



Southampton Voluntary Services Community Accountancy Project

Fixed Assets and Depreciation

A fixed asset is an item that is purchased for use within an organisation over a number of years. Examples would be buildings, furniture, equipment or vehicles.

There should be a minimum capitalisation limit, whereby items below a certain value are included as an expense on the Statement of Financial Activities (SOFA) and items above this are shown as an asset on the balance sheet and depreciated.

Fixed Asset Register

This is a record of assets owned by the organisation. It will show the date of purchase, a description of the item, the cost and depreciation.

The register will help the trustees to look after the assets of the charity. It can be checked on a regular basis to ensure that the assets still exist and are in good condition. It is also advisable to record serial numbers for insurance purposes.

Depreciation

This is a way of spreading the cost of an asset over the years in which it will be used. The value of the asset on the balance sheet will go down accordingly.

The trustees of the organisation will need to decide the expected life of the asset, known as the useful economic life and the method of depreciation.

Residual value is the amount that the asset could be sold for if it was disposed of at the end of its useful life, ignoring the effects of inflation.

There are two methods of calculating depreciation, the straight line method and the reducing balance method.

Straight line method

This charges an equal amount each year over the life of the asset. The charge for each year will be calculated as follows;

$$\text{Depreciation charge} = \frac{\text{Cost} - \text{residual value}}{\text{Useful economic life}}$$

Reducing balance method

With this method a fixed percentage is applied to the net book value of the asset each year, with the net book value being cost minus total depreciation to date. This means that the depreciation charge in earlier years will be greater than in later years. The annual depreciation charge will be calculated as follows;

$$\text{Depreciation} = \text{net book value} \times \text{annual depreciation rate}$$

The method that is chosen should reflect the way in which the asset will be used. If equal benefit will be gained each year, the straight line method would be most appropriate, and if the asset will be more productive in earlier than later years the reducing balance method should be used.

Fixed Assets in the Annual Accounts

Receipts and Payments Accounts

The entire cost of the asset should be recorded as a payment at the time of purchase. The Statement of Assets and Liabilities shows a list of fixed assets under non-monetary assets and liabilities. No depreciation is necessary.

Accruals Accounts

The asset will be included on the balance sheet and depreciated. The annual depreciation charge is then shown as an item of expenditure for the year, as well as reducing the net book value shown in the balance sheet. This is because the accruals basis matches income and expenditure to the year it relates to, so the costs needs to be spread to reflect the years in which benefit will be gained from the asset.

The depreciation policy should be explained in the notes to the accounts, under accounting policies.

The notes to the accounts will also need a breakdown per category of fixed assets, showing cost, depreciation and net book value at the start and end of the year, and any movements in between.

Other issues that may have to be dealt with include accounting for the sale of an asset, purchasing an asset on hire purchase, part exchanges or the revaluation of land and buildings. Further assistance is available in these areas where necessary.

For further information, or if you require this information in another format, contact:

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