

MAA OMWATI DEGREE COLLEGE HASSANPUR (PALWAL)

ASSIGNMENT/IMPORTANT QUESTION

CLASS –B.Com 4th SEM

SUBJECT – Corporate Accounting - II

Short Questions:

1. What is internal reconstruction of a company?
2. State two objectives of internal reconstruction.
3. What do you mean by reduction of share capital?
4. What is the difference between internal and external reconstruction?
5. Define purchase consideration.
6. Name any two methods of computing purchase consideration.
7. A Ltd. takes over B Ltd. for a consideration of ₹5,00,000. Goodwill worth ₹20,000 is included. What is the net asset taken over? *(Numerical)*
8. In internal reconstruction, a company reduces its ₹100 face value shares to ₹60. Pass the journal entry. *(Numerical)*
9. What is liquidation of a company?
10. What is the difference between voluntary and compulsory liquidation?
11. State the order of payments made by a liquidator.
12. What is meant by 'Preferential Creditors'?
13. A company has assets worth ₹6,00,000 and liabilities of ₹3,00,000. Calculate surplus available for shareholders. *(Numerical)*
14. What is a liquidator's final statement of account?
15. What is financial reporting for financial institutions?
16. State any two features of financial reporting in banks.
17. Name the schedules attached to a banking company's final accounts.
18. What is meant by rebate on bills discounted?
19. How is provision for doubtful debts treated in bank accounts?
20. What are the components of a bank's Profit and Loss Account?
21. A bank earns interest of ₹5,00,000 and pays interest on deposits ₹3,50,000. Calculate Net Interest Income. *(Numerical)*
22. Give journal entry for creation of provision for bad debts in bank books. *(Numerical)*
23. Name two items shown under "Other Liabilities and Provisions" in the Balance Sheet of a bank.

24. What is meant by holding company and subsidiary company?
25. Define minority interest.
26. What is cost of control or goodwill in consolidation?
27. Explain the treatment of unrealized profit in consolidation.
28. A holding company holds 75% shares in a subsidiary. Share capital = ₹4,00,000. What is the minority interest? (*Numerical*)
29. Inter-company sales amounted to ₹1,00,000 with unrealized profit of ₹10,000. How is this treated? (*Numerical*)
30. What is the objective of preparing a consolidated balance sheet?

Long Questions:

Unit 1

Q1. What is internal reconstruction? Explain the objectives, procedures, and journal entries related to internal reconstruction.

Q2. Differentiate between merger and purchase under external reconstruction. Discuss the accounting treatment as per AS-14.

Q3. A Ltd. has the following balance sheet before internal reconstruction:

- a) Share Capital (₹10 each): ₹5,00,000
- b) Accumulated Losses: ₹1,00,000
- c) Creditors: ₹2,00,000

After reconstruction, the face value of shares is reduced to ₹6 each, losses are written off, and ₹20,000 is paid to creditors. Pass journal entries and prepare a reconstructed balance sheet.

Q4. Compute the purchase consideration under Net Assets Method:

- a) Assets Taken Over: Building ₹1,50,000, Stock ₹1,00,000, Debtors ₹50,000
- b) Liabilities Taken Over: Creditors ₹60,000
- c) Agreed Purchase Price = Net Assets + ₹20,000 Goodwill.

Q5. X Ltd. is merged into Y Ltd. The following details are available:

- a. X Ltd. Share Capital: ₹3,00,000
- b. Reserves: ₹1,00,000
- c. Y Ltd. issues shares worth ₹3,50,000 to X Ltd.'s shareholders.
- d. Pass journal entries in the books of Y Ltd.

Unit 2

Q1. What is liquidation? Explain the order of payment and preparation of liquidator's final statement of account.

Q2. Write a detailed note on Financial Reporting for Financial Institutions and the RBI guidelines applicable.

Q3. The assets realized ₹5,00,000. The payments to be made:

- Liquidator's expenses: ₹10,000
- Secured Creditors: ₹2,00,000
- Preferential Creditors: ₹30,000
- Debentures: ₹1,50,000
- Unsecured Creditors: ₹70,000

Prepare Liquidator's Final Statement of Account.

Q4. From the following information, calculate payment to equity shareholders:

- Share Capital: ₹3,00,000
- Debentures: ₹1,00,000
- Creditors: ₹1,50,000
- Assets Realized: ₹5,00,000
- Expenses: ₹10,000

Q5. Prepare a journal entry and working notes for the payment of debenture holders with interest accrued till liquidation date of ₹6,000.

Unit 3

Q1. Discuss the format of final accounts of a banking company as per the Banking Regulation Act.

Q2. Write short notes on:

- Provision for bad debts
- Rebate on bills discounted
- Interest on doubtful debts

Q3. From the following information, prepare the Profit and Loss Account of a bank:

- Interest Earned: ₹10,00,000
- Interest Expended: ₹6,00,000
- Operating Expenses: ₹1,50,000
- Other Income: ₹1,00,000
- Provision for Bad Debts: ₹50,000

Q4. Calculate rebate on bills discounted:

- Total Bills = ₹3,00,000
- Unexpired Period = 2 months
- Annual Discount Rate = 12%
- (Rebate = ₹3,00,000 × 12% × 2/12)

Q5. From the following balances, prepare a Balance Sheet in prescribed format:

- Capital ₹10,00,000
- Reserves ₹3,00,000

- Deposits ₹15,00,000
- Investments ₹8,00,000
- Loans ₹7,00,000
- Cash ₹2,00,000
- Other Liabilities ₹1,00,000
- Fixed Assets ₹2,00,000

Unit 4

Q1. Explain the concept of consolidated balance sheet. How is it prepared by a holding company?

