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Consolidated Financial Statements of Group Companies

UNIT 1 : INTRODUCTION

1.1 Concept of Group, Holding Company and Subsidiary Company

It is an era of business growth. Many organization are growing into large corporations by the process of acquisition, mergers, gaining control by one company over the other company, restructuring etc. Acquisition and mergers ultimately leads to either cost reduction or controlling the market or sharing the material supplies or product diversification or availing tax benefits or synergy. Whatever the motto behind these ventures is, the ultimate result is the large scale corporation. Formation of holding company is the most popular device for achieving these objectives.

Group of companies: Many a times, company expands by keeping intact their separate corporate identity. In this situation, a company (holding company) gains control over the other company (subsidiary company).

This significant control is exercised by one company over the otherby-

1.Purchasing specified number of shares or

2.Exercising control over the board of directors or on voting power of that company.

Unit of companies connected in these ways is collectively called a Group of Companies.

Holding Company and Subsidiary Company have been defined in Section 4 of the Companies Act, 1956.

Holding company: It may be defined as one, which has one or more subsidiary companies and enjoys control over them. Legally a holding company and its subsidiaries are distinct and separate entities. However, in substance holding and subsidiary companies work as a group. Accordingly, users of holding company accounts need financial information of subsidiaries to understand the performance and financial position of the holding company.

Subsidiary Company: According to Section 4(1) of the Companies Act, 1956, a company shall be deemed to be a subsidiary of another if and only if, –

(a) that other controls the composition of its Board of directors; or
(b) that other –
    (i) where the first-mentioned company is an existing company in respect of which the holders of preference shares issued before the commencement of this Act have the

same voting rights in all respects as the holders of equity shares, exercises or controls more than half of the total voting power of such company;

(ii) where the first-mentioned company is any other company, holds more than half in nominal value of its equity share capital; or

(c) the first-mentioned company is a subsidiary of any company which is that other's subsidiary.

For example,

If A Ltd. is a subsidiary of B Ltd.	A ltd.--------→B ltd.
and B ltd. is subsidiary of C Ltd.	B ltd ------→C ltd.
then A Ltd. would also be the subsidiary of C Ltd.	A ltd. -------→C ltd.

by virtue of clause (c) above.

Section 42(1) of the Companies Act, 1956 prohibits a subsidiary company from holding shares in the holding company.

But a subsidiary may continue to be a member of its holding company if it was a member thereof at the commencement of the Act or before becoming a subsidiary of the holding company.

In such a case, the subsidiary shall not have any voting rights in respect of the shares held. A subsidiary may also hold shares in the holding company as the legal representative of a deceased member of the holding company or as trustee (unless the holding company or any subsidiary thereof is beneficially interested under the trust concerned).

Section 41 of the Companies Act defines 'member' as

1.The subscribers of the memorandum of a company shall be deemed to have agreed to become members of the company, and on its registration, shall be entered as members in its register of members.

2.Every other person who agrees in writing to become a member of a company and whose name is entered in its register of members, shall be a member of the company.

3.Every person holding equity share capital of a company and whose name is entered as beneficial owner in the records of the depository shall be deemed to be a member of the concerned company.

1.2 Wholly Owned and Partly Owned Subsidiaries

A wholly owned subsidiary company(Ex. A ltd.) is one in which all the shares with voting rights of 100% are owned by the holding company(Ex. B ltd.)

In a partly owned subsidiary, all the shares of subsidiary company are not acquired by the holding company i.e. only the majority of shares (i.e., more than 50%) are owned by the holding company.

In a wholly owned subsidiary, there is no minority interest because all the shares with voting rights are held by the holding company.

On the other hand, in a partly owned subsidiary company, there is a minority interest because less than 50% shares with voting rights are held by outsiders other than the holding company.

1.3 Purpose of Preparing the Consolidated Financial Statements

Consolidated financial statements are the financial statements of a 'group' presented as those of a single enterprise, where a 'group' refers to a parent and all its subsidiaries.

Parent company needs to inform the users about the financial position and results of operations of not only of their enterprise itself but also of the group as a whole. For this purpose, consolidated financial statements are prepared and presented by a parent/holding enterprise to provide financial information about a parent and its subsidiary(ies) as a single economic entity.

Consolidated Financial Statements are intended to show the financial position of the group as a whole

-by showing the economic resources controlled by them,

-the obligations of the group and the results the group achieves with its resources.

Thus, the information need of users is served by providing them alongwith the separate financial statements of the parent, consolidated financial statements. In some countries a holding company is required to prepare consolidated financial statements by inclusion of the financial statements of its subsidiaries with its own financial statements. In some other countries including India, holding companies are not required to prepare consolidated financial statements.

However, Accounting Standard (AS) 21 has now been issued by the Council of the Institute which lays down principles and procedures for preparation and presentation of consolidated financial statements. (For full text of AS 21, refer to Appendix II Study Material – Vol. II)

The International Accounting Standard 27 *"Consolidated Financial Statements and Accounting for Investments in Subsidiaries"* provides the basic framework for the preparation and presentation of consolidated statements as well as accounting for investments in subsidiaries in a parent's separate financial statements.

1.4 Legal Requirements for Presentation of Information to Members of the Holding Company

A holding company is required, under Section 212 of the Companies Act, 1956, to attach to its balance sheet the following documents in respect of each of its subsidiaries:

(a) a copy of the balance sheet of the subsidiary;

(b) a copy of its profit and loss account;

(c) a copy of the report of its Board of Directors;

(d) a copy of the report of its auditors;

(e) a statement of the holding company's interest in the subsidiary as specified in sub-section (3) of Section 212;

(f) the statement, if any, referred to in sub-section (5) of Section 212; (where the financial year of the holding and subsidiary companies do not coincide with the subsidiary companies) and

(g) the report, if any, referred to in sub-section (6) of Section 212 (that if, for any reason, the Board of Directors of the holding company is unable to obtain information on any of the matters required to be specified under sub-section (4))

The financial year of the subsidiary company must not have ended on a date more than six months prior to the date of the closing of accounts of the holding company.[Sec 212 (2) (c)]

The Central Government has the power to issue necessary instructions for this purpose in case the interval between the closing of the financial year of the subsidiary company and that of the holding company is longer than six months [Section 213(2)].

The statement referred to in (e) above should contain the under mentioned information:

(a) the extent of the holding company's interest in the subsidiary as at the end of the financial year of the subsidiary company;(% of holding in subsidiary co.)

(b) the net aggregate amount, so far as it concerns members of the holding company, but not yet dealt with in that company's account of the subsidiary's profits after deducting its losses.

   (i) for the financial year of the subsidiary covered by the balance sheet and the profit and loss account; and

   (ii) for the previous financial years of the subsidiary since it became the holding company's subsidiary;

(c) the net aggregate amount of the profits of the subsidiary after deducting its losses:

   (i) for the financial year under report; and

   (ii) for the previous financial year of the subsidiary since it became the holding company's subsidiary.

So far as these profits or losses have been dealt with in the holding company's accounts.

Note: *Profits and losses mentioned in paragraph (b) and (c) are only such amounts as may be treated by the holding company as revenue profits or losses. In other words, distinction must be made from the point of view of the holding company, between revenue and capital profit of the subsidiary. In the absence of information, profits of a year may be treated as accruing from day to day [sub-section (4) of Section 212].*

Sub-section (5) of Section 212 requires that where the financial year of the holding and subsidiary companies do not coincide, a statement containing the following particulars should also be attached to the balance sheet of the holding company:

(a) the change and the extent thereof, in the holding company's interest in the subsidiary after the close of the financial year of the subsidiary till the date of the balance sheet; and

(b) details of any material changes which have occurred in the same period in respect of:

   (i) the subsidiary's fixed assets; (ii) its investments; (iii) the moneys lent by it; and (iv) the moneys borrowed by it for any purpose other than that of meeting current liabilities.

Sub section (6) of section 212 requires that if, for any reason, the Board of Directors of the holding company is unable to obtain information on any of the matters required to be specified under sub-section (4) i.e., for making a distinction between capital and revenue profits, a report in writing to that effect should be attached to the balance sheet of the holding company.

Also the Central Government may, on the application or with the consent of the Board of Directors of the company, direct that in relation to any subsidiary, the provisions of Section 212 shall not apply at all or shall apply to a limited extent [sub-section (8) of Section 212].

Illustration 1

A Ltd., B Ltd. and C Ltd. are subsidiaries of H Ltd.

H Ltd.'s accounts for the year ending on 31st March, 2012 have been prepared. In respect of the income from the subsidiaries H Ltd. accounts only for dividend, if any, received from them.

Particulars in respect of the subsidiaries are:

	A Ltd. ₹	*B Ltd.* ₹	*C Ltd.* ₹
Equity Share Capital of ₹ 100 each on date of Respective Balance Sheets	*10,00,000*	*15,00,000*	*20,00,000*
Financial year ends on	*31st March*	*31st Dec.*	*31st Oct.*
Shares held by H Ltd. on 31.3.2012	*8,000*	*9,000*	*12,000*
Shares purchased by H Ltd. from 1.4.2011 to 31.3.2012	*Nil*	*Nil*	*Nil*
Dividend received in 2011-2012 by H Ltd. in respect of last year from	*—*	*—*	*1,80,000*
Dividend received in 2011-2012 by H Ltd. in respect of earlier years	*1,60,000*	*—*	*—*
Total divisible profit for the last year	*3,00,000*	*4,00,000*	*5,00,000*
Total undistributed profits for earlier years since they became subsidiaries of H Ltd.	*8,00,000*	*9,00,000*	*15,00,000*

B Ltd. purchased fixed assets for ₹ 2,00,000 and lent an amount of ₹ 1,00,000 upto 31.3.2012 since the last closing.

C Ltd. purchased investments for ₹ 1,25,000 and borrowed ₹ 1,00,000 upto 31.3.2012 since the last closing.

Prepare the statement pursuant to Section 212 of the Companies Act, 1956 to be furnished along with the accounts of H Ltd., for the year ending on 31st March, 2012.

Solution

Annexure to the Account of H. Ltd.
Statement pursuant to Section 212 of the Companies Act, 1956
relating to the subsidiary companies.

		A Ltd. ₹	*B Ltd.* ₹	*C Ltd.* ₹
1.	Financial year of the Subsidiary Companies	31st March 2012	31st Dec. 2011	31st Oct 2011
2.	(a) Nos. of shares held at the end of the financial year of the subsidiary	8,000	9,000	12,000
	(b) Extent of holding	80%	60%	60%
3.	Net aggregate profit/loss of the subsidiary so far as it concerns to the members of H Ltd.			
	(a) not dealt with in the accounts of H Ltd. for the year ended 31st March, 2012			
	(i) for subsidiary's financial year ending as above in (1)	2,40,000 [3,00,000 X 80 %]	2,40,000 [4,00,000 X 60 %]	1,20,000 [5,00,000 X 60 % - 1,80,000]
	(ii) for previous financial years of the subsidiary since it became subsidiary of H Ltd.	4,80,000 [8,00,000 X 80 % - 1,60,000]	5,40,000 [9,00,000 X 60 %]	9,00,000 [15,00,000 X 60 %]
	(b) dealt with in the accounts of H Ltd. for the year ended 31st March, 2012			
	(i) for the subsidiary's financial year as in (1) above	—	—	1,80,000
	(ii) for the previous financial years of the subsidiary since it become subsidiary of H Ltd.	1,60,000	—	—
4.	Changes in the interest of H Ltd.; between the end of the financial year of the subsidiary and 31st March, 2012			
	(a) Nos. of shares	Nil	Nil	Nil
	(b) Extent of holding	Nil	Nil	Nil
5.	Material changes between the end of the financial year of the			

		subsidiary and 31.3.2012			
	(a)	Fixed Assets	—	(+)2,00,000	—
	B	Investments	—	—	(+)1,25,000
	(c)	Moneys lent by subsidiary	—	1,00,000	—
	(d)	Moneys borrowed by subsidiary for any purpose other than that of meeting current liabilities	—	—	1,00,000

Let us now take one more illustration to discuss the technique of preparation of a statement covering certain financial information of subsidiaries.

Illustration 2

X Ltd., Y Ltd. and Z Ltd. are subsidiaries of H Ltd.

H Ltd.'s accounts for the year ended 31st March, 2012 have been prepared. In respect of the income from the subsidiaries H Ltd. accounts only for dividend, if any, received from them.

Particulars in respect of the subsidiaries are:

	X Ltd. ₹	*Y Ltd.* ₹	*Z Ltd.* ₹
Equity share capital of ₹ 100 each on the date of respective Balance sheets	*50,00,000*	*80,00,000*	*1,20,00,000*
12% Cumulative Preference share capital of ₹ 100 each	*5,00,000*	*—*	*10,00,000*
Financial year ends on	*31st March*	*31st Dec.*	*31st Oct.*
Equity dividend received in 2011-2012 by H Ltd. in respect of last year from	*—*	*—*	*14,00,000*
Equity dividend received in 2011-2012 by H Ltd. in respect of earlier years from	*7,50,000*	*—*	*—*
Total divisible profit for the last year	*15,00,000*	*18,00,000*	*25,00,000*
Total undistributed profits for earlier years since they became subsidiaries of H Ltd.	*32,00,000*	*40,00,000*	*60,00,000*

Y Ltd. purchased fixed assets for ₹ 6,00,000 and lent an amount of ₹ 4,00,000 upto 31st March, 2012 since the last closing. Z Ltd. purchased investments for ₹ 7,20,000 and borrowed ₹ 3,50,000 upto 31st March, 2012 since the last closing.

H Ltd.'s schedule of investments as on 31st March, 2012 includes, inter alia, the following:

		₹
1.	*40,000 Equity shares of X Ltd.*	
	@ ₹ 120 per share	*48,00,000*
2.	*72,000 Equity shares of Y Ltd.*	
	@ ₹ 110 per share	*79,20,000*
3.	*84,000 Equity shares of Z Ltd.*	
	@ ₹ 150 per share	*1,26,00,000*
4.	*3,000 12% Cumulative Preference shares*	
	of X Ltd. @ ₹ 100 each	*3,00,000*
5 .	*7,000 12% Cumulative Preference shares*	
	of Z Ltd. @ ₹ 100 each	*7,00,000*
		2,63,20,000

Prepare the statement pursuant to Section 212 of the Companies Act, 1956 to be furnished along with the accounts of H Ltd. for the year ended 31st March, 2012.

Solution

Annexure to the Accounts of H Ltd.
Statement pursuant to Section 212 of the Companies Act, 1956
relating to Subsidiary Companies

		X Ltd.	Y Ltd.	Z Ltd.
1.	Financial year of the subsidiary ended on 31st March '2012	31st Dec.'2011	31st Oct.'2011	
2.	(a) No. of equity shares of subsidiary company held at the end of the financial year	40,000	72,000	84,000
	Extent of holding	80%	90%	70%
	(b) No. of preference shares of subsidiary company held at the end of the financial year	3,000	—	7,000
	Extent of holding	60%	—	70%
3.	Net aggregate amounts of profits less losses of the subsidiary for the year as above so far as it concerns members of H Ltd.			
	(a) Dealt with in the accounts of H Ltd.	36,000	—	14,84,000
	Preference Share Dividend + Equity share dividend	[3,000 X 100 X 12 %]		[7,000 X 100 X 12 %] + 14,00,000

	(b) Not dealt with in the accounts of H Ltd Share of divisible profit after reducing preference share dividend	11,52,000 [15,00,000 – 60,000] X 80 %	16,20,000 [18,00,000 X 90 %]	2,66,000 [25,00,000 – 1,20,000] X 70 % - 14,00,000
4.	Net aggregate amount of profits less losses for previous financial years of the subsidiary since it became subsidiary so far as it concerns the members of H Ltd.			
	(a) Dealt with in the accounts of H Ltd	7,50,000	—	—
	(b) Not dealt with in the accounts of H Ltd	18,10,000 [32,00,000 X 80 %] – 7,50,000	36,00,000 [40,00,000 X 90 %]	42,00,000 [60,00,000 X 70 %]
5.	Changes of interest of H Ltd. in the subsidiary between the end of the financial year of the subsidiary and that of H Ltd.	—	—	—
6.	Material changes between the end of the financial year of the subsidiary and that of H Ltd.			
	(a) Fixed Assets	—	+ 6,00,000	—
	(b) Investments	—	—	+ 7,20,000
	(c) Moneys lent by subsidiary	—	+ 4,00,000	—
	(d) Moneys borrowed by Subsidiary for any purpose other than that of meeting current liabilities	—	—	+ 3,50,000

Note: While calculating the amounts for 3(a) above, preference dividends have also been considered. In the 4(a) & (b) above, preference dividend could not be considered because of lack of specific information about the number of earlier years covered.

UNIT 2 : CONSOLIDATED FINANCIAL STATEMENTS

As per AS 21, "Consolidated financial statements are the financial statements of a group presented as those of a single enterprise". In many developed countries like U.S.A., U.K., Germany, France and Japan the consolidation of financial statement of holding company with its subsidiary is required. Preparation of consolidated financial statements has certain specific advantages.

The main advantages of consolidation are given below:

(i) Single Source Document: From the consolidated financial statements, the users of accounts can get an overall picture of the holding company and its subsidiaries. Consolidated Profit and Loss Account gives the overall profitability of the group

(ii) Intrinsic value of share: Intrinsic share value of the holding company can be calculated directly from the Consolidated Balance Sheet.

(iii) Return on Investments in Subsidiaries: The holding company controls its subsidiary. So its return on investments in subsidiaries should not be measured in terms of dividend alone. Consolidated Financial Statements provide information for identifying revenue profit for determining return on investment.

(iv) Acquisition of Subsidiary: The Minority Interest data of the Consolidated Financial Statement indicates the amount payable to the outside shareholders of the subsidiary company at book value which is used as the starting point of bargaining at the time of acquisition of a subsidiary by the holding company.

(v) Evaluation of Holding Company in the market: The overall financial health of the holding company can be judged using Consolidated Financial Statements. Those who want to invest in the shares of the holding company or acquire it, need such consolidated statement for evaluation.

2.1 Requirements of Accounting Standard 21

Accounting Standard (AS) 21, 'Consolidated Financial Statements', does not lay down which enterprises need to prepare consolidated financial statements.

However, clause 32 of the Listing Agreement requires all listed companies to prepare consolidated financial statements in accordance with AS 21 annually and include the same in the annual report. Hence, all listed companies should prepare consolidated financial statements, subject to the exceptions as mentioned below, in which they consolidate their investments in subsidiaries in accordance with the Standard.

Therefore, an enterprise that presents consolidated financial statements should prepare and present these statements in accordance with this Standard.The consolidated financial statements are required to include all subsidiaries, domestic as well as foreign of the parent other than the ones referred below.

- Subsidiaries acquired for subsequent disposal
- Subsidiaries operating under severe long-term restrictions which significantly impair their

ability to transfer funds to the parent.

This Statement should be applied in the preparation and presentation of consolidated financial statements for a group of enterprises under the control of a parent.

As per AS 21, consolidated financial statements normally include

- Consolidated Balance Sheet
- Consolidated Statement of Profit and Loss Account
- Consolidated Cash Flow Statement (in case parent presents cash flow statement)
- Notes and statements and explanatory schedules that form the integral part thereof.

The consolidated financial statements are presented to the extent possible in the same format as that adopted by the parent for its separate financial statements.

2.2 Consolidation Procedures

When preparing consolidated financial statements, the individual balances of the parent and its subsidiaries are aggregated on a line-by-line basis, and then certain consolidation adjustments are made.

For example, the cash, trade receivables and prepayments of the parent and each subsidiary are added together to arrive at the cash, trade receivables and prepayments of the group, before consolidation adjustments are made.

The objective is that the consolidated financial statements should present the information contained in the consolidated financial statements of a parent and its subsidiaries as if they were the financial statements of a single economic entity.

In order that the consolidated financial statements present financial information about the group as that of a single enterprise, the following steps are then taken:

1. the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary are eliminated. In case cost of acquisition exceeds or is less than the acquirer's interest, goodwill or capital reserve is calculated retrospectively.
2. intragroup transactions, including sales, expenses and dividends, are eliminated, in full;
3. unrealised profits resulting from intragroup transactions that are included in the carrying amount of assets, such as inventory and fixed assets, are eliminated in full;
4. unrealised losses resulting from intragroup transactions that are deducted in arriving at the carrying amount of assets are also eliminated unless cost cannot be recovered;
5. minority interest in the net income of consolidated subsidiaries for the reporting period are identified and adjusted against the income of the group in order to arrive at the net income attributable to the owners of the parent; and
6. minority interests in the net assets of consolidated subsidiaries are identified and presented in the consolidated balance sheet separately from liabilities and the parent shareholders' equity.

2.3 Calculation of Goodwill/Capital Reserve (Cost of Control)

As on the date of investment, the cost of investment and the equity in the subsidiary needs to be calculated. AS 21 defines equity as the 'residual interest in the assets of an enterprise after deducting all its liabilities.' In other words, it is equal to the net worth of the enterprise.

Once the above is calculated, goodwill or capital reserve is calculated as under:

Goodwill = Cost of Investment - Parent's share in the equity of the subsidiary on date of investment

Capital Reserve = Parent's share in the equity of the subsidiary on date of investment - Cost of investment

The parent's portion of equity in a subsidiary, at the date on which investment is made, is determined on the basis of information contained in the financial statements of the subsidiary as on the date of investment.

However, if the financial statements of a subsidiary as on the date of investment are not available and if it is impracticable to draw the financial statements of the subsidiary as on that date, financial statements of the subsidiary for the immediately preceding period are used as a basis for consolidation.

Adjustments are made to these financial statements for the effects of significant transactions or other events that occur between the date of such financial statements and the date of investment in the subsidiary.

It may be mentioned that positive or negative differential is separately recognised only in purchase method. This differential calculated as cost of control is shown in the consolidated balance sheet.

For example,

1.H Ltd. acquires 70% of the equity shares of S Ltd. on 1st January, 2012. On that date, paid up capital of S Ltd. was 10,000 equity shares of ₹ 10 each; accumulated reserve balance was ₹ 1,00,000. H Ltd. paid ₹ 1,60,000 to acquire 70% interest in the S Ltd. Assets of S Ltd. were revalued on 1.1.2012 and a revaluation loss of ₹ 20,000 was ascertained. The book value of shares of S Ltd. is calculated as shown below:

	₹
70% of the Equity Share Capital 1,00,000	70,000
70% of Accumulated Reserve 1,00,000	70,000
70% of Revaluation Loss 20,000	(14,000)
	1,26,000

So, H Ltd. paid a positive differential of ₹ 34,000 i.e ₹(1,60,000 – 1,26,000). This differential is also called goodwill and is shown in the balance sheet under the head intangibles.

Let us take another example:

2. A Ltd. acquired 70% interest in B Ltd. on 1.1.2012. On that date, B Ltd. had paid-up capital of ₹ 1,00,000 consisting of 10,000 equity shares of ₹ 10 each and accumulated balance in reserve and surplus of ₹ 1,00,000. On that date, assets and liabilities of B Ltd. were also

revalued and revaluation profit of ₹ 20,000 were calculated. A Ltd. paid ₹ 1,30,000 to purchase the said interest.

In this case, the book value of Shares of B Ltd. is calculated as shown below:

	₹
70% of the Equity Share Capital ₹ 1,00,000	70,000
70% of Reserves and Surplus ₹ 1,00,000	70,000
70% of Revaluation Profit ₹ 20,000	14,000
	1,54,000

So, H Ltd. enjoyed negative differential of ₹ 24,000 i.e. (1,54,000 – 1,30,000).

Illustration 1

Exe Ltd. acquires 70% of equity shares of Zed Ltd. as on 31st March, 2012 at a cost of ₹ 70 lakhs. The following information is available from the balance sheet of Zed Ltd. as on 31st March, 2012:

	₹ in lakhs
Fixed Assets	*120*
Investments	*55*
Current Assets	*70*
Loans & Advances	*15*
15% Debentures	*90*
Current Liabilities	*50*

The following revaluations have been agreed upon (not included in the above figures):

Fixed Assets	*Up by 20%*
Investments	*Down by 10%*

Zed Ltd. declared and paid dividend @ 20% on its equity shares as on 31st March, 2012. Exe Ltd. purchased the shares of Zed Ltd. @ ₹ 20 per share.

