

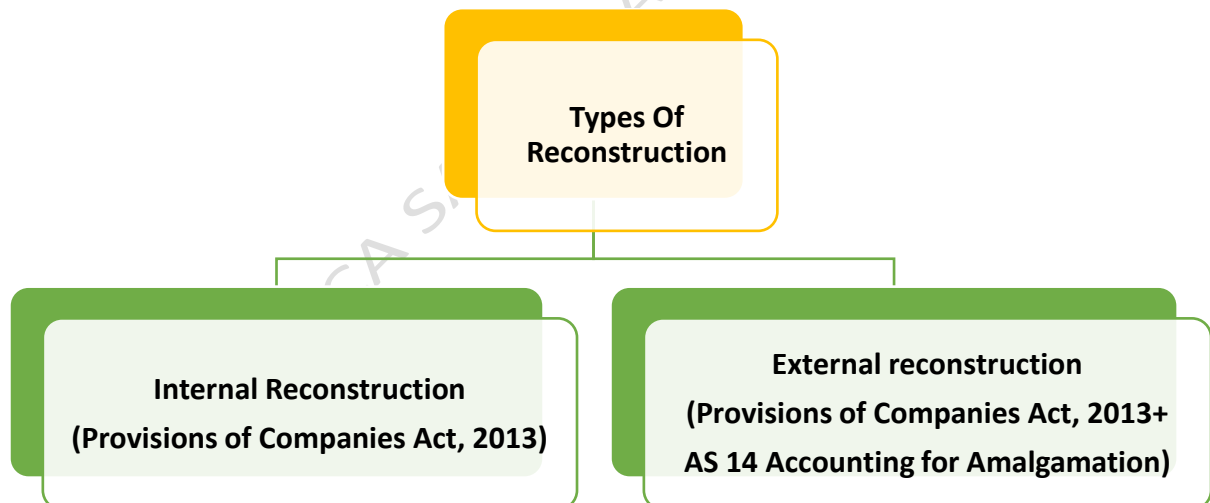
3.AMALGAMATION OF COMPANIES+AS-14

INTRODUCTION:

1. MEANING OF RECONSTRUCTION:

When a company has been making losses for several years, the financial position does not present a true and fair view of the state of the affairs of the company. In such a company the assets are generally overvalued, as the balance sheet consists of fictitious assets, unrepresented intangible assets and debit balance in the profit and loss account (showing the carry forward of losses). Such a situation always leads the company to show a higher net worth and not depicting a true picture of financial statements. In short, the company is over capitalized. Such a situation brings the need for reconstruction/reorganization of the affairs.

2. TYPES OF RECONSTRUCTION:



INTERNAL RECONSTRUCTION:

It is a process by which affairs of a company are reorganized by revaluation of assets, reassessment of liabilities and by writing off the losses already suffered, by reducing the paid-up value of shares and/or varying the rights attached to different classes of shares. The object of reconstruction is usually to reorganize capital or to compound with creditors, so that company can be bailed out from present situation without winding up the existing company.

EXTERNAL RECONSTRUCTION:

It is an undertaking is being carried on by a company and is in substance transferred, not to an outsider, but to another company consisting substantially of the same shareholders with a view to its

being continued by the transferee company. Such external reconstruction is essentially covered under the category of 'amalgamation in the nature of merger' in AS 14.

3. Difference Between Internal and External Reconstruction:

Basis	Internal Reconstruction	External Reconstruction
Liquidation and formation of new company	The existing company is not liquidated rather the capital and debt structure is changed to bring the company back to normalcy	The existing company is liquidated to form a new company in which the existing shareholders become shareholders of new company as well
Reduction of capital and varying rights	There is certain reduction of capital and sometimes the outside liabilities like debenture holders may have to reduce their claim in this scheme.	There is no reduction of capital. In fact, there is a fresh share capital of the company. The shareholders need not vary their rights in company
Legal position	Internal reconstruction is done as per provisions of section 61 and 66 of the Companies Act, 2013.	External reconstruction is regulated by section 232 of the Companies Act, 2013.
Legal formalities	It requires court's confirmation and other legal procedures before it can be implemented	It can be affected without the court's interference and less time-consuming process.

MEANING OF AMALGAMATION:

1. Amalgamation refers to the process of merger of two or more companies into a single entity or where one company takes over the other by outright purchase.
2. The term 'amalgamation' contemplates two kinds of activities:
 - a. Two or more companies join to form a new company or
 - b. Absorption and blending of one by the other.

3. This arrangement is sought by companies to receive various advantages such as economies of large-scale production, avoiding competition, increasing efficiency, expansion, increase in market share, etc
4. In amalgamation we have generally two companies called as –
 - a. Vendor or Transferor Company and
 - b. Vendee or Transferee Company.
5. Let us understand the concepts through the following examples

Example 1- Company A and Company B amalgamate to form Company C. Company A and Co B are called transferor companies and Company C is called as the transferee company- this strategy is called as AMALGAMATION.

Example 2- Company A is taken over by Company B (purchased). Here, Company A is called as Transferor Company and Company B is Transferee Company. This strategy is called as ABSORPTION.

Example 3- Company A has been suffering from losses for past 5 years, a new Company B is floated to take over the existing Company A. Here, Company A is the transferor company and Company B is Transferee Company. This strategy is termed as EXTERNAL RECONSTRUCTION.

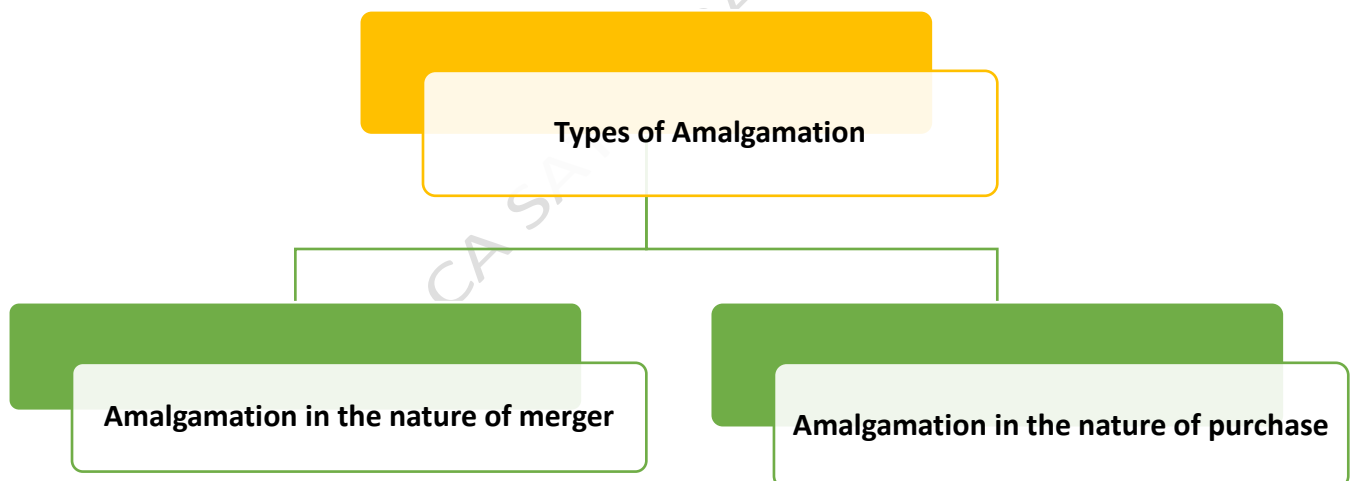
DIFFERENCE AMONG AMALGAMATION, ABSORPTION AND EXTERNAL RECNSTRUCTION:

Basis	Amalgamation	Absorption	External Reconstruction
Meaning	Two or more companies are wound up and a new company is formed to take over their business.	In this case an existing company takes over the business of one or more existing companies.	In this case, a newly formed company takes over the business of an existing company .
Minimum Number of companies involved	At least three companies are involved	At least two companies are involved	Only two companies are involved

Number of new resultant companies	Only one resultant company is formed. Two companies are wound up to form a single resultant company.	No new resultant company is formed.	Only one resultant company is formed. Under this case a newly formed company takes over the business of an existing company.
Objective	Amalgamation is done to cut competition & reap the economies in large scale.	Absorption is done to cut competition & reap the economies in large scale.	External reconstruction is done to reorganize the financial structure of the company.

TYPES OF AMALGAMATION:

- As per AS 14- "ACCOUNTING FOR AMALGAMATION", Amalgamation is of 2 types.



- Amalgamation in the nature of merger** is an amalgamation where there is a genuine pooling not only of assets and liabilities of the transferor and transferee companies but also of the shareholders' interests and of the businesses of the companies.

Amalgamation in the nature of merger is an amalgamation, which satisfies all the following conditions:

- All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.
- Shareholders holding not less than 90% of the face value of the equity shares of the transferor company (other than the equity shares already held therein, immediately before the amalgamation, by the transferee company or its subsidiaries or their nominees) become equity shareholders of the transferee company by virtue of the amalgamation.

- c. The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.
- d. The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company.
- e. No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies. For example, if transferor company is following weighted average method for inventory valuation, the book value of the inventory of the transferor company will be revised by applying the FIFO method (if the transferee company follows FIFO method for inventory valuation).

3. Amalgamation in the nature of purchase:

If any one or more of the above conditions are not satisfied in an amalgamation, such amalgamation is called amalgamation in the nature of purchase.

Difference between amalgamation in the nature of merger and amalgamation in the nature of purchase

Best of Distinction	Amalgamation in the Nature of Merger	Amalgamation in the Nature of Purchase
(a) Transfer of Assets and Liabilities	There is transfer of all assets & liabilities.	There need not be transfer for all assets & liabilities.
(b) Shareholders of transferor company	Equity shareholders holding 90% equity shares in transferor company become shareholders of transferee company.	Equity shareholders need not become shareholders of transferee company.

(c) Purchase Consideration	Purchase consideration is discharged wholly by issue of equity shares of transferee company (except cash only for fractional shares)	Purchase consideration need not be discharged wholly by issue of equity shares.
(d) Same Business	The same business of the transferor company is intended to be carried on by the transferee company.	The business of the transferor company need not be intended to be carried on by the transferee company.
Recording of Assets & Liabilities	The assets & liabilities taken over are recorded at their existing carrying amounts except where adjustment is required to ensure uniformity of accounting policies.	The assets & liabilities taken over are recorded at their existing carrying amounts or the basis of their fair values.
(f) Method of Accounting	Journal entries for recording the merger are passed by pooling of interest method.	Journal entries for recording the purchase of business are passed by purchase method.

PROBLEMATIC TOPICS

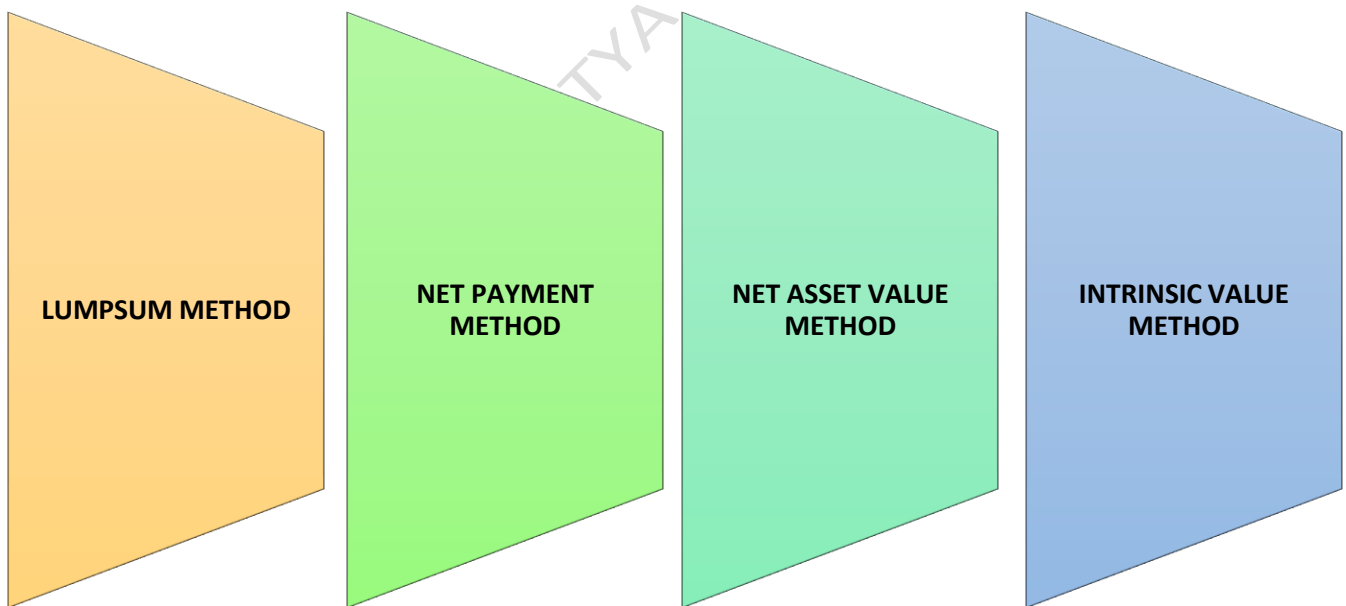
CALCULATION OF
PURCHASE
CONSIDERATION

ACCOUNTING
TREATMENT IN THE
BOOKS OF VENDOR
COMPANY

ACCOUNTING
TREATMENT IN THE
BOOKS OF PURCHASING
COMPANY

PURCHASE CONSIDERATION:

1. As per AS-14, Purchase consideration is the “aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company”.
2. In simple words, it is the price payable by the transferee company to the transferor company for taking over the business of the transferor company.
3. The important point to be noted here is the amount paid towards the equity shareholders and preference shareholders is only considered as part of the purchase consideration as per the definition under AS-14. Hence, it should be noted that purchase consideration does not include the sum which the transferee company will directly pay to the debenture-holders or creditors of the transferor company.

