# CALCULATING DEPRECIATION AND INVENTORY CHANGES

**Calculating Depreciation**

Depreciation is defined by the Internal Revenue Service as "an annual allowance for the wear and tear, deterioration or obsolescence of the property." Most types of tangible property are depreciable, such as buildings, machinery, vehicles and equipment, but land is not. When estimating depreciation, the Center for Farm Financial Management suggests using 10 percent per year of the purchase price of machinery and equipment, 15 percent per year of the purchase price of titled vehicles, and 5 percent per year of the purchase price of buildings and other improvements. Use the table below to estimate the total value of depreciation for your farm assets. You will use this information when compiling farm expenses. A spreadsheet is available to assist with these calculations at http://misadocuments.info/OrganicTransitionPlanner_spreadsheets.xlsx.

|  | Beginning $ | Purchases $ | Sales $ | Ending Value $ | Depreciation % | Depreciation Expense $ |
|---|---|---|---|---|---|---|
|  | + | + | − | = | * | = |
| Machinery (a) |  |  |  |  | 10% (0.1) |  |
| Vehicles (b) |  |  |  |  | 15% (0.15) |  |
| Buildings (c) |  |  |  |  | 5% (0.05) |  |
| Breeding livestock replacements (d) |  |  |  |  | 25% (0.25) |  |
| Total Depreciation  = (a+b+c+d) |  |  |  |  |  |  |

**Calculating Inventory Changes**

Inventory changes affect net farm income and should be accounted for each year. Use the space below to record the value of inventory at the beginning of the year and at the end of the year. Subtract the ending inventory value from the beginning inventory value. You will be asked to add or subtract the final change in inventory when calculating net farm income on **Worksheet 2T.14: Current Income Statement**.

|  | Beginning Inventory $ | Ending Inventory $ | Ending–Beginning Inventory $ |
|---|---|---|---|
| Crops and feed (a) |  |  |  |
| Livestock held for sale (b) |  |  |  |
| Accounts receivable (c) |  |  |  |
| Hedging accounts (d) |  |  |  |
| Other inventory (e) |  |  |  |
| Prepaid expenses and supplies (f) |  |  |  |
| Growing crops (g) |  |  |  |
| Inventory change (h) = (a+b+c+d+e+f+g) |  |  |  |
| Accounts payable (i) |  |  |  |
| Accrued interest (j) |  |  |  |
| Inventory change (k) = (i+j) |  |  |  |
| TOTAL INVENTORY CHANGE = (h-k) |  |  |  |