

Statutory Issue Paper No. 121

Accounting for the Impairment or Disposal of Real Estate Investments

- d. The sale of the asset is probable, and transfer of the asset is expected to qualify for recognition as a completed sale, within one year, except as permitted by paragraph 24;
- e. The asset is being actively marketed for sale at a price that is reasonable in relation to its current fair value;
- f. Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

If at any time the criteria in this paragraph are no longer met (except as permitted by paragraph 24), a long-lived asset classified as held for sale shall be reclassified as held and used in accordance with

Measurement

27. A long-lived asset classified as held for sale shall be measured at the lower of its carrying amount or fair value less cost to sell. If the asset is newly acquired, the carrying amount of the asset shall be established based on its fair value less cost to sell at the acquisition date. A long-lived asset shall not be depreciated (amortized) while it is classified as held for sale. Interest and other expenses attributable to the liabilities of a disposal classified as held for sale shall continue to be accrued.

28. Costs to sell are the incremental direct costs to transact a sale, that is, the costs that result directly from and are essential to a sale transaction and that would not have been incurred by the entity had the decision to sell not been made. Those costs include broker commissions, legal and title transfer fees, and closing costs that must be incurred before legal title can be transferred. Those costs exclude expected future losses associated with the operations of a long-lived asset while it is classified as held for sale.

29. The carrying amounts of any assets that are not covered by this Statement that are included in a disposal classified as held for sale shall be adjusted in accordance with other applicable statements of statutory accounting principles prior to measurement.

30. A realized loss shall be recognized in the summary of operations for any initial or subsequent write-down to fair value less cost to sell. A gain shall not be recognized for any subsequent increase in fair value less cost to sell until the asset is sold. The loss shall adjust only the carrying amount of a long-lived asset, whether classified as held for sale individually or as part of a disposal group. A gain or loss not previously recognized that results from the sale of a long-lived asset shall be recognized at the date{ from7nj fa50lived)3y

Reporting a Long-Lived Asset or Disposal Group Classified as Held for Sale

35. A long-lived asset classified as held for sale shall be presented separately in the balance sheet. The assets and liabilities of a disposal classified as held for sale shall be presented separately in the asset and liability sections, respectively, of the balance sheet. 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 on the face of the balance sheet or in the notes to financial statements (paragraph 39).

Reporting Impairment

36. Any impairment loss recognized on long-lived assets shall be recorded in the summary of operations as a realized loss.

Disclosures

37. The following information shall be disclosed in the notes to the financial statements that include the period in which an impairment loss is recognized:

- a. A description of the impaired assets and the facts and circumstances leading to the impairment;
- b. The amount of the impairment loss and how fair value was determined; and

38. The caption in the summary of operations, which includes the impairment loss.

39. The following information shall be disclosed in the notes to the financial statements that cover the period in which a long-lived asset either has been sold or is classified as held for sale:

- a. A description of the facts and circumstances leading to the expected disposal, the expected manner and timing of that disposal.
- b. If applicable, the gain or loss recognized (and the amount of the loss recognized) and the amount of the gain or loss recognized (and the amount of the loss recognized) and the amount of the gain or loss recognized (and the amount of the loss recognized).

DISCUSSION

42. FAS 144 supersedes FAS 121 and in part APB 30. FAS 144 retains the requirements of FAS 121 to (a) recognize an impairment loss only if the carrying amount of a long-lived asset is not recoverable from its undiscounted cash flows and (b) measure an impairment loss as the difference between the carrying amount and fair value of the asset. FAS 144 requires that a long-lived asset to be abandoned, exchanged for a similar productive asset, or distributed to owners in a spinoff be considered held and used until it is disposed of. FAS 144 also sets forth that the accounting model for long-lived assets to be disposed of by sale is used for all long-lived assets, whether previously held and used or newly acquired. FAS 144 also resolves implementation issues that came about in the application of existing guidance.

43. SSAP No. 40 states that real estate investments shall be reported in the balance sheet categories of properties occupied by the company, properties held for the production of income, and properties held for sale. However, the accounting guidance in FAS 144 distinguishes between long-lived assets to be held and used and long-lived assets to be disposed of. For statutory accounting purposes, long-lived assets to be held and used encompass properties occupied by the company and properties held for the production of income and will be referred to as such in this issue paper. Further, FAS 144 bifurcates the category of long-lived assets to be disposed of into long-lived assets to be disposed of other than by sale and long-lived assets to be disposed of by sale. In this issue paper, long-lived assets to be disposed of other than by sale shall be classified either as properties occupied by the company or as properties held for the production of income, as set forth in paragraph 27 of FAS 144 which is adopted in this issue paper. Long-lived assets to be disposed of by sale shall be classified as properties held for sale.

