

CA - Corporate Level CONSOLIDATION GOODWILL

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B.Sc. (Acct.) Hons. Gold medal winner, ACA, SAT, ACMA (SL), CIMA Passed Finalist, CA Prize winner for AFR subject and CAB II First in Order of Merit, CIMA Strategic Level Aggregate Prize winner, Reading for MBA (PIM - USJP).

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LOLC Group acquires Serendib Hotels from Hemas for Rs.792mn

16 December 2020 09:32 am 0 - 663

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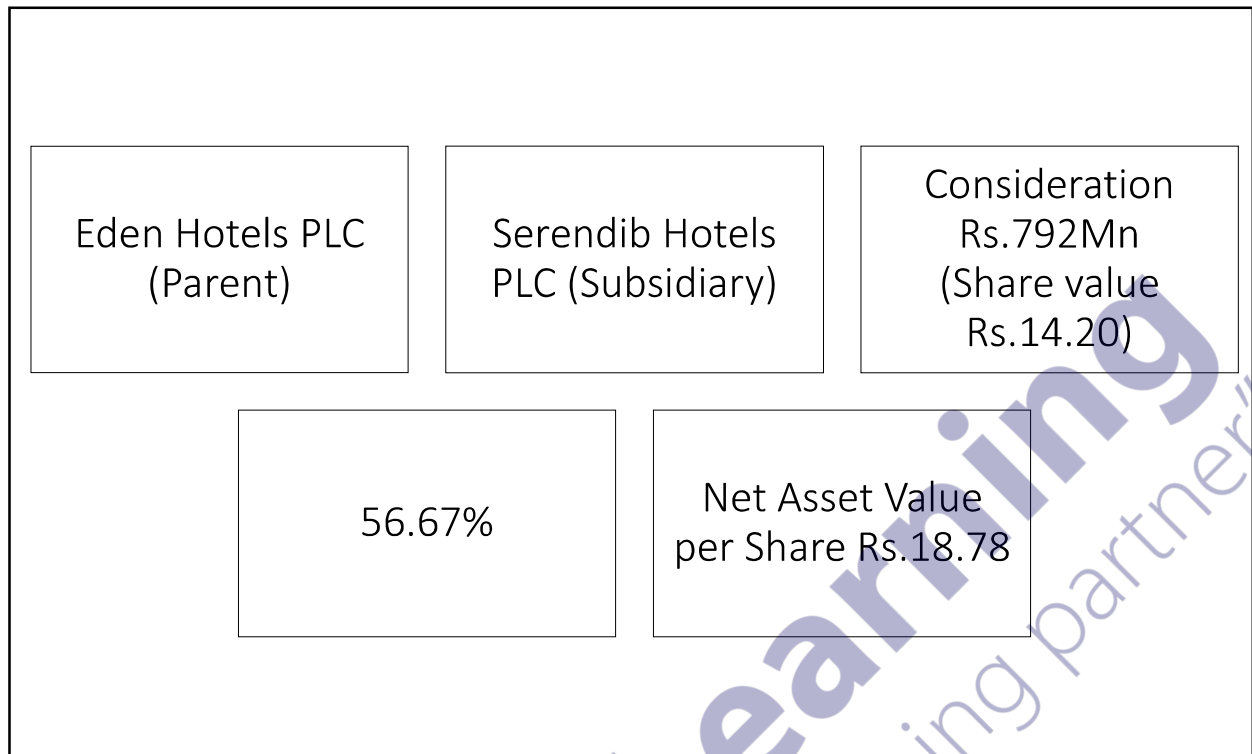
A A A

- LOLC says acquisition is aimed at capturing post-COVID growth in tourism business
- Hemas says divestment is part of group's portfolio direction and focuses on uplifting return on equity from core segments

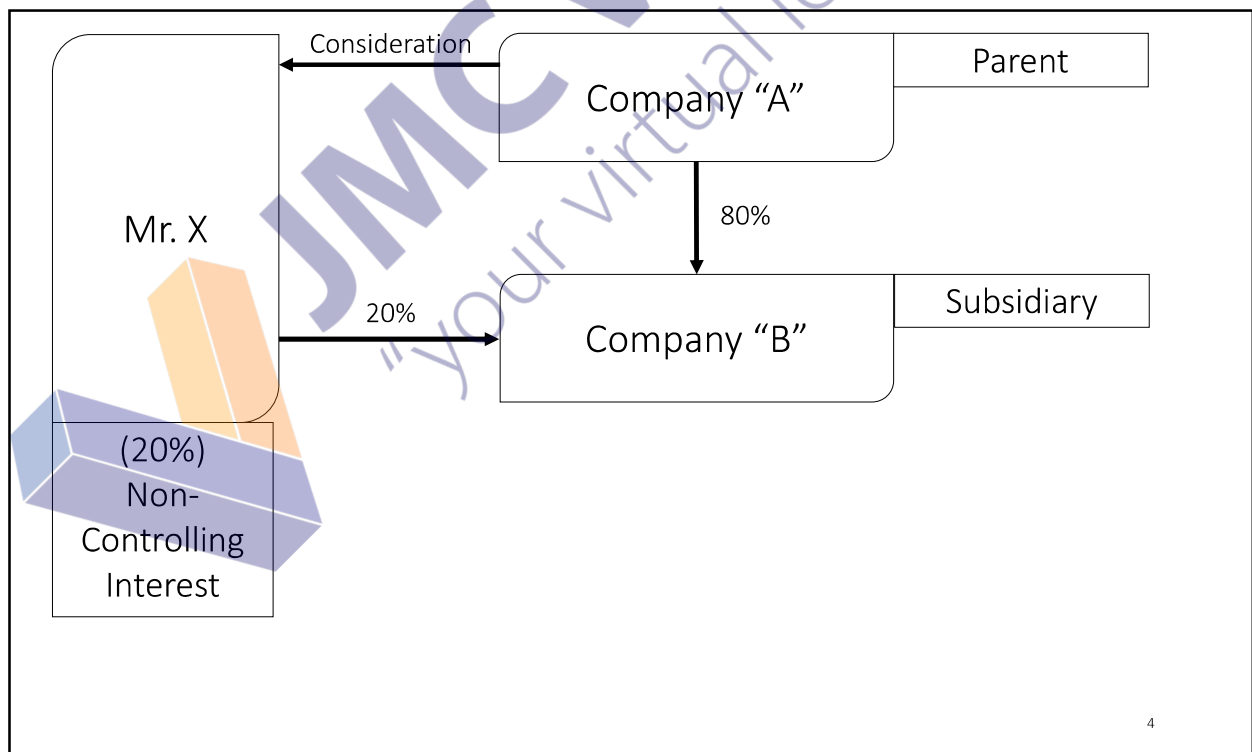
LOLC Holdings PLC's strategic investment arm, Browns Investments PLC (BI), yesterday acquired the controlling stake of 55.65 percent of Serendib Hotel PLC, a subsidiary of Hemas Group, for a consideration of Rs.792 million. With this acquisition, BI will hold 56.67 percent of voting shares and 53.48 percent of non-voting shares of Serendib.

<http://www.dailymirror.lk/business-news/LOLC-Group-acquires-Serendib-Hotels-from-Hemas-for-Rs-792mn/273-201923>

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HAYLEYS GROUP IN HISTORIC ACQUISITION OF SINGER (SRI LANKA) PLC FOR RS. 10.9 BILLION

September 15, 2017



Colombo, September 15, 2017:

Hayleys PLC and its subsidiaries are pleased to announce the purchase of 61.73% of shares of Singer (Sri Lanka) PLC, for a consideration of LKR 10.9 billion, making it the single largest acquisition for a listed company in Sri Lanka in recent times.

