

# INTERNAL RECONSTRUCTION

## Illustration 1

On 31-12-20X1, B Ltd. had 20,000, ₹ 10 Equity Shares as authorized capital and the shares were all issued on which ₹ 8 was paid up. In June, 20X2 the company in general meeting decided to sub-divide each share into two shares of ₹ 5 with ₹ 4 paid up. In June, 20X3 the company in general meeting resolved to consolidate 20 shares of ₹ 5, ₹ 4 per share paid up into one share of ₹ 100 each, ₹ 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		₹	₹
June	Equity Share Capital (₹ 10) A/c Dr. To Equity Share Capital (₹ 5) A/c (Being the sub-division of 20,000 shares of ₹ 10 each with ₹ 8 paid up into 40,000 shares ₹ 5 each with ₹ 4 paid up by resolution in general meeting dated....)	1,60,000	1,60,000
20X3	Equity Share Capital (₹ 5) A/c Dr.	1,60,000	
June	To Equity Share Capital (₹ 100) A/c (Being consolidation of 40,000 shares of ₹ 5 with ₹ 4 paid up into 2,000 ₹ 100 shares with ₹ 80 paid up)		1,60,000

### Notes to Balance Sheet

Liabilities:	₹
As on 31-12-20X1	
<b>1. Share Capital</b>	
Authorized:	
20,000 Equity Shares of ₹ 10 each	2,00,000
Issued, Subscribed and Paid up:	
20,000 Equity Shares of ₹ 10 each ₹ 8 per share paid up	1,60,000
As on 31-12-20X2	
<b>1. Share Capital</b>	
Authorized:	
40,000 Equity Shares of ₹ 5 each	2,00,000
Issued, Subscribed and Paid up:	
40,000 Equity Shares of ₹ 5 each ₹ 4 per share paid up	1,60,000
As on 31-12-20X3	
<b>1. Share Capital</b>	
Authorized:	
2,000 Equity Shares of ₹ 100 each	2,00,000
Issued, Subscribed and Paid up:	
2,000 Equity Shares of ₹ 100 each ₹ 80 per share paid up	1,60,000

The Balance Sheet of A & Co. Ltd. as at 31-3-20X2 is as follows:

	Particulars	Notes	₹
	<b>Equity and Liabilities</b>		
<b>1</b>	<b>Shareholders' funds</b>		
	A Share capital	1	11,50,000
	B Reserves and Surplus	2	(5,35,000)
<b>2</b>	<b>Non-current liabilities</b>		
	A Long-term borrowings	3	3,75,000
<b>3</b>	<b>Current liabilities</b>		
	A Trade Payables		3,00,000
	B Short term borrowings - Bank Overdraft		1,95,000
	C Other current liabilities	4	1,22,500
	Total		16,07,500
	<b>Assets</b>		
<b>1</b>	<b>Non-current assets</b>		
	A Property, plant and equipment	5	4,75,000
	B Intangible assets	6	1,67,500
	C Non-current investments	7	55,000
<b>2</b>	<b>Current assets</b>		
	A Inventories		4,25,000
	B Trade receivables		4,85,000
	Total		<u>16,07,500</u>

#### Notes to accounts

		₹
<b>1</b>	<b>Share Capital</b>	
	Equity share capital:	
	75,000 Equity Shares of ₹ 10 each	7,50,000
	Preference share capital:	
	4,000 6% Cumulative Preference Shares of ₹ 100 each	<u>4,00,000</u>
		<u>11,50,000</u>
<b>2</b>	<b>Reserves and Surplus</b>	
	Debit balance of Profit and loss Account	<u>(5,35,000)</u>
		<u>(5,35,000)</u>
<b>3</b>	<b>Long-term borrowings</b>	
	Secured	
	6% Debentures (secured on the freehold property)	<u>3,75,000</u>
		<u>3,75,000</u>
<b>4</b>	<b>Other current liabilities</b>	
	Loan from directors	1,00,000
	Interest payable on 6% debentures	<u>22,500</u>

		<u>1,22,500</u>
<b>5</b>	<b>Property plant and Equipment</b>	
	Freehold property	4,25,000
	Plant	<u>50,000</u>
		<u>4,75,000</u>
<b>6</b>	<b>Intangible assets</b> Goodwill	1,30,000
	Patents	<u>37,500</u>
<b>7</b>	<b>Non-current investments</b>	<u>1,67,500</u>
	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 ₹ 75 each and Equity Shares to ₹2 each.
- (ii) Of the Preference Share dividends which are in arrears for four years, three fourths to be waived and Equity Shares of ₹ 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 ₹ 1,00,000 at a valuation of ₹ 1,20,000 in part repayment of their holdings and to provide additional cash of ₹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 ₹ 65,000.
- (vii) Amount of ₹ 68,500 to be provided for bad debts.
- (viii) Remaining freehold property after giving to debenture holders, to be revalued at ₹ 3,87,500.
- (ix) Investments be sold for ₹ 1,40,000.
- (x) Directors to accept settlement of their loans as to 90% thereof by allotment of equity shares of ₹ 2 each and as to 5% in cash, and balance 5% being waived.
- (xi) There were capital commitments totalling ₹ 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. **(10 Marks)**

### Solution

#### Journal of A & Co. Ltd.

		<b>Dr.</b> ₹	<b>Cr.</b> ₹
20X2	Equity Share Capital A/c (₹ 10) Dr.	7,50,000	
April 1	To Capital Reduction A/c		6,00,000
	To Equity Share Capital A/c (₹ 2)		1,50,000
	(Reduction of equity shares of ₹ 10 each to shares of ₹ 2 each as per Reconstruction Scheme dated...)		
"	6% Cum. Preference Share Capital A/c Dr.	4,00,000	
	(₹ 100)		
	To Capital Reduction A/c		1,00,000
	To Pref. Share Capital A/c (₹ 75)		3,00,000

