

Thematic Review

Impairment of non-financial assets

October 2019



Financial Reporting Council

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Key to symbols

- ✓ Represents good practice
- ▲ Represents an omission of required disclosure or other issue
- 💡 Represents an opportunity for enhancing disclosures

Example of better disclosure practice

Including some identified from our routine monitoring of corporate reports (marked *).

Introduction

Scope

As part of CRR's routine monitoring activity, we often ask companies for additional information about their impairment testing. This is either because disclosures are not sufficiently clear for users of the accounts to understand the outcome of that process, or because information required by IAS 36 has not been given. The questions apply both to the annual testing of cash generating units ('CGUs') including goodwill and intangible assets with indefinite useful lives, and to testing prompted by an indicator of impairment, such as a change in market conditions or regulations affecting the business. In some instances, it is not clear how the directors concluded that the carrying amount was recoverable.

We have conducted a thematic review of selected companies' disclosures relating to the impairment of non-financial assets to identify and encourage more transparent reporting of the:

- events and circumstances that led to the recognition or reversal of an impairment loss; and
- basis on which the directors concluded that the carrying amounts of non-financial assets are recoverable.

Disclosures about the key assumptions made by management are highly relevant, because describing how management determines their values gives investors and other users additional information to assess the reliability of impairment testing and compare management's outlook with their own.

We also considered each entity's strategic report to assess the adequacy of commentary on impairment, where it arose, and the broader performance and prospects of the business.

Sample

We performed a limited scope desktop review of the annual reports and accounts of twenty companies. We selected listed companies that had either recognised material impairment charges or reversals in their 2018/2019 accounts or that had a material goodwill balance. We did not notify companies in advance of their inclusion in the sample, which was mainly drawn from FTSE 350 companies, with a focus on retail and business services.

The sample included two companies in extractive industries, with certain assets accounted for under IFRS 6 'Exploration for and Evaluation of Mineral Resources'. This standard gives examples of indicators of impairment for extractive industries, and requires impairment to be measured and recognised in accordance with IAS 36.

Sample by industry sector

Retail & consumer services	8
Travel & leisure	3
Business Support Services	3
Media	2
Extractive	2
Healthcare	1
Transportation	1

Introduction (2)

Insights from investors

Before scoping our work, we met with investors to understand what they find helpful in impairment disclosures and what they would like to see more of to enhance the information management provides. They told us that they appreciate the following.

- 💡 Clear and consistent information in the financial statements, strategic report, description of the business model and principal risks and uncertainties. This helps them gain an understanding of management's approach to the impairment testing of non-financial assets.
- 💡 More comparative information. This helps them understand trends in key assumptions, discount rates and growth rates, and especially the amount of headroom available in the prior and earlier periods.
- 💡 Explanations and values for assumptions. These provide valuable insights into management's thinking. Generic statements about forecasting based on experience and expectations for the future, and key assumptions that are not quantified, are not as helpful.
- 💡 More granular assessment of CGUs. This increases credibility and demonstrates that 'bad news' in one CGU is not being sheltered by the recoverable amount of a more profitable CGU.

Summary of key findings

Overview

We found numerous instances of good practice across each aspect of disclosure – events and circumstances triggering an impairment loss, description of cash generating units, key assumptions used to estimate the recoverable amount, and sensitivity analysis. However, no company stood out as clearly providing fully compliant disclosures in all relevant areas.

Alongside instances of good practice, we also identified a number of common disclosure omissions and opportunities to clarify and enhance disclosures, particularly around sensitivity and significant judgements and estimates.

Assets and CGUs subject to impairment

- ✓ Better disclosures described how the entity identified single sites or clusters of sites as CGUs, and grouped CGUs for the purposes of testing goodwill for impairment.
- ✓ They gave clear explanation of the trigger(s) for impairment.
- ▲ Some companies omitted the recoverable amount of the assets and CGUs subject to an impairment loss (or reversal).

Of the companies in our sample, two-thirds reported a material impairment loss, and a quarter a material reversal of a previous impairment.

Impairments



Reversals



Key assumptions

- ✓ Better disclosures identified the key assumptions used in the cashflow projections to estimate the recoverable amount of a CGU or group of CGUs, not just the long term growth rate and discount rate.
- ✓ They explained how management determines the key assumptions, linking future expectations to external conditions and/or the company's own strategy.
- ✓ They disclosed the values assigned to the key assumptions, with comparative figures, for each significant CGU or group of CGUs being tested.
- ▲ Some companies omitted 'base case' values for key assumptions for which sensitivity is given. Where required by IAS 36.134(f), sensitivity disclosures should include the assigned value, and it is useful information to help users understand estimation uncertainty.

Discount and growth rates

- ✓ Better disclosures explained clearly how the discount rate had been derived, differentiating among CGUs with different risk profiles.
- ✓ They provided details of short term growth rates, and why the 'short term' is extended beyond five years in specific circumstances.
- 💡 Companies applying value in use ('VIU') should make it clearer that they are using an appropriate discount rate, i.e. pre-tax and not based on entity-specific leverage.

Summary of key findings (2)

Sensitivity analysis

- ✓ Better disclosures clearly stated what changes in key assumptions management thinks are reasonably possible, and the impact of such change (whether reducing headroom to nil or giving rise to a potentially material adjustment to the carrying value)
- ⚠ Some companies omitted the disclosure of the excess of the recoverable amount over the carrying amount ('headroom') of a CGU, which is required where a reasonably possible change in key assumptions would reduce its headroom to nil.
- ⚠ Some companies stated that headroom was sensitive to changes in key assumptions, but gave the effect of changes of, say, +/- 1% in sales growth or discount rates, rather than the specific changes in assumptions that would erode headroom to nil.
- 💡 Companies should apply the disclosure requirements for headroom sensitivity (page 14) and estimation uncertainty (page 15) consistently, clearly marking additional information they provide over and above those requirements.
- 💡 In cases where no reasonably possible change would either erode headroom for CGUs when testing goodwill (IAS 36.134) or give rise to a material adjustment to any carrying value in the next year (IAS 1.125), companies should take care that additional sensitivity disclosures do not give the wrong impression or become confusing to users.
- 💡 Companies can distinguish more clearly between matters of significant judgement, such as the determination of CGUs, and estimating uncertain amounts, such as future cash flows and discount rates.

Disclosure requirements of IAS 36

Assets and CGUs for which an impairment loss or reversal has been recognised (IAS 36.130-132)

For each individual asset or CGU, for which a material impairment loss has been recognised or reversed, disclosure is required of:

- the amount of the loss recognised or reversed, and the events and circumstances leading to the recognition or reversal;
- the nature of the asset or a description of the CGU;
- for a CGU, analysis of the loss or reversal by class of assets and, where applicable, details of any change in how assets are aggregated to make up the CGU;
- the recoverable amount of the asset or CGU, and whether that is calculated using VIU or fair value less costs of disposal ('FVLCD');
- where applicable, the fair value hierarchy, a description of the valuation technique(s) used and the key assumptions underlying the estimation of FVLCD, including the discount rate(s) used, if it is measured using a present value technique; and
- where applicable, the discount rate(s) used to estimate VIU.

