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New Zealand Society of Accountants

STATEMENT OF STANDARD
ACCOUNTING PRACTICE NO. 3
Revised 1984, 2002

ACCOUNTING FOR DEPRECIATION

Issued by the Council, New Zealand Society of Accountants

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This Statement should be read in the context of the Explanatory Foreword to Statements of Standard Accounting Practice

1 INTRODUCTION

1.1 This Statement deals with accounting for depreciation and applies to all depreciable assets except —

(a) forests and similar regenerative natural resources;
(b) expenditures on the exploration for and extraction of minerals, oil, natural gas and similar non-regenerative resources;
(c) expenditures on research and development (refer to SSAP-13 *Accounting for Research and Development Costs*);
(d) goodwill;
(e) property, plant and equipment required to be depreciated in accordance with FRS-3: *Accounting for Property, Plant and Equipment.*

2 APPLICATION

2.1 The standards in this Statement apply to all external financial statements.

2.2 This Statement of Standard Accounting Practice becomes operative for financial statements covering periods ending on or after 31 March 1985.

3 DEFINITIONS

3.1 *Depreciation* is the wearing out, consumption or other loss of value of an asset whether arising from use, effluxion of time or obsolescence through technological and market changes. It is accounted for by the allocation of the depreciable amount of a depreciable asset over its useful life. (The term “amortisation” is sometimes used as an alternative term to depreciation.)

3.2 *Depreciable amount* is the historical cost (or revalued amount) of a depreciable asset in the financial statements, less the residual value.

3.3 *Depreciable asset* is an asset which —
(a) is expected to be used during more than one accounting period, and
(b) has a limited useful life, and
(c) is held by an enterprise for use in the production or supply of goods and services, or for administrative purposes.

3.4 Useful life is either —
(a) the period over which a depreciable asset is expected to be used by the enterprise; or
(b) the number of production or similar units expected to be obtained from the asset by the enterprise.

3.5 *Residual value* is the estimated realisable value (less costs of disposal) of a depreciable asset at the end of its useful life. Residual value is estimated at the date of acquisition, and may be re-estimated at any later time, when, as a result of experience or changed circumstances, it is considered that the original estimate of residual value requires revision.

3.6 *Recoverable amount* is the greater of the amount recoverable from an asset's further use and ultimate disposal, and its current net realisable value.

4 EXPLANATION

4.1 Depreciable assets comprise a significant portion of the assets of many enterprises. Depreciation can therefore have a significant effect in determining and presenting the financial position and results of operations of those enterprises.

4.2 Depreciation should be charged in each accounting period on the basis of the depreciable amount.

4.3 The depreciable amount should be allocated on a systematic basis to each accounting period during the useful life of the asset.

4.4 The useful life of a depreciable asset for an enterprise may be shorter than its physical life. In addition to physical wear and tear, which depends on operational factors such as the number of shifts for which the asset is to be used and the repair and maintenance programme of the enterprise, other factors need to be taken into consideration. These include obsolescence arising from technological changes or improvements in production methods, obsolescence arising from a change in the market demand for the product or service output of the asset, and legal limits such as the expiry dates of related leases.

4.5 The depreciable amount should be allocated as fairly as possible to the periods expected to benefit from the use of the asset and the method selected should be the most appropriate for the type of asset and its use in the enterprise. The method of allocation should correspond to the expected pattern of exhaustion of the asset's service potential.

4.6 The amount of depreciation charged to each accounting period involves the exercise of judgement in the light of technical, commercial and other considerations and accordingly requires periodic review. When, as the result of experience or of changed circumstances, it is considered that the original estimate of useful life of an asset requires revision, the remaining portion of the depreciable amount of the asset should be allocated over the revised remaining useful life.

4.7 If at any time the carrying amount of a depreciable asset is greater than the estimated recoverable amount (perhaps as a result of obsolescence or a fall in demand for a product), it should be written down immediately to the recoverable amount.

4.8 A change from one method of providing depreciation to another should be made only on the grounds that the new method will give a fairer allocation of the depreciable amount. Such a change should be dealt with in accordance with the provisions of SSAP-7, *Extraordinary Items and Prior Period Adjustments*.

4.9 Where a depreciable asset is disposed of for an amount which is greater or less than its carrying amount, the surplus or deficit should be reflected in the profit and loss account or other operating statement for the year.

4.10 Where an asset is revalued the charge for depreciation should be based on the revalued amount. In the year in which the revaluation takes place, for the period prior to the date of revaluation the charge should be based on the existing depreciable amount, and for the period after the date of revaluation the charge should be calculated on the revalued amount.

4.11 The total depreciation charged for the period should be disclosed in the financial statements together with the following for each major class of depreciable asset—

(a) the depreciation method used;

(b) a summary of the useful lives or depreciation rates used;

(c) the gross amount (ie. historical cost or revalued amount) and the related accumulated depreciation.

The information to be disclosed with regard to depreciation rates and the related carrying amounts of assets should be classified in sufficient detail so as to provide information of use to readers of financial statements.

5 STANDARD ACCOUNTING PRACTICE

Accounting for Depreciation

The Standards set out in the following paragraphs should be read in the context of the foregoing paragraphs of this Statement and the Explanatory Foreword issued by the Council of the Society.

5.1 The depreciable amount of a depreciable asset should be allocated on a systematic basis to each accounting period during the useful life of the asset.

5.2 The depreciable amount should be allocated as fairly as possible to the periods expected to benefit from the use of the asset. The method of allocation should correspond to the expected pattern of exhaustion of the asset's service potential.

5.3 A change from one method of providing depreciation to another should be made only on the grounds that the new method will give a fairer allocation of the depreciable amount. Such a change should be dealt with in accordance with the provisions of SSAP-7, *Extraordinary Items and Prior Period Adjustments.*

5.4 The useful life of a depreciable asset should be reviewed periodically and the depreciation charge adjusted for the current and future periods if expectations are significantly different from the previous estimates. The effect of the change should be disclosed in the accounting period in which the change takes place.

5.5 If at any time the carrying amount of a depreciable asset is greater than the estimated recoverable amount it should be written down immediately to the recoverable amount.

5.6 Where an asset is revalued the charge for depreciation should be based on the revalued amount. In the year in which the revaluation takes place the charge for depreciation should be calculated having reference to the revalued amount and the date of that revaluation.

5.7 Where a depreciable asset is disposed of for an amount which is greater or less than its carrying amount, the surplus or deficit should be reflected in the profit and loss account or other operating statement for the year.

5.8 The total depreciation charged for the period should be disclosed in the financial statements together with the following for each major class of depreciable asset —

(a) the depreciation method used;

(b) a summary of the useful lives or the depreciation rates used;

(c) the gross amount (ie. historical cost or the revalued amount) and the related accumulated depreciation.

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