MACHAKOS UNIVERSITY

University Examinations for 2016/2017 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING, BANKING AND FINANCE

FOURTH YEAR SECOND SEMESTER EXAMINATION FOR DEGREE IN

BACHELOR OF COMMERCE (ACCOUNTING OPTION)

BAC 411: TRUST AND EXECUTORSHIPS ACCOUNTS

DATE: 5/6/2017 **TIME: 8:30 – 10:30 AM**

INSTRUCTIONS:

Answer Question One and Any Other Two Questions

QUESTION ONE (COMPULSORY) (30MARKS)

(a) Distinguish between completely and incompletely constituted trusts.

(b) Explain the provisions of maintenance and advancement in a trustee.

(c) Explain the remedies available to a beneficiary in case of breach of a trust.

(d) Kiura and Maina are life tenants of a trust set up by their uncle. The trustees have investment powers restricted to those contained in the Trustee Act (Chapter 167 of the Laws of Kenya) except they could hold at their absolute discretion 300,000 shares of Sh.10 each in Kilimanjaro Enterprises Limited, a horticultural exporting company run by the uncle..

On 31 March 2002, the balance sheet of the trust was as follows:

	Sh.'000'	Sh.'000'
Fixed interest investment: Sh.2 million 10% Kenya stock 2007 (cost)	2,000	
9% Kenya stock 2006 (cost)	1,800	
Cash at bank	200	4,000
Wider range investments: 40,000 shares of Sh.100 in E.A. Breweries Ltd (cost)		4,000
Special range investment: 300,000 shares in Kilimanjaro Enterprises Ltd. (cost)		3,000
		11,000
Trust capital		4,000
Fixed interest fund		4,000
Wider range fund		3,000
Special Range fund		11,000

In the year to 31 March 2003, the following occurred:
2002 30 June, Interest for the year ended 30 June 2002 was received on 10% Kenya stock.

School fees for Kiura and Maina were paid immediately using the whole amount received.

30 September, a final dividend of 75% for the year ended 30 June 2002 was received from E.A. Breweries Ltd. (payout rate 10%).

30 September The E.A. Breweries Ltd. shares were sold at Sh.110 each. At the same time, a satisfactory buyer was found for the 300,000 shares in Kilimanjaro Enterprises Limited – these shares were sold for Sh.15 each. Some high yielding 12%Kenya stock 2008 was available at par on this date. It was decided to use all the wider range cash available to purchase this stock and designate it a wider range investment.

31 December, Interest was received for the year on the 9% Kenya stock and Sh.42,000 interest was received on the fixed interest cash at bank.

2003 28 February, 61,250 Sh.10 ordinary shares in ICDL Limited were purchased for Sh.40 per share using the fixed interest cash and a suitable switch was made to ensure adherence to the requirements of the Trustee Act. The market value of the 12% Kenya stock on this date was still par.

31 March All remaining income cash was paid across to the life tenants, after trust administration expenses of Sh.120,000 were paid for the year.

Required:

(i) Write up the trust cash account, the income account (showing payments to beneficiaries in this account) and the trust capital account for the year ended 31 March 2003.

(ii) Prepare the trust balance sheet as at 31 March 2003.

QUESTION TWO (20 MARKS)

a) Explain the defense available to a trustee in case of breach of trust.

b) Kamau died on 30 June 20X4, leaving a net estate of Shs.3,600,000 (after all legacies, duties, debts and other outgoings had been paid). By his will Kamau bequeathed the residue of his estate to his three sons, Maina, Njoroge and Karanja in equal shares; the will also contained a wider investment clause so that the provisions of the Trustee Act were not to be applied by the trustees of the estate.

At the date of Kamau's death all three residuary legatees were under 18 years of age, but Karanja (the eldest) became 18 on 31st March 20X6, when the trustees of Kamau's estate arranged to transfer to him his due share of the estate.

