

## Solution 9.1

**a)** Capital expenditure is expenditure on the purchase or improvement of fixed assets. A fixed asset relates to items purchased (not for resale at a profit) that will be used in the business for more than one accounting year and is of significant monetary value. It can also include money spent to add value to fixed assets and can include any costs in bringing the assets to their present location and condition. Capital expenditure can include the purchase cost of an asset as well as legal costs, transportation costs and installation costs relating to the asset. An example of capital expenditure is the purchase and installation of refrigeration equipment in a supermarket.

Revenue expenditure is expenditure which does not increase the value of fixed assets but relates to the operating costs of the business. Revenue expenditure relates to the day to day running costs of a business. Examples of revenue expenditure include; rent, insurance, wages and electricity.

**b)** Key questions to address when classifying items as 'capital' are:

1. Is the item bought for use in the organisation and not for resale at a profit?
2. Will it be of use in the organisation, or add benefit, for more than one accounting year?
3. Is it of significant value?

## Solution 9.2

1. Purchase of new van	<b>Capital</b>
2. Cost of road tax for new van.	<b>Capital</b>
3. Cost of painting firms name on new van	<b>Revenue</b>
4. Purchase of stock for re-sale	<b>Revenue</b>
5. Carriage inwards on stock for re-sale	<b>Revenue</b>
6. Carriage costs on sales	<b>Revenue</b>
7. Legal costs of collecting debts	<b>Revenue</b>
8. Legal costs in relation to acquiring a new office premises	<b>Capital</b>

9. Costs of installing new machine	<b>Capital</b>
10. Installing security equipment	<b>Capital</b>
11. Roof repairs	<b>Revenue</b>
12. Fitting partitions in the shop	<b>Capital</b>
13. Installing a security hut	<b>Capital</b>
14. Wages	<b>Revenue</b>
15. Fire insurance premium	<b>Revenue</b>
16. Carriage costs on bricks for security hut	<b>Capital</b>
17. Cost of altering the interior of new van to increase capacity	<b>Capital</b>
18. Purchase of replacement engine for existing van.	<b>Revenue</b>

### Solution 9.3

- a) Treating a fixed asset as an expense in the profit and loss account will result in profit being understated by the €25,000. In the balance sheet both fixed assets and capital will be understated by €25,000.
- b) Treating repairs as capital expenditure will result in the profit being overstated by €5,000 in the profit and loss account. In the balance sheet both fixed assets and capital will be overstated by €5,000.

### Solution 9.4

**The capital cost for the Hilda Hotel will amount to:**

Purchase cost	€22,000
Installation and testing	€ 2,000
Training	€ 1,000
Total capital cost	€25,000

## Solution 9.5

- a) Depreciation is a measure of the wear and tear or loss in value of an asset over its life. It is the difference between the cost of a non-current (fixed) asset and the amount received when it is sold. Assets such as plant, equipment, motor vehicles and furniture are all assets that lose value over time due to either wear and tear or, economic factors such as inadequacy and obsolescence or, the simple passing of time.
- b) The purpose of depreciation charge in the accounts is to ensure that the value of non-current assets in the balance sheet is reflective of the current value of the assets. Non-current assets must be depreciated in accordance with the accruals and prudence concepts, except non depreciable land which under normal economic conditions appreciates in value. Each year the asset will appear in the balance sheet at its reduced book value (net book value), while the reduction, called depreciation, is treated as an expense in the profit and loss account.
- c) Capital costs relating to fixed assets

Original cost of the asset.	✓Capital
Delivery costs of the asset.	✓Capital
The legal costs in acquiring the asset.	✓Capital
Repairs to the asset.	X Revenue
Installation costs of the asset.	✓Capital
VAT on the cost of the asset.	? Capital only if the business cannot reclaim the VAT
Wages of maintenance	? Capital only if they worked on installation otherwise treat as revenue expenditure.