	(Reduction of preference shares of ₹ 100 each to shares of ₹ 75 each as per reconstruction scheme)														
"	Capital Reduction Account Dr. To Equity Share Capital Account (Arrears of preference dividends satisfied by the issue of equity shares, 25% of the amount due, ₹ 96,000)	24,000	24,000												
"	Freehold Property A/c Dr. 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>₹ 1,00,000</td><td>₹ 1,20,000</td></tr><tr><td></td><td><u>₹ 3,25,000</u></td><td><u>₹ 3,87,500</u></td></tr><tr><td>Total</td><td>₹ 4,25,000</td><td>₹ 5,07,500</td></tr></table> Profit on revaluation: ₹ 82,500)		Book value	Revalued Figure		₹ 1,00,000	₹ 1,20,000		<u>₹ 3,25,000</u>	<u>₹ 3,87,500</u>	Total	₹ 4,25,000	₹ 5,07,500	82,500	82,500
	Book value	Revalued Figure													
	₹ 1,00,000	₹ 1,20,000													
	<u>₹ 3,25,000</u>	<u>₹ 3,87,500</u>													
Total	₹ 4,25,000	₹ 5,07,500													
"	6% Debentures A/c Dr. 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)	1,20,000	1,20,000												
"	Interest payable A/c Dr. To Bank A/c (Debenture interest paid)	22,500	22,500												
"	Bank A/c Dr. To 8% Debentures A/c (8% Debentures issued for cash)	1,30,000	1,30,000												
"	Bank A/c Dr. To Investment A/c To Capital Reduction A/c (Sale of Investment for ₹ 1,40,000 cost being ₹ 55,000; profit credited to Capital Reduction Account)	1,40,000	55,000 85,000												
"	Directors' Loan A/c Dr. To Equity Share Capital A/c To Bank A/c To Capital Reduction A/c (Directors' loan discharged by issue of equity shares of ₹ 90,000, cash payments of ₹ 5,000 and surrender of ₹ 5,000, vide Scheme of Reconstruction)	1,00,000	90,000 5,000 5,000												
"	Capital Reduction A/c Dr. To Patents To Goodwill To Inventory To Provision for Doubtful Debts	8,48,500	37,500 1,30,000 65,000 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 ₹ 12,500 (2,50,000X5%) being paid in cash.

**Balance Sheet of A & Co. Ltd. (And Reduced) as at 1st April, 20X2**

		Particulars	Notes	₹
		<b>Equity and Liabilities</b>		
<b>1</b>		<b>Shareholders' funds</b>		
	A	Share capital	1	5,64,000
<b>2</b>		<b>Non-current liabilities</b>		
	A	Long-term borrowings	2	3,85,000
<b>3</b>		<b>Current liabilities</b>		
	A	Trade Payables		3,00,000
		Total		12,49,000
		<b>Assets</b>		
<b>1</b>		<b>Non-current assets</b>		
	A	Property, plant and equipment	3	4,37,500
	B	Intangible assets	4	-
<b>2</b>		<b>Current assets</b>		
	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**

<b>1</b>	<b>Share Capital</b>		
	<b>Equity share capital</b>		
	1,32,000 Equity shares of ₹ 2 each (of the above		2,64,000
	57,000 shares have been issued for consideration other than cash)		
	<b>Preference share capital</b>		
	4,000 6% Preference shares of ₹ 75 each		<u>3,00,000</u>
	Total		<u>5,64,000</u>
<b>2</b>	<b>Long-term borrowings</b>		
	Secured		
	6% Debentures		2,55,000
	8% Debentures		<u>1,30,000</u>
	Total		<u>3,85,000</u>

<b>3</b>	<b>Property, plant and equipment</b>		
	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>
<b>4</b>	<b>Intangible assets</b>		
	Goodwill	1,30,000	
	Less: Written off under scheme of Reconstruction	<u>(1,30,000)</u>	
	Net carrying value		NIL
	Patents	37,500	
	Less: Written off under scheme of Reconstruction	<u>(37,500)</u>	=
	Net carrying value	=	<u>NIL</u>
<b>5</b>	<b>Trade Receivables</b>	4,85,000	
	Less: Provision for doubtful debts	<u>68,500</u>	
			<u>4,16,500</u>

**Illustration 4 (RTP May'23, Past Exam Nov'19)**

Given below is the Balance sheet of Rebuilt Ltd. as at 31.3.20X1:

		Particulars	Notes	₹
		<b>Equity and Liabilities</b>		
<b>1</b>		<b>Shareholders' funds</b>		
	A	Share capital	1	13,50,000
	B	Reserves and Surplus	2	(4,51,000)
<b>2</b>		<b>Non-current liabilities</b>		
	A	Long-term borrowings (Loan)	3	5,73,000
<b>3</b>		<b>Current liabilities</b>		
	A	Trade Payables		2,07,000
	B	Other current liabilities		<u>35,000</u>
		Total		<u>17,14,000</u>
		<b>Assets</b>		
<b>1</b>		<b>Non-current assets</b>		
	A	Property, plant and equipment	4	6,68,000
	B	Intangible assets	5	3,18,000
<b>2</b>		<b>Current assets</b>		
	A	Inventories		4,00,000
	B	Trade receivables		<u>3,28,000</u>
		Total		<u>17,14,000</u>

**Notes to accounts**

		₹
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<b>Issued, subscribed and paid up</b>		
2,60,000 equity shares of ₹ 40 each (of the above 60,000 shares have been issued for consideration other than cash)		1,04,00,000
<b>Preference share capital</b>		
<b>Issued, subscribed and paid up</b>		
1,00,000 6% Cumulative Preference shares of ₹ 60 each		60,00,000
<b>Total</b>		<b>1,64,00,000</b>
<b>2. Reserves and Surplus</b>		
Capital Reserve		<u>26,00,000</u>
<b>3. Long-term borrowings Secured</b>		
6% Debentures		<u>56,00,000</u>
<b>4. Property, Plant and Equipment</b>		
Carrying value		2,50,00,000
Adjustment under scheme of reconstruction		(50,00,000) <u>2,00,00,000</u>
<b>5. Investments</b>		
Adjustment under scheme of reconstruction		20,00,000 <u>(1,00,000)</u> <u>19,00,000</u>
<b>6. Current assets</b>		
Adjustment under scheme of reconstruction		2,00,00,000 <u>(1,10,00,000)</u>
Taxation liability paid		90,00,000 <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	Share capital	40,00,000
To Current assets	1,10,00,000	By 5% Debentures	24,00,000
To Investment	1,00,000	By Sundry creditors	16,00,000
To Capital Reserve			
(Bal. fig.)	26,00,000		
	<u>2,00,00,000</u>		<u>2,00,00,000</u>

**Illustration 6 (MTP Mar'24)**

Following is the Balance Sheet of ABC Ltd. as at 31st March, 20X1:

		Particulars	Notes	₹
1		<b>Equity and Liabilities</b>		
		<b>Shareholders' funds</b>		
	A	Share capital	1	26,00,000

2	B	Reserves and Surplus	2	(4,05,000)
		<b>Non-current liabilities</b>		
3	A	Long-term borrowings	3	12,00,000
		<b>Current liabilities</b>		
	A	Trade Payables		5,92,000
	B	Short term borrowings - Bank overdraft		<u>1,50,000</u>
		Total		<u>41,37,000</u>
		<b>Assets</b>		
1		<b>Non-current assets</b>		
	A	Property, plant and equipment	4	11,50,000
	B	Intangible assets	5	70,000
	C	Non-current investment	6	68,000
2		<b>Current assets</b>		
	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:**

