

Insights into PAS 36

Overview of the Standard

PAS 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 PAS 36's guidance is detailed, prescriptive and complex in some areas.

The articles in our 'Insights into PAS 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 PAS 36, and revisit some areas where confusion has been seen in practice.

This article provides an 'at a glance' overview of PAS 36's main requirements and outlines the major steps in applying those requirements.

Objective of PAS 36

The objective of PAS 36 is to outline the procedures an entity should apply to ensure the carrying values of all its assets are not stated above their recoverable amounts (the amounts to be recovered through use or sale of the assets). To accomplish this objective, PAS 36 provides guidance on:

- the level at which to review for impairment (e.g., individual asset level, cash-generating units (CGU) level or groups of CGUs)
- if and when a quantitative impairment test is required, including the indicator-based approach for an individual asset that is not goodwill, an indefinite life intangible asset or intangible asset not yet ready for use
- how to perform the quantitative impairment test by estimating the asset's (or CGU's) recoverable amount
- how to recognize and reverse an impairment loss
- when and under what circumstances an entity must reverse an impairment loss, and
- the detailed disclosure requirements (both in the case of impairment and also in the absence of impairment).



PAS 36 Key definitions

PAS 36 defines key terms that are essential to understanding its guidance. The most significant definitions are highlighted below:

Carrying amount	Impairment loss	Recoverable amount	Value in use
The amount at which an asset is recognized after deducting any accumulated depreciation (amortization) and accumulated impairment losses thereon	The amount by which the carrying amount of asset or a CGU exceeds its recoverable amount	The higher of an asset or CGU's fair value less costs of disposal (FVL COD) and its value in use (VIU)	The present value of the future cash flows expected to be derived from an asset or CGU

Below is a summary of PAS 36's main requirements:

Area of PAS 36	Requirement
Principle	The overall principle in PAS 36 is that assets should not be carried above their recoverable amount.
Scope	<p>PAS 36 applies to all assets other than those for which the measurement requirements of other PFRS are such that a PAS 36-based impairment review is irrelevant or unnecessary. Assets outside PAS 36's scope include:</p> <ul style="list-style-type: none"> • Inventories • financial assets in the scope of PFRS 9 'Financial Instruments' • contract assets and assets arising from costs to obtain or fulfill a contract recognized in accordance with PFRS 15 'Revenue from Contracts with Customers' • deferred tax assets • assets arising from employee benefits • assets classified as held for sale • investment property measured using the fair value model • biological assets related to agricultural activity within the scope of PAS 41 'Agriculture' measured at fair value less costs to sell, and • contracts that are assets and any assets for insurance acquisition cash flows in the scope of PFRS 17 'Insurance Contracts'. <p>PAS 36 does apply to:</p> <ul style="list-style-type: none"> • financial assets classified as subsidiaries, associates and joint ventures (unless measured at fair value) • property, plant and equipment and intangible assets carried at a revalued amount in accordance with other PFRS, and • Right-of-use assets measured in accordance with PFRS 16 'Leases'.
Key definitions	<p>PAS 36 defines key terms that are essential to understanding its guidance including, but not limited to:</p> <ul style="list-style-type: none"> • CGU • corporate assets • costs of disposal • impairment loss • recoverable amount • VIU, and • FVL COD.

