Group Account Questions

1. On 1 October 2010 Prodigal purchased 75% of the equity shares in Sentinel. The acquisition was through a share exchange of two shares in Prodigal for every three shares in Sentinel. The stock market price of Prodigal's shares at 1 October 2010 was $4 per share.

The summarised statement of profit or loss and other comprehensive income for the two companies for the year ended 31 March 2011 are:

	Prodigal $'000	Sentinel $'000
Revenue	450,000	240,000
Cost of sales	(260,000)	(110,000)
Gross profit	190,000	130,000
Distribution costs	(23,600)	(12,000)
Administrative expenses	(27,000)	(23,000)
Finance costs	(1,500)	(1,200)
Profit before tax	137,900	93,800
Income tax expense	(48,000)	(27,800)
Profit for the year	89,900	66,000
Other comprehensive income		
Gain on revaluation of land (note (i))	2,500	1,000
Loss on fair value of equity financial asset investment	(700)	(400)
	1,800	600
Total comprehensive income	91,700	66,600

The following information for the equity of the companies at 1 April 2010 (i.e. before the share exchange took place) is available:

	$'000	$'000
Equity shares of $1 each	250,000	160,000
Share premium	100,000	nil
Revaluation reserve (land)	8,400	nil
Other equity reserve (re equity financial asset investment)	3,200	2,200
Retained earnings	90,000	125,000

The following information is relevant:

(i) Prodigal's policy is to revalue the group's land to market value at the end of each accounting period. Prior to its acquisition Sentinel's land had been valued at historical cost. During the post acquisition period Sentinel's land had increased in value over its value at the date of acquisition by $1 million. Sentinel has recognised the revaluation within its own financial statements.

(ii) Immediately after the acquisition of Sentinel on 1 October 2010, Prodigal transferred an item of plant with a carrying amount of $4 million to Sentinel at an agreed value of $5 million. At this date the plant had a remaining life of two and half years. Prodigal had included the profit on this transfer as a reduction in its depreciation costs. All depreciation is charged to cost of sales.

(iii) After the acquisition Sentinel sold goods to Prodigal for $40 million. These goods had cost Sentinel $30 million. $12 million of the goods sold remained in Prodigal's closing inventory.

(iv) Prodigal's policy is to value the non-controlling interest of Sentinel at the date of acquisition at its fair value which the directors determined to be $100 million.

(v) The goodwill of Sentinel has not suffered any impairment.

(vi) All items in the above statement of profit or loss and other comprehensive income are deemed to accrue evenly over the year unless otherwise indicated.

Required:

(a) (i) Prepare the consolidated statement of comprehensive income of Prodigal for the year ended 31 March 2011;

(ii) Prepare the equity section (including the non-controlling interest) of the consolidated statement of financial position of Prodigal as at 31 March 2011.

Note: you are NOT required to calculate consolidated goodwill or produce the statement of changes in equity. The following mark allocation is provided as guidance for this requirement:

(i) **15 marks**
(ii) **9 marks** (24 marks)

(b) IFRS 3 *Business combinations* permit a non-controlling interest at the date of acquisition to be valued by one of two methods:

(i) at its proportionate share of the subsidiary's identifiable net assets; or
(ii) at its fair value (usually determined by the directors of the parent company).

Required:

Explain the difference that the accounting treatment of these alternative methods could have on the consolidated financial statements, including where consolidated goodwill may be impaired.

(6 marks)
(30 marks)

2 Highveldt, a public listed company, acquired 75% of Samson's ordinary shares on 1 April 2004. Highveldt paid an immediate \$3·50 per share in cash and agreed to pay a further amount of \$108 million on 1 April 2005. Highveldt's cost of capital is 8% per annum. Highveldt has only recorded the cash consideration of \$3·50 per share.

The summarised statements of financial position of the two companies at 31 March 2005 are shown below:

	Highveldt		**Samson**	
	\$million	**\$million**	**\$million**	**\$million**
Tangible non-current assets (note (i))		420		320
Development costs (note (iv))		nil		40
Investments (note (ii))		300		20
		720		380
Current assets		133		91
Total assets		853		471
Equity and liabilities:				
Ordinary shares of \$1 each		270		80
Reserves:				
Share premium		80		40
Other reserve		45		nil
Retained earnings – 1 April 2004	160		134	
– year to 31 March 2005	190	350	76	210
		745		330
Non-current liabilities: 10% inter company loan (note (ii))		nil		60
Current liabilities		108		81
Total equity and liabilities		853		471

The following information is relevant:

(i) Highveldt has a policy of revaluing land and buildings to fair value. At the date of acquisition Samson's land and buildings had a fair value $20 million higher than their book value and at 31 March 2005 this had increased by a further $4 million (ignore any additional depreciation).