Less detailed information is required for aggregated, but individually immaterial, impairment losses or reversals.

IAS 36 also encourages the disclosure of assumptions used to determine the recoverable amounts of assets or CGUs subject to impairment loss or reversal. This information is required when the CGU includes goodwill or an intangible asset with indefinite useful life (see below).

Estimates of the recoverable amount of CGUs containing goodwill or intangible assets with indefinite useful lives (IAS 36.134-135)

IAS 36 requires disclosures about these CGUs (or groups of CGUs) whether or not an impairment loss (or reversal) is recognised in the period.

The disclosures are primarily concerned with the assumptions and estimates used in determining VIU or FVLCD, whichever supports the recoverable amount.

An entity must also disclose headroom and sensitivity to changes in any key assumption where a reasonably possible change would cause the recoverable amount to fall below the carrying value of the CGU.

Less detailed, aggregated information is required for CGUs (or groups of CGUs) whose goodwill or intangible assets with indefinite useful lives are not individually significant.

Sensitivity disclosures

For impairment losses recognised or reversed:

- There is no requirement in IAS 36, paragraph 130.
- The entity should disclose estimation uncertainty under IAS 1, paragraphs 125 and 129, where there is significant risk of a material adjustment in the following year. As noted in CRR's Judgements and Estimates review in 2017,¹ we expect these disclosures to include sensitivity analysis or the range of reasonably possible outcomes.

For CGUs with goodwill or indefinite life intangibles:

- Sensitivity is only *required* by IAS 36 when a reasonably possible change would completely erode headroom.
- Voluntary disclosure may be helpful in other cases.
- Disclosure of estimation uncertainty may be required by IAS 1, paragraph 125, for example where changing assumptions could erode headroom *and* give rise to a material impairment loss in the following year.

Cash generating units

A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. [IAS 36.6]

The Group had four cash-generating units at the beginning of the year ... During the year it was recognised that the cash inflows of the Nationals and Regionals cash-generating units were largely interdependent such that they have been combined into a single cash-generating unit. The increase in the interdependency has been accelerated due to the increased scale of advertising packages sold across all titles and websites and reflects the groupwide nature of our wholesale and distribution contracts.

Reach plc Annual Report 2018*

Property, plant and equipment and non-current other assets are reviewed for impairment if events or changes in circumstances indicate that the carrying amount of an asset or a cash-generating unit is not recoverable. A cash-generating unit is an individual store. ...

Goodwill is allocated to groups of cash-generating units and is tested annually for impairment and whenever there is an indication that the goodwill may be impaired. The cash-generating units used are individual stores and the groups of cash-generating units are either the store portfolios or individual businesses acquired.

JD Sports Fashion plc Annual Report & Accounts 2019

Better disclosures about CGUs had the following attributes; they:

- ✓ described how CGUs were identified, and whether that had changed from the prior period;
- ✓ explained how individual CGUs had been grouped for the purposes of allocating goodwill or intangible assets;
- ✓ distinguished impairment at the individual CGU level from testing of goodwill (and other assets) allocated to a group of CGUs;
- ✓ reported significant judgement exercised in defining CGUs and groups of CGUs; and
- ✓ identified significant judgement exercised in determining 'dependent' cash flows attributable to each CGU.

Cash generating units are deemed to be individual units or a cluster of units depending on the nature of the trading environment in which they operate. We only consider sites as a cluster of units, i.e. as a single CGU, where they are in a single, shared location, such as an airport, such that demand at one unit can directly affect that of other units in the same location.

The Restaurant Group plc Annual Report 2018

Judgement is required as to whether E-commerce sales (and associated costs) could be attributed to stores for the purposes of impairment testing when calculating the value in use of each store CGU. While management believes that a proportion of E-commerce sales could be attributed to stores, the basis of such attribution was difficult to determine, due to insufficient evidence to reliably estimate. For this reason, only iKiosk and Click & Collect E-commerce sales have been deemed directly attributable to a store within the individual store CGU value in use calculations. Attributing 10% of unallocated e-commerce sales and the related costs, would decrease the impairment and onerous lease charge by £1.5m and £7.7m respectively.

Superdry plc Annual Report 2019

Cash generating units (2)

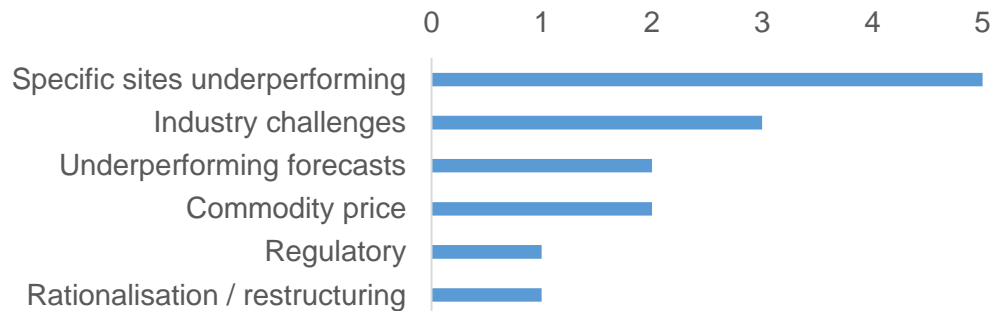
A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. [IAS 36.6]

- ▲ Some companies operating from multiple outlets and treating each outlet as a CGU for the purposes of impairment of most PP&E, some intangible assets and certain other non-current assets failed to explain this. It was then less clear that goodwill and 'firm-wide' intangible assets can only be allocated to groups of these CGUs.
- 💡 Where outlets (or smaller units in any business) are grouped, is it helpful to explain the basis for doing so.
- 💡 Distinguish the *grouping* of CGUs for testing goodwill impairment from *aggregating* CGUs that do not have individually significant amounts of goodwill. Use *consistent terminology* across different contexts, to maintain this distinction.

- 💡 Where testing is performed at several levels, make it clear that impairment testing has been applied in the order set out by IAS 36.98: assets within a CGU first, where there is indication of impairment, then the CGU, then the group of CGUs to which goodwill has been allocated. We found that companies do not usually explain this in their disclosure of testing processes for their specific circumstances.
- 💡 We expect companies with sales via outlets and e-commerce to explain significant judgements made in identifying revenues and costs attributable to respective CGUs or groups of CGUs.

