CAS -16

COST ACCOUNTING STANDARD ON DEPRECIATION AND AMORTISATION

The following is the COST ACCOUNTING STANDARD – 16 (CAS – 16) issued by the Council of The Institute of Cost Accountants of India on **"DEPRECIATION AND AMORTISATION"**. In this Standard, the standard portions have been set in ***bold italic*** type. This standard should be read in the context of the background material which has been set in normal type.

1. Introduction

This standard deals with the principles and methods of measurement and assignment of Depreciation and Amortisation for determination of the cost of product or service, and the presentation and disclosure in cost statements.

2. Objective

The objective of this standard is to bring uniformity and consistency in the principles and methods of determining the Depreciation and Amortisation with reasonable accuracy.

3. Scope

This standard shall be applied to cost statements which require measurement, assignment, presentation and disclosure of Depreciation and Amortisation, including those requiring attestation.

4. Definitions

The following terms are being used in this standard with the meaning specified:-

4.1. Amortisation: Amortisation is the systematic allocation of the depreciable amount of an intangible asset over its useful life.

It refers to expensing the acquisition cost minus the residual value of intangible assets such as Franchise, Patents and Trademarks or Copyrights in a systematic manner over their estimated useful economic life so as to reflect their consumption in the production of goods and services.

4.2. Asset: An Asset is a resource;

(a) controlled by an entity as a result of past events; and

(b) from which future economic benefits are expected to flow to the entity.

An asset is a resource controlled by the enterprise as a result of past events from which future economic benefits are expected to flow to the enterprise. In case of some assets which are acquired for safety or environmental reasons, the acquisition of such assets may not provide future economic benefits directly but may be necessary for an entity to obtain the future economic benefits from other assets. Such items also qualify for recognition as assets.

4.3. Cost Object: An activity, contract, cost centre, customer, process, product, project, service or any other object for which costs are ascertained.

4.4. Current asset: An entity shall classify an asset as current when :

(a) it expects to realise the asset, or intends to sell or consume it, in its normal operating cycle;

(b) it holds the asset primarily for the purpose of trading;

(c) it expects to realise the asset within twelve months after the reporting period; or

(d) the asset is cash or a cash equivalent unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

4.5. Depreciation: Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life.

4.6. Depreciable amount: The cost of an asset, or other amount substituted for cost in the financial statement, less its residual value.

4.7. Depreciable property, plant and equipment are tangible assets that:

(a) are held for use in the production of goods or supply of services, for rental to others, for administrative, selling or distribution purposes; and

(b) are expected to be used during more than one accounting period.

Land is not a depreciable asset as it does not have a defined useful life.

4.8. Impairment Loss: An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount.

4.9. Intangible Asset: An intangible asset is an identifiable non-monetary asset without physical substance.

4.10. Residual (salvage) value: The estimated amount that an entity would currently obtain from disposal of an asset, after deducting the estimated costs of disposal, if the assets were already of the age and in the condition expected at the end of its useful life.

4.11. Useful life of asset: Useful life of asset is either:

(a) the period over which a asset is expected to be available for use by an entity ; or

(b) the number of production or similar units expected to be obtained from use of the asset by the entity.

5. Principles of Measurement

5.1. Depreciation and Amortisation shall be measured based on the depreciable amount and the useful life.

The residual value of an intangible asset shall be assumed to be zero unless:

(a) there is a commitment by a third party to purchase the asset at the end of its useful life; or

(b) there is an active market for the asset and:

1. residual value can be determined by reference to that market; and

2. it is probable that such a market will exist at the end of the asset's useful life.

3. The residual value of a property, plant and equipment shall be considered as zero if the entity is unable to estimate the same with reasonable accuracy.

The minimum amount of depreciation to be provided shall not be less than the amount calculated as per principles and methods as prescribed by any law or regulations applicable to the entity and followed by it.

5.2. In case of regulated industry the amount of depreciation shall be the same as prescribed by the concerned regulator.

5.3. While estimating the useful life of a depreciable asset, consideration shall be given to the following factors:

(a) Expected physical wear and tear;

(b) Obsolescence; and

(c) Legal or other limits on the use of the asset.

5.4. The useful life of an intangible asset that arises from contractual or other legal rights shall not exceed the period of the contractual or other legal rights, but may be shorter depending on the period over which the entity expects to use the asset.

