Solution:

Maximum shares that can be bought back

		Situation I	*Situation II*	*Situation III*
a.	Shares outstanding test (WN # 1)	7.5	7.5	7.5
b.	Resources test (WN # 2)	6	6	6
c.	Debt Equity ratio test (WN # 3)	10.67	4	—
d.	Maximum number of shares for buy back - LEAST of the above	6	4	—

	Particulars		**Situation I**		**Situation II**	
			Debit	**Credit**	**Debit**	**Credit**
a.	Shares bought back A/c	Dr.	180		120	
	To Bank A/c			180		120
	[Being purchase of shares from public]					
b.	Share capital A/c	Dr.	60		40	
	Securities premium A/c	Dr.	100		80	
	General reserve A/c (*balancing figure*)	Dr.	20		—	
	To Shares bought back A/c			180		120
	[Being cancellation of shares bought on buy back]					
c.	General Reserves A/c					
	To Capital Redemption Reserve A/c					
	[Being transfer of reserves to capital redemption reserve to the extent capital is redeemed]					

Note: Under situation III, the company does not qualify the debt equity ratio test. Therefore the company cannot perform the buy back of shares (Under section 77A of the Companies Act, 1956)

WORKING NOTES:

WN # 1 : Shares outstanding test

	Particulars	**Amount**
a.	No. of shares outstanding	30 crores
b.	25% of shares outstanding	7.5 crores

WN # 2 : Resources test

(Rs. in Crores)

	Particulars	Amount
a.	Paid up capital	300
b.	Free reserves	420
c.	Shareholders fund (a+b)	720
d.	25% of shareholders fund	180
e.	Buyback price per share	Rs. 30
f.	Number of shares that can be bought back	6 Crores

WN # 3 : Debt Equity ratio test:

(Rs. in Crores)

	Particulars	*Situation I*	*Situation II*	*Situation III*
a.	Borrowed Funds	800	1,200	1,500
b.	Minimum equity to be maintained after buy back in the ratio 2:1	400	600	750
c.	Present equity	720	720	720
d.	Maximum possible dilution in equity	320	120	—
e.	Maximum shares that can be bought back @ Rs. 30/- per share	10.67	4	—

XV. Conversion:

Illustration - 46

X Co. Ltd. was incorporated on 1st July, 2008 to take over the business of Mr. A as and from 1st April, 2008, Mr. A's Balance Sheet, as at that date, was as under :

Liabilities	*Rs.*	*Assets*	*Rs.*
Trade creditors	36,000	Building	80,000
Capital	1,94,000	Furniture and Fittings	10,000
		Debtors	90,000
		Stock	30,000
		Bank	20,000
	2,30,000		**2,30,000**

Debtors and Bank balance are to be retained by the vendor and creditors are to be paid off by him. Realisation of debtors will be made by the company on a commission of 5% on cash collected. The company is to issue A with 10,000 equity shares of Rs. 10 each, Rs. 8 per share paid up and cash of Rs. 5,000.

The company issued to the public for cash 20,000 equity shares of Rs. 10 each on which by 31 st March, 2009, Rs.8 per share was called and paid up except in the case of 1,000 shares on which the 3rd call of Rs. 2 per share had not been reatised. In the case of 2,000 shares, the entire face value of the shares has been realised. The share issue was underwritten for 2% commission, payable in shares fully paid up.

Liabilities	*AB Ltd. Rs.*	*XY Ltd. Rs.*	*Assets*	*AB Ltd. Rs.*	*XY Ltd. Rs.*
Bank Overdraft	–	100			
Sundry creditors	300	300			
Proposed Dividend	200	–			
Total	**4,050**	**1,800**	**Total**	**4,050**	**1,800**

It was decided that XY Ltd. will acquire the business of AB Ltd. for enjoying the benefit of carry forward of business loss. After acquisition, XY Ltd. will be renamed as Z Ltd. The following scheme has been approved for the merger.

i. XY Ltd. will reduce its shares to Rs. 10 and then consolidate 10 such shares into one share of Rs. 100 each (New Share).

ii. Financial institutions agreed to waive 15% of the loan of XY Ltd.

iii. Shareholders of AB Ltd. will be given one new share of XY Ltd. in exchange of every share held in AB Ltd.

iv. AB Ltd. will cancel 20% holdings of XY Ltd. Investments were held at Rs. 250 thousands.

v. After merger, the proposed dividend of AB Ltd. will be paid to the shareholders of ABLtd.

vi. Authorised Capital of XY Ltd. will be raised accordingly to carry out the scheme. vii. Sundry creditors of XY Ltd. includes payables to AB Ltd. Rs. 1,00,000.

Pass the necessary entries to implement the scheme in the books of AB Ltd. and XY Ltd. and prepare a Balance Sheet of Z Ltd.