Impairment: events and circumstances

We categorised the reasons for impairment, based on the companies' commentary. Retail and leisure businesses, with a network of premises to service customers, had the highest incidence of impairment outside the extractive sector, which is affected every year by changing commodity prices.



- ✓ The company that recognised an impairment owing to regulatory change explained the trigger clearly, noting that the change was an indicator of impairment prompting an additional review.
- ✓ This company also set out the implications for greater uncertainty in its forecasting model, disclosing additional key assumptions affecting the specific CGU.
- ✓ Best practice makes clear the timing as well as the nature of changes in circumstances that affected impairment testing.

An entity shall disclose ... : (a) the events and circumstances that led to the recognition or reversal of the impairment loss. [IAS 36.130]

Retail impairment review In May 2018, the DCMS concluded its Triennial Review of stakes and prizes and announced maximum stakes on B2 gaming products are to be reduced from £100 to £2, with the change being brought into effect from 1 April 2019. A regulatory change of this nature is unprecedented and its impact on customer behaviour will not be known until some years after implementation. Based on a series of assumptions, preliminary estimates suggest that this could reduce the Retail segment's annualised adjusted operating profit following mitigation measures by c£70-100m, based on the size of the Retail estate at the time of the announcement in May 2018.

William Hill PLC Annual Report and Accounts 2018

... the continued subdued external environment and the deterioration in trading, which became apparent after conclusion of the 2018 business planning process that underpinned the 2017 impairment review, resulted in impairment charges taken at the half year to 30 June 2018.

Countrywide plc Annual report 2018

Impairment: events and circumstances (2)

✓ One company, citing industry challenges, provided specific external data on market trends alongside its own experience of profit margins.

⚠ In another case, however, it was not clear whether the impairment loss was prompted by external data or changes in the company's own estimates.

⚠ One company attributed its impairment to 'underperforming forecasts', without explaining why forecasts had not been met. Such generic language is not informative.

⚠ We challenge companies about the timing, where an impairment loss is recognised in the subsequent interim accounts but there is no indication of a possible impairment in the previous year's accounts.

💡 Some changes in circumstances are gradual. Companies could convey this by disclosing, for example, a history of headroom in recent periods. Investors told us that this trend information, while not generally required, provides useful insight.

An entity shall disclose ... : (a) **the events and circumstances that led to the recognition or reversal of the impairment loss.** [IAS 36.130]

During 2018, the UK New car market declined by 6.8% (source: SMMT), continuing the weak trend from 2017, with the sale of diesel vehicles down 29.6%. In addition, the supply imbalance and the elevated level of pre-registration activity resulted in pressure on both New and Used margins. In light of this and the recent performance of the Retail business in the UK, the Board has reassessed its short and medium-term forecasts and has updated the impairment test for the UK Retail CGU group based on a value in use calculation.

Inchcape plc Annual Report and Accounts 2018

Interaction with the Strategic Report

💡 Companies should address impairment losses and the recoverability of non-financial assets as part of the fair, balanced and comprehensive review of the business required by the Companies Act, section 414C.

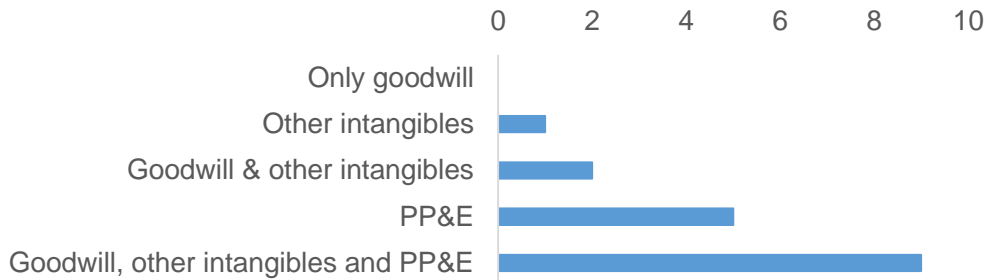
💡 A balanced review may need to explain that management's forecasts may be more optimistic than those implied by market indications, including where market capitalisation is an indicator of impairment.

💡 It is better to provide a single, thorough explanation – cross-referenced from the Strategic Report and other sections – than scattered superficial or repetitive commentary.

Impairment: other disclosures

Nature of assets affected

The distribution of impairments across asset types, for our sample, shows that goodwill tends not to be affected in isolation, but that other assets may become impaired without affecting goodwill.



Disclosures for individually immaterial amounts

Disclosures should be proportionate to the amount of impairment loss (or reversal). Immaterial impairments do not require extensive disclosure.

Aggregated information for individually immaterial impairment losses and reversals is required by IAS 36.131, where the aggregate amount is material, to disclose:

- the aggregate impairment loss and aggregate reversal;
- the main classes of assets affected; and
- the main events and circumstances that led to the recognition of these losses and reversals.

Comparative information

- The disclosures required by IAS 36 are subject to the requirement of IAS 1.38 to provide comparative figures for all amounts reported in the current period's financial statements and for narrative and descriptive information if it is relevant to understanding the current period's financial statements.
- Comparative information may not always be relevant. For example, where a company had no impairment loss in the prior period, there will be no comparative for the disclosures under IAS 36.130.

The total net impairment reversal of £73m (£219m reversal offset by £146m losses) largely reflects normal fluctuations expected from store level performance, property fair values and changes in discount rates. ... The impairment reversal of £219m (2018: £275m) relates to properties in the UK & ROI of £129m (2018: £154m), Central Europe of £86m (2018: £112m) and Asia of £4m (2018: £9m), while the impairment losses of £146m (2018: £88m) relate to properties in the UK & ROI of £46m (2018: £50m), Central Europe of £64m (2018: £6m) and Asia of £36m (2018: £32m).

Tesco PLC Annual Report and Financial Statements 2019

The company also disclosed its sensitivity analysis for the trading stores portfolio, based on adjustments for each geographic region to discount rates, sales growth and property fair values which materially affect the amount of aggregate impairment losses and reversals.

Impairment: other disclosures (2)

Recoverable amount of impaired assets and CGUs

- ✓ Better disclosures specify the recoverable amount.

The goodwill impairment charge ... primarily relates to a charge of £148.0 million on VMLY&R ... The recoverable amount for the VMLY&R cash-generating unit is £1,327.3 million. It is based on a value in use calculation, ...

WPP plc Annual Report 2018

A few companies disclosed the carrying amount of assets impaired (or with impairment reversal) in the period, but this may not represent the recoverable amount. Companies should make this clear, together with the measurement basis for the recoverable amount.

Plant & machinery assets were impaired to their 'value in use' recoverable amount of £Xm, which is their carrying value at year end.

This information is useful for estimating the relative importance of an impaired CGU, the carrying value of assets in the CGU other than goodwill and intangible assets with indefinite useful lives (which may still have 'headroom' in their individual recoverable amounts) and the potential for further impairment losses.

