhs, Rs.40 lakhs and Rs.65 lakhs.
- The actual cost of the shares to the foreign company was Rs.5,40,000 only. The profit that would accrue to them would be taxable at an average rate of 30%. The tax payable will be deducted from the proceeds and Variety Ltd. will pay it to the Government.
- Out of the net consideration, 50% would be remitted to the foreign company immediately and the balance will be an unsecured loan repayable after two years.

The above agreement was approved by all concerned for being given effect to on 1.4.20X1. The total assets of VR Ltd. as on 31st March, 20X1 was Rs.1,00,00,000. It was decided to write down Property, Plant and Equipment by Rs.1,75,000. Current liabilities of VR Ltd. as on the same date were Rs.20,00,000. The paid-up share capital of VR Ltd. was Rs.20,00,000 divided into 2,00,000 equity shares of Rs.10 each.

Find out goodwill/capital reserve to Variety Ltd. on acquiring wholly the shares of VR Ltd.

Solution:**1. Computation of Purchase Consideration**

$$(a) \text{ Yield of VR Ltd.: } \left[\frac{40}{100} \times \frac{30+40+65}{3} \right] \quad \text{Rs.18 lakhs}$$

(b) Price per share of VR Ltd.:

$$\text{Capitalized Yield: } \left[\frac{18 \text{ lakhs}}{0.15} \right] \quad \text{Rs.120 lakhs}$$

No. of shares 2 lakhsTherefore, price per share Rs.60**(c) Purchase Consideration for 54% shares in VR Ltd.**2 lakh shares x 54% x Rs.60 per shares Rs.64.80 lakhs**(d) Discharge of Purchase Consideration:**

$$\text{Tax at source (Rs.64.80 lakhs – Rs.5.40 lakhs)} \times \frac{30}{100} \quad \text{Rs.17.82 lakhs}$$
50% of purchase consideration (net of tax) in cash Rs.23.49 lakhs

[Rs.(64.80 – 17.82) x 50%]

Balance – Unsecured Loan Rs.23.49 lakhs**2. Goodwill / Capital Reserve to Variety Ltd.**

	Rs.in lakhs	
Total Assets	100.00	
Less: Reduction in Value of Property, Plant and Equipment	(1.75)	
	98.25	
Less: Current Liabilities	(20.00)	
Net Assets of VR Ltd. on Date of Acquisition		78.25
Purchase Consideration: 54% purchased from Foreign Co.	64.80	
Investment: 46% existing stake	15.64	(80.44)
Goodwill on Date of Acquisition		2.19

Illustration 6

A Ltd. acquired 60% shares of B Ltd. @ Rs.20 per share. Following is the extract of Balance Sheet of B Ltd.:

	Rs.
10,00,000 Equity Shares of Rs.10 each	1,00,00,000
10% Debentures	10,00,000
Trade Payables	55,00,000
Property, Plant and Equipment	70,00,000

Investments	45,00,000
Current Assets	68,00,000
Loans and Advances	22,00,000

On the same day B Ltd. declared dividend at 20% and as agreed between both the companies Property, Plant and Equipment were to be depreciated @ 10% and investment to be taken at market value of Rs.60,00,000. Calculate the Goodwill or Capital Reserve to be recorded in Consolidated Financial Statements.

Solution:

Since dividend is declared by B Ltd. on the date of acquisition itself, it would be out of the divisible profits of B Ltd. existing on the date of acquisition i.e., pre-acquisition profits from the perspective of A Ltd. Accordingly, as per AS 13, such pre-acquisition dividend would be reduced from the cost of investment, as seen below in the determination of Goodwill on the date of acquisition.

	Rs.	Rs.
Assets		
Property, Plant and Equipment	70,00,000	
Less: Value written off (Rs.70 lakhs x 10%)	(7,00,000)	
	63,00,000	
Investments at Market Value	60,00,000	
Current Assets	68,00,000	
Loans and Advances	22,00,000	2,13,00,000
Less: Liabilities		
Trade Payables	55,00,000	
10% Debentures	10,00,000	(65,00,000)
Net Assets of B Ltd.		1,48,00,000
Share of A Ltd. in Net Assets of B Ltd.: 60%		88,80,000
Less: Cost of Investment in B Ltd. (60% stake):		
10,00,000 Equity Shares x 60% x Rs.20 per share	1,20,00,000	
Less: Pre-acquisition dividend: 6,00,000 shares x Rs.2	(12,00,000)	(1,08,00,000)
Goodwill on Date of Acquisition		19,20,000

Illustration 7

H Ltd. acquired 3,000 shares in S Ltd., at a cost of Rs.4,80,000 on 31.7.20X1. The capital of S Ltd. consisted of 5,000 shares of Rs.100 each fully paid. The Profit & Loss Account of this company for 20X1 showed an opening balance of Rs.1,25,000 and profit for the year was Rs.3,00,000. At the end of the year, it declared a dividend of 40%. Record the entry in the books of H Ltd., in respect of the dividend. Assume the profit is accruing evenly and calendar year as financial year.

Solution:

The profits of S Ltd., have to be divided between capital and revenue profits from the point of view of the holding company:

	Capital Profit (Pre- acquisition) Rs.		Revenue Profit (Post- acquisition) Rs.
Balance on 1.1.20X1	1,25,000	—	
Profit for 20X1 ($3,00,000 \times 7/12$)	<u>1,75,000</u>	($3,00,000 \times 5/12$)	<u>1,25,000</u>
Total	3,00,000		1,25,000
Proportionate share of H Ltd. ($3/5$)	1,80,000		75,000

Total dividend declared = $\text{Rs.}5,00,000 \times 40\% = \text{Rs.}2,00,000$

H Ltd.'s share in the dividend = $\text{Rs.}2,00,000 \times 3/5 = \text{Rs.}1,20,000$

There can be two situations as regards the treatment of dividend of Rs.1,20,000:

(1) The profit for 20X1 has been utilised to pay the dividend.

The share of H Ltd in profit for the first seven months of S Ltd = Rs.1,05,000

(i.e. $\text{Rs.}1,75,000 \times 3/5$)

Profit for the remaining five months = Rs.75,000

(i.e. $\text{Rs.}1,25,000 \times 3/5$).

The dividend of Rs.1,20,000 will be adjusted in this ratio of 1,05,000: 75,000 = Rs.70,000 out of profits up to 31.7.20X1 and Rs.50,000 out of profits after that date.

The dividend out of profits subsequent to 31.7.20X1 will be revenue income and that out of earlier profits will be capital receipt. Hence the entry will be:

	Rs.	Rs.
Bank Dr.	1,20,000	
To Investment Account		70,000
To Profit and Loss Account		50,000

(2) Later profits have been utilised first and then pre- acquisition profits.

In such a case, the whole of Rs.75,000 (share of H Ltd. in profits of S Ltd., after 31.7.20X1) would be received and treated as revenue income; the remaining dividend, Rs.45,000 (Rs.1,20,000 less Rs.75,000) would be capital receipt. The entry would be:

	Rs.	Rs.
Bank Dr.	1,20,000	
To Investment Account		45,000
To Profit & Loss Account		75,000

Note: Point (2) discussed above can arise only if there is definite information about the profits utilized. In practice, such treatment is rare.

Illustration 8

A Ltd. and B Ltd. provide the following information:

	Rs. '000s	
	A Ltd.	B Ltd.
Equity Shares	6,000	5,000
6% Preference Shares	NIL	1,000
General Reserve	1,200	800
Profit and Loss Account	1,020	1,790
Trade Payables	3,850	3,410
Dividend Payable	600	500
Goodwill	100	20
Property, Plant and Equipment	3,850	2,750
Investment	1,620	1,100
Inventory	1,900	4,150
Trade Receivables	4,600	4,080
Cash & Bank	600	400

A Ltd. purchased 3/4th interest in B Ltd. at the beginning of the year at the premium of 25%.

Following other information is available:

- Profit & Loss Account of B Ltd. includes ₹ 1,000 thousands brought forward from the previous year.
- The General Reserve balance is brought forward from the previous year.
- The directors of both the companies have declared a dividend of 10% on equity share capital for the previous and current year.

From the above information calculate Pre- and Post-acquisition Profits, Minority Interest and Cost of Control.

Solution:

Calculation of Pre- and Post-Acquisition Profits:

	Pre-Acquisition Profits (₹)	Post-Acquisition Profits (₹)
Profit & Loss Account	10,00,000	7,90,000
General Reserve	8,00,000	NIL
	18,00,000	7,90,000
Less: Share of Minority Interest: ($\frac{1}{4}$)	(4,50,000)	(1,97,500)
Attributable to Parent	13,50,000 (Cost of Control)	5,92,500 (Post-acquisition Profits)

Calculation of Minority Interest:

Particulars	₹
Paid-up Equity Share Capital ($₹ 50,00,000 \times \frac{1}{4}$)	12,50,000
Paid-up Preference Share Capital	10,00,000
Share in Reserves:	
Profit & Loss Account: $₹ 17,90,000 \times \frac{1}{4}$	4,47,500
General Reserve: $₹ 8,00,000 \times \frac{1}{4}$	2,00,000
Minority Interest	28,97,500

Calculation of Goodwill/Capital Reserve

	₹	₹
Cost of Investment in Subsidiary: $₹ 50,00,000 \times 75\% \times 125\%$ (cost + 25% premium)	46,87,500	
Less: Pre-acquisition dividend	(3,75,000)	43,12,500
Less: Net Worth of B Ltd. on Date of Acquisition (attributable to A Ltd.):		
Paid-up Capital	37,50,000	
Pre-acquisition Reserves	13,50,000	(51,00,000)
Capital Reserve		7,87,500

Illustration 9

On 31st March, 20X1, P Ltd. acquired 1,05,000 shares of Q Ltd. for Rs.12,00,000. The position of Q Ltd. on that date was as under:

	Rs.
Property, plant and equipment	10,50,000
Current Assets	6,45,000
1,50,000 equity shares of Rs.10 each fully paid	15,00,000
Pre-incorporation profits	30,000
Profit and Loss Account	60,000
Trade payables	1,05,000

P Ltd. and Q Ltd. give the following information on 31st March, 20X3:

	P Ltd.	Q Ltd.
	Rs.	Rs.
Equity shares of Rs.10 each fully paid (before bonus issue)	45,00,000	15,00,000
Securities Premium	9,00,000	—
Pre-incorporation profits	—	30,000
General Reserve	60,00,000	19,05,000
Profit and Loss Account	15,75,000	4,20,000

Trade payables	5,55,000	2,10,000
Property, plant and equipment	79,20,000	23,10,000
Investment: 1,05,000 Equity shares in Q Ltd. at cost	12,00,000	–
Current Assets	44,10,000	17,55,000

Directors of Q Ltd. made bonus issue on 31.3.20X3 in the ratio of one equity share of Rs.10 each fully paid for every two equity shares held on that date. Bonus shares were issued out of post-acquisition profits by using General Reserve.

Calculate as on 31st March, 20X3 (i) Cost of Control/Capital Reserve; (ii) Minority Interest; (iii) Consolidated Profit and Loss Account in each of the following cases:

(a) Before issue of bonus shares;

(b) Immediately After issue of bonus shares.

Solution:

Shareholding pattern

Particulars	Number of Shares	% of holding
a. P Ltd.		
(i) Purchased on 31.03.20X1	1,05,000	
(ii) Bonus Issue (1,05,000/2)	52,500	
Total	1,57,500	70%
b. Minority Interest	67,500	30%

Calculations of (i) Cost of Control/Capital Reserve; (ii) Minority Interest; (iii) Consolidated Profit and Loss Account as on 31st March, 20X3:

(a) Before issue of bonus shares

(i)	Cost of control/capital reserve	Rs.	Rs.
	Investment in Q Ltd.		12,00,000
	Less: Face value of investments (Share Capital)	10,50,000	
	Capital profits (W.N.)	<u>63,000</u>	<u>(11,13,000)</u>
	Cost of control (i.e., Goodwill)		<u>87,000</u>
(ii)	Minority Interest		Rs.
	Share Capital		4,50,000
	Capital profits (W.N.)		27,000
	Revenue profits (W.N.)		<u>6,79,500</u>
			<u>11,56,500</u>
(iii)	Consolidated profit and loss account – P Ltd.		Rs.
	Balance		15,75,000
	Add: Share in revenue profits of Q Ltd. (W.N.)		<u>15,85,500</u>
			<u>31,60,500</u>

(b) Immediately after issue of bonus shares

(i)	Cost of control/capital reserve	Rs.	Rs.
	Face value of investments (Rs.10,50,000 + Rs.5,25,000)	15,75,000	
	Capital Profits (W.N.)	<u>63,000</u>	16,38,000
	Less: Investment in Q Ltd.		<u>(12,00,000)</u>
	Capital reserve		<u>4,38,000</u>
(ii)	Minority Interest		Rs.
	Share Capital (Rs.4,50,000 + Rs.2,25,000)		6,75,000
	Capital Profits (W.N.)		27,000
	Revenue Profits (W.N.)		<u>4,54,500</u>
			<u>11,56,500</u>
(iii)	Consolidated Profit and Loss Account – P Ltd.		Rs.
	Balance		15,75,000
	Add: Share in revenue profits of Q Ltd. (W.N.)		<u>10,60,500</u>
			<u>26,35,500</u>

Working Note:**Analysis of Profits of Q Ltd.**

	Capital Profits (Pre-acquisition) (Before and after issue of bonus shares) Rs.	Revenue Profits (Post-acquisition)	
		Before Bonus Issue Rs.	After Bonus Issue Rs.
Pre-incorporation profits	30,000		
Profit and loss account on 31.3.20X1	<u>60,000</u>		
	<u>90,000</u>		
General reserve*		19,05,000	19,05,000
Less: Bonus shares			<u>(7,50,000)</u>
			11,55,000
Profit for period of 1st April, 20X1 to 31 st March,		<u>3,60,000</u>	<u>3,60,000</u>
20X3			
(Rs.4,20,000 – Rs.60,000)		<u>22,65,000</u>	<u>15,15,000</u>
P Ltd.'s share (70%)	63,000	15,85,500	10,60,500
Minority's share (30%)	27,000	6,79,500	4,54,500

*Share of P Ltd. in General reserve has been adjusted in Consolidated Profit and Loss Account.

Illustration 10

Prepare consolidated balance sheet of H Ltd. and its subsidiary as at 31 March, 20X1 from the following information:

	H Ltd.	S Ltd.
	Rs.	Rs.
PPE	5,00,000	3,00,000
Investments (20,000 equity shares of S Ltd.)	2,20,000	
Current Assets	1,55,000	1,00,000
Share capital (Fully paid equity shares of Rs.10 each)	5,00,000	2,50,000
Profit and loss account	2,00,000	1,00,000
Trade Payables	1,75,000	50,000

H Ltd. acquired the shares of S Ltd. on 31st March, 20X1.

Solution:

Percentage of holding:

	No. of Shares	Percentage
Holding Co :	20,000	(80%)
Minority shareholders :	<u>5,000</u>	(20%)
TOTAL SHARES :	<u>25,000</u>	

Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 20X1

		Note No	Amount (Rs.)
1	I EQUITY AND LIABILITIES		
	Shareholder's Fund	1	5,00,000
	(a) Share Capital	2	2,60,000
	(b) Reserve and Surplus		
2	Minority interest	3	
3	Current Liabilities		70,000
	(a) Trade payables	4	2,25,000
	Total		10,55,000
	II ASSETS		
1.	Non-Current Assets		
	PPE	5	8,00,000
2.	Current Assets	6	2,55,000
	Total		10,55,000

Notes to Accounts

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		Amounts (Rs.)
1	Share capital 50,000 Equity Shares @ Rs.10 each	5,00,000
2	Reserve and Surplus Capital Reserve (W.N.) Profit and loss account	60,000 2,00,000 2,60,000
3	Minority Interest Paid up value of shares 50,000 Add: Share in Profit and loss account <u>20,000</u>	70,000
4	Trade payables H Ltd. 1,75,000 S Ltd. 50,000	2,25,000
5	PPE H Ltd. 5,00,000 S Ltd. 3,00,000	8,00,000
6	Current Assets H Ltd. 1,55,000 S Ltd. <u>1,00,000</u>	2,55,000

Working Note:

Determination of Goodwill/(Capital Reserve)	(Rs.)
Cost of investment	2,20,000
Less: Paid up value of shares (80% of 2,50,000) 2,00,000	
Share in pre-acquisition profits (80% of 1,00,000) <u>80,000</u>	(2,80,000)
Capital Reserve	(60,000)

Illustration 11

H Ltd. and S Ltd. provide the following information as at 31st March,20X2:

	H Ltd.	S Ltd.
	Rs.	Rs.
PPE	1,00,000	1,30,000
Investments (8,000 equity shares of S Ltd.)	1,26,000	
Current Assets	74,000	70,000

Share capital (Fully paid equity shares of Rs.10 each)	1,50,000	1,00,000
Profit and loss account	50,000	40,000
Trade Payables	1,00,000	60,000

Additional information:

H Ltd. acquired the shares of S Ltd. on 1-7-20X1 and Balance of profit and loss account of S Ltd. on 1-4-20X1 was 30,000.

