CHAPTER 22

Preparation of consolidated statements of comprehensive income, changes in equity and cash flows

22.1 Introduction

The main purpose of this chapter is to explain how to prepare a consolidated statement of comprehensive income.

Objectives

By the end of this chapter, you should be able to:

- prepare a consolidated statement of comprehensive income;
- eliminate inter-company transactions from a consolidated statement of comprehensive income;
- attribute comprehensive income to the non-controlling shareholders;
- prepare a consolidated statement of changes in equity.

22.2 Preparation of a consolidated statement of comprehensive income – the Ante Group

The following information is available:

At the date of acquisition on 1 January 20X1
Ante plc acquired 75% of the common shares and 20% of the preferred shares in Post plc.
(Shows that Ante had control)
At that date the retained earnings of Post were £30,000.
(These are pre-acquisition profits and should not be included in the Group profit for the year)
Ante had paid £10,000 more than the fair value of the net assets acquired. Method 1 has been used to measure the non-controlling interest.
(This represents positive goodwill)

During the year ended 31 December 20X2
Ante had sold Post goods at their cost price of £9,000 plus a mark up of one-third. These were the only inter-company sales.
(Indicates that the group sales and cost of sales require adjusting)

At the end of the financial year on 31 December 20X2
Half of these goods were still in the inventory at the end of the year.
(There is unrealised profit to be removed from the Group gross profit)

20% is to be written-off goodwill as an impairment loss.
Dividends paid in the year by group companies were as follows:

	Ante	*Post*
On ordinary shares	40,000	5,000
On preferred shares	—	3,000

Set out below are the individual statements of comprehensive income and statement of changes in equity of Ante and Post together with the consolidated statement of comprehensive income for the year ended 31 December 20X2 with explanatory notes.

Statements of comprehensive income for the year ended 31 December 20X2

	Ante	*Post*	*Consolidated*	
	£	£	£	
Sales	200,000	120,000	308,000	Notes 1/3
Cost of sales	60,000	60,000	109,500	Notes 1/2/3
Gross profit	140,000	60,000	198,500	
Expenses	59,082	40,000	99,082	Note 4
Impairment of goodwill	—		2,000	Note 5
Profit from operations	80,918	20,000	97,418	
Dividends received – common shares	3,750	—	—	Note 6
Dividends received – preferred shares	600	—	—	Note 6
Profit before tax	85,268	20,000	97,418	
Income tax expense	14,004	6,000	20,004	Note 7
Profit for the period	71,264	14,000	77,414	
Attributable to:				
Ordinary shareholders of Ante (balance)			72,264	
Non-controlling shareholders in Post (Note 8)			5,150	
			77,414	

Profit realised from operations – £97,418 – see Notes 1–5
Adjustments are required to establish the profit **realised** from operations. This entails eliminating the effects of inter-company sales and inventory transferred within the group with a profit loading but not sold at the statement of financial position date and charging any goodwill impairment.

Notes:

1 **Eliminate inter-company sales on consolidation.**

Cancel the inter-company sales of £12,000 (9,000 + $^1/_3$) by.

(i) reducing the sales of Ante from £200,000 to £188,000; and

(ii) reducing the cost of sales of Post by the same amount from £60,000 to £48,000.

2 **Eliminate unrealised profit on inter-company goods still in closing inventory.**

(i) Ante had sold the goods to Post at a mark up £3,000.

(ii) Half of the goods remain in the inventory of Post at the year-end.

(iii) From the group's view there is an unrealised profit of half of the mark-up, i.e. £1,500. Therefore:

- deduct £1,500 from the gross profit of Ante by adding this amount to the cost of sales;
- add this amount to a provision for unrealised profit;

- reduce the inventories in the consolidated statement of financial position by the amount of the provision (as explained in the previous chapter).

3 Aggregate the adjusted sales and cost of sales figures for items in Notes 1 and 2.

(i) Add the adjusted sales figures
((200,000 – 12,000 inter-company sales) + 120,000) = **£308,000**

(ii) Add the adjusted cost of sales figures;
60,000 + (60,000 – 12,000) + 1,500 provision = **£109,500**

4 Aggregate expenses
No adjustment is required to the parent or subsidiary total figures.

5 Deduct the impairment loss.
The goodwill was given as £10,000, and it has been estimated that there has been a £2,000 impairment loss.

Profit after tax – £97,418

Adjustments are required[1] to establish the profit after tax earned by the group as a whole. This entails eliminating dividends and interest that have been paid to the parent by the subsidiaries. If this were not done, there would be a double counting as these would appear in the profit from operations of the subsidiary, which has been included in the consolidated profit from operations, and again as dividends and interests received by the group.

6 Accounting for inter-company dividends

(i) **The ordinary dividend** £3,750 received by Ante is 75% of the £5,000 dividend paid by Post.

(ii) Cancel the inter-company dividend received by Ante with £3,750 dividend paid by Post, leaving the £1,250 dividend paid by Post to the non-controlling interest.

