

Cambridge IGCSE · Accounting 0452 · Notes

Depreciation and disposal of non-current assets

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Read first: [Capital and revenue expenditure and receipts](#), [The double entry system of book-keeping](#)

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What you need to know

By the end of this topic you should be able to:

1. **Define depreciation:** the part of the cost of a non-current asset that is used up over its useful life, charged as an expense year by year.
2. **Explain why a business accounts for depreciation:** to match the cost of an asset against the revenue it helps to earn in each year, and so that profit and the value of non-current assets are not overstated.
3. **Name and describe the three methods:** straight-line, reducing balance and revaluation, and say which suits which kind of asset.
4. **Prepare ledger accounts and journal entries for the provision for depreciation:** the non-current asset account at cost, the provision for depreciation account, and the yearly charge to the income statement.
5. **Prepare ledger accounts and journal entries for the sale of a non-current asset,** using a disposal account to find the profit or loss on disposal.

Showing depreciation in the income statement and the statement of financial position is practised again in the financial statements topics; here you need the figures and the ledger accounts.

Understand it

What depreciation is

A **non-current asset**, such as a van, a machine or office furniture, is bought to be used in the business for several years. It does not last for ever. Its value falls because of:

- **wear and tear** from being used (a van's engine and tyres wear out);
- **the passing of time** (a lease runs out, a building ages);
- **obsolescence:** a newer, better model makes it out of date (computers);
- **depletion:** the asset is used up (a mine or a quarry).

Depreciation is the part of the asset's cost that is treated as used up in each year of its useful life. It is an **expense**, so it reduces profit, but it is **not a payment**: no money leaves the business when depreciation is charged. The money left when the asset was bought. Depreciation is also an **estimate**, because nobody knows exactly how long an asset will last or what it will be worth at the end.

Why it is charged

- **Matching.** A van bought for \$24 000 helps to earn revenue for five years. Charging all \$24 000 as an expense in the first year would make that year's profit far too low and the next four years' too high. Depreciation spreads the cost over the years that benefit, so each year's profit is matched with the cost of earning it.
- **Not overstating.** Without depreciation, the statement of financial position would show a five-year-old van at the price paid for it, and profit would be too high because a real cost had been left out. That breaks prudence.

Three things depreciation is **not**, which multiple-choice options often suggest:

- it is **not a fund of cash** set aside to replace the asset (no money is put aside);
- it does **not** show the asset's **market value** (net book value is cost less depreciation to date, not what the asset would sell for);
- it applies to **non-current** assets, never to current assets such as inventory.

Non-current assets appearing at a lower book value is a **result** of depreciation, not the reason for charging it; the reason is to match the cost against revenue.

Straight-line method

The same amount is charged every year:

$$\text{Annual depreciation} = \frac{\text{cost} - \text{residual value}}{\text{useful life in years}}$$

The **residual value** (or scrap value) is what the business expects to get for the asset at the end of its life. A van costing \$24 000, expected to last 5 years and then sell for \$4 000, is depreciated by $(24\,000 - 4\,000) \div 5 = 4\,000$ a year.

Often the question gives a **percentage** instead, such as "20% per annum on cost": that is $20\% \times \text{cost}$ every year. If a residual value is given as well, apply the rate to **cost minus residual value**: a van costing \$35 000 with a residual value of \$5 000, at 20% straight-line, is depreciated by $20\% \times (35\,000 - 5\,000) = 6\,000$ a year, not \$7 000.

Straight-line suits assets that give the **same benefit every year**, such as fixtures and fittings or furniture. The asset is written down to its residual value (or to nil) by the end of its life.

Reducing balance method

A fixed percentage is charged each year on the **net book value at the start of that year** (cost less all depreciation charged so far), so the charge gets smaller every year.