Q2. Define minority interest and cost of control. How are inter-company transactions treated in consolidation?

Q3. H Ltd. holds 80% shares in S Ltd. The balance sheets show:

- Share Capital of S Ltd.: ₹2,00,000
- Reserves: ₹50,000
- H Ltd. paid ₹1,80,000 for its share.

Calculate cost of control and minority interest.

Q19. From the following information, prepare a Consolidated Balance Sheet:

- H Ltd. Share Capital ₹5,00,000
- S Ltd. Share Capital ₹2,00,000
- H Ltd. holds 75% of S Ltd.
- Profits of S Ltd. before acquisition: ₹20,000; after acquisition: ₹30,000
- Inter-company owing: ₹10,000
- Unrealized profit in stock: ₹5,000

Q20. Calculate the adjusted profit of holding company after consolidation:

- Holding company's profit: ₹3,00,000
- Share in subsidiary's post-acquisition profit: ₹25,000
- Less: Unrealized profit in inventory: ₹5,000
- Less: Dividend received from pre-acquisition profit: ₹10,000

Syllabus

Unit 1

Internal Reconstruction, External Reconstruction in the nature of merger and purchase

Unit 2

Liquidation of a Company, Financial Reporting for Financial Institutions

Unit 3

Final Accounts of Banking Companies

Unit 4

ANSWER OF SHORT QUESTIONS

Q1. What is internal reconstruction of a company?

Ans: Internal reconstruction is the process by which a company reorganizes its financial structure without undergoing liquidation. It involves steps like reduction of capital, revaluation of assets, and writing off accumulated losses to clean the balance sheet.

Q2. State two objectives of internal reconstruction.

Ans:

1. To eliminate past losses from the company's books.
2. To improve the company's financial position by restructuring capital.

Q3. What do you mean by reduction of share capital?

Ans: It refers to decreasing the face value or paid-up value of shares to write off losses, cancel unpaid capital, or return excess capital to shareholders with legal approval.

Q4. What is the difference between internal and external reconstruction?

Ans: Internal reconstruction is a reorganization within the same company, while external reconstruction involves closing the old company and transferring its business to a new one.

Q5. Define purchase consideration.

Ans: Purchase consideration is the total amount payable by the purchasing company to the vendor company in exchange for acquiring its business.

Q6. Name any two methods of computing purchase consideration.

Ans:

1. Net Assets Method
2. Net Payment Method

Q7. A Ltd. takes over B Ltd. for ₹5,00,000. Goodwill is ₹20,000. What is the net asset taken over?

Ans:

Net Assets = ₹5,00,000 – ₹20,000 = ₹4,80,000 ✓

Q8. In internal reconstruction, a company reduces its ₹100 face value shares to ₹60. Pass the journal entry.

Ans:

```
Share Capital A/c Dr. ₹100
    To Capital Reduction A/c ₹40
    To Share Capital A/c ₹60
```

Q9. What is liquidation of a company?

Ans: Liquidation is the process of closing a company, selling its assets, and distributing the proceeds to creditors and shareholders.

Q10. What is the difference between voluntary and compulsory liquidation?

Ans:

- Voluntary liquidation is initiated by members or creditors.
- Compulsory liquidation is ordered by a court or tribunal.

Q11. State the order of payments made by a liquidator.

Ans:

1. Legal charges
2. Liquidator's remuneration
3. Secured creditors
4. Preferential creditors
5. Unsecured creditors
6. Shareholders

Q12. What is meant by 'Preferential Creditors'?

Ans: Preferential creditors have legal priority in receiving payments, e.g., employees' wages, taxes, and government dues.

Q13. A company has assets of ₹6,00,000 and liabilities of ₹3,00,000. Calculate surplus for shareholders.

Ans:

Surplus = ₹6,00,000 – ₹3,00,000 = ₹3,00,000 ✓

Q14. What is a liquidator's final statement of account?

Ans: It's a summary showing how the liquidator realized assets and paid off liabilities during the liquidation process.

Q15. What is financial reporting for financial institutions?

Ans: It refers to the preparation of financial statements by financial institutions following RBI guidelines and other statutory norms.

Q16. State any two features of financial reporting in banks.

Ans:

1. Mandatory adherence to RBI formats
2. Greater transparency and regulatory compliance

Q17. Name the schedules attached to a banking company's final accounts.

Ans:

- Schedule 13: Interest Earned
- Schedule 14: Other Income
- Schedule 15: Interest Expended
- Schedule 16: Operating Expenses

Q18. What is meant by rebate on bills discounted?

Ans: It is the unearned portion of interest on bills that mature after the balance sheet date, shown as a liability.

Q19. How is provision for doubtful debts treated in bank accounts?

Ans: It is created by debiting P&L A/c and shown as a deduction from advances or under provisions in the balance sheet.

Q20. What are the components of a bank's Profit and Loss Account?

Ans:

- Interest Earned
- Interest Expended
- Operating Expenses
- Provisions
- Net Profit

Q21. A bank earns ₹5,00,000 interest, pays ₹3,50,000 as deposit interest. Calculate Net Interest Income.

Ans:

Net Interest Income = ₹5,00,000 – ₹3,50,000 = ₹1,50,000 ✓

Q22. Give journal entry for provision for bad debts in bank books.

Ans:

```
Profit & Loss A/c Dr.  
    To Provision for Bad Debts A/c
```

Q23. Name two items shown under “Other Liabilities and Provisions” in a bank’s Balance Sheet.

Ans:

1. Bills Payable
2. Provisions for taxation

Q24. What is meant by holding company and subsidiary company?

Ans: A holding company controls another company, known as the subsidiary, by owning more than 50% of its shares or controlling its board.

Q25. Define minority interest.

