TOPIC 20

INDAS-103

BUSINESS COMBINATION

Additional Sheet for Lecture No. 32 and 33

(Refer these notes while watching Lecture no. 32 and 33)

WHAT IS BUSINESS COMBINATION

A business combination is a transaction in which the **acquirer obtains control of another business** (the acquiree).

The term 'business' is defined as an **integrated set of activities and assets** that is capable of being conducted and managed for the purpose of **providing a return** in the form of **dividends, lower costs or other economic benefits** directly to investors or other owners, members or participants.

Business generally means major Assets and Liabilities. If the assets acquired are not a business, the reporting entity shall account for the transaction or other event as an asset acquisition. For example acquisition of a "Shell" company is not a business combination.

In a simple language, Business combination covers accounting of Amalgamation of Companies, Consolidation issues, Business Takeovers and Mergers.

Consolidation means: Grouping of Financial Statements of group companies. Group companies means Holding co. (Parent Co.), Subsidiary Co., Associates and Joint Ventures.

Scope of IndAS 103

- Recognizes and measures the ***identifiable assets*** acquired, the ***liabilities*** assumed and ***any non-controlling interest*** in the acquiree;
- Recognizes and measures the ***goodwill*** acquired in the business combination, or a **gain from a bargain purchase;**
- Determines what ***information to disclose*** about the business combination.

What to do now when these transactions of Business Combinations arise?

Apply 'ACQUISITION METHOD' ….. This method has 4 steps:

a. Identifying the Acquirer - the entity that obtains the control of another entity (will be discussed under IndAS 110 later)

Note:

In order to ascertain control do not look at the voting rights only. Evaluate other factors also like board control, potential voting rights etc.

b. Determining the Acquisition date - the date on which it obtains control of the acquiree.

Note:

(a) The date on which the acquirer obtains control of the acquiree is generally the date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree—the closing date.

Example:1

Company A acquired 80% equity interest in Company B for cash consideration. The relevant dates are as under:

- ✓ Date of shareholder agreement — 1st April, 20X1
- ✓ Appointed date as per shareholder agreement — 1st June, 20X1
- ✓ Date of obtaining control over the board representation — 1st July, 20X1
- ✓ Date of payment of consideration — 15th July, 20X1
- ✓ Date of transfer of shares to Company A — 1st August, 20X1

In this case, as the control over financial and operating policies are acquired through obtaining board representation on 1st July, 20X1, it is this date that is considered as the acquisition date. It may be noted that the appointed date as per the agreement is not considered as the acquisition date, as the Company A did not have control over Company B as at that date.

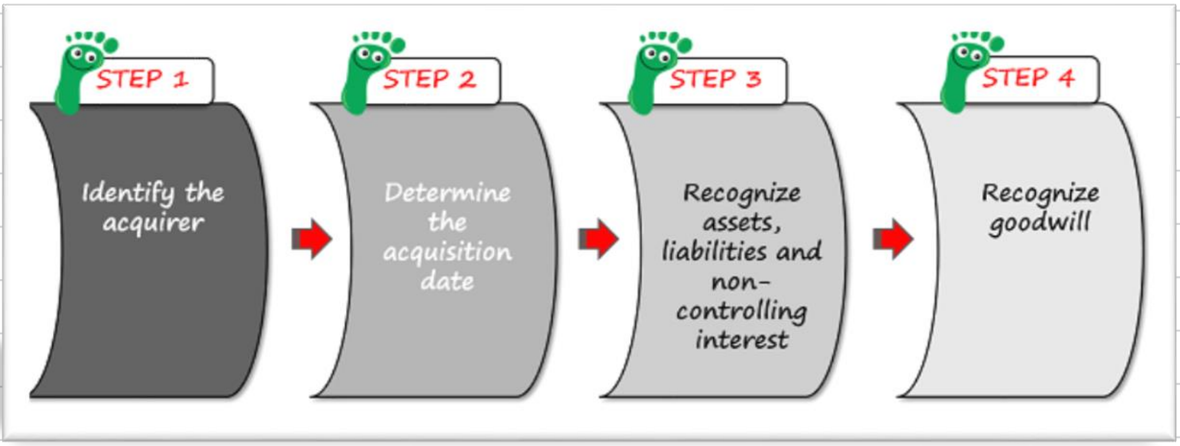
(b) On Acquisition date – Consideration, Identifiable Net Assets, Non-Controlling Interest & Goodwill/Gain on bargain purchase is to be measured or determined.

