CORPORATE ACCOUNTING – I

SUBJECT CODE: 7BCS5C2

Unit I

Issue of shares – Underwriting and redemption of preference shares

Unit II

Issue of debentures – underwriting and redemption of debentures – profit prior to incorporation

Unit III

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Unit I

Issue of shares – Underwriting and redemption of preference shares

UNIT—I

SHARES

Shares -- Meaning

A Share in a company is one of the units of fixed amount into which the total share capital of a company is divided.

Shares - Definition

"Share means a share in the capital of a company and includes stock except where a distinction between stock and shares expressed or implied".

Types of Shares

There are two types of shares namely preference shares and equity shares.

1. Preference Shares:

The Preference Shares are those which enjoy preferential rights over other classes of shares for the payment of dividend during the life-time of the company and repayment of capital over the other classes of shares at the time of winding up.

2. Equity Shares:

Equity Shares are those which do not enjoy the preferential right in payment of dividend and repayment of capital. The holders of these shares are paid dividend only after payment to the preferential shareholders is made. The rate of dividend is not fixed on equity shares and it varies from time to time.

ISSUE OF SHARES

PROCEDURE FOR ISSUE

From the accounting point of view, the following should be noted Every prospectus must mention the number of shares issued. Prospectus must mention the minimum subscription. The minimum amount of share capital is determined to cover. The purchase price of any property purchased or to be purchased;

Preliminary expenses;

Money borrowed for the foregoing matters and working Each application for shares must be accompanied by the prescribed application money. All application money must be kept intact in a schedule bank. If allotment takes place, a letter of allotment is sent to the allottees. If no allotment of shares is made, a letter of regret together with application money is sent to the applicants. The allotted has to pay the allotment money on allotment. On the receipt of the allotment money, the company issues share certificate. The balance due on shares may be called by the company in installments.

ISSUE OF EQUITY SHARES

Shares may be issued by a joint stock company for the following two different considerations. For consideration other than cash and For cash For consideration other than cash

i) Issue of shares to the vendors:

A company may purchase a running business or some assets from the vendors and they may be paid by giving equity shares.

The difference between the purchase consideration and the net assets acquired by the company is debited to Goodwill a/c or credited to Capital Reserve a/c.

ii) Issue of shares to the promoters:

The promoters or any other person may be compensated by the company for providing technical information, engineering services, plan outlay etc. by issuing fully paid shares.

iii) Issue of sweat equity shares:

Sweat equity shares means equity shares issued by the company to employees or directors at a discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions.

Legal provisions:

a) Sweat equity shares should be of a class of shares already issued.

b) Issue should be authorized by a special resolution passed by the company in the general meeting.

c) A period of one year must have expired since the date on which the company was entitled to commence business.

B. Issue of shares for cash

Companies generally issue shares for cash. These shares may be issued at different values as detailed below:

Issue of shares at par:

When a shareholder is required to pay an amount equal to the face value or nominal value of the shares, it is called issue of shares at par.

Issue of shares at premium:

When shares are issued at a price higher than the face value of the shares, it is called issue of shares at premium.

Issue of shares at discount:

When a shareholder is required to pay less than the face value, it is called issue of shares at a discount.

PROCEDURE FOR ISSUE OF SHARES FOR CASH

Applications:

The company issues a prospectus which contains the details of the amount to subscribe for its shares. The company may demand the full value of shares on application itself or it may demand only a part of it. The application money should not be less than 5% of the issue price.

Allotment:

Allotment of shares means acceptance of the offer of the applicant for the purchase of shares. Applicants to whom the shares are to be allotted will be issued 'Letter of Allotment' and if no allotment of shares is to be made, a letter of regret with application money is sent to the applicants.

Under subscription:

If a company is not received applications for all the shares offered by it to the public is called under subscription.

Over subscription:

If a company receive applications for a larger number of shares than offered by it to the public it is called over subscription. The company may treat the excess applications received in one or more of the following ways: Certain applications may straightway be rejected.

Partial allotment may be made (or) Pro-rata allotment may be made. Pro-rata allotment is one in means the shares are allotted on the basis of the proportion of the number of shares applied.

Calls:

Out of face value of the shares, at least 5% is payable with application, a part will be paid on allotment and rest of the money will be paid as and when calls are made.

Calls in Arrears:

If any amount, called in respect of a share either as allotment or call money, which is not paid is called calls in arrears.

The company can charge interest of 5% for the period for which such amount remained in arrear from the shareholder.

Calls in Advance:

The money received by the company in excess of what has been called up is known as calls in advance.

FORFEITURE OF SHARES

Forfeiture of shares means the cancellation of membership and taking away of the shares because of default in payment on allotment and / or call money by a shareholder. The following conditions must be satisfied for the valid forfeiture of shares:

The power to forfeit shares must be expressly given in Articles of Association of the company. The procedure given in the Articles must be followed. A notice of demand, requiring the shareholder to pay calls of a specified amount within the specified period must be given. The Board of Directors must pass a resolution for forfeiture of shares.

REISSUE OF FORFEITED SHARES

Forfeited shares become the property of the company and the company can cancel or reissue them at its convenience. They can be reissued at par, premium or discount. However, in case they are reissued at discount, the amount of discount should not exceed the amount that had been already paid by the defaulter.

After reissue of all forfeited shares if there is any balance in shares forfeited account, such profit should be treated as capital profit and it must be transferred to Capital Reserve Account.

JOURNAL ENTRIES FOR ISSUE OF SHARES

Journal Entries

Date	**Particulars**	**LF.**	**Debit Rs.**	**Credit Rs.**
	Bank a/c Dr. To Share Application a/c (Being the application money received.)		xxx	xxx
	Share Application a/c Dr. To Share Capital a/c (Being the application money transferred to share capital a/c)		xxx	 xxx
	Share Application a/c Dr. To Bank a/c (Being the excess application rejected.)		xxx	 xxx
	Share Allotment a/c Dr. To Share Capital a/c (Being the share allotment money due.)		xxx	 Xxx
	PREMIUM Share Allotment a/c Dr. To share capital a/c To share premium a/c (Being the share allotment due)		 xxx	 Xxx xxx
	DISCOUNT Share Allotment a/c Dr. Discount on shares a/c Dr. To share capital a/c (Being the share allotment due)		 Xxx xxx	 xxx

	Bank a/c Dr. To share allotment a/c (Being share allotment money received.)		xxx	 xxx
	Pro-rata allotment Bank a/c Dr. Share Application a/c Dr. To share capital a/c (Being the surplus on application)		 Xxx xxx	 Xxx
	Share first call a/c Dr. To share capital a/c (Being the first call money due)		xxx	 xxx
	Bank a/c Dr. To share first call a/c (Being share first call money received)		xxx	 xxx
	Forfeiture of shares Share capital a/c Dr. Share premium a/c Dr. To first call a/c To final call a/c To share forfeited a/c (Being shares forfeited)		 Xxx xxx	 xxx xxx xxx
	Re-issue of forfeited shares Bank a/c Dr. Share forfeited a/c Dr. To share capital a/c (Being forfeited share reissued) Share forfeited a/c Dr. To capital reserve a/c (Being the balance of share forfeited a/c transfer to capital reserve)		Xxx Xxx	 xxx

ISSUE OF SHARES AT PAR

1. On 1.1.2010, R Ltd., offers 10000 shares of Rs. 10 each payable as follows:

On Application Rs.3 per share

On Allotment Rs.2 per share

On First call Rs.3 per share

On Final call Rs.2 per share

All the shares are subscribed and amounts duly received. Pass journal entries.

