

OREGON ACCOUNTING MANUAL	
SUBJECT: Accounting and Reporting	Number: 15.60.25
DIVISION: Chief Financial Office	Effective date: August 1, 2010
Chapter: Accounting and Financial Reporting	
Part: Capital Assets	
Section: Capital Asset Impairments	
APPROVED: George Naughton, Chief Financial Officer	Signature on file

PURPOSE: This policy provides guidance on accounting and financial reporting for impairments of capital assets and for insurance recoveries related to impairments of capital assets.

For insurance recoveries related to theft or embezzlement of cash or other monetary assets, refer to [OAM 15.35.00](#).

AUTHORITY: **ORS 293.590**
GASB Statement No. 42

APPLICABILITY: This policy applies to all state agencies included in the State’s annual financial statements, except for those agencies specifically exempted by OAM Policy 01.05.00.

DEFINITIONS: **Impairment:** *A significant and unexpected decline in the service utility of a capital asset.*

NOTE: The events or changes in circumstances that lead to impairments are not considered normal and ordinary. Such events or changes in circumstances are prominent and most likely have prompted discussion by agency management or the media. Absent such conditions, agencies are not required to perform additional procedures to identify impaired capital assets beyond those already performed as part of their normal operations.

POLICY:

101. Agency management must ensure the proper accounting and reporting of capital asset impairments and related insurance recoveries.
102. When a capital asset has been permanently impaired, write down the carrying value of the asset by the amount of the impairment loss. If an impairment is temporary (not permanent), do not adjust the asset’s carrying value.
103. To calculate the amount of a capital asset impairment loss, use one of the four methods outlined in the accompanying procedure.

104. Recognize insurance recoveries only when:
- *Realized* (received) by recording the cash receipt, or
 - *Realizable* (a claim is pending for which the insurer has admitted or acknowledged coverage) by accruing a receivable.
105. When an insurance recovery and the related impairment loss occur in the same fiscal year, offset the insurance recovery against the impairment loss by using the same comptroller object to record both (C/O 7510 - *Gain/Loss on Capital Asset Impairments*).
106. If an insurance recovery is received in a subsequent fiscal year, record the insurance proceeds in C/O 7511 - *Insurance Recovery Subsequent to Loss*. Do not record the insurance recovery in the same comptroller object used to record the related impairment loss.
107. After recognizing an impairment loss, do not reverse the loss in future years, even if the events or circumstances underlying the impairment change.
108. Record the restoration or replacement of the impaired capital asset using the insurance recovery as a separate transaction.

PROCEDURE:

Indicators of Potential Impairment

109. Impairment occurs when events or changes in circumstances suggest that the service utility of a capital asset may have significantly and unexpectedly declined. Common indicators of potential impairment include:
- a. Evidence of physical damage, such as a building damaged by fire or flood that requires restoration efforts to restore service utility
 - b. Changes in laws or regulations and changes in environmental factors, such as new water quality standards that a water treatment plant does not meet (and cannot be modified to meet)
 - c. Technological changes or evidence of obsolescence, such as a major piece of diagnostic or research equipment that is rarely used because newer equipment provides better service
 - d. A change in the manner or expected duration of use of a capital asset, such as closure of a school prior to the end of its useful life
 - e. Construction or development stoppage, such as stoppage of construction of a building or stoppage of software development, due to lack of funding.

NOTE: A change in demand for the services of a capital asset is not an indicator of impairment. However, changes in demand may be linked to conditions such as those listed above and, under those circumstances, capital assets should be tested for impairment. For example, if demand for the processing services of a mainframe computer decreases because former users of the mainframe transitioned to PC- and server-based systems (evidence of obsolescence), the mainframe should be tested for impairment. However, if the decrease in demand is due to the completion of a special project that required large amounts of processing time on a mainframe computer that also runs other applications, the change in demand is not an indicator of impairment; a test for impairment is not required.

Testing for Impairment

110. Once you have identified a potentially impaired capital asset, test the asset to determine whether both of the following factors are present. (Refer to the flowchart in **Appendix A** for assistance in the decision-making process.)
- The magnitude of the decline in service utility is *significant*; and
 - The decline in service utility is *unexpected* (i.e., event or change must be outside the normal life cycle of the capital asset, including outside the normal effects of age and use).
111. If the test for impairment results in a finding that no impairment has occurred, reevaluate the estimates used in the depreciation calculations (remaining useful life and salvage value) and adjust them, if necessary. Account for any changes on a prospective basis only. Do not record a prior period adjustment. For more information on depreciation and amortization, refer to **OAM 15.60.20**.

