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THE INSTITUTE OF CHARTERED ACCOUNTANTS OF SRI LANKA

SL-25-1 – Advanced Corporate Reporting

Strategic Level (2025 Curriculum)

- Consolidated Financial Statements – Part 7

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Complex Group Structures

COMPLEX GROUP STRUCTURES

Complex group structures can arise when a subsidiary of a parent company holds a significant ownership stake in another entity, effectively making that second entity as a subsidiary of the parent company as well.

Complex structures can be classified under two headings:

- Vertical groups
- Mixed groups – D shaped groups

How to address when one parent has several subsidiaries

When a company (Parent/Holding company), denoted as "H," possesses multiple subsidiaries such as "S," "T," and others, the consolidation process will be happened same as the principles we learned in basic consolidation.

The cancellation of intercompany transactions occurs within the holding company, which holds investments in subsidiaries like "S" and "T," and extends to each of these multiple subsidiaries.

The consolidated statement of financial position will show:

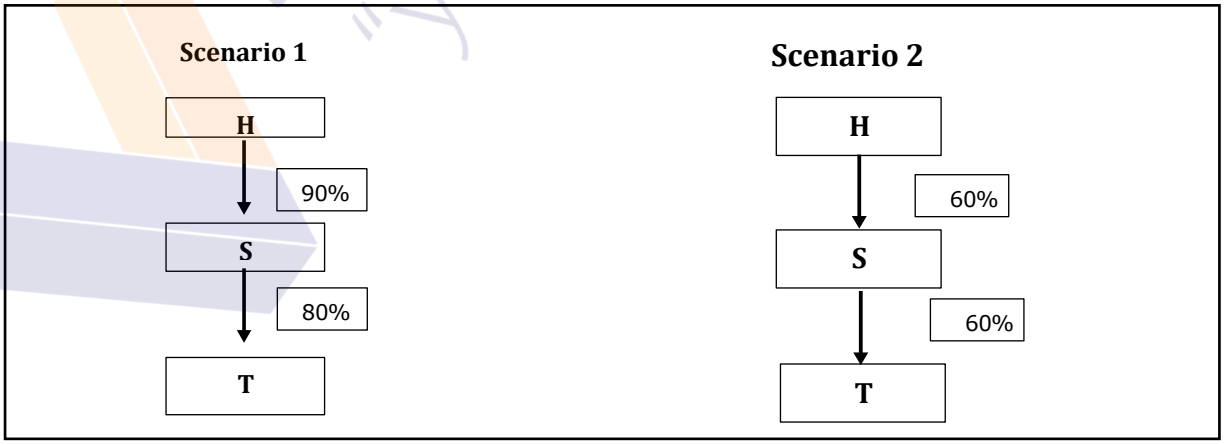
(a) A single figure for non-controlling interest, and
(b) A single figure for goodwill arising from all of the subsidiaries

A dedicated working should be prepared for each element included in the consolidated statement of financial position. This means having one working for goodwill, another for non-controlling interest, a separate one for retained earnings (including reserves), and so forth.

VERTICAL GROUPS

A vertical group exists where a parent has a subsidiary, and that subsidiary has its own subsidiary. The parent entity therefore controls both the subsidiary entity and, in turn, its subsidiary (often referred to as a sub subsidiary entity).

Look at the following two situations.



In both the situations, Company H controls Subsidiary S, and Subsidiary S, in turn, controls Subsidiary T. H is therefore able to control T by virtue of its ability to control S. All three companies form a vertical group.

Both companies that are controlled by the parent are consolidated. The basic techniques of consolidation are the same as seen previously, with some changes to the goodwill, NCI, and group reserves calculations.

Important – When determining the ultimate parent's controlling power do not just look at the effective holding. It is required to look at whether the immediate parent's controlling power via immediate holding %.

APPROACH TO A QUESTION

When configuring the group structure, adhere to the following steps:

- **Control** – which entities does the parent control directly or indirectly?
- **Percentages** – what are the effective ownership percentages for consolidation?
- **Dates** – when did the parent achieve control over the subsidiary and the sub-subsidiary?

