IAS 36: Impairment of Assets Review

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In an increasingly dynamic and complex world of financial reporting, transparency and accuracy are of utmost importance. Investors, stakeholders, and regulatory bodies rely heavily on financial statements to make informed decisions. Among the various accounting standards that govern financial reporting, IAS 36 *Impairment of Assets* stands out as a critical guideline. This standard helps to ensure that assets are fairly presented on the statement of financial position, reflecting their true economic value.

Understanding IAS 36:

IAS 36 *Impairment of Assets*, outlines the procedures to recognise, calculate and assess if there is an impairment. It also prescribes the treatment in the event that an asset; now impaired has been previously revalued.

IAS 36 *Impairment of Assets* suggests that an asset is impaired when its carrying amount (net book value) exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use.

Importance of Impairment Review:

1. Accurate Asset Valuation: The primary objective of IAS 36 is to ensure that assets are recorded at their recoverable amounts, preventing overstatement of asset values on the statement of financial position.

   By conducting impairment reviews, companies can provide a more accurate reflection of their financial position to stakeholders.

2. Timely Identification of Impairments: Regular impairment reviews enable businesses to promptly identify any declines in the value of their assets. This proactive approach helps in mitigating potential losses and allows for strategic decision-making regarding asset management and disposal.

3. **Enhanced Transparency and Disclosure:** Compliance with IAS 36 requires companies to disclose information regarding the assumptions and methodologies used in impairment assessments. This transparency promotes investor confidence and trust in financial reporting.

4. **Risk Management:** Effective impairment reviews play a crucial role in risk management. By assessing the recoverability of assets, companies can identify areas of concern and take appropriate measures to mitigate risks associated with asset depreciation or obsolescence.

5. **Legal and Regulatory Compliance:** Adhering to IAS 36 is not just a matter of good practice; it is a legal and regulatory requirement in many jurisdictions. Failure to comply with impairment testing obligations can lead to legal repercussions and damage the reputation of the company.

Challenges and Considerations:

Despite its importance, conducting impairment reviews can be challenging for businesses. Factors such as determining appropriate discount rates, estimating future cash flows, and assessing market conditions require careful consideration. Moreover, the subjective nature of impairment assessments may introduce complexities and uncertainties into the process.

Furthermore, the impact of external events, such as economic downturns or changes in market conditions, can significantly influence impairment outcomes. Companies must remain vigilant and adaptable in responding to these external factors to ensure the reliability of their impairment assessments.

Indicators of impairment:

Where the is evidence, either internal or external, of an impairment, an impairment review should be carried out.

Step 1

Calculate / confirm the recoverable amount. This can be done by way of engaging experts from the field. For instance, if an entity were concerned about the recoverable value of their buildings, they would contact commercial estate agents.

Step 2

The asset should be written down to is recoverable amount, less costs to sell, with an impairment loss being recognised for the full difference in the statement of profit or loss.

The only exception to this is if the asset has been previously revalued and a gain taken to revaluation surplus. In this case the revaluation surplus entry is reversed up to and including the full amount of the revalued amounts. If this is insufficient, then a loss must be taken to the statemen of profit or loss at this time. Below is an example of an impairment where an asset has previously revalued upward with a final impairment loss needing to be recorded in the Statement of Profit or Loss.

Example:

An entity owns a property that was revalued to €1,500,000 on 30 September 2021 with a revaluation gain of €650,000 being recognised as other comprehensive income and recorded in the revaluation reserve. This company does not make a transfer from revaluation surplus to offset higher depreciation charges to the statement of profit or loss.

At 30 September 2023, the property had a carrying amount of €1,380,000 but a reasonable value has been established at €625,000 less €25,000 worth of advertising and agency fees.

The recoverable amount of the property is therefore €600,000 (€625,000 - €25,000).

Solution:

Impairment = €1,380,000– €600,000 = €780,000

Of this €650,000 is debited to the revaluation reserve to reverse the previous upward revaluation (and recorded as other comprehensive income) and the remaining €130,000 is charged to the statement of profit or loss.

Conclusion:

In conclusion, IAS 36 Impairment of Assets plays a pivotal role in financial reporting by ensuring the accurate valuation of assets and promoting transparency and accountability. By conducting regular impairment reviews, companies can mitigate risks, enhance decision-making, and maintain compliance with regulatory requirements. While challenges may exist, the benefits of adhering to IAS 36 far outweigh the complexities involved. As businesses navigate the ever-changing landscape of financial reporting, a thorough understanding of IAS 36 and its implications is essential for fostering trust and confidence among stakeholders.