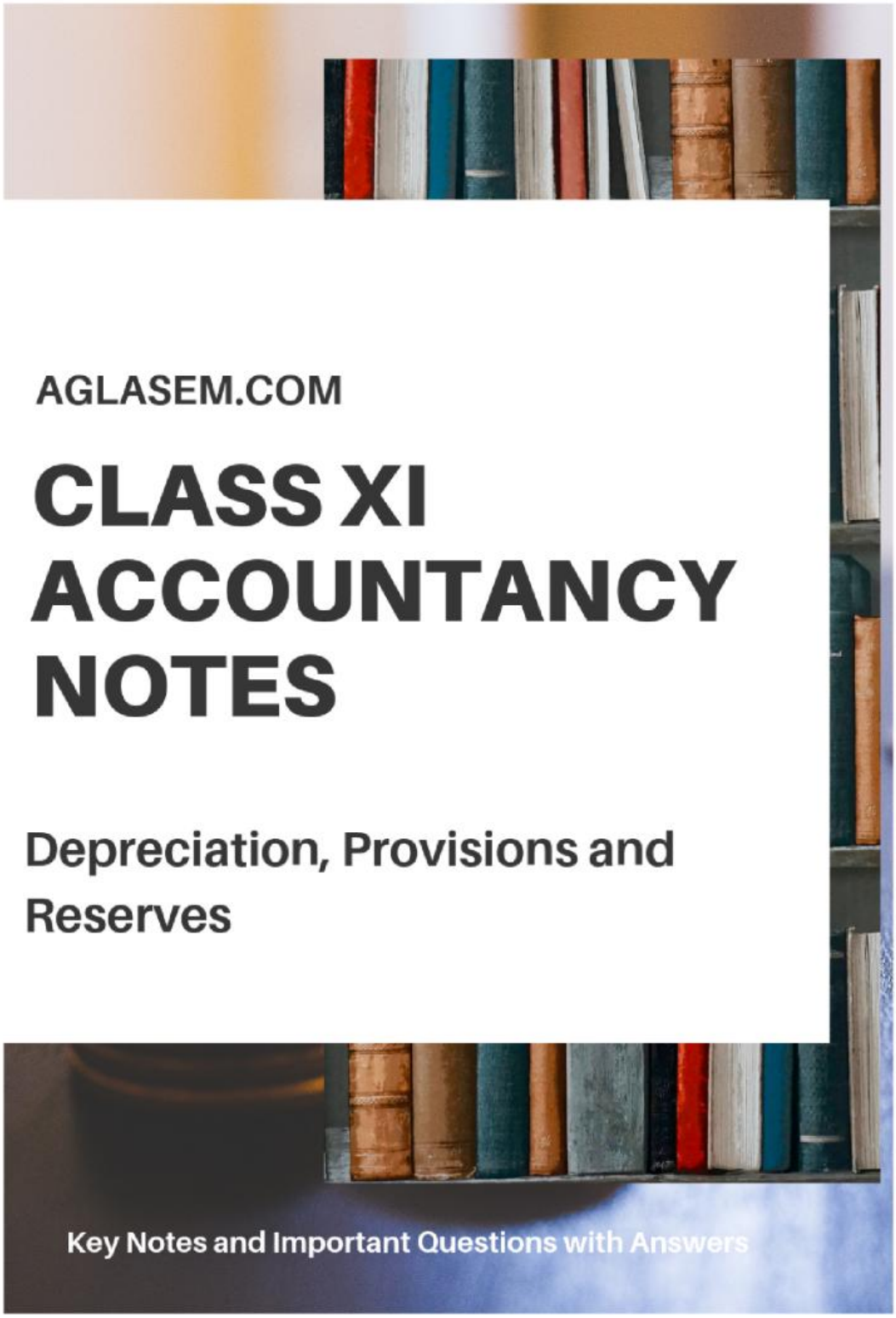


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CLASS XI ACCOUNTANCY NOTES

Depreciation, Provisions and Reserves

Key Notes and Important Questions with Answers

CHAPTER-6

DEPRECIATION, PROVISIONS AND RESERVES

LEARNING OBJECTIVES

After studying this lesson you will be able to:

- State the meaning and concept of depreciation.
- Explain the need and factors affecting depreciation.
- Explain the methods of charging depreciation.
- Show the Accounting Treatment of Depreciation.
- State the meaning of Provisions and Reserve
- Differentiate between Provision and Reserve.

Teaching Methods

Teachers are advised to use various examples from daily life in order to clear the concept of depreciation.

Depreciation : Concept

Fixed assets are held on a long term basis and used to generate periodic revenue. That portion of assets, which is believed to have been consumed or expired to earn the revenue, needs to be charged as cost. Such an appropriate proportion of the cost of fixed assets is called Depreciation.

Business enterprises require fixed assets for their business operations such as furniture and fixtures, office equipments. plant and machinery, motor vehicles. land and building etc. In the process of converting **Raw material into finished products, the fixed assets depreciate in value over a period of time, i.e. its useful life.**

In other words, the process of allocation of the cost of a fixed asset over its useful life is known as depreciation.

