Accounting Standard

AASB 1024
May 1992

Consolidated Accounts

AASB 1024

CONTENTS

Starting at Paragraph:

Citation

1 This Accounting Standard may be cited as Accounting Standard AASB 1024: Consolidated Accounts.

Accounting Standards and Commentary

STANDARDS

2 **The accounting standards set out in this Standard are shown in bold print. Commentary is shown in normal print immediately after the accounting standards to which it relates.**

3 **This Standard is to be interpreted in accordance with the Corporations Law, including Parts 1.2 and 3.6. The commentary contained in this Standard can be used, subject to section 109J of the Corporations Law, as an aid to interpreting the accounting standards set out in this Standard.**

4 **Except for a citation of a superseded Standard in an application paragraph, any reference in this Standard to another Standard made by the Australian Accounting Standards Board shall be taken to include a reference to that Standard, as subsequently replaced or amended by a Standard (if any) made by the Board, as it applies to the financial year for which the consolidated accounts are being prepared.**

Application and Operative Date

STANDARDS

5 **This Standard:**

(a) **applies to each company that is the parent entity in an economic entity which is a reporting entity in relation to the economic entity's first financial year that ends on or after 30 June 1992 and later financial years; and**

(b) **when operative, supersedes Accounting Standard AASB 1024: Consolidated Accounts, the making of which was notified in *Gazette* No. S260 on 20 September 1991.**

6 **When a parent entity prepares a financial report which it purports to be a general purpose financial report for an economic entity which is not a reporting entity, it shall apply this Standard as if the economic entity is a reporting entity.**

COMMENTARY

(i) The Australian Accounting Standards Board made this Standard on 22 May 1992, having had regard to the matters stated in subsection 32(3) of the *Corporations Act 1989*. Notice of the making of this Standard was published in the *Commonwealth of Australia Gazette* on 26 May 1992.

(ii) In all cases, complying with a requirement of this Standard is subject to any applicable provision of the Corporations Law.

Applying the Standard to economic entities

COMMENTARY

(iii) Adoption of the criterion of control for defining an economic entity has significant implications in respect of the parent entity/ subsidiary relationships identified in accordance with this Standard and the legal form of the entities involved. Adoption of the criterion of control will enable a complete economic entity to be reflected in consolidated accounts even though, for example, some of the subsidiaries may be in the form of partnerships or trusts.

(iv) There may be circumstances where an economic entity is not a reporting entity as defined in this Standard. This might occur, for instance, where the economic entity is within another economic entity which is a reporting entity. Where an economic entity is not a reporting entity, the preparation of consolidated accounts for that entity is not required by this Standard.

Claims for exclusion from scope of the Standard

COMMENTARY

(v) It is sometimes argued that in certain circumstances parent entity/ subsidiary relationships should be exempted from the requirement to prepare consolidated accounts. However, the adoption in this Standard of control as the criterion for determining a parent entity/subsidiary relationship enables identification of an economic entity for which consolidated accounts may be prepared and, provided the economic entity is a reporting entity, no exemptions from the standards set out in this Standard are justified. Some commonly suggested exclusions are identified below and explanations are provided as to why they do not constitute exclusions from the standards set out in this Standard.

Temporary control

COMMENTARY

(vi) Temporary control does not of itself affect the economic entity for which consolidated accounts are to be prepared. During the time that control is held and until such time as control ceases, the subsidiary is part of the economic entity and needs to be reflected in the consolidated accounts.

Impaired control

COMMENTARY

(vii) The existence of severe restrictions which impair control means that the consolidation criterion is not satisfied and would result in the entity in question no longer being part of the economic entity. This would include, for instance, where a subsidiary is located in a country in which the government has undertaken certain actions, such as adopting legislation to provide for expropriation of the assets of the subsidiary, which impair control by the parent entity. Another example would be where a subsidiary is in the process of being liquidated. While the existence of such restrictions would generally constitute an impairment of the parent entity's control, each case would need to be assessed in the light of the prevailing circumstances. No exclusion or exemption is necessary where control is impaired since consolidation of the entity in these circumstances would contravene the standards set out in this Standard.

Dissimilar activities

COMMENTARY

(viii) Where the activities of entities within the economic entity are dissimilar it is sometimes claimed that aggregation of the accounts of each of the component entities may reduce the usefulness of the consolidated accounts. However, since the objective in preparing consolidated accounts is to reflect the economic entity as a single reporting entity, it does not matter whether the entities comprising the economic entity are involved in dissimilar activities. Where economic entities are involved in dissimilar activities, the extent of this involvement can be conveyed in the consolidated accounts by the provision of disaggregated information on the various lines of activity. Accounting Standard AASB 1005: Financial Reporting by Segments provides guidance on the provision of information about significant industry and geographical segments.

<u>*Parent entity holds a minority ownership interest in a subsidiary*</u>

COMMENTARY

(ix) Exemption from the requirement to include a subsidiary in consolidated accounts is also sometimes proposed where the parent entity does not hold a majority ownership interest in the subsidiary. However, because control rather than ownership interest is the consolidation criterion in this Standard, the absence of a majority ownership interest does not affect the economic entity or the requirement to prepare consolidated accounts, provided that control exists. The extent of the parent entity's ownership interest in the subsidiary will be evident from the equity disclosures in the consolidated accounts.

<u>*Statement of Purpose*</u>

STANDARDS

7 **The purpose of this Standard is to:**

(a) identify for financial reporting purposes parent entities and subsidiaries; and

(b) prescribe the circumstances in which consolidated accounts are to be prepared and the financial information to be included in those accounts;

so that the consolidated accounts reflect the performance, financial position and financing and investing of a group of related entities as a single economic entity.

COMMENTARY

(x) In this Standard, the concept of the reporting entity is extended from the legal entity or other single entity to recognise the existence of an economic entity stemming from interrelationships between entities. The objective underlying the preparation of accounts for this economic entity is to provide relevant and reliable financial information about the related entities as a single reporting entity to reflect that these entities operate as a single economic unit. For a number of entities to be able to operate together as a single economic unit, they need to be under common direction, thereby providing consistency in the objectives being pursued. This occurs when entities are related by being under the common control of one entity. Hence, in this Standard it is contended that it is control rather than ownership that provides the criterion which is fundamental to identification of the group of related entities for which the presentation of consolidated accounts is required. The preparation of consolidated accounts for this economic entity is consistent with Statement of Accounting Concepts SAC 2 "Objective of General Purpose Financial Reporting", which states that general purpose financial reports shall provide information useful to users for making and evaluating decisions about the allocation of scarce resources.

Application of Materiality

STANDARDS

8 **The accounting standards set out in this Standard shall apply to consolidated accounts where such application is of material consequence. Information in consolidated accounts is material if its omission, non-disclosure or misstatement has the potential to adversely affect:**

(a) decisions about the allocation of scarce resources made by users of the consolidated accounts; or

(b) the discharge of accountability by directors.

COMMENTARY

(xi) In deciding whether an item is material, its nature and amount usually need to be evaluated together.

