

UNIVERSITY OF CALIFORNIA

GASB STATEMENT NO. 42

**ACCOUNTING AND FINANCIAL REPORTING FOR IMPAIRMENT OF
CAPITAL ASSETS AND INSURANCE RECOVERIES—DRAFT**

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1. INTRODUCTION

GASB Statement No. 42 addresses the potential overstatement of an organization's capital assets. Capital assets are the most substantial component of the University's statement of net assets. Current GASB standards do not have a specific requirement to reduce the book value of capital assets should anything other than normal deterioration over the estimated useful life occur or should the capital asset become obsolete. The longer the life of a capital asset, the greater the possibility that unexpected events may affect the service utility of the capital asset and therefore the financial statements would be misstated for a number of years.

Under GASB Statement No. 42, the University is required to:

- Record an impairment loss in the statement of revenues, expenses and changes in net assets for a capital asset when its service utility has declined significantly and unexpectedly;
- Disclose capital assets that are idle;
- Record insurance recoveries associated with an impaired capital asset as an offset to the impairment loss; and
- Disclose the amount of insurance recoveries.

GASB Statement No. 42:

- Generally prescribes new reporting requirements, rather than amending previous guidance.
- Is effective for FY 2005-2006, although FY 2004-2005 will need to be restated for comparative purposes if impairment losses exist as of June 30, 2004. However, early implementation may be considered (see Section 3 for further discussion).
- Will be applied retroactively. The University will report the cumulative effect, if any, of applying the Statement as a restatement of beginning net assets in the restated year.
- Does not apply to the separately audited UCRS financial statements, including the UCRP, 403(b), 457(b) and PERS-VERIP plans since they have no capital assets. However, to the extent that these entities receive insurance recoveries those recoveries may need to be reported as a separate line item on the statement of changes in plan's fiduciary net assets, disclosed in the footnotes to the financial statements or both.
- Does not apply to the campus foundations since they have no capital assets (with certain limited exceptions). However, to the extent that these entities receive insurance recoveries, those recoveries may need to be reported as a separate line item on the statement of revenues, expenses and changes in net assets, disclosed in the footnotes to the financial statements or both.
- Applies to the separately audited Medical Center, UC Press and CEB financial statements.
- Does not apply to the separately audited Health and Welfare Plan financial statements since they have no capital assets or insurance recoveries.

This document is primarily prepared to outline the University's approach to the application of GASB Statement No. 42 to the University's financial statements.

GASB Statement No. 42 may be ordered from the GASB's website at www.gasb.org. There is no Implementation Guide from the GASB for this Statement.

2. BROAD OUTLINE OF GASB STATEMENT NO. 42

Asset Impairment

GASB Statement No. 42, paragraph 5 defines asset impairment as “a significant, unexpected decline in the service utility of a capital asset.” The events or changes in circumstances that lead to impairments are not considered to be normal and ordinary. That is, at the time the capital asset was acquired, the event or change in circumstance would not have been expected to occur during the useful life of the asset.

Each campus and medical center must undertake an evaluation each year that must include the following basic steps:

- Identify “potential” impairments (§7-10).
- Perform tests for impairment (§11).
- Measure the impairment (§12-16).
- Record and report the impairment loss (§17-18).
- Disclose the impairment loss (§17 and 20).

A detailed decision tree is provided in Exhibit 1, *Asset Impairment Decision Process*.

Insurance Recoveries

GASB Statement No. 42, paragraph 21 outlines the appropriate financial reporting treatment for insurance recoveries. Insurance recoveries should be recognized only when they are realized or realizable. In general, the steps to record insurance recoveries are as outlined below.

For insurance recoveries related to capital assets (§21):

- Record the impairment loss as an operating expense.
- Record the impairment loss net of recovery as an operating expense, when the loss and recovery occur in the same year. (In the highly unlikely event the loss and recovery qualify as either special or extraordinary, as defined, the loss and recovery would be recorded as part of Other Changes in Net Assets.)
- Record the recovery as nonoperating income, if the recovery occurs in a subsequent year.
- Record the recovery in the statement of cash flows as Proceeds from Insurance Recovery in the Capital and Related Financing Activities section (GASB Statement No. 9, §24d).
- Disclose the amount and classification of the insurance recovery.

The restoration or replacement of an impaired capital asset should be reported as a separate transaction from the impairment loss and associated insurance recovery.

A detailed decision tree is provided in Exhibit 2, *Insurance Recovery Decision Process for Insurance Recoveries Related to Impairment of Capital Assets*.

For insurance recoveries unrelated to capital assets, e.g., theft, embezzlement of cash or other monetary assets, etc. (§22) :

- Record the loss as a nonoperating loss.
- Record the loss as a nonoperating loss, net of recovery, when the loss and recovery occur in the same year.
- Record the recovery as nonoperating income, if the recovery occurs in a subsequent year.
- Record the recovery in the statement of cash flows as Other Receipts (Payments) in the Noncapital Financing Activities section (GASB Statement No. 9, §21c).
- Disclose the amount and classification of the insurance recovery.

A detailed decision tree is provided in Exhibit 3, *Insurance Recovery Decision Process for Insurance Recoveries Unrelated to Impairment of Capital Assets*.

3. POSSIBLE EARLY IMPLEMENTATION

The University will consider an early implementation of GASB Statement No. 42 in accordance with the following approach:

- The cumulative potential population of impaired capital assets, if any, will be identified by November 2004 (historical, through June 30, 2004, and June 30, 2004 through October 31, 2004). If there are any capital assets that require a loss to be recorded, early implementation likely will not be adopted.
- If the November 2004 review indicates there are no capital assets that require an impairment loss to be recorded, an updated review will be conducted through June 2005. If the June 2005 review indicates that a capital asset became impaired between November 2004 and June 2005, early implementation likely will not be adopted.
- If both the November 2004 and June 2005 reviews indicate there are no capital assets that require an impairment loss to be recorded, early implementation likely will be adopted in conjunction with the June 30, 2005 financial statements resulting in no change to net assets or restatement of prior-year results.

4. ASSET IMPAIRMENT

STEP 1: Identify “Potential” Impairments to Capital Assets (§7-10)

The first step in the process is to identify “potential” impairments to capital assets. Identifying “potential” impairments to capital assets may not necessarily lead to recording an impairment loss. Refer to Step 1 of Exhibit 1 for a detailed decision tree.

How is asset impairment defined?

As stated above, GASB Statement No. 42, paragraphs 5 and 6 define asset impairment as “a significant, unexpected decline in the service utility of a capital asset.”

- *Significant:* The events or changes in circumstances that lead to impairments are not considered to be normal and ordinary.
- *Unexpected:* At the time the capital asset was acquired, the event or change in circumstance would not have been expected to occur during the useful life of the asset.
- *Decline in service utility:* A reduction in the *usable* capacity that at acquisition was expected to be used to provide service, as distinguished from the level of utilization.
 - The *current usable capacity* of a capital asset less than its *original usable capacity* due to a) the normal wear and tear and expected decline in useful life is not considered to be an impairment, however b) impairing events or changes in circumstances that reduce usable capacity may indicate impairment.
 - Decreases in utilization and existence of, or increases in, surplus capacity that are not associated with a decline in *usable* capacity are generally not considered to be impairment.

How should the campus identify the population of “potential” impairments to capital assets?

It is important to highlight that the possible population of capital assets that have potential for meeting the definition of impairment are identified through significant events or changes in circumstances that may suggest that the service utility of a capital asset may have declined significantly and unexpectedly. The guidelines are:

- The events and circumstances are known by the University financial management and **are generally known** from discussions by the Regents, senior management, or the media. At a minimum, Regents’ Items pertaining to your campus during the year, particularly those that are considered by the Committee on Grounds and Buildings or Committee on Finance, should be reviewed and evaluated. Other sources of information that should be used to identify “potential” impairments to capital assets may include your campus’ press releases. Your review should include press releases or information considered at Regents’ meetings that are held after year end, but before the opinion date.

