

PRINCIPLES OF CONSOLIDATION

THE CONSOLIDATED BALANCE SHEET

The basic principle of a consolidated balance sheet is that it shows all assets and liabilities of the parent and subsidiary.

Intra-group items are excluded e.g. debtors and creditors shown in the consolidated balance sheet only include amounts owed from/to third parties.

Basic method of Preparation

- (1) The investment in the subsidiary (S) shown in the parent's (P's) balance sheet is replaced by the net assets of S.
- (2) The cost of the investment in S is effectively cancelled with the ordinary share capital and reserves of the subsidiary

This leaves a consolidated balance sheet showing;

- The net assets of the whole group (P + S)
- The share capital of the group always equals the share capital of P only
- The retained profits, comprising profits made by the group (i.e. all of P's historical profits + profits made by S post acquisition)

EXAMPLE 1

On 1 January 2012, Austin Ltd acquired all of Reed Ltd.'s ordinary shares, paying £15000 cash.

Reproduced below are the balance sheets of the two companies as 31 January 2012.

	A		R	
	£000	£000	£000	£000
Fixed assets				
Plant and equipment		80		8
Investment in Reed Ltd		<u>15</u>		<u>-</u>
		95		8
Current assets				
Stocks	100		12	
Debtors	80		12	
Cash at bank	<u>20</u>		<u>-</u>	
	<u>200</u>		<u>24</u>	
Creditors: amounts falling due within one year				
Trade creditors	<u>165</u>		<u>17</u>	
Net current assets		35		7
		<u>130</u>		<u>15</u>
Share capital and reserves				
Ordinary shares of £1 each		100		10
Profit and loss reserve		<u>30</u>		<u>5</u>
		<u>130</u>		<u>15</u>

REQUIREMENT

Prepare the consolidated balance sheet at 1ST January 2012.

EXAMPLE 1

CONSOLIDATED B/S AT 1-1-12 £1000

£1000

Tangible Fixed Assets:

Plant + Equipment (80+8)

88

Current Assets:

Stock (100+12)

112

Debtors (80+12)

92

Cash at Bank

20

224

Creditors > 1 yr:

Trade creditors (165+17)

(182)

Net Current Assets

42

130

Ordinary share capital
Profit and Loss Account

100

30

130

GOODWILL ON CONSOLIDATION (FRS 102: Section 19)

The acquirer shall, at the acquisition date:

- (a) recognise goodwill acquired in a business combination as an asset; and
- (b) initially measure that goodwill at its cost, being the excess of the cost of the business combination over the acquirer's interest in the net amount of the identifiable assets, liabilities and contingent liabilities

After initial recognition, the acquirer shall measure goodwill acquired in a business combination at cost less accumulated amortisation and accumulated impairment losses.

Goodwill shall be considered to have a finite useful life, and shall be amortised on a systematic basis over its life. If, in exceptional cases, an entity is unable to make a reliable estimate of the useful life of goodwill, the life shall not exceed 10 years.

EXAMPLE 2

On 1 January 2012, Austin Ltd acquired all of Reed Ltd.'s ordinary shares, paying £17000 cash.

Reproduced below are the balance sheets of the two companies as 1 January 2012.

	A		R	
	£000	£000	£000	£000
Fixed assets				
Plant and equipment		80		8
Investment in Reed Ltd		<u>17</u>		<u>-</u>
		97		8
Current assets				
Stocks	100		12	
Debtors	80		12	
Cash at bank	<u>18</u>		<u>-</u>	
	198		24	
Creditors: amounts falling due within one year				
Trade creditors	<u>165</u>		<u>17</u>	
Net current assets		33		7
		<u>130</u>		<u>15</u>
Share capital and reserves				
Ordinary shares of £1 each		100		10
Profit and loss reserve		<u>30</u>		<u>5</u>
		<u>130</u>		<u>15</u>

REQUIREMENT

Prepare the consolidated balance sheet at 1ST January 2012.

