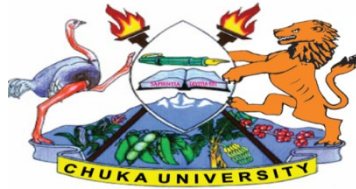


CHUKA



UNIVERSITY

## UNIVERSITY EXAMINATIONS

EXAMINATION FOR THE AWARD OF DEGREE OF BACHELOR OF MASTER OF  
BUSINESS ADMINISTRATION

MBAD 813: ADVANCED FINANCIAL ACCOUNTING

STREAMS: MBAD Y2S1

TIME: 3 HOURS

DAY/DATE: WEDNESDAY 07/04/2021

2.30 P.M – 5.30 P.M

## INSTRUCTIONS:

Answer question ONE and any other THREE questions.  
Do not write anything on the question paper

## QUESTION ONE

- a) Explain five reasons for group formations by companies. (10 marks)
- b) Bora limited, its subsidiary Ruka Limited and sub-subsidiary Leri limited operates in the media industry.

The following financial statements relates to the three companies for the year ended 31 December 2015.

## Income for the year ended 31 December 2015.

	Bora Ltd Sh'Million'	Ruka Ltd Sh'Million'	Leri Ltd Sh'Milli on'
Revenue	45,600	24,700	22,800
Cost of sales	<u>(18,050)</u>	<u>(5,463)</u>	<u>(5,320)</u>
Gross profit	27,550	19,237	17,480
Distribution Costs	(3,325)	(2,137)	(1,900)
Administration expense	(3,475)	(950)	(1,900)
Finance cost	<u>(325)</u>	<u>-</u>	<u>-</u>
Profit before tax	20,425	16,150	13,680

Income tax expense	<u>(8,300)</u>	<u>(5,390)</u>	<u>(4,241)</u>
Profit for the period	<u>12,125</u>	<u>10,760</u>	<u>9,439</u>
Retained profits brought forward	<u>10,513</u>	<u>13,315</u>	<u>10,459</u>
			<u>=</u>

**Statement of financial position as at December 2015**

	<b>Bora Ltd</b> <b>Sh'Million'</b>	<b>Ruka Ltd</b> <b>Sh'Million'</b>	<b>Leri Ltd</b> <b>Sh'Million'</b>
<b>Assets:</b>			
<b>Non-current assets:</b>			
Property, plant and equipment	35,483	24,273	13,063
Investment in Ruka limited	6,650	-	
Investment in Leri limited	<u>-</u>	<u>3,800</u>	<u>-</u>
	42,133	28,073	13,063
<b>Current Assets:</b>			
Inventory	462	4,265	3,682
Trade receivables	884	3,824	2,864
Cash at Bank and in hand	<u>222</u>	<u>936</u>	<u>2,337</u>
Total Assets	<u>43,701</u>	<u>37,098</u>	<u>21,946</u>
<b>Equity and Liabilities</b>			
<b>Capital and reserves</b>			
Ordinary shares (sh.100 par value)	8,000	3,000	2,000
Retained profits	<u>22,638</u>	<u>24,075</u>	<u>19,898</u>
Shareholder's fund	30,638	27,075	21,898
<b>Non-current liability</b>			
Loan from bank	3,250	-	-
<b>Current liabilities:</b>			
Trade payables	7,313	8,223	28
Current tax	<u>2,500</u>	<u>1,800</u>	<u>20</u>
Total equity and liabilities	<u>43,701</u>	<u>37,098</u>	<u>21,946</u>

**Additional information:**

1. Bora limited acquired 90% of the ordinary share capital of Ruka limited on 1 January 2010 when the retained profits Ruka limited were Sh.1,425 million. Subsequently Ruka limited acquired 80% of the ordinary share capital of Leri limited on 1 Jan 2012 when the retained earnings of Leri limited were Sh.950 million.
2. During the year 2015, Leri limited sold goods to Ruka limited at a selling price of Sh.480 million making a profit of 25% on cost. Sh. 75 million of these goods were still in the inventory of Ruka limited at the end of the year. Ruka limited still owed Leri limited sh.100 million as at 31 December 2015.
3. During the year, Ruka limited sold goods to Bora limited at a selling price of Sh.260 million making a profit of a third (1/3) on cost. Sh.60 million worth of these goods were still in the inventory of Bora limited as at the end of the year. Bora limited still owed Ruka limited Sh.50 million as at 31 December 2015.
4. During the year, Bora limited sold an item of plant to Ruka limited at a selling price of Sh.240 million reporting a profit of 20% on cost. The group charges depreciation at a rate of 20% and this is included as part of the cost of sales.
5. The entire goodwill of Ruka limited has been impaired and by 31 December 2014, 60% of the goodwill of Leri limited was impaired. An additional half of the balance of goodwill in Leri limited is considered impaired.

