Statement of Financial Accounting Standards No. 144

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FAS144 Summary

Accounting for the Impairment or Disposal of Long-Lived Assets

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Accounting for the Impairment or Disposal of Long-Lived Assets

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FAS 144: Accounting for the Impairment or Disposal of Long-Lived Assets

FAS 144 Summary

This Statement addresses financial accounting and reporting for the impairment or disposal of long-lived assets. This Statement supersedes FASB Statement No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of,* and the accounting and reporting provisions of APB Opinion No. 30, *Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions,* for the disposal of a *segment of a business* (as previously defined in that Opinion). This Statement also amends ARB No. 51, *Consolidated Financial Statements,* to eliminate the exception to consolidation for a subsidiary for which control is likely to be temporary.

Reasons for Issuing This Statement

Because Statement 121 did not address the accounting for a segment of a business accounted for as a discontinued operation under Opinion 30, two accounting models existed for long-lived assets to be disposed of. The Board decided to establish a single accounting model, based on the framework established in Statement 121, for long-lived assets to be disposed of by sale. The Board also decided to resolve significant implementation issues related to Statement 121.

Differences between This Statement, Statement 121, and Opinion 30 and Additional Implementation Guidance

Long-Lived Assets to Be Held and Used

This Statement retains the requirements of Statement 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. To resolve implementation issues, this Statement:

- Removes goodwill from its scope and, therefore, eliminates the requirement of Statement 121 to allocate goodwill to long-lived assets to be tested for impairment

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- Describes a probability-weighted cash flow estimation approach to deal with situations in which alternative courses of action to recover the carrying amount of a long-lived asset are under consideration or a range is estimated for the amount of possible future cash flows
- Establishes a "primary-asset" approach to determine the cash flow estimation period for a group of assets and liabilities that represents the unit of accounting for a long-lived asset to be held and used

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

This Statement 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. To resolve implementation issues, this Statement:

- Requires that the depreciable life of a long-lived asset to be abandoned be revised in accordance with APB Opinion No. 20, *Accounting Changes*
- Amends APB Opinion No. 29, *Accounting for Nonmonetary Transactions,* to require that an impairment loss be recognized at the date a long-lived asset is exchanged for a similar productive asset or distributed to owners in a spinoff if the carrying amount of the asset exceeds its fair value.

Long-Lived Assets to Be Disposed Of by Sale

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. That accounting model retains the requirement of Statement 121 to measure a long-lived asset classified as held for sale at the lower of its carrying amount or fair value less cost to sell and to cease depreciation (amortization). Therefore, discontinued operations are no longer measured on a net realizable value basis, and future operating losses are no longer recognized before they occur.

This Statement retains the basic provisions of Opinion 30 for the presentation of discontinued operations in the income statement but broadens that presentation to include a component of an entity (rather than a segment of a business). 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 that is classified as held for sale or that has been disposed of is presented as a discontinued operation if the operations and cash flows of the component will be (or have been) eliminated from the ongoing operations of the entity and the entity will not have any significant continuing involvement in the operations of the component.

To resolve implementation issues, this Statement:

- Establishes criteria beyond that previously specified in Statement 121 to determine when a long-lived asset is held for sale, including a group of assets and liabilities that represents the unit of accounting for a long-lived asset classified as held for sale. Among other things, those criteria specify that (a) the asset must be available for immediate sale in its present

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condition subject only to terms that are usual and customary for sales of such assets and (b) the sale of the asset must be probable, and its transfer expected to qualify for recognition as a completed sale, within one year, with certain exceptions.

- Provides guidance on the accounting for a long-lived asset if the criteria for classification as held for sale are met after the balance sheet date but before issuance of the financial statements. That guidance prohibits retroactive reclassification of the asset as held for sale at the balance sheet date. Therefore, the guidance in EITF Issue No. 95-18, "Accounting and Reporting for a Discontinued Business Segment When the Measurement Date Occurs after the Balance Sheet Date but before the Issuance of Financial Statements," is superseded.
- Provides guidance on the accounting for a long-lived asset classified as held for sale if the asset is reclassified as held and used. The reclassified asset is measured at the lower of its (a) carrying amount before being classified as held for sale, adjusted for any depreciation (amortization) expense that would have been recognized had the asset been continuously classified as held and used, or (b) fair value at the date the asset is reclassified as held and used.

How the Changes in This Statement Improve Financial Reporting

The changes in this Statement improve financial reporting by requiring that one accounting model be used for long-lived assets to be disposed of by sale, whether previously held and used or newly acquired, and by broadening the presentation of discontinued operations to include more disposal transactions. Therefore, the accounting for similar events and circumstances will be the same. Additionally, the information value of reported financial information will be improved. Finally, resolving significant implementation issues will improve compliance with the requirements of this Statement and, therefore, comparability among entities and the representational faithfulness of reported financial information.

How the Conclusions in This Statement Relate to the Conceptual Framework

In reconsidering the use of a measurement approach based on net realizable value, and the accrual of future operating losses required under that approach, the Board used the definition of a liability in FASB Concepts Statement No. 6, *Elements of Financial Statements*. The Board determined that future operating losses do not meet the definition of a liability.

In considering changes to Statement 121, the Board focused on the qualitative characteristics discussed in FASB Concepts Statement No. 2, *Qualitative Characteristics of Accounting Information*. In particular, the Board determined that:

- Broadening the presentation of discontinued operations to include more disposal transactions provides investors, creditors, and others with decision-useful information that is relevant in assessing the effects of disposal transactions on the ongoing operations of an entity
- Eliminating inconsistencies from having two accounting models for long-lived assets to be disposed of by sale improves comparability in financial reporting among entities, enabling

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users to identify similarities in and differences between two sets of economic events.

This Statement also incorporates the guidance in FASB Concepts Statement No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements,* for using present value techniques to measure fair value.

The Effective Date of This Statement

The provisions of this Statement are effective for financial statements issued for fiscal years beginning after December 15, 2001, and interim periods within those fiscal years, with early application encouraged. The provisions of this Statement generally are to be applied prospectively.

INTRODUCTION

1. This Statement addresses financial accounting and reporting for the impairment of long-lived assets and for long-lived assets to be disposed of. This Statement supersedes FASB Statement No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of.* However, this Statement retains the fundamental provisions of Statement 121 for (a) recognition and measurement of the impairment of long-lived assets to be held and used and (b) measurement of long-lived assets to be disposed of by sale.

2. This Statement supersedes the accounting and reporting provisions of APB Opinion No. 30, *Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions,* for segments of a business to be disposed of. However, this Statement retains the requirement of Opinion 30 to report discontinued operations separately from continuing operations and extends that reporting to a component of an entity that either has been disposed of (by sale, by abandonment, or in a distribution to owners) or is classified as held for sale. This Statement also amends ARB No. 51, *Consolidated Financial Statements,* to eliminate the exception to consolidation for a temporarily controlled subsidiary.

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

Scope

3. Except as indicated in paragraphs 4 and 5, this Statement applies to recognized long-lived

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assets of an *entity* [1] to be held and used or to be disposed of, including (a) capital leases of lessees, (b) long-lived assets of lessors subject to operating leases, (c) proved oil and gas properties that are being accounted for using the successful-efforts method of accounting,[2] and (d) long-term prepaid assets.[3]

4. If a long-lived asset (or assets) is part of a group that includes other assets and liabilities not covered by this Statement, this Statement applies to the group. In those situations, the unit of accounting for the long-lived asset is its group. For a long-lived asset or assets to be held and used, that group (hereinafter referred to as an *asset group*) represents the lowest level for which identifiable cash flows are largely independent of the cash flows of other groups of assets and liabilities. For a long-lived asset or assets to be disposed of by sale or otherwise, that group (hereinafter referred to as a *disposal group*) represents assets to be disposed of together as a group in a single transaction and liabilities directly associated with those assets that will be transferred in the transaction.[4] This Statement does not change generally accepted accounting principles applicable to those other individual 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 such groups.

5. This Statement does not apply to (a) goodwill, (b) intangible assets not being amortized, (c) long-term customer relationships of a financial institution, such as core deposit intangibles, credit cardholder intangibles, and servicing assets, (d) financial instruments, including investments in equity securities accounted for under the cost or equity method, (e) deferred policy acquisition costs, (f) deferred tax assets, and (g) unproved oil and gas properties that are being accounted for using the successful-efforts method of accounting. This Statement also does not apply to long-lived assets for which the accounting is prescribed by:

- FASB Statement No. 44, Accounting for Intangible Assets of Motor Carriers
- FASB Statement No. 50, *Financial Reporting in the Record and Music Industry*
- FASB Statement No. 63, *Financial Reporting by Broadcasters*
- FASB Statement No. 86, *Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed*
- FASB Statement No. 90, *Regulated Enterprises—Accounting for Abandonments and Disallowances of Plant Costs.*

6. Appendix C lists the accounting pronouncements affected by this Statement. Appendix D shows the status of FASB and Accounting Principles Board (APB) pronouncements that refer to impairment of long-lived assets, including those pronouncements that remain authoritative.[5]

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Long-Lived Assets to Be Held and Used

Recognition and Measurement of an Impairment Loss

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 if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset (asset group). That assessment shall be based on the carrying amount of the asset (asset group) at the date it is tested for recoverability, whether in use (paragraph 19) or under development (paragraph 20). An impairment loss shall be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.

When to Test a Long-Lived Asset for Recoverability

8. A long-lived asset (asset group) shall be tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. The following are examples of such events or changes in circumstances:

a. A significant decrease in the market price of a long-lived asset (asset group)
b. A significant adverse change in the extent or manner in which a long-lived asset (asset group) is being used or in its physical condition
c. A significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset (asset group), including an adverse action or assessment by a regulator
d. An accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of a long-lived asset (asset group)
e. A current-period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset (asset group)
f. A current expectation that, *more likely than not,*[6] a long-lived asset (asset group) will be sold or otherwise disposed of significantly before the end of its previously estimated useful life.

9. When a long-lived asset (asset group) is tested for recoverability, it also may be necessary to review depreciation estimates and method as required by APB Opinion No. 20, *Accounting Changes,* or the amortization period as required by FASB Statement No. 142, *Goodwill and Other Intangible Assets*.[7] Any revision to the remaining useful life of a long-lived asset resulting from that review also shall be considered in developing estimates of future cash flows used to test the asset (asset group) for recoverability (paragraph 18). However, any change in the

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accounting method for the asset resulting from that review shall be made only after applying this Statement.

Grouping Long-Lived Assets to Be Held and Used

10. For purposes of recognition and measurement of an impairment loss, a long-lived asset or assets shall be grouped with other assets and liabilities at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities. However, an impairment loss, if any, that results from applying this Statement shall reduce only the carrying amount of a long-lived asset or assets of the group in accordance with paragraph 14

11. In limited circumstances, a long-lived asset (for example, a corporate headquarters facility) may not have identifiable cash flows that are largely independent of the cash flows of other assets and liabilities and of other asset groups. In those circumstances, the asset group for that long-lived asset shall include all assets and liabilities of the entity.

12. Goodwill shall be included in an asset group to be tested for impairment under this Statement only if the asset group is or includes a *reporting unit*.[8] Goodwill shall not be included in 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.[9]

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

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impairment loss is prohibited.

Estimates of Future Cash Flows Used to Test a Long-Lived Asset for Recoverability

16. Estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) shall include only the future cash flows (cash inflows less associated cash outflows) that are directly associated with and that are expected to arise as a direct result of the use and eventual disposition of the asset (asset group). Those estimates shall exclude interest charges that will be recognized as an expense when incurred.

17. Estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) shall incorporate the entity's own assumptions about its use of the asset (asset group) and shall consider all available evidence. The assumptions used in developing those estimates shall be reasonable in relation to the assumptions used in developing other information used by the entity for comparable periods, such as internal budgets and projections, accruals related to incentive compensation plans, or information communicated to others. However, if alternative courses of action to recover the carrying amount of a long-lived asset (asset group) are under consideration or if a range is estimated for the amount of possible future cash flows associated with the likely course of action, the likelihood of those possible outcomes shall be considered. A probability-weighted approach may be useful in considering the likelihood of those possible outcomes. (Example 2 of Appendix A illustrates the use of that approach when alternative courses of action are under consideration.)

18. Estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) shall be made for the remaining useful life of the asset (asset group) to the entity. The remaining useful life of an asset group shall be based on the remaining useful life of the primary asset of the group. For purposes of this Statement, the *primary asset* is the principal long-lived tangible asset being depreciated or intangible asset being amortized that is the most significant component asset from which the asset group derives its cash-flow-generating capacity.[10] Factors that an entity generally should consider in determining whether a long-lived asset is the primary asset of an asset group include the following: (a) whether other assets of the group would have been acquired by the entity without the asset, (b) the level of investment that would be required to replace the asset, and (c) the remaining useful life of the asset relative to other assets of the group. If the primary asset is not the asset of the group with the longest remaining useful life, estimates of future cash flows for the group should assume the sale of the group at the end of the remaining useful life of the primary asset.

19. Estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) that is in use, including a long-lived asset (asset group) for which development is substantially complete, shall be based on the existing service potential of the asset (asset group) at the date it is tested. The service potential of a long-lived asset (asset group) encompasses its remaining useful life, cash-flow-generating capacity, and for tangible assets, physical output

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capacity. Those estimates shall include cash flows associated with future expenditures necessary to maintain the existing service potential of a long-lived asset (asset group), including those that replace the service potential of component parts of a long-lived asset (for example, the roof of a building) and component assets other than the primary asset of an asset group. Those estimates shall exclude cash flows associated with future capital expenditures that would increase the service potential of a long-lived asset (asset group).

20. Estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) that is under development shall be based on the expected service potential of the asset (group) when development is substantially complete. Those estimates shall include cash flows associated with all future expenditures necessary to develop a long-lived asset (asset group), including interest payments that will be capitalized as part of the cost of the asset (asset group).[11]

21. If a long-lived asset that is under development is part of an asset group that is in use, estimates of future cash flows used to test the recoverability of that group shall include the cash flows associated with future expenditures necessary to maintain the existing service potential of the group (paragraph 19) as well as the cash flows associated with all future expenditures necessary to substantially complete the asset that is under development (paragraph 20). (Example 3 of Appendix A illustrates that situation.)

Fair Value

22. The fair value of an asset (liability) is the amount at which that asset (liability) could be bought (incurred) or sold (settled) in a current transaction between willing parties, that is, other than in a forced or liquidation sale.[12] Quoted market prices in active markets are the best evidence of fair value and shall be used as the basis for the measurement, if available. However, in many instances, quoted market prices in active markets will not be available for the long-lived assets (asset groups) covered by this Statement. In those instances, the estimate of fair value shall be based on the best information available, including prices for similar assets (groups) and the results of using other valuation techniques.

23. A present value technique is often the best available valuation technique with which to estimate the fair value of a long-lived asset (asset group). Paragraphs 39–54 of FASB Concepts Statement No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements,* discuss the use of two present value techniques to measure the fair value of an asset (liability).[13] The first is expected present value, in which multiple cash flow scenarios that reflect the range of possible outcomes and a risk-free rate are used to estimate fair value. The second is traditional present value, in which a single set of estimated cash flows and a single interest rate (a rate commensurate with the risk) are used to estimate fair value. Either present value technique can be used for a fair value measurement. However, for long-lived assets (asset groups) that have uncertainties both in timing and amount, an expected present value technique will often be the

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appropriate technique. (Example 4 of Appendix A illustrates the use of that technique.)

24. If a present value technique is used, estimates of future cash flows shall be consistent with the objective of measuring fair value. Assumptions that marketplace participants would use in their estimates of fair value shall be incorporated whenever that information is available without undue cost and effort.[14] Otherwise, the entity may use its own assumptions.

Reporting and Disclosure

25. An impairment loss recognized for a long-lived asset (asset group) to be held and used shall be included in income from continuing operations before income taxes in the income statement of a business enterprise and in income from continuing operations in the statement of 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,*[15] 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

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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).[16] 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 flows used in that test shall be based on the use of the asset for its remaining useful life, assuming that the disposal transaction will not occur. In addition to any impairment losses required to be recognized while the asset is classified as held and used, an impairment loss, if any, shall be recognized when the asset is disposed of if the carrying amount of the asset (disposal group) exceeds its fair value. [17]

Long-Lived Assets to Be Disposed Of by Sale

Recognition

30. A long-lived asset (disposal group) to be sold shall be classified as held for sale in the period in which all of the following criteria are met:

a. Management, having the authority to approve the action, commits to a plan to sell the asset (disposal group).
b. The asset (disposal group) is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (disposal groups). (Examples 5–7 of Appendix A illustrate when that criterion would be met.)
c. An active program to locate a buyer and other actions required to complete the plan to sell the asset (disposal group) have been initiated.
d. The sale of the asset (disposal group) is probable,[18] and transfer of the asset (disposal group) is expected to qualify for recognition as a completed sale, within one year, except as permitted by paragraph 31. (Example 8 of Appendix A illustrates when that criterion would be met.)
e. The asset (disposal group) 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

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31), a long-lived asset (disposal group) classified as held for sale shall be reclassified as held and used in accordance with paragraph 38.

31. Events or circumstances beyond an entity's control may extend the period required to complete the sale of a long-lived asset (disposal group) beyond one year. An exception to the one-year requirement in paragraph 30(d) shall apply in the following situations in which such events or circumstances arise:

a. If at the date an entity commits to a plan to sell a long-lived asset (disposal group) the entity reasonably expects that others (not a buyer) will impose conditions on the transfer of the asset (group) that will extend the period required to complete the sale and (1) actions necessary to respond to those conditions cannot be initiated until after a *firm purchase commitment* [19] is obtained and (2) a firm purchase commitment is probable within one year. (Example 9 of Appendix A illustrates that situation.)
b. If an entity obtains a firm purchase commitment and, as a result, a buyer or others unexpectedly impose conditions on the transfer of a long-lived asset (disposal group) previously classified as held for sale that will extend the period required to complete the sale and (1) actions necessary to respond to the conditions have been or will be timely initiated and (2) a favorable resolution of the delaying factors is expected. (Example 10 of Appendix A illustrates that situation.)
c. If during the initial one-year period, circumstances arise that previously were considered unlikely and, as a result, a long-lived asset (disposal group) previously classified as held for sale is not sold by the end of that period and (1) during the initial one-year period the entity initiated actions necessary to respond to the change in circumstances, (2) the asset (group) is being actively marketed at a price that is reasonable given the change in circumstances, and (3) the criteria in paragraph 30 are met. (Example 11 of Appendix A illustrates that situation.)