Prepare consolidated balance sheet of H Ltd. and its subsidiary as at 31st March, 20X2.

Solution:

Percentage of holding:

	No. of Shares	Percentage
Holding Co. :	8,000	(80%)
Minority shareholders :	<u>2,000</u>	(20%)
TOTAL SHARES :	<u>10,000</u>	

Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 20X2

		Note No	Amount (Rs.)
1	I EQUITY AND LIABILITIES		
	Shareholder's Fund		
	(a) Share Capital	1	1,50,000
	(b) Reserve and Surplus	2	56,000
2	(c) Minority interest	3	28,000
3	Current Liabilities		
	(a) Trade payables	4	1,60,000
	Total		3,94,000
	II ASSETS		
1	Non-Current Assets:		
	PPE	5	2,30,000
	Intangible Asset	6	20,000
2	Current Assets	7	1,44,000
	Total		3,94,000

Notes to Accounts

		Amount (Rs.)
1	Share capital 15,000 Equity Shares @ Rs.10 each	1,50,000
2	Reserve and Surplus Profit and loss account (Rs.50,000+ 80% of 9/12 x 10,000)	56,000
3	Minority Interest	

	Share capital (20% of Rs.1,00,000)	20,000	
	Share in Profit and loss account (Rs.40,000 X 20%)	<u>8,000</u>	28,000
4	Trade payables		
	H Ltd.		1,00,000
	S Ltd.		60,000
			1,60,000
5	PPE		
	H Ltd.		1,00,000
	S Ltd.		1,30,000
			2,30,000
6	Intangible Asset		
	Cost of Investment		1,26,000
	Less: Paid up value of shares (80% of Rs.1,00,000)		
	Share in pre-acquisition profits		(80,000)
	80% of [30,000+3/12(40,000-30,000)]		(26,000)
	Goodwill		20,000
7	Current Assets		
	H Ltd.		74,000
	S Ltd.		<u>70,000</u>
			1,44,000

Illustration 12

From the Balance Sheets and information given below, prepare Consolidated Balance Sheet of Virat Ltd. and Anushka Ltd. as at 31st March. Virat Ltd. holds 80% of Equity Shares in Anushka Ltd. since its (Anushka Ltd.'s) incorporation.

Balance Sheet of Virat Ltd. and Anushka Ltd. as at 31st March, 20X1

Particulars	Note No.	Virat Ltd. (Rs.)	Anushka Ltd. (Rs.)
I. Equity and Liabilities			
(1) Shareholder's Funds			
(a) Share Capital	1	6,00,000	4,00,000
(b) Reserves and Surplus	2	1,00,000	1,00,000
(2) Non-current Liabilities			
Long Term Borrowings		2,00,000	1,00,000
(3) Current Liabilities			
(a) Trade Payables		1,00,000	1,00,000

Total		10,00,000	7,00,000
II. Assets			
(1) Non-current assets			
(a) Property, Plant and Equipment		4,00,000	3,00,000
(b) Non-current investments	3	3,20,000	-
(2) Current Assets			
(a) Inventories		1,60,000	2,00,000
(b) Trade Receivables		80,000	1,40,000
(c) Cash & Cash Equivalents		40,000	60,000
Total		10,00,000	7,00,000

Notes to Accounts

	Particulars	(Rs.)	Virat Ltd. (Rs.)	Anushka Ltd. (Rs.)
1. Share capital				
	60,000 equity shares of Rs.10 each fully paid up		6,00,000	--
	40,000 equity shares of Rs.10 each fully paid up		--	<u>4,00,000</u>
	Total		<u>6,00,000</u>	<u>4,00,000</u>
2. Reserves and Surplus				
	General Reserve		<u>1,00,000</u>	<u>1,00,000</u>
	Total		<u>1,00,000</u>	<u>1,00,000</u>
3. Non-current investments				
	Shares in Anushka Ltd		<u>3,20,000</u>	--

Solution:

Consolidated balance Sheet of Virat Ltd. and its Subsidiary Anushka Ltd. as at 31st March, 20X1

Particulars		Note	Amount (Rs.)
I	EQUITY AND LIABILITIES:		
(1)	Shareholders' Funds:		
	(a) Share Capital	1	6,00,000
	(b) Reserve and Surplus	2	1,80,000
(2)	Minority Interest	3	1,00,000
(3)	Non-Current Liabilities:		
	Long Term Borrowings	4	3,00,000
(4)	Current Liabilities:		
	Trade Payables	5	2,00,000
	Total		13,80,000

II (1)	ASSETS:		
	Non-Current Assets		
	Property, Plant & Equipment	6	7,00,000
(2)	Current Assets:		
	(a) Inventories	7	3,60,000
	(b) Trade receivables	8	2,20,000
	(c) Cash and Cash Equivalents	9	1,00,000
	Total		13,80,000

Notes to Accounts

	Particulars	Rs.	Rs.
1.	Share capital 60,000 equity shares of Rs.10 each fully paid up		<u>6,00,000</u>
2.	Reserves and Surplus General Reserve Add: General reserve of Anushka Ltd (80%) Total	1,00,000 <u>80,000</u>	<u>1,80,000</u>
3.	Minority interest 20% share in Anushka Ltd (WN 3)		<u>1,00,000</u>
4.	Long term borrowings Long term borrowings of Virat Add: Long term borrowings of Anushka Total	2,00,000 <u>1,00,000</u>	<u>3,00,000</u>
5.	Trade payables Trade payables of Virat Add: Trade payables of Anushka Total	1,00,000 <u>1,00,000</u>	<u>2,00,000</u>
6.	Property, Plant and Equipment (PPE) PPE of Virat Ltd Add: PPE of Anushka Ltd Total	4,00,000 <u>3,00,000</u>	<u>7,00,000</u>
7.	Inventories Inventories of Virat Ltd Add: Inventories of Anushka Ltd Total	1,60,000 <u>2,00,000</u>	<u>3,60,000</u>
8.	Trade receivables Trade receivables of Virat Ltd Add: Trade receivables of Anushka Ltd Total	80,000 <u>1,40,000</u>	<u>2,20,000</u>

9	Cash and cash equivalents		
	Cash and cash equivalents of Virat Ltd	40,000	
	Add: Cash and cash equivalents of Anushka Ltd	<u>60,000</u>	
	Total		<u>1,00,000</u>

Working Notes:

1. Basic Information

Company Status	Dates	Holding Status
Holding Co. = Virat Ltd. Subsidiary = Anushka Ltd.	Acquisition: Anushka's Incorporation Consolidation: 31 st March, 20X1	Holding Company = 80% Minority Interest = 20%

2. Analysis of General Reserves of Anushka Ltd

Since Virat holds shares in Anushka since its incorporation, the entire Reserve balance of Rs.1,00,000 will be Revenue.

3. Consolidation of Balances

Holding- 80%, Minority - 20%	Total	Minority Interest	Holding Company	
Equity Capital	4,00,000	80,000	3,20,000	-
General Reserves	1,00,000	20,000	Nil (pre-acq)	80,000 (post-acq)
Total		<u>1,00,000</u>	3,20,000	80,000
Cost of Investment			<u>(3,20,000)</u>	-
Goodwill/capital reserve			<u>NIL</u>	
Parent's Balance				1,00,000
Amount for Consolidated Balance Sheet				1,80,000

Illustration 13

From the following balance sheets of H Ltd. And its subsidiary S Ltd. drawn up at 31st March, 20X1, prepare a consolidated balance sheet as at that date, having regard to the following:

- Reserves and Profit and Loss Account of S Ltd. stood at Rs.25,000 and Rs.15,000 respectively on the date of acquisition of its 80% shares by H Ltd. on 1st April, 20X0.
- Machinery (Book-value Rs.1,00,000) and Furniture (Book value Rs.20,000) of S Ltd. were revalued at Rs.1,50,000 and Rs.15,000 respectively on 1st April, 20X0 for the purpose of fixing the price of its shares. [Rates of depreciation computed on the basis of useful lives: Machinery

10%, Furniture 15%.]

Balance Sheet of H Ltd. and S Ltd. as at 31st March, 20X1

Particulars	Note No.	H Ltd. (Rs.)	S Ltd. (Rs.)
I. Equity and Liabilities			
(1) Shareholder's Funds			
(a) Share Capital	1	6,00,000	1,00,000
(b) Reserves and Surplus	2	3,00,000	1,00,000
(2) Current Liabilities			
(a) Trade Payables		1,50,000	57,000
Total		10,50,000	2,57,000
II. Assets			
(1) Non-current assets			
(a) Property, Plant and Equipment	3	4,50,000	1,07,000
(b) Other non-current investments	4	6,00,000	1,50,000
Total		10,50,000	2,57,000

Notes to Accounts

		Rs.	H Ltd. (Rs.)	S Ltd. (Rs.)
1.	Share capital 6,000 equity shares of Rs.100 each, fully paid up 1,000 equity shares of Rs.100 each, fully paid up Total		6,00,000 -- <u>6,00,000</u>	-- <u>1,00,000</u> <u>1,00,000</u>
2.	Reserves and Surplus General reserves Profit and loss account		2,00,000 <u>1,00,000</u>	75,000 <u>25,000</u>
3.	Total Property, Plant and Equipment Machinery Furniture Total		<u>3,00,000</u> 3,00,000 <u>1,50,000</u> <u>4,50,000</u>	<u>1,00,000</u> 90,000 <u>17,000</u> <u>1,07,000</u>
4.	Other Non-current investments Non-current Investments Shares in S Ltd.		4,40,000	1,50,000

	(800 shares at Rs.200 each)		<u>1,60,000</u>	--
	Total		<u>6,00,000</u>	<u>1,50,000</u>

Solution:

Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 20X1

Particulars	Note No.	(Rs.)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	6,00,000
(b) Reserves and Surplus	2	3,44,600
(2) Minority Interest	3	48,150
(3) Current Liabilities		
(a) Trade Payables		2,07,000
Total		11,99,750
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment	4	5,97,750
(b) Intangible assets	5	12,000
(c) Other non-current investments	6	5,90,000
Total		11,99,750

Notes to Accounts

		Rs.		
1.	Share capital			
	6,000 equity shares of Rs.100 each, fully paid up			<u>6,00,000</u>
	Total			<u>6,00,000</u>
2.	Reserves and Surplus			
	Reserves	2,00,000		
	Add: 4/5th share of S Ltd.'s post- acquisition reserves (W.N.3)	<u>40,000</u>		2,40,000
	Profit and Loss Account	1,00,000		
	Add: 4/5th share of S Ltd.'s post- acquisition profits (W.N.4)	<u>4,600</u>		<u>1,04,600</u>
	Total			<u>3,44,600</u>
3.	Minority interest in S Ltd. (WN 5)			48,150
4.	plant and equipment Machinery			
	H. Ltd.	3,00,000		

	S Ltd.	1,00,000		
	Add: Appreciation	<u>50,000</u>		
		1,50,000		
	Less: Depreciation (1,50,000 X 10%)*	<u>(15,000)</u>	1,35,000	
	Furniture			
	H. Ltd.		1,50,000	
	S Ltd.	20,000		
	Less: Decrease in value	<u>(5,000)</u>		
		15,000		
	Less: Depreciation (15,000 X 15%)*	<u>(2,250)</u>	<u>12,750</u>	5,97,750
	Intangible assets			
5.	Goodwill [WN 6]			<u>12,000</u>
	Other non-current investments			
6.	H Ltd.		4,40,000	
	S Ltd.		<u>1,50,000</u>	
	Total			5,90,000

* As an alternative manner of presentation, the Solution: contains only the 'additional depreciation'.

Working Notes:

1. Pre-acquisition profits and reserves of S Ltd.	Rs.
Reserves	25,000
Profit and Loss Account	<u>15,000</u>
	<u>40,000</u>
H Ltd.'s = $\frac{4}{5}$ (or 80%) $\times$ 40,000	32,000
Minority Interest = $\frac{1}{5}$ (or 20%) $\times$ 40,000	8,000
2. Profit on revaluation of assets of S Ltd.	
Profit on Machinery Rs.(1,50,000 – 1,00,000)	50,000
Less: Loss on Furniture Rs.(20,000 – 15,000)	<u>5,000</u>
Net Profit on revaluation	<u>45,000</u>
H Ltd.'s share $\frac{4}{5} \times 45,000$	36,000
Minority Interest $\frac{1}{5} \times 45,000$	9,000
3. Post-acquisition reserves of S Ltd.	
Post-acquisition reserves (Total reserves less pre-acquisition reserves = Rs.75,000 – 25,000)	<u>50,000</u>
H Ltd.'s share $\frac{4}{5} \times 50,000$	40,000
Minority interest $\frac{1}{5} \times 50,000$	<u>10,000</u>
4. Post -acquisition profits of S Ltd.	
Post-acquisition profits (Profit & loss account balance less pre-acquisition	10,000

profits = Rs.25,000 – 15,000)	
Add: Excess depreciation charged on furniture @ 15% on Rs.5,000 i.e. (20,000 – 15,000)	<u>750</u> 10,750
Less: Under depreciation on machinery @ 10% on Rs.50,000 i.e. (1,50,000 – 1,00,000)	<u>(5,000)</u>
Adjusted post-acquisition profits	<u>5,750</u>
H Ltd.'s share $4/5 \times 5,750$	4,600
Minority Interest $1/5 \times 5,750$	<u>1,150</u>
5. Minority Interest	
Paid-up value of (1,000 – 800) = 200 shares held by outsiders i.e. $200 \times \text{Rs.}100$ (or $1,00,000 \times 20\%$)	20,000
Add: $1/5$ th share of pre-acquisition profits and reserves	8,000
$1/5$ th share of profit on revaluation	9,000
$1/5$ th share of post-acquisition reserves	10,000
$1/5$ th share of post-acquisition profit	<u>1,150</u>
	<u>48,150</u>
6. Cost of Control or Goodwill	
Price paid by H Ltd. for 800 shares(A) Intrinsic value of the shares-	1,60,000
Paid-up value of 800 shares held by H Ltd. i.e. $800 \times \text{Rs.}100$ (or $1,00,000 \times 80\%$)	80,000
Add: $4/5$ th share of pre-acquisition profits and reserves	32,000
$4/5$ th share of profit on the revaluation	<u>36,000</u>
Intrinsic value of shares on the date of acquisition (B)	<u>1,48,000</u>
Cost of control or Goodwill (A – B)	12,000

Illustration 14

- A Ltd. holds 80% of the equity capital and voting power in B Ltd. A Ltd. sells inventories costing Rs.180 lacs to B Ltd at a price of Rs.200 lacs. The entire inventories remain unsold with B Ltd. at the financial year end i.e. 31 March 20X1.
- A Ltd. holds 75% of the equity capital and voting power in B Ltd. A Ltd. purchases inventories costing Rs.150 lacs from B Ltd at a price of Rs.200 lacs. The entire inventories remain unsold with A Ltd. at the financial year end i.e. 31 March 20X1.

Suggest the accounting treatment for the above mentioned transactions in the consolidated financial statements of A Ltd. giving reference of the relevant guidance/standard.

Solution:

As per para 16 and 17 of AS 21, intragroup balances and intragroup transactions and resulting unrealized profits should be eliminated in full. Unrealized losses resulting from intragroup transactions should also be eliminated unless cost cannot be recovered.

Intragroup balances and intragroup transactions, including sales, expenses and dividends, are eliminated in full. Unrealized profits resulting from intragroup transactions that are included in the carrying amount of assets, such as inventory and fixed assets, are eliminated in full. Unrealized losses resulting from intragroup transactions that are deducted in arriving at the carrying amount of assets are also eliminated unless cost cannot be recovered.

One also needs to see whether the intragroup transaction is “upstream” or “down- stream”. Upstream transaction is a transaction in which the subsidiary company sells goods to holding company. While in the downstream transaction, holding company is the seller and subsidiary company is the buyer.

In the case of upstream transaction, since the goods are sold by the subsidiary to holding company; profit is made by the subsidiary company, which is ultimately shared by the holding company and the minority shareholders. In such a transaction, if some goods remain unsold at the balance sheet date, the unrealized profit on such goods should be eliminated from minority interest as well as from consolidated profit on the basis of their share-holding besides deducting the same from unsold inventory.

But in the case of downstream transaction, the whole profit is earned by the holding company, therefore, whole unrealized profit should be adjusted from unsold inventory and consolidated profit and loss account only irrespective of the percentage of the shares held by the parent.

Using above mentioned guidance, following adjustments would be required:

- a. This would be the case of downstream transaction. In the consolidated profit and loss account for the year ended 31 March 20X1, entire transaction of sale and purchase of Rs.200 lacs each, would be eliminated by reducing both sales and purchases (cost of sales).

