



QAO Guidelines on Accounting Standard AASB 136

Impairment of Assets

July 2004

Disclaimer

This publication is a guide based on information available as at July 2004 and is not a substitute for the Standards, exposure drafts, AASB and IASB Standards. Users of this publication should be aware that the requirements of IFRS could change over time. For further information, please refer to the AASB website.

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INDEX

PURPOSE	1
INTRODUCTION	1
OBJECTIVE OF AASB 136	1
APPLICATION TO PUBLIC SECTOR ENTITIES	1
TRANSITION AND FIRST TIME APPLICATION	2
SCOPE	2
IDENTIFICATION OF IMPAIRED ASSETS	2
IMPACT OF ASSESSMENT FOR IMPAIRMENT	3
OTHER IMPACTS	4
ESTIMATION OF FUTURE CASH FLOWS IN DETERMINING VALUE IN USE	6
IDENTIFICATION OF CASH-GENERATING UNITS	7
RECOGNITION OF IMPAIRMENT LOSSES	9
RECOGNISING IMPAIRMENT LOSSES FOR CASH-GENERATING UNITS	11
REVERSING AN IMPAIRMENT LOSS	12
REQUIRED DISCLOSURES	14
APPENDIX A — DIFFERENCES BETWEEN AASB 136 AND EXISTING AASB 1010	15
APPENDIX B — DIFFERENCES BETWEEN AASB 136 AND EXISTING TREASURY GUIDELINES	16
APPENDIX C — DETERMINATION OF RECOVERABLE AMOUNT	17
APPENDIX D — RECOGNITION AND REVERSAL OF IMPAIRMENT LOSS	18

PURPOSE

The QAO Guidelines on Accounting Standard AASB 136 – Impairment of Assets are designed to assist public sector entities in accounting for and assessing impairment of assets under the new requirements of AASB 136. This publication should be considered in conjunction with the Queensland Treasury's Non-Current Asset Accounting Guidelines for the Queensland Public Sector and QAO Better Practice Guidelines for Non-Current Assets.

The QAO Guidelines on AASB 136 have been prepared in order to discuss the concepts behind the requirements of the Standard and to provide information and practical examples which may be considered in applying AASB 136 to your entities.

The AASB 136 Guidelines have specifically been tailored for the public sector environment and therefore draws on the key requirements of the Standard that have application to public sector entities. The Guidelines do not cover the following aspects of the Standard —

- Foreign Currency Future Cash Flows;
- Goodwill;
- Timing of impairment tests for Cash Generating Units to which goodwill has been allocated; and
- Reversal of impairment loss for goodwill.

For more information on Australian-equivalents-to-International Financial Reporting Standards (IFRS), QAO has produced a number of publications with application to the public sector. These include —

- IFRS – Frequently Asked Questions Booklet;
- IFRS – Practical Examples Booklet; and
- IFRS Checklist for Public Sector Agencies.

These publications are available on the QAO website at www.gao.qld.gov.au and will be updated progressively by QAO.

INTRODUCTION

OBJECTIVE OF AASB 136

AASB 136 Impairment of Assets is based on the international equivalent of the existing standard AAS 10/AASB 1010 Recoverable Amount. Both standards have the same objective of ensuring that assets are not carried at more than their recoverable amount, although AASB 136 has a wider scope than the existing standards as it applies to all assets other than those exceptions noted in AASB 136 paragraph 2 of the Standard, for example inventories and investment property. In contrast AAS 10/AASB 1010 does not apply to non-current assets of not-for-profit entities where the future economic benefits comprising those assets are not primarily dependent on the assets' ability to generate net cash inflows, non-current assets measured at fair value, net market value, net fair value, and inventories. Appendix A to this paper further considers the differences between these standards.

APPLICATION TO PUBLIC SECTOR ENTITIES

Accordingly, all public sector entities will be required to undertake an annual assessment of impairment of assets regardless of whether they are classified as "for-profit" or "not-for-profit". While entities classified as "not-for-profit" must now undertake an annual assessment of impairment, the provisions of the standard provide an allowance for these entities in determining "recoverable amount". Specifically, the standard allows that where the future economic benefits of an asset of a "not-for-profit" entity are not primarily dependent on the asset's ability to generate net cash inflows and the entity would if deprived of the asset, replace its remaining future economic benefits, the entity can use depreciated replacement cost in determining the value in use of the asset (the recoverable amount is the higher of fair value less costs to sell, and value in use). This is likely to limit the potential impact of the standard on these entities. The potential impact of this standard on public sector entities will also be dependent on the extent to which present Queensland Treasury asset accounting requirements are maintained or modified. A consideration of the potential impacts based on the existing Treasury requirements is included in Appendix B to these Guidelines.

TRANSITION AND FIRST TIME APPLICATION

Application of this standard will begin in the first annual reporting period on or after 1 January 2005 in the context of adopting all Australian-equivalents-to-International Financial Reporting Standards. *AASB 1 First-time Adoption of Australian Equivalents to International Financial Reporting Standards* requires prior period information presented as comparative information to be restated as if the requirements of AASB 136 had always applied.

AASB 1 also requires entities to use the same accounting policies in its opening Australian-equivalents-to-IFRSs balance sheet and throughout all periods presented in its first Australian-equivalents-to-IFRSs financial report. Those accounting policies shall comply with each of the Australian equivalents to IFRSs effective at the reporting date for its first Australian-equivalents-to-IFRSs financial report except for a number of optional and mandatory exemptions.

In particular AASB 1 para 39(c) requires that where an entity recognises or reverses any impairment losses for the first time in preparing its opening Australian-equivalents-to-IFRSs balance sheet, the disclosures that AASB 136 Impairment of Assets would have required if the entity had recognised those impairment losses or reversals in the period beginning with the date of transition to Australian-equivalents-to-IFRSs, shall be included in the first Australian-equivalent-to-IFRS financial report.

An entity recognises adjustments from applying AASB 136 to its opening IFRS Balance Sheet, directly in retained earnings, or if appropriate, another category of equity.

SCOPE

This standard applies to all assets excluding —

- Inventories;
- Assets arising from construction contracts;
- Deferred tax assets;
- Assets arising from employee benefits;
- Most types of financial assets;
- Investment properties;
- Certain biological assets related to agricultural activity;
- Assets arising from an insurer's contractual rights; and
- Non-current assets classified as held for sale.

The justification for these exclusions is that these type of asset classes are covered by other standards which impose their own type of impairment test.