Calculate the amount of goodwill/capital reserve on acquisition of shares of Zed Ltd.

Solution

Revalued net assets of Zed Ltd. as on 31st March, 2012

	₹ in lakhs	*₹ in lakhs*
Fixed Assets [120 X 120 %]		144.0
Investments [55 X 90 %]		49.5
Current Assets		70.0
Loans and Advances		15.0
Total Assets after revaluation		278.5

Less: 15% Debentures	90.0	
Current Liabilities	50.0	(140.0)
Equity / Net Worth		138.5
Exe Ltd.'s share of net assets (70%)		96.95
Exe Ltd.'s cost of acquisition of shares of Zed Ltd.		
(₹ 70 lakhs – ₹ 7 lakhs*)		63.00
Capital reserve		33.95

* Total Cost of 70 % Equity of Zed Ltd	₹ 70 lakhs
Purchase Price of each share	₹ 20
Number of shares purchased [70/20]	3.5 lakhs
Dividend @ 20 % i.e. ₹ 2 per share	₹ 7 lakhs

Since dividend received is for pre acquisition period, it has been reduced from the cost of investment in the subsidiary company.

Illustration 2

Variety Ltd. holds 46% of the paid-up share capital of VR Ltd. The shares were acquired at a market price of ₹ 17 per share. The balance of shares of VR Ltd. are held by a foreign collaborating company. A memorandum of understanding has been entered into with the foreign company providing for the following:

(a) The shares held by the foreign company will be sold to Variety Ltd. The price per share will be calculated by capitalising the yield at 15%. Yield, for this purpose, would mean 40% of the average of pre-tax profits for the last 3 years, which were ₹ 30 lakhs, ₹ 40 lakhs and ₹ 65 lakhs.

(b) The actual cost of the shares to the foreign company was ₹ 5,40,000 only. The profit that would accrue to them would be taxable at an average rate of 30%. The tax payable will be deducted from the proceeds and Variety Ltd. will pay it to the Government.

(c) Out of the net consideration, 50% would be remitted to the foreign company immediately and the balance will be an unsecured loan repayable after two years.

The above agreement was approved by all concerned for being given effect to on 1.4.2012. The total assets of VR Ltd. as on 31st March, 2012 was ₹ 1,00,00,000. It was decided to write down fixed assets by ₹ 1,75,000. Current liabilities of VR Ltd. as on the same date were ₹ 20,00,000. The paid-up share capital of VR Ltd. was ₹ 20,00,000 divided into 2,00,000 equity shares of ₹ 10 each.

Find out goodwill/capital reserve to Variety Ltd. on acquiring wholly the shares of VR Ltd.

Solution

(1) Computation of purchase consideration:

(a)	Yield of VR Ltd.: $\left[\frac{40}{100} \times \frac{30+40+65}{3}\right]$	₹ 18 Lakhs
(b)	Price per share of VR Ltd.	
	Capitalised yield $\left[\frac{18 \text{ lakhs}}{0.15}\right]$	₹ 120 lakhs
	Number of shares	2,00,000
	Price per share	₹ 60
(c)	Purchase consideration for 54% shares in VR Ltd. $2,00,000 \times \frac{54}{100} \times$ ₹ 60	₹ 64.80
(d)	Discharge of purchase consideration:	
	Tax deducted at source (₹ 64.80 lakhs–₹ 5.40 lakhs)$\times \frac{30}{100}$	₹ 17.82
	50% of purchase consideration (net of tax) in cash ₹ (64.80 – 17.82) x 50%	₹ 23.49
	Balance – Unsecured Loan	₹ 23.49

(2) Goodwill/Capital Reserve to Variety Ltd.:

	₹ in lakhs	
Total Assets		100.00
Less: Reduction in value of Fixed Assets		(1.75)
		98.25
Less: Current Liabilities		(20.00)
Net Assets		78.25
Purchase consideration	64.80	
Investments [2,00,000 X 46 % X ₹ 17]	15.64	(80.44)
Goodwill		2.19

2.4 Minority Interests

Minority interest is that part of the net results of operations and of net assets of a subsidiary attributable to interests which are not owned, directly or indirectly through subsidiaries, by the holding (parent) company.

In short, minority interest represents the claims of the outside shareholders of a subsidiary. Minority interests in the net income of consolidated subsidiaries for the reporting period are identified and adjusted against the income of the group in order to arrive at the net income attributable to the shareholders of the holding company.

Minority interest in the income of the group should be separately presented.

The losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. The excess, and any further losses applicable to the minority, are adjusted against the majority interest except to the extent that the minority has a binding obligation to, and is able to make good the losses. If the subsidiary subsequently reports profit, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered.

As per para. 13(e) of AS 21, minority interest in the net assets of consolidated subsidiaries should be identified and presented in the consolidated balance sheet separately from liabilities and the equity of the parent's shareholders. Minority interest in the net assets consist of:

(i) the amount of equity attributable to minorities at the date on which investment in a subsidiary is made; and
(ii) the minorities share of movements in equity since the date the parent-subsidiary relationship came in existence.

2.5 Profit or Loss of Subsidiary Company

For the purpose of consolidated balance sheet preparation all reserves and profits (or losses) of subsidiary company should be classified into pre and post acquisition reserves and profits (or losses).

Profits (or losses) earned (or incurred) by subsidiary company upto the date of acquisition of the shares by the holding company are pre acquisition or capital profits (or loss).

Similarly, all reserves of subsidiary company upto the date of acquisition are capital reserves from the view point of holding company. If the holding interest in subsidiary is acquired during the middle or some other period of the current year, pre-acquisition profit should be calculated accordingly.

In addition profit or loss on revaluation of fixed assets of subsidiary should also be treated as capital profit or loss. But if the fall in the value of the asset occurs after the date of acquisition, the loss should be treated as revenue loss. Adjustment for depreciation would be made in the profit and loss account of the subsidiary.

The minority interest in the reserves and profits (or losses) of subsidiary company should be transferred to minority interest account which will also include share capital of subsidiary company held by outsiders / minority shareholders.

Minority Interest Account : Share Capital of subsidiary related to outsiders + Minority interest in reserves and profits of subsidiary co.

The holding company's interest in the pre acquisition reserves and profits (or losses) should be adjusted against cost of control to find out goodwill or capital reserve on consolidation. The

balance of reserves and profits (or loss) of subsidiary company, representing holding company's interest in post acquisition or revenue reserves and profits (or losses), should be added to the balances of reserves and profits (or losses) of holding company..

2.6 Dividend Received From Subsidiary Companies

The holding company, when it receives a dividend from a subsidiary company, must distinguish between the part received out of capital profits and that out of revenue profits - the former is credited to Investment Account, it being a capital receipt, and the latter is adjusted as revenue income for being credited to the Profit & Loss Account. It must be understood that the term 'capital profit', in this context, apart from the generic meaning of the term, connotes profit earned by the subsidiary company till the date of acquisition. As a result, profits which may be of revenue nature for the subsidiary company may be capital profits so far as the holding company is concerned. If the controlling interest was acquired during the course of a year, profit for that year must be apportioned into the pre-acquisition and post-acquisition portions, on the basis of time in the absence of information on the point.

Illustration 3

H Ltd. acquired 3,000 shares in S Ltd., at a cost of ₹ 4,80,000 on 1st August, 2012. The capital of S Ltd. consisted of 5,000 shares of ₹ 100 each fully paid. The Profit & Loss Account of this company for 2012 showed an opening balance of ₹ 1,25,000 and profit for the year of ₹ 3,00,000. At the end of the year, it declared a dividend of 40%. Record the entry in the books of H Ltd., in respect of the dividend.

Solution

The profits of S Ltd., have to be divided between capital and revenue profits from the point of view of the holding company.

	Capital Profit ₹		*Revenue Profit* ₹
Balance on 1.1.2012	1,25,000	—	
Profit for 2012 (3,00,000 × 7/12)	1,75,000	(3,00,000×5/12)	1,25,000
Total	3,00,000		1,25,000
Proportionate share of H Ltd. (3/5)	1,80,000		75,000

Total Dividend Declared = ₹ 5,00,000 X 40 % = ₹ 2,00,000

H Ltd's share in the dividend = ₹ 2,00,000 X 3/5 = ₹ 1,20,000

The treatment of the dividend of ₹ 1,20,000 received by H Ltd., will depend on the character of profits which have been utilised by S Ltd., to pay the dividend. There are four possibilities:

(1) Earlier profits, included in the profit brought forward from the previous year have been used up first. In that case, the dividend of ₹ 1,20,000 would be paid wholly out of capital or pre-acquisition profits. The entry in that case will be:

		₹	₹
Bank Account	Dr.	1,20,000	
To Investment Account			1,20,000

(2) The profit for 2012 alone has been utilised to pay the dividend, and no part of the profit brought forward has been utilised for the purpose. The share of H Ltd., in profit for the first seven months of S Ltd., is ₹ 1,05,000 i.e., ₹ 1,75,000 × 3/5 and that the profit for the remaining five months is ₹ 75,000. The dividend of ₹ 1,20,000 will be adjusted in this ratio: ₹ 70,000 out of profits up to the 1st August and ₹ 50,000 out of profits after that date. The dividend out of profits subsequent to August 1st will be revenue income and that out of earlier profits capital receipt. Hence the entry:

		₹	₹
Bank	Dr.	1,20,000	
To Investment Account			70,000
To Profit and Loss Account			50,000

(3) Later profits have been utilised first and then pre- acquisition profits. In such a case, the whole of ₹ 75,000 (share of H Ltd. in profits of S Ltd., after 1st August) would be received and treated as revenue income; the remaining dividend, ₹ 45,000 (₹ 1,20,000 less ₹ 75,000) would be capital receipt. The entry would be:

		₹	₹
Bank	Dr.	1,20,000	
To Investment Account			45,000
To Profit & Loss Account			75,000

(4) The two profits, pre-and post-acquisition, have been used up proportionally. The ratio would be ₹ 1,80,000:75,000; 1,20,000 × $\frac{75,000}{2,55,000}$ would be revenue receipt and the remaining capital. The entry would be:

		₹	₹
Bank	Dr.	1,20,000	
To Investment Account			84,706
To Profit & Loss Account			35,294

Notes:

(1) Points (3) and (4) above can arise only if there is definite information about the profits utilised; in practice such treatment is rare.

(2) The treatment outlined above in fact is not peculiar to holding companies-dividends received out of profits earned before purchase of investments normally also are credited to

the Investment Account. For instance, if shares in X Ltd., are purchased in January, 2012 and in April X Ltd., declares a dividend in respect of 2011, the dividend received by the holder of the shares correctly should not be treated as income but as capital receipt, and credited to Investment Account.

(3) The holding company, like other holders, records no entry on issue of bonus shares by the subsidiary company - only the number of shares held is increased.

Illustration 4

(a) From the following data, determine in each case:(1)Minority interest at the date of acquisition and at the date of consolidation.(2)Goodwill or Capital Reserve.(3) Amount of holding company's profit in the consolidated Balance Sheet assuming holding company's own Profit & Loss Account to be ₹ 2,00,000 in each case

Case	*Subsidiary Company*	*% shares owned*	*Cost*	*Date of acquisition*		*Consolidation Date*	
				1.1.2011 Share Capital	*31.12.2011 Profit & Loss Account*	*Share Capital*	*Profit & Loss Account*
			₹	*₹*	*₹*	*₹*	*₹*
Case 1	*A*	*90%*	*1,40,000*	*1,00,000*	*50,000*	*1,00,000*	*70,000*
Case 2	*B*	*85%*	*1,04,000*	*1,00,000*	*30,000*	*1,00,000*	*20,000*
Case 3	*C*	*80%*	*56,000*	*50,000*	*20,000*	*50,000*	*20,000*
Case 4	*D*	*100%*	*1,00,000*	*50,000*	*40,000*	*50,000*	*55,000*

Solution

(1) Minority Interest = Equity Attributable to minorities

Equity is the residual interest in the assets of an enterprise after deducting all its liabilities i.e. in this given case Share Capital + Profit & Loss A/c

	Minority % Shares Owned [E]	*Minority interest as at the date of acquisition [E] x [A + B]₹*	*Minority interest as at the date of consolidation [E] X [C + D]₹*
Case 1 [100-90]	10 %	15,000	17,000
Case 2 [100-85]	15 %	19,500	18,000
Case 3 [100-80]	20 %	14,000	14,000
Case 4 [100-100]	NIL	Nil	Nil

(2) Calculation of Goodwill or Capital Reserve

	Shareholding % [F]	*Cost [G]*	*Total Equity [A] + [B] = [H]*	*Parent's Portion of equity [F] x [H]*	*Goodwill ₹ [G] – [H]*	*Capital Reserve ₹ [H] – [G]*
Case 1	90 %	1,40,000	1,50,000	1,35,000	5,000	—
Case 2	85 %	1,04,000	1,30,000	1,10,500	—	6,500
Case 3	80 %	56,000	70,000	56,000	Nil	Nil
Case 4	100 %	1,00,000	90,000	90,000	10,000	—

(3) The balance in the Profit & Loss Account on the date of acquisition (1.1.2011) is Capital Profit, as such the balance of Consolidated Profit & Loss Account shall be equal to holding Co.'s Profit.

On 31.12.2011 in each case the following amount shall be added or deducted from the balance of holding Co.'s Profit & Loss Accounts.

Case	% Share holding [K]	P & L as on 31.12.2011 [L]	P & L as on consolidation date [M]	P & L post acquisition [N] = [M]-[L]	Amount to be added / (deducted) from holding's P & L [O] = [K] x [N]
1	90 %	50,000	70,000	20,000	18,000
2	85 %	30,000	20,000	(10,000)	(8,500)
3	80 %	20,000	20,000	NIL	NIL
4	100 %	40,000	55,000	15,000	15,000

(b) XYZ Ltd. purchased 80% shares of ABC Ltd. on 1st January, 2011 for ₹ 1,40,000. The issued capital of ABC Ltd., on 1st January, 2011 was ₹ 1,00,000 and the balance in the Profit & Loss Account was ₹ 60,000.

For the year ending on 31st December, 2011 ABC Ltd. has earned a profit of ₹ 20,000 and, at the same time, declared and paid a dividend of ₹ 30,000.

Show by an entry how the dividend should be recorded in the books of XYZ Ltd.

What is the amount of minority interest as on 1st January, 2011 and 31st December, 2011?

Solution:

Total Dividend Paid = ₹ 30,000

Out of post acquisition profit = ₹ 20,000

Out of pre acquisition profit = ₹ 10,000

Hence, 2/3rd of dividend received by XYZ will be credited to P & L and 1/3rd will be credited to Investments.

XYZ Ltd.'s share of dividend = ₹ 30,000 X 80 % = ₹ 24,000

Book of XYZ Ltd.

		₹	₹	₹
Bank A/c	Dr.	24,000		
To Profit & Loss A/c			16,000	
To Investments in ABC Ltd.			8,000	
(Dividend received from ABC Ltd. 1/3 credited to investment A/c being out of capital profits – as explained above)				
Goodwill on Consolidation:			₹	₹
Cost of shares less dividend out of capital profits				1,32,000
Less: Face value of capital			80,000	
Add: Share of capital profits [60,000-10,000 (dividend portion)] X 80 %			40,000	(1,20,000)
Goodwill				12,000
Minority interest on: 1st January, 2011: 20% of ₹ 1,60,000 [1,00,000 + 60,000]				32,000
31st December, 2011: 20% of ₹ 1,50,000 [1,00,000 + 60,000 + 20,000 – 30,000]				30,000

(c) The following balances appear in the books of a holding Co. and its subsidiary on the dates stated:

	Jan. 1 2009	*Dec. 31 2009*	*Dec. 31 2010*	*Dec. 31 2011*
Holding Company	₹	₹	₹	₹
Investments in Subsidiary	*1,28,000*	*1,28,000*	*1,19,000*	*1,40,000*
Profit & Loss Account (Balance)	*1,35,000*	*1,60,000*	*1,48,000*	*1,55,000*
Subsidiary Company				
Share Capital	*1,00,000*	*1,00,000*	*1,00,000*	*1,00,000*
Profit & Loss Account (Balance before providing for dividend)	*50,000*	*62,000*	*70,000*	*80,000*

Subsidiary's issued capital consisted of 1,000 equity shares of ₹ 100 each. The holding Co.

purchased 800 shares on 1st January, 2009. It sold 50 shares on 1st January, 2010 and purchased 100 shares on lst January, 2011. The Investment Account was debited with the cost of shares purchased and credited with the sale proceeds. The holding Co. has made no other entries in the Investment Account and credited all dividends received to the Profit & Loss Account. The subsidiary company paid a dividend of 15% in March each year in respect of the previous year.

Prepare a statement showing the amount of goodwill/cost of control and minority interest at the end of each year.

Solution:

Statement showing Goodwill or Cost of Control as on

	31st Dec. 2009 ₹	*31st Dec.* 2010 ₹		*31st Dec.* *2011* ₹
Number of Shares held	800	750		850
% of Holding Co's shareholding	80 %	75 %		85 %
Cost of investment	1,28,000	1,16,000		1,08,750
Less: Dividend out of Capital Profit received on 31st March 2009	(12,000)			
	1,16,000			
Less: Cost of investment sold on 1st Jan 2010 $\left[\frac{50}{800} \times 1,16,000\right]$	—	(7,250)		
Add: Cost of investment purchased			21,000	
Less: Capital Dividend			(1,500)*	19,500
(A)	1,16,000	1,08,750		1,28,250
Nominal Value of Shares	80,000	75,000		85,000
Capital Profit	28,000 [50,000 × 80 % - 12,000]	26,250 [50,000 – 15,000 (dividend of last year) × 75 %]		31,750** [50,000 – 15,000] × 75 % + [70,000 – 15,000] × 10 %
(B)	1,08,000	1,01,250		1,16,750
Goodwill (A-B)	8,000	7,500		11,500

* Dividend out of Capital Profits

** Alternative Calculation :

10% of 20,000 i.e. profit earned and not yet distributed after Jan., 2009 till 31st Dec. 2010 (55,000-35,000) plus 85% of ₹ 35,000 profit remaining undistributed out of profits as on 1.1.2009

Note: In 2011, ₹ 21,000 must have been spent since by that amount the book value of investment has gone up. [1,40,000 – 1,19,000]

Minority interest		Capital & Profits		
		₹	₹	₹
31st Dec. 2009	20%	20,000	12,400 [62,000 X 20 %]	= 32,400
31st Dec. 2010	25%	25,000	17,500 [70,000 X 25 %]	= 42,500
31st Dec. 2011	15%	15,000	12,000 [80,000 X 15 %]	= 27,000

In a particular situation it may so happen that the losses applicable to the minority in a consolidated subsidiary exceed the minority interest in the equity of the subsidiary. Such excess and any further losses should be charged against majority interest. If the subsidiary company subsequently reports profits, such profits should be allocated to majority interest unless the minority's share of losses previously absorbed has been recovered.

Illustration 5

A Ltd. acquired 70% of equity shares of B Ltd. as on 1st January, 2005 at a cost of ₹ 10,00,000 when B Ltd. had an equity share capital of ₹ 10,00,000 and reserves and surplus of ₹ 80,000. Both the companies follow calendar year as the accounting year. In the four consecutive years B Ltd. fared badly and suffered losses of ₹ 2,50,000, 4,00,000, ₹ 5,00,000 and ₹ 1,20,000 respectively. Thereafter in 2009, B Ltd. experienced turnaround and registered an annual profit of ₹ 50,000. In the next two years i.e. 2010 and 2011, B Ltd. recorded annual profits of ₹ 1,00,000 and ₹ 1,50,000 respectively.

Show the minority interests and cost of control at the end of each year for the purpose of consolidation.

Solution

	Minority Interest (30%) ₹	*Holding Interest (70%)* ₹	
Share of net assets of B Ltd. as on 1.1.2005	3,24,000	7,56,000	
Cost of acquisition	—	10,00,000	
	3,24,000	2,44,000	(goodwill)
Minority's share of losses of B Ltd: year ended 31.12.2005	75,000		
Minority interest as on' 31.12.2005	2,49,000		

Minority's share of losses of B Ltd.:		
year ended 31.12.2006	1,20,000	
Minority interest as on 31.12.2006	1,29,000	
Minority's share of losses of B Ltd.		
year ended 31.12.2007	1,29,000*	
Minority interest as on 31.12.2007	Nil	
Minority's share of losses for 2008	Nil	
Minority's share of profits of B Ltd. for 2009	Nil	
Minority's share of profit for 2010	Nil	
Minority's share of profit for 2011 (₹, 45,000 – ₹ 12,000)	33,000*	
Minority interest as on 31.12.2011	33,000	

2.7 Preparation of Consolidated Balance Sheet

While preparing the consolidated balance sheet, assets and outside liabilities of the subsidiary company are merged with those of the holding company. Share capital and reserves and surplus of subsidiary company are apportioned between holding company and minority shareholders. These items, along with investments of holding company in shares of subsidiary company are not separately shown in consolidated balance sheet. The net amounts resulting from various computations on these items, shown as (a) minority interest (b) cost of control (c) holding company's share in post-acquisition profits of the subsidiary company (added to appropriate concerned account of the holding company) are entered in consolidated balance sheet. The method of calculation of these items with detailed treatment of other relevant issues has been dealt with in various paras separately.

As per para 15 of AS 21, if an enterprise makes two or more investments in another enterprise at different dates and eventually obtain control of the other enterprise the consolidated financial statements are presented only from the date on which holding-subsidiary relationship comes in existence.

If two or more investments are made over a period of time, the equity of the subsidiary at the date of investment for the purposes of paragraph 13 of AS 21, is generally determined on a step-by-step basis; however, if small investments are made over a period of time and then an investment is made that results in control, the date of the latest investment, as a practicable measure, may be considered as the date of investment.

* In the year 2007, the minority's share of losses actually comes to ₹1,50,000. But since minority interest as on 31.12.2006 was less than the share of loss, the excess of loss of ₹21,000 is to be added to A Ltd.'s share of losses. Similarly for the year 2008, the entire loss of B Ltd. is to be adjusted against A Ltd.'s profits for the purpose of consolidation. Therefore, upto 2008, the minority's share of B Ltd.'s losses of ₹57,000 are to be borne by A Ltd. Thereafter, the entire profits of B Ltd. will be allocated to A Ltd. unless the minority's share of losses previously absorbed (₹57,000) has been recovered. Such recovery is fully made in 2011 and therefore minority interest of ₹ 33,000 is shown after adjusting fully the share of losses of minority previously absorbed by A Ltd.

Illustration 6

From the following summarized balance sheets of H Ltd. and its subsidiary S Ltd. drawn up at 31st March, 2012, prepare a consolidated balance sheet as at that date, having regard to the following :

(i) Reserves and Profit and Loss Account of S Ltd. stood at ₹ 25,000 and ₹ 15,000 respectively on the date of acquisition of its 80% shares by H Ltd. on 1st April, 2011.

(ii) Machinery (Book-value ₹ 1,00,000) and Furniture (Book value ₹ 20,000) of S Ltd. were revalued at ₹ 1,50,000 and ₹ 15,000 respectively on 1.4.2011 for the purpose of fixing the price of its shares. [Rates of depreciation: Machinery 10%, Furniture 15%.]