Definitions

STANDARDS

9 **In this Standard:**

"capacity" means ability or power, whether direct or indirect, and includes ability or power that is presently exercisable as a result of, by means of, in breach of, or by revocation of, any of or any combination of the following:

(a) trusts;

(b) relevant agreements; and

(c) practices;

whether or not enforceable;

"control" means the capacity of an entity to dominate decision-making, directly or indirectly, in relation to the financial and operating policies of another entity so as to enable that other entity to operate with it in pursuing the objectives of the controlling entity;

"economic entity" means a group of entities comprising the parent entity and each of its subsidiaries;

"entity" means any legal, administrative, or fiduciary arrangement, organisational structure or other party (including a person) having the capacity to deploy scarce resources in order to achieve objectives;

"financial report" means accounts or consolidated accounts or both;

"general purpose financial report" means a financial report intended to meet the information needs common to users who are unable to command the preparation of reports tailored so as to satisfy, specifically, all of their information needs;

"outside equity interest" means the equity in the economic entity other than that which can be attributed to the ownership group of the parent entity;

"ownership interest" means the capital held by an entity directly, and/or indirectly through another entity;

"parent entity" means an entity which controls another entity;

"recognised" means reported on, or incorporated in amounts reported on, the face of the profit and loss account or balance sheet (whether or not further disclosure of the item is made in notes thereto);

"reporting date" means the end of the financial year to which the accounts or consolidated accounts relate;

"reporting entity" means an entity (including an economic entity) in respect of which it is reasonable to expect the existence of users dependent on general purpose financial

reports for information which will be useful to them for making and evaluating decisions about the allocation of scarce resources, and includes but is not limited to an economic entity in which the parent entity is one of the following:

(a) **a listed corporation;**

(b) **a borrowing corporation; and**

(c) **a company which is not a subsidiary of a holding company incorporated in Australia and which is a subsidiary of a foreign company where that foreign company has its securities listed for quotation on a stock market or those securities are traded on a stock market; and**

"subsidiary" means an entity which is controlled by a parent entity.

COMMENTARY

(xii) Relevant provisions of the Corporations Law include:

Section 286: an expression in a Standard has the same meaning as it has in Parts 1.2 or 3.6 of the Corporations Law except so far as the contrary intention appears.

Section 9: definition of "accounting standard", "accounts", "borrowing corporation", "company", "consolidated accounts", "financial year", "holding company", "listed corporation", "profit and loss account" and "stock market".

Reporting entities

COMMENTARY

(xiii) Economic entities other than the types identified in the definition of "reporting entity" may, in particular circumstances, be reporting entities. Such entities are required to comply with this Standard in those circumstances. Paragraphs 19 to 37 of Statement of Accounting Concepts SAC 1 "Definition of the Reporting Entity" provide guidance for determining whether an entity is a reporting entity.

(xiv) General purpose financial reports are required to be prepared for economic entities which are reporting entities and in which the parent entity is a company in accordance with all Accounting Standards and Statements of Accounting Concepts, except that to the extent of any incompatibility between a Standard and a Statement of Accounting Concepts, the requirements of the Standard prevail.

Control

COMMENTARY

(xv) Whether an entity has control of another entity will always be a question to be decided in the light of the prevailing circumstances. The definition of control depends upon substance rather than form and, accordingly, determination of the existence of control will involve the preparer of the financial reports in exercising professional skill and judgement.

(xvi) Any of the following factors would normally indicate the existence of control by one entity of another entity:

(a) the capacity to dominate the composition of the board of directors or governing board of another entity;

(b) the capacity to appoint or remove all or a majority of the directors or governing members of another entity;

(c) the capacity to control the casting of a majority of the votes cast at a meeting of the board of directors or governing board of another entity;

(d) the capacity to cast, or regulate the casting of, a majority of the votes that are likely to be cast at a general meeting of another entity, irrespective of whether the capacity is held through shares or options; and

(e) the existence of a statute, agreement, or trust deed, or any other scheme, arrangement or device, which, in substance, gives an entity the capacity to enjoy the majority of the benefits and to be exposed to the majority of the risks of that entity, notwithstanding that control may appear to be vested in another party.

(xvii) Another factor which may indicate the existence of control is ownership interest. The holding of an ownership interest usually entitles the investor to an equivalent percentage interest in the voting rights of the investee. Consequently, a majority ownership interest would normally, though not necessarily, be accompanied by the existence of control. However, it is the voting rights rather than the ownership interest that provide the potential for control. In fact, it may be possible to control another entity without holding any ownership interest in that entity. This would be rare in the private sector where it is normal for an entity to have owners with an equity interest therein, especially where a third unrelated party holds a majority ownership interest.

(xviii) The concept of control is defined as a capacity, thereby allowing for the role of dominance to be a passive one rather than one which is necessarily actively exercised. If doubt exists as to whether an entity has the capacity to dominate another entity, there may, on occasions, need to be an active demonstration of control. This may be evident, for instance, by an entity being able to obtain financial information, internal management forecasts and budgets, and entity records from the other entity on request.

(xix) It may be possible to control the voting rights of another entity without holding a majority interest in the voting rights. This would happen where, in the absence of another entity dominating the composition of the board of directors, voting rights held by one entity, while less than 50 per cent, constitute a majority of those voting rights which are exercised.

(xx) The indicators of control outlined in the preceding paragraphs need to be distinguished from the circumstance where control of a particular entity is jointly held by two or more unrelated entities such that none unilaterally controls that entity. In this case none of the entities would qualify as the parent entity; however, it is important to consider the substance of the relationship between the entities which are deemed to have joint control of that other entity. For example, it is not unusual for an entity to be established to avoid recognising certain assets and liabilities in the accounts. While ownership interests and board representation of the new entity may be vested equally in the entity which sought to establish the new entity and in its financiers or legal advisors, this relationship may not constitute joint control as discussed above. To determine with whom control lies, it will be necessary to examine the manner in which major policy decisions are reached and the nature of the control over ongoing activities of the entity, rather than accepting that the nominal powers reflect the substance of the relationship.

(xxi) The definition of "control" is such that, on rare occasions, an entity may appear to be the subsidiary of two unrelated entities. An example of this would occur where an entity exercises dominance of the decision-making in relation to the operating policies of another entity while another entity simultaneously possesses the capacity to dominate decision-making without exercising that power. This form of control, while rare, may be evident where institutional investors hold investments with the objective of generating positive cash flows through dividends and capital gains rather than for the purpose of managing the operations of the other entity. It is important to establish that the entity actually exercising dominance over the operating policies is not merely doing so, either implicitly or explicitly, in accordance with the wishes of the other "controlling" entity. The concept of control employed in this Standard is defined in terms of dominance of both the financial and operating policy decisions, which implies a singular line of power. In the example cited in this paragraph, if neither of the entities is in the position of absolute dominance over the third entity, the relationship would be one of joint control determined by implicit agreement rather than control.

(xxii) Sometimes an entity is regarded as being economically dependent on another entity. This is usually the case when the viability of the ongoing operations of one entity depends on funding by, or on a significant volume of business with, another entity. However, it ought not to be assumed that economic dependence is synonymous with control. While economic dependence would usually give rise to a relationship based on influence it is unlikely, in the absence of some very restrictive contractual condition, that it would enable an entity to dominate decision-making in relation to both the financial and operating policies of the other entity as would be necessary for control to exist.

(xxiii) The capacity of one entity to dominate decision-making, in relation to the financial and operating policies of another entity, is insufficient in itself to ensure the existence of control as defined in this Standard. The parent entity needs to be able to dominate decision-making so as to enable that other entity to operate with it as part of an economic entity in pursuing its objectives. This will have the effect of excluding from the definitions of "parent entity" and "subsidiary" relationships which do not extend beyond, for instance, that of a liquidator and the entity being liquidated and would normally exclude a lender and borrower relationship and a receivership relationship. Similarly, a trustee whose relationship with a trust does not extend beyond the normal responsibilities of a trustee would not be considered to control the trust for the purposes of this Standard.