		₹
1	<b>Share Capital</b>	
	Equity share capital:	
	2,00,000 Equity Shares of ₹ 10 each	20,00,000
	6,000, 8% Preference shares of ₹ 100 each	<u>6,00,000</u>
		<u>26,00,000</u>
2	<b>Reserves and Surplus</b>	
	Debit balance of Profit and loss A/c	<u>(4,05,000)</u>
		<u>(4,05,000)</u>
3	<b>Long-term borrowings</b>	
	9% debentures	<u>12,00,000</u>
		<u>12,00,000</u>
4	<b>Property, Plant and Equipment</b>	
	Plant and machinery	9,00,000
	Furniture and fixtures	<u>2,50,000</u>
		<u>11,50,000</u>
5	<b>Intangible assets</b>	
	Patents and copyrights	<u>70,000</u>
		<u>70,000</u>
6	<b>Non-current investments</b>	
	Investments (market value of ₹55,000)	<u>68,000</u>
		<u>68,000</u>

The following scheme of reconstruction was finalized:



- (i) Preference shareholders would give up 30% of their capital in exchange for allotment of 11% Debentures to them.
- (ii) Debenture holders having charge on plant and machinery would accept plant and machinery in full settlement of their dues.
- (iii) Inventory equal to ₹ 5,00,000 in book value will be taken over by trade payables in full settlement of their dues.
- (iv) Investment value to be reduced to market price.
- (v) The company would issue 11% Debentures for ₹ 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. **(10 Marks)**

**Solution****In the Books of ABC Ltd.****Journal Entries**

Particulars		₹	₹
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**

	₹		₹
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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	1,54,000	By Trade payables A/c	92,000
	<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	₹
<b>I. Equity and Liabilities</b>		
<b>(1) Shareholder's Funds</b>		
(a) Share Capital	1	20,00,000
(b) Reserves and Surplus	2	1,54,000
<b>(2) Non-Current Liabilities</b>		
(a) Long-term borrowings	3	7,20,000
Total		28,74,000
<b>II. Assets</b>		
<b>(1) Non-current assets</b>		
(a) Property, plant and equipment	4	2,50,000
(b) Intangible assets	5	70,000
(c) Non-current investments	6	55,000
<b>(2) Current assets</b>		9,00,000
a) Inventories (₹ 14,00,000 – ₹ 5,00,000)		
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**

		₹
<b>1.</b>	<b>Share Capital</b>	
	2,00,000 Equity shares of ₹ 10 each fully paid-up	20,00,000
<b>2.</b>	<b>Reserve and Surplus</b>	
	Capital Reserve	1,54,000
<b>3.</b>	<b>Long Term Borrowings</b>	
	11% Debentures (₹ 4,20,000 + ₹ 3,00,000)	7,20,000
<b>4.</b>	<b>Property, Plant and Equipment</b>	
	Plant & machinery	9,00,000
	Less: Adjustment on scheme of reconstruction	<u>9,00,000</u>
	Furniture & fixtures	2,50,000
<b>5.</b>	<b>Intangible assets</b>	
	Patents & copyrights	<u>70,000</u>

6.	<b>Non-Current Investments</b>	3,20,000
	Investments (₹ 68,000 – ₹ 13,000)	
		55,000

**Working Note:**

Cash at bank = Opening balance + 11% Debentures issued – Bank overdraft paid  
 = ₹ 10,000 + ₹ 3,00,000 – ₹ 1,50,000 = ₹ 1,60,000

**Illustration 7 (MTP Oct'20, Mar'22)**

The Balance Sheet of Revise Limited as at 31st March, 20X1 was as follows :

		Particulars	Notes	₹
		<b>Equity and Liabilities</b>		
1		<b>Shareholders' funds</b>		
	A	Share capital	1	10,00,000
	B	Reserves and surplus	2	(6,00,000)
2		<b>Non-current liabilities</b>		
	A	Long-term borrowings	3	2,00,000
3		<b>Current liabilities</b>		
	A	Trade Payables		72,000
	B	Other current liabilities	4	24,000
	C	Short term provisions	5	24,000
		Total		<u>7,20,000</u>
		<b>Assets</b>		
1		<b>Non-current assets</b>		
	A	Property, Plant and Equipment	6	1,00,000
2		<b>Current assets</b>		
	A	Inventory		3,20,000
	B	Trade receivables		2,70,000
	C	Cash and cash equivalents		30,000
		Total		<u>7,20,000</u>

**Notes to accounts**

		₹
1	<b>Share Capital</b>	
	<b>Equity share capital</b>	
	10,000 Equity Shares of ₹ 100 each	10,00,000
		10,00,000
2	<b>Reserves and Surplus</b>	
	Debit balance of Profit and loss Account	(6,00,000)
		(6,00,000)
3	<b>Long-term borrowings</b>	

	12% debentures		2,00,000
			2,00,000
<b>4</b>	<b>Other current liabilities</b>		
	Interest payable on debentures		24,000
			24,000
<b>5</b>	<b>Short term provisions</b>		
	Provision for taxation		24,000
			24,000
<b>6</b>	<b>Property, Plant and Equipment</b>		
	Machinery		1,00,000
			<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:

- Each share is sub-divided into ten fully paid up equity shares of ₹10 each.
- 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.
- Out of shares surrendered, 10,000 shares of ₹10 each shall be converted into 12% preference shares of ₹10 each, fully paid up.
- 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 ₹1,00,000 which are converted out of shares surrendered.
- Trade payables claim shall be reduced to 50 per cent, it is to be settled by the issue of equity shares of ₹10 each out of shares surrendered.
- Balance of profit and loss account to be written off.
- 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

(8 Marks)

	Dr. ₹	Cr. ₹
Equity Share Capital (r 100) A/c Dr. To Share Surrender A/c To Equity Share Capital (₹ 10) A/c (Subdivision of 10,000 equity shares of ₹r 100 each into 1,00,000 equity shares of ₹10 each and surrender of 50,000 of such subdivided shares as per capital reduction scheme)	10,00,000	5,00,000 5,00,000
12% Debentures A/c Dr. Interest payable A/c Dr. To Reconstruction A/c (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)	1,50,000 18,000	1,68,000
Trade payables A/c Dr. To Reconstruction A/c	72,000	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.	₹
<b>I. Equity and Liabilities</b>		
<b>(1) Shareholder's Funds</b>		
(a) Share Capital	1	6,36,000
(b) Reserves and Surplus	2	4,000
<b>(2) Non-Current Liabilities</b>		
(a) Long-term borrowings	3	50,000
<b>(3) Current Liabilities</b>	4	6,000
(a) Other current liabilities		
(b) Short-term provisions	5	<u>24,000</u>
Total		<u>7,20,000</u>
<b>II. Assets</b>		
<b>(1) Non-current assets</b>		
(a) Property, plant and equipment	6	1,00,000
<b>(2) Current assets</b>		
a) Inventories		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**

		₹
1.	<b>Share Capital</b>	
	Equity Share Capital	

	Issued Capital: 53,600 Equity Shares of ₹ 10 each	5,36,000
	Preference Share Capital	
	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.	<b>Reserve and Surplus</b>	
	Capital Reserve	<u>4,000</u>
3.	<b>Long-term borrowings</b>	
	Unsecured Loans	
	12% Debentures	<u>50,000</u>
4.	<b>Other current liabilities</b>	
	Interest payable on debentures	<u>6,000</u>
5.	<b>Short-term provisions</b>	
	Provision for Income-tax	<u>24,000</u>
6.	<b>Property, plant and Equipment</b>	
	Machinery	<u>1,00,000</u>

