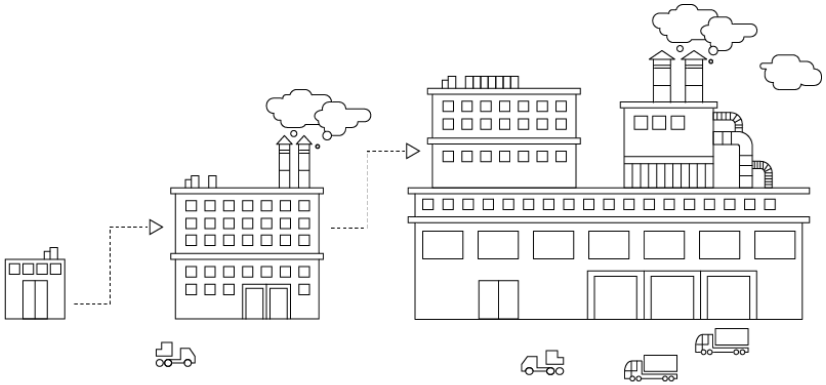
IAS 36 IMPAIRMENT OF ASSETS

Assurance updates – 12/2019

Objective

The objective of IAS 36 Impairment of assets is to make sure that entity's assets are carried at no more than their recoverable amount.

The Standard also defines when an asset is impaired, how to recognize an impairment loss, when an entity should reverse this loss and what information related to impairment should be disclosed in the financial statements.



Scope of application

IAS 36 IMPAIRMENT OF ASSETS

xxx DOES NOT apply to

x Inventories (IAS 2)
x Financial assets (IFRS 9)
x Deferred tax asset (IAS 12)
x Employee benefits (IAS 19)
x Construction contract (IAS 11)
x Investment property at FV (IAS 40)
x Agricultural asset at FV (IAS 41)
x Insurance contract (IFRS 4)
x Non-current assets held for sale (IFRS 5)

✓✓✓ DOES apply to

✓ Land, building, machinery (IAS 16)
✓ Investment property at cost (IAS 40)
✓ Intangible assets (IAS 38)
✓ Goodwill
✓ Subsidiary, associate, joint venture at cost
✓ Assets at revalued amounts

What is an impairment of assets?

ASSET IS IMPAIRED WHEN

Carrying amount
(accounting record)

>

Recoverable amount
(fair value – cost of disposal or value in use)

IDENTIFYING AN ASSET MAY BE IMPAIRED

Following procedures are needed to perform to be compliant with IAS 36

Assess whether there is any indication that an asset might be impaired at the end of each reporting period. No need to perform impairment testing if there's no indication

Intangible asset with an indefinite useful life (such as trademarks) or intangible asset not yet available for use need to be tested for impairment annually

Goodwill acquired in a business combination is needed to test for impairment annually

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Indication of impairment

External indicator

- The asset's value has declined during the period significantly more than would be expected as a result of the passage of time or normal use
- Significant changes with an adverse effect on the entity in the technological, market, economic or legal environment in which the entity operates or in the market to which an asset is dedicated
- Market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect the discount rate used in calculating an asset's value in use and decrease the asset's recoverable amount materially
- The carrying amount of the net assets of the entity is higher than its market capitalization

Internal indicator

- Obsolescence or physical damage of an asset
- Significant changes with an adverse effect on the entity related to the use of an asset, for example: an asset becoming idle, plans to discontinue or restructure the operation to which an asset belongs, plans to dispose of an asset before the previously expected date, and reassessing the useful life of an asset as finite rather than indefinite
- Evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected

Standard also outlines the indications related to subsidiaries, associates and joint ventures.

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Measuring recoverable amount (RA)

RECOVERABLE AMOUNT

Higher of asset's/CGU's

Fair value less cost of disposal

Value in use

When an individual asset does not generate cash inflows that are largely independent of those from other assets (or groups of assets), then determine recoverable amount for the cash-generating unit (CGU) to which this asset belongs.