The following transactions affecting Kamau's estate, and the interests of his sons therein, occurred between 30 June 20X4 and 31 March 20X6:

Assets held in trust on capital account on 31 March 20X6:

	Shs
Shs.1,000,000 M Ltd 9% Debenture Stock at cost	830,000
Shs.1,500,000 N Ltd 10% Loan Stock at cost	1,480,000
Shs.1,800,000 O Ltd 6% Stock (as valued at 30 June 20X4)	1,100,000
Shs.300,000 P Ltd 6% Debenture Stock (as valued at	
30 June 20X4)	190,000
	3,600,000

Income received from investments:

On general fund:	Year to 30 June 20X5	300,000
	9 months to 31 March 20X6	270,000
On accumulations:	Year to 30 June 20X5	Nil
	9 months to 31 March 20X6	25,200

Payments made for infants' maintenance:

	Maina	Njoroge	Karanja
	Shs.	Shs.	Shs.
31 December 20X4	15,000	5,000	10,000
30 June 20X5	15,000	25,000	30,000
31 December 20X5	20,000	40,000	50,000

On 1 July 20X5 the trustees purchased the following stocks out of accumulated income:

	Cost
	Shs.
Shs.70,000 M Ltd 9% Debenture Stock	61,000
Shs.150,000 N Ltd 10% Loan Stock	149,000

It was agreed that Karanja's entitlement would be satisfied as follows:

From General Fund

a) One-third share of nominal values of N Ltd and O Ltd stocks.
b) Sufficient M Ltd stock to cover balance due.

From Accumulations Fund

c) All M Ltd stock held on fund.
d) Sufficient cash to cover balance due.

On 31 March 20X6 the prices of the stocks held in trust were as follows:

M Ltd 9% Debenture stock	86-88
N Ltd 10% Loan Stock	94-96
O Ltd 6% Stock	58-60
P Ltd 6% Debenture Stock	56-58

From the above information prepare:

a) The accumulations accounts (in columnar form) for the period from Kamau's death to 31 March 20X6 (which you may assume to be the date when the relevant distributions were made to Karanja);

b) Statements of distribution for:
1. The general fund; and
2. The accumulations fund;
Showing the items transferred to Karanja and the balances remaining in trust for Maina and Njoroge;

c) The trust balance sheet showing the position immediately after the distribution to Karanja.

QUESTION THREE (20 MARKS)

(a) Describe the following:

i) protective trusts.

ii) Implied trusts

iii) Constructive trusts .

(b) Mr. Ruare dies, leaving his two wives Lucky and Chity whom he married under a system of law which permits polygamy. A third wife Beaty had predeceased him. Lucky has three children Peter , Lowe and Ricci. Beaty had two children Short and Tall. Chity had no children.

All the children are alive at the time of Mr. Ruare's death. The value of his personal and household effects was Sh.350,000 and the value of the net intestate estate was Sh.3,150,000.

Required:

A statement showing how the estate of Mr. Ruare would devolve

(c) Lazarus Koech, who had two sons,Seroney and Kiptoo and two daughters, Esther and Sarah, died intestate on 31st January 1995, leaving a widow, emilly.

Saroney had died some years earlier leaving a son, John and a daughter Helen. Sarah had also predeceased her father leaving two sons, Ken and James.

During his lifetime, Koech had made the following cash gifts to his children and grandchildren:

	Sh.
Seroney	16,000
Kiptoo	60,000
Esther	20,000
Ken	10,000
James	12,000

The residue of the estate net of the advances and after distributing the chattels to the widow amounted to Sh.292,000. Emily died a year later after her husband.

Required: Prepare a statement showing the distribution of the estate on the death of Koech and also on the death of Emily, assuming that there had been no change on the value of the estate in the intervening period.