- ⚠ Most of the companies with a material impairment loss or reversal failed to disclose the recoverable amount of the asset(s) or CGU(s) affected. Companies should satisfy the requirement of IAS 36.130(e) by specifying the recoverable amount.

An entity shall disclose ... : (e) the recoverable amount of the asset (cash-generating unit) and whether [this] is its fair value less costs of disposal or its value in use. [IAS 36.130]

Recoverable amount: key assumptions

Key assumptions are those to which the unit's (group of units') recoverable amount is most sensitive. [IAS 36.134]

Specific requirements of IAS 36

For an asset or CGU not containing goodwill or an intangible asset with an indefinite useful life, disclosure of assumptions used to determine the recoverable amount is encouraged, but not required [IAS 36.132].

For CGUs (or groups of CGUs) containing goodwill or intangible assets with indefinite useful lives, disclosure of key assumptions and management's approach to determining their values is required where:

- the recoverable amount is based on VIU [IAS 36.134(d)(i)], or
- the recoverable amount is based on FVLCD and FVLCD is not measured using a quoted price for an identical unit [IAS 36.134(e)(i)].

There are separate requirements relating to the long term growth rate and discount rate used for VIU or discounted cash flow FVLCD. Key assumptions relate to short-term forecasts of net cash flows, and should therefore take account of cost inflation or operating margins as well as sales growth.

The value assigned to a key assumption is required only if the company needs to give sensitivity analysis for that assumption [IAS 36.134(f)].

💡 Investors told us that they appreciate disclosure of key assumption values because they give an insight into management's outlook and expectations. We encourage companies to disclose these values.

💡 Where a FVLCD calculation uses the same key cash flow assumptions as VIU, modified to reflect a market participant's perspective, it is helpful to explain this.

Recoverable amount: key assumptions (2)

Key assumptions are those to which the unit's (group of units') recoverable amount is most sensitive. [IAS 36.134]

Key assumptions are given specifically for the five-year forecasts – the company discloses long term growth and discount rates separately.

This explains the key drivers – market maturity and local inflation – lying behind the range of values for the nominal growth rate assumption.

The key assumptions used by management in setting the financial budgets for the initial five-year period were as follows:

Forecast sales growth rates *Forecast sales growth rates are based on past experience adjusted for the strategic direction and near-term investment priorities within each CGU. Key assumptions include growth in Online Program Management, Virtual Schools and Professional Certification, stabilisation in UK Qualifications and US Assessments, and ongoing pressures in the US Higher Education Courseware market. The five-year sales forecasts use average nominal growth rates between 2% and 3% for mature markets and between (1)% and 12% for emerging markets with high inflation.*

Operating profits *Operating profits are forecast based on historical experience of operating margins, adjusted for the impact of changes to product costs and cost-saving initiatives, including the impact of the implementation of our cost efficiency programme.*

Cash conversion *Cash conversion is the ratio of operating cash flow to operating profit. Management forecasts cash conversion rates based on historical experience.*

Pearson plc Annual report and accounts 2018

This explains how the values are determined and the background to differences between CGUs.

This explains how the values are determined, linked to strategic planning.

This links profit forecast to cash flow – few companies do this.

This explains the rationale for higher growth and better margins than recently experienced.

Sales projections ... assume sales increases in each country that are higher than recent experience and market growth expectations, driven by an improved and differentiated offer. Assumed margin percentage improvements reflect a lower cost of goods sold from leveraging the Group's buying scale through a unified offer, which will be partially offset by range clearance and implementation costs. Higher assumed operating profit percentages reflect operational leverage from increased sales as well as cost savings through operational efficiencies, in particular from unifying goods not for resale spend.

Kingfisher plc 2018/19 annual report & accounts

This company's key assumptions disclosure also explains the source of key assumptions on cash flow, linked to key drivers in the strategic plans as set out in its Strategic Report.

Recoverable amount: VIU and FVLCD

Comparison of estimation methods

IAS 36 prescribes two methods for determining the estimated recoverable amount of an asset or CGU. A company uses whichever gives the higher amount, but need not calculate both if the first method used shows that the recoverable amount exceeds the carrying value.

Most companies in our sample used VIU only; three companies used FVLCD only, while three used both methods.

- ✓ Better disclosures of DCF measurements for FVLCD explained the cash flow assumptions, management's approach to determining their values and how the discount and long term growth rates had been calculated. The example on page 9, from Pearson plc, illustrates this.
- ▲ We will continue to challenge companies where the recoverable amount is measured using VIU, but the cash flow forecasts appear to include the benefits of developing new business or to rely on future investment in capacity.

	VIU	FVLCD
Valuation method	DCF using short term forecasts and perpetuity of the terminal value	Any fair value measurement technique as per IFRS 13 'Fair Value Measurement', less estimated costs of disposal
Relevant cash flows	Based on approved budgets/forecasts, for the asset or CGU in its current condition, excluding acquisitions, enhancements, financing and tax	As per IFRS 13.B14, the assumptions used for the cash flows and discount rate reflect market participants' views, and they should be internally consistent
Long term growth rate	Must not exceed the long term average growth rate for the relevant market, product or country	No specific restrictions
Discount rate	Pre-tax	As per IFRS 13.B14, discount rate reflects assumptions that are consistent with those inherent in the cash flows (typically post-tax).

Recoverable amount: VIU and FVLCD (2)

- ▲ Accounting policy disclosure should be consistent with the basis used. One company described discounting VIU cash flows at a pre-tax rate, but its recoverable amounts were based on FVLCD; another's FVLCD methodology differed from that implied in its policy.
- ▲ Two companies, using FVLCD for some impairment testing of goodwill, failed to disclose the fair value hierarchy level for the fair value measurement.
- ▲ One company disclosed that it used FVLCD for some CGUs, but did not identify which specific CGUs' recoverable amounts represented FVLCD in the current or prior period. Its disclosure of assumptions suggested only VIU had been used.
- 💡 When the other basis was used in the prior period, it is good practice to explain the circumstances for the change, i.e. why one method now gives a higher or lower result than in the past, as illustrated by the case below.

The Directors assessed the recoverable amount of the ABC group of CGUs on a VIU basis, as in the prior period, and found that it was less than the carrying value owing to reduced profit margin forecasts. The Directors reassessed the recoverable amount using discounted cash flows determined according to market participant assumptions. These include the costs and benefits of budgeted (but not committed) investment in additional and more efficient production machinery. Projecting the revised cash flows and discounting at the rates shown below, management concluded that the FVLCD recoverable amount exceeds the carrying value.

This explains the basis for using FVLCD; some companies' disclosure suggests different criteria, such as availability of information or reliability of forecasting.

This states clearly which CGUs' recoverable amount is based on VIU and FVLCD.

