## FINANCIAL ACCOUNTING

REVISION KIT

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## Syllabus

## FINANCIAL ACCOUNTING

## OBJECTIVE

To develop the candidate"s understanding of accounting principles, concepts and conventions and their application to organisations.

## SPECIFIC OBJECTIVES

A candidate who passes this subject should be able to:
$\square$
Apply the principles, concepts and conventions of accounting in keeping financial records

- Prepare financial statements
- Interpret information contained in financial statements.


## CONTENT

### 1.1 Introduction to Accounting

The nature and purpose of accounting
The basic principles, concepts and conventions underlying accounting reports The accounting equation
Accounting terminology
Organisation of the accounting profession in Kenya
The users of financial statements and their information needs

## Accounting Procedures and Techniques

Double entry book-keeping
The journals
The ledgers and their role in recording and summarising accounting data
Cash book and bank reconciliation statement
Extraction of trial balance
Correction of errors and use of suspense account
Control Accounts
Imprest system of petty cash

## Accounting for Assets and Liabilities

Accounting for current assets: cash; stocks; accounting for debtors provision for bad and doubtful debts
Tangible and intangible assets
Accounting treatment of current and long-term liabilities

## Preparation of Financial Statements

Year end adjustments and use of worksheets
Preparation of trading and profit and loss accounts and balance sheet of sole proprietorship Preparation of manufacturing accounts, trading and profit and loss accounts and balance sheets Income and expenditure accounts and balance sheets for non-trading organizations Closing of the books of accounts and use of income summary account

## Partnership Accounts

Basic contents for a partnership agreement; provisions of the Kenya Partnership Act; formatiots of a partnership
Accounting for initial investment of
partners Current and capital accounts
Division of profits and losses, preparation of trading and profit and loss accounts, appropriation accounts and balance sheets
Admission of partner(s)
Retirement of partner(s)

## Company Accounts

The financial and legal framework of limited liability companies
Issue of shares
Distinction between reserves, provisions and liabilities
Preparation of financial statements of limited liability companies

## Financial Ratio Analysis

Calculation and interpretation of elementary accounting ratios

## Incomplete Records

Preparation of accounts from incomplete records

## Topical Guide to Past Paper Questions

## ANALYSIS OF RECENT EXAMINATIONS

The paper consists of five compulsory questions, each carrying between 15 to 25 marks, but mostly averaging 20 marks. The analysis below shows the areas which have been examined in the past sittings and further in the Mocks and Revision Questions.

JUNE 2013
Question 1 Partnership and Manufacturing Accounts
Question 2 Not For Profit Organisation Accounts
Question 3 Company Accounts - Issue of Shares
Question 4 Control Accounts
Question 5 Accounting Ratios and Accounting Concepts

## DECEMBER 2012

Question 1 Correction of Errors and Use of Suspense Accounts
Question 2 Bank Reconciliation Statements
Question 3 Depreciation
Question 4 Company Accounts
Question 5 Financial Ratios

## JUNE 2012

Question 1 Incomplete Records
Question 2 Manufacturing Accounts
Question 3 Correction of Errors and Use of Suspense Accounts
Question 4 Partnerships - Admission of a new partner
Question 5 Company Accounts

## DECEMBER 2011

Question 1 Incomplete Records
Question 2 Financial ratio analysis
Question 3 Not For Profit Organisations Accounts
Question 4 Company Accounts - Issue of Shares
Question 5 Theory of Accounting Concepts
JUNE 2012
Question 1 Manufacturing Accounts
Question 2 Theory on Cashbooks and Bank Reconciliations
Question 3 Company Accounts
Question 4 Partnerships - Incomplete Records
Question 5 Theory on Users of Financial Statements

## DECMBER 2010

Question 1 Incomplete Records
Question 2 Not For Profit Organisation Accounts
Question 3 Company Accounts - Issues and Redemptions of Shares
Question 4 Accounting treatment for Long-term Assets
Question 5 Theory on Accounting treatment of Transactions

## MOCKS

## MOCK 1

Question 1 Company Accounts - Issue of Shares
Question 2 Company Accounts
Question 3 Bank Reconciliation Statement
Question 4 Depreciation
Question 5 Accounting Concepts

## MOCK 2

Question 1 Company Accounts
Question 2 Company Accounts - Expense Appropriation
Question 3 Not for Profit Organisations Accounts
Question 4 Bank Reconciliation Statement
Question 5 Correction of Errors

## MOCK 3

Question 1 Partnerships
Question 2 Control Accounts
Question 3 Bank Reconciliation Statements
Question 4 Depreciation
Question 5 Accounting Concepts

## MOCK 4

Question 1 Company Accounts
Question 2 Manufacturing Accounts
Question 3 Bank Reconciliation Statements
Question 4 Control Accounts
Question 5 Partnerships and Limited Companies Theory

## MOCK 5

Question 1 Accounts for Not For Profit Organizations
Question 2 Company Accounts
Question 3 Incomplete Records
Question 4 Corrections of Errors
Question 5 Theory on Types of Errors

## REVISION PAPERS

## REVISION PAPER 1

Question 1 Partnership Accounts
Question 2 Accounting for Non Current Assets
Question 3 Company Accounts
Question 4 Control Accounts
Question 5 Accounting Concepts and Company Accounts

## REVISION PAPER 2

Question 1 Partnership Accounts - Correction of Errors
Question 2 Partnership Accounts - Admission of a new Partner
Question 3 Company Accounts - Issue of Shares

Question 4 Ratio Analysis
Question 5 Preparation of Financial Statements Theory

## REVISION PAPER 3

Question 1 Bank Reconciliation Statement
Question 2 Depreciation, Disposal \& Acquisition of Fixed Assets
Question 3 Manufacturing Accounts
Question 4 Incomplete Records
Question 5 Accounting Concepts

## REVISION PAPER 4

Question 1 Bank Reconciliation Statement
Question 2 Depreciation
Question 3 Correction of Errors
Question 4 Incomplete Records
Question 5 Accounting Concepts

## REVISION PAPER 5

Question 1 Accounting Standards
Question 2 Accounting Concepts
Question 3 Accounting Ratios
Question 4 Petty Cash Books
Question 5 Accounting Ratios and Partnership Accounts

## PART II: Past Paper Questions and Answers

## Questions - Past Papers

## FINANCIAL ACCOUNTING 1

July 2008.
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 trial balance of Zach Ltd. as at 3I December 1999 was as follows:

|  | Sh. | Sh. |
| :--- | ---: | ---: |
| Share capital (10,000 Sh. 20 Ordinary shares) | 200,000 |  |
| Purchases and Sales | $1,220,000$ | $2,000,000$ |
| Debtors and Creditors | 400,000 | 140,000 |
| Profit and loss 1 January 1999 | 40,000 | 380,000 |
| Sales returns | 800,000 |  |
| Buildings at cost | $1,000,000$ |  |
| Plant at cost |  | 400,000 |
| Provision for depreciation: |  | 40,000 |
| Plant | 140,000 | 80,000 |
| Buildings |  | 160,000 |
| Purchases returns | 300,000 | 600,000 |
| Selling expenses |  | 20,000 |
| Bank | 180,000 |  |
| 10\% Debentures | 140,000 |  |
| Stock 1 January 1999 | $\underline{4,220,000}$ | $\underline{4,200,000}$ |
| Provision for bad debts |  |  |
| Operating expenses |  |  |
| Administrative expenses |  |  |
| Suspense account |  |  |
|  |  |  |

## Additional information:

1. Stock at 31 December 1999 was Sh. 360,000 .
2. Sales returns of $\operatorname{Sh} \cdot 20,000$ have been entered in the sales day book as if they were sales. When this error was discovered, the debtors account had been corrected but the sales figure was not rectified.
3. 5000 new shares were issued during the year at Sh.32. The proceeds have been credited to the suspense account.
4. A fully depreciated plant which cost Sh. 200,000 was sold during the year. No other entries except bank have been made. The remaining balance on the suspense account after ( 2 and 3 ) above represents the sale proceeds.
5. A debtor of Sh. 20,000 has been declared bankrupt. A general provision is required at $5 \%$ of debtors.
6. Rates of Sh. 30,000 paid in December covering half year to 31 March 2000 have not been entered in the books.
7. Debenture interest has not been paid.
8. Depreciation on plant is at $10 \%$ on cost and buildings at $2 \%$ on cost.
9. The directors propose to pay a dividend of Sh. 2 per share and transfer Sh. 20,000 to the general reserve.
10. Corporation tax at a rate of $32^{\prime} / 2 \%$ on profits is estimated to be Sh. 90,000 .

## Required:

(a)Suspense account for the year ended 3I December 1999
(b)Trading,profit and loss ccount for the year ended 31December1999.
(c) Balance sheet as at 31 December 1999.
(Total: 20marks)

## QUESTION TWO

Mr. Ancentus Okwengo is the sole proprietor of a small business. The following trial balance was extracted from his books at 31 March 2000.

| Capital | Sh. \#000 | $4,896$ |
| :---: | :---: | :---: |
| Freehold land and buildings (at cost) | 3,600 |  |
| Plant and machinery at cost | 3,480 |  |
| Provision for depreciation - plant and machinery |  | 1,680 |
| Delivery vans | 960 |  |
| Provision for depreciation - delivery vans |  | 672 |
| Loose tools at valuation on 1 April 1999 | 288 |  |
| Stocks 1 April 1999 | 2,232 |  |
| Purchases | 4,440 |  |
| Loose tools | 192 |  |
| Sales |  | 15,840 |
| Wages and Salaries | 5,288 |  |
| Rates and Insurance | 384 |  |
| Repairs and maintenance of buildings | 240 |  |
| Sales expenses including vehicle running costs | 344 |  |
| Electricity and power | 1,440 |  |
| Industrial training levy | 72 |  |
| Administration expenses | 672 |  |
| Provision for doubtfuldebts |  | 240 |
| Debtors and Creditors | 1,984 | 1,928 |
| Drawings | 480 |  |
| Bank |  | 864 |
| Cash in hand | $\underline{24}$ |  |
|  | 26,120 | 26,120 |

## Additional information:

1. Closing stock on 31 March

2000 was Sh.2, 008,000.
Loose tools at valuation
Sh.384, 000.

2 .Provision is to be made for the following amount
owing on 31 March 2000: Electricity and power Sh.192,000.
3. Payments in advance on 31 March

2000 were as follows: Van licenses
Sh.2,520 and rates Sh.13,800.
4. Depreciation on plant and machinery and delivery vans is to be provided at the rate of $20 \%$ and $25 \%$ respectively on cost at the end of the year.
5. Bad debts amounting to Sh. 26,000 are to be written off and the provision for doubtful debts is to be $10 \%$ of trade debtors.

## Required:

A ten-column worksheet for the year ended 31 March 2000.
(Total: 20 marks)

## QUESTION THREE

Kamau and Kimani are partners sharing profits and losses in the ratio 3:2 respectively. The partnership agreement provides for Kimani to receive a salary of Sh.4,000,000 per annum, and interest on capitals for both partners at $5 \%$ per annum. The partnership balance sheet as at 31 December 1998 was as follows:


On I April 1999 Kimata was admitted to the partnership. He had been a salaried employee, earning Sh. $8,000,000$ per annum. The terms of his admission to the partnership were as follows:

1. Kimata should introduce Sh. $12,000,000$ in cash as capital into the business.
2. Goodwill should be valued at Sh.14, 000,000 for the purpose of his admission. It was agreed that goodwill should not be included in the balance sheet of the new partnership.
3. Kimata should receive a salary as a partner of Sh.6, 000,000 per annum. Kimani's salary should be raised to Sh.6, 000,000.
4. Interest on capital should be raised from $5 \%$ to $6 \%$ per annum and calculated on the capital accounts after the elimination of goodwill.
5. The new profit sharing ratio for Kamau, Kimani and Kimata should be 4:2:1 respectively.

In preparing the draft financial statements for the year ended 31 December 1999, the partnership accountant, Otieno, calculated that the partnerships profit for the year was Sh. 55, 155,000, and that the working capital of the business as at 31 December 1999 was:

Sh. „000"
Stock
12,555
Debtors 3,500
Cash 8,800
Creditors and accruals 3,480
Profit is assumed to accrue evenly during the year.
Partners cash drawings for the year were Kamau Sh.23,705,000, Kimani Sh.19,525,000 and Kimata Sh.8,250,000.

## Required:

(a) The profit and loss appropriation account for the year ended 31 December 1999.
(b) The current and capital accounts of the partners for the year ended 31 December 1999.
(7 marks)
(c) Balance Sheet as at 31 December 1999.

## QUESTION FOUR

Joyce Njeri runs a City Market stall selling curios of all descriptions. Most of her sales are for cash, although regular customers are allowed credit. No double entry accounting records have been kept, but the following information is available.

Net Assets Summary at 31 March 1999
Sh. „000" Sh. „000"
Motor Van (Pick up)
Cost
Depreciation
3,000
2,500
Net Book value 500
Current Assets
Stock 500
Debtors 170
Cash at bank 2,800
Cash in hand $\underline{55}$
Current liabilities
Creditors $\underline{230}$
Net current assets $\quad \underline{3,295}$
Net assets $\quad \underline{3,795}$

## Additional information:

1. Joyce Njeri bought a new motor van in January 2000 receiving a part-exchange allowance of Sh.1,800,000 for her old van. A full year's depreciation is to be provided on the new van, calculated at $20 \%$ on cost.
2. Joyce Njeri has taken Sh. 50,000 per week for her personal use. She also estimates that petrol for the van, paid in cash, averages Sh.10,000 per week.
3. Other items paid in cash during the year were:

- Sundry expenses Sh.24, 000
- Repairs stall roof Sh. 20 1,000

4. Joyce Njeri makes a gross profit of $40 \%$ on selling prices. She is certain that no goods have been stolen but remembers that when her friend Anne Mwende was getting married, she gave her a wedding gift of curios worth Sh.100,000. Earlier in the year, she had presented curios worth Sh. 200,000 to her mother to be sold at her brother's university fees fundraiser. Both these figures are stated at selling prices.
5. Trade debtors and creditors at 31 March 2000 are Sh. 320,000 and Sh.233,000 respectively, and cash in hand amounts to Sh. 39,000 . No stock count has been made and there are no accrued or prepaid expenses.

A summary of bank statements for the twelve months shows:
Sh. „000"

## Credits

Cash banked (all cash sales) 7,521
Cheques banked (all credit sales) 1,500
Dividend income $\underline{210}$
$\begin{array}{ll}\text { Debits } & \underline{, 231} \\ \text { Purchase of motor van } & 3,200\end{array}$
Road license 80
Insurance on van 323
Creditors for purchases 7,777
Rent 970
Sundry 31
Accountancy fees 75
Bank overdraft interest 20
Returned cheque (assumed bad debt) $\underline{29}$

Interest amounting to Sh.27, 000 on bank overdraft for six months ended 31 March 2000 was debited in the bank statement on 1 April 2000.

## Required:

Joyce Njeri's trading and profit and loss account for the year to 31 March 2000 and a balance sheet as at that date. (Assume a 52 -week year). ( 20 marks)

## QUESTION FIVE

(a) Define the following accounting concepts and for each explain their implication in the preparation of financial Statements.
(i) The Going concern concept. (4 marks)
(ii) Business entity concept. (4 marks)
(iii) Materiality. (4 marks)
(iv) Realisation.
(b) Two accounting concepts or conventions could clash or there could be inconsistency between them.
Give two examples of such situations and explain how the inconsistency should be resolved.
(4 marks)
(Total: 20 marks)

## FINANCIAL ACCOUNTING 1

FRIDAY: 1 December 2008.
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) Briefly state the reasons why a company would not wish to distribute all its profits to its shareholders.
(b) The following balances were extracted from the books of Wamu Traders Ltd.as at 30 September 2000:

|  | Sh | Sh. |
| :--- | ---: | ---: |
| Ordinary shares of Sh. 20 each. Fully paid | 600,000 |  |
| $8 \%$ preference shares Sh. 20 each. Fully paid | 100,000 |  |
| Share premium account | 80,000 |  |
| $6^{\circ}$-o loan stock | 100,000 |  |
| Trade creditors | 148,000 |  |
| Trade debtors | $4,800,000$ | 330,000 |
| Sales | $4,220,000$ |  |
| Purchases |  | 5,000 |
| Discounts allowed |  | 13,000 |
| Discounts received |  | 500,000 |
| Freehold buildings: |  | 50,000 |
| $\quad$ At cost |  |  |
| $\quad$ Provision for depreciation |  | 640,000 |
| Fixtures and fittings: |  | 256,000 |
| $\quad$ At cost |  | 420.000 |
| $\quad$ Provision for depreciation | 130,000 |  |
| Stock I October 1999 |  | 56,000 |
| Returns outwards |  | 167,000 |
| Establishment expenses | 4,000 |  |
| Administration expenses | 18,000 |  |
| Selling and distribution expenses |  | 362,000 |
| Bad debts written off |  | 160,000 |
| Provision for doubtful debts |  | 25,000 |

The following additional information is available:

1. Depreciation is provided annually on the cost of fixed assets held at the end of the financial year at the following rate:

$$
\begin{array}{ll}
\text { Freehold buildings } & 20 \% \\
\text { Fixtures and fittings } & 10 \%
\end{array}
$$

2. The trade debtors balance includes Sh. 10,000 due from Musa who has now been declared bankrupt. In the circumstances, it has been decided to write the debt off as a bad debt.
3. The provision for doubtful debts as at 30 September 2000 is to be $5^{\circ}, \%$ of trade debtors
4. Establishment expenses prepaid at 30 September 2000 amounted to Sh.4,000.
5. Administration expenses accrued at 30 September 2000 amounted to Sh.7.000.
6. The company paid the interest on the loan stock for the year, ended 30 September 2000 on 30 October 2000.
7. Closing stock was valued at Sh.560,000.
8. The company's directors propose that the preference share dividend be paid and a dividend of $10 \%$ the ordinary shares he paid.

## Required:

(i) Trading and profit and loss account and appropriation account for the sear ended 30 September 2000 of Wamu Traders Ltd.
(ii) Balance sheet as at 30 September 2000.

## QUESTION TWO

(a) List the main advantages of ratio analysis.
(b) Munyah Ltd. is an expanding company and the following accounts relate to its operations for the years 1999 and 2000:

## Profit statement for the year ended 30 June

19992000
Sh. Sh.

| Sales | $3,000,000$ | $4,800,000$ |
| :--- | ---: | ---: |
| Less: cost of goods sold | $\underline{1,650,000}$ | $\underline{2,700,000}$ |
| Gross profit | $1,150,000$ | $\underline{2,100,000}$ |
| Less: trading expenses | $\underline{675,000}$ | $\underline{875,000}$ |
| Trading profit | $\underline{37,500}$ | $\underline{1,275,000}$ |
| Less: Debenture interest | 637,500 | $1,275,500$ |
| Net profit before taxation | $\underline{240,000}$ | $\underline{480,000}$ |
| Less: Corporation tax | 397,500 | 757,500 |
| Net profit after taxation | $\underline{187,500}$ | $\underline{262,500}$ |
| Less: Ordinary share dividend | 210,000 | 495,000 |


| Balance sheet as at 30 June | 1999 |  | 2000 |  |
| :---: | :---: | :---: | :---: | :---: |
|  | Sh. | Sh. | Sh. | Sh. |
| Fixed assets at cost | 1,500,000 |  | 2,100,000 |  |
| Less: Depreciation | 300,000 | 1,200,000 | 375,000 | 1,725,000 |
| Current assets: |  |  |  |  |
| Stock | 600,000 |  | 825,000 |  |
| Debtors | 375,000 |  | 525,000 |  |
| Cash | 120,000 |  | 1,350,000 |  |
| Less: current liabilities |  | 1,095,000 |  |  |
| Creditors | 217,500 |  | 300,000 |  |
| Taxation | 240,000 |  | 480,000 |  |
| Proposed dividend | 187,500 |  | 262,500 |  |
| Bank overdraft |  |  | 97,500 |  |
|  |  | (645,000) |  | (1,140,000) |
|  |  | 1,650,000 |  | 1,935,000 |
| Financed by: |  |  |  |  |
| Ordinary share capital (Authorised and issued) |  | 750,000 |  | 750,000 |
| Undistributed profits |  | 525,000 |  | 1,020,000 |
| $10 \%$ debentures |  | 375,000 |  | 165,000 |
|  |  | 1,650,000 |  | 1,935,000 |

## Required:

(i) Compute six accounting ratios for both 1999 and 200 (1 which you feel would be of particular value in assessing the Profitability and Liquidity of Munyah Ltd. (12 marks)
(ii) Comment on the current position of the company with the aid of the accounting ratios computed in (i) above and any other information that you consider to be relevant.
(3marks)

## QUESTION THREE

The following trial balance was extracted from the books of Literary and, Philosophical Society as at 30 September 2000:

| Balance at bank current account | $\begin{array}{r} \text { Sh. } \\ 724,800 \end{array}$ | Sh. |
| :---: | :---: | :---: |
| Accumulated fund 1 October 1999 |  | 5,771,200 |
| Land and building at cost | 3,700,000 |  |
| Debtors for subscription | 62,000 |  |
| Furniture and fittings | 1,874,000 |  |
| Provision for depreciation of furniture and fittings |  | 284,000 |
| Subscriptions |  | 1,450,800 |
| Lecturers" fees | 920,000 |  |
| Lecturers" travel and accommodation expenses | 358,000 |  |
| Donations |  | 108,000 |
| Camera and projector repairs | 17,000 |  |
| Projectors, cameras and audio equipment | 190,400 |  |
| Depreciation of equipment |  | 54,400 |
| Rates and water | 277,000 |  |
| Lighting and heating | 367,200 |  |
| Rental of rooms |  | 495,000 |
| Wages - caretaker | 880,000 |  |
| Restaurant | 1,600,000 |  |
| Bar staff | 800,000 |  |
| Purchase of food | 1,565,800 |  |
| Stock- bar I October 1999 | 473,600 |  |
| Bar receipts, |  | 4,032,000 |
| Bar purchases | 2,842,000 |  |
| Restaurant receipts |  | 3,642,000 |
| Loan |  | 1,600,000 |
| Deposit account - bank | 1,000,000 |  |
| Interest payable and receivable |  | 36,000 |
| Creditors for bar an d food |  | 178,400 |
|  | 17,651,800 | 17,651,800 |

## Additional information:

1: The bar stock was valued at Sh. 642.800 as at 30 September 2000.
2. It is expected that of the debtors for subscriptions, Sh. 43.600 will not be collectable.
3. The interest account is net. The loan is at a concessional rate of $4 \%$ while $\mathrm{I} 0 \%$ has been earned on the deposit account. No changes have taken place all year in the principal sums involved.
4. An invoice for Sh. 43.000 of wine had been omitted from the records at the close of the year although the wine had been included in the bar stock valuation.
5.Depreciation for the rear is to be provided as
follows: Furniture and fittings Sh. 194.000
Projectors. Cameras etc. Sh. 19.000

## Required:

(a) Bar and restaurant trading account for the year ended 30 September 2000 . ( 6 marks)
(b) An income and expenditure account for the year ended 30 September 2000. (8 marks)
(c) A balance sheet as at 30 September 2000.
(6 marks)
(Total: 20 marks)

## QUESTION FOUR

Nzioka is a grocer who had not kept complete books of account. The following was a summary of his bank statements for the ear ended 31 October 2000:

Sh.
7,034,000 Balance 1 November 1999
Amounts credited by bank

| Payments to trade | $6,100,000$ |
| :--- | ---: |
| creditors |  |
| Rent and rates | 95,000 |
| Fixtures | 20,000 |
| Lighting and heating | 42,000 |
| General expenses | 160,000 |
| Loan interest | 24,000 |
| Drawings | 180,000 |
| Customer cheque | 36,000 |
| dishonoured |  |
| $\mathbf{7 , 0 3 4 , 0 0 0}$ | Balance 31 October 2000 |

The following information is also available

1. Trading receipts consists partly of cash and party of cheques. During the year. Nzioka had paid out of his cash takings wages amounting to Sh. 590.000 and sundry expenditure of Sh 28.000. He retained $S h .600$ a week (assume $52 \sim$ weeks in a year) pocket money and maintained a balance of Sh.4.000 in the till tot-change. The balance of his takings. together with cheques amounting to Sh. 50,000 which he had cashed out of his takings was paid into the bank.
2. Cheque drawn payable to trade creditors. But not presented at I November 1999 amounted to Sh56000 and at 3I October 2000 Sh.64.000.
3. All dishonoured cheques were re-presented and honoured during the year.
4. The loan interest was paid to the lender who had lent Nzioka Sh. 800.000 some years ago at a rate of $3^{\circ}$ o p.a. The interest was duly paid half-yearly on 31 January and 31 July and the loan was still outstanding at the close of the year.
5. Discounts allowed by trade creditors amounted to Sh. 96.000 and those allowed to debtors were Sh. 104.000.
6. 

31 October 2000

Accrued general expenses
Rates paid in advance
Fixtures valued at
Trade creditors
Creditors for lighting and heating

As at 1 November $\begin{array}{r}\mathbf{1 9 9 9} \\ \text { Sh. } \\ 900,000 \\ 560,000\end{array}$
As at 1 November
$\mathbf{1 9 9 9}$
Sh.
900,000
560,000
As at 1 November
$\mathbf{1 9 9 9}$
Sh.
900,000
560,000
As at 1 November
$\mathbf{1 9 9 9}$
Sh.
900,000
560,000
As at 1 November
$\mathbf{1 9 9 9}$
Sh.
900,000
560,000
48,000
8,000
560,000
360,000
16,000

Sh.
1,600,000
640,000 (includes a bad debt Sh. 40,000)
38,000 (to be written off)
10,000
510,000
440,000
14,000

Required:
(a) A statement of Nzioka's capital on 1 November 1999.
(b) Profit and loss account for the year ended 31 October 2000 and a balance sheet at that date.

## QUESTION FIVE

(a) Explain giving examples the distinguishing features of liabilities, provisions and reserves. (9 marks),
(b) State how each of these items in (a) above are to be included and shown in the financial statements of a company ( 6 marks)
(Total: 15marks)

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

## QUESTION ONE

Atieno, Babu and Chesire have been trading in partnership sharing profits/losses in the ration of 5:3:2 respectively. On 1 April 2000 they admitted their manager, Dagana as a partner and the profit sharing ratio was changed to 4:3:2:1 FOR Atieno, Babu, Chesire and Dagana respectively.

The partners valued the goodwill at Sh.510,000. Dagana paid Sh.200,000 as capital and his share of goodwill, which should be based on capital contributions.

The partners do not wish to retain the goodwill account after admission of Dagana. The admission of Dagana has not been fully recorded other than the cash receipt of Sh.376,500.

The following is the trial balance of the partnership as at 31 March 2001:

Sh.
Capital accounts - Atieno

- Chesire

Current accounts- Atieno

- Babu
- Chesire

Drawings- Atieno

- Babu
- Chesire
- Dagana

Land and buildings at cost
Furniture and fittings at cost
Provision for depreciation of furniture and fittings
Motor vehicles
Provision for depreciation on motor vehicles
Trade debtors and creditors 365,000
Dagana account
Purchases and sales
Stock 1 April 2000
Salaries and wages
Rates
Telephone and postage
Vehicles running expenses
Insurance and subscriptions
General expenses
Bank charges and interest
Bad debts
Returns inwards and outwards
Cash in hand
Cash in bank

| Sh. | Sh. |
| ---: | ---: |
|  | 700,000 |
|  | 600,000 |
|  | 400,000 |
|  | 350,000 |
|  | 325,000 |
| 250,000 |  |
| 260,000 |  |
| 250,000 |  |
| 175,000 |  |
| $2,000,000$ |  |
| 500,000 | 150,000 |
| 860,000 |  |
|  | 480,000 |
| 365,000 | 823,500 |
|  | 376,500 |
| $3,380,000$ | $5,975,000$ |
| 465,000 |  |
| 295,000 |  |
| 137,000 |  |
| 116,000 |  |
| 396,000 |  |
| 162,000 |  |
| 72,000 |  |
| 124,000 |  |
| 48,000 | 75,000 |
| 61,000 |  |
| 24,000 |  |
| 490,000 | $-450,000$ |

## Notes:

1) Depreciation on furniture and fittings and motor vehicles is at $10 \%$ and $20 \%$ on reducing balance respectively.
2) The closing stocks were valued at Sh.560,000.
3) Accrued salaries and wages and telephone bills amounted to Sh. 24,000 and Sh. 14,000 repectively.
4) Prepaid subscriptions and rates amounted to Sh.5,000 and Sh.25,000 respectively.
5) The partners decided that Dagana should be given a monthly salary of Sh. 20,000 for the whole year from 1 April 2000 to 31 March 2001.
6) Dagana took goods for own use at cost amounting to Sh.185,000. No entry has been made in the books.
7) The old partners shared the cash paid by Dagana for part of his goodwill.

## Required:

a) Trading, profit and loss account for the year ended 31 March 2001. (10 marks)
b) Partners capital accounts.
c) Partners current accounts.
(3 marks)
d) Balance sheet as at 31 March 2001.
(5 marks)
(Total: 20 marks)

## QUESTION TWO

a) Explain the following terms:
i) Share premium (2 marks)
ii) Rights issue (3marks)
b) The Wide Trading Company Limited has an authorised capital of Sh.500,000 divided into 5,000 ordinary shares of Sh. 100 each.

On 1 January 2001, the Board of directors decided to issue 4,000 shares at Sh. 125 each payable as Sh. 50 on application. Sh. 50 on allotment (including the Sh. 25 premium) and Sh. 25 on first and final call. The applications were receivable on 20 January 2001 when allotment was made. The allotment money was receivable by 15 February 2001. The first and final call was made on 15 March 2001 and the call money receivable by 31 March 2001. Applications were received for 6,000 shares. The directors decided to refund money for 1,000 shares and the other applicants were allotted prorata with the excess money utilised to meet part of the allotment money. The balance of the allotment money was received on the due date. The first and final call was made and the call money received on the due date except for allotees of 200 shares.

The 200 shares with calls arrears were forfeited on 10 April 2001 and sold for cash at Sh. 85 eacg ib 12 April 2001.

Note: No other transactions took place during the above period.

## Required:

i) Application and Allotment Account, First and Final Call Account, Ordinary Shate Capital Account. Share Premium Account, Calls in Arrears Account. Forfeited Shates Account and the bank account.
ii) Balance sheet as at 12 April 2001
(12 marks)
(3 marks)
(Total: 20 marks)

## QUESTION THREE

Kimeu commenced his business of making furniture on 1 April 2000. Due to his limited accounting knowledge he has not maintained proper books of account. You have been engaged to examine his records and prepare appropriate accounts therefrom. You perform an examination of the records and from interviews with Kimeu, you ascertain the following information:

1. At the commencement of business on 1 April 2000, he deposited Sh. 1,200,000 into a business bank account. On the same day he brought into the firm his pickup and estimated that it was worth Sh. 660,000 then and that from 1 April 2000 it will have useful life of three years.
2. To increase his working capital he borrowed Sh. 400,000 at $15 \%$ interest per annum on 1 July 2000 from his sister but no interest has yet been paid.
3. On 1 April 2000, Sally was employed as a clerk at a salary of Sh. 720,000 per annum.
4. He had drawn Sh. 18,000 per week from the business account for private use during the year.
5. He purchased timber worth Sh. $1,960,000$ out of which Sh. 158,000 worth of stock was retained in the workshop on 31 March 2001. He also spent Sh. 960,000 on the purchase of some equipment at the commencement of the business which he estimates will last him five years.
6. Electricity bills received up to 31 January 2001 were Sh. 240,000 . Bills for the remaining two months were estimated to be Sh. 48,000 . Motor vehicle expenses were Sh. 182,000 while general expenses amounted to Sh. 270,000 for the year. Insurance premium for the year to 30 June 2001 was Sh.160,000. All these expenses have been paid by cheque.
7. Rates for the year to June 2001 were Sh. 36,000 but these had not been paid.
8. Sally sent out invoices to customers for Sh. $6,178,000$ but only Sh.5,080,000had been received by 31 March 2001. Debts totalling to Sh. 17,000 were abandoned during the year as bad. Other customers for jobs too small to invoice have paid Sh.726,000 in cash for work done of which Sh. 560,000 was banked . Kimeu used Sh.75,000 of the difference to pay for his family"s food stuff bought Kenya Charity Sweepstake tickets worth Sh. 24,000 and Sally used the rest on general expenses except for Sh. 30,100 which was left over in the drawer in the office on 31 March 2001.
9. You agree with Kimeu that he will pay you Sh. 55,000 for accountancy fee.

## Required:

a) Profit and loss account for the year ended 31 March 2001.
(10 marks)
b) Balance sheet as at 31 March 2001.

## QUESTION FOUR

Kaluwax Ltd. manufactures one product which it sells to the wholesale trade. The following trial balance was extracted from the books of the company at 30 April 2001:

## Sh. <br> Sh.

Stocks at 1 May 2000
Raw materials, at cost
Work- in-progress, at factory cost
350,000
Finished goods (3,500 units) at factory cost
1,800,000
Raw materials purchased
3,500,000
Sales (12,000 units)
3,950,000

Manufacturing wages
3,000,000
Factory rent and rates
$3,000,000$
$1,400,000$
Factory light, heat and power
655,000
Plant at cost
Plant depreciation at 1 May 2000
Works manager"s salary
245,000
Plant repairs
400,000
Administrative overheads
Factory lease at cost (20 years duration)
Amortisation at 1 May 2000
Share capital
1,200,000
Debtors
Bank balance
Creditors
1,800,000
4,000,000
18,000,000
$6,000,000$
2,800,000

7,500,000
3,050,000
1,600,000

Carriage inwards
200,000
$\underline{31,950,000}$$\underline{ }$

The following additional information is available:

1. Plant depreciation is to be provided at $10 \%$ on the cost of plant owned at the year end.
2. Raw materials costing Sh.500,000 were in stock on 30 April 2001.
3. Finished goods are transferred to the warehouse as soon as they are completed. During the year, 10,000 units were completed and transferred to the warehouse. Work-in-progress at the end of the financial year (at factory cost) amounted to Sh.2,300,000.
4. There was no wastage or pilferage during the current year.

## Required:

a) Manufacturing, trading and profit and loss account for the year ended 30 April 2001.
(12 marks)
b) Assume the facts as in (a) above, except that it had always been the company"s practice to transfer completed units from the factory to the warehouse at cost plus $25 \%$ and to value stocks of finished goods at the transfer price for the trading account but at factory cost for balance sheet purposes. Show how the manufacturing, trading and profit and loss account for the year ended 30 April 2001 would appear.
(8 marks)
(Total: 20 marks)

## QUESTION FIVE

You have been asked to advise on the appropriate accounting treatment for the following situations arising in the books of various companies. The year end in each case can be taken as 30 April 2001 and you should assume that the amounts involved are material.

## Required:

For each of the situations below, outline the accounting treatment you would recommend and give the reasoning principles involved.
a) At the year end there was a debit balance in the books of a company for Sh. 150,000 representing an estimate of the amount receivable from an insurance company for an accident claim. In May 2001 before the directors had agreed on the final draft of the published accounts, the amount of the claim was finally settled as Sh.186,000. (4 marks)
b) A company has an item of equipment which cost Sh.4,000,000 in 1999 and was expected to last for ten years. At the beginning of the year ended 30 April 2001 the book value was Sh. $2,800,000$. It is now thought that the company will soon cease to make the product for which the equipment was specifically purchased. Its recoverable amount is only Sh.800,000 at 30 April 2001. (4 marks)
c) On 31 March 2001, a company entered into legal action defending a claim for supplying faulty machinery. The company"s lawyers advise that there is a $20 \%$ probability that theclaim will succeed. The amount of the claim is Sh.5,000,000. (4 marks)
d) An item has been produced at a manufacturing cost of Sh.18,000 against a customer"s order at an agreed price of Sh.23,000. The item was in stock at the year end awaiting delivery against instructions. In May 2001, the customer was declared bankrupt and the most reasonable course of action seems to be to make a modification to the unit, costing approximately Sh.3,000 which is expected to make it marketable with other customers at a price of about Sh.19,000. (4 marks)
e) At 30 April, the company has a total potential liability of Sh.10,004,000 for warranty work on contracts. Past experience shows that $10 \%$ of these costs are likely to be incurred, $30 \%$ may be incurred but that the remaining $60 \%$ is highly unlikely to be incurred. (4 marks)
(Total: 20 marks)

## DECEMBER 2009

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

QUESTION ONE
Nafuu Foods Ltd. is a company in the hospitality industry. The following trial balance has been extracted from its books on 31 October 2001:

|  | Sh.'000' | Sh. ${ }^{\prime} 000{ }^{\prime}$ |
| :---: | :---: | :---: |
| Revenue |  | 816,160 |
| Cost of sales | 401,000 |  |
| Wages and salaries | 186,440 |  |
| Operating expenses | 95,860 |  |
| Insurance | 1,180 |  |
| Directors' fees | 960 |  |
| Ordinary share capital; 5,200,000 shares of Sh. 20 each fully paid |  | $\begin{array}{r} 104,000 \\ 77,600 \end{array}$ |
| Profit and loss account, 1 November 2000 |  | 160,000 |
| $9 \%$ debenture stock - secured |  | 18,000 |
| Share premium |  | 56,400 |
| Capital redemption reserve | 63,860 | 61,520 |
| Trade debtors and creditors | 240 |  |
| Bad debts written off | 400 |  |
| Audit fees | 13,900 |  |
| Interest on loan and overdraft | 17,300 |  |
| Depreciation expense |  | 900 |
| Accruals |  |  |
| Interim dividends paid | 26,000 |  |
| Freehold land and buildings | 164,600 |  |
| Leasehold land and buildings (over 50 years) | 125,600 |  |
| Leasehold land and buildings (under 50 years) | 51,900 |  |
| Furniture and equipment | 85,600 |  |
| Stock | 46,400 |  |
| Prepayments | 720 |  |
| Bank balance | 2,820 |  |
| Investments | 9,800 |  |
|  | 294,580 | 294,580 |

## You are provided with the following additional information:

1. The balances of fixed asset accounts as at the beginning of the year and additions during the year were as follows:

|  | Cost or valuation <br> 1 November 2000 <br> Sh.'000' | Accumulated <br> depreciation <br> Sh.'000' | Additions <br> during the year |
| :--- | ---: | ---: | ---: |
| Sh.'000 |  |  |  |

a. The company does not provide for depreciation on freehold properties pro properties held on lease with 50 years or more to run at the balance sheet date. Properties held on lease with less than 50 years to run are depreciated over the unexpired term. Items of equipment are depreciated over their estimated useful life.
2. Some of the leasehold property in the books costing Sh. $7,500,000$ had just 50 years remaining on the lease in October 2000 and has not yet been transferred to the under 50 years category.
3. Disposals during the year included the following:

|  | Cost | Accumulated depreciation | Sale proceeds |
| :---: | :---: | :---: | :---: |
|  | Sh. ${ }^{\mathbf{0}}{ }^{\prime}{ }^{\prime}$ | Sh. ${ }^{(000}{ }^{\prime}$ | Sh.'000.' |
| Freehold land and buildings | 3,600 | - | 4,800 |
| Leasehold under 50 year | 2,300 | 1,700 | 960 |

All the sale proceeds have been included in the revenue; no other adjustment has been made.

The determination of depreciation expense for the year included in the trial balance above has correctly been done for those properties not disposed of and included in the under 50 years category at the beginning of the year.
4. Freehold land was revalued on an existing use basis by a professional valuer but the Surplus of Sh.6,000.000 has not yet been brought into account.
5. The investments in the trial balance are temporary quoted securities. As at 31 October 2001 their market value was Sh.10,500,000. Income from the investments of Sh.450,000 is included in revenue
6. Additional audit fees of Sh. 600,000 need to be provided for.
7. The total balance of cash at bank includes Sh. 1,500,000 overdraft on one of the accounts.
8. The corporation tax oil the year's profit has been estimated at Sh. $27,000,000$. Corporation tax on the previous years profit was finally agreed with the tax authorities to be Sh. 3 10,000 more than had been provided for in the profit and loss account of the year.

The directors have decided to recommend a final dividend of Sh. 5 per ordinary share.

## Required:

(a) A schedule showing fixed assets movements for the year ended 31 October 2001.
(10 marks)
(b) Profit and loss account for the year ended 31 October 2001.
(c) Balance sheet as at 31 October 2001.
(5 marks)
(Total: 25 marks)

## QUESTION TWO

Rotich and Sinei have been in partnership for several years, sharing profits and losses in the ratio $2: 1$. Interest on fixed capitals was allowed at the rate of $10 \%$ per annum, but no interest was charged or allowed on current accounts.

T he following was the partnership trial balance as at 30 April 2001:

|  | Sh. | Sh. |
| :---: | :---: | :---: |
| Fixed capital accounts |  |  |
| Rotich |  | 750,000 |
| Sinei |  | 500,000 |
| Current accounts |  |  |
| Rotich |  | 400,000 |
| S in e i |  | 300,000 |
| Leasehold premises (purchased 1 May | 2,250,000 |  |
| 2000) |  |  |
| Purchases | 4,100,000 |  |
| Motor vehicle (cost) | 1,600,000 |  |
| Balance at bank | 820,000 |  |
| Salaries (including partners' drawings) | 1,300,000 |  |
| Stocks: 30 April 2000 | 1,200,000 |  |
| Furniture and fittings (cost) | 300,000 |  |
| Debtors | 225,000 |  |
| Accountancy and audit fees | 105,000 |  |
| Wages | 550,000 |  |
| Rent, rates and electricity | 310,000 |  |
| General expenses (Sh. 352.400 for the six months To 31 October 2000) | 660,000 |  |
| Cash introduced - Tonui |  | 1,250,000 |
| Sales (Sh.3, 500,000 to 31 October 2000) |  | 8,750,000 |
| Accumulated depreciation: I May 2000 D |  |  |
| Motor vehicle |  | 300,000 |
| Furniture and fittings |  | 100,000 |
| Creditors |  | 1,070,000 |
|  | 13,420,000 | 13,420,000 |

## Additional information:

1. On 1 November 2000,'Tonui was admitted as a partner and from that date, profits and losses were shared in the ratio 2:2:1. For the purpose of this admission, the value of goodwill was agreed at Sh.3, 000,000. No account for goodwill was to be maintained in the books, adjusting entries for transactions between the partners being made in their current accounts. On that date, Tonui introduced Sh.1, 250,000 into the firm of which Sh.375, 000 comprised his fixed capital and the balance was credited to his current account
2. Interest on fixed capitals was still to be allowed at the rate of $10 \%$, per annum after Tonui admission, no interest was to be charged or allowed on current accounts.
3. Any apportionment of gross profit was to he made on the basis of sales. Expenses, unless otherwise indicated, were to be apportioned on a time basis.
4. A charge was to be made for depreciation on motor vehicle and furniture and fittings at $20 \%$ and $\mathrm{I} 0 \%$ per annum respectively, calculated on cost.
5. On 30 April 2001, the stock was valued at Sh. 1,275,000.
6. Salaries included the following partners' drawings:

Rotich Sh.150,000 , Sinei Sh. 120,000 and Tonui Sh.62,500
7. A difference in the books of Sh. 48,000 had been written off at 30 April 2001 to general expenses, which was later found to be due to the following clerical errors:

- Sales returns of Sh.32, 000 had been debited to sales returns but had hot been posted to the account of the customer concerned;
- The purchases journal had been under cast by Sh.80, 000.

8 Doubtful debts (for which full provision was required) amounted to Sh.30, 000 and Sh.40, 000 as at 31 October and 30 April 2001 respectively.
8. On 30 April 2001, rates and rent paid in advance amounted to $S h .50,000$ and a provision of Sh. 15,000 for electricity consumed was required.

## Required:

(a) Trading and profit and loss account for the year ended 30 April 2001,
(9mark)
(b) Partners current accounts for the year ended 30 April 2001. (4 marks)
(c) Balance sheet as at 30 April 2001.
(7 marks)
(Total: 20 marks)

## QUESTION THREE

(a) State and briefly explain any three distinguishing features between
(i) A receipts and payments account and
(ii) Income and expenditure account.
(6 marks)
(b) The accountant of Mamba Sports Club has extracted the following information from the books of account for the year ended 31 March 2001:

| Receipts | Sh. | Payments | Sh. |
| :---: | :---: | :---: | :---: |
| Balance brought forward | 288,000 | Salaries and wages | 254,000 |
| Subscriptions: |  | New equipment | 565,000 |
| Year 1999/2000 | 249,000 | Repairs and maintenance | 124,000 |
| 2000/2001 | 2,050,000 | Office expenses | 415,000 |
| $2001 / 2002$ | 194,000 | Printing and stationery | 168,000 |
| Dinner dance | 723,000 | Purchase of beverages | 497,000 |
| Beverage sales | 657,000 | Dinner dance expenses | 315, 000 |
| Investments income | 400,000 | Refund of subscriptions | 45,000 |
|  |  | Sports prizes | 25.000 |
|  |  | Transport | 248,000 |
|  |  | Investments | 1,500,000 |
|  |  | Balance carried forward | 405,000 |
|  | 4,561,000 |  | 4, 561,000 |
| Balances as at |  | 31 March 2000 | 31 March 2001 |
|  |  | Sh. | Sh. |
| Furniture and fittings (net) |  | 240,000 | - |
| Equipment (net) |  | 690,000 | - |
| Investments at cost |  | 3,500,000 | - |
| Subscriptions in arrears |  | 300,000 | 375,000 |
| Salaries accrued |  | 68,000 | 72,000 |
| Stock of beverages |  | 162,000 | 184,000 |
| Subscriptions in advance |  | 85,000 | - |

## Additional information:

1. Subscriptions in arrears are written-off after twelve months.
2. Depreciation is provided for on reducing balance method at $10 \%$ and $20 \%$ per annum on furniture and fittings and equipment respectively.
3. Investments, which had cost Sh.500, 000 were sold on 30 March 2001 for Sh.625,

0 . No entries have been made in the books in this respect.

## Required:

(a) Income and expenditure account for the year ended 31 March 2001.
(b) Balance sheet as at 31 March 2001.
(Total: 20 marks)

## QUESTION FOUR

(a) Explain the term "bank reconciliation" and state the reasons for its preparation. (6 marks)
(b) Ssemakula, a sole trader received his bank statement for the month of June 2001. At that date the bank balance was Sh. 706,500 whereas his cash book balance was Sh. $2,366,500$. His accountant investigated the matter and discovered the following discrepancies:

1. Bank charges of Sh.3, 000 had not been entered in the cashbook.
2. Cheques drawn by Ssemakula totaling Sh.22,500 had not yet been presented to the bank
3. He had not entered receipts of Sh.26,500 in his cashbook.
4. The bank had not credited Mr. Ssemakula with receipts of Sh.98, 500 paid into the bank on 30 June 2001.
5. Standing order payments amounting to Sh.62, 000 had not been entered into the cashbook.
6. In the cash book Ssemakula had entered a payment of Sh. 74,900 Sh. 79400 .
7. A cheque for Sh. 15,000 from a debtor had been returned by the bank ma rked "refer to drawer" but had not been written back into the cashbook.
8. Ssemakula had brought forward the opening cash balance of Sh.329, 250 as a debit balance instead of a credit balance.
9. An old cheque payment amounting to Sh. 44,000 had been written back in the cashbook but the bank had already honoured it.
10. Some of Ssemakula's customers had agreed to settle their debts by paying directly into his bank account. Unfortunately, the bank had credited some deposits amounting to Sh.832, 500 to another customer's account. However, acting on information from his customers, Ssemakula had actually entered the expected receipts from the debtors in his cashbook.

## Required:

(i) A statement showing Ssemakula's adjusted cash book balance as at 30 June 2001.
(9 marks)
(ii) A bank reconciliation statement as at 30 June 2001.
(Total: 20 marks)

## QUESTION FIVE

The accounting profession has for a long time relied on certain accounting conventions to guide accounting practice. Yet the application of the sane conventions has been the source of cripicism of the quality and relevance of information contained in financial reports.
Some of these conventions include:
(a) The business entity principle.
(h) The historical cost principle.
(c) The monetary principle.
(d) The matching principle.
(e) The conservatism principle.

## Required:

For each of the principles listed above:
(a) Explain its meaning.
(b) Justify its use.
(c) Explain any weaknesses associated with its use.

## FINANCIAL ACCOUNTING 1

May 2010.
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

On 31 December 2001. an inexperienced book-keeper working for Wanji, a sole trader, extracted a trial balance. Due to errors committed by the book-keeper, the trial balance failed to balance by Sh.369.400. He placed the difference in a suspense account as shown below:

## Wanji trial balance as at 31 December 2001

| Fixed assets-cost | $\begin{array}{r} \text { Sh. } \\ 832,000 \end{array}$ | Sh. |
| :---: | :---: | :---: |
| Stocks |  |  |
| 1 January 2001 | 148.000 |  |
| 31 December 2001 |  | 98,800 |
| Trade debtors |  | 76,000 |
| Prepayments |  | 10,000 |
| Trade creditors | 34.600 |  |
| Bank overdraft |  | 15,200 |
| Accruals |  | 16,000 |
| Drawings | 359.600 |  |
| Capital |  | 1,054,000 |
| Sales | 1,043,200 |  |
| Provision for depreciation |  | 166,400 |
| Purchases |  | 733.000 |
| Operating expenses | 126.000 |  |
| Provision for doubtful debts |  | 3,800 |
| Discounts received | 5,000 |  |
| Discounts allowed |  | 5,800 |
| Suspense account |  | 369. 400 |
|  | 2,548 400 | 248400 |

Investigations carried out after preparing the above trial balance detected the following errors:

1. The total of the sales day book for December 2001 was overcast by Sh. 25,700 .
2. On 2 July 2001 the business purchased office equipment for Sh. 40 . 000 . These were debited to purchases account.
3. Depreciation on the equipment is at the rate of $10 \%$ per annum on cost and based on the period (months) of usage in the year.
4. A payment to a creditor by cheque of Sh. 8.500 was erroneously credited to the creditor's account.
5. A payment of Sh.4.500 for telephone expenses was debited to telephone account as Sh.5.400.
6. An amount of Sh. 15.000 received from a debtor was not posted to the debtor's account from the cash book.
7. An amount of discounts received of Sh. 2.500 was debited to discounts allowed account.
8. Purchases day book for October 2001 was undercast by Sh. 28,000 .
9. Assume the business had reported a net profit of $\mathrm{Sh} .85,800$ before adjusting for the above errors.

## Required:

(a) The adjusted trial balance and the correct balance of the suspense account (6 marks)
(b) Journal entries to correct the errors (Narrations not required)
(6 marks)
(c) Suspense account starting with the balance determined in the adjusted trial balance in (a)above.
(d) The adjusted net profit for the year.
(Total: 20 marks)

## QUESTION TWO

The following information has been extracted from the accounts of Madaraka Investments Ltd. for the year ended 31 December 2001. Comparable figures for the previous year are also shown.

Profit statement for the year ended 31 December 2001

|  | Sh. ${ }^{0} 000{ }^{\prime}$ | Sh'000' |
| :---: | :---: | :---: |
| Sales | 115,200 | 72.000 |
| Cost of goods sold | 70800 | 42,000 |
| Gross profit | 44,400 | 30,000 |
| Less: Trading expenses | 19800 | 16,200 |
|  | 24,600 | 13,800 |
| Less: Debenture interest | 900 | 900 |
| Net profit before taxation | 23,700 | 12,900 |
| Less: Corporation tax | 11520 | $\underline{5.760}$ |
| Net profit after taxation | 12.180 | 7.140 |
| Less: Ordinary share dividend | 6.300 | 4,500 |
| Undistributed profit for the year | 5,880 | 2,640 |


| Balance sheet as at 31 December |  |  |  |
| :---: | :---: | :---: | :---: |
| 2001 | 2000 |  |  |
| Sh. ${ }^{\prime} 000{ }^{\prime}$ | Sh. ${ }^{\prime} 000{ }^{\prime}$ | Sh. '000' | Sh. ${ }^{\prime} 000{ }^{\prime}$ |
| at | 44.400 |  | 33.600 |
| n | $\underline{9000}$ |  | 7,200 |
|  | 35,400 |  | 26,400 |

Current assets:

| Stock | 19,800 |  | 14,400 |  |
| :--- | ---: | ---: | ---: | ---: |
| Debtors | 12,600 |  | 9.000 |  |
| Cash | - | $\underline{32400}$ | $\underline{2,880}$ | $\underline{26,280}$ |
|  |  | $\mathbf{6 7 . 8 0 0}$ |  | 52.680 |


| Less: Current liabilities |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: |
| Creditors | 7,200 |  | 5.220 |  |
| Taxation | 11,520 |  | 5,760 |  |
| Proposed | 6,300 |  | 4,500 |  |
| dividends |  |  |  |  |
| Bank overdraft | 2,340 | 27,360 | - | 15.480 |
| Net assets |  | 40440 |  | 3 7,200 |
| Financed by: |  |  |  |  |
| Ordinary share capital |  |  |  |  |
| Authorised, issued and fully paid |  | 18,000 |  | 18,000 |
| (Sh. 25 per share) |  |  |  |  |
| Undistributed profits |  | 16080 |  | 10,200 |
|  |  | 34,080 |  | 28.200 |
| Long-tern loan: |  | 6360 |  | $\underline{9.000}$ |
| 10\% debentures (secured) |  | 40440 |  | 37200 |

## Required:

(a) Calculate six accounting ratios for both 2000 and 2001 that would help in assessing the profitability and liquidity positions of Madaraka Investments Ltd. (12 marks)
(b) Comment on Madaraka Investment's liquidity position.
(c) Comment on Madaraka Investment's profitability position.

## QUESTION THREE

Kyamba, Onyango and Wakil were partners in a manufacturing and retail business and shared profits and losses in the ratio 2:2:1 respectively.

Given below is the balance sheet of the partnership as at 31 March 2001:

Balance sheet as at 31 March 2001

Assets
Non-current assets:
Fixed assets 465,000
Current assets:
Stocks 294,000
Debtors
209,000
503,000
$\underline{968000}$

## Capital and liabilities:

Capital accounts:

| Kyamba | 160,000 |
| :--- | :--- |
| Onyango | 140,000 |
| Wakil | $\underline{200} 000$ |

## Current accounts:

| Kyamba | 65,300 |
| :--- | :--- |
| Onyango | 49.000 |
| Wakil | $\underline{53.000}$ |

167,300
667,300

## Current liabilities:

Bank overdraft 48,700
Trade creditors 252,000
300,700
$\underline{968000}$

## Additional information:

1. On 1 April 2001. Wakil retired from the partnership and was to start a business as a sole trader while Kyamba and Onyango continued in partnership.

On retirement of Wakil, the manufacturing business was transferred to hum while Kyamba and Onyango continued with the retail business.
2. The assets and liabilities transferred to Wakil were as follows:

|  | Net book value | Transfer value |
| :--- | ---: | ---: |
| Sixed assets | Sh. | Sh. |
| Stocks | 260,000 | 306,000 |
| Debtors | 166,000 | 157,000 |
| Creditors | 172,000 | 165,000 |
|  | 156,000 | 156,000 |

Wakil obtained a loan from a commercial bank and paid into the partnership the net amount due from him.

On retirement of Wakil from the partnership, goodwill was valued at Sh.200, 000 but was not to be maintained in the books of the partnership of Kyamba and Onyango.

After retirement of Wakil on 1 April 2001. Kyamba and Onyango agreed on the following terms and details of the new partnership:

- Kyamba and Onyango to introduce additional capital of Sh.48,000 and Sh.68,000 respectively.
- Each partner was entitled to interest on capital at $10 \%$ per annum with effect
from 1 April 2001 and the balance
of the profits was to be shared equally after allowing for annual salaries of Sh.72,000 to Kyamba and Sh.60,000 to Onyango.

5. The profit of the new partnership before interest on capitals and partners' salaries was Sh.240, 000 for the year ended 31 March 2002.
6. The profits made by the new partnership increased stocks by Sh.100.000; debtors by Sh. 90.000 and bank balance by Sh.50, 000 .
7. Drawings by the partners in the year were Kyamba Sh.85, 000 and OnyanSh go.70,000.

## Required:

(a) Profit and loss and appropriation account for the year ended 31 March 2002. (4 marks)
(b) Capital accounts for the year ended 31 March $2002 . \quad$ ( 4 marks)
(c) Current accounts for the year ended 31 March $2002 . \quad$ ( 8 marks)
(d) Balance sheet of the new partnership as at 31 March $2002 . \quad$ (4 marks)
(Total: 20 marks)

## QUESTION FOUR

(a) State the reasons for maintaining control accounts.
(b) The following information has been extracted from the books of Mutero Traders Limited for the month of April 2002.

Balances as at I April 2002:

|  | Sh. |
| :--- | ---: |
| Sales ledger - Debit balances | 838,000 |
| - Credit balances | 184,000 |
| Purchases ledger - Credit balances | 196.000 |
| 5 | 598.000 |
| Transactions during the month: | $8,784.000$ |
| Sales on credit | 7.849 .000 |
| Purchases on credit | 248,000 |
| Returns inwards | 179,000 |
| Returns outwards | 2.968 .000 |
| Cheques received from trade debtors | $4,674.000$ |
| Cash paid to trade creditors | 1.393 .000 |
| Cheques paid to trade creditors | 139.000 |
| Bad debts written-off | 162.000 |
| Discounts allowed to trade debtors | 231.000 |
| Discounts received from trade creditors | 356.000 |
| Credit sales off-set against credit purchases | 598.000 |
| Credit purchase of a motor vehicle posted in the purchases ledger | 193,000 |
| Dishonoured cheques from trade debtors | 106.000 |
| Cash received to replace dishonoured cheques from trade debtor | 147.000 |
| An invoice to trade debtors of Sh.174,000 posted as |  |

## Balances as at 30 April 2002:

Sales ledger credit balances 123.000
Purchases ledger debit balances 177,000

## Required:

The sales ledger and purchases ledger control accounts for the month ended 30 April 2002.
(16 marks)
(Total: 20 marks)

## QUESTION FIVE

(a) Distinguish between each of the following pairs of terms:
(i) Receipts and revenue.
(ii) Balance sheet and statement of affairs.
(iii) Cash basis of accounting and accrual basis of accounting.
(iv)Materiality and substance over form.
(b) What conflicts may exist in the application of the fundamental accounting concepts? (4 marks)
(Total: 20 marks)

## DECEMBER 2010

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

## QUESTION ONE

On 1 October 2001, Mr. Robert Kanyarna bought Premium Meat Suppliers Ltd., a business dealing in meat products, for a cash price of Sh.8, 000,000. He took over the following assets and liabilities of the company:

|  | Sh. |
| :--- | ---: |
| Buildings 2\% | $\mathbf{0 0 0 0}^{\prime}$ |
| Plant and equipment | $10 \%$ |
| Debtors | 6,000 |
| Stock of meat | 1,400 |
| Creditors (for purchases) | 800 |
|  |  |

Mr. Kanyama immediately opened a business bank account in which he deposited as working capital, Sh.1, 600,000 from himself and Sh.4,000,000 being a long - term loan from J.K. Bank Ltd. The loan from the bank carried an interest rate of $10 \%$ per year.
During the year ended 30 September 2002, Mr. Kanyama did not keep a full set of double entry accounting records but relied heavily on close and personal involvement in the business to ensure proper control and safekeeping of assets of the business. In addition, daily cash summaries were prepared and counterfoil cheque stubs and bank statements reconciled. The following information relates to transactions in the year ended 30 September 2002:

1. Before banking proceeds from sales and debtors, payments were made out of cash as summarised below:

Sh.
`000'
Stock purchase 19,456
Slaughter charges 1,008
Sundry expenses $\quad 1,744$
Electricity charges 304
Wages expense 328
2. A summary of cheques counterfoil stubs disclosed the following payments through the bank:

|  | Sh. |
| :--- | ---: |
|  | $\mathbf{0 0 0}$ |
| Stock purchases | 22,608 |
| Shop wages | 1,728 |
| Personal drawings | 2,096 |
| Rates and licences | 1,560 |
| Interest on loan | 200 |

3. Mr. Kanyama had, each week, made deposits into his business bank account all cash on hand after payments in (I) above) except a till float of Sh.40,000 maintained throughout the year. An examination of the pay-in slips and bank statements revealed total deposits of Sh32,280,00Q2 exclusive of capital and loan) during the year.
4. At 30 September 2002, Mr. Kanyama was owed Sh.592, 000 by debtors and owed Sh1,720,000 to trade creditors. Wages outstanding at that date amounted to Sh. $270,0 \mathrm{O} 0$. The stock at 30 September 2002 was valued at cost at Sh. 1, 160,000. The only cash on hand at the year-end was in the till float.
5. Mr. Kanyama consulted with Chania Accountants and has accepted their advice to make a provision of $2 \%$ per annum for depreciation on buildings and $10^{\circ} \%$ per annum for depreciation on plant and equipment. Mr. Kanyama also considers it prudent to provide for the fact that $1 \%$ of the debtors outstanding at the year end will not honour their obligations.

## Required:

(a) Bank and cash accounts for the year ended 30 September2002.
(b) Trading, profit and loss account for the year ended 30 September2002. (8 marks)
(c) Balance sheet as at 30 September 2002.
(Total: 20 marks)

## QUESTION TWO

The Swara Sports Club had the following assets and liabilities as at 30 September 2002:

$$
\text { Sh. }{ }^{\prime} 000 \quad \text { Sh. }{ }^{\prime} 000^{\prime}
$$

## Assets

| Clubhouse (at cost) | 16,800 |  |
| :--- | ---: | ---: |
| Equipment Cost | 4,600 |  |
| $\quad$ Accumulated depreciation | $\underline{2,200}$ | 2,400 |
| Bar stock |  | 800 |
| Rates prepaid | 200 |  |
| Insurance prepaid | 70 |  |
| Subscriptions in arrears (one year"s) | 32 |  |
| Cash at bank | 1,960 |  |
| Cash in hand | 20 |  |

## Liabilities

Creditors for bar purchases 1,600
Subscriptions in advance (one year"s) 16
Electricity account owing $\quad 60$

The treasurer of the club, Mr. Lutomia is in process of drawing up the financial forecast of the club for the coming year, ending on $30^{\text {th }}$ September2003.
He wishes to prepare a forecast income and expenditure account for the year and a balance sheet as at that date.

The following information has been collected to assist in the forecast:

1. The club has 300 members and it is intended to raise the subscriptions per member from the current Sh. 8,000 to Sh. 10,000 per year. The members who have paid in advance will be allowed subscriptions at the old rates. It is anticipated that the members currently in arrears with their subscriptions will pay the arrears during the coming year. It is also anticipated that the number of members whose subscriptions would be in arrears and those who would have paid in advance on 30 September 2003 would be the same as the corresponding numbers on 30 September 2002.
2. Extensions to the clubhouse are planned which will cost an estimated amount of Sh. $3,000,000$. Of this sum, it is anticipated that $\mathrm{Sh} .2,000,000$ will be paid during the year.
3. Some of the club's sports equipment which cost Sh. 500,000 and has a written value of Sh.200,000 will be sold for u estimated value of Sh. 100,000 and replaced by new equipment costing Sh.680,000. All equipment is depreciated on a straight-line basis over four years and none of the equipment is more than three years old. A full year's provision is charged in the year of acquisition and none in the year of disposal.
4. Bar purchases are made monthly on credit and paid for in the month following purchase. It is anticipated that the same volume of business, which is fairly constant on a monthly basis, will be realised during the coming year but that stock costs will rise by $25 \%$ from 1 October 2002. Bar stocks are normally held at the level of one half of one month's purchases. The bar makes a gross profit margin of $20 \%$ on all sales regardless of stock costs. Bar sales are on cash, all of which is banked daily. The barman, who is paid Sh. 20,000 per month, receives a commission of $5 \%$ of the gross profit for the year. This is paid with his final wage cheque by the year end.
5. The club runs monthly social evenings and charges members Sh.2, 000 per head admission. An average of 200 members attend each of these evenings. Expenses usually amount to Sh. 1,400 per head.
6. The following expenditure payments are expected to be made by the club during the coming year:

|  | Sh |
| :--- | ---: |
| Rates | $1,000,000$ |
| Insurance | 160,000 |
| Salary of Club manager | $1,200,000$ |
| Salary of club grounds man | 960,000 |
| Bar annual licence | 100,000 |
| Electricity | 500,000 |
| Miscellaneous | 140,000 |

The rates are paid on 1 January in respect of the following twelve months. The insurance payment will be for the Period 1 April 2003 to 31 March 2004. One-fifth of electricity consumption is in respect of the bar. All payments are made by cheque.

## Required:

(a) Forecast bank account for the year ending 30 September 2003.
(b) Forecast bar. Trading, profit and loss account for the year ending 30 September 2003
(4marks)
(c) Forecast income and expenditure account for the year ending 30 September 2003.
(8marks)
(d) Balance sheet as at 30 September 2003.
(Total: 25 marks)

## QUESTION THREE

(a) Explain the legal provisions regarding the establishment and subsequent use of the following reserves:
(i) Share premium account.
(4marks)
(ii) Capital redemption reserve fund.
(4marks)
(b) Masaba Company Ltd. is a retail provider with an authorised share capital of 800,000 Sh. 20 ordinary shares and $250,0008 \%$ Sh. 20 redeemable preference shares.

The following financial information reflects the position of the company as at 31 December 2001 after preparing the Trading, profit and loss account:

|  | $\begin{gathered} \text { Sh. } \\ \end{gathered}$ |
| :---: | :---: |
| Provision for depreciation Fittings | 1,500, |
| Motor vehicles | 3,740 |
| Goodwill | 1,200 |
| Issued share capital: 600,000 Sh. 20 Ordinary shares | 12,000 |
| 250,000 Sh. 20 Redeemable preference shares | 5,000 |
| Share premium account | 400 |
| Trade debtors and prepayments | 1,708 |
| Land and buildings at valuation (Cost Sh. $4,400,000$ ) | 18,400 |
| Capital redemption reserve fund | 3,000 |
| Fittings at cost | 3,000 |
| Motor vehicles at cost | 7,940 |
| 10\%\% Debentures | 1,600 |
| Trade creditors and accruals | 960 |
| Short-term investments (Market value Sh.860,000) | 780 |
| Stock at 31 December 2001 | 2,960 |
| Bank overdraft | 540 |
| Revaluation reserve | 1,000 |
| Net profit for the year | 1,440 |
| Retained profit at 1 January 2001 | 4,460 |
| General Reserve | 1,100 |
| Provision for doubtful debts | 48 |
| Interim dividend paid - Ordinary | 600 |
| - Preference | 200 |

The following resolutions relating to year ended 31 December 2001 have been passed by the board of directors of the company

1. Transfer Sh.500,000 to General Reserve.
2. Provide for $5 \%$ final dividend and final preference dividend on shares issued and outstanding on 31 December 2001.
3. Make a bonus issue of 100,000 fully paid ordinary shares from the retained profits account.

## Required:

(i) The appropriations account of Masaba Company Ltd. for the year ended 31 December 2001.
(ii) The balance sheet of Masaba Company Ltd. as at 31 December 2001. (8 marks)
(Total: 20 marks)

## QUESTION FOUR

Denticare Limited makes its accounts on 30 June every year.
On 1 July 2001, the company's balance sheet included the following figures for non -current assets:

| Cost | Accumulated <br> Depreciation |  |
| :--- | ---: | ---: |
|  | Sh. | $\mathbf{S h .}$ |
| Land | , $\mathbf{0 0 0}$ | , $\mathbf{0 0 0}$ |
| Buildings | 40,000 | Nil |
| Plant and machinery | 22,000 | 8,000 |
| Motor vehicles | 16,000 | 6,000 |
| n | 6,000 | 2,000 |

The company's policy is to charge depreciation at the following rates:

|  | Rate |
| :--- | :--- |
| Land | Nil |
| Buildings | $2 \%$ on cost |
| Plant and machinery | $15 \%$ on cost |
| Motor vehicles | $20 \%$ on cost |

A proportionate charge is made in the year of purchase, sale or revaluation of an asset.
During the year ended 30 June 2002, the following transactions took place:

1. On 1 January 2002 the company decided to adopt a policy of revaluing its buildings. A professional valuer engaged for this purpose revalued the buildings at Sh. 34 million.
2. On 1 Janua ry a plant that had cost Sh. 3 million was sold for Sh.500, 000. Accumulated depreciation on this plant on 30 June2001 amounted to Sh.2.3 million. A new plant was then purchased at a cost of Sh. 4 million.
3. On 1 April 2002 a new motor vehicle was purchased for Sh.300, 000 Part of the purchase price was settled by exchanging another motor vehicle at an agreed value of sh.120, 000 The balance of Sh.180,000 was paid in cash. The vehicle which was given in part exchange had cost Sh.200, 000 and had a net book value of Sh.100, 000 as at 30 June 2001

## Required:

(a) The following ledge accounts to record the above transactions:
(i) Buildings account.
(ii) Provision for depreciation: Buildings.
(iii) Plant and machinery account.
(iv) Provision for depreciation: Plant and Machinery.
(v) Motor vehicles account.
(vi) Provision for depreciation: Motor vehicles. (9 marks)
(b) Property, plant and equipment movement schedule for the year ended 30 June 2002. (6
marks)
(Total: 15 marks)

## QUESTION FIVE

Write short notes to distinguish the following:
(a) Purchased goodwill and non-purchased goodwill. (5marks)
(b) Amortisation and depreciation of fixed assets
(5marks)
(c) Provisions and reserves.
(d) Compensating errors and errors of principle

## FINANCIAL ACCOUNTING 1

MAY 2011.
Time Allowed: 3 hours.

## QUESTION ONE

The following balances have been extracted from the books of Limuru Manufacturers, a small scale manufacturing enterprise, as at 31 December 2002:

|  |  | $\begin{array}{r} \text { Sh. } \\ , 000^{" \prime} \end{array}$ |
| :---: | :---: | :---: |
| Stocks as at 1 January 2002: | Raw materials | 7,000 |
|  | Work in progress | 5,000 |
|  | Finished goods | 6,900 |
| Purchases of raw materials |  | 38,000 |
| Direct labour |  | 28,000 |
| Factory overheads: | Variable | 16,000 |
|  | Fixed | 9,000 |
| Administrative expenses: | Rent and rates | 19,000 |
|  | Lighting | 6,000 |
|  | Stationery and postage | 2,000 |
|  | Staff salaries | 19,380 |
| Sales |  | 192,000 |
| Plant and machinery: | At cost | 30,000 |
|  | Provision for depreciation | 12,000 |
| Motor vehicles (for sales deliveries): | At cost | 16,000 |
|  | Provision for depreciation | 4,000 |
| Creditors |  | 5,500 |
| Debtors |  | 28,000 |
| Drawings |  | 11,500 |
| Balance at bank |  | 16,600 |
| Capital at 1 January 2002 |  | 48,000 |
| Provision for unrealized profit at 1 January 2002 |  | 1,380 |
| Motor Vehicle running costs |  | 4,500 |

## Additional information:

1. Stocks at 31 December 2002 were as follows:

|  | Sh. |
| :--- | ---: |
| Raw materials | , $\mathbf{0 0 0}$ |
| Work in progress | 9,000 |
| Finished goods | 8,000 |
|  | 10,350 |

2. The factory output is transferred to the trading account at factory cost plus $25 \%$ of factory profit.
3. Depreciation is provided at the rates shown below on the original cost of fixed assets held at the end of each financial year.
Plant and machinery - $10 \%$ per annum
Motor vehicles - 25\% per annum
4. Amounts accrued at 31 December 2002 for direct labour amounted to Sh. 3,000,000 and rent and rates prepaid at 31 December 2002 amounted to Sh. 2,000,000.

## Required:

(a) Manufacturing, trading and profit and loss account for the year ended 31 December 2002.
(b) Balance sheet as at 31 December 2002.

## QUESTION TWO

(a) Differentiate between a petty cashbook and a three-column cashbook. (5 marks)
(b) Briefly explain why it is important for a business entity to prepare a bank reconciliation statement.
(3 marks)
(c) You have recently been employed in a medium size company and deployed in the accounts department. Your head of section has given you the following extract from the cashbook for the month of April 2003:

| Sh. |  |  | Sh. |
| :---: | :---: | :---: | :---: |
| Receipts during the month | 2,938,000 | Balance brought forward (1.4.2003) | 1,522,000 |
| Balance carried forward (30.4.2003) | 1,108,000 | Payments during the month | 2,524,000 |
|  | 4,046,000 |  | 4,046,000 |

The head of section further informs you that all receipts are banked intact and all payments are made by cheque. On investigation, you discover the following:

1. Bank charges and commissions amounting to Sh. 272,000 entered on the bank statement had not been entered in the cashbook.
2. Cheques drawn amounting to Sh. 534,000 had not been presented to the bank for payment.
3. Cheques received totaling Sh. 1,524,000 had been entered in the cashbook and paid into the bank, but had not been credited by the bank until May 2003.
4. A cheque for Sh. 44,000 had been entered as a receipt in the cashbook instead of a payment.
5. A cheque for Sh. 50,000 had been debited by the bank by mistake.
6. A cheque received for $\mathrm{Sh} .160,000$ had been returned unpaid. No adjustment had been made in the cashbook.
7. All dividends receivable are credited direct to the bank account. During the month of April 2003. Dividends totaling Sh. 124,000 were credited by the bank and no entries had been made in the cashbook.
8. A cheque drawn for Sh. 12,000 had been incorrectly entered in the cash book as Sh. 132,000.
9. The balance brought forward should have been Sh. 1,422,000.
10. The bank statement as at 30 April 2003 showed on overdraft of Sh. 2,324,000.

## Required:

(i) The adjusted cashbook as at 30 April $2003 . \quad$ (6 marks)
(ii) Bank reconciliation statement as at 30 April 2003. (6 marks)
(Total: 20 marks)

## QUESTION THREE

The following balances remained in the books of Ahadi Ltd. as at 30 April 2003 after the preparation of the trading account:

Share capital, authorized and issued:
Sh.

> 2,400,000 Sh. 20 ordinary shares
> $800,0008 \%$ Sh. 20 preference shares

Stock - 30 April 2003
48,000,000
16,000,000
Accounts receivable and prepayments
33,540,000
Accounts payable and accruals
10,880,000
5,488,800
Balance at bank 3,118,400
$10 \%$ debentures 6,400,000
General reserve 11,200,000
Bad debts 136,000
Gross profit for the year 32,603,200
Salaries and wages 11,280,000
Rates and insurance 564,000
Postage and telephone 248,000
Water and electricity 486,400
Debenture interest 320,000
Directors" fees 1,000,000
General expenses 1,243,200
Motor vehicles (Cost Sh. 11,640,000) 2,720,000
Office fittings and equipment (Cost Sh. 17,856,000) 10,976,000
Land and buildings at cost 52,880,000
Profit and loss account - 1 May $2002 \quad 9,700,800$

## Additional information:

1. A bill for Sh. 219,200 in respect of electricity for the period up to 30 April 2003 has not been accrued.
2. The amount for insurance includes a premium of Sh. 120,000 paid in January 2003 to cover the company for six months, February to July, 2003.
3. Office fittings and equipment are to be depreciated at $15 \%$ per annum on cost and motor vehicles at $20 \%$ per annum on cost.
4. Provision is to be made for:

Directors" fees - Sh. 2,000,000
Audit fee - Sh. 480,000
The outstanding debenture interest.
5. The directors have recommended that:

- A sum of Sh. 4,800,000 be transferred to general reserve.
- The preference dividend be paid.
- A $10 \%$ ordinary dividend be paid.


## Required:

(a) Profit and loss and appropriation accounts for the year ended 30 April 2003. (10 marks)
(b) Balance sheet as at 30 April 2003.
(Total: 20 marks)

## QUESTION FOUR

Munyaka and Opiyo commenced trading on 1 May 2002 as wholesalers, sharing profits and losses in the ration $2: 1$, after allowing interest on the capital introduced by the partners at the rate of $10 \%$ per annum. Opiyo was to receive a salary of Sh. 440,000 per annum. Munyaka and Opiyo do not operate a complete set of accounting records.

The following summary of the bank statements for the year ended 30 April 2003 has been
provided:

Receipts: Cash introduced as capital on 1 May 2002: Munyaka Sh. 3,500,000 and Opiyo Sh. 2,000,000. Balance of receipts from customers amounted to Sh. 12,700,000.

Payments: Equipment Sh. 2,500,000: Pick-up Sh. 1,000,000: furniture and fittings Sh. 375,000: go-down rental Sh. 375,000, wages Sh. 1,772,000; salary of Sales Manager Sh. 1,200,000; purchases for resale Sh. 9,900,000; rates Sh. 200,000; repairs Sh. 62,500; insurance Sh. 55,000; motor expenses Sh. 186,500.

The following cash payments were made before banking the balance of the takings; Motor expenses Sh. 129,000, wages Sh. 148,000; Sundry expenses Sh. 25,000; Drawings - Munyaka Sh. 7,500 per week and Opiyo Sh. 6,000 per week.

## Additional information:

1. The partners had taken goods for their domestic use as follows: Munyaka Sh. 50,000; Opiyo Sh. 75,000 (both at selling price).
2. During the year to 30 April 2003, discounts allowed to customers amounted to Sh. 122,500 while discounts received from suppliers amounted to Sh. 55,000.
3. At 30 April 2003, l the amounts owing to suppliers amounted to Sh. 750,000 and the amount owing by customers was Sh. 1,550,000. An amount of Sh. 200,000 owing by a customer proved irrecoverable and was treated as a bad debt.
4. As at 30 April 2003, rates and insureance were prepaid to the extent of Sh. 25,000 and Sh. 5,000 respectively. Stock on hand at cost amounted to Sh. 1,205,000.
5. The go-down had been occupied since 1 May 2002 at an annual rental of Sh. 500,000.
6. Depreciation is to be provided on a straight-line basis as follows: Motor vehicles $20 \%$ per amount: Equipment, furniture and fittings at the rate of $10 \%$ per annum.