- The events and circumstances are prominent, conspicuous and, as expressed above, are not considered to be normal and ordinary. Any known event should be properly reported, regardless of the amount. In order to perform a review for potential unknown circumstances, they should be considered “significant.” Campus review efforts should focus on identifying events and circumstances that may lead to potential impairments that are in excess of \$5 million, unless materiality guidelines warrant a review at a lower threshold at a particular location.
- The events and circumstances denote the presence of “indicators of impairment.”

How should the campus treat impairments that become known during the ordinary course of business?

Absent such significant events and circumstances described above, University management is not required to perform additional procedures to identify potential impairments to capital assets. However, if during the normal course of recording transactions during the year there are “insignificant” events or circumstances that result from any of the indicators of impairment as outlined below, they should be recorded as outlined in this document. For example, if there is a fire in a laboratory that results in a write off of \$500,000 in book value of capital assets, it should be recorded as an Operating Impairment Loss as discussed below even though it did not result from the review as outlined above that we have defined as a significant event or circumstance.

GASB Statement No. 42, paragraph 34, excludes considerations of impairment that may be attributable to deferred maintenance or the condition of a capital asset.

What are the “indicators of impairment” and how are they defined?

The Statement outlines five common “indicators of impairment.” They are:

- Evidence of physical damage, such as for a building damaged by fire or flood, when the level of damage is such that restoration efforts are needed to restore service utility.
- Enactment or approval of laws or regulations or other changes in environmental factors, such as new earthquake standards that a facility does not meet, and cannot be modified to meet.
- Technological development or evidence of obsolescence, such as that related to a major piece of diagnostic or research equipment.
- A change in the manner or expected duration of use of a capital asset, such as closure of a building prior to the end of its useful life.
- Construction stoppage, such as stoppage of construction as a result of a lack of funding.

Is there a distinction between a permanent and temporary impairment?

In the absence of compelling facts, as discussed in paragraph 18 of GASB Statement No. 42, an impairment should be considered permanent. However, in certain cases, evidence may be available to demonstrate that the impairment will be temporary. If that is the case, the capital asset should not be written down.

Does a change in demand for the services of a capital asset always result in an impairment of a capital asset?

A change in the demand for the services of a capital asset is not, by itself, considered to be an indicator of an impairment of a capital asset and would not immediately result in a conclusion that the asset should be included in the population of capital assets that are tested for impairment. However, changes in demand for the services of a capital asset may be caused by one of the five indicators of impairment discussed above. In that case, the capital asset should be included in the population that is tested for impairment. An example is as follows:

- Decreased demand for the processing services of a mainframe computer because users have transitioned to PC and server-based systems should be considered a change in demand associated with an indicator of impairment, evidence of obsolescence, and the mainframe should be tested for impairment.
- On the other hand, if the decreased demand for the processing services of a mainframe computer was attributable to the conclusion of a special project requiring large amounts of processing time on the mainframe computer that runs other applications it should not be considered to be a change in demand associated with an indicator of impairment and a test of impairment is not required.

If the University has decided a capital asset should be sold, does that decision always result in an impairment of a capital asset?

A capital asset that the University has decided to sell, but is continuing to use as originally intended until the sale occurs, is not considered to exhibit a change in manner or expected duration of use. Therefore, it would not be included in the population of capital assets that may potentially be impaired. However, a capital asset that the University has decided to sell and is not continuing to use is considered to exhibit a change in manner or expected duration of use and should be included in the population of capital assets that may potentially be impaired.

Examples of impairment are provided in GASB Statement No. 42, paragraphs 34 through 47.

STEP 2: Perform Tests for Impairment of Capital Assets (¶11)

If the conclusion from Step 1 is that an indicator of impairment is present for certain capital assets, a potential impairment may exist and Step 2, a test for impairment, must be performed on the capital asset. Refer to Step 2 of Exhibit 1 for a detailed decision tree.

The test for impairment includes *two* factors. **Both** factors must be present in order to conclude that the capital asset is, in fact, impaired. The tests are:

- *The decline in service utility is unexpected.* The restoration cost or other impairment circumstance is not a part of the normal life cycle of the capital asset. Management is not expected to foresee with precision the useful life of a capital asset or the service utility throughout its useful life. However, there is a reasonable range of expectations about the service utility and useful life at the time of acquisition.

- *The magnitude of the decline in service utility is significant.* The expenses associated with continued operation and maintenance (including depreciation) or costs associated with restoration of the capital asset are significant in relationship to the current service utility. In cases where there is physical damage to a capital asset, the costs of restoration may be relatively easy to determine, at least within a range of estimates, and therefore the significance can be objectively assessed. In circumstances other than those involving physical damage, management's action to address the situation is an indication that the expenses are too high in relation to the benefit. If the Board has not addressed the matter, and management has not initiated any action, there may be a presumption, absent other facts, that the magnitude of the decline is not significant and this test would not be met.

If both factors are not present, there is no impairment loss to measure and record. However, GASB Statement No. 42, paragraph 19 indicates that does not mean that the estimate of the remaining useful life used in depreciation calculations should not be reevaluated and shortened, if necessary. Changes to estimated useful lives are accounted for on a prospective basis in future depreciation expense.

How should adjustments to useful lives be accomplished in the EFA or AST files?

If as a result of the impairment evaluation process, the campus Controller concludes that the remaining useful life is shorter than the remaining useful life in the system, the University's AST or EFA files and the depreciation system must include an adjustment so the remaining book value is extinguished over the remaining useful life. Currently, the system cannot accept these modifications. Systems specifications will need to be developed and modifications will need to be accomplished by February 2005.

STEP 3: Measure the Impairment of Capital Assets (¶12-16)

If the result from the tests in Step 2 is that both factors are present and there is a conclusion that there is an impairment of a capital asset, then Step 3 must be performed in order to measure the impairment. Refer to Step 3 of Exhibit 1 for a detailed decision tree.

The methods for measuring the impairment depend on whether the capital asset will continue to be used by the University, or not.

For impaired capital assets that will continue to be used by the University (¶12-15):

The portion of the historical cost that should be written off depends on the indicator of impairment associated with the capital asset and should be measured by the method described below that most appropriately reflects the decline in service utility of the capital asset. The circumstances under which each method can be used and a description of the methods for measuring impairment are as follows:

- *Method to be used to measure impaired capital assets attributable to the “evidence of physical damage” indicator (§13)*
 - *Restoration cost approach (§12a).* The amount of impairment (portion of the historical cost that should be written off) is derived from the estimated costs to restore the utility of the capital asset. Restoration cost is the amount necessary to return the capital asset to its original condition and does not include any amount attributable to improvements and additions. The estimated restoration cost can be translated into the amount of the historical cost to be written off using one of two approaches:
 - Restating (deflating) the estimated restoration cost using an appropriate cost index:

$$\frac{\text{Deflated restoration cost}}{\text{Historical cost}} \times \text{Carrying (book) value} = \text{Impairment loss}$$

Where:

$$\text{Deflated restoration cost} = \text{Current restoration cost} \times \frac{1}{(\text{Average inflation index since original acquisition})^n}$$

n = number of years since acquisition

- Or, applying a ratio of estimated restoration cost over estimated replacement cost to the net book value of the capital asset:

$$\frac{\text{Current restoration cost}}{\text{Current total replacement cost}} \times \text{Carrying (book) value} = \text{Impairment loss}$$

