

FINANCIAL REPORTING PRACTICES

IN KENYAN PUBLIC COMPANIES

//
A Survey of Published Annual Reports of 58 Kenyan
Public Companies for the Fiscal Years Ended in
1974, 1975, and 1976. //

By

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A thesis submitted in part fulfilment for the
degree of Master of Business Administration
(M.B.A.) in the University of Nairobi.

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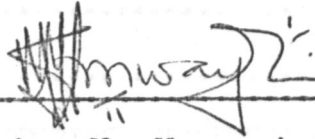
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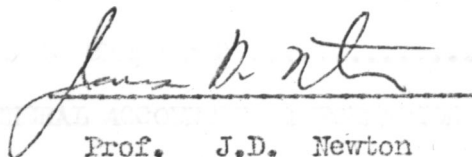
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A handwritten signature in black ink, appearing to read "Amwayi". The signature is written over a horizontal line and includes some scribbled-out text on the left side.

Francis M. M. Amwayi

This thesis has been submitted for examination with my approval as University Supervisor

A handwritten signature in black ink, appearing to read "J.D. Newton". The signature is written over a horizontal line.

Prof. J.D. Newton

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A B S T R A C T

The accounting field is full of many acceptable ways and methods of doing things: there are many ways of treating and accounting for certain items of accounts, many varieties of reporting formats, etc. All these are summed up in what is normally referred to as "Generally Accepted Accounting Principles (GAAP)". The accountant is therefore faced with the problem of choosing, from the many acceptable ways and methods, the way or method to use in any particular situation. It is also true that accounting or financial reporting practices have been changing over time. These changes have been brought about by several factors which include the following:

- (1) Recommendations by accounting bodies all over the world, including recommendations by individual accountants;
- (2) Changes in the legal requirements and statutes governing accounting and financial reporting practices; and
- (3) Changes in the business world that affect accounting and financial reporting practices either directly or indirectly.

This thesis presents the results of a survey study of the published annual reports of 58 Kenyan public companies for the fiscal years ended in 1974, 1975 and 1976. The survey was aimed at examining the financial reporting practices followed by the 58 companies over the three year survey period. The thesis analysis covers matters such as types of financial statements presented, form and terminology used, accounting treatment of some of the various transactions and items reflected in the

statements, form and content of the auditors' report, and some other general accounting information relating to the survey companies. Particular emphasis has been placed on the requirements of the Companies Act, and references are made to the Act from time to time in the discussion of most of the survey items. Examples are given in the thesis from the published annual reports in order to highlight some points made in discussion of some of the survey items.

The thesis starts, in Chapter 1, by introducing the reader to the theoretical framework within which accounting practice operates. A statement of the purpose of the thesis is also made in this Chapter. Chapter 2 discusses the methods used in collection and analysis of the data for the thesis, and also gives some general information on the 58 survey companies. Survey results are presented in Chapters 3 and 4. Chapter 3 deals mainly with the survey relating to general accounting information, while Chapter 4 deals with the Balance Sheet and the Profit and Loss Account. Chapter 5 contains a summary of the main survey findings and possible conclusions on the survey results. The last part of Chapter 5 makes recommendations as to the possible ways of improving accounting and financial reporting practice in Kenya, and suggests possible areas of further research and study in the field of accounting in Kenya.

ACKNOWLEDGEMENTS

Thanks are due to the many individuals and organizations who contributed directly or indirectly to make this thesis possible.

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I cannot forget my mum, Ziporah, and my late dad, Alex Amwayi (God bless his soul), for their moral and financial support, patience, and forbearance during my time of study. To all friends and relatives who have been encouraging me all along, I say THANK YOU.

F.M.A

CHAPTER 1

INTRODUCTION, STATEMENT OF THE PROBLEM, AND RELATED LITERATURE

The purpose of this chapter is to introduce the reader to the theoretical framework within which accounting practice operates, and to state, as well, the purpose of this thesis as a whole. A point is made that there are many generally accepted accounting principles which can be followed by companies in the preparation and dissemination of financial reports. This thesis is in the form of a survey to find out which of these generally accepted accounting principles are being practised by companies in Kenya. The survey centres mainly on the financial reporting practices followed by 58 Kenyan public companies, all of which are listed on the Nairobi Stock Exchange. The first part of the chapter is an introduction. The second part is a statement of the problem and purpose of the thesis. And the last part deals mainly with a review of the related literature.

1.1. Introduction

The business world is a world of alternatives. There are many alternative business investments, many alternative techniques of managing or running a business, many alternative ways of accounting for economic realities, etc. Decisions are there-

fore always being made as to which alternative should be chosen in a given situation. Whichever alternative chosen, it is aimed at achieving certain objectives of the decision maker.¹ The economists will talk about "scarcity and choice", that is, because resources are scarce, a choice must necessarily be made in such a way that will result in an efficient allocation of the resources. The allocation of scarce resources by choosing from a set of competing alternatives is done with the objective of "maximising utility"². It is, however, necessary to add that the term "utility", or satisfaction, must be defined in broad terms in order to include the impact of the chosen alternative on the environment within which the choice process is made, as well as the impact of the environment on the chosen alternative. In other words, a choice has more to it than achieving maximum satisfaction of the individual decision maker. The choice process does not happen in a vacuum, under its own rules. The environment has "rules" which must also be taken into account. This is true in any choice situation - even when it comes to choosing the accounting and financial reporting practices to be followed.

Decisions are normally made in the light of the information available to the decision maker about the choice object. In the business world, accounting has become a major source of information about business. It is not uncommon to find accounting being described as "the language of business"³.

Accountants all over the world are engaged in what is basically a system of communication, that is, they are trying to devise better ways of providing information that can be used by interested parties for decision making.⁴ Financial statements can therefore be looked at as a language with which accountants or company management communicates with parties interested in the status and operations of the firm. This is why Ross says:

"... no statement, however, ingenious or logically put together has any merit whatever unless it communicates useful information - that is to say unless it helps someone to make a decision."⁵

And so accountants have been arguing for a long time as to how to present useful or, at least, better financial statements.

Tradition in accounting practice has resulted in what is commonly referred to as "Generally accepted accounting principles".⁶ While accountants, auditors, courts, government authorities, etc., recognize the existence of generally accepted accounting principles, it is difficult to list exhaustively what these principles are.⁷ It seems that these principles develop depending on what is considered to be the most important objectives of financial reporting at any point in time.⁸ General acceptance will therefore depend on what any particular group considers to be the general objective of financial reporting.⁹ The various groups that may determine general acceptance include the government, professional accounting bodies, financial institutions, individuals, and the public

at large. These various groups act as sources of the so called GAAP and they influence the trends in financial reporting.¹⁰

Accounting practice in any country is done within the framework of the laws of that country. In almost all countries there are statutes that govern accounting practice, and, in some cases, there are bodies established by legislatures to regulate accounting practice in these countries. In U.S.A. for example, the Securities and Exchange Commission (SEC) plays an important part in the development of accounting principles followed by companies. In addition to the legal requirements, in countries with well developed professional accounting bodies - like U.S.A., Britain, Canada, Australia - the main source of accounting principles seems to be these professional accounting bodies, which, in most cases, control the accounting practice in these countries.¹¹ Adherence to rules and standards which are set from time to time by these professional bodies lead to what become generally accepted as accounting principles. In most developing countries with no established professional accounting bodies, accounting practice is, to a large extent, controlled by Law or Acts of Parliament. In most cases these developing countries depend on the pronouncements and suggestions of professional accounting bodies in the developed countries in enacting laws that govern the accounting practice, or, as it often happens, they inherit the laws and practices of their former Colonial Masters.¹²

One may safely conclude that the accountants in these developing

countries have a wide choice of accounting practices which may be adopted from the developed countries provided the practices chosen meet the requirements of the government statutes.

In Kenya the Companies Act, Cap. 486 of the Laws of Kenya,¹³ stipulates, in broad terms, the accounting procedures to be followed by Companies operating in Kenya. Companies have, however, a wide range of financial reporting practices from which to choose. The choice of terminologies, styles of reporting, treatment of items of account, etc., is in most cases, left to the companies concerned. And since there is a wide variety of accepted accounting procedures, terminologies, styles, etc. to choose from in the accounting profession all over the world, one would expect that accounting practices would differ from firm to firm depending on several factors which may include:

- (1) The home country of the company, that is whether the company is a branch of a parent company incorporated in the U.S., Britain, etc.
- (2) Where the accountants who man the company accounts were educated (with their resulting biases). Here too we may include the impact of recommendations of professional accounting bodies to which these company accountants belong.
- (3) Flexibility in the wording and requirements of the Cos. Act.
- (4) Tax requirements as well as the requirements of other

institutions such as banks and stock exchanges.

1.2 Statement of the Problem and Purpose of the Thesis

The above discussion indicates that there is a wide range of accepted accounting and financial reporting practices that could be followed by companies.¹⁴ It is also true that accounting practices change from time to time due to forces in the accounting profession itself, forces in the environment of accounting, forces in the business world affecting the company concerned, etc. Companies at times find it necessary to change from one accounting practice and adopt another due to these forces.

In some countries like Canada, Britain, the U.S.A., a study and analysis of published annual reports of companies is made and published.¹⁵ These publications in the various countries show the accounting practices followed by companies operating in these countries, and reveal any changes and trends in the accounting and financial reporting practices. Such publications of financial reporting practices may help in several ways, such as:

- (1) Helping the professional accounting bodies in these countries in the formulation of accounting standards to be followed. Formulation of standards must take into account what is in practice. This may indicate what those in the accounting field consider to be

acceptable or best in the environment.

- (2) Helping the governments in these countries and other interested parties like financial institutions in finding out what practices are being followed by the various companies.
- (3) Helping the companies concerned to see whether and how their practices differ from each other.
- (4) Helping the academic institutions involved in the teaching of accounting - as a guide to the actual practice in firms.

In Kenya, at the moment, there is not a publication that studies financial reporting practices followed by Kenyan firms.

The purpose of this thesis is to make a study survey of the financial reporting practices followed by public companies in Kenya. The study analysis is intended to cover areas in the accounting field including matters such as:

- (1) the types of financial statements presented,
- (2) the form and terminology used,
- (3) the accounting treatment of various transactions and items reflected in the statements,
- (4) the form and content of the auditors report,
- (5) the effect, or otherwise, on financial reporting practices of environmental changes e.g. Inflation and recommendations of various accounting bodies such as the American Institute of Certified Public Accountants (AICPA), the Canadian

Institute of Chartered Accountants (CICA) etc.,

(6) application of some specific requirements of the Cos. Act.

The study is also designed to find out whether there is a standardized way of financial reporting in Kenyan firms, that is, whether

- (1) the companies selected for the study use identical styles in reporting,
- (2) they use the same terminology for the various accounting items,
- (3) the treatment of the various accounting items in the various firms follows the same procedures, and
- (4) the content and form of the auditors report is the same for all firms audited.

Since practices change over time, the study will also examine the trend of accounting and financial reporting practices in the survey companies over the survey period (1974-1976), and note any specific changes that have occurred over this period of time.

1.3 Related Literature

As already stated above, there is no publication that surveys financial reporting practices in Kenya at the moment. The only publications in Kenya on accounting that may relate indirectly to the area of study covered by this thesis include the following:

- (a) There was an annual publication by the Nairobi Stock Exchange entitled "Nairobi Stock Exchange Official Year Book."¹⁶ In this booklet they give a summary of the financial reports of companies listed on the stock market. Major information given include a summary of the balance sheet of each of the companies listed, a summary of the profit and loss account, some points from the directors report, and explanatory notes on the information given in the booklet. The information regarding individual companies included in this publication is obtained from published annual reports of the companies.
- (b) A thesis dissertation for a Master of Business and Administration degree of the University of Nairobi by S.C. Masita¹⁷ which relates indirectly to this study. In this thesis, Masita traces out the development of accounting and the accounting profession, particularly in Britain and U.S.A., and its application to East Africa - or its impact on the development of accounting in East Africa. This is mainly a historical survey of the accounting profession and it does not deal very much with accounting or financial reporting practices in East Africa - or Kenya.
- (c) A study by Adolf J.H. Enthoven¹⁸ also relates indirectly to this study. In his study, Enthoven

tries to evaluate the accountancy systems, developments and requirements in some African countries -- Tanzania, Zambia, Kenya, Uganda, Ethiopia, Ghana, Nigeria and Zaire. The analysis that relates to Kenya in this book is mainly an outline of the accounting requirements, particularly as regards accounting manpower planning. It does not deal with accounting and financial reporting practices in Kenya.

The analysis and presentation of the material in this thesis is based mainly on two publications mentioned above by the AICPA¹⁹ and CICA²⁰. The AICPA publication is a series of annual publications which started in 1946, and makes an annual study of the accounting trends and techniques in published annual reports of U.S.A. companies. The CICA publication, a programme introduced in 1955, is published after every two years and summarises the trends and latest developments in financial reporting in Canadian companies. The approach to the studies in these two publications is basically the same: An analysis is made to show such accounting matters as the financial statements presented, how many companies use particular practices, etc. This thesis takes the same approach of analysis and presentation in Chapters three and four. Chapter two deals mainly with the method used in the collection and analysis of the data for this thesis, as well as some general information on the survey companies. Chapter three presents a survey and discussion of some general

accounting information that cannot be logically included with the discussion of either the balance sheet or the Income statement (Profit and Loss Account). These two financial statements (Balance Sheet and the Profit and Loss Account) are discussed in Chapter four. Chapter five concludes the thesis by drawing out a summary of findings and conclusions, and giving some recommendations - policy recommendations as well as recommendations for further study and research in the accounting field in Kenya.

FOOTNOTES TO CHAPTER 1

1. It may be noted here that whoever the decision maker is -- Management, investor, creditor, accountant, etc. -- the process involved in choosing among competing alternatives is basically the same. However, the decision maker discussed in this thesis is the company accountant or Management who is involved in choosing from among the many available accounting and financial reporting practices, which practices to follow. The accountant is in this case actually trying to reflect and communicate economic reality of the firm to interested parties, and the way or method chosen to do this reflects what the accountant or management thinks to be the best.

2. A good discussion on "scarcity and choice" and "Maximisation of Utility" is given in most basic economics textbooks. For example see Michael J. Brennan, Theory of Economic Statics, 2nd Ed. (Englewood Cliffs, N.J.: Prentice Hall, Inc., 1970), pp. 3-6 and pp. 45-49.

3. See for example Howard Ross, The Elusive Art of Accounting, (New York: The Ronald Press Co., 1966), pp. 57-75.

4. It is assumed here that the interested parties use the accounting information for making decisions concerning the accounting entity.
5. H. Ross, P. 58
6. The term "principle" is sometimes referred to as postulates, standards, basic assumptions, basic concepts, axioms, or conventions in various accounting textbooks. Whichever term is used, it refers to the fundamental notions upon which accounting practice is based. ("Generally Accepted Accounting Principles" is hereafter cited as GAAP)
7. Several authors including professional accounting bodies like the American Institute of Certified Public Accountants (AICPA) have tried to make a list of what they consider to be the GAAP, as well as defining the basic postulates of accounting. See for example Maurice Moonitz, The Basic Postulates of Accounting, Accounting Research Study No. 1. (New York: AICPA, 1961), and Maurice Moonitz and Robert T. Sprouse, A Tentative Set of Broad Accounting Principles for Business Enterprises, Accounting Research Study No. 3 (New York: AICPA, 1962). These two studies were aimed at defining the basic postulates of accounting (fundamental notions of accounting). A list of GAAP is given by Paul Grady,

Inventory of Generally Accepted Accounting Principles for Business Enterprises, Accounting Research Study No. 7

(New York: AICPA, 1965)

It is, however, difficult to say "what constitutes general acceptance, either by whom or to what extent", as Arthur Andersen & Co. puts it in Accounting and Reporting Problems of the Accounting Profession, 2nd Ed. (Arthur Andersen & Co., 1962), p. 1. There is still a controversy as to what are generally accepted accounting principles because what may be accepted in one situation or firm may not be accepted in another. See also G.A. Lee, Modern Financial Accounting. (London: Nelson & Sons Ltd., 1973), p. 3. Note also that statements by the Financial Accounting Standards Board (FASB) are attempts to define GAAP.

8. A good discussion on the objectives of financial statements is given by Arthur Andersen & Co., Objectives of Financial Statements for Business Enterprises, (Arthur Andersen & Co., 1972). See also the following studies on the objectives of financial statements:
- (a) W.J. Kenley and G.J. Staubus, Objectives and Concepts of Financial Statements, Accounting Research Study No. 3. (Melbourne: Accounting Research Foundation, 1972).
 - (b) Objectives of Financial Statements: Report of the Study Group on the Objectives of Financial Statements.

(c) The Corporate Report, (London: Accounting Standards Steering Committee, 1975)

9. Arthur Andersen & Co., Accounting and Reporting Problems of the Accounting Profession, Op. Cit., says that "a comprehensive and co-ordinated structure of accounting theory is necessary for the development of accounting principles" (p. 1). It is, however, necessary to know which comes first - either accounting principles or a "comprehensive and coordinated structure of accounting theory". It seems that the structure of accounting theory is a result of the development of accounting principles which become generally accepted by a particular group.

Arthur Andersen & Co. continues to argue that "new development in accounting principles and related practices, in general, go through transitional periods as a result of an evolution process" (p.3). Five general phases of this process are listed on the same page.

10. P.N. McMonnies argues that there is a "possible conflict as a result of proliferation of accounting requirements by an increasing circle of legislating bodies." See P.N. McMonnies, "EEC, UEC, ASC, IASC, IASG, ICCAP - IFAC, Old Uncle Tom Cobbleigh and all," Accounting and Business Research, No. 27 (Summer 1977), p. 162.

He contends that "... unless a lot of research is done to establish a fundamental framework for financial reporting, standards [Accounting principles] will always be 'rule of thumb' and therefore unacceptable to some people" (p. 164). The current controversy in the accounting profession as regards generally accepted accounting principles seems to support McMonnies' philosophy.

11. Examples of these professional accounting bodies include:
 - (a) The American Institute of Certified Public Accountants (AICPA),
 - (b) The Institute of Chartered Accountants in England and Wales,
 - (c) The Canadian Institute of Chartered Accountants (CICA),
 - (d) The Institute of Chartered Accountants in Australia, etc.

12. See a discussion by Thomas W. Lelievre, "Accounting in the Third World", Journal of Accountancy, (January 1978), pp. 72-75

13. Referred to as "The Companies Ordinance" in the Laws of Kenya, Chapter 486. In this thesis analysis reference is made to the Companies Ordinance Cap. 486 of the Laws of Kenya as revised in 1962 (Hereafter cited as the "Cos. Act")

or "The Act").

14. As Robert G. May, Gerhard G. Mueller, and Thomas H. Williams, say, "The reporting process is a complex one, involving a variety of reporting formats and numerous legal requirements ...

"The content of the annual financial report will vary among corporations, but for corporations that are 'publicly held', certain inclusions have evolved as a matter of law, listing requirements and/or accounting policy." See Robert G. May, Gerhard G. Mueller, and Thomas H. Williams, A New Introduction to Financial Accounting. (London: Prentice Hall, Inc., 1976), pp. 538-539.

15. Examples of such publications include:

- (a) AICPA, Accounting Trends and Techniques: An Annual Survey of Accounting practices followed in stockholder Reports. This is published annually.
- (b) CICA, Financial Reporting in Canada: A Summary of Financial Reports of Canadian Public Companies. This is published after every two years.
- (c) Survey of Published Accounts, A study sponsored by the Research Committee of the Institute of Chartered Accountants in England and Wales and published by the Institute's Trustees of Chartered

Accountants' Trust for Education and Research. (This is quoted in CICA, Financial Reporting in Canada, 1973, preface and throughout the CICA study. It was not possible to get a copy of this publication, although inquiries reveal that, like the AICPA publication above, this is published annually)

16. Nairobi Stock Exchange Official Year Book, (Nairobi: Committee, Nairobi Stock Exchange). This used to be published annually but has since the last publication in 1972 ceased to be published. However, the secretaries to the Nairobi Stock Exchange say that the publication of the same is to be resumed "soon."
17. S.C. Masita, The Development of Accounting and the Accounting Profession and its Application to East Africa. Unpublished M.B.A. Thesis, University of Nairobi (1976)
18. A.J.H. Enthoven, An Evaluation of Accountancy Systems, Developments and Requirements in Africa: Appraisal Report, Ford Foundation Sponsored study project. (Chapel Hill, North Carolina: University of North Carolina, February, 1975).
19. AICPA, Accounting Trends and Techniques, Op. Cit., (References in this thesis are to the 1976 publication).

