

Accounting for Corporate Restructuring

BASIC CONCEPTS

Corporate restructuring (CR) is a broad term to denote significant reorientation or realignment of the investment (assets) and/or financing (liabilities) structure of a company through conscious management action with a view to drastically alter the quality and quantum of its future cash flow streams. This broad definition includes such corporate actions as mergers, acquisitions/ amalgamations/ absorption, divestitures, demergers (spin-offs) and debt-equity changes.

The different methods of restructuring and their implications are discussed below:

- (1) External Restructuring
 - (a) Asset-based (portfolio) restructuring
 - (b) Financial or capital restructuring
- (2) Internal Restructuring
 - (a) Portfolio restructuring (Cost reduction through closure of units, redundancy programmes etc.)
 - (b) Organisational restructuring (Management or organisational restructuring involving decentralisation, delayering, product-market based divisionalisation, matrix structure etc.)
- (3) Amalgamation, absorption or external reconstruction.

Asset-based Restructuring

(i) Mergers and Acquisitions (M & A)

In the Indian context the term merger is used to denote consolidation of separate legal entities, not necessarily of similar sizes, into one through a statutory process of amalgamation. The motives of merger or acquisition are the same and both involve transfer of ownership and control of assets and the right to manage corporate cash flows.

For Example-Reliance Natural and Reliance Power Merger

(ii) Divestitures and Asset Swaps

Divestiture refers to disposal (in favour of third party) of business units, subsidiary companies or significant holdings in associates, often for cash. Asset swap, on other hand, entails simultaneous divesting and acquisition of each others' business by two companies, settling the difference in valuation, if any in cash.

(iii) **Demergers or Spin-offs**

Demerger involves spinning off (profitable or robust) parts of a diversified company into a new company and undertaking free distribution of the shares of the new (spun-off) company to the shareholders of the original company. For Example-RIL gets split among several companies between two brothers-Mukesh and Anil Ambani.

Unlike in a divestiture, the “parent” company or group does not receive any proceeds from a demerger as the demerged company’s shares are directly distributed to the “parent” company’s shareholders.

Capital and Financial Restructuring

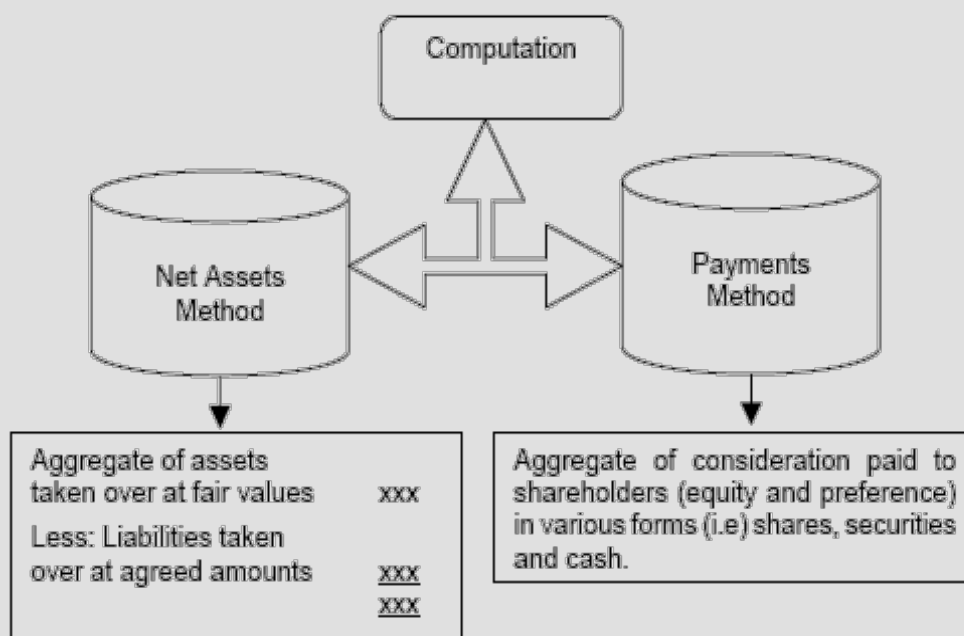
This type of restructuring includes buy back of shares, debt to equity conversions etc.

Purchase Consideration (PC)

In the problem information for PC will be available in two ways. Firstly, list of the various consideration paid is given, one should take care to add only those items paid to the members of the company and not to any outsider.

Secondly, assets and liabilities taken over are given in the problem. Purchase consideration in this case will be the net assets taken over by the amalgamated company.

Computation of Purchase consideration



Discharge of Purchase Consideration

The purchase consideration in the case of amalgamation is payable to the shareholders, both preference and equity, of the transferor company. This may be discharged by issuing preference and/or equity shares of the transferee company and partly by cash. Often the transferee company discharges claims of the preference shareholders of the transferor company at a premium or at a discount by issuing preference shares. Similarly, claims of the equity shareholders of the transferor company may also be discharged by issuing equity shares of the transferee company either at par or at premium or at discount. Debentures paid to shareholders of the transferor company will be considered as part of purchase consideration but debentures paid to the debenture holders or to the sundry creditors of the transferor company will not form part of purchase consideration.

Methods of Accounting for Amalgamation

There are two main methods of accounting for amalgamations:

- (a) The Pooling of Interest Method (for amalgamation in the nature of merger), and
- (b) The Purchase Method (for amalgamation in the nature of purchase).

The first method is applied in case of amalgamation in the nature of merger and the second method in case of amalgamation in the nature of purchase.

- **The Pooling of Interest Method:** Under this method the assets, liabilities and all reserves of the transferor company are recorded by transferee company at their existing carrying amounts unless the carrying amounts are to be adjusted to follow a uniform set of accounting policies. The balance of the profit and loss account of the transferor company should be aggregated with the corresponding balance of the transferee company or transferred to general reserve, if any.

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 reserves.

Therefore, no 'goodwill' arises in case of amalgamations in the nature of merger.

- **The Purchase Method :** Here the assets and liabilities of the transferor company should be incorporated in the transferee company's financial statements in either of the following two ways:
 - (i) at their existing carrying amounts; or
 - (ii) the purchase consideration should be allocated to individual identifiable assets and liabilities on the basis of their fair values at the date of amalgamation.

Question 1

The summarized Balance Sheet of Z Ltd. as at 31st March, 2012 is given below. In it, the respective shares of the company's two divisions namely S Division and W Division in the various assets and liabilities have also been shown.

(₹ in crores)

	S Division	W Division	Total
Fixed Assets:			
Cost	875	249	
Less: Depreciation	<u>(360)</u>	<u>(81)</u>	
Written-down value	<u>515</u>	<u>168</u>	683
Investments			97
Net Current assets:			
Current Assets	445	585	
Less: Current Liabilities	<u>(270)</u>	<u>(93)</u>	
	<u>175</u>	<u>492</u>	<u>667</u>
			<u>1,447</u>
Financed by:			
Loan funds		15	417
Own funds:			
Equity share capital: shares of ₹ 10 each			345
Reserves and surplus			<u>685</u>
			<u>1,447</u>

Loan funds included, inter alia, Bank Loans of ₹ 15 crores specifically taken for W Division and Debentures of the paid up value of ₹ 125 crores redeemable at any time between 1st October, 2011 and 30th September, 2012.

On 1st April, 2012 the company sold all of its investments for ₹ 102 crores and redeemed all the debentures at par, the cash transactions being recorded in the Bank Account pertaining to S Division.

Then a new company named Y Ltd. was incorporated with an authorized capital of ₹ 900 crores divided into shares of ₹ 10 each. All the assets and liabilities pertaining to W Division were transferred to the newly formed company; Y Ltd. allotting to Z Ltd.'s shareholders its two fully paid equity shares of ₹ 10 each at par for every fully paid equity share of ₹ 10 each held in Z Ltd. as discharge of consideration for the division taken over.

Y Ltd. recorded in its books the fixed assets at ₹ 218 crores and all other assets and liabilities at the same values at which they appeared in the books of Z Ltd.

4.6 Financial Reporting

You are required to:

- Show the journal entries in the books of Z Ltd.
- Prepare Z Ltd.'s Balance Sheet immediately after the demerger and the initial Balance Sheet of Y Ltd.
- Calculate the intrinsic value of one share of Z Ltd. immediately before the demerger and immediately after the demerger; and
- Calculate the gain, if any, per share to the shareholders of Z Ltd. arising out of the demerger.

Answer

(i) **Journal Entries in Z Ltd.'s books** (*₹ in crores*)

	Dr. Amount	Cr. Amount
Bank Account (Current Assets) Dr.	102	
To Investments		97
To Profit and Loss Account (Reserves and Surplus)		5
(Sale of investments at a profit of ₹ 5 crores)		
Debentures (Loan Funds) Dr.	125	
To Bank Account (Current Assets)		125
(Redemption of debentures at par)		
Current Liabilities Dr.	93	
Bank Loan (Loan Funds) Dr.	15	
Provision for Depreciation Dr.	81	
Reserves and Surplus (Loss on Demerger) Dr.	645	
To Fixed Assets		249
To Current Assets		585
(Assets and liabilities pertaining to W Division taken out of the books on transfer of the division to Y Ltd.)		

(ii) (a) **Z Ltd.'s Balance Sheet after demerger**

Particulars	Note No.	(₹ in crores)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		345
(b) Reserve and Surplus	1	45
(2) Non-Current Liabilities		

Long-term borrowings	2	277
(3) Current Liabilities		270
Total		937
II. Assets		
(1) Non-current assets		
Fixed assets		
Tangible assets		515
(2) Current assets	3	422
Total		937

Notes to Accounts:

	(₹ in crores)
1. Reserves and Surplus	
Balance as on 31st March, 2012	685
Add: Profit on sale of investments	<u>5</u>
	690
Less: Loss on demerger	<u>(645)</u>
Balance shown in balance sheet after demerger	<u>45</u>
2. Loan Funds	
Balance as on 31st March, 2012	417
Less: Bank Loan transferred to Y Ltd. 15	
Debentures redeemed <u>125</u>	<u>(140)</u>
Balance shown in balance sheet after demerger	<u>277</u>
3. Current Assets	
Balance as on 31st March, 2012	445
Add: Cash received from sale of investments	<u>102</u>
	547
Less: Cash paid to redeem debentures	<u>(125)</u>
Balance in balance sheet after demerger	<u>422</u>

(b) Initial Balance Sheet of Y Ltd.

Particulars	Note No.	(₹ in crores)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	690

4.8 Financial Reporting

(b) Reserves and Surplus	2	5
(2) Non-Current Liabilities		
Long-term borrowings	3	15
(3) Current Liabilities		93
Total		803
II. Assets		
(1) Non-current assets		
Fixed assets		218
(2) Current assets		585
Total		803

Notes to Accounts:

1. Share Capital

	(₹ in crores)
Authorised capital	
90 crores Equity shares of ₹ 10 each	900
Issued and subscribed capital	
69 crores Equity shares of ₹ 10 each	690
(issued for consideration other than cash)	

2. Reserves and Surplus

	(₹ in crores)
Capital Reserve	
Purchase consideration	690
Less: Assets transferred	710
Loan funds transferred	(15)
Capital reserve	5

3. Long-term borrowing

Loan Funds	15
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(iii) Calculation of intrinsic value of one share of Z Ltd.

	₹ in crores
<i>Before demerger</i>	
Fixed Assets	683
Net current assets ₹ (667 + 102 – 125)	644
	1,327

Less: Loan funds ₹ (417 – 125)	<u>(292)</u>
	<u>1,035</u>
Intrinsic Value per share = ₹ $\frac{1,035 \text{ crores}}{34.5 \text{ crores}}$ = ₹ 30 per share	
<i>After demerger</i>	
Fixed Assets	515
Net Current Assets ₹ (175 + 102 – 125)	<u>152</u>
	667
Less: Loan funds	<u>(277)</u>
	<u>390</u>

Intrinsic Value of one share = ₹ $\frac{390 \text{ crores}}{34.5 \text{ crores}}$ = ₹ 11.30 per share

(iv) Gain per share to Shareholders:

After demerger, for every share in Z Ltd. the shareholder holds 2 shares in Y Ltd.

	₹
Value of one share in Z Ltd.	11.30
Value of two shares in Y Ltd. (₹ 10 × 2)	<u>20.00</u>
	31.30
Less: Value of one share before demerger	<u>(30.00)</u>
Gain per share	<u>1.30</u>

The gain per share amounting ₹ 1.30 is due to appreciation in the value of fixed assets by Y Ltd.

Question 2

Ksha Ltd. and Yaa Ltd. are two companies. On 31st March, 2012 their summarised Balance Sheets were as under:

(₹ in crores)

	Ksha Ltd.		Yaa Ltd.	
	₹	₹	₹	₹
Sources of funds:				
Share Capital:				
Authorised:		<u>500</u>		<u>500</u>
Issued: Equity shares of ₹ 10 each fully paid up		300		200
Reserves and surplus:				
Capital reserves	40		20	

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Revenue reserves	700		425	
Surplus	<u>10</u>	<u>750</u>	<u>5</u>	<u>450</u>
Owners' funds		1,050		650
Loan funds		<u>250</u>		<u>350</u>
		<u>1,300</u>		<u>1,000</u>
Fund employed in:				
Fixed assets:				
Cost	1,000		700	
Less: Depreciation	<u>(400)</u>	600	<u>(300)</u>	400
Net current assets:				
Current assets	2,000		1,500	
Less: Current liabilities	<u>(1,300)</u>	<u>700</u>	<u>(900)</u>	<u>600</u>
		<u>1,300</u>		<u>1,000</u>

Ksha Ltd. has 2 divisions very profitable division A and loss making division B. Yaa Ltd. similarly has 2 divisions very profitable division B and loss making division A.

The two companies decided to reorganize. Necessary approvals from creditors and members and sanction by High Court have been obtained to the following scheme:

1. Division B of Ksha Ltd. which has fixed assets costing ₹ 400 crores (written down value ₹ 160 crores), Current assets ₹ 900 crores, Current liabilities ₹ 750 crores and loan funds of ₹ 200 crores is to be transferred at ₹ 125 crores to Yaa Ltd.
2. Division A of Yaa Ltd. which has fixed assets costing ₹ 500 crores (depreciation ₹ 200 crores), Current assets ₹ 800 crores, Current liabilities ₹ 700 crores, and loan funds ₹ 250 crores is to be transferred at ₹ 140 crores to Ksha Ltd.
3. The difference in the two considerations is to be treated as loan carrying interest at 15% per annum.
4. The directors of each of the companies revalued the fixed assets taken over as follows:
 - (i) Division of A of Yaa Ltd. taken over: ₹ 325 crores.
 - (ii) Division B of Ksha Ltd. taken over: ₹ 200 crores.

All the other assets and liabilities are recorded at the balance sheet values.

- (a) The directors of both the companies ask you to prepare the balance sheets after reconstruction (showing the corresponding figures before reconstruction).

- (b) Master Richie Rich, who owns 50,000 equity shares of Ksha Ltd. and 30,000 equity shares of Yaa Ltd. wants to know whether he has gained or lost in terms of net asset value of equity shares on the above reorganizations.

Answer

(a)

Ksha Ltd.
Balance Sheet as at 31st March, 2012

Particulars	Note No.	After reconstruction (₹ in crores)	Before reconstruction (₹ in crores)
I. Equity and Liabilities			
(1) Shareholder's Funds			
(a) Share Capital	1	300	300
(b) Reserve and Surplus	2	800	750
(2) Non-Current Liabilities			
Long-term borrowings	3	315	250
(3) Current Liabilities		1250	1300
Total		2665	2600
II. Assets			
(1) Non-current assets			
(a) Fixed assets			
Tangible assets	4	765	600
(2) Current assets		1900	2000
Total		2665	2600

Notes to Accounts

Particulars	After reconstruction (₹ in Crores)	Before reconstruction (₹ in Crores)
1. Share Capital		
Authorised:		
50 crores equity shares of ₹10 each	<u>500</u>	<u>500</u>
Issued and subscribed:		
30 crores equity shares of ₹10 each fully paid up	300	300

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2.	Reserves and surplus				
	Capital reserves	40		40	
	Add: Capital profit on reconstruction	50		-	
	Revenue reserves	700		700	
	Surplus	<u>10</u>	800	<u>10</u>	750
3.	Long term Borrowings				
	Yaa Ltd. (Interest @ 15% p.a.)	15			
	Others	<u>300</u>	315		250
4.	Fixed assets:				
	Gross block	925		1,000	
	Less: Depreciation	<u>(160)</u>		<u>(400)</u>	
	Net block		765		600

Yaa Ltd.

Balance Sheet as at 31st March, 2012

Particulars	Note No.	After reconstruction	Before reconstruction
		(₹ in Crores)	(₹ in Crores)
I. Equity and Liabilities			
(1) Shareholder's Funds			
(a) Share Capital	1	200	200
(b) Reserves and Surplus	2	465	450
(2) Non-Current Liabilities			
Long-term borrowings		300	350
(3) Current Liabilities		950	900
Total		1915	1900
II. Assets			
(1) Non-current assets			
Fixed assets			
Tangible assets	3	300	400
(2) Current assets			
(a) Short term loans and advances	4	15	-
(b) Other current assets		1600	1500
Total		1915	1900

Notes to Accounts

Particulars		After reconstruction		Before reconstruction	
		(₹ in Crores)		(₹ in Crores)	
1.	Share Capital				
	Authorized:				
	50 crores equity shares of ₹ 10 each		<u>500</u>		<u>500</u>
	Issued and subscribed:				
	30 crores equity shares of ₹ 10 each fully paid up		200		200
2.	Reserves and surplus				
	Capital reserves	20		20	
	Add: Capital profit on reconstruction	<u>15</u>	35	—	20
	Revenue reserves		425		425
	Surplus		<u>5</u>		<u>5</u>
			<u>465</u>		<u>450</u>
3.	Tangible assets:				
	Gross block	400		700	
	Less: Depreciation	<u>(100)</u>		<u>(300)</u>	
	Net block		300		400
4.	Short term loans and advances				
	Loan to Ksha Ltd.		15		----

(b) Net asset value of Master Riche Rich's holdings

	Pre-reorganisation	Post-reorganisation	Change (Gain)
	(₹)	(₹)	(₹)
Net asset value of one equity share: (Refer to working notes)			
Ksha Ltd.	35.00	36.67	1.67
Yaa Ltd.	32.50	33.25	0.75
Net asset value of equity shares owned by Master Riche Rich			
Ksha Ltd. (50,000 shares)	17,50,000	18,33,500	83,500
Yaa Ltd. (30,000 shares)	<u>9,75,000</u>	<u>9,97,500</u>	<u>22,500</u>
	<u>27,25,000</u>	<u>28,31,000</u>	<u>1,06,000</u>

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Master Riche Rich has gained in terms of net asset value of his holdings as indicated in the last column.

Working Notes:

(1) Ksha Ltd.

(₹ in crores)

		Pre-re- organisation figures	Sale of division B	Purchase of division A of Yaa Ltd.	Post-re- organisation figures
		(a)	(b)	(c)	(d) = (a) – (b) + (c)
(i)	Fixed assets:				
	Cost	1,000	400	325	925
	Depreciation	<u>(400)</u>	<u>(240)</u>	—	<u>(160)</u>
	Written down value (I)	<u>600</u>	<u>160</u>	<u>325</u>	<u>765</u>
	Current assets	2,000	900	800	1,900
	Current liabilities	<u>(1,300)</u>	<u>(750)</u>	<u>(700)</u>	<u>(1,250)</u>
	Net current assets (II)	<u>700</u>	<u>150</u>	<u>100</u>	<u>650</u>
	Funds employed [(I) + (II)]	1,300	310	425	1,415
	Loan funds:				
	Others (III)	(250)	(200)	(250)	(300)
	Yaa Ltd. (balance payable on transfers of divisions i.e. ₹ 140 – ₹ 125) (IV)	—	—	—	<u>(15)</u>
	Net worth (I + II – III – IV)	<u>1,050</u>	<u>110</u>	<u>175</u>	<u>1,100</u>

(ii)	Sale of division B	(₹ in crores)
	Transfer price	125
	Cost of the division (₹160 + ₹ 150 – ₹ 200)	<u>(110)</u>
	Capital Profit	<u>15</u>
(iii)	Purchase of division A of Yaa Ltd.	(₹ in crores)
	Agreed value of assets less liabilities taken over ₹ (325 + 100 – 250)	175
	Less: Transfer price	<u>(140)</u>
	Capital Profit	<u>35</u>

(iv)		(₹ in crores)
	Pre-reorganisation net worth	1,050
	Add: Capital profit on	
	Sale	15
	Acquisition	<u>35</u>
	Post-reorganisation net worth	<u>1,100</u>

No. of equity shares	30 crores
Net asset value of equity share:	₹
Pre-reorganisation	1,050/30 = 35.00
Post-reorganisation	1,100/30 = 36.67 (rounded off)

(2) Yaa Ltd.

(i)

(₹ in crores)

	<i>Pre-re- organisation figures</i>	<i>Sale of division A</i>	<i>Purchase of division B of Ksha Ltd.</i>	<i>Post-re- organisation figures</i>
	(a)	(b)	(c)	(d) = (a) – (b) + (c)
Fixed assets:				
Cost	700	500	200	400
Depreciation	<u>(300)</u>	<u>(200)</u>	—	<u>(100)</u>
Written down value (I)	<u>400</u>	<u>300</u>	<u>200</u>	<u>300</u>
Current assets	1,500	800	900	1,600
Current liabilities	<u>(900)</u>	<u>(700)</u>	<u>(750)</u>	<u>(950)</u>
Net current assets (II)	<u>600</u>	<u>100</u>	<u>150</u>	<u>650</u>
Funds employed [(I) + (II)]	1,000	400	350	950
Loan funds—others (III)	<u>(350)</u>	<u>(250)</u>	<u>(200)</u>	<u>(300)</u>
	650	150	150	650
Ksha Ltd. (balance on account of transfers of divisions) (IV)	—	—	—	15
Net worth (I + II – III + IV)	<u>650</u>	<u>150</u>	<u>150</u>	<u>665</u>

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(ii) (₹ in crores)

	Purchase of division B of Ksha Ltd.		Sale of division A
Value of assets less liabilities (Value to Yaa Ltd.) (200 + 900 – 750 – 200)	150	(300 + 800 – 700 – 250)	150
Less: Transfer Price	<u>(125)</u>		<u>(140)</u>
Capital Profit	<u>25</u>		<u>(10)</u>

(iii) (₹ in crores)

Pre-reorganisation net worth		650
Add: Capital profit - on acquisition	25	
- Sale	<u>(10)</u>	<u>15</u>
Post-reorganisation net worth		<u>665</u>

No. of equity shares 20 crores

Net asset value of equity share: ₹

Pre-reorganisation 650/20 = 32.50

Post-reorganisation 665/20 = 33.25

Question 3

The summarized Balance Sheet of Gunshot Ltd. as on 31.3.2012 is given:

(₹ in '000)

Liabilities	Amount	Assets	Amount
Share Capital :		Fixed Assets	2,700
Equity shares of ₹ 10 each	800	Non-trade Investments	300
Securities Premium	100	Stock	600
General Reserve	780	Sundry Debtors	360
Profit and Loss Account	120	Cash and Bank	160
10% Debenture	2,000		
Creditors	<u>320</u>		
	<u>4,120</u>		<u>4,120</u>

Gunshot Ltd. buy back 16,000 shares of ₹ 20 per share. For this purpose, the Company sold its all non-trade investments for ₹ 3,20,000. Give Journal Entries with full narrations affecting the buy back.

