STUDY MATERIAL

Prepared for

II M.Com (III Sem)

Subject

Advanced Corporate Accounting

Prepared by

Dr. T. JESI, M.Com., M.Phil., M.B.A., P.G.D.C.A., Ph.D.,

Assistant Professor, Department of Commerce

Department of Commerce

Government Arts & Science College (Women)

Sathankulam - 628704

Unit I : **Alteration of Share Capital& Amalgamation Absorption and Reconstruction:**

Alteration of Share Capital – Procedure for Reducing Share capital. **Amalgamation, absorption and External reconstruction** – Methods of Computing purchase consideration - types of amalgamation. Internal reconstruction Vs External reconstruction – simple problems.

Unit II : **Valuation of Goodwill& Liquidation of companies:**

Valuation of Goodwill – Factors determining the value of Goodwill – Methods of valuation of Goodwill. **Valuation of shares** – Methods of valuation of shares – **Liquidation of companies** – Liquidators final statement of accounts – simple problems.

Unit III : **Accounts of Banking Companies:**

Accounts of Banking companies – Rebate on bills discount – Assets classification and provisions – preparation of various schedules and final accounts – Simple problems.

Unit IV : **Accounts of Insurance companies:**

Accounts of Insurance companies: Life Insurance and General Insurance – Preparation of various schedules and final accounts. Simple problems.

Unit V : **Double Accounting & Accounts of Holding Companies:**

Double Accounting – Accounts of Electric supply companies (including railways and public utilities). Replacement of assets – preparation of final accounts. **Accounts of Holding companies:** steps involved in preparation of consolidated balance sheet – legal provisions – simple problems.

UNIT - I

ALTERATION OF SHARE CAPITAL & AMALGAMATION ABSORPTION AND RECONSTRUCTION

INTERNAL RECONSTRUCTION

MEANING

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

This arrangement made for one or more of the following 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.

ALTERARTION OF SHARE CAPITAL

Alteration of share capital can be done under provision of Sections 94 to 97 of the Companies Act 1956. This includes the following:

i) Increase of Share Capital
ii) Consolidation of Shares
iii) Sub-division of Shares
iv) Conversion of Shares into Stock
v) Cancellation of Unissued Shares

STEPPS FOR RECONSTRUCTION

Step 1 : Estimating the Losses

Step 2 : Writing off the Loss

Step 3 : Compensating the Various Parties

Step 4 : Arranging the Working Capital

SUM - 1

The following is the Balance Sheet of Weak & Co. as on 31.03.2019.

Liabilities	Rs.	Assets	Rs.
1,00,000 equity shares of		Land	1,00,000
Rs. 10 each	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 & L a/c	5,50,000
	11,73,000		11,73,000

Scheme of Capital Reduction was:

a) The equity shares to be reduced to Rs. 4 per share.
b) Plant and Machinery to be written down to Rs. 1,50,000.
c) Stock to be revalued at Rs. 1,40,000.
d) The provision on debtors for doubtful debts to be created Rs. 2,000.
e) Land to be revalued at Rs. 1,42,000.

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)			

AMALGAMATION

When two or more companies go into liquidation and a new company is formed to take over the business of the above two or more companies it is said to be amalgamation. To avoid competition and to fix the price of an article, amalgamation takes place.

ABSORPTION

When one or more existing companies go into liquidation and some existing company takes over the business, it is said to be absorption. That is, the business of a small company is absorbed by the big company.

RECONSTRUCTION

Reconstruction refers to the reconstruction of a company's financial structure. It may take place with or without the liquidation of the company. If a company goes into liquidation for reconstruction, then it is known as external reconstruction. If a company does not go into liquidation, then it is known as internal reconstruction.

Reconstruction may be of two types:

i) External reconstruction
ii) Internal reconstruction

Reconstruction means the structure of share capital, debentures and creditors are reconstructed.