## Solution 9.6

### Straight line approach

$$\frac{\text{Cost } \text{€}20,000 - \text{scrap } \text{€}4,800}{4 \text{ years}} = \text{€}3,800 \text{ per annum}$$

### Reducing balance approach

Original cost	€ 20,000
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Depreciation end of year 1 (€20,000 x 30%)	<b><u>6,000</u></b>
NBV end of year 1	14,000
Depreciation end of year 2 (€14,000 x 30%)	<b><u>4,200</u></b>
NBV end of year 2	9,800
Depreciation end of year 3 (€9,800 x 30%)	<b><u>2,940</u></b>
NBV end of year 3	6,860
Depreciation end of year 4 (€6,860 x 30%)	<b><u>2,058</u></b>
NBV end of year 4	4,802

### Solution 9.7

DR		Office Equipment Account		CR	
		€			€
1/1/02	Bal b/d	100,000			
2002	Bank a/c	25,000			
2002	Bank a/c	35,000	31/12/02	Bal c/d	160,000
		<u>160,000</u>			<u>160,000</u>
1/1/03	Bal b/d	160,000			

DR		Provision for Depreciation of Equipment Account		CR	
		€			€
			1/1/02	Bal b/d	50,000
31/12/02	Bal c/d	82,000	31/12/02	P & L a/c	32,000
		<u>82,000</u>			<u>82,000</u>
			1/1/03	Bal b/d	82,000

Annual depreciation is  
 $€160,000 \times 20\% = €32,000$

DR		Income statement (Extract)		CR	
		€			€
31/12/02	Depreciation	32,000			

**Statement of Financial Position (Extract)**

<b>Non Current Assets</b>	Cost	Accumulated Depreciation	Net Book Value
	€	€	€
Office equipment	160,000	(82,000)	78,000

**Solution 9.8**

<b>DR</b>		<b>Equipment Account</b>		<b>CR</b>	
		€		€	
1/1/09	Bank a/c	80,000			
20/10/09	Bank a/c	<u>100,000</u>	31/12/09	Bal c/d	<u>180,000</u>
		<u>180,000</u>			<u>180,000</u>
1/1/10	Bal b/d	180,000			
15/2/10	Bank	70,000			
20/11/10	Bank	<u>50,000</u>	31/12/10	Bal c/d	<u>300,000</u>
		<u>300,000</u>			<u>300,000</u>
1/1/11	Bal b/d	300,000			
20/3/11	Bank	<u>100,000</u>	31/12/11	Bal c/d	<u>400,000</u>
		<u>400,000</u>			<u>400,000</u>
1/1/12	Bal b/d	400,000			
15/5/12	Bank	<u>150,000</u>	31/12/12	Bal c/d	<u>550,000</u>
		<u>550,000</u>			<u>550,000</u>

<b>DR</b>		<b>Provision for Depreciation of Equipment Account</b>		<b>CR</b>	
		€		€	
31/12/09	Bal c/d	<u>18,000</u>	31/12/09	P & L a/c	<u>18,000</u>
1/10/04			1/1/10	Bal b/d	18,000
31/12/10	Bal c/d	<u>48,000</u>	31/12/10	P & L a/c	<u>30,000</u>
		<u>48,000</u>			<u>48,000</u>
			1/1/11	Bal b/d	48,000
31/12/11	Bal c/d	<u>88,000</u>	31/12/11	P & L	<u>40,000</u>
		<u>88,000</u>			<u>88,000</u>
			1/1/12	Bal b/d	88,000

31/12/12 Bal c/d	<u>143,000</u>	31/12/12 P & L	<u>55,000</u>
	<u>143,000</u>		<u>143,000</u>

<b>DR</b>	<b>Income Statement (P&amp;L Extract)</b>		<b>CR</b>
		€	€
2009 Depreciation - equipment		18,000	
2010 Depreciation - equipment		30,000	
2011 Depreciation - equipment		40,000	
2012 Depreciation - equipment		55,000	

#### Statement of Financial Position (Extract)

	Cost	Accumulated Depreciation	Net Book Value
	€	€	€
<b>Non Current Assets</b>			
<b>2009</b>			
Equipment	180,000	(18,000)	162,000
<b>2010</b>			
Equipment	300,000	(48,000)	152,000
<b>2011</b>			
Equipment	400,000	(88,000)	312,000
<b>2012</b>			
Equipment	550,000	(143,000)	407,000

## Solution 9.9

DR		Equipment Account		CR	
		€			€
1/1/10	Bank a/c	50,000			
20/10/10	Bank a/c	90,000	31/12/10	Bal c/d	140,000
		<u>140,000</u>			<u>140,000</u>
1/1/11	Bal b/d	140,000			
15/2/11	Bank	80,000			
20/11/11	Bank	60,000	31/12/11	Bal c/d	280,000
		<u>280,000</u>			<u>280,000</u>
1/1/12	Bal b/d	280,000		Disposal	30,000
20/3/12	Bank	120,000	31/12/11	Bal c/d	370,000
		<u>400,000</u>			<u>400,000</u>
1/1/13	Bal b/d	370,000			