Answer

In the books of Gunshot Ltd.
Journal Entries for Buy-back of shares

			₹	₹
(i)	Bank A/c To Non-trade Investments To Profit & Loss A/c (Being the entry for sale of Non-trade Investments)	Dr.	3,20,000	3,00,000 20,000
(ii)	Shares Buy back A/c (16,000 x ₹ 20) To Bank A/c (Being purchase of 16,000 shares @ ₹ 20 per share)	Dr.	3,20,000	3,20,000
(iii)	Equity Share Capital A/c (16,000 x ₹ 10) Buy-back Premium (16,000 x ₹ 10) To Shares Buy-back A/c (Being cancellation of shares bought back)	Dr. Dr.	1,60,000 1,60,000	3,20,000
(iv)	Securities Premium A/c General Reserve To Buy-back Premium (Being adjustment of buy-back premium)	Dr. Dr.	1,00,000 60,000	1,60,000
(v)	General Reserve To Capital Redemption Reserve (Being the entry for transfer of General Reserve to Capital Redemption Reserve to the extent of face value of equity shares bought back)	Dr.	1,60,000	1,60,000

Question 4

A Ltd. and B Ltd. were amalgamated on and from 1st April, 2012. A new company C Ltd. was formed to take over the business of the existing companies. The summarized Balance Sheets of A Ltd. and B Ltd. as on 31st March, 2012 are given below:

Liabilities	(₹ in lakhs)		Assets	(₹ in lakhs)	
	A Ltd.	B Ltd.		A Ltd.	B Ltd.
Share Capital			Fixed Assets		
Equity Shares of ₹ 100 each	800	750	Land and Building	550	400
12% Preference shares of ₹ 100 each	300	200	Plant and Machinery	350	250
Reserves and Surplus			Investments	150	50
Revaluation Reserve	150	100	Current Assets,		

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General Reserve	170	150	Loans and Advances		
Investment Allowance Reserve	50	50	Stock	350	250
Profit and Loss Account	50	30	Sundry Debtors	250	300
Secured Loans			Bills Receivable	50	50
10% Debentures (₹ 100 each)	60	30	Cash and Bank	300	200
Current Liabilities and provisions					
Sundry Creditors	270	120			
Bills Payable	<u>150</u>	<u>70</u>			
	<u>2,000</u>	<u>1,500</u>		<u>2,000</u>	<u>1,500</u>

Additional Information:

- (1) 10% Debentureholders of A Ltd. and B Ltd. are discharged by C Ltd. issuing such number of its 15% Debentures of ₹ 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 ₹ 150 per share (face value of ₹ 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 @ ₹ 30 each, having a face value of ₹ 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, 2012 after the amalgamation has been carried out on the basis of Amalgamation in the nature of purchase.

Answer

Balance Sheet of C Ltd. as at 1st April, 2012

Particulars	Note No.	(₹ in lakhs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1200
(b) Reserves and Surplus	2	1750
(2) Non-Current Liabilities		
Long-term borrowings	3	60
(3) Current Liabilities		
Trade payables	9	610
Total		3620
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
i. Tangible assets	4	1550

ii. Intangible assets	5	20
(b) Non-current investments	6	200
(c) Other non-current assets	7	100
(2) Current assets		
(a) Stock		600
(b) Trade receivables	8	650
(c) Cash and cash equivalents		500
Total		3620

Notes to Accounts

		(₹ in lakhs)	(₹ in lakhs)
1.	Share Capital		
	Equity share capital (W.N.2)		
	70,00,000 Equity shares of ₹ 10 each	700	
	5,00,000 Preference shares of ₹ 100 each	500	
	(all the above shares are allotted as fully paid-up pursuant to contracts without payment being received in cash)		1200
2.	Reserves and surplus		
	Securities Premium Account	1,650	
	Investment Allowance Reserve	100	1750
3.	Long-term borrowings		
	15% Debentures		60
4.	Tangible assets		
	Land and Building	950	
	Plant and Machinery	600	1550
5.	Intangible assets		
	Goodwill [W.N. 2]		20
6.	Non-current Investments		
	Investments		200
7.	Other non-current assets		
	Amalgamation Adjustment Account		100
8.	Trade receivables		
	Sundry Debtors	550	

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9.	Bills receivable	100	650
	Trade payables		
	Sundry creditors	390	
	Acceptances	<u>220</u>	610

Working Notes:

		(₹ in lakhs)	
		A Ltd.	B Ltd.
(1)	Computation of Purchase consideration		
	(a) Preference shareholders:		
	$\frac{₹ 3,00,00,000}{₹ 100} \div \frac{₹}{₹}$ i.e. 3,00,000 shares' Rs. 150 each	450	
	$\frac{₹ 2,00,00,000}{₹ 100} \div \frac{₹}{₹}$ i.e. 2,00,000 shares' Rs. 150 each		300
	(b) Equity shareholders:		
	$\frac{₹ 8,00,00,000}{₹ 100} \div \frac{₹}{₹} \times \frac{5}{₹}$ i.e. 40,00,000 shares' Rs. 30 each	1,200	
	$\frac{₹ 7,50,00,000}{₹ 100} \div \frac{₹}{₹} \times \frac{4}{₹}$ i.e. 30,00,000 shares' Rs. 30 each		<u>900</u>
	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
	Stock	350	250
	Sundry Debtors	250	300
	Bills receivable	50	50
	Cash and bank	<u>300</u>	<u>200</u>
		2,000	1,500
	Less: Liabilities taken over:		
	Debentures	40	20
	Sundry Creditors	270	120
	Bills payable	<u>150</u>	<u>70</u>

			(460)		(210)
	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>

Question 5

The following are the summarized Balance Sheets of Big Ltd. and Small Ltd. for the year ending on 31st March, 2012: (₹ in crores)

	Big Ltd.	Small Ltd.
Equity share capital – in equity shares of ₹ 10 each	50	40
Preference share capital – in 10% preference shares of ₹ 100 each	-	60
Reserves and Surplus	<u>200</u>	<u>150</u>
	250	250
Loans – Secured	<u>100</u>	<u>100</u>
Total funds	<u>350</u>	<u>350</u>
Applied for: Fixed assets at cost less depreciation	150	150
Current assets	<u>200</u>	<u>200</u>
	<u>350</u>	<u>350</u>

The present worth of fixed assets of Big Ltd. is ₹ 200 crores and that of Small Ltd. is ₹ 429 crores. Goodwill of Big Ltd. is ₹ 40 crores and of Small Ltd. is 75 crores.

Small Ltd. absorbs Big Ltd. by issuing equity shares at par in such a way that intrinsic net worth is maintained.

Goodwill account is not to appear in the books. Fixed assets are to appear at old figures.

- Show the Balance Sheet after absorption.
- Draft a statement of valuation of shares on intrinsic value basis and prove the accuracy of your workings.

Answer

(a)

Small Ltd.
Balance Sheet as at 1st April, 2012

Particulars	Note No.	(₹ in crores)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	125
(b) Reserves and Surplus	2	375

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(2) Non-Current Liabilities			
Long-term borrowings	3	200	
Total		700	
II. Assets			
(1) Non-current assets			
(a) Fixed assets			
Tangible assets	4	300	
(2) Current assets	5	400	
Total		700	

Notes to Accounts

		(₹ in Crores)	(₹ in Crores)
1.	Share Capital		
	6.5 crores equity shares of ₹ 10 each (of the above shares, 2.5 crores equity shares are allotted as fully paid-up for consideration other than cash)	65	
	60 lakhs 10% Preference shares of ₹ 100 each	<u>60</u>	125
2.	Reserves and surplus		
	As per last Balance Sheet	150	
	Capital Reserve	<u>225</u>	375
3.	Long Term Borrowings		
	Secured Loans:		
	As per last Balance Sheet	100	
	Taken over on absorption of Big Ltd.	<u>100</u>	200
4.	Tangible Assets		
	As per last Balance Sheet	150	
	Taken over on absorption of Big Ltd.	<u>150</u>	300
5.	Current assets		
	As per last Balance Sheet	200	
	Taken over on absorption of Big Ltd.	<u>200</u>	400

(b) Valuation of shares on intrinsic value basis

(i)	Big Ltd. (₹ in crores)	Small Ltd. (₹ in crores)
Equity share capital	50	40

Reserves and Surplus	<u>200</u>	<u>150</u>
	250	190
Goodwill agreed upon	40	75
Increase in the value of fixed assets (Present worth less book value)	<u>50</u>	<u>279</u>
	<u>340</u>	<u>544</u>

(ii)	Big Ltd.	Small Ltd.
Number of Equity shares	5 crores	4 crores
Intrinsic value per equity share	₹ 68	₹ 136
(iii) Ratio of intrinsic value of shares in the two companies	1 : 2	

Since the shares are to be issued at par, the number of equity shares of ₹ 10 each to be issued to maintain the intrinsic net worth = 5 crores / 2 = 2.5 crores

(iv) Statement to prove the accuracy of workings

		(₹ in crores)	
(1)	Equity share capital (after absorption)		65
	Reserves and Surplus (after absorption)		<u>375</u>
			440
	Add: Unrecorded value of goodwill ₹ (40 + 75)		115
	Add: Unrecorded incremental value of fixed assets ₹ (50+279)		<u>329</u>
			<u>884</u>
(2)	Number of equity shares	6.5 crores	
(3)	Intrinsic value of an equity share (884/6.5)	₹ 136	

Working Note:

Calculation of Capital Reserve on Absorption

	(₹ in crores)
Fixed Assets taken over	150
Net current assets taken over	<u>200</u>
	350
Less: Secured loans taken over	<u>(100)</u>
Net Assets taken over	250
Less: Purchase consideration	<u>(25)</u>
Capital Reserve	<u>225</u>

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Question 6

Given below is the summarized Balance Sheet of H Ltd. as on 31.3.2011:

(₹ in lakhs)

Equity share capital (in equity shares of ₹ 10 each)	4.00	Block assets less depreciation to date	6.00
10% preference share capital	3.00	Stock and debtors	5.30
General reserve	1.00	Cash and bank	0.70
Profit and loss account	1.00		
Creditors	<u>3.00</u>		
	<u>12.00</u>		<u>12.00</u>

M Ltd. another existing company holds 25% of equity share capital of H Ltd. purchased at ₹ 10 per share.

It was agreed that M Ltd. should take over the entire undertaking of H Ltd. on 30.9.2011 on which date the position of current assets (except cash and bank balances) and creditors was as follows:

Stock and debtors	₹ 4 lakhs
Creditors	₹ 2 lakhs

Profits earned for half year ended 30.09.2011 by H Ltd. was ₹ 70,500 after charging depreciation of ₹ 32,500 on block assets. H Ltd. declared 10% dividend for 2010-11 on 30.08.2011 and the same was paid within a week.

Goodwill of H Ltd. was valued at ₹ 80,000 and block assets were valued at 10% over their book value as on 31.3.2011 for purposes of take over. Preference shareholders of H Ltd. will be allotted 10% preference shares of ₹ 10 each by M Ltd. Equity shareholders of H Ltd. will receive requisite number of equity shares of ₹ 10 each from M Ltd. valued at ₹ 10 per share.

- Compute the purchase consideration.
- Explain, how the capital reserve or goodwill, if any, will appear in the Balance Sheet of M Ltd. after absorption.

Answer

(a) Calculation of Purchase Consideration (for net assets of H Ltd. taken over)

Assets taken over:	₹
Goodwill as agreed	80,000
Block Assets at 10% over their book value as on 31.3.2011 (agreed value for purposes of take over)	6,60,000
Stock and Debtors	4,00,000
Cash and Bank (See Working Note)	<u>1,33,000</u>

	12,73,000
Less: Liabilities taken over:	
Creditors	<u>(2,00,000)</u>
	<u>10,73,000</u>
Calculation of Shares Allotted:	₹
Net Assets taken over	10,73,000
Less: Allotment of 10% preference shares to preference shareholders of H Ltd.	<u>(3,00,000)</u>
	7,73,000
Less: Belonging to M Ltd. (1/4 of ₹ 7,73,000)	<u>(1,93,250)</u>
Payable to other equity shareholders	<u>5,79,750</u>

Number of equity shares of ₹ 10 each to be issued (valued at ₹ 10 each) = 57,975

Calculation of Capital Reserve:	₹	₹
Net Assets taken over		10,73,000
Less: Preference shares to be allotted	(3,00,000)	
Equity shares to be allotted	(5,79,750)	
Cost of investments	<u>(1,00,000)</u>	<u>(9,79,750)</u>
Capital Reserve		<u>93,250</u>
Alternatively, Capital Reserve may be computed as follows:		
Value of investments in H Ltd.		1,93,250
Less: Cost of investments		<u>(1,00,000)</u>
		<u>93,250</u>

(b) Balance Sheet of M Ltd. as at 30th September, 2011 (Extract)

Particulars	Note No.	₹
I. Equity and Liabilities		
(1) Shareholder's Funds		
Reserves and Surplus	1	13,250

Notes to accounts

1. Reserves and Surplus		₹
Capital Reserve	93,250	
Less: Goodwill	<u>(80,000)</u>	13,250

Working Note:**Ascertainment of Cash and Bank Balances as on 30th September, 2011****Balance Sheet as at 30th September, 2011**

Particulars	Note No.	₹
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	7,00,000
(b) Reserves and Surplus	2	2,00,500
(2) Current Liabilities		
Trade Payables	3	2,00,000
Total		11,00,500
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	4	5,67,500
(2) Current assets		
(a) Inventories & Trade receivables	5	4,00,000
(b) Cash and cash equivalents (Bal. fig.)		1,33,000
Total		11,00,500

Notes to Accounts

		₹	₹
1.	Share Capital		
	Equity Share Capital	4,00,000	
	10% Preference Share Capital	<u>3,00,000</u>	7,00,000
2.	Reserves and surplus		
	General Reserve		1,00,000
	Profit and Loss Account:		
	Balance brought forward	1,00,000	
	Add: Profit for the first half	<u>70,500</u>	
	Less: Dividend on preference share capital paid	30,000	
	Dividend on equity share capital paid	<u>40,000</u>	
		<u>(70,000)</u>	1,00,500
			2,00,500
3.	Trade Payables		
	Creditors		2,00,000
4.	Tangible Assets		
	Block Assets	6,00,000	

5.	Less: Depreciation	(32,500)	5,67,500
	Inventories & Trade receivables		
	Stock and Debtors		4,00,000

Question 7

AB Ltd. and MB Ltd. decide to amalgamate and to form a new company AM Ltd. The following are their summarised balance sheets as at 31.3.2012: (₹)

Liabilities	AB Ltd.	MB Ltd.	Assets	AB Ltd.	MB Ltd.
Share Capital (₹ 100) each	10,00,000	6,00,000	Fixed Assets	7,50,000	2,00,000
General Reserve	1,00,000	50,000	Investments:		
Investment Allowance			1,500 Shares in MB	3,50,000	-
Reserve	40,000	30,000	4,000 Shares in AB	-	5,00,000
12% Debentures (₹ 100 each)	3,00,000	1,00,000	Current Assets	4,00,000	1,00,000
Sundry Creditors	60,000	20,000			
	<u>15,00,000</u>	<u>8,00,000</u>		<u>15,00,000</u>	<u>8,00,000</u>

Calculate the amount of purchase consideration for AB Ltd. and MB Ltd. and draw up the balance sheet of AM Ltd. after considering the following:

- Assume amalgamation is in the nature of purchase.
- Fixed assets of AB Ltd. are to be reduced by ₹ 50,000 and that of MB Ltd. are to be taken at ₹ 3,00,000.
- 12% debentureholders of AB Ltd. and MB Ltd. are discharged by AM Ltd. by issuing such number of its 15% debentures of ₹ 100 each so as to maintain the same amount of interest.
- Shares of AM Ltd. are of ₹ 100 each.

Also show, how the investment allowance reserve will be treated in the Financial Statement assuming the Reserve will be maintained for 3 years.

Answer**Calculation of Purchase consideration**

- Value of Net Assets of AB Ltd. and MB Ltd. as on 31st March, 2012

		AB Ltd. (₹)		MB Ltd. (₹)
Assets taken over:				
Fixed Assets	7,00,000		3,00,000	

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Current Assets	<u>4,00,000</u>	11,00,000	<u>1,00,000</u>	4,00,000
Less: Liabilities taken over:				
Debentures	2,40,000*		80,000**	
Sundry Creditors	<u>60,000</u>	<u>(3,00,000)</u>	<u>20,000</u>	<u>(1,00,000)</u>
		<u>8,00,000</u>		<u>3,00,000</u>

$$* 3,00,000 \times \frac{12}{100} \times \frac{100}{15} = ₹ 2,40,000$$

$$** 1,00,000 \times \frac{12}{100} \times \frac{100}{15} = ₹ 80,000$$

(ii) Value of Shares of AB Ltd. and MB Ltd.

The value of shares of AB Ltd. is ₹ 8,00,000 plus 1/4 of the value of the shares of MB Ltd.

Similarly, the value of shares of MB Ltd. is ₹ 3,00,000 plus 2/5 of the value of shares of AB Ltd.

Let 'a' denote the value of shares of AB Ltd. and 'm' denote the value of shares of MB Ltd. then

$$a = 8,00,000 + 1/4 m ; \text{ and}$$

$$m = 3,00,000 + 2/5 a.$$

Substituting the value of m,

$$a = 8,00,000 + 1/4 (3,00,000 + 2/5 a)$$

$$a = 8,00,000 + 75,000 + 1/10 a$$

$$9/10 a = 8,75,000$$

$$a = 9,72,222$$

$$m = 3,00,000 + 2/5 (9,72,222)$$

$$m = 6,88,889$$

(iii) Amount of Purchase Consideration

	AB Ltd. ₹	MB Ltd. ₹
Total value of shares (as determined above)	9,72,222	6,88,889
Less: Internal investments:		
2/5 for shares held by MB Ltd.	(3,88,889)	
1/4 for shares held by AB Ltd.		<u>(1,72,222)</u>
Amount due to outsiders	<u>5,83,333</u>	<u>5,16,667</u>

Purchase Consideration will be satisfied by AM Ltd. as follows:

	<i>AB Ltd.</i> ₹	<i>MB Ltd.</i> ₹
In shares (of ₹ 100 each)	5,83,300	5,16,600
In cash	33	67

(iv) Net Amount of Goodwill/Capital Reserve

	₹	₹
Total Purchase Consideration		
AB Ltd.	5,83,333	
MB Ltd.	<u>5,16,667</u>	11,00,000
Less: Net Assets taken over		
AB Ltd.	8,00,000	
MB Ltd.	<u>3,00,000</u>	<u>(11,00,000)</u>
		<u>Nil</u>

(Alternatively, the calculations may be made separately for both the companies)

**Balance Sheet of AM Ltd.
as at 31st March, 2012**

Particulars	Note No.	Amount (₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	10,99,900
(b) Reserves and Surplus	2	70,000
(2) Non-Current Liabilities		
Long-term borrowings	3	3,20,000
(3) Current Liabilities		
Trade payables		80,000
Total		15,69,900
II. Assets		
(1) Non-current assets		
(a) Fixed assets		10,00,000
(b) Other non-current assets	4	70,000
(2) Current assets	5	4,99,900
Total		15,69,900

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Notes to Accounts

		(₹)	(₹)
1.	Share Capital 10,999 shares of ₹ 100 each (All the above shares are allotted as fully paid-up for consideration other than cash)		10,99,900
2.	Reserves and surplus Investment Allowance Reserve		70,000
3.	Long Term Borrowings 15% Debentures		3,20,000
4.	Other non-current assets Amalgamation Adjustment Account		70,000
5.	Current assets Current assets	5,00,000	
	Less: Purchase consideration paid in cash ₹ (33+67)	<u>(100)</u>	4,99,900

Question 8

The summarised Balance Sheets of R Ltd. and P Ltd. for the year ending on 31.3.2012 are as under:

	R Ltd. ₹	P Ltd. ₹		R Ltd. ₹	P Ltd. ₹
Equity share Capital (in shares of ₹ 10 each)	24,00,000	12,00,000	Fixed Assets	55,00,000	27,00,000
8% Preference Share Capital (in shares of ₹ 10 each)	8,00,000	—	Current Assets	25,00,000	23,00,000
10% Preference Share Capital (in shares of ₹ 10 each)	—	4,00,000			
Reserves	30,00,000	24,00,000			
Current Liabilities	<u>18,00,000</u>	<u>10,00,000</u>			
	<u>80,00,000</u>	<u>50,00,000</u>		<u>80,00,000</u>	<u>50,00,000</u>

The following information is provided:

			R Ltd. ₹	P Ltd. ₹
(1)	(a)	Profit before tax	10,64,000	4,80,000
	(b)	Taxation	4,00,000	2,00,000
	(c)	Preference dividend	64,000	40,000
	(d)	Equity dividend	2,88,000	1,92,000

(2) The equity shares of both the companies are quoted in the market. Both the companies are carrying on similar manufacturing operations.

(3) R Ltd. proposes to absorb P Ltd. as on 31.3.2012. The terms of absorption are as under:

(a) Preference shareholders of P Ltd. will receive 8% preference shares of R Ltd. sufficient to increase the income of preference shareholders of P Ltd. by 10%.

(b) The equity shareholders of P Ltd. will receive equity shares of R Ltd. on the following basis:

(i) The equity shares of P Ltd. will be valued by applying to the earnings per share of P Ltd. 75% of price earnings ratio of R Ltd. based on the results of 2011-2012 of both the companies.

(ii) The market price of equity shares of R Ltd. is ₹ 40 per share.

(iii) The number of shares to be issued to the equity shareholders of P Ltd. will be based on the above market value.

(iv) In addition to equity shares, 8% preference shares of R Ltd. will be issued to the equity shareholders of P Ltd. to make up for the loss in income arising from the above exchange of shares based on the dividends for the year 2011-2012.

(4) The assets and liabilities of P Ltd. as on 31.3.2012 are revalued by professional valuer as under:

	Increased by ₹	Decreased by ₹
Fixed Assets	1,00,000	—
Current Assets	—	2,00,000
Current Liabilities	—	40,000

(5) For the next two years, no increase in the rate of equity dividend is expected.

You are required to:

(i) Set out in detail the purchase consideration.

(ii) Give the Balance Sheet as on 31.3.2012 after absorption.

Note: Journal entries are not required.

