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University Examinations 2023/2024

FOURTH YEAR SECOND SEMESTER EXAMINATION FOR THE DEGREE OF
BACHELOR OF EDUCATION ARTS

BFC 3427: ADVANCED FINANCIAL REPORTING

DATE: APRIL 2024

TIME: 2 HOURS

INSTRUCTIONS: Answer question *one* and any other *two* questions

QUESTION ONE (30 MARKS)

- a) Control in a company can only be achieved when the holding company holds over 50% of the ordinary share capital in another company. Discuss (10 marks)
- b) On 1st April 2021 Mega Ltd acquired 4,500,000 ordinary shares of Ksh. 20 par value in Lenga Ltd at a cost of KShs 152,000,000. Further on 1 July 2021 Mega Ltd acquired 15,000,000 ordinary shares of Ksh 20 par value in Tera Ltd at a cost of KSh 716,000,000. Directors were appointed to the boards of both companies by Mega Ltd so as to take an active part in their management. Given below is the information extracted from the books of the companies as at 31 march 2023.

	Balance sheet as at 31 March 2023		
	Mega Sh. '000'	Lenga Sh. '000'	Tera Sh. '000'
Freehold property at cost	720,000	o	200,000
Plant and machinery at cost	5,000	450,000	350,000
Stock	380,000	218,000	360,600

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Debtors	374,800,	185,000	125,000
Amount due from Mega Ltd			48,000
Investments	868000	-	
Bank balances	<u>3,717,800</u>	<u>9 000</u>	<u>40 000</u>
		<u>862 000</u>	
Share capital	0,000	300,000	400,000
Share premium	200,000	24,000	
Capital reserve	300,000	-	56,000
Retained profit (as at 31 March 2023)	<u>786000</u>	<u>218 000</u>	<u>288 000</u>
	<u>2 286 000</u>	<u>542 000</u>	<u>744 000</u>
Creditors	590,000	110,000	152,000
Amount due to Tera Ltd.	36,000		
Accumulated depreciation —plant and machinery	521,800	120,000	124,600
Taxation	190,000	<u>90,000</u>	<u>103,000</u>
Bank balance	<u>94,000</u>	-	-
	<u>3,717,800</u>	<u>862 000</u>	<u>1,123,000</u>

Additional information is given as follows

1. Profit for the year ended 31 March 2023 after tax and before dividends were as follows;

	Sh.
Mega Ltd	252,000,000
Lenga Ltd	102,000,000
Tena Ltd	128,000,000

These profits are included in the retained profits.

2. No interim dividends were paid in the year but final proposed dividends are as follows;

Mega Ltd	20%
Lenga Ltd	10%
Tera Ltd	10%

3. Profits accrued uniformly throughout the year.

4. Included in the stock of Mega Ltd. were goods purchased from Tera Ltd. At Sh.40, 000,000. Tera had made profits of 25% on cost of the goods.

5. A Remittance of Sh 12,000,000 from Mega ltd to Tera Ltd at the end of financial

year was received in April 2023.

6. On 1 April 2021 plant and machinery of Lenga Ltd was revalued upwards by Sh 240,000,000 and the revaluation was not incorporated in the books. Plant and machinery is depreciated at the rate of 10% per annum based on cost.
7. Goodwill or premium on consolidation is amortized on a straight line basis over five years.

Required

Consolidated balance sheet of Mega Ltd and its subsidiary as at 31 March 2023 (20 marks)

QUESTION TWO (20 MARKS)

Billow Limited gained control of Kerrow Limited in 2023 when it acquired 60% of the shareholding as follows:

January 2019	25%
January 2019	20%
January 2020	15%
Total	60%

The profit/ revenue reserves of XYZ limited were as follows:

31 December 2018	6,000,000
31 December 2018	18,000,000
31 December 2019	25,000,000
31 December 2020	29,200,000

Required:

- a) Compute the minority interest, post-acquisition profit and pre-acquisition profit using the conventional method. (4 marks)
- b) Compute as per the above using step by step Approach. (4 marks)
- c) Outline any consideration that the management would consider in deciding which approach to adopt. (4 marks)
- d) State factors that might influence Billow limited to acquire shares of Kerrow Limited on piecemeal basis. (4 marks)

- e) Explain the equity method used in accounting for associates (4

marks)

QUESTION THREE (20 MARKS)

- a) Discuss the advantages of accounting standards (10 marks)
 b) Explain the disadvantages of accounting standards (10 marks)

QUESTION FOUR (20 MARKS)

Given below are the comparative statements of financial positions of Tausi Ltd., a trading company, for the years ended 31 October 2017 and 2018:

Assets	KES '000	2018		2017	
		KES '000	KES '000	KES '000	KES '000
Non-current assets:					
Goodwill	23,500		32,650		
Premises	200,000		80,000		
Plant and machinery	290,100		278,200		
Office equipment	126,250	639,850	87,360		478,210
Current assets:					
Stock	88,890		67,815		
Accounts receivables	57,890		52,015		
Bank	9,210	155,990	-		119,830
		<u>795,840</u>			<u>598,040</u>
Capital and Liabilities:					
Capital:					
Ordinary shares		425,000		250,000	
10% redeemable pref. shares		75,000		160,000	
Share premium		33,000			
Capital redemption reserve		30,000			
General reserve		38,000		12,000	
Profit and loss account		<u>22,300</u>	623,300	<u>11,200</u>	433,200