Solution:

Part - I Purchase consideration

WN # 1: ***Shareholding of AB Ltd. in XY Ltd.***

Particulars		*Amount Rs.*
a.	Original Share capital of XY Ltd. [10,000 equity shares of Rs. 100 each]	10,00,000
b.	Share capital of XY Ltd. after reduction [10,000 equity shares of Rs. 10 each]	1,00,000
c.	Share capital of XY Ltd. after reconsolidation [1000 equity shares of Rs. 100 each]	1,00,000
d.	Holding of AB Ltd in XY Ltd.	20%
e.	Value of holding of AB Ltd in XY Ltd. [200 equity shares of Rs. 100 each]	20,000

WN # 2 : *Purchase consideration*

a.	No. of equity shares of AB Ltd. (20,00,000 ÷ 100)	20,000
b.	Exchange ratio	1:1
c.	No. of equity shares to be given by XY Ltd. to AB Ltd.	20,000
d.	Less : No. of Equity shares held by AB Ltd. in XY Ltd.	200
e.	No. of shares now to be given	19,800
f.	Purchase consideration (19,800 equity shares of Rs. 100 each)	19,80,000

Part - II : Journal entries in the books of AB Ltd.

(Rs. '000)

Particulars		*Debit*	*Credit*
1. a. Transfer to realisation account of all Assets taken *over* except investment held by selling company in purchasing company			
Realisation A/c	Dr.	3,800	
To Fixed assets A/c			2,700
To Investments [700 - 250] A/c			450
To Sundry Debtors A/c			400
To Cash and Bank A/c			250
b. Transfer to realisation account of all liabilities taken over			
10% Debentures A/c	Dr.	500	
Loan from financial institations A/c	Dr.	250	
Sundry Creditors A/c	Dr.	300	
Proposed Dividend A/c	Dr.	200	
To Realisation A/c			1250
2. Purchase consideration			
a. Due entry			
XY Ltd. A/c	Dr.	1,980	
To Realisation A/c			1,980
b. Receipt			
Shares in XY Ltd. A/c	Dr.	1,980	
To XY Ltd. A/c			1,980
3. Transfer of realisation loss to share holders			
Equity shareholders A/ c	Dr.	570	
To Realisation A/c			570
4. Transfer of Share capital and Reserves and surplus to equity share holders			
Share capital A/c	Dr.	2,000	
Reserves and surplus A/c	Dr.	800	
To Equity shareholders			2,800
5. Settlement to share holders by transfer of purchase consideration now received and shares already held by AB Ltd. in XY Ltd.			
Equity shareholders A/c	Dr.	2,230	
To Equity shares of XY Ltd.			2,230

Part.* III. *Journal entries in the books of XY Ltd.

(Rs. '000)

Particulars		*Debit*	*Credit*
1. Reduction of Share capital			
Equity Share Capital (Rs. 100) A/c	Dr.	1,000	
To Equity Share Capital (Rs. 10) A/c			100
To Reconstruction A/c			900
2. Consolidation of equity shares of Rs.10 each to Rs. 100 each			
Equity Share Capital (Rs. 10) A/c	Dr.	100	
To Equity Share Capital (Rs. 100) A/c			100
3. Waiver of loan by financial institution			
Loan from financial institution A/c	Dr.	60	
To Reconstruction A/c			60
4. Write off the debit balance of Profit and Loss A/c by utilising Reconstruction A/c and balance of Reconstruction A/c transferred to Capital reserve			
Reconstruction A/c	Dr.	960	
To Profit and Loss A/c			800
To Capital Reserve A/c			160

***Entries relating to Amalgamation* :**

- Nature of Amalgamation - Merger
- Method of Accounting - Pooling of Interest Method

(Rs. '000)

Particulars			*Debit*	*Credit*
1. For Purchase Consideration Due				
Business Purchase A/c Dr.			1,980	
To Liquidator of AB Ltd. A/c				1,980
2. For assets and liabilities taken over				
Purchase consideration now paid		1,980		
Shares already held by AB Ltd.		250		
Total consideration		2,230		
Less: Paid-up Share capital of AB Ltd.		2,000		
Excess Purchase Consideration Paid		230		
This excess is to be adjusted against reserves of AB Ltd.				
Reserves of AB Ltd.	800			
Less: Excess as above	230			
Balance to be incorporated	570			

Particulars		Debit	Credit
Fxed assets (net of depreciation) A/c	Dr.	2,700	
Investment A/c	Dr.	450	
Sundry Debtors A/c	Dr.	400	
Cash and Bank A/c	Dr.	250	
To Reserves and Surplus A/c			570
To Debentures A/c			500
To Loan from financial institutions A/c			250
To Sundry Creditors A/c			300
To Proposed Dividend A/c			200
To Business Purchase A/c			1,980
3. Discharge of purchase consideration			
Liquidator of AB Ltd. A/c	Dr.	1,980	
To Equity Share capital of XY Ltd. A/c			1,980
4. Payment of proposed divided to shareholders of AB Ltd.			
Proposed Dividend A/c	Dr.	200	
To Bank A/c			200
5. Cancellation of inter company owings			
Sundry Creditors A/c	Dr.	100	
To Sundry Debtors A/c			100

***Balance sheet of Z Ltd. as* on 31st *March* 09**
(After Acquisition)

(Rs.'000)

Liabilities	*Amount Rs.*	*Assets*	*Amount Rs.*
Share capital		Fixed assets net of depreciation	3,550
20,800 equity shares @		[2,700 + 850]	
Rs.100/- each [1980+20+80]	2,080		
Reserves and surplus		Investments [700-250]	450
Capital reserves	160	Sundry debtors [400 + 150 – 100]	450
General reserves	570		
Secured loan :			
10% Debentures	500		
Loan from Finanacial			
Institution (340 + 250)	590		
Bank over draft			
[200+100-250]	50		
Current liabilities and			
provisions			
Creditors [600-100)	500		
	4,450		**4,450**