20. CICA, Financial Reporting in Canada, Op. Cit., (References in this thesis are to the 10th Ed. 1973. It was not possible to get a more recent publication due to the time constraint).

CHAPTER 2

METHODOLOGY AND GENERAL INFORMATION ON THE

SURVEY COMPANIES

The purpose of this chapter is to present the method used in the collection and analysis of data for this thesis. Included in the chapter is also an outline of the items selected for the survey as well as a general discussion on the survey companies.

2.1 METHODOLOGY

2.1.1 Sources of data and information

As already stated in Chapter 1, this thesis makes a study survey of the financial reporting practices followed by Kenyan public companies. It therefore follows that private companies are not included in the survey since the private companies do not normally publish their financial reports. Subsection (1) of section 30 of the Cos. Act defines a private company as "a company which by its articles -

- (a) restricts the right to transfer its shares, and
- (b) limits the number of its members to fifty, not including persons who are in the employment of the company and persons who, having been formerly in the employment of the company, were while in that employment, and have continued after the determination of that employment to be, members of the company; and
- (c) prohibits any invitation to the public to subscribe for

any shares or debentures of the company."

For the purpose of this thesis, a public company may be defined as a company which is not a private company as defined in the Cos. Act.

The main source of the data and information for this thesis was the published financial reports of 58 Kenyan public companies all of which are listed on the Nairobi Stock Exchange (Listed as of June 30th, 1978). The list of the 58 survey companies is given in Appendix A at the end of this thesis.

At the time of the study survey both the University's Main Library and the Faculty of Commerce Library had a very limited number of the relevant financial reports. It was therefore necessary to devise a method of getting the missing statements. Several alternatives were available:

- (a) Go personally to these companies and ask them for the statements,
- (b) Write to these companies to get the required statements, or
- (c) Get Xerox copies of the statements from either the Nairobi Stock Exchange or the Registrar of Companies.

The second alternative was chosen because this appeared a cheaper, more practical alternative as compared to the other two. A number of companies responded by sending in their financial reports. To complete the data collection the third alternative was used. Some of the statements were missing at the Nairobi Stock Exchange and these were found at the Registrar of Companies.

It may be mentioned here that at first over 100 companies selected randomly from a list of companies at the Registrar of Companies were requested, in writing, to submit their financial reports. A number of these companies responded by sending in their financial reports. Of the companies that sent in their financial reports, it was found out that most of them were the companies listed on the Nairobi Stock Exchange. Most of the non-listed companies responded negatively by saying that they could not submit their reports. It was therefore found fitting to take only the companies listed on the Nairobi Stock Exchange as the population for this survey.

It was also found that companies leave and some are newly listed on the Stock Exchange from time to time, that is, the list of companies listed on the Stock Exchange changes from time to time. To be therefore consistent as regards the chosen population, a date was chosen - June 30th, 1978 - as the date to determine the number of the listed companies. The survey was thus based on the number of companies listed on the Nairobi Stock Exchange as of this date. As of this date, 60 companies were listed. Of the listed companies, one company was incorporated as a public company in 1976 and had no financial reports for 1974 and 1975. Since statements for all the survey years (1974, 1975 and 1976) were required for the survey, this particular company was excluded from the survey. Another company was in the process of winding up and it was not possible to get the required financial reports of this company.

This too, was excluded from the survey thus leaving the number of companies included in the survey at 58. To give some light as to the trend over time in the financial reporting practices followed by these survey companies, a time period of three years (1974, 1975 and 1976) was taken as the survey period.

The other main source of information was the Companies Act. This Act gives some guidelines as to the financial reporting practices to be followed by companies operating in Kenya.

2.1.2 Treatment of data

As will be noted in the two subsequent chapters, the approach taken in the analysis of the data and information found in the financial reports of the survey companies was mainly the tabular form. An examination of selected financial reporting practices discussed in this thesis was made for each of the survey companies over the survey period of three years (1974-1976). For each item discussed a table was prepared showing the number of companies (Both in absolute and percentage terms) that used such a practice in each of the three years. This tabulation was aimed at:

- (1) Showing what financial reporting practices prevailed in each of the years of the survey period.
- (2) Showing the trend in the use of any of the practices surveyed over the survey period, that is, whether there is an increase or decrease over the years in the number

of companies using a particular financial reporting practice.

- (3) Showing the general nature of financial reporting practices in the survey companies, that is, to help in drawing a conclusion as to what financial reporting practices seem to be generally accepted in the survey companies.
- (4) Showing any new practices adopted by the companies over the survey period. This may reflect the impact of the changes in the accounting professional requirements in other countries, or changes in the accounting environment -- both legal or otherwise.

In analysing the survey data, it was assumed that the accounting practice in Kenya works mainly within the framework of the requirements of the Cos. Act. Consequently, reference is made from time to time to the requirements of the Act in the discussion of some of the items discussed in this thesis. Reference is also made to the practices followed in other countries like Britain, Canada and the U.S.A., as revealed in the publications in these countries quoted in Chapter 1. For some items discussed, referenced is also made to what some writers in the field of accounting think to be the appropriate practice.

2.1.3 Basic Assumptions

Since this thesis is mainly a survey and presentation of the financial reporting practices followed in Kenyan firms, it

was not found necessary to advance any working hypothesis. However, certain assumptions were made in the course of the analysis of the data. These include the following:

- (1) Financial reporting is mainly a process of communicating information about the status and operations of the firm to interested parties external to the firm. It is therefore assumed here that the practices followed by the companies in their financial reporting are the practices that the companies consider appropriate to communicate better to the external parties, information about the status and operations of the companies.
- (2) Accounting practice in Kenya is done within the limits of its environment. We may take the environment within which accounting practice operates to be the requirements of the law as well as the requirements of the accounting profession itself. It therefore follows that since there is no established and active professional accounting body to regulate accounting practice in Kenya,¹ most of the practices in firms depend on the requirements of the Cos. Act. At the same time it may be rightly assumed that companies are free to adopt any accepted accounting practice or recommendations from international accounting bodies so long as the minimum requirements of the Cos. Act. are met.

2.1.4 Items Selected for Survey

It is evident that accounting is a wide field, and although this survey study is designed to determine the financial reporting practices in the survey companies, it is difficult to cover every aspect of accounting or financial reporting in a single study. In chapter 5 recommendations are given as to the possible areas of further study, which include the areas and items left out by this survey. This thesis dealt mainly with items which were considered by the author as being the "highlights" in financial reporting. The following is an outline of the survey items discussed in chapters 3 and 4.

The items discussed in Chapter 3, which deals mainly with general accounting information, include the information required by the Cos. Act to be included in the annual reports to shareholders, the fiscal year end of the survey companies, the use of the Swahili language in financial reporting, the presentation of comparative statements in the reports, the disclosure of accounting policies, the notes to financial statements, the presentation of supplementary financial data, inflation accounting and the auditors' report.

The Balance Sheet and the Profit and Loss Account items are discussed in Chapter 4. Items discussed in this chapter include the title and format of the Balance Sheet and the Profit and Loss Account; some current asset items like cash, debtors, and stocks; fixed assets; investments; deferred taxation; long term liabilities; shareholders' equity; revenue

from operations; expenses; and the depreciation methods used.

In the discussion of some of these items examples are presented from the published reports of the survey companies in order to highlight some of the points made in the discussion.² In some of these examples comparative figures for the previous year have been left out for convenience.

2.2. COMPANIES SELECTED FOR SURVEY

2.2.1 Industrial Classification

As already stated, all the companies included in this survey were selected from those listed on the Nairobi Stock Exchange as of 30th June, 1978. Table 2(a) gives a classification by industry of the 58 survey companies. While it is not easy to see from the table what exact business a company deals in, it is necessary to note that most of the companies are widely diversified in operations,³ and it is not uncommon to find a company like B.A.T. (Kenya) Ltd. dealing in poultry in addition to its main line of business operations - tobacco products. Looking at table 2(a) this statement may seem contradictory, taking into account the number of companies listed under "widely diversified or not otherwise classified". This is because the classification was based on what forms the dominant business activity of each of the companies - i.e. a business activity that forms over 50 per cent of all the company's business. Where a company deals in several activities

such that none of them forms its main or dominant business activity it was listed under "widely diversified or not otherwise classified".

Table 2(a) shows that most of the companies -- over 41 per cent are in the manufacturing sector of the economy. The Agricultural sector follows with over 25 per cent of the companies; then other services including dry cleaning, transportation, warehousing and other utilities, and tourism and hotel, follows forming about 13 per cent. The remaining sectors include financial institutions, trading companies and other companies not otherwise classified.

Table 2(a) - Industrial Classification of the Survey Companies

	No. of Companies	Per- centage
<u>Manufacturing:</u>		
Food - including flour milling and fruit canning	6	
Beverage	2	
Tobacco products	1	
Rubber products	1	
Wood, paper and allied products	3	
Printing, publishing and allied	2	
Cement	2	
Electric products	3	
Petroleum products	1	
Chemicals and Chemical products	2	
Sisal and jute products	1	
Total Manufacturing	24	41.38
<u>Agriculture:</u>		
Coffee and Tea	10	
Ranching, pig and allied products	5	
Total Agriculture	15	25.87
<u>Trading:</u>		
Motor distribution and allied	3	5.17
<u>Financial Institutions, including</u>		
Insurance Companies, hire purchase companies	5	8.62
<u>Other Services:</u>		
Dry cleaning	1	
Transportation, Warehousing and other utilities	3	
Tourism and Hotel	4	
Total Other Services	8	13.79
<u>Widely diversified or not otherwise</u>		
Classified	3	5.17
Total Number of Companies	58	100.00

2.2.2 Size of the Survey Companies

If the size of a company is defined in terms of the share capital invested,⁴ table 2(b) gives the relative sizes of the survey companies. The table is based on the share capital of the companies as reflected in the 1976 financial reports.

Table 2(b) Size of the Survey Companies Based on Share Capital
As of 1976

	No. of Companies	Per-centage
Less than or equal to £500,000	29	50.00
Between £500,000 and £1,000,000	12	20.69
Between £1,000,000 and £1,500,000	6	10.34
Over £1,500,000	11	18.97
Total	58	100.00

The table shows that the majority of the survey companies (81.03%) have share capital of less than £1,500,000. Of those companies with share capital over £1,500,000, three companies -- E.A. Breweries Ltd., Booke Bond Liebig Kenya Ltd., and E.A. Power and Lighting Co. Ltd., had share capitals of £12,342,894; £9,775,000; and £9,741,504 respectively.

2.3 CONCLUSION

This chapter has dealt mainly with the methods used on the collection and analysis of the data and information for this thesis, items selected for survey, and some general discussion on the survey companies. It has been noted that all the 58 survey companies are public companies listed on the Nairobi Stock Exchange as of 30th June 1978.

An industrial classification of the survey companies as well as their relative sizes was given in the chapter. In the discussion of the survey items it was noted that not all items that relate to accounting were included in the survey. Chapter 3 begins the presentation of the survey on some of the survey items, and deals mainly with general accounting information that cannot be logically included with the discussion of either the Balance Sheet or the Profit and Loss Account items discussed in Chapter 4.

FOOTNOTES TO CHAPTER 2

1. Although up to the time of writing this thesis steps have been taken toward establishing a professional accounting body in Kenya, this body has not reached the stage where it can be in a position to actively regulate accounting practice.
2. It should be mentioned here that the examples presented are those which, in the opinion of the author, highlights some of the points made in the discussion of the related items. They are designed to show the reader some of the actual practices discussed, and are not necessarily what the author considers to be either good or bad practice.
3. The nature of business of some of the companies is given, in brief for each company, in (1) The Nairobi Stock Exchange Official Year Book, 1972; (2) Central Bureau of Statistics, Directory of Industries, 1974. (Nairobi: Government Printer, 1974); and (3) Unpublished compiled report on some of the listed companies by J.S. Donovan & Co. Ltd. and Dyer & Blair Ltd.; Brokers to the Nairobi Stock Exchange, 1976.

An examination of these sources shows that the companies fairly maintained their main or dominant business activities over the survey period.

4. Other widely used measures of company size include:
- (a) the number of employees, (b) the area occupied (Company premises), (c) the number of subsidiaries, (d) the sales volume, etc.

CHAPTER 3

GENERAL ACCOUNTING INFORMATION

This chapter presents a survey and discussion of some general accounting information that cannot be logically included with the discussion of any of the customary financial statements (Balance Sheet and Profit and Loss Account) discussed in chapter 4. The information relates to the 58 survey companies and includes such matters as the information required by the Cos. Act to be included in annual reports to stockholders (shareholders), fiscal year end, the Swahili language version of financial reports, presentation of comparative statements, disclosure of accounting policies, notes to financial statements, the presentation of supplementary financial data, inflation accounting and the auditors' report.

3.1 The information required by the Cos. Act to be included in the annual reports to stockholders (Shareholders)

"... one of the responsibilities often imposed by law on [a] Corporation is to report at least annually to the shareholders".¹

Subsections (1) and (2) of Section 148 of the Cos. Act states in parts as follows:

"The directors of every company shall, at some date not later than eighteen months after the incorporation of the company and subsequently once at least on every calendar year, lay before the company in general meeting a profit and loss account or, in the case of a

company not trading for profit, an income and expenditure account for the period ... (148(1))

"the directors shall cause to be made out in every calendar year, and to be laid before the company in general meeting, a balance sheet ..." (148 (1))

In the case of a holding company, subsection (1) of section 150 requires that group accounts "be laid before the company in general meeting when the company's own balance sheet and profit and loss account are so laid."

The Cos. Act specifies that annual reports sent to the stockholders in connection with the annual general meeting of the company include the following information:²

- (1) Profit and loss account (or income and expenditure account),
- (2) Balance sheet,
- (3) Group accounts -- which includes a consolidated balance sheet and a consolidated profit and loss account -- in the case of a holding company,
- (4) The Directors' report, and
- (5) The Auditors' report.

A comparison with the U.S.A. reveals that the Cos. Act in Kenya requires a limited amount of information to be included in annual reports as opposed to the requirements of the Securities and Exchange Commission (SEC). Rule 14C - 3 of the Securities Exchange Act of 1934 requires the inclusion

of the following information in annual reports:³

- (1) "Certified" Comparative financial statements,
- (2) A five year summary of operations,
- (3) A Management's analysis of the summary of operations,
- (4) A brief description of the company's business,
- (5) A five year line of business breakdown,
- (6) Identification of the company's directors and executive officers and their principal occupations,
- (7) A statement of the market price range and dividends paid on voting securities for each quarterly period during the past two fiscal years.

As will be seen later, some companies in Kenya do include some other information in addition to that required by the Cos. Act.⁴ In general, companies in Kenya use the following form in the presentation of their annual financial reports:

- (1) Officers and officials of the company,
- (2) Notice of annual general meeting,
- (3) Chairman's statement,
- (4) The Directors' report,
- (5) The auditors report,
- (6) The profit account,
- (7) The balance sheet,
- (8) Notes to the accounts, and
- (9) Supplementary financial information which may include a historical summary of operations, a statement of

source and application of funds etc.

The order of presentation of these items vary from company to company, and, as will be seen later, some companies present both the English and Swahili version of some or all of these items.

3.2. Group Accounts - The extent and degree of Consolidation.

Most companies operate under the parent-sub subsidiary form of organization. As business expands, companies find it necessary to acquire subsidiaries either as a means of entering into new business, entering a new market area or acquiring more control over the line of business in which the company is involved. The purpose of consolidated statements, or group accounts, is to present the financial position and the results of operations of the parent and subsidiary companies as a single economic entity. This is done by combining the accounts of the parent company and the subsidiary companies so as to present the accounts of the group as a single unit. Parties, with interest in the group of companies, which include shareholders, creditors, as well as the Management of these companies, will be more interested in the overall performance and financial position of the group as a whole than in the performance and financial position of the separate companies. As a result, group accounts become more meaningful to these interested parties than separate financial statements.⁵

One statement of accounting policies, that of Nation Printers and Publishers, Ltd., as it relates to Consolidation in the 1974 and 1975 annual reports, states as follows:

"These consolidated accounts include the assets and liabilities and revenue results of the company and its subsidiaries as defined in the Companies Act."

This statement indicates that the extent and degree of consolidation, as is also true with the preparation of other financial statements, is based mainly on the requirements of the Cos. Act. The Act defines what a "holding Company" and "Subsidiary Company" are in section 154. A holding company is supposed to prepare group accounts which includes the holding company and its subsidiaries. Subsection (1) of section 150 states:

"Where at the end of its financial year a company has subsidiaries, accounts or statements (in this Ordinance referred to as group accounts) dealing as herein-after mentioned with the state of affairs and profit and loss of the company and subsidiaries shall, subject to subsection (2) of this section, be laid before the company in general meeting when the company's own balance sheet and profit and loss account are so laid" (Subsection (2) of this section gives the exceptional cases where group accounts may not be prepared).

The required group accounts are a consolidated balance sheet and a consolidated profit and loss account. A guideline as to the preparation of these accounts is given in section 150 of the Act.

A survey done in the U.K. (1971-1972) indicates that virtually all the survey companies which had subsidiaries at the end of the financial year presented group accounts in the form of consolidated financial statements.⁶ This is mainly due to the requirement in the U.K. of the Companies Act, 1948, which requires the presentation of group accounts. In Canada and U.S.A. the results of the surveys quoted before indicate that the majority of the companies with subsidiaries at the end of their financial year prepare group accounts which include all their subsidiaries.

As part of the study for this thesis, a survey was made to find out the extent and degree of consolidation in Kenyan firms as indicated in the survey companies' reports. The results are presented in table 3(a).

The results of the survey indicate that most companies in Kenya operate under the parent - subsidiary form of organization. In 1974, about 64 per cent of the survey companies indicated the existence of subsidiaries. The corresponding figures for 1975 and 1976 were 64 per cent and 62 per cent respectively. All the companies indicating the existence of subsidiaries in 1975 and 1976 included all their subsidiaries in their consoli-

Table 3(a) Extent and degree of Consolidation

	Number of Cos.			Percentage		
	1974	1975	1976	1974	1975	1976
All subsidiaries included	34	37	36	91.89	100.00	100.00
Certain subsidiaries excluded	1	-	-	2.70	-	-
Subsidiaries but no consolidation	2	-	-	5.41	-	-
Number of companies indicating subsidiaries	37	37	36	100.00	100.00	100.00
No subsidiaries disclosed	21	21	22			
Total No. of Companies	58	58	58			
Number of companies disclosing names of subsidiaries	18	21	16	48.65	56.76	44.44
Subsidiaries but no names disclosed*	19	16	20	51.35	43.24	55.56
Number of companies indicating subsidiaries	37	37	36	100.00	100.00	100.00

* The existence of subsidiaries in this case was inferred from either the existence of group accounts or reference to a subsidiary company in the financial report.

dated accounts. However, in 1974, one company (Diamond Trust) excluded one subsidiary and gave a separate statement of the profits of the excluded subsidiary; and two companies (K.C.C. Ltd. and City Breweries Investment Ltd.) did not present group accounts although they indicated having subsidiaries (see examples below). Some of the companies with subsidiaries disclosed the names of their subsidiaries and others did not as is shown in table 3(a).

Examples - Extent and degree of Consolidation

1. City Brewery Investment Ltd. 1974 annual report:

Notes on Balance Sheet (P.3)

Note 2. Subsidiary Companies

The Directors have not submitted Group Accounts as they are of the opinion that these would involve expenses out of proportion to the value to members of the company. The amount of K.£22,224 comprises shares held K.£200 and amounts owing K.£22,024, these being represented in the Accounts of the two subsidiaries by Balances at Bank K.£100 each in Uganda and Tanzania and Debtors less Creditors K.£22,024 in Tanzania.

2. Diamond Trust of Kenya Ltd., 1974 annual report:

Notes on Accounts. ↓

Note 3(a) Subsidiary Companies

The accounts of Mombasa Savings and Finance Ltd. (formerly known as the Ismailia Corporation Ltd.) for the year ended 30th September, 1974 have not been consolidated with the Group Accounts as the Directors are of the opinion that it could be of no real value to members of the company in view of the insignificant amounts involved. (A separate statement on the profits of this excluded subsidiary and the company's share therein was given on page thirteen of the annual report).

