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Code Letter : AC02

This set of lectures contains:-

LECTURE 1 : Hire-Purchase Accounts.

LECTURE 2 : Lease Accounts.

TEST AC02.

NOTE: The test on this set of lectures is bound in at the back of the book.

16 395

HIRE-PURCHASE ACCOUNTS.

DEFINITION OF HIRE-PURCHASE:

When payments are spread over a period, charges for interest will be included. Each payment, made at regular intervals, is usually of equal amount. In each payment, however, is included an amount For interest and another amount (the balance) which operates as a reduction of the debt owing for the ordinary selling price of the article. It is this apportionment which sometimes give rise to difficulty.
cases the hire purchase selling price is quoted as the normal se
price plus interest at a certain rate, but sometimes a special i
price is quoted. In the latter case i
re Purchase
he article
(1) The Seller; and
(2) The Buyer.

BUYER’S BOOK

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Second Method:
When the Hire Purchase Agreement is signed ---
Credit Supplier) with cash purchase price of
Debit Asset A/c) the asset.
As the instalments are paid ---
Credit Cash) with the amount of each
Debit Supplier) instalment paid.
Credit Supplier) with interest on balance
Debit Interest (or) outstanding at beginning of
Hire) A/c) each period.
Third Method:
When Hire Purchase Agreement is signed ---
Debit Asset A/c with cash purchase price of asset.
Debit Interest Suspense A/c with the total amount
payable in respect of
interest.
Credit Supplier with total amount payable including
interest.
When instalments paid ---
Debit Supplier) with full amount of each
Credit Cash) instalment.
At end of each financial year, or at shorter periods if
necessary ---
Debit Profit and Loss Account) with interest on the
Credit Interest Suspense A/c) outstanding balance of
the Cash price due to
the supplier.
This method has the advantage of showing all the relevant
transactions in the books, and although it is sometimes argued

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that the buyer does not become the owner until the lost instalment is paid, and, consequently, the entries should only be made as each instalment is paid, it must be borne in mind that the buyer is responsible for the asset purchased once it has been delivered to him, and he must look after it, as though it is his own.
If either the second or third method is adopted, the balance on the Supplier’s A/c (a credit) should be deducted from the book value of the asset when the Balance Sheet is prepared, and shown as "Assets on Hire Purchase Agreement". (See illustration later in this lecture).
Depreciation on the Full cash price of the asset MUST be allowed for in each method.
EXAMPLE:
A Gold Mining Company purchases machinery on the hire purchase system. An initial deposit of R600 is to be paid and 5 yearly instalments of the same amount are payable at the end of each year. Interest of 5% p.a. is to be charged on the yearly balances.
You are to show the accounts in the books of the buyer, and to provide for depreciation at the rate of 10% p.o.
Discussion:
Where we are not aetually told the cash selling price of the articles purchased we must find it out. We would do so in this case by consulting Annuity Tables (in examinations you will always be given either the cash value or an extract from tables from which you can work it out).
Our First step then is to find the present value of annuity of R600 payable for 5 years (at the egg of each year) reckoning interest at 5% p.0. Annuity Tables show that the present value of an annuity of R1 payable for 5 years (at the end of each year) with interest at 5% p.0. is R4,329477. Our annuity is worth 600 times as much, i.e., R2 597, 6862.
It is important to note the interval between the payments - monthly, quarterly or yearly, etc. - and also when the first instalment falls due. R1 which Falls due 6 months ahead is worth more than Rl which falls due in twelve months’ time.

To R2 597,69 we add the deposit of R600 (since as this is paid at once, its present value is the same as its face value), thus giving R3 197,69 as the cash value of the machinery.

FIRST METHOD: BOOKS OF BUYER.

JOURNAL

1990
Jun. 1
Machinery (on H.P.) A/c Dr.
To Machinery Co.
being deposit on machinery purchased under hire-purchose agreement dated this day.

1990
Dec. 31
Machinery A/c Dr.
Machinery Hire A/c Dr.
(5% on R2597,69 the outstanding balance at end of first year)
To Machinery Co.
being first instalment, etc.

1991
Dec. 31
Machinery A/c Dr.
Machinery Hire A/c (5% on R2597,69 - R470,12)
To Machinery Co.
493 62
106 38
600 00
being second instalment, etc.

1992
Dec. 31
Machinery A/c Dr.
Machinery Hire A/c (5% on R1633,95)
To Machinery Co.
518 30
81 70
600 00
being third instalment, etc.

1993
Dec. 31
Machinery AC3 Dr.
Machinery Hire A/c (5% on Rlll5,65) Dr.
To Machinery Co.
544 22
55 78
600 00
being fourth instalment, etc.

_____________.______________________
JOURNAL $CONTINUED2.
R c R c
1994
Dec. 31 Machinery A/c Dr. 571 43
Machinery Hire A/c (5% on
R571,43) Dr. 28 57
To Machinery Co. 600 00
being fifth and final instalment,
etc.
I
The interest charges are heavy in the early years when most of
the purchase price is unpaid, but become less as payments are made.
The capital value of the instalment correspondingly increased.
MACHINERY gON HIRE-PURCHASEZ ACCOUNT.
1990 R c 1990 1 R , c
Jan. 1 Machinery Co. 600 00 Dec. 31 Dep’n (10% 3
Dec. 31 do. 470 12 on R3 197,69); 319! 77
Balance c/d . 750 35
R1 070 1R1 070 , 12
_____ u----T::-
1990 1991 1 1
Dec. 31 Balance b/f 750 35 Dec. 31 Dep’n (10%
1991 on R2 877,92) 287 79
Dec. 31 Machinery Co. 493 62 Balance c/d
R1 243
1991 1992
Dec. 31 Balance b/f 956 18 Dec. 31 Dep’n (10%
1992 on R2 590,13)
Dec. 31 Machinery Co. 518 30 Balance c/d
.R1 474

MACHINERY 0N HIRE-PURCHASE ACCOUNT. CONTINUED).
19921 R c
Dec.$ 31 Balance b/f 1 215 47
19933
Dec. 31 Machinery Co. 544 22
31 Dep’n (10%
on R2331,12) 233 11
Balance c/d 1 526 58
R1 759 69 R1 759 69
1993
Dec. 31 Balance b/f 1 526 58 Dep’n (10%
1994 on R2098,01) 209 80
Dec. 31 Machinery Co. 571 43 Balance c/d l 888 21
R2 098 01 R2 098 01
1994
Dec. 31 Balance b/f l 888 21
MACHINERY HIRE ACCOUNT.
__.____
Machinery Co. . Income Stat.

________.______________________
This account shows the yearly interest charge.
MACHINERY COMPANY.
____
Machinery
Sundries
Do you understand the first method of re
cording 0 Hire-
Purchase in the buyer’s books?
SECOND METHOD:
MACHINERY ON HIRE-PURCHASE ACCOUNT.
Jon. 1 Machinery Co.

