CHAPTER-6

ACCOUNTING FOR SPECIAL TRANSACTIONS

UNIT-1

BILLS OF EXCHANGE AND PROMISORY NOTES

BILLS OF EXCHANGE:

* A bill of exchange has been defined as an "instrument in writing containing an unconditional order signed by the maker directing certain person to pay a certain sum of money only to or to the order of a certain person or to the bearer of the instrument"

PARTIES:

* Drawer - the party which makes the order.
* Drawee / acceptor - the party which accepts the order.
* Payee - the party to whom the amount has to be paid.

[NOTE: Drawer & the payee can be the same]

FOREIGN BILL OF EXCHANGE:

* Bill of exchange drawn for foreign trade operations is known as foreign bill of exchange.
* It is drawn in one country and is payable in another.
* It is generally drawn up in triplicate wherein each copy is sent by separate post so that at least one copy reaches the intended party.
* Payment will be made only on one of the copies and when such payment is made the other copies become useless.
* Section 12 of the Negotiable Instrument Act provides that all instruments, which are not inland instrument, are foreign.

PROMISSORY NOTES:

* A promissory note is an instrument in writing, not being a bank note or currency note containing an unconditional undertaking signed by the maker to pay a

certain sum of money only to or to the order of a certain person.

* Under section 31(2) of the Reserve Bank Act a promissory note cannot be made payable to bearer.

DIFFERENCE BETWEEN BILL OF EXCHANGE AND PROMISSORY NOTE :

BILL OF EXCHANGE	PROMISSORY NOTE
* It contains an unconditional order to pay.	* It contains only a promise to pay certain sum of money.
* There are 3 parties. (Drawer, drawee & payee)	* There are 2 parties. (Maker & payee)
* A bill is paid by acceptor.	* A promissory note is paid by maker.
* A bill is drawn by Creditor.	* A promissory note is made by debtor.

* The drawer and payee may be same person in case of bill of exchange	* Maker and payee cannot be same person in case of promissory note.
* The liability of drawer is secondary & conditional.	* The liability of a maker is primary & absolute.
* It can be accepted conditionally.	* It cannot be made conditionally.
* Notice of dishonour must be given.	* Notice of dishonour is not required.
* In case of dishonour, a bill of exchange must be noted & protested.	* In case of dishonour, noting & protest is not required.

NOTING CHARGES:

* It is necessary that the fact of dishonour and the causes of dishonour should be established.

* If the acceptor can prove that the bill was not properly presented to him for payment, he may escape liability.
* Therefore, if there is dishonour, or fear of dishonour, the bill will be given to a public official known as "Notary Public".
* These officials present the bill for payment and if the money is received, they will hand over the money to the original party.
* But, if the bill is dishonoured they will note the fact of dishonour, with the reasons and give the bill back to their client.
* For this service they charge a small fee.
* This fee is known as noting charges.
* The amount of noting charges is recoverable from the party which is responsible for dishonour.

RENEWAL OF BILL:

* Renewal of bill happens when acceptor is unable to pay the amount and he himself moves that he should be given extension of

time and agrees to pay the amount with interest.

* If this happen, entries should be passed for
  i) cancellation of the old bill.
  ii) receipt of the new bill with interest.

RETIREMENT OF BILL :

* Retirement of bill happens when the acceptor has spare funds much before the maturity date of the bill of exchange.
* Acceptor approches payee of the bill of exchange & asks him whether the payee is prepared to accept cash before the maturity date with certain rebate or interest or discount.
* The rebate becomes the income of the acceptor and expenses of the payee.
* It is a consideration of a premature payment.

INSOLVENCY:

* Insolvency of a person means that he is unable to pay his liabilities.

* If this happens, entries should be passed for:
  i) Cancellation of the bill.
  ii) Recoverable amount from his estate.
  iii) Bad debts.