Determining the date of effective control

Before preparing the consolidated financial statements of a vertical group it is important to identify the date on which control over the sub-subsidiary was achieved.

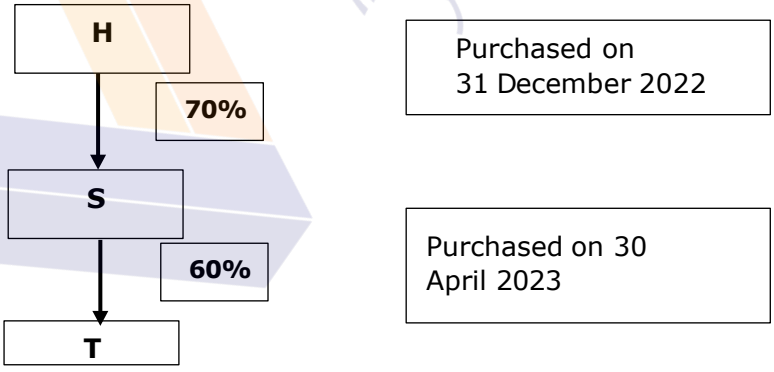
This may be one of two dates:

(a) If Subsidiary controlled sub-subsidiary prior to joining the group, it will be the date on which Parent acquired control of Subsidiary.
(b) If Subsidiary did not control sub-subsidiary prior to joining the group, it will be the date on which Subsidiary acquired control of sub-subsidiary.

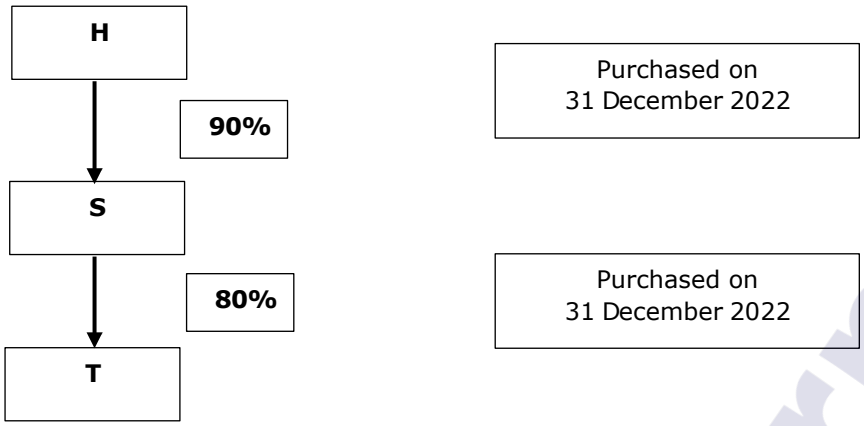
Determining the acquisition date of SS is important **when identifying the pre-acquisition reserves of the sub-subsidiary**.

Test Your Understanding 7.1

Comment on the control, effective holding and the dates.



Test Your Understanding 7.2



Comment on the control, effective holding and the dates.

Test Your Understanding 7.3

Top owns 60% of the equity of Middle Co, which owns 75% of the equity of Bottom Co.

Required:

1. Draw the group structure.
2. Identify the controlling relationship.
3. What is Top Co's effective holding in Bottom Co?

Working out a question can be done by adhering to the following steps.

1) **Sketch** the group structure and check it to the question.
2) Add details to the sketch of dates of acquisition, holdings acquired and cost.
3) Draw up a proforma for the statement of financial position.
4) Work methodically down the statement of financial position, transferring figures to proforma or workings.
5) Use the notes in the question to adjust such as eliminating intra-group balances and unrealized profits.
6) Goodwill working. Compare consideration transferred with effective group interests acquired.
7) Reserves working. Include the group share of subsidiary and sub subsidiary post-acquisition retained earnings (effective holdings again).
8) Non-controlling interests working - total NCI in subsidiary plus total NCI in sub-subsidiary.
9) **Prepare** the consolidated statement of financial position (and statement of profit or loss if required).

INDIRECT HOLDING ADJUSTMENT

Accounting for a sub-subsidiary requires an indirect holding adjustment.

