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CPA INTERMEDIATE LEVEL

FINANCIAL REPORTING AND ANALYSIS

WEDNESDAY: 20 August 2025. Morning Paper. **Time Allowed: 3 hours.**

Answer ALL questions. Marks allocated to each question are shown at the end of the question. Show ALL your workings. Do NOT write anything on this paper.

QUESTION ONE

(a) International Public Sector Accounting Standard (IPSAS) 31 – "Intangible assets", requires intangible assets to be recognised if identifiable and controlled by the public entity.

With reference to the above statement, explain **TWO** components of identifiability as per IPSAS 31. (4 marks)

(b) When an entity transfers its product to a dealer or distributor for sale to end customers, it must determine whether the contract is a sale or a consignment arrangement.

In relation to the above statement, explain **TWO** indicators of a consignment arrangement. (4 marks)

(c) Zee Energy has entered into a contract with GasB Limited to purchase 100,000 units of gas at Sh.50 per unit. The contract allows Zee Energy to pay a penalty of Sh.15 per unit of gas that it does not purchase.

The market price of gas has fallen to Sh.30 per unit and Zee Energy has decided to invoke the penalty clause rather than pay the Sh.50 per unit. It is still contracted to buy 74,000 units of gas.

Required:
Determine the amount of provision that Zee Energy should make in its books of account. (3 marks)

(d) International Accounting Standard (IAS) 2 – "Inventory", provides guidance on the determination of cost and its subsequent recognition as an expense including any write down to net realisable value.

In relation to the above statement, highlight **THREE** situations in which net realisable value is likely to be less than cost. (3 marks)

(e) As at 31 December 2023, a plantation consisted of 100 insignis pine trees that were planted 10 years earlier. Insignis pine takes 30 years to mature and will ultimately be processed into building material for houses or furniture.

Only mature trees have established fair values by reference to a quoted price in an active market. The fair value (inclusive of current transport costs to get 100 logs to market) for a mature tree of the same grade as the plantation is:

	Sh.
As at 31 December 2023	171
As at 31 December 2024	165

The appropriate discount rate is 6% per annum.

Required:

(i) Estimate fair value of plantation as at 31 December 2023 and 31 December 2024. (4 marks)

(ii) Using suitable computation, explain the accounting treatment of the change in fair value in the year 2024. (2 marks)

(Total: 20 marks)

QUESTION TWO

(a) The consideration given by an investor to acquire an interest in an investee may be settled in different forms.

Required:

Identify **FOUR** forms of consideration that might be used to settle the interest in an investee. (4 marks)

(b) On 1 October 2024, Chui Ltd. acquired 80% of the ordinary shares of Swara Ltd. at a cost of Sh.2,570,000. On the same date, it also acquired 50% of Swara Ltd. 10% loan notes at par. The summarised draft financial statements of both companies are as follows:

Statement of profit or loss for the year ended 30 June 2025:

	Chui Ltd.	**Swara Ltd.**
	Sh."000"	**Sh."000"**
Sales revenue	15,000	6,000
Cost of sales	(10,500)	(5,000)
Gross profit	4,500	1,000
Operating expenses	(1,500)	(50)
Loan interest received/paid	18.75	(50)
Profit before tax	3,018.75	900
Income tax expense	(750)	(150)
Profit for the year	2,268.75	750

Statement of financial position as at 30 June 2025:

	Chui Ltd.	**Swara Ltd.**
	Sh."000"	**Sh."000"**
Non-current assets:		
Property, plant and equipment	4,830	2,000
Investments	2,820	-
	7,650	2,000
Current assets	3,750	2,000
Total assets	11,400	4,000
Equity and liabilities:		
Equity:		
Share capital	2,500	500
Retained earnings	6,400	2,100
	8,900	2,600
Non-current liabilities:		
10% loan notes	-	500
Current liabilities	2,500	900
Total equity and liabilities	11,400	4,000

Additional information:

1. The fair value of Swara Ltd.'s assets was equal to their book values with the exception of its plant, which had fair values of Sh.800,000 in excess of its book value at the date of acquisition. The remaining useful life of all of Swara Ltd.'s plant at the date of its acquisition was four years and this period has not changed as a result of the acquisition. Depreciation of plant is on a straight line basis and charged to cost of sales. Swara Ltd. has not adjusted the value of its plant as a result of the fair valuation of the assets.
2. In the post-acquisition period, Chui Ltd. sold goods worth Sh.3 million to Swara Ltd. These goods had cost Chui Ltd. Sh.2,250,000. During the year, Swara Ltd. managed to sell Sh.2,500,000 of the Sh.3,000,000 goods from Chui Ltd. for Sh.3,750,000.
3. The current accounts of the two companies were reconciled at the year end with Swara Ltd. owing Chui Ltd. Sh.187,500.
4. The goodwill was reviewed for impairment at the end of the reporting period and had suffered an impairment loss of Sh.75,000 which is to be treated as an operating expense.
5. Chui Ltd. and Swara Ltd. retained earnings as at 1 July 2024 were Sh.4,131,250 and Sh.1,350,000 respectively. No dividends were paid or declared by either entity during the year.
6. It is the group policy to value the non-controlling interest at acquisition at fair value. The directors valued the non-controlling interest at Sh.625,000 at the date of acquisition.
7. Revenue and expenses are deemed to accrue evenly throughout the year.

Required:

(i) Consolidated statement of profit or loss for the year ended 30 June 2025. (8 marks)

(ii) Consolidated statement of financial position as at 30 June 2025. (8 marks)

(Total: 20 marks)

QUESTION THREE

(a) A company enjoys a number of benefits over a partnership business enterprise. This is the reason as to why conversion of partnership to a company offers several advantages.

With reference to the above statement, explain **FIVE** advantages of converting a partnership into a limited liability company. (5 marks)

(b) James Mwala set up a business on 1 April 2024 in Nairobi with a branch in Mombasa. Purchases are made exclusively by Nairobi office where packaging and weighing occur. The branch handles packaged goods and these are charged thereto at packaged cost plus 10%. All sales by both branches are sold at a uniform gross profit of 25% on the packaged cost. The following details have been extracted from the business on 31 March 2025:

	Nairobi Head Office		Mombasa Branch:	
	Sh.	Sh.	Sh.	Sh.
Capital		2,640,000		
Drawings	300,000			
Purchases	23,920,200			
Cost of weighting and packing	415,800			
Sales		17,040,000		7,680,000
Goods sent to and received by branch		7,814,400	7,682,400	
Selling and sundry expenses	2,688,000		324,000	
Accounts receivable and accounts payable	2,760,000	7,000,200	1,104,000	28,800
Head office and branch current account	2,466,600			1,809,600
Balance at bank	1,944,000		408,000	
	34,494,600	34,494,600	9,518,400	9,518,400

Additional information:

1. Goods delivered by Nairobi office to Mombasa branch in March 2025 at Sh.132,000 were not received or recorded by the branch until 4 April 2025. A remittance of Sh.525,000 from the branch to Nairobi in March 2025 was not received until 2 April 2025.
2. Inventory taking at the branch disclosed a shortage of goods of a selling value of Sh.60,000. There was no shortage or surplus in Nairobi.
3. The cost of the inventory of unpacked goods in Nairobi as at 31 March was Sh.2,160,000.
4. All inventories are valued at cost to each entity and there was no loss or wastage in weighing and packaging.

Required:

(i) The valuation of closing inventory at the head office and branch. (6 marks)

(ii) The trading profit or loss account in columnar form for the year ended 31 March 2025 for the head office, branch and combined. (9 marks)

(Total: 20 marks)

QUESTION FOUR

(a) Explain **THREE** benefits of using common size approach in analysing financial statements compared to other methods. (6 marks)

(b) In reference to International Financial Reporting Standard (IFRS) 6 "Exploration for and Evaluation of Mineral Resources".