32. A long-lived asset (disposal group) that is newly acquired and that will be sold rather than held and used shall be classified as held for sale at the acquisition date only if the one-year requirement in paragraph 30(d) is met (except as permitted by paragraph 31) and any other criteria in paragraph 30 that are not met at that date are probable of being met within a short period following the acquisition (usually within three months).

33. If the criteria in paragraph 30 are met after the balance sheet date but before issuance of the financial statements, a long-lived asset shall continue to be classified as held and used in those financial statements when issued.[20] The information required by paragraph 47(a) shall be disclosed in the notes to the financial statements. If the asset (asset group) is tested for recoverability (on a held-and-used basis) as of the balance sheet date, the estimates of future 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.[21] An impairment loss, if any, to be recognized shall be measured as

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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, 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 (disposal group) while it is classified as held for sale.[22] If the sale is expected to occur beyond one year as permitted in limited situations by paragraph 31, the cost to sell shall be discounted.

36. The carrying amounts of any assets that are not covered by this Statement, including goodwill, that are included in a disposal group classified as held for sale shall be adjusted in accordance with other applicable generally accepted accounting principles prior to measuring the fair value less cost to sell of the disposal group.[23]

37. A loss shall be recognized for any initial or subsequent write-down to fair value less cost to sell. A gain shall be recognized for any subsequent increase in fair value less cost to sell, but not in excess of the cumulative loss previously recognized (for a write-down to fair value less cost to sell). The loss or gain 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 (disposal group) shall be recognized at the date of sale.

Changes to a Plan of Sale

38. If circumstances arise that previously were considered unlikely and, as a result, an entity decides not to sell a long-lived asset (disposal group) previously classified as held for sale, the asset (disposal group) shall be reclassified as held and used. A long-lived asset that is reclassified shall be measured individually at the lower of its (a) carrying amount before the asset (disposal group) was classified as held for sale, adjusted for any depreciation (amortization) expense that would have been recognized had the asset (disposal group) been continuously classified as held and used, or (b) fair value at the date of the subsequent decision not to sell.

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39. Any required adjustment to the carrying amount of a long-lived asset that is reclassified as held and used shall be included in income from continuing operations in the period of the subsequent decision not to sell. That adjustment shall be reported in the same income statement caption used to report a loss, if any, recognized in accordance with paragraph 45. If a component of an entity is reclassified as held and used, the results of operations of the component previously reported in discontinued operations in accordance with paragraph 43 shall be reclassified and included in income from continuing operations for all periods presented.

40. If an entity removes an individual asset or liability from a disposal group previously classified as held for sale, the remaining assets and liabilities of the disposal group to be sold shall continue to be measured as a group only if the criteria in paragraph 30 are met. Otherwise, the remaining long-lived assets of the group shall be measured individually at the lower of their 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

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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	XXX	
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		XXXX
Loss on discontinued operations		XXXX
Net income		$XXXX

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
b. The resolution of contingencies that arise from and that are directly related to the operations of the component prior to its disposal, such as environmental and product warranty obligations retained by the seller
c. The settlement of employee benefit plan obligations (pension, postemployment benefits other than pensions, and other postemployment benefits), provided that the settlement is directly related to the disposal transaction.[25]

Reporting Disposal Gains or Losses in Continuing Operations

45. A gain or loss recognized for a long-lived asset (disposal group) classified as held for sale that is not a component of an entity shall be included in income from continuing operations before income taxes in the income statement of a business enterprise and in income from continuing operations in the statement of activities of a not-for-profit organization. If a subtotal such as "income from operations" is presented, it shall include the amounts of those gains or

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losses.

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

46. A long-lived asset classified as held for sale shall be presented separately in the statement of financial position. The assets and liabilities of a disposal group classified as held for sale shall be presented separately in the asset and liability sections, respectively, of the statement of financial position. Those assets and liabilities shall not be offset and presented as a single amount. The major classes of assets and liabilities classified as held for sale shall be separately disclosed either on the face of the statement of financial position or in the notes to financial statements (paragraph 47(a)).

Disclosure

47. The following information shall be disclosed in the notes to the financial statements that cover the period in which a long-lived asset (disposal group) 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, and, if not separately presented on the face of the statement, the carrying amount(s) of the major classes of assets and liabilities included as part of a disposal group
b. The gain or loss recognized in accordance with paragraph 37 and if not separately presented on the face of the income statement, the caption in the income statement or the statement of activities that includes that gain or loss
c. If applicable, amounts of revenue and pretax profit or loss reported in discontinued operations
d. If applicable, the segment in which the long-lived asset (disposal group) is reported under Statement 131.

48. If either paragraph 38 or paragraph 40 applies, a description of the facts and circumstances leading to the decision to change the plan to sell the long-lived asset (disposal group) and its effect on the results of operations for the period and any prior periods presented shall be disclosed in the notes to financial statements that include the period of that decision.

Effective Date and Transition

49. Except as specified in paragraphs 50 and 51, the provisions of this Statement shall be effective for financial statements issued for fiscal years beginning after December 15, 2001, and interim periods within those fiscal years. Early application is encouraged. Initial application of this Statement shall be as of the beginning of an entity's fiscal year. That is, if the Statement is

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initially applied prior to the effective date and during an interim period other than the first interim period, all prior interim periods of that fiscal year shall be restated. Restatement of previously issued annual financial statements is not permitted.[26] However, previously issued statements of financial position presented for comparative purposes shall be reclassified to reflect application of the provisions of paragraph 46 of this Statement for reporting disposal groups classified as held for sale.

50. The provisions of this Statement for long-lived assets (disposal groups) to be disposed of by sale or otherwise (paragraphs 27–45 and paragraphs 47 and 48) shall be effective for disposal activities initiated by an entity's commitment to a plan after the effective date of this Statement or after it is initially applied.

51. Except as provided in the following sentence, long-lived assets (disposal groups) classified as held for disposal as a result of disposal activities that were initiated prior to this Statement's initial application shall continue to be accounted for in accordance with the prior pronouncement (Statement 121 or Opinion 30) applicable for that disposal. If the criteria in paragraph 30 of this Statement are not met by the end of the fiscal year in which this Statement is initially applied, the related long-lived assets shall be reclassified as held and used in accordance with paragraph 38 of this Statement.

The provisions of this Statement need not be applied to immaterial items.

This Statement was adopted by the unanimous vote of the six members of the Financial Accounting Standards Board:

Edmund L. Jenkins, *Chairman*
G. Michael Crooch
John M. Foster
Gary S. Schieneman
Edward W. Trott
John K. Wulff

Appendix A: IMPLEMENTATION GUIDANCE

Introduction

A1. This appendix illustrates application of some of the provisions of this Statement in certain specific situations. The relevant paragraphs of this Statement are identified in the parenthetical

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notes. The examples do not address all possible situations or applications of this Statement. This appendix is an integral part of the standards provided in this Statement.

Example 1—Allocating an Impairment Loss

A2. This example illustrates the allocation of an impairment loss to the long-lived assets of an asset group (paragraph 14).

A3. An entity owns a manufacturing facility that together with other assets is tested for recoverability as a group. In addition to long-lived assets (Assets A–D), the asset group includes inventory, which is reported at the lower of cost or market in accordance with ARB No. 43, Chapter 4, "Inventory Pricing," and other current assets and liabilities that are not covered by this Statement. The $2.75 million aggregate carrying amount of the asset group is not recoverable and exceeds its fair value by $600,000. In accordance with paragraph 14, the impairment loss of $600,000 would be allocated as shown below to the long-lived assets of the group.

Asset Group	Carrying Amount	Pro Rata Allocation Factor	Allocation of Impairment (Loss)	Adjusted Carrying Amount
		(in $ 000s)		
Current assets	$400	—	—	$400
Liabilities	(150)	—	—	(150)
Long-lived assets:				
Asset A	590	24%	$(144)	446
Asset B	780	31	(186)	594
Asset C	950	38	(228)	722
Asset D	180	7	(42)	138
Subtotal—long-lived assets	2,500	100	(600)	1,900
Total	$2,750	100%	$(600)	$2,150

A4. If the fair value of an individual long-lived asset of an asset group is determinable without undue cost and effort and exceeds the adjusted carrying amount of that asset after an impairment loss is allocated initially, the excess impairment loss initially allocated to that asset would be reallocated to the other long-lived assets of the group. For example, if the fair value of Asset C is $822,000, the excess impairment loss of $100,000 initially allocated to that asset (based on its adjusted carrying amount of $722,000) would be reallocated as shown below to the other long-lived assets of the group on a pro rata basis using the relative adjusted carrying amounts of those assets.

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Long-Lived Assets of Asset Group	Adjusted Carrying Amount	Pro Rata Reallocation Factor	Reallocation of Excess Impairment (Loss)	Adjusted Carrying Amount after Reallocation
		(in $ 000s)		
Asset A	$446	38%	$(38)	$408
Asset B	594	50	(50)	544
Asset D	138	12	(12)	126
Subtotal	1,178	100%	(100)	1,078
Asset C	722		100	822
Total—long-lived assets	$1,900		$ 0	$1,900

Example 2—Probability-Weighted Cash Flows

A5. This example illustrates the use of a probability-weighted approach for developing estimates of future cash flows used to test a long-lived asset for recoverability when alternative courses of action are under consideration (paragraph 17).

A6. At December 31, 20X2, a manufacturing facility with a carrying amount of $48 million is tested for recoverability. At that date, 2 courses of action to recover the carrying amount of the facility are under consideration—sell in 2 years or sell at the end of its remaining useful life of 10 years. The facility has identifiable cash flows that are largely independent of the cash flows of other assets.

A7. The following table shows the range and probability of possible estimated cash flows expected to result from the use and eventual disposition of the facility assuming that (a) it is sold at the end of 2 years or (b) it is sold at the end of 10 years. Among other things, the range of possible estimated cash flows considers future sales levels (volume and price) and associated manufacturing costs in varying scenarios that consider (a) the likelihood that existing customer relationships will continue and (b) future economic (market) conditions. The probability assessments consider all information available without undue cost and effort. Such assessments are by their nature subjective and, in many situations, may be limited to management's best judgment about the probabilities of the best, worst, and most-likely scenarios.

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Course of Action	Cash Flow Estimate (Use)	Cash Flow Estimate (Disposition)	Cash Flow Estimate	Probability Assessment	Probability-Weighted Cash Flows
		(in $ millions)			
Sell in 2 years	$ 8	$30	$38	20%	$ 7.6
	11	30	41	50	20.5
	13	30	43	30	12.9
					$41.0
Sell in 10 years	36	1	37	20%	$ 7.4
	48	1	49	50	24.5
	55	1	56	30	16.8
					$48.7

A8. In computing the future cash flows used to test the facility for recoverability, the entity concludes that there is (a) a 60 percent probability that the facility will be sold at the end of 2 years and (b) a 40 percent probability that the facility will continue to be used for its remaining estimated useful life of 10 years. The following table shows the computation of future cash flows based on the probability of those alternative courses of action.[27] As shown, those future cash flows are $44.1 million (undiscounted). Therefore, the carrying amount of the facility of $48 million would not be recoverable.

Course of Action	Probability-Weighted Cash Flows	Probability Assessment (Course of Action)	Expected Cash Flows
	(in $ millions)		
Sell in 2 years	$41.0	60%	$24.6
Sell in 10 years	48.7	40	19.5
			$44.1

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Example 3 —Estimates of Future Cash Flows Used to Test an Asset Group for Recoverability

A9. A long-lived asset that is under development may be part of an asset group that is in use. In that situation, estimates of future cash flows used to test the recoverability of that group shall include the cash flows associated with future expenditures necessary to maintain the existing service potential of the group as well as the cash flows associated with future expenditures necessary to substantially complete the asset that is under development (paragraph 21).

A10. An entity engaged in mining and selling phosphate estimates future cash flows from its commercially minable phosphate deposits in order to test the recoverability of the asset group that includes the mine and related long-lived assets (plant and equipment). Deposits from the mined rock must be processed in order to extract the phosphate. As the active mining area expands along the geological structure of the mine, a new processing plant is constructed near the production area. Depending on the size of the mine, extracting the minable deposits may require building numerous processing plants over the life of the mine. In testing the recoverability of the mine and related long-lived assets, the estimates of future cash flows from its commercially minable phosphate deposits would include cash flows associated with future expenditures necessary to build all of the required processing plants.

Example 4—Expected Present Value Technique

A11. This example illustrates the application of an expected present value technique to estimate the fair value of a long-lived asset in the absence of an observable market price (paragraph 23).[28] It is based on the facts provided for the manufacturing facility in Example 2.

A12. Consistent with an objective of measuring fair value, the entity's estimates of future cash flows used to test the manufacturing facility for recoverability in Example 2 are adjusted to incorporate assumptions that, based on available information, marketplace participants would use in their estimates of the fair value of the asset. The net effect of those adjustments is to increase the entity's estimates of future cash flows (on an undiscounted basis) by approximately 15 percent.[29]

A13. The following table shows by year the range and probability of possible cash flows expected to result from the use and eventual disposition of the facility over its remaining useful life of 10 years (Example 2), adjusted for market assumptions. It also shows by year the computation of expected cash flows.

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Year	Total Cash Flow Estimate (Market) (in $ millions)	Probability Assessment	Expected Cash Flows
1	$4.6	20%	$ .9
	6.3	50	3.2
	7.5	30	2.3
			$6.4
2	$4.6	20%	$ .9
	6.3	50	3.2
	7.5	30	2.3
			$6.4
3	$4.3	20%	$ .9
	5.8	50	2.9
	6.7	30	2.0
			$5.8
4	$4.3	20%	$ .9
	5.8	50	2.9
	6.7	30	2.0
			$5.8
5	$4.0	20%	$ .8
	5.4	50	2.7
	6.4	30	1.9
			$5.4
6	$4.0	20%	$ .8
	5.4	50	2.7
	6.4	30	1.9
			$5.4
7	$3.9	20%	$ .8
	5.1	50	2.6
	5.6	30	1.7
			$5.1
8	$3.9	20%	$ .8
	5.1	50	2.6

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	5.6	30	1.7
			$5.1
9	$3.9	20%	$ .8
	5.0	50	2.5
	5.5	30	1.7
			$5.0
10	$4.9	20%	$1.0
	6.0	50	3.0
	6.5	30	2.0
			$6.0

A14. The following table shows the computation of the present value of the expected cash flows; that is, the sum of the present values of the expected cash flows by year, which are calculated by discounting those cash flows at a risk-free rate. As shown, the expected present value is $42.3 million. In accordance with paragraph 7, the entity would recognize an impairment loss of $5.7 million ($48 million less $42.3 million).

Year	**Expected Cash Flows**	**Risk-Free Rate of Interest**	**Present Value**	**Expected Present Value**
		(in $ millions)		
1	$6.4	5.0%	$6.1	
2	6.4	5.1	5.8	
3	5.8	5.2	5.0	
4	5.8	5.4	4.7	
5	5.4	5.6	4.1	
6	5.4	5.8	3.9	
7	5.1	6.0	3.4	
8	5.1	6.2	3.2	

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9	5.0	6.4	2.9	
10	6.0	6.6	3.2	
				$42.3

Examples 5–7—Plan-of-Sale Criterion 30(b)

A15. To qualify for classification as held for sale, a long-lived asset (disposal group) must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (disposal groups) (paragraph 30(b)). A long-lived asset (disposal group) is available for immediate sale if an entity currently has the intent and ability to transfer the asset (disposal group) to a buyer in its present condition. Examples 5–7 illustrate situations in which the criterion in paragraph 30(b) would or would not be met.

Example 5

A16. An entity commits to a plan to sell its headquarters building and has initiated actions to locate a buyer.

a. The entity intends to transfer the building to a buyer after it vacates the building. The time necessary to vacate the building is usual and customary for sales of such assets. The criterion in paragraph 30(b) would be met at the plan commitment date.
b. The entity will continue to use the building until construction of a new headquarters building is completed. The entity does not intend to transfer the existing building to a buyer until after construction of the new building is completed (and it vacates the existing building). The delay in the timing of the transfer of the existing building imposed by the entity (seller) demonstrates that the building is not available for immediate sale. The criterion in paragraph 30(b) would not be met until construction of the new building is completed, even if a firm purchase commitment for the future transfer of the existing building is obtained earlier.

Example 6

A17. An entity commits to a plan to sell a manufacturing facility and has initiated actions to locate a buyer. At the plan commitment date, there is a backlog of uncompleted customer orders.

a. The entity intends to sell the manufacturing facility with its operations. Any uncompleted

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customer orders at the sale date would transfer to the buyer. The transfer of uncompleted customer orders at the sale date will not affect the timing of the transfer of the facility. The criterion in paragraph 30(b) would be met at the plan commitment date.

b. The entity intends to sell the manufacturing facility, but without its operations. The entity does not intend to transfer the facility to a buyer until after it ceases all operations of the facility and eliminates the backlog of uncompleted customer orders. The delay in the timing of the transfer of the facility imposed by the entity (seller) demonstrates that the facility is not available for immediate sale. The criterion in paragraph 30(b) would not be met until the operations of the facility cease, even if a firm purchase commitment for the future transfer of the facility is obtained earlier.

Example 7

A18. An entity acquires through foreclosure a real estate property that it intends to sell.

a. The entity does not intend to transfer the property to a buyer until after it completes renovations to increase its sales value. The delay in the timing of the transfer of the property imposed by the entity (seller) demonstrates that the property is not available for immediate sale. The criterion in paragraph 30(b) would not be met until the renovations are completed.
b. After the renovations are completed and the property is classified as held for sale but before a firm purchase commitment is obtained, the entity becomes aware of environmental damage requiring remediation. The entity still intends to sell the property. However, the entity does not have the ability to transfer the property to a buyer until after the remediation is completed. The delay in the timing of the transfer of the property imposed by others before a firm purchase commitment is obtained demonstrates that the property is not available for immediate sale. The criterion in paragraph 30(b) would not continue to be met. The property would be reclassified as held and used in accordance with paragraph 39.

