

Manage Your Asset Retirement Obligations More Accurately

New Application Automates the ARO Management Process

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Asset retirement obligation (ARO) may not mean much to people outside the finance department, but it's an important accounting requirement that companies must fulfill, for both regulatory compliance and business reasons. For many years, it has involved manual, time-consuming steps, especially for companies in asset-intensive industries such as utilities, telecommunications, oil and gas, mining, and retail.

To help our customers streamline their efforts and increase the accuracy of their ledgers, SAP has developed an application that automates the data management and accounting processes associated with managing AROs. **SAP Asset Retirement Obligation Management**, scheduled to be generally available this year, will be a welcome solution to companies with a large number of assets or with a significant amount of asset retirement costs that must be calculated according to one or more accounting principles.

Why ARO Management Is Important

Regulatory requirements and accounting rules implemented in the past decade call for deeper visibility into companies' current and future financial obligations. Regulators and investors don't like surprises, so regulations and accounting principles now govern how companies account for and display the costs they will incur when they retire assets in the future (see callout on the next page). Those assets include equipment, buildings, land, or other items.

For example, if a telecom company leases land and building space to erect thousands of cell towers, the leases will likely require the company to remove the towers and restore the land and building

space to their original state at the end of the leases. After all, the land and building owners don't want to incur the cost of removing the towers, so the telecom company will have to bear the cost of "retiring those assets" when the leases expire.

To satisfy auditors, companies must take several accounting steps to show on their books what that retirement cost will be and when it will come due. A company has to:

- Determine how much it would cost to retire each of those assets in today's value. In our example, the telecom company must estimate the cost of removing each cell tower today.
- Perform an inflation calculation based on an estimated inflation rate to determine how much it will cost to retire those assets at the time they plan to be retired. If the telecom company's leases run for 20 years, it must calculate the projected future costs to remove the cell towers in 2032.
- Perform a discounting of the future costs to determine the net present value (that is, today's value), and post this value to its ledger.
- Continually post interest accretion to adjust the value and to show that the company can cover the costs when they come due at the time of the assets' retirement.
- Adjust the calculations and postings over the life of the assets as necessary based on changes to relevant parameters such as costs, terms, and discounting rates, so the retirement obligation remains an accurate projection.

Companies also need to track the timing of the asset retirements. If a business doesn't forecast these costs accurately, its asset retirement costs



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for a given year could swell and negatively affect the company's financial performance.

How ARO Is Handled Today

Today, the most common method for performing ARO calculations and recordkeeping is using spreadsheets. Each ARO has a corresponding spreadsheet with updated formulas for the calculations and formats that conform to the accounting principles of the country for which the accounting is taking place. Once the data is entered or updated in the document, the numbers must be manually posted to the ledger in the SAP system.

For a company that owns thousands of cell towers, managing a separate spreadsheet for each asset is nearly impossible. So a company will create clusters of assets and maintain a separate spreadsheet for each cluster, but that still results in hundreds or thousands of spreadsheets to manage manually. If that process takes one employee half a day to complete, with 500 spreadsheets to calculate, it means that 250 days of an employee's time is dedicated to this single process. Using spreadsheets also prevents a company from tracing manual changes to formulas, which may create problems during an audit. And having disparate sets of spreadsheets may make it difficult to generate accurate reports.

SAP Asset Retirement Obligation Management to the Rescue

To help customers manage this complicated and time-consuming process, SAP has developed the SAP Asset Retirement Obligation Management application.¹ With this solution, companies no longer have to keep track of hundreds of spreadsheets and manually input data. Instead, the entire ARO process can be completed within the SAP environment. Users can create, adjust, update, and store obligations within the SAP system.

The application focuses on two areas: data management and accounting.

Automating Data Management

First, a user creates an obligation in the application, enters parameters, and provides an initial cost estimate for retiring that asset and an expected retirement date. The application then automatically calculates the retirement obligation

provisions based on built-in logic for the applicable countries and regulations. The application will apply the required financial standards, such as US GAAP, to perform the calculation. If multiple accounting principles are applicable, it performs the appropriate calculations in parallel.

All of the data and information around the ARO calculations, including the formulas and estimated interest rates, is stored in the SAP system for future reference, making the data more easily accessible across the enterprise.

Automating Accounting

After the application generates the correct obligation provision amount and interest accretion, the next step is the automated posting process. If a company still used spreadsheets, a user would have to manually take data from the spreadsheet and enter it into SAP General Ledger. SAP Asset Retirement Obligation Management is integrated directly with SAP ERP Financials, so a user can instantly post the relevant amounts to, for example, SAP General Ledger and the Asset Accounting module in SAP ERP Financials, with the push of a single button. Again, if multiple accounting principles are applicable, the solution posts the relevant amounts in parallel.

The result is dramatic time savings in the ARO process. Rather than take a half-day to produce and calculate each ARO, that process can be reduced to a few minutes. Multiply that time savings by the number of AROs a company has, and the annual time savings are significant.

Beyond Time Savings

In addition to automating the process, SAP Asset Retirement Obligation Management creates a much clearer audit trail. All of the historical data and calculations are housed within the SAP system, all changes to the data are tracked, and manual, ad hoc data changes are not possible. This level of visibility makes auditing and regulatory compliance even more streamlined.

Creating and storing the data in the SAP system, rather than across various spreadsheets, opens up new possibilities for enterprise reporting. In addition to proving regulatory compliance more easily, the improved reporting allows companies to gain a clearer picture of how much their total ARO spend will impact them in the future. For more details, visit <http://help.sap.com/aro>. ■

What's Driving ARO Management?

Several regulations require companies to perform asset retirement obligation (ARO) calculations on their ledgers:

- US GAAP (FASB/FAS143)
- International Financial Reporting Standards (IASB/IAS37)
- German Accounting Principle HGB (BilMoG §249/§253)

SAP Asset Retirement Obligation Management currently handles ARO calculations according to these accounting principles.

¹ Working with customers, SAP developed the solution in the Focus Area Financials group of SAP Custom Development.