(ii) Included in Highveldt's investments is a loan of $60 million made to Samson at the date of acquisition. Interest is payable annually in arrears. Samson paid the interest due for the year on 31 March 2005, but Highveldt did not receive this until after the year end. Highveldt has not accounted for the accrued interest from Samson.

(iii) Samson had established a line of products under the brand name of Titanware. Acting on behalf of Highveldt, a firm of specialists, had valued the brand name at a value of $40 million with an estimated life of 10 years as at 1 April 2004. The brand is not included in Samson's statement of financial position.

(iv) Samson's development project was completed on 30 September 2004 at a cost of $50 million. $10 million of this had been amortised by 31 March 2005. Development costs capitalised by Samson at the date of acquisition were $18 million. Highveldt's directors are of the opinion that Samson's development costs do not meet the criteria in IAS 38 'Intangible Assets' for recognition as an asset.

(v) Samson sold goods to Highveldt during the year at a profit of $6 million, one-third of these goods were still in the inventory of Highveldt at 31 March 2005.

(vi) An impairment test at 31 March 2005 on the consolidated goodwill concluded that it should be written down by $20 million. No other assets were impaired.

(vii) The fair value of non-controlling interest at the date of acquisition was $100 million.

Required:

(a) Prepare consolidated statement of financial position of Highveldt at 31 March 2005: 20 marks

(b) Explain why consolidated financial statements are useful to the users of financial statements (as opposed to just the parent company's separate (entity) financial statements). 10 marks

(30 marks)

3 Hostelling purchased the following equity investments:

On 1 October 2005: 80% of the issued share capital of Sunlee. The acquisition was through a share exchange of three shares in Hosterling for every five shares in Sunlee. The market price of Hosterling's shares at 1 October 2005 was $5 per share.

On 1 July 2006: 6 million shares in Amber paying $3 per share in cash and issuing to Amber's shareholders 6% (actual and effective rate) loan notes on the basis of $100 loan note for every 100 shares acquired.

The summarised statement of profit or loss for the three companies for the year ended 30 September 2006 are:

	Hosterling	**Sunlee**	**Amber**
	$'000	**$'000**	**$'000**
Revenue	105,000	62,000	50,000
Cost of sales	(68,000)	(36,500)	(61,000)
Gross profit/(loss)	37,000	25,500	(11,000)
Other income (note (i))	400	nil	nil
Distribution costs	(4,000)	(2,000)	(4,500)
Administrative expenses	(7,500)	(7,000)	(8,500)
Finance costs	(1,200)	(900)	nil
Profit/(loss) before tax	24,700	15,600	(24,000)
Income tax (expense)/credit	(8,700)	(2,600)	4,000
Profit/(loss) for the period	16,000	13,000	(20,000)

The following information is relevant:

(i) The other income is a dividend received from Sunlee on 31 March 2006.

(ii) The details of Sunlee's and Amber's share capital and reserves at 1 October 2005 were:

	Sunlee	**Amber**
	$'000	$'000
Equity shares of $1 each	20,000	15,000
Retained earnings	18,000	35,000

(iii) A fair value exercise was carried out at the date of acquisition of Sunlee with the following results:

	carrying amount	**fair value**	**remaining life (straight line)**
	$'000	$'000	
Intellectual property	18,000	22,000	still in development
Land	17,000	20,000	not applicable
Plant	30,000	35,000	five years

The fair values have not been reflected in Sunlee's financial statements. Plant depreciation is included in cost of sales. No fair value adjustments were required on the acquisition of Amber.

(iv) In the year ended 30 September 2006 Hosterling sold goods to Sunlee at a selling price of $18 million. Hosterling made a profit of cost plus 25% on these sales. $7·5 million (at cost to Sunlee) of these goods were still in the inventories of Sunlee at 30 September 2006.

(v) Impairment tests for both Sunlee and Amber were conducted on 30 September 2006. They concluded that the goodwill of Sunlee should be written down by $1·6 million and, due to its losses since acquisition, the investment in Amber was worth $21·5 million.

(v). All trading profits and losses are deemed to accrue evenly throughout the year.

(vi).The fair value of non-controlling interest at the date of acquisition was $12 million.

Required:

(a) Calculate the goodwill arising on the acquisition of Sunlee at 1 October 2005. (7 marks)

(b) Calculate the carrying amount of the investment in Amber at 30 September 2006 under the equity method prior to the impairment test. (6 marks)

(c) Prepare the consolidated income statement for the Hosterling Group for the year ended 30 September 2006. (17 marks)

(30 marks)

4 Holdrite purchased 75% of the issued share capital of Staybrite and 40% of the issued share capital of Allbrite on 1 April 2004.

Details of the purchase consideration given at the date of purchase are:

Staybrite: a share exchange of 2 shares in Holdrite for every 3 shares in Staybrite plus an issue to the shareholders of Staybrite 8% loan notes redeemable at par on 30 June 2006 on the basis of $100 loan note for every 250 shares held in Staybrite.

