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CPA PART II SECTION 3

FINANCIAL REPORTING

THURSDAY: 29 November 2018. **Time Allowed: 3 hours.**

Answer ALL questions. Marks allocated to each question are shown at the end of the question. Show ALL your workings.

QUESTION ONE

(a) The objective of International Accounting Standard (IAS) 2 "Inventories" is to prescribe the accounting treatment for inventories. IAS 2 provides useful guidance particularly in economies which are dependent on agriculture.

Required:
Summarise the key requirements of IAS 2 under the following headings:

(i) Scope of the term "inventories". (2 marks)

(ii) Measurement of inventories. (3 marks)

(iii) Disclosure requirements. (4 marks)

(b) The following trial balance relates to Marine Insurance Company Ltd. for the year ended 30 June 2018:

	Sh."000"	Sh."000"
Ordinary shares of Sh.10 each		50,000
9% cumulative preference shares		20,000
Statutory reserve		4,200
Retained earnings		15,800
Freehold land	18,000	
Building: Cost	60,000	
Accumulated depreciation		5,000
Equipment: Cost	60,000	
Accumulated depreciation		13,000
Government securities	28,500	
Investment in shares	12,500	
Claims paid	28,400	
Gross premiums earned		86,000
Re-insurance premiums ceded	10,700	
Legal expenses	3,800	
Commissions earned		450
Commissions payable	700	
Unearned premiums		47,500
Operating expenses	14,250	
Accrued preference dividends payable		5,400
Fees received		4,400
Repairs and maintenance	8,500	
Trade receivables	15,350	
Trade payables		8,500
Investment income		1,800
Claims outstanding		4,100
Bank balances	3,900	
Receivables arising out of re-insurance arrangements	1,550	
	266,150	266,150

Additional information:

1. The freehold land was revalued upwards by Sh.2 million but the revaluation had not been incorporated in the accounts.
2. Dividends on preference shares were in arrears for four years. The board has decided to pay the dividends for only three years.

3. Depreciation is to be charged per annum using the straight line method as follows:

Asset	Rate per annum
Building	2%
Equipment	15%

4. Claims amounting to Sh.2,850,000 were estimated to be outstanding as at 30 June 2018.
5. Current year's estimated tax is Sh.5,000,000.
6. Out of the total legal expenses incurred in the year ended 30 June 2018, Sh.2,450,000 was on claims paid.
7. The directors have recommended a first and final dividend of 20% on ordinary shares.

Required:

(i) Statement of comprehensive income for the year ended 30 June 2018. (6 marks)

(ii) Statement of financial position as at 30 June 2018. (5 marks)

(Total: 20 marks)

QUESTION TWO

Safina Ltd., a manufacturing company, presented the following trial balance as at 31 October 2018:

	Sh."000"	Sh."000"
Revenue		8,700
Purchases	1,500	
Production cost	1,200	
Administrative expenses	980	
Distribution cost	370	
Interest on loan	50	
Research and development	470	
Land and buildings at valuation (1 November 2017)	1,700	
Equipment at cost	4,500	
Investment property at valuation (1 November 2017)	2,200	
Accumulated depreciation (1 November 2017):		
Buildings		400
Equipment		450
Intangible asset at cost	500	
Accumulated amortisation (1 November 2017)		50
Inventory (1 November 2017)	50	
Bank balances	400	
Trade receivables	350	
10% bank loan		1,000
Interim dividend paid	350	
Trade payables		400
Corporation tax		35
Ordinary share capital		1,250
Share premium		250
Revaluation reserve (1 November 2017)		300
Retained earnings (1 November 2017)		1,785
	14,620	14,620

Additional information:

1. Included in the revenue is a government grant of Sh.150,000 that Safina Ltd. received. The grant relates to the employment of additional staff that is expected during the next financial year.
2. Research and development expenditure comprises the following:
   - Sh.80,000 on general research.
   - Sh.67,000 on developing new technology. At the year end, the directors do not think that the development will be successful.
   - Sh.323,000 on development of new production technology. The development is almost complete and the directors are highly confident that the technology will result in significant cost savings.
3. Intangible asset at cost relates to a development that was being amortised over a useful life of 10 years. As at 1 November 2017, this was reviewed and the development was then assessed as having a remaining useful life of six years.
4. The Sh.1,700,000 relating to land and buildings is based on last year's revaluation and includes land at a valuation of Sh.1,000,000. Land has an indefinite useful life. The buildings should be depreciated on the value at the start of the year and the remaining useful life was 20 years as at 1 November 2017.
5. As at the year end, the directors obtained the following valuations:
   - Land Sh.1,250,000
   - Buildings Sh.570,000