According to accounting standard - 6 (Revised) issued by the ICA "Depreciation is a measure of wearing out, consumption or other loss of value of a depreciable asset arising from use, effusion of time or obsolescence through technology and market changes. Depreciation is allocated so as to charge a fair proportion of the

depreciable in each accounting period-during the expected useful life of the asset. Depreciation includes amortization of assets whose useful life is predetermined.

Some Important Terms

1. **Obsolescence :-** When a fixed tangible assets become useless or unwanted due to new invention.
2. **Amortization :-** The term amortization is used for writing off intangible assets such as goodwill, copyright, patents, etc.
3. **Depletion :-** The term depletion is used in relation to decreasing the value of wasting assets or natural resources such as mines, oil wells, timber trees & fishing etc. due to the continue removal or extraction of things.

Need or objectives of providing Depreciation

1. **Ascertaining true profit or loss :**

(i) The true profit of an enterprise can be ascertained when all cost; incurred for the purpose of earning revenues have been debited to the profit and loss account.

(ii) Fall in the value of assets used in business operations is a part of the cost and should be shown in the profit and loss account of concerned accounting period.

(iii) Keeping this in view, depreciation must be debited to profit & loss account, since loss in value of fixed assets is also an expenses like other expenses.

2. **Presentation of True and Fair value of assets :** If depreciation is not provided, the value of assets shown in Balance sheet will not present the true and fair value of assets because assets are shown at the cost price but actual value is less than cost price of the assets.

3. **To ascertain the accurate cost of the Production :** Depreciation is an item of expense, the correct cost of production cannot be calculated unless it is also taken into consideration. Hence, depreciation must be provided to ascertain the correct cost of production.

4. **Computation of correct income tax:**

(i) Income tax of an enterprise is determined after charging all the costs of production.

(ii) If depreciation is not charged, the profits will be higher and the income tax will also be higher.

(iii) If depreciation is charged, Tax liability is reduced.

5. **Provision of funds and replacement of assets:** Depreciation is a non cash expense. So that amount of depreciation charged to profit and loss accounts is retained in business every year. These funds are available for replacement of the assets when its useful life is over.

Methods of providing depreciation

1. **Straight line method**

(i) This method is also known as 'original cost method'

(ii) Under this method, depreciation is charged at fixed percentage on the original cost of the asset, throughout its estimated life.

(iii) Under this method, the amount of depreciation is uniform from year to year. That is why this method is also known as 'Fixed Installment Method' or 'Equal installment method'.

(iv) The annual amount of depreciation can be easily calculated by the following formula :

$$\text{Annual Depreciation} = \frac{\text{Original Cost - Estimated scrap value}}{\text{Estimated Life in year}}$$

For examples : A firm purchases a machine for Rs. 2,25,000 on April 1, 2013. The expected life of this machine is 5 years. After 5 years the scrap of this machine would be realized Rs. 25.000. Under straight line method, the amount of depreciation can be calculated as under :

$$\text{Annual Depreciable} = \frac{2,25,000 - 25,000}{5}$$

$$= ₹\ 40,000$$

Hence ₹ 40,000 will be charged every year as depreciation on this machine.

2. **Diminishing balance method :** Under this method, depreciation is charged as a fixed percentage on the book value of the asset every year. In first year the depreciation will be charged at the end of the year, on the total cost the asset.

Example: A machine is purchase for ₹ 2,00,000 on April

1.2009. It is decided to charge depreciation on this machine @ 10% p.a. The amounts of depreciation for first four years by using both the methods **(Straight line method and Diminishing balance method)** are shown as under :

Year	Book Value	Dep. @ 10%	Book Value	Dep. @ 10%
2009-10	20,000	2,000	20,000	2,000
2010-11	18,000 (20,000 - 2,000)	2,000	18,000 (20.000 - 2,000)	1,800
2011-12	16, 000 (18,000 - 2,000)	2,000	16.200 (18.000 - 1,800)	1,620
2012-13	14,000 (16,000 - 2,000)	2,000	14,580 (16.200 - 1,620)	1.458

Hence, in Straight Line method, amount of depreciation is same but in Diminishing Balance Method amount of depreciation goes on decreasing every year. Depreciation can be recorded by crediting it to the Assets account.

Illustration 1: On January 1, 2013, a firm bought a machine for ₹90,000 and spend ₹ 6,000 on its installation and ₹ 4,000 on its carriage. It is decided to charge depreciation @ 10% on straight line method. Books are closed on December 31st each year. Show Machinery Account for the year 2013 to 2015.

Solution :

Machinery Account

Dr. Cr.

Date	Particulars	J.F.	Rs.	Date	Particulars	J.F.	Rs.
2013				2013			
Jan. 1	To Bank A/c		90,00	Dec. 31	By Depreciation A/c		10,000
Jan. 1	To Cash A/c		6,000	Dec. 31	By Balance c/d		90.000
Jan. 1	To Cash A/c		4.000				
			1.00.000				1,00,000
2014				2014			
Jan. 1	To Balance b/d		90.000	Dec. 31	By Depreciation A/c		10.000
				Dec. 31	By Balance c/d		80,000
			90.000				90,000
2015				2015			
Jan. 1	To Balance b/d		80.000	Dec. 31	By Depreciation A/c		10,000
				Dec. 31	By Balance c/d		70,000
			80,000				80,000

Illustration 2 : On the basis of information given in Illustration I, Show machinery Account for the year 2013 to 2015 if depreciation is charged @ 10% on diminishing balance method.

