

R-00174104  
HMS CROSS-Exam. Ex. #1  
Pittsburgh 12-15-97  
EWA

Item No. : HSS-5-06  
Witness: Clayton  
Page 1 of 1

DUQUESNE LIGHT COMPANY

Fifth Set of Interrogatories of Hospital Shared Services and Administrative Resources, Inc.

- 6. At page 45 of Mr. Clayton's rebuttal testimony, he states that OCA's, OTS', DII's, and HSS' proposal "would cause write-offs of \$658 million, \$181 million, \$461 million and \$1.8 billion in 1998." To the extent that any portion of the write-offs referred to by Mr. Clayton relate to generation assets (as opposed to regulatory assets), please describe with specificity the basis for any such write-offs. Please identify the amount of write-off for each generation asset. Please also describe with specificity the rules that would allow for such write-offs under financial reporting standards.

Response:

The basis for the identified write-offs is the difference in stranded cost identified in Exhibit DJC-10. For the OTS it is implied that Duquesne's market value estimates are used in the calculations. The amount of generation asset write-offs including the BV-2 lease are \$614 million, \$177 million, \$370 million and \$1,542 million for OCA, OTS, DII and HSS/ARJ, respectively. These write-offs would be required under the provisions of SFAS 121 which deals with impaired assets. A more detailed discussion of the basis for generating asset write-offs is included in Mr. O'Brien's direct testimony at pp. 21 and 22.

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ANDREWS  
**Financial Accounting Series**

**Statement of Financial Accounting Standards No. 121**

Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of



Financial Accounting Standards Board  
of the Financial Accounting Foundation

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Statement of Financial Accounting Standards No. 121

Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of

March 1995

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## Statement of Financial Accounting Standards No. 121

### Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of

March 1995

#### INTRODUCTION

1. This Statement establishes accounting standards for the impairment of long-lived assets, certain identifiable intangibles, and goodwill related to those assets to be held and used and for long-lived assets and certain identifiable intangibles to be disposed of.
2. Long-lived assets such as plant and equipment generally are recorded at cost, which is usually fair value at the date of acquisition. The original cost usually is reduced over time by depreciation (amortization) so that the cost of the asset is allocated to the periods in which the asset is used. That practice has been modified in some circumstances when an asset has been determined to be impaired, in which case the asset has been written down to a new carrying amount that is less than the remaining cost and a loss has been recognized. Accounting standards generally have not addressed when impairment losses should be recognized or how impairment losses should be measured. As a result, practice has been diverse.

#### STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

##### Scope

3. This Statement applies to long-lived assets, certain identifiable intangibles, and goodwill related to those assets to be held and used and to long-lived assets and certain identifiable intangibles to be disposed of. The Statement applies to all entities. This Statement does not apply to financial instruments, long-term customer relationships of a financial institution (for example, core deposit intangibles and credit cardholder intangibles), mortgage and other servicing rights, deferred policy acquisition costs, or deferred tax assets. It also does not apply to assets whose accounting is prescribed by:
  - a. FASB Statement No. 50, *Financial Reporting in the Record and Music Industry*
  - b. FASB Statement No. 53, *Financial Reporting by Producers and Distributors of Motion Picture Films*
  - c. FASB Statement No. 63, *Financial Reporting by Broadcasters*

- d. FASB Statement No. 86, *Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed*
- e. FASB Statement No. 90, *Regulated Enterprises—Accounting for Abandonments and Disallowances of Plant Costs*.

Appendix B contains a list of certain pronouncements that refer to impairment or disposal of assets and indicates which pronouncements are amended by this Statement and which pronouncements remain as authoritative literature. All references to an asset in this Statement also refer to groups of assets representing the lowest level of identifiable cash flows as described in paragraph 8.

#### Assets to Be Held and Used

##### Recognition and Measurement of Impairment

4. An entity shall review long-lived assets and certain identifiable intangibles to be held and used for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

5. The following are examples of events or changes in circumstances that indicate that the recoverability of the carrying amount of an asset should be assessed:

- a. A significant decrease in the market value of an asset
- b. A significant change in the extent or manner in which an asset is used or a significant physical change in an asset
- c. A significant adverse change in legal factors or in the business climate that could affect the value of an asset or an adverse action or assessment by a regulator
- d. An accumulation of costs significantly in excess of the amount originally expected to acquire or construct an asset
- e. A current period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with an asset used for the purpose of producing revenue.

6. If the examples of events or changes in circumstances set forth in paragraph 5 are present or if other events or changes in circumstances indicate that the carrying amount of an asset that an entity expects to hold and use may not be recoverable, the entity shall estimate the future cash flows expected to result from the use of the asset and its eventual disposition. Future cash flows are the future cash inflows expected to be generated by an asset less the future cash outflows expected to be necessary to obtain those inflows. If the sum of the expected future cash flows (undiscounted and without interest charges)

is less than the carrying amount of the asset, the entity shall recognize an impairment loss in accordance with this Statement. Otherwise, an impairment loss shall not be recognized; however, a review of depreciation policies may be appropriate.<sup>1</sup>

7. An impairment loss recognized in accordance with paragraph 6 shall be measured as the amount by which the carrying amount of the asset exceeds the fair value of the asset. The fair value of an asset is the amount at which the asset could be bought or sold in a current transaction between willing parties, that is, other than in a forced or liquidation sale. Quoted market prices in active markets are the best evidence of fair value and shall be used as the basis for the measurement, if available. If quoted market prices are not available, the estimate of fair value shall consider prices for available in the circumstances. The estimate of fair value shall be based on the best information available in the circumstances. Examples of valuation techniques include the present value of estimated future cash flows using a discount rate commensurate with the risks involved, option-pricing models, matrix pricing, option-adjusted spread models, and fundamental analysis.

8. In estimating expected future cash flows for determining whether an asset is impaired (paragraph 6), and if expected future cash flows are used in measuring assets that are impaired (paragraph 7), assets shall be grouped at the lowest level for which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets.

9. Estimates of expected future cash flows shall be the best estimate based on reasonable and supportable assumptions and projections. All available evidence should be considered in developing estimates of expected future cash flows. The weight given to the evidence should be commensurate with the extent to which the evidence can be verified objectively. If a range is estimated for either the amount or timing of possible cash flows, the likelihood of possible outcomes shall be considered in determining the best estimate of future cash flows.

<sup>1</sup>Paragraph 10 of APB Opinion No. 20, *Accounting Changes*, addresses the accounting for changes in depreciation estimates, and paragraph 32 addresses the accounting for changes in the method of depreciation. Whenever there is reason to assess the recoverability of the carrying amount of an asset under paragraphs 4 and 5 of this Statement, there may be reason to review the depreciation estimates and method under paragraphs 10 and 32 of Opinion 20. However, an impairment loss that results from applying this Statement should be recognized prior to performing that review. The provisions of Opinion 20 apply to the reporting of changes in the depreciation estimates and method regardless of whether an impairment loss is recognized under paragraph 6 of this Statement.