CHAPTER 21

Non-current assets: Revaluation, disposal and other aspects

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ADDITIONAL PROBLEMS

Problem 21.1 Non-current asset disposals

During the year ended 31 December 2003, Modest Ltd disposed of four different non-current assets. On 1 January 2003 the accounts showed the following:

Asset	Cost	Residual value	Estimated life	Accumulated depreciation
Truck No. 2	$ 42 000	$ 6 000	5 years	$21 600
Truck No. 5	36 000	4 000	4 years	24 000
Machine B	114 000	14 000	5 years	60 000
Machine C	64 000	4 000	15 years	42 000

Modest Ltd depreciates its trucks and machines by the straight-line method and records depreciation to the nearest whole month. Assets were disposed of as follows:

Truck No. 5, which was not insured, was completely destroyed by fire on 6 January 2003. A towing company was paid $1120 to remove the truck and to clean up any debris.

Truck No. 2 was traded in on a new truck on 3 July 2003. Trade-in allowance was $20 000. The old truck plus cash of $42 000 were given in exchange.

Machine B was sold for $44 000 cash on 1 October 2003.

Machine C was traded in on a new machine on 22 December 2003. The old machine plus cash of $62 500 were given in exchange. Trade-in allowance was $18 000.

Required:

Prepare journal entries needed to account for the above transactions.

Solution

MODEST LTD

2003				
Jan.	6	Accum. Depreciation - Trucks	24 000	
		Fire Loss	13 120	
		Trucks		36 000
		Cash at Bank		1 120
		To dispose of Truck No. 5.		
July	3	Depreciation Expense - Trucks	3 600	
		Accum. Depreciation - Trucks		3 600
		To record depreciation on trucks.		
		(42 000 − 6000)/5 years = \$7 200 × 6/12)		
	3	Trucks	62 000	
		Cash at Bank		42 000
		Proceeds from Sale of Trucks		20 000
		To exchange trucks.		
	3	Carrying Amount of Trucks Sold	16 800	
		Accum. Depr. - Trucks	25 200	
		Trucks		42 000
		To write off truck traded in.		
Oct.	1	Depreciation Expense - Machinery	5 000	
		Accum. Depreciation - Machinery		15 000
		To record depn. on machine sold.		
		(114 000 − 14 000)/5 years = 20 000 × 9/12)		
	1	Cash at Bank	44 000	
		Proceeds from Sale of Machinery		44 000
		To record sale of machine A.		
	1	Carrying Amount of Machinery Sold	39 000	
		Accum. Depr. - Machinery		75 000
		Machinery		114 000
		To write off machine A.		
Dec.	22	Depreciation Expense - Machinery	4 000	
		Accum. Depreciation - Machinery		4 000
		To record depreciation on machine sold.		
	22	Machinery	80 500	
		Cash at Bank		62 500
		Proceeds from Sale of Machinery		18 000
		To exchange machines.		
	22	Carrying Amount of Machinery Sold	18 000	
		Accum. Depr. - Machinery	46 000	
		Machinery		64 000
		To write off machine traded in.		

Problem 21.2 Revaluation and disposal

Below are extracts from the financial reports of Tuart Hill Traders for the years ended 30 June 2001 and 30 June 2002.

TUART HILL TRADERS
Statement of Financial Position (extract)
as at 30 June 2001

NON-CURRENT ASSETS			
Land		$720 000	
Building	$450 000		
Less: Accum. depreciation	120 000	330 000	
TOTAL NON-CURRENT ASSETS			$1 050 000
OWNERS' EQUITY			
Asset revaluation reserve		180 000	
Capital at 1 July 2000	140 000		
Add: Net profit for year	37 000		
Capital at 30 June 2001		177 000	
TOTAL OWNERS' EQUITY			$ 357 000

TUART HILL TRADERS
Statement of Financial Position (extract)
as at 30 June 2002

NON-CURRENT ASSETS			
Land		$630 000	
Building		280 000	
TOTAL NON-CURRENT ASSETS			$910 000
OWNERS' EQUITY			
Asset revaluation reserve		90 000	
Capital at 1 July 2001	$177 000		
Add: Net profit for year	20 000		
Capital at 30 June 2002		197 000	
TOTAL OWNERS' EQUITY			$287 000

TUART HILL TRADERS
Statement of Financial Performance (extract)
for the year ended 30 June 2002

