

Consolidated Financial Statements (IFRS 10)

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1. Overview and objective of IFRS 10

IFRS 10 *Consolidated Financial Statements* establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities.

Objective:

- **Main aim:** To require an entity that controls one or more other entities (subsidiaries) to present consolidated financial statements.
- **Single economic entity view:** Consolidated financial statements present the assets, liabilities, equity, income, expenses and cash flows of a parent and its subsidiaries as if they were a single economic entity.

Why IFRS 10 was introduced:

- **Consistency in “control” assessment:** IFRS 10 replaced the previous control guidance in IAS 27 and SIC-12, creating a single, principle-based definition of control applicable to all types of investees, including structured entities.
- **Focus on substance over form:** It emphasises the *substance* of the relationship (power, exposure to returns, and the link between them) rather than only legal ownership or majority voting rights.

2. Scope of IFRS 10

IFRS 10 applies to all entities that have one or more subsidiaries and are required (or choose) to present consolidated financial statements.

In-scope situations:

- **Parent entities:** Any entity that controls one or more subsidiaries must present consolidated financial statements, except in limited circumstances (e.g. certain parent entities that themselves are wholly-owned or investment entities—discussed later).
- **All types of investees:** Includes traditional operating subsidiaries, special purpose entities (SPEs), structured entities, and entities with complex capital structures.

Out-of-scope or exceptions (high level):

- **Investment entities:** These have a specific exception from consolidating certain subsidiaries (see Paragraph 11).
- **Some intermediate parents:** In certain cases, a parent that is itself a subsidiary may be exempt from presenting consolidated financial statements if strict conditions are met (e.g. ultimate parent produces IFRS-compliant consolidated financial statements).

3. The core principle of IFRS 10 — Control

3.1 Definition of control

IFRS 10 defines *control* as follows: an investor controls an investee when the investor:

1. **Has power** over the investee;
2. **Is exposed, or has rights, to variable returns** from its involvement with the investee; and
3. **Has the ability to use its power** over the investee to affect the amount of the investor's returns.

All three elements must be present for control to exist.

3.2 Key components of control

(a) Power over the investee

- **Meaning:** Power is existing rights that give the current ability to direct the relevant activities—those activities that significantly affect the investee's returns.
- **Sources of power:**
 - Voting rights (e.g. ordinary shares).
 - Contractual arrangements (e.g. management agreements, supply contracts).
 - Rights to appoint or remove key management or governing body members.
 - Rights embedded in laws or regulations.

(b) Exposure to variable returns

- **Variable returns:** Returns that are not fixed and can vary as a result of the investee's performance. These include:
 - Dividends and other distributions.
 - Changes in fair value of the investment.
 - Residual interests in net assets.
 - Fees, synergies, cost savings, or other benefits.
- **Negative returns:** Exposure can be positive or negative (e.g. losses, reputational risk).

(c) Ability to use power to affect returns

- **Link between power and returns:** The investor must be able to use its power to influence the investee's relevant activities in a way that affects its own returns.
- **Practical ability:** It is not enough to have power and variable returns separately; there must be a *link*—the investor can direct relevant activities and thereby influence the returns it receives.

4. Assessing power — relevant activities and rights

4.1 Relevant activities

Relevant activities are the activities of the investee that significantly affect its returns.

Examples:

- **Operating decisions:** e.g. production, sales, pricing, marketing strategies.
- **Financing decisions:** e.g. obtaining funding, managing capital structure.
- **Investment decisions:** e.g. acquiring or disposing of assets.
- **Other key policies:** e.g. risk management, hedging strategies.

The identification of relevant activities is crucial because power is defined relative to these activities.

4.2 Rights that confer power

Types of rights that may give power:

- **Substantive voting rights:**
 - Majority of voting rights in the investee.
 - Rights to direct decisions about relevant activities through voting.
- **Contractual rights:**
 - Rights to direct operating and financing policies via contracts.
 - Rights to appoint or remove key management or board members.
- **Other decision-making rights:**
 - Rights to approve budgets, business plans, or major transactions.
 - Rights to veto or approve changes in relevant activities.