Summarised Balance Sheet of H Ltd. as on 31st March, 2012

	H Ltd.	S. Ltd.	Assets	H Ltd.	S Ltd.
	₹	₹		₹	₹
Equity and Liabilities			Non-current assets		
Shareholders' funds			Fixed assets		
Share Capital			Machinery	3,00,000	90,000
Shares of			Furniture	1,50,000	17,000
₹ 100 each	6,00,000	1,00,000	Other non-current assets	4,40,000	1,50,000
			Non-current Investments		
Reserves	2,00,000	75,000	Shares in		
Profit and Loss			S Ltd.:		
Account	1,00,000	25,000	800 shares at		
Creditors	1,50,000	57,000	₹ 200 each	1,60,000	—
	10,50,000	2,57,000		10,50,000	2,57,000

Solution

Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd.
as at 31st March, 2012

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		6,00,000
(b) Reserves and Surplus	1	3,44,600

	(2) Minority Interest		48,150
	(3) Current Liabilities		
	(a) Trade Payables	2	2,07,000
	Total		11,99,750
II.	Assets		
	(1) Non-current assets		
	(a) Fixed assets		
	(i) Tangible assets	3	5,97,750
	(ii) Intangible assets	4	12,000
	(b) Other non- current assets	5	5,90,000
	Total		11,99,750

Notes to Accounts

				₹
1.	Reserves and Surplus			
	Reserves (W.N.3)		2,00,000	
	Add: 4/5th share of S Ltd.'s post-acquisition reserves		40,000	2,40,000
	Profit and Loss Account		1,00,000	
	Add: 4/5th share of S Ltd.'s post-acquisition profits		4,600	1,04,600
				3,44,600
2.	Trade Payables			
	H Ltd.		1,50,000	
	S Ltd.		57,000	2,07,000
3.	Tangible Assets			
	Machinery			
	H. Ltd.		3,00,000	
	S Ltd.	1,00,000		
	Add: Appreciation	50,000		
		1,50,000		
	Less: Depreciation	(15,000)	1,35,000	
	Furniture			
	H. Ltd.		1,50,000	
	S Ltd.	20,000		
	Less: Decrease in value	(5,000)		

		15,000		
	Less: Depreciation	(2,250)	12,750	5,97,750
4.	Intangible assets			
	Goodwill [WN 6]			12,000
5.	Other non-current assets			
	H Ltd.		4,40,000	
	S Ltd.		1,50,000	5,90,000

Working Notes:

1.	Pre-acquisition profits and reserves of S Ltd.	₹
	Reserves	25,000
	Profit and Loss Account	15,000
		40,000
	H Ltd.'s = 4/5 × 40,000	32,000
	Minority Interest= 1/5 × 40,000	8,000
2.	Profit on revaluation of assets of S Ltd.	
	Profit on Machinery ₹ (1,50,000 – 1,00,000)	50,000
	Less: Loss on Furniture ₹ (20,000 – 15,000)	5,000
	Net Profit on revaluation	45,000
	H Ltd.'s share 4/5 × 45,000	36,000
	Minority Interest 1/5 × 45,000	9,000
3.	Post-acquisition reserves of S Ltd.	
	Post acquisition reserves = ₹ (75,000 – 25,000)	50,000
	H Ltd.'s share 4/5 × 50,000	40,000
	Minority interest 1/5 × 50,000	10,000
4.	Post -acquisition profits of S Ltd.	
	Post-acquisition profits ₹ (25,000 – 15,000)	10,000
	Add: Excess depreciation charged furniture @ 15% on ₹ 5,000 i.e. (20,000 – 15,000)	750
		10,750
	Less: Under depreciation on machinery @ 10% on ₹ 50,000 i.e. (1,50,000 – 1,00,000)	(5,000)
	Adjusted post-acquisition profits	5,750
	H Ltd.'s share 4/5 × 5,750	4,600
	Minority Interest 1/5 × 5,750	1,150
5.	Minority Interest	
	Paid-up value of (1,000 – 800) = 200 shares held by outsiders i.e. 200 × ₹ 100	20,000

Add: 1/5th share of pre-acquisition profits and reserves	8,000
1/5th share of profit on revaluation	9,000
1/5th share of post-acquisition reserves	10,000
1/5th share of post-acquisition profit	1,150
	48,150
6. Cost of Control or Goodwill	
Paid-up value of 800 shares held by H Ltd. i.e. 800 × ₹ 100	80,000
Add: 4/5th share of pre-acquisition profits and reserves	32,000
4/5th share of profit on the revaluation	36,000
Intrinsic value of shares on the date of acquisition	1,48,000
Price paid up by H Ltd. for 800 shares	1,60,000
Less: Intrinsic value of the shares	(1,48,000)
Cost of control or Goodwill	12,000

2.8 Elimination of Intra-Group Transactions

General rules: In order to present financial statements for the group in a consolidated format, the effect of transactions between group enterprises should be eliminated. Para 16 of AS 21 states that intragroup balances and intragroup transactions and resulting unrealised profits should be eliminated in full. Unrealised losses resulting from intragroup transactions should also be eliminated unless cost cannot be recovered.

Liabilities due to one group enterprise by another will be set off against the corresponding asset in the other group enterprise's financial statements; sales made by one group enterprise to another should be excluded both from turnover and from cost of sales or the appropriate expense heading in the consolidated statement of profit and loss.

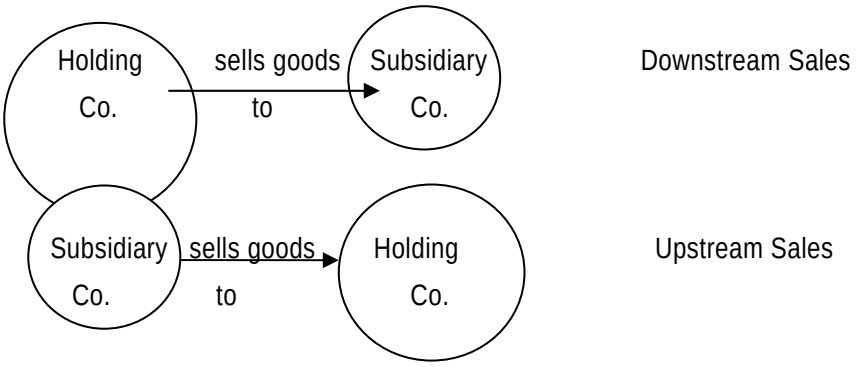
To the extent that the buying enterprise has further sold the goods in question to a third party, the eliminations to sales and cost of sales are all that is required, and no adjustments to consolidated profit or loss for the period, or to net assets, are needed. However, to the extent that the goods in question are still on hand at year end, they may be carried at an amount that is in excess of cost to the group and the amount of the intra-group profit must be eliminated, and assets reduced to cost to the group.

For transactions between group enterprises, unrealized profits resulting from intra-group transactions that are included in the carrying amount of assets, such as inventories and tangible fixed assets, are eliminated in full. The requirement to eliminate such profits in full applies to the transactions of all subsidiaries that are consolidated – even those in which the group's interest is less than 100%.

Unrealised profit in inventories: Where a group enterprise sells goods to another, the selling enterprise, as a separate legal enterprise, records profits made on those sales. If these goods are still held in inventory by the buying enterprise at the year end, however, the profit recorded by the selling enterprise, when viewed from the standpoint of the group as a whole, has not yet been earned, and will not be earned until the goods are eventually sold outside the group.

On consolidation, the unrealized profit on closing inventories will be eliminated from the group's profit, and the closing inventories of the group will be recorded at cost to the group.

Here, the point to be noted is that one has to see whether the intragroup transaction is "upstream" or "down stream". Upstream transaction is a transaction in which the subsidiary company sells goods to holding company. While in the downstream transaction holding company is the seller and subsidiary company is the buyer.



In the case of upstream transaction, goods are sold by the subsidiary to holding company; profit is made by the subsidiary company, which is ultimately shared by the holding company and the minority shareholders. In such a transaction, if some goods remain unsold at the balance sheet date, the unrealized profit on such goods should be eliminated from minority interest as well as from consolidated profit on the basis of their share holding besides deducting the same from unsold stock. But in the case of downstream transaction the whole profit is earned by the holding company, therefore whole unrealized profit should be adjusted from unsold stock account and consolidated profit and loss account only irrespective of the percentage of the shares held by the parent

Unrealised profit on transfers of non-current assets: Similar to the treatment described above for unrealized profits in inventories, unrealized inter-company profits arising from intra-group transfers of fixed assets are also eliminated from the consolidated financial statements.

Unrealised losses: Unrealised losses resulting from intra-group transactions that are deducted in arriving at the carrying amount of assets are also eliminated unless cost cannot be recovered.

2.9 Preparation of Consolidated Profit and Loss Account

Preparation of Consolidated Profit and Loss Account of holding company and its subsidiaries is not very difficult.

All the revenue items are to be added on line by line basis and from the consolidated revenue items inter-company transactions should be eliminated.

For example, a holding company may sell goods or services to its subsidiary, receives consultancy fees, commission, royalty etc. These items are included in sales and other income of the holding company and in the expense items of the subsidiary. Alternatively, the subsidiary may also sell goods or services to the holding company. These inter-company

transactions are to be eliminated in full.

If there remains any unrealised profit in the stock of good, of any of the Group Company, such unrealised profit is to be eliminated from the value of stock to arrive at the consolidated profit.

Also it is necessary to eliminate the share of holding company in the proposed dividend of the subsidiary. See Illustrations 10, 11 to understand the technique of preparation of the consolidated profit and loss account.

Illustration 7

Given below are the Profit & Loss Account of H Ltd. and its subsidiary Ltd. for the year ended 31st March, 2012.

	H Ltd. (₹ *in lacs)*	*S Ltd.* (₹ *in lacs)*
Incomes:		
Sales and other income	*5,000*	*1,000*
Increase in stock	*1,000*	*200*
	6,000	*1,200*
Expenses:		
Raw material consumed	*800*	*200*
Wages and Salaries	*800*	*150*
Production expenses	*200*	*100*
Administrative Expenses	*200*	*100*
Selling and Distribution Expenses	*200*	*50*
Interest	*100*	*50*
Depreciation	*100*	*50*
	2,400	*700*
Profit before tax	*3,600*	*500*
Provision for tax	*1,200*	*200*
Profit after tax	*2,400*	*300*
Proposed dividend	*1,200*	*150*
Balance of Profit	*1,200*	*150*

Other Information:

H Ltd. sold goods to S Ltd. of ₹ 120 lacs at cost plus 20%. Stock of S Ltd. includes such goods valuing ₹ 24 lacs. Administrative Expenses of S Ltd. include ₹ 5 lacs paid to H Ltd. as consultancy fees. Selling and Distribution expenses of H Ltd. include ₹ 10 lacs paid to S Ltd. as commission.

H Ltd. holds 80% of equity share capital of ₹ 1,000 lacs in S Ltd. H Ltd. took credit to its Profit and Loss Account, the proportionate amount of dividend declared and paid by S Ltd. for the year 2010-2011.

Solution

Consolidated Profit & Loss Account of H Ltd. and its subsidiary S Ltd.
for the year ended on 31st March, 2012

Particulars		Note No.	₹ in Lacs
I.	Revenue from operations	1	5,865
II.	Total revenue		5,865
III.	Expenses		
	Cost of Material purchased/Consumed	3	1,180
	Changes of Inventories of finished goods	2	(1,196)
	Employee benefit expense	4	950
	Finance cost	6	150
	Depreciation and amortization expense	7	150
	Other expenses	5	535
	Total expenses		1,769
IV.	Profit before Tax (II-III)		4,096
V.	Tax Expenses	8	1,400
VI.	Profit After Tax		2,696
Profit transferred to Consolidated Balance Sheet			
Profit After Tax			2,696
Proposed dividend			
	H Ltd.	1,200	
	S Ltd.	150	
		1,350	
Less: Share of H Ltd. in proposed dividend of S Ltd.			
	80% of ₹ 150 lacs	(120)	(1,230)
Profit to be transferred to consolidated balance sheet			1,466

Notes to Accounts

		₹ in Lacs	₹ in Lacs
1.	Revenue form Operations		
	Sales and other income		
	H Ltd.	5,000	
	S Ltd.	1,000	
		6,000	
	Less: Inter-company Sales	(120)	

	Consultancy fees received by H Ltd. from S Ltd.	(5)	
	Commission received by S Ltd. from H Ltd.	(10)	5,865
2.	Increase in Stock		
	H Ltd.	1,000	
	S Ltd.	200	
		1,200	
	Less: Unrealised profits ₹ 24 lacs × $\frac{20}{120}$	(4)	1,196
			7,061
3.	Cost of Material purchased/consumed		
	H Ltd.	800	
	S Ltd.	200	
		1,000	
	Less: Purchases by S Ltd. from H Ltd.	(120)	880
	Direct Expenses		
	H Ltd.	200	
	S Ltd.	100	300
			1,180
4.	Employee benefits and expenses		
	Wages and Salaries:		
	H Ltd.	800	
	S Ltd.	150	950
5.	Other Expenses		
	Administrative Expenses		
	H Ltd.	200	
	S Ltd.	100	
		300	
	Less: Consultancy fees received by H Ltd. from S Ltd.	(5)	295
	Selling and Distribution Expenses:		
	H Ltd.	200	
	S Ltd.	50	
		250	
	Less: Commission received from S Ltd. from H Ltd.	(10)	240
			535
6.	Finance Cost		
	Interest:		
	H Ltd.	100	
	S Ltd.	50	150

7.	Depreciation and Amortisation		
	Depreciation:		
	H Ltd.	100	
	S Ltd.	50	150
8.	Provision for tax		
	H Ltd.	1,200	
	S. Ltd.	200	1,400

It is assumed that H Ltd. acquired shares in S Ltd. before 2010-2011.

Note: Since the amount of dividend received by H Ltd. for the year 2010-2011 is not given, it has not been deducted from 'sales and other income' in consolidated profit and loss account and not added to consolidated opening retained earnings (which is also not given).

Illustration 8

The Trial Balances of H Ltd. and S Ltd. as on 31st December 2011 were as under:

	H Ltd.		*S Ltd.*	
	Dr. ₹	*Cr.* ₹	*Dr.* ₹	*Cr.* ₹
Equity Share Capital (Share of ₹ 100 each)		*10,00,000*		*2,00,000*
7% Preference Share Capital (Share of ₹ 100 each)		*—*		*2,00,000*
Reserves		*3,00,000*		*1,00,000*
6% Debentures		*2,00,000*		*2,00,000*
Sundry Debtors/Creditors	*80,000*	*90,000*	*50,000*	*60,000*
P&L A/c balance		*20,000*		*15,000*
Purchases/Sales	*5,00,000*	*9,00,000*	*6,00,000*	*9,50,000*
Wages & Salaries	*1,00,000*	*—*	*1,50,000*	
Debenture Interest	*12,000*		*12,000*	
General Expenses	*80,000*		*60,000*	
Preference-Dividend up to 30.6.2011		*3,500*	*7,000*	
Stock (31.12.2011)	*1,00,000*		*50,000*	
Cash at Bank	*13,500*		*6,000*	
Investment in S Ltd.	*5,28,000*		*—*	
Fixed Assets	*11,00,000*		*7,90,000*	
	25,13,500	*25,13,500*	*17,25,000*	*17,25,000*

Investment in S Ltd. were acquired on 1.4.2011 and consisted of 80% of Equity Capital and 50% of Preference Capital. Depreciation on fixed assets is written off @ 10% p.a. After acquiring control over S Ltd., H Ltd. supplied to it goods at cost plus 20%, the total invoice value of such goods being ₹ 60,000; 1/4 of such goods was still in stock at the end of the year.

Prepare the Consolidated Profit and Loss Account for the year ended on 31st December, 2011.

Solution

Consolidated Profit and Loss Account of H Ltd. and S Ltd.
for the year ended 31st December, 2011

Particulars		Note No.	₹
I.	Revenue from operations	1	17,90,000
II.	Total revenue		17,90,000
III.	Expenses		
	Cost of Material purchased/Consumed	2	10,40,000
	Changes of Inventories of finished goods		
	Employee benefit expense (1,00,000 + 1,50,000)		2,50,000
	Finance cost (12,000 + 12,000)		24,000
	Depreciation and amortization expense[1,10,000+79,000]		1,89,000
	Other expenses [80,000 + 60,000]		1,40,000
	Total expenses		16,43,000
IV.	Profit before Tax (II-III)		1,47,000
Profit transferred to Consolidated Balance Sheet			
Profit After Tax			1,47,000
Preference dividend		3,500	
Preference dividend payable		3,500	(7,000)
			1,40,000
Less: Minority interest (WN 3)			(7,000)
	Capital reserve*		(7,000)
	Investment Account- dividend for 3 months (prior to acquisition)		(1,750)
	Stock reserve $\left[\frac{60,000}{4} \times \frac{20}{120}\right]$		(2,500)
Profit to be transferred to consolidated balance sheet			1,21,750

Notes to Accounts

		₹	₹
1	Revenue from Operations		
	H Ltd.	9,00,000	
	S Ltd.	9,50,000	
	Total	18,50,000	
	Less : Intragroup sales (H sold to S)	(60,000)	17,90,000

* Capital Reserve is made up of 3 month's profit upto 1.4.2009 i.e. ¼ x 35,000 x 80/100.

2	Cost of Materials Purchased/Consumed		
	H Ltd.	5,00,000	
	S Ltd.	6,00,000	
	Total	11,00,000	
	Less : Intragroup sales (H sold to S)	(60,000)	10,40,000

Working Note

Profit of Subsidiary

Revenue From Operations		9,50,000
Less : Expenses		
Cost of Material purchased/Consumed	6,00,000	
Changes of Inventories of finished goods		
Employee benefit expense	1,50,000	
Finance cost	12,000	
Depreciation and amortization expense	79,000	
Other expenses	60,000	
Total expenses		(9,01,000)
Profit Before Tax		49,000
Preference Dividend		7,000
Preference Dividend Payable		7,000
Profit available for shareholders		35,000
Minority Share (20 %)		7,000

2.10 Preparation of Consolidated Cash Flow Statement

A holding company has to prepare a consolidated cash flow statement if it is required to prepare cash flow statement.

Same as Consolidated Profit and Loss account, the preparation of consolidated Cash flow statement is also not difficult. All the items of Cash flow from operating activities, investing activities and financing activities are to be added on line by line basis and from the consolidated items, inter-company transactions should be eliminated. Below given is the Consolidated Cash Flow Statement with hypothetical figures:

Consolidated Cash Flow Statement

			(₹ in million)
	A Company	*B Company*	*Total*
Cash Flow From Operating Activities			
Change in Reserve	8	2	10

Change in P & L A/c	0	1	1
Proposed Dividend	22		22
Tax Provision	20	1	21
Depreciation	10	5	15
Interest	-10	10	0
	50	19	69
Less: Tax payment	-20	-1	-21
	30	18	48
Working Capital Adjustment	-13	12	-1
(A)	17	30	47
Cash Flow from Investment Activities			
Sale of fixed assets	30	0	30
Purchase of fixed assets	-30	-20	-50
(B)	0	-20	-20
Cash Flow from Financing Activities (C)	-22	-10	-32
Net cash flows (A+B+C)	-5	0	-5

2.11 Acquisition of Interest in Subsidiary at Different Dates

Often a holding company acquires a subsidiary in steps. As per para 15 of AS 21, "If an enterprise makes two or more investments in another enterprise at different dates and eventually obtains control of the other enterprise, the consolidated financial statements are presented only from the date on which holding-subsidiary relationship comes in existence. If two or more investments are made over a period of time, the equity of the subsidiary at the date of investment, is generally determined on a step-by-step basis; however, if small investments are made over a period of time and then an investment is made that results in control, the date of the latest investment, as a practicable measure, may be considered as the date of investment.

Illustration 9

H Ltd. acquired 20% shares in S Ltd. on 1-7-2011 for ₹ 50 million, then another 20% on 1-10-2011 for ₹ 60 million and finally, another 20% on 1-11-2011 for ₹ 80 million. S Ltd. became subsidiary of H Ltd. on and from1-11-2011. Balance of Reserve of S Ltd. as on 1-4-2011 (₹ in million) 60.

Summarised Balance Sheets of H Ltd. and S Ltd.
as on 31-3-2012

₹ in Million

	H Ltd.	*S Ltd.*
Equity Share Capital	*500*	*200*
General Reserve	*400*	*120*
Profit & Loss A/c	*10*	*12*
Sources	*910*	*332*

Fixed Assets		
Gross Block	*800*	*350*
Less: Accumulated Depreciation	*(100)*	*(30)*
Net Block	*700*	*320*
Investments	*190*	
Current Assets	*20*	*12*
Applications	*910*	*332*

Solution

In this case goodwill paid in acquiring cost of control should be computed step by step basis:

₹ in million

Goodwill	1-7-2011	1-10-2011	1-11-2011	Total	Minority Interest
Cost of investments (A)	50	60	80	190	
Book Value of Investments:					
Equity Share Capital	40 (200 X 20 %)	40 (200 X 20 %)	40 (200 X 20 %)	120.00	80 (200-120)
General Reserve 1-4-2011	12 (60 X 20 %)	12 (60 X 20 %)	12 (60 X 20 %)	36.00	24 (60-36)
Pre-acquisition profit of 2011-2012 WN 1	3.6	7.2	8.40	19.20	
(B)	55.6	59.2	60.40	175.20	
Cost of Control (A-B)	-5.60	0.80	19.60	14.80	
40% of post-acquisition reserve and profit					28.80
					132.80

Consolidated Profit & Loss a/c					
Balance of P & L A/c of H Ltd.					10
Share of current reserve [72 x 60 % - 19.2]					24
					34

Working Note:

Total Profit from 1-4-2011 to 31-03-2012 = 120 + 12 – 60 = 72 Million

Acquistion Date	Pre Acquistion Period	Pre Acquistion Duration [A]	% Holding [B]	Profit amount 72 x [A]/12 X [B]
1-7-2011	1-4-2011 to 1-7-2011	3 Months	20	3.6
1-10-2011	1-4-2011 to 1-10-2011	6 Months	20	7.2
1-11-2011	1-4-2011 to 1-11-2011	7 Months	20	8.4

Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd.
as at 31st March, 2012

Particulars	Note No.	(₹ *in Million*)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		500.00
(b) Reserves and Surplus	1	434.00
(2) Minority Interest		132.80
Total		1,066.80
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
(i) Tangible assets	2	1,020.00
(ii) Intangible assets (Goodwill)		14.80
(2) Current assets (20 + 12)		32.00
Total		1,066.80

Notes to Accounts

		(₹ *in Million*)
1. Reserves and Surplus		
General reserve	400	
Profit and Loss A/c [As calculated above]	34	434.00
2. Tangible assets		
Gross Block		1,150.0
Less: Accumulated Depreciation		(130.0)
Net Block		1,020.0

Another situation may be that a parent company increases or decreases its stake in the subsidiary.

For example, H Ltd. Acquired 70% of the equity shares in S Ltd. It further acquires 10% of the equity shares subsequently or sells 10% of the equity shares. In both the cases step by step method should be followed for measuring goodwill/capital reserve.

2.12 Uniform Accounting Policies

Para 20 of AS 21 mentions that consolidated financial statements shall be prepared using uniform accounting policies for like transactions and other events in similar circumstances

If any company in the same group uses accounting policies other than those adopted in consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments should be made.

If it is not practicable to use uniform accounting policies in preparing the consolidated financial statements, the fact should be disclosed together with the proportions of items to which

different accounting policies have been applied.

For example, if the subsidiary company follows LIFO method for valuation of inventories and the holding company follows FIFO method, the financial statement of subsidiary company should be restated by adjusting the value of inventories to bring the same in line with the valuation procedure adopted by the holding company. Then only consolidation can be considered.

