CHAPTER 10

CONSOLIDATED FINANCIAL STATEMENTS

LEARNING OUTCOMES

After studying this chapter, you will be able to:

- Understand the concepts of Group, holding company and subsidiary company.
- Apply the consolidation procedures for consolidation of financial statements of subsidiaries with the holding companies.
- Prepare the consolidated financial statements and solve related problems.

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CHAPTER OVERVIEW

- Concept of Group, Holding Company and Subsidiary Company
- Purpose and method of preparing consolidated financial statements
- Components of Consolidated Financial Statements
- Calculation of Goodwill/ Capital Reserve
- Minority Interests; Profit or Loss of Subsidiary Company
- Elimination of Intra-Group Transactions and other Adjustments

1 CONCEPT OF GROUP, HOLDING COMPANY AND SUBSIDIARY COMPANY

In an era of business growth, many organizations are growing into large corporations by the process of acquisition, mergers, gaining control by one company over the other company, restructuring etc. Acquisitions and mergers ultimately lead 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.

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Group of companies

Many a times, a company expands by keeping intact its separate corporate identity. In this situation, a company (i.e. holding company) gains control over the other company (subsidiary company). This control is exercised by one company over the other by-

1. Purchasing specified number of shares i.e. ownership through voting power of that company or
2. Exercising control over the board of directors.

The companies connected in these ways are collectively called as a **Group of Companies.**

Holding Company and Subsidiary Company have also been defined in Section 2 of the Companies Act, 2013.

Holding company

As per Section 2(46) of the Companies Act, 2013,

"Holding company", in relation to one or more other companies, means a company of which such companies are subsidiary companies.

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's accounts need financial information of subsidiaries also to understand the performance and financial position of the group (i.e. holding company and subsidiaries on a combined basis).

Subsidiary Company

Section 2(87) of the Companies Act, 2013 defines "subsidiary company" as a company in which the holding company -

(i) controls the composition of the Board of Directors; or

(ii) exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies:

A company shall be deemed to be a subsidiary company of the holding company even if there is indirect control through the subsidiary company (ies).

The control over the composition of a subsidiary company's Board of Directors means exercise of power to appoint or remove all or a majority of the directors of the subsidiary company.

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Total share capital, as mentioned in section 2(87) (ii) above, has been further clarified by the Rule 2(1)(r) of the Companies (Specification of Definitions Details) Rules, 2016. As per the Rule, total share capital includes

(a) paid up equity share capital; and

(b) convertible preference share capital.

Section 19 of the Companies Act, 2013 prohibits a subsidiary company from holding shares in the holding company. According to this section, no company shall, either by itself or through its nominees, hold any shares in its holding company and no holding company shall allot or transfer its shares to any of its subsidiary companies and any such allotment or transfer of shares of a company to its subsidiary company shall be void.

However, a subsidiary may continue to be a member of its holding company when

(a) the subsidiary company holds such shares as the legal representative of a deceased member of the holding company; or

(b) the subsidiary company holds such shares as a trustee; or

(c) the subsidiary company is a shareholder even before it became a subsidiary company of the holding company.

The subsidiary company shall have a right to vote at a meeting of the holding company only in respect of the shares held by it as a legal representative or as a trustee, as mentioned above in point (a) and (b).

Definitions as per Accounting Standard (AS) 21

Control:

(a) the ownership, directly or indirectly through subsidiary(ies), of more than one-half of the voting power of an enterprise; or

(b) control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise so as to obtain economic benefits from its activities.

Subsidiary is an enterprise that is controlled by another enterprise (known as the parent).

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

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2 WHOLLY OWNED AND PARTLY OWNED SUBSIDIARIES

S.No.	Wholly owned subsidiary company	Partly owned subsidiary company
1.	A wholly owned subsidiary company is one in which all the shares are owned by the holding company.	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.
2.	100% voting rights are vested by the holding company.	Voting rights of more than 50% but less than 100% are vested by the holding company.
3.	There is no minority interest because all the shares with voting rights are held by the holding company.	There is a minority interest because less than 50% shares with voting rights are held by outsiders other than the holding company.

3 PURPOSE OF PREPARING THE CONSOLIDATED FINANCIAL STATEMENTS

Consolidated financial statements (CFS) 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.

CFS are intended to show the financial position of the group as a whole - by showing the economic resources controlled by them, by presenting the obligations of the group and the results the group achieves with its resources.

CFS normally include consolidated balance sheet, consolidated statement of profit and loss, and notes, other statements and explanatory material that form an integral part thereof. Consolidated cash flow statement is presented in case a parent presents its own cash flow statement. The consolidated financial statements

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

[**Section 129(3) of the Companies Act 2013**]

Where a company has one or more subsidiaries or associate companies, it shall, in addition to the standalone financial statements, prepare a consolidated financial statement of the company and of all the subsidiaries and associate companies in the same form and manner as that of its own and in accordance with applicable accounting standards, which shall also be laid before the annual general meeting (AGM) of the company along with the laying of its financial statement.

The company shall also attach along with its financial statement, a separate statement containing the salient features of the financial statement of its subsidiary or subsidiaries in Form AOC-1 as per Rule 5 of the Companies (Accounts) Rules, 2014.

For the purpose of section 129, 'subsidiary' includes 'associate company' and 'joint venture' which means that the company would be required to prepare consolidated financial statements including associate/ joint venture even if there is no subsidiary of a company.

The consolidation of financial statements of the company shall be made in accordance with the provisions of Schedule III of the Companies Act 2013 and the applicable accounting standards.

A company covered under sub-section (3) of section 129 which is not required to prepare consolidated financial statements under the Accounting Standards, it shall be sufficient if the company complies with provisions of consolidated financial statements provided in Schedule III of the Act.

Exemptions from preparation of CFS:

As per Companies (Accounts) Amendment Rules, 2016, preparation of consolidated financial statements by a company is not required if it meets the following conditions:

(i) it is a wholly-owned subsidiary, or is a partially-owned subsidiary of another company and all its other members, including those not otherwise entitled to vote, having been intimated in writing and for which the proof of delivery of such intimation is available with the company, do not object to the company not presenting consolidated financial statements;

(ii) it is a company whose securities are not listed or are not in the process of listing on any stock exchange, whether in or outside India; and

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(iii) its ultimate or any intermediate holding company files consolidated financial statements with the Registrar which are in compliance with the applicable Accounting Standards.

AS 21 also lays down the accounting principles and procedures for preparation and presentation of consolidated financial statements which have been covered in the later part of this chapter.

4 SCOPE OF AS 21

1. This Standard should be applied in the preparation and presentation of consolidated financial statements for a group of enterprises under the control of a parent.
2. This Standard should also be applied in accounting for investments in subsidiaries in the separate financial statements of a parent.
3. In the preparation of consolidated financial statements, other Accounting Standards also apply in the same manner as they apply to the separate statements.
4. This Standard does not deal with:
    a. methods of accounting for amalgamations and their effects on consolidation, including goodwill arising on amalgamation (see AS 14, Accounting for Amalgamations);
    b. accounting for investments in associates (at present governed by AS 13, Accounting for Investments); and
    c. accounting for investments in joint ventures (at present governed by AS 13, Accounting for Investments).

Note:

AS 21 is mandatory if an enterprise presents consolidated financial statements. In other words, the accounting standard does not mandate an enterprise to present consolidated financial statements but, if the enterprise presents consolidated financial statements for complying with the requirements of any statute or otherwise, it should prepare and present consolidated financial statements in accordance with AS 21.

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5 CONTROL

The consolidated financial statements are prepared on the basis of financial statements of parent and all enterprises that are controlled by the parent, other than those subsidiaries excluded for the reasons set out in paragraph 11 of AS 21.

Control exists when the parent owns, directly or indirectly through subsidiary(ies), more than one-half of the voting power of an enterprise. Control also exists when an enterprise controls the composition of the board of directors (in the case of a company) or of the corresponding governing body (in case of an enterprise not being a company) so as to obtain economic benefits from its activities.

