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Exposure Draft E 55: Impairment of Assets

Dear Sir,

We have pleasure in enclosing our answers to the questions on pages 5 to 10 of E 55. Where appropriate we summarize our comments on several questions.

Questions 1-3:

We disagree that the recoverable amount of an asset should be measured as the higher of its net selling price and its value in use. Instead, we support that the recoverable amount of an asset should be measured as the fair value of the asset. Moreover, we are of the opinion that it should be differentiated between a definition of recoverable amount of assets held for use and a definition of recoverable amount of assets held for disposal. We developed this opinion for the following reasons:

- We disagree with the Board's assumption that an enterprise will make an investment decision once the recoverability of the asset has been tested as mentioned in paragraph 8 of the Basis for Conclusion. In our opinion, the decision to dispose or to continue to use an asset is depending on internal considerations and not on the external figures to be reported in the

financial statements. When the recoverable amount of an asset is to be estimated for external reporting the decision to dispose or to continue to use an asset has already been made. Thus, in our opinion for measuring an impairment loss it is necessary to differentiate between a definition of recoverable amount of assets held for use and a definition of recoverable amount of assets held for disposal.

- Moreover, the necessity to use differentiated measurements is reasonable because for measuring the recoverable amount of assets held to dispose the cost of sales has to be taken into account. While, for measuring the recoverable amount of assets held to use, it would be wrong to subtract the cost of sales with respect to the underlying going concern assumption.
- Since the decision to continue to use an asset is economically similar to the decision to invest in that asset the recoverable amount of an asset held to use should be measured as the fair value of the asset. Presuming that an enterprise would not decide to continue to use an asset unless this decision generates a higher expected future cash flow than the alternative of selling and reinvesting in that asset, the fair value is the best measure of the cost of continuing to use an impaired asset.
- An estimate of the present value of an asset is always influenced by judgement and is therefore less reliable than using a market price. Applying the fair value approach the recoverable amount will be identified as the reliable market price, if available. However, using the approach favoured by the IASC (i.e. the higher of its net selling price and its value in use) an asset might be valued at the less reliable value in use even if the more reliable market price is available.
- The requirement to measure the recoverable amount as the higher of its net selling price and its value in use the enterprise has to estimate two additional values for each potentially impaired asset. An enterprise using the allowed alternative treatment for measurement of property, plant and equipment subsequent to initial recognition has to estimate even three values, which are the net selling price, the value in use and the fair value. In contrast to this approach, the fair value approach requires only to estimate one value, the fair value. Especially, because - as even admitted by the IASC - only in few cases both approaches will

lead to different recoverable amounts, we think it is not reasonable to require to estimate two more values which are costly to provide and might be even less reliable and not always more relevant. This „balance between benefit and cost“-argument is even more important, since the IASC prefers the economic criterion, which requires to estimate the recoverable amount whenever several indicators identify a potentially impaired asset.

Question 4:

We object that recognition of an impairment loss should be based on an economic criterion, but prefer that recognition of an impairment loss should be based on a probability criterion, for the following reason:

The list of indicators to identify potentially impaired assets is a good tool to give a first hint of impairment of assets. However, because of the high dynamic in several industries there might be always at least one indicator that identifies an asset as potentially impaired. Thus, using the economic criterion many enterprises have to estimate the recoverable amount of almost all of their assets every year. If a market price is available, it is easy to estimate the recoverable amount. However, if a market price is not available, the present value of these assets has to be estimated. Using the approach to define the recoverable amount favoured by the IASC the present value has to be estimated even for every potentially impaired asset.

Furthermore, the listed indicators are qualitative factors identifying an impairment of asset, which requires subjective judgements. Thus, a numerical probability test would reduce the arbitrariness connected with the impairment test.

Questions 5 and 6:

We disagree that an impairment loss of an asset held to use recognised in prior years should be reversed if there has been a change in the estimates to determine the recoverable amount resulting in an again increased recoverable amount.

