

***Association pour la participation des entreprises françaises
à l'harmonisation comptable internationale***

Sir Bryan Carlsberg
Secretary General
IASC
Fleet Street, 167
London EC4A 2ES
UNITED KINGDOM

Le Président
CVT\GM\25.97

Paris, July 31st 1997

Dear Sir,

The « Association pour la participation des entreprises françaises à l'harmonisation comptable internationale » has considered the Exposure Draft E55 on « Impairment of assets » and is pleased to submit to you its comments as set out in the enclosed document.

As you can see by yourself, our comments are consistent with the french answer to E50 (december 1995).

Yours sincerely,

9/5 
Bruno Lafont

Association pour la participation des entreprises françaises à l'harmonisation comptable internationale

Response to E55 « Impairment of assets »

General comments

Because the exposure draft on impairment of assets contains requirements which result directly from the revised standards on intangible assets and business combinations, we believe that it should not be discussed separately, but that the three standards should be discussed as a whole.

In particular, we understand that the Board has introduced an annual impairment test on long term assets as a consequence for not enforcing maximum limit to the useful life and period of amortisation of intangible assets and goodwill.

We wish to reaffirm that we disagree with the obligation included in E50 on intangible assets to amortise any intangible asset, of whatever nature. **We support the view that certain intangible assets may have an indefinite useful life ; in such case, amortisation is not the adequate method and should be deleted : the carrying amount should be then validated by a systematic impairment test.**

Therefore, we intend to answer E55 from a strictly technical point of view, without being engaged on issues regarding the exposure draft on intangible assets. Because of the strong links existing between Impairment and Intangible assets issues, our comments on E55 might change once the exposure draft on intangible assets is published.

Regarding E55, our opinion is that applying the impairment test as specified is too stringent and burdensome for companies. Our specific proposals are as follows :

- E55 should apply only to intangible assets and those of tangible assets which are part of cash generating unit comprising both tangible and intangible assets. We think that for other tangible assets, a less stringent method should be used.
- We believe that preliminary tests on long term assets should be authorized based on undiscounted indicators.
- The discounted cash flows method is not the only reliable method to measure the value in use of an asset. According to the nature of the business and the way the related assets were measured on initial recognition, other methods, which are based on indicators often closely linked to profitability, can be more appropriate and could then be relied upon as alternatives to the discounted cash flows method.

- The recognition of an impairment loss in the financial statements should be based on a « permanent criterion » rather than on an « economic criterion ».

In this case, it should be possible not to recognise an impairment loss which results from a pure arithmetical calculation if the management is able to demonstrate its temporary or accidental character and expects to see it reversed. Otherwise, systematic recognition of impairment losses could be misleading in interpreting the performance of the enterprise and could lead to an increasing volatility of the net income of companies.

- For similar reasons, we are opposed to consider the market interest rate as a triggering indicator for the impairment test.

Responses to specific questions

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 ?*
- (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 ?*
- (c) *other (please specify) ?*

We support the (a) approach.

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). 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 **do not agree** to use present value technics for the test (see our genaral comment above). But, if the test shows the necessity to calculate te recoverable amount of an asset, we **agree** to use the present value technics (see also question 10).

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 ?*

We agree.

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 ;*
and
 - (b) only, if the cash generating unit to which the asset belongs is impaired ?*

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

We **agree** that an impairment loss should be recognised for an asset only if the cash generating unit to which the asset belongs is impaired.

However, we **do not support** the « economic criterion » which has been elected by the steering committee. We support the « permanent criterion » : an impairment loss should be recognised if the recoverable amount is lower than the carrying amount and it is expected that such an impairment loss will not reverse.

We believe that the choice of the « permanent criterion » avoids the recognition of temporary decreases in the recoverable amount of an asset which would be misleading in interpreting the performance of the enterprise. It should be possible not to recognise an impairment loss which results from a pure arithmetical calculation if the management is able to demonstrate that the impairment loss has a temporary or an accidental character and expects to see it reversed.

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 ?*

We agree.

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 ?*

We **disagree**. We believe both indicators, internal and external, should be taken into account for the reversal as well as they have been used for the recognition of the impairment loss.

Scope

7. *Do you agree that the standard should apply to all assets except those listed in paragraph 1 of the exposure draft ?*

Subject to our general comment on tangible assets, we **agree** and we would like to **add** to that list :

- assets held for satisfying insurance obligations ;
- interest in associates and joint ventures accounted for by the equity method.

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 ?*

We **support** that the recoverable amount of an asset should be estimated if, and only if, there is an indication that the asset is impaired.

We **concur** with the list of indicators **except** for the following :

- **we do not agree** with the present wording of paragraph (c) : an increase in market interest rates or other market rate of return on investments should not be an indicator for considering that an asset may be impaired. In particular, a company should not incur an impairment loss if the actual rate of return of an asset is not materially lower than the rate that was expected at the date of acquisition.

We then believe that paragraph (c) should be limited to assets generating current and projected cash flow losses or which have an actual rate of return which is expected to be materially lower than the one forecasted initially ;

- criteria (g) which should be merged with criteria (f).

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 ; 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) ?*

We **agree**.

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 ;*
- (b) the composition of estimates of future cash flows ; and*
- (c) selecting the discount rate ?*

We believe that various methods are possible to determine the value in use and not only the cash flows method. These methods, which are based on indicators closely linked to profitability, depend on the nature of the business and the way related assets were measured on initial recognition.

Regarding the cash flows method, our comments are the following :

- (a) we **do not agree** with the limit set by the steering committee : short term projections should cover a maximum period of five years unless a larger period can be justified. We believe that the short terms projections should be adjusted to the forecast period used by the company as it depends on business features.
- (b) we **agree**.
- (c) we **disagree**. We believe that the specific risk of the asset should be taken into account either in the discount rate, or in the projections of cash flows, according to the internal business plan procedures of each company.

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 ?*

We **agree**.

12. *Do you agree with the requirements and guidance for determining the items that are included in a cash generating unit ?*

We **agree**.

13. *Do you agree with the requirements (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 ?*

We **agree**.

14. *Do you agree with the procedures for allocating an impairment loss of a cash generating unit between the assets of that unit ?*

We **do not agree**. We believe that the company should be free to allocate, proportionally or totally, the impairment loss to goodwill, intangible or tangible assets. This choice should reflect the economic situation of the cash generating unit and of each of its components.

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 ?*

We **agree**.

16. *Do you agree with the disclosure requirements in paragraphs 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 :*

- (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.*

We **do not agree** with the disclosure requirements.

The level of disclosure is not appropriate and should be reduced to the following information :

- for each class of assets, an analysis splitting the total amount of the impaired assets between assets for which recoverable amount is based on the value in use and those for which the recoverable amount is based on the net selling price ;
- the range of discount rates used in the calculation of the value in use.

We **agree** with the unrequired disclosure.

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 for which :*

- (a) recoverable amount has been determined during the period ;*
- (b) no impairment loss was recognised 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 ?*

We **do not agree** with the information required (see above answer to question 16).

18. *Do you agree with the disclosure requirements in paragraph 85 of the exposure draft ?*

We **do not agree** (see above).

19. *Do you agree that an enterprise should not be required to give information on how cash generating units are determined ? If you believe that such information should be required, please indicate which details should be required.*

We **agree** (see above).

20. *Should an enterprise be required to disclose any information other than that discussed in question 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 ?*

No.

22. *Do you agree with the consequential changes to IAS16, property, plant and equipment ?*

No.

Other comments

23. *Do you have any other comments on the proposed international accounting standard ?*

Please refer to our general comments above.



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