

AS-6 : Depreciation Accounting

- 1) This accounting standard is applicable to all entities.
- 2) This standard deals with depreciation and applicable to all depreciable asset.
- 3) This AS is not applicable to following assets.
 - a) Forests, plantations and other similar regenerative natural resources
 - b) Wasting assets like mines, oil exploration etc.
 - c) Expenditure on Research & Development (Intangible assets)
 - d) Goodwill
 - e) Live stock
 - f) Land - unless having limited use.

4) Depreciation

Depreciation is a measure of wearing out, consumption or other loss of value of depreciable asset arising from use, effluxion of time or obsolescence through technology and market changes. (As per Para 3 of AS-6)
or in other words

Depreciation is provision for replacement of asset.

5) Depreciable asset :

- a) Is an asset which is expected to be used for more than one year
- b) having limited useful life
- c) held by enterprise for production of goods, rendering of services or for administrative purpose.

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Class Notes

<u>e.g</u>	Particulars	Life more than one year	Limited Life	Used for Production etc	Depreciable Asset/net
	Machine	yes	yes	yes	yes
	Computer	yes	yes	yes	yes
	Land	yes	No	N/A	No
	Building	yes	yes	yes	yes
	Debtors recoverable after 2 years	yes	yes	No	No
	Stock of flats	yes	yes	No	No

Useful life : Is either the period over which a depreciable asset is expected to be used by enterprise or The number of production or similar units expected to be obtained from use of asset

Depreciable amount :

= Cost of asset (Historical or revalued)	x x x
Less: Residual value	<u>x x x</u>
∴ Depreciable amount	<u>x x x</u>

Notes Cost of asset will be determined as per AS-10 (Fixed Assets)

Notes: Useful life of asset is normally shorter than its physical life.

Notes: Some times useful life may be determined by a law or contract.

Notes: Useful life is a matter of estimation.

5) changes in useful life

If useful life of asset is revised then depreciation amount will be revised prospectively.

e.g. original cost of asset ₹ 10,00,000
original estimated life 10 years
Method of depⁿ SLM.

After 2 years it was estimated that asset can be used for 4 years further compute original amount of depⁿ and revised amount of depⁿ.

Ans

a) original amount of depⁿ = $\frac{10,00,000}{10 \text{ yrs}}$ = ₹ 1,00,000

b) Computation of revised amount of depreciation.

WDV of asset after 2 years 8,00,000
[10,00,000 - 2,00,000]

Remaining useful life 4 years
Revised depⁿ ($\frac{8,00,000}{4}$) ₹ 2,00,000.

6) Residual value: Is the amount which can be recovered after its useful life by way of Sale or scrap.

Notes If residual value is insignificant then it can be considered as nil.

Note: Some times residual value may be determined by law e.g. in Sch-II of Co's act 2013 it is mentioned that residual value of building will be 5% of cost.

7) Method of depreciation

Methods recommended by AS - 6 are .

a) Straight line method (SLM)

$$\text{Dep}^n = \frac{\text{Cost of asset} - \text{Residual value}}{\text{Life of asset}}.$$

b) Reducing balance method. (WDV method).

$$\text{Rate of dep}^n \text{ as per WDV method} = 1 - \left(\frac{R}{C}\right)^{\frac{1}{\text{Life}}}$$

Where $R =$ Residual value
 $C =$ Cost of asset

e.g	Cost of asset	₹ 1,00,000
	Residual value	₹ 10,000
	Useful life	4 years.

Ans Rate = $1 - \left(\frac{10,000}{1,00,000}\right)^{\frac{1}{4}} = 1 - (0.10)^{\frac{1}{4}} = 1 - 0.5623$
 $= 0.4377 \text{ or } 43.77\%$

8) Method of selection

Depreciation should be charged in ratio of benefit that is expected to arise from the use of asset

Situation 1 : If benefits will be more in initial years and less in later years

Appropriate method of charging depreciation should be WDV method as under this method depreciation will be more in initial years & will be less in later years.

Situation 2 : Benefits will remain same throughout the life
Straight line method should be used for computing depⁿ.

9) change in method of depⁿ

- a) Method of depreciation once selected should be consistently applied
- b) Method of depreciation can be changed if.
 - i) It is required by law
 - ii) It is required by AS
 - iii) If it is considered that such change would result into more appropriate preparation or presentation of financial statement.
- 10) Change in method of depⁿ is treated as change in accounting policy and change in accounting policy are accounted for with retrospective effect

- 11) Depⁿ will be recalculated in accordance with new method and
- If there is surplus / deficiency then treatment should be given in P & L acc
 - If surplus — Credit to P & L acc
 - If deficit — Debit to P & L acc

12) Change in other factors

a) Change in historical cost

- Depreciation is calculated prospectively over the residual useful life.

b) Change in useful life

Unamortised depreciation is charged over revised remaining useful life of asset.

c) Addition or extension to fixed asset

Calculate depreciation at the same rate over remaining useful life.

13) Disposal or Retirement of asset (AS-10)

If fixed assets are retired from active use and held for disposal then they are stated at lower of

- a) Net book value or
- b) Net realisable value.

Note: Such fixed assets are shown separately in financial statements and any loss expected on disposal is immediately recognized in P & L acc

Note: If there is expected gain it will not be recognized.

- 14) When fixed asset is disposed off then that item of fixed asset will be eliminated from financial statement and gain/loss will be recognized in P&L acc.

Journal entry

Cash/bank acc

P & L acc

To Fixed Asset acc

To P & L acc

Dr (Sale value)

Dr (Amount of loss)

(Net book value)

(Amount of Profit).