Solution :

Machinery Account

Dr. Cr.

Date	Particulars	J.F		Date	Particulars	J.F	
2013				2013			
Jan. 1	To Bank A/c		90,000	Dec. 31	By Depreciation A/c		10,000
Jan. 1	To Cash A/c		6,000	Dec. 31	By Balance c/d		90,000
Jan. 1	To Cash A/c		4,000				
			1,00,000				1,00,000
2014				2014			
Jan. 1	To Balance b/d		90,000	Dec. 31	By Depreciation A/c		9,000
				Dec. 31	By Balance c/d		81,000
			90,000				90,000
2015				2015			
Jan. 1	To Balance c/d		81,000	Dec. 31	By Depreciation A/c		8,100
				Dec. 31	By Balance c/d		72,900
			81,000				81,000

Illustration 3 : On April 1, 2013 Kannu bought Machinery costing ₹80,000. On July 1, 2015 Machinery was sold for ₹40,000. Prepare Machinery Account from April, 1 2013 till July 1. 2015 assuming depreciation was charged @ 10% per annum on March 31, every year on the basis of Original cost method.

Solution :

Machinery Account

Dr. Cr.

Date	Particulars	J.F.		Date	Particulars	J.F.	
2013				2014			
Apr. 1	To Bank A/c		80,000	Mar. 31	By Depreciation A/c		8,000
				Mar. 31	By Balance c/d		72,000
			80,000				80,000

Date	*Particulars*	*J.F.*	*Rs.*	*Date*	*Particulars*	*J.F.*	*Rs.*
2014				2015			
Apr. 1	To Balance b/d		72,000	Mar. 31	By Depreciation A/c		8.000
				Mar. 31	By Balance cid		64.000
			72,000				**72,000**
2015				2015			
Apr. 1	To Balance b/d		64,000	July 1	By Bank A/c		40,000
				July 1	By Depreciation A/c		2,000
				July 1	By Loss on sale		
					of Machinery A/c		22,000
			64,000				**64,000**

Illustration 4

On the basis of information given in Illustration 3, prepare Machinery Account assuming depreciation was charged @ 15% per annum on reducing installment method.

Solution

Machinery Account

Dr. Cr.

Date	Particulars	J.F.	Rs.	Date	Particulars	Rs.
2013				2014		
April 1	To Bank A/c		80,000	Mar. 31	By Depreciation A/C	12,000
				Mar. 31	By Balance C/d	68,000
2014			**80,000**			**80,000**
April 1	To Balance b/d			2015		
			68,000	Mar. 31	By Depreciation A/c	10,200
2015				Mar. 31	By Balance c/d	57,800
April 1	To Balance b/d		**68,000**			**68,000**
				2015	By Bank A/c	40,000
			57,800	Jul. 1	By Depreciation A/c	2168
				Jul. 1	By Loss on Sale	15,632
			57,800	Jul. 1	of Machinery	**57,800**

There is another treatment for charging Depreciation. In this treatment, Provision for Depreciation Account is opened and depreciation is charged in this account instead of Asset Account.

In this treatment the balance of Asset Account remains same throughout its useful life. Provision for Depreciation is shown in the liabilities side of Balance Sheet.

Methods of Recording Depreciation

First Method
In this method one account is prepared :
(i) Asset A/c
In this case, each year, Depreciation is directly credited to the Asset A/c with the help of this entry:
Depreciation A/c Dr
To Asset A/c

Second Method
In this method two accounts are prepared :
(i) Asset A/c
(ii) Provision for Depreciation A/c
In such case, every year depreciation is directly credited to provision for Depreciation A/c. P.F.D. A/c shows the accumulated amount of depreciation to date. At the time sale of asset, the total accumulated depreciation of concern asset is transferred to the credit side of asset with the help of following entry.

Accumulated Depreciation A/c or Prov. for Depreciation A/c Dr.
To Asset A/c

Illustration 5 :

Vinod limited purchased a machine for ₹ 2,50,000 including installation cost on January 1, 2012. On October 1, 2014, machine was sold for ₹1,50,000. Depreciation was provided @ 10% p.a. on Fixed Installment method and accounts are closed on December 31, each year.

Show the Machinery Account and Provision for Depreciation Account for the year. 2012 to 2014.

Solution :

Machinery Account

Dr. Cr.

Date	Particulars	J.F.	Rs.	Date	Particulars	J.F.	Rs.
2012				2012			
Jan. 1	To Bank A/c		2,50.000	Dec. 31	By Balance c/d		2,50,000
			2,50,000				2,50,000
2013				2013			
Jan. 1	To Balance b/d		2,50,000	Dec. 31	By Balance c/d		2,50,000
			2,50,000				2,50,000
2014				2014			
Jan. 1	To Balance b/d		2.50,000	Oct. 1	By Provision for Dep. A/c		68,750
				Oct. 1	By Bank A/c		1,50,000
				Oct. 1	By Profit & Loss A/c		31,250
			2,50,000				2,50,000

Provision for Depreciation Account

Dr. Cr.

