AMENDMENTS TO THE STANDARDS OF GRAP

ON

IMPAIRMENT OF NON-CASH-GENERATING ASSETS

(GRAP 21)

AND

IMPAIRMENT OF CASH-GENERATING ASSETS (GRAP 26)

Issued by the
Accounting Standards Board
Month 2015

Introduction

Standards of Generally Recognised Accounting Practice

The Accounting Standards Board (the Board) is required in terms of the Public Finance Management Act, Act No. 1 of 1999, as amended (PFMA), to determine generally recognised accounting practice referred to as Standards of Generally Recognised Accounting Practice (GRAP).

The Board must determine GRAP for:

(a) departments (including national and provincial and government components);

(b) public entities;

(c) trading entities (as defined in the PFMA);

(d) constitutional institutions;

(e) municipalities and boards, commissions, companies, corporations, funds or other entities under the ownership control of a municipality; and

(f) Parliament and the provincial legislatures.

The above are collectively referred to as "entities".

The Board has approved the application of Statements of Generally Accepted Accounting Practice (GAAP), as codified by the Accounting Practices Board and issued by the South African Institute of Chartered Accountants as at 1 April 2012, to be GRAP for:

(a) government business enterprises (as defined in the PFMA);

(b) any other entity, other than a municipality, whose ordinary shares, potential ordinary shares or debt are publicly tradable on the capital markets; and

(c) entities under the ownership control of any of these entities.

The Board has approved the application of International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board to be GRAP for these entities where they are applying IFRSs.

Financial statements should be described as complying with Standards of GRAP only if they comply with all the requirements of each applicable Standard of GRAP and any related Interpretations of the Standards of GRAP.

Any limitation of the applicability of specific Standards or Interpretations is made clear in those Standards or Interpretations of the Standards of GRAP.

All paragraphs in this Standard of GRAP have equal authority. The status and authority of appendices are dealt with in the preamble to each appendix. This Standard should be read in the context of its objective, its basis for conclusions if applicable, the *Preface to Standards of GRAP,* the *Preface to the Interpretations of the Standards of GRAP* and the *Framework for the Preparation and Presentation of Financial Statements*.

Standards of GRAP and Interpretations of the Standards of GRAP should also be read in conjunction with any directives issued by the Board prescribing transitional provisions, as well as any regulations issued by the Minister of Finance regarding the effective dates of the Standards of GRAP, published in the Government Gazette.

Reference may be made here to a Standard of GRAP that has not been issued at the time of issue of this Standard. This is done to avoid having to change the Standards already issued when a later Standard is subsequently issued. Paragraph .11 of the Standard of GRAP on *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

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Amendments to the Standards of Generally Recognised Accounting Practice (GRAP)

PART 1: Amendments to the Standard of GRAP on *Impairment of Non-cash-generating Assets*

Amended text is shown with new text underlined, deleted text struck through and text that has been relocated is indicated with a double underline. The following paragraphs in GRAP 21 have been amended:

…

Scope

…

.03 An entity shall first apply this Standard of GRAP to designate its assets as either non-cash-generating or cash-generating in accordance with paragraphs .13A to .16C of this Standard. Entities that designate their assets as ~~manage~~ non-cash-generating assets ~~as defined in paragraph .10~~ shall apply the requirements of this ~~the~~ Standard ~~of GRAP on Impairment of Cash-generating Assets to such assets~~. For assets that are designated as ~~non-~~cash-generating assets, e~~E~~ntities ~~that hold non-cash-generating assets~~ shall apply the requirements of ~~this~~ the Standard of GRAP on Impairment of Cash-generating Assets ~~to non-cash-generating assets.~~

…

Definitions

.10 The following terms are used in this Standard with the meanings specified:

Cash-generating assets are assets used ~~managed~~ with the objective of generating a commercial return. Commercial return means that positive cash flows are expected to be significantly higher than the cost of the asset.

Costs of disposal are incremental costs directly attributable to the disposal of an asset, excluding finance costs and income tax expense.

Fair value less costs to sell is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.

An impairment is a loss in the future economic benefits or service potential of an asset, over and above the systematic recognition of the loss of the asset's future economic benefits or service potential through depreciation.

An impairment loss of a non-cash-generating asset is the amount by which the carrying amount of an asset exceeds its recoverable service amount.

Non-cash-generating assets are assets other than cash-generating assets.

Recoverable service amount is the higher of a non-cash-generating asset's fair value less costs to sell and its value in use.

<u>Value in use of a non-cash-generating asset</u> is the present value of the asset's remaining service potential.

Terms defined in other Standards of GRAP are used in this Standard with the same meaning as in those other Standards.

~~Cash-generating assets and non-cash-generating assets~~

~~.11 Even though most entities normally have service delivery as their objective, management can exercise discretion to acquire and manage assets to generate a commercial return. Some assets may be managed solely as non-cash-generating assets, while others may be managed as cash-generating assets that generate a commercial return.~~

~~.12 Cash-generating assets are assets managed with the objective of generating a commercial return. An asset generates a commercial return when it is deployed in a manner consistent with that adopted by a profit-oriented entity. Managing an asset to generate a "commercial return" indicates that an entity intends to generate positive cash inflows from the asset (or from the cash-generating unit of which the asset is a part) and earn a commercial return that reflects the risk involved in managing the asset. An asset may be managed with the objective of generating a commercial return even though it does not meet that objective during a particular reporting period. Conversely, an asset may be a non-cash-generating asset even though it may be breaking even or generating a commercial return during a particular reporting period. Unless stated otherwise, references to "an asset" or "assets" in the following paragraphs of this Standard are references to "non-cash-generating asset(s)".~~

~~.13 There are a number of circumstances in which entities may manage some assets with the objective of generating a commercial return, although the majority of assets are not managed for that purpose. For example, a hospital may deploy a building for fee-paying patients. Cash-generating assets of an entity may operate independently of the non-cash-generating assets of the entity.~~

~~.14 In certain instances, an asset may generate cash flows although it is managed for service delivery purposes. For example, a waste disposal plant is operated to ensure the safe disposal of medical waste generated by state controlled hospitals, but the plant also treats a small amount of medical waste generated by other private hospitals on a commercial basis. The treatment of medical waste from the private hospitals is incidental to the activities of the plant, and the assets that generate cash flows cannot be distinguished from the non-cash-generating assets.~~

~~.15 In other instances, an asset may generate cash flows and also be managed for non-cash-generating purposes. For example, a public hospital has ten wards, nine of which are managed for fee paying patients on a commercial basis, and the other is managed for non-fee paying patients. Patients from both wards jointly use other hospital facilities (for example, operating facilities). The extent to which the asset is managed with the objective of providing a commercial return needs to be considered to determine whether the entity should apply the provisions of this Standard or the Standard of GRAP on *Impairment of Cash-generating Assets*. If, as in this example, the non-cash-generating component is an~~

~~insignificant component of the arrangement as a whole, the entity applies the Standard of GRAP *on Impairment of Cash-generating Assets* rather than this Standard.~~

~~.16 In some cases, it may not be clear whether the objective of managing an asset is to generate a commercial return. In such cases, it is necessary to evaluate the significance of the cash flows. It may be difficult to determine whether the extent to which the asset generates cash inflows is so significant that this Standard is applicable rather than the Standard of GRAP on *Impairment of Cash-generating Assets*. Judgement is needed to determine which Standard to apply. An entity develops criteria so that it can exercise that judgement consistently in accordance with the definition of cash-generating assets and non-cash-generating assets and with the related guidance in paragraphs .11 to .15. Paragraph .74 requires an entity to disclose the criteria used in making this judgement. However, given the overall objectives of most entities, the presumption is that assets are non-cash-generating and, therefore, this Standard will apply.~~

…

Designation of an asset as cash-generating or non-cash-generating

.13A At initial recognition, an entity shall designate:

(a) an asset as non-cash-generating; or

(b) an asset or cash-generating unit as cash-generating.