MACHINERY 0N HIRE-PURCHASE ACCOUNT CONTINUED .
1990 R c
Dec. 2 877 92 Dep’n
Balance
R2 877 92
1991
Dec. 2 590 13 . Dep’n
Balance
R2 590 13
1992
Dec. Balance 2 331 12 Dep’n
Balance
R2 331 12
1993
Dec. 2 098 01
1994
Dec. Balance
NOTE: The final balance brought down is the some as under the first method when 011 the instalments have been paid.
MACHINERY COMPANY.
R c
Jun. Cash - Mach. A/c
deposit 600 00 Interest
Dec. do. 600 00
Balance c/d 2 127 57
R3 327

MACHINERY COMPANY CONTINUED.
600 00 . Balance b/f
l 633 96
Interest
600 00 . Balance
1 115 65
. Interest
R1 715
Cash 600 00 . Balance b/f
Balance 571 43
. Interest
R1 171
Balance b/f
Interest
The Interest Account is exoctl
y the some as the Machinery Hire
Account under the first method.
To fix in your mind this second method of recording a

HIRE-PURCHASE ACCOUNTS. PAGE 10.
THIRD METHOD:
MACHINERY 0N HIRE-PURCHASE ACCOUNT.
R c
Jon. Machinery Co. 3 197 69 . 31 Depreciation E
Balance c/d
R3 a
1990
Dec. Balance 2 877 92 Depreciation
Balance c/d
1991
Dec. 2 590 13 . Depreciation
Balance c/d
1992
Dec. Balance 2 331 12 . Depreciation
Balance c/d
R2 331
1993
Dec. Balance 2 098 01 . Depreciation
Balance c/d
1994
Dec. Balance 1 888 21
NOTE: This Account is the some as under the Second Method.

Cash -
Deposit
Balance
MACHINERY COMPANY.
Mach. A/c
Interest Sus-
pense A/:
Balance
Balance
Balance

INTEREST SUSPENSE ACCOUNT.
1990
Jan. Mach. C0. Income Stat.
Balance c/d
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1990
Dec. Balance . Income Stat.
Balance c/d
His?
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1991
Dec. 1 Income Stat. 81
Balance c/d 84
R166
1992
Dec. Balance Income Stat.
Balance c/d
1998
Dac. Bulancn Income Stat.
Ila!
At Slut Documber, 1992, the Machinery would appear in the Balance
Sheet:-
Mochinery at cout (purchauod under Hire
Purchouo Agreement) R3 197,69
Lou: Aggregate Depreciation to date 866I57
R2 331,12
Loll Balance owing under agreement
R1 200,00
Lola Interest not accrued 84:35 1 115.65
R1 215,47

The figure of R1 215,47 is, of course, the same as that arrived at under the First method. Note how the balance owing under the agreement is deducted from the value of the asset, and not included with other creditors. This must be shown in the manner indicated for until the full amount of the instalments have been paid, the erogertx in the machinery has not passed. The hire-purchaser is sometimes said to have an "equity" in the subject of the agreement and R1 215,47 measures the value of the equity. It is only permissible to show this figure as an asset because the hire-purchaser intends to carry out the contract and pay all the instalments as they become due. If this is not his intention, if he only regards the contract as one of hire and does not intend to purchase the machinery, all instalments will be debited to Income Statement. This may occasionally happen, for there are certain classes of articles that cannot be hired in the normal way, and a hire-purchase agreement may be the only way for a person who wishes to use the articles, without purchasing them. Always, of course, the instalment under a hire-purchase agreement will be greater than a normal "hire only" charge.

The second or third method is much to be preferred to the first, because

(1) it is complete, and

(2) it is easier when computing depreciation.

Before continuing with this lecture, revise the text to this point. Make sure that you Fully understand all three methods of recording a Hire-Purchase in the buyer"s books.

Pay particular attention to the presentation of the Hire-Purchase Asset in the Balance Sheet.

l SELLER’S BOOKS i

Here there are three methods in general use.

FIRST METHOD:

This method is used when the hire-purchase transactions are on a large scale, but their number is small. A ledger account is opened for

each hire-purchoser, this account being debited with the cash-purchase price at the time the hire-purchase agreement is signed, and periodically debited with interest on the balance unpaid. The interest will be credited to Interest on Hire-Purchase Sales Account, and from there, at the end of the period, will be credited to Income Statement.
The H.P. sale is, in other words, dealt with as a cash sale and credited (with sales) to the Trading Account. Since the hire-purchaser may, however, discontinue the agreement at any time by handing back the goods to the seller, in whom the property is legally vested until the lust instalment is paid, the following special steps are usually taken in preparing the Balance Sheet of the Seller.
(1) Goods not paid For in the hands of hire-purchosers are shown as "Goods out on Hire-Purchose" on the assets side of the Balance Sheet. This figure will be the balance of the personal account of the hire-purchoser; it does not appear among Sundry Debtors.
(2) The whole of the profit on the sale has been taken into credit in the year the sale was effected. A provision should therefore be created to provide for losses which may result From the default of the purchaser. (If 0 question does not give specific instructions concerning the making of a provision, however, you should not make one).
EXAMPLE:
Taking the details of the example quoted on Page 3 of this Lecture you are required to record the transaction in the books of the Machinery Company.
LEDGER
GOLD MINING COMPANY
(here follow full details of the contract.) This is most important and must be shown on each H.P. Debtors Account).
Hire-Purchose
Sales
Interest
Cosh deposit
do.
Dec. Balance c/d

31 Balance
Interest
LEDGER
GOLD MINING COMPANY fCONTINUEDZ.
b/f
HIRE-PURCHASE SALES ACCOUNT

R 1990 R
Jan. 1 Gold Mining
R3 197 C0. R3 197
I’ll. IIIIIII

u

The Gold Mining Co’s Account is, of course, the exact reverse of the Machinery Company’s Account in the books of the Gold Mining Co. (under the second method).

In the some way the Seller’s Interest on Hire-Purchase Sales Account would carry the some figures, but on different sides, as the buyer’s Interest Suspense Account compiled under the buyer’s third method.

On Blst December, 1993, the Balance Sheet (Assets side) would show

Machinery out on Hire-Purchase R57l,43

Before continuing with this lecture, write up the Interest on Hire-Purchose Sales Account, as it would appear for the five years covered by this example.

SECOND METHOD:

If the hire vendor has numerous transactions each reegyoble over the some number of years, he can avoid separate interest calculations on each account by using 0 Hire Purchase Interest Acc0unt.

Under this method, which is the same as the third method explained under Buyers Book, except that the entries are on the reverse side of the account, the hire-purchaser is debited with the full price payable under the agreement.

Hire-purchose Sales Account is credited with the cash selling price.

Hire-purchose Interest Account is credited with the interest "loading".

The hire-purchoser’s account is cleared by the receipt of the instalments from him. Hire-Purchase Sales are transferred each year to Trading Account. There remains the Hire Purchase Interest Account to be considered.