Ans: It is the portion of net assets and profits of the subsidiary attributable to shareholders other than the holding company.

Q26. What is cost of control or goodwill in consolidation?

Ans: It is the difference between the cost of investment in the subsidiary and the holding company’s share in net assets of the subsidiary.

Q27. Explain the treatment of unrealized profit in consolidation.

Ans: Unrealized profits from inter-company transactions are deducted from consolidated profits and inventory to avoid overstated earnings.

Q28. A holding company holds 75% of ₹4,00,000 share capital. What is the minority interest?

Ans:

Minority Interest = 25% of ₹4,00,000 = ₹1,00,000 ✓

Q29. Inter-company sales = ₹1,00,000; Unrealized profit = ₹10,000. How is it treated?

Ans: Unrealized profit of ₹10,000 is deducted from consolidated stock and consolidated profit.

Q30. What is the objective of preparing a consolidated balance sheet?

Ans: To present the financial position of the holding and subsidiary companies as a single economic unit for transparency and analysis.

ANSWER OF LONG QUESTIONS

Unit 1

Q1. What is internal reconstruction? Explain the objectives, procedures, and journal entries related to internal reconstruction.

Ans: Internal reconstruction refers to the process by which a company reorganizes its financial structure without undergoing liquidation. It is carried out to revive financially distressed companies that have incurred heavy losses and whose balance sheets show inflated asset values and accumulated losses. Unlike external reconstruction, the company continues to exist and operates under the same legal entity.

Objectives of Internal Reconstruction:

1. **To write off accumulated losses** that are appearing on the balance sheet.
2. **To revalue assets and liabilities** so that they reflect fair market value.
3. **To reduce capital** that is not represented by tangible assets.
4. **To improve financial stability** and enhance the company's creditworthiness.
5. **To attract new investments** by presenting a cleaner and more realistic financial position.

Common Procedures in Internal Reconstruction:

1. **Reduction of Share Capital:** Reducing either the face value or the paid-up value of shares.
2. **Writing off Fictitious Assets:** Removing intangible assets like goodwill, preliminary expenses, and accumulated losses.
3. **Revaluation of Assets and Liabilities:** Adjusting asset values to their fair value and settling over/under-valued liabilities.
4. **Settlement with Creditors:** Negotiating with creditors to reduce outstanding dues.

5. **Creation of Capital Reduction Account:** The reduction amount is transferred to this account, which is then used to write off accumulated losses.

Journal Entries for Internal Reconstruction:

1. For reduction of share capital:

```
Equity Share Capital A/c Dr.      XXXX
    To Share Capital A/c (Reduced Value)  XXXX
    To Capital Reduction A/c                XXXX
```

2. For writing off losses and fictitious assets:

```
Capital Reduction A/c Dr.      XXXX
    To Profit and Loss A/c                XXXX
    To Goodwill A/c                      XXXX
    To Preliminary Expenses A/c          XXXX
    To Other Overvalued Assets A/c        XXXX
```

3. For payment to creditors at reduced amount:

```
Creditors A/c Dr.              XXXX
    To Bank A/c                  XXXX
    To Capital Reserve A/c (Gain)  XXXX
```

Internal reconstruction enables a financially troubled company to restart with a healthier balance sheet, avoiding liquidation and preserving stakeholder interest.

Q2. Differentiate between merger and purchase under external reconstruction. Discuss the accounting treatment as per AS-14.

Ans: External reconstruction involves winding up an existing company and transferring its business to another existing or new company. According to Accounting Standard 14 (AS-14), external reconstruction may take the form of either a **merger** or a **purchase**.

Differences Between Merger and Purchase:

Basis	Merger	Purchase
Definition	Combination of two or more companies into one with continuity	One company takes over another and continues the business
Transfer of Assets & Liabilities	All assets and liabilities must be transferred	Only selected assets/liabilities may be transferred
Shareholders	90% of equity shareholders must become shareholders in new entity	No such condition

Basis	Merger	Purchase
Reserves	Transferred as-is to the new company	Not transferred
Method of Accounting	Pooling of Interest Method	Purchase Method

Accounting Treatment as per AS-14:

1. Amalgamation in the Nature of Merger (Pooling of Interest Method):

- All assets, liabilities, and reserves of transferor company are recorded at book value.
- No goodwill or capital reserve arises.
- Identity of reserves is preserved.

2. Amalgamation in the Nature of Purchase (Purchase Method):

- Assets and liabilities are recorded at their agreed values (may be fair or book value).
- Reserves are not carried forward.
- The difference between purchase consideration and net assets acquired is treated as **Goodwill** or **Capital Reserve**.

AS-14 ensures consistency in accounting treatment and better comparability for users of financial statements.

Q3. A Ltd. has the following balance sheet before internal reconstruction:

- Share Capital (₹10 each): ₹5,00,000
- Accumulated Losses: ₹1,00,000
- Creditors: ₹2,00,000

After Reconstruction:

- Face value of shares reduced to ₹6 each
- Losses written off
- ₹20,000 paid to creditors (balance waived)

Journal Entries:

1. Reduction of Capital:

Share Capital A/c Dr. ₹5,00,000
To Share Capital (₹6) A/c ₹3,00,000
To Capital Reduction A/c ₹2,00,000

2. Write off Accumulated Losses:

Capital Reduction A/c Dr. ₹1,00,000
To Profit and Loss A/c ₹1,00,000

3. Settlement with Creditors:

Creditors A/c Dr. ₹2,00,000
To Bank A/c ₹20,000
To Capital Reduction A/c ₹1,80,000

Reconstructed Balance Sheet:

Liabilities	₹	Assets	₹
Share Capital (₹6)	3,00,000	Cash/Bank	3,00,000

All losses and liabilities have been written off, leaving a clean balance sheet.

