Commonwealth of Massachusetts

OFFICE OF THE COMPTROLLER

ONE ASHBURTON PLACE, 9TH FLOOR
BOSTON, MASSACHUSETTS 02108
TELEPHONE (617) 727-5000
WWW.MASS.GOV/COMPTROLLER

THOMAS G. SHACK III, ESQ.
COMPTROLLER

MMARS Policy: **Fixed Assets**

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Impairment of Fixed or Other Assets and Insurance Recoveries

Executive Summary

The Government Accounting Standards Board (GASB) has released Statement No. 42 *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, applicable starting in FY06. The Commonwealth is required to evaluate prominent events or changes in circumstances affecting fixed or other assets, such as cash, to determine whether impairment has occurred.

Considerations

In the case of a theft, fire, flood, obsolescence or other event regarding the usefulness of an asset, be it fixed or non-fixed such as cash, departments need to evaluate the usefulness or availability of that asset in the future. This may require outside assistance from an appraiser and or the Office of the Comptroller (CTR) to determine significance and applicability. Impairment must be conspicuous – e.g. known to the Commonwealth that a material event has occurred. These events may be known by management or the media.

Policy

All impaired assets if significant (greater than $100,000 in value) need to be reported to the CTR General Accounting Bureau within 7 days of event occurrence. For all unaccounted for variances, losses, shortages or thefts of funds or property, the rules established under Chapter 647 of the Acts of 1989 apply. The CTR General Accounting Bureau will work with you to determine if impairment exists and if there is an event that needs to occur in MMARS.

"Impairment" may include physical damage, enactment or approval of laws or regulations or other changes in environmental factors, technical changes or evidence of obsolescence, changes in the manner or duration of use of an asset and construction stoppage.

A fixed asset is impaired if **both:**

(a) The decline in the ability to use an asset is large in magnitude and

(b) The event is outside the normal life cycle of a capital asset.

Assets that are impaired that will no longer be of service to the Commonwealth will need to be either evaluated for either the lower of their fair market value or their "book" value after depreciation with their value adjusted on MMARS accordingly.

Insurance recoveries associated with impairment should be reported as a separate transaction, especially if in a different fiscal year.

Role of the Office of the Comptroller (CTR)

The CTR General Accounting Bureau will work with the affected department to determine and document if impairment exists and if there is an event that needs to occur in MMARS, using the following decision tree:

1. Is the asset impairment significant (>$100,000) resulting in an unexpected decline in the usefulness of the asset and is it unexpected. For example, a wing of a building is no longer useful because of newly discovered asbestos. Or is physical damage present from fire or flood when the level of damage is such that restoration efforts are needed to restore the asset to useful service?
2. Is there a decline in service utility? For example, if an information system can only run at 80% instead of 100% due to obsolescence, enactment or approval of laws or regulations or changes in environmental factors. Another example is that new water quality standards have rendered a treatment system obsolete.
3. Is there technological obsolescence such as a major piece of equipment that no longer is in use due to better equipment becoming available?
4. Is there a change in the duration of use? For example a building closing prior to its 40-year life cycle being completed?
5. Is there a construction stoppage on a new asset due to lack of funding?
6. Is the impairment temporary or permanent?

Impairment exists if these factors are significant (>$100,000 effect)
<u>AND</u> the occurrence is unexpected.

Impairment Measurement and Reporting

To measure the amount of impairment, CTR will need to work with the department to determine if the above factors exist. If so, the portion of the asset to be adjusted would depend on the usefulness after repair (if applicable.) Usefulness assessments will need to be known as soon as possible. Other items that will need to be known include:

1. What is the estimated cost to restore the asset to full utility?
2. What would be the current cost to replace the asset?
3. What is the salvage value, if any?

If there is impairment, these items will be used to measure impairment, given the facts of the occurrence.

Assets no longer in use or construction stoppages

Assets no longer in use or that are part of a permanent construction stoppage will have their value adjusted to fair market value or "book" value in MMARS, whichever is lower. For assets where this occurs, an appraisal in writing needs to be provided by the department to the Office of the Comptroller as soon as possible.