Date	Particulars	J.F.	₹	Date	Particulars	₹
2012				2012		
Dec. 31	To Balance c/d		25,000	Dec. 31	By Depreciation A/C	25,000
			25,000			**25,000**
2013				2013		
Dec. 31	To Balance c/d		50,000	Jan. 1	By Balance b/d	25,000
				Dec. 31	By Depreciation b/d	25,000
			50,000			**50,000**
2014				2014		
Oct. 1	To Machinery		68,750	Jan. 1	By Balance b/d	50,000
				Oct. 1	By Depreciation A/c	18,750
			68,750			**68,750**

Important Point : Total Depredation charged on Machinery from Jan 1, 2011 to Oct. 1, 2013 : ₹25,000+ ₹ 25.000 + ₹ 18,750 = ₹ 68,750.

Illustration 6 :

On the basis of information given in Illustration 5, show the Machinery Account and Provision for Depreciation is provided @ 20 % p.a. on Written Down Value Method.

Solution :

Machinery Account

Dr. Cr.

Date	Particulars	J.F.		Date	Particulars	J.F.	
2012				2012			
Jan. 1	To Bank A/c		2,50,000	Dec. 31	By Balance c/d		2,50,000
			2,50,000				2,50,000
2013				2013			
Jan. 1	To Balance b/d		2,50,000	Dec. 31	By Balance c/d		2,50,000
			2,50,000				2,50,000
2014				2014			
Jan. 1	To Balance b/d		2,50,000	Oct. 1	By Provision for Dep. A/c		1,14,000
Oct. 1	To Profit & Loss A/c		14,000	Oct. 1	By Bank A/c		1,50,000
			264,000				264,000

Provision for Depreciation Account

Dr. Cr.

Date	Particulars	J.F.	Rs.	Date	Particulars	J.F.	Rs.
2012				2012			
Dec. 31	To Balance c/d		50,000	Dec. 31	By Depreciation A/c		50,000
			50,000				50,000
2013				2013			
Dec. 31	To Balance c/d		90,000	Jan. 1	By Balance b/d		50.000
				Dec. 31	By Depreciation Ac		40.000
			90,000				90.000
2014				2014			
Oct. 1	To Machinery		1,14,000	Jan 1	By Balance b/d		90,000
				Oct. 1	By Depreciation A/c		24,000
			1,14,000				1,14,000

Important Point : Total Depreciation charged on Machinery from Jan. 1,2012 to Oct. 1, 2014: ₹50,000+ ₹ 40,000 + 24,000 = ₹1,14,000

Illustration 7 :

A Company purchased a machine for Rs. 40,000 on April 1, 2014. On October 1, 2015 it was sold for Rs. 13,000. The company charges depreciation @ 10% p.a. on straight line method.

Show Machinery Account, Provision for Depreciation Account and Machinery Disposal account if books are closed on March 31 each year.

Machinery Account

Dr. Cr.

Date	Particulars	J. F.	Rs.	Date	Particulars	J. F.	Rs.
2014				2015			
Apr. 1	To Bank A/c		40,000	Mar. 31	By Balance c/d		40,000
			40,000				40,000
2015				2015			
Apr. 1	To Balance b/d		40,000	Oct. 1	By Machinery Disposal A/c		40,000
			40,000				40,000

Provision for Depreciation Account

Dr. Cr.

Date	Particulars	J. F.	Rs.	Date	Particulars	J. F	Rs.
2015				2015			
Mar. 31	To Balance c/d		4,000	Mar. 31	By Depreciation A/c		4,000
			4,000				4,000
2015				2015			
Oct 31	To Machinery Disposal A/c		6,000	Apr. 1	By Balance b/d		4,000
				Oct. 1	By Depreciation A/c		2,000
			6,000				6,000

Machinery Disposal Account

Dr. Cr.

Date	Particulars	J.F.	Rs.	Date	Particulars	J.F.	Rs.
2015				2015			
Oct. 1	To Machinery A c		40.000	Oct. 1	By Prov. For Dep. A/c		6,000
					By Cash A/c		13,000
					By profit & loss A/c		21,000
			40.000				40,000

Important Point : Total Depreciation charged on Machine : ₹ 4,000 + ₹ 2,000 = ₹6,000

Illustration 8 :

On Oct. 1, 2012, Arora Auto Limited Purchased Furniture for ₹1,00,000 and spent ₹ 4,000 towards its installation. On July 1, 2013, the Furniture was disposed off ₹59,820 and on the same day furniture costing ₹1,60,000 were purchased.

Show the Furniture Account, Provision for Depreciation Account and Furniture Disposal Account for the year 2012, 2013 and 2014 if the rate of Depreciation is 15% per annum by Diminishing Balance method and accounts are closed or 31st march of every year.

Solution :

Furniture Account

Dr. Cr.

Date	Particulars	J.F.	Rs.	Date	Particulars	J.F.	Rs.
2012				2013			
Oct. 1	To Bank A/c		1,00,000	Mar. 31	By Balance c/d		1,04,000
Oct.1	To Bank A/c		4,000				
			1,04,000				**1,04,000**
2013				2013			
Apr. 1	To Balance bid		1,04,000	Jul. 1	By Furniture Disposal A/c		1,04,000
Jul. 1	To Bank A/c		1,60,000	2014 Mar. 31	By Balance c/d		1,60,000
			2,64,000				**2,64,000**
2014				2015			
Apr. 1	To Balance b/d		1,60,000	Mar. 31	By Balance c/d		1,60.000
			1,60,000				**1,60,000**

Provision for Depreciation Account

Dr. Cr.

