Impairment of long-lived assets, goodwill and intangible assets

US GAAP and IFRS

Media & Entertainment
Overview of impairment principles

For a media and entertainment company that is considering converting to International Financial Reporting Standards (IFRS), one of the changes to consider is the impact on testing long-lived assets, goodwill and intangible assets for impairment. While the objective of testing for impairment under IFRS is similar to the objective of US GAAP, there are striking differences in the way that a media and entertainment company tests, recognizes and measures impairment under IFRS, as compared to US GAAP.

In addition to exploring the differences between US GAAP and IFRS in recognizing and measuring impairment, this publication focuses on practical issues for media and entertainment companies applying IFRS in an impairment analysis. It includes disclosures that illustrate how companies apply IFRS. We also indicate potential obstacles in converting to IFRS, thereby enabling media and entertainment companies to think strategically about the implications of adopting IFRS.

As shown in Figure 1, goodwill and intangible assets are often a significant portion of the values assigned and recognized in any business combination in the media and entertainment industry.

These assets frequently include brands and trademarks, mastheads, copyrights, music and film rights and catalogs, domain names, customer and contractual relationships, and other technology.

![Figure 1](image-url)

**Figure 1**
Purchase price allocations for media and entertainment companies

1 Other intangibles include music/film catalogs, domain names, etc.

Source: Ernst & Young sample of 49 Media & Entertainment business combinations in 2007.
A company reporting under IFRS follows the principles in IAS 36, Impairment of Assets (IAS 36). US GAAP and IFRS contain similar impairment indicators for assessing the impairment of long-lived assets (“non-current assets” in IFRS).

Both standards require the testing of goodwill and intangible assets with indefinite lives for impairment at least annually, and more frequently if impairment indicators are present. Long-lived assets are not tested annually, but rather when there are indicators of impairment. Both US GAAP and IFRS require write-downs of impaired assets and recognition of an impairment loss. These similarities and differences are summarized in Table 1.
### Overview of impairment principles (continued)

Table 1: Impairment tests under US GAAP vs. IFRS

<table>
<thead>
<tr>
<th>Method of determining impairment — long-lived assets</th>
<th>US GAAP</th>
<th>IFRS</th>
</tr>
</thead>
<tbody>
<tr>
<td>If impairment indicators exist, two-step approach requires first a recoverability test (carrying amount of the asset is compared to the sum of future undiscounted cash flows generated through use and eventual disposition). If the asset is not recoverable (as determined in the first step), the second step is to calculate the impairment loss.</td>
<td>If impairment indicators exist, one-step approach requires that impairment loss (if any) must be calculated.</td>
<td></td>
</tr>
</tbody>
</table>

| Impairment loss calculation — long-lived assets | The amount by which the carrying amount of the asset exceeds its fair value, as calculated in accordance with US GAAP. | The amount by which the carrying amount of the asset exceeds its recoverable amount. The recoverable amount is the higher of: (1) fair value less costs to sell, and (2) value in use (the present value of future cash flows in use including disposal value). ‘Fair value’ in IFRS might differ from US GAAP. |

| Allocation of goodwill | Goodwill is allocated to a reporting unit, which is defined in US GAAP as an operating segment or one level below an operating segment (component). | Goodwill is allocated to a cash-generating unit (CGU) or group of CGUs, which represents the lowest level at which the goodwill is monitored internally and cannot be larger than an operating segment. |

| Method of determining impairment — goodwill | Two-step approach requires a recoverability test to be performed first at the reporting unit level (carrying amount of the reporting unit is compared with the reporting unit fair value). If the carrying amount of the reporting unit exceeds its fair value, then calculate impairment loss. | One-step approach requires calculating the impairment loss for the CGU, or group of CGUs, by comparing the CGU’s (or group of CGUs) carrying amount, including goodwill, to its recoverable amount. |

| Impairment loss calculation — goodwill | The amount by which the carrying amount of goodwill exceeds the implied fair value, as defined, of the goodwill within its reporting unit. Fair value is determined in accordance with US GAAP. | All other assets are tested for impairment prior to testing goodwill for impairment. The impairment loss is the amount by which the CGU’s carrying amount, including goodwill, exceeds its recoverable amount. This loss is allocated first to reduce goodwill to zero, then to the other assets in the CGU on a pro rata basis, based on the carrying amount of each asset. However, the carrying amount of an asset within that CGU may not be reduced below the highest of (a) its fair value less costs to sell (b) its value in use, and (c) zero. |

| Impairment loss calculation — indefinite-lived intangible assets | The amount by which the carrying value of the asset exceeds its fair value. | The amount by which the carrying value of the asset exceeds its recoverable amount. |

| Reversal of loss | Prohibited for all assets to be held and used. | Prohibited for goodwill. Other long-lived assets must be reviewed annually for reversal indicators. If appropriate, loss may be reversed up to the newly estimated recoverable amount, not to exceed the initial carrying amount adjusted for depreciation. |
Figure 2 illustrates the process to follow when determining an impairment under IFRS.

**Figure 2**
Process for determining an impairment under IFRS

### Key
- **RA** = Recoverable amount
- **CA** = Carrying amount
- **CGU** = Cash-generating Unit

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**Convergence**

In 2002, the US Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) agreed to eliminate major differences between their standards. In 2006, the FASB and IASB agreed that impairment would be one of the short-term convergence projects; however, in 2008, the FASB and IASB deferred working on this project until completing other convergence projects. Thus, there are currently no plans to address differences between US GAAP and IFRS with respect to impairment.

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2 IASB and FASB Memorandum of Understanding, 2006 and 2008

3 Based on the IASB’s and FASB’s workplans dated as of February 1, 2011
Indicators of impairment for long-lived assets

In principle

At each reporting date, management assesses whether impairment indicators exist for long-lived assets. The presence of an indicator does not definitively mean that a long-lived asset is impaired; rather, it means that a company must perform the next step in determining whether impairment exists. Although both US GAAP and IFRS identify indicators, they both state that the lists are not intended to be all-inclusive, and there is significant overlap of the examples listed between the two standards. Internal and external indicators that are listed in IAS 36 are shown in Table 2.