Reporting

Asset Impairment changes will require the use of **Increase or Decrease of a Fixed Asset (FI) documents (for assets still in use) or Fixed Asset Disposition (FD)** for permanent losses. If the loss is permanent, the Commonwealth will report these losses as part of its GAAP financial statements. If losses are deemed to be temporary by the department in conjunction with and with the concurrence of CTR after evidence is reviewed will be adjusted.

Idle Capital Assets

Capital assets that are unused or idle, in excess of $100,000 will be disclosed to the Office of the Comptroller as part of the department's GAAP reporting package beginning in FY06 and forward.

Insurance and other Recoveries including those from Embezzlement

Pursuant to M.G.L. c. 29, § 30, "*No officer or board shall insure any property of the Commonwealth without special authority of law*." Therefore, unless a department has special legislation to insure Commonwealth property, the department may not purchase insurance for property damage. Authorized insurance recoveries will be reported as separate transactions within the General Fund and will not be netted against any current or future expenditure, absent legislation to the contrary. Normal Cash Receipt (CR)

transactions will be used with a revenue source code 6900 with separate documentation forwarded to the CTR General Accounting Bureau, which will track these recoveries.

Internal Controls

All FI documents need to be submitted to the CTR General Accounting Bureau with amounts and actions agreed upon between the Department and the Bureau. All CR documents related to recoveries must be filed with the Office of the Comptroller.