## Required:

(a) Trading, profit and loss and appropriation accounts for the year ended 30 April 2003.
(b) Balance sheet as at 30 April 2003.
(12 marks)
(8 marks)
(Assume a 52 - week year)
(Total: 20 marks)

## QUESTION FIVE

(a) What is an "accounting policy"?
(2 marks)
(b) Briefly explain three circumstances under which "goodwill" can be recorded in a business firm"s books of account.
(9 marks)
(c) The following categories of people are recognized as users of the information contained in financial statements:

- Owners.
- Financial analysts
- Lenders.

For each of the above users of financial statements, identify the kind of information they may require, why they require it and the decisions they make from that information.
(9 marks)
(Total: 20 marks)

## DECEMBER 2011

## QUESTION ONE

Muthusi is a businessman operating a retail business in a small town. Due to the size of his business, he is not able to employ a qualified accountant on a permanent basis.

The following information was extracted from the books of the business as at 31 October 2002:

|  | Shs. |
| :--- | ---: |
| Freehold property (cost) | 600,000 |
| Motor vehicles (NBV) | 750,000 |
| Furniture and fixtures (NBV) | 240,000 |
| Stock | 390,000 |
| Trade debtors | 500,000 |
| Bank overdraft | 60,000 |
| Trade creditors | 380,000 |
| Accruals | 15,000 |
| $10 \%$ loan | 600,000 |
| Provision for doubtful debts | 25,000 |

The following transactions took place during the financial year ended 31 October 2003:

1. Sales and purchases on credit amounted to Sh.2,080,000 and Sh.1,900,000 respectively.
2. The following transactions were carried out through the bank account:

## Shs.

Sales - Cash
Purchases - Cash
Payments to trade creditors
Purchase of furniture 200,000
Salaries and wages 160,000
Lighting 65,000
General expenses 35,000
Interest on loan 30,000
Drawings 60,000
Repayment of loan on 30 April 2003
Collections from trade debtors 1,890,000
Proceeds from sale of motor vehicle 120,000

720,000
240,000
1,940,000

100,000
3. The business depreciates motor vehicles at $20 \%$ per annum on a reducing balance basis. A full year"s depreciation is provided on a motor vehicle acquired in the course of the year and no depreciation is provided on a motor vehicle disposed of in the course of the year.

The motor vehicle sold in the year had been purchased at Sh.250,000 and an accumulated depreciation of Sh. 122,000 had been provided on it at the time of disposal.
4. Furniture is depreciated at $10 \%$ per annum on cost and in proportion to the period used in the year. The additional furniture was purchased on 1 May 20903 while the cost of furniture held on 31 October 2002 was Sh. 400,000
5. Loan interest paid was for one-half year up to 30 April 2003
6. The business received discounts of Sh. 40,000 and allowed discounts of Sh.70,000 during the year.
7. Bad debts of Sh. 20,000 were written off. Provision for doubtful debts is to be maintained at $5 \%$ of the debtor"s balance at the end of the year.
8. Accruals are in respect of lighting and on 31 October 2003, the amount accrued was Sh.19,000
9. Muthusi"s business obtains a normal gross profit rate of $25 \%$ on selling price.

## Required:

(a) Trading and profit and loss account for the year ended 31 October 2003 (12 marks)
(b) Balance sheet as at 31 October 2003.
(8 marks)
(Total: 20 marks)

## QUESTION TWO

The following are the summarized financial statements of Deweto limited:
Trading and profit and loss account for the year ended 31 October.

|  | $\mathbf{2 0 0 2}$ | $\mathbf{2 0 0 3}$ |
| :--- | ---: | ---: |
| Sales | Sh."000 | Sh."000 |
| Cost of sales | 93,500 | 11,350 |
| Gross profit | $(55,120)$ | $(72,970)$ |
| Expenses | 38,380 | 38,380 |
| Net profit before interest and tax | $(\mathbf{2 6 , 2 3 0 )}$ | $\underline{(23,960)}$ |
| Loan interest | 12,150 | 14,420 |
| Net profit before tax | $\underline{(450)}$ | $\underline{(375)}$ |
| Taxation | 11,700 | 14,045 |
| Net profit after tax | $\underline{(3,510)}$ | $(\underline{5,413.5)}$ |
| Dividend | $\underline{(6,00)}$ | $8,631.5$ |
| Retained profit | $\underline{(6,000)}$ |  |

Balance sheet as at 31 October

## Fixed assets:

Freehold premises
Plant and equipment
Motor vehicles
Current assets:
Stock
Debtors
Bank balance and cash in hand

## Current liabilities:

Creditors
Taxation
Dividend
Ordinary share capital
Reserves
$15 \%$ loan

| 2002 |  | 2003 |  |
| ---: | ---: | ---: | ---: |
| Sh." $\mathbf{0 0 0}$ | Sh."000 | Sh. "000 | Sh."000 |
| 10,500 |  | 10,500 |  |
| 7,200 |  | 9,500 |  |
| 5,350 | 23,050 | 7,300 | 27,300 |
| 12,500 |  | 11,800 |  |
| 9,850 |  | 8,900 |  |
| 5,950 | 28,300 | $\underline{5,864.5}$ | $26,564.5$ |
| 8,350 |  | 7,830 |  |
| 3,510 |  | $5,413.5$ |  |
| $\underline{3,000}$ | $\underline{14,860)}$ | $\underline{3,000}$ | $\underline{(16,243.5)}$ |
|  | $\underline{36,490}$ |  | $\underline{37,621}$ |
|  | 30,000 |  | 30,000 |
|  | $\underline{3,490}$ |  | $\underline{5,121}$ |
|  | 33,490 |  | 35,121 |
|  | $\underline{3,000}$ |  | $\underline{2,500}$ |
|  | $\underline{36,490}$ |  | $\underline{37,621}$ |

Note:

1. $80 \%$ of the sales are no credit
2. The stock as at 31 October 2001 was valued at Sh. 13,000,000

## Required:

(a) Calculate two ratios for each classification identified below for the financial years ended 31 October 2002 and 2003:
(i) Profitability ratios (4 marks)
(ii) Liquidity ratios (4 marks)
(iii) Gearing ratios (4 marks)
(iv) Activity ratios
(b) Comment on Deweto Ltd"s profitability and liquidity positions.

## QUESTION THREE

The following version of the receipts and payments account has been provided by the treasurer of Maendeleo Social club for the year ended 31 October 2003:

|  | Receipts <br> Shs. " 000 | Payments Shs." 000 |
| :---: | :---: | :---: |
| Opening Balance | 500 |  |
| Accountancy Fees |  | 200 |
| Bar Purchases |  | 24,000 |
| Bar sales | 55,000 |  |
| Dances: Expenses |  | 900 |
| Ticket Sales | 1,600 |  |
| Foods: Purchases |  | 4,500 |
| Sales | 8,000 |  |
| Insurance |  | 500 |
| Electricity |  | 1,500 |
| Members Subscriptions | 35,000 |  |
| Office Expenses |  | 22,000 |
| Purchase of Furniture |  | 4,000 |
| Rates |  | 2,000 |
| Salaries and Wages: Bar Staff |  | 10,000 |
| Other Staff |  | 14,000 |
| Telephone |  | 3,000 |
| Travelling Expenses |  | 13,000 |
| Balance c/f |  | $\underline{500}$ |
|  | 100,100, | 100,100 |
| Additional Information: | Shs. 000 | Shs. 000 |
| 1. Fixed Assets: At November 2002 |  |  |
| Club Premises at Cost |  | 18,000 |
| Furniture and Fittings at Cost | 35,000 |  |
| Less Provision for depreciation | 14,000 | 21,000 |
|  |  | 39,000 |

2. Accruals and Sundry Creditors

| At Nov 2002 | At 31 Oct |
| :---: | :---: |
| Shs. 000 | Shs. 000 |
| 200 | 250 |
| 1,500 | 2,000 |
| 400 | 300 |
| 1,000 | 800 |
| 600 | 700 |
|  |  |
| 300 | 200 |
| 6,000 | 7,000 |

4. Maendeleo Social Club had a Bank Account, which had a balance of Shs. 2,500,000 on 1 Nov 2002. This Bank account was not used during the year to 31 Oct 2003and the only entry made in this account was for the interest of shs. 200,000 which was credited yo the bank on 31 Oct 2003.
5. Depreciation on Furniture and fittings is at the rate of $10 \%$ per annum on cost. A full years depreciation is provided for any furniture bought during the year.
6. Bar stock was valued at shs. 7,000,000 0n 1 Nov 2002 and at Shs. 1,500,000 on 31 Oct 2003.
7. No Apportionment of costs is made between bar activities and other club activities.

## Required:

i. Income and Expenditure Account for the year 31 Oct 2003.
ii. Balance Sheet

## QUESTION FOUR

Meza Ltd has an authorized share capital of Sh.20,000,000 divided into 1,500,000 ordinary shares of Sh. 10 each and $250,0008 \%$ preference shares of Sh. 20 each.

An extract of the balance sheet as at 30 June 2003 was as follows:

## Sh."000

Sh."000
Fixed assets

| Current assets |  |
| :--- | ---: |
| Stock | 2,300 |
| Debtors | 980 |
| Bank balance | $\underline{530}$ |
|  | 3,810 |
| Creditors | $\underline{(550)}$ |

7,040 Equity 500,000 ordinary shares of Sh. 10 par value 5,000 250,000 $8 \%$ preference shares of Sh .20 par value Share premium
3,260
10,300 $\quad \underline{10,300}$

On 1 July 2003, the company offered 500,000 ordinary shares for sale to the public at Sh. 15 each payable as follows:

- On application Sh. 7 including the premium
- On allotment Sh. 5
- On first and final call, Sh. 3

Applications were received on 15 July 2003 and allotment made on 31 July 2003. The allotment money was received on 15 August 2003.

The first and final call was made on 15 September 2003 and the money received on 30 September 2003.

The company received applications for 650,000 shares. Applications for 25,000 shares were rejected and the application money was refunded. The shares were then allocated to the remaining applicants on a pro rata basis, the excess of the application money being carried forward in part satisfaction of the amounts due on allotment.

An allotee of 3,000 shares failed to pay both the allotment and first and final call money and the shares were forfeited on 13 October 2003.

The forfeited shares were then re-issued at Sh. 12 each on 21 October 2003.

## Required:

(a) Ledger accounts to record the above transactions
(b) Balance sheet as at 21 October 2003
(6 marks)
(Total: 20 marks)

## QUESTION FIVE

(a) Briefly explain the meaning of each of the following accounting concepts, giving in each case, an example of the application of each:
(i) Materiality (4 marks)
(ii) Substance over form
(4 marks)
(iii) Money measurement
(b) Briefly explain whether revenue may be recognized in the following circumstances in respect of sales made by a business entity:
(i) Goods have acquired by the business entity which it confidently expects to resell very quickly
(ii) A customer places a firm order for goods
(iii) Goods are delivered to the customer"s premises
(iv) The customer"s cheque in payment for the goods has been cleared by the bank.
(2 marks)
(Total: 20 marks)

## JUNE 2012

## QUESTION ONE

Mali Mingi is the sole distribution agent of roofing sheets in Mombasa. Under an agreement with the manufacturers, Mabati Ltd., Mali Mingi purchases roofing sheets from Mabati Ltd. at a trade discount of $20 \%$ of the list price. Every year in the month of May, Mali Mingi receives an agency commission of $1 \%$ of his purchases for previous year ended 31 March.

Mali Mingi has been making a gross profit of $40 \%$ on all sales. In a burglary that occurred in January 2004, Mali Mingi lost stock costing Sh.480,000 as well as the bulk of his accounting records.

After thorough investigation, the accountant has obtained the following information relating to the year ended 31 March 2004:

1. Assets and liabilities as at 31 March 2003 were:

|  | Sh. |
| :--- | ---: |
| Buildings at cost | $1,200,000$ |
| Provision for depreciation on buildings | 720,000 |
| Motor vehicles at cost | 600,000 |
| Provision for depreciation on motor vehicles | 240,000 |
| Stock at cost | 384,000 |
| Trade debtors (sales) | 756,000 |
| Prepayment (Trade expenses) | 14,400 |
| Agency commission receivable | 36,000 |
| Balance at bank and cash in hand | 517,200 |
| Trade creditors | 504,000 |
| Accrued motor vehicle expenses | 27,600 |

2. Mali Mingi has been notified that he will receive an agency commission of SH. 52,800 on 1 May 2004. Commissions are paid directly to the bank.
3. Stock, at cost, at 31 March 2004 was valued at Sh. 360,000 more than the value as at 31 March 2003. In October 2003, stock worth Sh. 120,000 was scrapped as worthless.
4. Other details relating to the period up to 31 March 2004 are as follows:

|  | Sh. |
| :--- | ---: |
| Discounts allowed | 194,400 |
| Discounts received | 144,000 |
| Prepaid trade expenses | 9,600 |
| Motor vehicle expenses | 842,400 |

5. Balances as at 31 March 2004:

|  | Sh. |
| :--- | ---: |
| Trade creditors at list prices | $1,140,000$ |
| Trade debtors | 804,000 |

6. Depreciation is provided at the following rates:

Buildings - 5\% per annum on cost Motor
vehicles - $20 \%$ per annum on cost
7. In addition to purchases, the following payments were made through the bank:

|  | Sh. |
| :--- | ---: |
| Motor vehicle expenses | 806,400 |
| Drawings | 516,000 |
| Trade expenses | 883,200 |

8. All receipts pass through the bank and Mali Mingi is not insured against burglary.
9. The agency commission due as at 31 March 2003, was received during the year through the bank.
10. All purchases and sales are on credit.

## Required:

(a) Trading and profit and loss accounts for the year ended 31 March 2004.
(10 marks)
(b) Balance sheet as at 31 March 2004.
(Total: 20 marks)

## QUESTION TWO

J Kiarie carries on a manufacturing business in Eldoret. The trial balance extracted from his books as at 31 March 2004 was as follows:

|  | Sh. "000 | Sh. ${ }^{\text {"000 }}$ |
| :---: | :---: | :---: |
| Stock at 1 April 2003: |  |  |
| Raw materials | 16,200 |  |
| Finished goods | 58,000 |  |
| Purchases of raw materials | 409,600 |  |
| Manufacturing wages | 92,200 |  |
| Rent, rates and insurance | 15,400 |  |
| Salaries | 102,400 |  |
| Discounts allowed | 4,000 |  |
| Carriage inwards | 7,600 |  |
| General expenses | 53,800 |  |
| Professional charges | 6,400 |  |
| Carriage outwards | 9,400 |  |
| Motor vehicles at cost | 24,400 |  |
| Plant and machinery at cost | 96,000 |  |
| Leasehold premises (acquired on 1 April 2003) | 140,000 |  |
| Capital as at 1 April 2003 |  | 200,000 |
| Sales |  | 841,600 |
| Discounts received |  | 5,000 |
| Provision for doubtful debts (1 April 2003) |  | 10,000 |
| Sundry creditors |  | 59,000 |
| Provision for depreciation (1 April 2003): |  |  |
| Plant and machinery |  | 26,800 |
| Motor vehicles |  | 11,600 |
| Sundry debtors | 79,000 |  |
| Bank balance | 39,600 |  |
|  | 1,154,000 | 1,154,000 |

## Additional information:

1. Sales included $S h .46,000,000$ in respect of goods charged out to customers at cost plus $25 \%$ on a sale or return basis. The goods remained unsold as at 31 March 2004.
2. The stock of finished goods and raw materials at cost as at 31 March 2004 amounted to Sh.63,600,000 and Sh.15,800,000 respectively.
3. Prepaid insurance as at 31 March 2004 was Sh. 400,000 and Sh. $1,000,000$ was owing for lighting and heating as at the same date. Lighting and heating is accounted for through the general expense account.
4. Included in the salaries account were drawings by J.Kiarie amounting to Sh. 400,000 per week. (Assume a 52 - week year)
5. A debt of Sh. $1,000,000$ is to be written off and provision for doubtful debts is to be reduced to Sh. $8,000,000$
6. During the year, motor vehicles which had cost Sh. 12,000,000 and which had been written down to Sh. $4,000,000$ were sold for Sh.9,600,000. This amount has been credited to motor vehicles account.
7. Legal fees amounting to $\mathrm{Sh} \cdot 2,800,000$ in respect of acquisition of the leasehold premises are included in the professional charges account. The lease costs are to be amortised over 20 years.
8. Provision for depreciation on motor vehicles and plant and machinery is to be made at Sh.3,800,000 and Sh.5,000,000 respectively.

## Required:

(a) Manufacturing, trading and profit and loss accounts for the year ended 31 March 2004.
(10 marks)
(b) Balance sheet as at 31 March 2004. (10 marks) (Total: 20 marks)

## QUESTION THREE

(a) Briefly explain the following types of errors:

| (i) Error of commission | $(2 \mathrm{marks})$ |
| :--- | :--- |
| (ii) Error of principle | $(2$ marks $)$ |
| (iii) Complete reversal of entries | $(2$ marks $)$ |
| (iv) Compensating errors | $(2$ marks $)$ |

(b) The trial balance of Amanda Ltd as at 30 April 2004 did not balance. On investigation, the following errors were discovered:

1. A loan of Sh. $2,000,000$ from one of the directors has been correctly entered in the cashbook but posted to the wrong side of the loan account.
2. The purchase of a motor vehicle on credit fro $S h .2,860,000$ had been recorded by debiting the supplier"s account and crediting the motor expenses account.
3. A cheque for $\mathrm{Sh} .80,000$ from Ogola, a customer to whom goods are regularly supplied on credit, was correctly entered in the cashbook but was posted to the credit of bad debts recovered account in the mistaken belief that it was a receipt from Agola, a customer whose debt had been written off three years earlier.
4. In reconciling the company"s cash book with the bank statement, it was found that bank charges of Sh. 38,000 had not been entered in the company"s records.
5. The totals of the cash discount columns in the cashbook for the month of April 2004 had not been posted to the respective discount accounts.

The figures were:

Discounts allowed
Sh. 184,000
Discounts received
397,000
6. The company had purchased some plant on 1 March 2003 for Sh.1,600,000. The payment was correctly entered in the cashbook but was debited to the plant repairs
account. Depreciation on such plant is provided for at the rate of $20 \%$ per annum on cost.

## Required:

(i) Journal entries with narrations to correct the above errors.
(ii) Suspense accounts showing the original difference
(2 marks)
(Total: 20 marks)

## QUESTION FOUR

Kalamu and Karatasi have been trading in partnership for several years, sharing profits and losses equally after allowing interest on their capitals at the rate of $8 \%$ per annum. On 1 September 2003, the manager of their business, Barua, was admitted as a partner and was to share one fifth of the profits after interest on capital Kalamu and Karatasi were to share the balance of the profits equally but guaranteed that Barua"s share would not fall below Sh.600,000 per annum.

Barua was not required to introduce any capital at the date of admission but agreed to retain Sh. 150,000 of his profit share at the end of each financial year to be credited to his capital account until the balance reached Sh.750,000. Until that time, no interest was to be allowed on his capital.

Goodwill was agreed at Sh.1,500,000 at 1 September 2003, but was not to be maintained in the accounts. Land and buildings were professionally valued at Sh.2,840,000 on the same date while the book value of equipment and motor vehicles was to be reduced to Sh.1,500,000 as at that date.
Barua was previously entitled to a bonus of $5 \%$ of the gross profit. This bonus was payable half yearly. The manager"s bonus and the manager"s salary were to cease when he became a partner.

The trial balance below was extracted as at 31 December 2003. No adjustments had yet been made in respect of Barua"s admission and the amount he introduced as his contribution forgoodwill had been posted to his current account. The drawings of all the partners had been charged to their current accounts.

Trial balance as at 31 December 2003

|  |  | Sh | Sh |
| :--- | :--- | ---: | ---: |
| Capital accounts : | Kalamu |  | $3,000,000$ |
| Current accounts : | Karatasi | Kalamu |  |
|  | Karatasi | 780,000 |  |
|  | Barua | 710,000 |  |
| Land and buildings |  | $1,800,000$ | 180,000 |
| Equipment and motor vehicles | $2,100,000$ |  |  |
| Stock | 920,000 |  |  |
| Gross profit | $1,600,000$ | $4,200,000$ |  |
| General expenses | 400,000 |  |  |
| Manager"s salary | 105,000 |  |  |
| Manager"s bonus | 485,000 |  |  |
| Debtors | $\underline{290,000}$ | $\mathbf{3 1 0 , 0 0 0}$ |  |
| Creditors | $\underline{9,190,000}$ | $\underline{9,190,000}$ |  |
| Bank balance |  |  |  |

## Additional information:

1. It is assumed that gross profit and general expenses accrued evenly throughout the year except that Sh. 100,000 of the general expenses relate to a bad debt that arose in the period after Barua"s admission. The balance of the general expenses accrued evenly.
2. Depreciation is to be charged on equipment and motor vehicles at the rate of $20 \%$ per annum on the book value. No depreciation is to be charged on land and buildings.

## Required:

(a) Profit and loss account for the year ended 31 December 2003
(b) Partner"s capital accounts as at 31 December 2003.
(c) Partner"s current accounts as at 31 December 2003.

## QUESTION FIVE

The book keeper of Bidii Ltd. prepared the following trial balance as at 31 December 2003:

|  | Sh. "000 | Sh. ${ }^{\text {"000 }}$ |
| :---: | :---: | :---: |
| Share capital |  | 100,000 |
| Share premium |  | 50,000 |
| Retained profits as at 1 January 2003 |  | 100,000 |
| 10\% debentures |  | 100,000 |
| Stock (1 January 2003) | 200,000 |  |
| Motor vehicles | 100,000 |  |
| Provision for depreciation as at 1 January 2003 - motor vehicles |  | 60,000 |
| Machinery | 120,000 |  |
| Provision for depreciation as at 1 January 2003 - machinery |  | 50,000 |
| Buildings at cost | 230,000 |  |
| Sales |  | 750,000 |
| Purchases | 350,000 |  |
| Discounts | 2,000 |  |
| Returns | 2,000 |  |
| Carriage | 2,000 |  |
| General expenses | 200,000 |  |
| Advertising | 10,000 |  |
| Creditors |  | 200,000 |
| Debtors | 200,000 |  |
| Provision for doubtful debts (1 January 2003) |  | 6,000 |
| Debenture interest | 5,000 |  |
| Cash at bank |  | 5,000 |
|  | 1,421,000 | 1,421,000 |

## Additional information:

1. In an effort to simplify the accounting process, the book keeper posted both discounts received and discounts allowed to the discounts account. He has also posted both returns inwards and returns outwards to the returns accounts, and both carriage inwards and carriage outwards to the carriage account. Discounts received, returns outwards and carriage outwards were as follows:

Sh.
Discounts received
Returns outwards Carriage outwards

1,000,000
1,000,000
$1,000,000$
2. The following items are already included in general expenses:

- Rates for the 12 months to 31 March 2004, Sh.4,000,000
- Insurance for the 12 months to 31 December 2003 amounted to Sh.2,000,000. Half of this amount relates to the managing director"s private expenses.

3. Accountancy fees of Sh. $1,000,000$ should be provided for
4. A debtor for Sh. $20,000,000$ has been declared bankrupt. The provision for doubtful debts is to be made at $5 \%$ of the debtors.
5. Dividends of Sh. $10,000,000$ have been proposed by the board of directors.
6. Stock as at 31 December 2003 is valued at Sh.180,000,000
7. Depreciation of $S h \cdot 20,000,000$ is to be provided on the motor vehicles and Sh. $10,000,000$ on the machinery. The buildings are to be revalued upwards by Sh.30,000,000

## Required:

(a) Trading and profit and loss and appropriation accounts for the year ended 31 December 2003.
(b) Balance sheet as at 31 December 2003
(Total: 20 marks)

## DECEMBER 2012

## QUESTION ONE

Okech and Wanjala are in a partnership business that sells hardware. They share profits and losses equally after allowing for an annual salary of Sh.600,000 to Okech. Interest is allowed on capital at $10 \%$ per annum. Their bookkeeper has produced the following list of balances as at 30 June 2004:

|  | Sh $^{\text {" }} \mathbf{0 0 0}$ |
| :--- | ---: |
| Capital accounts: Okech | 1,080 |
|  | Wanjala |
| 10\% loan accounts: Wanjala | 1,200 |
| 10\% debentures from bank | 600 |
| Drawings : Okech | 720 |
| Wanjala | 780 |
| Sales | 660 |
| Returns inwards | 13,572 |
| Closing inventory | 360 |
| Cost of sales | 2,040 |
| Sales ledger control account | 8,400 |
| Purchase ledger control account | 3,600 |
| Operating expense | 3,000 |
| Non-current asset | 3,132 |
| Provision for depreciation | 4,440 |
| Bank overdraft | 2,160 |
|  | 360 |

You ascertain that the bookkeeper is not sure whether the above balances are correct and on further investigation you discover the following:

1. The sales ledger control account does not agree with the list of balances from the ledger due to:

- The sales return day book has been under cast by Sh. 14,000 while a contra entry with the creditors ledger for Sh. 24,000 has been omitted from the control account.
- An invoice for Sh.240,000 was incorrectly entered in the sales day book as Sh.24,000.

2. Wanjala had paid some business expenses amounting to Sh. 60,000 from his personal bank account while Okech had taken goods costing Sh.120,000 for his own use. No entries have been made for these items.
3. A fully depreciated motor vehicle which cost Sh.600,000 was sold during the year for Sh. 120,000 . The entry for the proceeds was only posted in the bank account.
4. The bookkeeper had understated the bank overdraft by Sh.240,000.

## Required:

(a) A trial balance and a suspense account showing how the difference is accounted for.
(b) Trading, Profit and loss account for the year ended 30 June 2004.
(c) Balance sheet as at 30 June 2004.
(6 marks)
(Total: 20 marks)

## QUESTION TWO

(a) The bank statement and cashbook balances should agree, but sometimes these balancestmay not agree:

## Required:

Discuss this statement and explain why it is important to prepare a bank reconciliation statement. (8 marks)
(b) On 31 October 2004, the cashbook of Mwea Enterprises Ltd. Showed a debit balance of Sh.1,710,000. This did not agree with the balance shown in the bank statement.

Upon investigation, the accountant discovered the following errors:

1. A cheque paid to Kindaruma for Sh. 306,000 had been entered in the cashbook as Sh.387,000
2. Cash paid into the bank by a customer for Sh. 90,000 had been entered in the cashbook as Sh.81,000
3. A transfer of Sh. $1,110,000$ to Central Savings Bank had not been posted to the cash book.
4. A receipt of $S h .9,000$ shown in the bank statement had not been posted in the cashbook.
5. Cheques drawn amounting to Sh. 36,000 had not been paid into the bank.
6. The cash book balance had been incorrectly brought down at 1 November 2003 as a debit balance of Sh.1,080,000 instead of a debit balance of Sh.990,000
7. Bank charges of $S h .18,000$ do not appear in the cash book.
8. A receipt of $\mathrm{Sh} .810,000$ paid into the bank on 31 October 2004 appeared in the bank statement on 1 November 2004.
9. A standing order of $\mathrm{Sh} .27,000$ had not been recorded in the cash book.
10. A cheque for $S h .45,000$ previously received and paid into the bank had been returned by the customer"s bank marked "account closed".
11. The bank received a direct debit of Sh. 90,000 from an anonymous customer.
12. Cheques banked had been totaled at Sh. 135,000 instead of $\operatorname{Sh} .153,000$.
13. A cheque drawn in favour of Nyaga for $S h .120,000 \mathrm{had}$ been entered on the debit side of the cashbook.

## Required;

(i) Adjusted cash book as at 31 October 2004.
(6 marks)
(ii) A bank reconciliation statement as at 31 October 2004.
(Total: 20 marks)

## QUESTION THREE

An extract from the balance sheet of Kimwa Construction Ltd as at 30 June 2003 showed the following summary of property, plant and equipment:

|  | Equipment | Furniture | Motor vehicles |
| :--- | ---: | ---: | ---: |
| Sh."000 | Sh."000 | Sh."000 |  |
| Cost | 700,000 | 140,000 | 140,000 |
| Accumulated depreciation | $\underline{336,000}$ | $\underline{70,000}$ | $\underline{98,000}$ |
|  | $\underline{364,000}$ | $\underline{70,000}$ | $\underline{42,000}$ |

The following transactions took place during the year ended 30 June 2004:

1. The company incurred the following costs in acquiring new equipment

## Sh. "000

Invoice price of equipment"
Freight
Installation
Insurance in transit

140,000
10,500
10,500
14,000
175,000
2. Property, plant and equipment disposed of during the year were as follows:

In addition, a new truck was acquired by trading in an old truck at an agreed value of Sh. 10.5 million and making an additional cash payment of Sh. 15 million. The old truck had cost Sh. 15 million in July 2000.
3. The directors recommended a reclassification of some items of equipment to furniture. These items had cost Sh. 15 million and had accumulated depreciation of Sh. 3 million.
4. The company"s policy is to charge depreciation on a straight line basis at the following rates:
Equipment $20 \%$ per annum
Furniture $\quad 12 \frac{1}{2} \%$ per annum
Motor vehicles $30 \%$ per annum
5. A full year"s depreciation was charged in the year of acquisition but none in the year of disposal.

## Required:

(a) Explain two other methods of charging depreciation that Kimwa construction Ltd could have used.
(b) A property, plant and equipment disposal account for the year ended 30 June 2004.
(4 marks)
(c) A property, plant and equipment movement Schedule for the year ended 30 June 2004
(12 marks)
(Total: 20 marks)
Hint:; International financial reporting standards use the term property, plant andequipment while Kenyan Accounting Standards (no longer applicable) used the term fixed assets.

## QUESTION FOUR

(a) Distinguish reserves from share capital.
(b) The trial balance of Plastics Ltd as at 31 October 2004 is as follows:

## Sh."000 <br> Sh. "000

Ordinary shares of Sh. 50 each
$10 \%$ preference shares of Sh. 100 each
$10 \%$ debentures
Land and buildings (net book value)
25,000
Plant and machinery (net book value)
Motor vehicles (net book value)
8,000
Inventory
Accounts receivables and payables
Cash at bank
Capital redemption reserve
2,000
6,000
20,000
19,000
4,100
Share premium
Retained profits as at (November 2003)
Debenture interest
400
Preference dividend 450
Gross profit
Other operating income
Administrative expenses
Distribution costs
Other operating expenses 13,000 1,550
Interim ordinary dividend paid
2,000
Corporation tax
$\overline{88,500}$
500
$\underline{88,500}$

## Additional information:

1. A building whose net book value is currently Sh. 5 million is to be revalued to Sh. 9 million
2. A final ordinary dividend of Sh. 2 million is proposed.
3. The balance on the corporation tax for the current year is estimated at Sh. 3 million.

## Required:

(i) Income statement for the year ended 31 October 2004.
(8 marks)
(ii) Balance sheet as at 31 October 2004.
(7 marks)
(Total: 20 marks)

## QUESTION FIVE

(a) Explain the meaning of prudence concept showing how this is applied in stock valuation. (3 marks)
(b) The summarized financial statements of Baraka Enterprises Ltd. are as follows:

## Income statement for the year ended 30 September

|  | $\mathbf{2 0 0 3}$ | $\mathbf{2 0 0 4}$ |
| :--- | ---: | ---: |
| Sales | Sh."000 | Sh."000 |
| Cost of sales | 20,000 | 28,000 |
| Gross profit | $(15,000)$ | $(21,000)$ |
| Administrative expenses | 5,000 | 7,000 |
| (4, | $(3,800)$ | $(4,600)$ |

Debenture interest
(400)

Net profit $\quad 1,200 \quad \underline{2,000}$

## Balance sheet as at 30 September

2003
2004
Sh."000 Sh."000
Assets:

| Non-current assets (net book value) | $\underline{11,000}$ | $\underline{14,000}$ |
| :--- | ---: | ---: |
| Current assets: | 2,000 | 3,000 |
| Inventories | 2,500 | 2,800 |
| Trade and other receivables | $\underline{4,500}$ | $\underline{500}$ |
| Balance at bank | $\underline{6,300}$ |  |
| Total assets | $\underline{15,500}$ | $\underline{20,300}$ |

Equity and liabilities:
Capital and reserves:
Issued and fully paid
$1,000,000$ ordinary shares of Sh. 10 each $\quad 10,000 \quad 10,000$
Revenue reserves
3,000
$\underline{13,000}$$\underline{\underline{14,100}}$

Non current liabilities
$8 \%$ debentures

- $\quad$, 0 ,000

Current liabilities
Trade and other payables
Bank overdraft
Total equity and liabilities

| 1,500 | 1,200 |
| ---: | ---: |
| 1,000 | $\underline{1,200}$ |
| $\underline{2,500}$ | $\underline{15,500}$ |
| $\underline{20,300}$ |  |

Stock as at 1 October 2002 was Sh.5,000,000

## Required:

For each year, calculate the following:
(a) Gross profit margin
(2 marks)
(b) Inventory turnover (2 marks)
(c) Return on equity
(2 marks)
(d) Return on assets (2 marks)
(e) Acid test ratio
(2 marks)
(f) Current ratio
(2 marks)
(g) Financial leverage
(2 marks)
(c) Comment on the liquidity position of the company giving possible reasons for the change.
(3 marks)
(Total: 20 marks)

## JUNE 2013

## QUESTION ONE

Chacha and Mushi are in partnership sharing profits and losses equally. They manufacturer shoes whose brand name is "DAWO". Their trial balance as at 31 December 2004 was as follows:

|  | Sh. ${ }^{\text {"000 }}$ | Sh."000 |
| :---: | :---: | :---: |
| Capital accounts: |  |  |
| Chacha |  | 4,000 |
| Mushi |  | 4,000 |
| Current accounts: |  |  |
| Chacha |  | 500 |
| Mushi | 100 |  |
| Drawings: |  |  |
| Chacha | 200 |  |
| Mushi | 300 |  |
| Stock (1 January 2004) |  |  |
| Raw materials | 1,500 |  |
| Work in progress | 2,200 |  |
| Finished goods | 1,200 |  |
| Factory land and buildings at cost (land Sh. 17 million) | 18,000 |  |
| Plant and machinery at cost | 3,500 |  |
| Delivery van (for sales distribution) | 1,400 |  |
| Provision for depreciation on: |  |  |
| Factory buildings |  | 40 |
| Plant and machinery |  | 1,400 |
| Delivery van |  | 700 |
| Sales |  | 86,240 |
| Purchases of raw materials | 40,000 |  |
| Production wages | 10,000 |  |
| Factory manager"s salary | 480 |  |
| Office salaries | 5,000 |  |
| Distribution costs | 3,250 |  |
| Factory rates and insurance | 700 |  |
| Fuel and electricity | 800 |  |
| Office rates and insurance | 500 |  |
| Bad debts | 20 |  |
| Provision for doubtful debts |  | 20 |
| Royalties payable | 1,000 |  |
| Trade debtors and creditors | 800 | 700 |
| Bank balance | 6,390 |  |
| Carriage on raw materials | 500 |  |
| Provision for unrealized profit |  | 240 |
|  | 97,840 | 97,840 |

## Additional information:

1. Stock at 31 December 2004 was valued as follows:

Sh. "000
Raw materials
2,000
Work in progress 4,200
Finished goods 1,000
2. Insurance prepaid (31 December 2004)

|  | Sh. "000 |
| :--- | :--- |
| Factory | 200 |
| Office | 35 |

Rates owing (31 December 2004)

|  | Sh."000 |
| :--- | :--- |
| Factory | 500 |
| Office | 25 |

3. Depreciation is provided at the following rates:

Factory buildings - 2\% per annum on cost
Delivery van $-25 \%$ per annum on cost
Plant and machinery - 20\% per annum on cost
4. Provision for doubtful debts is to be maintained at $5 \%$ of the debtor"s balance at the end of the year.
5. Manufactured goods are transferred to the warehouse at cost plus $25 \%$ of factory profit
6. The partnership agreement has the following provisions:
(i) A commission of $10 \%$ to Mushi based on factory profit while Chacha is entitled to a commission of $10 \%$ based on net profit from trading.
(ii) Partners are allowed interest on their fixed capitals at a rate of $10 \%$ per annum.
(iii) Chacha had guaranteed Mushi a total income from the partnership of not less than Sh.15,000,000 per annum.

## Required:

(a) Manufacturing, trading and profit and loss and appropriation accounts for the year ended 31

December 2004.
(12 marks)
(b) Balance sheet as at 31 December 2004.
(Total: 20 marks)

## QUESTION TWO

The following draft accounts have been prepared by the treasurer of Wasomaji Members Club:

## Income and expenditure account for the year ended 31 December 2004

Sh. "000
Sh. "000
Sundry income
24,127
Expenditure
Use of premises 4,812
Printing, postage and stationery 783
Overdue members subscriptions written off 120
Member"s welfare 520
Bar purchases 7,720
Wages 2,080
Reference books purchased $\quad \underline{(18,366)}$
Surplus for the year
5,761

## Balance sheet as at 31 December 2004

Assets: Minibus (Cost:: 1 January 2002)
Sh. "000
Library and furniture
6300
$1,1,380$
Members subscriptions due $\quad 5,400$
Cash in hand 120
Bank: Fixed deposit account 1,500
Current account 2,810
$10 \%$ Treasury bond (Sh. 10 million nominal value) 10,000
27,210
Less: Owing for bar purchases $\quad \underline{1,867}$
Club funds as at 31 December $2004 \quad \underline{25,343}$

## Additional information:

1. The treasurer had little accounting knowledge and some figures appearing in the draft accounts were incorrect.
2. The club"s policy on outstanding subscriptions was to write off amounts outstanding for a period exceeding five years. As at 1 January 2004, subscriptions outstanding from members were Sh.3,120,000
3. The club"s premises were purchased on 1 October 2004 for Sh. 4 million. This amount was posted to the use of premises account in the draft accounts.
4. The treasury bond was purchased for Sh. 9.3 million on 1 January 2000 by utilizing donations earmarked for a member"s welfare fund. Up to 31 December 2003, the income received from this investment had been distributed to members. The income for the year ended 31 December 2004 was included under sundry income as resolved at the annual general meeting held on 10 April 2004.
5. The club runs a bar for the benefit of members. This bar sells stock at a mark-up of $30 \%$. The income from bar sales amounting to Sh. $9,927,000$ was included under sundry income. There was no opening stock as at 1 January 2004 and the club owed suppliers Sh.1,625,000 as at 1 January 2004. Bar closing stock as at 31 December 2004 was not ascertained.
6. The balance of the fixed deposit account as at 1 January 2004 amounted to Sh. 1,500,000 reflected in the balance sheet as at 31 December 2004. No account was taken of interest amounting to Sh.100,000 which had been credited to the fixed deposit during the year.
7. As at 1 January 2004, cash in hand was Sh.100,000 and the bank current account was overdrawn by Sh.893,000.
8. The reference books purchased during the year are to be capitalized as part of the library. Library and furniture are to be revalued to Sh.5,000,000
9. Depreciation is to be provided based on the cost of the assets as follows:

| Club premises | $-2 \%$ per annum |
| :--- | :--- |
| Minibus | $-20 \%$ per annum |

## Required:

(a) Income and expenditure account for the year ended 31 December 2004. (10 marks)
(b) Balance sheet as at 31 December 2004.
(Total: 20 marks)

## QUESTION THREE

Faida Commercial Bank Ltd. offered 200,000 ordinary shares for sale to the public at a par value of Sh. 25 each on 1 April 2004, payable as follows:

- On application, Sh. 5 due on 15 April 2004
- On allotment, Sh. 5 due on 30 April 2004
- On first call, Sh. 7.50 due three months after allotment
- On second and final call, Sh.7.50 due three months after the first call.


## Additional information:

1. The company received applications for 530,000 shares on the due dates. Applications for 30,000 shares were rejected and the application money refunded. The rest of the applicants were allotted shares on a prorate basis.
2. One month after allotment, one shareholder of 2,000 shares remitted Sh. 25,000 as calls in advance. The rest of the calls were received on the due dates except for money due on second and final call for Sh. 8,000 shares which was paid three months late.
3. The surplus application monies were treated as calls in advance.
4. The company"s articles of association provided for charging of interest on calls in arrears at $10 \%$ per annum.

## Required:

Ledger accounts to record the above transactions.
(20 marks)

## QUESTION FOUR

(a) Explain the advantages of maintaining control accounts.
(6 marks)
(b) The following balances were extracted from the books of Katee Ltd. for the month of April 2005:

| Debit balances (1 April 2005): Sales ledger |  |
| :--- | ---: |
|  | Purchases ledger |
|  | $1,428,000$ |
| Credit balances (1 April 2005): Sales ledger |  |
|  | Purchases ledger |
| Discounts received | 10,500 |
| Discounts allowed | 40,500 |
| Purchase (including cash purchases of Sh.152,000) | 553,800 |
| Cash sales | 142,500 |
| Credit sales | 209,700 |
| Credit notes issued to customers for returned goods | $1,334,000$ |
| Sales ledger debit balances off-set against purchases ledger | 618,000 |
| Payment to creditors | $2,068,200$ |
| Interest charged by creditors on overdue accounts | 75,000 |
| Receipt from customers | 36,900 |
| Bad debts written off | $1,159,200$ |
| Customer"s unpaid cheques | 69,000 |
| Interest charged to customers on overdue accounts | $1,578,000$ |
| Debt collection expenses charged to debtors | 37,200 |
| Credit notes received from suppliers | 26,100 |
| Balances as at 30 April 2005: Purchases ledger (debt) | 96,100 |
|  | 10,800 |
|  | 26,700 |
|  | Sales ledger (credit) |

## Required:

(i) Sales ledger control account for the month ended 30 April 2005.
(ii) Purchases ledger control account for the month ended 30 April 2005.

## QUESTION FIVE

a) Explain the importance of ratio analysis to a business enterprise.
b) Identify with reasons, one party who may be interested in each of the following ratios:

| (i) | Current ratio | $(2$ marks $)$ |
| :--- | :--- | :--- |
| (ii) | Net profit margin | $(2$ marks |
| (iii) | Stock turnover | $(2$ marks $)$ |

c) Citing suitable examples, briefly explain of the following terms:

| (i) | Accounting concepts | $(2 \mathrm{marks})$ |
| :--- | :--- | ---: |
| (ii) | Accounting policies | $(2 \mathrm{marks})$ |
| (iii) | Accounting standards | $(2 \mathrm{marks})$ |

d) Explain the accounting treatment that would be applicable in dealing with the following transactions relating to the accounts of Mlachake Ltd. for the year ended 31 December 2004:
(i) A debtor who owed the company Sh.200,000 was declared bankrupt on 1 February 2005. 25\% of the debt had been recovered when the accounts were approved by the directors on 15 March 2005. (2 marks)
(ii) Some items of inventory purchased for Sh.300,000 were damaged in the warehouse during the year. These items were repaired at Sh.50,000 and sold to a customer on 2 February 2005 at $75 \%$ of the normal selling price of Sh.400,000 (2 marks)
(iii) On 10 December 2004, the company secured an order worth Sh.1.2 million from a foreign based company. The goods were shipped on 10 January 2005 and included in sales for December $2004 . \quad$ ( 2 marks)
(Total: 20 marks)

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

## QUESTION ONE

Araka Ltd., a company dealing in retail products, extracted from the following trial balance as at 30 September 2005:

Accumulated depreciation
Sales
Purchases
Cash in hand
Creditors ledger control account
Electricity
Ordinary share capital
Cash at bank
Debtors ledger control account
Suspense account
Inventory as at 1 October 2004
Retained profits
Motor vehicle expenses
Sundry expenses
Salaries and wages
Directors remuneration
Bank charges
Motor vehicles: Cost
Accumulated depreciation

Shs. ,000" Shs. „000"
121,500
431,000

64,172
68,960

16,074
1,312,567
839,004
1,268

6,917

1,210
61,074
4,300
41,912

4,174
2,002
121,600

| 48,999 |  |
| ---: | ---: |
| 1,621 |  |
| 28,900 |  |
| $\underline{1,779,542}$ | $\underline{1,779,542}$ |

## Additional information:

1. Provision for doubtful debts should be made at $2 \%$ of the debtors ledger balances after writing of bad debts amounting to Shs. 1,370,000.
2. The suspense account was analysed as follows:

|  | Shs. „000" | Shs. „000" |
| :--- | ---: | ---: |
| Bad debts written off during the year | 512, |  |
| Motor vehicle purchased on 1 April 2005 | 7,400 |  |
|  |  | 7,912 |
| Less: motor vehicle sold on 1 April 2005 | 3,000 |  |
| Amounts received in respect of a bad debt recovered | $\underline{612}$ | $\underline{(3,612)}$ |
|  |  | $\underline{4,300}$ |

3. The motor vehicle sold during the year had been purchased on 1 February 2002 for Sh.6,500,000.
4. Bank statement as at 30 September 2005 showed bank charges of Sh. 533,000 . This had not been recorded in the cash book.
5. The debtors ledger control account did not agree with the list of balances in personal accounts. You ascertain that some invoices for October 2005 had been posted in the personal accounts as at September 2005. The list of balances was overstated by Sh.4,300,000.
6. Estimated corporation tax for the year ended 30 September 2005 was Sh. $131,700,000$.
7. The value of inventory as at 30 September 2005 was amounted to Sh. $62,047,000$.
8. The directors proposed to pay ordinary dividend of $10 \%$.
9. The following petty cash expenditure had not been recorded:

Shs. „000"
Motor vehicle expenses 412
Sundry expenses 91
Casual workers wages 36
10. Depreciation is provided at the following rates: Buildings- $2 \%$ per annum on cost
Plant and machinery - $20 \%$ per annum on reducing balance basis. Motor vehicle $-25 \%$ per annum on cost
Full year"s depreciation is provided in the year of purchase and none in the year of disposal.

## Required:

a) Trading profit and loss account for the year ended 30 September 2005.
(12 marks)
b) Balance sheet as at 30 September 2005
(8 marks)
(Total: 20 marks)

## QUESTION TWO

Omondi and Maina trade as partners in a brick manufacturing firm sharing profits and losses in the ration of 3:2 after charging their annual salaries of Shs. 2,500,000 each.

The trial balance extracted from their records as at 31 October 2005 were as follows:

|  | Sh. „000" | Sh. „,000" |
| :--- | ---: | ---: |
| Capital accounts:Omondi <br> Maina |  | 23,400 |
|  |  | 3,000 |
| Current accounts: Omondi | Maina |  |
|  |  | 3,400 |
| Cash from Ombati | 8,000 | 3,400 |
| Life assurance policy | 192,000 | 248,000 |
| Sales | 20,000 |  |
| Purchases | 10,000 |  |
| Wages | 9,000 |  |
| Salaries | 24,000 |  |
| General expenses | 9,400 |  |
| Plant and machinery | 18,000 |  |
| Motor vehicles | 16,000 | 10,200 |
| Accounts receivable | 1,600 | 1,400 |
| Accounts payable | $\underline{12,800}$ |  |
| Inventory as at 1 November 2004 | $\underline{320,000}$ | $\underline{320,000}$ |
| Provision for doubtful debts |  |  |

## Additional Information:

1. On 1 March 2005, the partners agreed to admit Ombati into the partnership on the following terms:

- Ombati to pay sh. $3,400,000$ as his capital contribution.
- Ombati to be entitled to a salary of Sh.2,000,00 per annum and a share of $10 \%$ of the profits.
Omondi and Maina were to continue sharing profits in their old ratios, but guaranteed that
Ombati"s share of profits after salaries would not fall below Sh.1,200,000 per year.
Goodwill was agreed at Sh.2,100,000 but was not to be retained in the books.

2. The life assurance policy was surrendered on 1 December 2004 for Sh.9,500,000 and the proceeds paid directly to Omondi and Maina in their profit sharing ratio. The necessary entries in the current accounts were not made to account for this transaction.
3. The details of the savings bank account were as follows:

Sh. „000"
Paid in by Ombati as per agreement 3,400
Receipts from general cash account $\quad \underline{9,400}$
12,800
4. The actual balance on the bank savings account as at 31 October 2005 amounted to Sh. 400,000 . The difference was due to drawings by Omondi Sh.3,400,000. Maina Sh. $3,000,000$, Ombati Sh.1,200,000 and tax amounting to Sh.4,800,000 paid on behalf of the partners (Omondi Sh.2,400,000, Maina Sh.2,000,000 and Ombati Sh.400,000).
5. Inventory as at 31 October 2005 was valued at Sh. 19,000,000.

Depreciation is to be provided on plant and machinery at $10 \%$ per annum and on motor vehicles at $20 \%$ per annum.
6. Provision for doubtful debts should be maintained at $5 \%$ of the balance in the debtors ledger.

## Required:

a) Trading, profit and loss and appropriation accounts for the year ended 31 October 2005.
b) Partners" current accounts.
( 12 mariss) (4 marks)
c) Partners" capital accounts.
(4 marks)
(Total: 20 marks)

## QUESTION THREE

(a) State four purposes of ratio analysis
(b) The following information was extracted from the financial statements of Sunrise Ltd. and Sunset Ltd. in respect of the year ended 30 September 2005:

Income statement extracts for the year ended 30 September 2005:

| Sunrise Ltd. | Sunset Ltd. <br> Shs. ,000" |
| ---: | ---: |
| Shs. ,000" |  |

Sales
Cost of sales
258,000 153,000
Operating profit
19,000
Balance sheet extracts as at 30 September 2005:

| Sunrise Ltd. | Sunset Ltd. |
| ---: | ---: |
| Shs. ,000" | Shs. ,000" |
| 142,000 | 92,000 |

Non-current assets
142,000
92,000

Current assets:

| Inventory | 100,000 | 87,000 |
| :--- | ---: | ---: |
| Debtors | 46,000 | 42,000 |
| Cash at bank | 40,000 | 44,000 |
| Current liabilities | 98,000 | 108,000 |
|  |  |  |
| Long-term loan | 33,000 | - |
| Shareholders funds | 197,000 | 157,000 |

## Required:

For each company, compute the following ratios:

| (i) | Acid test ratio | $(2 \mathrm{marks})$ |
| :--- | :--- | :--- |
| (ii) | Inventory turnover | $(2 \mathrm{marks})$ |
| (iii) | Average collection period | $(2 \mathrm{marks})$ |
| (iv) | Return on capital employed | $(2 \mathrm{marks})$ |
| (v) | Debt equity ratio | $(2 \mathrm{marks})$ |

(c) (i)On the basis of the ratios computed in (b) above, comment on the overall performance of Sunrise Ltd. and Sunset Ltd. and advise which of the two companies would provide better investment. ( 3 marks)
(ii) Explain the possible shortcomings of relying on your analysis in (b) above.
(Total: 20 marks)

## QUESTION FOUR

## (a) Briefly explain the concept "substance over form" with respect to:

(i) Motor vehicles acquired on hire purchase. (2 marks)
(ii) Leasehold land. (2 marks)
(b) Photomap Ltd. is a leading manufacturer of digital video disks (DVDs). As part of its modernization programme, the company decided to replace its old machinery with a state of the art machine imported from Denmark. The following expenses were incurred for the purpose in the year ended 30 September 2005:

> Shs. „000"

Catalogue price less cash discount at $10 \%$ of the list price 30,000
Freight and insurance 7,000
Customs and excise duty $\quad 7,300$
Value added tax $\quad 7,100$
Installation costs 2,000
Pre-production testing 700
Training costs (machine attendant) 50
Insurance (annual) 700
$\begin{array}{ll}\text { Salary paid to machine attendant (annual) } & 100\end{array}$

## Additional information:

1. The old machinery disposed of in the year ended 30 September 2005 for Shs. 1,500,000 had cost the company Shs. 2,000,000 on 1 October 2002. An air conditioner equipment purchased for Shs. 545,000 at the same time with the disposed of machinery was scrapped during the year since it was no longer required.
2. The furniture used by the company was acquired on 1 October 2003 at a cost of Shs. 800,000.
3. The value added tax incurred by the company in respect of the machinery was recovered from the tax authority against output value added tax.
4. Depreciation per annum is provided at the following rates:

| Machinery | $-25 \%$ on reducing balance basis |
| :--- | :--- |
| Equipment | $-\quad 20 \%$ on cost |
| Furniture | $-\quad 15 \%$ on cost |

Full year"s depreciation is provided in the year of acquisition and none in the year of disposal.

## Required:

(i) Ascertain the cost of the new machinery. (3 marks)
(ii) Disposal accounts.
(iii) Provision for depreciation accounts.
(iv) A property, plant and equipment movement schedule for the year ended 30 September 2005.
( 7 marks)

## QUESTION FIVE

(a) Using suitable examples, explain the meaning of the following terms: (i) Accounting standards.
(ii) Accounting policies. (2 marks)
(iii) Accounting bases
(b) 'Qualitative characteristics are the attributes that make information provided in financial statements useful to users."

Briefly explain the four main qualitative characteristics of financial statements with reference to shareholders of a company. (6 marks)
(c) While research and development costs of a project may meet the definition of an asset, the cost may not meet the criteria used in recognizing an asset.

Define the term "asset" and explain the criteria used in recognizing an asset. (3 marks)
(d) Give five purposes of control accounts.

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

## QUESTION ONE

Panter limited is a medium-sized company engaged in the business of selling sports accessories. The business premises are rented for sh. 8 million per annum. During the year ended 30 September 2005, the book keeper maintained incomplete records and some information was lost. However, the balances availed as at 30 September 2004 were as follows:

| Authorised, issued and fully paid |  | sh. 000 |  | Sh. 000 |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  |  |  |  | Motor vehicles (net | 12,000 |
| Ordinary shares of | each | 30,000 |  | Fixtures and fittings | 4,000 |
| Retained profit |  | 27,500 |  | Inventory | 20,000 |
| Accounts payable: | Trade |  | 14,000 | Accounts receivable | 16,800 |
|  | Other |  | 360 | Prepayments - rent | 3,000 |
|  |  |  |  | Cash at bank | 15,230 |
|  |  |  |  | Cash in hand | 830 |
|  |  |  | 71,860 |  | 71,860 |

An examination of panter's books of account for the year ended 30 September 2005 revealed the following:

1 Amounts banked:
Sh.'000'

Loan from Len Ltd. (1 January 2005)
5,000
Sale of old stocks
12,000
Other collections
214,170
231,170
2 Payments by cheque:

|  | Sh.'000' |
| :--- | :---: |
| Purchase of inventory | 162,040 |
| Wages | 21,220 |
| Rent | 7,500 |
| Motor vehicle expenses | 12,140 |
| Purchase of: $\quad$ Motor vehicles | 15,000 |
|  | Fixture and fittings |
| Repairs | 5,000 |
| Sundry expenses | 6,220 |

234,250

3 Amounts paid out from the cash before bankings were made:

|  | Sh.'000' |
| :--- | ---: |
| Wages | 5,160 |
| Motor vehicle expenses | 830 |
| Sundry expenses | 750 |
|  | $\underline{6,740}$ |

4 The following closing balances were ascertained as at 30 September 2005.

|  | Sh.'000' |  |
| :--- | ---: | ---: |
| Cash in hand | 370 |  |
| Inventory (Sh.4,700,000 from Kitale Sports Dealers) | 19,100 |  |
| Accounts payable: | Trade | 13,410 |
|  | Other | 470 |
|  |  | 33,350 |

5 Panter Ltd. Applies a uniform gross profit margin of $40 \%$ on all sales except for goods purchased from Kitale Sports Dealers, where a $15 \%$ gross profit margin is charged.

During the year ,the cost of goods purchased from Kitale Sports Dealers was sh. 37 million.
6 The loan from Len carried interest at the rate of $12 \%$ per annum. Panter Limited had paid sh. 400,000 from the cash in hand as part of the interest payment.

7 The sale of old stock related to goods which had been included in the opening inventory. These goods were sold at $20 \%$ below the normal selling price and all the receipts were in cash.
8 During the year, all the motor vehicles were replaced with new ones. The new motor vehicles cost sh. 29 milion and were traded in with old motor vehicle at their book values.
Depreciation on motor vehicles and fixtures and fittings is to be provided on reducing balance at the rate of 20 per cent per annum. Full year's charge is to be made in the year of purchase and none in the year of disposal.

9 Panter limited owed sh. 710,000 for wages and sh.1,130,000 for motor vehicle expenses.
10 Tax of Sh. 10 million should be provided for.

## Required:

(a) Income statements for the year ended 30 September 2005
(12 marks)
(b) Balance sheet
(8 marks)

## (Total: 20 marks)

## QUESTION TWO

Umoja Women's Welfare Society sells water tanks at subsidised prices to its members and the general public. The members" contributions are used to meet the cost of manufacturing the water tanks.
The trial balance extracted from the books of account of the society as at 30 April 2006 was as follows:
$\begin{array}{lll}\text { Accumulated fund as at } 1 \text { may } 2005 & \text { Sh.'000' } & \text { Sh.'000 } \\ \text { Annual subscriptions received } & & 25,000 \\ & 10,000\end{array}$

| Stock of raw materials as at 30 April 2006 | 20,000 |  |
| :---: | :---: | :---: |
| Motor vehicle: Cost | 10,000 |  |
| Accumulated depreciation |  | 4,000 |
| Machinery: Cost | 22,000 |  |
| Accumulated depreciation |  | 5,000 |
| Donations from members |  | 2,500 |
| Raw materials used in production of water tanks | 35,000 |  |
| Sale of water tanks |  | 45,000 |
| Selling expenses | 2,000 |  |
| Factory wages | 600 |  |
| Factory overheads | 1,000 |  |
| Creditors for raw materials |  | 2,800 |
| Cash at bank and in hand | 500 |  |
| Society's office expenses | 4,100 |  |
| Membership fees fund |  | 7,500 |
| Sale of Raffle tickets |  | 2,800 |
| Raffle prizes paid | 1,200 |  |
| Cost of raffle tickets | 300 |  |
| Suspense account | 7,900 |  |
|  | 104,600 | 104,600 |

## Additional information:

1 An investigation carried out on the suspense account revealed that it comprised:

## Sh.'000'

Subscriptions in arrears as at 30 April 2005
3,500
Bonus paid to factory staff during the year
1,500
Rent for factory building
1,000
Rent for the society's offices
4,000
Subscriptions in advance as at 30 April 2005

2,100
7,900

2 Annual subscriptions in arrears as at 30 April 2006 amounted to Sh.2,000,000 while subscriptions received in advance as at 30 April 2006 amounted to sh.1,500,000.

3 The membership fee is levied every ten years. The membership fees attributable to the year ended 30 April 2006 amounted to sh.800,000

4 Accrued society's office expenses as at 30 April 2006 amounted Sh.400,000.

5 The motor vehicle usage should be apportioned to the factory and society's offices at $80 \%$ and $20 \%$ respectively. Depreciation should be provided on cost at $5 \%$ per annum on machinery and $10 \%$ per annum on motor vehicles.

## Required:

(a) Water tanks trading and profit and loss account for the year ended 30 April 2006 (6 marks)
(b) Income and expenditure account for the year ended 30 April 2006 (8 marks)
(c) Balance sheet as at 30 April 2006. (6 marks)
(Total: 20 marks)

## QUESTION THREE

Ben Mogaka prepared the following draft balance sheet for BM Enterprises as at 31 December 2005:

| Non current assets | Cost Sh. | Accumulated depreciation Sh. | Net book value Sh. |
| :---: | :---: | :---: | :---: |
| Equipment | 450,000 | 220,000 | 230,000 |
| Furniture | 300,000 | 150,000 | 150,000 |
| Motor vehicles | 600,000 | 300,000 | 300,000 |
|  | 1,350,000 | 670,000 | 680,000 |
| Current Assets: |  |  |  |
| Inventory |  | 122,800 |  |
| Accounts receivable |  | 19,600 |  |
| Deposit account |  | 50,000 |  |
| Suspense account |  | 9,000 | $\begin{aligned} & \underline{201,400} \\ & \underline{881,400} \end{aligned}$ |
| Financed by: |  |  |  |
| Capital |  | 652,000 |  |
| Net profit |  | 153,200 |  |
| Drawings |  | $(13,200)$ | 792,000 |
| Current liabilities: |  |  |  |
| Accounts payable |  | 81,400 |  |
| Bank over draft |  | 8,000 | 89,400 |
|  |  |  | 881,400 |

## Additional information:

On further investigation, the suspense account was discovered to have resulted from the following errors:

1 The sales of goods on credit to Alex Otis amounting to Sh.19,000had been recorded in the sales journal as sh. 9,000 .
2 A receipt of $S h .20,000$ from sale of an item of equipment had been credited to sales account. The equipment was shown in the books of account at costs of account of Sh. 90,000 and accumulated depreciation of Sh.72,000.

3 A credit note from a supplier, Simon Masound for Sh.15,000 had been omitted from the books.

4 A bank overdraft for Sh.7,000 reflected in the cash book as at 31 December 2005 was omitted In the trial balance.
5 A payment of Sh. 9,700 to Tom Wambugu, a creditor, was correctly entered in the cahs book but posted to his personal account as Sh.7,900.

6 The debit side of rent expense account had been undercast by Sh.1,000.
7 A provision of Sh.2,000 for sundry expenses outstanding as at 31 December 2004 and debited to sundry expenses at that dated had not been brought forward to the credit of the account in the following period. No credit entry had been made in any other account in respect to this account in respect to this item.

8 Discount received from the supplier of Sh.8,200 had been entered on the wrong side of purchases ledger control account.
9 On 31 December, goods valued at Sh.9,600 (selling price) were returned by Jane Kerubo (a debtor). No entry had been made in the books to reflect this transaction. These goods were not included in the closing stock.

10 Discounts allowed were overcast by Sh.1,200.

## Required:

(a) Journal entries to correct the above errors (Narration not required) (7 marks)
(b) Suspense account. (3 marks)
(c) Statement of corrected net profit for the year ended 31 December 2005 (6 marks)
(d) Corrected balance sheet as 31 December 2005. (4 marks)
(Total: 20 marks)

## QUESTION FOUR

(a) Briefly explain why goodwill should be paid under the following circumstances:
i. By a partner on admission to a partnership.
(2 marks)
ii. To a partner on retirement from a partnership.
(2 marks)
(b) Akili, Busara and Chema are in partnership sharing profits sharing profits and losses equally after allowing for interest on capital at $5 \%$ per annum to the partners and a salary to Busara of Sh.20,000 per month.

The trial balance of the partnership as at 30 April 2006 was as follows:

|  |  | Sh. ${ }^{\prime} 000{ }^{\prime}$ | Sh. ${ }^{\prime} 000$ |
| :---: | :---: | :---: | :---: |
| Capital accounts: | Akili |  | 2,500 |
|  | Busara |  | 2,000 |
|  | Chema |  | 1,000 |
| Current accounts: | Akili |  | 200 |
|  | Busara |  | 300 |
|  | Chema |  | 200 |
| Drawings: $\quad \begin{aligned} & \text { A } \\ & \\ & \\ & \end{aligned}$ |  | 300 |  |
|  |  | 400 |  |
|  |  | 200 |  |
| Sales |  |  | 20,000 |
| Inventory as at 1 May 2005 |  | 3,000 |  |
| Purchases |  | 10,300 |  |
| Operating expenses |  | 6,400 |  |
| Loan: Busara (Interest at $10 \%$ per annum) Chema (Interest at $10 \%$ per annum) |  |  | 1,000 |
|  |  |  | 2,000 |
| Land |  | 1,000 |  |
| Buildings |  | 5,000 |  |
| Plant and machinery: | Cost | 7,000 |  |
|  | Accumulated depreciation (30 April 2006) |  | 4,000 |
| Accounts receivable/accounts payable |  | 4,000 | 3,300 |
| Cash at Bank |  |  | 1,100 |
|  |  | 37,600 | 37,600 |

## Additional Information

1. Closing inventory as at 30 April was valued at sh.2,400,000.
2. Interest on loans had not been paid.
3. Sales include credit sales of $\mathrm{Sh} \cdot 600,000$ in respect of two items sold on the basis of confirmation by the customers. The items had cost Sh. 100,000 each. As at 30 April 2006, the customers had not confirmed whether they would buy the goods.
4. On 1 November 2005, the terms of th epartnership agreement were changed. The new terms provided for:

- Profit sharing ratio of 5:3:2 for Askili, Busara and Chema respectively.
- Interest on capital at $5 \%$ per annum.
- Salaries of Sh.10,000 per month to Busara and Chema.

For the purpose of the change, goodwill was valued at Sh.1,200,000 and was to be written off immediately while the land buildings were valued at Sh.2,000,000 and Sh.6,400,000 respectively.

## Required:

a) Trading, Profit and loss and appropriation accounts for the year ended 30 April 2006 (6 marks)
b) Partners' capital and current accounts (6 marks)
c) Balance sheet as at 30 April 2006 (4 marks)

## (Total: 20 marks)

QUESTION FIVE:
(a) Briefly explain why the following parties may be interested in the financial statements of an organisation:

| (i) Employees | $(2$ marks $)$ |
| :--- | :--- |
| (ii) Financial analysis | $(2$ marks |
| (iii) The Government. | $(2$ marks $)$ |
| (iv) The public. | $(2$ marks $)$ |

(b) State any two circumstances that may hinder a firm from improving on the usefulness of its financial statements.
(4 marks)
(c) Dickson Kimula is an electronic equipment dealer. He has sought your advice on certain matters relating to his financial statements for the year ended 30 April 2006.

Citing the relevant accounting principle, advise Dickson Kimula how to deal with each of the following:
(i) All his electrical equipment is sold with a one year warranty for repair and service, which on average costs Sh. 480 per item. The value of equipment returned annually average $1 \%$ of the sales. The sales of the year ended 30 April 2006 were 200,000units. (2 marks)
(ii) Closing stock as at 30 April 2006 was valued at Sh.500,000. However, some items of stock whose initial cost was Sh. 200,000 can only realise Sh.150,000 after major repairs costing Sh.40,000
(2 marks)
(iii) Sales for the year include deposits from customers amounting to Sh.2,000,000. The goods had not been delivered to the customers as at 30 April 2006 (2 marks)
(iv) The firms' VAT returns for the month of April 2006 had not been filed with the Revenue Authority. The penalty for late filing of VAT returns is Sh.10,000. (2 marks)
(Total: 20 marks)

## FINANCIAL ACCOUNTING I

DECEMBER 2014
Time allowed: 3 hours

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

## QUESTION ONE

Mr. Hassan Baraka retired from employment on 1 October 2005 and was paid terminal benefits of Sh. 3,000,000 He utilized Sh. 2,500,000 in purchasing business premises and deposited the balance in a new business account at Faida Bank Ltd."

Mr. Baraka did not maintain proper books of account. However, he kept files of statements from suppliers, cheque counter foils and unpaid invoices for purchases made. He also maintained a note book in which he recorded sales to customers who had credit accounts and settled their accounts by cheque. Cash collected from sales was banked at the end of each week after payment of certain expenses. Mr. Baraka also maintained some petty cash for office use. Mr. Baraka estimates to have paid the following business expenses from his personal bank account.

$$
\text { Sh. }{ }^{\prime} 000 \text { ' }
$$

Rent and rates for additional apace 100
Lighting expenses 50
Stationery and postage expenses
26

An analysis of the bank statements for the year ended 30 September 2006 was as follows:

| Receipts | Sh.'000' |  | Payments |
| :--- | ---: | :--- | :---: |
| Account opening | 500 | Petty cash withdrawn | Sh.'000' |
| Weekly bankings | 3,769 | Fixtures and fittings | 30 |
| Cheques from customers | 382 | Suppliers for goods | 3,728 |
| Cash refunded by a supplier | 10 | Insurance for inventory | 40 |
|  |  | Bank charges | 110 |
|  |  | Balance carried down | 463 |
|  | 4,661 |  | 4,661 |

## Additional information:

1. Baraka estimates that during the year ended 30 September 2006, he utilized cash collected from sales for the following purposes:

## Sh.'000'

Wages payment
Sundry expenses payment
Drawings
600
2 Cheques received from credit customers amounting to Sh .30 , 000 had not been credited by the bank as at 30 September 2006.

3 Insurance paid for inventory during the year include Sh. 20,000 relating to premium for the year ending 30 September 2007.
4 Petty cash balance as at 30 September 2006 was Sh. 15,000 which included a post dated cheque of Sh. 5,000 drawn by Mr. Baraka's friend in exchange for cash advanced from petty cash.
5 Credit customers owed Sh. 172,000 as at 30 September 2006.
6 As at 30 September 2006, the following were due on accounts payable:

## Sh. „000"

| Suppliers | 403 |
| :--- | :---: |
| Wages | 10 |
| Sundry expenses | 6 |

7 Depreciation is to provided on a straight-line basis at the following rates:
Business premises $2 \%$
Fixtures and fittings $10 \%$
8 The value of inventory as at 30 September 2006 was Sh. 360,000.

## Required:

(a) Trading, profit and loss account for the year ended 30 September 2006. (12 Marks)
(b) Balance sheet as at 30 September 2006.

## QUESTION TWO

Auto Transmitters Ltd. is a medium-size factory in Nairobi Industrial Area which manufactures transmitters. The following trial balance was extracted from the books of the company as at 31 December 2005.

|  | Sh. | Sh. <br> Ordinary share capital <br> Preference share capital |
| :--- | :--- | :--- |
| 2,000,000 |  |  |
| Profit and loss account (1 January 2005) |  | 424,750 |
| Freehold land and building (land Sh.400,000) | $1,700,000$ |  |
| Plant and machinery at cost | $7,300,000$ |  |
| Office equipment at cost | $1,100,000$ |  |
| Motor vehicles at cost | $2,000,000$ |  |


| Accumulated depreciation (1 January 2005): |  |  |
| :---: | :---: | :---: |
| Plant and machinery |  | 2,245,000 |
| Office equipment |  | 245,00e |
| Motor vehicles |  | 800,000 |
| Accounts receivable and payable | 5,000,000 | 3,562,260 |
| Provision for bad and doubtful debts |  | 10,000 |
| Manufacturing wages | 5,014,000 |  |
| Stock at cost (1 January 2005): |  |  |
| Raw materials | 700,000 |  |
| Work-in-progress | 1,260,000 |  |
| Finished goods | 2,500,000 |  |
| Distribution costs | 850,130 |  |
| Returns inwards | 151,060 |  |
| Purchase of raw materials | 5,186,000 |  |
| Sales |  | 26,001,470 |
| Balance at bank |  | 600,200 |
| Directors salaries | 601,140 |  |
| Maintenance of plant and machinery | 301,020 |  |
| Rent | 400,630 |  |
| Advertising | 1,900,480 |  |
| Rates | 501,710 |  |
| Insurance | 201,160 |  |
| Office salaries | 1,660,130 |  |
| Electricity | 460,270 |  |
| Factory lightning | 300,140 |  |
| Bank interest | 70,700 |  |
| Interim preference dividend paid | 100,000 |  |
| General administration expenses | 630,110 |  |
|  | 39,888,680 | 39,888,680 |

## Additional information:

1 Depreciation is to be provided as follows:

- Plant and machinery at $15 \%$ on cost.
- Office equipment at $10 \%$ on cost.
- Motor vehicles at $25 \%$ on written down value.
- Building (erected during the year) at $2 \%$ on straight-line basis.

2 Prepaid rates as at 31 December 2005 were sh.31,400.

3 An insurance premium for public liability cover in the sum of sh.33,520 was paid for a period of one year to 31 march 2006. The amount owing for electricity and rent as at 31 December 2005 was sh. 12,140 and sh. 23,210 respectively.

4 Rent, rates, electricity and insurance expenses are to be apportioned in the ratio, $5 / 6$ to the factory and $1 / 6$ to office expenses.

5 A provision for bad and doubtful debts at $1 \%$ of the debtors is to be made.

6 The share capital (authorized and fully paid) as at 31 December 2005 was as follows:

- 800,000 ordinary shares of shares of sh.5. Each"
- 200,000 10\%preference'shares of sh. 10 each"

A provision for the final preference dividend and a dividend of sh. 2.25 per ordinary shares is to be made.
7 Office salaries include Sh. 642,370 paid to salesmen while director's salaries include sh. 200,000 paid to the production director.
8 Corporation tax of sh. $1,000,000$ is to be provided for.
$9 \quad 1,500$ transmitters were completed and transferred to the warehouse at a transfer price of Sh. 10,000 per transmitter.
10 The value of stocks as at 31 December 2005 were as follows:

## Sh.

- Raw materials at cost

562,000

- Work -in-progress at cost
- Finished goods at transfer price

471,900
1,000,000 (100 transmitters)
(Notes that owing to a change in accounting policy, the closing stock of finished goods were valued at transfer price during the year ended 31 December 2005)

## Required:

Manufacturing, trading and profit and loss account for the year ended 31 December 2005"

## QUESTION THREE

Grace and Beatrice were operating a retail business sharing profits and losses in the ratio of $2: 1$ respectively up to 31 March 2006 when they admitted Catherine to the partnership. The paremers allowed payment of interest on partners' fixed capital accounts but did not allow for interest on partners' current accounts.

The following balances were extracted from the partnership's book of account as at 30 September 2006:


## Additional information:

1 On 31 March 2006 when Catherine was admitted as a partner, the profit sharing ratio changed to Grace $2 / 5$, Beatrice $2 / 5$ and Catherine $1 / 5$. For the purpose of admission, goodwill was valued at Sh. 12,000,000 and was written off the books immediately. On 1 April 2006, Catherine paid Sh.5,000,000 which comprised her fixed capital of sh.1,500,000 and her current account contribution of sh.3,500,000."

2 The partners also agreed that any apportionment of gross profit was to be made on the basis of sales. The apportionment of expenses, unless otherwise indicated, were to be on time basis.
3 On 30September 2006, stock was valued at Sh.5,100,000.
4 Provision was to be made for depreciation on motor vehicles and shop fittings at the rate of $20 \%$ and $5 \%$ per annum respectively, based on cost.

5 Salaries included the following partners drawings during the year:

| Grace | - | Sh. 600,000 |
| :--- | :--- | :--- |
| Beatrice | - | Sh. 480,000 |
| Catherine | - | "Sh. $250,000 "$ |

6 At 30 September 2006, rates paid in advance amounted to sh. 260,000 while electricity accrued amounted to sh. 60,000 .

7 A difference in the books of sh. 120,000 that had been written off to general expenses as at 30 September 2006 was later found to have been due to the following errors:

- Sales returns of sh. 180,000 had been debited to sales but was omitted from the customers account.
- The purchase journal had been undercast by sh.200,000.

8 Doubtful debts (for which full provision was required) as at 31 March 2006 amounted to Sh. 120,000 and sh. 160,000 as at 30 September 2006.

9 Professional charges included sh. 200,000 paid in respect to the acquisition of leasehold premises. These fees are to be capitalized as part of the lease, the total cost of which was to be depreciated in 25 equal annual installments. Other premises owned by Beatrice were leased to the partnership at Sh. 600,000 per annum but no rent had been paid or credited to her for the year to 30 September 2006.

## Required:

(a) Income statement for the year ended 30 September 2006. (10 Marks)
(b) Balance sheet as at 30 September 2006. (6 Marks)
(c) Partners' current accounts. (4 Marks)
(Total:20 Marks)

## QUESSTION FOUR

(a) Outline the extent to which a trial balance is an indicator of correct book-keeping by an entity.
(4 Marks)
(b) After preparation of the trial balance or Bakari Brothers Enterprises as at 31 September 2005, the firm"s accountant has been provided with the following additional informationfor the purpose of preparation of the final accounts:

1 Due to an oversight, discount has been allowed to a credit customer on the gross • invoiced amount of Sh. 80,000 at the rate $10 \%$. The firm should have used a rate if $6 \%$.

2 Electricity accrued amounts to Sh. 36,710 while insurance premiums of Sh. 22,450 have been prepaid.

3 In October 2005, the employees of the firm received a general salary increase, backdated to 1 July 2005. Amounts totalling Sh.126,550 in salary arrears are payabre to former employees who left shortly before the salary award was announced and who have not yet been traced. It has been decided that the salary packets will be opened and the cash banked until the ex-employees are traced.

4 Wages due to casuals amounting to Sh. 464,120 for services rendered in the last week of December 2005 were paid in January 2006 together with the salaries for the month of December 2005 which amounted to Sh.301,700.

5 During the year, the exterior of the warehouse was repaired and repainted at a cost of Sh.500,000. This"
amount was erroneously debited to office premises account. It is policy of Bakari Brothers Enterprises to provide for depreciation on the closing balances of non-current assets and this has already been done. The annual rate of depreciation on office premises is $2 \%$ calculated on the straight-line basis.

6 In December 2005 2005, Bakari Brothers Enterprises had bought goods on credit from CB Ltd. for Sh. 452,100 and has also sold goods on credit to the same company for Sh.163,040. These amounts were correctly posted to their respective accounts. However, these accounts are to be offset as at 31 December 2005 and the remaining balance settled by cheque in January 2006.

7 The provision for discounts allowed to debtors, which at present has a balance of Sh.229,530 needs to be reduced to Sh. 157,400.

8 Debts totaling Sh.64,800 are irrecoverable and should be written off. However, amount of Sh. 21,440
written off as a bad debt in the previous year has now been recovered in full but the cheque in settlement has not been banked or posted in the accounts.