The designation is made on the basis of an entity's objective of using the asset.

.13B Assets are designated as cash-generating or non-cash-generating based on the entity's objective of using the assets. Assets can either be used with the objective of generating a commercial return or delivering services. In some cases, an entity may use its assets to fulfil both objectives.

.13C Cash generating assets are assets used with the objective of generating a commercial return. For the purposes of this Standard, assets that generate a commercial return are those that generate positive cash flows which are expected to be significantly higher than the cost of the assets.

.13D Non-cash-generating assets are assets that are not used with the objective to generate a commercial return. Instead they are used to deliver services.

.13E The assessment of an entity's objective of using the asset is performed at initial recognition, based on management's expected use of the asset over its useful life. Subsequent to initial recognition and designation, an entity ~~should~~shall redesignate an asset in accordance with paragraphs .72 and .73 of this Standard or paragraphs .114 and .115 of the Standard of GRAP on *Impairment of Cash-generating Assets*~~,~~ if there has been a change in an entity's expected use of the asset that is expected to result~~s~~ in positive cash flows that are significantly higher than the cost of the asset.

.13F An entity ~~should~~shall assess the objective of using an asset or cash-generating unit instead of assessing the entity's overall objective. In the case of infrastructure assets, as described in the Standard of GRAP on *Property, Plant and Equipment,* an asset can be a group of assets that are part of a system or network. As the designation of assets is undertaken for assets or cash-generating units, it is possible for different assets of an entity to be classified as cash-generating assets or non-cash-generating assets.

.13G Since the initial designation of an asset as cash-generating or non-cash-generating is based on the initial expected use of the asset, this Standard does not require an entity to demonstrate on an annual basis whether it has achieved that initial expectation. Therefore, an asset may be used with the objective of generating a commercial return even though it does not meet that objective during a particular reporting period. Conversely, an asset may be a non-cash-generating asset even though it may be generating a commercial return during a particular reporting period. The designation of an asset will not change between reporting periods unless there has been a change in the entity's objective of using the asset that is expected to result~~s~~ in positive cash flows that are significantly higher than the cost of the asset.

Cash-generating assets

.14A An entity shall designate an asset or a cash-generating unit as cash-generating when:

(a) its objective is to use the asset or cash-generating unit in a manner that generates a commercial return; such that

(b) the asset or cash-generating unit will generate positive cash flows, from continuing use and its ultimate disposal, that are expected to be significantly higher than the cost of the asset.

Entities that designate their assets or cash-generating units as cash-generating shall apply the Standard of GRAP on Impairment of Cash-generating Assets to such assets rather than this Standard.

.14B An entity's objective is to use the assets to generate a commercial return when those assets are deployed in a manner consistent with that adopted by a profit-oriented entity. In such cases, management's plans and decisions will indicate that the entity intends to generate positive cash flows that are expected to be significantly higher than the cost of the assets at acquisition. These positive cash flows must be significantly higher than the cost of the asset and not result in a break even position or be marginally higher than the cost of the asset. Where the positive cash flows are marginally higher than the cost of the asset, an entity applies judgement to assess their significance.

.14C An assessment of management's plans and decisions at initial recognition will indicate the extent to which the asset will be used with the objective of generating a commercial return. Evidence will be available from external and internal reporting which supports the entity's objective. For example, a review of strategy plans, budgets, submissions to external bodies (such as regulators), asset acquisition proposals, and cost and revenue reports will indicate that the asset will be used, or is expected to be used, to generate a commercial return.

.14D For assets acquired through a non-exchange transaction, the cost of the asset is its fair value as at the date of acquisition.

Non-cash-generating assets

.15A ***An entity shall designate an asset as non-cash-generating when its objective is not to use the asset to generate a commercial return but to deliver services. An entity shall apply this Standard rather than the Standard of GRAP on Impairment of Cash-generating Assets for assets that are designated as non-cash-generating assets.***

.15B Assets held in the public sector are generally not used with the objective of generating a commercial return but are used for delivering services. When an entity does not use its assets with the objective of generating a commercial return, it may deliver those services at no charge or by generating positive cash flows that are sufficient to break even or generating a marginal return. As the entity's objective is not to generate a commercial return, the assets are designated as non-cash-generating assets.

.15C When an entity does not use its assets with the objective of generating a commercial return, management's decisions and plans to continue deploying assets in that manner will not be influenced by the assets' ability to generate a commercial return. Since the entity's objective is not to generate a commercial return, the entity is not required to assess the significance of any cash flows generated in relation to the cost, at initial recognition.

Dual-purpose assets

.16A ***An asset used with the objective of generating a commercial return and service delivery shall be designated either as a cash-generating asset or non-cash-generating asset based on whether an entity expects to use that asset to generate a commercial return. When it is not clear whether the objective is to use the asset to generate a commercial return, an entity designates the asset as a non-cash-generating asset and applies the provisions of this Standard rather than the Standard of GRAP on Impairment of Cash-generating Assets.***

.16B Some assets may be used to fulfil both objectives of generating a commercial return and service delivery. An entity ~~should~~shall firstly assess whether it expects to use the assets to generate a commercial return to determine whether the assets should be designated as cash-generating asset or non-cash-generating assets. In cases when it is not clear what the overall objective of using the assets is, the presumption is that assets are used with the objective to deliver services. As a result, an entity applies the provisions of this Standard rather than the Standard of GRAP on *Impairment of Cash-generating Assets.* For example, a municipality may use its infrastructure assets to provide free basic services to indigent households and also charge a fee based on cost plus a specific return to non-indigent households. If the entity's objective of using the asset is to generate a commercial return, an entity applies the Standard of GRAP on *Impairment of Cash-generating Assets* rather than this Standard. When it is not clear what the overall objective of using the assets is, the presumption is that the assets are used with the objective of delivering services.

.16C In some cases, an entity may use an asset with the objective of generating a commercial return and use the return generated by that asset to cross-subsidise other assets that are used for service delivery purposes. In such cases, an entity applies the Standard GRAP on *Impairment of Cash-generating Assets* rather than this Standard because its objective of using the asset is to generate a commercial return. An entity cannot conclude that the asset is not a cash-generating asset on the basis that it uses the positive cash flows derived by that asset for service delivery.

