MANONMANIAM SUNDARANAR UNIVERSITY

DIRECTORATE OF DISTANCE
&
CONTINUING EDUCATION

ADVANCED CORPORATE ACCOUNTING

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ADVANCED CORPORATE ACCOUNTING

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ADVANCED CORPORATE ACCOUNTING

UNIT–I

ALTERATION OF SHARE CAPITAL & AMALGAMATION, ABSORPTION AND RECONSTRUCTION

Internal Reconstruction or Capital Reduction - Meaning

Reconstruction refers to reorganization of the capital structure of a company. The claims of both the shareholders and creditors against a company with a bad or sinking financial position necessitate a scheme of capital reconstruction which is called as Internal Reconstruction.

This arrangement made for the following purposes:

i) Reduction of share capital
ii) To differentiate the rights of different types of shareholders, debenture holders and creditors.
iii) To write off the accumulated losses of the company.
iv) To reduce the overvaluation of assets of the company.

Alteration of Share Capital

Alteration of share capital can be done under the provision of Sections94 to 97 of the Companies Act 1956. This includes the following:

i) Increasing the share capital by issue of fresh shares.
ii)Consolidation of shares means conversion of all or part of existing shares of smaller amounts into shares of larger amounts.
iii) Sub-division of Shares means dividing all or part of the existing shares of larger amounts into shares of smaller amounts.
iv) Conversion of fully paid up shares into stock and vice-versa.
v) Cancellation of unissued Shares

Reduction of Share Capital

Reduction of capital means cancellation of any paid-up share capital which is lost or unrepresented by available assets.

Different ways of Capital Reduction

There are three ways of capital reduction :

i) Reducing or extinguishing the uncalled liability of shareholders.
ii)Reducing by returning the excess paid-up capital of the company which is found to be in surplus of the needs of the company.
iii) Reducing or cancelling or writing off paid up capital which is lost and not represented by assets.

Procedure for Reducing share capital

i)The Articles of Association of the company should permit such reduction.
ii) A special resolution should be passed at shareholders meeting.
iii) Confirmation of the court for capital reduction must be obtained.
iv) A copy of the resolution to reduce capital and the court's order of confirmation should be filed with the Registrar of Joint Stock Companies.

Internal Reconstruction (capital Reduction) Journal Entries:-

1. For reducing the equity capital without reducing the liability

Equity Share Capital a/c Dr
To Capital Reduction a/c
(Being the paid-up equity share capital reduced)

2. For reducing the face value and paid up value of equity capital

Eq. Share Capital a/c Dr
(Old share with full value)
To Eq. Share Capital a/c
(New share with reduced value)
To Capital Reduction a/c
(Being the face value and paid up value of Eq. share capital reduced)

3. For reducing the Preference share

-% Pref. share capital a/c Dr
(Old share with old value)
To -% Pref. Share Capital
(New share with reduced value)
To Capital Reduction
(Being reduction of paid up value of P.share)

4. On sacrifice by the debenture holders / creditors

Debenture holders a/c Dr
Creditors a/c Dr
To Capital Reduction a/c
(Being the claim of debenture holder &creditors reduced)

5. For eliminating past losses and writing down the value of assets

Capital Reduction a/c
To Profit & Loss a/c
To Preliminary expenses a/c
To Goodwill a/c
To Discount on Debentures a/c
To Patents a/c
To Plant & Machinery
To Others
(Being various losses written off and assets written down)

6. For transferring the capital reduction a/c balance, if any

Capital Reduction a/c Dr
To Capital Reserve a/c
(Being the balance of capital reduction a/c transferred to capital reserve a/c)

SOLVED PROBLEMS

Problem No.1

Moon Ltd., having a share capital of Rs.3,00,000 divided into 3,000 shares of Rs.100 each, resolves to sub-divide the shares into 30,000 shares of Rs.10 each. Pass the necessary journal entry.

Books of Moon Ltd.

Journal Entry

Date	Particulars	L.F	Dr.	Cr.
	Share Capital (Rs.100) A/c Dr		3,00,000	
	To Share Capital (Rs.10) A/c			3,00,000
	(Being 3,000 shares of Rs.100 each sub-divided into 30,000 shares of Rs.10 each as per Board's resolution dated ……..)			

Problem No.2

The following is the Balance Sheet of Star Ltdason31.03.2021

Liabilities	Rs.	Assets	Rs.
1,00,000equitysharesof		Land	1,00,000
Rs.10each	10,00,000	Plant & Machinery	2,30,000
Sundry Creditors	1,73,000	Furniture & Fittings	68,000
		Stock	1,50,000
		Debtors	70,000
		Cash at Bank	5,000
		P & La/c	5,50,000
	11,73,000		11,73,000

Scheme of Capital Reduction was:

a) The equity shares to be reduced toRs.4pershare.
b) Plant and Machinery to be written down to Rs.1,50,000.
c) Stock to be revalued atRs.1,40,000.
d) TheprovisionondebtorsfordoubtfuldebtstobecreatedRs.2,000.
e) Land to be revalued at Rs. 1,42,000.

Pass journal entries to give effect to the above arrangement and also prepare reconstruction a/c.

Solution:

Journal Entries

Date	Particulars		L.F.	Debit Rs.	Credit Rs.
	Equity Share Capital a/c (Rs.10)	Dr.		10,00,000	
	To Equity Share Capital a/c (Rs.4)				4,00,000
	To Capital Reduction a/c				6,00,000
	(Being the Rs. 10 equity shares converted into Rs. 4 equity share and the balance transferred to capital reduction a/c)				
	Land a/c	Dr.		42,000	
	To Capital Reduction a/c				42,000
	(Being the appreciation of Land taken for capital reduction)				
	Capital Reduction a/c	Dr.		6,42,000	
	To Profit & Loss a/c				5,50,000
	To Plant & Machinery a/c				80,000
	To Stock a/c				10,000
	To Provision for Doubtful Debts a/c				2,000
	(Being the accumulated loss written off and the assets were reduced)				

Capital Reduction a/c

Particulars	Rs.	Particulars	Rs.
To Plant and Machinery a/c	80,000	By Equity Share Capital a/c	6,00,000
To Stock a/c	10,000	By Land a/c	42,000
To Provision for Doubtful debts a/c	2,000		
To Profit & Loss a/c	5,50,000		
	6,42,000		6,42,000

Problem No.3

The Balance sheet of Anbu Ltd on 31.12.2019 was as follows.

Liabilities	Rs.	Assets	Rs.
Authorized capital 20,000 shares of Rs.100 each	20,00,000	Land and Buildings	1,00,000
Subscribed capital 19,000 Share of Rs.10 each	19,00,000	Machinery	2,60,000
Creditors	1,00,000	Furniture	20,000
Due to Raju & Co.,	1,00,000	Stock	3,70,000
		Debtors	1,80,000
		Goodwill	2,00,000
		Profit & Loss a/c	9,70,000
	21,00,000		21,00,000

The following scheme of reconstruction was followed

a) The 19000 shares of Rs.100 each are to be reduced to an equal number of fullypaidsharesofRs.40each.

b) TheamountRs.1,00,000duetoRaju&Co.,was also to be reduced the remaining 1000 unissued shares being issued to them as fully paid up shares of Rs.40 each in full settlement of the amount due to them.

c) The amount available by the above reduction is to be utilized in writing off the goodwill, profit and Loss a/c and in writing down the value machinery.

Pass necessary journal entries and prepare the Balance sheet.

Solution:

1. 19,000 shares are reduced to Rs.40each

Old Equity share capital a/c Dr 19,00,000(19000x100)

To New Equity share capital a/c 7,60,000(19000x40)

To capital Reduction a/c 11,40,000(19000x60)

2. Raju &Co.,a/c settled by issuing 1000 shares of Rs.40 each

Raju & Co., a/c Dr	100000	
To Equity share capital (1000sharesxRs.40)		40,000
To Capital reduction a/c(1000hsaresxRs.60)		60,000

3. Utilisation of capital Reduction account:-

Capital Reduction a/c Dr	12,00,000	
To Goodwill a/c		2,00,000
To profit & Loss a/c		9,70,000
To Machinery a/c		30,000

Balance sheet (and Reduced)

Liabilities	Rs.	Assets	Rs.
Authorised capital 20,000shares of Rs.40each	8,00,000	Land & Building	1,00,000
		Machinery	2,30,000
Subscribed capital:		Furniture	20,000
20,000 share of Rs.40 each	8,00,000	Stock	3,70,000
		Debtors	1,80,000
Creditors	1,00,000		
	9,00,000		9,00,000

Amalgamation - Meaning

When two or more existing companies doing similar business go into liquidation and form a new company is called amalgamation.

Example: Hero + Honda = Hero Honda, Maruti + Suzuki = Maruti Suzuki

Absorption - Meaning

When one existing company takes over the business of one or more existing companies it is called absorption. Here no new company formed.

Example: Hutch + Vodafone = Vodafone

Reconstruction

The reconstruction is needed when a company has financially suffered due to heavy accumulated losses. For this purpose the company reorganized their financial structure it is called Reconstruction. Reconstruction may be two types.

i) External Reconstruction:

External reconstruction means the winding up of an existing company goes into liquidation and a new company is formed to taken over the business of the liquidated company which is similarly named and owned by the same shareholders.

ii) Internal Reconstruction:

It is neither liquidation nor formation of a new company. It means reduction of share capital and rearrangement of share capital and reorganization. In this case the capital structure of company is being reorganized. Thus internal reconstruction means reduction of capital to cancel any paid up share capital which is lost or unrepresented by available assets.

Purchase consideration:

Purchase consideration means the amount paid by the purchasing company to the liquidators of the selling company. The purchasing company may pay purchase amount in the form of cash, shares and debentures of a company.

Methods of Computing Purchase Consideration

The following are the different methods for calculating the amount of purchase consideration.

i) Lump Sum Method

Under this method, the purchase consideration is the agreed amount paid in lump sum.

ii) Net Payment Method

Under this method, the purchase consideration is calculated by adding the various payments made by the purchasing company in the form of cash, shares and debenture.

iii) Net assets method:

Under this method, the purchase consideration is calculated by adding the value of all assets taken over and deduct there from the amount of liabilities taken over by the purchasing company.

iv) Intrinsic value method or Value of share method or Shares exchanged method

Under this method, the purchase consideration is calculated on the basis of the ratio in which the shares of purchasing company are exchanged for the shares of selling company.

$$\text{Intrinsic value} = \frac{\text{Assets available for equity shareholders}}{\text{Number of equity share}}$$

Types of Amalgamation

According to AS – 14 amalgamations can be classified into two main categories.

i) Amalgamation in the nature of merger and

ii) Amalgamation in the nature of the purchase

i) Amalgamation in the nature of merger

An amalgamation should be considered to be an amalgamation in the nature of merger when all the following conditions are satisfied:

1. All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.

2. Shareholders holding not less than 90% of the face value of the equity shares of the transferor company (other than equity shares already hold by the transferee company or its subsidiaries or their nominees) become equity shareholders of the transferee company by virtue of the amalgamation.

3. 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 share in the transferee company, except that cash may be paid in respect of any fractional shares.

4. The business of the transferor company is intended to be carried on, after amalgamation, by the transferee company.

5. 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.

ii) Amalgamation in the nature of purchase

Amalgamations which do not satisfy one or more conditions specified for amalgamations in the nature of merger should be treated as 'Amalgamations in the nature of purchase'.

Methods of Accounting for Amalgamation

There are two main methods of accounting for amalgamation.

i) The pooling of interest method and
ii) The purchase method.

Internal Reconstruction Vs External Reconstruction

Internal Reconstruction	External Reconstruction
A company is to reorganize is capital structure or reduction of share.	One company goes into liquidation (closed).
No new company is formed	New company is formed
Capital is reduced due to construction.	Share capital is not reduced due to reconstruction.
Internal arrangement	External arrangement
It does not take over other company assets and liabilities	It takes over other company assets and liabilities

Accounting Treatment for Amalgamation
In the books of Transferor company or Selling company
Model Journal entries in the books of Selling Company (or) transferor company

1. Transferring all the assets at book value

Realisation a/c Dr
To Assets a/c(Book value)
(Being various assets transferred to realization a/c)

2. Liabilities taken over:-

Liabilities a/c Dr.
To Realisation a/c(Book value)
(Being various liabilities transferred to realization a/c)

3. Purchase consideration due

Purchasing Company a/c Dr

To Realisation a/c

(Being the Purchase Consideration due)

4. For receiving the purchase consideration

Bank a/c Dr

Shares in purchasing company a/c Dr

Debenture in the purchasing company a/c Dr

To Purchasing company a/c

(Being the purchase consideration received)

5. For assets sold by the vendor company not taken over by the purchasing company

Bank a/c Dr

To Realization a/c

(Being the Assets sold)

6. Liabilities paid by the vendor company not taken over by the purchasing company

Liabilities a/c Dr

Realisation a/c Dr

To Bank a/c

(Being repayment of liabilities)

7. a) Realisation Expenses paid by vendor company

Realisation a/c Dr.

To Bank a/c

(Being the liquidation expenses paid)

b) Realisation expenses paid by purchasing company

NoEntry

c) Liquidation expenses are reimbursed by the purchasing company

i) For payment of expenses

Purchasing company a/c Dr

To Bank a/c

ii) For getting the expenses reimbursed

Bank a/c Dr

To Purchasing company a/c

8.For settlement of pref. shareholder

a) To transfer the preference share capital

If excess payment is made:

Preference Share Capital a/c Dr

Realisation a/c Dr

To Pref. Shareholders a/c (or)

If agree to accept less than the amount due:

Preference Share Capital a/c Dr
To Preference Shareholders a/c
To Realisation a/c

b) For Settlement of the amount :

Preference Shareholders a/c Dr
To Bank

9. Transfer of Profit or Loss on realisation account:

For Profit

Realisation a/c Dr
To Equity shareholders a/c (or)

For Loss:

Equity Shareholders a/c Dr
To Realisation a/c

10. For transferring the equity share capital, accumulated profits etc.

Equity Share Capital a/c Dr
General Reserve a/c Dr
Dividend Equalization Fund a/c Dr
Share Premium a/c Dr
Profit & Loss a/c Dr
Any other reserve or Profit a/c Dr
To Equity shareholders a/c
(Being all the accumulated profits and capital transferred)

11. For transferring the accumulated losses and expenses not yet written off, if any

Equity shareholders a/c Dr
To Profit & Loss (loss) a/c
To Preliminary expenses a/c
To Discount on shares a/c
To Discount on Debentures a/c
(Being all accumulated losses transferred)

12. For final settlement

Equity Shareholders a/c Dr
To Shares in purchasing company a/c
To Debenture in the purchasing company a/c
To Bank a/c
(Being the final settlement)

Model Journal Entries in the Books of Purchasing Company (or) Transferee Company

1. For the purchase consideration due

Business Purchase a/c Dr
To Liquidators of the vendor company.
(Being the purchase consideration due)

2. For recording the assets and liabilities taken over

Various Assets a/c Dr
*Goodwill a/c (Bal. Fig.)
To Various Liabilities a/c
To Business Purchase a/c
To Capital Reserve a/c* (Bal.Fig.)
(Being the assets and liabilities taken over recorded)

Note: "Only one item will appear

3. For settlement of the purchase consideration

Liquidators of the vendor company a/c Dr.
To Equity Share Capital a/c
To Debenture a/c
To Bank a/c
(Being the final settlement made)

Note: If the shares and debentures are issued at a premium or at a discount appropriate entry should be passed)

4. For meeting the liquidation expenses of the vendor company directly

Goodwill a/c Dr
To Bank a/c
(Being the liquidation expenses paid)

I) Amalgamation in the nature of merger, under pooling of interests method:

1. For purchase consideration payable

Business Purchase A/c Dr
To Liquidator of Transferor company
[Being purchase price payable]

2. For Assets and Liabilities

Sundry Assets A/c Dr
(Each asset separately at their book values)
To Sundry Liabilities
(Each liability separately at their book values)
To Business Purchase A/c
To Profit and loss A/c
To Reserves
(Each reserve separately)
[Being assets and liabilities taken over and reserves of transferor company recorded]

3. For Payment of purchase price

Liquidator of transferor Company A/c Dr
To Bank A/c
To Share Capital A/c
To Securities Premium A/c
[Being shares issued to settle the purchase consideration]

Note: In pooling of interests method cash is paid for fractions of shares alone.