An enterprise may control the composition of the governing bodies of entities such as gratuity trust, provident fund trust etc. Since the objective of control over such entities is not to obtain economic benefits from their activities, these are not considered for the purpose of preparation of consolidated financial statements.

For the purpose of this Standard, an enterprise is considered to control the composition of

(i) the board of directors of a company, if it has the power, without the consent or concurrence of any other person, to appoint or remove all or a majority of directors of that company. An enterprise is deemed to have the power to appoint a director, if any of the following conditions is satisfied:

   a. a person cannot be appointed as director without the exercise in his favour by that enterprise of such a power as aforesaid; or

   b. a person's appointment as director follows necessarily from his appointment to a position held by him in that enterprise; or

   c. the director is nominated by that enterprise or a subsidiary thereof.

(ii) (ii) the governing body of an enterprise that is not a company, if it has the power, without the consent or the concurrence of any other person, to appoint or remove all or a majority of members of the governing body of that other enterprise. An enterprise is deemed to have the power to appoint a member, if any of the following conditions is satisfied:

   a. a person cannot be appointed as member of the governing body without the exercise in his favour by that other enterprise of such a power as aforesaid; or

   b. a person's appointment as member of the governing body follows necessarily from his appointment to a position held by him in that other

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enterprise; or

c. the member of the governing body is nominated by that other enterprise.

Note:

It is possible that an enterprise is controlled by two enterprises – one controls by virtue of ownership of majority of the voting power of that enterprise and the other controls, by virtue of an agreement or otherwise, the composition of the board of directors so as to obtain economic benefits from its activities.

In such a rare situation, when an enterprise is controlled by two enterprises as per the definition of 'control', the first mentioned enterprise will be considered as subsidiary of both the controlling enterprises within the meaning of AS 21 and, therefore, both the enterprises need to consolidate the financial statements of that enterprise.

6 EXCLUSION FROM PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS

As per AS 21, a subsidiary should be excluded from consolidation when:

(a) **control is intended to be temporary** because the subsidiary is acquired ***and*** **held** exclusively **with a view to its subsequent disposal in the near future**; ***or***

(b) it operates under **severe long-term restrictions** which significantly impair its ability to transfer funds to the parent.

In consolidated financial statements, investments in such subsidiaries should be accounted for in accordance with AS 13 'Accounting for Investments'. The reasons for not consolidating a subsidiary should be disclosed in the consolidated financial statements.

Where an enterprise owns majority of voting power by virtue of ownership of the shares of another enterprise and all the shares are held as 'stock-in-trade' and are acquired and held exclusively with a view to their subsequent disposal in the near future, the control by the first mentioned enterprise is considered to be temporary.

The period of time, which is considered as "**near future**" as mentioned above, primarily depends on the facts and circumstances of each case. However, ordinarily, the meaning of the words '**near future**' is considered as not more than twelve months from acquisition of relevant investments unless a longer period can be justified on the basis of facts and circumstances of the case. The intention with regard to disposal of the relevant investment is considered at the time of

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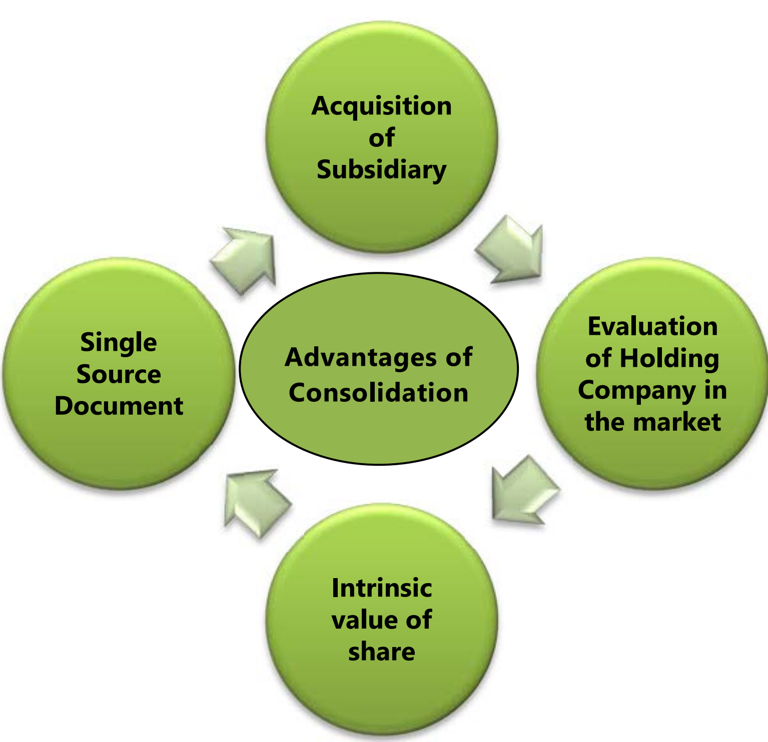
acquisition of the investment. Accordingly if the relevant investment is acquired *without* an intention to its subsequent disposal in near future, and subsequently, it is decided to dispose off the investments, such an investment is not excluded from consolidation, until the investment is actually disposed off.

Conversely, if the relevant investment is acquired with an intention to its subsequent disposal in near future, but, due to some valid reasons, it could not be disposed off within that period, the same will continue to be excluded from consolidation, provided there is no change in the intention.

Exclusion of a subsidiary from consolidation on the ground that its business activities are dissimilar from those of the other enterprises within the group is not justified because better information is provided by consolidating such subsidiaries and disclosing additional information in the consolidated financial statements about the different business activities of subsidiaries. For example, the disclosures required by AS 17 'Segment Reporting', help to explain the significance of different business activities within the group.

7 ADVANTAGES OF CONSOLIDATED FINANCIAL STATEMENTS



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 Group (i.e. holding company and its subsidiaries). Consolidated profit and loss account gives the overall profitability of the group.

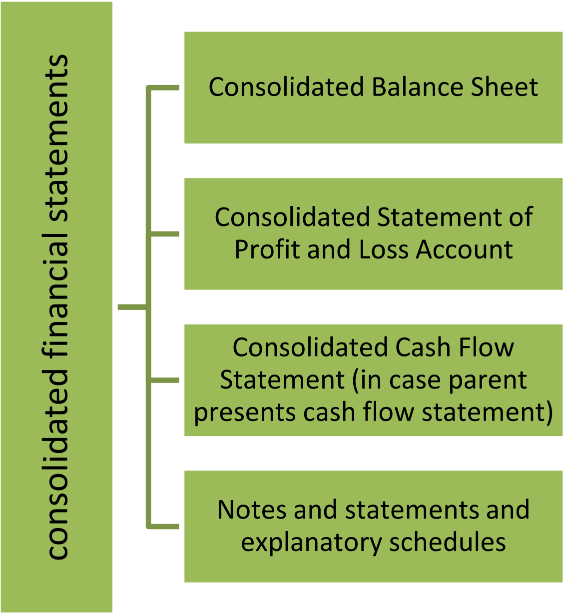
(ii) **Intrinsic value of share:** Intrinsic share value of the holding company can be calculated directly from the Consolidated Balance Sheet.

(iii) **Acquisition of subsidiary:** The minority interest data of the consolidated financial statement indicates that 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.

(iv) **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.

8. COMPONENTS OF CONSOLIDATED FINANCIAL STATEMENTS

As per AS 21, consolidated financial statements normally include the following:



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- 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.

All the notes appearing in the separate financial statements of the parent enterprise and its subsidiaries need not be included in the notes to the consolidated financial statement. For preparing consolidated financial statements, the following principles may be observed in respect of notes and other explanatory material that form an integral part thereof:

(a) Notes which are necessary for presenting a true and fair view of the consolidated financial statements are included in the consolidated financial statements as an integral part thereof.

(b) Only the notes involving items which are material need to be disclosed. Materiality for this purpose is assessed in relation to the information contained in consolidated financial statements. In view of this, it is possible that certain notes which are disclosed in separate financial statements of a parent or a subsidiary would not be required to be disclosed in the consolidated financial statements when the test of materiality is applied in the context of consolidated financial statements.

