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KIRIRI WOMENS' UNIVERSITY OF SCIENCE AND TECHNOLOGY
UNIVERSITY EXAMINATIONS, 2024/2025 ACADEMIC YEAR
SECOND YEAR, FIRST SEMESTER EXAMINATION
FOR MASTER IN BUSINESS ADMINISTRATION (ACCOUNTING OPTION)

KAC 3202: ADVANCED FINANCIAL ACCOUNTING

Date: 7TH DECEMBER, 2024
Time: 9:00 AM – 12:00 PM

INSTRUCTIONS TO CANDIDATES
ANSWER QUESTION ONE (COMPULSORY) AND ANY OTHER THREE QUESTIONS

QUESTION ONE: COMPULSORY (40 MARKS)

Case study: Financial Reporting Challenges and Ethical Dilemmas at Nairobi Retail Ltd.

Nairobi Retail Ltd. is a large retail chain in Kenya, operating across major cities. In recent years, the company has expanded rapidly, opening new branches in strategic locations. However, its expansion has led to challenges in financial reporting, especially with the adoption of new accounting standards and ethical concerns.

In the last fiscal year, the company entered into several lease agreements for its new branches. These leases range from 5 to 15 years, and Nairobi Retail Ltd. has struggled to apply IFRS 16 accurately. Additionally, with increasing inflation rates in Kenya, the company is considering how best to reflect the price-level changes in its financial statements to ensure a fair valuation of assets and liabilities. At the same time, the company is facing significant foreign exchange volatility due to its transactions with international suppliers. The CFO is unsure of the appropriate treatment of foreign currency transactions and translation under IAS 21.

Furthermore, the CEO has expressed interest in acquiring a smaller competitor, Mombasa Traders Ltd. and the board is in discussions about how this acquisition should be structured and reported under IFRS 3. There are also concerns that some senior managers have been manipulating sales figures to meet performance targets and receive higher bonuses, raising ethical issues about the integrity of the company's financial reports.

Nairobi Retail Ltd. needs your expertise as an Accounting expert to address the following issues:

Required

a) Nairobi Retail Ltd. has signed a lease for a new branch for KES 30 million over 10 years. Using IFRS 16, explain how Nairobi Retail Ltd. should account for this lease, focusing on both the initial recognition and subsequent measurement. **(8 Marks)**

b) Analyze how Nairobi Retail Ltd. can apply accounting for price-level changes, particularly using the Current Purchasing Power (CPP) model. Use Kenyan inflation data and relevant financial figures to illustrate how price-level changes can impact the valuation of non-monetary assets. **(8 Marks)**

c) Nairobi Retail Ltd. imports goods from suppliers in the USA and the UK, paying in USD and GBP, respectively. Discuss how IAS 21 should be applied to translate foreign currency transactions and prepare financial statements, considering exchange rate fluctuations. **(8 Marks)**

d) Nairobi Retail Ltd. plans to acquire Mombasa Traders Ltd. Explain how this business combination should be accounted for under IFRS 3, focusing on the identification of the acquirer, the recognition of goodwill, and the accounting treatment of contingent consideration. **(8 Marks)**

e) Several senior managers have been found inflating sales figures to meet performance targets. Discuss the ethical implications of this action and propose measures that Nairobi Retail Ltd. should implement to uphold ethical standards in its financial reporting. **(8 Marks)**

QUESTION TWO: (20 MARKS)

Hesabu Moto, a firm associated with you, recently got a license to offer accounting and auditing services to the public. The first client is a partnership that requires your services to reorganize their operations

a) Ann and Bernard share profits in a ratio of 3:2. Catherine is admitted into the partnership, contributing KES 500,000, and is entitled to 25% of the profits. Explain the necessary accounting entries, including the revaluation of assets and the goodwill adjustment upon the admission of Catherine. **(8 Marks)**

b) David retires from a partnership, and the remaining partners Emma and Fadhili agree to share profits equally. The partnership balance sheet shows goodwill of KES 200,000. How should the goodwill be adjusted in the books of the partnership after the retirement of Partner David? Provide detailed accounting entries. **(6 Marks)**

c) Outline the key steps and accounting treatments required for the dissolution of a partnership, including the settlement of liabilities and realization of assets. Provide relevant journal entries. **(6 Marks)**

QUESTION THREE: (20 MARKS)

a) PamojaCo Ltd. holds an 80% interest in SubukiaCo Ltd. On the date of acquisition, SubikiaCo Ltd.'s identifiable net assets were valued at KES 2,500,000. Demonstrate and explain how to account for the non-controlling interest (NCI) in the consolidated financial statements of PamojaCo Ltd. under IFRS 10, and calculate the amount of NCI. **(8 Marks)**

b) PamojaCo Ltd. sold goods worth KES 600,000 to SubukiaCo Ltd. at a 20% profit margin. SubukiaCo Ltd. still holds 40% of these goods in inventory at year-end. Explain how this intercompany transaction should be eliminated in the consolidated financial statements. **(6 Marks)**

c) Explain how the financial statements of a foreign subsidiary operating in Tanzania should be translated into the parent company's currency under IAS 21 based in Kenya, and describe how foreign exchange translation differences should be treated in the consolidated financial statements. **(6 Marks)**

QUESTION FOUR: (20 MARKS)

a) Explain how Current Cost Accounting (CCA) differs from historical cost accounting and demonstrate, with an example, how to adjust the value of an asset using CCA in a high-inflation environment. Use Kenyan inflation data for illustration. **(8 Marks)**

b) A Kenyan company purchases equipment from a US supplier for \$50,000 when the exchange rate is KES 110 to \$1. By the payment date, the exchange rate has moved to KES 115 to \$1. Explain how to account for the foreign currency transaction, and compute the exchange difference to be recognized in the financial statements. **(6 Marks)**

c) Discuss how inflation can distort financial statements and the measures that can be taken to mitigate these effects, referencing both the Current Purchasing Power (CPP) and Current Cost Accounting (CCA) methods. **(6 Marks)**

QUESTION FIVE: (20 MARKS)

a) Explain the steps involved in the liquidation of a company under a solvent scenario. Highlight the role of the liquidator and how the assets are distributed to creditors and shareholders. **(8 Marks)**

b) During liquidation, the statement of affairs reveals that the company’s assets are KES 3,500,000 and its liabilities to unsecured creditors are KES 2,000,000. Calculate the amount available for distribution to shareholders and explain how this amount is determined. **(6 Marks)**

c) Jamii Ltd. was incorporated on July 1, 2023. The company's profit for the year ending December 31, 2023, is KES 600,000. The turnover for the pre-incorporation period (January 1 to June 30) was KES 1,200,000, and for the post-incorporation period (July 1 to December 31), it was KES 1,800,000. Apportion the profit between the pre-and post-incorporation periods. **(6 Marks)**.