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CONSOLIDATED AND SEPARATE FINANCIAL STATEMENTS

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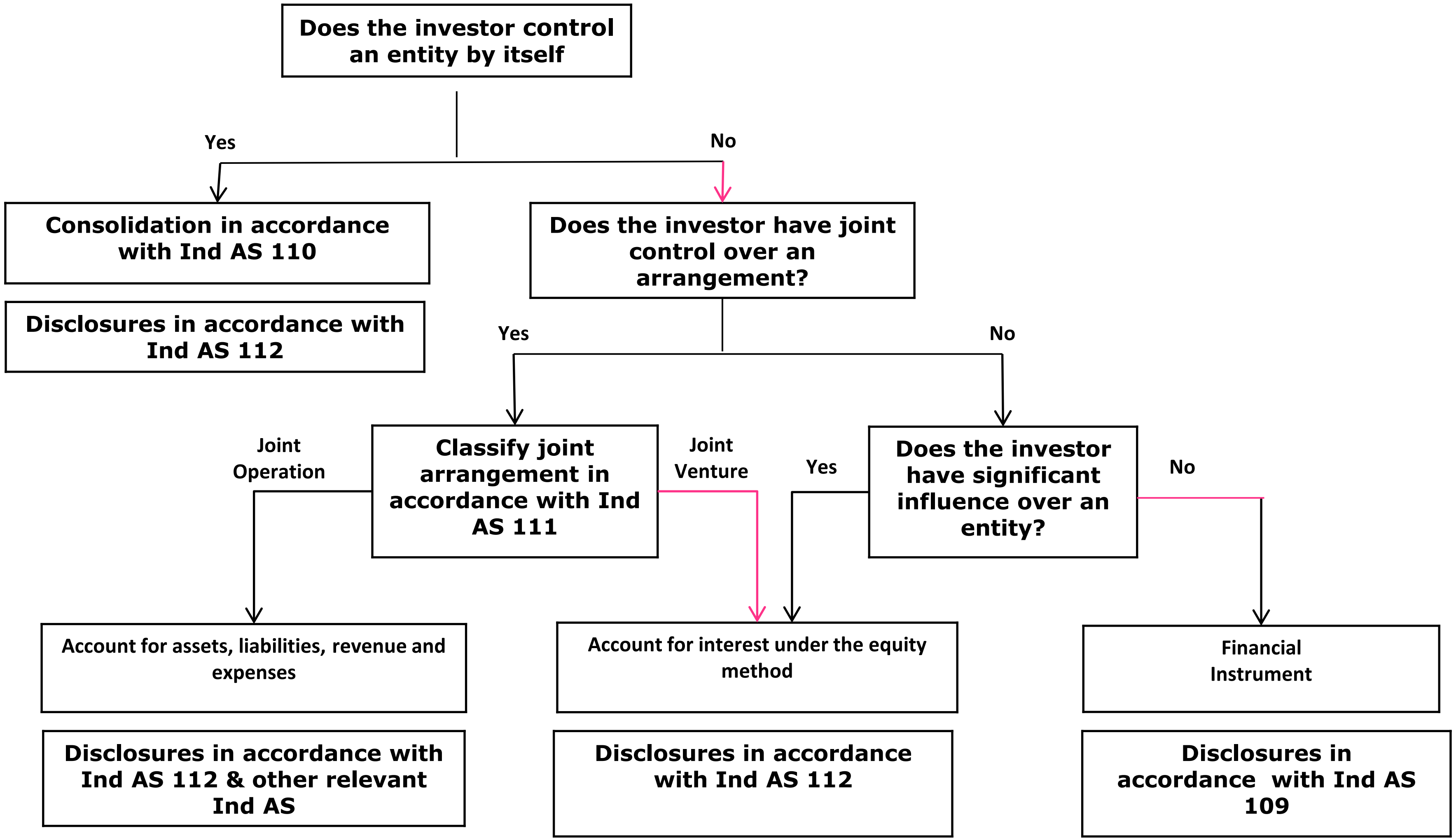
Interaction between Ind-AS110, 111, 112 & Ind-AS 28



Ind-AS 110- Scope, exemption and exceptions

Exemption from preapring consolidated financial statements for a parent if:

Exemption from preapring consolidated financial statements for a parent if:

- it is a wholly-owned subsidiary, or is a partially-owned subsidiary of another entity and all its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting CFS;
- its debt/ equity instruments are not traded in a public market;
- it did not file/in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; and
- its ultimate or any intermediate parent produces CFS that are available for public use and comply with Ind-AS

Scope exclusion

- Post employment benefit plans (for e.g. Gratuity trust) and other long-term employee benefit plan to which Ind-AS 19 applies

Financial statements

Individual financial statements are prepared by an entity that does not have a subsidiary, an associate or a joint venture’s interest in a joint venture

Separate financial statements are statements of an investor where investments in the subsidiary, joint venture and associate are accounted for at cost or in accordance with Ind AS 109, Financial Instruments

Consolidated financial statements are the financial statements of a group in which the assets, liabilities, equity, income and cash flows of the parent and its subsidiaries are presented as those of a single entity. Financial statements in which equity method is applied for investments in joint ventures and associates and there is no subsidiary are technically called 'Economic Entity Financial Statements'. However, in India, the 'Economic Entity Financial Statements' (EEFS) are also termed as Consolidated Financial Statements.

Key definitions

Parent
An entity that controls one or more entities.

Subsidiary
An entity that is controlled by another entity

Control over an investee
An investor controls an investee when the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee

Non-controlling interest
Equity in a subsidiary not attributable, directly or indirectly, to a parent.

Power
Existing rights that give the current ability to direct the relevant activities.

Substantive rights are those rights that an investor holds that gives it current ability to direct the investee's relevant activities. In order for a right to be substantive, the holder must have the practical ability to exercise the right

Key definitions

Protective rights
Rights designed to protect the interest of the party holding those rights without giving that party power over the entity to which those rights relate.
An investor that only holds protective rights, which meet this definition, has no power over an investee and consequently does not control the investee.

Relevant activities
For the purpose of this Ind AS, relevant activities are activities of the investee that significantly affect the investee's returns

Separate Vehicle
A separately identifiable financial structure, including separate legal entities or entities recognised by statute, regardless of whether those entities have a legal personality.

Key definitions

An associate is an entity over which the investor has significant influence.

Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control of those policies.

Equity method is a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition change in the investor's share of the investee's net assets. The investor's profit or loss includes its share of the investee's profit or loss and the investor's other comprehensive income includes its share of the investee's other comprehensive income.

Key definitions

Joint arrangement is an arrangement of which two or more parties have joint control

Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

A joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement.

A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.

A joint venturer is a party to a joint venture that has joint control of that joint venture.

Investment entity

- An entity that:
- (a) obtains funds from one or more investors for purpose of providing those
- investor(s) with investment management services;
- (b) commits to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and
- (c) measures and evaluates performance of substantially all of its investments
- on a fair value basis.

Assessing control

Assessing control

Identity power

Power
Determine which party if any, has power, that is, the current ability to direct relevant activities. Power arises from the rights which may include

- Voting rights
- Potential voting rights (e.g. Options or convertible instruments)
- Rights to appoint key personnel
- Decision making rights within a management contract.
- De-facto control
- Casting vote

However power does not arise from protective rights.

Assess Return

Returns
Assess whether the investor is exposed or has rights to variable returns from its involvement with the investee. Returns can be positive, negative, or both.

Example of returns include

- Dividends
- Remuneration
- Residual interest
- Tax benefits
- Economies of scale, cost savings, scarce product, proprietary knowledge, synergies.

Evaluate linkage

Linkage (Delegated rights)
Evaluate whether the investor has the ability to use its power to affect the investor's returns from its involvement with the investee applicable. Determine whether the investor is a principal or an agent considering

- Scope of its authority
- Rights held by other parties (Rights to remove a decision-maker)
- Remuneration
- Exposure to variability from other interests

Understand purpose and design of investee
Continuous assessment

New definition of control

Identifying relevant activities

Relevant activities are those that significantly affect the investee's returns

- Examples:
  - Establishing operating, capital and financing policies
  - Determining funding structure or obtaining funding
  - Appointing, remunerating, and terminating employment of service providers or key management personnel
- Understand purpose and design of the investee
- If two investors direct different relevant activities
  - Identify which investor can direct the activities that ***most*** significantly affect returns

Potential voting rights

Evaluation	Non-substantive	Depends on facts and circumstances	Substantive
Exercise price	Deeply-out-of -the-money	Out-of-the-money	At market (fair value) or in-the-money
Financial ability to exercise	Holder has no financial ability	Holder would have to raise financing	Holder has cash or financing readily available
Exercise period	Not exercisable	Exercisable before decisions need to be made	Currently exercisable

Out-of-the-money (but not deeply) <u>Judgement will be needed to assess whether cost of paying more than fair value is worth the potential benefits of exercise including exposures to variable returns that are associated with exercising that option</u>