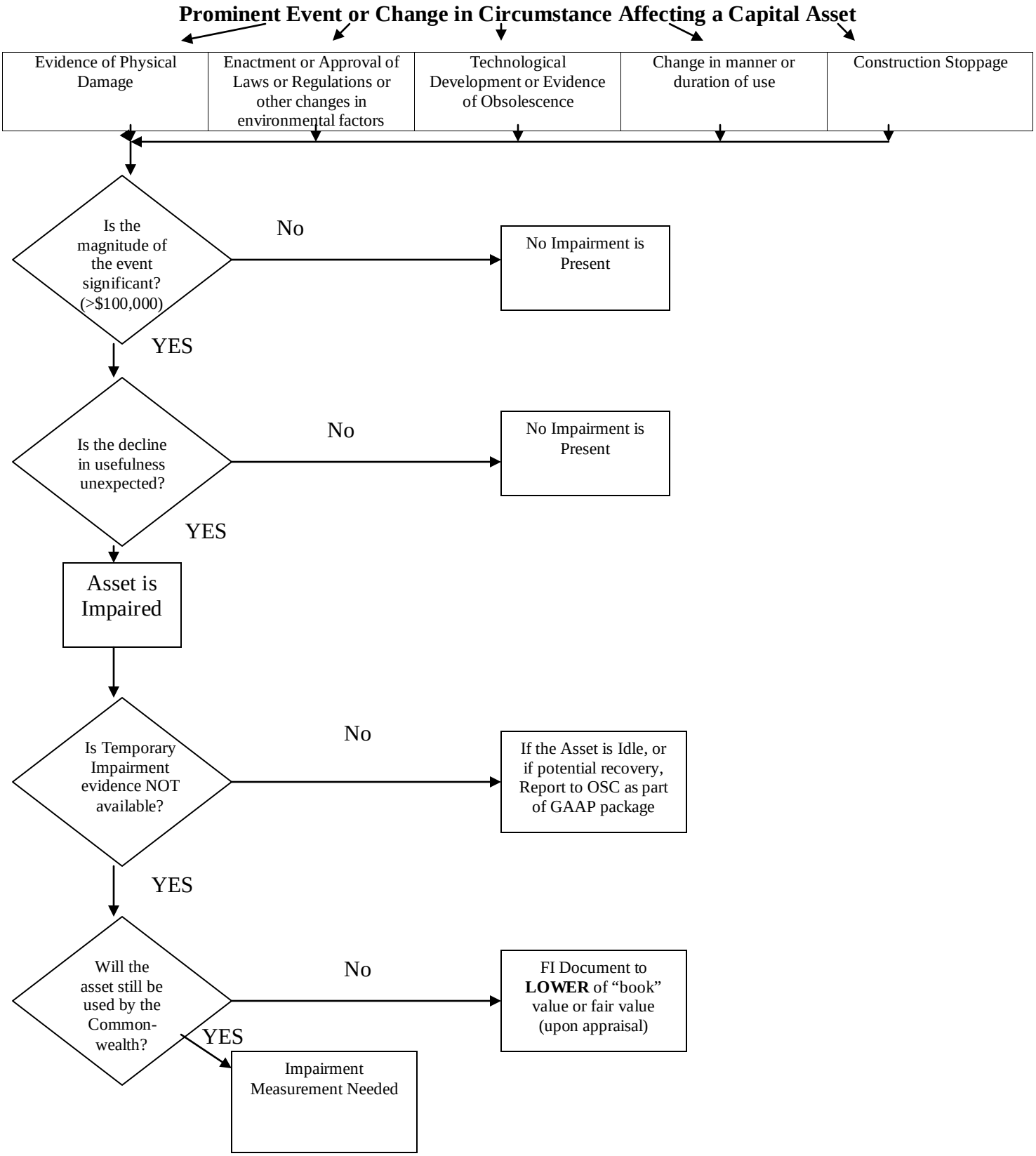
Information Sources

- Related Procedure
  - Increase or Decrease of a Fixed Asset (FI) document
  - Disposition of Fixed Asset Document (FD)
  - Cash receipt (CR) document
- Related Policies:
  - Fixed Assets - Accounting and Management Policy
  - Fixed Assets – Acquisition Policy
- Legal Authority:
  - M.G.L. c. 7A (Office of the Comptroller); M.G.L. c. 29 (State Finance Law);
  - Chapter 647 of the Acts of 1989
  - M.G.L. c.29, § 66 (State Finance Law Violations)
  - Government Accounting Standards Board Statement No. 42 (Accounting and Financial Reporting for Impairment of Capital Assets and Insurance Recoveries.)
- Attachments:
  - Quick Reference Decision Tree – Impairment Decision Process
  - Measurement of Asset Impairment for assets that will continue to be used by the Commonwealth
  - Selection of Methods of Measuring Impairment

Historical Changes:

- 3/10/05- Fixed Assets - Accounting and Management Policy released – The reporting section above will augment the existing reporting section.
- 2/9/06- Fixed Assets – New Policy contained herein on Impairment.
- **November 1, 2006** – Removed language referencing Knowledge Center and updated relevant links to Mass.gov/osc portal site.

ASSET IMPAIRMENT DECISION PROCESS



MEASUREMENT OF IMPAIRMENT

Indicator of Impairment	Measurement		
Physical Damage ***Example - fire***	Impairment = Cost to Restore	(Estimated Restore Cost / Estimated Replacement Cost) x Basis	Report Impairment Loss
Legal / Environmental Change - ***lawsuit*** **Tech Change –** ***obsolete software*** **Change in Use –** ***conversion of school to nursing home***	**Service Units Approach – what is the % of usefulness lost?**	Determine cost of remaining usefulness	Report Impairment Loss
Construction Stoppage	Lower of "Book Value" or Fair Value (per Appraisal)		Report Impairment Loss

SELECTION OF METHODS TO MEASURE IMPAIRMENT

Indicator of Impairment	Method Generally Used in Measurement
Evidence of physical damage	**If asset will continue to be used – what is the cost to restore? If no longer used – FI document to lower of "book value" or appraisal**
Enactment or approval of laws or regulations or other changes in environmental factors	**If asset will continue to be used – what % will continue to be used – adjust asset value to that percentage using an FI document. If no longer used – FI document to lower of "book value" or appraisal**
Technological Development or Obsolescence	**If asset will continue to be used – what % will continue to be used – adjust asset value to that percentage using an FI document. If no longer used – FI document to lower of "book value" or appraisal**
Change in Manner or Duration of Use	**If asset will continue to be used – what % will continue to be used – adjust asset value to that percentage using an FI document. If no longer used – FI document to lower of "book value" or appraisal**
Construction Stoppage	**Use FI document to lower of book value or appraisal.**