(c) Additional statutory information disclosed in separate financial statements of the subsidiary and/or a parent having no bearing on the true and fair view of the consolidated financial statements need not be disclosed in the consolidated financial statements.

In addition, the consolidated financial statements shall disclose the information as per the requirements specified in the applicable Accounting Standards including the following as per the requirements of Schedule III to the Companies Act, 2013 which contains the 'General Instructions for Preparation of Consolidated Financial Statements':

(i) Profit or loss attributable to "minority interest" and to owners of the parent in the statement of profit and loss shall be presented as allocation for the period.

(ii) "Minority interests" in the balance sheet within equity shall be presented separately from the equity of the owners of the parent.

Students are also advised to refer the Schedule III to the Companies Act, 2013.

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9. CONSOLIDATION PROCEDURES

Rule 6 of the Companies (Accounts) Rules, 2014 states that the manner of consolidation of financial statements of the company shall be in accordance with the provisions of Schedule III of the Act and the applicable accounting standards. AS 21, lays down the procedure for consolidation of financial statements of the companies within the group.

When preparing consolidated financial statements, the individual balances of the parent and its subsidiaries are combined or consolidated 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.

The various steps involved in the consolidation process are as follows:

1. the cost to the parent of its investment (cost of acquisition) in each subsidiary and the parent's portion of equity of each subsidiary (acquirer's interest), at the date on which investment in each subsidiary is made, should be eliminated. In case, cost of acquisition exceeds or is less than the acquirer's interest, at the date on which investment in the subsidiary is made, goodwill or capital reserve should be recognized respectively in the CFS.
2. intragroup transactions, including sales, expenses and dividends, are eliminated, in full;
3. Adjustments in respect of unrealised profits/ losses should be made;
4. 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
5. minority interests 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 interests in the net assets consist of:

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(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.

Note:

Where the carrying amount of the investment in the subsidiary is different from its cost, the carrying amount is considered for the purpose of above computations.

6. The results of operations of a subsidiary are included in the CFS as from the date on which parent-subsidiary relationship came in existence.

   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.

   The difference between the proceeds from the disposal of investment in a subsidiary and the carrying amount of its assets less liabilities as of the date of disposal is recognised in the consolidated statement of profit and loss as the profit or loss on the disposal of the investment in the subsidiary.

   In order to ensure the comparability of the financial statements from one accounting period to the next, supplementary information is often provided about the effect of the acquisition and disposal of subsidiaries on the financial position at the reporting date and the results for the reporting period and on the corresponding amounts for the preceding period.

7. An investment in an enterprise should be accounted for in accordance with AS 13, Accounting for Investments, from the date that the enterprise ceases to be a subsidiary and does not become an associate.

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

10. 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.

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Equity is defined 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.

Example:

1. H Ltd. acquires 70% of the equity shares of S Ltd. on 1.1.2017. 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 1.1.2017 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

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

2. A Ltd. acquired 70% interest in B Ltd. on 1.1.2017. 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 was 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

In this case, H Ltd. enjoyed negative differential of ₹24,000 i.e. (1,54,000 – 1,30,000) which is called and presented as capital reserve.

11. 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 interests should be presented in the consolidated balance sheet separately from liabilities and the equity of the parent's shareholders. 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.

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12. 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.

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 = Share Capital of subsidiary belonging to outsiders + Minority interest in reserves and profits of subsidiary company

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 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 reserves and profits (or losses) of holding company.

13. REVALUATION OF ASSETS OF SUBSIDIARY COMPANY

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.

Depreciation on changed value of the assets shall be given effect to. Depreciation on revalued assets will be taken as capital or revenue depending on the period for which the depreciation belongs to.

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14. DIVIDEND RECEIVED FROM SUBSIDIARY COMPANIES

As per AS 13, 'Accounting for Investments', Interest, dividends and rentals receivables in connection with an investment are generally regarded as income, being the return on the investment.

However, in some circumstances, such inflows represent a recovery of cost and do not form part of income.

Example: When unpaid interest has accrued before the acquisition of an interest-bearing investment and is therefore included in the price paid for the investment, the subsequent receipt of interest is allocated between pre-acquisition and post-acquisition periods; the pre-acquisition portion is deducted from cost.

When dividends on equity are declared from pre-acquisition profits, a similar treatment (i.e. as mentioned above) may apply. If it is difficult to make such an allocation except on an arbitrary basis, the cost of investment is normally reduced by dividends receivable only if they clearly represent a recovery of a part of the cost.

When holding company receives dividend from a subsidiary company, it must distinguish between the part received out of capital profits (i.e. pre-acquisition profits) and revenue profits (i.e. post-acquisition profits); capital profits are credited to Investment account (being capital receipts) and revenue profits are credited to the Profit & Loss Account.

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.

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.

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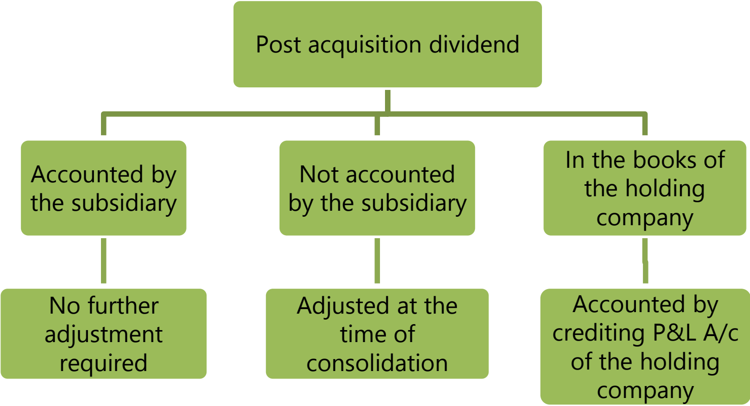
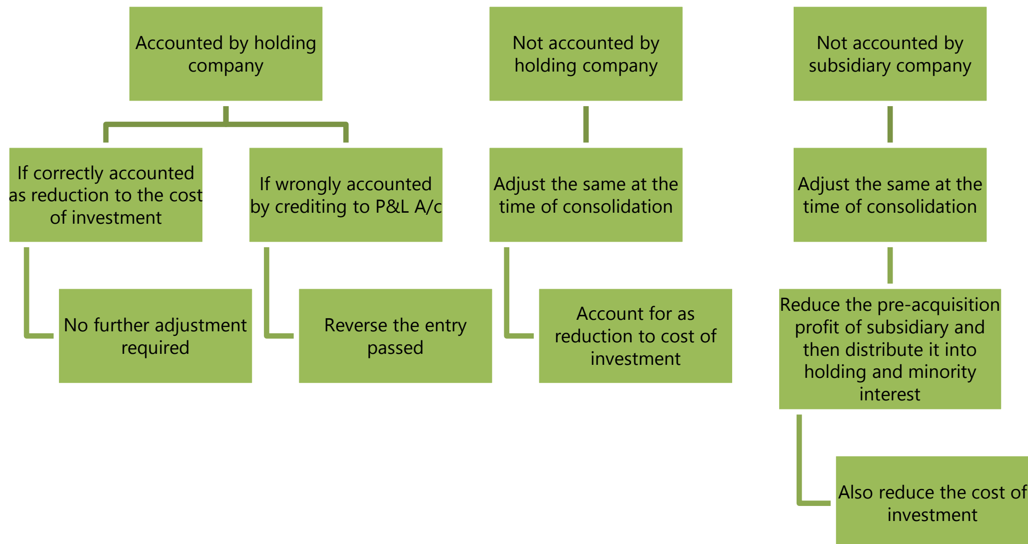
Treatment in case of post-acquisition dividend



Treatment in case of pre-acquisition dividend



Dividends received out of profits earned before purchase of investments normally also are credited to the Investment Account.

Example:

If shares in X Ltd., are purchased in January 2016 and in April 2016, X Ltd., declares a dividend in respect of 2015, 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.

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Note:

In case of issue of bonus shares by the subsidiary company, the holding company, like other holders, record no entry; only the number of shares held is increased.