ACCOMMODATION BILLS:

* The mechanism of bill can be utilized to raise finance also.
* When bills are used for such purpose, they are known as accomodation bill.
* If this happens, entries should be passed for:
  i) Ordinary bills.
  ii) Sending the remittance.

JOURNAL ENTRIES:

ENTRIES	IN THE BOOKS OF X (DRAWER)	IN THE BOOKS OF Y (DRAWEE)
X sold goods to Y	Y a/c Dr. To sales a/c	Purchase a/c Dr. To X a/c
Drawee accepted the bill	Bills receivable a/c Dr. To Y a/c	X a/c Dr. To bills payable a/c

X hold the bill till maturity:

Met or honour -ed	Cash a/c Dr. To bills receivable a/c	Bills payable a/c Dr To cash a/c
Dishonoured	Y a/c Dr To bills receivable a/c	Bills payable a/c Dr. To X a/c

Discounted the bill of exchange with the bank:

Discounted with bank	Bank a/c Dr. Discount a/c Dr. To bills receivable a/c	-
Met or honore -d	-	Bills payable a/c Dr. To cash a/c
Dishonoured	Y a/c Dr. To bank a/c	Bills payable a/c Dr. To X a/c

Endorsed the bill to Z:

Endorsed the bill	Z a/c Dr. To bills receivable -a/c	-

Met or honoured	-	Bills payable a/c Dr. To cash a/c
Dishonoured	Y a/c Dr. To Z a/c	Bills payable a/c Dr. To X a/c
Renewal of old bill:		
Cancellation of old bill.	Y a/c Dr. To bills receivable a/c	Bills payable a/c Dr. To x a/c
Receipt of new bill	Bills receivable a/c Dr To Y a/c	X a/c Dr. To bills payable a/c
Cash / interest paid immediately	Y a/c Dr. To interest a/c Cash a/c Dr. Y a/c	Interest a/c Dr. To X a/c X a/c Dr. To cash a/c
Retirement of bill:		
Retirement of bill	Bank a/c Dr. Rebate a/c Dr. To bills receivable a/c	Bills payable a/c Dr. To rebate a/c To bank a/c.

INSOLVENCY:

Cancellation of bill	Y a/c Dr. To bills receivable a/c	Bills payable a/c Dr. To X a/c
Recoverable amount from his estate	Bank a/c Dr. To Y a/c	X a/c Dr. To bank a/c
Bad debts.	Bad debts a/c Dr. To Y a/c	X a/c Dr. To deficiency a/c

ACCOMODATION BILLS:

Sending the remmittance	Y a/c Dr. To cash a/c To discount a/c	Cash a/c Dr. Discount a/c Dr. To X a/c

NOTING CHARGES:

Hold till maturity	Y a/c Dr. To bills receivable a/c To bank a/c	Bills payable a/c Dr. Noting charges a/c Dr. To X a/c

Discounted with bank.	Y a/c Dr. To bank a/c	Bills payable Dr. Noting charges Dr. To X a/c
Endorsed the bill.	Y a/c To Z a/c	Bills payable a/c Dr. Noting charges a/c Dr To X a/c

BILLS OF COLLECTION:

* Sometimes, when a person receives a bills of exchange, he may send it to bank with instructions that the bill should be retained till maturity and should be realised on that date.
* This is known as bills sent for collection.

When bills sent for collection:

Bills for collection a/c Dr.
To bills receivable a/c

When the amount is realised:

Bank a/c Dr.
To bills for collection a/c

When the amount is not honoured:

Y a/c Dr.

To bills for collection a/c

CHAPTER-7

PREPARATION OF FINAL ACCOUNTS

OF SOLE PROPRIETORS.

UNIT-1

FINAL ACCOUNTS OF NON-

MANUFACTURING ENTITIES.

NON-MANUFACTURING ENTITIES:

* Non-manufacturing entities do not process the goods purchased & sell them in its original form.
* To ascertain the final outcome of the business i.e., the income & financial position, they prepare financial statements at the end of the year.

