QUESTION 48: ADVANCED CONSOLIDATION

The following draft group financial statements relate to Angel, a public limited company:

Angel Group: Statement of financial position as at 30 November 2013

	30 November 2013 $m	30 November 2012 $m
Assets		
Non-current assets		
Property, plant and equipment	475	465
Goodwill	105	120
Other intangible assets	150	240
Investment in associate	80	–
Financial assets	215	180
	1,025	1,005
Current assets		
Inventories	155	190
Trade receivables	125	180
Cash and cash equivalents	465	355
	745	725
Total assets	1,770	1,730
Equity and liabilities		
Share capital	850	625
Retained earnings	456	359
Other components of equity	29	20
	1,335	1,004
Non-controlling interest	90	65
Total equity	1,425	1,069
Non-current liabilities		
Long-term borrowings	26	57
Deferred tax	35	31
Retirement benefit liability	80	74
Total non-current liabilities	141	162
Current liabilities		
Trade payables	155	361
Current tax payable	49	138
Total current liabilities	204	499
Total liabilities	345	661
Total equity and liabilities	1,770	1,730

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Angel Group: Statement of profit or loss and other comprehensive income for the year ended 30 November 2013

	$m
Revenue	1,238
Cost of sales	(986)
Gross profit	252
Other income	30
Administrative expenses	(45)
Other expenses	(50)
Operating profit	187
Finance costs	(11)
Share of profit of equity accounted investees (net of tax)	12
Profit before tax	188
Income tax expense	(46)
Profit for the year	142
Profit attributable to:	
Owners of parent	111
Non-controlling interest	31
	142
Other comprehensive income:	
Items that will not be reclassified to profit or loss	
Revaluation of property, plant and equipment	8
Actuarial losses on defined benefit plan	(4)
Tax relating to items not reclassified	(2)
Total items that will not be reclassified to profit or loss	2
Items that may be reclassified to profit or loss	
Financial assets	4
Tax relating to items that may be reclassified	(1)
Total items that may be reclassified subsequently to profit or loss	3
Other comprehensive income (net of tax) for the year	5
Total comprehensive income for year	147
Total comprehensive income attributable to:	
	$m
Owners of the parent	116
Non-controlling interest	31
	147

Angel Group: Statement of changes in equity for the year ended 30 November 2013

	Share capital	Retained earnings	Other components of equity – financial assets reserve	Other components of equity – revaluation reserve	Total	Non-controlling interest	Total
	$m	$m	$m	$m	$m	$m	$m
Balance 1 Dec 2012	625	359	15	5	1,004	65	1,069
Share capital issued	225				225		225
Dividends for the year		(10)			(10)	(6)	(16)
Total comprehensive income for the year		107	3	6	116	31	147
Balance 30 Nov 2013	850	456	18	11	1,335	90	1,425

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The following information relates to the financial statements of the Angel Group:

(i) Angel decided to renovate a building which had a zero book value at 1 December 2012. As a result, $3 million was spent during the year on its renovation. On 30 November 2013, Angel received a cash grant of $2 million from the government to cover some of the refurbishment cost and the creation of new jobs which had resulted from the use of the building. The grant related equally to both job creation and renovation. The only elements recorded in the financial statements were a charge to revenue for the refurbishment of the building and the receipt of the cash grant, which has been credited to additions of property, plant and equipment (PPE). The building was revalued at 30 November 2013 at $7 million. Angel treats grant income on capital-based projects as deferred income.

(ii) On 1 December 2012, Angel acquired all of the share capital of Sweety for $30 million. The book values and fair values of the identifiable assets and liabilities of Sweety at the date of acquisition are set out below, together with their tax base. Goodwill arising on acquisition is not deductible for tax purposes. There were no other acquisitions in the period. The tax rate is 30%. The fair values in the table below have been reflected in the year-end balances of the Angel Group.