Illustration 1

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*	
				1.1.2016		*31.12.2016*	
				Share Capital	*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 case it should be equal to 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

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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

A = Share capital on 1.1.2016

B = Profit & loss account balance on 1.1.2016

C = Share capital on 31.12.2016

D = Profit & loss account balance on 31.12.2016

(2) Calculation of Goodwill or Capital Reserve

	Sharehold-ing *% [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 (1.1.2016) is Capital profit, as such the balance of Consolidated Profit & Loss Account shall be equal to Holding Co.'s profit.

On 31.12.2016 in each case the following amount shall be added or deducted from the balance of holding Co.'s Profit & Loss account.

	% Share holding [K]	P & L as on 1.1.2016 [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

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Illustration 2

XYZ Ltd. purchased 80% shares of ABC Ltd. on 1st January, 2016 for ₹ 1,40,000. The issued capital of ABC Ltd., on 1st January, 2016 was ₹ 1,00,000 and the balance in the Profit & Loss Account was ₹ 60,000.

During the year ended 31st December, 2016, ABC Ltd. earned a profit of ₹ 20,000 and at year end, declared and paid a dividend of ₹ 15,000.

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, 2016 and 31st December, 2016? Also please check whether there should be any goodwill/ capital reserve at the date of acquisition.

Solution

Total dividend paid is ₹ 15,000 (out of post-acquisition profits), hence dividend received by XYZ will be credited to P & L.

XYZ Ltd.'s share of dividend = ₹ 15,000 X 80% = ₹ 12,000

In the books of XYZ Ltd.

		₹	₹
Bank A/c	Dr.	12,000	
To Profit & Loss A/c			12,000
(Dividend received from ABC Ltd credited to P&L A/c being out of post-acquisitoin profits – as explained above)			
Goodwill on consolidation (at the date of acquisition):		₹	₹
Cost of shares			1,40,000
Less: Face value of capital i.e. 80% of capital		80,000	
Add: Share of capital profits [60,000 X 80 %]		48,000	(1,28,000)
Goodwill			12,000
Minority interest on:			
- **1st January, 2016:**			
20% of ₹ 1,60,000 [1,00,000 + 60,000]			32,000
- **31st December, 2016:**			33,000
20% of ₹1,65,000 [1,00,000 + 60,000 + 20,000 – 15,000]			

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Illustration 3

Exe Ltd. acquires 70% of equity shares of Zed Ltd. as on 31st March, 2017 at a cost of ₹ 70 lakhs. The following information is available from the balance sheet of Zed Ltd. as on 31st March, 2017:

	₹ 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, 2017. 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, 2017

	₹ 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% of 138.5)		96.95
Exe Ltd.'s cost of acquisition of shares of Zed Ltd.		

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(₹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 lakhs /₹ 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 4

A Ltd. acquired 70% of equity shares of B Ltd. on 1.4.2010 at cost of ₹ 10,00,000 when B Ltd. had an equity share capital of ₹ 10,00,000 and reserves and surplus of ₹ 80,000. 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 2014-15, B Ltd. experienced turnaround and registered an annual profit of ₹ 50,000. In the next two years i.e. 2015-16 and 2016-17, 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

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 profits, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered. Accordingly, the minority interests will be computed as follows:

Year	*Profit/(Loss)*	*Minority Interest (30%)*	*Additional Consolidated P & L (Dr.) Cr.*	*Minority's Share of losses borne by A Ltd.*		*Cost of Control*
				₹	*Balance*	
At the time of acquisition in 2010		3,24,000 (W.N.)	-			
2010-11	(2,50,000)	(75,000)	(1,75,000)			2,44,000

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						(W.N.)
Balance		2,49,000				
2011-12	(4,00,000)	(1,20,000)	(2,80,000)			2,44,000
Balance		1,29,000				
2012-13	(5,00,000)	(1,50,000)	(3,50,000)			2,44,000
		(21,000)				
	Loss of minority borne by Holding Co.	21,000	(21,000)	21,000	21,000	
Balance		Nil	(3,71,000)			
2013-14	(1,20,000)	(36,000)	(84,000)			2,44,000
	Loss of minority borne by Holding Co.	36,000	(36,000)	36,000	57,000	
Balance		Nil	(1,20,000)			
2014-15	50,000	15,000	35,000			2,44,000
	Profit share of minority adjusted against losses of minority absorbed by Holding Co.	(15,000)	15,000	(15,000)	42,000	
Balance		Nil	50,000			
2015-16	1,00,000	30,000	70,000			
	Profit share of minority adjusted against losses of minority absorbed by Holding Co.	(30,000)	30,000	(30,000)	12,000	2,44,000

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Balance		Nil	100,000			
2016-17	1,50,000	45,000	1,05,000	(12,000)	Nil	2,44,000
		(12,000)	12,000			
Balance		33,000	1,17,000			

Working Note:

Calculation of Minority interest and Cost of control on 1.4.2010

		Share of Holding Co.	*Minority Interest*
	100%	*70%*	*30%*
	(₹)	*(₹)*	*(₹)*
Share Capital	10,00,000	7,00,000	3,00,000
Reserve	80,000	56,000	24,000
		7,56,000	3,24,000
Less: Cost of investment		(10,00,000)	
Goodwill		2,44,000	

Illustration 5

H Ltd. acquired 3,000 shares in S Ltd., at a cost of ₹4,80,000 on 31.7.2016. The capital of S Ltd. consisted of 5,000 shares of ₹ 100 each fully paid. The Profit & Loss Account of this company for 2016 showed an opening balance of ₹1,25,000 and profit for the year was ₹ 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.

Assume calendar year as financial year.

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 1.1.2016	1,25,000	—	
Profit for 2016 (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

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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

There can be two situations as regards the treatment of dividend of ₹1,20,000:

(1) The profit for 2016 has been utilised to pay the dividend.

The share of H Ltd in profit for the first seven months of S Ltd = ₹ 1,05,000

(i.e. ₹ 1,75,000 × 3/5)

Profit for the remaining five months = ₹ 75,000

(i.e. ₹ 1,25,000 × 3/5).

The dividend of ₹ 1,20,000 will be adjusted in this ratio of 1,05,000 : 75,000

= ₹ 70,000 out of profits up to 1.7.2016 and ₹ 50,000 out of profits after that date.

The dividend out of profits subsequent to 1.7.2016 will be revenue income and that out of earlier profits will be capital receipt. Hence the entry will be:

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

(2) **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 1.7.2016) 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

Note:

Point (2) discussed above can arise only if there is definite information about the profits utilized. In practice, such treatment is rare.

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15. PREPARATION OF CONSOLIDATED BALANCE SHEET

While preparing the consolidated balance sheet, assets and 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 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 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.

Illustration 6

From the following summarized balance sheets of H Ltd. and its subsidiary S Ltd. drawn up at 31st March, 2017, 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, 2016.

(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 1st April, 2016 for the purpose of fixing the price of its shares. [Rates of depreciation computed on the basis of useful lives: Machinery 10%, Furniture 15%.]

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Summarised Balance Sheet of H Ltd. as on 31st March, 2017

	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 ₹ 100 each	*6,00,000*	*1,00,000*	*Furniture*	*1,50,000*	*17,000*
Reserves	*2,00,000*	*75,000*	*Other non-current assets*	*4,40,000*	*1,50,000*
			Non-current Investments		
Profit and Loss Account	*1,00,000*	*25,000*	*Shares in S Ltd.:*		
Trade Payables	*1,50,000*	*57,000*	*800 shares at ₹ 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, 2017

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 (W.N.5)		48,150
(3) Current Liabilities		
(a) Trade Payables	2	2,07,000
Total		11,99,750
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment		
(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		2,00,000	
	Add: 4/5th share of S Ltd.'s post-acquisition reserves (W.N.3)		40,000	2,40,000
	Profit and Loss Account		1,00,000	
	Add: 4/5th share of S Ltd.'s post-acquisition profits (W.N.4)		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 (1,50,000 X 10%)	(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 (15,000 X 15%)	(2,250)	12,750	5,97,750