SUM - 2

X Co. Ltd. agreed to acquire the assets excluding cash as on 31st December 2000 of Y Co. Ltd. The balance sheet of Y Ltd. as on that date was:

Liabilities	Rs.	Assets	Rs.
Equity capital Rs.10 each	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 share of Y Ltd.
b) The issues of one share of Rs.10 each (Market value Rs.12.50) in the X Co. Ltd. for every share in Y Co. Ltd.
c) The issue of the debenture of Rs.50 each in X Co. Ltd. to enable Y Ltd to discharge its debentures at a premium of 10%.
d) The expenses of liquidation of Y Ltd. amounting to Rs. 4000 were to be met by themselves.

Give the journal entries in the books of both the companies and balance sheet.

SOLUTION:

Journals Entries in the Books of Y 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			55,000
4.	X 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 X 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.	Share holders a/c	Dr	24,000	
	To Realisation a/c			24,000
9.	Share holders 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

Journals Entries in the Books of X Co. Ltd.

1.	Business purchase a/c	Dr	4,75,000	
	To Liquidator of Y co.			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	
	Business purchase			4,75,000
3.	Liquidator of Y co.	Dr	4,75,000	
	To Share capital			2,40,000
	To Share premium			60,000
	To Debenture			55,000
	To Bank			1,20,000

SUM - 3

The following is the balance sheet of X Ltd.

	Rs.		**Rs.**
20,000 10% Pref. shares of		Goodwill	50,000
Rs.10 each	2,00,000	Other Fixed Assets	1,80,000
2,000 equity shares of		Stock	50,000
Rs.100 each	2,00,000	Debtors	60,000
Creditors	30,000	P/L a/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 X 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 & Lose a/c			90,000
	To Fixed asset 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 Asset a/c	40,000		
	1,80,000		**1,80,000**

Balance sheet of X 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**

UNIT - II

VALUATION OF GOODWILL & LIQUDATION OF COMPANIES

GOODWILL

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

FACTORS AFFECTING GOODWILL

The following factors are to be considered while valuing the goodwill a business.

i) Skill of management.
ii) Size of the business
iii) Location the business
iv) Quality of the products produced
v) Use of patents
vi) Employees working in the business
vii) Profitability
viii) Capital employed

CIRCUMSTANCES UNDER WHICH GOODWILL MAY BE VALUED

Goodwill of a company may be valued under the following circumstances

i) When two or more firms decided to amalgamate
ii) When a company takes over another
iii) When there is external reconstruction of a company
iv) When a partnership business is sold to a company
v) When there is exchange of shares
vi) When a new partner is admitted
vii) When a partner is retired
viii) When the Government takes over the business of a company

SUM - 1

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 percent.
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 purchased
= 13,723 x 3
= **Rs. 41,169**

ii) Super Profit Method

Goodwill = Super Profit x Number of years of purchased
Super Profit = Average Profit – Normal Profit
Normal Profit = Normal rate of return x capital employed
= 70,000 x 18/100
= Rs. 12,600
Super Profit = 13,723 – 12,600
= Rs. 1,123
Goodwill = 1,123 x 3
= **Rs. 3,369**

iii) Capitalisation of super profit method

Goodwill = Super Profit / Normal rate return
= 1,123 x 100 / 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 = 3,723 x 100 / 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 pastes 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.

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

SUM - 2

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:

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) Assets method and
ii) Yield method.

SOLUTION:

i) Net Assets Method

$$\text{Value per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}}$$

$$\text{Value per Share} = \frac{7{,}40{,}000}{80{,}000}$$

$$= \text{Rs.}\,9.25$$

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**

ii) Yield Method

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

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

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

$$\text{Expected rate of return} = \frac{82{,}800}{8{,}00{,}000} \times 100$$

$$= 10.35\ \%$$

PURCHASE CONSIDERATION

Accounting Standard – 14 defines the term consideration as follows, "consideration for amalgamation means the aggregate of the shares and other securities issued and payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company". Payment made to debenture holders should not be considered as part of purchase consideration. Purchase consideration should not include the amount of liabilities taken over by the transferee company.

