MACHAKOS UNIVERSITY

University Examinations for 2016/2017 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF BUSINESS ENTREPRENEURSHIP AND MANAGEMENT SCIENCES

FOUTH YEAR SECOND SEMESTER EXAMINATION FOR DEGREE IN

BACHELOR OF COMMERCE (ACCOUNTING OPTION)

BAC 405: ACCOUNTING THEORY

DATE: 29/5/2017 **TIME: 8:30 – 10:30 AM**

INSTRUCTIONS:

Answer Question One and Any Other Two Questions

Question one (COMPULSORY) (30 MARKS)

(a) Distinguish between accounting theory and accounting standards. Is the former always likely to lead to and necessary to the development of the latter? (6 marks)

(b) The statement of A, B and C who are equal partners stood as follows on 31st march 2015.

Statement of financial position

capital accounts	**sh**		**Assets**	
A	82,500		Furniture	1,250
B	**55,000**		**In**vestments	25,000
C	(10000)	**127,**000	inventory	87,500
Account payables		55,000	account receivables	62,500
			Bank	6,250
		182,500		**182,500**

The firm was dissolved as on that date for the purpose of dissolution the investment were valued at sh 40,000 and stock at sh 70,000.B agreed to take over the investments and A to take over the inventory. A also took over the furniture at book value. The account receivable realized sh 59,000 and the account payables were paid of sh 53,500 in full satisfaction of their claims.

Assuming that c is insolvent and is unable to bring anything in respect of his debt to the firm, show the realization and capital accounts of all the partners the final adjustments being made in accordance with decision in Garners vs. Murray. (12 marks)

(c)H Holding ltd accrued 80% of s subsidiaries ltd shareholding on 1st January 2010 .The share capital of s stood at ksh 1,000,000 while its revenue reserves stood at ksh 600,000.H paid sh 1,500,000 for the purchase. The fair value of assets were equivalent to the book value at acquisition. On 31st December 2012 reserve of s stood at sh 800,000

Required:

compute: (i) Goodwill on computation

(ii) Minority interest as at 31st December 2012 (6 marks)

(c) Discuss the objectives of financial reporting. (6 marks)

QUESTION TWO (20 MARKS)

ABC company operates a branch at nakuru. The following information relates to Nakuru branch for the year ending 31st December 2015

Opening balance (1st January 2015.

	sh
Branch stock (at cost)	55,000
Branch debtors	40,000
Closing balances (31st December 2015)	
Branch stock (at cost)	70,000
Transaction for the year:	
Goods sent to the head office to branch (at cost)	600,000
Goods returned by branch to head office	15,000
Cash sales	250,000
Credit sales	700,000

Good stolen at branch	5,000
Cash stolen at branch	3,500
Returns from branch debtor (at selling price)	30,000
Cash received from branch debtor	630,000
Discount allowed	12,000
Bad debts written off	7,500
Expenses paid by head office	
Salaries	40,000
Rent and rates	25,000
General expenses	13,000

Required: Prepare the necessary accounts in the head office books for Nakuru branch for the year ending 31st December 2015) (14 marks)

b) Discuss the arguments for the need for an accounting theory. (6 marks)

QUESTION THREE (20 MARKS)

You are presented with the following summarized information for Norbreck plc and its subsidiary, Bispham Ltd:

Income statements for the year ending 30 September 2007

	Norbreck plc	Bispham Ltd
Revenue	1,700	450
Cost of sales	[920]	[75]
Gross profit	780	375
Administration expenses	[300]	[175]
Income from shares in group company	120	-
Profit before taxation	600	200
Taxation	[30]	[20]
Profit for the year	570	180

Balance sheets at 30th September 2007

	Norbreck plc	Bispham Ltd
Non-current tangible assets	1,280	440
Investments: shares in group company	400	_
	1,680	440
Current assets		
Inventory	300	250
Accounts receivable	280	150
Cash at bank and in hand	40	10
	620	410
Total assets	2,300	850
Current liabilities		
Trade accounts payable	[80]	[160]
Other payables, taxation and social security	[160]	[70]
-	[240]	[230]
Non-current liabilities		
Deferred taxation	[460]	[20]
Total liabilities	[700]	[250]
Net assets	1,600	600
Equity		
Called-up share capital [ordinary shares of 1 each]	900	400
Reserves [including retained profits]	700	200
	1,600	600

Additional information:

[a] Norbreck plc acquired 80% of the shares in Bispham Ltd on 1 October 2004. Bispham's retained profits balance as at that date was 10,000.

[b] During the year, Norbreck paid dividends of 360,000 and Bispham paid dividends of 150,000.

Required:

Prepare norbreck plc consolidated income statement for the year ending 30 September 2007 and a consolidated balance sheet as at that date. (20 marks)

QUESTION FOUR (20 MARKS)

(a) The qualitative characteristics underlying good accounting information can be divided into primary and secondary characteristic. **Discuss** (12 marks)

(b) Discuss the arguments **for** support and **against** the accounting standards. [8marks]

QUESTION FIVE (20 MARKS)

Total lady investment Ltd has three cash generating unit based in Mombasa road [M], Athriver [A] and Ruaraka [R] with carrying amount of Shs 400, Shs 500 and 600 respectively on 31 December 2OXO.

These carrying amounts do not include goodwill. Total lady investment Ltd is experiencing a lot of changes in both political and technological environment and conducts annually impairment tests of each of its cash generating unit.

The operations of M, A, R, are conducted at the headquarter which is situated in upper hill away from the city centre. The headquarter is composed headquarter building and an operation research centre with a carrying amount of Shs 1,500 and 3,000 respectively.

1. The expected remaining life of cash generating unit M is 5 years and that of A and R is 10 years. The headquarter is depreciated on a straight line method with a nil residual value.
2. The carrying of the research centre which cannot be allocated on a reasonable and consistent basis to the individual cash generating unit under review.
3. The recoverable amount of each cash generating unit is based on its value in use.
4. The discount rate is 20%
5. Ignore taxation.

Required

[a] i) Allocation of impairment loss to the cash-generating units

ii] Amount to be recognized income statement. (12 marks)

(b) What is meant by the going concern principle of accounting, how does it affect the valuation of asset? [8 marks]