Q4. Compute the purchase consideration under Net Assets Method:

- Building ₹1,50,000
- Stock ₹1,00,000
- Debtors ₹50,000
- Creditors ₹60,000
- Goodwill ₹20,000

Ans:

Step 1: Compute Net Assets

= Total Assets – Liabilities
= ₹(1,50,000 + 1,00,000 + 50,000) – ₹60,000
= ₹3,00,000 – ₹60,000 = ₹2,40,000

Step 2: Add Goodwill

= ₹2,40,000 + ₹20,000 = ₹2,60,000 ✓

So, **Purchase Consideration = ₹2,60,000** under Net Assets Method.

Q5. X Ltd. is merged into Y Ltd. following details are available:

- X Ltd. Share Capital: ₹3,00,000
- Reserves: ₹1,00,000
- Y Ltd. issues shares worth ₹3,50,000 to X Ltd.'s shareholders

Journal Entries in the books of Y Ltd.:

Journal Entries in the books of Y Ltd.:

1. For Business Purchase:

```
Business Purchase A/c Dr. ₹3,50,000
    To Liquidator of X Ltd. A/c ₹3,50,000
```

2. For Assets and Liabilities Taken Over (Assumed):

```
Assets A/c Dr. ₹4,00,000
    To Business Purchase A/c ₹3,50,000
    To Capital Reserve A/c ₹50,000
```

(Assuming no liabilities and total assets of ₹4,00,000)

3. For Issue of Shares:

```
Liquidator of X Ltd. A/c Dr. ₹3,50,000
    To Equity Share Capital A/c ₹3,50,000
```

Unit- 2

Q1. What is liquidation? Explain the order of payment and preparation of liquidator's final statement of account.

Ans: Liquidation is the legal process through which a company is brought to an end and its assets are distributed to claimants. It usually occurs when a company is insolvent, meaning it cannot pay its obligations when they come due. The assets are sold off (liquidated), and the proceeds are used to repay creditors and shareholders in a specific order of priority.

Types of Liquidation:

1. **Voluntary Liquidation** – Initiated by members or creditors of the company.
2. **Compulsory Liquidation** – Initiated by a tribunal or court order.

Order of Payments in Liquidation:

As per the Companies Act and Insolvency regulations, the proceeds from asset realization are distributed in the following order:

1. **Legal Charges:** Court or tribunal costs.

2. **Liquidator's Remuneration and Expenses:** Includes all costs related to liquidation.
3. **Secured Creditors:** Paid to the extent of their security.
4. **Preferential Creditors:** Wages, taxes due to government, etc.
5. **Debenture Holders (with floating charge):** After paying preferential creditors.
6. **Unsecured Creditors:** Includes trade creditors and others.
7. **Shareholders:** Any remaining amount is paid to shareholders.

Liquidator's Final Statement of Account:

This is a summary showing:

- Realization of assets
- Payment to various stakeholders in the correct order
- Surplus or deficiency at the end

It is prepared as follows:

Receipts Side:

- Proceeds from asset sales
- Interest on investments, etc.

Payments Side:

- Liquidator's expenses
- Secured creditors
- Preferential creditors
- Unsecured creditors
- Return of capital to shareholders

This statement ensures transparency and accountability in the winding-up process.

Q2. Write a detailed note on Financial Reporting for Financial Institutions and the RBI guidelines applicable.

Ans: Financial reporting for financial institutions (mainly banks and NBFCs) involves the preparation and presentation of financial statements in accordance with regulatory guidelines issued by the Reserve Bank of India (RBI) and other statutory bodies.

Importance of Financial Reporting in Financial Institutions:

- Ensures regulatory compliance
- Helps in decision-making by stakeholders
- Provides information on risk, capital adequacy, and liquidity
- Ensures uniformity and comparability

RBI Guidelines for Financial Reporting:

The Reserve Bank of India provides detailed formats and instructions under:

1. **Master Circulars** on income recognition, asset classification, and provisioning (IRAC norms)
2. **Balance Sheet and P&L Format** under the Banking Regulation Act, 1949
3. **Statutory Disclosures** as per Basel norms and Ind AS (for scheduled banks and NBFCs)

Key Features of RBI Reporting:

- Banks must prepare **Schedules 1 to 16** attached to Balance Sheet and Profit & Loss Account
- Disclosure of **Non-performing Assets (NPAs)** and provisions
- Statement of Capital Adequacy and Tier I/II capital
- Reporting of **Rebate on Bills Discounted**
- Provision for standard and doubtful advances

Other Reporting Requirements:

- **Quarterly results** to stock exchanges (for listed entities)
- **CAR (Capital Adequacy Ratio)** must be disclosed
- **Segment reporting** for domestic and international operations

This ensures that stakeholders have a clear and accurate picture of the financial health and risk exposure of the financial institution.

Q3. The assets realized ₹5,00,000. The payments to be made:

- Liquidator's expenses: ₹10,000
- Secured Creditors: ₹2,00,000
- Preferential Creditors: ₹30,000
- Debentures: ₹1,50,000
- Unsecured Creditors: ₹70,000

Liquidator's Final Statement of Account:

Receipts Side:

- Asset Realization: ₹5,00,000

Payments Side:

1. Liquidator's Expenses: ₹10,000
2. Secured Creditors: ₹2,00,000
3. Preferential Creditors: ₹30,000

4. Debenture Holders: ₹1,50,000

5. Unsecured Creditors: ₹70,000

Total Payments = ₹4,60,000

Surplus Available: ₹5,00,000 – ₹4,60,000 = ₹40,000 (to be returned to shareholders if any capital exists) ✓

Q4. From the following information, calculate payment to equity shareholders:

- Share Capital: ₹3,00,000
- Debentures: ₹1,00,000
- Creditors: ₹1,50,000
- Assets Realized: ₹5,00,000
- Expenses: ₹10,000

Calculation:

Total Payments Before Shareholders:

- Debentures = ₹1,00,000
- Creditors = ₹1,50,000
- Expenses = ₹10,000

Total = ₹2,60,000

Available Funds = ₹5,00,000

Surplus for Shareholders = ₹5,00,000 – ₹2,60,000 = ₹2,40,000 ✓

But since Share Capital is ₹3,00,000 and surplus is only ₹2,40,000, payment will be: **Equity Shareholders get = ₹2,40,000** (partial payment)

Q5. Prepare a journal entry and working notes for the payment of debenture holders with interest accrued till liquidation date of ₹6,000.