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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 (or 80%) × 40,000	32,000
	Minority Interest= 1/5 (or 20%) × 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 (Total reserves less pre-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 (Profit & loss account balance less pre-acquisition profits = ₹ 25,000 – 15,000)	10,000
	Add: Excess depreciation charged on furniture @ 15%	
	on ₹ 5,000 i.e. (20,000 – 15,000)	750
		10,750
	Less: Under depreciation on machinery @ 10%	

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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 (or 1,00,000 X 20%)	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	
Price paid by H Ltd. for 800 shares (A)	**1,60,000**
***Less:* Intrinsic value of the shares**	
Paid-up value of 800 shares held by H Ltd. i.e. 800 × ₹ 100 (or 1,00,000 X 80%)	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 (B)	**1,48,000**
Cost of control or Goodwill (A – B)	**12,000**

16. ELIMINATION OF INTRA-GROUP TRANSACTIONS

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

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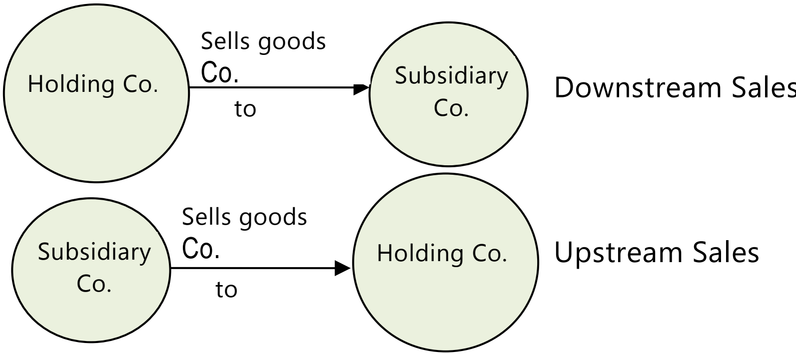
and from cost of sales or the appropriate expense heading in the consolidated statement of profit and loss.

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 are 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, 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.



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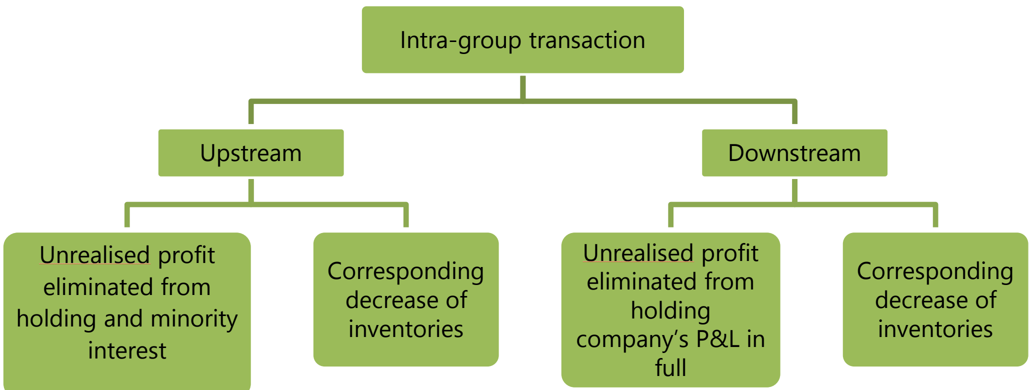
In the case of upstream transaction, since the goods are sold by the subsidiary to holding company; profit is made by the subsidiary company, which is ultimately shared by the holding company and the minority shareholders. In such a transaction, if some goods remain unsold at the balance sheet date, 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 inventory.

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 inventory and consolidated profit and loss account only irrespective of the percentage of the shares held by the parent.



Unrealised profit on transfer of non-current asset: 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.**

Example:

If net realizable value (NRV) expected from sale of such goods is more than the actual cost of the goods, then unrealized loss should be reversed during consolidation process. However, if it is expected that NRV would not be sufficient to recover the loss incurred on transfer of goods from one entity to another, the unrealized loss should not be reversed.

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Illustration 7

a. A Ltd holds 80% of the equity capital and voting power in B Ltd. A Ltd sells inventories costing ₹ 180 lacs to B Ltd at a price of ₹ 200 lacs. The entire inventories remain unsold with B Ltd at the financial year end i.e. 31 March 2019.

b. A Ltd holds 75% of the equity capital and voting power in B Ltd. A Ltd purchases inventories costing ₹ 150 lacs from B Ltd at a price of ₹ 200 lacs. The entire inventories remain unsold with A Ltd at the financial year end i.e. 31 March 2019.

Suggest the accounting treatment for the above mentioned transactions in the consolidated financial statements of A Ltd giving reference of the relevant guidance/standard.

Solution

As per para 16 and 17 of AS 21

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.

Intragroup balances and intragroup transactions, including sales, expenses and dividends, are eliminated in full. 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. 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.

One also needs 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, since the 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 inventory.

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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 inventory and consolidated profit and loss account only irrespective of the percentage of the shares held by the parent.

Using above mentioned guidance, following adjustments would be required:

a. This would be the case of downstream transaction. In the consolidated profit and loss account for the year ended 31 March 2019, entire transaction of sale and purchase of ₹ 130 lacs each, would be eliminated by reducing both sales and purchases (cost of sales).

   Further, the unrealized profits of ₹ 20 lacs (i.e. ₹ 200 lacs – ₹ 180 lacs), would be eliminated from the consolidated financial statements for financial year ended 31 March 2019, by reducing the consolidated profits/ increasing the consolidated losses, and reducing the value of closing inventories as of 31 March 2019.

b. This would be the case of upstream transaction. In the consolidated profit and loss account for the year ended 31 March 2019, entire transaction of sale and purchase of ₹ 200 lacs each, would be eliminated by reducing both sales and purchases (cost of sales).

   Further, the unrealized profits of ₹ 50 lacs (i.e. ₹ 200 lacs – ₹ 150 lacs), would be eliminated in the consolidated financial statements for financial year ended 31 March 2019, by reducing the value of closing inventories by ₹ 50 lacs as of 31 March 2019. In the consolidated balance sheet as of 31 March 2019, A Ltd's share of profit from B Ltd will be reduced by ₹ 37.50 lacs (being 75% of ₹ 50 lacs) and the minority's share of the profits of B Ltd would be reduced by ₹ 12.50 lacs (being 25% of ₹ 50 lacs).

17. PREPARATION OF CONSOLIDATED PROFIT AND LOSS ACCOUNT

All the items of profit and loss account are to be added on line by line basis and inter-company transactions should be eliminated from the consolidated figures.

For example, a holding company may sell goods or services to its subsidiary, receive 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.

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

Illustration 8

Given below are the Profit & Loss Accounts of H Ltd and its subsidiary S Ltd for the year ended 31st March, 2017:

	H Ltd. (₹ in lacs)	S Ltd. (₹ in lacs)
Incomes:		
Sales and other income	5,000	1,000
Increase in Inventory	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
Dividend paid	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%. Inventory 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. prior to 2015-2016.

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H Ltd. took credit to its Profit and Loss Account, the proportionate amount of dividend declared and paid by S Ltd. for the year 2015-2016.

Prepare a consolidated profit and loss account.

Solution

Consolidated Profit & Loss Account of H Ltd. and its subsidiary S Ltd. for the year ended on 31st March, 2017

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**

Notes to Accounts

		₹ in Lacs	*₹ in Lacs*
1.	Revenue from 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 inventory		

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	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 (Production)		
	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

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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

18. PREPARATION OF CONSOLIDATED CASH FLOW STATEMENT

As per AS 21, Consolidated cash flow statement is presented in case a parent presents its own cash flow statement.

For the purpose of preparation of consolidated cash flow statement, 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 an illustrative consolidated cash flow statement with hypothetical figures:

Consolidated Cash Flow Statement (Illustrative only)

		(₹ in million)	
	A Company	*B Company*	*Total*
Cash Flows from Operating Activities			
Change in Reserve	8	2	10
Change in P & L A/c	-	1	1
Dividend Paid	22	-	22
Tax Provision	20	1	21
Depreciation	10	5	15

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Interest	(10)	10	-
	50	19	69
Less: Tax payment	(20)	(1)	(21)
	30	18	48
Working capital adjustment	(13)	12	(1)
(A)	17	30	47
Cash Flows from Investment Activities			
Sale of fixed assets	30	-	30
Purchase of fixed assets	(30)	(20)	(50)
(B)	-	(20)	(20)
Cash Flows from Financing Activities	(5)	(10)	(15)
(C)			
Net cash flows (A+B+C)	**12**	**-**	**12**

19. UNIFORM ACCOUNTING POLICIES

Para 20 of AS 21 states 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 are made to its financial statements when they are used in preparing the consolidated financial statements.