44. FAS 144 contains substantial guidance concerning the concept of grouping of assets for the purposes of measurement of an impairment loss. Grouping would seem to allow for the offsetting of gains on certain assets with losses on other assets in the same grouping, possibly resulting in no impairment loss being recognized. This is contrary to the concept of conservatism in the Statement of Concepts. As such, grouping of assets for the purpose of determining whether an impairment loss has occurred will not be allowed for statutory accounting purposes.

45. During the drafting process of this issue paper, an initial determination was made that SSAP Nos. 24, 40, 68 would be amended as a result of adopting FAS 144. Ultimately, only SSAP No. 40 was amended relative to adoption of FAS 144 as discussed below.

46. This issue paper adopts FAS 144 with modification to paragraphs 9, 17, 18, 19, 21, 25, 28, 35, 36, 37, 41, 42, 44, 45 and 47. Further, this issue paper rejects paragraphs 10-14, paragraphs 22-24, 26.d., and 43 of FAS 144. Refer to paragraph 47 of this issue paper for additional information with regard to these paragraphs.

47. The following modifications to FAS 144 were made in order to maintain consistency with current statutory accounting principles and the Statement of Concepts:

- a. Paragraph 9 is amended to require that changes in depreciation estimates and methods and amortization periods found as a result of a test for recoverability should be accounted for in accordance with SSAP No. 3;
- b. Paragraphs 10-14, which address the grouping of assets, are rejected, as reporting entities should apply the guidance in this statement to each of its assets on an individual basis;
- c. Paragraphs 17, 18, 19 and 21 discuss estimates of future cash flows used to test the recoverability of a long-lived asset, and states that a probability-weighted approach may be useful in considering the likelihood of those possible outcomes. For statutory accounting purposes, reporting entities shall use their best estimate in testing the recoverability of a long-lived asset;

- d. Paragraphs 22-24, which discuss fair value, are rejected. The definition of fair value is in the glossary to the Statement of Statutory Accounting Principles. In addition, this statement allows a modification to use for determining the fair value of properties occupied by company.
- e. Paragraph 25 is amended to require that an impairment loss on properties occupied by the company and properties held for the production of income shall be recorded in the summary of operations as a realized loss;
- f. Paragraph 28 is amended to require that changes in depreciation estimates shall be accounted for in accordance with SSAP No. 3;
- g. If the sale is expected to occur beyond one year, paragraph 35 allows the cost to sell to be discounted. For statutory accounting purposes, the cost to sell shall not be discounted;
- h. Paragraph 36 is amended to remove the reference to goodwill, as FAS 144 does not include goodwill within its scope unless such goodwill is included in an asset group that is or includes a reporting unit; paragraph 18 of this issue paper does not recognize a reporting unit. Paragraph 36 is further amended to require reporting entities to adjust all assets in accordance with other applicable statements of statutory accounting principles prior to measurement;
- i. Paragraph 37 is amended to clarify that losses recognized as a result of adjustments to fair value less cost to sell shall be recorded in the summary of operations as a realized gain/loss. Paragraph 37 is also modified to disallow the recognition of any gain for subsequent increases in fair value less cost to sell until the asset is sold. This is consistent with the concept of conservatism found in the Statement of Concepts;
- j. Within paragraphs 41, 42 and 44 of FAS 144 addressing discontinued operations, any reference to the phrase “component of an entity” is replaced with “segment” as defined in SSAP No. 24;
- k. Paragraph 42 is amended to state that the results of operations of a discontinued operation shall be reported consistently with the entity’s reporting of continuing operations. This is consistent with the guidance found in paragraph 5 of SSAP No. 24;
- l. Paragraph 44 is amended to state that adjustments to amounts previously reported related to continuing operations shall be reported consistently with the entity’s reporting of continuing operations. This is consistent with the guidance found in paragraph 5 of SSAP No. 24. In addition, subparagraphs a. through c. of paragraph 44 are adopted into paragraph 5 of SSAP No. 24;
- m. Paragraph 45 is amended to state that a gain or loss on an asset classified as held for sale that has been disposed of shall be included in the summary of operations as a realized gain or loss;
- n. The disclosures in paragraphs 47.a. and 47.b. are adopted with respect to properties held for sale, except for the disclosures related to major classes of assets, as grouping has been

- o. Paragraph 26.d. requires the disclosure of the segment in which an impaired asset is reported. This paragraph is rejected, as statutory accounting requires accounting and reporting at the legal entity level. Further, any additional references to segments, reporting units, or disposal groups found in FAS 144 are also rejected, except with regard to a segment within the context of discontinued operations; and
- p. Paragraph 43 is rejected and the guidance related to the recognition of losses/income expected between the measurement date and the expected disposal date included in paragraph 4 of SSAP No. 24 is retained, as such guidance is consistent with the concept of conservatism in the Statement of Concepts.