- *Methods to be used to measure impaired capital assets attributable to either the a) “enactment or approval of laws or regulations or other changes in environmental factors,” or b) “technological development or evidence of obsolescence” indicators (§14):*
 - *Service units approach (§12b).* The historical cost of the service utility of the capital asset that cannot be used is isolated. The amount of the impairment is determined by evaluating the service units throughout the life of the capital asset, before and after the impairment event.

$$\frac{\text{Carrying (book) value}}{\text{Original total service units}} \times \text{Service units reduced} = \text{Impairment loss}$$

- *Method to be used to measure impaired capital assets attributable to a “change in manner or duration of use” indicator (¶15):*
 - *Service units approach* described above, or
 - *Deflated depreciated replacement cost (¶12c)*. The historical cost of the service produced is replicated. A current cost for a capital asset to replace the current level of service is estimated. This estimated current cost is then depreciated to reflect the fact that the capital asset is not new, and then is deflated to convert it to historical costs dollars. The difference between this result and the historical cost in the financial system is the amount of the historical cost to be written off.

$$\text{Carrying (book) value} - (\text{Depreciated current replacement cost} \times \text{Deflation factor}) = \text{Impairment loss}$$

Where:

$$\text{Deflation factor} = \frac{\text{Original cost year index}}{\text{Current year index}}$$

For impaired capital assets that will no longer be used by the University, or construction stoppage (¶16):

Impaired capital assets that will no longer be used by the University, or capital assets impaired from construction stoppage, should be reported at the lower of carrying value or fair value. The historical cost should be written down to this level. Transaction codes will need to be designated to distinguish impairment write-offs from routine disposals. This will need to be similar to a partial disposal, but applied on a LIFO basis to the amounts capitalized for the most recent years. Systems specifications will need to be developed and modifications to the depreciation system will need to be accomplished by February 2005.

STEP 4: Record the Impairment Loss Attributable to Capital Assets (¶17-18)

If, as a result of working through Steps 1-3 above, the conclusion is that an impairment loss for a particular capital asset should be recorded, it must be reported in the University’s statement of revenues, expenditures and changes in net assets in one of three new categories: an operating impairment loss, a special impairment loss or an extraordinary impairment loss. Refer to Step 4 of Exhibit 1 for a detailed decision tree.

- *Operating impairment loss*. All impairment losses must be recorded as an operating impairment loss unless they specifically meet the definition of a special or extraordinary impairment loss. For example, a major renovation of a campus building where a portion of the existing structure has to be demolished, or a fire started in a laboratory that destroys a major portion of a building may be considered an operating impairment loss. Accounting codes for this type of loss are provided in Exhibit 4.

In the case of either a special or extraordinary impairment loss, the loss is classified within the Other Changes in Net Assets section of the University's statement of revenues, expenses and changes in net assets. The distinguishing features between an operating impairment loss and either a special or extraordinary impairment loss depend on whether the event or circumstance is either unusual, infrequent, or both. Generally, recording an impairment loss as special and/or extraordinary is difficult to justify.

Events or circumstances that are considered to be unusual in nature should possess a high degree of abnormality and be of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the University, taking into account the environment in which the University operates. Unusual in nature is not established by the fact that an event or transaction is beyond the control of management.

Events or circumstances that are considered to be infrequent in occurrence would not reasonably be expected to recur in the foreseeable future, taking into account the environment in which the University operates. Paragraphs 20-22 of APB 30 provide a more detailed definition of unusual in nature and infrequency in occurrence.

The distinguishing features between a special impairment loss and an extraordinary impairment loss depend on whether the event or circumstance is within the control of campus or University management.

- *Special impairment loss.* The special impairment loss category includes impairment losses that are associated with circumstances within the control of campus or University management and are either unusual in nature or infrequent in occurrence (GASB Statement No. 34, ¶56). Record the special impairment loss in transaction code 2582.
- *Extraordinary impairment loss.* The extraordinary impairment loss category includes losses that are not within the control of campus or University management and are both unusual in nature and infrequent in occurrence (GASB Statement No. 34, ¶55). Record the extraordinary impairment loss in transaction code 2583.

Recognizing that differences among the three categories may be subtle, UCOP–Financial Management can assist in researching the appropriate accounting codes to use in any given situation. In any event, if the loss is recorded as an operating loss, it must also be recorded by the function that used the capital asset. If the loss is recorded as a special or extraordinary loss, there is no need to identify the loss by function.

Impairment losses recognized in accordance with GASB Statement No. 42 should not be reversed in future years, even if the events or circumstances causing the impairment have changed (¶18).

Exhibit 5 provides a worksheet designed for use by campuses in order to document the ultimate financial reporting conclusion for capital assets that are identified as being potentially impaired.

What changes must be made to the AST or EFA files to accommodate an impairment loss?

UCOP–Financial Management is reviewing potential changes to the AST and/or EFA files to accommodate impairment losses. Campuses will be notified of necessary changes when UCOP's review is complete.

STEP 5: Disclose the Impairment Loss Attributable to Capital Assets (¶17 and 20)

For disclosure purposes, UCOP will need the information on impaired capital assets in order to disclose in the University's footnotes a general description of the asset impaired, the event or circumstance that caused the impairment, the amount of the impairment, and the account and function where the impairment loss was charged.

In addition, the carrying amounts of impaired capital assets that are idle at year-end must be disclosed, regardless of whether the impairment is considered permanent or temporary.

In order to accumulate the information described above, a closing step will be added to the University's fiscal closing schedule. Exhibit 6 provides a closing schedule worksheet designed to capture this information that will be needed to be prepared by campuses and submitted to UCOP.

5. INSURANCE RECOVERIES

Restoration or replacement of an impaired capital asset should be reported as a separate transaction from the impairment loss and associated insurance recovery.

Insurance recoveries should be recognized only when either realized or realizable. Clearly, if insurance proceeds have been received, the recovery must be recognized and recorded. In addition, if the insurance company has admitted or acknowledged coverage, an insurance **recovery** would be realizable and should be recorded. If the insurer has denied coverage, the insurance recovery generally is not recognizable.

Insurance Recoveries Related to the Impairment of Capital Assets (¶21)

Insurance recoveries are recorded and classified differently depending on whether the impairment loss and associated recovery occur in the same fiscal year.

- *Insurance recovery realized, or realizable, in the same fiscal year as the associated impairment loss.* The impairment loss should be reported net of the insurance recovery when the recovery and loss occur in the same fiscal year. Therefore, use the following account group codes depending on where the impairment loss was recorded:
 - *Insurance recovery associated with an operating impairment loss:* Record the realized or realizable insurance recovery in account group code 208440.
 - *Insurance recovery associated with a special impairment loss:* Record the realized or realizable insurance recovery in account group code 208434.
 - *Insurance recovery associated with a extraordinary impairment loss:* Record the realized or realizable insurance recovery in account group code 208436.
- *Insurance recovery realized, or realizable, in the subsequent fiscal year as the associated impairment loss.* If the insurance recovery is realized or realizable in a subsequent year from the associated loss, use the following account group codes depending on where the associated impairment loss was initially recorded:
 - *Insurance recovery associated initially with an operating impairment loss:* Record the realized or realizable insurance recovery in account group code 208431 that will be classified in the nonoperating section of the University's statement of revenues, expenses and changes in net assets.
 - *Insurance recovery associated initially with a special impairment loss:* Record the realized or realizable insurance recovery in account group code 208435 that will be classified in the Other Changes in Net Assets section of the University's statement of revenues, expenses and changes in net assets.
 - *Insurance recovery associated initially with an extraordinary impairment loss:* Record the realized or realizable insurance recovery in account group code 208437 that will be classified in the Other Changes in Net Assets section of the University's statement of revenues, expenses and changes in net assets.