Area of PAS 36	Requirement
Identifying an asset that may be impaired	<p>PAS 36 prescribes the timing requirements for performing quantitative impairment testing as well as potential ‘indicators’ of impairment that may trigger impairment testing for some assets or groups of assets. Specifically, PAS 36 requires that:</p> <ul style="list-style-type: none"> • goodwill, indefinite life intangibles and intangible assets not yet available for use are tested for impairment at least annually, in addition to when there is any indication of impairment, and • all other assets are tested for impairment when there is any indication that the asset may be impaired. <p>PAS 36 also outlines some limited exceptions to the requirements noted above.</p>
Level of review (individual asset or group of assets)	<p>PAS 36 prescribes the level of review for impairment:</p> <ul style="list-style-type: none"> • where possible, an entity will estimate the recoverable amount of an individual asset, or • when this is not possible, an entity will determine the recoverable amount of the CGU to which an asset belongs. <p>For the purposes of impairment testing, PAS 36 prescribes how to allocate goodwill and corporate assets to CGUs.</p>
Measuring recoverable amount	<p>When an entity needs to test an asset or CGU for impairment, it must determine its recoverable amount. PAS 36 defines the recoverable amount as the higher of the asset’s or CGU’s FVL COD and VIU.</p>
FVL COD	<p>PAS 36 provides guidance to determine FVL COD including:</p> <ul style="list-style-type: none"> • providing examples of ‘costs of disposal’ and items that do not meet that definition, and • outlining situations where it may be necessary to consider some recognized liabilities to determine the recoverable amount.
VIU	<p>PAS 36 prescribes the elements that should be reflected in the calculation of an asset’s or CGU’s VIU including:</p> <ul style="list-style-type: none"> • 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 • 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. <p>The guidance provides additional considerations in determining an appropriate estimate/rate for each of the above elements.</p>
Recognizing an impairment loss	<p>PAS 36 requires an entity to recognize an impairment loss when the carrying amount of an asset or CGU exceeds its recoverable amount, and provides guidance on how to recognize that loss, by outlining:</p> <ul style="list-style-type: none"> • the requirements for recognizing and measuring impairment losses for an individual asset • the requirements for allocating losses when such losses are calculated for a CGU, and • additional considerations for allocating an impairment loss when there is a non-controlling interest.

Area of PAS 36	Requirement
Reversing an impairment loss	<p>PAS 36 sets out the requirements for reversing an impairment loss recognized for an asset or CGU in prior periods by:</p> <ul style="list-style-type: none"> • prescribing timing for assessment • providing indicators that an impairment loss recognized in prior periods for an asset (other than goodwill) or CGU may no longer exist or may have decreased, and • prescribing the accounting for reversing a prior impairment loss, including limitations on the amount that can be reversed.
Disclosures	<p>PAS 36 sets out the disclosure requirements related to impairment. Some disclosures apply in the event an entity records an impairment loss while others are required irrespective of any impairment loss.</p>

PAS 36's step by step impairment approach

PAS 36 prescribes the procedures that an entity applies to ensure that assets are carried at no more than their recoverable amounts (the impairment review). Very broadly, the impairment review comprises:

- an assessment phase, and
- a testing phase, if required.

Assessment phase	What?	Identifying assets within the scope of PAS 36 and determining the structure of the impairment review (scope and structure).
	If and when?	Determining if an impairment test is required and if so, when.
Testing phase	How?	If required, understanding how to estimate the recoverable amount, compare the recoverable amount to the carrying amount, and recognize or reverse any impairment loss (the reversal of goodwill impairment loss is not allowed).