IDENTIFICATION OF IMPAIRED ASSETS

Before undertaking a recoverable amount test an entity must first assess at each reporting date whether there is any indication that an asset **may** be impaired.

In assessing whether there is an indication that an asset may be impaired, an entity shall consider **as a minimum** a number of prescribed internal and external factors.

External factors to be considered include —

- Has the assets market value declined significantly more than would be expected as a result of the passage of time or normal use, during the period?
- Have significant changes occurred during the period (or will occur in the near future) which adversely impact on the technological, market, economic or legal environment in which the entity operates or in the market to which the asset is dedicated?
- Have market interest rates or other market rates of return on investments increased during the period such that those increases are likely to affect the discount rate used in calculating the asset's "value in use" and decrease the assets recoverable amount materially?
- Is the carrying amount of the net assets of the entity more than its market capitalisation?

Internal factors to be considered include —

- Is there available evidence of obsolescence or physical damage of the asset?
- Are there any significant changes with an adverse effect on the entity which have taken place during the period or are expected to take place in the near future, which impact on the extent to which or the manner in which the asset is used or is expected to be used
- Is there available evidence from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected?

Example 1

- An entity owns a building for which it rents floor space to external parties. There is significant decline in the property market effecting property rentals.
- Government declares that all rail lines are available for use by private operators.
- Due to terrorism concerns it is anticipated that tourism will be effected decreasing the number of international flights and passengers landing at Queensland airports.
- Due to increased health and environmental concerns the Government imposes additional legislative requirements increasing the cost of operating and maintaining of high voltage power lines.
- A review of useful lives of assets results in significant write-downs in useful lives of existing assets. In the past future cash flows have been estimated over the entire life of the asset.
- An entity decides to discontinue or reduce the provision of certain services eg QR decide it no longer intends to run passenger services.
- Based on internal reports analysing traffic volume on the Gateway Bridge it is noted that actual traffic levels are significantly below those previously expected.

Other factors

There are two provisos to the consideration of the above factors —

- The considerations included in the standard are not intended to be exhaustive; and
- Materiality.

In taking materiality into account it may be that previous assessments of recoverable amount have concluded that the recoverable amount of the asset is significantly greater than its carrying amount. Accordingly, factors which indicate existence of a slight impairment may not be sufficient to eliminate the difference previously identified and as such the entity would not need to re-estimate the asset's recoverable amount.

Example 2

- If there is an increase in short-term interest rates but the asset has a long remaining useful life, this may have no impact on the discount rate used for determining recoverable amount.
- If there was an increase in market rates which did impact on the calculation of recoverable amount, but based on previous sensitivity analysis undertaken increases in interest rates are also accompanied by increases to future cash inflows.

IMPACT OF ASSESSMENT FOR IMPAIRMENT

If indicators exist that there may be a material impairment loss then the entity will need to estimate the recoverable amount of the asset.

If there is no indication of material impairment then an estimate of recoverable amount is not required.

However, whether an indication of impairment exists tests must be conducted for —

- Intangible assets with indefinite useful lives or intangible assets not yet available for use; and
- Goodwill acquired as part of a business combination.
- This paper focuses largely on the impact on property, plant and equipment and does not consider the impact on goodwill and intangible assets.

OTHER IMPACTS

Indications of impairment may also indicate that remaining useful lives, depreciation methods or residual value of the asset require review and adjustment.

Carrying Amount of an Asset

The pending standard defines "carrying amount:" as the amount at which an asset is recognised after deducting any accumulated depreciation (or amortisation) **and accumulated impairment losses**. The carrying values of the assets are to be determined in accordance with other standards and prescribed requirements eg AASB 116 and Treasury's *Non-Current Asset Accounting Guidelines in the Queensland Public Sector*.

Measuring Recoverable Amount

The pending standard defines recoverable amount as the **higher** of —

- an asset/cash generating unit's fair value less costs to sell; and
- it's value in use

As the pending standard only requires the higher of the two amounts to be used for the recoverable amount test an entity may not need to calculate both amounts to assess impairment. If either of the amounts is above carrying value then an impairment loss will not need to be recognised for the asset/CGU.

Example 3

Case (a)

There will be no impairment loss recorded if an entity in undertaking a recoverable amount test on Asset A has determined the following values for the asset —

Basis of Value	Amount
Carrying amount	\$1,200,000
Fair value less costs to sell	\$1,100,000
Value in use	\$1,400,000

In this instance the recoverable amount would be equal to value in use as it is higher than fair value less costs to sell. Accordingly, an impairment loss would not be recognised as the recoverable amount of \$1,400,000 exceeds the carrying amount of \$1,200,000.

Case (b)

This can be compared to the following case where an impairment loss would need to be recorded in undertaking a recoverable amount test on Asset B where the entity has determined the following values for the asset —

Basis of Value	Amount
Carrying amount	\$1,200,000
Fair value less costs to sell	\$1,100,000
Value in use	\$1,000,000

In this instance an impairment loss of \$100,000 would be recorded as the recoverable amount would equal fair value less costs to sell as it is higher than value in use. As the recoverable amount (\$1,100,000) is less than the carrying value of Asset B (\$1,200,000) an impairment loss would be recorded for the difference (\$100,000).

Fair Value Less Costs to Sell

Fair value less costs to sell is defined by the pending standard as the amount obtainable from the sale of an asset or cash-generating unit in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.

Fair value may be determined by reference to —

- binding sale agreement in an arm's length transaction;
- the current market value of the asset where the asset can be traded in an active market;
- where current market prices are not available, the price of the most recent transaction may provide a basis for estimating fair value (subject to changes in key economic conditions since time of transaction); or
- best information available to reflect the amount an entity could obtain at the reporting date for the disposal of the asset in an arm's length transaction.

The pending standard defines active market as a market in which all of the following conditions are met —

- the items traded within the market are homogenous;
- willing buyers and sellers can normally be found at any time; and
- prices are available to the public.

Examples of costs of disposal include legal costs, stamp duty and other transaction taxes, costs of removing the asset, and direct incremental costs to bring the asset into condition for its sale.

Value in Use

Value in use is defined by the pending standard to mean the **present value** of the future cash flows expected to be derived from an asset or cash-generating unit.

This requires a two step process of —

- estimating the future cash inflows and outflows to be derived from the continuing use of the asset and from its ultimate disposal; and
- applying an appropriate discount rate to those future cash flows.

In undertaking the present value calculation, the pending standard requires the following elements to be included in the calculation —

- an estimate of 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; and
- other factors, such as illiquidity, that market participants would reflect in pricing the future cash flows the entity expects to derive from the asset.