Regardless of the timing of the insurance recovery, it will be classified as Proceeds from Insurance Recovery in the Capital and Related Financing Activities section of the statement of cash flows.

In certain instances, insurance reserves held at UCOP are transferred to a campus in advance of the receipt of an insurance recovery. In these cases, UCOP will transfer Unexpended Balances to campuses using transaction code 08XX. Campuses will respond to the transfer of reserve funds using transaction code 0814. UCOP will record the insurance recovery when realized or realizable.

Insurance Recoveries Unrelated to the Impairment of Capital Assets (¶22)

Losses that are unrelated to the impairment of capital assets will always be recorded as Other Nonoperating Expenses regardless of whether there is a recovery. Object code 7810 has been established to record losses unrelated to the impairment of capital assets.

Insurance recoveries unrelated to impairment of capital assets, such as for theft, embezzlement, lawsuit settlements, etc. are also recorded in different accounts depending on whether the loss and recovery occur in the same fiscal year. It is necessary to establish separate account group codes so that UCOP–Financial Management can track impairment losses separate from other types of losses.

- *Insurance recovery realized, or realizable, in the same fiscal year as the associated loss.* The loss should be reported net of the insurance recovery when the recovery and loss occur in the same fiscal year. Record the realized or realizable insurance recovery in object code 7820. This object code will be classified in the nonoperating section of the University’s statement of revenues, expenses and changes in net assets.
- *Insurance recovery realized, or realizable, in the subsequent fiscal year as the associated loss.* If the insurance recovery is realized or realizable in a subsequent year from the loss, record the realized or realizable insurance recovery in account group code 208432. This account group code will be classified in the nonoperating section of the University’s statement of revenues, expenses and changes in net assets.

Regardless of the timing of the insurance recovery, it will be classified as Other Receipts (Payments) in the Noncapital Financing Activities section of the statement of cash flows.

In certain instances, insurance reserves held at UCOP are transferred to a campus in advance of the receipt of an insurance recovery. In these cases, UCOP will transfer Unexpended Balances to campuses using transaction code 08XX. Campuses will respond to the transfer of reserve funds using transaction code 0814. UCOP will record the insurance recovery when realized or realizable.

Insurance Recoveries Disclosure (¶22)

For disclosure purposes, UCOP will need the information on insurance recoveries in order to disclose in the University’s footnotes a general description of the recovery, the event or circumstance that caused the recovery, the amount of the recovery, and the account and function where the recovery was recorded.

In order to accumulate the information described above, a closing step will be added to the University’s fiscal closing schedule. Exhibit 6 is a closing schedule worksheet that includes the information that will be needed to be prepared by campuses and sent to UCOP.

6. NEXT STEPS / REQUIRED ACTIONS

Responsibility (C, OP)	Required Completion Date	Action Item/Task
OP	2-Jul-04	Assign new accounting codes —Assign new accounting codes to record impairment losses and insurance recoveries (Exhibit 4).
OP	11-Aug-04	<p>Develop specifications to modify UCOP systems to accommodate approach related to accounting for the impairment of capital assets—</p> <ul style="list-style-type: none"> ▪ Develop specifications to modify the depreciation system to include adjustments so that the remaining book value for impaired assets is extinguished over the revised useful life. ▪ Develop specifications to modify the depreciation system to make appropriate reductions to assets related to partial disposals resulting from the impairment of capital assets. ▪ Develop specifications to modify AST file submissions.
OP	11-Aug-04	Add accounting codes to CFR driver tables —Add new impairment loss and insurance recovery accounting codes to CFR driver tables.
C	30-Nov-04	Establish new accounting codes in campus ledger —Establish new impairment loss and insurance recovery accounting codes in campus ledger.
C	30-Nov-04	Identify historical impairment losses —Perform asset impairment test to identify any potential capital asset impairments through June 30, 2004 and from July 1, 2004 through October 31, 2004. Discuss any potential impairment losses with UCOP–Financial Management.
OP	31-Jan-05	Develop footnote reports —Develop CFR footnote report to accumulate annual impairment and recovery information (see Exhibit 7).
OP	15-May-05	<p>Modify UCOP systems to accommodate the approach related to accounting for the impairment of capital assets—</p> <ul style="list-style-type: none"> ▪ Modify the depreciation system to include adjustments so that the remaining book value for impaired assets is extinguished over the revised useful life. ▪ Modify the depreciation system to make appropriate reductions to assets related to partial disposals resulting from the impairment of capital assets.
C	1-Jun-05	Identify historical impairment losses —Identify historical impairment losses between July 1, 2004 and June 30, 2005. Discuss any potential impairment losses with UCOP–Financial Management.

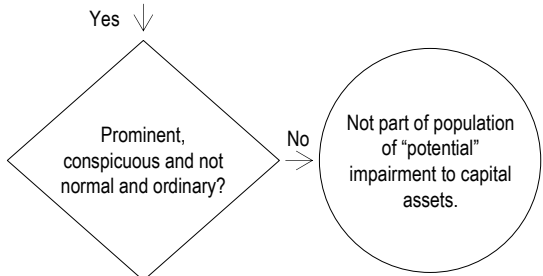
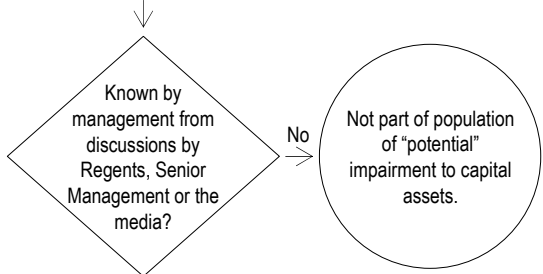
Responsibility (C, OP)	Required Completion Date	Action Item/Task
OP	30-Jun-05	Determine GASB Statement No. 42 implementation date —Based upon the results of the campus review of historical impairment losses through June 30, 2005, determine whether the University will implement GASB Statement 42 early, i.e., for the FY 2004-2005 fiscal year (assumes there are not cumulative impairment losses through June 30, 2005).
OP	31-Oct-05	Update AST and EFA reconciliation worksheets —Update AST and EFA reconciliation worksheets to accommodate an impairment loss, as necessary.
C	31-Dec-05	Record impairment losses and related insurance recoveries —Record capital asset impairment losses and related insurance recoveries. This includes historical impairment losses through June 30, 2005, as well as impairment losses that may have occurred from July 1, 2005 through December 31, 2005.
C	10-Feb-06	Modify AST file —Modify campus AST file in accordance with changes provided to campus from UCOP.
C	30-Jun-06	Identify potential asset impairments — Perform asset impairment test to identify any potential capital asset impairments from January 1, 2006 through June 30, 2006. Discuss any potential impairment losses with UCOP–Financial Management.
C	5-Aug-06	Record impairment losses and related insurance recoveries —Record capital asset impairment losses and related insurance recoveries in campus general ledger.