3. Kenya Co-Operative Creameries Ltd. 1974 annual report:

Report of the Directors.

Subsidiary Companies.

The subsidiary companies have not traded during the year. The Milk Producers Company Ltd. has been struck off and application has been made to strike off Uganda Creameries Ltd. from the Register of Companies.

Notes to Accounts.

Note 5. Subsidiary Companies.

Consolidated accounts have not been produced as the subsidiary is non-trading. In the opinion of the Directors, the total investment is recoverable in full.

4. Kenya National Mills Ltd., 1976 annual report:

Accounting policies.

Group Accounts.

The Group Consolidated accounts include the accounts of all subsidiaries and their financial year end dates are coterminous with the parent company. The profits and losses of associated companies (consisting of companies in which the group has a beneficial interest of between 20% and 50%) are excluded from the consolidated profit and loss account except to the extent of dividends received in the financial year.

5. Consolidated Holdings Ltd., 1976 annual report:

Accounting Policies.

(a) Consolidation of Group Companies.

The consolidated accounts include the assets, liabilities and revenue results of the company and its subsidiary companies as defined in the Companies Act Cap. 486.

(b) Associated Companies.

An associated company is a company, other than a subsidiary, in which the group's interest is considered to be long term and is at least 20 per cent of the equity capital of that company and where the group participates in commercial and financial policy decisions through representation on the board.

The Consolidated profit and loss account includes the group's share of the trading results of the associated companies and the group balance sheet asset comprises shares at cost or valuation and loans to associated companies plus the group's share of undistributed profits

arising since their acquisition. The associated companies make up their accounts to 30th September.

6. Loresho & Kiora (Plantations) Ltd., 1976 annual report:

Accounting Policies.

(a) Consolidation

The consolidated profit and loss account and balance sheet includes the accounts of the Holding Company and its Subsidiary, Kacharoba Ltd.

7. Nation Printers and Publishers Ltd. 1976, annual report:

Accounting Policies.

(a) Basis of Consolidation

The group accounts consolidate the accounts of the company and its subsidiaries which are made up to a date co-terminous with the financial year of the company.

3.3. The Directors' and The Chairman's Reports.

One of the items which will normally appear in the annual report of a company is the report by the directors and, in some cases, the Chairman's report. The purpose of these reports is to give a general view on the operations of the company during the last accounting period and to point out how the company intends to operate in the coming period, or any factors which may affect the operation of the company in future.

Section 157 of the Cos. Act requires the Directors' report to "be attached to every balance sheet laid before a company in general meeting". This report should deal with "the state of the company's

affairs, the amount, if any which they recommend should be paid by way of dividend, and the amount, if any, which they propose to carry to reserves ..." (157(1)). "The said report shall deal, so far as is material for the appreciation of the state of the company's affairs by its members and will not in the directors' opinion be harmful to the business of the company or of any of its subsidiaries ..." (157(2)).

There is no specific requirement by the Cos. Act of the attachment of the Chairman's report to the financial statements. However, while all the survey companies attached the Directors' report as is required by the Cos. Act, some of these companies attached the Chairman's report as well. Some of the titles used for such a report included the Chairman's review, the Chairman's statement, and the Chairman's report.

The Directors' report was in most cases very brief .. particularly in the cases where the Chairman's report was given as well (see examples below). In such a case the Chairman's report was more detailed dealing with many areas that affected the status and operations of the company or group during the financial year. Table 3(b) shows the number and percentage of companies attaching to their annual statements either both the Directors' and Chairman's reports or the Directors' report only. As can be seen from the table, the trend over the survey period seems to be toward the presentation of the Directors' report only.

Table 3(b) The Directors' and Chairman's reports

	Number of Cos.			Percentage		
	1974	1975	1976	1974	1975	1976
Both Directors' and Chairman's reports	43	42	39	74.14	72.41	67.24
Directors' report only	15	16	19	25.86	27.59	32.76
Chairman's report only	-	-	-	-	-	-
Total number of companies.	58	58	58	100.00	100.00	100.00

Examples - Directors' and Chairman's reports(a) Directors' Report1. Consolidated Holdings Ltd., 1976 annual report P.3

The Directors submit their report together with the audited accounts for the year ended 30th September, 1976.

1. Results

	<u>K.£</u>
Profit for the year attributable to shareholders	719,682
Undistributed profit brought forward	419,381
Prior year adjustment	<u>713</u>
	1,139,776
Dividends	<u>256,849</u>
Retained profit carried forward	<u><u>882,927</u></u>

2. Dividends

The directors have announced dividends of 12% in total.

3. Directorate

Changes which have occurred since last Directors' report are as follows:

Resignations: J.O. Owako, 3rd May, 1976. R.E. Hoffler,

13th July, 1976.

Appointments: F.A. Butcher (alternate J.J. Austen-Brown),
26th February, 1976; J.C. Skett, 3rd May, 1976.

The Directors who retire this year by rotation are
Messrs. Sharples and Gecaga who, being eligible, offer
themselves for re-election.

Messrs J.C. Skett and F.A. Butcher retire under Article
84 and, being eligible, offer themselves for re-election.

4. Auditors

The Auditors, Peat, Marwick, Mitchell & Co., will continue
in office in accordance with section 159(2) of the
Companies Act.

2. Loresho and Kiora (Plantations) Ltd., 1975 annual report, P.1

Directors report on the accounts to 31st March, 1975.

The profit for the year amounts to K.£8,748.

No dividend is recommended for the year under review,
and the balance on revenue to be carried forward, after
crediting the profit for the year stands at K.£168,653.

(b) Extracts from the Chairman's reports

1. Credit Finance Corporation Ltd., 1976 annual report:

The year just completed was one of considerable

expansion and during the period no further restrictions were placed on our activities by the Central Bank and we were able to make an uninterrupted run of business throughout the year. This assisted in obtaining the improved results noted. However, the Central Bank have advised Institutions that the liquidity requirement will be increased from 15% to 19% as from 1st July 1976 which will mean, in money terms, that we will need to withdraw a further K.£250,000 from our working capital to lodge with Banks or buy Treasury Bills. We are presently adjusting our finances to meet this future liquidity requirement.

2. East African Breweries Ltd., 1976 annual report:

Following a Presidential Decree, Uganda Breweries Ltd. was nationalised on 5th May 1976 and ceased to be a subsidiary company with effect from that date. In order that a realistic comparison can be made with the 1975 results the comparative figures for the year have been adjusted accordingly both in the consolidated profit and loss account and the balance sheets.

3. Nation Printers and Publishers Ltd. 1976 annual report:

The turnover of your Group continued to exhibit an upward trend in the year under review. Escalating costs of raw materials, to which I referred in my Report last

year, resulted, however, in considerably reduced profit margins in the subsidiary companies.

The effect of inflation, especially on the cost of financial stocks, has been a world-wide phenomenon in recent years, the newspaper industry being especially vulnerable as depressed economic conditions have also resulted in lower advertising income.

4. The East African Power and Lighting Co. Ltd. 1976 annual report:

The past year has been one of the most difficult ever experienced by your company. Despite some improvement in the country's overall economic performance due to the recovery of industrial countries from recession, your company operated under far worse trading conditions than were anticipated in my review last year.

With a below average rainfall, 1976 went on record as the driest year in the last decade. The situation was further aggravated by the temporary loss of the Uganda Electricity Board supply between July, 23rd and September, 14th, when the Board arbitrarily abrogated the Supply Agreement.

In order to satisfy the country's energy requirements under this difficult situation, the company was compelled to operate, for a considerable part of the year, all available thermal, diesel and gas plant. This substan-

tially increased operating costs ...

3.4. Fiscal Year End.

The preparation of financial reports is normally done over a period of time. The period for which financial reports are prepared - called the fiscal, financial or accounting period - is normally one year, beginning on any given date and ending twelve months later.

Some companies, however, prepare financial reports for periods of less than or more than a year. The Cos. Act defines the financial year as "the period in respect of which any profit and loss account of the body corporate laid before it in general meeting is made up, whether that period is a year or not." (2(1))

Most firms use the calendar year or what the Income Tax Act refers to as the "Year of income" i.e. "the period of twelve months commencing on 1st January in any year and ending on 31st December in that year."⁷ Other firms prefer using their natural business year. This is the period beginning and ending in the slack seasons of the business activity of the firm. The reason for using a natural business year is, as Walter B. Meigs, et al, put it "... to simplify year end procedures and facilitate a better measurement of income and financial position."⁸

However, while it may be true that year end procedures are simplified by using a natural business year, the idea of facilitating "a better measurement of income and financial position" is questionable. Furthermore, it is difficult to tell

what time of the year will result in a financial position statement that will be representative of the asset and equity balances which were held during the period.

(a) Year End.

The Cos. Act leaves the choice of a financial year end to the companies concerned. However, in the case of a holding company section 153(1) requires that "a holding company's directors shall ensure that except where in their opinion there are good reasons against it, the financial year of each of its subsidiaries shall coincide with the company's own financial year".

A survey on the fiscal year endings of the 58 survey companies revealed that the popular months for year endings were December, September, June, March and July. Most firms, however, used December as the financial year end. (see table 3(c)(i)). A comparison with the U.S.A., Canada, and U.K. show that December is also the most frequently used month for the end of the financial year.

(b) Period Covered

As already noted, firms normally prepare financial reports for a period of one year. Some companies, however, may prepare reports covering a period of more than or less than a year. A survey was made to find out the period covered by the financial reports of the survey companies.

The result of the survey (see Table 3(c)(ii) show that most of the companies used a one year period, one company (E.A. Cables Ltd.) maintained a 52-53 week financial period, two companies used a less than one year period (E.A. Portland Cement Co. Ltd. -- 10 months in 1974, and Iimuru Tea Co. -- 9 months in 1976), and one company (City Brewery Investment Ltd.) used a more than one year (19 months) financial period (1976 financial report).

Table 3(c) (i) Fiscal Year End

	Number of Cos.			Percentage		
	1974	1975	1976	1974	1975	1976
January	-	1	-	-	1.72	-
February	1	1	1	1.72	1.72	1.72
March	8	8	8	13.79	13.79	13.79
April	-	-	-	-	-	-
May	2	1	1	3.45	1.72	1.72
June	11	11	13	18.97	18.98	22.41
July	5	5	6	8.62	8.62	10.35
August	-	-	-	-	-	-
September	11	11	10	18.97	18.97	17.25
October	1	1	1	1.72	1.72	1.72
November	-	-	-	-	-	-
December	19	19	18	32.76	32.76	31.04
Total	58	58	58	100.00	100.00	100.00

Table 3(c) (ii) Period Covered by Financial Statements

	Number of Cos.			Percentage		
	1974	1975	1976	1974	1975	1976
One year period	56	56	55	96.56	96.56	94.84
52-53 weeks	1	1	1	1.72	1.72	1.72
Less than a year	1	1	1	1.72	1.72	1.72
More than a year	-	-	1	-	-	1.72
Total	58	58	58	100.00	100.00	100.00

3.5 Swahili Language Version of Reports.

Swahili is the official national language of Kenya. However, English is still predominant as the major language in business. There is no specific requirements in the Cos. Act that refers to the language to be used in financial reports. Section 147(1) of the Act refers to the keeping of books of account:

"Every company shall cause to be kept in the English language proper books of account ..."

An analysis was made to find out the extent to which the Swahili language is used in financial reports. The results are presented in Table 3(d)(i). The results show that most companies still use the English language only in their financial reports. However, some companies have, of late, realized the importance of the Swahili language in the Kenyan economy and are increasingly incorporating a Swahili language version in their financial reports. However, the majority of those companies which have some Swahili version in their reports use the Swahili version for only the

Chairman's, Directors' and Auditors' reports and a few companies use the Swahili language for all the statements in the report.

Table 3(d)(i) Swahili Language Version

	No. of Cos.			Percentage		
	1974	1975	1976	1974	1975	1976
English and Swahili together*	4	6	6	6.90	10.34	10.34
Swahili only	--	--	--	--	--	--
Swahili for Chairman's Directors' and Auditors' reports	9	6	8	15.51	10.34	13.80
Total Companies using some Swahili	13	12	14	22.41	20.68	24.14
English only	45	46	44	77.59	93.32	75.86
Total	58	58	58	100.00	100.00	100.00

*English and Swahili together means both languages were used for all statements in the report.

The presentation of both English and Swahili versions in the same report may be printed in several ways:⁹

- (1) "Flip-Flop" Method. In this method the English version begins from one cover and continues to the middle of the report and, when the report is turned over, the other cover begins the Swahili version which continues to the middle of the report -- in this case there is no back cover as such.
- (2) Interspersed English and Swahili versions -- this is

where a financial statement or report in the English language may or may not be followed by its Swahili Version. There is no specific sequence of Swahili -- English Versions.

- (3) English version preceding the Swahili version. In this case there is a back cover unlike the flip-flop method. The English version is printed first, and then the Swahili version follows.

The analysis revealed that the reports were printed as follows:

Table 3(d)(ii) Swahili Language Version

	No. of Cos.			Percentage		
	1974	1975	1976	1974	1975	1976
Flip-Flop	4	6	6	30.77	50.00	42.86
Interspersed English and Swahili	--	--	--	--	--	--
English precedes Swahili	9	6	8	69.23	50.00	57.14
Total Cos. showing Swahili version	13	12	14	100.00	100.00	100.00

3.6 Comparative Statements

Paragraphs II(ii) and 14(5) of the Sixth Schedule of the Cos. Act requires that Comparative Statements be given showing "the corresponding amounts for the immediately preceding financial year for all items shown in the balance sheet", (II(ii)) and "... in the profit and loss account" (14(5)). With the

exception of one company (Bird & Co. Africa Ltd.), all the survey companies presented comparative statements. In the case of Bird & Co. (Africa) Ltd., comparative figures for the previous year were not given for some of the financial statements of the various survey years. The reason given in these cases was that the inclusion of comparative figures would be confusing.

Paragraph 1500.09 of the Accounting Recommendations Section of the CICA Handbook¹⁰ recommends as follows:

"... where changes have been made during the current period in classifying items in the financial statements, the figures for the preceding period should be restated to conform with the new basis and the fact that such figures have been restated should be disclosed."

The CICA 1973 Financial Reporting in Canada, page 3, shows that for Canadian Companies, where changes had occurred during the current period in the manner of presenting specific items in the financial statements, the figures of the previous year had been restated for comparative purposes to conform with the current presentation.

In Kenya, the Cos. Act does not require a restatement of the figures of the preceding year. However, the results for the survey in Kenyan firms show that for the survey companies disclosing a change in the manner of presenting or treating specific items, restatements for the items had been made for the previous year for comparative purposes. Examples of such restatement disclosures are given in the examples below. In some cases the effect of the change on the statements was

disclosed only in the notes to the accounts.

Examples - Comparative figure restatements and disclosures

1. African Tours and Hotels Ltd., 1975 annual report:

Changes in accounting policies.

(a) Associated Companies.

In accordance with current accounting practice the group's share of the results of Associated Companies have been included in the Consolidated profit and loss for the year ended 31st March, 1975 for the first time.

The group's share of profits less losses of Associated Companies for the year ended 31st March, 1974 which were not accounted for in the accounts ended on that date amounted to K.£s 23,328. This is based on the audited accounts of Mnarani Ltd. and Mountain Lodges Ltd. for the year ended 31st May, 1974.

(b) Instalment Purchases of Fixed Assets

The accounting policy followed in respect of instalment purchases of fixed assets, which in prior years were written off in the profit and loss account as hire charges, changed in the year to 31st March, 1975.

It is considered that the new policy (Note 1d) will give a fairer presentation of the results and financial position of the Group.

The new policy gives rise to an increase in the group profit for the year of £s 54,771. If this policy had been

followed in previous years the profit for the year ended 31st March, 1974 would have increased by £s. 9,087.

2. Kapchorua Tea Co. Ltd. 1975 annual report:

Accounting Policies.

(E) Prior Year Adjustment

The depreciation basis adopted by the company was changed during the year from written down value to straight line. The 1974 comparatives have been adjusted to reflect this change of policy.

3. Pan Africa Insurance Co. 1974 annual report:

Notes on Accounts.

Note 3. Restatement.

The audited accounts of the principal subsidiary, Mae Properties Ltd., have been included in the consolidated balance sheet and profit and loss account for the first time. The comparative figures for 1973 have been restated.

4. Sasini Tea and Coffee Ltd. 1974 annual report:

Notes on consolidated Profit and Loss Account.

Note 4 Associated Companies.

In accordance with recognised accounting practice, the Company has accounted for results of its Associated Companies by disclosing its share of profit less losses before and after taxation. Formerly only dividend income received was accounted

for. This change in accounting policy necessitated an adjustment to the Unappropriated Profits brought forward at 1st October 1972.

3.7 Disclosure of Accounting Policies and Notes to Financial Statements

It was noted in Chapter 1 that accountants have several acceptable ways of presenting financial reports and treating each of certain items of account at their disposal. A company may therefore adopt any of these acceptable accounting policies. Unless the policies adopted are disclosed, the reports may not be understood by the users. The purpose of disclosure of accounting policies is therefore to draw the attention of the users of the financial statements to the accounting policies adopted. Such a disclosure is normally presented either in the Notes to the Accounts or under a separate caption - Disclosure of Accounting Policies.

The SEC advisory committee states the objective of Corporate accounting disclosure as:

"To assure the public availability in an efficient and reasonable manner on a timely basis of reliable, firm-oriented information material to informed investment, and corporate suffrage decision making"

It is due to the effort of accountants to fulfil this objective that corporate disclosure requirements are increasing all over the world. As H. Beaver states, "corporate disclosure requirements have substantially increased in the last five

years ... what is not self-evident is the form of the increased disclosure ..."¹²

Paragraph 11 and 14 of the Sixth Schedule of the Cos. Act gives some guidelines as to the amount of disclosure required by law. An analysis was made to find out the extent of disclosure in the survey companies.

(a) Disclosure of Accounting Policies.

The Cos. Act does not require the presentation of "Disclosure of accounting policies" as a separate statement. Some companies have, however, realized the importance of such a disclosure and show this as a separate item. Other firms include the disclosure of accounting policies as a subheading of the "Notes to financial statements". Table 3(e) gives the results of the analysis of the disclosure of accounting policies. The table shows that there was an increase in the number of companies disclosing their accounting policies over the survey period. Unlike 1974 when only about 22% of the companies disclosed their accounting policies, over 86% gave a disclosure of accounting policies in 1976. The majority of the companies included the disclosure of accounting policies under the notes to financial statements rather than giving it as a separate item. The various titles used to denote disclosure of accounting policies included accounting policies, principal or significant accounting policies, accounting bases, and statement of accounting policies. Most

of the Companies, however, used the title "accounting policies".

The increase in the number of companies disclosing their accounting policies over the survey period is an indication that companies are now realising that the financial reports are more meaningful to their users with such a disclosure.

Table 3(e) Disclosure of Accounting Policies.

<u>Presentation:</u>	<u>No. of Cos.</u>			<u>Percentage</u>		
	1974	1975	1976	1974	1975	1976
As a separate item	1	6	4	7.69	19.35	8.00
Under Notes to account	12	25	46	92.31	80.65	92.00
Total giving disclosure	13	31	50	100.00	100.00	100.00
No disclosure of accounting policies	45	27	8			
Total companies	58	58	58			
<u>Titles Used:</u>						
Accounting policies	13	25	42	100.00	80.65	84.00
Principal/significant accounting policies	--	--	5	--	--	10.00
Accounting bases	--	4	--	--	12.90	--
Statement of accounting policies	--	2	3	--	6.45	6.00
Total giving disclosure	13	31	50	100.00	100.00	100.00

(b) Notes to Financial Statements.

The Cos. Act requires that certain information be "stated by way of note, or in a statement or report annexed, if not otherwise shown" (paragraph 11 (1) of Sixth Schedule. See also Paragraph 14(1) of the Sixth Schedule). As will be seen in Chapter 4, the Cos. Act requires a summary of the items of the Balance Sheet (although not so specific as

regards the items of the Profit and Loss Account). Most of the survey companies presented summarized statements of the Balance Sheet and the Profit and Loss Account, and gave the detailed information relating to the items of these two financial statements in the notes to the financial statements. Only one company (Hutchings Biemer Ltd.) gave a detailed Balance Sheet and Profit and Loss Account and so did not have much by way of notes to the statements. The notes in this case were given immediately under the statement concerned. For the rest of the companies detailed "Notes to Financial Statements" were given as a separate item in the report. The following table gives some of the titles used for such notes:

Table 3(f) Notes to Financial Statements -- Titles Used.