**Illustration 8 (RTP May'21)**

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	₹
		<b>Equity and Liabilities</b>		
1		<b>Shareholders' funds</b>		
	A	<b>Share capital</b>	1	3,50,000
	B	<b>Reserves and surplus</b>	2	(70,000)
2		<b>Non-current liabilities</b>		
	A	<b>Long-term borrowings</b>	3	50,000
3		<b>Current liabilities</b>		
	A	<b>Trade Payables</b>		80,000
		<b>Short term Borrowings – Bank</b>		
	B	<b>overdraft</b>		90,000
		<b>Other Current Liabilities (Interest</b>		
	C	<b>payable on Debentures)</b>		<u>5,000</u>
				<u>5,05,000</u>
		<b>Assets</b>		
1		<b>Non-current assets</b>		
	A	Property, Plant Equipment	4	3,35,000
	B	Intangible assets	5	50,000

**MTP / RTP / Past Exam****Question 1 (MTP Oct'19, RTP May'18, Nov'19)**

M/s Xylem Limited has decided to reconstruct the Balance Sheet since it has accumulated huge losses.

The following is the summarized Balance Sheet of the company as on 31st March, 2019 before reconstruction:

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
Share Capital		Land & Building	42,70,000
50,000 shares of Rs. 50		Machinery	8,50,000
each fully paid up	25,00,000	Computers	5,20,000
1,00,000 shares of Rs. 50		Inventories	3,20,000
each Rs. 40 paid up	40,00,000	Trade receivables	10,90,000
Capital Reserve	5,00,000	Cash at Bank	2,68,000
8% Debentures of Rs. 100 each	4,00,000	Profit & Loss Account	29,82,000
12% Debentures of Rs. 100 each	6,00,000		
Trade payables	12,40,000		
Outstanding Expenses	10,60,000		
	<b>1,03,00,000</b>		<b>1,03,00,000</b>

Following is the interest of Mr. A and Mr. B in M/s Xylem Limited:

	Mr. A	Mr. B
8% Debentures	3,00,000	1,00,000
12% Debentures	4,00,000	2,00,000
<b>Total</b>	<b>7,00,000</b>	<b>3,00,000</b>

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

- 1) Uncalled capital is to be called up in full and then all the shares to be converted into Equity Shares of Rs. 40 each.
- 2) The existing shareholders agree to subscribe in cash, fully paid up equity shares of 40 each for Rs. 12,50,000.
- 3) Trade payables are given option of either to accept fully paid equity shares of Rs. 40 each for the amount due to them or to accept 70% of the amount due to them in cash in full settlement of their claim. Trade payables for Rs. 7,50,000 accept equity shares and rest of them opted for cash towards full and final settlement of their claim.
- 4) Mr. A agrees to cancel debentures amounting to Rs. 2,00,000 out of total debentures due to him and agree to accept 15% Debentures for the balance amount due. He also agree to subscribe further 15% Debentures in cash amounting to Rs. 1,00,000.
- 5) Mr. B agrees to cancel debentures amounting to Rs. 50,000 out of total debentures due to him and agree to accept 15% Debentures for the balance amount due.
- 6) Land & Building to be revalued at Rs. 51,84,000, Machinery at Rs. 7,20,000, Computers at Rs. 4,00,000, Inventories at Rs. 3,50,000 and Trade receivables at 10% less to as they are appearing in Balance Sheet as above.
- 7) Outstanding Expenses are fully paid in cash.
- 8) Profit & Loss A/c will be written off and balance, if any, of Capital Reduction A/c will be adjusted against Capital Reserve.

You are required to pass necessary Journal Entries for all the above transactions and draft the company's Balance Sheet immediately after the reconstruction.

(b) A Liquidator is entitled to receive remuneration at 2% on the assets realized, 3% on the amount distributed to Preferential Creditors and 3% on the payment made to Unsecured Creditors. The assets were realized for Rs. 25,00,000 against which payment was made as follows:

Liquidation expenses	Rs. 25,000
Secured Creditors	Rs. 10,00,000
Preferential Creditors	Rs. 75,000

The amount due to Unsecured Creditors was Rs. 15,00,000. You are asked to calculate the total Remuneration payable to Liquidator. Calculation shall be made to the nearest multiple of a rupee.

**Solution:**

**(15 Marks)**

**Journal Entries**

		Rs.	Rs.
Bank A/c	Dr	10,00,000	
To Equity share capital A/c			10,00,000
(Being money on final call received)			
Equity share capital (Rs. 50) A/c	Dr	75,00,000	
To Equity share capital (Rs. 40) A/c			60,00,000
To Capital Reduction A/c			15,00,000
(Being conversion of equity share capital of Rs. 50 each into Rs. 40 each as per reconstruction scheme)			
Bank A/c	Dr.	12,50,000	
To Equity Share Capital A/c			12,50,000
(Being new shares allotted at Rs. 40 each)			
Trade payables A/c	Dr.	12,40,000	
To Equity share capital A/c			7,50,000
To Bank A/c (4,90,000 x 70%)			3,43,000
To Capital Reduction A/c			1,47,000
(Being payment made to trade payables in shares or cash to the extent of 70% as per reconstruction scheme)			
8% Debentures A/c	Dr.	3,00,000	
12% Debentures A/c	Dr.	4,00,000	
To A A/c			7,00,000
(Being cancellation of 8% and 12% debentures of A)			
A A/c	Dr.	8,00,000	
To 15% Debentures A/c			6,00,000
To Capital Reduction A/c			2,00,000
(Being issuance of new 15% debentures and balance Transferred to capital reduction account as per reconstruction scheme)			
Bank A/c	Dr.	1,00,000	
To A A/c			1,00,000
(Being new debentures subscribed by A)			
8% Debentures A/c	Dr.	1,00,000	
12% Debentures A/c	Dr.	2,00,000	
To B A/c			3,00,000
(Being cancellation of 8% and 12% debentures of B)			
B A/c	Dr.	3,00,000	
To 15% Debentures A/c			2,50,000
To Capital Reduction A/c			50,000
(Being issuance of new 15% debentures and Transferred to capital			



reduction account as per reconstruction scheme)			
Land and Building	Dr		
.(51,84,000 – 42,70,000)		9,14,000	
Inventories	Dr.	30,000	
To Capital Reduction A/c			9,44,000
(Being value of assets appreciated)			
Outstanding expenses A/c	Dr.	10,60,000	
To Bank A/c			10,60,000
(Being outstanding expenses paid in cash)			
Capital Reduction A/c	Dr.	33,41,000	
To Machinery A/c			1,30,000
To Computers A/c			1,20,000
To Trade receivables A/c			1,09,000
To Profit and Loss A/c			29,82,000
(Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) balance and downfall in value of other assets)			
Capital Reserve A/c	Dr.	5,00,000	
To Capital Reduction A/c			5,00,000
(Being debit balance of capital reduction account adjusted Against capital reserve)			