- Goodwill in the sub-subsidiary is calculated from the perspective of the ultimate parent company. Therefore, the **cost of the investment in the sub-subsidiary should be the parent's share of the amount paid by its subsidiary**.
    - The NCI's share of the cost of the investment in the sub-subsidiary must be eliminated from the goodwill calculation.
- The value of the **non-controlling interest in the subsidiary includes the NCI's share of the cost of the investment in the sub-subsidiary**.
    - The NCI's share of the cost of the investment in the sub-subsidiary must be eliminated from the NCI calculation.

Test Your Understanding 7.4

On 31 December 2023, A purchased 90% of the equity shares in B for Rs.150,000 and B purchased 80% of the equity shares in C for Rs.100,000.

At this date, the fair value of the net assets of B and C were Rs.144,000 and Rs.90,000 respectively. The fair value of the non-controlling interest in B and C was Rs.17,000 and Rs.15,000 respectively (Assume FV of NCI in C is from the group perspective).

Required:

1. Calculate goodwill and the non-controlling interest for inclusion in the consolidated statement of financial position as at 31 December 2023.
2. Explain what is required to be done if the FV of NCI in C is given in the perspective of B and not in the perspective of group.

Test Your Understanding 7.5

On 01 April 2023, H purchased 80% of the equity shares in S for Rs.200,000 and S purchased 90% of the equity shares in T for Rs.150,000 on the same day.

At this date, the fair value of the net assets of S and T were Rs.164,000 and Rs.100,000 respectively. The fair value of the non-controlling interest in S and T was Rs.19,000 and Rs.18,000 respectively (Assume FV of NCI in C is from the group perspective).

Required:

1. Calculate goodwill and the non-controlling interest for inclusion in the consolidated statement of financial position as at 01 April 2023.

Test Your Understanding 7.6

The draft statements of the financial position of David, Chethan and James, as at 31 December 2023, are as follows.

	David	Chethan	James
	LKR'000	LKR'000	LKR'000
Sundry assets	280	180	130
Shares in subsidiary	120	80	-
	400	**260**	**130**
Equity capital (Rs.1 shares)	200	100	50
Retained earnings	100	60	30
Liabilities	100	100	50
	400	**260**	**130**

The following information is also available:

a) David acquired 75,000 Rs.1 shares in Chethan on 1 January 2023 when the retained earnings of Chethan amounted to Rs. 40,000. At that date, the fair value of the non- controlling interest in Chethan was valued at Rs. 38,000.

b) Chethan acquired 40,000 Rs.1 shares in James on 30 June 2023 when the retained earnings of James amounted to Rs. 25,000. The retained earnings of James had been Rs. 20,000 on the date of David's acquisition of Chethan. On 30 June 2023, the fair value of the non-controlling interest in James (both direct and indirect), based upon effective shareholdings, was Rs. 31,000.

c) Goodwill has suffered no impairment. It is group policy to use the full goodwill method.

Required:

Prepare the consolidated statement of financial position of the David group as at 31 December 2023.

Test Your Understanding 7.7

The draft statements of the financial position of Dora, Cordon and Jeffry as at 31 December 2023 are as follows.

	Dora	Cordon	Jeffry
Sundry assets	180	80	80
Shares in subsidiary	120	80	
	300	**160**	**80**
Equity capital (Rs. 1 shares)	200	100	50
Retained earnings	100	60	30
	300	**160**	**80**

a) Cordon acquired 40,000 Rs.1 shares in Jeffry on 1 January 2023 when the retained earnings of Jeffry amounted to Rs. 25,000.

