



PAN AFRICA CHRISTIAN UNIVERSITY

SCHOOL OF LEADERSHIP, BUSINESS & TECHNOLOGY

END OF SEMESTER EXAMINATION FOR THE DEGREE OF

BACHELOR OF COMMERCE

SEPTEMBER-DECEMBER 2019

CAMPUS: ROYSAMBU

DEPARTMENT: BUSINESS STUDIES

COURSE CODE: CAC303

COURSE TITLE: ACCOUNTING FOR LIABILITIES

EXAM DATE: WEDNESDAY 4th DECEMBER 2019

DURATION: 2 HOURS

TIME: 2:00PM-4:00PM

INSTRUCTIONS

- Read the instructions and questions carefully before you write the answers.
- Write your **STUDENT NUMBER** in the Answer Booklet given
- *Write clearly and legibly.*
- This exam script consists of **Six (6)** questions.
- Answer question **ONE** and ANY other **three** Questions.
- *ALL PAC University's examination rules and regulations apply*

Question One (Compulsory)**(30 marks)**

a. Outline the accounting treatment of the following items

- i. Accounts payable (2 marks)
- ii. Short term notes payable (2 marks)
- iii. Dividend payable (2 marks)

b. Define the following terms.

- i. Basic earnings per share. (2 marks)
- ii. Potentially dilutive security. (2 marks)
- iii. Diluted earnings per share. (2 marks)
- iv. Complex capital structure. (2 marks)
- v. Potential common stock (2 marks)

c. In 2012, Best Stuff, Inc. had sales of shs. 90,000 of its new video recorders. The company gives a two-year warranty with the purchase of a video recorder. When Best Stuff recorded the sales, the company also estimated that it would spend shs.8,400 to honor those warranties. When the company prepared its annual financial statements for 2012, no video recorders had been brought in for repair. In January 2013, however, 20 people brought in their broken video recorders, and Best Stuff spent a total of shs. 750 repairing them (at no charge to the customers, because the video recorders were under warranty). Assume no additional sales were made in January 2013 (i.e., no new warranties were given in January).

Required:

Show the journal entries for the above transactions.

(4 marks)

- d. On April 1, 2002, Maritim manufacturing purchased a machine for use in its operations by paying Sh120,000 cash and signing an Sh1,300,000 (face amount) non-interest bearing note due in one year (on March 31, 2003). The going rate of interest for this type of note was 14% per year. The company uses straight line depreciation. The accounting period ends on December 31. Assume a five year life for the machine and 10% residual value.

Required:

Give all entries from

- i. 1st April , 2002 (3 marks)
- ii. 31st December, 2002 (3 marks)
- iii. 31st March 31, 2003. (4 marks)

Question Two (10 Marks)

On January 1, 2000, ABC Ltd. issued Sh. 100,000 par value, 5-year life of 8% term bonds with interest payable on July 1 and January 1. The market rate of interest for the company's bonds is 10%. In exchange for the purchase price, investors of these bonds obtain the right to receive two different future cash inflows. First, the right to receive Sh. 100,000 at the end of the bond issue's five-year life and secondly, the right to receive Sh. 4,000 in interest at the end of each six-month interest period throughout the five-year life of the bonds

Required:

Calculate the:

- i. present value and the discount amount on bonds and (5 marks)
- ii. Record the calculations in a journal. (5 marks)

Question Three (10 Marks)

- a. Using examples distinguish between an operating lease and a capital lease. (4 marks)
- b. Explain three circumstances might lead to termination of a lease. (6 marks)

Question Four**(10 Marks)**

On January 1, 1998, Lessor company and Lessee company signed a 3-year concealable lease for an asset with an estimate life of three years.

- Three lease payments of Sh36,556 are to be made at the beginning of each year.
- The fair market value of the asset at the inception of the lease is Sh100,000, which is also the carrying value (cost) on the Lessor's books.
- The leased asset will revert to the lessor at the end of the 3-year period.
- The lessee's incremental borrowing rate is 10%.
- Both companies apply the straight-line method of depreciation. Salvage value is zero.
- Accounting year ends on December 31, for each party.
- Lessor's implicit interest rate (target rate of return) is 10%.

The lessee decided to terminate the lease agreement on January 1, 1999, before making the lease payment of Sh36,556. The fair market value of the asset on this date was Sh61,000.

Required:

Show the entries to terminate the lease agreement in the books of:

- a. the lessor (5 marks)
- b. the lessee (5 marks)

Question Five**(10 marks)**

- a. Current year net income for Cynmos International is Shs. 600,000. All year 1,000, 6%, Sh1,000 debentures were outstanding, each convertible to 20 common shares. The weighted average shares outstanding before considering potentially dilutive securities is 200,000, and the tax rate is 40%.
 - i. Calculate the EPS (3 marks)
 - ii. Calculate the dilutive EPS (3 marks)
- b. Assume Cynmos issued the debentures on October 1 (financial year ends on December 31). Calculate the dilutive EPS (4 marks)

Question Six**(10 marks)**

- a. Give the definition of a liability as per the Financial Accounting Standards Board (FASB) (4 marks)

- b. Explain **three** characteristics of a liability as per the definition in (a) above.(6 marks)