		Year 1	Year 2
Company A	Fin. Inv./B	600	600
Company B	Capital	1,000	1,000
	Reserves	800	950
	Result	200	100

Let's now proceed as we did before starting by considering this new situation and noticing that if the direct percentage between A and B remains unchanged, the indirect percentage in company B becomes 54%.

Consolidated reserves of company B are

- 480 = 48% * [1000+800+200] – 80% * 600 for Year 1
- 567 = 54% * [1000+950+100] – 90% * 600 for Year 2

giving a variation of 87 = 567 – 480 which consists in the following components,

- 54 = 54% * 100 corresponding to the group part of the result
- (24) = 48% * (50) corresponding to the group part of the dividend
- 117 = 6% * 1950 for the same reason as explained in precious step
- (60) = 10% * (600) because we increase by 10% the group part in the opening value of the Year 1 Financial investment in B.

The two last components can be considered as a group price acquisition of 60 to compare to the corresponding group part of equity we receive for that price, which is 117. This looks like a badwill calculation giving a value of 57. That amount, again, cannot remain in the reserves.

The problem is just a little bit more complicated here because the company P transaction of acquiring 10% of company A shares has probably produced a goodwill. We mean that this badwill should be netted with the goodwill.

To confirm this point of view, the best economical reason we can give is that the company P transaction is not buying shares of a company but shares of a subgroup which is A+B.

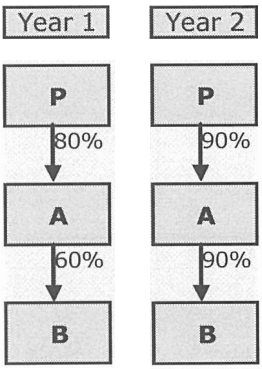
In such situation, we recommend to book that badwill in the most appropriate way in company P accounts. By doing this, the two last components are not there anymore.

Situation 6 : And if all transactions were happening at the same time

Indeed, we can imagine all the previous transactions happening at the same time (1st of January Year 2), we mean

- Capital increase in company B for an amount of 500, 3rd Parties not subscribing to that capital increase
- Company A acquiring shares of company B for a price of 500
- Company P acquiring shares of company A for a price of 700

Here are the group structure and the statutory accounts



		Year 1	Year 2
Company A	Fin. Inv./B	600	1,800
Company B	Capital	1,000	1,500
	Reserves	800	950
	Result	200	100

Consolidated reserves of company B are

- 480 = 48% * [1000 + 800 + 200] - 80% * 600 for Year 1
- 445.5 = 81% * [1500 + 950 + 100] - 90% * 1800 for Year 2

and the difference to justify is (34.5).

In such a complex structure situation, we recommend to calculate consolidated reserves of B just before the transaction and just after the transaction. The difference should be considered as a goodwill or a badwill.

Here are the amounts found for our example

- Consolidated reserves before transaction : 480 = 48% * 2000 - 80% * 600
- Consolidated reserves after transaction : 364.5 = 81% * 2450 - 90% * 1800

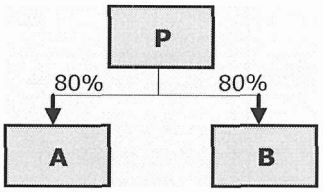
This implies a net variation of (115.5). This amount represents a goodwill we book at company P level as an additional goodwill related to the 10% shares acquired by company P in company A.

Situation 7 : Elimination of group profit between two companies

In this last situation, we consider two companies A and B consolidated with the integral consolidation method at the same percentage.

The only transaction happening between them is a disposal of an asset from company A to company B with a group profit of 100.

Here are the group structure and the adjusted accounts concerned by the transaction.



A			
Tang. Assets	0	Capital	500
		Reserves	300
		(a)	*100*
Assets	900	Result	100
		(a)	*(100)*

Tang. Assets	500	Capital	1,000
(b)	*(100)*	Reserves	
		(b)	*(100)*
Assets	1,600	Result	

In company A accounts, consolidation adjustment (a) eliminates the group profit of 100 by booking the counterpart on the Reserves.

In company B accounts, we eliminate the group profit of 100 included in the Tangible asset acquired and the counterpart is also the Reserves.

By booking this way, we see that the net group impact on the reserves is 0 = 80% * 100 + 80% * (100), but at the same time consolidated reserves of company A increase by 80 and consolidated reserves of B decrease by (80).

Moreover, these variations do not impact the P&L. In fact we have what we call a transfer of reserves between both companies. At group level, the net amount is zero as announced above.

We are aware to present a particularly easy case by supposing both companies are owned at the same percentage. Some special topics in Part 4 will consider more realistic situations, but the principles explained here are still valid.

2.3 A status board to justify consolidated reserves evolution

The situations explained in previous section illustrate the difficulty to validate the evolution of the consolidated reserves of a group and consequently justify the use of some status board to help validation of this technical account.