FINANCIAL STATEMENTS:

* Financial statements are the systematically organised summary of all the ledger account heads presented in such a manner that it gives detailed information about the financial position & the performance of the enterprise.

FINANCIAL STATEMENTS OF NON MANUFACTURING ENTITIES:

1, Income statement.

* Trading account - Gross profit or gross loss.
* Profit & loss account - Net profit or net loss.

2, Position statement.

* Balance sheet - Position of assets & liabilities.

DIFFERENCE BETWEEN INCOME STATEMENT & POSITION STATEMENT:

INCOME STATEMENT.	POSITION STATEMENT
* Profit or loss is disclosed.	* Assets & liabilities are exhibited.
* Income statement is sub-divided into: i, Trading account ii, Profit & loss account.	* Apart from balance sheet, cash flow statement, Value added statement, etc are also prepared which is not mandatory for non-corporate entities.

TRADING ACCOUNT:

* Gross profit is the difference between the selling price & the cost of the goods sold.

Sales - COGS = Gross profit / Gross loss.

Opening stock	xxx
(+) Purchases	xxx
(+) Direct expenses	xxx
	xxx
(-) Closing stock	(xxx)
Cost of goods sold.	xxx

* Trading account will be debited with all expenses incurred in bringing the goods to their present location & condition.
* If closing stock appears in the trial balance, the closing inventory is then not entered in the trading account, it is shown only in the balance sheet. This is because it has already been adjusted to arrive at cost of goods sold.

CLOSING ENTRIES:

1, Trading account	Dr.	xxx	
To opening stock a/c			xxx
To purchases a/c			xxx
To wages a/c			xxx
To direct expenses a/c			xxx
2, Sales a/c	Dr.	xxx	
Closing stock a/c		xxx	
To trading a/c			xxx.
3, Trading a/c	Dr.	xxx	
To Profit & loss a/c			xxx
4, Profit & loss a/c	Dr.	xxx	
To trading a/c			xxx.

PROFIT & LOSS ACCOUNT:

* All the expenses will be debited and all the incomes will be credited.

CLOSING ENTRIES:

1, Profit & loss a/c	Dr.	xxx	
To salaries a/c			xxx
To rent a/c			xxx
To interest a/c			xxx
To other expenses a/c			xxx
2, Discount received a/c	Dr.	xxx	
Bad debt recovered a/c	Dr.	xxx	
To profit & loss a/c			xxx
3. Profit & loss a/c	Dr.	xxx	
To capital a/c			xxx
4, Capital a/c	Dr.	xxx	
To profit & loss a/c			xxx

BALANCE SHEET:

* The balance sheet may be defined as "a statement which sets out the assets and liabilities of a firm or an institution as at a certain date.

ARRANGEMENTS OF ASSETS & LIABILITIES :

1, ASSETS :

a, Liquidity :

* Asset which can be converted into cash first, is presented first.

b, Permanence :

* Assets which are used for a long term and not meant to be sold are presented first.

2, LIABILITIES :

* Shown according to the urgency with which payment has to be made.

i, Capital
Long-term liabilities.
Short-term liabilities.

ii, Short-term liabilities.
Long-term liabilities.
Capital.

BAD DEBTS & PBDD :

PROFIT & LOSS ACCOUNT

PARTICULARS	₹	₹	PARTICULARS	₹
To bad debts a/c	xxx			
(+) Bad debts (New)	xxx			
	xxx			
(+) PBDD (New)	xxx			
	xxx			
(-) PBDD (old)	xxx	xxx		
To discount allowed	xxx			
(+) PDD (New)	xxx			
	xxx			
(-) PDD (old)	xxx	xxx		

BALANCE SHEET

LIABILITIES	₹	ASSETS	₹	₹
		Sundry debtors	xxx	
		(-) Bad debts (New)	xxx	
		(-) PBDD (New)	xxx	
		(-) PDD	xxx	xxx

POINTS TO REMEMBER:

* The amount of provision is required to be calculated after deducting the provision for bad debts from the total debtors. This is because ~~provision~~ provision for discount is created only on good debtors.
* The words 'outstanding', 'accrued', 'due' has the same meaning.
* In case of companies, the income tax payable is treated like other expenses.
* In case of soleproprietoship, income tax is treated as a personal expense.
* In case of partnership business, firm's tax liability is to be debited to profit & loss account but partner's tax liability are not to be borne by the firm.