**Balance Sheet of Xylem Ltd. (as reduced) as on 31.3.2019**

	Particulars	Notes	Rs.
	<b>Equity and Liabilities</b>		
<b>1</b>	<b>Shareholders' funds</b>		
a	Share capital	1	80,00,000
<b>2</b>	<b>Non-current liabilities</b>		
a	Long-term borrowings	2	8,50,000
	<b>Total</b>		<b>88,50,000</b>
	<b>Assets</b>	3	
<b>1</b>	<b>Non-current assets</b>		
a	<b>Property, Plant and Equipment</b>		
	Tangible assets		63,04,000
<b>2</b>	<b>Current assets</b>		
a	Inventories		3,50,000
b	Trade receivables		9,81,000
c	Cash and cash equivalents		12,15,000
	<b>Total</b>		<b>88,50,000</b>

**Notes to accounts**

			Rs.
<b>1.</b>	<b>Share Capital</b>		
	2,00,000 Equity shares of Rs. 40		80,00,000
<b>2.</b>	<b>Long-term borrowings</b>		
	Secured		
	15% Debentures (assumed to be secured)		8,50,000
<b>3.</b>	<b>Tangible assets</b>		
	Land & Building	51,84,000	
	Machinery	7,20,000	
	Computers	4,00,000	63,04,000

**Working Notes:****1. Cash at Bank Account**

Particulars	Rs.	Particulars	Rs.
To Balance b/d	2,68,000	By Trade payables A/c	3,43,000
To Equity Share capital A/c	10,00,000	By Outstanding expenses, A/c	10,60,000
To Equity Share Capital A/c	12,50,000	By Balance c/d (bal. fig.)	12,15,000
To A A/c	1,00,000		
	26,18,000		26,18,000

**2. Capital Reduction Account**

Particulars	Rs.	Particulars	Rs.
To Machinery A/c	1,30,000	By Equity Share Capital A/c	15,00,000
To Computers A/c	1,20,000	By Trade payables A/c	1,47,000
To Trade receivables A/c	1,09,000	By A A/c	2,00,000
To Profit and Loss A/c	29,82,000	By B A/c	50,000
		By Land & Building	9,14,000
		By Inventories	30,000
		By Capital Reserve A/c 5,00,000	
	33,41,000		33,41,000

**(b) Calculation of Total Remuneration payable to Liquidator**

		Amount in Rs.
2% on Assets realised	25,00,000 x 2%	50,000
3% on payment made to Preferential creditors	75,000 x 3%	2,250
3% on payment made to Unsecured creditors (Refer W.N)		39,255
Total Remuneration payable to Liquidator		91,505

**Working Note:**

Liquidator's remuneration on payment to unsecured creditors = Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors, preferential creditors & liquidator's remuneration

= Rs. 25,00,000 – Rs. 25,000 – Rs. 10,00,000 – Rs. 75,000 – Rs. 50,000 – Rs. 2,250 = Rs. 13,47,750.

Liquidator's remuneration on payment to unsecured creditors =  $\frac{3}{103} \times \text{Rs. } 13,47,750 = \text{Rs. } 39,255$ .

**Question 2 (MTP Mar'19)**

The shareholders of Lili Ltd. decided on a corporate restructuring exercise necessitated because of economic recession. From the given summarised balance sheet as on 31-3-2017 and the information supplied, you are required to prepare (i) Journal entries reflecting the scheme of reconstruction, (ii) Capital reduction account, (iii) Cash account in the books of Lili Ltd.

**Summarized Balance Sheet of Lili Ltd. as on 31.3.2017**

Liabilities	Rs.	Assets	Rs.
Share Capital		Property, Plant & Equipment	
30,000 Equity shares of Rs. 10 each	3,00,000	Trademarks and Patents	1,10,000
40,000 8% Cumulative Preference		Goodwill at cost	36,100
shares Rs. 10 each	4,00,000	Freehold Land	1,20,000
Reserves and Surplus		Freehold Premises	2,44,000
Securities Premium Account	10,000	Plant and Equipment Investment	3,20,000
Profit and Loss Account	(1,38,400)	Investment (marked to market)	64,000

Secured Borrowings		Current Assets	
9% Debentures (Rs. 100)	1,20,000	Inventories:	
Accrued Interest 5,400	1,25,400	Raw materials and packing materials 60,000	
Current liabilities Trade payables	1,20,000	Finished goods 16,000	76,000
Tax payable	50,000		
Temporary bank overdraft	2,23,100	Trade receivables	1,20,000
	<b>10,90,100</b>		<b>10,90,100</b>

Note: Preference dividends are in arrears for 4 years.

The scheme of reconstruction that received the permission of the Court was on the following lines:

- 1) The authorized capital of the Company to be re-fixed at Rs. 10 lakhs (preference capital of Rs. 3 lakhs and equity capital of Rs. 7 lakhs). Both classes of shares are of Rs. 10 each.
- 2) The preference shares are to be reduced to Rs. 5 each and equity shares reduced by Rs. 3 per share. Post reduction, both classes of shares to be re-consolidated into Rs. 10 shares.
- 3) Trade Investments are to be liquidated in open market.
- 4) One fresh equity shares of Rs.10 to be issued for every Rs.40 of preference dividends in arrears (ignore taxation).
- 5) Expenses for the scheme were Rs. 10,000.
- 6) The debenture holders took over freehold land at Rs. 2,10,000 and settled the balance after adjusting their dues.
- 7) Unprovided contingent liabilities were settled at Rs. 54,000 and a pending insurance claim receivable settled at Rs. 12,500.
- 8) The intangible assets were all to be written off along with Rs. 10,000 worth obsolete packing material and 10% of the receivables.
- 9) Remaining cash available as a result of the above transactions is to be utilized to pay off the bank overdraft to that extent.
- 10) The Equity shareholders agree that they will bring in necessary cash to liquidate the balance outstanding on the overdraft account by subscribing the fresh shares. The equity shares will be issued at par for this purpose.

