CONCEPT: DEPRECIATION – STRAIGHT LINE METHOD

● ***Depreciation –*** breaks up the up-front cost of a long-term asset over its ________________

☐ The use of depreciation is an example of the _______________ principle

January, Year 1: Purchase airplane for $20,000,000	Year 1-20: Generate yearly revenue of $5,000,000
January, Year 1: Purchase airplane for $20,000,000	Year 1-20: Generate yearly revenue of $5,000,000

☐ Depreciation is a ______________ expense. It also does not relate to the __________________ of the asset.

☐ When calculating depreciation (in all methods), we must know three things about the asset:

1. ***Cost*** – The initial cost of the asset
2. ***Useful Life*** – how long the company __________ the asset to help generate revenue
3. ***Residual Value*** – how much the company __________ the asset to be worth at the end of its useful life
   - Residual Value is also called *salvage value* or *scrap value*

$$Straight\ Line\ Depreciation\ per\ period = \frac{Cost - Residual\ Value}{Useful\ Life, usually\ in\ years}$$

EXAMPLE: On January 1, Year 1, Johnson & Johnson & Johnson Company purchased a delivery truck for $42,000. The company estimated a useful life of 5 years and a residual value of $2,000. What would be the entry to record depreciation when preparing the December 31, Year 1 financial statements and the net book value on that date?

Cost = \$42,000; Estimated Residual Value = \$2,000; Estimated Useful Life = 5 years			
Date	Depreciation Expense	Accumulated Depreciation	Net Book Value
January 1, Year 1			
December 31, Year 1			
December 31, Year 2			
December 31, Year 3			
December 31, Year 4			
December 31, Year 5			
December 31, Year 6			

PRACTICE: ABC Company purchased a new machine on January 1, Year 1 for \$44,000. The company expects the machine to last ten years. The company thinks it could sell the scrap metal from the machine for \$4,000 at the end of its useful life. If the company uses the straight-line method for depreciation, what will be the net book value of the machine on December 31, Year 4?

a) \$22,400
b) \$24,000
c) \$26,400
d) \$28,000

PRACTICE: DBQ Company purchased a machine on January 1, Year 1 for \$60,000. The company estimated a five year useful life and \$8,000 residual value. If the company uses the straight-line method for depreciation, what will be the amount of accumulated depreciation on December 31, Year 2?

a) \$10,400
b) \$12,000
c) \$20,800
d) \$24,000