



LIVE COACHING CLASSES BOARD OF STUDIES (A), ICAI

CA FINAL PAPER 1: FINANCIAL REPORTING

TOPIC: IND AS 110 - CONSOLIDATED FINANCIAL STATEMENTS

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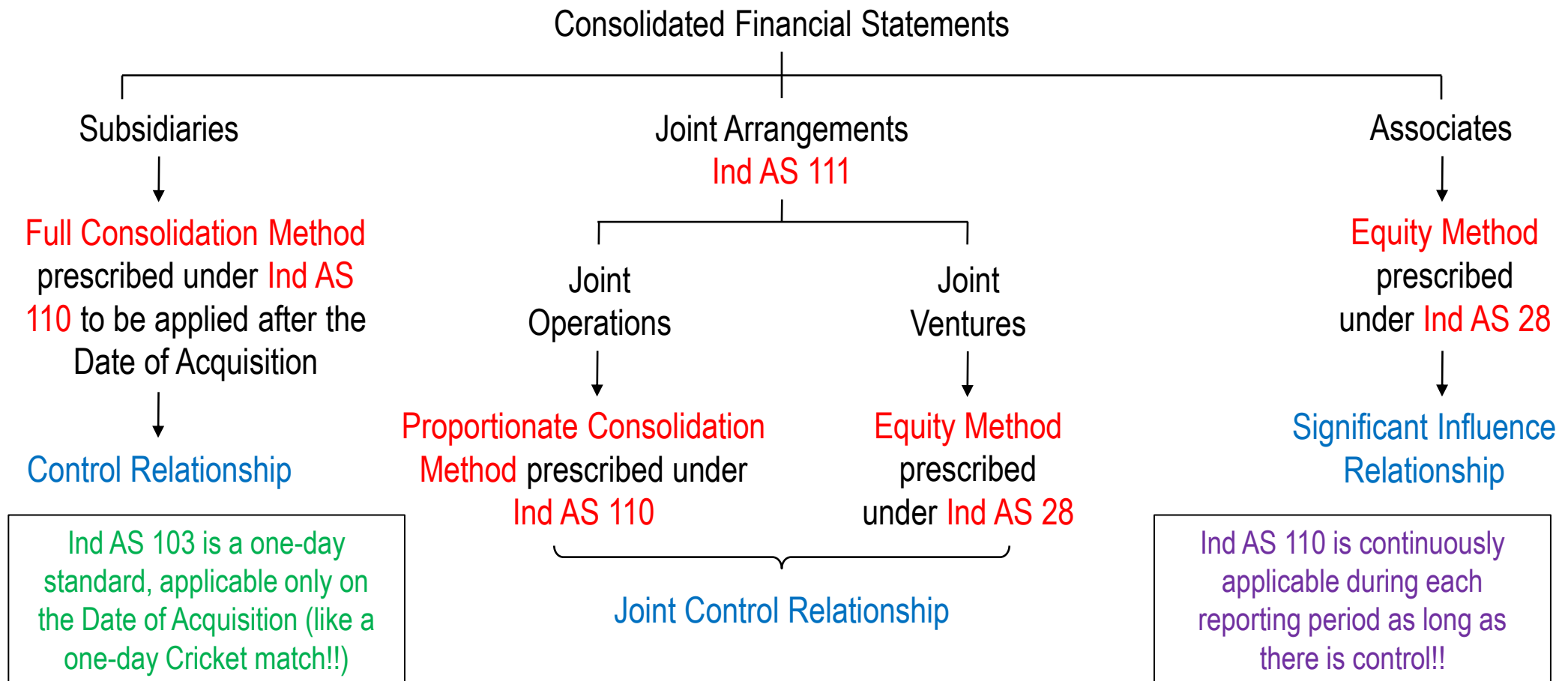


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FRAMEWORK OF CONSOLIDATED FINANCIAL STATEMENTS





LEGAL PERSPECTIVE W.R.T. CONSOLIDATION

Section 129(3) of the Companies Act, 2013:

- Where a company has **one or more subsidiaries**, it shall,
- **in addition** to the standalone financial statements,
- **prepare consolidated financial statements** of the company and of all the subsidiaries **in the same form and manner as that of its own**
- which shall also be **laid before the annual general meeting** of the company along with the laying of its standalone financial statements.

Thus, there is a legal requirement to prepare BOTH consolidated financial statements and standalone financial statements, both of which shall be laid before the Annual General Meeting.



CONSOLIDATION PRINCIPLES

1. Consolidation commences from the date an entity acquires control over another entity and ends upon loss of such control. The controlling entity is also known as 'parent company', or 'holding company', and the entity being controlled is also known as a 'subsidiary'. *The accounting guidance under Ind AS 103, Business Combinations is applicable only on the date of acquisition. Subsequent consolidated financial statements are prepared in accordance with the guidance of Ind AS 110, Consolidated Financial Statements.*
2. Irrespective of the stake in the subsidiary (academically, could be any number between 51% to 100%; practically, perform the test of control as discussed at length in the Business Combinations chapter) all items of assets and liabilities (excluding share capital and reserves / other equity), incomes and expenses of the subsidiary shall be added line-by-line with that of the parent.
3. The **Parent's Investment in Subsidiary** shall be **eliminated against the Parent's share in the Subsidiary's equity** (i.e., Equity Share Capital and Pre-acquisition Reserves) on the date of acquisition. The difference, if any, on such elimination would represent goodwill / capital reserve / gain on bargain purchase. *This is because such Equity Share Capital and Pre-acquisition Reserves of the Subsidiary are nothing but the Net Assets of the Subsidiary on the date of acquisition, which are being compared with the purchase consideration shown as Investment in Subsidiary in the books of the Parent.* Academically, unless otherwise mentioned, the Investment in Subsidiary appearing the standalone financial statements of the parent is always at cost. This elimination could be done by opening a 'Cost of Control A/c' in the Consolidated Books (and not in the standalone books). Alternatively, the elimination could be done in the form of a statement.