COMMISSION BASED ON PROFIT:

1) Commission on net profit before charging such commission

$$= \text{Profit before commission} \times \frac{\text{Rate of commission}}{100}$$

2, Commission on net profit after charging such commission

$$= \text{Profit before commission} \times \frac{\text{Rate of commission}}{100 + \text{Rate of commission}}$$

OPENING ENTRY:

Assets a/c	Dr.	xxx	
To liabilities a/c			xxx
To capital a/c			xxx

PROVISIONS:

* Provision means "any amount written off or retained by way of providing for depreciation, renewal or diminution in the value of assets or retained by way of providing for any known liability of which the amount cannot be determined with substantial accuracy.
* A provision is a liability which can be measured only by using a substantial degree of estimation.

RESERVES:

* The portion of earnings, receipts or suplus of an enterprise (whether capital or revenue) appropriated by the management for a general or a specific purpose other than a provision for depreciation or diminution in the value of assets or for a known liability is known as reserves.

POINTS TO REMEMBER:

* Provisions are charge against profits while reserves is an appropriation of profits.
* Depreciation, increase in provision for doubtful debts, liability for tax are transferred to provisions.
* Retained profit for the year is transferred to reserves.
* Bad debts & proposed dividend are neither related to provisions nor reserves.

LIMITATIONS OF FINANCIAL STATEMENTS:

* Historical cost
* Intangible strengths & weakness.
* Perpetual continuity & periodical account.
* Different accounting policies.
* Management policies.

UNIT-2

FINAL ACCOUNTS OF MANUFACTURING ENTITIES.

MANUFACTURING ACCOUNT:

* The objective of preparing manufacturing account is to determine manufacturing costs of finished goods for assessing the cost of effectiveness of manufacturing activities.
* Direct manufacturing expenses are costs, other than material or wages, which are incurred for a specific product or saleable service.
* Indirect manufacturing expenses are also called Manufacturing overhead, production overhead, works overhead, etc.,
* Overhead is defined as total cost of indirect material, indirect wages & indirect expenses.
* By product is a secondary /subsidiary product.
* If the question does not state the total number of items sold, the quantity can be worked out by adding opening inventory & units manufactured and deducting closing inventory.
* Manufacturing account should have units & amount -column.

FORMAT OF A MANUFACTURING ACCOUNT:

MANUFACTURING ACCOUNT

PARTICULARS	UNITS	AMT	PARTICULARS	UNITS	AMT
To raw materials :			By by-products at		
Opening	XXX		net realisable value		XXX
(+) Purchase	XXX		By closing work-in		
(-) Closing	XXX	XXX	-process		XXX
To direct wages		XXX	By trading a/c		
To direct expenses			cost of goods		
Prime cost	XXX		manufactured		XXX
Freight inwards	XXX	XXX			
To factory overheads:					
Royalty	XXX				
Hire charges	XXX	XXX			
To indirect expenses:					
Repairs & maintanence	XXX				
Depreciation	XXX				
Factory cost	XXX				
Rent	XXX				
Lighting	XXX				
Coal & fuel & power	XXX	XXX			
To opening W.IP		XXX			
		XXX		XXX	

CHAPTER - 9

FINANCIAL STATEMENTS OF NOT - FOR - PROFIT ORGANISATIONS.

NON- PROFIT ORGANISATION:

* It is a legal accounting entity that is operated for the benefit of the society as a whole, rather than for the benefit of a sole proprietor or a group of partners or shareholders.
* The main motive behind the non-profitable organization is to render service to the society or the members of the organisation.