In the previous example we noticed that the Machinery Company would receive interest of R402,31 over a period of 5 years. Each year’s interest bears the following proportions to the total:-

1990 R129,88 32,28x
1991 106,38 26,44%
1992 81,70 20,31%
1993 55,78 13,86%
1994 28,57 7,11%
R402,31 1oo,oo%

Now whatever the rice at which the articles are sold, where the agreement is spread over 5 years, with a deposit equal to the annual instalments and interest at 5% p.a., the annual interest charges will always be in the same proportions. With different interest rates and different numbers of instalments the proportions will be different, but the principle remains. We can, therefore, at the time when the contract is signed, take the interest loading of each transaction and apportion it over the years in which it will actually be earned (and credited to Income Statement). If the interest loading is R100, then R32,28 will be earned in the first year, R26,44 in the second year and so on. Each separate amount will be placed to the credit of a separate Hire Purchase Interest Account marked with the appropriate year, and as that year is reached, then the balance of the account will be credited to Income Statement.

There are, however, not many concerns in which all sales can-veniently take place on lst January, so that the first year can receive a Full year’s interest credit. In the absence of other information we must assume that the average date of all sales in the year is 30th June, so that the percentages must be re-allocated over six accounting periodsz- ___

lst period (assuming only 6 months interest due).
% x 32,28% : l6,l4%
2nd period % x 32,28% e % x 26,44% : 29,36%
3rd period % X 26,44% t % X 20,31% : 23,38%
4th period % X 20,31% t % X l3,86% : l7,08%
5th period % x 13,86% t % x 7,11% : 10,492
6th period % x 7,11% : 3:55%
1oo,oo%

%

As an example of the manner in which this works let us assume that an ageeement is entered into in 1990 on which the interest loading is R293 on a cash sale price of R2,310.

We debit the hire-purchaser with R2 603 and credit Hire-Purchase Sales with R2 310. The balance of R293 is credited over a number of Hire Purchase Interest Accounts in the above proportions. e.g., - "Hire Purchase Interest Account 1993" receives a credit of 17,685 of R293 (1993 is the M year, 1990 being the first) - R50,04. In 1993, the balance of this particular account, which includes the amount of R50,04, is credited to Income Statement.

The method is only appropriate where all contracts cover the same period of time.

The point to remember in using this system is that there will be a number of Hire-Purchase Interest Accounts open at any one time. The balance on each will be transferred to the credit of the Income Statement of the xear denoted bx the heading of the Hire-Purchase Interest Account.

THIRD METHOD:

The methods given above are rather elaborate ones and suitable only for large transactions. Where the transactions are numerous but small in value, a less elaborate system is usually employed. A Hire-Purchase Sales Journal is opened in which are recorded all the sales under hire-purchase agreement at cost Brice. A Hire-Purchose Ledger is also kept in which would be recorded the names of all the customers. Their accounts are debited with the full price of the goods, i.e., cash value plus interest, and the instalments credited when received. The balances shown by these accounts will, therefore, always show what is owing by each customer in respect of his hire-purchase. But this Hire-Purchase Ledger is merelx a Memorandum book and not Bart of the financial books of the concern. In the financial books, the total of the Hire-Purchose Journal is periodically posted to the debit of a Hire-Purchase Account, (and also to tho urodit of Hire-Purchase Sales Account), the latter being closed by transfer to the Trading Account, where they should be shown as a deduction from Purchases. Instalments received are periodically credited in total to the Hire-Purchose Account.

At balancing time, the stock in the hands of customers is token and valued at cost. The amount of such cost is then credited to the Hire-Purchose Account and brought down as an opening debit balance for the next period. The difference between the two sides 0? the Hire-Purchase Account will then represent the profit on tlc ere-purchose business and be transferred to the Income Statement.

The value of the stock out on Hire-Purchose is ascertained from the Memorandum Hire-Purchase Ledger and from the Hire-Purchase Soles Journal. Each personal account in the Memorandum Ledger shows the total number of instalments which has to be paid and the number which has actually been Raid. If the cost price of the item sold, as shown by the Hire-Purchose Sales Journal is multiplied by the proportion of instalments unpaid, the value of the Hire-Purchose Stock is given by the product.

Thus it the cost price of an article sold on Hire-Purchase Agreement is R10 and 3 of the 9 instalments have been paid, this article should be included in Hire Purchases Stock at (g x R10) : R6,67.

The following will help to fix in your mind the workings of an H.P. account.

HIRE-PURCHASE ACCOUNT

Stock in hand
of customers
(Instalments
(at cost) y for year)
Dec. 31 Hire-Purchase i Stock in
Sales for 1 hands of
year (at customers
cost) T (at cost)
Inc. Stat. I c/d
(Profit) 988 02
I
1--
R28 826 32
8 962liil
1990
Dec.
31 Balance b/f

In this system, all figures of Sales are purely memoranda, both in the Hire-Purchase Soles Journal and in the Hire-Purchose Ledger.

The Hire-Purchase Account is in effect a subsidiary Trading Account to which purchases (in the form of the cost values of the goods sold under Hire-Purchase terms) are debited, and the cash, from instalments paid, is credited.

After stock has been taken into account, the Hire-Purchase Account'will show a gross profit. This is composed partly of interest and partly of profit.

A slight extension of this method is often adopted to show a more accurate picture. Instolments actually due but remaining unpaid are really actual debit balances upon which profit has been earned. They are therefore credited to Hire-Purchase Account and debited to Debtors Account, and stock is then valued on the basis of instalments not yet due.

The individual debtors' accounts in the memorandum ledger are outside the normal double-entry. They will not appear on the Balance Sheet. From a double-entry point of view these accounts do not matter, but in fact they are of course most vital, and provide the only basis Upon which stock in the hands of hire-purchosers can be valued.

For reasons of space, the following example deals with four hire-purchcse transactions only. It is however, fully illustrative of the principles involved and should be studied carefully.

Examele.

The H.P. Hire Co. sells the following on hire-purchase terns:-

1989

Jon. 31 Furniture (cost price R70) to Mr. A.B. payable by 8 quarterly instalments of R12.

Feb. 28 Radio set (cost price R30) to Mr. C.D. payable by 4 quarterly instalments of R10.

Aug. 31 Second-hand car (cost price R300) to Mr. E.F. payable by 12 monthly instalments of R30.

Sep. 30 Second-hond lorry (cost price R300) to Mr. G.H. payable by 26 monthly instalments of R15.

In each case, the first instalment is due, as a deposit, on the signing of the agreement.

Solution:

H.P. Sale
Price
Memorandum
Date Articles
Cost Price
1989
Jan. 31 Furniture
Feb. 28 Radio Set 30,00
Aug. 31 Car 300,00
Lorry 300:00
Posted to credit of
Purchase A/c. and
debit of H.P. Account

MEMORANDUM HIRE-PURCHASE LEDGER.