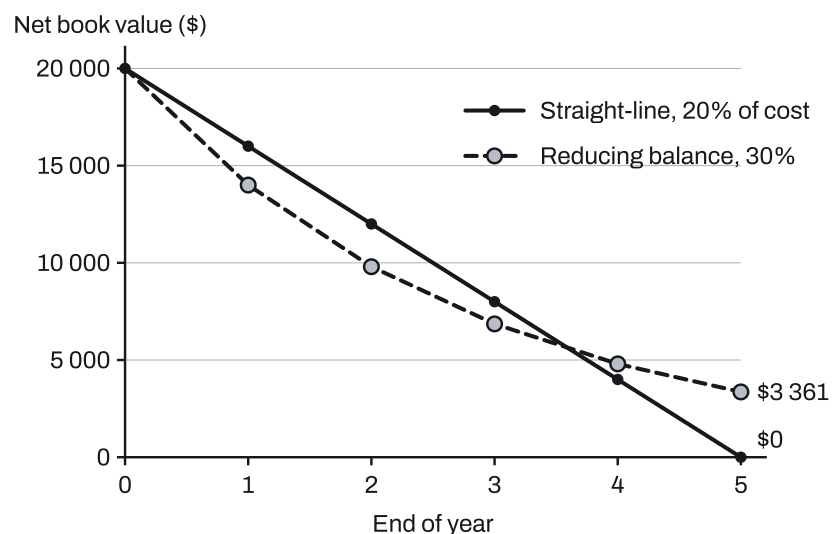
A machine costing \$24 000 depreciated at 25% a year:

Year	Net book value at start	Depreciation (25%)	Net book value at end
1	24 000	6 000	18 000
2	18 000	4 500	13 500
3	13 500	3 375	10 125

With reducing balance the rate always goes on the net book value; any residual value or useful life given in the question is **not used** in the calculation (they are there for comparison, or to tempt you).

A quick way to reach the net book value after n years is $\text{cost} \times (1 - \text{rate})^n$: here $24\,000 \times 0.75^3 = 10\,125$.

Reducing balance suits assets that give **more benefit in their early years** or lose value quickly at first, such as **motor vehicles** and assets subject to **rapid technological change** (computers). Their running and repair costs usually rise as they get older, so a falling depreciation charge keeps the total yearly cost more even. The net book value **never reaches nil**.



Revaluation method

Some assets are made up of many small items that are hard to track one by one, such as **loose tools** (hand tools, spanners, drill bits) or kitchen utensils. At each year end they are counted and **valued**, and the fall in value is the depreciation:

$$\text{Depreciation} = \text{value at start of year} + \text{cost of items bought in the year} - \text{value at end of year}$$

A workshop's loose tools were valued at \$1 800 at the start of the year, it bought tools for \$450, and they were valued at \$1 650 at the year end: $\text{depreciation} = 1\,800 + 450 - 1\,650 = 600$.

Land is normally not depreciated at all, because it does not wear out.

Part years: read the policy

Assets are bought and sold during the year, so every question states a policy. The common ones are:

- **"A full year's depreciation in the year of purchase and none in the year of disposal."** Count whole financial years: the year the asset was bought counts in full, however late it was bought; the year it was sold gets nothing.
- **"Depreciation is calculated monthly" or "for each part of the year for which the asset is owned".** Time-apportion: for an asset costing \$15 000 bought on 1 October, with a year end of 31 December and 20% straight-line, the first year's charge is $15\,000 \times 20\% \times \frac{3}{12} = 750$. In the year of sale, charge the months up to the date of sale as well.

Always work in **financial years**, not calendar years. If the year ends on 30 April, an asset bought on 1 October 2021 is in the year ended 30 April 2022.

Recording depreciation in the ledger

The asset itself stays at **cost** in its own account. Depreciation builds up in a separate account, the **provision for depreciation** (accumulated depreciation), which has a **credit** balance.

At each year end:

Entry	Debit	Credit
Charge for the year	Income statement	Provision for depreciation

Suppose Kofi bought a van for \$24 000 on 1 January 2024 and depreciates it at 25% reducing balance, with a year end of 31 December. The charges are \$6 000 for 2024 and \$4 500 for 2025. His provision account for 2025 is:

Provision for depreciation of motor vehicles account

Date	Details	\$	Date	Details	\$
2025			2025		
Dec 31	Balance c/d	10 500	Jan 1	Balance b/d	6 000
			Dec 31	Income statement	4 500
		10 500			10 500
			2026		
			Jan 1	Balance b/d	10 500

In the statement of financial position the two balances sit side by side:

Non-current assets	Cost	Accumulated depreciation	Net book value
Motor vehicles	24 000	10 500	13 500

Selling a non-current asset: the disposal account

When an asset is sold, its cost and its depreciation have to be taken out of the books, and the proceeds brought in. All three meet in a **disposal account**, and the figure that balances it is the **profit or loss on disposal**.