4.3 Substantive vs protective rights

Substantive rights:

- **Definition:** Rights that give the holder the *practical ability* to direct relevant activities when decisions need to be made.
- **Characteristics:**
 - Exercisable when decisions about relevant activities are made.
 - Not merely theoretical; the holder can realistically exercise them (consider barriers such as financial penalties, legal restrictions, or practical obstacles).
- ❖ Example: A right to appoint the majority of board members who direct the investee's operations.

Protective rights:

- **Definition:** Rights designed to protect the interest of the holder without giving power over relevant activities.

- **Characteristics:**
 - Typically relate to fundamental changes (e.g. liquidation, major asset disposals).
 - Do not confer current ability to direct day-to-day relevant activities.
- ❖ Example: A lender's right to veto major capital expenditures to protect its loan.

Only *substantive* rights are considered when assessing power. Protective rights alone do not give control.

5. Assessing exposure to variable returns

5.1 Nature of variable returns

Variable returns arise from the investor's involvement with the investee and can include:

- **Equity returns:** Dividends, share of profits, residual interest on liquidation.
- **Fair value changes:** Gains or losses from changes in the value of the investment.
- **Fees and commissions:** Management fees, performance fees, servicing fees.
- **Synergies:** Cost savings, economies of scale, access to new markets.
- **Other benefits:** Tax advantages, access to proprietary technology, or reputational benefits.

5.2 Examples of variable returns

Example 1 — Traditional subsidiary:

- Parent holds 80% of the ordinary shares of Subsidiary A.
- Parent receives dividends and is exposed to changes in the value of its investment.
- Parent is clearly exposed to variable returns.

Example 2 — Structured entity:

- Investor sponsors a securitisation vehicle and holds residual interests.
- Investor receives residual cash flows after senior tranches are paid.
- These residual cash flows vary with the performance of the underlying assets—variable returns.

6. The link between power and returns

6.1 Combining the three elements

Control exists only when **all three elements** are present:

1. **Power over relevant activities;**

2. **Exposure to variable returns;** and
3. **Ability to use power to affect those returns.**

The assessment is holistic—no single factor is determinative. The investor must consider all facts and circumstances.

6.2 Practical examples

Example 3 — Majority voting rights with active involvement

- Parent P holds 60% of voting rights in Subsidiary S.
- P can appoint the majority of board members and approve budgets.
- P receives dividends and benefits from synergies.
- P uses its power to direct S's operations and influence returns.
- **Conclusion:** P controls S and must consolidate.

Example 4 — Majority voting rights but no relevant activities

- Investor I holds 55% of voting rights in Investee X.
- However, relevant activities are predetermined by contract and cannot be changed by voting.
- Another party (Manager M) has contractual rights to direct relevant activities.
- I receives variable returns but cannot use power to affect them.
- **Conclusion:** I does *not* control X; M may control X.

7. Special considerations in assessing control

7.1 *De facto* control (control without majority voting rights)

An investor may control an investee even without holding a majority of voting rights, if:

- Its voting rights are **sufficiently dominant** relative to other dispersed shareholders; and
- Other shareholders are not organised, do not actively participate, or have no realistic ability to outvote the investor.

Example 5 — *De facto* control:

- Investor A holds 40% of voting rights in Company B.
- The remaining 60% is widely dispersed among many shareholders, none holding more than 2%.
- Historically, only 50% of the dispersed shareholders vote at meetings.
- A's 40% effectively represents 80% of votes cast (40 / 50).
- A can direct relevant activities through its voting power.
- **Conclusion:** A may have *de facto* control and must consolidate B.

7.2 Potential voting rights

Potential voting rights (e.g. options, convertible instruments) are considered in assessing control if they are **substantive**.

- **Substantive potential voting rights:**
 - Currently exercisable or convertible.
 - The holder has an economic incentive to exercise them.
- **Non-substantive potential voting rights:**
 - Deep out-of-the-money options with no realistic chance of exercise.
 - Rights that cannot be exercised until a distant future date.

If substantive potential voting rights give the investor the current ability to direct relevant activities, they may confer control.