FINAL ACCOUNTS:

* Receipts & payments account.
* Income & expenditure account.
* Balance sheet.
  - i) Opening balance sheet.
  - ii) Closing balance sheet.

ADVANTAGES OF NPO:

* Tax exemption.

DISADVANTAGES OF NPO:

* No one can claim to be the owner of the NPO.
* Distribution & withdrawal of profits is prohibited.

RECIEPTS AND PAYMENTS ACCOUNT:

* Summary of the cash book without date column.
* It is not based on the accrual system of book keeping.
* This account is usually not a part of double entry system.
* It starts with opening cash & bank balances & also ends with their closing balances.
* All capital & revenue receipts are debited & capital & revenue payments are credited.
* Suitable only to the organisation, the results of which are to be exhibited, are simple & modest, involve no carry over from one period to the next and it has no assets, apart from cash balance & no liabilities.
* It is a elementary form of account.

LIMITATIONS:

* It does not truly represent the surplus or deficit, since it does not take into account the other important transactions like depreciation, outstanding or prepaid subscription, etc,...
* As it includes items relating to all periods, there is a need to construct an account which considers all the relevant revenue transactions for the current period.

INCOME AND EXPENDITURE ACCOUNT:

* It is equivalent to the profit & loss account.
* It is prepared by following accrual principle.
* It includes both cash and non-cash items of revenue nature.
* It is prepared by matching expenses against the revenue of that period concerned.
* Profit is termed as surplus - Excess of income over expenditure and loss is termed as deficit - Excess of expenditure over income.
* This surplus / deficit is taken to the balance sheet and is added / deducted respectively with the capital fund.

BALANCE SHEET:

* In not for profit organisations, the excess of total assets over total outside liabilities is known as capital fund.
* The capital fund represents the amount contributed by members, through legacies, special donations, entrance fees and accumulated surplus over the years.
* If however, members have not contributed any amount, it shall be termed as "Accumulated fund" instead of "capital fund".
* The surplus or deficit, if any, on the year's working as disclosed by the Income and Expenditure account is shown either as an addition to or deduction from the capital/ Accumulated Fund brought forward from the previous period respectively.
* Any amount raised for a special activity, e.g. on sale of match tickets, is deducted from the expenditure of that activity and net amount is shown in the income & expenditure account.

* Any receipt of capital nature shall not be shown as income but will be credited to the capital fund or special purpose fund eg: "Building fund" or if the receipts is on account of sale of a fixed asset, it shall be credited to the asset account.
* This system of showing the donation towards specific purposes separately is termed as fund accounting.
* Any expenditure for acquisition of a fixed asset will be capitalised, though the amount of annual depreciation shall be debited to revenue expenditure.
* The term "Fund" is strictly applicable to the amounts collected for a special purpose when these are invested, e.g. Scholarship Fund, Prize Fund etc.,
* In other case, when the amounts collected are not invested in securities or assets distinguishable from those belonging to the institution, the word "Account" is more appropriate, e.g., Building account, Tournament Account, etc.,

* If capital fund or accumulated fund in the begining of the year is not given, it is calculated by deducting liabilities from assets in the begining of year.

TREATMENT OF IMPORTANT ITEMS IN NOT-FOR-PROFIT ORGANISATION:

ITEM	MEANING	TREATMENT
DONATION	Gift in cash or kind from some person.	
a, SPECIFIC DONATION	Received for specific purpose like Building donation, library books donation, etc.,	Liabilities side of the balance sheet.
b, GENERAL DONATION	Not received for any specific purpose.	Credit side of income & expenditure a/c.
ENTRANCE FEES	Also known as admission fees.	Added to the capital fund ⊗