Example 8—Plan-of-Sale Criterion 30(d)

A19. To qualify for classification as held for sale, the sale of a long-lived asset (disposal group) must be probable, and transfer of the asset (disposal group) must be expected to qualify for recognition as a completed sale, within one year (paragraph 30(d)). That criterion would not be met if, for example:

a. An entity that is a commercial leasing and finance company is holding for sale or lease equipment that has recently come off lease and the ultimate form of a future transaction (sale or lease) has not yet been determined.
b. An entity commits to a plan to "sell" a property that is in use, and the transfer of the property will be accounted for as a sale-leaseback through which the seller-lessee will retain

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more than a minor portion of the use of the property. The property would continue to be classified as held and used and paragraphs 7–26 would apply.[30]

Examples 9–11—Exceptions to Plan-of-Sale Criterion 30(d)

A20. An exception to the one-year requirement in paragraph 30(d) applies in limited situations in which the period required to complete the sale of a long-lived asset (disposal group) will be (or has been) extended by events or circumstances beyond an entity's control and certain conditions are met (paragraph 31). Examples 9–11 illustrate those situations.

Example 9

A21. An entity in the utility industry commits to a plan to sell a disposal group that represents a significant portion of its regulated operations. The sale will require regulatory approval, which could extend the period required to complete the sale beyond one year. Actions necessary to obtain that approval cannot be initiated until after a buyer is known and a firm purchase commitment is obtained. However, a firm purchase commitment is probable within one year. In that situation, the conditions in paragraph 31(a) for an exception to the one-year requirement in paragraph 30(d) would be met.

Example 10

A22. An entity commits to a plan to sell a manufacturing facility in its present condition and classifies the facility as held for sale at that date. After a firm purchase commitment is obtained, the buyer's inspection of the property identifies environmental damage not previously known to exist. The entity is required by the buyer to remediate the damage, which will extend the period required to complete the sale beyond one year. However, the entity has initiated actions to remediate the damage, and satisfactory remediation of the damage is probable. In that situation, the conditions in paragraph 31(b) for an exception to the one-year requirement in paragraph 30(d) would be met.

Example 11

A23. An entity commits to a plan to sell a long-lived asset and classifies the asset as held for sale at that date.

a. During the initial one-year period, the market conditions that existed at the date the asset was classified initially as held for sale deteriorate and, as a result, the asset is not sold by the end of that period. During that period, the entity actively solicited but did not receive any reasonable offers to purchase the asset and, in response, reduced the price. The asset continues to be actively marketed at a price that is reasonable given the change in market

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conditions, and the criteria in paragraph 30 are met. In that situation, the conditions in paragraph 31(c) for an exception to the one-year requirement in paragraph 30(d) would be met. At the end of the initial one-year period, the asset would continue to be classified as held for sale.

b. During the following one-year period, market conditions deteriorate further, and the asset is not sold by the end of that period. The entity believes that the market conditions will improve and has not further reduced the price of the asset. The asset continues to be held for sale, but at a price in excess of its current fair value. In that situation, the absence of a price reduction demonstrates that the asset is not available for immediate sale as required by the criterion in paragraph 30(b). In addition, the criterion in paragraph 30(e) requires that an asset be marketed at a price that is reasonable in relation to its current fair value. Therefore, the conditions in paragraph 31(c) for an exception to the one-year requirement in paragraph 30(d) would not be met. The asset would be reclassified as held and used in accordance with paragraph 38.

Examples 12–15—Reporting Discontinued Operations

A24. 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 if (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 (paragraph 42). Examples 12–15 illustrate disposal activities that do or do not qualify for reporting as discontinued operations.

Example 12

A25. An entity that manufactures and sells consumer products has several product groups, each with different product lines and brands. For that entity, a product group is the lowest level at which the operations and cash flows can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity. Therefore, each product group is a component of the entity.

A26. The entity has experienced losses associated with certain brands in its beauty care products group.

a. The entity decides to exit the beauty care business and commits to a plan to sell the product group with its operations. The product group is classified as held for sale at that date. The operations and cash flows of the product group will be eliminated from the ongoing operations of the entity as a result of the sale transaction, and the entity will not have any continuing involvement in the operations of the product group after it is sold. In that

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situation, the conditions in paragraph 42 for reporting in discontinued operations the operations of the product group while it is classified as held for sale would be met.

b. The entity decides to remain in the beauty care business but will discontinue the brands with which the losses are associated. Because the brands are part of a larger cash-flow-generating product group and, in the aggregate, do not represent a group that on its own is a component of the entity, the conditions in paragraph 42 for reporting in discontinued operations the losses associated with the brands that are discontinued would not be met.

Example 13

A27. An entity that is a franchiser in the quick-service restaurant business also operates company-owned restaurants. For that entity, an individual company-owned restaurant is the lowest level at which the operations and cash flows can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity. Therefore, each company-owned restaurant is a component of the entity.

a. The entity has experienced losses on its company-owned restaurants in one region. The entity decides to exit the quick-service restaurant business in that region and commits to a plan to sell the restaurants in that region. The restaurants are classified as held for sale at that date. The operations and cash flows of the restaurants in that region will be eliminated from the ongoing operations of the entity as a result of the sale transaction, and the entity will not have any continuing involvement in the operations of the restaurants after they are sold. In that situation, the conditions in paragraph 42 for reporting in discontinued operations the operations of the restaurants while they are classified as held for sale would be met.

b. Based on its evaluation of the ownership mix of its system-wide restaurants in certain markets, the entity commits to a plan to sell its company-owned restaurants in one region to an existing franchisee. The restaurants are classified as held for sale at that date. Although each company-owned restaurant, on its own, is a component of the entity, through the franchise agreement, the entity will (1) receive franchise fees determined, in part, based on the future revenues of the restaurants and (2) have significant continuing involvement in the operations of the restaurants after they are sold. In that situation, the conditions in paragraph 42 for reporting in discontinued operations the operations of the restaurants would not be met.

Example 14

A28. An entity that manufactures sporting goods has a bicycle division that designs, manufactures, markets, and distributes bicycles. For that entity, the bicycle division is the lowest level at which the operations and cash flows can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity. Therefore, the bicycle division is a

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component of the entity.

A29. The entity has experienced losses in its bicycle division resulting from an increase in manufacturing costs (principally labor costs).

a. The entity decides to exit the bicycle business and commits to a plan to sell the division with its operations. The bicycle division is classified as held for sale at that date. The operations and cash flows of the division will be eliminated from the ongoing operations of the entity as a result of the sale transaction, and the entity will not have any continuing involvement in the operations of the division after it is sold. In that situation, the conditions in paragraph 42 for reporting in discontinued operations the operations of the division while it is classified as held for sale would be met.
b. The entity decides to remain in the bicycle business but will outsource the manufacturing operations and commits to a plan to sell the related manufacturing facility. The facility is classified as held for sale at that date. Because the manufacturing facility is part of a larger cash-flow-generating group (the bicycle division), and on its own is not a component of the entity, the conditions in paragraph 42 for reporting in discontinued operations the operations (losses) of the manufacturing facility would not be met. (Those conditions also would not be met if the manufacturing facility on its own was a component of the entity because the decision to outsource the manufacturing operations of the division will not eliminate the operations and cash flows of the division [and its bicycle business] from the ongoing operations of the entity.)

Example 15

A30. An entity owns and operates retail stores that sell household goods. For that entity, each store is the lowest level at which the operations and cash flows can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity. Therefore, each store is a component of the entity.

A31. To expand its retail store operations in one region, the entity decides to close two of its retail stores and open a new "superstore" in that region. The new superstore will continue to sell the household goods previously sold through the two retail stores as well as other related products not previously sold. Although each retail store on its own is a component of the entity, the operations and cash flows from the sale of household goods previously sold through the two retail stores in that region will not be eliminated from the ongoing operations of the entity. In that situation, the conditions in paragraph 42 for reporting in discontinued operations the operations of the stores would not be met.

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Appendix B

BACKGROUND INFORMATION AND BASIS FOR CONCLUSIONS

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Appendix B: BACKGROUND INFORMATION AND BASIS FOR CONCLUSIONS

Introduction

B1. This appendix summarizes considerations that Board members deemed significant in reaching the conclusions in this Statement. It includes the reasons for accepting certain approaches and rejecting others. Individual Board members gave greater weight to some factors than to others. This appendix also summarizes the considerations that Board members deemed significant in reaching the conclusions in FASB Statement No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of,* that are still relevant.

Background

B2. Statement 121, which was issued in 1995, established accounting standards for the impairment of long-lived assets to be held and used, including certain identifiable intangibles and goodwill related to those assets. It also established accounting standards for long-lived assets to be disposed of, including certain identifiable intangibles, that were not covered by APB Opinion No. 30, *Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions*. Opinion 30 established, among other things, accounting and reporting standards for segments of a business to be disposed of. Paragraph 13 of Opinion 30 defined a segment of a business as "a component of an entity whose activities represent a separate major line of business or class of customer."

B3. After the issuance of Statement 121, significant differences existed in the accounting for long-lived assets to be disposed of covered by that Statement and by Opinion 30. The principal differences related to measurement and presentation.

B4. Under Statement 121, a long-lived asset classified as held for disposal was measured at the lower of its carrying amount or fair value less cost to sell, which excludes expected future operating losses that marketplace participants would not similarly consider in their estimates of the fair value less cost to sell of a long-lived asset classified as held for disposal. The gain or loss recognized on the disposal and any related results of operations were reported in continuing operations and separately disclosed in the notes to the financial statements.

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B5. Under Opinion 30, a segment of a business to be disposed of was measured at the lower of its carrying amount or net realizable value, adjusted for expected future operating losses of the segment held for disposal. The accrual of future operating losses as previously required under Opinion 30 generally is inappropriate under the Board's conceptual framework, which was developed after the issuance of Opinion 30. The gain or loss recognized on the disposal and the related results of operations were reported in discontinued operations, separately from continuing operations. Under other accounting pronouncements, the measurement but not reporting requirements of Opinion 30 were extended to certain other disposal transactions.

B6. In Statement 121, the Board acknowledged that inconsistency in accounting for long-lived assets to be disposed of. However, at that time, the Board decided not to expand the scope of that Statement to reconsider the requirements of Opinion 30.

B7. Soon after the issuance of Statement 121, the Emerging Issues Task Force (EITF) and others identified significant issues related to the implementation of that Statement. They asked the Board to address those issues, including:

a. How to apply the provisions for long-lived assets to be held and used to a long-lived asset that an entity expects to sell or otherwise dispose of if the entity has not yet committed to a plan to sell or otherwise dispose of the asset
b. How to determine an "indicated impairment of value" of a long-lived asset to be exchanged for a similar productive long-lived asset or to be distributed to owners
c. What criteria must be met to classify a long-lived asset as held for sale and how to account for the asset if those criteria are met after the balance sheet date but before issuance of the financial statements
d. How to account for a long-lived asset classified as held for sale if the plan to sell the asset changes
e. How to display in the income statement the results of operations while a long-lived asset or a group of long-lived assets with separately identifiable operations is classified as held for sale
f. How to display in the statement of financial position a long-lived asset or a group of long-lived assets and liabilities classified as held for sale.

B8. In August 1996, the Board added this project to its agenda to (a) develop a single accounting model, based on the framework established in Statement 121, for long-lived assets to be disposed of by sale and (b) address significant implementation issues.

B9. In June 2000, the Board issued an Exposure Draft of a proposed Statement, *Accounting for the Impairment or Disposal of Long-Lived Assets and for Obligations Associated with Disposal Activities*. The Board received comment letters from 53 respondents to the Exposure Draft. In January 2001, the Board held a public roundtable meeting with some of those respondents to discuss significant issues raised in comment letters. The Board considered respondents' comments during its redeliberations of the issues addressed by the Exposure Draft in public

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meetings in 2001.

Scope

B10. Except as discussed in paragraphs B11–B14, this Statement applies to recognized long-lived assets to be held and used or to be disposed of. If a long-lived asset is part of a group that includes other assets and liabilities not covered by this Statement, this Statement applies to its asset group or disposal group, as discussed in paragraph 4 of this Statement.

B11. Long-lived assets excluded from the scope of Statement 121 also are excluded from the scope of this Statement. The Board concluded that the objectives of this project could be achieved without reconsidering the accounting for the impairment or disposal of those long-lived assets. Accordingly, this Statement does not apply to (a) financial assets, (b) long-lived assets for which the accounting is prescribed in other broadly applicable accounting pronouncements (such as deferred tax assets), and (c) long-lived assets for which the accounting is prescribed in accounting pronouncements that apply to certain specialized industries (including the record and music, motion picture, broadcasting, software, and insurance industries).

B12. The scope of Statement 121 included goodwill related to an asset group but not goodwill related to a disposal group. Goodwill not covered by Statement 121 was covered by APB Opinion No. 17, *Intangible Assets*. The Exposure Draft would have included in its scope goodwill related to an asset group, and would have amended Opinion 17 to also include in its scope goodwill related to a disposal group. However, after issuance of the Exposure Draft, the Board decided to reconsider the accounting for goodwill and intangible assets in its project on accounting for business combinations. In that project, the Board decided that goodwill and certain other intangible assets should no longer be amortized and should be tested for impairment in a manner different from how the long-lived assets covered by this Statement are tested for impairment. FASB Statement No. 142, *Goodwill and Other Intangible Assets,* addresses the accounting for the impairment of those assets. It also addresses the allocation of goodwill to a disposal group that constitutes a business. Accordingly, this Statement does not apply to goodwill or to intangible assets not being amortized.

B13. Statement 121 did not address the accounting for obligations associated with the disposal of a long-lived asset (disposal group) or for the results of operations during the holding period of the asset (disposal group). Instead, Statement 121 referred to EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." Issue 94-3 provides guidance on recognition of liabilities for costs associated with restructuring and related disposal activities, including certain employee termination benefits and lease termination costs. During its deliberations of the Exposure Draft, the Board noted that liabilities are recognized under Issue 94-3 even though some of those items might not meet the definition of a liability set forth in the Board's conceptual framework. Because the types of costs covered by Issue 94-3 often are

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associated with the disposal of long-lived assets, the Board decided to reconsider the guidance in Issue 94-3 and include obligations associated with a disposal activity in the scope of this project.

B14. The Exposure Draft proposed significant changes to the guidance in Issue 94-3. Many respondents to the Exposure Draft disagreed with those proposed changes. Some of those respondents noted potential inconsistencies between the accounting requirements proposed in the Exposure Draft and the accounting requirements of other existing accounting pronouncements. Other respondents said that the Board should not reconsider the guidance in Issue 94-3 until after it undertakes a full conceptual reconsideration of all liabilities. Yet other respondents said that the Board should not reconsider that guidance at all, noting that SEC Staff Accounting Bulletin No. 100, *Restructuring and Impairment Charges,* now provides additional guidance for applying Issue 94-3. To avoid delaying the issuance of guidance on the accounting for the impairment or disposal of long-lived assets to address those issues, the Board decided to remove obligations associated with a disposal activity from the scope of this Statement. The Board plans to redeliberate those issues addressed by the Exposure Draft in a separate project.

Long-Lived Assets to Be Held and Used

Recognition of an Impairment Loss

B15. This Statement retains the requirement of Statement 121 to recognize an impairment loss only if the carrying amount of a long-lived asset (asset group) is not recoverable from its undiscounted cash flows and exceeds its fair value. In Statement 121, the Board decided for practical reasons to require an undiscounted cash flows recoverability test. In reaching that decision, the Board considered but rejected alternative criteria for recognition of an impairment loss. Specifically, the Board considered (a) an economic (fair value) criterion, (b) a permanence criterion, and (c) a probability criterion. Those criteria were discussed in paragraphs 60-62 of Statement 121:

> The economic criterion calls for loss recognition whenever the carrying amount of an asset exceeds the asset's fair value. It is an approach that would require continuous evaluation for impairment of long-lived assets similar to the ongoing lower-of-cost-or-market measurement of inventory. The economic criterion is based on the measurement of the asset. Using the same measure for recognition and measurement assures consistent outcomes for identical fact situations. However, the economic criterion presupposes that a fair value is available for every asset on an ongoing basis. Otherwise, an event or change in circumstance would be needed to determine which assets needed to be measured and in which period. Some respondents to the Discussion Memorandum indicated that the results of a measurement should not be sufficient reason to trigger recognition of an impairment loss. They favored using either the permanence or probability criterion to avoid recognition of write-downs that might result from measurements reflecting only temporary market fluctuations.

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> The permanence criterion calls for loss recognition when the carrying amount of an asset exceeds the asset's fair value and the condition is judged to be permanent. Some respondents to the Discussion Memorandum indicated that a loss must be permanent rather than temporary before recognition should occur. In their view, a high hurdle for recognition of an impairment loss is necessary to prevent premature write-offs of productive assets. Others stated that requiring the impairment loss to be permanent makes the criterion too restrictive and virtually impossible to apply with any reliability. Still others noted that the permanence criterion is not practical to implement; in their view, requiring management to assess whether a loss is permanent goes beyond management's ability to apply judgment and becomes a requirement for management to predict future events with certainty.
>
> The probability criterion, initially presented in the Issues Paper, calls for loss recognition based on the approach taken in FASB Statement No. 5, *Accounting for Contingencies*. Using that approach, an impairment loss would be recognized when it is deemed probable that the carrying amount of an asset cannot be fully recovered. Some respondents to the Discussion Memorandum stated that assessing the probability that an impairment loss has occurred is preferable to other recognition alternatives because it is already required by Statement 5. Most respondents to the Discussion Memorandum supported the probability criterion because, in their view, it best provides for management judgment.

When to Test a Long-Lived Asset for Recoverability

B16. This Statement retains the requirement of Statement 121 to test a long-lived asset (asset group) for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. Paragraph 57 of Statement 121 discussed the basis for the Board's conclusion:

> The Board concluded . . . that management has the responsibility to consider whether an asset is impaired but that to test each asset each period would be too costly. Existing information and analyses developed for management review of the entity and its operations generally will be the principal evidence needed to determine when an impairment exists. Indicators of impairment, therefore, are useful examples of events or changes in circumstances that suggest that the recoverability of the carrying amount of an asset should be assessed.

B17. Statement 121 provided examples of such events or changes in circumstances. The Board decided to expand those examples, carried forward in paragraph 8 of this Statement, to also refer to a current expectation that a long-lived asset (asset group) will be disposed of significantly before the end of its previously estimated useful life (paragraph 8(f)). The Board reasoned that a current expectation that a long-lived asset (asset group) will be disposed of significantly before

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the end of its previously estimated useful life might indicate that the carrying amount of the asset (group) is not recoverable.