CONSOLIDATION PRINCIPLES

4. The share in the Subsidiary's Equity which is not attributable to the Parent would be shown as Non-Controlling Interest (NCI). Ind AS 103, *Business Combinations* permits NCI to be valued at Fair Value (thereby giving rise to full goodwill attributable to both Parent and NCI), or at Proportionate Share in Net Assets (thereby giving rise to partial goodwill attributable to only the Parent). However, post-acquisition, NCI would change due to NCI's share in post-acquisition reserves of the Subsidiary. In other words, fair valuing the NCI is done only on the date of acquisition and not thereafter; any subsequent movement in the NCI is only due to share in post-acquisition profits.
5. The Reserves of the Subsidiary need to be analysed as pre-acquisition and post-acquisition, which would thereafter be allocated between Parent and NCI based on their respective holdings.

The Parent's share in the Pre-acquisition Reserves would appear in the Cost of Control against the Investment in the Subsidiary, as the parent would have paid the Purchase Consideration to acquire those shares. In other words, Pre-acquisition Reserves and Equity Share Capital would always be 'purchased' from the owners of Subsidiary on the date of acquisition. Accordingly, if there is any profit on such business acquisition, it is regarded as a Capital Profit, credited to Capital Reserve. Shortfall, if any would be regarded as goodwill.

Further, the Parent's share in the Post-acquisition Reserves would be added while calculating Consolidated Reserves, as these profits are earned by the Parent (and not purchased), while the Parents was in control of the subsidiary.



STEPS IN THE CONSOLIDATION PROCESS

1. Prepare Balance Sheet in Schedule III Format.
2. Prepare Consolidation Notes as under: (Illustrative list only)

Note 1: Assets and Liabilities

Particulars	Parent	Subsidiary	Consol. Adj.	Total
Property, Plant and Equipment	xxx	xxx	xxx	xxx
Inventories	xxx	xxx	xxx	xxx
Trade Receivables	xxx	xxx	xxx	xxx
Long-term Borrowings	xxx	xxx	xxx	xxx

All items of assets / liabilities as appearing in the Standalone Balance Sheets of the Parent and Subsidiary **before** making any adjustments should be recorded above. However, the following items shall be excluded :

- a. Investment in subsidiary, as appearing in the parent's books
- b. Equity Share Capital of the parent and the subsidiary
- c. Reserves and Other Equity (of the parent and the subsidiary)



STEPS IN THE CONSOLIDATION PROCESS

Note 2: Equity Share Capital –

Only the Parent's Share Capital shall be recorded

Note 3: Other Equity (prepared in case there are more than one item of Reserves - from Working Note 1)

3. Prepare the following Working Notes:

Working Note 1: Consolidated Other Equity (8-10 lines)

Particulars	P/L	General Reserve	Securities Premium	Total
Balance on Date of Consolidation (from Parent's Standalone Balance Sheet)	xxx	xxx	xxx	xxx
Add: Share in Post- acquisition Profits of Subsidiaries (from Working Note 4)	xxx	xxx	xxx	xxx
TOTAL CONSOLIDATED BALANCE (transferred to Note 3)	xxx	xxx	xxx	xxx



STEPS IN THE CONSOLIDATION PROCESS

Working Note 2: Cost of Control – COC A/c (% Stake of Parent in Subsidiary)

Particulars	Rs.	Particulars	Rs.
To Investment in Subsidiary (from Parent's Standalone Balance Sheet)	xxx	By Equity Share Capital (Subsidiary's Capital x % of Parent Holding)	xxx
To Gain on Bargain Purchase / Capital Reserve (balancing figure)	xxx	By Pre-Acquisition Reserves (from Working Note 4)	xxx
		By Goodwill (balancing figure)	xxx
	xxx		xxx

The above may be prepared in a statement form as well.

For academic understanding, the above ledger account is prepared in the 'Consolidated / Group Books'. This ledger cancels out the Investment in the Subsidiary by the Parent, resulting in comparison of the Investment Value in the Subsidiary with the % of Net Assets (represented by Equity Share Capital + Reserves on the Date of Acquisition) thereby giving rise to Goodwill / Capital Reserve as a balancing figure.



STEPS IN THE CONSOLIDATION PROCESS

Working Note 3: Non-Controlling Interest – NCI A/c (% Stake of NCI)

Particulars	Rs.	Particulars	Rs.
		By Equity Share Capital (Subsidiary's Capital x % of NCI Holding)	xxx
To balance c/d (on Date of Acquisition)	xxx	By Pre-Acquisition Reserves (from Working Note 4)	xxx
	xxx		xxx
		By balance b/d	xxx
To balance c/d (on Date of Consolidation)	xxx	By Post-Acquisition Reserves (from Working Note 4)	xxx
	xxx		xxx

The above may be prepared in a statement form as well.