(xxiv) Where control appears to be vested entirely with one party, another party might, in substance, be the controlling party. Consider, for example, a trust where the capacity for decision-making appears to rest entirely with the trustee, even to the extent that the trust deed precludes the unitholders from changing the trustee or holding effective meetings. Because the trustee's capacity to dominate decision-making is governed by the trustee's fiduciary responsibility at law to act in the best interests of the beneficiaries of the trust, those beneficiaries indirectly have the capacity to dominate decision-making in respect of the net assets of the trust.

Defining the economic entity

COMMENTARY

(xxv) In this Standard, consistent with the objective of reporting for related entities so as to reflect that they operate as a single economic entity, the criterion of control has been used to determine a parent entity/subsidiary relationship and for identifying an economic entity for which consolidated accounts may be prepared. Under this approach, the economic entity is defined as the group of entities comprising the parent entity and each of the entities which it controls. The consolidated accounts for the economic entity would reflect the performance of that group and the resources under the control of the parent entity irrespective of whether an ownership interest is held. This approach is considered to provide the most meaningful consolidated accounts in that it enables a number of individual but related entities to be identified as a single entity for financial reporting purposes in a manner which is consistent with the substance of the economic entity operating as a single economic unit.

(xxvi) Where a member of the economic entity is structured in a form which differs from the legal form of other members of the economic entity or where the parent entity does not hold an ownership interest in an entity which, in all respects, is a member of the economic entity, these factors would not cause those entities to be excluded from consolidated accounts for that economic entity. To prepare consolidated accounts to reflect primarily the parent entity's ownership interests would unnecessarily restrict the financial information that can be made available to users. However, it is considered that disclosure in consolidated accounts of information about ownership interests is of relevance to users of financial reports. Therefore, this Standard requires that the consolidated accounts disclose the extent to which the equity of the economic entity is attributable to the ownership group of the parent entity and to the outside equity interest.

Preparation of Consolidated Accounts

STANDARDS

10 **Each company required to apply this Standard shall prepare and present consolidated accounts for the economic entity in which it is the parent entity.**

11 **Consolidated accounts shall be prepared by combining the accounts of each of the entities comprising the economic entity and this aggregated information shall be presented as one set of accounts. This aggregation shall be subject to such adjustments as may be necessary under this Standard.**

Use of consolidated accounts

COMMENTARY

(xxvii) The provision of one set of accounts for the economic entity enhances the ability of those users of financial reports who have an interest in the existence of the economic entity to assess the performance, financial position, and financing and investing of the economic entity, rather than having to rely solely on individual accounts. However, the preparation of consolidated accounts does not, of itself, overcome the need to prepare individual accounts for the entities within the economic entity. The consolidated accounts are required in addition to any such individual accounts. The alternative presentation format for the economic entity, whereby the individual accounts for some, or all, of the entities comprising the economic entity are presented without aggregation, is not permitted by this Standard. Consolidated accounts are the only presentation format which satisfies the objective of reporting for the economic entity as a single reporting entity.

Consolidation adjustments

COMMENTARY

(xxviii) In combining the accounts of a parent entity and those of its subsidiaries, various adjustments may be necessary to reflect the performance, financial position and financing and investing of the economic entity as a single reporting entity. Principally these adjustments will be necessary whenever entities within an economic entity have had transactions with each other or where there is a change in the composition of the economic entity. Two distinct types of transactions can be identified. The first of these relates to the holding of investments by a parent entity in its subsidiaries and is discussed in paragraphs (xxxi) to (xxxvi). The second covers all other transactions within the economic entity, examples of which would include interentity sales of inventory or other assets and interentity loans. The necessary consolidation adjustments for the effects of these transactions are outlined in paragraphs (xxxvii) to (xxxix). The consolidation adjustments necessary where there is a change in the composition of the economic entity are covered in paragraphs (xl) to (xliv).

Composition of Consolidated Accounts

STANDARDS

12 **The consolidated accounts shall comprise a consolidated profit and loss account, a consolidated balance sheet, a consolidated statement of cash flows, and notes thereto.**

13 **A parent entity shall include in the consolidated accounts, in an aggregated form and subject to such adjustments as may be necessary under this Standard, the information contained in the accounts of each of its subsidiaries as from the date on which the parent entity obtains control of each of the subsidiaries until such time as the parent entity ceases to control each of the subsidiaries.**

14 **Consolidated accounts shall be presented for the same financial year for which the parent entity's accounts are presented and shall contain comparative amounts for the preceding corresponding financial year.**

15 **The comparative amounts required under paragraph 14 shall not be adjusted for the effects of transactions which have taken place during the current financial year, except in so far as reclassification would assist comparison, but shall, where practicable, reflect the results of the economic entity for the preceding corresponding financial year and the financial position of the economic entity in existence as at the end of that financial year.**

Reporting dates

COMMENTARY

(xxix) The requirement to prepare and present consolidated accounts for the same financial year for which the parent entity's accounts are presented may necessitate the preparation of interim accounts in respect of a subsidiary or such other appropriate adjustments as may be necessary to prepare consolidated accounts as if the reporting dates were the same.

Accounting policies

STANDARDS

16 **The accounting policies employed in the preparation and presentation of consolidated accounts shall be consistent.**

17 **Where the accounting policies adopted by entities within the economic entity are dissimilar and are not required by another Accounting Standard, adjustments to achieve consistency shall be made in preparing the consolidated accounts.**

COMMENTARY

(xxx) Since the consolidated accounts provide financial information about an economic entity as a single reporting entity, consistent accounting policies need to be adopted in the preparation of those accounts. Where the accounting policies adopted by entities within the economic entity are dissimilar, adjustments need to be made in preparing the consolidated accounts to achieve consistency, unless the dissimilar policies were required by Accounting Standards. An example of dissimilar policies required by Accounting Standards is the differing measurement bases for investments pursuant to Accounting Standard AASB 1023: Financial Reporting of General Insurance Activities. Examples of dissimilar accounting policies necessitating adjustment in preparing consolidated accounts include the use by an overseas subsidiary of policies that are not permitted by Accounting Standards, such as the net-of-tax method of tax-effect accounting or an inventory valuation method like last-in-first-out. However, where alternative accounting methods or treatments are currently available within an entity, for instance differing depreciation or inventory valuation methods, the use of both within an economic entity would necessitate an adjustment only where they were not applied on a consistent basis within like segments or for similar classes of assets and there was a material effect.

Parent Entity Holds an Ownership Interest in a Subsidiary

STANDARDS

18 **In preparing the consolidated accounts where the parent entity holds an ownership interest in a subsidiary, the investment in the subsidiary shall be eliminated in full together with the parent entity's corresponding entitlement to the subsidiary's equity as at the date of acquisition.**

19 **Where elimination of the investment in the subsidiary and the parent entity's corresponding entitlement to the subsidiary's equity gives rise to a difference on consolidation, such difference shall be accounted for in accordance with Accounting Standards AASB 1013: Accounting for Goodwill and AASB 1015: Accounting for the Acquisition of Assets.**

20 **Where the net assets of the subsidiary are revalued in the accounting records of the subsidiary to their fair values as at the date on which the parent entity acquired its investment, the resulting revaluation reserve shall, in the consolidated accounts, be attributed to the outside equity interest to the extent that it reflects increments or decrements in asset values that can be attributed to the outside equity interest.**

21 **Where an adjustment is made on consolidation to revalue the net assets of the subsidiary to their fair values as at the date on which the parent entity acquired its investment and to recognise goodwill (if any), adjustments shall be made on consolidation:**

(a) **to the depreciation and amortisation expenses recognised by the subsidiary in relation to assets subject to depreciation or amortisation, so as to reflect the expenses to the economic entity;**

(b) **in eliminating the equity balances of the subsidiary in accordance with paragraph 18; and**

(c) **to attribute the remaining revaluation reserve, if any, to the outside equity interest.**

22 **Where an asset is disposed of, the carrying amount of which has been adjusted on consolidation in accordance with paragraph 19, the resulting gain or loss to the subsidiary shall be adjusted on consolidation to reflect the gain or loss to the economic entity, with a corresponding adjustment on consolidation in eliminating the equity balances of the subsidiary in accordance with paragraph 18.**

COMMENTARY

(xxxi) While preparation of the consolidated accounts is a relatively straightforward aggregation process where the relationship between entities within the economic entity is limited to a control relationship and there are no transactions between the entities, consolidation adjustments are necessary where the parent entity holds an ownership interest in a subsidiary. In the private sector it is common for a parent entity to hold an ownership interest in a subsidiary since, typically, a parent entity's control of a subsidiary is derived from a majority voting interest in the subsidiary stemming from the holding of an ownership interest in that entity.