Illustration 10

Consider the following summarized balance sheets of subsidiary B Ltd.:

	2010 ₹	2011 ₹		2010 ₹	2011 ₹
Share-Capital			Fixed Assets		
Issued & subscribed			Cost	3,20,000	3,20,000
5,000 equity shares			Less: Accumulated		
of ₹ 100 each	5,00,000	5,00,000	depreciation	(48,000)	(96,000)
Reserves & Surplus				2,72,000	2,24,000
Revenue reserves	2,86,000	7,14,000	Investments		
Current Liabilities &			at cost	—	4,00,000
Provisions:			Current Assets:		
Sundry Creditors	4,90,000	4,94,000	Stock	5,97,000	7,42,000
Bank overdraft	—	1,70,000	Sundry Debtors	5,94,000	8,91,000
Provision for taxation	3,10,000	4,30,000	Prepaid Expenses	72,000	48,000
			Cash at Bank	51,000	3,000
	15,86,000	23,08,000		15,86,000	23,08,000

Consider also the following information:

(a) *B Ltd. is a subsidiary of A Ltd. Both the companies follow calendar year as the accounting year.*

(b) *A Ltd. values stocks on LIFO basis while B Ltd. used FIFO basis. To bring B Ltd.'s values in line with those of A Ltd. its value of stock is required to be reduced by ₹ 12,000 at the end of 2010 and ₹ 34,000 at the end of 2011.*

(c) *Both the companies use straight-line method of depreciation. However A Ltd. charges depreciation @ 10%.*

(d) *B Ltd. deducts 1% from sundry debtors as a general provision against doubtful debts.*

(e) *Prepaid expenses in B Ltd. include advertising expenditure carried forward of ₹ 60,000 in 2010 and ₹ 30,000 in 2011, being part of initial advertising expenditure of ₹ 90,000 in 2010 which is being written off over three years. Similar amount of advertising expenditure of A Ltd. has been fully written off in 2010.*

Restate the balance sheet of B Ltd. as on 31st December, 2011 after considering the above information for the purpose of consolidation. Such restatement is necessary to make the accounting policies adopted by A Ltd. and B Ltd. uniform:

Solution

Adjusted revenue reserves of B Ltd.:

	₹	₹
Revenue reserves as given		7,14,000
Add: Depreciation over charged (₹ 16,000 × 2)	32,000	—
Provision for doubtful debts [8,91,000 / 99 X 1]	9,000	41,000
		7,55,000
Less: Reduction in stock-in-trade	34,000	
Advertising expenditure to be written off	30,000	(64,000)
Adjusted revenue reserve		6,91,000

Restated Balance Sheet of B Ltd.
as at 31st December, 2011

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		5,00,000
(b) Reserves and Surplus	1	6,91,000
(2) Current Liabilities		
(a) Short term borrowings	2	1,70,000
(b) Trade Payables		4,94,000
(c) Other current liabilities	3	4,30,000
Total		22,85,000
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	4	2,56,000
(b) Non Current Investments		4,00,000
(2) Current assets		
(a) Inventories		7,08,000
(b) Trade Receivables		9,00,000
(c) Cash & Cash Equivalents		3,000
(d) Other current assets	5	18,000
Total		22,85,000

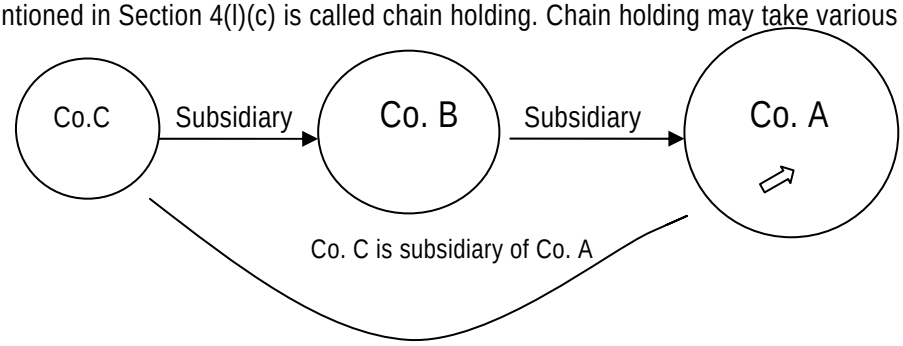
Notes to Accounts

			₹
1.	Reserves and Surplus		
	Revenue Reserve		6,91,000
2.	Short term borrowings		
	Bank overdraft		1,70,000
3.	Other current liabilities		
	Provision for taxation		4,30,000
4.	Tangible Assets		
	Cost	3,20,000	
	Less : Depreciation to date	(64,000)	2,56,000
5.	Other current assets		
	Prepaid expenses		18,000

2.13 Chain Holding

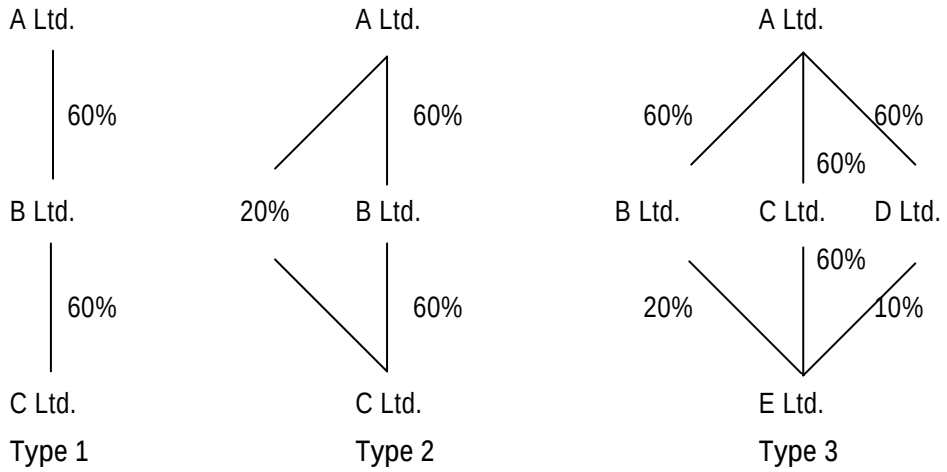
Suppose that Company B is subsidiary of Company A and Company C is subsidiary of Company B.

By virtue of Section 4(1)(c) of the Companies Act, 1956 C becomes subsidiary of Company A. Popularly, Company C is called sub-subsidiary of Company A and the type of holding mentioned in Section 4(l)(c) is called chain holding. Chain holding may take various forms



Chain Holding

In Type 1 the parent company does not hold any share in the sub-subsidiary. In Type 2 both the parent and subsidiary hold shares of sub-subsidiary. In Type 3 more than one subsidiaries of the parent company hold shares in the sub-subsidiary. There may be different other types of chain holding.



2.13.1 Treatment of Capital Profit of Sub-subsidiary in the Consolidation Process: There are two approaches, namely, **direct method and indirect method.** Capital Profit of the sub-subsidiary should be firstly apportioned between minority interest and group interest. The group interest should be taken directly for calculation of goodwill/capital reserve. This is called direct method.

Let us take an example. A Ltd.; holds 60% shares of B Ltd. and 20% shares of C Ltd.; B Ltd. holds 60% shares of C Ltd. Total profit of C Ltd. is ₹ 1,00,000 of which pre-acquisition profit is ₹ 40,000.

As per direct method capital profit (i.e., pre-acquisition profit in this case) should be apportioned as follows:

₹ $40,000 \times \frac{20}{100}$ = ₹ 8,000 to minorities of C Ltd.

₹ $40,000 \times \frac{80}{100}$ = ₹ 32,000 to the group which is to be considered for calculating goodwill or capital reserve.

For computation of goodwill / capital reserve for the purpose of consolidation, cost of group investments is compared to their face value. Cost of investments should be arrived at after adjusting pre-acquisition profit/loss relating to such investments. So direct approach appears to be more logical.

In the indirect approach, pre-acquisition profit/loss is apportioned among minorities of the sub-subsidiaries and to the respective group companies. From the shares of respective group companies, their minority interests are deducted and the parent company gets its indirect shares. In the example given above A Ltd.'s direct shares to C Ltd.; is to the extent of 20% and indirect through B Ltd. is 60% of 60% i.e. 36%. So while computing goodwill or capital reserve for the purpose of consolidation (only 20% + 36%) i.e. 56% of the capital profit of C Ltd. is considered. In other words, the calculation will be as follows:

$$₹\ 40,000 \times \frac{20}{100} = ₹\ 8,000 \text{ to minorities of C Ltd.}$$

$$₹\ 40,000 \times \frac{20}{100} = ₹\ 8,000 \text{ to A Ltd.}$$

$$₹\ 40,000 \times \frac{60}{100} = ₹\ 24,000 \text{ to B Ltd.}$$

Out of B Ltd.'s share of ₹ 24,000 A Ltd. will get 60%. This means A Ltd.'s indirect share in capital profit of C Ltd. is ₹ 24,000 × 60% i.e. ₹ 14,400. In total ₹ 22,400 (14,400 + 8,000) is to be taken for computation for goodwill/capital reserve. This comes to 56% of ₹ 40,000.

Illustration 11

Prepare the Consolidated Balance Sheet as on December 31, 2011 of group of companies A Ltd., B Ltd. and C Ltd. Their summarized balance sheets on that date are given below:

Liabilities	*A Ltd.* ₹	*B Ltd.* ₹	*C Ltd.* ₹
Share Capital (share of ₹ 100 each)	*1,25,000*	*1,00,000*	*60,000*
Reserves	*18,000*	*10,000*	*7,200*
Profit & Loss A/c	*16,000*	*4,000*	*5,000*
Sundry Creditors	*7,000*	*3,000*	*—*
A Ltd.	*—*	*7,000*	*—*
C Ltd.	*3,300*	*—*	*—*
Total	*1,69,300*	*1,24,000*	*72,200*
Assets			
Fixed Assets	*28,000*	*55,000*	*37,400*
Investments in shares-			
B Ltd.	*85,000*	*—*	*—*
C Ltd.	*—*	*53,000*	*—*
Stocks	*22,000*	*6,000*	*—*
B Ltd.	*8,000*	*—*	*—*
Debtors	*26,300*	*10,000*	*31,500*
A Ltd.	*—*	*—*	*3,300*
Total	*1,69,300*	*1,24,000*	*72,200*

Other information:

(i) A Ltd. holds 750 shares in B Ltd. and B Ltd. holds 400 shares in C Ltd. These holdings were acquired on 30th June, 2011

(ii) On 1st January, 2011 the following balances stood in the books of B Ltd. and C Ltd.

	B Ltd. ₹	*C Ltd.* ₹
Reserves	*8,000*	*6,000*
P & L Account	*1,000*	*1,000*

(iii) C Ltd., sold goods costing ₹ 2,500 to B Ltd. for ₹ 3,100. These goods still remain unsold.

Solution

Workings Notes:

Shareholding Pattern

	B Ltd.	C Ltd.
Total Number of Shares	1,000	600
A Ltd's Holding	750	NA
B Ltd's Holding	NA	400
Minority Holding	250	200
Minority %	25 %	33.33%

(1) Analysis of Profits:

	Capital Profit ₹	*Revenue Reserve* ₹	*Revenue Profit* ₹
C Ltd.			
Reserve on 1.1.2011	6,000	—	—
Additional Reserve created in 2011 [7,200 – 6,000] = 1,200	600 [1,200 X ½]	600 [1,200 X ½]	—
P & L A/c, Balance on 1.1.2011	1,000	—	—
Profit for 2011 [5,000 – 1,000] = 4,000	2,000 [4,000 X ½]	—	2,000 [4,000 X ½]
	9,600	600	2,000
Due to outsiders, 1/3	3,200	200	667
Share of B Ltd. (2/3)	6,400	400	1,333
B Ltd.			
From C Ltd.	6,400*	400	1,333
Reserve on 1.1.2011	8,000	—	—
Additional Reserve created in 2011 [10,000-8,000] = 2,000	1,000 [2,000 X ½]	1,000 [2,000 X ½]	—
Profit and Loss A/c:			
Balance on 1.1.2011	1000	—	—
Profit during 2011 [4,000-1,000]=3,000	1,500 [3,000 X ½]	—	1,500 [3,000 X ½]
	17,900	1,400	2,833

* This problem has been solved by following 'indirect approach'. All subsequent illustrations are solved by following 'direct approach'.

Due to outsiders (1/4)	4,475	350	708
Share of A Ltd.	13,425	1,050	2,125
A Ltd.		18,000	16,000
			18,125
Less: Stock Reserve			(600)
		19,050	17,525

Notes:

(i) During 2011, ₹ 1,200 has been added to the Reserves of C Ltd., and ₹ 2,000 to the Reserves of B Ltd. The profit must have been earned during the whole of the year; hence, half of these figures (i.e., up to 30.6.2011) must be considered as capital pre-acquisition and the remaining revenue.

(ii) Total unrealised profit is ₹ 600, i.e., ₹ 3,100 less ₹ 2,500.

(2) Minority Interest: [From the calculations above]

	B Ltd. ₹	C Ltd. ₹
Share Capital	25,000	20,000
Share of Capital Profits	4,475	3,200
Share of Revenue Reserves	350	200
Share of Revenue Profits	708	667
Total	30,533	24,067
Grand Total		54,600

(3) Cost of Control:

Amount paid:		
A Ltd.	85,000	
B Ltd.	53,000	1,38,000
Less: Par value of shares in:		
B Ltd.	75,000	
C Ltd.	40,000	
Capital Profits*	13,425	(1,28,425)
Cost of Control*/ Goodwill		9,575

* The whole of this amount may preferably be adjusted against cost of control, instead of being added to the profits of B Ltd. Consequently capital profits will increase by ₹ 1,600 with a corresponding reduction in Minority interest.

(4) Since X Ltd. shows ₹ 8,000 against B Ltd. whereas B Ltd., shows only ₹ 7,000 in favour of A Ltd., it must be assumed that B Ltd., has remitted ₹ 1,000 to A Ltd.; not yet received by A Ltd. The amount is in transit.

(5) If capital profit is increased by ₹ 1,600 cost of control will be ₹ 7,975.

Consolidated Balance Sheet of A Ltd.
and its subsidiaries B Ltd. and C Ltd.,
as on 31st December, 2011

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		1,25,000
(b) Reserves and Surplus	1	36,575
(2) Minority Interest (W.N 2)		54,600
(3) Current Liabilities		
Trade Payables	2	10,000
Total		2,26,175
II. Assets		
(1) Non-current assets		
Fixed assets		
(i) Tangible assets	3	1,20,400
(ii) Intangible assets	4	9,575
(2) Current assets		
(a) Inventories	5	27,400
(b) Trade receivables	6	67,800
(c) Cash & Cash equivalents	7	1,000
Total		2,26,175

Notes to Accounts

			₹
1.	Reserves and Surplus		
	Reserves (W.N.1)	19,050	
	Profit and Loss Account (W.N.1)	17,525	36,575
2.	Trade Payables		
	A Ltd.	7,000	
	B Ltd.	3,000	10,000
3.	Tangible Assets		
	A Ltd.	28,000	

	B Ltd.	55,000	
	C Ltd.	37,400	1,20,400
4.	Intangible assets		
	Goodwill (W.N 3)		9,575
5.	Inventories		
	A Ltd.	22,000	
	B Ltd.	6,000	
		28,000	
	Less : Stock reserve	(600)	27,400
6	Trade Receivables		
	A Ltd.	26,300	
	B Ltd.	10,000	
	C Ltd.	31,500	67,800
7	Cash & Cash equivalents		
	Cash in transit		1,000

2.14 Treatment of Subsidiary Company Having Preference Share Capital

If the holding company has some investments in the preference shares of subsidiary, the carrying amount of such investments along with carrying amount of investments in equity shares of subsidiary company should be set off against the holding company's share in the equity of such subsidiary. The difference is treated as goodwillor capital reserve . The interest of minority shareholders of the subsidiary company will then include such portion of preference share capital of the subsidiary company which is not held by holding company.

However, if a subsidiary company has cumulative preference shares which are partly held outside the group, the holding company should compute its share of profits or losses of subsidiary after adjusting for the subsidiary's preference dividend attributable to minority shareholders, whether or not such dividends have been declared. By comparison, dividends in respect of non-cumulative shares are only recognized when declared.

2.15 Inter-Company Holdings

It is possible that the subsidiary company may also hold shares in the holding company the law would permit this only if the subsidiary company had already required the shares when the Companies Act of 1956 came into force or before the holding company acquired the shares in the subsidiary. However the subsidiary company would have no voting rights at a meeting of its holding company.

In such a situation, the calculation of the minority interest would have to be based on the fact that the subsidiary also has a claim on the profits of the holding company. The calculation will

have to be made separately for revenue and capital profits since, otherwise, cost of control cannot be ascertained correctly.

For the purpose, such profits of the holding company as existed when the subsidiary company acquired the shares should be treated as capital profits. The calculation of the minority interest would involve an algebraical equation shown below.

Illustration 12

You are given below the summarized balance sheets of two companies A Ltd. and B Ltd. as at 31-12-2011.

Prepare their consolidated Balance Sheet.

Liabilities	*A Ltd.* ₹	*B Ltd.* ₹	*Assets*	*A Ltd.* ₹	*B Ltd.* ₹
Share Capital:			*Investment:*		
(₹ 100 each)	*5,00,000*	*2,00,000*	*1,600 shares*		
Profits:			*in B Ltd.*	*2,20,000*	
Capital profit	*1,00,000*	*80,000*	*1,000 shares*		
Revenue profit	*3,00,000*	*50,000*	*in A Ltd.*		*1,50,000*
Creditors	*1,50,000*	*60,000*	*Sundry Assets*	*8,30,000*	*2,40,000*
	10,50,000	*3,90,000*		*10,50,000*	*3,90,000*

Solution

A holds 1,600 shares out of 2,000 shares of B Ltd. i.e. 4/5th of B Ltd.

B holds 1,000 shares out of 5,000 shares of A Ltd. i.e. 1/5th of A Ltd.

Suppose:

A = Revenue Profits of A Ltd., and

B = Revenue Profits of B Ltd.

Then,

$$A = 3,00,000 + \frac{4}{5}B$$

$$B = 50,000 + \frac{1}{5}A$$

$$B = 50,000 + \frac{1}{5}(3,00,000 + \frac{4}{5}B) \text{ [Substituting for A]}$$

$$B = 50,000 + 60,000 + \frac{4}{25}B$$

$$B = 1,10,000 + \frac{4}{25}B$$

25B = 27,50,000 + 4B
21B = 27,50,000
B = 1,30,952

Minority interest in Revenue profits is 1/5 of ₹ 1,30,952 or ₹ 26,190. Total revenue profits being ₹ 3,50,000 [3,00,000 + 50,000] for A Ltd. and B Ltd together, ₹ 3,23,810 [3,50,000 – 26,190] remains for the group.

Capital Profits:

$A = 1,00,000 + \frac{4}{5} B$

$B = 80,000 + \frac{1}{5} A$

$B = 80,000 + \frac{1}{5}(1,00,000 + \frac{4}{5} B)$

$B = 80,000 + 20,000 + \frac{4}{25} B$

$B = 1,00,000 + \frac{4}{25} B$

25B= 25,00,000 + 4B

21B = 25,00,000

B = 1,19,048

Minority Interest @1/5 would be ₹ 23,810.

Total being ₹ 1,80,000 for the group it would be ₹ 1,56,190

Total Minority interest:

	₹
Shares held by outsiders [2,00,000 X 1/5]	40,000
Revenue Profit	26,190
Capital Profit	23,810
	90,000

Cost of control:

		(₹)
Amount paid by both companies		3,70,000
Less : Face Value:		
Shares in B Ltd.	1,60,000	
Shares in A Ltd.	1,00,000	
Capital Profits (₹ 1,19,048 – ₹ 23,810)	95,238	(3,55,238)
Goodwill		14,762

Alternative working note:

	A Ltd. ₹	B Ltd. ₹
Capital Profits	1,00,000	80,000
Less: Transfer to make B's Capital Profit ₹ 1,19,048	(39,048)	+39,048
	60,952	1,19,048
Minority Interest		(23,810)
Share of A Ltd.		95,238
Revenue Profits	3,00,000	50,000
Less: Transfer to make B's Profit ₹ 1,30,952	(80,952)	+80,952
	2,19,048	1,30,952
Less: Minority Interest		(26,190)
Share of A Ltd.	1,04,762	
	3,23,810	1,04,762

Consolidated Balance Sheet of A Ltd. and its subsidiary B Ltd.
as on 31st December, 2011

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	4,00,000
(b) Reserves and Surplus	2	3,84,762
(2) Minority Interest		90,000
(3) Current Liabilities		
(a) Trade Payables	3	2,10,000
Total		10,84,762
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	4	10,70,000
Intangible assets		14,762
Total		10,84,762

Notes to Accounts

			₹
1.	Share Capital		
	(5000-1000) Shares of ₹ 100 each		4,00,000

2.	Reserves and Surplus		
	Capital profit	60,950	
	Revenue profit	3,23,810	3,84,760
3.	Trade Payables		
	A Ltd.	1,50,000	
	B Ltd.	60,000	2,10,000
4.	Tangible Assets		
	A Ltd.	8,30,000	
	B Ltd.	2,40,000	10,70,000

2.16 Different Reporting Dates

For the purposes of preparing consolidated financial statements, the financial statements of all subsidiaries should, wherever practicable, be prepared:

- To the same reporting date; and
- For the same reporting period as of the parent.

When the reporting dates are different, the subsidiary often prepares, for consolidation purposes, statements as at the same date as that of the parent.

(Reference : Para 18 & 19 of AS 21)

When it is impracticable to do this, financial statements drawn up to different reporting dates may be used provided that difference in reporting dates is not more than six months.

However, adjustments should be made for the effects of significant transactions or other events that occur between the date of the subsidiary's financial statements and the date of the parent's financial statements. The length of the reporting periods and any difference in the reporting dates should be the same from period to period.

AS 21 does not define 'significant events and transactions', but they may include business combinations, asset impairments, and the crystallization of contingent liabilities. A potentially significant transaction or other event requires a careful analysis of the relevant facts and circumstances to determine if an adjustment is required.

Illustration 13

Consider the following summarised balance sheets:

	A Ltd. (As on 31.3.2012)	*B Ltd. (As on 31.12.2011)*		*A Ltd. (As on 31.3.2012)*	*B Ltd. (As on 31.12.2011)*
	₹	*₹*		*₹*	*₹*
Share Capital (Shares of ₹ 10 each)	*10,00,000*	*5,00,000*	*Fixed Assets*	*6,50,000*	*4,05,000*
Reserves and Surplus	*4,50,000*	*2,05,000*	*Investment: 40,000 Shares in B Ltd.*	*8,00,000*	*—*
Secured Loan:					

13% Debentures			*1,000 Debentures*		
(₹ 100 each)	*—*	*3,00,000*	*in B Ltd.*	*1,50,000*	*—*
Current Liabilities:			*Current Assets:*		
Creditors	*3,80,000*	*80,000*	*Stock*	*2,00,000*	*3,50,000*
Other liabilities	*2,00,000*	*40,000*	*Debtors*	*1,50,000*	*2,65,000*
			Cash and Bank	*80,000*	*1,05,000*
	20,30,000	*11,25,000*		*20,30,000*	*11,25,000*

On 5th January 2012, certain stocks of B Ltd. costing ₹ 20,000 were completely destroyed by fire. The insurance company paid 75% of the claim.

On 20th January, 2012, A Ltd. sold goods to B Ltd. costing ₹ 1,50,000 at an invoice price of cost plus 20%.

50% of those goods were resold by B Ltd. to A Ltd. within 31st March, 2012 (these were then sold by A Ltd. to a third party before 31st March, 2012). As on 31st March, 2012, B Ltd. owes ₹ 60,000 to A Ltd. in respect of those goods. Pre-acquisition profits of B Ltd. were ₹ 75,000.Prepare consolidated balance sheet as on 31st March, 2012 after making necessary adjustments in the balance sheet of B Ltd.

