JMC vLearning
"your virtual learning partner"

Consolidated Financial Statements
Section 01

Mr. Nazeel Mohamad

ජයසේකර කළමනාකරණ මධ්‍යස්ථානය
JMC JAYASEKERA MANAGEMENT CENTRE (PVT) LTD Estd. 1972

JMC Jayasekera Management Centre (Pvt) Ltd
Pioneers in Professional Education
65/2A, Chittampalam Gardiner Mawatha, Colombo 02 | T: +94 112 430451 | E: info@jmc.lk | F: +94 115 377917

Section 01

Key Terms

1. A business combination is: Transaction or event in which acquirer obtains control over a business (e.g. acquisition of shares or net assets, legal mergers, reverse acquisitions).

2. Definition of a Business: An integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing goods or services to customers, generating investment income (such as dividends or interest) or generating other income from ordinary activities.

3. The acquisition method, an entity shall account for each business combination by applying the acquisition method. Applying the acquisition method requires:

   a) identifying the acquirer;

      a. The entity that obtains control of the acquire,
      b. So an acquiree is , The business or business that the acquirer obtains control of in a business combination.

   b) determining the acquisition date; The date on which the acquirer obtains control of the acquire
   c) recognizing and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquire;
   d) and recognizing and measuring goodwill or a gain from a bargain purchase.

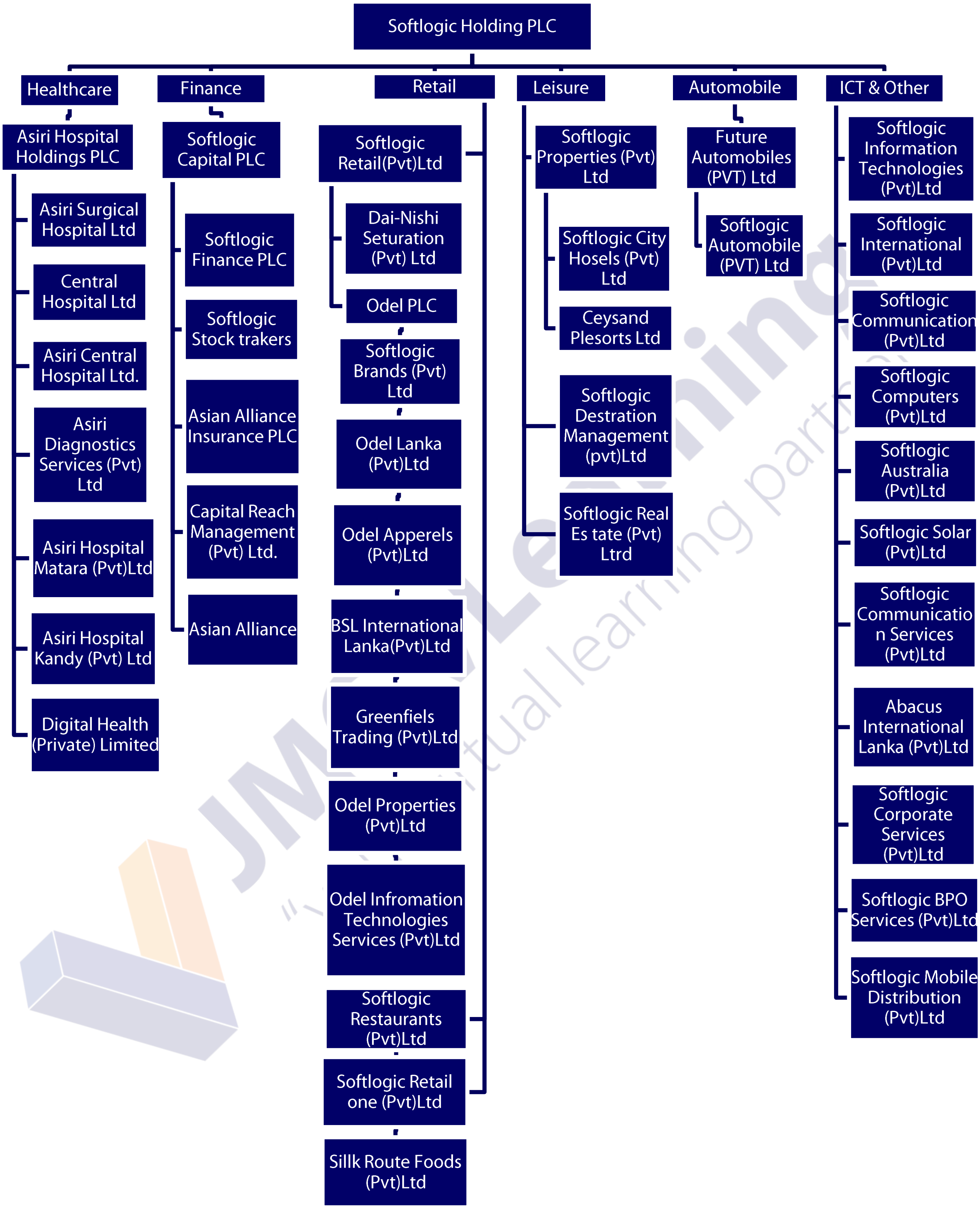
4. Group; A parent and its subsidiaries.
5. Parent; An entity that controls one or more entities.
6. Subsidiary; An entity that is controlled by another entity.

