

Accounting for non-current assets AS

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Last checked 30 September 2026

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What you need to know

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

1. **Tell capital from revenue:** say whether a payment is capital or revenue expenditure, and whether money received is capital or revenue income, and show how each is treated in the financial statements.
2. **Explain the effect of getting it wrong:** what happens to profit (or loss) and to the value of non-current assets when capital expenditure is treated as revenue, or revenue as capital.
3. **Give the causes of depreciation:** why non-current assets lose value (wear and tear, obsolescence, the passing of time, using up).
4. **Explain why we depreciate,** and which accounting concepts depreciation applies (matching, prudence, consistency).
5. **Calculate depreciation** with the straight-line and the reducing balance methods, including part years.
6. **Choose the most suitable method** for an asset and justify the choice.
7. **Value non-current assets** with the cost model or the revaluation model.
8. **Prepare ledger accounts and journal entries** for buying and revaluing non-current assets, for depreciation, and for disposals, including a part exchange.
9. **Calculate the profit or loss on disposal** of a non-current asset.
10. **Show depreciation in the statements:** the charge in the statement of profit or loss, and cost less accumulated depreciation in the statement of financial position.

Understand it

Capital and revenue expenditure

A **non-current asset** is something a business keeps and uses for more than one year to help it earn income, and does not intend to sell: premises, machinery, vehicles, furniture, computers. Whether it is a non-current asset depends on the business: a car in a car dealer's showroom is **inventory**, but the dealer's own breakdown truck is a non-current asset.

Capital expenditure is money spent to buy a non-current asset, to get it ready for use, or to **improve** it (make it bigger, faster or longer-lasting). It is added to the asset's cost in the statement of financial position, and it reaches the statement of profit or loss only slowly, through depreciation.

Revenue expenditure is money spent on running the business day to day, and on **keeping** assets in their present condition. It goes straight into the statement of profit or loss as an expense this year.

Capital expenditure (add to the asset's cost)	Revenue expenditure (an expense)
Purchase price (after any trade discount)	Repairs and maintenance, including a maintenance contract
Delivery (carriage) of the new asset	Insurance, road tax and licence fees
Installation, and wages of staff who install it	Fuel, electricity and running costs
Legal fees and taxes on buying property	Training staff to use the asset
Extensions and improvements, upgrading an engine	Redecorating or repainting (unless part of a new extension)
Fitting shelves in a van, painting the business's name on a new van	Interest on a loan used to buy the asset

A maintenance contract or insurance that covers more than one year is still revenue expenditure: only this year's share is an expense, and the rest is a **prepayment**, a current asset.

Capital income is money received that does not come from trading: the proceeds from selling a non-current asset, a loan received, capital put in by the owner, or money from issuing shares. **Revenue income** comes from normal operations: sales, rent received, commission and interest received. Revenue income is included in profit; capital income is not (only the **profit or loss** on selling an asset reaches the statement of profit or loss).

Getting it wrong

If a capital item is treated as revenue, the whole cost is charged as an expense this year instead of being spread out. Profit is too low and the non-current assets are too low. The opposite error does the opposite.

Error	Profit for the year	Non-current assets
Capital expenditure treated as revenue	Understated (a loss is overstated)	Understated
Revenue expenditure treated as capital	Overstated	Overstated
Capital income treated as revenue income	Overstated	No effect

The size of the error is the item **less the depreciation that should (or should not) have been charged on it**. A \$20 000 machine written off as repairs, when the business depreciates machinery at 10% of cost, understates profit by $20\,000 - 2\,000 = 18\,000$ and understates non-current assets by the same \$18 000 (it should show at $20\,000 - 2\,000$).

Why assets lose value

Most non-current assets lose value because of:

- **wear and tear:** physical deterioration from use (vehicles, machinery);
- **obsolescence:** new technology or changing demand makes them out of date (computers, older machines);
- **the passing of time:** a 10-year lease is worth less each year, whether or not it is used;
- **depletion:** using up a natural resource (a mine or a quarry).

A change in the **estimate** of an asset's useful life or residual value is not a cause of depreciation; it only changes how the figure is calculated. Land does not usually wear out, so it is not normally depreciated; buildings are.

