

# Alert

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## Long Live the Asset! SFAS 144 Impairment Testing

The recent economic turmoil has forced many companies to deal with asset impairment issues. SFAS 142 (goodwill and other indefinite-lived intangibles) and SFAS 144 (the impairment or disposal of long-lived assets) provide guidance for the recognition and measurement of asset impairment. This issue of the *Valuation Researcher Alert* focuses on the impairment of long-lived assets.

Under SFAS 144, "impairment is the condition that exists when the carrying amount of a long-lived asset (asset group) exceeds its fair value. An impairment loss shall be recognized only if the carrying amount of a long-lived asset (asset group) is not recoverable and exceeds its fair value."

### VRC NEWS

VRC will be holding a webcast, *Long Live the Asset! Impairment Testing in the Current Environment*, on Feb. 24.

To register go to [www.valuationresearch.com](http://www.valuationresearch.com).

### WHEN TO TEST FOR RECOVERABILITY

A long-lived asset (or, more often, an asset group) shall be tested for impairment whenever events indicate that its carrying amount may not be recoverable. The following are examples of such events:

- a) A significant decrease in the market price of a long-lived asset
- b) A significant adverse change in the extent or manner in which a long-lived asset is being used or in its physical condition
- c) A significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset including an adverse action or assessment by a regulator
- d) An accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of a long-lived asset
- e) A current-period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset
- f) A current expectation that, more likely than not, a long-lived asset will be sold or otherwise disposed of significantly before the end of its previously estimated useful life

### ASSET-TESTING ORDER

If goodwill and long-lived assets of a reporting unit are tested for impairment concurrently, the impairment testing is performed in the following order:

1. Assets and liabilities not covered by SFAS 144 (including indefinite-lived intangible assets, such as trademarks, tested under SFAS 142; other non-goodwill, non-long-lived assets such as working capital)
2. Long-lived assets covered by SFAS 144 (primarily PP&E and finite-lived intangibles)
3. Goodwill

### ASSET GROUPS

Assets are grouped at the lowest level for which there are identifiable cash flows which are independent of other assets and liabilities. For many businesses, a typical asset group is a collection of:

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*“VRC regularly assists clients with SFAS 144 by valuing asset groups and their underlying tangible and intangible assets.”*

## Long Live the Asset! SFAS 144 Impairment Testing

1. Working capital,
2. PP&E, and
3. Intangible assets that operate as a group.

Goodwill is included in the carrying value if the asset group is also defined as a reporting unit. If a reporting unit is comprised of multiple asset groups, the goodwill is not allocated to the underlying asset groups.

### RECOVERABILITY

The first step is a test of the asset group's recoverability. The recoverability test compares the carrying value of the asset group to the undiscounted cash flows directly attributable to the asset group over the life of the primary asset. Cash flows are inflows less outflows, including any inflows or outflows which occur at the end of the primary asset's life (most commonly working capital and fixed assets, but may also include intangible assets). The primary asset is the principle long-lived tangible or intangible asset being depreciated or amortized. It is generally the asset group's most important asset.

### IMPAIRMENT

If the asset group is determined not to be recoverable by the undiscounted cash flows, the next step is to measure its fair value. If the fair value conclusion is less than the carrying value, the asset group is impaired. If impaired, the carrying values of the individual assets of the asset group are adjusted by allocating the impairment amount to the long-lived intangibles based on their relative carrying values, e.g. if long-lived asset A contributes 40% of the total carrying value of the long-lived assets, it is allocated 40% of the impairment. The carrying values of the long-lived assets are not impaired below their respective fair values. However, assets may be impaired by more than their pro-rata amounts if unallocated impairment amounts remain as a result of the fair value setting a floor on the adjusted carrying value of another asset.

Testing and impairment of assets under SFAS 144 may also be a triggering event for interim goodwill impairment testing under SFAS 142.

### RELY ON OUR EXPERIENCE

VRC regularly assists clients with SFAS 144 by valuing asset groups and their underlying tangible and intangible assets. For more information contact your Valuation Research representative or PJ Patel at 609-243-7030. **VR**



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