.17 Unless stated otherwise, references to “an asset” or “assets” in the following paragraphs of this Standard are references to “non-cash-generating asset(s)”.

Identifying an asset that may be impaired

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.26A Physical damage would trigger an impairment test when it results in a permanent or significant decline in the service potential of the asset. Judgement is needed to determine whether the decline is permanent or significant. Such judgements may be based on the relative costs of providing the service before and after the decline, the percentage decline in service potential or other considerations. The decline in service potential is expected to be permanent when management has no reasonable expectation that the lost service potential will be replaced or restored. In certain circumstances evidence may be available to demonstrate that the impairment will be temporary. In such circumstances, management considers whether the decline in service potential will be significant.

…

Measuring recoverable service amount

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Depreciated replacement cost approach

.43 Under this approach, the present value of the remaining service potential of an asset is determined as the depreciated replacement cost of the asset. The replacement cost of an asset is the cost to replace the asset’s gross service potential. This cost is depreciated to reflect the asset in its used condition. An asset may be replaced either through reproduction (replication) of the existing asset or through replacement of its gross service potential. The depreciated replacement cost is measured as the current reproduction or replacement cost of the asset, whichever is lower, less accumulated depreciation calculated on the basis of such cost, to reflect the already consumed or expired service potential of the asset.

…

Reversing an impairment loss

.57 Paragraphs .58 to .71 set out the requirements for reversing an impairment loss recognised for an asset in prior periods.

.58 An entity shall assess at each reporting date whether there is any indication that an impairment loss recognised in prior periods for an asset may no longer exist or may have decreased. If any such indication exists, the entity shall estimate the recoverable service amount of that asset.

.59 In assessing whether there is any indication that an impairment loss recognised in prior periods for an asset may no longer exist or may have decreased, an entity shall consider, as a minimum, the following indications:

External sources of information

(a) Resurgence of the demand or need for services provided by the asset.

(b) Significant long-term changes with a favourable effect on the entity have taken place during the period, or will take place in the near future, in the technological, legal or government policy environment in which the entity operates.

Internal sources of information

(bA) Evidence is available that indicates that the service potential of the asset has been restored following physical damage to the asset.

(c) Significant long-term changes with a favourable effect on the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, the asset is used or is expected to be used. These changes include costs incurred during the period to improve or enhance an asset's performance, restructure the operation to which the asset belongs or a decision to use rather than dispose of an asset.

(d) A decision to resume construction of the asset that was previously halted before it was completed or in a usable condition.

(e) Evidence is available from internal reporting that indicates that the service performance of the asset is, or will be, significantly better than expected.

…

Redesignation of assets

.72 The redesignation of assets from a cash-generating asset to a non-cash-generating asset or from a non-cash-generating asset to a cash-generating asset shall only occur when there is clear evidence that such a redesignation is appropriate. A redesignation, by itself, does not necessarily trigger an impairment test or a reversal of an impairment loss. Instead, the indication for an impairment test or a reversal of an impairment loss arises from, as a minimum, the listed indications in paragraph .23.

.73 When there has been a change in the manner in which an entity uses an asset that is expected to result~~s~~ in positive cash flows that are significantly higher than the cost of the asset, an entity~~There are circumstances in which entities may~~ shall ~~decide that it is appropriate to~~ redesignate a non-cash-generating asset as a cash-generating asset. ~~For example, an effluent treatment plant was constructed primarily to treat industrial effluent from a social housing unit, for which no charge is made. The social housing unit has been demolished and the site will be redeveloped for industrial and retail purposes. It is intended that, in future, the plant will be used to treat industrial effluent at commercial rates. In light of this decision, the entity decides to redesignate the effluent treatment plant as a cash-generating asset.~~ For example, an entity that previously used an asset with the objective of delivering services makes a policy decision to use that asset and charge a fee, based on cost plus a specific return such that it generates a commercial return. This change in objective results in the entity using the asset in a way that generates a commercial return. The entity will redesignate that asset from non-cash-generating to a cash-generating.

Disclosure

.74 ***An entity shall disclose in the summary of accounting policies, the judgements management has made in applying the criteria ~~developed by the entity to distinguish~~ to designate assets as non-cash-generating assets or ~~from~~ cash-generating assets.***

…

Transitional provisions

Initial adoption of the Standards of GRAP

.82 ***The transitional provisions to be applied by entities on the initial adoption of this Standard are prescribed in a directive(s). The provisions of this Standard should be read in conjunction with each applicable directive.***

Amendments to Standards of GRAP

.83 ***Paragraphs .03, .10, .12, .13, .14, .15, .16, .19, .23, .24, .26, .34, .78 and .79 were amended and paragraph .11 was added by the Improvements to the Standards of GRAP issued on 1 April 2014. An entity shall apply these amendments prospectively for annual financial periods beginning on or after 1 April 2015. If an entity elects to apply these amendments earlier, it shall disclose this fact.***

.83A ***Paragraphs .03, .10, .43 .59 .73 and .74 were amended, paragraphs .11, to .16 were deleted and paragraphs .13A to .13G, .14A to .14D, .15A to .15C, .16A to .16C, .17 and .26A were added by the Amendments to the Standards of GRAP issued on [Day Month Year]. An entity shall apply these amendments prospectively for annual financial periods beginning on or after [Day Month Year]. If an entity elects to apply these amendments earlier, it shall disclose this fact.***

.83B ***Where the application of the amendments in paragraph .83A result in the redesignation of existing assets from cash-generating asset to non-cash-generating asset or from non-cash-generating asset to a cash-generating***

asset, an entity shall assess whether that redesignation triggers an impairment test or a reversal of an impairment loss.

Effective date

Initial adoption of the Standards of GRAP

.84 An entity shall apply this Standard of GRAP for annual financial statements covering periods beginning on or after a date to be determined by the Minister of Finance in a regulation to be published in accordance with section 91(1)(b) of the Public Finance Management Act, Act No. 1 of 1999, as amended.

Entities already applying Standards of GRAP

.85 An entity shall apply amendments to this Standard of GRAP for annual financial statements covering periods beginning on or after [Day Month Year]~~1 April 2015~~. Earlier application is encouraged. If an entity applies these amendments for a period beginning before [Day Month Year] ~~1 April 2015~~, it shall disclose that fact.

Basis for conclusions

This basis for conclusions gives the Accounting Standards Board's (the Board's) reasons for accepting or rejecting certain solutions related to the accounting for impairment of non-cash-generating assets. This basis for conclusions accompanies, but is not part of, the Standard of GRAP on Impairment of Non-cash-generating Assets (GRAP 21).

Introduction

BC1. This Standard of GRAP prescribes the procedures that an entity applies to determine whether a non-cash-generating asset is impaired and establishes how the impairment is recognised and measured. This Standard is primarily drawn from the International Public Sector Accounting Standard on *Impairment of Non-cash-generating Assets* (IPSAS 21). In developing this Standard, the Board also considered pronouncements issued by other standard setting bodies dealing with the accounting for impairment of assets.