## Required:

Journal entries, including narrations, necessary to record the above transactions in the books of
Bakari Bothers
Enterprises.
(16 Marks)

## (Total: 20 Marks)

## QUESTION FIVE

(a) Define the following ratios:
(i) Return on capital employed (ROCE)
(ii) Return on owners' equity (ROOE)
(iii) Leverage ratio
(iv) Inventory turnover
(v) Earnings per share (EPS)
(1 Mark)
(1 Mark)
(1 Mark)
(1 Mark)
(b) The information below relates to KC Investments Ltd, a company that sells computer accessories for the year ended 31 October 2005 and 31 October 2006. The industry average has also been provided.

| Industry average As at 31 October | $\mathbf{2 0 0 5}$ | $\mathbf{2 0 0 6}$ | $\mathbf{2 0 0 6}$ |
| :--- | :--- | :--- | :--- |
| Return on capital employed (before tax) | $19 \%$ | $19 \%$ | $19 \%$ |
| Return on owners' equity (before tax) | $24 \%$ | $21 \%$ | $16 \%$ |
| Gross profit margin | $23 \%$ | $25 \%$ | $20 \%$ |
| Net profit margin | $14 \%$ | $12 \%$ | $9 \%$ |
| Leverage | $45 \%$ | $51 \%$ | $65 \%$ |
| Accounts receivable collection period | 32 days | 26 days 29 days |  |
| Accounts payable payment period | 63 days | 42 days 42 days |  |
| Inventory turnover | 68 days | 72 days 72 days |  |

## Required:

From the shareholders perspective, comment on the ratios for KC Investments Ltd in relation to the industry average ratios.
(15 marks)
(Total: 20 Marks)

## Answers - Past Papers

## SUGGESTED SOLUTIONS TO THE PAST PAPER QUESTIONS

JULY 2008

## QUESTION ONE

a)

Suspense account

|  | Shs |  | Shs |
| :--- | ---: | :--- | ---: |
| Share capital (W3) | 100,000 | B/f | 200,000 |
| Share premium (N5) | 60,000 | Sales a/c (N1) | 20,000 |
| Disposal (proceeds) (N4) | $\underline{80,000}$ | Sales Returns (N2) | $\underline{20,000}$ |
|  | $\underline{240,000}$ | $\underline{240,000}$ |  |

## WORKINGS

Note 1
Sales $=2,000,000-20,000=1,980,000$
Note 2
Sales Returns $=40,000+20,000 \div$ Sh 60,000
Note 3
Share capital
B/f Shs 200,000
Additional issue

| $5,000 \times 20$ | $\underline{100,000}$ |
| :--- | :--- |
| Total c/f | $\underline{300,000}$ |

Share premium $=5,000 \times 12$

$$
=\text { Shs } 60,000
$$

Note 4
DR: Disposal $\}$ at cost
CR: Assets $\quad\}$
DR: Prov a/c $\quad\}$ accumulated depreciation
CR: Disposal a/c \}
DR: Bank a/c $\}$ sales proceeds
CR: Disposal a/c \}
Adjustment for disposal $=1,000,000-200,000=800,000$
Disposal account

|  | Shs |  |
| :--- | :--- | ---: |
| Plant | 200,000 | Prov a/c |


| P \& L | $\underline{80,000}$ |
| :--- | :--- |
|  | Suspense $\quad \frac{80,000}{\underline{280,000}}$ |

## ZACH LTD

TRADING, PROFIT \& LOSS ACCOUNT FOR THE YEAR ENDED 31 DEC 99

|  | Shs | Shs |
| :---: | :---: | :---: |
| Sales ( $\mathrm{N}-\mathrm{I}$ ) |  | 1,980,000 |
| Returns inwards |  | 60,000 |
|  |  | 1,920,000 |
| Less cost of sales |  |  |
| Opening stock | 300,000 |  |
| Purchases (net) | 1,140,000 |  |
|  | 1,440,000 |  |
| Stock | $(360,000)$ | (1,080,000) |
| Gross profit |  | 840,000 |
| Profit on disposal |  | 80,000 |
| Decrease in provisions for bad debts |  | 1,000 |
|  |  | 921,000 |
| Less expenses |  |  |
| Depreciation - Plant | 8,000 |  |
| - Building | 16,000 |  |
| Admin expenses | 155,000 |  |
| Debenture interest | 6,000 |  |
| Selling expenses | 140,000 |  |
| Operating expenses | 180,000 |  |
| Bad debts | 20,000 | 651,000 |
| Profit before tax |  | 270,000 |
| Less taxation |  | (90,000) |
| Profit after tax |  | 180,000 |
| Add retained profit b/d |  | 380,000 |
|  |  | 560,000 |
| To general reserves | 20,000 |  |
| Proposed dividend (ordinary) | 3,000 | 50,000 |
| Bal (retained) c/f |  | 510,000 |

Note 5
Depreciation of plant
$10 / 100 \times 800,000=80,000$

## Provision for depreciation

|  | Shs |  | Shs |
| :--- | ---: | ---: | ---: |
| Disposal a/c | 200,000 | Bal b/f | 400,000 |
| Bal c/d | $\underline{280,000}$ | $\mathrm{P} \& \mathrm{~L}$ | $\underline{80,000}$ |
|  | $\underline{480,000}$ | $\underline{480,000}$ |  |

## Depreciation of buildings

Provision b/f 40,000

| Current @ $2 \%$ | $\underline{16,000}$ |
| :--- | :---: |
| Accumulation | $\underline{56,000}$ |
| Debtor"s adjustments |  |
|  | Shs |
| Bal b/f | 400,000 |
| w/off | $\underline{20,000}$ |
|  | $\underline{380,000}$ |
| Provision b/f | $\underline{20,000}$ |
| Provision c/f @ 5\% | $\underline{19,000}$ |
| Decrease (P \& L) | $\underline{1,000}$ |

## Administration expenses (Rates a/c)

|  | Shs |  | Shs |
| :--- | ---: | ---: | ---: |
| Recorded | 140,000 | P \& L | 155,000 |
| Bank | $\underline{30,000}$ | Prepaid c/d | $\underline{170,000}$ |

Debenture interest:
Owing $=10 / 100 \times 600,000=\operatorname{Sh} 60,000$
ZACK LTD
BALANCE SHEET
AS AT 31 DEC 1999

|  | SHS | SHS | SHS |
| :---: | :---: | :---: | :---: |
|  | COST | DEPR | NET |
| NON CURRENT ASSETS |  |  |  |
| Buildings | 800,000 | 56,000 | 744,000 |
| Plants | 800,000 | 280,000 | 520,000 |
|  | 1,600,000 | 336,000 | 1,264,000 |
| CURRENT ASSETS |  |  |  |
| Stocks |  | 360,000 |  |
| Debtors | 380,000 |  |  |
| Provision | $(19,000)$ | 361,000 |  |
| Prepaid rates |  | -15,000 | 736,000 |
| TOTAL ASSETS |  |  | $\underline{2,000,000}$ |
| EQUITY \& LIABILITIES |  |  |  |
| (i) Capital \& Reserves |  |  |  |
| Share capital |  |  | 300,000 |
| Reserves: |  |  |  |
| General reserve |  | 20,000 |  |
| Share premium |  | 60,000 |  |
| P \& La/c |  | 510,000 | 590,000 |
| Equity |  |  | 890,000 |
| (ii) Long term liabilities |  |  |  |
| Debentures |  |  | 600,000 |
|  |  |  | 1,490,000 |

## Workings

1. Loose tools

| Bal b/f | 288,000 |  |
| :--- | ---: | :--- |
| Additional | $\underline{192,000}$ |  |
|  | 480,000 |  |
| Bal b/f | $\underline{384,000}$ |  |
| Depreciation | $\underline{96,000}$ | P \& L A/c |

2. Depreciation

|  | Plant \& machinery | Vans |
| :--- | ---: | :---: |
| Prov b/f | $1,680,000$ | 672,000 |
| Current | $\underline{696,000}$ | $\underline{240,000}$ |
| Accumulated depreciation | $\underline{2,376,000}$ | $\underline{912,000}$ |

3. Electricity and power

$$
1,440,000+192,000=1,632,000
$$

4. Prepaid expenses

Bal b/f
Selling \& Distribution expenses Rates

Prepayment

| 344,000 | 384,000 |
| :--- | :--- |
| 2,520 | $\underline{13,800}$ |
| $\underline{341,480}$ | $\underline{370,200}$ |

5. Provision for Bad debts
$\begin{array}{lll}\text { Provision b/f } & & 240,000 \\ \text { Provision c/f } & 10 / 100 \times(1,984,000-26,000) & \underline{195,800} \\ & \underline{435,800}\end{array}$

Bad and doubtful debts a/c

|  | Shs |  | Shs |
| :--- | ---: | ---: | ---: |
| Debtors | 26,000 | Provision | 44,200 |
| P \& L | $\underline{18,200}$ |  | $\underline{44,200}$ |

QUESTION TWO

| WORKSHEET PERIOD ENDED 31 MARCH 2000 |  |  |  |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | TRIAL BAL |  | ADJUSTMENTS |  | ADJSTED T/BAL |  | P \& L A/C |  | BAL. SHEET |  |
|  | DR | CR | DR | CR | DR | CR | DR | CR | DR | CR |
|  | Shs"000 | $\begin{aligned} & \text { Shs"00 } \\ & 0 \\ & \hline \end{aligned}$ | Shs"000 | Shs"000 | Shs"000 | Shs"000 | Shs"000 | Shs"000 | Shs"000 | Shs"000 |
| Capital |  | 4896 |  |  |  | 4896 |  |  |  | 4896 |
| Land \& B | 3600 |  |  |  | 3600 |  |  |  | 3600 |  |
| Plant \& M. | 3480 |  |  |  | 3480 |  |  |  | 3480 |  |
| Dep - P \& M |  | 1680 |  | 696000 |  | 2376 |  |  |  | 2376 |
| Delivery van | 960 |  |  |  | 960 |  |  |  | 960 |  |
| Depr - van |  | 672 |  | 240000 |  | 912 |  |  |  | 912000 |
| Tools | 480 |  |  | 96000 | 384 |  |  |  |  |  |
| Stocks | 2232 |  |  |  | 2232 |  | 2232 |  |  |  |
| Purchase | 4440 |  |  | 2008 | 2432 |  | 2432 |  |  |  |
| Sales |  | 15840 |  |  |  | 15840 |  | 15840 |  |  |
| W \& S | 5288 |  |  |  | 5288 |  | 5288 |  |  |  |
| R \& Ins | 384 |  |  | 13800 | 370200 |  | 370200 |  |  |  |
| Repair \& Maint. |  |  |  |  |  |  |  |  |  |  |
|  | 240 |  |  |  | 240 |  | 240 |  |  |  |
| Sales ex | 344 |  |  | 2520 | 341480 |  | 341480 |  |  |  |
| Elec \& Power | 1440 |  | 192000 |  | 1632 |  | 1632 |  |  |  |
| Ind.T.L | 72 |  |  |  | 72 |  | 72 |  |  |  |
| Adm ex | 672 |  |  |  | 672 |  | 672 |  |  |  |
| Prov - d\&d |  | 240 | 44200 |  |  | 195800 |  |  |  | 195800 |
| Debtors | 1984 |  |  | 26000 | 1958000 |  |  |  | 1958000 |  |
| Creditors |  | 1928 |  |  |  | 1928 |  |  |  | 1928 |


| Drawings | 480 |  |  |  | 480 |  |  |  | 480000 |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Bank |  | 864 |  |  |  |  | 864 |  |  | 864000 |
| Cash(hand) | 24 |  |  |  | 24 |  |  |  | 24000 |  |
|  | 26120 | 26120 |  |  |  |  |  |  |  |  |
| DEPRN |  |  |  |  |  |  |  |  |  |  |
| P \& M |  |  | 696000 |  | 696000 |  | 696000 |  |  |  |
| Vans |  |  | 24000 |  | 240000 |  | 240000 |  |  |  |
| Tools |  |  | 96000 |  | 96000 |  | 96000 |  |  |  |
| Acc. Exp |  |  |  | 192000 |  | 192000 |  |  |  | 192000 |
| Prepaid ex |  |  |  |  |  |  |  |  |  |  |
| Selling |  |  | 2520 |  | 2520 |  |  |  | 2520 |  |
| Rates |  |  | 13800 |  | 13800 |  |  |  | 13800 |  |
| B \& d. debts |  |  |  | 44200 |  |  |  |  |  |  |
| Stock (Closing) |  |  | 2008 |  | 2008 |  |  |  | 2008 |  |
| Bad debts (w/off) |  |  | 26000 |  |  | 18200 | 26000 | 44200 |  |  |
|  |  |  |  |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |  |  |  |
|  |  |  | 3318520 | 3318520 | 27222000 | 27222000 | 15884200 | 15884200 | 12910320 | 12910320 |

## QUESTION THREE

(a)

KAMAU, KIMANI \& KAMATA PARTNERSHIP
PROFIT \& LOSS \& APPROPRIATION ACCOUNT FOR THE YEAR ENDED

| Net profit | Shs. $\mathbf{0 0 0}$ | Shs. $\mathbf{0 0 0}$ |
| :--- | ---: | ---: |
| Salary (W1) |  | 55,155 |
| Kimani | 5,500 |  |
| Kimata | 4,500 |  |
| Interest on Capital (W2) | 560 |  |
| Kamau | 395 |  |
| Kimani | 450 |  |
| Kimata |  |  |
| Share of profit (W3) | 2,500 |  |
| Kamau | 12,500 |  |
| Kimani | 6,250 |  |
| Kimata |  | $\underline{55,155}$ |
|  |  | - |

b. (i)

Current account

| Bal b/d | Kamau | Kimani | Kimata | Bal b/d <br> Interest on capital Share of profit | Kamau | Kimani | Kimata |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | ,000 | ,000 | ,000 |  | ,000 | ,000 | ,000 |
|  |  | 300 | 8,250 |  | 3,200 |  | 450 |
| Drawings | 23,705 | 19,525 |  |  | 560 | 395 |  |
| Bal c/d |  |  |  | Bal c/d | 25,000 | $\begin{array}{r}12,500 \\ 1,430 \\ \hline\end{array}$ | 6,250 |
|  | 5,055 | - | 2,950 |  |  |  |  |
|  | $\underline{28,760}$ | 19,825 | 11,200 |  | $\underline{28,760}$ | 19,825 | 11,200 |

(ii)

| Capital account |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Goodwill w/off | Kamau | Kimani | Kimata | Bal b/d | Kamau | Kimani | Kimata |
|  | 8,000 | 4,000 | 2,000 |  | 16,000 | 10,000 |  |
|  |  |  |  | Cash <br> Goodwill |  |  | 12,000 |
| Bal c/d | 16,400 | 11,600 | 10,000 | w/off | 8,400 | 5,600 |  |
|  | 24,400 | 15,600 | 12,000 |  | 24,400 | 15,600 | 12,000 |

C.

KAMAU, KIMANI \& KIMATA
BALANCE SHEET
AS AT

NON CURRENT ASSETS
Premises
Equipment

## CURRENT ASSETS

Stock
Debtors
Cash
TOTAL ASSETS
EQUITY \& LIABILITIES
CAPITAL \& RESERVES
Capital : Kamau

| Cost | Acc deprn | Net book value |
| :---: | :---: | :---: |
| ,000 | ,000 | ,000 |
| 8,000 | 5,600 | $\begin{array}{r} 20,800 \\ 2,400 \\ \hline 23,200 \end{array}$ |
|  | $\begin{array}{r}12,555 \\ 3,500 \\ 8,800 \\ \hline\end{array}$ | $\begin{aligned} & \underline{24,855} \\ & \underline{48,055} \end{aligned}$ |
|  |  |  |
|  |  | $\begin{array}{r} 5,055 \\ (14,300) \\ 2,950 \\ 3,480 \\ \hline \underline{48,055} \\ \hline \end{array}$ |

## WORKINGS

W1
(a) Salary to $1^{\text {st }}$ April (3 months)

Kimani - 4,000,000 $\times \frac{3}{12}=1,000,000$
(b) From $1^{\text {st }}$ April to $31^{\text {st }}$ Dec 1999 (9 months)

$$
\begin{aligned}
6,000,000 \times \frac{9}{12} & =4,500,000 \\
\text { Total salary } & =1,000,000+4,500,000 \\
& =5,500,000
\end{aligned}
$$

Kimata - For 9 months

$$
-6,000,000 \times \frac{9}{12}=4,500,000
$$

W2
Interest on Capital
(a) Kamau

$$
\begin{aligned}
& 3 \text { months }=\frac{3}{12} \times \frac{5}{100} \times 16,000,000= \\
& 9 \text { months }=\frac{9}{12} \times \frac{6}{100} \times(16,000,000-8,000,000)= \\
& \text { TOTAL }
\end{aligned}
$$

(b) Kimani

$$
\begin{aligned}
& 3 \text { months }=\frac{3}{12} \times \frac{5}{100} \times 10,000,000= \\
& 9 \text { months }=\frac{9}{12} \times \frac{125,000}{100} \times(10,000,000-4,000,000)= \\
& \text { TOTAL }
\end{aligned}
$$

(c) Kimata

$$
9 \text { months }=\frac{9}{12} \times \frac{6}{100} \times(12,000,000-2,000,000)=450,000
$$

W3
Share of profit

$$
\begin{aligned}
& \text { Kamau }=\frac{4}{7} \times 43,750,000=25,000,000 \\
& \text { Kimani }=\frac{2}{7} \times 43,750,000=12,500,000 \\
& \text { Kimata }=\frac{1}{7} \times 43,750,000=6,250,000
\end{aligned}
$$

W4
Goodwill a/c

|  | SHS"O00 |  | SHS"000 |
| :--- | ---: | :--- | ---: |
| Capital accounts |  | Capital accounts | 8,000 |
| Kamau | 8,400 | Kamau | 4,000 |
| Kimani | 5,600 | Kimani | $\underline{2,000}$ |
|  | $\underline{14,000}$ | Kimata | $\underline{14,000}$ |

W5
DEPRECIATION ON EQUIPMENT
Lifespan is usually 10 years

$$
\begin{aligned}
\text { Depreciation } & =\frac{\text { Cost of equipment }}{\text { Lifespan }} \\
& =\frac{8,000,000}{10} \\
& =800,000
\end{aligned}
$$

## QUESTION FOUR

## JOYCE NJERI

TRADING, PROFIT \& LOSS ACCOUNT FOR THE YEAR ENDED 31 MARCH 2000


## JOYCE NJERI

BALANCE SHEET
AS AT $31{ }^{\text {ST }}$ MARCH 2000

|  | Sh"000 | Sin'000 |
| :---: | :---: | :---: |
| Assets |  |  |
| Non current assets |  |  |
| Motor van: cost (W5) | 5,000 |  |
| depreciation (W5) | 1,000 |  |
| net book value |  | 4,000 |
| Current assets |  |  |
| Inventory (W4) | 600 |  |
| Receivables (W2) | 320 |  |
| Cash in hand (W1) | 39 |  |
|  |  | 959 |
| Total assets |  | 4,959 |
| Capital and liabilities |  |  |
| Proprietors capital |  |  |
| Balance at 31 March 1999 | 3,795 |  |
| Profit for the year | 3,000 |  |
| Less drawings (W7) | $(2,570)$ |  |
| Balance as at 31 March 2000 |  | 4,225 |
| Current liabilities |  |  |
| Bank overdraft (W1) | 474 |  |
| Bank interest (presumably not paid until 1 April) | 27 |  |
| Payables (W3) | 233 |  |
|  |  |  |
| Total capital and liabilities |  | 4,959 |

## Workings

1. 

| Cashbook |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | $\begin{array}{r} \text { Cash } \\ \text { Sh" } 000 \end{array}$ | $\begin{gathered} \text { Bank } \\ \text { Sh"00 } \end{gathered}$ |  | $\begin{array}{r} \text { Cash } \\ \text { Sh" } 000 \end{array}$ | $\begin{aligned} & \hline \text { Bank } \\ & \text { Sh" } 00 \end{aligned}$ |
| Balance b/d | 55 | 2,800 | Drawings ( $52 \times 50,000$ ) | 2,600 |  |
| Cash takings banked |  |  | Petrol (52 x 10,000) | 520 |  |
| (contra entry) |  | 7,521 | Sundry expenses | 24 |  |
| Cheques banked |  | 1,500 | Repairs to canopy | 201 |  |
| Dividend income: |  |  | Taking banked (contra |  |  |
| drawings |  | 210 | Entry) | 7,521 |  |
| Cash takings (balancing |  |  | Purchase of van |  | 3,200 |
| Figures) | 10,850 |  | Road fund licence |  | 80 |
|  |  |  | Insurance on van |  | 323 |
|  |  |  | Payables |  | 7,777 |
|  |  |  | Rent |  | 970 |
|  |  |  | Sundry |  | 31 |
|  |  |  | Accounting work |  | 75 |
|  |  |  | Bank interest |  | 20 |
|  |  |  | Returned cheque: bad debt |  | 29 |
| Balance c/d (overdraft) |  | 474 | Balance c/d | 39 |  |
|  | 10,905 | 12,505 |  | 10,905 | 12,505 |
| Balance b/d | 39 |  | Balance b/d |  | 474 |

## Trade Receivables

|  | Shs $^{\text {"1000 }}$ |  | Shs |
| :--- | ---: | :--- | ---: |
| Balance $\mathrm{b} / \mathrm{d}$ | 170 | Cash | 1,500 |
| Credit sales (balancing figure) | $\underline{1,650}$ | Balance c/d | $\underline{320}$ |
|  | $\underline{1,820}$ | $\underline{1,820}$ |  |
|  |  |  |  |

3
Trade payables

| Trade payables |  |  |  |
| :--- | ---: | ---: | ---: |
|  | $\mathbf{S h}^{\text {"000 }}$ |  | $\mathbf{S h}^{\text {"0000 }}$ |
| Bank | 7,777 | Balance b/d | 230 |
| Balance c/d | $\underline{233}$ | Purchases (balancing figure) | $\underline{7,780}$ |
|  | $\underline{8,010}$ | $\underline{8,010}$ |  |

Goods taken as withdrawals on account of profit are as follows:

## Sh"000

| Selling price | $(100 \%)$ | 300 |
| :--- | :--- | :--- |
| Gross profit | $(40 \%)$ | $\underline{120}$ |
| Cost | $(60 \%)$ | $\underline{180}$ |

Therefore, purchases taken to the trading account $=$ Sh. $7,780,000-\operatorname{Sh} 180,000=\operatorname{Sh} 7,600,000$
4 Closing stock

Sales Sh"000 (10,850 + 1,650)
Gross profit
Cost of goods sold
Opening inventory
Purchases (W3)

Cost of goods sold
Closing inventory (balancing figure)

## Sh"000

12,500
(100\%)
$\begin{array}{ll}(40 \%) & \underline{5,000} \\ (60 \%) & \underline{7,500}\end{array}$
(60\%)
7,500

5 New van

The bank statement shows that the cash paid for the new van was Sh 3,200,000. Since there was a part exchange of Sh 1,800,000 on the old van, the cost of the new van must be Sh $5,000,000$ with first year depreciation ( $20 \%$ ) Sh $1,000,000$

6
Disposal of van

| Disposal of van |  |  |  |
| :--- | ---: | ---: | ---: |
| Van at cost | $\mathbf{S h}^{\prime \prime} \mathbf{0 0 0}$ |  | $\mathbf{S h}^{\prime \prime} \mathbf{0 0 0}$ |
| Profit on disposal | 3,000 | Provn for depreciation at date of sale | 2,500 |
|  | $\underline{1,300}$ | Asset a/c (trade in value for new van) | $\underline{1,800}$ |
|  | $\underline{4,300}$ |  | $\underline{4,300}$ |

7. 

| Drawings |  |  |  |
| :--- | ---: | ---: | ---: |
|  | Sh"000 $^{\text {"0 }}$ |  | $\mathbf{S h}^{\text {"N00 }}$ |
| Cash | 2,600 | Dividend income | 210 |
| Inventory (glasses taken (W3) | $\underline{180}$ | Capital a/c | $\underline{2,570}$ |
|  | $\underline{2,780}$ | $\underline{2,780}$ |  |

Since there are no investments in the business balance sheet, the dividend income must be separate from the business. However, since it is paid into the business bank account, it should be accounted for, in effect, as reduction in drawings.

## QUESTION FIVE

## Explanation of accounting concepts

I) Going Concern Concept

This is the assumption underlying the preparation of Accounts in that the firm is assumed to be continuing in operation to the foreseeable future.
It is further assumed the firm has neither the intention for the need to liquidate or reduce significantly the scale of its operations. If a firm is a going concern then the accounts should be prepared by use of Historical cost concept when valuing the assets.
This concept should not be used if:
i) If the business is going to close down in the near future.
ii) Where shortage of cash makes it almost certain that the firm will not go on.
iii) Where a large portion of the co. will be closed down due to shortage of cash.
II) The Business Entity Concept

The concept implies that the affairs of a business are to be treated as being separate from the non business activities of its owners.
The only time the activities of the owners are to affect the activities of the business is when he has injected capital into the firm.
The effects of this is that the income and expense of the firm are not mixed with those of the proprietor and as such even reporting is totally different and done in different books.
This ensures that the performance of the company is well know to avoid any collapse due to a lack of accountability.
III) Materiality

Information is said to be material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements. It depends on the size of the particular item judged in a particular circumstance. It provides a cut-off point which a co. can use to decide which items are to be disclosed in its financial statements.
IV) Realisation

This is part of the prudence concept.
It holds that profit and gains can only be taken into account when realization has occurred and that realization occurs only when the ultimate cash realized is capable of being determined with reasonable certainty.

Examples of this are:

- Goods or services are provided for the buyer
- The buyer accepts liability to pay the goods or services
- The monetary value of the goods or services has been established. Etc

It should be noted that under the realization concept the worst scenario is assumed to avoid the company disclosing information which could subsequently found to be misleading to parties who usually deal with the business.
b) Examples of instances where two accounting concepts could clash or there be inconsistency and how such inconsistency would be resolved.

## Prudence Vs. Realisation

When calculating the profit of an organization the amount of sales used is both the credit and the cash sales. This would seem to be a contradiction of the prudence concept, since we are not sure that the credit sales will actually be realized.
However, the realization concept is to the extent that you should recognize incomes when it is reasonably certain that they will be realized.
As such in this case the prudence concept will override the realization concept.

## Consistency Vs. Prudence

The consistency concept is to the extent that various items in the financial statements should be treated in the same way in various accounting periods. These thus means if a valuation of stock is done in historical cost, then that should be the standard method of use for several years after. However, according to the prudence concept, if the stocks net realizable value is less than its historical cost then the net realizable value should be used instead of the Historical cost.

## Prudence Vs. Substance over Form

In a situation where we are purchasing some goods on hire purchase and the goods have not been fully paid for. The true state of the goods is that we do not own them as they are recorded in law in the names of the purchase vendor.
This would pose a conflict where prudence dictates that the item should not be recorded in our books since we do not seem to be of the opinion that it should be recorded as it represents the substance of the transaction.
In such a case the substance over form concept would override and as such the item would be recorded in our books.

## DECEMBER 2008

## QUESTION ONE

a) i) To retain funds within the firm so that it can finance the acquisition of non current assets or major expansions.
ii) The company may not have sufficient cash to pay out dividends.
iii) To increase its capital base and improve it's liquidity position.
b) Wamu Traders Ltd

Trading Profit and Loss Account for the year ended 30 September

|  | Sh. | Sh. | Sh. |
| :---: | :---: | :---: | :---: |
| Sales |  |  | 4,800,000.00 |
| Less cost of sales |  |  |  |
| Opening stock |  | 420,000.00 |  |
| Purchases | 4,220,000.00 |  |  |
| Less returns out | (80,000.00) | 4,140,000.00 |  |
|  |  | 4,560,000.00 |  |
| Less closing stock |  | (560,000.00) | (4,000,000.00) |
| Gross Profit |  |  | 800,000.00 |
| Add Discount received |  |  | 13,000.00 |
| Less Provision for doubtful debts |  |  | 2,000.00 |
| Less Expenses |  |  | 815,000.00 |
| Loan Interest |  | 6,000.00 |  |
| Bad Debts |  | 14,000.00 |  |
| Discount allowed |  | 5,000.00 |  |
| Depreciation Buildings |  | 10,000.00 |  |
| Fixtures and fittings |  | 64,000.00 |  |
| Establishment expenses |  | 126,000.00 |  |
| Administration expenses |  | 63,000.00 |  |
| Selling and distribution expenses |  | 167,000.00 | (455,000.00) |
| Net Profit |  |  | 360,000.00 |
| Less: Dividends : Pref |  | 8,000.00 |  |
| Ordinary |  | 60,000.00 | (68,000.00) |
| Retained Profits for year |  |  | 292,000.00 |
| Retained Profits b/f |  |  | 362,000.00 |
| Retained Profits c/f |  |  | 654,000.00 |

## Wamu Traders Ltd

Balance Sheet as at 30 September 2000

| Non current Assets | Sh. | Sh. | Sh. |
| :---: | :---: | :---: | :---: |
| Buildings | 500,000.00 | (60,000.00) | 440,000.00 |
| Fixtures and fittings | 640,000.00 | (320,000.00) | 320,000.00 |
|  | 1,140,000.00 | (380,000.00) | 760,000.00 |
| Goodwill |  |  | 160,000.00 |
| Current Assets |  |  |  |
| Stock |  | 560,000.00 |  |
| Debtors | 320,000.00 |  |  |
| Less Provision | $(16,000.00)$ | 304,000.00 |  |
| Prepayments |  | 4,000.00 |  |
|  |  | 868,000.00 |  |
| Current Liabilities |  |  |  |
| Bank Overdraft | 25,000.00 |  |  |
| Creditors | 148,000.00 |  |  |
| Accruals | 7,000.00 |  |  |
| Loan interest payable | 6,000.00 |  |  |
| Dividends Payable | 68,000.00 | (254,000.00) | 614,000.00 |
|  |  |  | 1,534,000.00 |
| Financed by: |  |  |  |
| Share Capital |  |  |  |
| Ordinary shares of sh. 20 each fully paid | 600,000.00 |  |  |
| fully paid |  |  |  |
|  |  |  | 700,000.00 |
| Capital Reserves |  |  |  |
| Share Premium Account |  |  | 80,000.00 |
| Revenue reserves |  |  |  |
| Retained Profits Carried forward |  |  | 654,000.00 |
|  |  |  | 1,434,000.00 |
| Non Current liabilities |  |  |  |
| 6\% loan stock |  |  | 100,000.00 |
|  |  |  | 1,534,000.00 |

## Workings

The question is again fairly straightforward as the final accounts items can be picked from the balances given.

1 Depreciation
Buildings $(500,000 \times 2 \%)=10,000$
Fixtures $(640,000 \times 10 \%)=640,000$
2 Provision for doubtful debts

| Debtor balance | $330,000.00$ |
| :--- | :---: |
| Less Bade Debts | $(10,000.00)$ |
| Balance | $320,000.00$ Provision at $5 \% 16,000.00$ |

## QUESTION TWO

a) i)Helps us check on profitability of the firm.
ii) Facilitates comparison of a company's performance over time and with other companies.
iii) Enables us to assess the liquidity of the firm.
iv) Assess how efficiently a firm is using it's resources.
v) Measure the value of the firm.
b)
i) Current ratio
1999
2000
Current Assets

| $1,095,000.00$ <br> $645,000.00$ | $\frac{1,350,000.00}{1,140,000.00}$ |
| ---: | ---: |
| 1.697674419 | 1.184210526 |

- Quick ratio

Current Assets - Stock $1,095,000.00-645,000.00$ 1,350,000.00-825,000.00
Current Liabilities

| $645,000.00$ | $1,140,000.00$ |
| ---: | :--- |
| 0.697674419 | 0.460526316 |

- Gross Profit margin

| Gross Profit | $\frac{1,350,000.00}{3,000,000.00}$ | $\frac{2,100,000.00}{4,800,000.00}$ |
| :--- | ---: | ---: |
| Sales | $45.00 \%$ | $43.75 \%$ |

- Net Profit Margin

$$
\begin{array}{r}
\underline{637,500.00} \\
3,000,000.00
\end{array} \frac{1,237,500.00}{4,800,000.00}
$$

Net Profit before tax
Sales
$21.25 \%$
25.78\%

- Return on investments
(ROTA)
Net Profit before tax
637,500.00 $\quad 1,237,500.00$
Total Assets

$$
\begin{array}{rr}
2,295,000.00 & 3,075,000.00 \\
27.78 \% & 40.24 \%
\end{array}
$$

- Return on Capital employed

| Net Profit before tax | $\underline{637,500.00}$ | $1,237,500.00$ |
| :--- | ---: | ---: |
| Shareholders fund + Debt | $1,650,000.00$ | $1,935,000.00$ |
|  | $38.64 \%$ | $63.95 \%$ |

ii) The liquidity position of Munyah limited has declined as shown by both the Current ratio and quick ratio. The current ratio has declined from 1.6976 to 1.184. The
increase in current liabilities was more than the increase in current assets. The position is also confirmed by the change from the cash position to overdraft.

The profitability of the firm has improved as reflected by the net profit margin, return on investment and return on capital employed. Although the gross profit margin has declined slightly by $1 \%$ to $44 \%$, the net profit has increased from $21 \%$ to $26 \%$ this may be due to the managements ability to control operational costs.

## QUESTION THREE

a) Literary and Philosophical society

Bar and restaurant trading A/C for the year ended 30 September 2000

|  | Sh. | Sh. | Sh. |
| :---: | :---: | :---: | :---: |
| Sales |  |  |  |
| Bar |  |  | $\begin{aligned} & 4,032,000.00 \\ & 3,642,000.00 \\ & \hline \end{aligned}$ |
| Restaurant |  |  |  |
|  |  | 7,674,000.00 |  |
| Less cost of sales |  |  |  |
| Opening Stock |  | 473,600.00 |  |
| Purchases |  |  |  |
| Food | 1,565,800.00 |  |  |
| Bar | 2,885,000.00 | 4,450,800.00 |  |
|  | 4,924,400.00 |  |  |
| Less closing stock - Bar | (642,800.00) | (4,281,600.00) |  |
| Gross Profit |  | 3,392,400.00 |  |
| Less expenses |  |  |  |
| Wages: Restaurant |  | 1,600,000.00 |  |
| Bar |  | 800,000.00 | (2,400,000.00) |
| Net Profit to Income and expenditure Account |  |  | 992,400.00 |

b) Literary and Philosophical society Income and expenditure account for the year ended 30 September 2000

| Income | Sh | Sh |
| :--- | ---: | ---: |
| Bar and restaurant |  | $992,400.00$ |
| Subscriptions |  | $1,450,800.00$ |
| Donations | $108,000.00$ |  |
| Rental of rooms | $495,000.00$ |  |
| Interest from deposit account |  | $\underline{100,000.00}$ |
|  |  | $3,146,200.00$ |
| Expenditure |  |  |
| Depreciation Furniture \& Fittings |  |  |
|  |  |  |
| Lecturers fees |  |  |
| Lecturers travel and accommodation | $194,000.00$ |  |
| Camera and Projector repairs | $920,000.00$ |  |
| Rates and water | $358,000.00$ |  |
| Lighting and Heating | $17,000.00$ |  |
| Wages - Caretaker | $27,000.00$ |  |
| Loan Interest | $367,200.00$ |  |
| Subscriptions written off | $880,000.00$ |  |
| Surplus | $64,000.00$ |  |
|  |  | $43,600.00$ |
|  |  | $\underline{(3,139,800.00)}$ |

c) Literary and Philosophical society

Balance Sheet as at 30 September 2000

| Non Current Assets | Sh | Sh | Sh |
| :---: | :---: | :---: | :---: |
| Land and Buildings | 3,700,000.00 | - | 3,700,000.00 |
| Furniture \& Fittings | 1,874,000.00 | (478,000.00) | 1,396,000.00 |
| Equipment | 190,400.00 | $(73,400.00)$ | 117,000.00 |
|  | 5,764,400.00 | $(551,400.00)$ | 5,213,000.00 |
| Current Assets |  |  |  |
| Stock |  | 642,800.00 |  |
| Debtors - Subscriptions |  | 18,400.00 |  |
| Deposit at bank |  | 1,000,000.00 |  |
| Balance at bank |  | 724,800.00 |  |
|  |  | 2,386,000.00 |  |
| Current Liabilities |  |  |  |
| Creditors |  | (221,400.00) | $\underline{2,164,600.00}$ |
|  |  | 7,377,600.00 |  |
| Accumulated fund b/f |  |  | 5,771,200.00 |
| Add Surplus |  |  | 6,400.00 |
|  |  |  | 5,777,600.00 |
| Non Current Liabilities |  |  |  |
| Loan |  |  | 1,600,000.00 |
|  |  |  | 7,377,600.00 |

## QUESTION FOUR

a) Nzioka

Statement of affairs as at 1 November 1999

Assets
Stock
Debtors
Rates Prepaid
Fixtures
Liabilities
Accrued expenses
Creditors
Accrued lighting and heating
Loan
Bank
Loan interest
Assets - Liabilities
Capital

Sh.
Sh.
900,000.00
560,000.00
8,000.00
560,000.00
2,028,000.00
$(1,464,400.00)$
563,600.00
563,600.00

## Nzioka <br> Trading Profit and Loss Account for the year ended 31 October 2000

|  | Sh. | Sh. |
| :---: | :---: | :---: |
| Sales |  | 7,835,200.00 |
| Less: Cost of sales |  |  |
| Opening Stock | 900,000.00 |  |
| Purchases | 6,284,000.00 |  |
|  | 7,184,000.00 |  |
| Closing Stock | (1,160,000.00) | (6,032,000.00) |
| Gross Profit |  | 1,811,200.00 |
| Add Discounts received |  | 96,000.00 |
|  |  | 1,907,200.00 |
| Less Expenses |  |  |
| Rent and rates | 93,000.00 |  |
| Depreciation - Fixtures | 70,000.00 |  |
| Lighting and heating | 40,000.00 |  |
| General expenses | 150,000.00 |  |
| Loan interest | 24,000.00 |  |
| Bad Debts | 40,000.00 |  |
| Discount allowed | 104,000.00 |  |
| Wages | 590,000.00 |  |
| Sundry expenses | 28,000.00 | (1,139,000.00) |
| Net profit |  | $\underline{768,200.00}$ |

## Nzioka

Balance sheet as at 31 October 2000
Non Current Assets
Fixtures
Sh Sh
510,000.00
Current assets

| Stock |  | $1,160,000.00$ |  |
| :--- | ---: | ---: | :--- |
| Debtors | $600,000.00$ |  |  |
| Prepaid expenses |  | $10,000.00$ |  |
| Bank | $134,600.00$ |  |  |
| in hand |  | $4,000.00$ |  |
| Current Liabilities |  | $1,908,600.00$ |  |
| Creditors |  |  |  |
| Accrued expenses | $\underline{480,000.000 .00}$ | $\underline{(498,000.00)}$ | $\underline{1,410,600.00}$ |
|  |  |  | $\underline{1,920,600.00}$ |


| Capital b/f | $563,600.00$ |
| :--- | ---: |
| Add net profit | $\underline{768,200.00}$ |
| Less drawings | $1,331,800.00$ |
|  | $\underline{(211,200.00)}$ |
|  | $1,120,600.00$ |
| Loan | $\underline{800,000.00}$ |
|  | $\underline{2,920,600.00}$ |

## Cash in hand

|  |  | Sh. | Wages |
| :--- | ---: | :--- | ---: |

Accruals c/f
38,000.00
150,000.00
5 Amount banked from cash Credits on bank statement Less cheques dishonoured by bank now banked

Payments to creditors
Amount per bank statement
Unpresented cheques b/f
Add unpresented cheques $\mathrm{c} / \mathrm{f}$
7 Bank:
Balance as per bank statement 198,600.00
Less unpresented cheques $\quad \underline{64,000.00}$
Balance as per cashbook
262,600.00
8 Accrued expenses
General expenses
Lighting and heating
38,000.00
Loan interest (3 months)

14,000.00
6,000.00
58,000.00

## QUESTION FIVE

a) A provision is an amount written off or retained by charging it in the profit and loss account i.e. writing off by way of providing for depreciation or reduction in value of assets. A provision is retained by way of providing for any known liability of which the amount cannot be ascertained accurately.

A liability is an amount owing which is accurately known. Therefore the difference between a provision and a liability will be based on the accuracy of the amount. Rent owing at the end of the financial year would normally be known with precision thus it would be a liability. Legal charges for a court case for which the lawyers have not yet submitted their bill would be a provision.

A reserve is an amount set aside from the profits (from the profit and loss appropriation account). A reserve may also arise fro events out of the profit and loss account (e.g. for capital reserves we have share premium). Normally the reserves are set aside for specific purpose as sometimes it may not be necessary to distribute all the profits of the company to shareholders. E.g. revenue reserves may be used to pay out bonus shares, share premium may be used to write off preliminary expenses and so on.
b) A provision is normally charged in the profit and loss account and reduced from the relevant asset e.g. a provision for doubtful debt is deducted from the debtors figure as shown in the balance sheet.

A liability depending on whether it is current or non-current liability will be shown under the relevant headings in the balance sheet e.g. the creditors will be shown under current liabilities and Debenture will be shown under non-current liabilities.

A reserve is normally shown under it's relevant headings in the balance sheet together with the other shareholders funds. E.g. Share premium is shown under capital reserves apdo General reserves is shown under revenue reserves.

JUNE 2009

## QUESTION ONE

## Atieno, Babu, Chesire and Dagana

Trading, Profit and Loss Appropriation Account for the year ended 31 March 2001

|  |  | Sh | Sh |
| :---: | :---: | :---: | :---: |
| Sales |  |  | 5,975,000.00 |
| Less returns inwards |  |  | (61,000.00) |
|  |  |  | 5,914,000.00 |
| Less Cost of sales |  |  |  |
| Opening Stock |  | 465,000.00 |  |
| Add : Purchases |  | 3,380,000.00 |  |
| Less Drawings |  | (185,000.00) |  |
|  |  | (75,000.00) |  |
| Closing stock |  | (560,000.00) | (3,025,000.00) |
|  |  |  | 2,889,000.00 |
| Less: Expenses |  |  |  |
| Depreciation: Furniture \& Fittings |  | 35,000.00 |  |
| Motor Vehicles |  | 76,000.00 |  |
| Salaries and wages |  | 319,000.00 |  |
| Telephone and Postage |  | 130,000.00 |  |
| Rates |  | 112,000.00 |  |
| Insurance and Subscriptions |  | 157,000.00 |  |
| Vehicle running expenses |  | 396,000.00 |  |
| General expenses |  | 72,000.00 |  |
| Bank Charges and interest |  | 124,000.00 |  |
| Bad debts |  |  | 68,000.00 |
|  |  |  | (1,489,000.00) |
| Net Profit |  |  | 1,400,000.00 |
| Less Salary : Dagana |  |  | - (240,000.00) |
| Balance of Profit shared in Profit Sharing ratio |  |  | (1,160,000.00) |
| Atieno 4 |  | 464,000.00 |  |
| Babu | 3 | 348,000.00 |  |
| Chesire | 2 | 232,000.00 |  |
| Dagana | 1 | 116,000.00 | (1,160,000.00) |
|  |  |  | NIL |

Capital Account

|  | Atieno | $\begin{gathered} \hline \text { Babu } \\ \text { Sh. } \end{gathered}$ | Chesire Sh. | $\begin{array}{r} \text { Dagana } \\ \text { Sh. } \end{array}$ | Bal b/d Goodwill Curr. a/c | Atieno Sh. | $\begin{gathered} \hline \text { Babu } \\ \text { Sh. } \end{gathered}$ | Chesire Sh. | $\begin{gathered} \hline \text { Dagana } \\ \text { Sh. } \end{gathered}$ |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Goodwill | 187,895 | 161,053 | 107,368 | 53,684 |  | 700,000 | 600,000 | 400,000 |  |
| w/o | 22,105 | 18,947 | 12,632 |  |  | 210,000 | 180,000 | 120,000 |  |
| Cash | 700,000 | 600,000 | 400,000 | 200,000 |  |  |  |  | 253,684 |
| Bal. c/d | 910,000 | 780,000 | 520,000 | $\underline{253,684}$ |  | $\underline{910,000}$ | $\underline{780,000}$ | $\underline{520,000}$ | $\underline{253,684}$ |

Current Account

|  | Atieno Sh. | $\begin{gathered} \hline \text { Babu } \\ \text { Sh. } \end{gathered}$ | Chesire Sh | $\begin{array}{r} \hline \text { Dagana } \\ \mathrm{Sh} . \end{array}$ | Bal.b/d <br> Cash <br> Salaries <br> Prof.shared | $\begin{array}{r} \hline \text { Atieno } \\ \mathrm{Sh} . \end{array}$ | $\begin{array}{r} \hline \text { Babu } \\ \text { Sh. } \end{array}$ | Chesire Sh. | $\begin{array}{r} \text { Dagana } \\ \mathrm{Sh} . \end{array}$ |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Drawings | 250,000 | 260,000 | 250,000 | 175,000 |  | 350,000 | 325,000 | 195,000 |  |
| Capital |  |  |  | 253,684 |  |  |  |  | 376,500 |
| Goods |  |  |  | 185,000 |  |  |  |  | 240,000 |
| Bal. c/d | 564,000 | 413,000 | 177,000 | 118,816 |  | 464,000 | 348,000 | 232,000 | 116,000 |
|  | 814,000 | 673,000 | 427,000 | 732,500 |  | 814,000 | 673,000 | 427,000 | 732,500 |

Atieno, Babu, Chesire and Dagana
Balance Sheet as at 31 March

| Non current Assets | , $\mathbf{0 0 0}$ | , $\mathbf{0 0 0}$ | , $\mathbf{0 0 0}$ |
| :--- | ---: | ---: | ---: |
| Land and buildings | $2,000,000.00$ | - | $2,000,000.00$ |
| Furniture \& Fittings | $500,000.00$ | $(185,000.00)$ | $315,000.00$ |
| Motor Vehicles | $\underline{860,000.00}$ | $\underline{(556,000.00)}$ | $\underline{304,000.00}$ |
|  | $\underline{3,360,000.00}$ | $\underline{(741,000.00)}$ | $2,619,000.00$ |

## Current Assets

| Stock | $560,000.00$ |  |
| :--- | ---: | ---: |
| Debtors | $365,000.00$ |  |
| Prepayments | $30,000.00$ |  |
| Bank | $436,316.00$ |  |
| Hand | $\underline{24,000.00}$ |  |
|  | $1,415,316.00$ | $\underline{1,415,316.00}$ |
| TOTAL ASSETS |  | $\underline{4,034,316.00}$ |

CAPITAL \& RESERVES

| Capital Accounts | Atieno |  | $700,000.00$ |
| :--- | :---: | ---: | ---: |
|  | Babu |  | $600,000.00$ |
|  | Chesire |  | $400,000.00$ |
|  | Dagana |  | $1,900,000.00$ |
| Current Accounts | Atieno | $564,000.00$ |  |
|  | Babu | $413,000.00$ |  |
|  | Chesire | $177,000.00$ |  |
|  | Dagana | $\underline{118,816.00}$ | $\underline{1,272,816.00}$ |
| Current Liabilities |  |  | $\underline{3,172,816.00}$ |
| Creditors |  | $823,500.00$ |  |
| Accruals | $38,000.00$ | $\underline{(861,500.00}$ |  |
|  |  |  | $\underline{4,034,316.00}$ |

## Workings

| Purchases (as per trial balance) | $3,380,000.00$ |
| :--- | :---: |
| Less goods taken by Dagana | $\underline{(185,000.00)}$ |
|  | $\underline{3,195,000.00}$ |

Depreciation:
$($ Furniture and fittings $10 \% \mathrm{X}(500,000-150,000))=\quad \underline{35,000.00}$

| (Motor vehicles $20 \% \mathrm{X}(860,000-480,000))=$ | $\underline{76,000.00}$ |
| :--- | :---: |
| Salaries and wages ( as per trial balance ) | $295,000.00$ |
| Accruals | $\underline{24,000.00}$ |
|  | $\underline{319,000.00}$ |
| Telephone and Postage (as per trial balance) | $116,000.00$ |
| Accruals | $\underline{130,000.00}$ |
|  | $\underline{137,000.00}$ |
| Rates (as per trial balance) | $\underline{(25,000.00})$ |
| Prepayments | $\underline{112,000.00}$ |
|  | $162,000.00$ |
| Insurance and subscriptions (as per trial balance) | $\underline{(5,000.00)}$ |
| Prepayments | $\underline{157,000.00}$ |

## Notes

1) The goodwill is passed through the current account as the partners are to withdraw cash paid in for the goodwill. The cash withdrawn by the partners is included in the drawings figure shown in the trial balance.

## QUESTION TWO

a) i) Share Premium: A share premium arises when a company issues shares at a price that is more than the par value. The share Premium may be applied in:

- Paying un issued shares.
- Writing off preliminary expenses.
ii) Rights issue

A rights issue is an option on the part of the shareholder given by the company to existing shareholders at a price lower than the market price. It involves selling ordinary shares to existing shareholders of the company on a prorata basis. When the rights are issued the shareholders have 3 options available.

- Buy the new shares and exercise their rights.
- Sell the rights in the market,
- Ignore the rights.

A rights issue therefore gives the shareholder the right(but not an obligation ) to buy the new shares issued by the company.
b)

| Application and Allotment |  |  |  |
| :--- | ---: | :--- | ---: |
|  | Sh. |  | Sh. |
| OSC | $300,000.00$ | Bank | $300,000.00$ |
| Share Premium | $100,000.00$ | Bank | $150,000.00$ |
| Cashbook | $\underline{50,000.00}$ |  | $\underline{450,000.00}$ |

First and final Call

Share Premium Account $\quad \underline{\underline{112,000.00}}$

## Workings

1) Cash received on application $(6,000 \times 50)=300,000.00$
2) Application Account

$$
\begin{array}{lll}
- \text { Entry to Ordinary share capital Application }-(4,000 \mathrm{X} \text { sh } 50)= & 200,000.00 \\
- \text { Entry to Ordinary share capital Allotment }-(4,000 \mathrm{X} \text { sh } 25)= & \underline{100,000.00} \\
& \underline{\underline{300,000.00}}
\end{array}
$$

- Entry to Share Premium Account - Allotment (4,000 X sh. 25) $=100,000.00$

3) Shares refunded ( $1,000 \mathrm{X}$ sh. 50 ) $50,000.00$
4) Cash received on allotment

Receivable ( $4,000 \mathrm{X}$ sh 50 )
Less Excess received on application (1,000 X sh 50$)$ 150,000.00 150,000.00
5) First and Final Call

Entry on Ordinary Share Capital (4,000 X sh. 25) 100,000.00
6) Cash received on First and final Call ( $3,800 \mathrm{X}$ sh 25 )

Calls in arrears (200 X sh.25)
7) Transfer from Ordinary share capital to forfeited shares A/C
(200 X sh. 100 par)
From Share premium to forfeited shares ( 200 X sh. 25) 5,000.00
95,000.00
5,000.00

## QUESTION THREE

a) Kimeu

Profit and Loss Account for the year ended 31 March 2001

|  | Shs | Shs |
| :--- | ---: | ---: |
| Income |  | $6,178,000.00$ |
| Sales Credit |  | $\underline{726,000.00}$ |
| Cash |  | $6,904,000.00$ |
|  | $1,960,000.00$ | $(1,802,000.00)$ |
| Purchases | $\underline{158,000.00)}$ | $5,102,000.00$ |
| Closing stock |  |  |
|  |  |  |
| Less Expenses | $720,000.00$ |  |
| Salary | $280,000.00$ |  |
| Elec bills | $182,000.00$ |  |
| Motor expenses | $306,900.00$ |  |
| General exp | $120,000.00$ |  |
| Insurance | $45,000.00$ |  |
| Interest on Loan | $220,000.00$ |  |
| Depreciation-MV | $192,000.00$ |  |
| Depreciation-Eq | $27,000.00$ |  |
| Rates | $17,000.00$ |  |
| Bad debts | $55,000.00$ | $\underline{(2,164,900.00)}$ |
| Accountancy Fee |  | $\underline{2,937,100.00}$ |
| Net profit |  |  |

b) Mutiso Mwema

Balance Sheet as at 31 December 1990

| Fixed Assets | Shs | Shs | Shs |
| :--- | ---: | ---: | ---: |
| Equipment | $960,000.00$ | 192,000 | $768,000.00$ |
| Motor Vehicle | $\underline{660,000.00}$ | $\underline{220,000}$ | $\underline{440,000.00}$ |
| Current Assets | $\underline{1,620,000.00}$ | $\underline{412,000}$ | $1,208,000.00$ |
| Stocks | $158,000.00$ |  |  |
| Debtors | $1,081,000.00$ |  |  |
| Prepayments | $40,000.00$ |  |  |
| Cash at bank | $2,532,000.00$ |  |  |
| Cash in Hand | $\underline{30,100.00}$ | $\underline{5,049,100.00}$ |  |
|  | $\underline{3,841,100.00}$ |  |  |
| TOTAL ASSETS |  | $\underline{1,860,000.00}$ |  |
| EQUITY AND LIABILITIES |  | $\underline{2,929,100.00}$ |  |
| Capital and Reserves |  | $\underline{1,789,100.00}$ |  |
| Capital |  | $3,754,000.00)$ |  |
| Opening balance |  | $\underline{400,000.00}$ |  |
| Add : Net Profit |  |  |  |
| Less Drawings |  |  |  |
| Loan |  | $\underline{5,049,100.00}$ |  |

## Workings

## Capital

|  | Sh. |  | Sh. |
| ---: | ---: | :--- | ---: |
| Balance c/d | $\underline{1,860,000.00}$ | Bank | Motor vehicles |

## Bank

|  | Sh. |  | Sh. |
| :--- | ---: | :--- | :---: |
| Capital | $1,200,000.00$ | Salary | $720,000.00$ |
| Loan | $400,000.00$ | Drawings | $936,000.00$ |
| Debtors | $5,080,000.00$ | Purchases | $1,960,000.00$ |
| Cash banked | $560,000.00$ | Equipment | $960,000.00$ |
|  |  | Elec bills | $240,000.00$ |
|  |  | Motor expenses | $182,000.00$ |
|  |  | General exp | $270,000.00$ |
|  | Insurance | $160,000.00$ |  |
|  |  | Balance c/d | $\underline{1,812,000.00}$ |
|  | $\underline{7,240,000.00}$ |  | $\underline{7,240,000.00}$ |

Sales Ledger Control Account


## QUESTION FOUR

## a) Kaluwax Ltd

Manufacturing, trading and Profit and Loss Account for the year ended 30 April 2001

|  | Sh | Sh |
| :---: | :---: | :---: |
| Opening Stock of raw materials |  | 350,000.00 |
| Purchases of raw materials |  | 3,950,000.00 |
| Add Carriage inwards |  | 200,000.00 |
|  |  | 4,500,000.00 |
| Less closing stock of raw materials |  | (500,000.00) |
| Cost of raw materials consumed |  | 4,000,000.00 |
| Manufacturing wages |  | 3,000,000.00 |
| PRIME COST |  | 7,000,000.00 |
| Factory Overheads |  |  |
| Factory rent and rates | 1,400,000.00 |  |
| Factory Light, Heat and power | 655,000.00 |  |
| Depreciation of plant | 600,000.00 |  |
| Works manager salary | 245,000.00 |  |
| Plant repairs | 400,000.00 |  |
| Amortization of Lease on factory | $\underline{200,000.00}$ | 3,500,000.00 |
| Factory cost of production |  | 10,500,000.00 |
| Add opening work in Progress |  | 1,800,000.00 |
|  |  | 12,300,000.00 |
| Less Closing Work in Progress |  | (2,300,000.00) |
| Cost of goods produced |  | 10,000,000.00 |
| Sales |  | 18,000,000.00 |
| Less cost of sales |  |  |
| Opening stock of finished goods | 3,500,000.00 |  |
| Cost of goods produced | $\underline{10,000,000.00}$ |  |
|  | 13,500,000.00 |  |
| Less closing stock of finished goods | (1,500,000.00) | (12,000,000.00) |
| Gross Profit |  | 6,000,000.00 |
| Administrative overheads |  | (1,800,000.00) |
| Net Profit |  | 4,200,000.00 |

KALUWAX LTD

## BALANCE SHEET

AS AT 30 ${ }^{\text {TH }}$ APRIL 2001

|  | Shs $^{\text {"0000 }}$ | Shs"000 | Shs"000 |
| :--- | ---: | ---: | ---: |
| NON CURRENT ASSETS |  |  |  |
| Factory lease | $4,000,000$ | $1,400,000$ | $2,600,000$ |
| Plant | $\underline{6,000,000}$ | $\underline{3,400,000}$ | $\underline{2,600,000}$ |
|  | $\underline{10,000,000}$ | $\underline{4,800,000}$ | $5,200,000$ |
| CURRENT ASSETS |  |  |  |
| Stock, raw materials |  | 500,000 |  |
| $\quad$ Work in progress |  | $2,300,000$ |  |
| $\quad$ Finished goods |  | $3,500,000$ |  |
| Debtors | $\underline{1,600,000}$ |  |  |
| Bank balance |  | $\underline{8,950,000}$ |  |
| TOTAL ASSETS |  |  | $\underline{14,150,000}$ |

EQUITY \& LIABILITIES
Capital \& Reserves

| Share capital | $7,500,000$ |  |
| :--- | :--- | :--- |
| Net profit | $\underline{4,200,000}$ | $11,700,000$ |

## CURRENT LIABILITIES

| Creditors | $\underline{2,450,000}$ |
| :--- | ---: |
| $14,150,000$ |  |

## Manufacturing Account Extract

Production cost
Add: $25 \%$ of Production cost $\quad$ (manufact

| Units produced $(10,000$ units) |  |
| ---: | :--- |
| Unit cost | $=12,500,000 \div$ |
|  | $=1,250$ |


\[\)| 10,000 |
| :--- |

\]

KALUWAX LTD
TRADING, PROFIT \& LOSS A/C

|  | Shs | Shs |
| :--- | ---: | ---: |
| Sales |  | $18,000,000$ |
| Less : Cost of sales | $4,375,000$ |  |
| Opening stock of finished goods $(3,800 \times 1,250)$ | $12,500,000$ |  |
| Add : Market value of goods completed | $\underline{(1,875,000)}$ | $\underline{(15,000,000)}$ |
| Less : Closing stock, finished goods $(1,500 \times 1,250)$ | $3,000,000$ |  |
| Gross profit | $\underline{2,000,000}$ |  |
| Add : Manufacturing profit | $5,500,000$ |  |
| Less : Expenses | $\underline{(1,800,000)}$ |  |
| Overhead administration | $3,700,000$ |  |
| Add : Opening stock figure prov for unrealised profit | 875,000 |  |
| Less: Closing stock figure for unrealised profit | $\underline{(375,000)}$ |  |
| Net profit | $\underline{4,200,000}$ |  |

## Workings

1 Working for closing stock in units

| Opening Stock | 3,500 |
| :--- | ---: |
| Manufactured | 10,000 |
|  | 13,500 |
| Less sold units | $-12,000$ |
| Closing Stock | 1,500 |

Cost Per Unit $(10,000,000 / 10,000) \quad 1,000.00$
Total cost (1,500 X Sh 1,000.00)
2 Unrealised Profit on closing stock (1,500,000.00 X 25\%) 375,000.00
Closing Stock of $1,875,000$ has a profit of ( $1,875,000-1,500,000$ ) Sh. 375,000 included which will be deducted from stock figure in the balance sheet.

## QUESTION FIVE

a) The amount should now be restated at Sh. 186,000 by debiting the Insurance recievable by Sh. $36,000.00$ and crediting the profit and loss account by the same. Under matching concept this is income which has now become certain (insurance is another debtor).
b) The loss of value on the equipment should be charged in the Profit and Loss account so that the equipment is shown in the books at Sh. 800,000 . The loss Sh.2,200,000 should be debited in the profit and loss account and credited to the provision for depreciation therefore getting a Net book value of Sh.800,000.
c) The company should mention the item by way of note but not provide for it in the accounts. Under International Accounting standard 37 Provisions, Contingent liabilities and Contingent Assets, this item is a possible contingent liability and the accounting treatment is to mention by way of note.
d)
e) Under International Accounting Standard No. 2 Inventories stock should be stated at the lower of cost and Net realisable value. The cost of these item is Sh.18,000. The net realisable value (Selling price less expenses to get unit to a saleable condition) is Sh.16,000. (Sh.19,000 - Sh.3,000)
f) Again International Accounting standard 37 Provisions, Contingent liabilities and Contingent Assets applies but in this case the company will treat the amount as follows:

This is a contingent liability classified as follows

| Probability | Amount | Treatment |
| :--- | :---: | :--- |
| $10 \%$ Probably | $1,000,400.00$ | Provide in the accounts |
| $30 \%$ Possible | $3,001,200.00$ | Mention by way of note |
| $60 \%$ Remote | $\underline{6,002,400.00}$ | ignore, do not mention. |
|  | $\underline{T O T A L}$ |  |

## DECEMBER 2009

## QUESTION ONE

| a)Freehold  <br> Landland \& bldgs Leasehold <br> Equipment and buildings  | Furniture | Total |
| :--- | :---: | :---: |


|  | Shs 000" Over 50 years |  | Shs „000" | Shs „000" | Under 50 years |
| :---: | :---: | :---: | :---: | :---: | :---: |
| Cost or Valuation | Shs „000" | Shs „000" |  |  | Shs „000" |
| Balance b/f | 157,000.00 | 121,800.00 | 60,200.00 | 150,800.00 | 489,800.00 |
| Additions | 7,600.00 | 3,800.00 |  | 1,800.00 | 13,200.00 |
| Reclassifications |  | $(7,500.00)$ | 7,500.00 |  |  |
| Disposals | (3,600.00) |  | (2,300.00) |  | (5,900.00) |
| Gains on | 6,000.00 |  |  |  | 6,000.00 |
| revaluation <br> Balance c/f | 167,000.00 | 118,100.00 | 65,400.00 | 152,600.00 | 503,100.00 |

Depreciation

| Balance b/f | - | - | 5,800.00 | 52,200.00 | 58,000.00 |
| :---: | :---: | :---: | :---: | :---: | :---: |
| Charge for the year |  | - | 2,650.00 | 14,800.00 | 17,450.00 |
| Eliminated on disposal | - - | - | (1,700.00) |  | $(1,700.00)$ |
| Balance c/f | - | - | 6,750.00 | 67,000.00 | 73,750.00 |
| NBV b/f | 157,000 | 121,800.00 | 60,200.00 | 150,800.00 | 489,800.00 |
| NBV c/f | 167,000.00 | 118,100.00 | 58,050.00 | 85,000.00 | 429,350.00 |

b) Nafuu Foods Ltd

Profit and Loss Account for the year ended 31 October 2001

Shs '000' Shs '000
408,950.00

## Add;

Profit on disposal
Add investment income
Less Expenses
Wages and Salaries
Operating expenses
Insurance
Directors Fees
Bad Debts Written off
Debenture Interest
Audit Fees
Depreciation expense
Net Profit Before tax
Tax : Current Year
Previous years under provisions
Profit After Tax
Less Dividends

| Interim Paid | $26,000.00$ |  |
| :--- | ---: | ---: |
| Final Proposed | $26,000.00$ | $\underline{(52,000.00)}$ |
| Retained Profit for year |  | $14,120.00$ |
| Retained Profit b/f | $\underline{77,600.00}$ |  |
| Retained Profit c/f | $\underline{91,720.00}$ |  |

c) Nafuu Foods Ltd

Balance Sheet as at 31 October 2001

| Non Current Assets | Sh ' $000{ }^{\prime}$ | Sh ' $000{ }^{\prime}$ | Sh ' $000{ }^{\prime}$ |
| :---: | :---: | :---: | :---: |
| Freehold Land \& Buil | 167,000.00 | - | 167,000.00 |
| Leasehold land \& B | 183,500.00 | (6,750.00) | 176,750.00 |
| Furniture \& Equipment | 152,600.00 | $(67,000.00)$ | 85,600.00 |
|  | 503,100.00 | (73,750.00) | 429,350.00 |
| Current Assets |  |  |  |
| Stock |  | 46,400.00 |  |
| Debtors |  | 63,860.00 |  |
| Prepayments |  | 720.00 |  |
| Investments (mkt value 10,500) |  | 9,800.00 |  |
| Bank |  | 4,320.00 |  |
|  |  | 125,100.00 |  |
| Current Liabilities |  |  |  |
| Bank Overdraft | 1,500.00 |  |  |
| Creditors | 61,520.00 |  |  |
| Accruals | 1,500.00 |  |  |
| Debenture Interest | 500.00 |  |  |
| Tax Payable | 27,310.00 |  |  |
| Proposed Dividends | $\underline{\mathbf{2 6 , 0 0 0 . 0 0}}$ | (118,330.00) | 6,770.00 |
|  |  |  | $\underline{436,120.00}$ |
| Financed by; |  |  |  |
| 5,200,00 ordinary shares of Sh. 20 |  |  | 104,000.00 |
| Capital Reserves |  |  |  |
| Share Premium |  | 18,000.00 |  |
| Revaluation reserve |  | 6,000.00 |  |
| Capital Redemption Reserve |  | 56,400.00 | 80,400.00 |
| Revenue Reserves |  |  |  |
| Profit and Loss Account |  |  | 91,720.00 |
| Shareholdersfunds |  |  | 276,120.00 |
| Debenture |  |  | 160,000.00 |
|  |  |  | 436,120.00 |

## QUESTION TWO

## Rotich Sinei and Tonui

Trading ,Profit and Loss and appropriation Account for the year ended 30 April 2001

| Sales | Sh. | Sh. | Sh. <br> 8,750,000.00 |
| :---: | :---: | :---: | :---: |
| Less cost of sales |  |  |  |
| Opening stocks |  | 1,200,000.00 |  |
| Purchases |  | 4,180,000.00 |  |
| Less Closing stock |  | 5,380,000.00 |  |
| Gross profit |  | (1,275,000.00) | (4,105,000.00) |
|  |  |  | 4,645,000.00 |
|  | 1.5.2000to 30.09.2000 | 1.11.2000 to 30.4.2001 |  |
|  | $(3,500 / 8,750 \times 4,645)$ | (5,250/8,750)x4,645 |  |
| Gross Profit | 1,858,000.00 | 2,787,000.00 | 4,645,000.00 |
| Salaries | 483,750.00 | 483,750.00 | 967,500.00 |
| Rent rates lighting and |  |  |  |
| heating | 137,500.00 | 137,500.00 | 275,000.00 |
| Wages | 275,000.00 | 275,000.00 | 550,000.00 |
| Accountancy and audit |  |  |  |
| fees | 52,500.00 | 52,500.00 | 105,000.00 |
| General expenses | 352,400.00 | 259,600.00 | 612,000.00 |
| Depreciation Motor vehicles | 160,000.00 | 160,000.00 | 320,000.00 |
| Shop fittings | 15,000.00 | 15,000.00 |  |
| Provision for doubtful debts | 30,000.00 | 10,000.00 | $\begin{aligned} & 30,000.00 \\ & 40,000.00 \\ & \hline \end{aligned}$ |
| Total expenses | 1,506,150.00 | 1,393,350.00 | $\underline{2,899,500.00}$ |
| Net Profit | 351,850.00 | 1,393,650.00 | 1,745,500.00 |

Less: Interest on Capital

| Green | $37,500.00$ | $37,500.00$ | $75,000.00$ |
| :--- | ---: | ---: | ---: |
| Blue | $25,000.00$ | $25,000.00$ | $50,000.00$ |
| Black |  | $\underline{6,250.00}$ | $\underline{0,250.00}$ |

Balance of profits shares in PSR

| Green | $289,350.00$ | $1,324,900.00$ | $1,614,250.00$ |
| :--- | :--- | ---: | ---: |
| Blue | $192,900.00$ | $529,960.00$ | $722,860.00$ |
| Black | $\underline{529,960.00}$ | $\underline{626,410.00}$ |  |
|  | $\underline{96,450.00}$ | $\underline{264,980.00}$ | $\underline{264,980.00}$ |


| Rotich, Sinei and Tonui |  |  |  |
| :---: | :---: | :---: | :---: |
| Balance Sheet as at 30 April 2001 |  |  |  |
| Fixed Assets | Sh | Sh | $\checkmark$ Sh |
| Leasehold Premises | 2,250,000.00 | - | 2,250,000.00 |
| Furniture and fittings | 300,000.00 | $(130,000.00)$ | 170,000.00 |
| Motor Vehicles | 1,600,000.00 | $(620,000.00)$ | 980,000.00 |
|  | 4,150,000.00 | (750,000.00) | 3,400,000.00 |
| Current Assets |  |  |  |
| Stocks |  | 1,275,000.00 |  |
| Debtors | 193,000.00 |  |  |
| Less Provision for doubtful debts | (40,000.00) | 153,000.00 |  |
| Prepayments |  | 50,000.00 |  |
| Cash at bank |  | 820,000.00 |  |
|  |  | 2,298,000.00 |  |
| Current Liabilities |  |  |  |
| Creditors | (1,085,000.00) | 1,213,000.00 |  |
|  |  | 4,613,000.00 |  |
| Capital Accounts |  |  |  |
| Green |  | 750,000.00 |  |
| Blue |  | 500,000.00 |  |
| Black |  | 375,000.00 | 1,625,000.00 |
| Current Accounts |  |  |  |
| Green |  | 1,847,860.00 |  |
| Blue |  | 656,410.00 |  |
| Black |  | 483,730.00 | 2,988,000.00 |
|  |  |  | 4,613,000.00 |

## QUESTION THREE

Current A/C

|  | Sh. | Sh. | Sh. |  | Sh. | Sh. | Sh. |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Goodwill | 1,200,000 | 1,200,000 | 600,000 | Bal b/f | 400,000 | 300,000 | 875,000 |
| Drawings | 150,000 | 120,000 | 62,500 | Interest recd. | 75,000 | 50,000 | 6,250 |
|  |  |  |  | Share of Prof. | 722,860 | 626,410 | 264,980 |
|  |  |  |  | Goodwill | 2,000,000 | 1,000,000 |  |
| Bal c/d | 1,847,860 | 656,410 | 483,730 |  |  |  |  |
|  | 3,197,860 | 1,976,410 | 1,146,230 |  | 3,197,860 | 1,976,410 | 1,146,230 |

b) Mamba Sports club

Bar Trading Profit and Loss Account for the year ended 31 March 2001

Sales
Less cost of sales
Opening Stock
Purchases

Less closing stock
Profit to income and expenditure

Sh.
Sh.
657,000.00

62,000.00
497,000.00
659,000.00
$(184,000.00) \quad(475,000.00)$
182,000.00

## Mamba Sports club <br> Income and expenditure Account for the year ended 31 March

| Incomes | Sh | Sh |
| :--- | ---: | ---: |
| Profit from trading |  | $182,000.00$ |
| Subscriptions |  | $2,465,000.00$ |
| Dinner dance |  | $723,000.00$ |
| Investments income |  | $400,000.00$ |
| Profit on sale of Investments |  | $\underline{125,000.00}$ |
|  |  | $895,000.00$ |
| Expenditure | $258,000.00$ |  |
| Salaries and wages | $124,000.00$ |  |
| Repairs and Maintenance | $415,000.00$ |  |
| Office expenses | $168,000.00$ |  |
| Printing and Stationary | $315,000.00$ |  |
| Dinner dance expenses | $25,000.00$ |  |
| Sports Prizes | $248,000.00$ |  |
| Transport | $251,000.00$ |  |
| Depreciation: Equipment | $24,000.00$ |  |
| ,Furniture \& Fittings | $\underline{51,000.00}$ | $\underline{(1,879,000.00)}$ |
| Subscription written off |  | $\underline{2,016,000.00}$ |
| Surplus |  |  |

## Mamba Sports club <br> Balance Sheet as at 31 March 2001

| Non Current Assets | Sh | Sh | Sh |
| :---: | :---: | :---: | :---: |
| Equipment |  |  | 1,004,000.00 |
| Furniture and fittings |  |  | 216,000.00 |
|  |  |  | 1,220,000.00 |
| Investments |  |  | 4,500,000.00 |
| Current Assets |  |  |  |
| Current Assets |  | 184,000.00 |  |
| Subscriptions in arrears |  | 375,000.00 |  |
| Cash at bank |  | 1,030,000.00 |  |
|  |  | 1,589,000.00 |  |
| Current Liabilities |  |  |  |
| Subscription in advance | 194,000.00 |  |  |
| Salaries accrued | 72,000.00 | (266,000.00) | 1,323,000.00 |
|  |  |  | 7,043,000.00 |
| Accumulated fund b/f |  |  | 5,027,000.00 |
| Add Surplus |  |  | 2,016,000.00 |
|  |  |  | 7,043,000.00 |

## Workings

Accumulated fund $b / f$

| Assets | Sh | Sh |
| :--- | ---: | ---: |
| Furniture and fittings |  | $240,000.00$ |
| Equipment |  | $690,000.00$ |
| Receipts and Payments |  | $388,000.00$ |
| Investments at cost |  | $300,000.00$ |
| Subscriptions in arrears |  | $162,000.00$ |
| Stock of beverages |  | $5,180,000.00$ |
|  |  |  |
| Liabilities | $\underline{85,000.00}$ |  |
| Subscriptions prepaid |  | $\underline{(153,000.00)}$ |
| Accrued salaries |  | $\underline{5,027,000.00}$ |


| Subscriptions |  |  |  |
| :--- | ---: | :--- | ---: |
| Balance b/f | Sh. |  | Sh. |
| Receipts and payments | $300,000.00$ | Balance b/f | $85,000.00$ |
| Income \& Expenditure (Bal fig.) | $45,000.00$ | Receipts \& Payments | $2,493,000.00$ |
| Balance c/f | $2,465,000.00$ | Income and Expenditure | $51,000.00$ |
|  | $\underline{3,004,000.00}$ | Balance c/f | $\underline{375,000.00}$ |
|  |  |  | $\underline{3,004,000.00}$ |

## QUESTION FOUR

a) A bank reconciliation explains the difference between balance at the bank as per cashbook and balance at bank as per the bank statement.
The functions are
i) To update the cashbook with transactions that have gone through the bank e.g. bank charges.
ii) to check and correct any errors in the cashbook,
iii) To Detect and prevent any frauds that relate to the cashbook and bank transactions.
b)

| Cashbook |  |  |  |  |  |  |
| :--- | ---: | :--- | ---: | :---: | :---: | :---: |
|  | Sh. |  |  |  |  | Sh. |
| Balance b/f | $2,366,500.00$ | Bank Charges | $3,000.00$ |  |  |  |
| Receipts | $26,500.00$ | Standing Order | $62,000.00$ |  |  |  |
| Overcast in Payment | $4,500.00$ | Overcast in opening bal; | $658,500.00$ |  |  |  |
|  |  | Dishonoured cheque | $15,000.00$ |  |  |  |
|  |  | Cheque paid by bank | $44,000.00$ |  |  |  |
|  |  | Balance c/d | $\underline{1,615,000.00}$ |  |  |  |
|  | $\underline{2,397,500.00}$ |  | $\underline{2,397,500.00}$ |  |  |  |

## Bank statement as at 30 June 2001

Balance as per cashbook

$$
\begin{array}{r}
1,615,000.00 \\
22,500.00 \\
1,637,500.00
\end{array}
$$

Add:
Unpresented cheques

Less Uncredited cheques
98,500.00
Error
832,500.00
(931,000.00)
Balance as per bank statement
706,500.00

## QUESTION FIVE

| Business entity | Meaning | Reason for use | Weakness |
| :---: | :---: | :---: | :---: |
|  | A business is regarded as a separate entity distinct from its owners or managers | When preparing accounts the true state of the business is shown as having it's own assets and liabilities | Practically it is difficult to distinguish the owners and the business |
| Historical cost | Resources are normally stated in accounts at the amount which the business paid to acquire them. | It tends to be a more easy and objective measure of the value of transactions and assets recorded at the cost when they occurred | It times of inflation it is unrealistic to state the value of assets at historical cost. Transactions are and liabilities in the accounts. |
| Monetary Principle | Accounts will only deal with those items to which monetary value can be attached. | The limits the element of subjectivity in accounts as those events that cannot be valued are avoided. | The overall performance of a business is not shown by the accounts e.g. quality of products or staff. |
| Matching or accrual concept | Revenue and costs are recognised as they are earned or incurred (not as money is received or paid) matched with one another and dealt with in the P \& L in the period in which they relate. | It is the central point of preparing the profit and loss account as the incomes will be matched with the relevant expenses. | The matching concept is often arbitrary as some expenses are matched with the income, they are often estimates e.g. depreciation. |
| Conservatism or prudence | Revenues andprofits are not anticipated but are recognised by inclusion in the $\mathrm{P} \& \mathrm{~L}$ account only when realised inform of cash or other assets. Provision is made for all known liabilities whether the amount is known with certainty or best estimate. | Due to uncertainties surrounding transactions and events in a firm, it will be important for accountants to be cautious in selecting policies so that incomes and assets are not overstated and liabilities are not understated. and | In practise it conflicts with many concepts e.g. matching. It introduces a lot of subjectivity in accounts. |

## MAY 2010

## QUESTION ONE

WANJI
ADJUSTED TRIAL BALANCE
AS AT 31 ${ }^{\text {ST }}$ DECEMBER 2001

|  | Shs | Shs |
| :---: | :---: | :---: |
| Fixed assets | 832,000 |  |
| Stock : opening stock | 148,000 |  |
| Trade debtors | 76,000 |  |
| Prepayments | 10,000 |  |
| Trade creditors |  | 34,600 |
| Bank overdraft |  | 15,200 |
| Accruals |  | 16,000 |
| Drawings | 359,600 |  |
| Capital |  | 1,054,000 |
| Sales |  | 1,043,200 |
| Provision for depreciation |  | 166,400 |
| Purchases | 733,000 |  |
| Operating expenses | 126,000 |  |
| Provision for doubtful debts |  | 3,800 |
| Discount received |  | 5,000 |
| Discount allowed | 5,800 |  |
| Suspense a/c | 47,800 |  |
|  | 2,338,200 | 2,338,200 |

JOURNAL ENTRIES TO CORRECT ERRORS

| 1. | Sales <br> Suspense a/c <br> To correct an overcast in the sales figure <br> NB: Narrations are not required | Dr Shs 25,700 | $\begin{gathered} \hline \mathbf{C r} \\ \text { Shs } \end{gathered}$ |
| :---: | :---: | :---: | :---: |
| 2(i) | Fixed assets Purchases | 40,000 | 40,000 |
| (ii) | P \& L: Depreciation for the year Provision for depreciation | 2,000 | 2,000 |
| 3 | Creditors Suspense a/c | 17,000 | 17,000 |
| 4 | Operating expenses <br> Telephone | 900 | 900 |
| 5. | Suspense a/c Debtors | 15,000 | 15,000 |
| 6 | Suspense a/c Discount allowed Discount received | 5,000 | $\begin{aligned} & 2,500 \\ & 2,500 \end{aligned}$ |
| 7 | Purchases a/c Suspense a/c | 28,000 | 28,000 |

## Suspense account

|  | Shs | Shs |  |
| :--- | ---: | :--- | ---: |
| Bal b/d | 47,800 | Sales | 25,700 |
| Telephone | 900 | Creditors | 17,000 |
| Debtors | 15,000 | Purchases | 28,000 |
| Discount allowed | 2,500 |  |  |
| Discount received | 2,500 | $\underline{70,700}$ |  |
| Balance c/d | $\underline{2,000}$ | $\underline{70,700}$ |  |

## Adjusted net profit

|  | Shs |
| :--- | ---: |
| Net profit | 85,800 |
|  |  |
| Adjustments | $(25,700)$ |
| Overcast sales | 40,000 |
| Overcasted purchases | $(2,000)$ |
| Depreciation | 900 |
| Telephone expenses overcast | $(2,500)$ |
| Discount allowed | 2,500 |
| Discount received | $\underline{(28,000)}$ |
| Purchases undercasted | $\underline{71,000}$ |
| Adjusted NET PROFIT |  |
|  |  |

a) Gross profit to sales ratio $=\underline{\text { Gross profit }}$

> Sales

$$
\begin{aligned}
& \text { Year }-2,000=\frac{30,000}{72,000} \times 100=41.67 \% \\
& \text { Year }-2001=\frac{44,400}{115,200} \times 100=38.54 \%
\end{aligned}
$$

b) Markup $=\underline{\text { Gross profit }}$

Cost of sales

$$
\begin{aligned}
& \text { Year }-2,001=\frac{44,400}{70,800} \times 100=62.71 \% \\
& \text { Year }-2,000=\frac{30,000}{42,000} \times 100=71.43 \%
\end{aligned}
$$

c) Net profit to sales ratio $=$ N.P before tax x 100 Sales

$$
\begin{aligned}
& \text { Year }-2,001=\frac{237,000}{115,200} \times 100=20.57 \% \\
& \text { Year }-2,000=\underline{12,900} \times 100=17.92 \%
\end{aligned}
$$

72,000
d) Return on capital employed $=\underline{\text { Profit on Ordinary Activities Before Interest \& Tax x } 100}$

Shareholders+Debentures[or Total Assets - Current Liabilides]

$$
\begin{aligned}
& \text { Year }-2001=\frac{24,600}{40,440} \times 100=60.83 \% \\
& \text { Year }-2000=\frac{13,600}{37,200} \times 100=36.56 \%
\end{aligned}
$$

## LIQUIDITY RATIOS

I) Current Ratio $=\frac{\text { Current Assets }}{\text { Current Liabilities }}$

2001
$\underline{32,400}=1.18: 1$
27,360
II) Quick Ratio $=$ Current Assets - Stock
$\underline{2001}$
$\underline{32,400-19,800}=0.46: 1$ 27,360

Current Liabilities
$\underline{2000}$
$\underline{26,280}=1.7: 1$
15,480

## Comments

b) In the year 2000 the current ratio was $1.7: 1$ and in the current year it decreased to 1.18:1. This decline was as a result of the fact that the current liabilities increased at a higher rate than the current assets. This may be due to the use of Bank overdraft facilities and a general increment in other liabilities. This indicates that the companies ability to meet its short term debts e.g. creditors has decreased and the companies operations are now riskier.
The ideal ratio should be at 2:1
c) The mark up margin \& net profit ratio in 2,000 were $71.43 \%, 41.67 \%$ \& $17.92 \%$ respectively. In the current year 2001 they are $62.71 \%, 38.54 \%$ and $20.57 \%$.
The trend shows a decrease in all the ratios except the net profit ratio which increases This may signify that costs of production have increased while at the same time the company is able to minimize it"s costs (expenses) thus the high net profit ratio. The return on capital employed ratio on the other hand has increased from $36.56 \%$ to $60.83 \%$. It indicates that the company is utilizing it"s fixed assets more optimally in coming up with more profit for the shareholders.

