QUESTION 26: BASIC CONSOLIDATION

Innovators Ltd., an engineering company, is engaged in manufacturing and supply of industrial machines. The company is specialized in textile machinery and is engaged in this business for the last 20 years. In 2010, management decided to increase the business by manufacturing machinery for other industries as well. This required huge investment and long time to setup the basic structure, so the management decided to acquire another company. On July 1, 2011, Innovators Ltd., purchased 8 million shares of Elite Engineering at Rs. 25 per share.

Elite Engineering is newly incorporated company engaged in manufacturing and supply of machinery related to a Fast-Moving Consumer Goods (FMCG) company. Till the time of acquisition, Elite Engineering could not gain good market share but Innovators Ltd., expected that they would capture good market share using their experience and goodwill. On January 1, 2013, after successful operation of Elite Engineering, the management of Innovators Ltd., also acquired 60% share in Alco Company, importer and supplier of machine parts. Innovators Ltd., paid Rs. 12.5 per share at the time of acquisition and would pay Rs. 2.8 per share after one year. Innovators Ltd.'s cost of capital is 12%.

The summarised statements of profit or loss of three companies for the year ended June 30, 2013 are:

Statement of Profit or Loss

	Innovators Limited	Elite Engineering	Alco Company
		Rs. 000	
Revenue	225,000	105,300	72,000
Cost of sales	(141,000)	(68,850)	(54,000)
Gross profit	84,000	36,450	18,000
Marketing and distribution expenses	(11,100)	(4,050)	(3,150)
Administrative expenses	(18,750)	(8,100)	(5,850)
Other income (including dividend)	15,000	1,000	500
Financial charges	(3,000)	(1,215)	(450)
Profit before tax	66,150	24,085	9,050
Income tax	(15,600)	(4,860)	(3,600)
Profit after tax	**50,550**	**19,225**	**5,450**

Additional Information:

(i) The fair value of net assets of Elite Engineering was higher than carrying value by Rs. 20 million, which pertains to the property having remaining useful life of 20 years at acquisition. While the fair value of Alco Company was higher than carrying value by Rs. 10 million, which pertains to the plant having remaining useful life of 10 years at the date of acquisition. It is the company policy to charge depreciation of above assets to cost of sales.

(ii) The statement of changes in equity showed following balances: **Rs. in .000.**

Items	Innovators Ltd.	Elite Engineering		Alco Company
	30/06/2012	30/06/2011	30/06/2012	30/06/2012
Share capital (Rs.10 each)	250,000	100,000	100,000	80,000
Share premium	100,000	25,000	25,000	5,000
Retained earnings	160,000	40,000	55,000	12,000

No new shares have been issued by any company in 2012-2013.

(iii) In May 2013, Innovators Ltd., received an order of supply of a machine from a FMCG company for Rs. 5 million. The management of Innovators Ltd., asked Elite Engineering to supply the machine. In June 2013, Elite Engineering imported this machine for Rs. 3.50 million and supplied the same to Innovators Ltd., for Rs. 4.50 million. Innovators Ltd., after customer satisfaction delivered the machine in July 2013. The revenue from the machine was recorded in the month of July 2013 by Innovators Ltd.

(iv) In March 2013, Alco Company sold machine parts to Innovators Ltd., for Rs. 2.50 million and charged 20% margin on sales. 50% of these parts are still in the inventory of Innovators Ltd., at year-end.

(v) In January 2013, Innovators Ltd., and Alco Company paid interim dividends of Rs. 2 and Re. 1 per share respectively on all shares in issue at that date. On June 30, 2013, Elite Engineering also paid dividend of Rs. 1.5 per share as final dividend.

(vi) On July 1, 2012, Elite Engineering recognized development expenditure of Rs. 2.50 million as intangible assets. This is being amortized over its useful life of four years. However, on further investigation, it was discovered that only Rs. 1.50 million of the development expenditure should have been capitalized at July 1, 2012. The remaining balance does not meet the capitalization criteria of IAS-38, Intangible Assets. The useful life was reassessed and this was confirmed as being correct as at the date of capitalization. All research and development costs are presented in marketing and distribution cost.