(xxxii) Where a parent entity holds an ownership interest in a subsidiary, the investment account reflected in the parent entity's accounts represents the cost of acquiring a share of the subsidiary's equity. Consequently, when combining the individual accounts to prepare the consolidated accounts, a consolidation adjustment will need to be made to eliminate the investment account together with the corresponding portion of the investee's equity balances as at the date of acquisition. Any difference arising from the adjustment would need to be accounted for on consolidation in accordance with Accounting Standards AASB 1013: Accounting for Goodwill and AASB 1015: Accounting for the Acquisition of Assets. This would mean that the net assets acquired would need to be recognised at fair value or, where applicable, at fair value less any discount on acquisition. This may necessitate adjustments to the carrying amounts of assets which are not normally revalued, for example, inventory.

(xxxiii) Where the assets of the subsidiary are recognised at amounts which differ from their fair values as at the date of acquisition, there are two approaches to recognising the necessary adjustments. These are:

(a) to revalue the identifiable assets in the accounting records of the subsidiary; or

(b) to recognise the necessary adjustments on consolidation.

(xxxiv) Under the first approach, all of the non-current assets of the subsidiary would be revalued to their fair values in the accounting records of the subsidiary in accordance with Accounting Standard AASB 1010: Accounting for the Revaluation of Non-current Assets. The portion of the resulting revaluation reserve which is not eliminated on consolidation as pre-acquisition equity would need to be attributed to the outside equity interest. Where an adjustment is necessary to write down the carrying amount of inventory this would need to be processed in the accounting records of the subsidiary in accordance with Accounting Standard AASB 1019: Measurement and Presentation of Inventories in the Context of the Historical Cost System.

(xxxv) Under the second approach, in preparing the consolidated accounts, an adjustment would be processed to eliminate the investment and the corresponding equity in the subsidiary and to recognise any increments or decrements necessary to restate the carrying amounts of the identifiable net assets acquired to their fair values as at the date of acquisition. That portion of the identifiable non-current assets of the subsidiary attributed to any outside equity interest would also need to be revalued to fair values as at the date of acquisition. This would ensure that the subsidiary's assets recognised in the consolidated accounts are measured on a consistent basis as at the date of acquisition. The resulting revaluation reserve would need to be attributed to the outside equity interest.

(xxxvi) Where an adjustment is made on consolidation to revalue the net assets of the subsidiary on the basis of their fair values at acquisition and these assets are subject to depreciation or amortisation, an adjustment will also need to be made on consolidation to ensure that the depreciation and amortisation expenses reflect the revisions in the carrying amounts and thereby correctly reflect the depreciation and amortisation expenses to the economic entity. Since the cost incurred by the parent entity when acquiring the assets of the subsidiary reflects the profit-making potential of the assets, the component of retained profits or accumulated losses which is pre-acquisition in nature will be increased or decreased as the assets acquired are used and as depreciation or amortisation expense is recognised. Therefore, to the extent of the parent entity's ownership interest in the subsidiary, the consolidation adjustments to depreciation and amortisation affect the equities of the subsidiary which are in the nature of pre-acquisition equities and an appropriate adjustment would need to be made on consolidation in eliminating these equities. Similarly, where an asset is disposed of, the carrying amount of which has been adjusted on consolidation, the resulting gain or loss to the subsidiary would need to be redetermined from the viewpoint of the economic entity and, on consolidation, adjusted accordingly. This adjustment would constitute the realisation of pre-acquisition equities and an adjustment would need to be made on consolidation in eliminating pre-acquisition equities. These adjustments are illustrated in Appendix 1 of this Standard.

Transactions within the Economic Entity

STANDARDS

23 **In preparing the consolidated accounts, the effects of all transactions between entities within the economic entity shall be eliminated in full.**

COMMENTARY

(xxxvii) When preparing the consolidated accounts, the financial effects of transactions between entities within the economic entity need to be eliminated on consolidation. This is to enable the economic entity to be reflected as a single reporting entity, since, for financial reporting purposes, an entity cannot transact with itself. This will be the case irrespective of whether an ownership interest is held. The entity concept of consolidation, whereby the economic entity comprises the parent entity and its subsidiaries, is adopted in this Standard. Consistent with this concept the financial effects of transactions between entities within the economic entity, irrespective of an outside equity interest, need to be eliminated in full since they are wholly within the economic entity. In combining the accounts of the parent entity and its subsidiaries to prepare the consolidated accounts, the effects of these transactions would be eliminated by reversing, as consolidation adjustments, the original accounting entries made to recognise the transactions.

(xxxviii) To the extent that a balance is outstanding at the end of the current financial year and has resulted from a transaction within the economic entity in a previous financial year, such balances would need to be eliminated in preparing the consolidated accounts. This would include, for example, loans between a parent entity and a subsidiary and the transfer within the economic entity of an asset which remains on hand at the end of the current financial year at an amount different from the original cost to the economic entity. Where such a transaction gives rise to a profit or loss which at the end of the financial year remains unrealised with respect to a party external to the economic entity, the unrealised profit or loss would need to be eliminated. The profit or loss would become realised when the asset on which the profit or loss accrued is sold to a party external to the economic entity or as the future benefits embodied in the asset are consumed by the economic entity.

(xxxix) Adjustments may need to be made for the tax-effect of transactions eliminated in preparing the consolidated accounts. Profits and losses which are unrealised with respect to the economic entity may be realised in the accounting records of the entity making the sale and therefore may be subject to income tax. Since the income tax relates to results which will not be reported in consolidated accounts until subsequent financial years, the relevant tax expense needs to be determined and accounted for in the consolidated accounts in accordance with Accounting Standard AASB 1020: Accounting for Income Tax (Tax-effect Accounting).

Reciprocal Ownership Interests within the Economic Entity

STANDARDS

24 **In preparing the consolidated accounts, where two entities within the economic entity each hold an ownership interest in one another, the amounts of the interentity investments shall be eliminated.**

25 **In the circumstances set out in paragraph 24, in allocating the equity of the economic entity between the ownership group of the parent entity and the outside equity interest, the respective percentage ownership interests shall be determined after negating the effect of the interrelationship between the entities within the economic entity.**

Loss of Control of a Subsidiary

STANDARDS

26 **Subject to paragraph 27, where a parent entity ceases to control a subsidiary, information relating to that subsidiary shall, as from the date when control ceases, be excluded from any** consolidated accounts prepared by that parent entity.