Given:

Debentures: ₹1,00,000 Interest accrued: ₹6,000

Journal Entry:

Debenture Holders A/c Dr. ₹1,06,000

To Bank A/c ₹1,06,000

(Being payment of principal and interest on debentures)

Working Notes:

- Amount payable on debentures = Principal + Accrued Interest
- = ₹1,00,000 + ₹6,000 = ₹1,06,000

Debenture holders must be paid fully before unsecured creditors or shareholders.

Unit 3

Q1. Discuss the format of final accounts of a banking company as per the Banking Regulation Act.

Ans: The preparation of final accounts for banking companies in India is governed by the Banking Regulation Act, 1949. This Act provides a uniform and standardized format that ensures the consistency, transparency, and comparability of the financial statements of all banks operating in the country. The final accounts of banking companies include the **Balance Sheet (Form A)** and the **Profit and Loss Account (Form B)**, along with **Schedules** that provide detailed information and breakdowns of various items.

Form A – Balance Sheet

The Balance Sheet is structured to reflect the bank's financial position as of a particular date. It includes the following heads, each supported by a specific schedule:

1. **Capital (Schedule 1):** Details of authorized, issued, subscribed, and paid-up capital of the bank.
2. **Reserves and Surplus (Schedule 2):** Includes statutory reserves, capital reserves, revenue reserves, and other reserves.
3. **Deposits (Schedule 3):** Comprises demand deposits, savings deposits, and term deposits.
4. **Borrowings (Schedule 4):** Includes borrowings from RBI, other banks, and institutions in India or abroad.
5. **Other Liabilities and Provisions (Schedule 5):** Covers bills payable, provisions, accrued expenses, and other liabilities.
6. **Cash and Balances with RBI (Schedule 6):** Contains cash in hand and balances with the Reserve Bank of India.
7. **Balances with Banks and Money at Call (Schedule 7):** Includes balances with other banks and short-term funds.
8. **Investments (Schedule 8):** Investments in government securities, shares, bonds, and debentures.
9. **Advances (Schedule 9):** Loans, cash credits, overdrafts, and bills purchased or discounted.
10. **Fixed Assets (Schedule 10):** Covers premises, equipment, and other fixed assets.
11. **Other Assets (Schedule 11):** Includes accrued income, prepaid expenses, and other miscellaneous assets.

12. Contingent Liabilities (Schedule 12): Items not reflected directly in the balance sheet such as guarantees and acceptances.

Each schedule provides a detailed breakdown, which improves transparency and offers a better understanding of the financial condition of the bank.

Form B – Profit and Loss Account

The Profit and Loss Account shows the performance of the bank over a specific accounting period. It includes:

Income Side:

1. **Interest Earned (Schedule 13):** Includes interest on loans, advances, and investments.
2. **Other Income (Schedule 14):** Includes commission, exchange income, profit on sale of investments, etc.

Expenditure Side:

1. **Interest Expended (Schedule 15):** Interest paid on deposits and borrowings.
2. **Operating Expenses (Schedule 16):** Payments on salaries, rent, taxes, printing, communication, etc.
3. **Provisions and Contingencies:** Includes provisions made for bad debts, standard assets, taxation, etc.

After accounting for all incomes and expenses, the **Net Profit** is transferred to the reserves or paid out as dividends.

Objectives and Importance of Final Accounts Format

- Ensures **uniformity** across all banks.
- Helps in **regulatory compliance** with RBI norms.
- Facilitates **comparison and benchmarking** among banks.
- Improves **transparency** in financial disclosures.
- Helps stakeholders in **decision-making**.

Illustration – Balance Sheet Format (Form A)

Below is a simplified representation:

Liabilities	₹	Assets	₹
Capital	X	Cash and Balances	X
Reserves and Surplus	X	Investments	X

Liabilities	₹	Assets	₹
Deposits	X	Advances	X
Borrowings	X	Fixed Assets	X
Other Liabilities	X	Other Assets	X
Total	XXX	Total	XXX

Illustration – Profit and Loss Account (Form B)

Particulars	₹
Interest Earned	X
Other Income	X
Total Income	XXX
Interest Expended	X
Operating Expenses	X
Provisions & Contingencies	X
Total Expenses	XXX
Net Profit	XXX

Final accounts in the prescribed format help banks maintain consistency in their reporting and enable the Reserve Bank of India to monitor their operations efficiently. The use of schedules offers depth to financial disclosures and makes it easier for investors, regulators, and stakeholders to assess a bank's performance. The Banking Regulation Act's emphasis on this structure ensures uniformity, clarity, and financial discipline in the banking sector.

Q2. Write short notes on:

a. Provision for Bad Debts

Ans: Provision for bad debts is an accounting adjustment made by banks to set aside an estimated amount to cover potential loan defaults. Since all loans and advances do not guarantee recovery, banks must ensure that their books reflect the true realizable value of assets. The Reserve Bank of India (RBI) mandates specific provisioning norms based on the classification of assets as standard, sub-standard, doubtful, or loss assets.

