# A Company Purchased A Building For $850,000 On January 1, 2010. As Of December 31, 2014, $200,000 Of

**A Company Purchased A Building For $850,000 On January 1, 2010. As Of December 31, 2014, $200,000 Of** the building's value has been recognized as depreciation. This scenario is a common example in accounting and financial reporting, illustrating how companies account for long-term assets over time. Understanding the intricacies of property depreciation, book value calculation, and the implications for financial statements is essential for business owners, accountants, and investors alike. In this article, we will explore the key concepts surrounding the purchase, depreciation methods, and how to accurately report the building's value on financial statements as of December 31, 2014.

## Understanding the Purchase of a Building as a Long-Term Asset

### The Initial Investment

When a company purchases a building, it records the transaction as a long-term asset on its balance sheet at the purchase price. In this case, the building was acquired for $850,000 on January 1, 2010. This amount includes the purchase price plus any costs necessary to prepare the asset for use, such as legal fees, title fees, or renovation costs.

### Significance of Long-Term Asset Classification

Classifying a building as a long-term asset impacts the company's financial health by:

- Reflecting the company's investment in property
- Enabling depreciation calculations over the asset's useful life
- Providing a more accurate picture of net income and asset value over time

# Depreciation: Spreading the Cost Over Time

## What Is Depreciation?

Depreciation is an accounting method that allocates the cost of a tangible asset over its useful life. It recognizes the wear and tear, obsolescence, or decline in value of the asset as an expense on the income statement.

## Common Depreciation Methods

Different methods can be used to calculate depreciation, including:

1. **Straight-Line Method:** Equal expense allocation over the asset's estimated useful life

2. **Declining Balance Method:** Accelerated depreciation, higher in early years

3. **Units of Production:** Based on usage or output

For simplicity, most companies use the straight-line method unless a different approach better matches the asset's usage.

## Applying Depreciation to the Building

Assuming the company uses the straight-line method and estimates the building's useful life at 50 years with no residual value, the annual depreciation expense would be:

$$
\frac{\$850,000}{50 \text{ years}} = \$17,000 \text{ per year}
$$

Over four years (from January 1, 2010, through December 31, 2014), total depreciation would be:

$$
\$17,000 \times 4 = \$68,000
$$

# Accumulated Depreciation as of December 31, 2014

### Total Depreciation Recognized

In this scenario, the company has accumulated $200,000 of depreciation expense by December 31, 2014. This amount surpasses the simple straight-line estimate, suggesting that either:

- The company used a different depreciation method (accelerated)
- Additional costs or impairments have been factored in
- Revisions to the asset’s useful life or residual value occurred

### Implications of Increased Depreciation

A higher accumulated depreciation affects:

- Net book value of the building
- Taxable income, as depreciation is a deductible expense
- Financial ratios such as return on assets (ROA)

The net book value of the building as of December 31, 2014, is calculated as:

$$
\$850,000 - \$200,000 = \$650,000
$$

This amount appears on the balance sheet and reflects the asset’s remaining undepreciated value.

## Book Value and Its Significance in Financial Reporting

### Definition of Book Value

Book value (or carrying amount) of an asset is the original cost minus accumulated depreciation and impairment costs. It indicates the asset’s value on the books at a specific point in time.

### Importance for Stakeholders

The book value impacts:

- Financial ratios analysis

- Tax calculations
- Decision-making for asset disposal or sale

# Impairment and Revaluation Considerations

## When to Revalue or Recognize Impairment

If the building's market value drops below its book value due to damage, obsolescence, or market conditions, impairment may be required. Conversely, revaluation might be performed if the asset's fair market value appreciates.

## Accounting Standards and Regulations

International Financial Reporting Standards (IFRS) allow revaluation of assets to fair value, while Generally Accepted Accounting Principles (GAAP) tend to favor historical cost with depreciation unless impairment is recognized.