4. For expenses of winding up paid by Transferee company

General Reserve A/c Dr
To Bank
[Being expenses of transferee co., paid as per agreement]

5. For Formation Expenses paid

Preliminary expenses A/c Dr
To Bank A/c
[Being formation expenses paid]

6. For payment of any Debentures of transferor company

Debentures (Transferor Co.,) A/c Dr
To Debentures A/c
To Bank A/c
[Being payment made to debenture holders of Transferor Co., as per agreement]

7. For payment to creditors of Transferor Co.

Creditors (Transferor Co.,) A/c Dr
To Bank A/c
[Being payment as per agreement]

(II) In case of Amalgamation in the nature of purchase, under Purchase Method:

1. For Purchase consideration payable

Business purchase A/c Dr
To Liquidator of Transferor Co.,
[Being purchase price payable]

2. For Assets and Liabilities taken over

Sundry Assets A/c
(Each asset separately) Dr
Goodwill A/c Dr
To Sundry Liabilities A/c
(Each liability separately)
To Business purchase A/c
To Capital Reserve A/c
[Being assets and liabilities taken over and goodwill/capital reserve there on]

Note: In the above entry, either goodwill or capital reserve will be the Balancing figure.

3. For Payment of Purchase price

Liquidator of Selling Co. A/c Dr
To Bank A/c
To Share Capital A/c
To Securities Premium A/c
To Debentures A/c
[Being purchase price paid in the form of cash, shares and debentures]

4. For expenses of Liquidation agreed to be paid by Transferee Co.

Goodwill A/c Dr
To Bank A/c
[Being expenses agreed to be paid]

5. For Formation expenses of Transferee Co.,

Preliminary expenses A/c Dr
To Bank A/c
[Being formation expenses paid]

6. For statutory reserves of the Transferor Co. to be continued

Amalgamation adjustment A/c Dr
To Statutory Reserves A/c
[Being reserves to be continued]

7. For settlement of Debentures holders or creditors of Transferor Co.,

Debentures (transferor co.) A/c Dr
Creditors (transferor co.) A/c Dr
To Debentures A/c
To Bank A/c
[Being settlement of Transferor company's liabilities as per agreement]

Problem No.4

A Co.Ltd. agreed to acquire the assets excluding cash as on 31st December 2020 of B Co.Ltd. The balance sheet of B Ltd. as on that date was:

Liabilities	Rs.	Assets	Rs.
Equity capitalRs.10each	3,00,000	Goodwill	60,000
General reserve	60,000	Land & Building	1,20,000
Debentures	50,000	Plant & Machinery	2,00,000
Creditors	10,000	Stock	80,000
Profit & Loss	80,000	Debtors	30,000
		Bank	10,000
	5,00,000		5,00,000

The consideration was as follows:

a) A cash payment of Rs.4 for every shares of B Ltd.
b) The issues of one share of Rs.10 each (Market value Rs.12.50) in the A Co. Ltd. For every share in B Co.Ltd.
c) The issue of 1100 debentures of Rs.50 each in A Co.Ltd.to enables B Ltd to discharge its debentures at a premium of 10%.
d) The expenses of liquidation of B Ltd. Amounting to Rs.4000 were to be met by themselves.

Give the journal entries in the books of both the companies.

Solution:

Journal Entries in the Books of B Co.Ltd.

1.	Realisation a/c	Dr	4,90,000	
	To Goodwill			60,000
	To Land & building			1,20,000
	To Plant & machinery			2,00,000
	To Stock			80,000
	To Debtors			30,000
2.	Creditors a/c	Dr	10,000	
	To Realisation			10,000
3.	Debentures a/c	Dr	50,000	
	Realisation a/c	Dr	5,000	
	To Debenture holders a/c			55,000
4.	White Co.Ltd.	Dr	4,75,000	
	To Realisation			4,75,000
5.	Bank a/c	Dr	1,20,000	
	Shares a/c	Dr	3,00,000	
	Debentures a/c	Dr	55,000	
	To White Co.Ltd			4,75,000
6.	Realization a/c	Dr	10,000	
	To bank a/c			10,000
7.	Share capital a/c	Dr	3,00,000	
	General reserve a/c	Dr	60,000	
	Profit & Loss a/c	Dr	80,000	
	To Shareholders a/c			4,40,000
8.	Shareholders a/c	Dr	24,000	
	To Realisation a/c			24,000

9.	Shareholders a/c	Dr	4,16,000	
	To Shares			3,00,000
	To Bank			1,16,000
10.	Debenture holders a/c	Dr	55,000	
	To Debentures			55,000
11.	Realisation a/c	Dr	4,000	
	To Cash			4,000

Journal Entries in the Books of A Co.Ltd.

1.	Business purchase a/c	Dr	4,75,000	
	To Liquidator of B co. a/c			4,75,000
2.	Goodwill	Dr	45,000	
	Land & building	Dr	1,20,000	
	Plant & machinery	Dr	2,00,000	
	Stock	Dr	80,000	
	Debtors	Dr	30,000	
	To Business purchase a/c			4,75,000
3.	Liquidator of B co.a/c	Dr	4,75,000	
	To Share capital			2,40,000
	To Share premium			60,000
	To Debenture			55,000
	To Bank			1,20,000

Problem No.5

The following is the balance sheet of Ambika Ltd.

Liabilities	Rs.	Assets	Rs.
20,000 10% Pref. shares of Rs.10 each	2,00,000	Goodwill	50,000
2,000 equity shares of Rs.100 each	2,00,000	Other Fixed Assets	1,80,000
Creditors	30,000	Stock	50,000
		Debtors	60,000
		P & La/c	90,000
	4,30,000		**4,30,000**

The following resolutions were passed and the scheme was duly approved by the court:

i) Equity shares of Rs.100 each be reduced to fully paid up shares of Rs.50 each.

ii) 10% Pref. shares of Rs.10 each be reduced to 10% Pref. shares of Rs.6 each fully paid up.

iii) Goodwill and debit balance of Profit & Loss a/c fully written off.

iv) The balance of the amount be used to write off other fixed assets.

Give journal entries and revised Balance Sheet of the company. Also prepare Capital Reduction Account.

Solution:

Journal Entries in the Books of Ambika Ltd.

1.	Old Equity Share Capital a/c	Dr	2,00,000	
	To New Eq. Share capital a/c			1,00,000
	To Capital Reduction a/c			1,00,000
2.	Old Pref. share capital a/c	Dr	2,00,000	
	To New Pref. share capital a/c			1,20,000
	To Capital Reduction a//c			80,000
3.	Capital Reduction a/c	Dr	1,80,000	
	To Goodwill a/c			50,000
	To Profit & Loss a/c			90,000
	To Fixed assets a/c			40,000

Capital Reduction Account

	Rs.		Rs.
To Goodwill a/c	50,000	By Eq. share capital	1,00,000
To P/L a/c	90,000	By Pref.share capital	80,000
To Fixed Assets a/c	40,000		
	1,80,000		**1,80,000**

Balance Sheet of Ambika Ltd.

	Rs.		Rs.
Pref. share capital	1,20,000	Fixed assets	1,40,000
Equity share capital	1,00,000	Stock	50,000
Creditors	30,000	Debtors	60,000
	2,50,000		**2,50,000**

Absorption

Problem No.6

White Ltd agreed to acquire the business to Green Ltd as an 31st December 2020, The Balance sheet of Green Ltd on that date was as follows:

Liabilities	Rs.	Assets	Rs.
Share capital in fully paid shares of Rs.10	6,00,000	Goodwill	1,00,000
General Reserve	1,70,000	Land and Buildings	3,00,000
Profit & Loss a/c	1,10,000	Plant	3,40,000
6% Debentures	1,00,000	Stock	1,68,000
Creditors	20,000	Debtors	36,000
		Cash	56,000
	10,00,000		10,00,000

The consideration payable by White Ltd was agreed as follows

a) A cash payment equivalent to Rs2.50 for every Rs.10 shares in Green Ltd.

b) The issue of Rs. 90,000 Rs.10 shares fully paid in white Ltd having an agreed value of Rs.12.50pershare.

c) The issue of such an amount of fully paid 5% Debenture of white Ltd at 96% as is sufficient to discharge the 6% Debentures of Green Ltd at a premium of 20%.The directors of white Ltd valued Land and Buildings at Rs.4,00,000 and created 5% provision on debtors. Expenses of Liquidation Rs.6,000 were paid by white Ltd.

Give journal entries to close the books of Green Ltd. and to record the acquisition of business in the books ofwhite Ltd.

Solution: **Calculation of purchase consideration:**

Form		Amounts
1) Cash 60,000 shares x Rs.2.50	=	1,50,000
2) Equity shares 90,000 shares xRs.12.50	=	11,25,000
3) 5% Debentures1,00,000x20/100	=	1,20,000
Purchase consideration	=	**13,95,000**

Journal entries:

In the books of Green Ltd (Liquidator of Vendor company)

1) Assets taken over by white Ltd (Book value)

Realisation a/c Dr	10,00,000	
To Good will a/c		1,00,000
To Land and Building a/c		6,40,000
To Stock a/c		1,68,000
To Debtors a/c		36,000
To Cash a/c		56,000

2) For Liabilities taken over by white Ltd

Creditors a/c Dr	20,000	
To Realisation a/c		20,000

3) Purchase consideration due from white ltd:

White Ltd a/c Dr	13,95,000	
To Realisation a/c		13,95,000

4) Purchase consideration

Cash a/c	Dr	1,50,000	
Equity shares a/c	Dr	11,25,000	
5% Debentures a/c	Dr	1,20,000	
To white Ltd a/c			13,95,000

5) 6% debentures is discharged by issuing 5% Debentures in white Ltd:

6% Debenture a/c Dr	1,00,000	
Realisation a/c Dr (Loss)	20,000	
To Debenture holders a/c		1,20,000

6) **Transfer:**

Debenture holders a/c Dr	1,20,000	
To 5% Debenture a/c		1,20,000

7) Accumulated profits and share capital transferred:

General Reserve a/c Dr 1,70,000

Profit and Loss a/c Dr 1,10,000

Equity share capital a/c Dr 6,00,000

To Equity shareholders a/c 8,80,000

8) Profit on realisation

Realisation a/c Dr 3,95,000

To Equity shareholders a/c 3,95,000

9) Final payment made

Equity shareholders a/c Dr 12,75,000

To Shares in White Ltd a/c 11,25,000

To Bank a/c 1,50,000

Realisation Account

To Goodwill	1,00,000	By Creditors	20,000
To Land & Buildings	3,00,000	By white Ltd	13,95,000
To Plant	3,40,000		
To Stock	1,68,000		
To Debtors	36,000		
To Cash	56,000		
To Debenture holders(loss)	20,000		
To Equity shareholders (profit)(b.f.)	3,95,000		
	14,15,000		14,15,000

In the books of White Ltd., (purchasing company)

1) **Purchase consideration to be paid**

Business purchase a/c Dr 13,95,000

To Liquidator of Green Ltd 13,95,000

2) **Assets and Liabilities recorded at revised value**

Land and Buildings a/c Dr 4,00,000
Stock a/c Dr 1,68,000
Plant a/c Dr 3,40,000

Debtors a/c	Dr	56,000	
Cash a/c	Dr	36,000	
Goodwill a/c (b.f)	Dr	4,17,800	
To Creditors a/c			20,000
To Provision for doubtful debts			2,800
To Business purchase a/c			13,95,000

3) Purchase Consideration paid

Liquidator's of Green Ltd. a/c	Dr	13,95,000	
Discount on issue of Debenture a/c	Dr	5,000	
To Equity Share Capital			9,00,000
To Share premium			2,25,000
To 5% Debenture			1,25,000
To Bank			1,50,000

4) Liquidation expenses paid

Goodwill a/c	Dr	6,000	
To Bank			6,000

Unit –II

Valuation of Goodwill & Liquidation of Companies

Valuation of Goodwill

Meaning of Goodwill

Goodwill means the 'good name' or the 'reputation' of the business house. It is an Intangible asset. It helps to earn more profits in future.

Definition of Goodwill

"Goodwill is the present value of a firm's anticipated excess earnings".

- Dr.Canning

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

Factors determining the value of Goodwill

The following are the main factors which affect the value of the goodwill of the firm.

1. Profitability:

The term profitability refers to the profit which the firm's expected to earn in future. The profit earning capacity of the business depends upon

i) Nature of business and goods

ii) Location of business

iii) Efficiency of management and employees.

2. Normal rate of return

It refers to the rate of earnings which investors in general expect on their investment in a particular type of industry.

3. Capital employed

The term capital employed represents the equity shareholders funds in the company along with long term borrowings.

1. Other factors

Some other factors are also determining the value of goodwill. They are

i) Market conditions

ii) Competition

iii) Better financial relationship

iv) Risk in business

Methods of valuation of goodwill

The following methods are followed for valuing goodwill

1. Average profit method
2. Super profit method
3. Capitalisation method

1. Average profit method.

This method is adopted by sole traders and partnership firm. Under this method goodwill is valued on the basis of an agreed number of year's purchase of the average maintainable profit.

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

Value of goodwill = Average Profit x No.of year's purchase

2. Super profit method:-

Super profit is the difference between average profits and normal profits.

a) Super profit=Average profit–Normal profit

b) Goodwill=Super profit x Number of year's purchase

i) Normal profit = Average capital employed x Normal rate of return

ii) Average capital employed = Opening (or) Closing Capital employed + ½ of the profit

3. Capitalisation Method:

Under this method the goodwill will be the difference between the total value of the business and its net assets.

$$\text{Capitalised value of profit} = \frac{\text{Average maintainable profit}}{\text{Normal rate of return}} \times 100$$

Value of goodwill = Capitalised value of profit – Net Tangible Assets

Note: Net Tangible Assets = Total assets (excluding goodwill) – Liabilities

Problem No.1

Calculate the amount of goodwill on the basis of 3 years purchase of the last five years' average profits. The profits for the last five years are: 8,200; 10,500; 5,100; 7,700; 12,000.

Solution:

Years	**Rs.**
I year	8,200
II year	10,500
III year	5,100
IV year	7,700
V year	12,000
Total	**43,500**

Calculation of Average Profit

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

$$= 43{,}500/5 = \text{Rs.}8{,}700$$

Value of goodwill = Average Profit x No.of years' purchase
= Rs.8,700 x 3 = Rs.26,100.

Problem No.2

Goodwill is to be valued at 2 years purchase of five years' average profits. The profits for the last five years of the firm were:

2014 – Rs.24,000;

2015 – Rs.30,000;

2016 – Rs.34,000;

2017 – Rs.32,000;

2018 – Rs.40,000.

Calculate the amount of goodwill.

Solution:

Calculation of Average Profit

Years	Rs.
2014	24,000
2015	30,000
2016	34,000
2017	32,000
2018	40,000
Total	**1,60,000**

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

= 1,60,000/5 = Rs.32,000

Value of goodwill = Average Profit x No.of years' purchase
= Rs.32,000 x 2 = Rs.64,000.

Problem No.3

A firm earned net profits during the last three years as follows:

I year Rs.36,000
II year Rs.40,000
III year Rs.44,000

The capital investment of the firm is Rs.1,00,000.

A fair return on the capital, having regard to the risk involved is 10%.

Calculate the value of goodwill on the basis of 3 years' purchase of super profit.

Solution:

i) Calculation of average profit

I year	36,000
II year	40,000
III year	44,000
	=======
Total profit	1,20,000
	=======

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

= 1,20,000/3 = Rs.40,000.

ii) Calculation of normal profit

Normal profit = Capital employed X Normal rate of return
= 1,00,000 X 10%
= Rs.10,000.

iii) Calculation of super profits

Super profit = Average profit – Normal profit
= Rs.40,000 – Rs.10,000
= Rs.30,000.

iv) Calculation of value of goodwill

Goodwill = Super profits x No.of years' purchase
= Rs.30,000 x 3
= Rs.90,000.

Problem No.4

From the following information calculate the value of goodwill according to super profit basis at five years purchase.

Average capital employed in the business Rs.5,00,000. Net trading profits of the concern for the past four years:

Rs.1,00,000; Rs.1,20,000; Rs.1,40,000; Rs.1,60,000.

Rate of interest expected from capital having regard to the risk involved 15%. Fair remuneration to the proprietor for services Rs.30,000 per annum.

Solution:

i) Calculation of average profit

I year	1,00,000
II year	1,20,000
III year	1,40,000
IV year	1,60,000
	=======
Total profit	5,20,000
	=======

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

= 5,20,000/4 = Rs.1,30,000.

Less: Remuneration to proprietor	30,000
	=======
Average adjusted profit	1,00,000
	=======

ii) Calculation of normal profit

Normal profit = Capital employed X Normal rate of return
= 5,00,000 X 15%
= Rs.75,000.

iii) Calculation of super profits

Super profit = Average profit – Normal profit
= Rs.1,00,000 – Rs.75,000
= Rs.25,000.

iv) Calculation of value of goodwill

Goodwill = Super profits x No.of years' purchase
= Rs.25,000 x 5
= Rs.1,25,000.

Problem No.5

From the following information, calculate the value of goodwill:

i) Average capital employed in the business Rs.70,000.
ii) Trading profit of the firm for the past three years Rs. 14,760, Rs. 14,810 and Rs.15,200.
iii) Normal rate of the return expected-18%.
iv) Fair remuneration to the partners for their services Rs.1,200 per annum.
v) Sundry assets (excluding goodwill) of the firm – Rs. 75,475 sundry liabilities–Rs.3,133.