Exhibit 1— Asset Impairment Decision Process

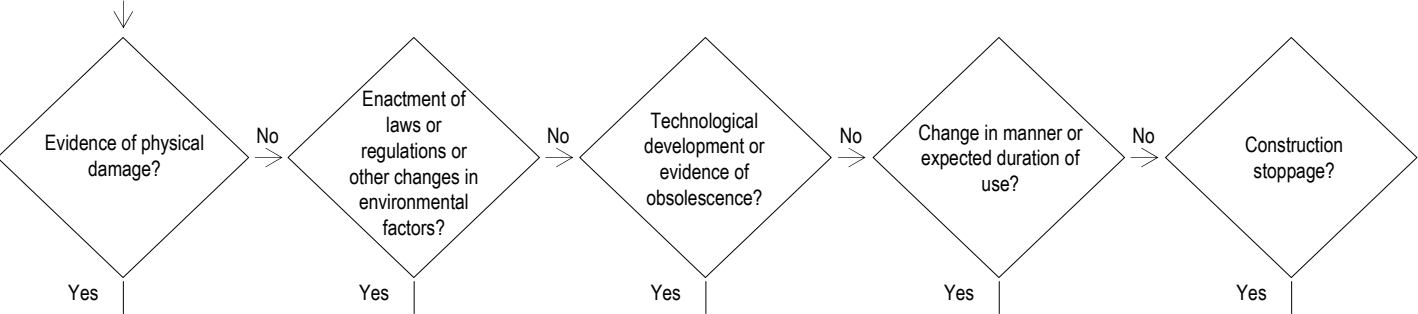
STEP 1: Identify “potential” impairments to capital assets.

Objective: Identify population of capital assets with a significant, unexpected decline in service utility.

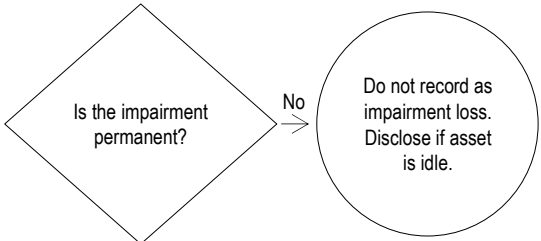
Evaluate events known during the routine course of business and significant events and circumstances over \$5 million.



Determine whether any ONE indicator of impairment is present.



Population of capital assets with “potential” impairment.



Proceed to Step 2: Perform tests for impairment of capital assets.

Not part of population of “potential” impairment to capital assets.

Exhibit 1— Asset Impairment Decision Process

STEP 2: Perform tests for impairment of capital assets.

Objective: Perform a test for impairment on each capital asset included in the final population of “potentially” impaired capital assets.

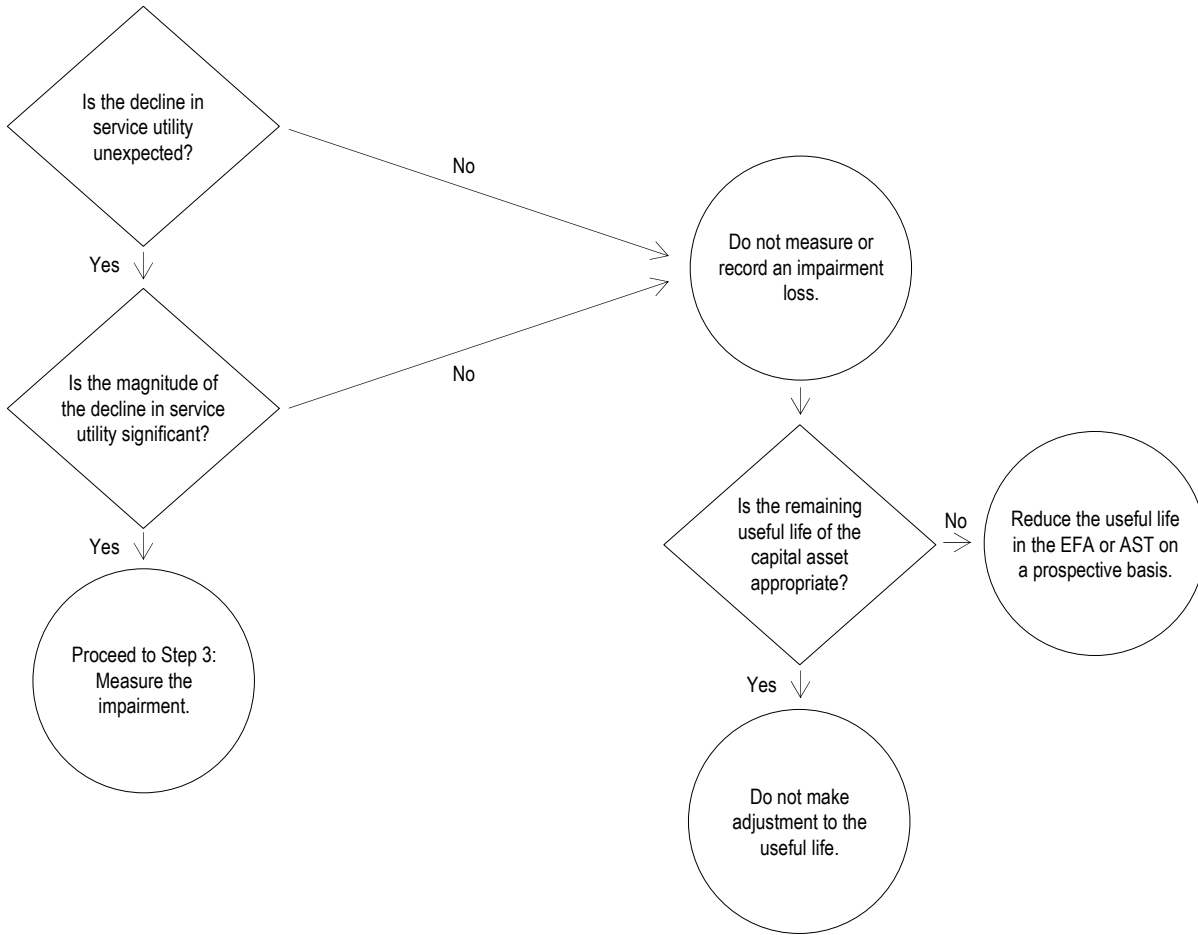


Exhibit 1— Asset Impairment Decision Process

STEP 3: Measure the impairment of capital assets.

Objective: Perform a test for impairment on each capital asset included in the final population of “potentially” impaired capital assets.