Table 2: Impairment indicators under IFRS

<table>
<thead>
<tr>
<th>Internal indicators</th>
<th>External indicators</th>
</tr>
</thead>
<tbody>
<tr>
<td>▶ Evidence of obsolescence or physical damage</td>
<td>▶ An asset’s market value has declined significantly more than would be expected as a result of the passage of time or normal use</td>
</tr>
<tr>
<td>▶ Significant changes with an adverse effect on the company have occurred (or will take place in the near future) that change how an asset is used (e.g., an asset is idle, plans to discontinue or restructure the operation to which an asset belongs, plans to dispose of an asset before the previously expected date, or the re-assessment the useful life of an asset as finite, rather than infinite)</td>
<td>▶ Increase in market interest rates or other market rates of return on investments that are likely to affect the discount rate used in calculating an asset’s value in use and materially decrease the asset’s recoverable amount</td>
</tr>
<tr>
<td>▶ Evidence is available from internal reporting that indicates that the economic performance of the asset is unsatisfactory, or will be or is worse than expected</td>
<td>▶ Significant changes with an adverse effect on the company have occurred (or will take place in the near future) in the technological, market, economic or legal environment in which the company operates or in the market to which an asset is dedicated</td>
</tr>
<tr>
<td></td>
<td>▶ Carrying amount of the net assets of the company is more than its market capitalization</td>
</tr>
</tbody>
</table>
In practice

Regardless of whether a company is reporting under US GAAP or IFRS, media and entertainment companies face significant internal and external pressures that might indicate that an asset is impaired:

- Sustained pricing pressures
- Increasing start-up costs for new projects
- Declining sales of CDs and DVDs
- Decreasing newspaper and magazine circulation
- Greater competition between printed content and free online service
- Declining print advertising
- Less trade show business
- Significant slowdown in television advertising
- Weaker audience share
- Growing fragmentation in the television market
- Diminishing brand recognition and loyalty

When preparing a company’s first IFRS financial statements, if these indicators were present in the past or are currently present at the date of transition to IFRS, assets should be tested for impairment under IFRS, even if the test under US GAAP did not result in an impairment.

One European media company described the indicators that were relevant to its business and considered in its impairment test as follows:

“Impairment is applied to programming assets if their costs can presumably not be covered by future revenues. The reasons for this assumption might include changes in the advertising environment, changing audience tastes, media-law restrictions on the usability of films, licenses that expire prior to broadcasting, or if a production has been commissioned but is not pursued further.”

An Australian public relations and communications group stated the following when describing the factors that led to the impairment that it recognized:

“Our strategic branding initiative has provided the Group with the ability to win global clients and represents a key opportunity for growth. We have reduced 26 brands to one health care brand and three public relations brands. As a result of the brand rationalization initiative, brands which are no longer used have been impaired to nil carrying value.”
Testing level for impairment of long-lived assets

In principle

Under IFRS, if an impairment indicator exists for a long-lived asset, then the recoverable amount of the individual asset is compared to its carrying amount. However, in many cases, the recoverable amount of the individual asset cannot be estimated because the asset does not generate cash inflows independently of other assets. In such cases, the recoverable amount is estimated for a group of assets, or “cash-generating unit” (CGU). A CGU 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. Assets that do not generate independent cash flows, such as company headquarters or central facilities (“corporate assets” in IAS 36), are allocated to CGUs on a reasonable and consistent basis.

Under US GAAP, if an impairment indicator exists, a long-lived asset may be grouped with other assets and liabilities so that the impairment test is performed at the lowest level for which identifiable (net) cash flows are largely independent of the cash flows of other assets and liabilities. A long-lived asset (e.g., corporate headquarters) that does not have identifiable cash flows that are largely independent of the cash flows of other assets and liabilities and of other asset groups is allocated to an asset group that includes all assets and liabilities of the company.

In practice, there may not be a significant difference between the levels at which impairment tests are performed for long-lived assets under IFRS as compared to under US GAAP. This is because net cash flows frequently are dependent on other assets (and are therefore tested together under US GAAP), because the cash inflows depend on other assets (which would make them a cash-generating unit, tested together under IFRS). However, it is important to note that IFRS focuses only on inflows, whereas US GAAP focuses on net cash flows. Thus, there might be situations when assets are grouped together to test for impairment under US GAAP, but must be disaggregated into distinct cash-generating units under IFRS. In addition, the difference in how corporate assets are treated under IFRS as compared to US GAAP will be a change for many companies.
Under IFRS, a media and entertainment company may face challenges in identifying its CGUs. While a company may separately monitor cash inflows from individual radio stations, broadcast licenses, book titles, magazine titles or music masters, the cash flows might be dependent on other assets, as shown in Example 1.

In practice

Example 1: Identifying a cash-generating unit

A publishing company may monitor the cash inflows from each newspaper masthead separately, but if each of the newspapers contains mostly advertisements that are bundled with other mastheads owned by the publisher, such cash inflows may be interdependent.

When identifying the cash-generating unit for each masthead, it is helpful to make the assessment in two steps:

- **Step 1** — Identify the smallest aggregation of assets for which a stream of cash inflows can be identified. Management monitors the cash inflows from each masthead; this means that each newspaper might be a CGU.

- **Step 2** — Assess whether the cash inflows generated are independent of other cash inflows. The newspapers contain advertisements that are “mostly” bundled with other mastheads owned; this means that the cash inflows are not largely independent, and therefore, the mastheads would form one CGU on a combined basis.
Testing level for impairment of long-lived assets (continued)

In practice

When comparing financial statements of media and entertainment companies, at first glance, it appears as though IFRS permits great latitude in how a CGU is identified, because there seems to be a wide spectrum in the level at which CGUs are identified. In reality, this is not so simplistic. Much of the range exists because there is such diversity in how various media and entertainment companies deliver services and generate cash flows, as well as in the assets that each owns. That is, the differences in the CGUs reflect how each company operates and which assets each company owns, as shown in Examples 2 and 3.

<table>
<thead>
<tr>
<th>Segments</th>
<th>Cash-generating units</th>
</tr>
</thead>
<tbody>
<tr>
<td>Music</td>
<td>Music recording</td>
</tr>
<tr>
<td></td>
<td>Artist services and merchandising</td>
</tr>
<tr>
<td></td>
<td>Music publishing</td>
</tr>
<tr>
<td>Television</td>
<td>Pay TV</td>
</tr>
<tr>
<td></td>
<td>Network TV</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>Mobile</td>
</tr>
<tr>
<td></td>
<td>Broadband internet</td>
</tr>
<tr>
<td>Content</td>
<td>Content</td>
</tr>
</tbody>
</table>
Example 3: Segments vs. cash-generating units
A European broadcaster’s CGUs focus on revenues generated and assets held, within a given country:

<table>
<thead>
<tr>
<th>Segments</th>
<th>Cash-generating units</th>
</tr>
</thead>
<tbody>
<tr>
<td>Germany</td>
<td>Television, Radio</td>
</tr>
<tr>
<td>France</td>
<td>Television, Radio</td>
</tr>
<tr>
<td>Netherlands</td>
<td>Television, Radio</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>Television, Radio</td>
</tr>
<tr>
<td>Other regions</td>
<td>Television, Radio</td>
</tr>
</tbody>
</table>

The following are examples of how media and entertainment companies in Europe disclose their policies for identifying CGUs:

“...the group is viewed as a single cash-generating unit and the group’s three services are based on a shared technological platform and organizational structure. The same IT system is used to invoice all group customers and all three of the group’s services (TV, broadband and telephony) face the same risks.”