METHODS OF PURCHASE CONSIDERATION:**1. LUMP SUM METHOD:**

Under this method, the transferee company agrees to pay a lumpsum/fixed amount to shareholders of the transferor company.

2. NET PAYMENT METHOD:

Under this method the transferee company makes individual payments to the equity shareholders and preference shareholders either by way of cash, issue of shares and debentures etc.

3. NET ASSET VALUE METHOD:

Under this method, the purchase consideration is arrived based on the value of the Assets less the outside liabilities (excluding share capital and reserves) taken over by the transferee company. As

per AS 14, the value of the assets and liabilities shall be at the value as agreed between the two parties. If there is no value agreed, then assets and liabilities taken at the book value.

4. **INTRINSIC VALUE METHOD:**

Under this method, the purchase consideration is calculated at the intrinsic value of shares of the transferor company.

Purchase consideration= Number of shares in transferor co. x Intrinsic value per share in transferor co.

➤ **Number of shares issued as Purchase consideration by transferee company**

Number of shares in transferor co. x Intrinsic value per share in transferor co.
Intrinsic value per share in transferee co.

NOTE: Any of the methods or a combination of the above methods can be used by the companies to calculate the purchase consideration.

Meaning of purchase consideration recorded at par value:

1. In generally purchase consideration will be recorded at Issue value.

I.e **Number of shares issued as P.C x Issue price per share**

2. If Management decide to record P.C at par value, then

Purchase consideration= Number of shares issued as P.C x Face value per share

ACCOUNTING TREATMENT IN THE BOOKS OF VENDOR COMPANY:

1. AS-14 is not applicable for Accounting in Vendor company. To close the books of selling company during the process of Amalgamation we will apply General Accounting principles related to closure of Books of Accounts.

2. **FIVE STEP APPROACH:**

STEP1: DISMANTLING OF BALANCE SHEET

- a. All Assets and Liabilities which are taken over by purchasing company will be closed and transferred to Realization a/c at book values.
- b. If any particular Asset or Liability which is not taken over by purchasing company, opened separately for the purpose of realization in outside market.
- c. Preference share capital will be transferred to Preference shareholders a/c.
- d. Equity share capital, Reserves & Surplus, Fictious Assets transferred to Equity shareholders a/c.

STEP 2: PURCHASE CONSIDERATION DUE

- a. Calculate Purchase consideration by providing separate working note.
- b. With the amount of Purchase consideration Debit the Purchasing company a/c and Credit the Realization a/c.

STEP3: PURCHASE CONSIDERATION RECEIVED

Purchasing Co. A/c will be closed by debiting the Equity shares of Purchasing co., Preference shares of purchasing co., Debentures of purchasing co., Cash etc.

STEP4: DISTRIBUTION OF PURCHASE CONSIDERATION

- a. Dispose those assets which are not taken over by the purchasing company in out side market and any profit or loss derived transferred to Realization a/c.
- b. With the available cash and P.c received by the Transferor co. will be distributed among various parties in particular order decided by Liquidation provisions.
 - (i) Realization expenses/Liquidation expenses
 - (ii) Secured creditors
 - (iii) Un secured creditors
 - (iv) Preference shareholders
 - (v) Finally Equity share holders

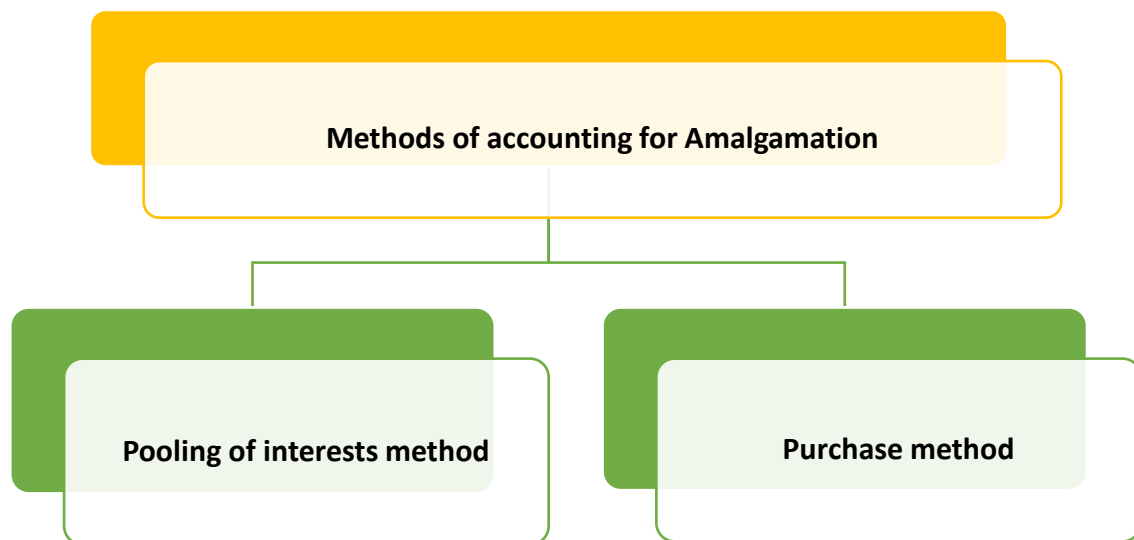
During this process of distribution any profit or loss derived will be transferred to Realization a/c.

STEP5: FINAL SETTLEMENT TO EQUITY SHAREHOLDERS

- a. Before making settlement to Equity shareholders, close Realization a/c and find Realization profit or loss. Such profit or loss will be transferred to Equity shareholders a/c.
- b. All the remaining Resources in selling company just distribute among Equity shareholders. All accounts in Selling company will be closed with this final step.

ACCOUNTING TREATMENT IN THE BOOKS OF PURCHASING COMPANY:

There are two main methods of accounting for amalgamation in purchasing company books. The first method is used in case of amalgamation in the nature of merger where the conditions as per AS-14, required are fulfilled and the second method is used in case of amalgamation in the nature of purchase.



Pooling of Interest Method

1. Under pooling of interest method, the assets, liabilities and reserves of the Transferor Company will be taken over by Transferee Company at existing carrying amounts unless any adjustment is required due to different accounting policies followed by these companies.
2. As a result the difference between the amount recorded as share capital issued as p.c and the amount of share capital of Transferor Company should be adjusted in the reserves of the financial statements of Transferee company .i.e Recorded as deduction from the reserves where the p.c issued is more than the capital of the transferor company, Otherwise treated as capital Reserve.
3. In simple terms, where in case of pooling method- the amount to be adjusted against the reserves- can be computed in the following 3 steps

Step I- Equity Share capital + Preference share capital issued+ any other additional consideration in form of cash and other assets by the Transferee Company.

Step II- Existing Equity share capital + Existing Preference share capital in the books of Transferor Company.

Step III- Step I- Step II= amount to be adjusted from the reserves of Transferee company or Capital reserve.

Purchase Method

1. Assets and Liabilities:

The assets and liabilities of the transferor company should be incorporated at their existing carrying amounts or the purchase consideration should be allocated to individual identifiable assets and liabilities on the basis of their fair values at the date of amalgamation.

2. Difference between the Purchase Consideration and Net Assets transferred:

- a. Any excess of the amount of purchase consideration over the value of the net assets of the transferor company acquired by the transferee company should be recognized as goodwill in the financial statement of the transferee company. Any short fall should be shown as capital reserve. Goodwill should be amortized over period of five years unless a somewhat longer period can be justified.
- b. In simple terms, where in case of purchase method- the amount to be transferred to capital reserve or to be recorded as Goodwill- can be computed in the following 3 steps.

Step I- Find out the Net assets amount using the following formula- Total assets-Outside liabilities (Non-current liabilities + Current Liabilities)

Step II- Compute the purchase consideration using any of the methods as given under Purchase consideration computation.

Step III-

- a. If Step I- Step II= Positive amount- then it is capital reserve- since the assets received more than the amount paid as purchase consideration to acquire them.
- b. If Step I- Step II= Negative amount- then it is to be recorded as Goodwill (intangible asset) - since the amount paid for acquiring business is more than the Net assets, which is technically due to its goodwill.

3. Treatment of reserves under purchase method

- a. No reserves, other than statutory reserves, of the transferor company should be incorporated in the financial statements of transferee-company. The balance of Profit and Loss account, general reserves of the transferor company are not recorded at all.
- b. Though, normally, in an amalgamation in the nature of purchase, the identity of reserves is not preserved, an exception is made only in respect of statutory reserves and such reserves shall retain their identity in the financial statements of the transferee company in the same form in which they appeared in the financial statements of the transferor company, till the time their identity is required to be maintained to comply with the relevant statute.
- c. Statutory reserves of the transferor company should be incorporated in the balance sheet of transferee company by way of the following journal entry.

Amalgamation Adjustment Reserve A/c Dr.

To Statutory Reserves

- d. 'Amalgamation Adjustment Reserve' is debited to bring in the statutory reserves of the transferor company. This is represented as deduction from the reserves of the transferee company after amalgamation. Once after the time period to show such statutory reserves is over, both the reserves and the aforesaid account are reversed.

Typical adjustments which shall be noted while working out the problems –

1. **Inter Company-owing** - Should the purchasing company owe an amount to the vendor company or vice versa, the amount will be included in the book debts of one company and trade payables of the other. This should be adjusted by the entry:

Trade payables	Dr.	XXXX	
To Trade receivables			XXXX

2. **Adjustment of the value of stock**

Inter-company owings arise usually from purchase and sale of goods; it is likely, therefore, that at the time, of the sale of business, the debtor company also has goods in stock which it purchased from the creditor company - the cost of the debtor company will include the profit made by the creditor company. After the takeover of the business it is essential that such a profit is eliminated. This should be adjusted by the entry:

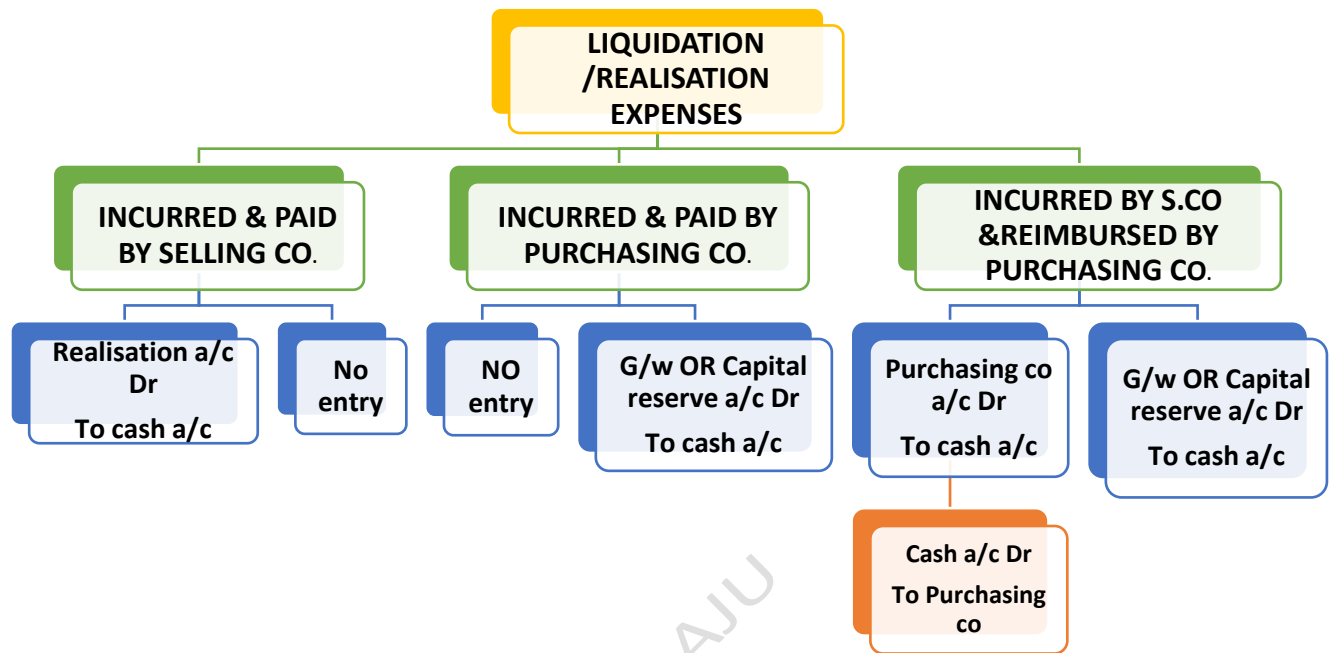
Good will/Capital reserve A/C	Dr	XXXX	
TO Stock reserve A/C			XXXX

3. **Inter-company Loans**

Where there is any loan taken by the transferor company from the transferee company then the amount of the loan shall be taken over by the transferee company and adjustment entry to be passed as follows:

Loan (liability of Transferor co) A/c	Dr	XXXX	
To Loans and advances (assets)			XXXX

4. LIQUIDATION/REALISATION EXPENSES



PROBLEMS FOR DISCUSSION

PROBLEM 1:

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

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

Notes to accounts:

	Rs.
1. Share Capital	
Equity Share capital (Rs. 100 each)	8,00,000
6% Preference Share capital (Rs. 100 each)	<u>4,00,000</u>

		<u>12,00,000</u>
2.	Reserves and Surplus	
	Capital reserve	1,00,000
	Profit and loss A/c	50,000
	Workmen compensation reserve (Expected liability Rs. 5,000)	8,000
		<u>1,58,000</u>
3.	Long-term borrowings	
	6% Debentures	<u>2,00,000</u>
		<u>2,00,000</u>
4.	Property, Plant and Equipment	
	Land and Building	4,00,000
	Plant and machinery	<u>6,00,000</u>
		<u>10,00,000</u>
5.	Intangible assets	
	Goodwill	2,40,000
	Patents	<u>50,000</u>
		<u>2,90,000</u>

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

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

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

Requirements:

- Calculate Purchase consideration.