## QUESTION THREE

KYAMBA \& ONYANGO PARTNERSHIP
PROFIT, LOSS \& APPROPRIATION ACCOUNT
FOR THE YEAR ENDED 31ST MAY 2002

| Net profit |  | Shs | $\begin{array}{r} \text { Shs } \\ 240,000 \end{array}$ |
| :---: | :---: | :---: | :---: |
| Less salaries | Kyamba | 72,000 |  |
|  | Onyango | 60,000 | $(132,000)$ |
|  |  |  | 108,000 |
| Less: Interest on capital : | Kyamba | 20,000 |  |
|  | Onyango | 20,000 | $(40,000)$ |
|  |  |  | 68,000 |
| Share of profit | Kyamba (1/2) | 34,000 |  |
|  | Onyango (1/2) | 34,000 | $(68,000)$ |
|  |  |  | NIL |

Capital accounts

|  | Kyamba | Onyango | Wakili |  | Kyamba | Onyango | Wakili |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Shs | Shs | Shs |  | Shs | Shs | Shs |
| Goodwill |  |  |  | Bal c/d | 160,000 | 140,000 | 200,000 |
| w/off | 100,000 | 100,000 |  | Current a/c: Wakili |  |  | 83,000 |
| Fixed |  |  |  | Revaluation gain | 12,000 | 12,000 | 6,000 |
| assets |  |  | 306,000 | Goodwill | 80,000 | 80,000 | 40,000 |
| Stocks |  |  | 157,000 | Creditors |  |  | 156,000 |
| Debtors |  |  | 165,000 | Bank |  |  | 173,000 |
| Bal c/d | 200,000 | 200,000 |  | Additional capital | 48,000 | 68,000 |  |
|  | 300,000 | 300,000 | 628,000 |  | 300,000 | 300,000 | 628,000 |

Current accounts

|  | Kyamba | Wakili |  | Kyamba | Wakili <br> Shs |
| :--- | ---: | ---: | :--- | ---: | ---: |
| Drawings | Shs | Shs |  | Shs | Shs |
|  | 85,000 | 70,000 | Bal b/d | 65,300 | 49,000 |
|  |  |  | Salaries | 72,000 | 60,000 |
| Bal c/d |  | Interest on capital | 20,000 | 20,000 |  |
|  | $\underline{106,300}$ | $\underline{93,000}$ | Share of profit | $\underline{34,000}$ | $\underline{34,000}$ |
|  | $\underline{191,300}$ | $\underline{163,000}$ |  | $\underline{191,300}$ | $\underline{163,000}$ |


| KYAMBA \& ONYANGO PARTNERSHIP BALANCE SHEET AS AT $31{ }^{\text {ST }}$ MARCH 2002 |  |  |
| :---: | :---: | :---: |
| NON CURRENT ASSETS | Shs | Shs |
| Property, Plant and Equipment |  | 205,000 |
| CURRENT ASSETS |  |  |
| Stock | 228,000 |  |
| Debtors | 127,000 |  |
| Bank | 135,300 | 490,300 |
| TOTAL ASSETS |  | 695,300 |
| EQUITY \& LIABILITIES CAPITAL \& RESERVES |  |  |
| Capital - Kyamba |  | 200,000 |
| Onyango |  | $\underline{200,000}$ |
|  |  | 400,000 |
| Current Accounts ; Kyamba | 106,300 |  |
| Onyango | 93,000 | 199,300 |
|  |  | 599,300 |
| CURRENT LIABILITY |  |  |
| Creditors |  | 96,000 |
|  |  | 695,300 |

## QUESTION FOUR

a) Reasons for preparing control accounts
i. Check accuracy of the ledgers
ii. Check accuracy of the debtors \& creditors totals
iii. Correct errors
iv. Prevent fraud
v. Speed up preparation of financial statements
b)

Sales ledger control account

|  | Shs |  | Shs |
| :--- | ---: | :--- | ---: |
| Balance b/d | 838,000 | Balance b/d | 184,000 |
| Credit sales | $8,784,000$ | Returns inwards | 248,000 |
| Dishonoured cheques | 193,000 | Cheques | $2,968,000$ |
| Error | 27,000 | Bad debts | 139,000 |
|  |  | Discounts allowed | 162,000 |
|  |  | Contra | Cash |
| Bal c/d | $\underline{123,000}$ | Bal c/d | 106,000 |
|  | $\underline{9,965,000}$ |  | $\underline{5,802,000}$ |
|  |  | $\underline{9,965,000}$ |  |

## Purchases ledger control account

|  | Shs | Shs |  |
| :--- | ---: | :--- | ---: |
| Bal b/d | 196,000 | Bal b/d | 598,000 |
| Returns inwards | 179,000 | Credit purchases | $7,849,000$ |
| Bank cheque | $4,674,000$ |  |  |
| Cash | $1,393,000$ |  |  |
| Discounts received | 231,000 | 356,000 |  |
| Contra | 598,000 | $\underline{8,024,000}$ |  |
| Error - motor vehicle | $\underline{997,000}$ | $\underline{8,624,000}$ |  |

## QUESTION FIVE

## Distinction Receipts <br> \& Revenue

Receipts are the cash amounts received in a business from the various activities the business is engaged in. They could be received from sales, debtors, investment incomes, etc

Revenue is the amount of sales made to its customers, it encompasses both credit items and cash items. It is the gross income during the period arising from the ordinary activities of the business. i.e. it"s core activities.

## Balance sheet and statement of affairs

The balance sheet is used by profit making companies and shows the financial position, assets, liabilities and capital as at a given point in time especially for a an organization that is made with the purpose of making profits.

The statement of affairs is less is a statement from which from which the capital of the owner can be found by estimating the asset and liabilities. It is the equivalent of a Balance Sheet but is mainly used ny Not For Profit Organizations e.g. clubs.

## Cash Basis of Accounting and Accrual Basis of Accounting

The cash basis of accounting entails the recording of revenue and expenses only when such has been received or paid out. This means that any credit items are not accounted for in the books.

On the other hand the accrual basis of accounting entails that incomes and expenses relating to any one financial period should be taken into account without regard to the date of receipt of payment. The amounts of expenses should be matched with the incomes which they have produced in the company in any one period.

## Materiality and Substance over form

It is an overriding rule applying to anything appearing in a financial accounting statement under which trivial matters are not included. That is, something should be significant (due to it"s size or cost) to merit inclusion in financial accounting statements. There is no need to set up a separate reporting segment for such amounts if they can simply be added to total sales without the inconvenience of separate accounts or separate ledgers. Dissimilar items may be aggregated only if they are individually immaterial.
The demerit in the concept lies in the fact that materiality is relative. For example, the loss of Kshs 200 may matter to a small Kiosk but to a business like Barclays Bank with a turnover of billions of dollars it does not. Nevertheless, the materiality concept does not apply while recording cash transactions. Thus, small amounts cannot be omitted from the cashbook on the
grounds that they are not material. As a general rule, therefore, every cash transaction has to be recorded in the cashbook - regardless of the materiality of the amount involved.
Again, the principle of materiality does not hold good when errors of principle are detected which need correction. If it is discovered that a capital item has been erroneously expensed, or a different method of depreciation other than that used in previous years has been applied for a particular asset, the errors should be corrected immediately. The concept of materiality cannot be used as a defense for not correcting the errors.

Substance over form entails that transactions and other events are accounted for and presented in accordance with their substance and economic health e.g. nature and not merely their legal form, in hire purchase the hirer records the goods as belonging to him even though legally he is not the owner of the goods.

DECEMBER 2010
QUESTION ONE
a) (i)

| Cash sales | Sh"000 |  | Sh "000 |
| :---: | :---: | :---: | :---: |
|  | 22,880 | Stock purchases | 19,456 |
|  |  | Slaughter charge | 1,008 |
|  |  | Sundry expenses | 1,744 |
|  |  | Electricity expenses | 304 |
|  |  | Wages expenses | 328 |
|  |  | Balance c/d | 40 |
|  | 22,880 |  | 22,880 |

(ii)

| Bank account |  |  | Sh"000 |
| :--- | ---: | :--- | :---: |
| Working capital | $\mathbf{S h " 0 0 0}$ |  | 22,608 |
| Loan from bank | 1,600 | Stock purchases | 1,728 |
| Cash sales | 4,000 | Shop wages | 2,096 |
|  | 32,280 | Personal drawings | 1,560 |
|  |  | Rates on licence | 200 |
|  |  | Interest on loans | Bal c/d |

MR. KANYAMA
BALANCE SHEET
AS AT 30 SEPTEMBER 2002

|  | Sh"000 | Sh"000 | Sh"000 |
| :---: | :---: | :---: | :---: |
| NON CURRENT ASSETS |  |  |  |
| Buildings |  |  | 5,880 |
| Plant |  |  | 1,260 |
| CURRENT ASSETS |  |  |  |
| Cash |  | 40 |  |
| Bank |  | 9,688 |  |
| Debtors |  | 586.08 |  |
| Stock |  | $\underline{1,160}$ | $\frac{11,474.08}{18,614.08}$ |
|  |  |  | 18,614.08 |
| CAPITAL \& RESERVES |  |  |  |
| Capital |  |  | 7,400 |
| Working capital |  |  | 1,600 |
| Less Drawings |  |  | (2,096) |
| Net profit |  |  | 5,520.08 |
| NON CURRENT LIABILITIES |  |  |  |
| Loan |  |  | 4,000 |
| CURRENT LIABILITIES |  |  |  |
| Creditors |  |  | 1,720 |
| Interest due |  |  | 200 |
| Wages due |  |  | 270 |
| Total equity and liabilities |  |  | 18,614.08 |

MR. KANYAMA
TRADING, PROFIT \& LOSS ACCOUNT FOR THE YEAR ENDED 30 SEPTEMBER 2002

|  | Shs"000 | Shs 000 |
| :---: | :---: | :---: |
| Sales (W1) |  | 55,160 |
| Return inwards (W2) |  | (208) |
|  |  | 54,952 |
| Less: Cost of sales |  |  |
| Opening stock | 400 |  |
| Add: Purchases | 42,584 |  |
| Less: Closing stock | $(1,160)$ | 41,824 |
| Gross profit |  | 13,128 |
| Less: Expenses |  |  |
| Wages (W3) | 2,326 |  |
| Depreciation (W4) |  |  |
| Buildings | 120 |  |
| Plant \& equipment | 140 |  |
| Provision for doubtful debts (W5) | 59.2 |  |
| Slaughter charge | 1,008 |  |
| Sundry expenses | 304 |  |
| Rates \& licences | 1,560 |  |
| Interest on loan (W6) | 400 | (7,661.2) |
| Net profit |  | -5,466.8 |

## QUESTION TWO

| Clubhouse a/c |  |  |  |
| :--- | ---: | ---: | ---: |
|  | Shs |  | Shs |
| Bal b/d | 16,800 |  |  |
| Bank | 2,000 |  |  |
| Accrued cost | $\underline{1,000}$ | Bal c/d | $\underline{19,800}$ |
|  | $\underline{19,800}$ |  | $\underline{19,800}$ |
|  | Rates a/c |  | Shs |
|  | Shs |  |  |

Insurance a/c

|  | Shs |  | Shs |
| :--- | ---: | :--- | ---: |
| Prepaid b/d | 70 | Prepaid c/d | 80 |
| Bank | $\underline{160}$ | I \& E a/c | $\underline{150}$ |
|  | $\underline{230}$ | $\underline{230}$ |  |

Provision for depreciation (Equipment) a/c

| Disposal <br> Bal c/d | Shs |  | Shs |
| :---: | :---: | :---: | :---: |
|  | 300 | Bal b/d | 2,200 |
|  | 3,095 | I \& E a./c | 1,195 |
|  | 3,395 |  | 3,395 |
| Subscription Income |  |  |  |
|  | Shs |  | Shs |
| Accrued b/d | 32 | Prepaid b/d | 16 |
| I \& E | 2,996 | Bank | 2,992 |
| Prepaid c/d | $\underline{20}$ | Owing c/d | -40 |
|  | 3,048 |  | 3,048 |
| (Creditors for bar purchases) |  |  |  |
|  | Shs |  | Shs |
| Bank | 23,600 | Bal b/d | 1,600 |
| Bal c/d | 2,000 | Purchases | $\underline{24,000}$ |
|  | 25,600 |  | 25,600 |
| Bank |  |  |  |
|  | Shs |  | Shs |
| Bal b/d | 1,960 | Club house | 2,000 |
| Sub. Income | 2,992 | Equipment | 680 |
| Disposal | 100 | PLCA | 23,600 |
| Sales | 29,750 | Salary - Barman | 240 |
| Social evening | 4,800 | Social evenings expenditure | 3,360 |
|  |  | Rates | 1,000 |
|  |  | Insurance | 160 |
|  |  | Salary (BM \& GM) | 2,160 |
|  |  | Annual licence | 100 |
|  |  | Electricity | 500 |
|  |  | Miscellaneous | 140 |
|  |  | Commission | 297.5 |
|  |  | Bal c/d | $\underline{5364.5}$ |
|  | 39,602 |  | 39,602 |

Electricity a/c

| Bank | Shs |  | Shs |
| :---: | :---: | :---: | :---: |
|  |  | Owing b/d | 60,000 |
|  | 500,000 | $I \& E a / c$ | 440,000 |
|  | 500,000 |  | 500,000 |
|  | (Long term liability) |  |  |
|  | Accrued Clubhouse Cost (liability) |  |  |
|  | Shs |  | Shs |
| Bal c/d | 1,000 | Clubhouse | 1,000 |

## Accumulated fund:

$=$ Total assets - Liabilities
$=22,282,000-1,676,000$
$=20,606,000$

Sub:
Bank to be received during the year $=3,000,000(300 \times 10,000)$
In arrears at year start $=32,000 / 8,000=4$ members
In advance at year start $=16,000 / 8,000=2$ members
Therefore $300-6=294$ members to pay at Sh. $10,000=294 \times 10,000=2,940,000$

$$
\begin{array}{ll}
=2 \text { members @Sh.10,000 } & =2 \times 10,000= \\
=4 \text { members @Sh. } 8,000 & =4 \times 8,000
\end{array}
$$

Subscriptions for the year: From 300 members

$$
\begin{aligned}
& =2 \text { members in advance pay at old rates }(8,000)=2 \times 8,000 \\
& =16,000
\end{aligned}
$$

$=298$ members to pay at new rate $(10,000)=298 \times 10,000$

$$
=2,980,000
$$

Therefore Subscriptions for the year $=2,980,000+$

$$
16,000=2,996,000
$$

Owing at year end $=4$ members x

$$
10,000=40,000
$$

Advance at year end $=2$ members x

$$
10,000=20,000
$$

3. 

Disposal a/c

|  | Shs |  | Shs |
| :--- | ---: | :--- | :--- |
| Equipment | 500 | Provn for depreciation | 300 |
|  |  | Bank | 100 |
|  | $\underline{500}$ | P \& L (loss) | $\underline{100}$ |
|  | $\underline{500}$ |  |  |

(Assumption - sale for cash)
4.

Opening stock $=1 / 2$ of one month"s purchases

$$
\begin{aligned}
& =1 / 2 \times 1,600,000 \\
& =800,000
\end{aligned}
$$

Purchases for the year $=1,600,000 \rightarrow$ Increase by $25 \%$ per month

$$
\begin{aligned}
& =1,600,000+400,000=2,000,000 \text { per month } \\
& =2,000,000 \times 12=24,000,000 \text { for year }
\end{aligned}
$$

Paid to creditors = Owing last year +11 month"s this year
$=1,600,000+(2,000,000 \times 11)$
$=1,600,000+22,000,000$
$=23,600,000$

## Bar Trading, Profit and Loss account

| Sales: | Shs | Shs |
| :--- | ---: | ---: |
| Opening stock | 800,000 |  |
| Purchases | $24,000,000$ |  |
| Closing stock | $1,000,000$ | $(23,800,000)$ |
| Gross profit (20\% sales) |  | $5,950,000$ |
| Gross profit b/d |  |  |
| Less: Expenses | $2,950,000$ |  |
| Salary of bar man (20,000 x 12) | 297,000 |  |
| Commission | 100,000 |  |
| Bar annual licence | 88,000 | $(725,500)$ |
| Electricity |  | $\underline{5,224,500}$ |
| Profit |  |  |

Gross profit $=20 \%$ of sales
Therefore $25 \%$ of cost of sales

$$
\begin{aligned}
& =25 / 100 \times 23,800 \\
& =5,950
\end{aligned}
$$

## Forecast Social Evenings a/c

Dinner tickets $=(2,000 \times 200 \times 12)=4,800,000$
Expenses $\quad=(1,400 \times 200 \times 12)=\underline{3,360,000}$
Gain on social evenings a/c $\quad 1,440,000$
Swara
Income and Expenditure a/c

| Income: | Shs |  |
| :--- | ---: | ---: |
| $\quad$ Subscription income | 2,996 | Shs |
| Gain on social evenings | 1,440 |  |
| $\quad$ Profit on bar | $5,224.5$ |  |
| Expenditure |  |  |
| $\quad$ Loan on disposal | 100 |  |
| Provision for depreciation Equipment | 1,195 |  |
| Rates | 950 |  |
| Insurance | 150 |  |
| Salary of club manager | 1,200 |  |
| Salary of groundsman | 950 |  |
| Electricity | 140 | $\underline{(5,047)}$ |
| Miscellaneous |  | $\underline{4,613.5}$ |

Rates: Accounting year $=1$ Oct 2002-30 Sept 2003
Rates to be paid $=1$ Jan -31 Dec of Sh. 1,000,000
Therefore 3 months advance
Rates prepaid $=1,000,000 \times 3 / 12=250,000$
I \& E

$$
=950,000
$$

Insurance: Paid 1 April 2003 - 31 March 2004

$$
\text { Prepaid }=1 \text { Oct 2003-31 Mar } 2004=6 / 12 \times 160,000=80,000
$$

| Swara Club <br> Balance sheet |  |  |
| :---: | :---: | :---: |
| Non Current asset | Shs | $\sqrt{3 h s}$ |
| Clubhouse |  | 19,800,000 |
| Equipment (Cost - acc) |  | $\frac{1,685,000}{21,485,000}$ |
| Current asset |  |  |
| Stock | 1,000,000 |  |
| Bank | 5,364,500 |  |
| Rates prepaid | 250,000 |  |
| Insurance prepaid | 80,000 |  |
| Cash | 20,000 |  |
| Sub in arrears | 40,000 | 6,754,500 |
|  |  | 28,239,500 |
| Financed by: |  |  |
| Accumulated fund |  | 20,606,000 |
| Surplus |  | 4,613,500 |
|  |  | 25,219,500 |
| Non current liabilities |  |  |
| Long term debt |  | 1,000,000 |
| Current liability |  |  |
| Creditor |  | 2,000,000 |
| Subscriptions prepaid |  | 20,000 |
|  |  | 28,239,500 |

## QUESTION THREE

a) Legal provisions regarding establishment and subsequent use of;
i) Share premium account

According to the Companies Act (Chapter 486 Laws of Kenya) where the company issues shares at a premium, the premium on such shares shall be transferred to the Share Premium Account.
Shares premium may be applied to:-
i) Finance a fully paid bonus issue
ii) Write off preliminary expenses
iii) Write off expenses or commission paid or discount allowed on any issue of shares or debentures.
iv) Provide for the premium payable on redemption of redeemable preference shares or debentures.
ii) Capital redemption reserve

As under the Companies Act (Chapter 486 Laws of Kenya) if Redeemable Shares are issued and are redeemed otherwise than out of the proceeds of a fresh issue then a part of dividend equivalent to the nominal amount of the shares to be redeemed shall be transferred to a reserve fund to be known as the Capital Redemption Reserve Fund.

The Capital redemption reserve Account can only be utilized to

- Redeem any redeemable fully paid up shares of the company.
- Pay up any un-issued shares of the company which are to be issued to the members of the company as fully paid Bonus Shares.


## b)

MASABA COMPANY LTD
APPROPRIATION ACCOUNT
FOR THE YEAR ENDED 31 DECEMBER 2001

|  | Shs"000 | Shs"000 |
| :--- | ---: | ---: |
| Net profit for the year |  | 1,440 |
| Retained profit as at 1.1.2001 |  | 4,460 |
|  | 500 | 5,900 |
| Transfer to general reserve | 400 |  |
| Preference dividend | 600 |  |
| Ordinary share dividends | $\underline{2,000}$ | $\underline{(3,500)}$ |
| Bonus issue | $\mathbf{2 , 4 0 0}$ |  |
| Retained profit c/d |  |  |

## MASABA LTD

## BALANCE SHEET

AS AT 31 ${ }^{\text {ST }}$ DECEMBER 2001

| Shs"000 | Shs"000 | Shs"000 |
| :---: | :---: | :---: |
| Non current assets |  |  |
| Land \& buildings |  | 18,400 |
| Motor vehicle |  | 4,200 |
| Fittings |  | 1,500 |
| Intangible asset: goodwill |  | 1,200 |
| Current assets |  |  |
| Debtor | 1,660 |  |
| Short term investment | 780 |  |
| Stock | 2,960 | 5,400 |
| Total assets |  | 30,700 |
| Equity \& liabilities |  |  |
| Capital: |  |  |
| Issued share capital 600,000 Sh 20 ordinary share | 12,000 |  |
| Add Bonus issue 100,000 Sh 20 ordinary share | 2,000 | 14,000 |
| Issued share capital 250,000 Sh 20 Redeemable Preference shares |  | 5,000 |
| Share premium |  | 400 |
| Capital redemption reserve fund |  | 3,000 |
| General reserve |  | 1,600 |
| Retained profits |  | 2,400 |
|  |  | 26,400 |
| Revaluation Reserve |  | 1,000 |
| Long - term liability |  |  |
| 10\% Debenture |  | 1,600 |
| Current liabilities |  |  |
| Creditors |  | 960 |
| Bank overdraft |  | 540 |
| Outstanding preference interim dividend |  | 200 |
| Total equity \& liabilities |  | 30,700 |

## QUESTION FOUR

| Buildings account |  |  |
| :--- | ---: | ---: |
|  | Shs"000 | Shso00 |
| Cost | 22,000 |  |
| Revaluation | $\underline{12,000}$ | Bal c/d |
|  | $\underline{34,000}$ | $\underline{34,000}$ |

Provision for depreciation on Buildings account


Provision for depreciation on Plant \& Machinery account

|  | Shs ${ }^{\text {12000 }}$ |  | Shs ${ }^{\text {"1000 }}$ |
| :---: | :---: | :---: | :---: |
| Disposal | 925 | Bal b/d | 6,000 |
| Bal c/d | 7,550 | P \& L | 2,475 |
|  | 8,475 |  | 8,475 |
| Motor Vehicle account |  |  |  |
|  | Shs"000 |  | Shs ${ }^{\prime \prime} 000$ |
| Cost | 6,000 | Disposal | 200 |
| Motor vehicle exchange | 120 | Bal c/d | 6,100 |
| Cash | 180 |  |  |
|  | 6,300 |  | 6,300 |

Provision for depreciation on Motor vehicle account

|  | Shs $^{\prime \prime} \mathbf{0 0 0}$ |  | Shs $^{\prime \prime} \mathbf{0 0 0}$ |
| :--- | ---: | :--- | ---: |
| Disposal | 130 | $\mathrm{Bal} \mathrm{b} / \mathrm{d}$ | 2,000 |
| Bal c/d | $\underline{3,075}$ | $\mathrm{P} \& \mathrm{~L}$ | $\underline{1,205}$ |
|  | $\underline{3,205}$ |  | $\underline{3,205}$ |

## PROPERTY, PLANT \& EQUIPMENT MOVEMENT

SCHEDULE AS AT 30 JUNE 2002

|  | Land | Buildings | Plant \& Machinery | Motor vehicle | Totals |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | Shs"000 | Shs"000 | Shs"000 | Shs"000 | Shs"000 |
| Cost | 40,000 | 22,000 | 16,000 | 6,000 | 84,000 |
| Disposal |  |  | $(3,000)$ | (200) | $(3,200)$ |
| Revaluation |  | 12,000 |  |  | 12,000 |
| Additions | - |  | 4,000 | 300 | 4,300 |
| ( a ) | 40,000 | 34,000 | 17,000 | 6,100 | 97,100 |
| Acc. deprn Disposal |  | 8,560 | $8,475$ | $3,205$ | $\begin{aligned} & \hline 20,240 \\ & (1,025) \end{aligned}$ |
| ( b ) |  | 8,560 | 7,550 | 3,075 | 19,185 |
| N B V | 40,000 | 25,440 | 9,450 | 3,025 | 77,915 |

## QUESTION FIVE

## a) Brief notes on:

(i) Purchased goodwill and non purchased goodwill

Goodwill is the term used by an accountant to describe the difference between the value added/placed upon a firm and the sum of the values of identifiable net assets of that firm. Goodwill is said to exist when a firm is earning profits over and above normal earnings of other similar enterprises in the same industry. It is an intangible asset.

Goodwill is the excess amount that has to be paid to acquire part or the whole of a business as a going concern over and above the value of the net assets owned by the business.

Purchased goodwill is the difference between the amount paid to acquire a part or the whole of a business as a going concern and the value of the net assets owned by the business.
Purchased goodwill $=$ Total price - Value of net identifiable assets
Non purchased goodwill is inherently generated and not a subject of acquisition. It arises out of a subjective valuation but not through a market transaction. It should not be recognised in the financial statements.
(ii) Amortisation and depreciation of fixed assets

Amortisation refers to the loss of value of a fixed asset due to passing of time. For example a business buys a patent for ten years. At the end of the ten years the asset is said to have been fully amortised. Examples of fixed assets that an amortised include leases, patents and goodwill.
Depreciation is the part of the cost of a fixed asset consumed during it"s period of use by the firm. Assets depreciate because of various reasons such as physical deterioration, depletion, obsolescence etc., Both amortisation and depreciation are treated as expense in the income statement.

## (iii) Provisions and reserves

## Provision

This is the money set aside for payment of foreseen expenses. For example in companies the profit earned may be set aside for payment of dividends, corporation tax.
A provision is charged against revenue as an expense. Its related either to the dimunition in the value of an asset e.g. doubtful debts or a liability e.g. audit fees, director"s fees, proposed dividend, taxation

## Reserves

This is an appropriation of distributable profits. A company may decide not to distribute part of the profits and during a financial year to the shareholders as dividends. Profits not distributed are revenue reserves. E.g general reserve, revaluation reserve, share premium
Capital reserves arise from causes other than those of normal trading e.g. share premium, capital redemption reserve.
(iv) Compensating errors and errors of principle

A compensating error will arise where two errors of equal amounts but on opposite sides of the accounts cancel each other out. For example, if the sales account has added up to be Sh 10 too much and the purchases account was also added up to Sh 10 too much, then these two errors would cancel out in the trial balance.
An error of principle will arise when an item is entered in the wrong class of account for example of a fixed asset such as a motor van is debited to an expenses account such as motor expenses account.

JUNE 2011

## QUESTION ONE

LIMURU MANUFACTURERS
MANUFACTURING ACCOUNT FOR THE YEAR ENDED 31 ${ }^{\text {ST }}$ DEC 2002
Opening stock of raw materials
Add: Purchases of raw materials
Less Closing stock of raw materials
Cost of raw materials consumed
Direct labour

| Shs"000 | Shs" ${ }^{\text {"000 }}$ |
| :---: | :---: |
|  | 7,000 |
|  | 38,000 |
|  | $(9,000)$ |
|  | 36,000 |
|  | 31,000 |
|  | 67,000 |
| $\begin{array}{r} 25,000 \\ 3,000 \\ \hline \end{array}$ |  |
|  | 28,000 |
|  | 95,000 |
|  | 5,000 |
|  | $(8,000)$ |
|  | 92,000 |
|  | 23,000 |
|  | 115,000 |

LIMURU
TRADING, PROFIT \& LOSS A/C
FOR THE YEAR ENDED 31 DEC 2002

|  | Shs"000 | Shs"000 |
| :--- | ---: | ---: |
| Sales |  | 192,000 |
| Less Cost of sales | 6,900 |  |
| Opening stock finished goods | 115,000 |  |
| Market value of goods produced | $\underline{(10,350)}$ | $\underline{(111,550)}$ |
| Less Closing stock of finished goods |  | 80,450 |
| Gross profit | $\underline{23,000}$ |  |
| Add: Manufacturing profit |  | 103,450 |
| Less: Expenses |  |  |
| Rent \& rates | 6,000 |  |
| Lighting | 2,000 |  |
| Stationery \& postage | 19,380 |  |
| Staff salaries | 4,000 |  |
| Depreciation of motor vehicles | $\underline{4,500}$ | $\underline{(52,880)}$ |
| Motor vehicle running costs |  | 50,570 |
| Add: Opening stock figure - unrealized profit |  | 1,380 |
| Less: Closing stock figure-unrealized profit | $\underline{(2,070)}$ |  |
| Net profit |  |  |

## LIMURU MANUFACTURERS

## BALANCE SHEET

AS AT 31 ${ }^{\text {ST }}$ DECEMBER 2002

## NON CURRENT ASSETS

Plant and machinery
Motor vehicles

## CURRENT ASSETS

Stock : Raw materials
WIP
Finished goods
Less; provision for unrealized profit
Debtors
Prepayments
Bank

TOTAL ASSETS
EQUITY \& LIABILITIES
Capital
Opening balance
Add: Net profit
Less: Drawings


## QUESTION TWO

a) Differentiate between a petty cashbook and a three column cashbook
i. The cashbook is a book of original entry which records all cash transactions either in bank or through cash while a petty cashbook is a type of cashbook that is used to record small amounts paid for in cash.
ii. In the three column cashbook there are three columns in each side while in a petty cashbook no three equal columns like in a three column cashbook rather each expense has a special column.
iii. In a petty cashbook, expenses are normally reimbursed periodically while in a cashbook that doesn"t take place. Therefore the way the cashbook is balanced is not the same way a petty cashbook is balanced.
b) Importance of a Bank reconciliation statement to a business

1) It establishes the correct balance of cash at bank at the end of the month
2) It corrects the errors in the cashbook or bank statement
3) It helps detect frauds
c) .

Adjusted cash book (as at 30.4.2003)

|  | Shs |  | Shs |
| :--- | ---: | :--- | ---: |
| Dividends received | 124,000 | Bal b/d | $1,108,000$ |
| Error in payment of cheque | 120,000 | Bank charges \& commission | 272,000 |
| Error in balance b/f | 100,000 | Error in payment of cheque | 88,000 |
| Balance c/f | $\underline{1,284,000}$ | Dishonoured cheque | $\underline{160,000}$ |
|  | $\underline{1,628,000}$ |  | $\underline{1,028,000}$ |

## BANK RECONCILIATION

AS AT 30.4.2003

|  | Shs |
| :--- | ---: |
| Balance as per updated cashbook | $(1,284,000)$ |
| Add: Unpresented cheques | $\frac{534,000}{(750,000)}$ |
| Less: Uncredited cheques | $(1,524,000)$ |
| Error by the bank | $\frac{(50,000)}{(2,324,000)}$ |

## QUESTION THREE

## AHADI LTD

PROFIT \& LOSS \& APPROPRIATION A/C FOR THE YEAR ENDED 30 ${ }^{\text {TH }}$ APRIL 2003

| Gross profit for the year | Shs"000 | $\begin{array}{r} \text { Shs }{ }^{\text {" } 0000} \\ 32,603.2 \end{array}$ |
| :---: | :---: | :---: |
| Less: Expenses |  |  |
| Bad debts | 136 |  |
| Salaries and wages | 11,280 |  |
| Rates and insurance | 504 |  |
| Postage and telephone | 248 |  |
| Water and electricity | 705.6 |  |
| Debenture interest | 640 |  |
| Director"s fees | 3,000 |  |
| General expenses | 1,243.2 |  |
| Depreciation - Motorvehicle (W1) | 2,328 |  |
| - Office fittings and equipment (W1) | 2,678.4 |  |
| Audit fees | 480 | $(23,243.2)$ |
| Net profit |  | 9,360.0 |
| Add: Retained profit from previous year |  | 9,700.8 |
| Less: Proposed preference dividends (W3) Ordinary dividends (W3) |  | $\begin{array}{r} 19,060.8 \\ (1,280) \end{array}$ |
| Ordinary dividends (W3) |  | 12,980.8 |
| Transfer to general reserve |  | $(4,800)$ |
| Retained profits |  | 8,180.8 |

## AHADI LTD

BALANCE SHEET AS AT $30^{\text {TH }}$ APRIL 2003

| NON CURRENT ASSETS | Shs"000 | Shs"000 | Shs |
| :---: | :---: | :---: | :---: |
| Land and buildings | 52,880 |  | 52,880 |
| Office fittings \& equipment | 17,856 | 9,558.4 | 8,297.6 |
| Motor vehicles | $\underline{11,640}$ | 11,248 | $\underline{392}$ |
|  | 82,376 | 20,806.4 | 61,569.6 |
| CURRENT ASSETS |  |  |  |
| Stock |  | 33,540.8 |  |
| Accounts receivable \& prepayments (W4) |  | 10,940 |  |
| Balance at bank |  | 3,118.4 | 47,599.20 |
| TOTAL ASSETS |  |  | 109,168.8 |
| EQUITY \& LIABILITIES <br> CAPITAL \& RESERVES |  |  |  |
| 800,000 8 \% Shs 20 preference shares |  |  | 16,000 |
| $2,400,000$ Shs 20 ordinary shares |  |  | $\begin{aligned} & 48,000 \\ & 64,000 \end{aligned}$ |
| Retained profits |  | 8,180.8 |  |
| General reserve |  | 16,000 |  |
| Proposed dividends* |  | 6,080 | 30,260.8 |
|  |  |  | 94,260.8 |
| NON CURRENT LIABILITIES <br> $10 \%$ debentures |  |  | 6,400 |
| CURRENT LIABILITIES |  |  |  |
| Accounts payable \& accruals (W5) |  |  | 8,508 |
| TOTAL EQUITY \& LIABILITIES |  |  | 109,168.8 |

## * Note: Proposed Dividends

Under IAS 10 Events after the Balance sheet date, if an entity declares dividends to share holders after the Balance sheet date as above it should not be recognized as a liability as at the Balance sheet date but should be indicated as a note to the accounts. However, for the purposes of Internal Accounts like the one above which will not be circulated to outside parties, it can be recognized as such since it is money which does not belong to the company and as such a liability. Since it will be paid in less than 1 year. It then means that it is a current liability.

## Workings

W1 Depreciation
$\begin{array}{cr}\text { i) Office fittings and equipments } & \text { SHS } \\ 15 \% \times 17,856,000 & 2,678,400 \\ \text { Accumulated depreciation } & \\ \text { b/d }(17,856,000-10,976,000) & \underline{6,880,000} \\ \text { c/f } & \underline{9,558,400}\end{array}$
ii) Motor vehicles
$20 \% \times 11,640,000 \quad 2,328,000$
Accumulated depreciation
b/d (11,640,000-2,720,000) $\underline{8,920,000}$
c/f $\quad 11,248,000$

W2 Prepaid insurance premiums
$3 / 6 \times 120,000=$ Shs 60,000

W3 Proposed dividends
(i) Preference dividends $\quad(8 \% \times 16,000,000)=1,280,000$
(ii) Ordinary dividends $\quad(10 \% \times 48,000,000)=\underline{4,800,000}$ 6,080,000

W4 Accounts receivable and prepayments
As per trial balance
10,880,000
Prepaid insurance premiums

$$
\begin{array}{r}
60,000 \\
\hline
\end{array}
$$

10,940,000

W5 Accounts payable and accruals

As per trial balance
Accrued electricity bill Director"s fee
Audit fee
Debenture interest

5,488,800
219,200
2,000,000
480,000
$\begin{array}{r}320,000 \\ \hline 8,508,000\end{array}$

## QUESTION FOUR

## MUNYAKA \& OPIYO

TRADING, PROFIT \& APPROPRIATION FOR THE YEAR ENDED $30^{\mathrm{TH}}$ APRIL 2003

| Sales | Shs | $\begin{array}{r} \text { Shs } \\ 15,576,500 \end{array}$ |
| :---: | :---: | :---: |
| Less: cost of sales |  |  |
| Purchases | 10,580,000 |  |
| Less: closing stock | $(1,205,00)$ | 9,375,000 |
| Gross profit |  | 6,201,500 |
| Add: Discount received |  | $\frac{55,000}{6,256,500}$ |
|  |  | 6,256,500 |
| Less: Expenses |  |  |
| Bad debts | 200,000 |  |
| Discount allowed | 122,500 |  |
| Go-down rental | 500,000 |  |
| Wages | 1,920,000 |  |
| Salary to sales manager | 1,200,000 |  |
| Rates | 175,000 |  |
| Repairs | 62,500 |  |
| Insurance | 50,000 |  |
| Motor expenses | 315,500 |  |
| Sundry expenses | 25,000 |  |
| Depreciation - Motor vehicle | 200,000 |  |
| - Equipment | 250,000 |  |
| - Furniture \& fittings | 37,500 | (5,058,000) |
| Net profit |  | 1,198,500 |
| Salary - Opiyo | 440,000 | $(440,000)$ |
|  |  | 758,500 |
| Interest on capital - Munyaka | 350,000 |  |
| - Opiyo | 200,000 | $(550,000)$ |
|  |  | 208,500 |
| Share of profit - Munyaka | 139,000 |  |
| - Opiyo | -69,500 | $(208,500)$ |
|  |  | NIL |

## MUNYAKA \& OPIYO

BALANCE SHEET
AS AT 30 ${ }^{\text {TH }}$ APRIL 2003

|  | Shs | Shs | Shs |
| :---: | :---: | :---: | :---: |
| NON CURRENT ASSETS |  |  |  |
| Equipment | 2,500,000 | 250,000 | 2,250,000 |
| Furniture and fittings | 375,000 | 37,500 | 337,500 |
| Motor vehicles | 1,000,000 | 200,000 | 800,000 |
|  | $\underline{3,875,000}$ | 487,500 | 3,387,500 |
| CURRENT ASSETS |  |  |  |
| Stock |  | 1,205,000 |  |
| Debtors |  | 1,550,000 |  |
| Prepayments |  | 30,000 |  |
| Bank |  | 574,000 |  |
|  |  |  | 3,359,000 |
| TOTAL ASSETS |  |  | 6,746,500 |
| Capital - Munyaka |  |  | 3,500,000 |
| - Opiyo |  |  | 2,000,000 |
|  |  |  | 5,500,000 |
| $\begin{aligned} \text { Current a/c"s } & \text { - Munyaka } \\ & - \text { Opiyo } \end{aligned}$ |  | $\begin{array}{r} 49,000 \\ 322,500 \\ \hline \end{array}$ | 371,500 |
|  |  |  | 5,871,500 |
| CURRENT LIABILITIES |  |  |  |
| Creditors |  | 750,000 |  |
| Accruals |  | 125,000 | 875,000 |
| TOTAL EQUITY \& LIABILITIES |  |  | 6,746,500 |

## Creditors control account

|  | Shs'000 $^{\prime \prime}$ |  | Shs"000 |
| :--- | ---: | :--- | ---: |
| Bank | 9,900 | Purchases | 10,705 |
| Discount received | 55 |  |  |
| Bal c/d | $\underline{750}$ | $-10,705$ | $\underline{10,705}$ |

Debtors control account

| Sales | Shs ${ }^{\text {11 }} 000$ |  | Shs ${ }^{\text {11000 }}$ |
| :---: | :---: | :---: | :---: |
|  | 15,576.50 | Cash | 13,704 |
|  |  | Discount allowed | 122.50 |
|  |  | Bad debts | 200 |
|  |  | Bal c/d | 1,550 |
|  | 15,576.50 |  | 15,576.50 |

## CASH FROM DEBTORS

|  | Shs |
| :--- | ---: |
| Bank | $12,700,000$ |
| Payments | $\underline{1,004,000}$ |
|  | $\underline{13,704,000}$ |

## Current accounts

|  | Munyaka Shs | Opiyo Shs |  | Munyaka | Qniyo |
| :---: | :---: | :---: | :---: | :---: | :---: |
| Drawings - Cash | 390,000 | 312,000 | Salary |  | 440,000 |
| . - Goods | 50,000 | 75,000 | Interest on capital | 350,000 | 200,000 |
| Balc/d | 49,000 | 322,500 | Share of profit | 139,000 | 69,500 |
|  | 489,000 | 709,500 |  | 489,000 | 709,500 |

## QUESTION FIVE

a) What is an accounting policy?

Accounting policies are specific accounting principles, rules, methods, procedures, conventions and bases selected and consistently followed by a reported entity to be the most appropriate circumstances in preparing financial statements
b) Briefly explain the three circumstances under which "goodwill" can be recorded in a business firm"s books of account
i) In case of a sole proprietorship business, when another person purchases a sole proprietorship business and the prospective buyer pays more than the net identifiable assets. Such goodwill should be recorded.
ii) In case of a business acquisition; This is whereby a company buys another company at a value in excess of its net identifiable assets. This is called purchased goodwill and should be recorded in a business/firm"s books of account.

Purchased goodwill $=$ Total price less value of identifiable net assets
[This goodwill is retained in the balance sheet and annually checked for impairment loss which loss is recognised in the income statement (IFRS)]
iii) In case of a partnership, when a new partner is being admitted to the partnership and pays in excess of his identifiable net assets contribution.

## c) Owners

They have invested in the business by providing capital. They would like to have information on the position performance and changes in the financial position in order to assess the profitability of their investments, stewardship of the firm by the managers and how much returns they expect.

## Financial analysts

Financial Analysts and advisors interpret financial information.(These include brokers and consultants) They need information on the financial position and performance so advice their clients ( or potential investors ) as to profitability and the value of the investment. Other advisors include the press who will pass the information to the public or interested parties.

## Lenders

Lenders have provided loans (both long-term e.g. debentures and short-term e.g. overdrafts) to the firm. They would like to have information about the firms financial performance and position so as to assess whether the firm is profitable enough to pay the interest on loans and the principal amount when it becomes due.

DECEMBER 2011

## QUESTION ONE

## MUTHUSI TRADERS

TRADING, PROFIT \& LOSS ACCOUNT FOR THE YEAR ENDED 31ST OCTOBER 2003

| Sales (W9) | Shs ${ }^{\text {" } 000}$ | $\begin{array}{r} \hline \text { Shs" }{ }^{\prime \prime} \mathbf{0 0 0} \\ 2,800 \end{array}$ |
| :---: | :---: | :---: |
| Less: Cost of sales |  |  |
| Opening stock | 390 |  |
| Purchase (W10) | 2,140 |  |
| Less: Closing stock | (430) | $(2,100)$ |
| Gross Profit (W11) |  | 700 |
| Add: Income |  |  |
| Discount received |  | 40 |
| Less: Expenses |  |  |
| Discount allowed | 70 |  |
| Provision for bad debt (W7) | 5 |  |
| Lighting (W8) | 69 |  |
| Loss on disposal of motor vehicle (W2) | 8 |  |
| Depreciation of motor vehicle (W3) | 124.4 |  |
| Depreciation of furniture (W3) | 50 |  |
| Interest on loan (W4) | 60 |  |
| General expenses | 35 |  |
| Salaries \& wages | 160 |  |
| Bad debts | 20 | (601.4) |
| NET PROFIT |  | $\underline{138.6}$ |

MUTHUSI BALANCE SHEET
AS AT $31{ }^{\text {ST }}$ OCTOBER 2003

|  | COST | ACCM. DEPRN | NETBK VALUE |
| :---: | :---: | :---: | :---: |
|  | Shs | Shs | Shs |
| NON CURRENT ASSETS |  |  |  |
| Furniture | 600 | 210 | 390 |
| Motor vehicle | 622 | 124.4 | 497.6 |
| Freehold property |  |  | 600 |
| CURRENT ASSETS |  |  |  |
| Debtors (W4) |  | 570 |  |
| Stock |  | 430 | 1,000 |
| TOTAL ASSETS |  |  | 2,487.6 |
| EQUITY \& LIABILITIES <br> CAPITAL \& RESERVES |  |  |  |
| Capital (W12) |  |  | 1,400 |
| Profit |  |  | 138.6 |
| Less Drawings |  |  | (60) |
| NON CURRENT LIABILITIES |  |  |  |
| 10 \% loan (W13) |  |  | 500 |
| CURRENT LIABILITIES |  |  |  |
| Creditors (W6) |  |  | 300 |
| Accruals |  |  | 19 |
| Bank overdraft (W1) |  |  | 160 |
| Loan interest due |  |  | 30 |
|  |  |  | 2,487.6 |

WORKINGS
W1
Bank account

|  | Shs"000 |  | Shs" |
| :--- | ---: | :--- | ---: |
| Cash sales | 720 | Balance b/d | 60 |
| Received from debtors | 1,890 | Cash purchases | 240 |
| Proceeds from motor vehicles | 120 | Payment to creditors | 1,940 |
|  |  | Purchases of furniture | 200 |
|  |  | Salaries \& wages | 160 |
|  |  | Lighting | 65 |
|  |  | General expenses | 35 |
|  |  | Interest on loan | 30 |
| Bal c/d | Drawings | 60 |  |
|  | $\underline{160}$ | Repayment of loan | $\underline{100}$ |
|  | $\underline{2,890}$ |  | $\underline{2,890}$ |

W2
Disposal of motor vehicle account

|  | Shs"000 |  | Shs"000 |
| :---: | :---: | :---: | :---: |
| Cost | 250 | Sale Proceeds <br> Accumulated deprn P \& L | 120 |
|  |  |  | 122 |
|  |  |  | 8 |
|  | 250 |  | $\underline{250}$ |

W3
(i) Depreciation on motor vehicles

Net book value
Shs ${ }^{\text {" }} 000$
Less: NBV of disposed vehicle (250 - 122)
750
Less:NBV of disposed vehicle (250-122)
128
Depreciation $=622 \times \underset{100}{ }=124.4$
100
(ii) Depreciation on furniture

Shs"000
$\begin{array}{ll}\text { New furniture }=200 \times \frac{10}{100} \times \frac{6}{12} & = \\ \text { Old furniture }=400 \times \frac{10}{100}= & 40 \\ \text { Total depreciation } & \underline{\underline{50}}\end{array}$

## W5

Interest on loan
Shs"000
Half paid loan interest
30
Outstanding interest
30 (Balance sheet item) 60 (P \& L item)

| W5 | Debtors control a/c |  |
| :--- | :--- | ---: |
|  | Shs"000 |  |
| Balance b/d | 500 | Discount allowed |
| Credit sales | 2,050 | Bad debt |
|  |  | Received from debtor |
|  | $\underline{2,580}$ | Bal c/d |


| W6 |  |  |  |
| :--- | ---: | :--- | ---: |
|  | Creditor"s control a/c |  |  |
|  | Shs"000 |  | Shs"000 |
| Payment to creditors | 1,940 | Bal b/d | 380 |
| Discount received | 40 | Credit purchases | 1,900 |
| Bal c/d | $\underline{300}$ |  |  |
|  | $\underline{2,280}$ | $\underline{2,280}$ |  |

## W7

| Provision for doubtful debts a/c |  |  |  |
| :---: | :---: | :---: | :---: |
|  | Shs"000 |  | Shs 000 |
|  |  | Bal b/d | 25 |
| Bal c/d | 30 | $\mathrm{P} \& \mathrm{~L}$ (increase) | 5 |
|  | 30 |  | 30 |

W8
Lighting a/c

|  | Shs"000 |  | Shs"000 |
| :--- | ---: | ---: | ---: |
| Cash | 65 | $\mathrm{Bal} \mathrm{b} / \mathrm{d}$ | 15 |
| Bal c/d | $\underline{9}$ | $\mathrm{P} \& \mathrm{~L}$ | $\underline{69}$ |
|  | $\underline{84}$ |  | $\underline{84}$ |

## QUESTION TWO

## A) Ratios (Profitability Ratio)


ii) Net Profit on Sales =

| $\frac{\mathrm{PBT}}{\text { Net sales }} \times 100 \%$ | $(\underline{12,150} \times 100)$ | $\frac{14,420}{111,350} \times 100 \%$ |
| :--- | :--- | :--- |
|  | $=12.99 \%$ | $12.95 \%$ |
|  | $=13.0 \%$ | $13.0 \%$ |

b) Liquidity ratios
i) Current Ratio $=\frac{\text { Current Assets }}{\text { Current Liabilities }}=\frac{28,300}{14,860}=1.9: 1 \quad \underline{26,564.5}=1.6: 1$
ii) $\quad$ Quick Ratio $=\underset{\text { Current Liabilities }}{\text { C. A. Stocks }}=\frac{15,800}{14,860}=1.1: 1 \quad \frac{14,764.5}{16,243.5}=1: 1$
c) Gearing Ratios

Gearing Ratio
$\begin{aligned}=\frac{\text { Fixed interest capital } \times 100 \%}{\text { Ordinary share capital + Reserves }}= & \frac{3,000}{8.95} \\ & \times 100 \%\end{aligned} \quad=\begin{aligned} & \frac{3,000}{8.5 \%} \times 100 \%= \\ & \\ & \\ & \\ & \end{aligned}$
ii) Debt Equity Ratio =

| Long term liabilities (L.T.L) | 3,000 | $\times 100 \%=9 \%$ | $\underline{3,000} \times 100 \%=$ |
| :---: | :---: | :---: | :---: |
| (Ordinary share capital + Preference <br> share capital + Reserves) |  | 35,490 |  |
|  |  | 35,121 |  |

## d) Activity Ratios

i) Fixed Asset Turnover $=$
$\frac{\text { Sales }}{\text { Net fixed assets }}=\quad \underline{93,500}=4$ times $\quad \frac{111,350}{23,050}=4$ times
ii) Working Capital Turnover =
$\frac{\text { Sales }}{\text { Net Current Assets }}=\frac{93,500}{13,440}=7$ times $\quad \frac{111,350}{10,321}=10$ times

## B) Comment on profitability \& liquidity position (Deweto"s Itd)

i) Profitability

The ratios show a small growth in profitability of the enterprise as portrayed by an increase in
ROCE of $5 \%$ from $33.3 \%$ in 2002 to $38.3 \%$ in 2003 . This indicates that the company has been utilizing it"s assets optimally so as to come up with high profits i.e. the returns fromassets investment has increased.
ii) Liquidity

$$
\begin{aligned}
& \text { Current ratio }=\frac{0.3}{1.9} \times 100=16 \% \text { decline } \\
& \text { Quick ratio }=\frac{0.2}{1.1} \times 100 \%=18 \% \text { decline }
\end{aligned}
$$

The decrease in the two liquidity ratios show that the companies ability to meet its short term maturing obligations (i.e. current liabilities) has decreased and as such the companies operations are riskier now.
The current liabilities have increased at a higher rate than the current assets.

## iii) Gearing

The gearing ratio as indicated by the Debt Equity ratio and the gearing/debt ratio has decreased slightly from $9 \%$ in both cases to $8.5 \%$. This indicates that the companies use of non owner supplied funds i.e. debt has decreased slightly. This means that the company has become less riskier to invest in.
This could have been caused by a decrease in the $15 \%$ loan from Shs $3,000,000$ to Shs $2,500,000$ which may have been due to repayment of part of it. Further the Revenue reserves of 2003 are higher than those of 2002.

## QUESTION THREE

(a)

MAENDELEO SOCIAL CLUB
INCOME \& EXPENDITURE STATEMENT
FOR THE YEAR ENDED 31 ${ }^{\text {ST }}$ OCTOBER 2003

|  | Shs"000 | Shs"000 |
| :--- | ---: | ---: |
| INCOME | 1,500 |  |
| Bar profit (W1) | 36,200 |  |
| Subscriptions (W2) | 200 |  |
| Interest on Bank a/c | 1,600 |  |
| Dance - sales of tickets | $\underline{8,000}$ | $\underline{61,000}$ |
| Food sales |  |  |
| EXPENSES |  |  |
|  | 250 |  |
| Accountancy fees (W3) | 1,400 |  |
| Electricity (W4) | 3,100 |  |
| Telephone (W5) | 600 |  |
| Insurance (W6) | 3,900 |  |
| Depreciation on furniture (W7) | 900 |  |
| Dance expenses | 2,200 |  |
| Office expenses | 4,500 |  |
| Food purchases | 2,000 |  |
| Rates | 14,000 |  |
| Salary \& wages | $\underline{13,000}$ | $(65,650)$ |
| Traveling expenses |  | $(4,650)$ |

MAENDELEO SOCIAL CLUB
BALANCE SHEET
AS AT 31 ${ }^{\text {ST }}$ OCTOBER 2003

|  | COST | DEPRN | NET BK VALUE |
| :---: | :---: | :---: | :---: |
|  | Shs"000 | Shs"000 | Shs"000 |
| NON CURRENT ASSETS |  |  |  |
| Club premises |  |  | 18,000 |
| Furniture | 39,000 | 17,900 | 21,100 |
| CURRENT ASSETS |  |  |  |
| Bar stock | 1,500 |  |  |
| Insurance prepaid | 200 |  |  |
| Subscriptions outstanding | 7,000 |  |  |
| Bank (W8) | 2,700 |  |  |
| Cash | 500 |  | 11,900 |
| TOTAL ASSETS |  |  | 51,000 |
| CAPITAL \& RESERVES |  |  |  |
| Capital (W9) ( Accumulated fund) |  |  | 51,600 |
| Deficit ( Income \& expenditure) |  |  | $\frac{(4,650)}{46,950}$ |
| CURRENT LIABILITY |  |  |  |
| Bar creditors |  | 2,000 |  |
| Accountancy fee accrual |  | 250 |  |
| Electricity accrual |  | 300 |  |
| Subscriptions received in advance |  | 800 |  |
| Telephone outstanding |  | 700 | 4,050 |
| TOTAL EQUITY \& LIABILITIES |  |  | 51,000 |

## WORKINGS

Bar trading account

|  | Shs"000 | Shs"000 |
| :---: | :---: | :---: |
| Bar Sales |  | 55,000 |
| Less Cost of Sales |  |  |
| Opening Stock | 7,000 |  |
| Add Purchases | 24,500 |  |
| Less Closing Stock | (1500) | $(30,000)$ |
| Gross Profit |  | 25,000 |
| Less Expenses |  |  |
| Bar Staff Salaries | 10,000 | $(10,000)$ |
| Bar Profit |  | $\underline{15000}$ |

W2

| Subscriptions A/c |  |  |  |
| :--- | ---: | ---: | ---: |
|  | $\mathbf{S h}^{\prime \prime 000}$ |  | $\mathbf{S h}^{\text {"0000 }}$ |
| Balance B/d | 6,000 | Balance B/d | 1,000 |
| I \& E | 36,200 | Cash | 35,000 |
| Balance C/d | $\underline{43,000}$ | Balance C/d | $\underline{7,000}$ |
|  | $\underline{43,000}$ |  |  |

W3
Accountancy Fee Account

|  | $\mathbf{S h}^{\prime \prime} \mathbf{0 0 0}$ |  | $\mathbf{S h}^{\mathbf{\prime 0 0 0 0}}$ |
| :--- | ---: | :--- | ---: |
| Cash | 200 | Balance b/d | 200 |
| Balance c/d | $\underline{250}$ | I \& E | $\underline{250}$ |
|  | $\underline{450}$ | $\underline{450}$ |  |

W4
Electricity Account

|  | $\mathbf{S h}^{\prime \prime} \mathbf{0 0 0}$ |  | $\mathbf{S h}^{\text {"0000 }}$ |
| :--- | ---: | :--- | ---: |
| Cash | 1,500 | Balance b/d | 400 |
| Balance c/d | $\underline{300}$ | I \& E | 1,400 |
|  | $\underline{1,800}$ |  | 1,800 |

W5
Telephone Account

|  | $\mathbf{S h}$ |  |  |
| :--- | ---: | :--- | ---: |
| Cash | 3,000 | Balance | $\mathbf{S h}^{\mathbf{0 0 0 0 0}}$ |
| Balance c/d | $\underline{700}$ | Income \& | 600 |
|  | $\underline{3,700}$ | Expenditure | $\underline{3,100}$ |
|  |  | $\underline{3,700}$ |  |

W6

| Insurance Account |  |  |  |
| :--- | ---: | ---: | ---: | ---: |
|  | $\mathbf{S h}$ |  |  |
| Balance b/d | 300 | Income \& | $\mathbf{S h}^{\text {"0000 }}$ |
| Cash | $\underline{500}$ | Expenditure | 600 |
|  | $\underline{800}$ |  | $\underline{200}$ |
|  | Balance c/d | $\underline{800}$ |  |

> W7
> Depreciation on Furniture
> $[3500+4000] * 10 / 100=3900$

W8
Sh"000
Bank Account
2,500
Add: Interest Credited

STATEMENT OF AFFAIRS

| STATEMENT OF AFFAIRS |  |  |
| :--- | ---: | ---: |
| Furniture | Sh $^{\text {"000 }}$ |  |
| Club Premises | 21,000 | $\mathbf{S h}^{\text {"000 }}$ |
| Accountancy Fee | 18,000 |  |
| Bar Creditors |  | 200 |
| Electricity Accrual |  | 1,500 |
| Subscriptions in Advance |  | 400 |
| Telephone Accrual | 300 | 1,000 |
| Insurance | 6,000 | 600 |
| Subscription Accrual | 2,500 |  |
| Bank balance | 7,000 |  |
| Bar Stock | $\underline{54,800}$ |  |
| Initial Capital (Accumulated Fund) | $\underline{51,600}$ |  |
|  | $\underline{54,800}$ |  |

## QUESTION FOUR

A) Ledger Accounts

| Application \& allotment a/c |  |  |  |
| :---: | :---: | :---: | :---: |
|  | Shs ${ }^{\text {" } 000}$ |  | Shs ${ }^{\prime \prime} 000$ |
| Bank | 175 | Bank | 4,550 |
| Share premium | 2,500 | Bank | 1,610 |
| Ordinary share capital | 3,500 | Call in arrears | $\underline{15}$ |
|  | 6,175 |  | 6,175 |
| Bank account |  |  |  |
|  | Shs ${ }^{\text {'0 }} 000$ |  | Shs ${ }^{\prime \prime} 000$ |
| Balance b/d | 530 | Application | 175 |
| Application (W1) | 4,550 |  |  |
| Allotment (W2) | 1,610 |  |  |
| $1^{\text {st }} \&$ Final call | 1,491 |  |  |
| Re issue | - 36 | Balance c/d | 8,042 |
|  | 8,217 |  | 8,217 |

1st \& final call a/c

|  | Shs"000 |  | Shs $^{\mathbf{\prime \prime} \mathbf{0 0 0}}$ |
| ---: | ---: | ---: | ---: |
| Ordinary share capital | 1,500 | Bank | 1,491 |
|  | $\underline{1,500}$ | Calls in arrears | $\underline{9}$ |
|  | $\underline{1,500}$ |  |  |

Call in arrears a/c

|  | Shs"'000 |  | Shs $^{\text {"1 }} \mathbf{0 0 0}$ |
| :--- | ---: | :--- | ---: |
| $1^{\text {st } \& ~ f i n a l ~ a / c ~}$ | 9 | Forfeiture | 24 |
| Allotment | $\underline{15}$ |  | $\underline{24}$ |

Forfeiture a/c

|  | Shs $^{\prime \prime} \mathbf{0 0 0}$ |  | Shs $^{\text {" }} \mathbf{0 0 0}$ |
| :--- | ---: | :--- | ---: |
| Calls in arrears | 21 | Re issue | 36 |
| Share premiums | $\underline{12}$ |  | -36 |
|  | $\underline{36}$ | $\underline{36}$ |  |


| Re-issue a/c |  |  |  |
| :--- | ---: | ---: | ---: |
| Forfeiture a/c | Shs $^{\text {"1000 }}$ |  | Shs $^{\prime \prime} 000$ |
|  | $\underline{36}$ | Bank a/c | $\underline{36}$ |

Ordinary share capital

|  | Shs ${ }^{\text {" }} 000$ |  | Shs ${ }^{\text {I' } 000}$ |
| :---: | :---: | :---: | :---: |
|  |  | Application | 3,500 |
| Balc/d | 5,000 | $1{ }^{\text {stt }} \&$ Final $\mathrm{a} / \mathrm{c}$ | 1,500 |
|  | 5,000 |  | 5,000 |

Share premium a/c

|  | Shs | Shs |  |
| ---: | ---: | ---: | ---: |
| Bal c/d | $\underline{2,812}$ | Balance b/d <br> Application | 300 |
| Forfeiture a/c | 2,500 |  |  |
| $\underline{2,812}$ |  | $\underline{12}$ |  |
|  |  | $\underline{2,812}$ |  |

b)

MEZA LTD
BALANCE SHEET
AS AT $21^{\text {ST }}$ OCTOBER 2003

|  | $\begin{array}{r} \text { COST } \\ \text { Shs" } 000 \end{array}$ | ACM DEPRN Shs" 000 | NET BK VALUE Shs" 000 |
| :---: | :---: | :---: | :---: |
| NON CURRENT ASSETS |  |  |  |
| Property, Plants and Equipment |  |  | 7,040 |
| CURRENT ASSETS |  |  |  |
| Stock |  | 2,300 |  |
| Debtors |  | 980 |  |
| Bank |  | 8,042 | 11,322 |
| TOTAL ASSETS |  |  | 18,362 |
| EQUITY \& LIABILITIES <br> CAPITAL \& RESERVES |  |  |  |
| 500,000 ordinary shares of Sh 10 per value |  |  | 5,000 |
| 500,000 ordinary shares of Sh 10 per value |  |  | 5,000 |
| $250,0008 \%$ preference shares of Sh 20 per value |  |  | 5,000 |
| Share premium |  |  | 2,812 |
| CURRENT LIABILITY |  |  |  |
| Creditors |  |  | 550 |
| TOTAL EQUITY \& LIABILITIES |  |  | 18,362 |

## QUESTION FIVE

## EXPLANATIONS

## (I) MATERIALITY

Information or a business item is material if its omission or misstatement would influence the economic decisions of users taken on the basis of financial statements. Materiality depends on the size of item or error judged in the particular circumstances of its omission or misstatement. Thus materiality provides a threshold or cut off point rather than being a primary qualitative characteristic that information must have if its to be useful.
Materiality would be applied to the amount of a trade debt written off as irrecoverable. It could be disclosed by a note if its material. It the materiality concept is not followed, financial statements would be confusing by inclusion of unnecessary trivial details or could be misleading by excluding important matters.

## (II) SUBSTANCE OVERFORM

States that transactions and other events should be accounted for with their substance and not merely with its legal form e.g. under finance lease and the hire purchase agreement.

## (III) MONEY MEASUREMENT

Under this concept, the financial statements are prepared by including only those items which have a monetary value e.g Financial accounting can only deal with items capable of being expressed in monetary items. The concept is relevant in deciding whether or not an asset should be included on the balance sheet.

## B) WHETHER THE FOLLOWING MAY BE RECOGNISED

(I) Goods acquired by a business entity which it confidently expects to resell very quickly
In this case revenue will not be recognised since there has been no sale. In accordance to the prudence concept, gains and revenues are not to be anticipated, they are only recognised when there is a reasonable certainty of their being realised. In this case expectations of being resold quickly does not amount to reasonable certainty that they will be sold.
(II) A customer places a firm order for goods

A sale should not be recognised when a customer places a firm order of goods even though the order will be of a specific quantity of goods \& a specific price, this is because it"s not certain that the sale or the transaction will go through. The customer may cancel the order ot the supplier may be unable to deliver goods ordered. This is in accordance with the prudence concept, that gains will be recognised only when there is a reasonable certainty of their being realised.
(III) Goods are delivered to a customer"s premises

A sale will only be recognised if the customer accepts delivery of the goods to his premises by signing a delivery note. In this case, there can be said to exist a reasonable certainty of the sales revenue being realised since the customer has accepted the goods that he/she had ordered and actually signed a delivery note. In case the customer rejects the delivery of goods then a sale can not be recognised. This is as per the prudence concept.
(IV) The customer"s cheque in payment for the goods has been cleared by the bank In this case where a customer"s cheque in payment for goods has been cleared by the bank, cash has already been received and therefore a sale has occurred and should be recognised. This can be said to be a cash sale as cash has been received and therefore goods should be dispatched to the customer"s premises. In accordance with the realization concept, gain or profit may only be recognised when it has crystallised as a result of the sales proceeds is reasonably assured.

JUNE 2012

## QUESTION ONE

MALI MENGI
TRADING, PROFIT \& LOSS A/C
FOR THE YEAR ENDED 21 ${ }^{\text {ST }}$ MARCH 2004


## Workings

W1 Opening capital $=$ Opening assets-Liabilities
Assets $=480,000+384,000+756,000+144,000+52,800+517,200=\underline{2,564,400}$
Liabilities $=504,000+27,600=\underline{531,600}$
Opening capital $=2,564,400-531,600=2,032,800$

## W2 Purchases

Agency commission receivable $=52,800 @ 1$ 1st May 2004
Purchases $=\frac{100 \% \times 52,800}{10}=5,280,000$ 1 \%

## W3 Sales

| Sales | 100 |
| :--- | :--- |
| Cost | 60 |
| Profit | 40 |

$$
\text { Sales }=\frac{100 \times 4,320,000}{60}=7,200,000
$$

W4

| Bank account |  |  |  |
| :--- | ---: | :--- | ---: |
|  | Shs | Shs |  |
| Bal b/d | 517,200 | Purchases ledger control a/c | $4,728,000$ |
| Commission receivable | 36,000 | Motor vehicle expenses | 806,400 |
| Sales ledger control a/c | $6,957,600$ | Drawings | 516,000 |
|  |  | Trade expenses | 883,200 |
|  | $\underline{7,510,800}$ | Bal c/d | $\underline{577,200}$ |
|  |  | $\underline{7,510,800}$ |  |

Sales ledger control a/c

|  | Shs |  | Shs |
| :--- | ---: | ---: | ---: |
| Discount received | 144,000 | Bal b/d | 504,000 |
| Bank | $4,728,000$ | Purchases | $5,280,000$ |
| Bal c/d | $\underline{912,000}$ |  |  |
|  | $\underline{5,784,000}$ | $\underline{5,784,000}$ |  |

## QUESTION TWO

J KIARIE
MANUFACTURING ACCOUNT AND TRADING, PROFIT \& LOSS ACCOUNT FOR THEY YEAR ENDED 31ST MARCH 2004

|  | Shs"000 | Shs ${ }^{\text {" }} \mathbf{0 0 0}$ |
| :---: | :---: | :---: |
| COST OF RAW MATERIALS |  |  |
| Opening stock |  | 16,200 |
| Add purchases of raw materials | 409,600 |  |
| Add carriage inwards | 7,600 | 417,200 |
|  |  | 433,400 |
| Less closing stock |  | $(15,800)$ |
| Cost of raw materials (overhead) |  | 417,600 |
| Direct costs |  |  |
| Direct labour; Manufacturing wages |  | 92,200 |
| PRIME COST |  | 509,800 |
| Factory Overheads |  |  |
| Depreciation : Plant \& machinery |  | 5,000 |
| PRODUCTION COST/ FACTORY COST |  | 514,800 |
| Sales |  | 795,600 |
| Less Cost of goods sold |  |  |
| Opening stock finished goods | 58,000 |  |
| Add Production cost | 514,800 |  |
| Less Closing stock finished goods | $(63,600)$ | 509,200 |
| GROSS PROFIT |  | 286,400 |
| Add Profit on disposal of motor vehicles |  | 5,600 |
| Discount received |  | 5,000 |
| Decrease in provision for doubtful debts |  | 2,000 |
|  |  | 299,000 |
| Less Expenses |  |  |
| Rent, rates \& insurance | 15,000 |  |
| Salaries | 81,600 |  |
| Discounts allowed | 4,000 |  |
| General expenses | 54,800 |  |
| Professional charges | 3,600 |  |
| Carriage outwards | 9,400 |  |
| Depreciation: Motor vehicle | 3,800 |  |
| Amortisation on leased premises | 7,140 |  |
| Bad debts | 1,000 | 180,340 |
| NET PROFIT |  | 118,660 |


| J KIARIE |  |  |  |
| :---: | :---: | :---: | :---: |
| BALANCE SHEET AS AT 31 ${ }^{\text {ST }}$ MARCH 2004 |  |  |  |
| NON CURRENT ASSETS | SHS | SHS | SHS |
| Leasehold premises | 142,800 | 7,140 | 135,660 |
| Plant \& machinery | 96,000 | 31,800 | 64,200 |
| Motor vehicles | 22,000 | 7,400 | 14,600 |
|  | $\underline{260,800}$ | 46,340 | 214,460 |
| CURRENT ASSETS |  |  |  |
| Stock : Raw materials |  | 15,800 |  |
| Finished goods |  | 63,600 |  |
| Debtors | 32,000 |  |  |
| Less Provision for bad debts | (800) | 24,000 |  |
| Prepayments |  | 400 |  |
| Bank |  | 39,600 | 143,400 |
| TOTAL ASSETS |  |  | 357,860 |
| EQUITY \& LIABILITIES |  |  |  |
| CAPITAL \& RESERVES |  |  |  |
| Capital Opening balance |  |  | 200,000 |
| Add Net profit |  |  | 118,600 |
| Less Drawings |  |  | $(20,800)$ |
|  |  |  | 297,860 |
| Sundry creditors |  | 59,000 |  |
| Accruals |  | 1,000 | 60,000 |
|  |  |  | 357,860 |

WORKINGS
W1
Disposal a/c - motor vehicle

|  | SHS |  | SHS |
| :---: | :---: | :---: | :---: |
| Motor vehicle | 12,000 | Depreciation | 8,000 |
| Profit | 5,000 | Motor vehicle | 9,600 |
|  | 17,600 |  | $\underline{17,600}$ |
| W2 |  |  |  |
| Trade expense a/c |  |  |  |
|  | SHS |  | SHS |
| Prepaid | 14,400 | P \& L | 888,000 |
| Bank | 883,200 | Prepaid | 9,600 |
|  | 897,600 |  | 897,600 |

W3
Lease hold premises cost

| Cost | 140,000 |
| :--- | :---: |
| Legal cost | 2,800 |
|  | $\underline{142,800}$ |

Ammortisation $\underline{142,800}=7,140$
20
W4

| Motor vehicle expense |  |  |  |
| :--- | ---: | ---: | ---: |
|  | SHS | S \& L | SHS |
| Bank | 806,400 | P L | 842,400 |
| Accruals | $\underline{63,600}$ | Accruals b/d | $\underline{27,600}$ |
|  | $\underline{870,000}$ | $\underline{870,000}$ |  |

## QUESTION THREE

## Briefly explain the following types of errors

i. Error of commission

This error is committed when a transaction is entered using the correct amount but the wrong personal account

## ii. Error of principle

Occurs when a transaction is entered in the wrong class of account.
iii. Complete reversal of entry

Occurs when the current amounts are used but the amounts have been entered on the wrong side of the accounts
iv. Compensating errors

This is where errors cancel each other out.

JOURNAL ENTRIES

## DETAILS

1. 
2. Motor vehicle a/c

Motor vehicle expense a/c
Supplies a/c
To correct the error done in posting entries
for purchases of motor vehicles
3. Bank charges

Cash book
To update cashbook with the bank statement
4.

Bad debts recovered
Debtors Ogola
To correct error of principle
5. Discount allowed a/c

Suspense a/c
Suspense a/c
Discount received a/c
To record discount allowed \& received to
their respective accounts
6.

