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KIRIRI WOMENS' UNIVERSITY OF SCIENCE AND TECHNOLOGY

UNIVERSITY EXAMINATION, 2024/2025ACADEMIC YEAR
FIRST YEAR, FIRST SEMESTER EXAMINATION
MASTER IN BUSINESS ADMIISTRATION

Date: 16th April, 2024
Time: 2.00pm –5.00pm

KAC 3103 - FINANCIAL ACCOUNTING

INSTRUCTIONS TO CANDIDATES

ANSWER **QUESTION ONE (COMPULSORY)** AND **ANY OTHER THREE** QUESTIONS

QUESTION ONE (40 MARKS)

APPLE CASE STUDY ON APPLICATION OF ACCOUNTING CONCEPT

Twenty years ago, Apple released the first iMac. This was just the beginning of Apple's success, the next iTunes, then the iPod, and in 2007 the iPhone. The trend continued and grew as did their "iRevenues". During Apple's life, how consumers viewed technology drastically changed, and how accountants viewed technology also changed. In 2014, The Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) jointly updated the revenue recognition to include guidelines for contracts involving software. The new accounting standard update, FASB 606, focuses on all revenue from contracts with customers. The update was needed to clarify revenue recognition guidelines and help prevent accounting fraud.Revenues are inflows of assets or increases in value of an asset from normal operations, gains arise from discontinued operations. Recognizing revenue can be simple if it is a routine sale where the revenue would be recorded at the point of the sale.

Recognizing revenue can be very complicated though, which is why the boards updated the revenue recognition standard. This standard provides a five-step guideline for recognizing revenue in more complex situations. Apple's financial statements from the case disclosed their criteria for recognizing revenue, which roughly aligns with the five-step process. Therefore, it makes sense to read in Apple's 2017 the adoption of the new standard will not have a material impact. The new standard also addresses multiple-element contracts, which will affect Apple's software and licensing contracts. Now companies should recognize revenue from these contracts on a stand-alone selling price if they are distinctive performance obligations. This change is outlined in the fourth step of the recognition process, which highlights three methods; adjusted market assessment approach, expected cost plus margin approach, and residual approach. One benefit of the new revenue recognition standard, and these approaches, is how it standardizes accounting across industries.

Required:

a) In your own words, describe revenues and demonstrate how revenues are different from gains. (8 marks)

b) Describe the accounting treatment for revenues recognition and identify the specific accounts and financial statements that are affected by the process of revenue recognition. (8 marks)

c) Discuss the five-step process of revenue recognition as per the updated guidelines issued by the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB). (8 marks).

d) With relevant examples, explain the meaning of the realization concept showing how this is applied in revenue recognition. (8 marks)

e) Accounting ratios have been used by many companies as indicators of their financial performance in the present and even in the future. Discuss the four limitations associated with their use for this purpose by Apple. (8 marks)

QUESTION TWO (20 MARKS)

a) Briefly state the reasons why a company would not wish to distribute all its profits to its shareholders. (5 marks)

b) The following is the trial balance of Transit Ltd on 31 March 2018

	Sh.	Sh.
Issued share capital (ordinary shares of Sh. 1 each)		42,000
Leasehold properties, at cost	75,000	
Motor vans, at cost (used for distribution)	2,500	
Provision for depreciation on motor vans to 31 March 2017		1,000
Administration expenses	7,650	
Distribution expenses	10,000	
Stock, 31 March 2017	12,000	
Purchases	138,750	
Sales		206,500
Directors' remuneration (administrative)	25,000	
Rents receivable		3,600
Investments at cost	6,750	
Investment Income		340
7% Debentures		15,000
Debenture interest	1,050	
Bank interest	162	
Bank Overdraft		730
Debtors and creditors	31,000	24,100
Interim dividend paid	1,260	
Profit and loss account, 31 March 2017		17,852
	311,122	311,122

You ascertain the following:

1. All the motor vans were purchased on 1 April 2015. Depreciation has been and is to be, provided at the rate of 20% per annum on cost from the date of purchase to the date of sale. On 31 March 2018 one van, which had cost Sh. 900, was sold for Sh. 550, as part settlement of the price of Sh. 800 of a new van, but no entries about these transactions were made in the books.
2. The estimated corporation tax liability for the year to 31 March 2018 is Sh. 12,700.
3. It is proposed to pay a final dividend of 10% for the year to 31 March 2018.
4. Stock at the lower of cost or net realizable value on 31 March 2018 is Sh. 16,700.