Allbrite: a share exchange of 3 shares in Holdrite for every 4 shares in Allbrite plus $1 per share acquired in cash.

The market price of Holdrite's shares at 1 April 2004 was $6 per share.

The summarised statements of profit or loss for the three companies for the year to 30 September 2004 are:

	Holdrite $000	Staybrite $000	Allbrite $000
Revenue	75,000	40,700	31,000
Cost of Sales	(47,400)	(19,700)	(15,300)
Gross Profit	27,600	21,000	15,700
Operating expenses	(10,480)	(9,000)	(9,700)
Operating Profit	17,120	12,000	6,000
Interest expense	(170)		
Profit before tax	16,950	12,000	6,000
Income tax expense	4,800)	(3,000)	(2,000)
Profit for period	12,150	9,000	4,000

The following information is relevant:

(i) A fair value exercise was carried out for Staybrite at the date of its acquisition with the following results:

	Book Value $000	Fair Value $000
Land	20,000	23,000
Plant	25,000	30,000

The fair values have not been reflected in Staybrite's financial statements. The increase in the fair value of the plant would create additional depreciation of $500,000 in the post acquisition period in the consolidated financial statements to 30 September 2004. Depreciation on plant is charged to cost of sales.

(ii) The details of each company's share capital and reserves at 1 October 2003 are:

	Holdrite $000	Staybrite $000	Allbrite $000
Equity shares of $1 each	20,000	10,000	5,000
Share premium	5,000	4,000	2,000
Retained profits	18,000	7,500	6,000

(iii) In the post-acquisition period Holdrite sold goods to Staybrite for $10 million. Holdrite made a profit of $4 million on these sales. One-quarter of these goods were still in the inventory of Staybrite at 30 September 2004.

(iv). Impairment tests on the goodwill of Staybrite and Allbrite at 30 September 2004 resulted in the need to write-down Staybrite's goodwill by $800,000. Allbrite's goodwill was not impaired.

(v) Holdrite paid a dividend of $5 million on 20 September 2004.

(vi)The fair value of NCI at the date of acquisition was $11million.

Required:

(a) Calculate the goodwill arising on the purchase of the shares in both Staybrite and Allbrite at 1 April 2004. (10 marks)

(b) Prepare a consolidated income statement for the Holdrite Group for the year to 30 September 2004. (17 marks)

(c) Show the movement on the consolidated retained profits attributable to Holdrite for the year to 30 September 2004. (3 marks) **(30 marks)**

5 Hedra, a public listed company, acquired the following investments:

(i) On 1 October 2004, 72 million shares in Salvador for an immediate cash payment of $195 million. Hedra agreed to pay further consideration on 30 September 2005 of $49 million if the post acquisition profits of Salvador exceeded an agreed figure at that date. Hedra has not accounted for this deferred payment as it did not believe it would be payable, however Salvador's profits have now exceeded the agreed amount (ignore discounting). Salvador also accepted a $50 million 8% loan from Hedra at the date of its acquisition.

(ii) On 1 April 2005, 40 million shares in Aragon by way of a share exchange of two shares in Hedra for each acquired share in Aragon. The stock market value of Hedra's shares at the date of this share exchange was $2·50. Hedra has not yet recorded the acquisition of the investment in Aragon.

The summarised statements of financial position of the three companies as at 30 September 2005 are:

	Hedra		Salvador		Aragon	
Non-current Assets	$m	$m	$m	$m	$m	$m
Property, plant and equipment		358		240		270
Investments – in Salvador		245		nil		nil
– other		45		nil		nil
		648		240		270
Current Assets						
Inventories	130		80		110	
Trade receivables	142		97		70	
Cash and bank	nil	272	4	181	20	200
Total assets		920		421		470
Equity and liabilities						
Ordinary share capital ($1 each)		400		120		100
Reserves:						
Share premium	40		50		nil	
Other Reserves	15		nil		nil	
Retained earnings	240	295	60	110	300	300
		695		230		400
Non-current liabilities						
8% loan note		nil		50		nil
Deferred tax	45	45	nil	50	nil	nil
Current liabilities						
Trade payables	118		141		40	
Bank overdraft	12		nil		nil	
Current tax payable	50	180	nil	141	30	70
Total equity and liabilities		920		421		470

The following information is relevant:

(a) Fair value adjustments and revaluations:

(i) Hedra's accounting policy for land and buildings is that they should be carried at their fair values. The fair value of Salvador's land at the date of acquisition was $20 million in excess of its carrying value. By 30 September 2005 this excess had increased by a further $5 million. Salvador's buildings did not require any fair value adjustments. The fair value of Hedra's own land and buildings at 30 September 2005 was $12 million in excess of its carrying value in the above statement of financial position.