(c) If any approval of regulating authority is required for business combination then the date of obtaining approval may be considered as DOA.

c. ***Recognizing and Measuring*** *the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree;*

d. Recognizing and Measuring **Goodwill or a Gain from a Bargain Purchase.**

Acquisition Method



We need Four Elements for solving Question			
Consideration (PC) or Investment made by Parent co. only on DOA	**Fair Value of 100% Net Assets as on DOA & Again 100% Net Assets as on Consolidation Date for preparing BS**	**Value of NCI as on DOA & Again NCI is to be recalculated as on Consolidation Date for preparing BS**	**Value of Goodwill or Gain from Bargain Purchase only on DOA**
I. Cash: i. immediate ii. Deferred II. Other than Cash (Eg. Debentures, other securities) III. Contingent Consideration IV. Step Acquisition	Here Net Assets Means – (a) Equity Capital (b) Balance of Other equity as on DOA Other equity means Profits accumulated by any name.	NCI can be calculated by any of the following two approaches- (a) Fair Value Or (b) Proportion of Net Assets Qualifying NCI either at FV or Prop. Of Net Assets Non-qualifying NCI at FV	Goodwill/GBP will be Different when Non-Controlling interest valued at: a) Net Asset: Proportionate Goodwill b) Fair Value: Full Goodwill (preferred) Goodwill is subject to Impairment under IndAS 36, but not amortization.

WHAT IS PURCHASE CONSIDERATION UNDER BUSINESS COMBINATION?

Fair Value of Assets given on acquisition date	-	xxx
Fair Value of Liabilities incurred by acquirer	-	xxx
Fair Value of equity shares issued by acquirer	-	xxx
Fair Value of Deferred Consideration (at PV)	-	xxx***
Fair Value of Contingent Consideration (at PV)	-	xxx***

*** Difference between the actual consideration to be paid and the Fair value of Consideration recognised on acquisition date or any change after 1^{st} recognition will be transferred to Profit and Loss as Finance Cost every year.

Acquisition related cost incurred by an acquirer to effect a business combination are not part of the consideration transferred, for example –

(a) **STAMP DUTY** payment on acquisition of Land pursuant to business combination shall not be capitalised and treated as acquisition related cost – to be expensed off.

(b) **Any Payment to the regulator of acquiree to run license.**

> **Note** – Any Transaction cost incurred on Business Combination shall be directly transferred to Profit and Loss account.

NON-CONTROLLING INTEREST

Meaning - The Equity in a Subsidiary

(a) Not Attributable directly or indirectly

(b) To a Parent

i.e. when parent owns less than 100% of the equity of acquiree.

Presentation of NCI – Separately in the CFS of parent (usually under separate column of SOCIE)

Measurment of NCI – IndAS 103 requires measuring NCI as per the following methods:

Method – I

Fair value of shares held by NCI also known as Full Goodwill method

A Limited acquires 80% shares of B Limited whose NA are Rs 140.00 crores by payment in cash of Rs 120.00 crores. The value of non-controlling interest is Rs 30 crores.

NCI = 120/80% x 20% = 30 Cr.

Method – 2

Proportionate Share in Net Assets method also known as Partial Goodwill

Continuing with the above example in method I-

Assume that the value of recognized amount of subsidiary's identifiable net assets is Rs 140.00 crores, as determined in accordance with Ind AS 103. The value of non-controlling interest is Rs 28.00 crores (i.e. Rs 140 crores x 20%).

Types of NCI –

Meaning	**Qualifying NCI** – Present ownership interest and entitles its holders to a proportionate share in the Net Assets	**Non-Qualifying NCI** – All other components of NCI
Examples	Ordinary Equity Shares Preference Shares entitled to a *pro-rata* share of net asset upon liquidation	Equity component of convertible debt and other compound financial instruments Share warrants Options under Share based payments
Measurement of NCI	**Option 1** – At the Fair Value of the NCI **Option 2** – Proportionate share of Net Assets acquired	At Fair Value only unless another measurement basis is required by Ind-AS. Eg. SBP options of NCI are measured as per IndAS 102

Qualifying NCI (Important Note):

- When FV per share of acquiree is given in the question then use FV Method.
- When question requires NCI to be measured at FV – then FV of NCI shall be computed based on the price per share paid by parent (acquirer) for acquiring the control at DOA
- When FV is not given or question doesn't requires to calculate as per FV – then use Proportionate share of Net Assets acquired.