QUESTION FOUR (20MARKS)

a) Robin (aged 54) died in a road accident on 31 December 20X1. On 1 May 20X2 after his executors had paid all his debts, (except for the mortgage on his freehold house referred to below) testamentary and funeral expenses, his estate was ascertained as follows:

	Shs'000	**Shs'000**
Cash on bank accounts		8,500
Freehold house		6,500
Jaguar motor car		720
Mercedes motor car		1,260
Stamp collection		850
Debt due from William		120
Furniture and other personal effects		1,345
10,000 Ordinary Shs.10 shares in Kenya Breweries Limited		1,200
4,500 Ordinary Shs.10 shares in Nation Printers Limited		740

Shs.800,000 5% Kenya Stock		235
Income received to date:		
Bank interest	230	
Dividend from Nation Printers Limited	37	
	267	
Less: Mortgage interest paid 31 March 20X2	120	
		147

Extracts from Robin's will left bequests as follows:

(a) 'To my wife Annie, I leave my furniture and other personal effects and the residue of my estate, after payment of my debts and expenses.'
(b) 'To each of my sons, David, Jack and Stuart, Shs.1m.
(c) 'To my unmarried daughter, Clare, my freehold house subject to any mortgage thereon.' The house was subject to a mortgage of Shs.2m. carrying interest at 12% per annum payable 31 March and 30 September.
(d) 'To my friend Tony, whichever of the motor cars owned by me at the time of my death he may choose.'
(e) 'To my good friend Gerry Gangla, Shs.100,000.
(f) 'To my friend Ben, some of my furniture.'
(g) 'To my cousin Susan, my painting of the "Street Scene" by Renoir.'
(h) 'To my friend Dennis, Shs.200,000 on condition he gives up the bad habit of smoking.'
(i) 'To my brother Joseph, 1,000 shares in Brooke Bond(K) Ltd.'
(j) 'To my sister Elsie, Shs.600,000.'
(k) 'To my secretary Betty, half of my holdings of Ordinary Shs.10 shares in Kenya Breweries Ltd.'
(l) 'To my cousin Miriam, my holding of Shs.800,000 5 1/2% Kenya Stock and my holding of shares in Cassava Ltd.'
(m) 'To my chauffeur, Malcolm, Shs.300,000.
(n) 'To my gardener Jeremiah, Shs.150,000 if still in my employ at the death of my death.'
(o) 'To my friend Eric, my 6,000 Ordinary shares in Printers Ltd.'
(p) 'To my nephew Frank, 4,000 Ordinary Shs.10 shares from my holding of such shares in Kenya Breweries Ltd.'
(q) 'To my niece Tracey, Shs.200,000 payable out of my holding of Shs.10 Ordinary shares in Kenya Breweries Ltd.'
(r) 'To my friend Timothy, Shs.150,000.'
(s) 'To my cousin Hazel, the Shs.120,000 which William owes me.'
(t) 'To St. Peter's Church Shs.100,000 to provide a stained glass window in memory of my mother.'
(u) 'To my good friend Gangla Shs.150,000 for looking after my house for many years when I went on holiday.'

Robin's executors ascertained that the following beneficiaries were dead:

- Son Jack, died 1989, leaving a wife and two children.
- Son Stuart, died 1988, leaving a wife.
- Sister Elsie, died 20x6, leaving a husband and two daughters.
- Chauffeur Malcolm (aged 60) killed in the same accident as Robin. It was impossible to determine the order in which Robin and Malcolm died.