SOLUTION:

Journal Entries

Date	Particulars	LF.	Debit Rs.	Credit Rs.
	Bank a/c Dr. To share application a/c (Being application money received)		30,000	 30,000
	Share application a/c Dr. To share capital a/c (Being application money transferred to share capital		30,000	 30,000
	Share allotment a/c Dr. To share capital a/c (Being allotment due)		20,000	 20,000
	Bank a/c Dr. To share allotment a/c (Being allotment money received)		20,000	 20,000
	Share first call a/c Dr. To share capital a/c (Being first call due)		30,000	 30,000

	Bank a/c Dr. To share first call a/c (Being first call received)		30,000	 30,000
	Share final call a/c Dr. To share capital a/c (Being final call due)		20,000	 20,000
	Bank a/c Dr. To share final call a/c (Being final call received)		20,000	 20,000

ISSUE OF SHARES AT PREMIUM

2. A Ltd., issued 15000 shares of Rs. 10 each at a premium of Rs. 2 per share, payable Re. 1 per share on application; Rs.6 per share on allotment including premium; Rs. 3 per share on first call and ERs. 2 per share on final call. The shares were all subscribed and money was duly received. Give journal entries in the books.

SOLUTION:

Date	Particulars	LF.	Debit Rs.	Credit Rs.
	Bank a/c Dr. To share application a/c (Being the application money received)		15,000	 15,000
	Share application a/c Dr. To share capital a/c (Being application money transferred to share capital)		15,000	 15,000
	Share allotment a/c Dr. To share capital a/c To share premium a/c (Being allotment due)		90,000	 60,000 30,000

	Bank a/c Dr. To share allotment a/c (Being allotment money received)		90,000	90,000
	Share first call a/c Dr. To share capital a/c (Being the first call money due)		45,000	45,000
	Bank a/c Dr. To share first call a/c (Being first call money received)		45,000	45,000
	Share final call a/c Dr. To share capital a/c (Being final call due)		30,000	30,000
	Bank a/c Dr. To share final call a/c (Being final call received)		30,000	30,000

OVER SUBSCRIPTION

3. X Ltd., invited applications for 20,000 shares of Rs.100 each payable:

Rs.25 on application

Rs.35 on allotment

Rs.40 on call

25,000 shares were applied for. The directors accepted applications for 20,000 shares and rejected the remaining applications. All moneys due were fully received. Give journal entries.

X LTD.

Journal Entries

Date	Particulars	LF	Debit Rs.	Credit Rs.
	Bank a/c Dr. To share application a/c (Being application money received)		6,25,000	6,25,000
	Share application a/c Dr. To share capital a/c (Being allotment of 20,000 shares and their application money transferred to share capital a/c)		5,00,000	5,00,000
	Share application a/c Dr. To Bank a/c (Being excess application money refunded)		1,25,000	1,25,000
	Share allotment a/c Dr. To share capital a/c (Being allotment due)		7,00,000	7,00,000
	Bank a/c Dr. To share allotment a/c (Being allotment money received)		7,00,000	7,00,000
	Share call a/c Dr. To share capital a/c (Being call money due)		8,00,000	8,00,000
	Bank a/c Dr. To share call a/c (Being call money received)		8,00,000	8,00,000

ENTRY FOR FORFEITURE AND RE-ISSUE ONLY

4. X Ltd. Forfeited 30 shares of Rs.10 each fully called up, held by Ram for nonpayment of allotment money of Rs.3 per share and first call of Rs.4 per share. He had paid the application money of Rs.3 per share. These shares were reissued to Raja for Rs.8 per share. Pass journal entries.

Journal Entries

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
	Share capital a/c Dr.		300	
	To share allotment a/c			90
	To share call a/c			120
	To share forfeited a/c			90
	(Being 30 shares forfeited)			
	Bank a/c Dr.		240	
	Share forfeited a/c Dr.		60	
	To share capital a/c			300
	(Being the 30 shares re-issued)			
	Share forfeited a/c Dr		30	
	To share capital reserve a/c			30
	(Being the balance transferred to CR)			

ISSUE OF SHARES FOR CONSIDERATION OTHER THAN CASH

5. S Ltd. Purchased a machinery for Rs.4,40,000 from S.K..& Sons. It issued equity shares of Rs.10 each fully paid up at a premium of 10%. Pass journal entries to record this transaction.

Journal Entries

Date	Particulars	L.F	Debit Rs.	Credit Rs.
	Machinery a/c Dr. To S.K. & Sons a/c (Being the machinery purchased from S.K.& Sons)		4,40,000	 4,40,000
	S.K.& Sons a/c Dr. To share capital a/c To share premium a/c (Being 40,000 fully paid shares are issued)		4,40,000	 4,00,000 40,000

Working Note.

4,40,000 = face value=4,40,000/- 11/10 = Rs.4,00,000

Premium = 4,40,000/11*1 = Rs.40,000

REDEMPTION OF PREFERENCE SHARES

Redeemable Preference Shares

The Redeemable Preference shares are those, the amount of which can be paid back to the holders of such shares. The paying back of capital is called the redemption.

Provision For The Redemption Of Preference Shares

The following are the important provisions of Sec.80 of the Companies Act, 1956, relating to redemption of redeemable preference shares:

The shares to be redeemed must be fully paid-up. If the company has partly paid preference shares, it must see that they are made fully paid up before they are redeemed.

The redeemable preference shares can be redeemed either out of the profits of the company which would otherwise be available for dividend or out of the proceeds of a fresh issue of shares made for this purpose only.

Any premium payable on redemption must be provided out of profits or out of the company's share premium account.

Where redemption is made out of profits, a sum equal to the nominal amount of the shares so redeemed must be transferred, out of the profits of the company to a reserve called the Capital Redemption Reserve a/c.

Capital Redemption Reserve a/c can be utilized for the issue of fully paid bonus shares to the equity shareholders.

Redemption of preference shares shall not be taken as the reduction of the authorized share capital.

CAPITAL REDEMPTION RESERVE

Capital Redemption Reserve is a reserve created out of profit of the company, if the preference shares are redeemed out of profit. The amount so credited will be equal to the nominal value of the shares to be redeemed.