Answer**(i) Computation of Purchase Consideration**

		₹
(a)	<i>Preference Shareholders</i>	
	Current income of preference shareholders of P Ltd.	40,000
	Add: 10% increase thereof	<u>4,000</u>
		<u>44,000</u>
	Preference shares to be issued	
	$= 44,000 \times \frac{100}{8}$	5,50,000
(b)	<i>Equity Shareholders</i>	
	(1) <i>Issue of Equity Shares</i>	
	Profit before tax	10,64,000
	Less: Tax	<u>(4,00,000)</u>
		6,64,000
	Less: Preference dividend	<u>(64,000)</u>
	Profit available for equity shareholders	<u>6,00,000</u>

$$\text{Earnings per share (EPS)} = \frac{6,00,000}{2,40,000} = ₹ 2.50$$

$$\text{Price earnings ratio (P/E)} = \frac{40}{2.50} = ₹ 16$$

EPS of P Ltd.

	₹
Profit before tax	4,80,000
Less: Tax	<u>(2,00,000)</u>
Profit after tax	2,80,000
Less: Preference dividend	<u>(40,000)</u>
Profit available for equity shareholders	<u>2,40,000</u>

$$\text{EPS} = \frac{2,40,000}{1,20,000} = ₹ 2$$

Valuation of equity shares of P Ltd.

$$= 1,20,000 \text{ shares} \times (₹ 2 \times 16 \times 0.75 \text{ i.e. } ₹ 24) = ₹ 28,80,000$$

$$\text{Number of equity shares to be issued} = \frac{28,80,000}{40} = 72,000$$

	₹
Equity Share Capital	7,20,000
Securities Premium	<u>21,60,000</u>
	<u>28,80,000</u>
(2) <i>Issue of Preference Shares</i>	₹
Current equity dividend	1,92,000
Less: Expected equity dividend from R Ltd. (₹ 7,20,000 × 2,88,000/24,00,000)	<u>(86,400)</u>
Loss in income	<u>1,05,600</u>
8% Preference Shares to be issued = $\frac{1,05,600}{0.08} = ₹ 13,20,000$	
Total Purchase Consideration:	₹
Preference shares to be issued	5,50,000
	<u>13,20,000</u>
Equity shares to be issued (at premium)	<u>28,80,000</u>
	<u>47,50,000</u>

(ii)

R Ltd.

**Balance Sheet as at 31st March, 2012
(after absorption)**

Particulars	Note No.	Amount (₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	57,90,000
(b) Reserves and Surplus	2	51,60,000
(2) Current Liabilities	3	27,60,000
Total		<u>1,37,10,000</u>
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
i. Tangible assets	4	83,00,000
ii. Intangible assets	5	8,10,000
(2) Current assets	6	46,00,000
Total		<u>1,37,10,000</u>

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Notes to Accounts

		(₹)	(₹)
1.	Share Capital		
	3,12,000 Equity Shares of ₹ 10 each (of the above shares, 72,000 Equity shares are allotted as fully paid up for consideration other than cash)	31,20,000	
	2,67,000 8% Preference Shares of ₹ 10 each (of the above, 1,87,000 are allotted as fully paid up for consideration other than cash)	<u>26,70,000</u>	57,90,000
2.	Reserves and surplus		
	Reserves (As per last Balance Sheet)	30,00,000	
	Securities Premium	<u>21,60,000</u>	51,60,000
3.	Current Liabilities		
	As per last balance sheet	18,00,000	
	Taken over on absorption of P Ltd. ₹ (10,00,000-40,000)	<u>9,60,000</u>	27,60,000
4.	Tangible Assets		
	As per last Balance Sheet	55,00,000	
	Taken over on absorption of P Ltd.	<u>28,00,000</u>	83,00,000
5.	Intangible assets		
	Goodwill (See Working Note)		8,10,000
6.	Current Assets		
	As per last Balance Sheet	25,00,000	
	Taken over on absorption of P Ltd. ₹ (23,00,000-2,00,000)	<u>21,00,000</u>	46,00,000

Working Note:

Calculation of Goodwill on Absorption

		₹
Purchase consideration		47,50,000
Fixed assets taken over	28,00,000	
Current assets taken over	<u>21,00,000</u>	
	49,00,000	
Less: Current liabilities	<u>(9,60,000)</u>	
Net assets taken over		<u>(39,40,000)</u>
Goodwill		<u>8,10,000</u>

Question 9

The summarized Balance Sheets of O Ltd. and P Ltd. as on 31st March, 2012 are as under:

(₹ in lakhs)

Liabilities	O	P	Assets	O	P
Equity Shares of ₹ 10 each	25.00	50.00	Fixed Assets	110.00	50.00
Reserves	131.00	29.25	Investments	16.25	25.00
12% Debentures	11.00	5.50	Current Assets	40.25	3.25
Creditors	8.00	2.75	Miscellaneous Expenditure	8.50	9.25
	<u>175.00</u>	<u>87.50</u>		<u>175.00</u>	<u>87.50</u>

Miscellaneous expenditure consist of item other than preliminary expenses.

Investments of O Ltd. represent 1,25,000 shares of P Ltd. Investments of P Ltd. are considered worth ₹ 30 lakhs.

P Ltd. is taken over by O Ltd. on the basis of the intrinsic value of shares in their respective books of account.

Prepare a statement showing the number of shares to be allotted by O Ltd. to P Ltd. and the Balance Sheet of O Ltd. after absorption of P Ltd.

Answer

**Balance sheet of O Ltd.
(after absorption)**

Particulars	Note No.	(₹ in lakhs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	34.375
(b) Reserves and Surplus	2	180.375
(2) Non-Current Liabilities		
Long-term borrowings	3	16.500
(3) Current Liabilities		
Trade payables	4	10.750
Total		242.00
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	5	160.00
(b) Non-current Investments		30.00

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(c).Other non-current assets	6	8.50
(2) Current assets	7	43.50
Total		242.00

Notes to Accounts

		(₹)	(₹)
1.	Share Capital 3,43,750 Equity Shares of ₹ 10 each (Of the above shares, 93,750 equity shares are allotted as fully paid-up for consideration other than cash)		34.375
2.	Reserves and surplus As per last Balance Sheet Capital Reserve Securities Premium	131.000 2.500 <u>46.875</u>	180.375
3.	Long Term Borrowings 12% Debentures Add: Taken over	11.000 <u>5.500</u>	16.500
4.	Trade payables Creditors Add: Taken over	8.000 <u>2.750</u>	<u>10.750</u>
5.	Tangible assets Fixed Assets Add: Taken over	110.000 <u>50.000</u>	160.000
6.	Other non-current assets Miscellaneous Expenditure *		8.500
7.	Current assets Current Assets Add: Taken over	40.250 <u>3.250</u>	43.500

Working Notes:

(a) (i) Calculation of Net Assets	(₹ in lakhs)	
	O Ltd.	P Ltd.
Fixed Assets	110.00	50.00
Investments	18.75*	30.00

* It has been assumed that Miscellaneous Expenditure will be written off over a period more than 1 year.

Current Assets	<u>40.25</u>	<u>3.25</u>
Total (A)	<u>169.00</u>	<u>83.25</u>
12% Debentures	11.00	5.50
Creditors	<u>8.00</u>	<u>2.75</u>
Total (B)	<u>19.00</u>	<u>8.25</u>
Net Assets (A – B)	<u>150.00</u>	<u>75.00</u>
	<i>O Ltd.</i>	<i>P Ltd.</i>
(ii) Number of equity shares	2.50 lakhs	5.00 lakhs
Intrinsic Value	₹ 60.00	₹ 15.00
* 1.25 lakhs shares @ ₹ 15		

(b) Calculation of Shares Allotted (₹ in lakhs)

Net assets taken over	75.00
Less: Belonging to O Ltd. $\frac{1,25,000}{5,00,000} \times 75 \text{ lakhs} = 23.75$	(23.75)
Payable to other equity shareholders	<u>56.25</u>
Number of equity shares of ₹ 10 each to be issued = $\frac{56,25,000}{60}$	
= 93,750 shares (valued at ₹ 60 each)	
Credit to share capital	₹ 9,37,500
Credit to securities premium	₹ 46,87,500

Question 10

A Ltd. agreed to take over B Ltd. as on 1st October, 2011. No Balance Sheet of B was prepared on that date:

Summarised Balance Sheets of A and B as at 31st March, 2011 were as follows:

	A ₹	B ₹		A ₹	B ₹
Share Capital: Equity shares of ₹ 10 each fully paid up	15,00,000	10,00,000	Fixed Assets	12,50,000	8,75,000
Reserves and Surplus:			Current Assets:		
Reserve	4,15,000	2,56,000	Stock	2,37,500	1,87,500
Profit and Loss	1,87,500	1,50,000	Debtors	3,90,000	2,56,000
			Bank	2,93,750	1,50,000
			Miscellaneous		

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Creditors	93,750	75,000	Expenditure: Preliminary Expenses	25,000	12,500
	<u>21,96,250</u>	<u>14,81,000</u>		<u>21,96,250</u>	<u>14,81,000</u>

Additional information available:

- For the six months period from 1st April, 2011, A made a profit of ₹ 4,20,000 after writing off depreciation at 10% per annum on its fixed assets.
- For the same period, B made a net profit of ₹ 2,04,000 after writing off depreciation at 10% p.a. on its fixed assets.
- Both the companies paid on 1st August, 2011, equity dividends of 15%. Tax at 10% on such payments was also paid by each of them.
- Goodwill of B was valued at ₹ 1,20,000 on the date of take-over; stock of B, subject to an abnormal item of ₹ 7,500 to be fully written off, would be appreciated by 25% for purpose of take-over.
- A to issue to B's shareholders fully paid equity shares of ₹ 10 each, on the basis of the comparative intrinsic values of the shares on the take-over date.

Draft the Balance Sheet of A after absorption of B. All workings are to form part of your answer.

Answer

Balance Sheet of A Ltd. (after absorption of B Ltd.)

Particulars	Note No.	₹
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	25,60,000
(b) Reserves and Surplus	2	12,80,000
(2) Current Liabilities		
Trade payables		1,68,750
Total		40,08,750
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
i. Tangible assets	3	20,18,750
ii. Intangible assets	4	1,20,000

(2) Current assets		
(a) Inventories (₹ 2,37,500 + ₹ 2,25,000)		4,62,500
(b) Trade receivables (₹ 3,90,000 + ₹ 2,56,000)		6,46,000
(c) Cash and cash equivalents (₹ 5,28,750 + ₹ 2,32,750)		7,61,500
Total		40,08,750

Notes to Accounts

		₹	₹
1.	Share Capital		
	2,56,000 Equity Shares of ₹ 10 each fully paid		25,60,000
	(1,06,000 shares allotted as fully paid without payment being received in cash)		
2.	Reserves and surplus		
	Securities Premium	5,30,000	
	Reserves	4,15,000	
	Profit and Loss Account ₹ 3,60,000		
	Less: Preliminary expenses (₹ 25,000*)	<u>3,35,000</u>	12,80,000
3.	Tangible Assets		
	Other Fixed Assets (₹ 12,50,000 + ₹ 8,75,000)	21,25,000	
	Less: Depreciation	<u>(1,06,250)</u>	20,18,750
4.	Intangible assets		
	Goodwill		1,20,000

Working Notes:

(1) Bank Balance on 1.10.2011

	A Ltd. ₹	B Ltd. ₹
Bank Balance as on 31.3.2011	2,93,750	1,50,000
Add: Net Profit	4,20,000	2,04,000
Depreciation	<u>62,500</u>	<u>43,750</u>
	7,76,250	3,97,750
Less: Dividend	<u>(2,25,000)</u>	<u>(1,50,000)</u>

* As per para 56 of AS 26, 'Intangible Assets', preliminary expenses are to be recognized as expenses as and when they are incurred.

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	5,51,250	2,47,750
Less: Dividend Tax	<u>(22,500)</u>	<u>(15,000)</u>
Bank Balance as on 1.10.2011	<u>5,28,750</u>	<u>2,32,750</u>

(2) Profit and Loss Account as on 1.10.2011

	A Ltd. ₹	B Ltd. ₹
Balance as on 31.3.2011	1,87,500	1,50,000
Add: 6 months' profit	<u>4,20,000</u>	<u>2,04,000</u>
	6,07,500	3,54,000
Less: Dividend	(2,25,000)	(1,50,000)
Dividend tax	<u>(22,500)</u>	<u>(15,000)</u>
	<u>3,60,000</u>	<u>1,89,000</u>

(3) **Balance Sheets of A Ltd. and B Ltd.
as on 1st October, 2011 (before absorption)**

Particulars	Note no.	A Ltd. (₹)	B Ltd. (₹)
I. Equity and Liabilities			
(1) Shareholder's Funds			
(a) Share Capital		15,00,000	10,00,000
(b) Reserves and Surplus	1	7,50,000	4,32,500
(2) Current Liabilities			
Trade payables		93,750	75,000
Total		23,43,750	15,07,500
II. Assets			
(1) Non-current assets			
(a) Fixed assets			
Tangible assets	2	11,87,500	8,31,250
(2) Current assets			
(a) Inventories*		2,37,500	1,87,500
(b) Trade receivables*		3,90,000	2,56,000
(c) Cash and cash equivalents		5,28,750	2,32,750
Total		23,43,750	15,07,500

*It is assumed that these amounts as on 1st October, 2011 are same in the absence of any other information.

Notes to Accounts

		A Ltd.		B Ltd.	
		(₹)	(₹)	(₹)	(₹)
1.	Reserves and surplus				
	Reserves	4,15,000		2,56,000	
	Profit and Loss less preliminary expenses	<u>3,35,000</u>	7,50,000	<u>1,76,500</u>	4,32,500
2.	Tangible Assets				
	Fixed Assets	12,50,000		8,75,000	
	Less: Depreciation	<u>(62,500)</u>		<u>(43,750)</u>	
	Net Fixed Assets		11,87,500		8,31,250

(4) Purchase consideration

	A Ltd. ₹	B Ltd. ₹
Goodwill	–	1,20,000
Fixed Assets	11,87,500	8,31,250
Stock	2,37,500	2,25,000
Debtors	3,90,000	2,56,000
Bank Balance	<u>5,28,750</u>	<u>2,32,750</u>
	23,43,750	16,65,000
Less: Creditors	<u>(93,750)</u>	<u>(75,000)</u>
Net Assets	<u>22,50,000</u>	<u>15,90,000</u>
Number of Shares	1,50,000	1,00,000
Intrinsic value	15.00	15.90

Purchase consideration ₹ 15,90,000 in the form of Share capital ₹ 10,60,000 and securities premium ₹ 5,30,000.

Question 11

The following are the summarized Balance Sheets of A Ltd. and B Ltd. as on 31st December, 2011:

Liabilities	A Ltd. ₹	B Ltd. ₹	Assets	A Ltd. ₹	B Ltd. ₹
Share Capital			Fixed Assets	7,00,000	2,50,000

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Equity Shares of ₹ 10 each	6,00,000	3,00,000	Investment:		
10% Pref. Shares of ₹ 100 each	2,00,000	1,00,000	6,000 Shares of B Ltd.	80,000	-
Reserves and Surplus	3,00,000	2,00,000	5,000 Shares of A Ltd.	-	80,000
Secured Loans:			Current Assets:		
12% Debentures	2,00,000	1,50,000	Stock	2,40,000	3,20,000
Current Liabilities:			Debtors	3,60,000	1,90,000
Sundry Creditors	2,20,000	1,25,000	Bills Receivable	60,000	20,000
Bills Payable	<u>30,000</u>	<u>25,000</u>	Cash at Bank	<u>1,10,000</u>	<u>40,000</u>
	<u>15,50,000</u>	<u>9,00,000</u>		<u>15,50,000</u>	<u>9,00,000</u>

Fixed Assets of both the companies are to be revalued at 15% above book value. Stock in Trade and Debtors are taken over at 5% lesser than their book value. Both the companies are to pay 10% Equity dividend, Preference dividend having been already paid.

After the above transactions are given effect to, A Ltd. will absorb B Ltd. on the following terms:

- 8 Equity Shares of ₹ 10 each will be issued by A Ltd. at par against 6 shares of B Ltd.
- 10% Preference Shareholders of B Ltd. will be paid at 10% discount by issue of 10% Preference Shares of ₹ 100 each at par in A Ltd.
- 12% Debentureholders of B Ltd. are to be paid at 8% premium by 12% Debentures in A Ltd. issued at a discount of 10%.
- ₹ 30,000 is to be paid by A Ltd. to B Ltd. for Liquidation expenses. Sundry Creditors of B Ltd. include ₹ 10,000 due to A Ltd.

Prepare:

- Absorption entries in the books of A Ltd.
- Statement of consideration payable by A Ltd.

Answer

(a) Absorption Entries in the Books of A Ltd.

		Dr. ₹	Cr. ₹
Fixed Assets	Dr.	1,05,000	
To Revaluation Reserve			1,05,000
(Revaluation of fixed assets at 15% above book value)			

Bank Account	Dr.	6,000	
To Reserves and Surplus (Dividend received from B Ltd. on 6,000 shares)			6,000
Reserve and Surplus	Dr.	60,000	
To Equity Dividend (Declaration of equity dividend @ 10%)			60,000
Equity Dividend	Dr.	60,000	
To Bank Account (Payment of equity dividend)			60,000
Business Purchase Account	Dr.	3,60,000	
To Liquidator of B Ltd. (Consideration payable for the business taken over from B Ltd.)			3,60,000
Fixed Assets (115% of ₹ 2,50,000)	Dr.	2,87,500	
Stock (95% of ₹ 3,20,000)	Dr.	3,04,000	
Debtors	Dr.	1,90,000	
Bills Receivable	Dr.	20,000	
Cash at Bank	Dr.	15,000	
(₹ 40,000 – ₹ 30,000 dividend paid + ₹ 5,000 dividend received)			
To Provision for Bad Debts (5% of ₹ 1,90,000)			9,500
To Sundry Creditors			1,25,000
To 12% Debentures in B Ltd.			1,62,000
To Bills Payable			25,000
To Business Purchase Account			3,90,000
To Investments in B Ltd.			80,000
To Capital Reserve (Balancing figure)			25,000
(Incorporation of various assets and liabilities taken over from B Ltd. at agreed values and cancellation of investment in B Ltd. account, profit being credited to capital reserve)			
Liquidator of B Ltd.	Dr.	3,60,000	
To Equity Share Capital			2,70,000
To 10% Preference Share Capital			90,000
Discharge of consideration for B Ltd.'s business)			

4.44 Financial Reporting

Capital Reserve To Bank Account (Payment of liquidation expenses)	Dr.	30,000	30,000
12% Debentures in B Ltd. (₹ 1,50,000 × 108%) Discount on Issue of Debentures To 12% Debentures (Allotment of 12% Debentures to debenture holders at a discount of 10% to discharge the liability on B Ltd. debentures)	Dr. Dr.	1,62,000 18,000	1,80,000
Sundry Creditors To Sundry Debtors (Cancellation of mutual owing)	Dr.	10,000	10,000

(b) Statement of Consideration payable by A Ltd.

For equity shares held by outsiders

Shares held by them 30,000 – 6,000 = 24,000

Shares to be allotted $\frac{24,000}{6} \times 8 = 32,000$

as 5,000 shares are already with B Ltd; i.e. A Ltd. will now issue only 27,000 shares of

₹ 10 each i.e. ₹ 2,70,000 (i).

For 10% preference shares, to be paid at 10% discount

₹ $\frac{1,00,000 \times 90}{100}$ ₹ 90,000 (ii)

Consideration amount [(i) + (ii)] ₹ 3,60,000

Note: It has been assumed that dividend on equity shares have been paid by both the companies.

Question 12

The following are the summarized Balance Sheets of RS Ltd. and XY Ltd. as on 31.3.2012:

₹ in '000

Liabilities	RS Ltd. ₹	XY Ltd. ₹	Assets	RS Ltd. ₹	XY Ltd. ₹
Share Capital: Equity Shares of ₹ 100 each fully paid up	2,000	1,000	Fixed Assets net of depreciation	2,700	850
Reserves and Surplus	800	–	Investments	700	–
			Sundry Debtors	400	150

10% Debentures	500	–	Cash and Bank	250	–
Loan from Financial Institutions	250	400	Profit and Loss Account	–	800
Bank Overdraft	–	100			
Sundry Creditors	300	300			
Proposed Dividend	<u>200</u>	<u>—</u>			
Total	<u>4,050</u>	<u>1,800</u>	Total	<u>4,050</u>	<u>1,800</u>

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

- (i) XY Ltd. will reduce its shares to ₹ 10 and then consolidate 10 such shares into one share of ₹ 100 each (New Share).
- (ii) Financial institutions agreed to waive 15% of the loan of XY Ltd.
- (iii) Shareholders of RS Ltd. will be given one new share of XY Ltd. in exchange of every share held in RS Ltd.
- (iv) RS Ltd. will cancel 20% holding of XY Ltd. Investments were held at ₹ 250 thousands.
- (v) After merger the proposed dividend of RS Ltd. will be paid to the shareholders of RS Ltd.
- (vi) Authorised Capital of XY Ltd. will be raised accordingly to carry out the scheme.
- (vii) Sundry creditors of XY Ltd. includes payable to RS Ltd. ₹ 1,00,000.

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

Answer

Journal Entries in the books of RS Ltd.

		Dr. ₹	(₹ '000) Cr. ₹
10% Debentures Account	Dr.	500	
Loan from Financial Institutions Account	Dr.	250	
Sundry Creditors Account	Dr.	300	
Proposed Dividend Account	Dr.	200	
Realisation Account	Dr.	2,800	
To Fixed Assets Account			2,700
To Investments Account			700

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To Sundry Debtors Account			400
To Cash and Bank Account			250
(Transfer of assets and liabilities to realisation account)			
Share Capital Account	Dr.	2,000	
Reserve and Surplus Account	Dr.	800	
To Equity Shareholders Account			2,800
(Transfer of share capital, reserve and surplus to shareholders account)			
Equity Shareholders Account	Dr.	250	
To Realisation Account			250
(Cancellation of 20% holding of XY Ltd. held as investments)			
Shares in XYZ Ltd.	Dr.	2,000	
To Realisation Account			2,000
(Issue of shares by XYZ Ltd. in the ratio of 1 : 1)			
Equity Shareholders Account	Dr.	550	
To Realisation Account			550
(Transfer of loss on realisation)			
Equity Shareholders Account	Dr.	2,000	
To Shares in XYZ Ltd.			2,000
(Distribution of Shares of XYZ Ltd. among the shareholders)			

Journal Entries in the books of XY Ltd.