What depreciation is for

Depreciation spreads the cost of a non-current asset, less what it should be sold for at the end (its **residual value**), over the years of its **useful life**. The machine helps earn revenue in every one of those years, so each year's statement of profit or loss should carry a share of its cost. This is the **matching** (accruals) concept.

It also applies:

- **prudence:** assets are not shown at more than they are worth to the business, and profit is not overstated;
- **consistency:** the same method and rate are used every year so the results can be compared from year to year;
- **going concern** and **historic cost:** assets are shown at cost less depreciation, not at what they would fetch if sold today.

Depreciation is **not** a way of saving money to replace the asset (no cash is set aside), and it does **not** show the asset's market value. It is a **non-cash** expense: charging it reduces profit but not the bank balance.

The straight-line method

The same charge every year:

$$\text{annual depreciation} = \frac{\text{cost} - \text{residual value}}{\text{useful life (years)}}$$

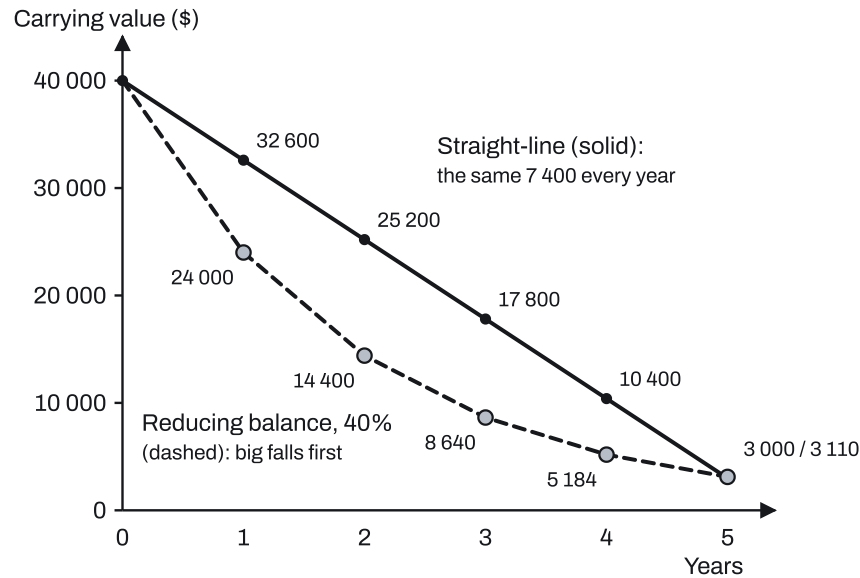
or, if you are given a rate, $\text{rate} \times \text{cost}$. A machine costing \$40 000 with a residual value of \$3 000 and a 5-year life is depreciated by $\frac{40\,000 - 3\,000}{5} = 7\,400$ a year, so its carrying value falls by the same \$7 400 each year until it reaches \$3 000.

The reducing balance method

A fixed **percentage** of the carrying value at the start of the year (cost less the provision so far):

$$\text{annual depreciation} = \text{rate} \times (\text{cost} - \text{accumulated depreciation})$$

The same \$40 000 machine at 40% reducing balance: year 1 $40\% \times 40\,000 = 16\,000$; year 2 $40\% \times 24\,000 = 9\,600$; year 3 $40\% \times 14\,400 = 5\,760$. The rate stays the same, but the charge falls every year, and the carrying value never reaches zero (after 5 years it is \$3 110). Residual value is ignored in the calculation.



Part years

The question always states the policy. The usual ones are:

- **month-by-month** (a time basis): depreciate only for the months owned. A machine costing \$24 000 bought on 1 April, straight-line 25% of cost, with a 31 December year end: $24\,000 \times 25\% \times \frac{9}{12} = 4\,500$ in the first year;
- **a full year in the year of purchase and none in the year of disposal**: ignore the dates within the year;
- the charge is based on the assets held **at the end of the year**.

With reducing balance on a time basis, work out the full-year figure on the carrying value, then take the fraction.

Choosing a method

Choose the method that matches the way the asset gives its benefit, so the charge follows the use:

- **straight-line** suits assets that give the **same benefit every year** (buildings, furniture, a lease). It is simple to calculate and understand;
- **reducing balance** suits assets that **lose more value early** or are most productive when new (vehicles, computers, machinery). The high early charges also balance the rising repair costs of later years, so the total cost each year stays fairly even.