(ii) Provide Journal entries in the books of Vendor co. and also provide closing Ledgers

(iii) Provide Journal entries in the books of Purchasing company.

(SM)

PROBLEM 2:

S. Ltd. is absorbed by P. Ltd. The draft balance sheet of S. Ltd. is as under:

Balance Sheet

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

P. Ltd. has agreed:

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

You are required to calculate the purchase consideration.

(SM)

PROBLEM 3:

Neel Ltd. and Gagan Ltd. amalgamated to form a new company on 1.04.2015. Following is the Draft Balance Sheet of Neel Ltd. and Gagan Ltd. as at 31.3.2015:

Liabilities	Neel	Gagan	Assets	Neel	Gagan
Capital	7,75,000	8,55,000	Plant & Machinery	4,85,000	6,14,000

Current Liabilities	6,23,500	5,57,600	Building	7,50,000	6,40,000
			Current assets	1,63,500	1,58,600
	13,98,500	14,12,600		13,98,500	14,12,600

Following are the additional information:

1. The authorised capital of the new company will be Rs. 25,00,000 divided into 1,00,000 equity shares of Rs. 25 each.
2. Liabilities of Neel Ltd. includes Rs. 50,000 due to Gagan Ltd. for the purchases made. Gagan Ltd. made a profit of 20% on sale to Neel Ltd.
3. Neel Ltd. had purchased goods costing Rs. 10,000 from Gagan Ltd. All these goods are included in the current asset of Neel Ltd. as at 31st March, 2015.
4. The assets of Neel Ltd. and Gagan Ltd. are to be revalued as under:

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

5. The purchase consideration is to be discharged as under:
 - b) Issue 24,000 equity shares of Rs. 25 each fully paid up in the proportion of their profitability in the preceding 2 years.
 - c) Profits for the preceding 2 years are given below:

Particulars	Neel	Gagan
1 st year	2,62,800	2,75,125
2 nd year	2,12,200	2,49,875
Total	4,75,000	5,25,000

- d) Issue 12% preference shares of Rs. 10 each fully paid up at par to provide income equivalent to 8% return on net assets in the business as on 31.3.2015 after revaluation of assets of Neel Ltd. and Gagan Ltd. respectively.

You are required to compute the

1. Equity and preference shares issued to Neel Ltd. and Gagan Ltd.,
2. Purchase consideration.

(SM)

PROBLEM 4:

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

Particulars				
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	100,00
	B	Reserves and Surplus	2	12,50
2		Non-current liabilities		
	A	Long-term borrowings	3	40,00
3		Current liabilities		
	A	Trade Payables		20.00
		Total		172,50
		Assets		
1		Non-current assets		
	A	Property, Plant and Equipment	4	105,50
	B	Non-current investments	5	5,00
2		Current assets		
	a	Inventories		23,00
	b	Trade receivables		24,00
	c	Cash and Cash equivalents		15,00
		Total		172,50

Notes to accounts

1.	Share Capital		Rs. in ('000)
	Equity share capital		75,00
	7.50,000 Equity Shares of Rs. 10 each		
	25,000 14% Preference Shares of Rs. 100 each		25,00
			100.00
2	Reserves and Surplus		12,50
	General reserve		
			12,50
3	Long-term borrowings		

	Secured		
	14% Debentures		40,00
			40,00
4	Property, plant and Equipment		50,00
	Land and Building		
	Plant and machinery		45,00
	Furniture		10.50
			105.50
5	Non-current investments		
	Investments at cost		5,00
			5.00

Other Information:

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

PROBLEM 5:

The following draft Balance Sheets are given as on 31st March, 2014:

Liabilities	(in lakhs)		Assets	(in lakhs)	
	Best Ltd	Better Ltd		Best Ltd	Better Ltd
Share Capital:			Fixed Assets	25	15
Shares of Rs. 100, each fully paid	20	10	Investments	5	-
Reserve and Surplus	10	8	Current Assets	20	5
Other Liabilities	20	2			
	50	20		50	20

The following further information is given:

- a) Better Limited issued bonus shares on 1st April, 2014, in the ratio of one share for every two held, out of Reserves and Surplus.
- b) It was agreed that Best Ltd. will take over the business of Better Ltd., on the basis of the latter's Balance Sheet, the consideration taking the form of allotment of shares in Best Ltd.
- c) The value of shares in Best Ltd. was considered to be Rs. 150 and the shares in Better Ltd. were valued at Rs. 100 after the issue of the bonus shares. The allotment of shares is to be made on the basis of these values.
- d) Liabilities of Better Ltd., included Rs. 1 lakh due to Best Ltd., for purchases from it, on which Best Ltd., made profit of 25% of the cost. The goods of Rs. 50,000 out of the said purchases, remained in stock on the date of the above Balance Sheet.

Make the closing ledger in the Books of Better Ltd. and the opening journal entries in the Books of Best Ltd., and prepare the Balance Sheet as at 1st April, 2014 after the takeover. **SM**

PROBLEM 6:

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

Balance Sheet of K Ltd. And L Ltd.

			Particulars	Notes No.	K Ltd (Rs.)	L Ltd (Rs.)
			1	2	3	4
1			EQUITY AND LIABILITIES:			
			Shareholder's funds			
	a		Share capital	1	12,00,000	6,00,000
	b		Reserves and Surplus	2	3,71,375	1,97,175
2			Non-current liabilities			
	a		Long term borrowings			
			5% Debentures		2,00,000	-
			Secured loan		-	2,00,000

3		Current liabilities			
	a	Trade Payable (Creditors)		1,00,000	2,10,000
		TOTAL		18,71,375	12,07,175
1		ASSETS:			
		Non-current assets			
	a	Fixed assets			
	(i)	Tangible assets	3	11,30,000	8,20,000
	(ii)	Intangible assets	4	80,000	-
2		Current Assets			
	a	Inventories (Stock)		2,25,000	1,40,000
	b	Trade receivables (Debtors)		2,75,000	1,75,000
	c	Cash and cash equivalents	5	1,61,375	72,175
		TOTAL		18,71,375	12,07,175

Note to Accounts:

Particulars	K Ltd (Rs.)	L Ltd (Rs.)
1. Share capital		
Equity Shares of Rs.100 each	8,00,000	3,00,000
7% Preference Share of Rs.100 each	4,00,000	3,00,000
2. Reserves and Surplus		
General Reserve	-	1,00,000
Profit and Loss A/c	3,71,375	97,175
3. Tangible Assets		
Land & Building	4,50,000	3,00,000
Plant & Machinery	6,20,000	5,00,000
Furniture & Fittings	60,000	20,000
4. Intangible Assets		
Goodwill	80,000	-

5. Cash and cash equivalents		
Cash at Bank	1,20,000	55,000
Cash in hand	41,375	17,175

The terms of amalgamation are as under:

A)

1. The assumption of assets and liabilities of both the Companies
2. Issue of 5 Preference shares of Rs.20 each in LK Ltd @ Rs.18 paid up at premium of Rs.4 per share for each preference share held in both the Companies.
3. Issue of 6 Equity shares of Rs.20 each in LK Ltd. @ Rs.18 paid up at a premium of Rs.4 per share for each equity share held in both the Companies. In addition necessary cash should be paid to the Equity Shareholders of both the Companies as is required to adjust the rights of shareholders of both the companies in accordance with the intrinsic value of the shares of both the companies.
4. Issue of such amount of fully paid 6% debentures in LK Ltd. as is sufficient to discharge the 5% debentures in K Ltd at a discount of 5% after takeover.

B)

1. The assets and liabilities are to be taken at book values Inventory and Trade receivables for which provisions at 2% and 2 ½ % respectively to be raised.
2. The trade receivables of K Ltd. included Rs.20,000 due from L Ltd.

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

(SM)

PROBLEM 7:

The following are the summarized Balance Sheets of A Ltd. and B Ltd. as on 31.3.20X1:

Particulars	(Rs.in thousands)	
LIABILITIES	A Ltd.	B Ltd.
Share capital:		
Equity shares of 100 each fully paid up	2,000	1,000
Reserves	1,000	---
10% Debentures	500	---

Loans from Banks	250	450
Bank overdrafts	---	50
Trade payables	300	300
Total	4,050	1,800
ASSETS		
Tangible assets/fixed assets	2,700	850
Investments	700	---
Trade receivables	400	150
Cash at bank	250	---
Accumulated loss	---	800
Total	4,050	1,800

B Ltd. has acquired the business of A Ltd. The following scheme of merger was approved:

- i) Banks agreed to waive off the loan of Rs.60 thousand of B Ltd.
- ii) B Ltd. will reduce its shares to Rs. 10 per share and then consolidate 10 such shares into one share of Rs. 100 each (new share).
- iii) Shareholders of A Ltd. will be given one share (new) of B Ltd. in exchange of every share held in A Ltd.
- iv) Trade payables of B Ltd. includes Rs. 1,00,000 payable to A Ltd.

Pass necessary entries in the books of B Ltd. and prepare Balance Sheet after merger. **(SM)**

PROBLEM 8:

The financial position of two companies Hari Ltd. and Vayu Ltd. as on 31st march, 2015 was as under:

Name of the Companies : Hari Ltd and Vayu Ltd

Balance Sheet as at : 31st march 2012

		Particulars	Notes No.	Hari Ltd (Rs.)	Vayu Ltd (Rs.)
		1	2	3	4
1		EQUITY AND LIABILITIES:			
		Shareholder's funds			
	a	Share capital	1	11,00,000	4,00,000
	b	Reserves and Surplus	2	70,000	70,000
2		Current liabilities			
	a	Trade Payable (sundry creditors)		1,30,000	80,000

	b	Short term provisions (Retirement and gratuity fund)		50,000	20,000
		TOTAL		13,50,000	5,70,000
		ASSETS:			
		Non-current assets			
1	a	Fixed assets			
	I	Tangible assets	3	8,00,000	2,50,000
	II	Intangible assets (Good will)		50,000	25,000
		Current Assets			
	a	Inventories (Stock)		2,50,000	1,75,000
2	b	Trade receivables (Debtors)		2,00,000	1,00,000
	c	Cash and cash equivalents (Cash at bank)		50,000	20,000
		TOTAL		13,50,000	5,70,000

Notes to Accounts:

Particulars	Hari (Rs.)	Vayu (Rs.)
1. Shareholder's funds:		
Equity share capital (Rs.10 each)	10,00,000	3,00,000
9% preference share capital (Rs.100 each)	1,00,000	-
10% preference share capital (Rs.100 each)	-	1,00,000
2. Reserves and Surplus:		
General reserve	70,000	70,000
3. Tangible assets:		
Building	3,00,000	1,00,000
Machinery	5,00,000	1,50,000

Hari Ltd. absorbs Vayu Ltd. on the following terms:

- 10% Preference Shareholders are to be paid at 10% premium by issue of 9% Preference Shares of Hari Ltd.
- Goodwill of Vayu Ltd. is valued at Rs.50,000, Buildings are valued at Rs.1,50,000 and the Machinery at Rs.1,60,000.

3. Inventory to be taken over at 10% less value and Provision for Doubtful Debts to be created @ 7.5%.
4. Equity Shareholders of Vayu Ltd. will be issued Equity Shares @ 5% premium.

Prepare necessary Ledger Accounts to close the books of Vayu Ltd. and Show the acquisition entries in the books of Hari Ltd. Also draft the Balance Sheet after absorption as at 31st March, 2015.

(SM)

PROBLEM 9:

Consider the following summarized balance sheets of X Ltd. and Y Ltd.