	(₹ '000)	
	Dr. ₹	Cr. ₹
Equity Share Capital (Face value – ₹ 100) Account Dr.	1,000	
To Equity Share Capital (Face value – ₹ 10) Account		100
To Reconstruction Account		900
(Face value of equity shares of ₹ 100 each reduced to ₹ 10 each)		
Equity Share Capital (Face value – ₹ 10 each) A/c Dr.	100	
To Equity Share Capital Account		100
(Face value – ₹ 100 each)		
(Consolidation of 10,000 equity shares of ₹ 10 each to 1,000 equity shares of ₹ 100 each)		

Loan from Financial Institutions Account	Dr.	60	
To Reconstruction Account			60
(Waiver of 15% of loan by financial institutions)			
Reconstruction Account ₹ (900 + 60)	Dr.	960	
To Profit and Loss Account			800
To Capital Reserve			160
(Utilisation of Reconstruction account balance to write off the Profit and Loss Account)			
Proposed Dividend Account	Dr.	200	
To Bank Account			200
(Payment of Proposed dividend to shareholders of RS Ltd.)			
Fixed Assets Account	Dr.	2,700	
Other Investments Account	Dr.	450	
Sundry Debtors Account	Dr.	400	
Cash and Bank Account	Dr.	250	
To Reserves Account			570
To 10% Debentures Account			500
To Loan from Financial Institutions Account			250
To Sundry Creditors Account			300
To Proposed Dividend Account			200
To Business Purchase Account			1,980
(Incorporation of various assets and liabilities acquired from RS Ltd. after cancellation of investment held by RS Ltd. in XY Ltd., profit on acquisition credited to Reserves Account)			
Business Purchase Account	Dr.	1,980	
To Liquidator of RS Ltd.			1,980
(Consideration Payable on business acquired from RS Ltd.)			
Liquidator of RS Ltd.	Dr.	1,980	
To Equity Share Capital of XYZ Ltd.			1,980
(Discharge of purchase consideration in the form of equity shares of XYZ Ltd.)			
Sundry Creditors Account	Dr.	100	
To Sundry Debtors Account			100
(Cancellation of intercompany owings)			

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Balance Sheet of XYZ Ltd.
as on 31st March, 2012 (immediately after acquisition)

(₹ in 000's)

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	2,080
(b) Reserves and Surplus	2	730
(2) Non-Current Liabilities		
Long-term borrowings	3	1090
(3) Current Liabilities		
(a) Short term borrowings	4	50
(b) Trade payables		500
Total		4,450
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	5	3,550
(b) Non-current investments*		450
(2) Current assets		
Trade receivables		450
Total		4,450

Notes to Accounts

		(₹ in 000's)	(₹ in 000's)
1.	Share Capital		
	2,56,000 Equity Shares of ₹ 10 each fully paid		25,60,000
	(1,06,000 shares allotted as fully paid without payment being received in cash)		
2.	Reserves and surplus		
	Securities Premium	5,30,000	
	Reserves	4,15,000	

* Investments are assumed as non-current investments.

	Profit and Loss Account	3,60,000		
	Less: Preliminary expenses	<u>(25,000*)</u>	<u>3,35,000</u>	12,80,000
3.	Tangible Assets			
	Other Fixed Assets (₹ 12,50,000 + ₹ 8,75,000)		21,25,000	
	Less: Depreciation		<u>(1,06,250)</u>	20,18,750
4.	Intangible assets			
	Goodwill			1,20,000

Working Notes:

		₹
1.	Original Share Capital of XY Ltd. 10,000 Equity Shares of ₹ 100 each	10,00,000
	Share Capital of XY Ltd. after Reduction 10,000 Equity Shares of ₹ 10 each	1,00,000
2.	Share Capital of XY Ltd. after Reconsolidation 1,000 Equity Shares of ₹ 100 each	1,00,000
3.	Reduced value of holdings of RS Ltd. in XY Ltd. RS Ltd. was holding 20% of XY Ltd., that is, 2,000 Equity Shares of ₹ 100 each which has now reduced to 200 Equity Shares of ₹ 100 each	2,00,000 20,000
4.	Calculation of Purchase Consideration Equity Share Capital of RS Ltd. 20,000 Equity Shares of ₹ 100 each	20,00,000

Exchange Ratio = 1 : 1

No. of Equity Shares to be given 20,000
Less: No. of Equity Shares already held by RS Ltd. (200)
19,800

Purchase consideration

19,800 Equity Shares of ₹ 100 each 19,80,000

5.	Aggregate Reserves in the new company on acquisition Reserves of RS Ltd. acquired	8,00,000
	Less: Loss on investments held by RS Ltd. Value of investments cancelled 2,50,000 Less: Reduced value of shares of XY Ltd. <u>(20,000)</u>	<u>(2,30,000)</u>
	Amount of Reserves to be carried to Balance Sheet	<u>5,70,000</u>
6.	Share Capital in Combined Balance Sheet of XYZ Ltd.	

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	Holding of RS Ltd. (200 Equity Shares @ ₹ 100 each)	20,000
	Other Existing Shares (800 Equity Shares of ₹ 100 each)	80,000
	Given as Purchase Consideration (19,800 equity shares @ ₹ 100 each)	<u>19,80,000</u>
		<u>20,80,000</u>
7.	It has been assumed that the bank overdraft and cash balance can be netted of.	

Alternative Solution:

The candidates may pass a journal entry in the books of XY Ltd. for cancellation of shares held by RS Ltd.

In that case the first three entries in books of XY Ltd. will remain the same, further:-

		(₹ '000)	
		Dr. ₹	Cr. ₹
Equity Share Capital Account	Dr.	20	
To Reconstruction Account			20
Equity Share Capital (₹ 10) Account	Dr.	80	
To Equity Share Capital Account (₹ 100)			80
Reconstruction Account	Dr.	980	
To Profit and Loss Account			800
To Capital Reserve			180
Fixed Assets Account	Dr.	2,700	
Other Investments Account	Dr.	450	
Sundry Debtors Account	Dr.	400	
Cash and Bank Account	Dr.	250	
To Reserves Account			550
To 10% Debentures Account			500
To Loan from Financial Institutions Account			250
To Sundry Creditors Account			300
To Proposed Dividend Account			200
To Business Purchase Account			2,000
Business Purchase Account	Dr.	2,000	
To Liquidator of RS Ltd.			2,000
Liquidator of RS Ltd.	Dr.	2,000	
To Equity Shares (₹ 10 each)			2,000

Note: In the Balance Sheet, capital reserve will go up by ₹ 20,000 and general reserve will come down by ₹ 20,000.

Question 13

The following are the summarized Balance Sheets of C Ltd. and D Ltd. on 31st March, 2012:

Balance Sheets

Liabilities	C Ltd. ₹	D Ltd. ₹	Assets	C Ltd. ₹	D Ltd. ₹
Equity Shares of ₹ 100 each fully paid	45,00,000	15,00,000	Fixed Assets	30,00,000	1,50,000
General Reserve	4,00,000	3,00,000	Investments		
Profit and Loss A/c	7,34,000	30,000	3,000 shares in D Ltd.	4,50,000	—
14% Debentures	—	9,00,000	9,000 Shares in C Ltd.	—	15,00,000
Current Liabilities	6,00,000	2,70,000	Debtors	8,70,000	4,50,000
			Stock	14,40,000	6,30,000
			Bank Balance	4,74,000	2,70,000
	<u>62,34,000</u>	<u>30,00,000</u>		<u>62,34,000</u>	<u>30,00,000</u>

Stock of C Ltd. includes goods worth ₹ 3,00,000 purchased from D Ltd., which made a profit of 20% on selling price. As on 31.3.2012, C Ltd. owes to D Ltd. ₹ 1,20,000. C Ltd. absorbs D Ltd. on the basis of the intrinsic value of the shares of both companies as on 31st March, 2012. Before absorption C Ltd. has declared a dividend of 12%. Dividend tax is 10%.

Show the Balance Sheet of C Ltd. after the absorption of D Ltd. and the working for the number of shares issued.

Answer**(a) (i) Computation of Net Assets excluding Inter-Company Investments**

	C Ltd ₹	D Ltd ₹
A Total Assets		
Tangible Assets	57,84,000	15,00,000
Dividend Receivable	—	<u>1,08,000</u>
	57,84,000	16,08,000
B. External Liabilities		
Current Liabilities	6,00,000	2,70,000
Proposed Dividend	5,40,000	—
Dividend Tax	54,000	—
-14% Debentures	—	<u>9,00,000</u>
	<u>11,94,000</u>	<u>11,70,000</u>
C. Net Assets (A – B)	<u>45,90,000</u>	<u>4,38,000</u>

(ii) Intrinsic value of equity shares

Assume 'a' is the intrinsic value (net assets including inter company investments) of equity shares of C Ltd and 'b' is the intrinsic value of equity shares of D Ltd.

$$a = ₹ 45,90,000 + \frac{1}{5} \cdot b \quad (1)$$

$$b = ₹ 4,38,000 + \frac{1}{5} \cdot a \quad (2)$$

$$\text{or } b = ₹ 4,38,000 + \frac{1}{5} \cdot ₹ 45,90,000 + \frac{1}{5} \cdot b$$

$$\text{or } b = ₹ 4,38,000 + ₹ 9,18,000 + \frac{b}{25}$$

$$\text{or } \frac{24}{25} \cdot b = ₹ 13,56,000$$

$$\text{or } b = \frac{₹ 13,56,000}{24} \cdot 25 = ₹ 14,12,500$$

Putting the value of b in equation (1) we get,

$$a = ₹ 45,90,000 + \frac{1}{5} \cdot 14,12,500 = ₹ 48,72,500$$

$$\text{Intrinsic value of share of C Ltd.} = \frac{₹ 48,72,500}{45,000} = ₹ 108.278 \text{ approximately}$$

$$\text{Intrinsic value of share of D Ltd} = \frac{₹ 14,12,500}{15,000} = ₹ 94.167 \text{ approximately.}$$

(iii) Calculation of Purchase consideration

Value of shares held by outside shareholders in D Ltd:

$$\frac{₹ 14,12,500 \cdot 12,000}{15,000} = ₹ 11,30,000$$

Shares to be issued by C Ltd on the basis of intrinsic value of shares

$$= ₹ 11,30,000 \times (45,000 / 48,72,500)$$

10,436.12

Less: Shares held by D Ltd

(9,000.00)

Number of shares to be issued

1,436.12

Total purchase price for outside shareholders	₹
Additional shares in C Ltd. (1,436 x ₹ 108.278)	1,55,487*
Cash for fractional shares (0.12 x ₹ 108.278)	13*
Value of 3000 shares held by C Ltd	<u>2,82,500</u>
	<u>4,38,000</u>

(iv) General Reserve (C Ltd)	₹
As per Balance sheet	4,00,000
Less: Reduction in value of shares held in D Ltd (₹ 4,50,000 - ₹ 2,82,500)	<u>(1,67,500)</u>
	<u>2,32,500</u>

(v) Bank Balance	C Ltd.	D Ltd.
	₹	₹
As per Balance Sheet	4,74,000	2,70,000
Add: Dividend received	<u>-</u>	<u>1,08,000</u>
	4,74,000	3,78,000
Less: Dividend	5,40,000	
Dividend tax	54,000	
Cash for fractional shares <u>13</u>	<u>(5,94,013)</u>	<u>-</u>
	<u>(1,20,013)</u>	<u>3,78,000</u>
		= ₹ 2,57,987.

Balance Sheet of C Ltd (after absorption of D Ltd)

Particulars	Note No.	Amount (₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	46,43,600
(b) Reserves and Surplus	2	3,24,387
(2) Non-Current Liabilities		
Long-term borrowings	3	9,00,000
(3) Current Liabilities	4	7,50,000
Total		<u>66,17,987</u>
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets		31,50,000

* Appropriate figures have been considered.

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(2) Current assets		
(a) Inventories	5	20,10,000
(b) Trade receivables	6	12,00,000
(c) Cash and cash equivalents		2,57,987
Total		66,17,987

Notes to Accounts

		₹	₹
1.	Share Capital Issued and Subscribed 46,436 shares of ₹ 100 each fully paid (1,436 shares allotted to vendors for consideration other than cash)		46,43,600
2.	Reserves and surplus		
	General Reserve	2,32,500	
	Profit and Loss Account (₹ 7,34,000 – ₹ 5,40,000 – ₹ 54,000 – ₹ 60,000)	80,000	
	Securities Premium (₹ 1,55,487 – ₹ 1,43,600)	<u>11,887</u>	3,24,387
3.	Long Term Borrowings Secured		
	14% Debentures		9,00,000
4.	Current Liabilities		
	Current Liabilities	8,70,000	
	Less: Inter-Co. dues	<u>(1,20,000)</u>	7,50,000
5.	Inventories		
	Stock	20,70,000	
	Less: Unrealized Profit	<u>(60,000)</u>	20,10,000
6.	Trade receivables		
	Debtors	13,20,000	
	Less: Inter Co. dues	<u>(1,20,000)</u>	12,00,000

Question 14

The summarized Balance sheets of X Ltd. and its subsidiary Y Ltd. as at 31.3.2012 were as follows:

Liabilities	X Ltd. ₹	Y Ltd. ₹	Assets	X Ltd. ₹	Y Ltd. ₹
Share capital (Share of ₹ 10	50,00,000	10,00,000	Fixed assets Investment in Y	60,00,000	18,00,000

each)			Ltd. (60,000 shares)	6,00,000	---
General reserves	50,00,000	20,00,000	Sundry debtors	35,00,000	5,00,000
Profit and Loss account	20,00,000	15,00,000	Inventories	30,00,000	25,00,000
Secured loan	20,00,000	2,50,000	Cash and bank	39,00,000	2,00,000
Current liabilities	<u>30,00,000</u>	<u>2,50,000</u>			
	<u>1,70,00,000</u>	<u>50,00,000</u>		<u>1,70,00,000</u>	<u>50,00,000</u>

X Ltd. holds 60% of the paid-up capital of Y Ltd. and the balance is held by a foreign company.

A memorandum of understanding has been entered into with the foreign company by X Ltd. to the following effect:

- (i) The shares held by the foreign company will be sold to X Ltd. at a price per share to be calculated by capitalizing the yield at 15%. Yield, for this purpose, would mean 50% of the average of pre-tax profits for the last 3 years, which were ₹ 12 lakhs, 18 lakhs and 24 lakhs respectively. (Average tax rate was 40%).
- (ii) The actual cost of shares to the foreign company was ₹ 4,40,000 only. Gains accruing to the foreign company are taxable at 20%. The tax payable will be deducted from the sale proceeds and paid to government by X. 50% of the consideration (after payment of tax) will be remitted to the foreign company by X Ltd. and also any cash for fractional shares allotted.
- (iii) For the balance of consideration, X Ltd. would issue its shares at their intrinsic value.

It was also decided that X Ltd. would absorb Y Ltd. Simultaneously by writing down the Fixed assets of Y Ltd. by 10%. The Balance Sheet figures included a sum of ₹ 1,00,000 due by Y Ltd. to X Ltd. and stock of X Ltd. included stock of ₹ 1,50,000 purchased from Y Ltd., who sold them at cost plus 20%.

The entire arrangement was approved and put through by all concern effective from 1.4.2012.

You are required to indicate how the above arrangements will be recorded in the books of X Ltd. and also prepare a Balance Sheet after absorption of Y Ltd. Workings should form part of your answer.

Answer

X Ltd.

Balance Sheet as at 1st April, 2012

Particulars	Note No.	Amount (₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	53,34,660

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(b) Reserves and Surplus	2	89,64,320
(2) Non-Current Liabilities		
Long-term borrowings	3	22,50,000
(3) Current Liabilities	4	31,50,000
Total		1,96,98,980
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	5	76,20,000
(2) Current assets		
(a) Inventories	6	54,75,000
(b) Trade receivables	7	39,00,000
(c) Cash and cash equivalents		27,03,980
Total		1,96,98,980

Notes to Accounts

		₹	₹
1.	Share Capital 5,33,466 shares of ₹10 each (Out of the above 33,466 shares of ₹ 10 each issued for consideration other than cash)		53,34,660
2.	Reserves and surplus General Reserve Capital Reserve Profit and Loss Account ₹20,00,000 Less: unrealized profit on stock (₹25,000) Securities Premium (₹33,466 - 20)	50,00,000 13,20,000 19,75,000 <u>6,69,320</u>	89,64,320
3.	Long Term Borrowings Secured Loans (₹20,00,000 + ₹2,50,000)		22,50,000
4.	Current Liabilities (₹30,00,000 + ₹2,50,000) Less: Mutual Debts	32,50,000 <u>(1,00,000)</u>	31,50,000
5.	Tangible Assets Fixed Assets Less :Revaluation loss	78,00,000 <u>(1,80,000)</u>	76,20,000
6.	Inventories (₹30,00,000+ ₹25,00,000) Less: Unrealised profit on stock	50,00,000 <u>(25,000)</u>	54,75,000

7.	Trade receivables		
	Sundry Debtors (₹ 35,00,000+ ₹ 5,00,000)	40,00,000	
	Less: Mutual Debts	<u>(1,00,000)</u>	39,00,000

Working Notes:**(1) Yield of Y Ltd.**

$$\text{Average of Pre Tax Profit} = \frac{12 + 18 + 24}{3} = ₹ 18 \text{ lakhs}^*$$

$$\text{Yield} = 18 \times \frac{50}{100} = ₹ 9 \text{ lakhs}$$

(2) Price per share of Y Ltd:-

$$\text{Capitalised value of yield of Y Ltd.} = \frac{9 \text{ lakhs}}{15} \times 100 = ₹ 60 \text{ lakhs}$$

$$\text{No. of shares} = 1,00,000$$

$$\text{Price per share} = \frac{60 \text{ lakhs}}{1 \text{ lakh}} = ₹ 60 \text{ per share}$$

(3) Purchase consideration for 40% of share capital of Y Ltd.

$$= 1,00,000 \times 60 \times \frac{40}{100} = ₹ 24,00,000$$

(4) Calculation of intrinsic value of shares of X Ltd.

		₹
Total Assets excluding Investments in Y Ltd.		1,64,00,000
Value of Investment 60,000 × ₹ 60		<u>36,00,000</u>
		2,00,00,000
Less: Outside Liabilities:		
Secured Loan	20,00,000	
Current Liabilities	<u>30,00,000</u>	<u>(50,00,000)</u>
Net Assets		<u>1,50,00,000</u>

$$\text{Intrinsic value per share} = \frac{\text{Net Assets}}{\text{No. of Shares}} = \frac{₹ 1,50,00,000}{5,00,000} = ₹ 30 \text{ per share}$$

* By setting the trend, weighted average profit can also be calculated.

(5) Discharge of purchase consideration by X Ltd.

		Equity share capital ₹	Cash ₹	Total ₹
(i)	Payment of Tax (₹ 24 Lakh - ₹ 4.40 Lakh) x $\frac{20}{100}$ =	---	3,92,000	3,92,000
(ii)	Issue of shares to foreign company [50% of (24 Lakh – 3.92 Lakh) = 10.04 lakhs No. of shares issued by X Ltd. $\frac{10,04,000}{30}$ = 33,466.6666 shares Value of shares capital = 33,466 × ₹ 30 =	10,03,980	---	10,03,980
(iii)	Cash Payment [50% of (₹ 24 Lakh – ₹ 3.92 Lakh) = 10.04 lakhs]	---	10,04,000	10,04,000
(iv)	Cash for fractional shares = 0.6666 × ₹ 30	---	20	20
	Total	10,03,980	13,96,020	24,00,000

(6) Calculation for Goodwill/Capital Reserve to X Ltd.

		₹
	Total of assets as per Balance Sheet of Y Ltd.	50,00,000
Less:	10% Reduction in the value of Fixed Assets $\frac{10}{100} \times 18,00,000 =$	<u>1,80,000</u>
		48,20,000
Less:	Secured Loan	2,50,000
	Current Liabilities	<u>2,50,000</u>
		(5,00,000)
	Net Assets	43,20,000
Less:	Purchase consideration (outside shareholders)	<u>(24,00,000)</u>
		19,20,000
Less:	Investment in Y Ltd. as per Balance Sheet of X Ltd.	<u>(6,00,000)</u>
	Capital Reserve	<u>13,20,000</u>

(7) Cash and Bank Balance of X Ltd. after acquisition of shares

	₹
Opening Balance (X Ltd.)	39,00,000
Cash and Bank Balance of Y Ltd.	<u>2,00,000</u>

	41,00,000
Less: Remittance to the foreign company	<u>(10,04,020)</u>
	30,95,980
Less: T.D.S. paid to Government	<u>(3,92,000)</u>
	<u>27,03,980</u>

(8) Unrealized profit included in stock of X Ltd. = ₹ 1,50,000 x $\frac{20}{120}$ = ₹ 25,000

Question 15

The following are the summarized Balance sheets (as at 31.3.2012) of A Ltd. and B Ltd.:

Liabilities	A Ltd. ₹	B. Ltd. ₹	Assets	A Ltd. ₹	B. Ltd. ₹
Share Capital:			Fixed Assets	50,00,000	30,00,000
Equity Shares of ₹ 10 each	36,00,000	18,00,000	Investments	5,00,000	5,00,000
10% Preference shares of ₹ 100 each	12,00,000	-	Current Assets		
12% Preference shares of ₹ 100 each	-	6,00,000	Stock	18,00,000	12,00,000
Reserves and Surplus:			Debtors	15,00,000	12,00,000
Statutory Reserve	1,00,000	1,00,000	Bills receivable	50,000	10,000
General Reserve	25,00,000	17,00,000	Cash at Bank	1,50,000	90,000
Secured Loan					
15% Debentures	5,00,000	-			
12% Debentures	-	5,00,000			
Current Liabilities					
Sundry creditors	10,80,000	12,80,000			
Bills payable	<u>20,000</u>	<u>20,000</u>			
	<u>90,00,000</u>	<u>60,00,000</u>		<u>90,00,000</u>	<u>60,00,000</u>

Contingent liabilities for bills receivable discounted ₹ 20,000.

(A) The following additional information is provided to you:

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	A Ltd. ₹	B Ltd. ₹
Profit before Interest and Tax	14,75,000	7,80,000
Rate of Income-tax	40%	40%
Preference dividend	1,20,000	72,000
Equity dividend	3,60,000	2,70,000
Balance profit transferred to Reserve account.		

- (B) The equity shares of both the companies are quoted on the Mumbai Stock Exchange. Both the companies are carrying on similar manufacturing operations.
- (C) A Ltd proposes to absorb business of B Ltd. as on 31.3.2012. The agreed terms for absorption are:
- 12% Preference shareholders of B Ltd. will receive 10% Preference shares of A Ltd. sufficient to increase their present income by 20%.
 - The Equity shareholders of B Ltd. will receive equity shares of A Ltd. on the following terms:
 - The Equity shares of B Ltd. will be valued by applying to the earnings per share of B Ltd. 60 per cent of price earnings ratio of A Ltd. based on the results of 2011-12 of both the Companies.
 - The market price of Equity shares of A Ltd. is ₹ 40 per share.
 - The number of shares to be issued to Equity shareholders of B Ltd. will be based on the 80% of market price.
 - In addition to Equity shares, 10% Preference shares of A Ltd. will be issued to the equity shareholders of B Ltd. to make up for the loss in income arising from the above exchange of shares based on the dividends for the year 2011-2012.
 - 12% Debenture holders of B Ltd. are to be paid at 8% premium by 15% debentures in A Ltd. issued at a discount of 10%.
 - ₹ 16,000 is to be paid by A Ltd. to B Ltd. for liquidation expenses. Sundry Creditors of B Ltd. include ₹ 20,000 due to A Ltd. Bills receivable discounted by A Ltd. were all accepted by B Ltd.
 - Fixed assets of both the companies are to be revalued at 20% above book value. Stock in trade is taken over at 10% less than their book value.
 - Statutory reserve has to be maintained for two more years.
 - For the next two years no increase in the rate of equity dividend is anticipated.
 - Liquidation expense is to be considered as part of purchase consideration.

