CHUKA **UNIVERSITY**

UNIVERSITY EXAMINATIONS

EXAMINATION FOR THE AWARD OF DEGREE OF BACHELOR OF COMMERCE

BCOM 213: INTERMEDIATE ACCOUNTING II

STREAMS: **TIME: 2 HOURS**

DAY/DATE: THURSDAY 12/04/2018 **8.30 A.M. – 10.30 A.M.**

INSTRUCTIONS:

- **Attempt question one and any other two questions.**

(a) Great Ltd. presented the following trial balance as at 31st March 2017

	Sh. '000'	Sh. '000'
Revenue		2,648
Interest	3	
Purchases	1,669	
Distribution costs	514	
Administrative expenses	345	
Interim dividends paid	6	
Inventory as at 1 April 2017	444	
Trade receivables and trade payables	545	434
Cash and cash equivalents	576	
Ordinary shares (Sh. 10 each)		100
Share premium		244
General reserve		570
Retained Earnings as at 1 April 2017		349
4%, 10 year Debentures		150
Land and buildings: Cost (Land Sh. 60 million)	380	
Accumulated Depreciation		64
Plant and equipment: cost	258	
Accumulated Depreciation		126
Rental Income		55
	4,740	4,740

Additional information:

1. Closing inventory as at 31st March 2017 amounted to Sh. 388,000.
2. Land and building were revalued on 1st April 2017 to Sh. 800,000 (including land at Sh. 100,000). The buildings have a remaining useful life of 40 years.
3. The income tax liability in the year was estimated at Sh. 20,000. Differed tax was to be provided at Sh. 7,000.
5. Depreciation as per the company's policy are as follows:
   Building-over the useful life period
   Plant and equipment-20% reducing balance

The company accounting policy is to charge a full year's depreciation in the year of purchase and none in the year of disposal.

The company treats depreciation of plant and equipment as a cost of sale and on building as an administrative expense.

Required:

(a) The statement of comprehensive income for the year ended 31st March 2018. (10 marks)

(b) The statement of changes in equity as at 31March 2018. (3 marks)

(c) The statement of financial position as at 31March 2018. (7 marks)

(b) Briefly describe the distinction between financial liability and equity instrument. (4 marks)

(c) At the reporting date of BK Limited, inventory which cost Sh. 10,000 had been written down to its net realizable value of Sh. 9,000.
The applicable tax rate is 30 percent.

Required:

Deffered tax asset or liability (3 marks)

(d) A company has decided to change its depreciation method to better reflect the patterns of use of its equipment.

Required:
Identify the nature of accounting change and explain how it will be applied in the financial statements. (3 marks)

Question two

(a) Using examples differentiate between capital reserves and revenue reserves. (3 marks)

(b) On 1stJanuary 2016, Point Limited issued Sh. 650,000, 10% three-year debentures values when the effective rate of interest was also 10%. At the end of the first accounting period, market interest rates had fallen to 8%. In the subsequent year, the market rates rose to 12%. The liability is presumable being held for trading purposes. The issue costs incurred were Sh. 50, 000. The financial year of the company ends on 31st December.

Required:

(i) Explain how the bond is classified and show the journal entry in the book of Point Ltd on 1st January 2016. (2 marks)

(ii) Journal entries to record finance charges and stamen of Income extract for the year ended 31st December 2016, 2017 and 2018. (10 marks)

(c) Using illustrations, explain the distinction between a constructive obligation and equitable obligation. (4 marks)

Question three

(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) Real Ltd is a manufacturing company quoted on the Nairobi Securities Exchange. The following information was extracted from the records of the company.

1. On 1st January 2017, the company had an issued and outstanding share capital of 300,000 ordinary shares of Sh. 20 each and 100,000 8% preference shares of Sh. 50.
2. On 1st April 2017, the company made a rights issue of one fully paid share at Sh. 60 for every 3 ordinary shares when the shares were trading at Sh. 84 each.
3. On 1st October 2017, the company issued 200,000 ordinary shares at the market price.

4. The company reported profit after tax of Sh. 1,200,000 for the year ended 31st December 2017

Required:
Basic Earning per share for the year ended 31st December 2017. (10 marks)

(c) A company provides a two year warranty for a new product. It sold 6000 units of the product at Sh. 1, 000 per unit by the end of the year. From the past experience with a similar product the company estimates that warranty costs will amount to 1% of the sales revenue by the end of the year. The company has paid out Sh. 30,000 in relation to the warranty claims.

Required:
Journal entries to record the transactions in the books of the company assuming the company applies the accrual basis. (6 marks)

Question four

(a) The balance brought forward for deferred tax asset as at 1st January 2017 for ABC Ltd was Sh. 3 million. The taxable temporary differences as at 31st December 2017 amounted to Sh. 16 million. The applicable corporation tax a rate is 30%

Required;

Journal to record deferred tax liability for the year and the deferred tax account as at 31st December 2017. (10 marks)

(b) Define a provision and describe the conditions to be met for recognition for provisions. (6 marks)

(c) Life Ltd was incorporated on 1st January 2018 and issued 1,000,000 Sh. Ordinary Shares at a price of Sh. 110 per share. The issue costs incurred amounted to Sh. 100,000.

Required:
Journal entry record issue of the ordinary shares. (4 marks)