Power – Protective rights

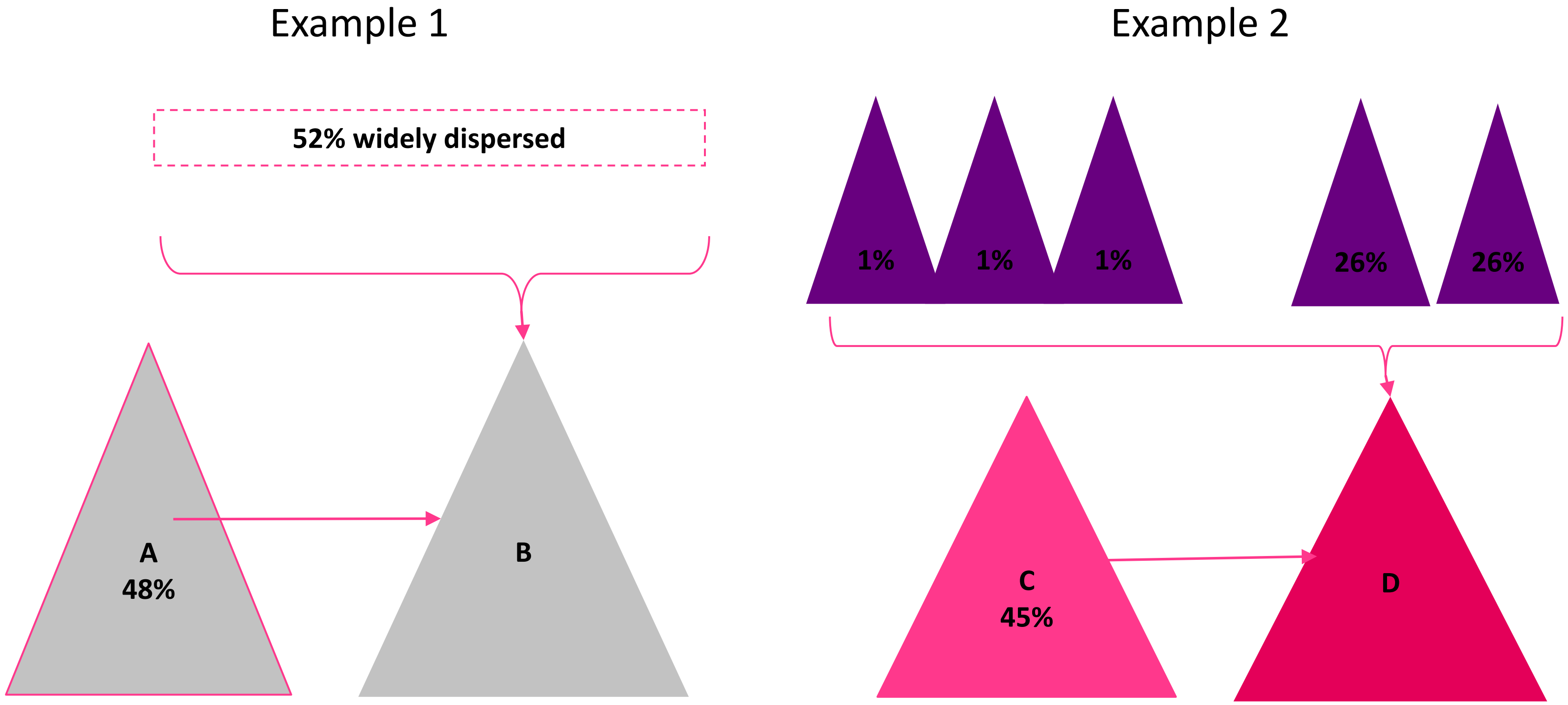
- Protective rights do not give power
- When are rights merely protective rights?
  - Fundamental changes in the activities of an investee
  - Only apply in exceptional circumstances
- Examples of protective rights include the right to:
  - Restrict an investee from undertaking activities that could significantly change the credit risk of the investee
  - Approve an investee's capital expenditures (greater than the amount spent in the ordinary business)
- Protective rights do not prevent another investor from having control

Power – De facto control

- An investor may have the power with less than half of the voting rights
- Consider facts and circumstances:
  - Contractual rights arising from other arrangements
  - Size of the investor’s holding of voting rights relative to the size and dispersion of other vote holders
    - Voting rights (absolute amount)
    - Voting rights relative to other vote holders
    - Number of other vote holders that would need to act together
  - Potential voting rights
  - Additional facts & circumstances
    - Voting patterns at previous shareholders meetings

Power – De facto control

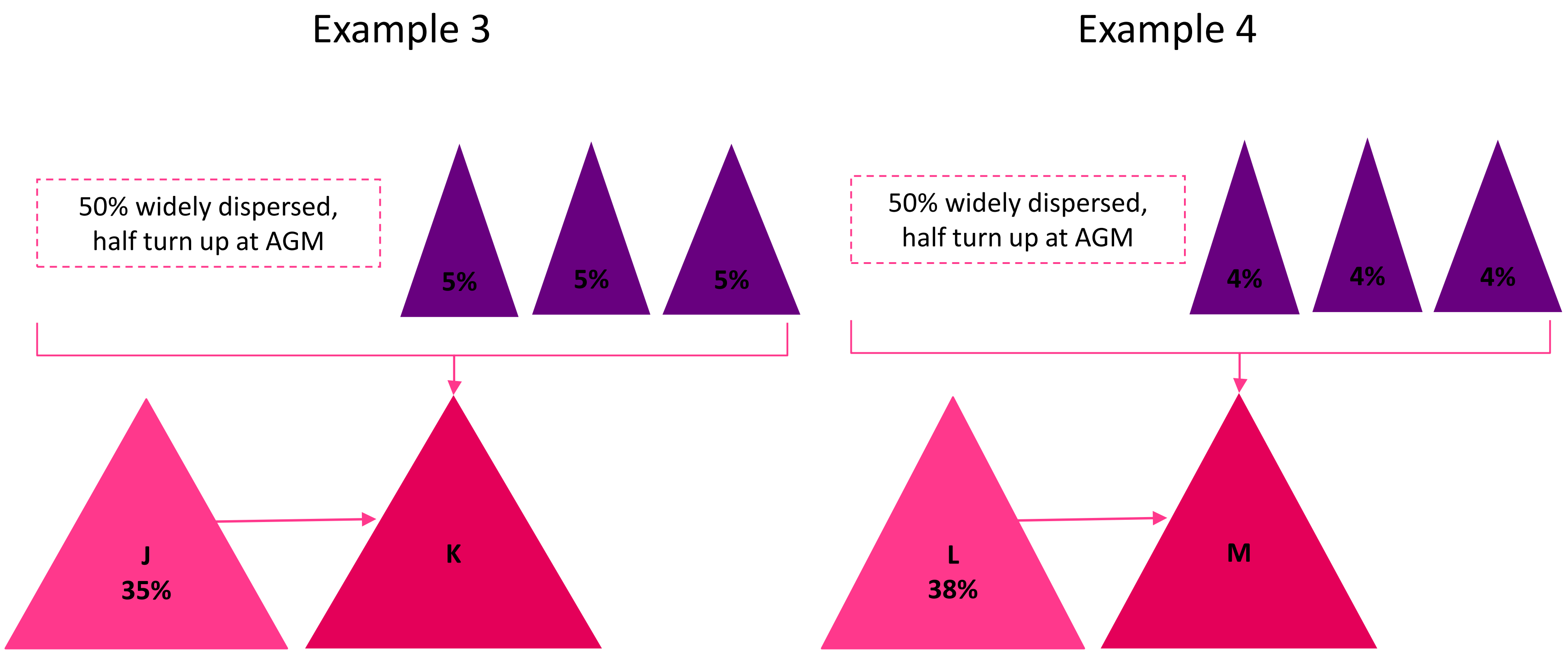
Examples 1 and 2



A has power

C does not have power

Power – De facto control
Examples 3 and 4



Definition of control- Assessing Returns

Definition of control
Assessing returns

Returns can be only positive, only negative or positive and negative, but must have the potential to vary as a result of the investee's performance

- Examples:
  - Dividends, distributions of economic benefits, changes in the value of an investment
  - Remuneration, fees, residual interests, tax benefits, exposure from providing support
  - Synergies, cost savings, economies of scale, scarce resources, proprietary knowledge
- Other parties may also share in the returns, e.g. NCI

Is there a link between power & returns?

Investment entities

Documents that indicate entity's objective are:

- memorandum
- publications distributed by the entity and
- other corporate or partnership documents.

Entity may also participate in many investment related activities

For assessing 'Investment entity', an entity also has to consider some typical characteristics as declared below (however absence of any characteristic does not necessarily disqualify an entity from being an investment entity)

a. Whether it has more than one investment
b. whether it has more than one investor
c. Whether its Investors are not related parties of the entity
d. Whether it has ownership interests in the form of equity or similar interest

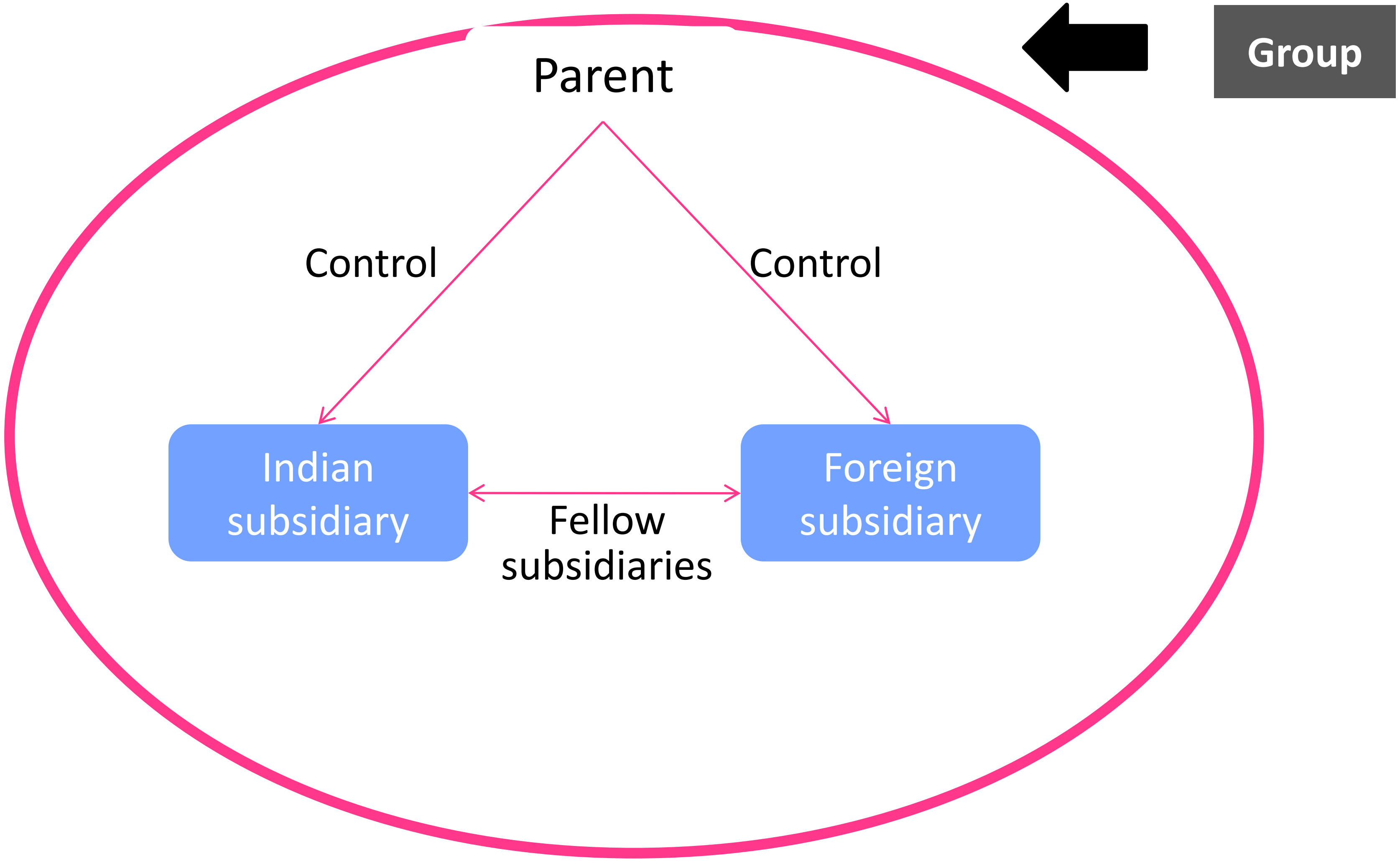
Continuous assessment

Continuous assessment

- Reassess if facts and circumstances suggest change to one of criteria of control
- Examples:
  - Changes to how activities are directed
  - Changes in exposure to variable returns
- Market conditions change:
  - If affect one of control criteria – re-evaluate control
  - If do not affect one of control criteria – no re-evaluation