LEGACY	Amount received by an organisation as per the will of the person after the death of the person.	Added to the capital fund.
LIFE MEMBERSHIP FEES	Non recurring in nature.	Liabilities side of the balance sheet. [Added to the capital fund] ✗
ENDOWMENT FUND DONATION	It is a donation received & only income from that donation is to be used for certain specific purpose.	Liabilities side of the balance sheet. [All expenses are deducted and incomes are added]
SALE OF OLD NEWSPAPER & PERIODICALS	Revenue receipts.	Credit side of the income & expenditure account.
SALE OF OLD FIXED ASSETS	Capital receipts.	Profit or loss is shown in income & expenditure a/c

HONORARIUM	It is paid to someone for receiving any services from person who are not the employees of the NPO	Liabilities side of the balance sheet.

REGISTRATION OF EDUCATIONAL INSTITUTIONS:

* The educational institutions which are functioning in India are mostly registered as Societies under the Indian Societies Registration Act of 1860, in some of the states, where Public Trust Acts have been passed all the societies registered under the Indian Societies Registration Act, 1860 are required to be simultaneously registered under the Trust Act.
* Accordingly, in the state of Maharashtra, all the societies have simultaneously been registered under the Bombay Public Trust Act, 1950.

SOURCES OF FINANCE FOR RUNNING THE EDUCATIONAL INSTITUTION:

* Donation from public.
* Fees in the form of annual tuition fees, term fees, admission fees, laboratory fee, etc.;
* Grants received from the Government.

GOVERNMENT GRANT:

* The government grants are of four kinds namely Maintenance grant, Equipment grant, Building grant and such other grants as may be sanctioned by the Goverment from time to time.

CHAPTER - 7

REDEMPTION OF PREFERENCE SHARES

REDEMPTION OF PREFERENCE SHARES:

* Redemption is the process of repaying an obligation, at prearranged amount & timing.
* Maximum time limit for redemption = 20 years from the date of issue of redeemable shares.

PURPOSE OF ISSUING REDEEMABLE PREFERENCE SHARES:

* It is a proper way of raising finance in a dull primary market.
* A company may face difficulty in raising share capital, as its shares are not traded on the stock exchange. Potential investors, hesitate in putting money into shares that cannot easily be sold, may be encouraged to invest if the shares are redeemable by the company.
* The preference shares may be redeemed when there is a surplus of capital and the surplus funds cannot be utilised in the business for profitable use.
* No dividend is required to be paid, if there is loss or no profit, whereas, interest is payable on

debentures or loans even in case of loss.

CONDITIONS FOR REDEMPTION OF PREFERENCE SHARE CAPITAL [SECTION 55 OF COMPANIES ACT, 2013]:

* Redemption of preference share capital should be Authorised by AOA.
* Only fully paid preference share can be redeemed. If shares are not fully paid, they Should be converted into fully paid shares,
  - ↳ By way of making final call & receiving final call money.
  - ↳ By way of forfeiting the shares.

If information about both fully paid and partly paid preference shares is provided, then, it is presumed that only fully paid shares are to be redeemed & partly paid shares are left intact.

* Sources available for funding Face value of redemption:
  - ↳ Divisible profits [Profits which are otherwise available for dividend distribution]
    - i) Investment Allowance Reserve.
    - ii) General reserve.
    - iii) Profit & loss account
    - iv) Dividend Equilisation fund

↳ Proceeds of fresh issue of shares (PS/ES)

[Mostly issue ES because it is not temporary]

An amount equal to face value of redemption funded from divisible profit shall be transferred to CRR a/c [only for issue of fully paid bonus shares].

If question says, it is issued through fresh issue, then it should be done accordingly. If question stays silent, then, it should be understood that divisible of profits is made.

* Sources available for premium on redemption of preference share capital:

↳ Sec 133 IND AS not applicable:

i) Securities premium.

ii) Divisible profit.

↳ Sec 133 IND AS applicable:

i) Divisible profit

All the questions in this chapter have been solved on the basis that IND AS is applicable.