27 **Where a parent entity's loss of control of a subsidiary occurs during a financial year, the consolidated profit and loss account shall include the results of the subsidiary for that part of the financial year during which the parent entity had control of the subsidiary.**

COMMENTARY

(xl) A parent entity may cease to control a subsidiary without selling an ownership interest in the subsidiary. Where such a loss of control occurs, that former subsidiary would need to be excluded, as from the date when control ceases, from any consolidated accounts prepared by the parent entity. This would necessitate including in the consolidated profit and loss account the results of the subsidiary for only that part of the current financial year during which the parent entity had control of the subsidiary. In presenting the appropriation of profits in the consolidated profit and loss account, the opening balance of retained profits or accumulated losses will need to be consistent with the closing balance for the previous financial year. To achieve this, it will be necessary to make an adjustment on consolidation to include the retained profits or accumulated losses of the former subsidiary recognised during those previous financial years during which it was a subsidiary of the parent entity. A similar adjustment will be necessary in relation to post-acquisition movements in reserves of the former subsidiary. The subsidiary would then be deconsolidated by the economic entity recognising an expense or revenue for the current financial year to reflect the loss or gain to the economic entity as a result of the parent entity's loss of control of the equity of that entity. This consolidation adjustment is illustrated in Appendix 2 of this Standard.

Sale of an Ownership Interest in a Subsidiary

STANDARDS

28 **Where an entity sells some or all of the ownership interest in another entity within the economic entity and the parent entity thereby loses control of that subsidiary, the gain or loss recognised on the sale shall, in preparing the consolidated accounts, be adjusted by the net post-acquisition movement to the date of sale in the retained profits or accumulated losses and reserves of the subsidiary.**

COMMENTARY

(xli) When entities within the economic entity sell some or all of the ownership interest in a subsidiary and the parent entity thereby loses control of that subsidiary, the gain or loss recognised on the sale will need to be adjusted when preparing the consolidated accounts so as to reflect the gain or loss to the economic entity. The gain or loss to the economic entity is the amount by which the economic entity is better or worse off as a result of the sale of the ownership interest and would be determined as the difference between the proceeds of sale and the initial cost of that portion of the ownership interest sold adjusted for post-acquisition movements in any equities in relation to which the parent entity loses control upon sale of the ownership interest. Appendix 2 illustrates this consolidation adjustment.

STANDARDS

29 **Where an entity sells some or all of the ownership interest in another entity within the economic entity and the parent entity retains control of that subsidiary, the gain or loss recognised on the sale shall, in preparing the consolidated accounts, be adjusted by the net pre-acquisition retained profits or accumulated losses and reserves of the subsidiary relating to the portion of the ownership interest sold.**

COMMENTARY

(xlii) Where some or all of the ownership interest in a subsidiary is sold but the parent entity retains control, the subsidiary would continue to be part of the economic entity and the accounts of the subsidiary would continue to be included in the consolidated accounts. The gain or loss recognised on the sale would be carried forward on consolidation rather than being eliminated, because the parent entity's retention of control of the subsidiary means that the information contained in the accounts of the subsidiary will continue to be included in the consolidated accounts. In addition, there will be an increase or decrease in the operating profit of the economic entity arising from pre-acquisition profits or losses and reserves which previously were eliminated on consolidation now being attributable to the outside equity interest. This will result in a total increase in the assets of the economic entity equal to the amount of the sale proceeds. In disclosing the operating profit and equity amounts attributable to the parent entity and to the outside equity interest, the consolidated accounts would need to reflect the proportionate decrease in the equity of the subsidiary held by the parent entity and the corresponding increase in the amount attributed to the outside equity interest. This consolidation adjustment is illustrated in Appendix 2 of this Standard.

Acquisition of an Additional Ownership Interest in a Subsidiary

STANDARDS

30 **Where a parent entity increases its ownership interest in a subsidiary through the acquisition of additional capital of the subsidiary, the acquisition shall, as at the date of acquisition, be accounted for separately from previous acquisitions of ownership interests in the subsidiary and, in preparing the consolidated accounts, the standards set out in paragraphs 18 to 22 shall be applied in respect of the amount of the additional investment.**

COMMENTARY

(xliii) Where a parent entity increases its ownership interest in a subsidiary through the acquisition of additional capital of the subsidiary, the acquisition is accounted for separately from previous acquisitions relating to the subsidiary. The necessary consolidation adjustments, including separate determination and recognition of the fair values of the net assets of the subsidiary and any goodwill/discount arising on the acquisition, would need to be made in accordance with the principles contained in paragraphs (xxxi) to (xxxvi). However, any resulting revaluation reserve which is not eliminated on consolidation as pre-acquisition equity would need to be attributed to the outside equity interest, except to the extent that it relates to the holding by the parent entity of an ownership interest in the subsidiary which was acquired prior to the above-mentioned acquisition.

New Issue of Capital by a Subsidiary

STANDARDS

31 **Where a subsidiary makes a new issue of capital, the share of retained profits or accumulated losses and reserves attributed to the parent entity and to the outside equity interest shall reflect the parent entity's ownership interest after the issue of the capital.**

COMMENTARY

(xliv) Where a subsidiary makes a new issue of capital, the only effect on the consolidated accounts will be an increase in the equity of the economic entity, to the extent that the issue of capital was subscribed by outside equity interests, and a corresponding increase in cash or other assets. The economic entity will not experience any movement in its retained profits or accumulated losses as a result of the capital issue. However, the parent entity may make a gain or loss by not maintaining its proportionate ownership interest in the subsidiary, and an equivalent loss or gain would be borne by the outside equity interest. In determining such gains and losses, the respective shares of the capital, retained profits or accumulated losses, and reserves of the economic entity that can be attributed to the parent entity and to the outside equity interest would need to be considered before and after the new issue of capital.

Outside Equity Interest

STANDARDS

32 **Where there exists an outside equity interest in the economic entity, it shall be described as such and disclosed as an equity item in the consolidated balance sheet, disclosing separately the capital, retained profits or accumulated losses and reserves comprising that amount.**

33 **Outside equity interest shall be determined as the aggregate of the equity of subsidiaries, other than that held either directly or indirectly by the ownership group of the parent entity, after making adjustments for unrealised profits and losses of subsidiaries and such other adjustments as may be necessary to comply with the standards set out in this Standard.**

34 **Where there exists an outside equity interest there shall be disclosed separately that portion of the operating profit or loss and extraordinary items after income tax of the economic entity for the financial year which can be attributed to outside equity interests.**

COMMENTARY

(xlv) Under the strict application of the entity concept of consolidation, the consolidated balance sheet would reflect the aggregate equity components of the economic entity without regard to the identity of the ownership group of the economic entity. However, it is considered relevant to disclose the amount of equity attributable to the parent entity shareholders and to the outside equity interest, disclosing separately the capital, retained profits or accumulated losses and reserves comprising each amount. This information will enable the users of the consolidated accounts to determine the aggregate capital, retained profits or accumulated losses and reserves of the economic entity.

(xlvi) The amount disclosed as being attributable to the outside equity interest would need to be determined as the aggregate of the respective proportionate shares in the equity of subsidiaries, after making adjustments for unrealised profits and unrealised losses of subsidiaries and such other adjustments as may be necessary to comply with the standards set out in this Standard. Where the outside equity interest is a negative amount it would be disclosed as an equity item of the outside equity interest, except to the extent that the parent entity agrees to bear the responsibility for outgoings resulting from the accumulated losses, in which case the item would be allocated to the parent entity shareholders.

