Provision for Depreciation and Disposal of Assets

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2 Depreciation may be thought of as the difference between the cost of an asset and the amount received from it on disposal.

The following extract from the schedule of non-current (fixed) assets applies to the year ended 30 April 2009.

Non-current (fixed) assets	Machinery	Motor vehicles
	$000	$000
Cost at 1 May 2008	4200	3200
Additions during year	1200	800
Disposals during year	(700)	(1000)
Cost at 30 April 2009	4700	3000
Depreciation at 1 May 2008	1560	840
Add charge for year	470	750
Less disposals for year	(520)	(800)
Depreciation at 30 April 2009	1510	790
Net book value at 30 April 2009	3190	2210

During the year ended 30 April 2010 the following took place:

1 New machinery costing $900 000 was purchased on 1 November 2009. Machinery, which had cost $400 000 on 1 July 2005, was sold for $200 000 in December 2009.

2 Three new motor vehicles were purchased on 1 April 2010 for $280 000 **each**. Two motor vehicles, which had been purchased on 1 March 2007, for $200 000 **each**, were taken in part-exchange. The part-exchange allowance for **each** vehicle was $60 000.

3 One vehicle which had been purchased for $360 000 on 31 January 2009 was involved in an accident on 2 December 2009. The insurance company decided that it could not be repaired and gave compensation of $210 000.

Depreciation is charged for the full year on all non-current (fixed) assets held at the year-end, using the straight-line method.

No depreciation is charged on a non-current (fixed) asset in the year of disposal.

Rates of depreciation have remained constant since the business began trading.

REQUIRED

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(a) (i) Calculate the profits or losses on disposals during the year ended 30 April 2010.

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(ii) Prepare a schedule of non-current (fixed) assets for the year ended 30 April 2010, using the layout given at the beginning of the question.

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(b) **(i)** State **three** causes of depreciation.

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(ii) Give an example of a non-current (fixed) asset for which **each** cause given in **(b)(i)** above might be appropriate.

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(c) State **four** factors which must be taken into account when deciding how much depreciation to charge.

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[Total: 30]

2 Amirtha commenced business on 1 January 2010. During the first two years of business the following non-current assets were purchased on the dates shown:

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Motor vehicles

2010		$
1 January	MV1	26 000
1 July	MV2	18 000
2011		
1 April	MV3	24 000

Equipment

2010		
1 January	EQ1	30 000
2011		
1 January	EQ2	44 000

Amirtha has a policy to depreciate motor vehicles at 20% per annum on cost (straight line method) and equipment at 15% per annum on cost (straight line method), rates being charged for each month of ownership.

REQUIRED

(a) Calculate the total depreciation for each of the years 2010 **and** 2011.

(i) Motor vehicles

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(ii) Equipment

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Early in 2012, consideration was given to changing to the reducing (diminishing) balance method, with the following rates applying to the balance at the end of each year.

Motor vehicles	25%
Equipment	20%

A full year's depreciation would be charged irrespective of the date of purchase.

REQUIRED

(b) Calculate the total depreciation for **each** of the years 2010 **and** 2011, using the reducing (diminishing) balance method for:

(i) Motor vehicles

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(ii) Equipment.

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The original profits for the first two years in business were:

2010	$86 000
2011	$94 000

REQUIRED

(c) Prepare a statement to show the revised profits for the years 2010 and 2011, if the reducing (diminishing) balance method had been used.

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(d) Explain why it is appropriate to use the reducing (diminishing) balance method for motor vehicles.

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The following information is also available from the books of Amirtha.

	1 January 2011 $		31 December 2011 $	
Wages	2 040	accrued	2 130	accrued
Insurance	130	accrued	610	prepaid
Rent received	1 490	prepaid	1 320	prepaid

During the year ended 31 December 2011 the following transactions took place.

	$
Wages paid	24 100
Insurance paid	1 400
Rent received	14 000

All transactions are through the bank account.

REQUIRED

(e) Prepare the following ledger accounts for the year ended 31 December 2011, showing the closing entry to the financial statements at the end of the year. Dates are not required.

