(Knowledge for Development)

# KIBABII UNIVERSITY

## UNIVERSITY EXAMINATIONS

## 2020/2021 ACADEMIC YEAR

## SECOND YEAR SECOND SEMESTER

## MAIN EXAMINATION

**FOR THE DEGREE OF MASTERS IN BUSINESS ADMINSTRATION**

**COURSE CODE: ADVANCED FINANCIAL ACCOUNTING**

COURSE TITLE: MBA 821

**DATE: 5-8-2021 TIME: 9-11 AM**

**INSTRUCTIONS TO CANDIDATES**

Answer Question One in Section A and Any other TWO (2) Questions in Section B

TIME: 3 Hours

KIBU observes ZERO tolerance to examination cheating

**SECTION A**

**QUESTION ONE**

Conceptual frameworks developed by accounting standard setters are essentially based on identification of 'good practice' from which principles are derived inductively. The criteria for identifying 'good practice' are related to the assumed objectives of financial reporting. At the same time, attention is paid to conceptual coherence, and the development process typically involves 'conceptual tidying up'. Conceptual frameworks may be written in a prescriptive style or a descriptive style, or a mixture of the two. In any event, they are essentially normative, since they seek to provide a set of principles as a guide to setting and interpreting accounting standards. Such guidance, however, does not necessarily preclude a standard being issued that, for compelling pragmatic reasons, departs from a principle set out in the applicable conceptual framework. In relation to the existing framework, explain the importance of a regulatory/accounting concepts framework and the key issues that such a framework should address considering what it addresses currently.**(12 marks)**

b) According to both Hendriksen (1977) and McDonald (1972) the development of an accounting theory should be possible. McDonald argues that a theory must have three elements:

1. Encoding of phenomena to symbolic representation
2. Manipulation or combination according to rules
3. Translation back to real-world phenomena.

**Required:** Does the three elements that McDonald states necessary for a theory to exist in accounting? **(10 marks)**

Flamhoitz defines HRA as 'accounting for people as an organizational resource. It involves measuring the costs incurred by organizations to recruit, select, hire, train, and develop human assets. It also involves measuring the economic value of people to the organization'. As a Chief Accountant at the County Government of Bungoma, account for the methodology of human resources accounting that is applicable and appropriate to enable the county achieve its core mandate. **(20 marks)**

**SECTION B : ( CHOOSE ANY TWO QUESTIONS )**

**QUESTION TWO**

The figures that relate to the Profit and Loss Accounts and to the Statement of Charges in Equity for Addis Limited and as subsidiaries Bunyala Limited and Chania Limited for the year ended 30 November 2014 are as follows:

| | Addis Ltd. **Sh. '000'** | **Bunyala Ltd. Sh. '000'** | **Chania Ltd. Sh. '000'** |
|---|---|---|---|
| Sales revenue | 84,000 | 66,000 | 48,000 |
| Inventory 1 December 2013 | (3,824) | (3,757) | (2,822) |

| | | | |
|---|---|---|---|
| Inventory 30 November 2014 | 4,286 | 4,124 | 2,452 |
| Purchases | (50,862) | (49,862) | (38,430) |
| Distribution cost | (13,440) | (8,050) | (9,600) |
| Administrative expenses | (8,400) | (3,950) | (6,400) |
| Taxation: Current | (2,140) | (1,050) | - |
| Deferred | (1,420) | (300) | 2,040 |
| Dividends | | | |
| Preference: Interim paid 31 May 2014 | - | (450) | - |
| Final paid 30 November 2014 | - | (450) | - |
| Ordinary: Interim paid 31 August 2014 | (3,000) | (500) | - |
| Final proposed 30 November 2014 | (4,500) | (750) | (150) |
| Dividends received | 580 | - | - |
| Retained profit: 1 December 2013 | 18,300 | 12,600 | 9,200 |
| Issued and paid-up share capital: | | | |
| Preference share capital | Nil | 9,000 | Nil |
| Ordinary share capital | 15,000 | 10,000 | 3,.000 |