Amount of purchase consideration can be computed under any one of the following four methods.

1. Lumpsum method
2. Net payment method
3. Net assets method
4. Instrinsic value method

1) Lumpsum Method

Under this method, the transferee company agrees to pay a fixed sum to the transferor company. The purchase price to be paid to shareholders may be stated in the agreement directly.

2) Net assets method

According to this method, the purchase consideration is calculated on the basis of net assets taken over by the transferee company.

A net asset to be taken by the purchasing company is considered to be the purchase consideration.

3) Net payment method

Under this method purchase consideration is calculated by adding the various payments in the form of shares, securities, cash etc made by the transferee company. No amount of liabilities is deducted even if these are assumed by purchasing company.

The total of payments represents the net payment made by the purchasing company as purchase price for the concern.

4) Intrinsic value method or shares exchange method

Under this method, purchase consideration is required to be calculated on the basis of the ration in which the shares of the purchasing company are exchanged with those of the selling company. The exchange ratio is calculated on the basis of intrinsic values of the respective companies' shares.

SUM - 3

The following is the balance sheet of X Ltd. as on March 2002.

Liabilities	Rs.	Assets	Rs.
20,000 6% Pref.shares of		Goodwill	40,000
Rs. 20 each	4,00,000	Premises	2,20,000
12,500 equity shares of		Plant & machinery	2,60,000
Rs.40 each	5,00,000	Investments	30,000
Loan from B	50,000	Patents	3,00,000
Creditors	1,00,000	Stock	70,000
		Debtors	44,300
		Bank	39,000
		Preliminary expenses	10,000
		P& L a/c	36,700
	10,50,000		**10,50,000**

The company suffered losses. The following scheme of reconstruction was adopted:

a) The pref. shares to be reduced to an equal number of Rs.10 each fully paid.
b) The equity shares to be reduced to an equal number of shares of Rs.10 each fully paid.
c) Loan creditor, B has agreed to accept Rs. 30,000 each and to forfeit the balance. The amount thus rendered available is to be used to:
    1. Write off premises Rs.20,000, Plant & Machinery Rs.60,000, Debtors Rs.14,300 and stock by 20% and
    2. To write off Goodwill, patents and other fictitious assets.

Journalise the transactions and prepare the balance sheet of the company after reconstruction has been carried out.

SOLUTION:

Journal Entries in the Books of X Ltd.

1.	Old Pref. share capital a/c	Dr	4,00,000	
	To New pref. share capital			2,00,000
	To capital reduction a/c			2,00,000
2.	Old equity shares a/c	Dr	5,00,000	
	To New equity shares a/c			1,25,000
	To capital reduction a/c			3,75,000
3.	Loan from B a/c	Dr	50,000	
	To Cash a/c			30,000
	To Capital reduction			20,000
4.	Capital reduction a/c	Dr	5,95,000	
	To Premises			20,000
	To Plant & Machinery			60,000
	To Debtors			14,300
	To Stock			14,000
	To Goodwill			40,000
	To Patents			3,00,000
	To Preliminary expenses			10,000
	To P&L			36,700
	To Capital reserve			1,00,000

BALANCE SHEET OF X LTD.

Liabilities	Rs.	Assets	Rs.
Pref. Share capital	2,00,000	Premises	2,00,000
Equity share capital	1,25,000	Plant & Machinery	2,00,000
Creditors	1,00,000	Investments	30,000
Capital reserve	1,00,000	Stock	56,000
		Debtors	30,000
		Bank	9,000
	5,25,000		**5,25,000**

LIQUDATION

Liquidation or winding up is a process, by which a company is dissolved and its assets realized and applied in paying off the liabilities of the company. If there is any surplus after closing off the liabilities, it is distributed to its contributories according to their rights.