Estimates of Future Cash Flows Used to Test a Long-Lived Asset for Recoverability

B18. Statement 121 provided general guidance for developing estimates of future cash flows used to estimate the fair value of a long-lived asset (asset group) in the absence of an observable market price. However, it did not specify whether that guidance also should apply for developing estimates of future cash flows used to test a long-lived asset (asset group) for recoverability. Consequently, in implementing Statement 121, questions emerged about how to develop those estimates.

B19. In considering that issue, the Board noted that in contrast to an objective of measuring fair value, the objective of the undiscounted cash flows recoverability test is to assess the recoverability of a long-lived asset (asset group) in the context of a particular entity. The Board decided that because the objectives of measuring fair value and testing a long-lived asset (asset group) for recoverability are different, this Statement should provide guidance for developing estimates of future cash flows used to test for recoverability. The Board acknowledges that significant judgment is required in developing estimates of future cash flows. However, the Board believes that the level of guidance provided by this Statement is sufficient for meeting the objective of an undiscounted cash flows recoverability test.

B20. The guidance provided by this Statement focuses on (a) the cash flow estimation approach, (b) the cash flow estimation period, and (c) the types of asset-related expenditures that should be considered in developing estimates of future cash flows.

Cash flow estimation approach

B21. The guidance in Statement 121 permitted the use of either a probability-weighted approach or a best-estimate approach in developing estimates of future cash flows used to test for recoverability. Both of those cash flow estimation approaches are discussed in FASB Concepts Statement No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements,* issued in February 2000. A probability-weighted approach refers to the sum of probability-weighted amounts in a range of possible estimated amounts. A best-estimate approach refers to the single most-likely amount in a range of possible estimated amounts. During its deliberations leading to the Exposure Draft, the Board reasoned that because the probability-weighted approach discussed in Concepts Statement 7 incorporates uncertainty in estimates of future cash flows, it would provide a more complete and disciplined estimate of future cash flows than would a best-estimate approach. Therefore, the Exposure Draft would have required, rather than permitted, the use of that approach in developing estimates of future cash flows used to test for recoverability.

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B22. Several respondents to the Exposure Draft disagreed with that proposed requirement, stating that, for many entities, a probability-weighted approach would not be practical or cost-beneficial in developing estimates of future cash flows used to test for recoverability. The principal concern expressed by respondents was that in many cases, reliable information about the likelihood of possible outcomes would not be available. They said that the Board should permit the use of either a best-estimate approach or a probability-weighted approach in developing those estimates, as under Statement 121. During its redeliberations of the Exposure Draft, the Board decided not to require the probability-weighted approach in Concepts Statement 7 in developing estimates of future cash flows used to test for recoverability. The Board noted that Concepts Statement 7 expresses a preference for a probability-weighted approach, but that preference is discussed in the context of developing estimates of future cash flows that provide the basis for an accounting measurement (fair value). The Board concluded that because estimates of future cash flows used to test for recoverability, in and of themselves, do not provide the basis for an accounting measurement, the preference for a probability-weighted approach in Concepts Statement 7 need not be extended to those estimates. However, the Board agreed that in situations in which alternative courses of action to recover the carrying amount of a long-lived asset (asset group) are under consideration or in which a range is estimated for the amount of possible future cash flows associated with the likely course of action, a probability-weighted approach may be useful in considering the likelihood of those possible outcomes.

Cash flow estimation period

B23. Statement 121 did not specify the cash flow estimation period for estimates of future cash flows used to test for recoverability. The Board decided that the cash flow estimation period should correspond to the period that a long-lived asset (asset group) is expected to provide service potential to the entity. Accordingly, the cash flow estimation period for a long-lived asset is based on its remaining useful life to the entity. If long-lived assets having different remaining useful lives are grouped, the cash flow estimation period for the asset group is based on the remaining useful life of the primary asset of the group to the entity. The definition of a primary asset proposed in the Exposure Draft limited that asset to a tangible long-lived asset. Several respondents to the Exposure Draft agreed with the primary asset approach for determining the cash flow estimation period for an asset group. However, many said that because intangible assets often are more significant than tangible assets, the Board should expand the definition of a primary asset to include those assets.

B24. The Board initially decided to limit the primary asset to a tangible long-lived asset principally to prohibit an entity from arbitrarily designating as the primary asset goodwill associated with the group. The Board's decision was influenced by the then-existing requirement to amortize goodwill over a period of up to 40 years. However, in view of its subsequent decision in Statement 142 that goodwill should no longer be amortized, the Board decided to broaden the definition of a primary asset to include either a recognized tangible asset being depreciated or an intangible asset being amortized. The Board concluded that because

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there needs to be some boundaries on the cash flow estimation period for an asset group, indefinite-lived assets, such as land and intangible assets not being amortized, are not eligible to be primary assets. The Board affirmed its conclusion in the Exposure Draft that, for many asset groups, the primary asset will be readily identifiable and that the remaining useful life of that asset to the entity is a reasonable basis for consistently determining the cash flow estimation period for an asset group.

B25. During its deliberations leading to the Exposure Draft, the Board considered but rejected alternative approaches for determining the cash flow estimation period for an asset group. One approach would have limited the estimation period to the shorter of (a) the remaining useful life of the primary asset of the group or (b) 10 years and would have assumed the sale of the group at the end of that shortened period (limited estimation approach). The Board observed that because a limited estimation approach would include estimated disposal values (fair values) in estimates of future cash flows used to test for recoverability, the effect of that approach would be to discount some portion of those cash flows. The Board concluded that a limited estimation approach would be inconsistent with the requirement of this Statement to recognize an impairment loss only if the carrying amount of a long-lived asset (asset group) is not recoverable from its undiscounted future cash flows.

B26. Another approach for determining the cash flow estimation period for an asset group would have used the average of the remaining useful lives of the long-lived assets of the group, weighted based on the relative carrying amounts of those assets (weighted-average approach). The Board acknowledged that for some asset groups, a weighted-average approach could avoid difficulties in identifying the primary asset, but it concluded that for many entities, that approach could be unduly burdensome and result in little, if any, incremental benefit. Some respondents to the Exposure Draft suggested that the Board reconsider a weighted-average approach for entities that use a group composite depreciation method. However, the Board noted that the cost-capitalization approach proposed in the Exposure Draft of a proposed AICPA Statement of Position, *Accounting for Certain Costs and Activities Related to Property, Plant, and Equipment,* issued in June 2001, would effectively eliminate that depreciation method. The Board also believes that the approach for determining the cash flow estimation period should be the same for all entities with long-lived assets covered by this Statement.

Asset-related expenditures for a long-lived asset in use

B27. Statement 121 did not identify the types of asset-related expenditures that should be considered in estimates of future cash flows used to test a long-lived asset (asset group) for recoverability. During its deliberations leading to the Exposure Draft, the Board observed that, as a result, an entity could avoid the write-down of a long-lived asset that is in use by including in those estimates the cash flows (cash outflows and cash inflows) associated with all possible improvements that would be capitalized in future periods. In that case, the recoverability of the long-lived asset (asset group) would be assessed based on its expected future service potential ("as improved"), rather than on its existing service potential ("as is").

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B28. The Board decided that a long-lived asset (asset group) that is in use, including a long-lived asset (asset group) for which development is substantially complete, should be tested for recoverability based on its existing service potential at the date of that test. Therefore, estimates of future cash flows used in that test should exclude the cash flows associated with asset-related expenditures that would enhance the existing service potential of a long-lived asset (asset group) that is in use.

B29. The Board decided that estimates of future cash flows used to test for recoverability should include cash flows (including estimated salvage values) associated with asset-related expenditures that replace (a) component parts of a long-lived asset or (b) component assets (other than the primary asset) of an asset group, whether those expenditures would be recognized as an expense or capitalized in future periods. The Board considered an alternative approach that would have excluded the cash flows associated with those expenditures. However, the Board observed that because an asset group could not continue to be used without replacing the component assets of the group, there would be an assumption that the asset of the group would be sold at the end of the remaining useful life of the primary asset. By including the estimated disposal values of those assets (fair values) in estimates of future cash flows used to test for recoverability, the effect of that approach would be to discount some portion of the cash flows. As discussed in paragraph B25, such an approach would be inconsistent with the requirement of this Statement to recognize an impairment loss only if the carrying amount of a long-lived asset (asset group) is not recoverable from its undiscounted future cash flows.

B30. Some respondents to the Exposure Draft noted that if an entity has a plan to improve a long-lived asset (asset group) that is in use, the entity could be required to write down the carrying amount of the asset (asset group) even if it would be recoverable after it is improved. They suggested that the Board permit an exception to the existing service potential requirement for a long-lived asset (asset group) that is in use in that situation. During its redeliberations of the Exposure Draft, the Board decided not to make that exception for the reason discussed in paragraph B27. However, the Board observed that in measuring fair value, if marketplace participants would assume the same improvements to the asset as the entity, the estimates of future cash flows used to measure fair value would include the cash flows (cash outflows and cash inflows) associated with those improvements. Consequently, it is possible that although the carrying amount of the asset (asset group) is not recoverable in its present condition, the fair value of the asset (asset group) could exceed its carrying amount and no impairment would exist.

Asset-related expenditures for a long-lived asset under development

B31. The Board observed that in contrast to a long-lived asset (asset group) that is in use, a long-lived asset (asset group) that is under development will not provide service potential until development is substantially complete. The Board decided that such an asset (asset group) should be tested for recoverability based on its expected service potential. Therefore, estimates of future cash flows used in that test should include the cash flows (cash outflows and cash

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inflows) associated with all future asset-related expenditures necessary to develop the asset (asset group), whether those expenditures would be recognized as an expense or capitalized in future periods.

B32. In Statement 121, the Board decided that estimates of future cash flows used to test a long-lived asset (asset group) for recoverability should exclude all future interest payments, whether those payments would be recognized as an expense or capitalized in future periods. In this Statement, the Board reconsidered that decision, noting that for a long-lived asset (asset group) that is under development, interest payments during the development period would be capitalized in accordance with paragraph 6 of FASB Statement No. 34, *Capitalization of Interest Cost,* which states:

> The historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use. If an asset requires a period of time in which to carry out the activities necessary to bring it to that condition and location, the interest cost incurred during that period as a result of expenditures for the asset is a part of the historical cost of acquiring the asset. [Footnote references omitted.]

The Board reasoned that for a long-lived asset (asset group) that is under development, there is no difference between interest payments and other asset-related expenditures that would be capitalized in future periods. Therefore, the Board decided that estimates of future cash flows used to test a long-lived asset (asset group) for recoverability should exclude only those interest payments that would be recognized as an expense when incurred.

B33. Some respondents to the Exposure Draft asked the Board to clarify how the service potential requirements of this Statement would apply if a long-lived asset that is under development is part of an asset group that includes other assets that are in use. This Statement clarifies that the estimates of future cash flows used to test such an asset group for recoverability should include the cash flows (cash outflows and cash inflows) associated with (a) future asset-related expenditures necessary to complete the asset that is under development and (b) future asset-related expenditures necessary to maintain the existing service potential of the other assets that are in use.

Measurement of an Impairment Loss

B34. This Statement retains the requirement of Statement 121 to measure an impairment loss for a long-lived asset, including an asset that is subject to nonrecourse debt, as the amount by which the carrying amount of the asset (asset group) exceeds its fair value. Paragraphs 69–72 and 103 and 104 of Statement 121 discussed the basis for the Board's conclusion:

> The Board concluded that a decision to continue to operate rather than sell an impaired asset is economically similar to a decision to invest in that asset and,

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therefore, the impaired asset should be measured at its fair value. The amount of the impairment loss should be the amount by which the carrying amount of the impaired asset exceeds the fair value of the asset. That fair value then becomes the asset's new cost basis.

When an entity determines that expected future cash flows from using an asset will not result in the recovery of the asset's carrying amount, it must decide whether to sell the asset and use the proceeds for an alternative purpose or to continue to use the impaired asset in its operations. The decision presumably is based on a comparison of expected future cash flows from those alternative courses of action and is essentially a capital investment decision. In either alternative, proceeds from the sale of the impaired asset are considered in the capital investment decision. Consequently, a decision to continue to use the impaired asset is equivalent to a new asset purchase decision, and a new basis of fair value is appropriate.

. . . The Board . . . concluded that the fair value of an impaired asset is the best measure of the cost of continuing to use that asset because it is consistent with management's decision process. Presumably, no entity would decide to continue to use an asset unless that alternative was expected to produce more in terms of expected future cash flows or service potential than the alternative of selling it and reinvesting the proceeds. The Board also believes that using fair value to measure the amount of an impairment loss is not a departure from the historical cost principle. Rather, it is a consistent application of principles practiced elsewhere in the current system of accounting whenever a cost basis for a newly acquired asset must be determined.

The Board believes that fair value is an easily understood notion. It is the amount at which an asset could be bought or sold in a current transaction between willing parties. The fair value measure is basic to economic theory and is grounded in the reality of the marketplace. Fair value estimates are readily available in published form for many assets, especially machinery and equipment. For some assets, multiple, on-line database services provide up-to-date market price information. Estimates of fair value also are subject to periodic verification whenever assets are exchanged in transactions between willing parties.

The Board considered requests for a limited exception to the fair value measurement for impaired long-lived assets that are subject to nonrecourse debt. Some believe that the nonrecourse provision is effectively a put option for which the borrower has paid a premium. They believe that the impairment loss on an asset subject entirely to nonrecourse debt should be limited to the loss that would occur if the asset were put back to the lender.

The Board decided not to provide an exception for assets subject to nonrecourse debt. The recognition of an impairment loss and the recognition of a gain on the extinguishment of debt are separate events, and each event should be recognized in the period in which it occurs. The Board believes that the recognition of an impairment loss should be based on the measurement of the

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asset at its fair value and that the existence of nonrecourse debt should not influence that measurement.

Alternative Measures of an Impairment Loss

B35. In Statement 121, the Board considered but rejected measures other than fair value for measuring an impairment loss that could have been achieved within the historical cost framework. Specifically, the Board considered (a) a recoverable cost measure, (b) a recoverable cost including interest measure, and (c) different measures for different impairment losses.

B36. Paragraphs 77–81 of Statement 121 discussed a recoverable cost measure:

> Recoverable cost is measured as the sum of the undiscounted future cash flows expected to be generated over the life of an asset. For example, if an asset has a carrying amount of $1,000,000, a remaining useful life of 5 years, and expected future cash flows over the 5 years of $180,000 per year, the recoverable cost would be $900,000 (5 × $180,000), and the impairment loss would be $100,000 ($1,000,000 – $900,000).
>
> The Board did not adopt recoverable cost as the measure of an impairment loss. Proponents of the recoverable cost measure believe that impairment is the result of the inability to recover the carrying amount of an asset. They do not view the decision to retain an impaired asset as an investment decision; rather, they view the recognition of an impairment loss as an adjustment to the historical cost of the asset. They contend that recoverable cost measured by the sum of the undiscounted expected future cash flows is the appropriate carrying amount for an impaired asset and the amount on which the impairment loss should be determined.
>
> Proponents of the recoverable cost measure do not believe that the fair value of an asset is a relevant measure unless a transaction or other event justifies a new basis for the asset at fair value. They do not view impairment to be such an event.
>
> Some proponents of the recoverable cost measure assert that measuring an impaired asset at either fair value or a discounted present value results in an inappropriate understatement of net income in the period of the impairment and an overstatement of net income in subsequent periods. The Board did not agree with that view. Board members noted that measuring an impaired asset at recoverable cost could result in reported losses in future periods if the entity had incurred debt directly associated with the asset.
>
> Proponents of the recoverable cost measure view interest cost as a period cost that should not be included as part of an impairment loss regardless of whether the interest is an accrual of actual debt costs or the result of discounting expected future cash flows using a debt rate.

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B37. Paragraphs 82–85 of Statement 121 discussed a recoverable cost including interest measure:

> Recoverable cost including interest generally is measured as either (a) the sum of the undiscounted expected future cash flows including interest costs on actual debt or (b) the present value of expected future cash flows discounted at some annual rate such as a debt rate. For example, if an asset has a carrying value of $1,000,000, a remaining useful life of 5 years, expected future cash flows (excluding interest) over the 5 years of $180,000 per year, and a debt rate of 6 percent, recoverable cost including interest would be $758,225 (4.21236 × $180,000), and the impairment loss would be $241,775 ($1,000,000 – $758,225).
>
> The Board did not adopt recoverable cost including interest as an appropriate measure of an impairment loss. Proponents of the recoverable cost including interest measure agree that the time value of money should be considered in the measure, but they view the time value of money as an element of cost recovery rather than as an element of fair value. Proponents believe that the measurement objective for an impaired asset should be recoverable cost and not fair value. However, they believe that interest should be included as a carrying cost in determining the recoverable cost. To them, the objective is to recognize the costs (including the time value of money) that are not recoverable as an impairment loss and to measure an impaired asset at the costs that are recoverable.
>
> Because of the difficulties in attempting to associate actual debt with individual assets, proponents of the recoverable cost including interest measure believe that the present value of expected future cash flows using a debt rate such as an incremental borrowing rate is a practical means of achieving their measurement objective. They recognize that an entity that has no debt may be required to discount expected future cash flows. They believe that the initial investment decision would have included consideration of the debt or equity cost of funds.
>
> The Board believes that use of the recoverable cost including interest measure would result in different carrying amounts for essentially the same impaired assets because they are owned by different entities that have different debt capacities. The Board does not believe that discounting expected future cash flows using a debt rate is an appropriate measure for determining the value of those assets.

B38. Paragraph 86 of Statement 121 discussed different measures for different impairment losses:

> The Board also considered but did not adopt an alternative approach that would require different measures for different impairments. At one extreme, an asset might be impaired because depreciation assumptions were not adjusted appropriately. At the other extreme, an asset might be impaired because of a major change in its use. Some believe that the first situation is similar to a

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> depreciation "catch-up" adjustment and that an undiscounted measure should be used. They believe that the second situation is similar to a new investment in an asset with the same intended use and that a fair value measure should be used. The Board was unable to develop a workable distinction between the first and second situations that would support the use of different measures.

Fair Value

B39. This Statement retains the hierarchy in Statement 121 for measuring fair value. Because quoted market prices in active markets are the best evidence of fair value, they should be used, if available. Otherwise, the estimate of fair value should be based on the best information available in the circumstances, including prices for similar assets (asset groups) and the results of using other valuation techniques.