Balance sheet as on 31st March, 20X1

Liabilities	X Ltd (Rs.000)	Y Ltd. (Rs.000)	Assets	X Ltd (Rs.000)	Y Ltd. (Rs.000)
Equity share capital (Rs. 10 each)	50,00	30,00	Land & Building	25,00	15,50
14% Preference share Capital (Rs.100 each)	22,00	17,00	Plant & Machinery	32,50	17,00
General reserve	5,00	2,50	Furniture & Fittings	5,75	3,50
Export profit reserve	3,00	2,00	Investment	7,00	5,00
Investment allowance Reserve		1,00	Inventory	12,50	9,50
Profit & Loss A/c	7,50	5,00	Trade receivables	9,00	10,30
13% Debentures (Rs.100 each)	5,00	3,50	Cash & Bank	7,25	5,20
Trade payables	4,50	3,50			
Other current liabilities	2,00	1,50			
	99,00	66,00		99,00	66,00

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

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

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

Show the balance sheet of X Ltd. after amalgamation on the assumption that:

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

(SM)

PROBLEM 10:

Super Express Ltd. and Fast Express Ltd. were in competing business. They decided to form a new company named Super-Fast Express Ltd. The summarized balance sheets of both the companies were as under:

Name of the Companies : Super Ltd and Fast Ltd

Balance Sheet as at : 31st march 2014

			Particulars	Notes No.	Super express Ltd. (Rs.)	Fast express Ltd. (Rs.)
			1	2	3	4
1			EQUITY AND LIABILITIES:			
			Shareholder's funds			
	A		Share capital	1	20,00,000	10,00,000
	B		Reserves and Surplus	2	1,00,000	2,60,000
2			Current liabilities			
	A		Trade Payable (sundry creditors)		60,000	40,000
	B		Short term provisions (Provident fund)		1,00,000	-
			TOTAL		22,60,000	13,00,000
1			ASSETS:			
			Non-current assets			
	A		Fixed assets			
		I	Tangible assets	3	14,00,000	11,00,000
		II	Intangible assets (Goodwill)		-	1,00,000
2			Current Assets			
	A		Inventories (Stock)		3,00,000	40,000
	B		Trade receivables (Debtors)		2,40,000	40,000

	C	Cash and cash equivalents	4	3,20,000	20,000
		TOTAL		22,60,000	13,00,000

Notes to Accounts:

Particulars	Super express	Fast express
1. Shareholder's funds		
20,000 equity shares of Rs.100 each	20,00,000	-
10,000 equity shares of Rs.100 each		10,00,000
2. Reserves and Surplus		
Insurance reserve	1,00,000	-
Employees profit sharing account	-	60,000
Reserve account	-	1,00,000
Surplus	-	1,00,000
3. Tangible assets		
Building	10,00,000	6,00,000
Machinery	4,00,000	5,00,000
4. Cash and cash equivalents		
Cash at bank	2,20,000	10,000
Cash in hand	1,00,000	10,000

The assets and liabilities of both the companies were taken over by the new company at their book values. The companies were allotted equity shares of Rs.100 each in lieu of purchase amounting to 30,000 shares, (20,000 for Super-Fast express Ltd. and 10,000 for fast express Ltd.). Decide type of Amalgamation and Prepare opening balance sheet of Super-Fast Express Ltd. **(SM)**

PROBLEM 11:

Galaxy Ltd. and Glory Ltd., are two companies engaged in the same business of chemicals. To mitigate competition, a new company Glorious Ltd, is to be formed to which the assets and liabilities of the existing companies, with certain exception, are to be transferred. The summarized Balance Sheet of Galaxy Ltd. and Glory Ltd. as at 31st March, 2020 are as follows.

				Galaxy Ltd.	Glory Ltd.
				Rs.	Rs.

(I)	Equity & Liabilities			
	(1) Shareholders' fund			
	<u>Share Capital</u>			
	Equity shares of Rs. 10 each		8,40,000	4,55,000
	<u>Reserves & Surplus</u>			
	General Reserve		4,48,000	40,000
	Profit & Loss A/c		1,12,000	72,000
	(2) Non-current Liabilities			
	Secured Loan-6% Debentures		-	3,30,000
	(3) Current Liabilities			
	Trade Payables		4,20,000	1,83,000
	Total		18,20,000	10,80,000
(II)	Assets			
	(1) Non-current assets			
	<u>Property, Plant & Equipment</u>			
	Freehold property, at cost		5,88,000	3,36,000
	Plant & Machinery, at cost less depreciation		1,40,000	84,000
	Motor vehicles, at cost less depreciation		56,000	-
	(2) Current Assets			
	Inventories		3,36,000	4,38,000
	Trade Receivables		4,62,000	1,18,000
	Cash at Bank		2,38,000	1,04,000
	Total		18,20,000	10,80,000

Assets and Liabilities are to be taken at book value, with the following exceptions:

1. The Debentures of Glory Ltd. are to be discharged, by the issue of 8% Debentures of Glorious Ltd. at a premium of 10%.
2. Plant and Machinery of Galaxy Ltd. are to be valued at Rs. 2,52,000.
3. Goodwill is to be valued at : Galaxy Ltd. Rs. 4,48,000 Glory Ltd. Rs. 1,68,000

4. Liquidator of Glory Ltd. is appointed for collection from trade debtors and payment to trade creditors. He retained the cash balance and collected Rs. 1,10,000 from debtors and paid Rs. 1,80,000 to trade creditors. Liquidator is entitled to receive 5% commission for collection and 2.5% for payments. The balance cash will be taken over by new company.

You are required to:

- A. Compute the number of shares to be issued to the shareholders of Galaxy Ltd. and Glory Ltd, assuming the nominal value of each share in Glorious Ltd. is Rs. 10.
- B. Prepare Balance Sheet of Glorious Ltd., as on 1st April, 2020 and also prepare notes to the accounts as per Schedule III of the Companies Act, 2013. **(QP-JAN 2021-Q.NO.2)**

PROBLEM 12:

The summarized Balance Sheets of Black Limited and White Limited as on 31st March, 2020 is as follows:

Particulars	Notes	Black Limited (Rs. In 000)	White Limited (Rs. In 000)
Equity and Liabilities			
Shareholders' Funds			
(a) Share Capital	1	6,000	3,600
(b) Reserves and Surplus	2	1,080	660
Current Liabilities			
Trade payables		600	360
Total		7,680	4,620
Assets			
Non-current assets			
Property, Plant and Equipment		3,600	2,400
Current assets			
(a) Inventories		960	720
(b) Trade receivables		1,680	1,080
(c) Cash and Cash Equivalents		1,440	420
Total		7,680	4,620

Note No.	Particulars	Black Limited (Rs. in 000)	White Limited (Rs. in 000)
1.	Share Capital Equity Shares of Rs. 100 each	6,000	3,600
	Reserves and Surplus		
2.	General Reserve	360	180
	Profit and Loss Account	720	480
	Total	1,080	660

1. Black Limited takes over White Limited on 1st July, 2020.
 2. No Balance Sheet of White Limited is available as on that date. It is, however estimated that White Limited earned profit of Rs. 2,40,000 after charging proportionate depreciation @ 10% p.a. on Property Plant and Equipment, during April-June, 2020.
 3. Estimated profit of Black Limited during these 3 months was Rs. 4,80,000 after charging proportionate depreciation @ 10% p.a. on Property Plant and Equipment
 4. Both the companies have declared and paid 10% dividend within this 3 months' period.
 5. Goodwill of White Limited is valued at Rs. 2,40,000 and Property Plant and Equipment are valued at Rs. 1,20,000 above the depreciated book value on the date of takeover.
 6. Purchase consideration is to be satisfied by Black Limited by issuing shares at par.
- Ignore income tax. You are required to:
- (i) Compute No. of shares to be issued by Black Limited to White Limited against purchase consideration.
 - (ii) Calculate the balance of Net Current Assets of Black Limited and White Limited as on 1st July, 2020.
 - (iii) Give balance of Profit or Loss of Black Limited as on 1st July, 2020
 - (iv) Give balance of Property Plant and Equipment as on 1st July, 2020 after takeover.

(QP-JULY 2021-5(a))

PROBLEM 13:

High Ltd. and Low Ltd. were amalgamated on and from, 1st April, 2020. A new company Little Ltd. was formed to take over the business of the existing Companies. The summarized Balance sheets of High Ltd. and Low Ltd. as on 31st March, 2020 are as under:

(Rs. in Lakhs)

Liabilities	High Ltd.	Low Ltd.	Assets	High Ltd.	Low Ltd.
Share Capital:			Property, Plant and Equipment:		
Equity Shares of Rs. 100 each	1000	850	Land & Building	670	385
14% Pref Shares of Rs. 100 each	320	175	Plant & Machinery	475	355
Reserves & Surplus:			Investments	95	80
Revaluation Reserve	225	110	Current Assets:		
General Reserve	360	240	Stock	415	389
Investment Allowance Reserve	80	40	Sundry Debtors	322	213
P & L Account	85	82	Bills Receivables	35	-
Non-Current Liabilities:			Cash & Bank	303	166
Secured Loans:					
13% Debentures (Rs. 100 each)	100	56			
Unsecured Loans (Public Deposits)	50	-			
Current Liabilities & Provisions:		-			
Sundry Creditors	65	35			
Bills Payable	30	-			
TOTAL	2315	1588	TOTAL	2315	1588

Other Information:

- (1) 13% Debenture holders of High Ltd. & Low Ltd. are discharged by Little Ltd. by issuing such number of its 15% Debentures of Rs. 100 each so as to maintain the same amount of interest.
- (2) Preference Shareholders of the two companies are issued equivalent number of 15% Preference shares of Little Ltd. at a price of Rs. 125 per share (Face Value Rs. 100)
- (3) Little Ltd. will issue 4 Equity Shares for each Equity Share of High Ltd. & 3 equity shares for each Equity Share of Low Ltd. The shares are to be issued at Rs. 35 each having a face value of Rs. 10 per share.

(4) Investment Allowance Reserve is to be maintained for two more years.

Prepare the Balance sheet of Little Ltd. as on 1st April, 2020 after the amalgamation has been carried out in basis of in the nature of Purchase.

(QP-Nov 2020 -3(a))

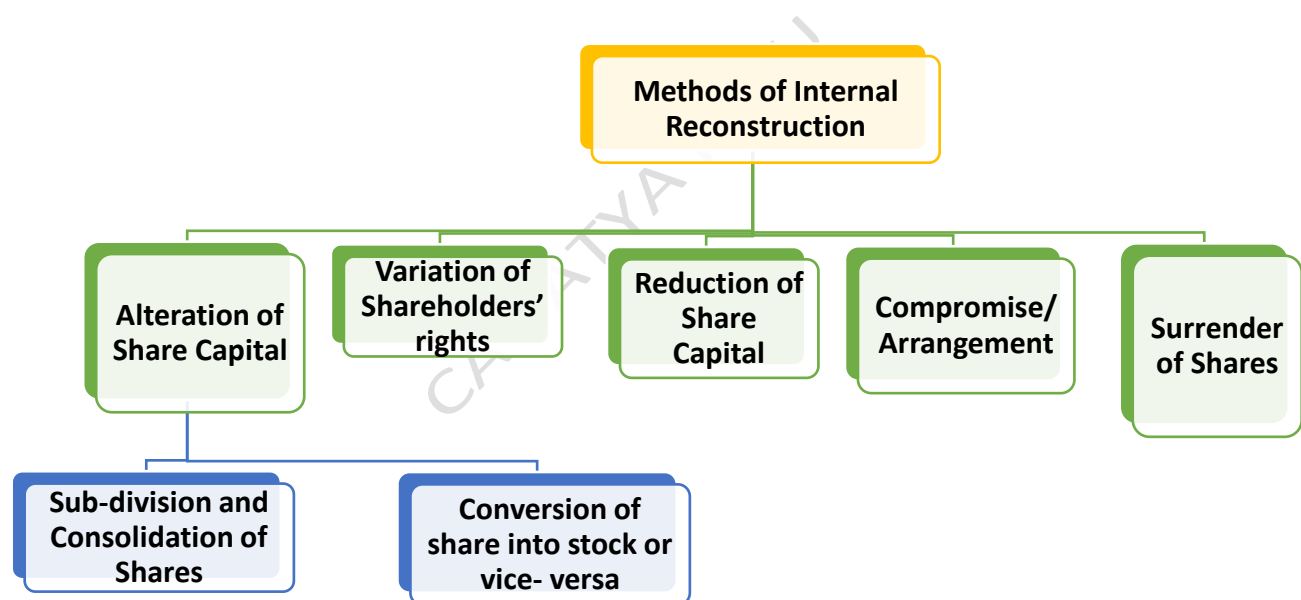
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4.ACCOUNTING FOR RECONSTRUCTION OF COMPANIES

INTERNAL RECONSTRUCTION:

It is a process by which affairs of a company are reorganized by revaluation of assets, reassessment of liabilities and by writing off the losses already suffered, by reducing the paid-up value of shares and/or varying the rights attached to different classes of shares. The object of reconstruction is usually to reorganize capital or to compound with creditors so that company can be bailed out from present situation without winding up the existing company.

