



IFRS Adviser Alert

Insights into IAS 36 *Impairment of Assets*

April 2022

Executive summary

The Grant Thornton International IFRS team has three new publications in the *Insights into IAS 36* series:

- *Comparing recoverable amount with carrying amount;*
- *Recognizing impairment losses;*
- *Reversing impairment losses.*

IAS 36 *Impairment of Assets* is not a new standard, and while many of its requirements are familiar, an impairment review of assets (either tangible or intangible) is frequently challenging to apply in practice. This is because IAS 36's guidance is detailed, prescriptive and complex in some areas.

The *Insights into IAS 36* series have been written to assist preparers of financial statements and those charged with the governance of reporting entities to understand the requirements set out in IAS 36, and revisit some areas where confusion has been seen in practice.

The next three publications in the *Insights into IAS 36* series cover steps 5 and 6 of the impairment review, namely comparing recoverable amount with carrying amount and recognizing or reversing any impairment losses:

- *Comparing recoverable amount with carrying amount;*
- *Recognizing impairment losses;*
- *Reversing impairment losses.*

Resource

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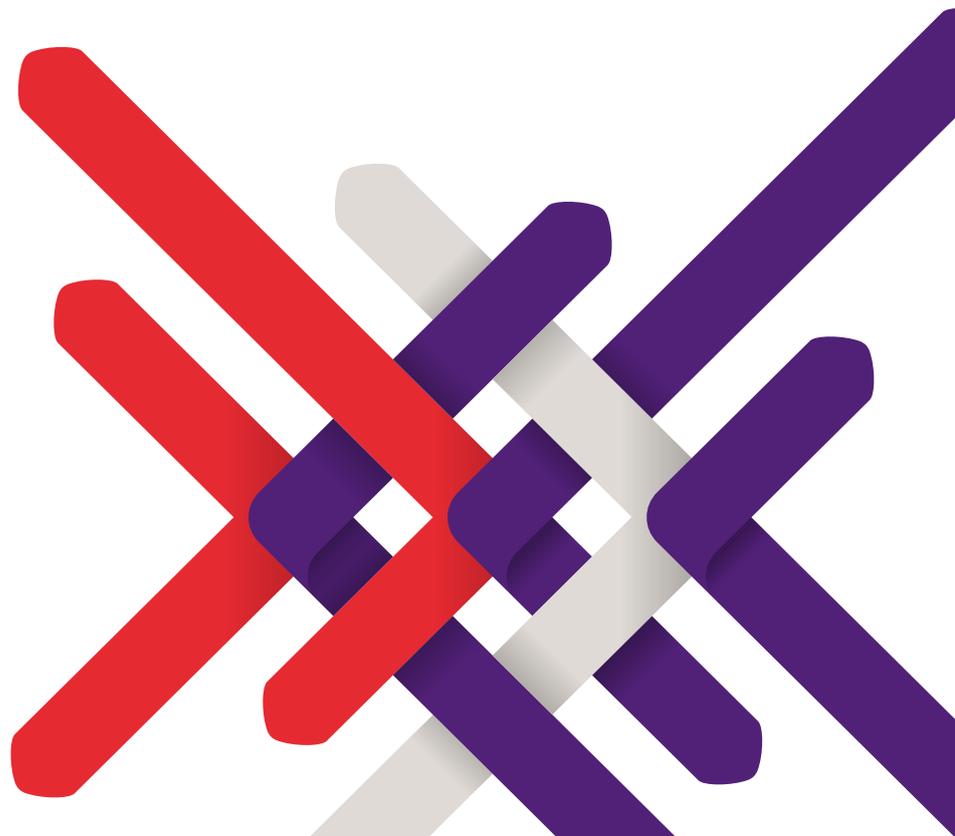
Insights into IAS 36

Comparing recoverable amount with carrying amount

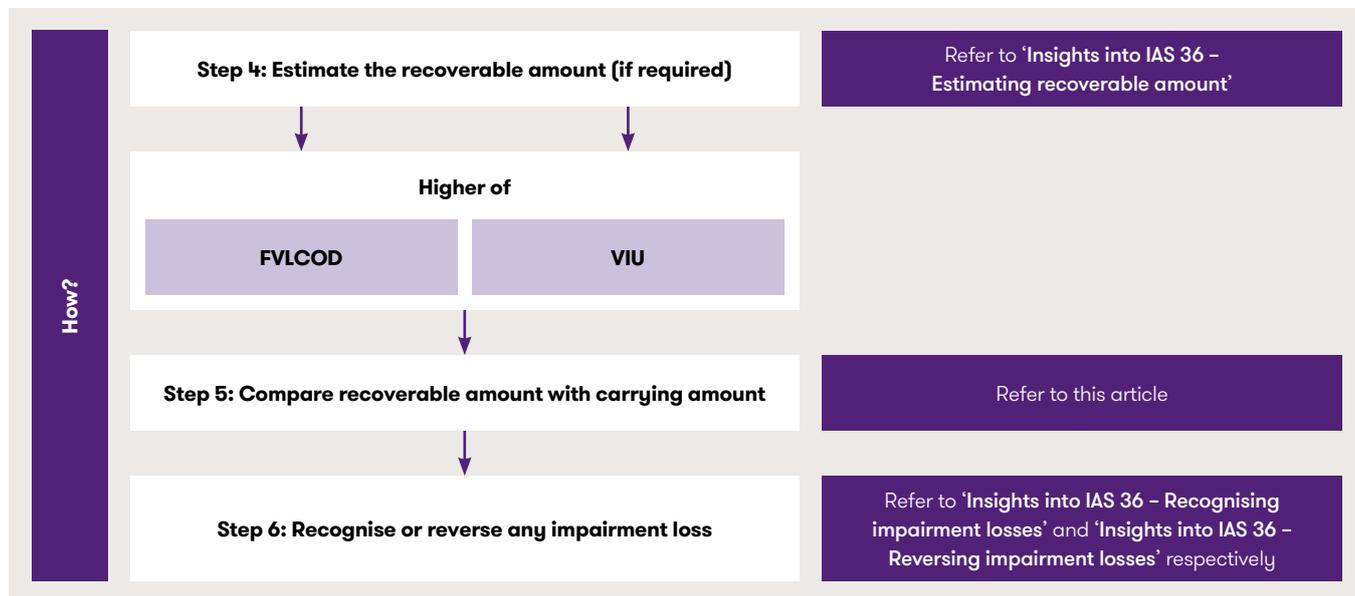
IAS 36 'Impairment of Assets' sets out the requirements for carrying out impairment reviews of assets (both tangible and intangible). IAS 36 is not a new Standard, and while many of its requirements are familiar, the guidance in IAS 36 is comprehensive but complex in some areas, and therefore it is challenging to apply in practice by preparers of financial statements.

The articles in our 'Insights into IAS 36' series have been written to assist preparers of financial statements and those charged with the governance of reporting entities understand the requirements set out in IAS 36, and revisit some areas where confusion has been seen in practice.