A.B.
(address)
Articles under Agreement: (Furniture)
Cost Price: R70
8 quarterly instalments of R12 commencing 31/1/1989
H.P. Sales Price: R96

HIRE-PURCHASE ACCOUNTS. PAGE 22.
MEMORANDUM HIRE-PURCHASE LEDGER CONTINUED
1989 1989 R c
Jan. 31 H.P. Sales 23 Jan, 31 Cash 12 00
Apr. 30 do. 12 00
Jul. 31 do. 12 00
Oct. 31 do. 12 00
Dec. 31 Balance c/d 48 00
m 00
888
1990 1 -___ 1990
Jon. 1 Balance b/d in Jan. 31 Cash
Apr. 30 do.
Jul. 31 do.
Oct. 31 do. 12 00
um .00
Note the headings to the memorandum ledger accounts. The other accounts will follow similar lines. Practice writing them out.
PURCHASES ACCOUNT
Sundries
HIRE- PURCHASE ACCOUNT
1989 1989 1 R C
Dec. 31 H.P. Sales Dec. Cash (1n- 1
for year stallents ’
(at cost) 700 00 for year): R ’
Income A.B. 43
Statement C.D. 40 ’
(interest E.F. 150 .
etc. earned G.H. 60 i 298 00
for year) 61 85 Stock in ___’ !
hands of 1
customers c/d 463 85

HIRE-PURCHASE ACCOUNT SCONTINUEDZ
Stock b/d
Cash in-
DeC- 31 Income stolments
Statement For year: R
(interest A.B. 48
etc. E.F. 210
earned b.H. 180
for year) Stock ir___
hands of
customers c/d
1991
Jan. Stock b/H 31 ’Cosh (in9
Dec. Income stolments
Statement for year):
G.H.
CALCULATION OF VALUES OF "STOCK" AT 315T DECEMBER 1989.
Total No. of
Instalments
No. of Instalments
Un-aid at 31/12/1989
Frac-
tion
A.B. 4 35,00
C.D. nil (A/c. closed) -
E.F. 7 175,00
G.H. 22 253185
R463,85

CALCULATIOV OF VALUES OF "STOCK" AT 315T DECEMBER 1990.
nil (A/c. closed)
E.F. 12 nil (A/c. closed)
10
INSTALMENT-PAYMENT 30R DEFERRED PAYMENT! PURCHASES:
The fundamental difference between a hire-purchcse end an instal-ment-payment purchase is one of legal ownership. In the case of o Hire-Purchase Agreement, ownership posses only on payment of the final instalment, whereas, in the case of on Instalment-Poyment Purchase, ownership passes on delivery of the goods. Should a hire-purchaser fail to pay his instalments, the owner can re-take possession of the goods. Where a purchaser under the instalment-puyment system defaults in his instalments, however, the seller cannot re-toke possession of the goods; his only remedy is to recover the amount due by Court action.
ENTRIES IN THE BUYER’S BOOKS:
The Asset Account is debited with the cash value of the asset and the amount credited to the account of the vendor. The interest, when due, is debited to Interest Account and credited to the Account of the vendor. On payment of each instalment the Cash Account is credited and the vendor’s account debited. An Interest Suspense Account can also be used, and is, in fact, preferable as then the whole amount owing (Cosh Price plus Interest) is credited to the Vendor.
In other words, the entries are the some as those used by the Second or Third Methods of recording Hire-Purchase transactions in the Buyer’s Books, but the position is recorded in the normal way in the Balance Sheet,i.e., the balance due to the vendor is included in Sundry

Creditors, less the balance on Interest Suspense Account and the asset
is shown at its full cash value less aggregate depreciation to date.

ENTRIES IN THE SELLER'S BOOKS:

A Journal entry is put through debiting the purchaser and crediting
Sales Account with the cash value of the goods. As each interest charge
Falls due, a Journal entry is passed debiting the purchaser and crediting
Interest Account. On receipt of each instalment, Cash Account would be
debited and the account of the purchaser credited. Again on Instolment
Interest Account can be used in which case the Purchaser is debited with
the full price (Cash Price plus Interest), and the Instalment Interest
Account is written off proportionately each year to Income Statement.
In this case the book entries will be the some as those shOwn on
page 12 of this Lecture except that the first entry in the purchaser's
personal account will be "Sales .... R3 197,69" instead of "Hire Purchase
Sales ---- R3 197,69".

HIRE-PURCHASE ACCOUNTS.

Hire-Purchuse : article purchased does not become the property of
the buyer until the last instalment is paid.

Deferred Payment Purchase) : article purchased becomes the property
Instalment " ") of the buyer on delivery (unless
otherwise agreed).

HIRE-PURCHASE:

BUYER'S BOOKS:

Method 1: Dr. Interest --- Amount charged
for interest when each
)
)
Asset A/c -- proportion of) instalment due
cash price)
Cr. Supplier
Dr. Supplier . .
Cr. Cosh) when each instalment paid.

Cash value of the
Article purchased.
Method 2: Dr. Asset A/c
Cr. Vendor
Dr. Interest A/c Interest when due.
vv vv vv
Cr. Vendor
Dr. Vendor .
Cr. Cosh Instalments paxd.
Method 3: Dr. Asset A/c - Cash Value of Article
purchased.
Dr. Interest Suspense A/c - with total interest.
Cr. Vendor - Full Purchase Price, i.e.,
Cosh Price plus interest.
Dr. Vendor) . .- .
Cr. Cosh) with 1nstolments pald.
Dr. Income Statement) with annual proportionate
Cr. Interest Suspense A/c) amount of interest.
The Third is the method which is preferred, as full details of
transactions are in books of account.
SELLER’S BOOKS:
Method 1:
Dr. A/cs of various hire-purchasers) Hire-Purchase solos
Cr. Hire-Purchase Sales Account) from Hire-Purchose
) Sales Journal
(Later transferred to Trading A/c)
Dr. Customer) Interest on alount
Cr. Hire-Purchase Interest A/c) outstanding as each
)
instalment falls due.
(Later transferred to Income
Statement)
Provision should be made for possible uncompleted contracts.

Method 2:
Dr. Hire-Purchaser with Hire-Purchose agreement price.
Cr. Hire-Purchose Sales with cash selling price.
(Transfer to Trading Account).
Cr. Various Hire-Purchose Interest Accounts with Interest loading in previously computed proportions.
As each year’s accounts are prepared transfer the balance on the Hire-Purchase Interest Account marked with that year to Income Statement.
Suitable only when all agreements cover the some number of instalments.

Method 3:
Dr. A/cs. of various hire-purchosers in) Memorandum
Hire-Purchase Ledger with full price) onl
of the goods, i.e., cash value plus) -"-XL
interest.)
Dr. Hire-Purchase Account
Cr. H.P. Sales Account
Total Hire-Purchose Sales
from Hire-Purchase Sales
journal at cost price.
(Later transferred to Trading A/c
as a deduction from Purchases
. instalments received.
Cr. lee-Purchase Account
Cr. Hire-Purchase A/c. (Old period
Dr. H u M (New n
) Cost price of goods in hands
of customers at balancing time.
Dr. Hire-Purchase A/c.
Cr. Income Statement
Profit on Hire-Purchose
Soles.
)
)
)
)
)
Dr. Cash)
)
)
)
)
)

INSTALMENT PAYMENT PURCHASES:

Buzer’s Books:
Dr. Asset A/c) Cosh value of the article
Cr. Vendor) purchased

Dr. Interest A/c Interest when due.
Cr. Vendor
Dr. Vendor
Cr. Cosh
vv vv
Instolments paid.
Seller's Books:
Dr. Purchaser
f .
Cr. Sales A/c Cash value 0 the goods
Dr. Purchaser
t h n d .
Cr. Interest Interes w e ue
Dr. Cash
Cr. Purchaser
VV vv VV
Instalnents received.
Remember that the Interest Suspense Account can be used in both Buyer's and Seller's Books.
1.
CHECK QUESTION:
When Assets are purchased on a Hire-Purchose basis, the buyer can choose one of three methods of crediting the seller's account. Name these methods. If you cannog read the relevant part of this lecture again. Make sure you understand each point as it is raised; do not lightly pass over any port of the syllabus.
LIKELY EXAMINATION QUESTIONS:
On lst January, the Witwatersrand Gold Mining Co. obtained trucks on the hire-purchase system. The cash price of the trucks was R1 150. Payment was to be made, as to R150 down and as to the balance at R200 per year plus 5% interest on the outstanding balances. The Witwatersrand Gold Mining Company write off 10% depreciation each year.
You are required to write up the necessary Ledger Accounts in the books of the Witwatersrand Gold Mining Company.