This strategic acquisition by Hayleys PLC and its subsidiaries is anticipated to yield substantial opportunities for new business synergies within the Hayleys Group. Both Hayleys PLC and Singer (Sri Lanka) PLC collectively account for over 280 years of

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Hayley's PLC
(Parent)

Singer PLC
(Subsidiary)

Consideration
Rs.10.9bn

61.73%

Goodwill
Rs.7.2Bn

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Understanding Goodwill Concept

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Example 01

Entity A has acquired 100% of Entity B for Rs.20/-. Following are the Statement of Financial Positions of Entity A and B

Description	Entity A	Entity B
Investment in A	20	0
Other Assets	180	100
Total Assets	200	100
Equity	100	20
Liabilities	100	80
Total Equity and Liabilities	200	100

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Investment Parent has Invested Rs.20	No Goodwill or Gain on Bargain Purchase	Entitlement Parent is Entitled for 100% of Net Assets Rs.20
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Description	Entity A	Entity B	Adj	Group A
Investment in A	20	0	-20	0
Other Assets	180	100	180+100	280
Total Assets	200	100		280
Equity	100	20	-20	100
Liabilities	100	80	100+80	180
Total Equity and Liabilities	200	100		280

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Example 02

Entity A has acquired 100% of Entity B for Rs.30/-.

Following are the Statement of Financial Positions of Entity A and B

Description	Entity A	Entity B
Investment in A	30	0
Other Assets	170	100
Total Assets	200	100
Equity	100	20
Liabilities	100	80
Total Equity and Liabilities	200	100

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Investment

- Parent has Invested Rs.30

Parent Paid
Rs.10/- Extra for Goodwill

Entitlement

- Parent is Entitled for 100% of Net Assets Rs.20

Description	Entity A	Entity B	Adj	Group A
Investment in A	30	-	-20-10	-
Goodwill			+10	10
Other Assets	170	100	170+100	270
Total Assets	200	100		280
Equity	100	20	-20	100
Liabilities	100	80	100+80	180
Total Equity and Liabilities	200	100		280

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Example 03

Entity A has acquired 100% of Entity B for Rs.10/-. Following are the Statement of Financial Positions of Entity A and B

Description	Entity A	Entity B
Investment in A	10	0
Other Assets	190	100
Total Assets	200	100
Equity	100	20
Liabilities	100	80
Total Equity and Liabilities	200	100

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Investment

- Parent has Invested Rs.10

Parent Acquired Subsidiary

at a Bargain Price.
Gain Received Rs.10/-

Entitlement

- Parent is Entitled for 100% of Net Assets Rs.20

Description	Entity A	Entity B	Adj	Group A
Investment in A	10	-	-20 +10	-
Other Assets	190	100	190+100	290
Total Assets	200	100		290
Equity	100	20	-20+10	110
Liabilities	100	80	100+80	180
Total Equity and Liabilities	200	100		290

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- Goodwill is the Additional Amount Invested by Owners to Acquire the Subsidiary
- It's an Intangible Asset in Consolidated Financials

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How to Calculate Goodwill?

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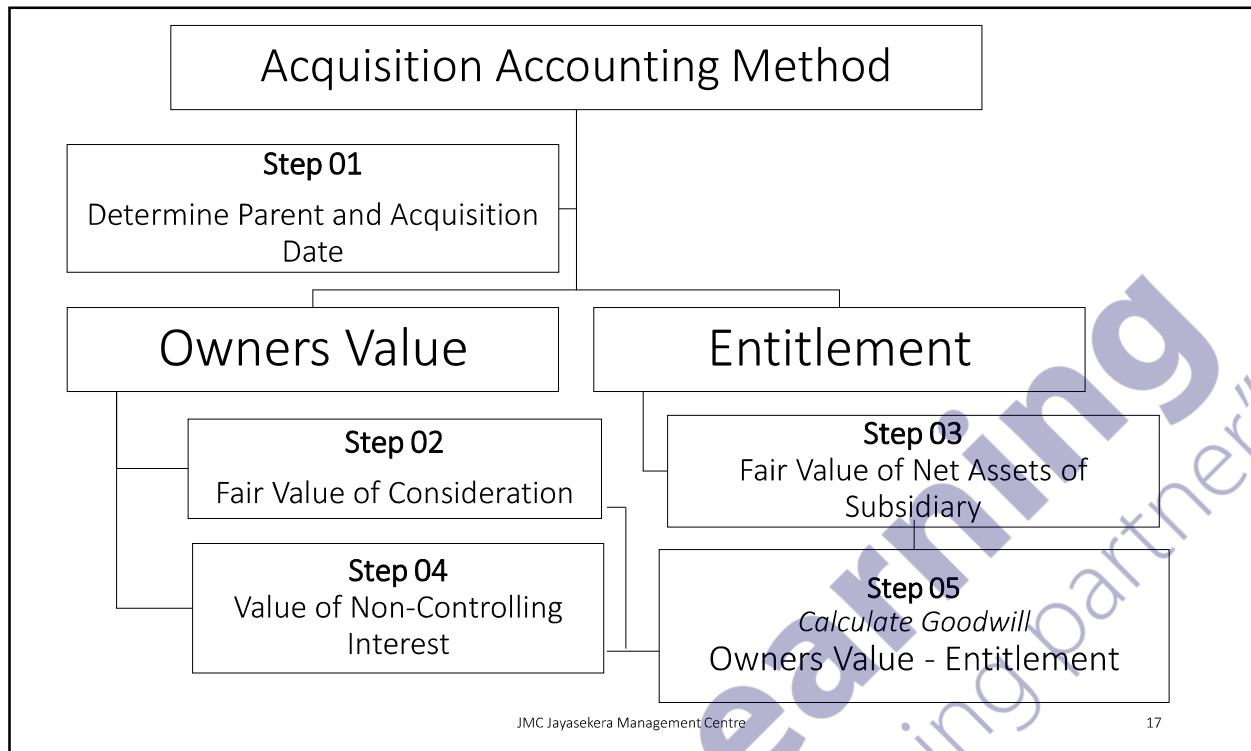
The acquisition method

4 An entity shall account for each business combination by applying the acquisition method.

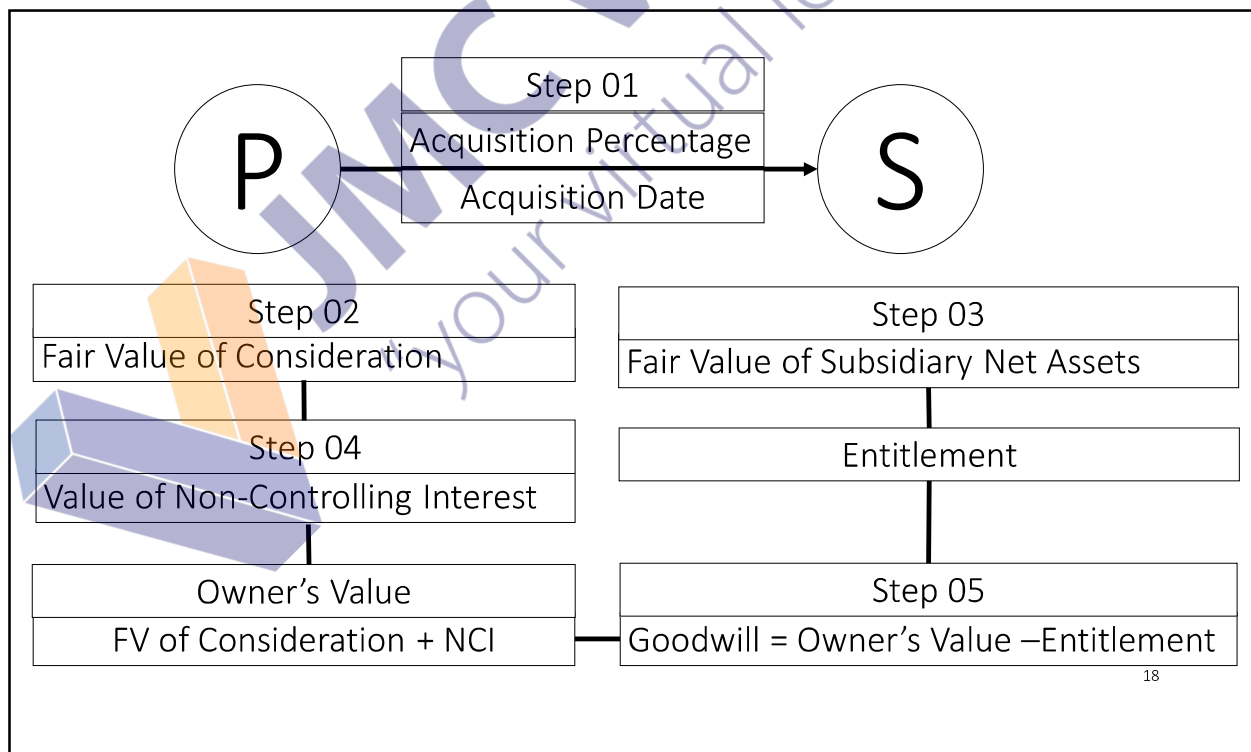
5 Applying the acquisition method requires:

- (a) identifying the acquirer;
- (b) determining the *acquisition date*;
- (c) recognising and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree; and
- (d) recognising and measuring goodwill or a gain from a bargain purchase.

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Fair Value of Consideration

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Consideration may include

Cash

- Fair Value = Face Value

Assets Transferred

- Fair Value = Market Value

Shares Issued

- Fair Value = Market Value

Deferred Consideration (Delayed consideration)

- Fair Value = Present Value

Contingent Consideration (Delayed + Condition)

- Fair Value = Probability Weighted Present Value

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Consideration Shall Exclude

Transaction Costs

- Lawyer Fees
- Broker Charges
- Documentation Charges

Provisions for Future Losses in Subsidiary

Subsequent Investments by Parent

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Question 01

- Anthony purchased 80% of Matheesha's 3,000 shares on 1 January 2020. The consideration included following items.
- Cash consideration paid of Rs 5,500,000/-.
- Land transferred to previous owners of Matheesha which had a market value of Rs. 2,700,000/- and a carrying value of Rs. 2,500,000/-.
- Shares issued of three shares for every four shares acquired of Matheesha. As at acquisition date market price per share of Anthony was Rs.1,000/- and Matheesha was Rs.1,500/-

1.1 Calculate the Fair Value of Share Issue

1.2 Calculate the Land Disposal Gain

1.3 Calculate the Fair Value of Consideration

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Question 02

- Imraz has invested in 80% of Jesmine's Rs.1,000,000 Rs.10 equity shares.
- Imraz paid Rs.500,000 as a cash consideration.
- Imraz issued 3 shares for every 5 shares acquired. At the date of acquisition, the market value of a Imraz share was Rs.25.
- Imraz agreed to pay Rs.3,630,000 cash 2 years after acquisition.
- Further Rs 1,331,000 cash will be paid 3 years after acquisition if Jesmine achieves a Rs.10Mn profit target at the third year. As of acquisition date the probability of achieving the profit target was assessed as 80%.
- Legal and professional fees incurred in relation to the acquisition were Rs.2,000. (Assume a discount rate of 10%)

2.1 Calculate the Fair Value of Shares Issued

2.2 Calculate the Present Value of Deferred Consideration

2.3 Calculate the Probability Weighted Present Value of Contingent Consideration

2.4 Calculate the Fair Value of Total Consideration

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Question 03

Ronan acquired 75% of Mohan on 01st January 2020 and paid Rs.150, 000/- as the cash consideration to the previous owner of Mohan.

Ronan also agreed to pay followings

Contingent Consideration

An additional amount equal to following year's profits that exceed Rs.30, 000/- Mohan historically has made profits of Rs.20, 000/- to Rs.30, 000/- each year and is forecasted to make a profit of Rs.42,777/-. Probability of occurrence 90%.

Assume 10% as the discount factor

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Question 03

Deferred consideration

- Rs.121,000/- to be paid after 2 years of acquisition
- Assume 10% as the discount factor

Asset transfer

- Ronan transferred a property to the previous owners of Mohan. The property had a market value of Rs. 300,000/-. However, the carrying value was Rs. 320,000/-.

Issue of parent company shares to previous owners

- Mohan had 100,000 shares in issue. Ronan has agreed to issue three shares for every five shares acquired of Mohan's to its previous owners as part of the settlement. Ronan's share trading price is Rs.7 and Mohan's share trading price is Rs.5

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Question 03

- 3.1 Calculate the probability weighted present value of contingent consideration
- 3.2 Calculate the finance cost of contingent consideration for year 2020
- 3.3 Calculate the present value of deferred consideration
- 3.4 Calculate the finance cost of deferred consideration for year 2020 and 2021
- 3.5 Calculate the fair value of shares issued
- 3.6 Calculate the property disposal loss
- 3.7 Calculate the value of total consideration

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Question 04

- Rachapaajitha acquired 80% of Gonja on 01/01/2020.
- Cash paid Rs 480,000
- Land having a carrying value of Rs. 1,000,000/- was transferred to previous owners of Gonja which had a market value of Rs. 1,200,000/- at the acquisition date.
- Rachapaajitha issued 100,000 shares to the shareholders of Gonja, each with a nominal value of Rs 1 and a market value of Rs 3.20.
- Cash of Rs 220,000 to be paid one year after the date of acquisition.
- Cash of Rs 2,200,000 may be paid one year after the date of acquisition, if Gonja achieves a Rs.10Mn profit target. It is thought that there is only a 40% chance that this will occur. The fair value of this consideration is to be measured at the present value of the expected value. (Discount Rate 10%)
- Legal fees associated with the acquisition amounted to Rs. 15,000.
- Rachapaajitha is expecting to restructure the business and a restructuring expenses is expected to be Rs. 200,000/-
- Gonja's call recording segment is expected to make losses in the first year after acquisition. The expected future loss is Rs. 50,000/-

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Question 04

- 4.1 Calculate fair value of share issue and determine the double entry
- 4.2 Calculate the present value of deferred consideration and determine the double entry
- 4.3 Calculate the probability weighted present value of contingent consideration and determine the double entry
- 4.4 Calculate the Land disposal gain and determine the double entry
- 4.5 Determine the double entry for Cash Consideration
- 4.6 Explain the accounting treatment for
 - 4.6.1 Legal fees
 - 4.6.2 Restructuring provision
 - 4.6.3 Future losses provision
- 4.7 Calculate the total fair value of consideration

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Question 04

4.8 Calculate the finance cost of deferred consideration for the year 2020 and determine the double entry

4.9 Calculate the finance cost of contingent consideration for year 2020 and determine the double entry

4.10 Explain the accounting treatment for subsequent changes in circumstance of a contingent consideration as to change in probability or achievement of target and non-achievement of target.

4.11 Provide the double entries in Rachapaajitha's books for

4.11.1 Settlement of deferred consideration liability as at 31/12/2020

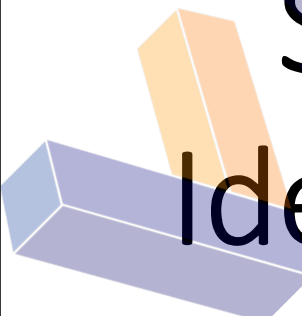
4.11.2 Settlement of contingent consideration liability as at 31/12/2020, if profit target is being achieved.

