Project	**IAS 36 *Impairment of Assets***
Topic	**Interaction with transition requirements of IFRS 8 *Operating Segments***

Purpose of this agenda paper

1. The IFRIC received a request for guidance on the transition arrangements in IFRS 8 *Operating Segments* and its interaction with IAS 36 *Impairment of Assets*. The objective of this paper is to obtain an IFRIC [tentative] decision on this issue. This agenda paper:

   (a) Provides **background information** on the issue,

   (b) Includes an **analysis of the issue** in the context of current IFRSs,

   (c) Includes a **staff recommendation** and supporting rationale, and

   (d) **Questions for the IFRIC** to confirm whether they agree with the staff's recommendations.

2. Appendix A shows the draft wording to be included in IFRIC Update.

Background information

3. The request asks the IFRIC to consider the appropriate treatment of differences that may arise as a result of the adoption of IFRS 8 and its replacement of IAS 14 *Reporting Segments*.

4. The IASB made a consequential amendment to IAS 36 when it issued IFRS 8 in November 2006. The consequential amendment replaced the reference to 'segments' (as determined in accordance with IAS 14) with 'operating segments'

(as determined in accordance with IFRS 8). IFRS 8 is applicable to annual periods beginning on or after 1 January 2009. Accordingly, the year ending 31 December 2009 will be the first application of the standard by most entities that have calendar year-ends.

5. In particular, paragraph 80(b) of IAS 36 was amended to refer to IFRS 8 when setting the limit for aggregation of cash generating units (CGUs) when testing for goodwill impairment. Previously the limit had been set by reference to segments identified by IAS 14. The consequential amendment to paragraph 80(b) of IAS 36 is:

> **80 For the purpose of impairment testing, goodwill acquired in a business combination shall, from the acquisition date, be allocated to each of the acquirer's cash-generating units, or groups of cash-generating units, that is expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated shall:**
>
> **(a) represent the lowest level within the entity at which the goodwill is monitored for internal management purposes; and**
>
> **(b) not be larger than an operating segment ~~based on either the entity's primary or the entity's secondary reporting format~~ determined in accordance with ~~IAS 14 *Segment Reporting*~~ IFRS 8 *Operating Segments*.**

6. Paragraph 36 of IFRS 8 specifies that upon transition, segment information for comparative periods is required to be presented on an IFRS 8 basis unless the information is not available and the cost to produce it would be excessive. There were no transition provisions specified for the consequential amendment to IAS 36. Where no transition provisions are provided, IAS 8 requires changes in accounting policy to be applied retrospectively (unless impracticable to determine either the period-specific effects or the cumulative effect of the change) and changes in accounting estimates to be applied prospectively.

7. Additionally, as part of the *Improvements to IFRSs* issued in April 2009 (April 2009 AIP), the IASB further amended paragraph 80(b) of IAS 36 to clarify that each unit or group of units to which goodwill is allocated shall:

> **(b) not be larger than an operating segment ~~determined in accordance with~~ as defined by paragraph 5 of IFRS 8 *Operating Segments* before aggregation.**

8. This April 2009 AIP amendment shall be applied prospectively for annual periods beginning on or after 1 January 2010. Earlier application is permitted.

9. The amendment in the April 2009 AIP is a clarification of the consequential amendment made to IAS 36 when IFRS 8 was published in November 2006. The November 2006 consequential amendment is therefore the key trigger for a potential change in the basis of allocation of goodwill to cash-generating units (CGUs) for impairment testing purposes.

10. The change from IAS 14 to IFRS 8 might require some entities to change the grouping of CGUs on which goodwill is tested for impairment. When entities test goodwill for impairment in the first year of adoption of the consequential amendment from IFRS 8 (or from the amendment included in the April 2009 AIP), some entities may need to recognise an impairment of goodwill, principally because of these changes in the segment definitions in IFRS 8 (and clarified by the April 2009 AIP).

11. Such situations may occur in particular when, according to IAS 36.80(b), goodwill was previously tested at the level of a geographical segment. Upon transition to IFRS 8, the entity might identify its operating segments based on the activities it is engaged in instead of a geographical disaggregation. The entity may, therefore, have to change the grouping of CGUs on which goodwill is tested.

12. The question asked of the IFRIC is **whether the incremental goodwill impairment charge (that would have been recognised in the prior year if CGUs were grouped by reference to IFRS 8) determined as a result of retrospective application of the change from IAS 14 to IFRS 8 should be presented as a prior period adjustment or a current period event**?

Analysis of the issue and staff recommendation

13. The staff note this issue is of particular relevance given the application of IFRS 8 for financial years commencing on or after 1 January 2009. Current indications are that two distinct views are emerging:

    (a) **View A – Prior period adjustment –** The amendment to IAS 36 when IFRS 8 was introduced did not include any transition provisions. Accordingly, paragraph 19b of IAS 8 requires that the change in accounting policy is accounted for retrospectively. Thus any impairment charge arising from the change in the definition of segments shall be recognised as a prior period adjustment.

    (b) **View B – Current period adjustment –** Any impairment charge recognised following the change in IFRS 8 should be recognised as a current year charge in profit or loss. There is no change in the policy for testing goodwill for impairment. Accordingly, IAS 36 continues to require that goodwill is tested for impairment at the level at which it is monitored for internal management purposes. The only change is in a limit on how that policy is applied.

View A – Prior period adjustment

14. Paragraph 36 of IFRS 8 requires retrospective application of the provisions of IFRS 8 to all comparative periods presented. Additionally, the introduction to Appendix B *Amendments to Other IFRSs* to IFRS 8 states:

    > The amendments in this appendix shall be applied for annual periods beginning on or after 1 January 2009. If an entity applies this IFRS for an earlier period, these amendments shall be applied for that earlier period. In the amended paragraphs, new text is underlined and deleted text is struck through.