Accounting requirements- Consolidation procedures

What is a ‘group’?



Financial statements prepared by parent

Separate financial statements	Consolidated financial statements
investments accounted for at: - cost, or - in accordance with Ind AS 109	- financial statements of a group - parent and subsidiaries presented as a single economic entity

Components of consolidated financial statements

- consolidated balance sheet
- consolidated statement of profit or loss and other comprehensive income
- consolidated statement of changes in equity
- consolidated statement of cash flows
- notes comprising significant accounting policies and other explanatory information

Accounting requirements -Consolidation Procedures

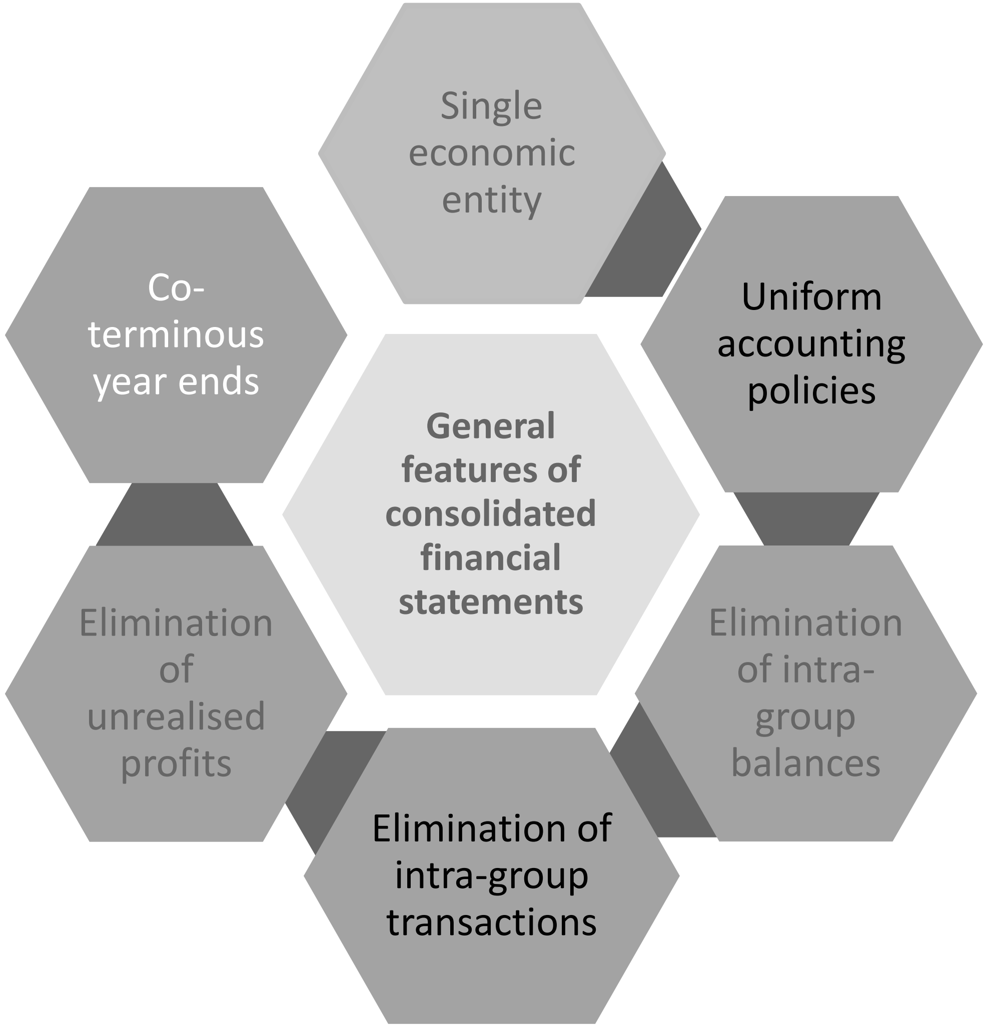
- Mostly the same however relevant Ind AS to be followed:
  - Ind AS 103 explains how to account for any <u>related goodwill</u>
  - Ind AS 12 Income Taxes applies to temporary differences that arise from the elimination of profits and losses resulting from intragroup transactions

- **Measurement:**
  - From the date it gains control until the date when the entity ceases to control the subsidiary. Potential voting rights are not considered, unless it gives access to the returns.
  - Combine like items of assets, liabilities, equity, income, expenses and cash flows of the parent with those of its subsidiaries.
  - offset (eliminate) the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary
  - eliminate in full intragroup assets and liabilities, equity, income, expenses and cashflows relating to transactions between entities of the group (profits or losses resulting from intragroup transactions that are recognized in assets, such as inventory and fixed assets, are eliminated in full).
  - Uniform accounting policies

Accounting requirements -Consolidation Procedures

- Subsidiary’s losses allocated between the parent and NCI, even if this results in deficit NCI balance.
- NCI presented in the consolidated balance sheet within equity, separately from the equity of the owners of the parent.
- Profit/loss attributable to NCI in the group P&L separately presented.
- Changes in the ownership interest of a subsidiary not resulting in loss of control accounted for as an equity transaction and do not impact Goodwill/ P&L.
- In calculating the gain/loss arising from the loss of control, retained interest in the former subsidiary is measured at its fair value at the date when control is lost.
- Intra-group balances and transactions, including income, expenses and dividends, are eliminated in full. Deferred tax should be calculated on temporary differences that arise from the elimination of profits and losses resulting from intra-group transactions.

Features of consolidated financial statements



Different reporting date of subsidiary

- **Step I**: Prepare special statements of subsidiary as at the same date as the group
- **Step II**: If step I is impracticable, use financial statements of subsidiary subject to:
  - difference ≤ 3 months
  - adjustments for effects of significant transactions/ events between these dates

Reporting date
Example

Query

- Parent is preparing its Ind AS consolidated financial statements (CFS) for the year ended 31 March 20X8. the financial year of one of its subsidiary ends on 31 December 20X7. In February 20X8, the subsidiary sold a property held at cost and realizing substantial profit which is material to the CFS of the parent.

Response

- Parent should obtain additional information for subsidiary, such as a reporting package or appropriately prepared management accounts, covering:
- the 3 month period from 1 January 20X8 to 31 March 20X8
- the comparative 3 months period from 1 January 20X7 to 31 March 20X7.
- Subsidiary's financial statements should be adjusted for consolidation purposes by adding its results for the current 3 months period and deducting those for the comparative period.
- If this is impracticable then subsidiary's financial statements may be used without including this comprehensive additional information. However, in that situation adjustments should still be made for the property sale in February 20X8 and for any other significant transactions or events of the subsidiary occurring during 1 January 20X8 to 31 March 20X8.

Substance of consolidation

replaced with

Cost of investment

Separate financial statements of parent

WHAT IT ACTUALLY REPRESENTS

Consolidated financial statements of parent

- parent's share of subsidiary's:
  - net assets (at fair value) as at the end of reporting date
  - post acquisition reserves

+

- goodwill/ gain on bargain purchase on date of acquisition

- ❑ equity in subsidiary not attributable to parent
  - ❑ known as non-controlling interests (NCI)
  - ❑ presented as a separate line item within equity

Overview of the technique

	Separate statement of financial position				Consolidated statement of financial position
	Parent		**Subsidiary**		
Net assets	xxx	+	xxx	+ consolidation adjustments	xxx
Issued capital	xxx		xxx		parent's Issued Capital
Reserves	xxx		xxx		to be calculated

Overview of the technique

Consolidated statement of profit or loss

Revenue [Parent + Subsidiary (100%) – intra-group items]	xxx
↓	↓
Profit for the period (CONTROL)	xxx
OWNERSHIP	
Owners (equity holders) of the parent	xxx
NCI (….% of subsidiary's profit after tax)	
Profit for the period	xxx

Intra-group balances

Eliminated on consolidation

Example

	Parent	Subsidiary	Adjustments on consolidation		Consolidated statement of financial position
			Dr.	Cr.	
Receivables					
Amounts receivable from subsidiary	100			100	-
Payables					
Amounts payable to parent		100	100		-

Accounting requirements - Consolidation Procedures

Changes in the proportion held by NCI

- When the proportion of the equity held by NCI changes, an entity shall adjust the carrying amounts of the controlling and non-controlling interests to reflect the changes in their relative interests in the subsidiary.

- The entity shall recognize directly in equity any difference between the amount by which the non-controlling interests are adjusted and fair value of the consideration paid or received, and attribute it to the owners of the parent.

Example

	As at 31 December 2015	
	Parent	***Subsidiary***
Non-current assets:		
Tangible assets	2,000	500
Investment in Subsidiary	1,000	
Net current assets	2,000	500
	5,000	1,000
Issued capital	500	1,000
Retained earnings	4,500	
	5,000	1,000

Further information:

Parent bought 100% of Subsidiary on 31 December 2015.