(iii) **The preferred dividend** of £600 received by Ante is 20% of the £3,000 paid by Post.

(iv) Cancel the £600 preferred dividend received by Ante with £600 of the preferred dividend paid by Post.

(v) the balance of £2,400 remaining was paid to the non-controlling interest.

7 Aggregate the taxation figures.
No adjustment is required to the parent or subsidiary total figures.

Allocation of profit to equity holders and non-controlling interest

Adjustment is required[2] to establish how much of the profit after tax is attributable to equity holders of the parent. This entails allocating the non-controlling interest in the subsidiary company as a percentage of the subsidiary's after-tax figure, as adjusted for any preference dividend (see note 8).

8 Calculate the share of post-taxation profits belonging to the non-controlling interest.

		£
Preferred shares – dividend on these shares:		
Non-controlling shareholders hold 80% of preferred shares		
	(80% × 3,000)	= 2,400
Common shares – % of profit after tax of the subsidiary *less* preferred share dividend		
Non-controlling shareholders hold 25% of the ordinary shares		
	25% × (14,000 – 3,000)	= 2,750
Total non-controlling interest in the profit after tax of the subsidiary		**5,150**

22.3 The statement of changes in equity (SOCE)[3]

We will prepare extracts from the consolidated statement of changes in equity for the Ante group (retained earnings columns only). In order to do this, we need the balances on retained earnings at the start of the year. These are as follows:

Ante – £69,336.
Post – £54,000.

The statement will be as follows:

	Ante group	*Non-controlling interest*	*Total*
	£	£	£
Opening balance (Notes 1 & 2)	87,336	13,500	100,836
Comprehensive income for the period (from the consolidated statement of comprehensive income)	72,264	5,150	77,414
Dividends paid (Note 3)	(40,000)	(3,650)	(43,650)
Closing balance	119,600	15,000	134,600

Note 1 – Opening balance for the Ante group

	£
Ante's retained earnings at the start of the year	69,336
The group share of Post's retained earnings since acquisition (75% × (54,000 – 30,000))	18,000
	87,336

Note 2 – Opening balance for the non-controlling shareholders

54,000 × 25% = £13,500. The relevant percentage to use is 25% because only **ordinary** shareholders will have any interest in the **retained** profits.

Note 3 – Dividends paid

In the Ante group column the dividends paid are those of the parent only. The parent company's share of Post's dividend cancels out with the parent company's investment income. The non-controlling share is dealt with in their column. The dividends paid to non-controlling shareholders are 25% × £5,000 + 80% × £3,000.

22.4 Other consolidation adjustments

In the above example we dealt with adjustments for intra-group sale of goods, unrealised profit on inventories and dividends received from a subsidiary. There are other adjustments that often appear in examination papers relating to depreciation.

Depreciation adjustment based on fair values

In the example, we assumed that the fair value of the non-current assets acquired was their book value. If the fair value was higher than the book value, we would need to adjust the Cost of sales figure. For example, assume that non-current assets with a book value of

£100,000 were acquired at a fair value of £150,000 and an estimated economic life of five years. The depreciation charge in the subsidairy would have been £20,000 (£100,000/5). The charge in the consolidation should be based on the £150,000 i.e. £30,000 (£150,000/5). A consolidation adjustment is required to charge the £10,000 difference. If there is no information as to the type of non-current asset, then this would be added to the Cost of sales figure. If the type of asset is identified, for example, as delivery lorries, then the adjustment would be made to the approppriate expense e.g. distribution costs.

Adjustment where non-current asset is acquired from a subsidiary

Digdeep plc is a civil engineering company that has a subsidairy, Heavylift plc, that manufactures digging equipment. Assume that at the beginning of the financial year Heavylift sold equipment costing £80,000 to Digdeep for £100,000, It is Digdeep's depreciation policy to depreciate at 5% using the straight line method.

On consolidation, the following adjustments are required:

(i) Revenue is reduced by £20,000 and the asset is reduced by £20,000 to bring the asset back to its cost of £80,000.

DR: Revenue	£20,000	
CR: Asset		£20,000

(ii) Revenue is then reduced by £80,000 and Cost of sales reduced by £80,000 to eliminate the intra-group sale.

DR: Revenue	£80,000	
CR: Cost of sales		£80,000

(iii) Depreciation needs to be based on the cost of £80,000 by crediting depreciation and debiting the accumulated depreciation. The depreciation charge was £5,000 (5% of £100,000); it should be £4,000 (5% of £80,000) so the adjustment is:

DR: Accumulated depreciation	£1,000
CR: Depreciation in the statement of income	£1,000

Revaluation of non-current assets

The revaluation of non-current assets to fair value on acquisition has an impact on the calculation of goodwill. The only impact on the consolidated statement of income is for the depreciation adjustment discussed above.

Any increase on a revaluation of the parent company's non-current assets will be reported under Other comprehensive income.

