

VALUATION FOR IMPAIRMENT TESTING

A Comprehensive Reference under Ind AS 36

Impairment of Assets

Based on the Educational Material issued by the Accounting Standards Board
The Institute of Chartered Accountants of India

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1. Introduction and Background

Ind AS 36, Impairment of Assets, prescribes the procedures that an entity applies to ensure that its assets are carried at no more than their recoverable amount. An asset is carried at more than its recoverable amount if its carrying amount exceeds the amount to be recovered through use or sale of the asset. If this is the case, the asset is described as impaired, and the Standard requires the entity to recognise an impairment loss.

The Standard also specifies when an entity should reverse an impairment loss and prescribes the requisite disclosures. Proper impairment testing requires a rigorous valuation exercise to determine the recoverable amount, which is the cornerstone of the entire assessment framework.

This document provides a structured overview of the valuation principles and methodologies applicable for impairment testing, drawing upon the requirements of Ind AS 36 and the guidance issued by the Accounting Standards Board of the Institute of Chartered Accountants of India.

2. Scope of Ind AS 36

Ind AS 36 applies to the impairment of all assets, other than those specifically excluded. The following categories of assets are excluded from its scope:

- Inventories (covered under Ind AS 2)
- Contract assets and assets arising from costs to obtain or fulfil a contract recognised under Ind AS 115
- Deferred tax assets (covered under Ind AS 12)
- Assets arising from employee benefits (covered under Ind AS 19)
- Financial assets within the scope of Ind AS 109
- Biological assets related to agricultural activity measured at fair value less costs to sell (covered under Ind AS 41)
- Contracts within the scope of Ind AS 117, Insurance Contracts, that are assets
- Non-current assets or disposal groups classified as held for sale under Ind AS 105

Notably, Ind AS 36 applies to financial assets classified as subsidiaries, associates, and joint ventures, as well as to assets carried at revalued amounts under the revaluation model in Ind AS 16 and Ind AS 38.

3. Key Definitions

| Term | Definition |
|-----------------------------------|---|
| Carrying Amount | The amount at which an asset is recognised after deducting any accumulated depreciation (amortisation) and accumulated impairment losses thereon. |
| Cash-Generating Unit (CGU) | 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. |
| Corporate Assets | Assets other than goodwill that contribute to the future cash flows of both the CGU under review and other cash-generating units. |
| Costs of Disposal | Incremental costs directly attributable to the disposal of an asset or CGU, excluding finance costs and income tax expense. |
| Fair Value | The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (per Ind AS 113). |
| Impairment Loss | The amount by which the carrying amount of an asset or CGU exceeds its recoverable amount. |
| Recoverable Amount | The higher of an asset's (or CGU's) fair value less costs of disposal and its value in use. |
| Value in Use | The present value of the future cash flows expected to be derived from an asset or CGU. |

4. Identifying an Asset that may be Impaired

An entity shall assess at the end of each reporting period whether there is any indication that an asset may be impaired. If any such indication exists, the entity shall estimate the recoverable amount of the asset. Irrespective of whether there is any indication of impairment, the following assets must be tested for impairment at least annually:

- An intangible asset with an indefinite useful life
- An intangible asset not yet available for use
- Goodwill acquired in a business combination

4.1 External Sources of Information

The following external indicators must be considered, at a minimum, in assessing potential impairment:

- Observable indications that the asset's value has declined during the period significantly more than would be expected as a result of the passage of time or normal use
- Significant adverse changes in the technological, market, economic, or legal environment in which the entity operates, or in the market to which an asset is dedicated
- Increases in market interest rates or market rates of return on investments that are likely to affect the discount rate used in the value in use calculation and decrease the recoverable amount materially
- Carrying amount of the net assets of the entity is more than its market capitalisation

4.2 Internal Sources of Information

The following internal indicators must also be considered:

- Evidence of obsolescence or physical damage of an asset
- Significant changes in the extent to which, or manner in which, an asset is used (including the asset becoming idle, plans to discontinue or restructure operations, plans to dispose of an asset earlier than expected, or reassessment of useful life from indefinite to finite)
- Evidence from internal reporting that the economic performance of an asset is, or will be, worse than expected

4.3 Dividend from a Subsidiary, Joint Venture, or Associate

Where an investor recognises a dividend from a subsidiary, joint venture, or associate, impairment may be indicated if:

- The carrying amount of the investment in the separate financial statements exceeds the carrying amounts in the consolidated financial statements of the investee's net assets, including associated goodwill; or
- The dividend exceeds the total comprehensive income of the subsidiary, joint venture, or associate in the period the dividend is declared

Note: The list of indicators prescribed in Ind AS 36 is not exhaustive. Entities must also consider other events or circumstances that may indicate impairment, including those arising from geo-political disruptions and climate-related matters.