This article discusses when there are exceptions to the rule of comparing recoverable amount with carrying amount, which is step 5 in the impairment review process, as shown below.



IAS 36's step by step impairment approach is explained and set out in full in our article '[Insights into IAS 36 – Overview of the Standard](#)'. However to give some context over how the next three articles fit into this approach, here is a reminder of steps 4 to 6 (the 'How' part of the process).



After calculating the asset's recoverable amount (as discussed in Step 4), the next step is to compare this to the carrying amount. Where the carrying amount exceeds the recoverable amount, the entity will record an impairment loss (Step 6).

Although making this comparison may appear straightforward, practical issues arise in relation to:

- including the right assets (and, in limited circumstances, liabilities) to ensure a 'like for like' correspondence with the cash flows underpinning the recoverable amount, and
- the order of testing for purposes of comparing the carrying amount to the recoverable amount when allocated corporate assets or goodwill relate to more than one cash-generating unit (CGU).



Like-for-like comparison of recoverable amount and carrying amount of a CGU

When assets are grouped for recoverability assessments, it is important to include in the CGU all assets that generate or are used to generate the relevant cash inflows. If assets are omitted inappropriately, the CGU may appear to be fully recoverable when an impairment loss has in fact occurred. The overarching objective is that the CGU's carrying amount is determined consistently with its recoverable amount.

The recoverable amount of a CGU (as discussed in Step 4, refer to our article '[Insights into IAS 36 – Estimating the recoverable amount](#)') is determined excluding cash flows that relate to:

- assets whose cash flows are largely independent of the cash inflows from the asset under review (for example, financial assets such as receivables), and
- liabilities that have already been recognised

Certain exceptions to this general rule apply and are discussed in more detail below.

Exceptions to the rule – including other assets and liabilities

Liabilities that are inseparable from the CGU

It may be necessary to consider some recognised liabilities to determine the recoverable amount of a CGU. This may be the case when the disposal of the CGU would require the buyer to assume the liability. As such, the fair value less cost of disposal (FVLCO) of the CGU might be estimated using pricing information that takes account of the liability that buyers would assume.

To perform a meaningful comparison between the carrying amount of the CGU and its recoverable amount, the liability is also deducted from the CGU's carrying amount and the cash flows from settling the liability are included in the value in use (VIU) calculation. The example below illustrates this point.

Example 1 – Including liabilities that relate to the CGU

A company operates a mine in a country where legislation requires that the owner must restore the site on completion of its mining operations. The cost of restoration includes the replacement of the overburden, which must be removed before mining operations commence. A provision for the costs to replace the overburden was recognised as soon as the overburden was removed. The amount provided was recognised as part of the cost of the mine and is being depreciated over the mine's useful life. The carrying amount of the provision for restoration costs is CU500, which is equal to the present value of the restoration costs. The entity is testing the mine for impairment. The CGU is the mine as a whole. The entity has received various offers to buy the mine at a price around CU800. The price reflects the fact the buyer will assume the obligation to restore the overburden. Disposal costs for the mine are negligible. The VIU of the mine is approximately CU1,200, excluding restoration costs. The carrying amount of the mine is CU1,000.

Analysis

The CGU's FVLCO is CU800. This amount considers the restoration costs that have been provided for. As a consequence, the VIU for the CGU is determined after consideration of the restoration costs and is estimated to be CU700 (CU1,200 less CU500). The carrying amount of the CGU is CU500, which is the carrying amount of the mine (CU1,000) less the carrying amount of the provision for restoration costs (CU500). Therefore, the recoverable amount of the CGU (CU800 being the higher of the FVLCO and VIU) exceeds its carrying amount (CU500) and the CGU is not impaired.

In this example, it should be noted, it would not be necessary in practice to calculate both FVLCO and VIU (as both amounts exceed carrying value).

Practical insight – Including liabilities that relate to the CGU

The key reason to include some liabilities in a CGU is the market-based transaction price on which fair value is based necessarily includes the transfer of any liabilities that are inseparable from the asset. If the impairment test is based solely on VIU (eg because FVL COD cannot be measured reliably) it may not be necessary to include inseparable liabilities and the related cash flows to achieve a meaningful and like-for-like comparison. In any case, including or excluding the liability (and related cash outflows) will often make little or no practical difference (eg if the liability is short-term or if it is discounted using a similar rate to that used for estimating VIU).

Other assets/liabilities

Sometimes, for practical reasons, the recoverable amount of a CGU is determined after consideration of assets that are not part of the CGU (for example, receivables or other financial assets) or liabilities that have been recognised (for example, payables, pensions and other provisions). In such cases the carrying amount of the CGU is:

- increased by the carrying amount of those assets, and
- decreased by the carrying amount of those liabilities.

Practical insight – Other assets/liabilities

The carrying amount of a liability may not be the present value of its future cash outflows or may not be discounted using the same rate as for estimating VIU. One such example is a pension obligation which might be discounted using a high quality corporate bond rate. If an entity includes the pension contributions in its cash flows for VIU purposes, it will need to consider if some portion of those contributions relates to past services and is therefore a settlement of part of the pension liability. Achieving a like-for-like comparison is potentially a complex exercise. However, it is not possible to simply ignore the costs of providing pensions and other employee benefits when estimating VIU and a pragmatic approach (such as including future service costs rather than contributions, and excluding the liability) might need to be taken.

Practical insight – Rent-free periods

A situation frequently met in practice is the case of ‘rent-free’ periods not arising as a consequence of the COVID-19 pandemic, whereby a lessee recognises a liability and expense during the period of time in which no cash payment is due to the lessor as a result of straight-lining the lease payments over the lease term. A question arises as to whether the lessee should include this liability as part of the carrying amount of the CGU being tested for impairment if the estimates of future cash flows include 100% of the future lease payments (therefore including those that effectively settle the liability).

As discussed in our article ‘[Insights into IAS 36 – Value in use: estimating future cash inflows and outflows](#)’, in estimating VIU, an entity will incorporate the future cash inflows and outflows from continuing to use the group of assets and from its ultimate disposal; however, estimates of future cash flows would not include cash outflows for settling liabilities that have already been recognised unless the associated liability is included as part of the CGU being tested for impairment. In the case of a rent-free period, comparing like-for-like could be achieved either by:

- including all the future lease payments in the cash outflows when estimating VIU and deducting the rent-free period liability from the CGU’s the carrying amount, or
- excluding both the liability and the portion of the future lease payments that effectively settle it. In many cases including the straight-lined based lease expense (instead of the full lease payment) should prove a sufficiently accurate approximation.

Practical insight - Working capital balances

In our view, cash flows from the settlement or realisation of working capital balances (that exist at the measurement date) may be included or excluded in the cash flow projections in estimating VIU, so long as a consistent approach is taken when deriving the carrying amount of the CGU. The net effect should be insignificant where the present value of cash flows from the settlement or realisation of working capital items would be similar to the balances themselves. However, in estimating future cash flows for VIU purposes, material changes in future working capital requirements associated with the asset or CGU under review need to be considered.