Plant a/c
Plant repairs a/c
To correct error of principle
7. Depreciation expense

Provision for depreciation
To record depreciation charge for the year omitted


| Suspense account |  |  |  |
| :--- | :---: | :--- | ---: |
|  | SHS | SHS |  |
| Discount received | 397,000 | Balance b/d | $4,213,000$ |
| Loan a/c | $\underline{4,000,000}$ | Discount allowed | $\underline{184,000}$ |
|  | $\underline{4,397,000}$ |  | $\underline{4,397,000}$ |

## QUESTION FOUR

## KALAMU, KARATASI \& BARUA PARTNERSHIP

PROFIT \& LOSS A/C FOR THE YEAR ENDED 31ST DEC 2003

|  | For the $1^{\text {st }} 8 \mathrm{mnths}$ |  | For the next 4 mnths |  | For the whole period |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Shs"000 | Shs"000 | Shs"000 | Shs"000 | Shs"000 | Shs" 000 |
| Gross profit |  | 2,800 |  | 1,400 |  | 4,200 |
| Less Expenses |  |  |  |  |  |  |
| Manager"s bonus | 140 |  |  |  | 140 |  |
| Manager"s salary | 400 |  |  |  | 400 |  |
| General expenses | 1,000 |  | 600 |  | 1,600 |  |
| Dpn: Equipment \& motor vehicle | 280 | $(1,820)$ | 100 | 700 | 380 | 2,520 |
| NET PROFIT |  | 980 |  | 700 |  | 1,680 |
| Less interest on capital (8\%) |  |  |  |  |  |  |
| Kalamu | 160 |  | 93.6 |  | 253.6 |  |
| Karatasi | -80 | (240) | 53.6 | (147.2) | 133.6 | 387.2 |
|  |  | 740 |  | 552.8 |  | 1292.8 |
| Share of Profit |  |  |  |  |  |  |
| Kalamu | 370 |  | 176.4 |  | 546.4 |  |
| Karatasi | 370 |  | 176.4 |  | 546.4 |  |
| Barua | - | 740 | 200 | 552.8 | 200 | 1,292.8 |
|  |  | NIL |  | NIL |  | NIL |

Current account

|  | Kalamu | Karatasi | Barua |  | Kalamu | Karatasi | Barua |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Bal b/d | 780 | 710 |  | Bal b/d |  |  | 180 |
| Bank |  |  | 505 | Mngr"s bonus |  |  | 140 |
| Capital a/c |  |  | 300 | Mngr"s salary |  |  | 400 |
| Capital a/c |  |  | 150 | Int on capital 8mts | 160 | 80 |  |
|  |  |  |  | Share of profit | 370 | 370 |  |
|  |  |  |  | 8 mts |  |  |  |
|  |  |  |  | Int on capital | 93.6 | 53.6 |  |
|  |  |  |  | 4 mths |  |  |  |
|  |  |  |  | Share of profit | 176.4 | 176.4 | 200 |
|  |  |  |  | 4mts |  |  |  |
| Bal c/d | 20 |  |  | Bal c/d |  | 30 | 25 |
|  | 800 | 710 | $\underline{955}$ |  | 800 | 710 | $\underline{955}$ |

Capital account

|  | Kalamu | Karatasi | Barua |  | Kalamu | Karatasi | Barua |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Goodwill w/off | 600 | 600 | 300 | Bal b/d | 3,000 | 1,500 | - |
|  |  |  |  | Goodwill | 750 | 750 |  |
|  |  |  |  | Current a/c | - | - | 300 |
|  |  |  |  | Revaluation gain | 360 | 360 | - |
| Bal c/d | 3,510 | $\underline{2,010}$ | 150 | Current a/c |  |  | 150 |
|  | 4,110 | 2,610 | 450 |  | 4,110 | 2,610 | 450 |

## QUESTION FIVE

## BIDII LTD

TRADING, PROFIT, LOSS \& APPROPRIATION A/C FOR THE YEAR ENDED 31 ${ }^{\text {ST }}$ DECEMBER 2003

|  | SHS ${ }^{\prime \prime} 000$ | SHS ${ }^{\prime \prime} 000$ |
| :---: | :---: | :---: |
| Sales |  | 750,000 |
| Less Returns inwards |  | $(3,000)$ |
| Net sales |  | 747,000 |
| Less cost of sales |  |  |
| Opening stock | 200,000 |  |
| Add Purchases | 350,000 |  |
| Carriage inwards | 1,000 |  |
| Less Returns outwards | $(1,000)$ |  |
| Closing stock | $(180,000)$ | $(370,000)$ |
| GROSS PROFIT |  | 377,000 |
| Add Discount received |  | 1,000 |
|  |  | 378,000 |
| Less Expenses |  |  |
| Depreciation: Motor vehicles | 20,000 |  |
| Machinery | 10,000 |  |
| Discounts allowed | 3,000 |  |
| Carriage outwards | 1,000 |  |
| General expense | 198,000 |  |
| Advertising | 10,000 |  |
| Managing Director Private Expenses | 1,000 |  |
| Increase in provision for doubtful debts | 3,000 |  |
| Debenture interest | 10,000 |  |
| Accounting fee | 1,000 |  |
| Bad debts | 20,000 | $(277,000)$ |
| Net profit |  | 101,000 |
| Add Retained profit b/f |  | 100,000 |
| Less Proposed dividends |  | 10,000 |
| Net retained profits ( P \& L a/c) |  | 191,000 |


| BIDII LTD |  |  |  |
| :---: | :---: | :---: | :---: |
| BALANCE SHEET AS AT 31 ${ }^{\text {ST }}$ DECEMBER 2003 |  |  |  |
| NON CURRENT ASSETS | SHS | SHS | SHS |
| Buildings at cost | 260,000 |  | 260,000 |
| Machinery | 120,000 | 60,000 | 60,000 |
| Motor vehicle | 100,000 | 80,000 | 20,000 |
|  | 480,000 | 140,000 | 340,000 |
| CURRENT ASSETS |  |  |  |
| Stock |  | 180,000 |  |
| Debtors | 180,000 |  |  |
| Less provision for bad \& doubtful debts | 9,000 | 171,000 |  |
| Prepayments |  | 1,000 | 352,000 |
| TOTAL ASSETS |  |  | $\underline{692,000}$ |
| EQUITY \& LIABILITIES <br> CAPITAL \& RESERVES |  |  |  |
| Share capital |  |  | 100,000 |
| Retained profits |  | 191,000 |  |
| Share premium |  | 50,000 |  |
| Revaluation reserve |  | 30,000 | 271,000 |
|  |  |  | 371,000 |
| NON CURRENT LIABILITY |  |  |  |
| 10 \% Debentures |  |  | 100,000 |
| CURRENT LIABILITY |  |  |  |
| Proposed dividend |  | 10,000 |  |
| Creditors |  | 200,000 |  |
| Accruals |  | 6,000 |  |
| Bank |  | 5,000 | 221,000 |
| TOTAL EQUITY \& LIABILITIES |  |  | $\underline{692,000}$ |

## Workings

Discounts account

|  | SHS |  | SHS |  |  |  |
| :--- | :---: | :--- | ---: | :---: | :---: | :---: |
| Discount allowed | 3,000 | Discount received | 1,000 |  |  |  |
|  | $\underline{3,000}$ | Bal c/d | $\underline{2,000}$ |  |  |  |
|  |  |  |  |  |  | $\underline{000}$ |

Returns account

| Returns account |  |  |  |
| :--- | :---: | :--- | ---: |
| Returns inward | SHS |  | SHS |
|  | 3,000 | Returns outwards | 1,000 |
|  | $\underline{3,000}$ | Bal c/d | $\underline{2,000}$ |
|  |  | $\underline{3,000}$ |  |

Carriage account

|  | SHS |  | SHS |
| :--- | ---: | :--- | :---: |
| Carriage outwards | 1,000 | Bal c/d | 2,000 |
| Carriage inwards | $\underline{1,000}$ |  | $\underline{2,000}$ |

## DECEMBER 2012

QUESTION ONE

## THE JOURNAL

| Returns Inward <br> Suspense account | 14,000.00 | 14,000.00 |
| :---: | :---: | :---: |
| Creditors account Suspense account | 24,000.00 | 24,000.00 |
| Debtor Account Sales | 216,000.00 | 216,000.00 |
| Expenses Capital Wanjala | 60,000.00 | 60,000.00 |
| Drawings Current Account Okech Purchases | 120,000.00 | 120,000.00 |
| Suspense account Disposal account | 120,000.00 | 120,000.00 |
| Disposals account Non current assets | 600,000.00 | 600,000.00 |
| Provision for depreciation Disposals | 600,000.00 | 600,000.00 |
| Suspense Bank | 240,000.00 | 240,000.00 |

## Suspense account

|  | Shs |  | Shs |
| :--- | ---: | :--- | ---: |
| Disposal | 120.00 | Balance b/f | 720.00 |
| Bank | 240.00 | Creditors | 24.00 |
| Balance c/d | $\underline{398.00}$ | Returns inwards | $\underline{14.00}$ |
|  | $\underline{758.00}$ |  | $\underline{758.00}$ |

## OKECH \& WANJALA

TRADING, PROFIT AND LOSS ACCOUNT
FOR YEAR ENDED 30 ${ }^{\text {TH }}$ JUNE 2004

|  | Shs"000 | Shs"000 |
| :--- | ---: | ---: |
| Sales |  | $13,788.00$ |
| Returns Inwards |  | $(374.00)$ |
| Less Cost of Sales |  | $13,414.00$ |
| Opening stock | - |  |
| Add Factory cost of production | $8,280.00$ | $(8,280.00)$ |
| Less closing stock | - | $\mathbf{5 , 1 3 4 . 0 0}$ |
| Gross profit |  | 120.00 |
|  |  |  |
| Less Expenses | $3,132.00$ |  |
| Operating expense | 60.00 | $\underline{(3,192.00)}$ |
| Expenses |  | $\underline{\mathbf{2 , 0 6 2 . 0 0}}$ |

## OKECH \& WANJALA

BALANCE SHEET
AS AT 30 ${ }^{\text {TH }}$ APRIL 2003

|  | Sh ${ }^{\text {"1 }} 000$ | Sh ${ }^{\text {"000 }}$ | Sh ${ }^{\text {"100 }}$ |
| :---: | :---: | :---: | :---: |
| Non current assets | 4,440.00 | $(2,160.00)$ | 2,280.00 |
| CURRENT ASSETS |  |  |  |
| Stock |  | 2,040.00 |  |
| Debtors |  | $\underline{3,816.00}$ |  |
|  |  | 5,856.00 |  |
| CURRENT LIABILITIES |  |  |  |
| Creditors |  | 2,976.00 |  |
| Bank overdraft |  | 600.00 |  |
|  |  | $(3,576.00)$ | $\begin{aligned} & 2,280.00 \\ & 4,560.00 \end{aligned}$ |
| Capital Okech |  | 1,080.00 |  |
|  |  | 1,260.00 | 2,340.00 |
| 10\% Loan |  |  | 600.00 |
| 10\% Debentures |  |  | 720.00 |
| $\begin{array}{cc}\text { Drawings } & \text { Okech } \\ & \text { Wanjala }\end{array}$ |  | $900.00$ |  |
|  |  | $660.00$ | (1,560.00) |
|  |  |  | 2,100.00 |
| Net Profit |  |  | 2,062.00 |
|  |  |  | 4,162.00 |
| SUSPENSE ACCOUNT |  |  | 398.00 |
|  |  |  | 4,560.00 |

## TRIAL BALANCE

|  | Sh"000 | Sh ${ }^{\text {"000 }}$ |
| :---: | :---: | :---: |
| Capital account Okech |  | 1,080.00 |
| Wanjala |  | 1,200.00 |
| 10\% loan account |  | 600.00 |
| 10\% Debentures |  | 720.00 |
| Drawings Okech | 780.00 |  |
| Wanjala | 660.00 |  |
| Sales |  | 13,572.00 |
| Returns inwards | 360.00 |  |
| Closing stock | 2,040.00 |  |
| Cost of sales | 8,400.00 |  |
| Sales ledger control account | 3,600.00 |  |
| Purchases ledger control account |  | 3,000.00 |
| Operating expense | 3,132.00 |  |
| Non current asset | 4,440.00 |  |
| Provision for depreciation |  | 2,160.00 |
| Bank overdraft |  | 360.00 |
| Suspense |  | 720.00 |
|  | 23,412.00 | $\underline{23,412.00}$ |

## QUESTION ONE

## OKECH \& WANJALA

TRIAL BALANCE AS AT 30 JUNE 2004

|  | DR | CR |
| :--- | ---: | ---: |
| Capital accountsOkech <br> Wanjala |  | 1505 |
| 10\% loan account |  | 1277 |
| $10 \%$ debentures |  | 600 |
|  |  | 720 |
| Sales |  |  |
| Sales inwards | 8,280 | 13,788 |
| Cost of sales | 3,778 |  |
| Debtors |  |  |
| Creditors | 3,192 | 3,000 |
| Operating expenses | 4,440 |  |
| Non current assets |  | 2,160 |
| Provision for depreciation |  | 600 |
| Bank overdraft |  | 60 |
| Short term loan |  |  |
|  |  |  |
|  |  |  |

Suspense account

|  | Shs |  | Shs |
| :--- | ---: | :--- | ---: |
| Bal b/d | 1,500 | Sales returns undercast | 14 |
| Bank overdraft | 240 |  |  |
| Sales undercast | 216 |  |  |

## b) OKECH \& WANJALA

TRADING, PROFIT \& LOSS ACCOUNT
FOR THE YEAR ENDED 30 JUNE 2004


| $10 \%$ loan account: Wanjala | 600 |
| :--- | ---: |
| Current liabilities |  |
| Creditors | 3,000 |
| Bank overdraft | 600 |
| Short term loan | $\underline{60}$ |
| TOTAL EQUITY \& LIABILITIES | $\underline{7,762}$ |

## Workings

1. Adjustments

| Sales account |  |  |
| :--- | :--- | :--- |
| Bal c/d | Shs |  |
| Shs |  |  |
|  | 13,788 | Bal b/d |
| Sales undercast | 13,572 |  |
|  | $\underline{13,788}$ |  |
| 13,788 |  |  |

Sales Returns account

|  | Shs |  | Shs |
| :--- | ---: | ---: | ---: |
| Bal b/d | 360 |  |  |
| Sales undercast (suspense) | 14 | Bal c/d | $\underline{374}$ |
|  | $\underline{374}$ |  | $\underline{374}$ |

Sales Ledger Control account

| Bal b/d Sales | Shs |  | Shs |
| :---: | :---: | :---: | :---: |
|  | 3,600 | Sales Returns | 14 |
|  | 216 | Contra | 24 |
|  |  | Bal c/d | 3,778 |
|  | 3,816 |  | 3,816 |
| Purchases Ledger Control account |  |  |  |
| Bal c/d | Shs | Bal b/d | Shs |
|  | 3,000 |  | 3,000 |
|  | 3,000 |  | 3,000 |
| Bank overdraft a/c |  |  |  |
| Bal c/d | Shs |  | Shs |
|  |  | Bal b/d | 360 |
|  | $\underline{600}$ | Understatement (suspense) | $\underline{240}$ |
|  | $\underline{600}$ |  | 600 |

Disposal account

|  | Shs |  | Shs |
| :--- | :---: | :--- | ---: |
| Cost | 600 | Depreciation | 600 |
| Profit | $\underline{120}$ | Cashbook - bank | $\underline{120}$ |
|  | $\underline{720}$ | $\underline{720}$ |  |

Cost of Sales account

|  | Shs |  | Shs |
| :--- | :--- | :--- | ---: |
| Bal b/d | 8400 | Drawings | 120 |
|  |  | $\underline{8,400}$ | Bal c/d |

Operating Expenses account


Adj: Use of premises $4,812,000-4,000,000=812,000$

| Premises |
| :--- |
| Cash $\quad$ Sh $^{\text {"000 }}$ |
|  |
| $4,000,000$ |


| $\mathbf{1 0 \%}$ Treasury bond |  |  |  |
| :--- | ---: | ---: | ---: |
| $\mathbf{S h}^{\text {" }} \mathbf{0 0 0}$ |  | $\mathbf{S h}^{\text {" }} \mathbf{0 0 0}$ |  |
|  | 9,300 | Investment - sundry income | 700 |
|  |  | Bal c/d |  |
|  | $\underline{10,000}$ | $\underline{10,000}$ |  |

Investment income from treasury bond $=700,000$

Members welfare fund

| Sales | 130 | 9927 |
| :--- | ---: | :--- |
| Cost | 100 | 7636.154 |
| Profit | 30 | 2290.846 |

Bar Trading account

|  | Sh $^{\text {" } \mathbf{0 0 0}}$ | $\mathbf{S h}^{\text {"000 }}$ |
| :--- | ---: | ---: |
| Sales |  | 9,927 |
| Less Cost of sales | Nil |  |
| $\quad$Opening stock <br> Purchases | 7,692 |  |
| Less Closing stock | -326 |  |
| Gross profit |  | $\underline{7,636}$ |

Profit from bar $=$ Sh 2,291,000
Sundry income


## QUESTION TWO

a) The bank statement and cashbook balance should agree, but sometimes may not agree due to:
I.) Unpresented cheque i.e. bank payments drawn by the company which have not yet passed through the banking system.
II.) Bank lodgements not yet entered as receipts to a company in the bank statement.
III.) Credit transfers - These are payments or receipts direct through the banking system without use of cheque.
IV.) Bank charges of services offered by the bank to an account holder which the bank debits from the account.

## Purposes of a Bank Reconciliation Statement

i) To detect any errors either in the cashbook or in the Bank statement sent to the firm
ii) To correct such errors
iii) As a control to know whether the right entries have been done in the cashbook
iv) To let the person to whom it is sent, update his cashbook of all entries not in the Bank statement sent by use of the updated cashbook which is prepared before the Reconciliation statement is prepared.

## Adjusted Cash book

|  | "000 |  | SHS ${ }^{\text {"000 }}$ |
| :---: | :---: | :---: | :---: |
| Balance b/f | 1,710 | Transfers to centralizing bank Overstated $\mathrm{b} / \mathrm{f}$ as at 1.11.03 | 1,110 |
| Overstated payment | 81 |  | 90 |
| Understated receipt | 9 | Overstated $\mathrm{b} / \mathrm{f}$ as at 1.11.03 <br> Bank charges | 18 |
| Unrecorded receipt | 9 | Standing order | 27 |
| Direct debit | 90 | Dishonoured cheque | 45 |
| Understated cheques banked | 18 | Wrong entry of payment Balance c/d | 240 |
|  |  |  | 387 |
|  | 1,917 |  | 1,917 |
| b. |  |  |  |
| Bank reconciliation statement as at 31.10.2004 |  |  |  |
|  |  | Shs"000 | Shs"000 |
| Cash balance as per cashbook |  |  | 387 |
| Add: Unpresented cheque |  | 360 |  |
| Less: Bank lodgement not entered |  | (810) | (450) |
| Balance as per bank statement |  |  | (63) |

## QUESTION THREE

## a) Methods of charging depreciation

i) Straight line method
ii) Reducing balance
iii) Sum of digits method

## I) Straightline method

Under this method the depreciation charge is constant over the life of the asset. The depreciation charge is calculated as follows:

Annual depreciation charge $=\underline{\text { Original cost }- \text { Residual value }}$
Estimated useful life

## II) Reducing balance method

Under this method, a fixed percentage is applied each year to the net book value of the unit at the end of the previous accounting period.
Net book value $=$ Cost - accumulated depreciation of the asset.
To derive the percentage used $=$
$D p=\left(1-n V_{v} / c\right) \times \overline{100} \%$
Where $\mathrm{Dp}=$ depreciation percentage
$\mathrm{n}=$ useful life of the asset (years)
$\mathrm{v}=$ residual value (salvage/scrap value)
$\mathrm{c}=$ cost

## Advantage

The method provides higher depreciation charge in earlier years when repairs expense is lody, thus it evens out the total costs of using the asset.
Shortcomings in using this formula
(i) If there is no residual value Dp becomes $100 \%$
(ii) If the residual value is small relative to cost, Dp becomes a very high percentage.

## III) Sum of Digits Method

This is the variation on the reducing balance method, showing a higher depreciation charge in the early years of the life of the asset.
Formula:
To obtain the sums of digits for any number of years: $\underline{n(n+1)}=$ Sum of digits

2
Thus the sum of digits for 5 years $=\underline{5(5+1)}=152$
b) Property, plant \& equipment disposal account for the year ended
30.6.04 Disposal account

|  | SHS ${ }^{\text {"000 }}$ |  | SHS ${ }^{\text {"000 }}$ |
| :---: | :---: | :---: | :---: |
| Equipment | 150,000 | Accumulated depreciation: |  |
| Motor vehicle | 60,000 | Equipment | 120,000 |
| Furniture | 70,000 | Motor vehicle | 36,000 |
| Old truck | 15,000 | Furniture | 35,000 |
|  |  | Cash proceeds Equipment | 25,000 |
|  |  | Motor vehicle | 15,000 |
|  |  | Furniture | 45,000 |
|  |  | Accumulated depreciation: Old truck (W1) | 13,500 |
|  |  | Accumulated depreciation of reclassified equipment | 3,000 |
|  |  | Profit \& loss a/c | 2,500 |
|  | 295,000 |  | 295,000 |

c) Property, Plant \& Equipment Schedule

|  | Equipment Shs" 000 | Furniture Shs"000 | Motor vehicle Shs"000 |
| :---: | :---: | :---: | :---: |
| Cost | 700,000 | 140,000 | 140,000 |
| Additions |  |  |  |
| Equipment | 175,000 |  |  |
| Furniture |  | 15,000 |  |
| Motor vehicle |  |  | 25,500 |
|  | 875,000 | $\underline{155,000}$ | 165,000 |
| Less Disposals |  |  |  |
| Equipment | 150,000 |  |  |
| Motor vehicle |  |  | 60,000 |
| Furniture |  | 70,000 |  |
| Equipment | 15,000 |  |  |
| Old truck |  |  | 15,000 |
|  | $(165,000)$ | $(70,000)$ | $(75,000)$ |
|  | 710,000 | 85000 | 90000 |
| Less Accumulated depreciation |  |  |  |
| Equipment | $(336,000)$ |  |  |
| Furniture |  | $(70,000)$ |  |
| Motor vehicle |  |  | $(98,000)$ |
| Add accumulated depreciation on disposal Equipment | 123,000 |  |  |
| Furniture |  | 35,000 |  |
| Motor vehicle |  |  | 49,500 |
| Less Depreciation charge for the year |  |  |  |
| Equipment | $(142,000)$ |  |  |
| Furniture |  | $(10,625)$ |  |
| Motor vehicle |  |  | $(27,150)$ |
| Provision for depreciation $\mathrm{c} / \mathrm{f}$ | 355,000 | 45,625 | 75,650 |
| NBV as at 30.6.04 | 355,000 | 39,375 | 14,350 |

## Workings

1. Depreciation per year $=15 \times 0.3=4.5$

$$
\text { For } 3 \text { years }=4.5 \times 3=13.5
$$

## QUESTION FOUR

a) Distinction between reserves and share capital RESERVES
i) Consists of those unused profits remaining in appropriation account or transferred to a reserve account such as general reserve, fixed assets replacement, reserve etc
ii) Some reserves can be distributed as dividends
iii) Some reserves result from appropriation of profits
iv) Changes in reserves may not affect the company"s cash flow
v) No dividends are payable on reserves

## SHARE CAPITAL

Is a unit of ownership and includes ordinary share capital and preference share capital

Cannot be distributed as dividends

Results from a capital issue to the public or shareholder

Changes in share capital will reflect an increase or decrease on cash resources

Share capital earns a return in the form of dividends

PLASTICS LTD
INCOME STATEMENT
FOR THE YEAR ENDED $31^{\text {ST }}$ OCTOBER 2004

|  | SHS"000 | SHS ${ }^{\prime \prime} 000$ |
| :---: | :---: | :---: |
| Gross profit |  | 25,000 |
| Other operating income |  | 4,000 |
|  |  | 29,000 |
| Less: Operating expense |  |  |
| Debenture interest ( $400+400$ ) | 800 |  |
| Administrative expenses | 13,000 |  |
| Distribution costs | 6,000 |  |
| Other operating expenses | 1,550 | (21,350) |
| Net profit before tax |  | 7,650 |
| Less corporation tax |  | $(2,500)$ |
| Profit after tax |  | 5,150 |
| Retained profits b/f |  | 3,000 |
|  |  | 8,150 |
| Less: Interim paid : Preference shares Ordinary shares | 450 2,000 |  |
| Final dividend: Preference shares | 450 |  |
| Ordinary shares | $\underline{2,000}$ | (4,900) |
| Retained profit c/d |  | 3,250 |

PLASTICS LTD
BALANCE SHEET
AS AT 31 OCTOBER 2004

|  | SHS"000 | SHS ${ }^{\text {"000 }}$ |
| :---: | :---: | :---: |
| NON CURRENT ASSETS |  |  |
| Land and buildings | 29,000 |  |
| Plant and machinery | 8,000 |  |
| Motor vehicles | 2,000 | 39,000 |
| CURRENT ASSETS |  |  |
| Inventory | 6,000 |  |
| Accounts receivables | 20,000 |  |
| Cash at bank | 4,100 | 30,100 |
| TOTAL ASSETS |  | $\underline{69,100}$ |
| EQUITY \& LIABILITIES |  |  |
| Capital \& Reserves |  |  |
| Share capital: Ordinary shares | 10,000 |  |
| Preference shares | $\underline{9,000}$ | 19,000 |
| RESERVES |  |  |
| Revaluation reserve | 4,000 |  |
| Capital redemption reserve | 6,000 |  |
| Share premium | 4,000 |  |
| Retained profit $\mathrm{c} / \mathrm{f}$ | 3,250 | $\underline{17,250}$ |
|  |  | 36,250 |
| NON CURRENT LIABILITIES |  |  |
| 10\% debentures |  | 8,000 |
| CURRENT LIABILITIES |  |  |
| Accounts payable | 19,000 |  |
| Cooperatives tax payable (W1) | 3,000 |  |
| Debenture interest payable | 400 |  |
| Preference dividend payable | 2,450 | 24,850 |
| TOTAL EQUITY \& LIABILITIES |  | $\underline{69,100}$ |

## WORKINGS

1. 

## Corporation tax payable

|  | Shs"000 |  | Shs"000 |
| :--- | ---: | ---: | ---: |
| Bal c/d | $\underline{3,000}$ | Bal b/f | To P \& L a/c |
|  | $\underline{3,000}$ |  | $\underline{2,500}$ |
|  | $\underline{3,000}$ |  |  |

## QUESTION FIVE

a) Meaning of Prudence Concept

In accordance to the IFRS (International Financial Reporting Standards), prudence has been defined as the inclusion of a degree of caution in the exercise of judgements needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated.
This means that losses are recorded when anticipated but profits are recorded only when they are actually realized. This means that the figure that understates profits and not which will overstate profits should be taken. When dealing with stocks, the prudence concept is applied where the lower of cost or net realizable value of stocks is taken.
However, the exercise of prudence does not allow, for example, the creators of hidden reserves or excessive provisions, the deliberate understatement of assets, or income, or the deliberate overstatement of liabilities or expenses because the financial statements would not be neutral and therefore not have the quality and reliability.
b)

Shs"000
2003
$\frac{5,000}{20,000} \times 100=25 \%$
$\frac{15,000}{(5,000+2,000) \div 2}=4.29$ times
$\frac{21,000}{(2,000+3,000) \div 2}=8.4$ times
3 Return on equity $=$
Net profit+debenture int x100
Average shareholders funds
$\frac{1,200}{13,000} \times 100 \%=9.23 \%$
13,000
$2000+400 \times 100=17.7 \%$
$(13000+14100) \div 2$

4 Return on assets

5 Acld test ratio $=$

Current Assets - Stock
Current liabilities
6 Current ratio $=$
Current Assets
Current liabilities
$\underline{4,500-2,000}=1: 1$
2,500
$\underline{4,500}=1.8: 1$
2,500
$\frac{6,300-3,000}{1,200}=2.75: 1$
$\underline{6,300}=5.25: 1$
1,200

7 Financial gearing/leverage
c) This is indicated by the Acid test ratio and the Current ratio

Both have improved as indicated by the calculations i.e.
Acid test ratio from 1:1 to 2.73:1 and the Current ratio from 1.8:1 to 5.25:1
This is because the current assets in the year 2004 increased while the current liabilities decreased.
This indicates that the company is now in a better position to pay all it"s short term liabilities on time.

JUNE 2013

## QUESTION ONE

a)

Chacha and Muchi Partnership
Manufacturing and Trading, Profit and loss and Appropriation account For the year ended 31 December 2004

|  | Shs | Shs | Shs |
| :---: | :---: | :---: | :---: |
| COST OF RAW MATERIALS |  |  |  |
| Opening stock |  | 1,500 |  |
| Purchases | 40,000 |  |  |
| Add Carriage inwards | 500 | 40,500 |  |
|  |  | 42,000 |  |
| Less Closing stock |  | $(2,000)$ |  |
| Cost of raw materials consumed |  |  | 40,000 |
| Direct costs |  |  |  |
| Direct Production wages |  |  | $\underline{10,000}$ |
|  |  |  | 50,000 |
| Factory overheads |  |  |  |
| Factory manager"s salary |  | 480 |  |
| Factory rates and insurance (W1) |  | 1,000 |  |
| Depreciation |  |  |  |
| Factory buildings (W2) | 20 |  |  |
| Plant and machinery (W3) | 700 | 720 |  |
|  |  | 2,200 | 2,200 |
|  |  |  | 52,200 |
| Work in progress |  |  |  |
| Opening | 2,200 |  |  |
| Closing | $(4,200)$ |  | $(2,000)$ |
| Cost of goods manufactured |  |  | 50,200 |
| Manufacturing profit (W4) |  |  | 12,550 |
| Transfer price |  |  | 62,125 |
| Sales |  |  | 86,240 |
| Less: Cost of sales |  |  |  |
| Opening stock |  | 1,200 |  |
| Manufacturing account |  | 62,750 |  |
|  |  | 63,950 |  |
| Less Closing stock |  | $(1,000)$ |  |
| Cost of sales |  |  | (62,950) |
| Gross profit |  |  | 23,290 |
| Factory profit |  |  | 12,550 |
|  |  |  | 35,840 |
| Less: Expenses |  |  |  |
| Office salaries |  | 5,000 |  |
| Royalties |  | 1,000 |  |
| Distribution costs |  | 3,250 |  |
| Rates and insurance (W5) |  | 490 |  |
| Fuel and electricity |  | 800 |  |
| Bad debts |  | 20 |  |
| Increase in provision for bad debts (W6) |  | 20 |  |
| Depreciation: |  |  |  |
| Motor vehicle (W7) |  | 350 |  |
| Provision for unrealized profit |  | 10 | $\underline{11,400}$ |
| Net profit from trading |  |  | 24,900 |
| Appropriation: |  |  |  |
| Commission: Mushi ( $10 \% \times 12,550$ ) |  | 1,255 |  |
| : Chacha ( $10 \% \times 24,670$ ) |  | 2,490 |  |
| Partnership salary: Mushi |  | 15,000 |  |
| Interest on capital: Chacha |  | 400 |  |
| Mushi |  | 400 |  |



Current Account

| Current Account |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
| Balance b/d | A | M 100 | Balance b/d | A 500 | M |
| Drawings | 200 | 300 | Commission | 2,490 | 1,255 |
|  |  |  | Interest on capital | 400 | 400 |
|  |  |  | Salary |  | 15,000 |
| Balance c/d | $\underline{5,867.5}$ | 18,932.5 | Share of profit | 2,677.5 | $\underline{\text { 2,677.5 }}$ |
|  | $\underline{6,067.5}$ | 19,332.5 |  | 6,067.5 | 19,332.5 |

b)

Chacha and Mushi Partnership
Balance sheet as at 31 Dec 2004

## ASSETS

## Non current assets

Land
Factory and building ( $1,000-(40+20))$
Delivery van (1,400 - (350 + 700)
Plant and machinery $(3,500-(1,400+700)$

## Current assets

Stock:
Raw materials
Work in progress
Finished goods
Less provision for unrealized profit
Debtors
Less provision for bad debts
Prepaid insurance
Bank
TOTAL ASSETS
EQUITY AND LIABILITIES
Capital and Reserves
Capital: Chacha
Mushi
Current accounts: Chacha

## Current liabilities

Creditors
Accrued rate


## Workings <br> W1

Factory rates and insurance 700
Less prepaid (200)
500
Add owing $\underline{500}$
1,000
W2
Depreciation on buildings

$$
2 \% \times(18,000-17,000)=20
$$

## W3

Plant and machinery
$20 \% \times 3,500=700$
W4
Profit $=25 \% \times 50,200=12,550$

W5
Rates and Insurance $=$ Shs 500
Add: Accrued $\frac{25}{525}$
Less: Prepaid 490

W6
Provision for bad debts

$$
5 \% \times(800)=40
$$

Increase in provision $=40-20$

$$
=20
$$

W7
Depreciation on motor vehicles

$$
25 \% \times 1,400=350
$$

W8
Unrealised profit $=25 \% \times 100=250$

## QUESTION TWO

WASOMAJI MEMBER"S CLUB
INCOME \& EXPENDITURE ACCOUNT
FOR THE YEAR ENDED 31 DECEMBER 2004

|  | SHS | SHS |
| :--- | ---: | ---: |
| INCOMES |  | 13,200 |
| Subscriptions income (W1) | 2,290 |  |
| Profit from bar (W2) | 100 |  |
| Interest income from fixed deposit a/c |  | 1,289 |
| Other income: revaluation surplus (W3) |  | 16,879 |
|  | 812 |  |
| EXPENDITURE | 783 |  |
| Use of premises | 2,080 |  |
| Printing, postage \& stationery | 20 |  |
| Wages | 1,200 |  |
| Depreciation | $\underline{120}$ |  |
| $\quad$ Club premises (W4) |  | $(5,015)$ |
| $\quad$ Minibus |  |  |
| Subscriptions written off | $\underline{11,864}$ |  |
| Surplus |  |  |



## W2

Profit from bar
The bar sales stock at a markup of $30 \%$
Sales $=$ Sh 9,927

|  | $\%$ | Shs"000 |
| :--- | ---: | :--- |
| Cost | 100 | $\frac{9,927}{130} \times 100=7,636$ |
|  |  | $\underline{9,927} \times 30=2,290$ |
| Profit | 30 | 130 |
| Selling price | 130 | 9,927 |
| Profit therefore $=[9,927 / 130 \times$ | $30]=2,290$ |  |

W3
Revaluation surplus

# Library \& Furniture 

|  | Shs"000 |  | Shs"000 |
| :--- | ---: | ---: | ---: |
| Bal b/d | 1,380 |  |  |
| Reference books | 2,331 |  | $\underline{5,000}$ |
| Revaluation surplus | $\underline{1,289}$ | Bal c/d | $\underline{5,000}$ |

## W4

Depreciation on club premises

$$
\begin{aligned}
& =\frac{4,000}{50} \times \frac{3}{12} \\
& =20
\end{aligned}
$$

Note; The premises were acquired on $1^{\text {st }}$ October 2004 and the depreciation value is $2 \%$ per annum or $(1 / 50)$

## W5

Netbook value of minibus

| Cost | 6,000 |
| :--- | ---: |
| Accumulated depreciation | $\frac{(2,400)}{3,00}$ |

## W6

Bar stocks

## Bar Trading a/c



W7
Use of premises $=4,812,000-4 \mathrm{~m}=812,000$

## QUESTION THREE

| Bank account (extract) |  |  |  |  |
| :--- | :--- | ---: | :--- | ---: |
| 2004 |  | Sh"000 | 2004 |  |
| 5 April | Application | 2,650 | 5 April | Application |
| 30 April | Allotment | 1,000 |  |  |
| 31 May | Calls in advance | 25 |  | Sh"000 |
| 31 Oct | Second \& final call | $\underline{1,415}$ | 31 Dec | Bal c/d |
|  | $\underline{5,090}$ |  |  |  |
| 2005 |  | 4,940 |  | $\underline{4,940}$ |
| 1 Jan | Bal b/d | 60 |  | $\underline{5,090}$ |
| 31 Jan | Calls in arrears | 1.5 |  |  |
| 31 Jan | Interest |  |  |  |

Application account

| 2004 |  | Sh"000 | $\begin{aligned} & 2004 \\ & 5 \text { April } \end{aligned}$ | Bank | Sh"000 |
| :---: | :---: | :---: | :---: | :---: | :---: |
| 5 April | Bank | 150 |  |  | 2,650 |
| 30 April | Ordinary share capital | 1,000 |  |  |  |
| 30 April | Calls in advance | 1,500 |  |  |  |
|  |  | 2,650 |  |  | 2,650 |

Allotment account

| 2004 |  | Sh"000 | 2004 |  | $\mathbf{S h}^{\prime \prime 000}$ |
| :--- | :--- | ---: | :--- | :--- | ---: |
| 30 April | Ordinary share capital | 1,000 | 30 April | Bank | 1,000 |

Ordinary Share Capital

| 2004 | Bal c/d | Sh"000 | 2004 |  | Sh"000 |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  |  |  | 30 April | Application | 1,000 |
|  |  |  | 30 April | Allotment | 1,000 |
|  |  |  | 31 July | First call | 1,500 |
| 31 Dec |  | 5,000 | 31 Oct | Second \& Final call | 1,500 |
|  |  | 5,000 |  |  | 5,000 |

Calls in Advance

| 2004 |  | Sh"000 | 2004 |  | Sh"000 |
| :---: | :---: | :---: | :---: | :---: | :---: |
| 31 July | First call | 1,500 | 30 April | Application | 1,500 |
| 31 Oct | $2^{\text {nd }}$ and final call | 25 | 31 May | Bank | 25 |

Calls in Arrears

| 2004 |  | Sh"000 | 2004 |  | Sh"000 |
| :---: | :---: | :---: | :---: | :---: | :---: |
| 31 Oct | $2^{\text {nd }}$ and final call | 60.0 |  |  |  |
| 31 Dec | Interest | 1.0 | 31 Dec | Bal c/d | 61.0 |
|  |  | 61.0 |  |  | 61.0 |
| 2005 | Bal b/d | 61.0 | 2005 | Interest a/c | 1.5 |
| 31 Jan | Interest | -0.5 | 31 Jan | Bank | 60.0 |
|  |  | 61.5 |  |  | 61.5 |

First call

| 2004 |  | $\mathbf{S h}^{\prime \prime} \mathbf{0 0 0}$ | 2004 |  |  |
| :--- | :--- | ---: | :--- | :--- | :--- |
| 31 July | Ordinary share capital | $\underline{1,500}$ | 31 July | Calls in advance | $\mathbf{S h}^{\prime \prime} \mathbf{0 0 0}$ |
|  |  |  |  |  |  |

Second and Final Call

| 2004 | Ordinary share capital | Sh"000 | 2004 |  | Sh"000 |
| :---: | :---: | :---: | :---: | :---: | :---: |
| 31 Oct |  | 1,500 | 31 Oct | Calls in advance | 25 |
|  |  |  | 31 Oct | Bank | 1,415 |
|  |  |  | 31 Oct | Calls in arrears | 60 |
|  |  | 1,500 |  |  | 1,500 |

P \& L account (extract)

| 2005 |  | Sh"000 | 2005 | Sh'000 |
| :---: | :---: | :---: | :---: | :---: |
| 31 Jan | Interest a/c | 1.5 |  |  |

## Interest account

| 2005 |  | $\mathbf{S h}^{\prime \prime} \mathbf{0 0 0}$ | 2005 |  |  |
| :--- | :--- | ---: | :--- | :--- | ---: |
| 31 Jan | Bank | $\underline{1.5}$ | 31 Jan | Calls in arrears | $\underline{S^{\prime \prime} 000}$ |

Workings

1) Application monies received $=530,000 \times 5=2,650,000$
2) Refunded $=30,000 \times 5=150,000$
3) Calls in advance by shareholder $=25,000$
4) Interest charged on calls in arrears $=8,000 \times 7.5 \times 10 \% \times 3 / 12=\underline{1,500}$

## QUESTION FOUR

## Advantages of maintaining control accounts

I) To extract balances of debtors and creditors quickly for the trial balance.
II) To check and correct errors

This is done due to the fact that a control account records the amount of debtors and creditors anew. This balance is compared with that from the ledger accounts. If they agree then there is no error, but if they don"t agree then there is an error which needs correction.
III) To detect any fraud in debtors and creditors

This is done by the process of correction of errors.
IV) To facilitate delegation of duties to both the sales ledger and purchase ledger

Sales ledger control A/c

|  | Sh. |  | Sh. |
| :--- | ---: | :--- | ---: |
| Bal b/d | $1,428,000$ | Bal b/d | 40,000 |
| Credit sales | $2,068,200$ | Discounts allowed | 209,700 |
| Dishonoured cheques | 26,100 | Returns inwards | 75,000 |
| Interest on overdue accounts | 96,000 | Contra transfer | 36,900 |
| Debt collection expenses | 10,800 | Receipts from customers | $1,578,000$ |
|  |  | Bad debts w/0 | 37,200 |
| Bal c/d | $\underline{50,700}$ | Bal c/d | $\underline{2,002,500}$ |
|  | $\underline{3,979,800}$ |  | $\underline{3,979,800}$ |

## Purchases ledger control A/c

|  | Sh. |  | Sh. |
| :--- | ---: | :--- | ---: |
| Bal b/d | 10,500 | Bal b/d | 553,800 |
| Discount received | 142,500 | Purchases | $1,182,000$ |
| Contra transfer | 36,900 | Interest on accounts | 69,000 |
| Payments to creditors | $1,159,200$ |  |  |
| Returns outwards | 26,700 |  |  |
| Bal c/d | $\underline{440,400}$ | Bal c/d | $\underline{14,400}$ |
|  | $\underline{1,819,200}$ |  | $\underline{1,819,200}$ |

## QUESTION FIVE

## a) The importance of Ratio analysis

I.) Evaluation of performance

By use of ratio analysis a company is able to compare its performance with its past performance (vertical analysis) or even with other companies falling in the same industry (horizontal analysis)
II.) Acts as control

Ratios are at times used as controls by companies. The employees of a company are given goals which they need to attain. At the end of the accounting period their performance is reviewed with an aim of finding what the problem might have been.

## b) Parties interested in the following Ratios

I) Current Ratio

The current ratio measures the liquidity position of a business. The creditors would be interested in it so as to know the probability of their debt being paid.
II) Net Profit Margin

This measures the profitability of a company. Almost all parties are interested in this ratio from the company itself to the government, employers, creditor, the general public at large, potential investors etc.,. It helps to know whether to invest in the company i.e. the investors and public; future prospects for the employees etc.,
III) Stock Turnover

This represents how fast the company is able to turn stocks to sales. The company management and even potential investors are interested in this. Further the suppliers would like to know this so as to know how frequently they ought to supply goods.
c) Brief explanation of the following:
I) Accounting concepts

These are broad assumptions which underlie preparation of financial statements of a company.
Examples of accounting concepts include the Historical Concept, Prudence, Accrual Basis etc.,
II) Accounting standards

They are authoritative statements of how particular types of transactions and events should be reflected in financial statements. They are developed to achieve comparability of financial information between and among different organizations.
III) Accounting policies

These are the principles, bases, conventions, rules and practices applied by an entity that specify how the effects of transactions and other events are to be reflected jin its financial statements though
i) Recognising
ii) Selecting measurement basis for a/c
iii) Presenting
assets, liabilities, gains, losses and charges to shareholders funds.

## d) Explanation of Accounting Treatments

I) The debtor declared bankrupt

In the books of Mlachake ltd by 31 December 2004, the balance sheet shows debtor"s figure of Sh. 200,000. This was on assumption that such debtors would be recoverable. The declaration of the debtor bankrupt reduced the chances of realization of the debt. However this declaration is done after the balance sheet date. In accordance to International Financial Reporting Standards, this is an event after the balance sheet and it provides additional evidence of the conditions as they existed at the balance sheet date. This therefore is an adjusting event and therefore the following adjustments should be made:
(I) $75 \%$ of the debt (Sh 200,000 ) should be written off in the income statement as a bad debt
(II) Bad debts recovered of $25 \%$ of $\mathrm{Sh} 200,000$ should be recognised. However, if the financial statements had been finalised to the point that the reports had been sent to stakeholders and shareholders, then it should be disclosed by way of note.
II) The inventory which got damaged

Such inventory which has been damaged should be valued at the lower of cost and net realizable value. Further the cost of repairing the inventory should be incorporated in the cost of the inventory. As such, this would be consistent with Accounting Standard No. 2 which deals with inventories.
III) The secured order of Ksh. 12 million

In accordance to the Prudence concept, revenue/gains are recognised if their realisation can be determined with reasonable certainty. In this case, the fact that a foreign based company secured an order for goods to be later demonstrates commitment of the customer to buy the goods. However the commitment is not enough to warrant the recognition of the sale in our books of account.
Therefore it was not proper for the sale to be recognised in December as it was since as at December $19^{\text {th }}$ the Sale was still uncertain.
Those goods should only have been recognised for the month of January which is when their sale became certain.

## FINANCIAL ACCOUNTING 1

## DECEMBER 2013 SOLUTIONS

## QUESTION ONE

## ARAKA LIMITED

TRADING PROFIT AND LOSS ACCOUNT
For the year ended 30/9/2005

## Sales

Less cost of sales
Opening inventory
Purchases

Less closing inventory
Gross profit
Gain on disposal
Shs. „000"
Shs. ,000
1,312,567

Bad debt recovered
41,912
839,004
880,916
$(62,047)$
$(818,869)$
493,698
1,375
612
495,685

## Expenses

Electricity
6,917
Motor expenses $(4,174+412) \quad 4,586$
Sundry expenses $(2,002+91) \quad 2,093$
Salaries and wages $(121,600+36) \quad 121,636$
Directors" remuneration 48,888
Bank charges $(1,621+533) \quad 2,154$
Depreciation: Freehold building W3 8,620
Plant and machinery W3 9,620
Motor vehicle W3 7,450
Bad debts $(1,370+512) \quad 1,882$
Provision for bad debts W2 1,194
Profit before tax
$(215,040)$

Corporation tax
Profit after tax
$(131,700)$
Less proposed dividend
Retained profit for the year
$(5,000)$

Retained profit b/f
Retained profit c/f
296,057
440,002

## Araka Limited

Balance Sheet
As at 30/9/2005

| Non-current assets | Cost | Depreciation | NBV |
| :--- | ---: | ---: | ---: |
| Freehold land | 121,500 | - | 121,500 |
| Freehold buildings | 431,000 | $(77,580)$ | 353,420 |
| Plant and machinery | 64,172 | $(25,694)$ | 38,478 |
| Motor vehicles | $\underline{29,800}$ | $\underline{117,287)}$ | $\underline{12,513}$ |
|  | $\underline{646,472}$ | $\underline{120,561}$ | $\underline{525,911}$ |

## Current assets

| Inventory | 62,047 |
| :--- | ---: |
| Accounts receivable $(59,704-1,194)$ | 58,510 |
| Cash in hand $[1,268-(412+91+36)] \mathrm{N} 9$ | 729 |
| Cash at bank $(1,210-533) \mathrm{N} 4$ | $\frac{677}{121,963}$ |

## Current liabilities

| Accounts payable | 21,172 |  |  |
| :--- | ---: | ---: | ---: |
| Tax payable | 131,700 |  |  |
| Proposed dividends | $\underline{5,000}$ | $\underline{(157,872)}$ | $\underline{(35,909)}$ |
|  |  | $\underline{490,002}$ |  |
| Ordinary share |  | 50,000 |  |
| Retained profits |  | $\underline{440,002}$ |  |
|  |  | $\underline{490,002}$ |  |

## Workings:

1. Gain on sale of motor vehicles

Disposal of vehicles A/c

| Dr. | Sh. „000" |  | $\begin{array}{r} \text { Cr. } \\ \text { Sh. „ } 000^{\prime \prime} \end{array}$ |
| :---: | :---: | :---: | :---: |
| Cost | 6,500 | Depreciation | 4,875 |
| Profit and loss | 1,375 | Bank | 3,000 |
|  | 7,875 |  | 7,875 |

Depreciation $=6,500 \times 25 \% \times 3$ years $=$ Shs. 4,875
2. Accounts receivable

As per trial balance
Less bad debts W/o
General provision $2 \% \mathrm{x}(61,074-1,370)$

Sh. „000"
Sh. „000"
61,074
1,370
$1,194 \quad(2,564)$
58,510
3. Depreciation of non-current assets

Freehold building $\quad 20 \% \times 431,000$
Sh. „000"
Plant and machinery $20 \% \times[64,172-16,074]$
8,620
Motor vehicles $\quad 25 \%[28,900-6,500+7,400]$
9,620
7,450

## QUESTION TWO

# Omondi, Maina and Ombati <br> Trading, Profit and Loss and Appropriation A/C <br> For the year ended 31/10/05 

|  | Shs. „000" | Shs. „000 ${ }^{\text {" }}$ |
| :---: | :---: | :---: |
| Sales |  | 248,000 |
| Cost of sales |  |  |
| Opening inventory | 16,000 |  |
| Purchases | 192,000 |  |
|  | 208,000 |  |
| Less: Closing inventory | $(19,000)$ | 189,000 |
|  |  | 59,000 |
| All decrease in provision for doubtful debts W1 |  | 500 |
|  |  | 59,500 |
| Expenses |  |  |
| Wages | 20,000 |  |
| Salaries | 10,000 |  |
| General expenses | 9,000 |  |
| Depreciation: Plant and machinery | 2,400 |  |
| Motor vehicles | 1,880 | 43,280 |
| Net Profit |  | 16,220 |


|  | 4 months to 28/2/05 |  | 8 months to 31/10/05 |  | Total 12 months |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Shs. „000" | Shs. „000" | Shs. „000" | Shs. „000" | Shs. „000" | Shs. „000" |
| Net profit |  | 5,407 |  | 10,813 |  | 16,220 |
| Less: |  |  |  |  |  |  |
| Salaries: Omondi | 833 |  | 1,667 |  | 2,500 |  |
| Maina | 833 |  | 1,667 |  | 2,500 |  |
| Ombati | - | $(1,666)$ | 1,333 | $(4,667)$ | 1,333 | $(6,333)$ |
|  |  | 3,741 |  | 6,146 |  | 9,867 |
| Share of profits W2 |  |  |  |  |  |  |
| Omondi | 2,245 |  | 3,208 |  | 5,453 |  |
| Maina | 1,496 |  | 2,138 |  | 3,634 |  |
| Ombati | - | $(3,741)$ | $\underline{800}$ | $(6,146)$ | $\underline{800}$ | $(9,867)$ |

## Workings:

Provision for bad debts
$5 \% \times 18,000=900$
less provision $\mathrm{b} / \mathrm{f} \quad(1,400)$
Decrease in provision
Share of profit from February 2005 to October 2005
Share of profit from February 2005 to October 2005


## QUESTION THREE

a) Purposes of ratio analysis

- Assessing the company"s financial performance
- To evaluate financial stability of a company
- To predict future performance and stability of a business entity
- To compare performance of the firm with past performance and within the industry.
- To detect and investigate inconsistencies due to errors and fraud.
b)

| Ratio | Formula | Sunrise Ltd. | Sunset Etd. |
| :---: | :---: | :---: | :---: |
| i) Acid test ratio | Current asset - Inventory Current Liability | $\begin{aligned} & \frac{186-100}{98} \\ & =0.88: 1 \end{aligned}$ | $\begin{aligned} & \frac{173-87}{108} \\ & =0.80: 1 \end{aligned}$ |
| ii) Inventory turnover | Cost of sales Average stock | $\begin{aligned} & \frac{258}{100} \\ & =2.58 \end{aligned}$ | $\begin{aligned} & \begin{array}{l} \frac{153}{87} \\ =1.76 \end{array} \end{aligned}$ |
| iii) Average collection period | $\frac{365 \times \text { Average debtors }}{\text { Credit sales }}$ | $\begin{aligned} & \frac{365 \times 46}{497} \\ & 34 \text { days } \end{aligned}$ | $\begin{aligned} & \frac{365 \times 42}{371} \\ & =41 \mathrm{days} \end{aligned}$ |
| iv) Return on capital employed (ROCE) | Profit before interest \& tax x 100 Capital employed | $\begin{aligned} & \frac{157^{*}}{230} \times 100 \\ & =68.2 \% \end{aligned}$ | $\begin{aligned} & \frac{79}{157} \times 100 \\ & =50.3 \% \end{aligned}$ |

*Note that the operating profit is net of interest expense an this to be arrived at profits before interest. The interest expense must be added back. $19+138=157^{*}$

|  | Vebt Capital | $\underline{33} \times 100$ <br> 197 <br> $=17 \%$ | $\frac{0}{197} \times 100$ <br> $=0 \%$ |
| :--- | :--- | :--- | :--- |

(c)

## (i) Comments on Performance

- Sunrise Ltd. has a better performance gauging by the return on capital employed.
- Sunset Ltd. has a low gearing and thus less risky with high access to capital market.
- Sunrise Ltd. has better management of inventory.
- Sunrise Ltd. has a better credit policy.
- Overall sunrise has a better performance but a higher risk and thus for risk takers sunrise is the best and for risk averse investors sunset would be the film, to invest in.


## (ii) Shortcomings of relying on analysis in (b) above

- Ratios are historical since they use past data.
- Comparison of ratios for companies maybe misleading due to different bases adopted e.g. in valuation of stock or depreciation.
- Ratios alone do not provide all the information required by users
- Ratios computed from inaccurate information will be misleading.


## QUESTION FOUR

## a)

## Motor vehicles acquired on hire purchase

When a motor vehicle is bought on hire purchase the buyer obtains control over the use of the motor vehicle but the title is retained by the seller until payment of the final installment. In line with the substance over form the motor vehicle should be recognized when control over use is obtained even though the title has not yet passes.

## Leasehold land

Lease refers to a contract to use or occupy a piece of land over a specified periods. The entity has control over the land for that period after which possession reverts to the owner in line with the substance over form principle, therefore, it should be recognized when control over use of the land is obtained.
b)

## Cost of machine

Shs. „000"
Catalogue price
30,000

Add: Incidental expenses
Freight and insurance 7,000
Customs and excise duty $\quad 7,300$
Value added tax 7,100
Installation cost 2,000
Pre production testing $\quad \frac{700}{47,000}$
Initial cost $\underline{47,000}$
Disposal of Machinery Account

| Dr | Shs. ,000"" | $\mathbf{C r}$ |  |
| :--- | ---: | :--- | ---: |
|  | 2,000 | Bank | Shs. ,000" |
| Machinery cost | 375 | Depreciation | 1,500 |
| Profit and loss (gain) | $\underline{2,375}$ | 875 |  |
|  |  | $\underline{2,375}$ |  |

Disposal of Air Conditioner Account

| Dr |  |  | Cr |
| :---: | :---: | :---: | :---: |
|  | Shs. „000" |  | Shs. „000" |
| Air conditioner cost | 545 | Depreciation | 218 |
|  |  | Less disposal | 327 |
|  | 545 |  | 545 |

Provision for depreciation - machinery

| Dr | Shs. ,000" |  | Shs. , $000{ }^{\text {Cr }}$ |
| :---: | :---: | :---: | :---: |
| Disposal a/c | 875 | Bal. b/d | 875 |
| Balance c/d | 11,750 | Profit and loss | 11,750 |
|  | 12,625 |  | 12,625 |

Provision for depreciation - Air conditioner

| Dr |  |  | Cr |
| :---: | :---: | :---: | :---: |
|  | Shs. ,000" |  | Shs. „000 ${ }^{\text {" }}$ |
| Disposal | $\underline{218}$ | Bal b/d | $\underline{218}$ |

Provision for depreciation - furniture


## QUESTION

## FIVE a)

i) Accounting Standards

Accounting standards are authoritative statements that give guidance on accounting treatment and presentation of accounting items and events in the financial statements. They are usually produced by professional bodies.

An example is International Accounting Standard No. 2 an inventory

## ii) Accounting Policies

These are specific rules and regulations governing the accounting methods applied by an organization.

For example a firm may opt to use the last in first out (LILO) method of stock valuation and this becomes their policy

## iii) Accounting Bases

These are methods available for use by a firm from the which the firm chooses their policies.

For instance the various bases for depreciating non current assets include straight line method reducing balance method and revaluation method among others.
b) Qualitative Characteristics of Financial Statements

## i) Understandability

Information in the financial statements should be prepared in a simple language that can be interpreted by the shareholders. Complex issues should be simplified as much as possible and technical jargon minimized.

## ii) Relevant

Information in the financial statements should be appropriate to support the decision needs of the users. All material information which can influence the shareholders should be highlighted.

## iii) Reliability

The information should be free from material errors or misstatements. The financial statements should be complete in all respect and free from bius inorder to enable shareholders to make informed decisions.

## iv) Comparability

The shareholder should be able to evaluate the trend of performance of the company to be comparable the financial statements should be prepared on a consistent basis.
c) An asset refers to resources controlled by an entity as a result of past activity which is expected to benefit the organization for a long time. The asset may be owned by the business or hired but emphasis is placed on control

## Criteria for asset recognition

1. Probable that future benefit will flow to the entity either through continued use or eventual rule.
2. The value of the asset can be measured reliably at $h$ time of acquisition.

Purpose of Control Accounts

1. They facilitate preparation of interim and final accounts such as interim profit and loss and balance sheet. They facilitate the derivation of the sale, purchases, debtors and creditors figures.
2. They facilitate the correction of errors in the ledgers. Errors are easily identified by comparing the sum of the balances in the ledgers with the balances of the control account.
3. They reduce the possibility of fraudulent entries.
4. They act as on internal check on accuracy of debtors. They thus provide a guarantee of assurance to the management on the accuracy of the debtors figures.
5. They act as an aid in balancing the accounts.

MAY 2014
FINANCIAL ACCOUNTING 1

## SUGGESTED SOLUTIONS

## QUESTION ONE

(a) Panter Limted

Trading profit and loss account for year ended 30 September 2005
Shs „000" Shs."000"

| Sales | Shs „000 | Shs. "000" |
| :---: | :---: | :---: |
| Cost of sales |  |  |
| Opening inventory | 20,000 |  |
| Purchases | 161,450 |  |
|  | 181,450 |  |
| Closing inventory | $(19,100)$ | $(162,350)$ |
| Gross profit |  | 89,400 |
| Profit on sale of motor vehicles |  | 2,000 |
|  |  | 91,400 |
| Expenses |  |  |
| Wages ( $21,220+710+5,160$ ) | 27,090 |  |
| Rent | 8,000 |  |
| Motor expenses ( $12,140+1,130+830)$ | 14,100 |  |
| Depreciation - Fixtures \& Fittings (20\%X 9m) | 1,800 |  |
| - Motor vehicles ( $20 \% \times 29 \mathrm{~m}$ ) | 5,800 |  |
| Repairs | 5,220 |  |
| Sundry expenses ( 6,130+470+750-360) | 6,990 |  |
| Interest on loan ( $400+50$ ) | 450 | $(69,450)$ |
| Net profit |  | 21,950 |
| Income tax expense |  | $(10,000)$ |
| Profit after tax |  | 11,950 |
| Retained profit b/f |  | 27,500 |
| Retained profit $\mathrm{c} / \mathrm{f}$ |  | 39,450 |

(b)

Panter Limited
Balance sheet as at 30 September 2005
Non current as
Fixtures \& Fittin
Motor vehicles
Current assets
Shs."000"
Shs."000"
7,200
23,200
30,400

Inventory 19,100
Receivables 35,700
Rent prepaid
2,500
Cash at bank $(15,230+231,170-234,250) \quad 12,150$
Cash in hand $\underline{370}$
Total assets

69,820
100,220

Financed by
Ordinary Share capital

| Retained profits | $\underline{39,450}$ |
| :--- | ---: |
| Non current liabilities | 69,450 |
| Loan from Len Ltd |  |
| Current liabilities |  |
| Trade payables |  |
| Accrued expenses | 13,410 |
| Current tax | 2,360 |
| Total equity and liabilities | 10,000 |

## Workings

(i) Cash in hand

|  | Shs „000" |  | Shs. "000" |
| :---: | :---: | :---: | :---: |
| Balance b/f | 830 | Banking: Old inventory | 12,000 |
|  |  | Other | 214,170 |
|  |  | Wages | 5,160 |
|  |  | Loan interest | 400 |
|  |  | Motor vehicle expenses | 830 |
|  |  | Sundry expenses | 750 |
|  |  | Balance c/d | 370 |
|  | 233,680 |  | 233,680 |

(ii) Cost structure

|  | Normal | Old inventory | Kitale dealers |
| :--- | :---: | :---: | :---: |
| Sales | $\%$ | $\%$ | $\%$ |
| Cost of sales | 100 | 80 | 100 |
| Gross profit margin | $\underline{60}$ | $\underline{60}$ | $\underline{85}$ |
| $\underline{20}$ | $\underline{20}$ | $\underline{15}$ |  |

(iii) Cost of sales (shs. "000)
(a) Total 20,000

Purchases $\quad \underline{161,450}$
181,450
Closing inventory $(19,100)$
162,350
(b) Old inventory

$$
12,000 \times 60 / 80=9,000
$$

(c) Kitale dealers

$$
37,000-4.700=32,300
$$

(d) Others

$$
162,350-9,000-32,300=121,050
$$

(iv) Sales (shs."000)

| Old inventory | 12,000 |
| :--- | :---: |
| Kitale ealers (32,300 X 100/85) | 38,000 |
| Others (121,050 X 100/60) | $\underline{\underline{201,750}}$ |
|  | $\underline{251,750}$ |

(v) Receivables (shs. "000")

| Balance b/d | 16,800 |
| :--- | ---: |
| Sales | 251,750 |
| Cash received | $(232,850)$ |
|  | $\underline{35,700}$ |

(vi) Accrued expenses (Shs. "000")

Sundry 470
Wages 710
Motor expenses 1,130
Loan interest (450-400) $\underline{50}$
2,360
(vii) Rent prepaid (shs."000")

| Balance b/d | 3,000 |
| :--- | ---: |
| Cah paid | $\underline{7,500}$ |
|  | 10,500 |
| Profit and loss account | $\underline{(8,000)}$ |
| Balance c/d | $\underline{2,500}$ |

## QUESTION TWO

(a)

Umoja Women"s Welfare Society
Water tank trading profit and loss account for the year ended 30 April 2006

> Shs. „000"

| Sales | 45,000 |
| :--- | ---: |
| Cost of sales | $\underline{41,000})$ |
| Gross profit | 4,000 |
| Selling expenses | $\underline{(2,000)}$ |
| Net profit | $\underline{2,000}$ |

(b)
Umoja Women"s Welfare Society
Income and expenditure account for the year ended 30 April 2006IncomeShs. "000"Shs. "000"
Net profit from water tank ..... 2,000
Subscriptions ..... 9,100
Raffle tickets ..... 2,800
Donations from members ..... 2,500
Membership fees ..... 800
Expenditure
Office expenses $(4,100+400)$ ..... 4,500
Rent - Office ..... 4,000
Depreciation of Motor vehicle ..... 200
Raffle prizes paid ..... 1,200
Cost of raffle tickets ..... $\underline{300}$17,200
Surplus for the year ..... 7,000$(10,200)$
(c)
Umoja Women"s Welfare Society
Balance sheet as at 30 April 2006

Non current assets
Machinery
Motor Vehicles

Shs „000"
22,000
10,000
$\underline{32,000}$

| Shs."000" | Shs."000" |
| ---: | ---: |
| $(6,100)$ | 15,900 |
| $\underline{(5,000)}$ | $\underline{5,000}$ |
| $\underline{11,100}$ | 20,900 |

Current assets
Raw materials ..... 20,000
Subscriptions receivable ..... 2,000
Cash at bank ..... 500 ..... 22,500
$\frac{\text { Current li }}{}$ ..... 2,800
Subscriptions paid in advance ..... 1,500

| Accrued office expenses | $\underline{400}$ | $(4,700)$ | $\underline{17,800}$ |
| :--- | :--- | ---: | ---: |
| Accumulated fund b/f | $\underline{38,700}$ |  |  |
| Surplus for the year |  | 25,000 |  |
| Membership fees fund (see note) |  | 32,000 |  |
|  | $\underline{6,700}$ |  |  |
|  | $\underline{38,700}$ |  |  |

## Note on Membership fees fund

Note number 3 on the membership fee fund is ambiguous. The examiner does not indicate clearly the source of the fund (whether it is from the surplus from the period, whether there are donations made or whether it is funded by the members of the society). Therefore we have ignored the note, but other alternatives may apply and this will depend on the assumption. For example if we assume that the members are meant to fund the amount of sh. 800,000 , then we can increase the fund to sh. $7,500,000$ and have a receivable of sh. 800,000 as part of the current assets.

Other workings
(i) Cost of sales

|  | Shs. "O00" |  |  |  |
| :--- | ---: | :---: | :---: | :---: |
| Raw materials used | 35,000 |  |  |  |
| Factory wages | 600 |  |  |  |
| Factory overheads | 1,000 |  |  |  |
| Factory rent | 1,000 |  |  |  |
| Factory staff bonus | 1,500 |  |  |  |
| Depreciation - Machinery $(5 \% \mathrm{X} 22 \mathrm{~m})$ | 1,100 |  |  |  |
| - Motor vehicles $(80 \% \mathrm{X} 1 \mathrm{~m})$ |  |  |  | $\underline{800}$ |
|  | $\underline{41,000}$ |  |  |  |

(ii) Subscriptions

Balance b/d
Income \& Expenditure (bal)
Shs. "000"
Shs."000"
2,100
3,500 Balance b/d
9,100 Cash
1,500 Balance c/d 10,000
Balance c/d

$$
14,100
$$

2,000
14,100

## QUESTION THREE

(a) Journal entries


Note (8)
For the suspense to be rectified, this journal entry is necessary. Unfortunately, the examiner should ideally make reference to the personal accounts of the creditor and not the purchases ledger control account. In normal accounting systems we can either have Control accounts or ledger accounts for individual debtors and creditors but we cannot have the two at the same time.
(b)

Balance b/f
Bank
Sundry expenses
Discount allowed

Suspense a/c
Shs
9,000 Rent
7,000 Purchases ledger control
2,000 Tom Wambugu
1,200
19,200
19,200
(c)

Statement of corrected net profit for the year ended 31 December 2005

|  |  |  | Shs |  |  | Shs |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Reported Net profit |  |  |  |  | 153,200 |  |
| Add: |  |  |  |  |  |  |
| Sales understated |  |  |  | 10,000 |  |  |
| Profit on sale of equipment |  |  |  | 2,000 |  |  |
| Returns outwards |  |  |  | 15,000 |  |  |  |
| Sundry expenses |  |  |  | 2,000 |  |  |  |
| Closing inventory |  |  |  | 7,200 |  |  |  |  |
| Discount allowed |  |  | 1,200 |  |  |  |
|  |  |  |  |  | $190,600$ |  |
| Less |  |  |  |  |  |  |
| Sales overstated |  |  | 20,000 |  |  |  |
| Rent under cast |  |  | 1,000 |  |  |  |
| Returns Inwards |  |  | 9,600 |  | $\begin{array}{r} 30,600 \\ 160,000 \\ \hline \end{array}$ |  |
| Corrected Net profit |  |  |  |  |  |  |
| (d) Ben Mogaka |  |  |  |  |  |  |
| Balance Sheet as at 31 December 2005 |  |  |  |  |  |  |
| Non Current assets | Sh. |  | Sh | Sh |  |  |
| Equipment |  | 360,000 |  | $(148,000)$ |  | 212,000 |
| Furniture |  | 300,000 |  | $(150,000)$ |  | 150,000 |
| Motor Vehicles |  | 600,000 |  | $(300,000)$ |  | 300,000 |
|  |  | 1,260,000 |  | $(598,000)$ |  | 662,000 |
| Current assets |  |  |  |  |  |  |
| Inventory |  |  |  | 130,000 |  |  |
| Receivables (19,600+10,000-9,600) |  |  |  | 20,000 |  |  |
| Deposit account |  |  |  | 50,000 |  |  |
|  |  |  |  | 200,000 |  |  |

Current liabilities

| Payables(81,400-15,000-1,800-16,400) | 48,200 |  |
| :--- | :--- | :--- |
| Bank overdraft | $\underline{15,000}$ | $(63,200)$ |
|  |  | $\underline{798,800}$ |
| Capital |  | $\underline{136}$ |
| Net profit | $\underline{160,000}$ |  |
| Less drawings | $\underline{812,000}$ |  |
|  | $\underline{(13,200)}$ |  |

## QUESTION FOUR

(a) Goodwill is that advantage that an existing business may have over a newly established business. The advantage is in the form of the ability to generate revenue and profits as a result for example customer loyalty, location and marketing.
(i) On admission of a new partner, the new partner will start enjoying the benefits of the existing partnership as a result of the goodwill created by the previous partners. The newly admitted partner should therefore pay for his share of the goodwill.
(ii) On retirement of one of the partners, the remaining partners will continue enjoying the benefits that the retired partner helped create. Therefore it will be important for the retiring partner to be paid his share of the goodwill.
(b)

Akili, Busara and Chema
Trading, profit, loss and appropriation account for the year ended 30April 2006

|  |  |  |  |  | Sh"000" | Sh"000" |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Sales (20-0.6) |  |  |  |  |  | 19,400 |
| Cost of sales |  |  |  |  |  |  |
| Opening | Inventory |  |  |  | 3,000 |  |
| Purchases |  |  |  |  | 10,300 |  |
|  |  |  |  |  | 13,300 |  |
| Closing | Inventory |  |  |  | $(2,600)$ | $(10,700)$ |
| Gross profit |  |  |  |  |  | 8,700 |
| Expenses |  |  |  |  |  |  |
| Interest(10\% | X 3m) |  |  |  | 300 |  |
| Operating |  |  |  |  | 6,400 | (6,700) |
| Net profit |  |  |  |  |  | 2,000 |
|  | $1^{\text {st }}$ six | Months $1000$ | $2^{\text {nd }}$ six | Months $1000$ |  | 2000 |
| Int. on cap. |  |  |  |  |  |  |
| A | 62.5 |  | 71.5 |  | 140 |  |
| B | 50 |  | 71 |  | 121 |  |
| C | $\underline{25}$ | (137.5) | $\underline{49}$ | (197.5) | 74 | (335) |
|  |  | 862.5 |  | 802.5 |  | 1,665 |

[^0]| A | 0 |  | 0 |  | 0 |  |
| :--- | ---: | ---: | ---: | ---: | ---: | ---: |
| B | 120 |  | 60 | 180 |  |  |
| C | $\underline{0}$ | $\underline{(120)}$ | $\underline{60}$ | $\underline{(120)}$ | $\underline{60}$ | $\underline{(0) 40)}$ |
| Balance | 247.5 | 742.5 |  | 341.25 |  | 582.5 |
| A | 247.5 |  | 204.75 |  | 453.75 |  |
| B | $\underline{247.5}$ | $\underline{(742.5)}$ | $\underline{136.5}$ | $\underline{(682.5)}$ | $\underline{384}$ | $\underline{(1,425)}$ |
| C | $\underline{0}$ |  | $\underline{0}$ |  | $\underline{0}$ |  |

(b)
Capital account

|  | A | B | C |  | A | B | C |
| :--- | ---: | ---: | ---: | :--- | ---: | ---: | ---: |
|  | Sh."000" $^{\prime \prime}$ | Sh."000" $^{\prime \prime}$ | Sh."000" |  | Sh."000" | Sh."000" | Sh."000" |
| Goodwill | 600 | 360 | 240 | Bal.b/d | 2,500 | 2,000 | 1,000 |
|  |  |  |  | Goodwill | 400 | 400 | 400 |
| Bal.c/d | $\underline{3,100}$ | $\underline{2,840}$ | $\underline{1,960}$ | Rev.gain | $\underline{800}$ | $\underline{800}$ | $\underline{800}$ |
|  | $\underline{3,700}$ | $\underline{3,200}$ | $\underline{2,200}$ |  | $\underline{3,700}$ | $\underline{3,200}$ | $\underline{2,200}$ |
|  |  |  |  |  |  |  |  |

Current account

|  | A | B | C |  | A | B | C |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Sh. ${ }^{\text {0000" }}$ | Sh."000" | Sh. "000" |  | Sh. "000" | Sh. "000" | Sh. "000" |
| Drawings | 300 | 400 | 200 | Bal.b/d | 200 | 3,00 | 200 |
|  |  |  |  | Int. -cap | 140 | 121 | 74 |
|  |  |  |  | Salaries | 0 | 180 | 60 |
|  |  |  |  | Profits | 588.75 | 452.25 | 384 |
| Bal.c/d | $\underline{628.75}$ | 753.25 | 718 | Int.Loan | $\underline{0}$ | $\underline{100}$ | $\underline{\underline{200}}$ |
|  | 3,700 | 3,200 | 2,200 |  | 3,700 | 3,200 | 2,200 |
|  |  |  |  |  |  |  |  |

(c)
Akili, Busara and Chema
Balance sheet as at 30 April 2006

Non Current assets
Land and buildings
Plant and Machinery
Shs. "000
8,00
$\frac{15,000}{}$
Current assets
Inventory $(2,400+200)$
Receivables

Current liabilities
Bank Overdraft
Payables

Capital Accounts
Akili
Busara 2,840
Chema
1,100
3,300
$(4,400)$
1,600
13,000

3,100

1,960

| Current account |  | 7,900 |
| :--- | ---: | ---: |
| Akili | 628.75 |  |
| Busara | 753.25 |  |
| Chema | $\underline{718}$ | $\underline{2,100}$ |
|  |  | 10,000 |
| Non current liabilities | 1,000 |  |
| $10 \%$ Loan : Busara | $\underline{2,000}$ | $\underline{3,000}$ |
| Chema |  | $\underline{13,000}$ |

## QUESTION FIVE

(a) (i) Employees : They would like to know how the firm is performing and its financial position so as to make decisions about their terms (salaries and benefits) and job security.
(iii) Financial Analysts: They are experts who advise other users. They require information about the financial performance and position so as to advise their clients.
(iv) The Government: Concerned about tax and compliance with the law. Will need to know the performance of the company so as to assess the tax payable and also come up with the relevant national statistics.
(v) The public : They require information about the financial performance and position of the company so as to determine whether the firm can offer employment opportunities and also check on how socially responsible the firm is.
(vi) (i) It may be too costly for the firm to provide all the information in terms of resources committed, involvement of experts such as auditors and accountants and the information system.
(ii) There may also be not time to present all the information required because some of the financial statements have to be presented on a timely basis and within strict deadlines.
(b) (i) The firm has to create a provision of sh. $960,000(1 \% \mathrm{X} 200,000 \mathrm{X} 480)$.This is in line with the prudence concept and IAS 37 „Provisions, contingent liabilities and contingent assets"
(iii) Under IAS 2 on inventories, inventory should be held at the lower of cost and Net realizable Value (NRV). Net Realizable Value is the selling price less expenses to complete the sale. The firm should therefore reduce the value of stock by sh. 90,000 (from sh. 200, 000 to sh. $110,000(150,000-40,000)$.
(iv) Under the Realization concept, revenue is only recognized (reported in the accounts) when it has been realized in the form of cash or another asset. Unless the firm has already delivered the goods and the customer accepts liability, then there is no sale. Sales should be reduced by Sh. 2 million. Even though the deposit has been paid, the amount is refundable.
(v)

A provision should be made for this amount under the prudence concept

## DECEMBER 2014

FINANCIAL ACCOUNTING 1

## SUGGESTED SOLUTIONS

## QUESTION ONE

(a) Baraka

Trading , profit and loss account for year to 30 September 2006

Sales: Cash
Credit
Cost of sales:
Purchases 4,121
Less: Closing inventory
Gross profit
Expenses
Wages
410
Rent and rates 100
Lighting expenses 50
Insurance 20
Stationery and postage 26
Sundry expenses 56
Bank charges 110
Depreciation: Premises 50
Fixtures and fittings $\underline{30}$
Net profit
(b)Baraka

Balance sheet as at 30 September 2006

| Non Current assets | Sh.000 | Sh.000 | Sh.000 |
| :--- | :--- | :--- | :--- |
| Premises | 2,500 | $(50)$ | 2,450 |
| Fixtures and fittings | $\underline{300}$ | $\underline{(30)}$ | $\underline{270}$ |
| Current assets | $\underline{2,800}$ | $\underline{80}$ | 2,720 |
| Inventory |  | 360 |  |
| Receivables |  | 177 |  |
| Prepayments |  | 20 |  |
| Cash at bank | 493 | $\underline{10}$ |  |
| Cash in hand | $\underline{16}$ | 1,060 |  |
| Current liabilities |  | $\underline{(419)}$ | $\underline{641}$ |
| Payables |  | $\underline{3,361}$ |  |
| Accrued expenses |  |  | $\underline{3,176}$ |
| Capital |  |  | $\underline{3361}$ |
| Net profit for year |  | $\underline{(600})$ |  |
| Less: Drawings |  |  | $\underline{3,361}$ |


| $1 . \quad$ Cash and Bank |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | Cash | Bank |  | Cash | Bank |
|  | Sh. 000 | Sh. 000 |  | Sh. 000 | Sh. 000 |
| Capital | 500 |  | Cash Contra |  | 20 |
| Bank contra | 20 |  | Fixtures and fittings |  | 300 |
| Suppliers |  | 10 | Suppliers - purchases |  | 3,728 |
| Customers |  | 382 | Insurance of inventory |  | 40 |
| Banking-contra |  | 3,769 | Bank charges |  | 110 |
| Customers |  |  | Wages | 400 |  |
| Uncredited amount |  | 30 | Lighting expenses | 50 |  |
| Cash sales | 4,814 |  | Drawings | 600 |  |
|  |  |  | Bank contra | 3,769 |  |
|  |  |  | Bal. c/d (inclusive-5000) | 15 | 493 |
|  | 4,834 | 4,691 |  | 4,834 | 4,691 |
| 2. |  |  |  |  |  |
| Receivables |  |  |  |  |  |
| Sales | Sh. 000 | Sh. 000 |  |  |  |
|  | 584 | Cash 382 |  |  |  |
|  |  | Cash 30 |  |  |  |
|  | 584 | Balance c/d 172 |  |  |  |
|  |  |  | 584 |  |  |
| 3. |  |  |  |  |  |
|  | Sh. 000 |  | Sh. 000 |  |  |
| Cash | 3,728 | Cash | 10 |  |  |
| Balance c/d | 403 | Purchases 4,121 |  |  |  |
|  | 4,131 |  | 4,131 |  |  |
| 4. |  |  |  |  |  |
|  | Sh. 000 |  | Sh. 000 |  |  |
|  |  | Premise | s 2,500 |  |  |
|  |  | Cash at | bank 500 |  |  |
|  |  | Rent and | d rates 100 |  |  |
| Balance c/d |  | Lighting | g expenses 50 |  |  |
|  | 3,176 | Stationery and postage 26 |  |  |  |
|  | 3,176 |  | 3,176 |  |  |

## QUESTION TWO

Auto Transmission Ltd
Manufacturing, trading and profit and loss account for the year ended 31 December 2005

| Raw materials | Sh | Sh |
| :--- | ---: | ---: |
| Opening inventory | $\underline{5,186,000}$ |  |
| Purchases | $5,886,000$ |  |
|  | $\underline{562,000}$ |  |
| Closing inventory | $5,324,000$ |  |


| Manufacturing wages |  |  | $\frac{5,014,000}{10,338,000}$ |
| :---: | :---: | :---: | :---: |
| Prime cost |  |  |  |
| Factory overheads: | Lighting | 300,140 | N |
|  | Electricity | 393,675 |  |
|  | Insurance | 160,650 |  |
|  | Rates | 391,925 |  |
|  | Rent | 353,200 |  |
|  | Plant maintenance | 301,020 |  |
|  | Production directors salary | 200,000 |  |
|  | Depn plant \& machinery | 1,095,000 | 3195,610 |
| Factory Cost of | production |  | 13,533,590 |
| Opening work in progress |  |  | 1,260,000 |
|  |  |  | 14,793,590 |
| Closing work in pro |  |  | (471,900) |
| Factory Cost of fin | oods |  | 14,321,690 |
| Factory profit |  |  | 678,310 |
| Finished goods at transfer price (1500x100) |  |  | 15,000,000 |
| Sales |  |  | 26,001,470 |
| Less Returns |  |  | $(151,060)$ |
|  |  |  | 25,850,410 |
| Cost of sales |  |  |  |
| Opening Inventory of finished goods |  | 2,500,000 |  |
| Finished goods at transfer price |  | 15,000,000 |  |
|  |  | 17,500,000 |  |
| Closing inventory of finished goods |  | $(1,000,000)$ | (16,500,000) |
| Gross profit |  |  | 9,350,410 |
| Add Factory profit |  |  | 678,310 |
|  |  |  | 10,028,720 |
| Expenses |  |  |  |
| Administrative expenses |  |  |  |
| General |  | 630,110 |  |
| Office salaries |  | 1,017,760 |  |
| Electricity |  | 78,735 |  |
| Insurance |  | 32,130 |  |
| Rates |  | 78,385 |  |
| Rent |  | 70,640 |  |
| Directors salaries |  | 401,140 |  |
| Depreciation- office equipment - building |  | 110,000 |  |
|  |  | 26,000 |  |
| Selling and distribution expenses |  |  |  |
| Advertising |  | 1,900,480 |  |
| Distribution costs |  | 850,130 |  |
| Salesman salaries |  | 642,370 |  |
| Depreciation of motor vehicles |  | 300,000 |  |
| Others |  |  |  |
| Bank interest |  | 70,700 |  |
| Increase in provision for doubtful debts |  | 40,000 |  |
| Provision for UP on Finished Goods (1/15 x 678,310) |  | 45,220 | $(6,293,800)$ |
| Profit before tax |  |  | 3,734,920 |


| Income tax expense |  | (1,000,000) |
| :---: | :---: | :---: |
|  |  | 2,734,920 |
| Less: |  |  |
| Dividends: Preference dividend paid | 100,000 |  |
| Proposed preference | 100,000 |  |
| Proposed ordinary | 1,800,000 | (2,000,000) |
| Retained profit for the year |  | 734,920 |
| Retained profit bought forward |  | 424,750 |
| Retained profit carried forward |  | 1,159,670 |

## QUESTION THREE

a) Income statement for the year ended 30 September 2006

|  | Sh. 000 | Sh. 000 |
| :---: | :---: | :---: |
| Sales: |  |  |
| 1 October 2005 to 31 March 2006 <br> 1 April 2006 to September 2006 |  | 14,000 |
|  |  | 21,000 |
|  |  | 35,000 |
| Opening Inventory | 4,800 |  |
| Purchases (16,400 +200 ) | 16,600 |  |
|  | 21,400 |  |
| Closing inventory | $(5,100)$ | $(16,300)$ |
| Gross profit |  | 18,700 |
|  | Six months 1.10.2005 to | Six months (1.4.2005 to |
|  | 31.3.2006) | 30.9. 2006) |
| Gross profit ( ratio of 14:21) | $(7,480)$ | $(11,220)$ |
| Expenses: |  |  |
| Salaries (5,200-1,330) | $(1,935)$ | $(1,935)$ |
| Rent, rates and electricity | (820) | (820) |
| $1,240+600+60-260)$ |  |  |
| Shop wages | $(1,100)$ | $(1,100)$ |
| Professional charges (420-210) | (110) | (110) |
| General expenses (2,640-120) | $(1,410)$ | $(1,110)$ |
| Depreciation: Motor vehicles 680 | (340) | (340) |
| Shop fittings 60 | (30) | (30) |
| Amortisation of lease |  |  |
| (1/25 x ( $6,000+200)$ | (124) | (124) |
| Provision for doubtful debts | (120) | (40) |
| Net profit (Shared in PSR) | 1,491 | 5,611 |
| Grace $2: 2$ | 994 | 2,244.4 |
| Beatrice $\quad 1: 2$ | 497 | 2,244.4 |
| Catherine 0: 1 | 0 | 1,122.2 |

b) Balance sheet as at 30 September 2006

|  | Cost | Depreciation | Net book value |
| :--- | :--- | :--- | :--- |
|  | Sh. 000 | Sh. 000 | Sh.000 |
| Non-Current Assets: |  |  |  |
| Leasehold premises | 6,200 | 248 | 5,952 |
| Motor vehicles | 3,400 | 1,880 | 1,520 |


| Shop fittings | 1,200 | 460 | 740 |
| :--- | ---: | ---: | ---: |
|  | 10,800 | 2,588 | 8,212 |
|  |  |  |  |
| Current Assets: |  | 5100 |  |
| Stocks |  |  |  |
| Accounts receivable |  |  |  |
| $(900-180)$ | 760 | 560 |  |
| Provision for bad debts | 160 |  |  |
|  |  | 260 |  |
| Prepayments |  | 9.280 |  |
| Cash at bank |  | 100 | 15,300 |
| Suspense |  |  | 23,512 |
| Capital: |  |  |  |
| Fixed capital |  |  |  |


|  |  |  |
| :--- | ---: | ---: |
| Grace |  | 3,000 |
| Beatrice |  | 2,000 |
| Catherine |  | 1,500 |
|  |  | 6,500 |
| Current account |  |  |
| Grace |  |  |
| Beatrice | $7,438.4$ |  |
| Catherine | $3,261.4$ |  |
|  | $1,972.2$ |  |
| Accounts payable $(4,280+60$ |  | 12,672 |
|  |  | 4,340 |

c) Current accounts

|  | G | B | C |  | G | B | C |
| :--- | :--- | :--- | :--- | :--- | :--- | :--- | :--- |
|  | Sh.000 | Sh. 000 | Sh.000 |  | Sh.000 | Sh.000 | Sh.000 |
| Goodwill | 4,800 | 4,800 | 2,400 | Bal. b/d | 1,600 | 1,200 |  |
| Drawings | 600 | 480 | 250 | Profit | $3,238.4$ | $2,741.4$ | $1,122.2$ |
| Bal. c/f | $7,438.4$ | $3,261.4$ | $1,972.2$ | Goodwill | 8,000 | 4,000 |  |
|  |  |  |  | Rent |  | 600 |  |
|  |  |  |  | Cash |  |  | 3,500 |
|  | $12,838.4$ | $8,541.4$ | $4,622.2$ |  | $12,838.4$ | $8,541.4$ | $4,622.2$ |

## QUESTION FOUR

a) A trial balance normally reflects how accurate the double entry has been made in the accounts. It therefore indicates that every debit entry has a corresponding credit entry. Unfortunately a trial balance does not highlight some fundamental errors. These include:
i) Amounts entered in the accounts may not be correct.
ii) Entries have been made in the incorrect accounts
iii) Entries have been reversed i.e entered on the wrong side of the accounts.
iv) Compensating errors.

|  | Sh | Sh |
| :---: | :---: | :---: |
| b i) Receivables | 3,200 |  |
| Profit and loss (discount allowed) |  | 3,200 |
| Correction of incorrect discount rate given to customer |  |  |
| ii) Prepayments | 22,450 |  |
| Profit and loss (electricity) | 36,710 |  |
| Accruals |  | 36,710 |
| Profit and loss (insurance) |  | 22,450 |
| Being recording of prepaid insurance and accrued electricity |  |  |
| iii)Bank | 126,550 |  |
| Provision for unclaimed wages |  | 126,550 |
| Unclaimed wages arrears being banked pending further |  |  |
| Tracing of the beneficiaries |  |  |
| iv) Profit and loss account (salaries and wages) | 765,820 |  |
| Accruals |  |  |
| Incorporation of accrued wages and salaries | 765,820 |  |
| v) Profit and loss (repairs) | 500,000 |  |
| Provision for depreciation (premises) | 10,000 |  |
| Premises |  | 500,000 |
| Profit and loss (depreciation) |  | 10,000 |
| Correction of repairs wrongly capitalised and consequent depreciation |  |  |
| vi) Payables(CB Ltd) | 163,040 |  |
| Receivables (CB Ltd) |  | 163,040 |
| Settlement in contra |  |  |
| vii) Provision for discounts on debtors | 72,130 |  |
| Profit and loss account |  | 72,130 |
| Correction of over-provision debtors |  |  |
| viii) Profit and loss account (bad debts) | 64,800 |  |
| Receivables |  | 64,800 |
| Cash at bank |  | 21,440 |
| Bad debt recovered |  |  |

21,440
Write off a bad debts (Sh. 64,800 ) and incorporation of cheque $(21,440)$ being bad debt recovered

## QUESTION FIVE

## RATIO ANALYSIS

i) ROCE $=$ Profit and Ordinary activities before interest and

> taxation Capital employed

Where capital employed $=$ shareholders equity and long term liabilities
ii) $\mathrm{ROE}=\underline{\text { Profit after tax }}$ and preference dividend Ordinary share capital and any other equity
iii) Leverage ratio $=$ Share holders equity Shareholders equity + total long term debt

Or Shareholders equity
Total assets less current liabilities
iv) Inventory turnover $=$ inventory $\times 365$

Cost of sales
v) $\mathrm{EPS}=\underline{\text { Profit after tax }}$ and preference dividend Number of ordinary shares

## Profitability

Gross profit margin has declined slightly, although it is still higher than the industry average. The share holders may find the net profit margin more useful. This appears better than the industry average.