The method is not chosen to make profit look better. Once chosen it is used every year (consistency), and it is changed only if a different method gives a fairer view.

The cost model and the revaluation model

Under the **cost model** an asset is shown at **cost less accumulated depreciation**, its **carrying value** (also called net book value).

Under the **revaluation model** it is shown at a **fair value** set at a recent revaluation, less depreciation since then. Revaluations must be kept up to date, and the whole class of assets (for example all property) is revalued together. On an upward revaluation:

1. the asset account goes up from cost to the new value;
2. the accumulated depreciation is cleared, because the new value already allows for it;
3. the total gain (new value less carrying value) goes to a **revaluation reserve**, part of equity. It is **not** profit, because nothing has been sold.

After a revaluation, depreciation is based on the **new value** spread over the **remaining** useful life, so the charge usually rises. A later fall in value first uses up the revaluation reserve on that asset; any fall beyond that is a loss that reduces profit.

The revaluation method is different: it is used for many small, cheap items (loose tools, kitchen utensils) where depreciating each one separately is not practical. They are valued at the year end, and

$$\text{depreciation} = \text{opening valuation} + \text{purchases} - \text{closing valuation}.$$

With an opening valuation of \$1 800, purchases of \$600 and a closing valuation of \$1 900, the charge is \$500. All the entries go in the one asset account: the depreciation is **credited** there (and debited to the statement of profit or loss).

The ledger accounts

Each class of asset has two accounts: one at **cost** (a debit balance) and a **provision for depreciation** (a credit balance, the accumulated depreciation). The yearly charge is:

	Debit	Credit
Depreciation charge	Statement of profit or loss	Provision for depreciation

Buying an asset: debit the asset at cost; credit bank, a loan, or the supplier if bought on credit.

A typical provision for depreciation account for one year:

Dr	Provision for depreciation	\$	Cr	Provision for depreciation	\$
Sep 30	Disposal	9 000	Jan 1	Balance b/d	30 000
Dec 31	Balance c/d	33 000	Dec 31	Statement of profit or loss	12 000
		42 000			42 000
			Jan 1	Balance b/d	33 000

Disposing of an asset

When an asset is sold or scrapped, its figures are gathered in a **disposal account**:

Debit disposal account	Credit disposal account
Asset at cost (the asset's original cost)	Provision for depreciation (its accumulated depreciation)
Profit on disposal: statement of profit or loss	Bank (the sale proceeds) or the asset account (a part-exchange allowance)
Any selling costs (or deduct them from proceeds)	Loss on disposal: statement of profit or loss

$$\text{profit (loss) on disposal} = \text{proceeds} - \text{selling costs} - \text{carrying value at the date of disposal}$$

The disposal account is really a small calculation: if the credits are bigger (proceeds exceed carrying value) the balancing figure is a profit on the debit side; otherwise it is a loss on the credit side.

A profit on disposal is not "extra depreciation" but the sign that too much depreciation was charged; a loss means too little was charged. Either way it is shown in the statement of profit or loss: a profit as other income, a loss as an expense.

Part exchange. When an old asset is handed over as part payment for a new one, the allowance is its "sale proceeds". Debit the asset account (the new asset) and credit the disposal account with the part-exchange value; the rest of the new asset's price is credited to bank or a loan. The new asset's cost is the **full price** (part-exchange value plus the rest paid).

In the financial statements

- **Statement of profit or loss:** the charge for the year (and any profit or loss on disposal). A company may split it between distribution costs and administrative expenses.
- **Statement of financial position:** each class of non-current asset at cost (or valuation), less accumulated depreciation, giving the carrying value. The revaluation reserve is part of equity.

Key facts and formulas

There is no formula list in the 9706 exam, so learn all of these.

