ACCOUNTS OF HOLDING COMPANIES/ PARENT COMPANIES

A holding company is a limited liability company which acquires all or majority of equity shares of any limited company, called the subsidiary company, in order to control the composition of the board of directors or voting power of the subsidiary company.

According to section 4 of the Companies Act, a company is deemed to be a subsidiary company of another if the other:

(i) controls the composition of its Board of Directors; or

(ii) holds, in case of existing companies having preference shares with voting rights, more than half of the total voting power of such company and in other cases, holds more than half in nominal value of its equity share capital; or

(iii) it is a subsidiary of another company which itself is a subsidiary of a third company.

Wholly owned and partly owned subsidiaries

A wholly owned subsidiary is one in which all the shares with voting rights (100%) are owned by the holding company.

On the other hand, in partly owned subsidiary only the majority of shares (more than 50%) are owned by the holding company. In such partly owned subsidiaries, some shareholders do not sell their shares to the holding or parent company. Such share-holders are called 'minority shareholders' or 'outsiders', and their interest or share in the assets of the subsidiary company is technically termed as 'minority interest'.

Consolidation of financial statements

In India, holding companies are ~~not~~ legally required to publish consolidated or group accounts though it is a legal obligation under the Companies Act of England. ~~However~~, It is appropriate to group or combine the accounts so that the shareholders get a clear insight about their interest both in the holding company and its subsidiaries.

Consolidated Balance Sheet (2)

Consolidated B/S is ~~not~~ a legal requirement under the Companies Act, 2013, and hence, ~~there is no prescribed form or Schedule. Hence,~~ the consolidated B/S would be prepared in accordance with New Schedule VI.

(In simple terms, consolidation of balance sheets can be achieved by adding items in the accounts of the holding company to the same items in the accounts of the subsidiary company. However, this aggregation of items is subject to the following exceptions:

(i) The share capitals of the holding company and its subsidiary should never be aggregated.) If some amount of nominal capital of the holding company is held by the subsidiary, the same must be deducted from the share capital of the holding company. Similarly, any share of the holding company in the share capital of the subsidiary must be deducted from the amount of investment in the share of the subsidiary company given on the assets side of the holding company's B/S. In case it is a fully owned subsidiary company and the shares were purchased at par, the two accounts would cancel each other completely.

(ii) Any negative surplus in the P&L statement in the books of the holding company should not be added.

(iii) Necessary revaluation (i.e. appreciation or reduction in value) of assets must be carried out before aggregating them.

(iv) Inter-company or mutual transactions must be eliminated.

(v) Where the holding company and the subsidiary company have their accounts with the same bankers, it is appropriate to combine all bank balances and set off overdraft against credit accounts. However, if the bankers are not the same it is suggested that bank balance accounts on the one hand and overdraft accounts on the other should be shown separately in the consolidated B/S.

(vi) The date of the consolidated B/S and that of the B/Ss of the holding and subsidiary companies must be one and the same. In the case of variation, necessary adjustments)

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...arding profits or losses, (3)
depreciation for the interve-
ning period, etc. must be made
before consolidation.)

(While preparing consolidated B/S, the treatment of the following items must be noted carefully:

(1) Minority interest

In a partly owned subsidiary company, the share capital of the subsidiary company may be held jointly by the holding company and other persons. The collective interest of such persons is termed as interest of outside shareholders or minority interest and is shown as a separate item in the consolidated B/S, between Share Capital and Reserves and Surplus.

(Minority interest represents the claim of outsiders in the net assets (Assets - Liabilities) of the subsidiary company.) It is thus nothing but the amount payable to outsiders in respect of share capital and accumulated profits to the extent of their holdings. (In brief, the total interest of outside shareholders consists of:

(i) their proportionate share in the share capital of the subsidiary company;

(ii) their proportionate share in

(the Reserves (both pre-acquisition and post-acquisition) of the subsidiary company;

(iii) their proportionated share in the surplus (both pre-acquisition and post-acquisition) of the subsidiary.

(3) Cost of acquiring control (or goodwill)

In the balance sheet of the holding company, the shares purchased by it in the subsidiary company appear as non-current asset under the title 'investment in shares of subsidiary company'. The amount of this investment represents the cost price paid for acquiring shares of the subsidiary company. In preparing the consolidated B/S, the share capital of the subsidiary held by the holding company is cancelled against the investment in shares i.e. the cost of the shares paid by the holding company to acquire the said capital. If the holding company has purchased the shares at a price above the face value or nominal value

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... the excess price paid represents the 'Cost of control or goodwill' on consolidation. On the other hand, if the shares were purchased by the holding company at a discount, the difference between the purchase price and the face value represents 'Capital Reserve' on consolidation.)

In determining the net amount of goodwill on consolidation, the following points must also must be considered:

(i) The proportionate share of the holding company in pre-acquisition or capital reserves of the subsidiary must be added to capital reserve or adjusted against goodwill or cost of control.

(ii) Similarly, the proportionate share of the holding company in pre-acquisition or capital profits of the subsidiary must be added to capital reserve or adjusted against goodwill or cost of control.