Solution

Consolidated Balance Sheet of A Ltd. and its subsidiary B Ltd.
As on 31st March, 2012

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		10,00,000
(b) Reserves and Surplus (W.N.4.)		5,59,000
(2) Minority Interest (W.N 3.)		1,46,000
(3) Non-current liabilities		
(a) Long term borrowings	1	2,00,000
(4) Current Liabilities		
(a) Trade Payables	2	4,60,000
(b) Other current liabilities (₹ 2,00,000 + ₹ 40,000)		2,40,000
Total		26,05,000
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
(i) Tangible assets	3	10,55,000
(ii) Intangible assets	4	3,90,000

(2)	Current assets		
	(a) Inventories	5	6,05,000
	(b) Trade receivables	6	3,55,000
	(c) Cash & Cash equivalents	7	2,00,000
	Total		26,05,000

Notes to Accounts

			₹
1.	Long Term Borrowings		
	Secured loans		
	13% Debentures (₹ 100 each)		2,00,000
2.	Trade Payables		
	A Ltd.	3,80,000	
	B Ltd.(W.N 1)	1,40,000	
		5,20,000	
	Less : Mutual indebtedness	(60,000)	4,60,000
3.	Tangible Assets		
	A Ltd.	6,50,000	
	B Ltd.	4,05,000	10,55,000
4.	Intangible assets		
	Goodwill (W.N 2)		3,90,000
5.	Inventories		
	A Ltd.	2,00,000	
	B Ltd.[WN 1	4,20,000	
		6,20,000	
	Less : Unrealised profit [90,000 X 20/120]	(15,000)	6,05,000
6	Trade Receivables		
	A Ltd.	1,50,000	
	B Ltd.	2,65,000	
		4,15,000	
	Less : Mutual indebtedness	(60,000)	3,55,000
7	Cash & Cash equivalents		
	A Ltd.	80,000	
	B Ltd.[W.N 1	1,20,000	2,00,000

Working Notes:

1. Adjustments to be made in the balance sheet items of B Ltd.:

Assets side	₹
Stocks:	
As given on 31.12.2011	3,50,000
Add : Unsold stock out of goods purchased from A Ltd.	90,000
	4,40,000
Less: Loss of stock by fire	(20,000)
	4,20,000
Cash & Bank balance:	
As given on 31.12.2011	1,05,000
Add: Insurance claim received [20,000 × 75 %]	15,000
	1,20,000
Liabilities side:	
Creditors:	
As given on 31.12.2011	80,000
Add: Owings to A Ltd. on 31.3.2012	60,000
	1,40,000
Reserves and Surplus:	
As given on 31.12.2011	2,05,000
Less: Abnormal Loss on goods destroyed [20,000 – 15,000]	(5,000)
	2,00,000
Add: Profit from sale of goods purchased from A Ltd.	30,000
	2,30,000

2. Goodwill / capital reserve on consolidation :

	₹	₹
Amount paid for 40,000 Shares	8,00,000	
Amount paid for 1,000 Debentures	1,50,000	9,50,000
Less: Nominal value of proportionate share capital	4,00,000	
Nominal value of proportionate 13% debentures	1,00,000	
Share of pre-acquisition profits (80% of ₹ 75,000)	60,000	(5,60,000)
Goodwill		3,90,000

3. Minority Interest: 10,000 / 50,000 shares = 20 %

	₹
Paid up value of 10,000 shares	1,00,000
Add : 20% of Reserves & Surplus of B Ltd. (20% of ₹ 2,30,000)	46,000
	1,46,000

4. Reserves and Surplus of A Ltd.:

Balance as on 31.3.2012	4,50,000
Add : Share of revenue reserves of B Ltd. ([80% of ₹ 1,55,000 (2,30,000 – 75,000)]	1,24,000
	5,74,000
Less: Unrealised profit on stock $\left[\frac{1}{6} \times ₹\ 90,000\right]$	(15,000)
	5,59,000

2.17 Miscellaneous Illustrations

Illustration 14

A Ltd. acquired 1,600 ordinary shares of ₹ 100 each of B Ltd. on 1st July 2011. On December 31, 2011 the summarised Balance Sheets of the two companies were as given below:

Liabilities	*A Ltd.* ₹	*B Ltd.* ₹	*Assets*	*A Ltd.* ₹	*B Ltd.* ₹
Capital (Shares of ₹ 100 each fully paid)	*5,00,000*	*2,00,000*	*Land & Buildings*	*1,50,000*	*1,80,000*
Reserves	*2,40,000*	*1,00,000*	*Plant & Machinery*	*2,40,000*	*1,35,000*
Profit & Loss A/c	*57,200*	*82,000*	*Investment in B Ltd. at cost*	*3,40,000*	*—*
Bank Overdraft	*80,000*	*—*	*Stock*	*1,20,000*	*36,400*
Bills Payable	*—*	*8,400*	*Sundry Debtors*	*44,000*	*40,000*
Creditors	*47,100*	*9,000*	*Bills Receivable*	*15,800*	*—*
	9,24,300	*3,99,400*	*Cash*	*14,500*	*8,000*
				9,24,300	*3,99,400*

The Profit & Loss Account of B Ltd. showed a credit balance of ₹ 30,000 on 1st January, 2011 out of which a dividend of 10% was paid on 1st August; A Ltd. has credited the dividend received to its Profit & Loss Account. The Plant & Machinery which stood at ₹ 1,50,000 on 1st January, 2011 was considered as worth ₹ 1,80,000 on 1st July, 2011; this figure is to be considered while consolidating the Balance Sheets. The rate of depreciation on plant & machinery is 10 %.

Prepare consolidated Balance Sheet as on December 31, 2011.

Solution

Consolidated Balance Sheet of A Ltd. and its subsidiary, B Ltd.
as on 31st December, 2011

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	5,00,000

	(b) Reserves and Surplus	2	3,08,500
	(2) Minority Interest (W.N 5)		83,525
	(3) Current Liabilities		
	(a) Trade Payables	3	64,500
	(b) Short term borrowings	4	80,000
	Total		10,36,525
II.	Assets		
	(1) Non-current assets		
	Fixed assets		
	(i) Tangible assets	5	7,40,625
	(ii) Intangible assets	6	17,200
	(2) Current assets		
	(a) Inventories	7	1,56,400
	(b) Trade receivables	8	99,800
	(c) Cash & Cash equivalents (Cash)	9	22, 500
	Total		10,36, 525

Notes to Accounts

				₹
1.	Share Capital			
	5,000 shares of ₹ 100 each			5,00,000
2.	Reserves and Surplus			
	Reserves		2,40,000	
	Profit & loss(W.N.8)		68,500	3,08,500
3.	Trade Payables			
	Sundry Creditors			
	A Ltd.	47,100		
	B Ltd.	9,000	56,100	
	Bills Payable			
	B Ltd.		8,400	64,500
4.	Short term borrowings			
	Bank overdraft			80,000
5.	Tangible Assets			
	Land and building (1,50,000 + 1,80,000)		3,30,000	
	Plant & Machinery (W.N 7)		4,10,625	7,40,625
6.	Intangible assets			
	Goodwill (W.N 6)			17,200
7.	Inventories			
	A Ltd.		1,20,000	
	B Ltd.		36,400	1,56,400

8	Trade Receivables			
	Sundry debtors			
	A Ltd.	44,000		
	B Ltd.	40,000	84,000	
	Bills receivables		15,800	99,800
9	Cash & Cash equivalents			
	Cash			
	A Ltd.		14,500	
	B Ltd.		8,000	22,500

Share holding Pattern

Total Shares of B Ltd	2,000 shares
Shares held by A Ltd	1,600 shares i.e. 80 %
Minority Shareholding	400 shares i.e. 20 %

Working Notes:

1. The dividend @ 10% on 1,600 shares, ₹ 16,000 received by A Ltd. should have been credited to the investment A/c, being out of pre-acquisition profits. A Ltd., must pass a correcting entry, viz.

Profit & Loss Account	Dr. ₹ 16,000	
To investment		₹ 16,000

2. The Plant & Machinery of B Ltd. would stand in the books at ₹ 1,42,500 on 1st July, 2011, considering only six months' depreciation on ₹ 1,50,000 total depreciation being ₹ 15,000. The value put on the assets being ₹ 1,80,000 there is an appreciation to the extent of ₹ 37,500.

3. *Capital profits of B Ltd.*

	₹	₹
Reserve on 1.1.2011		1,00,000
Profit & Loss Account Balance on 1.1.2011	30,000	
Less: Dividend paid	(20,000)	10,000
Profit for 2011: Total ₹ 82,000 less ₹ 10,000		
i.e. ₹ 72,000; upto 1.7.2011		36,000
Appreciation in value of Plant & Machinery		37,500
		1,83,500
Less : 20% due to outsiders		(36,700)
Holding company's share		1,46,800

4. *Revenue profits of B Ltd.:*

Profit after 1.7.2011 [82,000 – 10,000] x ½	36,000
*Less:*10% depreciation on ₹ 37,500 (increase in value of plant & machinery)for 6 months	(1,875)
	34,125
Less: 1/5 due to outsiders	(6,825)
Share of A Ltd.	27,300

5. *Minority interest:*

Par value of 400 shares	40,000
Add: 1/5 Capital Profits [WN 3]	36,700
1/5 Revenue Profits [WN 4]	6,825
	83,525

6. *Cost of Control:*

Amount paid for 1,600 shares	3,40,000	
Less: Dividend out of pre-acquisition profits	(16,000)	3,24,000
Par value of shares	1,60,000	
Capital Profits –share of A Ltd. [WN 3]	1,46,800	(3,06,800)
Cost of Control or Goodwill		17,200

7. *Value of plant & Machinery:*

A Ltd.		2,40,000
B Ltd.	1,35,000	
Add: Appreciation on 1.7.2011	37,500	
	1,72,500	
Less: Depreciation on ₹ 37,500 for 6 months	(1,875)	1,70,625
		4,10,625

8. *Profit & Loss Account (Consolidated):*

A Ltd. as given	57,200	
Less: Dividend transferred to Investment A/c	(16,000)	41,200
Share of A Ltd. in revenue profits of B Ltd. (WN 4)		27,300
		68,500

Illustration 15

The summarised balance sheets of three companies, A Ltd., B Ltd., C Ltd., as on 31st December, 2011 are given below:

Liabilities:	*A Ltd.* ₹	*B Ltd.* ₹	*C Ltd.* ₹
Share Capital (shares of ₹ 100 each)	*1,50,000*	*1,00,000*	*60,000*
Reserves	*20,000*	*10,000*	*7,500*

Profit & Loss A/c	*50,000*	*30,000*	*25,000*
Sundry Creditors	*20,000*	*25,000*	*15,000*
A Ltd.	*—*	*10,000*	*8,000*
	2,40,000	*1,75,000*	*1,15,500*
Assets	*A Ltd.* ₹	*B Ltd.* ₹	*C Ltd.* ₹
Goodwill	*20,000*	*15,000*	*10,000*
Fixed Assets	*70,000*	*50,000*	*60,000*
Shares in B Ltd. (750 shares)	*90,000*	*—*	*—*
In C Ltd. (100 shares)	*15,000*	*—*	*—*
In C Ltd. (350 shares)	*—*	*52,000*	*—*
Due from: B Ltd.	*12,000*		
C Ltd.	*8,000*		
Current Assets	*25,000*	*58,000*	*45,500*
	2,40,000	*1,75,000*	*1,15,500*

All shares were acquired on 1st July, 2011. On 1st Jan., 2011, the balances were:

	A Ltd.	*B Ltd.*	*C Ltd.*
Reserves	*10,000*	*10,000*	*5,000*
Profit & Loss A/c	*5,000*	*5,000(Dr.)*	*3,000*

Profits during 2011 were earned evenly over the year.

In August, 2011 each company declared and paid an interim dividend of 10% p.a. for six months. A Ltd. and B Ltd., have credited their Profit & Loss Account with the dividends received. During 2011, C Ltd. fabricated a machine costing ₹ 10,000 which it sold to B Ltd. for ₹ 12,000, B Ltd. then sold the machine to A Ltd., for ₹ 13,000, the transactions being completed on 31st December, 2011.

Prepare the consolidated Balance Sheet of the group as on 31st December, 2011.

Solution

Consolidated Balance Sheet of A Ltd. and its Subsidiaries B Ltd. & C Ltd.,
as on 31st December, 2011

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1,50,000
(b) Reserves and Surplus	2	85,402
(2) Minority Interest [W.N (iv)]		59,691
(3) Current Liabilities		
(a) Trade Payables	3	60,000
Total		3,55,093

II.	Assets		
	(1) Non-current assets		
	Fixed assets		
	(i) Tangible assets	4	1,77,000
	(ii) Intangible assets	5	47,593
	(2) Current assets	6	1,30,500
	Total		3,55,093

Notes to Accounts

				₹
1.	Share Capital			
	1,500 shares of ₹ 100 each			1,50,000
2.	Reserves and Surplus			
	Reserves of A Ltd	20,000		
	Add : Share in C ltd [WN (i)]	208		
	Add : Share in B ltd [WN (ii)]	548	20,756	
	Profit & loss[W.N.(v)]		64,646	85,402
3.	Trade Payables			
	Sundry Creditors			
	A Ltd		20,000	
	B Ltd.		25,000	
	C Ltd		15,000	60,000
4.	Tangible Assets			
	Given in balance sheet		1,80,000	
	Less : Unrealised profit		(3,000)	1,77,000
5.	Intangible assets			
	Given in balance sheet		45,000	
	Add : Goodwill on consolidation (W.N iii)		2,593	47,593
6.	Current assets			
	A Ltd.		25,000	
	B Ltd.		58,000	
	C Ltd.		45,500	
			1,28,500	
	Add : Cash in Transit *		2,000	1,30,500

* A Ltd shows ₹ 12,000 receivable from B Ltd. whereas B Ltd. shows ₹ 10,000 payable to A Ltd. Hence, ₹ 2,000 has been treated as cash in transit

Working notes:

Shareholding Pattern

	B Ltd.	C Ltd.
Total Shares	1,000	600
Held By A Ltd.	750 i.e. 3/4th	100 i.e. 1/6th
Held by B Ltd.	NA	350 i.e. 7/12th
Outsiders	250 i.e. 1/4th	150 i.e. 1/4th

(i) Analysis of Profits of C Ltd.

	₹	*Capital Profit* ₹	*Revenue Reserve* ₹	*Revenue Profit* ₹
General Reserve on 1.1.2011		5,000		
Profit & Loss A/c on 1.1.2011		3,000		
Increase in Reserve [7,500 – 5,000]		1,250	1,250	
Profit for the year	12,500 [25,000 x ½]			
Less: Interim Dividend	(3,000)	9,500		12,500 [25,000 x ½]
		18,750	1,250	12,500
Less: Minority Interest 3/12		4,687	312	3,125
Brought Forward		14,063	938	9,375
Share of A Ltd. 2/12		3,125	208	2,083
Share of B Ltd. 7/12		10,938	730	7,292

(ii) Analysis of Profits of B Ltd.

		₹	₹	₹	₹
Reserve on 1.1.2011			10,000		
Profit & Loss on 1.1.2011			(5,000)		
Profit for the year [30,000+5,000+5,000]	40,000				
Less: Interim dividend of C Ltd.[3,000 X 7/12]	(1,750)				
	38,250	19,125 [38,250 × ½]			19,125 [38,250 × ½]
Less: Interim Div.		(5,000)	14,125		
Share in C Ltd.				730	7,292
			19,125	730	26,417
Minority Interest ¼			(4,781)	182	6,604
Share of A Ltd. [3/4]			14,344	548	19,813

(iii) Cost of Control / Capital Reserve

	₹	₹
Investments in B Ltd.		
(90,000 – 3,750)	86,250	
Investments in C Ltd.		
(15,000 – 500)	14,500	
(52,000 – 1,750)	50,250	1,51,000
Less: Paid up Value of Investments		
in B Ltd.	75,000	
in C Ltd.	45,000	
Capital Profit in B Ltd.[WN (ii)]	14,344	
Capital Profit in C Ltd.[WN (i)]	14,063	(1,48,407)
		2,593

(iv) Minority Interest

	B Ltd. ₹	C Ltd. ₹
Share Capital	25,000	15,000
Capital Profits [WN (i) & (ii)]	4,781	4,687
Revenue Reserve[WN (i) & (ii)]	182	312
Revenue Profits[WN (i) & (ii)]	6,604	3,125
	36,567	23,124

(v) Profit and Loss Account – A Ltd.

	₹
Balance	50,000
Less: Dividend credited to Investment (3,750+500)	(4,250)
	45,750
Share in B Ltd.	19,813
Share in C Ltd.	2,083
	67,646
Less: Intergroup Profit on Plant [13,000-10,000]	(3,000)
	64,646

Ilustration 16

The following information was extracted from the books of A Limited group as on 31st December, 2011:

	A Ltd. ₹	B Ltd. ₹	C Ltd. ₹
Profit and Loss Account:			
Balance on 31st December, 2009 after provision for dividends of 10% in respect of calendar year 2009 but excluding dividend received	50,000	36,000	26,000
Net trading profit earned in 2010	60,000	42,000	28,000
	1,10,000	78,000	54,000
Less: Dividends of 10 per cent (received in 2011) in respect of calendar year 2010	(40,000)	(30,000)	(20,000)
	70,000	48,000	34,000
Net trading profit earned in 2011 (before taking into account proposed dividends of 10 per cent in respect of calendar year 2011)	50,000	50,000	30,000
	1,20,000	98,000	64,000
Dividends Received:			
From B Limited in 2010	20,000		
From B Limited in 2011	25,000		
From C Limited in 2011		15,000	
Share Capital Authorised and Fully paid - Equity Shares of Re 1 each	4,00,000	3,00,000	2,00,000
Sundry Creditors	20,000	5,000	17,000
	5,85,000	4,18,000	2,81,000
Fixed Assets at cost less Depreciation	2,10,000	1,88,000	2,61,000
Current Assets	60,000	30,000	20,000
Investment at cost:			
2,00,000 Equity Shares in B Ltd. bought on December 31, 2009	2,50,000		
50,000 Equity Shares in B Ltd. bought on December 31, 2010	65,000		
1,50,000 Equity Shares in C Ltd. bought on December 31, 2010		2,00,000	
	5,85,000	4,18,000	2,81,000

All the companies pay dividends of 10 per cent on Paid-up share capital in March following the

end of the accounting year. The receiving companies enter the dividends in their books when dividends are received. You are required to prepare:

(a) Consolidated Balance Sheet as on 31st December, 2011.

(b) Statements showing the composition of :

(i) Consolidated Profit and Loss Account.

(ii) Minority Interest, and

(iii) Cost of Control, Goodwill. Ignore taxation.

Solution

(a) Consolidated Balance Sheet of A Ltd., and subsidiaries B Ltd. and C Ltd.

as on 31st December, 2011

Particulars	*Note No.*	*(₹)*
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	4,00,000
(b) Reserves and Surplus	2	1,68,417
(2) Minority Interest [Refer (ii)]		1,26,083
(3) Current Liabilities		
(a) Trade payables	3	42,000
(b) Other Current liabilities	4	50,000
Total		7,86,500
II. Assets		
(1) Non-current assets		
Fixed assets		
i. Tangible assets	5	6,59,000
ii. Intangible assets	6	17,500
(2) Current assets		1,10,000
Total		7,86,500

Notes to Accounts

		(₹)	*(₹)*
1.	Share Capital		
	4,00,000 Equity shares of ₹1 each fully paid		4,00,000
2.	Reserves and surplus		
	Profit and Loss Account {b(i)}		1,68,417

3.	Trade Payables			
	Sundry Creditors			42,000
4.	Other Current Liabilities			
	Proposed Dividend:			
	A Ltd.	40,000		
	Minority Interest	10,000*		50,000
5.	Tangible Assets			
	Fixed Assets less depreciation			6,59,000
6.	Intangible assets			
	Goodwill [Refer (iii)]			17,500

(b) (i) Consolidated Profit and Loss Account of A Ltd. and its subsidiaries, B Ltd. and C Ltd., for the year ended on 31st December, 2011.

	₹	₹
Profit and Loss account balance of last year		
A Ltd.	1,10,000	
B Ltd.	78,000	
C Ltd.	54,000	2,42,000
Add: Dividend received in 2010 (for 2009)*		20,000
Add: Profit for the year:		
A Ltd.	50,000	
B Ltd.	50,000	
C Ltd.	30,000	1,30,000
	`	`
Less: Dividend for 2010*		
A Ltd.	40,000	
B Ltd. (Net) [30,000-25,000]	5,000	
C Ltd. (Net) [20,000-150,000]	5,000	50,000
Minority Interest:		
B Ltd.	20,083	
C Ltd.	16,000	36,083
Capital Receipts**		40,000
Capital Profits		
B Ltd.	32,000	
C Ltd.	25,500	57,500
Proposed Dividend for 2011		40,000
Profit transferred to Consolidated P&L A/c		1,68,417

						Net Amount (₹) (after eliminating intragroup dividend)
For	*Dividend Paid By*	*₹*	*Dividend Received By*	*₹*	*Dividend Paid ₹*	*Dividend Received ₹*
2009			A Ltd. (from B Ltd.)	20,000		20,000 (By A Ltd.)
2010	A Ltd.	40,000			40,000 (By A Ltd.)	
2010	B Ltd.	30,000	A Ltd. (from B Ltd.)	25,000	5,000 (By B Ltd.)	
2010	C Ltd.	20,000	B Ltd. (from C Ltd.)	15,000	5,000 (By C Ltd.)	
				50,000		20,000

* Alternatively, this can be shown as a part of Minority Interest. However, the better disclosure is to show such proposed dividend separately because a distinction is always necessary between immediate liability of dividend payment and an artificial liability towards minorities.

** To be credited to Investments in subsidiaries ₹ 25,000 from B Ltd. [₹ 20,000 dividend received in 2010 (for 2009) + ₹ 5,000 dividend received in 2011 (for 2010)] and ₹ 15,000 from C Ltd.

(ii) Minority Interest :

B Ltd = 50,000 shares / 3,00,000 shares = 1/6th

C Ltd = 50,000 shares / 2,00,000 shares = 1/4th

	B Ltd. ₹	C Ltd. ₹
Share Capital	50,000	50,000
Capital Profits	6,000	8,500
Revenue Profits	14,083	7,500
	70,083	66,000
Total		1,36,083
Less: Shown as proposed dividend		(10,000)
		1,26,083

(iii) Cost of control/Goodwill

	₹	₹
Cost of Investment in B Ltd. – 2,00,000 (Shares ₹ 2,50,000 less Dividend, ₹ 20,000 received in 2010)		2,30,000
Cost of Investments in B Ltd. – 50,000 (Shares less dividend received in 2011)		60,000
Cost of Investment in C Ltd. held by B Ltd. (less dividend received in 2011)		1,85,000
		4,75,000

Paid-up value of Shares in B Ltd.	2,50,000	
Paid-up value of Shares in C Ltd.	1,50,000	
Capital Profits in B Ltd.	32,000	
Capital Profits in C Ltd.	25,500	4,57,500
Goodwill		17,500

Working Note:

Analysis of Profits

	Capital Profit ₹	*Revenue Profit* ₹
C Ltd.		
Balance on 31st Dec. 2010, after dividend	34,000	
Profit for the year ending on 31st Dec., 2011 before proposed dividend for 2011		30,000
	34,000	30,000
Minority Interest (1/4)	8,500	7,500
	25,500	22,500
B Ltd.		
Balance on 31st Dec., 2009	36,000	—
Profit in 2010 after dividend for 2010	—	12,000
Profit for 2011 (before dividend),	—	50,000
Revenue Profit from C Ltd.	—	22,500
	36,000	84,500
Minority Interest (1/6)	6,000	14,083
	30,000	70,417
1/6 of retained profit for 2010 treated as Capital profit on purchase of 50,000 shares on 31st Dec., 2010	+ 2,000	(2,000)
	32,000	68,417

Illustration 17

The summarised Balance Sheets of the following three companies are given below:

	As on 31st March, 2012 (₹ in lakhs)		
	Eagle Ltd.	*Garuda Ltd.*	*Bird Ltd.*
Liabilities			
Equity Shares (₹ 10 each, fully paid up)	*60*	*48*	*40*

7½% Cumulative Preference Shares			
(₹ 100 each fully paid up)	*15*	*12*	*10*
Capital Reserve on Revaluation of Land, Buildings and Machinery	*120*		
General Reserve	*25*	*15*	*10*
8% 2,500 Mortgage Debenture Bonds of ₹ 1,000 each	*25*		
Secured Loans and Advances from Banks	*153*	*71*	*52*
Unsecured Loans:			
(i) From Garuda Ltd.	*—*	*—*	*12*
(ii) From Bird Ltd.	*15*	*—*	*—*
(iii) Deposits from Public	*18*	*12*	*3*
Current Liabilities and Provisions:			
(i) Inter-Company Balances	*9*	*—*	*—*
(ii) Other liabilities and provisions	*314*	*125*	*72*
Total	*754*	*283*	*199*
Assets			
Fixed Assets (Net)	*272*	*104*	*42*
Investments (at Cost)			
2,50,000 Equity Shares of Garuda Ltd.	*25*		
80,000 Equity Shares of Bird Ltd.	*8*		
1,60,000 Equity Shares of Bird Ltd.		*20*	
10,000 Cumulative Preference Shares of Eagle Ltd.			*10*
1,500 Mortgage Debentures of Eagle Ltd.			*14*
Current Assets	*353*	*123*	*112*
Profit and Loss Account	*96*	*36*	*21*
Total	*754*	*283*	*199*

(i) Eagle Ltd. subscribed for the shares of Garuda Ltd. and Bird Ltd. at par at the time of first issue of shares by the latter companies.

