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The Secretary-General  
International Accounting Standards  
Committee  
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Basel, 15 August 1997  
AKM

Dear Sir

**Proposed International Accounting Standard - Impairment of Assets -  
Exposure Draft E55**

Coopers & Lybrand is pleased to submit comments on Exposure Draft E55, *Impairment of Assets*. Our comments reflect the views of our International Accounting Task Force which is composed of senior technical partners from the nine member firms of Coopers & Lybrand International, a limited liability association incorporated in Switzerland.

Our comments address the questions posed in the "Invitation to Comment". Our key comments can be summarised as follows:

- ♦ We support the principles of the impairment review and the measurement of recoverable amount, but we are concerned that the proposed requirements are too detailed and prescriptive for what is essentially a very subjective exercise that depends on individual circumstances. We would prefer to see much of the detail in the form of an illustrative appendix rather than detailed rules.
- ♦ We believe there will be practical difficulties in some areas, particularly for less sophisticated enterprises.
- ♦ We agree with the E55 proposals in respect of the reversal of impairment losses and accept that more restrictive reversal criteria should apply to goodwill and intangible assets for which no active market exists.
- ♦ The proposed disclosures are excessive, may require disclosure of commercially sensitive information and appear in large measure to be intended to discipline companies in their preparation of cash flow projections.

## Measurement of Recoverable Amount

1. Which of the following approaches do you support:

- (a) *the recoverable amount of an asset should be measured as the higher of its net selling price and its value in use (paragraphs 5 and 12-40 of the Exposure Draft and paragraphs 7-30 of the Basis for Conclusions)?*
- (b) *the recoverable amount of an asset should be measured as the fair value of the asset, that is, the amount obtainable for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction. Fair value would be primarily based on the asset's market price if a market exists for that asset regardless of the value in use of the asset. If no market exists for the asset, fair value would be estimated in a similar way to value in use as defined in the Exposure Draft (paragraphs 13-19 of the Basis for Conclusions)?*
- (c) *other (please specify)?*

We support option (a). Although we consider the two-step approach in FAS 121 is practical and operational, we do not oppose the Board's proposed one-step approach for recognizing and measuring the impairment of assets. If fair value is lower than value in use, the onus will clearly be on management to demonstrate that the higher carrying value is justified.

2. *One consequence of the approach adopted in this Exposure Draft (or the alternative definition of recoverable amount based on fair value) is that present value techniques should be used to measure the recoverable amount of an asset, implicitly (net selling price) or explicitly (value in use) (paragraphs 7-9 and 11-12 of the Basis for Conclusions). Do you agree that present value techniques should be used to measure the recoverable amount of an asset, implicitly (net selling price) or explicitly (value in use)?*

We agree that present value techniques should be used to measure the recoverability of an asset. We note that the basis for measuring net selling price should assume that the amount obtainable from the sale at the date of the impairment review is the price that could then be obtained after proper marketing of the asset during a normal period before the valuation date. In addition, for assets held for disposal, the recoverable amount based on net selling price may need to be discounted if disposal is not expected to occur within one year.

## Assets Held for Disposal

3. *Do you agree that the definition of recoverable amount in paragraph 5 of the Exposure Draft is just as applicable to an asset held for disposal as to an asset held for continuing use (paragraph 26 of the Basis for Conclusions)?*

We agree that the definition of recoverable amount (being the higher of an asset's net selling price and its value in use) can be applied to an asset held for disposal. We agree with the Board's conclusion that further guidance is not necessary for assessing whether the carrying amount of an asset is impaired. The fact that value in use will often be the same as net selling price does not mean that the definition itself is inapplicable.

## Recognition of Impairment Losses

4. *Do you agree that an impairment loss should be recognized for an asset:*
- (a) whenever the recoverable amount of the asset is less than its carrying amount (paragraph 41 of the Exposure Draft and paragraphs 59-67 of the Basis for Conclusions); and*
  - (b) only if the cash-generating unit to which the asset belongs is impaired (paragraphs 55-58 of the Exposure Draft and paragraphs 74-75 of the Basis for Conclusions)?*

*If you disagree with these proposals, please indicate criteria you would prefer for the recognition of an impairment loss in the financial statements.*

We believe that an impairment loss should be recognized whenever the recoverable amount of an asset (if the asset's cash flow can be separately identified) or of a cash generating unit to which the asset belongs is less than its carrying amount.