Provisioning helps in portraying a realistic picture of a bank's profitability and ensures financial discipline. For example:

- Standard Assets: 0.25%–1% provisioning

- Substandard Assets: 10%–20%
- Doubtful Assets: 20%–100% depending on the duration

Provisions for bad debts are shown under the 'Expenditure' head in the Profit and Loss Account and deducted from advances in the Balance Sheet.

b. Rebate on Bills Discounted

Ans: Banks often discount bills of exchange before their due dates by charging interest upfront for the entire tenure. If the bill extends beyond the financial year, the unearned portion of this interest is called a rebate on bills discounted. This is treated as a liability because it relates to the next accounting period.

The formula for calculating rebate:

$$\text{Rebate} = \text{Bill Amount} \times \text{Rate} \times \text{Unexpired Period} / 12$$

For example, if a bill of ₹2,00,000 is discounted for 3 months at 12% annual rate, and 1 month remains unexpired on the balance sheet date:

$$\text{Rebate} = 2,00,000 \times 12\% \times 1/12 = ₹2,000$$

Rebate is deducted from interest income and shown as a current liability.

c. Interest on Doubtful Debts

Ans: Interest accrued on doubtful debts (loans that have not been serviced for 90 days or more) is not recognized as income unless it is actually received in cash. This conservative accounting approach is mandated by the RBI to avoid overstating income and ensures prudent revenue recognition.

Such interest is suspended and shown under contingent income or as a memorandum note. Once the amount is received, it is credited to the Profit and Loss Account.

Q3. From the following information, prepare the Profit and Loss Account of a bank:

Interest Earned: ₹10,00,000

Interest Expended: ₹6,00,000

Operating Expenses: ₹1,50,000

Other Income: ₹1,00,000

Provision for Bad Debts: ₹50,000

Ans:

In banking companies, the Profit and Loss Account is prepared in the format prescribed under **Form B** of the Third Schedule to the **Banking Regulation Act, 1949**. The P&L account reflects all incomes and expenditures for the financial year, including interest income, interest expended, operating expenses, and provisions.

Let's first briefly understand the key components:

Components of Bank Profit and Loss Account

1. Interest Earned (Schedule 13): This includes interest on loans, advances, bills discounted, and investments. It is the bank's main source of revenue.

2. Other Income (Schedule 14): Commissions, exchange income, profit from sale of investments, and miscellaneous incomes.

3. Interest Expended (Schedule 15): Interest paid on deposits and borrowings.

4. Operating Expenses (Schedule 16): Expenses related to salaries, rent, stationery, legal charges, etc.

5. Provisions and Contingencies: This includes provisions for bad debts, standard and non-performing assets, tax provisions, etc.

Step-by-Step Calculation:

Particulars	₹
I. Income	
1. Interest Earned	10,00,000
2. Other Income	1,00,000
Total Income	11,00,000

| **II. Expenditure** || | 1. Interest Expended | 6,00,000 | | 2. Operating Expenses | 1,50,000 | | 3. Provision for Bad Debts | 50,000 | | **Total Expenditure** | **8,00,000** |

| **Net Profit for the Year** | **3,00,000** |

Illustration: Profit and Loss Account (Form B Format)

XYZ Bank Ltd.

Profit and Loss Account for the Year Ending 31st March XXXX

Particulars	₹
I. Income	
Interest Earned	10,00,000
Other Income	1,00,000
Total	11,00,000

| **II. Expenditure** || | Interest Expended | 6,00,000 | | Operating Expenses | 1,50,000 | | Provisions and Contingencies | 50,000 | | **Total** | **8,00,000** |

| **III. Profit/Loss** || | Profit for the year carried to Balance Sheet | **3,00,000** |

Notes and Explanations:

1. **Provision for Bad Debts:** This is made as per RBI norms and ensures the bank accounts for expected losses.
2. **Operating Expenses:** It includes salary to staff, rent, depreciation, etc., forming the administrative overhead.
3. **Net Profit Calculation:** The difference between total income and total expenditure gives the net profit before tax and appropriations.
4. **Other Income:** Represents fee-based income that is not from core lending operations, such as commissions or treasury profits.

The Profit and Loss Account prepared above provides a snapshot of the bank's performance. The net profit of ₹3,00,000 indicates a positive margin. It demonstrates the operational efficiency of the bank, and the structured format ensures compliance with statutory norms under the Banking Regulation Act. Such systematic presentation enables regulators, investors, and analysts to evaluate the profitability and sustainability of banking operations accurately.

Q4. Calculate rebate on bills discounted:**Given:**

- Total Bills = ₹3,00,000
- Unexpired Period = 2 months
- Annual Discount Rate = 12%

Ans: Rebate on bills discounted refers to the portion of discount that is not yet earned by the bank, because the bills will mature in the next accounting period. It is calculated on the basis of the outstanding or unexpired period and the agreed annual rate of discount.

This unearned discount is treated as a liability in the bank's balance sheet and is shown under the head "Other Liabilities and Provisions" because it represents income that belongs to the next accounting period.