Where the future economic benefits of an asset of a *not-for-profit* entity are not primarily dependent on the assets ability to generate net cash inflows and where the entity would, if deprived of the asset, replace its remaining future economic benefits, value in use shall be determined as the *depreciated replacement* cost of the asset.

ESTIMATION OF FUTURE CASH FLOWS IN DETERMINING VALUE IN USE

The pending standard specifies what information **must** be considered as the basis for estimating future cash flows.

1. Cash flow projections are to be based on reasonable and supportable assumptions that represents management's best estimate of the range of economic conditions that will exist over the remaining useful life of the asset.

Greater weight is to be given to those supported by external evidence. Accordingly management should reassess their assumptions on a regular basis and ensure they are consistent with past actual outcomes and the effects of subsequent events or circumstances that did not exist when those actual cash flows were generated.

2. Cash flow projections are to be based on the most recent financial budgets/forecasts approved by management, but shall exclude any estimated future cash inflows/outflows expected to arise from future restructuring or from improving or enhancing the asset's performance.

Projections based on these budgets/forecasts shall cover a maximum period of five years, unless a longer period can be justified. The pending standard considers that cash flows projected over a period greater than five years are less reliable. Management may use cash flow projections based on budgets/forecasts over a period longer than five years if it is confident that these projections are reliable and it can demonstrate its ability, based on past experience, to forecast cash flows accurately over that period.

3. Cash flow projections beyond the period covered by the most recent budgets/forecasts are to be estimated by extrapolating the projections based on the budgets/forecasts using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified.

The growth rate used is not to exceed the long-term average growth rate for the products, industries or country or countries in which the entity operates, or for the market in which the asset is used, unless a higher rate can be justified.

The estimated future cash flows for measuring value in use are required to include —

- projections of cash inflows from the continuing use of the asset;
- projected cash outflows that are necessarily incurred to generate the cash inflows from continuing use of the asset (including cash outflows to prepare the asset for use) and can be directly attributed, or allocated on a reasonable and consistent basis, to the asset; and
- net cash flows, if any, to be received (or paid) for the disposal of the asset at the end of its useful life.

Future cash flows are to be estimated based on the current condition of the asset. Accordingly these cash flows will not include estimated cash inflows/outflows expected to arise from —

- future restructuring to which the entity is not yet committed (refer AASB 137 for further guidance); and
- improving or enhancing the assets performance.

The estimate of net cash flows from the disposal of the asset at the end of its useful life is determined in a similar way to determining an assets fair value less costs to sell except in estimating the cash flows —

- prices prevailing at the date of the estimate for similar assets that have reached the end of their useful life and have operated under similar conditions to those in which the asset will operate are used; and
- those prices are adjusted for the effect of both future price increases due to general inflation and specific future price increases/decreases.

Use of Discount Rates

The discount rate to be used must be a pre-tax rate reflecting current market assessments of —

- the time value of money; and
- the risk specific to the asset for which the future cash flow estimates have been adjusted.

The discount rate used to measure an asset's value in use shall not reflect risks already adjusted for in the estimated future cash flows in order to ensure that the effect of certain assumptions are not double-counted.

Estimates of future cash flows and the discount rate are to reflect consistent assumptions about price increases attributable to general inflation. If the discount rate includes the effect of these increases, future cash flows are to be estimated in nominal terms. If the discount rate excludes these effects the future cash flows are to be estimated in real terms.

Further, because the time value of money is considered by discounting the estimated future cash flows, these cash flows exclude cash flows from financing activities. Similarly, because the discount rate used is a pre-tax rate the future cash flows are also estimated on a pre-tax basis.

Appendix A to the pending standard provides further guidance on using present value techniques to measure value in use, including estimation of future cash flows and identification of an appropriate discount rate.

IDENTIFICATION OF CASH-GENERATING UNITS

Recoverable amount is to be determined for an individual asset unless the asset does not generate cash inflows that are largely independent of those from other assets or group of assets. In this case recoverable amount is determined for the cash generating unit to which the asset belongs, unless —

- the asset's *fair value less costs* to sell is higher than its carrying amounts; or
- the asset's *value in use* can be estimated to be close to its fair value less costs to sell and *fair value less costs* to sell can be determined.

A cash-generating unit is defined in the pending standard as the smallest identifiable group of assets that generate cash inflows that are largely independent of the cash inflows from the other assets or groups of assets.

If there is any indication that an asset may be impaired, recoverable amount shall be estimated for the individual asset. If it is not possible to estimate the recoverable amount of the individual asset, the entity shall determine the recoverable amount of the cash-generating unit to which the asset belongs.

The recoverable amount of an individual asset cannot be determined if —

- *value in use* cannot be estimated to close to its *fair value less costs to sell*; and
- the asset does not generate cash inflows that are largely independent of those from other assets.

In such cases the assets value in use, and recoverable amount, can only be determined for the cash-generating unit to which the asset relates. Identification of an asset's cash-generating unit involves the use of professional judgement.

Example 4

A Port Authority owns a road which provides main access for trucks transporting goods to the wharves for loading on vessels. The road cannot be sold (without the remainder of the Port Authority) and does not generate cash inflows that are largely independent of the cash inflows from the other assets utilised at the port facility.

It is not possible to estimate the recoverable amount of the road because its value in use cannot be determined and there is no sale value for the asset. Therefore, the Port Authority would be required to estimate the recoverable amount of the cash generating unit to which the private road belongs. This may be the entire port facility including the wharves, channels, breakwaters and heavy equipment, such as cranes, on the basis that all of the assets are required to be utilised together to generate cash flows from the port operations.

In identifying a cash-generating unit the entity is required to identify the lowest aggregation of assets that generate largely independent cash inflows.

Example 5

A entity provides rail services under an agreement with the Government. This agreement requires the provision of passenger services on seven separate train lines. While some assets are devoted to each train line, others such as the passenger trains operate across the entire network. Some cash flows can be identified separately for each line while some expenses, such as payroll costs, apply to the entire network and are allocated across each line. Based on internal reports it has been identified that some of the lines operate at a significant loss. Cash inflows also include community service obligations paid to the entity for providing commuter services. These are paid for the entire service and are not allocated to specific lines.

In this instance because the entity does not have an option to cancel any of the services provided, and many of the cash flows and assets are shared across the entire network, the lowest level of identifiable cash inflows that are largely independent of the cash inflows from the other assets or group of assets is the cash inflows generated by the seven train lines together. Further, the cash flow streams from each line are not independent of each other. The provision of the commuter services on each line work together to generate cash flows for the entity eg passengers may purchase tickets for travel across more than one line and individual trains operate across the entire network and are not limited to one commuter line.