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 weighted average method for valuation of inventories and the holding company follows FIFO method, the financial statements 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. After that consolidation should be done.

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Illustration 9

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

	2015 ₹	2016 ₹		2015 ₹	2016 ₹
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)
				2,72,000	2,24,000
Reserves & Surplus	2,86,000	7,14,000	Investments at cost		
Current Liabilities & Provisions:			Non-current Assets:	—	4,00,000
Trade Payables	4,90,000	4,94,000	Inventory	5,97,000	7,42,000
Bank overdraft	—	1,70,000	Trade Receivables	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

Also consider 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 inventory on weighted average basis while B Ltd. used FIFO basis. To bring B Ltd.'s values in line with those of A Ltd, its value of inventory is required to be reduced by ₹12,000 at the end of 2015 and ₹ 34,000 at the end of 2016.*

(c) *B Ltd. deducts 1% from Trade Receivables as a general provision against doubtful debts.*

(d) *Prepaid expenses in B Ltd. include advertising expenditure carried forward of ₹ 60,000 in 2015 and ₹ 30,000 in 2016, being part of initial advertising expenditure of ₹ 90,000 in 2015 which is being written off over three years. Similar amount of advertising expenditure of A Ltd. has been fully written off in 2015.*

Restate the balance sheet of B Ltd. as on 31st December, 2016 after considering the above information, for the purpose of consolidation. Would restatement be necessary to make the accounting policies adopted by A Ltd. and B Ltd. uniform.

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Solution

As per para 20 and 21 of AS 21, Consolidated financial statements:

Consolidated financial statements should be prepared using uniform accounting policies for like transactions and other events in similar circumstances. If it is not practicable to use uniform accounting policies in preparing the consolidated financial statements, that fact should be disclosed together with the proportions of the items in the consolidated financial statements to which the different accounting policies have been applied.

If a member of the group uses accounting policies other than those adopted in the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to its financial statements when they are used in preparing the consolidated financial statements.

Accordingly in the given case, restatement would be required to make the accounting policies of A Ltd and B Ltd uniform.

Adjusted reserves of B Ltd.:

	₹	₹
Reserves as given		7,14,000
Add: Provision for doubtful debts		9,000
{[8,91,000 / 99 X 100]-8,91,000}		
		7,23,000
Less: Reduction in value of Inventory	34,000	
Advertising expenditure to be written off	30,000	(64,000)
Adjusted reserves		6,59,000

Note: No adjustment would be required in respect of opening inventory of B Ltd as that will not have any impact on P&L.

Restated Balance Sheet of B Ltd.
as at 31st December, 2016

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		5,00,000
(b) Reserves and Surplus	1	6,59,000

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	(2) Current Liabilities		
	(a) Short term borrowings	2	1,70,000
	(b) Trade Payables		4,94,000
	(c) Short-term provision	3	4,30,000
	Total		22,53,000
II.	**Assets**		
	(1) Non-current assets		
	(a) Property, Plant and Equipment		
	Tangible assets	4	2,24,000
	(b) Non-current Investment		4,00,000
	(2) Current assets		
	(a) Inventories	5	7,08,000
	(b) Trade Receivables	6	9,00,000
	(c) Cash & Cash Equivalents		3,000
	(d) Other current assets	7	18,000
	Total		22,53,000

Notes to Accounts

			₹
1.	**Reserves and Surplus**		
	Reserves (refer computation of adjusted reserves of B Ltd)		6,59,000
2.	**Short term borrowings**		
	Bank overdraft		1,70,000
3.	**Short-term provision**		
	Provision for taxation		4,30,000
4.	**Tangible Assets**		
	Cost	3,20,000	
	Less: Depreciation to date	(96,000)	2,24,000

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5.	**Inventory**		
	Cost	7,42,000	
	Less: Adjustment because of change in method of valuation	(34,000)	7,08,000
6.	Trade receivables		
	Cost	8,91,000	
	Add: Provision adjustment	9,000	9,00,000
7.	**Other current assets**		
	Prepaid expenses (After adjusting advertising expenditure to be written off each year)		18,000

20. TREATMENT OF SUBSIDIARY COMPANY HAVING PREFERENCE SHARE CAPITAL

While preparing CFS, outstanding cumulative preference shares issued by a subsidiary are considered in the same manner as any other liability, such as debentures etc. Accordingly, the cost associated with such cumulative preference shares needs to be adjusted for.

Therefore, while computing its share of profits or losses of the subsidiary, the parent should make adjustments in respect of preference dividends on outstanding cumulative preference shares issued by a subsidiary and held outside the group since, for the group, such preference shares represent external liabilities. It would be appropriate for the parent to compute its share of profits or losses after adjusting for subsidiary's cumulative preference dividends, whether or not profits are available or dividends have been declared.

However, in case of non-cumulative preference shares, no such adjustment is required unless the dividend is actually received.

21. ALIGNMENT OF REPORTING DATES

The financial statements used in the consolidation should be drawn up to the same reporting date. If it is not practicable to draw up the financial statements of one or more subsidiaries to such date and, accordingly, those financial statements are drawn up to different reporting dates, adjustments should be made for the effects

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of significant transactions or other events that occur between those dates and the date of the parent's financial statements.

In any case, the difference between reporting dates should not be more than six months.

The financial statements of the parent and its subsidiaries used in the preparation of the consolidated financial statements are usually drawn up to the same date. When the reporting dates are different, the subsidiary often prepares, for consolidation purposes, statements as at the same date as that of the parent.

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.

The consistency principle requires that the length of the reporting periods and any difference in the reporting dates should be the same from period to period.

SUMMARY

- "Holding company", in relation to one or more other companies, means a company of which such companies are subsidiary companies; "subsidiary company" or "subsidiary", in relation to any other company (that is to say the holding company), means a company in which the holding company—
    - controls the composition of the Board of Directors; or
    - exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies: Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.
- 'Total share capital', as defined in section 2(87) (ii) above, has been further clarified by the Rule 2(1)(r) of the Companies (Specification of Definitions Details) Rules, 2014. As per the Rule, total share capital includes
    - paid up equity share capital
    - convertible preference share capital.
- 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.

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- 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.

Preparation of Consolidated Profit and Loss Account

- 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.
- If there remains any unrealised profit in the inventory of goods, of any of the Group Company, such unrealised profit should be eliminated from the value of inventory to arrive at the consolidated profit.

Preparation of Consolidated Cash Flow Statement

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.

The financial statements used in the consolidation should be drawn up to the same reporting date. If it is not practicable to draw up the financial statements of one or more subsidiaries to such date and, accordingly, those financial statements are drawn up to different reporting dates, adjustments should be made for the effects of significant transactions or other events that occur between those dates and the date of the parent's financial statements.

In any case, the difference between reporting dates should not be more than six months.

TEST YOUR KNOWLEDGE

MCQs

1. Minority interest should be presented in the consolidated balance sheet
   - (a) As a part of liabilities
   - (b) As a part of equity of the parent's shareholders
   - (c) Separately from liabilities and the equity of the parent's shareholders
2. Minority of the subsidiary is entitled to
   - (a) Capital profits of the subsidiary company
   - (b) Revenue profits of the subsidiary company
   - (c) Both capital and revenue profits of the subsidiary company

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3. In consolidation of accounts of holding and subsidiary company ________ is eliminated in full.

   (a) Current liabilities of subsidiary company

   (b) Reserves and surplus of both holding and subsidiary company

   (c) Mutual indebtedness.

4. In consolidated balance sheet, the share of the outsiders in the net assets of the subsidiary must be shown as

   (a) Minority interest

   (b) Capital reserve

   (c) Current liability

5. Taxation provision made by the subsidiary company will appear in the consolidated balance sheet as an item of

   (a) Current liability.