The fair value method, its hierarchy level and key assumptions are clearly stated. The disclosure could be improved with an explanation of how management determines the estimated multiple and costs of disposal.

The recoverable amount is the higher of FVLCD and VIU. However, in line with IAS 36, FVLCD is only determined where VIU would result in an impairment. ...

Impairment review

... For all CGUs except for MX, the recoverable amount was determined by measuring their VIU. The recoverable amount for the MX CGU was calculated based on FVLCD.

... FVLCD was calculated based on a revenue multiple model based on budgeted revenues for 2019 and is therefore a level 3 measurement. Level 3 measurements are based inputs which are normally unobservable to market participants. Costs of disposal can be assumed to be 10% of expected disposal proceeds.

Just Eat plc Annual Report and Accounts 2018

Recoverable amount: value in use

Period of cash flow projections

An entity shall disclose ... : (d) [where VIU is used] (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 ... an explanation of why that longer period is justified.. [IAS 36.134]

The Board approved two-year forecasts for each segment in December 2018. These form the basis of our value in use calculation, with separate extrapolation of net revenue and expenses by segment based on a combination of recently observable trends, management expectations and known future events. For the purposes of the value in use calculation, the two-year forecasts were extended to cover a five-year period.

William Hill PLC Annual Report and Accounts 2018

In this example, budgeted year 1 growth rate is 8%, forecast growth in year 2 is 7% and in year 3 is 6%. The long-term country inflation rate is 2% so the year 4 growth rate is calculated to be the midpoint between 6% in year 3 and 2% in year 5, i.e. 4%. The terminal value calculation applies the long-term inflation rate of 2%.

G4S plc Integrated Report and Accounts 2018

Better disclosures about forecasting periods had the following attributes; they:

- ✓ specified the relevant period for each significant CGU (or group of CGUs), rather than merely stating the maximum period;
- ✓ linked forecasting for impairment testing purposes to strategic planning periods;
- ✓ explained how short-term budgets covering a shorter period are extrapolated up to five years, before applying the long-term growth rate;
- ✓ explained how the entity bridges between short term forecasting assumptions and the long term growth rate; and
- ✓ described the basis on which certain CGUs (or groups of CGUs) have a longer forecasting period.

One company disclosed that it evaluates two groups of CGUs using a forecasting period of eight years, but five years for others, whereas a few companies stated only that they forecast 'up to five years'.

All operating countries in the Group are required to submit a budget for the next financial year (for the year ending 31 December 2019) and strategic plan forecasts for the two years following the budget year (i.e. for the years ending 31 December 2020 and 31 December 2021) for both their Secure Solutions and Cash Solutions businesses.

G4S plc Integrated Report and Accounts 2018

Estimated future cash flows are based on these plan forecasts for the first three years, with year 4, year 5 and the terminal value projected by applying growth rates as set out in the growth rate section below.

G4S plc Integrated Report and Accounts 2018

Recoverable amount: value in use (2)

Period of cash flow projections

An entity shall disclose ... : (d) [where VIU is used] (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 ... an explanation of why that longer period is justified.. [IAS 36.134]

Better disclosures about forecasting periods had the following attributes; they:

- ✓ specified the relevant period for each significant CGU (or group of CGUs), rather than merely stating the maximum period;
- ✓ linked forecasting for impairment testing purposes to strategic planning periods;
- ✓ explained how short-term budgets covering a shorter period are extrapolated up to five years, before applying the long-term growth rate;
- ✓ explained how the entity bridges between short term forecasting assumptions and the long term growth rate; and
- ✓ described the basis on which certain CGUs (or groups of CGUs) have a longer forecasting period.

For CGU groups in Emerging Markets, cash flows after the five-year period are extrapolated for a further five years using declining growth rates which reduces the year five growth rate down to the long-term growth rate of 2.5%, to better reflect the medium-term growth expectations for those markets. A terminal value calculation is used to estimate the cash flows after year ten using these long-term growth rates. For all other markets, a terminal value calculation is used to estimate the cash flows after year five.

Inchcape plc Annual Report and Accounts 2018

For VIU, cash flows are typically forecast for periods up to five years, but there are some CGUs that are forecast for longer periods. [ANZ and IT CGUs use a period of 8 years.] These CGUs are located in immature markets which are currently lacking penetration, and where future investment in the business is expected to result in its long-term growth being achieved outside of five years. For these CGUs, it is appropriate to use forecasts extending beyond five years as they correlate with trading experienced in similar markets.

Just Eat plc Annual Report and Accounts 2018

Recoverable amount: discount rate

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money. The risks specific to the asset are reflected as an adjustment to the future estimated cash flows.

BBA Aviation plc Annual Report 2018

Our calculation of discount rates are performed based on a risk-free rate of interest appropriate to the geographic location of the cash flows related to the asset being tested, which is subsequently adjusted to factor in local market risks and risks specific to us and the asset itself. ... Pre-tax discount rates have been calculated using the capital asset pricing model, the inputs of which include a country risk-free rate, equity risk premium, Group size premium and a risk adjustment (beta).

Just Eat plc Annual Report and Accounts 2018

A pre-tax discount rate of 9.7% (2017: 10.0%), calculated by reference to a weighted average cost of capital (WACC) calculated by reference to an industry peer group of quoted companies.

HSS Hire Group plc Annual Report and Financial Statements 2018*

The discount rates are based on an assessment of a relevant peer group's post-tax weighted average cost of capital (WACC). The post-tax WACC is subsequently grossed up to a pre-tax rate.

Tullow Oil plc 2018 Annual Report and Accounts

An entity shall disclose ... : (g) if recoverable amount is value in use, the discount rate(s) used in the current estimate ... [IAS 36.130]

An entity shall disclose ... (d)/(e) (v) the discount rate(s) applied to the cash flow projections. [IAS 36.134]

Summary of guidance on discount rates for VIU estimation in IAS 36 Appendix A

- A3 Reflect assumptions that are consistent with the estimated cash flows and a range of possible outcomes.
- A15 Exclude risks for which cash flows have already been adjusted.
- A16 Unless an observable market rate is available, use surrogates to estimate a market assessment of the time value of money and risk factors (variation in cash flows, inherent uncertainty and other factors that market participants would reflect in their rate of return).
- A17 Estimation starting points: entity's WACC, incremental borrowing rate, other market borrowing rates.
- A18 Adjust these rates for market assessment of asset-specific risks.
- A19 Ensure that the discount rate is independent of the entity's capital structure.
- A20 Use a pre-tax discount rate for VIU, adjusting from a post-tax rate (such as WACC) if that has been used for estimation.
 - *The pre-tax discount rate may differ from the post-tax discount rate grossed up by the standard rate of tax, depending on the tax rate, the post-tax discount rate, the timing of future tax cash flows and the useful life of the asset, as shown by the example at IAS 36.BCZ85.*
- A21 Use different discount rates for different periods, if VIU is sensitive to different risks over time.