	No. of Cos.			Percentage		
	1974	1975	1976	1974	1975	1976
Notes on the accounts	30	31	21	51.72	53.45	36.21
Explanatory notes on accounts	4	2	--	6.90	3.45	--
Notes to (the) accounts	15	17	34	25.86	29.31	58.62
Notes to and forming part of the accounts	2	3	2	3.45	5.17	3.45
Notes to be read in conjunction with the accounts	2	1	1	3.45	1.72	1.72
No heading -- just note 1, 2, etc., or otherwise	5	4	--	8.62	6.90	--
Total number of companies	58	58	58	100.00	100.00	100.00

3.8 Supplementary Financial Data.

In addition to the main financial statements required by the Cos. Act, some companies in Kenya present additional or supplementary financial data. Such additional data include historical summaries, highlights of the year's operations, cash flow statements, departmental results, charts depicting performance for the year or over the years etc.

Supplementary financial data are necessitated by the fact that the main financial statements -- the Balance Sheet and the Profit and Loss Account -- are normally in a condensed form. The purpose of supplementary financial data is to give the users of financial statements any additional information on the status and operations of the company that may not be easily seen in either the Balance Sheet or the Profit and Loss Account. Such data give more detailed information necessary for gauging the present and future performance of the company. Table 3(g) gives the results of the survey on the presentation of supplementary financial data by the survey companies. The results show that there was an increasing trend over the survey period in the number of companies presenting supplementary financial information, although most of the survey companies did not present any supplementary financial information or data.

Table 3(g) Supplementary Financial Data.

	No. of Cos.			Percentage		
	1974	1975	1976	1974	1975	1976
Supplementary financial data	7	14	22	12.07	24.14	37.93
No supplementary financial data	51	44	36	87.93	75.86	62.07
Total	58	58	58	100.00	100.00	100.000

Table 3(g) cont'd.

Types of Supplementary Financial Data.*

	Number of Companies		
	1974	1975	1976
Historical summary	4	9	7
Cash flow statement/ statement of source and application of funds	7	10	19
Highlights of year's performance	1	1	2
Statistical Charts.....	1	1	1
Departmental/divisional performance	1	1	1
Movement in Shareholders' fund or changes in other items of account.....	1	1	1
Contribution to the economy	1	1	1

*Some companies had several of these supplementary data in the same report.

Examples - Supplementary Financial Data.(a) Historical Summary.1. East African Oxygen Ltd. 1976 annual report. P. 5Consolidated Comparative Results.

	1976	1975	1974	1973	1972
	£	£	£	£	£
Issued Share Capital	700,000	700,000	700,000	700,000	700,000
Reserves	793,035	581,378	519,474	348,935	283,905
Deferred Taxation	124,805	135,679	120,720	72,558	82,206
Shareholders' funds	1,617,840	1,417,057	1,340,194	1,121,493	1,066,110
Trading Profit	630,297	610,710	514,617	405,535	399,142
Dividends	126,000	203,000	182,000	182,000	182,000
Taxation	341,228	289,142	264,865	172,559	132,573
Retained	163,069	118,568	67,752	50,976	84,569
	630,297	610,710	514,617	405,535	399,142

2. Elliot's Bakeries Ltd. 1976 annual report. p. 14:
Five-Year Financial Review.

		Expressed in K£ '000				
<u>Group Results</u>	1976	1975	1974	1973	1972	
Sales	6,108	5,054	4,047	3,384	3,008	
Profit before taxation	106	109	210	316	308	
Taxation	70	60	75	133	116	
Profit after taxation	36	49	135	183	192	
Preference dividends	2	2	2	2	2	
Ordinary dividends	70	70	70	60	55	
Transfer to/(from) reserves	(36)	(23)	63	121	135	
<u>Assets Employed</u>						
Fixed assets	1,386	1,418	906	812	765	
Long-term loans	53	53	93	93	53	
Net Current assets	21	6	(44)	(13)	(47)	
	1,460	1,477	955	892	771	
<u>Financed By:</u>						
Share Capital	730	730	730	630	530	
Reserves	596	632	225	262	241	
Shareholders' funds	1,326	1,362	955	892	771	
Loan Capital	134	115	-	-	-	
	1,460	1,477	955	892	771	
<u>Ratios</u>						
		Expressed in K.Ss. per Share				
Earnings per ordinary share	0.48	0.67	1.90	2.58	2.58	
Dividends per ordinary share	1.00	1.00	1.00	0.86	0.79	
Net asset Cover	18.51	19.03	13.22	12.32	10.60	
<u>Profit before taxation to:</u>						
		Expressed as percentages				
Sales	1.74	2.17	5.20	9.34	10.24	
Capital employed	7.99	8.00	21.99	35.43	39.95	

(b) Highlights of year's Performance.1. Kenya National Mills Ltd., 1976 annual report (cover page)

<u>Results in Brief</u>	<u>1976</u>	<u>1975</u>
Sales	K.£ 23,826,732	K£ 19,725,000
Profit before taxation	K£ 835,498	K£ 586,681
Net Margin	3.5%	3.0%
Profit after taxation	K£ 407,508	K£ 231,101
Dividends per share	K.£s 0.50	K.£s 0.50
Shareholders' funds	K£ 6,389,722	K£ 6,232,214

2. Ol Pejeta Ranching Ltd., 1976 annual report.Chairman's Statement

<u>Financial Highlights.</u>	<u>1976</u>	<u>1975</u>
	K.£	K.£
Net Sales	216,285	143,021
Net Earnings before extraordinary item	36,946	26,893
Dividends Declared	45,000	25,000
Dividends per ordinary share	60 cents	40 cents
Shareholders' Equity	685,003	627,911

(c) Contribution to the economyConsolidated Holdings Ltd., 1976 annual report.

(Inside the back Cover page)

Part of your Group's Contribution to the East African
Economy in the financial year

Total number of employees	1,751
Total Wages and Salaries paid	K£ 1,648,927
Value of goods and services produced	K£ 7,236,434
Tax paid	K£ 175,927

3.9. Inflation Accounting

The impact of inflation on any society cannot be denied. Few people today would dispute the importance of inflation's effects on individuals, companies, and the economy as a whole. Decisions made by individuals, companies, or even nations have been affected in one way or another by inflation.

As commonly used, the term "inflation" refers to the general rise in prices of goods and services over time. "Deflation", on the other hand, refers to the situation where prices are falling. While we may talk about a general price change, it is necessary to note that prices of individual items may not necessarily change at the same rate as the general price change. This leads to the notion of "specific price changes".

Accounting bodies all over the world are at the moment concerned about accounting for inflation. In the past few years, hundreds of articles have been written and published, and many more hundreds of speeches made on the subject of inflation. Many recommendations have been made, many exposure drafts and discussion papers published, and many accounting standards

proposed on inflation accounting. Countries leading the discussion over this controversy on inflation accounting include Australia, Britain, Canada, U.S.A., and many other European countries such as France, Germany and Netherlands. Many more countries of the world have now joined in this controversy. Despite all this attention, however, relatively little has been accomplished; and the implementation aspect of the various inflation accounting proposals has been difficult to achieve. As a result, most companies continue to prepare financial statements using the traditional historical cost approach, and, in some cases, show some inflation effects on the business enterprise only in terms of notes to the financial statements.

A survey to determine the number of companies presenting some inflation accounting data in the U.S. in 1976 revealed that only 2 of the 600 survey companies presented supplementary information adjusted for price-level changes.¹³

In Kenya all the survey companies presented financial statements on a historical cost basis and none of them presented any supplementary data adjusted for inflation over the survey period. However, there are references here and there, either in the Chairman's or Directors' report, on inflation and how it has affected the operations of the company. For example in the Chairman's report of Nation Printers and Publishers Ltd., 1976 annual report, P.4, we find the following note on inflation:

"The effect of inflation, especially on the cost of financing stocks, has been a world-wide phenomenon in recent years, the newspaper industry being especially vulnerable as depressed economic conditions have also resulted in lower advertising income ..."

"In spite of the increased turnover, therefore, your Group experienced an overall drop in trading profits, attributable to rapid inflationary pressures at a time when the growth in Kenya's economy had slowed down considerably ..."

Some of the survey companies note that some of the items reflected in the statements do not reflect their current values. For example, note 7 of the notes to accounts of Sasini Tea and Coffee Ltd., 1976 annual report says the following in relation to fixed assets:

"In the opinion of the Directors, the net book value of the land, development, buildings and improvements is materially lower than the current market value."

And, as regards profits, the Directors' Report of Bamburi Portland Cement Co. Ltd., 1976 annual report, Page 6, says:

"When considering the profits for 1976 the inflationary factor underlying the figures must be borne in mind ..."

The Chairman's Statement in the 1975 annual report of the same company had this to say:

"... last year's statements forecasting improved results for 1975 were not too optimistic. One should not forget, however, the inflationary factor underlying such figures. The combined replacement value of the factory's old and new plant is about three times their book value. Related to replacement costs the achieved return is therefore modest."

The survey also revealed that most of the survey companies had revalued their fixed assets at one time or another during the survey period. This reflects the fact that the written down historical cost values of fixed assets may not necessarily reflect the current values of the assets.

One can therefore conclude that there is a general recognition that the traditional historical cost accounting does not communicate fully information that is necessary to make decisions during an inflationary period. Despite this realization, no effort was made by the survey companies to present data that reflected the effect of inflation. Maybe the lack of a generally accepted method of accounting for inflation, as discussed above, makes it difficult for the accountants in these companies to make a decision as to which method to use in accounting for the effects of inflation. This is reflected in the statement by one of the survey companies - Bamburi Portland Cement Co. Ltd., 1976 annual report (Directors' report, P.6) - which says:

"Various authorities have put forward theories on how this problem [Inflation] should best be dealt with but the Board has decided to make no changes to the Company's financial statements until there is a clearer consensus of opinion on the subject."

3.10. The Auditors' Report

The auditors' report is one of the items required by the Cos. Act to be furnished to shareholders in connection with the annual general meeting of the company (see sections 156(1) and 162 of the Cos. Act). Professor H.F. Stettler says that "The opinion of an [auditor] concerning the financial statements of a business is the best possible indication of whether persons who are not associated with the business may justifiably rely upon those statements in making important financial decisions".¹⁴ However, it is necessary to note that both persons associated with the business enterprise as well as those not associated with it will need to rely upon the auditors' opinion concerning the financial statements of the business in order to make decisions as regards the business enterprise.

3.10.1. Forms of the Auditors' Report.

Two main forms of the auditors' report may be distinguished: the short form report and the long form report.¹⁵ The short form auditors' report normally gives the scope of the auditors' examination and his professional opinion on the financial statements. This is the report that is normally furnished to the shareholders. The long form report is normally prepared for Company Management giving a detailed appraisal or recommendations concerning the operations of the company.

A short form auditors' report may be a "standard form" or

a "modified form." A standard form auditors' report is one that normally contains two paragraphs - the scope paragraph and the opinion paragraph.¹⁶ A modified form is where both the scope and opinion are combined in one paragraph.

The Seventh Schedule to the Cos. Act gives a guideline as to what should be included in the auditors' report. Briefly, the report should contain (1) the scope of the auditors' examination, (2) the auditors' opinion as regards the keeping of the company's books of account and (3) the auditors' opinion as regards the financial statements. Auditors sometimes present these three items in either two or three paragraphs. For the purpose of the survey analysis, a standard form auditors report for Kenya was taken to be the one which contained these three required items either in two or three paragraphs. Table 3(h) gives the forms of the auditors reports in the survey companies. As can be seen from the table, most auditing firms prefer using the standard form rather than the modified form. (see Examples below for the two forms). The caption "other forms" in table 3(h) refers to the auditors' reports with more than three paragraphs - a common feature of "qualified" auditors reports (See 3.10.3 - Expression of opinion).

Table 3(h) Forms of the Auditors' Report

	No. of Companies			Percentage		
	1974	1975	1976	1974	1975	1976
Standard form	48	49	45	82.76	84.48	77.59
Modified form	5	4	6	8.62	6.90	10.34
Other forms	5	5	7	8.62	8.62	12.07
Total reports	58	58	58	100.00	100.00	100.00

As already stated, a standard form report was taken to be one that presented the scope of the auditors' examination and the auditors' professional opinion in either two or three paragraphs. The number of paragraphs used by the auditors for the standard form report in the survey companies were as follows:

Table 3(i) Standard Auditors' Report

	No. of Companies			Percentage		
	1974	1975	1976	1974	1975	1976
Two paragraphs	27	28	32	56.25	57.14	71.11
Three paragraphs	21	21	13	43.75	42.86	28.89
Total standard form reports	48	49	45	100.00	100.00	100.00

The trend over the survey period seems to be towards the use of two rather than three paragraphs for the standard form auditors' report.

Several differences in the wording of the auditors' report may be noted between the auditors' report in Kenya¹⁷ and the auditors' reports in Canada and U.S.A. In the U.S.A., for example, the last sentence of the scope paragraph as suggested

by the AICPA, is worded as follows:¹⁸

"Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances."

In Canada this last sentence of the scope paragraph, as suggested by the CICA Handbook (paragraph 5500.10) reads as follows:

"Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances."

In Kenya, the last sentence of the scope paragraph for most of the survey companies read as follows:

"We obtained all the information and explanations we considered necessary for our audit."

Another notable difference in the wording of the auditors' report in these three countries is in the last phrase of the opinion paragraph. In Canada and U.S.A. this last phrase reads as follows:

"... in accordance (conformity) with generally accepted accounting principles applied on a basis consistent with that of the preceding year."

This phrase is missing in the auditors' reports of the Kenya survey companies, and in its place, the phrase "... comply with the Companies Act (Cap. 486)" is generally used.

Examples - Forms of the Auditors' Report(a) Standard Form Auditors' Report.

1. B.A.T. Kenya Ltd., 1976 annual report, Page 11
Report of the Auditors to the Members.

The Balance Sheet of the Company set out on page 13 is in agreement with the books which, in our opinion, have been properly kept. We obtained the information and explanations we required.

In our opinion the accounts set out on pages 12 to 16 give a true and fair view of the state of affairs at 30th September, 1976 and the profit for the year ended on that date and comply with the Companies Act (cap. 486).

Coopers & Lybrand.

2. African Tours and Hotels Ltd., annual report 1976, P. 5
Report of the Auditors to Members.

We have examined the accounts on pages 6 to 13 and have obtained all the information and explanations we have considered necessary for our audit.

Proper books of account have been kept by the Company and the Balance Sheet is in accordance therewith.

In our opinion, the Accounts of African Tours and Hotels Ltd. and its Subsidiary Companies set out on pages 6 to 13 give, so far as concerns the Members of African Tours and Hotels Ltd., a true and fair view of the state of affairs

at 31st March, 1976, and of the profit and source and application of funds for the year ended on that date and comply with the Companies Act.

Pannell Bellhouse Mwangi & Co.

3. Kenya Planters' Co-operative Union Ltd., 1976 annual report Report of the Auditors to the Members.

We have examined the accounts as set out on pages 7 to 13 and have obtained all the information and explanations considered necessary for our audit.

In our opinion proper books of account have been kept by the Company and the accounts, which are in agreement therewith, comply with the Companies Act and give a true and fair view of the state of the Company's affairs at 30th June, 1976 and of the profit for the year ended on that date.

We have also examined the Statement of Source and Application of Funds on Page 14. In our opinion this Statement gives a true and fair view of the source and application of the Companies' funds for the year ended 30th June, 1976.

Gill & Johnson.

(b) Modified Form Auditors' Report.

1. Bird & Co. (Africa) Ltd. 1976 annual report Page 6 Report of the Auditors to the Members.

We have examined the above balance sheet and annexed profit and loss appropriation account and income and expenditure account. In our opinion the balance sheet and annexed accounts give respectively a true and fair view of the Company's affairs as at 30th June, 1976, and of the results for the year ended on that date.

Parry & Co.

Chartered Accountants

2. Ol Pejeta Ranching Ltd. 1976 annual report.

Auditors' Report to the Members.

We have obtained all the information and explanations necessary for the purposes of our audit. Proper books have been kept and the accounts are in agreement therewith. In our opinion, the accounts on pages 3 to 6 which have been prepared under the historical cost convention give, under that convention, a true and fair view of the state of the Company's affairs at 31st December, 1976 and of its profit for the year then ended and comply with the Companies Act (Cap 486).

Price Waterhouse & Co.

Chartered Accountants.

3.10.2 Title and Addressee of the Auditors' Report

The Cos. Act uses the term "Auditors' report" to refer to the report by the auditors on the financial statements furnished to shareholders in connection with the annual general meeting of the company. And Section 162(1) says that "the auditors shall make a report to the members ...". It therefore follows that the Act requires the auditors' report to be addressed to the members of the Company.¹⁹ It is, however, normal for the auditors' report to be addressed to the person or group of persons responsible for engaging the auditor. There is no specific requirement as to the title to use for the report although the term "auditors' report" is used by the Act.

The 1976 AICPA Accounting Trends and Techniques, Page 345, shows that most of the auditors' reports in the U.S.A. survey companies are addressed to the "Directors (Board of Directors) and Stockholders." In Canada the 1973 CICA, Financial Reporting in Canada, Page 190, shows that the auditors' report is in most cases addressed to the Shareholders.

A survey was made, for the Kenyan Survey Companies, to find out whether there were any variations in the title used for the said report, and whether some of the auditors' reports were addressed to persons other than the members of the company as is required by Section 162(1) of the Cos. Act. Table 3(j) gives the results of the survey.

The results show that while the term "Auditors' report" is used by the Cos. Act, most companies use a variation of this -

"Report of the Auditors." With the exception of a few reports which had no addressees, most of the auditors' reports were addressed to the members of the company and used the full title of, either, "The auditors' report to Members", or, "The report of the auditors to Members".

Table 3(j) Title and addressee of the Auditors' Report.

<u>Title</u>	<u>No. of Companies</u>			<u>Percentage</u>		
	1974	1975	1976	1974	1975	1976
Auditors' report	8	3	4	13.79	5.17	6.90
Report of the auditors	50	55	54	86.21	94.83	93.10
Total	58	58	58	100.00	100.00	100.00
<u>Addressee</u>						
The Members of the Co.	50	54	57	86.21	93.10	98.28
Other	--	--	--	--	--	--
No addressee	8	4	1	13.79	6.90	1.72
Total	58	58	58	100.00	100.00	100.00

3.10.3 Expression of Opinion and the Statements Covered by the Auditors' Report.

(a) Expression of Opinion.

The auditors' opinion may be either qualified or unqualified. A qualified opinion gives some exceptions that might affect the given opinion. An unqualified opinion, on the other hand, is an express opinion with no exceptions. In other cases the auditors may make a disclaimer of opinion or a denial of opinion on the financial statements.

A disclaimer of opinion is normally made when the auditors are unable to give any opinion on the financial statements due to lack of complete information on any material items in the financial statements. Table 3(k) gives the opinions expressed in the auditors reports of the survey companies. The table shows that there was no disclaimer of opinion in the survey companies over the survey period. Most of the opinions given were unqualified. One auditing firm made reference to compliance with the U.K. Acts in its 1974 report, but the same firm did not make such references in its subsequent reports (See the examples of The East African Power and Lighting Co. Ltd., 1974 and 1976 annual reports below). Some of the auditors' reports referred to the examination of the statements or part of the statements by other auditors (see the example of CMC Holdings Ltd., 1975 annual report below).

All the examples given above under "Forms of the Auditors' Report" are examples of "Unqualified opinion" reports. Other examples of unqualified and qualified opinion auditors' reports are given below.

Table 3(k) Expression of Opinion

	No. of Companies			Percentage		
	1974	1975	1976	1974	1975	1976
Unqualified opinion	52	51	52	89.66	87.93	89.66
Qualified opinion	6	7	6	10.34	12.07	10.34
Disclaimer of opinion	-	-	-	-	-	-
Total	58	58	58	100.00	100.00	100.00

Examples - Expression of Opinion(1) Unqualified Opinion.

1. The E.A. Power and Lighting Co. Ltd., 1976 annual report,
Page 13.
Report of the Auditors to the Members.

We have examined the accounts of the Company set out on pages 14 to 19 and have obtained all the information and explanations considered necessary for our audit.

In our opinion proper books of account have been kept by the Company and the accounts, which are in agreement therewith, comply with the Companies Act and give a true and fair view of the state of the Company's affairs at 31st December, 1976 and of the profit for the year ended on that date.

