THEORETICAL AND PRACTICAL ASPECTS REGARDING THE IAS-36 APPLICATION TO “THE IMPAIRMENT OF ASSETS” TO C.E. OLTENIA

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ABSTRACT
The main characteristics of the assets are the incorporated economic benefits, the way in which these may enter in the patrimony and the derivation of the assets from previous events or transactions. In 1998 IASC Council approved the IAS – 36 percept, “the Impairment of assets”, that imposes the estimation and accounting of the loss of value for an asset, when the recoverable amount of this is inferior to its book value. The objective of this standard is to set the proceedings, which an enterprise applies in order to assure that its assets are accounting to a less or equal value with their recoverable value.

Introduction
An asset is accounted at a bigger value than its recoverable value, if its book value exceeds the amount which is to be recoverable by selling or using this asset. In this situation, the asset considered recoverable and according to this standard, some losses of appreciation are imposed to be recognised. At the end of each reporting period, the enterprise must estimate if there are indexes of the impairment of assets. If such indexes are identified, the enterprise is obliged to estimate the recoverable value of the asset. An asset is recognised in the balance sheet, in the moment in which it is likely the achievement of a future economic benefit by the enterprise and the asset has a cost or a value which may be evaluated in a credible way.

The book value is the value at which an asset is registered in the balance sheet, after the deducing of the depreciations amount and value losses. The value in use is the cash flow obtained through the estimation of the future treasury flows expected from the continuous use of an asset and from its cession at the end of its period use. The recoverable value is the bigger value between the net price of selling of the asset and its value in use.

The reversion of a value loss of an asset must be accounted on revenue accounts, in the profit and loss account, excepting the situation in which the asset would have been accounted at a revaluated size. A loss of book value for an asset during the previous exercises, must be decreased if it has taken place a change in the estimations used, in order to determine the recoverable amount of the asset, from the latest registration in the accounting of a loss value. In this case, the book value of the asset must be increased at the level of its recoverable amount.

The calculation of value in use should reflect the following elements:
- the estimation of the future cash flows, which the enterprise expects to derive from that asset;
- expectations about possible variations in the amount or timing of those future treasury cash flows
- the time value of money, represented by the current market risk-free rate of interest
- the price for bearing the uncertainty inherent in the asset
- 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 estimation of future cash inflows and outflows, generated by the continuous use of the asset and its cession.

The IAS-36 “Impairment of assets” combines the requests regarding the classification, evaluation, identification, recognition and reversion of a loss in the impairment of a single standard, assuring the performance of these requirements. The accounting treatment, according to this standard regarding the impairments of an asset is encountered both to the assets registered on the evaluation model at historic cost and also for the assets observed on the basis of fair value model.

In the first case, the recognition and derecognition of the impairment affect the profit and loss account, by affecting impairment expense categories of assets (recognition), respectively income (derecognition). The income
registration or the reversion of an impairment loss is limited, so the asset may not exceed the level of the impairment cost of acquisition. If it is found an increase of the assets value over the limit, it comes out from the scope of IAS – 36 “the Impairment of capital assets”.

This may register only according to IAS -16 “Tangible assets”, using the fair value model IAS -36 “the Impairment assets”. The identification and evaluation of the impairment losses make the difference between individual assets and cash – generating units. It is among the fewer international accounting standards, which deals with the problem of synergy in the use of a group of assets.

The IAS-36 “the Impairment of assets” requirements do not lead to recognition of the fair value of the cash-generating units, only if it has been registered the recognition of the assets, namely impairment. The requirements of this accounting standard create the necessary theoretical basis for treating the assets combinations under the valuation aspect, but in a negative way, because the generated values are not recognized, a limit of the cost of acquisition model being corrected, while a limit of the fair value model is created. The IAS -36 Impairment of assets do not apply to assets stocks which result from the construction contracts, claims regarding the deferred tax or to the assets classified from the benefits of the employees or the assets classified as held for selling, because the IFRS of these assets have availabilities regarding the recognition and evaluation of these assets.

This accounting standard applies also to some financial assets, considered branches, associated entities.

According to this accounting standard, at the end of each financial reporting period, the business enterprises must estimate if there are indexes of the impairment of the assets. If there are such indexes, this must estimate the recoverable amount of the asset.