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Measuring RA

Fair value less cost of disposal

- Rules and guidelines for measuring the fair value of any assets are set by the standard IFRS 13: Fair Value Measurement
- Costs of disposal are for example legal costs, stamp duties and similar transaction taxes, costs of removing the asset and direct incremental costs to bring an asset into condition for its sale

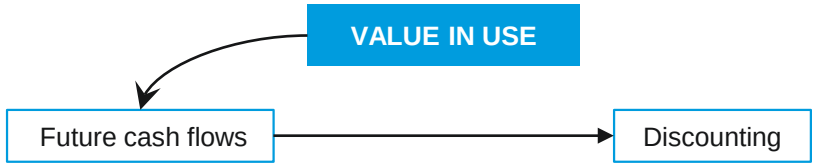
Value in use

Value in use is the present value of the future cash flows expected to be derived from an asset or cash-generating unit. In order to determine value in use, take the following elements into account:

- An estimate of the future cash flows the entity expects to derive from the asset
- Expectations about possible variations in the amount or timing of those future cash flows
- The time value of money, represented by the current market risk-free rate of interest
- The price for bearing the uncertainty inherent in the asset
- Other factors, such as illiquidity, that market participants would reflect in pricing the future cash flows the entity expects to derive from the asset

Year	Expected Future cash flows	Discount factor	Present value
1	10,000	0.909	9,090
2	12,000	0.826	9,912
3	15,000	0.751	11,265
4	9,000	0.683	6,147
5	5,000	0.621	3,105
Total	51,000		39,519

Value in use



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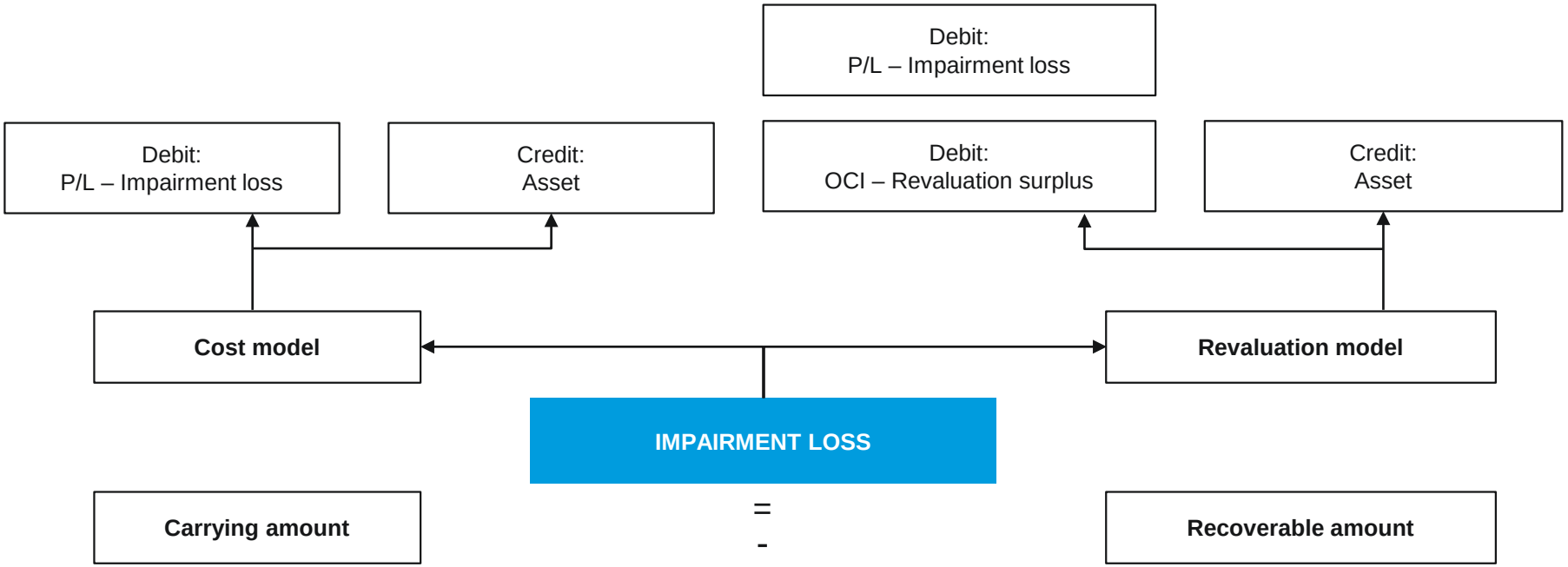
Recognize and measure impairment loss

