Key disclosures under AASB 136 *Impairment of Assets*

May 2020

Disclosures in the financial statements are the way you express your consideration and thought processes throughout the journey of testing for impairment. The disclosures tell your story.

Disclosure of key assumptions: focus for regulators

Disclosure of the key assumptions used in cash flow forecasts for impairment testing is a focus for regulators. Regulators have emphasised that more granular disclosures are needed, instead of the often aggregated disclosures showing wide ranges and grouping CGUs. The view expressed by many regulators is that, whilst the growth rate used to extrapolate cash flow projections and the pre-tax discount rate are important, they are not the 'key assumptions' that the cash flow projections are based upon. Rather, the growth rate and discount rate are applied to those cash flow projections after they have been prepared.

AASB 136 includes disclosure requirements for the growth and discount rates separately from (and in addition to) each key assumption on which the cash flow projections are based. In this context, the regulators' view is that a reference to 'growth' is meaningless unless the item is identified – for example, as sales, margins or costs. This is likely to remain an area that is subject to scrutiny for groups with large amounts of goodwill or indefinite-lived intangible assets on the balance sheet.

Disclosures are split between CGUs where an impairment has been recognised and CGUs with goodwill or indefinite-lived assets allocated to them. The amount of impairment recorded or reversed must be disclosed, including the circumstances leading to that impairment or reversal. The recoverable amount methodology must also be disclosed.

What to think about this reporting season

Determine and probability weight your possible scenarios

In considering the potential outlook for each CGU and the specific impacts of COVID-19, you should consider a **range of possible scenarios** and apply a **probability weighting** to each of these in order to determine an estimation of future cash flows which has an **appropriate basis.**

For each scenario, consider the:

- trajectory and depth of the downturn
- duration of downturn/demand reduction
- trajectory and extent of recovery

You should also consider the impact that these assumptions would have on other factors of your business, including:

- going concern assumptions
- funding requirements over the short, medium and long term
- debt covenants

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Impairment disclosure requirements

AASB 136 requires an entity to disclosure the following for each class of assets:

a. the amount of impairment losses recognised;
b. the amount of reversals of impairment losses;
c. the amount of impairment losses on revalued assets recognised in other comprehensive income during the period.
d. the amount of reversals of impairment losses on revalued assets recognised in other comprehensive income during the period.

Where an impairment loss is recognised or reversed for an individual asset (including goodwill) or CGU, an entity shall disclose:

1. the events and circumstances that led to the recognition or reversal of the impairment loss;
2. the amount of the impairment loss recognised or reversed;
3. for an individual asset:
   a. the nature of the asset; and
   b. if the entity reports segment information, reportable segment to which the asset belongs (AASB 8);
4. for a CGU:
   c. a description of the CGU;
   d. the amount of the impairment loss recognised or reversed
   e. if the aggregation of assets for identifying the CGU has changed, the entity should describe the current and former method of aggregating assets and the reasons for change.
5. the recoverable amount of the asset and whether the recoverable amount of the asset or CGU is its fair value less costs to sell or its value in use;

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6. if the recoverable amount is fair value less costs of disposal, disclose: a. The level of the fair value hierarchy within which the fair value measurement of the asset b. For fair value measurements categorised within Level 2 and Level 3 of the fair value hierarchy, a description of the valuation technique(s) used to measure fair value less costs of disposal; c. If there has been a change in valuation technique, the change and the reasons for making it; d. For fair value measurements categorised within Level 2 and Level 3 of the fair value hierarchy, each key assumption on which management has based its determination of fair value less costs of disposal; and e. The discount rate(s) used in the current measurement and previous measurement if fair value less costs of disposal is measured used a present value technique.	6. if the recoverable amount is value in use, the discount rates used in current estimate and previous estimate (if any) of value in use.

