



The Secretary General
International Accounting
Standards Committee
167 Fleet Street

GB - London EC4A 2ES

19 August 1997

IAS E55 - Impairment of Assets

Dear Sir

I have pleasure enclosing our Novartis comments on the specific areas requested in the Exposure Draft. As you can see there are the following two key areas where we have major disagreements:

Points 2 & 4

- utilisation should also be a criteria, especially where it is difficult to define a "cash generating" unit.

Points 8, 10 & 12

- it is unrealistic to assume that cash flows can always be calculated. It should be permissible to book impairment losses on, for example, infrastructure items even though the cash flow on the cash generating unit, which could be the whole group in these circumstances, may be positive. E55 as it is presently written is too restrictive and lacking prudence.

Yours sincerely,

A handwritten signature in dark ink, appearing to read "M.B. Cheetham", written over a light blue horizontal line.

M.B. Cheetham
Head of Group Reporting

Enclosure

IAS E55 – Impairment of Assets

Draft

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 (paragraph 5 and 12-40 of the Exposure Draft and paragraphs 7-30 of the Basis for Conclusions)?

Yes

(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)?

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(c) other (please specify)?

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)?

Novartis Comments

In principle accept present value techniques. We consider, however, that you should provide guidance as to how to calculate cash flows for:

- infrastructure assets
- fixed assets that are a small part of a large plant
- safety/environmental items.

Draft**Novartis Comments****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)?

Yes

Recognition of Impairment Losses

4. Do you agree that an impairment loss should be recognised 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)?

Agree to (a) only. Disagree that (b) is necessary. There is too much emphasis on linking impairment to a cash generating unit. We suggest that not only cash flows of an asset but also its utilisation percentage are important factors in determining whether or not there is an asset impairment.

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

Reversals of Impairment Losses

5. Do you agree that an impairment loss recognised 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 recognised (paragraphs 70-76 of the Exposure Draft and paragraphs 83-87 of the Basis for Conclusions)?

Agree

Draft

6. Do you agree that an impairment loss recognised 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)?

The Board also welcomes answers to the following questions, with reasons for those answers.

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)?

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)

Novartis Comments

Yes

Agree

Agree with the list given in ED para 8, however, we do not agree that these should be turned solely into cash flow impairment criteria. For example, the internal sources of information are on a micro-economic level. These can easily indicate that there is an asset impairment, without it necessarily resulting in an impairment for a cash generating unit.

Draft**Novartis Comments****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 it 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)?

Yes

Yes

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 for Conclusions); and
- (c) selecting the discount rate (paragraphs 36-40 of the Exposure Draft and paragraphs 47-49 of the Basis for Conclusions)?

Disagree with the concept that an impairment loss should be booked only if a cash generating unit is impaired. Furthermore, it is unrealistic to assume that cash flows can be determined for all assets. "Value in use" should be in accordance with the words used. For example, in your example in para 47, we consider that if the infrastructure, here a railway, is clearly underutilised or obsolete, then this, and not cash flow from the whole business, should be sufficient to justify an impairment adjustment. Where cash flows can be used then the ED proposals are acceptable.

Draft**Novartis Comments****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)?
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)?
13. Do you agree with the requirement (and related guidance) to recognise 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)?
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 Conclusions)?

No – See comments already provided above.

Description of a cash-generating unit is acceptable, however, this should not preclude impairments due to utilisation or obsolescence issues in sub-units.

In principle do not disagree although guidance is very theoretical.

Yes

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)?
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 recognised or reversed during the period:

Yes

Para 82 is far too detailed. At most asset groups should be disclosed. Only sub-paras (a) and (b) of para 82 are acceptable.

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- (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)?

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 recognised during the period; and

This should not be disclosed

This should not be disclosed

This should not be disclosed

This should not be disclosed

This should not be disclosed

Paras 83 & 84 should not be required. Furthermore, (a) – (c) below should also not be required.

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- (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)?

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)?

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.

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

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.)

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

Other Comments

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

Novartis Comments

Disagree

Yes

No

As far as it goes it is acceptable. It needs substantial additions, however, to cover all of the issues mentioned above concerning utilisation and obsolescence.

Para 74 of IAS 16 should not only refer to an asset's recoverable value being determined on a discounted basis.

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