3 lessons learned from navigating asset impairment in 2020

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Accounting for asset impairment took on new importance as the economy weathered unforeseen challenges in

2020. What lessons can be learned for 2021?

Before COVID-19 hit, most in-house accounting professionals probably never thought they'd need a crash course in **asset impairment** accounting to get through the year. But 2020 was a year unlike any other.

As the pandemic shut down the economy, businesses scrambled to adapt their operating plans and assess the financial fallout. Among other action steps required, businesses needed to evaluate whether their nonfinancial assets became impaired, and if so, to determine how much value those assets had lost. Accounting and finance teams wrestled with the complexities of triggering events and accounting models for impairment testing that vary across asset classes.

But here's the upside: Lessons learned from the asset impairment exercise can help organizations make better business decisions in 2021 and improve their resilience in the long term. Now is a perfect time to pause, take a deep breath, and review the takeaways from the start of the pandemic to today.

Lesson 1: Asset impairment will remain a priority in 2021

Now that the calendar year-end reporting season is here, assessing asset impairment will be unavoidable for many businesses closing their books on 2020. At the heart of the issue, businesses need to determine if key assets – such as inventory; property, plant, and equipment; or goodwill and intangibles – experienced a triggering event and now require an impairment charge. If assets are impaired, their loss in value must be recorded and reflected on the financial statements in the period the impairment occurred.

Over the course of 2020, businesses struggled to determine if their assets were actually impaired and what cashflows they could expect from them. Uncertainty reigned, as the market saw significant fluctuation. In many cases, significant company resources and management judgment were required to decide whether a triggering event had occurred and if further assessment of impairment was needed.

In 2021, as businesses prepare their 2020 financial statements and many go through their year-end audit process, organizations will need to report definitively whether any assets have been impaired and show auditors detailed documentation to back up their assertions, including whether triggering events occurred and, if so, whether and when assets became impaired.

Lesson 2: Asset impairments exposed the need for better documentation and data

When the economy is good and business is humming along, documentation on impairment assessments might consist of a short memo. That's not going to be enough after a year like 2020. Auditors will expect organizations to justify their conclusions in detail. Organizations should review their current documentation processes now and make any improvements or determine if they need a third party to supplement their evaluation and documentation.

Imperfect or inadequate data proved to be an even bigger concern in 2020. For example, in fair value analyses of an entity's equity used in a goodwill impairment assessment under ASC 350, most valuation professionals use three methods: the income approach (discounted cash flows (DCFs)), guideline public company comparisons (GPCs), and analysis of comparable control transactions. Given the economic uncertainty in 2020, two of those methods were limited in their application. GPCs and control transactions provided inconclusive data points in many cases, leaving valuation professionals with DCFs as the primary valuation method. Because this method requires a detailed set of projections of future cash flows, even this method proved challenging.

Now is the time to examine processes and systems: Is your organization able to collect data that's granular enough to make meaningful decisions?

Lesson 3: Inadequate processes made asset impairment evaluations harder

During the pandemic, businesses might have discovered that they didn't have robust processes in place to conduct impairment testing, or they didn't have the in-house expertise to research the multiple accounting models for asset impairment or determine nonfinancial asset valuations in the midst of so much market uncertainty. Businesses have not had to devote this level of scrutiny to evaluating asset impairment since the recession of 2007-2009.

Because asset impairment assessments might continue to be a focus throughout 2021, organizations should shore up their processes by:

- Familiarizing themselves with FASB's impairment testing requirements under ASC 330, ASC 350, and ASC 360, which define the frequency and order of testing for different assets.
- Reviewing detailed, step-by-step accounting guidance for all types of impairments, found in our on-demand webinar, "Triggering Events and Asset Impairment – What You Need to Know," and a summary of this guidance in our article, "Accounting for Nonfinancial Asset Impairment."
- Mapping out internal processes for collecting the necessary data and documentation to support judgments and get started early with impairment testing.
- Determining if they need a third-party adviser well-versed in asset impairment accounting and valuation. Organizations should consider establishing a relationship now so that they're prepared for new challenges as the pandemic continues.

As 2021 unfolds, a clearer picture will emerge about how impairments affected businesses in 2020, including which sectors were hardest hit. But looking forward, the need to assess asset impairment might continue to require management's judgment throughout 2021 and beyond. The businesses that have established strong processes and that excel at forecasting can gain an advantage by making better decisions and wasting less time on this effort.

Share your questions and concerns

Talk to a Crowe specialist about your asset impairment needs. We're ready to assist your organization with research, documentation, impairment testing, and much more.

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