EXAMPLE 2

CONSOLIDATION SCHEDULES

✓ Goodwill

	£1000
Cost of investment	17
less: share of net assets acquired (100% x 15000)	(15)
Goodwill	<u>2</u>

CONSOLIDATED BALANCE SHEET AT 1-1-12

	£1000	£1000
Intangible Fixed Assets: goodwill		2
Tangible Fixed Assets Plant + Machinery (80 + 8)		<u>88</u>
		90
Current Assets:		
Stock (100 + 12)	112	
Debtors (80 + 12)	92	
Cash at Bank	18	
	<u>222</u>	
Creditors > 1 yr:		
Trade Creditors (165 + 17)	(182)	
Net Current Assets	<u></u>	40
		<u>130</u>

Ordinary share capital
Profit & Loss Account

100

30

130

PRE – ACQUISITION PROFITS

The consolidated retained profits, comprising profits made by the group is calculated as all of P's historical profits + profits made by S *post acquisition*.

EXAMPLE 3

On 1 January 2012, Austin Ltd acquired all of Reed Ltd.'s ordinary shares, paying £17000 cash.

Reproduced below are the balance sheets of the two companies as 31 December 2014.

Goodwill on consolidation is amortised over a period of 5 years. A full year's charge is made in the year of acquisition.

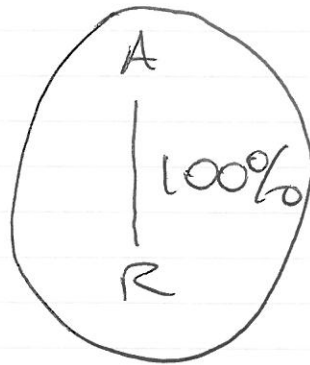
	A £000	£000	R £000	£000
Fixed assets				
Plant and equipment		85		11
Investment in Reed Ltd		<u>17</u>		<u>-</u>
		102		11
Current assets				
Stocks	120		20	
Debtors	80		13	
Cash at bank	<u>14</u>		<u>-</u>	
	<u>214</u>		<u>33</u>	
Creditors: amounts falling due within one year				
Trade creditors	<u>176</u>		<u>25</u>	
Net current assets		38		8
		<u>140</u>		<u>19</u>
Share capital and reserves				
Ordinary shares of £1 each		100		10
Profit and loss reserve		<u>40</u>		<u>9</u>
		<u>140</u>		<u>19</u>

REQUIREMENT

Prepare the consolidated balance sheet at 31ST December 2014.

EXAMPLE 3

(W1) GROUP STRUCTURE



(W2) NET ASSETS OF REED LTD

	(1-1-12) At Acquisition £'000	(31-12-14) At B/S DATE £'000
Share capital	10	10
P+L A/c	5	9
	<u>15</u>	<u>19</u>

CONSOLIDATION SCHEDULES

1/ GOODWILL

	£000
Cost of investment	17
less: share of net assets acquired (100% x 15000)	(15)
Goodwill	<u>2</u>
less: amortised to date (3/5 x 2000)	(1.2)
Intangible Asset	<u><u>0.8</u></u>

2/ CONSOLIDATED P+L A/C Reserve

	£000
Austin Ltd	40
Reed Ltd: share of post acquisition profits 100% x (9 - 5)	4
less: goodwill amortised to date	(1.2)
	<u><u>42.8</u></u>

CONSOLIDATED BALANCE SHEET AT 31-12-14

	£1000	£1000
Intangible Fixed Assets: goodwill		0.8
Tangible Fixed Assets		
Plant + Machinery (85 + 11)		96
		<u>96.8</u>
Current Assets:		
Stock (120 + 20)	140	
Debtors (80 + 13)	93	
Cash at Bank	14	
	<u>247</u>	
Creditors > 1 yr:		
Trade creditors (176 + 25)	(201)	
Net Current Assets		<u>46</u>
		<u><u>142.8</u></u>
Ordinary share capital		100
Profit + Loss account		42.8
		<u><u>142.8</u></u>

MINORITY INTERESTS

If control has been achieved by the parent, the minority shareholders will hold a non-controlling interest.