(ii) Garuda Ltd., subscribed for 80,000 shares of Bird Ltd. at par at the time of first issue and latter acquired by purchase in the market 80,000 shares of Bird Ltd. at ₹ 15 each when Reserves and Surplus of Bird Ltd. stood at ₹ 5 lakhs.

(iii) Current Assets of Garuda Ltd. and Bird Ltd. included ₹ 4 lakhs and ₹ 6 lakhs respectively being the current accounts balance against Eagle Ltd. These accounts remained unreconciled.

(iv) Preference dividends were in arrears for:-

8 years in the case of Eagle Ltd. and 4 years in the case of other two companies.

Prepare the Consolidated Balance Sheet.

Solution

Consolidated Balance Sheet of Eagle Ltd.,
and its subsidiaries Garuda Ltd., and Bird Ltd.
as on 31st March, 2012

Particulars	Note No.	(₹ in lakhs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	65.00
(b) Reserves and Surplus	2	31.94
(2) Minority Interest	3	44.06
(3) Non-current liabilities		
Long term borrowings	4	319.00
(4) Current Liabilities		
Other current liabilities (314+125+72)		511.00
Total		971.00
II. Assets		
(1) Non-current assets		
Fixed assets		
(i) Tangible assets(272+104+42)		418.00
(ii) Intangible assets	5	1.00
(2) Current assets [353+123+112-15-9-12]		552.00
Total		971.00

Notes to Accounts

			₹
1.	Share Capital		
	6,00,000 Equity shares of ₹ 10 each fully paid	60.00	
	5,000 [15,000 – 10,000], 7-1/2% preference share of ₹ 100 each	5.00	65.00
2.	Reserves and Surplus		
	Capital Reserve (Given in balance sheet)	120.00	
	Less : Profit & Loss Accounts(W.N. iii)	(88.06)	31.94
3.	Minority Interest		
	Garuda	23.00	
	Bird	16.00	
		39.00	
	Loss in subsidiaries		
	Garuda [WN (ii)]	(12.94)	
	Bird [WN (i)](6-2)	(4.00)	
		(16.94)	
		22.06	
	Preference share [12 +10]	22.00	44.06

4.	Long term borrowings		
	Secured		
	8% Mortgage Debentures [25 – 15]	10.00	
	Loan & Advances from banks(153+71+52)	276.00	286.00
	Unsecured		
	Public Deposits(18+12+3)	33.00	33.00
			319.00
5.	Intangible assets		
	Goodwill (W.N iv)		1.00

Note: Preference Dividends were in arrears for eight years in Eagle Ltd. and four years in subsidiaries.

Working Notes:

	Garuda	Bird
Total Shares	4,80,000	4,00,000
Held by Eagle Ltd.	2,50,000 i.e.25/48th	80,000 i.e 1/5th
Held By Garuda Ltd.	NA	1,60,000 i.e. 2/5th
Minority Interest	2,30,000 i.e. 23/48th	1,60,000 i.e. 2/5th

Garuda Ltd. is the subsidiary of Eagle Ltd. since the issue of shares by Garuda Ltd.

Bird Ltd. is subsidiary of Garuda Ltd. after the acquisition of 80,000 shares from the market. Thereafter, both Garuda and Bird Ltd. become the subsidiary of Eagle Ltd. Hence, the capital profit will be ₹ 5 lakhs

(i) Analysis of Profits of Bird Ltd.

		(₹ in lakhs)
Loss after adjusting Reserve and *Profit on Debenture in Eagle Ltd.*		10
	*Capital Profit**	*Revenue Loss*
Share of Eagle Ltd. [1/5th]	1	3
Share of Garuda Ltd.[2/5th]	2	6
Share of Minority [2/5th]	2	6
	5	15

(ii) Analysis of Garuda Ltd.

Loss, *less* Reserve [36-15]	21
Add : Loss in Bird Ltd.	6
	27
Share of Eagle Ltd. 25/48	14.06
Share of Minority [23/48]	12.94

(iii) Profit & Loss A/c Eagle Ltd.

Loss, *less* Reserve [96-25]		71.00
Loss in Garuda Ltd.	14.06	

Loss in Bird Ltd.	3.00	17.06
		88.06

(iv) Cost of Control

Cost of Investments in Garuda Ltd.		25
Cost of Investments in Bird Ltd.[8 + 20]		28
		53
Paid up value of shares in:		
Garuda Ltd.	25	
Bird Ltd.[8+16]	24	
Capital profit in Bird Ltd.[1+2]	3	52
		1

Note: In accordance with para 15 of AS 21, the consolidated financial statements have been presented from the date on which holding subsidiary relationship comes in existence.

Illustration 18

On 1st January, 2011, Investments Ltd. a new company, raised its first Capital of ₹ 3,00,000 from the issue of 30,000 shares of ₹ 10 each at par, and on that date acquired the following shareholdings:

A Ltd. – 3,000 shares of ₹ 10 each fully paid for ₹ 35,000
B Ltd. – 10,000 shares of ₹ 10 each fully paid for ₹ 72,000
C Ltd. – 8,000 shares of ₹ 10 each fully paid for ₹ 92,000.

Apart from these transactions and those detailed below, investments Ltd. neither paid not received other monies during 2011.

The following are the summarised Balance Sheets of the Subsidiary Companies on 31st December, 2011:

	A Ltd. ₹	B Ltd. ₹	C Ltd. ₹
Goodwill	4,000	—	15,000
Freehold Property	18,000	41,000	50,000
Plant	16,000	30,000	12,000
Stock	11,000	32,000	21,000
Debtors	4,000	8,000	17,000
Cash at Bank	1,000	2,000	11,500
Profit and Loss Account	—	18,000	—
	54,000	1,31,000	1,26,500
Share Capital	40,000	1,20,000	1,00,000
Reserves (as on 1.1.2011)	3,000	—	7,500
Profit and Loss Account	6,000	—	15,000
Creditors	5,000	11,000	4,000
	54,000	1,31,000	1,26,500

Other relevant information:

(1) The freehold property of C Ltd. is to be revalued at ₹ 65,000 as on 1.1.2011.

(2) Additional depreciation for the year 2011 of ₹ 3,000 on the plant of B Ltd is to be provided.

(3) The stock of A Ltd. as on 31st December, 2011 has been undervalued by ₹ 2,000 and is to be adjusted.

(4) As on 31st December, 2011 Investments Ltd. owed A Ltd. ₹ 3,500 and is owed ₹ 6,000 by B Ltd. C Ltd. is owed ₹ 1,000 by A Ltd. and ₹ 2,000 by B Ltd.

(5) The balances on Profit and Loss Accounts as on 31st December, 2010 were: A Ltd. ₹ 2,000 (credit); B Ltd ₹ 12,000 (debit); and C Ltd. ₹ 4,000 (credit).
The credit balances of A Ltd. and C Ltd. were wholly distributed as dividends in March, 2011.

(6) During 2011, A Ltd. and C Ltd. declared and paid interim dividends of 8% and 10% respectively.

You are required to prepare the Consolidated Balance Sheet of Investments Ltd. and its subsidiary companies as on 31st December, 2011, ignore taxation.

Solution

Consolidated Balance Sheet of Investments Ltd. and its subsidiaries A Ltd., B Ltd. and C Ltd. as on 31st December, 2011

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	3,00,000
(b) Reserves and Surplus	2	46,850
(2) Minority Interest (W.N vi)		56,750
(3) Current Liabilities		
(a) Trade Payables	3	11,000
Total		4,14,600
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	4	1,79,000
Intangible assets	5	19,000
(2) Current assets		
(a) Inventories (W.N viii)		66,000
(b) Trade receivables	6	22,500
(c) Cash & Cash equivalents(W.N vii)		1,28,100
Total		4,14,600

Notes to Accounts

			₹
1.	Share Capital		
	30,000 shares of ₹ 10 each		3,00,000

2.	Reserves and Surplus		
	Capital Reserves (W.N. v)	25,950	
	Profit & loss (W.N.iv)	20,900	46,850
3.	Trade Payables		
	Sundry Creditors [5+11+4+3.5]	23,500	
	Less : Inter Co.[3.5+6+1+2]	(12,500)	11,000
4.	Tangible Assets		
	Freehold property (W.N. viii)	1,24,000	
	Plant (W.N viii)	55,000	1,79,000
5.	Intangible assets		
	Goodwill (Given in balance sheet)		19,000
6.	Trade Receivables (W.N. viii)	35,000	
	Less : Inter Co. debts	(12,500)	22,500

Shareholding Pattern

	A Ltd.	B Ltd.	C Ltd.
No. of shares	4,000	12,000	10,000
Held by Investment	3,000 i.e. 3/4th	10,000 i.e. 5/6th	8,000 i.e. 4/5th
Minority Interest	1/4th	1/6th	1/5th

Working Notes:

Analysis of Profits:

		Capital Profit ₹	*Revenue Profit* ₹
(i)	C Ltd.		
	Profit & Loss Account on 1.1.2011 less Div. (4000 – 4000)	—	
	Reserve on 1st Jan., 2011	7,500	
	Appreciation in the value of Freehold Property [65,000-50,000]	15,000	
	Profit for the year after interim dividend		15,000
	Total	22,500	15,000
	Minority Interest 20%	4,500	3,000
	Share of Investments Ltd.	18,000	12,000
(ii)	B Ltd.		
	Loss on the date of acquisition	–12,000	
	Loss suffered during the year after additional dep of 3,000 (18,000+3,000– 12,000)		–9,000
		–12,000	–9,000
	Minority Interest (1/6)	2,000	1,500
	Share of Investment Ltd. (5/6)	–10,000	–7,500

(iii)	A Ltd.		
	Reserve on 1.1.2011	3,000	
	Profit on 1.1.2011 *less* Dividend (2,000 – 2,000)	—	—
	Profit earned during the year (after interim dividend ₹ 3,200) and stock adjustment [6,000 + 2,000]		8,000
		3,000	8,000
	Minority Interest (1/4)	750	2,000
		2,250	6,000
(iv)	Profit & Loss of Investment Ltd.		
	Revenue Profit of C Ltd.[WN (i)]	₹ 12,000	
	Revenue Loss of B Ltd. [WN (ii)]	– 7,500	
	Revenue Profit of A Ltd. [WN (iii)]	₹ 6,000	
			10,500
	Add: Interim dividend received [30,000 X 8 % +80,000 × 10 %]		10,400
			20,900
(v)	Cost of Control / Capital Reserve		
	Cost of Investments in A Ltd. *less* Dividend (35,000 – 1,500)		33,500
	Cost of Investments in B Ltd.		72,000
	Cost of Investments in C Ltd. *less* Dividend (92,000 – 3,200)		88,800
			1,94,300
	Paid up value of Shares held in A Ltd.	30,000	
	Paid up value of Shares held in B Ltd.	1,00,000	
	Paid up value of Shares held in C Ltd.	80,000	
	Capital Profits in A Ltd.	2,250	
	Capital Loss in B Ltd.	–10,000	
	Capital Profits in C Ltd.	18,000	2,20,250
	Capital Reserve		25,950

(vi) Minority Interest

	A Ltd. ₹	B Ltd. ₹	C Ltd. ₹
Share Capital	10,000	20,000	20,000
Capital Profits/(Loss)	750	–2,000	4,500
Revenue Profits	2,000	–1,500	3,000
	12,750	16,500	27,500
			56,750

(vii) Bank A/c - Investments Ltd.

	₹		₹
To Share Capital	3,00,000	By Investments in A Ltd.	35,000
To Investments in A Ltd.[Dividend]	1,500	By Investments in B Ltd.	72,000
To Investments in C Ltd.[Dividend]	3,200	By Investments in C Ltd.	92,000
To Dividends-A Ltd.[Dividend]	2,400	By B Ltd. (indebtedness)	6,000
C Ltd.[Dividend]	8,000	By Balance c/d	1,13,600
To A Ltd.	3,500		
	3,18,600		3,18,600

(viii) Sundry Assets

		Freehold Property ₹	*Plant* ₹	*Stock* ₹	*Debtors* ₹	*Cash at Bank* ₹
(a)	Investments Ltd.	—	—	—	6,000	1,13,600
(b)	A Ltd.	18,000	16,000	13,000	4,000	1,000
(c)	B Ltd	41,000	27,000	32,000	8,000	2,000
(d)	C Ltd.	65,000	12,000	21,000	17,000	11,500
		1,24,000	55,000	66,000	35,000	1,28,100
	Less : Inter Co. debts				(12,500)	
					22,500	

Illustration 19

The following condensed balance sheets of H Ltd. and S Ltd. were prepared as on 31st December, 2011:

Assets	*H Ltd.* ₹	*S Ltd.* ₹
Goodwill	*1,12,000*	*40,000*
Plant & Machinery	*95,000*	*50,400*
Furniture	*7,000*	*4,600*
9,000 ordinary shares in S Ltd.	*1,20,000*	—
2,000 ordinary shares in H Ltd.	—	*24,000*
Stock-in-trade	*48,000*	*1,14,000*
Sundry debtors	*70,000*	*45,000*
Cash at Bank	*17,000*	*13,000*
	4,69,000	*2,91,000*
Liabilities		
Share Capital		
Ordinary shares of 10 each	*1,80,000*	*1,00,000*
7½% Pref shares of ₹ 10 each	*1,50,000*	*80,000*
Premium on ordinary shares	*36,000*	—
Reserves	*26,000*	*30,000*
Sundry Creditors	*17,000*	*61,000*
Profit & Loss Account	*60,000*	*20,000*
	4,69,000	*2,91,000*

Sundry creditors of H Ltd. include ₹ 15,000 due to S Ltd. for goods supplied since the acquisition of the shares. These goods are charged at 10% above cost. The stock of H Ltd. include goods costing ₹ 33,000 purchased from S Ltd.

H Ltd. acquired the shares of S Ltd. on 1st July, 2011. As at the date of last preceding balance sheet of S Ltd., viz., 31st Dec., 2010; the plant and machinery stood in the booksat ₹ 56,000, the reserve at ₹ 30,000 and the profit and loss account at ₹ 8,000. The plant was revalued

by H Ltd. on the date of acquisition of the share of S Ltd. at ₹ 60,000 but no adjustments were made in the books of S Ltd. On 31st Dec., 2010, the debit balance of profit and, loss account was ₹ 22,750 in the books of H Ltd.

Both the companies have provided depreciation on all their fixed assets at 10% per annum. You are required to prepare a consolidated balance sheet on 31st Dec., 2011 and supporting schedule for computation.

Solution

Consolidated Balance Sheet or H Ltd., and its subsidiary S Ltd.,
as on 31st December, 2011

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	3,10,000
(b) Reserves and Surplus	2	1,01,116
(2) Minority Interest	3	1,02,545
(3) Current Liabilities		
(a) Trade Payables	4	63,000
(b) Other current liabilities (Pref. dividend of H ltd.)		11,250
Total		5,87,911
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	5	1,63,600
Intangible assets	6	1,35,311
(2) Current assets		
(a) Inventories ₹ (48,000+1,14,000-3,000)		1,59,000
(b) Trade receivables ₹ (70,000+45,000-15000)		1,00,000
(c) Cash & Cash equivalents₹ (17,000+13,000)		30,000
Total		5,87,911

Notes to Accounts

			₹
1.	Share Capital		
	18,000 equity shares of ₹ 10 each	1,80,000	
	Less : Held by S Ltd.	(20,000)	
		1,60,000	
	15,000 pref. shares of ₹ 10 each fully paid	1,50,000	3,10,000
2.	Reserves and Surplus		
	Reserve (W.N. iv)	17,479	

	Profit & Loss(W.N v)		50,637		
	Less : Stock Reserve		(3,000)	47,637	
	Securities Premium			36,000	1,01,116
3.	Minority Interest				
	Preference shares			80,000	
	Dividend			6,000	
	Equity shares			10,000	
	Capital profit(W.N.ii)			5,632	
	Revenue profit(W.N v)			913	1,02,545
4.	Trade Payables				
	Sundry Creditors			78,000	
	Less : Inter Co.			(15,000)	63,000
5.	Tangible Assets				
	Plant & Machinery				
	H Ltd.	95,000			
	S Ltd. ₹ (50,400+6,800-200)	57,000		1,52,000	
	Furniture ₹ (7,000+,4,600)			11,600	1,63,600
6.	Intangible assets				
	Goodwill (Given in balance sheet)			1,52,000	
	Add: On consolidation of S ltd. in H ltd.(W.N. vi)			4,000	
				1,56,000	
	Less : Capital Reserve (W.N vi)			(20,689)	1,35,311

Working Notes:

(i) (a) Analysis of profits of S Ltd. (Pre-allocation)

	Capital Profit ₹	*Revenue Profit* ₹
Reserves	30,000	
Profit and Loss Account 1.1.2011	8,000	
Profit for the year after Pref. Div. ₹ (12,000 – 6,000)	3,000	3,000
Profit on Revaluation ₹ (60,000 – 53,200)	6,800	
Additional Depreciation [3,000-2,800]		(200)
	47,800	2,800

(b) Analysis of Profits of H Ltd.

	Capital Profit ₹	*Revenue Profit* ₹
Reserves	13,000	13,000
Profit and Loss Account on 1.1.2011	(22,750)	
Profit for the year after preference dividend ₹ (82,750 – 11,250 =71,500)	35,750	35,750
	26,000	48,750

(ii) Capital profits of H Ltd. & S Ltd. (post allocation)

Suppose capital profits of H Ltd. = *a*
and capital profits of S Ltd. = *b*

Total Capital profits of H Ltd. $= 26,000 + \frac{9}{10} b$

Total Capital profits of S Ltd. $= 47,800 + \frac{1}{9} a$

$a = 26,000 + \frac{9}{10}\left[47,800 + \frac{1}{9}a\right]$

$a = 76,689$

$b = 47,800 + \frac{1}{9}(76,689)$

$b = 56,321$

	₹
Minority Interest in Capital profits of S Ltd.	5,632
Share of holding Co. H Ltd.	50,689
	56,321

(iii) Revenue profits of H Ltd. and S Ltd. (post allocation)

Assume revenue profits of H Ltd. = *x*
and revenue profits of S Ltd. = *y*

Total Revenue profits of H Ltd. $= 48,750 + \frac{9}{10} y$

Total Revenue profits of S Ltd. $= 2,800 + \frac{1}{9} x$

or $x = 48,750 + \frac{9}{10}(2,800 + \frac{1}{9}x)$

or $\frac{81}{90} x = 51,270$

or $x = 56,967$

$y = 2,800 + \frac{1}{9}(56,967)$

$y = 9,130$

		H Ltd. ₹	S Ltd. ₹
(iv)	Capital Profits		
	As per Working Note 1	26,000	47,800
	Adjustment as per equation	(8,521)	8,521
		17,479	56,321
	Minority Interest 10%		5,632
	Share of H Ltd.		50,689
(v)	Revenue Profits		
	(60,000 – 11,250 Pref. Dividend)	48,750	2,800
	Adjustment	(6,330)	+6,330
		42,420	9,130
	Minority interest	8,217	913
	Share of H Ltd.	50,637	8,217
(vi)	Cost of Control		
	H Ltd. in S Ltd.		
	Cost of Investments		1,20,000
	Paid up value	90,000	
	Capital Profits	50,689	1,40,689
	Capital Reserve		20,689
	Cost of Investments		24,000
	Paid up value		20,000
	Goodwill		4,000

Illustration 20

Able Ltd. made an offer to acquire all the shares of Baker Ltd. at a price of ₹ 25 per share, to be satisfied by the allotment of five shares in Able Ltd. for every four shares in Baker Ltd.

By the date of expiration of the offer, which was on 1st January, 2012, share-holders owning 75% of the shares in Baker Ltd. accepted the offer and the acquisition was effective from that date.

The accounting date of Baker Ltd. was on 31st March in each year, but to conform to Able Ltd., accounts were prepared to 30th June, 2012, covering the fifteen months to the date.

The draft summarised accounts of the companies on 30th June, 2012 which do not include any entries regarding the acquisition of shares in Baker Ltd., were as follows:

Balance Sheet as on 30th June, 2012

Equity and Liabilities *Shareholders' funds*	₹	*Able Ltd.* ₹	₹	*Baker Ltd.* ₹
Share Capital –				
Equity shares of ₹ 10 each				
Authorised :		*3,00,000*		*75,000*
Issued & fully paid:		*1,50,000*		*60,000*

Reserves & Surplus:				
General Reserve	*55,000*			
Surplus Profit & Loss Account	*62,000*	*1,17,000*		*20,000*
Creditors		*27,000*		*7,000*
Provision for taxation		*33,000*		*6,000*
		3,27,000		*93,000*
Assets				
Non-current assets				
Tangible assets				
Freehold property, at cost		*2,00,000*		*38,000*
Plant & Machinery at cost	*50,000*		*12,000*	
Less: Depreciation	*18,000*	*32,000*	*3,000*	*9,000*
Quoted Investment at Cost		*7,000*		*—*
Current assets				
Stock at Cost		*32,000*		*21,000*
Debtors		*41,000*		*17,000*
Balance at Bank		*15,000*		*8,000*
		3,27,000		*93,000*

Draft Profit & Loss Account for the period ended on 30th June, 2012

	Able Ltd. *One Year* *₹*	*Baker Ltd.* *15 months* *₹*
Balance brought forward	*14,000*	*12,000*
Profit for the period	*80,000*	*18,000*
	94,000	*30,000*
Taxation for the period	*32,000*	*6,000*
Interim Dividend paid, 30th Nov., 2011	*—*	*4,000*
Balance carried forward	*62,000*	*20,000*
	94,000	*30,000*

The Directors of Able Ltd. recommended a final dividend of 20% to the shareholders on register as on 30th June, 2012. The Directors of Baker Ltd., proposed a final dividend of 12½% payable on 30th September, 2012.

You are required to prepare the consolidated Balance Sheet of Able Ltd. and Baker Ltd. on 30th June, 2012.

Solution

Consolidated Balance Sheet of Able Ltd. and its subsidiary Baker Ltd.
as on 30th June, 2012

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	2,06,250

	(b) Reserves and Surplus	2	1,63,725
	(2) Minority Interest(W.N iii)		18,125
	(3) Current Liabilities		
	(a) Trade Payables (27,000+7,000)		34,000
	(b) Short term provisions	3	39,000
	(b) Other current liabilities	4	43,125
	Total		5,04,225
II.	Assets		
	(1) Non-current assets		
	(a) Fixed assets		
	Tangible assets	5	2,79,000
	Intangible assets	6	84,225
	(b) Non current investment		7,000
	(2) Current assets		
	(a) Inventories ₹ (32,000+21,000)		53,000
	(b) Trade Receivables ₹ (41,000+17,000)		58,000
	(c) Cash & Cash equivalents ₹ (15,000+8,000)		23,000
	Total		5,04,225

Notes to Accounts

			₹
1.	Share Capital		
	20,625 (15,000 + 5,625) equity shares of ₹ 10 each		2,06,250
2.	Reserves and Surplus		
	General Reserve (Given in balance sheet)	55,000	
	Profit & Loss [W.N (vi)]	24,350	
	Securities Premium	84,375	1,63,725
3.	Short term provisions		
	Provision for taxation		39,000
4.	Other current liabilities		
	Proposed Dividend		
	Minority Interest	1,875	
	Own Shareholders	41,250	43,125
5.	Tangible Assets		
	Plant & Machinery ₹ (32,000 + 9,000)	41,000	
	Freehold property ₹ (2,00,000 + 38,000)	2,38,000	2,79,000
6.	Intangible assets		
	Goodwill (W.N ii)		84,225

Working Notes:

		₹	₹
(i)	*Number of shares to be issued :*		
	75% of shares of Bakers Ltd.	4,500	
	No. of shares of Able Ltd. 4,500 × 5/4	5,625	
	Value of 5,625 Shares @₹ 25		1,40,625
	Face value of 5,625 Shares @ ₹ 10		56,250
	Securities Premium		84,375
(ii)	*Cost of Control :*		
	Cost of Shares in Baker Ltd.		
	Share Capital	56,250	
	Share Premium	84,375	1,40,625
	Less: Face value of shares acquired	45,000	
	Pre-acquisition profits	11,400	(56,400)
	Goodwill on consolidation		84,225
(iii)	*Minority Interest:*		
	Share Capital A/c, 1/4		15,000
	Profit & Loss A/c, 1/4		5,000
			20,000
	Less: Proposed Dividend, 12½% on ₹ 15,000 (shown separately)		(1,875)
			18,125
(iv)	*Pre-acquisition profit of Baker Ltd.:*		
	Profit & Loss A/c as per Balance Sheet		20,000
	Less: Post-acquisition profit, 6/15 of ₹ 18,000	7,200	
	Less: Taxation thereon 6/15 of ₹ 6,000	(2,400)	(4,800)
			15,200
	3/4 thereof		11,400
(v)	*Profit & Loss A/c – Able Ltd.*		
	Balance as per P & L A/c		62,000
	Less: Proposed Dividend (20% on ₹ 2,06,250)		41,250
	Balance to Consolidated P & L A/c		20,750
(vi)	*Profit and Loss A/c - Baker Ltd.*		
	Balance as per Profit and Loss A/c		20,000
	Less : Minority Interest (20,000 X 25 %)	5,000	
	Pre-acquisition profit (WN (iv))	11,400	16,400
	Balance in Consolidated P & L A/c		3,600
	Total of (v) and (vi)		24,350

Note: It is assumed that whole of the dividend of ₹ 41,250 proposed by Able Ltd. will be appropriated from revenue, although part of that dividend is due to the ex-shareholders of Baker Ltd.