The executors also advise you that:

i. Tony elected to have the Mercedes car.

ii. Robin sold the Renoir painting in 1987 for Shs.3m.

iii. Dennis replied in a letter to the executors that he had no intention of giving up smoking.

iv. Robin owned no shares in Brooke Bond Ltd. The value of 1,000 shares in that company is Shs.330,000.

v. There is no such investment as 5 1/2% Kenya Stock. The reference in Robin's will to 5 1/2% is thought to be a typing error not previously noticed.

vi. Robin sold his shares in Cassava Ltd. using the proceeds of Shs.900,000 to purchase his shareholding in Kenya Breweries Ltd.

vii. The gardener Jeremiah retired in June 20X0.

viii. In early 1990, Printer Ltd. merged with Nation Ltd. to form a new company Nation Printers Ltd. and Robin received 4,500 new Ordinary shares in Nation Printers Ltd. in exchange for his 6,000 Ordinary shares in Printers Ltd.

ix. Timothy replied in a letter that he 'didn't' want anything from Robin's estate because actually he hated the sight of him.'

x. In 1989 Robin had paid Shs.125,000 for a stained glass window in St. Peter's church in memory of his mother.

xi. His daughter Clare had married in April 1989.

xii. Gerry Gangla claimed both legacies.

Required:

(a) A statement showing the distribution of Robin's estate on 1 May 20X2. (12 marks)

(b) A list of legacies to which the executors should not assent, briefly explaining the reason why the legacy is invalidated. (8 marks)

QUESTION FIVE (20 MARKS)

When both parents of Alice and Beatrice died in a car accident, their rich uncle set up a trust to provide for them until they married. They were to share income equally. When Alice and Beatrice married the capital was to pass equally to the children of his nephews and nieces.
The uncle directed the trustees to invest only in investments authorised by the Trustees Act (Cap.167 of the Laws of Kenya) except:

1. They could retain at their absolute discretion 10,000 shares of Sh.10 each in Updown Limited, a private company;
2. They would not recall a loan of Sh.1,200,000 to Alice, unless Alice wished to repay the whole or part of it; the loan was secured by a mortgage on Alice's leasehold house of which 15 years remain unexpired. After the trust had been in existence for 2 years, the balance sheet at 31 March 1996 was as follows:

Fixed interest investments	Sh. '000'	Sh. '000'
Sh.3 million 12% Kenya stock at cost		2,955
Cash at bank		45
Water range investments:		3,000
30,000 shares in BAT (K) Ltd.		
Special range investments:		3,000
15% mortgage loan to Alice		
10,000 shares of Sh.10 in Updown Ltd.	1,200	
Income cash	150	1,300
		72
Trust capital:		7,422
Fixed Interest Fund		
Wide Range Fund	3,000	
Special Range Fund	3,000	
Life Tenants' Accounts	1,350	7,350
Alice		
Beatrice	36	
	36	72
		7,422

Interest on the Kenya Stock was received on 30 June 1996 and 31 December 1996. The interest on the mortgage loan to Alice was due on 31 March each year. She had paid interest due on 31 March 1996, but negotiated with the trustees that she would not draw out any income from the trust in respect of the year 31 March 1997. Instead her share of the income would be used to pay the interest on the loan and to pay any repairs relating to the house; any balance remaining would be used to pay part of the loan.

The trust's other receipts and payments were as follows:

1996			Sh. '000'
April 15	Amount paid to life tenants		72
April 30	Dividend of 60% on the share of Updown Ltd. for the year ended 31 December 1995		
May 28	Amount paid for repair for Alice's house		24
June 29	Proceeds of sale of 30,000 shares in BAT (K) Ltd.	3,600	
July 5	Purchase of 36,000 Sh.10 ordinary shares inNation (Kenya) Ltd. a wider range investment.		3,600
September 15	Receipt of interim dividend of 30% on the shares in Nation (K) Ltd., for the year to 31 December 1996.		
December 14	Receipt of proceeds of sale 10,000 shares in Updown Ltd.		360
December 31	Purchase of Sh. 450,000 nominal of 12% Kenya Stock at 90		
1997			
January 20	Paid to Beatrice in respect of income		150
March 31	Paid out of income administration expenses for the year		60

Required

(a) Write up the trust cash account, the income account, the life tenants' account and the trust capital account for the year ended 31 March 1997.

(b) Prepare the trust balance sheet as at 31 March 1997.