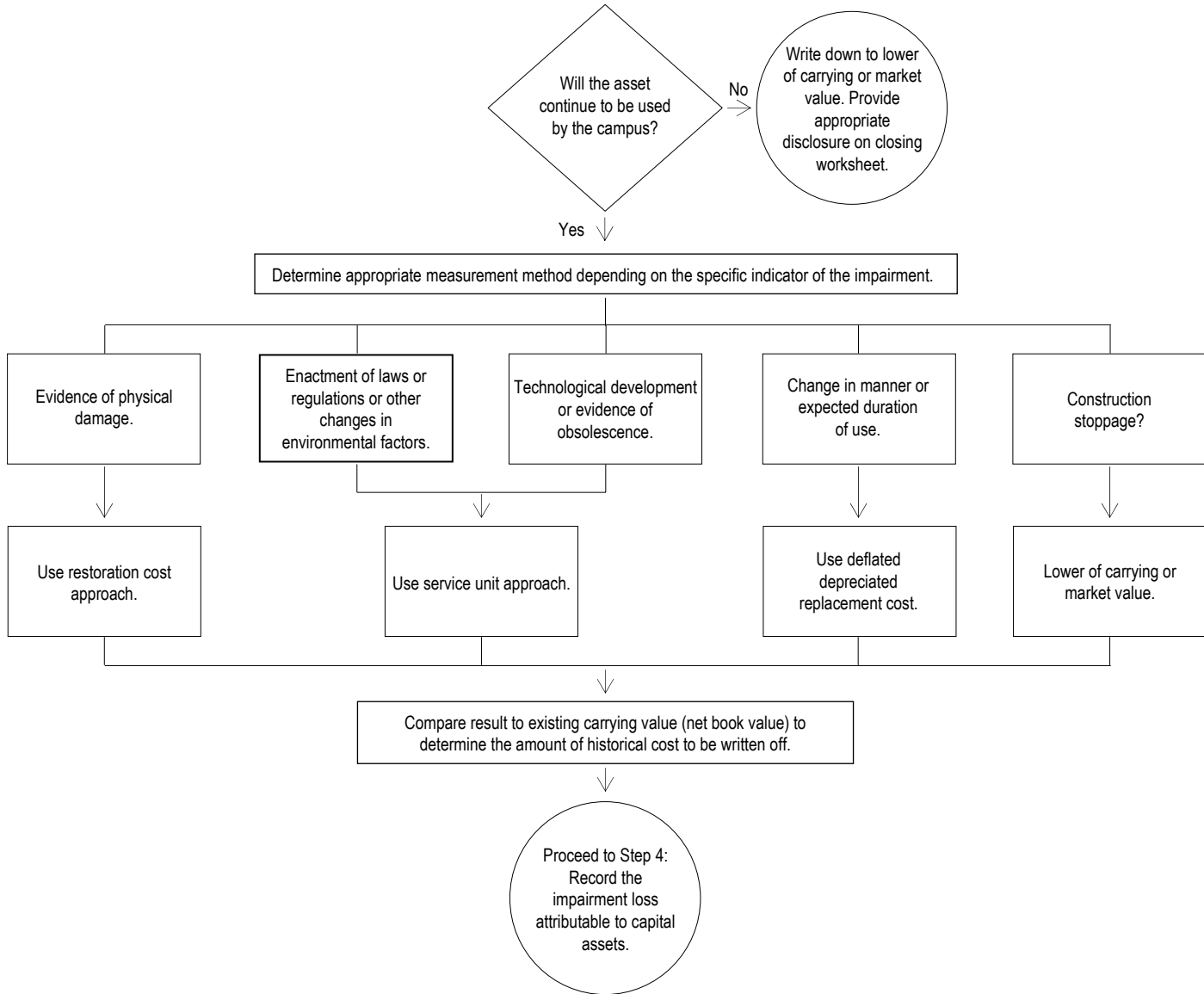


Exhibit 1— Asset Impairment Decision Process

STEP 4: Record the impairment loss attributable to capital assets.

Objective: Determine the appropriate account to record the impairment loss. Refer to accounting codes provided in Exhibit 4..

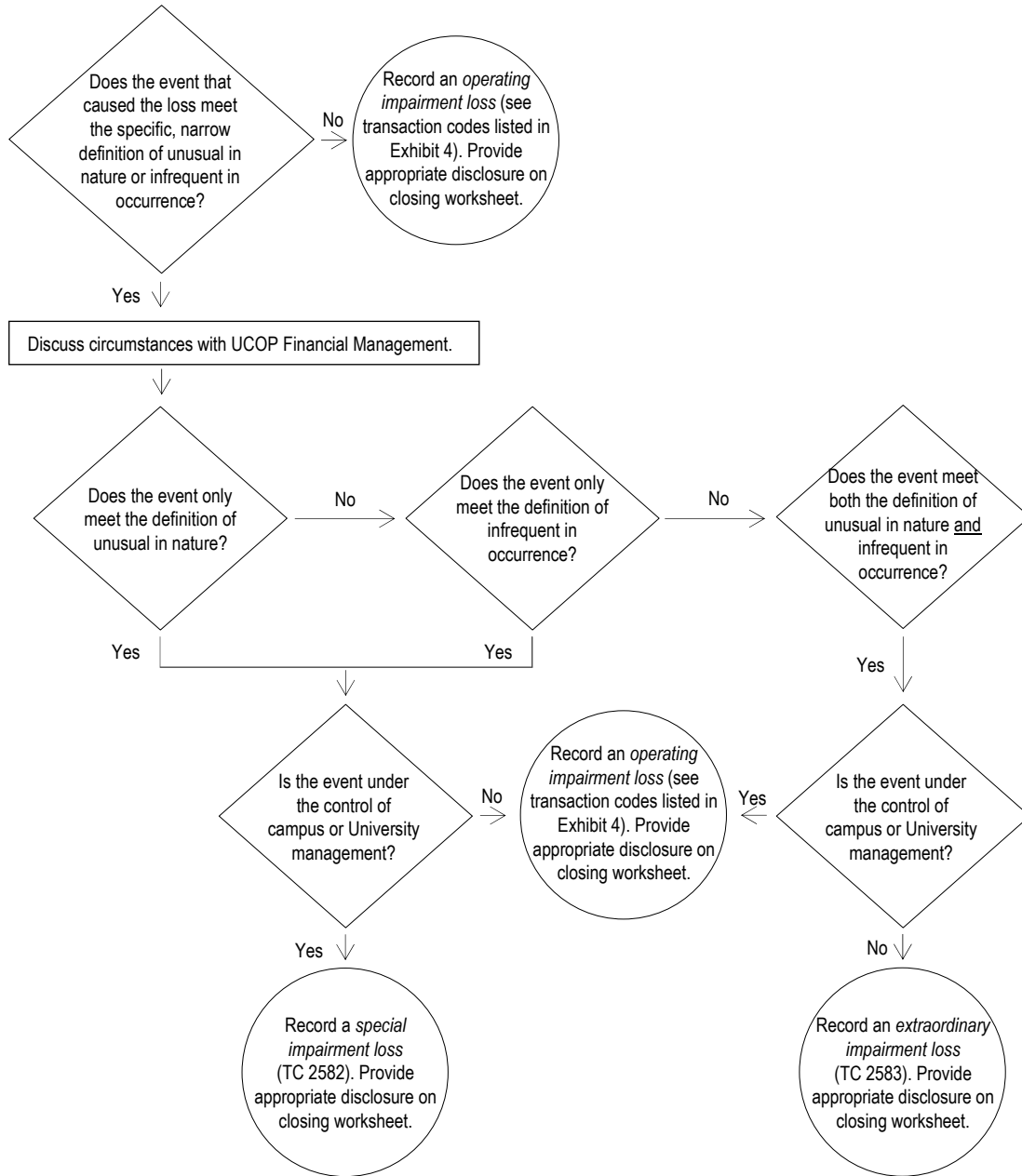


Exhibit 2— Insurance Recovery Decision Process for Insurance Recoveries Related to Impairment of Capital Assets

Objective: Determine the appropriate account to use to record an insurance recovery associated with impairment losses on capital assets.

