ASSIGNMENT – 4

Q-1

The statement of financial position of Sea and its subsidiaries River and Stream as at 31 March 20X0 – the accounting reference date for all three entities – are given below:

	Sea		River		Stream	
	Rs.000	**Rs.000**	**Rs.000**	**Rs.000**	**Rs.000**	**Rs.000**
Non-current assets						
Intangible assets						5,000
Tangible assets		41,000		30,000		20,000
Investments		17,000				
		58,000		30,000		25,000
Current assets						
Inventories	8,000		6,000		4,000	
Receivables	7,000		5,250		3,500	
Cash	2,000		500		300	
		17,000		11,750		7,800
		75,000		41,750		32,800
Capital and reserves						
Issued capital (Rs.1 shares)		20,000		17,000		12,000
Share premium account		15,000				1,500
Accumulated profits		11,600		18,450		5,948
		46,600		35,450		19,448
Long-term loans		20,000				8,052
Current liabilities						
Trade payables	5,200		4,000		2,700	
Income tax	3,200		2,300		1,600	
Provision	-		-		1,000	
		8,400		6,300		5,300
		75,000		41,750		32,800

Notes:

1. Sea subscribed for 100 per cent of the issued capital of River on the date of its incorporation. No changes have been place to the issued share capital of River since that date.
2. River supplies a component that is used by Sea in its manufacturing process. River applies a 20 per cent mark-up to the cost of manufacture of the component to arrive at the selling price to Sea. At 31 March 20X0 the inventories of Sea included Rs.600,000 in respect of components purchased from River.
3. Intra-group trading is meant to cease on 25 March each year to enable agreement of intra-group balances at the year-end. On 24 March 20X0 Sea made a payment of Rs.200,000 to River in respect of components purchased in February 20X0. This payment cleared the balance due for purchase up to February 20X0. Purchases of the component from 1 March to 24 March 20X0 by Sea amounted to Rs.180,000. This amount was included in the payables of Sea and the receivables of River at 31 March 20X0. On 30 March 20X0, contrary to normal practice, River dispatched goods having an invoiced price of Rs.150,000

and entered the transaction in its books. The transaction was not recorded by Sea in its statement of financial position that is given above.

4. Apart from any dividend transfers and the purchase of components by Sea from River there are no other inter-company transactions. There was no dividends payable at the year-end.

5. Following protracted negotiations the directors of Sea plc concluded an agreement whereby Sea acquired 9 million Rs.1 shares in Stream on 31 March 20X0. The terms of the acquisition were that Sea would issue two new Rs.1 shares for every three shares acquired in Stream. On 31 March 20X0 the market value of a Rs.1 share of Sea was Rs.3. The share issue by Sea on 31 March 20X0 is not reflected in the statement of financial position of Sea that appears above.

6. The intangible non-current assets of Stream at 31 March 20X0 consist of the estimated value of a brand that is associated with the company. This estimate has been made by the directors and no reliable external estimate of the market value of the brand is available.

7. Relevant details of tangible non-current assets of Stream at 31 March 20X0 are:

Description	Statement of financial position carrying value	Market value	Depreciated replacement cost	Recoverable amount
	Rs.000	**Rs.000**	**Rs.000**	**Rs.000**
Property	10,000	12,000	Not given	13,500
Plant	10,000	Not given	11,000	14,000

8. Inventories of Stream at 31 March 20X0 comprise:
   - Obsolete inventory (statement of financial position value: Rs.500,000). This inventory has a net realizable value of Rs.300,000.
   - The balance of inventory (statement of financial position value: Rs.3,500,000). This inventory has a fair value of Rs.4,200,000. A reasonable profit allowance for the sale of the inventory would be Rs.400,000.

9. The long-term loan of Stream is a zero-coupon bond that was issued on 1 April 20W5 for net proceeds of Rs.5 million. It is redeemable on 31 March 20X5 for a single payment of Rs.12,969,000. If the bond had been issued on 31 March 20X0 then the effective finance cost would have been eight per cent.

