

INTERNAL RECONSTRUCTION ACCOUNTING

SAI KRIPA INTERNAL RECONSTRUCTION ACCOUNTING

By: - CA RAKESH KALRA

Topics to be covered

- Meaning & terms
- Journal entries for reconstruction
- Surrender of shares Scheme

TOPIC – 1

MEANING & TERMS

Internal Reconstruction Accounting

Internal reconstruction is a process of making changes in the current balance sheet of a company; changes can be made by making alteration in share capital, payment of liabilities, writing of past losses, etc. Internal Reconstruction scheme is governed by the Indian companies Act-2013, according to Indian Companies Act-2013, a company has to call for the meeting of Preference share holders and equity share holders for approving them the scheme of reconstruction

Alteration of Share Capital

Alteration of share capital means where the face value of share change for the benefit of Entity and share holder. According to section – 94 of Indian Companies Act -2013, Share capital can be altered. Each share has paid up value and face value. Whenever face value of share capital is altered, it is called alteration of share capital.

Journal Entry

For Subdivision of Share

Equity/Preference Share Capital A/C	Dr	(Old Face value)
To Equity/Preference Share Capital A/C		(New Face value)

Stock Capital

Stock mean group of shares, which are fully paid up and consolidated into one unit. Stock is created for the stake of easy handling of share. Stock capital is shown under the head share capital in balance sheet. Stock can be again converted into shares if required.

Journal Entry

For Conversion of Share into stock

Equity/Preference Share Capital A/C	Dr	(Old Paid -up value)
To Equity/Preference Stock Capital A/C		(New Paid -up value)

For Conversion of Stock into Share

Equity/Preference Stock Capital A/C	Dr	(Old Paid -up value)
To Equity/Preference Share Capital A/C		(New Paid -up value)

Reduction of Share Capital

Reduction of share capital means reducing the paid up share capital of company that leads to income of the company as share capital of company is reduced. Such income is recorded in Capital reconstruction account.

Journal Entry

For Reduction of Share Capital

Equity/Preference Stock Capital A/C	Dr
To Capital Reconstruction A/C	

INTERNAL RECONSTRUCTION ACCOUNTING

Capital reconstruction account

Capital reconstruction account is opened to record the income and expenses on reconstruction, it is also known as "Capital Reduction A/C" or "Reconstruction A/C".

TOPIC – 2

JOURNAL ENTRIES FOR RECONSTRUCTION

Following Journal entries need to be understood in this chapter such as:

For Reducing Value of Assets

Capital reconstruction A/C	Dr
To Assets A/C	

For Increasing Value of Assets

Assets A/C	Dr
To Capital reconstruction A/C	

For Reducing Value of Liability

Liability A/C	Dr
To Capital reconstruction A/C	

For Increasing Value of Assets

Capital reconstruction A/C	Dr
To Liability A/C	

For Writing of the Fictitious Assets

Capital reconstruction A/C	Dr
To Profit and loss A/C	
To Preliminary Exp A/C	
To Underwriter Commission A/C	

Note: Following are the Fictitious Assets which need to be write off even if question is silent for same, such as:

- Profit & Loss A/C
- Preliminary Expenses
- Underwriter Commission
- Discount of issue of debentures
- Other deferred revenue expenses
- Goodwill