5. *Do you agree that an impairment loss recognized in prior years for an asset carried on an historical cost basis should be reversed up to the depreciated historical cost of the asset if, and only if, there has been a change in the estimates used to determine the impaired asset's recoverable amount since the last impairment loss was recognized (paragraphs 70-76 of the Exposure Draft and paragraphs 83-87 of the Basis of Conclusions)?*

We agree that, for assets other than goodwill and certain intangibles, previously recognised impairment losses should be reversed when there is a change in the estimates used to determine the asset's recoverable amount, as proposed in paragraphs 70 to 76 of the Exposure Draft. In our view, this is consistent with the general treatment of changes in estimates.

6. *Do you agree that an impairment loss recognized for goodwill and other intangible assets for which no active market exists should be reversed in a subsequent period if, and only if, the external event that caused the recognition of the impairment loss has reversed (paragraphs 77-78 of the Exposure Draft)?*

We agree with the limitation cited in paragraphs 77-78 of the Exposure Draft.

## Scope

7. *Do you agree that the Standard should apply to all assets except those listed in paragraph 1 of the Exposure Draft (paragraphs 1-4 of the Exposure Draft and paragraphs 106-110 of the Basis for Conclusions)?*

We agree, but we assume that paragraph 3's reference to investments in subsidiaries, associates and joint ventures only applies to non-consolidated entity accounts of the investor. When an investment in a subsidiary is consolidated, the underlying assets of the subsidiary would reflect any impairment loss recorded by that subsidiary. Similarly, an impairment loss would also be reflected in recording a proportionate share of results of investments in associates and joint ventures accounted for under the equity method.

In any case, it is unclear how the proposals in the Exposure Draft will apply to such investments. For instance, what is the "asset" for the purpose of determining recoverable amount? This is not discussed in E55. Therefore, it is not clear if the investor should treat the investment as a single asset or if it should look through the investment and perform impairment tests on the individual assets recorded in, say, the associate's books. The latter is likely to be impractical but it is not obvious how the definition of recoverable amount can be applied to the investment as a single asset.

## Identifying a Potentially Impaired Asset

8. *Do you agree that:*

- (a) *the recoverable amount of an asset should be estimated if, and only if, there is an indication that the asset is impaired; and*
  - (b) *the list of indicators of impairment included in paragraph 8 of the Exposure Draft will require an enterprise to estimate the recoverable amount whenever there is a significant risk that the asset is impaired?*
- (paragraphs 6-12 of the Exposure Draft)*

We agree that the recoverable amount of an asset (cash generating unit) should be estimated if there is an indication that the asset is impaired. The list of indicators of impairment provides adequate guidance as to the types of events and changes in circumstances that indicate that the carrying amount of an asset should be assessed.

## Net Selling Price

9. *Do you agree that net selling price should be determined:*

- (a) *based on "the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties" and that is not necessary to determine net selling price by reference to an active market (paragraphs 5 and 17-18 of the Exposure Draft and paragraphs 31-38 of the Basis for Conclusions); and*
- (b) *after deducting from the amount obtainable from the sale of an asset the incremental costs that are directly attributable to the disposal of the asset (excluding finance costs and income tax expense) (paragraphs 5 and 19-21 of the Exposure Draft and paragraph 35 of the Basis for Conclusions)?*

We agree with the definition of "net selling price".

## Value in Use

10. *Do you agree with the proposed requirements and guidance in the Exposure Draft for:*

- (a) *the basis for estimates of future cash flows (paragraphs 23-27 of the Exposure Draft and paragraphs 24 and 40-42 of the Basis for Conclusions);*
- (b) *the composition of estimates of future cash flows (paragraphs 28-35 of the Exposure Draft and paragraphs 43-46 and 50-58 of the Basis of Conclusions); and*
- (c) *selecting the discount rate (paragraphs 36-40 of the Exposure Draft and paragraphs 47-49 of the Basis for Conclusions)?*

We generally agree with the principles for calculating value in use. However, we are concerned that the requirements are too detailed (more so than FAS 121) and prescriptive for what is essentially an individual and very subjective business decision. We fear there will be considerable practical difficulties which could result in impairment reviews being done badly. Paradoxically, the calculations may be manipulable because some of the underlying variables (such as the choice of discount rate) are likely to be so subjective. The example in paragraph 29 is just one example that demonstrates the difficulty of designing a rule that will not be able to be applied rigidly in practice.