If the asset's recoverable amount is lower than it's carrying amount, then an entity must recognize an impairment loss as a difference between these 2 amounts.

An impairment loss shall be recognized to profit or loss or as a revaluation decrease if the asset is carried at revalued amount in line with other IFRS.



Recognize and measure impairment loss – Example

Question:

ABC Co purchased a machine worth 90,000,000 on 01/01/20X1. The machine is depreciated on a straight-line method over its useful life of 3 years. The recoverable amount through years are as below:

- 31/12/20X1: 120,000,000
- 31/12/20X2: 20,000,000
- 31/12/20X3: 0

Calculate the machine value presented in Financial Statement at the end of each year using cost model and revaluation model. The financial year of ABC Co is from 01/01 to 31/12. Assume opening balance of PPE is nil and the residual value of machine is also nil after its useful life. ABC Co continue to use the machine after fully depreciation.

- CA: Carrying amount RA: Recoverable amount

Cost model	**Revaluation model**
For the year ended 31/12/20X1: • Opening CA 90,000,000 • Depreciation charge (30,000,000) • Ending CA 60,000,000 • RA (given) 120,000,000 Ending CA is lower than RA so there is no impairment loss as at 31/12/20X1 and due to cost model is applied, the CA of machine will not be adjusted upward to RA. Therefore the machine value presented in Financial Statement as at 31/12/20X1 is 60,000,000.	For the year ended 31/12/20X1: • Opening CA 90,000,000 • Depreciation charge (30,000,000) • Ending CA 60,000,000 • RA (given) 120,000,000 • Revaluation surplus: 60,000,000 Ending CA is lower than RA so there is no impairment loss as at 31/12/20X1 and due to revaluation model is applied, the CA of machine will be adjusted upward to RA and the revaluation increase of 60,000,000 will be recorded in revaluation surplus (part of Equity). Therefore the machine value presented in Financial Statement as at 31/12/20X1 is 120,000,000 and the revaluation surplus is 60,000,000.

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Recognize and measure impairment loss – Example

Cost model	Revaluation model
For the year ended 31/12/20X2: • Opening CA 60,000,000 • Depreciation charge (30,000,000) • Ending CA 30,000,000 • RA (given) 20,000,000 Ending CA is higher than RA so there is impairment loss as at 31/12/20X2. The impairment loss will be recorded in Profit or loss and the machine value will be written down to 20,000,000. Therefore the machine value presented in Financial Statement as at 31/12/20X2 is 20,000,000.	For the year ended 31/12/20X2: • Opening CA 120,000,000 • Depreciation charge (60,000,000) • Ending CA 60,000,000 • RA (given) 20,000,000 • Revaluation surplus 20,000,000 Ending CA is higher than RA so there is impairment loss as at 31/12/20X2. The impairment loss of 40,000,000 will be deducted in revaluation surplus and the machine value will be written down to 20,000,000. Therefore the machine value presented in Financial Statement as at 31/12/20X2 is 20,000,000 and the revaluation surplus is 20,000,000.
For the year ended 31/12/20X3: • Opening CA (after adjusted): 20,000,000 • Depreciation charge (20,000,000) • Ending CA 0 • RA (given) 0 Ending CA is equal to RA after machine's useful life and equal to zero. Therefore the machine value presented in Financial Statement as at 31/12/20X3 is 0.	For the year ended 31/12/20X3: • Opening CA 20,000,000 • Depreciation charge (20,000,000) • Ending CA 0 • RA (given) 0 • Revaluation surplus 20,000,000 Ending CA is equal to RA after machine's useful life and equal to zero. Therefore the machine value presented in Financial Statement as at 31/12/20X3 is 0 and the revaluation surplus is 20,000,000.