10. The provision of Rs.1 million in the statement of financial position of Stream is against the reorganization costs expected to be incurred in integrating the company into the Sea group. These costs would not been necessary if Stream were to remain outside the group. Although the plan was agreed by the board of directors before 31 March 20X0, it was not made known to those affected by the plan until after 31 March 20X0.

11. The fair value of NCI is Rs. 4.5 million at the date of acquisition.

12. The deferred tax liability arising because of fair value adjustments of Stream at the date of acquisition is Rs. 2.5 million.

13. The applicable tax rate for the group is 30%.

14. No impairment of the goodwill on acquisition of Stream has taken place.

Requirement

a) Calculate the goodwill that arises on the acquisition of stream by Sea on 31 March 20X0. You should ensure that each component of the calculation is fully explained?

b) Prepare the consolidated statement of financial position of Sea as at 31 March 20X0?

Q-2

The statement of financial positions of George and its subsidiary entities Zippy and Bungle at 30 June 20X3 (Accounting date for all the three entities) are given below:

	George		Zippy		Bungle	
	Rs.000	**Rs.000**	**Rs.000**	**Rs.000**	**Rs.000**	**Rs.000**
Assets:						
Non-current assets						
Property, plant and equipment (Note-3)	45,000		25,000		18,000	
Franchise right					2,000	
Financial assets (Note 1 and 2)	20,000		Nil		1,000	
		65,000		25,000		21,000
Current assets:						
Inventories (Note 3 and 4)	18,000		12,000		10,000	
Trade and other receivables (Note 3 and 4)	15,000		10,000		9,000	
		33,000		22,000		19,000
Total assets		98,000		47,000		40,000
Equity and liabilities						
Capital and reserves:						
Issued ordinary share capital (Rs. 1 share)	25,000		15,000		10,000	
10% Rs.1 preferred shares	Nil		10,000		Nil	
Share premium account	10,000		Nil		4,000	
Other reserves	4,000		1,000		1,300	
Accumulated profits	20,000		7,000		8,000	
		59,000		33,000		23,300
Non-current liabilities						
Interest bearing borrowing (Note-3)	20,000		Nil		4,000	
Deferred tax (Note 5)	2,000		1,000		1,500	
		22,000		1,000		5,500
Current liabilities						
Trade payable (Note 4)	10,000		6,500		6,000	
Tax payable	2,000		1,500		1,000	
Proposed dividend (Note 5)	Nil		1,000		Nil	
Bank overdraft	5,000		4,000		3,000	
Provision (Note 3)	Nil		Nil		1,200	
		17,000		13,000		11,200
Total equity and liabilities		98,000		47,000		40,000

Notes to the statement of financial positions

1. On 1 July 20X0, the date of incorporation of Zippy, George subscribed for all the ordinary shares of Zippy at par. Then, on 1 July 20X2, when its balance of

accumulated profits was Rs.3 million, Zippy issued 10 million Rs.1 preferred shares at par. George sub-scribed for 50% of these shares.

2. On 30 June 20X3, George purchased 8 million Rs.1 shares in Bungle. The terms of the purchase consideration were as follows:

   2.1. On 30 June 20X3, George issued 3 Rs.1 ordinary shares for every 4 shares purchased in Bungle. The market value of the ordinary shares at 30 June 20X3 was Rs.4 per share.

   2.2. On 30 June 20X5, George will pay the former shareholders of Bungle Rs.1 in cash for every share in Bungle they have purchased. This payment is contingent on the cumulative profits after tax of Bungle for the 2 years ending 30 June 20X5 being at least Rs.3 million. The fair value of contingent consideration is Rs. 6.5 million on the date of acquisition.

   2.3. The franchise right was awarded by George three years ago for a period of fifteen years. The franchise right is renewable for another fifteen years. The fair value of franchise right is Rs. 4 millions; however, without considering the renewable period the fair value is only Rs. 2.3 million. The franchise right is un-favorable compared with market term by Rs. 0.5 million.

