

# The need to be “financially bilingual” US GAAP vs IFRS

## XIII. DEPRECIATION

This presentation contains information, in addition to the material prepared and provided by the professor, from:

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DEPRECIATION  
PROPERTY PLANT AND EQUIPMENT (PPE)

## **DEPRECIATION BY COMPONENTS**

### **US GAAP FASB ASC 410,420,845**

➤ **Allow but not Require:**

- Consequently, most firms **do not separate** their depreciable assets into components

### **IFRS IAS 16**

➤ **Allow but not Require:**

- Each part of an item of property, plant and equipment with a cost that is **significant** in relation to the total cost of the item shall be depreciated separately.

## **DEPRECIATION METHODS**

### **US GAAP FASB ASC 410,420,845**

- Various depreciation methods are used in practice.

### **IFRS IAS 16**

- Specifically mentions three depreciation methods:
  - straight-line
  - units-of-production
  - declining balance method

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## COMPONENTS EXAMPLE

### BUILDING

1. **Foundation**: useful life
2. **Frame**: useful life
3. **Heating** and air condition systems: machine hours

### AIRPLANE

1. **Airframe**: flying hours
2. **Engines**: machine hours
3. **Interior**: useful life

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## **DEPRECIATION: EXAMPLE**

ABC uses the straight line method and useful life for all components.

1. \$5,000,000 to the airframe, useful life of 20 years and \$500,000 residual value.
2. \$4,000,000 to engines, useful life 16 years and \$200,000 residual value.
3. \$1,000,000 to the interior, useful life 5 years and no residual value.

**What is the depreciation expense for the first year?**

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## IFRS:

Airframe: $\$5,000,000 - 500,000 / 20 =$	\$225,000
Engine: $\$4,000,000 - 200,000 / 16 =$	\$237,500
Interior: $\$1,000,000 / 5 =$	<u>\$200,000</u>
	<b>\$662,500</b>

## US GAAP:

$\$10,000,000 - 500,000 - 200,000 / *20 =$ * example: use the highest year	<b>\$465,000</b>
$\$10,000,000 - 500,000 - 200,000 / **13.67 =$ **estimates: use an average (20+16+5= 41 years/3)	<b>\$680,322</b>

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## EXAMPLE

<u>Components</u>	<u>Cost</u>	<u>Useful Life</u>
1. Motor	\$100,000	5
2. *Inspection (Engine)	\$25,000	2
3. Machine	<u>\$200,000</u> \$120,000	10

Motor- replace every 5 years

Engine replace every 2 years

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## EXAMPLE

<u>Components</u>	<u>Cost</u>	<u>Useful Life</u>	<u>Depreciation Expense</u>
1. Motor	\$100,000	5	\$20,000
2. *Inspection (Engine)	\$25,000	2	\$12,500
3. Machine	<u>\$200,000</u>	10	<u>\$20,000</u>
	\$325,000		\$ 52,500

Motor- replace every 5 years

Engine replace every 2 years

\*Component could be tangible or intangible

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## ASSESSMENT ACTIVITY

### *7. DEPRECIATION BY COMPONENTS*