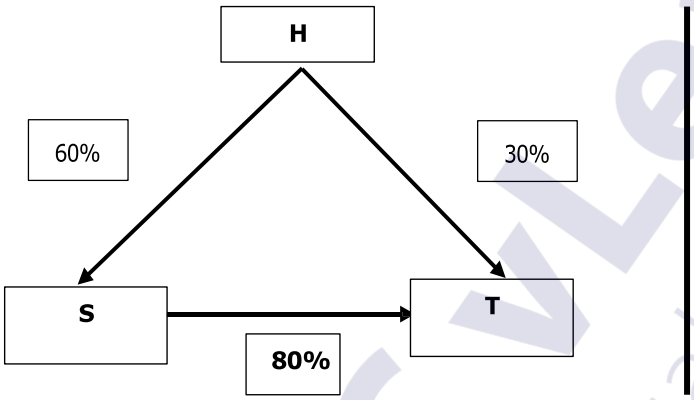
b) Dora acquired 75,000 Rs.1 shares in Cordon on 30 June 2023 when the retained earnings of Cordon amounted to Rs. 40,000 and those of Jeffry amounted to Rs.30,000.

c) It is group policy to value the non-controlling interest using the proportion of net assets method.

Required:

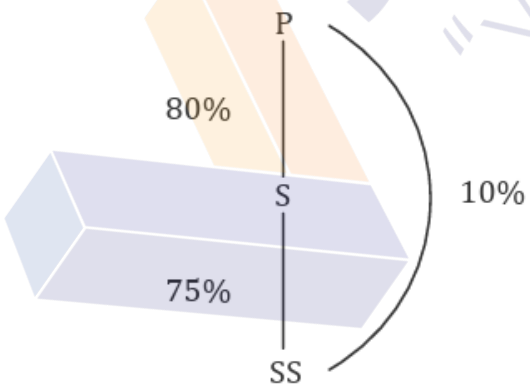
Prepare the consolidated statement of financial position of the Dora group at 31 December 2023.

MIXED (D-SHAPE) GROUPS



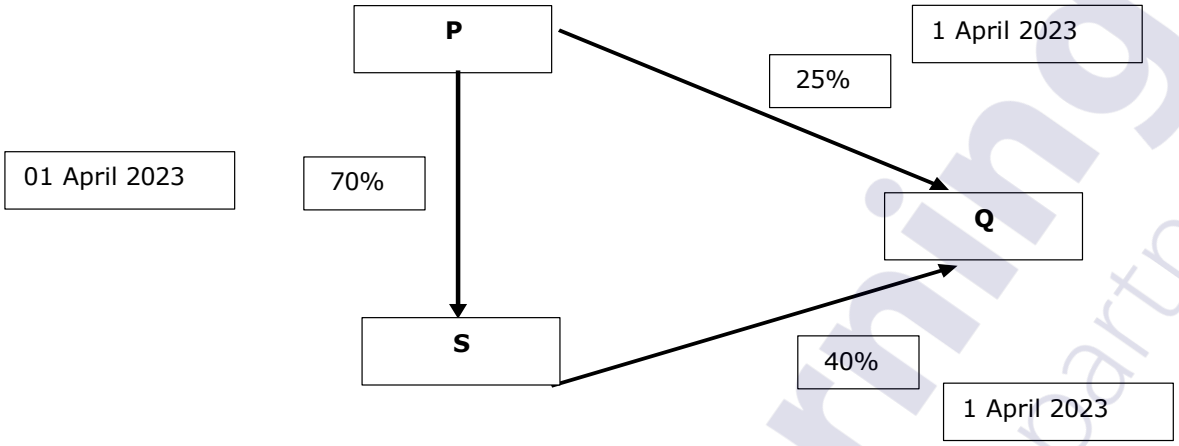
A D-shaped group exists where a parent company has **both a direct and an indirect ownership** interest in a sub-subsidiary. In a mixed group situation, the parent entity has a direct controlling interest in at least one subsidiary. In addition, the parent entity and the subsidiary together hold a controlling interest in a further entity.

H has 60% of the shares of S. S is therefore a subsidiary of H. Further, H has a 30% direct holding in T. H also controls S, who has a 30% holding in T. H therefore controls T through its direct and indirect holdings. This means that T is part of H's group and must be consolidated.



In this example, SS is a sub-subsidiary of P with additional shares held directly by P.