Example 6 — Options leading to control:

- Investor C holds 30% of voting rights in D.
- C also holds call options that are currently exercisable to acquire an additional 25%.
- The options are in-the-money and C has a strong incentive to exercise them.
- Considering these rights, C effectively has power over D.
- **Conclusion:** C may control D even before exercising the options.

7.3 Agency relationships (principal vs agent)

Sometimes a decision-maker (e.g. fund manager) has power over an investee but may be acting as an **agent** on behalf of others. IFRS 10 requires an assessment of whether the decision-maker is a **principal** (controls the investee) or an **agent** (does not control).

Factors to consider:

- **Scope of decision-making authority:**
 - What decisions can the decision-maker make?
 - Are these decisions about relevant activities?
- **Rights held by other parties:**
 - Removal rights (e.g. can other investors remove the decision-maker without cause?).
 - Participating rights in key decisions.
- **Remuneration:**
 - Is the decision-maker's remuneration commensurate with services provided?
 - Is it exposed to significant variability (e.g. performance fees)?
- **Exposure to variable returns:**
 - Does the decision-maker hold significant interests in the investee (e.g. units, shares)?

If the decision-maker is an **agent**, it does not control the investee; the principal(s) may control.

Example 7 — Fund manager as agent:

- Fund Manager FM manages Fund F's assets and has broad decision-making powers.
- Investors in F can remove FM without cause by a simple majority vote.
- FM receives a market-based fee and holds only a small investment in F.
- **Conclusion:** FM is likely an agent; the investors collectively may control F.

7.4 Structured entities and special purpose entities

Structured entities (including SPEs) often have:

- Narrow and well-defined objectives (e.g. securitisation, leasing).
- Pre-determined activities governed by contracts.
- Little or no voting rights in the traditional sense.

In such cases, control is assessed by:

- Identifying **who has power** over the relevant activities (e.g. who can change servicing arrangements, replace key service providers, or alter asset portfolios).
- Assessing **who is exposed to variable returns** (e.g. residual interest holders).
- Determining **who can use power to affect returns**.

Often, the sponsor or residual interest holder may control the structured entity.

8. Accounting requirements for consolidated financial statements

Once control is established, IFRS 10 requires the parent to prepare consolidated financial statements using the following principles.

8.1 Consolidation procedures

Step 1 — Line-by-line aggregation

- Combine the parent's and subsidiaries' assets, liabilities, equity, income, expenses and cash flows **line by line**.
- Present them as those of a single economic entity.

Step 2 — Elimination of intra-group balances and transactions

- Eliminate:
 - Intra-group receivables and payables.
 - Intra-group sales and purchases.
 - Intra-group profits and losses (e.g. unrealised profits on inventory still held within the group).

❖ Refer **Paragraph 16** for some typical consolidation spreadsheet adjustments.

Step 3 — Uniform accounting policies

- Use **uniform accounting policies** for like transactions and events in similar circumstances across the group.
- If a subsidiary uses different policies, adjust its financial statements to conform to the parent's policies.

Step 4 — Reporting date alignment

- Consolidate financial statements prepared as of the same reporting date.
- If this is not practicable, adjust for significant transactions or events between the reporting dates (subject to a maximum difference, typically not more than three months).

8.2 Non-controlling interests (NCI)

Definition: Non-controlling interests represent equity in a subsidiary not attributable, directly or indirectly, to the parent.

Presentation:

- Present NCI within equity in the consolidated statement of financial position, separately from the parent's equity.
- In the consolidated statement of profit or loss and other comprehensive income, allocate profit or loss and total comprehensive income between:
 - **Owners of the parent;** and
 - **Non-controlling interests.**

Measurement at acquisition: At the date of obtaining control, NCI can be measured using either:

- **Fair value (full goodwill method);** or
- **Proportionate share of the acquiree's identifiable net assets (partial goodwill method).**

The choice is made on a transaction-by-transaction basis (under IFRS 3), but IFRS 10 then governs the ongoing consolidation.

8.3 Changes in ownership interests without loss of control

When the parent's ownership interest in a subsidiary changes but the parent **retains control**, the transaction is accounted for as an **equity transaction**:

- **No gain or loss** is recognised in profit or loss.
- The carrying amounts of the parent's equity and NCI are adjusted to reflect the changes in ownership interests.