15. The consequential amendment to IAS 36 does not provide explicit guidance on its application. Additionally, the introduction to the consequential amendment does not state its application as prospective. Therefore, based on the guidance in IAS 8, the consequential amendment to IAS 36 should be applied retrospectively.

16. A practical difficulty of applying View A is that management would need to be able to estimate the recoverable amount of the operating segment(s) as at a date in the

comparative period. This would often require the use of hindsight which the Board has previously discouraged.

View B – Current period adjustment

17. IFRS 8 has explicit transition provisions that require retrospective application of and presentation of segment information. IFRS 8 does make a consequential amendment to IAS 36 that only makes changes to the different terminology between IAS 14 and IFRS 8. However, IFRS 8 does not provide specific guidance on the application of IAS 36.

18. Additionally, the Board's recent amendment to IAS 36 included in the April 2009 AIP specifically states prospective application of that amendment. This AIP amendment was meant to clarify the Board's intentions surrounding the interaction between IAS 36 and the adoption of IFRS 8.

Staff recommendation

19. The current wording of IFRS 8 requires retrospective application of IFRS 8 upon its adoption. The introduction to Appendix B (Amendments to Other IFRSs) to IFRS 8 does not specify retrospective or prospective adoption, therefore, the general principles of IAS 8 presume retrospective adoption (which is consistent with the explicit statement on transition in paragraph 36 of IFRS 8). Paragraph 36 of IFRS 8 states that the comparative information shall be restated to conform to the requirements of this IFRS which is a standard with only disclosure requirements.

20. A view is that IFRS 8 does not require reperformance of the determination of measurements in accordance with IAS 36. Therefore, any impairment determined in the current period shall be recognised in the statement of comprehensive income (P&L) in the current period. Additionally, many entities may not have the appropriate fair value information based on the IFRS 8 CGU groupings for comparative periods and determination of those amounts could require the use of hindsight.

21. Finally, the view that any impairment determined in the current period shall be recognised in the current period P&L is consistent with the Board's view of the

amendment finalised in the *Improvements to IFRSs* issued in April 2009 clarifying paragraph 80(b) of IAS 36 that 'Each unit or group of units to which the goodwill is so allocated [for impairment testing purposes] shall…not be larger than an operating segment as defined by paragraph 5 of IFRS 8 Operating Segments before aggregation.' That amendment added paragraph BC228A that states:

> The Board considered the transition provisions and effective date of the amendment to paragraph 80(b). The Board noted that the assessment of goodwill impairment might involve the use of hindsight in determining the fair values of the cash-generating units at the end of a past reporting period. Considering practicability, the Board decided that the effective date should be for annual periods beginning on or after 1 January 2010 although the Board noted that the effective date of IFRS 8 is 1 January 2009. Therefore, the Board decided that an entity should apply the amendment to paragraph 80(b) made by *Improvements to IFRSs* issued in April 2009 prospectively for annual periods beginning on or after 1 January 2010.

22. Based on the above, in the staff's opinion, any impairment determined in the current period shall be recognised in the current period statement of comprehensive income (P&L).

Question 1 – Prior period adjustment v Current period adjustment
Does the IFRIC agree with the staff opinion that any impairment determined in the current period shall be recognised in the current period statement of comprehensive income (P&L)?

IFRIC Agenda Criteria

1. The staff's preliminary assessment of the agenda criteria is as follows:

   (a) *Is the issue widespread and practical?*

   Yes. Many entities will be applying IFRS 8 for the first time in 2009 and potentially face a change in their segments.

   (b) *Does the issue involve significantly divergent interpretations (either emerging or already existing in practice)?*

   Yes. We are aware of two views evolving, as presented above.

(c) *Would financial reporting be improved through elimination of the diversity?*

Yes. Financial reporting would be improved if diversity was eliminated.

(d) Is the issue sufficiently narrow in scope to be capable of interpretation within the confines of IFRSs and the Framework for the Preparation and Presentation of Financial Statements*, but not so narrow that it is inefficient to apply the interpretation process?*

Yes. The issue is sufficiently narrow in scope as it relates exclusively to impairment testing of goodwill and other IFRS (IFRS 8, IAS 8, IAS 36, Framework, etc) provide relevant guidance to support the interpretation.

(e) *If the issue relates to a current or planned IASB project, is there a pressing need for guidance sooner than would be expected from the IASB project? (The IFRIC will not add an item to its agenda if an IASB project is expected to resolve the issue in a shorter period than the IFRIC would require to complete its due process.)*

Not applicable as there is not a current or planned IASB project; therefore, yes, the only current options available to the IFRIC are to add the issue to its agenda or to recommend the IASB add a project to its agenda.

However, given that the provisions of IFRS 8 and its consequential amendment to IAS 36 are effective for annual periods beginning on or after 1 January 2009, meaning years ending on or after 31 December 2009, any formal guidance the IFRIC or IASB could provide would not likely be finalized in time to be of benefit to users.

2. In the staff's opinion, based on the assessment of the agenda criteria, not all criteria are satisfied. Therefore, the staff recommends that the IFRIC tentatively decide not to add the issue to its agenda.

Question 2 – IFRIC Agenda Criteria
Does the IFRIC agree with the staff recommendation that not all of the IFRIC agenda criteria are met?

Question 3 – IFRIC Tentative Decision
Does the IFRIC agree with the staff recommendation to tentatively decide not to add the issue to its agenda?

Question 4 – IFRIC Tentative Agenda Decision Drafting
Does the IFRIC have any comments on the draft wording for the tentative agenda decision in Appendix A?

[Appendix A is omitted from this observer note]