



State of North Carolina Office of the State Controller

Michael F. Easley, Governor

Robert L. Powell, State Controller

March 10, 2006

MEMORANDUM NO. SAD 06-25

TO: Chief Fiscal Officers of State Agencies and
Component Units

FROM: Robert L. Powell, State Controller

SUBJECT: GASB Statement No. 42 Implementation Issues

In November 2003, the Governmental Accounting Standards Board (GASB) issued GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries* (GASB 42). This Statement establishes accounting and financial reporting standards for impairment of capital assets. A capital asset is considered impaired when its service utility has declined significantly and unexpectedly. Before the issuance of this Statement, there was no specific requirement to reduce the carrying value of a capital asset other than through the application of depreciation. This Statement also clarifies and establishes accounting requirements for insurance recoveries, including those not associated with asset impairments.

The requirements of GASB 42 are effective for the State fiscal year ending June 30, 2006. Therefore, state agencies and component units of the State of North Carolina should begin planning for the implementation of this new Statement.

As an initial step, state agencies should determine if they have any impaired capital assets **with material carrying values** that existed as of July 1, 2005 (*Note: the checklist in Appendix A of the attached summary should assist with this determination*). For state agencies, OSC will calculate the related impairment loss and will make entries in NCAS (or provide entries to state agencies) to report any such losses as prior period adjustments. However, before calculating any impairment losses, OSC will request additional information from state agencies related to their impaired capital assets. In addition, OSC will notify state agencies of the adjustment amount that should be recorded in the fixed asset system to reduce the carrying value of impaired capital assets. State agencies should post any adjustments to fixed assets by June 30. We will send a follow-up survey this month to obtain information about impaired capital assets of selected state agencies. Our office will also request information relating to capital asset impairments in the year-end CAFR package for the fiscal year ending June 30, 2006.

Likewise, component units should identify any impaired capital assets that existed as of July 1, 2005 and calculate the related impairment loss, **if the asset's carrying value is material**. For these assets, the impairment loss will need to be reported as a prior period adjustment and beginning net assets will need to be restated. Component units should establish a new account to report any impairment losses recognized during the 2005-06 fiscal year. Impairment losses should be recognized in the statement of revenues, expenses, and changes in net assets as an operating expense, special item, or extraordinary item.

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To assist with your implementation, we have attached a comprehensive summary of GASB 42. The attached summary also includes a *Checklist for Assessing Capital Asset Impairments* (see Appendix A), an illustrative example for a building with physical damage (see Appendix B), and an illustrative example on the retroactive application of GASB 42 (see Appendix C). The checklist in Appendix A will assist state agencies and component units in determining if they have any impaired capital assets and will also provide documentation for their auditors.

Please refer to the following for additional information on GASB 42:

- Copies of GASB 42 can be obtained by calling the GASB at (800) 748-0659 or by placing an order online at www.gasb.org (click "Publications" link).
- Appendix C of GASB 42 presents illustrative examples of asset impairments and the various methods used to calculate the amount of the impairment.
- The *GASB's Comprehensive Implementation Guide - 2005* includes questions on asset impairment (see questions 7.466 through 7.475).
- The November 2003 issue of the *GAAFR Review* examines in detail the new guidance offered in GASB 42. [Note: The *GAAFR Review* is the Government Finance Officers Association's (GFOA) monthly newsletter on government accounting, auditing, and financial reporting. To subscribe to the *GAAFR Review*, call the GFOA at (312) 977-9700 or email them at GAAFRReview@gfoa.org.]

If you have any questions about the statewide implementation of GASB 42, please contact Clayton Murphy at (919) 981-5474 or cmurphy@ncosc.net.

Attachment