Recoverable amount: discount rate (2)

- ▲ Where the company applies different rates to different CGUs, it should disclose them.
- 💡 We expect more specific disclosure than merely that the company has estimated a rate that reflects the current market assessment of the time value of money and the risks specific to the asset(s) or CGU(s).
- 💡 Better disclosures explain, concisely, the key inputs used in determining the discount rate.
- 💡 Fuller disclosures include the source of data used to estimate surrogates for time value of money, such as long-term government bond yields, and risk factors.
- ▲ We found that a few companies refer to peer group WACC as a starting point, but then adjust it to reflect their own group or CGU's gearing. This suggests that the discount rate may not be independent of their own capital structure.

An entity shall disclose ... : (g) if recoverable amount is value in use, the discount rate(s) used in the current estimate ... [IAS 36.130]
An entity shall disclose ... (d)/(e) (v) the discount rate(s) applied to the cash flow projections. [IAS 36.134]

Recoverable amount: growth rate

An entity shall disclose ... : (d) if the unit's (group of units') recoverable amount is based on value in use: iv) the growth rate used to extrapolate cash flow projections beyond the period covered by the most recent budgets/ forecasts, and the justification for using any growth rate that exceeds the long-term average growth rate for the products, industries, or country or countries in which the entity operates, or for the market to which the unit (group of units) is dedicated.. [IAS 36.134]

Cash flows for succeeding [5+] years had a long-term growth factor applied to them of 1.8% for each of the CGUs (2017: 2.5%). The Directors believe that it is appropriate to lower the growth rate assumptions from previous years to reflect the deterioration in the long-term outlook for the UK economy.

HSS Hire Group plc Annual Report and Financial Statements 2018*

Cash flows beyond the period of the strategic plans are calculated using a growth rate which does not exceed the long-term average growth rate for retail businesses operating in the same countries as the CGUs.

Kingfisher plc 2018/19 annual report & accounts

The growth rates used to extrapolate cash flows beyond the budget period ... do not exceed long-term industry averages and reflect the revenue growth and ongoing efficiency initiatives, and the relative maturity of the Retail and Autocentres businesses.

Halfords Group plc Annual Report 2019

Better disclosures about long term growth rates had the following attributes; they:

- ✓ identified the specific rate for each significant CGU;
- ✓ disclosed the prior period rate(s) and explained significant changes;
- ✓ explained the basis on which long term growth rates are determined, using product, industry or country specific information;
- ✓ confirmed that the growth rate does not exceed the relevant long-term average growth rate;
- ✓ explained how the applied rate differs from relevant long-term average growth rates;
- ✓ cited the source(s) used for long-term average growth rates; and
- ✓ explained how the long term growth rate is considered to be consistent with other assumptions.

Most of the companies with multiple CGUs or groups of CGUs for goodwill testing did provide CGU-specific figures.

The terminal growth rates do not exceed the long-term projected growth rates for the relevant markets, reflect the impact of future generic competition and take account of new product launches.

GSK plc Annual Report 2018

One company cited the long-term country inflation rate per the IMF as a 'cap' on its perpetuity growth rate, another referenced a GDP forecast from the Office for Budget Responsibility.

Recoverable amount: growth rate (2)

An entity shall disclose ... : (d) if the unit's (group of units') recoverable amount is based on value in use: iv) the growth rate used to extrapolate cash flow projections beyond the period covered by the most recent budgets/ forecasts, and the justification for using any growth rate that exceeds the long-term average growth rate for the products, industries, or country or countries in which the entity operates, or for the market to which the unit (group of units) is dedicated.. [IAS 36.134]

Growth rates are derived from management's estimates, which take into account the long-term nature of the industry in which each CGU operates, external industry forecasts of long-term growth in the aerospace and defence sectors, the maturity of the platforms supplied by the CGU and the technological content of the CGU's products.

Signature ... where the derived rate is higher than the long-term GDP growth rates for the countries in which the CGU operates, the latter has been used. As a result, an estimated long-term growth rate of 1.9% (2017: 2.0%) has been used for Signature which reflects forecast long-term US GDP growth.

Ontic For the purpose of impairment testing in [the OEM-licensed parts and maintenance business] ... an approach required by the accounting standard has been applied which assumes no licence acquisitions or other acquisition of businesses. As a result, no long-term growth rate has been applied for Ontic.

BBA Aviation plc Annual Report 2018

This company also provided key market measures underlying its estimates of demand in the long term, helping users understand the basis on which management concluded that goodwill is recoverable.

Better disclosures about long term growth rates had the following attributes; they:

- ✓ identified the specific rate for each significant CGU;
- ✓ disclosed the prior period rate(s) and explained significant changes;
- ✓ explained the basis on which long term growth rates are determined, using product, industry or country specific information;
- ✓ confirmed that the growth rate does not exceed the relevant long-term average growth rate;
- ✓ explained how the applied rate differs from relevant long-term average growth rates;
- ✓ cited the source(s) used for long-term average growth rates; and
- ✓ explained how the long term growth rate is considered to be consistent with other assumptions.

💡 Estimate long term growth using a rate that is specific to the market, product or country.

💡 Significant changes in assumptions such as growth rate are important signals to users about management's assessment of the future. We expect relevant factors to be explained, or cross-referenced to specific commentary, elsewhere in the annual report.

Recoverable amount: sensitivity


Headroom sensitivity to changes in key assumptions

Sensitivity disclosures are required because the estimate of recoverable amount is a complex calculation that lies within a range and is rarely a specific amount.

Investors told us that they appreciate disclosure of the headroom within a recoverable amount, as a buffer against future impairment, and insights into what management considers to be reasonably possible 'worst case' assumptions.







Disclosure of headroom is especially important where market indicators suggest that management's assumptions may be optimistic, deferring recognition of an impairment that appears to be already priced into the company's shares.

IAS 36.134(f) focuses on the case where changing a key assumption reduces headroom to nil. The required disclosure relates only to that assumption, and the amount of headroom under management's 'base case'.

 We were disappointed to note that no company in our sample provided all the information that met those requirements exactly. The case study example on page 25 includes the information we would expect a company to give.