“[The Company’s CGUs] represent its investment in a geographical area of operation by business segment except for the content business, which is considered as a sole cash-generating unit for worldwide operations.”
Recoverable amount

In principle

If impairment indicators exist, the next step under IFRS (as shown in Figure 3) is to determine the recoverable amount of an asset (or CGU). The recoverable amount of an asset (or CGU) is the higher of “fair value less costs to sell” (FVLCS) and “value in use” (VIU), as shown in Figure 3. It is not always necessary to determine both FVLCS and VIU, because if either amount exceeds the carrying amount of the asset, the asset or CGU is not impaired. Therefore, in certain situations, it is not necessary to estimate the recoverable amount under both methods.

In contrast, under US GAAP, there is a two-step approach if impairment indicators exist. The first step compares the carrying amount of the asset to the sum of its future undiscounted cash flows generated through the asset’s use and eventual disposition. Undiscounted cash flows, calculated in accordance with US GAAP, will differ from the recoverable amount (FVLCS or VIU) calculated under IFRS.

Figure 3
Determining impairment loss under IFRS

Fair value less costs to sell \( \rightarrow \) Value in use

Maximum

Recoverable amount (1) \( \rightarrow \) Net book value (2)

If (1) < (2)

Write-off

Fair value less costs to sell

Fair value is the amount obtainable from the sale of an asset (or CGU) in an arm’s-length transaction between knowledgeable, willing parties. IAS 36 provides a hierarchy for determining fair value:

- The best evidence of fair value is a price in a binding sale agreement in an arm’s-length transaction.
- The next best evidence of fair value is the price of an asset that is traded in an active market.
- In all other cases, fair value is determined using the best information available, which may be using a market approach, income approach or cost approach (as shown in Figure 4).
When estimating FVLCS for a long-lived asset, valuation professionals consider the following:

- Future events that would affect the cash flows arising for a typical market participant that holds such asset; that is, the measurement is not company-specific.
- Information that is available without undue cost or effort about the market’s assessment of the future cash flows (e.g., normal due diligence is performed).
- Market assumptions, if there is data indicating that market participants would not use the same assumptions as the company.
- Current market prices, unless reliable evidence indicates that current transactions are not between willing parties (e.g., forced).
- Transaction costs that would be incurred at the reporting date, when disposing of an asset.

If it is not possible to estimate FVLCS with sufficient reliability, the recoverable amount of the asset or CGU is based solely on VIU.
The main concept of value in use is to measure the present value of future cash flows from an asset or CGU in its current state. The concept of VIU is unique to IFRS. A company reflects the following elements in its estimate of VIU:

- Cash flows derived from the asset
- Expectations about variations in the amount or timing of cash flows
- Time value of money, using the current market risk-free rate of interest
- Price for bearing the uncertainty inherent in the asset
- Other factors, such as illiquidity, that market participants reflect in estimating the cash flows that the company expects to derive from the asset

In contrast to FVLCS, value in use is a company-specific measurement. The discounted cash flows are based on:

- Management’s best estimate of the range of economic conditions that will exist over the remaining useful life of the asset.
- The most recent financial budgets/forecasts approved by management, but excluding any estimated cash inflows or outflows from borrowing costs, income taxes, restructuring events or enhancing the asset. The projections based on these cash budgets/forecasts may not include more than five years, unless a longer period can be justified.
- Extrapolations of cash flows (beyond the period covered by the budgets/forecasts per the item above) using a steady or declining growth rate for subsequent years. The growth rate generally may not exceed the long-term average growth rate for products, industries or countries in which the company operates.

The discount rate is a pre-tax rate that reflects current market assessments of the time value of money, and the risks specific to the asset for which management did not adjust the future cash flows. This rate is estimated from the rate implicit in current market transactions for similar assets or from the weighted-average cost of capital of a listed company that has a single asset (or a portfolio of assets) similar in terms of service potential and risks to that asset.

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In practice

When there are impairment indicators and it is necessary to determine the recoverable amount, media and entertainment companies generally estimate VIU first (before estimating FVLCS), because, in practice, VIU is generally easier to determine for the types of assets they hold, as explained below. When VIU exceeds the carrying amount of the asset or CGU, there is no impairment and no further testing is required, as shown in Figure 3. However, when VIU is less than the carrying amount of the asset or CGU, management must also estimate FVLCS to determine the recoverable amount and whether an impairment exists. If it is not possible to determine FVLCS, the company uses VIU as its recoverable amount.\(^5\)

Fair value less costs to sell

While IFRS provides a hierarchy for determining FVLCS, management might find that the first and second options are rarely used for a media or entertainment asset for the reasons described below.

In practice, there is rarely a binding sale agreement in an arm’s-length transaction for the intangible asset being tested, which is the best evidence of fair value, because media and entertainment intangible assets are often unique. If there is a binding sale agreement, the asset is either already classified as held for sale, in which case the rules in IFRS 5, Non-current Assets Held for Sale and Discontinued Operations, apply, or the asset is about to be reclassified (to held for sale) and must be tested for impairment as described above.\(^5\)

The next best evidence of fair value is the price of an asset that is traded in an active market. IAS 36 currently defines an active market as one in which all of the following conditions exist:

- Items traded are homogeneous
- Willing buyers and sellers can normally be found
- Prices are available to the public

\(^5\) If there were a binding sale agreement for the specific intangible asset that is owned by the company, that asset would be outside the scope of IAS 36, because it would be held for sale in accordance with IFRS 5. However, IFRS 5 requires such assets to be measured immediately before its initial classification as held for sale in accordance with applicable IFRS. Since a decision to sell is a triggering event for an impairment review, any existing impairment is recognized at that time.
As a part of the joint project on fair value measurement, the definition of “active market” under IFRS may change. The IASB’s Exposure Draft on Fair Value Measurement issued in May 2009 proposed that an active market is “a market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.” In practice, this change should have little effect for media and entertainment companies.

Active markets are often scarce for unique intangible assets such as those held by media and entertainment companies (e.g., catalogs of music rights, TV rights). As a result, given the specific characteristics (e.g., the quality and size of the catalog, titles) of most intangible assets held by media and entertainment companies, FVLCS is usually estimated based on recent transactions for similar assets in the same industry. The best information available at the end of the reporting period is used to estimate the price that would be payable in an arm’s length transaction between knowledgeable, willing parties.

Where an income approach (e.g., discounted cash flows) is used to estimate fair value less costs to sell, the amounts used (or discount rate) must reflect market participant assumptions, and not company-specific assumptions. For example, in some cases, the cash flows applicable for a market participant might differ from the company-specific cash flows when management intends to use the intangible asset differently than a market participant would, as shown in Example 4.
Example 4: Differences in fair value based on cash flows vs. value in use

A media company acquired an intangible asset that it does not intend to use for competitive or other reasons (e.g., a brand name for which it has a similar brand name). Since the media company has a similar brand name, management does not intend to use that brand name post-acquisition. Sales will be discontinued under the acquired brand name, thereby eliminating competition and enhancing the value of its own brand name. Therefore, the cash flows under the acquired brand name will be minimal.