STEPS IN THE CONSOLIDATION PROCESS

Working Note 3: Non-Controlling Interest (% Stake of NCI)

- Unless given otherwise, NCI needs to be calculated using the Proportionate Net Assets method. A note to that effect would need to be given.
- Where NCI on the date of acquisition is specifically asked, the balance of share capital and pre-acquisition reserves should be shown as in the first part of the proforma above, showing NCI on the date of acquisition.
- If NCI on the date of acquisition should be calculated using the fair value method, the first part of the NCI A/c would be modified as follows:

Particulars	Rs.	Particulars	Rs.
To balance c/d (at Fair Value)	xxx	By Equity Share Capital (Subsidiary's Capital x % of NCI Holding)	xxx
		By Pre-Acquisition Reserves (from Working Note 4)	xxx
		By Goodwill (balancing figure)	xxx
	xxx		xxx



STEPS IN THE CONSOLIDATION PROCESS

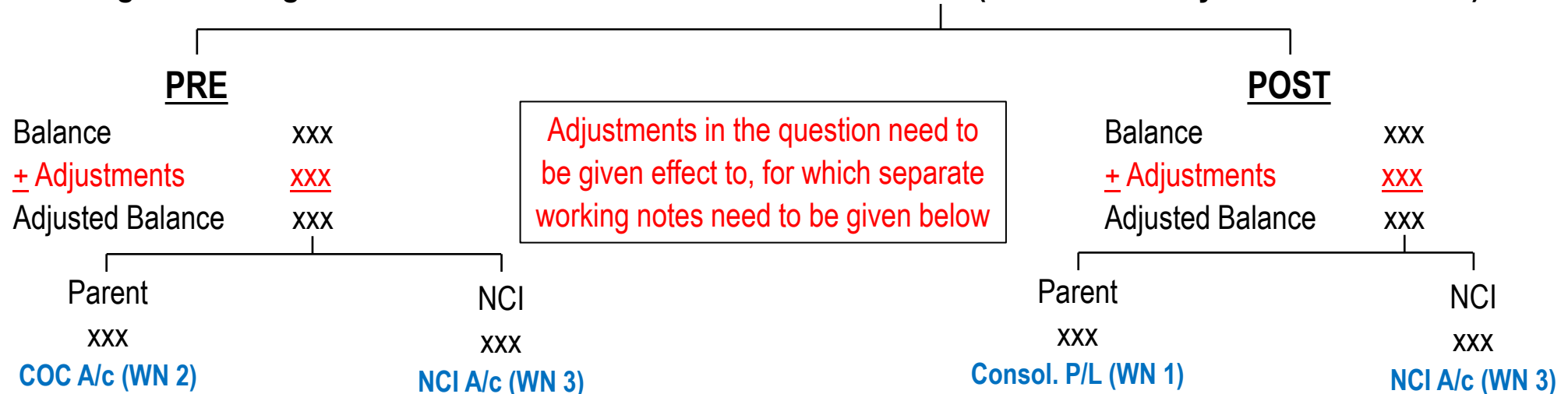
Working Note 3: Non-Controlling Interest (% Stake of NCI)

c. (continued) The second part of the NCI A/c would be the same as before (Slide No. 10). In such case, the Goodwill would be calculated as under:

$$\text{Goodwill (Full)} = \text{Goodwill from COC A/c (WN 2)} + \text{Goodwill from NCI A/c (WN 3)}$$

4. Analysis of Reserves of Subsidiary: to be done for each Reserve of the Subsidiary

Working Note 4: e.g. Balance in P/L on Date of Consolidation xxx (from subsidiary's standalone B/S)





STEPS IN THE CONSOLIDATION PROCESS

5. Give effect to all Consolidation Adjustments such as inter-company debtors / creditors, inter-company borrowings
6. After all adjustments are considered, balance / total the Working Notes 1, 2 and 3 in Step 3 above. Total up the items in Note 1, and post the amounts under the appropriate headings in the Consolidation Balance Sheet.

Can NCI be negative?

Under the Ind AS regime, NCI is treated as a part of Equity. This is because, from the perspective of the Parent, it does not represent any obligation to deliver cash.

Components of Equity can have a negative / debit balance (e.g. net worth can be negative in case of a P/L Debit balances (i.e., accumulated losses).

Since NCI is a part of Equity, it can also have a negative (i.e., debit) balance. No further adjustments are required in this regard.



CONSOLIDATION ADJUSTMENTS

I. Fair Value Adjustments

Ind AS 103 requires Net Assets of the Subsidiary to be taken over at fair values on the Date of Acquisition. Where the fair values are not given, it is safe to assume that book values are equal to fair values. However, where the fair values on the Date of Acquisition are separately given in the question, certain fair value adjustments need to be made for the purposes of Consolidation. These adjustments need to be made because it is permitted for the Subsidiary to record the assets using the Cost model in its standalone books and not necessarily revalue them merely because the Parent is attributing a higher / lower value of the Date of Acquisition.