PROFITS AVAILABLE FOR CAPITAL REDEMPTION RESERVE

Usually, the revenue profits or the profits available for dividend can be used to create the capital redemption reserve. They are:

General Reserve
Profits and Loss a/c
Dividend Equalization Fund
Reserve Fund
Revenue portion of profit on sale of investments
Revenue portion of profit on sale of fixed assets
Workmen's Accident Compensation Fund
Insurance Fund

PROFITS NOT AVAILABLE FOR CAPITAL REDEMPTION RESERVE

The capital profits or profits not available for dividend cannot be used for the purpose of creating the capital redemption reserve. They are

General Reserve
Capital Redemption Reserve
Development Rebate Reserve
Depreciation Reserve
Shares forfeited account
Profit prior to incorporation
Profit on sale of fixed assets
Share premium account

AMOUNT TO BE TRANSFERRED TO CAPITAL REDEMPTION RESERVE

Redeemable pref. shares Face value -- Fresh issue of share face value = Amount to be transferred to CRR

(or)

Redeemable pref. shares face value -- Actual amount received from fresh issue =Amount to be transferred to CRR a/c.

MINIMUM FRESH ISSUE OF SHARES

Fresh issue=RPS face value +premium on redemption –divisible profit in the B/S – share premium in the B/S – premium on fresh issue

JOURNAL ENTRIES FOR REDEMPTION OF PREFERENCE SHARES

Date	Particulars	LF	Debit Rs.	Credit Rs.
	WHEN THE RPS ARE NOT FULLY PAID a)Redeemable pref. shares final call a/c Dr. To Redeemable pref. shares capital a/c (Being the final call due)		xxx	 xxx
	b)Bank a/c Dr. To Redeemable pref. share final call a/c (Being final call received)		xxx	 xxx
	WHEN THE RPS ARE FULLY PAID i)For sale of investment etc. a) If sold at profit:			

	Bank a/c Dr. To Investment a/c To p & l a/c		xxx	 Xxx xxx
	b) If sold at loss : Bank a/c Dr. P&L a/c Dr. To investment a/c (Being the investment sold at loss)		 xxx	 xxx
	ii)For issue of debentures : Bank a/c Dr. To debenture a/c To debenture premium a/c (Being the debentures issued for augmenting the cash)		 xxx	 Xxx xxx
	For fresh issue of shares Bank a/c Dr. To share capital a/c To share premium a/c (Being the debentures premium)		 xxx	 Xxx xxx
	Share premium a/c Dr. P&L a/c Dr. General reserve a/c Dr. To premium on redemption a/c (Being the premium on redemption appropriated)		Xxx Xxx xxx	 xxx
	General reserve a/c Dr. Profit & loss a/c Dr. To capital redemption reserve a/c (Being the amount transferred to CRR)		Xxx xxx	 xxx
	Redeemable pref. share capital a/c Dr. Premium on redemption a/c Dr. To redeem pref. shareholders a/c (Being the capital & premium transferred)		Xxx xxx	 xxx

	Redeem pref. shareholder a/c Dr. To bank a/c (Being the final payment made.)		xxx	 xxx
	Capital redemption reserve a/c Dr. General reserve a/c Dr. Profit & loss a/c Dr. To bonus to shareholders a/c (Being the bonus payable.)		xxx	
	Bonus to shareholders a/c Dr. To equity share capital a/c (Being the bonus shares issued)		xxx	 xxx

CALCULATION OF FRESH ISSUE

1 . From the following information find out how much minimum fresh issue is necessary, if Redeemable preference share of Rs.2,00,000 is redeemed at 10% premium.

Profit shown in the balance sheet.

Profit Rs.30,000 ; General reserve Rs.20,000, share premium Rs.8,000.
Dividend equalization fund Rs.50,000.

SOLUTION:

Fresh issue = 20,000+2,00,000*10/100-(30,000+20,000+50,000)-8,000
= 2,00,000+20,000-1,00,000-8,000
= 2,20,000-1,08000 = Rs.112000

2. The following are the details taken from the records of B ltd. On June 30, 2009:

Share capital		
Equity shares (fully paid up)	Rs.	6,00,000
Preference shares (fully paid up)		3,00,000
General reserve		2,00,000
P&l a/c (credit balance)		1,25,000
Share premium		50,000

The company decided to redeem the preference shares at a premium of 10% out of its General reserve and p&l a/c .

Give journal entries relating to redemption of preference shares.

SOLUTION:

Journal entries

Date	**Particulars**	**LF**	**Debit Rs.**	**Credit Rs.**
	General reserve a/c Dr. P & l a/c Dr. To capital redemption reserve a/c (Being the amount transferred to CRR)		2,00,000 1,00,000	 3,00,000
	Share premium a/c Dr. To premium on redemption a/c (Being the premium on redemption a/c appropriated)		30,000	 30,000
	Preference share capital a/c Dr. Premium on redemption a/c Dr. To redeem pref. share capital a/c (Being share capital & premium transferred to RPS holder a/c)		3,00,000 30,000	 3,30,000
	Redeemable pref. share holder a/c Dr. To bank a/c (Being the final payment made.)		3,30,000	 3,30,000

UNDERWRITING

Meaning

Underwriting is a contract between a company and underwriters. They may be individuals or institutions, ready to take up the whole or a portion of the shares or debentures issued, which are not subscribed for by the public for a consideration called underwriting commission.

Types of Underwriting

i) Full underwriting

The Underwriting of the whole issue of shares or debentures of a company is called fu;l underwriting

ii) Partial underwriting

The underwriting of a part of the issue of shares or debentures of a company is called partial underwriting

iii) Firm underwriting

The agreement of an underwriting to by a definite number of shares or debentures in addition to the shares or debentures he has to take under the underwriting agreement is called firm underwriting.

Managers to the issue

The companies are tree to appoint one or more agencies managers to the issue. The aggregate amount payable as fees to the issue manager shall not exceed the following limit.

i) For issue up to Rs. 5 Crores – 0.5%

ii) For issue up to Rs. 5 Crores – 0.2%

Full underwriting

1. A company issued 10,000 shares of Rs.10 each. Those shares were underwriting as follows.

A-7000 shares and B-3000 shares

The public applied for 8000 shares which included marked applications as follows.

A-5000 shares, and B – 2000 shares

Determine the liability of A and B under both Gross liability and Remaining liability basis.

Solution

Statement showing liability of underwriter

(Gross Liability Basis)

Particulars	**A**	**B**	**Total**
Gross Liability (-)	7,000	3,000	10,000
(-) Unmarked Application	700	300	1,000
	6,300	2,700	900
(-) Marked Application	5,000	2,000	7,000
Net Liability	1,300	700	2,000

Statement showing Liability of underwriters

(Remaining Liability Basis)

Particulars	**A**	**B**	**Total**
Gross Liability (-)	7,000	3,000	10,000
(-) Unmarked Application	5,000	2,000	7,000
	2,000	1,000	3,000
(-) Marked Application	667	333	1,000
Net Liability	1,333	667	2,000

2. A company issued Rs.1,00,000 Shares of Rs.10 each. There shares were underwritten as follows.

X – Rs.30,000 Shares, Y – Rs.50,000/- Shares
The public applied for Rs.70,000/- Shares.
Determine the liability for X and Y

Statement showing Liability of underwriters

(Gross Liability Basis)

Particulars	**A**	**B**	**Com**	**Total**
Gross Liability	30,000	50,000	20,000	10,000
(-) Unmarked Application	21,000	35,000	14,000	70,000
Net Liability	9,000	15,000	6,000	30,000

Unit-II

Issue of debentures – underwriting and redemption of debentures – profit prior to incorporation

UNIT – II

Issues of Debentures

Definition

Debenture includes debenture shares bonds and any other securities of a company whether constituting a charge on the assets of the company or not"

-Section 2 (2) of the companies Act, 1956.