- Any difference between the amount by which NCI is adjusted and the fair value of the consideration paid or received is recognised directly in equity (attributable to owners of the parent).

Example 8 — Increase in ownership interest:

- Parent holds 70% of Subsidiary S and acquires an additional 10% from NCI.
- Parent still controls S (now 80%).
- The difference between consideration paid and the adjustment to NCI is recognised in equity, not profit or loss.

8.4 Loss of control

When the parent **loses control** of a subsidiary, IFRS 10 requires:

1. **Derecognition** of:
 - The assets and liabilities of the former subsidiary.
 - Any NCI related to the former subsidiary.
2. **Recognition** of:
 - Any investment retained in the former subsidiary at its **fair value** at the date of loss of control.
 - Any consideration received.
3. **Recognition of gain or loss** in profit or loss:
 - Calculated as the difference between:
 - The aggregate of fair value of consideration received and fair value of retained interest; and
 - The carrying amount of the former subsidiary's net assets and NCI at the date of loss of control.

If the retained interest becomes an associate or joint venture, it is accounted for under IAS 28 using the equity method.

Example 9 — Loss of control and retained interest:

- Parent P holds 80% of Subsidiary S.
- P sells 50% of S to an external party and retains 30%.
- P loses control (now only 30%).
- P derecognises S's assets, liabilities and NCI, recognises the retained 30% at fair value, and recognises any gain or loss in profit or loss.

9. Consolidation examples (numerical)

9.1 Basic consolidation example

Scenario:

- Parent Co acquires 75% of Subsidiary Co on 1 January 20X1.

- At acquisition date, Subsidiary Co's identifiable net assets have a fair value of R1,000.
- Consideration transferred by Parent Co is R900.
- NCI is measured at proportionate share of net assets.

Step 1 — Goodwill calculation (IFRS 3, but relevant to IFRS 10 consolidation):

- **Parent's share of net assets:**
 - $75\% \times 1,000 = 750$
- **Goodwill:**
 - Consideration (900) – Parent's share of net assets (750) = **R150**
- **NCI at acquisition:**
 - $25\% \times 1,000 = 250$

Step 2 — Consolidated statement of financial position (conceptually):

- **Assets:**
 - Parent's assets + share of Subsidiary's assets (including goodwill of 150).
- **Equity:**
 - Parent's equity.
 - NCI of 250 (presented separately).

In subsequent periods, profits of Subsidiary Co are allocated between Parent Co and NCI based on their ownership interests.

9.2 Intra-group transaction elimination

Scenario:

- Parent sells goods to Subsidiary for R100, cost R60.
- At year-end, Subsidiary still holds half of these goods in inventory.

Individual accounts:

- Parent recognises revenue R100 and cost of sales R60 (profit R40).
- Subsidiary recognises inventory R100.

Consolidation adjustments:

- **Eliminate intra-group sales:**
 - Remove R100 from group revenue and cost of sales.
- **Eliminate unrealised profit in inventory:**
 - Inventory still held: R50 (half of 100).
 - Embedded profit: $40 \times 50/100 = R20$.
 - Reduce inventory by R20 and reduce group profit by R20.

Result: Group financial statements reflect only profit realised from sales outside the group.

10. Investment entities — exception to consolidation

10.1 Definition of an investment entity

IFRS 10 introduces the concept of an **investment entity** and provides an exception from consolidating certain subsidiaries.

An **investment entity** is an entity that:

- **Obtains funds from one or more investors** for the purpose of providing them with investment management services;
- **Commits to its investors** that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and
- **Measures and evaluates** the performance of substantially all of its investments on a **fair value basis**.

Typical examples include certain investment funds (such as unit trusts), private equity funds, and venture capital organisations.

10.2 Characteristics of an investment entity

IFRS 10 provides typical characteristics (not all are mandatory, but they support the assessment):

- **Multiple investments:** Holds more than one investment.
- **Multiple investors:** Has more than one investor.
- **Unrelated investors:** Investors are not related parties of the entity.
- **Ownership interests:** Ownership interests are in the form of equity or similar interests.

