

Question

A firm is investing in an equipment which falls in 5-years MACRS. The cost of the machine is \$200,000 and the firm spent \$20,000 for shipping, at the end of its life the machine could be sell for \$30,000. If the firm is in 34% tax bracket compute the tax savings from depreciation in year-5.

Answer: =

Cost of machine: - \$200000

Shipping charge: - \$20000

Sold price salvage: - 30000

34% bracket compute tax saving

Depreciation in year 5 = Assets + Shipping charge + Tax 34%-Sold Price/Depreciation in years 5

$\$200000 + \$20000 + \$74800(\text{Tax}) - \$30000/5$

$\$294800 - \$30000/5$

$\$264800/5 = 52960$

After Less Tax:-

$\$200000 + \$20000 - \$30000/5$

$\$220000 - \$30000/5$

$\$190000/5 = \38000

$\$52960 - \$38000 = \$14960$

Explanation:

1. Sunk costs: costs that have accrued in the past, or will be paid regardless of the decision
2. Opportunity costs: costs of lost options
3. Side effects: Positive side effects, benefits to other projects, Negative side effects, costs to other projects

4. Changes in net working capital

5. Financing costs

6. Taxes