Distinction between A share And a Debenture

S.No	Shares	Debentures
1	They are owned capital of a company	They are borrowed funds of a company
2	The money paid on shares is not refundable	Debentures are redeemable in nature and the principal amount is repaid after the stipulated period.
3	Shares can be issued at a discount subject to certain conditions contained in the companies Act.	There are no legal; restrictions on the terms of the issue of debentures

Issue for cash

1. A ltd., issued 1000 12% debentures of Rs.10 each. Give journal entries under two situations.
   a) Issued at a premium of 6%
   b) Issued at a premium of 10%

Solution

Journal Entire's

Date	particulars	L.F	Debit	Credit
	a) Bank A/c Dr		11000	
	To 12% Debenture a/c			10000
	To Debenture Premium a/c			1000
	b) Bank A/c Dr		9000	
	To 12% Debenture a/c		1000	
	To Debenture Premium a/c			10000

Issue for Consideration

2. X ltd. acquired assets of Rs.5,00,000/- and took over the liabilities amounted to Rs.50,000 at on agreed value of Rs.4,00,000/- of Y ltd issued 12% Debentures at a discount of 20% full satisfaction of the purchase price. Show the entries.

Solution

Journal Entire's

Date	particulars	L.F	Debit	Credit
	a) Sunday Assets A/C Dr		5,00,000	
	To Sunday liability A/C			50,000
	To Y ltd a/c			4,00,000
	To Capital Reserve			50,000
	(Being purchase of assets and Liabilities)			
	Y ltd A/C Dr		4,00,000	
	Discount on Debenture A/C Dr		1,00,000	
	To 12% Debenture a/c			5,00,000
	(Being issue of debentures in settlement of purchase price)			

Issue on Condition

3. C ltd issued 1000 12% debentures of Rs.100 each. Give Journal entries under two situations

   a) Issued at par and redeemable at par

   b) Issued at a discount of 10% and redeemed at a premium of 10%

Solution

Journal Entire's

Date	particulars	L.F	Debit	Credit
	Bank A/C Dr To 12% Debenture a/c (Being purchase of assets and Liabilities)		1,00,000	 1,00,000
	b) Bank a/c Dr Discount on Debenture A/C Dr Loss on issue of debentures a/c Dr To 12% Debenture a/c To premium on Redemption a/c (Being issue of debentures in settlement of purchase price)		90,000 10,000 10,000	 1,00,00 10,000

Redemption of debentures

Method of Redemption

The debentures issued by a company may be redeemed in any of the following

i) Redemption of debentures out of profits

ii) Redemption of debentures out of Capital

iii) Redemption of conversion of debentures into shares or new debentures

iv) Redemption of debentures out of provisions made for redemption

v) By purchase of company own debenture

Purchase of own Debentures

Own Debentures

The purchase of its own debentures by a company in the open market to be kept as an investment or to cancel at a later date is called own debentures.

Interest on own debentures

The total amount of interest due on debentures is deemed to be outstanding. But payment of interest on debentures is made only to the outsiders.

Purchase of own Debentures

When own debentures are purchased on a date other that the date of interest, distinction must be made between the capita; and revenue portion of the price paid for the debentures.

Cum – Interest

Cum – interest means that it is with interest. Thus the cum – interest quotation price is a purchase price that includes interest also.

Ex – Interest

Ex – Interest means that is is without interest. Thus, the Ex – Interest quotation price is a purchase price that excludes interest.

1. On 1st Jan 2007, a company issued Rs.2,00,000 14% Debentures at 5% Discount repayable in five years at par. The interest is payable half yearly on 30th June and 31st December and the same was duly paid.

On 31th Dec .2007 the company purchased Rs.20,000 debentures at a cost of Rs.18,9000 pass necessary Journals entries in the books of the company up to 31.12.2007, including closing entries on that date if the above redemption was out of profit

Journal Entire's

Date	particulars	L.F	Debit Rs	Credit Rs
2007 Jan 1	Bank A/C Dr Discount on Debentures a/c Dr To 14% Debentures a/c (Being 14% Debentures issued)		1,90,000 10,000	 2,00,000
June 30	Interest on Debentures a/c Dr To Bank a/c (Being the half yearly interest paid)		14,000	 14,000
2007	Interest on December a/c Dr To Bank a/c (Being the half yearly interest paid)		14,000	 14,000
2007 Dec 31	Profits loss a/c Dr To Interest on Debenture a/c (Being inters on debenture transferred)		28,000	 28,000
2007	14% Debenture a/c Dr To Bank a/c To Profit on Red. of debenture a/c (Being the debentures redeemed out of profit by purchase in the marked)		20,000	 18,900 100
	Profit loss Appropriation a/c Dr To Debenture Red. Reserve a/c (Being the profit appropriated and transferred to debenture redemption reserve a/c)		20,000	 20,000
	Profit on Red. of debentures A/C Dr To capital Reserve a/c (Being the profit on redemption transferred to capital reserve)		1,100	 1,100

A company issued 6% debentures of Rs.6,00,000. The amount set aside for the redemption of Debenture is invested in 5% Govt. Securities. The Sinking fund table shows that 0.31720856 at 5% compound interest in three years will become Re 1

Prepare (a) debenture sinking Fund a/c and (b) Debenture sinking Fund Investment a/c for the 1st year.

Solution

Rs.6,00,000 x 0.31720856 = Rs.1,90,325

Debenture Sinking Fund a/c

Dr	Particulars	Rs	Date	Particulars	Cr
	To Balance c/d	1,90,325	Dec 31	By P & L (app) a/c	1,90,325
		1,90,325		By Balance b/d	1,90,325
			Jan 1		1,90,325

Debenture Sinking Fund a/c

Dr	Particulars	Rs	Date	Particulars	Cr
Dec 31	To Balance a/c	1,90,325	Dec 31		
Jan 31		1,90,325		By Balance c/d	1,90,325
	To Bank b/d	1,90,325			1,90,325

Profit Prior To Incorporation

Profit Prior to incorporation – Meaning

When company prepares its final account for the first year after purchasing a going concern if has to allocate the profit between the period of purchase to the date of incorporation and form the date of incorporation to the date of final account.

Loss prior to incorporation – Meaning

If the company has incurred any loss from the date of purchase to the date of incorporation such loss is called as loss prior to incorporation.