An entity must present the following information for each class assets:
- the value of the impairment losses recognised in the profit or loss period, and also the line of the comprehensive income in which those impairment losses are included;
- the value of the reversion of the impairment losses recognised in the profit or loss period, and also the line (items – lines) of the comprehensive income in which those impairment losses are reversed;
- the value of the impairment losses revaluated, losses recognised in other items of the comprehensive income during the period;
- the value of the reversion of the impairment losses recognised in other items of the comprehensive income.

When there are any kinds of indexes that an asset item may be assessed for impairment, the recoverable amount must be estimated for that individual asset. If is not possible the estimation of the recoverable amount of an individual asset, the business enterprise must calculate the recoverable amount for the cash – generating unit to which the asset belongs.

The recoverable amount of an individual asset may be determined in the following conditions:
- the value in use of the asset may not be estimated as appropriate to the fair value minus the costs of sale;
- the asset does not generate cash inflows that are independent from those generated by other assets.

In such situations, the value in use and also the recoverable amount may be calculated only for the cash – generating unit of the asset (1805).

If there is an active market for the production of an asset or group of assets, that asset or group of assets must be identified as cash – generating unit, even if a part or the entire production is used for own. If the cash inflows generated by an asset or cash – generating unit are affected by the internal prices, the entity must make use of the best estimation of the management, regarding the prices that may be obtained in the case of a transaction developed in objective conditions in order to estimate:
- the future cash inflows used for determining the value in use of the asset or cash – generating unit;
- the future cash outflows used for determining the value in use of any asset or cash – generating unit affected by the internal transfer price.

The cash-generating units must be identified after the same rules, from one period to another, for the same asset or the same kinds of assets, except for the cases when a change must be made.

The recoverable amount of a cash-generating unit is the bigger value between the fair value minus costs of sale and its value in use.

The book value of a cash-generating unit must be determined on the basis of the same criteria used for the determination of the recoverable amount of the cash-generating unit.

The book value of a cash-generating unit includes:
- only the book value of those assets that may be distributed directly or reasonably allocated to the cash-generating unit and that will generate the future cash inflows used to the determination of the cash-generating unit value in use and;
- does not include the book value of any unknown debt, excepting the situations in which the recoverable amount of the cash-generating unit may not be determined without taking into account this debt. This is taken into account because the fair value minus sale costs and the cash-generating unit value in use are determined by
excluding the treasury cash flows which are linked to the assets that are not part from the cash-generating unit and from the debts that had been recognised.

At the end of each reporting period, an entity must evaluate the existence of the reducing or cancelling indexes of an impairment loss recognised in the anterior periods for an asset, another than the goodwill. If there is such an index, the entity must estimate the recoverable amount of this asset.

In assessing the presence or absence of an index that an impairment loss recognised in the anterior periods for other asset than the goodwill, may no longer exist or has decreased an entity must take into account at least the following indexes:

- external source of information
- internal source of information.

The external sources of information include:
- the market value of the asset has increased significantly during the period
- during the period, significant changes with a favourable effect on the entity occurred, or such changes will occur in the near future over the technological, commercial, economic and legal environment, where the entity develops its activity or on the market, where the asset is dedicated to;
- the interest rates on the market or other market rates of the return on the investments have decreased during the period, being probable that these growths to affect the discount rate used in the calculation of an asset value in use and to determine the growth of the asset recoverable amount.

The internal sources include:
- during the period significant changes with a favourable effect on the entity occurred, or such changes will occur in the near future regarding the degree or manner in which the asset is used or is expected to be used. These changes include the costs from the period in order to improve and strengthen the asset performance or to reorganize the activity of the asset;
- the internal reports provide evidences that indicate the fact that the economic performance of an asset is or will be better than it has provided initially.

1st example

C.E. Oltenia has surface mining in Moldova, and after the depletion of coal deposits, is obliged to restore its emplacement. The restoration costs include the extracted soil replacement before the excavation of the coal seam. The provision for the costs of replacement of excavated soil was recognised soon as the stripping operations had begun. That amount was recognised as part of the mine costs and is depleted during the useful life of the mine. The book value of the provision for the restoration costs is 500,000 Euro, which is equal with the discounted value of the restoration costs.

C.E. Oltenia applies the impairment test mine, considering that treasury-generating unit is the mining as a whole. C.E. Oltenia has received many offers to purchase of the mine at about 800,000 Euro, taking into account that it is exploited inferior coal.