DR		Provision for Depreciation of Equipment Account		CR	
		€			€
31/12/10	Bal c/d	<u>14,000</u>	31/12/10	P & L a/c	<u>14,000</u>
31/12/11	Bal c/d	<u>42,000</u>	1/1/11	Bal b/d	14,000
		42,000	31/12/11	P & L a/c	<u>28,000</u>
	Disposal	6,000			<u>42,000</u>
31/12/11	Bal c/d	<u>73,000</u>	1/1/11	Bal b/d	42,000
		79,000	31/12/11	P & L	<u>37,000</u>
					<u>79,000</u>
			1/1/12	Bal b/d	73,000

DR		Disposal Account		CR	
		€			€
1/10/04	Equipment a/c	30,000	1/10/04	Depreciation a/c	6,000
			1/10/04	Bank a/c	20,000
			1/10/04	P & L a/c	<u>4,000</u>
		<u>30,000</u>			<u>30,000</u>

<b>DR</b>	<b>Income Statement (P&amp;L Extract)</b>		<b>CR</b>
		€	€
2010	Depreciation - equipment	14,000	
2011	Depreciation - equipment	28,000	
2012	Depreciation - equipment	37,000	
2012	Loss on disposal	4,000	

### Statement of Financial Position (Extract)

<b>Non Current Assets</b>	Cost €	Accumulated Depreciation €	Net Book Value €
<b>2010</b>			
Equipment	140,000	(14,000)	126,000
<b>2011</b>			
Equipment	280,000	(42,000)	238,000
<b>2012</b>			
Equipment	370,000	(73,000)	297,000

### Solution 9.10

<b>DR</b>	<b>Equipment Account</b>		<b>CR</b>
		€	€
1/1/Y1	Bank a/c	22,000	
1/10/Y1	Bank a/c	10,000	31/12/Y1 Bal c/d
		<u>32,000</u>	<u>32,000</u>
1/1/Y2	Bal b/d	32,000	1/10/Y2 Disposal a/c
		<u>32,000</u>	31/12/Y2 Bal c/d
		<u>32,000</u>	<u>24,000</u>
1/1/Y3	Bal b/d	24,000	<u>32,000</u>



<b>DR</b>		<b>Provision for Depreciation of Equipment Account</b>		<b>CR</b>	
		€			€
31/12/Y1	Bal c/d	<u>3,200</u>	31/12/Y1	P & L a/c	<u>3,200</u>
1/10/Y2	Disposal a/c	800	1/1/Y2	Bal b/d	3,200
31/12/Y2	Bal c/d	<u>4,800</u>	21/12/Y2	P & L a/c	<u>2,400</u>
		<u>5,600</u>			<u>5,600</u>
			1/1/Y3	Bal b/d	4,800

<b>DR</b>		<b>Disposal Account</b>		<b>CR</b>	
		€			€
1/10/Y2	Equipment a/c	8,000	1/10/Y2	Depreciation a/c	800
			1/10/Y2	Bank a/c	5,000
			1/10/Y2	P & L a/c	<u>2,200</u>
		<u>8,000</u>			<u>8,000</u>

<b>DR</b>		<b>Fixtures Account</b>		<b>CR</b>	
		€			€
1/1/Y1	Bank a/c	<u>30,000</u>	31/12/Y1	Bal c/d	<u>30,000</u>
1/1/Y2	Bal b/d	30,000			
1/7/Y2	Bank a/c	<u>5,000</u>	31/12/Y2	Bal c/d	<u>35,000</u>
		<u>35,000</u>			<u>35,000</u>
1/1/Y3	Bal b/d	35,000			

<b>DR</b>		<b>Provision for Depreciation of Equipment Account</b>		<b>CR</b>	
		€			€
31/12/Y1	Bal c/d	<u>3,750</u>	31/12/Y1	P & L a/c	<u>3,750</u>
			1/1/Y2	Bal b/d	3,750
31/12/Y2	Bal c/d	<u>8,125</u>	31/12/Y2	P & L a/c	<u>4,375</u>
		<u>8,125</u>			<u>8,125</u>
			1/1/Y3	Bal b/d	8,125

<b>DR</b>		<b>Income Statement (P&amp;L Extract)</b>		<b>CR</b>	
		€			€
Yr 1	Depreciation - equipment	3,200			
	Depreciation - fixtures	3,750			

Yr 2	Disposal loss	2,200
	Depreciation - equipment	2,400
	Depreciation - fixtures	4,375

