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CPA PART II SECTION 3

FINANCIAL REPORTING

FRIDAY: 27 November 2020. **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) Citing two examples, explain the accounting treatment of contingent assets. (4 marks)

(b) With reference to International Accounting Standard (IAS) – 16: Property, Plant and Equipment:

(i) Describe two conditions under which property, plant and equipment should be recognised. (4 marks)

(ii) Outline the provisions with regard to derecognition of property, plant and equipment. (4 marks)

(c) The objective of IFRS 15 – Revenue from Contracts with Customers, is to establish the principles that an entity shall apply to report useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue from a contract with a customer.

In context of the above statement:

(i) Discuss how contracts with customers will be presented in the financial statements in line with IFRS 15 requirements. (4 marks)

(ii) Summarise the disclosure requirements under IFRS 15. (4 marks)

(Total: 20 marks)

QUESTION TWO

The following trial balance relates to Tamutamu Ltd. as at 30 September 2019:

	Sh."000"	Sh."000"
Revenue		68,865
Inventory	3,150	
Cost of sales	35,500	
Selling and distribution expenses	5,600	
Administrative expenses	8,540	
Interest on loan note	110	
Investment income		360
Bank interest	85	
Leasehold building at valuation (1 October 2018)	14,000	
Plant and equipment – cost/depreciation	13,750	3,200
Computer equipment – cost/depreciation	7,200	2,000
Motor vehicles – cost/depreciation	1,500	400
Available for sale investments	8,700	
Trade receivables	9,200	
Bank balance		910
Trade payables		3,400
Deferred tax (1 October 2018)		2,300
Ordinary shares of Sh.29 each		14,500
8% loan note (2017 – 2021)		2,500
10% preference shares (redeemable)		3,000

	Sh."000"	Sh."000"
Revaluation surplus		800
General reserve		1,500
Retained earnings (1 October 2018)		3,600
	107,335	107,335

Additional information:

1. On 31 March 2019, the company made a bonus issue from retained earnings of one new share for every four shares in issue at Sh.10 each. This transaction is yet to be recorded in the books.

   The company paid ordinary dividends of Sh.2.20 per share on 31 January 2019 and Sh.2.60 per share on 30 June 2019. The dividend payments are included in administrative expenses in the trial balance.
2. Interest on loan notes and dividend on preference shares have not yet been accounted for.
3. Revenue includes Sh.8 million for credit sales made on a "sale or return basis". As at 30 September 2019, customers who had not paid for the goods, had the right to return Sh.2.6 million of them. Tamutamu Industries Ltd. applied a mark up of 30% on all sales. In the past, the company's customers have sometimes returned goods under this type of agreement.
4. Depreciation on property, plant and equipment is to be provided on the following basis; Plant and equipment – 10% on cost charged to cost of sales, computer equipment – 25% on cost charged to administrative expenses, motor vehicles – 20% on reducing balance charged to selling and distribution expenses.
5. Tamutamu Ltd. revalues its building at the end of each accounting year. At 30 September 2019, the relevant value to be incorporated into the financial statements was Sh.14,100,000.

   The building's remaining useful life at the beginning of the current year (1 October 2018) was 25 years. Tamutamu Ltd. does not make an annual transfer from the revaluation reserve to retained earnings in respect of the realisation of the revaluation surplus.

   Depreciation on building is an administrative expense. Ignore deferred tax on the revaluation surplus.
6. The available for sale investments held at 30 September 2019 had a fair value of Sh.8,400,000. There were no acquisitions or disposals of these investments during the year.
7. In February 2019, Tamutamu Ltd.'s internal audit unit discovered a fraud committed by the company's credit manager who did not return from a foreign business trip. The outcome of the fraud is that Sh.500,000 of the company's trade receivables have been stolen and are not recoverable. Of this amount, Sh.200,000 relates to the year ended 30 September 2018 and the remainder to the current year.
   Tamutamu Ltd. is not insured against this fraud.
8. Income tax payable on the profit for the year ended 30 September 2019 is estimated to be Sh.3,500,000. An amount of Sh.1,200,000 is to be transferred to the deferred tax account.

Required:

(a) A statement of comprehensive income for the year ended 30 September 2019. (10 marks)

(b) A statement of changes in equity for the year ended 30 September 2019. (2 marks)

(c) A statement of financial position as at 30 September 2019. (8 marks)

(Total: 20 marks)

QUESTION THREE

(a) With regard to International Public Sector Accounting Standard (IPSAS) 29 "Financial Instruments: Recognition and Measurement", describe the subsequent measurement of financial assets held by a public sector entity, indicating how this measurement differs from the requirements of International Financial Reporting Standard (IFRS) 9 "Financial Instruments: Recognition and measurement". (6 marks)

(b) The following are the draft statements of financial position of Aby Limited and Benta Limited as at 30 April 2020:

	Aby Limited Sh."million"	Benta Limited Sh."million"
Assets:		
Non-current assets:		
Property, plant and equipment	25,290	5,420
Investments	8,120	NIL
	33,410	5,420
Current assets:		
Inventory	2,750	1,295
Trade receivables	2,135	1,010

	Sh."million"	Sh."million"
Cash and bank balances	1,220	575
Total assets	39,515	8,300
Equity and liabilities:		
Equity:		
Ordinary shares of Sh.10 each	12,500	3,800
Revaluation surplus	2,700	260
Retained profit	13,600	2,350
	28,800	6,410
Non-current liabilities:		
Deferred consideration	1,800	NIL
10% debentures	2,450	500
Deferred tax	1,920	375
Current liabilities:		
Trade payables	3,200	655
Current tax	1,345	360
Total equity and liabilities	39,515	8,300

Additional information:

1. On 1 May 2019, Aby Limited acquired 80% of the share capital of Benta Limited. At this date, the retained profit of Benta Limited amounted to Sh.2,200 million and the revaluation surplus stood at Sh.260 million. Aby Limited paid an initial cash consideration of Sh.5,940 million and agreed to pay the owners of Benta Limited a further Sh.1,800 million on 1 May 2021. The accountant of Aby Limited has recorded the full amounts of both elements of the consideration in investments. Aby Limited has a cost of capital of 8% and the appropriated discount factor is 0.857.
2. On 1 May 2019, the fair values of Benta Limited's net assets were equal to their carrying amounts with the exception of some inventory which had cost Sh.193 million but had a fair value of Sh.233 million. On 30 April 2020, 10% of these goods remained in the inventory of Benta Limited.
3. During the year, Aby Limited sold goods worth Sh.515 million to Benta Limited at a profit mark up of 25% above the cost. At 30 April 2020, Benta Limited still held Sh.75 million of these goods in its inventory.
4. On 1 May 2019, Aby Limited also acquired an investment of 30% of the ordinary shares in Ceda Limited which cost Sh.380 million. Ceda Limited reported a profit of Sh.850 million during the year ended 30 April 2020.
5. Aby Limited has a policy of valuing non-controlling interests at fair value. On 1 May 2019, the non-controlling interest in Benta Limited had a fair value of Sh.1,317 million.
6. Impairment tests carried out on 30 April 2020 concluded that the value of the investment in Ceda Limited was impaired by Sh.85 million while the consolidated goodwill was impaired by Sh.100 million.

Required:

(i) Calculate the carrying amount of the investment in Ceda Limited to be included within the consolidated statement of financial position using the equity method. (2 marks)

(ii) The consolidated statement of financial position for the Aby Group as at 30 April 2020. (12 marks)

(Total: 20 marks)

QUESTION FOUR

Mika and Nira had been operating as sole traders. On 30 September 2018, they amalgamated and traded as partners under the name Minira Traders sharing profits and losses in the ratio of 4:1 respectively. One year later on 30 September 2019, they converted the partnership into a limited liability company trading as MN Ltd.

No adjustments have been made to record the amalgamation and conversion but the statements of financial position for the sole traders as at 30 September 2018 and the partnership as at 30 September 2019 were as follows:

	Sole Traders Statement of financial position as at 30 September 2018		Minira Traders Statement of financial position as at 30 September 2019
	Mika	Nira	
Assets:	Sh."000"	Sh."000"	Sh."000"
Freehold property	3,000	2,000	8,000
Plant and equipment	13,600	11,200	26,000
Fixtures and fittings	3,200	3,100	6,000
Inventory	3,600	700	6,700

	Sh."000"	Sh."000"	Sh."000"
Accounts receivable	3,800	2,000	12,840
Balance at bank	600	300	250
	27,800	19,300	59,790
Liabilities:			
Accounts payable	(13,600)	(8,000)	(19,840)
Bank overdraft	-	-	(11,250)
	14,200	11,300	28,700

Additional information:

1. On 1 October 2018, the partners agreed to take up the assets and liabilities of the individual traders at book values except for freehold property, plant and equipment and fixtures and fittings which were to be revalued as follows:

	Mika Sh."000"	Nira Sh."000"
Freehold property	4,000	3,000
Plant and equipment	13,000	11,000
Fixtures and fittings	3,000	3,000

2. During the year ended 30 September 2019, Mika made drawings of Sh.4,780,000 while Nira drew Sh.1,220,000.
3. The partnership was converted into a limited company, MN Ltd., on the following terms:
   (i) The freehold property and accounts receivable were revalued to Sh.12,000,000 and Sh.11,340,000 respectively.
   (ii) Mika and Nira were to receive 15% unsecured debentures at par so as to provide each partner with income equivalent to a 6% return on capital employed based on capital balances as at 30 September 2019 (that is after accounting for the profits, drawings and revaluation in note (i) above).
   (iii) MN Ltd.'s authorised share capital was made up of 150,000 ordinary shares of Sh.100 each out of which 130,000 shares were to be issued to the partners in their profit sharing ratio.
   (iv) Any balances in the partners' capital accounts were to be settled in cash.

Required:

(a) A computation showing the value of debentures and ordinary shares to be issued to the partners. (12 marks)

(b) Partners capital accounts as at 30 September 2019. (3 marks)

(c) Statement of financial position of MN Ltd. as at 30 September 2019. (5 marks)

(Total: 20 marks)

QUESTION FIVE

(a) The following trial balance was extracted from the books of David Wekesa, a farmer as at 31 October 2019:

		Sh."000"	Sh."000"
Inventory (1 November 2018):	Dairy cattle	54,900	
	Maize (growing)	3,600	
	Dairy cattle feeds	2,520	
	Fertilisers (for maize)	1,980	
Land and buildings		90,000	
Tractors (net book value)		32,400	
Other cattle (bulls)		6,000	
Carts (net book value)		3,000	
Purchases:	Dairy cattle	10,440	
	Fertilizers (for maize)	2,160	
	(for napier grass)	4,000	
	Maize seeds	1,080	
	Dairy cattle feeds	6,120	
Sales:	Milk		27,360
	Dry maize		36,000
	Green maize		11,340
	Dairy cattle		8,100
	Manure		3,000
Crop expenses:	Labour	6,480	
	Other expenses	720	
Napier grass (labour)		1,000	
General expenses		10,800	

		Sh."000"	Sh."000"
Trade payables			15,620
Capital (1 November 2018)			163,080
Cash at bank		15,300	
Dairy cattle expenses:	Medicine	1,080	
	Labour	9,480	
	Other expenses	1,440	
		264,500	264,500

Additional information:

1. Inventories as at 31 October 2019 were valued as follows:

	Sh."000"
Dairy cattle	54,000
Maize (growing)	2,700
Other cattle (bulls)	5,400
Dairy cattle feeds	1,620
Fertilizers for planting maize	1,080

2. During the financial year ended 31 October 2019, the following distributions of farm produce were made:

Product	Value Sh."000"
Maize consumed by family members	1,080
Milk delivered to relative's hotel	4,320
	5,400

3. Manure valued at Sh.600,000 was removed from the cow shed and used in the maize plantation.
4. Maize stocks valued at Sh.1,500,000 were used as dairy cattle feed.
5. Cattle bulls are used for pulling carts.
6. Depreciation is to be provided on tractors and carts on the reducing balance method at the rate of 25% and 12% per annum respectively.
7. Income tax is estimated at Sh.3,600,000.

Required:

(i) Revenue accounts for the year ended 31 October 2019. (6 marks)

(ii) Income statement for the year ended 31 October 2019. (3 marks)

(iii) Statement of financial position as at 31 October 2019. (3 marks)

(b) In the co-operative sector, a standardised accounting system is the use of similar accounting procedures in recording transactions. It means that similar documents and books of account are used in all societies of the same type.

Required:

Discuss four objectives of a standardised accounting system for co-operative societies. (8 marks)

(Total: 20 marks)

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CPA PART II SECTION 3

FINANCIAL REPORTING

WEDNESDAY: 27 November 2019. **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) International Accounting Standard (IAS) 10 defines events after the reporting date as those events which could be favourable or unfavourable, that occur between the end of the reporting period and the date that the financial statements are authorised for issue.

Required:
With reference to IAS 10:

(i) Distinguish between "adjusting" and "non-adjusting" events. (2 marks)

(ii) Describe the accounting treatment of events after the reporting period. (4 marks)

(b) Chanda, Pete and Tenda have been partners in a business for many years, sharing profits and losses in the ratio of 2:2:1 respectively.

On 30 June 2019, the partners agreed to convert their business into that of a limited liability company to be named Chapete Limited.

The trial balance extracted from the records of the partnership as at 30 June 2019 was as follows:

	Sh."000"	Sh."000"
Property at cost (Building: Sh.50 million)	60,000	
Plant and equipment at cost	25,000	
Motor vehicles at cost	12,000	
Furniture and fixtures at cost	4,000	
Provision for depreciation (1 July 2018):		
Building		5,000
Plant and equipment		13,000
Motor vehicles		4,800
Furniture and fixtures		1,600
Net profit for the year to 30 June 2019		28,800
Trade receivables and trade payables	18,200	14,700
Inventory (30 June 2019)	25,300	
Cash at bank balances	8,120	
Fixed capital accounts:		
Chanda		30,000
Pete		20,000
Tenda		10,000
Bank loan		18,000
Current accounts:		
Chanda		4,280
Pete		3,560
Tenda		2,340
Drawings:		
Chanda	1,580	
Pete	1,170	
Tenda	710	
	156,080	156,080

Additional information:

1. The property, plant and equipment in the partnership were being depreciated as follows:

Asset	Rate per annum	Basis
Building	2%	Straight line
Plant and equipment	12½%	Reducing balance
Motor vehicles	20%	Straight line
Furniture and fixtures	10%	Straight line

Depreciation for the year ended 30 June 2019 had not been provided for.

2. The partners were entitled to an interest on their fixed capital balances at the rate of 10% per annum. No salaries were paid to the partners.
3. The tangible non-current assets were to be transferred to the new company at their fair values as follows:

	Sh. "000"
Property	57,000
Plant and equipment	16,000
Motor vehicles	9,500
Furniture and fixtures	3,500

4. The current assets and the liabilities were taken over by the new company at their book values.
5. The purchase consideration amounted to Sh.110 million and was settled by the new company through the issue of ordinary shares of Sh.10 each to the partners in satisfaction of the amounts due to them upon conversion.

Required:

(i) Realisation account as at 30 June 2019. (6 marks)

(ii) Partners' capital accounts as at 30 June 2019. (4 marks)

(iii) Opening statement of financial position as at 1 July 2019 for Chapete Limited. (4 marks)

(Total: 20 marks)

QUESTION TWO

The following trial balance has been extracted from the accounting records of Skytex Limited as at 30 September 2019:

	Sh."000"	Sh."000"
6% convertible loan notes		25,000
Ordinary shares (Sh.10 each)		61,000
Retained earnings (1 October 2018)		177,000
Revenue		216,000
Cost of sales	108,500	
Distribution costs	23,600	
Administrative expenses	44,000	
Inventory (30 September 2019)	18,750	
Trade and other receivables	27,300	
Trade and other payables		23,800
Finance costs	6,200	
Investment income		600
Current tax		650
Deferred tax		13,900
Property at cost (Land: Sh.60 million)	170,000	
Accumulated depreciation (1 October 2018)		22,000
Plant and equipment at cost	56,000	
Accumulated depreciation (1 October 2018)		18,000
Bank balance	7,600	
Investment property	120,000	
Suspense account		24,000
	581,950	581,950

159 200

Additional information:

1. Skytex Limited entered into a contract with a customer where performance obligation is satisfied over time. The total contract price is Sh.45 million, with total expected contract costs of Sh.25 million.

