



MURANGA UNIVERSITY COLLEGE
(A constituent College of Jomo Kenyatta University of Agriculture & Technology)

MAIN CAMPUS

ORDINARY UNIVERSITY EXAMINATIONS

2015/2016 ACADEMIC YEAR

FOURTH YEAR FIRST SEMESTER EXAMINATIONS

**FOR THE DEGREE
OF
BACHELOR OF COMMERCE**

COURSE CODE: HBA 2401

COURSE TITLE: ADVANCED FINANCIAL REPORTING

DATE: 16th DECEMBER, 2015

TIME: 2 HOURS

INSTRUCTIONS TO CANDIDATES

Question ONE (1) is compulsory
Answer THREE (3) questions

MRUC observes ZERO tolerance to examination irregularities

QUESTION ONE:

- a) Regulatory framework refers to the various rules and regulations that are followed in financial reporting. Briefly explain the role of this framework in the context of financial reporting in Kenya. (7 marks)
- b) In determining the monetary amount at which elements in the financial statements are to be recognized in financial statements, different measurement bases can be adopted. Explain FOUR measurements basis, and in each case illustrate where the base may be adopted. (8 marks)
- c) Provide a brief description of the following terms:

Financial Instrument	(2 marks)
Equity Instrument	(1 marks)
Derivative Instrument	(2 marks)

- d) Rathbone Company issued 2,000 convertible bonds at the start of 2015. The bonds have a three year term, and are issued at par with a face value of KSh.1,000 per bond, giving total proceeds of KSh.2,000,000. Interest is payable annually in arrears at a nominal annual interest rate of 6%. Each bond is convertible at any time up to maturity into 250 common shares.

When the bonds are issued, the prevailing market interest rate for similar debt without conversion options is 9%. At the issue date, the market price of one common share is KSh.3. The dividends expected over the three year term of the bonds amount to 14c per share at the end of each year.

The risk-free annual interest rate for a three year term is 5%.

Required

What is the value of the equity component in the bond? (10 marks)

QUESTION TWO:

- a) On 1 January 2011 Biashara Company purchased a debt instrument for its value of KSh.1,000. The debt instrument is due to mature on 31 December 2015. The instrument has a principal amount of KSh.1,250 and the instrument carries fixed interest at 4.72% that is paid annually.

How should Biashara Company account for the debt instrument over its five year term?

(**HINT:**) Prepare a table to show the debt instrument at amortised cost
Show the extracts from the financial statements. (10 marks)

- b) With Illustrations, explain FIVE the indicators that a financial asset may be impaired. (10 marks)

QUESTION THREE:

- a) Explain the following terms with reference to International Accounting Standard 19. (Employee Benefits):
- (i) Current service cost (2 marks)
 - (ii) Past service cost (2 marks)
 - (iii) Vested employee benefits (2 marks)

- b) ABC Ltd. contributes sh.30 million per annum to a pension scheme and treats the amount as current service cost pension expense.
On 1 July 1998, the actuarial valuation of the scheme showed a deficit of sh.600 million. The actuary recommended that the deficit be cleared within four years by paying sh.150 million per year in addition to the annual service costs. The average remaining service life of employees in the scheme on 1 July 1998 was eight years.

Required:

For each of the remaining eight service years of the employees, calculate the pension expense and pension liability or prepayment. (8 marks)

- c) A company that extracts natural gas and oil has a drilling platform in the the country X. It is required by legislation of the country concerned to remove and dismantle the platform at the end of its useful life. Accordingly, the company has included an amount in its accounts for removal and dismantling costs, and is depreciating this amount over the platform's expected life. The company is carrying out an exercise to establish whether there has been an impairment of the platform. The following information is provided:
- i. Its carrying amount in the balance sheet is Kshs.3m
 - ii. The company has received an offer of Kshs.2.8m for the platform from another oil company. The bidder would take over the responsibility (and costs) for dismantling and removing the platform at the end of its life.
 - iii. The present value of the estimated cash flows from the platform's continued use is Kshs.3.3m
 - iv. The carrying amount in the balance sheet for the provision for dismantling and removal is currently Kshs.0.6m

What should be the value of the drilling platform in the balance sheet, and what if anything is the impairment loss? (6 marks)

QUESTION FOUR:

- a) With relevant illustrations, differentiate between current tax and deferred tax (2 marks)
- b) In reference to IAS 23(Borrowing costs); and with appropriate examples where necessary;
 - i. Give ANY two examples of borrowing costs (1 mark)
 - ii. Explain the meaning of qualifying assets. (1 marks)
 - iii. Differentiate between : Expense model and Capitalization model.(2 marks)
- c) Rain Ltd., Storm Ltd. firms are in the business of manufacturing tents. Their balance sheets as at 30 September 2013 are shown side-by-side below:

	Rain Ltd.		Storm Ltd.	
	Sh. "000"	Sh. "000"	Sh. "000"	Sh. "000"
Non-current assets:				
Machinery & Equipments(net of depreciation)		14,000		6,300
Premises		<u>5,000</u>		<u>1,900</u>
		19,000		8,200
Current assets:				
Stocks	2,000		1,200	
Trade debtors	4,800		2,000	
Cash	<u>2,700</u>		<u>1,400</u>	
	9,500		4,600	
Current liabilities:				
Trade creditors	5,000		2,600	
Net current assets		<u>4,500</u>		<u>2,000</u>
		<u>23,500</u>		<u>10,200</u>
Financed by:				
Authorized and issued Share capital:				
Ordinary shares of Sh.100; fully paid		15,000		5,000
10% preference shares of Sh. 100 fully paid		-		3,000
General reserve		6,000		3,000
Profit and loss account balance		<u>2,500</u>		-800
		<u>23,500</u>		<u>10,200</u>

Additional information:

- Rain Ltd. purchased 30,000 ordinary shares in Storm Ltd. on 1 October 2011 for Sh.3,400,000 and 5,000 preference shares on 1 October 2012 for Sh. 600,000.
- Profit and loss account Balances**

Storm Ltd.	1 October 2011	Sh. 500,000 (debit).
	1 October 2012	Sh. 600,000 (debit).

General reserve

Storm Ltd.	1 October 2011	Sh. 1,000,000
	1 October 2012	Sh. 2,000,000
- The following inter-company balance are included in the balances of trade debtors and trade creditors: Sh. 200,000 due from storm Ltd.
- Rain Ltd. sold goods to Storm Ltd. for Sh.800,000. The goods had originally cost Rain Ltd. Sh.600,000. Storm Ltd. still had Sh.200,000 worth of these goods (at invoiced price) in stock as at 30 September, 2013.

Required:

Prepare the consolidated balance sheet of Rain Ltd. and its subsidiary as at 30 September,2013 (14 marks)