Solution:

i) Average Profit Method

Goodwill =Average profit x Number of years of purchase
=13,723x3
=**Rs.41,169**

ii) Super Profit Method

Goodwill=Super Profit x Number of years of Purchase
Super Profit =Average Profit–Normal Profit
Normal Profit= Normal rate of return x capital employed
=70,000x18/100
=Rs.12,600
Super Profit =13,723–12,600
=Rs.1,123
Goodwill =1,123x3
=**Rs.3,369**

iii) Capitalisation of super profit method

Goodwill =Super Profit/Normal rate of return
=1,123x100/18
=**Rs.6,239**

iv) Capitalisation Method

Goodwill =Total value of business–Net assets
Total value of business =Average Profit x 100/Normal rate of return
Net assets =Total assets–Liabilities
=75,476–3,133
=Rs.72,343
Value of business =3,723x100/18
=Rs.76,239
Goodwill =76,239–72,343
=**Rs.3,896**

Valuation of shares

Every business will have its own capital. Like this a company will have its own Capital. The share capital of a company is divided into units of small denomination. Each unit of such small denomination is called a share. As per Sec. 2 (46) of the Companies Act, 1956, Share means one of the parts of capital of the company that is divided among several people and includes stock except where a distinction between stock and share is expressed or implied. Valuation of shares involves the use of financial and accounting data based on the objective and subjective consideration for a specific purpose.

Value of shares may be of the following types:

i) Par value ii) Book value
iii) Market value iv) Purchase value
v) Capitalized value vi) Intrinsic value
vii) Fair value

Need and Importance of valuation of shares

Shares must be valued due to the following reasons:-

1. For the purpose of purchase and sale of business in private companies
2. For estate duty and wealth tax purpose
3. For the purpose of Amalgamation and Absorption of companies
4. For the purpose of issuing bonus shares or making rights issue.
5. For the purpose of transfer of shares.
6. Holding company purpose.
7. When shares are pledged as a security against loan
8. Unquoted shares in the stock exchange market.
9. When shares of one class are converted into another class.
10. For the purpose of assessing the value of assets of finance and government trusts.

Factors affecting the valuation of shares

a] Profitability

b] Yield Expected by the Investors

c] Capital employed

d] Other factors [political, economical and social conditions,

Govt. policies etc.,

Methods of valuation of shares

The following are the various methods for valuation of shares

i) Net assets (or) intrinsic value method

ii)Yield method

iii) Earning capacity method

iv) Fair value method.

i) Net Asset Method [Intrinsic value or breakup value method]

Under this method net assets of the company are divided by the number of share to arrive at the net asset value of each share.

$$\text{Net assets value} = \frac{\text{Net value of assets – Liabilities – Preference shareholders claims}}{\text{Number of Equity shares}}$$

ii) Yield Method or Income method or market value method

Yield an effective rate of return from similar types of securities. The yield as prevailing in the industry is known as normal rate of return and is considered as a base while ascertaining the market value of shares.

$$\text{Value per share} = \frac{\text{Expected rate of return}}{\text{Normal rate of return}} \text{X Paidup value per equity share}$$

$$\text{Expected Rate} = \frac{\text{Profit available to equity shareholders}}{\text{Paid up equity share capital}} *100$$

iii) Earning Capacity method:

Under this method the value of share is found out by comparing the company's earning capacity and the normal rate of return on capital employed.

$$\text{Value per share} = \frac{\text{Rate of Earnings}}{\text{Normal rate of return}} \text{X Paid up value per equity share}$$

$$\text{Rate of earnings} = \frac{\text{Profit earned}}{\text{Capital employed}} \times 100$$

Expected profits may be calculated as follows:

Average Profit	xxx
Less:Tax	xxx
Profit after tax	xxx
Less: Transfer to Reserve	xxx
Preference dividend	xxx
Profit available to equity shareholders	xxx

iv) Fair value method

Fair value of share is the simple average of net assets value and yield value.

$$\text{Fair value} = \frac{\text{Net asset method} + \text{yield method}}{2}$$

Problem No.6

On 31st December 2016 the Balance Sheet of a limited company disclosed the following position:

Liabilities	Rs.	Assets	Rs.
Issued capital:		Fixed Assets	10,00,000
Shares of Rs.10 each	8,00,000	Current assets	4,00,000
Reserves	1,80,000	Goodwill	80,000
Profit & Loss a/c	40,000		
10% Debentures	2,00,000		
Current liabilities	2,60,000		
	14,80,000		**14,80,000**

On 31st December 2016 the fixed assets were independently valued at Rs.7,00,000 and goodwill at Rs.1,00,000.Net profit for the three years are:

2014 – Rs.1,03,200
2015 – Rs.1,04,000
2016 – Rs.1,03,300

Of these 20% as placed to reserve. This proportion was considered reasonable in the industry in which the company is engaged. Fair investment return may be taken at 10%.

Compute company's share value by

i) Net Assets method and
ii) Yield method.

Solution:

1. Net Assets Method

$$\text{Net asset value of each share} = \frac{\text{Net assets available for equity shareholder}}{\text{Number of equity shares}}$$

$$= \frac{7,40,000}{80,000} = \text{Rs.}9.30$$

Calculation of net assets available to equity shareholders:

	Fixed assets	7,00,000	
	Goodwill	1,00,000	
	Current assets	4,00,000	
	Total assets		12,00,000
Less:	Liabilities		
	10% Debentures	2,00,000	
	Current liabilities	2,60,000	4,60,000
	Net Assets		**7,40,000**

2. Yield Method

$$\text{Value per Share} = \frac{\text{Expected rate of return}}{\text{Normal rate of return}} \times \text{Paid up value per Share}$$

$$= \frac{10.35}{10} X 10$$

$$= \text{Rs. } 10.35$$

$$\text{Expected Rate of Return} = \frac{82,800}{8,00,000}$$

$$= 10.35\ \%$$

Problem No.7

Following is the Balance sheet of Mohan Ltd as on 31.12.2021

Liabilities		Assets	
Equity share capital		Fixed assets	45,00,000
Share of Rs.100 each	50,00,000	Current assets	24,50,000
Reserves	14,00,000	Goodwill	10,00,000
Profit & Loss a/c	1,00,000		
5%Debentures	12,00,000		
Current Liabilities	2,50,000		
	79,50,000		79,50,000

The fixed Assets were valued at rs.40,00,000 and good will Rs.2,00,000 the net profits for the past three years were Rs. 1,50,000 Rs.2,10,000 andRs.3,40,000respectively. Fair Return On Investments May be taken as 14% for companies engaged in similar business compute the Value of shares by a] Net asset method b] Yield method.

Solution:

1] Valuation of Equity share according to Net asset method (Asset at market value):

Fixed assets	=	40,00,000
Current assets	=	24,50,000.
Goodwill	=	2,00,000
Total Assets	=	66,50,000
Less: Liabilities		
5% Debentures	=	12,00,000
Current Liabilities	=	2,50,000
Amount available toequity shareholders		52,00,000

Value per Equity share = $\frac{\text{Amount available to Equity shareholders}}{\text{Number of Equity shares}}$

= $\frac{Rs.52,00,000}{50,000 \text{ shares}}$ =Rs.104 $\frac{Rs.50,00,000}{100 \text{ per share}}$ =50,000 shares

2] Valuation of Equity share according to yield method value per Equity share:

$$=\frac{\text{Expected rate of return}}{\text{Normal rate of return}} \times \text{Paid up value per share}$$

To calculate expected rate of return:

$$=\frac{\text{Profit available to Equity shareholders}}{\text{Paid up Equity share capital}} \times 100$$

Net Profits for the past three years	1,50,000
	2,10,000
	3,40,000
	7,00,000
Average profit	$\frac{7,00,000}{3}$=Rs.2,33,333

Profit available to Equity shareholders= Rs.2,33,333/-

Expected rate of return= $\frac{2,33,333 \times 100}{50,00,000}$=4.66

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

$= \frac{4.66}{14}$x100=Rs.33.33

3) Fair value per share

=Value as per Net assets method + Value as per yield method

$=\frac{\text{Rs.}104+33.33}{2} = \frac{137}{2}$=Rs.68.66

Problem No. 8

From the following information calculate value of Equity shares.

1. 4,000 8% preference shares of Rs.100 each Rs.4,00,000
2. 5,000 equity shares of Rs.20 each at Rs.16 per share paid up Rs.8,00,000
3. Expected profits for the year before tax Rs.5,00,000
4. Rate of tax 50%
5. Transfer to General reserve 20% of the profits
6. Normal rate of earnings (Return) 14%

Solution:

Calculation of profit available to Equity shareholders

Expected profits	Rs.5,00,000
Less: 50% Income tax	Rs.2,50,000
Profit after tax	Rs.2,50,000
Less: 20% Transfer to General reserve Rs.2,50,000 x $\frac{20}{100}$	Rs. 50,000
	Rs.2,00,000
Less: Preference dividend 4,00,000x8/100 =	32,000
Profit available to Equity shareholders	1,68,000

Expected Rate of Return

$$= \frac{\text{Profit available to Equity shareholders}}{\text{Paid up equity capital}} \times 100$$

$$= \frac{1,68,0000}{8,00,000} \times 100 = 21\%$$

Value per equity share as per yield method.

$$\text{Value per equity share} = \frac{\text{Expected rate of return}}{\text{Normal rate of return}} \times \text{Paid up value per share}$$

$$= 21/14 \times 16$$

= Rs.24

Problem No.9

Babu Ltd has 10000 equity shares of Rs.10 each (Rs.8 paid) and 1,00,000/- 6%preference shares of RS.10 each fully paid. The company has a practice of transferring 20% of the profit to general reserve every year. If the expected profit before tax is Rs.2,00,000/- and the rate of tax is 50% calculate the value of equity shares (Normal rate of dividend is 20%)

Solution:

Profit available to Equity shareholders

Expected profits	2,00,000
Less:50% tax(2,00,000x50/100)	1,00,000
Profit after tax	1,00,000
Less:20%Profit transferred to general reserve	20,000
(1,00,000x20/100)	80,000
Less: Dividend paid to preference shareholders	60,000
Profit available to Equity shareholders	20,000

Calculation of Expected rate of return

$$\text{Expected rate} = \frac{\text{Profit available}}{\text{Paid up Equity capital}} \times 100$$

Paid up Equity capital=10,000/-shares x Rs.8= Rs.80,000

$$= \frac{20,000}{80,000} \times 100 \quad = \text{Rs.}10$$

Value per Equity share as per yield method

$$\text{Value per Equity share} = \frac{\text{Expected rate of return}}{\text{Normal rate of return}} \times \text{paid up value per share}$$

$$= 25/20 \times \text{Rs.}8$$

$$= \text{Rs.}10.$$

Liquidator's Final Statement of Accounts

Meaning of Liquidation:-

Liquidation (or) winding up is the legal procedure by which the company comes to an end. It is a process by which a company is dissolved and its assets realized and applied in paying off the liabilities of the company.

Modes of winding up (Liquidation)

A company can be liquidated in any of the following three ways:

1. Compulsory winding up by the court
2. Voluntary winding up by the
   - i) Members voluntary winding up
   - ii) Creditors voluntary winding up
3. Winding up under the supervision of the court

Liquidator–meaning

Liquidator is a person appointed by the court or by the members or by the creditors to perform liquidation work of the company.

Liquidator's final statement of account:

It is the duty of the liquidator to realise the assets and settle the claim of the company. For this purpose he prepares a cash book for recording receipts and payments and submit the same to the court or members or creditors of the company as the case may be. He is required to prepare a statement which shows total cash received and amount distributed to creditors, debenture holders and shareholders of the company.
Such a statement is known as Liquidator's final statement of account.

Liquidator final statement of account (specimen)

Specimen form of Liquidator final statement of account

Receipts		Payments	
To Balance b/d			
To Opening balance of cash in hand	xx	By Secured Creditors	xx
Cash at Bank	xx	By Liquidation expenses	xx
To Assets realized	xx	By Liquidator’s Remuneration	xx
To Stock	xx	By % on amount realized	xx
To Machinery	xx	By % on amount distributed to unsecured creditors	xx
To Furniture	xx	By Debenture holders	xx
To Debtors	xx	By Preferential creditors	xx
To Surplus from securities	xx	By Unsecured creditors	xx
		By Preference shareholders	xx
		By Equity shareholders	xx
	xx		xx

Contributory

Contributory is a member who is liable to pay amount of the company at the time of liquidation of a company. He may be present members or past members.

Preferential creditors

Preferential creditors are those creditors having priority of claims over other unsecured creditors. They are 1) any amount due to Government 2) Salary payable employees.3) All sums due to compensation under the workmen compensation act 4) All sums due to an employee from provident fund, pension fund.

Liquidator's Final Statement of Account

Problem No.10

The following particulars relate to a limited company which has gone into voluntary liquidation. Prepare the liquidator's final account allowing for his remuneration at 2% on the amount realized and 2% on the amount distributed among unsecured creditors other than preferential creditors.

	Rs.
Preferential creditors	10,000
Unsecured creditors	32,000
Debentures	10,000

The assets realized the following sums:

Building	20,000
Machinery	18,650
Furniture	1,000

The Liquidation expenses amount to Rs.1000

Solution:

Liquidator's final statement of Account

Receipts	Rs	Payments	Rs
Building	20,000	By Liquidation expenses	1,000
Machinery	18,650	By Liquidator's Remuneration	
Furniture	1,000	By 2% on amount realized	
		39650x2/100= 793	
		By 2% on amount paid to	
		Unsecured creditors* 350	1,143
		By Debenture holders	10,000
		By Preferential creditors	10,000
		By Unsecured creditors**	17,507
	======		=======
	39,650		**39,650**

Calculation of amount paid to unsecured creditors:

Amount available to unsecured creditors:

Total Receipts		39,650
Less: Payments Liquidation expenses	1,000	
Liquidator's Remuneration amount realised	793	
Debenture holder-paid	10,000	
Preferential creditors-paid	10,000	21,793
Amount available to unsecured creditors		17,857
		=======

Calculation of Liquidators remuneration 2% on amount distributed among unsecured creditor:

Commission=Amount Availablex 2/102

17857x2/102=350

Amount paid to unsecured creditors17857– 350=17507**

Problem No.11

Krishnan Ltd was liquidated on 31-12-2021.The Balance sheet as on 31-12-2021.

Liabilities	Rs.	Assets	Rs.
Share capital	1,00,000	Land and Building	60,000
8% Debenture	1,00,000	Plant and Machinery	60,000
Mortgage Loan (Secured loan on Building)	50,000	Stock	60,000
Sundry Creditors	80,000	Debtors	70,000
		Cash in hand	5,000
		Profit and Loss a/c	75,000
	3,30,000		3,30,000

Assets realized as follows:

a) Land and Building Rs.55,000

b) Stock Rs.20,000

c) Plant & Machinery Rs.25,000

d) Half of the debtors were bad and the balance realized 60% book value.

e) Liquidator was entitled to a commission of 3% on amount realized other than cash and 2% on the amount paid to unsecured creditors.

f) Preferential creditors amount to Rs.10000(included in sundry creditors)

g) Liquidation expenses amount to Rs.970. Prepare liquidator's final statement of account.

Solution:

Liquidator's final statement of Accounts

Liabilities		Rs.	Assets	Rs.
To Cash in hand		5,000	By Secured creditors (mortgage Loan)	50,000
To Assets Realised:			Liquidation expenses	970
Land & Building	55,000		Liquidator's Remuneration 3% on amount realized except cash 121000 x 3/100	3,630
Stock	20,000		Amount paid to debenture holders	61,200
Plant & Machinery	25,000		Payment to preferential creditors	10,200
Debtors	21,000	1,21,000		
		1,26,000		1,26,000

Note:1)Debtors Realised:

Debtors	70000
Less:50% Bad	35000

Balance 60% realised	35000

35000x60/100=21000*

Illustration:11

The following particulars relate to a company which has gone into liquidation. You are required to prepare the liquidator's final statement of account allowing for his remuneration of 3% as amounts paid to unsecured creditor other than preferential creditors.

Preferential creditor Rs.12,000

Unsecured creditor Rs.40,000

Debentures Rs.14,000

Assets realized Rs.40,000 and liquidation expenses amounted Rs.4,000.

Solution:

Liquidator's final statement of account

Receipts	Rs.	Payments	Rs.
Assets realised	40000	Liquidation expenses Liquidator's Remuneration 3% amount paid to unsecured creditors Debentures Preferential creditors Unsecured creditors	4,000 291 14,000 12,000 9709
	40,000		40,000

Calculation of Commission Payable to Liquidator

Commission = Amount available x3/103

Amount available:

Total Receipts		40,000
Less: Payments liquidation expenses	4,000	
Debentures	14,000	
Preferential creditors	12,000	30,000
		10,000

10000x3/103=291*

ii) Amount payable to unsecured creditors

Amount available	10000
Less: Commission	291

	9709*

Unit- III
Accounts of Banking Companies

Meaning of Bank

Bank is a place for accepting money from the public, lending money to the public and keeping valuables safely, the amount being paid out on the customer's order, that is cheque.