Therefore, unless specifically given, it is always assumed that the Subsidiary's assets are not revalued in its standalone books. However, in consolidated books, the assets have to appear at fair values on the Acquisition Date.

General Rule:

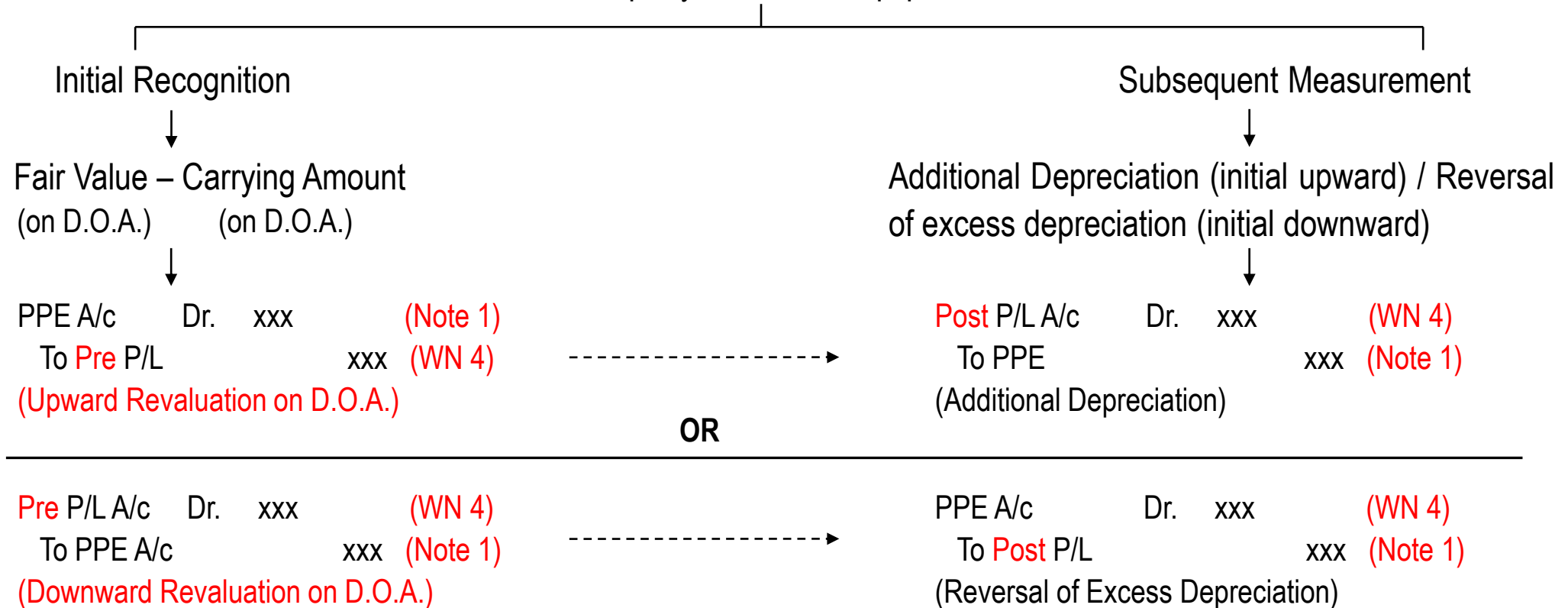
1. Initial changes in Fair Value (upward / downward) will always go to the Pre-reserves as they reflect the changes that have already happened till the Date of Acquisition.
2. Subsequent events like Depreciation / sale would always be adjusted against post-reserves, as these events happen after the Date of Acquisition.