Explain **FOUR** conditions that must be met for exploration and evaluation expenditures to be recognised as assets. (4 marks)

(c) The following information was extracted from the books of the Ministry of TVET for the fiscal year ended 30 June 2025:

	Sh."million"
Transfer from exchequer	3,750
Fees and licenses	750
Liabilities for long term benefits	300
Long term borrowings	1,500
Finance cost	150
Supplies and consumable used	600
Wages and salaries	1,500
Other expenses	1,800
Transfer from other ministries	75
Transfer to other ministries	750
Computer equipment and software	400
Motor vehicles	350
Land and buildings	5,250
Revenue from exchange transactions	150
Other revenues	900
Payables	750
Reserves	2,700
Accumulated funds	1,125
Cash and cash equivalent	750
Receivables	300
Inventory of consumables	150

Required:

(i) Statement of financial performance for the year ended 30 June 2025. (5 marks)

(ii) Statement of financial position as at 30 June 2025. (5 marks)

(Total: 20 marks)

QUESTION FIVE

The following trial balance relates to Flex Limited as at 31 March 2025:

		Sh."000"	**Sh."000"**
Equity shares of 50 cents each			45,000
Share premium			5,000
Retained earnings (1 April 2024)			5,100
Property at cost		48,000	
Plant and equipment at cost		47,500	
Accumulated depreciation:	Property (1 April 2024)		16,000
	Plant and equipment (1 April 2024)		33,500
Inventories (31 March 2025)		25,200	
Trade receivables		28,500	
Bank			1,400
Deferred tax			3,200
Trade payables			27,300
Revenue			350,000
Cost of sales		298,700	
Lease payments		8,000	
Selling expenses		16,100	
General and administrative expenses		26,900	
Bank interest		300	
Current tax		800	
Suspense account			13,500
		500,000	500,000

Additional information:

1. Suspense account represents the corresponding credit for cash received for a fully subscribed rights issue of equity shares made on 1 January 2025. The terms of the share issue were one new share for every five held and at a price of Sh.0.75 each. The market price of the company's equity shares immediately before the issue was Sh.1.20 each.
2. Non-current assets: Property had 12-year useful life on acquisition. To reflect a marked increase in property prices, Flex Ltd. decided to revalue it on 1 April 2024. The fair value of the property at that date was Sh.36 million. Flex Ltd. has not yet recorded the revaluation. The remaining useful life of the property is eight years at the date of revaluation. Flex Ltd. makes an annual transfer to retained earnings to reflect the realisation of the revaluation surplus. In Flex Ltd.'s tax jurisdiction, the revaluation does not give rise to a deferred tax liability.
3. On 1 April 2024, Flex Ltd. acquired an item of plant under a lease agreement that had an implicit interest rate of 10% per annum. The lease payments in the trial balance represents an initial deposit of Sh.2 million paid on 1 April 2024 and the first annual rental of Sh.6 million paid on 31 March 2025. The lease agreement requires further annual payments of Sh.6 million on 31 March each year for the next four years. The plant was initially measured at Sh.25 million on 1 April 2024.

   Plant and equipment (other than leased plant) is depreciated at a rate of 20% per annum using reducing balance method. No depreciation has yet been charged on non-current assets for year ended 31 March 2025. Depreciation is charged to cost of sales.
4. In the month of March 2025, internal audit in Flex Ltd. discovered a fraud committed by the company's credit controller who did not return from a sabbatical leave. The fraud revealed that Sh.4 million of the company's receivables had been stolen by the credit controller and are not recoverable. Of this amount, Sh.1 million relates to the year ended 31 March 2024 and the remainder to the current year. This fraud was not insured.
5. Flex Ltd. income tax calculation for the year ended 31 March 2025 shows a tax refund of Sh.2.4 million. The balance on current tax in the trial balance represents the under/over provision of the tax liability for the year ended 31 March 2024. As at 31 March 2025, Flex Ltd. had taxable temporary differences of Sh.12 million (requiring a deferred tax liability). The income tax rate of Flex Ltd. is 25%.

Required:

(a) Prepare a statement of profit or loss and other comprehensive incomes for the year ended 31 March 2025. (8 marks)

(b) Prepare statement of changes in equity for the year ended 31 March 2025. (5 marks)

(c) Prepare statement of financial position as at 31 March 2025. (7 marks)

(Total: 20 marks)

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