## Leverage

This has decreased and is significantly lower that the industry norm while a low leverage means greater returns to the shareholders (assuming an interest rate lower than the ROCE of $19 \%$, it is also associated with increased risk from the point of view of the lenders. The ROCE has increased in 2006 compared with 2005, which is consistent with the decrease in leverage.

## Other ratios

Accounts payment period and documents receivable collection period have both increased particularly the payments period. Both are above the industry norm. These increases suggest that the company has been allowing customers to take longer to pay in order to gain customers and holding back payment to suppliers. This is having an impact on liquidty.
(vi) In general, profitability looks favourable but liquidity and leverage need to be carefully monitored.
(15 mand IAS 37. A present obligation exists.)

## Part III: Comprehensive Mock Examinations

## Questions - Mocks

## MOCK PAPER 1

## QUESTION ONE

Anne, Charlotte and Emily have been in partnership for some years, sharing profits in the ratio 50.30 .20 and preparing their financial statements to 31 December each year.

On 30 June 1998 Anne retired and Charlotte and Emily decided to continue the partnership sharing profits equally.

The partnership list of account balances at 31 December 1998, before making any adjustments for Anne"s retirement or for the asset revaluation was as follows.

|  | Shs | Shs |
| :---: | :---: | :---: |
| Land at cost | 120,000 |  |
| Buildings: cost | 320,000 |  |
| Depreciation at 1 January 1998 |  | 24,000 |
| Shop and office equipment |  |  |
| Cost | 48,000 |  |
| Depreciation at 1 January 1998 |  | 11,000 |
| Accounts receivable | 68,400 |  |
| Allowance for doubtful debts 1 January 1998 |  | 2,100 |
| Cash at bank | 4,200 |  |
| Accounts payable |  | 81,200 |
| Capital accounts as at 1 January 1998 : Anne |  | 180,000 |
| Charlotte |  | 170,000 |
| Emily |  | 160,000 |
| Current accounts at 1 January 1998: Anne |  | 3,000 |
| Charlotte | 2,000 |  |
| Emily |  | 2,000 |
| Drawings accounts: Anne (to 30 June 1998) | 21,000 |  |
| Charlotte (to 31 December 1998) | 37,000 |  |
| Emily (to 31 December 1998) | 36,000 |  |
| Inventory at 1 January 1998 | 81,000 |  |
| Purchases | 291,000 |  |
| Sales revenue |  | 494,000 |
| Staff wages | 58,600 |  |
| Rent | 25,000 |  |
| General administrative expenses | 14,200 |  |
| Bad debts written off | 900 |  |
|  | 1,127,300 | 1,127,300 |

## Notes

(1) Profits are to be assumed to accrue equally in the periods before and after Anne"s retirement
(2) The balance due to Anne is to remain in the partnership from 1 July 1998 as a loan carrying no interest until 1 January
(3) The value of the partnership goodwill at 30 June 1998 was agreed by all three partners at Shs 200,000 . Goodwill is not to appear in the balance sheet after the adjustments necessary at 30 June 1998.
(4) It was decided, as part of the process of valuing Anne"s share of the partnership, to revalue the land at 30 June from Shs 120,000 to Shs 160,000 . The increased value is to be included in the balance sheet.
(5) The inventory at 31 December 1998 was Shs 90,000
(6) Accruals and prepayments at 31 December 1998 were:

Rent paid in advance to 31 March 1999 Shs 5,000
General administrative expenses:

| Prepayments | Shs 1,800 |
| :--- | :--- |
| Accruals | Shs 6,200 |

(7) The allowance for doubtful debts is to be increased to Shs 2,400
(8) Depreciation is to be provided as follows:

Buildings $2 \%$ per annum straight line
Shop and office equipment $15 \%$ per annum straight line

## Required:

(a) Prepare the income statement and a statement showing the division of the profit for the year ended 31 December 1998 and balance sheet as at that date; ( 16 marks)
(b) Show the partners" capital and current accounts for the year Anne"s loan account

## QUESTION TWO

Agatha, a limited company made up its financial statements to 31 December 1997, when the company changed its accounting date by making up its next financial statements for the fifteen months to 31 March 1999.

The company"s depreciation policy is to charge proportionate depreciation in the periods of purchase and sale of its non-current assets, charging depreciation as from the first day of the month in which assets are acquired, and up to the last day of the month before the month of any disposal. Annual rates of depreciation taken are:

| Plant and machinery | 15 per cent straight line |
| :--- | :--- |
| Motor vehicles | 25 per cent straight line |

At 1 January 1998 the following balances existed in the company"s accounting records.

| Shs |  |
| :---: | ---: |
| Plant and machinery: cost | 819,000 |
| Accumulated depreciation | 360,000 |
| Motor vehicles : Cost |  |
| Accumulated depreciation | 148,000 |
| 60,000 |  |

During the fifteen months ended 31 March 1999 the following transactions took place:
(1) 10 January 1998

An item of plant was purchased. The cost was made up as follows:

|  | Shs |
| :--- | ---: |
| Cost ex factory | 41,200 |
| Delivery | 300 |
| Installation costs | 800 |
| Construction of foundations | 3,600 |
| Spare parts for repairs | 4,000 |
| Cost of one year maintenance agreement | 2,000 |
|  | $\underline{51,900}$ |

(2) 18 April 1998

A new motor vehicle was purchased for Shs 18,000 . An existing vehicle which had cost Shs 12,000 and which had a book value at 1 January 1998 of Shs 6,000, was given in part exchange at an agreed value of Shs 5,000. The balance of Shs 13,000 was paid in cash.

## Required:

(a) Prepare the ledger accounts to show the balances at 1 January 1998 and to record the non-current asset transactions as stated.
(b) Prepare the schedule of figures detailing the movements in non-current assets and depreciation for the company"s financial statements for publication for the period ended 31 March 1999 required by IAS 16 Property Plant and equipment.
(5 marks)
(Figures may be rounded to the nearest Shs 100 for part (b)).

## QUESTION THREE

Atok, a limited liability company, compiles its financial statements to 30 June annually. At 30 June 1999, the company"s list of account balances was as follows:

|  | Shs | Shs |
| :---: | :---: | :---: |
| Sales revenue |  | 14,800 |
| Purchases | 8,280 |  |
| Inventory at 1 July 1998 | 1,390 |  |
| Distribution costs | 1,080 |  |
| Administrative expenses | 1,460 |  |
| Land at valuation | 10,500 |  |
| Buildings: cost accumulated depreciation at 1 July 1998 | 8,000 | 2,130 |
| Plant and equipment: cost accumulated depreciation at 1 July 1998 | 12,800 | 2,480 |
| Trade accounts receivable and payable | 4,120 | 2,240 |
| Cash at bank | 160 |  |
| Ordinary shares of 50c each: as at 1 July 1998 |  | 10,000 |
| issued during year |  | 4,000 |
| Share premium account: as at 1 July 1998 |  | 2,000 |
| arising on shares issued during year |  | 2,000 |
| Revaluation reserve as at 1 July 1998 |  | 3,000 |
| Accumulated profits |  | 3,140 |
| 10\% loan notes (redeemable 2008) |  | 2,000 |
| (issued 1 April 1999 with interest payable 31 March and 30 September each year) |  |  |

The following matters remain to be adjusted for in preparing the financial statements for the year ended 30 June 1999:
(1) Inventory at 30 June 1999 amounted to Shs $1,560,000$ at cost. A review of inventory items revealed the need for some adjustments for two inventory lines:
(i) Items which had cost Shs 80,000 and which would normally sell for Shs 120,000 were found to have deteriorated. Remedial work costing Shs 20,000 would be needed to enable the items to be sold for Shs 90,000 .
(ii) Some items sent to customers on sale or return terms had been omitted from inventory and included as sales in June 1999. The cost of these items was Shs 16,000 and they were included in sales at Shs 24,000. In July 1999, the items were returned in good condition by the customers.
(2) Depreciation is to be provided as follows:

Buildings: $2 \%$ per year on cost.
Plant and equipment: $20 \%$ per year on cost.
$80 \%$ of the depreciation is to be charged in cost of sales, and
$10 \%$ each in distribution costs and administrative expenses.
(3) The land is to be revalued to Shs $12,000,000$. No change was required to the value of the buildings.
(4) Accrued expenses and prepayments were:

|  | Accrued expenses | Prepayments |
| :--- | :---: | :---: |
| Shs"000 | Shs"000 |  |
| Distribution costs | 190 | 120 |
| Administrative expenses | 70 | 60 |

(5) No dividends were paid during the year and no dividend is proposed for the year.

## Required:

(a) Prepare the company"s income statement for the year ended 30 June 1999 and balance sheetas at that date for publication, complying as far as possible with the provisions of IAS1 Presentation of Financial Statements and other relevant International Accounting Standards.
(20 marks)
(b) Prepare the statement of changes in equity as presented in IAS1. Notes to the financial statements are not required. (5 marks)
(25 marks)

## QUESTION FOUR

Otter, a limited liability company, operates a computerised accounting system for its accounts receivable and accounts payable ledgers. The control accounts for the month of September 1999 are in balance and incorporate the following totals:

Shs
Accounts receivable ledger:
Balances at 1 September 1999: Debit 386,430
Credit
190
Sales revenue 163,194
Cash received 158,288
Discounts allowed 2,160
Sales returns inwards 590
Credit balances at 30 September 1999370
Accounts payable ledger:
Balances at 1 September 1999: Credit 184,740
Debit 520
Purchases 98,192
Cash payments 103,040
Discounts received 990
Purchases returns outwards 1,370
Debit balances at 30 September 1999520
Although the control accounts agree with the underlying ledgers, a number of errors have been found, and there are also several adjustments to be made. These errors and adjustments are detailed below:
(1) Four sales invoices totalling Shs 1,386 have been omitted from the records;
(2) A cash refund of Shs 350 paid to a customer, A Smith, was mistakenly treated as a payment to a supplier with the same name;
(3) A contra settlement offsetting a balance of Shs 870 due to a supplier against the accounts receivable ledger account for the same company is to be made;
(4) Bad debts totalling Shs1,360 are to be written off;
(5) During the month, settlement was reached with a supplier over a disputed account is a result, the supplier issued a credit note for Shs 2,000 on September 26. No entry has yet been made for this;
(6) A purchases invoice for Shs 1,395 was keyed in as Shs 1,359;
(7) A payment of Shs 2,130 to a supplier, B Jones, was mistakenly entered to the account of R Jones;
(8) A debit balance of Shs 420 existed in the accounts payable ledger at the end of August 1999. The supplier concerned cannot now be traced and it has been decided to write off this balance.

## Required:

Prepare the accounts receivable and accounts payable ledger control accounts as they should appear after allowing, where necessary, for the errors and adjustments listed. (16 marks)

## QUESTION FIVE

(a) List and briefly explain three ways in which the use of historical cost accounting may cause financial statements to be misleading.
(10 marks)
(b) The term „reserves" is frequently found in company balance sheets Required:
(i) Explain the meaning of „reserves" in this context;
(ii) Give two examples of reserves and explain how each of your examples comes into existence.
(c) A company"s issued share capital may be increased by a bonus (capitalization) issue or by a rights issue
Required:
Define "bonus issue" and "rights issue" and explain the fundamental difference between these two types of share issue. (5 marks)
(Total: 20 marks)

## MOCK PAPER 2

## QUESTION ONE

John and Dan are partners who run a wholesale shop. They share profits and losses equally. The accountant has provided a draft balance sheet as shown below:

## Balance Sheet as at 31 December 1998

| Fixed Assets: | Cost | Depreciation | Accumulated <br> Net Book Value |
| :---: | :---: | :---: | :---: |
| Land and buildings | 30,000,000 |  | 30,000,000 |
| Plant and Machinery | 32,000,000 | 15,000,000 | 17,000,000 |
| Motor vehicles | 12,000,000 | 4,400,000 | 7,600,000 |
|  | 74,000,000 | 19,400,000 | 54,600,000 |
| Current Assets: |  |  |  |
| Stock on hand |  | 9,000,000 |  |
| Sundry debtors |  | 24,000,000 |  |
| Cash and bank balances |  | 3,000,000 |  |
|  |  | 36,000,000 |  |
| Current Liabilities: |  | 18,600,000 |  |
| Sundry creditors |  |  | 17,400,000 |
| Net current assets |  |  | 72,000,000 |
| Capital accounts: | John | Dan |  |
|  | Sh. | Sh. | Sh. |
| Balances for January 1998 | 42,400,000 | 23,000,000 |  |
| Profit for year | 7,600,000 | 7,600,000 |  |
|  | 50,000,000 | 30,600,000 |  |
| Less drawings | 6,400,000 | 2,200,000 |  |
|  | 43,600,000 | 28,400,000 | 72,000,000 |

From your examination of the books, you find that adjustments to the accounts are necessary in respect of the following:

1) Sales included goods valued at Sh. 700,000 which had been taken by Dan for his own private use and debited to him in an account opened in the sales ledger. This is to be treated as drawings.
2) The bills for electricity amounting to Sh. $446,000 \mathrm{had}$ not been paid.
3) A cheque for $S h .100,000$ received from a debtor on 29 December 1998 had been put in the drawer by the cashier and forgotten.
4) The amount for sundry debtors is shown net of a provision for doubtful debts of Sh.600,000. The provision includes a bad debt of Sh. 120,000. The revised provision for doubtful debts was agreed at Sh.560,000.
5) A stock valued at $\mathrm{Sh} .3,300,000$ was considered to have a net realizable value of Sh.3,000,000. Some items of the stock for Sh.480,000 were not included in Sh.3,300,000.
6) Trade licenses for Sh. 344,000 paid during the year had been charged to the profit and loss account yet it will not expire until 31 March 1999.
7) Plant and machinery is considered to have a written down value of Sh.16,800,000.
8) During the year a building which cost Sh.5,800,000 was sold for Sh.5,600,000 and the amount credited to freehold premises.

A cheque for Sh.406,000 received from a debtor and paid into the bank on 13 December 1998 had been returned on 31 December 1998 marked "refer to drawer". No entries were made in the books of account.

## Required:

a) A statement showing the correct adjustments and the adjusted profit for the year ended 31 December 1998.
b) A revised balance sheet as at 31 December 1998.

## QUESTION TW0

Pesa and Akili were in partnership preparing their accounts to 31 March and sharing profits and losses in the ratio of $3: 2$ respectively. Interest was allowed on fixed capital at $10 \%$ per annum. Akili was entitled to a salary of Sh.3,000 per month. On 2 October 1995 the partners admitted Tajiri a well known businessman into the partnership. On that day Tajiri introduced a Sum of money which was equal to $50 \%$ of Pesa's fixed capital. The amount was credited to Tajiri's capital account.

## The new partnership agreement provided the following:

1) Interest on capital to be maintained at $10 \%$ per annum.
2) Tajiri is to receive a commission of $10 \%$ of the net profit before appropriations. This is due to his business acumen.
3) Profits will be shared equally among the partners.
4) Akili is now entitled to a salary of Sh. 3,500 per month.

The partners also agreed to guarantee Tajiri a minimum share of profit of Sh. 62,000 per annum. Any deficiency on that balance will be compensated by the other two partners in equal proportions. For the purposes of admission of a partner, goodwill was valued at two years purchase of average profits for the last three years. The profits for the years ended 31 March 1993, 1994 and 1995 were Sh.60,000, Sh.50,OOOand Sh.70,000 respectively. No goodwill account is to be maintained in the books. Adjusting entries are to be made in the partners current accounts. The net profit for the year ended 31 March 1996 was Sh.360,000. The profit accrued evenly over the year.

The following are the partners balances on I April 1995:

|  |  | Sh. |
| :--- | :--- | ---: |
| Fixed Capital: | Pesa, | 400,000 |
|  | Akili, | 300,000 |
| Current Accounts: | Pesa, Cr | 20,000 |
|  | Akili, Dr | 1,400 |
| Drawings during the year: Pesa, | 27,000 |  |
|  | Akili, | 16,800 |
|  | Tajiri | 9,000 |
| Salary withdrawn by | Akili, | 27,000 |

## Required:

a) Profit and Loss Appropriation Account for the year ended 31 March 1996. (7 marks)
b) Partners Current Accounts.

## QUESTION THREE

Kenya Caps Limited issued additional 100,000 ordinary shares and 50,000, 8\% preference shares on the following terms:
$\left.\begin{array}{lrc} & & \text { Payable per share } \\ \text { Ordinary } & \text { Preference }\end{array}\right\}$ Shs.

The par values were Sh. 10 and Sh. 9 for the ordinary and preference shares respectively. By 1 August 1993, applications had been received for 200,000 ordinary shares and 40,000 preference shares. The directors rejected the application for 80,000 ordinary shares and refunded the monies on 15 August 1993, and the remainder allotted five shares for every six shares applied for. Surplus application monies were carried forward to allotment.

All allotment took place on 20 August 1993 and the due amounts were received by 31 August 1993. The first and second calls were received by the due dates except for 3,000 ordinary shares which the directors declared forfeited on 20 November 1993. All the forfeited shares were reissued as fully paid to another shareholder on 30 November 1993 for Sh. 9 per share.

Assume that the number of shares outstanding prior to this additional issue amounted to: Ordinary -300,000 shares of Sh. 10 par
$-50,0007 \%$ preference shares of Sh. 7 par
All these shares had been issued at par.

## Required:

a) Journal entries including cash necessary to record the share transactions.
b) Prepare the share capital section of the Balance Sheet as at 31 December 1993.
(5 marks)
c) What is the importance of issuing bonus shares?
(Total: 20 marks)

## QUESTION FOUR



## Required:

Calculate for Mvita Ltd. for 1989 and 1990 the following ratios:
Return on capital employed;
Debtors turnover;
Creditors turnover;
Current ratio;
Quick assets (acid test) ratio;
Gross profit percentage;
Net profit percentage;
Dividend cover;
Gearing ratio.
Using the summarised accounts given and ratios you have just prepared, comment on the financial position and prospects of Mvita Ltd. (Total: 20marks)

## QUESTION FIVE

a) What are the qualities of useful financial statements
b) To what extent do International Accounting Standards assist in achieving some of these qualities.

## MOCK PAPER 3

## QUESTION ONE

Sijui is having difficulty in preparing a bank reconciliation statement as at 31 December 2001. He provides a summarized cashbook and a bank statement for the month of December as shown below. Although the bank statement is correct his cashbook has several errors.

Cashbook


Bank Statement - December 2001

|  |  |  | Dr | Cr | Balance |
| :---: | :---: | :---: | :---: | :---: | :---: |
| 1 Dec | Balance b/f |  | 44,000.00 |  | (44,000.00) |
|  |  | 8074 | 16,500.00 |  | (60,500.00) |
|  |  | 8080 | 10,555.05 |  | $(71,055.05)$ |
|  | Deposit |  |  | 9,800.45 | (61,254.60) |
|  |  | 8081 | 2,042.70 |  | $(63,297.30)$ |
|  | Deposit |  |  | 6,669.85 | $(56,627.45)$ |
|  | Deposit |  |  | 820.60 | $(55,806.85)$ |
|  |  | 8079 | 61,111.05 |  | (116,917.90) |
|  | Deposit |  |  | 928.40 | (115,989.50) |
|  |  | 8083 | 275,000.00 |  | $(390,989.50)$ |
|  | Standing order |  | 2,750.00 |  | (393,739.50) |
|  | Deposit |  |  | 170,500.00 | (223,239.50) |
|  | Deposit |  |  | 9,417.65 | $(213,821.85)$ |
|  | Deposit |  |  | 65,899.35 | (147,922.50) |
|  | Deposit |  |  | 6,488.90 | (141,433.60) |
|  |  | 8086 |  |  | $(141,514.45)$ |
|  |  | 8088 | 586.30 |  | (142,100.75) |
|  |  | 8082 | 7,138.45 |  | (149,239.20) |
|  |  | 8085 | 37,339.50 |  | (186,578.70) |
|  | Bank Charges |  | 4,400.00 |  | (190,978.70) |

## Required:

a) Prepare a corrected cashbook
b) A bank reconciliation as at 31 December and
c) A brief explanation as to the likely cause of the remaining difference.

## QUESTION TWO

Wananchi Transporters Company Ltd. was incorporated on 1 June 1994 and on the same day bought its first lorry, registration number KA 620, for Sh.4,536,000. On 3 April 1995, the company bought its second lorry, KA 735 for Sh.2,740,000. On 3 June 1997, the first lorry, KA 620 was involved in an accident and was completely written off. The insurance company paid the transport company Sh.l,350,000 for the loss. On 5 January 1998, the company bought its third lorry, KB 327 for Sh. $3,780,000$. Depreciation on the lorries was provided at 10 per cent on straight line basis. The policy of the company is to provide depreciation for the full year for all acquisitions made at any time during the year and to ignore depreciation on any lorry sold or disposed of during the year. All the lorries are insured. The company makes its accounts annually to 31 December. In 1998, the company decided to change its depreciation rate from 10 to 15 per cent on straight line basis for all its lorries still in use retroactively, that is from year of purchase. An adjusting entry will be made in the accounts for the year 1998.

## Required:

a) The motor lorries account for years 1994 to 1998.
(4 marks)
b) A schedule of additional depreciation arising from change of depreciation rate, for years 1994 to 1997.
c) Provision for depreciation account for the same period.
(9 marks)
d) Disposal of motor lorries account.
(3 marks)
(Total: 20 marks)

## QUESTION THREE (November 1998 Question 4)

a) Explain briefly the terms prime cost and factory cost as used by manufacturing firms.
(4 marks)
b) Rono Ltd. manufactures electric toys called Densta on small scale basis.

On 1 January 1997, 6000 units of Densta were in stock.
During 1997, the company manufactured 200,000 units and sold 190,000 units at a price of Sh. 6 each.

The following balances were extracted from the books of account on 31 December 1997.

| Stock of raw material 1.1.97 | 23,280 |
| :--- | ---: |
| Stock of raw material 31.12.97 | 32,560 |
| Purchase of raw material | 269,000 |
| Carriage on raw material | 82,400 |
| Direct wages | 185,400 |
| Factory expenses: | 76,800 |
| Rent and rates | 34,400 |
| Power | 31,280 |
| Insurance | 300,000 |

The following additional information was available:

1) Stocks of work-in-progress on 1 January and 31 December 1997 were of insignificant value and are to be ignored.
2) Plant and machinery are to be depreciated using reducing balance method at $10 \%$.
3) Finished units of Densta are valued at factory cost.
4) Factory cost per unit of Densta was the same in 1996 and 1997.

## Required:

i) The manufacturing account for the year ended 31 December 1997, showing clearly the prime cost and factory costs of producing Densta.
ii) The trading account for the year ended 31 December 1997.

## QUESTION FOUR

Mutiso Mwema started his business in Gikomba as a carpenter on 1 January1990 and he has not kept proper books of account. He engages you to examine his records and prepare appropriate accounts. From your examination of the records and from interviews with Mr. Mwema you ascertain the following information:
i) On starting the business on 1 January 1990, he put Sh.120,000 into a business bank account. On the same day, Mr. Mwema brought into the firm his pickup and reckoned that it was worth Sh. 66,000 then. He estimated that it will have another useful life of three years.
ii) To increase his working capital he borrowed Sh. 40,000 at $15 \%$ interest per annum on 1 April 1990 from his sister but no interest has yet been paid.
iii) On 1 January 1990 Miss Wambua was employed as a typist/clerk at a salary of Sh.72,000 per annum.
iv) Drawings were Sh. 1,800 per week from the business account for private use during the year.
v) He purchased timber worth Sh.196,000 out of which Sh.15,800 left in the workshop on 31 December 1990. He had also spent Sh.96,000 on some equipment at the commencement of the business which he estimates will last him five years.
vi) Electricity bills received up to 31 October 1990 came to Sh.24,000. Motor vehicle expenses were Sh.18, 200 while general expenses amounted to Sh. 27,000 for the year. The insurance premium for the year 31 March 1991 was Sh.16,000. All these expenses have been paid by cheque.
vii) Rates for the year to 31 March 1991 came to Sh.3,600 but they had not yet been paid.
viii) Miss Wambua sent out invoices to customers for Sh. 617,800 but only Sh.508,000 had been received by 31 December 1990. Debts totaling Sh.1,700 were abandoned during the year as bad. Other customers for jobs too small to invoice have paid Sh.72,600 in cash for work done of which Sh.56,000 was banked. Mr. Mwema used Sh. 7,500 of the difference to pay for his family's food stuff, bought Kenya Charity Sweepstake tickets worth Sh.2,400 and Miss Wambua used the rest of general expenses, except for Sh. 3,010 which was left over in the drawer in the office on 31 December 1990.
ix) You agree with Mr. Mwema that he will pay you Sh. 5,500 for accountancy fee.

## Required:

Prepare Profit and Loss Account for the year ended 31 December 1990 and a Balance Sheet as at that date. (Total: 20 marks)

## QUESTION FIVE

Comparability is a characteristic which adds to the usefulness of financial statements.
I.) Required:
(a) Explain what is meant by the term "comparability" in financial statements, referring to two types of comparison that users of financial statements may make.
(5 marks)
(b) Explain two ways in which the IAS (International Accounting Standards) aids the comparability of financial information.
II.) Explain four ways in which the use of historical cost accounting may cause users of financial statements to be misled when prices are rising.

## MOCK PAPER 4

## QUESTION ONE

a) Define the term bank reconciliation statement and indicate its three main functions.
(6 marks)
b) Juhudi Ltd. has two accounts "A" and "B" with different banks. On31 March 1995 the cash book showed a balance of Sh.200,000 in Account" A" and an overdraft of Sh. 90,000 in account"B". However the bank statements obtained on the same day showed different balances for the two accounts.

Further investigation reveals the following information: -

1. A deposit of Sh.60,000 made into account" A" on 1 March 1995 has been entered in the cash book in account "B".
2. A withdrawal of Sh. 20,000 from account" A" on 3 March 1995 has been debited in the cash book in account "B".
3. Cheques of Sh. 25,000 and Sh. 30,000 deposited in account" A" on 9 March 1995 were entered in the cash book in account" $\mathrm{B}^{\prime \prime}$. The second cheque has been dishonored by the bankers. The entry for this dishonored cheque has been entered in the cash book in account " B ".
4. Cheques for Sh. 40.000 and $S h .500 .000$ drawn on accounts" $A$ " and " $B$ " respectively on 30 March 1995 were not paid by the banks until 5 April 1995.
5. Incidental charges of Sh. 400 and Sh. 1.000 charged in the accounts" $A$ " and "B" respectively have not been entered in the cash book.
6. The bank has credited an interest of Sh.2.000 for account" A" and has debited bank charges of Sh.1,500 to account "B". These transactions have not been entered in the cash book.
7. Deposits of Sh.200,000 and Sh. 140,000 made into the accounts" A" and "B" respectively have not yet been credited by the bank.
8. Dividends amounting to $\mathrm{Sh} .8,000$ had been paid direct to the bank in account "B".
9. A cheque for Sh. 3.500 drawn on account" A" on 30 March 1995 in payment of an electricity bill had been entered in the cash book as Sh.5,300.
Required:
i) The necessary adjustments in both cash books in order to correct the errors.
(10 marks)
ii) Bank reconciliation statements for both cash books. (4 marks)
(Total: 20 marks)
(December 1995 Q5)

## QUESTION TWO

Reviewing the draft accounts of Uzee Ltd for the year ended 31 st December 2001 as prepared by the Chief Accountant, the Managing Director suggests that the written down value of plant is
too low. To support his argument he produces the following schedule of plant on hand at 31 December 2001:

| Item | Year of <br> Purchase | Cost | Life | Estimated Scrap <br> Value |  |
| :--- | ---: | ---: | ---: | ---: | ---: |
| Plant 1 | 1993 | 205,000 | 20 |  | 25,000 |
| Plant 2 | 1998 | 185,000 | 20 | 25,000 |  |
| Plant 3 | 1996 | 375,000 | 10 | 50,000 |  |
| Plant 4 | 1999 | 470,000 | 10 | 50,000 |  |
| Plant 5 | 1996 | 67,500 | 8 | 7,500 |  |
| Plant 6 | 2000 | 125,000 | 15 | 5,000 |  |
| Lorry | 2001 | $1,050,000$ | 4 | 250,000 |  |

After discussing the matter the following policy is agreed:

1) Each item of plant to be depreciated on a straight line basis to its estimated scrap value over its estimated life.
2) A full year's depreciation to be charged in the year of purchase. On investigation you ascertain that: There is no plant register.

Plant which includes the lorry is shown in the accounts at cost less proceeds of sales.
3) For some years depreciation was charged at $15 \%$ on the reducing balance and then from 31 st December 1994 at $10 \%$ of cost less proceeds of sales on a straight line basis.
4) The Plant account for the year ended 31st December 2001 was:

| Plant |  |  |  |
| :---: | :---: | :---: | :---: |
|  | Sh. |  | Sh. |
| Opening balance |  | Opening balance |  |
| Cost less sales | 4,100,000 | Depreciation todate | 3,050,000 |
| Lorry at cost less trade | 700,000 | Depreciation for year | 480,000 |
| Balance c/d | 3,530,000 | Balance c/d | 4,800,000 |
|  | 8,330,000 |  | 8,330,000 |

You are required to show, after implementing the new policy:
a) The Plant Account as it should appear in the books of the company for the year ended 31st December 2001
b) The entries which should appear in the Balance Sheet as on 31st December 2001 and
c) A note explaining the effect on the profits on the change of depreciation policy.
(Total: 20 marks)

## QUESTION THREE

The treasurer of Watembezi Sports Club has presented the following information for the year ended 31 October 1998:

|  | Sh. |  | Sh. |
| :---: | :---: | :---: | :---: |
| Receipts 1.11.97 |  | Payments:31.10.98 |  |
| Balance | 748,000 | Club extension | 650,000 |
| Subscriptions | 158,000 | Dinner dance expenses | 350,000 |
|  | 2,540,000 | New equipment | 300,000 |
|  | 67,000 | Bar purchases | 726,000 |
| Dinner Dance | 598,000 | Salaries and wages | 454,000 |
| Bar Sales | 932,000 | Other staff expenses | 129,000 |
| Harambee Donations | 529,000 | Coach fees | 260,000 |
| Seminar rentals | 158,000 | Life saver fees | 184,000 |
| Investment income | 247,000 | Investment purchased | 450,000 |
| Sale of old equipment (cost) | 62,000 | General expenses | 158,000 |
|  |  | Repairs and | 296,000 |
|  |  | maintenance | 2,082,000 |
|  | 6,039,000 | Balance c/d | 6,039,000 |


|  | 31.10 .97 | 31.10 .98 |
| :--- | ---: | ---: |
| Clubhouse | $2,450,000$ | $?$ |
| Equipment at cost | 325,000 | $?$ |
| Provision for depreciation | 95,000 | $?$ |
| Furniture and fittings at cost | 340,000 | $?$ |
| Provision for depreciation | 125,000 | $?$ |
| Subscription arrears - 1996/97 | 185,000 | $?$ |
| Subscriptions prepaid - $-1997 / 98$ |  | 324,000 |
|  | 124,000 | $?$ |
| Bar stock | 54,000 | 329,000 |
| Accrued salaries and wages | 254,000 | 28,000 |
| Unpaid dinner dance tickets | 23,000 | 29,000 |
| Investments |  | $?$ |
| Bar purchase creditors | $2,550,000$ | 234,000 |
| Unpaid club extension works | 168,000 | 85,000 |
| Club extension fund |  | $?$ |

## Notes:

1) The Harambee donations were for the extension of the club. The funds shall remain in this account until the works, are completed when' the balance will be transferred to the accumulated fund.
2) The depreciation on fixed assets is at $10 \%$ and $15 \%$ on cost on furniture and fittings; and equipment respectively.
3) Equipment which had cost Sh. 25,000 was sold on credit for Sh. 14,000 to a member who owed the club the money at the end of the year. The provision for depreciation on this equipment was Sh.7,000. Another equipment sold for cash had an accumulated provision for depreciation of Sh.19,000.
4) Audit fees of $S h .50,000$ should be provided.
5) Subscription in arrears are written-off after 12 months.

## Required:

a) Income and expenditure account for the year ended 31 October 1998
b) Balance as at 31 October 1998

## QUESTION FOUR

Mr. James Bulayi formed Malimia Traders, a sole proprietorship five years ago. His initial capital injection was Sh.1,000,000 cash. For a number of years, Bulayi's wife maintained the accounting records, but early in 1993 she became seriously ill. Mr. Bulayi consulted a CPA firm whose manager told him "you keep a record of your cash receipts and payments and a list of your assets and liabilities, at the beginning and end of the year, and I will prepare financial statements for you at the end of the year".

On 31 October 1993, Mr. Bulayi presented the following data to the Manager of the CPA firm.

|  | Sh. |
| :--- | ---: |
| Cash receipts during the current year: | $1,906,900$ |
| Collections from trade debtors | 400,000 |
| Proceeds of bank loan (repayable before 31 October 1994) | 873,000 |
| Cash sales | 15,900 |
| Interest on overdue customers account | $\underline{180,000}$ |
| Rent from building property | $\underline{, 375,800}$ |
| Total cash receipts |  |
|  |  |
| Cash payments during the current year: | $2,256,500$ |
| Trade creditor | 250,000 |
| Acquisition of equipment | 476,100 |
| Operating expenses | 9,800 |
| Insurance premium | 110,000 |
| Withdrawals by owner for personal use | 124,000 |
| Carriage inwards | 156,000 |
| Bank loan (including interest of Sh.6,000) | 34,000 |
| Other liabilities | $\underline{3,416,400}$ |
| Total cash payments |  |

## Additional information:

i) Although the primary source of revenue is from trading Malimia Traders also earns income from rent and interest. Malimia Trader conducts business from the ground floor of its twofloor storey building. The first floor is rented to a shoe-retailer for a monthly rent. The retailer pays 6 months rent in advance on 1 March and 1 September every year. Malimia Traders increased rent from Sh.15,000 per month to Sh. 20,000 per month with effect from 1 September 1993. Malimia Traders charges interest on overdue customers accounts, which customers usually pay together with the principal amount due. Interest owing by customers on 31 October 1993 was Sh.5,000.
ii) The following balances of assets and liabilities were extracted on 31 October 1992

|  | Sh |
| :--- | ---: |
| Prepaid insurance | 19,000 |
| Cash at bank | 184,600 |
| Trade debtors , | 585,600 |
| Interest due on customers accounts , | 9,000 |
| Stock | 389,000 |
| Equipment net | $1,240,000$ |
| Building net | $2,000,000$ |
| Bank loan | 100,000 |
| Interest owing on bank loan | 5,000 |
| Trade creditors | 475,000 |
| Other liabilities | 34,000 |

iii) Sh. 14,000 of debts had been written off during the accounting period, of which Sh. 8,500 was from sales of the previous accounting year, Bulayi estimated that Sh. 14,200 of the 31 October 1993 debtors balances may be uncollectable and a provision is required.
iv) Returns inwards and returns outward all applicable to current year's sales and purchases are Sh.60,000 and Sh.50,000 respectively.
v) Cash discount taken by credit customers in the year are Sh. 41,300 discounts on purchases are Sh.64,000.

Depreciation is to be provided on reducing balance on fixed assets held at year end at the rate of $5 \%$ per annum on building and $25 \%$ per annum on equipment. There were no disposals of plant assets during the year.

Interest owing on the bank loan at 31 October 1993 is Sh. 17,500 . The amount paid for insurance includes a premium of $\mathrm{Sh} 8,000$ paid to cover the firm against fire for the Co. six months to 31 January 1994.

Stock in hand on 31 October 1993 was valued at Sh985,000.

On 31 October 1993 the amounts owing to suppliers was Sh.523,000 and the amount owing by customers was Sh,663,2000 (excluding interest on overdue accounts). All purchases of stock are on credit.

Ground rent and land rates for the year amounted to Sh.50,000 The bills received in respect of the two are not yet paid.

## Required:

Malimia Traders' Trading, Profit and loss Account for the year ended 31 October 1993 and a Balance Sheet as at that date. (Toatal: 25 marks)

## QUESTION FIVE

a) What are accounting concepts, Bases, Policies?
b) Briefly explain the following accounting Concepts.
i) Going concern
ii) Accruals
iii) Consistency
iv) Prudence or conservatism
v) Materiality
vi) Substance over form
vii) Business entity concept
viii) Money measurement
ix) Historical cost
x) Objectivity
xi) Realization
xii) Duality

## MOCK PAPER 5

## QUESTION ONE

Cygnus is a sole trader selling antiques from a rented shop. He has not kept proper accounting records for the year ended 31 January 2001, in spite of his accountant"s advice after the preparation of his accounts for the year ended 31 January 2000.

His assets and liabilities at 31 January 2000 and 31 January 2001 were as follows:

|  | Reference to notes | 31 January |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  |  | 2000 |  | 2001 |  |
| Assets |  | Sh. | Sh. | Sh. | . Sh. |
| Shop equipment |  |  |  |  |  |
| Cost |  | 14,800 |  |  | To be |
| Less Depreciation | 2 | 6,900 | 7,900 |  | calculated |
| Inventory |  |  | 146,400 |  | 128,700 |
| Accounts receivable |  |  | 14,400 |  | 15,700 |
| Rent in advance | 3 |  | 1,000 |  | To be calculated |
| Cash at bank |  |  | - |  | 4,850 |
| Cash in hand |  |  | 800 |  | 900 |
| Liabilities |  |  |  |  |  |
| Loan - Draco | 4 |  | 24,000 |  | 12,000 |
| Accounts payable |  |  | 12,100 |  | 14,200 |
| Accrued expenses | 5 |  | 2,300 |  | To be calculated |
| Bank overdraft |  |  | 2,600 | See su | summary below |

The following summary shows receipts and payments by Cygnus.


Before banking the shop takings, Cygnus took various amounts as drawings.

## Notes

(1) Cygnus fixes his selling prices by doubling the cost of all items purchased.
(2) During the year, Cygnus sold for Sh. 300 equipment that had cost Sh. 800 , and had a written down value at 1 February 2000 of Sh .200 . He purchased further equipment on 1 August 2000 for Sh. 1,800.
(3) Depreciation is charged at $10 \%$ per year on the straight-line basis, with no depreciation in the year of sale and proportionate depreciation in the year of purchase.
(4) Rent is payable quarterly in advance on 1 January, 1 April, 1 July and 1 October each year. On 1 July 2000, the annual rent was increased from Sh.6,000 to Sh.9,000.
(5) The loan from Draco carries interest at $10 \%$ per year payable annually on 31 December. On 31 December 2000, Cygnus repaid Sh. 12,000 of the loan. The balance is repayable on 31 December 2004.
(6) The accrued expenses at 31 January 2000 consist of the Sh. 200 interest accrued on Draco.s loan (see Note 4) and sundry expenses of Sh.2,100. At 31 January 2001, accruals for sundry expenses amounted to Sh.3,300.

## Required:

(a) Prepare for Cygnus an income statement for the year ended 31 January 2001 and a balance sheet as at that date. (Total:20 marks)

## QUESTION TWO

Orion and Pegasus are two sole traders who decide to amalgamate their businesses into a partnership as from 1 January 2001.

Their balance sheets at 31 December 2000 are as follows:

|  | Orion |  | Pegasus |  |
| :---: | :---: | :---: | :---: | :---: |
|  | Sh."000 | Sh. "000 | Sh. ${ }^{\text {0 }} 000$ | Sh."000 |
| NON CURRENT ASSETS |  | 780 |  | 590 |
| CURRENT ASSETS |  |  |  |  |
| Inventory | 380 |  | 440 |  |
| Accounts receivable | 290 |  | 250 |  |
| Prepayments | 40 |  | 30 |  |
| Cash at bank | 420 | 1,130 | - | -720 |
|  |  | 1,910 |  | 1,310 |
| Capital accounts |  | 1,300 |  | 800 |
| Non - current liabilities |  |  |  |  |
| Loan - Nimrod |  | 300 |  |  |
| CURRENT LIABILITIES |  |  |  |  |
| Accounts payable | 280 |  | 310 |  |
| Accruals | 30 |  | 20 |  |
| Bank overdraft | -_ | 310 | 180 | 510 |
|  |  | 1,910 |  | 1,310 |

The agreed terms of the amalgamation are:
(1) Goodwill, which does not appear in the records of either business, is valued at:

Sh. "000
Orion
200
Pegasus 180

Goodwill is not to appear in the opening balance sheet of the partnership.
(2) Profit-sharing ratios in the partnership are agreed as:

| Orion | $60 \%$ |
| :--- | :--- |
| Pegasus | $40 \%$ |

(3) Land included in Orion.s non-current assets at Sh. 100,000 to be revalued to Sh.130,000.
(4) Orion and Pegasus did not transfer their motor cars to the new business but retained them personally. The motor cars are currently included in their non-current assets at their book value as follows:

Sh."000
Orion 18
Pegasus 16
(5) Orion"s loan from Nimrod was repaid by Orion on 31 December 2000.
(6) The remaining balance of Orion"s cash, and the overdraft of Pegasus, were combined into a single bank account for the partnership.
(7) All other assets and liabilities of the businesses were brought into the partnership at their stated book value.

## Required:

(a) Show the capital accounts of the two traders to record the closure of their businesses.
(5 marks)
(b) Prepare the opening balance sheet of the new partnership of Orion and Pegasus as at 1 January 2001.
(c) Explain why asset revaluations and a goodwill adjustment may be needed when a partner retires or dies, a new partner is admitted or there is a change in profit-sharing ratios.(4 marks)
(Total: 20 marks)

## QUESTION THREE

The directors of Hawk, a limited liability company, wish to compare the company"s most recent financial statements with those of the previous year. The company"s financial statements aregiven below:
Hawk
Income statements

|  | Year ended |  |
| :--- | :---: | ---: |
|  | 31 March $\mathbf{1 9 9 9}$ | 31 March 2000 |
| Sh. |  |  |
| Sales revenue ( $80 \%$ on credit and $20 \%$ cash $)$ | 1,800 | 2,500 |
| Cost of sales (see note below) | $\underline{(1,200)}$ | $\underline{(1,800)}$ |
| Gross profit | 600 | 700 |
| Distribution costs | $(160)$ | $(250)$ |
| Administrative expenses | $\underline{(200)}$ | $(\underline{200)}$ |
| Profit and operations | $-(50)$ | 250 |
| Finance cost | 190 | $-(50)$ |
| Profit before tax | $\underline{(44)}$ | 200 |
| Income tax expense | $\underline{146}$ | $\underline{(46)}$ |
| Net profit for the period |  | $\underline{154}$ |

Note: Cost of sales figures are made up as follows:

|  | Year ended |  |
| :--- | :---: | ---: |
|  | 31 March 1999 | 31 March 2000 |
|  | Sh.000 | Sh.000 |
| Opening inventory | 180 | 200 |
| Purchases (all on credit) | $\underline{1,220}$ | $\underline{1,960}$ |
|  | 1,400 | 2,160 |
| Less closing inventory | $\underline{(200)}$ | $\underline{(360)}$ |
| Cost of sales | $\underline{1,200}$ | $\underline{1,800}$ |


*The additional share capital was issued on 1 April 1999

## Required:

(a) Calculate, for each of the two years, eight accounting ratios which should assist the directors in their comparison, using closing figures for balance sheet items needed.
(8 marks)
(b) Suggest possible reasons for the changes in the ratios between the two years. (12 marks)

## QUESTION FOUR

(a) Why do some businesses keep a petty cashbook as well as a cashbook?
(b) Kathryn Rochford keeps her petty cashbook on the imprest system, the imprest being Sh.25. For the month of April 20X9 her petty cash transactions were as follows:

|  |  | Sh. |
| :---: | :--- | ---: |
| Apr 1 | Petty cash balance | 1.13 |
| " | 2 | Petty cashier presented vouchers to cashier and obtained cash to restore <br> the imprest |
|  |  | 23.87 |
| " | 4 | Bought postage stamps |
| " | 9 | Paid to Courtney Bishop, a creditor |
| " | 11 | Paid bus fares |
| " | 17 | Bought envelopes |
| " | 23 | Received cash for personal telephone call |
| " | 26 | Bought petrol |

(i) Enter the above transactions in the petty cashbook and balance the petty cashbook at 30 April, bringing down the balance on 1 May.
(ii) On 1 May Kathryn Rochford received an amount of cash from the cashier to restore the imprest. Enter this transaction in the petty cashbook.
(c) Open the ledger accounts to complete the double entry for the following:
(i) The petty cash analysis columns headed Postage and Stationery and Travelling Expenses;
(iii) The transactions dated 9 and 23 April 20X9.

## QUESTION FIVE

a) Accounting Ratios have been used by a number of companies as indicators of their financial performance in the present and even in the future. Discuss the five limitations associated with their use for this purpose.
b) List and explain five characteristics of a partnership.

## Answers - Mocks

## MOCK PAPER 1

## QUESTION ONE



Capital accounts

|  | Anne Shs | Charlotte Shs | Emily Shs | Balance <br> Goodwill <br> $50: 30: 20$ <br> Revaluation <br> $50: 30: 20$ | Anne Shs | Charlotte Shs | Emily Shs |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Goodwill |  | 100,000 | 100,000 |  | 180,000 | 170,000 | 160,000 |
| T"fer loan | 300,000 |  |  |  | 100,000 | 60,000 | 40,000 |
| Balance |  | 142,000 | 108,000 |  | 20,000 | 12,000 | 8,000 |
|  | 300,000 | 242,000 | 208,000 |  | 300,000 | 242,000 | 208,000 |

Current accounts

| Balance <br> Drawings | Anne Shs | Charlotte Shs | Emily Shs | Balance Share of profit: | Anne Shs | Charlotte Shs | Emily Shs |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | 21,000 | $\begin{array}{r} \hline 2,000 \\ 37,000 \end{array}$ | 36,000 |  | 3,000 |  | 2,000 |
|  |  |  |  |  |  |  |  |
| T"fer loan Balance | 7,000 |  |  | 50: 30 : 20 | 25,000 | 15,000 | 10,000 |
|  |  | 1,000 | 1,000 | $50: 50$ |  | 25,000 | 25,000 |
|  | 28,000 | 40,000 | 37,000 |  | 28,000 | 40,000 | 37,000 |

Loan Account - Anne

| Balance | Shs |  | Shs |
| ---: | ---: | ---: | ---: |
|  | 307,000 | Anne - Capital a/c | 300,000 |
|  | $\underline{307,000}$ | - Current a/c | $\underline{7,000}$ |
|  | $\underline{307,000}$ |  |  |

## QUESTION TWO

| Plant and Machinery - Cost |  |  |  |  |  |  |
| :--- | :--- | :--- | :--- | :---: | :---: | :---: |
| 1998 | Shs |  |  |  | $\mathbf{1 9 9 9}$ | Shs |
| 1 Jan | Opening balance | 819,000 | 31 Mar |  |  |  |
| 10 Jan | Cash | $\underline{45,900}$ |  |  |  |  |
| 864,900 |  |  |  |  |  |  |
|  |  | $\underline{864,900}$ |  |  |  |  |

Plant and Machinery - Accumulated depreciation

| $\mathbf{1 9 9 9}$ | Shs | 1998 |  | Shs |
| :--- | ---: | :--- | :--- | ---: |
| 31 | Balance | 522,169 | 1 Jan | Opening balance |


| Motor vehicles - cost |  |  |  |  |
| :--- | :--- | :--- | :--- | :---: |
| 1998 |  | Shs | 1998 |  |
| 1 Jan | Opening balance | 148,000 | 18 Apr | Transfer - disposal |
| 18 | M V Disposal | 5,000 | 1999 |  |
| Apr |  |  |  | 12,000 |
|  | Cash | $\underline{13,000}$ | 31 Mar | Balance |
|  |  | $\underline{166,000}$ |  | $\underline{154,000}$ |
|  |  |  | $\underline{166,000}$ |  |



## Workings

Plant and machinery
Shs $819,000 \times 15 \% \times 15$ months 153,563
Shs $45,900 \times 15 \% \times 15$ months $\quad 8,606$

Motor vehicles:

| Shs $136,000 \times 25 \% \times 15$ months | 42,500 |
| :--- | ---: |
| Shs $18,000 \times 25 \% \times 12$ months | 4,500 |
| Shs $12,000 \times 25 \% \times 3$ months | Shs $\underline{47,750}$ |

## QUESTION THREE

Income statement for the year ended 30 June 1999
Sh. "000
Sales revenue (14,800-24)
14,776
Cost of sales (W1)
10,280
Gross profit

| Distribution costs $(1,080+190-120+272)$ | $(1,422)$ |
| :--- | :---: |
| Administrative expenses $(1,460+70-60+272)$ | $(1,742)$ |
| Profit from operations | 1,332 |
| Finance cost | $\underline{(50)}$ |
| Net profit for the period | $\underline{1,282}$ |

Balance sheet as at 30 June 1999

| ASSETS | Shs"000 | Shs"000 |
| :--- | ---: | ---: |
| Non-current assets |  | 25,470 |
| Property, plant and equipment (W3) |  |  |
| Current assets | 1,566 |  |
| Inventory | 4,276 |  |
| Trade receivables $(4,120-24+180)$ | $\underline{60}$ | $\underline{6,002}$ |
| Cash at bank |  | $\underline{31,472}$ |
| EQUITY AND LIABILITIES |  |  |
| Capital and reserves |  | 14,000 |
| Issued share capital |  | 4,000 |
| Share premium account |  | 4,500 |
| Revaluation reserve $(3,000+1,500)$ | $\underline{4,422}$ |  |
| Accumulated profits $(3,140+1,282)$ |  | 2,922 |
| Non-current liabilities | 2,240 | 2,000 |
| 10\% loan notes | $\underline{310}$ | $\underline{2,550}$ |
| Current liabilities |  | $\underline{31,472}$ |
| Trade payables |  |  |
| Accrued expenses $(260+50)$ |  |  |

(b) Statement of changes in equity, year ended 30 June 1999

|  | Share <br> capital Shs. „000" | Share premium Shs. „000" | Revaluation reserve Shs. „000" | Accumulated profit <br> Shs. „000" | Total Shs. „000" |
| :---: | :---: | :---: | :---: | :---: | :---: |
| Balance at 1st July | 10,000 | 2,000 | 3,000 | 3,140 | 18,140 |
| 1998 |  |  |  |  |  |
| Surplus on revaluation of properties |  |  | 1,500 |  | 1,500 |
| Net profit for period |  |  |  | 1,282 | 1,282 |
| Issue of share capital | 4,000 | 2,000 |  |  | 6,000 |
|  | 14,000 | 4,000 | 4,500 | 4,422 | 26,922 |

## Workings

(1)

Cost of sale
Shs"000

## Shs"000

Opening inventory
1,390
Purchases
8,280
Less: closing inventory:
9,670
As originally taken
1,560
Reduction for adjustment (i)
Increase for adjustment (ii)
(10)
$16 \quad 1,566$

| Depreciation (W2) |  |  |  | $\begin{gathered} 8,104 \\ \underline{2,176} \\ \underline{10,280} \end{gathered}$ |
| :---: | :---: | :---: | :---: | :---: |
| (2) |  |  |  |  |
| Depreciation |  |  | Shs"000 |  |
| Buildings |  |  | 160 |  |
| Plant and equipment |  |  | 2,560 |  |
|  |  |  | 2,720 |  |
| Cost of sales |  |  | 2,176 |  |
| Distribution costs |  |  | 272 |  |
| Administrative expenses |  |  | 272 |  |
|  |  |  | 2,720 |  |
| (3) |  |  |  |  |
| Non-current assets |  |  |  |  |
|  | Shs. „000" | Buildings Shs. „000" | Plant and Equipment Shs. , $0000^{\prime \prime}$ | Shs. „000" ${ }^{\text {Total }}$ |
| Per list of account balances | 10,500 | 8,000 | 12,800 | 31,300 |
| Revaluation | 1,500 |  |  | 1,500 |
|  | 12,000 |  |  | 32,800 |
| $1998$ |  |  |  |  |
| charges for year |  | (160) | $(2,560)$ | $(2,720)$ |
|  | 12,000 | 5,710 | 7,760 | 25,470 |

## QUESTION FOUR

Accounts receivable ledger control account

|  | Shs |  | Shs |
| :--- | ---: | :--- | ---: |
| Opening balances | 386,430 | Opening balances | 190 |
| Sales $(163,194+1,386)$ | 164,580 | Cash received | 158,288 |
| Cash refund | 350 | Discounts allowed | 2,160 |
|  |  | Returns inwards | 590 |
|  |  | Contra | 870 |
| Cad debts written off | 1,360 |  |  |
| Closing balances | $\underline{370}$ | Closing balances | $\underline{388,272}$ |
|  | $\underline{551,730}$ |  |  |

Accounts payable ledger control account

|  | Shs | Shs |  |
| :--- | ---: | :--- | ---: |
| Opening balances | 520 | Opening balances | 184,740 |
| Cash paid $(103,040-350)$ | 102,690 | Purchases $(98,192+36)$ | 98,228 |
| Discounts received | 990 | Bad debt written off | 420 |
| Returns outwards $(1,370+2,000)$ | 3,370 | 870 |  |
| Contra | $\underline{175,048}$ | Closing balances |  |
| Closing balances | $\underline{283,488}$ |  | $\underline{100}$ |
|  |  | $\underline{283,488}$ |  |

## QUESTION FIVE

(b) (i) Depreciation is based on the historical cost of non-current assets and thus does notreflect the true value to the enterprise of the use of those assets.
(ii) The holding gain arising when inventory is held while prices are rising is included in trading profit, thus overstating the profit.
(iii) Assets are shown in the balance sheet at cost less depreciation when their true value may be much greater. The true value of the assets of the enterprise is thereby obscured.
(b) (i) Reserves are balances in a company"s balance sheet forming part of the equity interest and representing surpluses or gains, whether realised or not.
(ii) Share premium account

The surplus arising when shares are issued at a price in excess of their par value. Revaluation reserve
The unrealized gain when the amount at which non-current assets are carried is increased above cost.
(Other examples given credit on their merits)
(c) A bonus issue is the conversion of reserves into share capital, with shares being issued to existing members in proportion to their shareholdings, without any consideration being given by the shareholders.

A rights issue is again an issue of shares to existing members in proportion to their shareholdings, but with payment being made by the shareholders for the shares allotted to them.

The fundamental difference between them is that the rights issue raises funds for the company whereas the bonus issue does not.

## MOCK PAPER 2

## QUESTION ONE

a) Adjustments


John and Dan
Statement of adjusted Net profit for the year ended 31 December 1998.

Sh.
Sh.
Profit as per Accounts
Add
Stock omitted 480,000.00
Prepaid trade license

Less:

| Elec Accrued | $446,000.00$ |  |
| :--- | ---: | ---: |
| Decrease in stock | $300,000.00$ |  |
| Increase in Provision for doubtful debts | $80,000.00$ |  |
| Additional depreciation of plant | $200,000.00$ |  |
| Loss on disposal | $\underline{200,000.00}$ | $\underline{(1,226,000.00)}$ |
| Corrected Profit |  | $\underline{14,540,000.00}$ |

b) John and Dan

Balance Sheet as at 31 December 1998

|  | Cost | Depreciation | NBV |
| :---: | :---: | :---: | :---: |
| Non Current Assets |  |  |  |
| Land and buildings | 29,800,000.00 | - | 29,800,000.00 |
| Plant and Machinery | 32,000,000.00 | (15,200,000.00) | 16,800,000.00 |
| Motor Vehicles | 12,000,000.00 | (4,400,000.00) | 7,600,000.00 |
|  | 73,800,000.00 | (19,600,000.00) | 54,200,000.00 |
| Current Assets |  |  |  |
| Stock on Hand |  | 9,180,000.00 |  |
| Sundry Debtors | 24,086,000.00 |  |  |
| Less Provision for doubtful debts | (560,000.00) | 23,526,000.00 |  |
| Prepaid expenses |  | 86,000.00 |  |
| Cash and Bank balances |  | 2,694,000.00 |  |
|  |  | 35,486,000.00 |  |
| Current Liabilities |  |  |  |
| Sundry Creditors | 18,600,000.00 |  |  |
| Accruals | 446,000.00 | (19,046,000.00) | 16,440,000.00 |
|  |  | 70,640,000.00 |  |
| Capital | John |  | 43,270,000.00 |
|  | Dan |  | 27,370,000.00 |
|  |  |  | 70,640,000.00 |


|  |  |  |  |  |  |  |
| :--- | ---: | ---: | :--- | :---: | :---: | :---: |
|  | John | Dan |  | John | Dan |  |
| Drawings | $6,400,000.00$ | $2,900,000.00$ | Balance $/$ b/f | $42,400,000.00$ | $23,000,000.00$ |  |
| Balance c/d | $\underline{43,270,000.00}$ | $\underline{27,370,000.00}$ | Profit | for | $\underline{7,270,000.00}$ | $\underline{7,270,000.00}$ |
|  | $\underline{49,670,000.00}$ | $\underline{30,270,000.00}$ | year | $\underline{49,670,000.00}$ | $\underline{30,270,000.00}$ |  |

Debtors

|  | Sh. |  | Sh. |
| :--- | :---: | :--- | ---: |
| Balance b/f | $24,600,000.00$ | Dan - Drawings | $700,000.00$ |
| Cashbook | $406,000.00$ | Cashbook | $100,000.00$ |
|  |  | Provision for debts | $120,000.00$ |
|  |  | $\underline{25,006,000.00}$ |  |
|  |  | $\underline{24,086,000.00}$ |  |
|  |  | $\underline{25,006,000.00}$ |  |

Provision for doubtful debts

|  | Sh. |  | Sh. |
| :--- | :---: | :--- | ---: |
| Debtors | $120,000.00$ | Balance b/f | $600,000.00$ |
| Balance c/d | $\underline{560,000.00}$ | Profit and Loss a/c | $\underline{60,000.00}$ |
|  | $\underline{680,000.00}$ |  | $\underline{880,000.00}$ |

## QUESTION TWO

## a) Pesa, Akili and Tajiri

Profit and loss Appropriation account for the year ended 31 March 1996
Six months to Six months to Total
30.09.1995 31.03.1996

Total
Sh.
Net Profit for
180,000.00
Sh.
Sh.
360,000.00
year
Commission to Tajiri

$\overline{180,000.00} \quad$|  | $(18,000.00)$ | $(18,000.00)$ |
| :--- | :--- | :--- |
| $162,000.00$ | $342,000.00$ |  |

Less:
Interest on capital

| Pesa 20,000.00 | $20,000.00$ | $20,000.00$ | $40,000.00$ |
| :--- | ---: | ---: | ---: |
| Akili $15,000.00$ | $15,000.00$ | $15,000.00$ | $30,000.00$ |
| Tajiri | $\overline{(35,000.00)}$ | $10,000.00$ | $10,000.00$ |
|  | $145,000.00$ | $(45,000.00)$ | $(80,000.00)$ |
| Salaries | $(117,000.00$ | $262,000.00$ |  |
| Akili | $127,000.00)$ | $(21,000.00)$ | $(39,000.00)$ |
| Balance of Profits |  | $96,000.00$ | $223,000.00$ |
| shared in PSR |  |  |  |
| Pesa | $76,200.00$ | $32,000.00$ | $108,200.00$ |
| Akili | $50,800.00$ | $32,000.00$ | $82,800.00$ |
| Tajiri | $\underline{(127,000.00)}$ | $\underline{(96,000.00}$ | $\underline{32,000.00}$ |
|  |  | $\underline{223,000.00)}$ |  |

b)

Current Accounts


1. Capital contributed by Tajiri was sh. $200,000(50 \%$ X 400,000 )
2. Interest on capital is $5 \%$ on the respective capital balances for each period.
3. Akili's salary is sh $18,000(6 \times 3,000)$ for the first six months and $21,000(6 \times 3,500)$ for the last 6 months.
4. Because Tajiri's salary did not fall below sh $31,000(62,000 / 2)$ then his profit share remains sh. 32,000
Incase his share was below sh. 31,000 then Pesa and Akili would have contributed equally from their profits to make it sh. 31,000 .
5. Goodwill is arrived at as
follows: Year Profits
199360,000.00
199450,000.00
199570,000.00
TOTAL 180,000.00
Average Per year (3) 60,000.00
Goodwill $=$ Average Profits X 2 years purchase $120,000.00$

Goodwill shared between Akili and Pesa in the old profit sharing ratio and written off from the three partners accounts in the new profit sharing ratio.

## QUESTION THREE

a)
Debit Sh
600,000.00
i) Cashbook
Credit
Sh

> Workings
> OSC
$(200,000 \times 2.5)=500,000$
Application Account

$$
600,000.00
$$

Cash received on application
ii) Application Account 200,000.00
Cashbook

$$
\begin{array}{cc}
200,000.00 & \text { OSC } \\
(80,000 \times 2.5)=200,000
\end{array}
$$

Cash refunded to ordinary shares rejected
iii) Application Account 400,000.00
Ordinary Share capital

$$
\begin{aligned}
250,000.00 & \text { OSC } \\
& (100,000 \times 2.5)=250,000 \\
100,000.00 & \text { PSC } \\
& (40,000 \times 2.5)=100,000 \\
50,000.00 & \text { Bal OSC } \\
& (20,000 \text { X 2.5) }=50,000
\end{aligned}
$$

Preference Share capital
Allotment Account
Shares allotted to applicants balance to allotment account.
iv) Allotment Account 430,000.00
Ordinary Share capital

$$
\begin{aligned}
& \text { 250,000.00 OSC } \\
& (100,000 \times 2.5)=250,000 \\
& \text { 60,000.00 PSC } \\
& (40,000 \times 1.5)=60,000 \\
& \text { 120,000.00 } \\
& \{(100,000 \times 1)+(40,000 \times 0.5)=120,000
\end{aligned}
$$

Preference Share capital
Share Premium
Amounts receivable on Allotment
v) Cashbook 380,000.00
(430,000 receivable on allotment less the
Allotment Account

$$
380,000.00 \quad \text { overpayment on }
$$

Cash received on allotment of shares application of Sh. 50,000)
vi) First call Account

Ordinary Share capital
Preference share capital
400,000.00
$300,000.00(100,000 \times 3)=300,000$
$100,000.00 \quad(40,000 \times 2.5)=100,000$
Amount receivable on First call
vii) Dr Cashbook

Calls in arrears
First call Account
viii) Second Call account

Ordinary share capital
Preference share capital
ix) Cashbook

Second Call account
Cash received on second call
x) Ordinary share capital

Share premium Account
Forfeited shares

$$
\begin{aligned}
391,000.00 & (97,000 \times 3)+(40,000 \times 2.5)=391,000 \\
9,000.00 & (3,000 \times 3)=2900
\end{aligned}
$$

294,000.00

$$
\begin{array}{lr}
194,000.00 & (97,000 \times \text { X } 3)=194,000 \\
100,000.00 & (40,000 \times 2.5)=100,000
\end{array}
$$

294,000.00
294,000.00

| $24,000.00$ | (Application) OSC (3,000 X 2.5) $=7,500$ |
| :---: | :--- |
| $3,000.00$ | (Allotment) OSC $(3,000 \times 2.5)=7,500$ |
| $27,000.00$ | (First call) OSC $(3,000 \times 3)=9,000$ |
|  | (Allotment)Spre (3,000 X 1) $=3,000$ |

Shares cancelled and forfeited
xi) Forfeited shares $\quad 9,000.00$

Calls in arrears
9,000.00
Balance on calls in arrears now cancelled and forfeited.
xii) Cashbook 27,000.00 (3,000 X 9) $=27,000$

Forfeited shares
27,000.00
Cash received on forfeited shares now reissued.
xiii) Forfeited shares

45,000.00
Ordinary share capital
30,000.00
Share premium Account
15,000.00
Balance on forfeited shares now allocated between Ordinary shares and Share premium. Ledger Accounts although not required are shown for purpose of clarity.

|  | Application Account |  |  |
| :--- | :---: | ---: | :---: |
|  | Sh. |  | Sh. |
| Cashbook |  | $200,000.00$ | Cashbook |
| Ordinary | share | $250,000.00$ |  |
| capital |  | $\underline{00,000.00}$ |  |
| Preference <br> capital | share | $\underline{50,000.00}$ |  |
| Allotment Account | $\underline{600,000.00}$ |  |  |
|  |  |  | $\underline{600,000.00}$ |

## Allotment Account

|  | Sh. |  |  |  |
| :--- | :--- | ---: | ---: | :---: |
| Sh. |  |  |  |  |
| Ordinary | share | $250,000.00$ | Cashbook | $430,000.00$ |
| capital |  | $60,000.00$ |  |  |
| Preference | share | $\underline{120,000.00}$ |  | $\underline{430,000.00}$ |
| capital |  | $\underline{430,000.00}$ |  |  |



## QUESTION FOUR

MVITA
i) Return on Capital employed
(ROCE)
$\begin{array}{lll}\text { Net Profit before Int + tax } \\ \text { Shrhldrs funds + Long-term debt } & \underline{1,000,000} & \underline{700,000} \\ 5,180,000\end{array}$
$28.25 \% \quad 13.51 \%$
(Interest of 200,000 and 300,000 is added back to 1989 and 1990 profits before tax respectively)
ii) Debtors turnover

| Sales | $4,000,000$ <br> Average debtors | $4,000,000$ <br> 900,000 |
| :--- | ---: | ---: |
|  | 5 times | 4.44 times |

In 1989 the opening debtors is missing so closing debtors is taken as average debtors.
iii) Creditors turnover

| Cost of sales | $\underline{2,000,000}$ | $\underline{2,400,000}$ |
| :--- | ---: | :--- |
| Average creditors | 800,000 | $1,000,000$ |
|  | 2.5 times | 2.4 times |

iv) Current ratio

| Current assets | $\frac{1,960,000}{1,200,000}$ | $\frac{2,300,000}{1,680,000}$ |
| :--- | ---: | ---: |
| Current liabilities | 1.63 | 1.369 |

v) Quick ratio

| Current assets - Stock | $\underline{1,960,000}$ | $-1,100,000$ | $\underline{2,300,000-1,300,000}$ |
| :--- | :--- | :--- | :--- |
| Current liabilities | $1,200,000$ |  |  |

vi) Gross Profit Percentage $\quad \frac{1,960,000}{1,200,000} \underline{\underline{2,300,000}}$

| Gross Profit | $\underline{2,000,000}$ | $\underline{1,600,000}$ |
| :--- | ---: | ---: |
| Sales | $4,000,000$ | 4000,000 |
|  | $50 \%$ | $40 \%$ |

vii) Net Profit Percentage

Net Profit
$\frac{800,000}{4,000,000} \quad \underline{4,000,000}$
$20 \% \quad 10 \%$
viii) Dividend Cover

Net profit $\quad \underline{800,000} \quad \underline{400,000}$

Dividend

$$
400,000
$$

$$
400,000
$$

1
ix) Gearing ratio

Long-term debt ( Debentures ) 2,000,000 $\underline{3,000,000}$
Net Assets 3,540,000 5,180,000
$56.50 \% \quad 57.90 \%$
b) The overall performance of Mvita ltd for 1990 is not good as compared to 1989. This is reflected by the decline in the profitability as shown by the Return on Capital employed, the Gross profit and Net profit percentages as these ratios have reduced. Gross profit percentage has reduced due to increase in the cost of goods in 1990 with no corresponding increase in turnover.

The liquidity position has also declined marginally as shown by the decline in the current ration from 1.63 to 1.369 as the liabilities have increased to a greater proportion as compared to the increase in the current assets. This position also explains the change from cash position to overdraft.

Mvita's efficiency (use of resources) has declined but slightly as shown by the debtors and creditors turnover. This is caused by the increase in debtors and creditors level with minimal changes in the turnover and cost of sales.

The gearing level has increased but slightly again as shown by the gearing ratio which is not a good indicator a far as the financial risk is concerned. This is expected as Mvita has taken up additional debentures.

## QUESTION FIVE

## a) Qualities of useful Financial Information.

The four principal qualities of useful financial information are understandability, relevance, reliability and comparability.

Understandability: an essential quality of the information provided in the financialstatements is that it is readily understandable by users. For these reason users are assumed to have a reasonable knowledge of business and economic activities and accounting.

Relevance: information has the quality of being relevant when it influences the economic decisions of users by helping them evaluate past, present or future events or confirming or correcting their past evaluations. The relevance of information is affected by its nature and materiality.

Reliability: information is useful when it is free from material error and bias and can bedepended upon by users to represent faithfully that which it purports to represent or could reasonably be expected to represent. To be reliable then the information should:
a) Be represented faithfully,
b) Be accounted for and presented in accordance with their substance and economic reality and not merely their legal form,
c) Be neutral i.e. free from bias,
a) Include some degree of caution especially where uncertainties surround some events and transactions (Prudence),
b) Be complete i.e. must be within the bounds of materiality and cost. An omission an cause information to be false.

Comparability: Users must be able to compare the financial statements of an enterprisethrough time in order to identify trends in its financial position and performance. Users must also be able to compare the financial statements of different enterprises. Therefore users must be informed of the different accounting policies. Changes in the various policies and the effect of these changes in the accounts.

Compliance with International Accounting standards Promotes comparability of financial statements among different organizations.

## MOCK PAPER 3

## QUESTION ONE

a)

## Sijui Cashbook

|  | Sh. |  | Sh. |
| :--- | ---: | :--- | ---: |
| December | $590,411.25$ | December | $385,006.60$ |
| Opening balance | 110.00 | Error on opening balance | $385,006.60$ |
| Error on addition | $64,488.90$ | Opening | balance |
| Deposits (omitted) | $3,465.00$ | (overdraft) | $27,501.10$ |
| Error on cheque | $\underline{204,189.15}$ | Discounts | $2,750.00$ |
| Balance c/d | $\underline{804,664.30}$ | Standing order | $\underline{4,400.00}$ |
|  |  | $\underline{804,664.30}$ |  |
|  |  |  |  |

b) Bank reconciliation statement as at 31 December 2001

Sh.
Balance per updated cashbook (overdraft)
Add unpresented cheques

| 8084 | $6,789.75$ |  |
| ---: | ---: | ---: |
| 8087 | $1,091.20$ | $7,880.95$ |
|  | $(196,308.20)$ |  |
|  | $(190,978.70)$ |  |
|  | $(5,329.50)$ |  |

Balance as per bank statement Unexplained difference
c) The unexplained difference of Sh. 5236.5 could be due to a cheque or cheques from the previous period that have not been presented so far.