Test Your Understanding 7.8

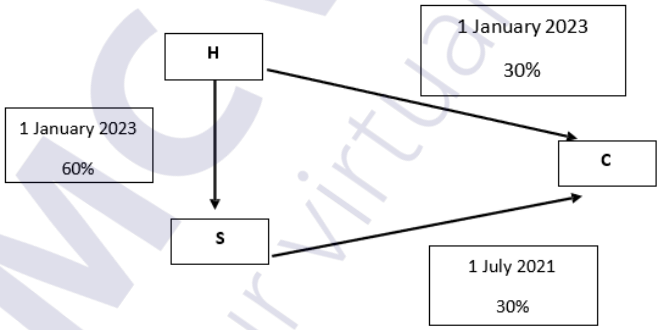


P acquired a 70% interest in S on 1 April 2023, and acquired a 25% interest in Q on the same date.

S acquired a 40% interest in Q on 1 April 2023.

Comment on the control, effective holding and the dates.

Test Your Understanding 7.9



H acquired a 60% interest in S on 1 January 2023 and acquired a 30% interest in T on the same date.

S acquired a 30% interest in T on 1 July 2021.

Comment on the control, effective holding and the dates.

Further detail on mixed groups

Note that the definition of a mixed group does not include the situation where the parent and an associate together hold a controlling interest in a further entity.

e.g., H owns 35% of S, S owns 40% of W and H owns 40% of W.

This is not a mixed group situation. Neither S nor W is a member of the H group, although S and W may both be 'associates' of H.

H's interest in W might be calculated as before as (35% × 40%) + 40% = 54%. Although H has an arithmetic interest in W that is more than 50%, it does not have parent entity control of W, as it does not control S's 40% stake in W.

Accounting for Mixed Groups

All consolidation workings are the same as those used in vertical group situations, with the exception of goodwill.

The goodwill calculation for the sub-subsidiary differs slightly from a vertical group. The cost of the sub-subsidiary must include the following:

- the cost of the parent's holding (**the direct holding**)
- the cost of the subsidiary's holding (**the indirect holding**)
- the indirect holding adjustment

Test Your Understanding 7.10

The statements of financial position of H, S and C as at 31 December 2022 were as follows:

	H	S	C
	LKR.	LKR.	LKR.
75% of shares in S	72,000	–	–
40% of shares in C	25,000	–	–
30% of shares in C	–	20,000	–
Sundry assets	125,000	120,000	78,000
	222,000	140,000	78,000
Equity share capital (Rs. 1 shares)	120,000	60,000	40,000
Retained earnings	95,000	75,000	35,000
Liabilities	7,000	5,000	3,000
	222,000	140,000	78,000

a) All shares were acquired on 31 December 2019 when the retained earnings of S amounted to Rs 30,000 and those of C amounted to Rs. 10,000.

b) It is group accounting policy to value the non-controlling interest on a proportionate basis.

Required:

Prepare the statement of financial position for the H group as at 31 December 2022.

Test Your Understanding 7.11

The draft statements of financial position of Hulk Co, Molehill Co and Pimple Co as at 31 May 20X5 are as follows.

	Hulk Co Rs m	Molehill Co Rs m	Pimple Co Rs m
Assets			
Non-current assets			
Tangible assets	90	60	60
Investments in Subsidiaries (cost)			
-Shares in Molehill Co	90	-	-
Shares in Pimple Co	25	42	-
	115	**102**	**60**
Current assets	40	50	40
	245	**152**	**100**
Equity and liabilities			
Equity			
Stated capital	100	50	50
Revaluation surplus	50	20	20
Retained earnings	45	32	25
	195	**102**	**75**
Non-current liabilities			
12% loan		10	-
Current liabilities			
Payables	50	40	25
	245	**152**	**100**

(a) Hulk Co acquired 60% of the shares in Molehill on 1 January 20X3 when the balance on that company's retained earnings was Rs. 8 m (credit).

(b) Hulk acquired 20% of the shares of Pimple Co and Molehill acquired 60% of the shares of Pimple Co on 1 January 20X4 when that company's retained earnings stood at Rs. 15 m.

(c) There has been no payment of dividends by either Molehill or Pimple since they became subsidiaries.

(d) There was no impairment of goodwill.

(e) It is the group's policy to measure the non-controlling interest at acquisition at its proportionate share of the fair value of the subsidiary's net assets.

Required : Prepare the consolidated statement of financial position of Hulk Co as at 31 May 20X5.