

lived asset (asset group) is not recoverable and exceeds its fair value. The carrying amount of a long-lived asset (asset group) is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset (asset group). The staff would object to a write down of long-lived assets to a "normalized depreciation" value as representing an acceptable alternative to the approaches required in Statement 144.

The staff also believes that registrants must continually evaluate the appropriateness of useful lives assigned to long-lived assets, including identifiable intangible assets and goodwill. In the above fact pattern, management had contemplated removal of the mainframe computers beginning in January 20X2 and, more formally, in August 20X2 as part of compiling the 20X3 capital expenditures budget. At those times, at a minimum, management should have reevaluated the original useful life assigned to the computers to determine whether a seven year amortization period remained appropriate given the company's current facts and circumstances, including ongoing technological changes in the market place. This reevaluation process should have continued at the time of the September 20X2 board of directors' meeting to discuss capital expenditure plans and, further, as the company pursued mainframe computer bids. Given the contemporaneous evidence that management's best estimate during much of 20X2 was that the current mainframe computers would be removed from service in 20X3, the depreciable life of the computers should have been adjusted prior to 20X3 to reflect this new estimate. The staff does not view the recognition of an impairment charge to be an acceptable substitute for choosing the appropriate initial amortization or depreciation period or subsequently adjusting this period as company or industry conditions change. The staff's view applies also to selection of, and changes to, estimated residual values.

Consequently, the staff may challenge impairment charges for which the timely evaluation of useful life and residual value cannot be demonstrated.

Question 3: Has the staff expressed any views with respect to company-determined estimates of cash flows used for assessing and measuring impairment of assets under Statement 144?

Interpretive Response: In providing guidance on the development of cash flows for purposes of applying the provisions of Statement 144, paragraph 17 of that Statement indicates that

"estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) shall incorporate the entity's own assumptions about its use of the asset (asset group) and shall consider all available evidence. The assumptions used in developing those estimates shall be reasonable in relation to the assumptions used in developing other information used by the entity for comparable periods, such as internal budgets and projections, accruals related to incentive compensation plans, or information communicated to others."

The staff recognizes that various factors, including management's judgments and assumptions about the business plans and strategies, affect the development of future cash flow projections for purposes of applying Statement 144. The staff, however, cautions registrants that the judgments and assumptions made for purposes of applying Statement 144 must be consistent with other financial statement calculations and disclosures and disclosures in MD&A. The staff also expects that forecasts made for purposes of applying Statement 144 be consistent with other forward-looking information prepared by the company, such as that used for internal budgets, incentive compensation plans, discussions with lenders or third parties, and/or reporting to management or the board of directors.

For example, the staff has reviewed a fact pattern where a registrant developed cash flow projections for purposes of applying the provisions of Statement 144 using one set of assumptions and utilized a second, more conservative set of assumptions for purposes of determining whether deferred tax valuation allowances were necessary when applying the provisions of Statement 109. In this case, the staff objected to the use of inconsistent assumptions.

In addition to disclosure of key assumptions used in the development of cash flow projections, the staff also has required discussion in MD&A of the implications of assumptions. For example, do the projections indicate that a company is likely to violate debt covenants in the future? What are the ramifications to the cash flow projections used in the impairment analysis? If growth rates used in the impairment analysis are lower than those used by outside analysts, has the company had discussions with the analysts regarding their overly optimistic projections? Has the company appropriately informed the market and its shareholders of its reduced expectations for the future that are sufficient to cause an impairment

charge? The staff believes that cash flow projections used in the impairment analysis must be both internally consistent with the company's other projections and externally consistent with financial statement and other public disclosures.

Topic 6: Interpretations of Accounting Series Releases and Financial Reporting Releases

A.1. Deleted by SAB 103

B. Accounting Series Release 280—General Revision of Regulation S-X: Income or Loss Applicable to Common Stock

Facts: A registrant has various classes of preferred stock. Dividends on those preferred stocks and accretions of their carrying amounts cause income applicable to common stock to be less than reported net income.

Question: In ASR 280, the Commission stated that although it had determined not to mandate presentation of income or loss applicable to common stock in all cases, it believes that disclosure of that amount is of value in certain situations. In what situations should the amount be reported, where should it be reported, and how should it be computed?

Interpretive Response: Income or loss applicable to common stock should be reported on the face of the income statement¹ when it is materially different in quantitative terms from reported net income or loss² or when it is indicative of significant trends or other qualitative considerations. The amount to be reported should be computed for each period as net income or loss less: (a) Dividends on preferred stock, including undeclared or unpaid dividends if cumulative; and (b) periodic increases in the carrying amounts of instruments reported as redeemable preferred stock (as discussed in Topic 3.C) or increasing rate preferred stock (as discussed in Topic 5.Q).

¹ If a registrant elects to follow the encouraged disclosure discussed in paragraph 23 of Statement 130, and displays the components of other comprehensive income and the total for comprehensive income using a one-statement approach, the registrant must continue to follow the guidance set forth in the SAB Topic. One approach may be to provide a separate reconciliation of net income to income available to common stock below comprehensive income reported on a statement of income and comprehensive income.

² The assessment of materiality is the responsibility of each registrant. However, absent concerns about trends or other qualitative considerations, the staff generally will not insist on the reporting of income or loss applicable to common stock if the amount differs from net income or loss by less than ten percent.