*An entity shall disclose ... : (f) if a **reasonably possible change in a key assumption** on which management has based its determination of the unit's (group of units') recoverable amount **would cause the unit's (group of units') carrying amount to exceed its recoverable amount:***

- (i) the amount by which the unit's (group of units') recoverable amount exceeds its carrying amount;*
- (ii) the value assigned to the key assumption;*
- (iii) the amount by which the value assigned to the key assumption must change, after incorporating any consequential effects of that change on the other variables used to measure recoverable amount, in order for the unit's (group of units') recoverable amount to be equal to its carrying amount. [IAS 36.134]*

-  Disclose the headroom of each CGU or group of CGUs for which sensitivity information is relevant.
-  Consider the consequential impact of changing one key assumption on others, to reflect a coherent alternative scenario.
-  Explain what changes in the value of key assumptions reduce headroom to nil, not what impairment would arise from a given change in a key assumption's value.
-  It is not necessary to disclose sensitivity for all key assumptions, only those which cause the headroom to be reduced to nil.
-  If additional sensitivity information would be helpful to users (e.g. for CGUs that are not critically sensitive, or to show the impact of flexing more than one assumption), distinguish it from the required disclosures.
-  It can be helpful to state that management considers that no reasonably possible changes would reduce a CGU's headroom to nil.

Recoverable amount: sensitivity (2)

Headroom sensitivity to changes in key assumptions

An entity shall disclose ... : (f) if a **reasonably possible change in a key assumption** on which management has based its determination of the unit's (group of units') recoverable amount **would cause the unit's (group of units') carrying amount to exceed its recoverable amount**:

- (i) the amount by which the unit's (group of units') recoverable amount exceeds its carrying amount;
- (ii) the value assigned to the key assumption;
- (iii) the amount by which the value assigned to the key assumption must change, after incorporating any consequential effects of that change on the other variables used to measure recoverable amount, in order for the unit's (group of units') recoverable amount to be equal to its carrying amount. [IAS 36.134]

The Directors performed sensitivity analysis on the estimates of recoverable amounts and found that the excess of recoverable amount over the carrying amount of the ABC group of CGUs would be reduced to nil as a result of a reasonably possible change in the key assumption of sales growth in the cash flow forecasts. The Directors do not consider that the relevant change in this assumption would have a consequential effect on other key assumptions.

The excess of the ABC group of CGUs' recoverable amount over its carrying value is £Xm. The value assigned to the sales growth assumption is 5% in years 1-3 of the forecast period and 3% in years 4-5. The recoverable amount would equal the carrying value if sales growth were reduced by 1.5% throughout the forecasting period.

For the XYZ group of CGUs, the Directors do not consider that any reasonably possible changes to the key assumptions would reduce the recoverable amount to its carrying value.

This identifies the key assumption whose change in value causes the erosion of headroom.

This shows that management has considered consequential effects of the change on other assumptions

This provides the information required by IAS 36.134(f). Additional information may be helpful to users, but it should not displace the required disclosures.

This confirms the comprehensiveness of management's review.

Estimation uncertainty

Significant risk of material adjustment

In addition to the requirements of IAS 36, companies must consider whether estimation uncertainty over the recoverable amount of CGUs and assets requires disclosure in accordance with IAS 1.125.

This arises where there is a significant risk that a material impairment loss (or reversal) would be recognised in the following year using alternative assumptions and estimates to determine the recoverable amount of any asset or CGU.

It is likely to be especially relevant where an impairment during the current year leaves little or no remaining headroom, so any 'worse case' estimates would lead to further impairment.

IAS 1.125 disclosure has different requirements from the 'break-even' sensitivity for headroom required by IAS 36.134 or IAS 36.135. It is important to distinguish disclosures intended to satisfy different requirements, though companies should have a consistent position on what are reasonably possible changes in estimates and assumptions.

▲ We would expect a company to disclose relevant information about estimates and assumptions carrying significant risk of material adjustment in the following year, as required by IAS 1.125, where the company's net assets exceed its market capitalisation, indicating a possible impairment, but no loss has been recognised.

An entity shall disclose information about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. [IAS 1.125]

An entity presents the disclosures in paragraph 125 in a manner that helps users of financial statements to understand the judgements that management makes about the future and about other sources of estimation uncertainty. [IAS 1.129]

- 💡 Focus on assumption changes with a material impact on carrying values in the following year. Information about longer-term impact may be useful, but should be distinguished from critical estimation uncertainty.
- 💡 Explain alternative scenarios clearly, identifying whether a figure represents the change in assumption / outcome or the absolute amount of an alternative assumption / outcome.
- 💡 Make it clear whether changes are reasonably possible or illustrative.
- 💡 For disclosures relating to goodwill or intangible assets with indefinite life, where IAS 36.134 is also relevant, the assumptions about sensitivity ranges should be consistent.

Estimation uncertainty (2)

Significant risk of material adjustment

An entity shall disclose information about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. [IAS 1.125]

An entity presents the disclosures in paragraph 125 in a manner that helps users of financial statements to understand the judgements that management makes about the future and about other sources of estimation uncertainty. [IAS 1.129]

Key sources of estimation uncertainty ... A regulatory change of this nature is unprecedented and its impact on customer behaviour will not be known until some years after implementation. As the implementation takes effect and customer behaviour becomes known, this could result in further impairments (or reversals of the existing impairment charge) of assets in the Retail segment. Refer to note 12 for an analysis of the sensitivity of the impairment to a range of reasonably possible changes in assumptions. ...

[Note 12] For the Retail CGU, the following reasonably possible changes in assumptions upon which the recoverable amount was estimated, would lead to the following changes in the net present value of the Retail CGU:


	<i>Decrease in the value in use of Retail CGU £m</i>
<i>Change in assumption</i>	
<i>Decrease in forecast operating cash flows by 20%</i>	109.0
<i>Increase in discount rate by 1%</i>	43.5
<i>Decrease in long term growth rate by 1%</i>	26.9

William Hill Annual Report and Accounts 2018

This identifies the assumptions whose change in value may lead to material adjustment.

The company has elsewhere disclosed the 'base case' values for discount rate and long term growth rate in the information about its VIU calculation.

This confirms that management has considered reasonably possible changes, consistent with a significant risk of material adjustment.

 In some instances, a company may also need to explain how a material adjustment arises from reasonably possible changes in several assumptions in combination.

Parent company accounts – investments in subsidiaries

The recognition of such an impairment [of E&E assets] by a subsidiary is used by the Company as the primary basis for determining whether or not there are indications that the investment in the related subsidiary may also be impaired, and thus whether an impairment test of the investment carrying value needs to be performed. The results of exploration activities are inherently uncertain and the assessment of impairment of E&E assets by the subsidiary, and that of the related investment by the Company, is judgemental.

Tullow Oil plc 2018 Annual Report and Accounts

The Group tests the investment balances for impairment annually. The recoverable amounts of the investments have been determined based on value-in-use calculations which require the use of estimates. Management has prepared discounted cash flows based on the latest strategic plan.