Further, the unrealized profits of Rs.20 lacs (i.e. Rs.200 lacs – Rs.180 lacs), would be eliminated from the consolidated financial statements for financial year ended 31 March 20X1, by reducing the consolidated profits/ increasing the consolidated losses, and reducing the value of closing inventories as of 31 March 20X1.

- b. This would be the case of upstream transaction. In the consolidated profit and loss account for the year ended 31 March 20X1, entire transaction of sale and purchase of Rs.200 lacs each, would be eliminated by reducing both sales and purchases (cost of sales).

Further, the unrealized profits of Rs.50 lacs (i.e. Rs.200 lacs – Rs.150 lacs), would be eliminated in the consolidated financial statements for financial year ended 31 March 20X1, by reducing the value of closing inventories by Rs.50 lacs as of 31 March 20X1. In the consolidated balance sheet as of 31 March 20X1, A Ltd.’s share of profit from B Ltd will be reduced by Rs.37.50 lacs (being

75% of Rs.50 lacs) and the minority's share of the profits of B Ltd would be reduced by Rs.12.50 lacs (being 25% of Rs.50 lacs).

Illustration 15

H Ltd and its subsidiary S Ltd provide the following information for the year ended 31st March, 20X3:

	H Ltd. (Rs.in lacs)	S Ltd. (Rs.in lacs)
Sales and other income	5,000	1,000
Increase in Inventory (closing less opening)	1,000	200
Raw material consumed	800	200
Wages and Salaries	800	150
Production expenses	200	100
Administrative Expenses	200	100
Selling and Distribution Expenses	200	50
Interest	100	50
Depreciation	100	50

Other Information:

H Ltd. sold goods to S Ltd. of Rs.120 lacs at cost plus 20%. Inventory of S Ltd. includes such goods valuing Rs.24 lacs. Administrative expenses of S Ltd. include

Rs.5 lacs paid to H Ltd. as consultancy fees. Selling and distribution expenses of H Ltd. include Rs.10 lacs paid to S Ltd. as commission.

H Ltd. holds 80% of equity share capital of Rs.1,000 lacs in S Ltd. prior to 20X1-20X2. H Ltd. took credit to its Profit and Loss Account, the proportionate amount of dividend declared and paid by S Ltd. for the year 20X1-20X2.

Prepare a consolidated statement of profit and loss..

Solution:

Consolidated statement of profit and loss of H Ltd. and its subsidiary S Ltd. for the year ended on 31st March, 20X3

Particulars	Note No.	Rs.in Lacs
I. Revenue from operations	1	<u>5,865</u>
II. Total Income		<u>5,865</u>
III. Expenses		
Cost of material purchased/consumed	2	1,180
Changes of inventories of finished goods	3	(1,196)
Employee benefit expense	4	950
Finance cost	5	150

Depreciation and amortization expense	6	150
Other expenses	7	<u>535</u>
Total expenses		<u>1,769</u>
IV. Profit before tax (II-III)		<u>4,096</u>

Notes to Accounts

		Rs.in Lacs	Rs.in Lacs
1.	Revenue from operations		
	Sales and other income		
	H Ltd.	5,000	
	S Ltd.	<u>1,000</u>	
		6,000	
	Less: Inter-company sales	(120)	
	Consultancy fees received by H Ltd. from S Ltd.	(5)	
	Commission received by S Ltd. from H Ltd.	<u>(10)</u>	5,865
2.	Cost of material purchased/consumed		
	H Ltd.	800	
	S Ltd.	<u>200</u>	
		1,000	
	Less: Purchases by S Ltd. from H Ltd.	<u>(120)</u>	880
	Direct expenses (Production)		
	H Ltd.	200	
	S Ltd.	<u>100</u>	<u>300</u>
			<u>1,180</u>
3.	Changes of inventories of finished goods		
	H Ltd.	1,000	
	S Ltd.	<u>200</u>	
	Less: Unrealized profits Rs.24 lacs × 20 / 120	<u>(4)</u>	<u>1,196</u>
	H Ltd.		
4.	Employee benefits and expenses		
	Wages and salaries:		
	H Ltd.	800	
	S Ltd.	<u>150</u>	<u>950</u>
5.	Finance cost		
	Interest:		
	H Ltd.	100	
	S Ltd.	<u>50</u>	<u>150</u>

6.	Depreciation		
	H Ltd.	100	
	S Ltd.	<u>50</u>	<u>150</u>
7.	Other expenses		
	Administrative expenses		
	H Ltd.	200	
	S Ltd.	<u>100</u>	
	Less: Consultancy fees received by H Ltd. from S Ltd.	<u>(5)</u>	295
	Selling and distribution Expenses:		
	H Ltd.	200	
	S Ltd.	50	
	Less: Commission received by S Ltd. from H Ltd.	(10)	240
			535

Illustration 16

Subsidiary B Ltd. provides the following balance sheet:

Particulars	Note No.	20X0 (Rs.)	20X1 (Rs.)
I. Equity and Liabilities			
(1) Shareholder's Funds			
(a) Share Capital	1	5,00,000	5,00,000
(b) Reserves and Surplus	2	2,86,000	7,14,000
(2) Current Liabilities			
(a) Short term borrowings	3	--	1,70,000
(b) Trade Payables		4,90,000	4,94,000
(c) Short-term provisions	4	3,10,000	4,30,000
Total		15,86,000	23,08,000
II. Assets			
(1) Non-current assets			
(a) Property, Plant and Equipment	5	2,72,000	2,24,000
(b) Non-current Investment			4,00,000
(2) Current assets			
(a) Inventories		5,97,000	7,42,000
(b) Trade Receivables		5,94,000	8,91,000
(c) Cash & Cash Equivalents		51,000	3,000
(d) Other current assets	6	72,000	48,000

Total		15,86,000	23,08,000
		20X0	20X1
		(Rs.)	(Rs.)
1.	Share capital 5,000 equity shares of Rs.10 each, fully paid up	<u>5,00,000</u>	<u>5,00,000</u>
2.	Reserves and Surplus General Reserves	<u>2,86,000</u>	<u>7,14,000</u>
3.	Short term borrowings Bank overdraft	--	<u>1,70,000</u>
4.	Short term provisions Provision for taxation	<u>3,10,000</u>	<u>4,30,000</u>
5.	Property, plant and equipment Cost Less: Depreciation Total	<u>3,20,000</u> <u>(48,000)</u> <u>2,72,000</u>	<u>3,20,000</u> <u>(96,000)</u> <u>2,24,000</u>
6.	Other current Assets Prepaid expenses	<u>72,000</u>	<u>48,000</u>

Also consider the following information:

- (a) B Ltd. is a subsidiary of A Ltd. Both the companies follow calendar year as the accounting year.
- (b) A Ltd. values inventory on weighted average basis while B Ltd. used FIFO basis. To bring B Ltd.'s values in line with those of A Ltd, its value of inventory is required to be reduced by Rs.12,000 at the end of 20X0 and Rs.34,000 at the end of 20X1.
- (c) B Ltd. deducts 1% from Trade Receivables as a general provision against doubtful debts.
- (d) Prepaid expenses in B Ltd. include advertising expenditure carried forward of Rs.60,000 in 20X0 and Rs.30,000 in 20X1, being part of initial advertising expenditure of Rs.90,000 in 20X0 which is being written off over three years. Similar amount of advertising expenditure of A Ltd. has been fully written off in 20X0.

Restate the balance sheet of B Ltd. as at 31st December, 20X1 after considering the above information, for the purpose of consolidation. Would restatement be necessary to make the accounting policies adopted by A Ltd. and B Ltd. uniform.

Solution:

As per para 20 and 21 of AS 21, Consolidated financial statements:

Consolidated financial statements should be prepared using uniform accounting policies for like transactions and other events in similar circumstances. If it is not practicable to use uniform accounting policies in preparing the consolidated financial statements, that fact should be disclosed together with the proportions of the items in the consolidated financial statements to which the different accounting policies have been applied.

If a member of the group uses accounting policies other than those adopted in the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to its financial statements when they are used in preparing the consolidated financial statements.

Accordingly in the given case, restatement would be required to make the accounting policies of A Ltd and B Ltd uniform.

Adjusted reserves of B Ltd.:

	Rs.	Rs.
Reserves as given		7,14,000
Add: Provision for doubtful debts {[8,91,000 / 99 X 100]-8,91,000}		<u>9,000</u>
		7,23,000
Less: Reduction in value of Inventory	34,000	
Advertising expenditure to be written off	<u>30,000</u>	<u>(64,000)</u>
Adjusted reserves		<u>6,59,000</u>

Note: No adjustment would be required in respect of opening inventory of B Ltd as that will not have any impact on P&L.

Restated Balance Sheet of B Ltd. as at 31st December, 20X1

Particulars	Note No.	(Rs.)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	5,00,000
(b) Reserves and Surplus	2	6,59,000
(2) Current Liabilities		
(a) Short term borrowings	3	1,70,000
(b) Trade Payables		4,94,000
(c) Short-term provision	4	4,30,000
Total		22,53,000
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment	5	2,24,000
(b) Non-current Investment		4,00,000
(2) Current assets		
(a) Inventories	6	7,08,000
(b) Trade Receivables	7	9,00,000
(c) Cash & Cash Equivalents		3,000
(d) Other current assets	8	18,000
Total		22,53,000

Notes to Accounts

			20X1 (Rs.)
1. Share capital			
5,000 equity shares of Rs 10 each, fully paid up			<u>5,00,000</u>
2. Reserves and Surplus			
General Reserves (refer to WN)			<u>6,59,000</u>
3. Short term borrowings			
Bank overdraft			<u>1,70,000</u>
4. Short term provisions			
Provision for taxation			<u>4,30,000</u>
5. Property, plant and equipment			
Cost			3,20,000
Less: Depreciation			<u>(96,000)</u>
Total			<u>2,24,000</u>
6. Inventory			
Actual inventory			7,42,000
Less: Change in method of valuation			<u>(34,000)</u>
Total			<u>7,08,000</u>
7. Trade receivables			
Actual trade receivables			8,91,000
Add: Adjustment for provision			<u>9,000</u>
Total			<u>9,00,000</u>
8. Other current Assets			
Prepaid expenses			<u>48,000</u>



TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. Minority interest should be presented in the consolidated balance sheet
 - (a) As a part of liabilities.
 - (b) As a part of equity of the parent's shareholders.
 - (c) Separately from liabilities and the equity of the parent's shareholders.
 - (d) As a part of assets.

2. Minority of the subsidiary is entitled to
 - (a) Capital profits of the subsidiary company.
 - (b) Revenue profits of the subsidiary company.
 - (c) Both capital and revenue profits of the subsidiary company.
 - (d) Neither capital nor revenue profits of the subsidiary..

3. In consolidation of accounts of holding and subsidiary company is eliminated in full.
 - (a) Current liabilities of subsidiary company.
 - (b) Reserves and surplus of both holding and subsidiary company.
 - (c) Mutual indebtedness.
 - (d) Nothing.

4. In consolidated balance sheet, the share of the outsiders in the net assets of the subsidiary must be shown as
 - (a) Minority interest.
 - (b) Capital reserve.
 - (c) Current liability.
 - (d) Current assets.

5. Provision for Tax made by the subsidiary company will appear in the consolidated balance sheet as an item of
 - (a) Current liability.
 - (b) Revenue profit.
 - (c) Capital profit.
 - (d) Current assets.



Answer to the Multiple Choice Questions

1.	(c)	2.	(c)	3.	(c)	4.	(a)	5.	(a)

SCENARIO-BASED QUESTIONS

6. Hemant Ltd. purchased 80% shares of Power Ltd. on 1st January, 20X1 for Rs.2,10,000. The issued capital of Power Ltd., on 1st January, 20X1 was Rs.1,50,000 and the balance in the Profit & Loss Account was Rs.90,000. During the year ended 31st December, 20X1, Power Ltd. earned a profit of Rs.30,000 and at year end, declared and paid a dividend of Rs.22,500. What is the amount of minority interest as on 1st January, 20X1 and 31st December, 20X1? Also compute goodwill/ capital reserve at the date of acquisition.

Answer:

Total dividend paid is Rs.22,500 (out of post-acquisition profits), hence dividend received by Hemant will be credited to P & L account. Hemant Ltd.'s share of dividend = Rs.22,500 X 80% = Rs.18,000

Goodwill on consolidation (at the date of acquisition):	Rs.	Rs.
Cost of shares		2,10,000
Less: Face value of capital i.e. 80% of capital	1,20,000	
Add: Share of capital profits [90,000 X 80 %]	<u>72,000</u>	<u>(1,92,000)</u>
Goodwill		<u>18,000</u>
Minority interest on:		
- 1st January, 20X1:		
20% of Rs.2,40,000 [1,50,000 + 90,000]		<u>48,000</u>
- 31st December, 20X1:		
20% of Rs.2,47,500 [1,50,000 + 90,000 + 30,000 – 22,500]		<u>49,500</u>

7. King Ltd. acquires 70% of equity shares of Queen Ltd. as on 31st March, 20X1 at a cost of Rs.140 lakhs. The following information is available from the balance sheet of Queen Ltd. as on 31st March, 20X1:

	Rs.in lakhs
Property, plant and equipment	240
Investments	110
Current Assets	140
Loans & Advances	30
15% Debentures	180
Current Liabilities	100

The following revaluations have been agreed upon (not included in the above figures):

Property, plant and equipment- up by 20% and Investments- down by 10%.

King Ltd. purchased the shares of Queen Ltd. @ Rs.20 per share (Face value - Rs.10).

Calculate the amount of goodwill/capital reserve on acquisition of shares of Queen Ltd.

Answer:

Revalued net assets of Queen Ltd. as on 31st March, 20X1

	Rs.in lakhs	Rs.in lakhs
PPE [240 X 120%]		288
Investments [110 X 90%]		99
Current Assets		140
Loans and Advances		<u>30</u>
Total Assets after revaluation		557
Less: 15% Debentures	180.0	
Current Liabilities	<u>100.0</u>	<u>(280)</u>
Equity / Net Worth		<u>277</u>
King Ltd.'s share of net assets (70% of 277)		193.9
King Ltd.'s cost of acquisition of shares of Queen Ltd. (Rs.140 lakhs)		<u>(140)</u>
Capital reserve		53.9

8. From the following information, determine Minority Interest on the date of acquisition and on the date of consolidation in each case:

Case	Subsidiary Company	% of Share owned	Cost	Date of Acquisition		Consolidation date	
				01-01-20X1		31-12-20X1	
				Share Capital	Profit and Loss A/c	Share Capital	Profit and Loss A/c
				Rs.	Rs.	Rs.	Rs.
Case-A	X	90%	2,00,000	1,50,000	75,000	1,50,000	85,000
Case-B	Y	75%	1,75,000	1,40,000	60,000	1,40,000	20,000
Case-C	Z	70%	98,000	40,000	20,000	40,000	20,000
Case-D	M	95%	75,000	60,000	35,000	60,000	55,000

Answer:

Minority Interest = Equity attributable to minorities

Equity is the residual interest in the assets of an enterprise after deducting all its liabilities i.e. in this case, it should be equal to Share Capital + Profit & Loss A/c

A = Share capital on 1.1.20X1

B = Profit & loss account balance on 1.1.20X1 C = Share capital on 31.12.20X1

D = Profit & loss account balance on 31.12.20X1

	Minority % Shares Owned	Minority interest as at the date of acquisition	Minority interest as at the date of consolidation
	[E]	[E] x [A + B] Rs.	[E] X [C + D] Rs.
Case A [100-90]	10 %	22,500	23,500
Case B [100-75]	25 %	50,000	40,000
Case C [100-70]	30 %	18,000	18,000
Case D [100-95]	5%	4,750	5,750

9. A Ltd acquired 1,600 ordinary shares of Rs.100 each of B Ltd on 1st July, 20X1. On 31st December, 20X1, the balance sheets of the two companies were as given below:

Balance Sheet of A Ltd. and its subsidiary, B Ltd. as at 31st December, 20X1

Particulars	Note No.	A Ltd. (Rs.)	B Ltd. (Rs.)
I. Equity and Liabilities			
(1) Shareholder's Funds			
(a) Share Capital	1	5,00,000	2,00,000
(b) Reserves and Surplus	2	2,97,200	1,82,000
(2) Current Liabilities			
(a) Trade Payables		47,100	17,400
(b) Short term borrowings	3	80,000	
Total		9,24,300	3,99,400
II. Assets			
(1) Non-current assets			
(a) Property, Plant and Equipment	4	3,90,000	3,15,000
(b) Non-current Investments	5	3,40,000	--
(2) Current assets			
(a) Inventories		1,20,000	36,400
(b) Trade receivables		59,800	40,000
(c) Cash & Cash equivalents	6	14,500	8,000
Total		9,24,300	3,99,400

Notes to Accounts

		A Ltd. Rs.	B Ltd. Rs.
1.	Share Capital 5,000 shares of Rs.100 each, fully paid up	5,00,000	-

	2,000 shares of Rs.100 each, fully paid up	-	<u>2,00,000</u>
	Total	<u>5,00,000</u>	<u>2,00,000</u>
2.	Reserves and Surplus		
	General Reserves	2,40,000	1,00,000
	Profit & loss	<u>57,200</u>	<u>82,000</u>
	Total	<u>2,97,200</u>	<u>1,82,000</u>
3.	Short term borrowings		
	Bank overdraft	<u>80,000</u>	--
4.	Property plant and equipment		
	Land and building	1,50,000	1,80,000
	Plant & Machinery	<u>2,40,000</u>	<u>1,35,000</u>
	Total	<u>3,90,000</u>	<u>3,15,000</u>
5.	Non-current Investments		
	Investment in B Ltd (at cost)	<u>3,40,000</u>	--
6.	Cash & Cash equivalents		
	Cash	<u>14,500</u>	<u>8,000</u>

The Profit & Loss Account of B Ltd. showed a credit balance of Rs.30,000 on 1st January, 20X1 out of which a dividend of 10% was paid on 1st August, 20X1; A Ltd. credited the dividend received to its Profit & Loss Account. The Plant & Machinery which stood at Rs.1,50,000 on 1st January, 20X1 was considered as worth Rs.1,80,000 on 1st July, 20X1; this figure is to be considered while consolidating the Balance Sheets. The rate of depreciation on plant & machinery is 10% (computed on the basis of useful lives).