5. Measuring Recoverable Amount

Recoverable amount is the higher of an asset's or cash-generating unit's:

- Fair value less costs of disposal; and
- Value in use

It is not always necessary to determine both amounts. If either of these exceeds the asset's carrying amount, the asset is not impaired, and there is no need to estimate the other amount. Recoverable amount is generally determined for an individual asset, unless the asset does not generate largely independent cash inflows, in which case it is determined for the CGU to which the asset belongs.

5.1 Fair Value Less Costs of Disposal

Fair value is measured in accordance with Ind AS 113 and represents the exit price — the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. Costs of disposal are deducted from fair value and include:

- Legal costs
- Stamp duty and similar transaction taxes
- Costs of removing the asset
- Direct incremental costs to bring an asset into condition for its sale

Termination benefits and costs associated with reducing or reorganising a business following disposal are not direct incremental costs and are therefore excluded.

The three principal valuation techniques prescribed under Ind AS 113 are:

| Approach | Description |
|------------------------|---|
| Market Approach | Uses prices and other relevant information generated by market transactions involving identical or comparable assets. |
| Cost Approach | Reflects the amount that would be required currently to replace the service capacity of an asset (current replacement cost). |
| Income Approach | Converts future amounts (cash flows or income and expenses) to a single current (discounted) amount, reflecting current market expectations about future amounts. |

The inputs used in fair value measurement follow a three-level hierarchy: Level 1 (quoted prices in active markets), Level 2 (observable inputs other than quoted prices), and Level 3 (unobservable inputs).

5.2 Value in Use

Value in use is the present value of the future cash flows expected to be derived from an asset or CGU. Its calculation shall reflect:

- An estimate of the future cash flows expected to be derived from the asset
- Expectations about possible variations in the amount or timing of those future 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 those future cash flows

6. Estimating Future Cash Flows for Value in Use

6.1 Cash Flows to be Included

Estimates of future cash flows for value in use purposes shall include:

- Projections of cash inflows from the continuing use of the asset
- Projections of cash outflows necessarily incurred to generate those cash inflows (including preparation costs), attributable directly or allocated on a reasonable and consistent basis to the asset
- Net cash flows, if any, to be received or paid for the disposal of the asset at the end of its useful life
- For a partly-completed asset or CGU: all expected cash outflows required to make the asset ready for use or sale
- Routine capital expenditure necessary to maintain the level of economic benefits expected to arise from the asset in its current condition

6.2 Cash Flows to be Excluded

Estimates of future cash flows shall not include:

- Cash flows expected to arise from future restructurings to which the entity is not yet committed
- Future cash outflows that will improve or enhance the asset's performance, or the related cash inflows expected to arise from such outflows (until the related expenditure is actually incurred)
- Cash flows from financing activities
- Income tax receipts or payments
- Lease payments for recognised lease liabilities (unless the carrying amount of the lease liability is deducted from the CGU carrying amount)

6.3 Basis of Estimates and Projection Period

Cash flow projections for value in use shall be based on:

- Reasonable and supportable assumptions that represent management's best estimate of the economic conditions that will exist over the asset's remaining useful life, giving greater weight to external evidence
- The most recent financial budgets and forecasts approved by management, covering a maximum period of five years (unless a longer period can be justified from past experience)
- For cash flows beyond the budget or forecast period: extrapolation using a steady or declining growth rate, unless an increasing rate can be justified — this growth rate must not exceed the long-term average growth rate for the products, industries, or country in which the entity operates

Two present value approaches are permissible under Appendix A to Ind AS 36:

- Traditional approach: a single most-likely cash flow projection
- Expected cash flow approach: multiple probability-weighted cash flow projections

7. Discount Rate

The discount rate for value in use purposes shall be a pre-tax rate that reflects:

- Current market assessments of the time value of money; and
- Risks specific to the asset for which the future cash flow estimates have not been adjusted

The discount rate must not be entity-specific in nature. It represents the return that investors would require if they were to choose an investment generating cash flows of equivalent amounts, timing, and risk profile.