(ii) The fair value of some of Salvador's plant at the date of acquisition was $20 million in excess of its carrying value and had a remaining life of four years (straight-line depreciation is used).

(iii) At the date of acquisition Salvador had unrelieved tax losses of $40 million from previous years. Salvador had not accounted for these as a deferred tax asset as its directors did not believe the

company would be sufficiently profitable in the near future. However, the directors of Hedra were confident that these losses would be utilised and accordingly they should be recognised as a deferred tax asset. By 30 September 2005 the group had not yet utilised any of these losses. The income tax rate is 25%.

(b) The retained earnings of Salvador and Aragon at 1 October 2004, as reported in their separate financial statements, were $20 million and $200 million respectively. All profits are deemed to accrue evenly throughout the year.

(c) An impairment test on 30 September 2005 showed that consolidated goodwill should be written down by $20 million. Hedra has applied IFRS 3 *Business combinations* since the acquisition of Salvador.

(d) The fair value of non-controlling interest at the date of acquisition was $56million

(e) The investment in Aragon has not suffered any impairment.

Required:
Prepare the statement of financial position of Hedra as at 30 September 2005. (30 marks)

6 Parentis, a public listed company, acquired 600 million equity shares in Offspring on 1 April 2006. The purchase consideration was made up of a share exchange of one share in Parentis for two shares in Offspring the issue of $100 10% loan note for every 500 shares acquired; and a deferred cash payment of 11 cents per share acquired payable on 1 April 2007.

Parentis has only recorded the issue of the loan notes. The value of each Parentis share at the date of acquisition was 75 cents and Parentis has a cost of capital of 10% per annum.

The statements of financial position of the two companies at 31 March 2007 are shown below:

	Parentis		**Offspring**	
	$ million	**$ million**	**$ million**	**$ million**
Assets				
Property, plant and equipment (note (i))		640		340
Investments		120		nil
Intellectual property (note (ii))		nil		30
		760		370
Current assets				
Inventory (note (iii))	76		22	
Trade receivables (note (iii))	84		44	
Bank	nil	160	4	70
Total assets		920		440
Equity and liabilities				
Equity shares of 25 cents each		300		200
Retained earnings – 1 April 2006	210		120	
– year ended 31 March 2007	90	300	20	140
		600		340
Non-current liabilities				
10% loan notes		120		20
Current liabilities				
Trade payables (note (iii))	130		57	
Current tax payable	45		23	
Overdraft	25	200	nil	80
Total equity and liabilities		920		440

The following information is relevant:

(i) At the date of acquisition the fair values of Offspring's net assets were approximately equal to their carrying amounts with the exception of its properties. These properties had a fair value of $40 million in excess of their carrying amounts which would create additional depreciation of $2 million in the post acquisition period to 31 March 2007. The fair values have not been reflected in Offspring's statement of financial position.

(ii) The intellectual property is a system of encryption designed for internet use. Offspring has been advised that government legislation (passed since acquisition) has now made this type of encryption illegal. Offspring will receive $10 million in compensation from the government.

(iii) Offspring sold Parentis goods for $15 million in the post acquisition period. $5 million of these goods are included in the inventory of Parentis at 31 March 2007. The profit made by Offspring on these sales was $6 million. Offspring's trade payable account (in the records of Parentis) of $7 million does not agree with Parentis's trade receivable account (in the records of Offspring) due to cash in transit of $4 million paid by Parentis.

(iv) Due to the impact of the above legislation, Parentis has concluded that the consolidated goodwill has been impaired by $27 million.

(v) Parentis's policy is to value the non-controlling interest at fair value at the date of acquisition. The amount for this purpose was $30 million.

Required: **Prepare the statement of financial position of Parentis as at 31 March 2007.**

(30 marks)

7. On 1 April 2009 Picant acquired 75% of Sander's equity shares in a share exchange of three shares in Picant for every two shares in Sander. The market prices of Picant's and Sander's shares at the date of acquisition were $3·20 and $4·50 respectively.

In addition to this Picant agreed to pay a further amount on 1 April 2010 that was contingent upon the post-acquisition performance of Sander. At the date of acquisition Picant assessed the fair value of this contingent consideration at $4·2 million, but by 31 March 2010 it was clear that the actual amount to be paid would be only $2·7 million (ignore discounting). Picant has recorded the share exchange and provided for the initial estimate of $4·2 million for the contingent consideration.

On 1 October 2009 Picant also acquired 40% of the equity shares of Adler paying $4 in cash per acquired share and issuing at par one $100 7% loan note for every 50 shares acquired in Adler. This consideration has also been recorded by Picant.
Picant has no other investments.