#### Solution:

##### (i) In the books of Lili Ltd. Journal Entries

			Dr.	Cr.
	2017		Rs.	Rs.
1.	March 31	Equity Share Capital A/c (Rs.10) Dr.	3,00,000	
		To Capital Reduction A/c		90,000
		To Equity Share Capital A/c (Rs.7)		2,10,000
		(Being reduction of equity shares of Rs.10 each to shares of Rs. 7 each as per Reconstruction Scheme dated...)		
2		8% Cum. Preference Share Capital A/c (Rs. 10) Dr.	4,00,000	
		To Capital Reduction A/c		2,00,000
		To Preference Share Capital A/c (Rs. 5)		2,00,000
		(Being reduction of preference shares of Rs.10 each to shares of Rs.5 each as per reconstruction scheme)		
3.		Equity Share Capital A/c (30,000 x Rs.7) Dr.	2,10,000	
		Preference Share Capital A/c (40,000 x Rs.5) Dr.	2,00,000	
		To Equity Share Capital A/c (21,000 x Rs. 10)		

				2,10,000
		To Preference Share Capital A/c (20,000 x Rs.10)		2,00,000
		(Being post reduction, both classes of shares re consolidated into Rs.10 each) s		
4.		Cash Account Dr.	64,000	
		To Trade Investments		64,000
		(Being trade investments liquidated in the open market)		
5.		Capital Reduction Account Dr.	32,000	
		To Equity Share Capital Account		32,000
		(Being arrears of preference dividends of 4 years satisfied by the issue of 3,200 equity shares of Rs.10 each)		
6.		Capital Reduction Account Dr.	10,000	
		To Cash Account		10,000
		(Being expenses of reconstruction scheme paid in cash)		
7.		9% Debentures Account Dr.	1,20,000	
		Accrued Interest Account Dr.	5,400	
		To Debenture holders Account		1,25,400
		(Being amount due to debenture holders)		
8.		Debenture holders Account Dr.	1,25,400	
		Cash Account (2,10,000 – 1,25,400) Dr.	84,600	
		To Freehold Land		1,20,000
		To Capital Reduction Account (2,10,000 – 1,20,000)		90,000
		(Being Debenture holders took over freehold land at Rs.2,10,000 and settled the balance)		
9.		Capital Reduction Account Dr.	54,000	
		To Cash Account		54,000
		(Being contingent liability of Rs.54,000 paid)		
10		Cash Account Dr.	12,500	
		To Capital Reduction Account		12,500
		(Being pending insurance claim received)		
11		Capital Reduction Account Dr.	1,68,100	
		To Trademarks and Patents		1,10,000
		To Goodwill		36,100
		To Raw materials & Packing materials		10,000
		To Trade receivables		12,000
		(Being intangible assets written off along with raw materials and packing materials worth Rs.10,000 and 10% of trade receivables)		
12		Cash Account Dr.	1,26,000	
		To Equity Share Capital Account		1,26,000
		(Being 12,600 shares issued to existing shareholders)		
13		Bank Overdraft Account Dr.	2,23,100	
		To Cash Account		2,23,100
		(Being cash balance utilized to pay off bank overdraft)		
14		Capital Reduction Account Dr.	1,28,400	
		To Capital reserve Account		1,28,400
		(Being balance of capital reduction account transferred to capital reserve account)		

**(ii) Capital Reduction Account**

Particulars	Rs.	Particulars	Rs.
-------------	-----	-------------	-----

To Equity share capital	32,000	By Preference share capital	2,00,000
To Cash (contingent liability settled)	54,000	By Equity share capital	90,000
To Trademarks and Patents	1,10,000	By Freehold land	90,000
To Goodwill	36,100	By Cash (insurance claim)	12,500
To Raw material and Packing materials	10,000		
To Trade receivables	12,000		
To Cash account	10,000		
To Capital reserve account	1,28,400		
	<b>3,92,500</b>		<b>3,92,500</b>

**(iii) Cash Account**

Particulars	Rs.	Particulars	Rs.
To Investment	64,000	By Capital reduction	
To 9% Debenture holders		(Contingent liability)	54,000
(2,10,000-1,25,400)	84,600	By Expenses	10,000
To Capital reduction	12,500	By Temporary bank overdraft	
(insurance claim)		- From available cash	
		(64,000+84,600+12,500	
		-54,000-10,000)	97,100
To Equity share capital 12,600		- From proceeds of equity share capital	
shares @ Rs. 10 each	1,26,000		
		(2,23,100-97,100) 1,26,000	2,23,100
	<b>2,87,100</b>		<b>2,87,100</b>

**Note:** Shares issued to existing equity shareholders for bringing cash for payment of balance of bank overdraft = Rs. 2,23,100 – Rs. 97,100 = Rs. 1,26,000

**Question 3 (MTP Mar'18, Apr'21, RTP May'19)**

The Balance Sheet of Lion Limited as on 31-03-2018 is given below:

Particulars	Note No.	Amount (₹ in lakh)
<b>Equity &amp; Liabilities</b>		
<b>Shareholders' Funds</b>		
Shares' Capital	1	1,400
Reserves & Surplus	2	(522)
<b>Non-Current Liabilities</b>		
Long term Borrowings	3	700
<b>Current Liabilities</b>		
Trade Payables	4	102
Other Liabilities	5	24
<b>Total</b>		<b>1704</b>
<b>Assets</b>		
<b>Non-Current Assets</b>		
PPE		
Tangible Assets	6	750
<b>Current Assets</b>		
Current Investments	7	200
Inventories	8	300
Trade Receivables	9	450

To Profit and loss A/c		522
To Trade receivables A/c (450 x 40%)		180
To Inventories-in-trade A/c (300x 80%)		240
To Bank A/c (600 x 5%)		30
(Being certain value of various assets, penalty on cancellation of contract, profit and loss account debit balance written off through Capital Reduction Account)		

(x)

Capital Reduction A/c	286	
To Capital reserve A/c		286
(Being balance transferred to capital reserve account as per the scheme)		

## Capital Reduction Account

	Dr. (Rs. in lakhs)		Cr. (Rs. in lakhs)
To Equity Share Capital	32	By Preference Share Capital	80
To Trade receivables	180	By Equity Share Capital	800
To Finished Goods	240	By Freehold Property	150
To Profit & Loss A/c	522	By Bank	50
To Bank A/c	30	By Director's Loan	210
To Capital Reserve	286		
	<b>1,290</b>		<b>1,290</b>

## Notes to Balance Sheet

		(Rs. in lakhs)	(Rs. in lakhs)
1.	Share Capital		
	Authorized:		
	200 lakhs Equity shares of Rs. 2 each		400
	8 lakhs 8% Preference shares of Rs. 80 each		640
			1,040
	Issued:		
	161 lakhs equity shares of Rs. 2 each		322
	4 lakhs Preference Shares of Rs. 80 each		320
			642
2.	Tangible Assets		
	Freehold Property	550	
	Less: Utilized to pay Debenture holders	(300)	
		250	
	Add: Appreciation	150	400
	Plant and Machinery		200
			600

## Question 4 (RTP May'20)

The following is the Balance Sheet of Star Ltd. as on 31st March, 2019: Rs.