OPERATING EXPENSES	
Supplies expense	$ 3 000
Wages expense	36 540
Depreciation expense—building	30 000
Bad debts expense	8 200
Insurance expense	15 160
Expense on revaluation of building	20 000
Total expenses	$ 112 900

(continued)

Additional information

1. The asset revaluation reserve at 30 June 2001 was raised entirely as the result of a prior revaluation increment in relation to the land.
2. No land or buildings were acquired or disposed of during the year ended 30 June 2002.
3. A revaluation of the land and buildings was carried out on 30 June 2002 after all adjusting entries had been entered and posted. The revaluation adjustment was entered into the accounts on 30 June 2002, and the balance sheet at that date reflects the recoverable amounts in accordance with the revaluation.
4. After the revaluation, the building was reassessed to have a residual value of \$40 000 and a remaining useful life of 15 years. The building is to be depreciated using the straight-line method of depreciation.
5. The land and buildings were sold on 31 December 2002. A lump sum of \$850 000 was received. The proceeds were allocated to the land and buildings at \$600 000 and \$250 000 respectively.

Required:

A. Calculate the balance of the Accumulated Depreciation—Building account immediately prior to the revaluation on 30 June 2002.

B. Prepare the general journal entries to record:
   1. the revaluation of the building on 30 June 2002
   2. the revaluation of the land on 30 June 2002
   3. the disposal of the land on 31 December 2002
   4. the disposal of the building on 31 December 2002.

Solution

A.

TUART HILL TRADERS

Accumulated depreciation - building at 30/6/01	\$120 000
Add: Depreciation charge for year ended 30/6/02	30 000
Accumulated depreciation - building at 30/6/02	150 000

B. 2002

1. June 30	Accumulated Depreciation - Building	150 000	
	Building		150 000
	To write back accum. depreciation.		
	Loss on Revaluation of Building	20 000	
	Building (450 – 150)	280 000	20 000
	To recognise revaluation decrement.		
2.	Asset Revaluation Reserve	90 000	
	Land 720 - 630		90 000
	To recognise revaluation decrement after a previous increment.		
3.	Cash at Bank	600 000	
	Proceeds on Sale of Land		600 000
	To record sale of land.		
	Carrying Amount of Land Sold	630 000	
	Land		630 000
	To write off land sold.		
4.	Depreciation Expense - Building	8 000	
	Accum. Depreciation - Building		8 000
	To record depreciation for six months.		
	Cash at Bank	250 000	
	Proceeds on Sale of Building		250 000
	To record sale of building.		
	Accum. Depreciation - Building	8 000	
	Carrying Amount of Building Sold	232 000	
	Building		240 000
	To write off building sold.		

WILEY

Problem 21.3 Intangibles and natural resources

The following transactions and events affected the accounts of Fine Ltd for the current year:

1. A patent with an estimated life of 10 years was purchased for cash of $840 000 on 3 January last year.
2. On 8 January of the current year, Fine Ltd paid $44 000 in legal fees for the successful defence of a patent infringement suit against the patent purchased in (1) above.
3. On 10 January of the current year, Fine Ltd signed a contract to lease a small warehouse from Clean Ltd. The lease is for 5 years and required an advance payment of $210 000 plus a $90 000 cash payment at the end of each year.
4. On 31 January, a valuable copyright held by the company was valued independently at $70 000. $35 000 of this had been previously included in the asset 'Research and Development'. It is expected that the copyright has a future useful life of 6 years.
5. On 6 February of the current year, Fine Ltd purchased a coal mine for $11 500 000. Of the total purchase price, $9 900 000 was assigned to the coal mine and the remaining $1 600 000 was assigned to mining machinery. The mine has a residual value of $1 500 000 and contains an estimated 20 000 000 tonnes of coal. The mining machinery is expected to be useful for the entire life of the mine and will be abandoned when the coal deposits are depleted. During the current year, 3 000 000 tonnes of coal were mined.
6. Improvements were made to the leased warehouse [(3) above] on 30 June of the current year at a cost of $45 000. The estimated life of the improvements is 8 years.

Required:

A. Prepare journal entries to record the events occurring in the current year.
B. Prepare journal entries to record amortisation and depreciation for the current year. Record to the nearest whole month.