## QUESTION TWO

a)

Motor Lorries Account

|  | Sh. ${ }^{\text {"000 }}$ |  | Sh. ${ }^{\text {"000" }}$ |
| :---: | :---: | :---: | :---: |
| 1994 |  | 1994 |  |
| Cashbook | 4,536.00 | Balance c/d | 4,536.00 |
| 1995 |  | 1995 |  |
| Balance b/f | 4,536.00 | Balance c/d | 7,276.00 |
| Cashbook | 2,740.00 |  | 7,276.00 |
|  | 7,276.00 |  |  |
| 1996 |  | 1996 |  |
| Balance b/f | 7,276.00 | Balance c/d | 7,276.00 |
| 1997 |  | 1997 |  |
| Balance b/f | 7,276.00 | Disposal | 4,536.00 |
| Balance c/d | $\underline{2,740.00}$ | Balance c/d | $\underline{\text { 2,740.00 }}$ |
|  | 7,276.00 |  | 7,276.00 |
| 1998 |  | 1998 |  |
| Balance b/f | 2,740.00 | Balance c/d | 6,520.00 |
| Cashbook | 3,780.00 |  |  |
|  | $\underline{6,520.00}$ |  | 6,520.00 |

b) Additional depreciation only affects vehicle number KA 735 as it was the only vehicle still in use in 1998.

d)

| Motor Lorries Disposal |  |  |  |
| :---: | :---: | :---: | :---: |
|  | Sh. |  | Sh. |
| 1997 |  | 1997 |  |
| Motor Vehicle | 4,536.00 | Depreciation | 1,360.80 |
|  |  | Cashbook | 1,350.00 |
|  |  | P \& L | 1,825.00 |
|  | 4,536.00 |  | 4,536.00 |

## QUESTION THREE

a) Prime Cost also called direct cost are the costs that can be traced to each unit produced examples include raw materials and direct labour. Factory overhead also called indirect costs are costs incurred in the production of goods but cannot be directly attributed to any one particular unit. Examples include Managers salaries. Factory rent, depreciation of plant and machinery and other factory expenses like lighting and water.
b)
i)

## Rono Ltd

Manufacturing account for the year ended 31 December 1997
Raw Materials

| Opening Stock |  |
| :--- | ---: |
| Purchases | $269,000.00$ |
| Carriage inwards | $82,400.00$ |

Less: closing stock
Cost of raw materials consumed
Direct wages
Prime Cost
Factory Overheads
Rent and rate 76,800.00
Power
34,400.00
Insurance
31,280.00
Depreciation of plant and machinery $\quad \underline{30,000.00} \quad \underline{172,480.00}$
Cost of Production - Finished goods
700,000.00
$\begin{array}{lr}\text { Number of units produced } & 200,000 \\ \text { Cost per unit }(700,000.00 / 200,000) & 3.50\end{array}$
ii) Rono Ltd

Trading account for the year ended 31 December 1997

|  | Sh | Sh |
| :--- | ---: | ---: |
| Sales |  | $1,140,000.00$ |
| Less Cost of sales | $21,000.00$ |  |
| Opening Stock | $700,000.00$ |  |
| Cost of goods produced | $721,000.00$ |  |
|  | $(56,000.00)$ | $(665,000.00)$ |
| Less closing stock |  | $\underline{475,000.00}$ |
| Gross Profit | $1,140,000.00$ |  |
| Workings: | $21,000.00$ |  |
| Sales (190,000 X 6) | $56,000.00$ | 16,000 |
| Opening Stock (6000 X 3.50) <br> Closing Stock - Units (6,000 + 200,000 - 190,000) <br> (value 16,000 X 3.50) |  |  |

## QUESTION FOUR

## Mutiso Mwema

Profit and Loss Account for the year ended 31 December 1990

Sh.
Sales
$\begin{array}{lr}\text { Credit } \\ \text { Cash } \\ & \\ \text { Purchases } & 196,000.00 \\ \text { Closing stock } & \underline{(15,800.00)}\end{array}$
Closing stock
Less Expenses
Salary
Electricity bills
Motor expenses
General expenses
Insurance
Interest on loan
Depreciation - MV
Depreciation - Eq.
Rates
Bad debts
Accountancy fee
Net profit

## Mutiso Mwema

72,000.00
28,000.00
18,200.00
30,690.00
12,000.00
4,500.00
22,000.00
19,200.00
2,700.00
1,700.00
5,500.00
$(216,490.00)$ 293,710.00

Balance Sheet as at 31 December 1990
Sh.
Fixed Assets
Equipment
Motor vehicle

| $96,000.00$ |
| ---: |
| $66,000.00$ |
| $162,000.00$ |

Sh.
Sh.

| $(19,200.00)$ | $76,800.00$ |
| :--- | ---: |
| $(22,000.00)$ | $\underline{44,000.00}$ |
| $(41,200.00)$ | $120,800.00$ |

## Current Assets

| Stocks | $15,800.00$ |
| :--- | ---: |
| Debtors | $108,100.00$ |
| Prepayments | $4,000.00$ |
| Cash at bank | $181,200.00$ |
| Cash in hand | $\frac{3,010.00}{312,110.00}$ |

Current Liabilities

| Accrued expenses | $\underline{(16,700.00)}$ | $\underline{295,410.00}$ |
| :--- | ---: | ---: |
|  | $\underline{416,210.00}$ |  |
| Capital | $\underline{186,000.00}$ |  |
| Add: Net profit | $\underline{293,710.00}$ |  |
|  | $479,710.00$ |  |
| Less drawings | $\underline{(103,500.00)}$ |  |
|  | $376,210.00$ |  |
| Loan | $\underline{40,000.00}$ |  |
|  | $\underline{416,210.00}$ |  |

Capital


## QUESTION FIVE

## I)

(a) Comparability means that users are able to draw conclusions about the performance or financial position of a business by relating figures for a particular period to other relevant figures. Possible types of comparison are:
(i). comparison with figures for the same business for earlier periods
(ii). comparison with figures for other businesses for the same period
(iii). comparison with budgets or forecasts
(Two types required for full marks)
(b) Two from:
(i). by requiring the disclosure of accounting policies and the effect of changes in them
(ii). by reducing or eliminating the number of possible alternative treatments for similar items available to businesses
(iii). by requiring businesses to treat similar items in the same way within each period and from one period to the next, unless a change is required to
comply with accounting standards or to ensure that a more appropriate presentation of events or transactions is provided.
II) The use of historical cost accounting can mislead users when prices are rising in the following ways:
(i). Depreciation is based on the original cost of non-current assets and thus understates the true value obtained by the business from the use of these assets. The result is that profit is overstated.
(ii). Inventory is often valued at cost, using FIFO or average costs. If prices are rising, sales in current terms are matched with cost of sales in historical cost terms. Profit is again overstated.
(iii). Balance sheet values of assets may become seriously below their current value.
(iv). The combined effects of the above three factors mean that return on capital employed is overstated.
(v). Year on year comparison of results is likely to be misleading as figures will show an automatic increase as prices rise, when in real terms sales and profits may have risen far less, or even have fallen.

Any four points needed for full marks.

## MOCK PAPER 4

## QUESTION ONE

c) A bank reconciliation statement is a statement that explains the difference between balance at the bank as per cashbook and balance at bank as per the bank statement.

The functions are:
i) To update the cashbook with transactions that have gone through the bank e.g. bank charges.
ii) To check and correct any errors in the cashbook.
iii) To Detect and prevent any frauds that relate to the cashbook and bank transactions.
b)

Cashbook A

| 1995 | Sh. | 1995 | Sh. |
| :---: | :---: | :---: | :---: |
| Balance b/f | 200,000.00 | Suspense | 20,000.00 |
| Cashbook B | 60,000.00 | Incidental Charges | 400.00 |
| Cashbook B | 25,000.00 | Balance c/d | 268,400.00 |
| Interest earned Electricity bill | $\begin{aligned} & 2,000.00 \\ & 1,800.00 \\ & \hline \end{aligned}$ |  |  |
| overstated | 288,800.00 |  | $\underline{\underline{288,800.00}}$ |
| Cashbook B |  |  |  |
|  | Sh. |  | Sh. |
| 1995 |  | 1995 |  |
| Dividends received | 8,000.00 | Balance b/f | 90,000.00 |
| Balance c/d | 189,500.00 | Cashbook A | 60,000.00 |
|  |  | Suspense | 20,000.00 |
|  |  | Cashbook A | 25,000.00 |
|  |  | Incidental Charges | 1,000.00 |
|  |  | Bank Charges | 1,500.00 |
|  | 197,500.00 |  | 197,500.00 |

ii) Juhudi Ltd

Bank Reconciliation Statement as at 31 March 1995 - Cashbook A
Sh.
Balance at bank as per the cashbook
268,400.00
Add: Unpresented cheques
40,000.00
308,400.00
Less: Uncredited cheques
(200,000.00)
Balance at bank as per the bank statement 108,400.00

Juhudi Ltd
Bank Reconciliation Statement as at 31 March 1995 - Cashbook B
Sh.
Balance at bank as per the cashbook
(189,500.00)
Add: Unpresented cheques
500,000.00
310,500.00
Less: Uncredited cheques
(140,000.00)
Balance at bank as per the bank statement $\quad \underline{170,500.00}$

## QUESTION TWO



## Lorries Account

|  | Sh. |  | Sh. |
| :---: | :---: | :---: | :---: |
| Transfer from plant | $\underline{1,050,000.00}$ | Balance c/d | $\underline{1,050,000.00}$ |
|  | $\underline{1,050,000.00}$ |  | $\underline{1,050,000.00}$ |

## Provision for Depreciation - Lorries

|  | Sh. |  | Sh. |
| :---: | :---: | :--- | :--- |
| Transfer from plant | $\underline{200,000.00}$ | P \& L charge for year | $\underline{200,000.00}$ |
|  | $\underline{200,000.00}$ |  | $\underline{200,000.00}$ |

b) Uzee Ltd

Balance Sheet as on 31 December 2001

|  | Sh. |  | Sh. |
| ---: | :---: | :--- | ---: |
| Non Current Assets: Plant | $3,750,000.00$ | $(2,817,500.00)$ | $932,500.00$ |
| Lorry | $1,050,000.00$ | $(200,000.00)$ | $850,000.00$ |

c) Changes in the charges for depreciation has affected the profit as follows;

Plant reduced by sh. 303,000 from sh. 410,000 to sh. 107,000
Lorry increased by sh. 130,000 from sh. 70,000 to sh. 200,000 Net Increase sh $303,000-$ sh. $130,000=$ sh. 173,000 .

| Workings |  |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Workings |  | Year of | Amount to depreciate | Estimated | Depreciation | Years | Total |
| Plant |  | Purchase | Cost less scrap | useful life | per year | held | Depreciation |
| Plant 1 | 1 | 1993 | 180,000.00 | 20 | 9,000.00 | 9 | 81,000 Ra |
| Plant 2 | 2 | 1998 | 160,000.00 | 20 | 8,000.00 | 4 | 32,000.00 |
| Plant 3 | 3 | 1996 | 325,000.00 | 10 | 32,500.00 | 6 | 195,000.00 |
| Plant 4 | 4 | 1999 | 420,000.00 | 10 | 42,000.00 | 3 | 126,000.00 |
| Plant 5 | 5 | 1996 | 60,000.00 | 8 | 7,500.00 | 6 | 45,000.00 |
| Plant 6 | 6 | 2000 | 120,000.00 | 15 | 8,000.00 | 2 | 16,000.00 |
|  |  |  |  |  | 107,000.00 |  | $\underline{495,000.00}$ |
| Lorry |  | 2001 | 800,000.00 | 4 | 200,000.00 |  |  |

Total Depreciation for year

| Plant | $\underline{107,000.00}$ |
| :--- | ---: |
| Lorry | $\underline{200,000.00}$ |
| Previously charge | $\underline{480,000.00}$ |
| Overprovision. | $\underline{173,000.00}$ |

## QUESTION THREE

## Watambezi Sports Club

Bar Trading Profit and Loss Account for the year ended 31 October 1998

|  | Sh. | Sh. |
| :--- | ---: | :---: |
| Sales |  | $932,000.00$ |
| Less: Cost of sales | $254,000.00$ |  |
| Opening stock | $\underline{792,000.00}$ |  |
| Purchases | $1,046,000.00$ | $(\underline{329,000.00)}$ |
| Less:Closing stock |  | $\underline{(717,000.00)}$ |
| Profit to Income and Expenditure |  |  |

## Watambezi Sports Club <br> Income and Expenditure Account for the year ended 31 October 1998

|  | Sh. | Sh. |
| :--- | ---: | ---: |
| Income | $215,000.00$ |  |
| Bar Trading |  | $2,988,000.00$ |
| Subscriptions |  | $627,000.00$ |
| Dinner dance tickets |  | $158,000.00$ |
| Seminar rentals | $247,000.00$ |  |
| Investment income |  | $17,000.00$ |
| Profit on disposal |  | $4,252,000.00$ |
| Expenditure |  |  |
| Dinner dance | $350,000.00$ |  |
| Salaries and wages | $459,000.00$ |  |
| Other staff expenses | $129,000.00$ |  |
| Coach fees | $260,000.00$ |  |
| Life savers fees | $184,000.00$ |  |
| General expenses | $158,000.00$ |  |
| Repairs and maintenance | $296,000.00$ |  |
| Audit fee | $50,000.00$ | $(2,028,000.00)$ |
| Subscriptions written off | $27,000.00$ | $\underline{2,224,000.00}$ |
| Depreciation: Equipment | $81,000.00$ |  |
| Furniture and Fittings | $34,000.00$ |  |

Watambezi Sports Club
Balance Sheet as at 31 October 1998

|  | Sh. | Sh. | Sh. |
| :---: | :---: | :---: | :---: |
| Non Current Assets |  |  |  |
| Clubhouse | 3,185,000.00 |  | 3,185,000.00 |
| Equipment | 540,000.00 | (150,000.00) | 390,000.00 |
| Furniture and Fittings | 340,000.00 | (159,000.00) | 181,000.00 |
|  | 4,065,000.00 | (309,000.00) | 3,756,000.00 |
| Investments |  |  | 3,000,000.00 |


| Current Assets | $329,000.00$ |
| :--- | ---: |
| Bar Stocks | $324,000.00$ |
| Debtors Subscriptions | $29,000.00$ |
| Dinner dance | $14,000.00$ |
| Equipment | $\underline{2,082,000.00}$ |
| Bank | $2,778,000.00$ |

Current Liabilities
Creditors 234,000.00
Subscriptions 121,000.00
Accruals $\quad 163,000.00$
$(518,000.00)$$\frac{2,260,000.00}{\frac{9,016,000.00}{S h .}}$

## Workings:

Accumulated Fund

## Assets

| Clubhouse |  | $2,450,000.00$ |
| :--- | :---: | :---: |
| Equipment | $325,000.00$ |  |
| Depreciation - Equipment | $(95,000.00)$ | $230,000.00$ |
| Furniture \& Fittings | $340,000.00$ |  |
| Depreciation - F \& F | $\underline{(125,000.00)}$ | $215,000.00$ |
| Subscriptions in arrears |  | $185,000.00$ |
| Bar stock | $254,000.00$ |  |
| Investment | $2,550,000.00$ |  |
| Cash | $\underline{748,000.00}$ |  |
|  |  | $6,632,000.00$ |

## Liabilities:

Subscriptions prepaid 178,000.00
Salaries $\quad 23,000.00$
Creditors 168,000.00
Club extension fund $\quad \underline{250,000.00}$
(619,000.00)
$6,013,000.00$

## Subscriptions

|  | Sh. |  |  | Sh. |
| :--- | ---: | ---: | :--- | ---: |
| Balance b/d |  | $185,000.00$ | Balance b/d 97/98 | $124,000.00$ |
| Income and Expenditure (bal fig.) |  | $2,988,000.00$ | Balance b/d 98/99 | $54,000.00$ |
| Balance c/d 98/99 - b/f | $54,000.00$ | Receipts and payments | $2,765,000.00$ |  |
| Balance c/d 98/99 R \& P |  | $67,000.00$ | Subs written off | $27,000.00$ |
|  |  |  |  | Balance c/d 97/98 |

## Disposals of Equipment

|  | Sh. |  | Sh. |
| :--- | :---: | :--- | :---: |
| Equipment | $85,000.00$ | Depreciation | $26,000.00$ |
| Income and Expenditure | $17,000.00$ | Receipts and Payments | $62,000.00$ |
|  | $\underline{102,000.00}$ | Debtors | $\underline{14,000.00}$ |
|  |  | $\underline{102,000.00}$ |  |
|  |  |  |  |

Accruals

| Salaries and wages | $28,000.00$ |
| :--- | ---: |
| Audit fees | $50,000.00$ |
| Unpaid extension | $\underline{85,000.00}$ |
|  | $\underline{163,000.00}$ |

## QUESTION FOUR

Malimia Traders ${ }^{\text {" }}$
Trading and Profit and Loss Account for the year ended 31 October 1993

Sales
Less returns inwards

Less: cost of sales
Opening stock
Purchases
Carriage inwards
Less Returns out
Less Closing stock
Gross Profit
Add Other incomes
Discounts received
Rent income
Interest on overdue customers

Less: Expenses
Depreciation
Equipment
Buildings
Operating expenses
Insurance premium
Loan interest
Bad debts
Provision for doubtful debts
Discounts allowed
Rent and rates
Net Profit
Sh.
Sh. Sh.

$$
\begin{array}{r}
2,972,800.00 \\
\begin{array}{c}
(60,000.00) \\
\hline 2,912,800.00
\end{array} .
\end{array}
$$

| 389,000.00 |  |
| :---: | :---: |
| 2,493,300.00 |  |
| 2,882,300.00 |  |
| (985,000.00) | (1,897,300.00) |
|  | 1,015,500.00 |
|  | 64,800.00 |
|  | 190,000.00 |
|  | 11,900.00 |
|  | 1,282,200.00 |


| $372,500.00$ |  |
| ---: | ---: |
| $100,000.00$ |  |
| $476,100.00$ |  |
| $24,800.00$ |  |
| $18,500.00$ |  |
| $14,000.00$ |  |
| $14,200.00$ |  |
| $41,300.00$ |  |
| $50,000.00$ | $\underline{(1,111,400.00)}$ |
|  | $\underline{170,800.00}$ |

## Balance Sheet

|  | Cost | Accumulated Depreciation | Net Book Value |
| :---: | :---: | :---: | :---: |
| Buildings | 2,000,000.00 | $(100,000.00)$ | 1,900,000.00 |
| Equipment | 1,490,000.00 | (372,500.00) | 1,117,500.00 |
|  | 3,490,000.00 | (472,500.00) | 3,017,500.00 |
| Current Assets |  |  |  |
| Stocks |  | 985,000.00 |  |
| Debtors | 663,200.00 |  |  |
| Provision | $(14,200.00)$ | 649,000.00 |  |
| Prepaid insurance |  | 4,000.00 |  |
| Interest due on customers a/c |  | 5,000.00 |  |
| Cash at bank |  | 144,000.00 |  |
|  |  | 1,787,000.00 |  |
| Current Liabilities |  |  |  |
| Creditors | 523,000.00 |  |  |
| Accruals (note) | 117,500.00 |  |  |
| Bank loan | 350,000.00 | (990,500.00) | 796,500.00 |
|  |  |  | 3,814,000.00 |
| Capital <br> Net Profit |  |  | 3,753,200.00 |
|  |  |  | 170,800.00 |
|  |  |  | 3,924,000.00 |
| Less: drawings |  |  | (110,000.00) |
|  |  |  | 3,814,000.00 |

## Workings

Statement of Affairs

| Assets | $19,000.00$ |  |
| :--- | ---: | ---: |
| Prepaid insurance | $184,600.00$ |  |
| Cash at bank | $585,600.00$ |  |
| Trade Debtors | $9,000.00$ |  |
| Interest due on customers |  | $389,000.00$ |
| Stock |  | $\underline{2,240,000.00}$ |
| Equipment |  | $4,427,000.00$ |
| Building |  |  |
| Liabilities | $100,000.00$ |  |
| Bank loan | $5,000.00$ |  |
| Interest due on bank loan | $475,000.00$ |  |
| Trade creditors | $34,000.00$ |  |
| Other Liabilities | $\underline{60,000.00}$ | $\underline{(674,000.00)}$ |
| Prepaid rent |  | $\underline{3,753,200.00}$ |

Sales Ledger Control A/c

|  | Sh. |  | Sh. |
| :--- | ---: | :--- | ---: |
| Balance b/f | $585,600.00$ | Bank | $1,906,900.00$ |
| Sales | $2,099,800.00$ | Bad debts | $14,000.00$ |
|  |  | Returns inwards | $60,000.00$ |
|  |  | Discount allowed | $41,300.00$ |
|  | $\underline{2,685,400.00}$ | Balance c/d | $\underline{663,200.00}$ |
|  |  | $\underline{2,685,400.00}$ |  |

Purchases Ledger Control A/c

|  | Sh. |  | Sh. |
| :--- | ---: | :--- | ---: |
| Bank | $2,256,500.00$ | Balance b/f | $475,000.00$ |
| Returns out | $50,000.00$ | Purchases | $2,419,300.00$ |
| Discounts received | $64,800.00$ |  |  |
| Bal c/d | $\underline{523,000.00}$ |  | $\underline{2,894,300.00}$ |
|  |  |  |  |

Insurance Premium a/c

|  | Sh. |  | Sh. |
| :--- | ---: | :--- | ---: |
| Balance b/f | $19,000.00$ | Profit \& Loss (bal fig) | $24,800.00$ |
| Cashbook | $\underline{9,800.00}$ | Balance c/d | $\underline{4,000.00}$ |
|  | $\underline{28,800.00}$ |  | $\underline{28,800.00}$ |

Accruals

| Rent and rates | $50,000.00$ |
| :--- | ---: |
| Interest on o/d | $17,500.00$ |
| Prepaid rent | $50,000.00$ |
|  | $\underline{117,500.00}$ |

## QUESTION FIVE

ii) Concepts/ conventions/ principles

Broad basic assumptions that underlie the periodic financial accounts of business enterprises.
Examples of concepts include going concern, prudence and Matching.
iii) Bases

The methods that have been developed for expressing or applying fundamental accounting concepts to financial transactions and items. Examples include:

- Depreciation of Non Current Assets (e.g. by straight line or reducing balance method )
- Treatment and amortization of intangible assets (patents and trade marks)
- Stocks and work in progress FIFO, LIFO and AVCO
iv) Policies

Accounting policies are the specific accounting bases judged by business enterprises to be the most appropriate to their circumstances and adopted by them for the purpose of preparing their financial accounts.

1. The Going Concern Concept: the enterprise will continue in operational existence forthe foreseeable future. This means that the profit and loss account and the balance sheet assume no intention or necessity to liquidate or curtail significantly the scale of operation.
2. The Accruals Concept (Matching): revenue and costs are accrued (that is, recognized asthey are earned or incurred, not as money is received or paid ) matched with one another so far as their relationship can be established or justifiably assumed, dealt with in the profit and loss account of the period to which they relate; but if the accruals concept conflicts with the prudence concept then the prudence concept prevails.
3. The Consistency Concept: there is consistency of accounting treatment of like itemswithin each accounting period and from one period to the next.
4. The Prudence (or Conservatism) Concept: Revenue and Profits are not anticipated butare recognized by inclusion in the profit and loss account only when realized in the from of either cash or of other assets the ultimate cash realization of which can be assessed with reasonable certainty; provision is made for all liabilities (expenses and losses) whether the amount of these is known with certainty or is best estimate in the light of the information available.
5. Materiality:Information is material if it"s omission or misstatement could influence theeconomic decisions of users taken on the basis of the financial statements. Materiality depends on the size of the item or error judged in the particular circumstances of its omission or misstatement.
6. Substance over form: The principle that transactions and other events are accounted forand presented in accordance with their substance and economic reality and not merely their legal form e.g. a non current assets on Hire purchase although is not legally owned by the enterprise until it .fully paid for, it is reflected in the accounts as an assets and depreciation provided for in the normal accounting.
7. The business entity: Accountants regard a business as a separate entity, distinct from itsowners or managers. When preparing accounts therefore the business is presented as having it"s own assets and incurring liabilities.
8. Money Measurement: Accounts will only deal with those items to which monetary valuecan be attributed. Example in the balance sheet of business, monetary values can be attributed to such assets such as machinery and inventories. This concept introduces limitations to the subject matter of accounts.
9. Historical Cost: this is a basic principle of accounting that states that resources arenormally stated in accounts at historical cost, i.e. at the amount which the business paid to acquire them. Historical cost means that transactions are recorded at the cost when they occurred.
10. Objectivity: This means that accountants must be free from bias. An accountant mustshow objectivity in his work. He should try to strip his answers of any personal opinion or prejudice and should be as precise and detailed as the situation warrants.
11. Realization: Revenue and profits are recognized when realized. The concept states thatrevenue and profits are not anticipated but are recognized by inclusion in the income statement only when realized in the form of either cash or of other assets the ultimate cash realization of which can be assessed with reasonable certainty.
12. Duality: Every transaction has twofold effect in the accounts and is the basis of doubleentry bookkeeping.

## MOCK FIVE

## QUESTION ONE

1 (a) Capital as at 1 February 2000

|  | Sh |  | Sh |
| :---: | :---: | :---: | :---: |
| Assets |  |  |  |
| Shop equipment |  |  | 7,900 |
| Inventory |  |  | 146,400 |
| Accounts receivable |  |  | 14,400 |
| Rent in advance |  |  | 1,000 |
| Cash in hand |  |  | 800 |
|  |  |  | 170,500 |
| Less: Liabilities |  |  |  |
| Loan - Draco | 24,000 |  |  |
| Accounts payable | 12,100 |  |  |
| Accrued expenses | 2,300 |  |  |
| Bank overdraft | _2,600 |  |  |
|  |  |  | 41,000 |
| Opening capital |  |  | 129,500 |
| Cygnus |  |  |  |
| Income statement for the year ended 31 January 2001 |  |  |  |
|  | Reference to workings | Sh | Sh |
| Sales revenue | 2 |  | 202,400 |
| Less: Cost of sales |  |  |  |
| Opening inventory |  | 146,400 |  |
| Purchases | 1 | 83,500 |  |
|  |  | 229,900 |  |
| Less: Closing inventory |  | 128,700 |  |
|  |  |  | 101,200 |
|  |  |  | 101,200 |
| Gross profit |  |  |  |
| Less: Expenses |  |  |  |
| Rent (8,250 + 1,000-1,500) |  | 7,750 |  |
| Sundry expenses (18,600-2,100 $+3,300$ ) |  | 19,800 |  |
| Depreciation | 3 | 1,490 |  |
| Profit on sale of equipment (300-200) |  | (100) |  |
| Interest on loan $\quad \underline{2,300}$ |  |  |  |
|  |  |  | 31,240 |
| Net profit |  |  | 69,960 |

## Cygnus

Balance sheet as at 31 January 2001

|  | Sh | Sh |
| :---: | :---: | :---: |
| Non - current assets |  |  |
| Shop equipment - cost (W3) | 15,800 |  |
| - accumulated depreciation |  |  |
| $(6,900-600+1,490)$ (W3) | 7,790 |  |
|  |  | 8,010 |
| Current assets |  |  |
| Inventory | 128,700 |  |
| Accounts receivable | 15,700 |  |
| Rent in advance | 1,500 |  |
| Cash at bank | 4,850 |  |
| Cash in hand | 900 |  |
|  |  | 151,650 |
|  |  | 159,660 |
| Capital |  |  |
| As at 1 February 2000 | 129,500 |  |
| Profit for year to date | 69,960 |  |
|  | 199,460 |  |
| Less: Drawings (W5) | _69,400 |  |
|  |  | 130,060 |
| Non-current liabilities |  |  |
| Loan - Draco |  | 12,000 |
| Current liabilities |  |  |
| Accounts payable | 14,200 |  |
| Accrued expenses (3,300 + 100) | -3,400 |  |
|  |  | 17,600 |
|  |  | 159,660 |
| Workings |  |  |
| W1 Calculation of purchases |  |  |

Purchases Total Account

|  | $\mathbf{S h}$ |  | Sh. |
| :--- | ---: | :--- | ---: |
| Cash payments for purchases | 81,400 | Opening balance | 12,100 |
| Closing balance | $\underline{14,200}$ | Purchases (balancing figure) | $\underline{83,500}$ |
|  | $\underline{95,600}$ | $\underline{95,600}$ |  |

W2 Calculation of sales revenue
Sales prices are fixed by doubling cost - sales revenue is therefore cost of sales Sh.101,200 x $2=$ 202,400

W3 Non-current assets and depreciation

|  | Cost | Accumulated depreciation |
| :---: | :---: | :---: |
|  | Sh. | Sh. |
| As at 1 February 2000 | 14,800 | 6,900 |
| Less: Items sold | (800) | (600) |
|  | 14,000 | 6,300 |
| Additions | 1,800 |  |
|  | 15,800 |  |
| Depreciation for the year |  |  |
| Sh.14,000 at 10\% |  | 1,400 |
| Sh. 1,800 at $10 \%$ for six months | - | 90 |
| As at 31 January 2001 | 15,800 | 7,790 |

W4 Calculation of cash received from sales revenue

| Sales total account |  |  |  |
| :--- | ---: | :--- | ---: |
|  | Sh. | Sh. |  |
| Opening balance | 14,400 | Cash for sales (balancing figure) | 201,100 |
| Sales (W2) | $\underline{202,400}$ | Closing balance | $\underline{15,700}$ |
|  | $\underline{216,800}$ | $\underline{216,800}$ |  |

W5 Calculation of drawings

| Cash summary |  |  | $\mathbf{S h .}$ |
| :--- | ---: | :--- | ---: |
|  | $\mathbf{S h}$. |  | 131,600 |
| Opening balance | 800 | Cash banked | 69,400 |
| Cash from customers | 201,100 |  | Drawings (balancing |
|  |  | figure) |  |
|  | $\underline{201,900}$ |  | $\underline{900}$ |
|  | Closing balance | $\underline{201,900}$ |  |

## QUESTION TWO

(a)

## Capital accounts

| Motor vehicles | Orion <br> Sh. "000 | Pegasus Sh."000 | Balance <br> Goodwill Revaluation | Orion <br> Sh. "000 | Pegasus Sh."000 |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | 18 | 16 |  | 1,300 | 800 |
|  |  |  |  | 200 | 180 |
| Balances to new firm | 1,512 | 964 |  | 30 |  |
|  | 1,530 | $\underline{980}$ |  | 1,530 | $\underline{980}$ |


| Orion and Pegasus <br> Balance sheet as at 1 January 2001 |  |  |
| :---: | :---: | :---: |
|  | Sh. ${ }^{\text {0 }} 000$ | Sh. ${ }^{1000}$ |
| Non-current assets (W1) |  | 1,366 |
| Current assets |  |  |
| Inventory | 820 |  |
| Accounts receivable | 540 |  |
| Prepayments | 70 |  |
|  |  | 1,430 |
|  |  | $\underline{2,796}$ |
| Capital accounts |  |  |
| Orion (1,512-228 (W2)) | 1,284 |  |
| Pegasus (964-152 (W2)) | 812 |  |
| Current liabilities |  | 2,096 |
| Accounts payable | 590 |  |
| Accruals | 50 |  |
| Bank overdraft (180-120) | -60 |  |
|  |  | $\frac{700}{2,796}$ |

## WORKINGS

W1 Non current assets

|  | Orion <br> Sh."000 | Pegasus <br> Sh."000 |
| :--- | ---: | ---: |
| Original balances | 780 | 590 |
| Revaluation of land | 30 |  |
| Motor cars taken over | $\underline{(18)}$ | $\underline{(16)}$ |
|  | $\underline{792}$ | $\underline{574}$ |

W2 Goodwill

Sh."000
Introduced into sole trader accounts
Orion
200
Pegasus
$\underline{180}$
$\underline{380}$
Written off in partnership accounts
Orion 60\%
228
Pegasus 40\% $\underline{152}$ $\underline{380}$
(c)

Asset revaluations and a goodwill adjustment are necessary when partnership personnel change or there is a change in profit-sharing ratios in order to reflect the interests of the partners fairly. If a partner gives up profit share, he or she is also giving up a share in unrecorded goodwill or unrecorded increase in value of partnership assets. By crediting the partner"s accounts in their old profit sharing ratios with their shares in goodwill or asset revaluations, they are given the
value that has accrued to them up to the date of the change. New partners entering the partnership, or partners with an increased profit share, will participate in their profit sharing ratio in the growth in value of the assets since their entry or since the date of the change in profit sharing ratios.

## QUESTION THREE

(a)
$\left.\begin{array}{lll} & \begin{array}{c}\text { Year ended } \mathbf{3 1} \text { March } \\ \mathbf{1 9 9 9}\end{array} & \mathbf{2 0 0 0} \\ \text { (i) Gross profit as percentage of sales } \\ 600 / 1,800 \times 100 & & \\ 700 / 2,500 \times 100 & 33 \cdot 3 \%\end{array}\right)$
(iv) Current ratio

| $700: 518$ | $1 \cdot 35: 1$ |  |
| :--- | :--- | :--- |
| $1,230: 860$ |  | $1 \cdot 43: 1$ |

(v) Quick ratio

500:518
$0 \cdot 96: 1$
$870: 860$
$1 \cdot 01: 1$
(vi) Inventory turnover (days)
$200 / 1,200 \times 365 \quad 60 \cdot 8$ days
360/1,800 x 365
$73 \cdot 0$ days
(vii) Trade receivables - sales (days)
$\begin{array}{ll}400 / 1,440 \times 365 & 101 \cdot 4 \text { days } \\ 750 / 2,000 \times 365 & 136 \cdot 9 \text { days }\end{array}$
(viii) Trade payables - purchases (days)
$210 / 1,220 \times 365 \quad 62 \cdot 8$ days
380/1,960 x 365
$70 \cdot 8$ days
(b) Comments on ratios
(i). Gross profit percentage on sales has declined from $33 \cdot 3 \%$ to $28 \cdot 0 \%$, a drop of $16 \%$. This is possibly due to a decision to lower prices to increase sales revenue, which has risen by $38 \cdot 9 \%$. A drop in the gross profit percentage is an indicator of possible error or fraud if an explanation such as a lowering of prices cannot be found.
(ii). Net profit to sales is down from $13 \cdot 3 \%$ to $10 \%$, down about $25 \%$. The net profit percentage has fallen more than the gross profit percentage, probably because distribution costs have risen sharply.
(iii). Return on capital employed has declined from $12 \cdot 1 \%$ to $9 \cdot 4 \%$, a drop of about $22 \%$. This is a reflection of the decline in profitability shown by ratid (ii) above.
(iv). And
(v). The two ratios measuring liquidity have changed little between the two periods. The levels are satisfactory at both dates.
(vi). The inventory turnover ratio has increased because the inventory level has risen faster than the increases in cost of sales and sales. The higher inventory could be a reflection of slowing demand for the company"s goods towards the end of the period and/or slackness in the company"s inventory control procedures.
(vii). The accounts receivable days have increased considerably from 101.4 days, a high level, to the even higher level of 136.9 days. The increase suggests slackness in the company"s credit control procedures.
(viii). There has been a relatively small increase in the number of days" purchases in trade payables. The increase is perhaps caused by pressure on the company"s liquid resources as a result of the increased inventory and trade receivables.

## QUESTION FOUR

(a) Briefly: To keep detail out of cashbook

To reduce postings to expense accounts
To enable petty cash to be kept by someone other than the main cashier.
(b)

Petty Cash Book

## Receipts

| Total | Post and | Travel | Ledger |
| :---: | :---: | :--- | :--- |
|  | Stationery | expenses | accounts |

1.13
(1) Balance b/d
23.87 (2) Cash
(4) Postages
8.50
8.50
(9) Courtney Bishop
2.35
8.5
(11) Bus fares
1.72
2.35
(17) Envelopes
0.70
0.70
0.68 (23) Telephone reimbursed (26)

| 10.00 |  | 10.00 |  |
| :--- | :--- | :--- | :--- |
| 23.27 | 9.20 | 11.72 | 2.35 |

$\underline{\underline{25.68}}$
(30) Balance c/d
$\underline{2.41}$
2.41 (1) Balance b/d
22.59 (1) Cash
(c).

| Post and Stationery |  |  |
| :--- | ---: | ---: |
| (30) Petty cash | $9.20 \mid$ |  |
| Travel Expenses |  |  |
| (30) Petty cash | 11.72 |  |
| Courtney Bishop |  |  |
| (9) Petty cash | 2.35 |  |

## QUESTION FIVE

## a) The limitation of Financial Ratios

## i) Historical

Ratios computed are usually computed using historical information. As such they cannot be used to forecast on what will happen in the future as they are usually used.
ii) Non qualitative

Ratios cannot be calculated for qualitative aspects e.g. the performance of a company in the social responsibility front or even the competency of a manager at his work. As such they are limited to the things they can discuss about a business.
iii) Monopolies

One of the uses of financial ratios is so that they can be compared with other firms in the industry that a firm is operating in. This however is not possible for companies which are monopolies since there are no firms to compare with e.g. KENGEN the electricity provider in Kenya
iv) Different Accounting Policies

Different firms use different accounting policies e.g. in depreciation costing their closing stock etc.,
This may be a hindrance in comparing the accounting policies of different companies as the ratios may be differently computed.
v) Companies falling under different Industries

These companies are hard to classify for purposes of ratio analysis in that it"s not possible to know under which industry to place them for comparison purposes.
An example would be Unilever Kenya who deal with very many goods and as such it may be hard to put them into a certain industry.

## b) Characteristics of a Partnership

## i) Voluntary Association

A partnership is usually a business of between 2 to 20 members who have gathered voluntarily with a common goal of running a business with a view of making a profit.

## ii) Based on a contract

When persons are interested in forming a partnership they have to make a contract or come to an agreement. The partnership agreement will be the one to resolve any issues which may arise e.g. the ratio of sharing profit, any salaries to be paid, admission of new partners etc,
iii) Limited life

Partnerships have a limited life, they become dissolved if certain events happen e.g. death of a partner, completion of the purpose they were formed for, bankruptcy etc,
iv) Mutual agency

In a partnership all the members/partners can act for the partnership in any contract and as such they are agents of each other.
If one partner entered into a contract on behalf of the partnership, the partnership and all the other members would be bound by his action.

## v) Unlimited liability

Partners in a partnership have unlimited liability, this means that if the partnership is unable to pay its debts the partners will be liable for those debts personally. As such their goods may be attached to repay those debts.

## Part IV: Revision Questions and Answers

## Questions

## REVISION PAPER ONE

## QUESTION ONE

Kenya Caps Limited issued additional 100,000 ordinary shares and $50,000,8 \%$ preference shares on the following terms:

|  | Payable per share |  |
| :--- | :---: | :---: |
| Ordinary | Preference |  |
| Application | Sh. | Sh |
| Allotment (including premium) | 2.50 | 2.50 |
| First call 30 days after allotment | 3.50 | 2.00 |
| Second and final call (60 days) | 3.00 | 2.50 |
|  | 2.00 | 2.50 |

The par values were Sh. 10 and Sh. 9 for the ordinary and preference shares respectively. By 1 August 1993, applications had been received for 200,000 ordinary shares and 40,000 preference shares. The directors rejected the application for 80,000 ordinary shares and refunded the monies on 15 August 1993, and the remainder allotted five shares for every six shares applied for. Surplus application monies were carried forward to allotment.

All allotment took place on 20 August 1993 and the due amounts were received by 31 August 1993. The first and second calls were received by the due dates except for 3,000 ordinary shares which the directors declared forfeited on 20 November 1993. All the forfeited shares were reissued as fully paid to another shareholder on 30 November 1993 for Sh. 9 per share.

Assume that the number of shares outstanding prior to this additional issue amounted to:

- Ordinary - 300,000 shares of Sh. 10 par

$$
-50,0007 \% \text { preference shares of Sh. } 7 \text { par }
$$

All these shares had been issued at par.

## Required:

(a) Journal entries including cash necessary to record the share transactions.
(b) Prepare the share capital section of the Balance Sheet as at 31 December 1993.
(c) What is the importance of issuing bonus shares
(Total: 22 marks)

## QUESTION TWO

The Chief Accountant of KK Ltd. has extracted the following trial balance as at 31 October 1998:

|  | Sh. 000' | Sh. 000' |
| :---: | :---: | :---: |
| Authorised and issued capital (shares of Sh. 20 each fully paid) |  | 30,000. |
| Share premium |  | , 50 |
| 10\% debentures |  | 3,500 |
| General reserve |  | 2,000 |
| Profit and loss account 1 November 1997 |  | 2,850 |
| Motor vehicles at cost | 3,500 |  |
| Provision for depreciation |  | 265 |
| Freehold property | 44,500 |  |
| Trade debtors | 1,375 |  |
| Trade creditors |  | 460 |
| Purchases and sales | 95,650 | 127,450 |
| Stock in hand 1 November 1997 | 3,478 |  |
| Furniture and fittings at cost | 1,540 |  |
| Provision for depreciation |  | 138 |
| Goodwill | 500 |  |
| Rent receivable |  | 385 |
| Salaries and wages | 2,285 |  |
| General expenses | 358 |  |
| Vehicles running expenses | 2,470 |  |
| Bad debts | 124 |  |
| Telephone and postage | 568 |  |
| Water and electricity | 269 |  |
| Rates and insurance | 289 |  |
| Cash at bank | 10,492 |  |
|  | 167398 | 167,398 |

## Notes:

1. Credit sales amounting to Sh. 165,000 were made on 31 October 1998 but no entries were made in the books.
2. Returns outwards amounting to Sh. 128,000 were dispatched on 31 October 1998 but no entries were made in the books.
3. Closing stock was valued at Sh.4, 398,000.
4. Accrued salaries and telephone bills amounted to Sh. 134,000 and Sh.55, 000 respectively.
5. Rent for the month of October 1998 amounting to $\mathrm{Sh} .35,000$ had not been received from the tenant.
6. Provision for depreciation on furniture and fittings and the motor vehicles are $10 \%$ and $20 \%$ on cost respectively.
7. Provision for bad and doubtful debts of $5 \%$ on trade debtors should be made.
8. Corporation tax should be provided at $35 \%$ of the net profit before tax.
9. The directors propose a dividend of $15 \%$ on issued share capital and a transfer of Sh.2, 500,000 to the general reserve.
10. The debenture interest has not yet been paid.

## Required:

(a) Trading, profit and loss account for the year ended 31 October 1998. (13 marks)
(b) Balance sheet as at 31 October

## QUESTION THREE

According to the cash hook of Gaitani Ltd. the company has a credit balance at the hank of Sh. 190.000 on 30 June 1994, but this is NOT borne out by the Bank Statement of the same date. An investigation into the difference yields the following information.

1 A standing order for a charitable subscription of Sh.20, 000 had been paid by the hank on 29 June but no entry had been made in the cash hook.
2. A cheque paid for advertising on 10 little for Sh. 89,500 had been entered into the cash hook as Sh. 98,500 .
3 Cheques for S11.5 18,500 sent to creditors on 30 June were not paid by the hank until 8 July.
4. Cheques received front customers amounting to sh. 840.000 were paid into the bank on 30 June but were not credited by the hank until 5 July.
5. On 20 Julie a cheque for h. 57,000 was received from a customer in settlement of an invoice for Sh. 60.000 . An entry of Sh. 60.000 had been made in the cash hook.

## Required:

(a) Prepare a statement reconciling the cash hook balance with the hank statement. (12 marks)
(b) Explain how a company may have reduced its hank balance during an accounting period but still have earned a profit fur that same period.
(6 marks)
(Total: 18 marks)

## QUESTION FOUR

James Mbuvi started a taxi business in Nairobi in March 1990 under the firm name Mbuvi Taxis. The firm had two vehicles KA and KB which had been purchased for Sh. 560,000 and Sh. 720,000 respectively earlier in the year.
In February 1992 vehicle KB was involved in an accident and was written off. The insurance company paid the firm Sh. 160,000 for the vehicle. In the same year the firm purchased two vehicles, KC and KD for Sh. 800,000 each.
In November 1993' vehicle KC was sold for Sh. 716,000 . In January 1994 vehicle KE was purchased for Sh. 840,000 . In March 1994 another vehicle KF was purchased for Sh.960.000.

The firm's policy is to depreciate vehicles at the rate of 25 per cent on cost on vehicles on hand at the end of the year irrespective of the date of purchase. Depreciation is not provided for vehicles disposed of during the year. The firm's year ends on 31 December.

## Required:

(a) Calculate the amount of depreciation charged in the profit and loss account for each of the five
years. (7 marks)
(b) Prepare the motor vehicle account (at cost).
(8 marks)
(c) Calculate the profit or loss on disposal of each of the vehicles disposed of by the company.
(5 marks)
(Total: 20 marks)

## QUESTION FIVE

With reference to International Accounting Standards explain the following:
(a) Fundamental accounting concepts
(12 marks)
(b) Accounting bases
(4 marks)
(c) Accounting policies

## REVISION PAPER TWO

## QUESTION ONE

The following trial balance was extracted from the books of Hiza Ltd. as on 30 September 1995:

|  | Sh. `000' & Sh. `000' |  |
| :--- | ---: | ---: |
| Share capital, authorized and issued 3,125,000 |  | 62,500 |
| Ordinary shares of Sh. 20 each |  | 1,700 |
| Directors' current accounts |  | 975 |
| - Ombima | 7,200 |  |
| - Mwangi | 50,000 |  |
| Motor vehicles (cost Sh. 12 million) | 18,400 |  |
| Freehold properties, at cost | 228,440 |  |
| Profit and loss account | 296,000 |  |
| Balance at 1 October 1994 | 26,875 |  |
| Purchases |  | 12,500 |
| Sales |  | 625 |
| Stock, 1 October 1994 | 7,500 |  |
| Special loan from bank at 5\% p. a. | 1,175 |  |
| Loan interest accrued at 30 September 1994 |  |  |
| Goodwill | 625 | 350 |
| Bad debts | 33,900 | 23,275 |
| Provision for bad debts 30 September 1994 | 1,930 |  |
| Rent receivable | 10,825 |  |
| Trade debtors and creditors | 5,020 |  |
| Motor vehicle running expenses | 42,935 |  |
| General expenses | $-1,150$ | $\boxed{416,950}$ |
| Balance at bank | $\underline{416,950}$ |  |
| Salaries and wages |  |  |

## You are given the following information:

1. Stock in trade, 30 September 1995 was Sh.28, 875,000.
2. The provisions for bad debts is to be increased to Sh. 750,000 .
3. Salaries and .wages outstanding at 30 September 1995 is Sh.500,000.
4. Rates and insurance paid in advance at 30 September 1995 is Sh. 155,000.
5. The item 'rent receivable Sh. 625,000 includes Sh. 125,000 in respect of the period from 1 October 1995 to 31 December 1995.
6. Provision is to be W de for depreciation of motor vehicles at the rate of 20 per cent per annum on cost.
7. During the year to 30 September 1995, Ombima, one of the directors took goods (cost Sh. 437,500 ) out of business stock for his own use. No entry for this transaction has been made in the books.

## Required:

(a) Trading and Profit and Loss Account for the year to 30 September $1995 . \quad$ (12 marks)
(b) Balance Sheet as at that date.

## QUESTION TWO

Manga Munene is the proprietor of a retail business, which has two main departments, which sell hardware and electrical goods, respectively. He had previously prepared his annual accounts in such a way that the relative profitability of the two departments was not ascertainable, but now he wishes to attempt to identify the profit attributable to each department in order that he may pay a bonus to the more successful of the departmental managers. At 30 September 1994, the balances in the books of the business were as follows:

|  | Sh. | Sh. |
| :--- | ---: | ---: |
| Capital |  | $8,520,000$ |
| Sales - Hardware | $7,080,000$ |  |
| $\quad$ Electrical |  | $3,540,000$ |
| Purchases - Hardware | $2,400,000$ |  |
| $\quad$ Electrical | $1,200,000$ |  |
| Stocks at 1 October 1993 - Hardware | 278,400 |  |
| $\quad$ Electrical | 256,320 |  |
| Salaries and Wages - Hardware | $2,467,200$ |  |
| $\quad$ Electrical | $1,852,800$ |  |
| Advertising | 73,800 |  |
| Discounts allowed - Hardware | 48,000 | 638,280 |
| $\quad$ Electrical | 24,000 |  |
| Drawings | 360,000 |  |
| Buildings (cost) | $5,160,000$ |  |
| Shop fittings and equipment - Hardware | $2,160,000$ |  |
| $\quad$ - Electrical | 840,000 |  |
| (At cost less depreciation) | $1,224,000$ |  |
| Debtors and creditors | 672,000 |  |
| Bank | 189,600 |  |
| Rent and rates | 105,000 | $19,778,280$ |
| Canteen charges | 105,600 |  |
| Electricity | 112,800 | 248,760 |
| Insurance on stock | $2,778,280$ |  |

## Notes:

|  | 1. At 30 September 1994 the <br> following amounts were owing: |
| :---: | :--- |
| Wages - Hardware - | Sh. |
| Electrical Electrical | 30,000 |
| expenses | 20,400 |
|  | 2,400 |

2. The general administrative expenses and the rent and rates included prepayments of Sh.3, 960 and Sh.6, 400 respectively.
3. Stocks at 30 September 1994 were:

| Hardware | Sh. |
| :--- | ---: |
| Electrical | 336,000 |
|  | 294,000 |

4. Depreciation is to he provided on shop fittings and equipment at $10 \%$ of the written down value.
5. The managers of the hardware and electrical departments are to he paid a commission of $5 \%$ of the net profit (prior to the commission payment) of the respective departments.
6. In apportioning the various expenses between the two departments due regard is to he taken of the following information:

|  | Hardware | Electrical |
| :--- | :---: | :---: |
| Number of workers | 9 | 6 |
| Average stock levels | Sh.300,000 | Sh.264, 000 |
| Floor area (Sq.meters) | 4,000 | 2,000 |

The general administrative expenses are primarily incurred in relation to the processing of purchases and sales invoices.

## Required:

(a) A schedule showing the basis oil which you have apportioned the various expenses between the two departments.
(b) The departmental and combined Trading and Profit and Loss Account for the year ended 30 September $1994 . \quad$ ( 15 marks )
(c) Balance Sheet at 30 September 1994.
(Total: 25 marks)

## QUESTION THREE

The treasurer of Kay Club and Ray Society has prepared the following receipts and payments account for the year ended 31 December 1994:

| Sh. |  |  | Sh. |
| :---: | :---: | :---: | :---: |
| Receipts |  | Payments: |  |
| Opening balance | 880,000 | Purchase of Amplifier (bought 1 July 1994) | 350,000 |
| Subscriptions (see note 1) |  | Kay Club: |  |
| Kay Club | 1,205,000 | Musician fees | 450,000 |
| Ray Society | 845,000 | Coaching fees | 410,000 |
| Annual Dinner - Ticket sales | 170,000 | Hall rent | 165,000 |
| Sale of mobile huts | 335,000 | Rates for the year to 31 December 1994 | 400,000 |
| Kay Club festivals - admissions | 470,000 | Decorating | 55,000 |
|  |  | Cleaning | 80,000 |
| Sales |  | Annual Ray expedition | 660,000 |
| Clothes | 1,050,000 | Annual dinner - hotel \& catering | 205,000 |
| Refreshments |  | Kay Club festival |  |
| Purchases | 4,150,000 | Prizes | 85,000 |
|  |  | Adjudicator"s fees | 45,000 |
|  |  | Clothes | 900,000 |
|  |  | Refreshments | 3,500,000 |
|  |  | Closing balance | 1,800,000 |
|  | 9,105,000 |  | 9,105,000 |

Note. It is the policy of the Society NOT to take into account subscriptions in arrear until theyare paid.

1) The mobile hut which was sold during 1994 had been valued at Sh. 400,000 on 31 December 1993, and was used for the society's activities until sold on 30 June 1994.
2) Immediately after the sale of the mobile hut, the Society rented a new hall at Sh.165,000 per annum.
3) The above receipts and payments account is a summary of the society's bank account for the year ended 31 December 1994; the opening and closing balances shown above were the balances shown in the bank statements on 31 December 1993 and 1994 respectively.
4) All cash is banked immediately and all payments are made by cheque.
5) A cheque for Sh.100,000 drawn by the society on 28 December 1994 for stationery was not paid by the bank until 4 January 1995.
6) The Society's assets and liabilities at 31 December 1993 and 1994, in addition to those mentioned earlier, were as follows:

19941993
Stocks for goods for resale at cost:

| Clothes | 650,000 | 550,000 |
| :--- | ---: | ---: |
| Refreshments | 155,000 | 300,000 |
| Sundry creditors Annual dinner - catering |  | 35,000 |
| Purchases- Clothes | 300,000 | 200,000 |
| Refreshments | 150,000 | 250,000 |

It is proposed to provide for depreciation on the amplifier at the rate of $20 \%$ per annum on cost, prorata to time.

## Required:

a) The Society's Income and Expenditure Account for the year ended 31 December 1994, and balance sheet as at that date. (Comparative figures are not required).
(18 marks)
b) Outline the advantages of income and expenditure accounts as compared with receipts and payments accounts.

## QUESTION FOUR

(a) What is the purpose of preparing a bank reconciliation statement?
(b) The following is the bank statement of Kakamega Retail Traders for the month of October 1996:

| Date1996 | Particulars | Debit | Credit | Balance |
| ---: | :--- | ---: | ---: | ---: |
|  |  | Sh. | Sh. | Sh. |
| October 1 | Balance b/d |  |  | 365,875 |
| 2 | Cheque no. 63 | 31,000 |  | 334,875 |
| 2 | Cheque no. 67 | 3,548 |  | 400,327 |
| 2 | Cheque no. 65 | 13,000 |  | 331,327 |
| 2 | Deposit |  | 82,000 | 318,327 |
| 4 | Cheque no. 69 | 6,000 |  | 394,327 |
| 4 | Cheque no. 68 | 3,115 |  | 391,212 |
| 4 | Cheque no. 64 | 51,000 |  | 340,212 |
| 4 | Deposit |  | 7,280 | 347,492 |
| 7 | Cheque no. 70 | 7,000 |  | 340,492 |
| 7 | Cheque no. 71 | 51,500 |  | 288,992 |
| 7 | Deposit |  | 36,100 | 325,092 |
| 8 | Cheque no. 66 | 9,000 |  | 316,092 |
| 8 | Deposit |  | 28,000 | 344,092 |


| $\begin{aligned} & \text { Date } \\ & 1996 \end{aligned}$ | Particulars | Debit Sh. | Credit Sh. | Balance Sh. |
| :---: | :---: | :---: | :---: | :---: |
| October 9 | Cheque no. 72 | 1,330 |  | 342,762 |
| 9 | Cheque no. 73 | 6,250 |  | 336,512 |
| 9 | Deposit |  | 51,000 | 387,512 |
| 15 | Cheque no. 74 | 2,800 |  | 384,712 |
| 15 | Deposit |  | 20,560 | 405,272 |
| 16 | Cheque no. 75 | 65,000 |  | 340,272 |
| 16 | Deposit |  | 18,014 | 358,286 |
| 17 | Deposit |  | 34,500 | 392,786 |
| 19 | Cheque no. 76 | 8,500 |  | 384,286 |
| 19 | Deposit |  | 42,750 | 427,036 |
| 21 | Cheque no. 79 | 2,410 |  | 424,626 |
| 21 | Cheque no. 77 | 12,506 |  | 412,120 |
| 21 | Cheque no. 78 | 4,000 |  | 408,120 |
| 21 | Cheque no. 81 | 6,500 |  | 401,620 |
| 21 | Deposit |  | 9,000 | 410,620 |
| 23 | Cheque no. 82 | 16,240 |  | 394,380 |
| 23 | Deposit |  | 63,000 | 457,380 |
| 26 | Cheque no. 84 | 1,500 |  | 455,880 |
| 26 | Dividends |  | 8,750 | 464,630 |
| 26 | Deposit |  | 62,500 | 527,130 |
| 28 | Cheque no. 88 | 35,500 |  | 491,630 |
| 28 | Standing order (Insurance) | 10,400 |  | 481,230 |
| 28 | Cheque no. 85 | 27,000 |  | 454,230 |
| 28 | Cheque no. 87 | 22,500 |  | 431,730 |
| 28 | Deposit |  | 13,025 | 444,755 |
| 31 | Service charge | 750 |  | 444,005 |
| 31 | Deposit |  | 28,050 | 472,055 |

The following is the bank column of the cashbook:

| Date 1996 | Particulars | Debit Sh. | Date 1996 | Particulars | $\begin{array}{r} \hline \text { Credit } \\ \text { Sh. } \end{array}$ |
| :---: | :---: | :---: | :---: | :---: | :---: |
| October 1 | Balance b/d | 365,875 | October 1 | Cheque no. 65 | 13,000 |
| 1 | Deposited at bank | 7,280 | 1 | Cheque no. 66 | 9,000 |
| 3 | Deposited at bank | 36,100 | 1 | Cheque no. 67 | 3,548 |
| 5 |  | 28,000 | 2 | Cheque no. 68 | 3,115 |
| 8 |  | 51,000 | 4 | Cheque no. 69 | 6,000 |
| 10. |  | 20,560 | 5 | Cheque no. 70 | 7,000 |
| 15 |  | 18,014 | 5 | Cheque no. 71 | 51,500 |
| 15 |  | 34,500 | 7 | Cheque no. 72 | 1,330 |
| 17 |  | 42,750 | 8 | Cheque no. 73 | 6,250 |
| 19 |  | 15,700 | 10 | Cheque no. 74 | 2,800 |
| 19 |  | 9,000 | 11 | Cheque no. 75 | 65,000 |
| 22 |  | 36,000 | 15 | Cheque no. 76 | 5,800 |
| 24 |  | 26,500 | 18 | Cheque no. 77 | 12,506 |
| 27 |  | 13,025 | 19 | Cheque no. 78 | 4,000 |
| 28 |  | 28,050 | 19 | Cheque no. 79 | 2,410 |
| 29 |  | 171,010 | 19 | Cheque no. 80 | 3,860 |
| 31 |  | 31,525 | 19 | Cheque no. 81 | 6,500 |
|  |  |  | 22 | Cheque no. 82 | 16,240 |
|  |  |  | 23 | Cheque no. 83 | 15,000 |
|  |  |  | 26 | Cheque no. 84 | 1,500 |
|  |  |  | 28 | Cheque no. 85 | 27,000 |
|  |  |  | 28 | Cheque no. 86 | 10,520 |
|  |  |  | 28 | Cheque no. 87 | 22,500 |
|  |  |  | 28 | Cheque no. 88 | 53,500 |
|  |  |  | 30 | Cheque no. 89 | 2,500 |
|  |  |  | 31 | Cheque no. 90 | 64,529 |
|  |  |  | 31 | Cheque no. 91 | 15,500 |
|  |  |  | 31 | Balance c/d | 502,481 |
|  |  | 934,889 |  |  | $\underline{934.889}$ |

## Notes:

1. The bank reconciliation on 30 September 1996 showed that one deposit was in transit and two cheques had not yet been presented to the bank.
2. Deposits of Sh.62, 500 and Sh.36, 000 had been entered in the cash book as Sh. 26,500 and Sh. 36,000 and in the bank statement as $\mathrm{Sh} .62,500$ and $\mathrm{Sh} .63,000$, respectively.
3. A cheque from Mkulima for Sh.15,700 was deposited on 18 October 1996 but was dishonoured and the advice was received on 4 November 1996.
4. Counterfoils for cheques no. 76 and no. 88 showed they had been drawn for Sh.5,800 and Sh.35,500 respectively.

## Required:

(a) A correct cashbook balance.
(b) A bank reconciliation statement on 31 October 1996.
(Total: 20 marks)

## QUESTION FIVE

Jaguar Traders Ltd. was incorporated on 4 May 1998 with a nominal capital of Sh. 1,000,000 divided into 50,000 ordinary shares of Sh. 20 each.

On 5 May 1998, the directors invited interested members of the public to apply for purchase of shares at par. The closing date for application was 15 May 1998. Applications were received for 60,000 ordinary shares and paid in full. The allotment was made on 20 May 1998 and the excess application money refunded.
On 26 May 1998, the directors bought: furniture Sh. 150,000, equipment Sh.250,000 and goods Sh.500,000. All these were delivered and paid for on the same date.

## Required:

(a) Journal entries, including bank to record the above transactions. (5 marks)
(b) Ledger accounts (5 marks)
(c) Balance sheet as at 26 May 1998

## REVISION PAPER THREE

## QUESTION ONE

Jim Mukora commenced business as the proprietor of 'stop-shop' on 1 April 1993, paying Sh. 480,000 into business bank account. The Sh. 480,000 was made up of Sh. 320,000 from his own funds, and further Sh. 160,000 borrowed from his friend, Bob Meme, who was to be paid interest at $20 \%$ per annum on prorata basis. On 1 January 1994, Meme joined Mukora as a partner and it was agreed that:

1. Mukora and Meme should bring their cars into the partnership at values of Sh. 144,000 and $\mathrm{Sh} .96,000$ respectively. .
2. Meme's loan should be converted to capital on 1 January 1994 and he should introduce further capital of Sh.160, 000.
3. From 1 January 1994, Mukora should receive a salary of Sh.128, 000 per annum.
4. The balance of the profits and losses to be shared equally between the partners. The partnership did not keep full records, but the following information was obtainable:
(i) The bank statement showed:

| Receipts | Sh. | Payments | Sh. |
| :--- | ---: | :--- | ---: |
| Capital/Loans | 640,000 | Payment to trade creditors | $6,024,000$ |
| Receipts from debtors | $5,000,000$ | Interest on loan | 24,000 |
| Cash sales | 880,000 | Drawings -Mukora | 232,000 |
| Balance at 31 |  | - Meme | 40,000 |
| March 1994 | 232,000 | Sundry expenses | 312,000 |
|  |  |  | Rent of shop (Sh.12, 000 per month $) \underline{120,000}$ |
|  | $\underline{6,752,000}$ |  | $\underline{6,752,000}$ |

(ii) From various notes it was discovered that the following expenses were paid out of the takings from cash sales before they were banked:

|  | Sh. |
| :--- | ---: |
| Wages of shop | assistants |
| Motor expenses | 9 months to 31 December 1993 |
|  | 320,000 |
| Purchases | 3 months to 31 March 1994 |
| Sundry expenses | 52,000 |
|  | 22,400 |
|  | 59,200 |

A cash float of Sh.2, 400 was retained at the end of each day.
(iii) The cars are to be depreciated on the straight line basis at a rate of $25 \%$ per annum.
(iv) It was established that the following items were to be taken into account on 31 March 1994:

Trade creditors
Unexpired sundry expenses
Trade debtors
(v) Stocks on 31 March 1994 were valued at

## Sh.

108,000
4,000
824,000
776,000

## Required:

(a) A Trading Account for the year ended 31 March 1994.
(5 marks)
(b) Profit and Loss and Appropriation Accounts for the nine months ended 31 December, 1993 and for the three months ended 31 March 1994 and the year to 31 March 1994. (Unless otherwise stated, you may assume that all expenses and sales accrued evenly over the year).
(c) A balance Sheet at 31 March 1994.
(5 marks)
(Total: 25 marks)

## QUESTION TWO

(a) Explain the purposes for which control accounts are prepared in a business organisation.
(b) XML Ltd. maintains control accounts in its business records. The balances and transactions relating to the company's control accounts for the month of December 1994 are listed below:

## Sh.

Balance at 1 December 1994:
Sales ledger
Purchases ledger
Transactions during December 1994:
Sales on credit 8,452,000
Purchases on credit 5,687,500
Returns inwards 203,500
Returns outwards 284,000
Bills of Exchange payable 930,000
Bills of Exchange receivable 615,000
Cheques received from customers 7,985,000
Cheques paid to suppliers 4,732,000
Cash paid to suppliers 88,500
Bill payable dishonoured 400,000
Charges on bill payable dishonoured 10,000
Cash received from credit customers 153,000
Bad debts written-off 64,500
Cash discounts allowed 302,000
Bill receivable dishonoured 88,500
Balances at 31 December 1994:
Sales ledger
44,000 (credit)
Purchases ledger 23,500 (debit)

## Required:

Post the sales ledger and the purchases ledger control accounts for the month of December 1994 and derive the respective debit and credit closing balances on 31 December 1994.
(Total 20 marks)

## QUESTION THREE

The cashbook column of Tatua Traders Company Ltd. had an overdraft of Sh.532, 400 as at 31 October 1998, which did not agree with balance as per bank statement of the same date.

On checking through the relevant records and documents, some details were established as shown below:

1. Bank charges and interest on overdraft as per the bank statement amounted to Sh. 12,450 and Sh. 135,480 respectively.
2. A debtor deposited Sh.254, 500 to the bank direct.
3. Insurance premium of the mortgaged property amounting to Sh. 35,485 was paid direct by the bank.
4. Standing orders of Sh. 138,000 have been effected by the bank.
5. Cheques for Sh. 354,890 which were banked on 29 October 1998 were credited by the bank on 5 November 1998.
6. Cheques drawn by the company amounting to Sh. 745,964 had not been presented for payment as at 31 October 1998.
7. A cheque for Sh. 74,500 was debited by the bank as Sh. 47,500 .
8. The payments side of the cashbook was undercast by Sh.32, 000.
9. The bank had debited the account with another customer's cheque of Sh.27, 500 but had not yet corrected the mistake on 31 October 1998.

## Required:

(a) Make adjustments in the cash book and show the adjusted cash book balance. (10 marks)
(b) A bank reconciliation statement as at 31 October 1998
(10 marks)
(Total: 20 marks)

## QUESTION FOUR

Wananchi Transporters Company Ltd. was incorporated on 1 June 1994 and on the same day bought its first lorry, registration number KA 620, for Sh.4, 536,000.
On 3 April 1995, the company bought its second lorry, KA 735 for Sh.2, 740,000.
On 3 June 1997, the first lorry, KA 620 was involved in an accident and was completely written off. The insurance company paid the transport company Sh.1, 350,000 for the loss. On 5 January 1998, the company bought its third lorry, KB 327 for Sh.3, 780,000. Depreciation on the lorries was provided at 10 per cent on straight -line basis. The policy of the company is to provide depreciation for the full year for all acquisitions made at any time during the year and to ignore depreciation on any lorry sold or disposed of during the year. All the lorries are insured.

The company makes its accounts annually to 31 December.
In 1998, the company decided to change its depreciation rate from 10 to 15 per cent on straight line basis for all its lorries still in use retroactively, that is from year of purchase. An adjusting entry will be made in the accounts for the year 1998.

## Required:

1. The motor lorries account for years 1994 to 1998.
(4 marks)
2. A schedule of additional depreciation arising from change of depreciation rate, for years 1994 to 1997
(4 marks)
3. Provision for depreciation account for the same period.
(9 marks)
4. Disposal of motor lorries account.
(3 marks)
(Total: 20 marks)

## QUESTION FIVE

Write explanatory notes on the following accounting concepts:
(a) Materiality;
(5 marks)
(b) Prudence;
(5 marks)
(c) Consistency.

## REVISION PAPER FOUR

## QUESTION ONE

The following trial balance was extracted from the books of Mapema Traders Ltd. as at 31 March 1998:

|  | Sh. | Sh. |
| :--- | ---: | ---: |
| Ordinary shares Sh. 10 each |  | $18,000,000$ |
| $10 \%$ Preference shares Sh. 10 each |  | $3,000,000$ |
| $8 \%$ Loan stock |  | $3,000,000$ |
| Share premium | $9,900,000$ | $2,400,000$ |
| Trade debtors | $126,600,000$ | $144,000,000$ |
| Trade creditors | 150,000 |  |
| Purchases and sales |  | 390,000 |
| Discounts allowed | $15,000,000$ |  |
| Discounts received |  | $19,500,000$ |
| Freehold buildings: | $19,200,000$ |  |
| At cost | $12,600,000$ | $7,680,000$ |
| Provision for depreciation | $5,010,000$ | $2,400,000$ |
| Fixtures and fittings: | $3,900,000$ |  |
| At cost | $1,680,000$ |  |
| Provision for depreciation | 120,000 |  |
| Stock April 1997 |  | 540,000 |
| Returns outwards |  | $10,860,000$ |
| Selling and distribution expenses | $4,800,000$ |  |
| Establishment expenses | $-\overline{750}$ |  |
| Administration expenses | $\underline{198,900,000}$ | $\underline{198,960,000}$ |
| Bad debts written off |  |  |

## Additional information:

1. The debtors balance includes Sh.600,000 due from Otieno who has now been declared bankrupt and it has been decided to write-off this debt as a bad debt.
2. The provision for doubtful debts is to be adjusted to $5 \%$ of trade debtors at 31 March 1998.
3. Establishment expenses prepaid at 31 March 1998 amount to Sh. 120,000 . The difference is to be written off during the year.
4. Administration expenses accrued due at 31 March 1998 amounted to Sh.210,000.
5. The company paid the interest on the loan stock for the year ended 31 March 1998 on 28 May 1998.
6. Gross profit is at the rate of $20 \%$ of sales.
7. Depreciation is provided annually on the cost of fixed assets held at the end of the year at the following rates:
Freehold buildings $2 \%$
Fixtures and fittings 10\%
8. The company's directors propose that the preference share dividend be paid, a dividend of $10 \%$ on the ordinary shares to be paid and to transfer an amount of Sh. $7,500,000$ to General Reserve.

## Required:

The trading and profit and loss account for the year ended 31 March 1998 of Mapema Traders Ltd. and a balance sheet as at that date. ( 20 marks)

## QUESTION TWO

(a) Explain briefly the terms prime cost and factory cost as used by manufacturing firms.
(4 marks)
(b) Rono Ltd. manufactures electric toys called Densta on small scale basis. On 1 January 1997, 6000 units of Densta were in stock. During 1997, the company manufactured 200,000 units and sold 190,000 units at a price of Sh. 6 each.

The following balances were extracted from the books of account on 31 December 1997.

|  | Sh |
| :--- | ---: |
| Stock of raw material 1.1.97 | 23,280 |
| Stock of raw material 31.12.97 | 32,560 |
| Purchase of raw material | 269,000 |
| Carriage on raw material | 82,400 |
| Direct wages | 185,400 |
| Factory expenses: | 76,800 |
| Rent and rates | 34,400 |
| Power | 31,280 |
| Insurance | 300,000 |

The following additional information was available:

1. Stocks of work-in-progress on 1 January and 31 December 1997 were of insignificant value and are to be ignored.
2. Plant and machinery are to be depreciated using reducing balance method at $10 \%$.
3. Finished units of Densta are valued at factory cost.
4. Factory cost per unit of Densta was the same in 1996 and 1997.

## Required:

(i) The manufacturing account for the year ended 31 December 1997, showing clearly the prime cost and factory costs of producing Densta. (10 marks)
(ii) The trading account for the year ended 31 December $1997 . \quad$ (6 marks)

## QUESTION THREE

Sabuni Ltd manufactures and sells soaps and Lotions. The two products pass through two manufacturing departments 1 and 2. You are supplied with the following trial balance as at 30 June 2002

Ordinary shares of Sh. 10 each fully paid
Preference shares of Sh. 10 each fully paid
Share premium
Profit and Loss Accounts as at 30 June 2001
Non Current assets
Depreciation of non current assets
Stocks at 1 July 2001
Raw materials
Work in progress
Department $1 \quad 12,600$
Department 2 18,200
Finished goods
Soaps
422,000
Lotions
Debtors and Creditors
Bad debtors provision as at 1 July 2001
SalesSoaps (60,000 units)
Lotions (180,000 units)
618,000
323,200
137,000
15,600
1,200,000
2,400,000
Purchases of raw materials $1,240,000$
Factory wages
Department $1 \quad 160,000$
Department 2 240,000
Factory expenses 652,400
Administration expenses 637,200
Distribution expenses 310,800
Interim dividend paid Preference 20,000
Ordinary 50,000
Cash and bank balances $\quad 2,200$
5,826,600
5,826,600

The following additional information is given:
a) During the year the cost of materials consumed was Sh.627,720 for department 1 and Sh.572,280 for department 2
b) Stocks as at 30 June 2002 were:
Raw materials 160,000

Work in Progress Department $1 \quad 12,000$ Department $2 \quad 20,000$
Finished goods Soaps 400,000
Lotions 700,000
c) Depreciation is to be provided on Non current assets at the rate of 10 per cent per annum on cost. additional non current assets were purchased on 1 January 2002 at a cost of Sh.80,000.The annual depreciation charge is to be divided among manufacturing , administration and distribution in the ratio of 8:1:1.
d) Prepaid and accrued administration amount to Shs.1,800 and Shs.3,000 respectively.
e) Bad debts of Sh.3,200 are to be written off and a provision for doubtful debts to be increased to Sh.16,000.This should be taken as a distribution cost.
f) The following allocations are to be made.

- Manufacturing expenses (between dept 1 and dept 2) in proportion to manufacturing wages
- Administration expenses (between soaps and Lotions) in proportion to number of units sold
- Distribution expenses (between soaps and Lotions) in the proportion of sales value.
- Cost of goods manufactured in dept 1 (between soaps and Lotions) in the ration of 5:4.
- Cost of goods manufactured in dept 2 (between soaps and Lotions) in the ration of 1:5
g) Corporation tax payable for the year is $\mathrm{Sh} .160,000$.
h) The directors propose a final dividend of sh. 100,000 .


## Required:

> a) A manufacturing account showing the results of department 1 and 2 ,
> ii) Trading, Profit and Loss account showing the results of soaps and Lotions, for the year ending 30 June 2002 .
> b) A balance sheet as at 30 June 2002 . ( 25 marks)

## QUESTION FOUR

The trial balance of Bidii Retailers, which was extracted on 30 September 1996, included the following items:

|  | Sh. |
| :--- | ---: |
| Sales ledger control account | 550,885 |
| Purchases ledger control account | 391,330 |
| Suspense account in trial balance (debit balance) | 11,550 |

The following additional information is available:

1. The balances from sales ledger were: Debit balances Sh.555, 555 Credit
balances Sh.6, 170
2. The balances from purchases ledger were: Credit balances Sh.388.88:

Debit balances Sh.5, 555.
3. The sales ledger includes a debit balance of Sh.3, 500 for Moco Fishing Ltd., and the purchase ledger includes a credit balance of Sh.4, 000 relating to the same firm. The debit balance will be offset against the credit balance and the difference will be settled in cash.
4. Included in the credit balance on the sales ledger is a balance of Sh.3, 000 in the name of John Oloo. This arose because a sales invoice of Sh.3, 000 had earlier been posted in error from the sales daybook to the debit of the account of Peter Oloo in the purchases ledger.
5. An allowance of Sh.1,500 against some damaged goods had been omitted from the appropriate account in the sales ledger. This allowance had been included in the control account.
6. An invoice for Sh.2.280 had been entered in the purchase daybook as Sh.3,270.
7. A cash receipt from a credit customer for Sh. 1,725 had been entered in the cash book as Sh.1,225.
8. The purchase day book had been overcast by Sh.5,000.
9. The bank balance of Sh. 6,000 had been included in the trial balance, in error, as an overdraft.
10. The book-keeper had been instructed to write off Sh.2,500 from customer XYZ's account as a bad debt, and to reduce the provision for bad and doubtful debts by Sh.3,500. He however wrote off $\mathrm{Sh} .3,500$ from the customers' account. He then increased the provision for bad and doubtful debts by Sh.2,500.
11. The debit balance on the insurance account in the nominal ledger of Sh. $17,050 \mathrm{had}$ been included in the Trial balance as Sh.17,500.

## Required:

(a) Corrected sales ledger control, purchase ledger control, and suspense accounts balances.
(10 marks)
(b) Reconcile the sales ledger balances with the corrected sales ledger control account balance, and also the purchases Ledger balances with the corrected purchase ledger control balance.
(10 marks)
(Total: 20 marks)

## QUESTION FIVE

List the principal distinctions between partnerships and limited companies.

## REVISION PAPER FIVE

## QUESTION ONE

a) Define the term accounting standard and give four reasons why a professional accounting body issues accounting standards.
b) Explain the meaning and significance of the revenue realization principle.

Indicate and give reasons the amount of revenue that should be recognized in the year ended 31 May 1996 in each of the following independent cases:
c)
i) Net credit sales for 1995 amounted to Sh. 1.5 million, three-fourths of which were collected in 1995. Past experience indicates that about $97 \%$ of all credit sales are eventually collected.
ii) Cash of Sh.350,000 is received from a customer during 1996 in payment for equipment that is to be manufactured and shipped to the customer during 1997.
(2 marks)

Indicate, giving reasons, the correct treatment of each of the following transactions in the books of a company:
d)
i) Closing stock for the current year has a cost of Sh. 890,000 and a replacement cost of Sh. 850,000 . The stock has not been reduced to its replacement cost because the company's accountant believes that the purchase price of similar stock items would probably rise during next year. (3 marks)
ii) A new machine was purchased at an auction for cash at Sh.1. 6 million: Since the cash price of the machine would have been Sh.1. 9 million if it was purchased from the normal supplier, the machinery account been debited with Sh.1. 9 million as shown below:

|  | Sh. | Sh. |
| :--- | ---: | ---: |
| Machinery | $1,900,000.00$ |  |
| Cash |  | $1,600,000.00$ |
| Gain from bargain purchase | $\overline{300,000.00}$ |  |
|  | $1,900,000.00$ | $1,900,000.00$ |

## QUESTION TWO

(a) Define the term accounting standard and give four reasons why a professional accounting body issues accounting standards.
(5 marks)
(b) Explain the meaning and significance of the revenue realization principle. (5 marks)

Indicate and give reasons the amount of revenue that should be recognized in the year ended 31 May 1996 in each of the following independent cases:
c)
i) Net credit sales for 1995 amounted to Sh. 1.5 million, three-fourths of which were collected in 1995. Past experience indicates that about $97 \%$ of all credit sales are eventually collected.
(2 marks)
ii) Cash of Sh.350,000 is received from a customer during 1996 in payment for equipment that is to be manufactured and shipped to the customer during 1997. (2 marks)

Indicate, giving reasons, the correct treatment of each of the following transactions in the books of a company:
d)
i) Closing stock for the current year has a cost of Sh. 890,000 and a replacement cost of Sh.850,000. The stock has not been reduced to its replacement cost because the company's accountant believes that the purchase price of similar stock items would probably rise during next year. (3 marks)
ii) A new machine was purchased at an auction for cash at Sh.1. 6 million: Since the cash price of the machine would have been Sh.1. 9 million if it was purchased from the normal supplier, the machinery account been debited with Sh.1. 9 million as shown below:

|  | Sh. | Sh. |
| :--- | :--- | :--- |
| Machinery | $1,900,000.00$ |  |
| Cash  <br> Gain from bargain purchase $\underline{1,900,000.00}$ | $\underline{300,000.00}$ |  |
|  | $\underline{1,900,000.00}$ |  |

## QUESTION THREE

Jackson Ndambuki, a businessman in Kangundo, does not maintain a double entry bookkeeping system.
On 1 July 1994 his capital was Sh. 172,500. An analysis of his cashbook for the year to 30 June 1995 gives the following particulars:

|  |  | Sh. |
| :--- | ---: | ---: |
| Debit Side Received from sundry debtors |  | 150,000 |
| Paid in on capital account |  | 12,500 |
| Credit side Due to bank on 1 July 1994 | 18,500 |  |
| Payment to sundry creditors | 62,500 |  |
| General business expenses | 25,000 |  |
| Wages paid | 38,750 |  |
| Drawings |  | 7,500 |
|  |  |  |
| Other balances on 30 June | $\mathbf{1 9 9 4}$ | $\mathbf{1 9 9 5}$ |
|  | $\mathbf{S h}$ | $\mathbf{S h}$ |
| Sundry debtors | 132,500 | 220,000 |
| Sundry creditors | 37,500 | 48,750 |
| Stock in hand | 42,500 | 47,500 |
| Plant and machinery | 50,000 | 50,000 |
| Furniture | 3,500 | 3,500 |

Discounts allowed and received amounted to $\mathrm{Sh} .15,000$ and $\mathrm{Sh} .7,500$ respectively.
Interest of 5 per cent per annum is to be provided on capital at the beginning of the year.
(Ignore payments in and drawings)
Depreciate plant and machinery at 10 per cent and furniture at 5 per cent on the book value. A provision for doubtful debts of 5 per cent is to be made on sundry debtors.

