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This significant transaction marks a pivotal moment in the financial and strategic landscape of both Pert Company and Sales Company. Understanding the details and implications of this acquisition requires a comprehensive analysis of the transaction, including the valuation, consolidation process, and financial reporting considerations. In this article, we will explore the background of the acquisition, the accounting treatment, and its impact on the financial statements of both companies, providing valuable insights for investors, accountants, and business analysts.

Background of the Acquisition

Company Profiles

- Pert Company: A well-established organization engaged in [industry/sector], with a history of strategic acquisitions to expand its market reach.
- Sales Company: A smaller entity operating within the same or a related industry, with a focus on [specific products/services].

Details of the Transaction

- Purchase Date: January 1, 2014
- Ownership Stake Acquired: 85%
- Purchase Price: \$350,000
- Implication: The acquisition grants Pert Company control over Sales Company, enabling consolidation of financial statements and strategic alignment.

Understanding the Purchase Price and Ownership Percentage

Calculating the Fair Value of Sales Company

Since Pert Company acquired 85% of Sales Company for \$350,000, it is essential to determine the implied fair value of the entire Sales Company at the acquisition date. This involves:

- Step 1: Recognize that the purchase price reflects 85% ownership.
- Step 2: Calculate the implied total value:

$$\text{Total Fair Value of Sales} = \frac{\text{Purchase Price}}{\text{Ownership Percentage}} = \frac{\$350,000}{0.85} \approx \$411,764.71$$

- Step 3: Recognize that the remaining 15% ownership has an implied fair value of:

$$15\% \times \$411,764.71 \approx \$61,764.71$$

Implications for Valuation and Goodwill

The difference between the purchase price and the fair value of net identifiable assets acquired may result in the recognition of goodwill or a gain from a bargain purchase.

- Goodwill Calculation:

$$\text{Goodwill} = \text{Purchase Price} + \text{Noncontrolling Interest (NCI)} - \text{Fair Value of Net Identifiable Assets}$$

- Noncontrolling Interest (NCI): Represents the 15% ownership not acquired by Pert, valued at approximately \$61,764.71.

Accounting for the Acquisition

Consolidation Process

Since Pert Company acquired control (more than 50%), the financial statements need to be consolidated. The consolidation involves:

- Combining the assets, liabilities, revenues, and expenses of both companies.
- Eliminating intercompany transactions and balances.
- Recognizing goodwill or gain from a bargain purchase.

Steps in Accounting for the Acquisition

1. Identify the acquisition date and determine the fair value of consideration transferred.
2. Recognize and measure the identifiable assets acquired and liabilities assumed.
3. Recognize any goodwill or gain from a bargain purchase.
4. Account for noncontrolling interest using either the full goodwill method or

proportionate method.

Goodwill Calculation Example

Assuming the fair value of net identifiable assets of Sales Company at acquisition was \$300,000, the calculation would be:

$$\text{Goodwill} = (\text{Purchase Price} + \text{NCI}) - \text{Fair Value of Net Assets}$$
$$\text{Goodwill} = (\$350,000 + \$61,764.71) - \$300,000 \approx \$111,764.71$$

This goodwill reflects the intangible value Pert Company expects to gain from the acquisition.

Financial Reporting Implications

Consolidated Financial Statements

- Balance Sheet: Combines assets, liabilities, and equity of Pert and Sales, adjusted for fair value and eliminations.
- Income Statement: Reflects consolidated revenues and expenses, including amortization of fair value adjustments.
- Cash Flow Statement: Presents cash flows from operating, investing, and financing activities related to the combined entities.

Impact on Financial Ratios

The acquisition affects key financial ratios such as:

- Debt-to-Equity Ratio: May increase if financing was used.
- Return on Assets (ROA): Could decrease due to the addition of goodwill and intangible assets.
- Earnings Per Share (EPS): May be diluted depending on the purchase price and share structure.

Strategic and Business Considerations

Synergies and Business Growth

The acquisition aims to achieve various strategic objectives including:

- Expanding market share.

- Gaining access to new customer segments.
- Achieving operational efficiencies.

Challenges and Risks

While acquisitions can be beneficial, they also pose risks such as:

- Overpayment leading to goodwill impairment.
- Integration challenges.
- Cultural differences between organizations.

Tax Considerations

- Amortization of Intangibles: Certain assets may be amortized for tax purposes.
- Goodwill Deduction: Depending on jurisdiction, goodwill may or may not be deductible.
- Tax Planning: Strategic structuring of the acquisition can optimize tax benefits.

Conclusion

The acquisition of 85% of Sales Company by Pert Company on January 1, 2014, for \$350,000 represents a strategic move with significant accounting and financial reporting implications. Properly accounting for this transaction involves determining fair values, recognizing goodwill, consolidating financial statements, and analyzing the impact on key financial ratios. This acquisition not only enhances Pert Company's market position but also requires meticulous financial analysis to ensure compliance with accounting standards and to accurately reflect the financial health of the combined entity.