Consolidated Profit and Loss Account

STANDARDS

35 **The consolidated profit and loss account shall disclose the results of the economic entity for the financial year and shall be prepared in accordance with Accounting Standard AASB 1018: Profit and Loss Accounts.**

Consolidated Balance Sheet

STANDARDS

36 **The consolidated balance sheet shall disclose the assets, liabilities and equities of the economic entity, as at the reporting date.**

Consolidated Statement of Cash Flows

STANDARDS

37 **The consolidated statement of cash flows shall disclose the cash flows of the economic entity for the financial year and shall be prepared on the basis set out in Accounting Standard AASB 1026: Statement of Cash Flows.**

38 **In preparing a consolidated statement of cash flows, amounts included in respect of the economic entity, especially in relation to subsidiaries entering or leaving the economic entity, shall be determined in accordance with the standards set out in this Standard.**

Additional Disclosures

STANDARDS

39 **The consolidated accounts shall disclose, by way of note:**

(a) **the identity of the parent entity within the economic entity and, if this economic entity is part of one or more larger economic entities, the identity of the ultimate parent entity in Australia and, if different, the identity of the ultimate parent entity;**

(b) **the identity and, where applicable, country of incorporation of each subsidiary within the economic entity, indicating those which have become part of the economic entity during the financial year;**

(c) **the identity of any entity which has ceased to be part of the economic entity during the financial year, the ownership interest, if any, which the parent entity retains in that entity and the aggregate gain or loss for the economic entity arising from those cessations;**

(d) **the identity of any subsidiary in which the parent entity holds an ownership interest and/or voting rights of 50 per cent or less, together with an explanation of how control exists;**

(e) **the identity of any entity in which the parent entity holds an ownership interest of more than 50 per cent but which is not a subsidiary of that parent entity, together with an explanation of why control does not exist; and**

(f) **the respective gain or loss, if any, made by the parent entity and the outside equity interest on new issues of shares by subsidiaries.**

Transitional Provisions

STANDARDS

40 **Where the accounting policies required by this Standard are not already being applied as at the beginning of the financial year to which this Standard is first applied, they shall be applied as at that date. Subject to paragraphs 41 to 43, where this gives rise to initial adjustments, the net amount of those adjustments shall, in accordance with Accounting Standard AASB 1018: Profit and Loss Accounts, be adjusted against retained profits or accumulated losses as at the beginning of the financial year to which this Standard is first applied.**

41 **Where the application of this Standard as at the beginning of the financial year to which this Standard is first applied causes the composition of the economic entity previously reflected in the group accounts or consolidated accounts to change so as to include or exclude an entity or entities:**

(a) **the identity of that entity or those entities shall be disclosed;**

(b) **the aggregate increases in assets, liabilities and equities of the economic entity caused by the inclusion or**

exclusion of entities shall be separately disclosed as at the beginning of that financial year;

(c) **the aggregate decreases in assets, liabilities and equities of the economic entity caused by the inclusion or exclusion of entities shall be separately disclosed as at the beginning of that financial year; and**

(d) **the standards set out in paragraphs 19 to 22 of this Standard shall be complied with to the extent practicable in relation to such included or excluded entities, and any resulting revenue or expense shall be adjusted against retained profits or accumulated losses as at the beginning of that financial year.**

42 **Where retrospective application of the standards set out in paragraphs 19 to 22 of this Standard is not practicable, the amounts attributed to the net assets of the subsidiary and any goodwill on consolidation thereof shall be deemed to have been determined in accordance with this Standard.**

43 **Where:**

(a) **the application of this Standard as at the beginning of the financial year to which this Standard is first applied does not cause the composition of the economic entity previously reflected in the group accounts to change so as to include or exclude an entity or entities;**

(b) **consolidated accounts were not prepared in accordance with the standards set out in this Standard for the preceding corresponding financial year; and**

(c) **the comparative amounts for the preceding corresponding financial year have not been adjusted to reflect the results of the economic entity for that financial year and the financial position of the economic entity in existence as at the end of that financial year;**

the aggregate assets, liabilities and equities of the economic entity in existence as at the beginning of the financial year to which this Standard is first applied shall be separately disclosed in the consolidated accounts for the financial year.

COMMENTARY

(xlvii) The condition set out in paragraph 43(b), that consolidated accounts were not provided for the preceding comparative financial year, will be satisfied when, for example, group accounts for that financial year were presented in a form other than one consolidation. "Consolidated accounts" are to be presented as one set of accounts, on the basis of the definition in the Corporations Law and the standards set out in this Standard. When paragraph 43 applies, the consolidated accounts for the financial year to which this Standard is first applied need to disclose the nominated aggregate comparative amounts determined as if this Standard had been applied to those amounts. Paragraph 43 does not apply when, for example, the comparative amounts are adjusted in accordance with paragraph 15.

APPENDIX 1

REALISATION OF PRE-ACQUISITION EQUITIES ARISING FROM DISPOSAL OR USE OF ASSETS REVALUED ON CONSOLIDATION

This Appendix forms part of the commentary and is provided for illustrative purposes only. The examples in this Appendix illustrate the accounting treatment outlined in paragraph (xxxvi) of this Standard concerning the realisation of pre-acquisition equities arising from the disposal or use of assets which are revalued on consolidation.

Disposal of Non-depreciable Assets

Example: The parent entity acquires all of the shares of another entity for $120,000, thereby gaining control of that entity. As at the date of acquisition the subsidiary had share capital of $80,000, retained profits of $10,000 and other reserves of $20,000. The subsidiary held land which, at the date of acquisition, had a fair value of $26,000, being an excess of $10,000 over its carrying amount of $16,000.

Where the asset is revalued on consolidation, the following journal entry would need to be made on consolidation to record the elimination of the investment and the pre-acquisition equities of the subsidiary:

	DR	CR
	$	$
Share Capital	80,000	
Retained Profits		
(Opening Balance)	10,000	
Other Reserves	20,000	
Land	10,000	
Shares in Subsidiary		120,000

Assume that two years after acquisition the subsidiary sells the land for $42,000 and recognises a gain of $26,000 in its accounting records. In preparing the consolidated accounts, the above journal entry would need to be amended to reflect that the land is no longer held and that, of the $26,000 gain on sale recognised in the current financial year, the gain on sale to the economic entity is only $16,000. This is because the fair value of the land at acquisition was $10,000 in excess of the carrying amount and this was reflected in the purchase consideration. Hence, the sale of the land at a gain has caused the component of retained profits which is in the nature of pre-acquisition profits to be increased. On consolidation the following journal entry to eliminate pre-acquisition equities would be necessary in the financial year in which the land is sold:

	DR $	CR $
Share Capital	80,000	
Retained Profits		
(Opening Balance)	10,000	
Other Reserves	20,000	
Gain on Sale of Land	10,000	
Shares in Subsidiary		120,000

In subsequent financial years the following journal entry on consolidation would be necessary, assuming no other adjustments:

	DR $	CR $
Share Capital	80,000	
Retained Profits		
(Opening Balance)	20,000	
Other Reserves	20,000	
Shares in Subsidiary		120,000

Use of Depreciable Assets

The above example shall now be varied to illustrate the effect on pre-acquisition equities where the subsidiary's asset which is revalued on consolidation is a depreciable asset.

Example: Assume the same as for the previous example except that rather than land being held, the subsidiary has plant and machinery which is carried at $16,000 but has a fair value at the date of acquisition of $26,000. This asset is considered to have a depreciable life of ten years as from the date of acquisition.