Formula	Status
Straight-line: charge = $\frac{\text{cost} - \text{residual value}}{\text{useful life}}$ or rate $\times$ cost	Learn it
Reducing balance: charge = rate $\times$ (cost – accumulated depreciation)	Learn it
Part year: full-year charge $\times \frac{\text{months owned}}{12}$	Learn it
carrying value = cost (or valuation) – accumulated depreciation	Learn it

Formula	Status
profit (loss) on disposal = proceeds – selling costs – carrying value	Learn it
revaluation gain = new value – carrying value	Learn it
After revaluation: charge = $\frac{\text{new value} - \text{residual value}}{\text{remaining useful life}}$	Learn it
Revaluation method: charge = opening value + purchases – closing value	Learn it
closing CV = opening CV + additions – CV of disposals – depreciation	Learn it

Key facts to learn:

- **Capital:** buying, getting ready for use, improving. **Revenue:** running and maintaining.
- **Depreciation charge:** Dr statement of profit or loss, Cr provision for depreciation.
- **Revaluation:** Dr asset (increase), Dr provision (all of it), Cr revaluation reserve.
- **Part exchange:** Dr asset (new), Cr disposal, with the part-exchange value.
- **Concepts:** matching, prudence, consistency. Realisation and materiality are not reasons for depreciating.

How to do it

We have 130 tagged questions for this topic from 2021 to 2025 (127 different: three appear on two paper variants). 21 of them mix two or more types, so the counts add up to 167.

Question type	Questions
Calculate profit or loss on disposal, or prepare the disposal account (including part exchange)	32
Classify capital or revenue expenditure and income, and find an asset's cost	29
Calculate depreciation, a provision balance or a carrying value	22
Explain the purpose and causes of depreciation and the concepts it applies	21
Find the effect of treating capital or revenue items wrongly	15
Prepare the asset and provision for depreciation accounts, or the depreciation journal	12
Choose or compare depreciation methods	11
Record a revaluation (revaluation model or revaluation method)	10
Correct an error in depreciation or disposal records, or a change of rate or method	9
Work back from carrying value movements to a missing figure	6

1. Calculate profit or loss on disposal, or prepare the disposal account (32 questions)

1. **Find the accumulated depreciation on the asset sold**, up to the date of disposal, following the stated policy exactly: count the months owned on a time basis, or give a full year in the year of purchase and none in the year of sale. Straight-line: charge per year $\times$ years. Reducing balance: work out each year in turn.

2. **Carrying value** = cost – accumulated depreciation.
3. **Compare** with the proceeds (or part-exchange value) less any selling costs: more is a profit, less is a loss.
4. **Disposal account** (Paper 2): debit the asset's cost; credit the provision for depreciation, then bank (or the asset account for a part exchange); the balancing figure goes to the "Statement of profit or loss", on the debit side for a profit and the credit side for a loss. Total both sides.

Variations you will meet:

- **Working backwards.** Given the loss and asked for the proceeds: $\text{proceeds} = \text{carrying value} - \text{loss} + \text{selling costs}$ (selling costs add to what you must receive to end up with that loss). Or given the profit, find the original cost.
- **Part exchange with a cheque or loan for the rest.** The disposal account credits the asset account with the part-exchange value; the asset account shows the new asset's full cost made up of the part-exchange value and the bank or loan amount.
- **Which entries:** a profit on disposal is Dr disposal, Cr statement of profit or loss; a part exchange is Dr asset, Cr disposal.
- **Combined effect on profit** of an asset sold: the depreciation charged in its last year plus the loss (or less the profit).
- **Cash flow:** only the sale proceeds are cash; the profit or loss and depreciation are not.

2. Classify capital or revenue expenditure and income, and find an asset's cost (29 questions)

1. **Test each item:** does it buy the asset, get it ready for use, or improve it? Capital. Does it run or maintain the asset? Revenue.
2. **Add the capital items** to get the asset's cost.
3. If asked for the **expenses in the statement of profit or loss:** depreciation on that cost, plus this year's share of each revenue item (spread a two-year contract over two years).

Variations you will meet:

- **Income:** proceeds from selling non-current assets, loans and new capital are capital income; rent, interest and commission received are revenue income.
- **Which assets are non-current** for this particular business (the dealer's showroom cars are inventory).
- **Define** capital expenditure (spending on acquiring or improving non-current assets, which benefits more than one year) and capital receipts (money received that is not from trading, such as loans or the sale of non-current assets), and total a list of each.

3. Calculate depreciation, a provision balance or a carrying value (22 questions)

1. **Read the policy:** method, rate, residual value, and the part-year rule.
2. **Straight-line:** $\text{rate} \times \text{cost}$, or $(\text{cost} - \text{residual}) \div \text{life}$, then $\times \text{months} \div 12$ for part years.

