

Introduction

This document clarifies financial accounting and reporting requirements for disposed assets and obligations associated with the retirement and disposal of the asset.

This document contains two sections. The first section will assist the agencies to determine when assets should be removed from the GPP&E account. The second section offers implementation guidance for asbestos related clean-up costs. The purpose of this section is to further clarify technical bulletin (TB) 2006-1, Recognition and Measurement of Asbestos-Related Cleanup Costs. This bulletin was released in September 2006 to address issues that arose as a result of the Financial Accounting Standards Board's (FASB) issuance of FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations (FIN 47) in March 2005.

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Scope

1. GPP&E Removed From Service

Section I of this document offers additional guidance based on SFFAS – 6 to identify standard trigger events used to deactivate an item's financial and accounting requirements when such items are no longer required, i.e., are identified for disposal, retirement or removal from service. The identification of a standard data element and definition to highlight the financial implications of a disposal action is a critical factor to the process of removing the assets' book value from the financial records and accurately representing the entity's operating position.

2. Recognition and Measurement of Asbestos Related Cleanup Costs

Section II of this document offers additional guidance based on SFFAS and clarification to the federal financial accounting and auditing technical release 2 and technical bulletin 2006-1. This document uses applicable SFFAS and SFAS requirements for recognition and measurement of asbestos related cleanup costs.

The applicable standards and guidance utilized are:

- SFFAS 6, Accounting for Property, Plant, and Equipment
- SFFAS 5, Accounting for Liabilities of the Federal Government

- Federal Financial Accounting and Auditing Technical Release (TR) Number 2, Determining Probable and Reasonably Estimated for Environmental Liabilities in the Federal Government
- FASAB Technical Bulletin 2006-1, Recognition and Measurement of Asbestos-Related Cleanup Costs
- SFAS 143, Accounting for Asset Retirement Obligations
- FASB Interpretation 47, Accounting for Conditional Asset Retirement Obligations

Section I – GPP&E Removed From Service

Background

This section offers federal financial requirements addressing the financial transactions of the assets identified for disposal.

1. Description of Federal Financial Requirements

An agency is required to remove the general PP&E book value from the asset account in the period of disposal, retirement, or removal from service. Any difference between the book value of the PP&E and amounts realized shall be recognized as a gain or a loss in the period that the general PP&E is disposed of, retired, or removed from service.

General PP&E shall be removed from general PP&E accounts along with associated accumulated depreciation/amortization, if prior to disposal, retirement or removal from service, it no longer provides service in the operations of the entity. This could be either because it suffered damage, became obsolete in advance of expectations, or was identified as excess. It shall be recorded in an appropriate asset account at its expected net realizable value. Any difference in the book value of the PP&E and its expected net realizable value shall be recognized as a gain or a loss in the period of adjustment. The expected net realizable value shall be adjusted at the end of each accounting period and any further adjustments in value recognized as a gain or a loss. However, no additional depreciation/amortization shall be taken once such assets are removed from general PP&E in anticipation of disposal, retirement, or removal from service.

2. Description of Issue

The guiding principles do not recognize that removal from the service may be temporary and not permanent. This has resulted in implementation & interpretation inconsistencies in applying the SFFAS-6 mandates. Specifically, clarity and standardization are needed to determine when in the disposal business process lifecycle the book value of the asset should be removed from the general PP&E asset account.

3. Recommendation

Agencies are required to remove the general PP&E book value from the asset account in the period of disposal, retirement, or removal from service. The underlying assumption is that the removal is permanent. However, at times agencies remove assets from service with the intention of returning them to service in the future. In this situation, the assets shall continue to be depreciated during periods of non-use since they would be deemed to continue to provide service to the operations of the entity.

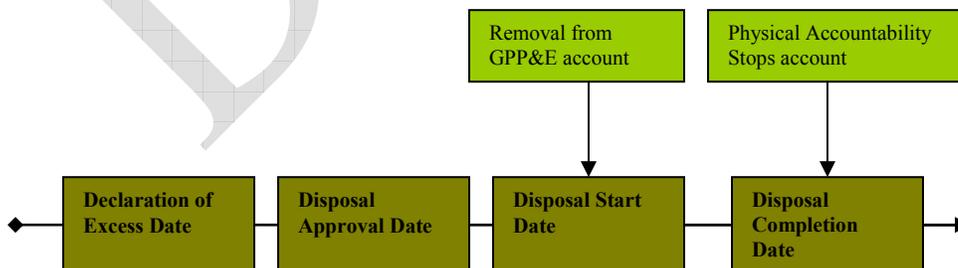
For purposes of determining the accounting treatment to apply, removal from service shall be presumed permanent unless there is **persuasive evidence** that the intent of the agency is to return the asset to service. The evidence should demonstrate that the return is more likely than not.

