

KASNEB

CS PART I SECTION 2

CICT PART I SECTION 2

CCP PART I SECTION 2

PRINCIPLES OF ACCOUNTING

TUESDAY: 24 November 2015.

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) Explain the following types of errors:

- (i) Errors of omission. (2 marks)
- (ii) Compensating errors. (2 marks)
- (iii) Errors of principle. (2 marks)
- (iv) Errors of commission. (2 marks)

(b) Ngugi Enterprise's draft accounts for the year ended 31 October 2015 showed a gross profit of Sh.10,500,000 and a net profit of Sh.2,120,000.

A thorough scrutiny by the auditors reveals the following errors:

1. Discount allowed to a customer of Sh.100,000 in November 2014 was debited to his account and credited in discounts allowed account.
2. Purchases day book had been overcast by Sh.1,000,000.
3. A receipt of a bad debt amounting to Sh.200,000 in May 2015 has been credited to sales account.
4. Machinery worth Sh.5,400,000 was purchased in August 2015 on credit but a journal entry was passed for Sh.4,500,000.
5. No adjustment has been made for an amount of Sh.200,000 relating to outstanding salaries as at 31 October 2015.
6. Wages of Sh.63,000 paid in July 2015 have not been posted from the cash book.
7. A payment by Julius Gichuru of Sh.94,000 in January 2015 had been posted to the credit of Julius Gichuki's account.
8. The stock sheets as at 31 October 2015 were recorded at selling price of Sh.2,400,000. One stock sheet totalling Sh.15,000 was omitted in the final tally. Ngugi Enterprise's marked up stock costs by 50%.
9. A purchase from a supplier of Sh.341,000 in May 2015 was recorded in the books as Sh.143,000.
10. Discounts received of Sh.324,000 in May 2015 have been posted to the debit side of the discounts allowed account.

Required:

- (i) Statement of corrected gross profit for the year ended 31 October 2015. (6 marks)
 - (ii) Statement of corrected net profit for the year ended 31 October 2015. (6 marks)
- (Total: 20 marks)**

QUESTION TWO

(a) In the context of public sector accounting, explain the following terms:

- (i) Commitment accounting. (3 marks)
- (ii) Revolving funds. (3 marks)
- (iii) Budget cycle. (3 marks)

- (b) Phala Ltd., a mobile phone accessories manufacturer, has obtained accounting ratios relating to averages for similar organisations in the industry.

The industry average ratios for the period 1 July 2014 to 30 June 2015 are as follows:

| | |
|-------------------------------------|-----------|
| Return on capital employed | 21.6% |
| Net assets turnover | 1.6 times |
| Gross profit margin | 25% |
| Net profit (before tax) margin | 10.5% |
| Current ratio | 1.5:1 |
| Quick ratio | 0.8:1 |
| Inventory holding period | 42 days |
| Trade receivables collection period | 41 days |
| Trade payables payment period | 59 days |
| Debt to equity | 35% |
| Dividend cover | 4 times |

The summarised financial statements of Phala Ltd. for the year ended 30 June 2015 are as follows:

| | |
|------------------------------------|-----------------|
| Income statement | Sh."000" |
| Sales revenue | 4,850 |
| Cost of sales | <u>(3,740)</u> |
| Gross profit | 1,110 |
| Other operating expenses | <u>(430)</u> |
| Operating profit | 680 |
| Interest payable | <u>(68)</u> |
| Loss on sale of obsolete inventory | <u>(240)</u> |
| Profit before tax | 372 |
| Tax expense | <u>(180)</u> |
| Profit after tax | <u>192</u> |

| | |
|--------------------------------|-----------------|
| Changes in equity | Sh."000" |
| Retained profits (1 July 2014) | 358 |
| Net profit for the year | 192 |
| Dividends paid | <u>(180)</u> |
| | <u>370</u> |

Statement of financial position as at 30 June 2015:

| | | |
|--------------------------------|-----------------|-----------------|
| | Sh."000" | Sh."000" |
| Non-current assets (net) | | 1,080 |
| Current assets: | | |
| Inventory | 550 | |
| Trade receivables | <u>640</u> | <u>1,190</u> |
| | | <u>2,270</u> |
| Equity and liabilities: | | |
| Equity: | | |
| Ordinary shares of Sh.0.5 each | | 300 |
| Retained profits | | 370 |
| Non-current liability: | | |
| 7% debentures | | 600 |
| Current liabilities: | | |
| Trade payables | 700 | |
| Tax expense | 170 | |
| Bank overdraft | <u>130</u> | <u>1,000</u> |
| | | <u>2,270</u> |

Additional information:

- The accumulated depreciation for non-current assets as at 30 June 2015 amounted to Sh.6,120,000.
- Phala Ltd.'s ordinary shares averaged a market price of Sh.12 throughout the year.
- Assume a 365 day year.

Required:

Compute the ratios for Phala Ltd. corresponding to those for the industry averages.

(11 marks)

(Total: 20 marks)

QUESTION THREE

(a) Describe the following terms:

(i) Fundamental accounting concepts. (3 marks)

(ii) Accounting bases. (3 marks)

(b) On 30 September 2015, a fire broke out at the premises of Revolution Chemicals Ltd. and destroyed its contents. Fortunately, certain accounting records had been kept in another building and the following information was retrieved for the period from 31 May 2015 to 30 September 2015:

| | Sh. |
|--------------------------------|------------|
| Raw materials purchased | 170,000 |
| Work-in-progress (31 May 2015) | 34,000,000 |
| Raw materials (31 May 2015) | 16,000,000 |
| Finished goods (31 May 2015) | 30,000,000 |

Additional information:

1. Sales of finished goods amounted to Sh.500,000,000.
2. Prime costs average 70% of the cost of goods manufactured.
3. Gross profit percentage based on net sales is 20%.
4. Cost of goods available for sale amounted to Sh.460,000,000.
5. Factory overheads are 40% of the cost of goods manufactured.
6. Direct labour amounted to Sh.180,000,000.
7. The loss was fully covered by an insurance policy.