If the contractual or other legal rights are conveyed for a limited term that can be renewed, the useful life of the intangible asset shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost. The useful life of a re-acquired right recognised as an intangible asset in a business combination is the remaining contractual period of the contract in which the right was granted and shall not include renewal periods.

The useful life of an intangible asset, in any situation, shall not exceed 10 years from the date it is available for use.

5.5. ***Depreciation of an asset begins when it is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by management.***

An asset which is used only when the need arises but is always held ready for use.

Example: fire extinguisher, stand by generator, safety equipment shall be considered to be an asset available for use.

Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale (or included in a disposal group that is classified as held for sale) or the date that the asset is de-recognized.

5.6. ***Depreciation of any addition or extension to an existing depreciable asset which becomes an integral part of that asset shall be based on the remaining useful life of that asset.***

5.7. ***Depreciation of any addition or extension to an existing depreciable asset which retains a separate identity and is capable of being used after the expiry of the useful life of that asset shall be based on the estimated useful life of that addition or extension.***

5.8. ***The impact of higher depreciation due to revaluation of assets shall not be assigned to cost object.***

5.9. ***Impairment loss on assets shall be excluded from cost of production.***

5.10. ***The method of depreciation used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.***

5.11. ***An entity can use any of the methods of depreciation to assign depreciable amount of an asset on a systematic basis over its useful life.***

For example:

a) Straight-line method;
b) Diminishing balance method; and
c) Units of production method.

5.12. ***The method of amortisation of intangible asset shall reflect the pattern in which the economic benefits are expected to be consumed by the entity.***

5.13. ***The methods and rates of depreciation applied shall be reviewed at least annually and, if there has been a change in the expected pattern of consumption or loss of future economic benefits, the method applied shall be changed to reflect the changed pattern.***

5.14. Items such as spare parts, stand-by equipment and servicing equipment are recognised as property, Plant and Equipment when they meet the definition of Property, Plant and Equipment and depreciated accordingly. Otherwise, such items are classified as inventory and recognised in cost as and when they are consumed.

5.15. Cost of small assets shall be written off in the period in which they were purchased as per the accounting policy of the entity.

5.16. Depreciation of an asset shall not be considered in case cumulative depreciation exceeds the original cost of the asset, net of residual value.

5.17. Where depreciation for an addition of an asset is measured on the basis of the number of days for which the asset was used for the preparation and presentation of financial statements, depreciation of the asset for assigning to cost of object shall be measured in relation to the period, the asset actually utilized.

6. **Assignment of Costs**

6.1. Depreciation shall be traced to the cost object to the extent economically feasible.

6.2. Where the depreciation is not directly traceable to cost object, it shall be assigned based on either of the following two principles:

i. Cause and effect - cause is a process or operation or activity and effect is the incurrence of cost.

ii. Benefits received– depreciation is to be apportioned to the various cost objects in proportion to the benefits received by them.

6.3. Depreciation on an asset which if remains idle or temporarily retired from production of goods and services or remains idle shall be considered as abnormal cost for the period when the asset is not in use.

6.4. The depreciation charged for a period is usually recognised in cost of goods or services.

6.5. Similarly, wherever the property plant and equipment are used for producing another asset, the related depreciation shall form part of cost of such asset.

7. **Presentation**

Depreciation and Amortisation, if material, shall be presented in the cost statement as a separate item of cost.

8. **Disclosures**

8.1. The cost statement shall disclose the following:-

1. ***The basis of distribution of Depreciation and Amortisation to the cost objects.***

2. ***Any credits / recoveries relating to Depreciation and Amortisation.***

3. ***Additional Depreciation on account of revaluation of asset, which is not included in cost.***

4. ***Amount of depreciation that is not included in cost because of temporary retirement of assets from production of goods and services.***

8.2. Disclosure shall be made only where material, significant and quantifiable.

8.3. Disclosures shall be made in the body of the cost statement or as a foot note or in a separate schedule.

8.4. Any change in the cost accounting principles and methods applied for the measurement and assignment of Depreciation and Amortisation during the period covered by the cost statement which has a material effect on Depreciation and Amortisation shall be disclosed. Where the effect of such change is not ascertainable wholly or partly, the fact shall be indicated.