REASONS BEHIND CREATION OF CRR:

To maintain debt equity ratio, i.e., to protect the interest of creditors, debt equity ratio is maintained

L	B/S	A	
ESC	1L	Bank	1L + 1L + 2L
PSC	1L		
10% debentures	2L		

Capital
4L

Owner's capital	Outsider's money
⇓	⇓
Equity	Debt
2L :	2L
1 :	1

↳ Debt Equity Ratio

REASON FOR FRESH ISSUE OF EQUITY SHARE:

* When company wants permanent capital
* When company does not have sufficient divisible profit.
* When company does not have sufficient liquidity.

ADVANTAGES OF REDEMPTION OF PREFERENCE SHARES BY ISSUE OF FRESH EQUITY SHARES:

* No cash outflow of money.
* New equity shares may be valued at a premium.
* Shareholder's retain their equity interest.

DISADVANTAGES OF REDEMPTION OF PREFERENCE SHARES BY ISSUE OF FRESH EQUITY SHARES:

* There will be dilution of future earnings.
* Share-holding in the company is changed.

ADVANTAGES OF REDEMPTION OF PREFERENCE SHARES BY CAPITALISATION OF UNDISTRIBUTED DIVISIBLE PROFITS:

* No change in the percentage of equity share holding of the company.
* Surplus funds can be used.

DISADVANTAGES OF REDEMPTION OF PREFERENCE SHARES BY CAPITALISATION OF UNDISTRIBUTED DIVISIBLE PROFITS:

* There may be a reduction in liquidity.

HOW TO CONVERT PARTLY PAID PREFERENCE SHARES INTO FULLY PAID PREFERENCE SHARE:

* Final call on these shares is demanded & received before proceeding with redemption of these shares.
* The company can forfeit the shares, if the call money is not received by the company in spite of giving opportunity to pay the same via reminders.

JOURNAL ENTRIES:

1. PREFERENCE SHARES REDEEMED AT PAR:

Redeemable preference share capital a/c Dr.

To preference shareholders a/c

2. PREFERENCE SHARES REDEEMED AT PREMIUM:

Redeemable preference share capital a/c Dr.

Premium on redemption of preference shares a/c Dr.

To preference shareholders a/c

3. FRESH ISSUE OF SHARES AT PAR:

Bank a/c Dr.

To share capital a/c

4. FRESH ISSUE OF SHARES AT PREMIUM:

Bank a/c Dr.

To share capital a/c

To securities premium a/c

5. TRANSFER TO CRR ACCOUNT:

Divisible profits a/c Dr.

To Capital Redemption Reserve a/c

6\. ADJUSTMENT OF PREMIUM ON REDEMPTION:

Divisible profit a/c Dr.

To premium on redemption of preference shares a/c

7\. PAYMENT MADE TO PREFERENCE SHAREHOLDERS:

Preference shareholders a/c Dr.

To bank a/c

8\. RECEIPT OF SHARE APPLICATION MONEY:

Bank a/c Dr.

To share application a/c

9\. TRANSFER OF SHARE APPLICATION MONEY:

Share application a/c Dr.

To share capital a/c

10\. SHARE ALLOTMENT MONEY DUE:

Share allotment a/c Dr.

To share capital a/c

11\. RECEIPT OF ALLOTMENT MONEY:

Bank a/c Dr.

To Share allotment a/c

12. SHARE CALL MONEY DUE:

Share call a/c Dr.

To share capital a/c

13. RECEIPT OF SHARE CALL MONEY:

Bank a/c Dr.

To share call a/c

14. CALLS IN ARREARS:

Bank a/c Dr.

Calls in arrears a/c Dr.

To share call a/c

15. FORFEITED SHARES:

Share capital a/c Dr.

To calls in arrears a/c

To shares forfeited a/c

CHAPTER-6

ACCOUNTING FOR BONUS ISSUE AND RIGHTS ISSUE

BONUS ISSUE:

* Bonus issue means an issue of additional shares to existing shareholders free of cost in proportion to their existing holding.
* Bonus issue is also known as a "Scrip issue" or "capitalisation issue" or "capitalisation of profits".