3. **Reducing balance:** $\text{rate} \times (\text{cost} - \text{provision brought forward})$. Assets bought this year have no provision yet.
4. **Several assets:** work each out separately and add. Show each line of working; each earns its own mark.
5. **Provision balance at the end** = all the depreciation charged so far on the assets still held.

Variations you will meet:

- **Assets bought and sold in the year:** charge the full year on assets held all year, and part years for the ones bought or sold (on a time basis).
- **Reverse:** find the cost from the charge. A van bought on 1 October (year end 31 December) is depreciated at 25% a year on cost less a residual value of \$4 000, charged by the month. The first year's charge was \$2 250, so $(\text{cost} - 4\,000) \times 25\% \times \frac{3}{12} = 2\,250$, giving $\text{cost} - 4\,000 = 36\,000$ and a cost of \$40 000.
- **Carrying value after a number of years:** straight-line, $\text{cost} - \text{years} \times \text{charge}$; reducing balance, $\text{cost} \times (1 - \text{rate})^{\text{years}}$.

4. Explain the purpose and causes of depreciation and the concepts it applies (21 questions)

1. **Purpose:** to spread the cost of an asset over the years that benefit from it (matching); to avoid overstating profit and asset values (prudence).
2. **Causes:** wear and tear, obsolescence, passage of time, depletion. Give causes other than wear and tear if the question rules it out.
3. **Concept questions:** name the concept, say what it requires, and link it to depreciation (see "How to get the marks").

Traps in multiple choice: depreciation does not provide funds for replacement, show market value, or show replacement cost. It is a non-cash expense. Realisation, materiality and objectivity are not the concepts behind it. A business **can** change its method if the new one gives a fairer view.

5. Find the effect of treating capital or revenue items wrongly (15 questions)

1. Decide which way the error goes, using the table in "Understand it".
2. For a number: the size is the item less the depreciation that should have been charged on it (capital treated as revenue), or the item less any depreciation wrongly charged (revenue treated as capital).
3. For a list of mixed errors, take each one separately and net them: items removed from non-current assets are a decrease; items that should be added are an increase.

Example: machinery at cost includes \$600 of repairs, and wages include \$400 paid to staff installing a new machine. Correcting them moves \$600 out of non-current assets and \$400 in: a net decrease of \$200 (ignoring depreciation).

6. Prepare the asset and provision for depreciation accounts, or the depreciation journal (12 questions)

1. **Asset at cost account:** debit the balance b/d and additions (with the other account named: bank, loan, or disposal for a part-exchange value); credit the cost of assets sold ("Disposal") and the balance c/d.
2. **Provision for depreciation account:** credit the balance b/d and the charge for the year ("Statement of profit or loss"); debit the accumulated depreciation on assets sold ("Disposal") and the balance c/d.
3. Date every line, balance off, and bring the balance down.
4. **Depreciation journal:** Dr statement of profit or loss (or depreciation), Cr provision for depreciation, with the amount; no narrative unless asked.

Variations you will meet:

- **Which side?** In multiple choice: the charge for the year is a credit in the provision account; the depreciation on an asset sold is a debit.
- **Where does it appear?** The charge is in the statement of profit or loss; the accumulated depreciation is deducted from cost in the statement of financial position.
- **Timing:** the transfer to disposal is made on the date of sale; the year's charge on the new asset is made at the year end.

7. Choose or compare depreciation methods (11 questions)

1. Say what the asset is and how it gives its benefit: evenly (straight-line) or mostly early (reducing balance).
2. For "advise" or "discuss": give points for **both** methods, then a decision with a reason linked to the asset.
3. If someone suggests a switch just for convenience or to lift profit, cite the **consistency** concept: the same method each year makes results comparable.

Points to use: straight-line is simple and gives the same charge each year; reducing balance charges more early when the asset is most productive and loses most value, balancing higher repairs later; its rate stays the same while the charge falls; it never reaches zero.

8. Record a revaluation (10 questions)

1. **Accumulated depreciation** to the revaluation date (years owned × charge).
2. **Journal:** Dr asset (new value – cost); Dr provision for depreciation (all of it); Cr revaluation reserve (new value – carrying value). Check: the two debits add up to the credit.
3. **Later depreciation:** new value ÷ remaining useful life.