An entity that lacks one or more of these characteristics may still be an investment entity if it otherwise meets the definition.

10.3 Exception to consolidation

If an entity is an **investment entity**, it **does not consolidate** its subsidiaries that are themselves investments. Instead, it measures those subsidiaries at **fair value through profit or loss** in accordance with IFRS 9.

However, an investment entity **must consolidate** subsidiaries that:

- Provide services related to the investment entity's investment activities (e.g. a subsidiary that provides investment management services).

Example 10 — Investment fund:

- Fund F meets the definition of an investment entity.

- F holds Subsidiary S1 and S2 solely for capital appreciation and investment income.
- F also owns Subsidiary M, which provides investment management services to F.
- **Accounting:**
 - S1 and S2 are measured at fair value through profit or loss (no consolidation).
 - M is consolidated because it provides investment-related services.

11. Interaction with other standards

While IFRS 10 focuses on **control and consolidation**, it interacts with several other standards:

- **IFRS 3 — Business Combinations:**
 - Governs the accounting for obtaining control (acquisition method, goodwill).
- **IFRS 12 — Disclosure of Interests in Other Entities:**
 - Requires extensive disclosures about subsidiaries, structured entities, associates, joint ventures, and unconsolidated interests.
- **IAS 28 — Investments in Associates and Joint Ventures:**
 - Applies when the investor has significant influence or *joint* control, but not control.
- **IFRS 9 — Financial Instruments:**
 - Governs measurement of investments that are not consolidated (e.g. investments held by investment entities).

12. Practical application and judgement

12.1 Importance of judgement

Applying IFRS 10 often requires **significant judgement**, especially in complex structures:

- Determining relevant activities.
- Assessing whether rights are substantive.
- Evaluating *de facto* control.
- Distinguishing principals from agents.
- Identifying investment entities.

Entities must document their assessments and revisit them when facts and circumstances change.

12.2 Reassessment of control

Control is not static. IFRS 10 requires reassessment when:

- **Changes in rights:** New contracts, amendments, or expiry of rights.
- **Changes in ownership:** Acquisitions or disposals of interests.
- **Changes in relevant activities:** New lines of business, regulatory changes.
- **Changes in involvement:** Increased or decreased exposure to variable returns.

If control is gained or lost, the entity must apply the appropriate accounting (e.g. acquisition accounting, loss of control).

13. Summary of key principles

To consolidate under IFRS 10, an entity must:

1. **Identify investees** and understand their relevant activities.
2. **Assess power:** Determine whether it has substantive rights that give current ability to direct relevant activities.
3. **Assess exposure to variable returns:** Identify how its involvement leads to variable returns.
4. **Assess the link:** Determine whether it can use its power to affect those returns.
5. **Conclude on control:** If all three elements are present, the entity controls the investee.
6. **Apply consolidation procedures:**
 - Line-by-line aggregation.
 - Elimination of intra-group balances and transactions.
 - Uniform accounting policies.
 - Proper treatment of NCI, changes in ownership, and loss of control.
7. **Consider investment entity exception:** If the entity is an investment entity, apply fair value through profit or loss for investment subsidiaries instead of consolidation.

14. Multiple-Choice Questions (with Answers)

1. IFRS 10 requires consolidated financial statements when an entity:

- A. Has significant influence over another entity
- B. Controls one or more subsidiaries
- C. Jointly controls an arrangement
- D. Holds more than 20% of voting rights

➤ **Answer: B**

2. Under IFRS 10, control exists only when the investor has:

- A. Power and majority voting rights
- B. More than 50% ownership
- C. Exposure to variable returns and protective rights
- D. Power, exposure to variable returns, and ability to use power to affect returns

➤ **Answer: D**

3. Which of the following best describes “relevant activities”?

- A. Activities that protect the interests of lenders
- B. Activities that significantly affect the investee’s returns
- C. Activities relating only to financing decisions
- D. Activities performed by the parent entity

➤ **Answer: B**

4. Protective rights:

- A. Confer control
- B. Are always substantive
- C. Do not give power over relevant activities
- D. Automatically lead to consolidation