Prepare consolidated Balance Sheet as at 31st December, 20X1.

Answer:

Consolidated Balance Sheet of A Ltd. and its subsidiary, B Ltd. as at 31st December, 20X1

Particulars	Note No.	(Rs.)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	5,00,000
(b) Reserves and Surplus	2	3,08,800
(2) Minority Interest		83,600
(3) Current Liabilities		
(a) Trade Payables	3	64,500
(b) Short term borrowings	4	80,000
Total		10,36,900
II. Assets		
(1) Non-current assets		

(a) Property, Plant and Equipment	5	7,41,000
(b) Intangible assets	6	17,200
(2) Current assets		
(a) Inventories	7	1,56,400
(b) Trade receivables	8	99,800
(c) Cash & Cash equivalents	9	22,500
Total		10,36,900

Notes to Accounts

			Rs.
1.	Share Capital		
	5,000 shares of Rs.100 each		<u>5,00,000</u>
2.	Reserves and Surplus		
	Reserves	2,40,000	
	Profit & loss (Refer to W.N 8)	<u>68,800</u>	
	Total		3,08,800
3.	Trade Payables		
	A Ltd. 47,100		
	Add: B Ltd <u>17,400</u>		
	Total		64,500
4.	Short term borrowings		
	Bank overdraft		<u>80,000</u>
5.	Property, plant and equipment		
	Land and building- A Ltd 1,50,000		
	Add: Land and building- B Ltd <u>1,80,000</u>	3,30,000	
	Plant & Machinery (Refer to W.N 7)	<u>4,11,000</u>	
	Total		<u>7,41,000</u>
6.	Intangible assets		
	Goodwill (refer to W.N 6)		<u>17,200</u>
7.	Inventories		
	A Ltd.	1,20,000	
	B Ltd.	<u>36,400</u>	
	Total		<u>1,56,400</u>
8	Trade Receivables		

4. Revenue profits of B Ltd.:

Profit after 1st July, 20X1 $[(82,000 - 10,000) \times \frac{1}{2}]$		36,000
Less: Depreciation		
10% depreciation on Rs.1,80,000 for 6 months	9,000	
Less: Depreciation already charged for 2 nd half year on 1,50,000	<u>(7,500)</u>	<u>(1,500)</u>
		34,500
Less: 1/5 due to outsiders		<u>(6,900)</u>
Share of A Ltd.		<u>27,600</u>

5. Minority interest:

Par value of 400 shares (2,00,000 X 20%)		40,000
Add: 1/5 Capital Profits [WN 3]		36,700
1/5 Revenue Profits [WN 4]		<u>6,900</u>
		<u>83,600</u>

6. Cost of Control:

Amount paid for 1,600 shares	3,40,000	
Less: Dividend out of pre-acquisition profits	<u>(16,000)</u>	3,24,000
Par value of shares	1,60,000	
Capital Profits –share of A Ltd. [WN 3]	<u>1,46,800</u>	<u>(3,06,800)</u>
Cost of Control or Goodwill		<u>17,200</u>

7. Value of plant & Machinery:

B Ltd.	1,35,000	2,40,000
Add: Appreciation on 1st July, 20X1		
$[1,80,000 - (1,50,000 - 7,500)]$	<u>37,500</u>	
	1,72,500	
Add: Depreciation for 2 nd half charged on pre- revalued value	7,500	
Less: Depreciation on Rs.1,80,000 for 6 months	<u>(9,000)</u>	<u>1,71,000</u>
		<u>4,11,000</u>

8. Profit & Loss Account (Consolidated):

A Ltd. as given	57,200	
Less: Dividend transferred to Investment A/c	<u>(16,000)</u>	41,200
Share of A Ltd. in revenue profits of B Ltd. (WN 4)		<u>27,600</u>
		<u>68,800</u>

10. On 31st March, 20X1, the Balance Sheets of H Ltd. and its subsidiary S Ltd. stood as follows:

Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 20X1

Particulars	Note No.	H Ltd. (Rs.in Lacs)	S Ltd. (Rs.in Lacs)
I. Equity and Liabilities			
(1) Shareholder's Funds			
(a) Share Capital	1	12,000	4,800
(b) Reserves and Surplus	2	5,499	3,000
(2) Current Liabilities			
(a) Trade payables	3	1,833	1,014
(b) Short term provisions	4	855	394
(c) Other current liabilities (Dividend payable)		1,200	-
Total		21,387	9,208
II. Assets			
(1) Non-current assets			
(a) Property, Plant and Equipment	5	9,468	5,486
(b) Non-current Investments (Shares in S Ltd.)		3,000	
(2) Current assets			
(a) Inventories		3,949	1,956
(b) Trade receivables	6	2,960	1,562
(c) Cash and cash equivalents		1,490	204
(d) Short term loans and advances	7	520	
Total		21,387	9,208

Notes to Accounts

		H Ltd. (Rs.in lacs)	S Ltd. (Rs.in lacs)
1.	Share Capital		
	Authorized share capital	<u>15,000</u>	<u>6,000</u>
	Equity shares of Rs.10 each, fully paid up		
	Issued and Subscribed:		
	Equity shares of Rs.10 each, fully paid up	12,000	4,800
2.	Reserves and surplus		
	General Reserve	2,784	1,380
	Profit and Loss Account:	<u>2,715</u>	<u>1,620</u>

	Total	<u>5,499</u>	<u>3,000</u>
3.	Trade Payables		
	Creditors	1,461	854
	Bills Payable	<u>372</u>	<u>160</u>
		<u>1,833</u>	<u>1,014</u>
4.	Short term provisions		
	Provision for Taxation	855	394
5.	Property, plant and equipment		
	Land and Buildings	2,718	-
	Plant and Machinery	4,905	4,900
	Furniture and Fittings Total	<u>1,845</u>	<u>586</u>
		<u>9,468</u>	<u>5,486</u>
6.	Trade receivables		
	Debtors	2,600	1,363
	Bills Receivable	<u>360</u>	<u>199</u>
	Total	<u>2,960</u>	<u>1,562</u>
7.	Short term loans and advances		
	Sundry Advances	520	--

The following information is also provided to you:

- H Ltd. purchased 180 lakh shares in S Ltd. on 31st March, 20X0 when the balances of General Reserve and Profit and Loss Account of S Ltd. stood at Rs.3,000 lakh and Rs.1,200 lakh respectively.
- On 1st April, 20X0, S Ltd. declared a dividend @ 20% for the year ended 31st March, 20X0. H Ltd. credited the dividend received by it to its Profit and Loss Account.
- On 1st January, 20X1, S Ltd. issued 3 fully paid-up bonus shares for every 5 shares held out of balances of its general reserve as on 31st March, 20X0.
- On 31st March, 20X1, all the bills payable in S Ltd.'s balance sheet were acceptances in favour of H Ltd. But on that date, H Ltd. held only Rs.45 lakh of these acceptances in hand, the rest having been endorsed in favour of its trade payables.
- On 31st March, 20X1, S Ltd.'s inventory included goods which it had purchased for Rs.100 lakh from H Ltd. which made a profit @ 25% on cost.

Prepare a Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 20X1.

Answer:

Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 20X1

Particulars	Note No.	(Rs.in Lacs)
I. Equity and Liabilities		
(1) Shareholder's Funds		

(a) Share Capital	1	12,000
(b) Reserves and Surplus	2	7,159
(2) Minority Interest [W.N.6]		3,120
(3) Current Liabilities		
(a) Trade payables	3	2,802
(b) Short term provisions	4	1,249
(c) Other current liabilities	5	1,200
Total		27,530
II. Assets		
(1) Non-current assets		
Property, Plant and Equipment	6	14,954
(2) Current assets		
(a) Inventories	7	5,885
(b) Trade receivables	8	4,477
(c) Short term loans and advances	9	520
(d) Cash and cash equivalents	10	1,694
Total		27,530

Notes to Accounts

		(Rs.in lacs)	(Rs.in lacs)
1.	Share Capital		
	Authorized share capital		<u>15,000</u>
	Equity shares of Rs.10 each, fully paid up Issued and Subscribed:		
	Equity shares of Rs.10 each, fully paid up		<u>12,000</u>
	Total		<u>12,000</u>
2.	Reserves and surplus		
	Capital Reserve (Note 5)	1,320	
	General Reserve (2,784 + 108)	2,892	
	Profit and Loss Account:		
	H Ltd.	2,715	
	Less: Dividend wrongly credited	360	
	Unrealized Profit	<u>20</u>	<u>(380)</u>
			2,335
	Add: Share in S Ltd.'s Revenue profits	<u>612</u>	<u>2,947</u>
	Total		<u>7,159</u>
3.	Trade payables		
	Creditors		

	H Ltd. 1,461			
	S Ltd. <u>854</u>		2,315	
	Bills Payable			
	H Ltd. Rs.372			
	S Ltd. <u>Rs.160</u>		<u>487</u>	2,802
4.	Rs.532			
	Less: Mutual owing Rs.(45)			
	Short term provisions Provision for Taxation H Ltd.		855	
	S Ltd.		<u>394</u>	
	Total			1,249
5.	Other current liabilities			
	Dividend payable H Ltd.			1,200
6.	Property, plant and equipment			
	Land and Buildings			
	H Ltd.		2,718	
	Plant and Machinery			
	H Ltd.	Rs.4,905		
	S Ltd.	<u>Rs.4,900</u>	9,805	
	Furniture and Fittings			
	H Ltd.	Rs.1,845		
	S Ltd.	<u>Rs. 586</u>	<u>2,431</u>	
	Total			14,954
7.	Inventories			
	Stock			
	H Ltd.		3,949	
	S Ltd.		<u>1,956</u>	
			5,905	
	Less: Unrealized profit		<u>(20)</u>	5,885
8.	Trade receivables			
	Debtors			
	H Ltd.	Rs.2,600		
	S Ltd.	<u>Rs.1,363</u>	3,963	
	Bills Receivable			
	H Ltd.	Rs.360		
	S Ltd.	<u>Rs.199</u>		
		Rs.559		



	Less: Mutual Owing	Rs. <u>(45)</u>	<u>514</u>	4,477
9.	Short term loans and advances			
	Sundry Advances			520
10.	Cash and cash equivalents			
	Cash and Bank Balances			1,694

Share holding pattern of S Ltd.

Shares as on 31st March, 20X1 (Includes bonus shares issued on 1st January, 20X1)	480 lakh shares (4,800 lakhs/ Rs.10)
H Ltd.'s holding as on 1st April, 20X0	180 lakhs
Add: Bonus received on 1st January, 20X1	108 lakhs (180 / 5 × 3)
Total H Ltd.'s holding as on 31st March, 20X1	288 lakhs i.e. 60 % [288/480×100]
Minority Shareholding	40%

Working Notes:

1. S Ltd.'s General Reserve Account

	Rs.in lakhs		Rs.in lakhs
To Bonus to equity shareholders (WN-8)	1,800	By Balance b/d	3,000
To Balance c/d	<u>1,380</u>	By Profit and Loss A/c	180
	<u>3,180</u>	(Balancing figure)	—
			<u>3,180</u>

2. S Ltd.'s Profit and Loss Account

	Rs.in lakhs		Rs.in lakhs
To General Reserve [WN 1]	180	By Balance b/d	1,200
To Dividend paid (20% on Rs.3,000 lakhs)	600	By Net Profit for the year*	1,200
To Balance c/d	<u>1,620</u>	(Balancing figure)	
	<u>2,400</u>		<u>2,400</u>

*Out of Rs.1,200 lakhs profit for the year, Rs.180 lakhs has been transferred to reserves.

3. Distribution of Revenue profits

	Rs.in lakhs
Revenue profits (W. N. 2)	1,200
Less: Share of H Ltd. 60% (General Reserve Rs.108 + Profit and Loss Account Rs.612)	(720)
Share of Minority Shareholders (40%)	<u>480</u>

Note: The question can also be solved by taking Rs.1,020 lakhs as post acquisition Profit and Loss balance and Rs.180 lakhs as post acquisition General Reserve balance. The final answer will be same.

4. Calculation of Capital Profits

	Rs.in lakhs
General Reserve on the date of acquisition less bonus shares (Rs.3,000 – Rs.1,800)	1,200
Profit and loss account on the date of acquisition less dividend paid (Rs.1,200 – Rs.600)	600
	<u>1,800</u>

H Ltd.'s share = 60% of Rs.1,800 lakhs = Rs.1,080 lakhs
Minority interest = Rs.1,800 – Rs.1,080 = Rs.720 lakhs

5. Calculation of capital reserve

	Rs.in lakhs
Paid up value of shares held (60% of Rs.4,800)	2,880
Add: Share in capital profits [WN 4]	<u>1,080</u>
	3,960
Less: Cost of shares less dividend received (Rs.3,000 – Rs.360)	<u>(2,640)</u>
Capital reserve	<u>1,320</u>

6. Calculation of Minority Interest

	Rs.in lakhs
40% of share capital (40% of Rs.4,800)	1,920
Add: Share in revenue profits [WN 3]	480
Share in capital profits [WN 4]	<u>720</u>
	<u>3,120</u>

7. Unrealized profit in respect of inventory

Rs.100 lakhs x 25/125 = Rs.20 lakhs

8. Computation of bonus to equity shareholders

	Rs.In lakhs
Shares as on 31 March 20X1 including bonus share issued on 1 January 20X1	4,800
Or we can say these are $1 + \frac{3}{5} + \frac{8}{5}$	
i.e. Shares before bonus issue should have been $\frac{4,800}{8/5} =$	3,000
Accordingly, bonus issue would be (4,800-3,000)	1,800

11. Chand Ltd. and its subsidiary Sitara Ltd. provided the following information for the year ended 31st March, 20X4:

Particulars	Chand Ltd (Rs.)	Sitara Ltd. (Rs.)
Equity Share Capital	20,00,000	6,00,000
Finished Goods Inventory as on 01.04.2022	4,20,000	3,01,000

Finished Goods Inventory as on 31.03.2023	8,57,500	3,76,250
Dividend Income	1,68,000	43,750
Other non-operating Income	35,000	10,500
Raw material consumed	13,93,000	4,72,500
Selling and Distribution Expenses	3,32,500	1,57,500
Production Expenses	3,15,000	1,40,000
Loss on sale of investments	26,250	Nil
Sales and other operating income	33,25,000	19,07,500
Wages and Salaries	13,30,000	2,45,000
General and Administrative Expenses	2,80,000	1,22,500
Royalty paid	Nil	5,000
Depreciation	31,500	14,000
Interest expense	17,500	5,250

Other information

- ♦ On 1st September 20X1 Chand Ltd., acquired 5,000 equity shares of Rs.100 each fully paid up in Sitara Ltd.
- ♦ Sitara Ltd. paid a dividend of 10% for the year ended 31st March 20X3. The dividend was correctly accounted for by Chand Ltd.
- ♦ Chand Ltd. sold goods of Rs.1,75,000 to Sitara Ltd. at a profit of 20% on selling price. Inventory of Sitara Ltd. includes goods of Rs.70,000 received from Chand Ltd.
- ♦ Selling and Distribution expenses of Sitara Ltd. include Rs.21,250 paid to Chand Ltd. as brokerage fees.
- ♦ General and Administrative expenses of Chand Ltd. include Rs.28,000 paid to Sitara Ltd. as consultancy fees.
- ♦ Sitara Ltd. used some resources of Chand Ltd., and Sitara Ltd. paid Rs.5,000 to Chand Ltd. as royalty.