__________.____________.____________
Apfel, Ltd., entered into a hire-purchose agreement on
lst January, 1990, with Bagsters, Ltd., for the purchase of
a fleet of motor cars. The agreement provided that on initial
deposit of R2 000 should be made, followed by 6 holf-yearly
instalments of R738,39 payable on 30th June and 3lst December.
The rate of interest charged is 6% p.0. with half yearly rests.
The cash value of the cars is R6 000.
Show the entries in the books of both parties, ignoring Journal
entries. Apfel, Ltd., write off depreciation at the rate of
8% p.a.
Dextrous, Ltd., sell goods on hire-purchose. All contracts
provide for 12 payments made quarterly over a period of three
years. Past experience has shown that the interest loading on
each contract may be allocated thus:-
1st year (covering 12 months from date of
contract) 52,4%
2nd year 33,9%
3rd year 13:7%
100,00%
Sales in 1990, 1991 and 1992 were respectively R12 000, R18 050
and R24 200. Interest loading may be reckoned at 7% on Sales
Price.
Show Hire Purchase Interest Accounts.

HIRE-PURCHASE ACCOUNTS. PAGE 30.
MODEL ANSWERS T0 LIKELY EXAMINATION QUESTIONS:
MODEL ANSWER TO QUESTION NO. 1:
- TRUCKS gON HIRE PURCHASE? ACCOUNT -
Year
1 Truck Co. Depn(10%
1 do on R1 150
4 Balance c/d
(Year
1 2 Balance Depn (10%
’ Truck Co. R1 035)
) Balance c/d
1
5
Year Y
1 3 Balance b/f 331 3 Depn. (10%
1 Truck Co. 200 R931 50)
I Balance c/d
?Year
) 4 Balance Depn. (10X
1 Truck Co. R838 35) 83 84
; Balance /d 554 51
s In
Year 7aw_w _A --
5 Balance
Depn. (10;
R754 51) 75 45
Balance /d 679 06
1 Truck Co.
) Balance
1

. ah.

MODEL ANSWER TO QUESTION N0. 1 gCONTINUED):
- TRUCK HIRE ACCOUNT. -
w t,"
Inc. Stat.
Inc. Stat.
Inc. Stat.
Inc. Stat.
Inc. Stat.
COMPANY -
Year: iR c Yeah
I 3 Truck Co. -__-?9499V 1
Year I i .
2 ’ Truck Co. ’ 40399u 2
Year I
3 Truck Co. 1 30:99" 3
Year
4 Truck Co. 20 00. 4
I .
Year E I
5 Truck Co. l 10 OO 5
- TRUCK
Year R c Year
1 150 00 l
250 OO
1-00
Year
2 _ 240 $51_ 2
Year
3 , ___.__ 3
Year I a
4 _ 220____ 4
Year a
5 5
I--I
NOTE:
Truck A/c
(Deposit)
Sundries
Sundries
Sundries
Sundries
Sundries
50 too
R i c
X
i 150 00
250 00
l R400 00
.00
In Example 1 in the Lecture you are given the total Boxments and the rate of interest and have to find the cash value.
In this question you are given the cash value and the rate of interest and you must calculate the total Eaxments.

HIRE-PURCHASE ACCOUNTS. PAGE 32.
MODEL ANSWER TO QUESTION NO. 2:
BOOKS OF APEL LTD.
BAGSTFRS LTD.
:r-zz-u ,_ -_._.__,-. "-1 9-11-791 "3-__,,----9-__,__-_ _____
1990 R c _1990 ’k
Jon 1 Cash
lDeposit 2 000100;
I
I
:June 30 - do _ 738 394 a/c 6 000 o.
3 Balance c/d 3 691 95: nterest 430
l
; R6 430 34! i ’R6 430
g :::::J::i I ._______
’ l
i
I
i
l 1
?Dec. 31 Cash J 738E397Ju1y 1
3’ JBolance c/d ’ 2 953156
,1 1 W194:
E1991 ’ I H1990 I
1June 30 Cash 738.39. Dec 31 EBolonce b/d .6
1 Balance :/d 2 215 171
R2,953156J ’ R2 953 56
:2b
,Dec 31 Cash
738 39 July 1 Balance b/d 2 215 17
Balance c/d
R2 215
I1991
738 39 Dec 31 Balance b/d 1 476 78
Bolche c/d .
’ R1 476 78II,R1 476
JUly 1 Balance b/d 1-H
1 1-9
.___. iii

MODEL ANSWER TO QUESTION NO. 2 CONTINUED :
MOTOR CARS ON HIRE PURCHASE ACCOUNT.
1990 ’ 1990 R _:V
Jan 1 -agsters
Ltd. 6 000 00 Dec Depn. 480 00
Balance c/- 5 520 00
I11 Inn
19913
1990 Dec Depn. . 441 60
Dec 31 Balance b/d 5 520 In Balance c/dl 5 078 40
um
1991 Dec .31 Depn. 406 27
Dec 31 :alance b/dl 5 078 40 Balance c/d 4 672 13
g l-5 078 40 ! I
I
1992 - ; I
Dec 31 Balance b/d 4 672l13M 1 I 1
HIRE-PURCHASE INTEREST ACCOUNT.
1..
1c
Q
1.
1990 R 1990
Jan 1 Bagsters
1 Ltd 430 Dec 31 Inc. Stat.
1 1 Balance
1 R430 I
1990 ’_"1991
Dec 31 Balance b/f 208 90 Dec
1
31 1Inc. Stat.
lBalance
R208 90’
1991
Dec 31 Balance b/f 63
4 __.
i I :1
i
1
19911
Dec;3l :Inc. Stat.
I
l
"Holf-yearly rests" means that interest is reckoned on the balance owing at the end of each hulf-yeor. It is necessary to balance Bugsters Account every six months, but there is no need to do so in the other accounts; in fact this would create confusion for depreciation is taken at 8% Bar onnum.

MODEL ANSWER TO QUESTION N0. 2 (CONTINUED):

The accounts in Bagsters, Ltd., books will be :-

1. Account for Apfel Ltd. This will be the reverse of Bagsters account in Apfel’s books.
2. Hire-Purchase Interest Account. This will be the reverse of the Interest account in Aptel’s books.
3. Hire-Purchase Sales Account;-

HIRE-PURCHASE SALES ACCOUNT.

