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# Week 6-Non-controlling interest

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## Nature of non-controlling interest

-Where parent entity controls a subsidiary but owns less than 100% of its voting shares, the ownership interest in the group include both shareholders of the parent entity (PI) and non-controlling shareholders in the subsidiary (NCI).

## Alternative concepts of consolidation

-**Entity concept (AASB 10):** the group entity – it does not matter what proportion of subsidiary's equity that parent holds; as long as parent controls the subsidiary, it is consolidated in 'full' and included in the group)

-**Parent concept:** 'full' consolidation except the NCI is treated as a liability by the parent

-**Proprietary concept:** uses proportional consolidation so that if parent controls 60% of voting shares of subsidiary, it would consolidate only 60% of subsidiary's income, expense, assets and liabilities

-AASB 10 follows the entity concept and requires preparation of consolidated financial statements for the group irrespective of whether it comprises wholly owned or partly owned subsidiaries. So a natural consequence of the AASB 10 entity concept is that the equity of the economic entity comprises parent entity interest (PI) and Direct NCI. The entity focus means that consolidated financial statements are presented for the group entity

## Disclosure and measurement of non-controlling interest

AASB 127.27  
(SOFP)

•Non-controlling interests shall be presented in the consolidated statement of financial position within equity, separately from the equity of the owners of the parent.

AASB 127.28  
(SOPI)

•Profit or loss and each component of OCI are attributable to the owners of the parent and the NCI. OCI is attributed to the owners of the parent and to the NCI even if this results in the NCI having a deficit balance.

## Pros and Cons of Full consolidation v Proprietary concept

## Pros

- ❖ Provides more relevant information for users than full consolidation if a parent entity owns less than 100% of the shares in its subsidiary.

*Explanation:* Measure debt better. (You don't want to record more debt than the % of debt you are liable for)

## Cons

- ❖ It is deficient for assessing the planning, management and performance of management in instances where a parent entity owns less than 100% of the shares in its subsidiary.

*Explanation:* A parent entity with control over subsidiary (ownership of voting right >50%) controls all its resources. Therefore it would have been more logical for a full consolidation.

The parent entity can usually arrange for the post acquisition profits of subsidiaries to be distributed as dividends, so that those profits of the subsidiaries will eventually form part of the profits of the parent company to the extent that they are received as dividends.

However, directors of a parent entity can only declare a dividend for that entity out of its own profits not out of the profit of other entities in the group.

Moreover, dividends flow to shareholders because of ownership, not control. Hence, the relevant earnings attributable to Shareholders of the parent company should only stem from the earnings of the parent entity.

## Brief summary of consolidation process

1. Obtain trial balances of parent and subsidiary
2. Line by line aggregation in 'full' on a consolidation worksheet
3. Do consolidation adjustments/ eliminations in 'full' to determine consolidated 'group' revenues, expenses, assets, liabilities and equity
4. Examine group equity and group profit and apply a consistent rule to determine a reasonable split of these two consolidated amounts between direct NCI and PI for disclosure in the financial statements
5. The consolidation adjustment journal entries we already know alter only slightly if the parent owns < 100% (see next slide)

## Some implication when P owns <100%

1. When, at acquisition date, we eliminate Sub's OE against the cost of the investment in S (to P), we only eliminate P's share of Subs's share capital, retained earnings, reserves (etc) – ie., the DNCI in those items is not eliminated
2. When we eliminate dividends subsequently paid by Subs we only eliminate P's share.
3. Intra group transactions

- When we allocate group OE to DNCI we are effectively allocating 'group' numbers between PI & DNCI. Group numbers have been subjected to Consolidation Journal entries e.g. 'unrealised' profits/gains from Subs's to P.
- Because the DNCI is in S only, we base our calculations on Subs's numbers (the 'Subs' column of the CWS) but we modify them on the basis of the Consolidation Journal entries applicable to Subs. So, in principle: DNCI in current year 'group' income is a function of S's transactions with outsiders during the year.