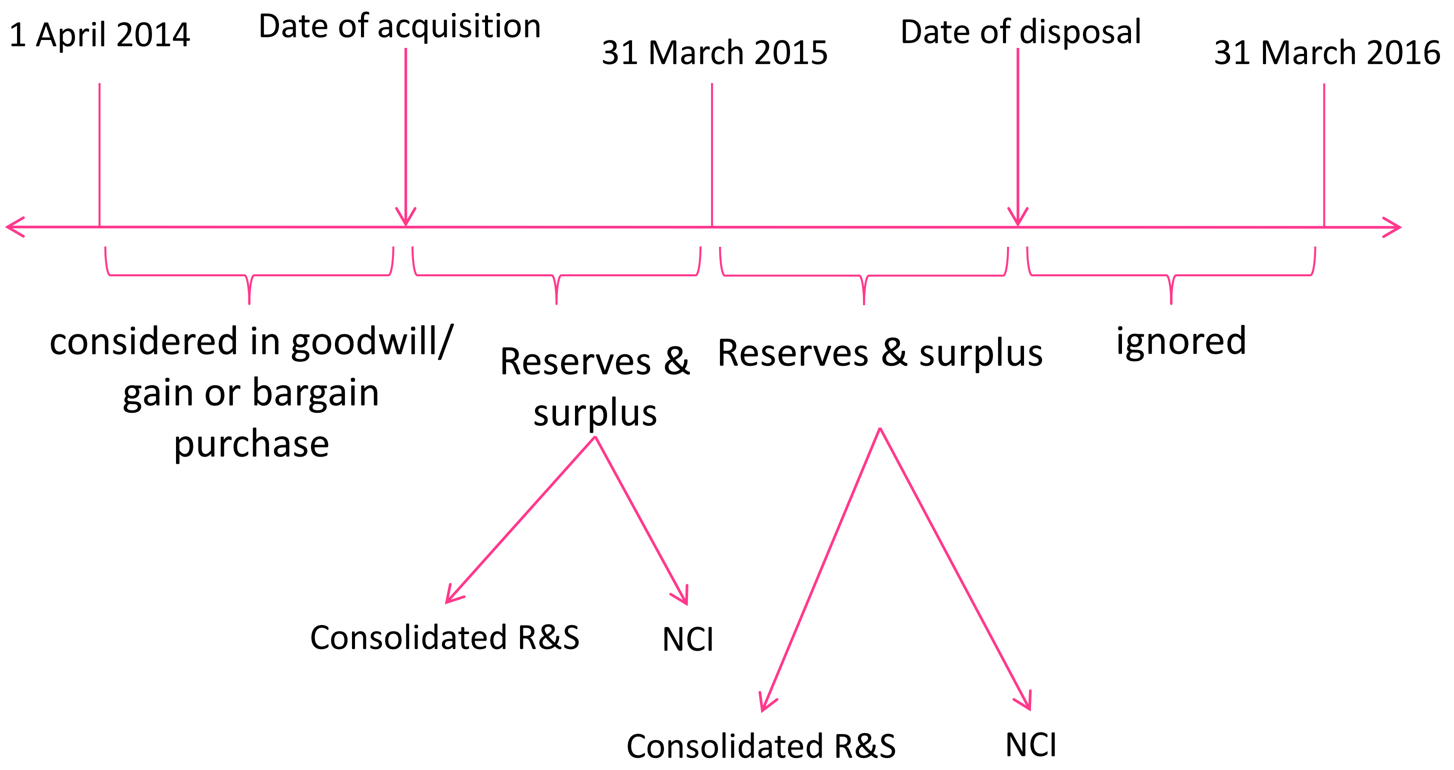
Solution

Consolidated balance sheet

	$	
Non-current assets:		
Tangible assets (2,000 + 500)	2,500	
		←Cost of investment has disappeared
Net current assets (2,000 + 500)	2,500	
	5,000	
Issued capital	500	←*Issued capital of Parent*
Retained earnings	4,500	
	5,000	

Period of consolidation

Results of operations of subsidiary



Goodwill/ Capital Reserve

In layman's term, goodwill is difference between:

a. value of business taken as a whole
b. fair value of separate net assets

Goodwill/ gain on bargain purchase is determined under Ind AS 103 as follows:

Particulars	Amount (INR)
Fair value of consideration	xxx
Amount of NCI	xxx
Less: Fair value of net assets at acquisition	xxx
Goodwill (if positive) Capital reserve (if negative)	xxx

Gain on bargain purchase arises in extremely rare circumstances

Example 1

At 31 December 2015

	Parent	Subsidiary
	$	**$**
Non-current assets		
Tangible assets	1000	800
Investment in Subsidiary	1200	
Net current assets	400	200
	--------	--------
	2600	1000
	--------	------
Issued capital	100	900
Retained earnings	2500	100
	---------	-------
	2600	1000
	-----------	-------

Further information:

- Parent bought 100% of Subsidiary on the 31 December 2015.
- Subsidiary's reserves are $100 at the date of acquisition.

Solution 1

Consolidated balance sheet

	$
Non-current assets:	
Goodwill (W2)	200
Tangible assets	1,800
Net current assets	600
	2,600
Issued capital	100
Retained earnings (W3)	2,500
	2,600

Solution 1

WORKINGS

(1) Subsidiary's net assets

	End of reporting period	*Acquisition*
	$	$
Issued capital	900	900
Retained earnings	100	100
	1,000	1,000

(2) Goodwill

	Solution 1 $
Cost	1,200
Non-controlling interest	–
Less: Net assets on acquisition (W1)	(1,000)
	200

(3) Retained earnings

	$
Parent (as given)	2,500
Share of Subsidiary (W1)	–
100% × (100 – 100)	
	2,500

Example 2

At 31 December 2015

	Parent	*Subsidiary*
Non-current assets	$	$
Tangible assets	1400	1000
Investment in Subsidiary	1200	
Net current assets	700	600
	--------	--------
	3300	1600
	--------	--------
Issued capital	100	900
Retained earnings	3200	700
	--------	--------
	3300	1600
	---------	--------

Further information:

- Parent bought 100% of Subsidiary two years ago.
- Subsidiary's reserves were $100 at the date of acquisition.
- Goodwill has been impaired by $80 since the date of acquisition.

Solution 2

Consolidated balance sheet

	$
Non-current assets:	
Goodwill (W2)	120
Tangible assets	2,400
Net current assets	1,300
	3,820
Issued capital	100
Retained earnings (W3)	3,720
	3,820

Solution 2

WORKING

1. Subsidiary's net assets

	End of reporting period	*Acquisition*
	$	$
Issued capital	900	900
Retained earnings	700	100
	1,600	1,000

2. Goodwill

	$
Cost	1,200
Non-controlling interest	–
Less: Net assets on acquisition (100% × 1,000)	(1,000)
	200
Impaired	80
As an asset	120

Solution 2

Retained earnings

	$
Parent (as given)	3,200
Share of Subsidiary (W1) 100% (700 – 100)	600
Goodwill written off (W2)	(80)
	3,720

Non-controlling interest (NCI)

Measurement of	NCI	
Methods	proportionate share of subsidiary's identifiable net assets	fair value
Goodwill impairment*	not allocated to NCI	allocated to NCI

Election of method on transaction-by-transaction basis

** goodwill amortisation not allowed*

Example 3

- A Ltd. acquired 60% equity shares of B Ltd. for INR 60 lacs
- At the date of acquisition:
  - Fair value of net assets of B Ltd. is INR 80 lacs
  - Fair value of NCI is INR 45 lacs

Calculate goodwill if NCI measured using:

a. proportionate interest method
b. fair value method

Goodwill (when NCI measured at proportionate interest) = INR 12 lacs

Goodwill (when NCI measured at fair value) = INR 25 lacs

Example 4

	Parent	Subsidiary
	$	$
Non-current assets		
Tangible assets	1,000	600
Investment in Subsidiary	1,200	–
Net current assets	500	600
	2,700	1200
Issued capital	100	50
Retained earnings	2600	1150
	2,700	1,200

Further information:

- Parent bought 80% of Subsidiary two years ago.
- Subsidiary's reserves were $150 at the date of acquisition.
- Goodwill has been impaired by $200 since the date of acquisition.
- Non-controlling interest is valued at the proportionate share of the subsidiary's identifiable net assets

Solution 4

Consolidated Balance Sheet

	$
Non-current assets:	
Goodwill (W2)	840
Tangible assets	1,600
Net current assets	1,100
	3,540
Equity attributable to owners of their parent	
Issued capital	100
Retained earnings (W4)	3,200
	3,300
Non-controlling interest (W3)	240
	3,540

Solution 4

WORKINGS

1. Subsidiary's net assets

	End of reporting period	*Acquisition*
	$	$
Issued capital	50	50
Retained earnings	1,150	150
	1,200	200

2. Goodwill

	$
Cost	1,200
Non-controlling interest (200 × 20%)	40
Less:Net assets on acquisition (100%)	(200)
	1,040

Solution 4

To retained earnings	
(via statement of profit or loss and other comprehensive income)	200
Asset in the balance sheet	840

• **Non-controlling interest**	$
Share of net assets (20% × 1,200 (W1))	240
	——

• **Retained earnings**	$
Parent (as given)	2,600
Share of subsidiary 80% × (1,150 – 150) (W1)	800
Goodwill impairment	(200)
	——
	3,200
	——

Example 5

	Parent	Subsidiary
Non-current assets	$	$
Tangible assets	1,000	600
Investment in Subsidiary	1,200	-
Net current assets	500	600
	2,700	1,200
Issued capital ($1 shares)	100	50
Retained earnings	2,600	1,150
	2,700	1,200

Further information:

1. Parent bought 80% of Subsidiary two years ago.
2. Subsidiary's reserves were $150 at the date of acquisition.
3. Goodwill has been impaired by $200 since date of acquisition.
4. Non-controlling interest is valued at fair value on acquisition. The market price of a share in the subsidiary at the date of acquisition was $29.60

Solution

Consolidated balance sheet

	$
Non-current assets:	
Goodwill (W2)	1,096
Tangible assets	1,600
Net current assets	1,100
	3,796
Issued capital	100
Retained earnings (W4)	3,240
Non-controlling interest (W3)	456
	3,796

Solution

WORKINGS

1. Subsidiary's net assets

	Reporting date	*Acquisition*
	$	$
Issued capital	50	50
Retained earnings	1,150	150
	1,200	200

2. Goodwill

	$
Cost	1,200
Add: Fair value of non-controlling interest [10 shares (i.e. 20% of 50 shares) × $29.60]	296
Less: Net assets on acquisition (100%)	(200)
	1,296
Impaired	200
Goodwill recognized	1,096

Solution

Of the goodwill impaired, 80% is debited to consolidated retained earnings and 20% is debited to non-controlling interest.