Negative NCI – NCI can be negative also when Net Assets acquired are negative (i.e. Assets are less and Liabilities are more)

CALCULATION OF GOODWILL OR GAIN ON BARGAIN PURCHASE:

Cost of Investments (FV of Consideration transferred)	Xxxx
Add: Fair Value of Previous Equity Interest (in case of Multiple Acquisition)	Xxxx
Add: Non-Controlling Interest as per above two methods	Xxxx
Less: Identifiable Net Assets of acquiree at Fair Value on DOA	Xxxx
Goodwill or Gain from Bargain Purchase	**XXXX**

*Gain on bargain purchase is recognised initially in OCI on the acquisition date and accumulate the same in equity as Capital Reserve under SOCE.

** Goodwill shall be presented in Consolidated Balance Sheet separately from Other Intangible Assets.

Carve Out –
IFRS 3 requires the entity to recognise Gain on Bargain Purchase to Profit or Loss A/c and not through OCI.

So basically from the above understanding of Consideration, NCI and goodwill we can conclude that, for consolidation of FS we need following elements:

a. Identifiable Net Assets
b. NCI
c. FV of Consideration transferred to acquire Control
d. Goodwill or Capital Reserve (Gain on bargain purchase)

How to solve the question when acquisition of control (DOA) is made during the year and balances of other equity (for the purpose of calculating Net Assets as on DOA) are not given on the same date?

Assume Profits (Other Equity) are accrued evenly throughout the year except when there are –

(a) Abnormal Items

(b) Non-Recurring Items

And Prepare "Statement of Changes in Net Assets"

	Particulars	Net Assets as on DOA	Changes during the period	Total Balance as on CFS date
	Balance of Share Capital			
+	Balance of other equity (profits)			
+/-	Abnormal Items/Non recurring items		XXX	
+	Dividend paid during the year		XXX	
=	Balances			
+/-	Time Adjustment (assume evenly accrued) **Time adjustment is done on Profit after Tax before any appropriation like dividend			
=	Balances after Time Adjustment			

- **Take Net Assets as on DOA as 100% for the purpose of calculating Goodwill/GBP**
- **Apportion the Change column between Parent's Share and NCI's Share**

FAIR VALUE OF IDENTIFIABLE NET ASSETS (REVALUATION)

Concept-

Identifiable Net Assets are always considered at Fair Value as on Date of Acquisition to calculate correct Goodwill or GBP, Since Purchase Consideration is by default at Fair Value (obviously if purchased from market then PC would be at Fair Value), therefore Net Assets should be taken at Fair Value for proper comparison.

Following Steps should be kept in mind if Separate Fair Values of Net Assets are given in the question:

1. Calculate **Revaluation Profit/loss** on the date of acquisition along with its Tax effect (i.e. DTL/DTA) – This shall be adjusted in the Net Asset as on acquisition date under "statement of Net Assets" in Pre-acquisition column.
2. **Calculate Additional Depreciation/Saving in Depreciation** due to revaluation of NA, and it shall be adjusted in the post-acquisition net assets along with its tax effect (i.e DTA/DTL)

How to Calculate Depreciation Effect on Revaluation of Assets:	
Depreciation that should be charged on Fair Value of PPE as on DOA till Date of Consolidation–	XXX
Less - Actual Depreciation charged in Books from DOA to Date of Consolidation -	XXX
Balancing Figure would be Additional Dep or Saving in Dep.	

3. In case of revaluation of Current Assets (like inventory or debtors) – if such CA are settled or realised during post-acquisition period, then above revaluation effect shall be reversed in the post-acquisition period of statement of NA along with Tax effect.

   If such CA are still o/s on balance sheet date (i.e not realised/settled yet) then no need to reverse the effect.

(In absence of any information, we will assume that Current Assets are still o/s on BS date)

Q131 - Business Combination without a Court approved scheme

ABC Ltd. acquired all the shares of XYZ Ltd. The negotiations had commenced on 1st January, 20X1 and the agreement was finalised on 1st March, 20X1. While ABC Ltd. obtains the power to control XYZ Ltd.'s operations on 1st March, 20X1, the agreement states that the acquisition is effective from 1st January, 20X1 and that ABC Ltd. is entitled to all profits after that date. In addition, the purchase price is based on XYZ Ltd.'s net asset position as at 1st January, 20X1. What is the date of acquisition?

Solution

Paragraph 8 of Ind AS 103 provides that acquisition date is the date on which the acquirer obtains control of the acquiree.