CONDITIONS FOR BONUS ISSUE OF SHARES AS PER COMPANIES ACT, 2013 AND SEBI REGULATIONS:

* Authorised by AOA
* Authorised in the general meeting of the company on recommendation of board.
* No default in repayment of principal / interest with respect to any loan
* No default in payment of statutory due to employees (PF, bonus, gratuity, etc.,)
* All shares should be fully paid.

POINTS TO REMEMBER:

* The company which has once announced the decision of its Board recommending a bonus issue, shall not subsequently withdraw the same.
* Bonus shares shall not be issued in lieu of dividend.

EFFECTS OF BONUS ISSUE:

* Increase in share capital
* Reduction in EPS and other per share values.
* Favourable act considered by market
* Adjustment in market price.
* Reduction in accumulated profits.

SOURCES AVAILABLE FOR BONUS ISSUE:

* CRR - No restriction.
* CR - Only that portion received in cash.
* SP - Only that portion received in cash
* GR - No restriction
* P&L - No restriction

POINTS TO REMEMBER:

* If subsequent to Bonus issue, paid up capital of company exceeds its authorised capital, then company shall pass resolution amending capital clause of MOA to increase its Authorised capital.
* If company has convertible debentures, then similar benefits shall be reserved for convertible debentures.

TYPES OF BONUS ISSUE:

* Issue of fully paid shares as bonus.
* Conversion of partly paid shares into fully paid shares by way of bonus.

JOURNAL ENTRIES:

1. i) AT THE TIME OF DECLARATION OF BONUS:

CRR a/c	Dr.
CR a/c	Dr.
SP a/c	Dr.
GR a/c	Dr.
P/L a/c	Dr.
To bonus to equity shareholder's a/c	

ii) WHEN BONUS SHARES ARE ISSUED:

Bonus to equity shareholder's a/c Dr.

To equity share capital a/c.

2. i) WHEN PARTLY PAID SHARES ARE CONVERTED INTO FULLY PAID SHARES BY WAY OF BONUS:

General reserve a/c Dr.

Profit & loss account

To bonus to equity shareholder's a/c

ii) ON MAKING THE FINAL CALL DUE:

Share final call a/c Dr.

To share capital a/c

iii) ON ADJUSTMENT OF FINAL CALL:

Bonus to shareholder's a/c Dr.

To share final call a/c

RIGHT ISSUE:

* Right issue means issue of "right" to subscribe for further shares to existing shareholder in proportion to holder's holding.
* Whenever company intends for subsequent issue of shares a chance will be given first to existing shareholders to protect their stake by way of rights.
* The shareholder should exercise right or reject or renounce it and the time limit should be not less than 15 days and not exceeding 30 days.
* The accounting treatment of right shares is the same as that of issue of ordinary shares.

ADVANTAGES:

* Maintenance of existing shareholder's proportional holding in company and retain their financial and governance rights.
* The existing shareholders are not affected by dilution in the value of share because getting new shares at a discounted value from their cum-right value will compensate decrease in the value of shares.

* Relatively simple logistics and cost effectiveness as compared to a full blown public issue.
* Image enhancement.

DISADVANTAGES:

* Assessed against its true worth to ensure that you get a bargained deal.
* Dilution in the value of shares.

EFFECTS:

* Maintenance of existing shareholder's proportional holding in company and retain their financial and governance rights.
* Dilution in the value of shares.
* Image enhancement.
* Convenience in handling issue.

VALUATION OF RIGHT:

Value of right = Cum right price - Ex right price.

Cum right MP of share = MP of share before RI.

Ex right MP of share = MP of share after RI.

Ex right MP of share

$$= \frac{\text{No. of shares before RI} \times \text{Cum right issue} + \text{No. of RI shares} \times \text{Issue price}}{\text{Total no. of Shares after RI}}$$