ORDER OF PAYMENT

i) Liquidation Expenses
ii) Liquidator's Remuneration
iii) Secured Creditors
iv) Debenture holders
v) Preferential Creditors
vi) Unsecured Creditors
vii) Preference Shareholders
viii) Equity Shareholders

SUM - 1

The Ultra Optimist went into liquidation. Its assets realized Rs. 3,50,000 excluding amount realized by sale of securities held by the secured creditors.

	Rs.
Share Capital : 1000 shares of Rs. 100 each	1,00,000
Secured Creditors (Securities realized Rs. 40,000)	35,000
Preferential Creditors	6,000
Unsecured Creditors	1,40,000
Debentures having floating charge	2,50,000
Liquidation Expenses	5,000
Liquidator's Remuneration	7,500

Prepare liquidator's final statement of account.

SOLUTION:

THE ULTRA OPTIMIST COMPNAY (In Liquidation)

Liquidator's Final Statement of Account

Receipt	Estimated Value Rs.	Value Realised Rs.	Payments	Payments Rs.
Assets Realised	-	3,50,000	Liquidator's Remuneration	7,500
Surplus from			Liquidation Expenses	5,000
Secured Creditors	-	5,000	Debenture having Floating Charge	2,50,000
(40,000 - 35,000)			Preferential Creditors	6,000
			Unsecured Creditors (Bal. Flg.)	86,500
			@ Re. 0.62 per rupee	
			(86,500 / 1,40,000 = 0.62)	
		3,55,000		3,55,000

UNIT - III

ACCOUNTS OF BANKING COMPANIES

BANK

Bank is a place for keeping money and valuables safely, the money being paid out on the customer's order, that is cheques.

BANKING - DEFINITION

"Accepting, for the purpose of lending or investment, or deposits of money from the public repayable on demand or otherwise and withdrawal by cheque, draft, order or othersise"

- Sec. 5 of the Banking Regulation Act. 1949

FORM OF BUSINESS IN WHICH BANKING COMPANIES MAY ENGAGE

Sec. 6 of the Banking Regulation Act contains d detailed list of the forms of business a banking company may engage in any one or more of the following forms of business, in addition to its banking business.

i) Borrowing, raising or taking up of money;
ii) Lending or advancing money;
iii) Drawing, making, accepting, discounting, buying, selling, collecting and dealing in bills of exchange, hundis, promissory notes and other instruments;
iv) Granting and issuing of letters of credit, traveller's cheques and circular notes;
v) Buying, selling and dealing in bullion.

FINAL ACCOUNTS

Banks are required to prepare final accounts for each financial year. Its books are closed every year on 31st March. But for internal purpose, banks usually close their books on 30th September.

PROFIT AND LOSS ACCOUNT

A banking company is required to prepare its Profit and Loss Account according to Form B in the Third Schedule to the Banking Regulation Act, 1949. Form B is in s summary form and the details of the various items are given in the schedules. Form B is given in the following form.

Form 'B'
PROFIT & LOSS ACCOUNT
for the year ended 31st March (Year) (000's omitted)

	Schedule	Year ended on 31.3… (Current Year)	Year ended on 31.3… (Prev. Year)
I. Income			
Interest Earned	13		
Other Income	14		
Total			
II. Expenditure			
Interest Expended	15		
Opening Expenses	16		
Provisions and Contingencies			
Total			
III. Profit / Loss			
Net Profit / Loss for the Year			
Profit / Loss Brought Forward			
Total			
IV. Appropriations			
Transfer to Statutory Reserve			
Transfer to other reserve			
Transfer to Government /Proposed dividend			
Balance Carried to Balance Sheet			
Total			

FORM OF BALANCE SHEET
BALANCE SHEET OF _______________ (Name of the Banking Company)
as on 31st March _________. (000's omitted)