A portion of the profit generated through the economic entity's use of the asset is pre-acquisition profit in that, on acquisition, the parent entity recognised the profit-making potential of the asset by paying more for it than the carrying amount in the subsidiary's accounting records. Hence, as the asset is being used and depreciation expense recognised, the component of retained profits which is in the nature of pre-acquisition profits is increased. At the end of the first year after acquisition, the following journal entry on consolidation would be necessary to reflect this:

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	DR $	CR $
Share Capital	80,000	
Retained Profits (Opening Balance)	10,000	
Other Reserves	20,000	
Plant and Machinery	10,000	
Depreciation	1,000	
Accumulated Depreciation		1,000
Shares in Subsidiary		120,000

In the next financial year the following journal entry on consolidation would be necessary, assuming no other adjustments:

	DR $	CR $
Share Capital	80,000	
Retained Profits (Opening Balance)	11,000	
Other Reserves	20,000	
Plant and Machinery	10,000	
Depreciation	1,000	
Accumulated Depreciation		2,000
Shares in Subsidiary		120,000

APPENDIX 2

LOSS OF CONTROL OF A SUBSIDIARY
AND/OR SALE OF AN OWNERSHIP INTEREST IN A SUBSIDIARY

This Appendix forms part of the commentary and is provided for illustrative purposes only. The examples in this Appendix illustrate the accounting treatment outlined in paragraphs (xl), (xli) and (xlii) of this Standard concerning the accounting treatment in the consolidated accounts of a loss of control of a subsidiary and a sale of an ownership interest in a subsidiary.

Loss of Control

Paragraph (xl) deals with the accounting treatment necessary on consolidation where a parent entity loses control of a subsidiary without selling an ownership interest in the subsidiary, that former subsidiary thereafter being excluded from the consolidated accounts of the parent entity.

Example: The parent entity obtains control of a subsidiary on 1 January 19X1 and loses control on 30 June 19X2. During the financial year ended 31 December 19X1 the subsidiary contributed $100,000 to the retained profits of the economic entity and a further $30,000 for the six months ended 30 June 19X2. During 19X1 the subsidiary revalued certain classes of non-current assets, with a revaluation increment of $20,000 recognised in reserves.

In preparing the consolidated accounts for the financial year ended 31 December 19X2, the following journal entry would be necessary on consolidation. This entry would reinstate the opening balance of the retained profits and reserves of the economic entity so as to include the retained profits and movements in reserves of the former subsidiary recognised during those previous financial years during which it was a subsidiary of the parent entity and would recognise the results of the entity for the six-month period ended 30 June 19X2 during which it was a subsidiary of the parent entity, with a corresponding adjustment against the profits of the economic entity to reflect the parent entity's loss of control of the equity of the former subsidiary:

	DR $	CR $
Operating Profit (Loss of Subsidiary)	150,000	
Retained Profits (Opening Balance)		100,000
Asset Revaluation Reserve (Opening Balance)		20,000
Operating Profit		30,000

Sale of All of the Ownership Interest and Loss of Control

Paragraph (xli) deals with the determination of the gain or loss to the economic entity when the parent entity sells some or all of its ownership interest in a subsidiary and in so doing loses control of that entity.

Example: The parent entity acquired a 100% ownership interest in a subsidiary on 1 January 19X1 for $100,000. On 30 June 19X3 the parent entity sold its ownership interest in the subsidiary for $300,000, and simultaneously lost control. During 19X1 and 19X2 the subsidiary contributed $140,000 to the retained profits of the economic entity. The operating profit of the subsidiary for the six months ended 30 June 19X3 was $40,000.

In preparing the consolidated accounts for the financial year ended 31 December 19X3, the gain on sale of $200,000 recognised by the parent entity would need to be adjusted to reflect the gain or loss to the economic entity on sale of the ownership interest. The gain or loss to the economic entity would be determined as the difference between the sale price of $300,000 and the original cost of $100,000 increased by $180,000, being the profits of the subsidiary recognised since the parent entity acquired its ownership interest. Hence, the gain to the economic entity on the sale of the subsidiary would be $20,000. The following journal entry would be necessary on consolidation:

	DR $	CR $
Gain on Sale	180,000	
Retained Profits (Opening Balance)		140,000
Operating Profit		40,000

Sale of Part of the Ownership Interest and Loss of Control

The above example, in which it was assumed that the sale of the parent entity's total ownership interest in a subsidiary and the loss of control were simultaneous, shall now be varied to illustrate the accounting treatment where some, but not all, of the ownership interest is sold and control is lost simultaneously.

Example: The parent entity acquired a 100% ownership interest in a subsidiary on 1 January 19X1 for $100,000. On 30 June 19X3 the parent entity sold 80% of its ownership interest in the subsidiary for $240,000, and simultaneously lost control. During 19X1 and 19X2 the subsidiary contributed $140,000 to the retained profits of the economic entity. The operating profit of the subsidiary for the six months ended 30 June 19X3 was $40,000.

In preparing the consolidated accounts for the financial year ended 31 December 19X3, the gain on sale of $160,000 recognised by the parent entity (being the sale price of $240,000 less the carrying amount of $80,000) would need to be adjusted to reflect the gain or loss to the economic entity on sale of the ownership interest since control of the subsidiary has been lost. The gain or loss to the economic entity would be determined as the difference between the sale price ($240,000) and the sum of the original cost of the ownership interest sold ($80,000) and the post-acquisition profits contributed to the economic entity by that 80% ownership interest in the subsidiary ($144,000). This results in a gain to the economic entity of $16,000 ($240,000 less $224,000), thus necessitating a reduction of $144,000 in the parent entity's recognised gain of $160,000.

Upon the parent entity's loss of control, the consolidated accounts could not include aggregation of the accounts of the former subsidiary. However, since that entity was part of the economic entity for part of the current financial year the opening balance of retained profits, as derived from aggregating the accounts of the entities comprising the economic entity at the end of the financial year, will need to be increased to reflect the former subsidiary's opening balance, that is, $140,000. (Note that it will be $140,000 and not 80% of this amount, since these are the profits that were able to be included in the consolidated accounts when the entity was part of the economic entity.) Similarly, the economic entity will need to reflect all of the profits of the subsidiary for the period to the loss of control of the subsidiary. Furthermore, because the consolidated accounts are compiled on the basis of control rather than ownership interest, all of the profits of the subsidiary must then be excluded from consolidation when the parent entity loses control. Therefore, the remaining $36,000 profits contributed by the subsidiary which have not been adjusted against the gain on sale will need to be deconsolidated. The following journal entry would be necessary in preparing the consolidated accounts:

	DR	CR
	$	$
Gain on Sale	144,000	
Operating Profit		
(Loss of Subsidiary)	36,000	
Retained Profits		
(Opening Balance		140,000
Operating Profit		40,000

Sale of Part of the Ownership Interest and Retention of Control

The following example illustrates the accounting treatment necessary on consolidation where a parent entity sells some or all of its ownership interest in a subsidiary but retains control of that subsidiary. Discussion of this is contained in paragraph (xlii) of the Standard.

Example: The parent entity acquired a 100% ownership interest in a subsidiary on 1 January 19X3 for $100,000, at which date the subsidiary's equity consisted of share capital of $80,000 and retained profits of $20,000. On 31 December 19X4 the parent entity sold 25% of its ownership interest in the subsidiary for $35,000. The parent entity retained control of the subsidiary after the sale. During 19X3 the parent entity and the subsidiary recognised profits of $15,000 and $40,000 respectively.