AA plc Annual Report and Accounts 2019

Better disclosures about testing for impairment in parent company accounts had the following attributes; they:

- ✓ explained the relationship between impairment of operating assets in group companies, as an indicator of impairment for the parent company, and the assessment of recoverability of the investment in that subsidiary;
- ✓ described the significant judgements and estimates made in relation to impairment testing assumptions;
- ✓ confirmed either that there had been an assessment of impairment relating to investments (and, where relevant, other non-financial assets) or that the directors considered there to be no indicators of impairment; and
- ✓ disclosed information required by IAS 36.130 where there is an impairment, unless the company takes the exemption in FRS 101.8(l), set out on page 29, and there is equivalent information **for the same asset** in the consolidated accounts.

A combination of reasonably possible changes in key assumptions, such as print revenue declining at a faster rate than forecast or digital revenue growth being significantly lower than forecast, could lead to a further impairment. A 0.5% increase in the discount rate or a 0.5% decrease in the growth rate would increase the impairment charge by some £35 million. A 5% reduction in operating profit in the third year of the projections would increase the impairment charge by some £50 million.

Reach plc Annual Report 2018*

Only one parent company in the sample directly holds goodwill; none holds indefinite life intangible assets, or the particular assets covered by impairment disclosures in the consolidated accounts.

Parent company accounts – investments in subsidiaries (2)

Disclosure exemptions in FRS 101.8(I)

Provided that *equivalent disclosures* are included in the consolidated financial statements, parent company accounts prepared under FRS 101 do not have to disclose:

- information about level 2 and level 3 fair value measurements (IAS 36.130(f)(ii) and (iii)); and
- details of VIU or FVLCD assumptions, or sensitivity, for impairment testing of CGUs containing goodwill or indefinite life intangibles (IAS 36.134(d) to (f), 36.135(c) to (e)).

The exemptions *do not cover* matters such as the discount rate used in VIU estimation for an impaired asset (IAS 36.130(g)) or relevant disclosure of significant judgement and estimation uncertainty (IAS 1.122 and 1.125).

- ▲ A statement of the directors' opinion, that the aggregate value of the assets of the company consisting of shares in, or amounts owing from (whether on account of a loan or otherwise), the company's subsidiary undertakings is not less than the aggregate of the amounts at which those assets are stated or included in the company's balance sheet, is no longer required.
- ▲ Impairment of intercompany balances, in accordance with IFRS 9 (or FRS 102, Section 11, or subsidiaries' local GAAP), may be an indicator of impairment for investments.

Other issues

Interaction with IFRS 16 ‘Leases’

- Companies recognising ‘right of use’ assets will need to take account of these in the carrying amount of the CGU to which they belong.
- There are also implications for the recoverable amount, because forecast cash flows will increase after excluding rental payments and the discount rate may be affected.
- Right of use assets themselves may become impaired. An onerous lease provision at the time of transition to IFRS 16 should trigger an impairment review of the asset. This is subject to a practical expedient in IFRS 16.C10(b), to reduce the asset’s carrying value by the amount of the pre-transitional provision instead.
- CRR has undertaken a separate thematic review on IFRS 16 adoption.¹

Interaction with IAS 37 ‘Onerous Contracts’

- Where assets are dedicated to a contract and the contract becomes onerous, IAS 37.69 requires the entity to recognise any impairment loss that has occurred on those assets, before establishing a separate provision for the onerous contract.
- There may be significant judgement exercised in determining whether (and which) assets are dedicated to a contract, requiring relevant disclosure under IAS 1.122.
- Conversely, impairment of premises and goodwill, particularly arising from current or planned closure of premises, may indicate that property leases are onerous. Where no provision is recognised, an explanation as to why this is the case would be helpful to users of the accounts.

IASB project on Goodwill and Impairment

- After feedback from the Post-implementation Review of IFRS 3 Business Combinations, the International Accounting Standards Board is exploring whether it can:
 - require disclosures that would improve the information provided to investors about acquired businesses; and
 - simplify the accounting for goodwill and improve some aspects of the impairment test.
- Further details of the project and its current stage are available on the IFRS Foundation’s website.²
- At the time of writing, the Board plans to issue a Discussion Paper by the end of 2019.

Climate change

- 💡 Investors are becoming increasingly interested in disclosure around climate change in impairment testing.
- We found only one company making overt references to the implications of adapting to climate change and other environment-related constraints or opportunities, such as shortages of key resources, foreseeable regulatory change or shifts in demand for the company’s goods or services. Even in this case, however, there was no direct linkage from these assumptions to forecasting the long term performance of the business.
- Several companies identified these issues as a principal risk, or as affecting their business model in the longer term, but not as a specific threat to recoverable values of goodwill or intangible assets.

¹ Thematic Review – Disclosures relating to the implementation of IFRS 16 within 2019 interim accounts ² <https://www.ifrs.org/projects/work-plan/goodwill-and-impairment/>

Next steps

Engagement with companies in the sample

- We are writing to a number of companies included in our sample, where we identified a substantive question relating to their disclosures and/or specific areas for improvement.
- The outcomes of this engagement will be reflected in our next annual report on corporate reporting.

Impact on our future monitoring work

- We will challenge those companies where it is unclear how the directors concluded that the carrying amount of non-financial assets was recoverable.
- We will continue to raise questions of companies whose impairment-related disclosures appear:
 - to omit information required by IAS 36;
 - to have mis-applied the requirements for identifying CGUs and groups of CGUs,
 - to include inappropriate cash flows, such as enhancement expenditure in a VIU calculation; and
 - to contain inconsistencies between key assumptions, or between key assumptions and other parts of the annual report.
- We expect companies to take account of information that is most useful to investors, such as deeper explanations of management's choice of key assumption values and changes over time.

Key points to consider in 2020

when preparing impairment-related disclosures in 2019 accounts

- Brexit and other political / macro-economic risks
 - Uncertainty over a 'no deal' exit from the EU may remain unresolved when reporting on 2019. Even if it has been resolved, businesses with larger import / export volumes may foresee a wider range of reasonably possible changes in key assumptions than in the past.
 - Similarly, businesses affected by developments in trading relationships and the prospect of growing protectionism globally should consider the impact on their forecasting.
 - Best practice will link these assessments with descriptions of business model, viability and principal risks and uncertainties.
- Climate change and environmental impact
 - There are growing societal and regulatory pressures on businesses to mitigate their impact on the environment, and adapt to 'zero carbon', 'closed loop' production, reduced or recyclable packaging, and changing usage patterns for durable assets.
 - Companies for whom climate change and environmental impact are significant will explain how such factors, specific to the company's industry and value chain, have been taken into account in assessing medium and long term growth potential, costs and licence to operate.
- Interaction with IFRS 16 (see also page 17) may raise issues around:
 - impairment of right of use assets when a lease becomes onerous (subject to the practical expedient on transition);
 - increased carrying value of a CGU that includes right of use assets;
 - impact on discount rate used; and
 - forecast cash flows excluding rental outflows.

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