Gill & Johnson.

2. Sasini Tea and Coffee Ltd, 1976 annual report P. 8
Auditors' report to the Members.

We have examined the books of account of the Company, which in our opinion have been properly kept, and we have obtained all the information and explanations which we considered necessary for our audit.

As explained in note 1(c) to the accounts, certain tea stock have been valued at net realisable value as, in the opinion of the directors, this is a more appropriate basis for stocks of this types than valuation at the lower of cost

and net realisable value. In the circumstances we concur with this departure from standard accounting practice.

Accordingly, in our opinion the accounts and notes on pages 9 to 17 comply with the Companies Act and so far as concerns the members of the Company give a true and fair view of the state of affairs at 30th September, 1976 of the Company and of the group and of the profit and source and application of funds of the group for the year ended on that date.

Murdoch, McCrae & Smith
Chartered Accountants.

(ii) Qualified Opinion

1. The East African Power and Lighting Co. Ltd., 1974 annual report. Page 24.
Report of the Auditors to Members.

We have examined the accounts of the company as set out on pages 18 to 21 and have obtained all the information and explanations which we considered necessary for our audit.

In our opinion proper books of account have been kept by the Company and the balance sheet and profit and loss account, which are in agreement therewith, comply with the Kenya Companies Act (Cap. 486) and the Companies Acts 1948 and 1967 of the United Kingdom (except for non-compliance with Schedule 2 paragraph 11 (6c) of the 1967 Act concerning

distinction between freehold, long and short leasehold land held by the company), and give respectively a true and fair view of the state of the Company's affairs at 31st December, 1974 and of its profit for the year ended on that date.

Gill & Johnson.

(This example would be unqualified if based on the Kenya Cos. Act only. However, the report becomes qualified in opinion if we assume that the British Act must also be complied with by the Kenyan Companies. The exception for non-compliance renders the report qualified in opinion. As stated above, the auditors who gave this report did not make references to the U.K. Acts in subsequent reports as can be seen in the report for the same company by the same auditors in the 1976 annual report above).

2. The Motor Mart & Exchange Ltd., 1976 annual report, Page 13.
Report of the Auditors to the Members.

We have examined the accounts set out on pages 8 to 13. In our opinion proper books of account have been kept by the Company and the Company's balance sheet is in agreement therewith. We have obtained all the information and explanations considered necessary for our audit and in our opinion the accounts comply with the Companies Act.

As stated in note 12(b) the directors are unable to express an opinion on the value of the net assets in Uganda

amounting to K.663,262. We are also unable to express an opinion on the value of these assets. With this reservation in our opinion the accounts give a true and fair view of the state of affairs at 30th September, 1976 of the Company and the group and of the profit for the year ended on that date of the group.

In addition we have examined the statement of source and application of funds set out on page 14. In our opinion this statement gives a true and fair view of the source and application of the group's funds for the year ended 30th September, 1976.

Deloitte & Co.

Chartered Accountants.

3. CMC Holdings Ltd., 1975 annual report Page 14

Report of the Auditors to the Members.

The balance sheet of the Company set out on page 9 is in agreement with the books which, in our opinion, have been properly kept. We obtained the information and explanations we required.

The consolidated accounts set out on pages 8 to 14 incorporate figures in respect of one subsidiary company which has not been audited by us. In our opinion, based upon our examination and the report of the other auditors, the balance sheet of the Company and the consolidated accounts comply with the Companies Act (Cap 486) and give a

true and fair view of the state of affairs at the 30th September, 1975 and the profit of the Company and the group for the year ended on that date.

Coopers & Lybrand.

(b) Statements Covered by the Auditors' Report.

The auditors' report may sometimes cover schedules and statements other than the basic financial statements required by the Cos. Act - that is, it may cover supplementary financial data in addition to the basic financial statements, in the case of a company presenting some supplementary financial data. The survey revealed that, in most cases, the only supplementary financial statement covered by the auditors' report was the cash flow statement (statement of source and application of funds). Other supplementary data such as historical summaries, financial highlights, etc., were not covered by the auditors' report. Where no supplementary financial data were provided, the auditors' report covered the basic financial statements - Profit and Loss Account and the Balance Sheet, including the notes to these statements.

3.11. Conclusion

This chapter has surveyed some of the general accounting information that relates to the 58 survey companies, all of which, as already mentioned, were listed on the Nairobi Stock Exchange as of 30th June, 1978. In conclusion, several points from the survey analysis presented in this chapter may be noted:

- (1) The Cos. Act requires a limited amount of information to be included in the annual reports unlike the requirements in some other countries -- for example, the requirement of SEC in the U.S.A.
- (2) Most of the survey companies operate under the parent -- subsidiary form of organization and therefore present group account.
- (3) Both the Directors' and the Chairman's reports are presented by most of the survey companies, but the trend is toward the presentation of the Directors' report only.
- (4) Most of the companies end their fiscal years in December, although other popular year end months are March, June, July and September. Most of the statements presented cover a one year period.
- (5) While most of the companies use the English language for the reports, some companies use some form of a Swahili language version in their reports.
- (6) Comparative figures for the previous year are presented by most of the companies in their reports.
- (7) There was an increasing number of companies disclosing their accounting policies over the survey period.

- (8) There was an increasing trend in the number of companies giving supplementary financial data in addition to the main statements required by the Cos. Act. However, most of the survey companies did not give any supplementary data over the survey period.
- (9) None of the survey companies presented data adjusted for the effect of inflation.
- (10) The auditors' report seems to be standardized, particularly, as regards the wording, form, title and addressee of the report. However, it was noted that the wording of the report in Kenya differs, in some respects, with the wording of the reports in Canada and in the U.S.A. (see section 3.10.1 of this chapter).

The following chapter presents a survey analysis on the reporting practices that relates to the Balance Sheet and the Profit and Loss Account.

FOOTNOTES TO CHAPTER 3

1. Robert G. May, Gerhard G. Mueller, and Thomas H. Williams,
A New Introduction to Financial Accounting, P. 539
2. See Sections 148 to 157 of the Cos. Act. The general contents and form of the required statements are given in these sections.
3. See AICPA, Accounting Trends and Techniques, 1976, P.2.
4. See under "Supplementary Financial data", Section 3.8 of this Chapter.
5. For a good discussion on the nature and purpose of group accounts See G.A. Lee, Modern Financial Accounting, Op. Cit., P. 378, and Sidney Davidson (Ed.), Handbook of Modern Accounting, (McGraw Hill Book Co., 1970) PP. 32-7 - 32-11.
6. Survey of Published Accounts 1971-1972, sponsored by the Research Committee of the Institute of Chartered Accountants in England and Wales, published by the Institutes' Trustees of Chartered Accountants' Trust for Education and Research. (Quoted in CICA, Financial Reporting in Canada, 1973, P.6)
7. The Income Tax Act, No. 16 of 1973, (Nairobi: Government Printer, 1973), Section 2(1)
8. Walter B. Meigs, et al., Intermediate Accounting, 3rd Ed., (McGraw Hill Book Co., 1974), P.40.
9. See CICA, Financial Reporting In Canada, 1973, P. 2 which gives an analysis of French and English version reports as practiced in Canada

10. References in this thesis are to the CICA Handbook as of September, 1973 as quoted in the CICA, Financial reporting in Canada, 1973.
11. Report of the Advisory Committee on Corporation Disclosure to the Securities and Exchange Commission, (Washington D.C.: Government Printing Office, 1976). Quoted in H. Beaver, "Current Trends in Corporate Disclosure", Journal of Accountancy, January 1978, P. 44.

This objective tends to emphasize the informational role of company accounting disclosures in that it looks at disclosure only as a means of giving more information to users. It is however, necessary to note that company accounting disclosures may also play a protective role for the company, for example, if a company does not disclose some accounting procedures required by law it might face a punitive action.
12. H. Beaver, *Ibid.* P. 44
13. See AICPA, Accounting Trends and Techniques, 1976, P. 72
14. Howard F. Stettler, Auditing Principles, 3rd Ed. (Englewood Cliffs, N.J.: Prentice Hall, Inc., 1970), P. 1
15. A good discussion on the short-form and long-form auditors' reports is given in chapters 21 and 22 of Stettler, *Ibid.*

16. See AICPA, Accounting Trends and Techniques, 1976, P. 346.
17. It should be noted here that the Kenya Cos. Act does not give a suggested form of the auditors' report to be followed by firms. But the survey showed that the auditors' reports in the survey companies seemed to use similar wording, and, therefore, standardized in the wording of the report.
18. See H.F. Stettler, Op. Cit, P. 6
19. See Sections 28 and 29 of the Cos. Act for the definition of Company Membership.
20. See H.F. Stettler, PP. 469-470 and PP. 477-479 for a discussion on disclaimers of opinion.

THE BALANCE SHEET AND THE PROFIT AND LOSS ACCOUNT

4.1. Introduction

The focus of financial reporting is mainly on two financial statements -- the Balance Sheet and the Profit and Loss Account. Financial report users will be most interested in these two statements. This is because users of financial statements are interested in getting some information as to the financial status as well as the results of the operations of the company in order to make rational economic decisions as concerns the company. Most of this information is contained in the two financial statements together with the notes accompanying these statements. The Balance Sheet is a statement which gives the financial position of a company as at the balance sheet date. The Profit and Loss Account, on the other hand, gives the results of the operations of the company over the accounting period.

As is true with most items of the financial reports, the presentation of the Balance Sheet and the Profit and Loss Account in the financial reports will be affected by the requirements of the Cos. Act. In addition, many authors have put forward recommendations for the preparation and presentation of these two financial statements.¹ It should be noted, however, that it will be of interest to Management to present these statements in a way that will be clear and understandable to the users. It may therefore be said that the format of these

statements, and the treatment of the items forming these statements will depend, in most cases, on what the company management considers to be of use to the statement users - taking into account the requirements of the Cos. Act and current acceptable practice.

This chapter presents a survey and discussion of the financial reporting practices that relates to these two main financial statements. The balance sheet is discussed first, and the Profit and Loss Account follows. A conclusion is then drawn on the matters discussed in the Chapter. In the discussion of these two statements an attempt has been made to point out some of the various formats of presentation of the items in the statements as well as the various available ways of treating certain items in the accounts.

As already noted in Chapter 2, not all the items which are normally included in the Balance Sheet and Profit and Loss Account of the survey companies are discussed in this chapter. The chapter deals mainly with what was considered by the author as being the highlights, or the Balance Sheet and Profit and Loss Account items which may be considered most important in financial reporting. In some cases a discussion of one item may touch on other items not surveyed and so a discussion or survey of such other items was not found necessary. For example, in the discussion of working capital, current liabilities are normally subtracted from current assets to get net current assets (or net current liabilities) - which is referred to as working capital. In such a case a discussion of the reporting practices that relates to working capital was assumed to cover both current

assets and current liabilities. As a result, although in this particular case certain items of the current assets are individually discussed in this chapter, a discussion of the individual items of the current liabilities was not found necessary.

4.2. The Balance Sheet

Section 149(1) of the Cos. Act states the objective of a Balance Sheet as to "give a true and fair view of the state of affairs of the company as at the end of its financial year ..."

The Act does not give a definition of "True and fair view".

G.A. Lee gives some insight as to the meaning of this term:

"Today, 'true and fair view' has become a term of art. It is generally understood to mean a presentation of accounts, drawn up according to accepted accounting principles, using accurate figures as far as possible, and reasonable estimates otherwise; and arranging them so as to show, within the limits of current accounting practice, as objective a picture as possible, free from wilful bias, distortion, manipulation, or concealment of material facts. In other words the spirit, as well as the letter, of the law must be observed ..."²

It can therefore be said that a Balance Sheet represents what, in the opinion of the Directors, is a "true and fair view of the affairs of the company" as of a specific date. The Sixth Schedule to the Act specifies in detail the information to be included in the Balance Sheet (as well as the Profit and Loss Account).

Section 149(2) requires that "a company's Balance Sheet and Profit and Loss Account shall comply with the requirements of the Sixth Schedule ... so far as applicable thereto." However, we note in Section 149(3) that "the requirements of subsection 2 ... and the said schedule shall be without prejudice either to the general requirements of subsection (1) or to any other requirement of this ordinance". From this we may say

that compliance with the Sixth Schedule must be aimed at giving the objective of "a true and fair view", and where compliance with the Sixth Schedule may not give the said required objective, then it is the duty of the directors to supplement the statements with any other information that will help to meet this objective. And since section 149(7)(a) provides that "any reference to a Balance Sheet or Profit and Loss Account shall include any notes thereon or document annexed thereto ...", it seems that such supplementary information may be given in the notes to the accounts or any other "document annexed thereto".

Paragraph 2 of the Sixth Schedule says, "the authorized share capital, ~~issued share~~ share capital, liabilities and assets shall be summarized, with such particulars as are necessary to disclose the general nature of the assets and liabilities ...". Again in Paragraph 4(1) we find that "the reserves, provisions, liabilities and fixed and current assets shall be classified under headings appropriate to the company's business". From this we can infer two facts about the requirement of the sixth schedule:

- (1) It requires a summarized balance sheet showing only the general nature of the items which make up the balance sheet.
- (2) Companies have to make their own choice of classification and headings for the balance sheet items.

4.2.1. Balance Sheet title and format.

The Cos. Act uses the term "Balance Sheet" throughout to refer to the statement of financial position or, as the Act puts it, the statement of the "state of affairs of the company as

at the end of its financial year". The 1976, AICPA, Accounting Trends and Techniques, and the 1973, CICA, Financial Reporting in Canada, show that the title "Balance Sheet" is used by most of the companies in U.S.A. and Canada. A survey to determine the titles used by the Kenyan survey companies show that all the companies surveyed used the title "Balance Sheet" to refer to the said statement.

The Act does not require any specific form of the balance sheet to be used in financial reporting. We may distinguish three main balance sheet formats³ - account form, report form and financial position form. The account form is the traditional balance sheet form whereby assets are listed on the left-hand (or right-hand) side, and liabilities and shareholders' equity are "balanced" against them on the right-hand (or left-hand) side. The report form shows a downward sequence of either assets minus liabilities equal to shareholders' equity or total assets equal to total liabilities plus shareholders' equity. The financial position form is a variation of the report form emphasizing the working capital - i.e. the difference between current assets and current liabilities. In this case working capital is added to other assets less other liabilities to give a balance equal to shareholders' equity. There are other variations of the financial position form, for example, working capital may be added to other assets to give a balance equal to shareholders' equity plus other liabilities.

Of the three forms, most Canadian and U.S.A. companies use the account form balance sheet.⁴ A summary of British Practice in the "Survey of Published Accounts 1971-72" showed that only 15% of the 300 British Survey companies used the account form.⁵ Table 4(a) shows the results of the survey on the Kenyan companies. From the table we can see that most companies use the financial position form balance sheet. There was an increasing trend in the number of companies using the financial position form balance sheet over the survey period.

Table 4(a) Balance Sheet Format.

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Account Form	5	4	1	8.62	6.90	1.72
Report form	9	7	4	15.52	12.07	6.90
Financial position form	44	47	53	75.86	81.03	91.38
Total	58	58	58	100.00	100.00	100.00

Whichever form of the balance sheet used, the balance sheet captions may be arranged or listed in different ways. Some companies start with the Equity Side and other companies start with the Assets side of the balance sheet. It may be assumed that such arrangement of captions depend on what the company concerned thinks to be the best or most acceptable method of arrangement, and sometimes may depend on what the company wants to emphasize to the user of the balance sheet.

4.2.2. Working Capital -- Net Current Items.

As indicated above, most companies are increasingly using the financial position form of balance sheet which, as stated, emphasizes working capital, that is, net current assets or liabilities. Some companies present working capital as a net figure in the balance sheet -- i.e. only the difference between current assets and current liabilities is shown in the balance sheet body. In this case detailed current items are listed in the notes to the account. In some other cases a detailed list of current assets and current liabilities is given in the balance sheet body itself and then the difference between them shown. In either case the net amount -- Working Capital is normally referred to as the "Net current assets/liabilities", or "the excess of current assets (liabilities) over liabilities (assets)". Table 4(b) shows the treatment of current items by the survey companies. As can be seen in the table, most of the survey companies presented all the current items in the main body of the balance sheet, and only a few companies showed the net figure only.

Table 4(b) Current Items.

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Showing all current items in the balance sheet body	50	50	50	86.21	86.21	86.21
Showing only the net asset/liabilities figure and detailed current items in notes	8	8	8	13.79	13.79	13.79
Total	58	58	58	100.00	100.00	100.00

4.2.3. Current Assets(a) Cash

Table 4(c) shows the balance sheet captions used by the survey companies for cash items. Most companies are increasingly using the caption "cash and bank balances" unlike the U.S. where, as the 1976 AICPA Accounting Trends and Techniques, P.77, shows, most companies present cash as a single item and use the caption "cash". In table 4(c) the caption "other" refers to balance sheet captions such as "cash and short term deposits", "Liquid funds", and "Tax reserve certificates and cash".

Table 4(c) Cash -- Balance Sheet Captions.

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Cash or Cash on hand or Cash balances	6	6	4	10.34	10.34	6.90
Cash and bank balances	21	25	37	36.21	43.10	63.79
Bank balances or Cash at bank	5	4	4	8.62	6.90	6.90
Cash at bank and in hand	21	18	8	36.21	31.04	13.79
Deposits, bank balances and cash	3	3	3	5.17	5.17	5.17
Other	2	2	2	3.45	3.45	3.45
Total	58	58	58	100.00	100.00	100.00

(b) Debtors (Accounts Receivable)

Debtors or accounts receivable was listed in various ways in the current assets section of the balance sheet. Table 4(d) shows the various captions used by the survey companies. In some cases debtors were combined with other current asset items. As shown in table 4(d) most of the survey companies are increasingly using the single caption "debtors" or a variation thereof, "Trade and sundry debtors". Of the companies showing debtors in their accounts, only a few companies referred to "bad debts" or "provision for doubtful debts". Most of these companies did not indicate whether bad debts or doubtful debts had been provided for in the determination of the debtors shown in the balance sheet. Only one company used the American term "Accounts receivable" for the years 1974 and

1975, but changed to the term debtors in 1976.

Table 4(d) Debtors - Accounts Receivable
(Balance Sheet Captions)

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Debtors, or Trade and Sundry debtors	30	35	46	52.63	62.50	82.14
Debtors and payments in advance (Prepayments)	14	13	7	24.56	23.21	12.50
Debtors, deposits and Prepayments less provision for doubtful debts	9	4	2	15.79	7.14	3.57
Sundry debtors and accrued charges/ interest	2	2	1	3.52	3.57	1.79
Stocks, debtors and Investments	1	1	--	1.75	1.79	--
Accounts receivable	1	1	--	1.75	1.79	--
Total companies showing debtors	57	56	56	100.00	100.00	100.00
No debtors shown	1	2	2			
Total companies	58	58	58			
Reference to doubtful debts	14	12	5	24.56	21.43	8.93
No reference to doubtful debts	43	44	51	75.44	78.57	91.07
Total companies showing debtors	57	56	56	100.00	100.00	100.00

(c) Stocks (Inventory) - Basis of Valuation

Table 4(e) shows the bases used in valuing stocks by the survey companies. As can be seen from the table, most of the survey companies indicated that they value stocks on the basis of "lower of cost and net (or estimated) realisable value".

There was an increasing trend in the number of companies valuing different stock items using different valuation bases. In such cases the various stock items were listed in the notes to the accounts giving the basis used to value each stock items (see the example on Theta Group Ltd., 1976 annual report below).

"Cost" may be determined using several methods: FIFO, LIFO, Average Cost, Specific identification, etc. Of the companies referring to "Cost" as a valuation basis (for example where stocks are valued at lower of cost or net realisable value, or at average cost), most of them did not disclose the method used for determining cost.

Table 4(e) Stocks - Basis of Valuation

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Lower of Cost and net realisable value, or lower of cost and estimated realisable value	32	32	32	62.75	64.00	64.00
Average Cost	5	5	3	9.80	10.00	6.00
Estimated (net) realisable value	4	2	2	7.84	4.00	4.00
Various bases shown for the various stock items	9	11	12	17.65	22.00	24.00
No valuation basis shown	1	-	1	1.96	-	2.00
Total companies showing stocks	51	50	50	100.00	100.00	100.00
No stocks shown	7	8	8			
Total companies	58	58	58			

Examples - Stocks (basis of Valuation)1. Marshalls (East Africa) Ltd., 1976 annual report P.5

Notes to Accounts

Note 1. Accounting Policies.