Date	Particulars	J.F.	Rs.	Date	Particulars	J.F.	Rs.
2013				2013			
Mar. 31	To Balance c/d		7,800	Mar. 31	By Depreciation A/c		7,800
			7,800				**7,800**
2013				2013			
Jul. 1	To Furniture Disposal A/c		11,408	Apr. 1	By Balance b/d		7,800
					By Depreciation A/c		3,608
2014				2014			
Mar. 31	To Balance c/d		18,000	Mar. 31	By Depreciation A/c		18,000
			29,408	2014			**29,408**
2015				1 Apr.	By Balance b/d		18,000
Mar. 31	To Balance c/d		39,300	2015 Mar. 31	By Depreciation A/c		21,300
			39,300				**39,300**

Furniture Disposal Account

Dr. Cr.

Date	Particulars	J. F.	Rs.	Date	Particulars	J.F.	Rs.
2013				2013			
Jul. 1	To Furniture Ac		1.04.000	Jul 1	By Prov. For Dep. A/c		11,408
					By Bank A/c		59,820
					By profit & loss A/c		32,772
			1.04.000				**1,04,000**

Important Point : Total Depreciation charged on Machinery sold : Rs. 7,800 + Rs. 3,608 = Rs. 11,408.

Illustration 9 :

A firm purchased on 1st January, 2012 certain Machinery for ₹ 5,82,000 and spent ₹ 18, 000 on its erection. On 1st July, 2012, additional machinery costing ₹ 2,00,000 was purchased. On 1st July, 2014, the machinery purchased on 1st January, 2012 was auctioned for ₹ 2,86,000 and a fresh machinery for ₹ 4,00,000 was purchased on same date. Depreciation was provided annually on 31st December at the rate of 10% on written down value method. Prepare Machinery account from 2012 to 2014.

Date	Particulars	J.F.	Rs.	Date	Particulars	J.F.	Rs.
2012				2012	By Depreciation A/C		
Jan. 1	To Bank A/c (i)		6,00,000	Dec. 31			
July 1	To Bank A/c (ii)		2,00,000		(i) (600,000x10/100) = 60000		
					(ii) (200,00x10/100x 6/12) = 10000		
				Dec. 31	By Balance c/d		70,000
					(5,40,000+1,90,000)		7,30,000
							8,00,000
			8,00,000	2013			
				Dec. 31	By Depreciation A/c		
2013							
Jan. 1	To Balance b/d		**7,30,000**		(i) (5,40,000x10/100) 54,000		
	(5,40,000+1,90,000)				(ii) (1,90,000x10/100 19,000		73,000
				Dec.31	By Balance c/d		6,57,000
					(4,86,000+1,71,00)		**7,30,000**
2014			7,30,000				
Jan.1	To Balance b/d		6,57,000	2014	By Bank A/c (Sale)		2,86,000
	(4,86,000+1,71,000)			July 1			
July 1	To Bank A/c (iii)		4,00,000				

					By Dep. (4,86,000x 10/100x6/12)		24,300
					By P &L A/c (loss)		1,75,700
				Dec. 31	By Dep. A/c		
					(ii) (1,71,000x10/100) 17,100		
					(iii) (400,000x10/100x 6/12)20,000		37,100
							5,33,900
			10,57,000		By Balance c/d		**10,57,000**

Working Notes :

Cost of 1st Machine = Rs. 5,82,000 + Rs. 18,000 = Rs. 6,00,000 Profit/Loss on sale of 1st

Loss on Sale of 1st Machine = Book Value on– Sale Value

(Rs. 4,86,000-Rs. 24,300)Rs. 4,61,700 - Rs. 2,86,000 Loss on Sale of Machine = Rs. 1,75,700

Illustration 10 :

The following balances appear in the books of Sankalp on 01-01-2015

Machinery A/c Rs. 8,00,000

Provision for Depreciation a/c Rs. 3,18,000

On 01-01-2015 they decided to sell a machine for Rs. 34,500. This machine was purchased for Rs. 1,20,000 on 01-01-2011.

Show the machinery A/c, Provision for Depreciation A/c for the year ended December 31, 2015 assuming that depreciation was charged at 10% p.a. on Written Down value method.

Machinery Account

Dr. Cr.

Date	Particulars	J.F.	Rs.	Date	Particulars	J.F.	Rs.
2015				2015			
Jan. 1	To Balance b/d		8,00,000	Jan. 1	By Bank A/c		34,500
				Jan. 1	By Provision for Depreciation A/c		41,268
				Jan. 1	By Profit & Loss A/c		44,232
				Dec. 31	By Balance c/d		6,80,000
			8,00,000				**8,00,000**

Provision for Depreciation Account

Dr. Cr.