3. Non-controlling interest	$
Fair value on acquisition (W2)	296
Add: Share of post-acquisition profits (1,000 × 20%)	200
Less: Share of goodwill impaired (200 × 20%)	(40)
	456

4. Retained earnings	$
Parent (as given)	2,600
Share of Subsidiary (80% × (1,150 – 150) (W1))	800
Goodwill impairment (200 × 80%)	(160)
	3,240

Fair value of consideration - cost of acquisition

- Acquisition accounted at FV
- Acquisition costs - expensed

Deferred consideration

- Cost of acquisition is **present value** of consideration
- No impact of deferred consideration in goodwill computation
  - Finance costs (post-acquisition expense)

Fair value

- Cash/ cash equivalents
- FV of other purchase consideration

Contingent consideration

- Cost of acquisition includes FV of contingent consideration
  - If settlement in cash- recognise liability
  - If settlement in equity- recognise equity
- Contingent consideration recognised as liability measured at FV at each reporting date (changes recognised in P&L)

Example

Parent acquired 60% of Subsidiary on 1 January 2015 for $100,000 cash payable immediately and $121,000 after two years. The fair value of Subsidiary's net assets at acquisition amounted to $300,000. Parent's cost of capital is 10%. The deferred consideration was completely ignored when preparing group accounts as at 31 December 2015.

Non-controlling interest is measured at the proportionate share of identifiable net assets.

Required:
Calculate the goodwill arising on acquisition and show how the deferred consideration should be accounted for in Parent's consolidated financial statements.

Solution

Cost of investment in Subsidiary at acquisition: $100,000 + $121,000/1.21 = $200,000

Goodwill	$000
Cost	200
Non-controlling interest (40% * 300,000)	120
Less: Net assets acquired	(300)
	20

Deferred consideration

Double entry at 1 January:

Dr Cost of Investment in Subsidiary		$100,000
Cr Deferred consideration	$100,000	

On 31 December, due to unwinding of discount, the deferred consideration will equal $121,000/1.1 = 110,000

Dr Group retained earnings	$10,000
Cr Deferred consideration	$10,000

In the consolidated balance sheet, the cost of investment in Subsidiary will be replaced by the goodwill of $20,000. The deferred consideration will equal $110,000.

Unrealised profit

Eliminated on consolidation

- Sale of goods by parent to subsidiary
  - Reduce consolidated retained earnings
  - Reduce inventory

- Sale of goods by subsidiary to parent
  - Reduce net assets of subsidiary
  - Reduce inventory

Example

Parent owns 80% of Subsidiary. During the current accounting period, Parent transferred goods to Subsidiary for $4,000, which earned Parent a profit of $1,000. These goods were included in Subsidiary's inventory at the end of the reporting period.

Required:

Show the adjustment in the consolidated balance sheet.

Solution

Dr	Retained earnings	$1,000	
Cr	Inventory		$1,000

Example

Parent owns 80% of Subsidiary. During the current accounting period, Subsidiary sold goods to Parent for $18,000 which earned Subsidiary a profit of $6,000. At the end of the reporting period, half of these goods are included in Parent’s inventory.

At the end of the reporting period, Parent’s accounts showed retained profits of $100,000 and Subsidiary’s accounts showed net assets of $75,000, including retained profits of $65,000. Subsidiary had retained profits of $20,000 at acquisition.

Required:

Show the adjustment to eliminate unrealized profits in the consolidated financial statements.

Solution

Dr	Retained earnings (1/2 × 6,000)	$3,000	
Cr	Inventory		$3,000

WORKING

1. Subsidiary's net assets

		Reporting date	*Acquisition date*
		$	$
Issued capital		10,000	10,000
Retained earnings			
Per the question	65,000		20,000
Unrealized profit	(3,000)	62,000	
	———	———	———
		72,000	30,000
		———	———

Solution

Non-controlling interest

Share of net assets (including the unrealized profit)	
(20% × 72,000)	$14,400
	————

Retained earnings

	$
Parent (as given)	100,000
Share of Subsidiary (including unrealized profit)	
80% × (62,000 – 20,000)	33,600
	———
	133,600
	———

Example

Whale owns 75% of Porpoise. The profit or loss for each company for the year ended 31 March 2016 is as follows:

	Whale \$	Porpoise \$
Revenue	120,000	70,000
Cost of sales	(80,000)	(50,000)
Gross profit	40,000	20,000

During the year Porpoise made sales to Whale amounting to \$30,000. \$15,000 of these sales were in inventory at the year end. Profit made on the year-end inventory items amounted to \$2,000.

Required:

Calculate group revenue, cost of sales and gross profit.

Solution

Seller adjustment

	Whale	Porpoise	Adjustment	Consolidated
	$	$	$	$
Revenue	120,000	70,000	(30,000)	160,000
Cost of sales – per question	(80,000)	(50,000)	30,000	
– unrealised profit		(2,000)		(102,000)
Gross profit	40,000	18,000		58,000

Non-current asset transfers

Eliminated on consolidation

Adjustments needed

Selling company

eliminate profit

Buying company

adjust depreciation

Example

Parent owns 80% of Subsidiary. Parent transferred an asset to Subsidiary at a value of $15,000 on 1 January 2015. The original cost to Parent was $20,000 and the accumulated depreciation at the date of transfer was $8,000. The asset had a useful life of 5 years when originally acquired, with a residual value of zero. The useful life at the date of transfer remains at 3 years. Full allowance is made for depreciation in the year of purchase and none in the year of sale.

Required:

Calculate the adjustment for the consolidated balance sheet at 31 December 2015.

Solution

	With transfer	Without transfer	Adjustment
	$	$	$
Cost	15,000	20,000	
Accumulated depreciation			
(15,000/3 years)	(5,000)	*(12,000)	
	10,000	8,000	2,000
Charge for the year	5,000	4,000	1,000
Profit on disposal			
Proceeds	15,000		
Carrying amount			
(20,000 – 8,000)	(12,000)		
	3,000	–	3,000

Solution

Dr Parent profit or loss – profit on disposal	3,000
Cr Non-current assets	3,000

and

Dr Non-current assets	1,000
Cr Subsidiary profit or loss – depreciation	1,000

* Accumulated depreciation of $12,000 is calculated as 3 years @ 20% per annum based on the original cost of $20,000.

Example

Parent owns 80% of subsidiary. Parent transferred a non-current asset to subsidiary on 1 January 2015 at a value of $15,000. The asset originally cost Parent $20,000 and depreciation to the date of transfer was $8,000. The asset had a useful life of 5 years when originally acquired, with a residual value of zero. The useful life at the date of transfer remains at 3 years. A full year's depreciation charge is made in the year of acquisition and none in the year of disposal. Total depreciation for 2014 was $700,000 for parent and $500,000 for subsidiary.

Required:

Show the adjustments required for the above transaction in the consolidated statement of profit or loss for the year ended 31 December 2015.

Solution

	Parent	Subsidiary	Adjustment	Consolidated
	$	$	$	$
Per question	700,000	500,000		1,200,000
Asset unrealized profit				
[15,000 – (20,000 – 8,000)]	3,000			3,000
Depreciation adjustment				
(15,000/3 years) – 4,000		(1,000)		(1,000)
				1,202,000

.

This depreciation adjustment would be part of the profit after tax of subsidiary and would therefore be shared with the non-controlling interest

Example

Elimination of unrealised profits or losses in full where transactions are between subsidiaries with non-controlling interests

The rationale for full elimination of unrealised profits or losses, even where the related transactions are between subsidiary entities with non-controlling interests, might not initially be obvious.

However, transactions between subsidiaries included in the consolidation are wholly within the control of the parent company, whether or not the subsidiaries are wholly owned. All of a subsidiary's assets and liabilities and transactions between subsidiaries are brought into the consolidation in full – again, whether or not they are wholly owned.

Therefore, because the group includes 100% of each subsidiary's assets and liabilities, intra-group transactions that give rise to profits or losses that are unrealised at the balance sheet date are wholly unrealised to the group and do not represent any increase or decrease in the group's net assets.

They should, therefore, be eliminated in full, even where the transactions involve subsidiaries with non-controlling interests.

The rules apply equally to any profit that might be included in the group's non-current assets as a result of one group company selling assets to another group company at a profit.

Example

Attributing earnings between controlling and non-controlling interests

If there are contractual arrangements that determine the attribution of earnings, such as a profit-sharing agreement, the attribution specified by the arrangement should be considered if it is determined to be substantive.

If there are no such contractual arrangements, the relative ownership interests in the entity should be used if the parent's ownership and the non-controlling interest's ownership in the assets and liabilities are proportional.

For example, if the controlling interest owns 60% of entity A and the non-controlling interest owns 40%, 60% of the earnings should be allocated to the controlling interest and 40% to the non-controlling interest.

If, however, the parties have a contractual arrangement specifying a 50/50 split of the earnings, 50% of the earnings should be allocated to the controlling interest and 50% to the non-controlling interest, provided the contractual arrangement is substantive.

Example

Profit attributable to non-controlling interest subsequent to acquisition

If A parent entity acquires a 60% subsidiary for INR 300 million at the beginning of the year. The fair value of the subsidiary's identifiable net assets at the date of acquisition is INR 370 million. In its first year after purchase, the subsidiary's income statement, as it is included in the group's consolidated financial statements (that is, after all consolidation adjustments, such as the amortisation of intangible assets), is as follows:.