As indicated above, the fair value of the brand name has to be determined based on its use by other market participants. Accordingly, management’s future intentions about the brand name should only be reflected in determining the fair value if that is what other market participants would do. In most situations, this would not be the case, because there are probably other market participants that would continue to use the brand name, and therefore, it would have a value. In fact, management probably could have sold the brand name, but decided not to, in order to protect its own brand name.

Accordingly, the fair value is estimated for that brand name based on its value (future cash flows) to other market participants—not the media company itself.

Value in use

When calculating VIU, assumptions in the cash flow projection must be reasonable and comply with IFRS. The concept of VIU does not exist in US GAAP, and accordingly, any cash flow forecasts used for any impairment tests under US GAAP may need to be modified to comply with IFRS.

For example, when estimating cash flows for a film under IFRS, management might consider the following (which it might also have considered when estimating cash flows for its US GAAP impairment test):

- Performance of the film in prior markets, if previously released
- Public perception of the film’s story, cast, director, or producer
- Historical results of similar films
- Historical results of the cast, director or producer on prior films
- Length of the film
To measure VIU, cash flow projections are based on the most recent financial budgets or forecasts approved by management, extrapolating the projections thereafter using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified. However, if the budgets or forecasts extend beyond five years, there is a presumption in IFRS not to use the projections after five years, unless a longer period can be justified. A longer cash flow period can be justified if this represents the characteristics of the assets more appropriately, and reliable forecasts can be made.

For example, if management prepares forecasts for seven years, it is generally appropriate to only use the specific forecasts for the first five years, and then an extrapolation (steady, declining, or, if justified, increasing) thereafter. However, using more than five years of specific forecasts might be justified if management can accurately project those cash flows. This might be the case for a license, publishing right, broadcast right or copyright for which management can reliably forecast cash flows.

The cash outflows that management uses to determine fair value under US GAAP (which reflect market participant assumptions) must be adjusted to company-specific assumptions before such cash flows can be used to determine VIU under IFRS.

Consider the following examples:

- If the company would have lower costs than other market participants due to synergies that would not be available to other market participants, the cash outflows in the fair value calculation used for US GAAP must be decreased to the company-specific amount for the VIU calculation.

- If the company has higher costs than other market participants, because the company would benefit from a reorganization to which management has not yet committed, the amounts in the fair value calculation used for US GAAP must be increased to the company-specific amount for the VIU calculation.

In addition, IFRS specifically requires VIU to be estimated using pre-tax cash flows. Therefore, if post-tax amounts were used in the cash flow forecasts used to determine fair value under US GAAP, the amounts will need to be adjusted to pre-tax amounts for the VIU calculation.

The discount rate would also have to be adjusted from that of a market participant (which was used to determine fair value under US GAAP) to a company-specific rate for the VIU calculation. IAS 36 requires the use of pre-tax discount rates when determining VIU. In practice, post-tax costs of equity are generally used in the computation of the discount rate.
Discounting post-tax cash flows at a post-tax discount rate should give the same results as discounting pre-tax cash flows at a pre-tax discount rate, when there are neither temporary differences nor available tax losses at the measurement date.

In practice, using a post-tax discount rate, grossed-up by a standard rate of tax, is often a reasonable estimate of the pre-tax rate.

When determining value in use for a media or entertainment intangible asset or CGU, the valuation expert considers trends in consumer demand, for example, toward new media and individual entertainment. Advertising revenues and trends continue to be an area of focus, as advertising revenues shift between different types of media, and are subject to the cyclical trends of the economy.

A European publishing company describes its process for estimating value in use:

“Projected cash flows are based on internal estimates for three planning periods. Two additional planning periods are applied in addition. For periods beyond this detailed horizon, a perpetual annuity is recognized, taking into account individual business-specific growth rates...”

A European communications company describes its process for estimating recoverable amount:

“During the fourth quarter of 2009, [the Company] tested the value of goodwill allocated to its cash-generating units (CGU) or groups of CGUs applying the same valuation methods used every year... The recoverable amount is determined as the higher of the value in use determined by the discounted value of future cash flows (discounted cash flow method (DCF)) and the fair value (less costs to sell), determined based on market data (stock market prices, comparison with similar listed companies, comparison with the value attributed to similar assets or companies in recent transactions). The test was performed by [the Company] on the basis of an internal valuation of the recoverable amounts, except in the case of [two CGUs] for which [the Company] required the assistance of independent experts. Regarding [the first CGU], the recoverable amount was determined using usual valuation methods (DCF and stock market multiples) using financial assumptions consistent with previous years, which are as follows regarding the DCF method: discount rate of 8.50% (compared to 9.30% as of December 31, 2008) and perpetual growth rate of 1.00% (unchanged compared to December 31, 2008)... management concluded that the carrying value exceeded the recoverable amount of [the CGU] and consequently recognized an impairment loss of €616 million as of December 31, 2009...”
Impairment testing for long-lived assets with definite lives

In principle

Under both IFRS and US GAAP, long-lived assets with definite lives are tested for impairment when indicators exist. However, assuming indicators exist, the impairment tests differ under IFRS and US GAAP.

Under IFRS, there is a one-step approach, which requires management to calculate the recoverable amount. When the recoverable amount of an asset or CGU is less than its carrying amount, then the carrying amount of the asset or CGU is reduced to its recoverable amount. The difference represents the impairment loss. When allocating an impairment loss to assets within a CGU (or group of CGUs), the carrying amount of an asset is not reduced below the higher of:

- Fair value less cost to sell
- Value in use
- Zero

In contrast, under US GAAP, there is a two-step approach. The first step compares the carrying amount of the asset with the sum of its future undiscounted cash flows generated through the asset’s use and eventual disposition. If the carrying amount of the asset is greater than the cash flows, the asset is not recoverable, and the second step is performed, which is to calculate the impairment loss. The impairment loss is the amount by which the carrying amount of the long-lived asset exceeds its fair value.
**In practice**

Reporting under IFRS could result in recognizing an impairment loss for a long-lived asset at an earlier reporting date, or at a different amount, as compared to reporting under US GAAP, as shown in Example 5 (assuming that impairment indicators exist under both IFRS and US GAAP). This is because US GAAP uses a two-step approach, which first determines if the carrying amount is less than undiscounted cash flows (step 1). Only where this occurs does the company then calculate the impairment loss (step 2).

Because the VIU concept does not exist in US GAAP, the impairment loss would be less under IFRS than under US GAAP when VIU is greater than FVLCS (assuming an impairment loss is actually recognized under US GAAP).