4.11.3 Writing back the contingent consideration liability as at 31/12/2020, if profit target is not being achieved.

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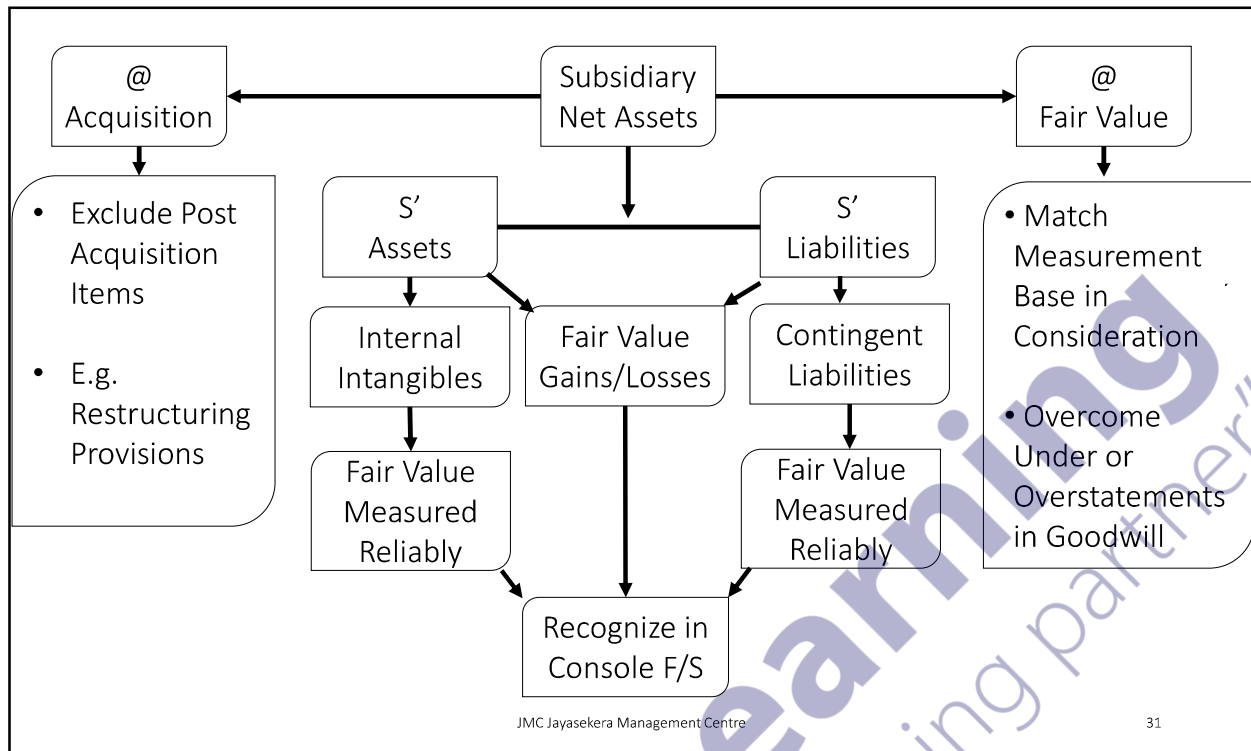
Fair Value of Subsidiary's Identifiable Net Assets



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Example – Why we need to take Fair Value of Subsidiary Net Assets!

P acquired 100% of S paying Rs.100 to previous owner. The Book Value of Net Assets at Acquisition was Rs.60. There was a fair value gain of Rs.20 on a Land.

Goodwill – Without Fair Value Gain Adjustment	
Investment	
(-) Net Assets	
Goodwill	

Goodwill – With Fair Value Gain Adjustment	
Investment	
(-) Net Assets	
Goodwill	

Goodwill will be overstated by Fair Value Gain Rs.20

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Example – Why we need to take Fair Value of Subsidiary Net Assets!

P acquired 100% of S paying Rs.100 to previous owner. The Book Value of Net Assets at Acquisition was Rs.60. There was a fair value loss of Rs.10 on a building.

Goodwill – Without Fair Value Loss Adjustment	
Investment	
(-) Net Assets	
Goodwill	

Goodwill – With Fair Value Loss Adjustment	
Investment	
(-) Net Assets	
Goodwill	

Goodwill will be understated by Fair Value Loss Rs.10

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Example – Why we need to adjust Internally generated Intangible Assets of Subsidiary!

P acquired 100% of S paying Rs.100 to previous owner. The Book Value of Net Assets at Acquisition was Rs.60. There was an unrecognized brand name worth of Rs.15

Goodwill – Without Intangible Asset Adjustment	
Investment	
(-) Net Assets	
Goodwill	

Goodwill – With Intangible Asset Adjustment	
Investment	
(-) Net Assets	
Goodwill	

Goodwill will be overstated by Intangible Asset Rs.15

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Example – Why we need to adjust Contingent Liabilities of Subsidiary!

P acquired 100% of S paying Rs.100 to previous owner. The Book Value of Net Assets at Acquisition was Rs.60. There was a pending court case against the Subsidiary of Rs.20.

Goodwill – Without Contingent Liability Adjustment	
Investment	
(-) Net Assets	
Goodwill	

Goodwill – With Contingent Liability Adjustment	
Investment	
(-) Net Assets	
Goodwill	

Goodwill will be understated by Contingent Liability Rs.20

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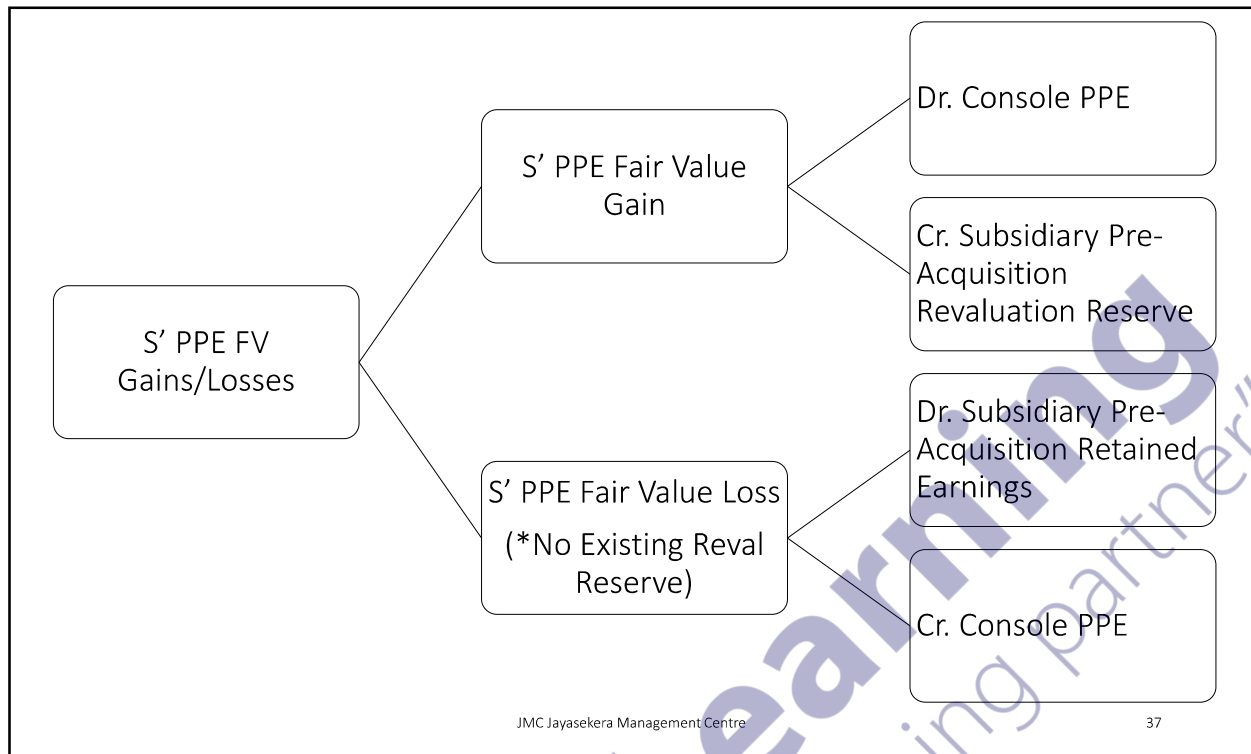
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Double Entries Relevant to Fair Value Adjustments