The summarised statements of financial position of the three companies at 31 March 2010 are:

	Picant	**Sander**	**Adler**
Assets	**$'000**	**$'000**	**$'000**
Non-current assets			
Property, plant and equipment	37,500	24,500	21,000
Investments	45,000	nil	nil
	82,500	24,500	21,000
Current assets			
Inventory	10,000	9,000	5,000
Trade receivables	6,500	1,500	3,000
Total assets	99,000	35,000	29,000
Equity and liabilities			
Equity			
Equity shares of $1 each	25,000	8,000	5,000
Share premium	19,800	nil	nil

Retained earnings – at 1 April 2009	16,200	16,500	15,000
– for the year ended 31 March 2010	11,000	1,000	6,000
	72,000	25,500	26,000
Non-current liabilities			
7% loan notes	14,500	2,000	nil
Current liabilities			
Contingent consideration	4,200	nil	nil
Other current liabilities	8,300	7,500	3,000
Total equity and liabilities	99,000	35,000	29,000

The following information is relevant:

(i) At the date of acquisition the fair values of Sander's property, plant and equipment was equal to its carrying amount with the exception of Sander's factory which had a fair value of $2 million above its carrying amount. Sander has not adjusted the carrying amount of the factory as a result of the fair value exercise. This requires additional annual depreciation of $100,000 in the consolidated financial statements in the post-acquisition period.

Also at the date of acquisition, Sander had an intangible asset of $500,000 for software in its statement of financial position. Picant's directors believed the software to have no recoverable value at the date of acquisition and Sander wrote it off shortly after its acquisition.

(ii) At 31 March 2010 Picant's current account with Sander was $3·4 million (debit). This did not agree with the equivalent balance in Sander's books due to some goods-in-transit invoiced at $1·8 million that were sent by Picant on 28 March 2010, but had not been received by Sander until after the year end. Picant sold all these goods at cost plus 50%.

(iii) Picant's policy is to value the non-controlling interest at fair value at the date of acquisition. For this purpose Sander's share price at that date can be deemed to be representative of the fair value of the shares held by the non-controlling interest.

(iv) Impairment tests were carried out on 31 March 2010 which concluded that the value of the investment in Adler was not impaired but, due to poor trading performance, consolidated goodwill was impaired by $3·8 million.

(v) Assume all profits accrue evenly through the year.

Required:

(a) Prepare the consolidated statement of financial position for Picant as at 31 March 2010. (25 marks)

(b) Picant has been approached by a potential new customer, Trilby, to supply it with a substantial quantity of goods on three months credit terms. Picant is concerned at the risk that such a large order represents in the current difficult economic climate, especially as Picant's normal credit terms are only one month's credit. To support its application for credit, Trilby has sent Picant a copy of Tradhat's most recent audited consolidated financial statements. Trilby is a wholly-owned subsidiary within the Tradhat group. Tradhat's consolidated financial statements show a strong statement of financial position including healthy liquidity ratios.

Required:
Comment on the importance that Picant should attach to Tradhat's consolidated financial statements when deciding on whether to grant credit terms to Trilby. (5 marks)

(30 marks)

8. On 1 April 2009 Pandar purchased 80% of the equity shares in Salva. The acquisition was through a share exchange of three shares in Pandar for every five shares in Salva. The market prices of Pandar's and Salva's shares at 1 April 2009 were $6 per share and $3.20 respectively.

On the same date Pandar acquired 40% of the equity shares in Ambra paying $2 per share.

The summarised statement of profit or loss for the three companies for the year ended 30 September 2009 are:

	Pandar	Salva	Ambra
	$'000	$'000	$'000
Revenue	210,000	150,000	50,000
Cost of sales	(126,000)	(100,000)	(40,000)
Gross profit	84,000	50,000	10,000
Distribution costs	(11,200)	(7,000)	(5,000)
Administrative expenses	(18,300)	(9,000)	(11,000)
Investment income (interest and dividends)	9,500	-	-
Finance costs	(1,800)	(3,000)	nil
Profit (loss) before tax	62,200	31,000	(6,000)
Income tax (expense) relief	(15,000)	(10,000)	1,000
Profit (loss) for the year	47,200	21,000	(5,000)

The following information for the equity of the companies at 30 September 2009 is available:

Equity shares of $1 each	200,000	120,000	40,000
Share premium	300,000	nil	nil
Retained earnings 1 October 2008	40,000	152,000	15,000
Profit (loss) for the year ended 30 September 2009	47,200	21,000	(5,000)
Dividends paid (26 September 2009)	nil	(8,000)	nil

The following information is relevant:

(i) The fair values of the net assets of Salva at the date of acquisition were equal to their carrying amounts with the exception of an item of plant which had a carrying amount of $12 million and a fair value of $17 million. This plant had a remaining life of five years (straight-line depreciation) at the date of acquisition of Salva. All depreciation is charged to cost of sales.

In addition Salva owns the registration of a popular internet domain name. The registration, which had a negligible cost, has a five year remaining life (at the date of acquisition); however, it is renewable indefinitely at a nominal cost. At the date of acquisition the domain name was valued by a specialist company at $20 million.