   Progress towards completion was measured at 50% on 30 September 2018 and at 80% on 30 September 2019. The correct entries were made in the year ended 30 September 2018, but no entries have been made for the year ended 30 September 2019.

2. On 1 April 2019, Skytex Limited was notified that an ex-employee had initiated court proceedings against them for unfair termination. Legal advice was that there was an 80% chance that Skytex Limited would lose the case and would be required to pay an estimated amount of Sh.5.06 million in damages on 1 April 2020.

   Based on this advice, Skytex Limited recorded a provision of Sh.4 million on 1 April 2019 and has made no further adjustments.

   The provision was recorded in administrative expenses and in trade and other payables.

   Skytex Limited's cost of capital is 10% per annum and the discount factor at 10% for one year is 0.9091.

3. The company's policy on depreciation is to charge depreciation on building on straight line basis to a nil residual value at the rate of 2% per annum.

   The plant and equipment should be depreciated on reducing balance basis at the rate of 12.5% per annum. All depreciation should be charged to cost of sales.

4. The company issued Sh.25 million 6% convertible loan notes on 1 October 2018. Interest is payable annually in arrears. The loan notes can be converted into one share for every Sh.2 of the loan note on 30 September 2020. Similar loan notes, without conversion rights, incur interest at the rate of 8%.

   Skytex Limited recorded the full amount in liabilities and has recorded the annual interest payment made on 30 September 2019 of Sh.1.5 million in finance costs.

   Relevant discount factors are as follows:

Present value of Sh.1 in:	**6%**	**8%**
1 year	0.943	0.926
2 years	0.890	0.857

5. The balance of current tax in the trial balance relates to an under/overprovision from the prior period. The tax estimate for the year ended 30 September 2019 is Sh.10.5 million. In addition, there has been a decrease in taxable temporary differences of Sh.10 million during the year. Skytex Limited pays tax at the rate of 30% and movements in deferred tax are to be taken to the statement of profit or loss.
6. On 1 February 2019, Skytex Limited issued 1.5 million ordinary shares at their full market price of Sh.16 per share. The proceeds were credited to a suspense account.
7. The investment property in the trial balance is stated at fair value as at 30 September 2018. The fair value as at 30 September 2019 amounted to Sh.121.5 million.

Required:

Prepare the following financial statements in a suitable format for publication:

(a) A statement of profit or loss for the year ended 30 September 2019. (8 marks)

(b) A statement of changes in equity for the year ended 30 September 2019. (4 marks)

(c) A statement of financial position as at 30 September 2019. (8 marks)

Note: All workings should be done to the nearest Sh."000".

(Total: 20 marks)

QUESTION THREE

(a) International Financial Reporting Standard (IFRS) 15 – Revenue from Contracts with Customers, specifies how and when an entity will recognise revenue.

The standard provides a single principle based five step model to be applied to all contracts with customers.

Required:
Describe the five-step model as specified under IFRS 15. (10 marks)

(b) The following trial balance was extracted from the books of Maweo Insurance Company Limited as at 30 September 2019:

			Sh."000"	Sh."000"
Property, plant and equipment			10,500	
Depreciation of non-current assets			905	
Investment in government bonds and other securities			1,400	
Gross premiums received from agents	-	Marine		3,000
	-	Fire		2,500
Gross premiums received from brokers	-	Marine		1,500
	-	Fire		600
Gross premiums received from direct clients	-	Marine		500
	-	Fire		1,000
Reinsurance premiums accepted	-	Marine		600
Reinsurance premiums ceded	-	Marine	700	
	-	Fire	300	
Sundry receivables			750	
Bank			90	
Directors fees			495	
Audit fee			240	
Unearned premiums as at 1 October 2018	-	Marine		4,800
	-	Fire		2,500
Claims outstanding as at 1 October 2018	-	Marine		1,100
	-	Fire		840
Claims paid	-	Marine	2,770	
	-	Fire	2,100	
Legal cost on claims	-	Marine	280	
	-	Fire	130	
Survey expenses on marine claims			220	
Bad debts	-	Marine	370	
	-	Fire	320	
Management expenses	-	Marine	450	
	-	Fire	380	
Trade payables				230
Investment income				280
Ordinary shares of Sh.1,000 each				4,000
Retained profits (1 October 2018)				450
Premiums outstanding (1 October 2018)	-	Marine	800	
	-	Fire	700	
			23,900	23,900

Additional information:

1. Premiums outstanding as at 30 September 2019 amounted to Sh.1,970,000 and Sh.1,200,000 for Marine Insurance and Fire Insurance respectively.
2. Claims intimated and outstanding as at 30 September 2019 amounted to Sh.750,000 for Marine Insurance and Sh.480,000 for Fire Insurance.
3. Unearned premium is maintained at 100% and 50% of the premiums received for marine insurance and fire insurance respectively.
4. The tax rate applicable is 30%.

Required:

(i) Revenue accounts for both marine and fire insurance for the year ended 30 September 2019. (6 marks)

(ii) Statement of financial position as at 30 September 2019. (4 marks)

(Total: 20 marks)

QUESTION FOUR

(a) With reference to International Public Sector Accounting Standard (IPSAS) 5: "Borrowing Costs", explain the accounting treatment of borrowing costs in the financial statements of a public sector entity and indicate how this treatment differs from the requirements of International Accounting Standard (IAS) 23: "Borrowing Costs". (4 marks)

(b) On 1 July 2018, Beyond Ltd. held a number of insignificant investments in equity instruments that do not have a quoted price and are therefore carried at cost. During the year ended 30 June 2019, Beyond Ltd. acquired a subsidiary company, Horizon Ltd. and an associate company, Sky Ltd.

The draft summarised statements of financial position of Beyond Ltd. and its subsidiary company as at 30 June 2019 are shown below:

Assets:	**Beyond Ltd.**	**Horizon Ltd.**
Non-current assets:	**Sh."000"**	**Sh."000"**
Property, plant and equipment	1,162,800	321,390
Investments	774,500	-
	1,937,300	321,390
Current assets:		
Inventories	523,600	398,500
Trade and other receivables	401,860	203,650
Cash and cash equivalents	52,600	1,100
	978,060	603,250
Total assets	**2,915,360**	**924,640**
Equity and liabilities:		
Equity:		
Ordinary share capital (Sh.10 each)	600,000	200,000
Share premium	100,000	50,000
Retained earnings	1,776,260	502,540
	2,476,260	752,540
Current liabilities:		
Trade and other payables	385,200	148,500
Income tax	53,900	23,600
	439,100	172,100
Total equity and liabilities	**2,915,360**	**924,640**

Additional information:

1. Beyond Ltd. acquired 80% of the ordinary shares of Horizon Ltd. on 1 January 2019. The purchase consideration was made up of cash of Sh.650 million paid on 1 January 2019 and a further cash payment of Sh.147 million deferred until 1 January 2020. No accounting entries have been made in respect of the deferred cash payment. An appropriate discount rate is 5% per annum. Beyond Ltd. recognises goodwill on non controlling interest using the fair value method.
2. The fair value of the assets, liabilities and contingent liabilities as at 1 January 2019 were equal to their carrying value with the exception of a machine which had a fair value of Sh.60 million in excess of its carrying amount. This machine had a 6 years remaining useful life on 1 January 2019.
3. The fair value of the non controlling interest in Horizon Ltd. on 1 January 2019 was estimated at Sh.150 million.
4. In June 2019, Horizon Ltd. sold goods to Beyond Ltd. for Sh.16 million. Half of these goods were still held in the stock of Beyond Ltd. on 30 June 2019. Horizon Ltd. marks up all goods by 20%.
5. On 30 June 2019, Horizon Ltd.'s trade receivables still included the Sh.16 million due from Beyond Ltd. However, Beyond Ltd.'s trade payables only included Sh.11 million in respect of this transaction as it had made a payment of Sh. 5 million to Horizon Ltd. on 30 June 2019.
6. On 1 July 2018, Beyond Ltd. acquired 30% of the ordinary shares in Sky Ltd. for cash payment of Sh.120.5 million which gave Beyond Ltd. significant influence over Sky Ltd. At that date, a property owned by Sky Ltd. had a fair value of Sh.50 million in excess of its carrying amount. This property had a remaining useful life of 20 years on 1 July 2018.
7. In the year ended 30 June 2019, Horizon Ltd. made a profit of Sh.56.8 million out of which it paid a dividend of Sh.20 million on 30 April 2019. Beyond Ltd. debited the dividend received to cash and credited it to investments.

Required:

Consolidated statement of financial position as at 30 June 2019. (16 marks)

(Total: 20 marks)

QUESTION FIVE

(a) With reference to International Accounting Standard (IAS) 41 – Agriculture, discuss the accounting treatment of a biological asset. (4 marks)

(**Note:** Do not discuss the disclosure requirements).

(b) The following financial statements relate to Orlando Bank Ltd. for the year ended 31 October 2019:

Statement of comprehensive income for the year ended 31 October 2019:

	Sh."000"
Interest income	364,524
Interest expense	(107,571)
Net interest income	256,953
Fees and commission income	132,374
Fees and commission expense	(24,183)
	108,191
Other income	9,727
Operating income	374,871
Impairment charge on loans and advances	(93,492)
Operating expenses	(169,317)
Profit before tax	112,062
Income tax expense	(33,617)
Profit for the year	78,445

Statement of financial position as at 31 October:

	2019	2018
Assets:	**Sh."000"**	**Sh."000"**
Cash and cash equivalents	577,767	752,303
Government securities	2,037,292	1,851,337
Advances to banks	214,875	107,407
Loans and advances to customers	1,190,782	1,145,133
Property and equipment	139,889	123,936
Intangible assets	18,131	12,162
Income tax assets	6,626	5,778
Equity and liabilities	**4,185,362**	**4,004,056**
Equity and liabilities:	**Sh."000"**	**Sh."000"**
Share capital	100,000	100,000
Retained earnings	545,238	466,793
	645,238	566,793
Labilities:		
Deposits from customers	3,368,406	3,078,071
Other liabilities and provisions	171,718	359,192
	3,540,124	3,437,263
Total equity and liabilities	**4,185,362**	**4,004,056**

Bank balance
5080
104,920
Bank c/a ~~135~~

Additional information:

1. Interest income comprised:

	Sh."000"
Cash and short term funds	37,652
Loans and advances	326,872
	364,524

During the year, interest received amounted to Sh.131,292,000 while interest paid amounted to Sh.94,578,000.

2. Interest expense comprised:

	Sh."000"
Current and savings account	57,253
Time and other deposits	38,828
Borrowings	11,490
	107,571

3. Other income comprised:

	Sh."000"
Dividends	9,685
Profit on sale of property and equipment	42
	9,727

Dividends paid during the year amounted to Sh.4,800,000.

4. Operating expense comprised:

	Sh."000"
Staff salaries	125,160
Advertising and marketing expenses	498
Training cost	4,241
Audit fees	696
Directors fees	1,957
Depreciation of property and equipment	30,688
Amortisation of software	6,077
	169,317

5. **Property, plant and equipment movement schedule:**

	2019	2018
Cost:	**Sh."000"**	**Sh."000"**
Balance brought forward	228,657	165,128
Additions	46,641	63,672
Disposal	(120)	(143)
Balance carried down	275,178	228,657
Depreciation:		
Balance brought forward	104,721	83,729
Charge for the year	30,688	21,135
Released on disposal	(120)	(143)
Balance carried down	135,289	104,721
Net book value	139,889	123,936

6. **Intangible assets:**

	2019	2018
Cost	**Sh."000"**	**Sh."000"**
Balance bought forward	24,241	13,077
Additions	12,046	11,164
Balance carried down	36,287	24,241
Amortisation:		
Balance brought forward	12,079	9,123
Charge for the year	6,077	2,956
Balance carried down	18,156	12,079
Net book value	18,131	12,162

Required:

Using the indirect method, prepare a statement of cash flows for the year ended 31 October 2019 in accordance with International Accounting Standard (IAS 7): Cash Flow Statement. (16 marks)

(Total: 20 marks)

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129,700

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CPA PART II SECTION 3

FINANCIAL REPORTING

THURSDAY: 23 May 2019. **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

The following trial balance was extracted from the books of Sombea Ltd. as at 31 March 2019:

	Sh."000"	Sh."000"
Land and buildings at valuation (1 April 2018)	468,000	
Plant at cost	460,800	
Accumulated depreciation (1 April 2018)		115,200
Available for sale investments	95,400	
Investment income		7,920
Cost of sales	321,120	
Distribution costs	39,600	
Administrative expenses	45,000	
Debenture interest paid	2,880	
Inventory (31 March 2019)	136,440	
Income tax liability		41,760
Trade receivables	126,360	
Revenue		649,440
Ordinary shares of Sh.50 (at par value)		216,000
Retained earnings (1 April 2018)		91,800
4% debentures		288,000
Trade payables		124,920
Revaluation surplus (Land and buildings)		50,400
Suspense account		86,400
Bank		23,760
	1,695,600	1,695,600

Additional information:

1. The 4% debentures were issued on 1 October 2018 under terms that provided for a large premium on redemption in year 2021. The finance officer has calculated that the effect of this is that the debenture has an effective interest rate of 6% per annum.
2. A provision of Sh.61,560,000 should be made for tax on the profit for the year ended 31 March 2019.
3. The suspense account contains the corresponding credit entry for the proceeds of a rights issue of shares made on 1 January 2019. The terms of the issue were one share for every four shares held at Sh.80 per share. Sombea Ltd.'s share price immediately before the issue was Sh.100. The issue was fully subscribed.
4. The fair value of available for sale investments as at 31 March 2019 was Sh.97,560,000.
5. Sombea Ltd. has a policy of revaluing its land and buildings at each year end. The valuation in the trial balance includes land element of Sh.108,000,000. The estimated remaining life of the buildings as at that date (1 April 2018) was 20 years. On 31 March 2019, a professional valuer valued the buildings at Sh.331,200,000 with no change in the value of the land. Depreciation on buildings is charged 60% to cost of sales and 20% each to distribution costs and administrative expenses.
6. During the year, Sombea Ltd. manufactured an item of plant which it was using as part of its own operating capacity. The details of the plant's cost which is included in the cost of sales in the trial balance, are:

	"Sh.000"
Material cost	21,600
Direct labour cost	14,400
Machine time cost	28,800
Directly attributable overheads	21,600

The manufacture of the plant was completed on 30 September 2018 and the plant was brought into immediate use, but its cost has not yet been capitalised. All plant is depreciated at a rate of 12.5% per annum (time apportioned where relevant) using the reducing balance method and charged to cost of sales. No non-current assets were sold during the year.

Required:

(a) Statement of comprehensive income for the year ended 31 March 2019. (8 marks)

(b) Statement of financial position as at 31 March 2019. (12 marks)

(Total: 20 marks)

QUESTION TWO

Fanaka Ltd. acquired 90% of the ordinary shares of Sh.10 par value in Mali Ltd. on 1 January 2015 when Mali Ltd. had revenue reserves of Sh.1,500 million.

Mali Ltd. acquired 160 million ordinary shares of Sh.10 par value in Kwetu Ltd. on 1 January 2016 when Kwetu Ltd. had revenue reserves of Sh.500 million.

The financial statements of the three companies for the year ended 31 December 2018 are provided below.

