



All-In-One Aspirant Hub ★

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5 Depreciation

1. Meaning & Concept

Depreciation is the systematic allocation of the cost of a depreciable asset over its estimated useful life. It reflects wear and tear, passage of time, obsolescence, or consumption of the asset's value.

Depreciable assets are those:

- Used over more than one accounting period
- With limited useful life
- Held for production, supply, rental, or administrative purposes—not for sale.

2. Objectives of Providing Depreciation

1. Correct Income Measurement - Ensures accurate profit determination.
2. True Position Statement - Presents fixed assets at realistic values.
3. Funds for Replacement - Helps accumulating replacement funds.
4. Cost of Production - Helps reflect true cost of production.

3. Factors in Measurement

- Cost of Asset: Includes purchase price plus installation, freight, insurance, etc.
- Estimated Useful Life: Based on years, usage hours, production units, etc.
- Residual/Scrap Value: Estimated realizable value at the end of useful life.
 - Depreciable amount = Cost - Residual Value.
- Others: Repairs and renewals, obsolescence, legal provisions (e.g., Companies Act, Income Tax Act).

4. Methods of Depreciation

Straight Line Method (SLM)

Depreciation = $(\text{Cost} - \text{Residual Value}) \div \text{Useful Life}$.

Charges equal depreciation every year.

Written Down Value (WDV) Method

Depreciation = Book Value at beginning \times Depreciation Rate.

Depreciation decreases each year.



Formula to find rate:

$$r = (1 - (\text{Residual Value} \div \text{Cost})^{(1/n)}) \times 100\%$$

where n = useful life.

Sum-of-Years'-Digits (SYD) Method

Depreciation = (Cost - Residual Value) × (Remaining Life / Sum of digits of total life).

First-year weight is highest, then declines. (Not widely used in India.)

5. Accounting Entries

(A) Direct Method	Depreciation A/c Dr To Asset A/c Profit & Loss A/c Dr To Depreciation A/c
(B) Provision Method	Depreciation A/c Dr To Provision for Depreciation A/c Dr Profit & Loss A/c Dr To Depreciation A/c

6. Sale of Asset & Disposal

Bank A/c	Dr
Provision for Depreciation A/c	Dr
To Asset A/c	
To Profit on Sale of Asset A/c	
(If loss, debit Profit & Loss A/c)	

7. Change in Method

- Compute retrospective effect and adjust through Profit & Loss A/c.

8. AS-10 Key Points

- Depreciation begins when asset is ready for use.
- Continues even if idle.
- Review useful life and residual value annually.
- Component accounting for major parts.

9. Quick Revision Table



a)

Basis	SLM	WDV
Calculation	On Original Cost	On Book Value
Amount	Fixed every year	Decreases every year
Suitable for	Leasehold Assets	Plant & Machinery

b)

Topic	Key Points
Definition	Cost allocation over useful life; non-cash; for fixed assets.
Depreciable Asset Criteria	Multi-period, limited life, held for use—not for sale.
Objectives	Accurate profit, true asset value, replacement funds, production cost.
Measurement Factors	Cost, useful life, residual value, repairs, obsolescence, law.
SLM	Fixed annual depreciation.
WDV	Declining depreciation based on book value.
SYD	Accelerated depreciation; more in early years.
Entries - Provision	Expense via P&L → Provision.
Entries - Direct	Depreciation reduces asset; Expense recognized.
Illustrations	Jain Bros. (SLM & WDV), M/s Raj & Co. (SYD).
Component Accounting	Separate depreciation for component parts.

All Subjects Revision Notes & Most IMP Topics

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