

Welcome students I doctor Champa Ramkrishna Parab Head Department of Commerce and Associate Professor MES College of Arts and Commerce Zuarinagar Goa extend .a very warm welcome to you all once again to module 11. In this model, we are going to deal with internal reconstruction and we are taking problem number One and the solution with regard to the Journal, the Balance sheet and the Capital Reduction Account will be presented to you.

Outline: The problem which I have taken is going to cover the adjustment with reference to change in the face and paid up value of preference and equity shares, sacrifices which are made by various stakeholders, like debenture holders and creditors Further as a part of our problem we also have writing off of fictitious assets, tangible and intangible assets and transferring balance in the capital reduction account to capital reserve account depending upon the situation.

Learning Outcomes: Students will be able to know the type of transactions and adjustments involved when company undergo internal reconstruction scheme. They will be able to complete the accounting treatment and prepare Journal, capital reduction account and balance sheet after the scheme of reconstruction.

Let's come to our problem number one on internal reconstruction where horizontal balance sheet and not the vertical balance sheet is presented to you, but that makes no difference or should not make any difference. The name of your company's balance sheet of Corona vaccine is on 31st December 2020.

You are presented in the balance sheet, the authorized capital 25,000 equity shares of 20 each. You have 300-6% preference shares of Rs. 100

each. Further there is issued and paid up capital as a part of our issued and paid up capital. We have both Equity as well as the Preference shares. We have 15,000 equity shares of 20 each fully paid. So please check, the company has in the balance sheet 15,000 equity shares of 20 each. The money is coming to Rs 30,000. We also have 100 - 6% preference shares of 100 each. Do look at the paid up value. The paid up value of the share is only 80, further you have 60-7% debentures of 100 each. The amount is coming to Rs. 60,000. There is Bills Payable, creditors both are the items of liabilities and there is outstanding Interest on Debentures to be paid by the company. So these are the items of your liabilities. We are moving to the asset side, so let's check here we have on the asset side plant, which is a tangible fixed asset. There are patterns which is an intangible fixed asset that our debtors Bills Receivables under the title trade receivable, there is stock which is inventory .There is cash and Bank balance .what is to be noted is these are two items. One is the debit balance in P and L A/C account which is item of your loss. As fictitious asset/ miscellaneous expenditure, and there is another item called Preliminary expenses. This is also the item of fictitious asset to be noted in the balance sheet as the company is undergoing the internal reconstruction scheme approved by the Court of Law. The basic purpose of the internal reconstruction scheme is to write off all the accumulated losses and in your question the accumulated losses appear under the titles debit balance P and L A/C account. and the second one is your preliminary expenses account. Do remember whether there is adjustment pertaining to debit balance in P and L Account as well as your Preliminary expenses compulsorily to be written off to Capital Reduction Account. Please check here. And pay attention to the explanation to each and every adjustment.

We are given in question that a special resolution was passed and confirmed by the Court of Law to the following effect. When you talk about internal reconstruction scheme, it has to be accepted by articles of Association at the same time.

We prepare Journal based on adjustments. Let me come to first adjustment where: 100 - 6% preference shares of 100 each rupees 80 paid up to be reduced to rupees 60 each rupees 40 per share paid up. Do focus. We have something called us 100 - 6% preference shares of 100 each rupees 80 paid up. So if you look at the balance sheet of the company in the balance sheet you are having issued and paid up capital. Under that there is something called us preference shares, and the name of the preference shares is 6% if you look at, let us go back to balance sheet. Please check there we found 100 -6% preference shares of ₹ 100 each.80 paid up 100 preferences in balance sheet. It was 80. Paid up now as a part of internal reconstruction scheme they are to be reduced to 60/- face value. and 40 per share paid up so What is to be noted by you all is that do not look at the face value of the share because the paid up value in the question or in the balance sheet was rupees 80. So compare your old balance sheet paid up value with new adjustment paid up value. What is to be compared is :you are having rupees 80 pay in your old balance sheet. What is? Presented to you in adjustment one is, these preferences are reduced to 60, meaning face value has become 60, wherein the paid up value is 40. So when you pass the Journal entry with regard to the reduction, kindly make comparison between 80 paid up and 40 paid up. That means in the old balance sheet the paid up value of the Preference was 80/ and new paid up is Rs.40 So you will be. You will be passing

Journal entry for the difference where in the difference of rupees 40 that is 80 – 40 will go to your Capital Reduction Account. Or in other words to say you'll be debiting your old preferential capital and crediting your new preference share capital of 40 paid up and difference will go to Capital Reduction Account.