**AASB 101 Presentation of Financial Statements** requires allocation of NCI in subsidiary to be disclosed in group's financial statements as follows:

-**NCI in equity** (equity section of consolidated balance sheet)

-**NCI in profit or loss** (on face of consolidated income statement)

-**NCI in total income and expense for the period** (on face of consolidated statement of changes in equity)

Our starting point is the equity and profits of the subsidiary entity (as the NCI only can only be attributed with a share in the subsidiary's results; not the parent's)

## AASB 127.4

- **Non-controlling interest is the equity in a subsidiary not attributable, directly or indirectly, to a parent.**
- NCI must be separately identified including - that portion of the profit or loss and net assets of a subsidiary attributable to equity interests that are not owned, directly or indirectly through subsidiaries, by the parent.

## AASB 127.18(c)

- (c) non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the parent's ownership interests in them. Non-controlling interests in the net assets consist of:
  - (i) the amount of those non-controlling interests at the date of the original combination calculated in accordance with AASB 3; and
  - (ii) the non-controlling interests' share of changes in equity since the date of the combination.

N/B: Even though NCI are aggregated for all partly owned subsidiaries, need split-up of closing retained earnings across opening RE, contribution to group profit or loss and appropriations such as dividends and transfers for the period.

### Residual interest method

Residual interest method treats Parent Interest (PI) as the residual interest after deducting NCI using final column from consolidation worksheet to pick up share capital, profit for the period, Opening Retained Earnings and dividends etc.

- ❖ Calculations are done in a separate allocation worksheet referred to as the memorandum account
- ❖ Prepare consolidated financial statements, use consolidation worksheet plus data from memorandum account

❖ Textbook says the residual interest method

The objective of NCI calculation is to show how much of the net assets of the group is represented by shareholder's equity balances that are attributable to the NCI and PI respectively.

Note: Memorandum account is a blank sheet to do calculation (There is no Debits and Credits)

### *Steps for creating memorandum accounting*

1. Insert section for each components of subsidiary's equity
  - a. Example: Share capital, Retained Earnings, Revaluation surplus, Profit
2. Insert balances as per subsidiary's financial statements or subsidiaries column from the Consolidated Worksheet
3. Adjust for upstream unrealized profit and depreciation adjustments
4. Add up the items and multiply by NCI ownership percentage

**Upstream transactions** = Subsidiary sells to parents

**Downstream transactions** = Parents sell to subsidiary

Note: Downstream transactions are ignored because here we are interested in calculating the NCI. We want to know how much of the unrealized profits belongs to NCI, therefore we are only interested in the upstream transactions.

All consolidation adjustment affect calculation of NCI except

- Elimination of Cost of Acquisition  
(Cost of acquisition is not affected by the NCI)
- Elimination of Downstream adjustments  
(Affect parent entity figures hence, not related to NCI)

These 2 transactions are ignored when it comes to the calculation of NCI because they are only related to parent entity figures.

### *List of Adjustment for Opening Retained Earnings and Profit for the year*

<b>Opening Retained Earnings</b>	
Opening Retained Earnings ( <b>Extracted from subsidiary accounting records</b> )	
<b>LESS</b> Unrealized after tax profit on <u>upstream intragroup transactions</u> realised in a later accounting period ( <b>Unrealised</b> )	
<b>LESS</b> previous years <u>after tax depreciation</u> adjustment in relation to fair value adjustment for Non-current assets on acquisition	
<b>ADD</b> <u>After tax depreciation</u> adjustment for upstream <u>intragroup sale of non current asset</u> in a previous accounting period ( <b>Part of profit is now realised</b> )	
<b>Contribution to consolidated retained earnings of the group</b>	

<b>Profit for the year</b>	
Record <b>profit for the period</b> extracted from <b>subsidiary's</b> accounting records	
<b>LESS Unrealised after tax profit on upstream</b> intra group transactions <b>realised in a later accounting period</b>	
<b>ADD Unrealised after tax profit on upstream</b> intra group transaction <b>realised in the current accounting period</b>	
<b>LESS</b> Current Year's after tax depreciation adjustment in relation to fair value adjustments for non-current asset on acquisition	
<b>ADD</b> Current year's realised after tax depreciation adjustment for upstream intra-group sale of non current asset in a previous accounting period ( <b>Part of the profit is now realised through use of the asset within the group</b> )	
<b>Contribution to consolidated profit for the year to the group</b>	

**Additional note:**

- ❖ Equity balances of subsidiary are used in calculation of NCI should be the same as the ones used to prepare consolidated financial statements. (Figures prior to consolidation)
- ❖ This is because the consolidated figures exclude intra-group transaction. As a result the figures may differ from those in subsidiary records.
- ❖ For NCI calculation we are only interested in upstream profit ONLY because the underlying profit is in the subsidiary account.
- ❖ (Downstream profit is contained in the parents account and it has nothing to do with the NCI)
- ❖ Calculation of NCI only affects equity, not revenue, expenses assets and liabilities.