Calculation of Various Ratios

i) Time ratio
ii) Weight Time ratio
iii) sales radio
iv) Weighted sales ratio
v) Purchase ratio

Calculations of Ratios

1. The monthly average of sales in Jan, Nov and Dec is double the monthly average for the remaining months of the year.

The date of incorporation of the business 1.4.07. The date of purchase of the business 1.1.07. The date of closing of accounts 31.12.2007. Ascertain sales ratio.

Date of purchase		Date of incorporation		Date of Final a/c
01.01.07	⟷	01.04.02	⟷	31.12.07

Jan, Feb, March — April, May, June, July, Aug, Sep, Oct, Nov, Dec

2 + 1 + 1 = 4 — 1+ 1 + 1 + 1 + 1 + 1 + 1+ 2 + 2 = 11

Sales Ratio = 4 : 1

Profits loss Account form

2. B.Ltd was incorporated on 30.06.03 to take over the business of T.Ltd as from 1st Jan 03. The Financial accounts of the business for the year ended 31.12.2003 disclosed the following information.

Date	particulars	L.F	Debit	Credit
	Sales		1,20,000	
	Jan to June		1,80,000	3,00,000
	July to Dec			
	Loss : Purchase			
	Jan to June		75,000	
	July to Dec		1,20,000	1,95,000
	Gross profit			1,05,000
	Less : Salaries		15,000	
	Selling exp		3,000	
	Depreciation		1500	
	Directors Remuneration		750	
	Debenture Interest		90	
	Administration expenses		4500	24,840
	Profit for the year			80,160

You are required to prepare a statement apportioning the balance of profit between the period prior to and since incorporation and show the profit loss appropriation account for the year ended 31.12.03.

Profit & loss Account of B Ltd for the year ended 31.12.03

Date	Particulars	Basis	Pre-incorporation	Post - Incorporation	Date	Particulars	Basis	Pre-incorporation	Post – Incorporation
	To purchase	Actual	75,000	1,20,000		By sales	Actual	1,20,000	1,80,000
	To salaries	Time	7,500	7,500					
	To selling expenses	Sales	1,200	1,800					
	To Depreciation	Time	750	750					
	To Directors Ram	Post	-	750					
	To Debenture Int	Post	-	90					
	To Administration exp.Time	Time	2,250	2,250					
	To capital Reserve		33,300	-					
	To Net Profit		-	46,860					
			1,20,000	1,80,000				1,20,000	1,80,000

Unit-III

Valuation of goodwill and shares – Methods.

UNIT – III

Valuation of Goodwill

Meaning

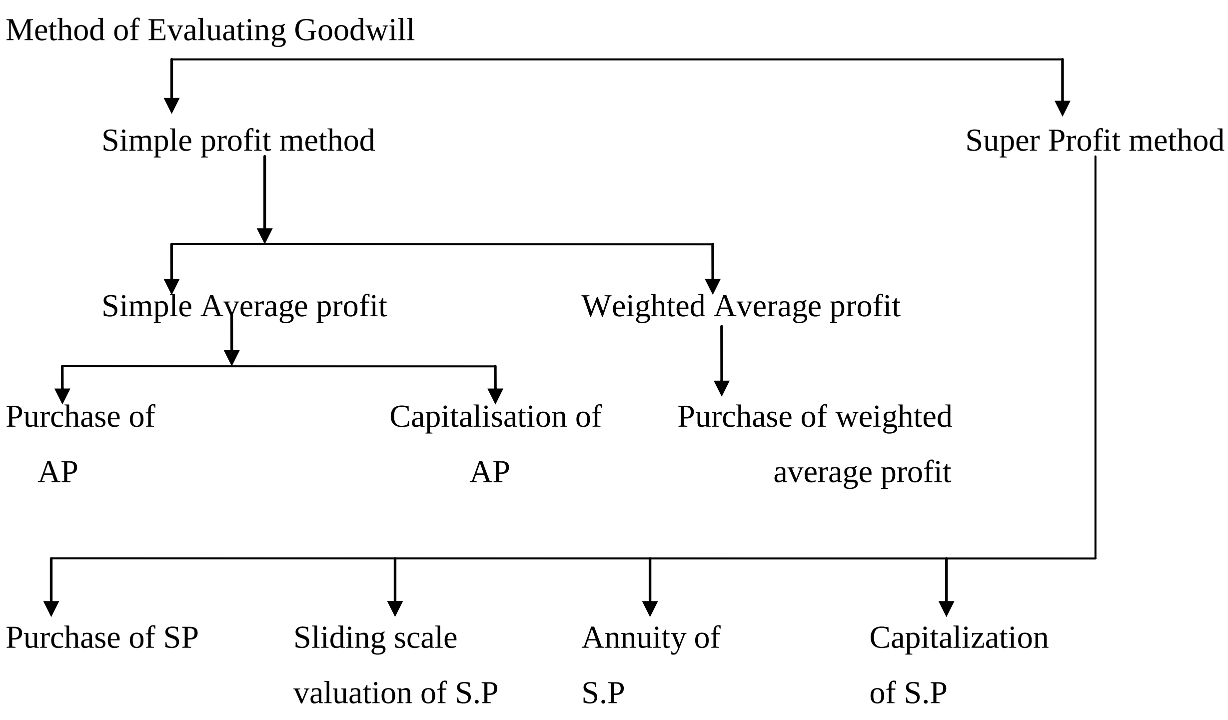
Goodwill is something which will bring to the firm in future profits almost without efforts. Goodwill is the reputation or good name earned by a business which is invisible and hence it is an intangible asset of a concern of a company.

Definition

"The capacity of a business to earn profits in future is basically what is meant by the term goodwill".

-J.D.Magee

Methods of Evaluating Goodwill



Purchase of Average profit

1. Calculate the amount of goodwill on the basis of 2 years purchase of the last five years average profits. The profits for the last five year are 8,200: 10,500: 5,100: 12,000, 7700.

Solution

Calculation of Average Profit

S.No	**Years**	**Rs**
1	1^{st} year	8200
2	2^{nd} year	10500
3	3^{rd} year	5100
4	4^{th} year	7700
5	5^{th} year	12000
	Total	43500

$$\text{Average} = \frac{\text{Total profit for all years}}{\text{Number of years}}$$

$$= 43500 \qquad = \qquad \text{Rs. } 8700$$

Value of Goodwill = Average profit x No. of year Rs purchase

= 8700 X 2 = Rs. 17400

2. The Net profit of a business after providing for fixation for the profit five years are: Rs.40,000, Rs.42,500, Rs.46,000, Rs.52,500 and Rs.59,000.