48. Paragraphs 12-14 of FAS 121 address the impairment of goodwill, and paragraphs 12, 14.a. and 14.b. of FAS 121 were adopted in SSAP No. 68. However, paragraph 12 of FAS 121 was superseded by FASB Statement No. 142, Goodwill and Other Intangible Assets (FAS 142), which was rejected in SSAP No. 68. Given the applicability of the guidance found in paragraph 12 of FAS 121 to statutory accounting principles, the impairment guidance found in FAS 121, paragraph 12 is retained. Paragraph 12 of FAS 121 has been excerpted in Issue Paper No. 68—Business Combinations and Goodwill, paragraph 31.

RELEVANT STATUTORY ACCOUNTING AND GAAP GUIDANCE

Statutory Accounting

49. SSAP No. 40 paragraphs 4, 8, 9, 10, 11, and 19:
- 4. Real estate investments shall be reported net of encumbrances in the following balance sheet categories, with parenthetical disclosure of the amount of related encumbrances:
 - a. Properties occupied by the company;
 - b. Properties held for the production of income; and
 - c. Properties held for sale.
 - 8. The cost of property included in real estate investments, other than land, shall be depreciated over the estimated useful life, not to exceed fifty y

10. Properties that the reporting entity has the intent to sell or is required to sell shall be classified as properties held for sale and carried at the lower of depreciated cost or fair value less encumbrances and estimated costs to sell the property consistent with paragraph 16 of FAS 121. The intent to sell a property exists when management, having the authority to approve the action, has committed to a plan to dispose of the asset, either by sale or abandonment. Fair value of the asset shall be determined in accordance with

6. Additionally, the financial statements for the period encompassing the measurement date

7. For purposes of this Statement, impairment is the condition that exists when the carrying amount of a long-lived asset (asset group) exceeds its fair value. An impairment loss shall be recognized only if the carrying amount of a long-lived asset (asset group) is not recoverable and exceeds its fair value. The carrying amount of a long-lived asset (asset group) is not recoverable

a lower-level asset group that includes only part of a reporting unit. Estimates of future cash flows used to test that lower-level asset group for recoverability shall not be adjusted for the effect of excluding goodwill from the group.

13. Other than goodwill, the carrying amounts of any assets (such as accounts receivable and inventory) and liabilities (such as accounts payable, long-term debt, and asset retirement obligations) not covered by this Statement that are included in an asset group shall be adjusted in accordance with other applicable generally accepted accounting principles prior to testing the asset group for recoverability.

14. An impairment loss for an asset group shall reduce only the carrying amounts of a long-lived asset or assets of the group. The loss shall be allocated to the long-lived assets of the group on a pro rata basis using the relative carrying amounts of those assets, except that the loss allocated to an individual long-lived asset of the group shall not reduce the carrying amount of that asset below its fair value whenever that fair value is determinable without undue cost and effort. (Example 1 of Appendix A illustrates the allocation of an impairment loss for an asset group.)

New Cost Basis

15. If an impairment loss is recognized, the adjusted carrying amount of a long-lived asset shall be its new cost basis. For a depreciable long-lived asset, the new cost basis shall be depreciated (amortized) over the remaining useful life of that asset. Restoration of a previously recognized impairment loss is prohibited.

activities of a not-for-profit organization. If a subtotal such as "income from operations" is presented, it shall include the amount of that loss.

26. The following information shall be disclosed in the notes to the financial statements that include the period in which an impairment loss is recognized:

- a. A description of the impaired long-lived asset (asset group) and the facts and circumstances leading to the impairment
- b. If not separately presented on the face of the statement, the amount of the impairment loss and the caption in the income statement or the statement of activities that includes that loss
- c. The method or methods for determining fair value (whether based on a quoted market price, prices for similar assets, or another valuation technique)
- d. If applicable, the segment in which the impaired long-lived asset (asset group) is reported under FASB Statement No. 131, Disclosures about Segments of an Enterprise and Related Information.

Long-Lived Assets to Be Disposed Of Other than by Sale

27. A long-lived asset to be disposed of other than by sale (for example, by abandonment, in an exchange for a similar productive long-lived asset, or in a distribution to owners in a spinoff) shall continue to be classified as held and used until it is disposed of. Paragraphs 7-26 shall apply while the asset is classified as held and used. If a long-lived asset is to be abandoned or distributed to owners in a spinoff together with other assets (and liabilities) as a group and that disposal group is a component of an entity, paragraphs 41-44 shall apply to the disposal group at the date it is disposed of.

