## Chapter 7

# PREPARATION OF THE CONSOLIDATED STATEMENT OF FINANCIAL POSITION

### Issue

- consolidation is the process of adjusting and combining financial information from the individual financial statements of a parent undertaking and its subsidiary undertakings to prepare consolidated financial statements that present financial information for the group as a single economic entity.

- the Consolidated Statement of Financial Position reflects the assets and liabilities within the control of the parent entity, and how they are owned.

- defined by IAS 27 Separate Financial Statements, consolidated financial statements are "the financial statements of a group presented as those of a single entity".

### Example 1

Rasa acquired 100% of the shares of Tatjana on 1 January, 2009 for $18,000. At that date the Statements of Financial Position were as follows:

| | *Rasa* | *Tatjana* |
|---|---|---|
| | *$* | *$* |
| Investment in Tatjana | 18,000 | - |
| Other assets | 30,000 | 20,000 |
| | 48,000 | 20,000 |
| $1 Equity shares | 20,000 | 8,000 |
| Retained earnings | 22,000 | 10,000 |
| | 42,000 | 18,000 |
| Liabilities | 6,000 | 2,000 |
| | 48,000 | 20,000 |

**Prepare the Consolidated Statement of Financial Position of the Rasa Group as at 1 January, 2009**

**(Aggregate the two Statements of Financial Position.)**

**Rasa Group Consolidated Statement of Financial Position as at 1 January, 2009**

- ***Note***

  - share capital is always, only, ever the share capital of the parent entity.

  - the retained earnings of $10,000 in Tatjana were all achieved prior to Rasa gaining control, and since this question asks for a CSoFP as at date of acquisition, then there has been no opportunity for Tatjana to make any profits subsequent to Rasa gaining control. Therefore, in this example, the consolidated retained earnings are simply those of Rasa.

## Post-acquisition reserves

### Example 2

One year later, 31 December, 2009 the Statements of Financial Position of Rasa and Tatjana are as follows:

| | *Rasa* | *Tatjana* |
|---|---|---|
| | *$* | *$* |
| Investment in Tatjana | 18,000 | |
| Other assets | 40,000 | 26,000 |
| | 58,000 | 26,000 |
| $1 Equity shares | 20,000 | 8,000 |
| Retained earnings | 31,000 | 14,000 |
| | 51,000 | 22,000 |
| Liabilities | 7,000 | 4,000 |
| | 58,000 | 26,000 |

**Prepare the Consolidated Statement of Financial Position of the Rasa Group as at 31 December, 2009.**

- ***Note***

  - the Consolidated Statement of Financial Position shows the assets which are under the control of Rasa, rather than the investment in shares of Tatjana

  - the share capital is always, only, ever that of the parent entity, because the group financial statements are prepared for the benefit of Rasa's shareholders only.

  - included in the Consolidated Statement of Financial Position are Rasa's share of the profits less losses made by Tatjana since acquisition.

## Example 3 - Comprehensive example

Aurimas acquired 100% of Oleg for $20,000 when the Statement of Financial Position of Oleg was as follows:

| | $ |
|---|---|
| Other assets | 23,000 |
| $1 Equity shares | 12,000 |
| Retained earnings | 8,000 |
| | 20,000 |
| Liabilities | 3,000 |
| | 23,000 |

On 31 December, 2009 the Statements of Financial Position of the two entities are as follows:

| | *Aurimas* | *Oleg* |
|---|---|---|
| | *$* | *$* |
| Investment in Oleg | 20,000 | - |
| Other assets | 40,000 | 30,000 |
| | 60,000 | 30,000 |
| $1 Equity shares | 10,000 | 12,000 |
| Retained earnings | 42,000 | 15,000 |
| | 52,000 | 27,000 |
| Liabilities | 8,000 | 3,000 |
| | 60,000 | 30,000 |

**Prepare the Consolidated Statement of Financial Position of the Aurimas Group as at 31 December, 2009**

- ***Note***
  - net assets controlled by the group are $59,000 (assets of $70,000 less liabilities of $11,000)
  - since Oleg is a 100% subsidiary, Aurimas also owns net assets of $27,000 ie ($30,000 – $3,000)
  - the consolidated retained earnings comprise the whole of Aurimas' retained earnings ($42,000) plus Aurimas' share (100%) of Oleg's retained earnings made since acquisition ($15,000 - $8,000)

## Complications

- **goodwill**

  - so far, the cost of the investment has equalled the value of the identifiable net assets acquired and therefore the buying entity has not paid any surplus over the worth of the subsidiary

  - where the cost of investment is greater than the fair value of the net assets acquired, the investor has paid for something more than the tangible net assets of the acquired business.

  - the difference is called GOODWILL and is defined in IFRS 3 Business Combinations as:

    - future economic benefits arising from assets that are not capable of being individually identified and separately recognised

- **accounting treatment of goodwill**

  - the accounting treatment of goodwill on acquisition of a subsidiary is governed by IFRS 3. It states that purchased positive goodwill should be capitalised and subjected to an annual impairment review.