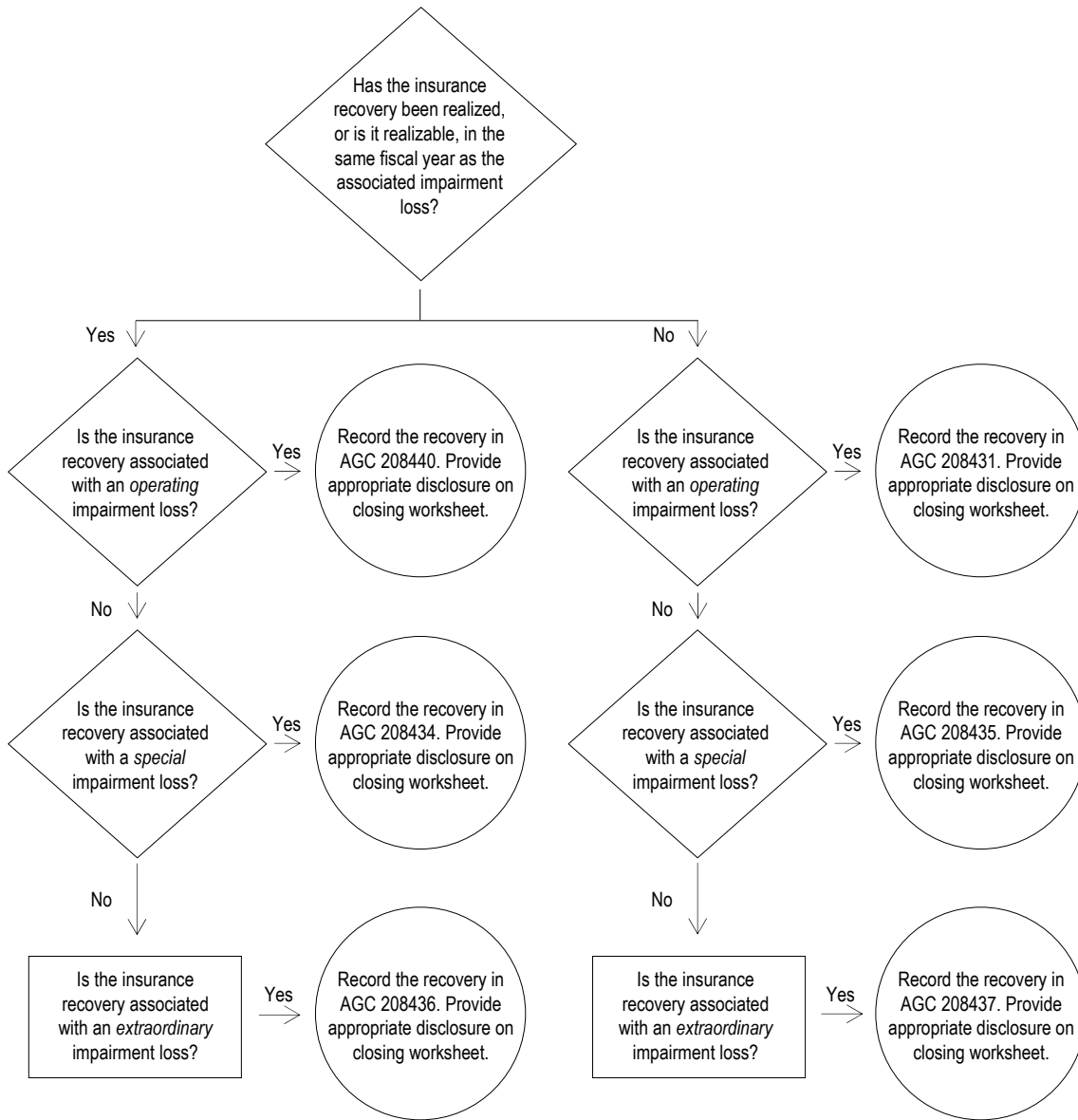


Exhibit 3— Insurance Recovery Decision Process for Insurance Recoveries Unrelated to Impairment of Capital Assets

Objective: Determine the appropriate account to use to record an insurance recovery unrelated to impairment losses on capital assets.

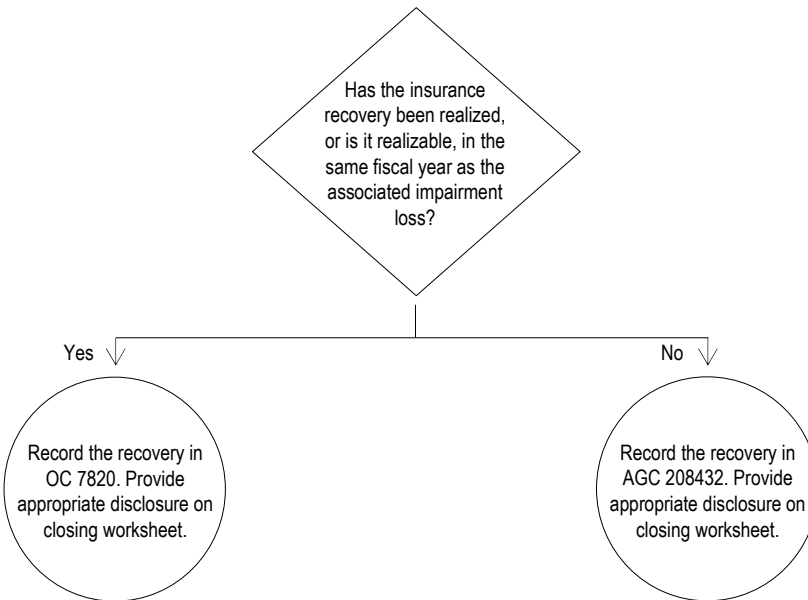


Exhibit 4—List of New Accounts and Account Roll Ups

Roll Up in *Other Operating Expenses*

Losses/recoveries, capital assets:	New
Operating impairment loss, capital assets	See list on following page
Insurance recoveries, current year capital assets	AGC 208440

Roll Up in *Other Nonoperating Income (Expenses)*

Losses/insurance recoveries, other than capital assets:	New
Other losses, other than capital assets	OC 7810
Insurance recoveries, current year other than capital assets	OC 7820
Insurance recoveries, prior-year losses:	New
Insurance recoveries, prior year capital asset loss	AGC 208431
Insurance recoveries, prior year other than capital assets	AGC 208432

New Line on Statement of Revenues, Expenses and Changes in Net Assets (below *Permanent Endowments*)

<i>Impairment losses and recoveries:</i>	New
Special impairment loss, net:	New
Special impairment loss	TC 2582
Special insurance recovery, current year losses	AGC 208434
Special insurance recovery, prior year losses	AGC 208435
Extraordinary impairment loss, net:	New
Extraordinary impairment loss	TC 2583
Extraordinary insurance recovery, current year losses	AGC 208436
Extraordinary insurance recovery, prior year losses	AGC 208437

Roll Up in *Other Receipts (Payments)*, Statement of Cash Flows, Cash Flows from Noncapital Financing Activities

Insurance recoveries, other than capital assets:	New
Insurance recoveries, current year other than capital assets	OC 7820
Insurance recoveries, prior year other than capital assets	AGC 208432

New Line in Statement of Cash Flows, Cash Flows from Capital and Related Financing Activities

<i>Proceeds from Insurance Recoveries</i>	New
Insurance recoveries, current year capital assets	AGC 208440
Insurance recoveries, prior year capital asset loss	AGC 208431
Special insurance recovery, current year losses	AGC 208434
Special insurance recovery, prior year losses	AGC 208435
Extraordinary insurance recovery, current year losses	AGC 208436
Extraordinary insurance recovery, prior year losses	AGC 208437

Transaction Codes: Operating impairment loss, capital assets

	Transaction Codes
Impairment of Cap. Assets-Orig Cost - Real Estate-Campus	TC2450
Impairment of Cap. Assets-Orig Cost - Real Estate-Med Ctr	TC2550
Impairment of Cap. Assets-Orig Cost - Bldg & Struct-Campus	TC2451
Impairment of Cap. Assets-Orig Cost - Bldg & Struct-Med Ctr	TC2551
Impairment of Cap. Assets-Orig Cost - Fixed Equip-Campus	TC2452
Impairment of Cap. Assets-Orig Cost - Fixed Equip-Med Ctr	TC2552
Impairment of Cap. Assets-Orig Cost - Gen Imprvmts-Campus	TC2453
Impairment of Cap. Assets-Orig Cost - Gen Imprvmts-Med Ctr	TC2553
Impairment of Cap. Assets-Orig Cost - Software > 10M-Campus	TC2454
Impairment of Cap. Assets-Orig Cost - Software > 10M-Med Ctr	TC2554
Impairment of Cap. Assets-Orig Cost - Software < 10M-Campus	TC2455
Impairment of Cap. Assets-Orig Cost - Software < 10M-Med Ctr	TC2555
Impairment of Cap. Assets-Orig Cost - Equipment-Campus	TC2456
Impairment of Cap. Assets-Orig Cost - Equipment-Med Ctr	TC2556
Impairment of Cap. Assets-Orig Cost - Intangible Assets-Campus	TC2457
Impairment of Cap. Assets-Orig Cost - Intangible Assets-Med Ctr	TC2557
Impairment of Cap. Assets-Orig Cost - Infrastructure Assets-Campus	TC2458
Impairment of Cap. Assets-Orig Cost - Infrastructure Assets-Med Ctr	TC2558
Impairment of Cap. Assets-Orig Cost - Spec. Collect.-Exc Lib-Campus	TC2459
Impairment of Cap. Assets-Orig Cost - Spec. Collect.-Exc Lib-Med Ctr	TC2559