MODEL ANSWER TO QUESTIONS N0. 3

We are given the interest allocations of each contract, but to don with the contracts as a whole, we must assume that the average date of sales was 30th June in each year. In this case, the year in whicl the sale took place can take credit for only i (6 months) of 52,4% of the interest loading.

The revised allocations ore:-

lst year % x 52,4% 26,2%
2nd year % x 52,4% t % x 33,9% 43,
3rd year % x 33,9% t i x 13,71 23,85
4th year i x 13,7% 6 9%
100,0%

MODEL ANSWER TO QUESTION NO. 3 (CONTINUED):
The interest loadings are:-
1990 7% of R12 000 : R840
1991 7% of R18 050 : R1263,50
1992 7% of R24,200 : R1694
The R840 in 1990 is allocated as to:-
26,2% i.e. R220,05 to Hire Purchase Interest A/c (1990)
43,1% " 362,00 do (1991)
23,8% " 199,90 do (1992)
6:9% " 57:95 do (1993)
1oo,0% R840,00
The other amounts are allocated in the some way.
Carefully check all the calculations.
HIRE PURCHASE INTEREST ACCOUNT (19902
_-____._.___._-_______.__
Debtors
(l990 Sale
t_vvv
_._______.___-_.
9 Dec 31 Income
Statement
’ c
362 00
331 04
l__ R693
R6-3 .04

____________.___________________
MODEL ANSWER TO QUESTION N0. 3 (CONTINUED):
HIRE PURCHASE INTEREST ACCOUNT $19922
The balance on this account will be transferred to Income Statement on 31/12/1993 when the 1993 Sales allocations have been posted to the appropriate accounts.
Ednrn-l u -.,

99wani3$i
HIRE-PURCHASE ACCOUNTS. PAGE 37.
MODEL ANSWER TO QUESTION NO. 3 gCONTINUED):
HIRE PURCHASE INTEREST ACCOUNT 1994
See note above. Transfer to Income Statement on 31/12/1994.
HIRE PURCHASE INTEREST ACCOUNT (1995)
31 Sundry
Debtors
(1992 Sales
8256

LEASE ACCOUNTS

A. INTRODUCTION

Leasing of assets can be divided into two categories: finance leases and operating leases.

(We will only be looking at the books of the lessee).

1.

FINANCE LEASES:

A finance lease is a lease that transfers substantially all the risks and rewards associated with ownership of an asset from o lessor to the lessee, without passing of the actual ownership.

OPERATING LEASES

An operating lease is a lease other than a finance lease, in which the risks and rewards associated with ownership of the asset remain with the lessor.

i.e.: Entering into 0 lease agreement for use of on office can be regarded as on operating lease.

ACCOUNTING PROBLEMS AND TREATMENT OF ABOVE LEASES

(0) Determining of the lease is a finance or operating lease.

(b) If the lease is a finance lease, deciding whether the leased asset should be capitalised or not.

(c) If the lease is capitalised, making the appropriate accounting entries and disclosures in the financial statements.

(d) Defferred taxation.

(e) Sale and lease back agreements.

B.

DETERMINING IF A LEASE IS A FINANCE LEASE

When making this type of decision it is important to consider the substance of the transaction rather than the form of the transaction.

Any one of the following conditions would indicate that a lease is a finance lease:

1. At the end of the lease term the lease provides for transfer of ownership from the lessor to the lessee.
2. The lessee has the option to buy the asset, the price payable being significantly less than the open market value of the asset i.e. bargain option.
3. The lease term is for most of the useful life of the asset. Use of the asset for more than 75% of the assets useful life would normally indicate a finance lease.
4. The present value of the inception of the lease, of the minimum lease payments, adjusted for any actual or estimated tax benefits therefrom, approximates or exceeds the open market value of the leased asset at the inception of the lease.

C. CAPITALISATION OF FINANCE LEASES t

In South Africa it is not mandatory to capitalise finance leases. Preparers of financial statements have the option of either capitolising or not capitalising. However once a decision is made as to either capitalising or not, it must be consistently applied.

It would be incorrect to capitalise certain finance leases and not others.

CAPITALISATION:
Those in favour of this treatment consider a lease as a finance arrangement which is no different from any others purchase of an asset, and as the lessee bears all the risks and rewards of ownership it would be incorrect not to show the asset in the balance sheet of the entity.
NOT CAPITALISING
Those in favour of this treatment argue that the asset should not be capatolised as ownership does not pass from the lessor to the lesee. The annual lease payments are written off to the profit and loss account. The Companies Act requires the amount of such lease payments to be disclosed separately in published financial statements.
HOW TO CAPITALISE FINANCIAL LEASES
The journal entries are as follows:
Stee 1: Raise the leased asset as an asset and the present value of lease payments as a corresponding liability.
Dr Fixed assets XXX
Cr Long term liability XXX
SteE 2: Allocate periodical lease payments between interest and capital.
Each lease payment can be divided into on interest portion and a capital portion. There are generally two methods of determining the split between interest and capital, namely the sum of the digits method and the effective interest rate method.
(0) Sum of the digits method
This method is easy to apply, and works as follows:

_________________._____.
therefore the total interest charge is allocated on the sum of the digits of all lease payments and weighted to earlier periods.

Exam le 1.

A.leases plant with a cost of R400 000. A. will make 4 payments of R125 000 each. Prepare a schedule showing the allocation of lease charges between capital and interest.

SOLUTION

Stee 1: Determine the total finance charges involved in the lease.

Cost of asset R400 000
Sum of lease Payments (4 x 125 000) R500 000
finance charges : R100 000

SteE 2: Determine the sum of the digits and weighing.

4 Payments 5. sum of the digits is (4 e 3 t 2 t l) 10.

Allocation:-

Payment 1 78
2 1-8
3 T62
4 %

Stee 3: Allocate by preparing a schedule.

Payment Capital Interest Total
500 000
1 125 000 (125 000191-61 x 100 000)
375 000; 3
2 125 000 (125 000)! (To_ x 100 000)
250 0001 2
3 125 000
(125 000)i (W x 100 000)
125 000 3 1
l (125 00011 (W x 100 000)
(b) Effective interest rate method
On this method the apportionment between capital and interest is done using the effective interest rate implicit in the lease agreement.
SteE 4: Depreciate the capatolised leased asset.
Journal entry.
Dr Depreciation XXX
Dr Accumulated depreciation
on capitalised leased assets XXX
SteE 5: Transfer current portion of lease payments to a current liability. Note: only the capital portion will be transferred.
Dr Long term liability XXX
Cr Current liability XXX

Stag 6: Make provision for different taxation: if a
timing difference arises bet
allowances.
Dr Taxation
Cr Taxation
Deferred
D. SUMMARY OF JOURNAL ENTRIES
(1)
(2)
(3)
(5)
Raise asset and liability.
Dr fixed asset
Cr long term liability
Allocate Payments
Dr long term liability
Dr Interest charge
Cr Bonk
Provide depreciation
Dr Depreciation
Cr Accumulated depreciation
Provide for deferred tax on
timing differences
Dr or Cr Taxation
Dr or Cr Deferred taxation
Make closing entries
Dx Profit and loss account
C In erest charge
Transfer portion of capital
payable during the current
year as a current liability
Dr Long term liability
Cr Current liability - curr nt
portion of capital payable
ween accounting and taxation
XXX
XXX
XXX
XXX
XXX
XXX
XXX
XXX
XXX
XXX
XXX
XXX
XXX

