MCM-505

ACCOUNTING THEORY & PRACTICES

UNIT-11 FINANCIAL REPORTING FOR GROUP OF COMPANIES

(M. COM. SECOND SEMESTER)

Compiled By

Dr. Gagan Singh

Consolidated Financial Statements

- Financial statements of a group i.e. holding and subsidiary company presented as those of a single economic entity. These statements are prepared and presented by the holding company by incorporating the financial statements of its subsidiaries in a single set of financial statements and the whole group is presented as one entity. Consolidated Financial Statements are prepared and presented by the holding company for all the companies that are, directly or indirectly, controlled by the parent company.

Legal Requirements Regarding Presentation of Financial Information of a Group of Companies

- **Companies Act, 1956**
- Section 212 of the companies act requires that there shall be attached to the balance-sheet of a holding company having a subsidiary or subsidiaries at the end of the financial year as at which the holding company's balance-sheet is made out, the following documents in respect of such subsidiary or of each such subsidiary, as the case may be:—
- (a) A copy of the balance-sheet of the subsidiary;
- (b) A copy of its profit and loss account;
- (c) A copy of the report of its Board of directors;
- (d) A copy of the report of its auditors;
- (e) A statement of the holding company's interest in the subsidiary as specified in sub-section (3);
- (f) The statement referred to in sub-section (5) of section 212 if any; and
- (g) The report referred to in sub-section (6) of section 212, if any.

Accounting Standard 21-Consolidation of Financial Statements

- Accounting standard 21 is issued by the Institute of Chartered Accountants. It became effective from 1-04-2001. It requires that companies should prepare and present their consolidated financial statements in accordance with the provisions of this standard. Basic theme of this standard is that the financial statements about the holding company and the subsidiary company should be presented as statements of single economic entity, should disclose resources controlled by the group and liabilities owed by the group.
- Consolidated financial statements are required to include information about all the subsidiaries be it domestic or foreign subsidiaries. However, consolidation is not required in the following cases:
- (a) When the control of the holding company on the subsidiary company is of temporary nature; or
- (b) When subsidiary company operates under severe long-term restrictions resulting in inability to transfer funds to the parent company.
- Such unconsolidated subsidiaries should be accounted for in accordance with AS13.

Step by Step Process of Preparing the Consolidated Financial Statements

- **Calculation of Goodwill or Capital Reserve:** Sometimes the holding company at the time of acquiring controlling interest in the subsidiary company pays more money than the value of assets it acquire in return and sometimes it pays less money. In case the money invested is more than the value of assets acquired in return, then the excess money invested is referred to as 'Goodwill'. In case value of money invested is less than the value of assets acquired in return, then the difference is referred to as 'Capital Reserve'.
- **Calculation of Goodwill or Capital Reserve when investment is made in Installment:** In case holding company has made investment in installments to acquire control in the subsidiary company then the date from which holding company acquired control over subsidiary company will be considered for step by step consolidation of the financial statements.
- **Minority Interest:** Minority interest is the interest of outsiders in the subsidiary company. In other words it can be described as the value of shares of subsidiary company held by the shareholders other than holding company. Minority Interest is shown as liability in the consolidated balance sheet.

Accounting Treatment of Other Items

- **Inter-Group Transactions**: In case holding and subsidiary companies are in a business of buying and selling goods with each other, then effect of any unrealized profits from inter-group transactions should be eliminated from the consolidated financial statements. Unrealized profits is that portion of the profit earned by holding from subsidiary or subsidiary from holding on goods sold to each other and which is unrealized because such goods or part of such goods is lying unsold with the buying company.
- **Disposal of Investment in Subsidiary**

Summary

- Companies holding more than 50% share capital of other companies are called holding companies. Holding companies are required to prepare and present consolidated financial statements for the perusal of their users. Section 212 and Accounting standard 21 provides the framework for preparation and presentation of consolidated financial statements. Step by step procedure is followed by the holding companies for the preparation and financial statements. The main issues which demand attention of the accounting at the time of preparation of consolidated financial statements include assessment of Goodwill or Capital Reserve as the case may be, calculation of minority interest, settlement of inter-group transactions, adjustment for the difference between accounting policies and reporting dates.

References

- SILM developed by Uttarakhand Open University for MCM-505 (Accounting Theory and Practices), Year 2017,