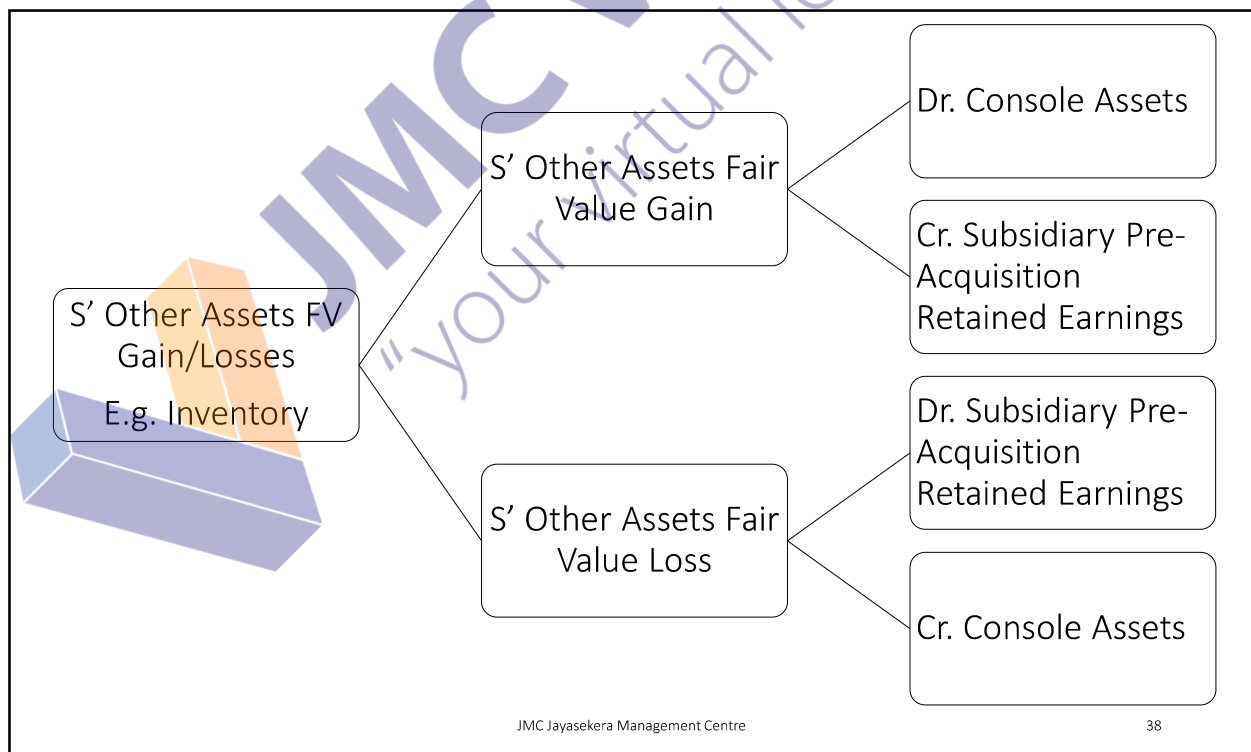
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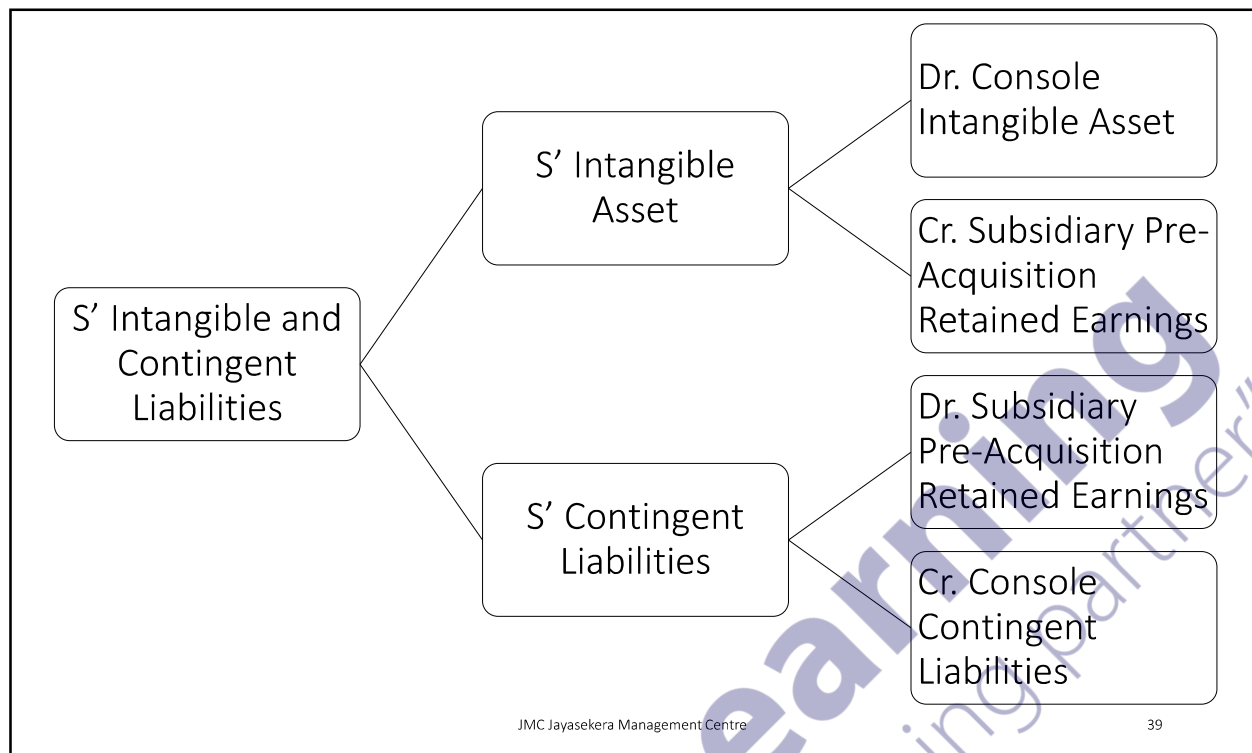
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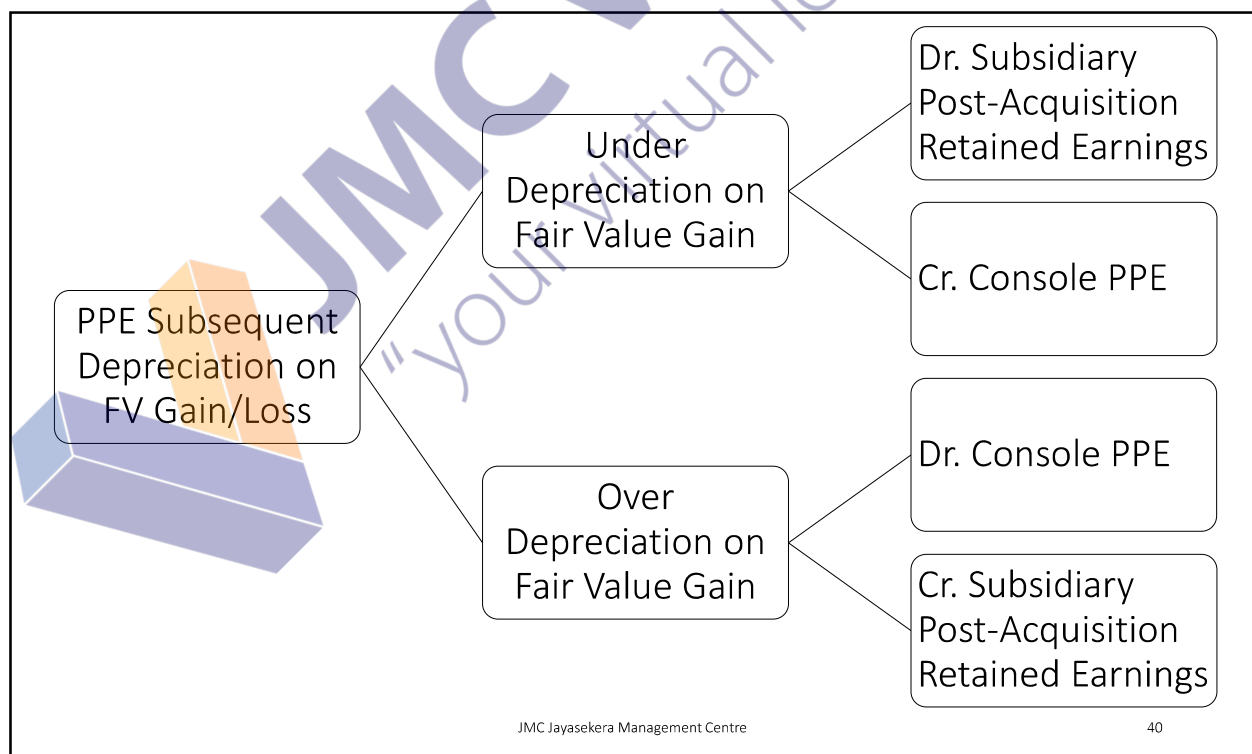
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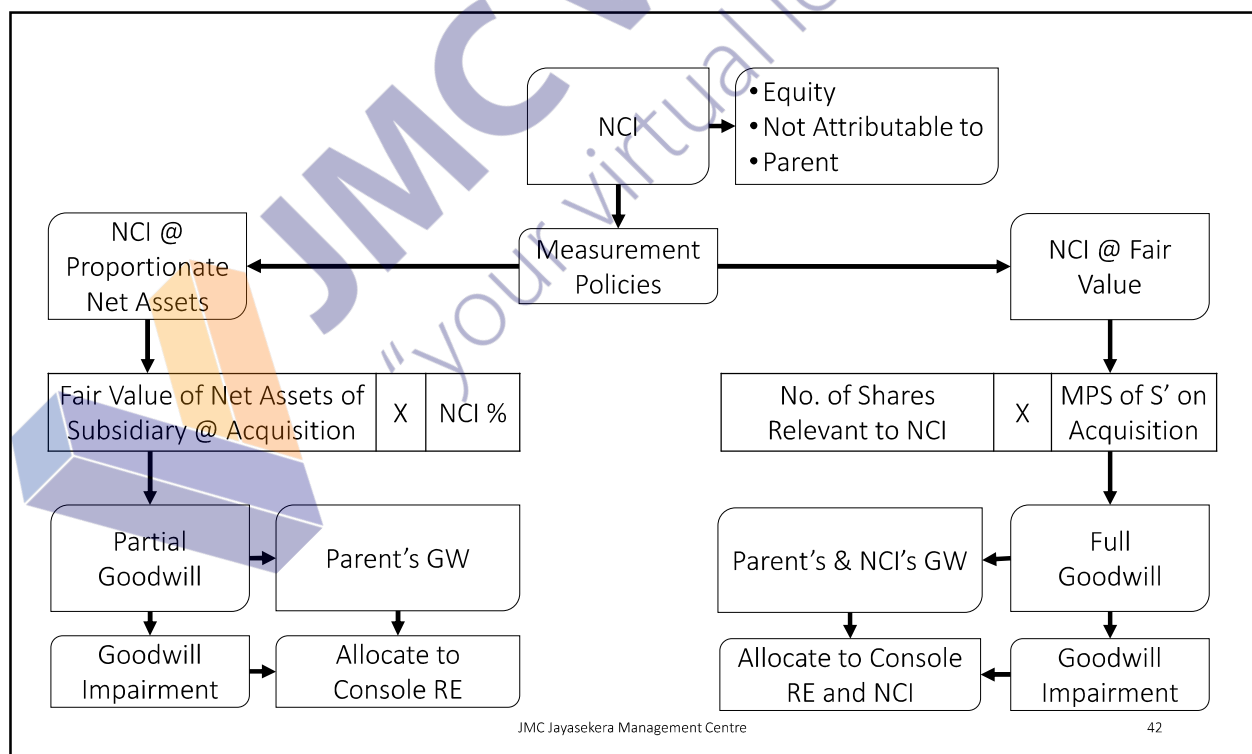
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Non-Controlling Interest