Income statement

	Fanaka Ltd. Sh."million"	Mali Ltd. Sh."million"	Kwetu Ltd. Sh."million"
Revenue	7,200	4,700	2,450
Cost of sales	(5,400)	(3,760)	(1,715)
Gross profit	1,800	940	735
Investment income	218	40	-
	2,018	980	735
Operating expenses	(740)	(390)	(295)
Profit before tax	1,278	590	440
Income tax expense	(420)	(230)	(176)
Profit after tax	858	360	264
Dividend - Paid	(200)	(120)	(100)
- Proposed	(300)	(120)	(100)
Retained profit	358	120	64

Statements of financial position as at December 2018:

	Fanaka Ltd. Sh."million"	Mali Ltd. Sh."million"	Kwetu Ltd. Sh."million"
Non-current assets:			
Property, plant and equipment	15,500	9,700	6,500
Goodwill	-	-	500
Investment in - Mali Ltd.	8,400	-	-
- Kwetu Ltd.	-	3,500	-
Current assets	4,400	2,800	1,700
	28,300	16,000	8,700
Equity and liabilities:			
Ordinary share capital	10,000	6,000	4,000
Share premium	4,000	2,500	2,500
Revenue reserves	3,800	2,720	1,354
	17,800	11,220	7,854
Non-current liabilities:			
Bank loan	8,000	3,000	-
Current liabilities	2,500	1,780	846
	10,500	4,780	846
	28,300	16,000	8,700

Additional information:

1. On 31 December 2017, Mali Ltd. held stock bought from Fanaka Ltd. for Sh.120 million and on which Fanaka Ltd. had made a profit of $33^1/_3$% on cost.
2. In the year ended 31 December 2018, Fanaka Ltd. made sales of Sh.400 million to Mali Ltd. at a profit of 20% on selling price. One quarter of the goods purchased by Mali Ltd. from Fanaka Ltd. in the year remained unsold as at 31 December 2018.

3. All the three companies paid the interim dividend on 15 June 2018. No company has accrued its share of proposed dividend from either its subsidiary or associate company.
4. The inter-company outstanding balances as a result of trading were as follows:
   - Due from Fanaka Ltd. to Mali Ltd. Sh.45 million.
   - Due from Mali Ltd. to Kwetu Ltd. Sh.20 million.
5. Any goodwill on acquisition of the subsidiary or associate is considered impaired by 20%.
6. Fair value of tangible assets were not materially different from their book values on the date Fanaka Ltd. acquired its control in Mali Ltd. and on the date Mali Ltd. acquired its holding in Kwetu Ltd.

Required:

(a) Consolidated income statement for the year ended 31 December 2018. (8 marks)

(b) Consolidated statement of changes in equity. (2 marks)

(c) Consolidated statement of financial position as at 31 December 2018. (10 marks)

(Total: 20 marks)

QUESTION THREE

(a) Describe the two types of post-employment benefit plans in accordance with International Accounting Standard (IAS) 19 "Employee Benefits". (6 marks)

(b) Exe, Wye and Zed have been partners for several years in a partnership business under the name, Eweza Holdings. Due to successive trading losses that the business has been posting in recent years, the partners agreed to dissolve their business with effect from 1 July 2018.

The latest statement of financial position of the firm as at 30 June 2018 showed:

		Sh. "000"
Non-current assets:	Land and building	18,400
	Motor vehicles	8,200
	Furniture and fixtures	3,100
	Investment in shares	4,600
		34,300
Current Assets:	Inventories	4,750
	Trade receivables	3,200
Total assets		42,250
Capital and liabilities:		
Capital accounts:	Exe	14,400
	Wye	7,200
	Zed	3,600
Current accounts:	Exe	2,700
	Wye	1,900
	Zed	600
Loan from a Sacco		4,000
Current liabilities:	Trade payables	6,400
	Bank overdraft	1,450
		42,250

Additional information:

1. The partners shared profits and losses in the ratio of 2:2:1 for Exe, Wye and Zed respectively.
2. Partner Wye agreed to settle the unsecured loan from the Sacco while Zed took over some of the inventory valued at Sh.2 million.
3. The trade payables accepted Sh.5.8 million in full settlement of the amounts due to them.
4. The assets of the partnership were auctioned and realised in stages on piece-meal basis as follows:

Date	Assets realised	Amount Sh."000"
20 July 2018:	Trade receivables (part)	2,200
	Inventory (part)	1,750
	Investment in shares	4,400
	Motor vehicles (part)	7,000
31 July 2018:	Trade receivables (balance)	1,000
	Furniture and fixtures	2,900
25 August 2018:	Inventory (balance)	700
	Motor vehicles (balance)	2,000
10 September 2018:	Land and building	18,000

5. The auctioneers fees were agreed at Sh.3.5 million and were to be paid upfront immediately there was an available bank balance.
6. The rule in Garner vs. Murray applies where necessary.

Required:

(i) A schedule of payments to the partners using the maximum possible loss method. (8 marks)

(ii) Realisation account. (3 marks)

(iii) Partners capital accounts. (3 marks)

(Total: 20 marks)

QUESTION FOUR

(a) Distinguish between the following terminologies as used in construction contracts:

(i) "Lumpsum contract" and "percentage rate contract". (4 marks)

(ii) "Indemnity clause" and "retention clause". (4 marks)

(b) Discuss two methods of determining the stage of completion of a construction contract. (4 marks)

(c) Mijengo Construction Ltd. carried out work on four construction contracts during the financial year ended 30 April 2019.

The details of the contracts are set out below:

	AO1 Sh."million"	**BO2** Sh."million"	**CO3** Sh."million"	**DO4** Sh."million"
Contract price	780	1,200	1,020	948
Costs to date	180	480	963.6	33.6
Estimated total cost	720	768	1,069.2	840
Payment on account	156	780	918	24
Revenue recognised in previous periods	78	180	504	-
Cost recognised in previous periods	60	72	480	-
Administrative expenses	1.5	15	2.5	-
Date of commencement	1 May 2017	1 February 2017	1 March 2017	1 March 2019

Additional information:

1. The company does not recognise profits until the contract is at least 5% complete.
2. The company's policy is to calculate the percentage of completion on cost basis.
3. The company prepares separate trading accounts for each contract.

Required:

(i) Trading account for each of the contracts showing clearly the revenue to be recognised for the year ended 30 April 2019. (3 marks)

(ii) An income statement extract for the year ended 30 April 2019. (3 marks)

(iii) An extract of the statement of financial position showing the combined totals for all the contracts. (2 marks)

(Total: 20 marks)

QUESTION FIVE

(a) In the context of International Accounting Standard (IAS) 16 "Property, Plant and Equipment", explain four disclosure requirements for items of property, plant and equipment which are stated at revalued amounts. (8 marks)

(b) Baraka Ltd. is a manufacturing firm with its head office in Kisumu, Kenya and a branch in Entebbe, Uganda. The branch carries out the final assembly of the products before selling them. The currency in Kenya is the Kenya shilling (Ksh.) while the currency in Uganda is the Uganda shilling (Ush.). The trial balances for both the head office and the branch in their respective currencies as at 31 March 2019 were as follows:

	Head office (Ksh.)		Branch (Ush.)	
	Sh."000"	Sh."000"	Sh."000"	Sh."000"
Sales		416,000		1,728,000
Freehold building at cost	56,000		252,000	
Trade receivables and trade payables	35,600	38,000	144,000	6,240
Share capital		160,000		
Goods sent to branch		140,000		
Head office/Branch account	240,400			2,017,040
Cost of sales (branch)			1,440,000	
Provision for depreciation on machinery		6,000		226,800
Head office cost of sales (including goods sent to branch)	236,000			
Administrative cost	60,800		72,000	
Inventory - 31 March 2019	115,600		46,080	
Profit and loss account - 1 April 2018		8,000		
Machinery at cost	24,000		504,000	
Remittances		112,000	1,088,000	
Bank balance	18,400		316,800	
Selling and distribution costs	93,200		115,200	
	880,000	880,000	3,978,080	3,978,080

Additional information:

1. The branch remitted Ush.64,000,000 on 30 March 2019 which was not received by the head office until 3 April 2019. The amount realised was Ksh.7,960,000.
2. In the month of February 2019, a customer of the branch paid the head office for goods supplied by the branch. The amount due from him was Ush.1,280,000 which realised Ksh.144,000. It has been correctly dealt with by the head office but not yet entered in the branch accounts.
3. Commission which is payable to the branch manager, is to be provided at a rate of 5% of the net profits of the branch after charging such commission.
4. The cost of sales figure includes a depreciation charge of 10% par annum on the cost of machinery.
5. A provision of Ksh.1,200,000 for unrealised profit in the branch inventory is to be made.
6. The relevant exchange rates were as follows:

	Ksh.	To	Ush.
On 1 April 2018	1		20
On 31 March 2019	1		16
Average rate for the year ended 31 March 2019	1		18
On date of purchase of freehold building and machinery	1		14

Required:

(i) Branch trial balance (after the necessary adjustments) in Kenya shillings. (4 marks)

(ii) Income statement for the head office, the branch and the combined business for the year ended 31 March 2019. (4 marks)

(iii) Combined statement of financial position as at 31 March 2019 (ignore the effects of taxation). (4 marks)

(Total: 20 marks)

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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

6. Equipment is depreciated on a straight line basis over 5 years. Safina Ltd. estimates that the equipment is used in the business on the following basis:
- 50% in production
- 25% in the administration functions
- 25% in distribution functions

7. The year end valuation of the investment property was Sh.2,500,000 and Safina Ltd.'s accounting policy is to use the fair value model for investment properties.
8. The year end inventory was valued at Sh.65,000 but it was subsequently discovered that goods included within this value with a cost of Sh.7,000 were sold for Sh.2,000.
9. Safina Ltd. took out the bank loan of Sh.1,000,000 on 1 November 2017 which is repayable in four equal annual instalments. The interest rate on the loan is 10% per annum payable semi-annually.
10. The corporation tax for the previous year was settled in July 2018 and the estimate for corporation tax for the year ended 31 October 2018 is Sh.625,000.
11. The directors have also discovered that a customer who owed Sh.125,000 as at the year end was declared bankrupt.

Required:

(a) A statement of comprehensive income for the year ended 31 October 2018. (10 marks)

(b) A statement of financial position as at 31 October 2018. (10 marks)

(Total: 20 marks)

QUESTION THREE

(a) International Financial Reporting Standard (IFRS) 9 "Financial Instruments" establishes principles of derecognising financial assets and financial liabilities. Derecognition is the removal of a previously recognised financial instrument from an entity's statement of financial position.

Required:

With reference to the principles of IFRS 9, describe the criteria for derecognition of financial assets and financial liabilities of an entity. (6 marks)

(b) The following financial statements relate to Sasumua Ltd. and its investment companies for the year ended 30 September 2018:

Consolidated statement of comprehensive income for the year ended 30 September 2018:

	Sh."million"
Revenue	4,805
Cost of sales	(3,844)
Gross profit	961
Other income	21
Selling and distribution costs	(283)
Administrative expenses	(304)
Finance costs	(85)
Share of profit of joint venture	85
Profit before tax	395
Income tax expense	(80)
Profit for the year	315
Other comprehensive income:	
Revaluation gain on property, plant and equipment (net of deferred tax)	105
Total comprehensive income	420
Profit for the year:	
Attributable to the owners of the parent	290
Attributable to the non-controlling interests	25
	315

Consolidated statement of financial position as at 30 September:

	2018	2017
Assets:	Sh."million"	Sh."million"
Non-current assets:		
Property, plant and equipment	2,831	2,345
Interest in joint venture	427	380
Goodwill on acquisition	432	455
	3,690	3,180
Current assets:		
Inventory	170	128
Accounts receivable	238	214
Cash and cash equivalents	78	63
	486	405
Total assets	4,176	3,585

	Sh."million"	Sh."million"
Equity and liabilities:		
Equity:		
Ordinary share capital	1,320	1,000
Share premium	460	400
Revaluation surplus	284	200
Retained profit	570	360
Owner's equity	2,634	1,960
Non-controlling interests	186	180
	2,820	2,140
Non-current liabilities:		
10% convertible loan stock	780	960
Deferred tax	150	185
Current liabilities:		
Accounts payable	234	175
Current tax	92	94
Interest payable	100	31
Total equity and liabilities	4,176	3,585

Consolidated statement of changes in equity for the year ended 30 September 2018

	Ordinary share capital Sh."million"	Share premium Sh."million"	Revaluation surplus Sh."million"	Retained profit Sh."million"	Total Sh."million"
As at 1 October 2017	1,000	400	200	360	1,960
New share issue	320	60			380
Revaluation of property, plant and equipment			84		84
Profit for the year				290	290
Dividend paid				(80)	(80)
As at 30 September 2018	1,320	460	284	570	2,634

Additional information:

1. The property, plant and equipment account comprised the following:

	30 September 2018 Sh."million"	30 September 2017 Sh."million"
Cost	3,765	2,970
Accumulated depreciation	(934)	(625)
Carrying amount	2,831	2,345

During the year ended 30 September 2018, an 80% owned subsidiary revalued its property upwards by Sh.150 million. The holding company disposed of an item of plant which had cost Sh.290 million and had accumulated depreciation of Sh.96 million. The disposal proceeds amounted to Sh.215 million.

2. The 10% convertible loan stock was convertible at any time at the holders' option into 20 ordinary shares of Sh.10 each for every Sh.200 of the loan stock. During the year ended 30 September 2018, holders of Sh.180 million of 10% convertible loan stock exercised their conversion option.
3. Impairment loss on goodwill and depreciation for the year ended 30 September 2018 have been charged to profit or loss for the year.
4. Assume a corporation tax rate of 30%.

Required:

Consolidated statement of cash flows for the year ended 30 September 2018 using the indirect method in conformity with the requirements of International Accounting Standard (IAS) 7 "Statement of Cash Flows". (14 marks)

(Total: 20 marks)

QUESTION FOUR

(a) Miaka Nenda Ltd.'s current year end is 30 June 2018. The company's financial statements were authorised for issue by its directors on 10 July 2018.

The following matters have been brought to your attention:

1. On 11 July 2018, a fire completely destroyed the company's largest warehouse and the inventory it contained. The carrying amounts of the warehouse and the inventory were Sh.80,000,000 and Sh.50,000,000 respectively. It appears that the company has not updated the value of its insurance cover and only expects to be able to recover a maximum of Sh.70,000,000 from its insurers. Miaka Nenda Ltd's trading operations have been severely disrupted since the fire and it expects significant trading losses for some time to come.
2. A single class of inventory held at another warehouse was valued at its cost of Sh.9,200,000 as at 30 June 2018. In July 2018, 70% of this inventory was sold for Sh.5,600,000 on which the company's staff earned a commission of 15% of the selling price.
3. On 10 August 2018, the government announced tax changes which had the effect of increasing the company's deferred tax liability by Sh.7,000,000 as at 30 June 2018.

Required:

With reference to International Accounting Standard (IAS) 10 "Events After the Balance Sheet Date", explain the required treatment of each of the above items in the financial statements of Miaka Nenda Ltd. for the year ended 30 June 2018. (6 marks)

(b) A, B and C have been in partnership sharing profits and losses in the ratio of 2:2:1 respectively. Their financial year end is 30 September. A decided to quit the partnership with effect from 10 May 2018. The remaining two partners, B and C, decided to dissolve the partnership from that date. The terms of dissolution were that the assets were to be realised, outstanding debts paid and the remainder to be shared by the partners. A was to be paid in an equitable manner, distribution of cash being made as soon as possible.

The following is the statement of financial position of the partnership as at 10 May 2018:

A, B and C
Statement of financial position as at 10 May 2018

		Sh."000"	Sh."000"
Assets:			
Non-current assets (net book value):			
Land and building			182,000
Plant and machinery			73,600
Fixtures and fittings			20,800
Motor vehicle			7,200
Intangible asset (goodwill)			89,200
			372,800
Current assets:			
Inventory		68,000	
Trade receivables		62,000	
Bank balance		9,200	
Cash balance		3,200	142,400
			515,200
Capital and liabilities:			
Capital accounts:	A		100,000
	B		64,000
	C		40,000
			204,000
Current accounts:	A	32,000	
	B	22,000	54,000
			258,000
Long-term liability:			
Bank loan			160,000
Current liabilities:			
Trade payables		33,200	
Bank overdraft		64,000	97,200
			515,200

Additional information:

1. The partnership had an insurance policy which entitled the firm to Sh.40,000,000 immediately a partner left.
2. Dissolution expenses amounted to Sh.1,800,000 and were paid on 30 August 2018.
3. As soon as sufficient money was available, all the outstanding payables were paid after the discount received which amounted to Sh.1,000,000.