**Comprehensive Example: Exercise 5.4**

On 1 April 2000, Major Ltd made a takeover offer for Minor Ltd and gained control of 75% of Minor Ltd's voting shares. AS a result, Major Ltd gained control of Minor Ltd's financial and operating policies on 1 April 2000. At this date, all assets of Minor Ltd were recorded at fair value. The statements of financial position of the two entities at 1 April 2000 are as follows:

	<b>Major Ltd</b> <b>\$,000</b>	<b>Minor Ltd</b> <b>\$,000</b>
<b>Assets</b>		
Current assets		
Inventories	9050	5800
Other current assets	<u>1950</u>	<u>2960</u>
Total current assets	11000	8760
Non-current assets		
PPE	21300	8540
Receivable from Minor Ltd	2300	-
Investment in Minor Ltd	<u>12000</u>	<u>      -</u>
Total non-current assets	<u>35600</u>	<u>  8540</u>
Total assets	46600	17300
<b>Liabilities</b>		
Current liabilities		
Trade and other payables	<u>8500</u>	<u>      -</u>
Total current liabilities	8500	-

Non-current liabilities		
Payable to Major Ltd	_____ -	<u>2300</u>
Total non-current liabilities	<u>8500</u>	<u>2300</u>
<b>Net assets</b>	<u>38100</u>	<u>15000</u>
<b>Equity</b>		
Issued Capital	20000	8000
Revaluation surplus	5600	2400
Retained earnings	<u>12500</u>	<u>4600</u>
Total Equity	<u>38100</u>	<u>15000</u>

### Additional information:

- At 1 April 2000, the fair value of the NCI in Minor Ltd was \$4,000,000
- The directors of Major Ltd are of the opinion an impairment loss will not be recognised in relation to its investment in Minor Ltd in its separate or consolidated financial statements at 1 April 2000.

### Measurement of Goodwill

Goodwill = Consideration transferred + Fair Value of the NCI – Fair value of net assets of the subsidiary acquired.

AASB 3.19 allows companies to choose between measuring the goodwill of NCI using full method or partial method.

Full method = Recognizes both NCI and PI interest in goodwill

Partial method = Recognizes only PI interest in goodwill

### (a) Acquisition Analysis using the “Partial” Method for Goodwill

	\$,000	\$,000
Consideration transferred:		
Purchase consideration		12,000
Identifiable assets and liabilities assumed at date of acquisition represented by:		
Issued Capital	8,000	
Revaluation Surplus	2,400	
Retained Earnings	<u>4,600</u>	
Identifiable assets and liabilities assumed at fair value	15,000	
Interest acquired	75%	<u>(11,250)</u>
Proportionate interest in goodwill		750

Date	Account	Debit (\$,000)	Credit (\$,000)
1/4/2000	Issued Capital	6,000	
	Revaluation Surplus	1,800	
	Retained Earnings	3,450	
	Goodwill	750	
	Investment in Minor Ltd		12,000



(Elimination of investment in Minor Ltd against 75% of pre-acquisition equities)			
	Payable to Major Ltd	2,300	
	Receivable from Minor Ltd		2,300
(Elimination of inter-company payable and receivable)			

### NCI Memorandum Account

		Minor Ltd	NCI
(a)	Issued Capital	8,000	
	Direct NCI – 25%		2,000
(b)	Revaluation Surplus	2,400	
	Direct NCI – 25%		600
(c)	Retained Earnings	4,600	
	Direct NCI – 25%		1,150
	<b>Total Shareholder's Equity of Minor Ltd</b>	<b>15,000</b>	
	<b>Total Direct NCI – 25%</b>		<b>3,750</b>

### Extract of Equity section of Consolidated Balance Sheet

	\$
Equity*	
Issued Capital	20,000
Revaluation Surplus	5,600
Retained Earnings	12,500
<b>Total equity attributable to equity holders of Major Ltd</b>	<b>38,100</b>
<b>NCI</b>	<b>3,750</b>
Total Equity	41,850
*Equity attributable to the parent and not the group	