   2.4. No entries in respect of the purchase of shares in Bungle have been made in the statement of financial position of George.

3. Following the acquisition of Bungle, the directors of George carried out a fair value exercise as required by IFRS 3 – Business combinations. The following matters are relevant and all potential fair value adjustments are material:

   3.1. Property, plant and equipment comprise land and building and plant and machinery. At 30 June 20X3, the land and buildings had a carrying value of Rs.10 million and a market value of Rs.18 million. The plant and machinery had a carrying value Rs.8 million. All the plant and machinery was purchased on 30 June 20X0 and was being depreciated on a straight-line basis over 8 years. No reliable estimate was available of the current market value of the plant and machinery, but at 30 June 20X3, the plant would have cost Rs.22 million to replace with new plant.

   3.2. Bungle has classified the financial assets as available for sale but the group has the intention to sell in the short term as early as possible when the prices exceeds the threshold determined by George.

   3.3. The inventory at 30 June 20X3 comprised:

   - Finished goods, costing Rs. 4 million which could be sold for Rs.8.5 million. A reasonable profit allowance for the selling effort of the group would be Rs.3 million.
   - The work in process of Rs. 4 million which is 80% complete. The selling price if the goods have been finished is Rs. 6 million. The selling effort of the group would be Rs. 1.5 million.
   - Raw material, costing Rs. 2 million, the replacement cost of which is Rs. 3.5 million.

   3.4. Trade receivables for which a local factoring company has assured for 85% of the total amount after taking into account of any doubtful debts.

   3.5. The interest bearing borrowing of Bungle is repayable at par on 30 June 20X6. Interest at 10% per annum is payable annually in arrears and the payment due on 30 June 20X3 has already been made. The fair market interest rate is 7% for such borrowings considering the current credit rating.

   3.6. The other provision of Bungle comprise:

   - Rs.400,000 in respect of the closure of various retail orders to which the directors the bungle became committed prior to entering into acquisition negotiations with the directors of George.

- Rs.800,000 in respect of the estimated cost of interacting Bunghe into the George group. No detailed integration plans had been formulated by 30 June 20X3.
- The old shareholders of Bungle have assured that if the payment relating to restructuring committed by them exceeded Rs. 400,000, they will indemnify George by the said amount. The fair value of additional payment is Rs. 200,000.

3.7. The additional deferred tax that needs to be provided on the adjustments that are necessary as a result of the fair value exercise is a liability of Rs.3 million.

4. George supplies a component to Zippy at cost plus a mark up of 20%. At 30 June 20X3, the inventories of Zippy included Rs.1.5 million in respect of this component. At 30 June 20X3, the receivables of George showed an amount receivable from Zippy of Rs.1.2 million, while the trade payables of Zippy showed an amount payable to George of Rs.600,000. One 29 June, George sent a consignment of component to Zippy at an invoiced price of Rs.600,000. The consignment was received and recorded by Zippy on 2 July 20X3.
5. The applicable tax rate for the group is 30%.
6. On 15 July 20X3 Zippy paid its preferred share dividend for the year ended 30 June 20X3, George made no entries in its financial statements in respect of this dividend until its was received in cash.

Requirements

a) Compute the goodwill on consolidation of Bungle what will be shown in the consolidated statement of financial position of George at 30 June 20X3. Provided justification for your figures where you consider this is needed?

b) Prepare the consolidated statement of financial position of George at 30 June 20X4?

Q-3

The statements of financial position of FAST and SHARP at 31 December 2009 are as follows:

Statements of financial position as at 31 December 2009

	FAST	**SHARP**
Assets	**Rs. (000)**	**Rs. (000)**
Non-current assets		
Property, plant and equipment	12,222	3,410
Investment in SHARP		
In equity	3,760	
In loan notes	600	
	16,582	3,410
Current assets		
Inventory	6,682	2,020
Trade receivables	5,586	852
Cash	273	58
	12,541	2,930
Total assets	29,123	6,340
Equity and liabilities		
Ordinary share capital	8,000	1,000
Share premium	2,500	400
Retained earnings	8,802	2,760
	19,302	4,160
Non-current liabilities		
10% loan notes		1,000
Current liabilities		
Accounts payable	8,987	980
Accrued interest	-	100