E. SUMMARY OF DISCLOSURE REQUIREMENTS
1. ACCOUNTING POLICIES
(0)
(b)
(C)
Statement concerning treatment of finance leaser whether copotalised or not.
Statement concerning allocation of lease payments: payments between capital and interest if lease is capotalised.
(i.e. sum of the digits or effective interest rate method)
Statement of long term liabilities.
2. INCOME STATEMENT
(a)
(b)
(C)
(d)
(e)
finance lease capitalised.
Depreciation on capitalised leased assets.
Finance income charges.
Finance lease not capitalised.
Total lease payments made under finance leases.
3. BALANCE SHEET
(0)
(b)
(c)
(d)
(e)
Finance lease copatalised.
Fixed assets appropriately described.
Long term liabilities appropriately described.
Current liability! lease payments payable during the current year.
Accumulated depreciation on copatolised leased assets.
Finance lease not capatolised.
There will be no assets raised in the books and no corresponding liability.

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A
(f) A: a note to tho balance shnot, stat. commitments on finance looses payable during the current your, and then commitments payable thereafter. s

F. TAXATION AND DEFERRED TAXATION

l. The losses will be able to claim the loose payments as a deduction.

2. The lessor will receive all the wear and tear and initial allowances on the plant.

3. When a finance lease is capatolisod a dofcrrod tax problem will arise. The lessee will depreciate the fixed asset and charge the interest portion of tho loose payments to tho incomc statomont. Tho rocoivor of rovonus will grant the loose payments as a deduction. Often a timing difference will arise and deferred tax should be provided.

In the above circumstances if a doforrod tax chargo results in a debit balance it would be appropriate to show a deferred tax account as a dobit.

0. SALE AND LEASEBACK

This is a type of loose agrosmont whoroby the owner of an asset sells it to a buyer, normally a financial institution, and immediately looses it back from the financial institution.

A. Limited sells a building to financo company.
(Seller) (Buyer)
Finance company looses building to A. Limitsd.
(Lessor) (Lessee)

Often the selling price and lease payments are determined by the parties and may not equate the fair market value of the property.
Generally a asset once it is sold to the lessor becomes an operating lease, and therefore, should not be copotolised. However, if the selling price of the asset or the lease payments are not realistic, these should be adjusted to satisfy the matching concept.
1. SALE AND LEASE BACK WHERE THE LEASE BACK IS A FINANCE LEASE
With this type of transaction certain accounting problems will arise:
(o) The profit on the sale of the plant i.e. the difference between the proceeds and the book value should be deterred and allocated to the income statement over the lease term.
(b) Deferred tax problems will arise, as the sole of the asset may result in a taxable recoupment, furthermore the lessee will now be able to deduct the lease payments for taxation purposes and will no longer receive the wear and tear allowances.
H. WORKED EXAMPLE
0n 1 January 19 x 0 A. Limited a company involves in the manufacture of Plastic mouldings leases on item of plant costing R500 000 from a finance company. A. Limited will make 4 annual payments of R175 000 commencing on 31 December 1980.
At the end of the lease term A. Limited has the option to buy the item of plant for a nominal charge.
It is the policy of A. Limited to copatalise leases that are finance leases.

A. Limited depreciates plant at a rate of 25% per annum on the straight line basis.
The interest charged is to be allocated on the sum of the digits method.
During X0 A Limited earned a net income of 500 000, before taking into account depreciation on this item of plant, and before finance charge on leased assets.
During X1 the company earned income of R600 000 before depreciation and interest on finance charges.

1. REQUIRED:
(0) Prepare the journal entries to take into account the above transactions for the years X0, X1.
(b) Show how the above items would be disclosed in the income statement and balance sheet of the company for X0, and X1.

2. SOLUTION:
(a) Stee 1:
Determine if the lease is a finance lease:
(i) The question states that A. has a option to buy the machine at a nominal rental at the end of the lease agreement.
(ii) The life of the asset is 4 years and the lease term is 4 years, thus the asset is leased for all of the useful life period of the asset.
(iii) The present value of the lease payments approximates the cost of the asset.

All three of the above factors clearly indicate that
the above lease is a finance lease.
(b) Stee 2:
If the lease is a finance lease, decide whether this
lease is to be capitalised or not.
The question states that it is company policy to
capotolise leases that are finance leases.
(c) Stee 3:
Determine the allocation of lease payments between
capital and interest.
Cost of assets R500 000
sum of lease payments
(4 x 175 000) R700 000
lease finance charges 200 000
Allocation of interest on sum of the digits method.
Payments Net Cost Interest 1 Gross Cost
500000 200000 ,700000 A
1- 175000 95000 (1)80000 1 175000 (1)10X200000
405000 120000 1525000 3
2- 175000 115000 (2)60000 1 175000 (2) szooooo
290000 60000 350000 2
3- 175000 135000 (3)40000 175000 (3)Wx200000
(4) TO_X 200000
155 000 20 000 175 000
155 000 (4) 20 000 175 000
NIL NIL NIL
Determine the tax implications of the above transactions
and provide for deferred taxation.
(d) SteE 4.

A. Limited will receive no wear and tear allowance on the loosed asset they will be allowed to deduct the lease payments.
As A. Limited has capitalised this asset for its income statement purposes it will deduct depreciation and lease finance charges.
Clearly a timing difference will arise, this must be determined and deferred tax provided.
Tax calculations.
X0 XI
Income 500 000 600 000
Deduct: Lease
chargers (175 000) (175 0002
Taxable income 325 000 425 000
Tax at 50% 162 500 212 500
Accounting profit
X0 XI
Income 500 000 6a) G1)
Depreciation
(500 000 - 25X) (125 000) (125 000)
lease interest g 80 0002 S60 0002
295 000 415 000
Tax a 50% 147 500 207 500
Tax actual 162 500 212 500
Defferred tax 150 000 5 000

Step 5 : less the appropriate journal entries.
(i)
(ii)
(iii)
(iV)
(vi)
(vii)
Dr Plant 500 000
Cr Long term liability 500 000
(capitolising plant leased and raising the present
value of lease payments as a long term liability).
Dr Long Term Liability 95 000
Dr lease finance charges 50 000
Cr Bank 175 000
(Payment of annual lease charge and allocation of
payment between interest and capitol. Refer to Step 3)
Dr Depreciation 125 000
Cr accumulated depreciation 125 000
(Depreciation on plant capitalised
500 000 x 25%)
Dr Taxation 162 500
Cr Receiver of Revenue 162 500
(Taxation charge for the year based on actual liability
to the Receiver of Revenue. Refer to step 5)
Dr Deffered Taxation 15 000
Cr Taxation 15 000
Provision for deferred taxation on timing differences
between accounting charges and tax deductions.
Refer to Step 5.
Dr long term liability 115 000
(Transfer of capital portion of lease payment payable
during X1, to a current liability as this portion of
the liability is payable during the current year.
Dr Trading account 500 000
Cr Depreciation 125 000
Cr lease finance charges 80 000
Ct Taxation 147 500
Cr Retained income 147 500