Stocks

Stocks are valued at the lower of cost, computed on a first-in-first-out basis, and the net amount realisable from disposal in the normal course of business.

2. Kenya Orchards Ltd., 1976 annual report P.5

Notes to Accounts.

Note 1 Accounting Policies

Stocks

Stocks are valued at the lower of cost and the net amount realisable from disposal in the normal course of business. Cost comprises expenditure incurred directly in purchasing or manufacturing the stocks together with production overheads where appropriate.

3. The Pan Africa Insurance Company Ltd., 1976 annual report P.10

Notes to Accounts.

Note 1 Principal Accounting Policies

(g) Stocks

Stocks are valued at estimated net realisable value.

4. Theta Group Ltd., 1976 annual report, P. 6Notes on the Accounts.

Note 1 Accounting Policies

(b) Stocks

Bases for valuation of stocks are as follows:

- (i) Clothing, guns and ammunition -- cost is calculated as selling price less the average mark-up.
- (ii) Ready tea is valued at subsequent realised value.
- (iii) Other stocks are valued at the lower of the cost or net realisable value.

(d) Other Current asset items

The other current asset items shown by the survey companies included such items as marketable securities, prepaid expenses, amounts due from subsidiaries, Tax reserve certificates, etc. In some cases these items were combined together in two or three items, for example prepayments were in most cases listed together with debtors and one figure given for both items.

4.2.4. Fixed Assets

The Sixth Schedule to the Act provides that fixed assets should be distinguished from current assets, and the method or methods used to arrive at the amount of the fixed assets should be stated (Paragraphs 4(2) and 4(3)). Paragraph 5(1) gives the method to use in calculating the amount of any fixed asset

other than the assets listed in paragraph 5(2). To get the amount of any fixed asset "take the difference between --

- (a) its cost or, if it stands in the company's books at a valuation, the amount of the valuation; and
- (b) the aggregate amount provided or written off since the date of acquisition or valuation, as the case may be, for depreciation or diminution in value".

In this case paragraph 5(3) requires that the aggregate amounts of both cost or valuation and write-offs should be shown.

(a) Disclosure of Balances of Major Classes of Fixed Assets and Accumulated Depreciation

Most of the survey companies presented only the net book value of the fixed assets in the balance sheet and showed the related calculations of arriving at the net book value in the notes to the accounts. Thus the aggregate amounts of cost/valuation and write-offs were shown in the notes to the accounts. Some companies presented a segregation of fixed assets and accumulated depreciation by categories of assets or group of assets. Table 4(f) below shows the companies segregating fixed assets and accumulated depreciation by categories or classes of fixed assets. As can be seen from the table, most of the companies showed fixed assets in categories or classes of assets.

Table 4(f) Segregation of Fixed Assets and Accumulated Depreciation by Categories of Fixed Assets or Groups of Fixed Assets

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Fixed Assets and accumulated depreciation not segregated (No asset classes or categories shown) - - -	1	1	1	1.72	1.72	1.72
Fixed assets segregated (categories or classes of fixed assets shown):						
Accumulated depreciation segregated--	53	54	54	91.38	93.10	93.10
Accumulated depreciation not segregated - - - - -	3	2	2	5.18	3.46	3.46
No fixed assets shown	1	1	1	1.72	1.72	1.72
Total Companies	58	58	58	100.00	100.00	100.00

(b) Valuation Basis

Table 4(g) shows the major fixed asset valuation bases disclosed by the survey companies. In some cases different valuation bases were used for various categories of fixed assets. The results in table 4(g) show that most companies used the "cost or valuation" basis. Where revaluations were recorded in the accounts the usual practice was to value subsequent additions at cost. In Canada, the CICA, Financial Reporting In Canada, 1973 shows that most companies used the "cost/cost less write off" valuation basis.

Table 4(g) - Major Bases of Valuation of Fixed Assets

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Cost/Cost less write off	15	16	17	25.86	27.59	29.31
Cost or Valuation	37	38	38	63.79	65.52	65.52
Appraisal plus additions at cost	5	3	2	8.63	5.17	3.45
No Fixed Assets shown	1	1	1	1.72	1.72	1.72
Total No. of Companies	58	58	58	100.00	100.00	100.00

4.2.5 Investments

Paragraph 8(1)(a) of the Sixth Schedule to the Cos. Act requires a distinction between various classes of investments...

"There shall be shown under separate headings --(a) the aggregate amounts respectively of the company's trade investments, quoted investments other than trade investments and unquoted investments other trade investments". And paragraph 8(3) requires that "the heading showing the amount of the quoted investments other than trade investments shall be subdivided, where necessary, to distinguish the investments as respects which there has, and those as respects which there has not, been granted a quotation or permission to deal on a stock exchange of repute". Paragraph 11(8) also requires showing "the aggregate market value of the company's quoted investments, other than trade investments, where it differs from the amount of the investments as stated, and the stock exchange value of any investment of which the market value is shown (whether

separately or not) and is taken as being higher than their stock exchange value". Most of the survey companies showed quoted investments at cost and the market values of such investments were shown either in note form or in brackets.

Investments in subsidiaries and associate companies may be valued using one of two principal methods:⁶ (1) the equity method, and (2) the cost method of valuation. Under the equity method, the investment is recorded at cost and the carrying value of the investment is increased or decreased to recognize the investor's share of the income or losses of the company in which investment is made subsequent to the date of investment. In this case revenue from investment is recognized whether or not dividends are received. Under the cost method the investment is recorded at cost and revenue or income from investment is recognized only when dividends are received.

The methods used by the survey companies in valuing their investments are set out in table 4(h). For the companies showing investments in their accounts, some companies did not state the basis of valuation as can be seen from table 4(h). Most of the companies stating the basis of valuation indicated that the cost method was the most used by the companies to value investments in subsidiaries and associated companies.

Table 4(h) Investments - Basis of Valuation

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Equity	5	5	7	11.63	12.50	15.91
Cost	18	16	19	41.86	40.00	43.18
Basis not stated	20	19	18	46.51	47.50	40.91
Companies showing Investments	43	40	44	100.00	100.00	100.00

4.2.6 Deferred Taxation (Inter-Period Tax Allocation)

The Cos. Act does not refer specifically to the treatment of deferred taxation⁷ in the accounts of companies. Paragraph 11(10) of the Sixth Schedule to the Act requires stating "the amount or the estimated amount of any liability to income tax in respect of the profits made by the company to the date of the balance sheet, together with the basis on which such amount, if any, set aside for income tax is computed."

A survey on the 58 survey companies showed that a liability in the form of deferred taxation was shown in the accounts of 3 companies, 8 companies and 12 companies, for the years 1974, 1975 and 1976 respectively. Some companies (0, 4 and 9 companies in 1974, 1975 and 1976 respectively) stated that they did not provide for deferred taxation in their accounts (see examples below). Other companies (5, 4 and 3 companies in 1974, 1975 and 1976 respectively) indicated having set up a reserve account to cater for any future tax differences. Such a reserve was variously referred to as Reserve For Future Taxation, Taxation Equalisation Fund, Amount Set Aside For Equalisation Of Taxation, etc. The amount that would be normally considered deferred

taxation was in such cases transferred to this reserve account.

Examples -- Deferred Taxation

1. Brooke Bond Liebig Kenya Ltd., 1976 annual report

Accounting Policies.

Taxation.

Taxation is provided in the profit and loss account at the rate of 45% on the profit for the year as adjusted according to the Kenya Income Tax Act 1973. With the exception of a provision for tax deferred on long term assets through differences of timing, no provision is made for tax liabilities which may arise on other differences in timing nor on any future sales of fixed and long term assets at their valued book figures.

2. Consolidated Holdings Ltd., 1976 annual report

Notes on the Accounts.

Note 3(b)

No provision has been made in these accounts for the liability to taxation that has been deferred by the benefit of taxation allowances on fixed assets which, in certain instances, exceed the related amounts provided for depreciation ...

3. East African Oxygen Ltd., 1976 annual report

Notes on the accounts.

Note 1(f) Deferred Taxation

Deferred taxation is calculated, principally on the deferral method, on the excess of capital allowances given for tax purposes over the depreciation provisions charged in the accounts.

On a revaluation of fixed assets provision is made for the tax liability which may arise if the assets are sold at the value stated in the balance sheet.

4. Sofar Investments Ltd., 1976 annual report

Notes on the accounts

Note 1 Statement of Accounting Policies

Taxation.

Provided on the basis of the profit for the year as adjusted in accordance with the tax legislation. No provision is made for tax deferred through differences of timing nor for any possible tax liabilities arising from the future sale of fixed assets at their revalued book figures.

5. Hughes Ltd., 1976 annual report.

Note 1 Accounting Policies

(d) Deferred Taxation:

No provision for deferred taxation has been made in these accounts as the amount involved is immaterial.

4.2.7 Long-Term Liabilities

In addition to the requirement in paragraph 2 of the Sixth Schedule of a summary of liabilities, paragraph 9 requires that

where any liability of the company is secured otherwise than by operation of law on any asset of the company, the fact that that liability is so secured shall be stated, but it shall not be necessary to specify the assets on which the liability is secured." And paragraph 4(1) says, in part, that "... liabilities ... shall be classified under headings appropriate to the company's business ...". It therefore follows that the classification of liabilities into short-term (Current) and long-term is a matter to be decided by the company concerned.

The survey showed that about 50%, 55% and 53% of the survey companies in 1974, 1975 and 1976 respectively, indicated the existence of long-term liabilities in their accounts. These companies disclosed the nature of such liabilities - i.e. whether loans, debentures, etc. - and whether such liabilities were secured or not. The examples below give some of the common practices used in reporting long-term liabilities by the survey companies.

Examples -- Long-term Liabilities

1. African Tours and Hotels Ltd., 1976 Annual Report

Balance Sheet:

Loan Capital ... (Note 5) K.Ss 508,704

Note 5 Loan Capital

1-5 years 1,262,704

5-10 years -

Less portion repayable within one year
included in current liabilities 1,262,704

754,000

K.Ss 508,704

Although the 1-5 year loans are repayable by equal annual instalments over a number of years they could be withdrawn on demand in accordance with standard banking practice.

The loans are secured on certain assets of subsidiary companies.

2. B.A.T. Kenya Ltd., 1976 Annual Report.

Balance Sheet:

Loan(Note 11)£4,732

Note 11 Loan:

Debenture

Long term £4,732 (secured by a first charge on freehold land at Mombasa).

3. Bamburi Portland Cement Co., 1976 Annual Report.

Balance Sheet:

Debentures and loans(Note 9) £ 2,858,125

Deferred liabilities(Note 10) 1,154,461

Note 9 Debentures and Loans

8 $\frac{3}{4}$ % 'A' debenture stock 1977/82 920,000

9 $\frac{1}{2}$ % (Variable) 'B' debenture stock 1977/80 500,000

8 $\frac{3}{4}$ % 'C' debenture stock 1977 (Note 17) 389,125

8 $\frac{3}{4}$ % 'D' debenture stock 1980 (note 17) 849,000

Secured on the assets and undertaking of

the company subject to a prior charge over

book debts and inventories to secure a bank

overdraft (Note 12) 2,658,125

8½% (1975 - 7%) unsecured stock redeemable at the option of the company	200,000
	<u>2,858,125</u>

Note 10 Deferred Liabilities

Amount payable within five years	1,102,508
Amount payable in excess of five years	<u>51,953</u>
	<u>1,154,461</u>

<u>Note 12</u> Secured Bank overdraft (Note 9)	<u>2,550,000</u>
--	------------------

Note 17 Contingent Liabilities:

(a) The repayment of 'C' and 'D' Debenture Stock

(Stg.£. 1,750,000), the Deferred Creditors (Stg.£ 787,434, DM. 2,230,845, S.Fr.444,697, U.S. \$308,086) and Short Term Bank Advances (S.Fr. 10,000,000) may result in the purchase of foreign currencies at a rate in excess of that at the date of these Accounts.

4. East African Packaging Industries Ltd., 1976 Annual ReportBalance Sheet

Long Term Liabilities (Note 4) K£ 112,131

Note 4 Long-term Liabilities:

This represents suppliers' credits for machinery purchases, repayable as follows:

Year end June 1978	K£ 33,495
Year end June 1979	33,495
Year end June 1980	33,495
Year end June 1981	<u>11,646</u>

5. Hughes Ltd., 1976 Annual ReportBalance Sheet:

Long Term Loan (Note 11) K.£ 62,379

Note 11 Long Term Loans:

The long term loan is secured and is repayable in seven equal half-yearly instalments commencing 30th June, 1978.

6. Inns of Africa Ltd., 1976 Annual ReportBalance Sheet:

Long Term Loan (secured) (Note 4) K.£ 30,265

Note 4 Exchange Rate:

The secured loan, which is repayable in Sterling, is stated in Kenya currency at actual cost for repayments made subsequent to 31st December, 1976, with the remainder at K£1 to sterling £1.4014.

4.2.8 Shareholders' Equity

The shareholders' equity was usually presented in the balance sheet as the sum of the share capital and reserves. In most cases the sum of these two items was shown separately in the equity section of the balance sheet, and the captions shown in table 4(i) were used to describe such a sum. While some companies (22, 21 and 20 companies in 1974, 1975 and 1976 respectively) showed the sum of the share capital and reserves, they did not give the sum any descriptive caption. Other companies (10, 5 and 4 companies in 1974, 1975 and 1976

respectively) did not show a subtotal for shareholders' equity but grouped the shareholders' equity together with liabilities other than current liabilities. As can be seen from the table there was an increasing trend in the use of the captions shareholders' funds, shareholders' equity (Equity interest) and Shareholders' (members' or stockholders') interest.

Table 4(i) Shareholders' Equity - Balance Sheet Captions

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Shareholders' funds	11	16	18	18.97	27.59	31.03
Share capital & Reserves	6	7	4	10.34	12.07	6.90
Equity Interest or Shareholders' equity	1	2	4	1.72	3.45	6.90
Shareholders' (Members', Stockholders') interest, funds attributable to Members	8	7	8	13.79	12.07	13.79
No descriptive Caption	22	21	20	37.94	36.20	34.48
No separation of Shareholders' equity	10	5	4	17.24	8.62	6.90
Total	58	58	58	100.00	100.00	100.00

(a) Share Capital

Paragraph 2 of the Sixth Schedule requires a summary of authorized share capital. Details of how to present share capital in company accounts are given in paragraphs 2(a) to 2(d), 11(2) and 11(3).

Most of the survey companies presented only the aggregate

amount of the issued share capital in the balance sheet body and showed the details relating to the share capital in the notes to the accounts. Such details shown in the notes included the amounts of authorized and issued share capital, amounts of ordinary shares, preference shares, etc.

Examples - Share Capital

1. Bamburi Portland Cement Co. Ltd., 1976 Annual Report.

Balance Sheet

Ordinary Capital (Note 7)	£3,028,473
Preference Capital (Note 7)	80,000

Note 7:

Authorised Share Capital

14,000,000 ordinary shares of Sh. 5 each	3,500,000
100,000 7% Cumulative Redeemable	
Preference shares of Sh 20 each	<u>100,000</u>
	<u>3,600,000</u>

Issued and Fully Paid Share Capital

Ordinary Shares:

At 1st January, 1976 - 12,111,291 shares	
of Sh 5/= each	3,027,823
Issued during the year <u>2,600</u> shares	
12,113,891	
of Sh 5/= each	<u>650</u>
	3,028,473
7% Cumulative Redeemable Preference	
shares: 80,000 shares of Sh 20/= each	<u>80,000</u>

(a) The Preference Shares are redeemable at par at the option of the company.

(b) The Company has granted options to 'A' and 'D' Debenture Stock-holders as follows:

'A' Debenture Stockholders 920,000 ordinary shares of Ss 5/= each.

'D' Debenture Stockholders 1,008,000 ordinary shares of Ss 5/= each.

Such options are exercisable at any time before the 30th September of the year stated at the following

prices:	1977 at Ss 17.60 each
	1978 at Ss 18.60 each
	1979 at Ss 19.60 each

2. The Kenya Power Co. Ltd. 1976 Annual Report

Balance Sheet

Share Capital (Note 3) K£ 100

Note 3 Share Capital:

Authorized, issued and fully

paid 100 shares of K.Ss 20/= each K£ 100

3. Uplands Bacon Factory (Kenya) Ltd., 1976 Annual Report

Balance Sheet

Authorised Capital

399,950 5% Redeemable cumulative
preference shares of Ss 20/= each

(Redeemable under Article 4 of the Company's Articles)	K£ 399,950
5,000,000 Ordinary Shares of ₦1/= each	<u>250,000</u>
	<u>649,950</u>

Issued Capital and fully paid

214,959 5% Redeemable Cumulative Preference Shares of ₦s 20/= each	214,959
1,316,920 Ordinary Shares of ₦s 1/= each ...	<u>65,846</u>
	<u>280,805</u>

(b) Reserves

Paragraph 6 of the Sixth Schedule requires stating the aggregate amounts of capital reserves, revenue reserves and provisions (other than provisions for depreciation, renewals or diminution in value of assets) under separate headings.⁸ Where there has been an increase or decrease in these items, paragraph 7 requires giving the source or application of such an increase or decrease.

Most of the survey companies indicated the existence of both capital and revenue reserves in their accounts. Like share capital, only the aggregate amounts of the reserves were shown in the balance sheet body and the related details were shown in the notes to the accounts. Such details included a classification of reserves - into capital reserves, revenue reserves, etc. - and the changes that affected the reserves during the accounting period. Examples of provisions which

were usually listed under reserves include Tax Equalisation Reserve, Exchange Equalisation Reserve and Capital Redemption Reserve Fund. Capital Reserves normally included share premium account and, in some cases, revaluation reserve (surplus on revaluation of assets). In some cases the revenue reserves were grouped together with provisions and other reserves under a "General Reserves" caption. In some other cases the capital reserves were usually shown as being "non-distributable" and reserves other than capital reserves as "distributable".

Examples - Reserves

1. The East African Power and Lighting Co. Ltd., 1976 Annual Report.

Balance Sheet

Reserves (Note 8)K£ 11,198,767

<u>Note 8 Reserves:</u>	Balance 31st Dec. 1975 K£	Transfers During the year K£	Balance at 31st Dec. 1976 K£
Capital Reserve	1,298,485	-	1,298,485
Revenue Reserve:			
Geothermal Steam			
Exploration	1,615,000	-	1,615,000
Development	1,250,000	-	1,250,000
General	1,500,000	-	1,500,000
Exchange Equalisation			
Reserve	800,00	861,000	1,661,000
Taxation Equalisation			
Reserve	2,000,000	200,000	2,200,000
Retained Profit	1,483,696	190,586	1,674,282
	<u>9,947,181</u>	<u>1,251,586</u>	<u>11,198,767</u>

2. The Kenya Power Co. Ltd., 1976 Annual ReportBalance Sheet

Reserves (Note 4) K£6,457,438

Note 4 Reserves

(a) Capital Reserve:

Balance at 1st January	123,958
Transfer from Reserve and Equalisation fund	<u>59,652</u>
	<u>183,610</u>

(b) Exchange Equalisation Reserve:

Balance at 1st January	464,542
Gain on Stock redeemed during year transferred to Debenture Stock Sinking Fund	(109,374)
Gain on Conversion of Stock at 31st Dec.	<u>366,890</u>
	<u>722,058</u>

(c) Reserve and Equalisation Fund:

Balance at 1st January	379,863
Allocation for the year	22,500
Income from investments	17,939
Loss on sale of investment	-
Transfer to Capital Reserve	<u>(59,652)</u>
	<u>360,650</u>

(d) Debenture Stock Sinking Fund:

Balance at 1st January	4,818,001
Allocation for the year	267,385
Premium on Stock redeemed	(3,640)
Transfer from Exchange Equalisation Reserve	<u>109,374</u>
	<u>5,191,120</u>
Total	<u><u>6,457,438</u></u>

(NB. Comparative figures for 1975 were given but have been left out here for convenience).