(vii) It is company policy to value non-controlling interest using the proportionate share of the subsidiary's identifiable net assets. All items in the above statement of profit or loss are deemed to accrue evenly over the year.

Required:

(a) Calculate Goodwill. **(08)**

(b) Prepare Consolidated Statement of Profit or Loss of Innovators Group for the year ended June 30, 2013. **(27)**

ICMAP 501 – Extra Attempt 2014 – Q1 (a, b)

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ANSWER TO QUESTION 26: BASIC CONSOLIDATION

Part (a)

W1 GROUP STRUCTURE

Elite	Subsidiary	Acquisition: 01.07.2011	Group = 80%	NCI 20%
Alco	Subsidiary	Acquisition: 01.01.2013	Group = 60%	NCI 40%

W2 NET ASSETS (of subsidiaries) AT ACQUISITION	**Elite**	**Alco**
		Rs. 000
Equity share capital	100,000	80,000
Share premium	25,000	5,000
Retained Earnings [40,000] ; [12,000 + 5,450 x 6/12]	40,000	14,725
J1	20,000	10,000
	185,000	**109,725**

W3 GOODWILL	**Elite**	**Alco**
Investment [8,000 x Rs. 25] ; [8,000 x 60% x (12.5 + (2.8 x 1.12^{-1}))]	200,000	72,000
Less: [185,000 **W2** x 80%] ; [109,725 **W2** x 60%]	(148,000)	(65,835)
	52,000	**6,165**

Part (b)

Innovator Group
Consolidated Statement of Profit or loss
For the year ended 30 June 2013

	Innovator	**Elite**	**Alco 6/12**	**Adj.**	**Rs. 000**
Revenue	225,000	105,300	36,000	(7,000 **J3**)	359,300
Cost of sales	(141,000)	(68,850 + 1000 **J2** + 1,000 **J4**)	(27,000 + 500 **J2** + 250 **J4**)	(-7,000 **J3**)	(232,600)
Gross profit					126,700
M&D expenses	(11,100)	(4,050 + 750 **J6**)	(1,575)		(17,475)
Admin expenses	(18,750)	(8,100)	(2,925)		(29,775)
Other income	15,000	1,000	250	(12,000 **J5**)	4,250
Finance cost	(3,000)	(1,215)	(225)		(4,440)
Profit before tax					79,260
Taxation	(15,600)	(4,860)	(1,800)		(22,260)
Profit after tax		16,475	1,975		57,000
NCI [16,475 x 20%] + [1,975 x 40%]					(4,085)
Profit attributable to parent					52,915

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(i)	**1**	PPE	30,000	
		RE (Elite) Pre		20,000
		RE (Alco) Pre		10,000
Fair value adjustment				

(i)	**2**	RE / COS (Elite) 20,000 / 20 years	1,000	
		RE / LY (Elite) 20,000 / 20 years	1,000	
		RE / COS (Alco) 10,000 / 10 years x 6/12	500	
		PPE		2,500
Extra depreciation on fair value adjustment				

(iii-iv)	**3**	Revenue (Adj)	7,000	
		COS (Adj)		7,000
Inter-company transactions 4500 + 2,500 = 7,000				

(iii -iv)	**4**	RE / COS (Elite)	1,000	
		RE / COS (Alco) 2,500 x 50% x 20%	250	
		Inventories		1,250
Unrealised profit in inventory				

(v)	**5**	Dividend income (Adj)	12,000	
		Dividend paid (Elico) Adj		12,000
10,000 x Rs. 1.5 x 80% = 12,000				

(-)	**6**	RE / Marketing and distribution cost (Elite)	750	
		Development asset		750
Development asset at Rs. 2,500 – 625 = Rs. 1,875 Development asset should be Rs. 1,500 – 375 = Rs. 1,125 Difference Rs. 750				

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