Calculation of Impairment Loss

112. The following chart specifies the measurement method to use for calculating the impairment loss associated with each of the common impairment indicators.

Impairment Indicator	Measurement Method
Evidence of physical damage	Restoration cost approach
Changes in laws or regulations and changes in environmental factors	Service units approach
Technological changes or evidence of obsolescence	Service units approach
Change in the manner or expected duration of use	Service units approach <u>or</u> deflated depreciated replacement cost approach
Construction stoppage	Lower of carrying value or fair value

113. **Restoration Cost Approach:** Under this approach, derive the amount of impairment from the estimated costs to restore the utility of the capital asset. *Restoration cost* is the cost necessary to return the capital asset to its original condition and does not include any amount for improvements or additions. Estimate the restoration costs in current year dollars, and then use one of two options to convert the estimated restoration costs to historical costs.

Option 1: *Use current year dollars.* Determine the replacement cost of the *entire* asset in current year dollars.

- Calculate a ratio by dividing the restoration cost (in current year dollars) by the current replacement cost. The resulting percentage represents the damaged portion of the capital asset.
- Multiply that percentage by the carrying value (historical cost less accumulated depreciation) to calculate the impairment loss.

Option 2: *Use year of acquisition dollars.*

- Using an appropriate cost index, convert the restoration cost (in current year dollars) to historical cost.
- Calculate a ratio by dividing the deflated restoration cost by the historical cost.
- Multiply the resulting percentage by the carrying value (historical cost less accumulated depreciation) to calculate the impairment loss.

114. **Service Units Approach:** This approach isolates the historical cost of the service utility of the capital asset that cannot be used. Using one of the three methods described below, determine the amount of impairment by evaluating the service provided by the capital asset (either maximum estimated service units or total estimated service units throughout the life of the capital asset) *before* and *after* the event or change in circumstance.
- a. Determine the amount of impairment loss by calculating the ratio of *lost units to the total units originally expected over the life of the asset* and multiply that ratio by the historical cost of the capital asset.
 - b. Determine the amount of impairment loss by calculating the ratio of *lost units per period to the total units per period originally expected over the life of the asset* and multiply that ratio by the carrying value of the capital asset.
 - c. Calculate the amount of impairment loss by subtracting the value of units remaining after the impairment from the carrying value of the capital asset. Calculate the value of remaining units by multiplying the unit cost by the number of remaining units. Calculate the unit cost by dividing the historical cost by the *total units originally expected over the life of the asset*.
115. **Deflated Depreciated Replacement Cost Approach:** This approach replicates the historical cost of the service produced. Estimate a current cost for a capital asset to replace the current level of service. Depreciate this estimated current cost to reflect the fact that the capital asset is not new, and then deflate it to convert it to historical cost dollars.
- a. Using current value, estimate a hypothetical replacement cost for an equivalent asset specifically suited to the new manner or expected duration of use.
 - b. Depreciate the cost of the replacement asset by multiplying the depreciated ratio of the actual asset (carrying value over historical cost) by the estimated replacement cost.
 - c. Using an appropriate cost index, deflate the cost of the depreciated replacement asset to restate it on the basis of acquisition year dollars.
 - d. Subtract the deflated depreciated replacement value from the carrying value of the impaired asset to calculate the impairment loss.
116. **Lower of Carrying Value or Fair Value:** Report capital assets impaired from stoppage of construction or stoppage of development (in the case of internally generated intangible capital assets) at the lower of carrying value or fair value. Calculate the impairment loss by subtracting the fair value of the asset (i.e., net realizable value) from the carrying value.

Permanently Retired Assets

117. If an agency *permanently* retires a capital asset from service (either voluntarily or involuntarily) and does not immediately sell or otherwise dispose of the asset, the asset ceases to be a capital asset (because it no longer will be *used in operations*) and must be reclassified to state owned property held for sale (GL 0927). Report assets held for sale at the lower of carrying value or fair value.