### (b) Acquisition Analysis using the “Full” Method for Goodwill

	\$,000	\$,000
Consideration transferred:		
Purchase consideration	12,000	
NCI	4,000	16,000
Identifiable assets and liabilities assumed at date of acquisition represented by:		
Issued Capital	8,000	
Revaluation Surplus	2,400	
Retained Earnings	4,600	
Identifiable assets and liabilities assumed at fair value	15,000	
Interest acquired		(15,000)
Full goodwill		1,000

	\$,000	\$,000
<b>Goodwill attributable to PI</b>		
Interest acquired in FV of identifiable net assets	(11,250)	
Less: Consideration paid	<u>12,000</u>	
<b>Goodwill attributable to PI</b>		<b>750</b>
<b>Goodwill attributable to NCI</b>		
Total goodwill	1,000	
Less: PI goodwill	<u>(750)</u>	
<b>NCI attributable goodwill</b>		<b>250</b>

Date	Account	Debit (\$,000)	Credit (\$,000)
1/4/2000	Issued Capital	6,000	
	Revaluation Surplus	1,800	
	Retained Earnings	3,450	
	<b>Goodwill</b>	<b>1,000</b>	
	<b>NCI-equity</b>		<b>250</b>
	Investment in Minor Ltd		12,000
(Elimination of investment in Minor Ltd against 75% of pre-acquisition equities)			
	Payable to Major Ltd	2,300	
	Receivable from Minor Ltd		2,300
(Elimination of inter-company payable and receivable)			

### NCI Memorandum Account

		Minor Ltd	NCI
(a)	Issued Capital	8,000	
	Direct NCI – 25%		2,000
(b)	Revaluation Surplus	2,400	
	Direct NCI – 25%		600
(c)	Retained Earnings	<u>4,600</u>	
	Direct NCI – 25%		<u>1,150</u>
			3,750
(d)	<b>NCI-equity</b>		<b>250</b>
	<b>Total NCI</b>		<b>4,000</b>

### Extract of Equity section of Consolidated Balance Sheet

	\$
Equity*	
Issued Capital	20,000
Revaluation Surplus	5,600
Retained Earnings	12,500

Total equity attributable to equity holders of Major Ltd	38,100
NCI	4,000
Total Equity	42,100
*Equity attributable to the parent and not the group	

### Additional things to take note:

- ❖ Elimination of interest (investment), is eliminated based on percentage interest of PI ownership.
- ❖ Intra group transactions are eliminated in FULL regardless of percentage of PI ownership
- ❖ Dividends are eliminated based on percentage of PI ownership

## Disclosure and Measurement of Non-controlling interest

### AASB 127.4 - What is NCI and what should be disclosed

Non-controlling interest is the equity in a subsidiary not attributable, directly or indirectly to a parent.

NCI must be separately identified including the portion of the profit and loss and net assets of a subsidiary attributable to equity interest that are not owned, directly or indirectly through subsidiaries, by parent.

### AASB 127.18(c)

Non-controlling interest in the net assets consists of

- i. The amount of those non-controlling interest at the date of the original combination calculated in accordance with AASB 3 – Business combinations
- ii. NCI share of changes in equity since the date of the combination

### AASB 127.27

Non-controlling interest shall be presented in the consolidated statement of financial position within equity, separately from the equity of the owners of the parent.

### AASB 127.28

Profit or loss and each component of other comprehensive income are attributable to the owners of the parent and the non-controlling interest. Total comprehensive income is attributed to the owners of the parent and to the non-controlling interest even if this results in the non-controlling interest having a deficit balance.

### AASB101 – Presentation of Financial Statements

Allocation of NCI in subsidiary to be disclosed in group's financial statements as follows;

- ❖ NCI in equity (equity section of consolidated balance sheet)
- ❖ NCI in profit or loss (on face of consolidated income statement)
- ❖ NCI in total income and expense for the period (on face of consolidated statement of changes in equity)

*Note:* even though NCI are aggregated for all partly owned subsidiaries, need split-up of closing retained earnings across opening RE, contribution to group profit or loss and appropriations such as dividends and transfers for the period. (What we want to know is the % of group interest represented by shareholdings of NCI and PI)

### Elements to be disclosed and measured:

- ❖ Share capital