Variations you will meet:

- **Effect of an upward revaluation:** the capital reserve (revaluation reserve) increases, retained earnings are unchanged; later depreciation increases and the carrying value is higher.
- **A downward revaluation:** reduces the revaluation reserve on that asset; any fall beyond it reduces profit.

- **The revaluation method for small items:** prepare the one asset account: debit the opening valuation and purchases (bank), credit the statement of profit or loss with the depreciation (the balancing figure) and the closing valuation as balance c/d. Explain why it is used: many low-value items, so separate depreciation for each would be impractical.

9. Correct an error in depreciation or disposal records, or a change of rate or method (9 questions)

1. **Work out what should have been charged** and compare with what was charged.
2. **Correct the difference:** too little charged: Dr statement of profit or loss, Cr provision; too much: the reverse. For example, a \$200 000 asset depreciated at 10% instead of 15% needs another \$10 000: Dr statement of profit or loss \$10 000, Cr provision for depreciation \$10 000.
3. **Revise profit and carrying value** by the same amount.

Variations you will meet:

- **Sale proceeds credited to sales:** sales and profit are overstated by the proceeds, when only the profit or loss on disposal belonged there, so the net overstatement of profit is the carrying value; non-current assets are also overstated by the carrying value (the asset was never removed).
- **Depreciation left out in an earlier year:** that year's profit was too high; the carrying value brought forward was too high, so the later loss on disposal is larger (or profit smaller) by the same amount.
- **A higher rate in earlier years** gives lower profits then, a lower carrying value and so a larger profit on disposal later.

10. Work back from carrying value movements to a missing figure (6 questions)

1. Write the movement: opening CV + additions – CV of disposals – depreciation = closing CV.
2. Put in what you know and solve for the missing figure.
3. If a profit or loss on disposal is given, find the proceeds from the carrying value of the asset sold.

For example, opening carrying value \$150 000, additions \$40 000, carrying value of an asset sold \$6 000, closing carrying value \$162 000: $150\,000 + 40\,000 - 6\,000 - D = 162\,000$, so depreciation $D = 22\,000$. A part-exchange value counts as part of the additions' cost.

Worked examples

The bold codes show where marks are earned, as in Cambridge mark schemes. The number is how many marks.

- **M1** method mark: for a correct method, even if the numbers slip.
- **A1** accuracy mark: for a correct answer; it needs the M mark before it.
- **B1** mark for a correct result on its own, with no method needed.

Example 1

A business buys a new machine and makes the following payments at the start of its financial year.

	\$
Machine	36 000
Delivery of the machine	1 200
Installation of the machine	800
Three-year service contract	2 700
Training staff to use the machine	900

Machinery is depreciated at 25% per annum using the straight-line method.

What is the total expense for the year in the statement of profit or loss from these payments?

A \$9 500 B \$10 400 C \$11 300 D \$12 200 **[1]**

The capital items are the machine, its delivery and its installation: $36\,000 + 1\,200 + 800 = 38\,000$.

Depreciation is $25\% \times 38\,000 = 9\,500$. The service contract covers three years, so this year's expense is $2\,700 \div 3 = 900$; the other \$1 800 is a prepayment. Training is revenue: \$900.

Total = $9\,500 + 900 + 900 = 11\,300$. The answer is **C** (1).

A leaves out the revenue items, B leaves out one of the revenue items, and D charges the whole service contract and leaves out training.

Example 2

At the start of the year a business bought a delivery vehicle for \$24 000. In error, it was recorded in the vehicle repairs account. Vehicles are depreciated at 25% per annum using the straight-line method.

What is the effect of the error on the profit for the year and on non-current assets?

	profit for the year	non-current assets
A	understated by \$24 000	understated by \$24 000
B	understated by \$18 000	understated by \$18 000
C	understated by \$18 000	understated by \$24 000
D	overstated by \$18 000	understated by \$18 000

[1]

Charged as repairs: \$24 000. Should have been charged as depreciation: $25\% \times 24\,000 = 6\,000$. So profit is understated by $24\,000 - 6\,000 = 18\,000$. The vehicle should appear at $24\,000 - 6\,000 = 18\,000$, but appears at nothing, so non-current assets are understated by \$18 000. The answer is **B** (1).