22.5 Dividends or interest paid by the subsidiary out of pre-acquisition profits

In the Ante Group example above, we illustrated the accounting treatment where a dividend was paid by a subsidiary out of post-acquisition profits. This showed that, when dividends and interest are received by a parent company from a company it has acquired, they will normally be credited as income in the parent company's statement of comprehensive income.

However, this treatment will not be appropriate where the dividend or interest has been paid out of profits earned by the subsidiary before acquisition. The reason is that the dividend or interest is paid out of the net assets acquired at the date of acquisition and these were paid for in the price paid for the investment. The dividend or interest received by the parent, therefore, is not income but a return of part of the purchase price, which must be reported as such in the parent's statement of financial position. This is illustrated in the Bow plc example below:

Illustration of a dividend paid out of pre-acquisition profits

Bow plc acquired 75% of the shares in Tie plc on 1 January 20X1 for £80,000 when the balance of the retained earnings of Tie was £40,000. There was no goodwill. On 10 January 20X1 Bow received a dividend of £3,000 from Tie out of the profits for the year ended 31/12/20X0. There were no inter-company transactions, other than the dividend. The summarised statements of comprehensive income for the year ended 31/12/20X1 were as follows:

	Bow	*Tie*	*Consolidated*
	£	£	£
Gross profit	130,000	70,000	200,000
Expenses	50,000	40,000	90,000
Profit from operations	80,000	30,000	110,000
Dividends received from Tie (see note)	3,000	—	—
Profit before tax	83,000	30,000	110,000
Income tax expense	24,000	6,000	30,000
Profit for the period	59,000	24,000	80,000

Note:
The £3,000 dividend received from Tie is not income and must not therefore appear in Bow statement of comprehensive income. The correct treatment is to deduct it from the investment in Tie, which will then become £77,000 (80,000 − 3,000). The consolidation would then proceed as usual.

22.6 A subsidiary acquired part of the way through the year

It would be attractive for a company whose results had not been as good as expected to acquire a profitable subsidiary at the end of the year and take its annual profit into the group accounts. However, this type of window dressing is not permitted and the group can only bring in a subsidiary's profits from the date of the acquisition. The Tight plc example below illustrates the approach.

22.6.1 Illustration of a subsidiary acquired part of the way through the year – Tight plc

The following information is available:

At date of acquisition – 30 September 20X1
Tight acquired 75% of the shares and 20% of the 5% bonds in Loose.
The purchase consideration (amount paid) was £10,000 more than book value.
The book value and fair value were the same amount.
The retained earnings of the Tight Group were £69,336.

During the year
All income and expenses are deemed to accrue evenly through the year and the dividend receivable may be apportioned to pre- and post-acquisition on a time basis.
On 30 June 20X1 Tight sold Loose goods for £4,000 plus a mark-up of one-third.

At end of financial year
The Tight Group prepares its accounts as at 31 December each year.
Half of the intra-group goods were still in inventory at the end of the year.

Set out below are the individual statements of comprehensive income of Tight and Loose together with the consolidated statement of comprehensive income for the year ended 31 December 20X1.

	Tight	*Loose*	*Consolidated*	
	£	£	£	
Revenue	200,000	120,000	**230,000**	Notes 1/2
Cost of sales	60,000	60,000	**75,000**	Note 2
Gross profit	140,000	60,000	155,000	
Expenses	59,082	30,000	**66,582**	Note 3
Interest paid on 5% bonds		10,000	**2,000**	Note 4
Interest received on Loose bonds	2,000		—	
	82,918	20,000	86,418	
Dividends received	3,600	NIL	NIL	Note 5
Profit before tax	86,518	20,000	86,418	
Income tax expense	14,004	6,000	**15,504**	Note 6
Profit for the period after tax	72,514	14,000	70,914	
Attributable to:				
Ordinary shareholders of Tight (balance)			70,039	
Non-controlling shareholders in Loose (Note 7)			875	
			70,914	

Notes:

1 **Inter-company sales**
These can be ignored as they took place before the date of acquisition.

2 **Time-apportion and aggregate the revenue and cost of sales figures.**
Group revenue includes a full year for the parent company and three months for the subsidiary (1 October to 31 December), i.e. £200,000 + (120,000 × $^3/_{12}$) = **£230,000**
Group cost of sales include a full year for the parent company and three months for the subsidiary (1 October – 31 December), i.e. £60,000 + (60,000 × $^3/_{12}$) = **£75,000**

3 **Aggregate the expense.**
This includes the whole of the parent and the time-apportioned subsidiary's expenses, i.e. £59,082 + (30,000 × $^3/_{12}$) = **£66,582**

4 **Accounting for inter-company interest**
The interest received by Tight is apportioned on a time basis: $^9/_{12}$ £2,000 = £1,500 is treated as being pre-acquisition and deducted from the cost of the investment in Loose.

The remainder (£500) is cancelled with £500 of the post-acquisition element of the interest payable by Loose. The interest payable figure in the consolidated financial statements will be the post-acquisition interest less the inter-company elimination, which represents the amount payable to the holders of 80% of the bonds.