(i) Wages account

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(ii) Insurance account

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(iii) Rent received account

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[Total: 30]

2 Alex's fixed asset accounts and provision for depreciation on fixed asset accounts for the year ended 30 April 2008 were as follows:

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Furniture and equipment account

		$000			$000
2007			2007		
1 May	Balance b/d	2 700	5 July	Disposal	450
3 June	Bank	720	2008		
			30 April	Balance c/d	2 970
		3 420			3 420
2008					
1 May	Balance b/d	2 970			

Provision for depreciation on furniture and equipment account

		$000			$000
2007			2007		
5 July	Disposal	345	1 May	Balance b/d	945
2008			2008		
30 April	Balance c/d	897	30 April	Profit & loss	297
		1 242			1 242
			1 May	Balance b/d	897

Motor vehicles account

		$000			$000
2007			2007		
1 May	Balance b/d	1 560	3 Oct	Disposal	330
3 Oct	Bank	570	2008		
			30 April	Balance c/d	1 800
		2 130			2 130
2008					
1 May	Balance b/d	1 800			

Provision for depreciation on motor vehicles account

		$000			$000
2007			2007		
3 Oct	Disposal	285	1 May	Balance b/d	675
2008			2008		
30 April	Balance c/d	840	30 April	Profit & loss	450
		1 125			1 125
			1 May	Balance b/d	840

ALTERNATIVE PRESENTATION USING RUNNING BALANCE

Furniture and equipment account

		Dr	Cr	Balance
2007		$000	$000	$000
1 May	Balance b/d			2 700 Dr
3 June	Bank	720		3 420
5 July	Disposal		450	2 970

Provision for depreciation on furniture and equipment account

		Dr	Cr	Balance
2007		$000	$000	$000
1 May	Balance b/d			945 Cr
5 July	Disposal	345		600
2008				
30 April	Profit and loss		297	897

Motor vehicles account

		Dr	Cr	Balance
2007		$000	$000	$000
1 May	Balance b/d			1 560 Dr
3 Oct	Disposal		330	1 230
	Bank	570		1 800

Provision for depreciation on motor vehicles account

		Dr	Cr	Balance
2007		$000	$000	$000
1 May	Balance b/d			675 Cr
3 Oct	Disposal	285		390
2008				
30 Apr	Profit and loss		450	840

During the year ended 30 April 2009 the following transactions took place:

1 On 1 June 2008 new equipment was purchased for $540 000.
On 3 December 2008 new furniture was purchased for $80 000.
On 3 September 2008 equipment which had been purchased on 31 March 2006 for $300 000 was sold for $132 000.

2 On 1 February 2009 three new motor vehicles were purchased for $80 000 each. On the same date a vehicle which had cost $56 000 on 15 May 2005 was sold for $20 000.

A full year's depreciation is provided for on all fixed assets in use at the end of the financial year but none is provided for in the year of disposal of a fixed asset.

The rates of depreciation applied on cost for the year ended 30 April 2008 continue to be applied for the year ended 30 April 2009.

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REQUIRED

(a) Prepare the following accounts for the year ended 30 April 2009:

(i) Furniture and equipment

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(ii) Motor vehicles

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(iii) Provision for depreciation on furniture and equipment

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(iv) Provision for depreciation on motor vehicles

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(v) Disposal of furniture and equipment

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(vi) Disposal of motor vehicles.

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(b) Explain the term 'depreciation' and give **one** example.

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[Total: 30]

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2 Answer Sections **A** and **B**.

A Sarah runs a wholesale business. An extract from her statement of financial position (balance sheet) at 31 December 2009 shows:

Motor vehicles at cost	$371 000
Motor vehicle accumulated depreciation	$130 000

During the financial year ended 31 December 2010 the following transactions took place.

1 A motor vehicle purchased on 1 January 2006 for $9200 was sold on 30 June 2010 for $500.

2 A motor vehicle was purchased on 1 April 2010 for $15 000.

Depreciation is charged at 20% per annum on cost, with the rate being applied for each part of the year. No allowance is made for any residual value.

All motor vehicles held by the company at 31 December 2010 had been purchased within the previous five years.

All transactions are by cheque.

REQUIRED

(a) Prepare the following ledger accounts for the year ended 31 December 2010.

(i) Motor vehicles account

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(ii) Provision for depreciation of motor vehicles account

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(iii) Motor vehicle disposal account

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(b) Prepare an extract from the statement of financial position (balance sheet) for non-current assets at 31 December 2010.

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(c) Explain why businesses provide for depreciation on their non-current assets.

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B The treasurer of Hamilton Social Club has provided the following information for the year ended 31 March 2011.

	31 March 2010	31 March 2011
	$	$
Café inventory at cost	3400	3950
Café trade payables	1570	880
Subscriptions in arrears	240	120
Equipment (net book value)	5400	9360
Stock of stationery at cost	110	85
Cash at bank	1800	340
5% loan (repayable 2015)	–	5000

Equipment costing $5000 was purchased on 1 April 2010. It was financed by the 5% loan. At the year end 31 March 2011, no payment of interest had been made.

Included in the café inventory at 31 March 2011 were items costing $120 that were out of date. They had a net realisable value of $30.

REQUIRED

(a) Prepare a statement of financial position (balance sheet) for Hamilton Social Club at 31 March 2011. Show clearly the surplus or deficit for the year. An income and expenditure account is **not** required.

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[Total: 30]