

Task 7.63: Exercise on Revaluations and Disposal (Leasing)

BILK Pty Ltd. enters in a lease with HAYES Ltd. about a production machine. BILK (Pty) Ltd. agrees to pay an initial amount at the commencement of the lease (1.10.20X4) 12,000 EUR. It further pays every monthend 1,000 EUR for the 1st year thereafter the lease escalates on October 1st by 5%. The lease term ends after 2 years. BILK (Pty) Ltd.'s incremental borrowing rate is 7.5%. For the general approach, assume there is a bulk payment at the end of each year but the initial payment takes place at the beginning of 20X4. (This gives you 4 payments: beginning 20X4: initial payment, end 20X4 rates, end 20X5 rates, end 20X6 rates)

Required: Record the lease in 20X4 ... 20X6 if BILK (Pty) Ltd. applies (A) the simplified approach and if it follows the (B) general approach. Disclose relevant balancing figures on BILK (Pty) Ltd.'s balance sheet incl. retained earnings. (for this task you are allowed to disclose a negative balancing figure on the balance sheet for the cash/bank item.) For the general approach you can discount figures accurate to the year, meaning you pretend the payment take place at the end of the year. Place the initial payment at the beginning of 20X4 accordingly.

Solution:

Find below the accounts and financial statements of BILK (Pty) Ltd.

Cash/Bank C/B			Lease expenses-20X4			Lease expenses-20X5		
D		C	D		C	D		C
c/d	15,000	(1)	15,000	(1)	4,650	(A)	18,600	P5L
		b/d	15,000					
c/d	27,300	(A)	12,300					
	27,300		27,300					
		b/d	27,300					
c/d	37,200	(a)	9,900					
	37,200		37,200					
		b/d	37,200					
Lease expenses-20X6			Prepaid expenses PRE					
D		C	D		C			
(a)	13,950	P6L	(1)	10,350	c/d	10,350		
			b/d	10,350	(A)	6,300		
					c/d	4,050		
					10,350	10,350		
			b/d	4,050	(a)	4,050		

Exhibit 1: Accounts for simplified approach

D Cash/Bank C/B C		D Right of Use Asset RuA C		D Lease liability L/L C	
	(1) 12,000	(1) 12,000		(4) 3,000	(2) 21,403
c/d 15,000	(4) 3,000	(2) 21,403		c/d 20,009	(3) 1,605
15,000	15,000	33,403		23,009	23,009
	b/d 15,000			(C) 12,300	b/d 20,009
c/d 27,300	(C) 12,300			c/d 9,209	(B) 1,501
27,300	27,300			21,509	21,509
	b/d 27,300			(c) 9,900	b/d 9,209
c/d 37,200	(c) 9,900			9,900	(b) 691
37,200	37,200			9,900	9,900
	b/d 37,200				
D Depreciation-20X4 C		D Depreciation-20X5 C		D Depreciation-20X6 C	
(3) 4,175	P4L	(A) 16,702	P5L	(a) 12,526	P6L
D Accumulated depreciation C		D Interest-20X4 C		D Interest-20X5 C	
c/d 4,175	(3) 4,175	(3) 1,605	P4L	(B) 1,501	P5L
	b/d 4,175				
c/d 20,877	(A) 16,702				
20,877	20,877				
	b/d 20,877				
c/d 33,403	(a) 12,526				
33,403	33,403				
	b/d 33,403				
D Interest-20X6 C					
691	P6L				

Exhibit 2: Accounts for general approach

Balance sheet	20X4	20X5	20X6
P, P, E			
Intangibles			
Financial assets			
Inventory			
Accounts receivables			
Prepaid expenses	10,350.00	4,050.00	0.00
Cash/Bank	(15,000.00)	(27,300.00)	(37,200.00)
Total assets	(4,650.00)	(23,250.00)	(37,200.00)
Share capital			
Reserves			
Retained earnings	(4,650.00)	(23,250.00)	(37,200.00)
Interest bear liab			
Accounts payables			
Provisions			
Tax liabilities			
Total equity and liab.	(4,650.00)	(23,250.00)	(37,200.00)

Exhibit 3: Simplified Approach

Balance sheet	20X4	20X5	20X6
P, P, E			
Intangibles	29,227.97	12,526.27	0.00
Financial assets			
Inventory			
Accounts receivables			
Prepaid expenses			
Cash/Bank	(15,000.00)	(27,300.00)	(37,200.00)
Total assets	14,227.97	(14,773.73)	(37,200.00)
Share capital			
Reserves			
Retained earnings	(5,780.68)	(23,983.03)	(37,200.00)
Interest bear liab	20,008.65	9,209.30	0.00
Accounts payables			
Provisions			
Tax liabilities			
Total equity and liab.	14,227.97	(14,773.73)	(37,200.00)

Exhibit 4: General approach