This is calculated as the minority's share of the net assets of the subsidiary at the balance sheet date.

EXAMPLE 4

On 1 January 2013, Dickens Ltd acquired 24000 of Jones Ltd.'s ordinary shares, paying £60000 cash. The profit and loss account of Jones at that date stood at £20000.

Reproduced below are the balance sheets of the two companies as 31 December 2014.

Goodwill on consolidation is amortised over a period of 5 years. A full year's charge is made in the year of acquisition.

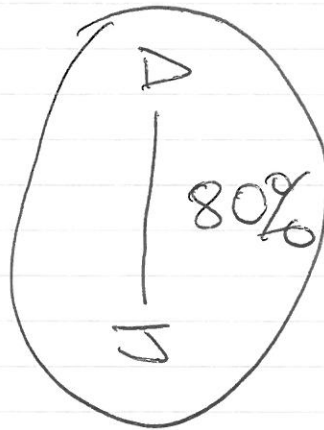
	D		J	
	£000	£000	£000	£000
Fixed assets				
Plant and equipment		85		18
Investment in Reed Ltd		<u>60</u>		<u>-</u>
		145		18
Current assets				
Stocks	120		20	
Debtors	30		64	
Cash at bank	<u>10</u>		<u>-</u>	
	<u>160</u>		<u>84</u>	
Creditors: amounts falling due within one year				
Trade creditors	<u>135</u>		<u>47</u>	
Net current assets		25		37
		<u>170</u>		<u>55</u>
Share capital and reserves				
Ordinary shares of £1 each		100		30
Profit and loss reserve		<u>70</u>		<u>25</u>
		<u>170</u>		<u>19</u>

REQUIREMENT

Prepare the consolidated balance sheet at 31ST December 2014.

EXAMPLE 4

(W1) GROUP STRUCTURE



$$\frac{24000}{30000} = \underline{80\%}$$

(W2) NET ASSETS OF JONES LTD

	(1-1-13) AT ACQUISITION £'000	(31-12-14) AT RE DATE £'000
Share capital	30	30
P+ C Account	20	25
	<u>50</u>	<u>55</u>

CONSOLIDATION SCHEDULE

1/ GOODWILL

£000

Cost of investment

60

less: share of net assets acquired
 $80\% \times 50000$

(40)

Goodwill

20

less: amortised to date
 $(\frac{2}{5} \times 20000)$

(8)

Intangible Asset

12

2/ Minority Interest

£

$$= 20\% \times 55000 =$$

11

3/ CONSOLIDATED P/L A/C RESERVE

f1000

DICKENS

70

JONES

share of post-acquisition profits
80% x (25 - 20)

4

less: goodwill amortised to date

(8)

66

Consolidated B/S At 31-12-14

	£1000	£1000
Intangible Fixed Assets: goodwill		12
Tangible Fixed Assets (85 + 18)		103
		115

Current Assets:	
Stock (120 + 20)	140
Debtors (30 + 64)	94
Cash at Bank	10
	244

Creditors < 1 yr:	
Trade creditors (135 + 47)	(182)
Net Current Assets	62
	177

Ordinary share capital	100
Profit & loss account	66
	166

Minority interest	11
	177

CANCELLATION OF INTRA – GROUP BALANCES

When group companies trade with each other, there are several ways in which balances with each other can arise:

- Loans and debentures
- Current accounts (intra group debtors and creditors)

The cancellation process is very easy in that the credit balance of one company is offset against the debit balance of the other company, thus eliminating both balances from the consolidated balance sheet.

EXAMPLE (CASH IN TRANSIT)

The following balances exist at 31 December 2014:

	Books of P Ltd	Books of S Ltd
S Ltd current account	10700 DR	
P Ltd current account		10000CR

On 31st December 2014, S Ltd sent a cheque to P Ltd for £700 which the latter company did not record until 2 January 2015.

In the books of P Ltd:	DR	Cash at bank	£700
	CR	S Ltd current account	£700

And the current account balances of £10000 can then be cancelled out.