BC2. This basis for conclusions summarises the significant departures that are made from IPSAS 21 and the reasons for such departures.

Scope

Inclusion of property, plant and equipment carried at revalued amounts

BC3. Property, plant and equipment carried at revalued amounts in accordance with the revaluation model are within the scope of the International Accounting Standard on *Impairment of Assets* (IAS 36).

BC4. The scope of IPSAS 21, however, excludes non-cash-generating property, plant and equipment carried at revalued amounts in accordance with the revaluation model in the International Public Sector Accounting Standard on *Property, Plant and Equipment* (IPSAS 17). The basis for conclusions in IPSAS 21 states that the IPSASB is of the view that assets carried at revalued amounts in accordance with the revaluation model in IPSAS 17 will be revalued with sufficient regularity to ensure that they are carried at an amount that is not materially different from their fair value at the reporting date. Impairment will therefore be taken into account in that valuation.

BC5. A similar scope exclusion for cash-generating property, plant and equipment carried at revalued amounts was included in the International Public Sector Accounting Standard on *Impairment of Cash-generating Assets* (IPSAS 26). The IPSASB concluded that it would be onerous to impose a requirement to test for impairment in addition to the existing requirement in IPSAS 17 that requires assets to be revalued with sufficient regularity to ensure that they are carried at an amount that is not materially different from their fair value at the reporting date. Therefore, on balance, the IPSASB concluded that IPSAS 26 should be consistent with the conclusion in IPSAS 21.

BC6. In its argument to exclude property, plant and equipment carried at revalued amounts from the scope of IPSAS 21 and IPSAS 26, the IPSASB noted that in IAS 36 the maximum amount of an impairment loss is the disposal costs. This is particularly relevant in cases where the fair value of an item of property, plant and equipment is its market value. The IPSASB is of the view that, in most cases, these will not be material and, from a practical point of view, it is not necessary to measure an asset's recoverable service amount and to recognise an impairment loss for the disposal costs of the asset.

BC7. The Board, however, agrees with the scope inclusion of property, plant and equipment carried at revalued amounts as in IAS 36. The Board is the view that it will not be too onerous to assess at each reporting date whether there is an indication that an asset may be impaired, or that an impairment loss recognised in prior periods for the asset may no longer exist.

BC8. The Board is also of the view that entities may not revalue their assets with "sufficient regularity", as the cost of revaluing certain public sector assets may initially be quite expensive. The disposal costs of certain specialised assets in the public sector therefore may well be significant. The scope exclusion for non-cash-generating property, plant and equipment carried at revalued amounts is therefore not included in this Standard.

Inclusion of intangible assets carried at revalued amounts

BC9. For similar reasons as those expressed for the scope exclusion of non-cash-generating property, plant and equipment carried at revalued amounts, the IPSASB also scoped out the impairment of cash-generating intangible assets carried at revalued amounts. IAS 36, however, includes the impairment of such intangible assets in the scope of the Standard.

BC10. The Board, for similar reasons as those expressed in the scope inclusion of non-cash-generating property, plant and equipment carried at revalued amounts, agrees with the scope inclusion of impairment of non-cash-generating intangible assets carried at revalued amounts as in IAS 36. The scope exclusion for the impairment of non-cash-generating intangible assets carried at revalued amounts is therefore not included in this Standard.

Designation of an asset as cash-generating or non-cash-generating

BC11. In responding to the concerns raised by many respondents to its Improvements Project for 2013, the Board considered how it can simplify and streamline the principles relating to the distinction between cash-generating and non-cash-generating assets.

BC12. The issues identified by respondents related to applying the concept of generating a commercial return in the public sector. There have been varying interpretations of what constitutes a commercial return and some hold the view that the primary objective of deploying most assets in the public sector cannot be to generate a commercial return as the primary objective is service delivery.

BC13. The Board noted that to adequately address the concerns raised, the classification of cash-generating and non-cash-generating should move away from an assessment of whether an asset is managed with the objective of generating a commercial return. The Board concluded that the classification should be based on an entity's objective for using the asset.

BC14. The Board observed that entities in the public sector usually use assets with the objective of delivering services and/or to generate positive cash flows. The Board agreed that the objective of using the assets should be applied as a basis to determine whether the assets are cash-generating or non-cash-generating. It noted that when an entity decides to construct or purchase an asset, it will usually have a predetermined objective for using an asset. The Board acknowledged that the principles it has set for the classification of assets may be difficult to apply in cases where an entity uses its assets with the objective of delivering services and also generating positive cash flows. The Board concluded that the principles in the Standards should also clarify how entities should determine the classification if the overall objectives of using the asset are unclear. The Board agreed that it is necessary to include what the presumption is in respect of assets used for dual-purposes.

BC15. As part of the simplification and streamlining the impairment requirements in the Standards, the Board considered the principles underpinning the value in use concept applicable to non-cash-generating assets in GRAP 21. In particular, the Board considered the deprival value model, which is applied mostly in Australia, United Kingdom and New Zealand to select a current measurement basis when preparing financial statements. The model is premised on the fact that if an entity has an asset, an entity should measure that asset at the value it would be deprived of if the entity lost that asset, which is its replacement cost. The model also notes that the value the entity is deprived of would be based on what the entity could replace the asset with, but also considers that an entity owns that asset and can therefore operate the asset in a certain manner. The Board adopted the thinking behind this model as a basis to support what it considers the best measurement basis for determining value in use in the public sector.

BC16. It is this thinking that supports the Board's observations that when an entity uses its assets with the objective of delivering services, the most relevant measurement basis to determine value in use is the depreciated replacement cost. This is because when an entity is deprived of an asset, the entity will incur a cost equivalent to the depreciated replacement cost to obtain the equivalent remaining service potential and economic benefits (including the net amount that would be received on disposal of the asset). As a result, the value of the asset to an entity cannot be higher than its depreciated replacement cost when it is used with the objective to deliver services. However, when the asset is used with the objective of generating cash flows that are expected to be significantly higher than the depreciated replacement cost, then the asset is a cash-generating asset and the most relevant measure of value in use is the discounted cash flows.

BC17. The Board believed that adopting this approach for classifying assets as either cash-generating or non-cash-generating would require less judgement and is suitable as entity-specific criteria can be subjective. Previously, the classification required management to apply judgement when assessing whether an entity is generating a commercial return and this proved to be problematic. In this approach the Board had substituted the idea of generating a commercial return with an entity's use of its assets with the objective of generating positive cash flows that are expected to be significantly higher than the cost of replacing the asset.

BC18. While respondents understood the Board's rationale for simplifying the requirements and moving away from the concept of generating a commercial return, they suggested that the Board consider not substituting the concept of generating a commercial return. They indicated that the previous guidance did not clearly explain this concept, which resulted in interpretation issues amongst preparers. These respondents observed that the introduction of the notion that a cash-generating asset is one that "generates positive cash flows that are expected to be significantly higher than the depreciated replacement cost" captures and explains clearly when an entity would be generating a commercial return. Consequently, the Board agreed not to move away from the concept of generating a commercial return.

