Accumulation Depreciation is a contra asset account. Land does not depreciate. Taxes assessed to transfer the ownership (title) on the land is included in the cost of land.

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| --- | --- | --- |
| Purchase price of land |  | $ 50,000 |
| Add related costs: |  |  |
| Property Taxes | $ 4,000 |  |
| Transfer taxes | $ 2,000 |  |
| Removal of Building | $ 5,000 |  |
| Survey fee | $ 1,000 | $ 12,000 |
| Total cost of land |  | $ 62,000 |

The cost of machinery and equipment includes the following: Purchase price (less any discounts), Transportation charges, Insurance while in transit, Sales tax and other taxes, Purchase commission, Installation costs, testing costs (prior to use of the asset).

Depreciation is the allocation of plant asset’s cost to expense over its useful life.

Obsolete is an asset is considered obsolete when a newer asset can perform the job more efficiently than the old.

Residual Value is the expected value of a depreciable asset at the end of its useful life.

Straight-line method: Straight-line depreciation = (Cost – Residual value)/Useful life

Units-of-production method: Depreciation per unit = (Cost – Residual value)/Useful life in Units

Units-of-production depreciation = Depreciation per unit x Current year usage

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| **Capital Expenditure:** | **Revenue Expenditure** |
| **Debit an Asset Account** | **Debit Repairs and Maintenance Expense** |
| *Extraordinary Repairs:* | *Revenue Expenditure* |
| Major engine or transmission overhaul | Repair of transmission or engine |
| Modification for new use | Oil change, lubrication, and so on |
| Addition to storage capacity | Replacement of tires or windshield |
| Anything that increases the life of the asset | Paint job |

Double-Declining-Balance Method- an accelerated depreciation method that computes annual depreciation by multiplying the depreciable asset’s decreasing book value by a constant percent that is two times the straight-line depreciation rate.

Double-declining-balance depreciation = (Cost – Accumulated depreciation) x 2 x (1/useful life)

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| --- | --- | --- | --- |
| **Date** | **Accounts and Explanation** | **Debit** | **Credit** |
| 1-Jul | Cash | $ 4,000 |  |
|  | Accumulated Depreciation-Equipment | $ 8,500 |  |
|  | Equipment |  | $ 10,000 |
|  | Gain on Disposal |  | $ 2,500 |
|  | Sold equipment for cash |  |  |

Patents get amortized. Asset turnover ratio = Net sales/Average total assets

Current Portion of Notes Payable- The amount of the principal that is payable within one year.

The times-interest-earned ratio is also called the *interest-coverage ratio.*

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| **Date** | **Accounts and Explanation** | **Debit** | **Credit** |
| 31-Dec | Equipment (new) | $ 8,000 |  |
|  | Accumulated Depreciation-Equipment | $ 9,000 |  |
|  | Equipment |  | $ 10,000 |
|  | Cash |  | $ 2,000 |
|  | Gain on Disposal |  | $ 5,000 |
|  | Exchanged old equipment and cash for new equipment |  |  |

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| --- | --- | --- | --- |
| **Date** | **Accounts and Explanation** | **Debit** | **Credit** |
| 31-Dec | Equipment (new) | $ 3,000 |  |
|  | Accumulated Depreciation-Equipment | $ 9,000 |  |
|  | Loss on Disposal | $ 500 |  |
|  | Equipment |  | $ 10,000 |
|  | Cash |  | $ 2,500 |
|  | Exchanged old equipment and cash for new equipment |  |  |

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| --- | --- | --- | --- |
| **Date** | **Accounts and Explanation** | **Debit** | **Credit** |
| 31-Dec | Interest Expense ($10,000 x 0.06 x 2/12) | $ 100 |  |
|  | Interest Payable |  | $ 100 |
|  | Accrued interest expense at year-end |  |  |

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| --- | --- | --- | --- |
| **Date** | **Accounts and Explanation** | **Debit** | **Credit** |
| 10-Jun | Warranty Expense ($50,000 x0.03) | $ 1,500 |  |
|  | Estimated Warranty Payable |  | $ 1,500 |
|  | To accrue warranty payable |  |  |

A high interest-coverage ratio indicates a business’s ease in paying interest expense; a low ratio suggests difficulty.