In this case, notwithstanding that the price is based on the net assets at 1st January, 20X1 and that XYZ Ltd.'s shareholders do not receive any dividends after that date, the date of acquisition for accounting purposes will be 1st March, 20X1. It is only on 1st March, 20X1 and not 1st January, 20X1, that ABC Ltd. has the power to direct the relevant activities of XYZ Ltd. so as to affect its returns from its involvement with XYZ Ltd. Accordingly, the date of acquisition is 1st March, 20X1.

Q132

Most Ltd. acquired 60% shares of Least Ltd. on 01/04/2017. It agreed to pay Rs. 20 lacs in cash, 25000 equity shares of Most Ltd. at a market value of Rs. 70/- each. Most Ltd. also agreed to pay deferred consideration of Rs. 18,00,000 after 2 years. In case least Ltd. performs beyond certain limits then additional consideration will be paid at the end of 1st Year for Rs. 250000/-. Fair value of Contingent consideration is Rs. 1,50,000/-. Discount rate is 10%. Most Ltd. follows Cost Method under Ind AS 27. Calculate Total Consideration under Business Combination. Fair value of shares of Least Ltd. is 80/- on 31.03.2018.

(Answer: Consideration – 53,87,600/-)

Q133

From the following Separate Balance Sheets of H Ltd. and S Ltd. as on 31.03.18, prepare Consolidated Balance Sheet of H Ltd. as per IndAS 110 and 103.

Particulars	H Ltd.	S Ltd.
Property Plant & Equipment	15,00,000	10,00,000
Investment in S Ltd. (80%)	9,00,000	-
Current Assets	6,00,000	5,00,000
Share Capital	12,00,000	6,00,000
Reserves and Surplus	8,00,000	4,00,000
Liabilities	10,00,000	5,00,000

Shares were acquired on 31.03.2018. Calculate identifiable NA to be recognised, NCI and Goodwill or Gain on bargain purchase if any. Also make journal entry.

(Answer: Full Goodwill – 125000/- and Partial Goodwill – 100000/-)

Q134

From the following Separate Balance Sheets of H Ltd. and S Ltd. as on **31.03.18,** prepare Consolidated Balance Sheet of H Ltd. as per IndAS 110 and 103.

Particulars	**H Ltd.**	**S Ltd.**
Property Plant & Equipment	15,00,000	10,00,000
Current Assets	6,00,000	5,00,000
Share Capital Fv 10/-	10,00,000	6,00,000
Reserves and Surplus	7,00,000	4,00,000
Liabilities	4,00,000	5,00,000

H Ltd. acquired **on 31.03.2018** shares in S Ltd. 45000 no. by paying Rs. 1,00,000 in cash, issuing 12000 its equity shares at 30/- and 250000 to be paid after 2 years (Discount rate is 10%). Fair value of share of S Ltd. on acquisition date is 16/-

Calculate identifiable NA to be recognised, NCI and Goodwill or Gain on bargain purchase if any. Also make journal entry.

(Answer: Consideration – 666500/-; NCI – 240000; CR – 93500; BS 3500000)

Q135

From the following Separate Balance Sheets of H Ltd. and S Ltd. as on 31.03.18, prepare Consolidated Balance Sheet as per IndAS 110 and 103 of H Ltd.

Particulars	**H Ltd.**	**S Ltd.**
Property Plant & Equipment	15,00,000	10,00,000
Current Assets	8,00,000	5,00,000
Investment in S Ltd.	7,00,000	-
Share Capital	10,00,000	6,00,000
Reserves and Surplus	10,00,000	4,00,000
Liabilities	10,00,000	5,00,000

H Ltd. acquired **on 01.04.2017** shares @ 75%. It is given that the opening balance (1.4.17) of R&S of S Ltd. is 1,00,000.

Calculate identifiable NA to be recognised, NCI and Goodwill or Gain on bargain purchase if any. Also make journal entry.

(Answer: - Goodwill – 175000(prop. Method) or 2,33,333 fair value method)

Q136: Goodwill recognised depends on how NCI is measured.

Ram Ltd. acquires Shyam Ltd. by purchasing 60% of its equity for Rs 15 lakh in cash. The fair value of non-controlling interest is determined as Rs 10 lakh. The net aggregate value of identifiable assets and liabilities, as measured in accordance with Ind AS 103 is determined as Rs 5 lakh.

How much goodwill is recognized based on two measurement bases of non-controlling interest (NCI)?

Solution:

A. NCI is measured at NCI's proportionate share of the acquiree's identifiable net assets

Ram Ltd. recognizes 100% of the identifiable net assets on the acquisition date and decides to measure NCI at proportionate share (40%) of Shyam Ltd. identifiable net assets.