How does this status board look like?

This following status board works perfectly well and is adapted

- To groups of any size (number of companies)
- To groups of any activity
- To groups independently of their evaluation rules (IFRS or Local Gaap) under the only condition that booking of reserves without impacting the P&L should be done on a specific account (not the consolidated reserves but revaluation reserves)

This status board justifies the group consolidated reserves, not the Minority Interests and the Translation Adjustments which require another format and content.

Let's explain its content.

	Conso. Reserves Year 1	Result Year 2	Dividends paid	Dividends received	Transfer of reserves	Other transfers	Parent dividends	Total	Conso. Reserves Year 2	Difference (9)-(8)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Parent company										
Company 1										
Company 2										
...										
Company N										
Total			X	(X)	0					

It looks like a matrix of 10 columns and as many lines as there are companies in the consolidation scope. We usually start with parent company on line 1.

Column (1) contains the consolidated reserves of each company as calculated in Year 1 consolidation

Column (2) contains the group part of the result of each company

Column (3) shows the group part of dividends paid by each company, parent company excluded

Column (4) shows the group part of dividends received by each company, parent company included

Column (5) contains all transfer of reserves between companies, as explained in Situation 7 of previous section

Column (6) is to be used only in case parent company transfers reserves to its capital account. Indeed, in such situation, we notice only a decrease of its reserves and not an increase of the capital because this account is not managed by this status board.

Column (7) shows the dividends paid by the parent company. These dividends are in a separate column with regard to the dividends of the other companies, for a reason that will be explained later in this section.

Column (8) is just the horizontal total of all amounts of each line

Column (9) contains the consolidated reserves of each company as calculated in Year 2 consolidation

Column (10) shows the difference between column (9) and column (8)

How to use this status board?

A certain number of visual checks can be done as explained below.

Check 1 consists to verify that total of column (3) and (4) together is zero. This means that all dividends paid by subsidiaries are effectively received. Supposing this is indeed the case and one dividend received has not been eliminated, then the status board will show an error in column (10). It is important to say that all amounts of column (3) are signed negative and those of column (4) are signed positive.

Check 2 consists in verifying that total of column (5) is zero. This means that all amounts of reserves transferred between companies are correctly mentioned.

Check 3 consists in verifying the dividends paid by the parent company, including interim dividends and allowances. The reason to use a specific column enables an easier check 1. This cell contains a negative amount.

Check 4 consists in verifying each cell of column (10) is equal to zero. If not, this means there is a problem somewhere for that company. Sometimes, it may happen that one line shows an amount and another line shows the same amount with the opposite sign. This means either an adjustment has been booked in a wrong company or some transfer amounts should be put in column (5).

Check 5 is a global check on the total line. Column (1) + Column (2) + Column (6) + Column (7) = Column (9). To say it with words, opening

reserves + group profit – parent company dividends + transfer of reserves to capital equal closing reserves.

Once all these validations are correct, we usually say that the consolidated equity is technically correct. It doesn't mean completely correct because some adjustments of the period may be wrong or forgotten. Moreover, the content of statutory accounts may contain some wrong information.

Anyway, when this status board is "in balance" with all zeros in column (10), the difficult step of justifying the consolidated reserves is achieved and the consolidation is under control for this item.

This status board has been applied thousands of times to groups sometimes having hundreds of companies. It has also been used for so many different activities and in different countries with a full success. Auditors are asking for this status board.

We will conclude by recommending to consolidators not to communicate consolidated figures outside their office before having checked the validity of the status board. If it is not in balance in the way we explained, there are some remaining errors in the consolidation. No doubt about that.

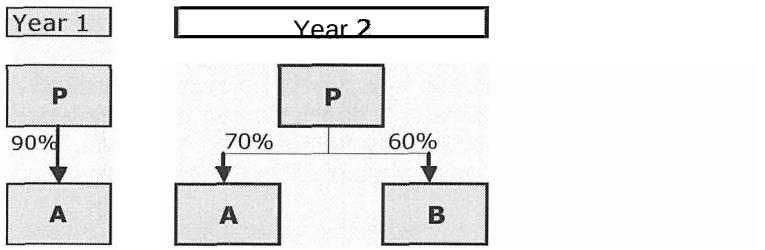
2.4 Consolidated reserves status board: A case study

Before leaving this difficult subject, we propose to give an illustration of how to produce such status board on the basis of an example, not too complex but sufficiently realistic to be interesting.

In Year 1, the group consists in two companies, P and A, founded by P a few years ago, owned at 90%.

In Year 2, P sells 20% of A shares to 3rd Parties and acquires 60% of a company B. All these companies are supposed to have the same currency and both transactions are concluded on January 1st, Year 2.

Here is the group structure for Year 1 and 2.