Date	Particulars	J.F.	Rs.	Date	Particulars	J.F.	Rs.
2015				2015			
Jan. 1	To Machinery A/c		41,268	Jan. 1	By Balance b/d		3,18,000
Dec. 31	To Balance A/c		3,17,095	Dec. 31	By Depreciation A/c		40,363
			3,58,363				**3,58,363**

Working Notes

Depreciation charged on Sold Machinery

Cost of the Machinery on 01-01-2011	1,20,000
Less : Depreciation on 31-12-2011	-12,000
Book Value on 01-01-2012	1,08,000
Less Depreciation on 31-12-2012	-10,800
Book Value on 01-01-2013	97,200
Less : Depreciation on 31-12-2013	-9,720
Book Value on 01-01-2014	87,480
Less : Depreciation on 31-12-2014	-8,748
Book Value on 01-01-2015	78,732
Cost of Machinery	1,20,000
Dep. Charged till Sale	41,268

(12,000+10,809+9,720+8,748)	
Book Value on 01-01-2015	78,732
Less : Sale Price	-34,500
Loss on sale of Machinery	44,232

Depreciation on Remaining Machinery	
Cost of Remaining Machinery (800,000 - 120,000)	6,80,000
Less : Accumulated Depreciation thereon (till 31-12-2014) (318,000 - 41,268)	-276,372
Book Value on 01-01-2015	4,03,628
Depreciation (4,03,628x10/100) = 40362.8 = 40363	

Illustration 11

(Problem Based on Missing Figures)

On 1st July 2012 Tata Private Ltd. purchased a machinery for ₹60,000. On 1st Oct. 2013 another machinery was purchased for ₹3,60000. On 1st July 2014, the machine purchased on July 2012 was sold for ₹3,36,000 and on the same date a fresh machinery was purchased for ₹4,00,00. Depreciation was provided @10% p.a. on the written down value method. Books are closed on 31st march every year.

You are required to prepare machinery account and provision for Depreciation for three years ending 31st March 2015.

MACHINERY ACCOUNT

Date	Particular	Amount (₹)	Date	Particular	Amount (₹)
2012 Jul-01	To Bank A/C	6,00,000	2013 March 31	By Balance c/d	6,00,000
		6,00,000			6,00,000
2013 April	To Balance b/d	6,00,000	2014 March 31	By Balance c/d	9,60,000
Oct1	To Bank A/C	360,000			9,60,000
		9,60,000			
2014 April-01	To Balance b/d	9,60,000	2014 July 1	By Bank A/C	3,36,000
July 1	To Bank A/C	4,00,000	–	By Prov. for Dep. A/C	(--------) (5)
			–	By Profit & Loss A/C	(--------) (7)
			2015 Mar 31	By Balance c/d	
		13,60,000			13,60,000

PROVISION OR DEPRECIATION ACCOUNT

Date	Particular	Amount (₹)	Date	Particular	Amount (₹)
2013 Mar-31	To Bank c/d	45000	2013 March 31	By Depreciation A/C	45000
		45000			45000
			2013 Apr-1	By Balance b/d	45000
2014 Mar 31	To Balance b/d	(-------)	2014 March 31	By Depreciation A/C	(-------) (1)
		(-------)			(-------)
2014 July 1	To Machinery A/C	(5) (-------)	2014 Apr 31	By Balance b/d	(--------) (2)
2015 Mar-31	To Balance c/d	(6) (-------)	July 1	By Depreciation A/C	(--------) (3)
				By Depreciation A/C	(--------) (4)
		(-------)	2015 Mar 31		(-------)

Answer:- 1) 73,500

2) 1,18,500

3) 12,488

4) 64,200

5) 1,12,988

6) 82,200

7) 1,33,012

Asset Disposal Account

Asset Disposal A/c is opened when an asset (partially or fully) is sold or disposed off. All entries related to sold asset are recorded in the asset disposal A/c. Methods of recording the entries in Asset Disposal A/C will depend on a fact whether a provisim for depreciation a/c is maintained or not.

Format of Assets Disposal Account

When provision for Depreciation Account is maintained

To Asset A/c	–	By provision for Depreciation	
(Original Value)		A/c	–
		By Bank A/c	–
To Statement of profile	–	By Statement of profile	–
Loss (if loss)	–	Loss (if Profit)	–

When provision for Depreciation Account is not maintained

To Asset A/c	–	By Bank A/c	–
(Original value - Depreciation)		By statement of profile	–
To Statement of profile &	–	Loss (if profit)	
Loss (if loss)	–		–

Illustration No. 12:

(Problem based on missing figures)

Fill up the missing figures in the plant Account given below. You are informed that the plant purchased on 1st October 2012 was sold on 1st April, 2014 for ₹ 95,000 . The depreciation is provided at the rate of 10% p.a on dimnishing balance by the company.

PLANT ACCOUNT

Date	Particular	Amount (₹)	Date	Particular	Amount (₹)
2010 Apr-31	To Bank A/C	(-------)	2011 March 31	By Depreciation A/C	30000
				By Balance c/d (1)	(-------)
		(-------)			(-------)
2011 Apr 1	To Balance b/d	(-------)	2012 March 31	By Depreciation A/C (2)	(-------)
			March 31	By Balance c/d (3)	(-------)
		(-------)			(-------)
2012 Apr 1	To Balance c/d	(-------)	2013 Mar 31	By Depreciation A/C (4)	(--------)
Oct 1	To Balance A/C	100,000	Mar 31	By Balance c/d (5)	(--------)
		(-------)			(--------)
			2014	By Depreciation A/C (6)	(--------)
2013 Apr 1	To Balance c/d	(-------)	Mar 31	By Balance c/d (7)	(--------)
					(--------)
		(-------)			
2014 Apr 1	To Balance c/d	(-------)	2014 Apr 1	Bank A/C	95000
Apr 1	To statement of profit & Loss (10)	(-------)	2015 Mar 31	By Depreciation A/C (8)	(--------)
			Mar 31	By Balance c/d (9)	(--------)
		(-------) (11)			(--------)