You are required to:

- (i) Find out the purchase consideration.
- (ii) Give journal entries in the books of A Ltd.
- (iii) Give the Balance Sheet as at 31.3.2012 after absorption.

Answer

(i) Computation of Purchase Consideration

	₹
<i>For Preference Shareholders</i>	
Present Income of Preference Shareholders of B Ltd.	72,000
Add : Required 20% increase	<u>14,400</u>
	<u>86,400</u>
10% Preference Shares to be issued of ₹ 8,64,000 (86,400/10x100)	
<i>For Equity Shareholders</i>	
Valuation of Equity Shares of B Ltd. =	
Number of shares x Value of one share	
(i.e. EPS of B Ltd. x P/E ratio of A Ltd. x 60/100)	
$= 1,80,000 \times \frac{₹ 20}{₹ 1} \times \frac{60}{100} = 1,80,000 \times 24 = ₹ 43,20,000$	
<i>Issue of Equity Shares</i>	
No. of Equity Shares to be issued at 80% of Market Price i.e.	
80% of ₹ 40 = ₹ 32	
$\frac{43,20,000}{32} = 1,35,000$ shares	
Equity Share Capital = 1,35,000 x ₹ 10 = ₹ 13,50,000	
Securities Premium = 1,35,000 x ₹ 22 = ₹ 29,70,000	
	<u>₹ 43,20,000</u>
<i>Issue of Preference Shares</i>	₹
Present Equity Dividend	2,70,000
Less: Expected Equity Dividend from A Ltd. $\frac{₹ 13,50,000}{₹ 10} \times \frac{10}{100}$	<u>(1,35,000)</u>
Loss in income	<u>1,35,000</u>
10% Preference Shares to be issued of ₹ 13,50,000 (1,35,000/10x 100)	

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Purchase Consideration	
Preference Shares Capital [₹ 8,64,000 + ₹ 13,50,000]	22,14,000
Equity Share Capital (1,35,000 shares of ₹ 10 each at ₹ 32 per share)	43,20,000
Liquidation Expenses (in cash)	<u>16,000</u>
	<u>65,50,000</u>

(ii) Journal Entries in the Books of A Ltd.

	Particulars		Dr. (₹)	Cr. (₹)
1.	Fixed Assets A/c To Revaluation Reserve (Being Revaluation of Fixed assets at 20% above book value)	Dr.	10,00,000	10,00,000
2.	Business Purchase A/c To Liquidator of B Ltd. (Being purchase consideration payable for the business taken over from B Ltd.)	Dr.	65,50,000	65,50,000
3.	Fixed Assets A/c Investment A/c Stock A/c Debtors A/c Bills Receivable A/c Cash at Bank A/c Goodwill A/c (Balancing figure) To 12% Debentures in B Ltd. To Creditors To Bills Payable To Business Purchase A/c (Being incorporation of different assets and liabilities of B Ltd. taken over at agreed values and balance debited to goodwill account)	Dr. Dr. Dr. Dr. Dr. Dr. Dr. Dr.	36,00,000 5,00,000 10,80,000 12,00,000 10,000 90,000 19,10,000	5,40,000 12,80,000 20,000 65,50,000
4.	Liquidator of B Ltd. To Equity Share Capital A/c To Securities Premium A/c To Preference Share Capital A/c To Bank A/c (Being discharge of consideration for B Ltd's business)	Dr.	65,50,000	13,50,000 29,70,000 22,14,000 16,000

5.	12% Debentures in B Ltd. Discount on issue of Debentures To 15% Debentures (Being allotment of 15% Debentures to debenture holders at a discount of 10% to discharge liability of B Ltd. debentures)	Dr. Dr.	5,40,000 60,000	6,00,000
6.	Sundry Creditors A/c To Sundry Debtors A/c (Being cancellation of Mutual owing)	Dr.	20,000	20,000
7.	Amalgamation Adjustment A/c To Statutory Reserve A/c (Being statutory reserve account is maintained under statutory requirements)	Dr.	1,00,000	1,00,000
8.	Securities Premium A/c To Discount on issue of Debentures A/c (Being discount on issue of Debentures written off out of securities premium)	Dr.	60,000	60,000

(iii) **Balance Sheet of A Ltd (after absorption of B Ltd.)**
as on 31.3.2012

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	83,64,000
(b) Reserves and Surplus	2	66,10,000
(2) Non-Current Liabilities		
Long-term borrowings	3	11,00,000
(3) Current Liabilities		
Trade payables	4	23,80,000
Total		1,84,54,000
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
i. Tangible assets	5	96,00,000
ii. Intangible assets	6	19,10,000

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(b) Non-current investments	7	10,00,000
(c) Other non-current assets	8	1,00,000
(2) Current assets		
(a) Inventories	9	28,80,000
(b) Trade receivables	10	27,40,000
(c) Cash and cash equivalents		2,24,000
Total		1,84,54,000

Notes to Accounts

		₹	₹
1.	Share Capital		
	4,95,000 Equity shares of ₹ 10 each fully paid	49,50,000	
	(1,35,000 shares have been allotted as fully paid-up for consideration other than cash)		
	10% Preference shares of ₹ 100 each fully paid	<u>34,14,000</u>	83,64,000
2.	Reserves and surplus		
	Statutory reserve	2,00,000	
	Revaluation reserve	10,00,000	
	General reserve	25,00,000	
	Securities Premium	<u>29,10,000</u>	66,10,000
3.	Long Term Borrowings		
	Secured borrowings		
	15% Debentures (₹ 5,00,000 + ₹ 6,00,000)		11,00,000
4.	Trade payables		
	Creditors (₹ 10,80,000 + ₹ 12,80,000 - ₹ 20,000)	23,40,000	
	Bills Payable (₹ 20,000 + ₹ 20,000)	<u>40,000</u>	23,80,000
5.	Tangible Assets		
	Other Fixed Assets (₹ 60,00,000 + ₹ 36,00,000)		96,00,000
6.	Intangible assets		
	Goodwill		19,10,000
7.	Non Current Investment		
	Investment (₹ 5,00,000 + ₹ 5,00,000)		10,00,000
8.	Other non-current assets		
	Amalgamation Adjustment A/c		1,00,000

9.	Inventories		
	Stock (₹ 18,00,000+ ₹ 10,80,000)		28,80,000
10.	Trade receivables		
	Debtors (₹ 15,00,000+ ₹ 12,00,000- ₹ 20,000)	26,80,000	
	Bills Receivable (₹ 50,000+ ₹ 10,000)	<u>60,000</u>	27,40,000

Note: No footnote will appear for contingent liability as it has been converted into actual liability after absorption of B Ltd.

Working Notes:

1. Calculation of EPS & P/E ratio

	A Ltd. ₹	B Ltd. ₹
Profit before Interest and Tax	14,75,000	7,80,000
Less: Interest on debentures	<u>(75,000)</u>	<u>(60,000)</u>
Profit before tax	14,00,000	7,20,000
Less: Tax @ 40%	<u>(5,60,000)</u>	<u>(2,88,000)</u>
	8,40,000	4,32,000
Less: Preference Dividend	<u>(1,20,000)</u>	<u>(72,000)</u>
Earnings available for equity shareholders	<u>7,20,000</u>	<u>3,60,000</u>
Number of shares	3,60,000 shares	1,80,000 shares
EPS (Earnings/ No. of shares)	2	2
Market Price	₹ 40	Not given
P/E ratio	40/2 = 20	N.A.

2. Computation of Goodwill/Capital Reserve on absorption:

	₹	₹	₹
Purchase Consideration			65,50,000
Fixed Assets taken over	30,00,000		
Add: Increase by 20%	<u>6,00,000</u>	36,00,000	
Investments		5,00,000	
Current Assets:			
Stock	12,00,000		
Less: Reduction in value by 10%	<u>(1,20,000)</u>		
	10,80,000		
Debtors	12,00,000		

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B/R	10,000		
Cash at Bank	<u>90,000</u>	<u>23,80,000</u>	
		64,80,000	
Less: Outside Liabilities:			
12% Debentures at premium	5,40,000		
Sundry Creditors	12,80,000		
Bills Payable	<u>20,000</u>	<u>(18,40,000)</u>	<u>46,40,000</u>
Goodwill			<u>19,10,000</u>

Question 16

The summarized Balance Sheets of Strong Ltd. and Weak Ltd. as on 31.03.2012 is as below:

Summarised Balance Sheet as on 31.03.2012

Liabilities	Strong Ltd. ₹	Weak Ltd. ₹	Assets	Strong Ltd. ₹	Weak Ltd. ₹
Equity Share Capital (₹ 100 each)	50,00,000	30,00,000	Fixed Assets other than Goodwill	30,00,000	20,00,000
Reserve	4,00,000	2,00,000	Stock	8,00,000	6,00,000
P/L A/c	6,00,000	4,00,000	Debtors	14,00,000	9,00,000
Creditors	5,00,000	3,00,000	Cash & Bank	12,00,000	3,50,000
			Preliminary Expenses	<u>1,00,000</u>	<u>50,000</u>
	<u>65,00,000</u>	<u>39,00,000</u>		<u>65,00,000</u>	<u>39,00,000</u>

Strong Ltd. takes over Weak Ltd. on 01.07.12. No Balance Sheet of Weak Ltd. is available as on that date. It is however estimated that Weak Ltd. earns estimated profit of ₹ 2,00,000 after charging proportionate depreciation @ 10% p.a. on fixed assets, during April-June, 2012.

Estimated profit of Strong Ltd. during these 3 months is ₹ 4,00,000 after charging proportionate depreciation @ 10% p.a. on fixed assets.

Both the companies have declared and paid 10% dividend within this 3 months' period. Goodwill of Weak Ltd. is valued at ₹ 2,00,000 and Fixed Assets are valued at ₹ 1,00,000 above the estimated book value. Purchase consideration is to be satisfied by Strong Ltd. by shares at par. Ignore Income-tax.

You are required to calculate the following:

- No. of shares to be issued by Strong Ltd. to Weak Ltd. against purchase consideration;
- Net Current Assets of Strong Ltd. and Weak Ltd. as on 01.07.2012;
- P/L A/c balance of the Strong Ltd. as on 01.07.2012;
- Fixed Assets as on 01.07.2012;
- Balance Sheet of Strong Ltd. as on 01.07.2012 after take over of Weak Ltd.

Answer

- (i) Number of shares to be issued by Strong Ltd. to Weak Ltd. against purchase consideration

<i>Weak Ltd.</i>	₹	₹
Goodwill		2,00,000
Fixed Assets	20,00,000	
Less: Depreciation	<u>(50,000)</u>	
	19,50,000	
Add: Appreciation	<u>1,00,000</u>	20,50,000
Stock		6,00,000
Debtors		9,00,000
Cash and Bank balances	3,50,000	
Add: Profit after depreciation	2,00,000	
Add: Depreciation (non-cash)	<u>50,000</u>	
Less: Dividend	<u>(3,00,000)</u>	<u>3,00,000</u>
		40,50,000
Less: Creditors		<u>(3,00,000)</u>
Purchase Consideration		<u>37,50,000</u>

- (ii) Calculation of Net Current Assets as on 01.07.2012

	₹	<i>Strong Ltd.</i> ₹		<i>Weak Ltd.</i> ₹
Current assets:				
Stock		8,00,000		6,00,000
Debtors		14,00,000		9,00,000
Cash and Bank	12,00,000		3,50,000	
Less: Dividend	<u>(5,00,000)</u>		<u>(3,00,000)</u>	
Add: Profit before depreciation	<u>4,75,000</u>	<u>11,75,000</u>	<u>2,50,000</u>	<u>3,00,000</u>
		33,75,000		18,00,000
Less: Creditors		<u>(5,00,000)</u>		<u>(3,00,000)</u>
		<u>28,75,000</u>		<u>15,00,000</u>

- (iii) Profit and Loss Account balance of Strong Ltd. as on 1.07.2012

	₹
P & L A/c balance as on 31.03.2012	6,00,000
Less: Dividend paid	<u>(5,00,000)</u>
	1,00,000

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Add: Estimated profit for 3 months after charging depreciation	4,00,000
	5,00,000
Less: Preliminary expenses*	(1,00,000)
	<u>4,00,000</u>

(iv) Fixed Assets as on 01.07.2012

Fixed Assets of Strong Ltd. as on 31.03.2012		30,00,000
Less: Depreciation for 3 months		(75,000)
		29,25,000
Fixed assets taken over of Weak Ltd. as on 31.03.2012	20,00,000	
Less: Proportionate depreciation for 3 months on fixed assets	<u>(50,000)</u>	
	19,50,000	
Add: Appreciation above the estimated book value	<u>1,00,000</u>	<u>20,50,000</u>
		<u>49,75,000</u>

(v) Balance Sheet of Strong Ltd. as on 01.07.2012 (after Take Over)

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	87,50,000
(b) Reserves and Surplus	2	8,00,000
(2) Current Liabilities		
Trade payables	3	8,00,000
Total		<u>1,03,50,000</u>
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
i. Tangible assets	4	49,75,000
ii. Intangible assets	5	2,00,000
(2) Current assets		
(a) Inventories		14,00,000
(b) Trade receivables		23,00,000
(c) Cash and cash equivalents		14,75,000
Total		<u>1,03,50,000</u>

* As per para 56 of AS 26, 'Intangible Assets', preliminary expenses are to be recognized as expenses as and when they are incurred.

Notes to Accounts:

		₹	₹
1.	Share Capital 87,500 (50,000+ 37,500) Equity shares of ₹100 each		87,50,000
2.	Reserves and surplus		
	Reserves	4,00,000	
	Profit and Loss Account [as computed in (iii)]	<u>4,00,000</u>	8,00,000
3.	Trade payables Creditors (₹ 5,00,000 + ₹ 3,00,000)		8,00,000
4.	Tangible Assets Fixed assets [as computed in (iv)]		49,75,000
5.	Intangible assets Goodwill		2,00,000

Question 17

T. Ltd. and V. Ltd. propose to amalgamate. Their summarized balance sheets as at 31st March, 2012 were as follows:

Liabilities	T. Ltd. ₹	V. Ltd. ₹	Assets	T. Ltd. ₹	V. Ltd. ₹
Share capital: Equity shares of ₹ 10 each	15,00,000	6,00,000	Fixed assets Less: Depreciation	12,00,000	3,00,000
General reserve	6,00,000	60,000	Investments (face value of ₹ 3 lakhs, 6% tax free G.P. notes)	3,00,000	-
Profit & Loss A/c	3,00,000	90,000	Stock	6,00,000	3,90,000
Creditors	3,00,000	1,50,000	Debtors	5,10,000	1,80,000
			Cash and bank balances	<u>90,000</u>	<u>30,000</u>
	<u>27,00,000</u>	<u>9,00,000</u>		<u>27,00,000</u>	<u>9,00,000</u>

Their net profits (after taxation) were as follows:

Year	T. Ltd.	V. Ltd.
2009-10	3,90,000	1,35,000

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2010-11	3,75,000	1,20,000
2011-12	4,50,000	1,68,000

Normal trading profit may be considered as 15% on closing capital invested. Goodwill may be taken as 4 years' purchase of average super profits. The stock of T. Ltd. and V. Ltd. are to be taken at ₹ 6,12,000 and ₹ 4,26,000 respectively for the purpose of amalgamation. W. Ltd. is formed for the purpose of amalgamation of two companies.

- Suggest a scheme of capitalization of W. Ltd. and ratio of exchange of shares; and
- Draft the opening balance sheet of W. Ltd. [£]

Answer

- Scheme of capitalization of W. Ltd. and ratio of exchange of shares**
Computation of Net Assets of amalgamating companies

	T. Ltd. ₹	V. Ltd. ₹
Goodwill (W.N.2)	3,19,200	1,21,200
Fixed Assets	12,00,000	3,00,000
6% investments (Non-trade)	3,00,000	-
Stock	6,12,000	4,26,000
Debtors	5,10,000	1,80,000
Cash and Bank Balances	<u>90,000</u>	<u>30,000</u>
	30,31,200	10,57,200
Less: Creditors	<u>(3,00,000)</u>	<u>(1,50,000)</u>
Net Assets	<u>27,31,200</u>	<u>9,07,200</u>
No. of Equity shares	1,50,000	60,000
Intrinsic value of a share	₹ 18.208	₹ 15.12
No of shares to be issued by W. Ltd to		
T. Ltd 1,50,000 x 18.208/10	2,73,120 shares	
V. Ltd 60,000 x 15.12/10		90,720 shares

In total 2,73,120 + 90,720 i.e. 3,63,840 shares will be issued by W. Ltd.

Ratio of exchange of shares will be as follows:

- Holders of 1,50,000 equity shares of T Ltd. will get 2,73,120 shares in W. Ltd.
- Similarly, holders of 60,000 equity shares of V Ltd. will get 90,720 shares in W. Ltd.

[£] The question involves the application of calculation of goodwill. Therefore, students are advised to go through this problem after preparing Chapter 9.

(b) Opening Balance Sheet of W. Ltd.

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
Share Capital	1	36,38,400
(2) Current Liabilities		
Trade payables		4,50,000
Total		40,88,400
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
i. Tangible assets	2	15,00,000
ii. Intangible assets	3	4,40,400
(b) Non-current investments	4	3,00,000
(2) Current assets		
(a) Inventories		10,38,000
(b) Trade receivables		6,90,000
(c) Cash and cash equivalents		1,20,000
Total		40,88,400

Notes to Accounts

	(₹)
1. Share Capital	
Equity share capital	
3,63,840 Equity shares of ₹ 10 each	36,38,400
(Issued for consideration other than cash, pursuant to scheme of amalgamation)	
2. Tangible Assets	
Other Fixed Assets (₹ 12,00,000 + ₹ 3,00,000)	15,00,000
3. Intangible assets	
Goodwill (W.N.2) (₹ 3,19,200 + ₹ 1,21,200)	4,40,400
4. Non-current investments	
Investments in 6% Tax free G.P. Notes	3,00,000

Working Notes:**1. Calculation of closing trading capital employed on the basis of net assets**

	<i>T. Ltd.</i> ₹	<i>V. Ltd.</i> ₹
Fixed Assets	12,00,000	3,00,000
Stock	6,12,000	4,26,000
Debtors	5,10,000	1,80,000
Cash and Bank Balances	<u>90,000</u>	<u>30,000</u>
	24,12,000	9,36,000
Less: Creditors	<u>(3,00,000)</u>	<u>(1,50,000)</u>
Net Assets	<u>21,12,000</u>	<u>7,86,000</u>

2. Calculation of value of goodwill

		<i>T. Ltd.</i> ₹	<i>V. Ltd.</i> ₹
(i)	Average Trading Profit		
	2009-10	3,90,000	1,35,000
	2010-11	3,75,000	1,20,000
	2011-12	<u>4,50,000</u>	<u>1,68,000</u>
	Profit after tax	<u>12,15,000</u>	<u>4,23,000</u>
	Profit before tax (40%)*	20,25,000	7,05,000
	Add : Under valuation of closing stock	<u>12,000</u>	<u>36,000</u>
		<u>20,37,000</u>	<u>7,41,000</u>
	Average of 3 years' profit before tax	6,79,000	2,47,000
	Less: Income from non-trade investments (₹ 3,00,000 x 6%)	<u>(18,000)</u>	<u>-</u>
	Average profit before tax	6,61,000	2,47,000
	Less: 40% tax	<u>(2,64,400)</u>	<u>(98,800)</u>
	Average profit after tax	<u>3,96,600</u>	<u>1,48,200</u>
(ii)	Super Profits		
	Average trading profit	3,96,600	1,48,200
	Less: Normal Profit		
	T. Ltd. ₹ 21,12,000 x 15%	(3,16,800)	
	V. Ltd ₹ 7,86,000 x 15%		(1,17,900)
		<u>79,800</u>	<u>30,300</u>
(iii)	Value of goodwill at 4 years' purchase of super profits	<u>3,19,200</u>	<u>1,21,200</u>

* Tax rate of 40% has been assumed.

Question 18

The following are the summarized Balance Sheets of Andrew Ltd. and Barry Ltd., as at 31.12.2011:

Andrew Ltd.

Liabilities	Amount (₹ '000)	Assets	Amount (₹ '000)
Share capital 3,00,000 Equity shares of ₹ 10 each	3,000	Fixed assets	3,400
10,000 Preference shares of ₹ 100 each	1,000	Stock (pledged with secured loan creditors)	18,400
General reserve	400	Other Current assets	3,600
Secured loans (secured against pledge of stocks)	16,000	Profit and Loss account	16,600
Unsecured loans	8,600		
Current liabilities	13,000		
	42,000		42,000

Barry Ltd.

Liabilities	Amount (₹ '000)	Assets	Amount (₹ '000)
Share capital 1,00,000 Equity shares of ₹ 10 each	1,000	Fixed assets	6,800
General reserve	2,800	Current assets	9,600
Secured loans	8,000		
Current liabilities	4,600		
	16,400		16,400

Both the companies go into liquidation and Charlie Ltd., is formed to take over their businesses. The following information is given:

- (a) All Current assets of two companies, except pledged stock are taken over by Charlie Ltd. The realisable value of all Current assets are 80% of book values in case of Andrew Ltd. and 70% for Barry Ltd. Fixed assets are taken over at book value.
- (b) The break up of Current liabilities is as follows:

	Andrew Ltd. ₹	Barry Ltd. ₹
Statutory liabilities (including ₹ 22 lakhs in case of Andrew Ltd. in case of a claim not having been admitted shown as contingent liability)	72,00,000	10,00,000
Liability to employees	30,00,000	18,00,000

The balance of Current liability is miscellaneous creditors.

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- (c) Secured loans include ₹ 16,00,000 accrued interest in case of Barry Ltd.
- (d) 2,00,000 equity shares of ₹ 10 each are allotted by Charlie Ltd. at par against cash payment of entire face value to the shareholders of Andrew Ltd. and Barry Ltd. in the ratio of shares held by them in Andrew Ltd. and Barry Ltd.
- (e) Preference shareholders are issued Equity shares worth ₹ 2,00,000 in lieu of present holdings.
- (f) Secured loan creditors agree to continue the balance amount of their loans to Charlie Ltd. after adjusting value of pledged security in case of Andrew Ltd. and after waiving 50% of interest due in the case of Barry Ltd.
- (g) Unsecured loans are taken over by Charlie Ltd. at 25% of Loan amounts.
- (h) Employees are issued fully paid Equity shares in Charlie Ltd. in full settlement of their dues.
- (i) Statutory liabilities are taken over by Charlie Ltd. at full values and miscellaneous creditors are taken over at 80% of the book value.

Show the opening Balance Sheet of Charlie Ltd. Workings should be part of the answer.