Example 3

Ravi's financial year ends on 31 December. On 1 April 2022 he bought a van for \$30 000. Vans are depreciated at 20% per annum on cost using the straight-line method, on a month-by-month basis.

On 30 September 2025 the van was part-exchanged for a new van costing \$45 000. The part-exchange allowance was \$12 500, and the balance was paid by cheque.

(a) Calculate the accumulated depreciation on the old van at 30 September 2025. [2]

(b) Prepare the disposal account. [4]

(c) State the two debit entries in the motor vans account for the new van. [2]

(a) Annual charge = $20\% \times 30\,000 = 6\,000$, so \$500 a month (**M1**). From 1 April 2022 to 30 September 2025 is $9 + 12 + 12 + 9 = 42$ months, so accumulated depreciation = $42 \times 500 = 21\,000$ (**A1**).

(b) Carrying value = $30\,000 - 21\,000 = 9\,000$; the allowance of \$12 500 is more, so there is a profit of \$3 500.

Dr	Disposal	\$	Cr	Disposal	\$
Sep 30	Motor vans	30 000	Sep 30	Provision for depreciation	21 000
Dec 31	Statement of profit or loss	3 500	Sep 30	Motor vans (part exchange)	12 500
		33 500			33 500

B1 cost, **B1** provision (own figure), **B1** part-exchange value, **B1** profit to the statement of profit or loss (own figure).

(c) Disposal \$12 500 (**B1**) and bank $45\,000 - 12\,500 = 32\,500$ (**B1**). The new van's cost is the full \$45 000.

Example 4

T Limited's financial year ends on 31 December.

At 1 January 2025 its motor vehicles cost \$120 000 and the provision for depreciation was \$43 800. On 1 July 2025 it bought another vehicle for \$20 000. Motor vehicles are depreciated at 30% per annum using the reducing balance method, with a full year's charge in the year of purchase.

(a) Prepare the provision for depreciation of motor vehicles account for the year ended 31 December 2025. [4]

The company's property cost \$600 000 on 1 January 2020 and is depreciated at 2% per annum on cost using the straight-line method. On 1 January 2025 it was revalued at \$690 000.

(b) Prepare the journal entry to record the revaluation. A narrative is not required. [4]

(c) Calculate the depreciation charge on the property for 2025, assuming its total useful life is unchanged. [2]

(d) Explain, with reference to one accounting concept, why T Limited should keep using the reducing balance method for its vehicles. [3]

(a) Charge = $30\% \times (120\,000 + 20\,000 - 43\,800) = 30\% \times 96\,200 = 28\,860$ (**M1 A1**).

Dr	Provision for depreciation of motor vehicles	\$	Cr	Provision for depreciation of motor vehicles	\$
Dec 31	Balance c/d	72 660	Jan 1	Balance b/d	43 800
			Dec 31	Statement of profit or loss	28 860
		72 660			72 660
			Jan 1	Balance b/d	72 660

B1 balance b/d, **B1** charge (own figure) with the correct label and balance c/d.

(b) Accumulated depreciation: $5 \times 2\% \times 600\,000 = 60\,000$ (**W**). Carrying value = 540 000, so the gain is $690\,000 - 540\,000 = 150\,000$.

Date	Account	Dr \$	Cr \$
2025 Jan 1	Property	90 000	
	Provision for depreciation of property	60 000	
	Revaluation reserve		150 000

B1 property 690 000 – 600 000, **B1** provision, **B1** revaluation reserve, **B1** for the working of \$60 000.

(c) At 2% a year the total life is 50 years, so 45 years remain (**M1**). Charge = $690\,000 \div 45 = 15\,333$ (nearest dollar) (**A1**).

(d) Consistency (1): the same depreciation method should be used from one year to the next (1), so that the profit and asset values of different years can be compared fairly (1).