CONSOLIDATION ADJUSTMENTS

I. Fair Value Adjustments

A. Property, Plant and Equipment

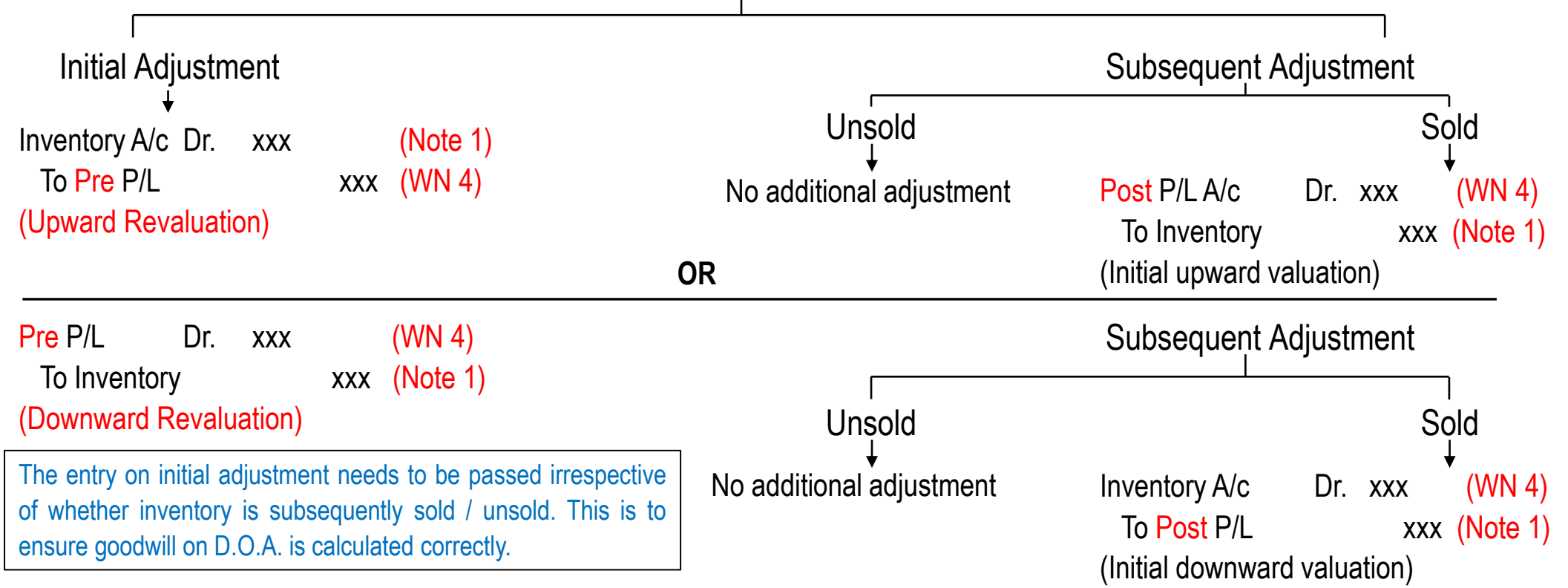




CONSOLIDATION ADJUSTMENTS

I. Fair Value Adjustments

B. Inventory



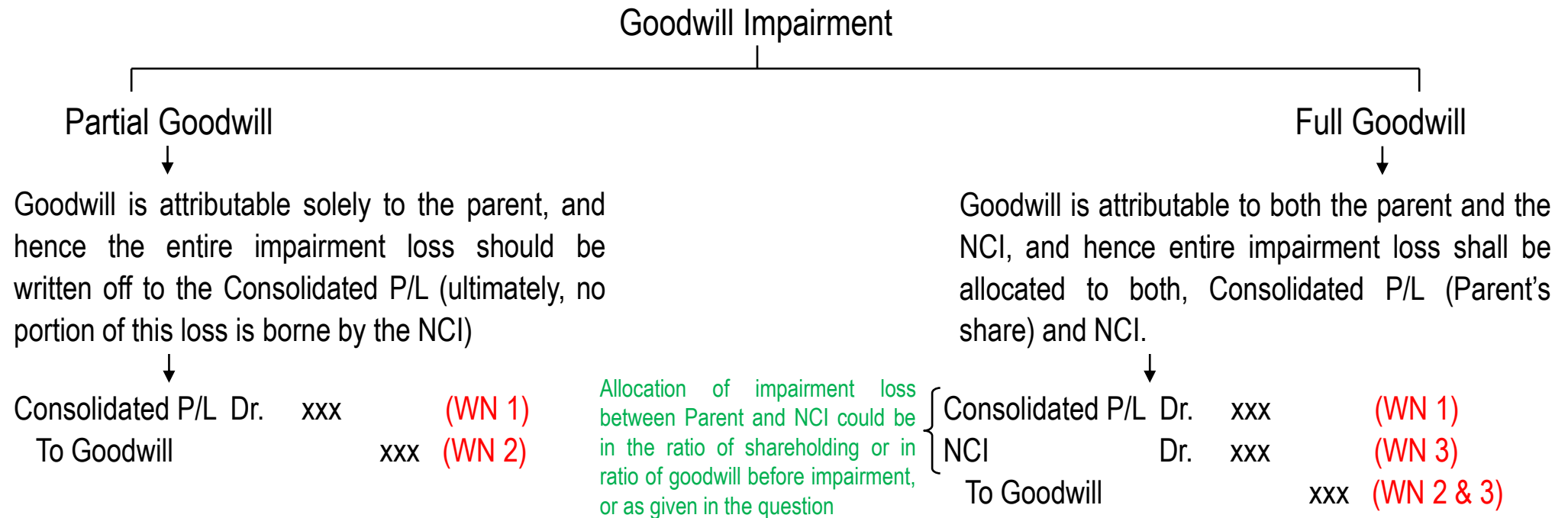
The entry on initial adjustment needs to be passed irrespective of whether inventory is subsequently sold / unsold. This is to ensure goodwill on D.O.A. is calculated correctly.



CONSOLIDATION ADJUSTMENTS

II. Impairment of Goodwill

Ind AS 36 requires goodwill to be tested annually for impairment. In case goodwill is impaired, the impairment loss needs to be written off as under:



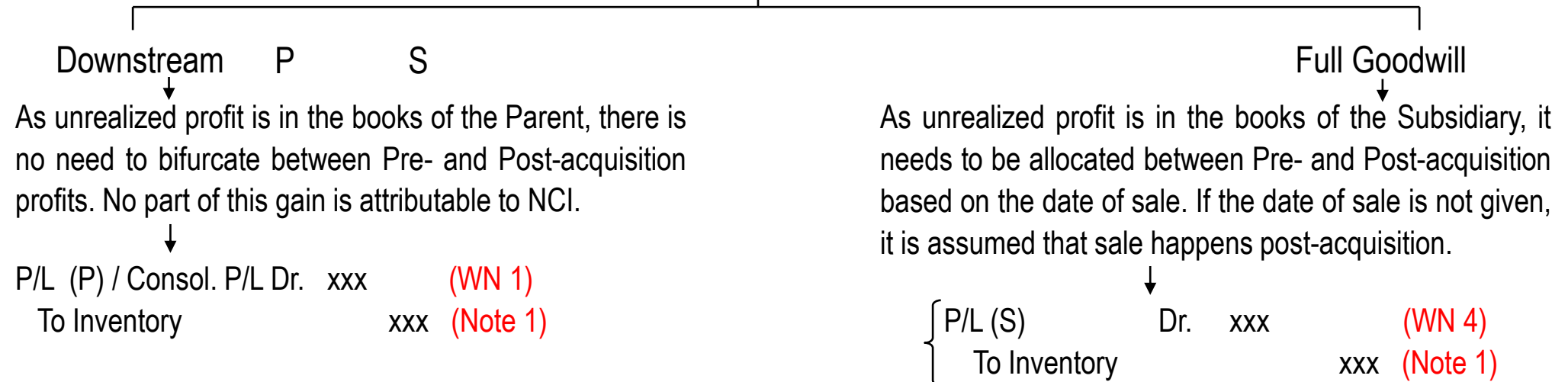


CONSOLIDATION ADJUSTMENTS

III. Unrealized Profit on inter-company transactions

Consolidated Financial Statements represent the Financial Statements of the group, presented as that of a single entity. Accordingly, unrealized profits should be eliminated from the books of the company which made the sale in an inter-company transaction. This elimination will be done till the time the goods remain unsold and are lying with either of the group entity i.e. till the time they are not ultimately sold to an outsider

Inventory Adjustment





CONSOLIDATION ADJUSTMENTS

III. Unrealized Profit on inter-company transactions

1. Upstream / Downstream transfer of PPE:

The adjustment would remain exactly as above in case of inventory, except that instead of adjusting inventory, PPE is adjusted. Further, there would be an additional entry to reverse additional depreciation (if any) that would be recorded in the standalone books of the acquirer.

2. Unrealised Losses

The accounting for unrealised losses would be the same as that of unrealised gains i.e. unrealised losses also need to be eliminated. This is because inter-company transfer price is not necessarily the NRV.



CONSOLIDATION ADJUSTMENTS

IV. Uniform Accounting Policies

Ind AS 110 requires preparation of Consolidated Financial Statements by following uniform accounting policies for the parent and subsidiary for like-to-like (i.e. similar) transactions.

This implies that the same items should be accounted as per the same accounting policies. If the accounting policies of the Subsidiary are different, then they need to be restated so as to bring them in line with the accounting policies of the Parent. A separate working note should be prepared for the Subsidiary prior to consolidation where the accounting policies would be restated as per Ind AS 8 principles. This restatement is required only for like-to-like items. Different items can continue to be accounted as per different accounting policies even in the Consolidated Financial Statements.

Further, the subsidiary, in its Standalone Financial Statements is permitted to follow accounting policies independent of the parent (although practically it is rare); just that at the time of Consolidation, the Subsidiary's financials need to be restated.

Adjustments for accounting policies are mandatory, whereas adjustments for accounting estimates are optional.



CONSOLIDATION ADJUSTMENTS

V. Different Reporting Dates

Different Reporting Dates of the Parent and the Subsidiary (rare, but possible)



Restate Subsidiary's Balance Sheet as on the Parent's Reporting Date

Reporting Date

Difference \leq 3 months



Material Events in the intermediate period should be adjusted and restated Balance Sheet should be prepared after incorporating the effects for the material items.

Material Events are those events which are identified by the management. It would be given in the question.

Difference $>$ 3 months



Detailed financial statements need to be prepared. Mere adjustments for material items not permitted.

In case of these questions, first prepare the draft balance sheet of the Subsidiary (restated) as on the date of Consolidation and then follow the usual steps.



CONSOLIDATION ADJUSTMENTS

VI. Inter-company Eliminations

1. Debtors / Creditors (OR Bills Receivable / Bills Payable):

Inter-company balances should be eliminated by giving effects in the Consolidation Adjustments Column of Note 1. usually, the inter-company balances are the same. In rare cases where such balances do not match, the difference would be usually attributable to cash/ cheques-in-transit.

2. Inter-company Loans given / taken:

These balances also need to be eliminated while preparing Note 1. Where interest on such loan is not recorded, a separate entry for such interest needs to be passed first followed by elimination.

3. Inter-company Debentures / Preference Shares:

Usually, redeemable debentures / preference shares issued are regarded as financial liabilities and hence inter-company debentures / preference shares should be eliminated by preparing Note 1.



CONSOLIDATION ADJUSTMENTS

VI. Inter-company Eliminations

3. Inter-company Debentures / Preference Shares (continued):

However, where such debentures are tradeable instruments, the purchase of such debentures might have happened at a price other than what is recorded by the issuer. Such difference, if any, on elimination must be adjusted in the Consolidated P/L as it represents a loss (or gain) on settlement of a liability.

However, in rare cases, if debentures / preference shares get classified as equity, their elimination should be similar to that of equity shares i.e. through COC A/c and NCI A/c and not through Note 1 as above.

Where the question is silent, it is assumed that the preference shares / debentures are in the nature of financial liabilities.