Total interest paid 10,000 – pre-acquisition 7,500 – inter-company 500 = **£2,000**

Profit before tax

Inter-company expense items need to be eliminated. These include items such as management charges, consulting fees and interest payments. In this example we illustrate the treatment of interest. Interest is an expense which is normally deemed to accrue evenly over the year and to be apportioned on a time basis.

5 Accounting for inter-company dividends

Amount received by Tight	=	£3,600
The dividend received by Tight is apportioned on a time basis, and the pre-acquisition element is credited to the cost of investment in Tight's statement of financial position, i.e. $^9/_{12} \times$ £3,600	=	(£2,700)
The post-acquisition element is cancelled with part of the dividend paid in Loose statement of comprehensive income prior to consolidation.	=	(£900)
Amount credited to consolidated statement of comprehensive income		**NIL**

6 Aggregate the tax figures.

This includes the whole of the parent's tax and the time-apportioned part of the subsidiary's tax, i.e. £14,004 + (6,000 $\times$ $^3/_{12}$)	=	**£15,504**

The group taxation is that of Tight plus $^3/_{12}$ of Loose.

7 Calculate the share of post-acquisition consolidated profits belonging to the non-controlling interest.

As only the post-acquisition proportion of the subsidiary's profit after tax has been included in the consolidated statement of comprehensive income, the amount deducted as the non-controlling interest in the profit after tax is also time-apportioned, i.e. 25% $\times$ (14,000 $\times$ $^3/_{12}$)	=	£875

22.7 Published format statement of comprehensive income

The statement of comprehensive income follows the classification of expenses by function as illustrated in IAS 1:

	£
Revenue	230,000
Cost of sales	75,000
Gross profit	155,000
Distribution costs	xxxxxx
Administrative expense	xxxxxx
	66,582
	88,418
Finance cost	2,000
	86,418
Income tax expense	15,504
Profit for the period	70,914
Attributable to:	
Equity holders of the parent	70,039
Non-controlling interest	875

22.8 Consolidated statements of cash flows

Statements of cash flow are explained in Chapter 26 for a single company. A consolidated statement of cash flows differs from that for a single company in two respects: there are additional items such as dividends paid to non-controlling interests; and adjustments may be required to the actual amounts to reflect the assets and liabilities brought in by the subsidiary.

22.8.1 Additional items when subsidiary acquired during the year

Adjustments are required if the closing statement of financial position items have been increased or reduced as a result of **non-cash movements**. Such movements occur if there has been a purchase of a subsidiary to reflect the fact that the asset and liabilities from the new subsidiary have not necessarily resulted from cash flows. The following illustrates such adjustments in relation to a subsidiary acquired at the end of the financial year where the net assets of the subsidiary were:

Net assets acquired	*£000*	*In consolidated statement of cash flows the effect will be:*
Working capital:		
Inventory	10	Reduce inventory increase
Trade payables	(12)	Reduce trade payables increase
Non-current assets:		
Vehicles	20	Reduce capital expenditure
Cash/bank:		
Cash	5	Reduce amount paid to acquire subsidiary in investing section
Net assets acquired	23	

Let us assume that the consideration for the acquisition were as follows:

Consideration:		
Shares	10	Reduce share cash inflow
Share premium	10	Reduce share cash inflow
Cash	3	Payment to acquire subsidiary in investing section
	23	

The consolidated statement of cash flows can then be prepared using the indirect method.

Statement of cash flows using the indirect method

Cash flows from operating activities		*£000*	*£000*
Net profit before tax		500	
Adjustments for:			
Depreciation		102	
Operating profit before working capital changes		602	
Increase in trade and other receivables		(260)	
Increase in inventories	(400)		
***Less*: inventory brought in on acquisition**	**10**	**(390)**	
Decrease in trade payables	(40)		
***Add*: trade payables brought in on acquisition**	**(12)**	**(52)**	
Cash generated from operations		160	
Income taxes paid (200 + 190 − 170)		(220)	
Net cash from operating activities			(60)
Cash flows from investing activities			
Purchase of property, plant and equipment	(563)		
***Less*: vehicles brought in on acquisition**	**20**	**(543)**	
Payment to acquire subsidiary		(3)	
Cash acquired with subsidiary		5	
Net cash used in investing activities			(541)
Cash flows from financing activities			
Proceeds from issuance of share capital	300		
***Less*: shares issued on acquisition not for cash**	**(20)**	**280**	
Dividends paid (*from statement of comprehensive income*)		(120)	
Net cash from financing activities			160
Net decrease in cash and cash equivalents			**(441)**
Cash and cash equivalents at the beginning of the period			**72**
Cash and cash equivalents at the end of the period			**(369)**

Supplemental disclosure of acquisition

	£
Total purchase consideration	23,000
Portion of purchase consideration discharged by means of cash or cash equivalents	3,000
Amount of cash and cash equivalents in the subsidiary acquired	5,000

Summary

The retained earnings of the subsidiary brought forward is divided into pre-acquisition profits and post-acquisition profits – the group share of the former are used in the goodwill calculation, and the share of the latter are brought into the consolidated shareholders' equity.