Investment in Plant Transfer Codes

Operating Impairment Loss to Special or Extraordinary Impairment Loss	TC2581	(Cr)	} <i>Must net to zero</i>
Special Impairment Loss from Operating Impairment Loss	TC2582	(Dr)	
Extraordinary Impairment Loss from Operating Impairment Loss	TC2583	(Dr)	

For purposes of recording the reductions in capital assets due to impairments, all three categories of impairments will initially use the same transaction codes for Impairment of Capital Assets–Original Cost. There are separate transaction codes based on asset classification. The entry will be as follows:

Debit Investment in Plant, Impairment of Capital Assets–Original Cost
(Transaction codes 245X or 255X)

Credit Capital Asset

If it is determined that the impairment loss is special or extraordinary, a fund balance transfer in Investment in Plant will be recorded. The entry will be as follows:

Debit Investment in Plant, Special Impairment Loss
(Transaction code 2582)

Credit Investment in Plant, Operating Impairment Loss
(Transaction code 2581)

OR

Debit Investment in Plant, Extraordinary Impairment Loss
(Transaction code 2583)

Credit Investment in Plant, Operating Impairment Loss
(Transaction code 2581)

Exhibit 5—Impairment Loss Summary Worksheet: Capital Assets

1. Description of potentially impaired capital asset.

Provide description here.

2. Information Source (select one):

Regents Item _____

Campus Management _____

News Report _____

Other _____

3. Per University Records:

Original Cost _____ \$
(by year of acquisition, plus subsequent additions and modifications)

Accumulated Depreciation _____ \$

Net Book Value _____ \$

Remaining Useful Life (years) _____

4. What is the indicator of the impairment? Select one.

Evidence of physical damage _____

Enactment or approval of laws or regulations or other changes in environmental factors _____

Technological development or evidence of obsolescence _____

Change in manner or expected duration of use _____

Construction stoppage _____

5. Is the impairment permanent?

Yes _____

No _____

6. What is the estimate of the impairment? _____

(Restoration cost, service unit cost, deflated depreciated replacement cost, lower of carrying value or fair value.)

7. Does the potential impairment exhibit BOTH of the following characteristics? (Y/N) _____

- A decline in service utility that is unexpected and not part of the normal life cycle.
- The magnitude of the decline in service utility is significant.

8. Is the campus required to re-evaluate the remaining useful life? (Y/N) _____

If yes, what is the revised estimate of the remaining useful life? _____

9. By which method is the impairment loss measured? Select one.

Restoration Cost Approach _____

Service Units Approach _____

Deflated Depreciated Replacement Cost Approach _____

10. Is the impairment loss recorded?

Yes _____

No _____

11. If yes, how much was the recorded loss? \$ _____

Recorded as one of the following:

▪ Operating Impairment Loss _____

▪ Special Impairment Loss (TC 2582)¹ _____

▪ Extraordinary Impairment Loss(TC 2583)¹ _____

12. Is the capital asset idle at year-end?

Yes _____

No _____

13. Is there a related insurance recovery recorded in the same fiscal year as the impairment loss? (Y/N) _____

Amount recorded: \$ _____

Recorded as one of the following:

▪ Operating Impairment Loss (AGC 208440) _____

▪ Special Impairment Loss (AGC 208434)¹ _____

▪ Extraordinary Impairment Loss (AGC 208436)¹ _____

¹ Contact UCOP–Financial Management if your evaluation seems to lead toward recording either a special or extraordinary loss or recovery since these would not be classified for financial statement purposes in operating results.

Exhibit 6—Closing Schedule Worksheet

Summary of Impairment Losses and Insurance Recoveries (GASB 42)
 As of June 30, 20XX
 (dollars in thousands)

Campus: _____
 Prepared by: _____
 Telephone No.: _____

Impairment Loss								Related Insurance Recovery		Recovery related to a loss incurred in:
Description of Asset Impaired	Event or Circumstance Causing Impairment Loss <i>(select from A-E, listed below)</i>	Amount of Impairment Loss Recorded	List Account Codes Where Recorded	Function(s)	Ordinary, Special or Extraordinary Loss?	Remaining Net Book Value After Impairment Loss	Is Asset Idle? Y / N	Recovery Amount Recorded	List AGC in CFR Where Recorded	Same Fiscal Year
(1)										
(2)										
(3)										
(4)										
(5)										

Insurance Recoveries—Capital Assets					Recovery related to a loss incurred in:
Description of Insurance Recovery	Event or Circumstance Causing Impairment Loss <i>(select from A-E, listed below)</i>	Recovery Amount Recorded	List AGC Where Recorded	Same Fiscal Year	<u>OR</u> Previous Fiscal Year
(1)					
(2)					
(3)					
(4)					
(5)					

Insurance Recoveries—Non-Capital Assets					Recovery related to a loss incurred in:
Description of Insurance Recovery	Event or Circumstance Causing Impairment Loss	Recovery Amount Recorded	List AGC Where Recorded	Same Fiscal Year	<u>OR</u> Previous Fiscal Year
(1)					
(2)					
(3)					
(4)					
(5)					

- Event or circumstance:**
- A Evidence of physical damage.
 - B Enactment or approval of laws or regulations or other changes in environmental factors.
 - C Technological development or evidence of obsolescence.
 - D Change in manner or expected duration of use.
 - E Construction stoppage.

**Exhibit 7—CFR Footnote Disclosure Report: Impairment Losses and Insurance Recoveries
DR/(CR)**

<u>OPERATING IMPAIRMENT LOSSES / RECOVERIES - CAPITAL ASSETS</u>	<u>Current Year</u>	<u>Prior Year</u>
Impairment Losses - Capital Assets	(1)	(1)
Insurance Recovery - Current Year	AGC 208440	AGC 208440
Net Losses - Capital Assets	SUM	SUM

OTHER NON-OPERATING (REVENUE) EXPENSE

Losses Other Than Capital Assets	OC 7810	OC 7810
Insurance Recoveries for other than Capital Assets - Current Year Losses	OC 7820	OC 7820
Net Losses - Other than Capital Assets	SUM	SUM

Other Insurance Recoveries - Capital Assets-Prior Year Losses	AGC 208431	AGC 208431
Other Insurance Recoveries - Other than Capital Assets-Prior Year Losses	AGC 208432	AGC 208432

OTHER CHANGES IN NET ASSETS

Special Impairment Losses

Special Impairment Losses	TC 2582	TC 2582
Special Insurance Recovery - Current Year Losses	AGC 208434	AGC 208434
Net Losses	SUM	SUM

Special Insurance Recovery - Prior Year Losses	AGC 208435	AGC 208435
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Extraordinary Impairment Losses

Extraordinary Impairment Losses	TC 2583	TC 2583
Extraordinary Insurance Recovery - Current Year Losses	AGC 208436	AGC 208436
Net Losses	SUM	SUM

Extraordinary Insurance Recovery - Prior year Losses	AGC 208437	AGC 208437
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(1) TC 2450 through 2459 + TC 2550 through 2559 + TC 2581