INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS OF KENYA

Asset Impairment Workshop

16th July to 17th July

Session Two: Impairment Testing

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3. Other aspects of impairment testing (9- Step testing pyramid)
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1. Introduction

When assets are shown in the Statement of Financial Position, it is assumed that they will be recovered(apart from cash which is already recovered and receivables which is on the way to recovery). Generally recovery is from selling or using the asset.

1. Introduction

As an application of the prudence concept, it is recommended that assets should not be carried in the books at a value that will not be recovered.

The purpose of impairment testing is to ensure that assets are presented at reasonable amounts.

1. Introduction

Different standards prescribe the valuation of assets and the standards indicate situations where assets have lost value.

The purpose of this section is to discuss impairment of some assets like Property, plant and equipment, intangibles and goodwill.

2. IAS 36: Requirments

2.1 Scope of IAS 36

All assets except:

Inventories, construction contracts, deferred tax assets, employee benefits, financial assets, investment property,

biological assets, insurance contract assets, and assets held for sale.

2. IAS 36: Requirments

2.2 Recognition of Impairment Loss

Generally an impairment loss arises when the Carrying amount (Value for Accounting purpose), is greater than recoverable amount.

Recoverable amount is the higher of Fair Value less costs to sell and Value in use

2. IAS 36: Requirments

2.3 Recognition of Impairment Loss

Impairment losses are recognized at TWO levels.

(i) An individual asset – Treat an impairment loss as a revaluation loss and charge to Profit or loss after reversing any revaluation gain if any.

2. IAS 36: Requirments

2.3 Recognition of Impairment Loss

(ii) Cash Generating Unit (CGU) – A group of assets used together like a branch or subsidiary. Allocate impairment loss to goodwill first and then prorate to the book value of other assets but do not reduce an asset below realizable value or zero.

2. IAS 36: Requirments

2.3 Recognition of Impairment Loss

An impairment review should be carried out (Check assets for impairment) at each reporting period and when there is an indication of impairment.

Indicators of impairment include:

2. IAS 36: Requirments

Internal indicators:

a)Evidence of obsolescence or physical damage

b) Discontinuance, disposal or restructuring plans

c) Declining asset performance.

2. IAS 36: Requirments

External indicators:

a) Significant decline in market value

b) Changes in technological, market, economic or legal environment

c) Changes in interest rates

d) Low market capitalization.

2. IAS 36: Requirments

Measuring Impairment losses:

As stated before:

If carrying amount > Recoverable amount, the difference is an impairment loss.

2. IAS 36: Requirments

Recoverable amount is the higher of Fair value less costs to sell (FVLCS) and Value in Use (VIU).

Fair Value = Market price or price from a binding agreement.

Value in use = Present value of net cash flows from using the asset. (Use cash from use and disposal and WACC)

2. IAS 36: Requirements

For a CGU, (a group of assets):

Compute and report impairment loss after allocating:

1. **Its share of goodwill if we have several CGU's and**
2. **Corporate assets (i.e. assets used in head office)**

2. IAS 36: Requirements

2.3 Can you reverse a previously reported impairment loss?

Yes, if both internal and external factors have improved. You can restate the value of the asset and report an income in the profit or loss.

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2. IAS 36: Requirements

However two restrictions:

1. **Once goodwill is impaired you cannot restate it. (This will be like creating an internally generated goodwill).**
2. **The new carrying amount should not be higher than what it would have been if no impairment loss had been reported.**

3. Other issues

Previously, under the 9 step model of impairment testing, the above concepts were combined such that both specific asset and CGU were analyzed under a framework. This is no longer applicable and we just talk of a 2- Step model for Specific asset and maybe a 4-step model for CGUs. (Can ignore).