Answer

Balance sheet of Charlie Ltd. as at 31st December, 2011

Particulars	Note No.	(₹ '000)
I. Equity and Liabilities		
(1) Shareholder's Funds		
Share Capital	1	7,000
(2) Non-Current Liabilities		
Long-term borrowings	2	10,630
(3) Current Liabilities	3	13,640
Total		31,270
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
i. Tangible assets	4	10,200
ii. Intangible assets	5	9,470
(2) Current assets	6	11,600
Total		31,270

Notes to Accounts

			(₹ 000)
1.	Share Capital <i>Issued, subscribed & Paid up:</i> 7,00,000 equity shares of ₹ 10 each, fully paid up (W.N.5) (of the above 5,00,000 shares have been issued for consideration other than cash)		7,000
2.	Long Term Borrowings Secured loans (₹ 1,280 + ₹ 7,200) Unsecured Loans (25% of ₹ 8,600)	8,480 <u>2,150</u>	10,630
3.	Current Liabilities (₹ 7,200 + ₹ 1,000 + ₹ 4,000 + ₹ 1,440)		13,640
4.	Tangible Assets Fixed Assets (₹ 3,400 + ₹ 6,800)		10,200
5.	Intangible assets Goodwill (W.N.4)		9,470
6.	Current Assets Cash & Cash Equivalent Other Current Assets (₹ 2,880 + ₹ 6,720)	2,000 <u>9,600</u>	11,600

Working Notes:

1. Value of miscellaneous creditors taken over by Charlie Ltd.

(₹ '000)

	Andrew Ltd.	Barry Ltd.
Given in balance sheet	13,000	4,600
Less: Statutory liabilities	(5,000)	(1,000)
Liability to employees	<u>(3,000)</u>	<u>(1,800)</u>
Miscellaneous creditors	<u>5,000</u>	<u>1,800</u>
80% thereof	<u>4,000</u>	<u>1,440</u>

2. Value of total liabilities taken over by Charlie Ltd.

(₹ '000)

	Andrew Ltd.	Barry Ltd.
Current liabilities		
Statutory liabilities	7,200	1,000

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Liability to employees	3,000		1,800	
Miscellaneous creditors (W.N.1)	<u>4,000</u>	14,200	<u>1,440</u>	4,240
<i>Secured loans</i>				
Given in Balance Sheet	16,000		8,000	
Interest waived	-		<u>800</u>	7,200
Value of Stock (80% of ₹ 184 lakhs)	<u>14,720</u>	1,280		
<i>Unsecured Loans</i> (25% of ₹ 86 lakhs)		<u>2,150</u>		-
		<u>17,630</u>		<u>11,440</u>

3. Assets taken over by Charlie Ltd.

(₹ '000)

	Andrew Ltd. ₹	Barry Ltd. ₹
Fixed Assets (Assumed on book value basis)	3,400	6,800
Current Assets 80% and 70% respectively of book value	<u>2,880</u>	<u>6,720</u>
	<u>6,280</u>	<u>13,520</u>

4. Goodwill / Capital Reserve on amalgamation

(₹ '000)

Liabilities taken over (W.N. 2)		17,630	11,440
Equity shares to be issued to Preference Shareholders		<u>200</u>	-
	A	17,830	11,440
Less: total assets taken over (W.N. 3)	B	<u>(6,280)</u>	<u>(13,520)</u>
	A-B	11,550	(2,080)
		Goodwill	Capital Reserve
Net Goodwill		9,470	

5. Equity shares issued by Charlie Ltd.

(i)	For Cash		Number 2,00,000
	For consideration other than cash		
(ii)	In Discharge of Liabilities to Employees	4,80,000	
(iii)	To Preference shareholders	<u>20,000</u>	<u>5,00,000</u>
			<u>7,00,000</u>
	Value of shares (₹ 10 x 7,00,000)		₹ 70 lakhs

Question 19

Agni Ltd. and Bayu Ltd. both engaged in similar merchanting activities since 2010, decide to amalgamate their businesses. A holding company, Chandrama Ltd. would be formed on 1st January, 2012 to acquire the entire shares in both the companies.

From the information given below you are required to prepare:

- (a) *A statement of purchase consideration, supported by requisite working notes.*
- (b) *Balance Sheet of Chandrama Ltd. after the transactions have been completed.*
 - (i) *The terms of the offer were:*
 - *₹ 100, 15 per cent debentures for every ₹ 100 of net assets owned by each company on 31st December, 2011.*
 - *₹ 100 equity shares based on two years purchase of profit before taxation. The profit is to be determined by taking weighted average profits of 2010 and 2011, weights being 1 and 2 respectively.*
 - (ii) *It was agreed that the accounts of Bayu Ltd. for the two years ended 31st December, 2011 be adjusted, where necessary, to conform to the accounting policies followed by Agni Ltd.*
 - (iii) *The Pre-tax profits, including investment income, of the two companies were as follows:*

	2010 ₹	2011 ₹
Agni Ltd.	16,38,000	16,36,000
Bayu Ltd.	17,88,300	25,74,000

- (iv) *Agni Ltd. values its stock on FIFO basis while Bayu Ltd. used a different basis. To bring Bayu Ltd.'s values in line with those of Agni Ltd, value of its stock will require to be reduced by ₹ 36,000 at the end of 2010 and ₹ 1,02,000 at the end of 2011.*
- (v) *Both the companies use straight line method of depreciation.*
- (vi) *Bayu Ltd. deducts 1 per cent from trade debtors as a general provision against doubtful debts.*
- (vii) *Prepaid expenses in Bayu Ltd. include advertisement expenditure carried forward of ₹ 1,80,000 in 2010 and ₹ 90,000 in 2011, being part of initial advertising in 2010, which is being written off over three years. Similar expenditure in Agni Ltd. has been fully written off in 2010.*
- (viii) *To bring Director's remuneration on to a comparative basis, the profits of Bayu Ltd. are to be reduced by ₹ 1,20,000 in 2010 and ₹ 1,80,000 in 2011 and the net assets are also to be adjusted accordingly.*

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Summarised Balance Sheets as at 31st December, 2010 and 2011 were as follows:

Agni Ltd.

Liabilities	2010 ₹	2011 ₹	Assets	2010 ₹	2011 ₹
Share capital issued and subscribed: 12,000 shares of ₹ 100 each, fully paid	12,00,000	12,00,000	Fixed assets: Furniture and Fixtures: at cost	6,90,000	6,90,000
Reserves and Surplus			Less: depreciation	(69,000)	(1,38,000)
Capital reserve	-	2,10,000	Investments: Quoted investments at market value	-	7,80,000
Revenue reserve	7,98,300	16,74,000	Current assets:		
Current Liabilities and provisions:			Stock at cost	18,30,000	21,75,000
Sundry creditors	15,02,700	18,21,000	Sundry debtors	18,00,000	22,20,000
Provision for taxation	8,40,000	9,60,000	Prepaid expenses	30,000	42,000
			Cash at bank	60,000	96,000
	43,41,000	58,65,000		43,41,000	58,65,000

Bayu Ltd.

Liabilities	2010 ₹	2011 ₹	Assets	2010 ₹	2011 ₹
Share capital: Issued and subscribed 15,000 equity shares of ₹ 100 each, fully paid	15,00,000	15,00,000	Fixed assets: Furniture and fixture at cost	9,60,000	9,60,000
Reserves and surplus:			Less: depreciation	(1,44,000)	(2,88,000)
Revenue reserve	8,58,000	21,42,000	Investments:		
Current liabilities and provisions:			Quoted investments (Market value ₹ 14,70,000)	-	12,00,000
Sundry creditors	14,70,000	14,82,000	Current assets:		
Bank overdraft	-	5,10,000	Stock at cost	17,91,000	22,26,000
Provision for taxation	9,30,000	12,90,000			

			Sundry debtors		
			Less: provision	17,82,000	26,73,000
			Prepaid expenses	2,16,000	1,44,000
			Cash at bank	1,53,000	9,000
	47,58,000	69,24,000		47,58,000	69,24,000

Answer

(a) Statement of Purchase Consideration

Agni Ltd. Bayu Ltd. (Refer W.N. 1)

Year	PBT (₹)	Weight	₹	PBT (₹)	Weight	₹
2010	16,38,000	1	16,38,000	15,18,300	1	15,18,300
2011	18,36,000	2	36,72,000	27,63,000	2	55,26,000
Total Profit			53,10,000			70,44,300
Weighted average profit (Divided by 3)			17,70,000			23,48,100
(i)	Two years' purchase of average profits		35,40,000			46,96,200
(ii)	Net assets (Refer working notes 2 and 3)		30,84,000			35,43,000
			66,24,000			82,39,200
(iii)	Discharge of purchase consideration 82,362 Shares will be issued for goodwill amounting ₹ 82,36,200 (₹ 35,40,000 + ₹ 46,96,200) 66,270 15% Debentures will be issued for net assets amounting ₹ 66,27,000 (30,84,000 + 35,43,000) Total purchase consideration will amount to ₹ 148,63,200.					

(b) Balance Sheet of Chandrama Ltd. as on 1st January, 2012

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Fund		
Share Capital	1	82,36,200
(2) Non-Current Liabilities		
Long-term borrowings	2	66,27,000
Total		1,48,63,200

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II. Assets		
(1) Non-current assets		
Non-current investments	3	1,48,63,200
Total		1,48,63,200

Notes to Accounts

		(₹)	(₹)
1.	Share Capital <i>Issued and subscribed</i> 82,362 shares of ₹ 100 each, fully paid up (Issued for consideration other than cash)		82,36,200
2.	Long Term Borrowings <i>Secured Loans</i> 66,270 15% Debentures of ₹100 each, fully paid		66,27,000
3.	Non-current investments Shares in Agni Ltd.	66,24,000	
	Shares in Bayu Ltd.	<u>82,39,200</u>	1,48,63,200

Working Notes:

1. Statement of adjusted Net Profits of Bayu Ltd.

	Year 2010		Year 2011	
	₹	₹	₹	₹
Net Profit as given		17,88,300	-	25,74,000
Add: Provision for Bad Debts-Note (a)	18,000		27,000	
Advertising	-		90,000	
Depreciation- Note(b)	48,000		48,000	
Appreciation in Investment	-		2,70,000	
Value of Opening Stock	-	66,000	<u>36,000</u>	4,71,000
		18,54,300		30,45,000
Less: Value of Closing Stock	36,000		1,02,000	
Advertising	1,80,000		-	
Directors' Remuneration	1,20,000	(3,36,000)	1,80,000	(2,82,000)
		15,18,300		27,63,000

Note:

		(₹) Year 2010	(₹) Year 2011
(a)	Sundry Debtors as per Balance sheet	17,82,000	26,73,000
	Provision created		
	1% of (₹ 17,82,000 / .99)	18,000	
	1% of (₹ 26,73,000 / .99)		27,000
(b)	Rate of depreciation under straight line method for Agni Ltd. is (₹ 69,000 / 6,90,000) × 100 = 10%. Rate of depreciation under straight line method for Bayu Ltd. is (₹ 1,44,000 / 9,60,000) × 100 = 15% Difference of 5% in depreciation amount i.e. (5% of ₹ 9,60,000 = ₹ 48,000) has been added back to ensure uniform accounting policies.		

2. Statement of Net Assets of Agni Ltd.

	₹	₹
Total Assets		58,65,000
Less: Sundry Creditors	18,21,000	
Provision for Taxation	<u>9,60,000</u>	(27,81,000)
		<u>30,84,000</u>

3. Statement of Adjusted Net Assets of Bayu Ltd.

	₹	₹
Furniture and Fixtures	9,60,000	
Less: Depreciation at 10% p.a. for two years	<u>(1,92,000)</u>	7,68,000
Quoted investments at market value		14,70,000
Stock (₹ 22,26,000 – ₹ 1,02,000)		21,24,000
Sundry Debtors after Reversal of Provision (₹ 26,73,000 + ₹ 27,000)		27,00,000
Prepaid Expenses (₹ 1,44,000 – ₹ 90,000)		54,000
Cash at Bank		<u>9,000</u>
		71,25,000
Less: Sundry Creditors	14,82,000	
Bank Overdraft	5,10,000	
Liability for Directors' Remuneration	3,00,000	
Provision for Taxation	<u>12,90,000</u>	(35,82,000)
		<u>35,43,000</u>

4.82 Financial Reporting

Question 20

Small Ltd. and Little Ltd., two companies in the field of speciality chemicals, decided to go in for a follow on Public Offer after completion of an amalgamation of their businesses. As per agreed terms initially a new company Big Ltd. will be incorporated on 1st January, 2012 with an authorized capital of ₹ 2 crore comprised of 20 lakh equity shares of ₹ 10 each. The holding company would acquire the entire shareholding of Small Ltd. & Little Ltd. and in turn would issue its shares to the outside holders of these shares. It is also agreed that the consideration would be a multiple of the average P/E ratio for the period 1st January, 2011 to 31st March, 2011 times the rectified profits of each company, subject to necessary adjustments for complying with the terms of the share issue.

The following information is supplied to you:

	Small Ltd.	Little Ltd.
Ordinary Shares of ₹ 10 each (Nos.)	40 lakhs	20 lakhs
10% Preference shares of ₹ 100 each (Nos.)	2 lakh	Nil
10% Preference shares of ₹ 10 each (Nos.)	Nil	2 lakh
5% debentures of ₹ 10 each (Nos.)	4 lakh	4 lakh
Investments Held		
(a) 4 lakh ordinary shares in Small Ltd.	-	₹ 40 lakhs
(b) 2 lakh ordinary shares in Little Ltd.	₹ 20 lakhs	-
Profit before Interest & Tax (PBIT) after considering impact of Inter-company Transactions and Holdings.	₹ 50 lakhs	₹ 25 lakhs
Average P/E ratio January, 2011 to March, 2011	10	8

The following additional information is also furnished to you in respect of adjustments required to the profit figure as given above:

1. The profits of the respective companies would be adjusted for half the value of contingent liabilities as on 31st March, 2011.
2. Debtors of Small Ltd. include an irrecoverable amount of ₹ 2 lakh against which ₹ 1 lakh was recovered but kept in Advance account.
3. Little Ltd. had omitted to provide for increased FOREX liability of US\$10,000 on loan availed in financial year 2007-08 for purchase of Machinery. The machinery was acquired on 1st January, 2008 and put to use in financial year 2008-09. The additional liability arose due to change in exchange rates and is arrived at in conformity with prevailing provisions of AS 11. The exchange rate is US \$ 1 = INR 50.

4. Small Ltd. has omitted to invoice a sale that took place on 31st March, 2011 of goods costing ₹ 2,50,000 at a mark up of 15 per cent instead the goods were considered as part of closing inventory.
5. Closing Inventory of ₹ 45 lakhs of Little Ltd. as on 31st March, 2011 stands undervalued by 10 per cent.
6. Contingent liabilities of Small Ltd. and Little Ltd. as on 31st March, 2011 stands at ₹ 5 lakhs and ₹ 10 lakhs respectively.

The terms of the share issue are as under:

- (i) Shares in Big Ltd. will be issued at a premium of ₹ 13 per share for all external shareholders of Small Ltd. The Premium will be ₹ 15 per share for shares in Big Ltd. issued to all external shareholders of Little Ltd.
- (ii) No shares in Big Ltd. will be issued in lieu of the investments (intercompany holdings) of both companies. Instead the shares so held shall be transferred to Big Ltd. at the close of the financial year ended 31st March, 2012 at Par Value consideration payable on date of transfer.
- (iii) Big Ltd. would in addition to the issue of shares to outside shareholders of Small Ltd. and Little Ltd. make a preferential allotment on 31st March, 2012 of 2 lakhs ordinary shares at a premium of ₹ 28 per share to Virgin Capital Ltd. (VCL). These shares will not be eligible for any dividends declared or paid till that date.
- (iv) Big Ltd. will go in for a 18 per cent unsecured Bank overdraft facility to meet incorporation costs of ₹ 16 lakhs and towards management expenses till 31st March, 2012 estimated at ₹ 14 lakhs. The overdraft is expected to be availed on 1st February, 2012 and closed on 31st March, 2012 out of the proceeds of the preferential allotment.
- (v) It is agreed that interim dividends will be paid on 31.03.2012 for the period January, 2012 to March, 2012 by Big Ltd. at 2 per cent; Small Ltd. at 3 per cent and Little Ltd. at 2.5 per cent. Ignore Dividend Distribution tax.
- (vi) The prevailing Income Tax Rate is 25 per cent.

You are required to compute the number of shares to be issued to the shareholders of each of the companies and prepare the projected Profit and Loss Account for the period from 1st January, 2012 to 31.03.2012 of Big Ltd. and its Balance Sheet as on 31st March, 2012.

Answer

Computation of number of shares issued

Calculation of Rectified Profits and Purchase consideration

	₹	₹
Small Ltd.		
Given profits		50,00,000

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Less: Irrecoverable Debtors	1,00,000	
50% Contingent Liability	<u>2,50,000</u>	<u>(3,50,000)</u>
		46,50,000
Add: Profit on omitted sale (15% of ₹ 2,50,000)		<u>37,500</u>
		46,87,500
Less: Debenture interest		<u>(2,00,000)</u>
		44,87,500
Less: Income Tax @ 25%		<u>(11,21,875)</u>
Profits after Tax (PAT)		33,65,625
Less: Preference Dividend (10% of ₹ 2,00,00,000)		<u>(20,00,000)</u>
Rectified Profits		<u>13,65,625</u>
Average PE ratio = 10		
Total consideration for all equity shareholders (Average PE ratio × Profit)		1,36,56,250
Less: 10% thereof for shareholders of Little Ltd.		<u>(13,65,625)</u>
Balance available for other shareholders of Small Ltd.		<u>1,22,90,625</u>
Little Ltd.		
Given profits		25,00,000
Less: Increase in FOREX liability (US\$10,000 × 50)	5,00,000	
50% Contingent Liability	<u>5,00,000</u>	<u>(10,00,000)</u>
		15,00,000
Add: Undervaluation of inventory (45,00,000 × 10/90)		<u>5,00,000</u>
		20,00,000
Less: Debenture interest		<u>(2,00,000)</u>
		18,00,000
Less: Income Tax @ 25%		<u>(4,50,000)</u>
Profits after Tax (PAT)		13,50,000
Less: Preference Dividend (10% of ₹ 20,00,000)		<u>(2,00,000)</u>
Rectified Profits		<u>11,50,000</u>
Average PE ratio = 8		
Total consideration for all equity shareholders (Average PE ratio × Profit)		92,00,000
Less: 10% thereof for shareholders of Small Ltd.		<u>(9,20,000)</u>
Balance available for other shareholders of Little Ltd.		<u>82,80,000</u>
<i>Statement showing Disposal of Purchase Consideration</i>		

	Small Ltd. ₹	Little Ltd. ₹	Total ₹
Number of shares [Purchase consideration/(Face Value + Securities Premium)]	<u>5,34,375</u>	<u>3,31,200</u>	<u>8,65,575</u>
Share Capital	53,43,750	33,12,000	86,55,750
Securities Premium	<u>69,46,875</u>	<u>49,68,000</u>	<u>1,19,14,875</u>
Purchase Consideration	<u>1,22,90,625</u>	<u>82,80,000</u>	<u>2,05,70,625</u>

**Projected Profit and Loss Account of Big Ltd.
for the period 1st January, 2012 to 31st March, 2012**

	Note No.	₹
I. Revenue from operations		—
II. Other income	5	<u>17,00,000</u>
III. Total Revenue(I+II)		<u>17,00,000</u>
IV. Expenses:		
Employee benefits expense	7	14,00,000
Finance costs	6	90,000
Other expenses	8	<u>16,00,000</u>
V. Total expenses		<u>30,90,000</u>
VI. Loss for the period (V - IV)		(13,90,000)

**Projected Balance Sheet of Big Ltd.
as on 31st March, 2012**

Particulars	Note No.	(₹ in Lacs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1,06,55,750
(b) Reserves and Surplus	2	1,59,51,760
Total		<u>2,66,07,510</u>
II. Assets		
(1) Non-current assets		
Non-current investments	3	2,65,70,625
(2) Current assets		
Cash and cash equivalents	4	36,885
Total		<u>2,66,07,510</u>

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Notes to Accounts

		(₹)	(₹)
1.	Share Capital		
	<i>Authorised</i>		
	20 lakhs shares of ₹ 10 each	<u>2,00,00,000</u>	
	<i>Issued & Paid up</i>		
	10,65,575 shares of ₹ 10 each (out of the	1,06,55,750	
	above 8,65,575 shares have been issued for		1,06,55,750
	consideration other than cash)		
2.	Reserves and surplus		
	Securities Premium (₹ 1,19,14,875 + 56,00,000)		1,75,14,875
	Loss for the period	(13,90,000)	
	Less: Proposed Dividend (2% of ₹ 86,55,750)	<u>(1,73,115)</u>	<u>(15,63,115)</u>
	Balance of Profit and Loss Account carried forward		<u>1,59,51,760</u>
3.	Non-current investments		
	Shares in Subsidiaries (W.N. 4)		2,65,70,625
4.	Cash and cash equivalents		
	Cash at Bank (W.N. 3)		36,885
5.	Other income		
	Dividends received from Subsidiaries (₹ 12,00,000		
	+ 5,00,000)		17,00,000
6.	Finance costs		
	Interest on Bank O/D		90,000
7.	Employee benefits expenses		
	Management expenses		14,00,000
8.	Other expenses		
	Preliminary expenses*		16,00,000

Working Notes:

1. Shares issued by Big Ltd. to Virgin capital Ltd. (VCL)

Number of shares issued	2,00,000
Face Value of Share Capital @ ₹ 10 each	₹ 20,00,000
Securities Premium @ ₹ 28 each	₹ <u>56,00,000</u>
Total cash received from VCL	₹ <u>76,00,000</u>

* As per para 56 of AS 26, 'Intangible Assets', preliminary expenses are to be recognized as expenses as and when they are incurred.

2. Overdraft of Big Ltd. as on 31.3.2012

	₹
Towards Incorporation expenses i.e. preliminary expenses	16,00,000
Towards Management expenses	<u>14,00,000</u>
Total Bank Overdraft availed	<u>30,00,000</u>
Interest @ 18% p.a. for 2 months	<u>90,000</u>

3. Bank balance of Big Ltd. as on 31.3.2012**Bank Account of Big Ltd.**

		₹			₹
01.02.2012	To Overdraft	30,00,000	01.02.2012	By Incorporation expenses	16,00,000
31.03.2012	To VCL	76,00,000	31.03.2012	By Management expenses	14,00,000
31.03.2012	To Dividend		31.03.2012	By Interest on Overdraft	90,000
	Small	12,00,000 ¹	31.03.2012	By Overdraft	30,00,000
	Little	5,00,000 ²	31.03.2012	By Dividend paid	1,73,115 ³
			31.03.2012	By Shares in Small Ltd. bought from Little Ltd.	40,00,000
			31.03.2012	By Shares in Little Ltd. bought from Small Ltd.	20,00,000
				By Balance c/d (Bal.fig.)	<u>36,885</u>
		<u>1,23,00,000</u>			<u>1,23,00,000</u>

4. Investments of Big Ltd. in Projected Balance Sheet

	₹
Purchase consideration paid for acquiring shares of outside holders of- Small Ltd Little Ltd.	1,22,90,625 82,80,000
Consideration paid in cash for acquiring cross holdings From Small Ltd. (shares of Little Ltd.) From Little Ltd. (shares of Small Ltd.)	20,00,000 <u>40,00,000</u>
	<u>2,65,70,625</u>

¹ (40,00,000 x 10) x 3% = 12,00,000.² (20,00,000 x 10) x 2.5% = 5,00,000.³ [(5,34,375 + 3,31,200) x 10] x 2% = 1,73,115.