**Example 5: Recoverable amount under IFRS vs. US GAAP**

A media company owns a customer list with the following characteristics:

- Carrying amount is $1.0 million
- Undiscounted cash flows are $1.2 million
- VIU (the discounted cash flows) is $0.9 million
- FVLCS is $0.7 million

An indicator of impairment exists under both US GAAP and IFRS.

Under US GAAP, the company does not recognize a loss on impairment because it passed “step 1.” That is, the undiscounted cash flows ($1.2 million) are greater than the carrying amount ($1.0 million) and therefore, the company does not perform “step 2.”

However, under IFRS, the company recognizes an impairment loss of $0.1 million, which is the difference between the $1.0 million carrying amount and the VIU of $0.9 million, because IFRS uses a single step and does not consider undiscounted cash flows. The company uses VIU (that is, discounted cash flows), as the recoverable amount, because it is greater than the FVLCS.
Reversing impairment losses

In principle

Under IFRS, at the end of each reporting period, management assesses if there is any indication that an impairment loss recognized in prior periods (for assets other than goodwill) no longer exists or has decreased. If any such indication exists, management estimates the recoverable amount of that asset. IAS 36 provides indicators to consider, which generally mirror the indicators in Table 2. If there are changes in the estimates used to determine the asset’s recoverable amount, the company reverses the impairment loss on that asset.

However, the revised carrying amount (after reversal) may not exceed the carrying amount that the company would have recognized (net of amortization or depreciation, if applicable) if the company had not recognized an impairment loss in prior reporting periods. This is a significant difference from US GAAP, which does not permit any reversals of impairment for any assets.
The ability to reverse impairment losses is a significant change for media and entertainment companies converting to IFRS from US GAAP. It might be appropriate to reverse an impairment charge in situations such as those described in Example 6.

Example 6: Reversing an impairment charge
An Australian entertainment company manufactured an interactive video game. After initial release, unit sales were lower than projected. This resulted in the carrying value of the software being higher than the recoverable amount, and the company recognized an impairment loss. The following year, a new gaming platform was released that was better suited to the game’s graphic abilities. As a result, sales outperformed the revised estimates. Because the advancement in technological hardware favorably affected the economic performance of the software, management determines the new recoverable amount for the software and reverses the impairment loss if the new recordable amount exceeds the carrying amount.

A European advertising company discloses its policy on reversal of impairment as follows:

“An impairment loss for an individual asset or cash generating unit shall be reversed if there has been a change in estimates used to determine the recoverable amount since the last impairment loss was recognized and is only reversed to the extent that the asset’s carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.”
Allocation of goodwill

In principle

While under both US GAAP and IFRS goodwill is grouped with other assets for testing impairment, differences may arise in how assets are grouped, which could affect the outcome of the impairment analysis (i.e., whether there is an impairment loss or the amount of the impairment loss).

Under IFRS, goodwill is allocated to a CGU or group of CGUs that represents the lowest level within the company at which goodwill is monitored by management, and cannot be larger than an operating segment, as defined in IFRS 8, Operating Segments. Similar to US GAAP, which requires allocation of goodwill to reporting units, under IFRS, goodwill is allocated to the CGU (or group of CGUs) that is expected to benefit from the synergies of the business combination in which the goodwill arose. This requirement applies irrespective of whether other assets or liabilities of the acquiree are assigned to that CGU (or group of CGUs).

Under US GAAP, goodwill is included in an asset group only if the asset group is or includes a reporting unit, which is an operating segment (as defined in US GAAP) or one level below an operating segment (component). A component of an operating segment is a reporting unit if the component constitutes a business for which discrete financial information is available and segment management regularly reviews the operating results of that component.

However, two or more components of an operating segment are aggregated and deemed a single reporting unit if the components have similar economic characteristics. An operating segment is deemed a reporting unit if all of its components are similar, if none of its components is a reporting unit or if it comprises only a single component.

While the definitions of “operating segment” are largely converged under IFRS and US GAAP, IFRS states that segments are determined based on the management approach, regardless of form of organization. This definition contrasts with US GAAP, in which companies with a “matrix” form of organization (that is, business components are managed in more than one way and the chief operating decision maker reviews all of the information provided) must determine segments based on products and services.
The following examples indicate how media and entertainment companies in Europe disclose their policies for allocating goodwill to each CGU:

“[The company] allocates its goodwill to CGUs that represent its investment in a geographical area of operation by business segment except for the content business, which is considered as a sole cash-generating unit for worldwide operations.”

“Goodwill and intangible assets to which it is not possible to directly match independent cash flows are grouped together, at the time they are first recorded, into the Cash-Generating Unit to which they belong.”

In practice

In practice, management may not directly monitor goodwill, although it may monitor the synergies that were the basis of the goodwill allocation or use other surrogates for direct monitoring. Regardless of this fact, under both IFRS and US GAAP, goodwill must be allocated to a CGU (or group of CGUs), or to a reporting unit, as applicable.

As noted above, the differences between US GAAP and IFRS might affect whether there is an impairment loss or the amount of the impairment loss, as shown in Example 7.

Example 7: Allocating goodwill to CGUs vs. Reporting Units

A media company has two operating segments: music and television. The music segment has three divisions: music recording, merchandising and music publishing. Each division has discrete cash inflows and financial information, which includes a goodwill allocation from acquisitions that benefit that division. Management regularly reviews the operating results of each division.

Under US GAAP, the three music divisions are each “components.” The company aggregated the music divisions (components) together as a “music” reporting unit for goodwill allocation and impairment testing, because they had similar economic characteristics, and thus qualified for aggregation as a reporting unit under US GAAP.

Under IFRS, the three music divisions are each CGUs. Because each division is a CGU, and goodwill is monitored at the division level, management is required to assess goodwill impairment for each music division separately.
Impairment testing for goodwill

In principle

IFRS includes specific requirements for recognizing and measuring an impairment of goodwill. Similar to US GAAP, under IFRS, management assesses impairment at the same time every year.

IFRS requires a cash-generating unit (including those containing goodwill) to be tested for impairment if indicators exist. US GAAP requires testing goodwill for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of the reporting unit below its carrying amount. Thus, in practice, there is not a significant difference in when impairment testing is required between reporting periods.

Unlike US GAAP, IAS 36 allows previous impairment calculations to be re-used when all of the following criteria are met:

- The assets and liabilities comprising the CGU (or group of CGUs) did not change significantly since the most recent calculation of recoverable amount
- The previously calculated recoverable amount exceeded the carrying amount by a substantial margin
- There is a remote likelihood that an updated calculation of the recoverable amount would be less than the asset’s carrying amount
The carrying amount of the CGU or group of CGUs, including goodwill, is compared with the recoverable amount of the CGU or group of CGUs. If the carrying amount of the CGU or group of CGUs exceeds the recoverable amount (the higher of the FVLCS or VIU) of the CGU or group of CGUs, a company recognizes an impairment loss on goodwill.