   (b) Revenue profit.

   (c) Capital profit.

6. Issue of bonus shares by the subsidiary company out of capital profits will

   (a) Decrease cost of control.

   (b) Increase cost of control.

   (c) Have no effect on cost of control.

7. Dividend paid by subsidiary to its parent, out of capital profits, should be credited by the parent company in its

   (a) Profit and loss account.

   (b) Dividend account.

   (c) Shares invested in subsidiary account.

Practical Questions

Question 1

A Ltd acquired 1,600 ordinary shares of ₹100 each of B Ltd on 1st July, 2016. On 31st December, 2016, the summarized balance sheets of the two companies were as given below:

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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	—	Inventory	1,20,000	36,400
Trade Payable	47,100	17400	Trade Receivable	59,800	40,000
			Cash	14,500	8,000
	9,24,300	3,99,400		9,24,300	3,99,400

The Profit & Loss Account of B Ltd. showed a credit balance of ₹30,000 on 1st January, 2016 out of which a dividend of 10% was paid on 1st August, 2016; A Ltd. credited the dividend received to its Profit & Loss Account. The Plant & Machinery which stood at ₹ 1,50,000 on 1st January, 2016 was considered as worth ₹ 1,80,000 on 1st July, 2016; this figure is to be considered while consolidating the Balance Sheets. The rate of depreciation on plant & machinery is 10% (computed on the basis of useful lives).

Prepare consolidated Balance Sheet as on 31st December, 2016.

Question 2

On 31st March, 2017 the summarized Balance Sheets of H Ltd. and its subsidiary S Ltd. stood as follows:

Liabilities	H Ltd.	S Ltd.
	₹ in lakhs	₹ in lakhs
Share Capital:		
Authorized	15,000	6,000
Issued and Subscribed:		
Equity Shares of ₹ 10 each, fully paid up	12,000	4,800

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General Reserve	2,784	1,380
Profit and Loss Account	2,715	1,620
Bills Payable	372	160
Trade Payables	1,461	854
Provision for Taxation	855	394
Dividend payable	1,200	-
	21,387	9,208
Assets	H Ltd.	S Ltd.
	₹ in lakhs	₹ in lakhs
Land and Buildings	2,718	–
Plant and Machinery	4,905	4,900
Furniture and Fittings	1,845	586
Investments in shares in S Ltd.	3,000	–
Stock	3,949	1,956
Trade Receivables	2,600	1,363
Cash and Bank Balances	1,490	204
Bills Receivable	360	199
Sundry Advances	520	–
	21,387	9,208

The following information is also provided to you:

(a) H Ltd. purchased 180 lakh shares in S Ltd. on 31st March, 2016 when the balances of General Reserve and Profit and Loss Account of S Ltd. stood at ₹ 3,000 lakh and ₹ 1,200 lakh respectively.

(b) On 1st April, 2016, S Ltd. declared a dividend @ 20% for the year ended 31st March, 2016. H Ltd. credited the dividend received by it to its Profit and Loss Account.

(c) On 1st January, 2017, S Ltd. issued 3 fully paid-up bonus shares for every 5 shares held out of balances of its general reserve as on 31st March, 2016.

(d) On 31st March, 2017, all the bills payable in S Ltd.'s balance sheet were acceptances in favour of H Ltd. But on that date, H Ltd. held only ₹ 45 lakh of these acceptances in hand, the rest having been endorsed in favour of its trade payables.

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(e) On 31st March, 2017, S Ltd.'s inventory included goods which it had purchased for ₹ 100 lakh from H Ltd. which made a profit @ 25% on cost.

Prepare a Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 2017.

Question 3

A Ltd. acquired 70% of equity shares of B Ltd. as on 1st January, 2010 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 2014, B Ltd. experienced turnaround and registered an annual profit of ₹ 50,000. In the next two years i.e. 2015 and 2016, 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.

ANSWERS/ HINTS

MCQs

1. (c); **2.** (c); **3.** (c); **4.** (a); **5.** (a); **6.** (c); **7.** (c)

Practical Questions

Answer 1

Consolidated Balance Sheet of A Ltd. and its subsidiary, B Ltd. as on 31st December, 2016

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	5,00,000
(b) Reserves and Surplus	2	3,08,800
(2) Minority Interest (W.N 5)		83,600
(3) Current Liabilities		
(a) Trade Payables	3	64,500

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			Note	₹
	(b)	Short term borrowings	4	80,000
		Total		10,36,900
II.	**Assets**			
	(1)	**Non-current assets**		
		Property, Plant and Equipment		
		(i) Tangible assets	5	7,41,000
		(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		10,36,900

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)		68,800	3,08,800
3.	**Trade Payables**			
	A Ltd.	47,100		
	B Ltd.	17,400		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)		4,11,000	7,41,000
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**			
	A Ltd.	59,800		
	B Ltd.	40,000		
				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 rectification 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, 2016, 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 (1,80,000 – 1,42,500).

3. **Capital profits of B Ltd.**

	₹	₹
Reserve on 1st January, 2016 (Assumed there is no movement in reserves during the year and hence balance as on 1st January 2016 is same as of 31st December 2016)		1,00,000
Profit & Loss Account Balance on 1st January, 2016	30,000	
Less: Dividend paid	(20,000)	10,000

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Profit for 2016: Total ₹ 82,000 Less: ₹ 10,000 ₹ 72,000		
Proportionate upto 1st July, 2016 on time basis (₹ 72,000/2)		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 1st July, 2016 [(82,000 – 10,000) x ½]		36,000
Less: Depreciation		
10% depreciation on ₹1,80,000 for 6 months	9,000	
Less: Depreciation already charged for 2nd half year on 1,50,000	(7,500)	(1,500)
		34,500
Less: 1/5 due to outsiders		(6,900)
Share of A Ltd.		**27,600**

5. Minority interest:

Par value of 400 shares (2,00,000 X 20%)	40,000
Add: 1/5 Capital Profits [WN 3]	36,700
1/5 Revenue Profits [WN 4]	6,900
	83,600

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

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7. Value of plant & Machinery:

A Ltd.		2,40,000
B Ltd.	1,35,000	
Add: Appreciation on 1st July, 2016 [1,80,000 – (1,50,000 – 7,500)]	37,500	
	1,72,500	
Add: Deprecation for 2nd half charged on pre-revalued value	7,500	
Less: Depreciation on ₹1,80,000 for 6 months	(9,000)	1,71,000
		4,11,000

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)		27,600
		68,800

Answer 2

Consolidated Balance Sheet of H Ltd.
and its subsidiary S Ltd. as on 31st March, 2017

Particulars	*Note No.*	*(₹ in Lacs)*
I. **Equity and Liabilities**		
(1) **Shareholder's Funds**		
(a) Share Capital	1	12,000
(b) Reserves and Surplus	2	7,159
(2) **Minority Interest [W.N.6]**		3,120
(3) **Current Liabilities**		
(a) Trade payables	3	2,315
(b) Short term provisions	4	1,249
(c) Other current liabilities	5	1,687
Total		27,530

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II. **Assets**		
(1) **Non-current assets**		
Property, Plant and Equipment		
Tangible assets	6	14,954
(2) **Current assets**		
(a) Inventories	7	5,885
(b) Trade receivables	8	3,963
(c) Cash and cash equivalents	10	1,694
(d) Short term loans and advances	11	520
(e) Other current assets	9	514
Total		27,530

Notes to Accounts

			(₹ in lacs)	(₹ in lacs)
1.	**Share Capital**			
	Authorised			15,000
	Issued and Subscribed:			
	Equity shares of ₹ 10 each, fully paid up			12,000
2.	**Reserves and surplus**			
	Capital Reserve (Note 5)		1,320	
	General Reserve (₹ 2,784 + 108)		2,892	
	Profit and Loss Account:			
	H Ltd.	₹ 2,715		
	Less: Dividend wrongly credited ₹ 360			
	Unrealized Profit ₹ 20	(₹ 380)		
		₹ 2,335		
	Add: Share in S Ltd.'s Revenue profits	₹ 612	2,947	7,159
3.	**Trade payables**			
	H Ltd.		1,461	
	S Ltd.		854	2,315
4.	**Short term provisions**			
	Provision for Taxation			
	H Ltd.		855	
	S Ltd.		394	1,249