# Reporting the Building's Value as of December 31, 2014

## Balance Sheet Presentation

On the balance sheet, the building would be reported at its net book value:

- Original cost: $850,000
- Less: Accumulated depreciation: $200,000
- Net book value: $650,000

## Impact on Financial Statements

This valuation affects:

- Assets section of the balance sheet
- Depreciation expense reported in the income statement for each period

- Overall financial health and valuation metrics

## Conclusion

Understanding how a building’s value decreases over time through depreciation is vital for accurately preparing financial statements and assessing company performance. In the example of the company that purchased a building for $850,000 on January 1, 2010, and recognized $200,000 of depreciation by December 31, 2014, the net book value of the asset is $650,000. Proper accounting for depreciation not only ensures compliance with standards but also provides stakeholders with a transparent view of the company’s assets and financial position. Whether through straight-line or accelerated methods, companies must diligently track depreciation and impairments to maintain accurate and meaningful financial reports.

## Frequently Asked Questions

### How should A Company record the purchase of the building on January 1, 2010?

The company should record the building at its purchase price of $850,000, including any costs necessary to acquire the asset, and then depreciate it over its useful life.

### What depreciation method is typically used for buildings, and how does it affect the book value as of December 31, 2014?

Common methods include straight-line depreciation, which spreads the cost evenly over the useful life. By December 31, 2014, depreciation accumulated would reduce the book value from the original $850,000, factoring in depreciation expense over that period.

### Given that $200,000 of depreciation has been recorded by December 31, 2014, what is the book value of the building at that date?

The book value would be $850,000 minus $200,000, totaling $650,000 as of December 31, 2014.

## How does the accumulated depreciation impact the company's financial statements?

Accumulated depreciation reduces the asset's book value on the balance sheet and increases expenses on the income statement, affecting net income and overall financial position.

## What are the tax implications of depreciation on the building for the company's financial reporting?

Depreciation expense reduces taxable income, providing tax benefits. However, for financial reporting, it reflects the systematic allocation of the asset’s cost over its useful life, which may differ from tax depreciation methods.

# Additional Resources

Comprehensive Review of A Company’s Building Investment from 2010 to 2014

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Introduction

When evaluating a company’s real estate asset, particularly a building purchased for a substantial amount like $850,000, it’s crucial to analyze the asset’s depreciation, valuation changes, and overall financial impact over time. The scenario in focus involves a company acquiring a building on January 1, 2010, for $850,000, with a noteworthy depreciation of $200,000 by December 31, 2014. This review delves into the various aspects surrounding this investment, including depreciation methods, accounting implications, property valuation considerations, and strategic insights.

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Background and Initial Purchase Details

Acquisition Overview

- Purchase Date: January 1, 2010
- Purchase Price: $850,000
- Property Type: Commercial/industrial/residential (assumed; details can influence depreciation methods)
- Funding Source: Typically financed via cash, loan, or a combination
- Intended Use: Operating premises, investment property, or speculative development

The initial purchase reflects a significant capital investment, indicating the company's strategic interest in real estate as part of its asset portfolio. The valuation at acquisition often considers market value, appraised worth, and expected income generation potential.

Initial Accounting Implications

- Asset Recognition: The building is recorded as a fixed asset at its purchase cost.
- Depreciation Start Date: January 1, 2010
- Estimated Useful Life: Varies depending on property type—commonly 27.5 years for residential or 39 years for commercial under U.S. GAAP; shorter or longer based on specific circumstances.
- Residual Value: Assumed to be zero unless specified.

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Depreciation Analysis (2010–2014)

Total Depreciation Recorded

- Total Depreciation by December 31, 2014: $200,000
- Period: 5 years (2010–2014)

This results in an average annual depreciation expense of approximately $40,000, assuming straight-line depreciation:

$$
\text{Annual Depreciation} = \frac{\$850,000}{\text{Useful Life (e.g., 20–30 years)}} \approx \$40,000
$$

But the total depreciation of $200,000 over five years suggests an accelerated depreciation or a different estimated useful life.