7. Control of an investee; An investor <u>controls an investee when the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.</u>

8. Consolidated financial statements; The financial statements of a group in which the assets, liabilities, equity, income, expenses and cash flows of the parent and its subsidiaries are presented as those of a single economic entity.

9. Non-controlling interest Equity in a subsidiary not attributable, directly or indirectly, to a parent.

Group Structure



Section 02

Consolidation Procedures

1. SLFRS 03, provides guidance for the accounting for business combinations. So will study how to account followings
   a. Investment made by parent
   b. Book value of net assets in subsidiary (Refer Step 12 for FV of NA)
   c. How to recognize and measure goodwill or GBP
   d. How to recognize and measure NCI
2. SLFRS 10, provide guidance for the preparation of consolidated financial statement and the procedure are as follows,

   Consolidation procedures

   Consolidated financial statements:

a) combine like items of assets, liabilities, equity, income, expenses and cash flows of the parent with those of its subsidiaries.

b) offset (eliminate) the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary (SLFRS 3 explains how to account for any related goodwill).

c) eliminate in full intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between entities of the group

d) profits or losses resulting from intragroup transactions that are recognized in assets, such as inventory and fixed assets, are eliminated in full.

e) Intragroup losses may indicate an impairment that requires recognition in the consolidated financial statements. LKAS 12 Income Taxes applies to temporary differences that arise from the elimination of profits and losses resulting from intragroup transactions.

<u>Step 01 - Investment made by the parent should be netted off against the net assets in subsidiary on the date of acquisition.</u>

Question 01.01

Description	A Ltd	B Ltd
Non-Current Assets	15,000.00	8,000.00
Investments B 100%	10,000.00	
Current Assets	5,000.00	7,000.00
Total	30,000.00	15,000.00
Stated Capital	15,000.00	10,000.00

Reserves	7,000.00	-
Liabilities	8,000.00	5,000.00
Total	30,000.00	15,000.00

Question 01.02

Description	A Ltd	B Ltd
Non Current Assets	25,000.00	15,000.00
Investments (B) 100%	12,000.00	
Investments (C)	5,000.00	7,000.00
Current Assets	8,000.00	7,000.00
Total	50,000.00	22,000.00
Stated Capital	30,000.00	12,000.00
Reserves	15,000.00	-
Liabilities	5,000.00	10,000.00
Total	50,000.00	22,000.00

Question 01.03

Description	A Ltd	B Ltd
Non-Current Assets	15,000.00	75,000.00
Investments B Ltd 100%	100,000.00	
Current Assets	88,000.00	70,000.00
Total	330,000.00	145,000.00
Stated Capital	200,000.00	100,000.00
Reserves	70,000.00	-
Liabilities	60,000.00	45,000.00
Total	330,000.00	145,000.00

Section 03

Step 02 – Goodwill

Goodwill is the excess consideration paid by the parent compared with the net assets in subsidiary, which is calculated as follows

Investment Made by the Parent = XXXXX

Less – NA in Subsidiary = (XXX)

Goodwill = XX

Please note, we have not yet discussed the NCI and Fair value adjustment in subsidiary

Working - goodwill calculation

Investment Made by the Parent = 12,000.00

Less- Net Assets in Subsidiary = 10,000.00

So Goodwill = 2,000.00

The Goodwill arising on consolidation should be recognized as an asset in the consolidated FS, subject to annual impairment assessment.