METHODS OF INTERNAL RECONSTRUCTION:



1. Alteration of Share Capital:

According to the Section 61 of the Companies Act 2013, a limited company can alter its share capital, if so authorized by its Articles, by passing an ordinary resolution in the general meeting.

The following types of Alteration can be done under Section 61

- a. Increase of authorized share capital;
- b. Consolidation and sub-division into shares of larger or smaller denominations;
- c. Conversion of all or any of the shares into stock or vice versa;
- d. Cancellation of shares which have not been taken or agreed to be taken by any person.

2. Variation of Shareholders Rights

Section 48 of the Companies Act, 2013 provides that when a company has issued different classes of shares with different rights or privileges attached to such shares e.g. rights as to dividend, voting rights etc., any of such right may be changed in any manner.

Example: The company may change rate of (a) dividend on preference shares or (b) convert cumulative preference shares into non-cumulative preference shares without changing the amount of share capital by passing the following journal entries:

- a. Debit (Old)% Cum. Pref. Share Capital Account
Credit (New)% Cum. Pref. Share Capital Account
- b. Debit ...% Cum. Pref. Share Capital Account
Credit ...% Non-cum. Pref. Share Capital Account

3. Reduction of Share Capital:

Section 66 of the Companies Act, 2013 lays down the procedure in respect of reduction of share capital. Subject to confirmation by the Tribunal on an application by the company, a company may, by a special resolution, reduce the share capital in the following manner-

(a) Extinguishing or reducing the liability of the shareholders in respect of unpaid amount on the shares held by them;

Here the shareholders are not called upon to pay the unpaid amount on shares held by them in future.

Example:

A company decides to reduce Rs. 10 per share, into Rs. 7.5 per share fully paid up, by cancelling the unpaid amount of Rs. 2.5 per share. The entry in this case would be

Share Capital (Partly Paid-Up) Account	Dr.	(Rs. 7.5 (Fv Rs.10) X No. of Shares)
To Share Capital (Fully Paid-up) Account		(Rs. 7.5 (Fv- Rs.7.5) X No. of Shares)

(b) Paying off any paid-up share capital which is in excess of its requirements:

When its not possible for the company to employ profitably its paid-up capital, then in such case it may decide to refund the excess capital to its shareholders.

Example:

A company having fully paid-up share of Rs. 10 each, decides to pay-off Rs. 2 per share to make it of Rs. 8 fully paid-up, entries in that case would be

- i. Share Capital Account (Rs. 10) Dr. (Rs. 10 X No. of Shares)
 To Share Capital Account (Rs. 8) (Rs. 8 X No. of Shares)
 To Sundry Shareholders Account (Rs. 2 X No. of Shares)
- ii. Sundry Shareholders Account Dr. (Rs. 2 X No. of Shares)
 To Bank Account (Rs. 2 X No. of Shares)

(c) Cancelling any paid-up share capital which is lost or is unrepresented by available assets:

i. Reduction in paid up value only-

Here the nominal value of the share remains the same and only the paid value is reduced.

Example: The shareholders may agree to reduce the paid capital of Rs. 100 per share to paid value of Rs. 10 per share. The sacrifice is Rs. 90 and the entry will be

- Share Capital Account Dr. (Rs. 90 X No. of Shares)
 To Capital Reduction Account (Rs. 90 X No. of Shares)

ii. Reduction in both nominal and paid-up values-

In this case, both the paid up capital and nominal value of the shares are reduced. Continuing the above example, the entry will be:

- Share Capital Account (Rs. 100 Share) Dr. (Rs. 100 X No. of Shares)
 To Share Capital (Rs. 10 Share) (Rs. 10 X No. of Shares)
 To Capital Reduction Account (Rs. 90 X No. of Shares)

Thus in such treatment we debit the original Share Capital Account so as to close it, credit new Share Capital Account with the amount treated as paid up; and credit Capital Reduction Account with the difference.

4. Compromise/Arrangements:

A scheme of compromise and arrangement is an agreement between a company and its members and outside liabilities when the company faces financial problems. Such an arrangement therefore also involves sacrifices by shareholders, or creditors or debenture holders or by all of them.

5. Surrender of Shares:

In this method, shares are divided into shares of smaller denominations and then the shareholders are made to surrender their shares to the company. These shares are then allotted to debenture holders and creditors so that their liabilities are reduced. The unutilized surrendered shares are then cancelled by transferring them to Reconstruction Account.

IMPORTANT POINTS:

1. Under the above-mentioned methods- the alteration of share capital and the varying of the shareholders rights do not involve opening the capital reduction/reconstruction account.
2. It is only under the reduction of share capital, unrepresented reserves, compromise/ arrangements with the outside liabilities and surrender of shares, there shall be capital reduction/reconstruction account used to which the unrepresented assets/liabilities will be transferred as per the arrangement.
3. An appreciation in the value of an asset or reduction in the amount of a liability should be debited to the account concerned and credited to Capital Reduction Account (or Reconstruction Account).
4. Eliminate debit balance of profit and loss account and all over-valuation of assets by crediting the accounts concerned and debiting the Capital Reduction (or Reconstruction) Account. For this purpose, any reserve appearing in the books of the company may be used. If any balance is left in the Capital Reduction (or Reconstruction) Account, it should be transferred to the Capital Reserve Account.
5. If there is any balance in the reconstruction account it is finally transferred to the Capital reserve under Reserves and Surplus. But if the amount for writing off the assets and accumulated losses is more than the reconstruction amount, then reserves will be adjusted against the same.
6. While preparing the balance sheet of a reconstructed company, the following points are to be kept in mind:
 - a. After the name of the company, the words “**and Reduced**” should be added only if the Court so orders.
 - b. In case of fixed assets, the amount written off under the scheme of reconstruction must be shown for five years.

PROBLEMS FOR DISCUSSION

PROBLEM 1:

On 31-12-20X1, B Ltd. had 20,000 Rs. 10 Equity Shares as authorised capital and the shares were all issued on which Rs. 8 was paid up. In June, 20X2 the company in general meeting decided to sub – divide each share into two shares of Rs. 5 with Rs. 4 paid up. In June, 20X3 the company in general meeting resolved to consolidate 20 shares of Rs. 5, Rs. 4 per share paid up into one share of Rs. 100 each, Rs. 80 paid up.

Pass entries and show how share capital will appear in notes to Balance Sheet as on 31-12-20X1, 31-12-20X2, 31-12-20X3. (SM)

PROBLEM 2:

C Ltd. had Rs. 5,00,000 authorised capital on 31-12-20X1 dividend into shares of Rs. 100 each out of which 4,000 shares were issued and fully paid up. In June 20X2 the company decided to convert the issued shares into stock. But in June, 20X3 the Company re – converted the stock into shares of Rs. 10 each, fully paid up.

Pass entries and show how share capital will appear in Notes to Balance Sheet as on 31-12-20X1, 31-12-20X2, 31-12-20X3. (SM)

PROBLEM 3:

The Balance Sheet of A & Co. Ltd. as on 31-12-20X1 is as follows:

Assets	Rs.	Rs.
Fixed Assets:		
Freehold property	4,25,000	
Plant	50,000	
Patent	37,500	
Goodwill	1,30,000	6,42,500
Traded Investments (at cost)		55,000
Current Assets:		
Trade receivables	4,85,000	

Inventory	4,25,000	9,10,000
Profit and Loss Account		5,35,000
Total		21,42,500
Liabilities		
Share Capital:		
4,000 6% Cumulative Preference Shares of Rs. 100 each	4,00,000	
75,000 Equity Shares of Rs. 10 each	7,50,000	11,50,000
6% Debentures (Secured on Freehold Property)	3,75,000	
Accrued Interest	22,500	3,97,500
Current Liabilities:		
Bank Overdraft	1,95,000	
Trade payables	3,00,000	
Directors' Loans	1,00,000	5,95,000
		21,42,500

The Court approved a Scheme of re-organisation to take effect on 1-1-20X2, whereby:

- i) The Preference shares to be written down to Rs. 75 each and Equity Shares to Rs. 2 each.
- ii) Of the Preference Share dividends which are in arrears for four years, three fourths to be waived and Equity Shares of Rs.2 each to be allotted for the remaining quarter.
- iii) Accrued interest on debentures to be paid in cash.
- iv) Debenture-holders agreed to take over freehold property, book value Rs.1,00,000 at a valuation of Rs.1,20,000 in part repayment of their holdings and to provide additional cash of Rs. 1,30,000 secured by a floating charge on company's assets at an interest rate of 8% p.a.
- v) Patents and Goodwill to be written off.
- vi) Inventory to be written off by Rs. 65,000.
- vii) Amount of Rs. 68,500 to be provided for bad debts.
- viii) Remaining freehold property to be re-valued at Rs. 3,87,500
- ix) Trade Investments be sold for Rs. 1,40,000.
- x) Directors to accept settlement of their loans as to 90% thereof by allotment of equity shares of Rs. 2 each and as to 5% in cash, and balance 5% being waived.

- xi) There were capital commitments totalling Rs. 2,50,000. These contracts are to be cancelled on payment of 5% of the contract price as a penalty.
- xii) Ignore taxation and cost of the scheme.

You are requested to show Journal entries reflecting the above transactions (including cash transactions) and prepare the Balance Sheet of the company after completion of the Scheme. **(SM)**

PROBLEM 4:

Given below is the summarized balance sheet of Rebuilt Ltd. as on 31.3.20X1:

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
Authorised and issued capital: 12,000, 7% Preference shares of Rs.50 each (Note: Preference dividend is in arrear for five years)	6,00,000	Building at cost less depreciation	4,00,000
15,000 Equity shares of Rs. 50 each	7,50,000	Plant at cost less depreciation	2,68,000
	13,50,000	Trademarks and goodwill at cost	3,18,000
Loan	5,73,000	Inventory	4,00,000
Trade payables	2,07,000	Trade receivables	3,28,000
Other liabilities	35,000	Profit and loss A/c	4,51,000
	21,65,000		21,65,000

The Company is now earning profits short of working capital and a scheme of reconstruction has been approved by both the classes of shareholders. A summary of the scheme is as follows:

- The equity shareholders have agreed that their Rs.50 shares should be reduced to Rs. 2.50 by cancellation of Rs. 47.50 per share. They have also agreed to subscribe for three new equity shares of Rs. 2.50 each for each equity share held.
- The preference shareholders have agreed to cancel the arrears of dividends and to accept for each Rs. 50 share, 4 new 5% preference shares of Rs. 10 each, plus 6 new equity shares of Rs. 2.50 each, all credited as fully paid.
- Lenders to the company for Rs.1,50,000 have agreed to convert their loan into share and for this purpose they will be allotted 12,000 new preference shares of Rs. 10 each and 12,000 new equity shares of Rs. 2.50 each.

- d) The directors have agreed to subscribe in cash for 40,000, new equity shares of Rs. 2.50 each in addition to any shares to be subscribed by them under (a) above.
- e) Of the cash received by the issue of new shares, Rs. 2,00,000 is to be used to reduce the loan due by the company.
- f) The equity share capital cancelled is to be applied:
- To write off the debit balance in the profit and loss A/c; and
 - To write off Rs. 35,000 from the value of plant.

Any balance remaining is to be used to write down the value of trademarks and goodwill.

Show by journal entries how the financial books are affected by the scheme and prepare the balance sheet of the company after reconstruction. The nominal capital as reduced is to be increased to Rs.6,50,000 for preference share capital and Rs.7,50,000 for equity share capital. (SM)

PROBLEM 5:

Repair Ltd. is in the hands of a receiver for debenture holders who holds a charge on all assets except uncalled capital. The following statement shows the position as regards creditors as on 30th June, 2015:

Liabilities	Amount	Assets	Amount
6,000 shares of Rs.60 each, Rs.30 paid up		Property, machinery and plant etc. (Cost Rs. 3,90,000) Estimated at	1,50,000
First debentures	3,00,000	Cash in hand of the receiver	<u>2,70,000</u>
Second debentures	6,00,000	Charged under debentures	4,20,000
Unsecured trade payables	4,50,000	Uncalled capital	<u>1,80,000</u>
			6,00,000
		Deficiency	7,50,000
	13,50,000		13,50,000

A holds the first debentures for Rs.3,00,000 and second debentures for Rs. 3,00,000. He is also an unsecured creditor for Rs.90,000. B holds second debentures for Rs. 3,00,000 and is an unsecured trade payables for Rs. 60,000.

The following scheme of reconstruction is proposed:

1. A is to cancel Rs.2,10,000 of the total debt owing to him, to bring Rs. 30,000 in cash and to take first debentures (in cancellation of those already issued to him) for Rs.5,10,000 in satisfaction of all his claims.
2. B is to accept Rs.90,000 in cash in satisfaction of all claims by him.
3. In full settlement of 75% of the claim, unsecured creditors (other than A and B) agreed to accept four shares of Rs.7.50 each, fully paid against their claim for each share of Rs.60. The balance of 25% is to be postponed and to be payable at the end of three years from the date of Court's approval of the scheme. The nominal share capital is to be increased accordingly.
4. Uncalled capital is to be called up in full and Rs.52.50 per share cancelled, thus making the shares of Rs. 7.50 each.