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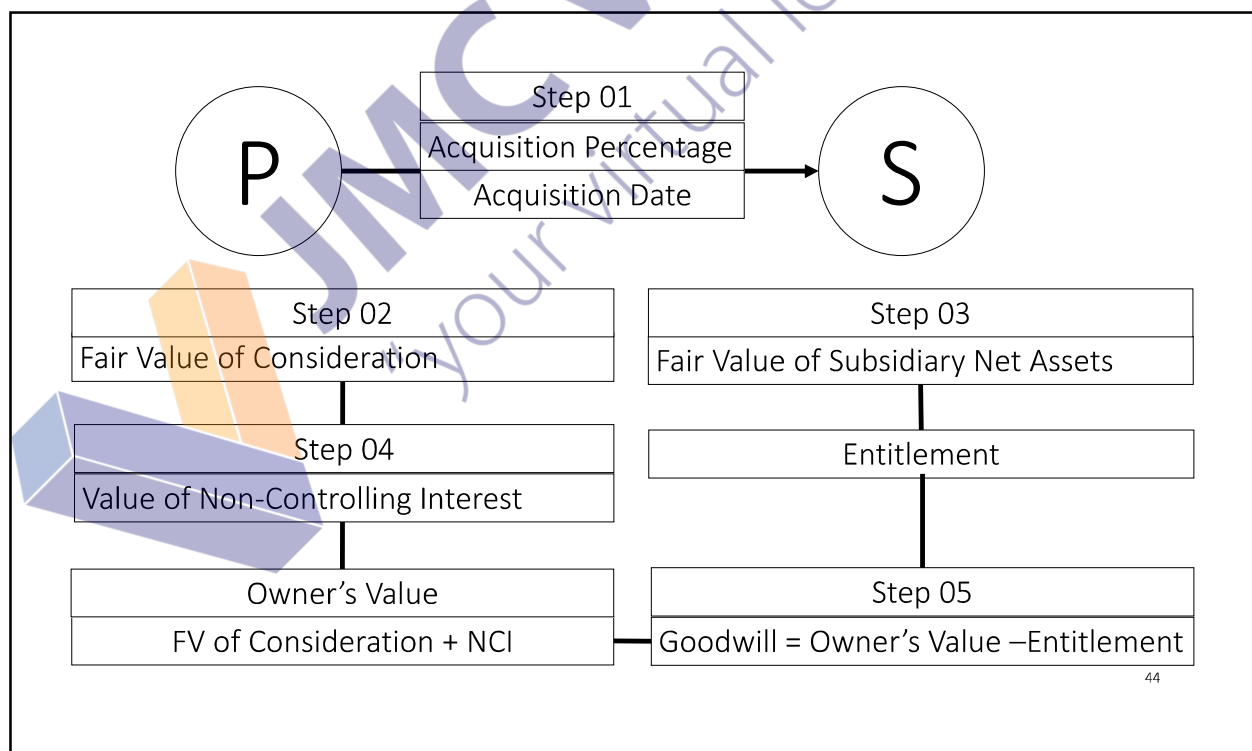
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GOODWILL

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Determinants of Goodwill

Staff Expertise

Customer Loyalty

Reputation

Locational Advantage

Quality of Service

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Question 05

Sameera purchased 60% of Kumar's 3,000, Rs.1/- shares on 1 January 2020. Sameera paid Rs 5,500 cash consideration. On 1 January 2020, the Fair value of Kumar's net assets was Rs 5,000. Kumar's share price at this date was Rs.2.25.