➤ **Answer: C**

5. Substantive rights must be:

- A. Exercisable only in the future
- B. Protective in nature
- C. Capable of being exercised when decisions about relevant activities are made
- D. Held by more than one investor

➤ **Answer: C**

6. *De facto* control may exist when:

- A. The investor holds potential voting rights
- B. Other shareholders are passive and widely dispersed
- C. The investor holds protective rights
- D. The investor holds exactly 50% of voting rights

➤ **Answer: B**

7. Potential voting rights are considered in assessing control only when:

- A. They are substantive
- B. They are out-of-the-money
- C. They cannot be exercised currently
- D. They are held by multiple investors

➤ **Answer: A**

8. A decision-maker is considered a principal when:

- A. It earns only a fixed fee
- B. It can be removed easily by other investors
- C. It has significant exposure to variable returns
- D. It holds protective rights

➤ **Answer: C**

9. Consolidation requires:

- A. Line-by-line aggregation of assets, liabilities, income and expenses
- B. Only combining profit or loss
- C. Using different accounting policies for each subsidiary
- D. Presenting subsidiaries separately

➤ **Answer: A**

10. Intra-group transactions must be:

- A. Ignored
- B. Eliminated in full
- C. Eliminated only if material
- D. Eliminated only for sales of inventory

➤ **Answer: B**

11. Non-controlling interests (NCI) are presented:

- A. As liabilities
- B. As part of parent equity
- C. Within equity, separately from parent equity
- D. As revenue

➤ **Answer: C**

12. When ownership changes but control is retained, the transaction is:

- A. Recognised in profit or loss
- B. Treated as an equity transaction
- C. Accounted for as a disposal
- D. Treated as a business combination

➤ **Answer: B**

13. When control is lost, the parent must:

- A. Continue consolidating
- B. Recognise a gain or loss in equity
- C. Derecognise assets, liabilities and NCI of the subsidiary
- D. Ignore any retained interest

➤ **Answer: C**

14. A retained interest after loss of control is measured at:

- A. Carrying amount
- B. Historical cost
- C. Fair value at the date of loss of control
- D. Net asset value

➤ **Answer: C**

15. Investment entities:

- A. Must consolidate all subsidiaries
- B. Do not consolidate investment subsidiaries
- C. Cannot have subsidiaries
- D. Must use the equity method

➤ **Answer: B**

16. An investment entity measures investment subsidiaries at:

- A. Fair value through profit or loss
- B. Cost
- C. Amortised cost
- D. Equity method

➤ **Answer: A**

17. Subsidiaries providing investment-related services to an investment entity:

- A. Are measured at fair value
- B. Are not recognised
- C. Must be consolidated
- D. Must be derecognised

➤ **Answer: C**

18. Uniform accounting policies across the group are:

- A. Optional
- B. Required
- C. Required only for listed entities
- D. Required only for foreign subsidiaries

➤ **Answer: B**

19. A parent may be exempt from presenting consolidated financial statements when:

- A. It has only one subsidiary
- B. It is an intermediate parent and certain conditions are met
- C. It chooses not to consolidate
- D. Its subsidiaries are immaterial

➤ **Answer: B**

20. Control must be reassessed when:

- A. Ownership changes
- B. Relevant activities change
- C. Rights change
- D. All of the above

➤ **Answer: D**

15. Comprehensive Question Bank (with Solutions)

SECTION A — Short-Answer Questions

1. Define “power” under IFRS 10.

Solution: Power refers to existing rights that give the investor the current ability to direct the relevant activities of the investee — those activities that significantly affect the investee’s returns.

2. What are “variable returns”?

Solution: Returns that vary based on the performance of the investee, including dividends, fair value changes, residual interests, fees, synergies, and negative returns such as losses.

3. What is the link requirement in IFRS 10?

Solution: The investor must be able to use its power over the investee to affect the amount of returns it receives.