Consultancy fees, Royalty and brokerage received is to be considered as operating revenues. Prepare Consolidated Statement of Profit and Loss of Chand Ltd. and its subsidiary Sitara Ltd. for the year ended 31st March, 20X4 as per Schedule III to the Companies Act, 2013.

Answer:

Consolidated statement of profit and loss of Chand Ltd. and its subsidiary Sitara Ltd. for the year ended on 31st March, 20X4

Particulars	Note No.	Rs.
Revenue from operations	1	50,03,250
Other Income	2	<u>1,81,000</u>
Total revenue (I)		<u>51,84,250</u>

Expenses:		
Cost of material purchased/consumed	3	21,45,500
Changes (Increase) in inventories of finished goods	4	(4,98,750)
Employee benefit expense	5	15,75,000
Finance cost	6	22,750
Depreciation and amortization expense	7	45,500
Other expenses	8	<u>8,43,250</u>
Total expenses (II)		<u>41,33,250</u>
Profit before tax (II-III)		<u>10,51,000</u>

Notes to Accounts:

			Rs.	Rs.
1.	Revenue from operations			
2.	Sales and other operating revenues			
	Chand Ltd.		33,25,000	
	Sitara Ltd.		<u>19,07,500</u>	
			52,32,500	
	Less: Inter-company sales		(1,75,000)	
	Consultancy fees received by Sitara Ltd. from Chand Ltd.		(28,000)	
	Royalty received by Chand Ltd. from Sitara Ltd.		(5,000)	
	Brokage received by Chand Ltd. from Sitara Ltd.		<u>(21,250)</u>	50,03,250
2.	Other Income			
	Dividend income:			
	Chand Ltd.	1,68,000		
	Sitara Ltd.	<u>43,750</u>	2,11,750	
	Loss on sale of investments Sitara Ltd.		(26,250)	
	Other Non-operating Income			
	Chand Ltd.	35,000		
	Sitara Ltd.	10,500		
	Less: Dividend realized from Sitara Ltd. (5,00,000 x 10%)	(50,000)	<u>4,500</u>	1,81,000
3.	Cost of material purchased/consumed			
	Chand Ltd.	13,93,000		
	Sitara Ltd.	<u>4,72,500</u>		
		18,65,500		

	Less: Purchases by Sitara Ltd. From Chand Ltd.	<u>(1,75,000)</u>	16,90,500	
	Direct expenses (Production) Chand Ltd.	3,15,000		
	Sitara Ltd.	<u>1,40,000</u>	<u>4,55,000</u>	21,45,500
4.	Changes (Increase) in inventories of finished goods			
	Chand Ltd.		4,37,500	
	Sitara Ltd.		<u>75,250</u>	
			5,12,750	
	Less: Unrealized profits Rs.7,00,00 × 20/100		<u>(14,000)</u>	4,98,750
5.	Employee benefits and expenses			
	Wages and salaries:			
	Chand Ltd.		13,30,000	
	Sitara Ltd.		<u>2,45,000</u>	15,75,000
6	Finance cost Interest:			
	Chand Ltd.		17,500	
	Sitara Ltd.		<u>5,250</u>	22,750
7.	Depreciation			
	Chand Ltd.		31,500	
	Sitara Ltd.		<u>14,000</u>	45,500
8.	Other expenses			
	General & Administrative expenses:			
	Chand Ltd.	2,80,000		
	Sitara Ltd.	<u>1,22,500</u>		
		4,02,500		
	Less: Consultancy fees received by Sitara Ltd. from Chand Ltd.	<u>(28,000)</u>	3,74,500	
	Royalty:			
	Sitara Ltd.	5,000		
	Less: Received by Chand Ltd.	<u>(5,000)</u>	Nil	
	Selling and distribution Expenses:			
	Chand Ltd.	3,32,500		
	Sitara Ltd.	<u>1,57,500</u>		
		4,90,000		
	Less: Brokerage received by Chand Ltd. from Sitara Ltd.	<u>(21,250)</u>	<u>4,68,750</u>	8,43,250

QUESTIONS FROM RTP'S, MTP'S, QP'S

Question 1

A Ltd. had acquired 80% shares of B Ltd. for Rs. 15 lakhs at the beginning of year. During the year, A Ltd. sold the investment for Rs. 30 lakhs and net assets of B Ltd. on the date of disposal was Rs. 35 lakhs. Calculate the profit or loss on disposal of this investment to be recognized in the Financial Statements of A Ltd. (MTP Oct '23)

Answer :

Calculation of Profit/Loss on disposal of investment in subsidiary

Particulars	Rs.
Proceeds from the sale of Investment	30,00,000
Less: A Ltd.'s share in net assets of B Ltd.	(28,00,000)
	2,00,000

Working Note:

A Ltd.'s share in net assets of B Ltd.

	Rs.
Net Assets of B Ltd. on the date of disposal	35,00,000
Less: Minority Interest (20% of Rs. 35 lakhs)	(7,00,000)
A Ltd.'s share in the net assets of B Ltd.	28,00,000



Question 2

On 31st March, 2023 H Ltd. and its subsidiary S Ltd. give the following information:

	H Ltd.	S Ltd.
	Rs.	Rs.
Shareholders' Fund:		
Equity shares of Rs. 10 each	13,40,000	2,40,000
Reserves and Surplus	4,80,000	1,80,000
Profit & Loss Account	2,40,000	60,000
Secured Loans:		
12% Debentures	1,00,000	-
Current Liabilities:		
Creditors	2,00,000	1,22,000
Bank Overdraft	1,00,000	-
Bills Payable	60,000	14,800
Property, Plant & Equipment:		
Machinery	7,20,000	2,16,000
Furniture	3,60,000	40,800

Investments:		
Investments in S Ltd.	3,84,000	-
(19,200 shares at Rs. 20 each)		
Current Assets:		
Inventories	6,00,000	2,00,000
Trade Receivables	3,00,000	90,000
Bill Receivables	1,00,000	30,000
Cash at Bank	56,000	40,000

The following information is also provided to you:

- (a) H Ltd. purchased 19,200 shares of S Ltd. on 1st April, 2019, when the balances of Reserves & Surplus and Profit & Loss Account of S Ltd. stood at Rs. 60,000 and Rs. 36,000 respectively.
- (b) Machinery (Book value Rs. 2,40,000) and Furniture (Book value Rs. 48,000) of S Ltd were revalued at Rs. 3,60,000 and Rs. 36,000 respectively on 1st April, 2019, for the purpose of fixing the price of its shares. (Rates of depreciation computed on the basis of useful lives: Machinery 10%, Furniture 15%).
- (c) On 31st March, 2022, Bills payable of Rs. 12,000 shown in S Ltd.'s Balance Sheet had been accepted in favour of H Ltd.
- (d) You are required to prepare Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 2023.

(MTP March '23 & April '23)

Answer :



Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 2023

Particulars			Note No.	(Rs.)
I.		Equity and Liabilities		
	1	Shareholder's Funds		
		(a) Share Capital	1	13,40,000
		(b) Reserves and Surplus	2	8,27,040
	2	(Minority Interest		1,15,560
	3	Non- Current Liabilities		
		(a) 12% Debentures		1,00,000
	4	Current Liabilities		
		(a) Trade Payables	3	3,84,800
		(b) Short term Borrowings (Bank)		1,00,000
		Total		28,67,400
II.		Assets		
	1	Non-current assets		
		(a)		

	(i) Property, Plant and Equipment	4	14,34,600
	(ii) Intangible assets	5	28,800
2	Current assets		
	(a) Inventory (6,00,000+2,00,000)		8,00,000
	(b) Trade Receivables	6	5,08,000
	(c) Cash and Cash equivalents		96,000
	Total		28,67,400

Notes to Accounts

		Rs.		
1.	Share Capital Equity share capital 1,34,000 shares of Rs. 10 each fully paid up			13,40,000
2.	Reserves and Surplus			
	Reserves		4,80,000	
	Add: 4/5th share of S Ltd.'s post- acquisition reserves (W.N.3)		<u>96,000</u>	5,76,000
	Profit and Loss Account		2,40,000	
	Add: 4/5th share of S Ltd.'s post- acquisition profits (W.N.4)		<u>11,040</u>	<u>2,51,040</u>
3.	Trade Payables			<u>8,27,040</u>
	Creditors			
	H Ltd.	2,00,000		
	S Ltd.	<u>1,22,000</u>	3,22,000	
	Bills Payables			
	H Ltd.	60,000		
	S Ltd.	<u>14,800</u>	<u>74,800</u>	
			3,96,800	
	Less: Mutual Owings		<u>(12,000)</u>	3,84,800
4.	Property Plant and Equipment			
	Machinery			
	H. Ltd.		7,20,000	
	S Ltd.	2,40,000		
	Add: Appreciation	<u>1,20,000</u>		
		3,60,000		
	Less: Depreciation (3,60,000 X 10%)	<u>(36,000)</u>	3,24,000	
	Furniture			
	H. Ltd.		3,60,000	

	S Ltd.	48,000		
	Less: Decrease in value	<u>(12,000)</u>		
		36,000		
	Less: Depreciation (36,000 X 15%)	<u>5,400</u>	<u>30,600</u>	14,34,600
5.	Intangible assets			
	Goodwill [WN 6]			28,800
6.	Trade receivables			
	H Ltd.	3,00,000		
	S Ltd.	<u>90,000</u>	3,90,000	
	Bills Receivables			
	H Ltd.	1,00,000		
	S Ltd.	<u>30,000</u>	<u>1,30,000</u>	
			5,20,000	
	Less: Mutual Owings		<u>(12,000)</u>	5,08,000

Working Notes:

1. Pre-acquisition profits and reserves of S Ltd.	Rs.
Reserves	60,000
Profit and Loss Account	<u>36,000</u>
	<u>96,000</u>
H Ltd.'s = $\frac{4}{5}$ (or 80%) $\times$ 96,000	76,800
Minority Interest = $\frac{1}{5}$ (or 20%) $\times$ 96,000	19,200
2. Profit on revaluation of assets of S Ltd.	
Profit on Machinery Rs. (3,60,000 – 2,40,000)	1,20,000
Less: Loss on Furniture Rs. (48,000 – 36,000)	<u>(12,000)</u>
Net Profit on revaluation	<u>1,08,000</u>
H Ltd.'s share $\frac{4}{5} \times 1,08,000$	86,400
Minority Interest $\frac{1}{5} \times 1,08,000$	21,600
3. Post-acquisition reserves of S Ltd. Total reserves	1,80,000
Less: Pre- acquisition reserves	<u>(60,000)</u>
Post-acquisition reserves	<u>1,20,000</u>
H Ltd.'s share $\frac{4}{5} \times 1,20,000$	96,000
Minority interest $\frac{1}{5} \times 1,20,000$	24,000
4. Post -acquisition profits of S Ltd.	
Post-acquisition profits (Profit & loss account balance less pre-acquisition profits = Rs. 60,000 – 36,000)	24,000
Add: Excess depreciation charged on furniture @ 15%	

on Rs. 12,000 i.e. (48,000 – 36,000)	<u>1,800</u>
Less: Under depreciation on machinery @ 10%	25,800
on Rs. 1,20,000 i.e. (3,60,000 – 2,40,000)	<u>(12,000)</u>
Adjusted post-acquisition profits	<u>13,800</u>
H Ltd.'s share $\frac{4}{5} \times 13,800$	11,040
Minority Interest $\frac{1}{5} \times 13,800$	2,760
5. Minority Interest	
Paid-up value of (24,000 – 19,200) = 4,800 shares	
held by outsiders i.e. 2,40,000 X 20%	48,000
Add: $\frac{1}{5}$ th share of pre-acquisition profits and reserves	19,200
$\frac{1}{5}$ th share of profit on revaluation	21,600
$\frac{1}{5}$ th share of post-acquisition reserves	24,000
$\frac{1}{5}$ th share of post-acquisition profit	<u>2,760</u>
6. Cost of Control or Goodwill	<u>1,15,560</u>
Price paid by H Ltd. for 19,200 shares (A)	3,84,000
Less: Intrinsic value of the shares	
Paid-up value of shares held by H Ltd. i.e. 2,40,000 X 80%	1,92,000
Add: $\frac{4}{5}$ th share of pre-acquisition profits and reserves	76,800
$\frac{4}{5}$ th share of profit on the revaluation	<u>86,400</u>
Intrinsic value of shares on the date of acquisition	(B)
Cost of control or Goodwill B)	(A) – 28,800

Question 3

On 31st March, 2022, H Ltd. and S Ltd. give the following information:

	H Ltd. (Rs.in 000's)	S Ltd. (Rs.in 000's)
Equity Share Capital – Authorised	5,000	3,000
Issued and subscribed in Equity Shares of Rs.10 each fully paid	4,000	2,400
General Reserve	928	690
Profit and Loss Account (Cr. Balance)	1,305	810
Trade payables	611	507
Provision for Taxation	220	180
Other Provisions	65	17
Plant and Machinery	2,541	2,450
Furniture and Fittings	615	298
Investment in the Equity Shares of S Ltd.	1,500	-

Inventory	983	786
Trade receivables	820	778
Cash and Bank Balances	410	102
Sundry Advances (Dr. balances)	260	190

Following Additional Information is available:

- (a) H Ltd. purchased 90 thousand Equity Shares in S Ltd. on 1st April, 2021 at which date the following balances stood in the books of S Ltd.:
- General Reserve Rs.1,500 thousand; Profit and Loss Account Rs.633 thousand.
- (b) On 14th July, 2021 S Ltd. declared a dividend of 20% out of pre-acquisition profits. H Ltd. credited the dividend received to its Profit and Loss Account.
- (c) On 1st November, 2021, S Ltd. issued 3 fully paid Equity Shares of Rs.10 each, for every 5 shares held as bonus shares out of pre-acquisition General Reserve.
- (d) On 31st March, 2021, the Inventory of S Ltd. included goods purchased for Rs.50 thousand from H Ltd., which had made a profit of 25% on cost.
- (e) Details of Trade payables and Trade receivables:

	H Ltd. (Rs.in 000's)	S Ltd. (Rs.in 000's)
Trade payables		
Bills Payable	124	80
Sundry creditors	487	427
Trade receivables	611	507
Debtors	700	683
Bills Receivables	120	95
	820	778

Prepare a consolidated Balance Sheet as on 31st March, 2022.

(RTP Nov'22)

Answer :

Consolidated Balance Sheet of H Ltd. with its subsidiary S Ltd. as at 31st March, 2022

Particulars	Note No.	(Rs.in 000's)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	4,000
(a) Reserves and Surplus	2	3,063
(2) Minority Interest (W.N.6)		1,560
(3) Current Liabilities		
Trade payables	3	1,118
Short term provisions	4	482
Total		10,223

II. Assets		
(1) Non-current assets		
PPE	5	5,904
(2) Current assets		
(a) Inventories	6	1,759
(b) Trade receivables	7	1,598
(c) Cash and cash equivalents	8	512
(d) Short term loans and advances	9	450
Total		10,223

Notes to Accounts

		(Rs.in 000's)	(Rs.in 000's)
1.	Share Capital		
	Authorised share capital		
	5 lakhs equity shares of Rs.10 each		5,000
	Issued, Subscribed and Paid up		
	4 lakhs equity shares of Rs.10 each fully paid		4,000
2.	Reserves and surplus		
	Capital Reserve (Note 5)	679.8	
	General Reserve	928	
	Profit and Loss Account:		
	H Ltd. Rs.1,305		
	Add: Share in S Ltd Rs.340.20		
	Rs.1,645.20		
	Less: Dividend wrongly credited Rs.(180)		
	Rs.1,465.20		
	Less: Unrealised profit (50 X 1/5) Rs.(10)	1,455.20	3,063
3.	Trade payables		
	H Ltd.	611	
	S Ltd.	507	1,118
4.	Short –term provisions		
	Provision for Taxation H Ltd. Rs.220		
	S Ltd. Rs.180	400	
	Other Provisions H Ltd Rs.65		
	S Ltd. Rs.17	82	482
5.	PPE		
	Plant and Machinery		

	H Ltd. Rs.2,541		
	S Ltd. Rs.2,450	4,991	
	Furniture and fittings		
	H Ltd. Rs.615		
	S Ltd. Rs.298	913	5,904
6.	Inventories		
	Inventory		
	H Ltd. Rs.983		
	S Ltd. Rs.786	1,769	
	Less: Unrealised profit (Rs.50 x 1/5)	(10)	1,759
7.	Trade receivables		
	H Ltd.	820	
	S Ltd.	778	1,598
8.	Cash and cash equivalents		
	Cash and Bank Balances H Ltd	410	
	S Ltd.	102	512
9.	Short term loans and advances		
	Sundry Advances H Ltd.	260	
	S Ltd.	190	450

Working Notes:

Share holding pattern

Particulars	Number of Shares	% of holding
a. S Ltd.		
(i) Purchased on 01.04.2021	90,000	
(ii) Bonus Issue (90,000/5 x 3)	54,000	
Total	1,44,000	60% (1,44,000 / 2,40,000* x 100)
b. Minority Interest	96,000	40%

*2,40,000 is after issue of bonus shares as per balance sheet as at 31.3.2022

1. S Ltd. General Reserve

	(Rs.in 000)			(Rs.in 000)	
To	Bonus to equity shareholders	900	By	Balance b/d	1,500
			By	Profit and Loss A/c	
To	Balance c/d $\frac{2,400 \times 3}{8}$	690		(Balancing figure)	90
		1,590			1,590

2. S Ltd.'s Profit and Loss Account

		(Rs.in 000)			(Rs.in 000)
To	General Reserve	90	By	Balance b/d	633
To	Dividend paid on 14.7.2021 $\frac{1,500 \times 20}{100}$	300	By	Net Profit for the year (Balancing figure)	567*
To	Balance c/d	810			
		1,200			1,200

* Out of Rs.5,67,000 profit for the year, Rs.90,000 has been transferred to reserves by S Ltd.