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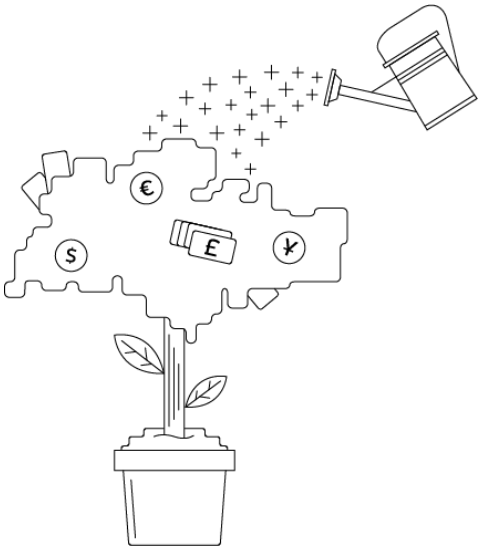
Cash-generating units

A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

If it is unable to determine recoverable amount for an individual asset, then establish cash-generating unit to which this asset belongs.

For example, if it is unable to set the fair value less costs of disposal for used 5 years-old pizza oven as the quotes might not be available. At the same time, it is unable to calculate pizza oven's value in use because future cash inflows from pizza oven cannot be estimated – this pizza oven does not generate any cash inflows itself. Therefore a cash-generating unit for this pizza oven has to be established – it would probably be the whole pizzeria.

In determining cash-generating unit, it is needed to be consistent from period to period to include the same asset or type of assets.

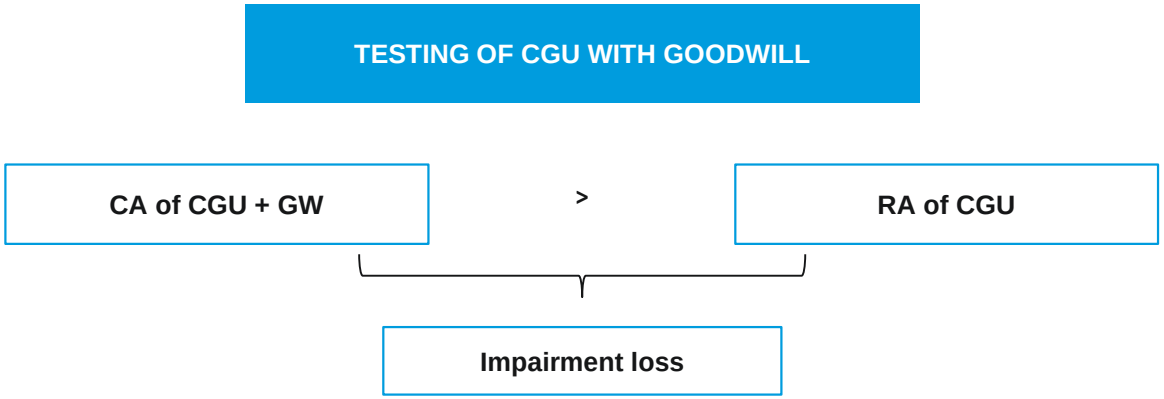


Goodwill

If there is a goodwill acquired in a business combination, then it must be allocated to each of the acquirer's cash-generating units (or group of them) that are expected to benefit from the synergies of the combination.

Goodwill should be tested for impairment on an annual basis. In this case testing means to compare:

- The carrying amount of CGU including the goodwill
- The recoverable amount of that CGU



Impairment loss of CGU

If the recoverable amount of CGU is lower than it's carrying amount, then an entity shall recognize the impairment loss.