B40. The Board acknowledges that in many instances, quoted market prices in active markets will not be available for the long-lived assets (asset groups) covered by this Statement. The Board concluded that for those long-lived assets (asset groups), a present value technique is often the best available valuation technique with which to estimate fair value. Paragraphs 39–54 of Concepts Statement 7, which are incorporated in Appendix E, discuss the use of two present value techniques—expected present value and traditional present value. During its deliberations leading to the Exposure Draft, the Board concluded that an expected present value technique is superior to a traditional present value technique, especially in situations in which the timing or amount of estimated future cash flows is uncertain. Because such situations often arise for the long-lived assets (asset groups) covered by this Statement, the Exposure Draft set forth the Board's expectation that when using a present value technique, most entities would use expected present value.

B41. Several respondents to the Exposure Draft suggested that the Board provide clearer guidance on whether and, if so, when entities are required to use an expected present value technique versus a traditional present value technique to minimize confusion and inconsistent application of this Statement. During its redeliberations of the Exposure Draft, the Board decided not to specify a requirement for either present value technique. The Board decided that preparers should determine the present value technique best suited to their specific circumstances based on the guidance in Concepts Statement 7. However, the Board noted that a traditional present value technique cannot accommodate uncertainties in the timing of future cash flows. Further, for nonfinancial assets, such as those covered by this Statement, paragraph 44 of Concepts Statement 7 explains:

> The traditional approach is useful for many measurements, especially those in which comparable assets and liabilities can be observed in the marketplace. However, the Board found that the traditional approach does not provide the tools needed to address some complex measurement problems, including the

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> measurement of nonfinancial assets and liabilities for which no market for the item or a comparable item exists. The traditional approach places most of the emphasis on selection of an interest rate. A proper search for "the rate commensurate with the risk" requires analysis of at least two items—one asset or liability that exists in the marketplace and has an observed interest rate and the asset or liability being measured. The appropriate rate of interest for the cash flows being measured must be inferred from the observable rate of interest in some other asset or liability and, to draw that inference, the characteristics of the cash flows must be similar to those of the asset being measured.

B42. In this Statement, the Board clarified that consistent with the objective of measuring fair value, assumptions that marketplace participants would use in their estimates of fair value should be incorporated in estimates of future cash flows whenever that information is available without undue cost and effort. The Exposure Draft provided examples of circumstances in which an entity's assumptions might differ from marketplace assumptions. During its redeliberations of the Exposure Draft, the Board decided that it was not necessary to include those examples in this Statement, noting that related guidance is provided in paragraphs 23 and 32 of Concepts Statement 7, which are incorporated in Appendix E.

B43. The Board recognizes that there may be practical problems in determining the fair value of certain types of long-lived assets (asset groups) covered by this Statement that do not have observable market prices. Because precise information about the relevant attributes of those assets (asset groups) seldom will be available, judgments, estimates, and projections will be required for estimating fair value. Although the objective of using a present value or other valuation technique is to determine fair value, the Board acknowledges that, in some circumstances, the only information available to estimate fair value without undue cost and effort will be the entity's estimates of future cash flows. Paragraph 38 of Concepts Statement 7 explains:

> As a practical matter, an entity that uses cash flows in accounting measurements often has little or no information about some or all of the assumptions that marketplace participants would use in assessing the fair value of an asset or a liability. In those situations, the entity must necessarily use the information that is available without undue cost and effort in developing cash flow estimates. The use of an entity's own assumptions about future cash flows is compatible with an estimate of fair value, as long as there are no contrary data indicating that marketplace participants would use different assumptions. If such data exist, the entity must adjust its assumptions to incorporate that market information.

Grouping Long-Lived Assets to Be Held and Used

B44. For purposes of recognition and measurement of an impairment loss, this Statement retains

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the requirement of Statement 121 to group a long-lived asset or assets with other assets and liabilities at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities. In Statement 121, the Board acknowledged that the primary issue underlying the grouping of long-lived assets is when, if ever, it is appropriate to offset unrealized losses on some assets by unrealized gains on other assets. However, the Board concluded that such offsetting is appropriate when a long-lived asset that is not an individual source of cash flows is part of a group of assets that are used together to generate joint cash flows. The Board affirmed that conclusion in this Statement. This Statement establishes that an asset group is the unit of accounting for a long-lived asset while it is classified as held and used.

B45. In Statement 121, the Board also acknowledged that grouping long-lived assets requires significant judgment. In that regard, the Board reviewed a series of cases that demonstrated the subjectivity of grouping issues. Paragraphs 96–98 of Statement 121 stated:

> Varying facts and circumstances introduced in the cases inevitably justified different groupings. Although most respondents to the Discussion Memorandum generally favored grouping at the lowest level for which there are identifiable cash flows for recognition and measurement of an impairment loss, determining that lowest level requires considerable judgment.
>
> The Board considered a case that illustrated the need for judgment in grouping assets for impairment. In that case, an entity operated a bus company that provided service under contract with a municipality that required minimum service on each of five separate routes. Assets devoted to serving each route and the cash flows from each route were discrete. One of the routes operated at a significant deficit that resulted in the inability to recover the carrying amounts of the dedicated assets. The Board concluded that the five bus routes would be an appropriate level at which to group assets to test for and measure impairment because the entity did not have the option to curtail any one bus route.
>
> The Board concluded that the grouping issue requires significant management judgment within certain parameters. Those parameters are that the assets should be grouped at the lowest level for which there are cash flows that are identifiable and that those cash flows should be largely independent of the cash flows of other groupings of assets.

B46. In this Statement, as in Statement 121, the Board acknowledges that in limited circumstances, an asset group will include all assets and liabilities of the entity. Paragraphs 99 and 100 of Statement 121 explained:

> Not-for-profit organizations that rely in part on contributions to maintain their assets may need to consider those contributions in determining the appropriate cash flows to compare with the carrying amount of an asset. Some respondents to the Exposure Draft stated that the recognition criteria in paragraph 6 would be problematic for many not-for-profit organizations because it may be difficult, if

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not impossible, for them to identify expected future cash flows with specific assets or asset groupings. In other cases, expected future cash flows can be identified with asset groups. However, if future unrestricted contributions to the organization as a whole are not considered, the sum of the expected future cash flows may be negative, or positive but less than the carrying amount of the asset. For example, the costs of administering a museum may exceed the admission fees charged, but the organization may fund the cash flow deficit with unrestricted contributions.

Other respondents indicated that similar difficulties would be experienced by business enterprises. For example, the cost of operating assets such as corporate headquarters or centralized research facilities may be funded by revenue-producing activities at lower levels of the enterprise. Accordingly, in limited circumstances, the lowest level of identifiable cash flows that are largely independent of other asset groups may be the entity level. The Board concluded that the recoverability test in paragraph 6 should be performed at the entity level if an asset does not have identifiable cash flows lower than the entity level. The cash flows used in the recoverability test should be reduced by the carrying amounts of the entity's other assets that are covered by this Statement to arrive at the cash flows expected to contribute to the recoverability of the asset being tested. Not-for-profit organizations should include unrestricted contributions to the organization as a whole that are a source of funds for the operation of the asset.

B47. Based on the Board's previous decisions discussed in paragraph 100 of Statement 121, the Exposure Draft would have required that estimates of future cash flows for an asset group be adjusted to exclude the portion of those cash flows necessary to recover the carrying amounts of the assets and liabilities of the group not covered by this Statement. However, during its redeliberations of the Exposure Draft, the Board decided to eliminate that requirement, noting that because the unit of accounting for a long-lived asset to be held and used is its asset group, such adjustments are unnecessary.

Goodwill

B48. In Statement 142, the Board decided that because goodwill should no longer be amortized, it should be tested for impairment in a manner different from how the long-lived assets covered by this Statement are tested for impairment. In developing the guidance in Statement 142, the Board decided that the reporting unit (as defined in that Statement) is the unit of measure for goodwill and that all goodwill should be tested for impairment at that level. The Board therefore decided to eliminate the requirement of Statement 121 to include goodwill in an asset group previously acquired in a business combination to be tested for impairment, which the Exposure Draft would have retained. The Board decided that goodwill should be included in such an asset group only if it is or includes a reporting unit. Goodwill should be excluded from such an asset

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group if it is only part of a reporting unit.

B49. During its redeliberations of the Exposure Draft, the Board considered the effect of excluding goodwill from an asset group that is only part of a reporting unit. The Board observed that although the carrying amount of the asset group would exclude goodwill, the estimates of future cash flows used to test the group for recoverability could include cash flows attributable to goodwill. However, the Board decided that those estimates of future cash flows should not be adjusted for the effect of excluding goodwill. The Board reasoned that because any adjustment likely would be arbitrary, adjusted estimates of future cash flows would not necessarily provide a better estimate of the cash flows expected to contribute to the recoverability of the group. Further, an additional requirement to determine a goodwill adjustment under this Statement would not be cost beneficial.

Allocation of an Impairment Loss

B50. Paragraph 12 of Statement 121 specified that "in instances where goodwill is identified with assets that are subject to an impairment loss, the carrying amount of the identified goodwill shall be eliminated before making any reduction of the carrying amounts of impaired long-lived assets and identifiable intangibles." However, it did not specify how the excess, if any, should be allocated to the other assets of the group. The Board observed that if long-lived assets having different depreciable lives are grouped, the method used to allocate the excess impairment loss, if any, to the assets of the group can affect the pattern of income recognition over the succeeding years. To improve the consistency and comparability of reported financial information over time and among entities, the Board decided that this Statement should specify an allocation method.

B51. The Board decided that because other accounting requirements prescribe the accounting for assets and liabilities not covered by this Statement that are included in an asset group, an impairment loss that is determined based on the carrying amount and fair value of an asset group should reduce only the carrying amounts of the long-lived assets of the group. Paragraph 14 of this Statement requires that an impairment loss be allocated to those long-lived assets on a pro rata basis using their relative carrying amounts, provided that the carrying amount of an individual long-lived asset of the group is not reduced to an amount less than its fair value whenever that fair value is determinable without undue cost and effort. The Board concluded that it would be inappropriate to reduce the carrying amount of a long-lived asset to an amount below its fair value. The Board believes that the allocation method for an impairment loss provides a consistent basis for adjusting the carrying amounts of the long-lived assets of an asset group.

Depreciation

B52. This Statement retains the requirement of Statement 121 to consider the need to review depreciation estimates and method for a long-lived asset in accordance with APB Opinion

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No. 20, *Accounting Changes,* if a long-lived asset is tested for recoverability. This Statement clarifies that any revision to the remaining useful life of a long-lived asset resulting from that review should be considered in developing estimates of future cash flows used to test for recoverability but that any change in the method of accounting for the asset should be made only after applying this Statement. In Statement 121, the Board decided not to expand the scope of that Statement to address depreciation issues. The Board affirmed its initial decision in Statement 121 and, therefore, this Statement does not prescribe the basis for revisions to depreciation estimates or method, or otherwise address depreciation issues.

Restoration of an Impairment Loss

B53. This Statement retains the prohibition in Statement 121 on the restoration of a previously recognized impairment loss. Paragraph 105 of Statement 121 discussed the basis for the Board's conclusion:

> The Board considered whether to prohibit or require restoration of previously recognized impairment losses. It decided that an impairment loss should result in a new cost basis for the impaired asset. That new cost basis puts the asset on an equal basis with other assets that are not impaired. In the Board's view, the new cost basis should not be adjusted subsequently other than as provided under the current accounting model for prospective changes in the depreciation estimates and method and for further impairment losses. Most respondents to the Exposure Draft agreed with the Board's decision that restoration should be prohibited.

Reporting and Disclosure

B54. Paragraph 25 of this Statement retains the requirements of Statement 121 for reporting an impairment loss recognized for a long-lived asset to be held and used. Paragraph 108 of Statement 121 discussed the basis for the Board's conclusion:

> The Board considered the alternative ways described in the Discussion Memorandum for reporting an impairment loss: reporting the loss as a component of continuing operations, reporting the loss as a special item outside continuing operations, or separate reporting of the loss without specifying the classification in the statement of operations. The Board concluded that an impairment loss should be reported as a component of income from continuing operations before income taxes for entities that present an income statement and in the statement of activities of a not-for-profit organization. If no impairment had occurred, an amount equal to the impairment loss would have been charged to operations over time through the allocation of depreciation or amortization. That depreciation or amortization charge would have been reported as part of continuing operations of a business enterprise or as an expense in the statement of activities of a not-for-profit organization. Further, an asset that is subject to a reduction in its

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> carrying amount due to an impairment loss will continue to be used in operations. The Board concluded that an impairment loss does not have characteristics that warrant special treatment, for instance, as an extraordinary item.

B55. Paragraph 26 of this Statement retains the disclosure requirements of Statement 121 relating to impairment losses. Paragraphs 109 and 94 of Statement 121 discussed the basis for the Board's conclusion:

> The Board believes that financial statements should include information on impairment losses that would be most useful to users. After considering responses to the Exposure Draft, the Board concluded that an entity that recognizes an impairment loss should describe the assets impaired and the facts and circumstances leading to the impairment; disclose the amount of the loss and how fair value was determined; disclose the caption in the income statement or the statement of activities in which the loss is aggregated unless that loss has been presented as a separate caption or reported parenthetically on the face of the statement; and, if applicable, disclose the business segment(s) affected. The Board decided not to require further disclosures, such as the assumptions used to estimate expected future cash flows and the discount rate used when fair value is estimated by discounting expected future cash flows.
>
> Several respondents to the Exposure Draft said that disclosure of the discount rate used to determine the present value of the estimated expected future cash flows should not be required. The Board decided that disclosure of the discount rate without disclosure of the other assumptions used in estimating expected future cash flows generally would not be meaningful to financial statement users. Therefore, this Statement does not require disclosure of the discount rate.

B56. A few respondents to the Exposure Draft suggested that the Board reconsider its decision in Statement 121 not to require disclosure of the discount rate and other assumptions used in measuring fair value. They said that such disclosures would provide useful information for evaluating impairment write-downs. However, the Board concluded that without access to management's cash flow projections and its methods of estimating those cash flows, the suggested disclosures would not necessarily be useful to users in evaluating impairment write-downs. The Board affirmed its initial conclusions in Statement 121 and, therefore, this Statement does not require disclosure of that information.

Early Warning Disclosures

B57. This Statement, like Statement 121, does not require early warning disclosures. Paragraphs 110 and 111 of Statement 121 discussed the basis for the Board's conclusion:

> In 1985, the AICPA established a task force to consider the need for improved disclosures about risks and uncertainties that affect companies and the manner in

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which they do business. In July 1987, the task force published *Report of the Task Force on Risks and Uncertainties,* which concluded that companies should make early warning disclosures in their financial statements. In December 1994, AcSEC issued AICPA Statement of Position 94-6, *Disclosure of Certain Significant Risks and Uncertainties*. That SOP requires entities to include in their financial statements disclosures about (a) the nature of operations, (b) the use of estimates in the preparation of financial statements, (c) certain significant estimates, and (d) current vulnerability due to certain concentrations.

The Board observed that early warning disclosures would be useful for certain potential impairments. However, most respondents to the Exposure Draft said that the Statement should not require early warning disclosures. The Board observed that SOP 94-6 uses essentially the same events or changes in circumstances as those in paragraph 5 of this Statement to illustrate when disclosures of certain significant estimates should be made for long-lived assets. Therefore, the Board concluded that it was not necessary for this Statement to require early warning disclosures.

Amendment to Statement 15

B58. This Statement carries forward the amendment made by Statement 121 to FASB Statement No. 15, *Accounting by Debtors and Creditors for Troubled Debt Restructurings,* discussed in paragraphs 136–138 of Statement 121:

> In May 1993, the Board issued FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan,* which requires certain impaired loans to be measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate, or as a practical expedient, at the loan's observable market price or the fair value of the collateral if the impaired loan is collateral dependent. Regardless of the measurement method, a creditor should measure impairment based on the fair value of the collateral when the creditor determines that foreclosure is probable. A creditor should consider estimated costs to sell, on a discounted basis, in the measure of impairment if those costs are expected to reduce the cash flows available to repay or otherwise satisfy the loan.
>
> As suggested by one commentator to the Exposure Draft, the Board decided to amend Statement 15 to make the measurement of long-lived assets that are received in full satisfaction of a receivable and that will be sold consistent with the measurement of other long-lived assets under this Statement. The amendment requires that those assets be measured at fair value less cost to sell. The Board considered amending Statement 15 to address shares of stock or equity interests in long-lived assets that are received in full satisfaction of a receivable and that will be sold, but it determined that those items are outside the scope of this Statement.
>
> Loans and long-lived assets are similar in that both are cash-generating assets

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that are subject to impairment. However, inherent differences between monetary and nonmonetary assets have resulted in different accounting treatments for them under the current reporting model.

Amendment to Statement 71

B59. This Statement carries forward the amendment made by Statement 121 to FASB Statement No. 71, *Accounting for the Effects of Certain Types of Regulation,* to apply the provisions of this Statement for long-lived assets to be held and used to all assets of a regulated enterprise except (a) regulatory assets that meet the criteria of paragraph 9 of Statement 71 and (b) costs of recently completed plants that are covered by paragraph 7 of FASB Statement No. 90, *Regulated Enterprises—Accounting for Abandonments and Disallowances of Plant Costs*. Therefore, regulatory assets capitalized as a result of paragraph 9 of Statement 71 should be tested for impairment whenever the criteria of that paragraph are no longer met. Paragraphs 127 and 128 of Statement 121 explained:

> FASB Statement No. 71, *Accounting for the Effects of Certain Types of Regulation,* establishes the accounting model for certain rate-regulated enterprises. Because the rates of rate-regulated enterprises generally are designed to recover the costs of providing regulated services or products, those enterprises are usually able to recover the carrying amounts of their assets. Paragraph 10 of Statement 71 states that when a regulator excludes a cost from rates, "the carrying amount of any related asset shall be reduced to the extent that the asset has been impaired. Whether the asset has been impaired shall be judged the same as for enterprises in general" (footnote reference omitted). Statement 71 does not provide any guidance about when an impairment has, in fact, occurred or about how to measure the amount of the impairment.
>
> The Board considered whether the accounting for the impairment of long-lived assets and identifiable intangibles by rate-regulated enterprises that meet the criteria for applying Statement 71 should be the same as for enterprises in general. In March 1993, the EITF discussed incurred costs capitalized pursuant to the criteria of paragraph 9 of Statement 71. The EITF reached a consensus in EITF Issue No. 93-4, "Accounting for Regulatory Assets," that a cost that does not meet the asset recognition criteria in paragraph 9 of Statement 71 at the date the cost is incurred should be recognized as a regulatory asset when it does meet those criteria at a later date. The EITF also reached a consensus that the carrying amount of a regulatory asset should be reduced to the extent that the asset has been impaired with impairment judged the same as for enterprises in general; the provisions of [Statement 121] nullify that consensus.

