



**The Institute of  
Chartered Accountants  
of Pakistan**

**HEAD OFFICE**

Circular No. 01/2009

February 26, 2009

**ALL MEMBERS OF THE INSTITUTE**

Dear Member

**ISSUANCE OF ACCOUNTING TECHNICAL RELEASE TR-31 –  
“ANNUITY METHOD OF DEPRECIATION”**

The Council of the Institute in its 204<sup>th</sup> meeting held on January 23, 2009 has decided to issue the enclosed TR-31 “*Annuity Method of Depreciation*”.

A revised Sectional Index is also enclosed, which is to be filed in Section C of Part I in Members' Handbook Volume II.

Yours truly

Muhammad Asif Iqbal  
Director Technical Services

Encl.: TR – 31 & Revised Sectional Index

(Established under the Chartered Accountants Ordinance, 1961-X of 1961)

## SECTIONAL INDEX

### PART I

#### SECTION C TECHNICAL RELEASES

- TR-1 **Withdrawn** -( Capitalization of Interest on Loan)
- TR-2 **Withdrawn**-( Financial Statement Presentation – Credit Cards)
- TR-3 **Withdrawn**-( Depreciation Treatment in Tax Holiday Companies)
- TR-4 **Withdrawn**-( Gratuity – Provision in the Accounts of Company)
- TR-5 IASB Standards-Council's Statement on Applicability  
(Revised - 2006)
- TR-6 Fixed Assets Inventory and Records (Reformatted - 2004)
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- TR-8 Clarification Regarding Basis of Calculation of Workers' Profit  
Participation Fund (Reformatted 2004)
- TR-9 **Withdrawn**-( Treatment of Post-dated Cheques or  
Promissory Notes )
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- TR-11 Depreciation on Idle Property, Plant and equipment  
(Reformatted - 2004)
- TR-12 **Withdrawn**-( Debt Extinguishment)
- TR-13 **Withdrawn**-( Accounting for Compensated Absences)
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- TR-15 Bonus Shares-Accounting Treatment (Reformatted 2004)

- TR-16 **Withdrawn**-( Pending Litigation Settled in Favour of Client After the Balance Sheet date).
- TR-17 **Withdrawn**-(Finished Pieces of Equipment held by Manufacturer for Customers)
- TR-18 **Withdrawn**-(Good Accounting Software )
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- TR-22 Book Value per Share (Revised - 2002)
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- TR-24 Exchange Risk Fee-Accounting Treatment (Reformatted - 2000)
- TR-25 **Withdrawn**-( Prudential Regulations for Banks )
- TR-26 **Withdrawn**-( Export Quota – Accounting Treatment )
- TR-27 IAS 12, Income Taxes (Revised 2003)
- TR-28 **Withdrawn**-( Golden Handshake – Accounting For )
- TR-29 Carry-Over-Transactions (COT)
- TR-30 Final Tax Accounting
- TR-31 Annuity Method of Depreciation

**ANNUITY METHOD OF DEPRECIATION****THE ISSUE**

- 1.1.1 Whether Annuity Method of Depreciation is an appropriate method of depreciation under IFRS.

**TECHNICAL COMMITTEE RECOMMENDATIONS**

- 2.1 The annuity method is a compounded interest method whereby the depreciation is calculated based on the assumption that depreciation plus the normal cost of capital to finance the assets are constant over the life of the assets. This results in lower depreciation charges in the earlier years of the assets life and higher charges in the later years.
- 2.2 Although IAS 16 'Property, Plant and Equipment' does neither expressly prohibit the annuity method nor mentions it as a permissible method, it states that the depreciation method should reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity (paragraph 60 of IAS 16). Therefore, depreciation should reflect the actual diminution of the value of the asset or the direct revenue streams arising from such assets duly ignoring indirect and inconsistent revenues and other associated costs which can, however, not be considered to be a part of the pattern of flow of economic benefits from such assets. This implies the straight-line method or the reducing balance method to be more appropriate for most of the leasing assets.
- 2.3 Further it needs to be noted that in case of applicability of annuity method of depreciation, the depreciation charged in the initial years is on the lower side and accordingly, there arises an inevitable risk that the carrying value of such assets would exceed their fair values, which might create accounting issues in future with regard to impairment testing in line with IAS -36 ' .
- 2.4 In view of the aforesaid, the Committee is of the considered opinion that annuity method of depreciation under IFRS is not an appropriate method of depreciation particularly for assets given on operating lease for a determined period.