

# GRAND METROPOLITAN

PUBLIC LIMITED COMPANY

8 HENRIETTA PLACE, LONDON W1M 9AG  
TELEPHONE 0171-518 5200 FAX 0171-518 4600

13 August 1997

The Secretary-General,  
International Accounting Standards Committee  
167 Fleet Street  
London EC4A 2ES

Dear Sir,

## **E55 - Impairment of Assets**

We have reviewed the IASC's proposed standard on the impairment of assets and set out our detailed comments below. As a general comment, we consider it useful that the IASC and ASB have issued exposure drafts on this topic concurrently, as this makes assessment and comparison between the two drafts much easier.

### **Restoration of past losses - double counting**

E55 paragraph 33 states that estimates of future cash flows used to calculate value in use should not include cash outflows that will be required to settle obligations that have already been recognised as liabilities. The IASC however do not address this issue in considering reversals of impairment losses, where a future major outflow (eg restructuring cost) is accounted for as a liability subsequent to it causing an asset impairment. In such cases, the outflow would impact the profit and loss account twice, firstly upon the asset write down, and secondly upon the cost being recorded as a liability. We believe that in such instances it would be appropriate for the impairment loss to be restored.

Incidentally, while cash flows associated with items already recognised as major liabilities, such as restructuring provisions, should be excluded from value in use calculations to avoid double counting, the blanket heading of 'liabilities' in paragraph 32 (a) would appear to exclude items such as trade creditors. For simplicity's sake, such items should be included in carrying amounts, with the associated outflows included within the value in use calculation.

### **Normalisation of cash flows for terminal value calculations**

Terminal values, which estimate the present value of the 'steady state' cash flows beyond the period covered by formal budgets, represent the bulk of the value of an asset or income generating unit - generally over 80% of the value in use in respect of 3 year specific forecasts and over 70% in respect of 5 year forecasts. Perhaps surprisingly, in cases where high growth is forecast initially this percentage *increases*. The significance of the terminal value to the calculation argues for a less rigid approach to growth rate assumptions, with disclosure required where a business expects to exceed average country growth rates.

....adding value



It is also important that the cash flow for the last specific year on which the terminal value is based is representative - any unusual variation in the opening year cash flows, eg heavy capital expenditure or large working capital swings will distort the terminal value and could have a material effect on the value in use calculated. We consider that in circumstances where the last specific year cash flows for a terminal value calculation are atypical for a particular reason which is not expected to continue into the future, some 'normalisation' process should be carried out to ensure that the terminal value calculation is as accurate as possible.

#### **Exclusion of corporate liabilities from impairment testing**

In all its references to the allocation of central assets for the purpose of calculating carrying amounts, the IASC refer to 'goodwill or other corporate assets' without referring to corporate liabilities. There may be corporate liabilities which should be included for impairment testing purposes and for completeness some mention should be given to these.

Please contact me if you wish to discuss any of the above,

Yours sincerely,

A handwritten signature in black ink, appearing to read 'JA Southern', written in a cursive style.

**Jonathan Southern**  
**Director of Accounting**