B60. Paragraphs 129–134 of Statement 121 discussed approaches considered and the basis for the Board’s conclusion:

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The Board considered several approaches to recognizing and measuring the impairment of long-lived assets and identifiable intangibles of rate-regulated enterprises. One approach the Board considered was to apply paragraph 7 of FASB Statement No. 90, *Regulated Enterprises—Accounting for Abandonments and Disallowances of Plant Costs,* to all assets of a regulated enterprise and not just to costs of recently completed plants. That paragraph requires that an impairment loss be recognized when a disallowance is probable and the amount can be reasonably estimated. If a regulator explicitly disallows a certain dollar amount of plant costs, an impairment loss should be recognized for that amount. If a regulator explicitly but indirectly disallows plant costs (for example, by excluding a return on investment on a portion of plant costs), an impairment loss should be recognized for the effective disallowance by estimating the expected future cash flows that have been disallowed as a result of the regulator's action and then computing the present value of those cash flows. That approach would recognize a probable disallowance as an impairment loss, the amount of the loss would be the discounted value of the expected future cash flows disallowed, and the discount rate would be the same as the rate of return used to estimate the expected future cash flows.

A second approach the Board considered was to supersede paragraph 7 of Statement 90 and apply this Statement's requirements to all plant costs. A disallowance would result in costs being excluded from the rate base. The recognition and measurement requirements of this Statement would be applied to determine whether an impairment loss would be recognized for financial reporting purposes.

A third approach the Board considered was to apply the general impairment provisions of this Statement to all assets of a regulated enterprise except for disallowances of costs of recently completed plants, which would continue to be covered by paragraph 7 of Statement 90. A disallowance would result in the exclusion of costs from the rate base. That disallowance would result in an impairment loss for financial reporting purposes if the costs disallowed relate to a recently completed plant. If the costs disallowed do not relate to a recently completed plant, the recognition and measurement requirements of this Statement would be applied to determine whether and how much of an impairment loss would be recognized for financial reporting purposes.

A fourth approach the Board considered was to apply the general impairment standard to all assets of a regulated enterprise except (a) regulatory assets that meet the criteria of paragraph 9 of Statement 71 and (b) costs of recently completed plants that are covered by paragraph 7 of Statement 90. Impairment of regulatory assets capitalized as a result of paragraph 9 of Statement 71 would be recognized whenever the criteria of that paragraph are no longer met.

The Board decided that the fourth approach should be used in accounting for the impairment of all assets of a rate-regulated enterprise. The Board amended

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> paragraph 9 of Statement 71 to provide that a rate-regulated enterprise should charge a regulatory asset to earnings if and when that asset no longer meets the criteria in paragraph 9(a) and (b) of that Statement. The Board also amended paragraph 10 of Statement 71 to require that a rate-regulated enterprise recognize an impairment for the amount of costs excluded when a regulator excludes all or part of a cost from rates, even if the regulator allows the rate-regulated enterprise to earn a return on the remaining costs allowed.
>
> The Board believes that because a rate-regulated enterprise is allowed to capitalize costs that enterprises in general would otherwise have charged to expense, the impairment criteria for those assets should be different from enterprises in general. The Board believes that symmetry should exist between the recognition of those assets and the subsequent impairment of those assets. The Board could see no reason that an asset created as a result of regulatory action could not be impaired by the actions of the same regulator. Other assets that are not regulatory assets covered by Statement 71 or recently completed plant costs covered by Statement 90, such as older plants or other nonregulatory assets of a rate-regulated enterprise, would be covered by the general provisions of this Statement.

B61. Paragraph 135 of Statement 121 further clarified the accounting for previously disallowed costs that are subsequently allowed by a regulator:

> The Board decided that previously disallowed costs that are subsequently allowed by a regulator should be recorded as an asset, consistent with the classification that would have resulted had those costs initially been included in allowable costs. Thus, plant costs subsequently allowed should be classified as plant assets, whereas other costs (expenses) subsequently allowed should be classified as regulatory assets. The Board amended Statement 71 to reflect this decision. The Board decided to restore the original classification because there is no economic change to the asset—it is as if the regulator never had disallowed the cost. The Board determined that restoration of cost is allowed for rate-regulated enterprises in this situation, in contrast to other impairment situations, because the event requiring recognition of the impairment resulted from actions of an independent party and not management's own judgment or determination of recoverability.

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

B62. In Statement 121, the Board decided that the provisions for long-lived assets to be disposed of, including the requirement to cease depreciating (amortizing) a long-lived asset when it is classified as held for disposal, should be applied to all long-lived assets to be disposed of, whether by sale or abandonment. During its deliberations leading to the Exposure Draft, the

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Board reconsidered that decision, noting that its rationale for not depreciating (amortizing) a long-lived asset to be disposed of by sale does not apply to a long-lived asset to be disposed of other than by sale. Such transactions include the abandonment of a long-lived asset, as well as the exchange of a long-lived asset for a similar productive long-lived asset and the distribution of a long-lived asset to owners in a spinoff (including a pro rata distribution to owners of shares of a subsidiary or other investee company that has been or is being consolidated or that has been or is being accounted for under the equity method) or other form of reorganization or liquidation or in a plan that is in substance the rescission of a prior business combination covered by APB Opinion No. 29, *Accounting for Nonmonetary Transactions*.

B63. Specifically, the Board observed that to the extent the carrying amount of a long-lived asset to be disposed of by abandonment is recoverable, it will be recovered principally through operations, rather than through the disposal transaction. Additionally, the accounting guidance in Opinion 29 for the exchange of a similar productive long-lived asset and for the distribution of a long-lived asset to owners in a spinoff is based on the carrying amount of the asset exchanged or distributed. The Board concluded that the Opinion 29 guidance is more consistent with the accounting for a long-lived asset to be held and used than for a long-lived asset to be sold. Thus, the Board decided that a long-lived asset to be disposed of other than by sale should continue to be classified as held and used and depreciated (amortized) until it is abandoned, exchanged, or distributed.

B64. Some respondents to the Exposure Draft said that there is no conceptual difference between sale and other disposal transactions and that the provisions of this Statement for long-lived assets to be disposed of by sale should be applied to other disposal transactions. During its redeliberations of the Exposure Draft, the Board affirmed its conclusion that a long-lived asset to be disposed of other than by sale should continue to be classified as held and used and depreciated (amortized) until disposed of for the reasons discussed in paragraph B63. Accordingly, paragraphs 7–26 of this Statement, except as modified by paragraph 29, apply to that asset or its asset group as previously determined on a held-and-used basis until it is disposed of. If that asset will be disposed of together with other assets and liabilities as a group and the group is a component of an entity, paragraphs 41–44 of this Statement apply to that disposal group when it is disposed of.

Long-Lived Asset to Be Abandoned

B65. The Board decided that if a long-lived asset that is being used is to be abandoned before the end of its previously estimated useful life, depreciation estimates should be revised in accordance with Opinion 20 to reflect the use of the asset over that shortened period. The Board reasoned that because the continued use of a long-lived asset demonstrates the presence of service potential, the immediate write-down of the asset to zero generally is inappropriate. A few respondents to the Exposure Draft suggested that the Board provide additional guidance for revising those depreciation estimates under Opinion 20. However, the Board decided not to

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address that issue because depreciation issues are beyond the scope of this Statement.

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

B66. Under Opinion 29 the accounting for the exchange of a long-lived asset for a similar productive long-lived asset and the distribution of a long-lived asset to owners in a spinoff is based on the recorded amount, "after reduction, if appropriate, for an indicated impairment of value" of the asset exchanged (paragraph 21) or distributed (paragraph 23). After Statement 121 was issued, questions emerged on how to determine "an indicated impairment of value" of the asset exchanged or distributed. The primary issue was whether to apply an undiscounted cash flows recoverability test and, if so, at what level. The EITF discussed the issue in Issue No. 96-2, "Impairment Recognition When a Nonmonetary Asset Is Exchanged or Is Distributed to Owners and Is Accounted for at the Asset's Recorded Amount," but did not reach a consensus.

B67. The Board did not redeliberate the Opinion 29 guidance for exchanges of similar productive assets or spinoffs. This Statement, however, resolves Issue 96-2 by requiring that an indicated impairment of value of a long-lived asset that is exchanged for a similar productive long-lived asset or distributed to owners in a spinoff be recognized if the carrying amount of the asset (disposal group) exceeds its fair value at the disposal date. The accounting guidance in Opinion 29 for an exchange of similar productive assets and for a distribution to owners in a spinoff is based on recorded amounts and not fair value. The Board concluded that using recorded amounts is more consistent with the accounting for a long-lived asset to be held and used than for a long-lived asset to be sold. For that reason, the Board believes that an undiscounted cash flows recoverability test should apply prior to the disposal date. The estimates of future cash flows used in that test are based on the use of the asset for its remaining useful life, assuming that the disposal transaction will not occur.

B68. The Board acknowledges the view of some respondents to the Exposure Draft that because the exchange of a long-lived asset for a similar productive long-lived asset does not culminate an earning process, an undiscounted cash flows recoverability test should apply up through the disposal date. The Board observed that the distribution of a long-lived asset to owners also does not culminate an earning process. However, the Board concluded that those disposal transactions are significant economic events that should result in recognition of an impairment loss if the carrying amount of the asset (disposal group) exceeds its fair value at the disposal date. The Board decided that because the fair value of the asset (disposal group) will be determined in connection with the decision to dispose, the practical expedient of an undiscounted cash flows recoverability test should not apply at the disposal date.

B69. This Statement amends Opinion 29 to require that an indicated impairment of value of a long-lived asset that is exchanged for a similar productive long-lived asset or distributed to owners in a spinoff be recognized if the carrying amount of the asset (disposal group) exceeds its

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fair value at the disposal date. It also amends paragraph 44(a) of FASB Statement No. 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies,* to extend that requirement to transactions involving the exchange of proved oil- and gas-producing assets that are being accounted for by the successful-efforts method of accounting.

Long-Lived Assets to Be Disposed Of by Sale

Recognition

Plan-of-Sale Criteria

B70. As a basis for determining when to classify a long-lived asset (disposal group) as held for sale, Statement 121 required a commitment to a plan to sell the asset (disposal group) but did not specify factors beyond that commitment that should be considered. Consequently, in implementing Statement 121, questions emerged about when to classify a long-lived asset (disposal group) as held for sale. Because a long-lived asset is not depreciated (amortized) while it is classified as held for sale, those questions raised concerns that an entity could improve its operating results by asserting a commitment to a plan to sell a long-lived asset (disposal group) at a future date. Because of those concerns, the Board decided that this Statement should specify criteria for determining when an entity's commitment to a plan to sell a long-lived asset (disposal group) is sufficient for purposes of classifying the asset (disposal group) as held for sale.

B71. The Board decided that a long-lived asset (disposal group) should be classified as held for sale in the period in which all of the criteria in paragraph 30 are met, except as permitted in limited situations by paragraphs 31 and 32. In developing those criteria, the Board considered the criteria established by Opinion 30 for a measurement date and by Issue 94-3 for a commitment date. Certain of those criteria are incorporated in paragraphs 30(a), (c), and (f) of this Statement. Additional criteria established by this Statement are incorporated in paragraphs 30(b), (d), and (e). The Board concluded, and many respondents agreed, that those criteria should enable entities to determine consistently when to classify assets (disposal groups) as held for sale.

Available for immediate sale

B72. Paragraph 30(b) of this Statement establishes a criterion that to qualify for classification as held for sale, a long-lived asset (disposal group) must be available for immediate sale in its present condition. The Board concluded that an asset (disposal group) is available for immediate sale if an entity currently has the intent and ability to transfer the asset (disposal group) to a buyer in its present condition within a period that is usual and customary for sales of such assets.

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In developing that criterion, the Board decided not to preclude a long-lived asset (disposal group) from being classified as held for sale while it is being used. The Board reasoned that if a long-lived asset (disposal group) is available for immediate sale, the remaining use of the asset (disposal group) is incidental to its recovery through sale and that the carrying amount of the asset (disposal group) will be recovered principally through sale. The Board also decided not to require a binding agreement for a future sale. The Board concluded that such a requirement would unduly delay reporting the effects of a commitment to a plan to sell a long-lived asset (disposal group).

Maximum one-year holding period

B73. In Statement 121, the Board decided not to limit the holding period for a long-lived asset (disposal group) classified as held for sale, principally to allow for situations in which environmental concerns extend the period required to complete a sale beyond one year. In this Statement, the Board reconsidered that decision, noting that in some other situations, a long-lived asset could, as a result, be inappropriately classified as held for sale and not depreciated (amortized) for an extended period. Consequently, paragraph 30(d) of this Statement establishes a maximum one-year holding period for a long-lived asset (disposal group) classified as held for sale. The Board concluded that for a long-lived asset (disposal group) covered by this Statement, a one-year period is a reasonable period within which to assess the probability of a future sale, noting that the APB previously reached a similar conclusion in Opinion 30 for the disposal of a segment.[31]

B74. Because in some situations events or circumstances might extend the period required to complete the sale of a long-lived asset (disposal group) beyond one year, the Board considered whether and, if so, when to permit an exception to the one-year requirement. The Board decided that a delay in the period required to complete a sale should not preclude a long-lived asset (disposal group) from being classified as held for sale if the delay is caused by events or circumstances beyond an entity's control and there is sufficient evidence that the entity remains committed to its plan to sell the asset (disposal group). The Board decided to permit an exception in such situations. The Board concluded that the usefulness and clarity of financial statements would not be improved by having long-lived assets (disposal groups) moving in and out of the held-for-sale classification.

B75. A few respondents to the Exposure Draft suggested that the Board permit an exception to the one-year requirement in all situations in which a long-lived asset is acquired through foreclosure by incorporating in this Statement the held-for-sale presumption in paragraph 10 of AICPA Statement of Position 92-3, *Accounting for Foreclosed Assets,* which stated:

> Most enterprises do not intend to hold foreclosed assets for the production of income but intend to sell them; in fact, some laws and regulations applicable to financial institutions require the sale of foreclosed assets. Therefore, under this

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SOP, it is presumed that foreclosed assets are held for sale and not for the production of income.

Those respondents said that in situations in which an entity acquires a long-lived asset through foreclosure, circumstances attendant to the foreclosure often extend the period required to complete the sale beyond one year. The Board concluded that this Statement sufficiently addresses the need for an exception to the one-year requirement for all long-lived assets (disposal groups) covered by this Statement, whether previously held and used or newly acquired. To be consistent with an objective of developing a single accounting model for long-lived assets to be disposed of by sale, the Board decided not to incorporate the held-for-sale presumption in SOP 92-3.

Market price reasonable in relation to current fair value

B76. Paragraph 30(e) of this Statement establishes a criterion that to qualify for classification as held for sale, an entity must be actively marketing a long-lived asset (disposal group) at a price that is reasonable in relation to its current fair value. The Board believes that the price at which a long-lived asset (disposal group) is being marketed is indicative of whether the entity currently has the intent and ability to sell the asset (disposal group). A market price that is reasonable in relation to fair value indicates that the asset (disposal group) is available for immediate sale, whereas a market price in excess of fair value indicates that the asset (disposal group) is not available for immediate sale.

Commitment to a Plan to Sell a Long-Lived Asset after the Balance Sheet Date but before Issuance of Financial Statements

B77. In implementing Statement 121, questions emerged about the required accounting if an entity commits to a plan to sell a long-lived asset after the balance sheet date but before issuance of the financial statements. Prior to this Statement, Opinion 30 and EITF Issue No. 95-18, “Accounting and Reporting for a Discontinued Business Segment When the Measurement Date Occurs after the Balance Sheet Date but before the Issuance of Financial Statements,” provided related guidance for a segment of a business (as defined in that Opinion). In an expected loss situation, Opinion 30 required that the financial statements be adjusted if the loss “provides evidence of conditions that existed at the date of such statements and affects estimates inherent in the process of preparing them” (footnote 5). Issue 95-18 later incorporated the presumption that an expected loss is evidence of a loss existing at the balance sheet date, unless the subsequent decision to dispose of the segment results from a discrete and identifiable event that occurs unexpectedly after the balance sheet date.

B78. The Board decided that if an entity commits to a plan to sell a long-lived asset after the balance sheet date but before issuance of the financial statements, the asset should continue to be classified as held and used. The Board concluded that retroactively classifying the asset as held

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for sale would be inconsistent with having specified criteria for determining when an entity's commitment to a plan to sell a long-lived asset (disposal group) is sufficient for purposes of classifying the asset (disposal group) as held for sale. Similarly, the Board concluded that if the asset (asset group) is tested for recoverability on a held-and-used basis as of the balance sheet date, the estimates of future cash flows used in that test should 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 should not be revised for a decision to sell the asset after the balance sheet date. Therefore, this Statement nullifies Issue 95-18.

B79. The Board considered the view of some respondents to the Exposure Draft that in an expected loss situation, a requirement to classify the asset as held and used could unduly delay recognition of a loss that existed at the balance sheet date. The Board concluded that, on balance, the benefits of having well-defined criteria for when to classify a long-lived asset as held for sale outweigh that concern, noting that the situation referred to by respondents can arise whenever a long-lived asset is expected to be sold but there is no commitment to a plan of sale. The Board observed that if the plan-of-sale criteria are met after the balance sheet date but before issuance of the financial statements, the entity could be required to perform a recoverability test in accordance with paragraph 8(f). In that situation, application of the recoverability test as well as any fair value assessment would be based on facts and circumstances existing at the balance sheet date and could result in an impairment adjustment as of the balance sheet date. The Board agreed that if prior to meeting the plan-of-sale criteria the entity had previously tested the asset (asset group) for impairment on a held-and-used basis at the balance sheet date, it would be inappropriate to undertake a new recoverability test.

Measurement

Lower of Carrying Amount or Fair Value Less Cost to Sell

B80. This Statement retains the requirement of Statement 121 to measure a long-lived asset (disposal group) classified as held for sale at the lower of its carrying amount or fair value less cost to sell. In contrast to a long-lived asset (asset group) to be held and used, a long-lived asset (disposal group) classified as held for sale will be recovered principally through sale rather than through operations. Therefore, accounting for that asset (disposal group) is a process of valuation rather than allocation. The asset (disposal group) is reported at the lower of its carrying amount or fair value less cost to sell, and fair value less cost to sell is evaluated each period to determine if it has changed. Losses (and gains, as permitted by paragraph 37) are reported as adjustments to the carrying amount of a long-lived asset while it is classified as held for sale.

