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**University Examinations 2015/2016**

SECOND YEAR FIRST SEMESTER EXAMINATION FOR THE DEGREE

OF

 BACHELOR OF COMMERCE

**BFC 3225: INTERMEDIATE ACCOUNTING I**

**DATE: APRIL 2016 TIME: 2 HOURS**

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

**QUESTION ONE (30 MARKS)**

1. Briefly describe the objectives of financial reporting (4 marks)
2. The two primary qualities of accounting information are relevance and reliability. Are these qualities as likely to be present in a forecast of future earnings as in an incomr statement? Explain. (4 marks)
3. What is meant by the going concern principle of accounting? How does it affect the valuation of assets? When is this principle not applicable (5 marks)
4. The following was extracted from the books of Kasoka Ltd as at 30th June 2013 and 2014

|  |  |  |
| --- | --- | --- |
|  | 2014 | 2013 |
|  | Shs ‘000’ | Shs ‘000’ |
| Fixed assets  | 159,200 | 80,000 |
| Depreciation  |  |  |
|  | 115,200 | 49,200 |
| Investiments  |  |  |
|  | 155,200 | 49,200 |
| Current assets |  |  |
| Stocks  | 92,000 | 64,000 |
| Debtors  | 40,400 | 36,800 |
| Bank  |  |  |
|  | 146,800 | 100,800 |
| Current liabilities  |  |  |
| Creditors  |  |  |
| Bankoverdraft  |  |  |
| Net current Assets  |  |  |
| TOTAL NET ASSETS  |  |  |
| Financed by: |  |  |
| Share capital  | 40,000 | 20,000 |
| Share premium  | 60,000 |  |
| Revenue reserves  |  |  |
| Shareholder funds | 226,000 | 108,000 |
| 15% Bank loan  |  |  |
|  |  |  |

**Required:**

A cash flow statement for the year ended 30th June 2014. (17 marks)

**QUESTION TWO (20 MARKS)**

The Tarrow Drilling Company paid shs. 80,000, 000 for the right to explore for a oil deposit on 1000 acres of land in North Eastern Kenya. Costs of exploring for the oil deposit totaled shs. 64, 000, 000 and intangible development costs incurred in digging and erecting the mine shaft were shs.40, 000, 000. In addition, Tarrow acquired new drilling equipment for the project at a cost of shs.48,000, 000. After the oil is extracted from the well, the equipment will be sold. Tarrwo is required by its contract to restore the land to a condition suitable for recreational use after it Drills th oil. The Company has provided the following three cashflow possibilities (good, average and Best) for the restoration costs to be paid in three yers, after oil drilling is completed:

|  |  |  |
| --- | --- | --- |
|  | Cash Outflow  | Probability  |
| Good  | 40,000,000 | 30% |
| Average  | 48,000,000 | 50% |
| Best | 56,000,000 | 20% |

The company’s risk adjusted interest rate is 8%.

**Required:**

1. Show the total cost to be capitalized for oil deposits excavation and restoration drilling

(10 marks)

1. Distinguish the following terms (10 marks)
2. Depreciation and amortization
3. Patent and a trade mark
4. Current and non-current asset
5. Operating lease and a finance lease
6. Revaluation and impairment

**QUESTION THREE (20 MARKS)**

1. The South Imenti Ltd. acquired all of the outstanding common stock of the North Imenti Ltd in exchange for shs. 180 million in cash. South Imentin Ltd assumed all of North Imenti Ltd. long identifiable assets of North Imenti are as follows: (in millions)

|  |  |
| --- | --- |
| Receivables  | 50 |
| Inventory  | 70 |
| Property, plant, and equipment  | 90 |
| Patent  | 40 |
| Total  |  |

**Required:**

1. Determine the amount of goodwill on acquisition (5 marks)
2. Show accounting/journal entries for the transaction (5 marks)
3. Describe three inventory valuation methods (6 marks)
4. Amedan Ltd prepares its financial statements according to IFRS. At the beginning of its 2013 fiscal year, the company pruchsed a franchise for shs. 500,000. The franchise has a 10 year contractual life and no residual value, so amortization in 2013 is shs. 50,000. The company does not use an accumulated amortization account and credits the franchise account directly when amortization is recorded. At the end of the year, Amedan Ltd. chosses to revalue the franchise as permitted by IAS No. 38. Assuming tha the fair value of the franchise, determined by reference to a active market, at year-end is shs. 600,000, show accounting entries/journal entries to record the above transaction in the books of Amedan Ltd (4 marks)

**QUESTION FOUR (20 MARKS)**

1. Menwe ltd made a lease agreement on 1.1.2012 with Farm Machinery ltd (Lessor) for a lease of tractor with a cost proce of shs. 4,746,000. The lease is a four year contract non cancelleable and requires menwe ltd to pay annual lease intalments of 1,461,000 payable in advance in each year of lease. The economic life of the tractor is four years with no residual value after the fourth year of use. Depreciation ofn the machine is on a straight lien basis and the accounting period for both Menwe ltd and Farm machinery ltd is on 31st of December each year.

Required:

1. Determine the implicit interest rate in the lease (4 marks)
2. Journal entries to record the initial transactionin the books of the lessor and lessee (6 marks)
3. Lease amortization schedule (6 marks)
4. Discus the economic advantages of leases as a way of financing acquisition of assets for business use (4 marks)

**QUESTION FIVE (20 MARKS)**

1. A company purchased a piece of equipment in 2008 for shs. 4 million, the useful life of the machinery was estimated to be 10 years with no residul value. The straight line method of depreciation was used in 2008 through 2010, with a full year depreciation taken in 2008. In 2009, the company revised the useful of machinery to eight years.

**Required:**

1. Show the depreciation expenses for 2011 and later years (4 marks)
2. Journal entry to show the change in accounting estimate (6 marks)
3. Describe the following terms
4. Financial assets (2 marks)
5. Investment property (2 marks)
6. Intangible assets (2 marks)
7. Goodwill (2 marks)
8. What is the basic criteria for determining the value of stock (2 marks)