CONSOLIDATION ADJUSTMENTS

VI. Inter-company Eliminations

3. Inter-company Debentures / Preference Shares (continued):

Classified as a **Financial Liability** (to be assumed as such unless otherwise given)



Eliminated through **Note 1** and difference taken to **Consolidated P/L**

Classified as **Equity** (should be specifically given)



Eliminated through **COC A/c (WN 2)** and **NCI (WN 3)**

Difference between investment and inter-company liability / capital will automatically be adjusted in goodwill



CONSOLIDATION ADJUSTMENTS

VI. Inter-company Eliminations

3. Inter-company Debentures / Preference Shares (continued):

E.g.:

Books of Parent:

Investment in Debentures / Preference Shares of Subsidiary	₹ 6,000
(5,000 Preference Shares / Debentures at Market Price of ₹ 1.20)	(Face Value ₹ 5,000)

Books of Subsidiary

Debentures / Preference Share Capital	₹ 10,000
(10,000 Preference Shares / Debentures x Face Value ₹ 1)	



CONSOLIDATION ADJUSTMENTS

VI. Inter-company Eliminations

3. Inter-company Debentures / Preference Shares (continued):

Solution:

Case 1: Instruments are classified as financial liabilities (no impact on COC A/c or NCI)

Note 1 - Extract

Particulars	Parent	Subsidiary	Consol. Adj.	Total
Investment in Debentures	6,000	---	(6,000)	---
			Entire balance eliminated as it is an inter-company balance)	
Debentures	---	10,000	(5,000)	5,000
			Only face value can be eliminated	



CONSOLIDATION ADJUSTMENTS

VI. Inter-company Eliminations

3. Inter-company Debentures / Preference Shares (continued):

Solution:

Case 1 (continued): Instruments are classified as financial liabilities (no impact on COC A/c or NCI)

Working Note 1: Consolidated P/L - Extract

Balance from Standalone P/L		xxx	
Less: Loss on Elimination		(1,000)	
Add: Share in Post-acquisition Profits of Subsidiary		xxx	
Consolidated P/L transferred to Balance Sheet		xxx	
<u>Journal Entry:</u>			
Debentures / Preference Share Capital (Subsidiary)	Dr.	xxx	
Loss on Elimination	Dr.	xxx	
To Investment in Debentures / Preference Shares(Parent)			xxx



CONSOLIDATION ADJUSTMENTS

VI. Inter-company Eliminations

3. Inter-company Debentures / Preference Shares (continued):

Solution:

Case 2: Instruments are classified as Equity (no effect in Note 1 / Working Note 1)

Particulars	<u>COC A/c</u>	
	₹	₹
To Invt. in Equity Share	xxx	By Equity Share Capital xxx
To Invt. in Preference Shares / Debentures	6,000	By Pre-acquisition Reserves xxx
		By Preference Share Capital / Debentures 5,000 (1,000 x 50%)
		By Goodwill (increases by ₹ 1,000) xxx
	<u>xxx</u>	<u>xxx</u>



CONSOLIDATION ADJUSTMENTS

VI. Inter-company Eliminations

3. Inter-company Debentures / Preference Shares (continued):

Solution:

Case 2 (continued): Instruments are classified as Equity (no effect in Note 1 / Working Note 1)

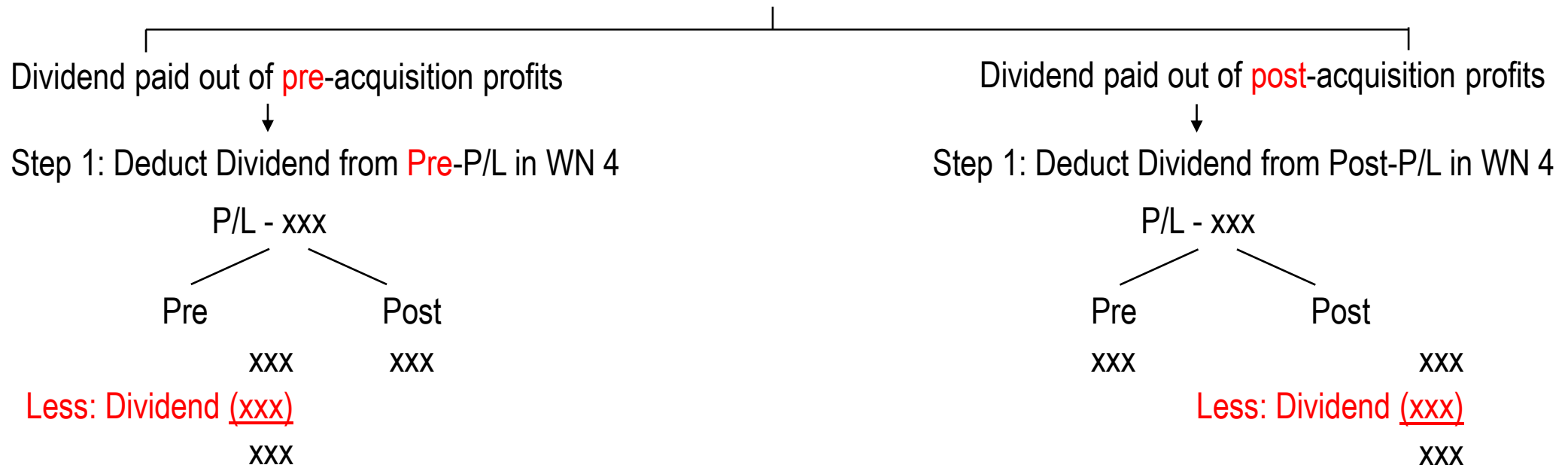
Particulars	<u>NCI A/c</u>		
	₹	Particulars	₹
		By Equity Share Capital	xxx
		By Pre-acquisition Reserves	xxx
		By Preference Share Capital / Debentures	5,000
To balance c/d. (increases by ₹ 5,000)	xxx	(10,000 x 50%)	
	<u>xxx</u>		<u>xxx</u>