	INR Million
Profit before tax	26
Tax	(1)
Profit for the year	25
Profit attributable to NCI (40% X 25)	10
Profit attributable to parent's equity holders	15
	25

Example

Sale of a 20% interest in a wholly owned subsidiary

Entity A sells a 20% interest in a wholly owned subsidiary to outside investors for INR 200 million in cash. It still maintains an 80% controlling interest in the subsidiary. The carrying value of the subsidiary's net assets is INR 600 million, including goodwill of INR 130 million from the subsidiary's initial acquisition.

The accounting entry recorded on the disposal date for the 20% interest sold is as follows:

		INR million
Dr Cash	200	
Cr NCI (20% X INR 600 M)		120
Cr Equity		80

The carrying value of the 20% non-controlling interest that is recognised is calculated as the proportionate interest in the subsidiary's carrying value/net assets.

Example

Acquisition of a further 20% interest in a subsidiary

Entity A acquired 60% of entity B some years ago for INR 3,000. At the time, entity B's fair value was INR 5,000. It had net assets with a fair value of INR 3,000 (which, for the purposes of this example, was the same as book value). Goodwill of INR 1,200 was recorded (being INR 3,000 − (60% × INR 3,000)). On 1 July 20X5, entity A acquires a further 20% interest in entity B, taking its holding to 80%. At that time, entity B's fair value is INR 10,000, and entity A pays INR 2,000 for the 20% interest. At the time of the acquisition, the fair value of entity B's net assets is INR 6,000 and the carrying amount of the non-controlling interest is INR 2,000.

The accounting entry recorded for the acquisition of the non-controlling interest is as follows:

		INR
Dr NCI	1,000	
Dr Equity	1,000	
Cr Cash		2,000

The carrying value of the 20% non-controlling interest that is eliminated is calculated at the proportionate interest in the non-controlling interest's carrying value.

Example

Acquisition of a further 40% interest in a subsidiary

A parent entity acquires a 60% subsidiary for INR 300 million at the beginning of the year. The fair value of the subsidiary's identifiable net assets at the date of acquisition is INR 370 million. In its first year after purchase, the subsidiary's income statement, as it is included in the group's consolidated financial statements (that is, after all consolidation adjustments, such as the amortisation of intangible assets), is as follows:

	INR million
Profit before tax	26
Tax	(1)
Profit for the year	25
Profit attributable to NCI (40% X INR 25 M)	10
Profit attributable to parent's equity holders	15

The non-controlling interest at the date of acquisition is stated at either:

- the initial amount of C200 million, if the parent entity recognises the non-controlling interest at fair value which, assuming there is no control premium, is calculated as follows (40% × (C300m/60%)); or
- the initial amount of C148 million, if the parent entity recognises the non-controlling interest at its proportionate share of the acquiree's net assets at acquisition (calculated as 40% × C370m).

Example

Acquisition of a further 40% interest in a subsidiary

The non-controlling interest's share of changes in equity at the year end (which are all due to the profit for the year) is C10 million. Depending on the basis used for the initial recognition, the non-controlling interest will be carried at C210 million or C158 million at the end of the first year after the subsidiary's purchase. The parent entity now acquires the remaining 40% interest in the subsidiary for C280 million.

The accounting entry recorded for the purchase of the non-controlling interest is as follows (if NCI was initially recorded at fair value):

		INR million
Dr NCI	210	
Dr Equity	70	
Cr Cash		280

Example

Acquisition of a further 40% interest in a subsidiary

The accounting entry recorded for the purchase of the non-controlling interest is as follows (if NCI was initially recorded at the proportionate share of the acquiree's identifiable net assets):

		INR million
Dr NCI	158	
Dr Equity	122	
Cr Cash		280

The purchase of the 40% non-controlling interest results in a larger reduction of the controlling interest's equity where the non-controlling interest was initially recorded as the proportionate share of the acquiree's identifiable net assets.

Loss of control

- If a parent loses control of a subsidiary, it shall:
  - derognize:
    - the assets (including any goodwill) and liabilities of a subsidiary at their carrying amounts at the date when control is lost; and
    - the carrying amount of any NCI in the former subsidiary at the date when control is lost (including any components of OCI attributable to them).
  - recognize:
    - the fair value of the consideration received, if any, from the transaction, event or circumstances that resulted in the loss of control;
    - if the transaction, event or circumstances that resulted in the loss of control involves a distribution of shares of the subsidiary to owners in their capacity as owners, that distribution; and
    - any investment retained in the former subsidiary at its fair value at the date when control is lost.
  - reclassify to profit or loss, or transfer directly to retained earnings if required by other Ind AS, the amounts recognized in OCI in relation to the subsidiary.
  - recognize any resulting difference as a gain or loss in profit or loss attributable to the parent.

Accounting requirements -Consolidation Procedures

Loss of control

- If a parent loses control of a subsidiary, the parent shall account for all amounts previously recognized in OCI in relation to that subsidiary on the same basis as would be required if the parent had directly disposed of the related assets or liabilities.

- Therefore, if a gain or loss previously recognized in OCI would be reclassified to profit or loss on disposal of related assets or liabilities, the parent shall reclassify the gain or loss from equity to profit or loss (as a reclassification adjustment) when it loses control of the subsidiary.

- If a revaluation surplus previously recognized in OCI would be transferred directly to retained earnings on the disposal of the asset, the parent shall transfer the revaluation surplus directly to retained earnings when it loses control of the subsidiary.

Accounting requirements -Consolidation Procedures

Example - Loss of control

- A parent sells an 85% interest in a wholly owned subsidiary. The relevant details are as follows:
- After the sale, the parent accounts for its remaining 15% interest as an FVTOCI investment
- The subsidiary did not recognize any amounts in OCI
- Net assets of the subsidiary before the disposal are INR 5000
- Cash proceeds from the sale of 85% interests are INR 7500 and
- The fair value of 15% interest retained by the parent is INR 1300.

- The parent accounts for the disposal of an 85% interest as follows:
- Debit FVTOCI Investments INR 1300
- Debit Bank INR 7500
- Credit Net assets of subsidiary derecognized (summarized) INR 5000
- Gain on loss of control of subsidiary INR 3800

Joint arrangements

Joint arrangements

Definition

A joint arrangement is an arrangement over which two or more parties have joint control

- A joint arrangement is either a joint operation or a joint venture and has the following characteristics:
  - The parties are bound by a contractual arrangement
  - That contractual arrangement gives two or more of those parties joint control of the arrangement
- Contractual arrangement defines the terms
  - Often, but not always, in writing
  - Documented discussions
  - Law or articles of association

Joint arrangements

Joint control

Joint control is the contractually agreed sharing of *control* of an arrangement , which exists only when the decisions about the *relevant activities* require the *unanimous consent* of the parties sharing control

- Control (as defined by Ind AS 110): the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee
- Relevant activities: the activities of the arrangement that significantly affect the investee's returns
- Unanimous consent: no single party controls the arrangement and two or more parties must agree to share control

Joint arrangements

Joint control

Does the contractual arrangement give all the parties (or a group of the parties) control of the arrangement collectively?

No → Outside the scope of Ind AS 111

(not a joint arrangement)

Yes ↓

Do the decisions about the relevant activities require the unanimous consent of all the parties that collectively control the arrangement?

No → Outside the scope of Ind AS 111

(not a joint arrangement)

Yes ↓

Joint Arrangement

→ Joint operation

→ Joint venture

Joint arrangements
Joint control - Examples

	Example 1	Example 2	Example 3
Requirement	75% vote to direct relevant activities	75% vote to direct relevant activities	Majority vote to direct relevant activities
Party A	50%	50%	35%
Party B	30%	25%	35%
Party C	20%	25%	Widely dispersed
Conclusion			

Joint arrangements
Joint control - Examples

	Example 1	Example 2	Example 3
Requirement	75% vote to direct relevant activities	75% vote to direct relevant activities	Majority vote to direct relevant activities
Party A	50%	50%	35%
Party B	30%	25%	35%
Party C	20%	25%	Widely dispersed
Conclusion	Even though A can block any decision, A does not control B, because A needs B to agree = **joint control** between A and B.		

Joint arrangements

Joint control - Examples

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Requirement	75% vote to direct relevant activities	75% vote to direct relevant activities	Majority vote to direct relevant activities
Party A	50%	50%	35%
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Party C	20%	25%	Widely dispersed
Conclusion	Even though A can block any decision, A does not control B, because A needs B to agree = **joint control** between A and B.	**No control (or joint control)** because multiple combinations could be used to reach agreement	

Joint arrangements

Joint control - Examples

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Requirement	75% vote to direct relevant activities	75% vote to direct relevant activities	Majority vote to direct relevant activities
Party A	50%	50%	35%
Party B	30%	25%	35%
Party C	20%	25%	Widely dispersed
Conclusion	Even though A can block any decision, A does not control B, because A needs B to agree = **joint control** between A and B.	**No control (or joint control)** because multiple combinations could be used to reach agreement	**No control (or joint control)** because multiple combinations could be used to reach agreement

Classification of a joint arrangement

Classification of a joint arrangement

Legal form of the separate vehicle

Does the legal form of the separate vehicle give the parties rights to the assets, and obligations for liabilities, relating to the arrangement?

Yes → Joint operation

No ↓

Contractual terms of the arrangement

Do the contractual terms of the arrangement specify that the parties have rights to the assets, and obligations for the liabilities, relating to the arrangement?

Yes → Joint operation

No ↓

Other facts & circumstances

Is the arrangement designed so that

- The parties have rights to substantially all of the economic benefits of the JA?
- The JA depends on the parties on a continuous basis for settling the liabilities?

Yes → Joint operation

No ↓

Joint venture

Classification of a joint arrangement
Legal form

- Classification of a joint arrangement
  Legal form

Joint Operations	Joint Ventures
Without a separate vehicle, the joint arrangement is a joint operation	To be a joint venture, there must be a separate vehicle
Parties have rights to the assets and obligations for the liabilities of the arrangement	Parties have rights to the net assets of the arrangement
The legal form of the separate vehicle does not confer separation between the parties and the separate vehicle (e.g., general partnership)	The legal form of the separate vehicle causes it to be considered in its own right (e.g., corporation)

- Separate vehicle: A separately identifiable financial structure, including separate legal entities or entities recognised by statute, regardless of whether those entities have a legal personality

Classification of a joint arrangement
Legal form - Example

- Fact pattern:
  - A and B jointly establish a new corporation (C) in which each party has a 50% ownership interest
  - Incorporation enables the separation of C from A and B
  - Assets and liabilities of C are the assets and liabilities of the incorporated entity
  - Legal form of the separate vehicle indicates that the parties have rights to the net assets of the arrangement

- Analysis:
  - Joint venture or Joint operation?

