

CHUKA



UNIVERSITY

UNIVERSITY EXAMINATIONS

**SECOND YEAR EXAMINATION FOR THE AWARD OF DIPLOMA IN
ACCOUNTANCY**

DIAC 0221: INTERMEDIATE ACCOUNTING II

STREAMS: DIP. (DIAC)

TIME: 2 HOURS

DAY/DATE: FRIDAY 06/12/2019

8.30 A.M. – 10.30 A.M.

INSTRUCTIONS:

- Answer question ONE and any other TWO questions.

QUESTION ONE

- (a) Briefly explain the types of accounting changes. (6 marks)
- (b) OT Limited presented the following Trial balance as at 31st Dec 2015.

	Sh. '000'	Sh. '00'
Revenue		5,920
Cost of sales	4,080	
Distribution cost	432	
Administrative expenses	584	
Land	4,200	
Building at cost	3,200	
Acc. Depreciation 1 Jan 2015		852
Motor vehicle at cost	5,120	
Acc. Depreciation 1 Jun 2015		992
Ordinary shares sh. 40 each 1 Jan 2015		4,000
Share premium		1,200
Retained earnings		3,852
10% debentures		800
	<u>17,616</u>	<u>17,616</u>

Additional information

1. The estimated corporation tax for the year was estimated at 400,000.
2. The debenture interest for the year is to be accrued as at 31st Dec 2015.
3. Depreciation is treated as an administrative expense and is provided on building and motor vehicle at 4% on straight line and 25% on reducing balance basis respectively.
4. The directors propose to pay the ordinary shareholders a final dividend of sh. 1 per share for the year ended 31st Dec 2015.

Required:

Statement of comprehensive income, statement of financial position and statement of changes in equity for the year ended 31st Dec 2015. (20 marks)

- (c) Briefly describe a liability highlighting its main characteristics. (4 marks)

QUESTION TWO

- (a) With the use of examples, differentiate between ‘financial liabilities at amortized cost’ and financial liabilities at fair value through profit or loss (FVTPL). (4 marks)
- (b) Pingo Ltd raises finance by issuing zero coupon bonds at par on 1st Jan 2018, with nominal value of Sh. 20,000. The bonds will be redeemed after two years at a premium of Sh. 1,449. The effective rate of interest is 7%. The financial year ends on 31st December.

Required:

Explain and illustrate how the zero coupon bonds are accounted for in the financial statements of Pingo Ltd for the year ended 31st Dec 2018 and 2019. (10 marks)

- (c) Kamimo Ltd purchased an item of plant for Sh. 4,000,000 on 1st Jan 2014. It had an estimated life of 8 years and a residual value sh. 800,000. The plant was depreciated on a straight line basis. The tax authorities allowed 40% of the cost of this type of asset to be claimed against income tax in the year of purchase and 20% per annum on reducing balance basis of its tax base thereafter. The income tax rate is 30%.

Required

Journal entry to record deferred tax liability as at 30th Dec 2016. (6 marks)

QUESTION THREE

- (a) Electrical Ltd sold 100 washing machines in 2014 for Sh. 200,000 each, together with a two-year warranty. Based on management’s experience, the average maintenance cost on each machine during the warranty period was Sh. 20,000. The actual warranty cost incurred in 2014 and 2015 were Sh. 2,700,000 and Sh. 2,800,000 respectively.

Required

- (i) Journal entries to record the sale of the washing machines and the related warranty costs, assuming that the accrual method is used. (10 marks)
- (ii) The appropriate journal entries, assuming that the cash basis method is used. (4 marks)
- (b) Giving two examples in each case, differentiate between constructive obligation and legal obligation. (6 marks)

QUESTION FOUR

- (a) The summarized income statement of DL Limited for the year ended 31st Dec 2016 is as follows

	Sh. ‘000’
Profit after tax	480
Preference dividend	<u>(42)</u>
	438
Ordinary dividend	<u>(300)</u>
Retained earnings for the year	138
Retained earnings b/f	<u>266</u>
Retained earnings c/f	<u><u>404</u></u>

As at Jan 2016, the company had an issued share capital of 200,000 ordinary shares and Sh. 600,000 7% cumulative preference shares.

Required:

- Basic earnings per share (EPS) (10 marks)
- (b) By use of an example, analyse the effect of errors on balance sheet, income statement and balance sheet and income statement together. (10 marks)
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