Chapter 17

Consolidation
Company Shark wants to acquire 60% of the shares in company Seal. Prior to takeover, the balance sheets of the two companies are as follows:

Shark balance sheet before takeover ($)

Assets		Sources	
Fixed Assets	3,500,000	Common stock	500,000
Current assets	2,750,000	Reserves	2,000,000
		Total Equity	2,500,000
		Loan	3,750,000
Total	*6,250,000*	*Total*	*6,250,000*

Seal balance sheet before takeover ($)

Assets		Sources	
Fixed Assets	2,800,000	Common stock	200,000
Current assets	2,400,000	Reserves	2,920,000
		Total Equity	3,120,000
		Loan	2,080,000
Total	*5,200,000*	*Total*	*5,200,000*

Shares in both companies have a par value of $10.

Seal's profits last year totaled $300,000. Seal shares have a price earnings (P/E) ratio of 12. Many Seal shareholders are reluctant to sell to Shark. Shark can only reel in 60% of the shares by offering a price that is 5% above the current market price.

Required:
A. The number of shares in each company
B. The market price of a Seal share.
C. The price per share Shark offers to Seal shareholders.
D. The total amount of money Shark needs to buy the 60% interest in Seal.
E. How much goodwill is involved in the takeover?

Shark only has $500,000 in cash available. To be able to buy 60% of Seal, they must borrow the remaining amount.

F. Present the consolidated balance sheet (full consolidation).

G. Explain what will happen to Shark's solvency position because of the takeover.

Solutions Consolidation
A. Number of Seal shares = $200,000/$10 = 20,000.

B. Seal EPS = $300,000/20,000 = $15.
Market price = $15*12 = $180.

C. Bid price = 1.05*$180 = $189.

D. Total sum = 20,000*0.6*$189 = $2,268,000.

E. Book value per share: $3,120,000/20,000 = $156. Goodwill = ($189 – $156)*20,000*0.6 = $396,000.

Borrow 2,268,000 – 500,000 = 1,768,000
F. ($1,000)

Assets		Sources	
Goodwill	396	Com stock	500
Fixed Assets	6,300	Reserves	2,000
Current assets	4,650	Loan	7,598
		Minority interest	1,248
Total	**11,346**	**Total**	**11,346**

G. Solvency will become weaker due to heavier borrowing.