Accounting for Impairments

118. When a capital asset is accounted for in a **proprietary fund** or **fiduciary fund**, account for the impairment loss and related insurance recovery within those funds. When a capital asset is accounted for in the **government-wide reporting fund**, record the impairment loss in the government-wide reporting fund; however, record the related insurance recovery in a **governmental fund**.
119. To recognize the impairment of a capital asset currently in service, reduce the carrying value by recording the entire impairment as an increase in accumulated depreciation. To recognize the impairment of a capital asset currently under construction or development, record the entire impairment as a decrease in the cost of the asset. Use the same transaction code to record an impairment loss in a proprietary fund, fiduciary fund, or the government-wide reporting fund.

Adjustment to Accumulated Depreciation

TC 542: To record an impairment loss using comptroller object 7510 – Gain/Loss on Capital Asset Impairments.

DR 3600 GAAP Expenditure Offset (C/O 7510)	500,000
DR 3018 Invested in Capital Assets	500,000
CR 3074 Change in Capital Assets	500,000
CR 08XX Accum Depreciation/Amortization-Capital Asset	500,000

Adjustment to Construction in Progress

TC 545R: To record an impairment loss for construction stoppage using comptroller object 7510 – Gain/Loss on Capital Asset Impairments.

DR 3600 GAAP Expenditure Offset (C/O 7510)	500,000
DR 3018 Invested in Capital Assets	500,000
CR 3074 Change in Capital Assets	500,000
CR 0861 Construction in Progress	500,000

Accounting for Insurance Recoveries

120. When an insurance recovery and the related impairment loss occur in the same fiscal year, report the impairment loss net of the insurance recovery by using the same comptroller object to record both the loss and the recovery.

TC 172: To record receipt of insurance recovery (in the same fiscal year as the impairment), using comptroller object 7510 – Gain/Loss on Capital Asset Impairment.

DR 0065 Unreconciled Deposit	350,000
CR 3500 Expenditure – Cash (C/O 7510)	350,000

121. When the insurance recovery is received in a fiscal year subsequent to the fiscal year in which the related impairment loss occurred, record the insurance recovery as a reduction of expense using comptroller object 7511.

TC 172: To record receipt of insurance recovery (in a subsequent fiscal year), using comptroller object 7511 – Insurance Recovery Subsequent to Loss.

DR 0065 Unreconciled Deposit	350,000
CR 3500 Expenditure – Cash (C/O 7511)	350,000

122. When the Department of Administrative Services (DAS), Risk Management transmits insurance proceeds to other state agencies electronically (rather than by issuance of a warrant), the receiving agency uses TC 741, rather than TC 172. DAS uses TC 740 to record a balanced transaction.

Financial Statement Reporting

123. The Statewide Accounting and Reporting Services (SARS) reports impairment gains/losses incurred by proprietary funds in the statement of revenues, expenses, and changes in fund net assets as an operating expense, a **special item**, or an **extraordinary item**, as appropriate. Impairment losses in the government-wide reporting fund are reported in the statement of activities as a program expense in the applicable function for governmental or business-type activities, a special item, or an extraordinary item, as appropriate.
124. SARS reports an impairment loss net of the associated insurance recovery when the recovery and loss occur in the same fiscal year. An insurance recovery received in a subsequent fiscal year is reported in proprietary funds in the statement of revenues, expenses, and changes in fund net assets as non-operating revenue or an extraordinary item, as appropriate. SARS reports an insurance recovery received in a subsequent fiscal year in the government-wide reporting fund in the statement of activities as program revenue in the applicable function for governmental or business-type activities or as an extraordinary item, as appropriate.
125. In governmental fund financial statements, SARS reports an insurance recovery as an other financing source or extraordinary item, as appropriate.
126. The GAAP level profiles (D08) established for comptroller object 7510, Gain/Loss on Capital Asset Impairments, and 7511, Insurance Recovery Subsequent to Loss, ensure that insurance recoveries are reported correctly in the financial statements, even though both comptroller objects are treated as a reduction of expense for budgetary purposes. SARS uses the information provided by agencies in the year-end General Disclosures to ensure that impairment losses and insurance recoveries are properly reported in the financial statements.

Disclosure Requirements

127. SARS discloses a general description, the amount, and financial statement classification of impairment losses and insurance recoveries in the notes to the financial statements.
128. SARS also discloses the carrying amount of impaired capital assets that are idle at year end, regardless of whether the impairment is considered permanent or temporary.

APPENDIX A

CAPITAL ASSET IMPAIRMENT DECISION PROCESS