Capital and Liabilities	Schedule	as on 31.3… (Current Year)	as on 31.3… (Prev. Year)
Capital	1		
Reserves	2		
Deposits	3		
Borrowings	4		
Other Liabilities and Provisions	5		
Total			
Assets			
Cash and Balance with Reserve Bank of India	6		
Balance with Banks and Money at call and Short Notice	7		
Investments	8		
Advances	9		
Fixed Assets	10		
Other Assets	11		
Total			
Contingent Liabilities			
Bills for Collection	12		

SUM - 1

On 31st March 2020 a Bank held the following bills, discounted by it earlier:

Date of the Bills	Terms of bills	Discounted Rate	Amount of Bill Rs.
January, 17	4 Months	10%	5,30,000
February, 7	3 Months	9%	6,40,000
March, 9	3 Months	11%	2,80,000

You are required to calculate the rebate on bills discounted.

Also show the necessary journal entry for the rebate.

SOLUTION:

Statement of Rebate on Bills Discounted as on 31.03.2020

Date of Bill 2020	Date of Maturity including 3 days	No. of days after 31.03.2020	Discount Rate	Amount Bill	Rebate on Bills Discount
Jan, 17	May 20	50	10%	5,30,000	$5{,}30{,}000 \times \frac{10}{100} \times \frac{50}{365} = 7{,}260$
Feb, 7	May 10	40	9%	6,40,000	$6{,}40{,}000 \times \frac{9}{100} \times \frac{40}{365} = 6{,}312$
Mar, 9	Jun 12	73	11%	2,80,000	$2{,}80{,}000 \times \frac{11}{100} \times \frac{73}{365} = 6{,}160$
Total Rebates on Bills to be Carried Forward					19,732

Journal Entry

Date	Particulars	Debit Rs.	Credit Rs.
31.03.2020	Discount Received a/c Dr.	19,732	
	To Rebate on bills discounted		19,732

SUM - 2

The following are the Trial Balance of Indian bank Ltd as on 31.03.2020.

	Debit Rs.	Credit Rs.
Share capital 25,000 equity shares of Rs. 20 each	-	5,00,000
Reserve fund	-	2,00,000
Loans and advances	23,85,000	-
Promises	60,000	-
Reserve Fund Investment	2,00,000	-
Investment in Government securities	1,60,000	-
Current and other deposits	-	20,80,000
Salaries	60,000	-
General expenses	32,000	
Rent, Rates and Taxes	3,000	-
Directors fees	20,000	-
Profit and Loss Account as on 1.1.2020	-	35,000
Interest and discounts		3,12,000
Money at call and short notice	80,000	-
Income tax paid	26,000	-
Bills discounted	36,000	-
Interim dividend paid	25,000	-
Cash in hand with RBI	40,000	-
	31,27,000	31,27,000

a) Interest accrued on Investment Rs. 22,000.

b) The market value of Government securities is Rs. 1,50,000 and provision is to made.

c) Authorised capital 50,000 shares of Rs. 20 each.

Prepare profit and loss account and balance sheet as on 31.03.2020.

SOLUTION:

INDIAN BANK LTD.,
Profit and Loss Account as on 31.03.2020

	Schedule	As on 31.03.20 Rs.
I. Income		
Interest Earned	13	3,34,000
Other Income	14	-
Total		3,34,000
II. Expenditure		
Interest Expended	15	-
Opening Expenses	16	1,15,000
Provisions and Contingencies		36,000
Total		1,51,000
III. Profit / Loss		
Net Profit for the Year		1,83,000
Profit Brought Forward		35,000
Total		2,18,000
IV. Appropriations		
Transfer to Statutory Reserve $1{,}83{,}000 \times \frac{25}{100}$		45,750
Dividend		25,000
Balance Carried to Balance Sheet		
Total		2,18,000