Careful consideration must be given to inventory. The basic approach would be to exclude inventory balances from the impairment review as it is excluded from the scope of IAS 36 (and addressed in IAS 2 'Inventories'). Under this approach, the estimated future cash flows from future sales of the inventory held at the measurement date should be excluded when estimating VIU. Where management includes inventory in its VIU calculation for practical reasons, it will include the estimated future cash flows from future sales of the inventory. An adjustment may be necessary for gross margins, where deemed significant.

The order of impairment testing for corporate assets and goodwill

IAS 36 specifies the order of testing in three circumstances:

Circumstances requiring guidance on order of testing	See the relevant section below
When a corporate asset cannot be allocated on a reasonable and consistent basis to the unit under review	Order of testing for corporate assets that cannot be allocated
When assets within a CGU to which goodwill has been allocated are tested for impairment at the same time as the unit	Order of testing for assets and cash generating units to which goodwill has been allocated
If a CGU making up a group of CGUs to which goodwill has been allocated is tested for impairment at the same time as the group of units	Order of testing for assets and cash generating units to which goodwill has been allocated

Order of testing for corporate assets that cannot be allocated

Our article ‘[Insights into IAS 36 – identifying cash generating units](#)’ discusses the process of allocating corporate assets to a CGU. If a portion of the carrying amount of a corporate asset can be allocated on a reasonable and consistent basis, the carrying amount of the CGU, including the portion of the carrying amount of the corporate asset allocated, is compared with its recoverable amount.

The assessment becomes more complex where a portion of the carrying amount of a corporate asset cannot be allocated on a reasonable and consistent basis to an individual CGU being tested. In this case, the entity should:

- first, compare the carrying amount of the unit, excluding the corporate asset, with its recoverable amount and recognise any impairment loss
- next, compare the carrying amount of the smallest group of CGUs under review to which a portion of the carrying amount of the corporate asset can be allocated on a reasonable and consistent basis and compare that amount with the recoverable amount of the group of units and recognise any impairment loss [see step 2 in the example below]. Any additional impairment loss calculated in this step should be recognised as follows:
 - first, to reduce the carrying amount of any goodwill allocated to the CGU (or groups of CGUs), and
 - next, to the other assets of the CGU (or groups of CGUs) pro rata based on the carrying amount of each asset in the CGU (or groups of CGUs), and
- when all or part of the corporate asset remains untested, the entity should test for impairment on an entity-wide basis and follow the same allocation process as outlined in bullet 2 above for any additional impairment calculated at this level.

The example below depicts the order of testing where the corporate asset cannot be allocated on a reasonable and consistent basis, other than on an entity-wide level.

Example 2 – Order of testing corporate assets that cannot be allocated on a reasonable and consistent basis

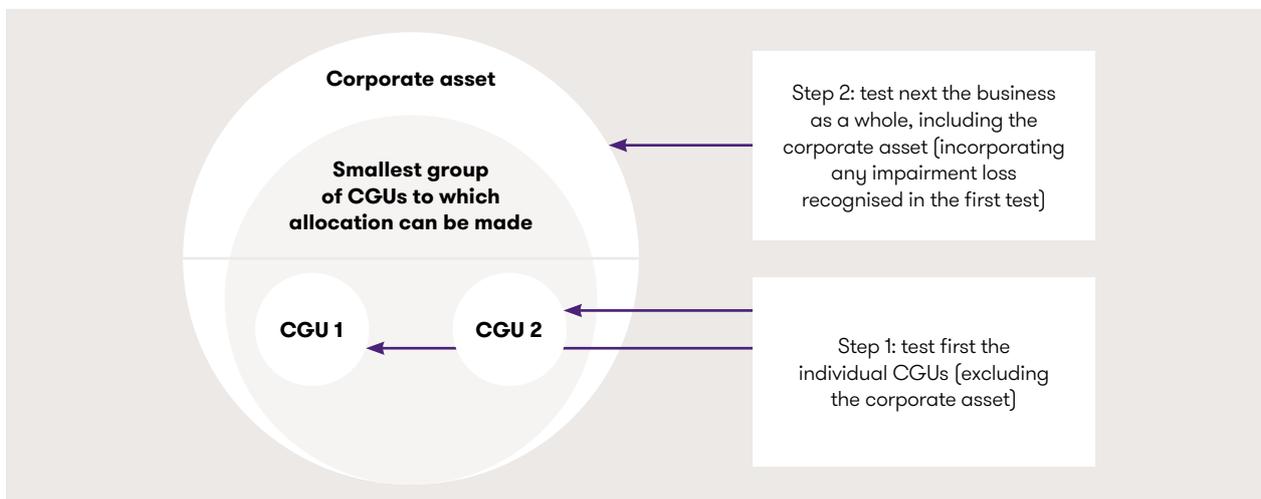
Entity A identifies two CGUs for impairment testing purposes. Entity A determines it cannot allocate its ‘brand’ asset to a CGU or group of CGUs on a reasonable and consistent basis.

Analysis

Entity A will first test the individual CGUs (CGU 1 and CGU 2) for impairment, excluding any allocation of the brand asset which cannot be allocated on a reasonable and consistent basis, and record any impairment loss if necessary.

Next, Entity A will compare the carrying amount of the entity as a whole with the recoverable amount of the group of units (including the brand). Any additional impairment loss arising from this step should be allocated:

- Step 1 – to reduce the carrying amount of any goodwill allocated to CGU 1, CGU 2 (or the group of CGUs) and
- Step 2 – on a pro rata basis to the other assets of CGU 1, CGU 2, and the brand corporate asset. However, the impairment loss does not reduce the carrying amount of any asset below the highest of:
 - its fair value less cost to sell
 - its value in use, and
 - zero.



Order of testing for assets and cash generating units to which goodwill has been allocated

If certain assets forming part of a CGU to which goodwill has been allocated are tested for impairment at the same time as the CGU, these assets are tested before the CGU as a whole is tested. This enables the entity to isolate any impairment at an individual asset level (if applicable) before proceeding to test at the CGU level. This requirement would apply only when the entity:

- is required to test the individual asset (eg because an impairment indicator has been identified), and
- it is possible to determine the asset's recoverable amount even though it is part of a CGU (eg an asset that does not generate largely independent cash flows but whose recoverable amount is estimated based on FVLCOB).

Similarly, if a group of CGUs to which goodwill has been allocated is tested for impairment at the same time as the individual CGUs, the individual CGUs are tested for impairment before the group of CGUs.