Assume that the balance sheets of the parent entity and the subsidiary are as follows:

Parent Entity Balance Sheet as at 31 December 19X3

		$		$
Share Capital		90,000	Cash	90,000
Retained Profits				
(Opening Bal)	85,000		Shares in	
Operating Profit	15,000	100,000	Subsidiary	100,000
		190,000		190,000

Subsidiary Balance Sheet as at 31 December 19X3

		$		$
Share Capital		80,000	Cash	70,000
Retained Profits				
(Opening Bal)	20,000			
Operating Profit	40,000	60,000	Other Assets	70,000

	140,000	140,000

In preparing the consolidated accounts for the financial year ended 31 December 19X3, the following journal entry would be necessary to eliminate the investment held by the parent entity at 31 December 19X3 and the corresponding pre-acquisition equity of the subsidiary:

	DR $	CR $
Share Capital	80,000	
Retained Profits (Opening Balance)	20,000	
Shares in Subsidiary		100,000

This would give rise to the following consolidated balance sheet:

Consolidated Balance Sheet as at 31 December 19X3

		$		$
Share Capital		90,000	Cash	160,000
Retained Profits				
(Opening Bal)	85,000			
Operating Profit	55,000	140,000	Other Assets	70,000
		230,000		230,000

Assume that during 19X4 the parent entity and subsidiary both recognised profits of $15,000. The parent entity's profit includes a gain of $10,000 on the sale of a 25% ownership interest in the subsidiary for $35,000. The balance sheets of the parent entity and subsidiary would be as follows:

Parent Entity Balance Sheet as at 31 December 19X4

		$		$
Share Capital		90,000	Cash	130,000
Retained Profits				
(Opening Bal)	100,000		Shares in	
Operating Profit	15,000	115,000	Subsidiary	75,000
		205,000		205,000

Subsidiary Balance Sheet as at 31 December 19X4

		$		$
Share Capital		80,000	Cash	85,000
Retained Profits				
(Opening Bal)	60,000			
Operating Profit	15,000	75,000	Other Assets	70,000

	155,000	155,000

In preparing the consolidated accounts for the financial year ended 31 December 19X4, the following journal entry would be necessary to eliminate the investment held by the parent entity at 31 December 19X4 and the corresponding pre-acquisition equity of the subsidiary:

	DR	CR
	$	$
Share Capital	60,000	
Retained Profits		
(Opening Balance)	20,000	
Operating Profit		
(Gain to economic entity)		5,000
Shares in Subsidiary		75,000

The debit of $20,000 restates the opening balance of the consolidated retained profits to the amount recognised in the consolidated balance sheet at the end of 19X3. The $20,000 represents the retained profits of the subsidiary as at 1 January 19X3, the date of acquisition of the ownership interest by the parent entity.

The credit of $5,000 represents 25% of the $20,000 pre-acquisition retained profits which are now attributable to the outside equity interest and no longer eliminated on consolidation. The credit entry thus represents a gain to the economic entity arising from the sale of the ownership interest by the parent entity, and does not relate to either the gain/loss for the ownership group of the parent entity pursuant to the sale or the parent entity's reported profit.

In future financial years, the debit to retained profits and the credit to operating profit would be combined because the $5,000 credit will be included in the closing balance of consolidated retained profits for the financial year in which the ownership interest is sold.

Note that only $75,000 of the subsidiary's pre-acquisition equity has been eliminated by the journal entry, compared with $100,000 at the end of the previous financial year. This is because $25,000 of the subsidiary's pre-acquisition equity has now been acquired by the outside equity interest, thus resulting in a $25,000 increase in the equity of the economic entity. This $25,000 comprises $20,000 capital of the subsidiary and the $5,000 relating to pre-acquisition profits of the subsidiary (25% of $20,000), which previously were eliminated on consolidation.

The equity attributable to the outside equity interest at the end of 19X4 is determined as follows:

Outside Equity Interest

		$
Share Capital	[25% of $80,000]	20,000
Retained Profits		
(Opening Balance)		-
Operating Profit	[25% of $75,000]	18,750
Total Equity		38,750

The outside equity interest did not exist at the beginning of 19X4 and thus has no entitlement to any part of the opening retained profits of the economic entity. The outside equity interest in the operating profit of the economic entity comprises $13,750 relating to post-acquisition profits of the subsidiary to which the outside equity interest is now entitled (being 25% of $55,000) and the $5,000 relating to pre-acquisition profits of the subsidiary (25% of $20,000) which are no longer eliminated on consolidation.

The interest of the ownership group of the parent entity in the operating profit of the economic entity for 19X4 is determined as follows:

Parent Entity Interest

	$
Parent entity's reported 19X4 profit (100% interest)	15,000
plus Subsidiary's reported 19X4 profit (100% interest)	15,000
	30,000
less Post-acquisition profits sold (25% of $55,000)	(13,750)
	16,250

The consolidated balance sheet could be presented as follows:

Consolidated Balance Sheet as at 31 December 19X4

	Parent Entity Interest	Outside Equity Interest	Economic Entity
	$	$	$
Share Capital	90,000	20,000	110,000
Retained Profits			
(Opening Balance)	140,000	-	140,000
Operating Profit	16,250	18,750	35,000
Total Equity	246,250	38,750	285,000
Cash			215,000
Other Assets			70,000
Total Assets			285,000

The consolidated operating profit of $35,000 recognised for 19X4 may be reconciled as:

	$
Parent entity's reported 19X4 profit (includes $10,000 profit on sale of 25% ownership interest in subsidiary)	15,000
Subsidiary's reported 19X4 profit	15,000
Gain to economic entity per journal entry	5,000
Consolidated operating profit for 19X4	35,000

Thus the consolidated operating profit includes a total profit of $15,000 relating to the sale by the parent entity of the 25% ownership interest in the subsidiary: $10,000 through the parent entity's reported profit and the $5,000 gain to the economic entity through the journal entry. This total profit of $15,000 equals the difference between the sale proceeds of $35,000 and the $20,000 increase in the capital of the economic entity, and is reconciled between the parent entity and outside equity interests as follows:

Parent Entity Interest	$
Profit on sale recognised by parent entity	10,000
less Post-acquisition profits sold (25% of $55,000)	(13,750)
Loss to parent entity ownership group	(3,750)
Outside Equity Interest	
Post-acquisition profits acquired (25% of $55,000)	13,750
Gain re pre-acquisition retained profits	5,000
Gain ascribed to outside equity interest	18,750
Total gain to economic entity	15,000

In determining the gain or loss of the outside equity interest from the perspective of the economic entity, the $35,000 acquisition cost incurred by the outside equity interest is not taken into account as it is not a cost incurred by the economic entity.

APPENDIX 3

EXTRACTS FROM EXAMPLE CONSOLIDATED BALANCE SHEET AND EXAMPLE CONSOLIDATED PROFIT AND LOSS ACCOUNT

This Appendix forms part of the commentary and is provided for illustrative purposes only. The example does not necessarily satisfy the disclosure requirements of other Accounting Standards.

Extract from Consolidated Balance Sheet as at 30 June 19X9

	$'000	$'000
SHAREHOLDERS' EQUITY		
Parent Entity Interest		
Share Capital	2,000	
Reserves	1,000	
Retained Profits	520	3,520
Outside Equity Interest		
Share Capital	400	
Reserves	200	
Retained Profits	120	720
		4,240

Extract from Consolidated Profit and Loss Account for the year ending 30 June 19X9

	Economic Entity
	$'000
Operating profit before income tax [Note 1]	360
Income tax expense attributable to operating profit	140
Operating profit after income tax	220

	Parent Entity Interest	Outside Equity Interest
	$'000	$'000
Operating profit after income tax	180	40
Retained profits at 1 July 19X8	320	80
Aggregate of amounts transferred from reserves	100	20
Total available for appropriation	600	140
Dividends provided for or paid to:		
Parent entity shareholders	80	
Outside equity interest		20
Retained profits at 30 June 19X9	520	120

Note 1

	Parent Entity Interest	Outside Equity Interest	Economic Entity
	$'000	$'000	$'000
Operating profit before income tax has been determined after inclusion of the following items:			
Profit (loss) on a new issue of shares by a subsidiary	(9)	9	-