However, the cash flows generated by the provision of the commuter services may be independent and separately identified from other services provided such freight and haulage services which may form a separate cash generating unit.

Cash inflows allocated to a cash-generating unit are those received from parties external to the entity. However, if an active market exists for the output produced by an asset or group of assets, that asset/group shall be identified as a cash-generating unit even if some or all of the output is used internally. This is because the asset/group could generate cash inflows that would be largely independent of the cash flows from other groups of assets.

If cash inflows generated by a cash-generating unit are affected by internal transfer pricing, an entity is to use management's best estimates of future prices to be achieved in arm's length transactions in estimating cash inflows and outflows used to determine value in use.

Cash-generating units are to be identified on a consistent basis from period to period for the same asset or type of assets, unless a change is justified.

When assets are grouped for recoverability assessments, it is important to include all assets that generate or are used to generate the relevant stream of cash inflows. In some cases, although some assets contribute to the estimated future cash flows of a cash-generating unit, they cannot be allocated on a reasonable and consistent basis. This may give rise to the identification of *corporate assets*.

Corporate assets are defined as assets, other than goodwill, that contribute to the future cash flows of both the cash-generating unit under review and other cash-generating units. The distinctive characteristics of corporate assets is that they do not generate cash flows independently of other assets or groups of assets and their carrying amount cannot be fully attributed to the cash-generating unit under review.

In testing a cash-generating unit for impairment, each entity is required to identify all corporate assets that relate to the cash-generating unit under review. In attempting to allocate the carrying amount of the corporate assets entities need to consider —

- (a) If the carrying amounts can be allocated on a reasonable and consistent basis to that unit, the entity must compare the carrying amount of the unit, including the portion of the carrying amount of the corporate asset allocated to the unit, with its recoverable amount.
- (b) If the carrying amounts of the corporate assets cannot be allocated on a reasonable and consistent basis to the unit, then the entity must —
 - (i) Compare the carrying amount of the unit, excluding the corporate asset, with its recoverable amount and recognise any impairment loss;
 - (ii) Identify the smallest group of cash-generating units that includes the cash-generating unit under review and to which a portion of the carrying amount of the corporate asset can be allocated on a reasonable and consistent basis; and
 - (iii) Compare the carrying amount of that group of cash-generating units, including the portion of the carrying amount of the corporate asset allocated to that group of units, with the recoverable amount of that group of units.

RECOGNITION OF IMPAIRMENT LOSSES

If, and only if, the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset shall be reduced to its recoverable amount with the difference recorded as an impairment loss.

Impairment losses are to be recognised immediately to profit/loss, unless the asset is carried at a revalued amount in accordance with another standard. In such a case the impairment loss is treated as a revaluation decrement in accordance with the relevant standard. Accordingly under AASB 116 Property, Plant and Equipment, the impairment loss would be —

- recognised directly in profit or loss; or
- debited directly to the asset revaluation reserve to the extent of any credit balance existing in the revaluation reserve in respect of that asset.

Example 6

At year end the XYZ Authority (a government owned corporation) identifies factors which may indicate that Asset B is impaired and the following values are identified when undertaking an assessment of recoverable amount.

Basis of Value	Amount
Carrying amount	\$1,200,000
Fair value less costs to sell	\$1,100,000
Value in use	\$1,000,000

Based on these values, recoverable amount of Asset B at year end is \$1,100,000. Accordingly, XYZ would need to record an impairment loss of \$100,000.

If this asset is not subject to regular revaluation the following journal entry would be required —

	DR	CR
Impairment loss expense	\$100,000	
Asset B – Accumulated Impairment Losses		\$100,000

If, however, Asset B had been previously revalued and an amount of \$50,000 was credited to the Asset Revaluation Reserve as a result of the revaluation, and this amount remains in the reserve, the following entry would be required —

	DR	CR
Impairment loss expense	\$50,000	
Asset Revaluation Reserve (Asset B)	\$50,000	
Asset B – Accumulated Impairment Losses		\$100,000

After recognising the impairment loss, the depreciation (amortisation) charges for the asset shall be adjusted in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.

Example 7

If Asset A has a cost of \$100,000 and a useful life of 10 years depreciation would be calculated as follows (assuming straight line depreciation used).

Year	Book Value	Depreciation	Acc Depreciation	Carrying Value
1	\$1,000,000	\$100,000	\$100,000	\$900,000
2	\$1,000,000	\$100,000	\$200,000	\$800,000
3	\$1,000,000	\$100,000	\$300,000	\$700,000
4	\$1,000,000	\$100,000	\$400,000	\$600,000
5	\$1,000,000	\$100,000	\$500,000	\$500,000
6	\$1,000,000	\$100,000	\$600,000	\$400,000
7	\$1,000,000	\$100,000	\$700,000	\$300,000
8	\$1,000,000	\$100,000	\$800,000	\$200,000
9	\$1,000,000	\$100,000	\$900,000	\$100,000
10	\$1,000,000	\$100,000	\$1,000,000	—

However, if we assume that Asset A recorded an impairment loss of \$150,000 at the end of year 4, then depreciation would be calculated as follows (assuming no change to remaining useful life) —

Year	Book Value	Depreciation	Acc Depreciation	Accumulated Impairment Loss	Carrying Value
1	\$1,000,000	\$100,000 ⁽¹⁾	\$100,000		\$900,000
2	\$1,000,000	\$100,000	\$200,000		\$800,000
3	\$1,000,000	\$100,000	\$300,000		\$700,000
4	\$1,000,000	\$100,000	\$400,000	(\$150,000)	\$450,000
5	\$1,000,000	\$75,000 ⁽²⁾	\$475,000	(\$150,000)	\$375,000
6	\$1,000,000	\$75,000	\$550,000	(\$150,000)	\$300,000
7	\$1,000,000	\$75,000	\$625,000	(\$150,000)	\$225,000
8	\$1,000,000	\$75,000	\$700,000	(\$150,000)	\$150,000
9	\$1,000,000	\$75,000	\$775,000	(\$150,000)	\$75,000
10	\$1,000,000	\$75,000	\$850,000	(\$150,000)	—

⁽¹⁾ Depreciation calculated on a straight line basis with carrying amount of \$1,000,000 allocated across the estimated 10 year useful life of the asset.