Definition of Banking

The Banking Regulation Act 1949 defines banking as "accepting, for the purpose of lending or investment, of deposits of money from the public repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise".

Legal Requirements

1. Prescribed form

As per sec 29 to 33 of the Banking Regulation Act every banking company isrequired to prepare a Balance sheet in accordance with form A set out in the Third Schedule and a profit & loss account in accordance with form B set out in the Third schedule.

2. Accountingyear

A Banking company closes its accounts on 31st March every year.

3. Prohibition of Trading

A banking company cannot directly or indirectly deal with buying (or) selling (or) bartering of goods.

4. Non–Banking assets

A banking company can not held any immovable property except certain assets charged due to failure of debtor repay loan on time. It can be disposed off by the banking company within 7 years of its purchase. It is termed as non-Banking assets.

5. Share capital

Minimum capital of Rs.20 lakhs if the bank has a place of business in Mumbai or Kolkatta city and if the bank has a place of business other than Mumbai or Kolkatta city is Rs.15 Lakhs.

6. Reserve fund

It is obligator for a banking company in India to create a reserve fund and 25% of its profits. Statutory Reserve is created 25% of its annual profits.

7. Payment of commission, Brokerage

A banking company can pay any commission, brokerage, discount or remuneration in respect of shares by it not exceeding 2 ½ % paid up value of the shares.

8. Charge on uncalled capital:

A banking company cannot create any charge upon its uncalled capital and any such charge shall be void.

9. Payment of Dividend:

A Banking company cannot pay dividend on its shares until all its capitalized expenses (preliminary expenses) have been completely written off.

10. Cash Reserve: **-**

Every scheduled Bank has to maintain a sum equal to at least 3% of its time and demand liabilities as cash reserve with Reserve Bank of India.

11. Statutory Reserve:-

It is compulsory for every banking company to create a statutory Reserve fund of 25% of its annual profits.

12. Statutory Liquidity Ratio (SLR)

In addition to the cash reserve every banking company is required to maintain in India in cash, Gold and unencumbered securities an amount which shall not be less than 25% of its time and demand Liabilities. It is known as statutory liquidity Reserve.

13. Loans and advances:-

As per Banking Regulation Act 1949, imposes certain restriction on loans granted by banks to the following persons any of its directors – any firm – any company, It cannot lend on the security of its own shares.

Rebate on Bills Discounted

When a bill is discounted, it credits the full amount of discounts on all bills to discount account.

Journal entry

Bill Discounted a/c(full amount) Dr xx

To Customer a/c (face value–(Discount) xx

To Discount a/c (discount) xx

Sometimes the discounted bills may not be maturing by the end of the year. The discount relating to the unexpired portion of the bill is strictly not earned for the current year hence it should be carried forward to the next year. All such discount relating to unexpired time of such bill is debited to discount onbill a/c and credited to rebate on bills discounted account.

Entry :-

Discount a/c Dr xx

To Rebate on Bills discounted a/c xx

It is an Income received in advance and it should be shown schedule 5 under the head other liabilities of the Balance sheet. It is known as Rebate on Bills discounted.

Non - performing assets (NPA)

A Bank earns interest from customers through term loans, cash credit and overdrafts. If the interest or instalment of principal or both from customer is delayed and not received before the specified time it is called as Non - performing assets. The specified time to receive Interest or principal is 180 days in case of term loan, cash credit and overdraft.

Assets classification and provisions for Doubtful debts:

Banks are required to classify the advances into four categories.

i) Standard Assets:

A standard asset is one which **is not a non-performing** asset which does not show any problem. The banks have to make general provisions of 0.25% on standard assets.

ii) Sub–standard Assets:

It is a non-performing asset for a period not exceeding 18 months for this a provision of10% of total outstanding is made.

iii) Doubtful Assets:

It is a non performing asset for a period exceeding 12 months.

A Provision for doubtful debts against such advances has to be created as follows:

a) First year: 100% of unsecured portion + 20% of secured portion.

b) Second and Third year: 100% of unsecured portion + 30% of secured portion.

c) Beyond 3 years: 100% of unsecured portion + 50% of secured portion.

iv) Loss assets:

These assets are not controllable for this purpose the entire assets should be written off or100% provision should be made.

Licensing of banking companies:-

Every banking can function in India only after obtain license from Reserve Bank of India. Even to open branches in India or overseas.

Specimen of Profit & Loss account of a Bank for the year ended 31st March ----- Form B –Third Schedule Rs.'000

		Schedule No	Year ended 31-03-........ Current year	Year ended 31-03-....... Previous year
I	**INCOME**			
	Interest earned	13	xx	xx
	Other Income	14	xx	xx
II	**EXPENDITURE:**			
	Interest expended	15	xx	xx
	Operating Expenses	16	xx	xx
	Provisions and contingencies		xx	xx
			xxx	xxx
III	**Profit/Loss**			
	Net profit / Loss for the year		xx	xx
	Profit/Loss brought forward		xx	xx
	Total		xx	xx
IV	**Appropriations**			
	Transfer to statutory reserve		xx	xx
	Transfer to other reserve		xx	xx
	Transfer to Govt. /Proposed Dividend		xx	xx
	Balance carried over to Balance sheet		xx	xx
	Total		xx	xx

Schedule 13–Interest Earned

		Year ended 31-03- Current year	Year ended 31-03---- Previous year
1.	Interest / Discount on advances / Bills	xx	xx
2.	Interest on Investment	xx	xx
3.	Interest on balance with RBI	xx	xx
4.	Others	xx	xx
	Total	xx	xx

Schedule 14 Other Income

		Year ended 31-03- Current year	Year ended 31-03---- Previous year
1.	Commission, Exchange & brokerage	xx	xx
2.	Profit on sale of Investments **Less**: Loss on sale of Investments	xx	xx
3.	Profit on revaluation of investment **Less:** Loss on revaluation of Investments	xx	xx
4.	Profit on sale of land, Building and other assets **Less:** Loss on sale of land, Building and Other assets.	xx xx	xx xx
5.	Profit on exchange transaction **Less:** Loss on exchange transaction	xx xx	xx xx
6.	Income earned by way of dividend	xx	xx
7.	Miscellaneous Income	xx	xx
	Total	xx	xx

Schedule 15 Interest Expended

S.No.		Year ended 31-03 Current year	Year ended 31-03- Previous year
1.	Interest on deposits	xx	xx
2.	Interest on RBI/Inter Bank Borrowings	xx	xx
3.	Others	xx	xx
	Total	xx	xx

Schedule –16 Operating Expenses

SNo.		Year ended 31-03 Current year	Year ended 31-03- Previous year
1)	Payments to and provision for employees	xx	xx
2)	Rent, taxes and lighting	xx	xx
3)	Printing & Stationery	xx	xx
4)	Advertisements	xx	xx
5)	Depreciation on Bank Property	xx	xx
6)	Director fees, allowances & expenses	xx	xx
7)	Auditor fees, allowances & expenses	xx	xx
8)	Law charges	xx	xx
9)	Postage, Telegrams & Telephone	xx	xx
10)	Repairs & Maintenance	xx	xx
11)	Insurance	xx	xx
12)	Other expenditure	xx	xx
	Total	xx	xx

Problem No.1

Prepare the profit & Loss a/c for the year ended 31-03-2022 of SBI bank from the following particulars

Particulars	Rs.	Particulars	Rs.
Interest on loan	250	Discount on Bills discounted	40
Interest on savings a/c	150	Rent, taxes, insurance	5
Interest on cash credit	160	Commission, exchange and brokerage	15
Interest on fixed deposit	190		
Interest on Overdraft	70	Audit fees	10
Payment to Employees	150	Director's fees	20

Solution:

SBI Bank Ltd

Profit and Loss account for the year ended 31-03-2022

S.No.	Particulars	Schedule No	Year ended 31-03-22 (Rs.000)	Year ended 31-03-21 (Rs.000)
I	**Income** Interest Earned Other income	 13 14	 520 15	 -- --
	Total		535	
II	**Expenditure** Interest expended Operating expenses	 15 16	 340 185	 -- --
	Total		525	
III	**Profit/Loss** Net profit for the year(I-II) Profit brought forward		 10 --	 -- --
	Total		10	---
IV	**Appropriation** Transfer to statutory reserve10x25/100 Transfer to other reserve Transfer to Govt./Proposed Dividend Balance carried over to balance sheet		 2.5 -- -- 7.5	 -- -- --
	Total		10	--

Working Notes:

Schedule 13–Interest earned

	(Rs.'000)
Interest on Loans	250
Interest on overdraft	70
Interest on cash credit	160
Discount on bills discounted	40

	520

Schedule14 - Other Income

	(Rs.'000)
Commission, exchange and brokerage	15

Total	15

Schedule15 - Interest expended (Rs.'000)

Interest on savings account	150
Interest on fixed Deposit	190

	340

Schedule-16 Operating expenses

	(Rs.'000)
Payment to employees	150
Rent, taxes & insurance	5
Audit fee	10
Director's fee	20

	185

Problem No.2

From the following particulars, Prepare the profit & Loss a/c of Dena bank ltd., for the year ending 31.03.2020.

Particulars	Rs.	Particulars	Rs.
Interest on deposits	3,200	Discount on bills discounted	1,490
Commission (Cr)	100	Interest on overdrafts	1,600
Interest on loans	2,490	Interest on cash credits	2,320
Sundry charges (Dr)	100	Auditor's fees	35
Rent and Taxes	200	Directors fees	16
Establishment	500	Bad debts written off	300

Solution:

Dena Bank Ltd

Profit and Loss account for the year ended 31-03-2020

S.No.	Particulars	Schedule No	Year ended 31-03-22 (Rs.000)	Year ended 31-03-21 (Rs.000)
I	**Income** Interest Earned Other income	 13 14	 7,900 100	 -- --
	Total		8,000	
II	**Expenditure** Interest expended Operating expenses	 15 16	 3,200 1,151	 -- --
	Total		4,351	
III	**Profit/Loss** Net profit for the year (I-II) Profit brought forward		 3,649 --	 -- --
	Total		3,649	---
IV	**Appropriation** Transfer to statutory Reserve 3,649x25/100 Transfer to otherReserve Transfer to Govt/Proposed Dividend Balance carried over to balance sheet		 912.30 -- -- 2,736.70	 -- -- --
	Total		3,649	--

WorkingNotes:

Schedule13–Interestearned

	(Rs.'000)
Interest on Loans	2,490
Interest on overdraft	1,600
Interest on cash credit	2,320
Discount on bills discounted	1,490

	7,900

Schedule 14- Other Income

	(Rs.'000)
Commission	100
Total	100

Schedule 15-Interest expended

	(Rs.'000)
Interest on deposits	3,200
	3,200

Schedule 16 Operating expenses

	(Rs.'000)
Sundry charges (Dr)	100
Rent, taxes & insurance	200
Establishment	500
Audit fees	35
Director's fees	16
Bad debts to be written off	300
	1,151

Specimen Form of Balance sheet

Balance sheet of.......................... (nameoftheBank)as on 31st March 20..............

(Rs.000)

	Schedule No.	**As on 31-03-…. Current year**	**As on 31-03-.... Previous year**
Capital & Liabilities:			
Capital	1	xx	xx
Reserves & Surplus	2	xx	xx
Deposits	3	xx	xx
Borrowings	4	xx	xx
Other Liabilities & Provisions	5	xx	xx
Total		xx	xx
Assets			
Cash and balance with Reserve Bank of India	6	xx	xx
Balance with banks and money at call and short notice	7	xx	xx
Investments	8	xx	xx
Advances	9	xx	xx
Fixed assets	10	xx	xx
Other assets	11	xx	xx
Total		xx	xx
Contingent Liabilities Bills for collection	12	xx	xx

Schedule –1 Capital

Schedule 1 Capital	**Current year**	**Previous year**
I. For Nationalized Banks Capital (fully owned by central Government)	xx	xx
II. For Banks incorporate outside India	xx	xx
III. For other Banks		
Authorized capital	xx	xx
Issued capital	xx	xx
Subscribed capital	xx	xx
Called up capital	xx	xx
Less: Calls unpaid	xx	xx
Add: Forfeited shares	xx	xx

Schedule 2 – Reserves & Surplus

	Current year	**Previous year**
I. <u>Statutory Reserves</u>		
Opening balance	xx	xx
Additions during the year	xx	xx
Deductions during the year	xx	xx
II. <u>Capital Reserves</u>		
Opening Balance	xx	xx
Additions during the year	xx	xx
Deductions during the year	xx	xx
III. <u>Securities premium</u>		
Opening Balance	xx	xx
Additions during the year	xx	xx
Deductions during the year	xx	xx

IV.	**<u>Revenues and other reserves</u>** Opening Balance Additions during the year Deductions during the year	xx xx xx	xx xx xx
V.	Balance in Profit & Loss account Total(I,II,III,IV,V)	xx	xx

Schedule –3 Deposits

		Current year	**Previous year**
I.	Demand Deposits From Banks From Others	 xx xx	 xx xx
II.	Savings Bank Deposits	xx	xx
III.	Terms Deposits From Banks From Others	 xx xx	 xx xx
	Total(I,II,III)	xx	xx
	B.I)Deposits of branches in India	xx	xx
	ii)Deposits of branches outside India	xx	xx

Schedule - 4 Borrowings

		Current year	Previous year
I.	**Borrowings in India**	xx	xx
	Borrowings in RBI	xx	xx
	Other banks	xx	xx
	Other Institutional Agencies	xx	xx
II.	Borrowings Outside India		
	Total(I,II,III,IV)	xx	xx

Schedule -5 Other Liabilities and Provisions

		Current year	Previous year
III.	Bills Payable	xx	xx
IV.	Inter–Office adjustment(Net)	xx	xx
V.	Interest accrued	xx	xx
VI.	Others	xx	xx
	Total(I,II,III,IV)	xx	xx

Schedule–6 Cash and Balance with Reserve Bank of India

		Current year	Previous year
I.	Cash in hand	xx	xx
II.	(including foreign exchange notes)	xx	xx
II.	Balance with Reserve Bank of India		
	1. In current accounts	xx	xx
	2. In other accounts	xx	xx
	Total(I,II)	xx	xx

Schedule–7 Balance with Banks & Money at call and short notice

I. In India

		Current year	Previous year
i)	Balance with banks		
	a) In current accounts	xx	xx
	b) In other deposit account	xx	xx
ii)	Money at call & short notice		
	a) With banks	xx	xx
	b) With other institutions	xx	xx
	Total(i&ii)	xx	xx

II. Outside India

		Current year	Previous year
i)	In current accounts	xx	xx
ii)	In other Deposit accounts	xx	xx
iii)	Money at call and short notice	xx	xx
	Total(i,ii, iii)	xx	xx
	GrandTotal (I,II)	xx	xx

Schedule8–Investments

I. Investments in India

		Current year	Previous year
i)	Government securities	xx	xx
ii)	Other approved securities	xx	xx
iii)	Shares	xx	xx
iv)	Debentures and Bonds	xx	xx
v)	Subsidiaries/Joint ventures	xx	xx
vi)	Others	xx	xx
	Total	xx	xx

II Investments outside India

		Current year	Previous year
i)	Government securities	xx	xx
ii)	Subsidiaries/Joint ventures	xx	xx
iii)	Other investments	xx	xx
	Total	xx	xx
	Grand Total (I and II)	xx	xx

Schedule 9 Advances

	Current year	Previous year
A) i)Bills purchased and discounted ii) Cash credit, overdraft and Loans repayable on demand. iii) Term loans	xx xx xx	xx xx xx
Total	xx	xx
B) i) Secured by Tangible assets ii) Covered by Bank / Govt. guarantees. iii) Unsecured	xx xx xx	xx xx xx
Total	xx	xx
C)Advances in India i) Priority Sectors ii) Public sectors iii) Banks iv) Others	 xx xx xx xx	 xx xx xx xx
Total	xx	xx
II. Advances outside India		
i) Due from Banks ii) Due from others a) Bills purchased and discounted b) Syndicated Loans c) Others	xx xx xx xx xx	xx xx xx xx xx
Total	xx	xx
Grand Total (C I and II)	xx	xx

Schedule 10–Fixed Assets

	Current year	Previous year
I.Premises		
Opening Balance	xx	xx
Additions during the year	xx	xx
Deductions during the year	xx	xx
Depreciation to date	xx	xx
II. Other Fixed Assets		
Opening Balance	xx	xx
Additions during the year	xx	xx
Deductions during the year	xx	xx
Depreciation to date	xx	xx
Total	xx	xx