BC19. Some respondents noted that while the Board's approach may achieve some simplification, they found the reference to the depreciated replacement cost when an entity is assessing the designation of its assets to be confusing. Some explained that the confusion stems from the following issues: (a) the idea that a depreciated replacement cost calculation is required to be performed and what other "evidence" would be necessary to support this assumption, and (b) issues have been raised about whether and how the assessment would need to be done to justify the designation on an ongoing basis.

BC20. Based on the feedback from respondents, the Board deliberated on the relevance of the proposed approach. The Board observed that many assets in the public sector are measured using a historical measurement basis. As a result, it concluded that the notion that positive cash flows from using the asset need to be higher than the cost of the asset at acquisition is appropriate, as the amounts charged for the services provided will include, or aim to recover, the depreciation based on the cost of the asset. The Board debated whether re-designations should be based on the cost of the asset or the depreciated replacement cost. It was agreed that the same measurement basis would be used for initial and subsequent designations as the historical cost measure is straightforward and the information readily available.

BC21. The Board concluded that, in applying the requirements of this Standard, it would not require entities to perform annual calculations to demonstrate what the entities' objectives of using the assets are. The Board's view is that an entity would have had a clear objective of how it would use its assets, and would have made certain calculations in setting its tariffs and understanding the basis of its cost structure, in order to reach the conclusion that its objective is to use its assets to generate a commercial return. The Board noted that it should clarify that the assessment is done initially, taking into account the overall long term objective of using the asset.

BC22. Part of the Board's considerations in the review project was assessing the feasibility of combining the two Standards into a single Standard. While there are similarities in the two Standards, and combining the Standards will result in the reduction of duplication of requirements, the Board considered those areas that are different and how it could respond to these dissimilarities. The Board concluded that it may be difficult to develop a single set of indicators suitable for both cash-generating and non-cash-generating assets, and that there is still merit in retaining two separate Standards. Respondents generally supported the Board's view.

BC23. After considering the amendments made to the designation of assets, the Board questioned the format of the two Standards. The Board believed that including the new section on the designation of assets in both Standards would create unnecessary duplication in the requirements. The Board agreed that the section on designations should only be included in GRAP 21, and a cross reference should be added to GRAP 26 that makes it clear that entities should first apply GRAP 21 to designate their assets, and thereafter apply the relevant Standard for the impairment of their assets.

Permanent or significant decline in service potential

BC24. One of the findings from the Board's post-implementation review project was that assets are being impaired for minor damage that could be rectified through repairs and maintenance. The Board concluded that it is necessary to clarify that the intention of the impairment Standards is to reflect those damages that have a permanent or significant impact on the value or service potential of an asset.

Comparison with the International Public Sector Accounting Standard on *Impairment of Non-Cash-Generating Assets* (February 2007)

The Standard of GRAP on *Impairment of Non-cash-generating Assets* is drawn primarily from the International Public Sector Accounting Standard on *Impairment of Non-Cash-Generating Assets* (IPSAS 21). The main differences between this Standard and IPSAS 21 are as follows:

- The definition of cash-generating assets in this Standard is different from IPSAS 21.
- This Standard uses different terminology, in certain instances, from IPSAS 21. The most significant example is the use of the term "net assets" in this Standard. The equivalent term in IPSAS 21 is "net assets/equity".
- The scope of the Standard of GRAP is different in that biological assets related to agricultural activities that are measured at fair value less costs to sell are excluded from the scope of this Standard. IPSAS 21 has no such scope exclusions.
- Non-cash generating property, plant and equipment that is measured at revalued amounts, and intangible assets that are measured at revalued amounts have not been scoped out of this Standard. Additional guidance on the treatment of impairment losses for assets measured at revalued amounts, and additional disclosures relating to such assets, were also included in this Standard. Assets measured at revaluated amounts are scoped out from IPSAS 21. Accordingly, guidance on the treatment of impairment losses related to such assets is also not included in IPSAS 21.
- The basis for classifying assets as non-cash-generating or cash-generating assets is based on the objective for which an asset will be used, and a section has been added in GRAP 21 to deal with the designation of assets.
- The concept of generating a commercial return has been modified to be consistent with the basis for classifying assets, and is based on whether the use of the asset will generate positive cash flows that are expected to be significantly higher than the cost of the asset.
- This Standard includes an indicator for the reversal of an impairment loss relating to the restoration of the service potential of an asset following physical damage to the asset.
- IPSAS 21 requires the disclosure of criteria developed to distinguish cash-generating assets from non-cash-generating assets.
- Transitional provisions applicable to this Standard of GRAP are dealt with differently than in IPSAS 21.
- A flow chart is included as an appendix to assist entities in assessing whether a non-cash-generating asset is impaired and to determine the recoverable service amount when one of the impairment indicators have been triggered.

- The appendices with illustrative examples on indications of impairment and measurement of impairment loss have been deleted from this Standard.

PART 2: Amendments to the Standard of GRAP on *Impairment of Cash-generating Assets*

Amended text is shown with new text underlined, deleted text struck through and text that has been relocated is indicated with a double underline. The following paragraphs in GRAP 26 have been amended:

…

Scope

…

.03 An entity shall first apply the Standard of GRAP on Impairment of Non-cash-generating Assets to designate its assets as either non-cash-generating or cash-generating in accordance with paragraphs .13A to .16C of that Standard. Entities that designate their assets ~~manage~~ as ~~non-~~cash-generating assets ~~as defined in paragraph .10~~ shall apply ~~the~~ this Standard ~~of GRAP on Impairment of Non-cash-generating Assets to such assets~~. For assets that are designated as non-cash-generating assets, ~~E~~entities ~~that hold cash-generating assets~~ shall apply the requirements of the~~this~~ Standard of GRAP on Impairment of Non-cash-generating Assets ~~to cash-generating assets~~.

…

Definitions

.10 The following terms are used in this Standard with the meanings specified:

Cash-generating assets are assets used ~~managed~~ with the objective of generating a commercial return. Commercial return means that positive cash flows are expected to be significantly higher than the cost of the asset.

A cash-generating unit is the smallest identifiable group of assets used ~~managed~~ with the objective of generating a commercial return that generates cash inflows from continuing use that are largely independent of the cash inflows from other assets or groups of assets. Commercial return means that positive cash flows are expected to be significantly higher than the cost of the asset.

Costs of disposal are incremental costs directly attributable to the disposal of an asset, excluding finance costs and income tax expense.

Fair value less costs to sell is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.

An <u>impairment</u> is a loss in the future economic benefits or service potential of an asset, over and above the systematic recognition of the loss of the asset's future economic benefits or service potential through depreciation.

An <u>impairment loss of a cash-generating asset</u> is the amount by which the carrying amount of an asset exceeds its recoverable amount.