## Required:

(a) Trading, Profit and Loss Account for the year ended 30 June 1995. (10 marks)
(b) Balance Sheet as at that date.
(10 marks)
(Total: 20 marks)

## QUESTION FOUR

The draft final account for the year ended 30 June 1994 of central limited, car dealers, show a gross profit of $\operatorname{Sh} 90,000$ and a net profit of $\operatorname{Sh} 2,250,000$. After subsequent investigations the following discoveries were made:

1. A debt of Sh. 75,000 due from J. Mema to the company was written off as irrecoverable in the company"s books in January 1994. Since preparing the draft accounts, J.Mema has settled the debt in full.
2. The company"s main warehouse was burgled in February 1994, when goods costing Sh. $5,000,000$ were stolen. This amount has been shown in the draft account as an overhead item "Loss due to burglary". Although the insurance company denied liability originally, in the past days or two that decision it has changed and central limited have advised that Sh. 3,500,000 will be paid in settlement.
3. Discounts received in March 1994 of Sh. 52,500 have been credited, in error, to purchases.
4. On 2 January 1994, a car, which had cost the company Sh. 450,000, was taken from the showroom for the use of one of the company"s sale representative whilst on company business. In the showroom, the is car had a Sh. 600,000 price label. Effect has not been given to this transfer in the books of the company, although the car was not included in the trading stock valuation at 30 June 1994.the company provides for depreciation on motor vehicles at the rate of $25 \%$ of the cost of vehicles held at the end of each financial year.
5. Goods bought and received from P.Nene on 29 June 1994 at a cost of Sh 300,000 were not recorded in the company"s books of account until early July 1994. Although they were unsold on 30 june 1994, the goods in question were not included in the stock valuation at that date.
6. The company is hoping to market a new car accessory product in January 1995. The venture is to be launched with an advertising campaign commencing in July 1994. The cost of this campaign is Sh. 1,250,000 and this has been debited in the company"s profit and loss account for the year ended 30 June 1994, and is included in current liabilities as a provision, notwithstanding the confident expectations that the new product will be a success.
7. On June 30 1994, the company paid an insurance premium of Sh. 150,000, the renewal being for the year commencing 1 July 994. This premium was included $n$ the insurances of Sh. 275,000 debited in the draft profit and loss account.

## Required:

(a) The journal entries necessary to effect corrections of all the above errors. (8 marks)
(b) A computations of the corrected gross profit and net profit for the year ended 30 June 1994
(10marks)
(Total: 20mark)

## QUESTION FIVE

(a) Name and explain four types of errors which are not disclosed by the trial balance.(8 matiks)
(b) The trial balance of S. Juma, a sole trader, did not balance on 30 April 1995. The difference was put in the suspense account. The final accounts, which were then prepared, showed a net profit of Sh.64, 000.

During audit, the following errors were noted:
(1) A loan from ABD Bank of Sh. 10,000 was entered correctly in cashbook but was not posted to the ledger.
(2) A cheque of Sh. 4,000 for rent received was not entered in the books.
(3) Closing stock was overvalued by Sh.1, 500 .
(4) Discount allowed of Sh. 500 was entered in the discount received account.
(5) The opening stock was understated by Sh.3,200.
(6) Prepaid insurance of Sh. 220 had been included in the profit and loss account.
(7) Goods destroyed by fire amounting to Sh. 12,000 were written off in the profit and loss account.

However the insurance company has agreed to compensate the full amount.

## Required:

| (a) | Journal entries to correct the errors. | $(8 \mathrm{marks})$ |
| :--- | :--- | :---: |
| (b) | Statement of corrected profit. | $(2$ marks |
| (c) | Suspense account | $(2$ marks $)$ |

## Answers

## REVISION PAPER ONE

## QUESTION ONE (June 94 Q.3)

1. 
2. 
3. 
4. 
5. 
6. 
7. 
8. 
9. 
10. 

Bank a/c
1st Call a/c
To record money received from 1 st Call of Preference shares
11. Bank a/c

2nd Call a/c
To record money received on 2 nd Call for
Preference shares
12.


|  | To close the call in arrears to forfeiture |  |  |
| :---: | :---: | :---: | :---: |
| 13. | DR. Re-issue a/c <br> CR. Forfeiture a/c <br> To record forfeited shares reissued | 39,000 |  |
| 14. | Forfeiture a/c <br> Share premium a/c <br> To record premium on reissue | 39,000 | 39,000 |
| 15. | Bank a/c <br> Re issue a/c <br> To record money received on reissued forfeited shares | 54,000 | 54,000 |
| 16. | Application and allotment a/c <br> Share premium a/c <br> To record premium received from application money ordinary | 100,000 | 100,000 |
| 17. | Application and allotment a/c <br> Share Premium a/c <br> To record premium received from application money (preference) | 20,000 | 20,000 |
| 18. | 1st Call a/c (Ordinary share capital) Ordinary share capital | 300,000 | 300,000 |
| 19. | 2nd Call a/c (Ordinary share capital) Ordinary share capital | 200,000 | 200,000 |
| b. Balance Sheet (extract) |  |  |  |
| EQUITY \& LIABILITIES |  |  | SHS |
| Capital and reserves |  |  |  |
| Ordinary share capital (300,000 shares @ Sh 10 per share) |  |  | 3,000,000 |
| New issue of 100,000 @ Sh 10 each |  |  | 1,000,000 |
|  |  |  | 4,000,000 |
| 50,000 7\% preference shares @ Sh 7 per value |  |  | 350,000 |
| New issue of 40,000 at Sh 9 each |  |  | 360,000 |
| Share premium |  |  | 159,000 |

## c. Explanation and Importance of Issuing Bonus shares

## Explanation

The directors of a limited company may decide to issue more shares to existing shareholders against the reserves or retained profits balance. Such an issue is referred to as bonus issue or script issue. These shares may also be issued against the share premium a/c. This is capitalization or reserves by a company.

## Entries

Dr. Reserve or P\&La/c
Cr. Share Capital a/c

## Importance

Since Bonus issue is capitalized or reserves which involves money set aside that will be used to pay unforeseen expenses.

## WORKINGS

W1
Application and Allotment (Ordinary shares)

|  | shs |  | shs |
| :--- | ---: | ---: | ---: |
| Bank | 200,000 | Bank | 500,000 |
| Share Premium | 100,000 | Bank | 300,000 |
| Ordinary Share Capital | $\underline{500,000}$ |  | $\underline{800,000}$ |
|  | $\underline{800,000}$ |  | $\underline{8}$ |

W2
Application and Allotment (Preference shares)

|  | shs |  | shs |
| :--- | ---: | :--- | ---: |
| Share premium | 20,000 | Bank | 100,000 |
| Preference Share Capital | $\underline{160,000}$ | Bank | $\underline{80,000}$ |
|  | $\underline{180,000}$ | $\underline{180,000}$ |  |

## W3

Bank Account

|  | shs |  | shs |
| :--- | ---: | ---: | ---: |
| Application (OSC) | 500,000 | Application (OSC) | 200,000 |
| Application (PSC) | 100,000 |  |  |
| Allotment (OSC) | 300,000 |  |  |
| Allotment (PSC) | 80,000 |  |  |
| 1st Call (OSC) | 291,000 |  |  |
| 2nd Call (OSC) | 194,000 |  |  |
| Reissue (OSC) | 54,000 |  | $\underline{1,519,000}$ |
| 1st Call (PSC) | 100,000 |  | $1,719,000$ |

## W4

1st Call (Ordinary Share Capital)

| Ordinary Share Capital | Shs | Bank <br> Call in arrears | s |
| :---: | :---: | :---: | :---: |
|  | 300,000 |  | 291,000 |
|  |  |  | 9,000 |
|  | 300,000 |  | 300,000 |

W5

| 2nd Call a/c |  |  |  |
| :--- | ---: | ---: | ---: |
| Ordinary Share Capital | Shs | Shs |  |
|  | 200,000 | Bank | 194,000 |
|  | $\underline{200,000}$ |  | $\underline{6,000}$ |
|  | Call in arrears | $\underline{200,000}$ |  |

W6
Calls in arrears

|  | Chs |  |
| :--- | ---: | ---: |
|  | 9,000 | Forfeiture |
| 1st Call | $\underline{6,000}$ |  |
| 2nd Call | $\underline{15,000}$ |  |
|  |  | $\underline{15,000}$ |
|  | $\underline{15,000}$ |  |


| W7 | Forfeiture a/c |  | $n$ |
| :---: | :---: | :---: | :---: |
|  |  |  | 1 |
|  | Shs |  | Shs |
| Calls in arrears | 15,000 | Ordinary Share Capital | 15,000 |
| Share Premiums | 39,000 | Reissue | 39,000 |
|  | 54,000 |  | 54,000 |
| W8 |  |  |  |
| Ordinary Share Capital |  |  |  |
| Forfeiture | Shs | Application \& allotment 1st Call | Shs |
|  | 15,000 |  | 500,000 |
|  |  |  | 300,000 |
|  |  | 2nd Call | 200,000 |
| Balc/d | 1,000,000 | Re-issue | 15,000 |
|  | 1,015,000 |  | 1,015,000 |
| W9 |  |  |  |
| Reissue a/c |  |  |  |
| Ordinary Share Capital Forfeiture | Shs | Bank | Shs |
|  | 15,000 |  | 54,000 |
|  | 39,000 |  |  |
|  | 54,000 |  | 54,000 |
| W10 |  |  |  |
| Share Premium a/c |  |  |  |
| Balc/d | Shs |  | Shs |
|  |  | Application \& allotment (OSC) | 100,000 |
|  |  | Application \& allotment (PSC) | 20,000 |
|  | 159,000 | Reissue a/c | 39,000 |
|  | 159,000 |  | 159,000 |
| W11 |  |  |  |
| 1st Call (Preference Shares) |  |  |  |
| Preference Share Capital | Shs | Bank | Shs |
|  | 100,000 |  | 100,000 |
|  | 100,000 |  | 100,000 |

W12
2nd Call (Preference Share Capital)

|  | Shs |  | Shs |
| :--- | ---: | ---: | ---: |
| Preference Share Capital | $\underline{100,000}$ | Bank | $\underline{100,000}$ |
|  | $\underline{100,000}$ | $\underline{100,000}$ |  |

W13
Preference Share Capital

| Preference Share Capital |  |  |  |
| :---: | :---: | :---: | :---: |
| Bal c/d | Shs |  | Shs |
|  |  | Application \& allotment | 160,000 |
|  |  | 1st Call a/c | 100,000 |
|  | 360,000 | 2nd Call a/c | 100,000 |
|  | 360,000 |  | 360,000 |

## QUESTION TWO (Nov 98 Q.2)

## KK LTD

TRADING, PROFIT \& LOSS ACCOUNT FOR THE YEAR ENDED 31 ${ }^{\text {ST }}$ OCTOBER 1998

| Sales (W1) | SHS | $\begin{array}{r} \text { SHS } \\ 127,615,000 \end{array}$ |
| :---: | :---: | :---: |
| Less; Cost of Sales |  |  |
| Opening Stock | 3,478,000 |  |
| Add: Purchases | 9,565,000 |  |
| Less: Returns inwards | $(128,000)$ |  |
| Less: Closing stock | $(4,398,000)$ | (94,602,000) |
| Gross Profit |  | 33,013,000 |
| Rent receivable |  | 4320,000 |
| Less: Expenses |  |  |
| Salaries (W6) | 2,419,000 |  |
| Telephone | 623,000 |  |
| Provision for doubtful debts | 77,000 |  |
| Depreciation - Furniture (W4) | 154,000 |  |
| Motor vehicle (W5) | 700,000 |  |
| Debenture interest (W9) | 350,000 |  |
| Rates | 289,000 |  |
| Water | 269,000 |  |
| Bad debts | 134,000 |  |
| Motor vehicle expenses | 2,470,000 |  |
| General expenses | 358,000 | $(7,833,000)$ |
| Net Profit |  | 25,600,000 |
| Corporate tax @ 35\% (35\% X 25,600,000) |  | (8,960,000) |
| Dividend (W8) |  | $\begin{array}{r} \overrightarrow{16,640,000} \\ (2,850,000) \end{array}$ |
| Transfer to general reserve | 4,500,000 | 19,490,000 |
| Appropriated profit | 2,500,000 | (7,000,000) |
|  |  | $\underline{12,490,000}$ |

## KK BALANCE SHEET

 AS AT $31^{\text {ST }}$ OCTOBER 1998| NON CURRENT ASSETS | Shs | Shs | Shs |
| :---: | :---: | :---: | :---: |
| Freehold property | 44,500,000 |  | 44,500,000 |
| Furniture | 1,540,000 | 2,920,000 | 1,248,000 |
| Motor vehicle | 3,500,000 | 965,000 | 2,535,000 |
| Goodwill |  |  | $\begin{array}{r} 48,283,000 \\ 500,000 \\ \hline \end{array}$ |
|  |  |  | 48,783,000 |
| CURRENT ASSETS |  |  |  |
| Stock |  |  | 4,398,000 |
| Debtors (W2) |  | 1,540,000 |  |
| Less Provision for bad \& doubtful debts |  | (77,000) | 1,463,000 |
| Accrued rent income |  |  | 35,000 |
| Bank |  |  | 10,492,000 |
|  |  |  | 16,388,000 |
| TOTAL ASSETS |  |  | 65,171,000 |
| EQUITY \& LIABILITIES |  |  |  |
| Capital \& reserves |  |  |  |
| Capital |  |  | 30,000,000 |
| General reserve |  |  | 4,500,000 |
| Share premium |  |  | 350,000 |
| Retained profit |  |  | 12,490,000 |
|  |  |  | 47,340,000 |
| CURRENT LIABILITIES |  |  |  |
| Trade creditors (W3) |  | 332,000 |  |
| Accruals |  | 189,000 |  |
| Current tax |  | 8,960,000 |  |
| Dividends |  | 4,500,000 |  |
| Debenture interest |  | -350,000 | 14,331,000 |
| TOTAL EQUITY \& LIABILITIES |  |  | $\underline{65,171,000}$ |

## Workings

W1 Sales
$127,450,000+165,000=127,615,000$

W2 Debtor
$1,375,000+165,000=1,540,000$
W3 Creditors
$460,000-128,000=332,000$
W4 Depreciation
(A) Furniture $(10 \% \times 1,540,000)=154,000$

W5 (B) Motor vehicle $(20 \% \times 3,500,000)=700,000$

W6 Salaries

> Paid Accrued

$$
\begin{array}{r}
2,285,000 \\
\hline 134,000 \\
\hline \underline{2,419,000}
\end{array}
$$

W7 Provision for bad and doubtful debts $5 \% \times 154,000=77,000$

W8 Dividend $15 \% \times 30,000,000=4,500,000$
$10 \% \times 3,500,000=350,000$
W9 Debenture interest

W10 Accruals

| Salaries | 134,000 <br> Telephone |
| :--- | ---: |
|  | $\underline{55,000}$ |
|  | $\underline{189,000}$ |

## QUESTION THREE (NOV 94 Q.3)

a)

UPDATED CASHBOOK

|  | Shs |
| :--- | ---: |
| Overdraft as per cashbook | $(190,000)$ |
| Add: Standing order | 20,000 |
| $\quad$ Advertising cheque error | 3,000 |
|  |  |
| Less: Cheques for payment of invoice error | $\underline{(9,000)}$ |
| Overdraft as per cashbook | $\underline{(204,000)}$ |

## BANK RECONCILIATION STATEMENT

|  | Shs |
| :--- | ---: |
| Updated Cashbook balance | $(204,000)$ |
| Add: Unpresented cheques | 518,500 |
| Less: Uncredited cheques | $(840,000)$ |
|  | $(525,500)$ |

b) Explain how a company may have a reduced bank balance with the bank statement during an accounting period but still have earned a profit that same period.

1. Operating a current account whereby customers on whom goods are sold, directly deposit money into the bank. This will reduce the bank balance in the cashbook of the company and increase balance in the bank statement and a profit is still earned.
2. Cases of cash recording errors on payment side of the cashbook whereby it is overstated. The bank statement will read higher than the cashbook and a profit is still earned.
3. Cases of bad debts written off in which the debtor knows the account of the company and pays the company"s account directly as Bad debts recovered. The company will have reduced its bank balance but on the other hand the bank statement reads high values and the company will have earned a profit.

## QUESTION FOUR (DEC 1995 Q.4)

a)

Amount of Depreciation

$$
\begin{array}{ll}
1.3 .1990 & \mathrm{KA}=560,000 \\
& \mathrm{~KB}=720,000
\end{array}
$$

1990
$\mathrm{KA}=25 \% \times 560,000=140,000$
$K B=25 \% \times 720,000=180,000$
1991
$K A=140,000$
$K B=180,000$
1992
$\mathrm{KA}=140,000$
$K C=800,000 \times 25 \%=200,000$
$\mathrm{KD}=800,000 \times 25 \%=200,000$
1993
$K A=140,000$
$K D=200,000$
1994
$K A=140,000$
$K D=200,000$
$\mathrm{KE}=840,000 \times 25 \%=210,000$
$K F=960,000 \times 25 \%=240,000$

## Provision for depreciation

| 1990 |  | 1990 |  |
| :---: | :---: | :---: | :---: |
|  |  | Profit \& loss - KA | 140,000 |
|  |  | - KB | 180,000 N |
| Bal c/d | 320,000 |  | 320,000 |
|  | 320,000 |  | 320,000 |
| 1991 |  | 1991 |  |
|  |  | Bal b/d | 320,000 |
|  |  | P \& L - KA | 140,000 |
| Bal c/d | 640,000 | - KB | 180,000 |
|  | 640,000 |  | 640,000 |
| $\begin{aligned} & 1992 \\ & \text { Disposal KB } \end{aligned}$ |  | 1992 |  |
|  | 360,000 | Bal b/d | 640,000 |
|  |  | P\&L KA | 140,000 |
|  |  | KC | 200,000 |
| Bal c/d | 820,000 | KD | 200,000 |
|  | 1,180,000 |  | 1,180,000 |
| 1993 |  | 1993 |  |
| Disposal | 200,000 | Balance b/d | 820,000 |
|  |  | P \& L KA | 140,000 |
| Bal c/d | 960,000 | KD | $\begin{array}{r} \underline{200,000} \\ \underline{1,160,000} \end{array}$ |
|  | 1,160,000 |  |  |
| 1994 |  | 1994 |  |
|  |  | Bal b/d | 960,000 |
|  |  | P \& L KA | 140,000 |
|  |  | KD | 200,000 |
|  |  | KE | 210,000 |
| Bal c/d | 1,750,000 | KF | 240,000 |
|  | 1,750,000 |  | 1,750,000 |

Motor Vehicle Account

|  | Shs |  | Shs |
| :---: | :---: | :---: | :---: |
| 1991 |  | 1991 |  |
| Cash - KA | 560,000 |  |  |
| KB | 720,000 | Bal c/d | 1,280,000 |
|  | 1,280,000 |  | 1,280,000 |
| 1992 |  | 1992 |  |
| Bal b/d | 1,280,000 |  |  |
| Cash - KC | 800,000 |  |  |
| KD | 800,000 | Bal c/d | 2,160,000 |
|  | 2,880,000 |  | 2,880,000 |
| 1993 |  |  |  |
| Bal b/d | 2,160,000 | Disposal | 800,000 |
|  |  | Bal c/d | 1,360,000 |
|  | 2,160,000 |  | 2,160,000 |
| 1994 |  | 1994 |  |
| Bal b/d | 1,360,000 |  |  |
| Cash - KE | 840,000 |  |  |
| KF | 960,000 | Bal c/d | 3,160,000 |
|  | 3,160,000 |  | 3,160,000 |

Motor Vehicle Disposal Account

|  | KB | KC |  | KB | TAC |
| :---: | :---: | :---: | :---: | :---: | :---: |
| Cost <br> Profit \& Loss a/c | $\begin{aligned} & \hline \text { (Shs) } \\ & 720,000 \\ & \hline 720,000 \end{aligned}$ | (Shs) <br> 800,000 <br> 116,000 <br> 916,000 | Proceeds <br> Accumulated deprn. P \& L | (Shs) <br> 160,000 <br> 360,000 <br> 200,000 <br> 720,000 | $\begin{aligned} & \text { (Shs) } \\ & 716,000 \\ & \overline{916,000} \end{aligned}$ |

## QUESTION FIVE (NOV 97 Q.5)

## Explanatory notes on

## (a) Fundamental accounting concepts

These are the broad basic assumptions which underline the periodic financial accounts of business enterprises. At present four fundamental accounting concepts are generally recognized;

## (I) The Going Concern or Continuity Assumption

In accounting for an accounting entity, it is to be assumed that the accounting entity will continue in operation for the foreseeable future. It is assumed that the accounting entity has neither the intention nor the necessity of liquidation or of curtailing materiality the scale of its operations. The assumptions provide the foundation for accrual accounting. When the accounting entity ceases to be a going concern, the accounting approach changes from accrual to realization and liquidation.

## (II) Accrual / Matching Concept

This simply means that revenue should be matched against the expenses. The incurred in the year in which they were incurred. This is shown when treating prepayment and accruals. Accruals at the end of the year relating to expenses or income are added while prepayments are deducted.
Under the basis, the effects of transactions and other events are recognized when this occur (and not as cash or its equivalent is received or paid) and they are recorded in the accounting records and reported in the financial statements or the periods which they relate. Financial statements prepared on the accrued basis inform users not only of past transactions involving the payment and receipt of cash but also of obligations to pay cash in the future and resources that represent cash to be received in future.

## (III) Consistency Concept

The accounting treatment of like items should be consistent e.g. in the application of the particular method of depreciation lets say straight line method then it should be applied consistently.

## (IV) Prudence Concept

Uncertainties inevitably surround many transactions and revenue and profit, should not be anticipated but recognized only when they are realized in the form of cash or other assets which can be treated as cash.
Prudence is the inclusion of a degree of caution in the exercise of the judgments needed in making the estimates required under conditions of uncertainty, such that assets or incomes are not overstated and liabilities or expenses are not overstated.

## (b) Accounting Bases

Extending from the four fundamental concepts are many other principles which are known as accounting bases. They are defined in statement as the methods developed for applying fundamental accounting concepts to financial transactions and items. For example;

- Stock Valuation
- Depreciation bases


## (c) Accounting Policies

These are the specific accounting bases selected and consistently followed by a business enterprise as being appropriate to its circumstances.

The following summary is fundamental for easy understanding.

| Concept | Base | Policy |
| :--- | :--- | :--- |
| Accruals | Depreciation of assets | Straight line over useful life |
| Prudence | Provision against debts | $5 \%$ of outstanding debts |
| Consistency | The use of constituent bases | The use of constituent policies |

## REVISION PAPER TWO

## QUESTION ONE (DEC 95 Q.)

## HIZA LTD

TRADING, PROFIT \& LOSS ACCOUNT FOR THE YEAR ENDED 30 ${ }^{\text {TH }}$ JUNE 1995

| Sales | SHS ${ }^{\prime \prime} 000$ | $\begin{aligned} & \hline \text { SHS "000 } \\ & 296,000.00 \end{aligned}$ |
| :---: | :---: | :---: |
| Less: Cost of sales |  |  |
| Opening stock | 26,875 |  |
| Add purchases | 228,440 |  |
| Less: Drawings (Ombima) | (437.5) |  |
| Less: Closing stock | (28875) | 226,002.50 |
| Gross Profit |  | 69,997.50 |
| Rent received (W1) |  | 500.00 |
|  |  | 70,497.50 |
| Less: Expenses |  |  |
| Provision for doubtful debts (W2) | 400 |  |
| Wages \& Salaries (W3) | 43,435 |  |
| Rates \& Insurance (W4) | 995 |  |
| Depreciation on motorvehicle (W5) | 2,400 |  |
| General expenses | 10,825 |  |
| Motor vehicle expenses | 1,930 |  |
| Bad debts | 1,175 |  |
| Loan interest (W6) | 625 | $(61,785)$ |
| Net profit |  | 8,712.50 |
| Add: Net profit b/d |  | $\underline{18400.00}$ |
|  |  | 27,112.50 |

## HIZA LTD

BALANCE SHEET
AS AT $30^{\mathrm{TH}}$ SEPTEMBER 1995

|  | Shs"000 | Shs"000 | Shs"000 |
| :---: | :---: | :---: | :---: |
| NON CURRENT ASSETS |  |  |  |
| Freehold property | 50,000 |  | 50,000 |
| Motor vehicle | 12,000 | 7,200 | 4,800 |
|  | 62,000 | 7,200 | 54,800 |
|  |  |  | 7,500 |
|  |  |  | 62,300 |
| CURRENT ASSETS |  |  |  |
| Stock |  | 28,875 |  |
| Debtors | 33,900 |  |  |
| Less: Provision for doubtful debt | (750) | 33,150 |  |
| Bank |  | 5,020 |  |
| Rates, Insurance prepaid |  | 155 | 67,200 |
| TOTAL ASSETS |  |  | 129,500 |
| CAPITAL \& RESERVES |  |  |  |
| $3,125,000$ ordinary shares of sh. 20 each |  |  | 62,500 |
| Current a/c (W7) Ombima |  |  | 1,262.5 |
| Mwangi |  |  | 975 |
| Profit |  |  | 27,112.5 |
|  |  |  | 91,850 |
| NON CURRENT LIABILITIES |  |  |  |
| Loan from Bank |  |  | 12,500 |
| CURRENT LIABILITIES |  |  |  |
| Creditors |  | 23,275 |  |
| Salaries \& Wages accrued |  | 500 |  |
| Rent income prepaid |  | 125 |  |
| Loan interest outstanding (W6) |  | 1250 | 25,150 |
| TOTAL EQUITY \& LIABILITIES |  |  | 129,500 |

## Workings

W1 Rent received

|  | SHS |
| :--- | ---: |
| Rent received | 625,000 |
| Less: prepaid | $(125,000)$ |
|  | $\underline{500,000}$ |

W2 Provision for doubtful debts a/c

|  | Shs |  | Shs |
| :--- | ---: | :--- | ---: |
| Bal c/d | $\underline{750,000}$ | Balance b/d | P \& L |
|  | $\underline{750,000}$ |  | 350,000 |
|  |  | $\underline{400,000}$ |  |

W3 Wages \& Salaries

| Paid | 42,935 |
| :--- | ---: |
| Add: Outstanding | $\underline{43,435}$ |

W4 Rates and Insurance

| Paid | 1150 |
| :--- | ---: |
| Less: prepaid | $\underline{(155)}$ |
|  | $\underline{995}$ |

W5 Depreciation on motor vehicle $12,000 \times 20 \%=24,000$

W6 Loan interest
$5 \% \times 12,500=625$
Loan Interest a/c

| Bal c/d |  | Bal b/d | 625 |
| :---: | :---: | :---: | :---: |
|  | 1250 | P \& L (1995) | 625 |
|  | 1250 |  | $\underline{1250}$ |

## QUESTION TWO (DECEMBER 1994 Q.2)

a) SCHEDULE OF APPORTIONING EXPENSES

Advertising - Sales ratio
Hardware $7,080,000 \times 73,800=49,200$

$$
10,620,000
$$

Electrical $=\frac{3,549,000}{10,620,000} \times 73,800=24,600$

Rent - Floor area
$4,000 \times 183,200=122,133.33$; Hardware
6,000
$\underline{2,000} \times \quad 183,200=61,066.67$; Electrical
6,000

Canteen charges ; Floor area
Hardware $\frac{4,000}{6,000} \times 105,000=70,000$

Electrical $\frac{2,000}{6,000} \times 105,000=35,000$

Insurance on stock - Average stock level
$\underline{300,000} \times 112,800=60,000 \quad$ Hardware
564,000
$\frac{264,000}{564,000} \times 112,800=52,800 \quad$ Electrical

Electrical expenses - Floor area

| $\frac{4,000}{6,000} \times 108,000=72,000$ | Hardware |
| :--- | :--- |
| $\frac{2,000}{6,000} \times 108,000=36,000$ | Electrical |

General administration expenses - Number of workers

$$
\begin{aligned}
& \frac{9}{15} \times 244,800=146,880 \quad \text { Hardware } \\
& \frac{6}{15} \times 244,800=97,920 \quad \text { Electrical }
\end{aligned}
$$

b) (i) Departmental Profit and Loss account

|  | Hardware |  | Electrical |  | Combined |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Sh"000 | Sh"000 | Sh"000 | Sh"000 | Sh"000 | Sh"000 |
| Sales |  | 7,080 |  | 3,540 |  | 10,620 |
| Less: Cost of sales |  |  |  |  |  |  |
| Opening stock | 278.4 |  | 256.32 |  | 534.72 |  |
| Add: Purchases | 2,400 |  | 1,200 |  | 3,600 |  |
| Less closing stock | (336) | $(2,342.4)$ | (294) | 1,162.32 | (630) | (3504.72) |
| Less: Expenses |  |  |  |  |  |  |
| Wages | 249,702 |  | 1,873.2 |  | 4,370.4 |  |
| Advertising | 49.2 |  | 24.6 |  | 73.8 |  |
| Discount allowed | 48 |  | 24 |  | 72 |  |
| Deprn on shop ftgs | 21.6 |  | 84 |  | 300 |  |
| Rent and rates | 122.133 |  | 61.067 |  | 183.20 |  |
| Canteen charges | 70 |  | 35 |  | 105 |  |
| Electricity | 72 |  | 36 |  | 108 |  |
| Insurance on stock | 60 |  | 52.8 |  | 112.8 |  |
| General admin expenses | 146.88 |  | 97.92 |  | 244.8 |  |
| Manager"s | 72.809 | (3,354,222) | 4,457 | $(2,293,044)$ | 72,266 | (5647.266) |
| commission |  |  |  |  |  |  |
| Net profit |  | 1,383,378 |  | 84,636 |  | 1,468.014 |

## MUNENE TRADERS

## COMBINED BALANCE SHEET

AS AT 30 ${ }^{\text {TH }}$ SEPTEMBER 1994

|  | SHS | SHS | SHS |
| :---: | :---: | :---: | :---: |
| NON CURRENT ASSETS |  |  |  |
| Buildings | 5,160,000 | - | 5,160,000 |
| Shop fittings \& equipment |  |  |  |
| Hardware |  |  | 1,944,000 |
| Electrical |  |  | 756,000 |
|  |  |  | 7,860,000 |
| CURRENT ASSETS |  |  |  |
| Stock; Hardware |  | 336,000 |  |
| Electrical |  | 294,000 |  |
| Debtors |  | 1,224,000 |  |
| Prepayment: Administration |  | 3,960 |  |
| Rent |  | 6,400 |  |
| Bank |  | 672,000 | 2,536,360 |
| TOTAL ASSETS |  |  | 10,396,360 |
| EQUITY \& LIABILITIES |  |  |  |
| CAPITAL \& RESERVES |  |  |  |
| Capital |  |  | 8,520,000 |
| Drawings |  |  | $(360,000)$ |
| Net profit |  |  | 1,468,014 |
|  |  |  | 9,628,014 |
| CURRENT LIABILITIES |  |  |  |
| Creditors |  | 638,280 |  |
| Wages owing: Hardware |  | 30,000 |  |
| Electrical |  | 20,400 |  |
| Electricity expenses |  | 2,400 |  |
| Commission outstanding: Hardware |  | 72,809 |  |
| Electrical |  | 4,957 | 768,346 |
| TOTAL EQUITY \& LIABILITIES |  |  | 10,396,360 |

## QUESTION THREE

Kay Club and Ray Society
Trading and Profit \& Loss Account for the year ended 31 December 1994

Sales
Less: Cost of sales
Opening stock
Add: Purchases

Less: Closing stock
Gross profit to income \& expenditure

Sh.
Sh.

850,000.00
4,400,000.00
5,250,000.00
(805,000.00)

5,200,000.00

4,445,000.00
755,000.00

## Kay Club and Ray Society

Income and Expenditure Account for the year ended 31 December 1994

Sh.

## Income

Profit from trading
Subscriptions
Ticket sales
Admissions - Kay club

## Expenditure

Loss on disposal
Depreciation of Amplifier
Musicians fees
Coaching fees
Hall rent
Rates
Decorating
Cleaning
Annual ray expedition
Annual dinner
Prizes
Adjudicators fees
Stationery

Kay Club and Ray Society
Balance Sheet as at 31 December 1994
Sh.
Non Current Assets

## Amplifier Current Assets

| Stocks |  | 805,000.00 |  |
| :---: | :---: | :---: | :---: |
| Prepayments |  | 82,500.00 |  |
| Bank |  | 1,700,000.00 |  |
|  |  | 2,587,500.00 |  |
| Current Liabilities |  |  |  |
| Creditors | 450,000.00 |  |  |
| Prepaid Subscriptions | 65,000.00 | (515,000.00) | 2,072,500.00 |
|  |  |  | 2,387,500.00 |
| Accumulated fund |  |  | 1,550,000.00 |
| Surplus |  |  | 837,500.00 |
|  |  |  | $\underline{2,387,500.00}$ |

## Workings

| Subscriptions - Kay Club |  |  | $N$ |
| :---: | :---: | :---: | :---: |
| Income and Expenditure Balance c/d | Sh. $1,220,000.00$ $50,000.00$ | Balance b/d <br> Receipts and Payments | Sh. $65,000.00$ $1,205,000.00$ |
|  | 1,270,000.00 |  | 1,270,000.00 |
| Subscriptions - Ray Society |  |  |  |
| Income and Expenditure | $\begin{array}{r} \text { Sh. } \\ 860,000.00 \end{array}$ | Balance b/f | Sh. $30,000.00$ |
| Balance c/d | 15,000.00 | Receipts and Payments | 845,000.00 |
|  | 875,000.00 |  | 875,000.00 |
| Total to Income and Expenditure | Kay Club Ray Club | 1,220,000.00 |  |
|  |  | 860,000.00 |  |
|  |  | 2,080,000.00 |  |

Remember the policy of the club is to report income from subscriptions when cash is received so there is no debtors for subscriptions.

| Creditors - Clothes |  |  |  |  |  |  |
| :--- | :---: | :--- | ---: | :---: | :---: | :---: |
|  | Sh. |  | Sh. |  |  |  |
| Receipts and Payments | $900,000.00$ | Balance b/f | $200,000.00$ |  |  |  |
| Balance c/d | $\underline{300,000.00}$ | Purchases | $\underline{1,000,000.00}$ |  |  |  |
|  | $\underline{1,200,000.00}$ |  | $\underline{1,200,000.00}$ |  |  |  |
|  |  |  |  |  |  |  |
|  | Creditors - Refreshments | Sh. |  |  |  |  |
| Receipts and Payments | $3,500,000.00$ | Balance b/f | $\underline{250,000.00}$ |  |  |  |
| Balance c/d | $\underline{150,000.00}$ | Purchases | $\underline{3,400,000.00}$ |  |  |  |
|  | $\underline{3,650,000.00}$ |  | $\underline{3,050,000.00}$ |  |  |  |
|  |  |  |  |  |  |  |

i) Income and expenditure account will show all the incomes and expenses that relate to the financial period in accordance e with the matching concept. Receipts and payments Accounts for cash received or paid out.
ii) Income and expenditure reports the overall performance of the club i.e. whether there is any surplus or deficit. Receipts and payments shows the cash position.

## QUESTION FOUR (NOV 1996 Q. 4 (a) and (b)

## a) Purpose of preparing a Bank Reconciliation Statement

i) To update the cashbook with items present in the bank statement and missing in the cashbook or vice versa
ii) To locate errors committed by the cashier in the cashbook
iii) To detect frauds since banking may be done by another person who may not be honest
iv) To identify cheques that are unpresented, uncredited and those that are dishonoured by the bank

UPDATED CASH BOOK

|  | Shs |  | Shs |
| :--- | ---: | :--- | ---: |
| Balance b/d | 502,481 | Service charge | 750 |
| Dividends | 8,750 | Standing Order | 10,400 |
| Errors on cashbook (W3) | 36,000 | Dishonoured cheques | 15,700 |
| Errors by overstating payment | $\underline{18,000}$ | Balance c/d | $\underline{538,381}$ |
|  | $\underline{565,231}$ |  | $\underline{565,231}$ |

## BANK RECONCILIATION STATEMENT

Balance as per updated cashbook
Add; Unpresented cheques
Cheques No. 80
Cheques No. 83
Cheques No. 86
Cheques No. 89
Cheques No. 90
Cheques No. 91
Add; Credit error ( W4 )
Less: Uncredited cheque
Deposit
Cheque No. 31
Debit error (W2)

| Shs | Shs |
| ---: | ---: |
|  | 538,381 |
| 3,360 |  |
| 15,500 |  |
| 10,520 |  |
| 2,500 |  |
| 64,529 |  |
| 15,500 | 111,909 |
|  | 27,000 |
| 171,010 |  |
| 31,525 | 202,535 |
|  | $\underline{(2,700)}$ |
|  | $\underline{472,055}$ |

## Workings

W1 Bank error (WK 1)

| Deposit | 63,000 |
| :--- | :--- |
| Error | $(36,000)$ |
|  | 27,000 |

W2 8500 (5800) 2700

W3 Cashbook error
62,500
$(26,500)$
36,000
W4 $53,500-35,500=18,000$

## QUESTION FIVE (JUNE 1998 Q.5)

## A) Journal entries

|  | DEBIT <br> Shs | CREDIT <br> Shs |
| :--- | ---: | ---: |
| Bank account <br> Application a/c <br> To record receipt of application money | $1,200,000$ | $1,200,000$ |
| Application a/c <br> Bank a/c | 200,000 | 200,000 |
| To record refund of money from rejected application | $1,000,000$ |  |
| Application a/c <br> Ordinary share capital a/c <br> To transfer money received on application to ordinary share <br> capital account |  | $1,000,000$ |


| Bank account |  |  | Shs |
| :--- | ---: | :--- | ---: |
|  | Shs |  | 200,000 |
| Application a/c | $1,200,000$ | Application a/c | 150,000 |
|  |  | Furniture a/c | Equipment a/c |
|  |  | Purchases a/c | 250,000 |
|  |  | Bal c/d | 500,000 |
|  | $\underline{1,200,000}$ |  | $\underline{100,000}$ |
|  |  | $\underline{1,200,000}$ |  |

## Application account

|  | Shs | Shs |  |
| :--- | ---: | ---: | ---: |
| Bank a/c | 200,000 | Bank a/c | $1,200,000$ |
| Ordinary Share Capital | $\underline{1,000,000}$ | $\underline{1,200,000}$ | $\underline{1,200,000}$ |

Ordinary share capital account

| Bal c/d | Shs |  | Shs |
| :--- | ---: | ---: | ---: |
|  | $\underline{1,000,000}$ | Application a/c | $\underline{1,000,000}$ |

JAGUAR TRADERS LTD
BALANCE SHEET AS AT $26{ }^{\text {TH }}$ MAY 1998
NON CURRENT ASSETS

| Furniture | 150,000 |
| :--- | ---: |
| Equipment | 250,000 |

## CURRENT ASSETS

| Stock | 500,000 |
| :--- | ---: |
| Bank | $\mathbf{1 0 0 , 0 0 0}$ |
|  | $1,000,000$ |

EQUITY \& LIABILITIES
Ordinary Share Capital
$1,000,000$

## REVISION PAPER THREE

QUESTION ONE (NOVEMBER 1994 Q.1)
MEME \& MUKORA
TRADING ACCOUNT FOR THE YEAR ENDED 31ST MARCH 1994

| Sales (W3) | Shs | $\begin{array}{r} \text { Shs } \\ 7,172,000 \end{array}$ |
| :---: | :---: | :---: |
| Less: Cost of sales |  |  |
| Purchases (W2) | 6,191,200 |  |
| Less: Closing stock | $(776,000)$ | $(5,415,200)$ |
|  |  | 1,756,800 |

## PROFIT, LOSS \& APPROPRIATION ACCOUNT

|  | FOR 3 | MONTHS | FOR 6 | MONTHS |
| :---: | :---: | :---: | :---: | :---: |
| Gross profit | Shs | $\begin{array}{r} \text { Shs } \\ 439,200 \end{array}$ | Shs | $\begin{array}{r} \text { Shs } \\ 1,317,600 \end{array}$ |
| Less: Expenses |  |  |  |  |
| Wages | 80,000 |  | 240,000 |  |
| Motor expenses | 22,400 |  | 52,000 |  |
| Sundry expenses | 82,000 |  | 246,000 |  |
| Depreciation on motor vehicle |  |  | 45,000 |  |
| Rent (W5) | 36,000 |  | 108,000 |  |
| Interest on loan | 24,000 | $(224,400)$ |  | $(691,000)$ |
| Net profit |  | 194,800 |  | 626,000 |
| Salaries: Mukora |  |  | 96,000 |  |
| Share of profit: Mukora |  |  | 265,300 |  |
| Meme | 194,800 | $(194,800)$ | 265,300 | (626,600) |

MEME \& MUKORA
BALANCE SHEET
AS AT 31 ${ }^{\text {ST }}$ DEC 1993

| NON CURRENT ASSETS | Shs | Shs | Shs |
| :---: | :---: | :---: | :---: |
| Motor vehicle (W4) | 240,000 | 45,000 | 195,000 |
| CURRENT ASSETS |  |  |  |
| Stock |  | 776,000 |  |
| Debtor |  | 824,000 |  |
| Cash |  | 2,400 |  |
|  |  |  | 1,602,400 |
| TOTAL ASSETS |  |  | 1,797,400 |
| EQUITY \& LIABILITIES |  |  |  |
| CAPITAL \& RESERVES |  |  |  |
| Capital : Mukora (W1) |  |  | 644,100 |
| Meme (W1) |  |  | 545,300 |
| Additional capital (W6) |  |  | 240,000 |
| CURRENT LIABILITIES |  |  |  |
| Creditors |  | 108,000 |  |
| Bank overdraft |  | 232,000 |  |
| Unexpired sundry expenses |  | 4,000 |  |
| Rent outstanding (W5) |  | 24,000 | 368,000 |
| TOTAL EQUITY \& LIABILITIES |  |  | 1,797,400 |

## Workings



W2
Purchases Control Account


W4 Depreciation of motor vehicle
$96,000+144,000=240,000$
$240,000 \times 25 \%=45,000$
W5 Rent $\quad 12,000 \times 12=144,000$
3 months $144,000 \times 3 / 12=36,000$
9 months $\quad 144,000 \times 9 / 12=108,000$
Rent outstanding $\quad 144,000$ Less $\quad 120,000$
$\underline{\underline{24,000}}$
W6 Additional capital

$$
144,000+96,000=240,000
$$

## QUESTION TWO (JUNE 1995 Q.5)

A) Purposes for which control accounts are prepared in business organizations
i. To be able to ascertain both creditors and debtors balance which are to be accounted for in the balance sheet.
ii. To detect errors and frauds committed in the preparation of debtors and creditors accounts in the ledger
iii. To obtain the credit purchases and sales in cases of single entries i.e. incomplete records
iv. To provide an internal check where clerical work of recording is done by different persons

## B) XML LTD

SALES LEDGER CONTROL ACCOUNT

|  | SHS |  | SHS |
| :--- | ---: | :--- | ---: |
| Balance b/d | $6,185,000$ | Balance b/d | 52,500 |
| Credit sales | $8,452,000$ | Returns inwards | 203,500 |
| Bills receivable dishonoured | 88,500 | Bills receivable | 615,000 |
|  |  | Cheques received | $7,985,000$ |
|  |  | Cash received | 153,000 |
|  | Bad debts written off | 64,500 |  |
|  | Discount allowed | 302,000 |  |
|  | Balance c/d | $\underline{5,394,000}$ |  |
|  | $\underline{14,769,500}$ |  | $\underline{14,769,500}$ |

## PURCHASES LEDGER CONTROL ACCOUNT

|  | SHS |  | SHS |
| :--- | ---: | :--- | ---: |
| Balance b/d | 16,500 | Balance b/d | $4,285,000$ |
| Returns outwards | 284,000 | Credit purchases | $5,687,500$ |
| Bills payable | 930,000 | Bills dishonoured | 400,000 |
| Cheques paid | $4,732,000$ | Charges on bills dishonoured | 10,000 |
| Cash paid to supplier | 88,500 |  |  |
| Bal c/d | $\underline{4,354,500}$ | $\underline{10,405,500}$ | $\underline{10,405,500}$ |

## QUESTION THREE (NOVEMBER 98 Q.3)

TAMA TRADERS CO LTD
UPDATED CASH BOOK

|  | SHS |  | SHS |
| :--- | ---: | ---: | ---: |
| Direct deposit | 254,500 | Bank overdraft | $5,324,000$ |
|  |  | Bank charges | 12,450 |
|  |  | Interest on overdraft | 135,480 |
|  |  | Insurance | 35,485 |
| Bal c/d | Standing orders | 138,000 |  |
|  | $\underline{631,315}$ | Payment undercast | $\underline{32,000}$ |
|  | $\underline{885,815}$ |  | $\underline{885,815}$ |

TAMA TRADERS CO LTD
BANK RECONCILIATION STATEMENT
Updated cashbook balance
Add: unpresented cheques
Debit error (W1)
Less: Uncredited cheques
Debit error
Balance as per bank statement

| SHS | SHS |
| ---: | ---: |
| 745,964 | $6 \$ 1,315$ |
| 27,000 |  |
| $(354,890)$ | 772,964 |
| $\underline{(27,500)}$ | $\underline{(382,390)}$ |
|  | $\underline{240,741}$ |

## Workings

W1 Bank error
Cheque 74,500
Less $\quad \underline{47,500}$
27,000
QUESTION FOUR (NOVEMBER 1998 Q.4)

|  |  |  | SHS |  |  |
| :--- | :--- | :--- | :--- | :--- | :--- |
|  |  |  |  |  |  |
| 1.6 .94 | $\rightarrow$ | KA 620 | $\rightarrow$ | $4,536,000$ |  |
| 3.4 .95 | $\rightarrow$ | KA 735 | $\rightarrow$ | $2,740,000$ |  |
| 3.6 .97 | $\rightarrow$ | KA 620 | $\rightarrow$ | Disposed | (Proceeds $\rightarrow 1,350,000$ ) |
| 5.1 .98 | $\rightarrow$ | KB 327 | $\rightarrow$ | $3,780,000$ |  |

MOTOR VEHICLES ACCOUNT

|  | SHS |  | SHS |
| :---: | :---: | :---: | :---: |
| 1994 |  | 1994 |  |
| Bank - KA 620 | 4,536,000 | Bal c/d | 4,536,000 |
| 1995 |  | 1995 |  |
| Bal b/d | 4,536,000 |  |  |
| KA 735 | 2,740,000 | Bal c/d | 7,276,000 |
|  | 7,276,000 |  | 7,276,000 |
| 1996 |  | 1996 |  |
| Bal b/d | 7,276,000 | Bal c/d | 7,276,000 |
| 1997 | 7,276,000 | 1997 |  |
| Bal b/d |  | Disposal KA 620 | 4,536,000 |
|  |  | Bal c/d | 2,740,000 |
|  | 7,276,000 |  | 7,276,000 |
| 1998 |  | 1998 |  |
| Bal b/d | 2,740,000 |  |  |
| Bank-327 | 3,780,000 | Bal c/d | 6,520,000 |
|  | 6,520,000 |  | 6,520,000 |



## QUESTION FIVE (NOV 96 Q.5)

## EXPLANATORY NOTES

## ON A) MATERIALITY

In accordance to the International Accounting Standards Framework (IASF), it is a qualitative characteristic of financial statements. As such it makes the information provided in financial statements useful to its users.
Information is material if is omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size of the item or error judged in the particular circumstance of its omission or misstatement. Thus materiality provides a threshold or cut off point rather than being a primary qualitative characteristic which information must have if it is to be useful. It therefore affects the relevance of information.

## B) PRUDENCE

Prudence can be defined as the inclusion of a degree of caution in the exercise of the judgments needed in making the estimates required under the conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated. However, the exercise of prudence does not allow, for example the creation of hidden reserves or excessive provisions, the deliberate understatement of assets or income or the deliberate overstatement of liabilities or expenses because the financial statements would not be neutral and therefore not have the quality of reliability.
Prudence is a fundamental concept of accounting in which reasonable estimates should be made to ensure that the profits shown in the income statement is realistic.

## C) CONSISTENCY

This is one of the fundamental accounting concepts. This refers to the convention that when a firm has once fixed a method for the accounting treatment of an item, it will enter all similar items that follow in exactly the same way.
However, a firm can change the method used, but such a change is not made without a lot of consideration. When such a change occurs and the profits calculated in that year are affected by a material amount, then either in the profit and loss account itself or in one of the reports with it, the effect of the change should be stated.

## REVISION PAPER FOUR

QUESTION ONE (JUNE 1998 Q.1)
MAPEMA TRADERS
TRADING, PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 ${ }^{\text {ST }}$ MARCH 1998

|  | SHS"000 | SHS"000 |
| :---: | :---: | :---: |
| Sales |  | 144,000 |
| Less; Cost of sales |  |  |
| Opening stock | 12,600 |  |
| Add; Purchases | 126,600 |  |
| Less; Returns outwards | $(2,400)$ |  |
| Less; Closing stock (W1) | $(21,600)$ | $(115,200)$ |
| Gross profit |  | 28,800 |
| Provision for doubtful debts (W2) |  | 75 |
| Discount received |  | 390 |
|  |  | 29,265 |
| Less: Expenses |  |  |
| Bad debts | 600 |  |
| Depreciation (W3) |  |  |
| Freehold buildings | 300 |  |
| Fixtures and fittings | 1,920 |  |
| Establishment expenses w/o (W4) | 3,780 |  |
| Administration expenses (W5) | 1,890 |  |
| Interest on loan (W6) | 240 |  |
| Selling and distribution expenses | 5,010 |  |
| Discount allowed | $\underline{150}$ | $(13,890)$ |
| Net profit |  | 15,775 |
| Profit b/d |  | 10,860 |
|  |  | 26,235 |
| Less: Provision dividend on preference shares (W7) |  | (300) |
| Provision dividend on ordinary shares (W8) |  | $(1,800)$ |
| Transfer to general reserve |  | (7,500) |
|  |  | $\frac{(9,600)}{16,635}$ |
| Retained profit |  | 16,635 |

## MAPEMA TRADERS

## BALANCE SHEET

AS AT 31 ${ }^{\text {ST }}$ MARCH 1998

| NON CURRENT ASSETS | $\begin{array}{r} \text { SHS } \\ \mathrm{COST} \end{array}$ | SHS DEPRN | $\begin{aligned} & \hline \text { SHS } \\ & \text { NBV } \end{aligned}$ |
| :---: | :---: | :---: | :---: |
| Freehold buildings | 15,000 | 1,800 | 13,200 |
| Fixtures and fittings | 19,200 | $\underline{9,600}$ | $\underline{9,600}$ |
|  | 34,200 | 11,400 | 22,800 |
| Goodwill |  |  | 4,800 |
|  |  |  | 27,600 |
| CURRENT ASSETS |  |  |  |
| Stock |  | 21,600 |  |
| Debtors | 9,300 |  |  |
| Less; Provision for doubtful debts | (465) | 8,835 | 30,435 |
| TOTAL ASSETS |  |  | 58,035 |
| EQUITY \& LIABILITIES CAPITAL \& RESERVES |  |  |  |
| Ordinary shares sh 10 each |  |  | 18,000 |
| 10\% preference shares sh 10 each |  |  | 3,000 |
| Share premium |  |  | 2,400 |
| General reserve |  |  | 7,500 |
| Retained profit |  |  | 16,635 |
|  |  |  | 47,535 |
| NON-CURRENT LIABILITIES |  |  |  |
| $8 \%$ loan stock |  |  | 3,000 |
| CURRENT LIABILITIES |  |  |  |
| Creditors |  | 4,440 |  |
| Provision for preference share dividend |  | 300 |  |
| Provision for ordinary share dividend |  | 1,800 |  |
| Accrued administrative expenses |  | 210 |  |
| Bank overdraft |  | 750 | -7,500 |
| TOTAL EQUITY \& LIABILITIES |  |  | 58,035 |

## Workings

W1 Computation of closing stock \& gross profit

Gross profit $=20 / 100 \times 144,000=28,800$

Closing stock $=136,800-115,200$

$$
=21,600
$$

W2 Provision for doubtful debts

$$
\begin{aligned}
\text { Debtors } & =9900-600 \\
& =9300 \\
5 \% & \times 9300=465
\end{aligned}
$$

## Provision for doubtful debts a/c

|  | SHS |  | SHS |
| :--- | ---: | :---: | :---: |
| Profit \& loss | 75 | Bal b/d | 540 |
| Balance c/d | $\underline{465}$ |  | $\underline{540}$ |

W3 Depreciation
Freehold buildings $=2 \% \times 15,000=300$
Fixtures and fittings $=10 \% \times 19,200=1,920$

## QUESTION TWO (JUNE 1998 Q.2)

a) Explanation of Prime cost \& Factory cost as used in manufacturing firms

## Prime cost

This is the total direct cost i.e. the cost of direct materials and direct expenses. Direct expenses include direct wages and royalties. These are the costs which can be directly traced to the materials produced.

## Factory cost

This is the total of prime cost and factory overheads. This factory overheads include all indirect expenses which cannot be directly traced to the materials produced.
b) RONO LTD MANUFACTURING

ACCOUNT
FOR THE YEAR ENDED 31ST DEC 1997

|  | SHS | SHS |
| :---: | :---: | :---: |
| Factory cost |  | 700,000 |
| Opening stock - Raw material | 23,280 |  |
| Add purchases, raw materials | 269,000 |  |
| Add carriage on raw materials | 82,400 |  |
| Less closing stock, raw materials | $(32,560)$ |  |
| Cost of raw materials consumed | 342,120 |  |
| Add: Direct expenses |  |  |
| Direct wages | $\underline{185,400}$ |  |
| PRIME COST | 527,520 |  |
| FACTORY EXPENSES |  |  |
| Rent \& rates | 76,800 |  |
| Power | 34,400 |  |
| Insurance | 31,280 |  |
| Deposit on plant | 30,000 |  |
| Factory cost | 700,000 | 700,000 |
| RONO LTD |  |  |
| TRADING ACCOUNT |  |  |
| FOR THE YEAR ENDED 31 ${ }^{\text {ST }}$ DEC 1997 |  |  |
|  | SHS | SHS |
| Sales (W1) |  | 1,140,000 |
| Less: Cost of sales |  |  |
| Opening stock of finished goods (W2) | 21,000 |  |
| Factory cost | 700,000 |  |
| Less; Closing stock of finished goods (W5) | $(56,000)$ | 665,000 |
| Gross profit |  | 475,000 |

## Workings

W1 Sales

$$
\begin{array}{ll}
\text { Total units sold } \\
\text { Selling price per unit } & \begin{array}{r}
190,000 \\
\\
\cline { 2 - 3 } \\
\hline 1,140,000
\end{array}
\end{array}
$$

W2 Opening stock of finished goods

$$
\text { Cost per unit }=\frac{700,000}{200,000}=\operatorname{sh} 3.5
$$

Opening stock $=6,000 \times 3.5=\operatorname{sh} 210,000$
W3 Closing stock of finished goods

|  | Units |
| :--- | ---: |
| Opening stock | 6,000 |
| Add; units produced | 200,000 |
| Less units sold | $\underline{(190,000)}$ |
| Closing stock | 16,000 |
| Value | $\mathbf{x} 3.5$ |
|  | $\underline{56,000}$ |

## QUESTION THREE

## Sabuni Manufacturing Account For the year ended 30 June 2002

|  | Dept 1 | Dept 2 | Total |
| :---: | :---: | :---: | :---: |
|  | Sh | Sh | Sh |
| Opening Stock of Raw Mat |  |  | 120,000.00 |
| Purchases of raw materials |  |  | 1,240,000.00 |
|  |  |  | 1,360,000.00 |
| Less closing Stock of RM |  |  | (160,000.00) |
| Cost of raw materials used | 627,720.00 | 572,280.00 | 1,200,000.00 |
| Manufacturing wages | 160,000.00 | 240,000.00 | 400,000.00 |
| Prime Cost | 787,720.00 | 812,280.00 | 1,600,000.00 |
| Factory Overheads |  |  |  |
| Manufacturing expense | 260,960.00 | 391,440.00 | 652,400.00 |
| Depreciation | 30,720.00 | 46,080.00 | 76,800.00 |
| Total Cost of Production | 1,079,400.00 | 1,249,800.00 | 2,329,200.00 |
| Add Opening Work in Progress | 12,600.00 | 18,200.00 | 30,800.00 |
| Less closing work in Progress | (12,000.00) | $(20,000.00)$ | (32,000.00) |
| Cost of Goods Produced | 1,080,000.00 | 1,248,000.00 | 2,328,000.00 |

## Sabuni Trading profit and loss account For the year ended 30 June 2002

Sh.
Sales
Less Cost of sales
Opening Stock
Cost of Goods Produced

|  | $1,230,000.00$ |
| :--- | ---: |
| Less Closing Stock | $(400,000.00)$ |
| Cost of Sales | $830,000.00$ |
| Gross Profit | $370,000.00$ |

Less Expenses

| Administration expense |  |
| :--- | ---: |
| $\quad$ General | $159,600.00$ |
| $\quad$ Depreciation | $2,400.00$ |
| Distribution |  |
| $\quad$ General | $103,600.00$ |
| Depreciation | $3,200.00$ |
| Bad Debts \& Provision | $1,200.00$ |
| Total Expenses | $270,000.00$ |
| Profit before tax | $100,000.00$ |

Less Corporation tax Profit after tax

## Cleansers

## Lotions

1,200,000.00

$$
\begin{array}{r}
422,000.00 \\
808,000.00 \\
1,230,000.00 \\
(400,000.00) \\
830,000.00 \\
370,000.00
\end{array}
$$

Sh.
$618,000.00$
$1,520,000.00$
$2,138,000.00$
$(700,000.00)$
$1,438,000.00$
$962,000.00$

$$
2,400,000.00
$$

## Total

Sh.
3,600,000.00

$$
\begin{gathered}
1,040,000.00 \\
2,328,000.00 \\
3,368,000.00 \\
(1,100,000.00) \\
2,268,000.00 \\
1,332,000.00
\end{gathered}
$$

(160,000.00)
200,000.00
Less Dividends:
Interim Dividend paid: Preference
Ordinary
Final Proposed Ordinary
Retained Profit for the year
Retained Profit b/f
Retained Profit c/f

20,000.00
50,000.00
(170,000.00)
30,000.00
470,000.00
500,000.00
b) Sabuni Ltd

Balance Sheet as at 30 June 2002

|  | $\begin{array}{c}\text { Sh. } \\ \text { Non Current Assets } \\ \\ \text { Furrent Assets }\end{array}$ | $\begin{array}{c}\text { Sh. } \\ (400,000.00)\end{array}$ | $\begin{array}{c}\text { Sh. } \\ \text { Finished goods }\end{array}$ |
| :--- | ---: | ---: | ---: |
| Stocks: Raw materials | $160,000.000 .00$ |  |  |$)$

## Workings: <br> Depreciation Charge

| Opening non current assets <br> Purchases during year | (920,000 x 10\%) |  | 92,000.00 |
| :---: | :---: | :---: | :---: |
|  | ( $80,000 \times 10 \% \times 0.5$ ) |  | 4,000.00 |
|  |  |  | 96,000.00 |
|  | Manufacturing | 76,800.00 |  |
|  | Administration | 9,600.00 |  |
|  | Distribution | 9,600.00 | 96,000.00 |
| Manufacturing ( 76,800 ) | Department | 1 | 5,504.00 |
|  | (160,000/400,000) |  | 46,080.00 |
| Apportionment | Department | 2 |  |
| Department 1 | (240,000/400,000) |  |  |
| Soaps |  | 600,000.00 |  |
| Lotions |  | 480,000.00 |  |
|  | (5/9 x 1,080,000) | 1,080,000.00 |  |
| Department 2 | (4/9 x 1,080,000) |  |  |
| Soaps |  | 208,000.00 |  |
| Lotions |  | 1,040,000.00 |  |
|  | (1/6 x 1,248,000) | 1,248,000.00 |  |
| Administration expenses | ( $5 / 6 \times 1,248,000$ ) |  |  |
| Paid |  | 637,200.00 |  |
| Add Accrued |  | 3,000.00 |  |
|  |  | 640,200.00 |  |
| Less Prepaid |  | (1,800.00) |  |
|  |  | 638,400.00 |  |
| Apportion: |  |  |  |
| General expenses |  |  |  |
| Soaps |  |  | 159,600.00 |
| Lotions |  |  | 478,800.00 |
|  | ( $60,000 / 240,000 \times 638,400)$ |  | 638,400.00 |
| Depreciation: | (180,000/240,000 x 638,400) |  |  |
| Soaps |  |  | 2,400.00 |
| Lotions |  |  | 7,200.00 |
|  | (60,000/240,000 x 9,600) |  | 9,600.00 |
| Distribution expenses | (180,000/240,000 x 9,600) |  |  |
| General expenses |  |  |  |
| Soaps |  |  | 103,600.00 |
| Lotions |  |  | 207,200.00 |
|  | (1,200,000/3,600,000 x 310,800) |  | 310,800.00 |
| Depreciation | (2,400,000/3,600,000 x 310,800) |  |  |
| Soaps |  |  | 3,200.00 |
| Lotions |  |  | 6,400.00 |
|  | (1,200,000/3,600,000 x 9,600) |  | 9,600.00 |
|  | (2,400,000/3,600,000 $\times 9,600$ ) |  |  |

Provision for doubtful debts

|  | Sh. | Sh. |  |
| :--- | ---: | :--- | ---: |
| Debtors (bad debt) | $3,200.00$ | Balance b/d | $15,000.00$ |
| Balance c/d | $16,000.00$ | Profit and Loss | $3,500.00$ |
|  | $19,200.00$ |  | $19,200.00$ |


| Apportion | $1,200.00$ |
| :--- | :--- |
| Soaps $\quad(1,200,000 / 3,600,000 \times 3,600)$ | $2,400.00$ |
| Lotions $(2,400,000 / 3,600,000 \times 3,600)$ | $3,600.00$ |

## QUESTION FOUR (NOV 1996 Q.2)

## A (i)

BIDII RETAILERS

|  | Sales ledger control a/c | Sales ledger balance |
| :---: | :---: | :---: |
| Unadjusted balance | 550,885 | 549,385 |
| Set off | $(3,500)$ | $(3,500)$ |
| Error in recording invoice |  | 300 |
| Return inwards not recorded in sales ledger |  | $(1,500)$ |
| Cash receipt understated | (500) | (500) |
| Error in writing off bad debts | 1,000 | 1,000 |
|  | 547,885 | 547,885 |


| (ii) |  |  |
| :--- | ---: | ---: |
|  | Purchases ledger <br> control a/c | Purchases ledger <br> balances |
| Unadjusted balance | 391,330 | 383,330 |
| Set off | $(3,500)$ | $(3,500)$ |
| Cash paid after set off | $(500)$ | $(500)$ |
| Error in recording invoice |  | 3,000 |
| Error in purchases journal | $(990)$ | $(990)$ |
| Purchases journal overcast | $\underline{(5,000)}$ | $\underline{381,340}$ |

(iii)

Suspense account

| Suspense account |  |  | SHS |
| :--- | ---: | ---: | ---: |
|  | 11,550 | Bank | 12,000 |
| Bal b/d | $\underline{450}$ |  | $\underline{12,000}$ |
| Error | $\underline{12,000}$ | $\underline{120}$ |  |

b.

Sales ledger control account

|  | SHS |  | SHS |
| :--- | ---: | ---: | ---: |
| Balance b/d | 550,885 | Set off | 3,500 |
| Error | 1,000 | Error | 500 |
|  |  | Balance c/d | $\underline{547,885}$ |
|  | $\underline{551,885}$ |  | $\underline{551,885}$ |

Purchases ledger control account

|  | SHS |  | SHS |
| :--- | ---: | ---: | ---: |
| Set off | 3,500 | Balance b/d | 391,330 |
| Payment | 500 |  |  |
| Error in purchases journal | 990 |  |  |
| Overcast in purchases journal | 5,000 |  | $\underline{381,340}$ |
| Balance c/d | $\underline{391,330}$ | $\underline{391,330}$ |  |

## Working

Note 10 affects only profit and loss account
10) Dr Profit and loss account 2,500

Cr Provision for bad debts 2,500
Dr Provision for bad debts 3,500
Cr Profit and loss account
3,500

## QUESTION FIVE (JUNE 1995 Q.5)

## Principle distinctions between partnerships and limited companies <br> PARTNERSHIPS <br> LIMITED COMPANIES

1. A relationship that subsists between 2-20 members with a view of profit
2. Capital raised by partners in accordance to partnership deed or if non existent then in accordance to Partnership Act
3. Managed by partners
4. Share profits in accordance with the Partnership deed
5. Not mandatory to have their accounts credited
6. Commence business upon receipt of certificate of registration
7. There is interest on capital, drawings, provisions of salary and commission to partners
8. The partners are taxed individually using graduated scale
9. Death, insanity will dissolve the partnership
10. Members can be sued through the name of the business
11. Keeping of books of accounts is optional

A legal entity formed by shareholders and registered under the Company"s Act

Capital raised by issue of shares to the shareholders and should not exceed the authorized share capital without the consent of the registrar of companies

Managed by a board of directors
The sharing of profit is in accordance to the voting power of members and is known as dividend

Mandatory to have their accounts audited
Commence business after receipt of certificate of registration and certificate of incorporation

Does not exist

The company is taxed using the corporation tax rate

Death, insanity does not dissolve a company, its only through legal process called liquidation

Being a legal entity a company can be sued rather than members

Keeping of books of accounts is mandatory

## REVISION PAPER FIVE

## QUESTION ONE

a) Accounting standards are authoritative statements of how particular types of transactions and events should be reflected in financial statements. They are developed to achieve comparability of financial information between and among different organizations.

Reasons why Standards are issued:
i) Reduce or eliminate different methods of preparing financial statements.
ii) Improve the quality of reporting financial information as they provide a base for discussions and debate by interested parties.
iii) To make companies disclose more information that is relevant to users.
iv) To promote objectivity in reporting financial information.
b) Revenue Realization: Revenue and profits are recognized when realized. The concept states that revenue and profits are not anticipated but are recognized by inclusion in the income statement only when realized in the form of either cash or of other assets the ultimate cash realization of which can be assessed with reasonable certainty. This concept eliminates the overstatement of profit as income that has been received or is receivable is reported. E.g. profit on cash sale is reported in the accounts but if a customer makes an order then until the customer receives an invoice and acknowledges liability.
c)

1) The full amount of Sh. 1.5 million is reported as sale in the accounts as the net credit sale falls within the definition of revenue as per revenue realization principle. Three fourth of the cash has been received (cash) and the balance is a debtor (a quarter). A Provision for doubtful debt should be made at $3 \%$ of the debtors in the same financial period.
2) This is an amount received for goods to be supplied in the future. This should be carried forward as a liability until the equipment is supplied to the customer then it is transferred to the P \& L in the next financial period.
d)
3) IAS 2 on Inventories requires that inventories should be shown at the lower of cost or Net realizable value. Therefore replacement cost method of valuing stock is not allowed. The firm should determine the net realizable is (selling price less expenses to complete sale) and compare it with the cost of Sh.890,000 and pick whichever is lowest.
4) This is not correct because in accounting we state the cost at which the transaction took place and any savings made on acquisition of assets are not shown at all. The machine should be shown at $\operatorname{Sh} 1,600,000$ and the saving of 300,000 is ignored. Revenue is also reported when realised in form of either cash or another asset.

## QUESTION TWO

a) Accounting standards are authoritative statements of how particular types of transactions and events should be reflected in financial statements. They are developed to achieve comparability of financial information between and among different organizations.

Reasons why Standards are issued:
a. Reduce or eliminate different methods of preparing financial statements.
b. Improve the quality of reporting financial information as they provide a base for discussions and debate by interested parties.
c. To make companies disclose more information that is relevant to users.
d. To promote objectivity in reporting financial information.
b) Revenue Realization: Revenue and profits are recognized when realized. The concept states that revenue and profits are not anticipated but are recognized by inclusion in the income statement only when realized in the form of either cash or of other assets the ultimate cash realization of which can be assessed with reasonable certainty. This concept eliminates the overstatement of profit as income that has been received or is receivable is reported. E.g. profit on cash sale is reported in the accounts but if a customer makes an order then until the customer receives an invoice and acknowledges liability.
c)
a) The full amount of Sh.1.5 million is reported as sale in the accounts as the net credit sale falls within the definition of revenue as per revenue realization principle. Three fourth of the cash has been received (cash) and the balance is a debtor (a quarter). A Provision for doubtful debt should be made at $3 \%$ of the debtors in the same financial period.
b) This is an amount received for goods to be supplied in the future. This should be carried forward as a liability until the equipment is supplied to the customer then it is transferred to the $\mathrm{P} \& \mathrm{~L}$ in the next financial period.
d)

1) IAS 2 on Inventories requires that inventories should be shown at the lower of cost or Net realizable value. Therefore replacement cost method of valuing stock is not allowed. The firm should determine the net realizable is (selling price less expenses to complete sale) and compare it with the cost of $\mathrm{Sh} .890,000$ and pick whichever is lowest.
This is not correct because in accounting we state the cost at which the transaction took place and any savings made on acquisition of assets are not shown at all. The machine should be shown at Sh 1,600,000 and the saving of 300,000 is ignored. Revenue is also reported when realised in form of either cash or another asset.

QUESTION THREE (DEC 1995 Q.3)
JACKSON NDAMBUKI TRADERS
TRADING, PROFIT \& LOSS ACCOUNT
FOR YEAR ENDED 30 ${ }^{\text {TH }}$ JUNE 1995
Sales (W3)
Less; Cost of sales
Opening stock
Add; Purchases (W2)
Less; Closing stock
Gross profit
Discount received

Less: Expenses
Discounts allowed
Depreciation; Bank (W4)
Furniture
Increase in provision for doubtful debt (W5)
General expenses
Wages
Net profit

| SHS | SHS |
| ---: | ---: |
|  |  |
| 42,500 |  |
| 81,250 |  |
| $(47,500)$ | $(76,250)$ |
|  | 176,250 |
|  | 7,500 |
|  | 183,750 |
|  |  |
| 15,000 |  |
| 5,000 |  |
| 175 |  |
| 11,000 |  |
| 25,000 |  |
| 38,750 | $\underline{88,825}$ |
|  |  |

JACKSON NDAMBUKI TRADERS
BALANCE SHEET
AS AT 30TH JUNE 1995

## Workings <br> W1

Cashbook a/c

|  | SHS |  | SHS |
| :--- | ---: | :--- | ---: |
| Receipts | 150,000 | Bal b/d | 18,500 |
| Capital | 12,500 | Payment | 62,500 |
|  |  | General expenses | 25,000 |
|  |  | Wages | 38,750 |
|  |  | Drawings | 7,500 |
|  | Bal c/d | $\underline{10,250}$ |  |
|  | $\underline{162,500}$ |  | $\underline{162,500}$ |

W2
Purchases ledger control a/c

|  | SHS |  | SHS |
| :---: | :---: | :---: | :---: |
| Payments | 62,500 | Bal b/d | 37,500 |
| Discounts received | 7,500 | Credit purchases | 811,250 |
| Bal c/d | 48,750 |  |  |
|  | 118,750 |  | $\underline{118,750}$ |
| W3 |  |  |  |
| Sales ledger control a/c |  |  |  |
|  | SHS |  | SHS |
| Bal b/d | 132,500 | Discount allowed | 15,000 |
| Sales | 252,500 | Receipts | 150,000 |
|  |  | Bal c/d | 220,000 |
|  | 385,000 |  | 385,000 |

W4
Depreciation
Plant $10 \%$ x $50,000=5,000$
Furniture $5 \% \times 3,500=175$

## W5

Provision for doubtful debt
$5 \% \times 220,000=11,000$

## QUESTION FOUR (NOV 1994 Q.4)

JOURNAL
Dr. Bad debts a/c
Dr Bad debts recovered a/c
Cr Profit \& loss a/c
CrBad debts recovered a/c
(Being bad debts recovered not entered)
Dr. Profit and loss a/c
Dr. Insurance (Debtor a/c)
Cr. Stock
(Being stock destroyed not entered as a debtor from insurance)
Dr Purchase a/c
Cr. Suspense a/c
(Being discount received wrongly entered in purchases)
Dr. Debtor"s a/c
Cr. Stock a/c
Cr. Profit \& loss a/c
(Being car held by a representer for salt who is our debtor)
Dr. Purchases a/c
Dr. Stock a/c
Cr. Cash a/c
Cr. Suspense a/c
(Goods purchased not entered in the books and not included in the closing stock)

Dr Advertising a/c
Cr. Profit \& loss a/c
(Being advertising campaign wrongly entered in the current year)
Dr. Suspense a/c
Cr. Profit \& loss a/c
(Being payment of insurance premiums for the coming year entered in the current year non corrected)


## B (i) CORRECTED GROSS PROFIT

|  | SHS | SHS |
| :--- | ---: | ---: |
| Reported gross profit | $9,000,000$ |  |
| Add: Insurance compensation | $3,500,000$ |  |
| $\quad$ Sales of cars | 600,000 |  |
| Closing stock omitted | 300,000 |  |
|  |  |  |
| Less: | 450,000 |  |
| Stock | 52,500 |  |
| Purchases | 450,000 | $(535,200)$ |
| $\quad$ Car transferred to the representative |  | $\underline{3,864,800}$ |

## (ii) CORRECTED NET PROFIT

Reported Net profit
Add: Bad debt leased from profit
" recovered as income
Loss on Burglary of stock leased
Advertising
Insurance premium

Less : Actual loss on stock after insurance compensation
Depreciation on car

| SHS | SHS |
| ---: | ---: |
| 75,000 |  |
| 75,000 | $2,250,000$ |
| $5,000,000$ |  |
| $1,250,000$ |  |
| 150,000 |  |
| $1,150,000$ |  |
| 112,500 | $\underline{(1,612,500)}$ |
|  | $\underline{7,187,000}$ |

## QUESTION FIVE (JUNE 1996 Q.4)

## a. Four types of errors not disclosed by the trial balance

## i) ERROR OF COMMISSION

This is an error in which the accountant records a transaction in the correct class of account, in the correct side but in the wrong name of the account.
For example, a sale of goods on credit to Gatura was recorded by debiting Gatura"s account.
ii) ERROR OF PRINCIPLE

This is an error committed due to lack of accounting principles. That is, a transaction is recorded in the wrong class of account, e.g. if a fixed asset such as motor van is debited to an expense account such as motor vehicle expenses account.
iii) ERROR OF COMPLETE REVERSAL OF ENTRIES

This is where the correct accounts are used to record a transaction but each item is shown on the wrong side of the account. For example, suppose we had paid a cheque to Ondieki for Shs 200, the double entry of which is Cr. Bank Shs 200, Dr. Ondieki Shs 200, Dr. Bank Shs 200. The trial balance totals will still agree.
iv) COMPENSATING ERRORS

This is an error that occur both on the debit side of an account and on the credit side of an account and the figures are equal which cancel each other.
E.g Sales account was undercast by Shs 20,000 and Purchase ledger was undercast with Shs 20,000 . The net effect is neutral and the trial balance will still balance.
v) ERROR OF ORIGINAL ENTRY

Where the original figure is incorrect, yet double entry is still observed using this incorrect figure. An instance of this could be where there were sales of Shs 150 goods but an error is made in calculating the sales invoice. If it were calculated as Shs 130 and Shs 130 and Shs 130 were credited as sales and debited to the personal account of the customer, the trial balance would still "balance".
vi) ERROR OF OMISSION

Where a transaction is completely omitted from the books, the trial balance will still agree.

## vii) TRANSPOSITION ERRORS

Where the wrong sequence of the individual characters within a number was entered e.g. 142 instead of 124 in both the debit and credit entries, the trial balance would still agree.

B a)
JOURNAL PROPER


| Suspense a/c |  |  | $\mathbf{S H S}$ |
| :--- | ---: | ---: | ---: |
|  | SHS |  | 7,520 |
| ABD bank | 10,000 | Difference in Trial balance | 1,000 |
| Closing stock | 1,500 | Discount allowed | $\underline{3,200}$ |
| Insurance prepaid | $\underline{220}$ | Opening stock | $\underline{11,720}$ |


[^0]:    Salaries

