IAS 36: Allocating Corporate Costs to a Cash-generating Unit

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IAS 36 *Impairment of Assets* defines recoverable amount as the higher of an asset or cash-generating unit's fair value less costs of disposal and its value in use. When calculating the value in use, paragraphs 39 and 41 of IAS 36 provide the applicable guidance. The requirements in these paragraphs indicate overheads that are necessarily incurred to generate the cash inflows from the asset or cash-generating unit, and are directly attributable, or can be reasonably allocated to the asset or cash-generating unit, should be included in the cash outflows when calculating its value in use.

When considering corporate costs as an overhead cost, such costs can be broken down into two broad categories:

- costs to provide identifiable services to the entity's cash-generating units (for example, centralized functions such as information technology that the entity's cash-generating units utilize to operate); and
- stewardship costs (for example, board of directors' costs, public company costs, senior officer salaries, etc.).

It is presumed that corporate costs incurred to provide identifiable services to the entity's cash-generating unit would typically be viewed as necessarily incurred to generate the cash inflows of the cash-generating unit. Therefore, such costs should be allocated to the cash-generating unit in determining its value in use provided that the costs are either directly attributable or a reasonable allocation method exists. However, for stewardship costs, this presumption may differ.

Issue: Consider stewardship costs and whether such costs should be allocated as a cash outflow in the value in use calculation for a cash-generating unit.

View A – Generally, stewardship costs are necessarily incurred to generate the cash inflows of a cash-generating unit and should be allocated to the cash-generating unit (provided an allocation can be done on a reasonable and consistent basis) for purposes of measuring the cash-generating unit's value in use.

This view presumes that all costs, including stewardship costs, are necessarily incurred by the entity to operate its business and generate cash inflows, and should be included in the cash outflows of the cash-generating unit when determining value in use. While it could be noted that stewardship costs and other entity-specific costs may be excluded on the basis that a typical market participant may already have the necessary infrastructure in place to operate the cash-generating unit, the purpose of the value in use calculation in IAS 36 is to consider the present value of all entity-specific cash flows that contribute to the cash inflows of the cash-generating unit.

View B – Stewardship costs are often not necessarily incurred in order for the individual cash-generating unit of an entity to generate cash inflows and, therefore, should not be allocated to individual cash-generating units when determining value in use.

This view focuses on the words “necessarily incurred” and presumes that stewardship costs are often not costs that the cash-generating unit must incur to generate inflows (for example, the costs may relate more to capital management and future investment or divestiture decisions). While acknowledging that the value in use calculation is based on entity-specific rather than market participant assumptions, the fact that a market participant may consider a plan to eliminate such costs may suggest the costs are not necessarily incurred to generate the cash inflows of the cash-generating unit.

View C – Generally, stewardship costs are necessarily incurred to generate the cash inflows of a cash-generating unit. However, an allocation of these costs on a reasonable and consistent basis for purposes of measuring the cash-generating unit’s value in use is often not possible. Therefore, an allocation should not be made.

This view notes that stewardship costs are often incurred at a significantly higher level within the corporate structure than the level at which the impairment test is being performed. The contribution of such costs to the generation of cash inflows at the lower cash-generating level is so indirect, it could be considered often not possible to allocate stewardship costs on a reasonable and consistent basis to individual cash-generating units.

View D – Any one of Views A, B or C may be appropriate depending on specific facts and circumstances.

Under this view, it is noted that the treatment of stewardship costs in determining the value in use of a cash-generating unit is dependent on specific facts and circumstances of the situation and the nature of the costs.

The Group’s Discussion

Group members expressed diverse views on this issue but emphasized that it depends on the nature of the stewardship costs. The Group discussed two important factors to consider when determining whether stewardship costs should be included in the value in use calculation of an asset or cash-generating unit. These two factors are identifying whether the stewardship costs are necessarily incurred to generate cash inflows and if the costs can be reasonably allocated on a consistent basis.

Several Group members tended to favour View A in that generally, stewardship costs are necessarily incurred from the perspective of the entity as a whole (i.e., similar to the concept of corporate assets). Since the entity is comprised of one or more cash-generating units, these costs should be fully allocated to an individual or group of cash-generating units. However, those Group members noted that there could be practical challenges to allocate the stewardship costs on a reasonable and consistent basis, thus echoing View C, because certain stewardship costs could be incurred at a significantly higher level in order to manage and operate multiple cash-generating units of an entity. It was also questioned whether certain costs such as board of directors' costs, senior officer salaries or public company costs are truly directly attributable to the cash flows of a specific cash-generating unit because these costs would likely still exist even if the asset was sold.

Nevertheless, Group members observed that stewardship costs could be significant in practice. Preparers are encouraged to exercise care when analyzing the nature of stewardship costs to determine whether to include or exclude them in the value in use calculation of a cash-generating unit in order to capture the appropriate amount of cash flows in the model.

The Group's discussion raises awareness about this item. No further action was recommended to the AcSB.