



THE CATHOLIC UNIVERSITY OF EASTERN AFRICA

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MAIN EXAMINATION

JANUARY – APRIL 2017 TRIMESTER

FACULTY OF COMMERCE

DEPARTMENT OF ACCOUNTING AND FINANCE

REGULAR PROGRAMME

CAC 322: ACCOUNTING FOR LIABILITIES

Date: April 2017

Duration: 2 Hours

INSTRUCTIONS: Answer Question ONE and any other TWO Questions

- Q1. a) Discuss the following terms as used in accounting for liabilities:
- i) Zero - interest bearing notes
 - ii) Accrued liabilities
 - iii) Unearned revenues **(9 marks)**
- b) Wells Fargo Bank agrees to lend some money to Lakehead Company in the form of a short term note payable and on January 1st, 2016, Lakehead Company signs a \$200,000, 10 percent, 12 - month note. The interest is payable semi-annually and the company's financial year end is 31st December. Prepare all journal entries necessary to record the cash received; interest expense and interest payable as at June 30th and December 31st and the payment at maturity on January 1st, 2017. **(6 marks)**
- c) List and describe in details at least **THREE** advantages of leasing over owning property. **(9 marks)**
- d) Broadway confectionary Ltd. a company that manufactures sweets, cakes and related items, on June 10, 2016, declared a

cash dividend of 50 cents per share on 900,000 shares payable July 16 2016, to all stockholders or shareholders of record or on the register, June 24, 2016. Write up the various entries required for the declaration and distribution of these dividends.

(6 marks)

Q2. On January 1, 2011, Warren Company issued Shs. 2,000,000 of 7% debentures dated January 1, 2011, which pay interest each December 31. The bonds matured on December 31, 2015. Daima Fidelity Company purchased the entire bond issue as an investment. Both companies have financial years running from January 1 to December 31. If the effective rate or market rate on similar bonds is 6%.

a) Record the issue of the bond in the books of the issuer and investor.

(6 Marks)

b) Using entries for the first two years and the interest method of amortizing interest, record the interest paid by the issuer and received by the investor for the bond investment.

(10 marks)

c) Using the information above define the following terms used in valuation of bonds:

i) Stated or coupon interest rate

ii) Market or effective interest rate

(4marks)

Q3. a) Discuss the difference between tax avoidance and tax evasion.

(4marks)

b) Trainers Ltd, a company involved with providing training in business management skills, had revenues of Shs. 300,000 for book purposes as at its financial year end, June 30, 2014 (its first year of operations) and Shs. 200,000 for tax purposes. It also had expenses of Shs. 100,000 for both book and tax purposes.

i) With a computation, how would Trainers Ltd report financial and taxable income for 2014?

(3 marks)

- ii) Assuming a tax rate of 40%, compute income tax payable **(3 marks)**
- iii) If the difference between the taxable income and financial income relates to accounts receivables or debtors as at 2014 and that the company expects to collect Shs. 60,000 of the receivables in 2015 and Shs. 40,000 in 2016, record in the books of Trainers Ltd the deferred tax consequences of the related receivables. Income tax payable for 2015 was Shs. 50,000 and for 2016 was Shs. 70,000. **(10 marks)**

- Q4. a) Very few companies pay dividends in amounts equal to their legally available retained earnings. What are the major reasons for this? **(10 marks)**
- b) Describe the following forms of dividend that may be offered to shareholders by a limited liability company. Accounting entries are not necessary.
- i) Property dividends
 - ii) Stock dividends **(5 marks)**
- c) Distinguish between preferred stock and ordinary or common stock. **(5 marks)**

END