Keywords for SEO Optimization:

- Acquisition accounting
- Consolidation process
- Goodwill calculation
- Fair value of assets
- Noncontrolling interest
- Financial reporting
- Business acquisition strategy
- Impact of acquisition on financial statements
- Equity investment valuation
- Strategic business expansion

Frequently Asked Questions

What is the significance of Pert Company's purchase of 85% of Sales Company's stock on January 1, 2014?

Pert Company's acquisition of 85% of Sales Company's stock indicates a controlling interest, allowing Pert to consolidate Sales's financial statements into its own and exert significant influence over Sales's operations.

How is the purchase price of \$350,000 allocated in the acquisition of Sales Company?

The purchase price is allocated to Sales Company's identifiable assets and liabilities based on their fair values, with any excess recorded as goodwill or a gain from a bargain purchase, depending on the fair value assessments.

What accounting method should Pert use to record the acquisition of Sales Company?

Pert should use the acquisition method (also known as the purchase method), which involves recognizing the identifiable assets acquired, liabilities assumed, and any goodwill or gain from a bargain purchase.

How does acquiring 85% of Sales Company impact Pert's consolidated financial statements?

Acquiring 85% of Sales allows Pert to consolidate Sales's financial results with its own, reflecting the majority ownership and control, leading to combined financial statements that include 100% of Sales's assets, liabilities, revenues, and expenses.

What are the potential implications of this acquisition for Pert Company's financial ratios?

The acquisition can affect key financial ratios such as return on assets, debt-to-equity, and earnings per share by increasing assets and liabilities, and potentially enhancing revenues and profits through consolidation.

What disclosures are required in Pert Company's financial statements regarding this acquisition?

Pert must disclose details about the acquisition, including purchase price, the fair value of assets and liabilities acquired, the amount of goodwill recognized, and any non-controlling interest if applicable.

How does the 85% ownership influence the recognition of non-controlling interest in Sales Company?

Since Pert owns 85%, the remaining 15% is considered non-controlling interest, which

must be separately recognized and presented in the consolidated financial statements, reflecting the portion of equity not owned by Pert.

Additional Resources

On January 1, 2014, Pert Company Purchased 85% Of The Outstanding Common Stock Of Sales Company For \$350,000

In the realm of corporate acquisitions and financial reporting, transactions involving the purchase of a significant stake in another company are pivotal. Such investments not only shape the strategic landscape of the acquiring firm but also have profound implications on financial statements, control, and future earnings. On January 1, 2014, Pert Company made a notable move by acquiring 85% of the outstanding common stock of Sales Company for \$350,000. This transaction set the stage for a comprehensive analysis of consolidation accounting, valuation of net assets, and the subsequent impact on financial statements.

This article explores the intricacies of this acquisition, breaking down the process from initial purchase considerations to consolidated financial reporting, providing a reader-friendly yet technically detailed perspective.

The Context of the Acquisition

Understanding the Stake and Its Significance

Pert Company's acquisition of 85% of Sales Company signifies a controlling interest. Typically, owning more than 50% of a company's voting stock grants control, allowing the parent company to influence policies, appoint management, and integrate operations. In this case, Pert's 85% stake indicates a dominant position, likely enabling full consolidation of Sales Company's financials into Pert's reports.

Such control is crucial because it transforms the nature of the investment. Instead of a passive equity investment, Pert now considers Sales Company a subsidiary, requiring consolidated financial statements that combine the financials of both entities, eliminating intercompany transactions.

Financial Implications of the Purchase Price

The purchase price of \$350,000 reflects Pert's valuation of its controlling interest. To understand whether this price is fair and how it impacts financial reporting, it's essential to analyze the fair value of Sales Company's net assets at the acquisition date. The difference between the purchase price and the fair value of net identifiable assets is termed goodwill or a gain from a bargain purchase, depending on whether it's positive or

negative.

The purchase price also sets the foundation for subsequent calculations, including the fair value of the non-controlling interest (NCI), which represents the 15% of Sales Company not owned by Pert.

Valuation of Net Assets and Purchase Price Allocation

Assessing the Fair Value of Sales Company's Net Assets

Prior to recording the acquisition, Pert needs to determine the fair value of Sales Company's net identifiable assets. This involves:

- Asset Valuation: Reviewing the carrying amounts of assets and liabilities and adjusting them to their fair values.
- Liabilities: Ensuring all liabilities are measured at fair value or at least at the amounts expected to be settled.
- Intangible Assets: Recognizing any identifiable intangible assets, such as trademarks or customer relationships, that may have a different fair value from their book value.

Suppose, for illustration purposes, Sales Company's net assets at the acquisition date are valued at \$300,000 after adjustments, with identifiable assets and liabilities properly measured at fair value.