Depreciation Methods and Their Impacts

- Straight-Line Depreciation: Equal expense annually; simplifies accounting and provides predictable expense recognition.

$$
\text{Annual Depreciation} = \frac{\text{Cost} - \text{Residual Value}}{\text{Useful Life}}
$$

- Declining Balance or Accelerated Methods: Front-load depreciation expenses, which could explain the $200,000 depreciation over five years if a shorter useful life or accelerated method was used.

- Impact of Depreciation Choice:
- Financial Statements: Lower net income in early years with accelerated depreciation.
- Tax Implications: Accelerated methods often provide tax benefits by deferring taxable income.

Residual Book Value (Net Book Value)

- Initial Cost: $850,000
- Less Accumulated Depreciation: $200,000
- Net Book Value (as of Dec 31, 2014): $650,000

This figure reflects the remaining undepreciated value of the building, which is critical for subsequent valuation, impairment testing, and potential sale considerations.

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Property Valuation and Market Considerations

Fair Market Value vs. Book Value

- The book value of $650,000 as of December 31, 2014, may differ significantly from the property’s current fair market value.
- Market conditions, location, property condition, and economic factors influence real estate valuation.

Appreciation or Depreciation of Property Value

- Appreciation Factors:
- Economic growth in the area
- Infrastructure improvements
- Increased demand for commercial/residential space
- Depreciation Factors:
- Physical deterioration
- Obsolescence
- Damage or environmental factors

If the property appreciated, the recorded book value might be below the actual market value, leading to potential revaluation or impairment considerations.

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Accounting and Tax Implications

Depreciation and Tax Deductions

- The depreciation expense reduces taxable income, providing cash flow benefits.
- The $200,000 depreciation over five years likely contributed to lower tax liabilities during this period.

Impairment Considerations

- If the property’s market value declines below the book value due to economic downturns or damages, impairment losses may need to be recognized.

- Regular impairment testing ensures the asset’s carrying amount reflects its recoverable amount.

Dispositions and Gains/Losses

- Upon eventual sale or disposal, the difference between sale proceeds and the net book value results in a gain or loss.
- For instance, if the company sells the building for more than $650,000, it realizes a gain; if less, a loss.

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Strategic and Financial Insights

Investment Performance

- A $200,000 depreciation over five years indicates the company’s approach to asset management and tax planning.
- The remaining net book value of $650,000 could be leveraged for further investments or refinancing.

Portfolio Diversification

- Real estate can act as a hedge against inflation and provide consistent income streams if leased.
- The building’s depreciation schedule impacts the company’s reported net income and cash flows.

Future Outlook

- Real estate valuation as of 2014 should incorporate trends, anticipated market movements, and potential redevelopment opportunities.
- The company might consider reassessment or revaluation depending on market conditions.

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Additional Considerations and Risks

- Environmental and Regulatory Risks: Changes in zoning laws, environmental regulations, or property taxes can impact valuation and profitability.
- Physical Risks: Deterioration, damage, or obsolescence can reduce the building’s value and necessitate capital expenditures.
- Market Risks: Fluctuations in the local real estate market can affect both the property’s fair value and the company's strategic plans.

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Conclusion

The purchase of a building for $850,000 on January 1, 2010, and the subsequent depreciated value of $650,000 by December 31, 2014, reflects a period of active asset management, strategic depreciation planning, and market considerations. The $200,000 depreciation indicates the company's efforts to align accounting practices with economic realities and tax optimization strategies.

Understanding the nuances of depreciation methods, property valuation, and market dynamics is essential for stakeholders evaluating the company’s financial health and long-term prospects. As the property continues to age and market conditions evolve, ongoing assessments, revaluations, and strategic decisions will shape the asset’s future role within the company's portfolio.

In essence, this case exemplifies the importance of integrating accounting standards, market insights, and strategic planning to optimize real estate investments effectively.

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