			Rs.
A.		Equity & Liabilities	

	<b>1.</b>		<b>Shareholders' Fund:</b>	
		<b>(a)</b>	<b>Share Capital:</b>	
			9,000 7% Preference Shares of Rs. 100 each fully paid	9,00,000
			10,000 Equity Shares of Rs. 100 each fully paid	10,00,000
		<b>(b)</b>	<b>Reserve &amp; Surplus:</b>	
			Profit & Loss Account	(2,00,000)
	<b>2.</b>		<b>Non-current liabilities:</b>	
			"A" 6% Debentures (Secured on Bombay Works)	3,00,000
			"B" 6% Debentures (Secured on Chennai Works)	3,50,000
	<b>3.</b>		<b>Current Liabilities and Provisions:</b>	
		<b>(a)</b>	<b>Workmen's Compensation Fund:</b>	
			Bombay Works	10,000
			Chennai Works	5,000
		<b>(b)</b>	<b>Trade Payables</b>	1,25,000
			<b>Total</b>	24,90,000
<b>B.</b>			<b>Assets:</b>	
			<b>Non- current Assets:</b>	
	<b>1.</b>		<b>PPE:</b>	
			Bombay Works	9,50,000
			Chennai Works	7,75,000
	<b>2.</b>		<b>Investment:</b>	
			Investments for Workman's Compensation Fund	15,000
	<b>3.</b>		<b>Current Assets:</b>	
		<b>(a)</b>	<b>Inventories</b>	4,50,000
		<b>(b)</b>	<b>Trade Receivables</b>	2,50,000
		<b>(c)</b>	<b>Cash at Bank</b>	50,000
				24,90,000

A reconstruction scheme was prepared and duly approved. The salient features of the scheme were as follows:

- (i) Paid up value of 7% Preference Share to be reduced to Rs. 80, but the rate of dividend being raised to 9%.
- (ii) Paid up value of Equity Shares to be reduced to Rs. 10.
- (iii) The directors to refund Rs. 50,000 of the fees previously received by them.
- (iv) Debenture holders forego their interest of Rs. 26,000 which is included among the trade payables.
- (v) The preference shareholders agreed to waive their claims for preference share dividend, which is in arrears for the last three years.
- (vi) "B" 6% Debenture holders agreed to take over the Chennai Works at Rs. 4,25,000 and to accept an allotment of 1,500 equity shares of Rs. 10 each at par, and upon their forming a company called Zia Ltd. (to take over the Chennai Works) they allotted 9,000 equity shares of Rs. 10 each fully paid at par to Star Ltd.
- (vii) The Chennai Workmen's compensation fund disclosed that there were actual liabilities of Rs. 1,000 only. As a consequence, the investments of the fund were realized to the extent of the balance. Entire investments were sold at a profit of 10% on book value and the proceeds were utilized for part payment of the creditors.
- (viii) Inventory was to be written off by Rs. 1,90,000 and a provision for doubtful debts is to be made to the extent of Rs. 20,000.
- (ix) Chennai works completely written off.

- (x) Any balance of the Capital Reduction Account is to be applied as two-third to write off the value of Bombay Works and one-third to Capital Reserve.

Pass necessary Journal Entries in the books of Star Ltd. after the scheme has been carried into effect.

**Solution:**

**In the books of Star Ltd. Journal Entries**

	Particulars	Amount	Amount
		Rs.	Rs.
(i)	7% Preference share capital (Rs. 100) Dr.	9,00,000	
	To 9% Preference share capital (Rs. 80)		7,20,000
	To Capital reduction A/c		1,80,000
	(Being preference shares reduced to Rs.80 and also rate of dividend raised from 7% to 9%)		
(ii)	Equity share capital A/c (Rs. 100 each) Dr.	10,00,000	
	To Equity share capital A/c (Rs. 10 each)		1,00,000
	To Capital reduction A/c		9,00,000
	(Being reduction of nominal value of one share of Rs. 100 each to Rs. 10 each)		
(iii)	Bank A/c Dr.	50,000	
	To Capital reduction A/c		50,000
	(Being directors refunded the fee amount)		
(iv)	Trade payables A/c (Interest on debentures) Dr.	26,000	
	To Capital reduction A/c		26,000
	(Being interest forgone by the debenture holders)		
(v)	No entry required		
(vi)	a 'B' 6% Debentures A/c Dr.	3,50,000	
	To Debentures holders A/c		3,50,000
	(Being amount due to Debentures holders)		
	b Debentures holders A/c Dr.	4,40,000	
	To Chennai Works A/c		4,25,000
	To Equity share capital A/c		15,000
	(Being Chennai works taken over and equity shares issued to 'B' 6% Debenture holders)		
	c Equity share of Zia Ltd. A/c Dr.	90,000	
	To Debentures holders A/c		90,000
	(Being 9,000 equity shares of Zia Ltd. issued by Debentures holders)		
(vii)	a Chennai Works – Workmen Compensation Fund Dr.	4,000	
	To Capital reduction A/c		4,000
	(Being difference due to reduced amount of actual liability transferred to capital reduction account)		
	b Bank A/c Dr.	15,400	
	To Investment for Workmen Compensation Fund		14,000
	To Capital reduction A/c		1,400
	(Being investment for Workmen Compensation Fund sold @ 10% profit)		
	c Trade Payables A/c Dr.	15,400	
	To Bank A/c		15,400
	(Being part payment made to trade payables)		
(viii)	Capital reduction A/c Dr.	2,10,000	
	To Provision for Doubtful Debts A/c		20,000
	To Inventory A/c		1,90,000
	(Being assets revalued)		



(ix)	Capital reduction A/c	Dr.	5,50,000	
	To Profit & Loss A/c			2,00,000
	To PPE – Chennai Works			3,50,000
	(Being assets revalued and losses written off)			
(x)	Capital reduction A/c	Dr.	4,01,400	
	To PPE – Bombay Works			2,67,600
	To Capital reserve A/c			1,33,800
	(Being assets revalued and remaining amount transferred to capital reserve account)			

**Question 5 (RTP Nov'18, RTP Nov'20, May'22)**

The summarized balance sheet of Z Limited as on 31st March, 2017 is as under:

Liabilities	Amount in Rs.
<b>Share Capital:</b>	
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
<b>Reserves and Surplus:</b>	
Profit and Loss Account	(14,60,000)
<b>Non-Current Liabilities:</b>	
10% Secured Debentures	16,00,000
<b>Current Liabilities:</b>	
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
<b>Total</b>	<b>81,00,000</b>
<b>Assets:</b>	
<b>Non-Current Assets:</b>	
Property, Plant & Equipment:	
<b>(a) Tangible Assets:</b>	
Land & Buildings	30,00,000
Plant & Machinery	12,50,000
Furniture & Fixtures	2,50,000
<b>(b) Intangible Assets:</b>	
Goodwill	10,00,000
Patents	5,00,000
<b>Current Assets:</b>	
Trade Investments	5,00,000
Trade Receivables	5,00,000
Inventory	10,00,000
Discount on issue of debentures	1,00,000
<b>Total</b>	<b>81,00,000</b>

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.

**MCQs**

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.

Two companies amalgamated.