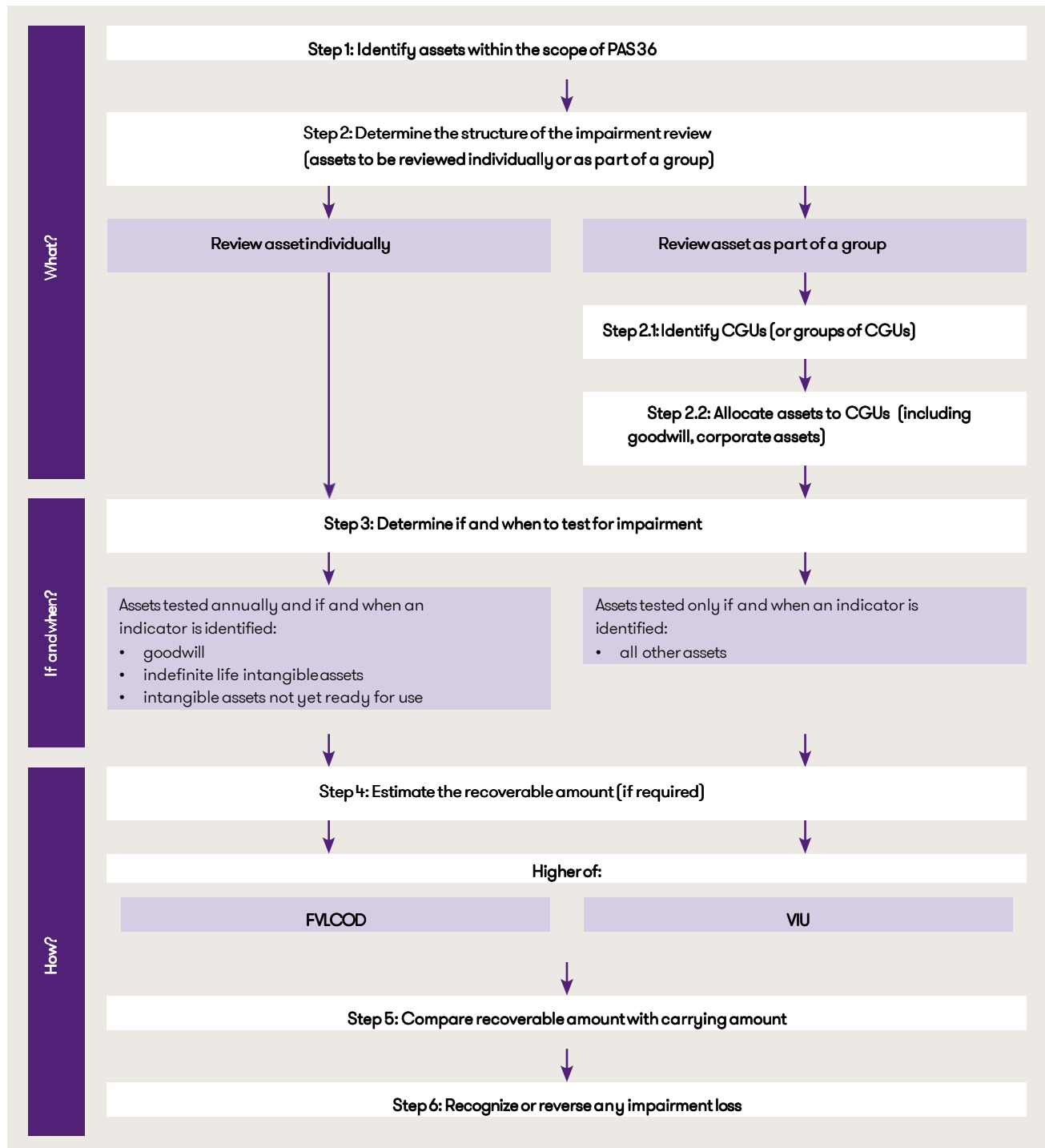
We use the phrase 'impairment review' to encompass both the assessment and testing phase. In the assessment phase management:

- identifies the assets within the scope of PAS 36
- identifies the assets for which a quantified impairment test is required. Goodwill, indefinite life intangibles and those not available for use are tested at least annually, even if there is no indication they might be impaired. Other assets are assessed and are tested only if one or more indicators are identified
- determines which assets will be tested individually and which as part of a CGU or group of CGUs, and identifies the CGUs to which assets belong (we refer to this as the 'structure' of the impairment review). PAS 36 requires that an entity tests individual assets wherever possible; however, it is usually not possible to determine the recoverable amount for an individual asset. As a result, more times than not, management must identify the CGU (or groups of CGUs) to which the individual asset relates. Additionally, management must allocate goodwill and corporate assets to a CGU (or groups of CGUs) for the purpose of applying PAS 36.

These steps determine the scope of the quantified impairment testing (the testing phase). In the testing phase, management:

- estimates the recoverable amount for the assets and CGUs as required
- compares the recoverable amount to the carrying amount, and
- records (or reverses, if applicable) any impairment loss, to the individual assets, or allocated among the assets in impaired CGUs in accordance with PAS 36's guidance.

With this in mind, the following step-by-step guide is useful in applying PAS 36:



How we can help

We hope you find the information in this article helpful in giving you some insight into PAS36. If you would like to discuss any of the points raised, please speak to your usual P&A Grant Thornton contact or visit www.grantthornton.com.ph/Contact



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