When an asset-specific rate is not directly available from the market, the entity may use the following as a starting point:

- The entity's weighted average cost of capital (WACC), determined using techniques such as the Capital Asset Pricing Model (CAPM)
- The entity's incremental borrowing rate
- Other market borrowing rates

The discount rate must be adjusted to:

- Reflect the specific risks associated with the asset's estimated cash flows (such as country risk, currency risk, and price risk)
- Exclude risks that are not relevant to the asset's estimated cash flows, or for which the cash flow estimates have already been adjusted (to avoid double-counting)
- Be independent of the entity's capital structure and the manner in which the purchase of the asset was financed
- Be converted to a pre-tax rate if the rate has been derived on a post-tax basis

A single discount rate is ordinarily used, but separate discount rates may be applied for different future periods where value in use is sensitive to differences in risks across periods, or to the term structure of interest rates.

8. Cash-Generating Units and Goodwill

8.1 Identification of Cash-Generating Units

A CGU is the smallest identifiable group of assets that generates cash inflows largely independent of those from other assets or groups of assets. Identification of CGUs involves the exercise of significant judgement and requires consideration of:

- How management monitors the entity's operations (e.g., by product lines, individual locations, districts, or regional areas)
- How management makes decisions about continuing or disposing of assets and operations

The identifying factor for a CGU is the existence of largely independent cash inflows, not independent net cash flows. Shared outflows (e.g., centralised infrastructure, marketing costs) are therefore not determinative.

If an active market exists for the output produced by an asset or group of assets, that asset or group shall be identified as a separate CGU, even if some or all of the output is used internally. Where internal transfer pricing affects cash inflows, management's best estimate of future arm's length prices shall be used.

CGUs shall be identified consistently from period to period for the same asset or types of assets, unless a change is justified.

8.2 Carrying Amount of a CGU

The carrying amount of a CGU includes only those assets that can be directly attributed, or allocated on a reasonable and consistent basis, to the CGU and that will generate the future cash flows used in determining the CGU's value in use. Liabilities are generally excluded, unless recoverable amount cannot be determined without considering such liabilities.

| Item | Treatment in CGU Carrying Amount |
|---|--|
| Corporate assets allocated on a reasonable basis | Included in the CGU's carrying amount (paragraph 101 of Ind AS 36). |
| Deferred tax assets on tax losses | Excluded — deferred tax assets are entity-specific, not CGU-specific (paragraphs 50 and 53A). |
| Decommissioning liability (present value) | Excluded unless the buyer of the CGU would be required to assume the liability; if so, deducted from both carrying amount and value in use (paragraph 78). |
| Pension obligation | Deducted from carrying amount where recoverable amount is determined after consideration of the pension obligation (paragraph 79). |

8.3 Goodwill — Allocation to CGUs

Goodwill acquired in a business combination shall, from the acquisition date, be allocated to each CGU (or group of CGUs) that is expected to benefit from the synergies of the combination. Each unit or group of units to which goodwill is allocated shall:

- Represent the lowest level within the entity at which the goodwill is monitored for internal management purposes; and
- Not be larger than an operating segment as defined in Ind AS 108, Operating Segments, before aggregation

A CGU to which goodwill has been allocated shall be tested for impairment annually, irrespective of whether any indication of impairment exists. The annual test may be performed at any time during the annual period, provided the same time is used consistently every year. If goodwill was allocated to a CGU during the current period, that CGU must be tested before the end of the current annual period.

Goodwill impairment loss shall not be reversed in a subsequent period.

9. Recognition and Measurement of Impairment Loss

If, and only if, the recoverable amount of an asset is less than its carrying amount, the carrying amount shall be reduced to its recoverable amount. That reduction constitutes an impairment loss, recognised immediately in profit or loss — unless the asset is carried at a revalued amount, in which case the impairment is treated as a revaluation decrease under the applicable standard.