Calculate the total Goodwill and Goodwill relevant to parent and NCI separately valuing the NCI:

5.1 Using the proportionate net assets method

5.2 Using the fair value method

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Question 06

Suchin Ltd purchased 80% of share capital of Dolan on 1/1/20. On this date statement of financial position of Dolan was as follows

PPE	60,000
Trade Receivables	7,000
Cash	3,000
Total Assets	70,000
Stated Capital	20,000
Retained Earnings	20,000
Liabilities	30,000
Total Liabilities	70,000

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Question 06

- Suchin paid Rs.30, 000/- to Dolan's previous owners to acquire Dolan.
- Rs.2,000/- was incurred by Suchin as the legal charges.
- Suchin transferred the ownership of a Machine having a carrying value of Rs.40, 000/- and market value of Rs.46,000/- to the previous owners of Dolan.
- Further Suchin issued 4 shares in exchange of every 10 shares of Dolan. Market value of a Dolan share was Rs.9/- and market value of an Suchin share was Rs.6/-. Dolan has 10,000 shares in issue.
- Suchin also entered into an agreement with Dolan's previous owner to pay an additional Rs.24,200/- on 1/1/22, in relation to the acquisition. Discount rate applicable is 10%.
- Suchin agreed to pay further Rs.12,100/- on 1/1/22 if Dolan achieves a revenue target of Rs.300,000/-. It was assumed that there's a 50% probability is there to achieve the profit target.

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Question 06

Calculate

6.1 Fair Value of consideration

6.2 Calculate NCI measured at fair value

6.3 Calculate Goodwill if NCI measured at fair value

6.4 Calculate NCI measured at proportionate share of net assets

6.5 Calculate Goodwill if NCI measured using proportionate net assets

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Question 07

- Spain acquired 80% of the share capital of Madrid paying consideration of Rs 8 million. At acquisition, the statement of financial position of Madrid showed equity share capital of Rs 3 million (Rs.10 per share) and retained earnings of Rs 4.5 million.
- The market price per share of Madrid as at the acquisition date was Rs.30 per share.
- Following additional information provided regarding the net assets of the Madrid.
- Freehold land with a book value of Rs 400,000 but a market value of Rs 900,000
- Machinery with a book value of Rs 1.2 million. No reliable market value exists for these items. They would cost Rs 1.5 million to replace as new. The machinery has an expected life at 10 years and Madrid's machines are 4 years old.

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Question 07

- An equipment with a book value of Rs.1 million. The market value details were not available. However, the details obtained to assess the market value using income approach were as follows.
 - Remaining useful life was 05 years
 - Cash inflows expected per annum over the useful life Rs.800,000/-
 - Cash outflows expected per annum over the useful life Rs.500,000/-
 - Residual value expected at the end of useful life Rs.101,082/-
 - 10% discount rate assumed
- The fair value of all other assets and liabilities are approximately equal to book value.
- Madrid's brand name was internally generated and so is not recognized in their statement of financial position. However, valuation experts have estimated its fair value to be Rs 800,000. The brand name has a remaining useful life of 05 years.

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Question 07

- A Supplier of Madrid has filed a case against the company claiming a compensation of Rs.200,000/- for a returned cheque. This case was not finalized at the date of acquisition.
- The directors of Spain intend to close down one of the divisions of Madrid and wish to provide for operating losses up to the date of closure which is estimated at Rs 729,000.
- An investment in plant and machinery will be required to bring the remaining production line of Madrid up to date. This will amount to Rs 1,200,000 in the next 12 months.

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Question 07

Calculate

7.1 The fair value of net assets acquired of Subsidiary

7.2 Explain the Accounting Treatments for

- Subsidiary PPE fair value Gains/Losses at acquisition
- Subsidiary Internally Generated Intangible Assets
- Subsidiary Contingent Liabilities at Acquisition
- Subsidiary Future Operating Losses
- Future Investments to be Made in Subsidiary

7.3 Goodwill if NCI measured at fair value

7.4 Goodwill if NCI measured at proportionate net assets

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Question 08

Wellington purchased 80% of the equity share capital of Boot on 1 April 2019.

Consideration includes following items

- Cash paid Rs 500,000
- Machine which had a carrying value of Rs. 750,000/- was transferred to the previous owners of Boot The machine had a market value of Rs. 800,000/- as at the acquisition date.
- Wellington issued four shares for every three shares acquired to the shareholders of Boot. Wellington's market price per share as at acquisition date was Rs.8.75/-
- Cash of Rs 440,000 to be paid one year after the date of acquisition.

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Question 08

Consideration includes following items

- Cash of Rs 1,100,000 may be paid one year after the date of acquisition, if Boot achieves a revenue target of Rs.200Mn in the year 2019/20. It is thought that there is only 80% chance that this will occur. The fair value of this consideration is to be measured at the present value of the expected value. Financials prepared for the year ended 31/3/2020 of Boot reflects a revenue of Rs.210Mn.
- Legal fees associated with the acquisition amounted to Rs. 25,000.
- Assume a discount rate of 10%.

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Question 08

Fair value of Net Assets of the Subsidiary

- Boot's share capital is made up of Rs. 3,000,000 Rs 10 shares and it had retained earnings of Rs 1,000,000 at the date of acquisition.
- Boot's property plant and equipment which had a carrying value of Rs. 3,200,000/- The fair value of those assets were Rs. 4,000,000/- as at the date of acquisition. The property plant and equipment had a remaining useful life of 04 years.
- Boot had an internally generated brand name which had a market value of Rs.500, 000/-. The brand name had a useful life of 05 years.
- An employee filed a case against Boot claiming a compensation of Rs.300, 000/-. The case was not finalized as at the acquisition date.

Non-Controlling Interest

- The fair value of the NCI at 1 April 2019 was Rs 1,250,000.

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Question 08

- 8.1 Calculate the value of total consideration
 - 8.2 Determine the double entries in Parent Company's books for the consideration.
 - 8.3 Calculate the fair value of net assets of subsidiary at acquisition
 - 8.4 Calculate and Explain the depreciation on fair value gain in subsidiary property plant and equipment for the year 2019/20
 - 8.5 Calculate and Explain the amortization of intangible asset for the year 2019/20
- Calculate the goodwill
 - NCI at fair value method
 - NCI at proportion of net assets method
 - Determine the double entries in for Goodwill in Consolidated Books

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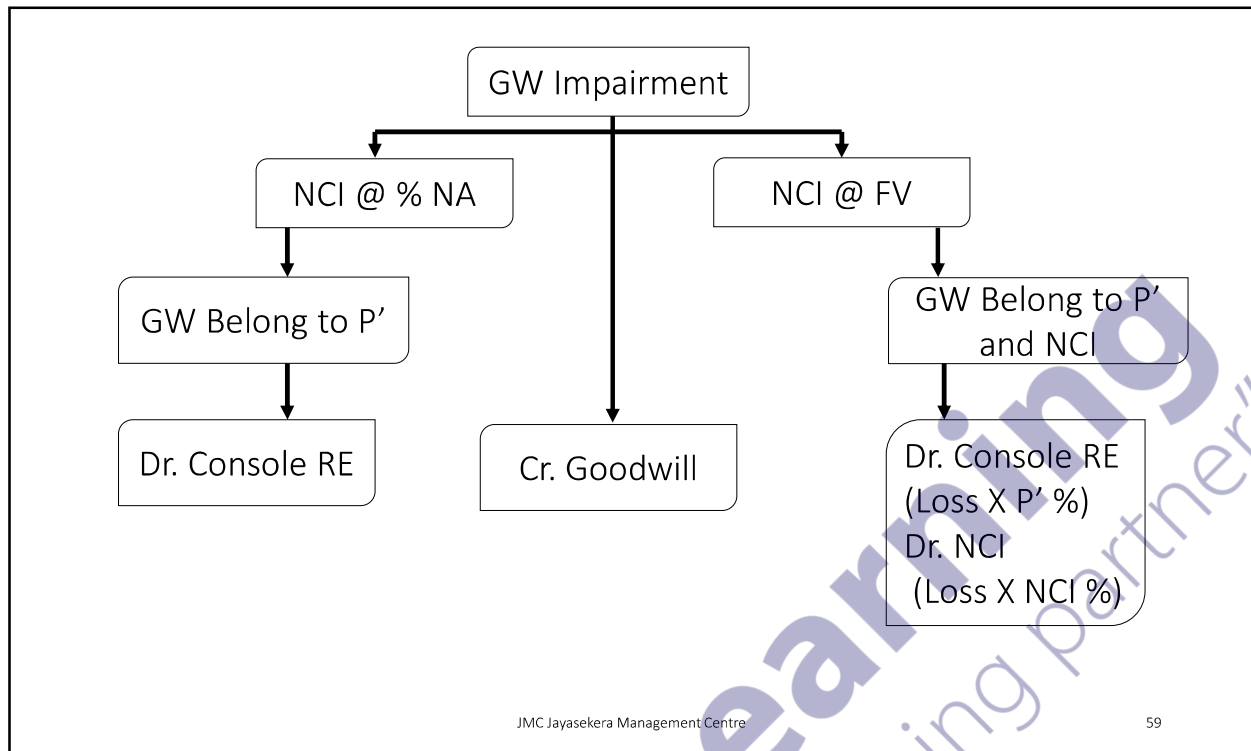
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IMPAIRMENT OF GOODWILL