Additional information:

1. Addis Limited acquired 180,000 10% preference shares of Sh.20 each and 800,000 ordinary shares of Sh.10 each on 1 December 2008 when the balance on the profit and loss account of Bunyala Limited was Sh.8,100,000. Goodwill of Sh.2,500,000 had arisen on the purchase of these shares. Addis Limited is amortizing this goodwill over 5 years on the straight line basis.
2. Addis Limited acquired 180,000 ordinary shares of Sh.10 each in Chania Limited on 1 March 2014: the purchase price of these shares was to be fixed once the results for the year ended 30 November 2014 to maintain its trustee status.
3. Bunyala Limited makes sales to Addis Limited at its nominal selling price. In the year ended 30 November 2014, Bunyala Limited's sales to Addis Limoted amounted to Sh.9,300,000. Stock purchased from Bunyala Limited and held by Addis Limited at cost amounted to Sh.540,000 and Sh.720,000 on 30 November 2013 and 30 November 2014 respectively.
4. Addis Limited sold an item of plant to Bunyala Limited on 1 December 2012 for Sh.2,400,000. Addis Limited had marked up its cost by 20%. Bunyala Limited is depreciating this item of plant to nil residual value on the straight line basis over 10 years with the charge appearing as part of cost of sales.
5. There has been no intra-group trade between Chania Limited and other two companies.
6. Group policy in relation to unrealised profit on intra-group sales is of assets os to remove the whole of the unrealised profit from the asset and from the company which made the profit on the sale of the

asset adjusting the minority interest's share of this profit as appropriate. The amortization of goodwill is classified as an administrative expense and deemed to be a charge against the profit of the holding company.

**Required:**

The consolidated Income Statement and the portion of the Consolidated Statement of Charges in Equity that relates to accumulated profit, giving the details required by International Accounting Standard and the Kenya Companies Act, including reconciliation of the group retained profit for the year and carried forward.

**(Total: 20 marks)**

## QUESTION THREE

Victoria Gowns is a fashionable ladies-wear chain of clothing stores, started in Kakamega, but now present in all the major towns in Kenya and in Kampala, Uganda and in Dar-es-salaam, Tanzania. The accounts of all the branches are maintained in the books of the head office, now situated in Nairobi. The figures below that refer to goods are stated at selling prices, following figures relate to transactions carried out by the Mombasa branch in the year ended 31 May 2011:

| | **Sh.'000'** |
|---|---|
| Opening stock at commencement of the year | 5,280 |
| Goods received from head office | 116,728 |
| Goods received from Voi branch | 560 |
| Goods sent to Taita branch | 720 |
| Goods returned to Mombasa branch by credit customer (normal goods) | 880 |
| Goods returned to Voi branch by Mombasa credit customer (approved by Head office: All these goods had been marked up by 15%) | 322<br>1,360 |
| Goods returned by Mombasa branch to Head office | 52,800 |
| Cash sales | 240 |
| Cash stolen from Mombasa branch on 12 December 2010 | 960 |
| Goods stolen from Mombasa branch on 12 December 2010 | 61,686 |
| Credit sales (mainly to boutiques in beach hotels) | 12,802 |

| | |
|---|---|
| Mombasa branch administrative expenses<br>Mombasa branch distribution costs | 17,072 |

**Additional information:**

1. The Mombasa branch is managed by a particularly competent group of women. Other than the thefts stated above, there were no shortages or surpluses of goods or cash during the year.
2. Demand for certain casual wear has been high during the year; to prevent stock-outs from occurring; these lines are normally marked up in price using a formula linked to the number of items sold in the proceeding week. Included in the opening stock were goods with a normal selling price of Sh. 800,000 but which had been marked up by a further 10% of this price. The normal selling price of the goods is head office cost plus 60% of cost. All these marked-up goods were sold in the year. Goods with a normal selling price of Sh. 1,120,000 had been marked up by an additional 15%. Three quarters of these goods had been sold by 31 May 2011.

