P2 – Corporate Reporting

Group Account Workbook

Highlights

- ✓ Introduction to Group Accounts
- ✓ Definitions
- ✓ F7 Group Refreshers‘ Course
- ✓ Complex Group
- ✓ Changes in Group Structure
- ✓ Calculations and Workings
- ✓ Presentation and Disclosure Issues
- ✓ Practical Illustrations/Past Exam Questions

Introduction to Group Accounts

- Group consists of a parent and its subsidiaries

(NB – THESE ASPECTS WILL BE DISCUSSED IN THE CLASS)

Definitions

- **Group -** consists of a parent and its subsidiaries
- **Parent -** an entity that controls one or more entities
- **Subsidiary -** an entity that is controlled by another entity
- **Control -** an investor controls an investee when the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee
- **Power -** existing rights that give the current ability to direct the relevant activities
- **Relevant activities** are activities of the investee that significantly affect the investee's returns
- **Non-controlling interest** is equity in a subsidiary not attributable, directly or indirectly, to a parent

Definitions – cont'd

- **Business Combination** is a transaction or other event in which an acquirer obtains control of one or more businesses
- **A business** is an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs or other economic benefits directly to investors or other owners, members or participants
- **Goodwill** is an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognised
- **Consolidated Financial Statement** is the financial statements of a group in which the assets, liabilities, equity, income, expenses and cash flows of the parent and its subsidiaries are presented as those of a single economic entity

Example 1

- On 1 January 2008, Almer acquired a 50% interest in Bolmer for $60m. Almer already held a 20% interest which had been acquired for $20m but which was valued at $24m at 1 January 2008.

- The fair value of the NCI at 1 January 2008 was $40m, and the fair value of the identifiable net assets of Bolmer was $110m.

- The goodwill calculation would be as follows, using the full goodwill method

Solution 1

	$m	$m
1 January 2008 consideration	60	
Fair value of interest held	24	
		84
NCI		40
		124
Fair value of identifiable net assets		(110)
Goodwill		14

A gain of $4m would be recorded on the increase in the value of the previous holding in Bolmer.

Example 2 – Acquisition from NCI

On 1 January 2008, Ragab acquired 70% of the equity interests of Piner, a public limited company. The purchase consideration comprised cash of $360m. The fair value of the identifiable net assets was $480m. The fair value of the NCI in Piner was $210m on 1 January 2008. Ragab wishes to use the full goodwill method for all acquisitions.

Ragab acquired a further 10% interest from the NCIs in Piner on 31 December 2008 for a cash consideration of $85m. The carrying value of the net assets of Piner was $535m at 31 December 2008.

Solution 2

	$m	$m
Fair value of consideration for 70% interest	360	
Fair value of NCI	210	570
Fair value of identifiable net assets		(480)
Goodwill		90

The net assets of Piner have increased by $(535 - 480)m ie $55m and therefore the NCI has increased by 30% of $55m, ie $16.5m. However, Ragab has purchased an additional 10% of the shares and this is treated as a treasury transaction. There is no adjustment to goodwill on the further acquisition

Solution 2 – cont'd

	$m
Piner NCI, 1 January 2008	210
Share of increase in net assets in post-acquisition period	16.5
Net assets, 31 December 2008	226.5
Transfer to equity of Rage (10/30 x 226.5)	(75.5)
Balance at 31 December 2008 – NCI	151
Fair value of consideration	85
Charge to NCI	(75.5)
Negative movement in equity	9.5

Ragab has effectively purchased a further share of the NCI, with the premium paid for that share naturally being charged to equity. The situation is comparable when a parent company sells part of its holding but retains control.

Example 3- Disposal of part of holding to NCI

Using **Example 2**, instead of acquiring a further 10%, Ragab disposes of a 10% interest to the NCIs in Piner on 31 December 2008 for a cash consideration of $65m.

The carrying value of the net assets of Piner is $535m at 31 December 2008.

Solution 3

	$m
Piner net assets at 1 January 2008	480
Increase in net assets	55
Net assets at 31 December 2008	535
Fair value of consideration	65
Transfer to NCI (10% x (535 net assets + 90 goodwill))	(62.5)
Positive movement in equity	2.5

The parent has effectively sold 10% of the carrying value of the net assets including goodwill) of the subsidiary ($62.5m) at 31 December 2008 for a consideration of $65m, giving a profit of $2.5m, which is taken to equity.

Disposal to retain Associate Holding

IAS 27 sets out the adjustments to be made when a parent loses control of a subsidiary:

- Derecognise the carrying amount of assets (including goodwill), liabilities and NCIs
- Recognise the fair value of consideration received
- Recognise any distribution of shares to owners
- Reclassify to profit or loss any amounts (the entire amount, not a proportion) relating to the subsidiary’s assets and liabilities previously recognised in other comprehensive income, as if the assets and liabilities had been disposed of directly
- Recognise any resulting difference as a gain or loss in profit or loss attributable to the parent
- Recognise the fair value of any residual interest.

Example 4- Disposal to remain Associate

On 1 January 2008, Rage acquired a 90% interest in Machine, a public limited company, for a cash consideration of $80m. Machine's identifiable net assets had a fair value of $74m and the NCI had a fair value of $6m.

Rage uses the full goodwill method. On 31 December 2008, Rage disposed of 65% of the equity of Machine (no other investor obtained control as a result of the disposal) when its identifiable net assets were $83m.

Of the increase in net assets, $6m had been reported in profit or loss, and $3m had been reported in comprehensive income. The sale proceeds were $65m, and the remaining equity interest was fair valued at $25m. After the disposal, Machine is classified as an associate under IAS 28, *Investments in Associates*.

Solution 4

	$m	
Fair value of consideration	65	
Fair value of residual interest to be recognised as an associate	25	
Gain reported in comprehensive income	<u>3</u>	
	93	
Less net assets and goodwill derecognised:		
net assets	(83)	
goodwill (80 + 6 – 74)	<u>(12)</u>	
Loss on disposal to profit or loss	<u>(2)</u>	

After the sale of the interest, the holding in the associate will be fair valued at $25m.