The journal entry recorded on the acquisition date for the 60% interest acquired is as follows: **(in lakhs)**

		Dr. (Rs in lakh)	Cr. (Rs in lakh)
Identifiable net assets	Dr.	5	
Goodwill (Balancing figure)	Dr.	12	
To Cash			15
To NCI			2

NCI is (Rs 5 lakh x 40%) = Rs 2 lakh. Hence, goodwill of Rs 12 lakh is calculated as consideration Rs 15 lakh plus NCI Rs 2 lakh less identifiable net assets and liabilities Rs 5 lakh.

The goodwill recognized under Ind AS 103, therefore, represents entity A's 60% share of the total goodwill attributable to Shyam Ltd. It does not include any amount of goodwill attributable to 40% NCI.

B. NCI is measured at fair value

The facts are as above, but Ram Ltd decides to measure NCI at fair value rather than at its share of identifiable net assets.

The fair value of NCI is determined as Rs10 lakh (given in the question), which is the same as the fair value on a per-share basis of the purchased interest.

The acquirer recognizes at the acquisition date

i. 100% of the identifiable net assets,

ii. NCI at fair value, and

iii. Goodwill.

The journal entry recorded on the acquisition date for the 60% interest acquired is as follows:

		Dr. (Rsin lakh)	Cr. (Rsin lakh)
Identifiable net assets	Dr.	5	
Goodwill (Balancing figure)	Dr.	20	
To Cash			15
To NCI			10

Therefore, goodwill recognized where NCI is measured at fair value as per Ind AS 103 represents the group's share to total goodwill attributable to Shyam Ltd. and the NCI's share of the total goodwill attributable to Shyam Ltd.

Q137: Gain on a bargain purchase when NCI is measured at fair value

Seeta Ltd. acquires Geeta Ltd. by purchasing 70% of its equity for Rs 15 lakh in cash. The fair value of NCI is determined as Rs 6.9 lakh. Management have elected to adopt full goodwill method and to measure NCI at fair value. The net aggregate value of the identifiable assets and liabilities, as measured in accordance with the standard is determined as Rs 22 lakh. (Tax consequences being ignored).

Solution

The bargain purchase gain is calculated as follows:

	(Rsin lakh)
Fair value of consideration transferred	15.00
Fair value of NCI	6.90
Fair value of previously held equity interest	n/a
	21.90
Less: Recognised value of 100% of the net identifiable assets, measured in accordance with the standards	(22.00)
Gain on bargain purchase	(0.10)

The recognized amount of the identifiable net assets is greater than the fair value of the consideration transferred plus fair value of NCI. Therefore, a bargain purchase gain of Rs0.10 lakh is either recognised in OCI and accumulated in equity as capital reserve or directly in equity as capital reserve.

The journal entry recorded on the acquisition date for 70% interest is as follows:

		Dr. (Rsin lakh)	Cr. (Rsin lakh)
Identifiable net assets	Dr.	22.00	
To Cash			15.00
To Gain on bargain purchase			0.10
To NCI			6.90

Since NCI is required to be recorded at fair value, a bargain purchase is recognized for Rs0.1 lakh.

Q138: Gain on a bargain purchase when NCI is measured at proportionate share of identifiable net assets.

Continuing the facts as stated in the above illustration, except that Seeta Ltd. chooses to measure NCI using a proportionate share method for this business combination. (Tax consequences have been ignored).

Solution

This method calculates the bargain purchase same as under the fair value method, except that NCI is measured as the proportionate share of the identifiable net assets.

The bargain purchase gain is as follows:

	(Rsin lakh)
Fair value of consideration transferred	15.00
Fair value of NCI (30% of Rs22.0 lakh)	6.60
Fair value of previously held equity interest	N/A
	21.60
Less: Recognised value of 100% of the net identifiable assets, measured in accordance with the standards	(22.00)
Gain on bargain purchase	(0.40)

As the recognized amount of the identifiable net assets is greater than the fair value of consideration transferred, plus the recognized amount of NCI (at proportionate share), a bargain purchase gain of Rs0.4 lakh is either recognised in OCI and accumulated in equity as capital reserve or directly in equity as capital reserve.

The journal entry recorded on the acquisition date for 70% interest is as follows:

		Dr. (Rsin lakh)	**Cr. (Rsin lakh)**
Identifiable net assets	Dr.	22.0	
To Cash			15.0
To Gain on bargain purchase			0.4
To NCI			6.6

Under the proportionate share method, NCI is recorded at its proportionate share of its net identifiable assets and not at fair value.