4. Give two examples of substantive rights.

Solution:

- Rights to appoint or remove key management
- Rights to direct operating or financing policies

5. Give two examples of protective rights.

Solution:

- Lender's right to veto major capital expenditure
- Rights relating to liquidation or fundamental changes

SECTION B — Long-Form Conceptual Questions

6. Explain the difference between substantive rights and protective rights.

Solution: Substantive rights give the holder the practical ability to direct relevant activities when decisions must be made. They are exercisable and realistic to use. Protective rights safeguard the interest of the holder but do not give power over relevant activities. They relate to fundamental changes and do not confer control.

7. Describe the principal–agent assessment under IFRS 10.

Solution: A decision-maker may have power but must be assessed to determine whether it acts as a principal (controls the investee) or an agent (acts on behalf of others). Key factors include:

- Scope of authority
- Rights held by other parties (e.g., removal rights)
- Remuneration structure
- Exposure to variable returns If the decision-maker has significant exposure to variable returns and cannot be easily removed, it is likely a principal.

8. Explain how IFRS 10 applies to structured entities.

Solution: Structured entities often have predetermined activities and limited voting rights. Control is assessed by identifying:

- Who has power over relevant activities (e.g., ability to change servicers)
- Who is exposed to variable returns (e.g., residual interest holders)

- Who can use power to affect returns Often, sponsors or residual interest holders control structured entities.

SECTION C — Computational / Numerical Questions

9. Goodwill Calculation

Scenario: Parent acquires 75% of Subsidiary for R900. Fair value of identifiable net assets = R1,000. NCI measured at proportionate share.

Required: Calculate goodwill.

Solution:

- Parent's share of net assets = $75\% \times 1,000 = 750$
- Goodwill = Consideration (900) – Parent's share (750) = **150**
- NCI = $25\% \times 1,000 = 250$

10. Intra-Group Inventory Profit Elimination

Scenario: Parent sells goods to Subsidiary for R100 (cost R60). Subsidiary still holds 50% of the inventory at year-end.

Required: Calculate unrealised profit.

Solution:

- Profit = $R100 - R60 = R40$
- Inventory remaining = 50%
- Unrealised profit = $R40 \times 50\% = \mathbf{R20}$
- Adjustment: Reduce inventory by R20 and reduce group profit by R20.

SECTION D — Case-Study Questions

11. *De Facto* Control Case

Scenario: Investor holds 40% of voting rights. Remaining 60% is dispersed among many shareholders, none holding more than 2%. Only 50% of dispersed shareholders vote.

Required: Assess control.

Solution:

Investor's 40% represents 80% of votes cast ($40 / 50$). Investor has practical ability to direct relevant activities. Investor controls the investee → must consolidate.

12. Loss of Control Case

Scenario: Parent holds 80% of Subsidiary. Parent sells 50% and retains 30%. Fair value of retained interest = R300. Consideration received = R500. Carrying amount of net assets = R600. NCI at date of loss of control = R120.

Required: Calculate gain/loss.

Solution:

- Aggregate fair value = 500 (50% sold) + 300 (30% retained) = 800
- Carrying amount removed = 600 + 120 = 720
- **Gain** = 800 – 720 = **R80**

13. Investment Entity Case

Scenario: Fund F meets definition of investment entity. Subsidiaries S1 and S2 held solely for capital appreciation. Subsidiary M provides investment management services.

Required: Determine consolidation requirements.

Solution:

- S1 and S2 → measured at fair value through profit or loss
- M → consolidated
- Fund F does not consolidate investment subsidiaries.

14. Principal vs Agent Case

Scenario: Manager M manages Fund X. Investors can remove M only with 90% vote. M receives performance-based fees and holds 15% of units.

Required: Assess whether M is principal or agent.

Solution:

High removal threshold + significant exposure to variable returns → M is a **principal** and controls Fund X.

15. Potential Voting Rights Case

Scenario: Investor holds 30% of voting rights and has in-the-money options to acquire 25% more, exercisable immediately.

Required: Assess control.

Solution:

- Options are substantive → Investor effectively has power.
- Investor controls the investee → must consolidate.

SECTION E — Extended Scenario Analysis

16. Complex Group Structure

Scenario: Parent P owns 60% of Subsidiary S. S owns 70% of Sub-Subsidiary SS. P also holds substantive call options to acquire 20% of SS directly. NCI in S is passive and dispersed.