The average capital employed in the beginning is Rs.4,00,000 and the normal rate of return expected in this type of business is 10%

Calculate the goodwill on the basis of

a) five years purchase of super profits

b) annuity method, taking the present value of annuity of Re.1 for five years at 10% as Rs.3.78 and

c) Capitalization of super profits

Solution

Average profit $= \dfrac{40,000 + 42500 + 46000 + 52500 + 59000}{5}$

Normal Profit = Average capital Employed x Normal Rate of Return

$= 400000 \times \dfrac{10}{100} = \text{Rs. } 40000$

Super Profit = 48000 – 40000 = Rs. 8000

Calculation of Goodwill

a) Purchase of super profit

Gw = SP x Purchase of No.of Yr'

= 8000 x 5 = Rs.40,000

b) Annuity Method

Gw = SP X Annuity table value

Gw = 8000 x 3.78 = Rs.30240

c) Capitalization of super profit

= SP x100

$= \dfrac{8000}{10} \times 100 = \text{Rs.}80,000$

Valuation of shares

Meaning

Valuation of shares involves the use of financial and accounting data based on the objective and subjective consideration for a specific purpose. Hence, for ordinary transactions in shares, the price prevailing in the stocks exchange may be taken as the proper value.

Methods of valuation of shares

The following are the various methods for valuation of shares

1. Net Asset (or) Intrinsic value method
2. Yield Method
3. Earning capacity method
4. Fair value Method

Net Asset Method

1. Balance sheet of Navin Company as on 31.12.2009.

Liabilities	**Rs**	**Assets**	**Rs**
20,000 Equality shares of Rs.10	2,00,000	Goodwill	2,00,000
each	1,50,000	Investment at cost (Market value)	3,00,000
Employee's Saving fund	1,50,000	Rs.2,50,000	5,00,000
Employee's provident fund	6,00,000	Stock cost	4,00,000
Creditors	3,70,000	Debtors	70,000
Profit loss a/c		Bank balance	
	14,70,000		14,70,000

The profits for the last five years were Rs.15,000/- Rs.20,000/- Rs.30,000/- and Rs.35,000/- and the goodwill is to be valued on the basis of 3 years purchase of the average annual profit for the last 5 years.

`Calculate the price of the share on the basis of net asset value.

Solution

$$AP = \frac{15,000 + 20,000 + 25,000 + 30,000 + 35,000}{5}$$

$$= \frac{1,25,000}{5} = \text{Rs. } 25,000$$

Good will = 25000 x = 75000

Calculation of Net Assets

Particulars	Rs	Rs
Goodwill		75,000
Investments		2,50,000
Stock		5,00,000
Debones		4,00,000
Bank Balance		70,000
Total		12,95,000
Less:		
Employee’s savings fund	1,50,000	
Employee’ s Provident Fund	1,50,000	
Creditors	6,00,000	9,00,000
Net Assets		395000

Net Assets = $\frac{\text{Net Assets for Equity Share holders}}{\text{No.of Equity Shares}}$

= $\frac{395000}{20000}$ = Rs.19.75

2. From the following particulars, calculate the value per equity share

Particulars	Rs.
2,000, 9% preference shares of Rs.100 each	2,00,000
50,000 Equity Shares of Rs.10 each Rs.8 per share paid	4,00,000
Expected profits per year before tax	2,18,000
Rate of Tax	50%
Transfer of General reserve every year	20% of the profit
Normal Rate of Earnings	15%

Solution

Calculation of profit to Equity shareholders

Expected profits per year before fax	218000
(-) Tax @ 50%	109000
Profit after tax	109000
(-) Transfer to General Reserve	21800
Profit available for preference Equity shareholders	87200
(-) Preference dividend	18000
Expected profit available to equity share holders	69200

Expected rate of return = $\frac{\text{Expected Profit}}{\text{Total paid up Equity share capital}}$ x 100

= $\frac{69{,}200}{4{,}00{,}000}$ x 100 = 17.03%

Yield Value per share = $\frac{\text{Expected Rate of Return}}{\text{Normal rate of return}}$ x paid up value per share

= $\frac{17.30}{15}$ x 8 = Rs.9.23

Unit IV

Final accounts of companies

UNIT – IV

Final Accounts of Companies

Final Account of companies

In case of sole trading concern or partnership firm the preparation of find accounts is not compulsory. But companies have a statutory obligation to prepare final accounts as required by section 209 & 210 of the companies Act 1956.

The companies Act requires every company to prepare every year Trading a/c, profit and loss a/c, profit loss appropriation a/c and Balance Sheet.

Limits to Managerial Remuneration

The limits of managerial remuneration payable on various circumstances are listed below

Managing Personal	Maximum Rumination on net profit
i) Overall limit to all the managerial persons	11%
ii) All directors – company managing directions, whole time director or manager	1%
iii) All directors – Company is not having a managing director, whole time director or manager	3%
iv) Manager	5%
v) Managing director	5%
vi) When there are more than one managing director or whole time directors	10%

Divisible profit

Profits available for dividend to shares holders are known as divisible profit.

Dividend

A dividend is a share of the profits of a company distributed to the share holders.

Interim Dividend

Interim Dividend is one which is declared and paid by the company in between two final dividends

Calculation of Managerial Remuneration

1. From the following particulars determine the medium remuneration available to a full time director of a manufacturing company.

   The profit & loss a/c of the company showed a net profit of Rs.40,00,000 after taking into account the following items

i) Depreciation (including Special depreciation of Rs.40,000)	1,00,000
ii) Provision for income tax	2,00,000
iii) Donation to political parties	50,000
iv) Ex-gratia payment to a worker	10,000
v) Capita; profit on sale of assets	15,000

Statement of profit for the purpose of managerial Remuneration

Net profit as per P&L		40,00,000
(+) Inadmissible items: special depreciation	40,000	
Provision for income tax	2,09,000	
Ex-gratia payment to a worker	10,000	2,50,000
		42,50,000
(-) Capital profit on sale of assets		15,000
Net profit managerial Rem		42,35,000

Managerial Ram = 4235000 x 5/100 = Rs.2,11,750

2. Ravi Ltd was registered with an authorized capital oif Rs.6,00,000 in enquiry shares of Rs.10 each. the following is its Trial Balance on 31 March 2008.