3. In the income statements produced for management, cash stolen and goods stolen are shown as separate line items.

**Required:**

Prepare the Mombasa Branch Stock Account and the Mombasa Branch Mark-up Account in the books of the Head office, and the Memorandum Trading and Profit and Loss Account for the Mombasa Branch for the year ended 31 May 2011

**(Total: 17 marks)**

## QUESTION FOUR

a) The objective of IAS 29 is to establish specific standards for enterprises reporting in the currency of a hyperinflationary economy, so that the financial information provided is meaningful. Discuss this statement ( 5 marks )

**b)** BZT Ltd. which deals in farm implements prepares its financial statements using both the historical cost accounting method and the inflation adjusted accounting method.

Provided below are the historical cost accounting comparative balance sheets prepared as at 31 December 2012 and 2013 and the trading profit and loss account for the financial year ended 31 December 2013.

| | Balance sheet as at December | |
|---|---|---|
| | 2013<br>Sh. "000" | 2012<br>Sh. "000" |
| **Assets:** | | |
| Non-current assets: | | |
| Buildings | 815,000 | 600,000 |
| Machinery and equipment | 200,000 | 350,000 |
| | 1,015,000 | 950,000 |
| **Current assets:** | | |
| Stock | 420,000 | 340,000 |
| Debtors | 270,000 | 230,000 |
| Bank balance and cash in hand | 210,000 | 180,000 |
| | 900,000 | 750,000 |
| Total assets. | 1,915,000 | 1,700,000 |
| | | |
| **Equity and liabilities:** | | |
| Capital and reserves: | 600,000 | 500,000 |
| Ordinary share capital | 300,000 | 200,000 |
| Share premium | 490,000 | 380,000 |
| Retained profit | 1,390,000 | 1,080,000 |
| | | |
| Non-current liability: | | |
| 10% debentures | 300,000 | 400,000 |
| Current liabilities: | | |
| Trade creditors | 185,000 | 200,000 |
| Proposed dividend | 40,000 | 20,000 |
| | 225,000 | 220,000 |
| Total equity and liabilities | 1,915,000 | 1,700,000 |

| *Trading profit and loss account for the year ended 31 December 2013* | |
|---|---|
| | **Sh. "000"** |
| Sales: | 3,600,000 |
| Stock – 1 January 2013 | 340,000 |
| Purchase | 2,780,000 |
| | 3,120,000 |
| Less: Stock – 31 December 2013 | 420,000 |
| Cost of sales | (2,700,000) |
| Gross profit | 900,000 |
| Selling and distribution costs | (215,000) |
| Administration costs | (180,000) |
| Depreciation | (185,000) |
| Debenture interest | (35,000) |
| | (615,000) |
| Operating profit | 285,000 |
| Profit on disposal of equipment | 45,000 |
| Profit before tax | 330,000 |
| Tax | (120,000) |
| Profit after tax | 210,000 |
| Dividends: Paid | (60,000) |
| Proposed | (40,000) |
| | (100,000) |
| Retained profit for the year | 110,000 |
| Retained profit brought forward | 380,000 |
| Retained profit carried forward | 490,000 |

**Additional information:**

1. Sales, purchases, selling and distribution costs and administration costs occurred evenly during the year ended 31 December 2013.

2. Debenture interest is paid semi-annually on 30 June and 31December. Debentures amounting to Sh. Sh.100, 000, 000 were redeemed on 1 July 2013.

3. The company sold equipment with a net value of Sh.100, 000,000 on 30 September 2013 at a profit of Sh.45, 000,000. No depreciation was provided on this equipment for the year ended 31 December 2013.