1. **Transfer the cost:** debit disposal, credit the asset account.
2. **Transfer the depreciation on that asset:** debit provision for depreciation, credit disposal.
3. **Record the proceeds:** debit bank or cash (or the buyer's account if sold on credit), credit disposal.
4. **Balance the account and transfer the difference to the income statement.** If the debit side is bigger, a **loss** is needed on the credit side; if the credit side is bigger, a **profit** is needed on the debit side.

Kofi sells the van on 1 March 2026 for \$12 800 by bank transfer, with no depreciation in the year of disposal. Its net book value is $24\,000 - 10\,500 = 13\,500$, so he makes a **loss** of $13\,500 - 12\,800 = 700$.

Disposal of motor vehicles account

Date	Details	\$	Date	Details	\$
2026			2026		
Mar 1	Motor vehicles	24 000	Mar 1	Provision for depreciation	10 500
				Bank	12 800
			Dec 31	Income statement	700
		24 000			24 000

The same sale as journal entries:

Account	Debit	Credit
Disposal of motor vehicles	24 000	
Motor vehicles		24 000
Provision for depreciation of motor vehicles	10 500	
Disposal of motor vehicles		10 500
Bank	12 800	
Disposal of motor vehicles		12 800
Income statement (loss on disposal)	700	
Disposal of motor vehicles		700

A **profit** on disposal is the reverse of the last entry: debit disposal, credit income statement. A loss is an extra expense; a profit is extra income. The proceeds themselves are a capital receipt and never go into sales.

Part exchange. If the old asset is traded in against a new one, the **trade-in allowance is the proceeds**. For a new van costing \$18 000, with \$6 000 allowed for the old one and \$12 000 paid by bank: debit motor vehicles \$18 000 (the full cost of the new van), credit disposal \$6 000 and credit bank \$12 000.

Consistency

Once a business chooses a method and rate for a type of asset, it should use the **same method every year** (the **consistency** principle), so that one year's profit can be compared with another's. Changing method just to make profit look higher is not a good reason; a change is justified only if the new method gives a truer picture, and its effect should be explained.

Key facts and formulas

There is no formula list in the IGCSE Accounting exam, so everything here must be learnt.

Formula	Status
Straight-line: annual depreciation = $\frac{\text{cost} - \text{residual value}}{\text{useful life}}$, or rate $\times$ (cost – residual value), with residual value 0 if none is given	Learn it
Reducing balance: depreciation = rate $\times$ net book value at the start of the year (ignore any residual value or life given)	Learn it
Net book value after n full years of reducing balance = cost $\times (1 - \text{rate})^n$	Learn it
Revaluation: depreciation = opening value + purchases – closing value	Learn it
Net book value = cost – accumulated depreciation	Learn it
Time-apportioned charge = annual charge $\times \frac{\text{months owned}}{12}$	Learn it
Straight-line on a group of assets (full year in purchase, none in disposal): rate $\times$ (opening cost + additions – cost of assets sold)	Learn it
Profit or loss on disposal = proceeds – net book value (positive: profit; negative: loss)	Learn it
Closing provision = opening provision + charge for the year – depreciation on assets sold	Learn it
Yearly charge: Dr income statement, Cr provision for depreciation	Learn it

Formula	Status
Disposal: Dr disposal, Cr asset (cost); Dr provision, Cr disposal (depreciation); Dr bank, Cr disposal (proceeds)	Learn it
Loss on disposal: Dr income statement, Cr disposal; profit on disposal: Dr disposal, Cr income statement	Learn it

How to do it

We have 75 tagged questions for this topic from 2021 to 2025 (49 different, as many appear on two or three paper variants): 60 one-mark multiple-choice questions from Paper 1 and 15 twenty-mark Paper 2 questions where this topic is one or more parts. 16 questions (12 on Paper 2, 4 on Paper 1) mix more than one type, so the counts add up to 102.