4. Assets were sold and the monies received on piecemeal basis as follows:

Date	Particulars	Amount Sh."000"
30 May 2018:	Insurance policy	40,000
	Insurance benefit received (interest)	16,000
	Land and building	180,000
25 June 2018:	Plant and machinery	41,200
	Trade receivables	26,000
20 July 2018:	Motor vehicle	6,400
	Fixtures and fittings	8,800
15 August 2018:	Plant and machinery	32,400
	Fixtures and fittings	8,000
20 September 2018:	Inventory	68,000
	Trade receivables	40,000

Required:

(i) Statement showing how the proceeds of the dissolution will be shared between the partners. (8 marks)

(ii) Realisation account. (3 marks)

(iii) Partners' capital accounts. (3 marks)

(Total: 20 marks)

QUESTION FIVE

(a) Citing relevant examples, summarise the accounting treatment of government grants received by an entity. (6 marks)

(b) The following trial balance was extracted from the books of DD Associates, a firm of advocates, as at 30 September 2018:

	Sh."000"	Sh."000"
Costs charged to clients on:		
Civil cases		4,250
Criminal cases		2,450
Oaths		260
Conveyance fees		340
Preparation of wills		200
Cases in progress as at 1 October 2017	1,104	
Clients account (money held on behalf of clients)		744
Accounts payable		816
Accounts receivable	2,440	
General office expenses	255	
Furniture, fittings and library books	1,350	
Cash at bank: Clients' account	744	
Office	1,671	
Capital		6,220
Disbursements on behalf of clients	360	
Drawings	1,800	
Salaries to office staff	2,160	
Rent and rates	1,800	
Postage and telephone	546	
Printing and stationery	1,050	
	15,280	15,280

Additional information:

1. It is estimated that debts amounting to Sh.165,000 might not be collected and should be written off.
2. Depreciation should be provided at the rate of 20% per annum on the book value of furniture, fittings and library books.
3. Cases in progress as at 30 September 2018 were valued at Sh.705,000.

Required:

(i) Statement of comprehensive income for the year ended 30 September 2018. (8 marks)

(ii) Statement of financial position as at 30 September 2018. (6 marks)

(Total: 20 marks)

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CPA PART II SECTION 3

FINANCIAL REPORTING

THURSDAY: 24 May 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) In the context of International Public Sector Accounting Standard (IPSAS) 19 – Provisions, Contingent Liabilities and Contingent Assets:

(i) Distinguish between a "provision" and a "contingent liability". (4 marks)

(ii) Summarise the recognition requirements for provisions, contingent liabilities and contingent assets. (6 marks)

(b) With reference to International Accounting Standard (IAS) 12 – Income Taxes:

(i) Differentiate between a "deferred tax liability" and a "deferred tax asset". (2 marks)

(ii) Explain the two types of temporary differences. (4 marks)

(iii) Describe the basis of measurement for current tax liabilities and deferred tax liabilities. (4 marks)

(Total: 20 marks)

QUESTION TWO

The following trial balance relates to Zambezi Ltd. as at 31 October 2017:

	Sh."000"	Sh."000"
Turnover		213,800
Cost of sales	143,800	
Trade receivables	13,500	
Bank balance		900
Distribution expenses	9,800	
Inventories (31 October 2017)	10,500	
Interest expenses	5,000	
Administrative expenses	12,600	
Rental income from investment property		1,200
Plant and equipment - cost	36,000	
Land and building - at valuation	63,000	
Accumulated depreciation - plant and equipment		16,800
Investment property - valuation (1 November 2016)	16,000	
Trade payables		11,800
Joint arrangement	8,000	
Deferred tax		5,200
Ordinary shares (Sh.25 each)		20,000
10% redeemable preference shares (Sh.1 each)		10,000
Retained earnings - 1 November 2016		17,500
Revaluation surplus		21,000
	318,200	318,200

Additional information:

1. An inventory count on 31 October 2017 listed goods with a cost of Sh.10.5 million. These included some damaged goods that had cost Sh.800,000. These goods would require repair works costing Sh.450,000 after which they could be sold for an estimated price of Sh.950,000.
2. Non-current assets:
   - **Plant**
     All plant, including that of the joint operation is depreciated at the rate of 12.5% per annum on reducing balance basis.
   - **Land and building**
     The land and building were revalued at Sh.15 million and Sh.48 million respectively on 1 November 2016 creating a Sh.21 million revaluation surplus. At this date, the building had a remaining useful life of 15 years.

Depreciation is on a straight line basis. Zambezi Ltd. does not make a transfer to realised profits in respect of excess depreciation.
Depreciation on both the building and the plant should be charged to the cost of sales.

- **Investment property**
  On 31 October 2017, a qualified surveyor valued the investment property at Sh.13.5 million. The company uses the fair value model as per IAS 40 – Investment Property, to value its investment property.

3. Interest expenses include overdraft charges, the full year's preference dividend and an ordinary dividend of Sh.4 per share that was paid in April 2017.
4. The directors have estimated the provision for income tax for the year ended 31 October 2017 at Sh.8 million. The deferred tax provision as at 31 October 2017 is to be adjusted (through the profit and loss statement) to reflect that the tax base of the company's net assets is Sh.12 million less than their carrying amounts. The tax rate is 30%.
5. On 1 November 2016, Zambezi Ltd. entered into a joint arrangement with two other entities. Each venturer contributes their own assets and is responsible for their own expenses including depreciation on assets of the joint arrangement. Zambezi Ltd. is entitled to 40% of the joint venture's total turnover. The joint arrangement is not a separate entity and is regarded as a joint operation.

   Details of Zambezi Ltd.'s joint venture transactions are as follows:

	Sh."000"
Plant and equipment (at cost)	12,000
Share of joint venture turnover (40% of total turnover)	(8,000)
Related joint venture cost of sales (excluding depreciation)	5,000
Trade receivables	1,500
Trade payables	(2,500)
Balance as per trial balance	8,000

Required:

(a) Statement of comprehensive income for the year ended 31 October 2017. (10 marks)

(b) Statement of financial position as at 31 October 2017. (10 marks)

(Total: 20 marks)

QUESTION THREE

(a) Outline three circumstances under which a partnership might be dissolved by operation of law. (3 marks)

(b) Chanda, Pete and Kidole are partners in a partnership business sharing profits and losses in the ratio of 2:2:1 respectively after allowing for a 10% per annum interest on fixed capital balances and commission entitled to a partner.

The trial balance extracted from the financial records of the partnership as at 30 September 2017 is as set out below:

		Sh."000"	Sh."000"
Land and buildings at cost		123,500	
Motor vehicles at cost		80,600	
Office equipment at cost		70,200	
Furniture and fixtures at cost		52,000	
Provision for depreciation:	Buildings		20,150
	Motor vehicles		54,600
	Office equipment		24,400
	Furniture and fixtures		18,500
Investments		44,800	
Goodwill		26,000	
Inventories (30 September 2017)		31,200	
Accounts receivable		25,400	
Accounts payable			62,400
Bank overdraft			17,550
Accrued expenses			4,000
Capital accounts:	Chanda		58,500
	Pete		37,000
	Kidole		31,500
Net profit for the year to 30 September 2017			91,000
Drawings:	Chanda	7,800	
	Pete	6,500	
	Kidole	3,900	
Current accounts:	Chanda		20,800
	Pete		18,200
	Kidole		13,300
		471,900	471,900

Additional information:

1. Kidole was the only active partner and was entitled to a commission of 15% based on the annual sales revenue which averaged Sh.20 million.
2. The partners resolved to convert their business into that of a company to be named Chapeki Limited with effect from 1 October 2017 under the following terms:
   - Investments comprised equity investments which partners had acquired jointly. Each partner was to take over a portion of the investments equivalent to the profit share. The investments had a market value of Sh.50 million on 30 September 2017.
   - Other assets and liabilities were transferred to the new company at the following agreed values:

	Sh."000"
Land and buildings	115,000
Motor vehicles	25,500
Office equipment	43,500
Furniture and fixtures	29,550
Inventories at book value less 5%	
Accounts receivable at book value less 2½%	
Current liabilities at book values	

     Goodwill was considered valueless and therefore was written off.
   - The purchase consideration on business purchase was agreed at Sh.250 million.
   - The partners were to become shareholders. The company issued ordinary shares at a par value of Sh.10 each to the partners to satisfy the balances due to them as at 30 September 2017.
3. Upon incorporation, the new company issued new debentures at par, carrying interest at 14% per annum. The cash proceeds from the issue amounting to Sh.50 million were used to purchase additional stock of raw materials worth Sh.15 million. Accrued expenses were settled in full.

Required:

(i) A realisation account, partners' capital accounts and Chapeki Limited's account to close off the partnership's books. (10 marks)

(ii) Opening statement of financial position of Chapeki Limited. (7 marks)

(Total: 20 marks)

QUESTION FOUR

(a) The following information was extracted from the books of Maendeleo Commercial Bank Ltd. as at 31 December 2017:

		Sh."million"
Property, plant and equipment		6,750
Intangible assets		6,450
Ordinary shares (Sh.20 each)		15,255
Share premium		270
Revaluation reserves		1,380
Statutory reserves		5,730
Interest income:	Loan advances to customers	15,042
	Finance lease	14,040
	Deposits with other banks	3,024
	Government bonds	7,230
Interest expenses:	On customer deposits	7,500
	On deposits with other banks	168
Fees and commissions received		5,592
Forex commission receivable		330
Other operating incomes		4,500
Fees and other expenses		450
Impairment of loans and advances		2,520
Administrative costs		11,580
General operating expenses		9,420
Income tax expenses		6,300
Retained revenue (1 January 2017)		49,920
Deposits with Central Bank		38,400
Deposits due from other banks		57,600
Government bonds and other securities		46,230
Loans and advances to customers		396,810
Other assets		2,145
Deferred tax assets		180

	Sh."million"
Other investments	468
Deferred tax liabilities	4,338
Other liabilities	3,300
Current tax liability	3,435
Deposits from other banks	6,600
Customer deposits	452,985

Additional information:

1. Intangible assets were impaired by 20% as at the end of the year.
2. Property, plant and equipment is to be revalued to Sh.12,750 million.
3. An allowance for unserviced loans is to be created at 2% of the outstanding loans and advances to customers.

Required:

(i) Income statement for the year ended 31 December 2017. (6 marks)

(ii) Statement of financial position as at 31 December 2017. (6 marks)

(b) Royal Contractors Ltd. owns an item of plant used for construction with a carrying value of Sh.14 million as at 31 December 2015. The firm won a construction contract and decided to sell and lease back the machine on that date under the following conditions.

- Selling price Sh.40 million. This was also the fair value of the plant.
- Lease rentals payable annually in arrears amounted to Sh.15,521,200.
- Lease duration for the machine was to be 3 years. The economic life of the machine was also 3 years.
- The implicit interest rate was 8% per annum.

Required:

The journal entries to record the necessary transactions in the books of Royal Contractors Ltd. for the three years, including the expected entries at the end of year 2018. (8 marks)

(Total: 20 marks)

QUESTION FIVE

(a) On 1 April 2017, H Ltd. acquired four million of the ordinary shares of S Ltd., paying Sh.4.50 per share. At the same time, H Ltd. purchased Sh.500,000 of S Ltd.'s 10% redeemable preference shares. At the acquisition date, the retained earnings of S Ltd. were Sh.400,000.

The following are the draft statements of financial position of the two companies as at 31 March 2018:

	H Ltd. Sh."000"	S Ltd. Sh."000"
Non-current assets:		
Land and buildings	22,000	12,000
Plant and equipment	20,450	10,220
Investments in S Ltd.:		
Equity	18,000	-
Preference shares	500	-
	60,950	22,220
Current assets:		
Inventories	9,850	6,590
Trade receivables	11,420	3,830
Cash and bank	490	-
	21,760	10,420
	82,710	32,640
Equity:		
Ordinary shares (Sh.1 each)	10,000	5,000
10% preference shares	-	2,000
Retained earnings	51,840	14,580
	61,840	21,580
Non-current liabilities:		
10% Debentures 2022	12,000	4,000
Current liabilities:		
Trade payables	6,400	4,510
Bank overdraft	-	570
Taxation	2,470	1,980
	8,870	7,060
Total equity and liabilities	82,710	32,640

Extracts from the income statement of S Ltd. before intra group adjustments for the year to 31 March 2018 were as follows:

	Sh."000"
Profit before tax	5,400
Taxation expenses	(1,600)
	3,800

Additional information:

1. Included in the land and buildings of S Ltd. is a large piece of development land at a cost of Sh.5 million. The fair value of the land on the date S Ltd. was acquired was Sh.7 million and by 31 March 2018, this value had risen to Sh.8.5 million. The group's valuation policy for development land is that it should be carried at fair value and not depreciated.
2. On the date of acquisition of S Ltd., the company's plant and equipment included plant that had a fair value of Sh.4 million in excess of its carrying value.
   This plant had a remaining useful life of 5 years. The group calculates depreciation on a straight-line basis. The fair value of the other net assets of S Ltd. approximated their carrying values.
3. During the year, S Ltd. sold goods to H Ltd. for Sh.1.8 million. S Ltd. adds a 20% mark up on cost to all its sales. Goods with a transfer price of Sh.450,000 were included in the inventory of H Ltd. as at 31 March 2018. The balance of the current accounts of H Ltd. and S Ltd. was Sh.240,000 on 31 March 2018.
4. An impairment test carried out on 31 March 2018 showed that the consolidated goodwill was impaired by Sh.1,488,000.
5. S Ltd. had paid its preference dividend in full and ordinary dividends of Sh.500,000.

Required:

Consolidated statement of financial position of H Ltd. and its subsidiary S Ltd. as at 31 March 2018. (14 marks)

(b) Discuss the impact of International Financial Reporting Standard (IFRS) 9 on the tax expenses of commercial banks. (6 marks)

(Total: 20 marks)

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CPA PART II SECTION 3

FINANCIAL REPORTING

THURSDAY: 30 November 2017. **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) In the context of International Public Sector Accounting Standard (IPSAS) 3 – Accounting Policies, Changes in Accounting Estimates and Errors:

(i) Explain the meaning of "prior period errors", citing two examples of such errors. (4 marks)

(ii) Summarise the accounting treatment of material prior period errors. (4 marks)

(b) IPSAS 8 – Financial Reporting of Interests in Joint Ventures identifies three forms of joint ventures:

Required:

(i) Highlight the three forms of joint ventures referred to above. (6 marks)

(ii) Describe the accounting treatment of each of the three forms of joint ventures. (6 marks)

(Total: 20 marks)

QUESTION TWO

(a) The new International Financial Reporting Standard (IFRS) 9 - Financial Instruments which was issued on 24 July 2014 and which will take effect from 1 January 2018, has generated significant discussions in your country, particularly within the banking sector.

Required:

Explain how IFRS 9 is likely to impact on the provisions for bad and doubtful debts by banks and by extension, the ease of accessing bank loans. (6 marks)

(b) Mwanzo Ltd., Safari Ltd. and Upya Ltd. operate in the clothing industry.

The following information relates to the financial position of the three companies as at 30 September 2017:

	Mwanzo Ltd. Sh."000"	Safari Ltd. Sh."000"	Upya Ltd. Sh."000"
Non-current assets:			
Property, plant and equipment	7,960	4,600	2,680
Patents	500	840	-
Investments in: Safari Ltd.	5,000		
Upya Ltd.	1,600		
Others	300	400	120
	15,360	5,840	2,800
Current assets:			
Inventories	1,140	800	600
Trade receivables	840	760	800
Bank	-	300	240
	1,980	1,860	1,640
Total assets	17,340	7,700	4,440
Equity and liabilities:			
Equity and reserves:			
Ordinary shares of Sh.20 each	4,000	2,000	1,000
Reserves: Share premium	2,000	1,000	200
Revenue reserves	9,000	3,800	2,400
	15,000	6,800	3,600

	Sh."000"	Sh."000"	Sh."000"
Non-current liabilities:			
Deferred tax	400	-	160
Current liabilities:			
Trade payables	1,500	900	560
Current tax	280	-	120
Bank overdraft	160	-	-
	1,940	900	680
Total equity and liabilities	17,340	7,700	4,440

Additional information:

1. Mwanzo Ltd. acquired its investments as shown below:

Company	Number of shares acquired	Cost of investment Sh."000"	Retained earnings Sh."000"	Date of acquisition
Safari Ltd.	80,000	5,000	2,400	1 October 2015
Upya Ltd.	20,000	1,600	1,600	1 October 2016

2. At the date of its acquisition, the fair value of Safari Ltd.'s net assets were equal to their book values, with the exception of land that had a fair value of Sh.400,000 in excess of its book value.
3. On 1 September 2017, Mwanzo Ltd. processed an invoice for Sh.100,000 in respect of an agreed allocation of management fee to Safari Ltd. As at 30 September 2017, Safari Ltd. had not accounted for this transaction. Prior to this, the current accounts between the two companies had been agreed at Safari Ltd. owing Sh.140,000 to Mwanzo Ltd. (included in trade receivables and trade payables respectively).
4. During the year ended 30 September 2017, Upya Ltd. sold goods to Mwanzo Ltd. at a selling price of Sh.280,000, which gave Upya Ltd. a profit of 40% on cost. Mwanzo Ltd. had half of these goods in inventory as at 30 September 2017.
5. The fair value of the non-controlling interest (NCI) in Safari Ltd. was Sh.1,500,000.