Long-Lived Asset to Be Abandoned

28. For purposes of this Statement, a long-lived asset to be abandoned is disposed of when it ceases to be used. If an entity commits to a plan to abandon a long-lived asset before the end of its previously estimated useful life, depreciation estimates shall be revised in accordance with Opinion 20 to reflect the use of the asset over its shortened useful life (refer to paragraph 9). A long-lived asset that has been temporarily idled shall not be accounted for as if abandoned.

Long-Lived Asset to Be Exchanged for a Similar Productive Long-Lived Asset or to Be Distributed to Owners in a Spinoff

29. For purposes of this Statement, a long-lived asset to be exchanged for a similar productive long-lived asset or to be distributed to owners in a spinoff is disposed of when it is exchanged or distributed. If the asset (asset group) is tested for recoverability while it is classified as held and used, the estimates of future cash flowlongcarryingfamng-lctivf aasset (asseosed sted rouposed-6(ange(f

cash flows used in that test shall consider the likelihood of possible outcomes that existed at the balance sheet date, including the assessment of the likelihood of the future sale of the asset. That assessment made as of the balance sheet date shall not be revised for a decision to sell the asset after the balance sheet date. An impairment loss, if any, to be recognized shall be measured as the amount by which the carrying amount of the asset (asset group) exceeds its fair value at the balance sheet date.

Measurement

34. A long-lived asset (disposal group) classified as held for sale shall be measured at the lower of its carrying amount or fair value less cost to sell. If the asset (disposal group) is newly acquired, the carrying amount of the asset (disposal group) shall be established based on its fair value less cost to sell at the acquisition date. A long-lived asset shall not be depreciated (amortized) while it is 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 accrued.

35. Costs to sell are the incremental direct costs to transact a sale, that is, the costs that result directly from and are essential to a sale transaction and that would not have been incurred by the entity had the decision to sell not been made. Those costs include broker commissions,

carrying amounts or fair values less cost to sell at that date. Any long-lived assets that will not be sold shall be reclassified as held and used in accordance with paragraph 38.

Reporting Long-Lived Assets and Disposal Groups to Be Disposed Of

Reporting Discontinued Operations

41. For purposes of this Statement, 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. A component of an entity may be a reportable segment or an operating segment (as those terms are defined in paragraph 10 of Statement 131), a reporting unit (as that term is defined in Statement 142), a subsidiary, or an asset group (as that term is defined in paragraph 4).

42. The results of operations of a component of an entity that either has been disposed of or is classified as held for sale shall be reported in discontinued operations in accordance with paragraph 43 if both of the following conditions are met: (a) the operations and cash flows of the component have been (or will be) eliminated from the ongoing operations of the entity as a result of the disposal transaction and (b) the entity will not have any significant continuing involvement in the operations of the component after the disposal transaction. (Examples 12-15 of Appendix A illustrate disposal activities that do or do not qualify for reporting as discontinued operations.)

43. In a period in which a component of an entity either has been disposed of or is classified as held for sale, the income statement of a business enterprise (or statement of activities of a not-for-profit organization) for current and prior periods shall report the results of operations of the component, including any gain or loss recognized in accordance with paragraph 37, in discontinued operations. The results of operations of a component classified as held for sale shall be reported in discontinued operations in the period(s) in which they occur. The results of discontinued operations, less applicable income taxes (benefit), shall be reported as a separate component of income before extraordinary items and the cumulative effect of accounting changes (if applicable). For example, the results of discontinued operations may be reported in the income statement of a business enterprise as follows:

Income from continuing operations before income taxes	\$XXXX
Income taxes	<u>XXX</u>
Income from continuing operations 24	\$XXXX
Discontinued operations (Note X)	
Loss from operations of discontinued Component X (including loss on disposal of \$XXX)	XXXX
Income tax benefit	<u>XXXX</u>
Loss on discontinued operations	<u>XXXX</u>
Net income	<u>\$XXXX</u>

A gain or loss recognized on the disposal shall be disclosed either on the face of the income statement or in the notes to the financial statements (paragraph 47.b.).

44. Adjustments to amounts previously reported in discontinued operations that are directly related to the disposal of a component of an entity in a prior period shall be classified separately in the current period in discontinued operations. The nature and amount of such adjustments shall be disclosed. Examples of circumstances in which those types of adjustments may arise include the following:

- a. The resolution of contingencies that arise pursuant to the terms of the disposal transaction, such as the resolution of purchase price adjustments and indemnification issues with the purchaser

- SSAP No. 40—Real Estate Investments

Generally Accepted Accounting Principles

- FASB Statement No. 12A Accounting for the Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of
- FASB Statement No. 144 Accounting for the Impairment or Disposal of Long-Lived Assets

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