(3) Pre-acquisition profits and pre-acquisition reserves

Pre-acquisition profits and pre-acquisition reserves must be shown in the consolidated B/S as capital profits and capital reserves respectively.) However, it is inappropriate to show capital reserve and goodwill simultaneously in the B/S. The goodwill account is therefore set off against the capital reserve account (or the vice versa) as far as possible.

General reserves of the subsidiary company must be divided into two parts:

(i) The proportion of such reserves attributable to minority shareholders should be included in the minority interest account.

(ii) The proportion attributable to holding company should be further split into two parts, namely:

(a) Pre-acquisition reserves are treated as capital reserves and adjusted against goodwill, if any.

(b) Post-acquisition reserves are added to the general) reserves of the holding company.

Like reserves, the surplus or profit of the subsidiary company is also divided into two parts:

(i) the share or proportion belonging to outsiders is to be included in minority interest account; and

(ii) the proportion belonging to the holding company is further split up as follows:

(a) Pre-acquisition profits are treated as capital profits and included in the capital reserves to be adjusted against goodwill, if any;

(b) Post-acquisition profits are treated as revenue profits and added to the surplus or profits of the holding company.

4) Pre-acquisition losses

Preacquisition losses of the subsidiary company are treated as capital losses in so far as the share of the holding company in such losses is concerned. It would ultimately increase the cost of acquiring control or goodwill or decrease)

(the capital reserves in the consolidated B/S. Post-acquisition losses are in the nature of revenue losses and the holding company's share of the same would be transferred to the accumulated balance in the P&L statement of the holding company. And if profits are not available, the same may be shown as a separate item as negative surplus under 'Reserves and Surplus' in the B/S.)

5) Inter-company transactions

(When the consolidated B/S is prepared, it must be ensured that inter-company balances are eliminated by offsetting liabilities in one company's balance sheet against the corresponding assets in the other company's B/S. In this connection, the following points may be noted carefully:

(i) **Loans** :- In the consolidated B/S, the loan amounts (advanced by the holding company to the subsidiary or vice versa) and the interest thereon are eliminated so that the same do not appear on any side of the consolidated B/S.) If, even after adjustment for elimination, there is a difference in loan account, it means that there is a cash-in-transit and the same will appear in the asset side of the B/S.

(ii) **Debtors and creditors** :- Elimination is done by deducting common amounts from both debtors and creditors.

(iii) **Bills receivable and bills payable** :- Here also the common (amounts are deducted from both B/R and B/P.

(6) Unrealised profit on stock (Inter-company stock)

When goods are purchased by the holding company from its subsidiary which made a profit thereon and all or a part of such goods remain unsold in stock on the date of the B/S with the holding company, the profit on sale would have been included in the P & L A/c of the subsidiary. It is therefore necessary to eliminate such unrealised profit on closing stock. The amount of unrealised profit on stock is to be deducted first from the profit of the subsidiary company belonging to the holding company and then from the closing stock of the holding company.

(7) Preference share capital in subsidiary company

Preference share capital in subsidiary company should be shown along with minority interest account in the consolidated B/S. However, if a part of the nominal)

…e of preference share capital of the subsidiary company is held by the holding company, it will be adjusted in cost of control A/C, against the cost of investment in preference shares of the subsidiary company held by the holding company. The balance of the preference share capital held by the outsiders will be included in the minority interest A/C in the B/S. This would normally include the nominal value of such shares (taken as fully paid up) held by the outsiders plus the amount of fixed dividend accrued thereon to the date of the consolidated B/S.

(8) Debentures in subsidiary company

As regards debentures of the holding company, the same will appear in the consolidated B/S separately just like share capital. Similarly, if there are debentures in the subsidiary company, they are to be shown as non-current liability)

(in the consolidated B/S
However, if a part of debentures of a subsidiary is held by the holding company as investment and a part by outsiders, the amount of debentures held by the former should be reduced to the extent of investments. Only the amount of debentures held by outsiders would appear as a separate item in the consolidated B/S.

(9) Contingent liabilities

As the name implies, the contingent liability may or may not involve payment i.e. the occurrence of the liability is uncertain. It may arise from the following:

(i) Liability in respect of bills discounted
(ii) Liability under guarantee
(iii) Arrears of dividend on cumulative preference shares
(iv) Liability for calls on partly paid up shares

The treatment of contingent liability on consolidation depends on its nature. If the contingent liability)

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(in respect of a transaction between the company in the group and an outside third party, it will appear as a 'note' to the consolidated B/S. However, if the contingent liability is in respect of a transaction between holding company and the subsidiary, it will disappear from the footnote of individual company's B/S since it appears as an actual liability in the consolidated B/S.)

(10) Revaluation of assets

At the time of acquisition of shares of the subsidiary, its fixed assets may be revalued for determination of the value of shares. Hence, adjustment for the profit or loss on revaluation must be made in the consolidated B/S.

(The impact of revaluation may be stated as follows

(i) Any increase in the value of assets is in the nature of capital profit from the holding company's point of view. It is immaterial) (whether the values ... appreciated in the pre-... post-acquisition periods. Consequently, the profit on revaluation would be added to capital reserve or used for reducing the value of goodwill.

