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Insights into MFRS 136

Overview of the Standard

MFRS 136 '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 MFRS 136's guidance is detailed, prescriptive and complex in some areas.

The articles in our 'Insights into MFRS 136' 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 MFRS 136, and revisit some areas where confusion has been seen in practice.

This article provides an 'at a glance' overview of MFRS 136's main requirements and outlines the major steps in applying those requirements.

Objective of MFRS 136

The objective of MFRS 136 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, MFRS 136 provides guidance on:

- the level at which to review for impairment (eg 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 recognise 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).

MFRS 136 Key definitions

MFRS 136 defines key terms that are essential to understanding its guidance. The most significant definitions are highlighted in below:

Carrying amount	Impairment loss	Recoverable amount	Value in use
The amount at which an asset is recognised after deducting any accumulated depreciation (amortisation) 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 (FVLCOD) 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 MFRS 136's main requirements:

Area of MFRS 136	Requirement
Principle	The overall principle in MFRS 136 is that assets should not be carried above their recoverable amount.
Scope	MFRS 136 applies to all assets other than those for which the measurement requirements of other MFRS are such that an MFRS 136-based impairment review is irrelevant or unnecessary. Assets outside MFRS 136's scope include: • inventories • financial assets in the scope of MFRS 9 'Financial Instruments' • contract assets and assets arising from costs to obtain or fulfill a contract recognised in accordance with MFRS 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 MFRS 141 '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 MFRS 17 'Insurance Contracts'. MFRS 136 does apply to: • 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 IFRS, and • Right-of-use assets measured in accordance with MFRS 16 'Leases'.
Key definitions	MFRS 136 defines key terms that are essential to understanding its guidance including, but not limited to: • CGU • corporate assets • costs of disposal • impairment loss • recoverable amount • VIU, and • FVLCOD.

Area of MFRS 136	Requirement
Identifying an asset that may be impaired	MFRS 136 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, MFRS 136 requires that: • 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. MFRS 136 also outlines some limited exceptions to the requirements noted above.
Level of review (individual asset or group of assets)	MFRS 136 prescribes the level of review for impairment: • 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. For the purposes of impairment testing, MFRS 136 prescribes how to allocate goodwill and coroporate assets to CGUs.
Measuring recoverable amount	When an entity needs to test an asset or CGU for impairment, it must determine its recoverable amount. MFRS 136 defines the recoverable amount as the higher of the asset's or CGU's FVLCOD and VIU.
FVLCOD	MFRS 136 provides guidance to determine FVLCOD including: • 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 recognised liabilities to determine the recoverable amount.
VIU	MFRS 136 prescribes the elements that should be reflected in the calculation of an asset's or CGU's VIU including: • 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. The guidance provides additional considerations in determining an appropriate estimate/rate for each of the above elements.
Recognising an impairment loss	MFRS 136 requires an entity to recognise an impairment loss when the carrying amount of an asset or CGU exceeds its recoverable amount, and provides guidance on how to recognise that loss, by outlining: • the requirements for recognising 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 MFRS 136	Requirement
Reversing an impairment loss	MFRS 136 sets out the requirements for reversing an impairment loss recognised for an asset or CGU in prior periods by: • prescribing timing for assessment • providing indicators that an impairment loss recognised 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	MFRS 136 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.

MFRS 136's step by step impairment approach

MFRS 136 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 MFRS 136 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 recognise or reverse any impairment loss (the reversal of goodwill impairment loss is not allowed).

