Chapter- 7

Depriciation, Provisions, & Reservations

Short question

Q1: What is Depreciation?

Q2: State briefly the need for providing depreciation.

Q3: What are the causes of depreciation?

Q4: Explain the basic factors affecting the amount of depreciation.

Q.5.Distinguish between the straight-line method and the written down value method of calculating depreciation.

Q6: In the case of a long term asset, repair and maintenance expenses are expected to rise in later years than in an earlier year. Which method is suitable for charging depreciation if the management does not want to increase the burden on profits and loss account on account of depreciation and repair.

Q7: What are the effects of depreciation on profit and loss account and balance sheet?

Q8: Distinguish between provision and reserve.

Q9: Give four examples each of provision and reserves.

Q10: Distinguish between revenue reserve and capital reserve.

Q11: Give four examples each of revenue reserve and capital reserves.

Q12: Distinguish between the general reserve and specific reserve.

Q13: Explain the concept of secret reserve.

Long answers :

Q1: Explain the concept of depreciation. What is the need for charging depreciation and what are the causes of depreciation?

Q2: Discuss in detail the straight-line method and written down value method of depreciation. Distinguish between the two and also give situations where they are useful.

Q3: Describe in detail two methods of recording depreciation. Also, give the necessary journal entries.

Q4: Explain determinants of the amount of depreciation.

Q5. Name and explain different types of reserves in details

Q5. What are the provisions? How are they created? Give accounting treatment in case of a provision for doubtful Debt.

NUMERICAL QUESTION

Q1 :

On April 01, 2000, Bajrang Marbles purchased a Machine for Rs 2,80,000 and spent Rs 10,000 on its carriage and Rs 10,000 on its installation. It is estimated that its working life is 10 years and after 10 years its scrap value will be Rs 20,000.

(a) Prepare a Machine account and Depreciation account for the first four years by providing depreciation on the straight-line method. Accounts are closed on March 31st every year.

(b) Prepare Machine account, Depreciation account and Provision for depreciation account (or accumulated depreciation account) for the first four years by providing depreciation using straight-line method accounts are closed on March
31 every year.

Q2 :

On July 01, 2000, Ashok Ltd. Purchased a Machine for Rs 1,08,000 and spent Rs 12,000 on its installation. At the time of purchase, it was estimated that the effective commercial life of the machine will be 12 years and after 12 years its salvage value will be Rs 12,000.

Prepare a machine account and depreciation Account in the books of Ashok Ltd. For the first three years, if depreciation is written off according to the straight-line method. The account is closed on December 31st, every year.

Q3 :

Reliance Ltd. Purchased a second-hand machine for Rs 56,000 on October 01, 2001, and spent Rs 28,000 on its overhaul and installation before putting it to operation. It is expected that the machine can be sold for Rs 6,000 at the end of its useful life of 15 years. Moreover, an estimated cost of Rs 1,000 is expected to be incurred to recover the salvage value of Rs 6,000. Prepare machine account and Provision for depreciation account for the first three years charging depreciation by fixed installment Method. Accounts are closed on December 31, every year.

Q4 :

Berlin Ltd. Purchased a second-hand machine for Rs 56,000 on July 01, 2001, and spent Rs 24,000 on its repair and installation and Rs 5,000 for its carriage. On September 01, 2002, it purchased another machine for Rs 2,50,000 and spent Rs 10,000 on its installation.

Depreciation is provided on machinery @10% p.a on the original cost method annually on December 31. Prepare machinery account and depreciation account from the year 2001 to 2004.

Prepare machinery account and depreciation account from the year 2001 to 2004, if depreciation is provided on machinery @10% p.a. on written down value method annually on December 31.

Q5 :

Ganga Ltd. purchased machinery on January 01, 2001, for Rs 5,50,000 and spent Rs 50,000 on its installation. On September 01, 2001, it purchased another machine for Rs 3,70,000. On May 01, 2002, it purchased another machine for Rs 8,40,000 (including installation expenses).