Question type	Questions
Calculate the depreciation charge, accumulated depreciation, net book value or provision balance	25
Calculate the profit or loss on disposal	20
Explain what depreciation is and why it is charged	13
Compare the methods and choose a suitable one	12
Prepare the disposal account	11
Prepare the asset account and the provision for depreciation account	8
Record depreciation and disposal as journal entries	7
Advise on changing the method or buying an asset	6

1. Calculate the depreciation charge, accumulated depreciation, net book value or provision balance (25 questions)

- Read the policy:** method, rate, full year in the year of purchase or monthly, and whether the year of disposal gets a charge.
- List the financial years** the asset was owned and which of them are charged. With a 30 April year end, an asset bought on 1 October 2021 and sold on 1 February 2025 is charged for the years ended 30 April 2022, 2023 and 2024 only.
- Work year by year** in a small table (net book value at start, charge, net book value at end), rounding only if the question asks. For straight-line the charge is the same every year; for reducing balance recalculate it from each new net book value.
- Add the charges** for the accumulated depreciation; take the total from cost for the net book value.

Variations you will meet:

- **Provision balance for a group of assets, reducing balance.** You are given the cost and the opening provision. $\text{Charge} = \text{rate} \times (\text{cost} - \text{opening provision})$; $\text{closing provision} = \text{opening provision} + \text{charge}$. For cost \$50 000 and opening provision \$18 000 at 25%: $\text{charge} = 25\% \times 32\,000 = 8\,000$, closing provision 26 000. Giving the opening provision, or the charge alone, is the usual wrong option.
- **Straight-line on a group of assets during a year of buying and selling** (full year in purchase, none in disposal): charge on the cost held at the year end, that is $\text{opening cost} + \text{additions} - \text{cost of the asset sold}$.
- **Monthly (time-apportioned) straight-line with a sale and a replacement.** Work each asset separately: the one kept, the one sold (months to the date of sale, then its depreciation leaves the provision) and the new one (months from the date bought). The closing provision includes only the assets still owned.
- **Residual value given with straight-line:** $\text{charge} = (\text{cost} - \text{residual}) \div \text{life}$, or, if a rate is given, $\text{rate} \times (\text{cost} - \text{residual})$. For cost \$35 000, residual \$5 000, 20%: \$6 000 a year, so \$12 000 after two years; \$14 000 (residual left out) is the trap.
- **Residual value or life given with reducing balance:** ignore them; apply the rate to the net book value each year.
- **"Two businesses, two methods": the difference in year 2.** Work out each year-2 charge separately; for reducing balance that is $\text{rate} \times (\text{cost} - \text{year-1 charge})$.
- **Revaluation** of loose tools: $\text{opening value} + \text{purchases} - \text{closing value}$. If tools bought this year are excluded from the closing valuation, add them to the closing value first.
- **An error in the asset account** (for example repairs debited to machinery): take the wrong amount out of the cost, then recalculate the charge, and the provision, on the corrected cost.
- **Total charge to the income statement in a part exchange:** $\text{depreciation on the new asset} + \text{the loss on the old one (or} - \text{the profit)}$.

2. Calculate the profit or loss on disposal (20 questions)

1. Work out the **accumulated depreciation on the asset sold** up to the date of sale, using the policy (type 1).
2. **Net book value** = $\text{cost} - \text{accumulated depreciation}$.
3. **Compare with the proceeds:** proceeds above net book value is a **profit**, below is a **loss**. State the word "profit" or "loss" with the amount.

For example, equipment costing \$9 000 with \$5 400 of depreciation is sold for \$4 100: net book value 3 600, so a **profit** of 500.

Variations you will meet:

- **Which side of the disposal account?** A loss is a **credit** entry (the balancing figure the credit side needs); a profit is a **debit** entry. Draw the T account if unsure.
- **Working backwards.** Given cost, proceeds and the profit, find the depreciation: in the disposal account, $\text{debits} = \text{cost} + \text{profit}$, so $\text{depreciation} = \text{cost} + \text{profit} - \text{proceeds}$, on the credit side. Given the loss instead, $\text{depreciation} = \text{cost} - \text{loss} - \text{proceeds}$, so $\text{proceeds} = \text{cost} - \text{depreciation} - \text{loss}$.

- **Net effect on cash of selling and replacing:** cash paid for the new asset — proceeds of the old one. Find the proceeds first from the disposal figures.
- **Part exchange:** the trade-in allowance is the proceeds.
- **The income statement for a later year** ("recorded in the year ended..."): the profit or loss belongs to the financial year in which the asset was sold. Check which year the date of sale falls in.