For Payment of reconstruction Expenses

Capital reconstruction A/C	Dr
To Bank A/C	

For Payment of Contingent Liability

Capital reconstruction A/C	Dr
To Bank A/C	

For Cancellation of Contingent Liability

=====No Entry=====

INTERNAL RECONSTRUCTION ACCOUNTING

For Fresh Issue of Share Capital

Bank A/C Dr
 To Share Capital A/C

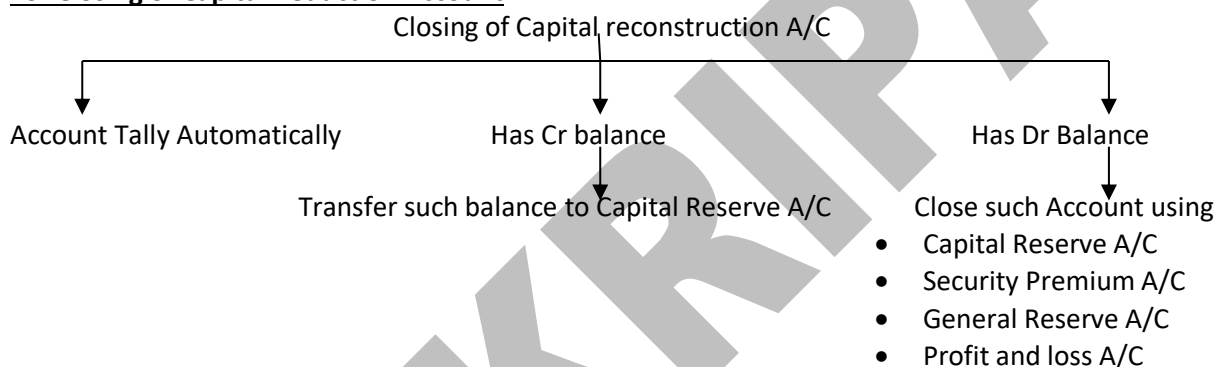
For Sale of any Assets

Bank A/C Dr
 Capital reconstruction A/C Dr (Loss on sale)
 To Assets A/C
 To Capital reconstruction A/C (Profit on sale)

For Reduction of Paid-up value and face value of share together

Equity/Preference Share Capital A/C Dr (Old Paid -up value)
 To Equity/Preference Stock Capital A/C (New Paid -up value)
 To Capital reconstruction A/C

For Closing of Capital Reduction Account



Example – 1

Surya limited has 10,000 shares of Rs 10 each at Rs 8 paid up as share capital. Now Surya limited has decided to sub divided its share into 20,000 shares of Rs 5 each at Rs 4 paid up.

Pass journal entry

Solution

Journal Entries

S.No	Particulars	Dr	Cr

Example – 2

C Ltd. had Rs 500,000 authorized capitals on 31-12-1996 divided into shares of Rs 100 each out of which 4,000 shares were issued and fully paid up In June 1997 the Company decided to converted the issued shares into stock. But in June, 1998 the Company reconverted the stock into shares of Rs 10 each fully paid up

Solution

INTERNAL RECONSTRUCTION ACCOUNTING

Journal Entries

S.No	Particulars	Dr	Cr

Example – 3

On 31-12-1996 B Ltd had 20,000 Rs 10 Equity Shares as authorized capital and the shares were all issued on which Rs 8 was paid up. In June 1997 the company in general meeting decided to sub divided each share into two shares of Rs 5 with Rs 4 paid up In June. 1998 the company in general meeting resolved to consolidate 20 shares of Rs 5 Rs 4 per share paid up into one share of Rs 100 each Rs 80 paid up

Pass entries for the above case.

Solution

Journal Entries

Date	Particulars	Dr	Cr

Example – 4

The paid up capital of Ria limited amounted to Rs 250,000 consisting 25000 equity shares of Rs 10 each. Due to losses incurred by the company continuously, the director of the company prepared a scheme for reconstruction which was dully approved by the court. The terms are as follows:

- I. In lieu of their present holdings, the shareholders are to receive:
 - a) Fully paid equity shares equal to 2/5th of their holding
 - b) 5% preference shares fully paid-up to the extent of 20% of the above new equity shares

- c) 3,000 6% second debentures of Rs 10 each
- II. An issue of 2,500 5% first debentures of Rs 10 each was made and fully subscribed in cash.
- III. The assets were reduced as follows
 - a) Goodwill from Rs 150,000 to Rs 75,000
 - b) Machinery from Rs 50,000 to 737,500
 - c) Leasehold premises from Rs 75,000 to Rs 62,500

Solution

Journal Entries			
S.No	Particulars	Dr	Cr

The following is the Balance Sheet of Rocky Ltd as at March 31st 2002.

Fully paid equity shares of Rs 10 each
Capital Reserve
12% Debentures
Debenture Interest Outstanding
Trade Creditors
Directors' Remuneration Outstanding
Other Outstanding Expenses
Provisions

500

6

40

48

165

10

11

33

1,173

Goodwill
Land and Building
Plant and Machinery

Rs in Lacs

15

184

286

INTERNAL RECONSTRUCTION ACCOUNTING

Furniture and Fixtures	41
Stock	142
Debtors	80
Cash at Bank	27
Discount on Issue of Debentures	8
Profit and Loss Account	390
	1,173

The following scheme of internal reconstruction was framed, approved by the court, all the concerned parties and implemented:

- I. All the equity shares be converted into the same number equity shares of Rs 2.50 P. Each.
- II. Directors agree to forgo their outstanding remuneration.
- III. The debenture holders also agree to forgo outstanding interest in return of their 12% debentures being converted into 13% debenture;
- IV. The existing shareholders agree to subscribe for cash, fully paid equity shares of Rs 2.50 P. each for Rs 125 Lacs.
- V. Trade creditors are given the option of either to accept fully paid equity shares of Rs 2.50 each for the amount due to them or to accept 80% of the amount due to them. Creditors for Rs 65 lacs accept equity shares whereas those for Rs 100 lacs accept Rs 80 lacs in cash in full settlement.
- VI. The assets are revalued as under:
 - a) Land and Building 230 Lacs
 - b) Plant and machinery 220 Lacs
 - c) Stock 120 Lacs
 - d) Debtor 76 Lacs

Pass Journal entries, prepare capital reconstruction account and Prepare balance sheet after reconstruction.

INTERNAL RECONSTRUCTION ACCOUNTING

Example – 6

Following is the Balance Sheet of ABC Ltd. as at 31st March. 2007:

Liabilities	Rs	Assets	Rs
Share Capital:		Plant and Machinery	9,00,000
2,00,000 Equity Shares of		Furniture and Fixtures	2,50,000
Rs 10 each fully paid up	20,00,000	Patents and Copyrights	70,000
6,000 8% preference shares		Investments (at cost)	68,000
of Rs 100 each	6,00,000	(Market value Rs 55,000)	
9% Debentures	12,00,000	Stock	14,00,000
Bank overdraft	1,50,000	Sundry Debtors	14,39,000
Sundry Creditors	5,92,000	Cash and Bank Balance	10,000
		Profit and Loss	4,05,000
	<u>45,42,000</u>		<u>45,42,000</u>

The following scheme of reconstruction was finalised:

- Preference shareholders would give up 30% of their Capital in exchange for allotment of 11% Debentures to them.
- Debenture holders having charge on Plant and Machinery would accept plant and machinery in full settlement of their claim.
- Stock equal to Rs 500,000 in book value will be taken over by creditor in full and final settlement of their dues.
- Investment to be valued at market price and intangible assets considered nil.
- Company issued 11% debentures for Rs 300,000 for their working capital requirement and payment of bank overdraft.

Pass Journal entries; prepare capital reconstruction account and Prepare balance sheet after reconstruction.

Example – 7

The Balance Sheet of Y Limited as on 31st March, 2003 was as follows:

Liabilities	Amount	Assets	Amount (Rs)
5,00,000 Equity Shares of	50,00,000	Goodwill	10,00,000
Rs 10 each fully paid		Patent	5,00,000
9% 20,000 Preference shares of	20,00,000	Land and Building	30,00,000
Rs 100 each fully paid		Plant and machinery	10,00,000
10% First debentures	6,00,000	Furniture and	
10% Second debentures	10,00,000	Fixtures	200,000
Debentures interest outstanding	1,60,000	Computers	3,00,000
Trade creditors	5,00,000	Trade Investment	5,00,000
Directors loan	1,00,000	Debtors	5,00,000
Bank O/D	1,00,000	Stock	10,00,000
Outstanding liabilities	40,000	Discount on issue of	1,00,000
Provision for Tax	1,00,000	debentures	
		Profit and Loss	15,00,000
		Account (Loss)	
	<u>96,00,000</u>		<u>96,00,000</u>

Note preference dividend is in arrears for last three years

A holds 10% first debentures for Rs 100,000 and 10% second debentures for Rs 6,00,000. He is also creditors for Rs 1,00,000.

B holds 10% first debentures for Rs 200,000 and 10% second debentures for Rs 400,000 and is also creditors for Rs 50,000.

INTERNAL RECONSTRUCTION ACCOUNTING

The following scheme of reconstruction has been agreed upon and duly approved by the court

- i. All the equity shares are converted into fully paid equity shares of Rs 5 each.
- ii. The preference shares are reduced to Rs 50 each and the preference shareholders agree to forego their arrears of preference dividends in consideration of which 9% preference shares are to be converted into 10% preference shares.
- iii. Mr. 'A' is to cancel Rs 600,000 of his total debt including interest on debentures and to pay Rs 100,000 to the company and to receive new 12% debentures for the Balance amount.
- iv. Mr. 'B' is to cancel Rs 300,000 of his total debt including interest on debentures and to accept new 12% debentures for the balance amount.
- v. Trade creditors (other than A and B) agreed to forego 50% of their claim.
- vi. Directors to accept settlement of their loans as to 60% thereof by allotment of equity shares and balance being waived
- vii. There were capital commitments totalling Rs 300,000. These contracts are to be cancelled on payment of 5% of the contract price as a penalty.
- viii. The Directors refund Rs 110,000 of the fees previously received by them.
- ix. Reconstruction expenses paid Rs 10,000.
- x. The taxation liability of a company was finalised for Rs 80,000 and paid immediately.
- xi. The Assets are revalued as under:

▪ Land and Building	2800,000
▪ Plant and Machinery	400,000
▪ Stock	700,000
▪ Debtor	300,000
▪ Computer	180,000
▪ Furniture and fixtures	100,000
▪ Trade investment	400,000

Pass journal entries for all the above mentioned transactions including amounts to be written off of Goodwill, Patents, Loss in Profit & Loss Account and Discount on issue of debentures Prepare Bank Account and working of allocation of Interest on Debentures between A and B.

Example – 8

M/s Platinum Limited has decided to reconstruct the Balance Sheet since it has accumulated huge losses. The following is the Balance Sheet of the company as on 31st March, 2012 before reconstruction:

Balance Sheet

Liabilities	Amount	Assets	Amount
Equity share Capital		Goodwill	2200,000
50,000 shares of Rs 50 each	2500,000	Land & Building	4270,000
Equity share Capital		Machinery	850,000
100,000 shares of Rs 40 each	4000,000	Computers	520,000
Capital Reserve	500,000	Stock	320,000
8% Debentures of Rs 100 each	400,000	Trade Debtors	1090,000
12% Debentures of Rs 100 each	600,000	Cash at Bank	268,000
Trade Creditors	1240,000	Profit & Loss Account	782,000
Outstanding Expenses	1060,000		
	103,00,000		103,00,000

Following is the interest of Mr. Shiv and Mr. Ganesh in M/s Platinum Limited:

	Mr. Shiv	Mr. Ganesh
8% Debentures	300,000	100,000
12% Debentures	400,000	200,000

INTERNAL RECONSTRUCTION ACCOUNTING

Total 700,000 Total 300,000

The following scheme of internal reconstruction was framed and implemented, as approved by the court and concerned parties

- i. Uncalled capital is to be called up in fully and then all the shares to be converted into Equity Shares of Rs40 each.
- ii. The existing shareholders agree to subscribe in cash, fully paid up equity shares of Rs40 each for Rs 1250,000
- iii. Trade Creditors are given option of either to accept fully paid equity shares of Rs 40 each for the amount due to them or to accept 70% of the amount due to them in cash in full settlement of their claim. Trade Creditors for Rs 750,000 accept equity shares and rest of them opted for cash towards full and final settlement of their claim.
- iv. Mr. Shiv agrees to cancel debenture amounting to Rs 200,000 out of total debentures due to him and agree to accept 15% Debentures for the balance amount due. He also agrees to subscribe further 15% Debentures in cash amounting to Rs 100,000.
- v. Mr Ganesh agrees to cancel debenture amounting to Rs 50,000 out of total debentures due to him and agree to accept 15% Debentures for the balance amount due.
- vi. Land & Building to be revalued at Rs 5184,000, Machinery at 720,000, Computers at Rs 400,000, Stock at Rs 350,000 and Trade Debtors at 10% less to as they are appearing in Balance Sheet as above.
- vii. Outstanding Expenses are fully paid in cash.
- viii. Goodwill and Profit and loss account is to be written off and balance if any in capital reduction account is to be transfer to capital reserve account.

Pass Journal entries; prepare capital reconstruction account and Prepare balance sheet after reconstruction.

Example – 9

The following Is the Balance Sheet of Weak Ltd. as on 31.3.2006:

Balance Sheet

Liabilities	Amount	Assets	Amount
Equity share Capital Rs 100 each	1,00,00,000	Fixed assets	1,25,00,000
12% cumulative preference shares of Rs 100 each	50,00,000	Investments (market value Rs 9.50.000)	10,00,000
10% Debentures of Rs 100 each	40,00,000	Current assets	1,00,00,000
Trade Creditors	50,00,000	Profit & loss	400,000
Provision for taxation	100,000	Preliminary expenses	200,000
	2,41,00,000		2,41,00,000

The following scheme of reorganisation is sanctioned:

- i. All the existing equity shares are reduced to Rs 40 each.
- ii. All preference shares are reduced to Rs 60 each.
- iii. The rate of interest on debentures is increased to 12%. The debenture holders surrender their existing debentures of Rs 100 each and exchange the same for fresh debentures of Rs 70 each for every debenture held by them.
- iv. One of the creditors of the company to whom the company owes Rs 20,00,000 decides to forego 40% of his claim. He is allotted 30,000 equity shares of Rs 40 each in full satisfaction of his claim
- v. The taxation liability of the company is settled at Rs 1.50.000.
- vi. Fixed assets are to be written down by 30%.