Assuming that the scheme is duly approved by all parties interested and by the Court, give necessary journal entries.

SM

PROBLEM 6:

The Balance Sheet of Vaibhav Ltd. as on 31st March 2014 is as follows:

Liabilities	Rs.	Assets	Rs.
Equity Shares of Rs. 100 each	2,00,00,000	PPE	2,50,00,000
6%, Cumulative Preference Shares of Rs. 100 each	1,00,00,000	Investments (Market Value Rs. 19,00,000)	20,00,000
5% Debentures of Rs. 100 each	80,00,000	Current Assets	2,00,00,000
Sundry Creditors	1,00,00,000	P & L A/c	12,00,000
Provision for taxation	2,00,000		
	4,82,00,000		4,82,00,000

The following scheme of Internal Reconstruction is sanctioned:

1. All the existing equity shares are reduced to Rs. 40 each.
2. All preference shares are reduced to Rs. 60 each.
3. The rate of Interest on Debentures increased to 6%. The Debenture holders surrender their existing debentures of Rs. 100 each and exchange the same for fresh debentures of Rs. 70 each for every debenture held by them.
4. PPE are to be written down by 20%.
5. Current assets are to be revalued at Rs. 90,00,000.

6. Investments are to be brought to their market value.
7. One of the creditors of the company to whom the company owes Rs. 40,00,000 decides to forgo 40% of his claim. The creditor is allotted with 60000 equity shares of Rs. 40 each in full and final settlement of his claim.
8. The taxation liability is to be settled at Rs. 3,00,000.
9. It is decided to write off the debit balance of Profit & Loss A/c.

Pass journal entries and show the Balance Sheet of the company after giving effect to the above. **SM**

PROBLEM 7:

Following is the Draft Balance Sheet of ABC Ltd. Co.as at 31st March, 2015:

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
Share capital:		Plant and Machinery	9,00,000
2,00,000 Equity shares of Rs.10 each fully paid up	20,00,000	Furniture and fixtures	2,50,000
6,000 8% Preference Shares of Rs.100 each	6,00,000	Patents and copy rights	70,000
9 % Debentures	12,00,000	Investments (at cost) (Market value Rs. 55,000)	68,000
Bank overdraft	1,50,000	Inventory	14,00,000
Trade Payable	5,92,000	Trade receivables	14,39,000
		Cash and bank balance	10,000
		Profit & Loss A/c	4,05,000
	45,42,000		45,42,000

The following scheme of reconstruction was finalized:

1. Preference shareholders would give up 30% of their capital in exchange for allotment of 11% Debentures to them.
2. Debenture holders having charge on plant and machinery would accept plant and machinery in full settlement of their dues.

3. Inventory equal to Rs. 5,00,000 in book value will be taken over by trade payables in full settlement of their dues.
4. Investment value to be reduced to market price.
5. The company would issue 11% Debentures for Rs.3,00,000 to augment its working capital requirement after settlement of bank overdraft.

Give necessary journal entries reflecting the above scheme of reconstruction in the books of the ABC Ltd. Co. Prepare capital reduction account and balance sheet of the company after internal reconstruction

SM

PROBLEM 8:

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

Liabilities	Rs.	Assets	Rs.
Authorised and subscribed capital:		Fixed Assets :	
10,000 Equity shares of Rs.100 each fully paid	10,00,000	Machineries	1,00,000
		Current assets :	
Unsecured Loans :		Inventory	3,20,000
12% Debentures	2,00,000	Trade receivables	2,70,000
Accrued interest	24,000	Bank	30,000
Current liabilities		Profit and loss account	6,00,000
Trade payables -	72,000		
Provision for income tax	24,000		
	13,20,000		13,20,000

It was decided to reconstruct the company for which necessary resolution was passed and sanctions were obtained from appropriate authorities. Accordingly, it was decided that:

1. Each share is sub-divided into ten fully paid up equity shares of Rs 10 each.
2. After sub-division, each shareholder shall surrender to the company 50% of his holding, for the purpose of re-issue to debenture holders and trade payables as necessary.
3. Out of shares surrendered, 10,000 shares of Rs 10 each shall be converted into 12% preference shares of Rs 10 each, fully paid up.

4. The claims of the debenture-holders shall be reduced by 75 per cent. In consideration of the reduction, the debenture holders shall receive preference shares of Rs 1,00,000 which are converted out of shares surrendered.
5. Trade payables claim shall be reduced to 50 per cent, it is to be settled by the issue of equity shares of Rs 10 each out of shares surrendered.
6. Balance of profit and loss account to be written off.
7. The shares surrendered and not re-issued shall be cancelled.

You are required to show the journal entries giving effect to the above and the resultant Balance Sheet.

SM

PROBLEM 9:

Parth Ltd, had laid down the following terms upon the sanction of the reconstruction plan by the court

1. Furniture and Fixtures which stood at the books at Rs. 1,50,000 to be written down to Rs. 95,000. The freehold premises which was valued at Rs. 7,00,000 showed an appreciation of Rs. 55,000.
2. Plant and machinery showed fall in value of Rs. 89,000, to be recorded in the books. Investment at Rs. 2,00,000 was brought down to the existing market value at Rs. 1,05,000.
3. Debenture holders accepted to receive the following in lieu of their present 9% debentures of Rs. 2,50,000
 - i. 1/5th of the total to be paid in cash to them.
 - ii. To take over the land and buildings of value Rs. 72,000.
 - iii. To forgo the remaining unpaid portion as a policy of reconstruction.

Write off the profit and loss A/c debit balance at Rs. 70,000 which had been accumulated over the years. In case of any shortfall, the balance of the General reserve of Rs. 1,50,000 can be utilized to write off the losses under reconstruction scheme.

Show the necessary journal entries as part of the reconstruction process considering that balance in general reserve utilized to write off the losses as per reconstruction scheme.

(PRACTICAL QUESTION-1- SM)

PROBLEM 10

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

		Rs.
A.	Equity & Liabilities	
1.	Shareholders' Fund:	

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

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

1. Paid up value of 7% Preference Share to be reduced to Rs. 80, but the rate of dividend being raised to 9%.
2. Paid up value of Equity Shares to be reduced to Rs. 10.

3. The directors to refund Rs. 50,000 of the fees previously received by them.
4. Debenture holders forego their interest of Rs. 26,000 which is included among the trade payables.
5. The preference shareholders agreed to waive their claims for preference share dividend, which is in arrears for the last three years.
6. "B" 6% Debenture holders agreed to take over the Chennai Works at Rs. 4,25,000 and to accept an allotment of 1,500 equity shares of Rs. 10 each at par, and upon their forming a company called Zia Ltd. (to take over the Chennai Works) they allotted 9,000 equity shares of Rs. 10 each fully paid at par to Star Ltd.
7. The Chennai Workmen's compensation fund disclosed that there were actual liabilities of Rs. 1,000 only. As a consequence, the investments of the fund were realized to the extent of the balance. Entire investments were sold at a profit of 10% on book value and the proceeds were utilized for part payment of the creditors.
8. Inventory was to be written off by Rs. 1,90,000 and a provision for doubtful debts is to be made to the extent of Rs. 20,000.
9. Chennai works completely written off.
10. Any balance of the Capital Reduction Account is to be applied as two-third to write off the value of Bombay Works and one-third to Capital Reserve.

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

(MAY 2020-RTP- PROBLEM NO.9)

5.ACCOUNTING FOR LIQUIDATION OF COMPANIES

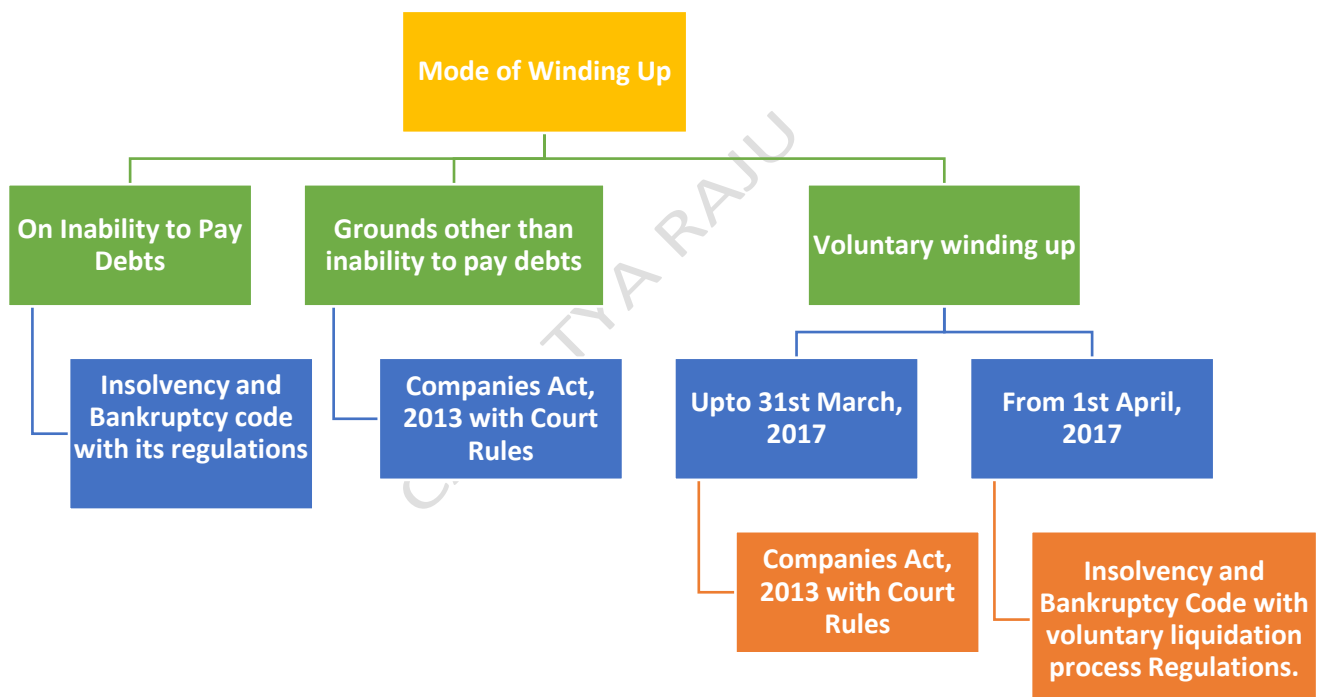
MEANING OF LIQUIDATION:

Liquidation is the legal procedure by which the company comes to an end.

DEFINITION OF WINDING UP:

As per Section 2 (94A) of the Companies Act, 2013, winding up means winding up under this Act or liquidation under the Insolvency and Bankruptcy Code, 2016, as applicable.

MODE OF WINDING UP:

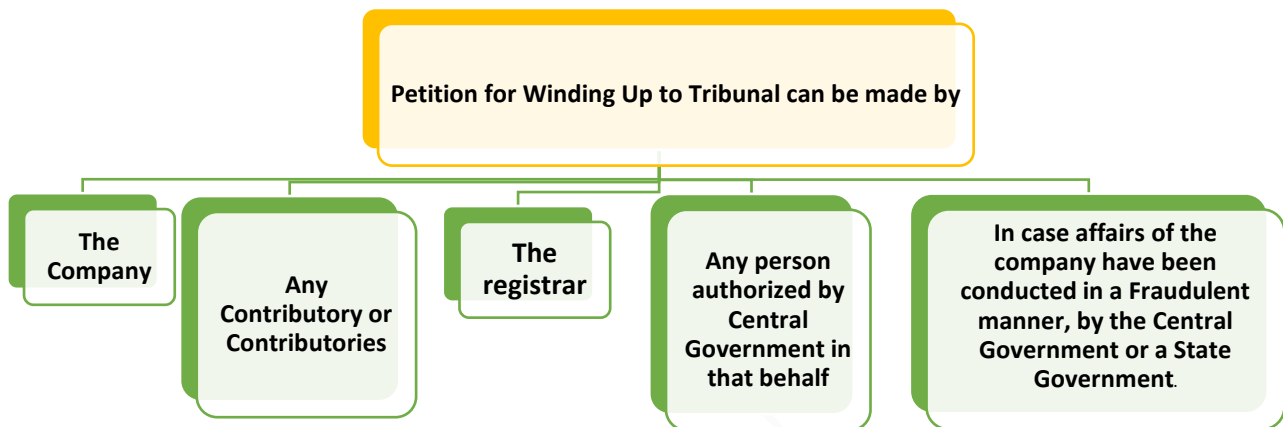


Circumstances in Which Company May be Wound Up by Tribunal:

1. The company has resolved that the company be wound up by the Tribunal. The company has require to pass special resolution.
2. The company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality
3. The Registrar or any other person authorised by the Central Government by notification under this Act can make an application to tribunal. The Tribunal is of the opinion that the affairs of the company have been conducted in a fraudulent manner or the company was formed for fraudulent and unlawful purpose or the persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith and that it is proper that the company be wound up.

4. The company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding 5 consecutive financial years.
5. The Tribunal is of the opinion that it is just and equitable that the company should be wound up.

