Group reorganization part II
Recognition of impairment losses and reversals
(Relevant to Paper I: PBE Financial Accounting)

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In order to assist the readers to update the changes of accounting standard, this article is divided into three parts to make your reading easier.

You can refer to Group reorganization Part I published in T/Dialogue October 2010 or find this on the "Learning Centre" in the HKIAAT website. The first part covers the reasons for disposal of assets, classification of "held for sale" and measurement of non-current assets (or disposal groups) classified as held for sale. In this part, we look at the recognition of impairment losses and reversals**,** changes to a plan of sale, presentation and disclosure. In the coming October 2011 issue, Part III will give more numerical examples to explain the theory clearly.

Recognizing impairment losses

1. An entity shall recognize an impairment loss for any initial or subsequent write-down of the asset (or disposal group) to fair value less costs to sell, to the extent that it has not been recognized in accordance with relevant HKFRS.

2. The following extracted from the Golden Harvest Entertainment (Holdings) Limited 2008 annual report can give you a clearer idea of the application of the above requirement:

    "A non-current asset (or disposal group) is classified as held for sale if it is highly probable that its carrying amount will be recovered through a sale transaction rather than through continuing use and the asset (or disposal group) is available for sale in its present condition. A disposal group is a group of assets to be disposed of together as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction.

    Immediately before classification as held for sale, the measurement of the non-current assets (and all individual assets and liabilities in a disposal group) *is brought up-to-date in accordance with the accounting policies before the classification. Then*, on initial classification as held for sale and until disposal, the non-current assets (except for certain assets as explained below), or disposal groups, are recognized at the lower of their carrying amount and fair value less costs to sell. The principal exceptions to this measurement policy so far as the financial statements of the Group and the Company are concerned are deferred tax assets, assets arising from employee benefits, financial assets (other than investments in subsidiaries, associates and joint ventures). These assets, even if held for sale, would continue to be measured in accordance with the policies set out elsewhere in notes to the financial statements.

    Impairment losses on initial classification as held for sale, and on subsequent remeasurement while held for sale, are recognised in the income statement. As long as a non-current asset is classified as held for sale, or is included in a disposal group that is classified as held for sale, the non-current asset is not depreciated or amortised." *[Italics are added by the author]*

3. An entity **shall recognize a gain for any subsequent increase in fair value** less costs to sell of an asset/disposal group, **but not in excess of the cumulative impairment loss** that has been recognized either in accordance with HKFRS5 or previously in accordance with HKAS 36 "Impairment of Assets".

4. An entity shall not depreciate (or amortize) a non-current asset while it is classified as held for sale or while it is part of a disposal group classified as held for sale. Interest and other expenses attributable to the liabilities of a disposal group classified as held for sale shall continue to be recognized.

Changes to a plan of sale

5. If an entity has classified an asset (or disposal group) as held for sale, but the criteria in Part I paragraphs 2 to 4 are no longer met, the entity shall cease to classify the asset (or disposal group) as held for sale.

6. The entity shall measure a non-current asset that ceases to be classified as held for sale (or ceases to be included in a disposal group classified as held for sale) at the lower of:

(a) its carrying amount before the asset (or disposal group) was classified as held for sale, adjusted for any depreciation, amortization or revaluations that would have been recognized had the asset (or disposal group) not been classified as held for sale, and

(b) its **recoverable amount** at the date of the subsequent decision not to sell.

7. It is not easy to find an example for the decision not to sell the asset/disposal group held for sale. An example using US GAAP appeared in the 2009 annual report of Focus Media Holdings Limited may give us an understanding on application of Part I paragraph 17.

   "On December 22, 2008, the Company announced that it entered into a definitive agreement with SINA Corporation ("SINA") to sell substantially all of the assets of Focus Media's LCD display network, poster frame network and certain in–store network (the "disposal group"). The disposal group was recorded as an asset group held–for–sale for the year ended December 31, 2008, and were not depreciated or amortized nor were they subject to the same impairment analysis as assets held and used in continuing operations. On September 28, 2009, the Company and SINA jointly reached a decision not to extend the deadline of the agreement announced on December 22, 2008. As such, the disposal group was reclassified as assets to be held and used thereafter. The results of the disposal group have been classified as continuing operations for the periods presented."

8. As the situation presented above is quite complicated, it is out of scope in this article to discuss the application of the above concepts other than the conceptual framework.

Presentation and disclosure

9. An entity shall present and disclose information that **enables users** of the financial statements **to evaluate the financial effects of discontinued operations and disposals** of non-current assets (or disposal groups).

Presenting discontinued operations

10. A **component of an entity** comprises operations and cash flows that can be clearly **distinguished, operationally and for financial reporting purposes**, from the rest of the entity. In other words, a component of an entity will have been **a cash-generating unit or a group of cash-generating units while being held for use.**

11. A discontinued operation is a component of an entity that either has been disposed of, or is classified as held for sale, and
    (a) represents a **separate major line of business or geographical area of operations**,
    (b) is **part of a single co-ordinated plan** to dispose of a separate major line of business or geographical area of operations, or
    (c) is a **subsidiary acquired exclusively with a view to resale**.