**ANSWERS/HINTS****MCQs**

1.	(b)	2.	(a)	3.	(a)	4.	(c)	5.	(a)	6.	(c)
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Wages		1,60,000
Fixed overhead		1,20,000
Variable overhead		<u>60,000</u>
		6,90,000
Less: NRV of by-product Fiber (W.N. 1)	(1,09,000)	
Sale value of scrap	<u>(5,000)</u>	<u>(1,14,000)</u>
Joint cost to be allocated between Polyester and Nylon		<u>5,76,000</u>

**Determination of "basis for allocation" and allocation of joint cost to Polyester and Nylon**

	Polyester	Nylon
Output in units (a)	12,500 units	10,000 units
Sales price per unit (b)	₹ 100	₹ 60
Sales value (a x b)	₹ 12,50,000	₹ 6,00,000
Total value (12,50,000 + 6,00,000) = 18,50,000		
Joint cost of ₹ 5,76,000 allocated in the ratio of 12,50,000 : 6,00,000	₹ 3,89,189	₹ 1,86,811
Cost per unit [c/a]	₹ 31.14	₹ 18.68

**Question 2**

Following is the summarized Balance Sheets of Z Limited as on 31<sup>st</sup> March, 2024:

Particulars	(₹)
<b>EQUITY AND LIABILITIES:</b>	
Share Capital	
Equity shares of ₹ 100 each	60,00,000
8% Preference shares of ₹ 100 each	21,00,000
10% Debentures of ₹ 100 each	18,00,000
Trade Payables	16,80,000
<b>Total</b>	<b>1,15,80,000</b>
<b>ASSETS:</b>	
Goodwill	81,000

Property, Plant and Equipment	72,00,000
Trade Receivables	13,75,000
Inventories	9,80,000
Cash at Bank	1,33,000
Own Debentures (Nominal value of ₹6 lakhs)	5,76,000
Profit and Loss A/c	12,35,000
<b>Total</b>	<b>1,15,80,000</b>

On 1<sup>st</sup> April, 2024, court approved the following reconstruction scheme for Z Limited:

- (i) Each equity share shall be sub-divided into 10 equity shares of ₹10 each fully paid up. After sub-division, equity share capital will be reduced by 40%.
- (ii) Preference share dividends are in arrear for last 4 years. Preference shareholders agreed to waive 75% of their dividend claim and accept payment for the balance.
- (iii) Own debentures of ₹2,40,000 (nominal value) were sold at 98 cum interest and remaining own debentures were cancelled.
- (iv) Debenture holders of ₹6,00,000 agreed to accept one machinery of book value of ₹9,00,000 in full settlement.
- (v) Remaining Property, Plant and Equipment were valued at ₹60,00,000.
- (vi) Trade Payables, Trade Receivables and Inventories were valued at ₹15,00,000, ₹13,00,000 and ₹9,44,000 respectively. Goodwill and Profit and Loss Account (Debit balance) are to be written off.
- (vii) Company paid ₹60,000 as penalty to avoid capital commitments of ₹12 lakhs.
- (viii) Interest on 10% Debentures is paid every year on 31<sup>st</sup> March.

**You are required to:**

- (1) Pass necessary journal entries in the books of Z Limited to implement the above schemes.
- (2) Prepare Capital Reduction Account.
- (3) Prepare Bank Account

**(14 Marks)**

**Answer****1. Journal entries****In the Books of Z Ltd. as on 1<sup>st</sup> April 2024**

	Particulars		Dr.	Cr.
01.04.2024			Amount (₹)	Amount (₹)
1.	Equity share capital A/c (₹ 100) To Equity share capital A/c (₹ 10) (Being sub-division of one share of ₹ 100 each into 10 shares of ₹ 10 each)	Dr.	60,00,000	60,00,000
2.	Equity share capital A/c (₹ 10) To Capital reduction A/c (Being reduction of Equity capital by 40%)	Dr.	24,00,000	24,00,000
3.	Capital reduction A/c To Bank A/c (Being payment in cash of 25% of arrear of preference dividend) [21,00,000x8%] x 4 years	Dr.	1,68,000	1,68,000
4.	Bank A/c To Own debentures A/c (5,76,000/6,00,000) x 2,40,000 To Capital reduction A/c (Being profit on sale of own debentures of ₹ 2,40,000 transferred to capital reduction A/c)	Dr.	2,35,200	2,30,400 4,800
5.	10% Debentures A/c (6,00,000 -2,40,000) To Own debentures A/c To Capital reduction A/c (Being profit on cancellation of own debentures transferred to capital reduction A/c)	Dr.	3,60,000	3,45,600 14,400

6.	10% Debentures A/c Capital reduction A/c To Machinery or PPE A/c (Being machinery taken up by debenture holders for ₹ 6,00,000)	Dr.	6,00,000	
		Dr.	3,00,000	9,00,000
7.	Capital reduction A/c (balancing figure) To PPE A/c (72,00,000 - 9,00,000 - 60,00,000) (Being PPE revalued)	Dr.	3,00,000	3,00,000
8.	Trade payables A/c (16,80,000 - 15,00,000) To Trade receivables A/c (13,75,000 - 13,00,000) To Inventory A/c (9,80,000 - 9,44,000) To Capital Reduction A/c (Being assets and liabilities revalued)	Dr.	1,80,000	75,000 36,000 69,000
9.	Capital reduction A/c To Goodwill A/c To Profit and Loss A/c (Being the above assets written off)	Dr.	13,16,000	81,000 12,35,000
10.	Capital reduction A/c To Bank A/c (Being penalty paid for avoidance of capital commitments)	Dr.	60,000	60,000
11.	Capital reduction A/c To Capital reserve A/c (Being the credit balance in Capital Reduction A/c transferred to Capital Reserve)	Dr.	3,44,200	3,44,200

2. **Capital Reduction Account**

	(₹)		(₹)
To Bank	1,68,000	By Equity Share Capital	24,00,000
To Property, Plant & Equipment	3,00,000	By Trade Payable	1,80,000
To Property, Plant & Equipment	3,00,000	By Bank A/c (Profit on Sale)	4,800
To Trade Receivables	75,000	By 10% debentures A/c (Profit on cancellation)	14,400
To Inventory	36,000		
To Goodwill	81,000		
To Profit and Loss A/c	12,35,000		
To Cash/Bank A/c	60,000		
To Capital Reserve	<u>3,44,200</u>		
	<u>25,99,200</u>		<u>25,99,200</u>

3. **Bank Account**

	₹		₹
To To balance b/d	1,33,000	By Capital Reduction	1,68,000
To Own Debenture	2,35,200	By Capital Reduction A/c	60,000
(2,30,400 + 4,800)	<u>        </u>	By balance c/d	<u>1,40,200</u>
	<u>3,68,200</u>		<u>3,68,200</u>

**Question 3**

- (a) *Constructions Limited is engaged in the business of constructing Flyovers and Railway over bridges. It obtained a contract from Railway Authorities to construct a railway over bridge for ₹ 400 crores. The construction of the railway over bridge is expected to be completed in 4 years.*

*At the outset of the contract, it was estimated that the total costs to be incurred will be ₹ 370 crores but by the end of year 1, this estimate stands revised to ₹ 375 crores.*