Question 02.01

Description	A Ltd	B Ltd
Non-Current Assets	15,000.00	8,000.00
Investments in B 100%	12,000.00	
Current Assets	5,000.00	
Total	32,000.00	
Stated Capital	15,000.00	10,000.00
Reserves	7,000.00	-
Liabilities	10,000.00	5,000.00
Total	32,000.00	15,000.00

Question 02.02

Description	A Ltd	B Ltd
Non-Current Assets	25,000.00	15,000.00
Investments in B 100%	15,000.00	
Current Assets	8,000.00	7,000.00
Total	48,000.00	22,000.00
Stated Capital	25,000.00	12,000.00
Reserves	15,000.00	
Liabilities	8,000.00	
Total	48,000.00	22,000.00

Question 02.03

Description	A Ltd	B Ltd
Non-Current Assets	150,000.00	75,000.00
Investments in B 100%	120,000.00	
Current Assets	80,000.00	70,000.00
Total	350,000.00	145,000.00
Stated Capital	200,000.00	100,000.00
Reserves	70,000.00	-
Liabilities	80,000.00	45,000.00
Total	350,000.00	145,000.00

Step 03 - Gain on bargain Purchase

Occasionally, an acquirer will make a bargain purchase, which is a business combination in which the fair value of net assets in subsidiary exceeds the aggregate of the amounts of parent's investment and NCI.

If that excess remains after reassessment, the acquirer shall recognize the resulting gain in profit or loss on the acquisition date. The gain shall be attributed to the acquirer.

Working - goodwill calculation

Investment Made by the Parent = 8,000.00

Less- Net Assets in Subsidiary = 10,000.00

So GBP = 2,000.00

The GBP arising on consolidation should be recognized as an income in the consolidated FS (Attributed to parent)

Question 03.01

Description	A Ltd	B Ltd
Non-Current Assets	15,000.00	8,000.00
Investments in B 100%	8,000.00	
Current Assets	5,000.00	7,000.00
Total	28,000.00	15,000.00
Stated Capital	15,000.00	10,000.00
Reserves	7,000.00	-
Liabilities	6,000.00	5,000.00
Total	28,000.00	15,000.00

Question 03.02

Description	A Ltd	B Ltd
Non-Current Assets	25,000.00	15,000.00
Investments in B 100%	11,000.00	
Current Assets	8,000.00	7,000.00
Total	44,000.00	22,000.00
Stated Capital	25,000.00	12,000.00
Reserves	11,000.00	-
Liabilities	8,000.00	10,000.00
Total	44,000.00	22,000.00

Question 03.03

Description	A Ltd	B Ltd
Non-Current Assets	150,000.00	75,000.00
Investments in B 100%	75,000.00	
Current Assets	80,000.00	70,000.00
Total	305,000.00	145,000.00
Stated Capital	200,000.00	100,000.00
Reserves	25,000.00	-
Liabilities	80,000.00	45,000.00
Total	305,000.00	145,000.00

Key point

1. If investment by parent is equal to net assets in subsidiary, then no goodwill
2. If investment by parent is greater than net assets in subsidiary, goodwill should be identified
3. If investment by parent is lesser than net assets in subsidiary, GBP should be identified

Section 04

Step 04 – Pre and Post Profits and Reserves

SLFRS 03 requires the parent to compare the net assets in subsidiary,

Net Assets = Total Assets – Total Liabilities, in subsidiary or alternatively the aggregate of stated capital and retained earnings, therefore the Pre-Acquisition reserves and profits should be taken to the goodwill calculation.

