Session : 2019-20

M.COM.- FIRST YEAR

(II SEMESTER)

CORPORATE FINANCIAL ACCOUNTING

(I-2002)

UNIT – I : AMALGAMATION & RECONSTRUCTION

Dr. S.K.GHAI

LEARNING OBJECTIVES

After you have gone through this unit, you should be able to describe –

- Meaning of Amalgamation & Absorption;
- Types of Amalgamation & Reconstruction;
- Difference between **'Amalgamation in the nature of Merger'** and '**Amalgamation in the nature of Purchase'**;
- Purchase Consideration and its methods;
- Accounting treatment in the books of Transferor Company (Vendor) and Transferee Company (Buyer);
- Difference between **'External Reconstruction'** and **'Amalgamation'**;
- Accounting for External Reconstruction

SITUATION III

- When shares are held by **both companies in each other**, then the main problem is to determine the purchase consideration.
- The calculation of purchase consideration is closely related with and solely depended on the method of calculation given in the question.

(A) When Net Payment Method is applied

STEP 1 – Determine the number of shares, the **outside shareholders** of the **transferor co.** are entitled to receive from the transferee co. on the basis of exchange ratio given in the question.

STEP 2 – Deduct from **STEP 1** the number of shares in transferee co. already held by the transferor co. This will give the number of **additional shares** to be issued to the transferor co. by the transferee co. in satisfaction of the purchase consideration.

STEP 3 – Multiply **STEP 2** with the **issue price** of shares in order to get the amount of purchase consideration.

SITUATION III

- **Example** – B Ltd. absorbs S Ltd. by issuing 20 shares of Rs.100 each at a premium of 20% for every 16 shares held in S Ltd.

On the date of absorption the balance sheets of both were as per overleaf.

You are required to calculate purchase consideration:

SITUATION III

PARTICULARS	B Ltd. (Rs.)	S Ltd. (Rs.)
EQUITIES & LIABILITIES		
Shareholders' Funds		
Share Capital (Rs.100)	50,00,000	30,00,000
Current Liabilities		
Sundry Creditors	6,00,000	4,00,000
	56,00,000	34,00,000
ASSETS		
Non-Current Assets		
Investments:		
6,000 shares in S Ltd.	6,50,000	
5,000 shares in B Ltd.		5,80,000
Current Assets		
Other Assets	49,50,000	28,20,000
	56,00,000	34,00,000

SOLUTION

Step 1 (a) : Shares held by outside shareholders in S Ltd. = 30,000 (-) 6,000 = 24,000

Step 1 (b) : Shares to be issued to outside shareholders 24,000 x 20/16 = 30,000

Step 2 : Fresh shares to be issued = **Step 1 (b)** (-) Shares already held by S Ltd.

= 30,000 (-) 5,000 = 25,000

Step 3 : Purchase consideration = **Step 2** x (Rs.100 + 20% Premium)= 25,000 x Rs.120 = 30,00,000

SITUATION III

(B) **When Net Assets Method is applied**

In such case of cross holdings, **only SIMULTANEOUS EQUATIONS*** *help to ascertain the net assets of each co. b'coz the value of shares held by one co.in the other co.is influenced by the value of the other co.*

STEP 1 – Calculate **net assets of each co.** ***without*** considering mutual holdings.

STEP 2 – Calculate **total value of shares** of **each co.**by using **simultaneous equations***. (Shares ***include*** mutual holdings also.)

STEP 3 – Calculate the **value per share** of **each co.**, i.e.,

Total Value as per STEP 2 / Number of Equity Shares

STEP 4 – Calculate amount of claim of outside shareholders of the transferor co. (S Ltd.)

= **Value per share** as per **STEP 2 x Shares held by outside shareholders.**

SITUATION III

STEP 5 (a) Find out the number of shares in transferee co. (B Ltd.) required to satisfy the claim of outside shareholders

= Amount of claim (as per **STEP 4**) / Value per share of the Transferee Co. (as per **STEP 3**)

STEP 5 (b) Number of **Fresh Shares in transferee co.** (B Ltd.) to be issued to outside shareholders of the transferor co. (S Ltd.)

= Shares obtained as per **5 (a)** above **(-)** Number of shares **already held** by the transferor co.(S Ltd.) in transferee co.(B Ltd.)

STEP 6 - **Purchase Consideration**

= Fresh Shares [as per **STEP 5 (b)] x Value per share of transferee co.(B Ltd.)**

Note : (1) ***Any fraction is paid in cash on the basis of intrinsic value of share.***

(2) In case of amalgamation of two companies, purchase consideration **is calculated by deducting the proportionate value of shares held by the other co. (amalgamated co.) from the total value of shares of each co. (amalgamating cos.) calculated as per STEP 2 above.**

REFERENCE BOOKS

1. **Warren/Reeve/Duchac's Corporate Financial Accounting 13E and CengageNOW™v2! Market-leading Corporate Financial Accounting (ISBN-13: 978-1285868783 ISBN-10: 1285868781)**
2. **International Journal of Accounting and Finance (ISSN online:1752-8232 ISSN print: 1752-8224)**
3. **Shukla S.M. & Gupta K.L., Corporate Financial Accounting (Sahitya Bhawan Publications)**
4. **Gupta K.G., Corporate Financial Accounting (K.G.Publications)**
5. **Gupta R.L. Advanced Financial Accounting, (S.Chand & Co.)**

REFERENCE BOOKS

6. **Maheshwari S.N., Advanced Accounting – Vol.II, (Vikas Publishing House)**
7. **Shukla M.C. & T.S.Grewal, Advanced Accountancy (Sultan Chand & Co.)**
8. **Jain & Narang, Financial Accounting (Kalyani Publishers)**

THANKS!