	Carrying values	Tax base	Fair values (excluding deferred taxation)
	$million	$million	$million
Property, plant and equipment	12	10	14
Inventory	5	4	6
Trade receivables	3	3	3
Cash and cash equivalents	2	2	2
Total assets	22	19	25
Trade payables	(4)	(4)	(4)
Retirement benefit obligations	(1)		(1)
Deferred tax liability	(0·6)		
Net assets at acquisition	16·4	15	20

(iii) The retirement benefit is classified as a long-term borrowing in the statement of financial position and comprises the following:

	$m
Net obligation at 1 December 2012	74
Net interest cost	3
Current service cost	8
Contributions to scheme	(9)
Remeasurements – actuarial losses	4
Net obligation at 30 November 2013	80

The benefits paid in the period by the trustees of the scheme were $6 million. Angel had included the obligation assumed on the purchase of Sweety in current service cost above, although the charge to administrative expenses was correct in the statement of profit and loss and other comprehensive income. There were no tax implications regarding the retirement benefit obligation. The defined benefit cost is included in administrative expenses.

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(iv) The property, plant and equipment (PPE) comprises the following:

	$m
Carrying value at 1 December 2012	465
Additions at cost including assets acquired on the purchase of subsidiary	80
Gains on property revaluation	8
Disposals	(49)
Depreciation	(29)
Carrying value at 30 November 2013	475

Angel has constructed a machine which is a qualifying asset under IAS 23 *Borrowing Costs* and has paid construction costs of $4 million. This amount has been charged to other expenses. Angel Group paid $11 million in interest in the year, which includes $1 million of interest which Angel wishes to capitalise under IAS 23. There was no deferred tax implication regarding this transaction.
The disposal proceeds were $63 million. The gain on disposal is included in administrative expenses.

(v) Angel purchased a 30% interest in an associate for cash on 1 December 2012. The net assets of the associate at the date of acquisition were $280 million. The associate made a profit after tax of $40 million and paid a dividend of $10 million out of these profits in the year ended 30 November 2013.

(vi) An impairment test carried out at 30 November 2013 showed that goodwill and other intangible assets were impaired. The impairment of goodwill relates to 100% owned subsidiaries.

(vii) The following schedule relates to the financial assets owned by Angel:

	$m
Balance 1 December 2012	180
Less sales of financial assets at carrying value	(26)
Add purchases of financial assets	57
Add gain on revaluation of financial assets	4
Balance at 30 November 2013	215

The sale proceeds of the financial assets were $40 million. Profit on the sale of the financial assets is included in 'other income' in the financial statements.

(viii) The finance costs were all paid in cash in the period.

Required:
Prepare a consolidated statement of cash flows using the indirect method for the Angel Group plc for the year ended 30 November 2013 in accordance with the requirements of IAS 7 *Statement of Cash Flows*.
Note: The notes to the statement of cash flows are not required. **(35 marks)**

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ANSWER TO QUESTION 48: ADVANCED CONSOLIDATION

Angel Group
Statement of cash flows for the year ended 30 November 2013

	$m
Cash flows from operating activities	
Profit for the year (W1)	197
Adjustments to operating activities	
Financial assets – profit on sale (W5)	(14)
Retirement benefit expense (W7)	10
Depreciation (W1)	29
Profit on sale of PPE (W1)	(14)
Associate's profit (W3)	(12)
Impairment of goodwill and intangible assets (26·5 + 90) (W6)	116·5
Finance costs	10
Operating profit before working capital changes	322·5
Decrease in trade receivables (180 – 125 + 3)	58
Decrease in inventories (190 – 155 + 6)	41
Decrease in trade payables (361 – 155 + 4)	(210)
Cash generated from operating activities	211·5
Cash paid to retirement benefit scheme (W7)	(9)
Interest paid	(10)
Income taxes paid (W4)	(135·5)
Net cash generated by operating activities	57
Cash flows from investing activities	
Sale of financial assets (W5)	40
Purchase of financial assets	(57)
Purchase of property, plant and equipment (PPE) (W1)	(76)
Cash grant for PPE (W1)	1
Purchase of subsidiary (30 – 2) (W2)	(28)
Proceeds from sale of PPE (W1)	63
Dividend received from associate (W3)	3
Purchase of associate (W3)	(71)
Net cash flows used by investing activities	(125)
Cash flows from financing activities	
Proceeds of issue of share capital	225
Repayment of long-term borrowings	(31)
Dividends paid	(10)
Non-controlling interest dividend	(6)
Net cash generated by financing activities	178
Net increase in cash and cash equivalents	110
Cash and cash equivalents at beginning of period	355
Cash and cash equivalents at end of period	465

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Workings

Working 1 Property, plant and equipment – building renovation

The following transactions would need to be made to recognise the asset in the entity's statement of financial position as of 30 November 2013.