Answer:-

1) 2,70,000
2) 27,000
3) 2,43,000
4) 27300
5) 3,13,700
6) 31,370
7) 2,82,330
8) 19,683
9) 1,77,147
10) 9500
11) 2,91830

Practical Questions

1) On 1st April, 2013 Ashok & Brothers bought a second hand machine for ₹ 6,00,000 and spent ₹ 100000 for its repair and installation. On Oct. 1, 2015 the machine was sold for ₹ 5,00,000. Prepare Machine Account after charging depreciation @10% p.a. by Written down value Method, assuming that the books are closed on 31st March every year.

2) Vijay Ltd. purchased a plant on 1st April 2012 for ₹ 2,50,000. On 1st 2013, it purchased a new plant for ₹ 1,50,000. The part of the machine which was purchased on 1st April 2012 costing ₹ 50,000 was sold for ₹ 18000 on 30th september 2015. Prepare the plant A/c for four years. Depreciation is charged @10% p.a. on 31st March every year on the Diminishing Balance Method.

Ans.: Loss on sale of plant 16627, Balance 31 March, 2015 ₹ 2,46,645

Q.No.3: On 1st April 2012 a firm purchased a machinery for ₹ 8,00,000. On 1st Oct. in the same accounting year, an additional machinery costing ₹ 4,00,000 was purchased. On 1st 2013, the machinery purchased on 1st April 2012 was sold off for ₹ 3,60,000. On 1st October 2014, a new machinery was purchased for ₹ 10,00,000 while the machinery purchased on 1st October 2012 was sold for ₹ 3,40,000 on the same date. The firm provides depreciation on its machinery @ 10% p.a. on original cost 31st March every year.

Prepare Machinery Account (ii) Provision for Depreciation Account (iii) Machinery Disposal Account

Ans:- Balance of Machinery Account 9,50,000 Loss on Sale of 1st Machinery 3,20,000 Profit on sale of second Machinery ₹ 20,000.

Q.No.4: You are given the following balances as on 1st April 2010

Plant Account = ₹ 10,00,000

Provision for Depreciation on Account = ₹ 2,32,000

Depreciation is charged on plant at 10% p.a by the Diminishing Balance Method. A piece of plant purchased on 1st April 2008 for ₹ 2,00,000 was sold on 1st october 2010 for ₹ 1,20,000.

Prepare the Plant Account and provision for the Depreciation Account for the year ended 31st March 2011 and also prepare the plant Disposal Account.

Ans. : Loss on sale Plant 233,900.

Balance of provision for Depreciation on A/c on April, 2011 ₹ 2,54,000

Q.No. 5: Fill up the missing information in the machinery account, provision for Depreciation Account and Disposal Account. You are informed that on 30th June 2008 it sold off the first machine purchsed in 2006 for ₹ 5,24000 Accumlated Depreciation Account in maintained changing depreciation @ 10% on straight line method.

MACHINERY ACCOUNT

Date	Particular	Amount	Date	Particular	Amount
2006 Oct-01	To Bank A/C	6,55,000	2007 March 31	By---------- 1	----------
2007 March-01	To Bank A/C	2,40,000			
		8,95,000			
		----------	2008		
2007 April-01	To Balance b/d (2)		March 31	By Balance c/d (3)	----------
		----------			
2008 April-01	To Balance b/d (4)	----------	2008 June 30	---------- (5)	----------
			2009 March 31	By Balance c/d (6)	----------

PROVISION FOR DEPRECIATION ACCOUNT

Date	Particular	Amount	Date	Particular	Amount
-------	To ------- (7)	----------	----------	---------- (8)	----------
		----------			----------
			2007		
2008 March-31	To Balance c/d (11)	----------	April 1	By -------- (9)	
			2008 March 31	By -------- (10)	----------
		----------			----------
2008 June-30	---------- (15)	----------	2008 April 31	By -------- (12)	----------
			----------	By -------- (13)	
2009 March-31	---------- (16)	----------	2009 March 31	By -------- (14)	(----------)
		----------			----------

MACHINERY DISPOSAL ACCOUNT

Date (year)	Particular	Amount	Date (year)	Particular	Amount
-------	To ------- (20)	----------	----------	By provission for Depreciation A/C (17)	----------
			----------	Bank A/C (18)	----------
			----------	Statement of Profit & Loss (19)	----------
		----------			----------

Ans:- 1) By Balance b/d ₹ 8,95,000

2) ₹8,95,000

3) ₹8,95,000

4) ₹8,95,000

5) Machinery Disposal A/C ₹ 6,55,000

6) ₹2,40,000

7) By Depreciation D/C ₹ 34750

8) To Balance c/d ₹ 34750

9) By Balance b/d ₹ 34750

10) By Depreciation A/C (1) ₹ 89500

11) To Balance c/d ₹ 1,14,250

12) By Balance c/d ₹ 1,24,250

13) By Depreciation A/C (1) ₹ 16375

14) By Depreciation A/C (4) ₹ 24000

15) To Machinery Disposal A/C ₹ 1,14,250

16) To Balance c/d ₹ 50,000

17) ₹ 1,14,625

18) ₹ 5,24,000

19) ₹ 16375

20) To Machinery A/C 6,55,000

Provisions

- Provisions is to be made is respect of a liability which is certain to be incurred, but its accurate amount is not known.
- It is charged in the profit and loss Account on estimate basis. It should be clearly understood that if the amount of a known liability can be determined with reasonable accuracy, it can not be a provision.