INTERNAL RECONSTRUCTION ACCOUNTING

- vii. Current assets are to be revalued at Rs 4500,000
- viii. Investments to be brought to their market value
- ix. It is decided to write off the fictitious assets.

Pass Journal entries and show the Balance Sheet of the company after giving effect to the above

TOPIC – 3

SURRENDER OF SHARES SCHEME

At the time of reconstruction sometimes equity share holder or preference share holders surrender their shares to the companies in such case following journal entries were passed:

Journal Entries

For Surrender of Share

Equity/Preference share capital A/C Dr
 To Equity/Preference share surrender A/C

For change of surrender share category

Equity share surrender A/C Dr
 To Preference share surrender A/C

For any surrender share given to liability

Liability A/C Dr
 To Capital reduction A/C
 (Being liability cancelled)

Equity/Preference share surrender A/C Dr
 To Equity/Preference share capital A/C

For Cancellation for surrender share

Equity/Preference share surrender A/C Dr
 To Capital reduction A/C

Example – 10

Balance Sheet of R Ltd as on 31-12-2000.

Liabilities	Amount	Assets	Amount
<i>Authorized Issued and Subscribed Capita/</i>		Goodwill	50.000
30,000 equity shares of Rs 10	3,00.000	Plant	3.00.000
2,000 8% Cumulative Preference		Loose Tools	10.000
Share of Rs of 100 each fully paid	200,000	Debtors	2.50.000
Share Premium	90,000	Stocks	1.50,000
Unsecured Loan		Cash	10,000
(From Director)	50.000	Bank	35.000
Sundry Creditors	3.00,000	Preliminary	5.000
Outstanding Exnses (including Directors remuneration - 20.000)	70.000	P & L A/c	2.00.000
	10.10,000		10.10.000

Note: Dividend on cumulative preference shares are in arrear for last three years.

The Following scheme of reconstruction was approved by court and dully implemented.

- i. Equity Share to be converted into 150,000 shares of Rs 2 each.

INTERNAL RECONSTRUCTION ACCOUNTING

- ii. Equity share holder to surrender to the company 90% of their holding
- iii. Preference share agree to forego their arrear dividend and to receive 9% preference share in place of 8% preference shares.
- iv. Sundry creditors agree to reduce their claim by 1/5 in consideration of their getting shares of Rs 35,000 out of the surrendered equity shares.
- v. Directors agree to forego loan and remuneration.
- vi. Surrendered shares not otherwise utilized to be cancelled
- vii. Assets to be reduced as under

• Goodwill by	Rs 50,000
• Plant by	Rs 40,000
• Tools by	Rs 8,000
• Sundry Debtors by	Rs 15,000
• Stock by	Rs 20,000
- viii. Any surplus after meeting the losses should be utilized in writing down the plant further.
- ix. Expenses of reconstruction amounted to Rs 10,000
- x. Further 50,000 equity shares were issued to the existing members for increasing the working capital the issue was fully subscribed ' and paid up.

You are required to pass the journal entries for giving effect to the above arrangement and also to draw up the resultant balance sheet of the company.

Example – 11

The summarised balance sheet of R G Ltd. as on 30-6-1998 was as follows:

Liabilities	Rs	Assets	Rs
Authorised and Issued Capital: 10,000 Shares of Rs 100 each	10,00,000	Land, Building & Machine	14.50.000
6% Debentures	14,00,000	Stock-in-trade	1.20.000
Accrued interest on the Above	70,000	Debtors	80.000
Trade Creditors	4,65,000	Investments	1.65.000
		Cash	1.05.000
		Profit and Loss Account	10.15.000
	29.35.000		29.35.000

The following scheme of reorganisation was approved and confirmed by the court:

- i. Each share shall be sub-divided into twenty fully paid equity shares of Rs 5 each.
- ii. After sub-division, each shareholder shall surrender to the company 95% of his holding, for the purpose of re-issue to debenture holders and creditors so far as required and otherwise for cancellation.
- iii. Of those surrendered. 46,000 shares of Rs 5 each shall be converted into 10% preference shares of Rs 5 each fully paid.
- iv. Debenture holder's total claim to be reduced to Rs 230,000. This will be satisfied by the issue to them 46,000, 10% cumulative preference shares of Rs 5 each fully paid.
- v. The claims of unsecured creditors shall be reduced by 80% and the balance shall be satisfied by allotting them equity shares of Rs 5 each fully paid from the shares surrendered
- vi. Shares surrendered and not issued shall be cancelled
- vii. Fixed Assets revalued at Rs 450,000

Pass the necessary journal entries for above transactions.

INTERNAL RECONSTRUCTION ACCOUNTING

Example – 12

Balance Sheet as at 31st March. 1993:

Liabilities	Rs	Assets	Rs
200,000 equity shares of Rs 10 each. Rs 5 paid	10.00.000	Fixed Assets	11.40.000
6.000 8% Preference Shares of Rs 100 each	6.00.000	Patents and Copynights	80.000
9% Debentures .	6.00.000	Investment at cost (Market value Rs 55.000)	65.000
Interest accrued on debentures	1.08.000	Current Assets:	
Bank of India	1.50.000	Stock	4.00.000
Interest accrued on Bank Overdraft	55.000	Debtors	4.39.000
Current Liabilities: Bank			10.000
Creditors	' 69.000	Profit & Loss	1,08.000
	25.42.000		25.42.000

Preference dividend is in arrear for one year.

- i. Preference shareholders to give up their claims, inclusive of dividends, to the extent: of 30% and desire to be paid of
 - ii. Debenture-holders agree to give up their claims to interest in consideration being enhanced to 12%
 - iii. Bank agrees to give up 50% of its interest outstanding in consideration of its being paid off at once
 - iv. Creditors would like to grant a discount of 6% if they are paid immediately
 - v. Balance of Profit & Loss Account, patent, copyright and Debtors of Rs 30,000 to be written off
 - vi. Fixed Assets to be written down by Rs 34,000
 - vii. Investments are to reflect their market value.
 - viii. To the extent not specifically stated, equity shareholders suffer on reduction of their rights
- Cost of reconstruction is Rs 3,350.

Draft journal entries in the books of the company assuming that the scheme has been put through fully with the equity shareholders bringing in necessary cash to pay off the parties and to leave a balance of Rs 30,000 and prepare the Balance Sheet after reconstruction.

Example – 13

The Balance Sheet of Revive limited as on 31st March 1999 was as follows:

Balance Sheet			
Authorized and subscribed capital:		Fixed Assets:	
10.000 Equity shares of Rs 100 each fully paid	1000,000	Machineries	100.000
Unsecured Loans:		Current assets:	
12% Debentures'	200.000	Stock	320.000
Accrued interest	24.000	Debtors	270.000
Current liabilities-creditors	72,000	Bank	30.000
Provision for income tax	24.000	Profit and Loss A/c	600.000
	13.20.000		13.20.000

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

- i. Each share to be sub-divided into ten fully paid up equity shares of Rs 10 each.

INTERNAL RECONSTRUCTION ACCOUNTING

- ii. After sub-division, each shareholder shall surrender to the company 50% of his holding, for the purpose of re-issue to debenture holders and creditors as necessary.
- iii. Out of shares surrendered. 10,000 shares of Rs 10 each shall be converted into 12% preference shares of Rs 10 each fully paid up.
- iv. The claims of the debenture-holders shall be reduced by 75 per cent. In consideration of the reduction, the debenture holders shall receive preference shares of Rs 100,000 which are converted out of shares surrendered.
- v. Creditors claim shall be reduced to 50 percent it is to be settled by the issue of equity shares of Rs 10 each out of shares surrendered.
- vi. Balance of profit and loss account to be written off.
- vii. The shares surrendered and not re-issued shall be cancelled.

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

Example – 14

S.P. Construction Co. finds itself in financial difficulty The following is the balance sheet on 31st December, 1999.

