Hello students welcome to this module on a problem with regards to internal reconstruction.

At this stage if it is advisable for you to go back to the module on legal aspects and revise the Journal entries with regards to internal reconstruction.

In this module I will be solving the Journal entries and the capital reduction of account in relation to problem #2.

Let us have a look at the problem. In this problem you are given the Balance Sheet of Dishtavo Ltd. as on 31st March 2020. The Balance Sheet in Schedule Three of the Companies Act of 2013.

You are given this note that says preference dividend are in areas for two years. If you look at any part of this problem, you cannot see any areas of preference dividend mentioned in the problem. Since preference dividend is not there is no provision made for it. We are not going to include the calculation for preference dividend in our problem.

Let's have a look at each of the transactions.

The Journal entry and the entry in the Capital Reduction Account side by side.

In the first case, equity shares are to be converted into the same number of equity shares of such face value as to reduce the paid-up share capital by 30%. So now in case of your equity shares, your equity shares, you have one like 20,000 equity shares at the rate of rupees 10 each fully paid. This adjustment says that you must reduce the face value by 30%. That means you have to take 30% of rupees 10 and. deduct that from ₹ 10 to arrive at the figure.
So, say for example, we've taken 10 and you calculate 30% of this rupee 10. You arrive at three, so. ₹10 -- 3. You will get ₹ 7. so now your equity shares are supposed to be ₹ 7 per share, and whatever's the balancing figure will be shown in the capital reduction account.

Let's have a look at the Journal entry. Now in case of your equity share capital, you had equity share capital worth Rupees 12 lakhs. The value was rupees 10 per share. Your new value is rupees 7 per share.And now it is equal to ₹ 8,40,000. How did I get ₹ 8,40,000. I have multiplied 1,20,000 equity shares with the new face value of ₹ 7 per share. Therefore, I get the answer of ₹ 8,40,000. The difference between ₹ 12,00,000 and ₹ 8,40,000 is ₹ 3,60,000, which is taken to the credit of the capital reduction account. So on the credit side we see by equity share capital rupees 10, ₹ 3,60,000.

Our next adjustment relates to the preference shares to be converted to the same number of preference shares of rupees 60, each fully paid up. So we are going to convert our preference shares. Currently, they are priced at rupees 100 per share, and we're going to convert them into shares worth rupees 60 so.
Now again, our preference shares are rupees 100.

Let us have a look at the Journal entry in case of the second adjustment. That is, a preference shares to be converted into the same number of rupees 60. Each preference shares fully paid up. Currently our preference shares are rupees 100. And now we are going to change them to rupees 60 per share. So 6000 preference shares of 100 each. It's equal to 6,06,000 preference shares of rupees 60 each will be equal to 3,60,000. This 3, 60,000 you will be minus from 6,00,000 and the balancing figure you will put in the capital reduction account. The figure of this 10% preference share capital which has been reduced. That is 2,40,000 will appear on the credit side of the capital reduction account.

The next Journal entry is in regard to the balance of generally reserved to be utilized for the purpose of reconstruction, so our entire balance of general Reserve, which is rupees 5 lacs will be transferred to the credit of the capital reduction account. So therefore, we pass this Journal Entry Capital Reserve account debit to capital reduction account in your capital reduction account 5 lacs will appear. On the credit side, the 4th adjustment is debentures are to be converted into 8% debentures of rupees 50 each, so as to generate the same amount of interest.

Now, for this particular adjustment, we need to prepare a working note because we have to find out what will be the value of our debentures. We are told that the interest rate on our debentures. if we have a look at the problem, our debentures are worth 6% interest and the total value of the debentures is rupees two lakhs. so interest on 6% debentures will be 12,000. That is, you calculated 6% of rupees two lacs and therefore you arrived at the figure of 12,000. Adjustment says that our new debentures have to give us the same amount of interest. That means our rate of interest is 8% and our interest whatever we calculate on the value should be 12,000. We do not know the value of debentures, so let us assume that the value of our 8% debentures is X. 8% of this value should give you ₹12,000, so if you cross multiply you have 12,000 * 100 / 8. You will get a value of ₹ 1,50,000. so your new debentures of 8% have a value of 1,50,000. To find out the number of debentures you have to divide it by the face value per debenture as given to you in the adjustment. Now here you are told that the debentures have to be rupees 50 each. So therefore this one got 15,000. When you divide by 50 you will get 3000 debentures. so in that case let's see how we pass the Journal entry. So are all debentures 6% having face value of 100 worth rupees? Two lacs is converted into 8% debentures or 50 worth rupees 1,50,000.

We've seen the first working note on how we arrived at this calculation and the balancing figure is transferred to the credit of the capital reduction account. So this 50,000 will come in our capital reduction account on the credit side.

Now let us have a look at the next adjustment. Fixed assets and stock to be reduced by 5,52,000 and 38,000 respectively. That means we are supposed to minus 5,52,000 from fixed assets, and we're supposed to minus 38,000 from our inventories. so let us do this adjustment last

Adjustment areas of preference. Dividend to be written off in full. You will have no Journal entry for such an adjustment because balance sheet as I already told you, there is no provision for the payment of this dividend, so no entry will we past balance of P&L will also be written off. This again will be shown when

This will be shown when we're closing our capital reduction account now the following are to be given effect to unrecorded debtors of 3,34,000, unrecorded payment to creditors and reconstruction expenses, now unrecorded debtors. We have to transfer to the debit of our capital reduction account like shown in the Journal Entry Debtors Account debited to capital reduction account. so, this amount will appear on the. Credit side of the capital reduction account. The next entry that is unrecorded payments to creditors that also needs to be made, and we have to pay off an unrecorded creditor by debiting creditors account and credit and crediting the bank account. This entry will not appear in the capital reduction account.

The next entry reconstruction expenses amounted to rupees 11,500. This will be shown as a capital reduction account. To bank account and your reconstruction expenses will be shown on the debit side of the capital reduction account as shown here. So you have 11,500.

Now we come to the closing of our capital reduction account. What is told to us is that fixed assets.
As we have seen, in adjustment #5 or they have been reduced by 5,52,000 stock has been reduced by 38,000 and we're going to write off a balance in the profit and loss account of Rupees 8,50,000. This was the loss that we had suffered. Whatever is the balancing figure.

OK, that is this 32,500. it will be shown in the Capital reserve account. So first we pass all these closing entries and finally whatever balancing figure of 32,500 that we have calculated in the capital reduction account, we transfer it to the. Capital reserve account. So this balancing figure will be shown here. OK, so this will be the closing entry in case of your Journal entries. This is the last entry that you have to pass.

Thank you students
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These are my references.

Thank you.