Any profit after acquisition, are the profit generated from our investment. Accordingly, such profit will be consolidated with parents' profits (or proportionally share between parent and NCI)

Working - goodwill calculation

Investment Made by the Parent	=	12,000.00
Less- Net Assets in Subsidiary	=	
Stated Capital	=	10,000.00
Pre-Profits	=	1,000.00
So Goodwill	=	1,000.00

Example of goodwill calculation

Question 04.01

Description	A Ltd	B Ltd
Non-Current Assets	25,000.00	12,000.00
Investments in B 100%	12,000.00	
Current Assets	5,000.00	7,000.00
Total	42,000.00	19,000.00
Stated Capital	25,000.00	10,000.00
Reserves	7,000.00	4,000.00
Liabilities	10,000.00	5,000.00
Total	42,000.00	19,000.00

At the date of acquisition retained earnings of subsidiary was 1,000

Question 04.02 – (Post Loss In subsidiary)

Description	A Ltd	B Ltd
Non-Current Assets	35,000.00	25,000.00
Investments in B 100%	27,500.00	
Current Assets	8,000.00	7,000.00
Total	70,500.00	32,000.00
Stated Capital	35,000.00	15,000.00
Reserves	22,500.00	7,000.00
Liabilities	13,000.00	10,000.00
Total	70,500.00	32,000.00

At the date of acquisition retained earnings of subsidiary was 9,000

Working – Goodwill

Investment by Parent	27,500
Less – NA	
Stated Capital	(15,000)
Pre-Profit	(9,000)
Goodwill	3,500
Working – Consolidated Profit	
Parent Profit	22.500

Post – Loss	(2,000)
Consolidated Profit	20,500

Question 04.03

Description	A Ltd	B Ltd
Non-Current Assets	150,000.00	76,000.00
Investments in B 100%	120,000.00	
Current Assets	80,000.00	70,000.00
Total	350,000.00	146,000.00
Stated Capital	200,000.00	100,000.00
Reserves	70,000.00	1,000.00
Liabilities	80,000.00	45,000.00
Total	350,000.00	146,000.00

At the date of acquisition retained earnings of subsidiary was 1,500

Revision Question

Volcano Co acquired 100% of the equity share capital of Lava Co on 1January 20X3. The retained profits of the two individual companies at the beginning and end of their financial year were as follows.

	Volcano Co	Lava Co
	$'000	$'000
Retained earnings at 1 January 20 X 3	596	264
Retained earnings at 31 December 20 X 3	650	336

What is the parent company's share of consolidated retained earnings that should be reported in the consolidated statement of financial position of the Volcano Group at 31 December 20 X 3?

A. $668,000

B. $674,000

C. $704,000

D. $722,000

Tin Co acquired 100% of the equity share capital of Drum Co on 1 January 20X3. The following information relates to the financial year to 31 December 20X3 for each company.

	Tin Co	Drum Co
	$'000	$'000

Retained earnings at 1 January 20 X 3	840	170
Profit for the year	70	60
Retained earnings at 31 December 20 X 3	910	230

Neither company paid any dividends during the year.

What is the parent company's share of consolidated retained earnings that should be reported in the consolidated statement of financial position of the Tin Group at 31 December 20 X 3.

A. $83,500

B. $110,500

C. $130,000

D. $970,000

Step 05 - Goodwill Impairment

The goodwill arising on business combination should be tested for impairment annually (SLFRS 03 and LKAS 36)

Any impairment should be accounted as

Dr. Consolidated Retained Earnings	=	xxxx	
Cr. Goodwill	=		xxxx

If NCI measured at the Fair value method,

Dr. Consolidated Retained Earning	=	xxxxx (Parent Portion)	
Dr. NCI	=	xxxxx (NCI Portion)	
Cr. Goodwill	=		xxxx

Question 05.01

Description	A Ltd	B Ltd
Non-Current Assets	15,000.00	8,000.00
Investments in B 100%	12,000.00	
Current Assets	5,000.00	7,000.00
Total	32,000.00	15,000.00
Stated Capital	15,000.00	10,000.00
Reserves	7,000.00	-
Liabilities	10,000.00	5,000.00
Total	32,000.00	15,000.00

Goodwill was impaired by 500, assumed no profit in subsidiary.