Depreciation was provided on machinery @10% p.a. on the original cost method annually on December 31. Prepare:

- Machinery account and depreciation account for the years 2001, 2002, 2003, and 2004.
- If depreciation is accumulated in provision for Depreciation account then prepare machine account and provision for depreciation account for the years 2001, 2002, 2003, and 2004.

Q6 :

Azad Ltd. purchased furniture on October 01, 2002, for Rs 4,50,000. On March 01, 2003, it purchased another furniture for Rs 3,00,000. On July 01, 2004, it sold off the first furniture purchased in 2002 for Rs 2,25,000. Depreciation is provided at 15% p.a. on written down value method each year. Accounts are closed each year on March 31. Prepare furniture account, and accumulated depreciation account for the years ended on March 31, 2003, March 31, 2004, and March 31, 2005. Also, give the above two accounts if the furniture disposal account is opened.

Q7 :

M/s Lokesh Fabrics purchased a Textile Machine on April 01, 2001, for Rs 1,00,000. On July 01, 2002, another machine costing Rs 2,50,000 was purchased. The machine purchased on April 01, 2001, was sold for Rs 25,000 on October 01, 2005. The company charges depreciation @15% p.a. on the straight-line method. Prepare machinery account and machinery disposal account for the year ended March 31, 2006.

Q8: The following balances appear in the books of Crystal Ltd, on Jan 01, 2005

	Rs
Machinery account on	15,00,000
Provision for depreciation account	5,50,000

On April 01, 2005, machinery which was purchased on January 01, 2002, for Rs 2,00,000 was sold for Rs 75,000. A new machine was purchased on July 01, 2005, for Rs 6,00,000. Depreciation is provided on machinery at 20% p.a. on the Straight-line method and books are closed on December 31 every year. Prepare the machinery account and provision for depreciation account for the year ending December 31, 2005.

Q9: M/s. Excel Computers has a debit balance of Rs 50,000 (original cost Rs 1,20,000) in the computers account on April 01, 2000. On July 01, 2000, it purchased another computer costing Rs 2,50,000. One more computer was purchased on January 01, 2001, for Rs 30,000. On April 01, 2004, the computer which has purchased on July 01, 2000, became obsolete and was sold for Rs 20,000. A new version of the IBM computer was purchased on August 01, 2004 for Rs 80,000. Show Computers account in the books of Excel Computers for the years ended on March 31, 2001, 2002, 2003, 2004 and 2005. The computer is depreciated @10 p.a. on a straight-line method basis.

Q10: Carriage Transport Company purchased 5 trucks at the cost of Rs 2,00,000 each on April 01, 2001. The company writes off depreciation @ 20% p.a. on original cost and closes its books on December 31, every year. On October 01, 2003, one of the trucks is involved in an accident and is destroyed. The insurance company has agreed to pay Rs 70,000 in full settlement of the claim. On the same date, the company purchased a second-hand truck for Rs 1,00,000 and spent Rs 20,000 on its overhauling. Prepare truck account and provision for depreciation account for the three years ended on December 31, 2003. Also, give the truck account if the truck disposal account is prepared.

Q11: Saraswati Ltd. purchased machinery costing Rs 10,00,000 on January 01, 2001. A new machinery was purchased on 01 May 2002 for Rs 15,00,000 and another on July 01, 2004 for Rs 12,00,000. A part of the machinery which originally cost Rs 2,00,000 in 2001 was sold for Rs 75,000 on October 31, 2004. Show the machinery account, provision for depreciation account and machinery disposal account from 2001 to 2005 if depreciation is provided at 10% p.a. on original cost and the account is closed on December 31, every year.

Q12: On July 01, 2001, Ashwani purchased a machine for Rs 2,00,000 on credit. Installation expenses Rs 25,000 are paid by cheque. The estimated life is 5 years and its scrap value after 5 years will be Rs 20,000. Depreciation is to be charged on a straight line basis. Show the journal entry for the year 2001 and prepare necessary ledger accounts for the first three years.