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Question 09

- H purchased 80% of S's on 1 January 2020. S paid Rs 6,000 cash for their investment. At 1 January 2020, the value of S's net assets was Rs 6,200. S's share price at this date was Rs 3.75
- S had 2,000 shares in issue.

Calculate

The goodwill arising on the acquisition of S, valuing the NCI:

09.1 Using the fair value method

09.2 Using the proportion of net assets method

If Goodwill is impaired by 20%, provide the double entries if NCI valued using

09.3 Using the fair value method

09.4 Using the proportion of net assets method

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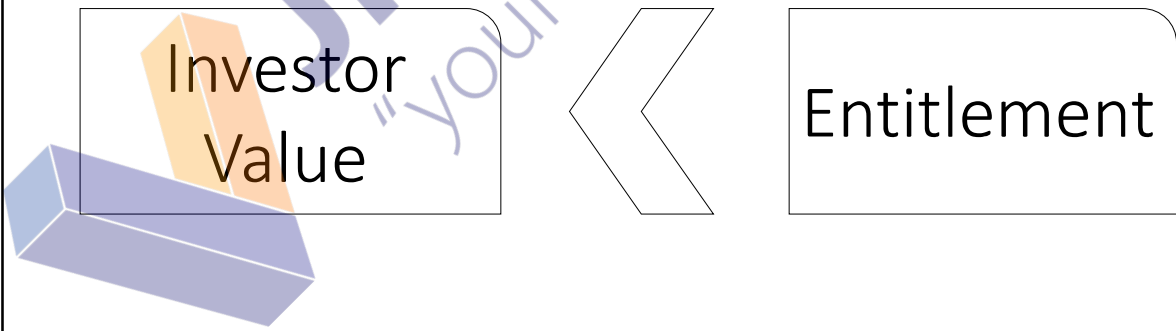
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GAIN ON BARGAIN PURCHASE

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Investor
Value

Entitlement

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Who is Entitled for Gain on Bargain Purchase? Parent or NCI?

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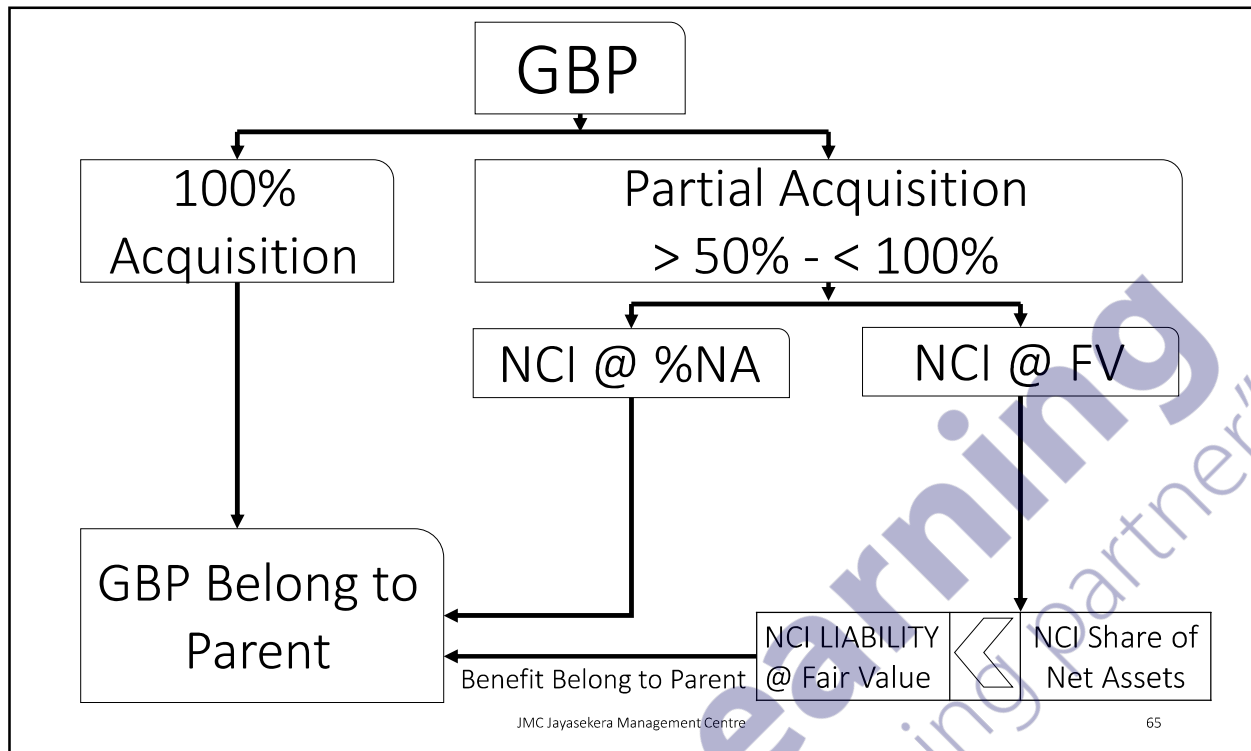
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	GW		
	P	NCI	Total
%	80%	20%	100%
Inv	400	100	500
Ent	320	80	400
GW	80	20	100

	GBP		
	P	NCI	Total
%	80%	20%	100%
Inv	240	60	300
Ent	320	80	400
GBP	80	20	100

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Question 10

- P Ltd purchased 70% of the share capital of S on 1/4/19 by paying Rs.250, 000/- in cash.
- P Agreed to pay an additional amount equal to 10% of the following year's profits if it exceeds Rs.500, 000/-. It's forecasted that S would make a profit of Rs.1, 100, 000/-. Discount rate applicable is 10%. A probability of occurrence of 100% assumed.
- P has given a Land to the previous owners of S as part of the settlement. The carrying value of the land is Rs.100, 000/- and the market value is Rs.150, 000/-.
- On 1/4/19 the statement of financial position of S was as follows

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Question 10

	Rs.000
PPE	800
Trade Receivables	150
Cash	50
Total Assets	1000
Stated Capital	500
Retained Earnings	200
Liabilities	300
Total Liabilities	1000

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Question 10

- On this date the PPE of S limited included a land carried at a value of Rs.300, 000/-, which had a fair value of Rs.400, 000/-.
- S was catering to a very specific customer segment and had a very well recognized trade mark and it was valued at Rs.40, 000/-. This has not been recognized in individual financials of S.
- An employee had filed a case against the company claiming a compensation of Rs.60, 000/-, no provision has been made in this regard.
- S Ltd had 1,000 shares in issue and market price of a share was Rs.750/- each.

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Question 10

Calculate,

10.1 Fair value of consideration

10.2 Fair value of the net assets acquired of S

10.3 Gain on Bargain Purchase on Acquisition if Non-Controlling interest was measured using proportionate net assets method

10.4 Gain on Bargain Purchase on Acquisition if Non-Controlling interest was measured using fair value method

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