3. Distribution of Revenue Profits

	Rs.in '000
Revenue Profit as above	567.00
Share of H Ltd. (60%)	340.20
Share of Minority shareholders (567– 340.20)	226.80

4. Computation of Capital Profits

	Rs.in 000	Rs.in 000
General Reserve on the date of acquisition		1,500
Less: Bonus issue of shares		(900)
Profit and Loss Account balance on the date of acquisition	633	600
Less: Dividends paid	(300)	333
		933
Share of H Ltd. (60%)		559.80
Share of Minority shareholders		373.20

5. Computation of Capital Reserve

	Rs.in '000
60% of share capital of S Ltd.	1,440
Add: Share of H Ltd. in the capital profits as in working note (4)	559.80
Less: Investments in S Ltd.	1,500
Less: Dividends received out of pre- acquisition profits $\frac{30 \times 60}{100}$	(180)
	679.80

6. Calculation of Minority Interest

	Rs.in '000
40% of share capital of S Ltd.	960.00
Add: Share of Revenue Profits (Note 3)	226.80
Share of Capital Profits (Note 4)	373.20
	1,560.00

Question 4

H Ltd acquired 15000 shares in S Ltd. for 1,55,000 on July 1, 2022. The Balance sheet of the two companies as on 31st March, 2023 were as follows:

	H Ltd.Rs.	S Ltd.Rs.
Equity and Liabilities:		
Equity Share Capital	9,00,000	2,50,000
(Fully paid shares of Rs.10 each)		
General Reserve	1,60,000	40,000
Surplus i.e., Balance in Statement of Profit and	80,000	25,000
Loss	40,000	20,000
Bills payable Trade Creditors	50,000	30,000
Total	12,30,000	3,65,000
Assets		
Machinery	7,00,000	1,50,000
Furniture	1,00,000	70,000
Investment in Equity Shares of S Ltd.	1,55,000	-
Stock-in Trade	1,00,000	50,000
Trade Debtors	60,000	35,000
Bills Receivable	25,000	20,000
Cash at Bank	90,000	40,000
Total	12,30,000	3,65,000

The following additional information is provided to you:

- (i) General reserve appearing in the Balance Sheet of S Ltd. remained unchanged since 31st March, 2022.
- (ii) Profit earned by S Ltd. for the year ended 31st March, 2023 amounted to Rs.20,000.
- (iii) H Ltd. sold goods to S Ltd. costing Rs.8,000 for Rs.10,000, 25% of these goods remained unsold with S Ltd. on 31st March, 2023.
- (iv) Creditors of S Ltd. include Rs.4000 due to H Ltd. on account of these goods.
- (v) Out of Bills payable issued by S Ltd. Rs.15,000 are those which have been accepted in favour of H Ltd. Out of these, H Ltd. had endorsed by 31st March, 2023, Rs.8000 worth of bills receivable in favour of its creditors.

You are required to draw a consolidated Balance Sheet as on 31st March, 2023. (PYP May '23)

Answer :

Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 2023

Particulars	Note No.	(Rs.)
I. Equity and Liabilities		
(1) Shareholder's Funds		

(a) Share Capital	1	9,00,000
(b) Reserves and Surplus	2	2,73,500
(2) Minority Interest	3	1,26,000
(3) Current Liabilities	4	
(a) Trade Payables		1,29,000
Total		14,28,500
II. Assets		
(1) Non-current assets	5	
(a) Property, Plant and Equipment		10,20,000
(2) Current assets		
(i) Inventory	6	1,49,500
(ii) Trade Receivables	7	1,29,000
(iii) Cash & cash equivalent	8	1,30,000
Total		14,28,500

Notes to Accounts

			Rs.
1.	Share capital Authorised, issued, subscribed and paid up capital 90,000 equity shares of Rs.10 each, fully paid up		9,00,000
2.	Reserves and Surplus General Reserves	1,60,000	
	Profit and Loss Account (W.N.5)	88,500	
	Capital Reserve (W.N. 4)	25,000	2,73,500
3.	Minority interest in S Ltd. (WN 3)		1,26,000
4.	Trade payables Bills Payable H Ltd. 40,000 S Ltd. 20,000 60,000 Less: Mutual payables (7,000)	53,000	
	Trade Creditors H Ltd. 50,000 S Ltd. 30,000 80,000 Less: Mutual owing (4,000)	76,000	1,29,000
5.	Property, plant and equipment Machinery H Ltd. 7,00,000 S Ltd. 1,50,000	8,50,000	

	Furniture			
	H Ltd.	1,00,000		
	S Ltd.	70,000	1,70,000	10,20,000
6.	Inventory			
	H Ltd.		1,00,000	
	S Ltd.		50,000	
	Less: Unrealized profit (2,000x 25%)		500	1,49,500
7.	Trade receivables Bills receivable			
	H Ltd.	25,000		
	S Ltd.	20,000		
		45,000		
	Less: Mutual payables	(7,000)	38,000	
	Debtors			
	H Ltd.	60,000		
	S Ltd.	35,000		
		95,000		
	Less: Mutual owing	(4,000)	91,000	1,29,000
8.	Cash & cash equivalent Cash at Bank			
	H Ltd.		90,000	
	S Ltd.		40,000	1,30,000

Working Notes:

1. Percentage of holding

	No. of Shares	Percentage
Holding Co.	15,000	(60%)
Minority shareholders	10,000	(40%)
Total Shares	25,000	

2. Analysis of Profits

	Pre-acquisition profits and reserves of S Ltd. (Rs.)	Post- acquisition profits of S Ltd. (Rs.)
General Reserve	40,000	---
Opening balance of Profit and Loss	5,000	---
Current Year's profit (in 1:3)	5,000	15,000
H Ltd.'s share (60%)	50,000	15,000
Minority Interest (40%)	30,000	9,000
	20,000	6,000

3. Minority Interest

Paid up value of 10,000 shares @ Rs.10 each	Rs.1,00,000
Add: Share in pre-acquisition profits and reserve (40%)	Rs.20,000
Add: Share in post-acquisition profits (40%)	Rs. 6,000
	Rs. 1,26,000

4. Capital Reserve for H Ltd.

(A)	Cost of acquiring 15,000 shares of S Ltd.	Rs.1,55,000
(B)	Paid up value of 15,000 shares of S Ltd. @ Rs.10 each	Rs.1,50,000
	Add: Share in pre-acquisition profit and reserves of S Ltd.	Rs.30,000
		Rs. 1,80,000
	Capital Reserve (B-A)	Rs.25,000

5. Consolidated Balance of Profits of H Ltd.

	Balance as per Statement of Profit and Loss	Rs.80,000
	Add: Share in post-acquisition profits of S Ltd.	Rs.9,000
	Less: Unrealised Profit in unsold stock of S Ltd.	Rs.(500)
		Rs.88,500

Question 5

White Ltd. acquired 2,250 shares of Black Ltd. on 1st October, 2020. The summarized balance sheets of both the companies as on 31st March, 2021 are given below:

	White Ltd. (₹)	Black Ltd. (₹)
(I) Equity and Liabilities		
1. Shareholder's fund		
Share capital (Equity shares of ₹ 100 each fully paid up)	6,50,000	3,00,000
Reserves and Surplus	60,000	30,000
General Reserve	1,50,000	90,000
Profit and loss account	1,15,000	75,000
2. Current Liabilities		
Trade payables Due to White Ltd.	-	30,000
Total	9,75,000	5,25,000
(II) Assets:		
Non-current assets		
Property, Plant and Equipment	5,80,000	3,51,000
Investments		

Shares in Black Ltd. (2,250 shares)	2,70,000	
Current assets		
Inventories	50,000	1,20,000
Due from Black Ltd.	36,000	
Cash and Cash equivalents	39,000	54,000
Total	9,75,000	5,25,000

Other information:

- (i) During the year, Black Limited fabricated a machine, which is sold to White Ltd. for ₹ 39,000, the transaction being completed on 30th March, 2021.
- (ii) Cash in transit from Black Ltd. to White Ltd. was ₹ 6,000 on 31st March, 2021. Profits during the year 2020-2021 were earned evenly
- (iii) The balances of Reserve and Profit and Loss account as on 1st April, 2020 were as follows:

	Reserves	Profit and Loss A/c
	₹	₹
White Ltd.	30,000	15,000 Profit
Black Ltd.	30,000	10,000 Loss

You are required to prepare consolidated Balance Sheet of the group as on 31st March, 2021 as per the requirement of Schedule III of the Companies Act, 2013. (PYP May '22)

Answer :

Consolidated Balance Sheet of White Ltd. and its Subsidiary Black Ltd. as at 31st March, 2021

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	6,50,000
(b) Reserves and Surplus	2	2,55,000
(2) Minority Interest	3	1,05,000
(3) Current Liabilities		
(a) Trade Payables	4	1,90,000
Total		12,00,000
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment	5	9,31,000
(2) Current assets		
(i) Inventory	6	1,70,000

(ii) Cash & cash equivalent	7	99,000
Total		12,00,000

Notes to Accounts

			₹
1.	Share capital		
	6,500 equity shares of ₹ 100 each, fully paid up		6,50,000
	Total		6,50,000
2.	Reserves and Surplus		
	General Reserves		60,000
	Profit and Loss Account	1,50,000	
	Add: 75% share of Black Ltd.'s post-acquisition profits (W.N.1)	37,500	1,87,500
	Capital reserve (W.N. 5)		7,500
	Total		2,55,000
3.	Minority interest in Black Ltd. (WN 4)		1,05,000
4.	Trade payables		
	White Ltd.	1,15,000	
	Black Ltd.	75,000	1,90,000
5.	Property, plant and equipment		
	White Ltd.	5,80,000	
	Black Ltd.	3,51,000	9,31,000
6	Inventory		
	White Ltd.	50,000	
	Black Ltd.	1,20,000	1,70,000
7	Cash & cash equivalent		
	White Ltd.	39,000	
	Black Ltd.	54,000	
	Cash in transit	6,000	99,000

Working Notes:

1. Post-acquisition profits of Black Ltd.	Rs.
Profits earned during the year = ₹ 90,000 + ₹10,000	1,00,000
Pre-acquisition profits (1.4.20 to 30.9.20)	50,000
Post-acquisition profits (1.10.20 to 31.3.21)	50,000
White Ltd.'s share 75% of 50,000	37,500
Minority Interest 25% of 50,000	12,500
2. Pre-acquisition profits and reserves of Black Ltd.	
Reserves as on 1.4.2020	30,000

Profit and Loss Account [10,000 (loss as on 1.4.20) +50,000 (6 month Adjusted pre-acquisition profits)]		40,000
		70,000
White Ltd.'s = (75%) × 70,000		52,500
Minority Interest= (25%) × 70,000		17,500
3. Post-acquisition reserves of Black Ltd.		
Post-acquisition reserves (Total reserves less pre-acquisition reserves = ₹30,000 – 30,000)		Nil
4. Minority Interest		
Paid-up value of (3,000 – 2,250) = 750 shares		
held by outsiders i.e. 750 × ₹ 100		75,000
Add: 25% share of pre-acquisition reserves & Profit		17,500
25% share of post-acquisition profit		12,500
5. Capital Reserve		1,05,000
Price paid by White Ltd. for 2,250 shares (A)		2,70,000
Intrinsic value of the shares-		
Paid-up value of 2,250 shares held by White Ltd. i.e. 2,250 × ₹ 100	2,25,000	
Add 75% share of pre-acquisition reserves & profit (70,000 × 75%)	52,500 (B)	2,77,500
Capital reserve (A – B)		7,500

AS - 23: ACCOUNTING FOR INVESTMENTS IN ASSOCIATES IN CONSOLIDATED FINANCIAL STATEMENTS

ILLUSTRATIONS

Illustration 1

A Ltd. acquire 45% of B Ltd. shares on April 01, 20X1, the price paid was Rs.15,00,000. Following are the extracts of balance sheet of B Ltd. as of 1 April 20X1: Paid up

Equity Share Capital	Rs.10,00,000
Securities Premium	Rs.1,00,000
Reserve & Surplus	Rs.5,00,000

B Ltd. has reported net profits of Rs.3,00,000 and paid dividends of Rs.1,00,000 for the year ended 31 March 20X2. Calculate the amount at which the investment in B Ltd. should be shown in the consolidated balance sheet of A Ltd. as on March 31, 20X2.

Solution:

Calculation of Goodwill/Capital Reserve under Equity Method

Particulars	Rs.	Rs.
Investment in B Ltd. (A)		15,00,000
Equity Shares	10,00,000	
Security Premium	1,00,000	
Reserves & Surplus	<u>5,00,000</u>	
Net Assets	<u>16,00,000</u>	
45% of Net Asset (B)		<u>7,20,000</u>
Goodwill (A-B)		<u>7,80,000</u>

Calculation of Carrying Amount of Investment in the year ended on 31st March, 20X2

Particulars	Rs.
Investment in Associate as per AS 23:	
Share of Net Assets on 1 April 20X1	7,20,000
Add: Goodwill	<u>7,80,000</u>
Cost of Investment	15,00,000
Add: Profit during the year (3,00,000 x 45%)	1,35,000
Less: Dividend paid (1,00,000 x 45%)	<u>(45,000)</u>
Carrying Amount of Investment	<u>15,90,000</u>

Illustration 2

A Ltd. acquired 40% share in B Ltd. on April 01, 20X1 for Rs.10 lacs. On that date B Ltd. had 1,00,000 equity shares of Rs.10 each fully paid and accumulated profits of Rs.2,00,000. During the year 20X1-20X2, B Ltd. suffered a loss of Rs.10,00,000; during 20X2-20X3 loss of Rs.12,50,000 and during 20X3-20X4 again a loss of Rs.5,00,000. Show the extract of consolidated balance sheet of A Ltd. on all the four dates recording the above events.

