

Task IM-7.25: Exercise on Disposals

(Impairment Loss)

MARIANDAH L Ltd. is an Australian tool rental shop. On 4.05.20X4, MARIANDAH L Ltd. buys 5 rotary power hammers at 1,000.00 AUD/u cost of acquisition. The rotary hammers are depreciated by declining method at 1.2 %/m.

On 2.10.20X4, one of the rotary hammers is damaged by a customer and needs repair. The repair costs are 200.00 AUD but the value of the rotary hammer drops to 600.00 AUD. Depreciation is resumed in October (for October).

On 30.06.20X6, MARIANDAH L Ltd. sells all 5 rotary hammers together at a gross selling price of 4,500.00 AUD.

Required: Determine the profit on disposal. It is recommended to disclose real accounts for earning marks in case your solution is partly faulty.

Solution:

(1) Acquisition (4+1) in order to prepare separate accounts.

DR P, P, E Rotary-4	4,000.00 AUD
DR P, P, E Rotary-1	1,000.00 AUD
DR VAT	1,000.00 AUD
CR Cash/Bank	6,000.00 AUD

(2) Depreciation on 4 Rotary hammers: Depr. costs are: $(4,000 - (4,000 \times (1 - 1.2\%)^8)) = 368.25 \text{ AUD}$.

DR Depreciation	368.25 AUD
CR Acc. Depr. Rotary-4	368.25 AUD

(3) Depreciation of the damaged rotary hammer before damage. Depreciation expenses are amounting to: $1,000 - (1,000 \times (1 - 1.2\%)^5) = 58.58 \text{ AUD}$.

DR Depreciation	58.58 AUD
CR Acc Depr. Rotary-1	58.58 AUD

(4) Repair of the rotary hammer:

DR Repair	200.00 AUD
DR VAT	40.00 AUD
CR Cash/Bank	240.00 AUD

(5) The impairment loss is amounting to $1,000 \times (1 - 1.2\%)^5 - 600 = 341.42 \text{ AUD}$.

DR Impairment Loss-20X4	341.42 AUD
CR Acc Depr Rotary-1	341.42 AUD

(6) Depreciation is resumed in October. The amount is $600 - (600 \times (1 - 1.2\%)^3) = 21.34 \text{ AUD}$.

DR Depreciation-20X4	21.34 AUD
CR Acc Depr Rotary-1	21.34 AUD

(A, B) In the next Accounting period, the rotary hammers are depreciated. The 4 rotary hammers are carried at the beginning of the Accounting period at: $4,000 - 368.25 = 3,631.75 \text{ AUD}$. The repaired rotary hammer is worth: $1,000 - 421.34 = 578.66 \text{ AUD}$. Depreciation for the 4 rotary hammers is amounting to $3,631.75 - (3,631.75 \times (1 - 1.2\%)^{12}) = 489.80 \text{ AUD}$. Depreciation on the single rotary hammer is: $578.66 - (578.66 \times (1 - 1.2\%)^{12}) = 78.04 \text{ AUD}$.

DR Depreciation-20X5	489.80 AUD
CR Acc Depr Rotary-4	489.80 AUD

DR Depreciation-20X5	78.04 AUD
CR Acc Depr Rotary-1	78.04 AUD

(C) MARIANDAHLLtd. receives an input VAT refund from last year's expenditures.

DR Cash/Bank	1,040.00 AUD
CR VAT	1,040.00 AUD

(a, b) In the next Accounting period, the rotary hammers are depreciated. The 4 rotary hammers are carried at the beginning of the Accounting period at: $4,000 - 858.05 = 3,141.95 \text{ AUD}$. The repaired rotary hammer is worth: $1,000 - 499.38 =$

500.62 AUD. Depreciation for the 4 rotary hammers is amounting to $3,141.95 - (3,141.95 \times (1 - 1.2\%)^6) = \mathbf{219.54 \text{ AUD}}$. Depreciation on the single rotary hammer is: $500.62 - (500.62 \times (1 - 1.2\%)^6) = \mathbf{34.98 \text{ AUD}}$.

DR Depreciation-20X6	219.54 AUD
CR Acc Depr Rotary-4	219.54 AUD

DR Depreciation-20X6	34.98 AUD
CR Acc Depr Rotary-1	34.98 AUD

The rotary hammers are sold on 30.06.20X6. MARIANDAHN Ltd. applies the Realisation Account (REA):

DR Cash/Bank	4,500.00 AUD
CR Realisation	4,500.00 AUD

DR Realisation	750.00 AUD
CR VAT	750.00 AUD

DR Realisation	5,000.00 AUD
CR P, P, E Rotary-4	4,000.00 AUD
CR P, P, E Rotary-1	1,000.00 AUD

DR Acc Depr Rotary-4	1,077.59 AUD
CR Realisation	1,077.59 AUD

DR Acc Depr Rotary-1	534.36 AUD
CR Realisation	534.36 AUD

From the Realisation account we read out a profit on disposal amounting 361.95 AUD.

Find below the accounts in Figure 1:

D P, P, E Rotary-4 PP4 C				D P, P, E Rotary-1 PP1 C			
(1)	4,000.00	c/d	4,000.00	(1)	1,000.00	c/d	1,000.00
b/d	4,000.00	REA	4,000.00	b/d	1,000.00	REA	1,000.00

D Acc depr Rotary-4 AC4 C				D Acc depr/IL Rotary-1 AC1 C			
c/d	368.25	(2)	368.25			(3)	58.58
		b/d	368.25			(5)	341.42
c/d	858.05	(A)	489.80	c/d	421.34	(6)	21.34
	858.05		858.05		421.34		421.34
		b/d	858.05			b/d	421.34
REA	1,077.59	(a)	219.54	c/d	499.38	(B)	78.04
	1,077.59		1,077.59		499.38		499.38
						b/d	499.38
				REA	534.36	(b)	34.98
					534.36		534.36

D Depreciation-20X4 C				D Cash/Bank C/B C			
(2)	368.25					(1)	6,000.00
(3)	58.58			c/d	6,240.00	(4)	240.00
(6)	21.34	P4L	448.17		6,240.00		6,240.00
	448.17		448.17	(C)	1,040.00	b/d	6,240.00
				c/d	5,200.00		
					6,240.00		6,240.00
				REA	4,500.00	b/d	5,200.00

D Value added tax VAT C				D Repair-20X4 REP C			
(1)	1,000.00			(4)	200.00	P4L	200.00
(4)	40.00	c/d	1,040.00				
	1,040.00		1,040.00				
b/d	1,040.00	(C)	1,040.00				
c/d	750.00	REA	750.00				
		b/d	750.00				

Figure 1: Accounts

D		Impairment loss-20X4		C	D		Depreciation-20X5		C
(5)	341.42	P4L	341.42		(A)	489.80			
					(B)	78.04	c/d	567.84	
						567.84		567.84	
					b/d	567.84	P5L	567.84	

D		Depreciation-20X6		C	D		Realisation		C
(a)	219.54				VAT	750.00	C/B	4,500.00	
(b)	34.98	P6L	254.52		PPE	5,000.00	AC4	1,077.59	
	254.52		254.52		PoD	361.95	AC1	534.36	
						6,111.95		6,111.95	

Figure 1: Accounts - continued