So let us check the solution simultaneously. Let us check our Journal entries simultaneously. We have very first entry, Journal is drawn in the books of Corona Vaccine, so under that we have the transaction is on 31st December 2020. Just look at what is being done. 6% preference share capital which are appearing in the balance sheet number is 1000 at the rate of 80 Paid up is debited. amount is coming to 80,000. Copied pasted as it is from your old balance sheet in place of this you will have new preferences shares paid up value is 40. There is no change in the number. Number of preferences shares and remains the same as 1,000 and to be multiplied with 40. So in the credit column what you have is 40,000. The difference between 80,000 and 40,000 is 40,000. to be transferred to Capital Reduction Account. Simple narration, 6% preference shares of 100 each, 80 paid up are reduced to 60 each 40 beta.

I proceed to I proceed to the question again for the next adjustment 2. 15,000 equity shares of 20 each fully paid up to be reduced to same number of fully paid up shares of rupees , reading out again 15,000 equity shares of 20 each fully paid up to be reduced to same number, meaning there is no change in the number but there is change in the paid up value. The paid up value from 20/- becoming 10 so come to the balance sheet we have item 15,000 equity shares of rupees 20 each fully paid now we need to change to or reduce from ₹ 20/ to ₹ 10.00. That means old fully paid up

value was 20, new paid up is reduced to 10. So there is a difference of ₹ 10 that is 20 -- 10 rupees which will go to your Capital Reduction Account

That is, we have 15,000 equity shares of 20 each. They were fully paid up shares and as a part of your adjustment we are having .Equity shares of 20/- will be debited, New equity shares of 10/- per share will be credited and difference of rupees 10 per share will be transferred to Capital Reduction Account. Let us come to solution part simultaneously and we have debited your equity share capital account copied pasted for your purposes your 15,000 number into 20, total amount 30000, in place of this. you have new Equity Shares, whose paid up amount is 10 per share. So equity shares capital new is coming to 1, 50,000. So difference is 1, 50,000 to be transferred to Capital Reduction Account. This is called as the sacrifice made by equity shareholder and adjustment one tells you about the sacrifice made by preference shareholders.

Let's move to third adjustment ,we are given.60-7% debentures of 100 each to be reduced to 8% debentures of rupees 90 each. Actually there are two things here. Please do note that old debentures were 7%Bentures in place of 7% debentures we are issuing 8% debenture but the paid up value will be now 90. That means 7% debentures what we have in the balance sheet number is 600 , the total amount is 60,000 in place of this you'll be having new one, whose name will be. 8%, where there is no change in number, 600 of ₹ 90 and difference of rupees 10. That is 100 -- 90 that comes to ₹ 10 that will go to Capital Reduction Account. So please confirm that we're coming to your entry number three please check that you have old 7% debentures debited .They are debited ,the number was 600 x

100. The money is coming to 60,000. In place of that the new name is 8%. There is no change in the number it is 600 but the paid up is 90. So it comes to 54000, and 60,000-- 54,000 difference is 6000 these differences to be credited to Capital Reduction Account because it is the sacrifice made by our debenture holders. You have a simple narration where ₹ 100 debentures are reduced to 90 rupees, and wherein there is change in the name of the debenture.

I proceed further to your next adjustment. where debenture holders to forgo the accumulated debenture interest due to them .Let us come back to the balance sheet in the balance sheet there is something called as outstanding interest on debenture. This outstanding interest on the debenture is called as a recorded liability because it is recorded in the amount column of the balance sheet of the. Company so that the debenture holders are sacrificing the money payable to them against the interest on their debentures, thereby sacrificing the money. They are giving up their claim. So this claim what they don't want is a profit to the company to be credited to Capital Reduction Account.