Revenue and cost of sales are adjusted in order to eliminate intra-group sales and unrealised profits.

Finance expenses and income are adjusted to eliminate intra-group payments of interest and dividends.

The non-controlling interest in the profit after tax of the subsidiary is deducted to arrive at the profit for the year attributable to the equity holders of the parent.

The amounts paid as dividends to the parent company's shareholders are shown as deductions in the consolidated statement of changes in equity.

If a subsidiary is acquired during a financial year, the items in its statement of comprehensive income require apportioning. In the illustration in the text we assumed that trading was evenly spread throughout the year – in practice you would need to consider any seasonal patterns that would make this assumption unrealistic, remembering that the important consideration is that the group accounts should only be credited with profits arising whilst the subsidiary was under the parent's control.

REVIEW QUESTIONS

1 Explain why the dividends deducted from the group in the statement of changes in equity are only those of the parent company.

2 Explain how unrealised profits arise from transactions between companies in a group and why it is important to remove them.

3 Explain why it is necessary to apportion a subsidiary's profit or loss if acquired part-way through a financial year.

4 Explain why dividends paid by a subsidiary to a parent company are eliminated on consolidation.

5 Give five examples of inter-company income and expense transactions that will need to be eliminated on consolidation and explain why each is necessary.

6 A shareholder was concerned that following an acquisition the profit from operations of the parent and subsidiary were less than the aggregate of the individual profit from operations figures. She was concerned that the acquisition, which the directors had supported as improving earnings per share, appeared to have reduced the combined profits. She wanted to know where the profits had gone.

Give an explanation to the shareholder.

EXERCISES

An extract from the solution is provided on the Companion website (www.pearsoned.co.uk/elliott-elliott) for exercises marked with an asterisk (*).

* Question 1

Bill plc acquired 80% of the common shares and 10% of the preferred shares in Ben plc on 31 December three years ago when Ben's accumulated retained profits were £45,000. During the year Bill sold Ben goods for £8,000 plus a mark-up of 50%. Half of these goods were still in stock at the end of the year. There was goodwill impairment loss of £3,000. Non-controlling interests are measured using method 1.

The statements of comprehensive income of the two companies for the year ended 31 December 20X1 were as follows:

	Bill	*Ben*
	£	*£*
Revenue	300,000	180,000
Cost of sales	90,000	90,000
Gross profit	210,000	90,000
Expenses	88,623	60,000
	121,377	30,000
Dividends received – common shares	6,000	—
Dividends received – preferred shares	450	—
Profit before tax	127,827	30,000
Income tax expense	21,006	9,000
Profit for the period	106,821	21,000

Required:
Prepare a consolidated statement of comprehensive income for the year ended 31 December 20X1.

Question 2

Morn Ltd acquired 90% of the shares in Eve Ltd on 1 January 20X1 for £90,000 when Eve Ltd's accumulated profits were £50,000. On 10 January 20X1 Morn Ltd received a dividend of £10,800 from Eve Ltd out of the profits for the year ended 31/12/20X0. On 31/12/20X1 Morn increased its non-current assets by £30,000 on revaluation. The summarised statements of comprehensive income for the year ended 31/12/20X1 were as follows:

	Morn	*Eve*
	£	*£*
Gross profit	360,000	180,000
Expenses	120,000	110,000
	240,000	70,000
Dividends received from Eve Ltd	10,800	—
Profit before tax	250,800	70,000
Income tax expense	69,000	18,000
Profit for the period	181,800	52,000

There were no inter-company transactions, other than the dividend. There was no goodwill.

Required:
Prepare a consolidated statement of comprehensive income for the year ended 31 December 20X1.

Question 3

River plc acquired 90% of the common shares and 10% of the 5% bonds in Pool Ltd on 31 March 20X1. All income and expenses are deemed to accrue evenly through the year. On 31 January 20X1 River sold Pool goods for £6,000 plus a mark up of one-third. 75% of these goods were still in stock at the end of the year. There was a goodwill impairment loss of £4,000. On 31/12/20X1 River increased its non-current assets by £15,000 on revaluation. Non-controlling interests are measured using method 1. Set out below are the individual statements of comprehensive income of River and Pool:

Statements of comprehensive income for the year ended 31 December 20X1

	River	*Pool*
	£	£
Net turnover	100,000	60,000
Cost of sales	30,000	30,000
Gross profit	70,000	30,000
Expenses	20,541	15,000
Interest payable on 5% bonds		5,000
Interest receivable on Pool Ltd bonds	500	
	49,959	10,000
Dividends received	2,160	NIL
Profit before tax	52,119	10,000
Income tax expense	7,002	3,000
Profit for the period	45,117	7,000

Required:
Prepare a consolidated statement of comprehensive income for the year ended 31 December 20X1.