INDIAN BANK LTD.,
Balance Sheet as on 31.03.2020

	Schedule	As on 31.03.20 Rs.
Capital and Liabilities:		
Capital	1	5,00,000
Reserve & Surplus	2	3,93,000
Deposits	3	20,80,000
Borrowings	4	-
Other Liabilities Provisions	5	-
Total		29,73,000
Assets:		
Cash & Balance with RBI	6	40,000
Balance with other Bank and Money at call and short notice	7	80,000
Investments	8	3,50,000
Advances	9	24,21,000
Fixed Assets	10	60,000
Other Assets	11	22,000
		29,73,000
Contingents Liabilities		
Bills for Collection	12	2,10,000

UNIT - IV

ACCOUNTS OF INSURANCE COMPANIES

MEANING

Insurance is a contact whereby insurers agree to compensate for a specific loss to the insured, who in consideration, agrees to pay regularly a sum of money called premium. The insurance company is known as the insurer and the person taking the policy from the insurance company is known as insured. Therefore, insurance is a commercialized form of spreading risk.

KINDS OF INSURANCE

1) Life Insurance

It is a contract between the insured and the insurance compnay in which the insurance company agrees to pay the policy amount on death of the insured or on the maturity of the policy whichever is earlier. For this purpose the insured agrees to regularly remit a certain sum of money as premium.

Example: Whole Life, Endowment, health Insurance and so on.

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, Accident Insurance.

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. With the increase of the socialistic ideas, the social insurance is an obligatory duty of the nation.

Example: Pension Plans, Disability Benefits, Sickness Insurance and Industrial insurance.

OBJECTIVES (or) AIMS OF PREPARING ACCOUNTS

- i) To know the real financial position of the insurance companies.
- ii) To determine the insurance policy of the insurance company.
- iii) To know the actual profits earned by the insurance companies.

SUM - 1

From the following Balances of Hi-Fi General Insurance Co. Ltd. as on 31st March, 2018. Prepare

i) Fire Revenue Account

ii) Marine Revenue Account and

iii) Profit and Loss Account

	Rs.		Rs.
Survey Expenses (Fire)	10,000	Commission Earned on	
Additional Reserve Opening (Fire)	50,000	Re-insurance Ceded (Marine)	60,000
Commission Paid (Marine)	1,08,000	Commission Earned on	
Commission Paid (Fire)	90,000	Re-insurance Ceded (Fire)	30,000
Claims Paid and Outstanding (Marine)	3,80,000	Management Expenses (Fire)	1,45,000
Claims Paid and Outstanding (Fire)	1,80,000	Management Expenses (Marine)	4,00,000
Fire Fund - Opening	2,50,000	Marine Premium	
Marine Fund - Opening	8,20,000	Less : Re-insurance	10,80,000
Bad Debts Recovered	1,200	Fire Premium	
Share Transfer Fee	800	Less : Re-insurance	6,00,000
Directors' Fees	5,000	Profit on Sale of Land	60,000
Auditors' Fees	1,200	Miscellaneous Receipts	5,000
Bad Debts (Marine)	12,000	Differences in Exchange (Cr.)	300
Bad Debts (Fire)	5,000	Interest, Dividends, etc. - Received	14,000
		Depreciation	35,000

In addition to usual reserves, additional reserve in case of fir insurance is to be increased by 5% of net premium.

SOLUTION:

FIRE REVENUE ACCOUNT

for the year ended 31st March, 2018

Particulars	Schedule	(Current Year) Rs.
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

MARINE REVENUE ACCOUNT

for the year ended 31st March, 2018

Particulars	Schedule	(Current Year) Rs.
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 related to Insurance Business	4	4,12,000
TOTAL (B)		8,40,000
Operating Loss (C) = (A - B)		(-) 20,000