Illustration 21

In preparing the consolidated balance sheet of H Ltd. as on 31st December, 2011 you are required to show clearly what amount, if any, you would include in respect of W Ltd. with regard to:

(a) Cost of control/reserve;

(b) Profit or loss; and

(c) Minority interest.

under each of the following assumptions :

(i) 48,000 of the shares then in issue of W Ltd. were acquired at a cost of ₹ 75,000 on 1st March, 2009 H Ltd. participated in the proposed dividend of ₹ 8,000.

(ii) 40,000 of the shares then in issue of W Ltd. were acquired at a cost of ₹ 60,000 on 31st Dec., 2009; H Ltd. participated in the bonus issue but not in the proposed dividend of ₹ 9,000.

(iii) 60,000 of the shares then in issue of W Ltd. were acquired at a cost of ₹ 80,000 on 1st July, 2011; H Ltd. did not participate in the proposed dividend of ₹ 6,000.

The balance sheet of W Ltd. as on 31st December, 2011 showed:

	₹
Share Capital, Authorised & Issued of Re. 1 each	*80,000*
Undistributed profits	*24,000*
7% Debentures	*40,000*

The Profit & Loss Appropriation Accounts, for four years ended 31st December, 2011 were as follows:

	2008 ₹	2009 ₹	2010 ₹	2011 ₹
Balance at the beginning of the year	16,000	22,000	43,000	28,000
Bonus issue of one for four - 1st January, 2010			16,000	
			27,000	
Profit for the year(loss)	14,000	30,000	7,000	4,000
	30,000	52,000	34,000	24,000
Proposed Dividends	8,000	9,000	6,000	Nil
Balance carried forward	22,000	43,000	28,000	24,000

Solution

Amounts to be included in the Consolidated Balance Sheet of H Limited as on 31st December, 2011 in respect of W Limited:

Share Capital before bonus issue $\frac{80,000}{5} \times 4 =$ ₹ 64,000 or ₹ 80,000 – ₹ 16,000

(i) *(a)* *Goodwill / Cost of Control:*

	₹	₹
Cost of 48,000 shares on 1st March, 2009		75,000
Less: Dividends from pre-acquisition profits:		
$\frac{48}{64} \times 8{,}000$	6,000	
$\frac{48}{64} \times \frac{2}{12} \times 9{,}000$	1,125	(7,125)
Cost of Investment	(a)	67,875
Nominal value of shares		48,000
Proportion of pre-acquisition profit as at 31st December, 2008	22,000	
Earned in 2009 less dividend $\left[\frac{2}{12} \times 21{,}000\right]$	3,500	
	25,500	
H Ltd.'s share ₹ $25{,}500 \times \frac{48}{64}$		19,125
	(b)	67,125
Goodwill, ₹ (67,875 – 67,125)		750

(b) *Consolidated Profit & Loss balance*

	₹	₹	₹
Profit & Loss Account as per Balance Sheet			24,000
Minority Interest: $\frac{20}{80} \times 24{,}000$		6,000	
Capital Profit :			
Pre-acquisition profit	25,500		
Less: Capitalised for bonus issue	(16,000)		
	9,500		
Share of H Ltd.: $\frac{60}{80} \times 9{,}500$		7,125	13,125
Balances for Consolidation			10,875

(c) *Minority Interest*

Share Capital (1/4)	20,000
Profit & Loss Account	6,000
	26,000

This answer assumes that 2/12th of the proposed dividends for 2009 and capitalisation for the bonus issue both came from pre-acquisition profits.

(ii) (a) *Cost of Control / Goodwill.*

	₹	₹
Cost of 40,000 shares - 31st December, 2009		60,000
Nominal value of shares purchased	40,000	

Pre-acquisition profits $\frac{40}{64}$ × 43,000	26,875	66,875
Capital Reserve		6,875
Shares held by the holding company after bonus issue will be 50,000.		
(b) Profits & Loss Account - as per Balance Sheet	24,000	
Minority Interest: $\frac{30}{80}$ x 24,000	9,000	
Pre-acquisition Profit: $\frac{50}{80}$ × (43,000 – 16,000)	16,875	
		25,875
Balance for Consolidation $\left[3{,}000 \times \frac{5}{8}\right]$		Dr. 1,875
(c) Minority Interest : $\frac{30}{80} \times 1{,}04{,}000$		39,000

(iii) Cost of Control/Goodwill

(a)	*Cost of 60,000 shares - 1st July, 2011*		80,000
	Nominal value of shares when purchased		60,000
	Pre-acquisition profit:		
	at 31st December, 2010	28,000	
	Less: $\frac{6}{12}$ × 4,000	(2,000)	
		26,000	
	H Ltd.'s shares : $\frac{60}{80}$ × 26,000	19,500	
			79,500
	Goodwill (80,000 – 79,500)		500
(b)	*Profit and Loss Account- as per Balance sheet*		24,000
	Minority Interest : $\frac{20}{80}$ x 24,000		6,000
	Pre-acquisition Profit		19,500
			25,500
	Balance for Consolidation		Dr.1,500
(c)	*Minority Interest:* $\frac{20}{80}$ × 1,04,000		26,000

Illustration 22

The Balance Sheet of A Ltd. and C Ltd. on 31st December, 2011 contained the following items relating to the profits and losses of the companies:

	A Ltd. ₹	*B Ltd.* ₹	*C Ltd.* ₹
Non Profit (or loss) for year	*800*	*1,800*	*Dr. 480*
Add : Balance forward	*1,500*	*Loss 800*	*Profit 1,920*
	2,300	*1,000*	*1,440*

A Ltd. acquired 10% of the share capital of B Ltd. on 1st August, 2010. B Ltd. was incorporated on 1st Jan., 2010.

A Ltd. acquired 75% of the share capital of C Ltd. on 1st December, 2011.

B Ltd. acquired 80% of the share capital of C Ltd. on 1st September, 2011.

Prepare draft schedule of consolidated profit and loss account of the group showing the amount to be transferred to other essential accounts to be included in the consolidated balance sheet, i.e., the credit total of ₹ 4,740.

Solution

(i) Analysis of profit of C Ltd.

	Capital Profit ₹	*Revenue Profit* ₹
Balance brought forward	1,920	
Profit/Loss for the year pre-post 8 : 4	–320	–160
	1,600	–160
Shares of Minority Interest (10%)	160	16
Balance	1,440	–144
Share of A Ltd.	160	16*
Share of B Ltd.	1,280	–128

(ii) Analysis of profit of B Ltd.

	Capital Profit ₹	*Revenue Profit* ₹
Balance brought forward divided in the ratio of 7:5 i.e., Capital upto 31st July and Revenue from August	– 467	–333
Revenue loss from C Ltd.		–128
		–461
Profit for the year		1,800
	–467	1,339
Minority Interest (1/4)	117	335
Share of A Ltd.	–350	+1004

* For A Ltd. this represents loss for Sept., Oct., Nov. & Dec. Loss upto lst Dec. is capital loss for A Ltd. Hence only ₹ 4 is Revenue loss; net capital profit for A Ltd. is ₹ 148.

(iii) Capital Profits for Consolidation

B Ltd. in C Ltd.	1,280
A Ltd. in C Ltd. (160 – 12)	148
	1,428
A Ltd. in B Ltd.	–350
	1,078

(iv) *Minority Interest C Ltd.*

in Capital Profit	+160
in Revenue Profit	–16
	144
in B Ltd.: Capital Profit	–117
	27
Revenue Profit	335
	362

(v) Revenue Profit

A Ltd. in B Ltd.	1,004
Less: A Ltd. in C Ltd. (Loss of Dec.)	(4)
	1,000

Illustration 23

As on 30th June, 2012 the draft balance sheets of the companies showed, the following position:

	Rock Ltd. ₹	*King Ltd.* ₹	*Chair Ltd.* ₹
Fixed assets	*1,35,000*	*60,000*	*70,000*
Investments at cost	*1,60,000*	*1,50,000*	*10,000*
	2,95,000	*2,10,000*	*80,000*
Current assets:			
Stock	*55,240*	*36,840*	*61,760*
Debtors	*1,10,070*	*69,120*	*93,880*
Balances at bank	*1,31,290*	*16,540*	*52,610*
	2,96,600	*1,22,500*	*2,08,250*
Less: Current liabilities:			
Creditors	*1,12,060*	*73,130*	*78,190*
Taxation	*30,000*	*—*	*22,000*
Proposed dividends	*1,00,000*	*60,000*	*40,000*
	2,42,060	*1,33,130*	*1,40,190*
Net current assets / (liabilities)	*54,540*	*(10,630)*	*68,060*
	3,49,540	*1,99,370*	*1,48,060*
Financed by:			
Issued ordinary shares of ₹ 10 each	*2,00,000*	*1,50,000*	*80,000*
Capital reserve	*50,000*	*—*	*23,000*
Revenue reserve	*99,540*	*49,370*	*45,060*
	3,49,540	*1,99,370*	*1,48,060*

You also obtain the following information:

(1) King Ltd. acquired 6,800 shares in Chair Ltd. at ₹ 22 per share in 2009 when the balance on capital reserve was ₹ 15,000 and on revenue reserve ₹ 30,500 consolidated.

(2) Rock Ltd. purchased 8,000 shares in King Ltd. in 2009 when the balance on the revenue reserve was ₹ 40,000. Rock Ltd. purchased a further 4,000 shares in King Ltd. in 2010 when the balance on the revenue reserve was ₹ 45,000. Rock Ltd. held no other investments on 30th June, 2012.

(3) Proposed dividends from subsidiary companies are included in the figure for debtors in the accounts of the parent companies.

Prepare the consolidated balance sheet of Rock Ltd. and its subsidiaries in vertical form as on 30th June, 2012, together with the consolidation schedules.

Solution:

Rock Limited
Consolidated Balance Sheet as on 30th June, 2012

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	2,00,000
(b) Reserves and Surplus	2	1,71,044
(2) Minority Interest(W.N iv)		65,918
(3) Current Liabilities		
(a) Trade Payables (1,12,060+73,130+78,190)		2,63,380
(c) Short term Provisions	3	52,000
(b) Other current liabilities	4	1,18,000
Total		8,70,342
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
(i) Tangible assets(1,35,000+60,000+70,000)		2,65,000
(ii) Intangible assets	5	49,592
(b) Non current investment(W.N v)		10,400
(2) Current assets		
(a) Inventories(55,240+36,840+61,760)		1,53,840
(b) Trade Receivables(W.N vi)		1,91,070
(c) Cash & Cash equivalents (1,31,290+16,540+52,610)		2,00,440
Total		8,70,342

Notes to Accounts

			₹
1.	Share Capital		
	20,000 equity shares of ₹ 10 each		2,00,000
2.	Reserves and Surplus		
	Revenue Reserve (99,540+16,064)	1,15,604	
	Capital reserve(50,000+5,440)	55,440	1,71,044
3.	Short term provisions		
	Provision for Taxation (30,000 + 22,000)		52,000
4.	Other current liabilities		
	Proposed Dividend		
	Minority Shareholders	18,000	
	Holding Company	1,00,000	1,18,000
5.	Intangible assets		
	Goodwill (W.N iii)		49,592

Working Notes:

Analysis of profit

(i) Chair Ltd.

	Capital Profit ₹	*Capital Reserve* ₹	*Revenue Reserve* ₹
Capital Reserve in 2009	15,000		
Increase in Capital Reserve		8,000	
Revenue Reserve in 2009	30,500		
Increase in Revenue Reserve			14,560
	45,500	8,000	14,560
Minority Interest 15%	6,825	1,200	2,184
Share of King	38,675	6,800	12,376

(ii) King Ltd.

Revenue Reserve in 2009	40,000		
Increase in Revenue Reserve			9,370
Share in Chair Ltd.		6,800	12,376
	40,000	6,800	21,746
Minority interest (20%)	8,000	1,360	4,349
	32,000	5,440	17,397
Less: $(5,000 \times \frac{4}{15})$ for second acquisition treated as capital	+1,333		–1,333
	33,333		16,064

(iii) Cost of Control / Goodwill

Cost of Investment in Chair		1,49,600	
Cost of Investment in king		1,60,000	
			3,09,600
Paid up value of shares			
in Chair		68,000	
in King		1,20,000	
Capital profits in			
Chair		38,675	
King		33,333	
			2,60,008
Goodwill			49,592

(iv) Minority Interest

	(20%) King Ltd.	*(15%)* Chair Ltd.
Capital	30,000	12,000
Capital Reserve	1,360	1,200
Revenue Reserve	4,349	2,184
Capital Profit	8,000	6,825
	43,709	22,209

(v) Investment

King Limited	1,50,000	
Less: Cost of Chair Limited (6,800 × ₹ 22)	(1,49,600)	
		400
Chair Limited	10,000	
		10,400

(vi) Debtors

Rock Limited		1,10,070
Less: Dividend from King Limited		(48,000)
		62,070
King Limited	69,120	
Less: Dividend from Chair Limited	(34,000)	35,120
Chair Limited		93,880
		1,91,070

2.18 Disposal of a Subsidiary

The results of operations of a subsidiary with which parent-subsidiary relationship ceases to exist are included in the consolidated statement of profit and loss until the date of cessation of the relationship.

Calculation of gain or loss on disposal

On disposal of a subsidiary, the gain or loss on disposal is recognized in the consolidated statement of profit and loss, and is calculated as the aggregate of:

The difference between the proceeds of disposal of the subsidiary and the carrying amount of its assets less liabilities as of the date of disposal;

The cumulative amount of any exchange differences that relate to the subsidiary (non-integral operations) recognized in equity, in accordance with "AS 11 The Effect of Changes in Foreign Exchange Rates".

For the purposes of the disposal calculation, the carrying amount of the subsidiary would include any amount of goodwill carried on the balance sheet in respect of the subsidiary.

Partial disposals

When part of an investment in a subsidiary is sold during the reporting period, the status of the investment immediately after the disposal should determine the accounting. For example:

- If a parent sells a portion of its investment in a subsidiary but still retains a controlling interest, the consolidated financial statements at the end of the period should include the assets, liabilities and operations of the subsidiary and reflect the new minority interest from the date of the transaction: The profit or loss on disposal should be transferred to profit and loss account of holding company.
- If the parent sells a controlling interest in the subsidiary but still retains significant influence over the enterprise, that remaining investment should be reflected in the balance sheet at the end of the period as a single line item using the equity method in accordance with AS 23 Accounting for Investments in Associates in the Consolidated Financial Statements. The subsequent results of operations should also be reported using the equity method. If the disposal qualifies as discontinuing operation, presentation of the discontinuing operation should follow AS 24 Discontinuing Operations; and
- When almost all of a subsidiary is sold (except for an interest which does not allow the parent to exert significant influence over the subsidiary) and if the sale of the subsidiary qualifies as a discontinuing operation, presentation of the discontinuing operation should follow AS 24 Discontinuing Operations. The remaining interest in equity should be accounted for in accordance with AS 30 Financial Instruments: Recognition and Measurement.

In a parent's separate financial statement, an investment in subsidiaries should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments, from the date the enterprise ceases to be a subsidiary and does not become an associate*.

The carrying amount of the investment at the date it ceases to be a subsidiary is regarded as cost thereafter.

Illustration 24

From the following summarised Balance Sheets of A Ltd. and its subsidiary B Ltd., prepare a consolidated Balance Sheet as on 31st December, 2011.

* Accounting Standard (AS) 23, 'Accounting for Investments in Associates in Consolidated Financial Statements', , defines the term 'associate' and specifies the requirements relating to accounting for investments in associates in Consolidated Financial Statements.

Equity and Liabilities	*A Ltd.* ₹	*B Ltd.* ₹	*Assets*	*A Ltd.* ₹	*B Ltd.* ₹
Share Capital			*Sundry Assets*	*93,000*	*32,000*
Equity Shares of ₹ 10 each	*1,00,000*	*20,000*	*Shares in B Ltd. 1,200 shares at ₹ 15 each*	*18,000*	
Profit on sale of shares	*3,000*				
Profit and Loss A/c					
Brought forward	*6,000*	*7,200*			
For the year	*2,000*	*4,800*			
	1,11,000	*32,000*		*1,11,000*	*32,000*

A Ltd. bought in earlier year 1,600 equity shares in B Ltd.@ 15 when the Profit and Loss Account balance in B Ltd. was ₹ 4,400. A sold 400 shares @ ₹ 22.50, credited the difference between the sale proceeds and cost to "Profit on sale of investment account" on 30th June, 2009 and crediting the balance to the investment account. Profit during the year accrued uniformly.

Solution:

Consolidated Balance Sheet of A Ltd., and its subsidiary B Ltd.
as at 31st December, 2011

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1,00,000
(b) Reserves and Surplus	2	15,560
(2) Minority Interest(W.N iii)		12,800
Total		1,28,360
II. Assets		
(1) Non-current assets		
Fixed assets		
(i) Tangible assets (93,000+32,000)		1,25,000
(ii) Intangible assets	3	3,360
Total		1,28,360

Notes to Accounts

			₹
1.	Share Capital		
	10,000 equity shares of ₹ 10 each		1,00,000
2.	Reserves and Surplus		
	Profit & Loss Account (W.N iv)		15,560
3.	Intangible assets		
	Goodwill (W.N ii)		3,360

Working Notes :

(i) Analysis of Profit of B Ltd.

	Capital Profit ₹	*Revenue Profit* ₹
P/L A/c Balance on the date of acquisition	4,400	
Increase in the balance after acquisition		2,800
Profit for the year		4,800
	4,400	7,600
Less : Minority Interest (40 per cent)	1,760	3,040
Share of A Ltd	2,640	4,560

(ii) Cost of Control

Cost of Investments		18,000
Less : Paid-up value of shares	12,000	
Share of Capital Profits	2,640	(14,640)
Goodwill		3,360

(iii) Minority Interest (40 per cent)

Paid-up value of shares held	8,000
Share of Capital Profits	1,760
Share of Revenue Profits	3,040
	12,800

(iv) Consolidated Revenue Profit

Balance as per Profit and Loss A/c of A Ltd.	8,000
Add: Profit on sale of shares	3,000
	11,000
Share in Revenue Profit of B Ltd.	4,560
	15,560

(v) Investments in B Ltd.

Particulars	₹	*Particulars*	₹
To Balance b/d	24,000	By Bank	9,000
To Profit on Sale	3,000	By Balance c/d	18,000
	27,000		27,000

Illustration 25

H Ltd. purchased on 1.4.2009, 8,000 equity shares of ₹ 100 each in S Ltd. when S Ltd. had ₹ 10,00,000 share capital.

It sold 500 such shares on 1.4.2010 and purchased 1,000 shares on 1.4.2011.

S Ltd. paid 15% dividend each year in September and there was no change in Share Capital Account upto 31.3.2012. Profit and Loss Account balances in S Ltd. and Investments of H Ltd. in S Ltd. on different dates were as under:

	Profit and Loss Account balance of S Ltd. ₹	*Investments of H Ltd. in S Ltd.* ₹
1st April, 2009	*5,00,000*	*12,80,000*
31st March, 2010	*6,20,000*	*12,80,000*
31st March, 2011	*7,00,000*	*11,90,000*
31st March, 2012	*8,00,000*	*14,00,000*

The amounts shown as investments represent cost price as reduced by sales and increased by further purchase without making any adjustment for profit or loss on sale for dividend.

Prepare statements to show the relevant figures as on 31st March, 2010, 2011 and 2012 for preparation of Consolidated Accounts in respect of:

(a) Goodwill or Cost of Control

(b) Revenue Profit.

Solution

(a) Goodwill or Cost of Control:

	31.3.2010 ₹	*31.3.2011* ₹	*31.3.2012* ₹
Correct Cost of Investment as per Working Note no. (i)	11,60,000	10,87,500	12,82,500
Less: Paid up value of shares in hand	(8,00,000)	(7,50,000)	(8,50,000)
	3,60,000	3,37,500	4,32,500
Less : H Ltd.'s share of capital profits as per working Notes no (ii)	(2,80,000)	(2,62,500)	(3,17,500)
Goodwill or Cost of Control	80,000	75,000	1,15,000

(b) Revenue Profit

	31.3.2010 ₹	*31.3.2011* ₹
Balance of Profit & Loss Account	6,20,000	7,00,000
Less : Capital Profits		
Balance of Profit & Loss Account as on 1st April, 2009 after deducting dividend for the year 2008-2009 @15%	(3,50,000)	(3,50,000)
	2,70,000	3,50,000
Less : Minority Interest		
20% on 31.3.2010	(54,000)	
25% on 31.3.2011		(87,500)
H Ltd.'s share	2,16,000	2,62,500

		₹
Balance of Profit & Loss Account on 31.3.2012		8,00,000
Less : Capital Profits as mentioned above		(3,50,000)
		4,50,000
Less : Minority Interest @ 15%		(67,500)
		3,82,500
But for 10% shares acquired on 1.4.2011 there are additional Capital Profits		
Balance of Profit & Loss Account as on 31.3.2011	7,00,000	
Less: Dividend for the year ended 31.3.2011 @ 15%	(1,50,000)	
	5,50,000	
Less : Capital Profit already taken into account above	(3,50,000)	
Additional Capital Profit	2,00,000	
H Ltd.'s share = ₹ 2,00,000 × 10/100		20,000
		3,62,500

Working Notes:

(i) Calculation of correct cost of investments

Investment in Shares in S Ltd. Account

2009		₹	*2010*		₹
April 1	To Bank (8,000 shares)	12,80,000	March 31	By Profit & Loss Account Rectification regarding pre-acquisition dividend – ₹ 8,00,000 × 15/100	1,20,000
				By Balance c/d (8,000 shares)	11,60,000
		12,80,000			12,80,000
2010		₹	*2010*		₹
April 1	To Balance b/d (8,000 shares)	11,60,000	April 1	By Bank (Sale proceeds of 500 shares = ₹ 12,80,000 – ₹11,90,000)	90,000
April 1	To Profit and Loss Account Profit on sale: ₹ 90,000 – (11,60,000 × 500/8,000)	17,500	2011 March 31	By Balance c/d (7,500 shares)	10,87,500
		11,77,500			11,77,500
2011		₹	*2012*		₹
April 1	To Balance b/d (7,500 shares)	10,87,500	March 31	By Profit & Loss	

	To Bank (1,000 shares purchased)	2,10,000		Account–Rectification regarding pre acquisition dividend on 1,000 shares	15,000
				By Balance c/d (8,500 shares)	12,82,500
		12,97,500			12,97,500
2012					
April 1	To Balance b/d	12,82,500			

(ii) Capital Profits :

31st March 2010:	₹
Balance of Profit & Loss Account as on 31.3.2009	5,00,000
Less: Dividend on ₹ 10,00,000 @15%	(1,50,000)
	3,50,000
H Ltd.'s share = ₹ 3,50,000 × $\frac{8,000}{10,000}$ = 2,80,000	
31st March, 2011:	
As H Ltd. has sold 500 shares, its share of capital profits is reduced.	
H Ltd.'s share = $\frac{₹3,50,000 \times 7,500}{10,000}$ = ₹ 2,62,500	
31st March, 2012 :	
Balance of Profit & Loss Account as on 31.3.2011	7,00,000
Less: Dividend on ₹ 10,00,000 @ 15%	(1,50,000)
	5,50,000
H Ltd.'s share in respect of 1,000 shares purchased on 1.4.2011 = $\frac{₹5,50,000 \times 1,000}{10,000}$	55,000
H Ltd.'s share of capital profits in respect of 7,500 shares purchased on 31.3.2009 as calculated above	2,62,500
Total	3,17,500

2.19 Foreign Subsidiaries

For consolidating foreign subsidiaries, the first step is to convert the figures of foreign subsidiary into reporting currency on the basis of rules as prescribed by AS 11 (revised 2003), "The Effects of Changes in Foreign Exchange Rates". The amount of exchange difference is calculated as the balancing figure, which is accounted for as post-acquisition profit/loss. After such conversion, the consolidation is done in usual manner.