Question 4

The statements of financial position of Mars plc and Jupiter plc at 31 December 20X2 are as follows:

	Mars	*Jupiter*
	£	£
ASSETS		
Non-current assets at cost	550,000	225,000
Depreciation	220,000	67,500
	330,000	157,500
Investment in Jupiter	187,500	
Current assets		
Inventories	225,000	67,500
Trade receivables	180,000	90,000
Current account – Jupiter	22,500	
Bank	36,000	18,000
	463,500	175,500
Total assets	**981,000**	**333,000**
EQUITY AND LIABILITIES		
Capital and reserves		
£1 common shares	196,000	90,000
General reserve	245,000	31,500
Retained earnings	225,000	135,000
	666,000	256,500
Current liabilities		
Trade payables	283,500	40,500
Taxation	31,500	13,500
Current account – Mars		22,500
	315,000	76,500
Total equity and liabilities	**981,000**	**333,000**

Statements of comprehensive income for the year ended 31 December 20X2

	£	£
Sales	1,440,000	270,000
Cost of sales	1,045,000	135,000
Gross profit	395,000	135,000
Expenses	123,500	90,000
Dividends received from Jupiter	9,000	NIL
Profit before tax	280,500	45,000
Income tax expense	31,500	13,500
Profit for the period	249,000	31,500
Dividends paid	180,000	11,250
	69,000	20,250
Retained earnings brought forward from previous years	156,000	114,750
	225,000	135,000

Mars acquired 80% of the shares in Jupiter on 1 January 20X0 when Jupiter's retained earnings were £80,000 and the balance on Jupiter's general reserve was £18,000. Non-controlling interests are measured using method 1. During the year Mars sold Jupiter goods for £18,000 which represented cost plus 50%. Half of these goods were still in stock at the end of the year.

During the year Mars and Jupiter paid dividends of £180,000 and £11,250 respectively. The opening balances of retained earnings for the two companies were £156,000 and £114,750 respectively.

Required:
Prepare a consolidated statement of comprehensive income for the year ended 31/12/20X2, a statement of financial position as at that date, and a consolidated statement of changes in equity. Also prepare the retained earnings columns of the consolidated statement of changes in equity for the year.

* Question 5

The statements of financial position of Red Ltd and Pink Ltd at 31 December 20X2 are as follows:

	Red $	*Pink* $
ASSETS		
Non-current assets	225,000	100,000
Depreciation	80,000	30,000
	145,000	70,000
Investment in Pink Ltd	110,000	
Current assets		
Inventories	100,000	30,000
Trade receivables	80,000	40,000
Current account – Pink Ltd	10,000	
Bank	16,000	8,000
	206,000	78,000
Total assets	**461,000**	**148,000**

EQUITY AND LIABILITIES		
Capital and reserves		
$1 common shares	176,000	40,000
General reserve	20,000	14,000
Revaluation reserve	25,000	
Retained earnings	100,000	60,000
	321,000	114,000
Current liabilities		
Trade payables	125,996	18,000
Taxation payable	14,004	6,000
Current account – Red Ltd		10,000
	140,000	34,000
Total equity and liabilities	**461,000**	**148,000**

Statements of comprehensive income for the year ended 31 December 20X2

	$	$
Sales	200,000	120,000
Cost of sales	60,000	60,000
Gross profit	140,000	60,000
Expenses	59,082	40,000
Dividends received	3,750	NIL
Profit before tax	84,668	20,000
Income tax expense	14,004	6,000
	70,664	14,000
Surplus on revaluation	25,000	—
Total comprehensive income	**95,664**	**14,000**

Red Ltd acquired 75% of the shares in Pink Ltd on 1 January 20X0 when Pink Ltd's retained earnings were $30,000 and the balance on Pink's general reserve was $8,000. The fair value of the non-controlling interest at the date was £32,000. Non-controlling interests are to be measured using method 2.

On 31 December 20X2 Red revalued its non-current assets. The revaluation surplus of £25,000 was credited to the revaluation reserve.

During the year Pink sold Red goods for $9,000 plus a mark-up of one-third. Half of these goods were still in inventory at the end of the year. Goodwill suffered an impairment loss of 20%.

Required:
Prepare a consolidated statement of comprehensive income for the year ended 31/12/20X2 and a statement of financial position as at that date.