<u>Non-cash-generating assets</u> are assets other than cash-generating assets.

The <u>recoverable amount</u> of an asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use.

<u>Value in use of a cash-generating asset</u> is the present value of the estimated future cash flows expected to be derived from the continuing use of an asset and from its disposal at the end of its useful life.

Terms defined in other Standards of GRAP are used in this Standard with the same meaning as in those other Standards.

~~Cash-generating assets and non-cash-generating assets~~

~~.11 Even though most entities normally have service delivery as their objective, management can exercise discretion to acquire and manage assets to generate a commercial return. Some assets may be managed solely as non-cash-generating assets, while others may be managed as cash-generating assets that generate a commercial return.~~

~~.12 Cash-generating assets are assets managed with the objective of generating a commercial return. An asset generates a commercial return when it is deployed in a manner consistent with that adopted by a profit-oriented entity. Managing an asset to generate a "commercial return" indicates that an entity intends to generate positive cash inflows from the asset (or from the cash-generating unit of which the asset is a part) and earn a commercial return that reflects the risk involved in managing the asset. An asset may be managed with the objective of generating a commercial return even though it does not meet that objective during a particular reporting period. Conversely, an asset may be a non-cash-generating asset even though it may be breaking even or generating a commercial return during a particular reporting period. Unless stated otherwise, references to "an asset" or "assets" in the following paragraphs of this Standard are references to "cash-generating asset(s)".~~

~~.13 There are a number of circumstances in which entities may manage some assets with the objective of generating a commercial return, although the majority of assets are not managed for that purpose. For example, a hospital may deploy a building for fee-paying patients. Cash-generating assets of an entity may operate independently of the non-cash-generating assets of the entity.~~

~~.14 In certain instances, an asset may generate cash flows although it is managed for service delivery purposes. For example, a waste disposal plant is operated to ensure the safe disposal of medical waste generated by state controlled hospitals, but the plant also treats a small amount of medical waste generated by other private hospitals on a commercial basis. The treatment of medical waste from the private hospitals is incidental to the activities of the plant, and the assets~~

~~that generate cash flows cannot be distinguished from the non-cash-generating assets.~~

~~.15 In other instances, an asset may generate cash flows and also be managed for non-cash-generating purposes. For example, a public hospital has ten wards, nine of which are managed for fee paying patients on a commercial basis, and the other is managed for non-fee paying patients. Patients from both wards jointly use other hospital facilities (for example, operating facilities). The extent to which the asset is managed with the objective of providing a commercial return needs to be considered to determine whether the entity should apply the provisions of this Standard or the Standard of GRAP on *Impairment of Non-cash-generating Assets*. If, as in this example, the non-cash-generating component is an insignificant component of the arrangement as a whole, the entity applies this Standard rather than the Standard of GRAP on *Impairment of Non-cash-generating Assets*.~~

~~.16 In some cases, it may not be clear whether the objective of managing an asset is to generate a commercial return. In such cases, it is necessary to evaluate the significance of the cash flows. It may be difficult to determine whether the extent to which the asset generates cash flows is so significant that this Standard is applicable, rather than the Standard of GRAP on *Impairment of Non-cash-generating Assets*. Judgement is needed to determine which Standard to apply. An entity develops criteria so that it can exercise that judgement consistently in accordance with the definition of cash-generating assets and non-cash-generating assets and with the related guidance in paragraphs .11 to .15. Paragraph .116 requires an entity to disclose the criteria used in making this judgement. However, given the overall objectives of most entities, the presumption is that assets are non-cash-generating in these circumstances and, therefore, the Standard of GRAP on *Impairment of Non-cash-generating Assets* will apply.~~

…

.13 Unless stated otherwise, references to "an asset" or "assets" in the following paragraphs of this Standard are references to "cash-generating asset(s)".

…

Reversing an impairment loss

…

.100 In assessing whether there is any indication that an impairment loss recognised in prior periods for an asset may no longer exist or may have decreased, an entity shall consider, as a minimum, the following indications:

External sources of information

(a) The asset's market value has increased significantly during the period.

(b) Significant changes with a favourable effect on the entity have taken place during the period, or will take place in the near future, in the

technological, market, economic or legal environment in which the entity operates or in the market to which the asset is dedicated.

(c) Market interest rates or other market rates of return on investments have decreased during the period, and those decreases are likely to affect the discount rate used in calculating the asset's value in use and increase the asset's recoverable amount materially.

Internal sources of information

(cA) Evidence is available that indicates that the asset has been restored following physical damage to the asset.

(d) Significant changes with a favourable effect on the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, the asset is used or is expected to be used. These changes include costs incurred during the period to improve or enhance the asset's performance, restructure the operation to which the asset belongs, or a decision to use rather than dispose of an asset.

(e) A decision to resume construction of the asset that was previously halted before it was completed or in a usable condition.

(f) Evidence is available from internal reporting that indicates that the economic performance of the asset is, or will be, better than expected.

…

Redesignation of assets

.114 The redesignation of an asset from a cash-generating asset to a non-cash generating asset or from a non-cash-generating asset to a cash-generating asset shall only occur when there is clear evidence that such a redesignation is appropriate. A redesignation, by itself, does not necessarily trigger an impairment test or a reversal of an impairment loss. At the subsequent reporting date after a redesignation, an entity shall consider, as a minimum, the listed indications in paragraph 23.

.115 When there has been a change in the manner in which an entity uses an asset that results in positive cash flows that are not expected to be significantly higher than the cost of the asset, an entity~~There are circumstances in which entities~~ shall ~~may decide that it is appropriate to~~ redesignate a cash-generating asset as a non-cash-generating asset.~~ For example, an effluent treatment plant was constructed primarily to treat industrial effluent from an industrial estate at commercial rates and excess capacity has been used to treat effluent from a social housing unit, for which no charge is made. The industrial estate has recently closed and, in future, the site will be developed for social housing purposes. In light of the closure of the industrial estate the entity decides to redesignate the effluent treatment plant as a non-cash-generating asset.~~ For example, an entity that previously used an asset with the objective of generating a commercial return makes a policy decision to use that asset to provide services to the public at a nominal fee. This change in objective results in the entity using the asset in a way that no longer generates a commercial return. The entity will redesignate that asset from cash-generating to a non-cash-generating asset.

Disclosure

.116 An entity shall disclose in the summary of accounting policies, the judgements management has made in applying the criteria ~~developed by the entity to distinguish~~ to designate assets as cash-generating assets or ~~from~~ non-cash-generating assets.

…

Transitional provisions

Initial adoption of the Standards of GRAP

.127 The transitional provisions to be applied by entities on the initial adoption of this Standard are prescribed in a directive(s). The provisions of this Standard should be read in conjunction with each applicable directive.

Amendments to Standards of GRAP

.128 Paragraphs .10, .12, .13, .14, .15, .16, .23, .26, .28, .80 .100 and .120 were amended and paragraph .11 was added by the Improvements to the Standards of GRAP issued on 1 April 2014. An entity shall apply these amendments prospectively for annual periods beginning on or after 1 April 2015. If an entity elects to apply these amendments earlier, it shall disclose this fact.