⁽²⁾ The depreciation has been adjusted to allocate the carrying amount of \$450,000 (book value less accumulated depreciation less aggregated impairment losses) across the remaining useful life of the asset (6 years).

When the amount estimated for an impairment loss is actually greater than the carrying amount of the asset to which it relates, the pending standard will only allow an entity to recognise a liability, if that is required by another Standard. This would be rare case as it would require the asset to have a negative present value (i.e. the present value of the estimated cash outflows exceed the estimated cash inflows expected from the continued use of the asset).

This situation may occur where an entity is required to use its assets to provide a service under a contract or community service obligation for a fixed return which is significantly less than the estimated cost of providing those services.

RECOGNISING IMPAIRMENT LOSSES FOR CASH-GENERATING UNITS

An impairment loss for a cash-generating unit will be recognised if, and only if, the recoverable amount of the unit, or group of units, is less than the carrying amount of the unit/group. The impairment loss is to be allocated to reduce the carrying amount of the assets of the unit/group on a pro rata basis based on the carrying value of each asset in the unit/group. These reductions are to be treated as impairment losses on the individual assets and recognised in accordance with requirements noted above.

In allocating the impairment loss, entities are not allowed to reduce the carrying amount of an asset below the higher of —

- its fair value less costs to sell (if determinable);
- its value in use (if determinable); and
- zero.

The amount of the impairment loss that would otherwise have been allocated to the asset shall be allocated pro rata to the other assets of the unit/group.

Example 8

Entity XYZ has identified three cash-generating units within its operations. As a result of identifying factors indicating impairment at year-end, XYZ is required under AASB 136 to undertake an assessment of impairment for each of the three cash-generating units.

Each of the relevant cash-generating units identified operate out of the same building and XYZ considers that the relative carrying values of the cash-generating units identified provide a reasonable indication of the proportion of the common building devoted to each of the cash-generating units. The carrying amount of the building is \$150,000.

There is no basis on which to calculate a net selling price of each cash-generating unit and accordingly the recoverable amount of each cash-generating unit is based on its *value in use*.

	Unit A	Unit B	Unit C	Total
Carrying amount	\$100,000	\$150,000	\$200,000	\$450,000
Value in use	\$200,000	\$160,000	\$250,000	\$610,000

Step 1 – Allocate the carrying amount of the corporate asset to each cash-generating unit.

	Unit A	Unit B	Unit C	Total
Carrying amount	\$100,000	\$150,000	\$200,000	\$450,000
Prorata allocation of building	22%	33%	44%	100%
Allocation of building based on %	\$33,333	\$50,000	\$66,667	\$150,000
Carrying amount after allocation	\$133,333	\$200,000	\$266,667	\$600,000

Step 2 – Review cash-generating units for impairment

	Unit A	Unit B	Unit C
Impairment Test			
Carrying amount (after allocation)	\$133,000	\$200,000	\$266,667
Recoverable amount	<u>\$200,000</u>	<u>\$160,000</u>	<u>\$250,000</u>
Difference	<u>\$66,666</u>	<u>(\$40,000)</u>	<u>(\$16,667)</u>

As recoverable amount is greater than carrying amount for Unit A no impairment loss will be recognised for this cash-generating unit.

Step 3 – Allocate the impairment loss between the cash-generating units and the corporate asset.

	Unit A	Unit B	Unit C
Allocation of Impairment Loss			
Allocation to building	\$-	(\$10,000)	(\$4,167)
Allocation to cash generating unit	<u>\$-</u>	<u>(\$30,000)</u>	<u>(\$12,500)</u>
Difference	<u>\$-</u>	<u>(\$40,000)</u>	<u>(\$16,667)</u>

- (a) No impairment loss was recognised for Unit A as noted above.
- (b) The impairment losses for Unit B and Unit C were allocated on basis of 25% to the building and 75% to the cash-generating units as follows —

	Carrying Amount	% Total	Impairment Loss
Unit B			
Building allocation	\$50,000	25%	\$10,000
CGU excluding building	\$150,000	75%	\$30,000
Total	\$200,000	100%	\$40,000
Unit C			
Building allocation	\$66,667	25%	\$4,167
CGU excluding building	\$200,000	75%	\$12,500
Total	\$266,667	100%	\$16,667

The above impairment losses would then be allocated pro rata across the assets within each CGU, based on their carrying amounts.

REVERSING AN IMPAIRMENT LOSS

An entity is to assess at each reporting date whether there is any indication that an impairment loss recognised in prior periods for an asset may no longer exist or may have decreased. If such an indication exists, the entity shall estimate the recoverable amount of that asset.

In assessing whether there is an indication that an impairment loss recognised in prior periods for an asset may no longer exist or may have decreased an entity shall consider, as a minimum, a number of prescribed internal and external indicators

External indicators to be considered include —

- Has the assets market value increased significantly, during the period?
- Have significant changes occurred during the period (or will occur in the near future) which favourably impact on the technological, market, economic or legal environment in which the entity operates or in the market to which the asset is dedicated?
- Have market interest rates or other market rates of return on investments decreased during the period such that those decreases are likely to affect the discount rate used in calculating the asset's value in use and increase the assets recoverable amount materially?

Internal indicators to be considered include —

- Are there any significant changes with a favourable effect on the entity which have taken place during the period or are expected to take place in the near future, which impact on the extent to which or the manner in which the asset is used or is expected to be used. These changes may include costs incurred during the period to add to improve or enhance the asset's performance or restructure the operation to which the asset belongs.
- Is there available evidence from internal reporting that indicates that the economic performance of an asset is, or will be, better than expected?

Where an impairment loss has been recognised in prior periods for an asset other than goodwill, the loss shall be reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the impairment loss was recognised. If this is the case the carrying amount of the asset shall be increased to the recoverable amount. This increase is a reversal of an impairment loss. However, the increased carrying value of the asset on reversal of the impairment loss shall not exceed the lower of the carrying amount that would have been determined (net of depreciation/amortisation) had no impairment loss been recognised for the asset in prior years and the recoverable amount.

A reversal of an impairment loss for an asset shall be recognised immediately in profit/loss, unless the asset is carried at revalued amount in accordance with another standard, including AASB 116. Any reversal of an impairment loss of a revalued asset shall be treated as a revaluation increment in accordance with the relevant Standard.

After a reversal of an impairment loss is recognised, the depreciation (amortisation) charge on the asset shall be adjusted in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.

Example 9

Consider Example 7 where Asset A had a cost of \$100,000 and a useful life of 10 years with depreciation calculated as follows (assuming straight line depreciation used).

