Quadrant II – Notes

Programme: Bachelor of Commerce

Subject: Commerce

Paper Code: COD117

Paper Title: Advanced Company Accounts (DSE 5)

Unit: IV

Module Name: Methods of Accounting for Purchase Method-Accounting Procedures and Journal Entries

Module No: 29

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Types of Amalgamation

According to AS-14 Accounting for Amalgamations, there are two types of amalgamations:

1. Amalgamation in the nature of merger and
2. Amalgamation in the nature of purchase.

Amalgamation in the nature of Purchase

An amalgamation will be treated as amalgamation in the nature of purchase if **any one or more** of the following conditions are not satisfied:

1. All the assets and liabilities of the transferor company become the assets and liabilities of the transferee company after amalgamation.
2. Shareholders of the transferor company holding greater than equal to 90% of the face value, become the equity shareholders of the transferee company after amalgamation.
3. The consideration for the amalgamation receivable by the equity shareholders of the transferor company who have agreed to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company. Cash may be paid in respect of fractional shares.
4. The transferee company intends to carry on the business of the transferee company after amalgamation.
5. No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are taken over by the transferee company.

METHODS OF ACCOUNTING FOR AMALGAMATION

PURCHASE METHOD

Features

1. The Purchase Method is applicable for Amalgamation in the nature of purchase
2. Assets, liabilities and retained earnings are taken by the new company at book value or at fair value on the date of amalgamation. Hidden assets or unrecorded assets are also transferred to the new company.
3. The reserves of the transferor company, other than statutory reserves, are not taken over by the transferred company.
4. Statutory Reserves retain their identity in the financial statements of the new company.
5. If purchase consideration is greater than the net assets taken over, the difference will be treated as Goodwill and debited to the Goodwill Account. The Goodwill should be amortized within a period of 5 years.
6. If Purchase consideration is lower than net assets taken over, the difference will be treated as Capital Reserve and credited to Capital Reserve Account.
7. None of the costs associated with the amalgamation are capitalized.

Steps to be followed when making Accounting Entries in the Books of the Transferee Company (New Company)

1. Record the purchase consideration due.
2. Record the different assets and liabilities taken over.
3. Record the payment of purchase consideration.
4. Record the liquidation expenses.
5. Record preliminary expenses.
6. Record the issue of new shares/debentures

Steps to be followed when making Accounting Entries in the Books of the Transferor Company (Old Company)

Step 1: Prepare the Balance Sheet of the Company as on the date of liquidation.

Step 2: Open a Realization Account and transfer all assets and liabilities to this account.

Step 3: Transfer Equity Share Capital, Reserves and Surplus and Profit/Loss in Profit and Loss Account to Equity Shareholders Account.

Step 4: Transfer Preference Share Capital to Preference Shareholders Account.

Step 5: Record purchase consideration due from the Transferee company

Step 6: Record the receipt of the purchase consideration from the Transferee Company.

Step 7: Record liquidation expenses If borne by the Transferor company.

Step 8: Record the assets and liabilities not taken over by the company.

Step 9: Record payment to preference shareholders.

Step 10: Record Profit/Loss on Realization

Step 11: Record Final Payment to Equity Shareholders.