The fair values of the plant and the domain name have not been reflected in Salva's financial statements.

No fair value adjustments were required on the acquisition of the investment in Ambra.

(ii) Immediately after its acquisition of Salva, Pandar invested $50 million in an 8% loan note from Salva. All interest accruing to 30 September 2009 had been accounted for by both companies. Salva also has other loans in issue at 30 September 2009.

(iii) Pandar has credited the whole of the dividend it received from Salva to investment income.

(iv) After the acquisition, Pandar sold goods to Salva for $15 million on which Pandar made a gross profit of 20%.Salva had one third of these goods still in its inventory at 30 September 2009. There are no intra-group current account balances at 30 September 2009.

(v) The non-controlling interest in Salva is to be valued at its (full) fair value at the date of acquisition. For this purpose Salva's share price at that date can be taken to be indicative of the fair value of the shareholding of the non-controlling interest.

(vi) The goodwill of Salva has not suffered any impairment; however, due to its losses, the value of Pandar's investment in Ambra has been impaired by $3 million at 30 September 2009.

(vii) All items in the above statement of profit or loss are deemed to accrue evenly over the year unless otherwise indicated.

Required:

(a) (i) Calculate the goodwill arising on the acquisition of Salva at 1 April 2009; (6 marks)

(ii) Calculate the carrying amount of the investment in Ambra to be included within the consolidated statement of financial position as at 30 September 2009. (4 marks)

(b) Prepare the consolidated income statement for the Pandar Group for the year ended 30 September 2009. (20 marks)

(30 marks)

9. Below are the summarised statements of financial position for three companies as at 31 March 2009:

	Pacemaker		Syclop		Vardine	
Assets	**$ million**	**$ million**	**$ million**	**$ million**	**$ million**	**$ million**
Non-current assets						
Property, plant and equipment		520		280		240
Investments		345		40		nil
		865		320		240
Current assets						
Inventory	142		160		120	
Trade receivables	95		88		50	
Cash and bank	8	245	22	270	10	180
Total assets		1,110		590		420
Equity and liabilities						
Equity shares of $1each		500		145		100
Share premium	100		nil		nil	
Retained earnings	130	230	260	260	240	240
		730		405		340
Non-current liabilities						
10% loan notes		180		20		nil
Current liabilities		200		165		80
Total equity and liabilities		1,110		590		420

Notes:

Pacemaker is a public listed company that acquired the following investments:

(i) Investment in Syclop

On 1 April 2007 Pacemaker acquired 116 million shares in Syclop for an immediate cash payment of $210 million and issued at par one 10% $100 loan note for every 200 shares acquired. Syclop's retained earnings at the date of acquisition were $120 million.

(ii) Investment in Vardine

On 1 October 2008 Pacemaker acquired 30 million shares in Vardine in exchange for 75 million of its own shares. The stock market value of Pacemaker's shares at the date of this share exchange was $1·60 each. Pacemaker has not yet recorded the investment in Vardine.

(i) Pacemaker's other investments, and those of Syclop, are financial assets measured at fair value through profit and loss which are carried at their fair values as at 31 March 2008. The fair value of these investments at 31 March 2009 is $82 million and $37 million respectively.

Other relevant information:

(ii) Pacemaker's policy is to value non-controlling interests at their fair values. The directors of Pacemaker assessed the fair value of the non-controlling interest in Syclop at the date of acquisition to be $65 million.

There has been no impairment to goodwill or the value of the investment in Vardine.

(v) At the date of acquisition of Syclop owned a recently built property that was carried at its (depreciated) construction cost of $62 million. The fair value of this property at the date of acquisition was $82 million and it had an estimated remaining life of 20 years.

For many years Syclop has been selling some of its products under the brand name of 'Kyklop'. At the date of acquisition the directors of Pacemaker valued this brand at $25 million with a remaining life of 10 years. The brand is not included in Syclop's statement of financial position.

The fair value of all other identifiable assets and liabilities of Syclop were equal to their carrying values at the date of its acquisition.

(vi) The inventory of Syclop at 31 March 2009 includes goods supplied by Pacemaker for $56 million (at selling price from Pacemaker). Pacemaker adds a mark-up of 40% on cost when selling goods to Syclop. There are no intra-group receivables or payables at 31 March 2009.

(vii) Vardine's profit is subject to seasonal variation. Its profit for the year ended 31 March 2009 was $100 million. $20 million of this profit was made from 1 April 2008 to 30 September 2008.

(viii) None of the companies have paid any dividends for many years.