Declared dividends	834	100
	9,821	1,180
Total equity and liabilities	29,123	6,340

1. FAST Ltd acquired 80,000 shares having Par value Rs. 10 each, in SHARP Ltd on 31 December 2004 at a cost of Rs. 3,760,000. The cost of investment includes Rs. 200,000 paid by FAST as commission to a broker for finalizing the deal with the old shareholders of SHARP Ltd. FAST Ltd. has also agreed to pay Rs. 10 per share if the average EPS of the company over five years has remained more than Rs. 5 per share. The discount rate Fast Ltd use for PV calculations is 10%. The contingent consideration has not become payable as the average EPS is below Rs. 5. Fast Ltd has not recorded the contingent consideration in its books at all.
2. At 31 December 2004, the balance on the profit and loss account and share premium of SHARP Ltd was Rs.2, 000,000 and Rs. 400,000 respectively.
3. The fair value of the Property Plant & Equipment of SHARP Ltd at 31 December 2004 was considered to be Rs.500,000 greater than shown in SHARP' Books at that time. Depreciation is charged at 10% straight line. The fair value gain has not been reflected in the Books of SHARP Ltd.
4. Included in SHARP accounts payable is Rs. 100,000 owing to FAST. This amount does not agree with the accounts receivable from SHARP in the books of FAST as Rs. 20,000 charged as management fee by FAST not yet recorded by SHARP.
5. FAST has not accounted for either its interest or dividends receivable from SHARP.
6. Consolidated goodwill is subjected to an annual impairment review. No impairment has been detected to date.
7. It is group policy to value non-controlling interest at its fair value. The shares of SHARP were trading at Rs. 5 per share at the date of acquisition.

Required:

Prepare the consolidated statement of financial position for the FAST group on 31 December 2009?

Q-4

The statements of financial position of P and its subsidiary S at 31 December 2009 were as follows:

Statement of financial position at December 31, 2009

	P	**S**
	Rs.	**Rs.**
Total assets		
Non-current assets		
Property, plant and equipment	80,000	70,000
Intangible assets	--	30,000
Investment in shares of S	100,000	
	180,000	100,000
Net current assets	40,000	40,000
	220,000	140,000
Equity and liabilities		
Capital and reserves		
Ordinary shares of Rs. 10 each	120,000	100,000
Retained profits	100,000	40,000
	220,000	140,000

1. P purchased 80% of Rs. 10 shares of S on 1 January 2007 for Rs. 100,000 when the reserves of S showed a balance of Rs. 20,000.
2. S has all the same accounting policies as P, except as regards intangible assets and property, plant and equipment (PPE). The intangible assets of S are all of a type where recognition would not be permitted under IAS 38. When P made its

investments in S on 1 January 2007 the intangible assets of S included Rs. 15,000 that would not qualify for recognition under IAS 38.

3. The group has the policy of measuring PPE at Revalued amount less subsequent accumulated depreciation and impairment losses. The revalued amount of PPE of P at the date of acquisition and current reporting date are equal to carrying value. However, the revalued amount of PPE of S was Rs. 15,000 more than their carrying value of which Rs. 5,000 relate to date of acquisition. The revaluation will result in extra depreciation of Rs. 2,000 in the post acquisition period.
4. During December 2009 P sold some goods to S for Rs. 12,000. P operates with a gross profit margin of 25%. At the 31 December 2009 S still holds one -third of these goods in inventory.
5. The intra group balances are reconciled and the amount due to P in the books of S is Rs. 4,000.
6. The Group has the policy of measuring Non Controlling Interest (NCI) fair value at the date of acquisition, the fair value of NCI was Rs. 30,000.
7. Consolidated goodwill has been fully written off by the current reporting date.

Required:

Prepare the consolidated statement of financial position for the P group on 31 December 2009?