TECHNICAL UNIVERSITY OF MOMBASA

School of Business

DEPARTMENT OF ACCOUNTING & FINANCE

UNIVERSITY EXAMINATION FOR:

BACHELOR OF SCIENCE IN MATHEMATICS AND FINANCE

BFI 4451 : FINANCIAL REPORTING

END OF SEMESTER EXAMINATION-MAIN EXAM

SERIES: DECEMBER 2024

TIME: 2 HOURS

Instructions to Candidates

You should have the following for this examination

-Answer Booklet, examination pass and student ID

This paper consists of **FIVE questions**.

Attempt **Question ONE** (Compulsory) and any other **TWO Questions**.

Do NOT write on the question paper.

Question ONE (Compulsory)

The draft summarized statements of financial position of Highland Ltd and Lowland Ltd at 31 December 20x2 are set out below. On 31 March 20x2 Highland Ltd acquired for cash 75% of the sh.1.00 ordinary shares in Lowland Ltd. The retained earnings of the two companies at 1 January 20x2 were sh.2.8 million and sh.1.5 million respectively.

	Highland Ltd		**Lowland Ltd**	
	Sh.000	**Sh.000**	**Sh.000**	**Sh.000**
ASSETS				
Non-current assets				
Property, Plant and equipment		3,560		2,800
Investment in Lowland Ltd		2,940		-
		6,500		2,800

Current Assets				
Inventories	1,150		550	
Trade receivables – group	400		-	
Trade receivables – other	1,500		800	
Cash and cash equivalents	100		50	
		3,150		1,400
Total Assets		9,650		4,200
EQUITY AND LIABILITIES				
Equity				
Ordinary Share Capital		3,500		900
Share Premium Account		700		170
Retained earnings		3,500		2,300
Total equity		7,700		3,370
Non-current liabilities				
Borrowings		1,100		110
Current liabilities				
Trade payables – group	-		400	
Trade payables – other	850		320	
		850		720
Total equity and liabilities		9,650		4,200

Additional information:

1. The fair value of Lowland Ltd.'s property on 31 March 20x2 was sh.200,000 above its carrying amount. All of this relates to the buildings element of the property, which is being depreciated at 4% per annum.

2. At the date of acquisition the replacement cost of raw material inventories was sh.400,000. The carrying amount was sh.300,000. At 31 December 20x2 30% of these raw materials remained in inventory. The rest had been converted to finished goods and sold to third parties.

3. Since the date of acquisition Highland Ltd. has sold to Lowland Ltd. inventories valued at sh.800,000; half of these goods remained in the inventories of Lowland

Ltd. at 31 December 20x2. Highland Ltd calculated the transfer price of the goods at cost plus a mark-up of 25%.

4. It is the accounting policy of Highland Ltd. to undertake annual reviews for goodwill impairment. At 31 December 20x2 and impairment of sh.20,000 was identified in respect of Lowland Ltd.

Required:

(a) Prepare the consolidated statement of financial position of Highland Ltd. as at 31 December 20x2. **(20 marks)**

(b) Explain the purpose of group financial statements and the concepts underlying their preparation. **(10 marks)**

Question TWO

Jambo ltd are specialist wholesalers. The following is their trial Balance as at 31st December, 2023:

	Dr	Cr
	Sh000	Sh000
Ordinary share capital of sh1.00 shares each		1,000,000
Share premium		120,000
General reserve		48,000
Retained earnings as at 31.12.2022		139,750
Inventory at 1.1.2023	336,720	
Sales		4,715,370
Purchases	2,475,910	
Return outwards		121,220
Return inwards	136,200	
Carriage inwards	6,340	
Carriage outwards	43,790	
Warehouse wages(average no. of workers 59)	410,240	
Salesmens' salaries (average no. of workers 21)	305,110	
Administrative wages and salaries	277,190	
Plant and Machinery	610,000	
Motor vehicle hire	84,770	
Provision for depreciation plant and machinery		216,290
General distribution expenses	27,130	
General administrative expenses	47,990	
Directors' remuneration	195,140	
Rent receivable		37,150

Trade debtors	1,623,570	
Cash at bank and in hand	179,250	
Trade creditors(payable before 31.3.2024)		304,570
Bills of exchange payable		57,000
	6,759,350	6,759,350

Notes

a) Inventory as at 31.12 2023: sh. 412,780,000, consists of goods for resale.
b) Plant and machinery is distributed : distributive 60%; administrative 40%.
c) Accrued auditors' remuneration: sh 71 million.
d) Depreciation to be charged on plant and machinery at 20% on the cost.
e) Of the motor hire, sh. 55 million is for distributive purposes.
f) Corporation tax on profits at a rate of 35% is estimated at sh. 238.5 million, and it is payable on 1.10.2024.
g) There is a proposed ordinary dividend on 37½% for the year.
h) All of the sales are on one type of goods. Net sales of sh. 3.62 billion have been made in Kenya with the reminder in Africa, and they are shown net of VAT.
i) Pension contributions for staff amounted to sh. 42, 550, 000 and NSSF contributions to sh. 80.12 million These figures are included in wages and salaries in the trial balance. No employee earned over sh. 30 million.
j) Plant of sh. 75 million had been bought during the year.
k) Directors' remuneration has been as follows:

	Sh.000
Chairman	46,640
Managing Director	51,500
Finance Director	46,000
Marketing Director	43,000
	187,140

In addition each of them drew sh. 2 million as directors' fees. Pension are the personal responsibilities of directors.