After recognising an impairment loss, the depreciation or amortisation charge for the asset shall be adjusted prospectively to allocate the revised carrying amount (less residual value) over its remaining useful life.

9.1 Allocation of Impairment Loss for a CGU

An impairment loss for a CGU shall be allocated to reduce the carrying amounts of the assets of the unit in the following order:

- First: reduce the carrying amount of any goodwill allocated to the CGU
- Then: reduce the carrying amounts of the remaining assets of the CGU pro rata on the basis of each asset's carrying amount

In allocating an impairment loss, the carrying amount of any individual asset must not be reduced below the highest of:

- Its fair value less costs of disposal (if measurable)
- Its value in use (if determinable)
- Zero

Any excess impairment loss that cannot be allocated to an asset (because of the above floor) is allocated pro rata to the other assets of the unit.

9.2 Illustrative Example — Allocation of Impairment Loss

The following example illustrates the allocation of an impairment loss within a CGU:

| Asset | Carrying Amount (INR Cr.) | Recoverable Amount (INR Cr.) | Impairment Allocated (INR Cr.) | Revised Carrying Amount (INR Cr.) |
|-------|---------------------------|------------------------------|--------------------------------|-----------------------------------|
|-------|---------------------------|------------------------------|--------------------------------|-----------------------------------|

| | | | | |
|------------------|--------------|----------|----------------|------------|
| Goodwill | 300 | — | (300) | — |
| Land | 500 | 550 | None (RA > CA) | 500 |
| Building | 90 | 50 | (40) | 50 |
| Production Plant | 250 | 100 | (100) | 150 |
| Total | 1,140 | — | (440) | 700 |

Note: RA = Recoverable Amount; CA = Carrying Amount. The carrying amount of Land is not reduced as its recoverable amount exceeds its carrying amount. The building is written down to its fair value less costs of disposal floor. The residual impairment after goodwill write-off is allocated pro rata to Building and Production Plant.

10. Reversal of Impairment Loss

At the end of each reporting period, an entity shall assess whether there is any indication that an impairment loss recognised in prior periods for an asset other than goodwill may no longer exist or may have decreased. If such indication exists, the recoverable amount shall be estimated.

An impairment loss shall be reversed if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised.

10.1 Reversal for Individual Assets (Other than Goodwill)

The increased carrying amount attributable to a reversal of impairment loss shall not exceed the carrying amount that would have been determined (net of depreciation or amortisation) had no impairment loss been recognised in prior years. A reversal is recognised immediately in profit or loss, unless the asset is carried at a revalued amount.

10.2 Reversal for a CGU

A reversal of an impairment loss for a CGU shall be allocated to the assets of the unit (excluding goodwill) pro rata with the carrying amounts of those assets. In allocating a reversal, the carrying amount of an asset shall not be increased above the lower of:

- Its recoverable amount (if determinable); and
- The carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior periods

10.3 Reversal for Goodwill

An impairment loss recognised for goodwill shall not be reversed in a subsequent period. This prohibition is absolute and admits no exceptions.

11. Comparison: Fair Value Less Costs of Disposal vs. Value in Use

The following table summarises the key distinctions between the two methods for measuring recoverable amount:

| Parameter | Fair Value Less Costs of Disposal | Value in Use |
|---|---|---|
| Perspective | Market participants' assumptions to price the asset. | Entity-specific; considers entity-specific factors. |
| Starting Point | Entity-specific budgets/forecasts, adjusted for market conditions when using a present value technique. | Entity-specific budgets and forecasts approved by management. |
| Future Restructuring (uncommitted) | Included if a market participant would reasonably expect such restructuring. | Excluded — cash flows estimated in current condition only. |
| Asset Enhancements | Included if a market participant would reasonably expect such enhancements. | Excluded until expenditure is actually incurred. |

| | | |
|--|--|--|
| Discount Rate | Rate reflecting assumptions a market participant would use. | Pre-tax rate reflecting time value of money and risks specific to the asset. |
| Synergies / Entity-specific value | Excluded to the extent not available to market participants generally. | May be included as they are entity-specific. |

12. Key Disclosures

12.1 Disclosures for Each Class of Assets

For each class of assets, the following shall be disclosed:

- Amount of impairment losses recognised in profit or loss during the period and the relevant line item(s) of the statement of profit and loss
- Amount of reversals of impairment losses recognised in profit or loss during the period
- Amount of impairment losses on revalued assets recognised in other comprehensive income
- Amount of reversals of impairment losses on revalued assets recognised in other comprehensive income

12.2 Disclosures for Individual Assets and CGUs

For each individual asset (including goodwill) or CGU for which an impairment loss or reversal has been recognised, the following shall be disclosed:

- Events and circumstances that led to the recognition or reversal
- Amount of the impairment loss recognised or reversed
- For an individual asset: nature of the asset and, if applicable, the reportable segment to which it belongs
- For a CGU: description of the CGU, amount of impairment by class and by segment, and any changes in CGU identification since the previous period
- The recoverable amount of the asset or CGU, and whether it is fair value less costs of disposal or value in use
- If recoverable amount is fair value less costs of disposal: the fair value hierarchy level, valuation technique, key assumptions, and discount rate(s) used
- If recoverable amount is value in use: the discount rate(s) used in the current and previous estimate

12.3 Disclosures for CGUs Containing Goodwill or Indefinite-Life Intangibles

For each CGU (or group of CGUs) for which the carrying amount of goodwill or intangible assets with indefinite useful lives is significant relative to the entity's total, the following additional disclosures are required:

- Carrying amount of goodwill and indefinite-life intangibles allocated to the unit
- Basis on which recoverable amount has been determined (value in use or fair value less costs of disposal)
- Key assumptions on which cash flow projections are based, and management's approach to determining the values assigned
- The projection period used and justification if it exceeds five years
- The growth rate used to extrapolate projections and justification for any rate exceeding the long-term average
- Discount rate(s) applied
- Sensitivity analysis: if a reasonably possible change in a key assumption would cause the carrying amount to exceed the recoverable amount, the amount of the excess, the value of the key assumption, and the change required to equalise the two

13. Comparison with IAS 36 and AS 28

13.1 Ind AS 36 vs. IAS 36

| No. | Key Difference |
|-----|--|
| 1. | Paragraph 2(f) of IAS 36 (relating to investment property at fair value) is deleted in Ind AS 36, as Ind AS 40 requires the cost model. |
| 2. | Transitional provisions of IAS 36 are not included in Ind AS 36; instead, Ind AS 101 covers all transitional matters. |
| 3. | Different terminology is used (e.g., 'Statement of Profit and Loss' instead of 'Statement of Comprehensive Income'; 'Balance Sheet' instead of 'Statement of Financial Position'). |

| | |
|----|---|
| 4. | Paragraphs 25–27 and 5(b) of IAS 36 are deleted in Ind AS 36 as a consequence of Ind AS 113, Fair Value Measurement. |
| 5. | Paragraphs 91–95 (appearing as 'Deleted' in IAS 36) retain their numbering in Ind AS 36 for consistency. |
| 6. | References to certain Illustrative Examples of IAS 36 (not forming integral parts of the Standard) are not included in Ind AS 36. |