3. Sasini Tea and Coffee Ltd., 1976 Annual ReportBalance Sheet.

Reserves (note 12)				341,788
<u>Note 12 Reserves:</u>		Non-distributable	Distributable	
(b) The Company:		Capital	Revenue	Unappropriated
	<u>Total</u>	<u>Reserve</u>	<u>Reserve</u>	<u>Profit</u>
	K£	K£	K£	K£
Balance at 1st				
October 1975	113,228	30,778	-	80,450
Transfer from Profit				
and Loss Account	230,560	-	-	230,560
Transfer from				
Unappropriated				
Profit to Revenue				
Reserve			<u>116,550</u>	<u>(116,550)</u>
	<u>K£ 341,788</u>	<u>30,778</u>	<u>116,550</u>	<u>194,460</u>

4.3 The Profit and Loss Account (Income Statement)

Section 149(1) of the Cos. Act states in part that "... every profit and loss account of a company shall give a true and fair view of the profit or loss of the company for the financial year." The Sixth Schedule to the Act specifies in detail the information to be included in the profit and loss account. However, like the balance sheet, compliance with the Sixth Schedule must be aimed at giving a true and fair view of the profit or loss of the company for the financial year, and where such compliance to the Sixth Schedule does not meet the objective of true and fair view, it is the duty of the directors to supplement the profit and loss account with any other information that will help to meet the said objective -- either by way of notes to the accounts or any other document annexed thereto. The Cos. Act does not require the profit and loss account to cover a one year (12 months) period although this seems to be the usual practice (see section 3.4 of chapter 3). As was seen in Chapter 3, some companies prepare statements for periods of more or less than a year.

4.3.1. Title and Form of the Profit and Loss Account

The Cos. Act uses the term "Profit and Loss Account" to refer to the Income Statement. The term "Income and Expenditure Account" is used by the Act in the case of a company not trading for profit. Table 4(j) shows the titles used by the survey companies to refer to the income statement.

Table 4(j) Profit and Loss Account -- Balance Sheet Captions

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Profit and Loss Account	50	50	52	86.21	86.21	89.66
Revenue Account or Revenue Appropriation Account	2	2	2	3.45	3.45	3.45
Manufacturing, Trading and Profit and Loss Account	1	1	1	1.72	1.72	1.72
Statement of Profit and Appropriations	2	2	2	3.45	3.45	3.45
Profit and Loss Appropriation Account	2	2	1	3.45	3.45	1.72
Income and Expenditure Account	1	1	-	1.72	1.72	-
Total	58	58	58	100.00	100.00	100.00

The Cos. Act does not advocate the use of any specific form of the Profit and Loss Account. But paragraph 14(6) of the Sixth Schedule seems to suggest the use of an "all-inclusive" Profit and Loss Account, whereby both operating and non-operating (extra-ordinary or non-recurrent) gains and losses are included in the Profit and Loss Account. A Profit and Loss Account which excludes extra-ordinary or non-recurrent items is sometimes referred to as a "Current Operating Performance Income Statement"⁹. Table 4(k) shows the number of survey companies that presented either an all-inclusive or current operating performance Profit and Loss Account. In most cases only the

profit or income before taxation was shown in the main body of the Profit and Loss Account and the related details which included the income sources and expenses were shown in the notes to the accounts. In some cases charges to revenue to arrive at the "Income before taxes" were given in a separate inset just below the caption "Income before taxes". In such cases the Caption "Income before taxes" was usually followed by the words "after charging the following items" or "after charging the items inset below." Table 4(k) shows that the majority of the survey companies used the all-inclusive income

Table 4(k) Forms of the Profit and Loss Account

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
All-inclusive	36	34	34	62.07	58.62	58.62
Current Operating Performance	22	24	24	37.93	41.38	41.38
Total No. of Companies	58	58	58	100.00	100.00	100.00

statement or Profit and Loss Account. The examples below show some of the common forms of the Profit and Loss Account used by the survey companies.

Examples - Profit and Loss Account Forms

1. Bird & Co. (Africa) Ltd., 1976 Annual Report

Profit and Loss Appropriation Account as at 30th June, 1976

	£Sterling	£Sterling
Accumulated Deficit at 30th June 1975		1,307,340
Less: Excess of Income Over		
Expenditure for the year ended 30th June, 1976	9,035	
Foreign Exchange Surplus		
re-compensation: Realized July 1976	8,410	
Revaluation of last two instalments	16,012	
Director's Fees Waived	<u>420</u>	<u>33,877</u>
Accumulated Deficit at June, 1976		<u>£ 1,273,463</u>

2. East African Cables Ltd., 1976 Annual Report

Profit and Loss Account for the 52 Weeks Period Ended
1st January, 1977

	<u>Note</u>	<u>1976</u> K£	<u>1975</u> K£
Sales		<u>1,729,176</u>	<u>1,560,483</u>
Profit before Taxation	2	359,887	209,205
Taxation	3	<u>167,000</u>	<u>98,000</u>
		192,887	111,205
Retained Profit brought forward		<u>125,598</u>	<u>94,393</u>
Profit available		<u>318,485</u>	<u>205,598</u>
Appropriations:			
Dividends: Final - Proposed		80,000	80,000
Bonus - Proposed		<u>20,000</u>	<u>-</u>
		<u>100,000</u>	<u>80,000</u>
Retained Profit Carried Forward		<u>218,485</u>	<u>125,598</u>

(NB. Note 2 gave the amounts charged to arrive at the profit before taxation and Note 3 indicated that taxation was based on the profit for the year.)

3. Eaagards Ltd., 1975 Annual Report

Profit and Loss Account for the Period 1st June, 1974
to 31st March, 1975

	<u>K.Šs</u>		<u>K.Šs</u>
Depreciation of fixed assets ...	80,014.00	Profit on farming activities	692,556.30
Audit fee (1973/74 additional K.Šs 1,270/90)	6,270.90	Interest on Overseas investment and deposit	12,557.40
Directors' fees ...	8,000.00	Dividend on Investments -	
Net profit carried down	796,544.15	Trade	1,702.00
		Other	-
		Interest -	
		holding company	575.35
		Profit on Sale of Investments	183,438.00
	<u>890,829.05</u>		<u>890,829.05</u>

(NB. Comparative figures for 1974 and a separate note on the Directors' remuneration were given but they have been left out here for convenience).

4. Ol Pejeta Ranching Ltd., 1976 Annual ReportProfit and Loss Account for the year ended 31st December,1976

	<u>Note</u>	1976	1975
	£	£	£
Profit for the year		66,981	48,225
After Charging:			
Depreciation		18,254	16,798
Auditors' remuneration and expense		377	675
Directors' emoluments - fees		2,000	1,900
Interest payable:			
Bank overdraft	3,843		2,987
Short term loan	<u>980</u>	4,823	980
Taxation	(2)	<u>30,035</u>	<u>21,332</u>
Profit before Extraordinary item		36,946	26,893
Add: Extraordinary item.....	(3)	<u>96,263</u>	<u>-</u>
Profit after taxation and Extraordinary item		<u>133,209</u>	<u>26,893</u>
Dividends:			
Ordinary 15% (1975 10%) (proposed).....	15,000		10,000
Deferred 15% (1975 7½%) (proposed).....	<u>30,000</u>		<u>15,000</u>
		<u>45,000</u>	<u>25,000</u>

	£	£
Retained Profit		
for the year	88,2099	1,893
Retained Profit brought forward	<u>70,548</u>	<u>68,655</u>
Retained Profit carried forward	<u>158,757</u>	<u>70,548</u>
Earnings per share of \$4/= each	\$ 49	36

The calculation of earnings per share is based on earnings of £36,946 (1975 £ 26,893) and 1,500,000 shares (1975 1,500,000) in issue throughout the year ended 31st December, 1976.

<u>Note 2 Taxation</u>	<u>1976</u>	<u>1975</u>
Taxation based on profit for the year:	£	£
Corporation tax (45%)	29,484	21,332
Underprovision in respect of previous year.....	<u>551</u>	<u>-</u>
	<u>£ 30,035</u>	<u>21,332</u>

Note 3 Extraordinary item

Profit on disposal of property	<u>£ 96,263</u>	<u>-</u>
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4.3.2. Revenue From Operations

The Sixth Schedule to the Cos. Act does not require disclosure of all or total revenue from operations with the exception of "income from investments, distinguishing between trade investments and other investments" (Paragraph 12(1)(g)). The survey showed that although there was an increasing trend in the number of companies disclosing total revenue from operations over the survey period, most of the survey companies did not give such a disclosure. However, income from investments was disclosed by the companies showing investments in their accounts.

For companies disclosing revenue table 4(1) shows the descriptive captions used to describe revenue derived from selling products and/or rendering services. Most of the companies disclosing revenue used the term "Turnover". In most cases whichever caption used was defined either in the Company's accounting policies or notes to the accounts (see some of the definitions in the examples below). The companies

Table 4(1) Revenue from Operations - Descriptive Captions

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Turnover	9	9	13	64.28	52.94	56.52
Gross revenue, Revenue or Revenue from sales	1	2	3	7.14	11.76	13.04
Sales or Net Sales	2	4	5	14.29	23.54	21.74
Income	2	2	2	14.29	11.76	8.70
Companies disclosing revenue	14	17	23	100.00	100.00	100.00
Companies not disclosing revenue	44	41	35			
Total number of companies	58	58	58			

giving a definition of turnover (or whichever caption used) were 12, 16 and 19 in the years 1974, 1975 and 1976 respectively.

Examples - Revenue from Operations - Definitions of CaptionsUsed(a) Gross Revenue1. Sasini Tea & Coffee Ltd., 1976 Annual Report

Note 1(f) Gross revenue represents amounts receivable from customers of the group.

2. The Kenya Power Company Ltd., 1976 Annual Report

Note 1(b) Revenue represents the ascertained cost of electrical energy supplied to the Authorised Distributor, The East African Power and Lighting Co. Ltd. computed in accordance with the Nairobi and Western Kenya (Bulk Supply) Agreement, 1955 and the Bulk Supply Licence No. 2 of 8th June 1955.

(b) Sales1. Kenya National Mills Ltd., 1976 Annual ReportAccounting Policies

Sales are net invoiced amounts to external customers.

(c) Turnover1. CMC Holdings Ltd., 1976 Annual Report

Note 1(G) Turnover is based on net invoiced sales, excluding inter-company and inter-departmental sales.

2. Joresho & Kiora (Plantations) Ltd., 1976 Annual Report

Note 1(b) Turnover is principally income from coffee and tea. The coffee income comprises current crop sales, stocks on hand and excess proceeds received in respect of the previous year's crop. Current crop sales represent payouts received up to 31st March 1976. Coffee stocks on hand are valued at estimated proceeds receivable, based on average payouts received up to 31st March.

Stocks, other than coffee, are valued at the lower of cost and net realisable value.

4.3.3 Expenses - Items charged against revenue to determine profit before taxation

Most of the survey companies did not disclose all the charges against revenue to determine the profit before taxation. The only charges which were separately disclosed by all the companies were the directors emoluments (pensions, etc.), the Auditors remuneration, depreciation or amortization expense (with the exception of one company - Bird & Co. Africa Ltd. - which showed no depreciation or amortization and showed no fixed assets or intangibles in its accounts), and the interest on loans (for companies which had loans on which interest was payable). The separate disclosure of these items by the survey companies may be due to the requirement for their disclosure by the Cos. Act (See section 197 of the Cos. Act and paragraphs

12(1) and 12(1)(b) of the Sixth Schedule to the Act).

Other charges to revenue disclosed by some of the survey companies included selling and general administration expenses, provision for bad debts, cost of production or factory cost of manufacturing, loss on disposal of assets, loss on devaluation, provision for replacement of fixed assets, compensation for Africanization and redundancy, staff training expenses, provision for abnormal contingency, plant hire charges, cost of capitalisation issue of shares, share of losses of Associates, and Cost of goods sold. Unlike most U.S.A. companies which disclose the cost of goods sold¹⁰, only one of the Kenyan survey companies - Uplands Bacon Factory Kenya Ltd. - disclosed the cost of goods sold and used the caption "cost of sales", and the East African Power Co. Ltd. disclosed the cost of electricity supplied and used the caption "Cost of Bulk Supply".

4.3.4. Depreciation Methods

Paragraph 12(1)(a) of the Sixth Schedule requires showing "the amount charged to revenue by way of provision for depreciation, renewals or diminution in value of fixed assets." And paragraph 14(2) requires stating by way of note or otherwise, "if depreciation or replacement of fixed assets is provided for by some method other than a depreciation charge or provision for renewals, or is not provided for, the method by which it is provided for or the fact that it is not provided for, as the case may be".

It is generally recognized that assets have a span of life during which services are received from the asset. Accountants normally measure the amount or value of services to be received from an asset over the asset's useful life by the cost incurred in acquiring that asset, less any salvage value. This cost is normally spread over the useful life of the asset in such a way that a portion of the cost is charged against the income of each period during which the asset provides services. The allocation of the cost of an asset over the asset's useful life is what accountants normally refer to as "depreciation". The period of allocation of the cost of the asset is normally the accounting period. It may be noted, therefore, that depreciation of an asset as used by accountants, being the allocation of the cost of the asset over the asset's useful life, may not necessarily reflect the physical deterioration or the decrease in the market value of the asset.

There are several methods used in computing depreciation of an asset:- Straight Line Method; Units of Output Method; Accelerated Methods, which include the Sum-of-the-year's digits method and the Declining balance Method; and, the Compound Interest Methods, which include the Sinking Fund Method and the Annuity Method.¹¹ Some authors have argued that the choice as to which method of depreciation to use should depend on the pattern of net receipts from the assets, that is, the earning power of the asset or the value of the services received from the asset.¹²

The depreciation methods used by the survey companies are set out in table 4(m). As can be seen from the table there was an increasing trend over the survey period in the number of companies disclosing the depreciation method used. The straight line method of depreciation was found to be most used by the survey companies which disclosed the depreciation method. Examples of depreciation method disclosures are presented below.

Table 4(m) The Depreciation Methods Used

	No. of Companies			Percentages		
	1974	1975	1976	1974	1975	1976
Straight line	11	26	44	91.67	89.66	86.28
Declining (reducing) Balance	1	2	4	8.33	6.90	7.84
Various Methods for various asset classes or categories	-	1	2	-	3.44	3.92
Other	-	-	1	-	-	1.96
Cos. disclosing Depreciation Method	12	29	51	100.00	100.00	100.00
No fixed assets hence no depreciation	1	1	1			
Cos. not disclosing depreciation method	45	28	6			
Total no. of companies	58	58	58			

Examples -- Depreciation Method Disclosures

1. A. Baumann and Company Ltd., 1976 Annual Report

1(b) Depreciation:

This is calculated to write off the cost or

valuation of fixed assets over their expected useful lives by equal annual instalments. Since 1st November 1970 depreciation has not been provided on freehold land and buildings, nor on non-industrial leaseholds where the balance of term exceeds 30 years.

2. Car & General (Kenya) Ltd., 1976 Annual Report

Accounting Policies

1(A) Depreciation:

Depreciation of fixed assets (other than properties) has been provided on a reducing balance method at rates calculated to write down the class of asset over the period of its estimated useful life. Properties are depreciated by equal annual amounts calculated to write down the asset over the unexpired portion of the lease.

3. CMC Holdings Ltd., 1976 Annual Report

Notes to the Accounts - Accounting Policies

(i) Depreciation is calculated to write off the book value of the assets on a straight line basis over the expected useful lives of the assets concerned. The principal annual rates used for this purpose, which are consistent with those of the previous year are as follows:

Land and buildings	2%
Plant, furniture and equipment:	
- Workshop plant and office equipment	15%
- Office and house furniture	10%

- Loose tools	33 1/3%
- Air Conditioners	20%

Motor Vehicles:

- Contract leased	33 1/3%
- Company	20%

(ii) Specific provision is not made for the replacement of fixed assets, but, in the opinion of the directors, profits retained and borrowing facilities available are adequate for this purpose.

4. Hughes Ltd., 1976 Annual Report

Accounting Policies

1(b) Depreciation

Depreciation has been provided on all fixed assets at rates calculated to write them off over the period of their estimated useful lives. With effect from 1st January, 1976 depreciation of fixed assets was changed from the reducing balance method to the straight line method.

5. Kenya Power Company Ltd., 1976 Annual Report

Accounting Policies

(d) Depreciation

No depreciation of fixed assets is charged in the accounts. Instead, a charge is made in the revenue account towards the redemption of the Debenture Stock in accordance with the provisions of the Bulk Supply Licence No. 2.

6. Theta Group Ltd., 1976 Annual ReportAccounting Policies(a) Depreciation

Depreciation of fixed assets is on a reducing balance basis calculated to reduce costs of the assets to a nominal value at the end of the terms of their useful lives. The rates used are as follows:

(i) Leasehold land and development	2 $\frac{1}{2}$ %
(ii) Buildings and Machinery at the estate	3 $\frac{1}{2}$ %
(iii) Improvement to rented premises.....	10%
(iv) Motor Vehicles	25%
(v) Plant, furniture and fittings	25%

4.4 Conclusion

The Balance Sheet and the Profit and Loss Account are the two main financial statements required by the Cos. Act to be furnished to shareholders in connection with the annual general meeting of the company. The Sixth Schedule to the Act specifies the information required by the Act to be included in these two financial statements. This chapter has surveyed the financial reporting and accounting practices that relates to the major items of these two financial statements, as reflected in the annual financial reports of the 58 Kenyan survey companies. As indicated in the survey results, some companies did not disclose the basis of valuing some assets, depreciation method used, etc. It therefore follows that the following conclusions are based

on disclosures of the procedures followed by only a portion of the survey companies as indicated in the chapter.

(a) Balance Sheet.

All the survey companies use the title "Balance Sheet" in their financial reporting and most of them use the financial position form of the balance sheet. Stocks are in most cases valued at the "lower of cost and net realisable value", and the fixed assets, which in most cases are shown in classes or categories of assets, are normally listed in the accounts "at cost or valuation". Investments in subsidiaries and associates are in most cases valued using the cost method rather than equity method. Survey results for some other balance sheet items are presented in the chapter.

(b) The Profit and Loss Account

The title used by most of the survey companies is "Profit and Loss Account", and most of the companies use the "all-inclusive" form of income statement. Most of the survey companies do not disclose sources and amounts of total revenue with the exception of the revenue from investments. Not all expense items charged against revenue to arrive at the Profit Before Taxation are disclosed by most of the survey companies. The only items charged against revenue that are disclosed by most of the survey companies are the Directors' emoluments, the Auditors' remuneration, the depreciation (Amortisation) expense; and the interest on loans. The survey on the depreciation method used shows that the straight line

method of depreciation is the most used by the survey companies.¹

FOOTNOTES TO CHAPTER 4

1. See for example S. Davidson, Op. Cit., pp. 3.6-3.8, 3.14-3.25, and 3.27-3.41.
2. G.A. Lee, Modern Financial Accounting, Op. Cit., P. 311
3. See AICPA, Accounting Trends and Techniques, 1976 P. 77 and Walter B. Meigs, et al., Op. Cit., P. 146
4. See CICA, Financial Reporting in Canada, 1973, P. 28 and AICPA, Accounting Trends and Techniques, P.77
5. Quoted in CICA, Ibid., P. 28
6. See CICA, Ibid., P. 40
7. For a discussion about deferred taxes see G.A. Lee, Op. Cit., PP. 280-284, and Walter B. Meigs, et al., Op. Cit., Chapter 20.
8. See paragraph 25 of the Sixth Schedule to the Act for the definitions of the terms "reserve" and "provision"
9. See W.B. Meigs and C.E. Johnson, Accounting, The Basis For Business Decisions, 2nd Ed. (McGraw-Hill Book Co., 1967) PP. 557-558.
10. See AICPA, Accounting Trends and Techniques, PP. 200-201
11. For a detailed discussion on the methods of depreciation used see W.B. Meigs and C.E. Johnson, Op. Cit., PP. 408-413, and S. Davidson, Op. Cit., pp. 18.1-18.25
12. See for example, J.R. Hanna, Accounting Income Determination: Selected Readings and Problems, 2nd Ed., (Hamilton, Ontario: McMaster University, 1976), Section 11A, P.3

CHAPTER 5

SUMMARY, CONCLUSIONS, AND RECOMMENDATIONS

This thesis has attempted to survey and present some of the accounting and financial reporting practices in 58 Kenyan public companies. The purpose of this chapter is to present a brief summary of the main findings of the survey, and to draw some possible conclusions as regards the survey findings. The chapter also presents some recommendations as to the possible ways of improving accounting and financial reporting practices in Kenya, and suggests possible areas of further research and study in the field of accounting in Kenya.

