

## AMALGAMATION, ABSORPTION & RECONSTRUCTION

### 1. Method to calculate Purchase Consideration:

Net Asset method	Intinsic value method	Net payment method
Agreed value of assets taken over                   xxx <b>Less:</b> Agreed value of Liab. taken over                   xxx <b>PC</b> xxx	MV of total assets                   xxx <b>Less:</b> MV of total Liab.           xxx Net intrinsic value                   xxx <hr/> Intrinsic Value = $\frac{\text{Net Intrinsic value}}{\text{No. of equity share}}$ Per share                                No. of equity share <hr/> <b>PC</b> = No. of equity shares purchased X Intrinsic value per share of vendor company	Amalgamation in nature of: - <b>Merger:</b> Amount paid to Equity shareholders only in the form of equity shares in purchasing company except cash for fraction of shares. <b>Purchase:</b> Cash and agreed value of shares, debentures and other assets given by purchasing company to the liquidator of vendor company <b>For the Shareholders</b> of vendor company.

**Note:** If information about all the three method is given in the question then we should follow **Net payment method**.

### 2. Amalgamation in nature of merger: Amalgamation deemed to be in the nature of merger if following conditions are satisfied: -

**(BARED)**

- ◆ **B**usiness of vendor company must be carried on by the purchasing company.
- ◆ **A**ll assets and liabilities of vendor company transferred to purchasing company.
- ◆ **R**ecorded in new company of assets and liabilities taken over at Book Value of vendor company. (Except to comply with accounting policy)
- ◆ **E**quity shareholders holding 90% shares (except already held) agree to become shareholders in new company.
- ◆ **D**isbursement of Purchase Consideration only in shares except cash for fraction of shares.

### 3. Entries in books of vendor company:

a) **Realisation account:** We have to follow the following procedure

- ◆ Transfer all **real** assets to debit side at **Gross Book Value** including goodwill but excluding fictitious assets.
- ◆ Transfer all **outside** liabilities to credit side at **Gross Book Value** but excluding accumulated reserves and surplus.
- ◆ If any asset/liabilities not taken over than any realisation on sale of such asset or payment on disbursement of such liabilities is credited/debited to realisation account.
- ◆ Amount of Purchase Consideration is credited to realisation account.
- ◆ Liquidation expenses debited to realisation account if born by vendor company
- ◆ Realisation account is balanced and the balance of this account is profit or loss on realisation, which is transferred to Equity Shareholders Account.

**Notes:**

1. **Assets not taken over if transferred to shareholders account:** it must be shown on debit side of shareholders account at **Current Value** of such asset and a corresponding credit is made to realisation account.

2. **What are outside liabilities:** Preference shareholders and Debenture holders are treated outside liabilities. But proposed dividend is not treated outside liabilities.
3. **If against any reserve there is any expected liabilities:** then to the extent of that expected liability the amount of reserve is transferred to realisation account and balance to shareholders account as usual.

**Example:**

Workmen compensation reserve given in Balance sheet = 8000

Expected liability to workmen =5000.

Therefore Rs 5000 will be transferred to the credit side of realisation account and balance Rs 3000 to the credit side of shareholders account.

4. **Any inter company owings or adjustments:** is ignored while preparing vendor company books, it is considered only while preparing purchasing company books.

**b) Equity Shareholders Account:**

- ◆ **Credit side:** Equity Share Capital, Accumulated profits and reserves, balance of realisation account.
- ◆ **Debit side:** Accumulated losses, Fictitious asset, amount of Purchase Consideration, balance of realisation account.

**c) Purchasing Company Account:**

- ◆ **Credit side:** Amount of Purchase Consideration due.
- ◆ **Debit side:** Discharge of Purchase Consideration.

**4. Entries in books of Purchasing Company**

**a) Three basic entries**

<b><u>For purchase consideration due</u></b>	
Business purchase a/c	Dr.
To liquidator of vendor company	
<b><u>For assets and liabilities taken over</u></b>	
Assets taken over	Dr.
Goodwill a/c	Dr.
To liabilities taken over	
To business purchase a/c	
To capital reserve a/c	
<b><u>For discharge of purchase consideration</u></b>	
Liquidator of vendor company a/c	Dr.
To equity share capital a/c	
To share premium a/c	
To debentures a/c	
To preference share capital a/c	
To cash	

**b) For liquidation expenses paid by purchasing company**

Goodwill/Capital reserve a/c	Dr.
To cash a/c	

**c) For cancellation of mutual owings**

Creditor /Bills payable a/c	Dr.
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To Debtors/Bills receivable a/c
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**d) For adjustment of unrealised profit**

Goodwill/Capital reserve a/c	Dr.
To Stock a/c	

**e) For carry forward of statutory reserves**

Amalgamation adjustment a/c	Dr.
To Statutory reserve a/c	

**f) If both capital reserve and goodwill appears in books**

Capital reserve a/c	Dr.
To Goodwill a/c	

**Note:**

- ◆ **Amalgamation in nature of merger:** The entries in the case of amalgamation in the nature of merger is almost similar to the entries given above, the only difference is:
  - ✓ In the second basic entry above, instead of opening the Goodwill/Capital reserve a/c, the difference between purchase consideration paid and book value of the share capital of **vendor company** is adjusted in general reserve. If general reserve is not sufficient then balance adjusted in profit & loss account. Similarly any difference in actual debenture value and the amount paid to them is also adjusted to general reserve. If general reserve is not sufficient then balance adjusted in profit & loss account.
  - ✓ Where ever Goodwill/Capital reserve a/c is debited or credited in above entries we will have to debit or credit general reserve account.
- ◆ Following will remain same in both the methods of amalgamation
  - ✓ Calculation of Purchase consideration.
  - ✓ Discharge of Purchase consideration.
  - ✓ Entries in books of vendor company.

**5. Inter company holding**

Purchasing company held shares in vendor company (P→V)	Vendor company held shares in purchasing company (V→P)	Both vendor and purchasing company held shares in each other (P↔V)
<b>Calculation of purchase consideration</b>		
PC (Given/calculated) xxx	PC (Given/calculated)	PC (Given/calculated) xxx
Less: % reduction for shares Held by purchasing company in vendor company xxx	xxx	Less: % reduction for shares Held by purchasing company in vendor company xxx
Net PC xxx	Less: Value of shares Held by vendor company in purchasing company xxx	Less: Value of shares Held by vendor company in purchasing company xxx
	Net PC xxx	Net PC xxx
	xxx	xxx

$\% = \frac{\text{Shares held by X}}{\text{Total shares of vendor comp.}} \times 100$ <b>purch. comp.</b>		<b>Value= No of shares held X</b> <b>Intrinsic value per share</b>			
<b>Books of Vendor company</b>					
<b>Realisation account</b>			<b>Realisation account</b>		
All assets					

**6. Other key points:**