Advanced Group Accounting (RIKA)

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Self-Study Exercises
Lecture Block 2: Acquisition Method

Exercise 1: Business Combinations and Goodwill

Fact Pattern:
On 1 January 20x5, Akquirer Corporation acquired 100% of Zeller for €75,000 in cash.

	Akquirer	Zeller
31 December 20x4 Balance Sheets		
Cash	€3,000	€2,000
Accounts receivable – net	1,000	3,000
Inventory	6,000	5,000
Plant assets – net	25,000	20,000
Total assets	*€35,000*	*€30,000*
Current liabilities	€4,000	€3,000
Bonds payable	6,000	7,000
Total liabilities	*€10,000*	*€10,000*
Common stock, par €1 per share	€2,000	€1,000
Additional paid-in capital	6,000	7,000
Retained earnings	17,000	12,000
Total stockholders' capital	*€25,000*	*€20,000*
Total liabilities plus stockholders' equity	*€35,000*	*€30,000*

- Except for PP&E, there are no differences between fair values and book values. On 1 January 20x5, the fair value of Zeller's plant assets amounts to €23,000. The fair value of Akquirer's plant assets is €32,000. Both companies depreciate PP&E over 10 years on a straight-line basis.

Exercise:
- Please calculate Zeller's goodwill as indicated by the transaction:
  a) Without considering taxes
  b) Considering taxes, assuming a tax rate of 30%.
  c) How does the consideration of taxes change the purchase price allocation? Please provide an economic interpretation.

Exercise 2: Deferred Taxes

Fact Pattern:
Company A acquires 100% shares of company B for €40 million in 20X1.
The only intangible asset of B (not recognized) is a self-generated brand (estimated brand value: €8 million)
The other assets contain hidden reserves of €6 million.
Assume that under tax law there is no fair value adjustment.

Company B			
Cash	20	Common stock	40
Other assets	40	Debt	20
Total Assets	60	Total E&L	60

To account for the acquisition, Company A shows the following journal entry:

Dr. XXXX

Cr. Deferred Tax Liability 5.6

Cr. XXX

Exercise:

a) Please calculate the statutory tax rate that would be consistent with the journal entry above.
b) Please calculate the goodwill or gain on bargain purchase that results from the transaction, assume that tax rate calculated in a).
c) Please perform the purchase price allocation for the transaction above, assuming a tax rate of 30% (different from the one calculated in a)).

Exercise 3: Non-controlling interest

Fact Pattern:

On 1 July 20X3, Heron Ltd. acquired 60% of the shares of Petrel Ltd. for €45,000 when the equity of Petrel Ltd. consisted of:

Equity:	
Share Capital	42,000
Retained Earnings	2,000

All the identifiable assets and liabilities of Petrel Ltd. were recorded at fair value expect for equipment and inventory:

Accounts:	Carrying Amount	Fair Value
Equipment (cost 250,000)	180,000	200,000
Inventory	40,000	50,000

The tax rate is 30%.

Exercise:

Determine NCI share of equity at acquisition date

1. as the proportionate share of revalued net assets
2. full fair value.