Solution:

Calculation of Goodwill/Capital Reserve under Equity Method

Particulars	Rs.
Equity Shares	10,00,000
Reserves & Surplus	<u>2,00,000</u>
Net Assets	12,00,000
40% share of Net Assets	4,80,000
Less: Cost of Investment	<u>(10,00,000)</u>
Goodwill	<u>5,20,000</u>

Consolidated Balance Sheet (Extract) as on April 01, 20X1: ASSETS

Investment in Associate as per AS 23	Rs.	Rs.
Share of Net Assets on April 1	4,80,000	
Add: Goodwill	<u>5,20,000</u>	10,00,000

Calculation of Carrying Amount of Investment as at 31 March 20X2:

Investment in Associate as per AS 23	Rs.
Share of Net Assets on 1 April, 20X1	4,80,000
Add: Goodwill	<u>5,20,000</u>
Cost of Investment	10,00,000
Less: Loss for the year (10,00,000 x 40%)	<u>(4,00,000)</u>
Carrying Amount of Investment	<u>6,00,000</u>

Consolidated Balance Sheet (Extract) as on March 31, 20X2: ASSETS

Investment in Associate as per AS 23	Rs.	Rs.
Share of Net Assets on 1 April, 20X1	4,80,000	
Less: Share of Loss as above	(4,00,000)	
	80,000	
Add: Goodwill	<u>5,20,000</u>	6,00,000

Calculation of Carrying Amount of Investment as at 31 March 20X3:

Investment in Associate as per AS 23	Rs.
Carrying Amount of Investment as on 31 March 20X2	6,00,000
Less: Loss for the year (12,50,000 x 40%)	<u>(5,00,000)</u>
Carrying Amount of Investment	<u>1,00,000</u>

Consolidated Balance Sheet (Extract) as on March 31, 20X3: ASSETS

Investment in Associate as per AS 23	Rs.	Rs.
Share of Net Assets on 1 April, 20X1	4,80,000	
Less: Share of Loss as above (Rs. 4,00,000 + Rs.5,00,000)	(4,20,000)	
Add: Goodwill		1,00,000

Calculation of Carrying Amount of Investment as at 31 March 20X4:

Investment in Associate as per AS 23	Rs.
Carrying Amount of Investment	1,00,000
Less: Loss for the year (5,00,000 x 40% = 2,00,000, restricted to Carrying amount of Investment in B Ltd.) -refer note below	
Carrying Amount of Investment	

Consolidated Balance Sheet (Extract) as on March 31, 20X4: ASSETS

Investment in Associate as per AS 23	Rs.
Investment in B Ltd.	-

- ◆ If, under the equity method, an investor's share of losses of an associate equals or exceeds the carrying amount of the investment, the investor ordinarily discontinues recognising its share of further losses and the investment is reported at nil value. Additional losses are provided for to the extent that the investor has incurred obligations or made payments on behalf of the associate to satisfy obligations of the associate that the investor has guaranteed or to which the investor is otherwise committed. If the associate subsequently reports profits, the investor resumes including its share of those profits only after its share of the profits equals the share of net losses that have not been recognised.
- ◆ As far as possible the reporting date of the financial statements should be same for consolidated financial statement. If practically it is not possible to draw up the financial statements of one or more enterprise to such date and, accordingly, those financial statements are drawn up to reporting dates different from the reporting date of the investor, adjustments should be made for the effects of significant transactions or other events that occur between those dates and the date of the consolidated financial statements. In any case, the difference between reporting dates of the concern and consolidated financial statement should not be more than six months.
- ◆ Accounting policies followed in the preparation of the financial statements of the investor, investee and consolidated financial statement should be uniform for like transactions and other events in similar circumstances.
If accounting policies followed by different enterprises in the group are not uniform, then adjustments should be made in the items of the individual financial statements to bring it in line with the accounting policy of the consolidated statement.
- ◆ The carrying amount of investment in an associate should be reduced to recognise a decline, other than temporary, in the value of the investment, such reduction being determined and made for each investment individually.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. Identity which of the statements are correct.

An enterprise can influence the significant economic decision making by many ways like:

- (i) Representation on the board of directors or governing body of the investee.
- (ii) Participation in policy-making processes.
- (iii) Interchange of managerial personnel.
- (iv) Provision of essential technical information.

- (a) Statement (i) and (ii) are correct.
- (b) Statement (i), (ii) and (iii) are correct.
- (c) Statement (i), (ii), (iii) and (iv) are correct.
- (d) Statement (ii) and (iii) are correct.

2. A Ltd. is holding 90% share in B Ltd. and 10% shares in C Ltd., and B Ltd. is holding 11% shares in C Ltd.

Identity which of the statements are incorrect.

- (i) In this case, A Ltd. is parent of B Ltd.
- (ii) As far as the relationship between A Ltd. and C Ltd. is concerned; A Ltd. has a total of direct and indirect holding of $(10\% + 90\% \text{ of } 11\%)$ 19.9 % in C Ltd.

- (iii) C Ltd. is an associate of A Ltd.

- (a) Statement (ii) is incorrect.
- (b) Statement (iii) is incorrect.
- (c) Statement (ii) and (iii) both are incorrect.
- (d) All statements are incorrect.

3. A Ltd. acquired 10% stake of B Ltd. on April 01 and further 15% on October 01 of the same year.

Other information is as follows:

Cost of Investment for 10% Rs.1,00,000 and for 15% Rs.1,55,000

Net asset on April 01 Rs.8,50,000 and on October 01 Rs.10,00,000.

What is the amount of goodwill or capital reserve arising on significant influence?

- (a) Goodwill = Rs.10,000.
- (b) Goodwill = Rs.20,000.
- (c) Capital Reserve = Rs.10,000.
- (d) Capital Reserve = Rs.20,000.

4. A Ltd. acquired 10% stake of B Ltd. on April 01 and further 15% on October 01 during the same year. Other information is as follow:

Cost of Investment for 10% Rs.1,00,000 and for 15% Rs.1,45,000

Net asset on April 01 Rs.8,50,000 and on October 01 Rs.10,00,000.

What is the amount of goodwill or capital reserve arising on significant influence?

- (a) Goodwill = Rs.10,000.
- (b) Goodwill = Rs.20,000.
- (c) Capital Reserve = Rs.10,000.
- (d) Capital Reserve = Rs.20,000.

5. Identity which of the statements are correct.

- (i) In case an associate has made a provision for proposed dividend (i.e. dividend declared after the reporting period but it pertains to that reporting year) in its financial statements, the investor's share of the results of operations of the associate should be computed without taking into consideration the proposed dividend.
 - (ii) In case an associate has made a provision for proposed dividend (i.e. dividend declared after the reporting period but it pertains to that reporting year) in its financial statements, the investor's share of the results of operations of the associate should be computed after taking into consideration the proposed dividend.
 - (iii) The potential equity shares of the investee held by the investor should not be taken into account for determining the voting power of the investor.
 - (iv) The potential equity shares of the investee held by the investor should be taken into account for determining the voting power of the investor.
- (a) Statement (i) and (iii).
 - (b) Statement (ii) and (iv).
 - (c) Statement (i) only.
 - (d) Statement (iii) only.

Answer to the Multiple Choice Questions

1.	(c)	2.	(a)	3.	(b)	4.	(a)	5.	(a)

THEORETICAL QUESTIONS

6. Describe the cases when AS 23 does not allow the use of equity method of accounting?

Answer:

Equity method of accounting is to be followed by all the enterprises having significant influence on their associates except in the following cases:

- a. Control is intended to be temporary because the investment is acquired and held exclusively with a view to its subsequent disposal in the near future.

The term 'Near Future' is explained with AS 21.

Or;

- b. It operates under severe long-term restrictions, which significantly impair its ability to transfer funds to the investor.

In both the above cases, investment of investor in the share of the investee is treated as investment according to AS 13.

7. When is an investor required to discontinue the use of the equity method of accounting?

Answer:

An investor should discontinue the use of the equity method from the date that:

- a. It ceases to have significant influence in an associate but retains, either in whole or in part, its investment.
- b. The use of the equity method is no longer appropriate because the associate operates under severe long-term restrictions that significantly impair its ability to transfer funds to the investor.

From the date of discontinuing the use of the equity method, investments in such associates should be accounted for in accordance with AS 13, Accounting for Investments. For this purpose, the carrying amount of the investment at that date should be regarded as cost thereafter.

SCENARIO BASED QUESTIONS

8. Bright Ltd. acquired 30% of East India Ltd. shares for Rs.2,00,000 on 01-06-20X1. By such an acquisition Bright can exercise significant influence over East India Ltd. During the financial year ending on 31-03-20X1 East India earned profits Rs.80,000 and declared a dividend of Rs.50,000 on 12-08-20X1. East India reported earnings of Rs.3,00,000 for the financial year ending on 31-03-20X2 (assume profits to accrue evenly) and declared dividends of Rs.60,000 on 12-06-20X2.

Calculate the carrying amount of investment in:

- (i) Separate financial statements of Bright Ltd. as on 31-03-20X2;
- (ii) Consolidated financial statements of Bright Ltd.; as on 31-03-20X2;
- (iii) What will be the carrying amount as on 30-06-20X2 in consolidated financial statements?

Answer:

- (i) Carrying amount of investment in Separate Financial Statement of Bright Ltd. as on 31.03.20X2

	Rs.
Amount paid for investment in Associate (on 1.06.20X1)	2,00,000
Less: Pre-acquisition dividend (Rs.50,000 x 30%)	<u>(15,000)</u>
Carrying amount as on 31.3.20X2 as per AS 13	<u>1,85,000</u>

- (ii) Carrying amount of investment in Consolidated Financial Statements of Bright Ltd. as on 31.3.20X2 as per AS 23

	Rs.
Carrying amount as per separate financial statements	1,85,000
Add: Proportionate share of 10-month profit of investee as per equity method (30% of Rs.3,00,000 x 10/12)	<u>75,000</u>
Carrying amount as on 31.3.20X2	<u>2,60,000</u>

- (iii) Carrying amount of investment in Consolidated Financial Statement of Bright Ltd. as on 30.6.20X2 as per AS 23

	Rs.
Carrying amount as on 31.3.20X2	2,60,000
Less: Dividend received (Rs.60,000 x 30%)	<u>(18,000)</u>
Carrying amount as on 30.6.20X2	<u>2,42,000</u>

9. A Ltd. acquired 25% of shares in B Ltd. as on 31.3.20X1 for Rs.3 lakhs. The Balance Sheet of B Ltd. as on 31.3.20X1 is given below:

	Rs.
Share Capital	5,00,000
Reserves and Surplus	<u>5,00,000</u>

	<u>10,00,000</u>
Property, Plant and Equipment	5,00,000
Investments	2,00,000
Current Assets	<u>3,00,000</u>
	<u>10,00,000</u>

During the year ended 31.3.20X2 the following are the additional information available:

(i) On 30.4.20X1 A Ltd. received a dividend from B Ltd. for the year ended 31.3.20X1 at 40% from the Reserves. The above balance sheet is before the adjustment of dividend.

(ii) B Ltd. made a profit after tax of Rs.7 lakhs for the year ended 31.3.20X2.

(iii) B Ltd. declared a dividend @ 50% for the year ended 31.3.20X2 on 30.4.20X2.

A Ltd. is preparing Consolidated Financial Statements for 20X1-X2 in accordance with AS 21 for its various subsidiaries. Calculate:

(i) Goodwill if any on investment in shares of B Ltd.'s .

(ii) How the dividend received for 31.3.20X2 on 30.4.20X2 from B Ltd. will be shown in the Consolidated Financial Statements?

(iii) How A Ltd. will reflect the value of investment in B Ltd., in its Consolidated Financial Statements?

Answer:

In terms of AS 23, B Ltd. will be considered as an associate company of A Ltd. as shares acquired represent to more than 20%.



(i) Calculation of Goodwill	(Rs.in lakhs)
Amount paid towards acquisition of stake in B Ltd.	3.00
Less: Pre-acquisition dividend (Rs.5,00,000 x 40% x 25%)	<u>0.50</u>
Cost of Investment in B Ltd.	2.50
Less: Share in the value of Equity of B Ltd. as at the date of investment [25% of Rs.8 lakhs (Rs.5 lakhs + Rs.5 lakhs – Rs.2 lakhs)]	<u>(2.00)</u>
Goodwill	<u>0.50</u>

(ii) A Ltd.

Consolidated Profit and Loss Account for the year ended 31st March, 20X2 (An extract)

		Rs.in lakhs
Other income:		
Share of profits in B Ltd. (7x 25%)		1.75
Pre-acquisition Dividend received from B Ltd.	0.50	
Transfer to investment A/c	<u>(0.50)</u>	Nil

(iii) A Ltd.

Consolidated Balance Sheet as on 31.3.20X2 (An extract)

		Rs.in lakhs
Non-current investments		
Investment in B Ltd. (including goodwill)	2.50	
Share of profit for year 20X1 – 20X2	<u>1.75</u>	4.25

Working Notes:

1. Pre-acquisition dividend received from B Ltd. amounting to Rs.0.50 lakhs will be reduced from investment value in the books of A Ltd.
2. B Ltd. made a profit of Rs.7 lakhs for the year ended 31st March, 20X2. A Ltd.'s share in the profits of Rs.7 lakhs is Rs.1.75 lakhs. Investment in B Ltd. will be increased by Rs.1.75 lakhs and consolidated profit and loss account of A Ltd. will be credited with Rs.1.75 lakhs in the consolidated financial statement of A Ltd.
3. Dividend declared on 30.4.20X2 will not be recognized in the consolidated financial statement of A Ltd.



AS - 27: FINANCIAL REPORTING OF INTERESTS IN JOINT VENTURES

ILLUSTRATIONS

Illustration 1

Mr. A, Mr. B and Mr. C entered into a joint venture to purchase a land, construct and sell flats. Mr. A purchased a land for Rs.60,00,000 on 01.01.20X1 and for the purpose he took loan from a bank for Rs.50,00,000 @ 8% interest p.a. He also paid registering fees Rs.60,000 on the same day. Mr. B supplied the materials for Rs.4,50,000 from his godown and further he purchased the materials for Rs.5,00,000 for the joint venture. Mr. C met all other expenses of advertising, labour and other incidental expenses which turnout to be Rs.9,00,000. On 30.06.20X1 each of the venturer agreed to take away one flat each to be valued at Rs.10,00,000 each flat and rest were sold by them as follow: Mr. A for Rs.40,00,000; Mr. B for Rs.20,00,000 and Mr. C for Rs.10,00,000. Loan was repaid on the same day by Mr. A along with the interest and net proceeds were shared by the partners equally.

You are required to prepare the draft Consolidated Profit & Loss Account and Joint Venture Account in the books of each venturer.

Solution:

Draft Consolidated Profit & Loss Account

Particulars	Rs.	Rs.	Particulars	Rs.	Rs.
To Purchase of Land:			By Sale of Flats:		
Mr. A		60,00,000	Mr. A	40,00,000	
To Registration Fees:			Mr. B	20,00,000	
Mr. A		60,000	Mr. C	<u>10,00,000</u>	70,00,000
To Materials:			By Flats taken by Venturers:		
Mr. B		9,50,000	Mr. A	10,00,000	
To Other Expenses:			Mr. B	10,00,000	
Mr. C		9,00,000	Mr. C	<u>10,00,000</u>	30,00,000
To Bank Interest:					
Mr. A		2,00,000			
To Profits:					
Mr. A	6,30,000				
Mr. B	6,30,000				
Mr. C	<u>6,30,000</u>	<u>18,90,000</u>			
		<u>1,00,00,000</u>			<u>1,00,00,000</u>

In the Books of Mr. A Joint Venture Account

Particulars	Rs.	Particulars	Rs.
To Bank Loan (Purchase of Land)	50,00,000	By Bank (Sale of Flats)	40,00,000
To Bank:(Purchase of Land)	10,00,000	By Land & Building	10,00,000
To Bank (Registration Fees)	60,000	By Bank (Received from Mr. B)	14,20,000
To Bank (Bank Interest)	2,00,000	By Bank (Received from Mr. C)	4,70,000
To Profit on JV	<u>6,30,000</u>		
	<u>68,90,000</u>		<u>68,90,000</u>

In the Books of Mr. B Joint Venture Account

Particulars	Rs.	Particulars	Rs.
To Purchases (Material Supplied)	4,50,000	By Bank (Sale of Flats)	20,00,000
To Bank (Materials)	5,00,000	By Land & Building	10,00,000
To Profit on JV	6,30,000		
To Bank (Paid to Mr. A)	<u>14,20,000</u>		
	<u>30,00,000</u>		<u>30,00,000</u>

In the Books of Mr. C Joint Venture Account

Particulars	Rs.	Particulars	Rs.
To Bank (Misc. Expenses)	9,00,000	By Bank (Sale of Flats)	10,00,000
To Profit on JV	6,30,000	By Land & Building	10,00,000
To Bank (Paid to Mr. A)	<u>4,70,000</u>		
	<u>20,00,000</u>		<u>20,00,000</u>

Illustration 2

A Ltd., B Ltd. and C Ltd. decided to jointly construct a pipeline to transport the gas from one place to another that was manufactured by them. For the purpose following expenditure was incurred by them: Buildings Rs.12,00,000 to be depreciated @ 5% p.a., Pipeline for Rs.60,00,000 to be depreciated @ 15% p.a., computers and other electronics for Rs.3,00,000 to be depreciated @ 40% p.a. and various vehicles of Rs.9,00,000 to be depreciated @ 20% p.a.

They also decided to equally bear the total expenditure incurred on the maintenance of the pipeline that comes to Rs.6,00,000 each year.

You are required to show the consolidated balance sheet and the extract of Statement of Profit & Loss and Balance Sheet for each venturer.