Outstanding interest on debenture being the item of liability and as all liability shows credit balance you need to close this particular liability by giving debit to the same. So let us come to the solution with regard to the same, check. here the solution : Interest on Debenture account is debited and what is credited is the Capital Reduction Account, entire money Is the sacrifice from debenture Holder. That is why the same is credited to Capital Reduction Account.

Further we're coming to our question where next adjustment is creditors agree to forego, forego meaning to give up the claim, moment you are saying giving up the claim it is the sacrifice and whatever sacrifice made by the stakeholders. Is the profit to the company to be credited to Capital Reduction A/C so please check here 20% of the money payable to creditors have been sacrificed by creditors and in return they are asking for equity shares for their 80% of the money in equity shares. I conclude on that adjustment saying that creditors as we have in the balance sheet to the extent of 50,000 out of 50,000 they are sacrificing /for going 20 percent. 20% of 50,000 if you calculate it will come to 10,000, so 50,000 you have against Creditors of that. What they don't want amounting is 10,000 that will go to Capital Reduction Account and 50000 -- 10000. What remain are 40,000. That will be by issue of your new equity shares

So let us confirm that you have secured creditors amounting to 50,000. As a part of your adjustment, you are giving them equity shares to the extent of 80%. So what I have done is I have taken their total amount that is ₹ 50,000 multiplied the same with 80%. The answer is coming to rupees 40,000 rupees. 40,000 is divided with the new value of your equity share as per adjustment, which is 10, and that's how we are getting the number of equity shares as 4000 and money is coming to 40,000. So 80% of 50,000 is coming to 40,000. And remaining money to be transferred to Capital Reduction Account because the money or the claim is forgone sacrifice, which is a profit to the company. So the narration what you have is : creditors have forgone 20% o their claim in exchange for equity shares for remaining 80%.

Further we have as a part of our question the sum does available to be applied as follows. You have been asked to make use of your Capital Reduction Account to write off debit balance in P and L A/C and Preliminary Expenses, you are wiping them off writing them off. They are to be credited and when you're crediting them as they are the item of losses the losses come on the debit side of Capital Reduction Account.

So just check here. You have further transaction where Capital Reduction is debited , and for the time being do not write the money what you have is preliminary Expenses Account .and debit balance in P and L A/C ,both to be added to arrive at Capital Reduction A/C amount column.

We are coming to our last adjustment as a part of our Capital Reduction scheme. We are given that plant and patents to be written down by 20% and 40% respectively. Plant is our tangible asset and Pattern intangible asset. When you talk about capital reduction A/C it stands for reduction so there is fall in the value of plant by 25% and Pattern by 40%. So to the extent of 25% of your plant and 40% of your Pattern will be credited and Capital Reduction account will be debited .I repeat what I said is it will be debited to your Capital Reduction Account and will be credited to your respective Asset because there is fall in the value of these assets. So let us check, the other entry. You have "To" plant. the total book value of the plant given in the question is asked to reduce by 25%.so let us calculate 25% which comes to 50,000 and.40% comes to 40,000.So in total there is decrease in the value of two are assets by rupees. 90,000, which is a loss to the company to be debited to you capital reduction account and

accordingly we have the narration for the same for writing down the value of your plant and Patterns.

And finally the adjustment says you need to whatever balance you have in the reduction account that you need to transfer to capital reserve. Students to write this last entry, you need to leave 5 lines in your Journal because unless and until you prepare the Capital. Reduction Account you won't be able to know how much is the difference in your reduction account to be transferred to your capital reserve account. So this is always the last entry to be prepared after preparation of your capital reduction account. So in the next module we are going to prepare the reduction account. But to complete my Journal I have posted the entry wherein the balancing figure in the reduction account is rupees 20,000 and this 20,000.how we are calculating or how we are getting that we are going to get in our next Module 13.

Thank you.