Classification of a joint arrangement

Examples of contractual terms

	Joint Operations	Joint Ventures
Assets	• Share all interests in the assets in a specified proportion • Hold assets of the arrangement as tenants in common in a specified proportion • Have rights to all of the economic benefits generated by the assets	Do **not** have interests (i.e., no rights, title, or ownership) in the assets of the arrangement
Liabilities	• Share all liabilities, obligations, costs and expenses in a specified proportion • Have liabilities for claims raised by third parties or to customers of the arrangement	• Are not liable for the debts and obligations of the arrangement • Liabilities to the arrangement do not exceed the parties' investment in the arrangement • Creditors do not have any recourse against any party in for debts or obligations

Classification of a joint arrangement

Contractual terms - Example

(Continued)

- Fact pattern:
  - A and B modify the features of C through their contractual arrangement so that each has an interest in the assets of C and each is liable for the liabilities of C in a specified proportion

- Analysis:
  - Joint venture or Joint operation?

Classification of a joint arrangement
Facts and circumstances

- Facts and circumstances might indicate a joint operation if they result in the parties having:
  - Rights to the assets
  - Obligations for the liabilities

- This may happen when there is:
  - Restrictions on customers
  - Commitments to purchase all the output produced
  - Expectations to fund losses by venturers
  - Venturers continuously settle liabilities of the arrangement
  - Designed to operate at breakeven
  - Consider purpose and design
  - Commitment upon default or guarantee is <u>not</u> determinative of being a joint operation

Classification of a joint arrangement

Facts and circumstances - Example

(Continued)

- Fact pattern:
  - Neither the legal form or contractual arrangement provide rights to assets and liabilities of the arrangement to the venturers; however
  - A and B agreed to purchase all the output produced by C in a ratio of 50:50
  - C cannot sell any of the output to third parties, unless this is approved by A and B (expected to be uncommon)
  - Price of the output sold is designed to cover expenses incurred by C (intended to operate at break-even level)

Example - Telecom

Fact pattern:

- A & B establish New Co.
- Transfer all tower equipment to New Co.
- A & B have direct rights to assets/liabilities based on their proportionate shareholding
- All New Co’s decisions are unanimously made by A & B

Ind AS 111

Joint Operation because A & B have direct rights to the assets/liabilities

Variation in the Example

- A & B do not have direct rights to assets / liabilities of New Co. based on their proportionate shareholding
- Network capacity will be shared by A & B only.
- Operated at breakeven level

Ind AS 111
Joint operations or Joint venture?

Accounting treatment

Accounting for joint operations

- For a joint operation, the joint operator recognises its:

Assets (including its share of jointly held assets)	Liabilities (including its share of jointly incurred liabilities)

Revenue from the sale of its share of the output arising from the joint operation	Share of the revenue from the sale of the output obtained from the joint operation	Expenses (including its share of jointly incurred expenses)

- The recognition and measurement (including impairment considerations) for each of these items shall be done in accordance with the applicable Ind ASs

Accounting treatment
Proportionate consolidation vs. joint operation

- When is accounting for a joint operation the same as ‘proportionate consolidation’?
  - Equal rights to all assets all liabilities – probably same
  - Rights to a specified percentage of certain assets and differing rights (and percentages) to other assets, and different obligations for various liabilities – likely to be a difference
  - Nature of assets and liabilities might change
    - Assets - same nature as recognised by joint operator OR (for example) reimbursement right?
    - Liabilities - same nature as recognised by joint operator OR (for example) cash due to joint operation?

Accounting treatment
Joint Operation Example

Fact pattern:

- D & E establish New Co. (F)
- The legal form of the separate vehicle does not confer separation between the parties
- D and E each own 50% of the equity (e.g., shares) in F. However, as per the contractual terms of the joint arrangement:
    - D has the rights to all of Building No. 1 and the obligation to pay all the third party debt in F.
    - D and E have rights to all other assets in F, and obligations for all other liabilities in F in proportion to their equity interests (i.e., 50%)

Accounting treatment

Joint Operation Example (continued)

F's balance sheet is as follows (in CU's):

Liabilities and Equity		Assets	
Debt	120	Cash	20
Employee obligation	50	Building 1	120
Equity	70	Building 2	100
	240		**240**

Under Ind AS 111, D would record the following in its financial statements. This likely will differ from the amounts recorded using proportionate consolidation.

Liabilities and Equity		Assets	
Debt	120	Cash	10
Employee obligation	25	Building 1	120
Equity	35	Building 2	50
	180		**180**

Accounting treatment

Joint Operation- Determining the relevant Ind AS

Joint operators are required to recognise their rights to assets and their obligations for liabilities in accordance with the relevant Ind AS:

A Joint operator will need to carefully analyse the nature of its rights to assets when determining the appropriate accounting.

For example, a Joint operator would recognise its share of an asset in accordance with Ind AS 16 Plant, Property and Equipment, or Ind AS 38 Intangible Assets, as applicable. When the contractual terms of the joint operation provide a joint operator with a right to use an asset, not a share of the asset itself, the Joint operator would consider determining Whether the Arrangement Contains a Lease in accordance with Ind AS 17.

Disposal of Joint Arrangement

- Ind AS 111 requires the equity method
- The application of the equity method continues to be covered in Ind AS 28, however it has below exemptions:
  - if the entity is a parent that is exempt from preparing CFSs by the scope exception in Ind AS 110, or
  - When an investment in an associate or a joint venture, is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure investments in those associates and joint ventures at fair value through profit or loss in accordance with Ind AS 109.

Disposal of Joint Arrangement

- Disposal of interest in a joint operation

  When an entity disposes of its interest in a joint operation, it ceases to account for the rights to assets and obligations for liabilities, and recognises any gain or loss as of the disposal date.

- Disposal of interest in a joint venture

  When an entity disposes of its interest in a joint venture, it ceases to use the equity method as of that date. It also de-recognises its interest and recognises any gain or loss upon sale.

In both the cases, an entity is not required to restate its financial statements as if it never held the interest in the disposed joint operation / joint venture

Continuous reassessment

Continuous reassessment

- Accounting for arrangements pre-Ind AS 111 changed mostly in line with changes in ownership interest or changes in contractual arrangements
- Due to revised definition of control, management also needs to reassess upon changes in facts and circumstances, in addition to the above, for example:
  - Changes in how activities are directed
  - Changes in legal form
  - Changes in other facts and circumstances (such as changes in how the output of the joint operation is sold or how liabilities of the operation are settled)
- Reassessment required even if steps are predetermined

Associates

What do you mean by an 'associate'?

An associate is an entity over which an investor has…….

What is a ?

Power to participate in financial and operating policy decisions of investee

not control/ joint control

General presumption

- 20% or more voting rights constitute significant influence

converse also true

Significant influence

- Indicators:

a) representation on the board of directors or equivalent governing body of the investee;

b) participation in policy-making processes, including participation in decisions about dividends or other distributions;

c) material transactions between the investor and the investee;

d) interchange of managerial personnel; or

e) provision of essential technical information.

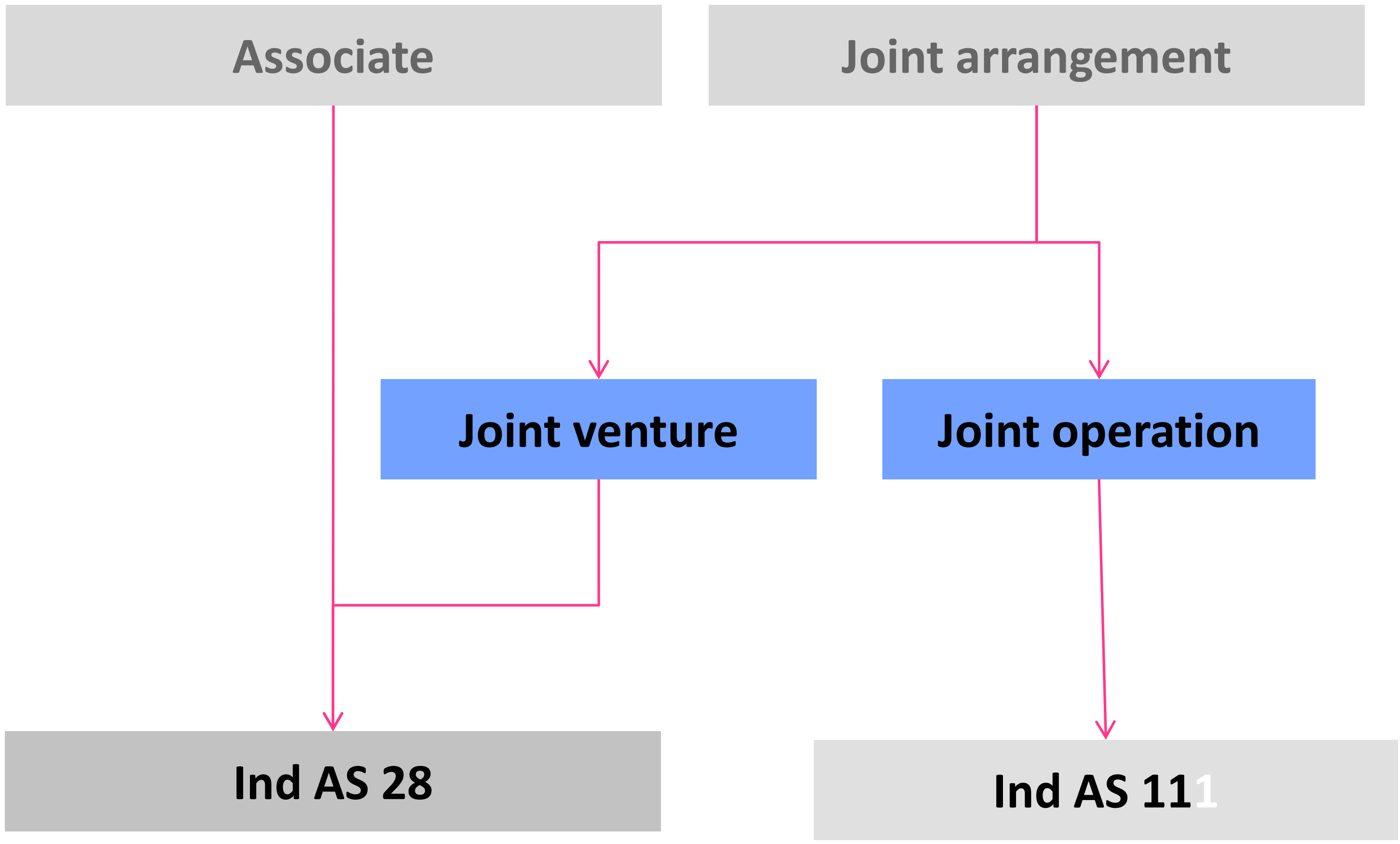
Significant influence

Potential voting rights

Can arise through share warrants, call options, debt or equity instruments that are convertible into ordinary shares, etc.