Trial Balance

Good will	25,000	-
Cash	750	-
Bank	39,900	-
Purchased	1,85,000	-
Primary expensed	5,000	-
Share Capita;	-	4,00,000
12% Debentures	-	3,00,000
P & L A/c (Cr)	-	26,250
Calls – in – arrears	7,500	-
Premises	3,00,000	-
Plant & Machinery	3,30,000	-
Interim dividend	39,250	-
Sales	-	4,15,000
Stock (1.4.07)	75,000	-
Furniture & fixtures	7,200	-
Sundry debtors	87,000	-
Wages	87,865	-
General expenses	6,835	-
Freight and carriage	13,115	-
Salaries	14,500	-
Directors fees	5,725	-
Bad debts	2,110	-
Debenture interest paid	18,000	-
Bills payable	-	37,000
Sundry creditors	-	40,000
General reserve	-	25,000
Provision for bad debts	-	3,500
	12,46,750	12,46,750

Prepare profit & Loss Account, profit & Loss Appropriation A/c and Balance Sheet in proper form after making the following adjustments.

i) Depreciate plant and machinery by 15%

ii) Write off Rs.500 from preliminary expenses

iii) Provide for 6 months interest on debentures

iv) Leave bad and doubtful debts provision at 5% on Sunday debtors

v) Provide for income tax at 50%

vi) Stock on 31.03.2008 was Rs.95,000

Trading and profit & Loss a/c Ram Ltd for the year ended 31.03.2008

Particulars	**Rs**	**Rs**	**Particulars**	**Rs**	**Rs**
To opening stock		75,000	By sales		4,15,000
To purchase		1,85,000	By Closing stock		95,000
To wages		84,865			
To Freight % Carriage		13,115			
To Gross profit c/d		1,52,020			
		5,10,000			5,10,000
To salaries		14,500	By Gross profit b/d		1,52,020
To General expenses		6,835			
To Directors fees		5,725			
To Bad debts	2100				
(+) New provision	4350				
	6460				
(-) Old provision	3500	2,960			
To preliminary expenses		500			
To int. on debentures	18,000				
(+) O/s for 6 months	18,000	36,000			
(3,00,000 x 12/100 x 6/12)		49,500			
To Depreciation on Plant & Machinery					
To provision for Tax		18,000			
(36,000 x 50/100)		18,000			
To Net profit c/d		1,52,020			1,52,020

Profit & Loss Appropriation a/c

Particulars	Rs	Particulars	Rs
To interim dividend	39,250	By Balance b/d	26,250
To Balance carried to Balance Sheet	5,000	By Net profit b/d	18,000
	44,250		44,250

Balance Sheet of R Ltd. as on 31st March 2008

Liabilities		Rs	Assets		Rs
Authorized Capital;			**Fixed Assets:**		25000
60,000 equality shares of			Goodwill		
10 each		6,00,000	Plant & Machinery	3,30,000	
Subscribed, called			Less: Depreciation		
up & paid up capital:			@ 15%	49,500	2,80,500
40,000 shares of					
Rs.10 each	4,00,000				
Less: Calls in arrears	7,500	3,92,500	Premises		3,00,000
Reserve & Surplus			Fixtures		7,200
General reserve		25,000	**Investments**		
P & L A/c		5,000	**Current assets &**		
Secured & Loans			**Loans and advances:**		**Nill**
12% debentures		3,00,000	Closing debtors		95,000
Outstanding interest on		18,000	Sundry debtors	87,000	
debenture		Nil	Less : New Provision	4,350	82,650
Unsecured loans					
Current liabilities:			Cash at bank		39,900
Bills Payable		37,000	Cash in hand		750
Sunday creditors		40,000	Miscellaneous expenditure		
Provisions:			Preliminary exp	5,000	
Provisions for income tax		18,000	Less: Written off	500	4,500
		8,35,500			8,35,500

Unit-V

Amalgamation – Absorption – Reconstruction (External and Internal)

UNIT – V

Amalgamation and Absorption

Amalgamation – Meaning

When two or more existing companies doing similar business combining together by dissolution to form a new company is called amalgamation. For example.

Existing Companies **Liquation** → **New Company**

A Ltd B Ltd C Ltd ABC Ltd

Selling Companies **Purchasing Company**

(or) **(or)**

Transferor Companies **Transferee Company**

Absorption – Meaning

When one existing company takes over the business of one or more existing companies, it is called absorption. The companies whose business is taken over liquidated and no new company is formed. For Example

Existing Companies **Liquation** → **New Company**

A Ltd B Ltd X Ltd

Selling Companies **Purchasing Company**

(or) **(or)**

Transferor Companies **Transferee Company**

Distinction between Amalgamation and Absorption

i)	Two or more companies carrying on similar business merged into one single company	An existing takes over the business of one or more existing companies
ii)	All amalgamating companies should go into liquidation	The companies whose business are taken over should go into liquidation
iii)	A new company is to be formed to take over these business	No new formation of a company is necessary
iv)	The purpose of amalgamation is to bring about the combination or for eliminating the companies	The purpose of absorption is to purchase other business for expanding the activities or size of the business
v)	The Central Government is empowered to order amalgamation of two or more companies in the national interest	Absorption of companies in national interest is not possible under the Act.

Calculation of Purchase Consideration

1. A purchasing company agrees to issue three shares of Rs.10 each paid up at market value of Rs.15 per share for every 5 shares in the vendor company.

Find out the number and amount of shares to be issued by the purchasing company if the vendor company has 1,00,000 shares of Rs.10 each Rs.5 paid up.

Solution

No.of Shares to be issued

by the purchasing company = Rs. $\frac{1,00,000 \times 3}{5}$ = 60, 000 shares

Amount of shares issued by the purchasing company:

Amount of share capital	=	60,000 x 10	=	Rs. 6,00,000
Amount of share premium	=	60,000 x 5	=	Rs. 3,00,000
		Total	=	Rs.9,00,000

Absorption of Companies

2. X Co.Ltd took over assess Rs.35,000 and liabilities of Rs.30,000 of Y Co. for the purchase consideration oF Rs.33,000 X Co.Ltd Paid the purchase consideration by issuing debenture of Rs.100 each at a premium of 10% Give journal entries.

Solution

In the Books of X Co. Ltd

Journal Entries

Date	**Particulars**	**L.F**	**Debit** **Rs**	**Credit** **Rs**
	Business Purchase a/c Dr To Liquidators of Y Coy. Lts (Bering the purchase consideration payable)		3,30,000	 3,30,000
	Assets a/c Dr Goodwill a/c (Bal. Fig) Dr To Liabilities a/c To Business Purchase a/c (Being the assets and ;Liabilities are taken over)		3,50,000 10,000	 30,000 3,30,000
	Liquidator's of Y co ltd a/c Dr To Debenture a/c To premium on Debenture a/c (Being the purchase consideration paid)		3,30,000	 3,00,000 30,000

Working Notes

Purchased Consideration = 3,30,000

Debenture $3,30,000 \times \frac{100}{110}$ = Rs. 3,00,000

Premium on Debenture $3,30,000 \times \frac{10}{110}$ = 30,000

Amalgamation of Companies

Net Asset Method

3. The A Company and B whose business are of similar nature, decided t amalgamation and a new company called AB Company Ltd is formed to take over their assets and liabilities. The following are their Balance sheets.

Balance Sheet as on 31st December 2004

Liabilities	**A** **Rs**	**B** **Rs**	**Assets**	**A** **Rs**	**B** **Rs**
7500 Eq. shares of			Goodwill	30,000	20,000
Rs.10 each	75,000		Plant	18,300	13,450
4550 Rg. shares of			Land	10,000	
Rs.10 each		45,500	Stock in trade	16,000	11,550
Sundry Creditors	3,300	2,000	Sunday Debtors	7,500	6,000
Reserves	4,200		Cash	1,500	1,000
Profit & Loss a/c	800	4,500			
	83,300	52,000		83,300	52,000

Assuring that the assets and liabilities are worth at their book values, what amount each company will get? Pass necessary journal entries in the books of the purchasing company and also prepare the Balance Sheet of AB Company Ltd.