Q139: Measurement of goodwill when there is no non-controlling interest

X Ltd. acquired Y Ltd. on payment of Rs25 crore cash and transferring a retail business, the fair value of which is Rs15 crore. Assets acquired and liabilities assumed in the acquisition are Rs36 crore.

Find out the Goodwill.

Solution

(All figures are Rsin crores)	
Fair value of the consideration paid (Rs25 cr + Rs15 cr)	40
Fair value of assets acquired net of fair value of liabilities assumed	(36)
Goodwill	4

Q140: Measurement of goodwill when there is non-controlling interest

Raja Ltd. purchased 60% shares of Ram Ltd. paying Rs525 lakh. Number of issued capital of Ram Ltd. is 1 lakh. Fair value of identifiable assets of Ram Ltd. is Rs640 lakh and that of liabilities is Rs50 lakh. As on the date of acquisition, market price per share of Ram Ltd. is Rs775. Find out the value of goodwill.

Solution

(Rs in lakh)	
(i) Fair value of consideration paid	525
(ii) Fair value of non-controlling interest (40% x 1 lakh x Rs775)	310
(A)	**835**
Fair value of identified assets	640
Less: Fair value of liabilities	(50)
Fair value of Net Identified Assets (B)	**590**
Goodwill [(A) – (B)]	**245**

Note: When goodwill is measured taking non-controlling interest at fair value, it is often termed as full goodwill.

On the other hand, it is possible to measure non-controlling at the proportionate value of net assets.

Amount in lakhs	
(i) Fair value of consideration paid	525
(ii) Proportionate value of non-controlling interest (40% x 590 lakh)	236
(A)	**761**
Fair value of identified assets	640
Minus fair value of liabilities	(50)
Fair value of Net assets (B)	590
Goodwill [(A)-(B)]	**171**

When non-controlling interest is measured at proportionate share of net asset, the goodwill is popularly termed as partial goodwill.

Q141. Abnormal Items

Balance Sheet 31.3.2020

Assets	**H**	**S**
Non Current Assets:		
Fixed Assets	500,000	300,000
Investment in 80% shares	200,000	-
Current Assets	150,000	200,000
	850,000	**500,000**
Equity & Liabilities		
Shareholder Funds:		
Share capital	400,000	300,000
Other Equity:		
Profit & Loss a/c	100,000	80,000
General reserve	200,000	50,000
Capital reserve	100,000	50,000
Current Liabilities:		
Creditors	50,000	20,000
	850,000	**500,000**

H Ltd. had acquired shares of S Ltd. on 1/8/19. Balance of S Ltd. reserves on. 1/4/19.

Profit & Loss a/c	20,000
General reserve	14,000
Capital reserve.	26,000

There were abnormal items on certain dates.

Date	**Item**	**Amount**
1-11-19	Abnormal loss	2000
1-7-19	Abnormal gain	3000

Prepare Consolidated Balance Sheet, Assume NCI as per Proportionate Share of Net Assets.

(Answer: CR: 122134, NCI: 96000, BS Total: 1150000)

Q142. Fair Value of Net Assets

Balance Sheet 31.3.2020

	H	S
Non-Current Assets:		
Fixed Assets	6,00,000	3,50,000
Investment 90% Shares	5,00,000	-
Current Assets	2,00,000	4,00,000
	13,00,000	**7,50,000**
Equity & Liabilities	**H**	**S**
Share Capital	6,00,000	3,00,000
Profit & Loss a/c	1,00,000	1,50,000
General reserve	2,00,000	40,000
Current Liabilities	4,00,000	2,60,000
	13,00,000	**7,50,000**

H Ltd. acquired share of S Ltd. on 31.3.2020 Market value of Fixed assets of H Ltd, 6.50,000 and S Ltd. 9,00,000. Assume Tax Rate is 30%. Prepare consolidated Balance sheet.

Q143. Fair Value of Net Assets

Balance Sheets as on 31.03.18

Particulars	H Ltd.	S Ltd.
Land	750000	500000
Investment in Sub 75%	840000	-
Other Assets	460000	400000
Share Capital	900000	500000
Other Equity	700000	200000
Liabilities	450000	200000

Investments were made on 1.04.17 when balance in other equity of S was 80,000.
Land is appreciated by Rs. 150000 on 1.4.17. Tax rate 30%. Prepare CBS
(Answer: Goodwill 326250/-; BS 2586250/-)

Student Notes:-

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