Times-interest-earned ration = (Net income + income tax expense + interest expense)/Interest expense

Stated Interest rate (also called *face rate, coupon rate, or nominal rate)-* The interest rate that determines the amount of cash interest the borrower pats and the investor receives each year.

Discount on Bonds Payable – Occurs when a bond’s issue price is less than face value. Premium on Bonds Payable – Occurs when a bond’s issue price is more than face value.

Debt to equity ratio = Total liabilities / Total equity

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| --- | --- | --- | --- |
| **Date** | **Accounts and Explanation** | **Debit** | **Credit** |
| 1-Jul | Cash | $ 500 |  |
|  | Accumulated Depreciation-Equipment | $ 8,500 |  |
|  | Loss on Disposal | $ 1,000 |  |
|  | Equipment |  | $ 10,000 |
|  | Sold equipment for cash |  |  |

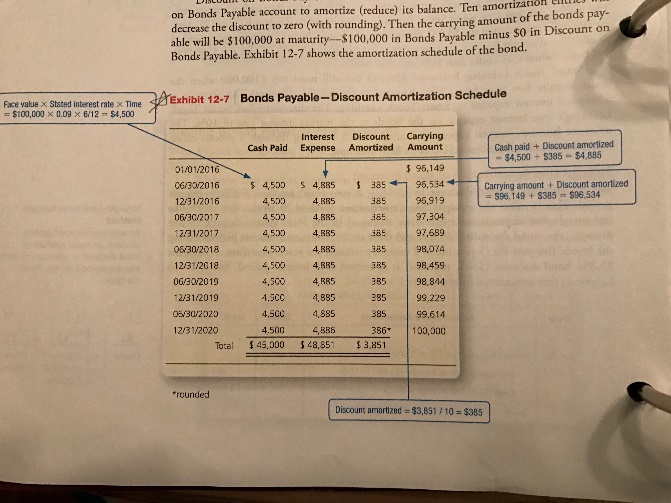
|  |  |
| --- | --- |
| **Likelihood of Future Event** | **How to Report the Contingency** |
| Remote | Do not disclose |
| Reasonably Possible | Describe the situation in a note to the financial statements |
| Probable and the amount of the expense cannot be estimated | Describe the situation in a note to the financial statements |
| Probable and the amount of the expense can be estimated | Record an expense and a liability based on the estimated amounts |

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| **Date** | **Accounts and Explanation** | **Debit** | **Credit** |
| 1-Jan | Cash | $ 100,000 |  |
|  | Bonds Payable |  | $ 100,000 |
|  | Issued bonds at face value |  |  |

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| --- | --- | --- | --- |
| **Date** | **Accounts and Explanation** | **Debit** | **Credit** |
| 30-Jun | Interest Expense ($100,000 x 0.09 x 6/12) | $ 4,500 |  |
|  | Cash |  | $ 4,500 |
|  | Paid Semiannual interest |  |  |

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| --- | --- | --- | --- |
| **Date** | **Accounts and Explanation** | **Debit** | **Credit** |
| 1-Jan | Cash | $ 96,149 |  |
|  | Discount on Bonds Payable | $ 3,851 |  |
|  | Bonds Payable |  | $ 100,000 |
|  | Issued bonds at a discount |  |  |

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| --- | --- | --- | --- |
| **Date** | **Accounts and Explanation** | **Debit** | **Credit** |
| 27-Jun | Estimated Warranty Payable | $ 800 |  |
|  | Merchandise Inventory |  | $ 800 |
|  | To replace merchandise inventory under warranty |  |  |

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