Question 05.02

Description	A Ltd	B Ltd
Non-Current Assets	25,000.00	15,000.00
Investments in B 100%	15,000.00	
Current Assets	8,000.00	9,000.00
Total	48,000.00	24,000.00
Stated Capital	25,000.00	12,000.00
Reserves	15,000.00	2,000.00
Liabilities	8,000.00	10,000.00
Total	48,000.00	24,000.00

Pre-profit at the date acquisition was 1,000.00 in B Ltd

Goodwill was impaired by 1000,

Question 05.03

Description	A Ltd	B Ltd
Non-Current Assets	150,000.00	75,000.00
Investments in B 100%	120,000.00	
Current Assets	80,000.00	75,000.00
Total	350,000.00	150,000.00
Stated Capital	200,000.00	100,000.00
Reserves	70,000.00	5,000.00
Liabilities	80,000.00	45,000.00
Total	350,000.00	150,000.00

Pre-profit in B Ltd was 3,000.00

Goodwill was impaired by 2500,

Section 05

Step 06 - Non-controlling Interest

Up-to now we assumed the parent has acquired subsidiary 100% , in the practical scenario parent want to establish the control to consolidate the subsidiary companies and this can be achieved through.

1. Obtaining more than 50% of voting right
2. Appointing majority of BOD
3. Through an agreement or statute.

Rest of the alternatives were excluded, as such were not related to the syllabus.

Accordingly, NCI represent amount of equity attributed to non-group shareholders. Therefore the NCI should recorded within the equity but separately from parent's equity.

Further the NCI can be measured under the

1. % of Net Assets Method (Subsidiary NA * NCI%)
2. Fair Value Method (No. of Share * Mkt Price or will be given in the exam)

Further any GBP, is only attributed to Parent Only.

Test your Understanding 1

Daniel acquired 80% of the ordinary share capital of Craig on 31 December 20X6 for $78,000. At this date the net assets of Craig were $85,000.

What goodwill arises on the acquisition?

I. If the NCI is valued using the proportion of net assets method

II. If the NCI is valued using the fair value method and the fair value of the NCI on the acquisition date is $19,000?

Working – Goodwill

	% NA	FV
Investment Made by Parent	78,000	78,000
Add NCI (85,000*.20%)	17,000	(FV Given) 19,000
Total	95,000	97,000
Less Net Assets in Subsidiary	(85,000)	(85,000)
Goodwill	10,000	12,000

According to FV Method the goodwill was 12,000, the incremental goodwill in attributed to NCI and any impairment under this method should be proportionately allocated to parent and NCI.

Test your Understanding 2

Fin PLC acquired 90% of the ordinary share capital of John PLC on 01 January 20X8 for $45,000. At this date the net assets of John PLC were $95,000.

What GBP arises on the acquisition?

I. If the NCI is valued using the proportion of net assets method

II. If the NCI is valued using the fair value method and the fair value of the NCI on the acquisition date is $20,000?

Working – Goodwill

	% NA	FV
Investment Made by Parent	45,000	45,000
Add NCI (95,000*.20%)	19,000	20,000
Total	64,000	65,000
Less Net Assets in Subsidiary	(95,000)	(95,000)
Goodwill	31,000	30,000

Under any method the GBP is only attribute to parent, no share fore NCI. The Parent is the person, who has acquired the subsidiary.

Test your Understanding 3

The following SFPs have been prepared at 31 December 20 X 8.

	Dickens $	Jones $

Non-current assets:		
Property, plant & equipment	85,000	18,000
Investment :		
Shares in Jones	60,000	
Current assets	160,000	84,000
	305,000	102,000
Equity:		
Ordinary $1 shares	100,000	20,000
Other Reserves	0	10,000
Retained earnings	70,000	25,000
	170,000	55,000
Current liabilities	135,000	47,000
	305,000	102,000

Dickens acquired 16,000 ordinary $1 shares in Jones on 1 January 20X8, when Jones' retained earnings and other reserves stood at $20,000 and 10,000. On this date, the market value of Jones share was 3.75.

Impairment of goodwill 31.12.20X8 was 2,000

The Dickens Group uses the fair value method to value the non-controlling interest.

Prepare the consolidated statement of financial position of Dickens as at 31 December 20X8.