PROFIT & LOSS ACCOUNT

for the year ended 31.03.2018

			Rs.
1.	Operating Profit / (Loss)		
	(a) Fire Insuracne		1,20,000
	(b) Marine Insurance		(-) 20,000
2.	Income from Investments		
	Interest, Dividend & Rent-Gross		14,000
	Profit on Sale of Land		60,000
3.	Other Incomes:		
	(a) Transfer Fees		800
	(b) Bad Debt Recovered		1,200
	(c) Misc Receipts		5,000
	(d) Difference in Exchange		300
		Total (A)	1,81,300
	Other Expenses:		
	i) Auditors' Fees		1,200
	ii) Directors' Fees		5,000
	Depreciation		35,000
		Total (B)	41,200
	Profit Before Tax		1,40,100
	Provision for Taxation		-
	Profit After Tax		1,40,100
	Appropriations:		
	Balance of Profit / Loss Brought Forward from Last Year		-
	Balance Carried Forward to Balance Sheet		1,40,100

UNIT - V

DOUBLE ACCOUNT & ACCOUNTS OF HOLDING COMPANIES

DOUBLE ACCOUNT SYSTEM

MEANING

It is a method of presenting annual financial statement generally used by the undertakings; prepare two balance sheets instead of one.

REPLACEMENT OF AN ASSET

Under double account system, if an asset is abandoned due to obsolescence or any other reasons, there is no need to write off such losses. The asset continues to be in the books at original cost. Once an asset appears in the capital a/c at a certain figure, its value is not reduced.

SUM - 1

The Indane Gas Company rebuilt and re-equipped part of their works at a cost of Rs. 5,00,000. The part of the old works thus superseded cost Rs. 3,00,000. The capacity of the new works is double the capacity of the old works. Rs. 20,000 is realized by the sale of old materials and old materials worth Rs. 10,000 are used in the construction of the new works and included in the total of Rs. 5,00,000 mentioned above. The costs of labour and materials are 25% higher than when the old works built.

Journalise the entries.

SOLUTION:

Calculation of Estimated Cost of Replacement

	Rs.
Cost of Old Works	3,00,000
Add : Increase in cost Rs. 3,00,000 × 25 / 100	75,000
Estimated cost of replacement	3,75,000

Cost of New Works = 5,00,000 -10,000 = Rs. 4,90,000

Calculation of Amount to be Capitalised

	Rs.
Cost of Re-Building	4,90,000
Less : Estimated Cost of Replacement	3,75,000
Amount to be Capitalised	1,15,000

Calculation of Amount to be Charged to Revenue a/c

			Rs.
Estimated Cost of Replacement			3,75,000
Less :	Materials Re-Used	10,000	
	Materials Realised	20,000	30,000
Amount to be Transferred to Revenue a/c			3,45,000

Journal Entries

Date	Particulars		L.F.	Debit Rs.	Credit Rs.
	New Works a/c	Dr.		3,75,000	
	Replacement a/c	Dr.		1,15,000	
	To Bank				4,90,000
	(Being the current cost of replacement charged to replacement a/c and the balance is capitalized)				
	New Works a/c	Dr.		10,000	
	To Replacement a/c				10,000
	(Being the cost of old parts used is new Plant)				
	Bank a/c	Dr.		20,000	
	To Replacement a/c				20,000
	(Being the old materials realized credited to replacement a/c)				
	Revenue a/c	Dr.		3,45,000	
	To Replacement a/c				3,45,000
	(Being the amount charged to revenue a/c)				

HOLDING COMPANY

DEFINITION:

A holding company may be defined as "a company which controls one or more other companies by means of holding shares in that company or companies of by having power to appoint directly or indirectly the whole or a majority of the board of directors of those".

SUBSIDIARY COMPANY

A company controlled by a holding company is termed as a subsidiary company.

OBJECTIVES OF HOLDING COMPANY

i) To promote combination movement, so that competition may be eliminated.
ii) To secure the benefits of large scale production.
iii) To have product diversification.
iv) To reduce cost through large scale purchase.
v) To control the market.

CONSOLIDATION

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

STEPS TO BE TAKEN FOR PREPARATION OF CONSOLIDATED BALANCE SHEET

I. ELEMINATION OF INVESTMENT

In the consolidated Balance Sheet the investment a/c of the holding company and the equity share capital a/c of the subsidiary company will not appear.