Consolidation of Year 1

Here are the statutory accounts of companies P and A. No consolidation adjustments being required for this Year 1, we present hereunder the consolidated accounts

Investments/A	180	Capital	
		Reserves	
		Result	
Other assets	720	Other liabilities	150

A			
Tang. assets	100	Capital	200
		Reserves	150
		Result	30
Other assets	400	Other liabilities	120

P + A			
		Capital	500
		Reserves	200
Tang. assets	100	Result	50
		Cons. Res.(A)	162
		Minor. Int.(A)	38
Other assets	1,120	Other liabilities	270

with the only following explanations

- Consolidated reserves of A = 162 = 90% * [200 + 150 + 30] - 180
- Minority interests of A = 38 = 10% * [200 + 150 + 30]

Consolidation of Year 2

Here are the statutory accounts of the three companies for Year 2

P			
Investments/A	140	Capital	500
Investments/B	400	Reserves	220
		Result	80
Other assets	660	Other liabilities	400

A			
Tang. Assets	0	Capital	200
		Reserves	160
		Result	50
Other assets	600	Other liabilities	190

B			
Tang. Assets	150	Capital	300
		Reserves	200
		Result	40
Other assets	650	Other liabilities	260

which reflect the following events

- P sells 20% of shares of company A to 3rd Parties for a price of 70
- P acquires 60% of shares of company B for a price of 400. This transaction leads to a goodwill that cannot be allocated to assets.
- A sells its tangible assets to B for a price of 150, making a group profit of 50
- Parent company P pays dividends of 30
- Company A pays dividends of 20. It has been agreed that P keeps the rights to receive dividends related to the 20% of shares disposed.

These different events need he following consolidation adjustments explained hereunder.

Adjustment (a) : Disposal of 20% of shares of company A

In statutory accounts, the 90% of shares owned by P have a value of 180. The 20% disposed have thus a value of 40 = 180 * (20% / 90%).

On the basis of a selling price of 70, the statutory gain is 30.

In consolidation, the gain or loss is the difference between the same sale price of 70 and the equity value on the 1st of January Year 2 of the 20% disposed. Translated into a formula, it becomes

$$(2) = 70 - 20\% * [200 + 160]$$

The statutory gain of 30 is turning into a loss of 2 in consolidation.

We have seen in Part 2 Section 8.14 that we have to book the following adjustment

Parent P	Debit	Credit
Gain on disposal	30	
Loss on disposal	2	
Reserves		32

in which we set to zero the statutory gain and we book an additional loss of 2.

Adjustment (b) : Goodwill on the acauisition of 60% of shares of company B

The acquisition price is 400 for a 60% of the opening equity of 500, which gives a goodwill of 100. As said above, we suppose it is not possible to allocate this goodwill to assets. Moreover, we will suppose consolidating under IFRS rules with no depreciation of the goodwill, giving the following adjustments in P accounts

Parent P	Debit	Credit
Goodwill		
Fin.Invest./B		100

Adjustments (c*) and (d) : Elimination of group profit on the assets disposal

This transaction is supposed to occur just after the disposal of the 20% of A shares. This means the seller is owned at 70% and the acquirer is owned at 60%. The statutory profit of A is 50 and the group part in consolidation becomes 35 = 70% * 50.

Because of these different percentages, we have to split these 35 into 30 = 60% * 50 which is really the group profit and 5 = 10% * 50 which represents the profit A realizes with the 3rd Parties of company B.

There will be two adjustments, one in company A and one in company B.

Company A	Debit	Credit
Result (*)	30	
Reserves (*)		30

Notice that this adjustment impacts the accounts of A at 100%.

Company B	Debit	Credit
Reserves	50	
Tang. Assets		50

Amounts of this adjustment will split into group and Minority interests on the basis of 60%.

After consolidation process, we will notice two interesting points

- Net impact on Reserves will be 30 from A and (30) = 60% * 50 from B, so an impact of zero
- Contribution of A profit for the group will be 5 = 70% * 50 + (30) as announced above.

Adjustment (e) : Elimination of dividends paid by company A

P negotiated the preservation of its rights on 90 % of dividends, although it owns now after the sale only 70 %. The amount of dividends to eliminate is thus 18 = 90% * 20.

Parent P	Debit	Credit
Reserves		

The dividends of 30 paid by parent company require no consolidation adjustment.

Let's now consider the accounts of each company, including these adjustments

P			
Goodwill/B		Capital	500
(b)	***100***	Reserves	220
Investments/A	140	*(a)*	***32***
		(e)	***18***
Investments/B	400	Result	80
(b)	***(100)***	*(a)*	***(32)***
		(e)	***(18)***
Other assets	660	Other liabilities	400

A			
Tang. Assets	0	Capital	200
		Reserves	160
		(c)*	***30***
		Result	50
		(c)*	***(30)***
Other assets	600	Other liabilities	190

Tang. Assets	150	Capital	
		Result	
Other assets	650	Other liabilities	