.128A Paragraphs .03, .10, .100, .115 and .116 were amended and paragraphs .11, to.16 were deleted by the Amendments to the Standards of GRAP issued on [Day Month Year]. An entity shall apply these amendments prospectively for annual financial periods beginning on or after [Day Month Year]. If an entity elects to apply these amendments earlier, it shall disclose this fact.

.128B Where the application of the amendments in paragraph .128A result in the redesignation of existing assets from cash-generating asset to non-cash-generating asset or from non-cash-generating asset to a cash-generating asset, an entity shall assess whether that redesignation triggers an impairment test or a reversal of an impairment loss.

Effective date

Initial adoption of the Standards of GRAP

.129 An entity shall apply this Standard of GRAP for annual financial statements covering periods beginning on or after a date to be determined by the Minister of Finance in a regulation to be published in accordance with section 91(1)(b) of the Public Finance Management Act, Act No. 1 of 1999, as amended.

Entities already applying Standards of GRAP

.130 ***An entity shall apply amendments to this Standard of GRAP for annual financial statements covering periods beginning on or after [Day Month Year] ~~1 April 2015~~. Earlier application is encouraged. If an entity applies these amendments for a period beginning before[Day Month Year] ~~1 April 2015~~, it shall disclose that fact.***

Basis for conclusions

This basis for conclusions gives the Accounting Standards Board's (the Board's) reasons for accepting or rejecting certain solutions related to the accounting for impairment of cash-generating assets. This basis for conclusions accompanies, but is not part of, the Standard of GRAP on Impairment of Cash-generating Assets (GRAP 26).

Introduction

BC1. This Standard of GRAP prescribes the procedures that an entity applies to determine whether a cash-generating asset is impaired and establishes how the impairment is recognised and measured. This Standard is primarily drawn from the International Public Sector Accounting Standard on *Impairment of Cash-generating Assets* (IPSAS 26). In developing this Standard, the Board also considered pronouncements issued by other standard setting bodies dealing with the accounting for impairment of assets.

BC2. This basis for conclusions summarises the significant departures that are made from IPSAS 26 and the reasons for such departures.

Scope

Inclusion of property, plant and equipment carried at revalued amounts

BC3. Property, plant and equipment carried at revalued amounts in accordance with the revaluation model are within the scope of the International Accounting Standard on *Impairment of Assets* (IAS 36).

BC4. The scope of IPSAS 21, however, excludes non-cash-generating property, plant and equipment carried at revalued amounts in accordance with the revaluation model in the International Public Sector Accounting Standard on *Property, Plant and Equipment* (IPSAS 17). The basis for conclusions in IPSAS 21 states that the IPSASB is of the view that assets carried at revalued amounts in accordance with the revaluation model in IPSAS 17 will be revalued with sufficient regularity to ensure that they are carried at an amount that is not materially different from their fair value at the reporting date. Impairment will therefore be taken into account in that valuation.

BC5. A similar scope exclusion for cash-generating property, plant and equipment carried at revalued amounts was included in IPSAS 26. The IPSASB concluded that it would be onerous to impose a requirement to test for impairment in addition to the existing requirement in IPSAS 17 that requires assets to be revalued with sufficient regularity to ensure that they are carried at an amount that is not materially different from their fair value at the reporting date. Therefore, on balance, the IPSASB concluded that consistency with IPSAS 21 should take precedence.

BC6. In its argument to exclude property, plant and equipment carried at revalued amounts from the scope of IPSAS26, the IPSASB noted that in IAS 36 the maximum amount of an impairment loss is the disposal costs. This is particularly relevant in cases where the fair value of an item of property, plant and equipment is its market value. The IPSASB is of the view that, in most cases, these will not be material and, from a practical point of view, it is not necessary to measure an asset's recoverable service amount and to recognise an impairment loss for the disposal costs of the asset.

BC7. The Board however agrees with the scope inclusion of property, plant and equipment carried at revalued amounts as in IAS 36. The Board is the view that it will not be too onerous to assess at each reporting date whether there is an indication that an asset may be impaired, or that an impairment loss recognised in prior periods for the asset may no longer exist.

BC8. The Board is also of the view that entities may not revalue their assets with "sufficient regularity", as the cost of revaluing certain public sector assets may initially be quite expensive. The disposal costs of certain specialised assets in the public sector therefore may well be significant. The scope exclusion for cash-generating property, plant and equipment carried at revalued amounts is therefore not included in this Standard.

Inclusion of intangible assets carried at revalued amounts

BC9. For similar reasons as those expressed for the scope exclusion of property, plant and equipment carried at revalued amounts, the IPSASB also scoped out the impairment of cash-generating intangible assets carried at revalued amounts. IAS 36, however, includes the impairment of such intangible assets in the scope of the Standard.

BC10. The Board, for similar reasons as those expressed in the scope inclusion of property, plant and equipment carried at revalued amounts, agrees with the scope inclusion of impairment of intangible assets carried at revalued amounts as in IAS 36. The scope exclusion for the impairment of cash-generating intangible assets carried at revalued amounts is therefore not included in this Standard.

Treatment of goodwill

BC11. IAS 36 contains extensive requirements and guidance on the impairment of goodwill, the allocation of goodwill to cash-generating units and testing cash-generating units with goodwill for impairment. The Standard of GRAP on *Transfer of Functions Between Entities Not Under Common Control* requires that the difference between the assets acquired and liabilities assumed and the consideration transferred (if any) as of the acquisition date in surplus or deficit. As no goodwill is recognised in the statement of financial position, the principles of the impairment of goodwill is not applicable.

Designation of an asset as cash-generating or non-cash-generating

BC12. In responding to the concerns raised by many respondents to its Improvements Project for 2013, the Board considered how it can simplify and streamline the principles relating to the distinction between cash-generating and non-cash-generating assets.

BC13. The issues identified by respondents related to applying the concept of generating a commercial return in the public sector. There have been varying interpretations of what constitutes a commercial return and some hold the view that the primary objective of deploying most assets in the public sector cannot be to generate a commercial return as the primary objective is service delivery.

BC14. The Board noted that to adequately address the concerns raised, the classification of cash-generating and non-cash-generating should move away from an assessment of whether an asset is managed with the objective of generating a commercial return. The Board concluded that the classification should be based on an entity's objective for using the asset.

BC15. The Board observed that entities in the public sector usually use assets with the objective of delivering services and/or to generate positive cash flows. The Board agreed that the objective of using the assets should be applied as a basis to determine whether the assets are cash-generating or non-cash-generating. It noted that when an entity decides to construct or purchase an asset, it will usually have a predetermined objective for using an asset. The Board acknowledged that the principles it has set for the classification of assets may be difficult to apply in cases where an entity uses its assets with the objective of delivering services and also generating positive cash flows. The Board concluded that the principles in the Standards should also clarify how entities should determine the classification if the overall objectives of using the asset are unclear. The Board agreed that it is necessary to include what the presumption is in respect of assets used for dual-purposes.

