What is Consolidation of Financial Statements?

Worksheet

Consolidation combines a parent and its subsidiaries into one set of financial statements by adding line items and eliminating intercompany balances, transactions, and the investment account against subsidiary equity, recognizing any non-controlling interest (NCI) separately.

Questions

1. What triggers the requirement to prepare consolidated financial statements?
A) Parent owns any equity in another company
B) Parent obtains control over a subsidiary
C) Two companies share a supplier
D) Companies are in the same industry

2. In consolidation, what happens to the parent's 'Investment in Subsidiary' account?
A) It is reported as an asset in consolidated accounts
B) It is eliminated against the subsidiary's equity
C) It is converted entirely to goodwill
D) It is transferred to retained earnings

3. An intercompany sale with unrealized profit in ending inventory must be:
A) Left as reported by each entity
B) Eliminated in consolidation
C) Doubled in consolidated revenue
D) Ignored if under $1,000

4. If a parent owns 75% of a subsidiary, the NCI's share of subsidiary equity is:
A) 0%
B) 25%
C) 75%
D) 100%

5. A parent owns 80% of a subsidiary; the subsidiary's fair value of net assets is $2,000,000. Compute NCI.

6. A parent sells inventory costing $80,000 to its subsidiary for $110,000; the subsidiary still holds all of it in ending inventory. Find the unrealized profit to eliminate.

7. NCI ownership is 30% and the subsidiary's net income is $500,000. Find NCI's share of income.

8. Define: When must a company consolidate another entity?

9. Define: What is Non-Controlling Interest (NCI)?

10. Define: Why eliminate intercompany transactions?

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Answer Key

1. B) Parent obtains control over a subsidiary - Consolidation is required when the parent obtains control (typically more than 50% voting rights, or de facto control under IFRS 10).

2. B) It is eliminated against the subsidiary's equity - The investment account is eliminated against the subsidiary's equity at acquisition, with any excess recognized as goodwill.

3. B) Eliminated in consolidation - Unrealized intercompany profit must be eliminated because the group hasn't sold the goods to an outside party yet.

4. B) 25% - NCI = 1 parent's ownership % = 1 75% = 25%.

5. 1 0.80 = 0.20 0.20 $2,000,000 = $400,000

6. Unrealized profit = $110,000 $80,000 = $30,000 Consolidation eliminates $30,000 from inventory and COGS/retained earnings

7. NCI share = 0.30 $500,000 = $150,000

8. When it obtains control - typically more than 50% of voting rights, or de facto control under IFRS 10 / ASC 810.

9. The portion of a subsidiary's equity and income not attributable to the parent, shown within consolidated equity.

10. To avoid double-counting revenue, expenses, and profit that hasn't been realized outside the consolidated group.

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