CONSOLIDATION ADJUSTMENTS

VII. Dividend Adjustments

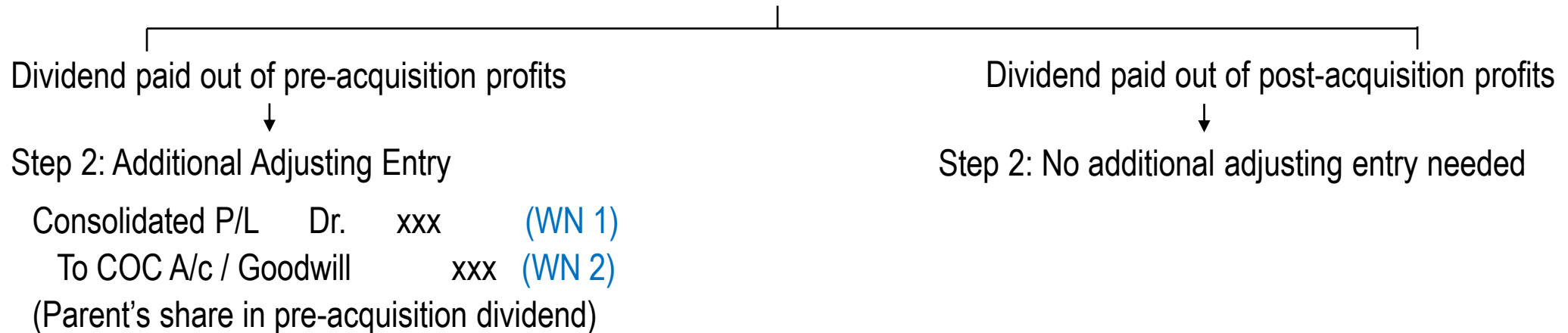
In case dividend is paid by the subsidiary, it must be analysed whether such dividend is paid out of pre-acquisition profits or post-acquisition profits. If the question is silent, it is assumed that the dividends are paid out of post-acquisition profits (unless profits are insufficient).





CONSOLIDATION ADJUSTMENTS

VII. Dividend Adjustments (continued)



The additional adjustment for pre-acquisition dividend is required because profits were actually in existence (i.e. undistributed) on the date of acquisition, and do not exist (i.e. distributed) on the date of consolidation. Since dividends are paid out of such pre-acquisition profit, these profits do not appear while analysing the Reserves of the Subsidiary (in WN 4) as on the date of consolidation. However, goodwill is calculated on the date of acquisition and since these profits did exist on the date of acquisition, they need to be considered in the goodwill calculation, else goodwill calculation will be incorrect.



CONSOLIDATION ADJUSTMENTS

VII. Dividend Adjustments (continued)

Moreover, in the standalone books of the parent, dividend income would have been recorded in its P/L as the parent was the shareholder on the record date when the dividend was distributed. However, as this dividend is distributed from the pre-acquisition profits, it should not appear in the consolidated P/L: since the pre-acquisition profits of the subsidiary are not consolidated.

Hence, the above adjusting entry needs to be passed in case of pre-acquisition dividends.

Where dividends are paid out of post-acquisition profits, it will not impact the goodwill since it does not pertain to profits on the date of acquisition. Further, since the profits have been earned post-acquisition, the parent's share of these profits should appear in the consolidated P/L. As parent must have already recorded the dividend received, it is already a part of Consolidated P/L and hence, no other adjustment is needed.



CONSOLIDATION ADJUSTMENTS

VIII. Acquisition date different from Opening Balance Sheet date

In such cases, prepare a working note to calculated profits after tax (PAT) after the opening balance sheet date. Profits can be assumed to accrue uniformly throughout the year if not specified otherwise, and hence these profits which are calculated will be proportionately split between pre- and post-acquisition periods.

Calculation of Profits (similar to P/L Appropriation A/c):

Opening Balance	xxx	(PRE ACQUISITION)
Add: Profits (balancing figure)	xxx	(Proportionate)
Less: Dividends	<u>(xxx)</u>	(As per data given)
Closing Balance	<u>xxx</u>	



CONSOLIDATION ADJUSTMENTS

- IX. Additional Stake Purchase (summary notes already shared and uploaded)**
- X. Stake Sale (summary notes already shared and uploaded)**
- XI. Chain Holding (summary notes already shared and uploaded)**



THEORY TO BE COVERED FROM STUDY MODULE

- **About Investment Entities**
- **Non-preparation of Consolidated Financial Statements: Exemption to Investment Entities**
- **Non-preparation of Consolidated Financial Statements: Exemption to Intermediate Entities**



THANK YOU