3. Explain what depreciation is and why it is charged (13 questions)

1. **Definition:** the estimated loss in value of a **non-current** asset over its useful life, charged as an expense.
2. **Reasons:** matching (spreading the cost over the years it helps earn revenue) and not overstating profit or assets (prudence).
3. **Reject** any option that says it is a **cash fund** for replacement, involves an outflow of money, shows **market value**, applies to **current** assets, or charges the whole cost in the year of purchase.

For "Which statements are correct?" questions, test each statement against those facts: "non-cash expense" and "an estimate" are true; "money set aside to replace the asset" is false.

Variation: "State how the principle of consistency is applied when charging depreciation": use the same method (and rate) every year.

4. Compare the methods and choose a suitable one (12 questions)

1. **Straight-line:** same charge each year; easy to calculate; asset reaches residual value or nil; suits assets used evenly (fixtures and fittings, furniture).
2. **Reducing balance:** higher charges early, falling each year; net book value never reaches nil; suits assets that give more benefit or lose more value early (vehicles, machinery, computers with rapid technological change).
3. **Revaluation:** for many small items valued at the year end (loose tools).
4. **No depreciation:** land.

One advantage and one disadvantage of reducing balance (1 mark each):

- advantages: matches the cost with the greater benefit in the early years; may give a more realistic net book value;
- disadvantages: must be recalculated every year, so harder to work out; the charge, and so the hit to profit, is higher in the early years.

Variation: identify the method from net book values. For example, equipment costing \$3 000 with a net book value of \$1 920 after two years: $3\,000 \times 0.8^2 = 1\,920$, so it is reducing balance at 20% (straight-line at 20% would give \$1 800). An asset "valued at 70% of cost" at the year end is using revaluation.

5. Prepare the disposal account (11 questions)

1. **Debit** the asset account's name with the **cost** of the asset sold.

2. **Credit** "Provision for depreciation" with the **accumulated depreciation** on that asset.
3. **Credit** the proceeds: "Bank" or "Cash", or the **buyer's name** if sold on credit.
4. **Balance** with "Income statement": on the **credit** side for a loss, the **debit** side for a profit. Total both sides.
5. Put in the **dates** (the date of sale for the first three, the year end for the transfer).

The details column must name the **other account**, for example "Motor vehicles", not "Cost" or "Vehicle at cost"; "Provision for depreciation", not "Depreciation"; "Bank", not "Proceeds"; "Income statement", not "Loss on sale".

6. Prepare the asset account and the provision for depreciation account (8 questions)

Asset account (at cost):

1. Debit: balance b/d (opening cost), then each purchase ("Bank", or the **supplier's name** if bought on credit).
2. Credit: "Disposal" with the **cost** of any asset sold; then balance c/d.
3. Total, and bring down the balance on the first day of the next year.

Provision for depreciation account:

1. Credit: balance b/d (opening provision).
2. Debit: "Disposal" with the depreciation on the asset sold.
3. Credit: "Income statement" with the charge for the year (from your calculation).
4. Debit: balance c/d; total; bring the balance down on the credit side.

Variations you will meet:

- **Two years in one question:** do the first year completely, bring the balances down, then do the second year starting from them.
- **Monthly depreciation with a sale during the year:** the depreciation on the asset sold includes its charge for the months of the year of sale, and that part-year charge is also part of the income statement figure. Show the parts of the charge (for example one line per asset) so each can earn its mark.
- **Only the provision account is asked for** (often alongside other adjustments): no asset account entries go into it; keep the vehicle's cost out.

7. Record depreciation and disposal as journal entries (7 questions)

1. **Yearly charge:** Dr income statement, Cr provision for depreciation. Work out the amount first (often the year-2 reducing balance charge).
2. **Removing the depreciation on an asset sold:** Dr provision for depreciation, Cr disposal.
3. **Removing its cost:** Dr disposal, Cr the asset account.
4. **Profit on disposal:** Dr disposal, Cr income statement; **loss:** Dr income statement, Cr disposal.

The wrong options usually credit the **asset account** with depreciation or reverse the debit and credit. The asset account only ever changes for purchases and disposals, at cost.

8. Advise on changing the method or buying an asset (6 questions)

These are 5-mark "Advise ... Justify your answer" parts. Marks are for points on each side (usually up to 3 a side, 4 in total) and **1 for a clear recommendation**, which needs at least one point on each side.