Question 6

Alpha has owned 80% of the equity shares of Beta since the incorporation of Beta. On 1 July 20X6 Alpha purchased 60% of the equity shares of Gamma. The statements of comprehensive income and summarised statements of changes in equity of the three entities for the year ended 31 March 20X7 are given below:

Statement of comprehensive income

	Alpha	*Beta*	*Gamma*
	$'000	*$'000*	*$'000*
Revenue (Note 1)	180,000	120,000	106,000
Cost of sales	(90,000)	(60,000)	(54,000)
Gross profit	90,000	60,000	52,000
Distribution costs	(9,000)	(8,000)	(8,000)
Administrative expenses	(10,000)	(9,000)	(8,000)
Investment income (Note 2)	26,450	Nil	Nil
Finance cost	(10,000)	(8,000)	(5,000)
Profit before tax	87,450	35,000	31,000
Income tax expense	(21,800)	(8,800)	(7,800)
Net profit for the period	65,650	26,200	23,200

Summarised statements of changes in equity

Balance at 1 April 20X6	152,000	111,000	102,000
Net profit for the period	65,650	26,200	23,200
Dividends paid on 31 January 20X7	(30,000)	(13,000)	(15,000)
Revaluation of non-current assets – 20,000 –			
Balance at 31 March 20X7	187,650	144,200	110,200

Notes to the financial statements

Note 1 – Inter-company sales

Alpha sells products to Beta and Gamma, making a profit of 30% on the cost of the products sold. All the sales to Gamma took place in the post-acquisition period. Details of the purchases of the products by Beta and Gamma, together with the amounts included in opening and closing inventories in respect of the products, are given below:

	Purchased in year	*Included in opening inventory*	*Included in closing inventory*
	$'000	*$'000*	*$'000*
Beta	20,000	2,600	3,640
Gamma	10,000	Nil	1,950

Note 2 – Investment income

Alpha's investment income includes dividends received from Beta and Gamma and interest receivable from Beta. The dividend received from Gamma has been credited to the statement of comprehensive income of Alpha without time apportionment. The interest receivable is in respect of a loan of $60 million to Beta at a fixed rate of interest of 6% per annum. The loan has been outstanding for the whole of the year ended 31 March 20X7.

Note 3 – Details of acquisition of shares in Gamma

On 1 July 20X6 Alpha purchased 15 million of Gamma's issued equity shares by a share exchange. Alpha issued 4 new equity shares for every 3 shares acquired in Gamma. The market value of the shares in Alpha and Gamma at 1 July 20X6 was $5 and $5.50 respectively. The non-controlling interest in Gamma is measured using method 1.

The fair values of the net assets of Gamma closely approximated to their carrying values in Gamma's financial statements with the exception of the following items:

(i) A property that had a carrying value of $20 million at the date of acquisition had a market value of $30 million. $16 million of this amount was attributable to the building, which had an estimated useful future economic life of 40 years at 1 July 20X6. In the year ended 31 March 20X7 Gamma had charged depreciation of $200,000 in its own financial statements in respect of this property.

(ii) Plant and equipment that had a carrying value of $6 million at the date of acquisition and a market value of $8 million. The estimated useful future economic life of the plant at 1 July 20X6 was 4 years. None of this plant and equipment had been sold or scrapped prior to 31 March 20X7.

(iii) Inventory that had a carrying value of $3 million at the date of acquisition had a fair value of $3.5 million. This entire inventory had been sold by Gamma prior to 31 March 20X7.

Note 4 – Other information

(i) Gamma charges depreciation and impairment of assets to cost of sales.

(ii) On 31 March 20X7 the directors of Alpha computed the recoverable amount of Gamma as a single cash-generating unit. They concluded that the recoverable amount was $150 million.

(iii) When the directors of Beta and Gamma prepared the individual financial statements of these companies no impairment of any assets of either company was found to be necessary.

(iv) On 31 March 20X7 Beta revalued its non-current assets. This resulted in a surplus of £20,000 which was credited to Beta's revaluation reserve.

Required:
Prepare the consolidated statement of comprehensive income and consolidated statement of changes in equity of Alpha for the year ended 31 March 20X7. Notes to the consolidated statement of comprehensive income are not required. Ignore deferred tax.

Question 7

H Ltd has one subsidiary, S Ltd. The company has held a controlling interest for several years. The latest financial statements for the two companies and the consolidated financial statements for the H Group are as shown below:

Statements of comprehensive income for the year ended 30 September 20X4

	H Ltd	*S Ltd*	*H Group*
	£000	*£000*	*£000*
Turnover	4,000	2,200	5,700
Cost of sales	(1,100)	(960)	(1,605)
	2,900	1,240	4,095
Administration	(420)	(130)	(550)
Distribution	(170)	(95)	(265)
Dividends received	180	—	—
Profit before tax	2,490	1,015	3,280
Income tax	(620)	(335)	(955)
Profit after tax	1,870	680	2,325
Attributable to:			
Equity shareholders of H Ltd			2,155
Non-controlling shareholders in S Ltd			170
			2,325

Statements of financial position at 30 September 20X4

	H Ltd		*S Ltd*		*H Group*	
	£000	*£000*	*£000*	*£000*	*£000*	*£000*
Non-current assets:						
Tangible	7,053		2,196		9,249	
Investment in S Ltd	1,700	8,753	—	2,196	—	9,249
Current assets:						
Inventory	410		420		785	
Receivables	535		220		595	
Bank	27	972	19	659	46	1,426
Current liabilities:						
Payables	(300)		(260)		(355)	
Dividend to non-controlling interest	—		—		(45)	
Taxation	(605)	(905)	(375)	(635)	(980)	(1,380)
		8,820		2,220		9,295

	H Ltd	*S Ltd*	*H Group*
	£000	*£000*	*£000*
Share capital	4,500	760	4,500
Retained earnings	4,320	1,460	4,240
	8,820	2,220	8,740
Non-controlling interest	—	—	555
	8,820	2,220	9,295

Goodwill of £410,000 was written off at the date of acquisition following an impairment review.