Year	Book Value	Depreciation	Acc Depreciation	Carrying Value
1	\$1,000,000	\$100,000	\$100,000	\$900,000
2	\$1,000,000	\$100,000	\$200,000	\$800,000
3	\$1,000,000	\$100,000	\$300,000	\$700,000
4	\$1,000,000	\$100,000	\$400,000	\$600,000
5	\$1,000,000	\$100,000	\$500,000	\$500,000
6	\$1,000,000	\$100,000	\$600,000	\$400,000
7	\$1,000,000	\$100,000	\$700,000	\$300,000
8	\$1,000,000	\$100,000	\$800,000	\$200,000
9	\$1,000,000	\$100,000	\$900,000	\$100,000
10	\$1,000,000	\$100,000	\$1,000,000	—

After recording an impairment loss of \$150,000 at the end of year 4, the carrying value and depreciation were adjusted as follows —

Year	Book Value	Depreciation	Acc Depreciation	Accumulated Impairment Loss	Carrying Value
1	\$1,000,000	\$100,000	\$100,000		\$900,000
2	\$1,000,000	\$100,000	\$200,000		\$800,000
3	\$1,000,000	\$100,000	\$300,000		\$700,000
4	\$1,000,000	\$100,000	\$400,000	(\$150,000)	\$450,000
5	\$1,000,000	\$75,000	\$475,000	(\$150,000)	\$375,000
6	\$1,000,000	\$75,000	\$550,000	(\$150,000)	\$300,000
7	\$1,000,000	\$75,000	\$625,000	(\$150,000)	\$225,000
8	\$1,000,000	\$75,000	\$700,000	(\$150,000)	\$150,000
9	\$1,000,000	\$75,000	\$775,000	(\$150,000)	\$75,000
10	\$1,000,000	\$75,000	\$850,000	(\$150,000)	—

Assume now that at the end of year 5 in assessing impairment that the entity had identified that the economic performance of the asset has increased significantly over the past twelve months to the extent that the asset now has a value in use of \$510,000. How much of the previous impairment loss is the entity entitled to reverse?

The difference between carrying amount (\$510,000) and value in use (\$375,000) at the end of year 5 is \$135,000 which is less than the original impairment loss of \$150,000 recorded for the asset. However, if the asset had not initially recorded the impairment loss, the carrying amount of Asset A at the end of year 5 would only have been \$500,000. Accordingly this is the maximum amount to which the carrying amount of the asset can be increased at the end of year 5. In this instance the entity will only be allowed to reverse an amount of \$125,000 against the original impairment loss being the difference between the carrying amount if the asset had not been impaired (\$500,000) and the existing carrying amount (\$375,000).

A reversal of an impairment loss for a cash-generating unit shall be allocated to the assets of the unit pro rata with the carrying amount of those assets. The increases in carrying amounts shall be treated as reversals of impairment losses for individual assets and recognised in accordance with the above requirements.

In allocating a reversal of an impairment loss for a cash-generating unit, the carrying amount of an asset shall not be increased above the lower of —

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

The amount of the reversal of the impairment loss that would otherwise have been allocated to the asset shall be allocated pro rata to the other assets of the unit.

REQUIRED DISCLOSURES

Reporting entities are required to disclose for *each class of assets* —

- the amount of impairment losses or reversal of impairment losses recognised in profit/loss during the period and the line item where the impairment losses are included;
- the amount of impairment losses and reversals of impairment losses in revalued assets recognised directly in equity during the period.

This information may be disclosed with other disclosures for the class of asset such as the reconciliation of the carrying amount at the beginning and end of the reporting period required by AASB 116.

An entity that reports segment information is required to disclose the amount of impairment losses and reversals of impairment losses in profit/loss and directly in equity for each reportable segment.

For each material impairment loss recognised or reversed during the period for an individual asset, or cash-generating unit, entities must disclose —

- the events and circumstances that led to the recognition or reversal of the impairment loss;
- the amount of the impairment loss recognised or reversed;
- for an individual asset —
 - the nature of the asset; and
 - the reportable segment to which the asset belongs (if any);
- for a cash-generating unit —
 - a description of the cash-generating unit;
 - the amount of the impairment loss recognised or reversed by class of asset and reportable segment (if any); and
 - if the aggregation of assets for identifying the cash-generating unit has changed since the previous estimate of recoverable amount, a description of the current and former method of aggregating the assets and reasons for change.
- whether recoverable amount was *fair value less costs of sale* or *value in use*;
- if recoverable amount is *fair value less costs to sell*, the basis used to determine it; and
- if recoverable amount is *value in use*, the discount rate(s) used in the current estimate and previous estimates (if any) of *value in use*.

Entities are encouraged to disclose assumptions used to determine the recoverable amount during the period

APPENDIX A — DIFFERENCES BETWEEN AASB 136 AND EXISTING AASB 1010

Some of the key differences between the Pending Accounting Standard and the existing standard are recorded below.