Solution:

Consolidated Balance Sheet

		Note	(Rs.)
I	Equity and liabilities		
	Shareholders' funds:		
	Share Capital	1	<u>71,40,000</u>
			<u>71,40,000</u>
II	Assets		
	Non-current Assets		
	Property, Plant and Equipment:	2	<u>71,40,000</u>
			<u>71,40,000</u>

Notes to Accounts

			(Rs.)
1.	Share capital		
	A Ltd.	23,80,000	
	B Ltd.	23,80,000	
	C Ltd.	23,80,000	71,40,000
2.	Property, Plant and Equipment		
	Land & Building:		
	A Ltd.	3,80,000	
	B Ltd.	3,80,000	
	C Ltd.	<u>3,80,000</u>	11,40,000
	Plant & Machinery:		
	A Ltd.	17,00,000	
	B Ltd.	17,00,000	
	C Ltd.	<u>17,00,000</u>	51,00,000
	Computers:		
	A Ltd.	60,000	
	B Ltd.	60,000	
	C Ltd.	<u>60,000</u>	1,80,000
	Vehicles:		
	A Ltd.	2,40,000	
	B Ltd.	2,40,000	
	C Ltd.	<u>2,40,000</u>	<u>7,20,000</u>

In the Books of A Ltd.
Extract of statement of Profit & Loss

Particulars	Note No.	Rs.
Depreciation and amortisation expense	1	4,20,000
Other operating Expenses (Pipeline Expenses)		200,000

Extract of Balance Sheet

	Note No.	Rs.
Assets		
Non-current assets		
Property, Plant and Equipment	2	23,80,000

Notes to Accounts

		Rs.	Rs.
1.	Depreciation and amortisation expense		
	Land & Building	20,000	
	Plant & Machinery	3,00,000	
	Computers	40,000	
	Vehicles	<u>60,000</u>	4,20,000
2.	Land & Building	4,00,000	
	Less: Depreciation	<u>(20,000)</u>	3,80,000
	Plant & Machinery	20,00,000	
	Less: Depreciation	<u>(3,00,000)</u>	17,00,000
	Computers	1,00,000	
	Less: Depreciation	<u>(40,000)</u>	60,000
	Vehicles	3,00,000	
	Less: Depreciation	<u>(60,000)</u>	<u>2,40,000</u>
			<u>23,80,000</u>

In the Books of B Ltd.

Extract of draft Profit & Loss Account

Particulars	Note No.	Rs.
Depreciation and amortisation expense	1	4,20,000
Other operating Expenses (Pipeline Expenses)		200,000

Extract of Balance Sheet

	Note No.	Rs.
Assets		
Non-current assets		
Property, Plant and Equipment	2	23,80,000

Notes to Accounts

		Rs.	Rs.
1.	Depreciation and amortisation expense		
	Land & Building	20,000	
	Plant & Machinery	3,00,000	
	Computers	40,000	
	Vehicles	<u>60,000</u>	4,20,000
2.	Land & Building	4,00,000	
	Less: Depreciation	<u>(20,000)</u>	3,80,000
	Plant & Machinery	20,00,000	
	Less: Depreciation	<u>(3,00,000)</u>	17,00,000
	Computers	1,00,000	
	Less: Depreciation	<u>(40,000)</u>	60,000
	Vehicles	3,00,000	
	Less: Depreciation	<u>(60,000)</u>	<u>2,40,000</u>
			<u>23,80,000</u>

In the Books of C Ltd.

Extract of Draft Profit & Loss Account	Note No.	Rs.
Depreciation and amortisation expense	1	4,20,000
Other operating Expenses (Pipeline Expenses)		200,000

Extract of Balance Sheet

	Note No.	Rs.
Assets		
Non-current assets		
Property, Plant and Equipment	2	23,80,000

Notes to Accounts

		Rs.	Rs.
1.	Depreciation and amortisation expense		
	Land & Building	20,000	
	Plant & Machinery	3,00,000	
	Computers	40,000	
	Vehicles	<u>60,000</u>	4,20,000
2.	Land & Building	4,00,000	
	Less: Depreciation	<u>(20,000)</u>	3,80,000
	Plant & Machinery	20,00,000	
	Less: Depreciation	<u>(3,00,000)</u>	17,00,000

Computers	1,00,000	
Less: Depreciation	<u>(40,000)</u>	60,000
Vehicles	3,00,000	
Less: Depreciation	<u>(60,000)</u>	<u>2,40,000</u>
		<u>23,80,000</u>

Illustration 3

A Ltd. a UK based company entered into a joint venture with B Ltd. in India, wherein B Ltd. will import the goods manufactured by A Ltd. on account of joint venture and sell them in India. A Ltd. and B Ltd. agreed to share the expenses & revenues in the ratio of 5:4 respectively whereas profits are distributed equally. A Ltd. invested 49% of total capital but has equal share in all the assets and is equally liable for all the liabilities of the joint venture. Following is the trial balance of the joint venture at the end of the first year:

Particulars	Dr. (Rs.)	Cr. (Rs.)
Purchases	9,00,000	
Other Expenses	3,06,000	
Sales		13,05,000
Property, Plant and Equipment	6,00,000	
Current Assets	2,00,000	
Unsecured Loans		2,00,000
Current Liabilities		1,00,000
Capital		4,01,000

Closing inventory was valued at Rs.1,00,000.

You are required to prepare the Consolidated Financial Statement.

Solution:

Consolidated Profit & Loss Account

Particulars	Note No.	(Rs.)
Revenue from operations	1	<u>13,05,000</u>
Total Revenue (A)		<u>13,05,000</u>
Less: Expenses		
Purchases	2	9,00,000
Other expenses	3	3,06,000
Changes in inventories of finished goods	4	<u>(1,00,000)</u>
Total Expenses (B)		<u>11,06,000</u>
Profit Before Tax (A-B)		<u>1,99,000</u>

Consolidated Balance Sheet

		Note No.	(Rs.)
I	Equity and liabilities		
	1. Shareholders' funds:		
	Share Capital	5	4,01,000
	Reserves and Surplus	6	1,99,000
	2. Non-current liabilities		
	Long term borrowings	7	2,00,000
	3. Current Liabilities	8	<u>1,00,000</u>
			<u>9,00,000</u>
II	Assets		
	Non-current Assets		
	Property, Plant and Equipment	9	6,00,000
	Current Assets		
	Inventories	10	1,00,000
	Other current assets	11	<u>2,00,000</u>
			<u>9,00,000</u>

Notes to Accounts

	Particulars		(Rs.)
1.	Revenue from operations		
	Sales:		
	A Ltd.	7,25,000	
	B Ltd.	<u>5,80,000</u>	13,05,000
2.	Purchases		
	A Ltd.	5,00,000	
	B Ltd.	<u>4,00,000</u>	9,00,000
3.	Other expenses		
	A Ltd.	1,70,000	
	B Ltd.	<u>1,36,000</u>	3,06,000
4.	Closing Inventory		
	A Ltd.	50,000	
	B Ltd.	<u>50,000</u>	1,00,000
5.	Share Capital		
	A Ltd.	1,96,490	
	B Ltd.	<u>2,04,510</u>	4,01,000
6.	Reserves and Surplus		

	Profit & Loss Account:		
	A Ltd.	99,500	
	B Ltd.	<u>99,500</u>	1,99,000
7.	Long Term Borrowings		
	Unsecured Loans:		
	A Ltd.	1,00,000	
	B Ltd.	<u>1,00,000</u>	2,00,000
8.	Current Liabilities		
	A Ltd.	50,000	
	B Ltd.	<u>50,000</u>	1,00,000
9.	Property, Plant and Equipment		
	A Ltd.	3,00,000	
	B Ltd.	<u>3,00,000</u>	6,00,000
10.	Inventories		
	A Ltd.	50,000	
	B Ltd.	<u>50,000</u>	1,00,000
11.	Other Current Assets		
	A Ltd.	1,00,000	
	B Ltd.	<u>1,00,000</u>	2,00,000

Illustration 4

A Ltd. entered into a joint venture with B Ltd. on 1:1 basis and a new company C Ltd. was formed for the same purpose and following is the balance sheet of all the three companies:

Particulars	A Ltd.	B Ltd.	C Ltd.
Share Capital	10,00,000	7,50,000	5,00,000
Reserve & Surplus	18,00,000	16,00,000	12,00,000
Loans	3,00,000	4,00,000	2,00,000
Current Liabilities	4,00,000	2,50,000	1,00,000
Property, Plant and Equipment	30,50,000	26,25,000	19,50,000
Investment in JV	2,50,000	2,50,000	-
Current Assets	2,00,000	1,25,000	50,000

Prepare the balance sheet of A Ltd. and B Ltd. under proportionate consolidation method.

Solution:

Balance Sheet of A Ltd.

		Note No.	(Rs.)
I	Equity and liabilities		

	1. Shareholders' funds:		
	Share Capital		10,00,000
	Reserves and Surplus	1	24,00,000
	2. Non-current liabilities	2	4,00,000
	3. Current Liabilities	3	<u>4,50,000</u>
	TOTAL		<u>42,50,000</u>
II	Assets		
	Non-current Assets		
	Property, Plant and Equipment:	4	40,25,000
	Current Assets	5	<u>2,25,000</u>
			<u>42,50,000</u>

Notes to Accounts

		Rs.	Rs.
1.	Reserves and Surplus		
	A Ltd.	18,00,000	
	C Ltd.	<u>6,00,000</u>	24,00,000
2.	Long Term Borrowings		
	Loans:		
	A Ltd.	3,00,000	
	C Ltd.	<u>1,00,000</u>	4,00,000
3.	Current Liabilities:		
	A Ltd.	4,00,000	
	C Ltd.	<u>50,000</u>	4,50,000
4.	Property, Plant and Equipment:		
	A Ltd.	30,50,000	
	C Ltd.	<u>9,75,000</u>	40,25,000
5.	Current Assets:		
	A Ltd.	2,00,000	
	C Ltd.	<u>25,000</u>	2,25,000

Balance Sheet of B Ltd.

		Note No.	(Rs.)
I	Equity and liabilities		
	1. Shareholders' funds:		
	Share Capital		7,50,000
	Reserves and Surplus	1	22,00,000
	2. Non-current liabilities	2	5,00,000

	3. Current Liabilities	3	<u>3,00,000</u> <u>37,50,000</u>
II	Assets		
	1. Non-current Assets		
	Property, Plant and Equipment	4	36,00,000
	2. Current Assets	5	<u>1,50,000</u> <u>37,50,000</u>

Notes to Accounts

		Rs.	Rs.
1.	Reserves and Surplus		
	A Ltd.	16,00,000	
	C Ltd.	<u>6,00,000</u>	22,00,000
2.	Long Term Borrowings		
	Loans:		
	A Ltd.	4,00,000	
	C Ltd.	<u>1,00,000</u>	5,00,000
3.	Current Liabilities:		
	A Ltd.	2,50,000	
	C Ltd.	<u>50,000</u>	3,00,000
4.	Property, Plant and Equipment:		
	A Ltd.	26,25,000	
	C Ltd.	<u>9,75,000</u>	36,00,000
5.	Current Assets:		
	A Ltd.	1,25,000	
	C Ltd.	25,000	1,50,000



TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. State which of the following statements are incorrect.
 - (i) The requirements relating to accounting for joint ventures in consolidated financial statements according to proportionate consolidation method, as contained in AS 27, applies only when consolidated financial statements are prepared by venturer.
 - (ii) The requirements relating to accounting for joint ventures in consolidated financial statements according to proportionate consolidation method, as contained in AS 27, applies irrespective whether consolidated financial statements are prepared by venturer or not.
 - (iii) An investor in joint venture, which does not have joint control, should report its interest in a joint venture in its consolidated financial statements in accordance with AS 13, AS 21 and AS 23 as the case may be.
 - (a) Point (i) is incorrect.
 - (b) Point (ii) is incorrect.
 - (c) Point (iii) is incorrect.
 - (d) None of the above.

2. Identify which of the following is not a feature of a Jointly controlled operations (JCO):
 - (a) Each venturer has his own separate business.
 - (b) There is a separate entity for joint venture business.
 - (c) Each venturer record only his own transactions without any separately set of books maintained for the joint venture business.
 - (d) There is a common agreement between all of them.

3. Identify which of the following is/are not a feature of a Jointly controlled assets (JCA):
 - (i) There is a separate legal identity.
 - (ii) There is a common control over the joint assets.
 - (iii) Expenses on jointly held assets are shared by the venturers as per the contract.
 - (iv) In their financial statement, venturer shows only their share of the asset and total income earned by them along with total expenses incurred by them.
 - (a) Point no. (i) only.
 - (b) Point no. (i) and (iii).
 - (c) Point no. (iii) and (iv).
 - (d) Point (i) and (ii).

4. Identify which is/ are features of a Jointly controlled entity (JCE):
 - (i) Venturer creates a new entity for their joint venture business.

(ii) All the venturers pool their resources under new banner and this entity purchases its own assets, create its own liabilities, expenses are incurred by the entity itself and sales are also made by this entity.

(iii) The revenues and expenses of the entity is shared by the venturers in the equal ratio only.

(a) Point no. (i) only.

(b) Point no. (i) and (ii).

(c) Point no. (ii).

(d) Point no. (iii).

5. Identify the correct statements.

From the date of discontinuing the use of the proportionate consolidation method:

(i) If interest in entity is more than 50%, investments in such joint ventures should be accounted for in accordance with AS 21, Consolidated Financial Statements.

(ii) If interest is 20% or more but upto 50%, investments are to be accounted for in accordance with AS 23, Accounting for Investment in Associates in Consolidated Financial Statements.

(iii) For all other cases investment in joint venture is treated as per AS 13, Accounting for Investments.

(iv) For this purpose, the fair value of the investment at the date on which joint venture relationship ceases to exist should be regarded as cost thereafter.

(a) Point no. 1 and 2.

(b) Point no. 1, 2 and 3.

(c) Point no. 1, 2, 3 and 4.

(d) None of the above.

Answer to the Multiple Choice Questions

1.	(b)	2.	(b)	3.	(a)	4.	(b)	5.	(b)

THEORETICAL QUESTIONS

6. Describe the cases when AS 27 does not allow the use of Proportionate consolidation method of accounting?

Answer:

Proportionate consolidation method of accounting is to be followed except in the following cases:

- a. Investment is intended to be temporary because the investment is acquired and held exclusively with a view to its subsequent disposal in the near future.

The term 'Near Future' is explained with AS 21.

Or

- b. joint venture operates under severe long-term restrictions, which significantly impair its ability to transfer funds to the venturers.

In both the above cases, investment of venturer in the share of the investee is treated as investment according to AS 13.

7. When is a venturer required to discontinue the use of the proportionate consolidation method?

Answer:

A venturer should discontinue the use of the proportionate consolidation method from the date that:

- a. It ceases to have joint control in the joint venture but retains, either in whole or in part, its investment.
- b. The use of the proportionate consolidation method is no longer appropriate because the joint venture operates under severe long-term restrictions that significantly impair its ability to transfer funds to the venturers.

From the date of discontinuing the use of the proportionate consolidation method,

- a. If interest in entity is more than 50%, investments in such joint ventures should be accounted for in accordance with AS 21, Consolidated Financial Statement.
- b. If interest is 20% or more but up to 50%, investments are to be accounted for in accordance with AS 23, Accounting for Investment in Associates in Consolidated Financial Statement.
- c. For all other cases investment in joint venture is treated as per AS 13, Accounting for Investment.
- d. For this purpose, the carrying amount of the investment at the date on which joint venture relationship ceases to exist should be regarded as cost thereafter.

SCENARIO BASED QUESTIONS

8. JVR Limited has made investments of Rs.97.84 crores in equity shares of QSR Limited in pursuance of Joint Venture agreement till 20X1-X2 (i.e., more than 12 months). The investment has been made at par. QSR Limited has been in continuous losses for the last 2 years. JVR Limited is willing to reassess the carrying amount of its investment in QSR Limited and wish to provide for diminution in value of investments. However, QSR Limited has a futuristic and profitable business plans and projection for the coming years. Discuss whether the contention of JVR Limited to bring down the carrying amount of investment in QSR Limited is in accordance with the Accounting Standard.

Answer:

As per para 26 of AS 27 “Financial Reporting of Interests in Joint Ventures”, in a venturer’s separate financial statements, interest in a jointly controlled entity should be accounted for as an investment in accordance with AS 13 ‘Accounting for Investments’.

As per para 17 of AS 13 “Accounting for Investments”, long-term investments are usually carried at cost. However, when there is a decline, other than temporary, in the value of a long-term investment, the carrying amount is reduced to recognize the decline. Indicators of the value of an investment are obtained by reference to its market value, the investee’s assets and results and the expected cash flows from the investment. The type and extent of the investor’s stake in the investee are also taken into account. However, where there is a decline, other than temporary, in the carrying amounts of long-term investments, the resultant reduction in the carrying amount is charged to the profit and loss statement.

Since the investment was made in the year 20X1-20X2 i.e., more than a year, it is a long-term investment. In the given case, though the QSR Ltd. is in continuous losses for past 2 years, yet it has a futuristic and profitable business plans and projections for the coming years. Here, one of the indicators i.e. ‘losses incurred to the company’ may lead to diminution in the value of the shares while the other indicator that ‘the company has positive expected cash flows from its business plans’ does not lead to decline in the value of shares.

Considering both the facts, in case the expectation of profitable business plans and positive cash flows is based reliable presumptions (such as tender in favour of QSR Ltd., strong order book etc.), the decline will be regarded as temporary in nature and the investment in equity shares will continue to be carried at cost only.

However, should the aforesaid presumptions be based on projections without reasonable evidence backing the claims, the decline could be regarded as non-temporary in nature in which case the write down of the carrying amount become necessary in line with AS 13, thereby implying the contention of QSR Ltd. to be correct.