Formula to Calculate Rebate:

$$\text{Rebate} = \text{Total Bills} \times \text{Discount Rate} \times \text{Unexpired Period} / 12$$

Substituting the given values:

$$\begin{aligned}\text{Rebate} &= ₹3,00,000 \times 12\% \times 2/12 \\ &= ₹3,00,000 \times 0.02 \\ &= ₹6,000\end{aligned}$$

Journal Entry for Rebate on Bills Discounted:

Interest Earned A/c Dr. ₹6,000
To Rebate on Bills Discounted A/c ₹6,000

(Being transfer of unearned interest to liability)

Accounting Treatment:

1. **In Profit and Loss Account:** The rebate is deducted from total interest income.
 2. **In Balance Sheet:** It appears as a liability under "Other Liabilities and Provisions."
-

Importance of Rebate:

1. **Accrual Basis of Accounting:** It ensures that income is matched with the period it is earned.
 2. **Regulatory Compliance:** Fulfills RBI's requirement for accurate income reporting.
 3. **Fair Presentation:** Prevents overstatement of profits.
-

Example Scenario:

If a bank discounts a bill of ₹3,00,000 on 1st March at 12% annual rate for 3 months, and the accounting year ends on 31st March, the unexpired period is 2 months.

Rebate on this bill = ₹3,00,000 × 12% × 2/12 = ₹6,000

Thus, ₹6,000 must be deducted from interest income of the current year and recorded as a liability to be recognized in the next accounting year.

Rebate on bills discounted is an essential adjustment in bank accounting, ensuring that income recognition follows the correct period of accrual. Accurate calculation and reporting of rebate maintains the integrity of financial statements and is a regulatory requirement for all banking institutions.

Q5. From the following balances, prepare a Balance Sheet in prescribed format:

- Capital ₹10,00,000
- Reserves ₹3,00,000
- Deposits ₹15,00,000
- Investments ₹8,00,000
- Loans ₹7,00,000
- Cash ₹2,00,000
- Other Liabilities ₹1,00,000
- Fixed Assets ₹2,00,000

Ans: As per the Banking Regulation Act, 1949, every banking company is required to prepare its Balance Sheet in the format prescribed under **Form A** of the **Third Schedule**. The Balance Sheet includes various heads like Capital, Reserves, Deposits, Borrowings, Investments, Loans, etc., which are detailed in Schedules 1 to 12.

Below is the preparation of the Balance Sheet in the prescribed format using the given balances:

XYZ Bank Ltd.

Balance Sheet as on 31st March XXXX

Liabilities	Amount (₹)	Assets	Amount (₹)
Schedule 1: Capital	10,00,000	Schedule 6: Cash & Balances with RBI	2,00,000
Schedule 2: Reserves & Surplus	3,00,000	Schedule 8: Investments	8,00,000
Schedule 3: Deposits	15,00,000	Schedule 9: Advances (Loans)	7,00,000
Schedule 5: Other Liabilities	1,00,000	Schedule 10: Fixed Assets	2,00,000
		Schedule 11: Other Assets (bal. fig.)	10,00,000
Total	29,00,000	Total	29,00,000

Notes:

1. **Capital and Reserves** appear under Schedules 1 and 2.
2. **Deposits** represent public liabilities and are shown under Schedule 3.
3. **Investments** include securities held by the bank and go under Schedule 8.
4. **Loans and Advances** are included in Schedule 9.
5. **Cash in hand** and with RBI is shown in Schedule 6.
6. **Other Liabilities** include any unpaid expenses or provision liabilities.
7. **Fixed Assets** like building, furniture, etc., go under Schedule 10.
8. **Other Assets** is the balancing figure, assuming no information on accrued income, etc., was provided.

This Balance Sheet follows the prescribed format under the Banking Regulation Act. All figures are shown under appropriate schedules and classified under either liabilities or assets. Preparing financial statements in this format ensures compliance and helps users analyze the bank's financial health accurately.

Unit – 4

Q1. Explain the concept of consolidated balance sheet. How is it prepared by a holding company?

Ans: A consolidated balance sheet is a financial statement that combines the assets, liabilities, and equity of a parent company and its subsidiaries, presenting them as a single entity. It is prepared to reflect the financial position of the group as a whole and eliminates intra-group transactions.

When a holding company controls one or more subsidiary companies (generally by holding more than 50% of the shares), it is required to prepare consolidated financial statements. This includes a consolidated balance sheet that presents the financial data of all the companies in the group in a unified manner.

Objectives:

- To provide a true and fair view of the financial position of the group.
- To eliminate the effects of intra-group transactions.
- To give stakeholders a clear picture of the group’s assets, liabilities, and equity.

Preparation Steps:

1. **Combine like items:** Add assets, liabilities, and equity items of the parent and subsidiaries line by line.
2. **Eliminate investments:** The investment made by the holding company in the shares of the subsidiary is eliminated against the subsidiary’s share capital.
3. **Calculate Minority Interest:** Share of net assets of subsidiary attributable to shareholders other than the holding company is shown separately as a liability.
4. **Compute Cost of Control (Goodwill or Capital Reserve):**
 - If the cost of investment is more than the holding’s share of net assets, the excess is goodwill.
 - If it is less, the difference is a capital reserve.
5. **Adjust Inter-company transactions:** Cancel out mutual obligations such as:
 - Inter-company receivables and payables
 - Inter-company profits in stock or assets
 - Inter-company bills and debentures
6. **Prepare the Final Consolidated Balance Sheet:** Present the total assets and liabilities after adjustments, including minority interest and goodwill or capital reserve.

Format (simplified):

Liabilities	₹	Assets	₹
Share Capital (of Holding Co.)	xxxxx	Fixed Assets	xxxxx
Reserves & Surplus	xxxxx	Current Assets	xxxxx
Minority Interest	xxxxx	Goodwill/Capital Reserve	xxxxx

Liabilities	₹	Assets	₹
Other Liabilities	xxxxx	Less: Inter-company balances	(xxxxx)
Total	xxxxx	Total	xxxxx

Importance:

- Provides a comprehensive financial view.
- Required for compliance with legal and accounting standards.
- Helps investors, lenders, and management to assess overall performance.

Q2. Define minority interest and cost of control. How are inter-company transactions treated in consolidation?