4.88 Financial Reporting

Question 21

Dawn Ltd. was incorporated to take over Arun Ltd., Brown Ltd. and Crown Ltd. Summarised Balance Sheets of all the three companies as on 31.03.2012 are as follows:

(₹ '000)

Particulars	Arun Ltd.	Brown Ltd.	Crown Ltd.
Liabilities :			
Equity Share Capital (Share of ₹ 10 each)	1,800	2,100	900
Reserves	300	150	300
10 % Debentures	600	---	300
Other Liabilities	<u>600</u>	<u>450</u>	<u>300</u>
Total	<u>3,300</u>	<u>2,700</u>	<u>1,800</u>

(₹ '000)

Particulars	Arun Ltd.	Brown Ltd.	Crown Ltd.
Assets :			
Net Tangible Block	2,400	1,800	1,500
Goodwill	-	150	-
Other Assets	<u>900</u>	<u>750</u>	<u>300</u>
Total	<u>3,300</u>	<u>2,700</u>	<u>1,800</u>

From the following information you are to:

- Work out the number of Equity shares and Debentures to be issued to the shareholders of each company.
- Prepare the Balance Sheet of Dawn Ltd. as on 31.03.2012.

Information:

- Assets are to be revalued and the revalued amount of Tangible Block and other Assets are as follows:

	Tangible Block	Other Assets
Arun Ltd.	₹ 30,00,000	₹ 10,50,000
Brown Ltd.	₹ 15,00,000	₹ 4,20,000
Crown Ltd.	₹ 18,00,000	₹ 2,40,000

- Normal profit on capital employed is to be taken at 10%

(iii) Average amount of profit for three years before charging interest on Debentures are:

Arun Ltd.	₹ 5,40,000
Brown Ltd.	₹ 4,32,000
Crown Ltd.	₹ 3,12,000

(iv) Goodwill is to be calculated at three years' purchase of average super profits for three years, such average is to be calculated after adjustment of 10% depreciation on Increase / Decrease on revaluation of Fixed Assets (Tangible Block).

(v) Capital employed being considered on the basis of net revaluation of Tangible Assets.

(vi) Equity Shares of ₹ 10 each fully paid up in Dawn Ltd. are to be distributed in the ratio of average profit after adjustment of depreciation on revaluation of Tangible Block.

(vii) 10% Debentures of ₹ 100 each fully paid up are to be issued by Dawn Ltd. for the balance due.

(viii) The ratio of issue of Equity shares and debentures of Dawn Ltd. are to be maintained at 3:1, towards the take over companies.

(ix) The amount required for preliminary expenses of ₹ 1,50,000 and for payment to existing Debenture holders, were provided by issuing Equity shares of ₹ 10 each in Dawn Ltd.

Answer

(a) Number of Equity shares and Debentures to be issued to the shareholders of each company

	Arun Ltd. ₹	Brown Ltd. ₹	Crown Ltd. ₹	Total paid by Dawn Ltd. in 3:1 ₹
Equity shares of ₹ 10 each in the ratio of adjusted profits (420:462:252)	20,65,000	22,71,500	12,39,000	55,75,500
10% Debentures [Balance of purchase consideration] – Refer W.N. 2	<u>11,90,000</u>	<u>1,43,500</u>	<u>5,25,000</u>	<u>18,58,500</u>
	<u>32,55,000</u>	<u>24,15,000</u>	<u>17,64,000</u>	<u>74,34,000</u>
No. of shares of ₹ 10 each	2,06,500	2,27,150	1,23,900	5,57,550
10% Debentures of ₹ 100 each in numbers	11,900	1,435	5,250	18,585

(b) Balance Sheet of Dawn Ltd. as at 31.3.2012

Particulars	Note No.	₹
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	66,25,500
(b) Reserves and Surplus	2	(1,50,000)
(2) Non-Current Liabilities		
Long-term borrowings	3	18,58,500
(3) Current Liabilities		13,50,000
Total		96,84,000
II. Assets		
(1) Non-current assets		
Fixed assets		
(a) Tangible assets	4	63,00,000
(b) Intangible assets		16,74,000
(2) Current assets		17,10,000
Total		96,84,000

Notes to Accounts

	(₹)
1. Share Capital	
Equity share capital (W.N.2)	
6,62,550 shares of ₹ 10 each, fully paid up (Including 5,57,550 shares of ₹ 10 each issued for consideration other than cash)	66,25,500
2. Reserves & Surplus	
Profit or loss A/c (Loss)*	(1,50,000)
3. Long Term Borrowings	
Secured	
18,585,10% Debentures of ₹100 each	18,58,500
4. Intangible assets	
Goodwill (W.N.1)	16,74,000

* As per para 56 of AS 26 "Intangible Assets", preliminary expenses are to be recognized as expenses as and when they are incurred.

Working Notes:**1. Computation of Goodwill**

	<i>Arun Ltd.</i>	<i>Brown Ltd.</i>	<i>Crown Ltd.</i>	<i>Total</i>
	₹	₹	₹	₹
Profit	5,40,000	4,32,000	3,12,000	12,84,000
Debenture Interest	<u>(60,000)</u>	<u>-</u>	<u>(30,000)</u>	<u>(90,000)</u>
Profit after Debenture Interest	4,80,000	4,32,000	2,82,000	11,94,000
Adjustment for increase/decrease in depreciation due to revaluation	<u>(60,000)</u>	<u>30,000</u>	<u>(30,000)</u>	<u>(60,000)</u>
	4,20,000	4,62,000	2,52,000	11,34,000
Less: Normal Profit @ 10% on Capital employed as per Working Note 2	<u>(2,85,000)</u>	<u>(1,47,000)</u>	<u>(1,44,000)</u>	<u>(5,76,000)</u>
Super Profits	<u>1,35,000</u>	<u>3,15,000</u>	<u>1,08,000</u>	<u>5,58,000</u>
Goodwill on 3 years of super profits	<u>4,05,000</u>	<u>9,45,000</u>	<u>3,24,000</u>	<u>16,74,000</u>

2. Statement showing calculation of Capital Employed and Purchase Consideration

	<i>Arun Ltd.</i>	<i>Brown Ltd.</i>	<i>Crown Ltd.</i>	<i>Total</i>
	₹	₹	₹	₹
Fixed Assets	30,00,000	15,00,000	18,00,000	63,00,000
Current Assets	<u>10,50,000</u>	<u>4,20,000</u>	<u>2,40,000</u>	<u>17,10,000</u>
	40,50,000	19,20,000	20,40,000	80,10,000
Less: Debentures	<u>(6,00,000)</u>	<u>---</u>	<u>(3,00,000)</u>	<u>(9,00,000)</u>
Current Liabilities	<u>(6,00,000)</u>	<u>(4,50,000)</u>	<u>(3,00,000)</u>	<u>(13,50,000)</u>
Capital Employed	28,50,000	14,70,000	14,40,000	57,60,000
Goodwill as per (i)	<u>4,05,000</u>	<u>9,45,000</u>	<u>3,24,000</u>	<u>16,74,000</u>
Purchase consideration	<u>32,55,000</u>	<u>24,15,000</u>	<u>17,64,000</u>	<u>74,34,000</u>

3. Total number of equity shares issued*Equity Shares*

For purchase consideration	5,57,500
preliminary expenses (₹ 1,50,000 / ₹ 10)	15,000
payment of existing debenture holders (₹ 6,00,000 + ₹ 3,00,000) / ₹ 10	<u>90,000</u>
	<u>6,62,500</u>

4.92 Financial Reporting

Question 22

The following are the summarized Balance Sheets of H Ltd. and S Ltd. as at 31.03.12:

	H Ltd. (₹)	S Ltd. (₹)		₹ in lakhs	
				H Ltd. (₹)	S Ltd. (₹)
Share capital			Fixed assets	60	18
Share of ₹ 10 each	50	10	Investment in S Ltd. (60,000 shares)	6	-
General reserve	50	20	Debtors	35	5
Profit and Loss	20	15	Inventories	30	25
Secured loan	20	3	Cash at Bank	39	2
Current liabilities	<u>30</u>	<u>2</u>			
	<u>170</u>	<u>50</u>		<u>170</u>	<u>50</u>

H Ltd. holds 60% of the paid up capital of S Ltd. and balance is held by a foreign company. The foreign company agreed with H Ltd. as under:

- The shares held by the foreign company will be sold to H Ltd. at ₹ 50 above than nominal value of per share.
- The actual cost per share to the Foreign Company was ₹ 11, gain accruing to Foreign Company is taxable @ 20%. The tax payable will be deducted from the sale proceeds and paid to Government by H Ltd. 50% of the consideration (after payment of tax) will be remitted to Foreign Company by H Ltd. and also any cash for fractional shares allotted.
- For the Balance of consideration H Ltd. would issue its shares at their intrinsic value.

It was also decided that H Ltd. would also absorb S Ltd. simultaneously by writing down the fixed assets of S Ltd. by 10%. The Balance Sheet figure included a sum of ₹ 1 lakh due by S Ltd. to H Ltd, included stock of ₹ 1.5 lakhs purchased from S Ltd. who sold them at cost plus 20%.

Pass Journal entries in the books of H Ltd. to record the above arrangement on 31.03.12 and prepare the Balance Sheet of H Ltd. after absorption of S Ltd. Workings should form part of your answer

Answer

Journal Entries in the books of H Ltd.

			₹	₹
1.	Business Purchase A/c To Foreign Company (Being business purchased)	Dr.	24,00,000	24,00,000
2.	Fixed Assets A/c	Dr.	16,20,000	
	Debtors A/c	Dr.	5,00,000	

	Inventories A/c	Dr.	25,00,000	
	Cash at Bank A/c	Dr.	2,00,000	
	To Current Liabilities A/c			2,00,000
	To Secured Loan A/c			3,00,000
	To Investment in S Ltd. A/c			6,00,000
	To Business Purchase A/c			24,00,000
	To Capital Reserve A/c (B.F.)			13,20,000
	(Being various assets and liabilities taken over)			
3.	Profit and Loss A/c	Dr.	25,000	
	To Inventories A/c			25,000
	(Being elimination of unrealized profit)			
4.	Current Liabilities A/c	Dr.	1,00,000	
	To Debtors A/c			1,00,000
	(Being elimination of mutual owing)			
5.	Foreign Company	Dr.	24,00,000	
	To Tax Payable A/c			3,92,000
	To Bank A/c (₹ 10,04,000 + ₹ 20)			10,04,020*
	To Equity Share Capital A/c			3,34,660
	To Securities Premium A/c			6,69,320
	(Being payment made to foreign company)			
6.	Tax Payable A/c	Dr.	3,92,000	
	To Bank A/c			3,92,000
	(Being tax paid to Government)			

Balance Sheet of H Ltd. (After Absorption)

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	53,34,660
(b) Reserves and Surplus	2	89,64,320
(2) Non-Current Liabilities		
Long-term borrowings	3	23,00,000
(3) Current Liabilities ₹ (30,00,000+2,00,000-1,00,000)		31,00,000
Total		1,96,98,980

* It is assumed that payment of fractional shares has also been routed through Bank A/c along with 50% payment remitted to Foreign Company.

4.94 Financial Reporting

II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	4	76,20,000
(2) Current assets		
(a) Inventories (₹ 30,00,000-₹ 25,000+₹ 25,00,000)		54,75,000
(b) Trade receivables		39,00,000
(₹ 35,00,000 – ₹ 1,00,000 + ₹ 5,00,000)		
(c) Cash and cash equivalents	5	27,03,980
Total		1,96,98,980

Notes to Accounts

		(₹)	(₹)
1.	Share Capital		
	5,34,466 Shares of ₹ 10 each (out of above, 33,466 shares issued for consideration other than cash)		53,34,660
2.	Reserves and surplus		
	General Reserve	50,00,000	
	Profit & Loss (₹ 20,00,000 – ₹ 25,000)	19,75,000	
	Capital Reserve	13,20,000	
	Securities Premium	<u>6,69,320</u>	89,64,320
3.	Long Term Borrowings		
	Secured Loan (₹ 20,00,000+₹ 3,00,000)		23,00,000
4.	Tangible Assets		
	Fixed Assets (₹ 60,00,000+₹ 16,20,000)		76,20,000
5.	Cash and cash equivalents		
	Cash at Bank (₹ 39,00,000 + ₹ 2,00,000 – ₹ 10,04,020 – ₹ 3,92,000)		27,03,980

Working Notes:

1. Amount payable to foreign company

Price per share of S Ltd. = ₹ 50 + ₹ 10 (Nominal value) = ₹ 60

Value of 40% shares held by foreign company = $10,00,000 \times 40\% \times \frac{60}{10} = ₹ 24,00,000$

Capital gain = ₹ 24,00,000 – $\frac{24,00,000}{10} \times \frac{11}{10} = ₹ 19,60,000$

Tax on capital gain = ₹ 19,60,000 × 20% = ₹ 3,92,000

Amount payable to Foreign Company after tax = ₹ 24,00,000 – ₹ 3,92,000
= ₹ 20,08,000

50% of ₹ 20,08,000 = ₹ 10,04,000 to be remitted to foreign company.

2. Intrinsic value of shares of H Ltd. and balance payment to foreign company

	₹	₹
Total assets (Excluding Investment in S Ltd.)		1,64,00,000
Add: Investment in S Ltd. (60,000 shares × ₹ 60)		<u>36,00,000</u>
		2,00,00,000
Less: Liabilities:		
Secured Loan	20,00,000	
Current Liability	<u>30,00,000</u>	<u>(50,00,000)</u>
		<u>1,50,00,000</u>
No. of equity shares		5,00,000
Intrinsic value per share		₹ 30

Number of shares to be issued for payment of 50% balance amount
 $\frac{₹ 10,04,000}{30} = 33,466$ shares

Cash for fractional shares = ₹ 10,04,000 – (33,466 × ₹ 30) = ₹ 20

Question 23

The following are the summarized Balance Sheets of Cat Ltd. and Bat Ltd. as on 31.3.2012:

Liabilities	(₹ in thousands)	
	Cat Ltd.	Bat Ltd.
Share capital:		
Equity shares of 100 each fully paid up	2,000	1,000
Reserves	800	---
10% Debentures	500	---
Loans from Banks	250	450
Bank overdrafts	---	50
Sundry creditors	300	300
Proposed dividend	<u>200</u>	<u>---</u>
Total	<u>4,050</u>	<u>1,800</u>

4.96 Financial Reporting

Assets		
Tangible assets/fixed assets	2,700	850
Investments (including investments in Bat Ltd.)	700	---
Sundry debtors	400	150
Cash at bank	250	---
Accumulated loss	---	800
Total	<u>4,050</u>	<u>1,800</u>

Bat Ltd. has acquired the business of Cat Ltd. The following scheme of merger was approved:

- Banks agreed to waive off the loan of ₹ 60 thousands of Bat Ltd.
- Bat Ltd. will reduce its shares to ₹10 per share and then consolidate 10 such shares into one share of ₹100 each (new share).
- Shareholders of Cat Ltd. will be given one share (new) of Bat Ltd. in exchange of every share held in Cat Ltd.
- Proposed dividend of Cat Ltd. will be paid after merger to shareholders of Cat Ltd.
- Sundry creditors of Bat Ltd. includes ₹ 100 thousands payable to Cat Ltd.
- Cat Ltd. will cancel 20% holding in Bat Ltd. as investment, which was held at a cost of ₹ 250 thousands.

Pass necessary entries in the books of Bat Ltd. and prepare Balance Sheet after merger.

Answer

Calculation of purchase consideration

	Shares
One share of Bat Ltd. will be issued in exchange of every share of Cat Ltd. (i.e. 20,000 equity shares of Bat Ltd will be issued against 20,000 equity shares of Cat Ltd.)	20,000
Less: Shares already held (20% of 10,000) 2,000 shares converted in new equity shares	<u>(200)</u>
Number of shares to be issued by Bat Ltd to shareholders of Cat Ltd.	19,800

Journal Entries in the books of Bat Ltd.

Date		(₹ in thousands)	
2012		Dr.	Cr.
March,31	Loan from bank A/c Dr.	60	
	To Reconstruction A/c		60
	(Being loan from bank waived off to the extent of ₹ 60 thousand)		

Equity share capital A/c (₹100) Dr.	1,000	
To Equity share capital A/c (₹10)		100
To Reconstruction A/c		900
(Being Equity share of ₹ 100 each reduced to ₹10 each)		
Equity share capital A/c (₹10) Dr.	100	
To Equity share capital A/c (₹100 each)		100
(Being 10 Equity shares of ₹ 10 each consolidated to one share of ₹100 each)		
Reconstruction A/c Dr.	960	
To Profit and loss A/c		800
To Capital reserve A/c		160
(Being accumulated losses set off against reconstruction A/c and balance transferred to capital reserve account)		
Business purchase A/c Dr.	1,980	
To Liquidator of Cat Ltd.		1,980
(Being purchase of business of Cat Ltd.)		
Fixed asset A/c Dr.	2,700	
Investment A/c ₹ (700 – 250) Dr.	450	
Sundry debtors A/c Dr.	400	
Cash at bank A/c Dr.	250	
To Sundry creditors A/c		300
To Proposed dividend A/c		200
To Loans from bank A/c		250
To 10% Debenture A/c		500
To Business purchase A/c		1,980
To Reserves A/c ₹ (800 – 230)		570
(Being assets, liabilities and reserves taken over under pooling of interest method)		
Liquidator of Cat Ltd. A/c Dr.	1,980	
To Equity share capital A/c		1,980
(Being payment made to liquidators of Cat Ltd. by allotment of 19,800 new equity shares))		

4.98 Financial Reporting

Sundry creditors A/c	Dr.	100	
To Sundry debtors A/c			100
(Being mutual owing cancelled)			
Proposed dividend A/c	Dr.	200	
To Bank A/c			200
(Being dividend paid off)			

Balance Sheet of Bat Ltd. after merger as on 31.3.2012

Particulars	Note No.	(₹ in thousands)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	2,080
(b) Reserves and Surplus	2	730
(2) Non-Current Liabilities		
Long-term borrowings	3	1,140
(3) Current Liabilities		
(a) Trade Payables		500
(b) Other current liabilities	4	50
Total		4,500
II. Assets		
(1) Non-current assets		
(a) Fixed assets		3,550
(b) Non-current investments		450
(2) Current assets		
(a) Trade receivables		450
(b) Cash and cash equivalents	5	50
Total		4,500

Notes to Accounts

		(₹ in thousands)	(₹ in thousands)
1.	Share Capital		
	Equity shares of 100 each fully paid		
	Out of the above, 19,800 shares have been issued for consideration other than cash)		2,080

2.	Reserves and Surplus		
	Capital reserve	160	
	General reserve	<u>570</u>	730
3.	Long Term Borrowings		
	Secured		
	10% Debentures	500	
	Loan from bank (₹ 250 + ₹450 – ₹ 60)	<u>640</u>	1140
4.	Other current liabilities		
	Bank overdraft		50
5.	Cash and cash equivalents		
	Cash at Bank (₹ 250 – ₹ 200)		50

Question 24

The following are the summarized Balance Sheets of X Ltd. and Y Ltd. as on 31st March, 2012:

Amount in ₹		
	X Ltd.	Y Ltd.
Assets		
Fixed Assets	7,00,000	2,50,000
Stock	2,40,000	3,20,000
Debtors	3,60,000	1,90,000
Bills Receivable	60,000	20,000
Cash at Bank	1,10,000	40,000
Investments in :		
6,000 shares of Y Ltd.	80,000	
5,000 shares of X Ltd.		<u>80,000</u>
	<u>15,50,000</u>	<u>9,00,000</u>
Liabilities		
Share Capital:		
Equity shares of ₹ 10 each	6,00,000	3,00,000
10% preference shares of ₹ 10 each	2,00,000	1,00,000
Reserve and Surplus	3,00,000	2,00,000
12% Debentures	2,00,000	1,50,000
Sundry Creditors	2,20,000	1,25,000
Bills payable	<u>30,000</u>	<u>25,000</u>
	<u>15,50,000</u>	<u>9,00,000</u>

4.100 Financial Reporting

Fixed assets of both the companies are to be revalued at 15% above book values and stock and debtors are to be taken over at 5% less than their book values. Both the companies are to pay 10% equity dividends, preference dividends having been paid already.

After the above transactions are given effect to, X Ltd. will absorb Y Ltd. on the following terms:

- (i) 8 equity shares of ₹10 each will be issued by X Ltd. at par against 6 shares of Y Ltd.
- (ii) 10% preference shares of Y Ltd. will be paid off at 10% discount by issue of 10% preference shares of ₹100 each of X Ltd. at par.
- (iii) 12% Debentureholders of Y Ltd. are to be paid off at a 8% premium by 12% debentures in X Ltd. issued at a discount of 10%.
- (iv) ₹30,000 to be paid by X Ltd. to Y Ltd. for liquidation expenses.
- (v) Sundry creditors of Y Ltd. include ₹10,000 due to X Ltd.

Prepare:

- (a) A statement of purchase consideration payable by X Ltd.
- (b) A Balance Sheet of X Ltd. after its absorption of Y Ltd.

Answer

- (a) Statement of Purchase Consideration payable by X Ltd.

- (i) 8 Equity Shares of X Ltd. for every 6 Equity Shares of Y Ltd.

	$30,000 \text{ shares} \times \frac{8}{6} =$	40,000 shares
Less: 1/5 already held by X Ltd. of Y Ltd.		<u>(8,000) shares</u>
		32,000 shares
Less: 5,000 Shares of X Ltd. with Y Ltd.		<u>(5,000) shares</u>
		<u>27,000 shares</u>
27,000 equity shares at ₹ 10		₹ 2,70,000

- (ii) Payment of 10% Preference Shares at 10% discount by issue of 10% Preference Shares of X Ltd. of ₹ 100 each

$(1,00,000 \times \frac{90}{100})$	₹ 90,000
	<u>₹ 3,60,000*</u>

*Reimbursement of liquidation expenses by X Ltd. to Y Ltd. has not been considered as part of purchase consideration. Alternatively, this can be included in computation of purchase consideration.

(b) Balance Sheet of X Ltd. after its absorption of Y Ltd.