Required:

Manufacturing and trading account for the 4-month period ended 30 September 2015.

(14 marks)

(Total: 20 marks)

QUESTION FOUR

The Nairobi Investment Society Club operates a professional club for its members to promote, among other things, sports and networking

The treasurer of the club has prepared the following receipts and payments account as at 31 October 2015:

| Receipts and payments account | | | |
|--------------------------------------|------------------|-------------------------|------------------|
| | Sh. "000" | | Sh. "000" |
| Balance brought forward | 748,000 | Club extension | 650,000 |
| Subscriptions: 2013/2014 | 158,000 | Dinner dance expenses | 350,000 |
| 2014/2015 | 2,540,000 | New equipment | 300,000 |
| 2015/2016 | 67,000 | Bar purchases | 726,000 |
| Dinner dance | 598,000 | Salaries and wages | 454,000 |
| Bar sales | 932,000 | Other staff expenses | 129,000 |
| Donations | 529,000 | Coach fees | 260,000 |
| Rental income | 158,000 | Life saver fees | 184,000 |
| Investment income | 247,000 | Investment purchases | 450,000 |
| Sale of old equipment | 62,000 | General expenses | 158,000 |
| | | Repairs and maintenance | 296,000 |
| | | Balance carried down | <u>2,082,000</u> |
| | <u>6,039,000</u> | | <u>6,039,000</u> |

Additional information:

1. The following balances were available at the beginning and at the end of the year:

| | 31 October 2014 | 31 October 2015 |
|-------------------------------------|-----------------|-----------------|
| | Sh. "000" | Sh. "000" |
| Clubhouse (building) | 2,450,000 | ? |
| Equipment: Cost | 325,000 | ? |
| Accumulated depreciation | 95,000 | ? |
| Furniture and fittings: Cost | 340,000 | ? |
| Accumulated depreciation | 125,000 | ? |
| Subscriptions in arrears: 2013/2014 | 185,000 | |
| 2014/2015 | | 324,000 |

| | | | |
|-----------------------------|-----------|-----------|---------|
| Subscriptions prepaid: | 2014/2015 | 124,000 | |
| | 2015/2016 | 54,000 | ? |
| Inventory | | 254,000 | 329,000 |
| Accrued salaries and wages | | 23,000 | 28,000 |
| Unpaid dinner dance tickets | | | 29,000 |
| Creditors for bar supplies | | 168,000 | 234,000 |
| Investments | | 2,550,000 | |
| Unpaid buildings extension | | | 85,000 |
| Club extension fund | | 250,000 | ? |

2. The donations were for the extension of the club. The funds will remain in the club extension fund until the works are completed when the balance will be transferred to the accumulated fund.
3. Equipment which had cost Sh.25 million and had a book value of Sh.18 million was sold on credit for Sh.14 million to a member who had not paid by the year end. Other equipment which had been bought for Sh.60 million and on which depreciation of Sh.19 million had been provided was also sold during the year.
4. Accounting and audit fees of Sh.50 million should be provided for.
5. Depreciation is to be provided on cost as follows:

| | |
|------------------------|-----------------------|
| Asset | Rate per annum |
| Furniture and fittings | 10% |
| Equipment | 15% |
6. Subscriptions in arrears are written off after 12 months.

Required:

- (a) Income and expenditure account for the year ended 31 October 2015. (10 marks)
- (b) Statement of financial position as at 31 October 2015. (10 marks)

(Total: 20 marks)

QUESTION FIVE

- (a) Explain four roles played by accounting regulatory bodies. (8 marks)
- (b) H Ltd. acquired 80% of the ordinary shares of S Ltd. on 1 February 2015. As at 31 October 2014, the balance on S Ltd.'s share premium account was Sh.4,000,000 and retained earnings was Sh.15,000,000. The statement of financial position of the two companies as at 31 October 2015 are as shown below:

| | H Ltd. Sh."000" | S Ltd. Sh."000" |
|---|--------------------|--------------------|
| Assets: | | |
| Property, plant and equipment | 32,000 | 30,000 |
| 16,000 ordinary shares of Sh.0.5 each in S Ltd. | 50,000 | - |
| | 82,000 | 30,000 |
| Current assets | 85,000 | 43,000 |
| Total assets | 167,000 | 73,000 |
| Financed by: | | |
| Equity | | |
| Ordinary shares of Sh.10 each | 100,000 | - |
| Ordinary shares of Sh.0.5 each | | 10,000 |
| Share premium account | 7,000 | 4,000 |
| Retained earnings | 40,000 | 39,000 |
| | 147,000 | 53,000 |
| Current liabilities | 20,000 | 20,000 |
| | 167,000 | 73,000 |

Additional information

1. None of the companies paid dividends during the year ended 31 October 2015.
2. Non-controlling interest should be valued at full value.
3. The goodwill attributable to the non-controlling interest is valued at Sh.3,000,000.
4. The profits of S Ltd. were assumed to accrue evenly throughout the year.

Required:

Group consolidated statement of financial position as at 31 October 2015.

(12 marks)

(Total: 20 marks)