Schedule 11 Other assets

	Current year	Previous year
I. Inter office adjustments (net)	xx	xx
II. Interest accrued	xx	xx
III. Tax paid in advance / tax deducted at source	xx	xx
IV. Stationery and stamps	xx	xx
V. Non–banking assets acquired in satisfaction of claims	xx	xx
VI. Others	xx	xx
Total	xx	xx

Schedule 12 Contingent Liabilities

	Current year	Previous year
I. Claims against the bank acknowledged as debt	xx	xx
II. Liability for partly paid Investment	xx	xx
III. Liability on account of outstanding forward exchange contracts	xx	xx
IV. Guarantee given on behalf of constituents	xx	xx
a) India	xx	xx
b) Outside India.	xx	xx
V. Acceptance, Endorsements and other obligations	xx	xx
VI. Other items for which the bank is Contingently liable	xx	xx
Total(I,II,III,IVV,VI)	xx	xx

Problem No.3

From the following particulars of Lakshmi Bank Ltd. Prepare a Balance sheet as on 31-03-2017

	(Rs.in '000)
Authorised capital	10,000
Subscribed capital	9,000
Investments	7,000
Bills discounted	15,000
Profit & Loss a/c(Cr)	850
Endorsement on bills for collection	100
Money at call and short notice	11,000

Cash in hand	4,000
Liability for customers for acceptances	5,000
Cash with RBI	6,000
Statutory Reserve	4,000
Cash with State Bank of India	4,000
Letters of credit issued	500
Telegraphic transfer payable	800
Bank draft payable	1,200
Short loans	40
Rebate on bills discounted	10
Acceptance for customers	5,000
Loans and advances	12,000
Cash credit	10,000
Overdraft	1,000
Bills purchased	1,000
Current and deposit accounts	60,000
Investment fluctuation fund	100
Bills for collection	100
Buildings	5,000

Solution:

Schedule 1 Share capital

Subscribed capital 9,000

Schedule 2 Reserves & Surplus

Profit & Loss a/c 850

Statutory reserve 4,000

Investment

Fluctuation fund 100

4,950

- - - - -

Schedule 3 Deposits

Current Deposit A /c's	60,000

Schedule 4 Borrowings

Short Loan	40

Schedule 5 Other liabilities

Telegraphic Transfer	800
Bank draft payable	1,200
Rebate in bills discounted	10

	2,010

Schedule 6 Cash balance with RBI

Cash in hand	4,000
Cash with RBI	6,000

	10,000

Schedule 7 Money at call & short notice

Money at call and short notice	11,000
Cash with State Bank of India	4,000

	15,000

Schedule 8 Investment

Investment	7,000

Schedule 9 Advances

Bills discounted	15,000
Loans & advances	12,000
Cash credit	10,000
Overdraft	1,000
Bills purchased	1,000

	39,000

Schedule 10 Fixed Assets

Building	5,000

Schedule 11 Other Assets

NIL

Schedule 12 Contingent Liabilities

Endorsement for bill	-	100
Liability for customers	-	5,000
Letter of credit issued	-	500

		5,600

Note: Acceptance for customer is not a liability hence it will not be taken into account.

Balance sheet of Lakshmi Bank Ltd for the year ended 31-03-2017

I. Capital and Liabilities	Schedule	As on 31-03-2017
Share capital	1	9,000
Reserves and surplus	2	4,950
Deposits	3	60,000
Borrowing (Shortterm)	4	40
Other liabilities and provision	5	2,010
Total		76,000
II. Assets		
Cash in hand	6	10,000
Moneyat calland short notice	7	15,000
Investment	8	7,000
Advances	9	39,000
Fixed assets	10	5,000
Other assets	11	NIL
Total		76,000
Contingent Liabilities	12	5,600

Problem No.4
Calculate Rebate on Bills discounted as on 31-03-2018

Bill Date	Amount	Period	Rate of Discount
15-01-2018	25,000	5 Months	8%
10-02-2018	15,000	4 Months	7%
25-02-2018	20,000	4 Months	7%
20-03-2018	30,000	3 Months	9%

Solution:

Calculation of Rebate on Bills discounted

Bill Date	Amount	Due Date	No.of days	Rate	Amount
15-01-2018	25,000	18-06-18	79	8%	433
10-02-2018	15,000	13-06-18	74	7%	213
25-02-2018	20,000	28-06-18	89	7%	341
20-03-2018	30,000	23-06-18	84	9%	621
	Rebate on Bills discounted Amount				1,608

Note: add 3 days as grace entry:

Problem No.5

On 31st March, 2020 Indus Bank Ltd had the following unmeasured Bills.

Date of Bill	Amount	Term Months	Discount(pa)
12-01-2017	30,000	6	12%
07-02-2017	70,000	4	11%
02-03-2017	20,000	3	10%

Calculate the Rebate on Bills discounted and record necessary entry on 31st March 2017.

Solution:

Calculation of Rebate on Bills Discounted

Dateof Bill	Due date	No.of days after 31st March	Amount	Rebate on Bill
12-01-2017	15-07-2017	106	30,000	1045.48
07-02-2017	10-06-2017	71	70,000	1497.81
02-03-2017	15-06-2017	66	20,000	361.44
			Total	2904.73

Entry:

Discount a/c Dr 2904.73

To Rebate on Bills discounted a/c 2904.73

Problem No.6

On 31st March 2020, South India Bank Ltd., finds its advances classified as follows:

		Rs.
Standard assets		14,91,300
Sub – Standard assets		92,800
Doubtful assets (secured)		
	Doubtful for one year	25,660
	Doubtful for one year to 3 years	15,640
	Doubtful for more than 3 years	6,580
Loss assets		10,350

Calculate the amount of provisions to be made by the bank against the above mentioned advances.

Solution:

Particulars	**Amount (Rs.)**	**% required as provision**	**Provision (Rs.)**
Standard assets	14,91,300	0.25	3,728
Sub – Standard assets	92,800	10	9,280
Doubtful assets (secured)			
Doubtful for one year	25,660	20	5,132
Doubtful for one year to 3 years	15,640	30	4,692
Doubtful for more than 3 years	6,580	50	3,290
Loss assets	10,350	100	10,350
Total provision required			36,472

Problem No.7

While closing its books of accounts, a commercial bank has its advances classified as follows:

		Rs.
Standard assets		16,000
Sub – Standard assets		1,300
Doubtful assets (secured)		
	Doubtful for one year	700
	Doubtful for one year to 3 years	400
	Doubtful for more than 3 years	200
Loss assets		500

You are required to calculate the amount of provisions to be made by the bank against the above mentioned advances.

Solution:

Particulars	Amount (Rs.)	% required as provision	Provision (Rs.)
Standard assets	16,000	0.25	40
Sub – Standard assets	1,300	10	130
Doubtful assets (secured)			
Doubtful for one year	700	20	140
Doubtful for one year to 3 years	400	30	120
Doubtful for more than 3 years	200	50	100
Loss assets	500	100	500
Total provision required			1,030

Problem No.8

While closing its books of accounts, a commercial bank has its advances classified as follows:

	Rs.
Standard assets	48,000
Sub – Standard assets	2,400
Doubtful assets (unsecured)	
Doubtful for one year	1,600
Doubtful for one year to 3 years	1,200
Doubtful for more than 3 years	800
Loss assets	1,800

You are required to calculate the amount of provisions to be made by the bank against the above mentioned advances.

Solution:

Particulars	Amount (Rs.)	% required as provision	Provision (Rs.)
Standard assets	48,000	0.25	120
Sub – Standard assets	2,400	10	240
Doubtful assets (secured)			
Doubtful for one year	1,600	100	1,600
Doubtful for one year to 3 years	1,200	100	1,200
Doubtful for more than 3 years	800	100	800
Loss assets	1,800	100	1,800
Total provision required			5,760

Unit - IV
Accounts of Insurance Companies

Insurance - Meaning

Insurance is a contract whereby insurers agree to compensate for specific loss to the insured, who in consideration, agrees to pay regularly a sum of money called premium. The insurance company agrees to pay compensation is known as insurer and the person who is taking policy from the insurance company is known as policy holder or insured.

Definition of Insurance

"Insurance is a contract in which a sum of money is paid to the insured in consideration of insurers incurring the risk of paying a large sum upon a given contingency"–Justice Tindle.

Kinds of Insurance:

There are three types of Insurance

1. Life Insurance
2. General Insurance
3. Social Insurance

1. Life Insurance:

It is a contract between the insured and the Insurance Company in which the insurance company agrees to pay the policy amount on the death of the insured or maturity of policy whichever is earlier .Hence the policy holder agrees to pay amount is called premium.

The following are the main varieties of life insurance policies

i) Whole life policy

ii) Endowment policy

iii) With profit policy

iv) Without profit policy

v) Annuity policy

2. **General Insurance:** All insurance contracts other than Life insurance are known as General insurance. Example: Fire Insurance, Marine Insurance, Liability insurance, Motor vehicle, Theft, Fidelity and Accident insurance. It is governed by General Insurance Act 1972.

3. **Social Insurance**

   It is to provide protection to the weaker section of the society who are unable to pay the premium for adequate insurance. Example: Pension plans, Disability benefits, sickness insurance and industrial insurance.

Difference between Life Insurance and General Insurance

	Life Insurance	**General Insurance**
1)	It is a contract of certainty	It is a contract of Indemnity.
2)	It is a long term Contract	It is one year contract
3)	It is governed by LIC Act	It is Governed by GIC Act
4)	Life policy can be assigned to others	It cannot be assigned to others
5)	It comprises of Investment and Protection	It consists of only protection
6)	Insurable Interest must exist at the time of proposal.	It must exist from the date of Proposal to the end of contract.
7)	Surrender value is possible	No surrender value
8)	Policy amount will be received in the event of death or maturity date Whichever is earlier.	Policy amount will be received in the event of risk or loss occurred.

Final Accounts of life Insurance companies

1) Revenue account
2) Profit & loss account
3) Balance sheet

Specimen form of Revenue account of LIC for the year ended 31-03-20.....

Policyholders account particulars	Schedule No	Current Year (Rs.000)	Previous Year (Rs.000)
Premium earned(Net)	1		
a) Premium		xx	
b) Reinsurance ceded		xx	
c) Reinsurance accepted.		xx	
Income from Investments:			
a) Interest, Dividends & Rent- Gross		xx	
b) Profit on sale/redemption of Investments		xx	
c) Loss on sale/redemption of Investments			
d)Transfer/Gain on revaluation/change in		xx	
Fair value other Income			
		xx	
Total (A)		xx	xx

Policy holders account particulars	Schedule No	Current year (Rs.000)	Previous year (Rs.000)
Commission	2	xx	xx
Operating Expenses	3	xx	xx
Provision for doubtful debts		xx	xx
Bad debts written off		xx	xx
Provision of Tax		xx	xx
Provision (other than taxation)			
a) For diminution The value of		xx	xx
Investments (Net)		xx	xx
b) Others		xx	xx
Total B		xx	xx
Benefits paid(Net)	4	xx	xx

Interim Bonus paid change in valuation of liability of life policies a) Gross b) Amount ceded in Reinsurance c) Amount accepted in reinsurance		xx xx xx xx xx	xx xx xx xx xx
Total C		xx	xx
Surplus(or)Deficit(D)=(A-B-C)		xx	xx
Appropriations Transfer to shareholders account Transfer to other Reserve Balance being fund for future Appropriations	xx xx xx	xx xx xx	xx xx xx
Total D	xx	xx	xx

Specimen form

Form– A-PL

Profit & Loss account for the year ended 31st March 2017 shareholders account (Non-Technical Account)

Particulars	Schedule	Current Year (Rs.000)	Previous Year (Rs.000)
Amount transferred from / to policy holders account		xx	xx
Income from Investments		xx	xx
a) Interest , Dividend & rent gross		xx	xx
b) Profit on sale/redemption of Investments			
c) Loss on sale/redemption of Investments		xx	xx
Other Income			
		xx	xx
Total(A)		--------	----------
		xx	xx
		------	--------

Expenses other than those directly related to Insurance business			
Bad debts written off	xx	xx	xx
Provisions (other than taxation)	xx	xx	xx
a) For diminution in the value of Investments (Net)			
b) Provisions for doubtful debts	xx	xx	xx
c) Others	xx	xx	xx
Total(B)	xx	xx	xx
Profit/Loss before Tax	xx	xx	xx
Provision for taxation	xx	xx	xx
Profit/Loss after tax	xx	xx	xx
Appropriation			
a) Balance at the beginning of the year	xx	xx	xx
b) Interim Dividend paid during the year	xx	xx	xx
c) Proposed final Dividend	xx	xx	xx
d) Dividend Distribution tax	xx	xx	xx
e) Transfer to reserve/Other accounts	xx	xx	xx
Profit carried …. To the Balance sheet	xx	xx	xx

Specimen form Life Insurance Balance sheet

Form A-Bs

Balance sheet as on 31st March 20...........

Particulars	Schedule	Current Year	Previous Year
Sources of Funds			
Shareholders funds			
Share capital	5		
Reserves &surplus	6		
Credit/Debit fair value Change account			
SubTotal			
Borrowings	7		
Policy holders funds			
Credit/Debit fair value Change account			
Policy Liabilities			
Insurance Reserves			
Provision for linked Liabilities			
Sub total			
Funds for future Appropriations			

Application of funds

Particulars	Schedule	Current Year	Previous Year
Application of funds			
Investments			
Shareholders	8		
Policyholders	8A		
Assets held to cover linked Liabilities	8B		
Loans	9		
Fixed Assets	10		
Current Assets(A)			
Cash and Bank	11		
Balances Advance and other Assets	12		
Sub total (A)			
Current Liabilities (B)	13		
Provisions	14		
Sub Total(B)			
Net current Assets C=A-B			
Miscellaneous Expenditure	15		
Debit balance in profit & Loss Account (shareholders account)			
Total (Application of funds + New current assets)			

Schedule forming part of financial statements

Schedule – 1 Premium

S.No.		Current year	Previous year
1.	First year Premiums	xx	xx
2.	Renewal Premiums	xx	xx
3.	Single premium	xx	xx
	Total Premiums	xx	xx

Schedule – 2 Commission Expenses

S.No.		Current year	Previous year
1.	Commission paid	xx	xx
	Direct–First year premiums	xx	xx
	Renewal premiums	xx	xx
	Single Premiums	xx	xx
	Add: Commission on reinsurance Accepted	xx	xx
	Less: Commission on reinsurance ceded	xx	xx
	Net Commission	xx	xx

Schedule -3 Operating Expenses related to Insurance Business

S.No.		Current year	Previous year
1.	Employees remuneration & welfare benefits	xx	xx
2.	Travel expenses	xx	xx
3.	Training Expenses	xx	xx
4.	Rent & Rates	xx	xx
5.	Repairs	xx	xx
6.	Printing and stationery	xx	xx
7.	Legal charges	xx	xx
8.	Medical fees	xx	xx
9.	Auditor fees	xx	xx
10.	Advertisement	xx	xx

11.	Interest charges	xx	xx
12.	Depreciation	xx	xx
	Total	xx	xx

Schedule– 4 Benefits paid (Net)

S.No.		Current year	Previous year
1.	**Insurance claim**		
	a) Claims by Death	xx	xx
	b) Claims by Maturity	xx	xx
	c) Annuities	xx	xx
	d) Other benefits	xx	xx
2.	**Amount ceded in Reinsurance**		
	a) Claim by Death	xx	xx
	b) Claim by Maturity	xx	xx
	c) Annuities	xx	xx
	d) Other benefits	xx	xx
3.	**Amount accepted in reinsurance**		
	a) Claim by Death	xx	xx
	b) Claim by Maturity	xx	xx
	c) Annuities	xx	xx
	d) Other benefits	xx	xx
	Total	**xx**	**xx**

Schedule - 5 Share Capital

Particulars		Current Year	Previous Year
Authorised Capital			
Issued Capital			
Subscribed Capital			
Called up Capital			
(-)Calls Unpaid			
(+)Share forfeited			
(-)Preliminary Expenses			
	Total		

Schedule– 6 Reserves and Surplus

Particulars	Current Year	Previous Year
Capital Reserve Capital Redemption Reserve Share Premium General Reserve Balance of Profit in profit & loss a/c		
Total		

Schedule –7 Borrowings

Particulars	Current Year	Previous Year
Debentures Banks Financial institutions Others		

Schedule –8 Investments

Particulars	Current Year	Previous Year
Long term Investments Short term Investments		

Schedule–9 Loans

Particulars	Current Year	Previous Year
1.Security wise classification: a) Secured b) Unsecured		
Total		
2.Borrower wise classification: a) Central & State Govt. b) Banks & Financial Institutions c) Others		
Total		
3.Performance wise classification: a) Loan classified as standard b) Non standard Loans Less provisions		
Total		
4. Maturity wise classification: a) Short term b) Long term		
Total		

Schedule – 10 Fixed assets (Rs.000)

Particulars	Cost /GrossBlock				Depreciation			As at year end	NetBlock	
	Opening	Additions	Deductions	Closing	Upto Last Year	For the year	On Sales/ Adjustment		As at year end	Previous year
Goodwill Intangibles Freehold Land Leasehold property Buildings Furniture Information Technology Equipment Vehicles Office Equipment										
Total										
Work inprogress										
GrandTotal										
PreviousYear										

Schedule -11 Cash and Bank Balances

Particulars	Current Year	Previous Year
1.Cash 2. Bank Balance a) Deposit A\c b) Current A\c Others 3. Money at call & short notice 4. Others		
Total		

Schedule – 12 Advances and other Assets

Particulars	Current Year	Previous Year
<u>Advances</u> 1.Reserve Deposits with ceding companies 2.Application money for Investments 3.Prepayments 4.Advances to Directors 5.Others		
Total (A)		

Other Assets 1.Income accrued on Investments 2.Outstanding Premium 3.Agents Balance 4.Foreign Agencies Balances 5.Deposits with RBI Total(B) Grand Total(A+B)		

Schedule -13 Current Liabilities

Particulars	Current Year	Previous Year
1.Agents Balances 2.Balance due to other Insurance Companies 3.Deposits held on reinsurance ceded 4.Premium received in advance 5. Unallocated Premium 6. Sundry creditors 7.Claimsoutstanding Total		

Schedule -14 Provisions

Particulars		Current Year	Previous Year
Reserve for unexpired Risk			
For taxation			
For proposed dividends			
For dividend distribution tax			
Others			
	Total		

Schedule -15–Miscellaneous Expenditure

Particulars	Current Year	Previous Year
Discount allowed in issue to shares/ debentures Others		
Total		

Some Important Terms:

1) Claims:

When the insured makes a statement for the loss on the date of happening of an event or on the date of maturity of the policy to the insurer the statement is known as claims.

