Accounting 100

Depreciation

Depreciation- the process of allocating to expense the cost of a plant asset over its useful life.

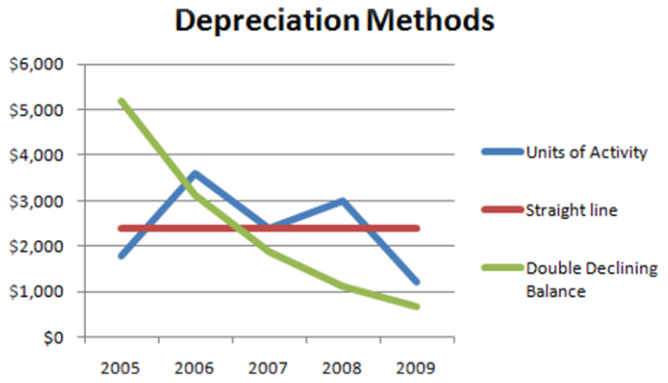
There are three types of plant assets: land improvements, buildings, and equipment.

Depreciation Methods

1. Straight-line

2. Declining-balance

3. Units-of-activity



1. **Straight-line-** an equal amount of depreciation is expensed each year of the asset's useful life.

Cost $13000

Expected Salvage Value $ 1000

Estimated Useful Life 5

Estimated Useful Life (in miles**)** 100,000

Cost - Salvage Value = Depreciable Cost

$13000 - $1000 = $12000

Depreciable Cost / Useful life = Depreciation Expense

$12000 / 5 = $2400

Depreciation rate= 100% / 5 years = 20%

Accumulated Depreciation- Depreciation taken throughout the useful life of an asset is accumulated in this account

	Computation					End of Year	
Year	Depreciable Cost	X	Depreciation Rate	=	Annual Depreciation	Accumulated Depreciation	Book Value
2005	$12,000		20%		$2,400	$2,400	*$10,600
2006	$12,000		20%		$2,400	$4,800	$8,200
2007	$12,000		20%		$2,400	$7,200	$5,800
2008	$12,000		20%		$2,400	$9,600	$3,400
2009	$12,000		20%		$2,400	$12,000	$1,000
				Total	$12,000		
*$13000	-	$2,400					

Book Value- the difference between the cost of any depreciable asset and its related accumulated depreciation

2. Declining Balance- computes periodic depreciation using a declining book value. It results in more depreciation in the early years of an asset's life than does the straight-line approach. The most common is the **double declining balance method** in which the depreciation rate is double the straight line method. Do not subtract salvage value.

Depreciation Rate = 2 X Straight- line Depreciation Rate

Depreciation Rate = 2 X 20% = 40%

Cost X Depreciable Rate = Annual Depreciation Expense

$13000 X 40% = $5200

	Computation					End of Year	
Year	Book Value Beginning of Year	X	Depreciation Rate	=	Annual Depreciation	Accumulated Depreciation	Book Value
2005	$13,000		40%		$5,200	$5,200	*$7800
2006	$7,800		40%		$3,120	$8,320	$4,680
2007	$4,680		40%		$1,872	$10,192	$2,808
2008	$2,808		40%		$1,123	$11,315	$1,685
2009	$1,685		40%		**$685	$11,315	$1,000
*$13000	minus	$5,200					

** Computation of $674 ($1685 X 40%) is adjusted to $685 in order for book value to equal salvage value.

3. Units-of-Activity- useful life is expected in terms of the total units of production or the use expected from the asset. The units- of- activity method is ideally suited to equipment whose activity can be measured in units of output, miles driven, or hours in use.

Depreciable Cost / Total Units- of- Activity = Depreciation Cost per Unit

$12000 / 100,000 miles = $0.12

Depreciation Cost per Unit X Units- of- Activity during the Year = Depreciation Expense

$0.12 X 15000 miles = $ 1800

	Computation					End of Year	
Year	Units of Activity	X	Depreciation Cost/Unit	=	Annual Depreciation	Accumulated Depreciation	Book Value
2005	15000		$ 0.12		$1,800	$1,800	*$11200
2006	30000		$ 0.12		$3,600	$5,400	$7,600
2007	20000		$ 0.12		$2,400	$7,800	$7,200
2008	25000		$ 0.12		$3,000	$10,800	$4,200
2009	10000		$ 0.12		$1,200	$12,000	$1,000
*$13000	minus	$1,800					