UNIT 3:TREATMENT OF INVESTMENT IN ASSOCIATES IN CONSOLIDATED FINANCIAL STATEMENTS

3.1 Meaning of Associates

An associate is an enterprise in which an investor has significant influence and which is neither a subsidiary nor a joint venture of the investor. 'Significant influence' means the power to participate in the financial and operating policy decisions of the investee, but the investor does not have control over those policies.

Indicators of significant influence

Significant influence may be gained by the investor by virtue of share ownership, statute or agreement.

When an investor exercises significant influence over the investee, one or more of the following indicators is usually present:

- representation on the board of directors or corresponding governing body of the investee;
- participation in policymaking processes;
- material transactions between the investor and the investee;
- interchange of managerial personnel; or
- provision of essential technical information.

Significant Influence - Holding 20% or more of voting power

As a general rule, significant influence is presumed to exist when an investor holds, directly or indirectly through subsidiaries, 20% or more of the voting power of the investee.

As with the classification of any investment, the substance of the arrangement in each case will need to be considered. If it can be clearly demonstrated that an investor holding 20% or more of the voting power of the investee does not have significant influence, the investment will not be accounted for as an associate.

As substantial or majority ownership by another investor does not necessarily preclude an investor from having significant influence.

If the investor holds, directly or indirectly through subsidiaries, less than 20% of the voting power of the investee, it is presumed that the investor does not have significant influence, unless such influence can be clearly demonstrated. The presence of one or more of the indicators as above may indicate that an investor has significant influence over a less than 20% owned corporate investee.

3.2 Accounting Method for Associates

AS 23 suggests equity method of accounting for investments in associates.

Under equity method of accounting investment is initially recorded at cost, identifying any goodwill/ capital reserve arising at the time of acquisition. The carrying amount of the

investment is adjusted thereafter for the post-acquisition change in investor's share of net assets in the investee. Distributions received from the investee reduce the carrying amount of the investment. The investor's share in the operational result of the investee is reflected in the consolidated statement of profit and loss.

The following procedure should be followed:

- Investment is initially recorded at cost. Subsequently, the carrying amount is increased on the basis of share of profit or decreased on the basis of share of loss in the associate.
- Step (1): Find out value of investments on the basis of proportionate value of net assets of the investee;
- Step (2): Find out goodwill or capital reserve arising out of the purchase consideration. If the purchase price is above the value of investments determined in step (1) then there is goodwill and if the purchase price is less than the value of the investments determined in step (1) then there is capital reserve.
- Step (3): Goodwill or capital reserve as determined in step (2) should be included in the carrying amount of the investments with a separate disclosure. On the contrary, investments are recognised at purchase price as per AS 13 without disclosing goodwill/capital reserve.

  Goodwill/capital reserve can be disclosed within bracket below the "Investments in Associates" in the following style and accumulated income which was not earlier recognized should be added to value of investments for first time consolidation with corresponding credit to consolidated reserve.

Investments

Long Term Investments

in Associates – at original cost

[including ₹.....goodwill/capital reserve (previous year ₹.....)
arising on acquisition of associates]

Add: Accumulated income from Associates.

- Unrealised profit or loss resulting from transactions between the investor (and its consolidated subsidiary) and the associate should be eliminated to the extent of interest of the investor in the associate.
- The carrying amount of investment in an associate is reduced to recognise decline in the value of investments computed in terms of proportionate net assets of the investee.
- Applying the logic of consolidation unrealized profit arising out of intra-group transactions should be eliminated.

In case an associate has made a provision for proposed dividend in its financial statements, the investor's share of the results of operations of the associate should be computed without taking into consideration the proposed dividend [ASI-16].

The investor may account for its share of proposed dividend in its profit and loss account. In that case this approach helps to reflect correct application of equity method.

But if the investor has not accounted for its proportionate share of proposed dividend, consolidated financial statement will not reflect fair position.

3.3 Non- Application of Equity Method

The general rule is that investments in associates are accounted for using the equity method of accounting. If, however, any of the two conditions under-mentioned are fulfilled, the investment is not accounted for using the equity method but is accounted for in accordance with AS 13 'Accounting for Investments' with disclosure of the reasons for not applying the equity method in accounting for investments;

(1) when an investment is acquired for the purpose of disposal in the near future, i.e., as short term investments; and

(2) there is severe long term restriction on fund transfer by the associate to the investor.

3.4 Treatment of change in equity of associate not arising out of profit and loss account

The situation may arise that change in equity of the associate which are not through profit and loss account.

For example, the associate may revalue its fixed assets and create revaluation reserve. In such cases, increase/decrease in the value of investments should be directly added to/subtracted from the carrying amount of investments with corresponding credit/debit to the balance of the consolidated profit and loss account in the balance sheet. This adjustment should not be routed through consolidated profit and loss account.

UNIT 4: TREATMENT OF INVESTMENT IN JOINT VENTURES IN CONSOLIDATED FINANCIAL STATEMENTS

Joint venture is defined as a contractual arrangement whereby **two or more parties undertake an economic activity, which is subject to joint control.**

Business entities, in their process to achieve improved performance and to provide value addition to stakeholders, exert themselves in establishing various forms of business relationships to have either access or control over the economic resources of other business entities. Joint ventures are one of such form of business relationship. Such relations are made either to promote trade, or to gain access to new markets.

Joint venture is controlled by two or more venturers. Additionally, there can also be investors who do not have control. By joint venture, its co-venturers who expect to achieve some common purpose or benefit. In India, The ICAI has come up with an Accounting Standard 27 on "Financial Reporting of interests in Joint Ventures" both in separate financial statements and also in consolidated financial statements.

4.1 Scope Under AS 27

AS 27 should be applied in accounting for interests in joint ventures and the reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers and investors, regardless of the structures or forms under which the joint venture activities take place.

The requirements relating to accounting for joint ventures in consolidated financial statements, contained in AS 27 are applicable only where consolidated financial statements are prepared and presented by the venturer.

4.2 Forms of Joint Venture

AS 27 identifies three broad types of Joint Ventures-

- jointly controlled operations,
- jointly controlled assets and
- jointly controlled entities.

4.2.1 **Jointly Controlled Operations:** No separate establishment: The operation of some joint ventures involves the use of the assets and other resources of the venturers rather than the establishment of a corporation, partnership or other entity, or a financial structure that is separate from the venturers themselves.

Each venture uses its own assets and liabilities: Each venturer uses its own fixed assets and carries its own inventories. It also incurs its own expenses and liabilities and raises its own finance, which represent its own obligations.

Own employees: The joint venture's activities may be carried out by the venturer's employees alongside the venturer's similar activities.

Sharing of common expenses and revenues:The joint venture agreement usually provides means by which the revenue from the jointly controlled operations and any expenses incurred in common are shared among the venturers.

An example of a jointly controlled operation is when two or more venturers combine their operations,

resources and expertise in order to manufacture, market and distribute, jointly, a particular product, such as an aircraft. Different parts of the manufacturing process are carried out by each of the venturers.

Each venturer bears its own costs and takes a share of the revenue from the sale of the aircraft, such share being determined in accordance with the contractual arrangement.

4.2.2 Jointly Controlled Assets: Some joint ventures involve the joint control, and often the joint ownership, by the venturers of one or more assets contributed to, or acquired for the purpose of, the joint venture and dedicated to the purposes of the joint venture.

The assets are used to obtain economic benefits for the venturers. Each venturer may take a share of the output from the assets and each bears an agreed share of the expenses incurred.

An example of a jointly controlled asset is an oil pipeline jointly controlled and operated by a number of oil production companies.

Each venturer uses the pipeline to transport its own product in return for which it bears an agreed proportion of the expenses of operating the pipeline.

Another example of a jointly controlled asset is when two enterprises jointly control a property, each taking a share of the rents received and bearing a share of the expenses.

4.2.3 Jointly Controlled Entities: A jointly controlled entity is a joint venture which is established as a separate legal entity which can be in form of a corporation, partnership or other entity in which each venturer has an interest.

The entity operates in the same way as other enterprises, except that a contractual arrangement between the venturers establishes joint control over the economic activity of the entity.

4.3 Accounting Treatment

4.3.1 Jointly Controlled Operations: As per para 13 of AS 27, in respect of its interests in jointly controlled operations, a venturer should recognise in its separate financial statements and consequently in its consolidated financial statements:

(a) the assets that it controls and the liabilities that it incurs; and

(b) the expenses that it incurs and its share of the income that it earns from the joint venture.

Because the assets, liabilities, income and expenses are already recognised in the separate financial statements of the venturer, and consequently in its consolidated financial statements, no adjustments or other consolidation procedures are required in respect of these items when the venturer presents consolidated financial statements.

The only accounting issue that arises is that the output from the project is to be shared among the venturers and, therefore, there must be some mechanism for specifying the allocation of the proceeds and the sharing of any joint expenses.

4.3.2 Jointly Controlled Assets As per para 19 of AS 27, in respect of its interest in jointly controlled assets, a venturer should recognise, in its separate financial statements, and consequently in its consolidated financial statements:

(a) its share of the jointly controlled assets, classified according to the nature of the assets;

(b) any liabilities which it has incurred;

(c) its share of any liabilities incurred jointly with the other venturers in relation to the joint venture;

(d) any income from the sale or use of its share of the output of the joint venture, together with its share of any expenses incurred by the joint venture; and

(e) any expenses which it has incurred in respect of its interest in the joint venture.

Because the assets, liabilities, income and expenses are already recognised in the separate financial statements of the venturer, and consequently in its consolidated financial statements, no adjustments or other consolidation procedures are required in respect of these items when the venturer presents consolidated financial statements.

4.3.3 Jointly Controlled Entities

A jointly controlled entity maintains its own accounting records and prepares and presents financial statements in the same way as other enterprises in conformity with the requirements of AS 27 applicable to that jointly controlled entity.

Separate Financial Statements of a Venturer

In a venturer's separate financial statements, interest in a jointly controlled entity should be accounted for as an investment in accordance with Accounting Standard (AS) 13, Accounting for Investments.

Consolidated Financial Statements of a Venturer

In its consolidated financial statements, a venturer should report its interest in a jointly controlled entity using proportionate consolidation except

(a) an interest in a jointly controlled entity which is acquired and held exclusively with a view to its subsequent disposal in the near future; and

(b) an interest in a jointly controlled entity which operates under severe long-term restrictions that significantly impair its ability to transfer funds to the venturer.

Interest in such a jointly controlled entity should be accounted for as an investment in accordance with Accounting Standard (AS) 13, Accounting for Investments.

4.4 Proportionate Consolidation Method

Separate line Items: AS 27 defines proportionate consolidation as a method of accounting and reporting whereby a venturer's share of each of the assets, liabilities, income and expenses of a jointly controlled entity is reported as separate line items in the venturer's financial statements.

Balance sheet and profit & loss account to include share of venturer: The application of proportionate consolidation means that the balance sheet of the venture includes its share of the assets that it controls jointly, and its share of the liabilities for which it is jointly responsible. The statement of profit and loss of the venture includes its share of the income and expenses of the jointly controlled entity.

4.4.1 Steps for Proportionate Consolidation: All the steps are similar to those of consolidation of Subsidiary except that when Consolidated Balance sheet is prepared; the venturer's (Investor) proportionate share of each asset and liability is added.

Step 1: Ascertain the date of Investment of venturer in Jointly Controlled Entities (JCE).

Step 2: Ascertain venturer's share of Interest in the Jointly Controlled Entities.

Step 3: Analyse profits of the Jointly Controlled Entities as pre-acquisition and post-acquisition with reference to date of acquisition.

Step 4: Ascertain the venturer's share of both pre-acquisition and post-acquisition profits of Jointly Controlled Entities analysed above.

Step 5: Ascertain Goodwill/Capital Reserve

A)	Cost of Investment		
	Amount invested *Less:* Pre acquisition dividend	XXX XXX	XXX
B)	*Less:* Venturer's share of net assets in JCE as at date of acquisition represented by venturer's share of: (i) Share Capital (ii) Pre acquisition profits	 XXX XXX	 XXX
C)	Goodwill/Capital Reserve (Difference between A & B)		XXX

Steps 6: Elimination of Inter Company transactions.

Elimination of unrealized profit on unsold stock forming part of intra group transactions to be eliminated to the extent of venturer's stake.

Step 7: Reserves for Consolidated Balance Sheet

a)	Aggregate reserves for Consolidated Balance Sheet of holding company and subsidiaries as per AS 21 and AS 23 where applicable.	XXX
b)	*Add:* Venturer's share of post acquisition profit (Step 4)	XXX
c)	*Less:* Venturer's share of unrealized profit (Step 6A)	(XXX)
		XXX

Step 8: Prepare Consolidated Balance Sheet

Liabilities

	Parents	*Subsidiary (Say 80%)* ₹	*Associate*	*JCE (Say 50%)*	*Adj.*	*Consolidated*
Share Capital	100%	--	--	--	Cancel Cross holding only	XXX
Reserves						Step 7
Minority Interest	-	20%	-	-	-	XXX
Outside Liabilities (Individually)	100%	100%	-	50%	Cancel Inter Company Balances Subsidiary – 100% JCE – 50%	XXX XXX

Assets

	Parent	*Subsidiary (Say 80%)*	*Associate*	*JCE (Say 50%)*	*Adj.*	*Consolidated*
Fixed Assets	100%	100%		50%	Adjust for -Revaluation -Unamortised profit on Intra group transaction	XXX
Investment	-	-	- Only Outside Investment and carrying amount of Investment in Associate as per Step 8			XXX
Current Assets Loans and Advances	100%	100%	-	50%	Adjust for -Unrealised profit on Intra group transaction	XXX
Miscellaneous Expenditure to the extent not written off	100%	-	-	-	-	XXX
						XXX
						XXX

4.5 Different Reporting Dates

- The financial statements of the jointly controlled entity used in applying proportionate consolidation are usually drawn up to the same date as the financial statements of the venturer.
- When the reporting dates are different, the jointly controlled entity often prepares, for applying proportionate consolidation, statements as at the same date as that of the venturer.
- When it is impracticable to do this, financial statements drawn up to different reporting dates - may be used provided the difference in reporting dates is not more than six months. In such a case, adjustments are made for the effects of significant transactions or other events that occur between the date of financial statements of the jointly controlled entity and the date of the venturer's financial statements.
- The consistency principle requires that the length of the reporting periods, and any difference in the reporting dates, are consistent from period to period.

4.6 Uniform Accounting Policies

- The venturer usually prepares consolidated financial statements using uniform accounting policies for the like transactions and events in similar circumstances.
- In case a jointly controlled entity uses accounting policies other than those adopted for the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to the financial statements of the jointly controlled entity when they are used by the venturer in applying proportionate consolidation.

- If it is not practicable to do so, that fact is disclosed together with the proportions of the items in the consolidated financial statements to which the different accounting policies have been applied.

4.7 Offsetting of Assets and Liabilities

While giving effect to proportionate consolidation, it is inappropriate to offset any assets or liabilities by the deduction of other liabilities or assets or any income or expenses by the deduction of other expenses or income, unless a legal right of set-off exists and the offsetting represents the expectation as to the realisation of the asset or the settlement of the liability.

4.8 Goodwill or Capital Reserve

Any excess of the cost to the venturer of its interest in a jointly controlled entity over its share of net assets of the jointly controlled entity, at the date on which interest in the jointly controlled entity is acquired, is recognised as goodwill, and separately disclosed in the consolidated financial statements. When the cost to the venturer of its interest in a jointly controlled entity is less than its share of the net assets of the jointly controlled entity, at the date on which interest in the jointly controlled entity is acquired, the difference is treated as a capital reserve in the consolidated financial statements. Where the carrying amount of the venturer's interest in a jointly controlled entity is different from its cost, the carrying amount is considered for the purpose of above computations.

4.9 Discontinuance of Proportionate Consolidation Method

A venturer should discontinue the use of proportionate consolidation from the date that:

(a) it ceases to have joint control over a jointly controlled entity but retains, either in whole or in part, its interest in the entity; or

(b) the use of the proportionate consolidation is no longer appropriate because the jointly controlled entity operates under severe long-term restrictions that significantly impair its ability to transfer funds to the venturer.

From the date of discontinuing the use of the proportionate consolidation, interest in a jointly controlled entity should be accounted for:

(a) in accordance with Accounting Standard (AS) 21, Consolidated Financial Statements, if the venturer acquires unilateral control over the entity and becomes parent within the meaning of that Standard; and

(b) in all other cases, as an investment in accordance with Accounting Standard (AS) 13, Accounting for Investments, or in accordance with Accounting Standard (AS) 23, Accounting for Investments in Associates in Consolidated Financial Statements, as appropriate. For this purpose, cost of the investment should be determined as under:

   (i) the venturer's share in the net assets of the jointly controlled entity as at the date of discontinuance of proportionate consolidation should be ascertained, and

   (ii) the amount of net assets so ascertained should be adjusted with the carrying amount of the relevant goodwill/capital reserve (see paragraph 37) as at the date of discontinuance of proportionate consolidation.

4.10 Joint Venture cum Subsidiary

When an enterprise establishes joint control over an Entity, which is also a subsidiary of that enterprise as per AS 21, such entity is treated as subsidiary company as per AS 21 and should be accounted accordingly. However, the consolidation of such entity does not preclude other venturers from treating such entity as a Joint Venture under AS 27.

Illustration 26

Consolidated data of X Ltd., and its 100% subsidiary Y Ltd. and also information of Z Ltd. relating to the year end 31st March, 2012 is given below:

BALANCE SHEET

(₹ in thousand)

	CBS of X Ltd. and its 100% Subsidiary Y Ltd.	*Z Ltd.*
Issued ordinary share capital	2,000	1,000
Reserves	3,450	2,000
Debentures	2,000	1,500
Current liabilities	4,550	2,500
Total	12,000	7,000
Fixed assets (net)	6,500	4,000
Investment in Z Ltd. at cost	2,000	---
Current assets	3,500	3,000
Total	12,000	7,000

PROFIT AND LOSS ACCOUNT

	X Ltd and its 100% Subsidiary Y Ltd.	*Z Ltd.*
Sales	2000	1000
Expenses	(900)	(500)
Trading profit before tax	1,100	500
Dividend from Uncertain Ltd.	100	----
Taxation	(600)	(200)
Profit after tax	600	300
Opening Balance	3150	1100
Dividends paid	(300)	(200)
Retained Profit	3450	1200

X Ltd. acquired 50% of the ordinary share capital of Z Ltd. on 1st April, 2011 for ₹ 2,000 thousands when its reserves were ₹ 1,900 thousands and sold this holding on 3rd April, 2012for ₹ 2,050 thousands.

You are required to prepare the 'Group' Profit and Loss account (draft) and Balance Sheet (draft) on four bases as follows:

1. When Z Ltd. is treated as a subsidiary
2. When Z Ltd. is treated as an associated company
3. When Z Ltd. is treated as an investment
4. When Z Ltd. is treated as a Joint Venture.

Solution

	Particulars	*Subsidiary*	*Investment*	*Associate*	*Joint Venture*
a.	Accounting Standard Applicable	21	13	23	27
b.	Method	Full Consolidation	Cost method	Equity method	Proportionate Consolidation
c.	Date of Acquisition	1st April 2011	1st April 2011	1st April 2011	1st April 2011
d.	Shareholding	X Ltd – 50% Minority Int. – 50%	Not applicable	Extent of investment 50%.	Extent of financial interest 50%.
e.	Analysis of reserves	1) Opening balance 1900 thousands pre-acquisition 2) Current year retained profit 100 thousands post-acquisition	Not applicable	1) Opening balance 1900 thousands pre-acquisition 2) Current year retained profit 100 thousands post acquisition	1) Opening balance 1900 thousands pre-acquisition 2) Current year retained profit 100 thousand post acquisition.
f.	Apportionment of Profits 1) Pre-acquisition 2) Post-acquisition	1) X Ltd. – 950 thousands 2) Minority – 950 thousands 1) X Ltd. – 50 thousands 2) Minority – 50 thousands	Not applicable	1) X Ltd. – 950 thousands (Investing Co. Interest) 2) X Ltd. – 50 thousands	1) X Ltd. – 950 thousands (Venturer Interest). 2) X Ltd. – 50 thousands.
g.	Outsider's interest	Minority Interest 1) Share capital - 500 thousands 2) Pre-acquisition – 950 thousands 3) Post acquisition - 50 thousands Total 1500 thousands	Not applicable		
h.	Goodwill/Capital Reserve	1) Cost of Investment – 2000 thousands 2) Share of Net Assets on the date of investment - Share Capital 500 thousands - Capital Profits 950 thousands	Not applicable	1) Cost of investment 2000 thousands 2) Share of net assets on the date of investment - share capital 500 thousands - capital profits 950 thousands	1) Cost of investment 2000 thousands 2) Share of net assets on the date of investment - Share capital 500 thousands - Capital profits 950 thousands

		- 1450 thousands 3) Goodwill 550 thousands		Total 1450 thousands - Goodwill 550 thousands	Total 1450 thousands - Goodwill 550 thousands
i.	Inter Company Transactions 1) Inter company owings 2) Unrealised Profits	Eliminate in full Eliminate in full	Not applicable	Not applicable Eliminate to the extent of investing co's interest	Eliminate to the extent of venturer's interest
J.	Reserves for CBS	*	Not Applicable	*	*
k.	Carrying amount of Investment in CBS	Nil	2000 thousands	a) Amount Invested i)Share of Net Assets 1450 thousands ii) Goodwill - 550 thousands 2000 thousands b) Add. Share of Post Acquisition profits 150 thousand c) Less: Dividend received 100 thousands Total 2050 thousands	Nil

* Reserves for CBS

Draft Consolidated Profit and Loss A/c
as at 31.03.2012

₹ in thousands

Particulars	*Subsidiary*	*Investment*	*Associate*	*Joint Venture*
Sales	3,000	2,000	2,000	2,500
Expenses	(1,400)	(900)	(900)	(1,150)
Dividend	-	100	-	-
PBT	1,600	1,200	1,100	1,350
Tax	(800)	(600)	(600)	(700)
PAT	800	600	500	650
Share of profits from Associate	-	-	150	-
Opening Balance B/d	3,150	3,150	3,150	3,150
Dividend Paid	(300)	(300)	(300)	(300)
Share of Minority Interest	(150)	-	-	-
Balance carried forward to Balance Sheet	3,500	3,450	3,500	3,500

Draft Consolidated Balance Sheet
as at 31.03.2012

₹ in thousands

	If Subsidiary	*If Investment*	*If Associate*	*If Joint Venture*
Equity and Liabilities				
Share Capital	2,000	2,000	2,000	2,000
Reserves	3,500	3,450	3,500	3,500
Debentures	3,500	2,000	2,000	2,750
Current Liabilities	7,050	4,550	4,550	5,800
Minority Interest	1,500	-		-
Total	17,550	12,000	12,050	14,050
Assets				
Non-current assets				
Fixed Assets				
Tangible Assets	10,500	6,500	6,500	8,500
Intangible Assets	550	-	-	550
Investments	-	2,000	2,050 (Goodwill – ₹ 550 thousands)	-
Current Assets	6,500	3,500	3,500	5,000
Total	17,550	12,000	12,050	14,050

References :

AS 13 : Accounting for Investments.

AS 21 : Consolidated Financial Statements

AS 23 : Accounting for Investments in Associates

AS 27 : Financial Reporting of Interests in Joint Ventures