(Closing entries transferring trading profit and deducting relevant charges.
(a) Journal entries for 19XI

---

(1) Dr current liability 115 000
Dr lease finance charges 60 000
Cr Bank 175 000
(Payment of annual lease charge and allocation between capital and interest)
(ii) Dr Depreciation 125 000
Cr Accumulated depreciation 125 000
(Entry iii 19x0)
(iii) Dr Taxation 212 500
Cr Receives of Revenue 212 500
(Refer to entry (iv) 14X0)
(iv) Dr Deferred taxation 5 000
Cr Taxation 5 000
(Refer to entry (v) 19X0)
(v) Long term liability 135 000
Cr Current liability 135 000
(Refer to Note (vi) 19X0)
(vI) Trading account 600 000
Depreciation 125 000
Lease finance charges 60 000
Taxation 207 500
Retained income 207 500
(Refer Note (vii) 19X0).

’ "W’TWW
(f)
LEASE ACCOUNTS. PAGE 15.
Income statements
X0 X1
Net Income 295 000 415 000
Taxations 147 500 207 500
S.A. Normal tax 162 500 212 500
Deferred (15 000) (5 000)
147 500 207 500
Net Income for --_- _-_-
the year 147 500 207 500
Notes to the income statement.
Income has been calculated after tokin into account
the following items:
Depreciation on capitalised
leased assets
125 000 125 000
finance charges
on leases assets 80 000 60 000
Balance sheet items
Caeitol emeloxed X0 X1
Deferred taxation (15 000) (20 000)
Long term liability
under capatilsed finance 210 000 155 000
Emeloxment of caeital
Fixed assets
capitalised leased assets
at Net book value 375 000 250 000

Current assets
Current liabilities
Receiver of Revenue I62 500 212 500
Current Portion of long term
liability payable 115 000 135 000
Notes to the balance sheet.
Fixed assets
Copitolised leased assets
Cost
Accumulated depreciation
I. EXAMPLE
X Limited leases on item of plant from Y Financing Limited. The cost at this plant is R100 000 and has a useful life of 5 years. X Limited will make five annual payments of 25 000 each.
The inception date of the lease is 1 January X0. The first lease payment will be made on 1 January X0. Use the sum of the digits method to allocate the finance charges.
X Limited will depreciate the asset on a straight line basis of a rate of 20% per annum and it is the policy of X Limited to capitalise finance leases.
1. REQUIRED: prepare journal entries for the years X0, X1 ignore closing entries.

(0)
(d)
(e)
2. WORKINGS
LEASE ACCOUNTS.
Journal entries
X0
Cr
Capitalised leased assets
Long term liability
Long ter
Bonk
m liability
Depreciation
Accumulated depreciation
PAGE 17.
100 000
25 000
20 000
on copotalised leased assets
Deferred
Taxation
taxation
Long term liability
Interest
Current
expense
liability
1 667
16 667
8 333
100 000
25 000
20 000
1 667
25 000
This current liability is made up of the capital portion
of the lease payments payable on the 1 January X1 and
the accrued interest.
Finance charge allocation
5 year lease
Yr
1
2
_n .1 _. _. _.
UI-I UlNUIQUI$UIU1
fifteen
Cost
Payments
5 x 25 000
lease finance
charges
100 000
M
25 000

-_ -
LEASE ACCOUNTS. PAGE 18.

Notes: In this question the first payment is made on the day the lease is signed.

Payments Interest
25 000
2 12x25C00
3 4 x 25 000
15

Deferred tax workings.

X0

Accounting Taxation
Depreciation 20 000 Lease payments 25 000
finance charges 8 333
28 333 25 000

Accounting deductions exceed tux allowances by 3333 therefore, at a tax rate of 50% this is 1667.

X1

Accounting Taxation
Depreciation 20 000 Lease payments 25 000
finance charges 6 667
26 667 25 000

Accounting deductions exceed tax allowances by 1667 at a taxation of 50% the transfer to deferred tax is 833.

LEASE ACCOUNTS. PAGE 19.
2. Journal entries X1
(0)
(b)
(d)
15 442
Dr Current liability
Cr Bank
Dr Depreciation
Cr Accumulated depreciation
Dr Long term liability
Dr Interest expense
Cr Current liability
Deferred tax
Taxation
25 000
20 000
19 333
6 667
833
25 000
20 000
25 000
833

T H E R A P I D R E S U L T S C O L L E G E
FINANCIAL ACCOUNTING
TEST ACQZ
(Time allowed : 1 1/2 hours)
-------- oOo--------
NOTES:
1. Credit will be given for neatness and method.
2. Answer all questions.
3. Scale of marks is indicated at the end of each question.
4. Leave sufficient space at the head of your answer paper for tutor’s comments.
5. Answer each question on a segcrate sheet of paper.
6. Attach this entire question paper to your answers.
7. PLEASE FILL IN STUDENT DETAILS ON THE FORM AT THE ELD 0F TkIS TEST AND ATTACH IT TO YOUR ANSWERS.
-------- oOo--------
QUESTION 1.
Toolmakers Limited buys machinery on Hire-Purchose from Lathe Supplies Ltd. The Cash Price of the purchase is R2 131,79. Under the Hire-Purchose terms.Toolmakers must pay an initial deposit of R400 (On 1/1/1990) and thereafter five equal payments of R400 at the end of each calendar year.
The interest position of these five instalments will be:_
R86,59; R70,92; R54,47; R37,19; R19,04.
(0) Using the Interest Suspense Account method, show the following Accounts in Toolmakers Limited books for the period 1/1/1990 31/12/1994.

1. Lathe Supplies Limited
2. Interest Suspense Account
(b) Show how this machinery would be presented on the Balance Sheet of Toolmakers Limited as at 31/12/1991, assuming that the aggregate depreciation of the machinery to that date was R405,04.
(25 marks)

QUESTION 2.

Transport Contractors (Pty) Ltd. acquired on hire-purchase, a large diesel lorry with trailer on the following terms:-
1. An initial payment of R4 000 due on or before delivery.
2. Four half-yearly payments of R3 000 each, commencing six months after date of delivery.

In arriving at these terms the supplier computed interest (to the nearest Rand) at 6% per annum with yearly rests, i.e. interest for each current year was calculated onthe capital amount outstanding at the beginning of the year, without any credit for interest on the instalment paid during the current year.
Delivery was effected on 1st July, 1979.
Transport Contractors (Pty) Ltd. provides for depreciation at an annual rate of 20% on cost.
Your are required:-
(0) to show the accounts in the books of Transport Contractors (Pty) Ltd. for the two years ended 30th June, 1981, recording the above transaction; and
(L, to show how the relevant items would appear in the balance sheet of Transport Contractors (Pty) Ltd. as at 30th June, 1980.
(25 marks)
(TOTAL : 50 MARKS).

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