Required:

- (a) Identify who controls S
- (b) Identify who controls SS
- (c) Explain consolidation structure

Solution:

- (a) P controls S (majority voting rights + dispersed NCI).
- (b) P controls SS indirectly through S ($60\% \times 70\% = 42\%$) plus substantive options (20%).
Total effective power = 62% → P controls SS.
- (c) P consolidates S and SS fully; NCI recognised at each level.

17. Change in Relevant Activities

Scenario: Investor I holds 55% of voting rights. Relevant activities were previously predetermined by contract. The contract expired, and voting rights now determine relevant activities.

Required: Assess control.

Solution:

Previously no control (contractual power elsewhere). After expiry, I's voting rights give power over relevant activities. I now controls the investee → must consolidate.

18. Structured Entity Servicer Replacement Case

Scenario: SE holds financial assets. Servicer A manages assets. Investor B has rights to replace Servicer A at any time without cause. Investor C holds residual interests.

Required: Assess control.

Solution:

- Power lies with party able to direct relevant activities → Investor B (replacement rights).
- Exposure to variable returns → Investor C.
- Link requirement: Investor B does not benefit from returns.
- Conclusion: Neither B nor C individually controls; further analysis needed.

SECTION F — Short Concept Checks

29. What is the consolidation method under IFRS 10?

Solution: Line-by-line aggregation with elimination of intra-group items.

30. When must control be reassessed?

Solution: Whenever facts or circumstances change (rights, ownership, relevant activities, involvement).

16. Typical Consolidation Spreadsheet Adjustments

(Refer next page)

10 Typical Consolidation Spreadsheet Entries

Account	Debit	Credit	Notes
1. Eliminate Parent's Investment Against Subsidiary's Equity			
Share Capital (Subsidiary)	XXX		Eliminate subsidiary equity
Retained Earnings (Subsidiary)	XXX		Eliminate subsidiary equity
NCI		XXX	Recognise NCI at acquisition
Investment in Subsidiary		XXX	Eliminate parent's investment
Goodwill	XXX		Recognise goodwill (if applicable)
2. Eliminate Intra-Group Sales			
Revenue (Parent/Sub)	XXX		Remove intra-group sales
Cost of Sales (Parent/Sub)		XXX	Remove matching intra-group cost
3. Eliminate Unrealised Profit in Closing Inventory			
Group Profit Adjustment	XXX		Reduce group profit
Inventory		XXX	Remove unrealised profit from inventory
4. Eliminate Intra-Group Receivables/Payables			
Accounts Payable (Sub)	XXX		Eliminate intra-group payable
Accounts Receivable (Parent)		XXX	Eliminate intra-group receivable
5. Eliminate Intra-Group Dividends			
Dividend Income (Parent)	XXX		Remove intra-group dividend income
Dividends Declared (Subsidiary)		XXX	Remove dividend declared
6. Fair Value Adjustment at Acquisition (Subsidiary Net Assets)			
PPE (Fair Value Adjustment)	XXX		Increase subsidiary PPE to fair value
Fair Value Reserve / Goodwill		XXX	Recognise fair value uplift
7. Post-Acquisition Profit Allocation			
Retained Earnings (Subsidiary)	XXX		Transfer post-acquisition profit
Group Retained Earnings		XXX	Parent's share of post-acquisition profit
NCI		XXX	NCI share of post-acquisition profit
8. Eliminate Intra-Group Interest			
Interest Income (Parent)	XXX		Remove intra-group interest income
Interest Expense (Subsidiary)		XXX	Remove intra-group interest expense
9. Eliminate Intra-Group Management Fees			
Management Fee Income (Parent)	XXX		Remove intra-group fee income
Management Fee Expense (Subsidiary)		XXX	Remove intra-group fee expense
10. Loss of Control — Derecognition Entries			
Assets of Former Subsidiary	XXX		Derecognise assets
Liabilities of Former Subsidiary		XXX	Derecognise liabilities
NCI	XXX		Derecognise NCI
Investment Retained (FV)	XXX		Recognise retained interest at fair value
Gain/Loss on Disposal		XXX	Recognise gain/loss