(*continued*)

Solution

FINE LTD

A.	Jan.	8	Patents	44 000	
			Cash at Bank		44 000
			For legal costs of defending patent.		
		10	Prepaid Rent under Lease	210 000	
			Cash at Bank		210 000
			To record lease of warehouse.		
		31	Copyright	70 000	
			Research and Development Costs		35 000
			Asset Revaluation Reserve		35 000
			To revalue patent (ED 49 treatment).		
	Feb.	6	Coal Deposits	9 900 000	
			Mining Machinery	1 600 000	
			Cash at Bank		11 500 000
			To acquire coal mine and machinery.		
	June	30	Leasehold Improvements	45 000	
			Cash at Bank		45 000
			To record improvements to warehouse.		
B.	Dec.	31	Amortisation Expense on Patents	88 889	
			Accum. Amortisation - Patents		88 889
			To amortise patent.		
			Initial patent cost		$840 000
			Less: Amortisation for last year		84 000
			Carrying amount on 1/1 of current year		756 000
			Add: 8 January payment		44 000
					800 000
			Remaining life		9 years
			Amortisation expense		$88 889
			Amortisation Expense - Copyright		10 694
			Accum. Amort. Copyright		10 694
			To amortise copyright.		
			($60 000/5 for 11 months from 31/1)		
		31	Amortisation Expense - Coal Deposits	1 260 000	
			Accum. Amort. - Coal Deposits		1 260 000
			To amortise coal deposits.		
			($9 900 000 − $1 500 000 = $8 400 000 ÷ 20 000 000 = $0.42 × 3 000 000)		
		31	Deprec. Exp. - Mining Machinery	240 000	
			Accum. Depr. - Mining Machinery		240 000
			To depreciate mine machinery.		
			($1 600 000 ÷ 20 000 000 tonnes = $0.08 × 3 000 000)		
		31`	Rent Expense	132 000	
			Prepaid Rent under Lease*	42 000	
			Cash at Bank		90 000
			To record rent expense and annual payment.		
			*$210 000/5 years		
		31	Amortisation Expense	2 625	
			Accum. Amort. - Leasehold Imp.		2 625
			To amortise leasehold improvements.		
			($42 000 /8 years × 6/12)		

Problem 21.4 Goodwill and discount on acquisition

Fast Ltd acquired the net assets of Slow Ltd and Stop Ltd on 30 June 2003. At that date, the carrying amounts and fair values of the identifiable net assets of Slow Ltd and Stop Ltd were as follows:

	Slow Ltd		Stop Ltd	
	Carrying amount	Fair value	Carrying amount	Fair value
Cash at bank	$30 000	$30 000	$15 000	$15 000
Inventory	17 000	19 000	10 000	11 000
Non-current assets	29 000	26 000	13 000	9 000
Liabilities	(7 000)	(7 000)	(4 000)	(4 000)
	$69 000	$68 000	$34 000	$31 000

Purchase prices paid by Fast Ltd were:
(a) for the net assets of Slow Ltd, $72 000 cash.
(b) for the net assets of Stop Ltd, $28 000 cash.

Required:
Prepare journal entries in the books of Fast Ltd to acquire the net assets of Slow Ltd and Stop Ltd.

Solution

FAST LTD

Cash at Bank	30 000	
Inventory	19 000	
Non-Current Assets	26 000	
Goodwill	4 000	
Liabilities		7 000
Vendor - Slow Ltd		72 000
To acquire net assets of Slow Ltd.		
Vendor - Slow Ltd.	72 000	
Cash at Bank		72 000
To pay vendor.		
Cash at Bank	15 000	
Inventory	9 350	
Non-Current Assets	7 650	
Liabilities		4 000
Vendor - Stop Ltd		28 000
To acquire net assets of Stop Ltd.		

Discount on acquisition = $35 000 – $32 000 = $3 000
Allocation of discount over non-monetary assets:

Asset	Fair value	Ratio	Discount allocation	Cost of acquisition
Inventory	$ 11 000	11/20	$1 650	$9 350
Non-current assets	9 000	9/20	1 350	7 650
	$20 000		$3 000	$17 000

Vendor - Stop Ltd	28 000	
Cash at Bank		28 000
To pay vendor		

Problem 21.5 Review question

The trial balance of Mercury Distributors is shown below. The trial balance shows the balances in the ledger accounts at 31 December 2003. However, due to a small fire at the business, certain accounting records were damaged and hence some ledger balances could not be finalised and have been left blank.