The impairment loss shall be allocated to reduce the carrying amount of the assets of the unit in the following order:

- Reduce the carrying amount of any goodwill allocated to the CGU
- Allocate remaining impairment loss to the other assets of the unit on the pro rata basis of the carrying amount of each asset in the unit. These reductions are recognized as impairment losses on individual assets

In allocating an impairment loss, do not reduce the carrying amount of an asset below the highest of:

- Its fair value less cost of disposal (FV – CoD)
- Its value in use
- Zero

Question:
The following information is extracted from the Statement of Financial Position at reporting day of a cash-generating unit (CGU):

• Building	30,000,000
• Intangible asset	12,000,000
• Equipment	9,000,000
• Goodwill	10,000,000

Following a recession, an impairment test has been carried out and the CGU now has a fair value of 39,000,000. The related disposal cost is 3,000,000. The estimated present value of the cash flow from the continue use is 42,000,000. The building has a fair value less cost of disposal (FV – CoD) of 27,000,000.

Calculate and allocate the impairment loss (rounded to the nearest 100,000).

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Impairment loss of CGU - Example

Answer:

Step 1: Recoverable amount measurement

Recoverable amount is the higher of a CGU's fair value less costs of disposal and its value in use.

- Fair value less cost of disposal (39,000,000 – 3,000,000): 36,000,000
- Value in use (given): 42,000,000

Therefore the recoverable amount is 42,000,000.

Step 2: Calculate impairment loss

An asset is impaired when it's carrying amount exceeds its recoverable amount.

- Carrying amount (CA) [(30 + 12 + 9 + 10) x 1,000,000]: 61,000,000
- Recoverable amount (RA): 42,000,000

The carrying amount is higher than its recoverable amount so the CGU has been impaired.

Impairment loss (IL) (42,000,000 – 61,000,000) (19,000,000)

Step 3: Impairment loss allocation

	CV	IL	RA	Working
Building	30,000,000	(3,000,000)	27,000,000	[2]
Intangible asset	12,000,000	(3,400,000)	8,600,000	[2]
Plant & Equipment	9,000,000	(2,600,000)	6,400,000	[2]
Goodwill	10,000,000	(10,000,000)	0	[1]
Total	61,000,000	19,000,000	42,000,000	

The impairment loss has been calculated and allocated as above.

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Impairment loss of CGU – Example

Working [1]: Allocate impairment loss for goodwill

As mentioned above, goodwill will be prioritized to reduce the carrying amount when the CGU is impaired. The impairment loss of the CGU will be allocated to goodwill until goodwill reaches zero (because goodwill does not have fair value less cost of disposal and value in use).

The impairment loss calculated in this example is 19,000,000, goodwill is given 10,000,000. Therefore an amount of impairment loss of 10,000,000 will be deducted in goodwill and goodwill will be nil after the impairment loss allocation.

Working [2]: Allocate impairment loss for remaining assets

If remaining impairment loss is allocated to building, intangible asset and equipment on a pro rata basis, it is as below:

- Remaining impairment loss (19,000,000 – 10,000,000): 9,000,000
- Remaining carrying amount (61,000,000 – 10,000,000): 51,000,000
- IL (building) [9,000,000 x (30,000,000/51,000,000)]: 5,300,000
- IL (intangible asset) [9,000,000 x (12,000,000/51,000,000)]: 2,100,000
- IL (plant & equipment) [9,000,000 x (9,000,000/51,000,000)]: 1,600,000

At that time, the recoverable amount of building will be 30,000,000 – 5,300,000 = 24,700,000, lower than the (FV – CoD) of building (given) of 27,000,000. But as mentioned above, in allocating an impairment loss, do not reduce the carrying amount of an asset below the highest of (FV – CoD), value in use and zero. Therefore the recoverable amount of building will be the (FV – CoD) of 27,000,000 which is given. As a result, the impairment loss allocated to building will be 3,000,000 (30,000,000 – 27,000,000).