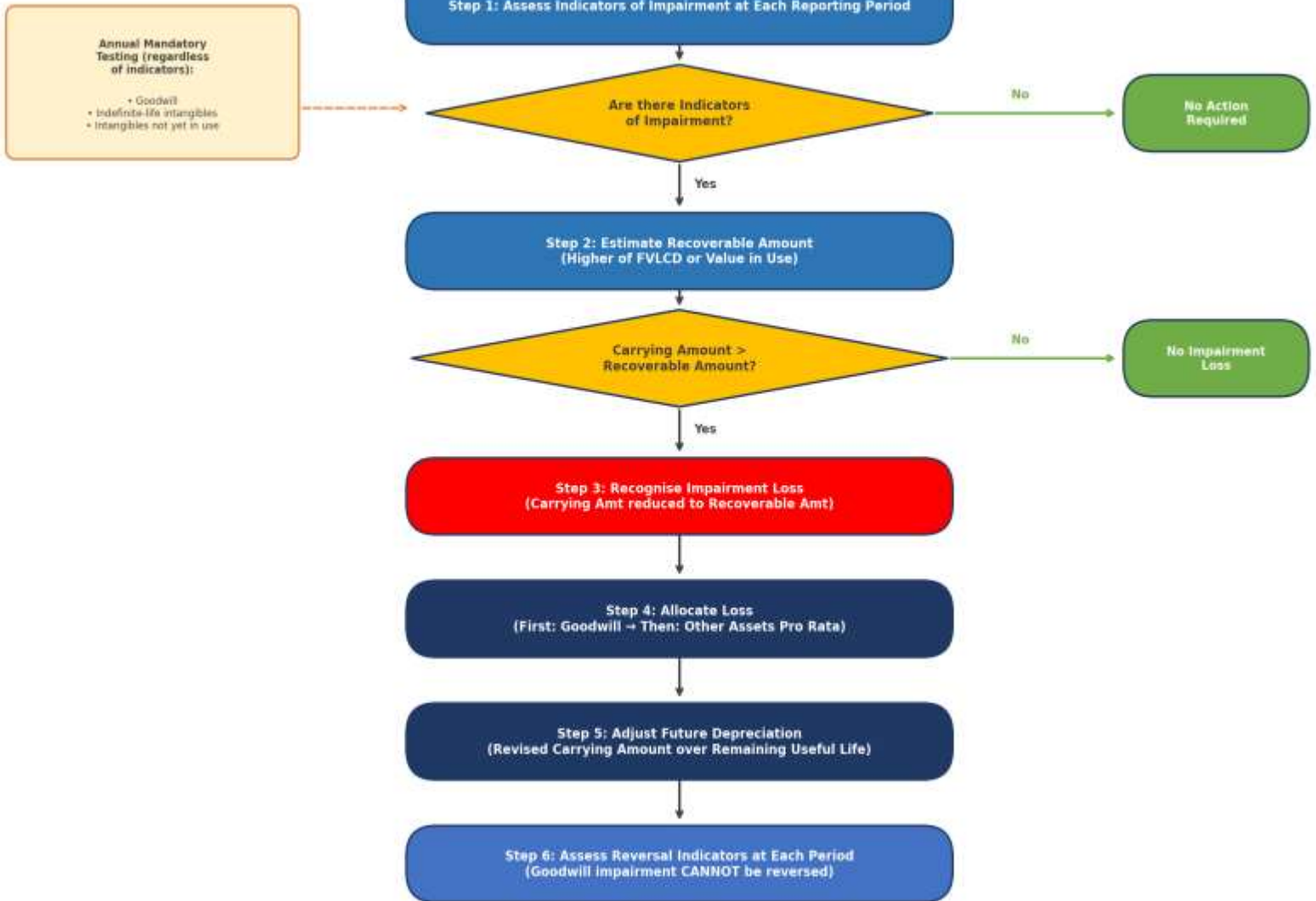
13.2 Ind AS 36 vs. AS 28

| No. | Key Difference |
|-----|---|
| 1. | Ind AS 36 applies to financial assets classified as subsidiaries, associates, and joint ventures. AS 28 does not apply to these assets. |
| 2. | Ind AS 36 explicitly excludes biological assets, assets arising from employee benefits, deferred acquisition costs, non-current assets held for sale, and discontinued operations. AS 28 does not have specific exclusions for these categories. |
| 3. | Ind AS 36 mandates annual impairment testing for intangible assets with indefinite useful lives, intangible assets not yet available for use, and goodwill acquired in business combinations. AS 28 does not require annual testing for goodwill absent an indicator. |
| 4. | Ind AS 36 prohibits the reversal of impairment losses on goodwill. AS 28 permits reversal if the original impairment was caused by a specific external event of exceptional nature that is not expected to recur and subsequent external events have reversed the effect. |
| 5. | In Ind AS 36, goodwill is allocated to CGUs or groups of CGUs expected to benefit from the synergies of the business combination. AS 28 employs a bottom-up and top-down approach for goodwill that cannot be reasonably allocated to individual CGUs. |
| 6. | Ind AS 36 uses the term 'fair value', while AS 28 refers to 'net selling value' for determining recoverable amount. |
| 7. | Ind AS 36 requires additional disclosures compared to AS 28. |

Visual Summary of Key Concepts

The following charts provide a visual reference to aid understanding of the key concepts covered in this document.