2) Premium:

It means the consideration received by Insurance Company in Consideration of the risk undertaken by it. It should be shown in revenue account.

3) **Bonus**:

It is a share of profit which a policy holder gets from the LIC.

4) **Reinsurance**:

It means transferring the whole or a part of the risk undertaken by insurer to another Insurer.

5) Commission on Reinsurance ceded:

It is a gain to the insurance company. Insurance Companies earn commission from other insurance companies for giving them business under Reinsurance contract.

6) Commission on Reinsurance Accepted:

It is an expense to the Insurance Company. Insurance Companies paid commission to other insurance companies for giving them business under Reinsurance contract.

Reserve for unexpired Risk:

It is a reserve created to meet the risk which is associated with all such policies. In fire Insurance 50% net premium is transferred and in marine Insurance 100% of Net Premium is too transferred to Reserve for unexpired Risk.

Problem No.1

The life assurance fund of SBI life assurance company ltd. Shows a balance of Rs.9,00,000 on 31.03.2021. It was later observed that the following had not been taken into account**.**

i) Bonus utilized in reduction on premium Rs.90,000
ii) Outstanding premium Rs.2,00,000
iii) Interest accrued on investments less income tax Rs.50,000
iv) Claim intimated but not yet admitted Rs.30,000
v) Claims covered under reinsurance Rs.10,000

Compute the balance of Life Assurance Fund.

Statement Showing Life Insurance Fund

Particulars	**Rs.**	**Rs.**
Life assurance fund as on 31.03.2021		9,00,000
Add:		
Bonus utilized in reduction of premium	90,000	
Outstanding premium	2,00,000	
Interest accrued on investment less income tax	50,000	
Claims covered under reinsurance	10,000	3,50,000
	------------	------------
Less:		12,50,000
Bonus utilized in reduction of premium	90,000	
Claims intimated but not yet admitted	30,000	1,20,000
	-------------	--------------
Life Assurance Fund		11,30,000
		========

Problem No.2

A life assurance company prepared its Revenue A/c for the year ended 31.03.2018 and ascertained its Life Assurance fund to be Rs.30,00,000. It was found later that the following had been omitted from the accounts:

i) Bonus utilized in reduction on premium Rs.6,700
ii) Outstanding premium Rs.33,300
iii) Interest accrued on investments less income tax Rs.40,000
iv) Claim intimated but not admitted Rs.17,500
v) Claims covered under reinsurance Rs.9,500

What is the true Life Assurance Fund?

Statement Showing Life Insurance Fund

Particulars	Rs.	Rs.
Life assurance fund as on 31.03.2018		30,00,000
Add:		
Bonus utilized in reduction of premium	6,700	
Outstanding premium	33,300	
Interest accrued on investment less income tax	40,000	
Claims covered under reinsurance	9,500	8,95,000
	------------	------------
		38,95,000
Less:		
Bonus utilized in reduction of premium	6,700	
Claims intimated but not admitted	17,500	24,200
	-------------	--------------
Life Assurance Fund		38,70,800
		========

Problem No.3

From the following, you are required to calculate the loss on account of claims to be shown in the Revenue Account for the year ending 31.03.2016.

Intimated in	Admitted in	Paid in	Rs.
2014 – 2015	2014 - 2015	2015 - 2016	45,000
2015 – 2016	2015 -2016	2016 - 2017	30,000
2013 – 2014	2014 - 2015	2014 - 2015	15,000
2013 – 2014	2014 - 2015	2015 - 2016	36,000
2015 – 2016	2016 – 2017	2016 - 2017	24,000
2015 – 2016	2015 - 2016	2015 - 2016	3,10,000

Claim on account of reinsurance was Rs.80,000.

Calculation of Claim incurred

Particulars	Rs.	Rs.
Total claim paid in 2015 – 2016 (45,000+36,000+3,10,000)		3,91,000
Less: Claims outstanding at the beginning of 2015-2016		
Intimated in 2014-2015 and paid in 2015-2016	45,000	
Intimated in 2013-2014 and paid in 2015-2016	36,000	81,000
	------------	-----------
Add: Claims outstanding at the end of 2015-2016		3,10,000
Intimated in 2015-2016 and paid 2016-2017	30,000	
Intimated in 2015-2016 and paid in 2016-2017	24,000	54,000
	-------------	------------
		3,64,000
Less: Reinsurance claim		80,000

Claims paid and outstanding in 2015-2016 to be shown in the revenue account		2,84,000 =======

ProblemNo.4

The following were the balances extracted from the trial Balance of Bajaj Life insurance company ltd for the year 31st March 2019.

Balance of account at the beginning of the year	Rs.8,00,000
Profit on realization of assets	Rs.1,000
Claims under policies by death	Rs.30,000
Claims under polices by Maturity	Rs.50,000
Premium (Other than single)	Rs.1,00,000
Single Premiums	Rs.40,000
Consideration for annuities granted	Rs.25,000
Interest Received	Rs.35,000
Depreciation on furniture	Rs.1,500
Administrative Expenses	Rs.18,000
Salaries	Rs.1,500

Surrenders	Rs.10,000
Auditor’s fee	Rs. 750
Legal Expenses	Rs. 500
Advertising	Rs.700
Printing	Rs.5,400
Director’s fee	Rs.150
Commission paid	Rs.12,000

Solution: **Bajaj Insurance Co., Ltd**

Revenue account for the year ended 31-03-2019.

	Schedule No	**31-03-2019**
Premium Earned– Net	1	1,40,000
Income from Investment		35,000
Interest, Dividend		1,000
Transfer/gain on revaluation		
Other income– consideration for annuities		25,000
Granted		------------
Total(A)		2,01,000

Commission		12,000
Operating Expenses	2	28,500
	3	-----------
Total(B)		40,500

Benefits paid(Net)	4	90,000
Interim Bonus paid		--

Total(c)		90,000
Surplus (P)=A-B-C		70,500
Appropriations		-------------
Balance being funds for future		
Appropriations		**70,500**

Workings:

Schedule 1 Premium Earned (Net)	31-03-19
Premium (other than single)	1,00,000
Single Premium	40,000
Total	1,40,000
	=========

Schedule 2 Commission Expenses

Commission paid	12,000

	12,000
	======

Schedule 3 Operating Expenses

Administrative Expenses	18,000
Salaries	1,500
Auditor’s fee	750
Director’s fee	150
Legal Expenses	500
Advertising	700
Printing	5,400
Depreciation on furniture	1,500

Total	28,500

Schedule –4 Benefits paid (Net)

Claims under policies by death	30,000
Claims under policies by Maturity	50,000
Surrenders	10,000

Total	90,000
	- - - - - -

Ascertainment of Profit

In Life Insurance business, profit is to be ascertained after expiry of 2 years for this purpose a valuation Balance sheet is prepared.

Valuation Balance sheet as on..............

Particulars	Rs.	Particulars	Rs.
To Net liability as per actuarial valuation	xxx	By Life assurance fund as Balance sheet	xxx
To Surplus if any (Bal.Fig)	xxx	Deficiency if any (Bal.Fig)	xxx
	xxx		xxx

Distribution statement Amount payable to policy holders

Surplus as per valuation Balance sheet	xx
Add: Interim Bonus	xx
Policy shareholders 95%	xx
Less: Interim Bonus paid	xx
Amount due to policyholders for bonus	xx

Problem No.5

From the following information, calculate surplus or deficit of a Life Insurance Business for the year ended 31st March 2020.

Balance of Life Assurance Fund on 31.03.2020 Rs.80,00,000. Net liabilities on 31.03.2020 Rs.67,00,000.

Solution

Life Insurance Company

Valuation Balance sheet as on 31-03-2017

Liabilities	Rs.	Assets	Rs.
To Net Liabilities	67,00,000	By Life Assurance fund	80,00,000
To Surplus	13,00,000		
	80,00,000		80,00,000

General Insurance Business

Form B –RA

Specimen form Revenue Account for the year ended 31-03..............

S.No.	Particulars	Schedule	Current Year	Previous Year
1. 2. 3. 4.	Premium earned (Net) Profit/Loss on sale/redemption of Investments Change in provision for unexpired risk Interest,Dividend Rent –Gross	1		
	Total (A)			
1. 2. 3.	Claim incurred (Net) Commission Operating Expenses related to Insurance Business	2 3 4		
	Total (B)			
	Operating profit/Loss from fire/marine Miscellaneous Business C=A-B **Appropriations:** Transfer to shareholders Account Transfer to catastrophe Reserve Transfer to other reserve			
	Total (C)			

Form B –PL

Profit & Loss account for the year ended 31-03.......

S.No.	**Particulars**	**Schedule**	**Current year**	**Previous years**
1.	Operating profit/loss a) Fire Insurance b) Miscellaneous Insurance			
2.	Income from Investment a) Interest, Dividend & Rent - gross b) Profit on sale of Investments.			
3.	Other Income			
	Total (A)			
4.	Provisions (Other than taxation) a) Diminution in value of Investments b) Doubtful debts c) Others			
5.	Other expenses a) Expenses not related to Insurance business b) Bad debts c) Others			
	Total(B)			
	Profit before Tax Provision for taxation Appropriations a) Interim Dividend paid b) Proposed Dividend c) Dividend Distribution tax d) Transfer to any Reserve Balance of profit/loss brought forward from last year Balance carried forward to Balance Sheet			

Form B–BS

Balance sheet as on 31^{st} March ....

Particulars	Schedule	Current Year	Previous Year
Sources of funds Share capital Reserves & Surplus Fair value change account Borrowings	 5 6 7		
Total(A)			
Application of funds Investments Loans Fixed Assets **Current Assets(A)** Cash and Bank Balances Advances and other assets	 8 9 10 11 12		
Sub Total (A)			
Current Liabilities(B) Provisions	13 14		
Sub Total (B)			
Net current Assets C=(A-B) Miscellaneous Expenditure Debit Balance in profit & loss a/c	15		
Total (Appl.of funds+NCA)			

Details of schedule

Schedule 1 Premium Earned (Net)

Particulars	Current Year	Previous Year
Premium from Direct Business **Add:** Premium on reinsurance accepted **Less:** Premium on reinsurance ceded Net premium Adjustment for change in reserve for unexpired risk Total Premium earned (Net)		

Schedule 2 Claims incurred (Net)

Particulars	Current Year	Previous Year
Claims paid Direct **Add:** Reinsurance accepted **Less:** Reinsurance ceded Net Claim Paid **Add:** Claim outstanding at the end of year **Less:** Claim outstanding at beginning Total Claims incurred		

Schedule 3 Commission

Particulars	Current Year	Previous Year
Commission Paid Direct **Add:** Reinsurance Accepted **Less:** Reinsurance ceded Net Commission		

Schedule 4 Operating Expenses related to insurance Business

Particulars	Current Year	Previous Year
Employees Remuneration and Welfare Benefits Travel Expenses Training Expenses Auditor’s fee Advertisement Interest & Bank charges Depreciation		
Total		

Schedule 5 Share capital

S.No.	Sharecapital	Current Year	Previous year
1.	Authorised capital	xx	xx
2.	Issued capital	xx	xx
3.	Subscribed capital	xx	xx
4.	Called up capital	xx	xx
	Less:Calls unpaid Add: Share forfeited Less: Preliminary Expenses	xx	xx
	Total	xx	xx

Schedule 6 Reserves and surplus

S.No.	Particulars	Current Year	Previous year
1.	Capital Reserve	xx	xx
2.	Capital Redemption Reserve	xx	xx
3.	Share Premium	xx	xx
4.	Revaluation Reserve	xx	xx
5.	General Reserve	xx	xx
6.	Balance of profit in P & L a/c	xx	xx
	Total	xx	xx

Schedule 7 Borrowings

S.No.	Borrowings	Current Year	Previous year
1.	Debentures	xx	xx
2.	Banks	xx	xx
3.	Financial Institutions	xx ----- 	xx -----
	Total	xx	xx

Schedule 8 Investments - Shareholders

S.No.	Shareholders	Current Year	Previous year
1.	Long term Investment	xx	xx
2.	Short term Investment	xx	xx
	Total	xx	xx

Schedule 8A Investments – Policyholders

S.No.	Particulars	Current Year	Previous year
1.	Long term Investments	X x	xx
2.	Short term Investments	X x	xx
	Total	X x	xx

Schedule – 8B Assets held to cover linked liabilities

S.No.	Particulars	Current Year	Previous year
1.	Long term Investments	xx	xx
2.	Short term Investments	xx	Xx
	Total	xx	xx

Schedule 9 Loans

S.No.	Particulars	Current Year	Previous year
1.	Security wise classifications Secured Unsecured Total		
2.	Borrower wise classification a) Central & state Govt. b) Banks &FinancialInstitutions c) Others		
3.	Performance wise classification a) Loan classified as standard b) Non-standard Less provisions		
	Total		
4.	Maturity– wise classification a) Short term b) Long term		
	Total		

Schedule 10 Fixed assets (Rs.000)

Particulars	Cost /GrossBlock				Depreciation			As at year end	NetBlock	
	Opening	Additions	Deductions	Closing	Upto Last Year	For the year	On Sales /Adjustment		As at year end	Previous year
Goodwill Intangibles Freehold Land Leasehold Property Buildings Furniture Information Technology Equipment Vehicles Office Equipment										
Total										
Work inprogress										
GrandTotal										
PreviousYear										

Schedule 11 Cash and Bank Balance

S.No.	Particulars	Current Year	Previous year
1.	Cash	xx	xx
2.	Bank Balances	xx	xx
3.	Money at call & short notices	xx	xx
4.	Others	xx	xx
	Total	xx	xx

Schedule 12 Advances and other Assets

S.No.	Advances	Current Year	Previous year
1.	Reserve Deposits	xx	Xx
2.	Application Money	xx	Xx
3.	Prepayments	xx	Xx
4.	Advances to Directors	xx	Xx
5.	Advance Tax Paid	xx	Xx
	Total (A)	xx	Xx

OtherAssets

S.No.	Particulars	Current Year	Previous year
1.	Income accrued on Investments	xxx	xxx
2.	Outstanding Premium	xxx	xxx
3.	Agent Balance	xxx	xxx
4.	Foreign Agencies Business	xxx	xxx
5.	Deposits with RBI	xxx	xxx
	Total(B)		
	Total(A+B)		

Schedule 13 Current Liabilities

S.No.	Particulars	Current Year	Previous year
1.	Agents Balance	xx	xx
2.	Balance due to other insurance business	xx	xx
3.	Deposits held on reinsurance ceded	xx	xx
4.	Premium received in advance	xx	xx
5.	Sundry creditors	xx	xx
6.	Claims outstanding	xx	xx
7.	Annuities Due	xx	xx
	Total	xx	xx

Schedule 14 Provisions

S.No.	Particulars	Current Year	Previous year
1.	For taxation	xx	xx
	Proposed Dividend	xx	xx
	Dividend Distribution tax	xx	xx
	Others	xx	xx
	Total	xx	xx

Schedule 15 Miscellaneous Expenditure

S.No.	Particulars	Current Year	Previous year
1.	Discount allowed on issue to shares	xx	xx
2.	Others	xx	xx
	Total	xx	xx

Fire Revenue Account

Problem No.6

From the following particulars you are required to prepare fire Revenue accountfortheyearending31March2018.