Remaining impairment loss is allocated to intangible asset and equipment on a pro rata basis as below:

- Remaining impairment loss (19,000,000 – 13,000,000): 6,000,000
- Remaining carrying amount (61,000,000 – 40,000,000): 21,000,000
- IL (intangible asset) [6,000,000 x (12,000,000/21,000,000)]: 3,400,000
- IL (plant & equipment) [6,000,000 x (9,000,000/21,000,000)]: 2,600,000

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Reversal of impairment loss

For individual asset

An impairment loss can be reversed only when there is a change in the estimates used to determine the asset's recoverable amount. It means that the impairment loss cannot be reversed due to passage of time or unwinding the discount.

Reversal of an impairment loss is recognized in the profit or loss unless it relates to a revalued asset. The increased carrying amount due to reversal should not be more than what the depreciated historical cost would have been if the impairment had not been recognized.

Remember to adjust the depreciation for future periods to reflect revised carrying amount.

For a cash-generating unit

When reversing an impairment loss for a cash-generating unit, it is needed to allocate reversal to the assets of the unit (except for goodwill) on a pro rata basis with the carrying amounts of these assets.

The carrying amount of an asset shall not be increased above the lower of:

- Its recoverable amount
- The carrying amount that would have been determined (net of amortization or depreciation) without any prior impairment loss

For goodwill

Reversal of an impairment loss for goodwill is prohibited.

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Reversal of impairment loss – Example

Question:

At 01/01/20X1, a head office building with a carrying amount (CA) of 30 billion is estimated to have a recoverable amount (RA) of 25 billion due to falling property values in the area. An impairment loss of 5 billion has been recognized.

At 01/01/20X6, five years later, property prices in the area have arisen, and the recoverable amount of the building increases to 23 billion. The building is depreciated on a straight-line method over its remaining useful life of 20 years from date of impairment measurement and the useful life will not be changed after all of the events above. The building is measured by cost model.

Answer:

The historical carrying amount would have been if the impairment had not been recognized (at 01/01/20X6):

30 – (30/20 x 5) = 22.50 (billion)

The actual carrying amount at 01/01/20X6 (impacted by impairment loss):

25 – (25/20 x 5) = 18.75 (billion)

Recoverable amount at 01/01/20X6 (given) is 23 billion.

Recoverable amount is higher than actual carrying amount so a reversal of impairment loss will be made. But in accordance with IAS 36, the increased carrying amount due to reversal should not be more than what the historical carrying amount would have been if the impairment had not been recognized.

- RA – actual CA (23 – 18.75): 4.25
- Historical CA – actual CA (22.50 – 18.75): 3.75

Therefore the reversal of impairment loss is 3.75 billion and the building is written back to 22.5 billion.

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Conclusion

This Standard issued to prescribe the procedures that an entity applies to ensure that its assets are carried at no more than their recoverable amount. An asset is carried at more than its recoverable amount if it's carrying amount exceeds the amount to be recovered through use or sale of the asset. If this is the case, the asset is described as impaired and the Standard requires the entity to recognize an impairment loss. The Standard also specifies when an entity should reverse an impairment loss and prescribes disclosures.

Vietnam has not had an Accounting Standard, regulations or guidelines that define basic accounting concepts for impairment loss testing. According to "Road map to IFRSs adoption in Vietnam", we are in the process of preparing for the application of International Financial Reporting Standards (IFRS). Hoping that in a near future, laws and regulations of accounting field in Vietnam will be amended to approach the international standards, making everything more transparence and comparable, hence increase competitiveness of economy.

CONTACT US

Ho Chi Minh City

Dang Xuan Canh
Managing Partner
Head of Audit Services
T: +84 28 3827 5026
E: canh.dang@rsm.com.vn

5th Floor, Sai Gon 3 Building
140 Nguyen Van Thu Street
Da Kao Ward, District 1
Ho Chi Minh City, Vietnam

Hanoi

Nguyen Thanh Lam
Partner
Head of Hanoi Office
T: +84 24 3795 5353
E: lam.nguyen@rsm.com.vn

25 Floor, Tower A, Discovery Complex
302 Cau Giay Street, Dich Vong Ward
Cau Giay District
Hanoi, Vietnam

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