Test your Understanding 4

Question 1

(A) Gamunu PLC acquired 70% of the share Capital of Beema Ltd. On 1st April 2016 for an investment of Rs. 12 million. On that day, the fair value of identifiable net assets of Beema Ltd. Was equal to its book value and fair value of the non-controlling interest was Rs. 3 million.

At the date of acquisition, the following ledger balances appeared in the books of Beema Ltd.

	Rs. ('000)
Stated capital – Ordinary shares	7,000
General Reserves	1,800
Retained Earning	2,000

You are required to:

Calculate the goodwill arising from the consolidation. (05 marks)

Question 2

(A) On 1st April 2018, sigma PLC acquired 75% of Beta PLC's 1,000,000 (1 million) ordinary shares for Rs.290 million. On the date of acquisition, the fair value of the identifiable net assets of Beta PLC was Rs. 340 millon. The market value of a share as at 1st April 2018 of Beta PLC was Rs.365/-.

(a) Calculate the Goodwill arising on acquisition. (05 marks)

Revision Questions – Set 01

Ken Co acquired 80% of the share capital of Fin Co on 1 January 20X6 for $280,000.

The statements of financial position of the two companies at 31 December 20X6 were as follows:

Statements of financial position

	Ken Co	Fin Co
	LKR	LKR
Sundry assets	660,000	290,000
Investment in Fin	280,000	-
	940,000	290,000
Issued share capital	400,000	140,000
Other Reserves	320,000	50,000
Retained earnings		
As at 1 Jan 20X6	140,000	60,000
Profit for 20X6	80,000	40,000
	940,000	290,000

There have been no changes in the share capital or other reserves account of either company since 1 January 20X6. The non-controlling interest is measure at the % NA Method.

Impairment of Goodwill was impaired by 5,000

1) What figure for goodwill on consolidation should appear in the consolidated statement of financial position of the Ken group at 31 December 20X6?

A. LKR 30,000
B. LKR 55,000
C. LKR 75,000
D. LKR (10,000)

2) What figure for non-controlling interest should appear in the consolidated statement of financial position of the Ken group at 31 December 20X6?

A. LKR 77,000
B. LKR 58,000
C. LKR 73,000
D. LKR 105,000

3) What figure for consolidated retained earnings and reserves should appear in the consolidated statement of financial position of the Ken group at 31 December 20X6?

A. LKR 247,000 and LKR 320,000
B. LKR 220,000 and LKR 320,000
C. LKR 252,000 and LKR 320,000
D. LKR 198,000 and LKR 320,000

Prepare the Consolidated accounts based on the workings.

Revision Questions – Set 02

On 1 January 20X0 Alpha Co purchased 90,000 ordinary $1 shares in Beta Co for $270,000. At that date Beta Co's retained earnings amounted to $90,000 and the fair values of Beta Co's assets at acquisition were equal to their book values

Three years later, on 31 December 20X2, the statements of financial position of the two companies were:

	Alpha Co	Beta Co
	$	$
Sundry net assets	230,000	260,000
Shares in Beta	270,000	-
	500,000	260,00
Share capital		
Ordinary shares of $1 each	290,000	100,000
Retained earnings	210,000	160,000
	500,000	260,000

The share capital of Beta Co has remained unchanged since 1 January 20X0. The fair value of the noncontrolling interest at acquisition was $42,000

Impairment of Goodwill was 10,000

1) What amount should appear in the group's consolidated statement of financial position at 31 December 20X2 for goodwill?

   A. $52,000
   B. $80,000
   C. $112,000
   D. $212,000

2) What amount should appear in the group's consolidated statement of financial position at 31 December 20X2 for non-controlling interest?

   A. $48,000
   B. $58,000
   C. $51,000
   D. $42,000

3) What amount should appear in the group's consolidated statement of financial position at 31 December 20X2 for retained earnings?

   A. $280,000
   B. $291,000
   C. $354,000
   D. $264,000

Prepare the Consolidated accounts

Formula to Remember

NCI = (% of NA of NCI or FV of NCI) + ((Post Profit in Sub – if any, Impairment under Full GW Method) * NCI)