Calculating Goodwill or Bargain Purchase

Once the fair value of net assets is established, the next step is to allocate the purchase price:

- Total Purchase Price: \$350,000
- Less: Fair Value of Net Assets: \$300,000
- Goodwill: \$50,000

In this scenario, because the purchase price exceeds the fair value of net assets, the excess is recognized as goodwill — an intangible asset representing future economic benefits arising from assets that are not individually identified and separately recognized.

Alternatively, if the purchase price were less than the fair value of net assets, a bargain purchase gain would be recognized.

Accounting for Non-Controlling Interest (NCI)

Although Pert owns 85%, the remaining 15% of Sales Company is held by other shareholders. For consolidated financial statements, Pert must also account for the NCI:

- Method: The most common approach is the fair value method, where NCI is measured at its proportionate share of the fair value of net assets or at its fair value, depending on the accounting standards.
- Implication: NCI's share of net assets and any goodwill associated with the NCI are recognized separately in the consolidated balance sheet.

In our example, NCI's fair value share of net assets would be 15% of \$300,000, which is \$45,000.

Consolidation Process and Journal Entries

Steps in Consolidation

Consolidation involves combining the financial statements of Pert and Sales to present as if they were a single entity. The key steps include:

1. Eliminate Investment Account: Remove the investment in Sales recorded on Pert's books.
2. Record Fair Value Adjustments: Adjust the assets and liabilities of Sales to their fair values.
3. Recognize Goodwill: Record goodwill or a gain from a bargain purchase.
4. Recognize NCI: Account for the non-controlling interest in the equity and net income.
5. Eliminate Intercompany Transactions: Remove any transactions between the two companies to avoid double counting.

Sample Journal Entries at Acquisition

- To record purchase of 85% of Sales Company:

Dr. Investment in Sales Company \$350,000

Cr. Cash or Accounts Payable \$350,000

- To record fair value adjustments (if assets are undervalued):

Dr. Identifiable Assets \$X

Cr. Gain on Revaluation \$X


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- To record goodwill:

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Dr. Goodwill \$50,000

Cr. Investment in Sales Company \$50,000

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- To record non-controlling interest at acquisition:

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Dr. Non-Controlling Interest \$45,000

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These entries are preliminary; subsequent entries during the first year of consolidation will address income, dividends, and adjustments.

## Post-Acquisition Financial Reporting

### Consolidated Financial Statements

Once the acquisition is complete, Pert must prepare consolidated financial statements, which include:

- Consolidated Balance Sheet: Combining assets, liabilities, and equity of Pert and Sales, including adjustments for fair value and goodwill.
- Consolidated Income Statement: Reflecting revenues, expenses, and net income of the combined entity, eliminating intercompany transactions.
- Consolidated Cash Flows: Summarizing the cash movements of both companies.

This process ensures transparency and provides a comprehensive view of the financial position and performance of the entire corporate group.

### Impact on Financial Ratios and Stakeholders

The acquisition impacts key financial ratios, such as:

- Earnings Per Share (EPS): Dilution or enhancement depending on the net income impact.
- Debt-to-Equity Ratio: Changes based on the new equity structure.
- Return on Assets (ROA): Adjusted for the combined assets and earnings.

Stakeholders, including investors, creditors, and analysts, rely on these consolidated figures to assess the company's health and strategic direction.

# Implications and Strategic Considerations

## Strategic Rationale for the Acquisition

Pert's decision to acquire a controlling stake in Sales Company could stem from various strategic motives:

- Expanding market share
- Gaining access to new customer bases or geographic regions
- Acquiring valuable intangible assets
- Achieving operational synergies

Understanding the strategic intent helps interpret the financial impact and future outlook.

## Challenges and Risks

While acquisitions offer growth opportunities, they also pose challenges:

- Integration Risks: Combining operations, cultures, and systems.
- Overpayment: Paying more than the fair value of net assets leading to excessive goodwill.
- Impairment Risks: Future declines in the value of goodwill or intangible assets.
- Regulatory Scrutiny: Ensuring compliance with anti-trust laws and reporting standards.

Effective post-acquisition management is vital to realize anticipated benefits.

## Conclusion

The acquisition of 85% of Sales Company by Pert on January 1, 2014, exemplifies a strategic move with significant financial reporting implications. From determining fair values and allocating purchase price to preparing consolidated financial statements, each step requires meticulous analysis and adherence to accounting standards. While such transactions can offer substantial growth opportunities, they also necessitate careful planning and transparent reporting to stakeholders. As companies navigate the complexities of acquisitions, understanding the technical nuances becomes essential to accurately reflect the financial realities and strategic intentions behind such corporate actions.

This detailed exploration underscores the importance of rigorous valuation, precise consolidation procedures, and strategic foresight in corporate acquisitions, ensuring that financial statements serve as reliable tools for decision-making and stakeholder trust.

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