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Cost to sell

B81. The Exposure Draft proposed to retain the requirements of Statement 121 for determining cost to sell. Those requirements were discussed in paragraph 116 of Statement 121, which stated:

> The Board concluded that the cost to sell an asset to be disposed of generally includes the incremental direct costs to transact the sale of the asset. Cost to sell is deducted from the fair value of an asset to be disposed of to arrive at the current value of the estimated net proceeds to be received from the asset's future sale. The Board decided that costs incurred during the holding period to protect or maintain an asset to be disposed of generally are excluded from the cost to sell an asset because those costs usually are not required to be incurred in order to sell the asset. However, the Board believes that costs required to be incurred under the terms of a contract for an asset's sale as a condition of the buyer's consummation of the sale should be included in determining the cost to sell an asset to be disposed of.

B82. Some respondents to the Exposure Draft noted that those requirements for determining cost to sell did not limit cost to sell to the incremental direct costs to transact a sale. They said that, as a result, cost to sell could be interpreted as including normal operating costs (losses) expected to be incurred while a long-lived asset (disposal group) is classified as held for sale, which they did not believe was consistent with the Board's intent. To convey its intent more clearly, the Board decided to revise those requirements to limit cost to sell in all circumstances to the incremental direct costs to transact the sale. Accordingly, costs that are "required to be incurred under the terms of a contract for an asset's sale as a condition of the buyer's consummation of the sale," as referred to in paragraph 116 of Statement 121, would be excluded. In addition, expected future operating losses that marketplace participants would not similarly consider in their estimates of the fair value less cost to sell of a long-lived asset (disposal group) classified as held for sale also would be excluded. In this Statement, the Board clarified that such losses should not be indirectly recognized as part of an expected loss on sale by reducing the carrying amount of the asset (disposal group) to an amount less than its current fair value less cost to sell. Excluding such losses from the measurement of a long-lived asset (disposal group) classified as held for sale supersedes the net realizable value measurement approach previously required under Opinion 30.

Ceasing depreciation (amortization)

B83. This Statement retains the requirement of Statement 121 to cease depreciating (amortizing) a long-lived asset when it is classified as held for sale and measured at the lower of its carrying amount or fair value less cost to sell. Some respondents disagreed with that requirement as also

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proposed in the Exposure Draft. They said that not depreciating (amortizing) a long-lived asset that is being used is inconsistent with the basic principle that the cost of a long-lived asset should be allocated over the period during which benefits are obtained from its use. The Board considered that view but affirmed its conclusion in Statement 121 that depreciation accounting is inconsistent with the use of a lower of carrying amount or fair value measure for a long-lived asset classified as held for sale because, as previously stated, accounting for that asset is a process of valuation rather than allocation.

B84. Some respondents also said that not depreciating (amortizing) a long-lived asset that is being used while it is classified as held for sale hinders the comparability of operating results during that period. They said that the comparability of operating results (reported in both continuing operations and in discontinued operations) between periods is more important than the valuation of the asset while it is classified as held for sale. The Board also considered those concerns but observed that in situations where the carrying amount of the asset (disposal group) is written down to its fair value less cost to sell, continuing to depreciate (amortize) the asset reduces its carrying amount below its fair value less cost to sell. The Board concluded that it would be inappropriate to reduce the carrying amount of the asset to an amount below its fair value. The Board further observed that because fair value less cost to sell is required to be evaluated each period, a subsequent decline in the fair value of the asset while it is classified as held for sale will be appropriately reflected in the period of decline.

Long-Lived Asset Acquired in a Purchase Business Combination

B85. Prior to the issuance of Statement 121, EITF Issue No. 87-11, "Allocation of Purchase Price to Assets to Be Sold," provided guidance on the accounting for a disposal group to be sold that was newly acquired in a purchase business combination, including, but not limited to, a segment of a business covered by Opinion 30. The guidance in Issue 87-11 extended the measurement provisions of Opinion 30 in determining the purchase price allocation under Opinion 16. Accordingly, the disposal group was measured at the lower of its carrying amount or net realizable value, adjusted for future operating losses.

B86. Statement 121 subsequently required that a long-lived asset (disposal group) to be sold other than a segment of a business covered by Opinion 30 be measured at the lower of its carrying amount or fair value less cost to sell. However, it did not nullify Issue 87-11 to reflect that change for a long-lived asset (disposal group) to be sold that was newly acquired in a purchase business combination. Consequently, in implementing Statement 121, questions emerged about the impact of that Statement on Issue 87-11. The primary issue was whether and, if so, how the measurement guidance provided by Issue 87-11 should be applied to a long-lived asset (disposal group) that was newly acquired in a purchase business combination. A related issue was how to account for the results of operations of the asset (disposal group) while it was classified as held for sale and whether future operating losses could be considered in measuring the fair value less cost to sell of the asset (disposal group). The EITF discussed that issue in

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Issue No. 95-21, "Accounting for Assets to Be Disposed Of Acquired in a Purchase Business Combination," but did not reach a consensus.

B87. This Statement resolves Issue 95-21 by requiring that a long-lived asset (disposal group) classified as held for sale be measured at the lower of its carrying amount or fair value less cost to sell, whether previously held and used or newly acquired. This Statement also requires that the results of operations of a long-lived asset (disposal group) classified as held for sale be recognized in the period in which those operations occur, whether reported in continuing operations or in discontinued operations. Therefore, this Statement nullifies Issue 87-11.

Grouping Assets and Liabilities to Be Sold

B88. During its deliberations leading to the Exposure Draft, the Board noted that long-lived assets often are sold together with other assets and liabilities as a group. The Board observed that, as is the case for long-lived assets to be held and used, measuring assets and liabilities classified as held for sale as a group raises the issue of when, if ever, it is appropriate to offset unrealized losses on some assets (liabilities) with unrealized gains on other assets (liabilities). In addition, because liabilities often can be settled separately from the sale of assets, measuring assets and liabilities classified as held for sale as a group also could permit an entity to achieve a desired result by selectively designating the liabilities to be included in a disposal group. To prevent grouping from being used inappropriately to offset unrealized losses with unrealized gains, the Board initially decided that the plan-of-sale criteria should address when assets and liabilities should be classified as held for sale and measured as a group.

B89. The Exposure Draft proposed a criterion that, to classify assets and liabilities as held for sale as a group, the estimated proceeds expected to result from the sale of the group must exceed those that would result from the sale of the assets of the group individually. The Board reasoned that because estimated proceeds reflect the underlying economics of an expected sale transaction, that criterion would provide evidence of an entity's commitment to a plan to sell assets (and liabilities) as a group. Several respondents to the Exposure Draft disagreed with a criterion based on estimated net proceeds, stating that proceeds alone do not necessarily reflect the total (direct and indirect) economic benefit that may result from the sale of assets (and liabilities) as a group. They said that in many situations, valid reasons may exist to sell assets and liabilities as a group even though the estimated net proceeds expected to result from the sale of that group may be less than those that would result from the sale of the assets individually. They also said that in other situations, particularly those in which several assets are to be sold as a group, a requirement to estimate the net proceeds that would result from the sale of assets individually would be unduly burdensome and costly.

B90. Upon reconsideration, the Board decided to eliminate a criterion based on estimated net proceeds. Instead, the Board decided that assets and liabilities should be classified as held for sale as a group if (a) the assets will be sold as a group in a single transaction and (b) the liabilities are directly related to the assets and will be transferred in that transaction. The Board

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concluded that if assets and liabilities will be sold as a group in a single transaction, accounting for those assets and liabilities as held for sale as a group is appropriate.

Allocation of a Loss

B91. During its deliberations leading to the Exposure Draft, the Board decided that this Statement should provide guidance for allocating a loss recognized for a disposal group classified as held for sale that includes assets and liabilities, principally to facilitate the requirement of this Statement to present those assets and liabilities separately in the asset and liability sections of the statement of financial position. The Exposure Draft proposed that a loss be allocated, first, by adjusting the carrying amounts of the liabilities of the group to their fair values and, then, by adjusting the carrying amounts of the long-lived assets of the group by the remaining amount, if any. The Board reasoned that the fair values of the liabilities included in a disposal group generally would be determinable and that the presentation of those liabilities at their fair values would improve the usefulness of the information provided by the statement of financial position.

B92. Upon further consideration, the Board subsequently decided not to retain that allocation method. Instead, the Board decided that because other accounting pronouncements prescribe the accounting for assets and liabilities not covered by this Statement that are included in a disposal group, a loss recognized for a disposal group classified as held for sale should reduce only the carrying amounts of the long-lived assets of the group. The Board concluded that the allocation method for a loss recognized for a disposal group classified as held for sale provides a reasonable basis for reporting both the assets and liabilities of the disposal group in the statement of financial position.

Changes to a Plan of Sale

Reversal of a Decision to Sell a Long-Lived Asset Classified as Held for Sale

B93. In implementing Statement 121, questions emerged about the required accounting if an entity subsequently decides not to sell a long-lived asset classified as held for sale. Prior to this Statement, other accounting pronouncements provided related guidance, but only for certain assets. If the asset previously was acquired through foreclosure, SOP 92-3 required that the asset be reclassified as held and used and measured at what would have been its carrying amount had the asset been continuously classified as held and used since the time of foreclosure. If the asset previously was acquired in a purchase business combination, EITF Issue No. 90-6, "Accounting for Certain Events Not Addressed in Issue No. 87-11 Relating to an Acquired Operating Unit to Be Sold," required that the asset be reclassified as held and used and measured as under SOP 92-3 if the subsequent decision not to sell was made within one year. If the asset was a segment accounted for as a discontinued operation under Opinion 30, EITF Issue No. 90-16,

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"Accounting for Discontinued Operations Subsequently Retained," provided guidance on the reclassification to continuing operations of amounts previously reported in discontinued operations.

B94. The Board decided that a long-lived asset to be reclassified as held and used should be measured at the lower of (a) its fair value at the date of the subsequent decision not to sell or (b) its carrying amount on a held-and-used basis at the date of the decision to sell, adjusted for any depreciation (amortization) expense that would have been recognized had the asset been continuously classified as held and used. Therefore, this Statement nullifies Issues 90-6 and 90-16.

B95. The Board considered but rejected an approach that, based on the guidance in SOP 92-3 and Issue 90-6, would have measured a long-lived asset to be reclassified as held and used at what would have been its carrying amount had the asset been continuously classified as held and used (held-and-used approach). The Board observed that a held-and-used approach could measure an asset previously written down to its fair value less cost to sell at an amount greater than its fair value at the date of the subsequent decision not to sell. That would be the case if, for example, the adjusted carrying amount of the asset is recoverable at the date of the subsequent decision not to sell. The Board concluded that it would be inappropriate to write up the carrying amount of a long-lived asset to an amount greater than its fair value based solely on an undiscounted cash flows recoverability test.

B96. Some respondents to the Exposure Draft suggested that the Board reconsider a held-and-used approach. They said that if the adjusted carrying amount of the asset is recoverable at the date of the subsequent decision not to sell, measuring the asset at its fair value would be inconsistent with the requirements of this Statement for other assets to be held and used, in particular, the requirement to write down the carrying amount of a long-lived asset (asset group) only if it is not recoverable. During its redeliberations of the Exposure Draft, the Board considered that inconsistency but again rejected that approach for the reason discussed in paragraph B95.

Removal of an Individual Asset or Liability from Disposal Group

B97. In view of its decision that assets and liabilities classified as held for sale should be measured as a group, the Board decided that this Statement should address the accounting if an entity subsequently removes an individual asset or liability from a disposal group previously classified as held for sale. The Board considered situations in which an entity decides not to sell an individual asset of the group, decides to sell an individual asset separately from the group, or settles before its maturity an individual liability of the group.

B98. The Exposure Draft would have required that the remaining long-lived assets of the disposal group be measured individually at the lower of their carrying amounts or fair values less

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cost to sell whenever an individual asset or liability is removed from the group. Several respondents to the Exposure Draft disagreed with that proposed requirement. They said that in many situations, valid reasons may exist for removing an individual asset or liability from a disposal group that have no bearing on an entity's intent and ability to sell the remaining assets and liabilities as a group. They also said that in other situations, particularly those in which several long-lived assets are included in a disposal group, a requirement to measure those assets individually would be unduly burdensome and costly.

B99. The Board considered those concerns raised by respondents. The Board decided that the remaining long-lived assets of the disposal group should be measured individually at the lower of their fair values less cost to sell only if the plan-of-sale criteria in paragraph 30 are no longer met for that group. The Board concluded that those criteria provide sufficient evidence of a commitment to a plan to sell the remaining assets and liabilities as a group and that continuing to account for those assets and liabilities as held for sale as a group is appropriate. In addition, the Board observed that for some disposal groups, there may not be significant offsetting issues.

Reporting and Disclosure of Long-Lived Assets (Disposal Groups) to Be Disposed Of

Reporting Discontinued Operations

B100. Prior to this Statement, guidance on reporting discontinued operations was provided by Opinion 30, which limited that reporting to the results of operations of a segment of a business to be disposed of. Paragraph 13 of Opinion 30 defined a segment of a business as a "component of an entity whose activities represent a separate major line of business or class of customer." Opinion 30 required that the results of operations of a segment to be disposed of be reported in discontinued operations, separately from continuing operations, in the period in which the measurement date occurred and in prior periods presented.

B101. During its deliberations leading to the Exposure Draft, the Board concluded that reporting discontinued operations separately from continuing operations provides investors, creditors, and others with information that is relevant in assessing the effects of disposal transactions on the ongoing operations of an entity. FASB Concepts Statement No. 1, *Objectives of Financial Reporting by Business Enterprises,* states, ". . . financial reporting should provide information to help investors, creditors, and others assess the amounts, timing, and uncertainty of prospective net cash inflows to the related enterprise" (paragraph 37; footnote reference omitted). FASB Concepts Statement No. 5, *Recognition and Measurement in Financial Statements of Business Enterprises,* further states:

> Classification in financial statements facilitates analysis by grouping items with essentially similar characteristics and separating items with essentially different characteristics. Analysis aimed at objectives such as predicting

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> amounts, timing, and uncertainty of future cash flows requires financial information segregated into reasonably homogenous groups. For example, components of financial statements that consist of items that have similar characteristics in one or more respects, such as continuity or recurrence, stability, risk, and reliability, are likely to have more predictive value than if their characteristics are dissimilar. [paragraph 20]

B102. The Board observed that the Opinion 30 definition of a segment of a business has been effective in distinguishing disposal transactions that are likely to have a significant effect on the ongoing operations of the entity. However, the Board also observed that the disposal of other disposal groups that are not reported separately in discontinued operations because they are not segments of a business covered by Opinion 30 also might have a significant effect on the ongoing operations of the entity. To improve the usefulness of the information provided to users, the Board decided to broaden the reporting of discontinued operations, consistent with the recommendation made by the AICPA Special Committee on Financial Reporting in its 1994 report, *Improving Business Reporting—A Customer Focus,* which states:

> Discontinued operations is defined in current practice as a component of a company whose activities represent a separate major line of business or class of customer. That definition should be broadened to include all significant discontinued operations whose assets and results of operations and activities can be distinguished physically and operationally and for business-reporting purposes. [page 138]

B103. The Exposure Draft proposed to broaden the reporting of discontinued operations to include the results of operations of a significant component of an entity, which was defined as a disposal group with operations and assets that can be clearly distinguished physically, operationally, and for financial reporting purposes from the rest of the entity. However, the Board chose not to define the term *significant* to allow for judgment in determining whether, based on facts and circumstances unique to a particular entity, a disposal transaction should be reported in discontinued operations.

B104. Nearly all of the respondents to the Exposure Draft that commented on the proposed requirements for reporting discontinued operations agreed with the Board's decision to broaden the reporting of discontinued operations. However, many of those respondents said that to promote consistent application of the Statement, the Board should provide additional guidance for determining the significance of a component of an entity. Many respondents also referred to the interaction of the significance notion proposed in the Exposure Draft with the materiality concept discussed in SEC Staff Accounting Bulletin No. 99, *Materiality*. Those respondents asked the Board to clarify whether the criteria for assessing materiality in SAB 99 also should apply in assessing significance.

B105. During its redeliberations of the Exposure Draft, the Board decided to eliminate the

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significance notion from the definition of a component of an entity. The Board concluded that the requirements for reporting discontinued operations should not focus on whether a component of an entity is significant or otherwise incorporate a quantitative criterion. Instead, the Board concluded that those requirements should focus on whether a component of an entity has operations and cash flows that can be clearly distinguished from the rest of the entity, consistent with its objective of broadening the reporting of discontinued operations.

B106. The Board also decided to eliminate the requirement proposed in the Exposure Draft that assets be eliminated in a disposal transaction as a condition for reporting discontinued operations. The Board observed that the emphasis on assets would preclude a component of an entity from being reported as a discontinued operation unless the disposal transaction involved all of the assets of the component—even if the component is separate business and was an operating segment under FASB Statement No. 131, *Disclosures about Segments of an Enterprise and Related Information*. The Board also decided to eliminate the Exposure Draft's reference to disposal activities that are incident to the evolution of an entity's business, which would have prohibited those disposal activities from being reported as discontinued operations. As noted by some respondents, many disposal transactions could be viewed as incident to the evolution of an entity's business.

B107. As revised, the requirements for reporting discontinued operations focus on whether a component of an entity has operations and cash flows that can be clearly distinguished from the rest of the entity and whether those operations and cash flows have been (or will be) eliminated from the ongoing operations of the entity in the disposal transaction. Given the emphasis on operations, the Board decided to incorporate as a condition for reporting discontinued operations the requirement that an entity have no significant continuing involvement in the operations of a component after it is disposed of. The Board concluded that it would be inappropriate to report a disposal transaction as a discontinued operation in circumstances in which an entity will have significant continuing involvement in the operations of a component after it is disposed of.

B108. During its deliberations of this Statement, the Board considered but rejected other approaches that would have reported in discontinued operations the results of operations of other asset groups as defined in other existing accounting pronouncements. One approach would have used the definition of an *operating segment* in paragraph 10 of Statement 131. Another approach would have used the definition of a *reporting unit* in Statement 142. Yet another approach would have used the definition of a *business* in EITF Issue No. 98-3, "Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business." The Board concluded that those approaches would not necessarily broaden the reporting of discontinued operations beyond that previously permitted by Opinion 30.