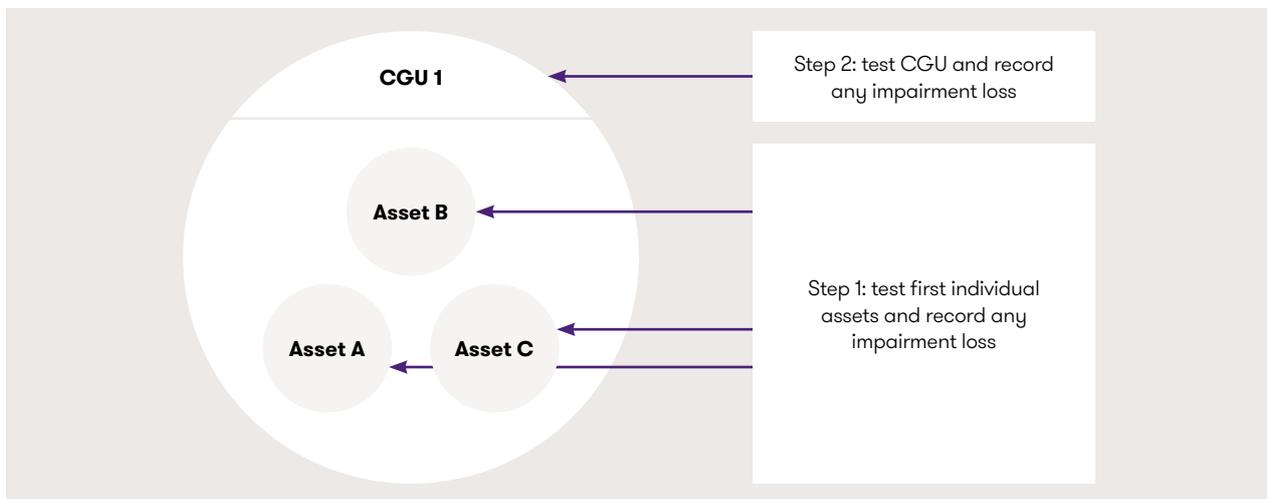
Not adhering to the prescribed order of testing in these particular cases will usually result in a different allocation of any impairment loss among the individual assets or CGUs. Step 6 discusses the allocation of impairment losses in more detail.

Example 3 – Order of testing for assets and CGUs to which goodwill has been allocated

Entity Z includes assets A, B, and C (among other assets) in CGU 1 for purposes of testing goodwill. Entity Z tests the goodwill for impairment annually at 30 June. At 30 June 20X0, management determines an impairment indicator necessitates the impairment testing of assets A, B and C.

Analysis

Entity Z first tests the individual assets (assuming their recoverable amount can be determined individually), recording any impairment loss(es) at the individual asset level. Next, Entity Z tests CGU 1 and records any remaining impairment loss (as outlined in 'Insights into IAS 36 – Recognising an impairment loss'). If any additional loss arises in this second step, it is first allocated to goodwill. Assets A, B and C are not reduced to less than their individual recoverable amounts.



How we can help

We hope you find the information in this article helpful in giving you some insight into IAS 36. If you would like to discuss any of the points raised, please speak to your usual Grant Thornton contact or visit www.grantthornton.global/locations to find your local member firm.



Insights into IAS 36

Recognising impairment losses

IAS 36 'Impairment of Assets' specifies the accounting for impairment reviews. There are some detailed requirements of IAS 36 that are complex and sometimes difficult to interpret and therefore are challenging to apply when preparing financial statements.

The articles in our 'Insights into IAS 36' series have been written to assist preparers of financial statements and those charged with the governance of reporting entities understand the requirements set out in IAS 36, and revisit some areas where confusion has been seen in practice.

Step 6 of applying the guidance in IAS 36 as set out in our article '[Insights into IAS 36 – Overview of the Standard](#)' and relates to recognising or reversing and impairment losses. This article focuses on part of this step; recognition of impairment losses. For reversing impairment losses refer to our article '[Insights into IAS 36 – Reversing impairment losses](#)'.



Step 6: Recognise or reverse any impairment loss

The requirements for recognising and measuring impairment losses differ based on the structure of the impairment testing as determined in Step 2, discussed in our article '[Insights into IAS 36 – Scope and structure of an impairment review](#)'. The requirements for recognising and measuring impairment losses for an individual asset (other than goodwill) are addressed in firstly below; and then the requirements for recognising and measuring impairment losses for cash-generating units (CGUs) and goodwill are addressed after that.

Recognising an impairment loss for an individual asset

When the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset needs to be reduced to its recoverable amount and that reduction is recognised as an impairment loss.

For assets accounted for using the revaluation model in IAS 16 'Property, Plant and Equipment' or IAS 38 'Intangible Assets', the impairment loss is treated in the same way as a downward revaluation in accordance with those standards. Accordingly any impairment is recognised in other comprehensive income to the extent it does not exceed a previous revaluation surplus. Any excess is recognised in profit or loss.

To the extent the amount estimated for an impairment loss exceeds the carrying amount of the asset to which it relates, an entity shall recognise a liability if, and only if, required by another standard.

Practical insight – Impairment loss exceeds the carrying amount of the asset to which it relates

An unallocated impairment loss for an individual asset (ie a loss exceeding the carrying amount of the asset in question) might arise if the asset is expected to generate negative net future cash flows – for example an asset that is nearing the end of its economic life and requires significant decommissioning or holding costs.

In such cases the value in use (VIU) estimate would be negative. In addition, the entity might need to pay potential buyers to acquire the asset in which case fair value less cost of disposal (FVLCD) would also be negative. In these cases, the entity would not reduce the carrying value of the asset to less than zero. The entity would look to IAS 37 'Provisions, Contingent Assets and Contingent Liabilities' to determine whether a provision for decommissioning costs must be recognised.

Finally, when an entity recognises an impairment loss for an individual asset, it must:

- adjust the future depreciation (amortisation) charge for the asset to allocate the asset's revised carrying amount, less its residual value (if any) on a systematic basis over its remaining useful life (see example 1 below), and
- determine any related deferred tax assets or liabilities in accordance with IAS 12 'Income Taxes' by comparing the revised carrying amount of the asset with its tax base (see example 2 below).

Example 1 – Adjusting future depreciation of an asset after recognising an impairment

A machine was purchased on 1 January 20X1 by Entity A for CU300,000 with an estimated useful life of 3 years and no residual value; therefore, CU100,000 of depreciation expense was recognised on a straight-line basis for both 20X1 and 20X2 (or CU8,333 per month). At 31 December 20X2, management determines an impairment indicator exists and estimates the recoverable amount of the machine to be CU80,000 (carrying amount at 31 December 20X2 is CU100,000).

Analysis

Entity A recognises an impairment loss for the difference (CU100,000-CU80,000 or CU20,000). In accordance with IAS 36, the entity also adjusts future depreciation of the machine after recording the impairment at 31 December 20X2 and will therefore recognise CU6,667 per month of depreciation from 1 January 20X3 – 31 December 20X3.