**Required:**

- (i) Consolidated income statement for the year ended 31 December 2015. [10 marks]
- (ii) Consolidated statement of financial position as at 31 December 2015. [10 marks]

**QUESTION TWO**

- a) The following information was extracted from the books of Waridi ltd for the year 2018. From the data given below calculate the gearing adjustment required under CCA method.

Current cost	Opening (shs)	Closing (shs)
Convertible Debentures	1,200,000	1,400,000
Bank overdraft	800,000	1,000,000
Cash	210,000	220,000
Paid up share capital	1,700,000	2,200,000
Reserves	100,000	180,000
COSA	200,000	
MWCA	150,000	
Depreciation	50,000	
	<b>400,000</b>	

**Required.** Calculate the gearing adjustment required under CCA method. (14marks)

- b) Explain any three features of Current Cost Accounting Method of accounting for price level changes. (6marks)

### QUESTION THREE

The following is a summarized statement of financial position of Real Tech ltd as at 30<sup>th</sup> June 2015.

	Sh'000	sh'000
Non-current assets		
Tangible assets -free hold property		85,000.00
Plant		10,000.00
tangible assets- patents	10,500.00	
Goodwill	<u>28,000.00</u>	38,500.00
Current assets		
Stock	85,000.00	
Debtors	97,000.00	
Investment (market value 25m)	11,000.00	
Deferred advertising	<u>20,000.00</u>	213,000.00

Current liabilities		
Bank overdraft	39,000.00	
Creditors	50,000.00	
Debenture interest payable	4,500.00	
Accruals	10,000.00	
Director's loan	<u>20,000.00</u>	(123,500.00)
		<u>223,000.00</u>
Financed by		
6% Cum. Preference shares @sh. 10		80,000.00
15M ordinary shares @sh. 10		150,000.00
Revenue reserves P&L		(82,000.00)
Non-current liabilities:6% debentures		75,000.00
		<u>223,000.00</u>

#### **Additional information**

The court approved the scheme of reorganization submitted by the major holders and agreed upon by other interested parties to take effect on 1<sup>st</sup> July, 2015 as follows;

- The preference shares to be written down to 7.5 and ordinary shares to sh.2 each
- The rate of dividends in preference shares be increased to 10%
- The preference dividends are for 4 years in arrears of which  $\frac{3}{4}$  are to be waived and ordinary shares to be allocated at par for the balance.
- The debenture holders to have their interest paid in cash and to take over free hold property whose book value is 20 million and is valued at Sh.24 million in part payment of their holding and also to provide additional capital of 26M secured by the floating charge over the company's assets at an interest rate of 12% p.a
- Patents goodwill and deferred advertising to be w/o (written off), sh. 15Million to be w/o on stock, sh.11.7 Million to be provided for bad debts and the remaining freehold property to be valued at sh.77.5M.
- Investments to be realized. The directors to accept settlement of their loans 90% therefore via allotment of ordinary shares at par and 5% in cash. The balance to be waived.

- The trade creditors to be paid sh.0.1 for every shilling and obtain an extension of a credit period.
- The bank sanctioned an overdraft limit of sh. 10M to provide working capital.
- There are capital commitments amounting to sh.75M which are to be cancelled on payment of  $3\frac{1}{3}\%$  of the contract price as penalty
- The authorized capital was restored to its original amount.

**Required**

- i) Capital reduction account to record the scheme of reorganization. (8marks)
- ii) A statement of financial position of Real tech ltd as at 1<sup>st</sup> July 2015 immediately after affecting the scheme. (12marks)

**QUESTION FOUR**

- (a) Discuss four limitations of financial statements prepared on the basis of historical cost accounting. (4marks)
- (b) Nyayo limited was established on 1 January 2011. Its opening statement of financial position as at this date was as follows:

	Sh'000'
Land	6,000
Equipment	4,000
Inventory	<u>2,000</u>
Equity	12,00
	0
	=====
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During the year ended 31December 2011, the company completed the following transitions.

- Purchased inventory at Sh.10,000,000
- Sold inventory for Sh.11,000,000 in cash. This inventory had a historical cost value of Sh.9,000,000.

**Additional information:**

1. Closing inventory on 31 December 2011 had a historical cost of Sh.3,000,000 and was bought when the retail price index (RPI) was 115 (average).
2. The equipment has an expected useful life of four years and a nil residue value.

3. The general price index during the year was as follows:

1 - Jan-11	100
30-Jun-11	110
31 -Dec-11	120

4. Assume that purchases and receipts occurred evenly throughout the year. 5. There were no debtors and creditors

**Required:**

- (a) The current purchasing power (CPP) Income statement for the year ended 31 December 2011. (8mks)
- (b) CPP Statement of financial position as at 31 December 2011. (8marks)

**QUESTION FIVE**

- a) IAS 1 prescribes the contents of published financial statements. Explain the five major reports that are included as part of the published financial statements. (10marks)
- b) Discuss the circumstances under which a company can be wound up. (10marks)
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