12. An entity shall disclose:
    (a) A single amount in the statement of comprehensive income comprising the total of:
        (i) the post-tax profit or loss of discontinued operations and
        (ii) the post-tax gain or loss recognized on the measurement to fair value less costs to sell or on the disposal of the assets or disposal group(s) constituting the discontinued operation.
    (b) An analysis of the single amount in (a) into:
        (i) the revenue, expenses and pre-tax profit or loss of discontinued operations;
        (ii) the related income tax expense as required by paragraph 81(h) of HKAS 12;
        (iii) the gain or loss recognized on the measurement to fair value less costs to sell or on the disposal of the assets or disposal group(s) constituting the discontinued operation; and
        (iv) the related income tax expense as required by paragraph 81(h) of HKAS 12.

        The analysis may be presented in the notes or in the statement of comprehensive income. If it is presented in the statement of comprehensive income it shall be presented in a section identified as relating to discontinued operations, i.e. separately from continuing operations. The analysis is not required for disposal groups that are newly acquired subsidiaries that meet the criteria to be classified as held for sale on acquisition.
    (c) The net cash flows attributable to the operating, investing and financing activities of discontinued operations. These disclosures may be presented either in the notes or in the financial statements. These disclosures are not required for disposal groups that are newly acquired subsidiaries that meet the criteria to be classified as held for sale on acquisition.

13. An entity shall re-present the above disclosures (paragraph 12) for prior periods presented in the financial statements so that the disclosures relate to all operations that have been discontinued by end of the reporting period for the latest period presented.

14. Adjustments in the current period to amounts previously presented in discontinued operations that are directly related to the disposal of a discontinued operation in a prior period shall be classified separately in discontinued operations. The nature and amount of such adjustments shall be disclosed. Examples of circumstances in which these adjustments may arise include the following:

(a) The resolution of uncertainties that arise from the terms of the disposal transaction, such as the resolution of purchase price adjustments and indemnification issues with the purchaser.

(b) The resolution of uncertainties that arise from and are directly related to the operations of the component before its disposal, such as environmental and product warranty obligations retained by the seller.

(c) The settlement of employee benefit plan obligations, provided that the settlement is directly related to the disposal transaction.

15. If an entity **ceases to classify a component of an entity as held for sale**, the results of operations of the component previously presented in discontinued operations in accordance with paragraphs 12 to 14 **shall be reclassified and included in income from continuing operations for all periods presented**. The amounts for prior periods shall be described as having been re-presented.

Gains or losses relating to continuing operations

16. Any **gain or loss** on the remeasurement of a **non-current asset (or disposal group)** classified as held for sale that does **not meet the definition of a discontinued operation** shall be included in profit or loss from **continuing operations**.

Presentation of a non-current asset or disposal group classified as held for sale

17. An entity shall present a non-current asset classified as held for sale and the assets of a disposal group classified as held for sale separately from other assets in the statement of financial position. The liabilities of a disposal group classified as held for sale shall be presented separately from other liabilities in the statement of financial position. Those assets and liabilities shall not be offset and presented as a single amount. The major classes of assets and liabilities classified as held for sale shall be separately disclosed either in the statement of financial position or in the notes, except as permitted by paragraph 18. An entity shall present separately any cumulative

income or expense recognized in other comprehensive income relating to a non-current asset (or disposal group) classified as held for sale.

18. If the disposal group is a newly acquired subsidiary that meets the criteria to be classified as held for sale on acquisition, disclosure of the major classes of assets and liabilities is not required.

19. An entity shall **not reclassify or re-present** amounts presented for non-current assets or for the assets and liabilities of disposal groups classified as held for sale in the statement of financial position for **prior periods** to reflect the classification in the statement of financial position for the latest period presented.

Additional disclosures

20. An entity shall disclose the following information in the notes in the period in which a non-current asset (or disposal group) has been either classified as held for sale or sold:
(a) a description of the non-current asset (or disposal group);
(b) a description of the facts and circumstances of the sale, or leading to the expected disposal, and the expected manner and timing of that disposal;
(c) the gain or loss recognized in accordance with Part I paragraphs 12 and 14 and, if not separately presented in the statement of comprehensive income, the caption in the statement of comprehensive income that includes that gain or loss;
(d) if applicable, the reportable segment in which the non-current asset (or disposal group) is presented in accordance with HKFRS 8 “Operating Segments”.

That's the end of Part II. The discussion of group reorganizations will continue in the October 2011 issue of T/Dialogue.

For more practical examples relating to HKFRS5, you may refer to the following annual reports.

http://www.hhop.com.hk/Reports/2010/20100729/e0450_100714_ar.pdf

http://www.chinaunicom.com.hk/files/doc/report/a2008/a2008en.pdf

http://www.irasia.com/listco/hk/goldenharvest/annual/ar33708-e01132.pdf