Similarly, agencies are required to remove the general PP&E book value if prior to disposal, retirement or removal from service, assets no longer provide service in the operations of the entity. This loss of utility may result from damage, obsolescence or excess capacity.

Implementation of this provision requires two separate assessments. The first is whether the assets continue to provide service to the operations of the entity. The second is whether the asset may be returned to service in the future.

For real property the determination as to whether an asset continues to provide service is based on the finalization of a legally enforceable and recognizable obligation to complete the disposal. Prior to that point there is no commitment to disposal.

For example, in the case of a real property asset that is declared as excess, there is no obligation to dispose of the asset at this point in time and the asset's status may be reversed due to an unexpected mission change. To further clarify the guidance, the timeline illustrated below is the chronological representation of the major milestones within the real property disposal process and the relevant financial and physical accountability events. The definitions for each of the major milestones are outlined below.



Declaration of Excess Date - Date the declaration of excess is signed. When a real property asset is declared as excess, the Component initiates disposal screening procedures, which includes soliciting proposals for the use of the excess space. At this point in time, the disposal is not definitive and if the mission changes, there is no

commitment to the disposal act. The occupancy and operation of the real property asset may continue during this time.

Disposal Approval Date - Date the asset is approved for disposal and the excess screening procedures are completed. This might include identifying or approving the specific method of disposal and the possible recipient. If the mission changes, there is no commitment to the disposal act. The occupancy and operation of the real property asset may continue during this time

Disposal Start Date - This represents the date of a legally enforceable and recognizable obligation to complete the disposal action or the date the operation has ceased, whichever comes later. On this date, the asset is no longer depreciated and the book value of the asset is removed from the financial records and the corresponding gain/loss is recorded. For assets that are part of a BRAC, this date represents the operation closure date that is established by BRAC law. For demolitions, this represents the demolition contract's start date. For transfers and sales, this represents the date the instrument is endorsed or operation is ceased, whichever comes later. For natural disasters, this represents the actual date of the incident.

Disposal Completion Date - The actual date the disposal of the asset is completed and there is no additional administrative accountability. This is determined by the effective date of the instrument for the actual method of disposal. The disposal methods consist of transfer, sale, natural disaster and demolition. For demolitions, this date represents the demolition contract's completion date. For transfers and sales, this may equal the real property asset disposal start date. For natural disasters, this equals the asset disposal start date.

For personal property assets that are in use are presumed to be providing service. However, there may be situations where assets that have not yet entered the disposal/retirement/removal process are no longer providing service. For example, the development of "stealth" technology could negate the effectiveness of a radar system. In this situation the radar would be recorded in an appropriate asset account at its expected net realizable value. A formal threat assessment could be used to document this determination.

As with disposed/retired assets, the presumption is that the change in status is permanent unless there is **persuasive evidence** that the intent of the agency is to return the asset to service. The evidence should demonstrate that the return to service is more likely than not. In the radar example, the pervasive evidence might be documentation of a research project designed to enhance the capability of the radar and thereby overcome the impairment.

Section II - Recognition and Measurement of Asbestos Related Cleanup Costs

Background

This section offers background information related to governing standards and issues related to the implementation of these standards:

4. Description of Federal Financial Requirements

An agency is required to recognize a liability for environmental cleanup costs as a result of past transactions or events when a future outflow or other sacrifice of resources is probable and reasonably estimable. Specifically, the federal entities should recognize a liability and related expense for the removal of asbestos for both friable and non-friable asbestos-related cleanup costs that are probable and reasonably estimable. The asbestos-related cleanup costs shall be estimated when the associated property, plant & equipment (PP&E) is placed in service.

TB 2006-1 states it is possible for certain types of nonfriable asbestos-containing material to remain nonfriable forever; therefore the estimate does not need to include nonfriable asbestos-containing roofing, flooring, siding, and other materials that when repaired, renovated, removed, contained, disposed of, or otherwise disturbed do not become friable and do not require additional costs above and beyond normal repair, renovation, removal, containment, or disposal costs to prevent them from becoming friable. For asbestos-related cleanup costs that are deemed to be probable but not reasonably estimable; the entity should disclose the presence of asbestos in its facilities and the inability to reasonably estimate an amount of the total clean up costs.

