

Depreciation 2,436

Balance sheet:

Show the accumulated depreciation as a deduction from cost, resulting in the Net Book Value (Carrying amount)

Balance Sheet (year 1)

| | | |
|--------------------|-------------------|---------|
| Non current assets | | £ |
| Motor vehicles | Cost | 10,000 |
| | Less depreciation | (2,436) |
| Net book value | (NBV) | 7,564 |

Balance Sheet (year 2)

| | | |
|--------------------|-------------------------------|---------|
| Non current assets | | £ |
| Motor vehicles | Cost | 10,000 |
| | Less accumulated depreciation | (4,872) |
| Net book value | (NBV) | 5,128 |

b) Reducing balance method

- Deducts a **fixed percentage** from the **net book value each year** (this is the cost / fair value in the first year and cost less accumulated depreciation in subsequent years)
- This means higher depreciation charges in earlier years and lower charges in later years

$D = (1 - \sqrt[n]{S/C}) \times 100\%$

Where D = depreciation percentage

n = useful life of asset in years
 S = scrap (residual) value of asset
 C = cost or fair value of asset

$D = (1 - \sqrt[4]{S/C}) \times 100\% = (1 - \sqrt[4]{56/10,000}) \times 100\% = 66 \text{ or } 60\%$

Depreciation applied to each of the 4 years:

| | |
|--|------------|
| Cost | £10,000 |
| Year 1: Depreciation charge 60% x cost = | (6,000) |
| Carrying amount | 4,000 |
| Year 2: Dep'n charge 60% x carrying amount | (2,400) |
| Carrying amount | 1,600 |
| Year 3: Dep'n charge 60% x carrying amount | (960) |
| Carrying amount | 640 |
| Year 4: Dep'n charge 60% x carrying amount | (384) |
| Carrying amount | <u>256</u> |

Comparison

(e.g. C = 1000; N = 3 years; S = 125)

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Straight line:
 $D = (C - S)/N$
 $= (1000 - 125)/3 = 292$

| | | |
|--------|-----|------------|
| | D | NBV |
| t_0 | | 1000 |
| Year 1 | 292 | 708 |
| Year 2 | 292 | 416 |
| Year 3 | 292 | <u>124</u> |
| | | 876 |

Reducing balance:
 $D\% = (1 - \sqrt[N]{S/C}) \times 100$
 $= 50\%$

| | | |
|--------|-----|------------|
| | D | NBV |
| t_0 | | 1000 |
| Year 1 | 500 | 500 |
| Year 2 | 250 | 250 |
| Year 3 | 125 | <u>125</u> |
| | | 875 |

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