Dr	Property, plant and equipment	$7m	
Cr	OCI		$4m
Cr	Retained earnings (to correct)		$3m

The accounting policy of the Angel Group is to treat capital-based grants as deferred income. However, the grant of $2m relates to capital expenditure and revenue. The grant should be split equally over revenue and capital.

The correcting entries should therefore be:

Dr	PPE	$2m	
Cr	Retained earnings		$1m
Cr	Deferred income (long-term liabilities)		$1m

Thus from a cash flow perspective, net profit before taxation should be adjusted by $3 million and additions to PPE increased by $3 million. Additionally, cash flows from investing activities should show the grant received of $1 million, net profit before taxation should increase by $1 million and additions to PPE increase by $2 million.

Current carrying amount of PPE before adjustments

	$m
Opening balance at 1 December 2012	465
Revaluation	8
Additions	66
Disposals	(49)
Subsidiary acquisition	14
Depreciation	(29)
Closing balance at 30 November 2013	475

Additions for the year are $66m above, plus the adjustments re the grant and building of $3 million and $2 million and the construction costs of $5 million, i.e. $76 million.

Thus profit before tax will be $188 million + $3 million + $1 million (grant) + $1 million capitalised interest + $4 million construction costs charged to other expenses, i.e. $197 million.

Working 2 Purchase of subsidiary

The purchase of the subsidiary is adjusted for in the statement of cash flows by eliminating the assets and liabilities acquired, as they were not included in the opening balances. The fair values will be used, as they will be the values utilised on acquisition.

Calculation of deferred tax arising on acquisition:

	$m
Fair values of Sweety's identifiable net assets excluding deferred tax	20
Less tax base	(15)
Temporary difference arising on acquisition	5
Net deferred tax liability arising on acquisition (30% x $5m)	1·5

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Calculation of goodwill:

	$m
Purchase consideration	30
Fair value of net assets (net of deferred tax)	(20)
Deferred taxation	1·5
Goodwill arising on acquisition	11·5

Working 3 Associate

	$m
Balance at 30 November 2013	80
Less profit for period $40m x 30%	(12)
Add dividend received $10m x 30%	3
Cost of acquisition (cash)	71

Therefore, cash paid for the investment is $71 million, and cash received from the dividend is $3 million.

Working 4 Taxation

	$m	$m
Opening tax balances at 1 December 2012		
Deferred tax	31	
Current tax	138	
		169
Charge for year		46
Deferred tax on acquisition (W2)		1·5
Tax on revaluation PPE		2
Tax on financial assets		1
Less closing tax balances at 30 November 2013:		
Deferred tax	35	
Current tax	49	
		(84)
Cash paid		135·5

Working 5 Financial assets

The sale proceeds of the financial assets were $40 million. Thus, an adjustment for the profit of $14 million on the sale of the financial assets has to be made. The deferred tax of $1 million arose on the gain on revaluation.

Working 6 Goodwill

	$m
Opening balance at 1 December 2012	120
Current year amount on subsidiary (W2)	11·5
Impairment	(26·5)
Closing balance at 30 November 2013	105

Impairments of other intangibles ($240m – 150m) $90m + $26·5m = $116·5m

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Working 7 Retirement benefit

	$m
Opening balance at 1 December 2012	74
Re-measurement – actuarial losses	4
Current year service cost plus interest	11
Contributions paid	(9)
Closing balance at 30 November 2013	80

An adjustment has to be made in the statement of cash flow for the current year amount ($11 million) and the purchase of the subsidiary ($1 million), giving a net adjustment of $10 million.

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