### Statement of financial position (Extract)

	Cost	Accumulated Depreciation	Net Book Value
	€	€	€
<b>Non-current assets</b>			
<b>Year 1</b>			
Equipment	32,000	(3,200)	28,800
Fixtures	30,000	(3,750)	26,250
<b>Year 2</b>			
Equipment	24,000	(4,800)	19,200
Fixtures	35,000	(8,125)	26,875

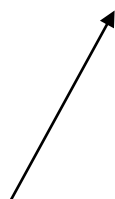
### Solution 9.11

DR		Vehicles Account		CR	
		€			€
1/1/12	Bal b/d	256,000	30/6/12	Disposal a/c	40,000
1/4/12	Bank a/c	56,000			
1/7/12	Bank a/c	25,000	31/12/12	Bal c/d	297,000
		<u>337,000</u>			<u>337,000</u>
1/1/13	Bal b/d	297,000			

DR		Provision for Depreciation of Vehicles Account		CR	
		€			€
30/6/12	Disposal a/c	31,360	1/1/12	Bal b/d	135,000
31/12/12	Bal c/d	180,984	31/12/12	P & L a/c	77,344
		<u>212,344</u>			<u>212,344</u>
			1/1/13	Bal b/d	180,984

€
40,000
(16,000) 40,000x40%
24,000
(9,600) 24,000x40%
14,400
(5,760) 14,400x40%
8,640
Depreciation to date is
16,000+9,600+5,760 =31,360

**Cost €297,000 - net depreciation  
€103,640 (i.e.€135,000 - €31,360) =  
€193,360 x 40% = €77,344**



DR		Disposal Account		CR	
		€			€
30/6/12	Vehicles a/c	40,000	30/6/12	Depreciation a/c	31,360
			30/6/12	Bank a/c	8,500
			30/6/12	P & L a/c	140
		<u>40,000</u>			<u>40,000</u>

DR		Income Statement 2012 (P&L Extract)		CR	
		€			€
	Disposal loss	140			
	Depreciation – vehicles	77,344			

### Statement of financial position 2012 (Extract)

Non Current Assets	Cost	Accumulated Depreciation	Net Book Value
	€	€	€
Vehicles	297,000	(180,984)	116,016

### Solution 9.12

DR		Machinery Account		CR	
		€			€
5/1/Y1	Bank a/c	100,000			
1/9/Y1	Bank a/c	<u>220,000</u>	31/12/Y1	Bal c/d	<u>320,000</u>
		<u>320,000</u>			<u>320,000</u>
1/1/Y2	Bal b/d	320,000	30/7/Y2	Disposal a/c	100,000
1/8/Y2	Bank a/c	<u>130,000</u>	31/12/Y2	Bal c/d	<u>350,000</u>
		<u>450,000</u>			<u>450,000</u>
1/1/Y3	Bal b/d	350,000			

DR		Provision for Depreciation of Machinery Account		CR	
		€			€
31/12/Y1	Bal c/d	<u>52,000</u>	31/12/Y1	P & L a/c	<u>52,000</u>
30/7/Y2	Disposal a/c	47,500	1/1/Y2	Bal b/d	52,000
31/12/Y2	Bal c/d	<u>104,250</u>	31/12/Y2	P & L a/c	<u>99,750</u>
		<u>151,750</u>			<u>151,750</u>
			1/1/Y3	Bal b/d	104,250

DR		Disposal Account		CR	
		€			€
30/7/Y2	Machinery a/c	100,000	30/7/Y2	Depreciation a/c	47,500
			30/7/Y2	Bank a/c	45,000
			30/7/Y2	P & L a/c	7,500
		<u>100,000</u>			<u>100,000</u>

DR		Income Statement (P&L Extract)		CR	
		€			€
Yr 1	Depreciation – machinery	52,000			
Yr 2	Disposal loss	7,500			
Yr 2	Depreciation – machinery	99,750			

### Statement of Financial position (Extract)

	Cost	Accumulated Depreciation	Net Book Value
	€	€	€
<b>Yr 1</b> Machinery	320,000	(52,000)	268,000
<b>Yr 2</b> Machinery	350,000	(104,250)	245,750

### Depreciation calculations:

#### Year 1

Machine 1 $100,000 \times 30\%$	30,000
Machine 2 $220,000 \times 30\% \times \frac{4}{12}$	22,000
	<b>52,000</b>

#### Year 2

Machine 1 $100,000 \times 30\% \times \frac{7}{12}$	17,500
Machine 2 $220,000 \times 30\%$	66,000
Machine 3 $130,000 \times 30\% \times \frac{5}{12}$	16,250
	<b>99,750</b>