Required:

Prepare the consolidated statement of financial position of Pacemaker as at 31 March 2009.
(30 marks)

10. On 1 June 2010, Premier acquired 80% of the equity share capital of Sanford. The consideration consisted of two elements: a share exchange of three shares in Premier for every fi ve acquired shares in Sanford and the issue of a $100 6% loan note for every 500 shares acquired in Sanford. The share issue has not yet been recorded by Premier, but the issue of the loan notes has been recorded. At the date of acquisition shares in Premier had a market value of $5 each and the shares of Sanford had a stock market price of $3·50 each. Below are the summarised draft financial statements of both companies.

Statement of profit or loss and other comprehensive income for the year ended 30 September 2010

	Premier	**Sanford**
	$'000	**$'000**
Revenue	92,500	45,000
Cost of sales	(70,500)	(36,000)
Gross profit	22,000	9,000
Distribution costs	(2,500)	(1,200)
Administrative expenses	(5,500)	(2,400)
Finance costs	(100)	nil
Profit before tax	13,900	5,400
Income tax expense	(3,900)	(1,500)
Profit for the year	10,000	3,900
Other comprehensive income:		
Gain on revaluation of land (note (i))	500	nil
Total comprehensive income	10,500	3,900

Statements of financial position as at 30 September 2010

Assets		
Non-current assets		
Property, plant and equipment	25,500	13,900
Investments	1,800	nil
	27,300	13,900
Current assets	12,500	2,400
Total assets	39,800	16,300
Equity and liabilities		
Equity		
Equity shares of $1 each	12,000	5,000
Land revaluation reserve – 30 September 2010 (note (i))	2,000	nil
Other equity reserve – 30 September 2009 (note (iv))	500	nil
Retained earnings	12,300	4,500
	26,800	9,500
Non-current liabilities		
6% loan notes	3,000	nil
Current liabilities	10,000	6,800
Total equity and liabilities	39,800	16,300

The following information is relevant:

(i) At the date of acquisition, the fair values of Sanford's assets were equal to their carrying amounts with the exception of its property. This had a fair value of $1·2 million below its carrying amount. This would lead to a reduction of the depreciation charge (in cost of sales) of $50,000 in the post-acquisition period. Sanford has not incorporated this value change into its entity financial statements. Premier's group policy is to revalue all properties to current value at each year end. On 30 September 2010, the value of Sanford's property was unchanged from its value at acquisition, but the land element of Premier's property had increased in value by $500,000 as shown in other comprehensive income.

(ii) Sales from Sanford to Premier throughout the year ended 30 September 2010 had consistently been $1 million per month. Sanford made a mark-up on cost of 25% on these sales. Premier had $2 million (at cost to Premier) of inventory that had been supplied in the post-acquisition period by Sanford as at 30 September 2010.

(iii) Premier had a trade payable balance owing to Sanford of $350,000 as at 30 September 2010. This agreed with the corresponding receivable in Sanford's books.

(iv) Premier's investments include some available-for-sale investments that have increased in value by $300,000 during the year. The other equity reserve relates to these investments and is based on their value as at 30 September 2009. There were no acquisitions or disposals of any of these investments during the year ended 30 September 2010.

(v) Premier's policy is to value the non-controlling interest at fair value at the date of acquisition. For this purpose Sanford's share price at that date can be deemed to be representative of the fair value of the shares held by the non-controlling interest.

(vi) There has been no impairment of consolidated goodwill.

Required:

(a) Prepare the consolidated statement of comprehensive income for Premier for the year ended 30 September 2010.

(b) Prepare the consolidated statement of financial position for Premier as at 30 September 2010.

The following mark allocation is provided as guidance for this question:
(a) 13 marks
(b) 17 marks **(30 marks)**

11. On 1 October 2010, Paladin secured a majority equity shareholding in Saracen on the following terms:
an immediate payment of $4 per share on 1 October 2010; and
a further amount deferred until 1 October 2011 of $5·4 million.

The immediate payment has been recorded in Paladin's financial statements, but the deferred payment has not been recorded. Paladin's cost of capital is 8% per annum. On 1 February 2011, Paladin also acquired 25% of the equity shares of Augusta paying $10 million in cash. The summarised statements of financial position of the three companies at 30 September 2011 are:

	Paladin	Saracen	Augusta
Assets	$'000	$'000	$'000
Non-current assets			
Property, plant and equipment	40,000	31,000	30,000
Intangible assets	7,500		
Investments – Saracen (8 million shares at $4 each)	32,000		
– Augusta	10,000	nil	nil
	89,500	31,000	30,000
Current assets			
Inventory	11,200	8,400	10,000
Trade receivables	7,400	5,300	5,000
Bank	3,400	nil	2,000
Total assets	111,500	44,700	47,000
Equity and liabilities			
Equity			
Equity shares of $1 each	50,000	10,000	10,000
Retained earnings – at 1 October 2010	25,700	12,000	31,800
– for year ended 30 September 2011	9,200	6,000	1,200
	84,900	28,000	43,000
Non-current liabilities			
Deferred tax	15,000	8,000	1,000
Current liabilities			
Bank	nil	2,500	nil
Trade payables	11,600	6,200	3,000
Total equity and liabilities	111,500	44,700	47,000

The following information is relevant:

(i) Paladin's policy is to value the non-controlling interest at fair value at the date of acquisition. For this purpose the directors of Paladin considered a share price for Saracen of $3·50 per share to be appropriate.