- Currently exercisable or currently convertible are to be considered for the assessment.
- Potential voting rights are not currently exercisable when , for example, they can not be exercised or converted until a future date or until the occurrence of a future event.
- Potential voting rights held by other investors also need to be considered for evaluation.
- Intention and the financial ability to exercise or convert to be ignored.
- Ceasing to have significant influence

Overview of accounting



Exemptions to equity accounting

- The application of the equity method continues to be covered in Ind AS 28, however it has below <u>exemptions</u>:

  – if the entity is a parent that is exempt from preparing CFSs by the scope exception in Ind AS 110, or

  – When an investment in an associate or a joint venture, is held by, or is held indirectly through, an entity that is a <u>venture capital organisation</u>, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity <u>may elect to measure investments in those associates and joint ventures at fair value through profit or loss</u> in accordance with Ind AS 109.

Status of investor

- wholly-owned; or partially-owned as long as other shareholders have no objection
- debt/ equity not traded on public market
- not filed its financial statements with a recognised stock exchange

Status of ultimate (or intermediate) parent

- presents consolidated financial statements in accordance with Ind AS

Measured at cost or as per Ind AS 109

Associate classified as held for sale accounted for under Ind AS 105

Equity method of accounting

- The equity method is a method of accounting whereby the investment is initially recognized at cost and adjusted thereafter for the post-acquisition change in the investor's share of net assets of the investee. The profit or loss of the investor includes the investor's share of the profit or loss of the investee.

Equity method of accounting

- **no line-by-line consolidation**
  - share of net assets included in consolidated balance sheet in one line
  - share of profits (after tax) included in consolidated statement of profit or loss in one line

Treatment in consolidated balance sheet

- include cost of investment +/- share of post-acquisition P&L – impairment loss (if any)
  - eliminate investment in separate financial statements
- include post acquisition reserves
- share of net assets in excess of cost of investments included in profit or loss

reatment in consolidated statement of profit or loss

- include share of profits (after tax)
  - eliminate dividend income

Equity method of accounting

- Initially recorded at cost and thereafter adjusted for:
  - Investor's share of post acquisition profit or loss;
  - Distributions from the investee
  - Changes in the investor's proportionate interest in the investee recorded in other comprehensive income
  - Fair value adjustments, if any.
- When potential voting rights exist only present ownership interests are considered.
- Outstanding cumulative preference shares that are held by parties other than the investor and classified as equity, the investor computes its share of profits or losses after adjusting for the dividends on such shares, whether or not the dividends have been declared.

Equity method of accounting

Date of commencing the use of the equity method

- From the date when the investment fallswithin the definition of an associate.

Recording the initial investment:

- Cost – net fair value of the identifiable assets and liabilities = Goodwill (not presented separately)/ income recognized in the income statement in the period in which the investment is acquired.

Goodwill neither amortized nor tested separately for impairment. Instead, entire carrying amount of investment is tested for impairment under Ind AS 36 as a single asset whenever there is an indication.

Example

Parent acquired, during the current year, a 40% holding in Associate for INR 18,600. Goodwill on acquisition was calculated as INR 1,000 and there has been no impairment of goodwill during the year. The fair value of Associate's net assets at the year end is INR 48,000.

Required:

Calculate the investment in associate to be included in the consolidated balance sheet and state the amount of Associate's profits to be included in the consolidated statement of profit or loss for the current year.

Solution

	INR
Net assets on acquisition	
Cost of investment	18,600
Less: Goodwill	(1,000)
40% of Associate's net assets on acquisition	17,600
Gross up to 100%	× 100/40
	44,000
Investment in associate	
Cost of investment	18,600
Plus: 40% of post-acquisition profits (48,000 – 44,000)	1,600
Less: Impairment loss recognised	0
	20,200
Income from associate	
included in consolidated statement of profit or loss	
40% of post-acquisition profits (48,000 – 44,000)	1,600

Accounting policies and year ends

counting policies

- should be uniform

- Ind AS 28 allows an investor to not adopt uniform accounting policies, in case of an associate, if it is impracticable to do so.
- Impracticability exemption exists only for an associate and not for joint venture

Year ends

- should be same
- if different
  - prepare special financial statements of associate as at the same date as the investor
  - if impracticable to do so, adjust for effects of significant transactions/ events between these dates (difference ≤ 3 months)

Inter-company items

Inter-company balances

- no elimination

Inter-company transactions

- dividend- eliminated
- others- no elimination

Unrealised profit

- eliminated to extent of investor's interest

Equity method of accounting

Associates with net asset deficiencies

- If an investor's share of losses of an associate equals or exceeds its interest in the associate, the investor discontinues recognising its share of further losses.

- The interest in an associate is the carrying amount of the investment in the associate under the equity method together with any long-term interests that, in substance, form part of the investor's net.

- Losses recognized under the equity method in excess of the investor's investment in ordinary shares are applied to the other components of the investor's interest in an associate in the reverse order of their seniority (i.e., priority in liquidation).

- After the investor's interest is reduced to zero, additional losses are provided for, and a liability is recognized, only to the extent that the investor has incurred legal or constructive obligations or made payments on behalf of the associate.

- If the associate subsequently reports profits, the investor resumes recognizing its share of those profits only after its share of the profits equals the share of losses not recognized.

Equity method of accounting

Discontinuing the use of equity method:
When the investor ceases to have significant influence
Apply Ind AS 109 from that date provided the associate has not become subsidiary or joint venture.

Discontinue when the investment is classified as held for sale under Ind AS 105
Measurement as at the date of discontinuing the use of equity method:
Measure at fair value.

Fair value of the retained interest and proceeds from the disposal of the part interest – carrying amount of investment = Recognized in profit or loss.

Amount recognized in OCI should be recycled to the Statement of P&L.

Disclosures

Disclosure requirements

- Disclosures requirements are governed by Ind AS 112

- Disclosures should enable users to understand:
  - Nature of, and risks associated with, involvement with other entities
  - Financial effects of that involvement on financial position, financial performance, and cash flows
  - Significant judgments and assumptions (and changes thereto) made by the investor in determining whether it controls another entity

- For subsidiaries with material NCI interests, summarised financial information
  - Name of the subsidiary
  - Principal place of business
  - Proportion of ownership interests held by non-controlling interests
  - Summarised financial information about the subsidiary, etc
- Disclosures for structured entities

Disclosure requirements

- The significant judgements and assumptions made (and changes to those judgements and assumptions) in determining that:-

  - it has control of another entity (as described in Ind AS 110.5 and Ind AS 110.6);

  - it controls another entity even though it holds less than half of the voting rights of the other entity;

  - it is an agent or a principal (Ind AS 110.B58-B72).

Disclosure requirements

- An entity shall disclose information that enables users of consolidated financial statements
  - a) to understand:
    - (i) the composition of the group; and
    - (ii) the interest that NCI has in the group's activities and cash flows; and
  - b) to evaluate:
    - i. the nature and extent of significant restrictions on its ability to access or use assets, and settle liabilities, of the group;
    - ii. the nature of, and changes in, the risks associated with interests in consolidated structured entities;
    - iii. the consequences of changes in ownership interest in a subsidiary that do not result in a loss of control;
    - iv. the consequences of losing control of a subsidiary during the reporting period

Disclosure requirements

For each subsidiary that has NCI which is material to the reporting entity:-

- the name of the subsidiary;
- the principal place of business (and country of incorporation if different from the principal place of business) of the subsidiary;
- the proportion of ownership interests as well as voting rights (if not the same as ownership interests) held by NCI;
- the profit or loss allocated to NCI of that subsidiary during the period;
- accumulated NCI of that subsidiary at the end of the period;
- summarised financial information about the subsidiary (see Ind AS 112.B10).

Disclosure requirements

- Significant restrictions (e.g. statutory, contractual and regulatory restrictions) o ability to access or use the assets and settle the liabilities of the group, such as:-
  - those that restrict the ability of a parent or its subsidiaries to transfer cash or other assets to (or from) other entities within the group;
  - guarantees or other requirements that may restrict dividends and other capital distributions being paid, or loans and advances being made or repaid, to (or from) other entities within the group;
- The nature and extent to which protective rights of NCIs can significantly restrict the entity's ability to access or use the assets and settle the liabilities of the group (such as when a parent is obliged to settle liabilities of a subsidiary before settling its own liabilities, or approval of NCIs is required either to access the assets or to settle the liabilities of a subsidiary); and
- The carrying amounts in the consolidated financial statements of the assets and liabilities to which those restrictions apply.

Disclosure requirements

- Significant judgements and assumptions made in determining that the reporting entity meets the definition of an investment entity
- If it does not exhibit one or more of the typical characteristics of an investment entity, description of why it nevertheless meets the definition of an investment entity
- Fact of change in status, reasons for the change and impact on the financial statements
- Fact that the entity has applied the exception to consolidation
- Explicit or implicit financial support provided to entities that it controls
- Nature and extent of any significant restrictions on the ability of investees to transfer funds to the investment entity.
- Other disclosures as given in Ind AS 112.19A to 19G.

Thank You