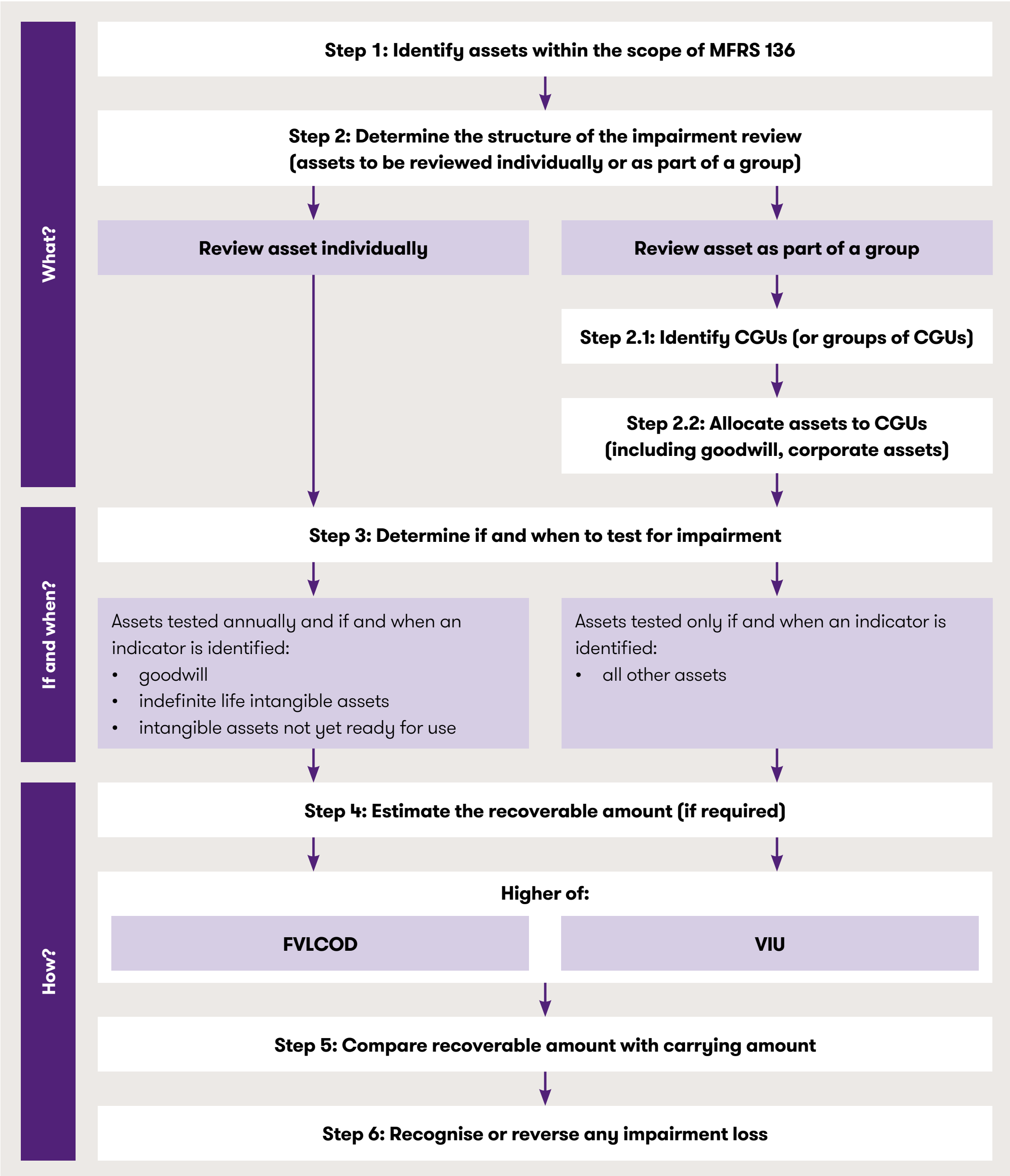
We use the phrase 'impairment review' to encompass both the assessment and testing phase. In the assessment phase management:

- identifies the assets within the scope of MFRS 136
- 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). MFRS 136 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 MFRS 136.

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 MFRS 136's guidance.

With this in mind, the following step-by-step guide is useful in applying MFRS 136:



How we can help

We hope you find the information in this article helpful in giving you some insight into MFRS 136. If you would like to discuss any of the points raised, please speak to your usual Grant Thornton contact.

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