Example 2 – Determining any related deferred tax assets/liabilities after recognising an impairment

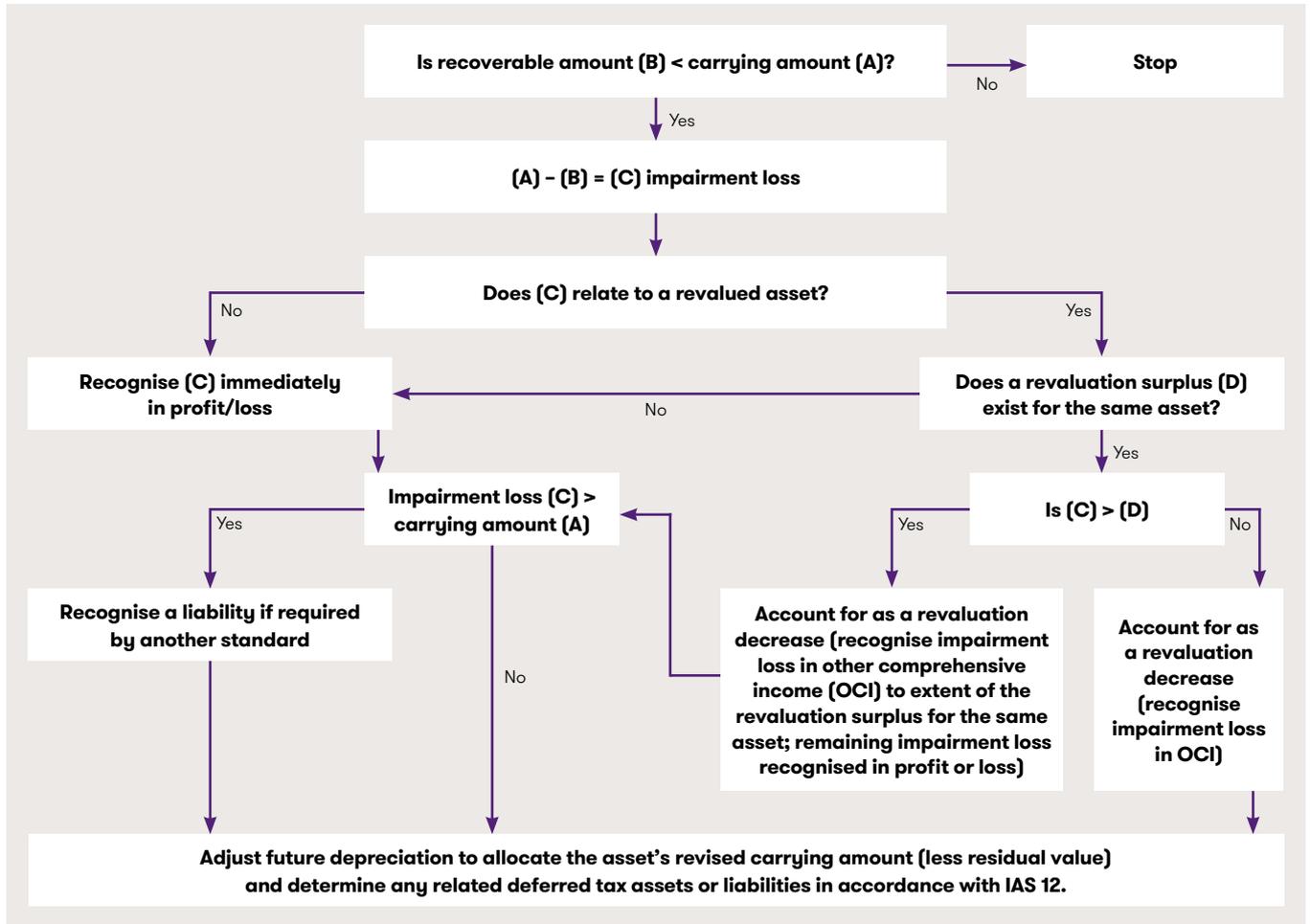
An entity owns a machine with a carrying amount of CU2,000. After finding evidence of an impairment indicator, management estimates the recoverable amount of the machine to be CU1,600. The entity records an impairment loss of CU400 (CU2,000 – CU1,600) for the machine. The tax rate is 35% and the tax base of the machine is CU1,800. Impairment losses are not deductible for tax purposes.

Analysis

The recognition of the impairment loss creates a deferred tax asset of CU70 as shown below, subject to meeting the criteria in IAS 12 'Income Taxes' for recognition of deferred tax assets.

	Before Impairment	Effect of Impairment	After Impairment
Carrying amount	2,000	(400)	1,600
Tax base	1,800	-	1,800
Taxable (deductible) temporary difference	200	(400)	(200)
Deferred tax liability (asset) at 35%	70	(140)	(70)

The below diagram summarises IAS 36's requirements for recording an impairment for an individual asset.



Recognising an impairment loss for CGUs

An impairment loss must be recognised for a CGU when the recoverable amount of the unit is less than its carrying amount. IAS 36 prescribes the impairment loss to be allocated:

- first, to reduce the carrying amount of any goodwill allocated to the CGU
- then, to the other assets of the unit, pro rata on the basis of the carrying amount of each asset in the unit.

However, in allocating the impairment loss, an entity cannot reduce the carrying amount of an individual asset below the highest of:

- its FVLCOB (if measurable)
- its VIU (if determinable), and
- zero.

These amounts serve as a 'floor' as outlined in the below diagram.

If, for an individual asset within an impaired CGU, it is possible to measure FVLCOB but not VIU (and therefore not possible to determine the individual asset's recoverable amount), then the floor is the higher of FVLCOB and zero. Under this scenario no impairment loss is recognised for the individual asset if the asset's CGU is not impaired, even if the asset's FVLCOB is less than its carrying amount.

Should the 'floor' be applicable for an asset; any amount that would have been allocated to the individual asset must be allocated pro rata to the other assets of the unit. The reductions in carrying amounts from applying the above requirements are treated as impairment losses on the individual assets and recognised as outlined above on page 2.

The following diagram demonstrates allocating an impairment loss to assets within a CGU:

1st	Reduce goodwill
2nd	Reduce other assets (as outlined on page 2) on a pro-rata basis using asset carrying amounts at the time the impairment testing is done, subject to the floor
Floor	No asset reduced below highest of its FVLCOB, VIU or zero

The below example illustrates the interaction of these requirements in allocating the impairment loss to individual assets comprising a CGU.

Example 3 – Allocating an impairment loss to assets within a CGU

Entity X carries out an impairment test of CGU 1 on 31 December 20X0. CGU 1 has a total carrying amount of CU800 and consists of two identifiable intangible assets (Asset A, CU400, and Asset B, CU300) in addition to allocated goodwill of CU100. Asset A was also tested for impairment at 31 December 20X0 and found not to be impaired because its FVLCOB (CU450) exceeds its carrying amount (CU400). Management has concluded Asset B's VIU cannot be determined individually and its FVLCOB cannot be measured reliably. The results of the impairment test of CGU 1 show a recoverable amount of CU500; as such, an impairment loss of CU300 must be recognised.