1. **Points for changing to reducing balance** (for vehicles): suits assets that lose more value early; more realistic net book value; better matching of cost with benefit.
2. **Points against**: harder to calculate each year; a higher charge (lower profit) in the early years; breaks the **consistency** principle; profits can no longer be compared with earlier years.
3. **If the reason given is "to increase profit"**: say that a higher profit on paper is not a good reason to change; it breaks consistency and may overstate profit and assets. The real reason must be a truer picture.
4. **Recommendation**: "I advise ... because ...", linked to the points you made.

Variation: whether to buy a (replacement) asset, often with a loan. For: saves hire costs, may earn more revenue and profit, the business owns the asset. Against: the cost is higher, loan interest and repayments, the bank may want security, hire costs continue until delivery. Then recommend.

Worked examples

Example 1

Chen's financial year ends on 31 December. On 1 July 2024 he bought a machine for \$36 000. He expects to use it for 8 years and then sell it for \$4 000. He uses the straight-line method, calculated monthly.

- (a) Calculate the depreciation charge for the years ended 31 December 2024 and 31 December 2025. **[3]**
- (b) Calculate the net book value of the machine at 31 December 2025. **[1]**
- (c) If Chen had used the reducing balance method at 20% per annum instead, with a full year's charge in the year of purchase, calculate the net book value at 31 December 2025, and state which method gives the higher profit for 2025. **[3]**

(a) Annual charge = $(36\,000 - 4\,000) \div 8 = 4\,000$. **(1)**

2024: owned July to December, 6 months: $4\,000 \times \frac{6}{12} = 2\,000$. **(1)** 2025: a full year, 4 000. **(1)**

(b) $36\,000 - (2\,000 + 4\,000) = 30\,000$. **(1) OF**

(c) 2024: $20\% \times 36\,000 = 7\,200$; 2025: $20\% \times (36\,000 - 7\,200) = 5\,760$. **(1)** Net book value = $36\,000 - 12\,960 = 23\,040$. **(1)** Straight-line charges \$4 000 in 2025 against \$5 760, so straight-line gives the higher profit for 2025. **(1)**

Example 2

Amara runs a delivery business. Her financial year ends on 31 December. At 1 January 2025 her delivery vehicles had cost \$180 000 and the provision for depreciation was \$72 000.

She depreciates delivery vehicles at 20% per annum on cost, using the straight-line method, for each month a vehicle is owned.

- On 1 May 2025 she bought a van for \$36 000 on credit from Zeta Motors.
- On 31 August 2025 she sold, for \$9 500 by bank transfer, a vehicle that had cost \$30 000 on 1 January 2022.

(a) Calculate the depreciation charge for the year ended 31 December 2025, showing the charge on each group of vehicles separately. **[4]**

(b) Prepare the provision for depreciation of delivery vehicles account and the disposal of delivery vehicles account for the year ended 31 December 2025. Balance the provision account and bring down the balance on 1 January 2026. **[8]**

(a) Work each group separately, counting months:

Vehicles	Working	\$
Kept all year	$20\% \times (180\,000 - 30\,000)$	30 000 (1)
Sold on 31 August (8 months)	$20\% \times 30\,000 \times \frac{8}{12}$	4 000 (1)
New van from 1 May (8 months)	$20\% \times 36\,000 \times \frac{8}{12}$	4 800 (1)
Charge for the year		38 800 (1)OF

(b) The vehicle sold had been depreciated for 2022, 2023 and 2024 ($3 \times 6\,000 = 18\,000$) before this year, plus the \$4 000 for 2025, so the depreciation to transfer on disposal is $18\,000 + 4\,000 = 22\,000$.

Provision for depreciation of delivery vehicles account

Date	Details	\$	Date	Details	\$
2025			2025		
Aug 31	Disposal (1)OF	22 000	Jan 1	Balance b/d	72 000
Dec 31	Balance c/d	88 800	Dec 31	Income statement (1)OF	38 800
	110 800			110 800	
			2026		
			Jan 1	Balance b/d (1)OF	88 800

Disposal of delivery vehicles account

Date	Details	\$	Date	Details	\$
2025			2025		
Aug 31	Delivery vehicles (1)	30 000	Aug 31	Provision for depreciation (1)OF	22 000
Dec 31	Income statement (1)OF	1 500		Bank (1)	9 500
		31 500			31 500

(1) for the dates. The vehicle's net book value was $30\,000 - 22\,000 = 8\,000$ and it sold for \$9 500, so the \$1 500 is a **profit**, on the debit side. The delivery vehicles account would show the \$30 000 credited to disposal and a closing balance of $180\,000 + 36\,000 - 30\,000 = 186\,000$.