Claims outstanding 31.3.2018	2,80,000	Expenses on Management	12,68,000
Claims outstanding 1.4.2017	1,60,000		
Commission	8,00,000	Premium received	4,84,800
Claims paid	19,20,000	Commission on Reinsurance accepted	20,000
Reinsurance Premium	4,80,000		
Commission on reinsurance ceded	40,000	Provision for unexpired Risk 1.4.2017 (Fire fund)	16,80,000
Additional provision for unexpired risk	80,000		

Solution:

Fire Revenue Account for the year ending on 31.03.2018

Particulars	Schedule	Current Year
1.Premium Earned (Net)	1	43,68,000
2.Others		
3.Changes in provision for unexpired Risk (2184000–1680000)		(-)5,04,000
Total (A)		38,64,000
1.Claims incurred (Net)	2	20,40,000
2.Commission	3	7,80,000
3.Operating Expenses	4	12,68,000
4.Others		
Total (B)		40,88,000
Operating Loss (C)=(A-B)		(-) 2,24,000

Workings:

Schedule–1-Premium earned (Net)

Premium received		48,48,000
Less: Reinsurance premium		4,80,000
	Total	43,68,000

Schedule 2 Claims incurred (Net)

Claims paid	19,20,000
Add: Outstanding 31.3.18	2,80,000
	22,00,000
Less: Outstanding 1.4.17	1,60,000
Total Claims paid	7,60,000

Schedule 3 Commission

Commission	8,00,000
Add: Commission on reinsurance	20,000
	8,20,000
Less: Commission on reinsurance ceded	40,000
Total	7,80,000

Marine Revenue Account

ProblemNo.7

From the following balance of united India Insurance Company as on 31.03.2021 prepare a Marine Revenue account.

Legal charges	2,400	Communication	10,000
Commission paid	2,16,000	Printing & Stationary	24,000
Marine fund opening	16,40,000	Claims paid & Outstanding	7,60,000
Premium received	21,60,000		
Commission earned on Reinsurance ceded	1,20,000	Expenses of management	8,00,000

Solution:

Schedule 1 Premium earned (Net)

Premium received		21,60,000
	Total	21,60,000

Schedule 2 Claims incurred (Net)

Claims paid & outstanding		7,60,000
	Total	7,60,000

Schedule 3 Commission

Commission paid	2,16,000
Less: Commission earned on reinsurance ceded	1,20,000
Total	96,000

Schedule –4– Operating Expenses

Expenses of Management	8,00,000
Legal Charges	2,400
Communication	10,000
Printing & Stationary	24,000
Total	8,36,400

Marine Revenue Account for the year ended on 31-03-2021

Particulars	Schedule	Current Year
1)Premium Earned (Net)	1	21,60,000
2)Profit/loss on sale/Redemption of Investment		-
3)Change in provision of unexpired risk		(-)5,20,000
4)Interest, Dividend & Rent - Gross		-
Total (A)		16,40,000
1. Claims incurred (Net)	2	7,60,000
2. Commission	3	96,000
3. Operating Expenses Related to Insurance Business	4	8,36,400
Total (B)		16,92,400
Operating loss (C)=(A-B)		52,400

Fire and Marine Revenue account and Profit & Loss Account

Problem No.8

From the following balances of Star General Insurance company Ltd on 31.03.2020. Prepare a) Fire Revenue account b) Marine Revenue account c) Profit & Loss account.

Particulars	Rs.	Particulars	Rs.
Survey expenses (Fire)	10,000	Commission earned on re-	
Additional reserve opening (fire)	50,000	insurance ceded (marine)	60,000
Commission paid (marine)	1,08,000	Commission earned on re-	
Commission paid (fire)	90,000	insurance ceded (fire)	30,000
Claims paid and outstanding	3,80,000	Management expenses (fire)	1,45,000
(marine)	1,80,000	Management expenses (marine)	4,00,000
Claims paid and outstanding (fire)	2,50,000	Marine premium less reinsurance	10,80,000
Fire fund – opening	8,20,000	Fire premium less reinsurance	6,00,000
Marine fund – opening	1,200	Profit on sale of land	60,000
Bad debts recovered	800	Miscellaneous receipts	5,000
Share transfer fee	5,000	Differences in exchange (Cr)	300
Director's fees	1,200	Interest, dividends etc received	14,000
Auditor's fees	12,000	Depreciation	35,000
Bad debts (marine)	5,000		
Bad debts (fire)			

In addition to usual reserves, additional reserve in case of fire insurance is to be increased by 5% of Net Premium.

Solution:

Schedule 1 Premium Earned (Net)

	Fire	Marine
Premium	6,00,000	10,80,000
Total Net Premium	6,00,000	10,80,000

Schedule 2 Claims incurred (Net)

	Fire	Marine
Claim paid	1,80,000	3,80,000
Add: Survey Expenses	10,000	---
Total Claim paid	1,90,000	3,80,000

Schedule 3 Commission

	Fire	Marine
Commission – Direct	90,000	1,08,000
Less: Reinsurance ceded	30,000	60,000
Total	60,000	48,000

Schedule 4 Operating Expenses

	Fire	Marine
Managerial Remuneration	1,45,000	4,00,000
Other–Bad debts	5,000	12,000
Total	1,50,000	4,12,000

Fire Revenue Account for the year ended on 31.03.2020

Particulars	Schedule	Current Year
Premium Earned (Net)	1	6,00,000
Change in provision for unexpired risk		(-)80,000
Total (A)		5,20,000
Claims incurred (Net)	2	1,90,000
Commission	3	60,000
Operating Expenses related to Insurance Business	4	1,50,000
Total (B)		4,00,000
Operating Profit(C)=A-B		1,20,000

Workings

1) Reserve for unexpired risk(31.03.2020)

50% Net Premium	3,00,000
Add: Additional Reserve	80,000
	3,80,000

2) Change in provision for unexpired

risk Opening Balance	3,00,000
Less: Closing Balance	3,80,000
Total	80,000

Marine Revenue account for the year ended on 31.03.2020

Particulars		Schedule	Current Year
Premium Earned (Net)		1	10,80,000
Change in provision for unexpired risk			(-)2,60,000
Total (A)			8,20,000
Claims incurred (Net)		2	3,80,000
Commission		3	48,000
Operating expenses		4	4,12,000
	Total (B)		8,40,000
Operating Profit (C)= (A-B)			(-)20,000

Workings

1) Reserve for unexpired risk 10,80,000

2) **Change in provision for unexpired risk**

Opening Balance	8,20,000
Less: Closing Balance	10,80,000
Total	2,60,000

Profit & Loss account for the year ended on 31.03.2020

1) <u>Operating Profit/Loss:</u>	
a) Fire Insurance	1,20,000
b) Marine Insurance	(-)20,000
2)<u>Income from Investment:</u>	
Interest, Dividend, Rent -Gross	14,000
Profit on sale of Land	60,000
3) <u>Other Incomes:</u>	
a) Transfer fees	800
b) Bad debts recovered	1,200
c) Miscellaneous Receipts	5,000
d) Difference in Exchange	300
Total (A)	1,81,300
Other Expenses:	
1) Auditor's fees	1,200
2) Director's fees	5,000
Depreciation	35,000
	41,200
Total (B)	
Profit Before Tax (A-B)	1,40,100
Provision for taxation	----
Profit after tax	1,40,100
Appropriations:	----
Balance of profit/loss brought forward from last year	
	1,40,100

Unit – V

Double Accounting System & Accounts of Holding Companies

Double Account System

Double account is a system of accounting and presenting annual accounts by public utility undertakings like Gas companies, Electricity, Railway Companies, Tram ways which operate under special Acts of parliament. They are rendering service to the society at a reasonable price. These companies require a large amount of fixed capital invested in fixed assets.

Under Double account system the balance sheet is divided into two parts.

i) Receipts and payments on capital account.

ii) General Balance sheet

And also prepare Revenue account and Net Revenue account.

Features of Double account system:-

1. Double accounting system is a system of presenting final accounts.
2. These systems are adopted by Railways, Electricity, Gas Companies formed under special Act of parliament.
3. In this system Revenue A/c, Net Revenue A/c , Capital A/c and General Balance sheet are prepared.
4. Its main object is to show the amount of fixed capital raised from the public and the manner in which fixed capital has been used in the purchase of fixed assets.
5. A revenue account prepared to show income and expenses of the company.
6. A Net revenue A/c is prepared to show the net profit of the company.
7. Under this system fixed assets are shown in the capital a/c at original cost.
8. Discount and premium on issue of shares and Debenture is deducted from shares and debentures and Net amount is shown in capital a/c.
9. Loans and debentures are treated as capital and shown in the credit side of the capital a/c.
10. General reserve, investment fluctuation reserves are shown in the general Balance sheet on the liabilities side.

Merits (Advantages) of Double Account system:-

1) This accounting system will be easy to understand by shareholders and debenture holder's capital a/c shows the total amount of receipts by way of shares, Debentures and Loans and expenses incurred for purchasing fixed assets.

2) Creation of appreciation fund will be useful to replace fixed assets.

3) Public utility companies render better services to the public at a reasonable price.

4) Revenue and Net revenue accounts are shown pure operating results of the company.

5) It helps in preparation of various statistical returns in a quick manner.

6) It helps in comparison of floating assets and floating liabilities.

7) In this system the Government exercises necessary control over Public Utility Company.

8) Under Double accounting system fixed assets are shown as original cost under capital accounts and current assets are shown in General Balance sheet.

Demerits (Disadvantages):

1. In this system interest paid (or) received is not included in revenue a/c. Hence revenue a/c does not show true and fair view of operating results.
2. It is very difficult to understand by general public.
3. Capital a/c does not show true position.
4. In this system fixed assets are shown at cost price in capital a/c. Hence Balance sheet does not show true and fair view of the financial position of the company.
5. It is very difficult to decide whether the expenditure is capital or revenue nature.

Difference between Double entry system and Double account system:-

S.No	Double entry system	Double Account system
1)	It is a method of book keeping	It is a method of presenting final accounts.
2)	Fixed assets are shown at cost less depreciation in the balance sheet.	Fixed assets are shown at cost price in capital a/c and Depreciation fund is shown in Balance sheet.
3)	Interest is charged to P&L a/c	Interest is charged to Net Revenue a/c.
4)	It consists of P&L A/c, P&L Appropriation a/c and Balance sheet.	It consists of Revenue a/c, Net Revenue a/c, capital a/c and General Balance sheet.
5)	Fixed assets and fixed liabilities are shown in the Balance sheet.	Only fixed assets and fixed liabilities are Shown in the capital a/c.

Difference between Double account and single account system:

S.No	Double A/c system	Single A/c System
1)	It is used by only public utility undertakings	It is used by all the companies.
2)	It consists of revenue a/c, Net Revenue a/c, Capital a/c and general Balance sheet	It consists of P&L a/c, P&L Appropriation a/c and Balance sheet.
3)	Balance sheet is presented into two parts: Capital a/c and general Balance sheet.	Only one Balance sheet is Presented.
4)	Share capital, Debentures will appear in Capital a/c	They are appear in Balance Sheet.
5)	Fixed assets are shown at cost price.	It is shown at cost less Depreciation.
6)	Its purpose is to how the capital is raised and how the same has been invested in fixed Assets.	Its purpose is to show the financial position of the Company.

Specimen form of Revenue account

Dr. **Revenue account** **Cr.**

To Staff Salaries	xx	By Sale of energy	xx
To Rent & Rates	xx	By Sale of lighting	xx
To Printing & Stationery	xx	By Transfer fees	xx
To Repairs & Renewals	xx	By Rent Received	xx
To Discount allowed	xx		
To Cost of generating	xx		
To Electricity	xx		
To Cost of distribution of electricity	xx		
To Management expenses	xx		
To Legal expenses	xx		
To Depreciation on fixed assets	xx		
To Balance carried to net revenue a/c	xx		
	xx		xx

Dr. **Net Revenue account** **Cr.**

To Balance b/d (if any)	xx	By Balance b/d (Balance from last year)	xx
To Revenue account	xx	By Revenue account	xx
To Interest on Loans	xx	By Government subsidy	xx
To Contingency reserve	xx	By Interest earned	xx
To Interest on debenture	xx	By Transfer from reserve	xx
To Dividend Control Reserve	xx	By General Balance Sheet (Loss-if any, transferred to general balance sheet – Bal.fig)	xx
To General Balance sheet (Bal.fig)	xx		
	xx		xx

Receipts and Expenditure on capital account

Expenditure	Previous year	Current year	Total	Receipts	Previous year	Current year	Total
To Land	xx	xx	xx	By Equity shares	xx	xx	xx
To Building	xx	xx	xx	By Preference Share capital	xx	xx	xx
To Machinery	xx	xx	xx	By Debentures	xx	xx	xx
To Plant	xx	xx	xx	By Loans	xx	xx	xx
To Main	xx	xx	xx	By Calls in advance	xx	xx	xx
Total Expenses	xx	xx	xx	Total Receipts	xx	xx	xx
To Balance transferred to general Balance sheet.	xx	xx	xx				
	xx	xx	xx		xx	xx	xx

General Balance sheet

Liabilities	Rs.	Assets	Rs.
Capital A/c (Balance brought forward from capital a/c)	xxx	Stores	xxx
Sundry creditors for capital account	xxx	Sundry Debtors	xxx
Sundry creditors on Open a/c	xxx	Cash at Bank	xxx
Net Revenue a/c	xxx	Cash in hand	xxx
Reserve fund	xxx	Securities	xxx
Depreciation fund	xxx	Special items	xxx
Sinking fund	xxx	Other assets	xxx
Investment fluctuation fund	xxx		
Other liabilities	xxx		
	xxx		xxx

Problem No.1

The following are the balances on 31st March 2021 in the books of Sivan Electric company Ltd.

Particulars	Dr	Cr
Land (01-04-2018)	60,000	----
Land expended during the year	2,000	----
Machinery (01-04-2018)	2,40,000	----
Machinery expended during the year	2,000	----
Mains	80,000	----
Mains expended during the year	20,400	----
Ordinary shares	----	2,19,600
Debentures	----	80,000
Creditors	-----	400
Depreciation fund a/c	16,000	1,00,000
Sundry Debtors for current supplied	----	
Other debtors	200	---

Cash	2,000	----
Cost of generation of electricity	14,000	---
Cost of distribution of electricity	2,000	----
Rent & Rates	2,000	----
Management Expenses	4,800	---
Depreciation	8,000	---
Sale of current	---	52,000
Rent of meters	----	2,000
Interest on debentures	4,000	----
Interim Dividend	8,000	----
Balance of Net Revenue a/c(01-04-16)	---	11,400
Total	**4,65,400**	**4,65,400**

From the above Trial balance prepare

i) Revenue a/c ii) Net Revenue a/c iii) Capital a/c iv) General Balance sheet.

Solution:

Revenue Account for the year ended on 31-03-2018.

To Cost of generation of electricity	14,000	By Sale of current	52,000
To Cost of Distribution of electricity	2,000	By Rent of meter	2,000
To Rent &Rates	2,000		
To Management Expenses	4,800		
To Depreciation	8,000		
To Balance carried to Net Revenue a/c	23,200		
	54,000		54,000

Net Revenue account for the year ended on 31-03-2018

To Interest on debentures	4,000	By Balance b/d	11,400
To Interim Dividend	8,000	By Balance from Revenue	23,200
To Balance carried to General Balance sheet	22,600		
	34,500		34,500

Receipts & Expenditure on capital account for the year ended on 31-03-2018

Expenditure	**Up to 31-03-17**	**Up to 31-03-18**	**Total**	**Receipts**	**Up to 31-03-17**	**Up to 31-03-18**	**Total**
To Land	60,000	2,000	**62,000**	By Equity Share capital	2,19,600	----	**2,19,600**
To Machinery	2,40,000	2,000	**2,42,000**	By Debentures	80,000	---	**80,000**
To Main	80,000	20,400	**1,00,400**				
Total Expenses	3,80,000	24,400	**4,04,400**	Total Receipts	2,99,600	----	**2,99,600**
				By Balance c/d			**1,04,800**
			4,04,400				**4,04,400**

General Balance sheet as on 31-03-2018

Liabilities	**Rs.**	**Assets**	**Rs.**
Total Capital Receipts	2,99,600	Total capital Expenses	4,04,400
Creditors	400	Sundry Debtors	16,000
Depreciation fund a/c	1,00,000	Other debtors	200
Net Revenue a/c	22,600	Cash	2,000
	4,22,600		4,22,600

Replacement of Asset

Replacement of asset means old asset is replaced and new asset is purchased.