Required:
Subject to the limits of the information: Prepare

a) Income statement for the year ending 31.12.2023 and **(12 marks)**
b) A statement of financial position as at that date **(8 marks)**

The above statements should be in published form and accompanied by the necessary notes prescribed by the companies of Act . (**Total 20 marks)**

Question THREE

P,F, and R have been in partnership for a number of years, sharing profits/ losses in the ratio 5:3:2 as merchants under the name of Maendeleo merchants

They decided to convert their partnership into a limited company with effect from 1 January 20 x1.to be known as Shanzu Company Limited.

Immediately prior to this conversion, the balance sheet of the partnership as at 31 December 20x0 disclosed the following figures:

Non-current assets (at written down values)	Sh.000	Sh.000	Sh.000
Premises		40,000	
Equipment		25,000	
Motor vehicles		15,000	
Total			80,000
Current assets			
Inventory		70,000	
Account receivable		25,000	
Bank (No. 1 Account)		6,000	
Total		101,000	
Less Current Liabilities			
Accounts payable	21,000		
Bank (No 2 Account)	16,000		
Total		(37,000)	
Net current assets			64,000
Total net assets			144,000
Financed by: Capital and current accounts	Capital account	Current account	
	Sh.000	Sh.000	Sh.000
P	80,000	5000	
F	30,000	2000	
R	10,000	3000	
	120,000		120,000
		10,000	10,000
Long term liabilities			

Loan-P	4,000		
Loan – small businesses			
(financing) Ltd	10,000		14,000
Total capital and liabilities			144,000

The terms of the conversion are that Shanzu Co Ltd is to take over the assets and liabilities of Maendeleo Merchants as follows:

	Valuations for takeover
	Sh.000
Premises	90,000
Equipment	20,000
Vehicles	8,000
Inventory	70,000
Accounts Receivable	24,000
Bank(No.2 Account)	(See below)
Accounts Payable	21,000
Good will	7,000

The closing balance on Bank (No. 1 Account) is to be transferred to bank (No. 2 Account) before all the other dissolution entries are effected in partnership ledgers.

F took over one of the partnership cars at an agreed figure of sh. 1.5 million . All other liabilities were paid from the Bank (No. 2 Account).

The purchase consideration is discharged by an issue at par of sh. 48 million 11% Debentures (fully paid) to the partners in their capital account proportions as shown in the above statement of financial position, plus 432,000 ordinary shares in Shanzu Ltd of sh. 250 per share (fully paid) to make up the balance due to each partner.

Required:

a) Prepare the closing entries in the ledger of Maendeleo Merchants for the following accounts only:

- Realisation
- Capital
- Shanzu Ltd
- Bank No. 1 Account
- Bank No.2 Account **(15 marks)**

b) Prepare the business Purchase and Maendeleo Merchant's account in Shanzu co. Ltd's ledger **(5 marks)**

(**Total 20 marks)**

Question FOUR

(a)

i. What is the basic principle for accounting for income taxes under IAS 12 ? **(2 marks)**
ii. What are the methods of accounting in income tax **(2 marks)**
iii. Discuss 3 possible methods of accounting for deferred tax **(2 marks)**

(b) On January 2021 Baobab Company Ltd bought machinery at the cost of sh. 500 million, and depreciates it on a straight line basis over 5 years . For tax purposes machinery is depreciated at 25%, straight line per annum on the qualifying tax base. Tax losses may be carried back against taxable profits of the previous 5 years. In the year 2020, the enterprises taxable profit was sh. 250 million. Profits in subsequent years are expected to average the year 2020 profit. The corporate tax rate is 30%.

Required:

Show the deferred tax impacts for years 2021 to 2025. (14 marks)

Question FIVE

The objective of IAS 19 is to prescribe the accounting and disclosure for employee benefits, requiring an entity to recognize a liability where an employee has provided services and an expense when the entity consumes the economic benefits of employee service.

Required:

(a) Explain the following key terms under employee benefits:

i. Defined contribution plans **(2 marks)**

ii. Defined benefit plans (**2 marks)**

iii. Past service cost **(2marks**)

iv. Current service cost (**2marks)**

v. Interest cost **(2mark)**

(b) On 31st December 2024, Mtwapa Ltd discontinues a segment of its business dealing with production of cooking oil. The employees of the discontinued segment will earn no further benefits. The actuarial assumptions immediately before the curtailment show a defined benefit obligation with a net present value of ksh. 100 million and a plan assets with a fair value of Ksh. 82 million . The cumulative unrecognized actuarial gains amount to Ksh 5 million . Mtwapa Ltd had adopted the new standard on employee benefit on 1st January 2024 a time when the increased net liability was recognized as sh 10 million which was to be recognized over 5 years. The curtailment has reduced the net present value of the obligation by Ksh. 10 million .

Required:

Compute the amount of net liability to be recognized on the balance sheet as at 31 st December 2024. **(10 marks)**