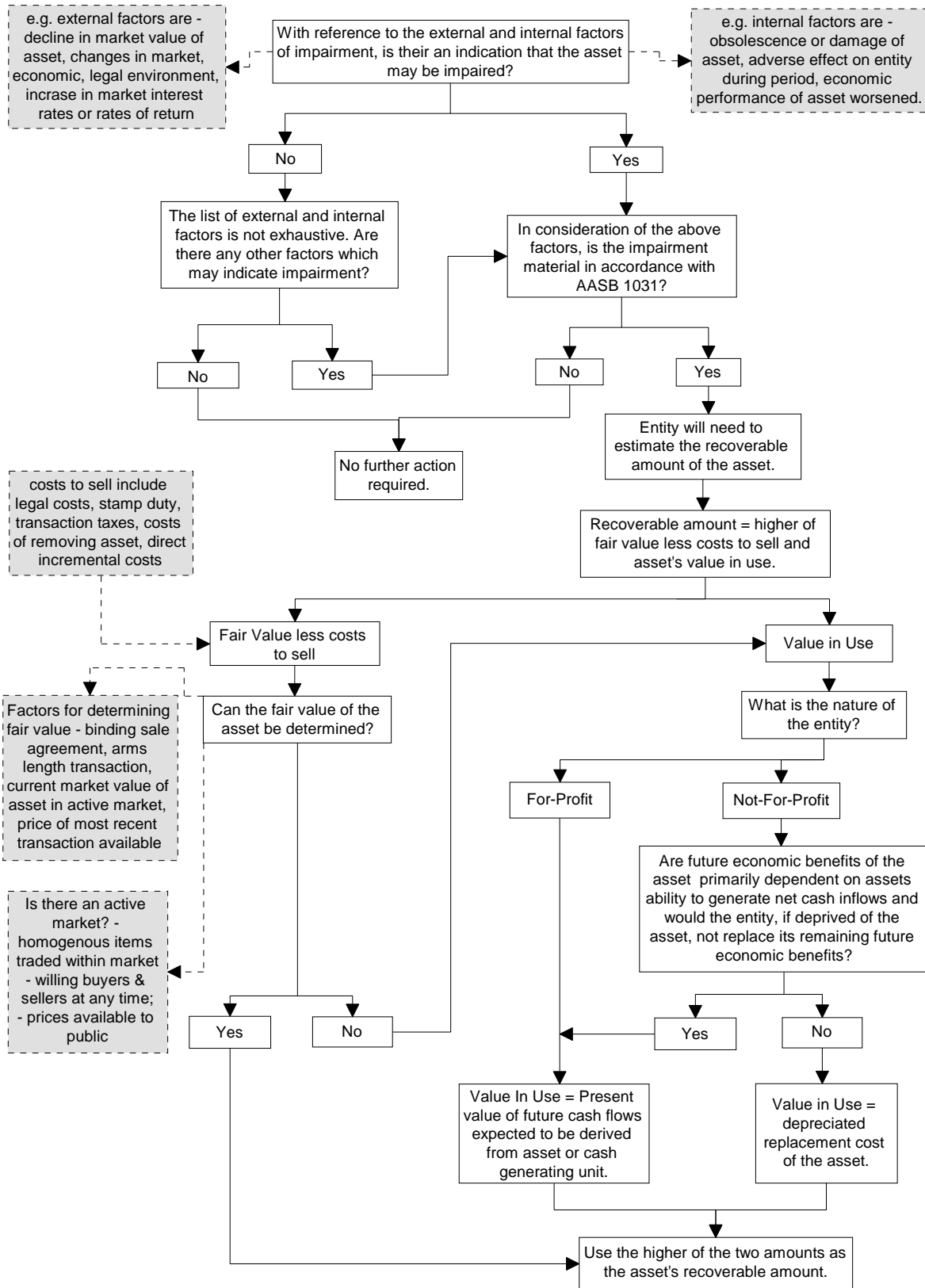
Area	AASB 136	AASB 1010
<i>Scope</i>	Applies to all assets, other than those specific exceptions noted in paragraph 136.2 regardless of whether the assets are recorded at cost or fair value.	Only applies to non-current assets, excluding Inventory, recorded at cost.
<i>Definition of recoverable amount</i>	Defined as the higher of fair value less costs to sell and its value in use.	Means the net amount that is expected to be recovered through cash inflows and outflows arising from its continued use and subsequent disposal.
<i>Cash flow projections</i>	Provides basis for determining estimated future cash flows when calculating value in use.	No specific guidance on the method to be used in determining future cash flows.
<i>Discounting</i>	Value in use requires a calculation of the present value of future cash flows associated with the asset. Specific requirements and guidance are provided on the discount rate to be used to calculate present value.	While discounting cash flows to their present value is allowed, it is not actually required by the standard.
<i>Identification of cash-generating units</i>	This standard identifies circumstances where it is not possible to associate cash flows with individual assets.	This standard recognises the concept of cash-generating units but does not provide specific guidance on how to identify cash-generating units..
<i>Allocation of impairment losses</i>	The standard provides requirements on how impairment losses are to be allocated to assets within a cash-generating unit including limits on write-downs and use of pro rata basis.	This standard does not provide any specific guidance on how recoverable amount write-downs are to be applied within a group of assets.
<i>Reversal of impairment loss</i>	The standard provides guidance as to when and how a previously recognised impairment loss may be reversed.	This standard does not provide for a reversal of previously recognised recoverable amount write-downs.
<i>Disclosures</i>	This standard requires disclosure of information in relation to — <ul style="list-style-type: none"> ● Segment reporting ● Impairment losses for individual assets and cash-generating units ● Material impairment losses 	The disclosure requirements of this standard are more general and are less prescriptive.

APPENDIX B — DIFFERENCES BETWEEN AASB 136 AND EXISTING TREASURY GUIDELINES

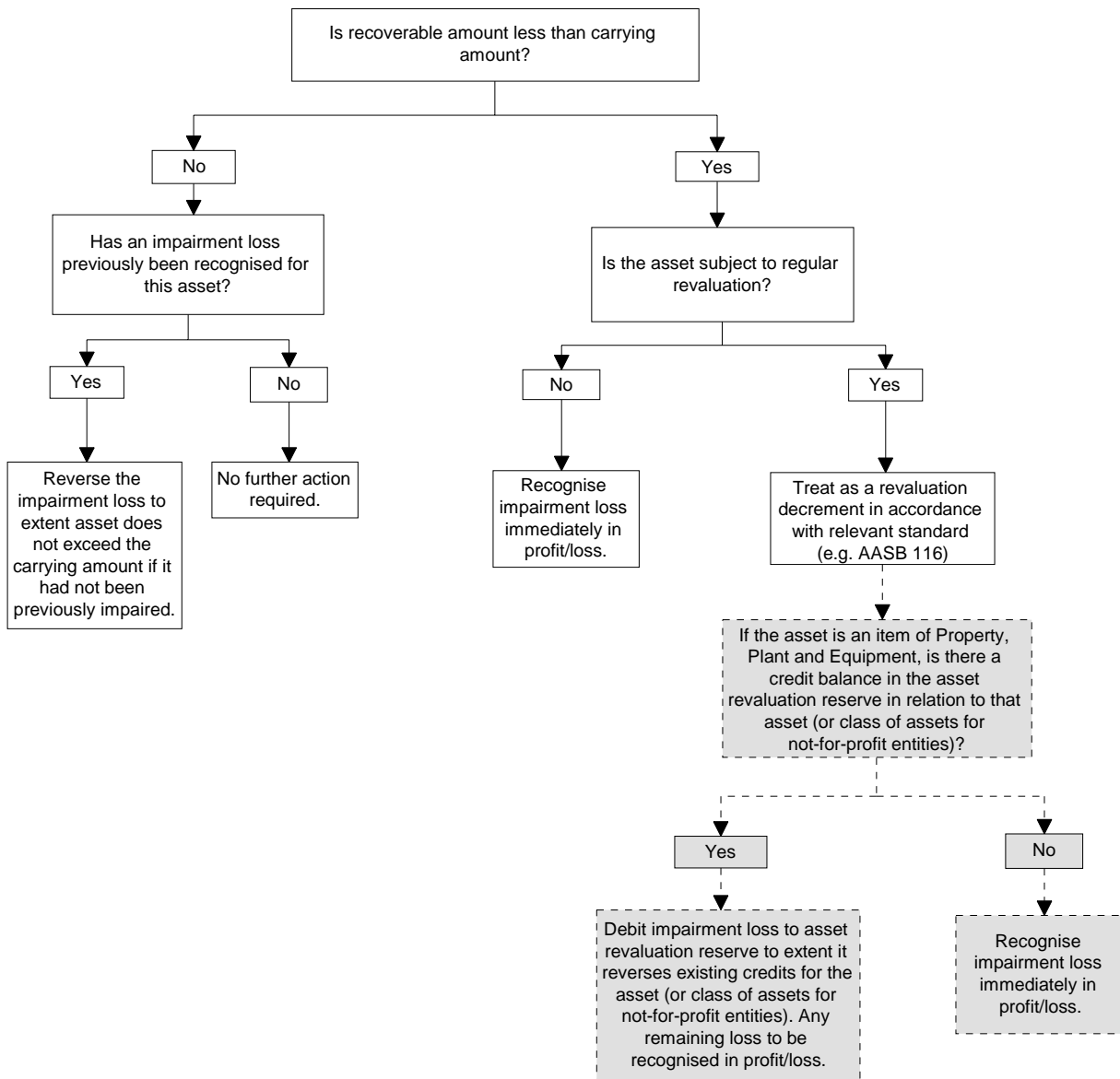
The following table considers how AASB 136 may impact on items of property, plant and equipment valued under Queensland Treasury's "Non-Current Asset Accounting Guidelines in the Queensland Public Sector".