Required:

(a) Calculate the percentage of S Ltd which is owned by H Ltd.

(b) Calculate the value of sales made between the two companies during the year.

(c) Calculate the amount of unrealised profit which had been included in the inventory figure as a result of inter-company trading and which had to be cancelled on consolidation.

(d) Calculate the value of inter-company receivables and payables cancelled on consolidation.

(e) Calculate the balance on S Ltd's retained earnings when H Ltd acquired its stake in the company. Non-controlling interests are measured using Method 1.

(CIMA)

Question 8

The following are the financial statements of White and its subsidiary Brown as at 30 September 20X9

Statement of income for the year ended 30 September 20X9	*White*	*Brown*
	£000	*£000*
Sales revenue	245,000	95,000
Cost of sales	(140,000)	(52,000)
Gross profit	105,000	43,000
Distribution costs	(12,000)	(10,000)
Admin expenses	(55,000)	(13,000)
Profit from operations	38,000	20,000
Dividend from Brown	7,000	—
Profit before tax	45,000	20,000
Tax	(13,250)	(5,000)
Net profit for the year	31,750	15,000

Statements of financial position as at 30 September 20X9	*White*	*Brown*
	£000	*£000*
Non-current assets:		
Property, plant & equipment	110,000	40,000
Investments – 21 million shares in Brown	24,000	—
Current assets:		
Inventory	13,360	3,890
Trade receivables & dividend receivable	14,640	6,280
Bank	3,500	2,570
	165,500	52,740
Equity & reserves:		
Ordinary shares of £1 each	100,000	30,000
Reserves	9,200	1,000
Retained earnings	27,300	9,280
	136,500	40,280
Current liabilities:		
Trade Payables	9,000	2,460
Dividend declared	20,000	10,000
	165,500	52,740

The following information is also available:

(i) White purchased its ordinary shares in Brown on 1 September 20X4 when Brown had credit balances on reserves of £0.5 million and on retained earnings of £1.5 million.

(ii) At 1 September 20X8 goodwill on the acquisition of Brown was £960,000. The impairment review at 30 September 20X9 reduced this to £800,000.

(iii) During the year ended 30 September 20X9 White sold goods which originally cost £12 million to Brown and were invoiced to Brown at cost plus 40%. Brown still had 30% of these goods in inventory as at 30 September 20X9.

(iv) Brown owed White £1.5 million at 30 September 20X9 for goods supplied during the year.

Required:

(a) Calculate the goodwill arising at the date of acquisition.

(b) Prepare the Consolidated Statement of Income for the year ended 30 September 20X9.

Question 9

Hyson plc acquired 75% of the shares in Green plc on 1 January 20X0 for £6 million when Green plc's accumulated profits were £4.5 million. At acquisition, the fair value of Green's non-current assets were £1.2 million in excess of their carrying value. The remaining life of these non-current assets is six years.

The summarised statements of comprehensive income for the year ended 31.12.X0 were as follows:

	Hyson	*Green*
	£000	*£000*
Revenue	23,500	6,400
Cost of sales	16,400	4,700
Gross profit	7,100	1,700
Expenses	4,650	1,240
Profit before tax	2,450	460
Income tax expense	740	140
Profit for the period	1,710	320

There were no inter-company transactions. Depreciation of non-current assets is charged to cost of sales.

Required:
Prepare a consolidated statement of comprehensive income for the year ended 31 December 20X0.

Question 10

Forest plc acquired 80% of the ordinary shares of Bulwell plc some years ago. At acquisition, the fair values of the assets of Bulwell plc were the same as their carrying value. Bulwell plc manufacture plant and equipment.

On 1 January 20X3, Bulwell sold an item of plant & equipment to Forest plc for $2 million. Forest plc depreciate plant and equipment at 10% per annum on cost, and charge this expense to cost of sales. Bulwell plc made a gross profit of 30% on the sale of the plant and equipment to Forest plc.

The income statements of Forest and Bulwell for the year ended 31 December 20X3 are:

	Forest	*Bulwell*
	$000	*$000*
Revenue	21,300	8,600
Cost of sales	14,900	6,020
Gross profit	6,400	2,580
Other operating expenses	3,700	1,750
Profit before tax	2,700	830
Taxation	820	250
Profit after tax	1,880	580

Required:
Prepare an income statement for the Forest plc group for the year ended 31 December 20X3.

References

1 IAS 27 *Consolidated and Separate Financial Statements*, IASB, revised 2008, para. 20.
2 *Ibid*., para. 28.
3 IAS 1 *Presentation of Financial Statements*, IASB, revised 2007, Implementation Guidance.