(ii) At the date of acquisition, the fair values of Saracen's property, plant and equipment was equal to its carrying amount with the exception of Saracen's plant which had a fair value of $4 million above its carrying amount. At that date the plant had a remaining life of four years. Saracen uses straight-line depreciation for plant assuming a nil residual value.

Also at the date of acquisition; Paladin valued Saracen's customer relationships as a customer base intangible asset at fair value of $3 million. Saracen has not accounted for this asset. Trading relationships with Saracen's customers last on average for six years.

(iii) At 30 September 2011, Saracen's inventory included goods bought from Paladin (at cost to Saracen) of

$2·6 million. Paladin had marked up these goods by 30% on cost. Paladin's agreed current account balance owed by Saracen at 30 September 2011 was $1·3 million.

(iv) Impairment tests were carried out on 30 September 2011 which concluded that consolidated goodwill was not impaired, but, due to disappointing earnings, the value of the investment in Augusta was impaired by $2·5 million.

(v) Assume all profits accrue evenly through the year.

Required:
Prepare the consolidated statement of financial position for Paladin as at 30 September 2011.
(30 marks)

12. (a) On 1 October 2012, Paradigm acquired 75% of Strata's equity shares by means of a share exchange of two new shares in Paradigm for every five acquired shares in Strata. In addition, Paradigm issued to the shareholders of Strata a $100 10% loan note for every 1,000 shares it acquired in Strata. Paradigm has not recorded any of the purchase consideration, although it does have other 10% loan notes already in issue.

The market value of Paradigm's shares at 1 October 2012 was $2 each.

The summarised statements of financial position of the two companies as at 31 March 2013 are:

	Paradigm	Strata
Assets	$'000	$'000
Non-current assets		
Property, plant and equipment	47,400	25,500
Financial asset: equity investments (notes (i) and (iv))	7,500	3,200
	54,900	28,700
Current assets		
Inventory (note (ii))	20,400	8,400
Trade receivables (note (iii))	14,800	9,000
Bank	2,100	nil
Total assets	92,200	46,100
Equity and liabilities		
Equity		
Equity shares of $1 each	40,000	20,000
Retained earnings/(losses) – at 1 April 2012	19,200	(4,000)
– for year ended 31 March 2013	7,400	8,000
	66,600	24,000
Non-current liabilities		
10% loan notes	8,000	nil
Current liabilities		
Trade payables (note (iii))	17,600	13,000
Bank overdraft	nil	9,100
Total equity and liabilities	92,200	46,100

The following information is relevant:

(i) At the date of acquisition, Strata produced a draft statement of profit or loss which showed it had made a net loss after tax of $2 million at that date. Paradigm accepted this figure as the basis for calculating the pre- and post-acquisition split of Strata's profit for the year ended 31 March 2013.

Also at the date of acquisition, Paradigm conducted a fair value exercise on Strata's net assets which were equal to their carrying amounts (including Strata's financial asset equity investments) with the exception of an

item of plant which had a fair value of $3 million below its carrying amount. The plant had a remaining economic life of three years at 1 October 2012.

Paradigm's policy is to value the non-controlling interest at fair value at the date of acquisition. For this purpose, a share price for Strata of $1·20 each is representative of the fair value of the shares held by the non-controlling interest.

(ii) Each month since acquisition, Paradigm's sales to Strata were consistently $4·6 million. Paradigm had marked these up by 15% on cost. Strata had one month's supply ($4·6 million) of these goods in inventory at 31 March 2013. Paradigm's normal mark-up (to third party customers) is 40%.

(iii) Strata's current account balance with Paradigm at 31 March 2013 was $2·8 million, which did not agree with Paradigm's equivalent receivable due to a payment of $900,000 made by Strata on 28 March 2013, which was not received by Paradigm until 3 April 2013.

(iv) The financial asset equity investments of Paradigm and Strata are carried at their fair values as at 1 April 2012. As at 31 March 2013, these had fair values of $7·1 million and $3·9 million respectively.

(v) There were no impairment losses within the group during the year ended 31 March 2013.

Required:
Prepare the consolidated statement of financial position for Paradigm as at 31 March 2013. (20 marks)

(b) Paradigm has a strategy of buying struggling businesses, reversing their decline and then selling them on at a profit within a short period of time. Paradigm is hoping to do this with Strata.

Required:
As an adviser to a prospective purchaser of Strata, explain any concerns you would raise about basing an investment decision on the information available in Paradigm's consolidated financial statements and Strata's entity financial statements. (5 marks)

(30 marks)