Required:

Group statement of financial position as at 30 September 2017. (14 marks)

(Total: 20 marks)

QUESTION THREE

Tenda, Mema and Nenda have been in partnership for many years as TMN Enterprises, sharing profits and losses in the ratio of 3:2:1 respectively. Due to the hard economic times, the partners made a resolution to dissolve the partnership.

The partnership's statement of financial position as at 31 August 2017, just prior to the dissolution was as follows:

TMN Enterprises
Statement of financial position as at 31 August 2017

		Sh."000"	Sh."000"
Non-current assets:			
Premises		10,500	
Motor vehicles		4,580	
Furniture and fittings		1,880	
Equipment		2,340	19,300
Current assets:			
Inventories		3,000	
Trade receivables		4,000	
Cash and bank		200	7,200
			26,500
Capital account	: Tenda	12,000	
	: Mema	8,000	
	: Nenda	4,000	24,000
Current account	: Tenda	(2,000)	
	: Mema	(3,000)	
	: Nenda	(6,000)	(11,000)
Non-current liabilities:			
Loan account - Mema		2,000	
Loan from microfinance bank		4,000	6,000
Current liabilities:			
Trade payables and accruals			7,500
			26,500

The terms of dissolution were as follows:

1. The partners to take over the following assets:
   Equipment to be taken over by Tenda at an agreed valuation of Sh.2,000,000.
   Furniture to be taken over by Mema at a valuation of Sh.920,000.
2. The remaining assets were realised on installment basis as follows:

1st installment	Sh.12,000,000
2nd installment	Sh.3,600,000
3rd installment	Sh.2,610,000

3. Nenda was adjudicated bankrupt before the dissolution and liquidation of the partnership was completed.
4. Liquidation expenses amounted to Sh.450,000.
5. Trade payables were settled net of a discount of Sh.700,000.

Required:

(a) A statement of cash distribution. (10 marks)

(b) Realisation account. (5 marks)

(c) Partners capital accounts. (5 marks)

(Total: 20 marks)

QUESTION FOUR

The following trial balance was extracted from the books of Savanna Ltd. as at 30 September 2017:

		Sh."000"	Sh."000"
Land		20,100	
Buildings		42,600	
Plant and machinery		216,600	
Accumulated depreciation:	Buildings		6,390
	Plant and machinery		127,710
Revenue			180,030
Cost of sales		65,670	
Inventory (30 September 2017)		6,450	
Distribution costs		6,690	
Administrative expenses		11,340	
Income tax		8,580	
Investment property at fair value (1 October 2016)		20,340	
Finance cost		7,020	
8% redeemable preference shares			15,000
10% debentures			30,000
Intangible assets		34,200	
Trade receivables and trade payables		8,700	5,340
Ordinary shares (each share Sh.20 par value)			90,000
Share premium			6,000
Retained profit (1 October 2016)			7,620
Deferred tax			8,490
Bank and cash balances		1,350	
Investment at fair value		26,940	
		476,580	476,580

Additional information:

1. The fair value of the investment property on 30 September 2017 was Sh.20,790,000.
2. Information relating to intangible assets was as follows:
   - The intangible assets include:

	Cost	Accumulated amortisation
	Sh."000"	Sh."000"
Development cost on software (it is to be amortised over 5 years)	25,800	15,480
Patent	15,600	-
Research costs	8,280	

   - The patent was acquired on 1 November 2014. It was determined that the patent had an indefinite useful life when it was acquired. However, on 1 October 2016, due to a new competitor gaining ground on the company's technology, the patent's estimated fair value was established to be Sh.13,500,000 with an estimated useful life of 3 years.
   - The research costs were incurred during the year in developing new software which was not successful.

3. The following details are relevant to the property, plant and equipment:
- Buildings are depreciated at 2½% per annum on straight line basis.
- Plant and machinery are depreciated on a straight line basis over 10 years.
- Depreciation for the current year has been provided.
- On 30 September 2017, the land and buildings were revalued to Sh.25,500,000 and Sh.45,600,000 respectively. The new values are to be included in the accounts for the financial year ended 30 September 2017.

4. Savanna Ltd. is also a sales agent for Majani Ltd. and is entitled to a sales commission of 10% on the sales made on behalf of Majani Ltd. The net proceeds obtained from the sales (after deducting the commission) are remitted to Majani Ltd. During the financial year ended 30 September 2017, Savanna Ltd. sold goods worth Sh.20,700,000 on behalf of Majani Ltd. This amount was included in the sales revenue disclosed in the above trial balance.
Savanna Ltd. had not remitted the net sales proceeds to Majani Ltd.

5. Inventory as at 30 September 2017 included partially damaged and slow moving goods. The cost of these goods was Sh.450,000 and they were eventually sold in October 2017 for Sh.128,400.

6. Finance costs comprised:

	Sh."000"
Interest on debentures	3,000
Interim dividends paid on ordinary shares	4,440
Dividends paid on redeemable preference shares	1,200
Investment income from tax exempt companies	(1,620)
	7,020

7. The corporation tax rate is 30%.

8. The balance on the income tax in the trial balance represents the amount paid for the year. The tax expense for the year is estimated to be Sh.7,770,000 inclusive of an increase in deferred tax liability of Sh.1,020,000.

Required:
The following statements in a format suitable for publication:

(a) Comprehensive income statement for the year ended 30 September 2017. (8 marks)

(b) Statement of changes in equity for the year ended 30 September 2017. (4 marks)

(c) Statement of financial position as at 30 September 2017. (8 marks)

(Total: 20 marks)

QUESTION FIVE

(a) Explain two key features of a sale and leaseback transaction, citing two advantages of such transactions. (6 marks)

(b) Rejareja Ltd. is a mid-size firm selling electronic keyboards both on cash and hire purchase terms. The following information has been extracted from the firm's books of account as at 30 September 2017:

	Sh."000"	Sh."000"
Share capital		37,500
General operating expenses	65,000	
Cash balance	3,104	
Cash recovered from hire purchase customers		157,734
Cash sales		36,000
Hire purchase trade receivables (1 October 2016)	1,134	
Property, plant and equipment	50,000	
Accumulated depreciation (1 October 2016)		22,500
Retained earnings (1 October 2016)		3,500
Provision for unrealised profit (1 October 2016)		504
Purchases	171,000	
Trade payables		40,000
Inventory (1 October 2016)	7,500	
	297,738	297,738

Additional information:

1. The company's policy is to take credit for gross profit including interest for hire purchase sales in proportion to the cash collected. It does this by raising a provision against the profit included in the hire purchase trade receivables not yet due.
2. The cash selling price is fixed at 50% and the hire purchase selling price at 80% respectively against the cost of goods purchased.

3. The hire purchase contract requires an initial deposit of 20% of the hire purchase selling price, the balance to be paid in four installments at quarterly intervals. The first installment is due three months after the agreement is signed.
4. Hire purchase sales for the year amounted to Sh.270,000,000 (including interest).
5. Depreciation is charged on property, plant and equipment at the rate of 15% per annum on cost. One third of the depreciation relates to cash sales.
6. Operating expenses are to be apportioned on the basis of cash and hire purchase sales.

Required:

Prepare for Rejareja Ltd.:

(i) Income statement for the year ended 30 September 2017 showing separate columns for cash, hire purchase and combined sales. (8 marks)

(ii) Statement of financial position as at 30 September 2017. (6 marks)

(Total: 20 marks)

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CPA PART II SECTION 3

FINANCIAL REPORTING

THURSDAY: 25 May 2017. **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) With reference to International Public Sector Accounting Standard (IPSAS) 14 – Events After the Balance Sheet Date:

(i) Describe the two categories of events after the balance sheet date. (4 marks)

(ii) Explain two disclosure requirements for each category of events identified in (a) (i) above. (4 marks)

(b) In the context of International Accounting Standard (IAS) 40 – Investment Property:

(i) Define an "investment property", citing two examples. (4 marks)

(ii) Identify two types of property that are specifically not considered as investment property. (2 marks)

(iii) Discuss the fair value model as applied in the valuation of investment property. (6 marks)

(Total: 20 marks)

QUESTION TWO

Dida and Vuma were partners in a wholesale business. The following balances were extracted from their books of account as at 30 April 2017:

	Debit Sh."000"	Credit Sh."000"
Accruals		9,000
Capital account: Dida		20,000
Vuma		30,000
Equipment	20,000	
Motor vehicles at cost	55,000	
Accumulated depreciation: Equipment		8,000
Motor vehicles		25,000
Cash and bank balances	21,000	
Drawings: Dida	15,000	
Vuma	10,000	
Net profit for the year to 30 April 2017		149,000
Prepayments	3,000	
Salary paid to Vuma	20,000	
Inventory at cost (30 April 2017)	70,000	
Trade payables		118,000
Trade receivables	100,000	
Premises	45,000	
	359,000	359,000

Additional information:

1. The partnership agreement includes the following arrangements between the partners:

   - Profits and losses are to be shared in the ratio of 3:1 for Dida and Vuma respectively.
   - Interest of 15% per annum is to be paid on the partners' fixed capital.
   - Interest at a rate of 10% per annum is to be charged on partners' drawings.
   - Vuma is entitled to a salary of Sh.20 million per annum.

2. On 1 May 2017, a company known as Fariji Ltd. was incorporated in order to make an offer for the purchase of the partnership business. The arrangements were as follows:

   - Vuma to take over one of the motor vehicles at an agreed valuation of Sh.5 million.

Other assets and liabilities (except cash) were taken over by the company at the following values:

	Sh. "000"
Premises	50,000
Motor vehicles	18,000
Equipment	10,000
Trade payables	80,000
Accruals	10,000

Inventory net of 10% for obsolete stock
Receivables net of provision for doubtful debts of 5%
Prepayments were valueless

3. Additional costs incurred by the partnership in arranging the sale of the business amounted to Sh.3 million.
4. The company agreed to issue 15 million shares of Sh.10 each at a premium of 24%. The shares were to be divided between Dida and Vuma in the ratio of 3:2 respectively.
5. The partners' drawings were made in the following months:
   Dida : November 2016
   Vuma : February 2017
6. The rule of Garner Vs Murray is to apply.

Required:

(a) Realisation account. (8 marks)
(b) Partners' capital accounts. (5 marks)
(c) Statement of financial position of Fariji Ltd. as at 2 May 2017. (7 marks)

(Total: 20 marks)

QUESTION THREE

The following trial balance relates to Apple Ltd. as at 31 March 2017:

		Sh. "000"	Sh. "000"
Ordinary shares of Sh.10 par value			100,000
Share premium			40,000
Retained earnings (1 April 2016)			22,400
Land and buildings at cost (Land Sh.40 million)		120,000	
Plant and equipment at cost		189,000	
Accumulated depreciation: 1 April 2016:	Buildings		40,000
	Plant and equipment		49,000
Inventories (31 March 2017)		87,400	
Trade receivables		84,400	
Bank balance			13,600
Deferred tax			12,400
Trade payables			70,200
Revenue			1,100,000
Cost of sales		823,000	
Distribution costs		43,000	
Administrative expenses		61,800	
Dividends paid		40,000	
Bank interest		1,400	
Current tax			2,400
		1,450,000	1,450,000

Additional information:

1. On 1 April 2016, the company's directors decided that land and buildings should be revalued at their market values. At that date, an independent expert valued land at Sh.24 million and buildings at Sh.70 million and these valuations were accepted by the directors. The remaining useful life of buildings on that date was 14 years. The company does not make a transfer to retained earnings for excess depreciation.
2. Plant and equipment is depreciated at 20% per annum using the reducing balance method and time apportioned as appropriate. Depreciation for the year is yet to be accounted for.
3. Directors' remuneration amounting to Sh.11 million should be provided for and is classified as administrative cost.
4. Income tax provision of Sh.54.4 million is required for the year ended 31 March 2017. As at that date, deferred tax liability amounted to Sh.18.8 million. The movement in deferred tax should be taken to profit or loss. The balance on the current tax in the trial balance represents over/under provision of tax liability for the year ended 31 March 2016.
5. On 1 July 2016, the company made a rights issue of 1 share for every 4 shares at Sh.24 each. Immediately before this issue, the stock market value of the shares was Sh.40 each.

Required:

(a) Statement of comprehensive income for the year ended 31 March 2017. (8 marks)

(b) Statement of changes in equity as at 31 March 2017. (4 marks)

(c) Statement of financial position as at 31 March 2017. (8 marks)

(Total: 20 marks)

QUESTION FOUR

The following financial statements relate to Hema Ltd. and its investment companies Shuka Ltd. and Ajabu Ltd. for the year ended 30 April 2017:

Income statement for the year ended 30 April 2017

	Hema Ltd. Sh. "million"	Shuka Ltd. Sh. "million"	Ajabu Ltd. Sh. "million"
Revenue	1,200	600	300
Cost of sales	(650)	(250)	(100)
Gross profit	550	350	200
Investment income	70	-	1
Distribution cost	(100)	(40)	(30)
Administrative expense	(130)	(90)	(50)
Finance cost	(40)	(20)	(20)
Profit before tax	350	200	101
Income tax expense	(70)	(50)	(31)
Profit for the year	280	150	70
Dividends paid	(50)	(50)	(30)
Retained profit for the year	230	100	40
Retained profit brought forward	480	275	160
Retained profit carried forward	710	375	200

Statement of financial position as at 30 April 2017

	Hema Ltd. Sh. "million"	Shuka Ltd. Sh. "million"	Ajabu Ltd. Sh. "million"
Assets:			
Non-current assets:			
Property, plant and equipment	1,250	800	650
Intangible assets	200	70	80
Investments	850	50	20
	2,300	920	750
Current assets:			
Inventory	200	75	60
Trade and other receivables	300	90	80
Financial assets at fair value	30	20	10
Cash and cash equivalents	150	40	40
	680	225	190
Total assets	2,980	1,145	940
Equity and liabilities:			
Equity:			
Ordinary share capital	1,000	200	200
Share premium	300	50	50
Revaluation reserve	200	50	50
Retained profits	710	375	200
	2,210	675	500
Non-current liabilities:			
10% loan stock	500	200	200
Current liabilities:			
Trade and other payables	250	250	220
Current tax	20	20	20
	270	270	240
Total equity and liabilities	2,980	1,145	940

Additional information:

1. Hema Ltd. acquired the investments in other companies as follows:

Company	Date	Shareholding	Cost of purchase Sh. "million"	Revaluation reserve Sh. "million"	Retained profits Sh. "million"
Shuka Ltd.	1 May 2014	80%	300	20	80
Ajabu Ltd.	1 May 2015	40%	200	25	150

Hema Ltd. also invested in half of the 10% loan stock in Shuka Ltd.

2. The fair value of the non-controlling interest in Shuka Ltd. was Sh.75 million on 1 May 2014.
3. During the year ended 30 April 2017, Hema Ltd. sold goods to Shuka Ltd. and Ajabu Ltd. as follows:

	Selling price Sh. "million"	Mark up %	% of goods held in stock
Shuka Ltd.	100	25	50
Ajabu Ltd.	50	25	Nil

4. On 1 May 2016, Hema Ltd. sold Shuka Ltd. an item of plant for Sh.200 million reporting a 25% profit on cost of the plant. The group charges depreciation at 20% per annum on cost of plant.
5. All the goodwill of the two companies in which Hema Ltd. has invested are estimated to be impaired by 60% to the year ended 30 April 2017. 20% of the impairment relates to the current year.
6. Trade receivables and trade payables included Sh.50 million due from Shuka Ltd. to Hema Ltd. and Sh.10 million due from Ajabu Ltd. to Hema Ltd.
7. All dividends and interest had been paid by the end of the year.

