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KIRIRI WOMENS' UNIVERSITY OF SCIENCE AND TECHNOLOGY
UNIVERSITY EXAMINATION, 2022/2023 ACADEMIC YEAR
FOURTH YEAR, SECOND SEMESTER EXAMINATION
FOR THE DEGREE OF BACHELOR OF SCIENCE
(BUSINESS ADMINISTRATION)

Date: 27th July, 2022
Time: 11.30am – 1.30pm

KAC 405 - ACCOUNTING THEORY

INSTRUCTIONS TO CANDIDATES

ANSWER QUESTION ONE (COMPULSORY) AND ANY OTHER TWO QUESTIONS

QUESTION ONE (30 MARKS)

- a) Briefly explain the meaning of each of the following accounting concepts, giving in each case, an example of the application of each:
- i) Materiality (3 marks)
 - ii) Substance over form (3 marks)
 - iii) Money measurement (3marks)
- b) The trial balance of Plastics Ltd as at 31 October 2014 is as follows:

	Sh.'000	Sh.'000
Ordinary shares of Sh.50 each		10,000
10% preference shares of Sh.100 each		9,000
10% debentures		8,000
Land and buildings (net book value)	25,000	
Plant and machinery (net book value)	8,000	
Motor vehicles (net book value)	2,000	
Inventory	6,000	
Accounts receivables and payables	20,000	19,000
Cash at bank	4,100	
Capital redemption reserve		6,000
Share premium		4,000
Retained profits as at (November 2013)		3,000
Debenture interest	400	
Preference dividend	450	
Gross profit		25,000
Other operating income		4,000
Administrative expenses	13,000	
Distribution costs	6,000	
Other operating expenses	1,550	
Interim ordinary dividend paid	2,000	
Corporation tax		500
	<u>88,500</u>	<u>88,500</u>

Additional information:

1. A building whose net book value is currently Sh.5 million is to be revalued to Sh.9 million
2. A final ordinary dividend of Sh.2 million is proposed.
3. The balance on the corporation tax for the current year is estimated at Sh.3 million.

Required:

- i) Income statement for the year ended 31 October 2014. (8 marks)
- ii) Statement of Financial Position as at 31 October 2014. (8 marks)
- c) Describe the purposes of the income statement and the statement of financial position
Above to the users of the financial statements (5 marks)

QUESTION TWO (20 MARKS)

- a) Explain the meaning of prudence concept showing how this is applied in stock valuation. (3 marks)
- b) The summarized financial statements of Baraka Enterprises Ltd. are as follows:

Income statement for the year ended 30 September

	2013	2014
	Sh.'000	Sh.'000
Sales	20,000	28,000
Cost of sales	<u>(15,000)</u>	<u>(21,000)</u>
Gross profit	5,000	7,000
Administrative expenses	<u>(3,800)</u>	<u>(4,600)</u>
Debenture interest		<u>(400)</u>
Net profit	<u>1,200</u>	<u>2,000</u>

Statement of Financial Position as at 30 September

	2013	2014
	Sh.'000	Sh.'000
Assets:		
Non-current assets (net book value)	<u>11,000</u>	<u>14,000</u>
Current assets:		
Inventories	2,000	3,000
Trade and other receivables	2,500	2,800
Balance at bank	<u>-</u>	<u>500</u>
	<u>4,500</u>	<u>6,300</u>
Total assets	<u>15,500</u>	<u>20,300</u>
Equity and liabilities:		
Capital and reserves:		
Issued and fully paid		
1,000,000 ordinary shares of Sh.10 each	10,000	10,000
Revenue reserves	<u>3,000</u>	<u>4,100</u>
	<u>13,000</u>	<u>14,100</u>
Noncurrent liabilities		
8% debentures	<u>-</u>	<u>5,000</u>
Current liabilities		
Trade and other payables	1,500	1,200
Bank overdraft	<u>1,000</u>	<u>-</u>
	<u>2,500</u>	<u>1,200</u>
Total equity and liabilities	<u>15,500</u>	<u>20,300</u>

Stock as at 1 October 2012 was Sh.5, 000,000

Required:

For each year, calculate the following:

- i) Gross profit margin (2 marks)
 - ii) Inventory turnover (2 marks)
 - iii) Return on equity (2 marks)
 - iv) Return on assets (2 marks)
 - v) Acid test ratio (2 marks)
 - vi) Current ratio (2 marks)
 - vii) Financial leverage (2 marks)
- c) Comment on the liquidity position of the company giving possible reasons for the change. (3 marks)

QUESTION THREE (20 MARKS)

Write short notes to distinguish the following:

- a) Purchased goodwill and non-purchased goodwill. (5marks)
- b) Amortization and depreciation of fixed assets (5marks)
- c) Provisions and reserves. (5marks)
- d) Compensating errors and errors of principle (5 marks)

QUESTION FOUR (20 MARKS)

- a) What is an “accounting policy”? (2 marks)
- b) Briefly explain three circumstances under which “goodwill” can be recorded in a business firm’s books of account. (9 marks)
- c) The following categories of people are recognized as users of the information contained in financial statements:
 - Owners.
 - Financial analysts
 - Lenders.

For each of the above users of financial statements, identify the kind of information they may require, why they require it and the decisions they make from that information.

(9 marks)

QUESTION FIVE(20 MARKS)

The accounting profession has for a long time relied on certain accounting conventions to guide accounting practice. Yet the application of the same conventions has been the source of criticism of the quality and relevance of information contained in financial reports.

Some of these conventions include:

- a) The business entity principle.
- b) The historical cost principle.
- c) The monetary principle.
- d) The matching principle.
- e) The conservatism principle.

Required:

For each of the principles listed above:

- i) Explain its meaning. (5 marks)
- ii) Justify its use. (8 marks)
- iii) Explain any weaknesses associated with its use. (7 marks)