Journal entries

1. For the amount spent on new works

New works a/c (amount to be capitalized)	Dr	xxx	
Replacement a/c (amount to be w/off to revenue)	Dr	xxx	
To Bank (Actual amount spent)			xxx

2. For the sale of old materials:

Bank a/c Dr	xxx	
To Replacement a/c		xxx

3. For the value of old material used in the construction

New works a/c Dr	xxx	
To Replacement a/c		xxx

(Being old materials used in new works)

4. For the balance in the Replacement a/c

Revenue a/c Dr	xxx
To Replacement a/c	xxx

(Being old materials sold)

5. For amount spent on new construction

New works a/c Dr	xxx	
To Bank a/c		xxx

Problem No: 2

A Railway station had to be replaced by a new station. The cost of new station is Rs.8,00,000. The old one had cost Rs.2,10,000 labour forming 3/10 of total expenditure and material accounting for the rest. Prices of raw materials have doubled and wage rates have gone by 250% materials of the old station Rs.38,000 were used in the new station and the sale proceeds of the old station materials were Rs.11,000. These materials were obtained by pulling down the old station. **Pass Journal entries.**

Solution

1)New works A/c Dr. 2,85,500

Replacement a/c Dr. 5,14,500

To Bank a/c 8,00,000

2) New works a/c Dr 38,000

To Replacement a/c 38,000

(Being old materials used in New works)

3) Bank a/c Dr 11,000

To Replacement a/c 11,000

(Being old materials sold)

4) Revenue a/c Dr 4,65,500

To Replacement a/c 4,65,500

(Being Replacement a/c transferred)

Working notes: Amount to be capitalized:

Cost of New works	8,00,000
Less: Estimated Replacement cost	6,14,500
Capitalized amount	2,85,500

Problem:3

The Southern Gas company rebuilt of their works with double the capacity at a cost of Rs.8,00,000/-.The cost of the part of old works was Rs.3,50,000. In working new works old materials of Rs.15,000 was reused and Material Rs.25,000 was sold away. The cost of Labour and Materials are 50% higher now than when the old works were built. Pass Journal entries.

Solution:

1) New works a/c Dr. 2,75,000

Replacement a/c Dr.5,25,000

To Bank 8,00,000

(Being amount paid for replacement)

2) New works a/c Dr 15,000

To Replacement a/c 15,000

(Being old materials used)

3) Bank a/c Dr 25,000

To Replacement a/c 25,000

4) Revenue a/c Dr 4,85,000

To Replacement a/c 4,85,000

(Being balance transferred to Revenue a/c)

Workings

Cost of new works	-	8,00,000
Less: Estimated Cost	-	5,25,000

Amount to be capitalized		2,75,000

Accounts of Holding Companies

Meaning:

A Company which controls one or more other companies by means of holds either the whole of the share capital or majority of the shares of another company. The controlling company is called as the holding company and the company so controlled is called as a subsidiary company.

Definition:

Section 4 of the companies Act 1956 defines a company shall be deemed to be the holding company of another, if that other is its subsidiary".

1. By holding more than 50% of the face value of the equity shares of the other company.
2. By controlling the composition of Board of directors of the other company.
3. By controlling a holding company which controls another subsidiary company.

For example:

If X Ltd is a subsidiary of Y Ltd and Y Ltd is a subsidiary of Z Ltd, then X Ltd is also considered to be subsidiary of Z Ltd.

Advantages of Holding company:

1) The object of holding companies is to promote combination movement and eliminate competition.

2) Enjoying economics in production and management may be secured.

3) Subsidiary companies retain their identities. Hence no liquidation is possible.

4) Holding companies getting advantages existing of goodwill of is possible subsidiary companies and also control is exercised on the affairs of subsidiary companies.

Disadvantages:

Manipulation of accounts, Manipulation of Intercompany transactions, oppression of minority shareholders, and exploitation of subsidiary companies by holding company are possible in the system of holding companies formation.

Procedure for preparing consolidated balance sheet, and consolidated profit & loss a/c:

Consolidated financial statement include consolidated balance sheet profit & loss account. This statement is to show the financial position and trading results of both holding & subsidiary companies. In consolidated Balance sheet in which assets and liabilities of all the subsidiaries are given along with the assets and liabilities of holding company in one single Balance sheet.

Steps to be taken for preparation of Consolidated Balance sheet

Step1: Wholly owned/ partly owned subsidiary company:

The share of the subsidiary company held by the holding company is treated as Investment. The Investment of the holding company in the subsidiary company is replaced by Net assets of subsidiary company.

Step 2: Calculation of Capital Profits and Revenue Profits

The profits of the subsidiary company can be divided into two namely capital profit and revenue profit.

Capital Profit

The profits earned by the subsidiary company up to the date of purchase (or) acquisition of shares by the holding company are called capital profit. These profits are shared by the outsiders and holding company according to their proportionate shares held by them. Capital profits of the holding company are shown as capital reserve in the consolidated Balance sheet and share of capital profit belonging to minority interest is added to be amount of minority interest.

Revenue Profit

The profits earned by the subsidiary company after the date of purchase (or) acquisition of shares by the holding company are called capital profit. Holding company's share is added to the profits of the holding company and a share of such profit belonging to the minority interest is added to the amount of minority interest.

Step 3: Calculation of Goodwill or Capital Reserve

When the holding company purchases the shares of the subsidiary company at a price above the face value, the excess amount paid represents the payment of goodwill. On the other hand, if the price paid for the purchase of shares is less than the paid up value, the difference is called capital reserve.

The goodwill / capital reserve is calculated as under:

Particulars	**Rs.**	**Rs.**
Paid up value of the equity held by the holding company		xxx
Add: Proportionate share in the capital profit	xxx	
Proportionate share in the capital reserve	xxx	xxx
		xxx
Less: Proportionate share in the capital loss		xxx
Total value		xxx
Less: Cost of equity (or) price paid for the investment		xxx
Goodwill / Capital reserve		xxx

Step 4: Calculation of Minority Interest

When some of the shares of the subsidiary company are held by outside shareholders, they will have a right to get a proportionate share in the assets and liabilities of that company their interest known as minority interest. The share of the outsiders in the subsidiary company is called minority interest. The Amount of minority is shown on the liabilities side of the balance sheet of the holding company.

Calculation of minority interest:

Paid up value of shares held by outsiders		xxx
Add: Proportionate share in the capital profit and reserve	xxx	
Proportionate share in the revenue profit	xxx	
Proportionate share in the increase in the value Of the assets of the subsidiary	xxx	
		xxx
Less: Proportionate share in the capital losses	xxx	
Proportionate share in the revenue losses	xxx	
Proportionate share in the decrease in the value Of the assets of the subsidiary	xxx	
Value of minority interest		xxx

Step 5: Preparation of Consolidated Balance sheet

Consolidation is to aggregate the assets and liabilities of both holding and subsidiary company or companies after adjusting and eliminating different items such as intercompany investments, intercompany owings, unrealized profits and so on.

Step 6: Elimination of common transactions:

While preparing consolidated Balance sheet, some common transactions appearing in both Balance sheet of holding company and subsidiary company should be eliminated.

Example: 1) Goods sold on credit by the holding company to the subsidiary company and vice versa.

2) Bill drawn by one company and accepted by another company.

3) Loan advanced by holding company to subsidiary company and vice

versa. 4) Debentures issued by one company and held by another company.

Step 7 Treatment of unrealized profits

If the goods sold at a profit by H to S company or S to H Company remains unsold at end of the year, profit charged by the company on unused goods remain unrealized. In this connection stock reserve is created and profit is reduced by unrealized profit. Further stock reserve is also reduced by share of minority interest. Stock reserve will be reduced on the liability side.

E.g. H Ltd purchased from S Ltd goods of the value of Rs.40000 on which S Ltd had charged a profit 20% on cost and goods worth Rs.12000 remained unsold at the end of the year.

Unrealized profit=12000x20/120 = Rs.2,000

Suppose H Ltd holds 75% equity shares of the subsidiary company

Stock reserve =2000x 75/100 = 1500s.1500 will be deducted from stock on asset side and 1,500 will be deducted from P&L a/c on the liabilities side.

Step 8 Treatments of Contingent Liabilities:

Contingent liability is that liability which arises or may not arise. Its payment depends on the occurrence of a future transaction which is not certain. Such a liability is shown by way of a footnote in the Balance sheet.

Example:

i) Arrears of dividend on cumulative preference shares.

ii) Claims against the company not acknowledged debt as yet.

iii) Bills discounted likely to be dishonoured.

iv) Amount uncalled on partly paid shares held.

Step 9 Revaluations of Assets and Liabilities:

If assets and liabilities of subsidiary company are revalued at the time of purchase of shares in the subsidiary company, profit or loss on account of such revaluation is treated as capital profit or capital loss and shared by minority shareholders and holding company according to the proportions of shares held by them. Holding company's share of capital profit is transferred to capital reserve, deducted from cost of control if there is loss on revaluation. Share of profit of minority shareholders is added to minority interest and deduction is made from the minority interest if there is a loss on revaluation.

Step10 Bonus Shares:

Bonus shares may be issued out of capital profits or revenue profits or reserves of the subsidiary company. There are two methods of issuing Bonus shares. They are:

a) Treatment of Issue of Bonus shares out of capital profit:

Issue of Bonus shares out of capital profits (Pre-acquisition profits) will have no effect on the consolidated Balance sheet.

b) Treatment of Issue of Bonus shares out of Revenue profits

Issue of Bonus shares out of revenue profits will have effect on the consolidated Balance sheet. The share of revenue profit earned by the holding company will be reduced and paid up value of shares held by the holding company will increase.

Problem No.1

From the following Balance sheet of holding company and subsidiary company prepare a consolidated balance sheet of holding company and its subsidiary company.

Balance sheet as on 31st March, 2020

Particulars	**H Rs.**	**S Rs.**	**Particulars**	**H Rs.**	**S Rs.**
Share Capital in Re.1 shares	20,000	10,000	Sundry Assets	25,000	12,000
Sundry Liabilities	15,000	2,000	Investments: 10,000 shares of Re.1 each in S Ltd	10,000	----
	35,000	12,000		35,000	12,000

Solution:

Consolidated Balance sheet as on 31st March, 2020

Liabilities	**Rs.**	**Rs.**	**Assets**	**Rs.**	**Rs.**
Share capital of H Company		20,000	Sundry Assets		
Sundry liabilities			H	25,000	
H	15,000		S	12,000	37,000
S	2,000	17,000			
		37,000			37,000

ProblemNo.2

The Balance Sheets of Anbu Ltd and Babu Ltd as on 31st December, 2017 were as follows:

Liabilities	**Anbu Ltd**	**Babu Ltd**	**Assets**	**Anbu Ltd**	**Babu Ltd**
Share capital in Rs.10 fully paid			Fixed Assets	10,000	6,000
Shares	12,000	5,000	Current Assets	11,500	2,000
Equity shares	4,000	1,000	Cash at Bank	7,000	1,000
Preference shares	2,500	1,000			
Profit and Loss A/c	10,000	2,000			
Creditors					
	28,500	9,000		28,500	9,000

On 1st January, 2018, Anbu Ltd acquired 90% of share capital of Babu Ltd at 15 per share. Prepare the consolidated Balance Sheet as on 1st Jan,2018.

Solution:

Consolidated Balance Sheet of A Ltd and its subsidiary B Ltd as on 1st January 2018

Liabilities	Rs.	Assets	Rs.
Share capital		Cost of control	1,350
(Rs.10 fully paid)	12,000	Fixed Assets Anbu Ltd 10,000	
Preference share	4,000	Babu Ltd 6,000	16,000
Profit and Loss A/c	2,500		
Minority interest	1,600	Current Assets	
Creditors		Anbu Ltd 11,500	
Anbu 10,000		Babu Ltd 2,000	13,500
Babu 2,000	12,000	Cash at Bank	
		Anbu Ltd 250	
		Babu Ltd 1,000	1,250
	32,100		32,100

(1) Ascertainment of cost of control

Investment A/c.(450 shares at Rs.15)		6,750
Less:Paid up value of 450 share	Rs.4,500	
90% of pre-acquisition Profits i.e.90% of 1,000	900	~~5,400~~
Cost of control		1,350

(2) Minority Interest:

Paid up value of 50 Equity shares @ Rs. 10	500
Paid up Value of preference shares	1,000
10% of Profits and Loss A/c balances	100
Minority Interest	1,600

Problem No.3

The following Balance sheet as on 31st March, 2017 is given:

Liabilities	H	S	Assets	H	S
Share Capital in Re.1 fully paid shares	12,000	6,000	Sundry Assets	20,000	12,000
Reserve	3,000	2,000	Investments 6,000 shares in S Ltd	7,500	----
Profit and Loss A/c	2,000	1,000			
Sundry liabilities	10,500	3,000			
	27,500	12,000		27,500	12,000

H Ltd. has acquired shares in S Ltd on 31st March, 2017. Prepare consolidated Balance Sheet as on 31.03.2017.

Solution:

Calculation of capital reserves:

Equity purchased in the subsidiary

Share Capital	6,000
Reserve	2,000
Profit and Loss A/c	1,000
Total	9,000
Less: Price paid for investment	7,500
Capital Reserve	1,500

Consolidated Balance sheet as on 31st March 2017

Share capital			Sundry assets		
Re.1 fully paid shares		12,000	H	20,000	
Capital reserve		1,500	S	12,000	32,000
Reserve (H Ltd)		3,000			
Profit & Loss A/c (H Ltd)		2,000			
Sundry Liabilities					
H	10,500				
S	3,000	13,500			
		32,000			32,000

Problem No. 4

Consolidate the following Balance sheet

Liabilities	H Ltd	S Ltd	Assets	H Ltd	S Ltd
Share Capital in Re.1fully paid shares	14,000	10,000	900 shares in S Ltd at cost	12,000	----
Creditors	---	5,000	Sundry Assets	2,000	18,000
Profit and Loss A/c	---	3,000			
	14,000	**18,000**		**14,000**	**18,000**

When H Ltd acquired the shares in S Ltd., the profit and loss account in the latter had a credit balance of Rs.2,000.

Solution:

Share of Holding company and minority shareholdings

= 900: 100 (or) 9:1

i) Calculation of Capital profit

Balance of profit on the date of acquisition Rs.2,000.

Holding company 2,000 x 9/10 = Rs.1,800

Minority Shareholders 2,000 x 1/10 = Rs.200

ii) Calculation of Revenue Profit

Balance in Profit & Loss a/c	3,000
Less: Capital profit	2,000

Revenue profit earned during the year	1,000
	========

Holding company 1,000 x 9/10 = Rs.900

Minority Shareholders 1,000 x 1/10 = Rs.100

iii) Calculation of Goodwill (or) Capital Reserve

Paid up value of equity capital		9,000
Add: Share of Capital profit		1,800

		10,800
Less: Price paid for investment		12,000

Goodwill		1,200
		=======

iv) Calculation of Minority Interest

Paid up value of equity capital		1,000
Add: Share of capital profit	200	
Share of revenue profit	100	300
Total		1,300

Consolidated Balance sheet

Liabilities	Rs.	Assets	Rs.
Share Capital	14,000	Sundry Assets	20,000
Creditors	5,000	Goodwill	1,200
Profit and Loss A/c	900		
Minority interest	1,300		
	21,200		**21,200**

Problem No. 5

Consolidate the following Balance sheet

Liabilities	H Ltd	S Ltd	Assets	H Ltd	S Ltd
Share Capital Rs.10 shares	2,400	1,600	Sundry Assets	1,400	1,950
Creditors	---	300	128 shares in S Ltd	1,000	----
Profit and Loss A/c	---	50			
	2,400	**1,950**		**2,400**	**1,950**

On the date of acquisition, S Ltd had a debit balance of Rs.100 on profit and loss a/c.

Solution:

Share of Holding company and minority shareholdings

=128 : 32 (or) 4:1

i) Calculation of Capital Loss

Loss on the date of acquisition Rs.100

Holding company 100 x 4/5 = Rs.80

Minority Shareholders 100x1/5 = Rs.20

ii) Calculation of Revenue Profit

Balance in Profit & Loss a/c	50
Add: Loss written off	100

Revenue profit earned during the year	150
	========

Holding company 150 x 4/5 = Rs.120

Minority Shareholders 150 x 1/5 = Rs.30

iii) Calculation of Goodwill (or) Capital Reserve

Paid up value of equity capital (128 x 10)	1,280
Less: Share of Capital loss	80

	1,200
Less: Price paid for investment	1,000

Capital Reserve	200
	=======

iv) Calculation of Minority Interest

Paid up value of equity capital (32 x 10)	320
Less: Share of capital loss	20
	300
Add: Share of Revenue profit	30
Total	330

Consolidated Balance sheet

Liabilities	Rs.	Assets	Rs.
Share Capital	2,400	Sundry Assets H Ltd 1,400 S Ltd 1,950	3,350
Creditors (S Ltd)	300		
Profit and Loss A/c (S Ltd)	120		
Minority interest	330		
Capital Reserve	200		
	3,350		**3,350**