PETITION FOR WINDING UP:



VOLUNTARY WINDING UP:

Provisions under Companies Act, 2013 relating to voluntary winding up stand omitted due to section 255 of Insolvency & Bankruptcy Code, 2016

Provisions of the Insolvency and Bankruptcy Code, 2016:

1. A corporate person who intends to liquidate itself voluntarily and has not committed any default may initiate voluntary liquidation proceedings under the provisions of the Chapter V- Voluntary liquidation of corporate persons of the Insolvency and Bankruptcy Code, 2016.
2. The voluntary liquidation of a corporate person shall meet such conditions and procedural requirements as may be specified by the Board.
3. Voluntary liquidation proceedings of a corporate person registered as a company shall meet the following conditions, namely:
 - a. A declaration from majority of the directors of the company verified by an affidavit stating that—
 - i. They have made a full inquiry into the affairs of the company and they have formed an opinion that either the company has no debt or that it will be able to pay its debts in full from the proceeds of assets to be sold in the voluntary liquidation; and
 - ii. The company is not being liquidated to defraud any person;
 - b. The declaration under sub-clause (a) shall be accompanied with the following documents, namely:

- i. Audited financial statements and record of business operations of the company for the previous two years or for the period since its incorporation, whichever is later;
 - ii. A report of the valuation of the assets of the company, if any prepared by a registered valuer;
- c. Within four weeks of a declaration under sub-clause (a), there shall be—
 - i. A special resolution of the members of the company in a general meeting requiring the company to be liquidated voluntarily and appointing an insolvency professional to act as the liquidator; or
 - ii. A resolution of the members of the company in a general meeting requiring the company to be liquidated voluntarily as a result of expiry of the period of its duration, if any, fixed by its articles or on the occurrence of any event in respect of which the articles provide that the company shall be dissolved, as the case may be and appointing an insolvency professional to act as the liquidator: Provided that the company owes any debt to any person, creditors representing two-thirds in value of the debt of the company shall approve the resolution passed under sub-clause (c) within seven days of such resolution.
- 4. The company shall notify the Registrar of Companies and the Board about the resolution under sub-section (3) to liquidate the company within seven days of such resolution or the subsequent approval by the creditors, as the case may be.
- 5. Subject to approval of the creditors under sub-section (3), the voluntary liquidation proceedings in respect of a company shall be deemed to have commenced from the date of passing of the resolution under sub-clause (c) of sub-section (3).
- 6. The provisions of sections 35 to 53 of Chapter III (Liquidation process) and Chapter VII (Offences and penalties) shall apply to voluntary liquidation proceedings for corporate persons with such modifications as may be necessary.
- 7. Where the affairs of the corporate person have been completely wound up, and its assets completely liquidated, the liquidator shall make an application to the Adjudicating Authority for the dissolution of such corporate person.
- 8. The Adjudicating Authority shall on an application filed by the liquidator under sub-section (7), pass an order that the corporate debtor shall be dissolved from the date of that order and the corporate debtor shall be dissolved accordingly.

9. A copy of an order under sub-section (8) shall within fourteen days from the date of such order, be forwarded to the authority with which the corporate person is registered.

STATEMENT OF AFFAIRS:

In case of winding up by Tribunal, Section 272(5) of the Companies Act, 2013 provides that a petition presented by the company for winding up before the Tribunal shall be admitted only if accompanied by a statement of affairs in such form and in such manner as may be prescribed.

The broad lines on which the Statement of Affairs is prepared are the following

1. Include assets on which there is no fixed charge at the value they are expected to realise. Students should note to include calls in arrear but not uncalled capital.
2. Include assets on which there is a fixed charge. The amount expected to be realised would be compared with the amount due to the creditor concerned. Any surplus is to be extended to the other column. A deficit (the amount owed to the creditor exceeding the amount realisable from the asset) is to be added to unsecured creditors.
3. The total of assets in point (1) and any surplus from assets mentioned in point (2) is available for all the creditors (except secured creditors already covered by specifically mortgaged assets).
4. From the total assets available, the following should be deducted one by one:- (i) Preferential creditors, (ii) Debentures having a floating charge, and (iii) Unsecured creditors. If a minus balance emerges, there would be deficiency as regards creditors, otherwise there would be a surplus.
5. The amount of total paid-up capital (giving details of each class of shares) should be added and the figure emerging will be deficiency (or surplus) as regards members.

Statement of affairs should accompany eight lists:

List A Full particulars of every description of property not specifically pledged and included in any other list are to be set forth in this list.

List B Assets specifically pledged and creditors fully or partly secured.

List C Preferential creditors for rates, taxes, salaries, wages and otherwise.

List D List of debenture holders secured by a floating charge.

List E Unsecured creditors.

List F List of preference shareholders.

List G List of equity shareholders.

List H Deficiency or surplus account.

DEFICIENCY ACCOUNT:

1. The official liquidator will specify a date for period (minimum three years) beginning with the date on which information is supplied for preparation of an account to explain the deficiency or surplus. On that date, either assets would exceed capital plus liabilities, that is, there would be a reserve or there would be a deficit or debit balance in the Profit and Loss Account.
2. The Deficiency account is divided into two parts:
 - a. The first part starts with the deficit (on the given date) and contains every item that increases deficiency or reduces surplus such as losses, dividends etc.
 - b. The second part starts with the surplus on the given date and includes all profits. If the total of the first exceeds that of the second, there would be a deficiency to the extent of the difference, and if the total of the second part exceeds that of the first, there would be a surplus.

<u>PARTICULARS</u>	<u>AMOUNT(RS)</u>
Opening Debit balance in P &I	XXXX
<u>ITEMS CONTRIBUTING TO DEFICIT OR REDUCES SURPLUS</u>	
a) Operating Losses	XXXX
b) Abnormal and any other losses	XXXX
c) Dividend and Bonus shares declared during the period	XXXX
d) Realization loss due to Assets & Liabilities realized as form part of Liquidation	XXXX
Opening Reserve	XXXX
<u>ITEMS CONTRIBUTING TO DEFICIT OR REDUCES SURPLUS</u>	
a) Operating Profits	XXXX
b) Abnormal and any other profits	XXXX
c) Realization profits due to Assets & Liabilities realized as form part of Liquidation	XXXX
NET SURPLUS/DEFISIT AS PER LIST H	XXXX

LIQUIDATOR'S FINAL STATEMENT OF ACCOUNT:

In case of voluntary winding up, the statement prepared by the Liquidator showing receipts and payment of cash is called "Liquidator's Statement of Account". In case of compulsory winding up, the statement is known as "Official Liquidator's Final Account".

While Preparing the Statement of Account, the following points should be noted:

1. Assets are included in the prescribed order of liquidity.
2. In case of assets specifically charged in favour of creditors, only the surplus from it, if any, is recognised as "Surplus from Securities".
3. Net result of trading entered on the receipts side, profits being added and losses being deducted.
4. Payments made to redeem securities and cost of execution, i.e. cost of collecting debts, are deducted from the total receipts.
5. Payments are made as shown in the following order:
 - a. Legal Charges;
 - b. Liquidator's Remuneration;
 - c. Liquidation Expenses;
 - d. Debenture holders (including interest up to the date of winding up if the company is insolvent and to the date of payment if it is solvent);
 - e. Preferential creditors (in actual practice, preferential creditors are paid before debenture holders having a floating charge).
 - f. Unsecured creditors, shareholders for dividends declared but not yet paid;
 - g. Preference shareholders; and
 - h. Equity shareholders.
6. Arrears of dividends on cumulative preference shares should be paid up to the date of winding up.
7. In case of partly paid shares, it should be seen whether any amount is to be called up on such shares.
 Firstly, the equity shareholders should be called up to pay the necessary amount (not exceeding the amount of uncalled capital). If creditors' claims cannot be satisfied with that amount, Preference shareholders would be called upon to contribute (not exceeding the amount as yet uncalled on the shares) for paying off creditors.
8. The loss suffered by each class of shareholders, i.e. the amount that cannot be repaid, should be proportionate to the nominal value of the share. The loss per shares have nominal value of Rs. 100, and one set of shareholders has paid Rs. 80 per share and other set has paid Rs. 60 per share. Suitable adjustment will have to be made in cash in such a case; the latter set must contribute Rs. 20 first or the first set must be paid Rs. 20 first.

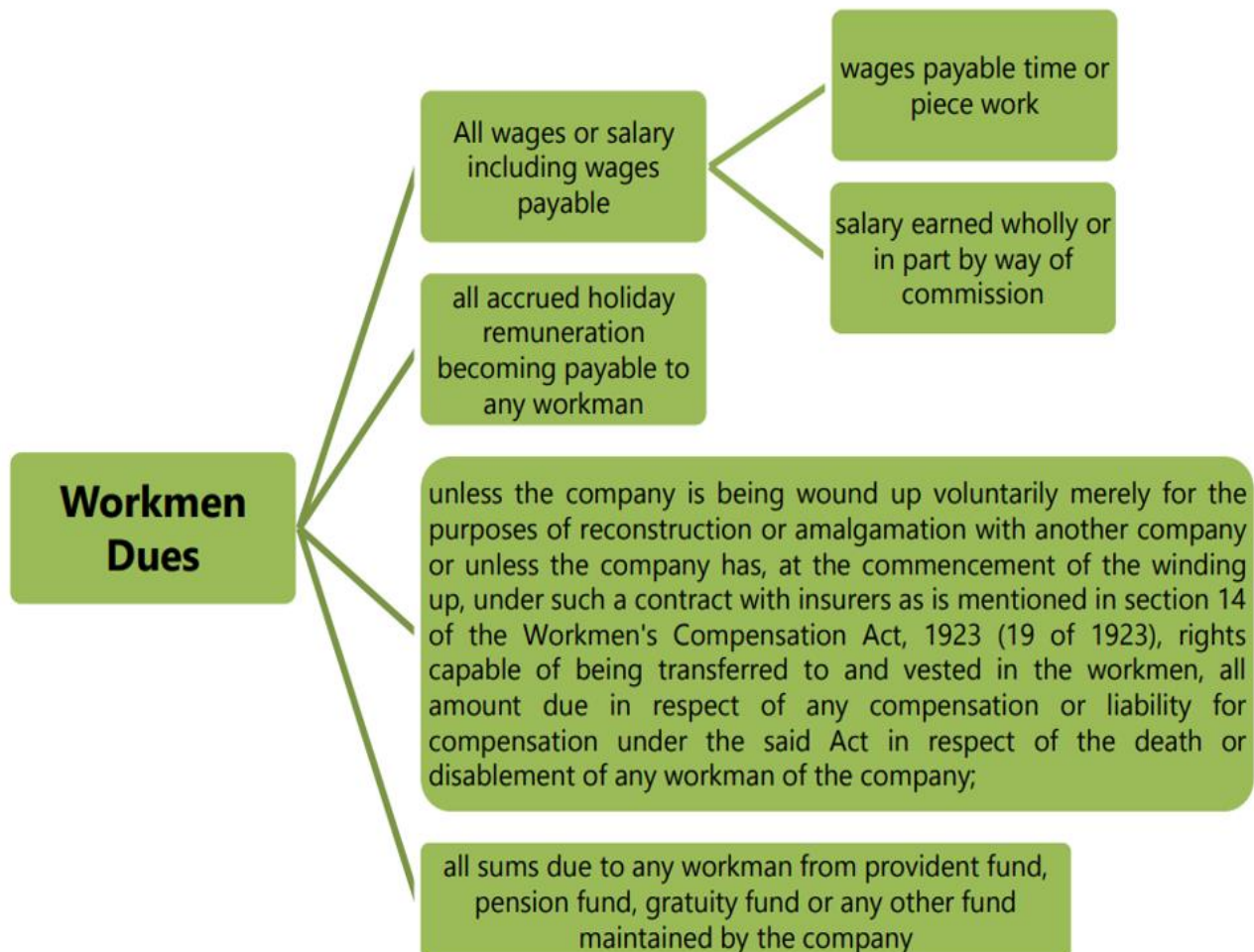
OVERRIDING PREFERENTIAL PAYMENTS (SECTION 326):

In the winding up of a company, the following debts should be paid in priority to all other debts, as per section 326:

1. Workmen's dues; and
2. Where a secured creditor has realized a secured asset, so much of the debts due to such secured creditor as could not be realized by him or the amount of the workmen's portion in his security (if payable under the law), whichever is less, pari-passu with the workmen's dues.

Explanation: For the purposes of this section

1. Workmen, in relation to a company, means the employees of the company, being workmen within the meaning of Section 2 (s) of the Industrial Disputes Act, 1947;
2. Workmen dues, in relation to a company, means the aggregate of the following sums due from the company to its workmen, namely:



(c) The following payment should be made in priority to secured creditors.

All wages or salary including wages payable

all accrued holiday remuneration becoming payable to any workman

If the above payments are payable for a period of 2 years preceding the winding up order then the same shall be paid in priority to all other debts (including debts due to secured creditors), within a period of 30 days of sale of assets and shall be subject to such charge over the security of secured creditors.

PREFERENTIAL CREDITORS (SECTION 327):

In a winding up there should be paid in priority to all other debts subject to the provisions of section 326.