Example 3

Leila's financial year ends on 31 March. On 1 April 2023 she bought a machine for \$50 000 by cheque. She depreciates machinery at 30% per annum using the reducing balance method, with a full year's charge in the year of purchase and none in the year of disposal. On 1 December 2025 she sold the machine for \$26 000 cash.

(a) Calculate the accumulated depreciation on the machine at the date of sale. [3]

(b) Calculate the profit or loss on disposal, stating whether it is a profit or a loss. [2]

(c) Prepare the journal entries to record the disposal. Narratives are not required. [4]

(a) The machine was owned in the years ended 31 March 2024 and 2025; 1 December 2025 falls in the year ended 31 March 2026, the year of disposal, so there is no charge for it.

Year ended 31 March 2024: $30\% \times 50\,000 = 15\,000$. (1)

Year ended 31 March 2025: $30\% \times (50\,000 - 15\,000) = 10\,500$. (1)

Accumulated depreciation = $15\,000 + 10\,500 = 25\,500$. (1)OF

(b) Net book value = $50\,000 - 25\,500 = 24\,500$; proceeds \$26 000. (1)OF Profit on disposal \$1 500. (1)OF

(c)

Account	Debit \$	Credit \$
Disposal of machinery	50 000	
Machinery		50 000
Provision for depreciation of machinery	25 500	
Disposal of machinery		25 500
Cash	26 000	
Disposal of machinery		26 000

Account	Debit \$	Credit \$
Disposal of machinery	1 500	
Income statement		1 500

(1) for each correct pair. The profit is debited to disposal because the credits (\$51 500) were more than the debit of \$50 000.

Example 4

Tomas runs a car repair workshop. His financial year ends on 31 December.

(a) His loose tools were valued at \$2 650 on 1 January 2025. He bought new tools for \$820 during the year, and all his tools were valued at \$2 390 on 31 December 2025. Calculate the depreciation of loose tools for the year. [2]

(b) State the most suitable method of depreciation, or no depreciation, for each of: land, office furniture, loose tools, computers. [4]

(c) Tomas depreciates his lifting equipment at 25% per annum using the reducing balance method. He wants to change to 10% per annum straight-line because it would increase his profit this year. Advise Tomas whether he should change his method of depreciation. Justify your answer. [5]

(a) $2\,650 + 820 - 2\,390 = 1\,080$ (1), so depreciation is \$1 080. (1)

(b) Land: no depreciation (1); office furniture: straight-line (1); loose tools: revaluation (1); computers: reducing balance, because they lose value quickly through technological change (1).

(c) For the change: straight-line is easier to calculate, with the same charge every year (1); the lower charge would increase his profit this year, which might please a lender (1).

Against the change: the consistency principle says the same method should be used each year, and changing makes profits hard to compare with earlier years (1); wanting a higher profit is not a good reason to change, so profit may be overstated (1); lifting equipment probably gives more benefit in its early years, so reducing balance gives a more realistic net book value (1).

Recommendation: Tomas should **not** change, because the only reason is a higher profit on paper, which breaks consistency and may overstate both profit and the value of his equipment. (1)

(Up to 4 marks for the points, with at least one on each side, and 1 for the justified recommendation.)

Common mistakes

- **Charging depreciation in the year of disposal** when the policy says none, or leaving out the year of purchase when a full year is charged. Examiners saw both in 2025. List the financial years first.
- **Putting the sale proceeds into the depreciation calculation.** Depreciation depends only on cost, rate and time; the proceeds appear only in the disposal account.