Estimates used to measure recoverable amounts of CGUs containing goodwill or intangible assets with indefinite useful lives

AASB 136 requires an entity to disclose the following for each CGU for which the carrying amount of goodwill or intangible assets is significant in comparison with the total carrying amount of the goodwill or intangible assets:

a. the carrying amount of goodwill allocated to the unit (group of units);

b. the carrying amount of intangible assets with indefinite useful lives allocated to the unit (group of units);

c. the basis on which the unit's (group of units') recoverable amount has been determined (i.e. value in use or fair value less costs of disposal);

d. if the unit's (group of units') recoverable amount is based on **value in use**:

   i. each key assumption on which management has based its cash flow projections for the period covered by the most recent budgets/forecasts.

   ii. a description of management's approach to determining the value(s) assigned to each key assumption

   iii. the period over which management has projected cash flows based on financial budgets/forecasts approved by management and, when a period greater than five years is used for a cash-generating unit (group of units), an explanation of why that longer period is justified.

   iv. the growth rate used `to extrapolate cash flow projections

   v. the discount rate(s) applied to the cash flow projections.

e. if the unit's (group of units') recoverable amount is based on fair value less costs of disposal, the valuation technique(s) used to measure **fair value less costs of disposal.**

For more details on disclosures, refer to AASB 136 paragraph 126 to 137 Compiled AASB 136 (Dec 2016)

TIP: It is our experience that the regulator has a significant focus on whether companies' assumptions compare favourably to external and independent data, such as industry growth rates. For each scenario, the specific assumptions applied should be sufficiently documented and, where possible, give greater weight to external information available at the time of finalising your estimated future cash flows. It is important to consider events and information that become available after year end and before reporting date to consider whether or not impairment testing should be updated for this new information..

Regulator focus and other considerations

AASB 136 includes specific disclosure requirements for the growth and discounts rates separately from (and in addition to) each key assumption on which the cash flow projections are based. In this context, the regulators' view is that a reference to 'growth' is meaningless unless the item is identified – for example, as sales, margins or costs. This is likely to remain an area that is subject to scrutiny for groups with large amounts of goodwill or indefinite-lived intangible assets on the balance sheet.

The key assumptions, judgments and estimates involved in impairment calculations are often significant and therefore should be disclosed. Regulators have emphasised a need for more granular disclosures instead of showing wide ranges of key assumptions.

Disclosure considerations

Given the rapidly evolving and highly uncertain situation surrounding the coronavirus pandemic, management is required to exercise significant judgement to assert reasonable and supportable assumptions which reflect the conditions existing at the impairment testing date. The majority of these assumptions are likely to be subject to significant uncertainties.

As such, management should consider providing detailed disclosures of those significant uncertainties and the rationale adopted in the significant judgements made to determine impairment valuation outcomes.

Your disclosures should include:

- the various scenarios considered or modelled
- probability weightings for each scenario
- key risks to forecast cash flows
- sensitivities related to those key risks
- key cash flow assumptions and, in particular, any assumptions based on external sources

For a CGU or asset with no impairment where a reasonably possible change in a key assumption would result in an impairment, you should disclose:

- the available headroom
- the quantum of the change in the key assumption needed to eliminate the available headroom

Although not issued as a guide for impairment related disclosures, **Regulatory Guide 170 – Prospective financial information** does provide helpful guidance on the disclosure of key assumptions underlying forward looking information. For example:

- RG170.61: "...assumptions about expenditures, revenues, inflation rates and other such variables should be clearly disclosed…"
- RG170.62: "Investors must be able to assess...the validity of the assumptions…the likelihood of the assumptions actually occurring...the effect…if the assumptions vary."
- RG170.63: "...disclose material assumptions about specific future economic conditions and particular circumstances affecting a company…"
- RG170.66: "It is not sufficient to state the general nature of an assumption. Specific quantities or amounts should be set out."

Illustrative disclosures

The following section aims to demonstrate how some companies have achieved the required disclosures of the accounting standards giving consideration to regulator focus.

These examples are not definitive and should not be used as boilerplate disclosures. While these disclosures are good examples of meeting the requirements of the standard, management should continue to review AASB 136 and latest guidance issued by their Auditors to ensure they are meeting the disclosures for the current reporting season.