- **negative goodwill arising on acquisition**

  - an acquirer should review at the first year end after the acquisition the fair value of assets on acquisition.

  - if negative goodwill still results, this should be credited to the Statement of Profit or Loss and Other Comprehensive Income at the earliest opportunity

**Example 4**

Maruta acquired the entire share capital of Liene for $30,000 on 1 January, 2009 when the Statements of Financial Position of the two entities were as follows:

| | *Maruta* | *Liene* |
|---|---|---|
| | $ | $ |
| Investment in Liene | 30,000 | - |
| Other assets | 40,000 | 27,000 |
| | 70,000 | 27,000 |
| $1 Equity shares | 25,000 | 15,000 |
| Retained earnings | 36,000 | 5,000 |
| | 61,000 | 20,000 |
| Liabilities | 9,000 | 7,000 |
| | 70,000 | 27,000 |

**Prepare the Consolidated Statement of Financial Position of the Maruta Group as at 1 January, 2009**

**Goodwill will be an intangible non-current asset in the top half of the Statement of Financial Position**

- ***Note***

  - net assets controlled by the group are $61,000
  - share capital is always, only, ever that of the parent entity.

## Non-controlling interests

- non-controlling interests arise where the parent entity controls a subsidiary but does not own 100% of it

- *Note*
  - remember you do not have to own 100% of an entity to control it
  - the group financial statements will need to show the extent to which the assets and liabilities are controlled by the parent entity but are owned by other parties, namely the non-controlling interests.

## Workings

- **(W1) Group Structure, as normal**

- **(W2) Goodwill**

| | | |
|---|---|---|
| Cost of investment | | X |
| NCI investment valuation | | X |
| | | X |
| Net assets @ doa | | |
| $1 Equity shares | X | |
| Retained earnings | X | |
| | | X |
| Goodwill | | X |
| Impaired since acquisition | | (X) |
| Therefore, on CSoFP | | (X) |

- **(W3) Consolidated retained earnings**

| | P | S |
|---|---|---|
| per question | X | X |
| - pre acquisition | | (X) |
| ∴ post acquisition | – | X |
| p's share | X | ? % |
| Post acquisition | X | |
| Less: goodwill impaired since acquisition (parent's share only) | (X) | |
| CSoFP | X | |

- **(W4) Non-controlling Interest (? %)**

They want their share of the subsidiary net assets at Statement of Financial Position date

| | |
|---|---|
| Value of nci investment at date of acquisition | X |
| Their share of S post acquisition retained | X |
| | X |
| Less: their share of goodwill impairment | (X) |
| Nci on CSoFP | X |

## The non-controlling interest in the goodwill of the subsidiary creates additional complications

- there are two distinct ways of guiding you in the calculation
- the examiner may say either:
  - the parent company policy is to value the non-controlling interest as their proportional share of the subsidiary's fair valued net assets at date of acquisition, or
  - the parent company policy is to value the non-controlling interest on a full or fair value basis
- the key is the use of the word "proportional" or "proportion" or "proportionate"

### Example 5

Remigijus acquires 75% of the issued share capital of Ilona for $80,000 when the Ilona retained earnings were $60,000. It is the policy of the directors to value the non-controlling interest as their proportional share of the subsidiary fair valued net assets at date of acquisition. Two years later on 31 March, 2010 the respective Statements of Financial Position were:

| | *Remigijus* | *Ilona* |
|---|---|---|
| | *$* | *$* |
| Investment in Ilona | 80,000 | - |
| Other assets | 100,000 | 150,000 |
| | 180,000 | 150,000 |
| $1 Equity shares | 50,000 | 32,000 |
| Retained earnings | 90,000 | 98,000 |
| | 140,000 | 130,000 |
| Liabilities | 40,000 | 20,000 |
| | 180,000 | 150,000 |

**Prepare the Consolidated Statement of Financial Position of the Remigijus Group as at 31 March, 2010.**

**NB. Goodwill has not been impaired since acquisition**

- but where the examiner tells us the value of the NCI is based on a full or fair value basis of the market value of the subsidiary information may be given in any one of three ways

- the exam question could say, for example, either

  - goodwill attributable to the NCI on acquisition was $2,000, or

  - the NCI investment was estimated at $30,000, or

  - the market value of the subsidiary shares immediately before acquisition was $4.

- looking at each possibility in turn:

## Example 6

Ivona bought 60% of the shares of Guido for $100,000 when the Guido retained earnings were $40,000. The Ivona directors have valued the goodwill attributable to the nci at $5,000. Goodwill has not been impaired since acquisition.
At 30 June, 2010, the respective Statements of Financial Position were:

| | *Ivona* | *Guido* |
|---|---|---|
| | *$* | *$* |
| Investment in Guido | 100,000 | - |
| Other net assets | 60,000 | 190,000 |
| | 160,000 | 190,000 |
| $1 Equity shares | 70,000 | 80,000 |
| Retained earnings | 90,000 | 110,000 |
| | 160,000 | 190,000 |

**Prepare the Consolidated Statement of Financial Position as at 30 June, 2010**

**Example 7**

Using Ivona and Guido, but with the information that the value of the nci investment was estimated at $55,000, prepare the Consolidated Statement of Financial Position as at 30 June, 2010

The other possibility which you could face is where the examiner gives a value for the Guido shares.