Solution

In the Books of AB Ltd

Journal Entries

Date	Particulars	L.F	Debit Rs	Credit Rs
2007 Dec 31	Business Purchases a/c Dr		1,30,000	
	To Liquidators of A Company			80,000
	To Liquidators A B Company			50,000
	(Being purchase consideration due)			
	Good will a/c Dr		30,000	
	Plant a/c Dr		18,300	
	Stock in trade a/c Dr		16,000	
	Sundry Debtors a/c Dr		7,500	
	Land a/c Dr		10,000	
	Cash a/c Dr		1,500	
	To Sundry Creditors a/c			3300
	To business a/c			80,000
	(Being assets and liabilities taken over from A Company)			
	Good will a/c Dr		2000	
	Plant a/c Dr		13450	
	Stock in trade a/c Dr		11550	
	Sundry Debtors a/c Dr		6000	
	Cash a/c Dr		1000	
	To Sundry Creditors a/c			2000
	To Business a/c			50000
	(Being assets and liabilities taken over from B Company)			
	Liquidators of A Company a/c Dr		80,000	
	Liquidators B Company a/c Dr		50,000	
	To share Capital a/c			1,30,000
	(Being the Purchase consideration paid)			

Balance Sheet of AB Company Ltd as on 1st January 2005

Liabilities	Rs	Assets	Rs
Issued Share Capital		Goodwill	50,000
13000 Shares of Rs.10 each	1,30,000	Land	10,000
Sundry creditors	5,300	Plant	31,750
		Stock in trade	27,550
		Sundry Debtors	13,500
		Cash	2,500
	1,35,300		1,35,300

Working Notes

Calculation of Purchase Consideration

		A Company	B Company
Various Assets taken over	Rs.	83,300	52,000
Less : Various liabilities taken over		3300	2,000
Purchase Consideration		80,000	50,000

External Reconstruction

External Reconstruction – Meaning

External Reconstruction mean the winding up of an existing company and transfer of its assets and liabilities to a new company formed to take the place existing company. It usually involves the conversion of shareholder of the existing company into the shareholders of the new company.

Composition of Amalgamation Absorption and External Reconstruction

	Amalgamation	Absorption	External Reconstructing
i)	Two or more similar companies go into liqudation	Small company goes into liquidation	One company goes into liquidation
ii	New Company formed is formed	New company is not formed	Same company is reformed ina anew name

1. The following is the balance sheet of play Boy as on 31st March 2008.

Liabilities	Rs	Assets	Rs
Authorized and issued		Goodwill	55,000
Share Capital		Sundry Assert	1,64,500
500 10% cumulative		Cash	500
preference shares of		Profit & Loss a/c	30,000
Rs.100 each, fully paid	50,000		
15,000 Equity shares of			
Rs.10 each fully paid	1,50,000		
7% debentures	20,000		
Sundry Creditors	30,000		
	2,50,000		2,50,000

A scheme of reconstruction detailed below was agreed upon:

a) Good Boy Ltd., a new company to be formed with authorized capital of Rs3,25,000 all in equity shares of Rs.10 each
b) One equity share (5 paid in the new company to be issued for each equity shares in the old company
c) 20 Equity shares (each Rs 5 paid up) in the new company to be issued for each cumulative preference shares in the old company.
d) Debenture holders to receive 2000 equity shares, fully equity in the new company
e) Sundry Creditors to be taken over by the new company
f) The remaining unissued equity shares to be taken over top a paid for in full by the direction
g) Good Boy Ltd to take over old company' s assets subject to a depreciation iof Rs.40000 and adjusting the goodwill as required

You are required to show the journal entries necessary to open the books of Good Bot Ltd. Show also the Balance sheet of Good Boy Ltd after having effect to the scheme.

Solution

Calculation of purchase Consideration

Equity Shares	:	15,000	Shares Rs.5 paid up	:	75,000
Preference Shares	:	10,000	Shares as Rs.5 paid up		5,000
Debenture holders	:	2,000	Shares as fully paid	;	20,000

Shares to be issued to Directors = 32,500 – 27,000 = 5,500

Journal Entries

In the Books of Good Boy Ltd

Date	Particulars	L.F	Debit Rs	Credit Rs
2008 Mar 31	Business Purchase a/c Dr To Liquidators of play Boy Ltd (Being the purchase consideration due)		1,45,000	 1,45,000
	Sundry Assets a/c Dr Cash a/c Dr Goodwill a/c (Bal.Fig) To Sundry Creditors a/c To Liquidator of play Boy Ltd. ac (Being the assets and liabilities taken over)		1,24,500 500 50,000	 30,000 1,45,000
	Liquidator of play Boy Ltd a/c Dr To Equity share capital a/c (Rs.5) To Equity share capital a/c (Rs.10) (Being discharge of purchase consideration)		1,45,000	 1,25,000 20,000
	Cash a/c Dr To Equity share Capital a/c (Being 5500 shares issued to directors)		55,000	 55,000

Balance Sheet of Good Boy as on 1st April 2008

Liabilities	Rs	Assets	Rs
Authorized Share Capital 32500 Equity shares of Rs. 10 each	 3,25,000	Goodwill Sundry Assets Cash (500 + 55000)	50,000 1,24,500 55,500
Issued& paid up: 25000 equity shares of Rs.10 each Rs.5 per share paid 7500 Equity shares of Rs.10 each fully paid (All party paid and 2000 fully paid shares have been issued for consideration) Sundry Creditors	 1,25,000 75,000 30,000		
	2,30,000		2,30,000

Internal Reconstruction

Internal Reconstruction

The claims of both the shareholders and creditors against a company with a bad or sinking financial position necessitate a scheme of capital reconstruction which is known as internal Reconstruction.

This arrangement made for one or more of the following shareholders

i) Reduction of share capital

ii) To difference the rights of different types of shareholders debenture holders and creditors

iii) To write off the accumulated losses of the company

iv) To reduce the overvaluation of assets of the company.

2. SAN Company Ltd. passed resolution and received sanction of the court for the reduction of share capital by Rd.2,50,000 After the arrangement, the credit balance of capita; reduction account was Rs.2,50,000. The amount available was utilized for write off profit and Loss a/c (Dr) 105000 reducing the value of plant and Machinery Rs.45000 Goodwill Rs.20000 Investment Rs.40,000. The balance available would be transferred to Capital Reserve. Pass Journal entry.

Solution

Date	Particulars	L.F	Debit Rs	Credit Rs
	Capital Reduction a/c Dr		2,50,000	
	To Profit and Loss a/c			1,05,000
	To Goodwill a/c			20,000
	To Plant and Machinery a/c			45,000
	To Investment a/c			40,000
	To Capital Reserve a/c (Bal.Fig)			40,000
	(Being accumulated losses & assets are reduced & balance is transferred to capital reserve)			