A suggestion is that the detail on how an impairment review should be carried out could be presented as an illustrative appendix (as used in other standards, for instance, IAS 18) rather than in the standard itself.

Taxation is one example of an issue where there may be valid alternative methods to fit different circumstances. We believe the proposed guidance should be silent on whether income tax receipts or payments should be included. Since there may be certain tax credits that could justify using a net-of-tax-approach, we believe the role of income taxes in the determination of value in use should be based on facts and circumstances. The important point is that both the carrying value and the recoverable amount must be evaluated on a consistent basis.

We believe that long-term cash flow estimates based on the short-term cash flow projection with a terminal value may be preferable to an estimate based on an extrapolation from short-term projections. The terminal value represents the stream of free cash flows beyond the last year of the projection period. For long lived assets, the terminal value is theoretically approximately equal to the sum of the present values of the future cash flows beyond the last projected year.

The choice of discount rate will be a difficult practical issue for many enterprises. Matters such as determining what the risks are and how to adjust for them, assessing rates relating to comparable assets, may be fine in theory but, for all but the most sophisticated enterprises, of little practical use. Discounting is a complex area and it is likely that further practical guidance will be necessary, possibly as part of a wider project on this subject.

## Cash-Generating Units

11. *Do you agree that, if an asset does not generate cash inflows that are largely independent of those from other assets, an enterprise should determine the recoverable amount of the asset's cash-generating unit (paragraphs 46-47 of the Exposure Draft)?*

We agree with the proposed guidance.

12. *Do you agree with the requirements and guidance for determining the items that are included in a cash-generating unit (paragraphs 5 and 48-53 of the Exposure Draft)?*

We agree with the proposed guidance but believe that it should be extended to include further guidance on the allocation of assets to cash-generating units as the notion of allocating assets could provide scope for manipulation.

13. *Do you agree with the requirement (and related guidance) to recognize and measure an impairment loss if there exists goodwill or other corporate assets (such as head office assets) that relate to a cash-generating unit (paragraphs 59-61 of the Exposure Draft and paragraphs 79-81 of the Basis for Conclusions)?*

We agree with the principle of the "bottom-up" and "top-down" test. However, as the Board admits, this approach will often make it easy for enterprises to avoid recognising impairments of purchased goodwill.

14. *Do you agree with the procedures for allocating an impairment loss of a cash-generating unit between the assets of that unit (paragraphs 62-65 of the Exposure Draft and paragraphs 77-78 of the Basis for Conclusion)?*

We agree with the procedures for allocating an impairment loss of a cash-generating unit between assets of that unit. In addition, we believe an example should be added to Appendix 1 to illustrate the application of paragraph 65.

## Disclosure

15. *Do you agree with the disclosure requirements in paragraphs 79-81 of the Exposure Draft and that an enterprise should not be required to disclose more information, such as the amount of impairment losses that can be reversed in subsequent periods (paragraphs 88-92 of the Basis for Conclusions)?*

We agree. We believe the guidance in paragraphs 79-81 should be expanded to require that if the income statement caption "income from operations" or its equivalent is used, impairment losses recognized or reversed should be included as a component of that item.

16. *Do you agree with the disclosure requirements in paragraph 82 of the Exposure Draft and that an enterprise should not be required to disclose for each individual asset (or cash-generating unit) for which significant impairment losses have been recognized or reversed during the period:*
- (a) the value in use of the asset (cash-generating unit) if the recoverable amount is based on the net selling price of the asset (cash-generating unit);*
  - (b) the net selling price of the asset (cash-generating unit) if the recoverable amount is based on the value in use of the asset (cash-generating unit);*
  - (c) if the recoverable amount is based on the value in use of the asset (cash-generating unit):*
    - (i) the discount rate(s) used in the calculation; and*
    - (ii) the assumed long-term average growth rate for the products, industries, and country or countries in which the enterprise operates or for the market in which the asset (cash-generating unit) is used; and*
  - (d) other key assumptions used to determine the recoverable amount of an asset (paragraphs 24, 93-95 and 98-99 of the Basis for Conclusions)?*

We believe that the disclosure requirements in paragraph 82 parts "a" and "b" provide adequate disclosures that are useful to users of financial statements.