## Example 8

**Using Ivona and Guido, but with the information that the Guido shares were worth $1.65 immediately before the acquisition by Ivona, prepare the Consolidated Statement of Financial Position as at 30 June, 2010.**

- there is a further complication which arises when goodwill is to be impaired.
- in the last of the Ivona / Guido examples, goodwill was $32,800
- now suppose that this goodwill is to be impaired by 10%
- 10% × $32,800 is $3,280 and this amount is allocated on the basis of shareholdings ie on a 60% / 40% basis

## Example 9

**Recalculate W2, W3 and W4 for the other Ivona / Guido example on the assumption that goodwill is to be impaired by 10% and reprepare the Consolidated Statement of Financial Position**

## Other reserves

- exam questions will often give other reserves (such as a revaluation surplus) as well as retained earnings. These reserves should be treated in exactly the same way as retained earnings.

- if the reserve is pre-acquisition it forms part of the calculation of net assets at the date of acquisition and is therefore used in the goodwill calculation.

- if the reserve is post-acquisition, or there has been some movement on a reserve which existed at acquisition, the Consolidated Statement of Financial Position will show the parent entity's reserve plus its share of the movement on the subsidiary's reserve.

## Mid-year acquisitions

- so far, we have considered acquisitions only at the Statement of Financial Position date. Thus, since entities produce Statements of Financial Position at that date anyway, there has been no special need to establish the net assets of the acquired entity at that date.

- with a mid-year acquisition, a Statement of Financial Position is unlikely to exist at the date of acquisition as required. Accordingly, we have to estimate the net assets at the date of acquisition using various assumptions.

- rule for mid-year acquisitions
    - assume that profits accrue evenly throughout the year unless specifically told otherwise.



### Example 10

Robertas acquired 75% of the issued share capital of Ingrida on 1 August, 2009.
At 31 December, 2009 the two entities have the following Statements of Financial Position:

The directors of Robertas have valued the NCI investment on a proportional basis.

| | | *Robertas* | | *Ingrida* |
|---|---|---|---|---|
| | *$* | *$* | *$* | *$* |
| Investment in Ingrida | | 15,000 | | - |
| TNCA | | 12,000 | | 30,000 |
| Other assets | | 13,000 | | 4,000 |
| | | 40,000 | | 34,000 |
| $1 Equity shares | | 5,000 | | 3,000 |
| Share premium | | - | | 1,500 |
| Retained earnings at 1 January, 2009 | 24,000 | | 20,000 | |
| Profit for 2009 | 10,000 | | 6,000 | |
| | | 34,000 | | 26,000 |
| | | 39,000 | | 30,500 |
| Liabilities | | 1,000 | | 3,500 |
| | | 40,000 | | 34,000 |

**Prepare the Consolidated Statement of Financial Position of the Robertas Group as at 31 December, 2009.**

## IFRS 13 Fair value measurement

## Fair value of assets and liabilities acquired

- **the fair value is calculated as:**
    - securities and tangible non-current assets - market value
    - receivables and payables - present value
    - finished goods and work in progress - net selling price less reasonable profit margin
    - raw materials - replacement cost
    - intangible assets - by reference to an active market, or otherwise on an arm's length basis
- if the fair value of an intangible asset cannot be measured with respect to an active market, then the amount recognised should be limited to an amount that does not create negative goodwill (or if it already exists, does not increase negative goodwill).
- **method**
    - adjust assets and liabilities to reflect fair values prior to consolidation.
    - prepare the consolidated financial statements using the adjusted values of assets and liabilities.
    - consider if any adjustments are needed as a result of this eg extra depreciation.

## Example 11

On 1 January 2008, Dalius acquired 70% of Ramuna for $250,000 when Ramuna's share capital and reserves were as follows:

| | $'000 |
|---|---|
| $1 Equity shares | 130 |
| Retained earnings | 20 |
| | 150 |

At acquisition, the fair value of some of Ramuna's assets were greater than their book value as follows:

| | $ |
|---|---|
| Inventory (all sold in the year) | 20,000 |
| Non-depreciable non-current assets | 15,000 |
| Depreciable non-current assets (over 5years) | 30,000 |
| | 65,000 |

At 31 December, 2009 the Statements of Financial Position of Dalius and Ramuna were as follows:

| | *Dalius* | *Ramuna* |
|---|---|---|
| | *$* | *$* |
| Cost of investment in Ramuna | 250,000 | - |
| Other assets | 350,000 | 300,000 |
| | 600,000 | 300,000 |
| $1 Equity shares | 200,000 | 130,000 |
| Retained earnings | 360,000 | 100,000 |
| | 560,000 | 230,000 |
| Liabilities | 40,000 | 70,000 |
| | 600,000 | 300,000 |

It is Dalius' policy to value the non-controlling interest on the proportionate basis

**Prepare the Consolidated Statement of Financial Position of Dalius as at 31 December, 2009**

**Goodwill is not impaired.**