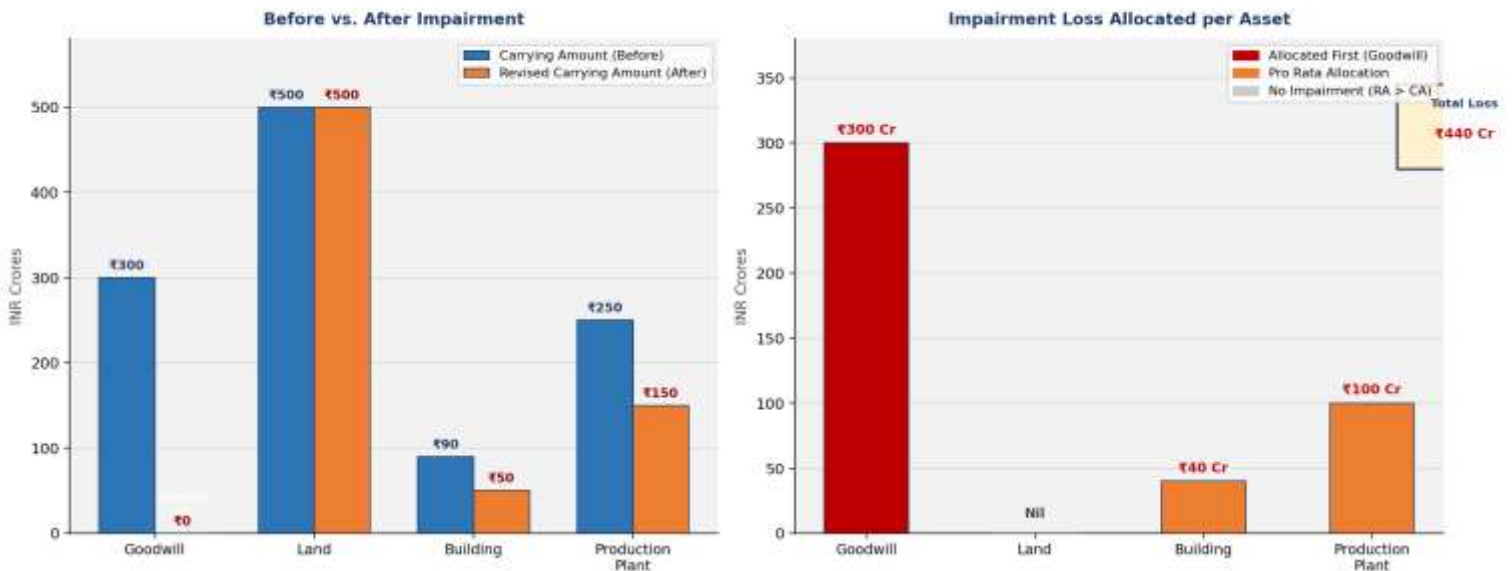
Ind AS 36 – Impairment Testing Process



Measuring Recoverable Amount – Decision Framework



Illustrative Example – Impairment Loss Allocation (Ind AS 36, Section 9.2)



Comparison: Ind AS 36 vs. IAS 36 vs. AS 28

Comparison: Ind AS 36 vs. IAS 36 vs. AS 28

| Feature | Ind AS 36 | IAS 36 | AS 28 |
|--|----------------------------|----------------------|----------------------------------|
| Scope - Financial Assets (Subs/JV/Assoc) | ✓ Applies | ✓ Applies | ✗ Not Applicable |
| Annual Mandatory Testing - Goodwill | ✓ Required | ✓ Required | ✗ Not Required |
| Goodwill Impairment Reversal | ✗ Prohibited | ✗ Prohibited | ✓ Permitted (exceptional events) |
| Goodwill Allocation Method | CGU / Group of CGUs | CGU / Group of CGUs | Bottom-up / Top-down |
| Terminology for Recoverable Amt | Fair Value (Ind AS 113) | Fair Value (IFRS 13) | Net Selling Value |
| Disclosure Requirements | Comprehensive (additional) | Comprehensive | Basic |

Note: ✓ = Applicable / Permitted ✗ = Not Applicable / Prohibited