Non-current liability:

Bank loan		63,000		50,000
Current liabilities:				
Accounts payable	49,840		40,290	
Current tax	30,500		28,500	
Proposed ord. dividends	26,000		18,000	
Accruals	3,200		5,420	
Bank overdraft	-	<u>109,540</u>	<u>22,630</u>	<u>114,840</u>
		<u>795,840</u>		<u>598,040</u>

The following additional information is provided:

1. Some of the redeemable preference shares which had been issued at par, were redeemed at a premium of 2%. To finance the redemption and comply with the Companies Act requirements, the company simultaneously carried out the following:
 - (i) Issued 5,500,000 additional ordinary shares of KES 10 at a total premium of KES 34,700,000.
 - (ii) Transferred sufficient amounts to the capital redemption reserve.
 - (iii) Financed the premium on redemption out of the premium received on issue of the additional ordinary shares.
2. Preference dividends are paid at the end of each financial year on shares outstanding then.
3. Part of plant and machinery which had cost KES 60,000,000 on acquisition and on which KES 42,000,000 accumulated depreciations had been provided was sold for KES 25,000,000 during the year.
4. Included in the depreciation charge for the year is KES 15, 100,000 in respect of plant and machinery.
5. New office equipment was purchased in the year for KES 55,000,000. There was no disposal of office equipment during the year.
6. It is the company's policy not to depreciate premises. The change in the premises account balance was due to a revaluation of the asset.
7. The revaluation reserve arising in (6) above was all to finance the issue of fully paid-up bonus shares of KES 10 each to ordinary shareholders.
8. A new bank loan of KES 25,000,000 was received in the year. Bank interest of KES 8,000,000 was also paid in the year.

9. Current tax liability is in respect of the tax charge for the respective year.
10. During the year ended 31 October 2018 an interim dividend of KES 14,000,000 was paid.

Required:

Cash flow statement in accordance with IAS 7. (20 marks)

QUESTION FIVE (20 MARKS)

(a) ABC Ltd. purchased equity shares in XYZ Ltd. for Sh.56 million when the latter's retained profits were Sh.88 million. The retained earnings of XYZ Ltd. now are Sh.100 million. ABC Ltd. holds 25% of XYZ Ltd.'s equity shares and has amortised Sh.3 million premium on acquisition. XYZ Ltd has declared ordinary dividends of Sh.4 million.

Required:

Determine the value of ABC Ltd.'s investment in XYZ Ltd. using the equity method of accounting for associate companies. (5 marks)

(b) G. Limited is a large manufacturing company that manufacture a wide range of products. Due to the fluctuating nature of economic environment, the company's management has sought to diversify its interests by purchasing shares in other companies in order to improve its reported performance. It has been G. Ltd's policy to appoint a director to the board of any company where its investment comprises more than 20% of the equity share capital, so as to take an active in the management of the said company.

The following investment have been made:

- ◆ On January 2021, 15% of the ordinary share capital of C Limited
- ◆ On 1 July 2021, 30% of the ordinary share capital of B. Limited
- ◆ On I July 2021, 75% of the ordinary share capital of T. Limited and also 5,000 of the 10,000, 9% preference shares of Sh.10 each in that company.
- ◆ The draft profit and loss accounts of the four companies for the year ended 30 June 2022 were as shown below

	G. Ltd.	C. Ltd.	B. Ltd.	T. Ltd.
Turnover	<u>2 100 000</u>	<u>3 900 000</u>	<u>1 900 00</u>	<u>1 200 000</u>
Trading profit	250,000	400,000	210,000	126,000
Dividends receivable:	<u>46 500</u>			<u>-</u>
	296,500	400,000	210,000	126,000

Corporation tax:	<u>(90,000)</u>	<u>(170,000)</u>	<u>(85,000)</u>	<u>(51,000)</u>
Profit after tax:	206,500	230,000	125,000	75,000
Less: Proposed dividends:				
Preference shares		(6,000)		(9,000)
Ordinary shares	<u>(132,000)</u>	<u>(100,000)</u>	<u>(60,000)</u>	<u>(32,000)</u>
Retained profits:	74,500	124,000	65,000	34,000
Balance brought forward	<u>450 000</u>	<u>306 000</u>	<u>235 000</u>	<u>200 000</u>
Balance carried down.	<u>524 000</u>	<u>430 000</u>	<u>300 000</u>	<u>234 000</u>

Additional information:

1. Included in the stock of T. Ltd. were goods purchased from G. Ltd. for Sh.24,000 after acquisition. G. Ltd. realized its usual 25% gross profit margin on this transaction.
2. The dividend due from C. Ltd have not yet been incorporated in the draft profit and loss account of G. Ltd.
3. There was no goodwill arising on consolidation.

Required:

The consolidated profit and loss account of G. Limited and its subsidiary for the year ended 30 June 2022. . (15 marks)