Common mistakes

- **Wrong labels in the disposal account.** Examiners report every year that the right figures are entered with the wrong details or on the wrong side. The transfer is labelled "Statement of profit or loss" (not "profit" or "loss"), the proceeds "Bank", the part exchange "Motor vehicles". Marks are not given for a wrong label.
- **Getting the years of ownership wrong.** Count the months or years carefully against the stated policy; a year too many or too few turns a loss into a profit.
- **Leaving out installation or delivery** when calculating the cost to depreciate, or including repairs, insurance and licences in it.
- **Forgetting the opening balance** in the provision for depreciation account, or putting the asset's cost in it.
- **Reducing balance on cost.** The rate is applied to cost **less** the provision brought forward, not to cost every year.
- **Ignoring assets bought or sold in the year.** Deduct the asset sold from cost before charging a full year on the rest, and give the part year on it separately.
- **Revaluation journal without the provision.** Very few candidates clear the accumulated depreciation; the reserve is new value less **carrying value**, not less cost.
- **Stating a concept without developing it.** "Consistency" alone scores 1 mark; say what it requires and that it makes years comparable.
- **Saying depreciation provides money to replace the asset.** It doesn't; no cash is set aside.
- **Messy workings.** When the final figure is wrong, method marks go only to clear, labelled workings.

How to get the marks

- **Multiple choice:** test each option or numbered statement separately; for numbers, work the figure out before looking at the options, since the distractors are the common slips.
- **"Calculate":** set out each line with its label (Machine 1, Machine 2, total). There is usually one mark for the working and one for the answer, and own-figure (**OF**) marks follow a wrong earlier figure.
- **Ledger accounts:** account title, dates, the other account's name in the details, amounts on the right side, totals level, balance c/d and b/d.
- **Journals:** debits first, then credits, in two columns. "A narrative is not required" means don't write one.
- **"State"** (two reasons, two causes): one short, different point per mark.
- **"Explain, with reference to one concept":** name it (1), say what it requires (1), link it to the situation (1).
- **"Define":** one precise sentence; for capital receipts, include what they are **not** (not from normal trading).
- **"Advise ... justify by discussing both":** points for and against each method, then a decision with a reason. The decision alone earns only its own mark.

Quick check

1. A machine costs \$18 000, has a residual value of \$2 000 and a useful life of 4 years. Find the annual straight-line charge and the carrying value after 3 years.
2. Equipment costing \$50 000 is depreciated at 20% per annum using the reducing balance method. Find the charge in year 3 and the carrying value at the end of year 3.
3. A machine costing \$25 000 was bought on 1 July 2023 and sold on 31 March 2026 for \$17 000. It is depreciated at 10% per annum on cost on a month-by-month basis. Find the profit or loss on disposal.
4. The carrying value of a business's equipment was \$84 000 at the start of the year and \$88 000 at the end. During the year it bought equipment for \$30 000 and sold equipment with a carrying value of \$9 000. Find the depreciation charge for the year.
5. A café values its utensils at \$2 400 at the start of the year and \$2 650 at the end. It bought utensils for \$900 during the year. Find the depreciation charge using the revaluation method, and state the entry that records it.

Answers

1. $\frac{18\,000 - 2\,000}{4} = 4\,000$ a year. After 3 years: $18\,000 - 3 \times 4\,000 = 6\,000$.
2. Year 1: $20\% \times 50\,000 = 10\,000$. Year 2: $20\% \times 40\,000 = 8\,000$. Year 3: $20\% \times 32\,000 = 6\,400$. Carrying value = $32\,000 - 6\,400 = 25\,600$ (or $50\,000 \times 0.8^3$).
3. Months owned: $6 + 24 + 3 = 33$. Depreciation = $2\,500 \times \frac{33}{12} = 6\,875$. Carrying value = $25\,000 - 6\,875 = 18\,125$. Loss = $18\,125 - 17\,000 = 1\,125$.
4. $84\,000 + 30\,000 - 9\,000 - D = 88\,000$, so $D = 17\,000$.
5. $2\,400 + 900 - 2\,650 = 650$. Dr statement of profit or loss \$650, Cr utensils account \$650.

Past questions to try

- [9706/22/O/N/25 Q3](#): provision balances, a revaluation journal and a disposal account.
- [9706/21/O/N/24 Q3](#): asset and provision accounts with a part exchange and a loan, then choosing a method.
- [9706/22/F/M/23 Q2](#): the revaluation method, a depreciation journal after a part exchange, and capital receipts.
- [9706/12/O/N/25 Q7](#): the depreciation charge after revaluing a property.