4. On 31 March 2013, the company purchased a building at Sh.350, 000,000. A full year's depreciation was provided on this newly purchased building at the rate of 10% per annum. Depreciation was provided on the other assets as follows:

| | **Sh.** |
|---|---|
| Old buildings | 100,000,000 |
| Machinery and equipment | 50,000,000 |

5. The company issued new ordinary shares at premium on 31 March 2013. The old shares were issued at the time of incorporation of the company when the general retail price index (RPI) was 100.

6. The closing stocks represent one month's purchases.

7. Tax was paid in two equal instalments on 30 June and 31 December 2013, while interim dividends were paid on 30 September 2013.

8. The general retail price index moved uniformly in the year.

9. Relevant indices were as follows:

| | **Retail price index** |
|---|---|
| Date of purchase of: Old buildings | 105 |
| New building | 122 |
| Machinery and equipment including that sold in the year | 110 |
| 30 November 2012 | 119.5 |
| 31 December 2012 | 120 |

| | |
|---|---|
| 31 March 2013 | 123 |
| 30 June 2013 | 126 |
| 30 September 2013 | 129 |
| 30 November 2013 | 131.5 |
| 31 December 2013 | 132 |
| Average index for the year ended 31 December 2013 | 126 |

**Required:**

The following financial statements using the current purchasing power accounting method:

(a) Income statement account for the year ended 31 December 2013. (10 marks)

(b) Statement of financial position as at 31 December 2013. (5 marks)

**(Total: 20 marks)**

**QUESTION FIVE**

a) Distinguish between "leasing" and "hire purchase" highlighting how each is accounted for.
b) Nzoia Limited has been in business for several years dealing in electronic goods. All the firm's goods are sold on hire purchase terms. The following trial balance extracted from the books of the firm as at 31 March 2014:

| | Sh.'000' | sh.'000' |
|---|---|---|
| Ordinary share capital | | 53,200 |
| Cash at bank and in hand | 1,800 | |
| Accounts payable | | 5,000 |
| Operating expenses | 16,000 | |
| Property, plants and equipment (1 April 2013) | 55,000 | |
| Depreciation (1 April 2013) | | 20,000 |
| Hire purchase instalments receivable | 34,200 | |
| Hire purchase sales | | 55,200 |
| Purchases | 24,600 | |
| Inventory (1 April 2013) | 1,800 | |
| | 133,400 | 133,400 |

**Additional information:**

1. Inventory as at 31 March 2014 was valued at sh.2, 400,000.
2. Property, plant and equipment should be depreciated at sh.5, 000,000 for the year ended 31 March 2014.
3. Each unit was sold on hire purchase basis on the following terms:

| | Sh. | Sh. | |
|---|---|---|---|
| Cash price | 40,000 | | |
| Deposits | (10,000) | | 30,000 |
| Interest | | 6,000 | |
| | | 36,000 | |

4 Assume that all sales are made at the end of each quarter. The quarters end on 31 March, 30 June, 30 September and 31 December respectively. The balance due on each hire purchase sale is payable in four equal instalments of Sh. 9,000 per quarter payable at the end of each quarter and commencing in the quarter following that in which the sale was made.

5 The number of units sold during each quarter was made as follows:

| **Quarter to** | **Number of units sold.** |
|---|---|
| 30-Jun-13 | 100 |
| 30-Sep-13 | 200 |
| 31-Dec-13 | 300 |
| 31-Mar-14 | 600 |

All instalments were received on their due dates.

6 The sum of digits method is to be used to apportion interest, the appropriate amount being credited to the quarter in which an instalment is received.

7 Included in the operating expense is a lease rental payment of Sh.2, 000,000 paid at the commencement of the financial year. This relates to equipment whose fair value is Sh.8, 000,000. The payment has been treated as an operating lease whereas it is a finance lease. The duration of the lease is 5 years and interest is at 10% per annum. Lease rentals are paid in advance.

**Required:**

(I) Income statement for the year ended 31 March 2014. 8 marks)

(ii) Statement of Financial Position as at 31 March 2014 6 marks)

(Total: 20 marks)