Particulars	Note No.	₹
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	11,60,000
(b) Reserves and Surplus	2	3,76,000
(2) Non-Current Liabilities		
Long-term borrowings	3	3,80,000
(3) Current Liabilities		
Trade payables	4	3,90,000
Total		23,06,000
II. Assets		
(1) Non-current assets		
(a) Fixed assets		10,92,500
(b) Other non-current assets	5	18,000
(2) Current assets		
(a) Inventories		5,44,000
(b) Trade receivables	6	6,10,500
(c) Cash and cash equivalents	7	41,000
Total		23,06,000

Notes to Accounts

		₹	₹
1.	Share Capital		
	Equity share capital		
	87,000 Equity shares of ₹10 each, fully paid up		
	Out of the above, 27,000 equity shares have been issued for consideration other than cash)	8,70,000	
	10% Preference shares of ₹10 each	2,00,000	
	10% Preference shares of ₹100 each	90,000	11,60,000
2.	Reserves and Surplus		
	Revaluation Reserve	1,05,000	
	Capital Reserve (15% of ₹ 7,00,000) (W. N.1)	25,000	
	Other Reserves (W.N.4)	2,46,000	3,76,000

4.102 Financial Reporting

3.	Long Term Borrowings Secured (assumed) 12% Debentures $\frac{₹ 2,00,000 + ₹ 1,62,000}{90\%}$		3,80,000
4.	Trade payables Sundry Creditors (₹ 2,20,000 + ₹ 1,25,000 – ₹ 10,000) Bills payable (₹ 30,000 + ₹ 25,000)	3,35,000 55,000	3,90,000
5.	Other non-current assets Discount on issue of Debentures [₹ 1,50,000 x 108% x (10/90)]		18,000
6.	Trade receivables Debtors (₹ 3,60,000 + ₹ 1,80,500 – ₹ 10,000) Bills receivable (₹ 60,000 + ₹ 20,000)	5,30,500 80,000	6,10,500
7.	Cash & cash equivalents Cash at Bank (W.N. 3)		41,000

Working Notes:

1. Calculation of Capital Reserve

Net Assets taken over from Y Ltd.	₹
Fixed Assets (₹ 2,50,000 × 115%)	2,87,500
Stock (₹ 3,20,000 × 95%)	3,04,000
Debtors (₹ 1,90,000 × 95%)	1,80,500
Bills Receivable	20,000
Cash at Bank	<u>15,000</u>
Total Assets (A)	<u>8,07,000</u>
Liabilities taken over:	
Debentures (₹ 1,50,000 × 108%)	1,62,000
Sundry Creditors	1,25,000
Bills Payable	<u>25,000</u>
Total Liabilities (B)	<u>3,12,000</u>
Net Asset taken over (A – B)	4,95,000
Less: Investment cancelled	<u>(80,000)</u>

	4,15,000
Purchase Consideration	<u>(3,60,000*)</u>
Capital Reserve	55,000
Less: Liquidation expenses reimbursed to Y Ltd.	<u>(30,000*)</u>
	<u>25,000</u>

2. Cash taken over from Y Ltd.

	₹
Cash balance given in Balance Sheet of Y Ltd.	40,000
Add: Dividend received from X Ltd.	<u>5,000</u>
	45,000
Less: Dividend paid	<u>(30,000)</u>
	<u>15,000</u>

3. Cash balance in Balance Sheet (after absorption)

	₹
Cash balance given in Balance Sheet of X Ltd.	1,10,000
Add: Cash taken over from Y Ltd.	<u>15,000</u>
	1,25,000
Less: Dividend paid ₹60,000	
Expenses on liquidation ₹30,000	<u>(90,000)</u>
	35,000
Add: Dividend from Y Ltd.	<u>6,000</u>
	<u>41,000</u>

4. Other Reserves in the Balance Sheet (after absorption)

	₹
Reserves given in the Balance Sheet of X Ltd.	3,00,000
Add: Dividend from Y Ltd.	<u>6,000</u>
	3,06,000
Less: Dividend declared	<u>(60,000)</u>
	<u>2,46,000</u>

* Reimbursement of liquidation expenses by X Ltd. to Y Ltd. has not been considered as part of purchase consideration. If these expenses are included in computation of purchase consideration, then ₹30,000 will not be deducted.

4.104 Financial Reporting

Question 25

A Ltd. and B Ltd. were amalgamated on and from 1st April, 2012. A new company C Ltd. was formed to take over the business of the existing companies. The summarized Balance Sheets of A Ltd., and B Ltd., as on 31st March, 2012 are given below:

	(₹ in lakhs)			(₹ in lakhs)	
Liabilities	A Ltd.	B Ltd.	Assets	A Ltd.	B Ltd.
Share capital:			Fixed Assets:		
Equity shares of ₹100 each	800	750	Land and Building	550	400
12% Preference shares of ₹ 100 each	300	200	Plant and Machinery	350	250
Reserves and surplus:			Investments:	150	50
Revaluation Reserve	150	100	Current Assets,		
General Reserve	170	150	Loans and Advances:		
Investment Allowance Reserve	50	50	Stock	350	250
Profit & Loss account	50	30	Sundry Debtors	250	300
Secured Loans:			Bills Receivable	50	50
10% Debentures (₹100 each)	60	30	Cash and Bank	300	200
Current Liabilities and Provisions:					
Sundry Creditors	270	120			
Bills Payable	<u>150</u>	<u>70</u>			
	<u>2,000</u>	<u>1,500</u>		<u>2,000</u>	<u>1,500</u>

Additional Information:

- (1) 10% Debentureholders of A Ltd., and B Ltd., are discharged by C Ltd., issuing such number of its 15% Debentures of ₹ 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 ₹ 150 per share (face value of ₹ 100).
- (3) C Ltd., will issue 5 equity shares for each equity share of A Ltd. and 4 equity shares for each share of B Ltd. The shares are to be issued @ ₹ 30 each, having a face value of ₹ 10 per share.
- (4) Investment allowance reserve to be maintained for 4 more years.

Prepare the Balance Sheet of C Ltd., as on 1st April, 2012 after the amalgamation has been carried out on the basis of amalgamation in the nature of purchase.

Answer

Balance Sheet of C Ltd. as on 1st April, 2012

Particulars	Note No.	(₹ in Lacs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1,200
(b) Reserves and Surplus	2	1,750
(2) Non-Current Liabilities		
Long-term borrowings	3	60
(3) Current Liabilities		
Trade payables	4	610
Total		3,620
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible Assets	5	1,550
Intangible Asset	6	20
(b) Non-current investments (₹ 150+ ₹ 50)		200
(c) Other non-current assets	7	100
(2) Current assets		
(a) Inventories		600
(b) Trade receivables	8	650
(c) Cash and cash equivalents	9	500
Total		3,620

Notes to Accounts

		₹	₹
1.	Share Capital		
	Equity share capital		
	70,00,000, Equity Shares of 10 each (W.N. 4)	700	
	5,00,000, 15% Preference Shares of ₹ 100 each (all the above shares are allotted for consideration other than cash) (V.N.U)	<u>500</u>	1,200

4.106 Financial Reporting

2.	Reserves and Surplus		
	Securities Premium Account (W.N.4)	1,650	
	Investment allowance reserve (₹50+₹ 50)	<u>100</u>	1,750
3.	Long Term Borrowings		
	Secured:		
	15% Debentures (₹40+₹ 20) (W.N.5)		60
4.	Trade payables		
	Sundry Creditors (₹270+₹ 120)	390	
	Bills payable (₹150+₹ 70)	<u>220</u>	610
5.	Tangible Assets		
	Land and Building (₹550+₹400)	950	
	Plant and Machinery (₹350+₹ 250)	<u>600</u>	1,550
6.	Intangible Asset		
	Goodwill (W.N. 3)		20
7.	Other non-current asset		
	Amalgamation Adjustment Account		100
8.	Trade receivables		
	Sundry Debtors (₹250+₹ 300)	550	
	Bills Receivable (₹ 50+ ₹ 50)	<u>100</u>	650
9.	Cash & cash equivalents		
	Cash and Bank (₹300+₹ 200)		500

Working Notes:

1. Computation of Purchase Consideration

	(₹ in lakhs)	
	A Ltd.	B Ltd.
(a) Preference Shareholders		
(3,00,00,000÷100) ie. 3,00,000 Shares x ₹ 150 each	450	
(2,00,00,000 ÷100) ie 2,00,000 Shares x ₹ 150 each		300
(b) Equity Shareholders:		
[(8,00,00,000÷100) x 5] ie 40,00,000 Shares x ₹ 30 each	1,200	
[(7,50,00,000 ÷100) x 4] ie. 30,00,000 Shares x ₹ 30 each		<u>900</u>
Amount of purchase consideration	<u>1,650</u>	<u>1,200</u>

2. Net Assets taken over

	₹ in lakhs			
	A Ltd.		B Ltd.	
Assets taken over:				
Land and Building		550		400
Plant and Machinery		350		250
Investments		150		50
Stock		350		250
Sundry Debtors		250		300
Bills Receivable		50		50
Cash and Bank		<u>300</u>		<u>200</u>
		2,000		1,500
Less: Liabilities taken over				
Debentures	40		20	
Sundry Creditors	270		120	
Bills Payable	<u>150</u>	<u>(460)</u>	<u>70</u>	<u>(210)</u>
Net Assets taken over		<u>1,540</u>		<u>1,290</u>

3. Goodwill / Capital Reserve

	₹ in lakhs	
	A Ltd.	B Ltd.
Purchase Consideration	1,650	1,200
Less: Net Assets taken over	<u>(1,540)</u>	<u>(1,290)</u>
Goodwill	<u>110</u>	-
Capital Reserve	-	<u>(90)</u>
Net Goodwill	₹ 110 – ₹ 90 = ₹ 20	

4. Share Capital / Securities Premium

Particulars	Share Capital		Securities
	Equity	Preference	Premium
	₹ in lakhs	₹ in lakhs	₹ in lakhs
A Ltd.			
Equity shares (8,00,000 shares x 5 x ₹ 10)	400		
Securities premium (8,00,000 shares x 5 x ₹ 20)			800

4.108 Financial Reporting

Preference shares (3,00,000 shares x ₹ 100)		300	
Securities premium (3,00,000 shares x ₹ 50)			150
B Ltd.			
Equity shares (7,50,000 shares x 4 x ₹ 10)	300		
Securities premium (7,50,000 shares x 4 x ₹ 20)			600
Preference shares (2,00,000 shares x ₹ 100)		200	
Securities premium (2,00,000 shares x ₹ 50)			100
	<u>700</u>	<u>500</u>	<u>1,650</u>

5. Debentures

	₹ in lakhs	
	A Ltd.	B Ltd.
Interest on debentures @ 10% = 60 x 10% = ₹6		
Number of 15% debentures to maintain same amount of interest	40	
$\frac{₹6}{₹15} \times 100 = \frac{40}{100}$		
Interest on debentures @ 10% = 30 x 10% = ₹3		
Number of 15% debentures to maintain same amount of interest		20
$\frac{₹3}{₹15} \times 100 = \frac{20}{100}$		

Question 26

A Ltd., agreed to absorb B Ltd., on 31st March 2011, whose summarized Balance Sheet stood as follows:

Liabilities	₹	Assets	₹
Share Capital:		Fixed Assets	7,00,000
80,000 Equity shares of ₹10 each fully paid up	8,00,000	Investments	-
Reserves & Surplus:		Current Assets,	
General Reserve	1,00,000	Loans and Advances:	
Current Liabilities and Provisions :		Stock-in-trade	1,00,000
Sundry Creditors	1,00,000	Sundry Debtors	2,00,000
	<u>10,00,000</u>		<u>10,00,000</u>

The consideration was agreed to be paid as follows:

(a) A payment in cash of ₹5 per share in B Ltd., and

- (b) The issue of shares of ₹ 10 each in A Ltd. on the basis of 2 equity shares (valued at ₹ 15) and one 10% Cumulative Preference shares (valued at ₹ 10) for every five shares held in B Ltd.

The whole of the share capital consists of shareholdings in exact multiple of five except the followings holdings:

A	116
B	76
C	72
D	28
Other individual	8 (each member holding one share each)
	<u>300</u>

It was agreed that A Ltd. will pay in cash for fractional shares equivalent at agreed value of shares in B Ltd., i.e. ₹ 65 for five shares of ₹ 50 paid.

Prepare a statement showing the purchase consideration receivable in shares and cash.

Answer

Purchase Consideration

	₹
31,994 Equity shares @ ₹ 15 each	4,79,910
15,997 Preference shares @ ₹ 10 each	1,59,970
Cash on 79,985 shares (i.e 80,000 – 15) of B Ltd. @ ₹ 5 each	<u>3,99,925</u>
	10,39,805
Add: Cash for fractional shares (W.N. 3)	<u>195</u>
	<u>10,40,000</u>

Working Notes:

- Schedule showing fractional shares

Holding of Shares		Exchangeable in multiple of five	Exchange in Equity shares	Exchange in preference shares	Non exchangeable shares
A	116	115	46	23	1
B	76	75	30	15	1
C	72	70	28	14	2
D	28	25	10	5	3
Others	8	-	-	-	8
	300	285	114	57	15

4.110 Financial Reporting

2. Shares Exchangeable: Equity Shares in A Ltd.

	No. of shares		No. of shares
(i) 80,000 – 300	79,700	2/5 thereof	31,880
(ii) 300 – 15	<u>285</u>	2/5 thereof	<u>114</u>
	<u>79,985</u>		<u>31,994</u>

Shares Exchangeable: Preference Shares in A Ltd.

	No. of shares		No. of shares
(i) 80,000 – 300	79,700	1/5 thereof	15,940
(ii) 300 – 15	<u>285</u>	1/5 thereof	<u>57</u>
	<u>79,985</u>		<u>15,997</u>

3. There are 15 shares (W.N.1) in B Ltd. which are not capable of exchange into equity and preference shares of A Ltd. They will be paid cash = $15 \times 10 \times \frac{65}{50} = 195$.

Exercises

Question 1

The summarized Balance Sheets of A Ltd. and its subsidiary B Ltd. as on 31.3.2012 are as follows:

	A Ltd. ₹	B Ltd. ₹
Shares of ₹ 10 each	1,00,00,000	20,00,000
Reserves and Surplus	1,40,00,000	60,00,000
Secured Loans	40,00,000	-
Current Liabilities	<u>60,00,000</u>	<u>20,00,000</u>
	<u>3,40,00,000</u>	<u>1,00,00,000</u>
Fixed Assets	1,20,00,000	35,00,000
Investment in B Ltd.	7,40,000	-
Sundry Debtors	70,00,000	10,00,000
Inventories	60,00,000	50,00,000
Cash and Bank	<u>82,60,000</u>	<u>5,00,000</u>
	<u>3,40,00,000</u>	<u>1,00,00,000</u>

A Ltd. holds 76% of the paid up capital of B Ltd. The balance shares in B Ltd. are held by a Foreign Collaborating company. A memorandum of understanding has been entered into with the foreign company providing for the following:

- (a) The shares held by the foreign company will be sold to A Ltd. The price per share will be calculated by capitalizing the yield at 16%. Yield, for this purpose, would mean 40% of

the average of pre-tax profits for the last 3 years, which were ₹ 35 lakhs. ₹ 44 lakhs and ₹ 65 lakhs.

- (b) The actual cost of shares to the foreign company was ₹ 2,40,000 only. The profit that would accrue to them would be taxable at an average rate of 30%. The tax payable be deducted from the proceeds and A Ltd. will pay it to the Government.
- (c) Out of the net consideration, 50% would be remitted to the foreign company immediately and the balance will be an unsecured loan repayable after one year. It was also decided that A Ltd. would absorb B Ltd. simultaneously by writing down the Fixed Assets of B Ltd. by 5%. The Balance Sheet figures included a sum of ₹ 1,50,000 due by B Ltd. to A Ltd.

The entire arrangement was approved by all concerned for giving effect to on 1.4.2012.

You are required to show the Balance Sheet of A Ltd. as it would appear after the arrangement is put through on 1.4.2012.

[Answer: Total of the balance sheet of A Ltd. ₹ 410.99 Lakhs; Yield of B Ltd.: ₹ 19.2 lakhs; Price per share of B Ltd. = ₹ 60; Purchase consideration for 24% of share capital of B Ltd. = ₹ 28.80 lakhs; Capital Reserve to A Ltd. ₹ 42.05 lakhs; Cash and bank balance of A Ltd. after acquisition of shares ₹ 69.24 lakhs.

Discharge of Purchase Consideration:

- (i) as Tax : ₹ 7.92 lakhs
- (ii) 50% of (28.80 – 7.92 i.e. ₹ 20.88 lakhs) = ₹ 10.44 lakhs (to be remitted immediately)
- (iii) Balance 50% = ₹ 10.44 lakhs (to be retained as unsecured loan)]

Question 2

Travels & Tours Ltd. has two divisions – 'Inland' and 'International'. The Balance Sheet as at 31st December, 2011 was as under:

	Inland (₹ crores)	International (₹ crores)	Total (₹ crores)
Fixed Assets:			
Cost	600	600	1,200
Depreciation	<u>500</u>	<u>200</u>	<u>700</u>
W.D.V. (written down value) (A)	100	400	500
Net Current Assets:			
Current assets	400	300	700
Less: Current liabilities	<u>200</u>	<u>200</u>	<u>400</u>
(B)	<u>200</u>	<u>100</u>	<u>300</u>
Total (A + B)	<u>300</u>	<u>500</u>	<u>800</u>

4.112 Financial Reporting

Financed by:			
Loan funds:			
(Secured by a charge on fixed assets)	-	100	100
Own Funds:			
Equity capital (fully paid up ₹ 10 shares)			50
Reserves and surplus			<u>650</u>
	<u>?</u>	<u>?</u>	<u>700</u>
Total	<u>300</u>	<u>500</u>	<u>800</u>

It is decided to form a new company 'IT Ltd.' for international tourism to take over the assets and liabilities of international division.

Accordingly 'IT Ltd.' was formed to takeover at Balance Sheet figures the assets and liabilities of international division. 'IT Ltd.' is to allot 5 crores equity shares of ₹ 10 each in the company to the members of 'Travels & Tours Ltd.' in full settlement of the consideration. The members of 'Travels & Tours Ltd.' are therefore to become members of 'IT Ltd.' as well without having to make any further investment.

- You are asked to pass journal entries in relation to the above in the books of 'Travels & Tours Ltd.' and also in 'IT Ltd.'. Also show the Balance Sheets of both the companies as on 1st January, 2012 showing corresponding figures, before the reconstruction also.
- The directors of both the companies ask you to find out the net asset value of equity shares pre and post-demerger.
- Comment on the impact of demerger on "shareholders wealth".

[Answer: Loss on reconstruction ₹ 400 crores, Total of the balance sheet of Travels & Tours Ltd. before and after reconstruction would be ₹ 800 crores and ₹ 300 crores respectively.]

Net Asset Value of an equity share	Pre-Demerger	Post-Demerger
Travels & Tours Ltd.	= ₹ 140	= ₹ 60]

Question 3

System Ltd. and HRD Ltd. decided to amalgamate as on 01.04.2012. Their Balance Sheets as on 31.03.2012 were as follows: (₹ in '000)

Particulars	System Ltd.	HRD Ltd.
Source of Funds :		
Equity share capital (₹ 10 each)	150	140
9% preference share Capital (₹ 100 each)	30	20
Investment allowance Reserve	5	2
Profit and Loss Account	10	6
10 % Debentures	50	30

Sundry Creditors	25	15
Tax provision	7	4
Equity Dividend Proposed	<u>30</u>	<u>28</u>
Total	<u>307</u>	<u>245</u>
Application of Funds :		
Building	60	50
Plant and Machinery	80	70
Investments	40	25
Sundry Debtors	45	35
Stock	36	40
Cash and Bank	40	25
Preliminary Expenses	<u>6</u>	<u>—</u>
Total	<u>307</u>	<u>245</u>

From the following information, you are to prepare the draft Balance Sheet as on 01.04.2012 of a new company, Intranet Ltd., which was formed to take over the business of both the companies and took over all the assets and liabilities:

- 50% Debenture are to be converted into Equity Shares of the New Company.
- Out of the investments, 20% are non-trade investments.
- Fixed Assets of Systems Ltd. were valued at 10% above cost and that of HRD Ltd. at 5% above cost.
- 10 % of sundry Debtors were doubtful for both the companies. Stocks to be carried at cost.
- Preference shareholders were discharged by issuing equal number of 9% preference shares at par.
- Equity shareholders of both the transferor companies are to be discharged by issuing Equity shares of ₹ 10 each of the new company at a premium of ₹ 5 per share.

Amalgamation is in the nature of purchase.

[Answer: Value of equity shares issued to System Ltd. ₹ 1,98,500 and to HRD Ltd. ₹1,78,500]

Cash paid for fraction of shares = ₹ 1,98,500 less ₹ 1,98,495 = ₹ 5 to System Ltd.

Cash paid for fraction of shares = ₹ 25,000 less ₹ 24,990 = ₹ 10 to HRD Ltd.

Total of M/s Intranet balance sheet as at 1.4.2012 ₹ 5,64,985]

Question 4

The Balance Sheet of Munna Ltd as on 31st March, 2012 is as follows:

Liabilities	₹	Assets	₹
Authorised and issued Share capital		Goodwill	2,00,000
20,000 equity shares of ₹ 100 each,	20,00,000	Plant & Machinery	18,00,000

4.114 Financial Reporting

fully paid 10,000, 7% Preference shares of ₹ 100 each	10,00,000	Stock	3,00,000
Sundry creditors	7,00,000	Debtors	7,50,000
Bank overdraft	3,00,000	Cash	1,50,000
		Preliminary expenses	1,00,000
		Profit and Loss Account	7,00,000
	40,00,000		40,00,000

Additional Information: Two years' preference share dividend is in arrears. The company had bad time during the last two years and hopes for better business in future, earning profit and paying dividend, provided the capital base is reduced.

An internal reconstruction scheme, agreed to by all concerned, is as follows:

- (i) Creditors agreed to forego 50% of their claim.
- (ii) Preference shareholders withdrew arrear dividend claim. They also agreed to lower down their capital claim by 20% by reducing nominal value in consideration of 9% dividend effective after reconstruction, in case equity shareholder's loss exceeded 50% on the application of the scheme.
- (iii) Bank has agreed to convert overdraft into term loan to the extent required for making current ratio to 2:1.
- (iv) Revalued amount for plant and machinery was accepted as ₹ 15,00,000.
- (v) Debtors to the extent of ₹ 4,00,000 were considered as good.
- (vi) Equity shares shall be exchanged for the same number of equity shares at a revised denomination as required after the reconstruction.

You are required to show the following:

- (a) Total loss to be borne by the equity and preference shareholders for the reconstruction.
- (b) Share of loss to the individual class of shareholders.
- (c) New structure of share capital after reconstruction.
- (d) Working capital of the reconstructed company, and
- (e) A Performa Balance Sheet after reconstruction.

[Answer: Loss to be borne by Equity and Preference Shareholders ₹ 14,40,000; New structure of share capital after reorganization ₹ 17,00,000; Working capital of the reorganized company ₹ 4,25,000; Balance Sheet (total) of Munna Ltd. (and reduced) ₹ 23,50,000]