- **Using the wrong words in the accounts.** Examiners regularly penalise details such as "MV at cost", "Depreciation", "Proceeds" and "Loss on sale". Write the name of the other account: "Motor vehicles", "Provision for depreciation", "Bank", "Income statement".
- **Entries on the wrong side, or all in one account.** Some candidates put every entry in the vehicles account or the provision account, or leave out the transfer from the provision to disposal. Each of the three accounts has its own entries (type 5 and 6 above).
- **Leaving out the opening balance** of the provision account, or putting a vehicle's cost into it. The provision account holds only depreciation.
- **Charging straight-line on the wrong total.** Deduct the cost of the asset sold before applying the rate to a group of assets, and do not include depreciation on an asset already sold in a later year's provision.
- **Giving the opening provision instead of the closing one**, or charging only one year when two have passed. Read "balance on the provision at ..." carefully.
- **Forgetting the residual value** in a straight-line calculation from cost, residual value and life.
- **Saying depreciation is a fund to replace the asset, or shows its market value.** It is neither; it matches cost with revenue.
- **Describing the methods instead of advising.** In "Advise ... whether to change the method", examiners want the advantages and disadvantages of the **change** in the business described, the consistency principle developed (profits can't be compared), and a clear recommendation, not a description of how each method is calculated or which gives the most profit.

How to get the marks

- **"Calculate":** show each year's figure on its own line. Mark schemes give a mark per year's charge and carry your own figure forward (**OF**), so a slip in year 1 does not lose the later marks.
- **Profit or loss on disposal:** show the net book value, the proceeds and the answer, and write the word **profit** or **loss**. An amount without the word is not a full answer.
- **Ledger accounts:** each entry needs a **date**, the **name of the other account** and the amount on the correct side. Total both sides, and bring the balance down on the first day of the next year when asked ("balance the account and bring down the balance").
- **Credit purchases and sales** of assets use the supplier's or buyer's **name**, not "Purchases", "Sales" or "Creditor".
- **Journal entries:** debit line first, credit line below, both amounts. Narratives only if asked.
- **"State"** needs a short answer: one advantage, one reason, or one method. **"Explain"** needs the point and why it matters.
- **"Advise ... Justify your answer":** points on both sides (up to 3 each, 4 in total), then a recommendation that follows from them. No recommendation, or a recommendation with only one side argued, loses the last mark.
- **Multiple choice:** work out the answer before looking at the options. The wrong options are usually the opening balance, one year only, the residual value left out, or the profit and loss on the wrong side.

Quick check

1. A van bought on 1 January 2024 for \$28 000 is depreciated at 20% per annum using the reducing balance method. Calculate its net book value and its accumulated depreciation at 31 December 2026.
2. Equipment that cost \$9 600, with accumulated depreciation of \$6 150, is sold for \$2 900. Calculate the profit or loss on disposal and state on which side of the disposal account it appears.
3. On 1 January 2025 a business's machinery had cost \$64 000 and its provision for depreciation was \$25 600. It depreciates machinery at 25% per annum using the reducing balance method, and bought and sold no machinery during 2025. Calculate the balance on the provision for depreciation account at 31 December 2025.
4. State two reasons why a business provides for depreciation, and one thing depreciation is not.
5. Prepare the journal entries (without narratives) to record: (i) depreciation of fixtures for the year, \$2 400; (ii) the transfer of \$5 100 of accumulated depreciation on a vehicle that has been sold.

Answers

1. Net book value = $28\,000 \times 0.8^3 = 14\,336$ (charges \$5 600, \$4 480 and \$3 584). Accumulated depreciation = $28\,000 - 14\,336 = 13\,664$.
2. Net book value = $9\,600 - 6\,150 = 3\,450$; proceeds \$2 900, so a **loss** of \$550, on the **credit** side of the disposal account (transferred to the debit of the income statement).
3. Charge = $25\% \times (64\,000 - 25\,600) = 25\% \times 38\,400 = 9\,600$. Closing provision = $25\,600 + 9\,600 = 35\,200$.
4. To match the cost of the asset against the revenue it helps to earn over its useful life; so that profit and the value of non-current assets are not overstated. It is not a cash fund for replacing the asset (nor its market value).
5. (i) Dr income statement \$2 400, Cr provision for depreciation of fixtures \$2 400. (ii) Dr provision for depreciation of motor vehicles \$5 100, Cr disposal of motor vehicles \$5 100.

Past questions to try

- 0452/23/M/J/25 Q2: parts (a) and (b), accumulated depreciation to the date of sale and the disposal account.
- 0452/22/O/N/21 Q5: the three accounts over two years, with monthly straight-line and a sale in March.
- 0452/12/F/M/22 Q17: identifying the methods from net book values.
- 0452/11/M/J/21 Q13: working backwards from a profit on disposal to the depreciation.