Liabilities	Rs	Assets	Rs
Share Capital		Land	1.56.000
20.000 Equity Shares of Rs10 each fully paid	2.00.000	Building (Net)	27.246
5% cum. Pref Shares of Rs 10 each fully paid	70.000	Equipment	10.754
8% Debentures	80.000	Goodwill	60.000
Loan from Directors	16.000	Investments	
Trade Creditors	96.247	(Quoted) in shares	27.000
Bank Overdrafts	36.713	Stock	1.20.247
Interest Payable on Debentures	12.800	Sundry Debtors	70.692
	<u>5.11.760</u>	Profit & Loss A/c	39.821
			<u>5.11.760</u>

The authorized capital of the company is 20.000 Equity Shares of Rs 10 each and 10,000 5% Cum. Preference Shares of Rs 10 each.

During a meeting of shareholders and directors, it was decided to carry out a scheme of internal reconstruction. The following scheme has been agreed:

- i. The equity shareholders are to accept reduction of Rs 7.50 per share. And each equity share is to be redesignated as a share of Rs 2.50 each.
- ii. The equity shareholders are to subscribe for a new share on the basis of 1 for 1 at a price of Rs 3 per share.
- iii. The existing 7,000 Preference Shares are to be exchanged for a new issue of 3,500 8% Cumulative Preference Shares of Rs 10 each and 14,000 Equity Shares of Rs 2.50 each.
- iv. The Debenture holders are to accept 2,000 Equity Shares of Rs 2.50 each in lieu of interest payable.
The interest rate is to be increased to 9.5%. Further Rs 9,000 of this 9.5% Debentures are to be issued and taken up by the existing holders at Rs 90 for Rs 100.
- v. Rs 6,000 of directors' Loan is to be debited. The balance is to be fully settled by issue of 1,000 Equity Shares of Rs 2.50 each.
- vi. Goodwill and Profit & loss Balance to be write off.
- vii. The Investment in share are sold at its current market value of Rs 60,000
- viii. The bank overdraft is to be repaid
- ix. Rs 46,000 to be paid to trade creditor now and balance in quarterly intervals
- x. 10% debtor to be written off

INTERNAL RECONSTRUCTION ACCOUNTING

- xi. The remaining assets were professionally valued and should be included in the books of account as follows:
- | | |
|-----------|-----------|
| Land | Rs 90,000 |
| Building | Rs 80,000 |
| Equipment | Rs 10,000 |
| Stock | Rs 50,000 |
- xii. It is expected that due to changed condition and new management operating profit will be earned at the rate of Rs 50,000 p.a after depreciation but before interest and tax

Due to losses brought forward it is unlikely that any lax liability will arise until **2002**.

You are required to show the necessary journal entries to effect the reconstruction scheme; prepare the balance sheet of the company immediately after the reconstruction.

Example – 15

The Balance Sheet of Gomi limited as on 31st December 2008 was as follows:

Balance Sheet

Liabilities	Amount	Assets	Amount
3,000 Cumulative Preference shares of Rs 100 each fully paid up	300,000	Fixed Assets (including goodwill of Rs 1.00,000)	10,80,000
7.500 Equity share of Rs100 each fully paid up	750,000	Investments	20,000
Securities Premium	12,000	Stock	200,000
-Preference Shares	80,000	Debtors	154,500
General Reserve	375,000	Bank	62,500
Trade Creditors	1517,000		1517,000

Contingent liability: Preference Dividends in arrears Rs 66,000.

The Board of Directors of the Company decided upon the following scheme of reconstructions:

- i. The preference shares are to be converted into 13% unsecured debentures of Rs 100 each in regard to 80% of the dues (including arrears of dividends) and for the balance equity shares of Rs 50 paid up would be issued. The authorized capital of the company permitted the issue of additional shares.
- ii. Equity shares would be reduced to share of Rs50 each paid up.
- iii. All equity holders agree to pay the balance in cash.
- iv. Goodwill has lost its value and is to be written off fully. Investments are to reflect their market value of Rs 30,000. Obsolete items in stock of Rs 50,000 are to be written off. Bad debts to the extent of 5% of the total debtors would be provided for. Fixed assets to be written down by Rs 150,000

The scheme was duly approved and put into effect.

The company carried on trading for six months and after writing off depreciation at 20% p.a. on the revised value of fixed assets, made a net profit of Rs 80,000. The half-yearly working resulted in an increase of Sundry Debtors by Rs 60,000. Stock by Rs 80,000 and cash by Rs 40,000

Show the journal entries (without narration) necessary in the Company's books to give effect to the scheme and draw the Balance sheet as at 30th June, 2009.