BC16. As part of the simplification and streamlining the impairment requirements in the Standards, the Board considered the principles underpinning the value in use concept applicable to non-cash-generating assets in GRAP 21. In particular, the Board considered the deprival value model, which is applied mostly in Australia, United Kingdom and New Zealand to select a current measurement basis when preparing financial statements. The model is premised on the fact that if an entity has an asset, an entity should measure that asset at the value it would be deprived of if the entity lost that asset, which is its replacement cost. The model also notes that the value the entity is deprived of would be based on what the entity could replace the asset with, but also considers that an entity owns that asset and can therefore operate the asset in a certain manner. The Board adopted the thinking behind this model as a basis to support what it considers the best measurement basis for determining value in use in the public sector.

BC17. It is this thinking that supports the Board's observations that when an entity uses its assets with the objective of delivering services, the most relevant measurement basis to determine value in use is the depreciated replacement cost. This is because when an entity is deprived of an asset, the entity will incur a cost equivalent to the depreciated replacement cost to obtain the equivalent remaining service potential and economic benefits (including the net amount that would be received on disposal of the asset). As a result, the value of the asset to an entity cannot be higher than its depreciated replacement cost when it is used with the objective to deliver services. However, when the asset is used with the objective of generating cash flows that are expected to be significantly higher than the depreciated replacement cost, then the asset is a cash-generating asset and the most relevant measure of value in use is the discounted cash flows.

BC18. The Board believed that adopting this approach for classifying assets as either cash-generating or non-cash-generating would require less judgement and is suitable as entity-specific criteria can be subjective. Previously, the classification required management to apply judgement when assessing whether an entity is generating a commercial return and this proved to be problematic. In this approach the Board had substituted the idea of generating a commercial return with an entity's use of its assets with the objective of generating positive cash flows that are expected to be significantly higher than the cost of replacing the asset.

BC19. While respondents understood the Board's rationale for simplifying the requirements and moving away from the concept of generating a commercial return, they suggested that the Board consider not substituting the concept of generating a commercial return. They indicated that the previous guidance did not clearly explain this concept, which resulted in interpretation issues amongst preparers. These respondents observed that the introduction of the notion that a cash-generating asset is one that "generates positive cash flows that are expected to be significantly higher than the depreciated replacement cost" captures and explains clearly when an entity would be generating a commercial return. Consequently, the Board agreed not to move away from the concept of generating a commercial return.

BC20. Some respondents noted that while the Board's approach may achieve some simplification, they found the reference to the depreciated replacement cost when an entity is assessing the designation of its assets to be confusing. Some explained that the confusion stems from the following issues: (a) the idea that a depreciated replacement cost calculation is required to be performed and what other "evidence" would be necessary to support this assumption, and (b) issues have been raised about whether and how the assessment would need to be done to justify the designation on an ongoing basis.

BC21. Based on the feedback from respondents, the Board deliberated on the relevance of the proposed approach. The Board observed that many assets in the public sector are measured using a historical measurement basis. As a result, it concluded that the notion that positive cash flows from using the asset need to be higher than the cost of the asset at acquisition is appropriate, as the amounts charged for the services provided will include, or aim to recover, the depreciation based on the cost of the asset. The Board debated whether re-designations should be based on the cost of the asset or the depreciated replacement cost. It was agreed that the same measurement basis would be used for initial and subsequent designations as the historical cost measure is straightforward and the information readily available.

BC22. The Board concluded that, in applying the requirements of this Standard, it would not require entities to perform annual calculations to demonstrate what the entities' objectives of using the assets are. The Board's view is that an entity would have had a clear objective of how it would use its assets, and would have made certain calculations in setting its tariffs and understanding the basis of its cost structure, in order to reach the conclusion that its objective is to use its assets to generate a commercial return. The Board noted that it should clarify that the assessment is done initially, taking into account the overall long term objective of using the asset.

BC23. Part of the Board's considerations in the review project was assessing the feasibility of combining the two Standards into a single Standard. While there are similarities in the two Standards, and combining the Standards will result in the reduction of duplication of requirements, the Board considered those areas that are different and how it could respond to these dissimilarities. The Board concluded that it may be difficult to develop a single set of indicators suitable for both cash-generating and non-cash-generating assets, and that there is still merit in retaining two separate Standards. Respondents generally supported the Board's view.

BC24. After considering the amendments made to the designation of assets, the Board questioned the format of the two Standards. The Board believed that including the new section on the designation of assets in both Standards would create unnecessary duplication in the requirements. The Board agreed that the section on designations should only be included in GRAP 21, and a cross reference should be added to GRAP 26 that makes it clear that entities should first apply GRAP 21 to designate their assets, and thereafter apply the relevant Standard for their impairment of the assets.

Comparison with the International Public Sector Accounting Standard on *Impairment of Cash-Generating Assets* (January 2008)

The Standard of GRAP on *Impairment of Cash-generating Assets* is drawn primarily from the International Public Sector Accounting Standard on *Impairment of Cash-generating assets* (IPSAS 26). The main differences between this standard and IPSAS 26 are as follows*:*

- The definitions of cash-generating assets and cash-generating unit in this Standard are different from IPSAS 26.
- This Standard of GRAP uses different terminology, in certain instances, from IPSAS 26. The most significant example is the use of the term "net assets" in this Standard. The equivalent term in IPSAS 21 is "net assets/equity".
- Cash-generating property, plant and equipment that is measured at revalued amounts, and intangible assets that are measured at revalued amounts have not been scoped out of this Standard. Additional guidance on the treatment of impairment losses for assets measured at revalued amounts, and additional disclosures relating to such assets, were also included in this Standard. Assets measured at revalued amounts are scoped out from IPSAS 26. Accordingly, guidance on the treatment of impairment losses related to such assets is also not included in IPSAS 26.
- The guidance in this Standard has been aligned with the guidance in the Standard of GRAP on *Impairment of Non-cash-generating Assets* (GRAP 21).
- The basis for classifying assets as cash-generating or non-cash-generating assets is based on the objective for which an asset will be used. The classification of assets has been removed from GRAP 26, and entities are now required to make this distinction between assets using the guidance that has been added in GRAP 21.
- The concept of generating a commercial return has been modified to be consistent with the basis for classifying assets, and is based on whether the use of the asset will generate positive cash flows that are expected to be significantly higher than the cost of the asset.
- This Standard includes an indicator for the reversal of an impairment relating to the restoration of an asset following physical damage to the asset.
- IPSAS 26 requires the disclosure of criteria developed to distinguish cash-generating assets from non-cash-generating assets.
- Transitional provisions applicable to this Standard of GRAP are dealt with differently than in IPSAS 26.
- A flow chart is included as an appendix to assist entities in assessing whether a cash-generating asset or cash-generating unit is impaired and to determine the recoverable amount when one of the impairment indicators have been triggered.

- The appendices with illustrative examples on using present value techniques to measure value in use and illustrative guidance have been deleted in this Standard.