Notes: Provision is a charge against profits, it means provision has to be made irrespective of business enterprise is earning enough profits or Incurring losses.

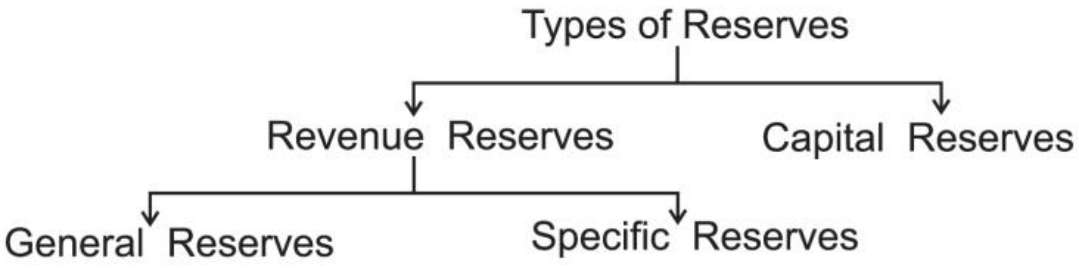
Examples of provisions : Provisions for Depreciation on assets, Provision for Repairs and Renewals of assets. Provision for Taxation. Provision for Discount on Debtors , Provision for Bad and Doubtful Debts.

Reserves

- Reserves are the amount set aside out of profits. It is an appropriation of profits and not a charge on the profits.
- The amount of profit retained is used in the business when difficult time comes. Since reserves are neither expenses nor losses. so these are not charged to profit & loss Account rather these are debited to Profit & Loss Appropriation Account which is prepared after Profit and Loss Account.
- Reserves are also known as 'Ploughing Back of Profits'.
- Reserves are created to strengthening the financial positions of the business enterprise.
- Examples are General Reserves, Divided Equalization Reserves etc.
- If the amount of reserve is invested outside the business then, it is called 'Reserve Fund'.
- Creation of reserve does not reduce the net profit but only reduced the divisible profits.

DIFFERENCE BETWEEN PROVISIONS AND RESERVE

Basis	Provision	Reserve
1. Meaning	It is created to meet a known liability.	It is create to strengthen the financial position of business enterprise.
2. Charge or Appropriation	Provision are charge against profits	Reserve is an appropriation of profit.
3. Objective	The object is to provide for known liability cannot be calculated accurately.	It is created to strengthen the financial position and to meet unforeseen liability.
4. Effect on profit & Loss A/c	It is debited to the profit. Hence' profit is reduced.	Reserve reduces divisible profits.
5. Creation	Provisions are to be created even if there are insufficient profits.	Reserve is created out of adequate profits only.
6. Mode of creation	Provision are created by debiting the Profit & loss A/c.	It is created through Profit & Loss Appropriation Account.
7. Investment	It cannot be invested outside the business	Reserve can be invested outside the business.
8. Necessity	Creation of provision is necessary as per law.	Its creation is not necessary. It is created as a matter of prudence.



Revenue Reserves

Revenue Reserves are those reserves which are created by setting aside a part of the net profit of business. Since reserves represent undistributed profit of the company so they are available for declaration of dividend and distribution among shareholders. Revenue reserves are of two types namely. (1) General Reserves (2) Specific Reserves.

(1) General Reserves :- Those reserves which are created out of profit to meet out the unforseen contigencies is called general reserves. They are termed as 'Free Reserves' or 'Contingency Reserves'. Creation of general reserve is optional. It is an appropriation of profit so it is made only if adequate profit is earned

by the company. They are shown on liability side of the balance sheet under the head," Reserve and surplus".

(2) **Specific Reserves:-** These reserves are created for specific purpose and can be utilised for that purpose only. Examples:- Divindend Equalization Reserves, Debentures Redemption Reserve, workmen Compensation fund, Investment Fluctuation Reserves etc.

Reserve fund :- If reserves are invested in outside securities, it is known as Reserve fund.

Capital Reserves:-

The reserves created out of capital profits are known as capital Reserve. Such reserves, generally are not available for distribution as cash dividend among the share holders of a company.

Examples:-

i) Profit on sale of fixed assets.

ii) Profit on revaluation of assets and liabilities.

iii) Securities premium earned on issue of share or debentures.

iv) Profit on the purchase of running business.

v) Profit earned on forfeiture of shares.

vi) Profit on redemption of debentures.

vii) Profit prior to the incorporation of a company

Capital profits can be used to write off capital losses and to issue fully paid up bonus shares among the equity share holders. However, company can declare dividend out of capital profits on the fulfilment of the following conditions.

i) Articles of Associations of a company permits the declaration of dividend out of such profile.

ii) Capital profits realised in cash.

iii) Profile remains after revaluation of assets and liabilities.