Required:

(a) Consolidated income statement for the year ended 30 April 2017. (10 marks)

(b) Statement of changes in equity for the year ended 30 April 2017. (2 marks)

(c) Consolidated statement of financial position as at 30 April 2017. (8 marks)

(Total: 20 marks)

QUESTION FIVE

(a) Distinguish between "value based" and "cost based" method in determining the stage of completion of a construction contract. (6 marks)

(b) The following trial balance was extracted from the books of Malipo Insurance Company Ltd. which specialises in general insurance as at 31 March 2017:

		Sh. "million"	Sh. "million"
Freehold property		5,040	
Motor vehicle (net book value)		4,200	
Machinery and equipment (net book value)		1,800	
Furniture (net book value)		1,560	
Audit fees paid		288	
Directors fees		594	
Depreciation on non-current assets		1,086	
Management expenses:	Marine	780	
	Fire	696	
Accounts receivable and accounts payable		876	396
Investment income			336
Ordinary share capital			3,600
Share premium			1,200
Retained profit as at 1 April 2016			540
Premiums outstanding as at 1 April 2016:	Marine	1,080	
	Fire	840	
Unearned premiums as at 1 April 2016:	Marine		5,760
	Fire		3,000
Claims outstanding as at 1 April 2016:	Marine		960
	Fire		648
Claims paid:	Marine	2,964	
	Fire	2,160	

		Sh. "million"	Sh. "million"
Legal costs:	Marine	216	
	Fire	156	
Expenses relating to claims (Marine)		384	
Bad debts written off:	Marine	204	
	Fire	144	
Investment in shares		1,680	
Direct premiums received:	Marine		5,400
	Fire		4,200
Re-insurance premiums received:	Marine		1,440
	Fire		960
Re-insurance premiums paid:	Marine	960	
	Fire	600	
Bank balance and cash in hand		132	
		28,440	28,440

Additional information:

1. Unearned premiums reserve for unexpired risk is to be maintained at 100% and 50% of the premiums for marine insurance and fire insurance respectively.
2. Commission on both insurance ceded and re-insurance accepted is at a rate of 5% of the premiums.
3. The directors have proposed a dividend of 5% on the outstanding share capital as at 31 March 2017.
4. The tax rate applicable is 30%.
5. Premiums outstanding as at 31 March 2017 amounted to Sh.1,800 million and Sh.840 million for marine insurance and fire insurance respectively.
6. Claims intimated and outstanding as at 31 March 2017 amounted to Sh.900 million for marine insurance and Sh.576 million for fire insurance.

Required:

(i) Revenue account for both marine insurance and fire insurance for the year ended 31 March 2017. (5 marks)

(ii) Statement of comprehensive income for the year ended 31 March 2017. (3 marks)

(iii) Statement of financial position as at 31 March 2017. (6 marks)

(Total: 20 marks)

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KASNEB

CPA PART II SECTION 3

FINANCIAL REPORTING

THURSDAY: 24 November 2016. **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) (i) "The determination of whether the going concern assumption is appropriate is primarily relevant for individual entities rather than for a government as a whole". [Extract from International Public Sector Accounting Standard (IPSAS) 1 – Presentation of Financial Statements].

Required:
In the context of the above statement, outline four factors to be considered in determining whether a public sector entity is a going concern. (4 marks)

(ii) With reference to IPSAS 11 – Construction Contracts, summarise four disclosure requirements for public sector entities with regard to construction contracts. (4 marks)

(b) Digital Limited is a dealer in locally manufactured desktop computers. The following trial balance has been prepared for the company as at 31 August 2016:

	Sh."000"	Sh."000"
Ordinary share capital (Sh.10 par value)		5,000
Share premium		2,500
Retained profits as at 1 July 2015		500
Sales		27,200
Opening inventory	1,440	
Purchases	20,160	
Account receivables	5,030	
Account payables		576
Distribution costs	800	
Administrative expenses	1,000	
Dividends paid	1,400	
Furniture and fittings	3,200	
Motor vehicles	1,800	
Cash at bank	810	
Cash at hand	136	
	35,776	35,776

Additional information:

1. The company buys one computer at Sh.72,000 and sells it on normal cash or credit terms at Sh.100,000.
2. Beginning June 2016, the company started selling computers on hire purchase terms that required a deposit of Sh.34,000 and 15 monthly instalments of Sh.6,000 each with the first instalment being received in the month of sale. The following units were sold on hire purchase:

Month	Units
June 2016	12
July 2016	20
August 2016	30

Two of the units sold in June 2016 were repossessed in early August 2016 after the customer failed to pay the instalment for July 2016. The two units were valued at Sh.98,000 in total and were still unsold by the year end. No adjustments have been made for the repossessions.

3. Depreciation is charged on reducing balance as follows:

Asset	Rate per annum
Furniture	10%
Motor vehicles	20%

4. The sales price presented in the trial balance represents all units sold at cash price. Any hire purchase interest is to be accrued using the sum of digits method.
5. Assume a tax liability of Sh.1,500,000 for the year.

Required:

(i) Income statement for the year ended 31 August 2016. (7 marks)

(ii) Statement of financial position as at 31 August 2016. (5 marks)

(Total: 20 marks)

QUESTION TWO

The following trial balance was extracted from the books of Peak Ltd. as at 31 October 2016:

	Sh."million"	Sh."million"
Land (cost)	400	
Buildings (cost)	1,200	
Plant (cost)	936	
Purchases	469.2	
Distribution expenses	60	
Administrative expenses	33	
Loan interest paid	12	
Leased plant rental	132	
Inventory (1 November 2015)	226.8	
Account receivables	327.2	
Long-term investment	540	
Revenue		1,670.4
Ordinary share capital (Sh.20 par value)		900
Income from investment		27
Retained earnings		717
8% debentures		300
Dividend paid	90	
Account payables		202.4
Cash in hand	2	
Deferred tax		75
Bank overdraft		20.4
Accumulated depreciation: Buildings		360
Plant		156
	4,428.2	4,428.2

Additional information:

1. The 8% debentures were issued on 1 January 2016. Interest is payable six months in arrears.
2. Inventory was valued at Sh.259.2 million as at 31 October 2016.
3. On 1 November 2015, Peak Ltd. entered into a five year lease agreement for an item of plant. This item had an estimated useful life of five years. The annual rental which was payable in advance with effect from 1 November 2015 was Sh.132 million. The fair value of the plant is Sh.552 million and the implicit interest rate is 10% per annum.
4. Plant is depreciated at a rate of 15% per annum using the reducing balance method. Depreciation expense is to be included under cost of sales in the income statement.
5. Land and buildings were revalued on 1 November 2015 at Sh.600 million and Sh.1,050 million respectively. After revaluation, the buildings were estimated to have a useful life of 35 years with nil book value at the end of their economic lives.
6. The corporate tax for the year ended 31 October 2016 was estimated at Sh.169.8 million. The deferred tax provision as at 31 October 2016 was increased to Sh.84.6 million.

Required:

(a) Income statement for Peak Ltd. in a form suitable for publication for the year ended 31 October 2016. (8 marks)

(b) Statement of changes in equity for the period ended 31 October 2016. (4 marks)

(c) Statement of financial position as at 31 October 2016. (8 marks)

(Total: 20 marks)

QUESTION THREE

(a) With reference to International Financial Reporting Standard (IFRS) 9 - Financial Instruments:

(i) Describe the provisions governing the initial measurement and subsequent measurement of financial instruments. (4 marks)

(ii) Explain the requirements for derecognition of financial instruments. (4 marks)

(b) Magari Insurance Company Limited specialises in motor vehicle insurance business. The following trial balance was extracted from the books of the company as at 31 October 2016:

	Sh. "000"	Sh. "000"
Ordinary share capital (Sh.100 par value)		200,000
Retained earnings		65,000
Investment income		89,564
Receivables arising out of direct insurance business	8,940	
Payables arising from reinsurance arrangements		6,000
Bank balances		6,000
Investment	79,846	
Property, plant and equipment (net book value)	495,600	
Premium acquisition costs	12,000	
Other operating expenses	101,424	
Depreciation expenses for the year	40,000	
Legal fees on claim settlements	81,690	
Reinsurance share of claims outstanding as at 1 November 2015	16,000	
Gross claims outstanding as at 1 November 2015		240,000
Reinsurance share of sale of salvaged motor vehicles	4,000	
Sale of salvaged motor vehicles		26,000
Gross claims paid	381,784	
Reinsurance share of claims paid		200,000
Unearned premium reserves as at 1 November 2015		40,000
Gross premiums: From brokers		139,124
From direct clients		400,000
Reinsurance premiums ceded to: Reinsurance companies	92,000	
Reinsurance brokers	88,000	
Commissions payable	30,404	
Reinsurance commissions receivable from: Reinsurance companies		4,000
Reinsurance brokers		16,000
	1,431,688	1,431,688

Additional information:

1. The following valuations were made as at 31 October 2016:

	Sh."000"
• Claims outstanding	90,000
• Claims incurred but not reported	158,000

2. Income tax on current year's profit is estimated at Sh.28,000,000.

Required:

(i) Income statement for the year ended 31 October 2016. (8 marks)

(ii) Statement of financial position as at 31 October 2016. (4 marks)

(Total: 20 marks)

QUESTION FOUR

The following information was extracted from the financial statements of A Ltd., B Ltd and C Ltd. for the year ended 30 September 2016:

Statement of financial position as at 30 September 2016:

	A Ltd. Sh. "million"	B Ltd. Sh. "million"	C Ltd. Sh. "million"
Non-current assets:			
Property, plant and equipment	950	750	450
Investments	700	-	-
Intangible assets	200	150	100
Current assets:			
Inventories	250	200	120
Trade receivables	220	170	80
Financial assets at fair value	180	130	120
Cash and bank balances	100	50	80
Total assets	2,600	1,450	950
Equity and liabilities:			
Equity and reserves			
Ordinary share capital (Sh.10 par value)	500	200	100
Share premium	200	100	50
Retained earnings	400	350	250
Shareholders funds	1100	650	400
Non-current liabilities:			
10% debentures	600	200	200
Deferred tax	250	100	50
Current liabilities:			
Trade payables	300	250	150
Current tax	250	150	100
Proposed dividends	100	100	50
Total equity and liabilities	2,600	1,450	950

Additional information:

1. A Ltd. acquired its investments as shown below:

Company	Number of shares acquired	Cost of investment Sh. "million"	Retained earnings Sh. "million"	Date of acquisition
B Ltd.	16 million	480	150	1 October 2014
C Ltd.	3 million	120	100	1 October 2015

A Ltd. also invested in half of the 10% debentures of B Ltd. The fair value of the non-controlling interest in B Ltd. amounted to Sh.120 million.

2. Immediately prior to the date of its acquisition, B Ltd. revalued its non-current assets in readiness for the acquisition as shown below:

Item	Carrying amount Sh. "million"	Fair value Sh. "million"	Remaining life (years)
Equipment	250	290	10
Patents	150	160	5

Equipment and patents are depreciated or amortised on a straight-line basis over their remaining useful lives respectively.

3. During the year, A Ltd. sold a non-current asset to B Ltd. for Sh.180 million. A Ltd. marked up the equipment at 20% on cost. B Ltd. included the equipment in its non-current assets and charged depreciation at the rate of 20% per annum on cost.
4. B Ltd. sold inventories to A Ltd. during the year for Sh.150 million. B Ltd. marked up these goods at 50% on cost. Half of these goods were still held by A Ltd. as at the year end.
5. A Ltd. owed B Ltd. Sh.100 million as at the year end with regard to the transaction in note 4 above. The books of A Ltd. however showed that it owed B Ltd. only Sh.80 million. A Ltd. had sent a cheque to B Ltd. on 25 September 2016 which was not received by B Ltd. until 5 October 2016.
6. The group uses the full goodwill method. However, it does not amortise goodwill, instead goodwill is assessed for impairment annually. Impairment test for the year ended 30 September 2016 revealed that none of the goodwill had suffered any impairment since acquisition.

Required:

Group statement of financial position as at 30 September 2016. **(20 marks)**

QUESTION FIVE

Ali, Baba and Chake have been partners sharing profits and losses in the ratio of 2:2:1 respectively. Accounts have been prepared on an annual basis to 31 December of each year. Ali, the only active partner died on 31 May 2016 and the remaining partners decided to dissolve the business from that date. The assets are to be realised, outstanding debts paid and any remaining cash is to be shared by the partners (including the executors of Ali's estate) in an equitable manner, distribution of cash being made as soon as possible.

The statement of financial position as at 31 May 2016 revealed the following:

Ali, Baba and Chake
Statement of financial position as at 31 May 2016:

Non-current assets:	**"Sh.000"**	**"Sh.000"**	**"Sh.000"**
Freehold land and buildings			75,000
Plant and machinery			38,600
Fixtures and fittings			8,500
Motor vehicles			4,000
Intangible assets (goodwill)			50,000
			176,100
Current assets:			
Inventory		32,000	
Trade receivables	32,500		
Less: Allowance for doubtful debts	(3,000)	29,500	
Cash		80	61,580
			237,680
Capital and liabilities:			
Capital accounts:			
Ali		50,000	
Baba		30,000	
Chake		20,000	100,000
Current accounts:			
Ali		20,000	
Baba		15,000	35,000
Long-term liabilities:			
Loan - Ali			10,000
Current liabilities:			
Trade payables		28,500	
Bank overdraft		64,180	92,680
			237,680

Additional information:

1. Provision was to be made for dissolution expenses of Sh.1,200,000.
2. Premiums have been paid on life assurance policies for each partner to provide the firm with cash on death. The premiums have been charged to insurance expenses and the cash payable on death of any partner is Sh.20,000,000.

3. The assets were duly sold or settled and the monies received as follows:

		"Sh.000"
20 June 2016:	Life policy on Ali's life	20,000
	Life policy on the lives of Baba and Chake surrendered	10,000
21 July 2016:	Freehold land and buildings	100,000
	Trade receivables (part)	15,000
	Inventory (part)	10,000
18 August 2016:	Plant and machinery	25,500
	Fixtures and fittings	6,000
	Motor vehicles	2,500
25 October 2016:	Inventory (remainder)	18,000
	Trades receivables (remainder)	21,000

4. Dissolution expenses amounted to Sh.1,000,000 and these were paid on 31 October 2016.
5. As soon as sufficient money was available to pay all outstanding creditors, this was done, discounts being received amounting to Sh.500,000.

Required:

(a) Statement showing how the proceeds of the dissolution would be shared among the partners using maximum possible loss method. (12 marks)

(b) Realisation account. (5 marks)

(c) Capital accounts. (3 marks)

(Total: 20 marks)

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CPA PART II SECTION 3

FINANCIAL REPORTING

THURSDAY: 26 May 2016. **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) For public sector entities with limited internally generated funds, external borrowings may constitute a viable alternative source of finance. Such borrowings are usually accessed at a cost.

Required:

In the context of International Public Sector Accounting Standard (IPSAS) 5 - Borrowing Costs:

(i) Identify three items that could be considered as borrowing costs. (3 marks)

(ii) Describe the two alternative accounting treatments for borrowing costs. (4 marks)

(b) Government grants are a common source of finance in developing economies.

Required:

(i) Explain the term "government grants" in the context of International Financial Reporting Standards (IFRSs). (3 marks)

(ii) Government grants may be accounted for using either the "income" approach or the "capital" approach.