Example disclosure from Value Accounts 31 December 2019

https://www.pwc.com.au/ifrs/value-accounts.html

Current publications include:

- Value Accounting Holdings December 2019
- Value Account Holdings Interim Financial Reporting June 2020
- Value Accounts Reduced Disclosure- December 2019
- Value Accounts Simplified Disclosure Summary 2020
- Value Accounts Superannuation Funds 2019
- Value Accounts Investment Funds 2020

Integrated tests for goodwill

(iv) Impairment tests for goodwill

Goodwill is monitored by management at the level of the six operating segments identified in note 2.

A segment-level summary of the goodwill allocation is presented below:

2019	Australia $'000	US $'000	China $'000	Europe $'000	Total $'000
IT consulting	-	4,200	-	2,870	7,070
Furniture manufacturing and wholesale	120	-	-	-	120
Electronic equipment	1,115	-	-	-	1,115
	1,235	4,200	-	2,870	8,305

2018	Australia $'000	US $'000	China $'000	Europe $'000	Total $'000
IT consulting	-	4,200	-	3,015	7,215
Furniture manufacturing and wholesale	120	-	2,410	-	2,530
	120	4,200	2,410	3,015	9,745

(v) Significant estimate: key assumptions used for value-in-use calculations [97]

The group tests whether goodwill has suffered any impairment on an annual basis. For the 2019 and 2018 reporting periods, the recoverable amount of the cash-generating units (CGUs) was determined based on value-in-use calculations which require the use of assumptions. The calculations use cash flow projections based on financial budgets approved by management covering a five-year period.

Cash flows beyond the five-year period are extrapolated using the estimated growth rates stated below. These growth rates are consistent with forecasts included in industry reports specific to the industry in which each CGU operates.

(d) Intangible assets

The following table sets out the key assumptions for those CGUs that have significant goodwill allocated to them: [11,12]

2019	Furniture manufacturing and wholesale China	IT consulting US	IT consulting Europe	Electronic equipment Australia
Sales volume (% annual growth rate)	**2.7**	**3.2**	**4.1**	**2.9**
Sales price (% annual growth rate)	**1.4**	**1.7**	**1.8**	**1.8**
Budgeted gross margin (%)	**47.0**	**60.0**	**55.5**	**40.0**
Other operating costs ($'000)	**9,500**	**8,400**	**5,600**	**1,650**
Annual capital expenditure ($'000)	**1,900**	**500**	**230**	**150**
Long-term growth rate (%)	**3.5**	**2.2**	**2.0**	**3.1**
Pre-tax discount rate (%)	**14.7**	**14.0**	**14.8**	**16.0**
2018				
Sales volume (% annual growth rate)	2.5	3.0	3.9	-
Sales price (% annual growth rate)	1.3	1.6	1.8	-
Budgeted gross margin (%)	44.0	60.0	54.0	-
Other operating costs ($'000)	9,300	8,300	4,350	-
Annual capital expenditure ($'000)	1,850	580	225	-
Long-term growth rate (%)	3.2	2.2	1.8	-
Pre-tax discount rate (%)	14.3	14.4	15.1	-

Management has determined the values assigned to each of the above key assumptions as follows:

Assumption	Approach used to determining values
Sales volume	Average annual growth rate over the five-year forecast period; based on past performance and management's expectations of market development.
Sales price	Average annual growth rate over the five-year forecast period; based on current industry trends and including long-term inflation forecasts for each territory.
Budgeted gross margin	Based on past performance and management's expectations for the future.
Other operating costs	Fixed costs of the CGUs, which do not vary significantly with sales volumes or prices. Management forecasts these costs based on the current structure of the business, adjusting for inflationary increases but not reflecting any future restructurings or cost-saving measures. The amounts disclosed above are the average operating costs for the five-year forecast period.
Annual capital expenditure	Expected cash costs in the CGUs. This is based on the historical experience of management, and the planned refurbishment expenditure. No incremental revenue or cost savings are assumed in the value-in-use model as a result of this expenditure.
Long-term growth rate	This is the weighted average growth rate used to extrapolate cash flows beyond the budget period. The rates are consistent with forecasts included in industry reports.
Pre-tax discount rates	Reflect specific risks relating to the relevant segments and the countries in which they operate.

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