**Fixed Assets – Part 2 Script**

Slide 1: In this presentation, we will continue our discussions of accounting for Fixed Assets or PP&E. If you haven’t yet, you might want to view the Fixed Assets Part 1 presentation as much of what we learn here builds on Part 1 material.

Slide 2: In Part 1, we saw there were 4 main considerations when working with Fixed Assets. Those are: Valuation, Cost Allocation, Improvements and Disposal. In part 1, we covered Valuation and Cost Allocation. Improvements and Disposal will be covered in this Part 2 presentation.

Slide 3: The next of our four main considerations has to do with what we call Improvements. These are different that normal repairs and maintenance in that Improvements – also called Betterments – will Extend the useful life of an asset, Increase the salvage value of an asset, or both.

Improvements are Capitalized, or depreciated over the life of the asset. Repairs and Maintenance are not – they are considered Period Expenses and are expensed in the period they are incurred.

Slide 4: Let’s look at two different Scenarios. Suppose we spend $3,000 to replace the motor on our delivery truck. This is expected to increase the life of the truck for another 3 years. We record this 3,000 in the Truck account as this is definitely an improvement – extending the useful life.

In the next scenario, we repair the bumper of the truck for $1,500. This is a normal Repairs and Maintenance expense; neither the useful life nor the salvage value is increased.

Slide 5: When we first set up a depreciation schedule for an asset, we are relying on assumptions for useful life and salvage value. While these are best guesses at the time, things can change – we may use the asset more or less than originally considered. There also may have been improvements. Luckily, we can revise our depreciation expense quite easily with the formula shown.

This formula takes the Book Value less Revised Salvage Value and divides that by the Revised Remaining Life. We can use this formula if salvage value changes, if the expected life changes or both. Let’s see how this works on the following slide.

Slide 6: Let’s assume we have the same asset we depreciated in Part 1, Slide #7. Let’s assume further that, at the end of Year 2, we discover we are using the machine more than planned. This has caused the salvage value to drop to $1,000 and the life to decrease to four years.

If we plug these new assumptions into the formula from slide #3, and use the book value of $17,000 from the end of year 2, we get a new depreciation expense of $8,000 per year. I’ve replaced years 3 and 4 of the depreciation schedule with the new depreciation expense. We can see that, at the end of year 4, we have arrived at the revised 1,000 salvage value.

Slide 7: Now we will discuss the last consideration we have with respect to PP&E – disposal. Selling and donating assets are a few ways we can dispose of assets and I will show examples of each.

It’s important to remember that assets stay on the books until disposal (the Cost Principle in action). Upon disposal we need to do a couple things: we remove the asset, we remove accumulated depreciation associated with that asset, account for any cash received and account for any gain or loss on disposal.

Slide 8: I’m using the depreciation schedule we’ve seen a few times before and we will assume in this slide that the asset is sold at the end of year 3 for $14,000.

The book value of this asset is $12,000 and we therefore have a gain of $2,000 on disposal. To journalize this, we debit Cash for $14,000 and debit Accumulated Depreciation for $15,000 (obtained from the schedule). We credit the Asset for the full $27,000 and credit Gain on Disposal $2,000 (total debits = 29,000 and total credits = 29,000).

Slide 9: On this slide, we’ll use the same schedule we’ve been using, however we assume this time we sell the asset for $10,000 at the end of year 3. Since the book value of the asset is $12,000, we have a $2,000 loss on disposal.

To journalize this, we debit Cash for $10,000, debit Accumulated Depreciation for $15,000, debit Loss on Disposal for $2,000 and credit the Asset for $27,000 (total debits = 27,000 and total credits = 27,000).

Slide 10: In this last slide, we’ll use the same $27,000 asset, but this time assume the asset is donated to a charity at the end of year 3.

To journalize this, we debit Charitable Donations (an expense) for the book value of $12,000, debit Accumulated Depreciation for $15,000 and credit the Asset for $27,000 (total debits = 27,000 and total credits = 27,000).

Slide 11: I hope this has helped your understanding of the treatment of Fixed Assets / PP&E. Good luck with your studies.