CGU 1	Carrying amount	Recoverable amount (individual asset level)	Impairment loss allocation
Goodwill	100	N/A	100
Asset A	400	450	-
Asset B	300	N/A	200
Total	800		
Recoverable amount of CGU 1	500		
Impairment loss	300		300

Analysis

Entity X first allocates the impairment loss to goodwill. Next, Entity X allocates the remaining impairment loss (in this case CU200) to the individual assets comprising the CGU, subject to the floor. No impairment loss can be allocated to Asset A (due to the floor) as the asset cannot be reduced to less than its recoverable amount. Therefore, the remaining impairment loss of CU200 is allocated to Asset B.

Example 4 – Understanding if the recoverable amount can be determined for individual assets and the effect on recognising an impairment

A machine has suffered physical damage but is still working, although not as well as before it was damaged. The machine's FVLCOB is less than its carrying amount. The machine does not generate independent cash inflows.

The smallest identifiable group of assets that includes the machine and generates cash inflows are largely independent of the cash inflows from other assets, is the production line to which the machine belongs. The recoverable amount of the production line shows the production line (taken as a whole) is not impaired.

Scenario 1: budgets/forecasts approved by management reflect no commitment of management to replace the machine.

Scenario 2: budgets/forecasts approved by management reflect a commitment to replace the machine and sell it in the near future. Cash flows from continuing to use the machine until its disposal are estimated to be negligible.

Analysis – Scenario 1

The recoverable amount of the machine alone cannot be estimated because the machine's VIU:

- may differ from its FVLCOB, and
- can be determined only for the CGU to which the machine belongs (the production line).

The production line is not impaired. Therefore, no impairment loss is recognised for the machine. Nevertheless, the entity may need to reassess the depreciation period or the depreciation method for the machine.

Analysis – Scenario 2

The machine's VIU can be estimated to be close to its FVLCOB. Therefore, the recoverable amount of the machine can be determined. Because the machine's FVLCOB is less than its carrying amount, an impairment loss is recognised for the machine.

Remaining (unallocated) amount of an impairment loss for a CGU

When the requirements above have been applied and result in a remaining unallocated amount of impairment loss for a CGU, such an amount is only recognised as a liability if required by another IFRS.

Practical insight – Any remaining (unallocated) amount of an impairment loss for a CGU

This situation might arise for example, in relation to a loss-making CGU that is in need of restructuring. As noted in our article '[Insights into IAS 36 – Value in use: estimating future cash inflows and outflows](#)', the effects of a future restructuring would be excluded from the VIU estimate before the entity has an obligation for the restructuring in accordance with IAS 37. Also, the need for future restructuring may result in FVLCOB being negative. In this situation the entity would limit any impairment loss to the carrying value of the CGU's assets and separately evaluate whether the criteria in IAS 37 to recognise a restructuring provision have been met.

Considerations for foreign operations

Any impairment loss is not a partial disposal for the purposes of IAS 21 'The Effects of Changes in Foreign Exchange Rates'. The foreign exchange gain or loss recognised in other comprehensive income on translating the foreign operation's financial statements is not therefore reclassified to profit or loss when recognising an impairment.

How we can help

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Insights into IAS 36

Reversing impairment losses

IAS 36 'Impairment of Assets' sets out the requirements to follow prior to concluding if and when an asset should be impaired. However, due to the complex nature of the Standard, the requirements of IAS 36 can be challenging to apply in practice.

The articles in our 'Insights into IAS 36' series have been written to assist preparers of financial statements and those charged with the governance of reporting entities understand the requirements set out in IAS 36, and revisit some areas where confusion has been seen in practice.

Step 6 of applying the guidance in IAS 36 as set out in our article '**Insights into IAS 36 – Overview of the Standard**' relates to recognising or reversing and impairment losses. This article focuses on part of this step; reversing impairment losses. For recognising impairment losses refer to our article '**Insights into IAS 36 – Recognising impairment losses**'.



Indicators for reversing an impairment loss

In addition to assessing evidence of possible impairment, entities must also assess whether there is any indication a previously recognised impairment loss for an asset (other than goodwill) no longer exists or the assessed impairment amount may have decreased. If an indication of possible reversal is identified, the entity must estimate the recoverable amount of that asset.

Guidance note: Goodwill impairment cannot be reversed

IAS 36 prohibits any reversal of impairment losses recognised on goodwill. The reason for this is because IAS 36 views any increase in the recoverable amount of goodwill after the recognition of an impairment loss to likely be an increase in the internally generated goodwill (not a reversal of the impairment loss recognised for the acquired goodwill). IAS 38 'Intangible Assets' prohibits the recognition of internally generated goodwill.

Accordingly, the references to impairment reversals in this article do not include goodwill.

Similar to the list provided in IAS 36 indicating when there might be an impairment loss, the Standard also provides a non-exhaustive list of circumstances when a previously recognised impairment loss may no longer exist. These are summarised below.

Non-exhaustive list of impairment reversal indicators from IAS 36

External sources of information	<ul style="list-style-type: none">• Observable indications that the asset's value has increased significantly during the period• Significant favourable changes (have occurred or are expected) in the technological, market, economic or legal environment• Market interest rates or other market rates of return on investments have decreased during the period (which will decrease the discount rate used in calculating the asset's value in use (VIU))
Internal sources of information	<ul style="list-style-type: none">• Significant favourable changes (have occurred or are expected) in the extent to which an asset is used (or is expected to be used) (eg, costs incurred during the period to improve or enhance the asset's performance or restructure the operation to which the asset belongs)• Evidence is available from internal reporting that indicates the economic performance of an asset is, or will be, better than expected.

The reversal of an impairment loss reflects an increase in the estimated service potential of an asset (either from use or from sale) since the date when an entity last recognised the impairment loss for the asset. A reversal of an impairment loss should therefore only be recognised if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. Said differently, an impairment loss is not reversed solely because of the passage of time or the unwinding of the discount, even if the recoverable amount of the asset becomes higher than its carrying amount.

Guidance note: Disclosure required for an increase in the estimated service potential

The Standard requires the entity to identify and disclose the change in estimates that cause the increase in the estimated service potential. Examples include:

- a change in the basis for measuring recoverable amount (ie whether recoverable amount is based on fair value less costs of disposal (FVLCO) or VIU)
- where the recoverable amount was based on VIU, a change in the amount or timing of estimated future cash flows or in the discount rate, or
- where the recoverable amount was based on FVLCO, and there has been a change in the previously estimated components of the FVLCO amount reflected in the financial statements.

Regardless of whether an impairment loss is reversed for an asset, if the entity identifies an indication a previously recognised impairment loss may no longer exist, the entity may need to review and adjust the:

- the remaining useful life
- the depreciation (amortisation method), and/or
- the residual value of the asset.