5.1 General Considerations

It was noted in Chapter 1 that the business world is a world of alternatives. A choice has to be made as to which alternative to select so as to achieve the desired goals. The notion of GAAP in accounting leads to a variety of alternative accounting and financial reporting practices, all of which are acceptable. Even the flexibility in legal requirements allow different ways of treating certain items of account. The problem for accountants in the various firms, at the moment, is to decide which of the several accepted methods to use in accounting and financial reporting for their firms. At the same time changes in the environment as well as in the accounting profession itself call for adaptability of accounting practice to such

changes.

Although there are a number of acceptable methods of accounting and financial reporting, some particular methods may provide better economic information and therefore be more widely used than others. This is clear from the survey results presented in Chapters 3 and 4 of this thesis. A look at the survey results shown in the tables in these two chapters may help to draw some conclusions as to the general acceptability of particular practices.

One of the assumptions made in Chapter 2 was that accounting practice in Kenya is done within the limits of its environment. The environment of accounting practice was then defined as the legal requirements as well as the requirements of the accounting profession itself. It was therefore assumed that since the professional accounting body in Kenya is still at the "take off" stage, most of the accounting practice is regulated by the requirements of the Cos. Act. Consequently, references to the requirements of the Cos. Act were made from time to time in the analysis of the survey items, the aim in such cases being to examine how and whether such requirements of the Act are followed by the survey companies, and whether practices other than those required by the Act are followed by these companies. Such other practices may include those followed in other countries and those recommended by professional accounting bodies all over the world. Comparison was therefore made, in some cases, with the accounting and financial reporting practices in three countries - Britain, Canada and U.S.A. While the

accounting profession is also highly developed in countries other than these three countries, practice in Kenya has been most affected by practice in Britain, Canada and U.S.A. Therefore, comparison with these countries appears most reasonable, even though the comparisons are made only for the purpose of shedding light on how the accounting practice in Kenya differs from practices in other countries of the world. Actual differences between Kenya and other countries can best be seen by comparing the survey results in this thesis with practices in the other countries that may be of interest to the reader of this thesis.

In the survey results presented in Chapters 3 and 4, an attempt was made to indicate the various ways of treating or reporting each of the survey items and which of these ways were used by the survey companies. The use of the tabular method in presenting the results of the survey over the period of three years was also designed to show the trend in practices over the survey period. Examples from some of the annual reports of the survey companies were presented in order to highlight some of the points made in the discussion of the reported items.

It should be noted, however, that while the survey dealt mainly with the annual reports which are normally furnished to shareholders in connection with the annual general meeting of the company, reporting as to the status and operations of companies in Kenya is also done in several other ways. Such other common ways include the use of interim statements (reports), news-letters to members, news announcements (through the press), preliminary statements, etc. These are normally released by

companies at various time intervals throughout the year.

5.2 Summary of Findings and Conclusions

The detailed survey results are presented in chapters 3 and 4. However, the purpose of this section is to recapitulate and summarize the survey results as presented.

As noted in chapter 2, most of the survey companies (over 67%) are in the Manufacturing and Agricultural sectors of the Kenyan economy. In chapter 3 it was noted that most of the companies operate under the parent - subsidiary form of organization and present group accounts (Consolidated Statements). In addition to the statements required by the Cos. Act, some companies give additional information and the survey results show that there was an increasing trend in the number of companies presenting supplementary or additional financial information over the survey period - although most of the companies did not give such supplementary data (See table 3(g)). There was an increase over the survey period in the number of companies disclosing their accounting policies, and although the Cos. Act requires the presentation of the Directors' report - and does not mention the Chairman's report - most companies presented both the Directors' and Chairman's reports. Most of the survey companies use a one year accounting period and most of them end their years in December, June, September or March (See table 3(c)). Although Swahili is the national language of Kenya, only a few companies present the Swahili version of their

financial report. All the survey companies presented financial statements on a historical cost basis and none of them presented any supplementary data adjusted for inflation although some companies showed a willingness to present such data if there were a consensus as to which inflation accounting method to use (See Section 3.9 of Chapter 3). A survey on the auditors' report showed that most of the auditing firms use a standard form report which in most cases consist of two paragraphs -- containing the scope of the auditors' examination and their professional opinion.

In Chapter 4 a survey of practices relating to the Balance Sheet and Profit and Loss Account was presented. The results show that there was an increasing trend in the number of companies using the financial position form of Balance Sheet over the survey period, and most of the companies used the all-inclusive form of profit and loss account. Some of the companies did not disclose certain information such as the valuation basis of some balance sheet items, sources and amounts of total revenue, etc. The straight line method was found to be in use in most of the survey companies. In most cases it was found that most of the terms used in financial reporting were those used by the Cos. Act -- for example, Balance Sheet, Profit and Loss Account, Debtors, Creditors, Stocks, etc.

The results of the survey as summarized above leads one to draw several conclusions as regards accounting and financial reporting practices in Kenya:

- (1) All survey companies present the Balance Sheet and Profit and Loss Account in their annual report. While this may be due to the requirement of the Cos. Act, it could be that these two statements are the most important statements in financial reporting. In addition to these two statements, companies are increasingly giving additional financial data, which may imply that the two statements - Balance Sheet and Profit and Loss Account - may not necessarily give a "true and fair view" of the status and operations of the firm alone unless they are supplemented by other information.
- (2) While accounting practice in Kenya follows closely the requirements of the Cos. Act, the fact that information other than that required by the Act is given, and the fact that there were changes in practices over the survey period, indicate that accounting practice is in itself dynamic and changes with time, being affected by changes in the environment as are many other professions. It therefore, follows that any rules or laws governing accounting practice have to be flexible to allow for any necessary changes. The Cos. Act seems to be flexible in this respect in that it allows some adaptation of accounting practice to changes and seems to stipulate only the minimum requirements to be met by companies in financial reporting.
- (3) While there are variations here and there as regards practices followed by the survey companies, a general look at the statements presented by these companies will indicate that

there is some standardization in financial reporting, particularly as regards such matters as:

- (a) The general presentation of statements and items in the financial reports as well as the types of statements presented.
- (b) The types of terminologies used for the various statements and items of the reports. It could be said that the need by the companies to highlight disclosures required by the Cos. Act in the reports is amplified by the use of the terms used by the Act.
- (c) The wording and presentation of the auditors' report. Most auditing firms seem to use a standardized form of report - the form, wording, title and addressee of the reports seems to be standardized with little variations from one auditors' report to another.

5.3 Recommendations

(a) Policy Recommendations.

It was stated in chapter 1 that accounting has been described as "the language of business" (See footnote 2 in chapter 1). Business of one kind or another has become the main source of income for many Kenyans today. Many businesses are therefore springing up in many sectors of the economy and many more businesses are going public. The necessity to report on the financial status and operations of firms to

interested external parties is thus growing. As the Kenyan economy grows and businesses expand, the need for financial reporting becomes more important. This calls for the following policy recommendations:

- (1) There is a need for a strong professional accounting body to regulate and give guidance to accounting practice which will meet the needs and requirements of the users of the accounting information in the Kenyan environment. As stated in Chapter 2, there is already a step towards the establishment of such a body although it has not taken up strongly so as to compare favourably with other professional accounting bodies elsewhere.¹ This body needs the government's support as well as the support of the accountants in Kenya and the support of the Kenyan business community so that it can get the strength necessary to regulate and give guidance to the accounting practice in Kenya. Since such a body needs guidelines as to what is actually happening in practice, it is hoped that the survey results in this thesis will help this body as well as the government in their efforts to regulate and legislate laws affecting accounting practice in Kenya.
- (2) Although at the moment most of the accounting and financial reporting practice in Kenya is based mainly on the requirements of the Cos. Act, care must be taken so as not to present the status and operations of the business firms only in accordance with the Cos. Act. This is because

accounting, as noted elsewhere in this thesis, is dynamic in itself and accounting practice develops as the need for it arises. The purpose of accounting reports is to reflect economic reality. Therefore, presentation of accounts only in accordance with the minimum requirements of the Act may make it impossible to disclose some factors which affect the business in one way or another just because the Cos. Act does not require their disclosure. It is therefore necessary for the companies to be free to adapt any accounting practice recommended by other accounting bodies outside and inside Kenya - so long as such recommendations are feasible and culturally compatible in the Kenyan environment. The Cos. Act should act as a minimum disclosure requirement, but companies should present such other financial information that may be deemed necessary. M. Eaton says:

"It would be a great misfortune for ... business, and the whole economy if uniform accounting rules were to be prescribed by governmental fiat. It would mean the end of progress ..."²

It may be mentioned here that the survey results show that some companies do in fact give financial information in addition to that required by the Cos. Act. At the same time, financial reporting should not be used to obscure the real facts relating to the status and operations of the firm so as to achieve social and political objectives of a particular group in the society. Bray and Shearsby have this to say:

"If financial [Statements] are to serve all the purposes which society is beginning to require of them it is essential that they should give a clear and orderly picture, which can be readily assimilated and understood, of the operations of an enterprise. The preparation of such [Statements] involves the accurate analysis and classification of the transactions arising out of the conduct of the business, expressed in terms of money. Ambiguity of any kind is to be avoided, and so far as possible emphasis should rest upon those figures which tend most clearly to bring to light the financial strength and weakness of the business and the causes which have brought this about"³.

- (3) As already stated, the survey results show that all the survey companies presented their financial statements on a historical cost basis. None of the survey companies presented any supplementary data to show the effect of inflation. However, the fact that the Cos. Act. requires disclosure of the current values of some assets and permits a valuation of fixed assets means that it is flexible in its application of the historical cost basis. The impact of inflation on the status and operations of the business is, at the moment, a factor which needs some consideration and it is necessary for accountants in Kenya to determine the best way of showing the effect of inflation on the reported historical cost financial statements.⁴

(b) Recommendations for further Study

It is evident that the survey in this thesis has dealt mainly with the reporting or dissemination aspect of financial accounting as reflected in the annual financial reports of the 58 survey companies. Little has been said as

regards the pre-reporting aspect of accounting, i.e., matters such as the keeping of books of accounts, treatment of certain items of accounts, etc. By contributing to studies of what is actually happening in practice in the accounting field in Kenya, this study implies a need for further research in this area. Topics that may be of interest for further study include the following:

- (1) Financial reporting practices in the years subsequent to the period covered by this thesis. This will help to examine the trend in financial reporting practices, and how such practices differ from what the thesis survey has found out.
- (2) The pre-reporting aspect of financial accounting in Kenya, which may involve an indepth study of the treatment of various items of account in company books and matters incidental thereto, thus bringing to light some of the actual accounting practices followed by Kenyan Companies.
- (3) The effects, or otherwise, of changes in the accounting and financial reporting practices in other countries on the accounting and financial reporting practices in Kenya. This may also include the effects on the practices in Kenya of recommendations by professional accounting bodies all over the world.

- (4) The effects of the legal requirements on Company Accounts in Kenya.
- (5) The comparability and the variability of accounting and financial reporting practices between firms in various industries in Kenya. This may help the regulatory and legislative bodies in their efforts to devise appropriate practices for firms in the various industries. In addition, this will aid in the gathering and dissemination of industry statistics, a great and largely unfilled need in Kenya today.
- (6) A survey of the users of financial statements in Kenya and their influence on the accounting and financial reporting practices. (This assumes that the needs of the users of financial reports will influence financial reporting practices in firms).
- (7) A search into better methods of treating certain items of accounts. For example, as regards the choice of the best depreciation method to use, it is argued that "... the conventional depreciation method (straight line, sum - of - the - years digits, declining balance, or other method) which is most appropriate is dependent upon the pattern of net receipts, and that this should at least be considered in the selection of the depreciation method to be used in the accounts."⁵ If it is therefore assumed that depreciation or the decline in value of an asset depends on the pattern of net receipts, then it is

necessary to find out the pattern of earnings or net receipts in Kenyan firms in order to determine the appropriate depreciation methods to be used by these firms.

- (8) The extent to which reporting practices in Kenya are influenced by the auditors. That is, are the auditors exerting heavy influence on reporting practice, and is this influence beneficial?
- (9) This thesis has basically attempted to provide descriptive rather than narrative analysis of reporting practices. While this in itself has been a considerable task, an analysis of reporting practices with respect to "best" or "conceptually correct" practices would greatly improve the usefulness of such studies and would represent a logical extension of this thesis.

5.4 Concluding Remarks

This chapter has briefly summarised the main findings and conclusions of the survey that forms the basis of this thesis. Some policy recommendations which may help to improve the accounting practice in Kenya were made in the chapter. It was also noted that the survey did not deal with every aspect of accounting or financial reporting. Recommendations were therefore made as to the possible areas for further study in the field of accounting practice in Kenya. In concluding the chapter - and the thesis as a whole - it may be noted that the

accounting field is a wide one. It is also evident that accounting or financial reporting, is an essential ingredient of the business world. Like many other professions, accounting practice develops and changes over time. It is therefore necessary for researchers in this field in Kenya to continue coming up with studies in this area so that the Kenyan accountants, and businessmen in general, may be kept informed of the trend in accounting practice as well as the acceptability or otherwise of any accounting practices in Kenya. This has to be a continuous effort. To all accountants in Kenya, to all students and lecturers of accounting in Kenya, and to all researchers in the field of accounting in Kenya, one can only say that let the struggle to improve and consolidate accounting practice in Kenya - and in the whole world at large - continue unabated.

FOOTNOTES TO CHAPTER 5

1. See footnote 1 in Chapter 2.
2. From address by M. Eaton, then president of AICPA, delivered before the Illinois Society of CPA, June 7th, 1957. Quoted in D.R. Ladd, Contemporary Corporate Accounting and the Public, (R.D. Irwin, Inc. 1963), p. 29.
3. F.S. Bray and H.B. Shearsby, Design of Accounts, 3rd Ed., (Oxford: Oxford University Press, 1949), P. 1
4. It may be noted here that other countries do not currently report either price-level adjusted statements or current-value statements - although there is a general feeling that such statements would be appropriate in periods of changing prices. Kenya should, however, be aware of changes in practice elsewhere in this respect and adopt appropriate reporting practices when such can be determined.
5. J.R. Hanna, Op. Cit., Section 11A, P.3

APPENDIX A

List of Companies Included in the Survey

1. African Tours and Hotels Ltd.
2. A. Baumann & Co. Ltd.
3. Bamburi Portland Cement Co. Ltd.
4. B.A.T. Kenya Ltd.
5. Bird & Co. (Africa) Ltd.
6. Brooke Bond Liebig (Kenya) Ltd.
7. Car & General (Kenya) Ltd.
8. Carbacid Investments Ltd.
9. City Brewery Investments Ltd.
10. C.M.C. Holdings Ltd.
11. Consolidated Holdings Ltd.
12. Credit Finance Corporation Ltd.
13. Diamond Trust Company of Kenya
14. Dunlop Kenya Ltd.
15. Eaagads Ltd.
16. E.A. Bag and Cordage Co. Ltd.
17. E.A. Breweries Ltd.
18. E.A. Cables Ltd.
19. E.A. Oxygen Ltd.
20. E.A. Packaging Industries Ltd.
21. E.A. Portland Cement Ltd.
22. E.A.P. and Lighting Co. Ltd.
23. E.A. Road Services Ltd.
24. Elliot's Bakeries Ltd.

25. Etco Ltd.
26. George Williamson (Kenya) Ltd.
27. Hughes Ltd.
28. Hutchings Biemer Ltd.
29. I.C.D.C. Investment Co. Ltd.
30. Inns of Africa Ltd.
31. Kakuzi Ltd.
32. Kamiti Valley Coffee Estates Ltd.
33. Kapchorua Tea Co. Ltd.
34. The Kenya Farmers Association Co-operative Ltd.
35. Kenya Co-operative Creameries Ltd.
36. Kenya Hotels Ltd.
37. Kenya National Mills Ltd.
38. Kenya Oil Co. Ltd.
39. Kenya Orchards Ltd.
40. K.P.C.U. Ltd.
41. Kenya Power Company
42. Kulia Investments Ltd. (Block Hotels Ltd.)
43. Idmuru Tea Co. Ltd.
44. Loresho & Kiora (Plantations) Ltd.
45. Marshalls (E.A.) Ltd.
46. Mercat Ltd.
47. Motor Mart and Exchange Ltd.
48. Nation Printers and Publishers Ltd.
49. National Industrial Credit (E.A.) Ltd.
50. Ol Pejeta Ranching Ltd.

51. Pan Africa Insurance Co. Ltd.
52. Pearl Dry Cleaners Ltd.
53. Phillips, Harrisons and Crossfield Ltd.
54. Sasini Tea and Coffee Ltd.
55. Sofar Investments Ltd.
56. Theta Group Ltd.
57. Timsales Ltd.
58. Uplands Bacon Factory (K) Ltd.

The above list represents one firm which was audited by the survey companies. Effectively, therefore, the number of auditing firms represented in the survey for the years 1974, 1975 and 1976, were 2, 4 and 6 respectively.

As can be seen from the table, the number of auditing firms, taken together as one firm, which audited the survey companies over the survey period was 2, 4 and 6 respectively. The analysis in Section 3.10 shows that the number of auditing firms represented in the survey was significantly higher than the number of other auditing firms.

(A) *Number of auditing firms represented in the survey as compared to the number of other auditing firms.* Several tests were conducted to determine whether the fact that one auditing firm represented the survey companies affects the results of the tests. In Section 3.10 significantly more firms were represented in the survey than other auditing firms.

APPENDIX B

Number of Auditing Firms Represented

The table below gives the number of auditing firms represented in the survey, and the number of companies audited by each auditing firm over the survey period. The table shows that the number of auditing firms represented in the survey for the years 1974, 1975 and 1976, were 10, 12 and 11 firms respectively. However, it may be mentioned that Deloitte & Co., and Gill & Johnson represent one firm operating under two different names. Effectively, therefore, it can be said that the number of auditing firms represented in the survey for the years 1974, 1975 and 1976, were 9, 11 and 10 respectively.

As can be seen from the table Deloitte & Co., and Gill & Johnson, taken together as one firm, audited about 48% of the survey companies over the survey period. It would therefore seem that the analysis in Section 3.10. of Chapter 3 that relates to the auditors' report would be biased since one firm (Deloitte & Co., and Gill & Johnson) audited most of the companies as compared to the number of companies audited by other auditing firms. Several tests were made to determine whether the fact that one auditing firm audited most of the survey companies affects the results and conclusions drawn in section 3.10 significantly. These tests included the following:

- (1) An analysis excluding the companies audited by Gill & Johnson (Since Gill & Johnson audited an extreme number of companies), but including companies audited by Deloitte & Co.
- (2) An analysis excluding the companies audited by both Gill & Johnson and Deloitte & Co.
- (3) An analysis involving a random selection of a maximum of 6 survey companies audited by each of the auditing firms for each of the survey years. (The average number of companies audited by each auditing firm over the survey period of 3 years, assuming that the effective number of auditing firms represented is 9, 11 and 10 for 1974, 1975 and 1976 respectively, is 5.8 or approximately 6 companies).

In all these three test cases, it was found that the conclusions drawn in Section 3.10. as regards the items discussed under the auditors' report were unaffected.

9 Parvill, Williams & Co.	2	2	2
10 Perry & Co.	1	1	1
11 Price Waterhouse & Co.			
12 Price, Waterhouse & Co.			

Auditing Firms Represented and the Number
of Companies Audited by Each Firm

	No. of Companies Audited			Percentage		
	1974	1975	1976	1974	1975	1976
1 Alexander, Maclellan, Trundell & Co.	4	2	1	6.90	3.45	1.72
2 Coopers & Lybrand	8	7	7	13.79	12.07	12.07
3 Deloitte & Co.	8	9	9	13.79	15.52	15.12
4 Dunstan Adams, May & Story	2	1	--	3.45	1.72	--
5 Gill & Johnson	20	19	19	34.49	32.76	32.76
6 Kassim - Iakha Abdulla & Co.	1	1	1	1.72	1.72	1.72
7 Murdock, McGrae & Smith	1	1	1	1.72	1.72	1.72
8 Nyagah Associates & Co.	--	1	1	--	1.72	1.72
9 Pannell, Bellhouse, Mwangi & Co.	2	2	2	3.45	3.45	3.45
10 Parry & Co.	1	1	1	1.72	1.72	1.72
11 Price Waterhouse & Co.	--	3	5	--	5.18	8.63
12 Peat, Marwick, Mitchell & Co.	11	11	11	18.97	18.97	18.97
Total number of Companies Audited	58	58	58	100.00	100.00	100.00
Number of Auditing Firms represented	10	12	11			

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