DEPRECIATION

Depreciation represents the estimated reduction in value of a fixed assets within a fiscal year. Tangible assets, such as buildings, equipment, vehicles and so on, are purchased in large lump sums.
Depreciation is a decrease in the book value of fixed assets. Depreciation involves loss of value of assets due to the passage of time and obsolescence.

Following are the 3 principal features of depreciation:

Depreciation is a decrease in the book value of fixed assets.

Depreciation involves loss of value of assets due to the passage of time and obsolescence.

Depreciation is an ongoing process until the end of the life of assets.

Main Types of Depreciation Methods

1.Straight-line

2.Double declining balance

3.Units of production

Straight-Line Depreciation Method

Straight-line depreciation is a very common, and the simplest, method of calculating depreciation expense. In straight-line depreciation, the expense amount is the same every year over the useful life of the asset.

Depreciation Formula for the Straight Line Method:

The rate of Depreciation = (Annual Depreciation x 100) / Cost of Asset

Diminishing Balance Method

This method is also known as reducing balance method, written down value method or declining balance method. A fixed percentage of depreciation is charged in each accounting period to the net balance of the fixed asset under this method. This net balance is nothing but the value of asset that remains after deducting accumulated depreciation.

Thus, it means that depreciation rate is charged on the reducing balance of the asset. This asset is the one reflected in the books of accounts at the beginning of an accounting period.So, the book value of the asset is written down so as to to reduce it to its residual value.

Diminishing Balance Method Formula

Depreciation Expense = (Book value of asset at beginning of the year x Rate of Depreciation)/100

Units of Production Method

Under this method, the fraction of the number of fixed asset units (machinery) produced per year and the total number of units generated in a lifetime is multiplied with the fixed asset cost to yield the depreciated expense of each year. Hence, if the production decreases, the depreciated cost also steeps down and vice versa.

Units of Production Method Formula:

$$\text{Depreciation Rate Per Unit} = \frac{\text{Fixed Asset Cost} - \text{Salvage Value}}{\text{Total number of units produced during the useful life}}$$