1. **Government Taxes**: All revenues, taxes, cess and rates due from the company to the Central Government or a State Government or to a local authority at the relevant date, and having become due and payable within the twelve months immediately before that date.
2. **Salary and Wages**: All wages or salary including wages payable for time or piece work and salary earned wholly or in part by way of commission of any employee in respect of services rendered to the company and due for a period not exceeding four months within the 12 months immediately before the relevant date.
3. The debts enumerated in this section should rank equally among themselves and be paid in full, unless the assets are insufficient to meet them, in which case they should abate in equal proportions.
4. Employee does not include a workman.

LIST B CONTRIBUTORIES:

1. **Persons**: Shareholders who had transferred Partly Paid Shares (otherwise than by operation of law or by death) within one year, prior to the date of winding up may be called upon to pay an amount to pay off such Creditors as existed on the date of transfer of shares. These Transferors are called as B List Contributories.
2. **Liability**: Their liability is restricted to the amount not called up when the shares were transferred. They cannot be called upon to pay more than the entire face value of the share. For example, if Shares having Face Value Rs. 100 were paid up Rs. 60, the B List Contributory can be called up to pay a maximum of Rs. 40 only.
3. **Conditions**: Liability of B List Contributories will crystallize only
 - a. When the existing assets available with the liquidator are not sufficient to cover the liabilities;
 - b. When the existing shareholders fail to pay the amount due on the shares to the Liquidator.

PROBLEMS FOR DISCUSSION

PROBLEM 1:

In Which sequence the following payments will be made while preparing the liquidator's statement of account?

1. Debenture holders
2. Unsecured creditors
3. Legal charges
4. Equity shareholders.
5. Preference shareholders.

(SM)

PROBLEM 2:

Amounts payable in winding-up of a company are as follows:

- Secured Creditors Rs. 1,25,000
- Workmen's Due Rs. 2,50,000

Show the payments made and treatment of balance in the following two instances:

(i) If the security realized is RS.2,00,000

(ii) If the security realized is RS.1,00,000

(SM)

PROBLEM 3:

A company went into liquidation whose creditors are Rs. 36,000. This amount of Rs. 36,000 includes Rs. 6,000 on account of wages of 15 men at Rs. 100 per month for 4 months, immediately before the date of winding up, Rs. 9,000 being the salaries of 5 employees at Rs. 300 per month for the previous 6 months, Rent for godown for the last six months amounting to Rs. 3,000; Income-tax deducted out of salaries of employees Rs.1,000. In addition it is estimated that the company would have to pay Rs. 3,000 as compensation to an employees for injuries suffered by him, which was contingent liability not accepted by the company and not included in above said creditors figure. Find the amount of Preferential Creditors.

(SM)

PROBLEM 4:

In a liquidation which commenced on April 2, 2011 certain creditors could not receive payments out of the realisation of assets and out of the contributions from "A" list contributories. The following are the details of certain transfers, which took place in 2010 and 2011.

Shareholders	Number of shares transferred at the date of ceasing to be member	Date of ceasing to be member	Creditors remaining unpaid and outstanding
X	1,500	1st March 2010	4,000
A	1,000	1st May 2010	6,000
B	1,500	1st July 2010	7,500
C	300	1st Nov. 2010	8,000
D	200	1st Feb. 2011	9,500

All the shares were Rs. 10 each, Rs. 6 paid up ignoring expenses of and remuneration to liquidators, etc., show the amount to be realised from the various persons listed above. (SM)

PROBLEM 5:

A liquidator is entitled to receive remuneration at 2% on the assets realized, 3% on the amount distributed to Preferential creditors and 3% on the payment made to unsecured creditors. The assets were realized for Rs. 50,00,000 against which payment was made as follows: Liquidation expenses Rs. 50,000 Secured Creditors Rs. 20,00,000 Preferential Creditors Rs. 1,50,000 The amount due to Unsecured creditors was Rs. 30,00,000 You are asked to calculate the total Remuneration payable to Liquidator. Calculation shall be made to the nearest multiple of a rupee. (SM)

PROBLEM 6:

Sky Ltd. went into liquidation on 1st April, 20X1. Following are the details regarding share capital of the company.

- I. 20,000 Equity shares of Rs. 100 each, Rs. 75 paid up.
- II. 30,000 Equity shares of Rs. 100 each, Rs. 40 paid up.
- III. 80,000 Equity shares of Rs. 100 each, Rs. 65 paid up.

Surplus available with the Liquidator, after discharging all the liabilities is Rs. 20,00,000. Distribute this surplus money among different categories of shareholders. (SM)

PROBLEM 7:

Wind Ltd. went into liquidation on 31st March, 20X1. Following are the details regarding share capital of the company.

1. 15,000 Equity shares of Rs. 100 each, Rs. 90 paid up.
2. 40,000 Equity shares of Rs. 50 each, Rs. 25 paid up.
3. 2,00,000 Equity shares of Rs. 10 each, Rs. fully paid up.

Surplus available with the Liquidator, after payment of all the liabilities is Rs. 12,00,000. Distribute this surplus money among different categories of shareholders.

SM**PROBLEM 8:**

Omega Ltd. resolved on 31st March, 20X1 that the company be wound up voluntarily. The following was the trail balance extracted from its books as on the date:

PARTICULARS	Rs.	Rs.
Property, Plant and equipment	2,00,000	
Inventory	1,20,000	
Book debts	2,40,000	
Cash in Hand	40,000	
Profit and loss A/c (Dr. balance)	3,00,000	
1,000, 6% Preference shares of Rs. 100 each, fully paid		1,00,000
2,000 Equity shares of Rs. 100 each, fully paid		2,00,000
2,000 Equity shares of Rs. 100 each Rs. 75 paid up		1,50,000
Loan from bank (on security of stock)		1,00,000
Trade Payables		3,50,000
	9,00,000	9,00,000

The assets realized the following amounts (after all costs of realization and liquidator's commission amounting to Rs. 5,000 paid out of cash in hand).

PARTICULARS	Rs.
Property, Plant and equipment	1,68,000
Inventory	1,10,000
Trade receivables	2,30,000

Calls on partly paid shares were made but the amounts due on 200 shares were found to be irrecoverable.

You are required to prepare Liquidator's Final statement of account.

SM

PROBLEM 9:

M. Ltd. resolved on 31st December, 20X0 that the company be wound up voluntarily.

The following were the ledger balances extracted from its books as on that date:

	Rs.
Equity shares of Rs. 10 each	2,00,000
9% Preference shares of Rs. 10 each	1,00,000
Plant (less depreciation w/o Rs. 85,000)	2,15,000
Stock in trade	2,50,000
Trade receivables	55,000
Trade payables	75,000
Bank balance	74,000
Preliminary Expenses	6,000
Profit & Loss A/c (Dr. balance on 1st January, 20X0)	30,000
Outstanding Expenses (including mortgage interest)	25,000
4% Mortgage loan (secured by floating charge)	2,00,000

On 1st January, 20X1 the liquidator sold M. Ltd.'s Plant for Rs. 2,05,000 and stock intrade for Rs. 2,00,000. The sale was completed in January, 20X1 and the consideration satisfied as to Rs. 2,62,200 in cash and as to the balance in 6% Debentures of the purchasing company issued to the liquidator at a premium of 2%.

The remaining steps in the liquidation were as follows:

- (1) The liquidator realized Rs. 52,000 out of the book debts and the cost of collection amounted to Rs. 2,000.
- (2) The loan mortgage was discharged on 31st January, 20X1 along with interest from 31st July, 20X0. Trade payables were discharged subject to 2% and outstanding expenses excluding mortgage interest were settled for Rs. 2,000;
- (3) On 30th June 20X1 six month's interest on debentures was received from M. Ltd.
- (4) Liquidation expenses amounting to Rs. 3,000 and liquidator's remuneration of 3% on disbursements to members were paid on 30th June, 20X1 when:
 - (a) The preference shareholders were paid out in cash; and
 - (b) The debentures on M. Ltd. and the balance of cash were distributed rateably among the equity shareholders.

Prepare the Liquidator's Statement of Account showing the distribution.

(ILLUSTRATION-9 SM)

PROBLEM 10:

Confidence builders Ltd. gives the following ledger balances as on 30th September, 20X3:

	Rs.
Land and Building	1,20,000
Sundry current assets	3,95,000
Profit and loss account (Dr. balance)	38,500
Debenture issue expenses not written off	2,000
<u>Share Capital</u>	
Issued: 11% Preference shares of Rs. 10 each	1,00,000
10,000 equity shares of Rs. 10 each fully paid up	1,00,000
5,000 equity shares of Rs. 10 each, Rs. 7.50 per share paid up	37,500
13% Debentures	1,50,000
Mortgage Loan	80,000
Bank Overdraft	30,000
Creditors for trade	32,000
Income tax arrears: (assessment concluded in July 20X3)	
Assessment year 20X1-20X2	21,000
Assessment year 20X2-20X3	5,000

Mortgage loan was secured against land and buildings. Debentures were secured by a floating charge on all the other assets. The company was unable to meet the payments and therefore the debenture holders appointed a receiver for the debenture holders, he brought the land and buildings to auction and realized Rs. 1,50,000. He also took charge of sundry assets of value of Rs. 2,40,000 and realized Rs. 2,00,000. The bank overdraft was secured by a personal guarantee of two of the directors of the company and on the bank raising demand, the directors paid off the due from their personal resources. Costs incurred by the receiver were Rs. 2,000 and by the liquidator Rs. 2,800. The Receiver was not entitled to any remuneration but the liquidator was to receive 3% fee on the value of assets realized by him. Preference shareholders had not been paid dividend for the period after 30th September 20X1 and interest for the last half year was due to the debenture holders. Rest of the assets were realized at Rs. 1,00,000.

Prepare the accounts to be submitted by the Receiver and Liquidator.

SM

PROBLEM 11:

X Ltd. was ordered to be wound up on 31st March, 20X2 on which date the following balances were extracted from its books:

	Rs.
Goodwill	1,00,000
Building	3,50,000
Plant	5,50,000
Fixtures	23,000
Stock	38,000
Debtors	25,000
Cash	500
Profit and loss account (Dr. balance)	1,38,500
Share Capital: 10,000 Equity Shares of Rs. 100 each	10,00,000
5% Debentures (Secured by Floating charge on all assets)	1,60,000
Interest payable on these debentures	4,000
Bank overdraft (secured by hypothecation of stock)	25,000
Creditors	36,000

The amounts estimated to be realized are: Goodwill Rs. 1,000; Building Rs. 3,00,000; Plant Rs. 5,25,000; Fixtures Rs. 10,000; Stock Rs. 31,000; Debtors Rs. 20,000.

Creditors included Rs. 6,000 on account of wages of 15 men at Rs. 100 per month for 4 months immediately before the date of winding up ; Rs. 9,000 being the salaries of 5 employees at Rs. 300 per month for the previous 6 months; Rent for godown for the last six months amounting to Rs. 3,000; Income-tax deducted out of salaries of employees Rs. 1,000 and Directors Fees Rs. 500.

Three years ago, the debit balance in the Profit and Loss Account was Rs. 77,925 and since that date the accounts of the company have shown the following figures:

	Year	Year	Year
	31-3-20X0	31-3-20X1	31-3-20X2
	Rs.	Rs.	Rs.
Gross Profit	65,000	45,000	40,000
Wages and Salaries	40,500	36,000	34,400
Electricity and Water Tax	5,750	6,380	5,260
Debentures interest	8,000	8,000	8,000
Bad Debts	8,540	7,600	6,700
Depreciation	6,700		
Directors' Fees	1,000	1,000	1,000
Miscellaneous Expenses	10,500	7,265	7,980
Total	80,990	66,245	63,340

In addition it is estimated that the company would have to pay Rs. 5,000 as compensation to an employee for injuries suffered by him which was contingent liability not accepted by the company.

Prepare the Statement of Affairs and the Deficiency account.

(ILLUSTRATION 14 –SM)

TEST YOUR KNOWLEDGE

Theoretical Questions

1. Explain Overriding preferential payments as per Companies Act, 2013.
2. Explain B List Contributories and the liability of contributories included in the list.
3. Write the LISTS which should accompany the Statement of Affairs, in case of a winding up by Court.

MCQs

1. Liability of B List Contributories will crystallize only When
 - (a) Existing assets available with the liquidator are not sufficient to cover the liabilities.
 - (b) Existing shareholders fail to pay the amount due on the shares to the Liquidator.
 - (c) both (a) and (b).

2. If Shares having Face Value Rs. 100 were paid up Rs. 70, the B List Contributory can be called up to pay
- (a) Maximum of Rs. 30 only.
 - (b) Maximum of Rs. 70 only.
 - (c) Maximum of 100 only.
3. In case of winding up of company by Tribunal, which statement is prepared to be presented to the Tribunal?
- (a) Statement of affairs.
 - (b) Statement of assets and liabilities.
 - (c) Statement of deficiency.
4. Which of the following will be treated as preferential creditors?
- (a) Govt. taxes.
 - (b) Trade Creditors.
 - (c) Unsecured loans.