Q13: On October 01, 2000, a Truck was purchased for Rs 8,00,000 by Laxmi Transport Ltd. Depreciation was provided at 15% p.a. on the diminishing balance basis on this truck. On December 31, 2003, this Truck was sold for Rs 5,00,000. Accounts are closed on 31st March every year. Prepare a Truck Account for the four years

Q14: Kapil Ltd. purchased machinery on July 01, 2001, for Rs 3,50,000. It purchased two additional machines, on April 01, 2002 costing Rs 1,50,000 and on October 01, 2002 costing Rs 1,00,000. Depreciation is provided at @10% p.a. on a straight-line basis. On January 01, 2003, the first machinery becomes useless due to technical changes. This machinery was sold for Rs 1,00,000, prepare machinery account for 4 years based on the calendar year.

Q15: On January 01, 2001, Satkar Transport Ltd, purchased 3 buses for Rs 10,00,000 each. On July 01, 2003, one bus was involved in an accident and was completely destroyed and Rs 7,00,000 were received from the Insurance Company in full settlement. Depreciation is written off @15% p.a. on a diminishing balance method. Prepare a bus account from 2001 to 2004. Books are closed on December 31 every year.

Q16: On October 01, 2001, Juneja Transport Company purchased 2 Trucks for Rs 10,00,000 each. On July 01, 2003, One Truck was involved in an accident and was completely destroyed and Rs 6,00,000 were received from the insurance company in full settlement. On December 31, 2003, another truck was involved in an accident and destroyed partially, which was not insured. It was sold off for Rs 1,50,000. On January 31, 2004, the company purchased a fresh truck for Rs 12,00,000. Depreciation is to be provided at 10% p.a. on the written down value every year. The books are closed every year on March 31. Give the truck account from 2001 to 2004.

Q17: A Noida based Construction Company owns 5 cranes and the value of this asset in its books on April 01, 2001, is Rs 40,00,000. On October 01, 2001, it sold one of its cranes whose value was Rs 5,00,000 on April 01, 2001, at a 10% profit. On the same day, it purchased 2 cranes for Rs 4,50,000 each. Prepare a cranes account. It closes the books on December 31 and provides for depreciation on 10% written down value.

Q18: Shri Krishan Manufacturing Company purchased 10 machines for Rs 75,000 each on July 01, 2000. On October 01, 2002, one of the machines got destroyed by fire and an insurance claim of Rs 45,000 was admitted by the company. On the same date, another machine is purchased by the company for Rs 1,25,000.

The company writes off 15% p.a. depreciation on written down value basis. The company maintains the calendar year as its financial year. Prepare the machinery account from 2000 to 2003.

Q19: On January 01, 2000, a Limited Company purchased machinery for Rs 20,00,000. Depreciation is provided @15% p.a. on a diminishing balance method. On March 01, 2002, one-fourth of the machinery was damaged by fire and Rs 40,000 were received from the insurance company in full settlement. On September 01, 2002, another machinery was purchased by the company for Rs 15,00,000.

Write up the machinery account from 2002 to 2003. Books are closed on December 31, every year.

Q20: A Plant was purchased on 1st July 2000 for Rs 3,00,000 and Rs 50,000 were spent on its installation. The depreciation is written off at 15% p.a. on the straight-line method. The plant was sold for Rs 1,50,000 on October 01, 2002, and on the same date, a new Plant was installed at the cost of Rs 4,00,000 including purchasing value. The accounts are closed on December 31 every year.

Show the machinery account and provision for depreciation account for 3 years

Q21: An extract of Trial balance from the books of Tahiliani and Sons Enterprises on December 31 2005 is given below:

Name of the Account	Debit Amount Rs	Credit Amount Rs
Sundry debtors	50,000	
Bad debts	6,000	
Provision for doubtful debts		4,000

Additional Information:

- Bad Debts proved bad; however, not recorded amounted to Rs 2,000.
- Provision is to be maintained at 8% of debtors

Give necessary accounting entries for writing off the bad debts and creating the provision for doubtful debts account. Also, show the necessary accounts.

Q22: The following information is extracted from the Trial Balance of M/s Nisha Traders on 31 December 2005.

Sundry Debtors	80,500
Bad Debts	1,000
Provision for Bad Debts	5,000

Additional Information Bad Debts Rs 500

- Provision is to be maintained at 2% of Debtors
- Prepare bad debts account, Provision for bad debts account, and profit and loss account.