The impairment loss on the CGU or group of CGUs equals the excess of the carrying amount of the CGU or group of CGUs, including goodwill, over the recoverable amount of the CGU or group of CGUs. Such impairment loss is allocated first to reduce goodwill to zero; then the carrying amount of other assets in the CGU or group of CGUs are reduced pro rata, based on the carrying amount of each asset in the CGU or group of CGUs. However, as noted above, the carrying amount of an asset (within the CGU or group of CGUs) is not reduced below the higher of fair value less cost to sell, value in use or zero. The impairment loss that would have otherwise have been allocated to the assets is allocated pro rata to other assets within the CGU or group of CGUs.
However, before assessing impairment for a CGU or group of CGUs that contains goodwill, if there is an indication that an asset within the CGU or group of CGUs is impaired, management first assesses that asset for impairment, in accordance with the requirements discussed above, before assessing the CGU or group of CGUs for goodwill impairment.

In contrast, under US GAAP, goodwill is tested for impairment in two steps:

- **Step 1**: The fair value of the reporting unit is compared with its carrying amount. If the carrying amount of the reporting unit exceeds its fair value, perform step 2 to measure the amount of impairment loss that is recognized.

- **Step 2**: The goodwill impairment loss is the amount by which the carrying amount of the goodwill exceeds the implied fair value of the goodwill. The “implied fair value of the goodwill” is determined by assigning the fair value of the reporting unit to all of the assets and liabilities of that unit (including any unrecognized intangible assets) as if the reporting unit was acquired in a business combination. The amount of the impairment loss is limited to the carrying amount of the goodwill.
Media and entertainment companies may test different CGUs or groups of CGUs for impairment at different times, and should determine the optimal time for assessing CGUs or groups of CGUs based on the availability of data. Seasonality of businesses, the availability of forecast or budget figures, and the year-end closing process timetable should be considered when determining at which point it will test for impairment each year, as shown in Example 8.

Example 8: Timing of impairment tests
A US multimedia company applying IFRS determines that the optimal time for assessing impairment for its CGUs are as follows:

- Advertising — in May, because that is when it purchases the “up fronts” for the next season
- Film — in December, which is the end of the Christmas film season and coincides with its fiscal year-end

However, caution should be exercised if a company uses more than one date for testing impairment. When testing a CGU or group of CGUs that contains goodwill for impairment, if there is an indication that an asset within the CGU or group of CGUs is impaired, the company must first test that asset for impairment before testing the CGU or group of CGUs for goodwill impairment. In addition, if the annual impairment test for a CGU or group of CGUs containing goodwill is during the reporting period, the recoverable amount might still have to be estimated for that CGU or group of CGUs at the end of the reporting period if indicators of impairment exist for one of the CGUs in that group.
In practice

A European media company discloses its policy for testing impairment of goodwill and CGUs as follows:

“[The] Group tests the Group’s goodwill for impairment at least once a year, in compliance with the Group’s reporting policies. Deciding the recoverable amount of a line of business to which goodwill is attributed involves management estimates. The recoverable amount is the higher of the fair value less costs to sell, and the value in use. The Company normally determines these values using methods based on discounted cash flows. These discounted cash flows are founded on five-year projections built on financial plans approved by management. The cash flow projections take account of past experience, and are based on management’s best estimates of future developments. Cash flows beyond the planning period are extrapolated using individual growth rates. The most important assumptions underlying the changes in value in use involve estimates of growth rates, weighted average costs of capital, and tax rates.

These assumptions, as well as the method employed, may have a material effect on the resulting values, and ultimately on the amount of a possible impairment of goodwill. If property, plant and equipment and intangible assets are tested for impairment, determining the recoverable amount of the assets likewise involves management estimates that may have a significant influence on the resulting values and ultimately on the amount of a potential impairment. Impairment losses for goodwill cannot be reversed.”

A European media company describes its process for testing goodwill for impairment:

“The impairment test for [one CGU’s] goodwill is based on management’s business forecast in a detailed planning period of five years... For impairment testing, a growth rate of 1% was assumed for the period after the end of the detailed planning period. Accordingly, it was ascertained that no impairment was needed for the goodwill carried in the financial [statements]. Validation with stock market prices over the period prior to and on the balance sheet date confirmed this estimate.”
### Example 9: Goodwill impairment calculation

A broadcaster has one CGU related to its network.

#### Year 1

**Facts:**
- Carrying amount of network/CGU is $1,400
- Additionally, there is $500 of goodwill associated with the network/CGU
- FVLCS of the network/CGU is $1,600
- VIU of the network/CGU is $1,550

**Analysis:**
The recoverable amount of the network/CGU is therefore $1,600 (FVLCS), which is the greater of FVLCS and VIU. The difference in the recoverable amount of the network/CGU ($1,600) and the carrying amount of $1,900 (the sum of $1,400 and $500 of goodwill) is $300. This amount is attributed to goodwill impairment.

#### Year 2

**Facts:**
- Carrying amount of network/CGU is $1,350
- Additionally, there is $200 of goodwill associated with the network/CGU ($500 of original goodwill less $300 impairment recognized in Year 1)
- FVLCS of the network/CGU is $1,600
- VIU of the network/CGU is $1,650

**Analysis:**
The recoverable amount of the network/CGU is therefore $1,650 (VIU), which is the greater of FVLCS and VIU. The difference in the recoverable amount of the network/CGU ($1,650) and the carrying amount of $1,550 (the sum of $1,350 and $200 goodwill) indicates there is no impairment of the network/CGU in Year 2. The broadcaster may not reverse any of the $300 of goodwill impairment charge from Year 1 under IFRS.
Impairment testing for intangible assets with indefinite lives

In principle

Intangible assets with “indefinite” lives are those assets for which unforeseeable factors may affect management’s ability and intention to maintain the asset at its standard of performance assessed at the time of estimating the asset’s useful life. “Indefinite” should not be confused with “infinite.” For example, depending on the facts and circumstances, a broadcasting license might be deemed to have an indefinite life.

An intangible asset with an indefinite useful life may generate independent cash inflows as an individual asset, in which case the impairment testing for a single intangible asset applies (as discussed above with respect to intangible assets with a definite life). Alternatively, if the indefinite-lived asset does not have independent cash inflows, it is tested as part of a CGU, as described above, and that CGU has to be tested for impairment annually. However, the most recent calculation of such an asset’s recoverable amount may be re-used in the impairment test in the current reporting period if certain criteria are met (the same criteria that apply for re-using a goodwill impairment test, discussed above).