Practical insight – Indicators for reversing a previously recognised impairment loss

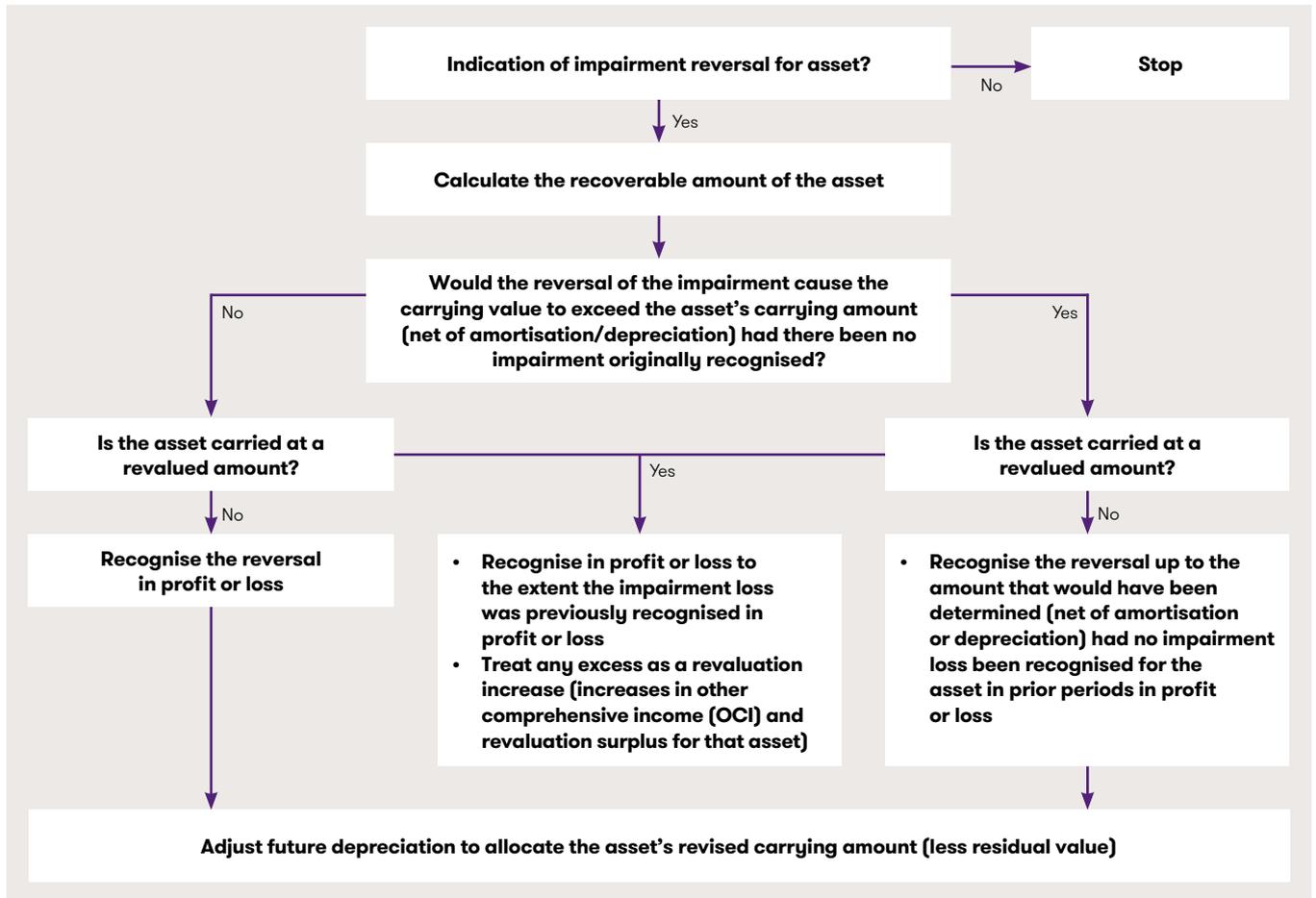
Most of the ‘reversal indicators’ listed are the inverse of the loss indicators listed in IAS 36 (discussed in ‘**Insights into IAS 36 – If and when to test for impairment**’); there are however some exceptions to this. In particular, an increase in market capitalisation above carrying value of an entity’s net assets is not listed as a reversal indicator.

Reversing impairment losses for individual assets (other than goodwill)

When recoverable amount is recalculated and exceeds the asset’s carrying value, the carrying amount is increased to the recoverable amount subject to a ‘ceiling’ (ie an upper limit). The increased carrying amount cannot exceed the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years.

For assets accounted for using the revaluation model in IAS 16 ‘Property, Plant and Equipment’ or IAS 38, the reversal of the impairment loss is accounted for in the same way as a revaluation increase in accordance with those standards.

The diagram below depicts the requirements for reversals of impairment losses for individual assets and the following example illustrates their practical application.



Example 1 – Reversing a previously recognised impairment loss for an individual asset

At 1 January 20X1, Entity T purchased an item of PP&E (a machine) for CU1,800 (Entity T will depreciate the machine on a straight-line basis over its useful life of 15 years). In 20X1, Entity T recognised an impairment loss of CU500 on this machine, having identified indicators showing a reduction in expected demand for the machine output due to the introduction of a superior product released by a competitor. Entity T applies the cost model in accordance with IAS 16 and the impairment loss was recognised in profit or loss. The amounts before and after the recognition of the impairment loss were as follows with respect to the machine:

31 December 20X1	Machine
Historical cost	1,800
Accumulated depreciation	(120)
Carrying amount	1,680
Impairment loss	(500)
Carrying amount after impairment loss	1,180

In 20X3, Entity T determines the competitor product is experiencing technical issues and that its effect on demand for Entity T's output is less than expected. Sales have exceeded forecast and management estimates production will increase by 25%. At 31 December 20X3, Entity T estimates the recoverable amount of the machine in accordance with IAS 36. The recoverable amount of the machine is estimated to be CU1,300.

31 December 20X3	Machine
31 December 20X1 carrying amount after impairment loss	1,180
Accumulated depreciation (20X2 and 20X3)	(168)
Carrying amount	1,012
Recoverable amount	1,300
Excess of recoverable amount over carrying amount	288

* Entity T revised the depreciation charge (from CU120 per year to CU84 per year) for the machine based on the revised carrying amount and remaining useful life at 31 December 20X1 (CU1,180/14 years or CU84 depreciation expense per year). Depreciated historical cost of the machine at 31 December 20X3 is as follows:

31 December 20X1	Machine
Historical cost	1,800
Accumulated depreciation (CU120 X 3)	(360)
Depreciated historical cost	1,440
Carrying amount	1,012
Carrying amount after impairment loss	428

Analysis

Entity T recognises a reversal of the impairment loss recognised in 20X1 in accordance with IAS 36. Entity T increases the carrying amount of the machine by CU316 (to lower of recoverable amount (CU1,300) and the depreciated historical cost (CU1,440)). The increase is recognised immediately in profit or loss and Entity T will again adjust future depreciation to allocate the asset's revised carrying amount.