Ans:

Minority Interest:

Minority interest (also called non-controlling interest) is the portion of the subsidiary's net assets and profits that belong to shareholders other than the holding company.

Formula: Minority Interest = % not held by holding company × (Share Capital + Reserves + Post-acquisition Profits of Subsidiary)

It is shown separately on the liabilities side of the consolidated balance sheet.

Cost of Control:

Cost of control is the difference between the price paid by the holding company for the shares of the subsidiary and the proportionate share of net assets acquired.

- If investment > share in net assets ⇒ **Goodwill**
- If investment < share in net assets ⇒ **Capital Reserve**

Formula: Cost of Control = Investment – Holding's Share in Net Assets

Example:

Let's say Holding Co. acquires 80% of Subsidiary Co. for ₹1,80,000. Subsidiary's Share Capital is ₹2,00,000 and Reserves ₹50,000.

- Net assets = ₹2,50,000
- Holding's Share = ₹2,50,000 × 80% = ₹2,00,000
- Investment = ₹1,80,000

Cost of Control = ₹1,80,000 – ₹2,00,000 = (₹20,000) ⇒ Capital Reserve

Minority Interest = 20% × ₹2,50,000 = ₹50,000

Inter-company Transactions:

During consolidation, all inter-company transactions must be eliminated to avoid overstatement:

1. Inter-company Debts:

If the holding company shows a debtor balance from the subsidiary, and the subsidiary shows a creditor balance from the holding, these are eliminated.

2. Unrealized Profits:

If stock is sold by one company to another in the group and remains unsold at year-end, any profit included in this stock must be eliminated from consolidated profit and inventory.

3. Inter-company Bills and Loans:

Bills receivable/payable, and loans/advances given within the group must be adjusted against each other.

Purpose of Elimination:

- To ensure the consolidated statements reflect only external transactions.
- To avoid overstatement of assets, liabilities, income, or expenses.

Minority interest and cost of control are critical components in consolidation. Accurate treatment of inter-company transactions is essential to ensure that the consolidated balance sheet reflects the true financial position of the group.

Q3. H Ltd. holds 80% shares in S Ltd. The balance sheets show:

- Share Capital of S Ltd.: ₹2,00,000
- Reserves: ₹50,000
- H Ltd. paid ₹1,80,000 for its share.

Calculate cost of control and minority interest.

Ans: To calculate cost of control and minority interest, we begin by finding the total net assets of S Ltd. and compute the holding and minority share.

Step 1: Compute Net Assets of Subsidiary

Net Assets = Share Capital + Reserves = ₹2,00,000 + ₹50,000 = ₹2,50,000

Step 2: Compute Holding Company's Share in Net Assets

Holding Percentage = 80% Holding's Share = ₹2,50,000 × 80% = ₹2,00,000

Step 3: Investment by H Ltd.

Investment in S Ltd. = ₹1,80,000

Step 4: Cost of Control

Cost of Control = Investment – Share in Net Assets = ₹1,80,000 – ₹2,00,000 = **(₹20,000)** (Capital Reserve)

Step 5: Minority Interest

Minority Share = 20% of ₹2,50,000 = ₹50,000

Conclusion:

- **Cost of Control (Capital Reserve)** = ₹20,000
- **Minority Interest** = ₹50,000

This treatment reflects the holding’s economic interest and adjusts the difference as goodwill or capital reserve.

Q4. From the following information, prepare a Consolidated Balance Sheet:

- H Ltd. Share Capital ₹5,00,000
- S Ltd. Share Capital ₹2,00,000
- H Ltd. holds 75% of S Ltd.
- Profits of S Ltd. before acquisition: ₹20,000; after acquisition: ₹30,000
- Inter-company owing: ₹10,000
- Unrealized profit in stock: ₹5,000

Ans: To prepare the consolidated balance sheet, we need to eliminate inter-company balances, compute cost of control, and calculate adjusted profits.

Step 1: Compute Net Assets of S Ltd.

Share Capital + Reserves = ₹2,00,000 + ₹20,000 + ₹30,000 = ₹2,50,000

Step 2: Holding Company’s Share = 75%

Holding’s Share in Net Assets = ₹2,50,000 × 75% = ₹1,87,500

Step 3: Minority Interest = 25%

= ₹2,50,000 × 25% = ₹62,500

Step 4: Post-Acquisition Profit Share for H Ltd.

= 75% × ₹30,000 = ₹22,500

Step 5: Unrealized Profit Adjustment

Unrealized profit = ₹5,000 to be reduced from stock and profits

Step 6: Consolidated Share Capital = ₹5,00,000

Step 7: Consolidated Reserves = ₹22,500 – ₹5,000 = ₹17,500

Final Consolidated Balance Sheet:

Liabilities	₹	Assets	₹
Share Capital (H Ltd.)	5,00,000	Fixed & Current Assets	Balancing
Reserves & Surplus	17,500	Inter-company Due Adjusted	

Minority Interest	62,500		
Total	5,80,000	Total	5,80,000

Q5. Calculate the adjusted profit of holding company after consolidation:

- Holding company's profit: ₹3,00,000
- Share in subsidiary's post-acquisition profit: ₹25,000
- Less: Unrealized profit in inventory: ₹5,000
- Less: Dividend received from pre-acquisition profit: ₹10,000

Ans:

Step-by-step:

1. Holding Company Profit = ₹3,00,000
2. Add: Share in Post-acquisition Profits = ₹25,000
3. Less: Unrealized Profit = ₹5,000
4. Less: Pre-acquisition Dividend = ₹10,000

Adjusted Consolidated Profit = ₹3,00,000 + ₹25,000 – ₹5,000 – ₹10,000 = ₹3,10,000

This amount will be shown under consolidated reserves and surplus in the balance sheet.