Discuss the arguments for each of the two approaches above. (6 marks)

(c) Evaluate four criteria for consideration of a lease as a capital lease. (4 marks)

(Total: 20 marks)

QUESTION TWO

The following trial balance relates to Dodoma Ltd. as at 30 April 2016:

	Sh."000"	**Sh."000"**
Revenue		315,000
Inventory	32,000	
Raw materials purchased	150,000	
Production cost	60,000	
Distribution cost	12,000	
Administrative expenses	22,000	
Lease rentals paid	23,000	
Property, plant and equipment:		
- Cost	180,000	
- Accumulated depreciation (1 May 2015)		35,000
Income tax account	400	
Deferred tax		7,200
Trade receivables	50,000	
Cash and cash equivalents	24,800	
Trade payables		30,000
Ordinary share capital		154,000
Ordinary dividend paid	30,000	
Retained earnings		43,000
	584,200	584,200

Additional information:

1. On 20 April 2016, Dodoma Ltd. agreed with a customer to supply goods in the month of June 2016. The customer paid a deposit of Sh.5,000,000 which Dodoma Ltd. credited to its revenue account. Dodoma Ltd. has not made any adjustments to inventory on account of the deposit.
2. A stock take was done on 30 April 2016 that showed closing inventory at a cost of Sh.40,000,000. However, there were some damaged goods with a cost of Sh.4,000,000 that required to be repaired at a cost of Sh.400,000 and then sold for Sh.3,500,000.
3. On 1 May 2015, Dodoma Ltd. entered into two leasing contracts as explained below:

   Contract A
   The contract was to lease motor vehicles for a two year period. The estimated useful life of the vehicles at the start of the lease was 5 years. It was the responsibility of the lessor to repair and insure the vehicles. The lease stated that Dodoma Ltd. should pay a deposit of Sh.600,000 at the start of the lease followed by monthly payments of Sh.200,000 in arrears. The lease rentals figure for the year ended 30 April 2016 includes Sh.3,000,000 in respect of this lease. The vehicles were to be used by office staff.

   Contract B
   The contract was to lease a number of machines. The lease was for a four year period which was the estimated useful life of the machines. Dodoma Ltd. was required to repair and insure the machines which would have no residual value at the end of the lease. The lease rentals were set at Sh.10,000,000 every six months payable in advance. The lease rental figure for the year includes Sh.20,000,000 in respect of this lease. The rate of interest implicit in this lease was 5% per six months period. The fair value of the machines at inception of the lease was estimated at Sh.70,000,000.

4. Property, plant and equipment included:

	Cost Sh."000"	Accumulated depreciation Sh."000"
Property	90,000	5,000
Plant and equipment	90,000	30,000
	180,000	35,000

   - The plant and equipment is being depreciated on a straight line basis at a rate of 25% per annum.
   - The depreciable element of the property has an allocated carrying value of Sh.50,000,000 and is being depreciated on a straight line basis over 50 years from the date of original purchase. On 1 May 2015, the directors of Dodoma Ltd. revalued this property for the first time. The property had an estimated market value of Sh.100,000,000 as at 1 May 2015. It is further estimated that Sh.54,000,000 of this value relates to the depreciable element.

     The directors have decided not to make a transfer of excess depreciation on the revalued asset to retained earnings. Depreciation on all property, plant and equipment should be charged to cost of sales.

5. The estimated income tax liability for the year ended 30 April 2016 is Sh.5,000,000. The balance on the income tax account in the trial balance is the residue of the previous year after making the payment for that year.

6. A transfer of Sh.600,000 needs to be made to the deferred tax account for the period.

7. Trade receivables include an amount of Sh.10,000,000 owed by a customer who experienced cash flow problems prior to the year end. Dodoma Ltd. agreed to accept a payment of Sh.8,000,000 in full and final settlement of the debt and to defer the payment until April 2017. The expected return on sums invested for one year is 10%.

Required:

(a) Statement of comprehensive income for the year ended 30 April 2016. (10 marks)

(b) Statement of financial position as at 30 April 2016. (10 marks)

(Total: 20 marks)

QUESTION THREE

Faith and Hope were partners in a business of manufacturing and distributing construction materials, sharing profits and losses equally. The partners agreed that with effect from 1 January 2016, the business be split off and transferred to two separate companies; Mabati Ltd. and Nyumba Ltd. Mabati Ltd. took over the manufacturing business while Nyumba Ltd. took over the distribution business.

The partnership's statement of financial position as at 31 December 2015 was as follows:

		Sh."000"	Sh."000"
Non-current assets			
Land and building (at cost)			200,000
Motor vehicles (net book value)			150,000
Equipment (net book value)			33,000
			383,000
Current assets			
Cash in hand		1,000	
Account receivables:	Manufacturing	128,000	
	Distribution	216,000	
Inventory:	Manufacturing	460,000	
	Distribution	225,000	1,030,000
			1,413,000
Capital and liabilities			
Capital:	Faith	526,000	
	Hope	324,000	850,000
Non-current liability			
Bank loan			24,000
Current liabilities			
Bank overdraft		179,000	
Account payables:	Manufacturing	308,000	
	Distribution	52,000	539,000
			1,413,000

Additional information:

1. Mabati Ltd. took over all the non-current assets, cash, bank overdraft and its share of account receivables, inventory and account payables. Nyumba Ltd. took its share of account receivables, inventory and account payables.
   The assets and liabilities were transferred at book values and the partners were paid Sh.100 million being goodwill for the distribution business and Sh.80 million being goodwill for the manufacturing business.
2. The bank that had provided the loan agreed to accept Sh.14.4 million 10% debentures in Mabati Ltd. and Sh.9.6 million 10% debentures in Nyumba Ltd.
3. On 1 January 2016, the purchase consideration was settled by the allotment of fully paid ordinary shares of Sh.20 each in the respective companies as follows:

   Faith: 23,750,000 shares in Mabati Ltd. and the balance in shares in Nyumba Ltd.

   Hope: 15,920,000 shares in Nyumba Ltd. and the balance in shares in Mabati Ltd.
4. Mabati Ltd. also raised a 12% debenture of Sh.200 million on 1 January 2016 and paid-off the bank overdraft. The expenses incurred in raising the 12% debenture amounted to Sh.7 million.
5. Mabati Ltd. and Nyumba Ltd. also issued 1,000,000 and 1,500,000 fully paid ordinary shares of Sh.20 each respectively to two corporate investors, A Ltd. and B Ltd. on 1 January 2016.
6. None of the companies has amortised the goodwill.
7. The formation expenses were paid by the respective companies as follows:

	Sh. "million"
Mabati Ltd.	13
Nyumba Ltd.	8

Required:

Prepare the following accounts in a columnar format where applicable:

(a) Business purchases accounts. (6 marks)

(b) Partners' capital accounts. (2 marks)

(c) Bank account. (2 marks)

(d) Vendor's account. (2 marks)

(e) Statements of financial position for the two companies after formation. (8 marks)

(Total: 20 marks)

QUESTION FOUR

Jamii Ltd is a listed company operating in the service industry. During the year ended 30 April 2016, the company acquired two companies, Bora Ltd. and Njema Ltd. as part of its expansion plan. The following statements of comprehensive income relate to Jamii Ltd. and its investee companies Bora Ltd. and Njema Ltd. for the year ended 30 April 2016:

	Jamii Ltd. Sh. "million"	Bora Ltd. Sh. "million"	Njema Ltd. Sh. "million"
Revenue	102,180	52,800	33,150
Cost of sales	(76,635)	(36,990)	(26,520)
Gross profit	25,545	15,810	6,630
Investment income	584	60	-
	26,129	15,870	6,630
Operating expenses:			
Distribution expenses	(12,810)	(7,260)	(2,880)
Administrative expenses	(7,779)	(4,815)	(1,695)
Finance costs	(720)	(600)	(45)
Profit before taxation	4,820	3,195	2,010
Income tax expense	(1,530)	(1,125)	(645)
Profit after tax	3,290	2,070	1,365
Other comprehensive income:			
Revaluation of intangible asset	-	530	-
Total comprehensive income	3,290	2,600	1,365

Additional information:

1. On 1 May 2015, Jamii Ltd. acquired 80% of 1,125 million ordinary shares of Sh.10 each in Bora Ltd. for Sh.18,000 million. As at that date, the share premium account of Bora Ltd. had a balance of Sh.3,750 million while retained profit was Sh.3,705 million.
2. On 1 November 2015, Jamii Ltd. acquired 50% of 600 million ordinary shares of Sh.10 each of Njema Ltd. for Sh.6,300 million. As at that date, the share premium account of Njema Ltd. had a balance of Sh.1,500 million. The retained profit as at 1 May 2015 was Sh.2,085 million. The profit of Njema Ltd. accrued evenly throughout the year. The investment should be accounted for using the equity method.
3. On the date of acquisition of Bora Ltd., the property, plant and equipment of the company had a fair value which was in excess of book value by Sh.390 million, with a remaining useful life of 5 years.
4. The fair value of net assets acquired in Njema Ltd. approximated the book value as at the date of acquisition.
5. During the year ended 30 April 2016, Bora Ltd. sold goods worth Sh.6,000 million to Jamii Ltd. Bora Ltd. had marked up the goods by 25% above the cost. One quarter of these goods were included in the closing inventory of Jamii Ltd.
6. The goodwill arising on acquisition of the investee companies had suffered impairment losses to the extent of 25% during the year ended 30 April 2016. The group's policy is to apply the partial goodwill method.

Required:

(a) Computation of goodwill on each investment. (4 marks)

(b) Group statement of comprehensive income for the year ended 30 April 2016. (12 marks)

(c) Group statement of changes in equity for the year ended 30 April 2016. (4 marks)

(Total: 20 marks)

QUESTION FIVE

(a) With reference to International Accounting Standard (IAS) 10 "Events After the Reporting Period", explain the following terms:

(i) Events after the reporting period. (2 marks)

(ii) Adjusting events. (2 marks)

(iii) Non-adjusting events. (2 marks)

(b) The following trial balance was extracted from the books of Maendeleo Bank Ltd. as at 31 March 2016:

	Sh. "000"	Sh. "000"
Property, plant and equipment	28,854	
Interest on loans and advances		16,790
Interest on customers deposits	10,616	
Customers deposits		164,460
Share capital		20,000
Revaluation reserve		4,960
Salaries and wages	4,368	
Borrowed funds		7,040
Directors emoluments	1,290	
Depreciation on plant and equipment	1,630	
Other interest income		860
Specific provisions for doubtful debts		5,500
Interest on government securities		9,536
Other operating expenses	3,260	
Repairs and maintenance	420	
Printing and stationery	556	
Deposits and placements due from other banks	17,120	
Loans and advances to customers	135,310	
Deposits and placements due to other banks		12,820
Interest received on deposits and placements with other banks		7,600
Other interest expense	628	
Interest paid on deposits and placements from other banks	2,560	
Cash and balances with Central Bank	7,260	
Interim dividends paid	800	
Bad debts written off	558	
Share premium		6,000
Fees and commission income		1,528
Dividend income		816
Investment in securities	10,920	
Miscellaneous accruals		280
Government securities	26,400	
Retained earnings (1 April 2015)		4,960
Other assets	10,600	
	263,150	263,150

Additional information:

1. Analysis of debtors balances at the end of the year revealed that an additional provision of Sh3,700,000 for non performing loans should be made.
2. A provision of Sh.2,100,000 should be made for tax on the profit for the year ended 31 March 2016.
3. Interest accrued and not accounted for in the books as at 31 March 2016 was as follows:

	Sh."000"
Interest on loans and advances	1,284
Interest on customers deposits	896

4. Directors of the bank have proposed a final dividend at a rate of 5%.

Required:

Prepare for Maendeleo Bank Ltd.:

(i) Income statement for the year ended 31 March 2016. (8 marks)

(ii) Statement of financial position as at 31 March 2016. (6 marks)

(Total: 20 marks)

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KASNEB

CPA PART II SECTION 3

FINANCIAL REPORTING

THURSDAY: 26 November 2015. **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

Dola Ltd., a quoted company dealing in household goods has prepared the following trial balance as at 31 December 2014:

	Sh."million"	Sh."million"
Revenue		2,648
Loan interest paid	3	
Purchases	1,669	
Distribution costs	514	
Administrative expenses	345	
Interim dividends paid	6	
Inventory as at 1 January 2014	444	
Trade receivables and trade payables	545	434
Cash and cash equivalents	28	
Ordinary shares (Sh.10 each)		100
Share premium		244
General reserve		570
Retained earnings as at 1 January 2014		349
4% loan (payable 2024)		150
Land and buildings: Cost (Land Sh.60 million)	380	
Accumulated depreciation		64
Plant and equipment: Cost	258	
Accumulated depreciation		126
Investment property as at 1 January 2014	548	
Rental income		48
Proceeds from sale of equipment		7
	4,740	4,740

Additional information:

1. Closing inventory (as at 31 December 2014) amounted to Sh.388 million at cost. However, shortly after the year end, some inventory with a cost of Sh.15 million were sold for Sh.8 million.
2. Land and buildings were revalued on 1 January 2014 to Sh.800 million (including land at Sh.100 million). The buildings have a remaining useful life of 40 years.
3. The income tax liability in the year was estimated at Sh.20 million. Deferred tax was to be provided at Sh.7 million.
4. During the year, the company sold some equipment which had cost Sh.15 million with accumulated depreciation as at 1 January 2014 of Sh.3 million. An item of plant was also estimated to be impaired by Sh.4 million during the year.
5. Depreciation rates as per the company's policy are as follows:
   Buildings - over the useful life period.
   Plant and equipment - 20% reducing balance
   The company's accounting policy is to charge a full year's depreciation in the year of an asset's purchase and none in the year of disposal.
   The company treats depreciation of plant and equipment as a cost of sale and on land and buildings as an administrative expense.
6. Dola Ltd. values investment property at fair value. The fair value of the investment property as at 31 December 2014 was Sh.586 million.
7. During the year, the company made a one for three bonus issue capitalising its general reserves. This transaction has not been accounted for.

Required:
Prepare in a format suitable for publication the following financial statements for Dola Ltd. for the year ended 31 December 2014:

(a) Income statement. (6 marks)

(b) Statement of changes in equity. (6 marks)

(c) Statement of financial position. (8 marks)
(Total: 20 marks)

Note: Notes to the financial statements are not required. Round your figures to the nearest Sh. million.

QUESTION TWO

(a) With reference to International Financial Reporting Standards (IFRSs), discuss the accounting treatment of government grants, including the disclosure requirements. (6 marks)

(b) The following financial information was extracted from the books of Bondeni Commercial Bank Ltd. as at 30 September 2015:

	Sh."million"
Interest income - Loans and advances to customers	5,014
- Finance leases	4,680
- Government bonds	2,410
- Deposits with other banks	1,008
Interest expenses on customer deposits	2,500
Interest paid on deposits with other banks	56
Fees and commissions received	1,864
Foreign exchange commission receivable	110
Other operating incomes	1,500
Fees and other expenses	150
Impairment of loans and advances	840
Administrative costs	3,860
General operating expenses	3,140
Income tax expenses	2,100
Retained profits (1 October 2014)	16,640
Cash and balances with Central Bank	12,800
Deposits and balances due from other banks	19,200
Government bonds and other securities	15,410
Loans and advances to customers	132,270
Other assets	715
Deferred tax assets	60
Other investments	156
Property, plant and equipment	2,250
Intangible assets	2,150
Ordinary shares (Sh.10 each)	5,085
Share premium	90
Revaluation reserves	460
Statutory reserves	1,910
Customer deposits	150,995
Deposits from other banks	2,200
Current tax liabilities	1,145
Other liabilities	1,100
Deferred tax liabilities	1,446

Additional information:
1. Property, plant and equipment is to be revalued to Sh.4,250 million.
2. An allowance for unservised loans is to be created at 2% of the outstanding loans and advances to customers.
3. Intangible assets were impaired by 20% as at the end of the year.

Required:
Prepare the following for Bondeni Commercial Bank Ltd.:

(i) Income statement for the year ended 30 September 2015. (8 marks)

(ii) Statement of financial position as at 30 September 2015. (6 marks)
(Total: 20 marks)

QUESTION THREE

Amu and Bala are equal partners in a firm that buys and sells jewellery. The financial year end of the business is 31 December.