Impairment losses on intangible assets with an indefinite useful life are recognized the same as for intangible assets with definite useful lives, either as an individual asset or as part of a CGU, as applicable. However, there is an important distinction when allocating losses in a CGU, between how goodwill and intangible assets with an indefinite useful life are treated. As described above, if goodwill forms part of the assets of a CGU, any impairment loss first reduces the goodwill, and thereafter, the remaining assets are reduced pro rata. However, if an intangible asset with an indefinite life is part of a CGU that is impaired, there is no requirement to write down the intangible asset with the indefinite life before the other assets in the CGU; rather all assets are written down pro rata.
In practice

Assets that have “indefinite” lives under US GAAP will need to be re-evaluated to assess whether they have “indefinite” lives under IFRS.

If there was sufficient “cushion” between the recoverable amount and the carrying amount in the last impairment test calculation and little has changed in the CGU that includes the intangible asset with an indefinite life, that calculation can be re-used, rather than starting from scratch. Using this practical exception considerably reduces the work involved in the impairment annual test. However, the impairment test cannot be rolled forward forever; caution is needed when estimating whether circumstances have changed sufficiently to require a new test.

Two European M&E companies disclose their policies for assessing impairment of indefinite-lived intangible assets as follows:

“Each time events or changes in the economic environment indicate a current risk of impairment of goodwill, other intangible assets, property, plant and equipment and assets in progress, [the Company] re-examines the value of these assets. In addition, goodwill, other indefinite life intangible assets and intangible assets in progress are all subject to an annual impairment test during the fourth quarter of each fiscal year.”

“Included in market and customer-related intangible assets are ... brands and imprints relating to [the Company] determined to have indefinite lives based on an assessment of their historical longevity and stable market positions. Indefinite-lived intangibles are tested for impairment at least annually...”
Disclosures

In principle

Generally, the disclosures required by US GAAP and IFRS are similar. Below is a description of some of the main disclosure requirements under IFRS, particularly where they differ from US GAAP.

Both US GAAP and IFRS require disclosure of the following for each impairment loss recognized:

- The amount
- The line in which such amount is presented in the statement of comprehensive income
- The reportable segment to which the loss relates (if the company discloses segment information)
- The events or circumstances that led to such recognition

However, under IFRS, management must also disclose the related cash-generating unit, which may differ from a reportable segment. Both IFRS and US GAAP require disclosure of any changes in the aggregation of assets within the cash-generating unit (reporting unit), and the reasons for changing the way that the cash-generating unit (reporting unit) is identified.
While US GAAP requires disclosure of the fair value, and the method of determining fair value, which is used to calculate the impairment loss under US GAAP, IFRS requires disclosure of the basis for determining recoverable amount (fair value less costs to sell or value in use) for that asset or CGU. When recoverable amount is determined based on fair value less costs to sell, the company must disclose the basis used (e.g., active market, discounted cash flow). When recoverable amount is determined based on value in use, the company must disclose key assumptions, such as the discount rate used and growth rates applied.

IFRS also requires that for each CGU that includes goodwill or intangible assets with indefinite lives within its carrying amount, a company must disclose items such as the key assumptions used to measure the recoverable amount of the CGU. Key assumptions are those to which the CGU’s recoverable amount is most sensitive. Management is also required to disclose its approach for determining the value assigned to each key assumption, whether those values reflect past experience, or, if appropriate, are consistent with external sources of information, and if not, how and why they differ from past experience or external sources of information.
Disclosures (continued)

In principle

If a reasonably possible change in a key assumption would cause the CGU’s carrying amount to exceed its recoverable amount, management is required to disclose all of the following:

- That excess amount
- The value assigned to the key assumption
- The amount by which the value assigned to the key assumption must change (including consequential affects) for the CGU’s recoverable amount to be equal to its carrying amount

Under IFRS, management is encouraged to disclose assumptions used to determine recoverable amount of the cash-generating unit (or asset) even when it does not contain goodwill or an intangible asset with an indefinite life.

If an impairment loss is reversed (which is not permitted at all under US GAAP or for goodwill under IFRS), a company is required to disclose (among other things):

- The amount
- The line in which such amount is presented in the statement of comprehensive income
- The reportable segment to which the reversal relates (if the company discloses segment information)
- The events or circumstances that led to such reversal
IFRS and US GAAP require disclosure if any goodwill has not yet been allocated to a cash-generating unit or reporting unit, respectively. However, the cutoff under IFRS is as of the end of the reporting period, whereas the cutoff under US GAAP is as of the date the financial statements are issued. In both cases, the reasons why that amount remains unallocated must be disclosed.

Both US GAAP and IFRS require a reconciliation of changes in the carrying amount of goodwill during the period, in addition to requiring disclosure of the balances at the beginning and end of each reporting period. While US GAAP requires the reconciliation to be provided by reportable segment (if the company provides segment information), and in total, in contrast, IFRS requires that a company disclose the total addition of assets to non-current assets (which would include additions to goodwill and intangible assets) by reportable segment (if the company provides segment information).

The following EY publications are available to assist when preparing disclosures under IFRS:

- Good Group (International) Limited illustrative financial statements
- International GAAP® Disclosure Checklist
Disclosures (continued)

**In practice**

The US Securities and Exchange Commission (SEC) and other regulators continue to ask companies (both those reporting under US GAAP and under IFRS) to expand their disclosures on the impairment of assets (such as equipment, investments, film and television costs), particularly when a company uses “boilerplate” language.

Recent comment letters issued by the SEC to companies reporting under IFRS have focused on the adequacy of disclosures regarding:

- The company’s specific policy for assessing impairment
- How the recoverable amount was determined for specific assets
- How management determined the company’s cash-generating units
- The factors that led to specific impairments
- Key assumptions used in valuation models
- The percentage by which recoverable amount exceeded the carrying amount for any cash-generating unit for which recoverable amount is not substantially in excess of the carrying amount

Other stakeholders also emphasize the importance of improving the transparency of the assumptions that management used, and the sensitivity of those assumptions. Through disclosure of the sensitivity analysis, users can better understand the effects of future changes in the environment on the business — particularly when there is a high level of market uncertainty — and compare management’s assumptions with those of the company’s peers.
One M&E company discloses its key assumptions as follows:

“The value in use calculations and impairment reviews are sensitive to changes in key assumptions, particularly relating to discount rates and cash flow growth. A sensitivity analysis has been performed based on changes in key assumptions considered to be possible by management: an increase in the discount rate of 0.5%; a decrease in the compound annual growth rate (CAGR) for adjusted operating cash flow in the five-year forecast period of between 2.0% and 5.0% depending on the CGU; and a decrease in perpetuity growth rates of 0.5%. The sensitivity analysis shows that no impairments would result under each of the sensitivity scenarios other than in the case of a 5.0% decline in adjusted operating cash flow CAGR over the five-year forecast period which, if applied across all CGUs, would result in an impairment of £111m.”