II. CALCULATION OF CAPITAL PROFITS AND REVENUE PROFITS

The profits of the subsidiary company should be divided into capital profit and revenue profit.

Capital Profit

Profits existing in the subsidiary or earned by the subsidiary company upto the date of acquisition of shares by the holding company are called capital profit.

Revenue Profit

The profits earned by the subsidiary company after the purchase of shares by the holding are called revenue profits.

III. CALCULATION OF GOODWILL OR CAPITAL RESERVE

The goodwill / capital reserve is calculated as under:

		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 the Equity (or) Price paid for the investment		XXX
	(-) Goodwill / (+) Capital Reserve		XXX

IV. CALCULATION OF MINORITY INTEREST

The minority interest is calculated as under:

		Rs.	Rs.
Paid-up value of the 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
			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 assets	XXX	XXX
	Minority Interest		XXX

SUM - 2

The following are the extracts from the Balance Sheet of H Ltd. and S Ltd. as on 31st December 2019.

Liabilities	H Ltd. Rs.	S Ltd. Rs.	Assets	H Ltd. Rs.	S Ltd. Rs.
Share capital (Rs.10 Each)	5,00,000	1,00,000	Fixed Assets	4,00,000	60,000
Profit & Loss a/c	2,00,000	60,000	Stock	3,00,000	1,20,000
Reserves	60,000	30,000	Debtors	75,000	70,000
Creditors	90,000	60,000	7500 shares in S Ltd. at cost	75,000	-
	8,50,000	2,50,000		8,50,000	2,50,000

The Stock of H Ltd. includes Rs. 25,000 bought from S Ltd. at a profit to latter of 20% on sales.

All the profits of S Ltd. has been earned since the shares were acquired by H Ltd. but there was already the reserve of Rs. 30,000 at that date.

SOLUTION:

I. Share of Holding Company and Minority Shareholdings

7500 : 2,500 (or) 75 : 25 (or) 3 : 1

II. Calculation of Revenue Profit

Revenue Profit Rs. 60,000

Holding Company $60{,}000 \times \frac{3}{4} = Rs. 45{,}000$

Minority Shareholder $60{,}000 \times \frac{1}{4} = Rs. 15{,}000$

III. Calculation of Capital Profit

Capital Profit Rs. 30,000

Holding Company $30{,}000 \times \frac{3}{4} = Rs. 22{,}500$

Minority Shareholder $30{,}000 \times \frac{1}{4} = Rs. 7{,}500$

IV. Calculation of Good will / Capital Reserve

Paid-up value of share purchased		Rs.	75,000
Add :	Capital Profit		22,500
			97,500
Less :	Price paid for the purchase of Investment		75,000
	Capital Reserve (+)		22,500

V. Calculation of Minority Interest

Paid-up value of shares held		Rs.	25,000
Add :	Capital Profit		7,500
	Revenue Profit		15,000
		Total	47,500

VI. Calculation of Stock Reserve ad Unrealised Profit

$$Stock\ Reserve = Rs. 25{,}000 \times \frac{20}{100} = Rs. 5{,}000$$

CONSOLIDATED BALANCE SHEET

as on 31st December 2019

Liabilities			Rs.	Assets			Rs.
Share Capital (Rs. 10 each)			5,00,000	Fixed Assets :	H -	4,00,000	
Capital Reserve			22,500		S -	60,000	4,60,000
Reserves			60,000				
Profit & Loss a/c				Stock :	H -	3,00,000	
	H -	2,00,000			S -	1,20,000	
	S -	45,000				4,20,000	
		2,45,000		(-) Stock Reserve		5,000	4,15,000
(-) Unrealised Profit		5,000	2,40,000				
Creditors :	H -	90,000		Debtors :	H -	75,000	
	S -	60,000	1,50,000		S -	70,000	1,45,000
Minority Interest			47,500				
			10,20,000				10,20,000

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