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5.	**Other current liabilities**			
	Bills Payable			
	H Ltd.		₹ 372	
	S Ltd.		₹ 160	
			₹ 532	
	Less: Mutual owing		₹ (45)	487
	Dividend payable			
	H Ltd.			1,200
				1,687
6.	**Tangible assets**			
	Land and Buildings			
	H Ltd.		2,718	
	Plant and Machinery			
	H Ltd.	₹ 4,905		
	S Ltd.	₹ 4,900	9,805	
	Furniture and Fittings			
	H Ltd.	₹ 1,845		
	S Ltd.	₹ 586	2,431	14,954
7.	**Inventories**			
	Stock			
	H Ltd.		3,949	
	S Ltd.		1,956	
			5,905	
	Less: Unrealized profit		(20)	5,885
8.	**Trade receivables**			
	H Ltd. ₹ 2,600			
	S Ltd. ₹ 1,363			3,963

9.	**Other current assets**			
	Bills Receivable			
	H Ltd. ₹ 360			
	S Ltd. ₹ 199			
	₹ 559			
	Less: Mutual Owing ₹ (45)			514

10.	**Cash and cash equivalents**		
	Cash and Bank Balances		
	H Ltd.	1,490	
	S Ltd.	204	1,694
11.	**Short term loans and advances**		
	Sundry Advances		
	H Ltd.		520

Working Notes:

Share holding pattern of S Ltd.

Shares as on 31st March, 2017 (Includes bonus shares issued on 1st January, 2017)	480 lakh shares (4,800 lakhs/₹ 10)
H Ltd.'s holding as on 1st April, 2016	180 lakhs
Add: Bonus received on 1st January, 2017	108 lakhs (180 / 5 × 3)
Total H Ltd.'s holding as on 31st March, 2017	288 lakhs i.e. 60 % [288/480×100]
Minority Shareholding	40%

1. S Ltd.'s General Reserve Account

	₹ in lakhs		*₹ in lakhs*
To Bonus to equity shareholders (WN-8)	1,800	By Balance b/d	3,000
To Balance c/d	1,380	By Profit and Loss A/c (Balancing figure)	180
	3,180		3,180

2. S Ltd.'s Profit and Loss Account

	₹ in lakhs		*₹ in lakhs*
To General Reserve [WN 1]	180	By Balance b/d	1,200
To Dividend paid (20% on ₹3,000 lakhs)	600	By Net Profit for the year* (Balancing figure)	1,200
To Balance c/d	1,620		
	2,400		2,400

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*Out of ₹ 1,200 lakhs profit for the year, ₹ 180 lakhs has been transferred to reserves.

3. Distribution of Revenue profits

	₹ in lakhs
Revenue profits (W. N. 2)	1,200
Less: Share of H Ltd. 60% (General Reserve ₹ 108 + Profit and Loss Account ₹ 612)	(720)
Share of Minority Shareholders (40%)	480

Note: The question can also be solved by taking ₹ 1,080 lakhs as post acquisition Profit and Loss balance and ₹ 180 lakhs as post acquisition General Reserve balance. The final answer will be same.

4. Calculation of Capital Profits

	₹ in lakhs
General Reserve on the date of acquisition less bonus shares (₹ 3,000 – ₹ 1,800)	1,200
Profit and loss account on the date of acquisition less dividend paid (₹ 1,200 – ₹ 600)	600
	1,800

H Ltd.'s share = 60% of ₹ 1,800 lakhs = ₹ 1,080 lakhs

Minority interest = ₹ 1,800 – ₹ 1,080 = ₹ 720 lakhs

5. Calculation of capital reserve

	₹ in lakhs
Paid up value of shares held (60% of ₹4,800)	2,880
Add: Share in capital profits [WN 4]	1,080
	3,960
Less: Cost of shares less dividend received (₹ 3,000 – ₹ 360)	(2,640)
Capital reserve	1,320

6. Calculation of Minority Interest

	₹ in lakhs
40% of share capital (40% of ₹ 4,800)	1,920
Add: Share in revenue profits [WN 3]	480

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... Share in capital profits [WN 4]	720
	3,120

7. Unrealized profit in respect of inventory

$$₹\ 100 \text{ lakhs} \times \frac{25}{125} = ₹\ 20 \text{ lakhs}$$

8. Computation of bonus to equity shareholders

	₹ In lakhs
Shares as on 31 March 2017 including bonus share issued on 1 January 2017	4,800
Or we can say these are $1 + \frac{3}{5}$ or $\frac{8}{5}$	
i.e. Shares before bonus issue should have been $\frac{4,800}{8/5}$ =	3,000
Accordingly, bonus issue would be (4,800-3,000)	1,800

Answer 3

	Minority Interest (30%) ₹	*Holding Interest (70%)* ₹
Share of net assets of B Ltd. as on 1.1.2010	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 31.12.2010	75,000	
Minority interest as on 31.12.2010	2,49,000	
Minority's share of losses of B Ltd.:		
year ended 31.12.2011	1,20,000	
Minority interest as on 31.12.2011	1,29,000	
Minority's share of losses of B Ltd.		
year ended 31.12.2012	1,29,000*	
Minority interest as on 31.12.2012	Nil	

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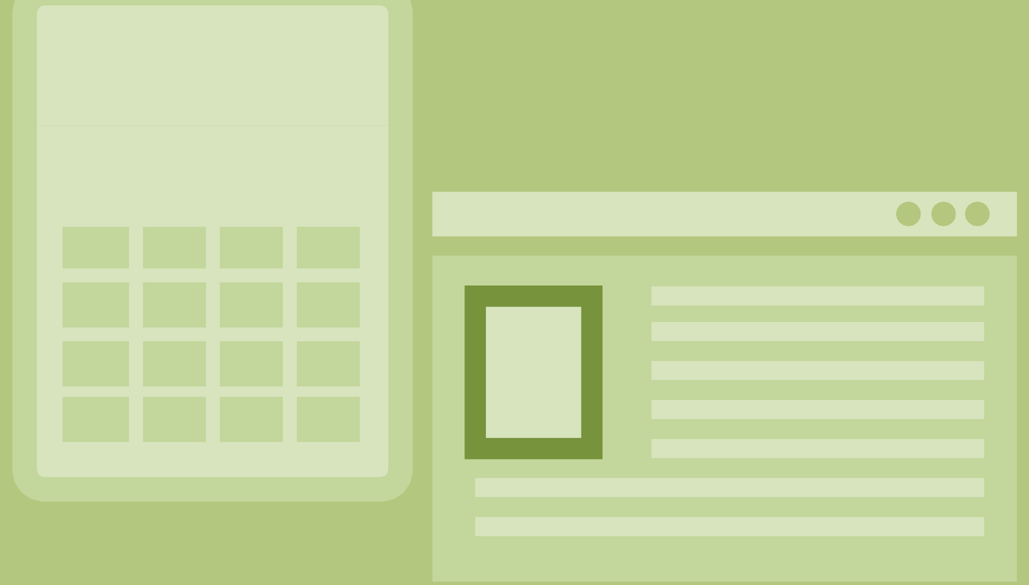
Minority's share of losses for 2013	Nil	
Minority's share of profits of B Ltd. for 2014	Nil	
Minority's share of profit for 2015	Nil	
Minority's share of profit for 2016 (₹ 45,000 – ₹ 12,000)	33,000*	
Minority interest as on 31.12.2016	33,000	



*In the year 2012, the minority's share of losses actually comes to ₹ 1,50,000.
But since minority interest as on 31.12.2011 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 2013, the entire loss of B Ltd is to be adjusted against A Ltd's profits for the purpose of consolidation.
Therefore, upto 2013, 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 2016 and therefore, minority interest of ₹ 33,000 is shown after adjusting fully the share of losses of minority previously absorbed by A Ltd.

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