We do not support the disclosures proposed in parts "c" and "d" of paragraph 82.

We believe the information required by paragraph 82 part "c" may be confusing to financial statement users and is extraneous to understanding the nature of an impairment loss. In addition, we are concerned that the proposed disclosures in paragraph 82 part "d" are intended to discipline a company in its preparation of cash flow projections. In our view, these items are audit issues that should be resolved between a company and their outside auditors. We are also concerned that these disclosure requirements will cause companies to make more optimistic cash flow projections. They may also involve commercially sensitive information.

We agree that the additional disclosures described in Question 16 should not be required.

17. *Do you agree with the disclosure requirements in paragraphs 83-84 of the Exposure Draft and that an enterprise should not be required to disclose information similar to that proposed in question 16 above for each individual asset (cash-generating unit) for which:*

- (a) recoverable amount has been determined during the period;*
- (b) no impairment loss was recognized or reversed during the period; and*
- (c) a small change in key assumptions could lead to the recognition or reversal of a significant impairment loss  
(paragraphs 24 and 96-97 of the Basis for Conclusions)?*

We do not support the disclosure requirements proposed in paragraphs 83-84. Disclosure of the kind of information proposed in paragraph 83 is likely to give confusing messages to the markets. If a company's management and auditors have been satisfied that there has been no impairment, it is unreasonable to require the company to disclose details of the impairment review.

However, we do believe that if it is reasonably possible that a change in key assumptions could lead to the recognition or reversal of a significant impairment loss, then that fact should be disclosed. This disclosure could be given in the Management Discussion and Analysis (or its equivalent statement) or could be required as part of a larger exercise to enhance disclosures of measurement uncertainties generally.

We agree that the additional disclosures described in Question 17 should not be required

18. *Do you agree with the disclosure requirements in paragraph 85 of the Exposure Draft (paragraphs 24 and 100-101 of the Basis for Conclusions)?*



We disagree with the disclosure requirements proposed in paragraph 85 as we believe that these could be misleading/misunderstood. Once again, we are concerned with the Board's attempt to use financial statement disclosure to discipline company's cash flow assessments. We question whether requiring such disclosures will cause an enterprise to make overly optimistic estimates of future cash flows.

The first part of paragraph 85 is an accounting rather than a disclosure requirement.

*19. Do you agree that an enterprise should not be required to give information on how cash-generating units are determined (paragraphs 102-105 of the Basis for Conclusions)? If you believe that such information should be required, please indicate which details should be required.*

We do not believe that information on how cash-generating units are determined should be disclosed. The benefits of such disclosures do not justify the cost, and in some cases, would require that companies disclose sensitive, proprietary information.

*20. Should an enterprise be required to disclose any information other than that discussed in questions 15-19 to this Invitation to Comment?*

No.

## Appendices

*21. Should any material in Appendix 1 be amended or deleted? Should any further guidance be added to the appendix? (Note: the Board does not intend to publish appendix 3, Basis for Conclusions, with the final Standard.)*

We believe that Example 3 should be amended to include an illustration of (1) an impairment loss that would not be reversed (paragraph 73) and, (2) an impairment loss that would be reversed for goodwill and other intangible assets for which no active market exists (paragraph 77).

It would also be helpful if an example was added to illustrate the identification of a cash-generating unit.

*22. Do you agree with the consequential changes to IAS 16, Property, Plant and Equipment (Appendix 2, Proposed Amendments to Other International Accounting Standards)?*

The changes to IAS 16 appear appropriate.

## Other Comments

*Do you have any other comments on the proposed International Accounting Standard?*

The IASC should address implementation and transition requirements in the final standard. In our view, implementation of the proposed standard should be done uniformly and consistently among all entities. We believe that the proposed standard should be applied prospectively, that is, impairment losses (including pre-existing losses) recognised for the first time on implementation of the standard should be reported in the current year income statement.

We would be pleased to discuss these comments with you. Any questions should be addressed to Martin Aked, STG Coopers & Lybrand, Postfach 4152, CH-4002, Basel, Switzerland.

Kind regards

*Martin Aked*

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