

Accounting 402
Illustration of a change in accounting principle

This accounting treatment was eliminated by FAS Statement No. 154

Assume the following facts concerning a plant asset for the Washington Company:

Asset cost	\$360,000
salvage value	\$ 10,000
estimated useful life	10 years
depreciation method:	Double declining balance

This asset is depreciated during year 1 and year 2 using the Double declining balance method. During year 3, the management of the company decided that the straight line method of depreciation would be more appropriate.

Discuss and illustrate how this change in accounting would be reported.

Step one: Determine the differences in depreciation

	Year		
	1	2	3
depr- Double declining balance			
depr- Straight-line			
Difference			

Cumulative effect = sum of year 1 and year 2 differences = _____ Note: Do not include year 3.

Step two: Determine the tax effect of the change

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Step three: Prepare the journal entry(ies) to effect the change:

Date	ACCOUNT	DR	CR
01/01/03			
	To record the cumulative effect of a change in accounting principle		

Date	ACCOUNT	DR	CR
01/01/03			
	To record the tax effect of a change in accounting principle		

Partial Comparative Income statement for 20X3:
Washington Company
Comparative Income Statement-Partial
for the Years Ended December 31,

	<u>20X3</u>	<u>20X2</u>
Depreciation expense	_____	_____
~~~~~	~~~~~	~~~~~
~~~~~	~~~~~	~~~~~
Income before extraordinary items and cumulative effect of a change in accounting principle	\$52,000	\$50,000
Extraordinary item, net of tax	(5,000)	2,000
Cumulative effect of a change in accounting principle, net of tax	_____	_____
Net income	=====	=====
Earnings per common share:		
Income before extraordinary items and cumulative effect of a change in accounting principle	_____	_____
Extraordinary item, net of tax	_____	_____
Cumulative effect of a change in accounting principle, net of tax	_____	_____
Net income	=====	=====
Pro-forma presentation, assuming retroactive application of newly adopted accounting principle:		
Income Before extraordinary items	=====	=====
Net income	=====	=====
Earnings per share:		
Income before extraordinary items	=====	=====
Net income	=====	=====