In a survey of investors, analysts and lenders, a common theme was the need to disclose how the factors that contributed to the impairment will affect the future prospects of the business—and to place at least as much importance on that information as they do on the size, magnitude and reason for the impairment.6 Even though in many cases the importance of an impairment charge might be downplayed because it is a non-cash charge, management should consider how to best and consistently communicate the fact that the impairment charge (or lack thereof) reflects:

- Management’s view on the future of the business (e.g., growth rate)
- The company’s ability to generate future cash flows and continue as a going concern
- Key factors influencing the industry

In addition, since there is not currently one set of global valuation standards, it is important to disclose the approach taken and the technique applied, to enable effective comparisons by users of the financial statements. In particular, users commented on the need for greater disclosure of the assumptions used in projecting cash flows, and the discount rate applied. For example, where an income approach (e.g., discounted cash flows) is used to estimate fair value less costs to sell, management should disclose how the amounts used (or discount rate) reflect market participant assumptions, and how such amounts might differ from the cash flows and discount rate used to estimate value in use, which reflect company-specific assumptions.

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6 “Meeting today’s financial challenges – Impairment reporting: improving stakeholder confidence” Ernst & Young survey in September and October 2009 of 170 users of financial statements, covering 32 countries.

7 The International Valuation Standards Council released its Exposure Draft Proposed New International Valuation Standards in June 2010. The proposed standards are not endorsed by the IASB and are not authoritative. However, they are being promoted as a source of authority and consistency in valuations. The final standard is expected to be published in April 2011.
First-time adopters of IFRS are required to test goodwill for impairment at the transition date when business combinations occurring prior to transition have not been retrospectively restated, regardless of whether there are indicators of impairment. For other long-lived assets, a first-time adopter only tests an asset for impairment at the date of transition to IFRS if there are indicators of impairment, as described above. Any impairment loss at the date of transition is recognized as an adjustment to retained earnings.

The underlying estimates (e.g., cash flow assumptions) used to determine whether a first-time adopter recognizes an impairment loss as of the transition date must be consistent with any impairment estimates made under US GAAP as of the transition date, unless there is objective evidence that those estimates were in error. If the first-time adopter needs to make estimates as of the transition date that were not necessary under US GAAP, such estimates and assumptions must reflect conditions that were present as of the date of transition to IFRS and may not reflect conditions that arose thereafter.
When considering what amount to test for impairment under IFRS upon transition, management should be aware that generally, IFRS requires full retrospective application of standards that are effective at the end of a first-time adopter’s first IFRS reporting period. Therefore, a first-time adopter must account for an intangible asset as if the first-time adopter had always accounted for that intangible asset under IFRS. However, there are several possible exemptions from this requirement for intangible assets (such as when the intangible asset was acquired in a business combination), that management should consider when determining the carrying amount on which to test for impairment.

The Ernst & Young publication International Financial Reporting Developments: IFRS 1—First-time Adoption of International Financial Reporting Standards provides additional information to assist management in converting to IFRS.
First-time adopters (continued)

In practice

The conversion to IFRS brings many changes in how to test for impairment of assets. Additional expertise may be required to assist with the valuations, particularly by those individuals who are knowledgeable about how to estimate VIU, since this concept does not exist under US GAAP.

The use of hindsight can be tricky when considering impairment in the context of a first-time adopter. Therefore, we recommend that when preparing for the adoption of IFRS, a first-time adopter that is required to evaluate its long-lived assets for impairment under US GAAP should evaluate such assets under IFRS, also to avoid the unnecessary burden of re-performing impairment analyses under IAS 36 several years later at the date of adoption of IFRS, as shown in Example 10.

Example 10: Preparing for first-time adoption

A US media company plans to adopt IFRS on December 31, 2016. It will be required to present full financial statements for the years ending December 31, 2014, 2015 and 2016. Therefore, beginning January 1, 2014, during the three-year period leading up to the adoption of IFRS, management evaluates its long-lived assets for impairment under both US GAAP and IFRS, thereby ensuring that estimates are made contemporaneously within the period.

Given the significance of intangible assets for first-time adopters in the media and entertainment industry, restatement of the carrying amount of an intangible asset as if the company had always accounted for that intangible asset under IFRS might involve significant cost and effort.

Table 3 includes suggested actions to consider when planning for the adoption of IFRS:
Table 3: Planning for impairment tests under IFRS

<table>
<thead>
<tr>
<th>Key Actions</th>
<th>First-time adopter</th>
<th>Annually thereafter</th>
</tr>
</thead>
<tbody>
<tr>
<td>Determine the carrying amount of intangible assets and goodwill on which the impairment test is performed</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Consider whether an indicator of impairment exists for each asset, and if so, determine the recoverable amount of that asset</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Identify which assets have specifically identifiable cash flows and which are part of a CGU</td>
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<td></td>
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<tr>
<td>Allocate goodwill to a CGU or group of CGUs and test for impairment</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Identify which, and to what extent, corporate assets are allocated to a CGU</td>
<td></td>
<td>X</td>
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<tr>
<td>Determine optimal time for impairment assessment for goodwill and indefinite-lived intangibles</td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Assess recoverable amount at transition date for goodwill and indefinite-lived intangibles</td>
<td></td>
<td></td>
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<tr>
<td>As part of determining VIU:</td>
<td></td>
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<tr>
<td>▶ If impairment tests have previously been required, compare previous estimates of cash flows to historical results to access the reasonableness of current period assumptions</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>▶ Review forecasts for inclusion of the most recent information and for exclusion of cash inflows or outflows from future performance enhancements or restructurings</td>
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<td>X</td>
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<tr>
<td>▶ Assess assumptions regarding growth rates and discount rates</td>
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<td>X</td>
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<tr>
<td>▶ Review valuation model and ensure it includes all of the factors identified by IAS 36</td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Consider whether there is any indication that an impairment loss recognized in prior periods (for assets other than goodwill) no longer exists or decreased</td>
<td>X</td>
<td>X</td>
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<tr>
<td>Consider whether changes to internal financial reporting systems are required to meet disclosure requirements</td>
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<td>X</td>
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<tr>
<td>Build time for annual impairment testing for goodwill and indefinite-lived intangibles into reporting timetable</td>
<td>X</td>
<td>X</td>
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<tr>
<td>Organize appropriate valuations experts as necessary</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Consider the accounting implications of pending acquisitions on future results – amortization and impairment charges impact results</td>
<td>X</td>
<td>X</td>
</tr>
</tbody>
</table>
Conclusion

Many judgments and estimates are involved in assessing whether there are indicators of impairment, identifying CGUs and determining the recoverable amount of assets, CGUs and groups of CGUs. Management should assess where there might be differences between IFRS and US GAAP, and plan carefully to ensure that systems, processes and the necessary valuation expertise are developed or obtained to meet the requirements of IAS 36. In addition, management should consider how it currently monitors goodwill (if at all) and whether any changes are needed upon conversion to IFRS.
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<th>Telephone</th>
<th>Email</th>
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