(ii) As a result of appreciation in the value of assets, depreciation charge would be increased proportionately and the same would be deducted from the revenue profits of the subsidiary company.

(iii) Any reduction in the value of assets is a:

(a) capital loss if revaluation is done before or at the time of acquisition of control by the holding company, and it will increase the cost of control or goodwill or reduce the amount of capital reserve.

(b) revenue loss if the revaluation is done in the post-acquisition period.

(iv) As a result of decrease in the value of assets, depreciation would be decreased proportionately and added to the revenue profits of the subsidiary.)

Bonus shares (11)

(When the subsidiary company issues bonus shares it will obviously increase the number of shares with the holding company i.e. an automatic increase in the paid-up value of shares held in the subsidiary company. The treatment of bonus shares would depend upon the source utilized for issuing bonus shares i.e. whether the bonus shares are issued from pre-acquisition or post-acquisition profits.

(2) Bonus shares from pre-acquisition profits

As the share of the holding company in the pre-acquisition profits is in the nature of capital profits, it is immaterial whether such profit is appropriated by the holding company as pre-acquisition profit or bonus shares for the purpose of calculating the cost of control or goodwill. It will have no accounting effect because while calculating the cost of control, the share of the holding company in

(the pre-acquisition profit is reduced and the paid-up value of shares held in the subsidiary company increases. Hence, the net effect on the cost of control is same when the bonus shares are issued from the pre-acquisition profit.)

(13) Bonus issue from post-acquisition profits

When the subsidiary company issues bonus shares from the post-acquisition surplus (revenue surplus), the following procedure is adopted:

(i) The amount of bonus issue is to be deducted from the revenue surplus before the share of the holding company and minority interest in such surplus is calculated.

(ii) The bonus share amount is to be deducted from the cost of acquiring control or goodwill or, alternatively the paid-up share capital held by the holding company in the share of the subsidiary company is to be increased.

(iii) The proportionate share of bonus amount is to be added to minority interest.)

 (10)

(14) Dividend received from a subsidiary company

When a subsidiary company declares and remits dividend, the holding company will receive its due share on the paid-up value of shares held by it. On receipt, the bank amount will be debited but the problem is : which account should be credited ?

If the dividend has been paid from pre-acquisition surplus, it is treated as capital gain and credited to Investment in the shares of subsidiary company A/c.) It will then reduce the cost of such investment and ultimately come either reduction in goodwill A/c or increase in capital reserve. (If, however, dividend has been paid from post-acquisition surplus, it is treated as revenue income and transferred to P&L statement of the holding company.

(15) Goodwill in the B/S of the subsidiary company

There may be goodwill already existing in the B/S of the subsidiary company.)

(The common practice is to show this goodwill in aggregate in the consolidated B/S along with the value of goodwill or cost of control arrived at by elimination.)
In other words, goodwill already appearing in the B/S of the subsidiary is added to goodwill or cost of control in the consolidated B/S.
(Some accountants feel that it is advisable to adjust the share of minority interest in such goodwill of the subsidiary already appearing in the books. Thus, from the goodwill of the subsidiary company, only the holding company's share is to be added to the cost of control.) //

6) Proposed dividend in the B/S

(The amount of proposed dividend in the B/S of subsidiary company must be added to the current year's profits of the subsidiary company. After that, the cost of control and minority interest are

...ulated in the usual manner. Finally, the share of minority shareholders in the proposed dividend must be deducted from 'minority interest' and shown as a separate item in the consolidated B/s under Current Liabilities : Short-term provisions. (11)

In case the directors of the subsidiary company have not appropriated the surplus for proposed dividend, this item will not be found in the B/s of the subsidiary company. However, if there is a proposal to do so, the following procedure is adopted:

(i) The cost of control and minority interest are to be calculated in the usual manner with the help of given figures and without any adjustment for proposed dividend.

(ii) The share of minority shareholders in the proposed dividend must be deducted from 'minority interest' and shown as a separate item in the consolidated B/s as indicated above.

(17) Interim dividend paid (subsidiary company)

The amount of interim dividend paid by subsidiary company during the accounting year must be added to the balance of the current years profits of the subsidiary. Holding company's share of the same must be deducted from the consolidated profit. Minority's share of the same will be deducted from 'minority interest'. Interim dividend will not be shown anywhere in the consolidated B/S.

(18) Unclaimed dividend

This item appearing in the B/S of the subsidiary company must be added in full to the total of the minority interest in the consolidated B/S.

(19) Preliminary expenses, discount on issue of shares and debentures, underwriting commission, etc

These items in the balance sheet of the subsidiary company are in the nature of capital losses and hence must be taken into consideration while calculating the)

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(12)

of control and minority interest, In other (words, the proportionate share of holding company in preliminary expenses, discount on issue of shares and debentures, underwriting commission, etc. would be added to the cost of control or deducted from capital reserve, as the case may be. Similarly, the proportionate share of minority shareholders in such losses must be deducted from minority interest itself. Thus, in the consolidated B/S, these capital losses of the subsidiary company shall never appear as separate items and must be eliminated.)