Since we support the historical cost accounting system, we assume that the recoverable amount becomes the new cost basis for the impaired asset. Thus, reversing an impairment loss is comparable with revaluing an asset. Therefore, a reversal of an impairment loss may at the most be recognised in equity. However, since we do not agree to revaluation for property, plant, equipment and intangible assets held to use, we are of the opinion that the reversal of an impairment loss should not be allowed.

Furthermore, since the identification of an potentially impaired asset as well as the estimation of a recoverable amount is depending on subjective judgements, the requirement to reverse an impairment loss also influenced by subjective judgements allows an company to smooth its income.

Also, to review the impairment loss every year increases even more the already above criticized high costs connected with the proposed impairment test.

Question 7:

We agree with the scope.

Question 8:

We agree with the list of indicators of impairment. However, as already mentioned in our answer to question 4 we are of the opinion that these indicators can only give a first hint for impairment of assets. Thus in our opinion, there should be another probability test before having to estimate the recoverable amount of a potentially impaired asset.

Question 9 and 10:

Generally, we agree with the definition of the net selling price and of the value in use. However, as already mentioned in our comment to question 1 to 3 we do not agree that the recoverable amount of an asset should be measured as the higher of its net selling price and its value in use.

Question 11 and 12:

We agree.

Question 13:

We do not agree with your proposal to recognise and measure an impairment loss if there exists goodwill or other corporate assets that relate to a cash-generating unit.

The special feature of goodwill is that it contains values, which cannot be assigned to separable assets. Thus, in our opinion in most cases it is impossible to allocate the goodwill to cash-generating units. We can only imagine one case where a reasonable basis exists for allocating a goodwill to a cash-generating unit. This is the case where all assets of an acquisition accounted for using the purchase method belong to one cash-generating unit. At the most, it might be even reasonable to allocate a goodwill on a pro rata basis using the fair value of the cash generating unit, if only some but not all of the assets of the acquisition belongs to a cash-generating unit.

However, in our opinion it is arbitrary to allocate other corporate assets or a goodwill for which no reasonable basis for allocating exists.

Thus, in our opinion paragraph 59 to 61 has to be totally amended. At first the requirement to allocate goodwill to a cash-generating unit should be limited to the special cases mentioned above. Secondly the top-down test should be deleted.

Question 14:

In our opinion an impairment loss should be at first allocated to goodwill (if any), secondly to any intangible asset for which no active market exists and thirdly to the remaining assets of the unit on a pro rata basis.

We disagree that the remaining assets should be further divided in those assets whose net selling price is less than their carrying amount and the other assets. This is consistent with our opinion that the recoverable amount should be measured as the fair value and not as stated by the IASC as the higher of its net selling price and its value in use (see our comment on questions 1 to 3).

The procedure for allocating impairment losses stated in paragraph 65 seems to be impracticable, complicated and arbitrary. Therefore, we suggest to delete this paragraph.

Questions 15 to 20:

In our opinion, the required disclosures are much too excessive.

Beside the fact that we object the requirement of several disclosures like 79 b), 82 c) etc., according to our disagreement with how to identify impaired assets and to estimate recoverable amounts as well as our disagreement with the reversal requirement, we do also not agree to the requirement of disclosure for each individual asset, whether impaired or not.

In our opinion the disclosures should be limited to a description of the impaired assets and the indicators leading to the impairment, the total amount of the impairment loss recognised in the period and a description of how the fair value was determined. If the impairment loss is not reported as a separate item in the income statement, it should be disclosed in which item the loss is aggregated.

Question 21 and 22:

We are of the opinion that the appendices are very helpful to understand and apply the IAS „impairment of asset“. Therefore we recommend to publish the appendices, including appendix 3 with the final IAS.

We thank you for your attention to the above and hope that our comments are helpful to the Steering Committee in order to modify the regulations for accounting for impairment of assets.

Yours faithfully,

VEBA Aktiengesellschaft

Mr. Linn i.B. von Kopp