This price reflects the fact that the acquirer will assume the obligation to restore the emplacement. The disposal mine costs are very low and refer to the documentation for sale and purchase, taxes and local charges. The mine value in use is about 1,200,000 Euro, only the restoration costs, and then the mine book value is 1,000,000 Euro.

The fair value minus the costs generated by the purchasing of the cash-generating unit is 800,000 Euro. This amount takes into account the restoration costs, already calculated. Consequently, the mine value in use is determined after taking into account of the restoration costs and is about 700,000 Euro (1,200,000 – 500,000 Euro). The mine book value is 500,000 Euro, namely the mine book value (1,000,000 Euro) minus the provision book value for restoration costs (500,000 Euro). In conclusion, the mine recoverable amount exceeds its book value.

2nd example

C.E. Oltenia has a mill for crushing coal to the return head of a coal transport tape, which works, but not at maximum. We mention that the mining machineries may work without this mill. It has the role to grind the big clods of coal, from the big excavators from the surface mines.

The machinery fair value minus sale costs is less than its book value. The mill for crushing coal does not generate independent treasury inflows. The production line composed of transport tapes, reductants, mill for crushing coal, return heads, generates cash inflows. The recoverable amount of the production line indicates that the production line as a whole is not impaired.
If the expenditure and revenue budget does not include the replacement of the machinery (the mill for crushing coal), the machinery recoverable amount may not be estimated, because the machinery value in use may differ by its fair value minus sale cost and may be determined only for the cash-generating unit which the machinery (the mill for crushing coal) belongs to.

The production line is not impaired and it is not recognised any machinery impairment loss.

It is necessary that C.E. Oltenia revalues the depreciation period or method of the machinery.

A short period or a rapid method of depreciation may be imposed to reflect the machinery useful life or the manner in which the economic benefits will be used by C.E. Oltenia.

If C.E. Oltenia provides expenses for the machinery replacement, which is from import and its selling in the near future, the cash flows generated by the continuous use of the machinery till the moment of the sale are estimated to be very low.

The machinery value in use may be estimated as appropriate to its fair value minus sale expense. The recoverable amount, in these conditions, may be calculated without taking into account the cash-generating unit (the technologic line) of the machinery. Because the machinery fair value minus sale cost is lower than its book value, an impairment loss will be registered for that machinery.

3rd example

C.E. Oltenia bought a building with 20,000,000 lei ten years ago. Up to the present, the property market has collapsed and the market value of the building at the balance sheet date is estimated to be 10,000,000 lei. The building sale costs are negligible. The building book value at the balance sheet date is 15,000,000 lei, the exploitation period is 30 years. The building fulfils all the conditions for functioning as an office for a mine.

It is found, that in near future, C.E. Oltenia will not use this office for several reasons (heating, big distance from head office, water etc.). The building value in use may not be determined because the building does not generate independent cash inflows. So, C.E. Oltenia determines the recoverable amount of the cash-generating unit to which the building belongs, namely C.E. Oltenia, as a whole. If it is appealed to the fair value (based in the first place on observable market values) it would be evaluated the building recoverable amount to its market value (10,000,000 lei) and would recognize an impairment loss of 5,000,000 lei (15,000,000 lei – 10,000,000 lei), although from the calculations did not result that the cash-generating unit of the building would be impaired.

4th example

C.E. Oltenia bought a computer with 2000 lei, in order to be used by Accounting Compartment, at the end of 2004. The computer is linearly amortized in four years. The disposal value is estimated to be 0. The computer book value is 10,000 lei, at the end of 2010. There is an active market for second hand computers, where these may be recovered on parts. The computer market value is 600 lei.

C.E. Oltenia does not intend to replace this computer before the end of duration use. The cash-generating unit of the computer is not impaired. If it is appealed to the fair value (in the first place based on prices imposed by the market), it would evaluate the computer recoverable amount to its market value (600 lei) and would recognise an impairment loss of 400 lei (1,000 lei – 600 lei), even if the cash-generating unit of the computer is not exceeded.

Conclusion

In conclusion, IAS-36 “the Impairment of assets” is based on “economic” criteria for the recognition of a loss assessment: an impairment loss is always recognised when the recoverable amount of an asset is inferior to its book value. This criteria was used in many International Accounting Standards before IAS-36, for example IAS-16 “Tangible assets”, IAS-19 “Costs of research and development”, IAS-22 “Business combinations”. The following examples refer to C.E. Oltenia activity.

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