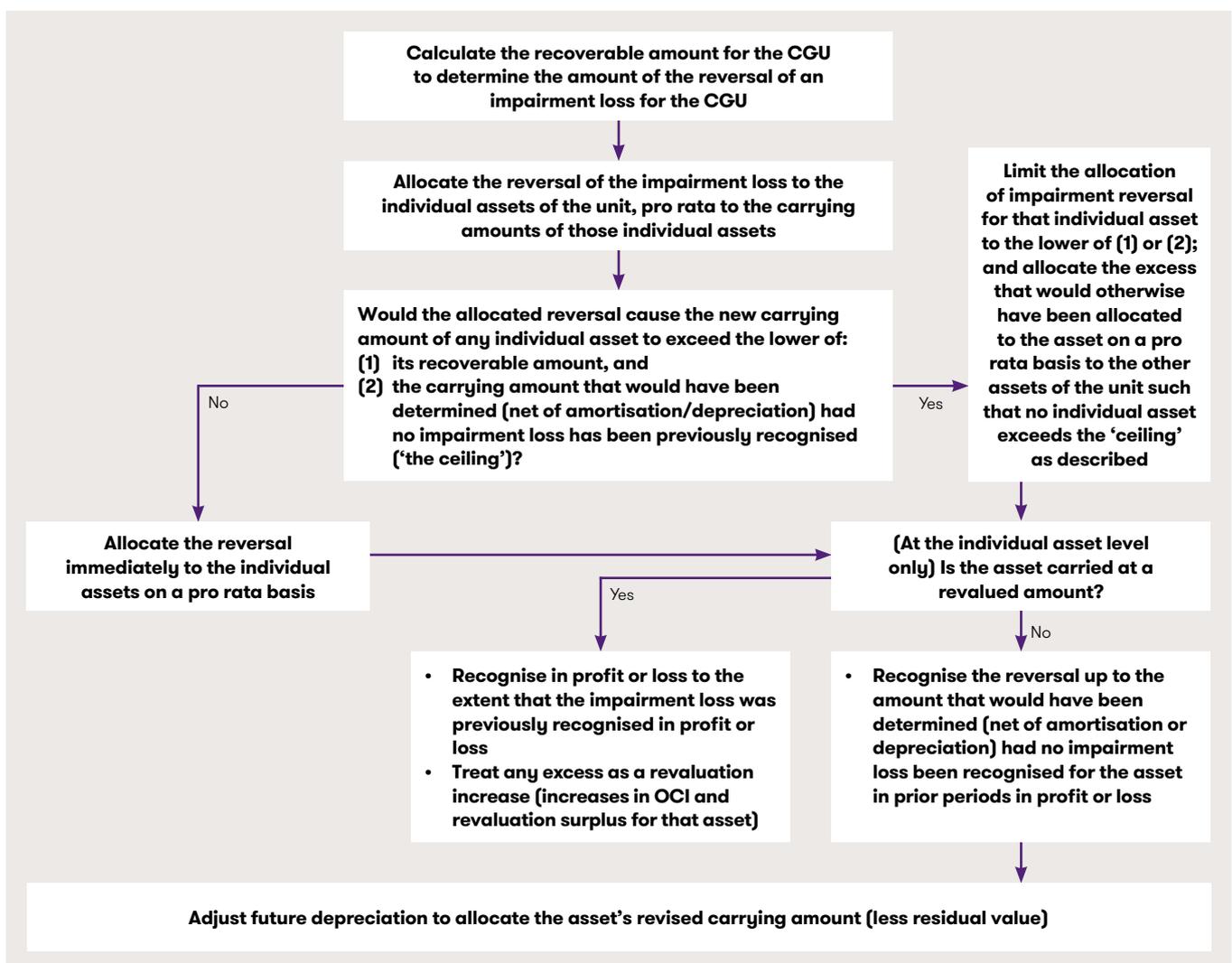
Reversing impairment losses for cash-generating units

Any reversal of an impairment loss for a cash-generating unit (CGU) must be allocated to the individual assets that make up the CGU (excluding goodwill). The entity is required to allocate the reversal of an impairment loss to the CGU's assets pro rata to their carrying amounts. This is again however subject to a 'ceiling' whereby no individual asset's carrying amount is increased above the lower of:

- its recoverable amount (if determinable), and
- its carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior periods.

If this 'ceiling' takes effect for one or more of the CGU's assets, the reversal of the impairment loss that would otherwise have been allocated to those assets is allocated on a pro rata basis to the other assets, subject to the same ceiling.

The below flowchart depicts the allocation process.



The following example illustrates the practical application of these requirements.

Example 2 - Reversing a previously recognised impairment loss for a CGU with allocated goodwill

Entity T is in the healthcare industry and has identified three CGUs for impairment review purposes (CGU 1, CGU 2 and CGU 3), each located in a different country. In 20X1, Entity T recognised an impairment loss of CU1,250 with respect to CGU 1, following the election of a new government in the country in which CGU 1 operates and anticipated changes in healthcare laws that would reduce demand for Entity T's products. The amounts before and after the recognition of the impairment loss were as follows with respect to CGU 1:

31 December 20X1	Goodwill	CGU 1 identifiable assets	Total
Historical cost	750	1,800	2,550
Accumulated depreciation (20X1)	-	(120)	(120)
Carrying amount	750	1,680	2,430
Impairment loss	(750)	(500)	(1,250)
Carrying amount after impairment loss	-	1,180	1,180

In 20X3 Entity T determines the impact of the new healthcare laws is less than expected. Sales have exceeded forecast and management estimates production will increase by 25%. At 31 December 20X3, Entity T estimates the recoverable amount of CGU 1 in accordance with IAS 36. The recoverable amount of CGU 1 is estimated to be CU1,500. It is not possible to determine recoverable amount for any of the individual assets in the CGU.

31 December 20X3	Goodwill	CGU 1 identifiable assets	Total
31 December 20X1	-	1,180	1,180
Accumulated depreciation (20X2 and 20X3)	-	(168)	(168)
Carrying amount	-	1,012	1,012
Recoverable amount			1,500
Excess of recoverable amount over carrying amount			488

* Entity T revised the depreciation charge (from CU120 per year to CU84 per year) for the identifiable assets of CGU 1 based on the revised carrying amount and remaining useful life at 31 December 20X1. Depreciated historical cost of CGU 1 at 31 December 20X3 is as follows:

31 December 20X3	CGU 1 identifiable assets
Historical cost	1,800
Accumulated depreciation (CU120 X 3)	(360)
Depreciated historical cost	1,440
Carrying amount	1,012
Difference	428

Analysis

At 31 December 20X3, Entity T recognises a reversal of the impairment loss (recognised at 31 December 20X1) in accordance with IAS 36. Entity T will increase the carrying amount of CGU 1's identifiable assets by CU428 (to the lower of recoverable amount (CU1,500) and the depreciated historical cost of the non-goodwill assets (CU1,440) had no impairment loss been recognised in prior periods). The increase is recognised immediately in profit or loss. The impairment loss recognised for goodwill in 20X1 is not reversed.

How we can help

We hope you find the information in this article helpful in giving you some insight into IAS 36. If you would like to discuss any of the points raised, please speak to your usual Grant Thornton contact or visit www.grantthornton.global/locations to find your local member firm.