On 1 April 2014, they converted the partnership into a company, Ambala Ltd. The trial balance as at 31 December 2014 was given as follows:

	Sh."000"	Sh."000"
Sales		77,025
Purchases	57,000	
Discounts allowed	1,600	
Bad debts	800	
Rent	1,800	
Salaries	5,400	
Distribution expenses	600	
Formation expenses (company)	240	
Sundry expenses	950	
Capital: Amu		18,000
Bala		13,000
Trade payables		9,300
Furniture and fittings	2,400	
Motor vehicles	2,800	
Inventory as at 1 January 2014	25,000	
Trade receivables	8,100	
Cash at bank	5,635	
Drawings: Amu	2,700	
Bala	2,300	
	117,325	117,325

Additional information:

1. The partners have not made any changes to reflect the conversion of the partnership into a company.
2. Sales and purchases accrued in the ratio of 20% and 80% for the partnership and company respectively during the year.
3. Discounts allowed are to be apportioned in accordance with sales. Other expenses accrued evenly unless stated otherwise.
4. All the bad debts were written off in the last nine months of the year.
5. Depreciation per annum is to be provided using the reducing balance method as follows:

	Partnership	Company
Furniture and fittings	10%	12%
Motor vehicles	20%	18%

   Included in the motor vehicles balance in the trial balance is a purchase of a motor vehicle for Sh.700,000 on 1 May 2014.
6. Inventory as at 31 December 2014 was valued at Sh.20,825,000.
7. Amu and Bala withdrew Sh.600,000 and Sh.1,300,000 respectively in the quarter ended 31 March 2014. They are entitled to director's salary of Sh.1,800,000 each per annum.
8. The company issued 200,000 ordinary shares of Sh.150 each in settlement of the purchase of the assets and liabilities of the partnership.

Required:

(a) Income statement in columnar format for the partnership and company for the year ended 31 December 2014. (10 marks)

(b) Statement of financial position for the company as at 31 December 2014. (10 marks)

(Total: 20 marks)

QUESTION FOUR

(a) In the context of International Public Sector Accounting Standard (IPSAS) 19 - Provisions, Contingent Liabilities and Contingent Assets:

(i) Distinguish between an "executory contract" and an "onerous contract". (2 marks)

(ii) Summarise four disclosure requirements in relation to provisions. (4 marks)

(b) The following data has been collected from the Ministry of Commerce and Industrialisation for the fiscal year ended 30 June 2015:

	Sh. "million"
Reserves	22,500
Long-term borrowings	7,500
Accumulated surplus (1 July 2014)	9,375
Cash and cash equivalents	6,250
Receivable from exchange transactions	2,500
Inventory	1,250
Employee benefits obligation	5,000
Transfer from exchequer	31,250
Fines, penalties and levies	6,250
Revenue from exchange transactions	1,250
Property taxes revenue	7,500
Transfer from other ministries	625
Property, plant and equipment	43,750
Trade and other payables	6,250
Investment property	6,250
Employee costs	12,500
Transfers to other ministries	6,250
Impairment losses	1,250
Supplies and consumables used	5,000
Other expenses	15,000
Payments received in advance	2,500

Required:
Statement of financial position for the Ministry of Commerce and Industrialisation as at 30 June 2015 in accordance with IPSAS 1 - Presentation of Financial Statements. (6 marks)

(c) Europa Ltd., a manufacturing company, leased a plant from Smart Equipments Ltd. on a finance lease.

The details of the lease agreement are as follows:

Date of commencement of the lease	1 January 2015
Fair value of the plant on 1 January 2015	Sh.120 million
Expected useful life of plant	3 years
Annual lease payment (paid in advance)	Sh. 50 million
Interest rate implicit in lease	12% per annum
Lease period	3 years
Residual value of plant	Sh.6 million

Required:
Show by way of extracts, how the above transaction would be reflected by Europa Ltd. in the following:

(i) Income statements for the years ending 31 December 2015 and 31 December 2016. (3 marks)

(ii) Statements of financial position as at 31 December 2015 and 31 December 2016. (3 marks)

(d) Outline the main benefit of a sale and leaseback transaction to the vendor. (2 marks)
(Total: 20 marks)

QUESTION FIVE

The following is an extract of the financial statements of A Ltd., B Ltd. and C Ltd. for the year ended 30 September 2015:

Income statement for the year ended 30 September 2015

	A Ltd. Sh."million"	B. Ltd. Sh."million"	C. Ltd. Sh."million"
Revenue	9,120	4,940	4,560
Cost of sales	(3,610)	(1,092)	(1,064)
Gross profit	5,510	3,848	3,496
Distribution cost	(665)	(428)	(380)
Administrative expenses	(695)	(170)	(380)

	A Ltd.	B Ltd.	C Ltd.
Finance cost	(65)	(20)	-
	Sh."million"	Sh."million"	Sh."million"
Profit before tax	4,085	3,230	2,736
Income tax expense	(1,660)	(1,078)	(848)
Profit for the period	2,425	2,152	1,888
Retained profit brought forward	7,612	1,452	1,250

Statement of financial position as at 30 September 2015

	A Ltd. Sh."million"	B. Ltd. Sh."million"	C. Ltd. Sh."million"
Non-current assets:			
Property, plant and equipment	6,096	4,855	2,612
Investments	4,350	50	-
	10,446	4,905	2,612
Current assets:			
Inventory	1,460	853	737
Accounts receivable	1,880	765	573
Cash and bank balances	1,224	187	468
	4,564	1,805	1,778
Total assets	15,010	6,710	4,390
Equity and liabilities:			
Capital and reserves:			
Ordinary share capital	2,600	1,600	400
Share premium	1,500	300	-
Retained profit	8,237	3,604	3,138
	12,337	5,504	3,538
Non-current liability:			
Loan from bank	650	200	-
Current liabilities:			
Trade payables	1,463	646	382
Current tax	560	360	220
Bank overdraft	-	-	250
	2,023	1,006	852
Total equity and liabilities	15,010	6,710	4,390

Additional information:

1. A Ltd. acquired 40% of C Ltd. on 1 October 2014 for Sh.700 million.
2. A Ltd. also acquired 80% of the ordinary shares of B Ltd. on 1 January 2015 at a cost of Sh.3,430 million. The fair value of non-controlling interest as at this date amounted to Sh.800 million.
3. The fair value of B Ltd.'s property, plant and equipment on the date of acquisition was Sh.210 million above the book value with exactly 5 years remaining on the useful life of this property.
4. During the year ended 30 September 2015, B Ltd. sold goods to A Ltd. for Sh.140 million. B Ltd. marked up the goods at $16\,^2/_3$% on cost. Half of the goods remained in the stock of A Ltd. as at the year end.
5. As at 30 September 2015, A Ltd. owed B Ltd. Sh.80 million while C Ltd. owed A Ltd. Sh.15 million.
6. Goodwill was impaired as follows:
   B Ltd. 25%.
   C Ltd. 10%.

Required:
Prepare the following financial statements in the books of A Ltd. for the year ended 30 September 2015:

(a) Consolidated statement of comprehensive income. (7 marks)

(b) Statement of changes in equity. (3 marks)

(c) Statement of financial position. (10 marks)
(Total: 20 marks)

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CPA PART II SECTION 3

FINANCIAL REPORTING

PILOT PAPER

September 2015. **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) On 1 October 2014, P Ltd. acquired 60% of the equity share capital of S Ltd. in a share exchange of two shares of P Ltd. for three shares of S Ltd. On this date, shares of P Ltd. were trading at Sh.8 each.

Below are the financial statements for the two companies for the year ended 31 March 2015.

Income statements for the year ended 31 March 2015:

	P Ltd. Sh."000"	S Ltd. Sh."000"
Revenue	170,000	84,000
Cost of sales	(126,000)	(64,000)
Gross profit	44,000	20,000
Distribution costs	(4,000)	(4,000)
Administrative expenses	(12,000)	(6,400)
Finance costs	(600)	(800)
Profit before tax	27,400	8,800
Income tax expense	(9,400)	(2,800)
Profit for year	18,000	6,000

Statements of financial position as at 31 March 2015:

	Sh."000"	Sh."000"
Assets		
Non-current assets		
Property, plant and equipment	60,900	18,900
Investment property	20,300	6,300
	81,200	25,200
Current assets		
Inventory	12,080	5,000
Receivables	11,920	4,900
Bank	8,000	3,300
	32,000	13,200
	113,200	38,400
Equity and liabilities		
Capital and reserves		
Ordinary share capital (Sh.1 each)	20,000	8,000
Retained earnings	70,800	13,000
	90,800	21,000
Non-current liabilities		
10% loan notes	6,000	8,000
Current liabilities		
Trade payables	12,300	7,050
Accruals	4,100	2,350
	16,400	9,400
	113,200	38,400

Additional information:

1. The issue of shares on acquisition of S Ltd. has not yet been recorded by P Ltd.

2. As at the acquisition date, fair values of S Ltd.'s assets were equal to their carrying amount except for an item of plant, which had a fair value of Sh.2 million in excess of the carrying amount. The plant had a remaining useful life 5 years as at the acquisition date. S Ltd. has not revalued its assets.
3. Sales from S Ltd. to Patterson Ltd. in the post acquisition period amounted to Sh.8 million. S Ltd. made a mark up of 40%. Sh.2.8 million of these goods at cost to P Ltd. were still included in inventory on 31 March 2015.
4. S Ltd.'s trade receivables include Sh.800,000 due from P Ltd. which did not agree with the corresponding payables. This was due to cash paid by P Ltd. which was yet to be received by S Ltd.
5. P Ltd. has a policy of accounting for any non controlling interest at fair value. Fair value of goodwill attributable to non controlling interest in S Ltd. was Sh.2.4 million.
6. Neither of the company declared dividends in the year ended 31 March 2015.

Required:

(i) Consolidated statement of comprehensive income for the year ended 31 March 2015. (10 marks)

(ii) Consolidated statement of financial position as at 31 March 2015. (10 marks)

(Total: 20 marks)

QUESTION TWO

The following trial balance relates to B Ltd. as at 30 June 2015:

	Sh."000"	Sh."000"
Leasehold property at valuation 1 July 2014	75,000	
Plant and equipment at cost	114,900	
Accumulated depreciation - plant and equipment		36,900
Capitalised development expenditure 1 July 2014	30,000	
Inventory	30,000	
Trade receivables	64,650	
Trade payables and provisions		35,700
Revenue		450,000
Cost of sales	306,000	
Distribution costs	21,750	
Administrative expenses	33,300	
Preference dividend paid	1,200	
Interest on bank borrowings	300	
Ordinary dividend paid	9,000	
Research and development costs	12,900	
Ordinary shares Sh.1 each		75,000
8% redeemable preference shares		30,000
Retained earnings		36,750
Deferred tax		8,700
Leasehold property revaluation reserve		15,000
Accumulated amortisation 1 July 2014		9,000
Bank		1,950
	699,000	699,000

Additional information:

1. Leasehold property had a remaining useful life of 30 years as at 1 July 2014. The company's policy is to revalue its property at each year end. As at 30 June 2015 the leasehold property was valued at Sh.64.5 million. On 1 July 2014, an item of plant was disposed of for Sh.3.75 million cash. The proceeds were treated as sales revenue. The plant was still included in the trial balance at cost of Sh.12 million with the accumulated depreciation of Sh.6 million. All plant is depreciated at 20% per annum using the reducing balance method. Depreciation and amortisation on all non-current assets is charged to cost of sales and amounts for the year had not been provided.
2. Ignore deferred tax on revaluation charges.
3. In addition to capitalised development expenditure in the year amounting to Sh.30 million, further research and development costs were incurred in the year on a project that commenced on 1 July 2014. The research stage of the new project lasted until 30 September 2014 taking up Sh.2.1 million of the costs. From 1 October 2014, the project's development cost Sh.1.2 million per month. On 1 January 2015 the directors established the project's technical and commercial feasibility and committed to completion of the project. The project was still under development as at 30 June 2015.
4. Capitalised development is amortised at 20% per annum on a straight line basis and expensed research is charged to cost of sales.

5. B Ltd. is being sued by a customer for Sh.3 million for breach of contract. The company has obtained legal opinion that there is a 20% chance of losing the case. Accordingly the company has provided Sh.600,000 (20% of Sh.3 million) included in administrative expenses. The irrecoverable legal costs of defending the action are estimated at Sh.150,000 and these costs have not been provided for as the legal action is not expected in court until the next financial year.
6. The redeemable preference shares were issued on 1 January 2015 and have an effective interest rate of 12%.
7. Income tax should be provided for the year at Sh.17.1 million and the required deferred tax liability is Sh.9 million.

Required:
Prepare in a format suitable for publication:

(a) Statement of comprehensive income for the year ended 30 June 2015. (12 marks)

(b) Statement of financial position as at 30 June 2015. (8 marks)
(Total: 20 marks)

QUESTION THREE

(a) Enumerate four enhancing qualitative characteristics of good financial information. (4 marks)

(b) Fulcon Ltd. deals in Italian shoes. It has a head office in Westlands, Nairobi and branches in several parts of the city. Accounts of all branches are maintained in the head office books. The following information relates to transactions carried out by the Eastlands branch for the year ended 31 December 2014. The amounts are stated at selling price.

	Sh. "000"
Opening inventory	31,680
Goods received from head office	700,368
Goods received from Southlands branch	3,360
Goods sent to Northlands branch from Eastlands branch	4,320
Goods returned to Eastlands branch by credit customers	5,280
Goods returned to Northlands branch by an Eastlands branch customer	1,932
Goods returned to head office	8,160
Goods stolen from Eastlands branch	5,760
Cash sales	316,800
Credit sales	370,116

Additional information:
1. Goods were marked at a normal markup of $^3/_5$.
2. To clear some old stocks, goods with a normal selling price of Sh.3 million were marked down by 20%. Two thirds of these goods had been sold as at 31 December 2014.
3. Other than the goods stolen there were no shortages or surpluses of goods in the year.

Required:
(i) Eastlands branch inventory account for year ended 31 December 2014. (6 marks)

(ii) Eastlands branch markup account for year ended 31 December 2014. (6 marks)

(iii) Goods sent to Eastlands branch account for the year ended 31 December 2014. (4 marks)
(Total: 20 marks)

QUESTION FOUR

(a) Bien Ltd. has provided the following schedule of its long-term loans for the year ended 31 March 2015:

	1 April 2014 Sh."million"	**31 March 2015** Sh."million"
10% bank loan 2021	120	120
24% bank loan 2030	80	80
8% debentures	0	60

Additional information:
1. The 8% debenture was used to finance production of a mining equipment which commenced on 1 October 2014.
2. On 1 April 2014, the company had commenced construction of a power plant using existing borrowings. Expenditure for the construction was drawn with Sh.40 million being drawn on 1 April 2014 and Sh.30 million on 1 November 2014.

Required:
In line with provisions of IAS 23 (borrowing costs):

(i) Compute the borrowing costs to be capitalised. (4 marks)

(ii) Determine the cost of the assets constructed in the year. (4 marks)

(b) Madwang Ltd. leased out its plant to Kasheshe Hauliers Ltd. under a finance lease on 1 January 2010. The fair value of the plant on 1 January 2010 was Sh.870,000. The lease provided for 6 annual rentals of Sh.200,000 each receivable at the end of each year.

The interest rate implicit in the lease is 10%.

Required:
Using the actuarial method, show in the books of Madwang Ltd:

(i) Income statement extracts over the lease term. (6 marks)

(ii) Statement of financial position extracts suitably classified. (6 marks)
(Total: 20 marks)

QUESTION FIVE

(a) Explain the fair value model of accounting for investment property as per IAS 40 (Investment Property). (4 marks)

(b) The following information was extracted from the books of the Ministry of Tourism for the fiscal year ended 30 June 2015:

	Sh."000"
Accumulated fund	562,500
Cash and cash equivalents	375,000
Receivables	150,000
Inventory of consumables	75,000
Transfers from exchequer	1,875,000
Fees fines and licences	375,000
Liability for long term benefits	150,000
Long term borrowing	750,000
Finance costs	75,000
Supplies and consumables used	300,000
Wages and salaries	750,000
Other expenses	900,000
Transfers from other ministries	37,500
Transfers to other ministries	375,000
Computer equipment	200,000
Vehicles	175,000
Land and buildings	2,625,000
Revenue from exchange transactions	75,000
Other revenue	450,000
Payables	375,000
Reserves	1,350,000

Required:

(i) Statement of financial performance for the year ended 30 June 2015. (8 marks)

(ii) Statement of financial position as at 30 June 2015. (8 marks)
(Total: 20 marks)

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