Required:
Prepare, without taking into account the relevant statutory provisions:

i) The income statement for the year ended 31 March 2018. (8 marks)

ii) A statement of financial position as of that date. (7 marks)

QUESTION THREE (20 MARKS)

a) The aim of IAS 7 is to provide information to users of financial statements about the cash flows of an enterprise's ability to generate cash and cash equivalents. Explain why it is important to prepare a cash flow statement. (5 marks)

b) Mhasibu Limited's income statement for the year ended 31st December 2016 and statement of financial position as of 31st December 2015 and 31st December 2016 were as follows:

Income Statement for the period ended 31.12.2016

	Sh. '000'
Sales	30,650
Cost of sales	(26,000)
Gross profit	4,650
Depreciation	(450)
Administrative and selling expenses	(910)
Interest expense	(400)
Interest income	300
Dividend income	200
Foreign exchange loss	(40)
Net profit before taxation and extraordinary item	3,350
Extraordinary item – Insurance proceeds from earthquake disaster settlement	180
Net profit after extraordinary item	3,530
Income-tax	(300)
Net profit	3,230

Statement of Financial Position as of 31.12.2016

		2015 Sh. '000'		2016 Sh. '000'
Assets				
Cash on hand and balances with banks		200		25
Short-term investments		670		135
Sundry debtors		1,700		1,200
Interest receivable		100		–
Inventories		900		1,950
Long-term investments		2,500		2,500
Fixed assets at cost	2,180		1,910	
Accumulated depreciation	(1,450)		(1,060)	
Fixed assets (net)		730		850
Total assets		6,800		6,600
Liabilities				
Sundry creditors		150		1,890
Interest payable		230		100
Income taxes payable		400		1,000
Long-term debt		1,110		1,040
Total liabilities		1,890		4,030
Shareholder's Funds				
Share capital		1,500		1,250
Reserves		3,410		1,380
Total shareholders' funds		4,910		2,630
Total liabilities and shareholders' funds		6,800		6,600

The following additional information is also relevant for the preparation of the statement of cash flows (figures are in Sh.'000').

- An amount of 250 was raised from the issue of share capital and a further 250 was raised from long-term borrowings.
- Interest expense was 400 of which 170 was paid during the period. 100 relating to interest expense of the prior period was also paid during the period.
- Dividends paid were 1,200.
- Tax deducted at source on dividends received (included in the tax expense of 300 for the year) amounted to 40.
- During the period, the enterprise acquired fixed assets for 350. The payment was made in cash.
- A plant with the original cost of 80 and accumulated depreciation of 60 was sold for 20.
- Foreign exchange loss of 40 represents the reduction in the carrying amount of short-term investment in foreign-currency designated bonds arising out of a change in the exchange rate between the date of acquisition of the investment and the balance sheet date.
- Sundry debtors and sundry creditors include amounts relating to credit sales and credit purchases only.

Required:

Compute the following:

i) The net cash from operating activities using the indirect method. (8 marks)

ii) The cash and cash equivalents for the year ended 31st December 2016. (7 marks)

QUESTION FOUR (20 MARKS)

a) Explain any FOUR errors not detected in the trial balance. (8 marks)

b) The following information has been extracted from the accounts of Madaraka Investments Ltd. for the year ended 31 December 2018. Comparable figures for the previous year are also shown.

	Cost	Dec.	2017 Net Book Value	Cost	Dec.	2018 Net Book Value
	Sh. '000'	Sh. '000'	Sh. '000'	Sh. '000'	Sh. '000'	Sh. '000'
Plant	200	80	120	220	100	120
Building	1,000	200	800	1,800	220	1,580
			920			1,700
Investments at Cost			1,000			1,600
Land			860			1,260
Stock			1,100			1,300
Debtors			800			1,000
Bank			60			–
			4,740			6,860
Ordinary shares at Sh.20 each			800			1,000
Share premium			240			280
Revaluation Reserve			–			400
Profit and Loss Account			500			500
10% Debentures			2,000			3,000
Creditors			800			1,200
Proposed Dividends			400			400
Bank			–			80
			4,740			6,860
Profit & Loss Account						
Sales			4,000			4,000
Cost of Sales			2,000			2,400
			2,000			1,600
Expenses			1,200			1,200
			800			400
Dividends			400			400
			400			–
Balance b/f			100			500
Balance c/f			500			500

Required:

Calculate for Madaraka Investments Ltd. for 2017 and 2018 the following ratios:

i) Return on capital employed.

ii) Debtors turnover.

iii) Creditors turnover.

iv) Current ratio.

v) Net profit percentage.

vi) Gearing ratio. (8 marks)

c) Using the summarised accounts given and ratios you have just prepared, comment on the financial position and prospects of Madaraka Investments Ltd.

(4 marks)

QUESTION FIVE (20 MARKS)

a) Many corporate boards have now agreed on the need to take responsibility for any potential or actual social impacts caused by their company's activities. This is done through a social responsibility report. In light of this:

i) Discuss the main issues that may be addressed by a company in its social responsibility report.
(5 marks)

ii) Comparing conventional financial accounting reporting with social responsibility reporting, identify the challenges peculiar to social responsibility accounting.
(5 marks)

iii) Explain the benefits that would accrue to a company from the reporting of its social responsibility activities.
(5 marks)

b) Highlight the arguments against human resource accounting.
(5 marks)