5. Description of FIN 47 Requirements

FIN 47 clarifies that the term conditional asset retirement obligation as used in FASB Statement No. 143, *Accounting for Asset Retirement Obligations*, refers to a legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. FIN 47 provides that the obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and (or) method of settlement.

Accordingly, FIN 47 requires that if an entity has sufficient information to reasonably estimate the fair value of an asset retirement obligation, it must recognize a liability at the time the liability is incurred. An asset retirement obligation would be reasonably estimable if (a) it is evident that the fair value of the obligation is embodied in the acquisition price of the asset, (b) an active market exists for the transfer of the obligation, or (c) sufficient information exists to apply an expected present value technique. An entity would have sufficient information to apply an expected present value technique and therefore an asset retirement obligation would be reasonably estimable if either of the following conditions exists:

- The settlement date and method of settlement for the obligation have been specified by others. For example, the law, regulation, or contract that gives rise to the legal obligation specifies the settlement date and method of settlement
- The information is available to reasonably estimate (1) the settlement date or the range of potential settlement dates, (2) the method of settlement or potential

methods of settlement,⁷ and (3) the probabilities associated with the potential settlement dates and potential methods of settlement

Appendix A of FIN 47 includes examples that illustrate the application of the interpretation specifically relating to when an entity would be required to initially recognize the fair value of an obligation based on the facts provided. Example 3 illustrates the recognition provision when an entity does not have sufficient information to reasonably estimate the fair value of an asbestos related cleanup cost at the time the asset is acquired. In this scenario, an entity acquires a factory that contains asbestos. After the acquisition date, regulations are put in place that require the entity to handle and dispose of this type of asbestos in a special manner if the factory undergoes major renovations or is demolished. Otherwise, the entity is not required to remove asbestos from the factory. The entity believes it does not have sufficient information to estimate the fair value of the asset retirement obligation because the settlement date or the range of potential settlement dates has not been specified by others and information is not available to apply an expected present value technique. For example, there are no plans or expectation of plans to undertake a major renovation that would require removal of the asbestos or demolition of the factory.

6. Description of Issue

The guiding standards and requirements for the federal government have not been properly interpreted. The federal agencies have interpreted the standard to suggest recognition of *asbestos and asset disposal related cleanup* costs at the time the asset is placed in service without regard to FIN 47 recognition provision when sufficient information such as settlement date or method or plan to undertake a major renovation, which would require the removal of the asbestos, is not available. Thus, if sufficient information is not available at the time the liability is incurred (e.g., asset is placed in service), the liability shall be recognized initially in the period in which sufficient information becomes available to estimate its fair value.

In some cases to report the clean up cost associated with asbestos, the agencies are advised to undertake extensive and expensive engineering studies to determine the estimated cost of cleanup when there are no existing plans to dispose or renovate the asset which would require removal of the asbestos. In addition, agencies can not determine the nonfriable asbestos that would remain nonfriable and/or will not require additional costs above and beyond normal repair, renovation, removal, containment, or disposal costs before a settlement method is determined because the closure or disposal conditions and requirements are unknown.

Environmental liabilities associated with the disposal or retirement of military equipment changed significantly with the implementation of SFFAS No. 23. Prior to this standard the following language, which relates to the reporting stewardship assets, applied:

Para 101 - Consistent with the treatment of the acquisition cost of stewardship PP&E (i.e., expensing in the period placed in service), the total estimated cleanup cost shall be

recognized as expense in the period that the stewardship asset is placed in service and a liability established.

SFFAS No. 23, classified military equipment as General PP&E, which required that it be reported in accordance with the following paragraph of SFFAS No. 6:

Para 98 - Recognition of the expense and accumulation of the liability shall begin on the date that the PP&E is placed into service, continue in each period that operation continues, and be completed when the PP&E ceases operation.

Since the full liability for cleanup of assets such as nuclear submarines applies at the date of acquisition the original stewardship reporting policy would appear to recognize the liability more accurately. The AAPC may choose to raise this issue to the FASAB for consideration,

7. Recommendation

- a. The federal entities would not recognize an asbestos cleanup liability at the time the asset is placed in service for non-friable asbestos if the entity does not have sufficient information to estimate the value of the obligation. Sufficient information is available when the settlement date and method of settlement for the obligation have been specified. The entity would, however, disclose (a) a description of the obligation (presence of asbestos), (b) the fact that a liability has not been recognized because the value cannot be reasonably estimated, and (c) the reasons why value can not be reasonably estimated.

There is a need for additional information regarding the disposal of equipment and personal property prior to the completion of recommendations for its disposal.