MERCURY DISTRIBUTORS
Trial Balance
as at 31 December 2003

Account	Debit	Credit
Cash at bank	$ 16 400	
Accounts receivable	26 500	
Inventory (1 January 2003)	70 000	
Prepaid insurance	3 600	
Office supplies	2 400	
Furniture and fittings	14 000	
Accumulated depreciation—furniture and fittings		$ 5 400
Delivery equipment	40 000	
Accumulated depreciation—delivery equipment		
Land	230 000	
Accounts payable		34 700
Loan payable ($2000 payable before 31 December 2004)		15 000
Capital, F. Misiti (1 January 2003)		
Drawings, F. Misiti		
Asset revaluation reserve		
Sales revenue		
Revenue/expense on revaluation		
Discounts received		8 200
Purchases	395 000	
Purchases returns and allowances		1 600
Discounts allowed	4 200	
Freight inwards	17 400	
Sales salaries expense	54 000	
Delivery expense	18 400	
Advertising expense	13 100	
Rent expense	15 000	
Office salaries expense	36 000	
Insurance expense	2 050	
Depreciation expense—delivery equipment	1 250	
Depreciation expense—furniture and fittings	1 000	
Totals		

(continued)

Additional information

1. All goods are sold at prices calculated at 1.5 times the 'cost of goods sold'.
2. (a)Current assets at 31 December 2002 were $130 000.
   (a) Current liabilities at 31 December 2002 were $115 150.
   (b) Non-current assets at 31 December 2002 were $290 000.
   (c) Non-current liabilities at 31 December 2002 were $14 000.
   (d) Asset revaluation reserve at 31 December 2002 was $100 000.
3. A revaluation increment of $100 000 had been recorded in 2000 in relation to the land. On 30 June 2003 a revaluation decrement of $20 000 was recorded in relation to the land.
4. The delivery equipment had been revalued downwards initially by $7000 in 2000 and was revalued upwards on 30 September 2003 by $15 000. Immediately prior to the upward revaluation, the delivery equipment was recorded in the accounts at $35 000 and the accumulated depreciation on the delivery equipment (to the date of the revaluation) was $10 000.

   After the upward revaluation, the remaining estimated useful life was reassessed to be 12 years (from the date of the revaluation) with an expected residual value of $10 000. The delivery equipment was depreciated using the reducing-balance method (rate = 12.5% p.a.).
5. Other than those revaluations described in (3) and (4) above, no other revaluations have taken place during the life of the business.
6. Ending inventory at cost on 31 December 2003 is $68 800.

Required:

Use the additional information to calculate the following amounts in the 31 December 2003 trial balance of Mercury Distributors, i.e.:

1. sales revenue
2. asset revaluation reserve
3. revenue/expense on revaluation
4. accumulated depreciation—delivery equipment
5. Capital, F. Misiti (1 January 2003)
6. trial balance column totals
7. Drawings, F. Misiti.

(*Hint:* You will find it useful to calculate the missing amounts in the above order.)

Solution

MERCURY DISTRIBUTORS

1. Cost of goods sold:

Beginning inventory		$70 000
Purchases	395 000	
Less: Purchase returns and allowances	1 600	393 400
Freight In		17 400
		480 800
Less: Ending inventory		68 800
Cost of goods sold		412 000

Therefore Sales revenue = $412 000 × 1.5 = $618 000

2.

Asset Revaluation Reserve

			1900	Land	100 000
30/6/03	Land*	20 000			
	Balance c/d	88 000	30/9/03	Delivery equip.**	8 000
		108 000			108 000
			31/12/03	Balance b/d	88 000

* Reversal of previous increment

** Increment over and above previous $7 000 revaluation decrement.

3. Reversal of previous decrement ($7 000) goes to profit. Therefore the gain on revaluation is $7 000. Note that the additional $8 000 on revaluation of the delivery equipment goes to the asset revaluation reserve.

4. Accumulated depreciation was written off against the asset account on 30 September 1903 i.e. at the time of the revaluation and will only show depreciation since that date.

Carrying amount at date of revaluation (30/9/03)	= $35 000 − 10 000
	= 25 000
Add: Revaluation increment of $15 000	= 40 000
Depreciation = 40 000 × 12.5% × 3/12	= $1 250

5. Beginning capital balance can be found by working from 2002 data:

Current assets (31/12/02)	130 000
Non-current assets	290 000
Current liabilities	(115 150)
Non-current liabilities	(14 000)
Asset revaluation reserve	(100 000)
Capital at 31/12/02 (Capital at 1/1/03)	$190 850

6. You are now in a position to add up the credit column of the trial balance as all credit information is now available.

Credit column total	= $970 000
Hence debit total is also	$970 000

7. If the debit column total is $970 000 then working backwards the drawings balance for F Misiti must be $9 700. (It is the only debit missing.)