Basis of Carrying Value	Treasury Guidelines	AASB 136
<i>Fair Value</i>	<ul style="list-style-type: none"> Land, buildings, infrastructure, heritage and cultural assets are required to have "fair value" as their carrying value. Provides a number of options for determining fair value depending on the type of entity and the nature of the asset. Assets carried at fair value are not subject to impairment testing. 	<ul style="list-style-type: none"> <i>Fair value less costs to sell</i> is defined by the standard as the amount obtainable from the sale of an asset or cash-generating unit in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal. Only one part of the recoverable amount test.
<i>Option 1 — Assets for which a market price can be determined.</i>	<ul style="list-style-type: none"> Where there is an active liquid market for assets similar in type and condition, the fair value of the asset is its price in that market. 	<ul style="list-style-type: none"> This definition would equate to "fair value" used in the recoverable amount test under AASB 136. Accordingly whether there was an impairment loss would depend on — <ul style="list-style-type: none"> (a) Whether "value in use" was greater than fair value less costs to sell; and (b) whether "costs to sell" were material as this would reduce fair value less costs to sell to below the carrying value (i.e. fair value).
<i>Option 2 — Assets with no market price – For Profit Entities</i>	<ul style="list-style-type: none"> Where there is no active market "fair value" is equivalent to the depreciated current replacement cost or depreciated current reproduction cost of the asset. However, the above value is not to exceed the net present value of the cash flows of the operations of which the assets form part. 	<ul style="list-style-type: none"> As there is no active market for these assets "fair value less costs to sell" is unlikely to be determinable. Accordingly recoverable amount under AASB 136 will equate to the asset's "value in use". As the carrying amounts of the asset under Treasury Guidelines cannot exceed the net present value of the associated cash flows of the asset, this should not materially differ from value in use, unless the methodology used does not comply with AASB 136.
<i>Option 3 — Assets where no market price exists – service potential to Not For Profit entity not dependent on generating cash flows</i>	<ul style="list-style-type: none"> In this situation "fair value" is to be determined as the lower of depreciated current replacement cost or depreciated current reproduction cost. 	<ul style="list-style-type: none"> Under AASB 136 recoverable amount would be based on "value in use" as there would be no way of determining "fair value less costs to sell". AASB 136 specifically requires that in these circumstances "value in use" will be determined as depreciated replacement cost. Based on the above requirements carrying value should not exceed the recoverable amount of the asset and accordingly no impairment loss will be recognised.
<i>Option 4 — Assets where no market price exists – service potential to Not For Profit entity is dependent on generating cash flows</i>	<ul style="list-style-type: none"> Assets in these circumstances are to be valued at current replacement cost or current reproduction cost. However, the value determined above cannot exceed the net present value of the cash flows associated with the asset. 	<ul style="list-style-type: none"> As there is no active market for these assets "fair value less costs to sell" is unlikely to be determinable. Accordingly recoverable amount under AASB 136 will equate to the asset's "value in use". AASB 136 specifically requires that in these circumstances "value in use" will be determined as depreciated replacement cost. As the carrying amount of the asset under Treasury Guidelines cannot exceed the net present value of the associated cash flows of the asset, this should not materially differ from value in use, unless methodology used does not comply with AASB 136.
<i>Cost</i>	<ul style="list-style-type: none"> The Treasury Guidelines require all classes of non-current assets other than land, buildings, infrastructure, heritage and cultural assets to be recorded at cost i.e. depreciated historical cost or depreciated deemed cost. If the entity was a "for profit" the carrying amount of these assets could not exceed recoverable amount. If the entity was a "not for profit" entity then generally, a recoverable amount test was not required. Recoverable amount was only determined by reference to expected future cash flows from use and subsequent disposal 	<ul style="list-style-type: none"> Under AASB 136 recoverable amount is determined as the higher of – <ul style="list-style-type: none"> (a) Fair value less costs to sell; and (b) Value in use, which requires discounting of expected future cash flows. Not for profit entities are now required to undertake a recoverable amount test as noted above. The recoverable amount of assets of a not for profit entity that are not dependent on cash flows will be based on depreciated replacement cost where fair value cannot be determined. Accordingly, the greatest potential impact of AASB 136 rests within assets recorded at cost.

APPENDIX C — DETERMINATION OF RECOVERABLE AMOUNT



APPENDIX D — RECOGNITION AND REVERSAL OF IMPAIRMENT LOSS



Disclaimer
 This publication is a guide based on information available as at July 2004 and is not a substitute for the Standards, exposure drafts, AASB and IASB Standards. Users of this publication should be aware that the requirements of IFRS could change over time. For further information or clarification, please refer to the AASB website.

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