B109. The Board acknowledges that judgment will be required in distinguishing components of an entity from other disposal groups. However, the Board affirmed its conclusion in the Exposure Draft that, on balance, the advantages of broadening the presentation of discontinued operations (primarily enhanced decision usefulness) outweigh the disadvantages of broadening

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that presentation (primarily the possibility that the use of inconsistent judgments will affect the comparability of information reported about disposal transactions).

Subsequent Adjustments to Discontinued Operations

B110. This Statement specifies requirements for reporting in discontinued operations adjustments in the current period that are related to the disposal of a component of an entity in a prior period. Those requirements carry forward certain of the provisions of other accounting pronouncements relating to the disposal of an Opinion 30 segment that are still relevant.

B111. Paragraphs 44(a) and (b) of this Statement refer to adjustments relating to the resolution of contingencies that arise pursuant to the terms of the disposal transaction, as well as to those that arise from, and that are directly related to, the operations of a component of an entity prior to its disposal. Paragraph 25 of Opinion 30 specified requirements for reporting in discontinued operations adjustments related to the disposal of a segment of a business that was reported in a prior period. It did not, however, specify the types of adjustments to which that reporting was intended to apply. Paragraph 25 of Opinion 30, as amended by FASB Statement No. 16, *Prior Period Adjustments,* stated:

> Circumstances attendant to disposals of a segment of a business and extraordinary items frequently require estimates, for example, of associated costs and occasionally of associated revenue, based on judgment and evaluation of the facts known at the time of first accounting for the event. Each adjustment in the current period of a loss on disposal of a business segment or of an element of an extraordinary item that was reported in a prior period should be separately disclosed as to year of origin, nature, and amount and classified separately in the current period in the same manner as the original item. If the adjustment is the correction of an error, the provisions of APB Opinion No. 20, *Accounting Changes,* paragraphs 36 and 37 should be applied.

B112. SEC Staff Accounting Bulletin No. 93, *Accounting and Disclosures Relating to Discontinued Operations,* clarified for public enterprises the reporting required by paragraph 25 of Opinion 30 as follows:

> The [SEC] staff believes that the provisions of paragraph 25 apply only to adjustments that are necessary to reflect new information about events that have occurred that becomes available prior to disposal of the business, to reflect the actual timing and terms of the disposal when it is consummated, and to reflect the resolution of contingencies associated with that business, such as warranties and environmental liabilities retained by the seller.

B113. Paragraph 44(c) of this Statement refers to adjustments (gains or losses) associated with

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the settlement of employee benefit plan obligations (pension, postemployment benefits other than pensions, and other postemployment benefits). Paragraph 3 of FASB Statement No. 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits,* defines *settlement* as:

> . . . a transaction that (a) is an irrevocable action, (b) relieves the employer (or the plan) of primary responsibility for a pension benefit obligation, and (c) eliminates significant risks related to the obligation and the assets used to effect the settlement.

B114. In accordance with FASB Statement No. 43, *Accounting for Compensated Absences,* Statement 88, and FASB Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions,* as amended by this Statement, settlement gains or losses should be recognized in the period in which the settlement occurs. Such gains or losses should be reported in discontinued operations if the settlement is directly related to the disposal of a component of an entity. The Board concluded that a settlement is directly related to the disposal of a component of an entity if (a) there is a demonstrated cause-and-effect relationship and (b) the settlement occurs no later than one year following the disposal transaction, unless it is delayed by events or circumstances beyond an entity's control.

B115. The requirement that a demonstrated cause-and-effect relationship exist incorporates guidance from Statement 88 related to the disposal of a segment of a business previously covered by Opinion 30. Specifically, the answer to Question 37 in the FASB Special Report, *A Guide to Implementation of Statement 88 on Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits,* clarifies that a cause-and-effect relationship can be demonstrated if, for example, settlement of a pension benefit obligation for those employees affected by the sale is a necessary condition of the sale. It further clarifies that "in a disposal of all or a portion of a line of business, the timing of a settlement may be at the discretion of the employer. If the employer simply chooses to settle a pension benefit obligation at the time of the sale, the resulting coincidence of events is not, in and of itself, an indication of a cause-and-effect relationship. . . ." In addition, the Board reasoned that a decision to settle later than one year after the disposal date is unlikely to be a direct consequence of the disposal transaction unless that decision is delayed beyond one year by events and circumstances beyond an entity's control.

Reporting Disposal Gains or Losses in Continuing Operations

B116. This Statement retains the requirements of Statement 121 to report gains or losses recognized on long-lived assets (disposal groups) to be sold that are not components of an entity presented in discontinued operations as a component of income from continuing operations. In Statement 121, the Board concluded that the requirements for reporting gains or losses recognized on long-lived assets (disposal groups) to be sold should be consistent with the requirements for reporting impairment losses recognized on long-lived assets (asset groups) to be

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held and used. The Board affirmed that conclusion in this Statement.

Reporting Long-Lived Assets (Disposal Groups) Classified as Held for Sale

B117. Under Opinion 30, the assets and liabilities of a segment of a business accounted for as a discontinued operation were permitted to be offset and reported in the statement of financial position "net." Footnote 7 of paragraph 18(d) of Opinion 30 explained:

> Consideration should be given to disclosing this information by segregation in the balance sheet of the net assets and liabilities (current and noncurrent) of the discontinued segment. Only liabilities which will be assumed by others should be designated as liabilities of the discontinued segment.

B118. The Board noted that the reporting previously permitted under Opinion 30 is an exception to the general rule that assets and liabilities should not be offset. Assets and liabilities that an entity expects to transfer to a buyer in connection with the sale of assets do not meet the conditions for offsetting in FASB Interpretation No. 39, *Offsetting of Amounts Related to Certain Contracts*. Paragraph 5 of Interpretation 39 carries forward from APB Opinion No. 10, *Omnibus Opinion—1966,* the general principle that ". . . the offsetting of assets and liabilities in the balance sheet is improper except where a right of setoff exists." In addition, liabilities that an entity expects to transfer to a potential buyer in a disposal transaction do not qualify for derecognition prior to being assumed by a purchaser (or otherwise settled). Paragraph 42 of Concepts Statement 6 states, "Once incurred, a liability continues as a liability of the entity until the entity settles it, or another event or circumstance discharges it or removes the entity's responsibility to settle it."

B119. The Board decided that the assets and liabilities of a disposal group classified as held for sale should not be offset in the statement of financial position. Accordingly, this Statement eliminates the exception to consolidation for a subsidiary for which control is likely to be temporary in paragraph 2 of ARB No. 51, *Consolidated Financial Statements,* as amended by FASB Statement No. 94, *Consolidation of All Majority-Owned Subsidiaries*. The Board concluded that for any disposal group, information about the nature of both the assets and the liabilities of an asset group classified as held for sale is useful to users. Separately presenting those items in the statement of financial position provides information that is relevant and faithfully reports an entity's assets and its liabilities. Also, it segregates (a) those assets that have been measured at the lower of carrying amount or fair value less cost to sell and are not being depreciated from (b) those assets that are measured on a cost basis and are being depreciated. Therefore, this Statement requires that those assets and liabilities be presented separately in the asset and liability sections of the statement of financial position.

B120. The Board decided not to specify whether assets and liabilities held for sale should be classified as current or noncurrent in the statement of financial position. The Board concluded that because requirements for classifying assets and liabilities as current or noncurrent are

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provided by other accounting pronouncements, including ARB No. 43, Chapter 3, "Working Capital," further guidance in this Statement is not needed.

Disclosure

B121. The Board concluded that the financial statement disclosures previously required by paragraph 19 of Statement 121 and by paragraph 18 of Opinion 30 provide information that is useful in understanding the effects of the disposal of a long-lived asset (disposal group), including a component of an entity. In the Exposure Draft, the Board decided to retain those disclosures that were still relevant, including the requirement of Opinion 30 to disclose the proceeds from a disposal transaction. Some respondents to the Exposure Draft stated that disclosure of proceeds is of little value, noting that information about cash proceeds is now provided in the statement of cash flows. The Board agreed and decided to eliminate that requirement.

Amendment to Statement 67

B122. Statement 121 amended FASB Statement No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects,* to apply (a) its provisions for long-lived assets to be held and used to land to be developed and projects under development and (b) its provisions for long-lived assets to be disposed of to all completed real estate projects. At that time, the Board believed that assets under development were similar to long-lived assets to be held and used and that all completed projects were "clearly assets to be disposed of." Paragraphs 124–126 of Statement 121 explained:

> The Exposure Draft proposed amending FASB Statements No. 66, *Accounting for Sales of Real Estate,* and No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects,* to change the lower of carrying amount or net realizable value measure to the lower of carrying amount or fair value less cost to sell measure. The Board initially decided to amend those Statements to conform the measurement of assets subject to those Statements with the measurement of assets to be disposed of.
>
> Some real estate development organizations objected to the proposed amendments in the Exposure Draft. They questioned why the scope of a project on long-lived assets included real estate development. They argued that real estate development assets are more like inventory and, therefore, the lower of carrying amount or net realizable value measure is more relevant. They did not address, however, why that measure would be more appropriate for real estate inventory than the lower of cost or market measure required for inventory under paragraph 4 of ARB No. 43, Chapter 4, "Inventory Pricing."
>
> Others disagreed with the inventory argument, asserting that although real

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> estate development assets will eventually be disposed of, the provisions of the Exposure Draft would have required long-term real estate projects to recognize impairments far too frequently. They said that nearly all long-term projects, regardless of their overall profitability, would become subject to write-downs in their early stages of development, only to be reversed later in the life of the project due to revised estimates of fair value less cost to sell. The Board considered alternative approaches to measuring those real estate assets. The Board decided to apply the provisions of paragraphs 4—7 to land to be developed and projects under development and to apply paragraphs 15—17 to completed projects. The Board believes that assets under development are similar to assets held for use, whereas completed projects are clearly assets to be disposed of.

B123. In this Statement, the Board reconsidered the amendment to Statement 67, noting that a completed real estate project might be held available for occupancy (either for rental or for use in the entity's operations), in which case the asset would be similar to a long-lived asset to be held and used. The Board concluded that the provisions of this Statement for long-lived assets to be held and used should be applied to those real estate assets. Therefore, this Statement revises the previous amendment to Statement 67. The provisions of this Statement for long-lived assets to be held and used should be applied to completed real estate projects to be held available for occupancy. The provisions of this Statement for long-lived assets to be disposed of by sale should be applied to completed real estate projects to be sold.

B124. In implementing Statement 121, questions also emerged about the application of its impairment provisions to rental real estate property to be held and used. The primary issue was whether property-related assets should be grouped together with the real estate property in determining whether to recognize, and in measuring, an impairment loss. Such property-related assets include accrued rent and deferred leasing costs recognized for operating leases in accordance with FASB Statement No. 13, *Accounting for Leases* (paragraph 19 and paragraph 5(m), as amended by FASB Statement No. 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*), and FASB Technical Bulletin No. 85-3, *Accounting for Operating Leases with Scheduled Rent Increases*. The Board concluded that the provisions of paragraphs 10–14 of this Statement for grouping long-lived assets to be held and used should be applied to those real estate assets.

Benefits and Costs

B125. The mission of the FASB is to establish and improve standards of financial accounting and reporting for the guidance and education of the public, including preparers, auditors, and users of financial information. In fulfilling that mission, the Board endeavors to determine that a proposed standard will fill a significant need and that the costs imposed to meet that standard, as compared with other alternatives, are justified in relation to the overall benefits of the resulting information. Although the costs to implement a new standard may not be borne evenly,

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investors and creditors—both present and potential—as well as others, benefit from improvements in financial reporting, thereby facilitating the functioning of markets for capital and credit and the efficient allocation of resources in the economy.

B126. The Board determined that the requirements in this Statement will result in improved financial reporting. In Statement 121, the Board determined that the information provided to users of financial statements about long-lived assets could be improved by eliminating inconsistencies in the accounting and reporting of the impairment of those assets, thereby improving comparability in financial reporting. In this Statement, the Board determined that the information provided to users of financial statements about long-lived assets could be further improved by eliminating inconsistencies in the accounting and reporting of the disposal of those assets. As discussed in FASB Concepts Statement No. 2, *Qualitative Characteristics of Accounting Information,* providing comparable financial information enables users to identify similarities in and differences between two sets of economic events.

B127. The Board believes that the incremental costs of implementing this Statement have been minimized principally by retaining certain of the fundamental provisions of Statement 121 that are already in effect, in particular, its recognition and measurement provisions for the impairment of long-lived assets to be held and used and its measurement provisions for long-lived assets classified as held for sale. In addition, the Board decided to eliminate from this Statement certain of the proposals in the Exposure Draft that would have changed those existing requirements. Further, the provisions of this Statement generally are to be applied prospectively. Although there may be one-time costs for changes needed to apply the accounting requirements of this Statement, the benefits from more consistent, comparable, and reliable information will be ongoing. The Board believes that the benefits of this Statement outweigh the costs of implementing it.

Effective Date and Transition

B128. The Board decided, except as follows, to require that this Statement be effective for financial statements issued for fiscal years beginning after December 15, 2001, and interim periods within those fiscal years. The Board decided that the provisions relating to disposal transactions should be effective for disposal transactions initiated by a commitment to a plan after the earlier of the effective date of this Statement or the entity's initial application of this Statement. The Board believes that that effective date provides sufficient time for entities and their auditors to analyze, interpret, and prepare for implementation of the provisions of this Statement.

B129. This Statement requires that impairment losses resulting from the initial application of its provisions for long-lived assets to be held and used be reported in the period in which the recognition criteria are initially applied and met based on facts and circumstances existing at that date. This Statement, like Statement 121, requires consideration of the continuing effect of

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events or changes in circumstances that occurred prior to the Statement's initial application. The Board recognizes the benefits of comparative financial statements but questions the ability of entities to reconstruct estimates of future cash flows based on assessments of events and circumstances as they existed in prior periods and without the use of hindsight.

B130. This Statement requires prospective application of its provisions for disposal transactions, including its provisions for the presentation of discontinued operations, and prohibits retroactive application.[32] The Board concluded that obtaining or developing the information necessary to apply this Statement retroactively could be burdensome for many entities. In addition, the Board observed that information about disposal transactions generally is disclosed by public enterprises (for example, in management's discussion and analysis and in press releases). Disposal transactions involving a component of an entity that are "grandfathered" under Statement 121 would continue to be reported in continuing operations, while disposal transactions involving a segment of a business that are "grandfathered" under Opinion 30 would continue to be reported in discontinued operations. The Board noted that segregating those disposal transactions would mitigate the effect of having different measurement approaches under Statement 121 and Opinion 30—one based on the fair value less cost to sell and the other based on net realizable value. The Board concluded that prospective application for disposal transactions is the most reasonable and practical transition approach when considered together with the need for consistent transition provisions for disposal transactions and the cost associated with retroactive application.

B131. The Board observed that for long-lived assets (disposal groups) to be sold that meet the criteria for a qualifying plan of sale when this Statement is initially applied, a cumulative-effect adjustment would not require an entity to retroactively derive fair values for those assets to be disposed of. Rather, the adjustment would be based on fair values at the date this Statement is initially applied. The Board concluded, however, that it would be inappropriate to require retroactive application for some, but not all, of the provisions for disposal transactions. The Board expects that, based on the requirements of previous accounting pronouncements that address the accounting for disposal transactions, many disposal transactions that are in process when this Statement is initially applied will be completed within one year. Therefore, prospective application should not have a significant, continuing impact on the comparability and consistency of the financial statements.

B132. The Board observed, however, that in some cases assets that are classified as held for disposal when this Statement is initially applied may not meet the criteria in paragraph 30 by the end of the fiscal year in which the Statement is initially applied. The Board concluded that it would be inappropriate to allow the accounting for those assets to be "grandfathered" indefinitely. Doing so could impair the comparability and consistency of the financial statements and extend the provisions of Opinion 30 that require the accrual of future operating losses for several reporting periods. Therefore, for a long-lived asset (disposal group) classified as held for disposal when this Statement is initially applied, the asset (disposal group) must be reclassified as held and used in accordance with paragraph 38 if the criteria in paragraph 30 are

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not met by the end of the fiscal year in which this Statement is initially applied.

B133. This Statement requires reclassification of previously issued statements of financial position included for comparative purposes to reflect application of the reporting provisions in paragraph 46 for long-lived assets and disposal groups, including a temporarily controlled subsidiary, classified as held for sale under Statement 121 (that is, the prohibition of offsetting assets and liabilities). The Board believes that requiring reclassification will improve the comparability of those financial statements. Moreover, because that reporting affects only how the assets and liabilities of disposal groups previously classified as held for sale are displayed, the Board concluded that the information necessary to disaggregate and separately report those assets and liabilities would be available.

Appendix C: AMENDMENTS TO EXISTING PRONOUNCEMENTS

C1. This Statement supersedes FASB Statement No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of.*

C2. Accounting Research Bulletin No. 51, *Consolidated Financial Statements,* is amended as follows:

a. In the last sentence of paragraph 2, as amended by FASB Statement No. 94, *Consolidation of All Majority-Owned Subsidiaries,* the phrase *is likely to be temporary or if it* is deleted.

b. Paragraph 12 is deleted.

C3. In paragraphs 21 and the heading preceding it, 30(e), and 31 of APB Opinion No. 28, *Interim Financial Reporting,* all references to *segment of a business* or *segments of a business* are replaced by *component of an entity* or *components of an entity*, respectively.

C4. APB Opinion No. 29, *Accounting for Nonmonetary Transactions,* is amended as follows:

a. The following footnote is added to the end of the first sentence of paragraph 21 and to the first sentence of paragraph 23 after the parenthetical phrase:

> *An indicated impairment of value of a long-lived asset covered by FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets,* shall be determined in accordance with paragraph 29 of that Statement.

C5. APB Opinion No. 30, *Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions,* is amended as follows:

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a. In paragraph 3, *to specify the accounting and reporting for disposal of a segment of a business, (4)* is deleted.

b. Paragraphs 8 and 9 and footnote 2 are deleted.

c. Paragraph 11 is amended as follows:

(1) The following footnote is added to the first sentence immediately following *discontinued operations*:

*Paragraphs 41–44 of Statement 144 address the reporting of discontinued operations.

(2) In the second sentence, *segment of a business* is replaced by *component of an entity.*

d. Paragraphs 13–18 and the heading preceding those paragraphs are deleted.

e. Footnotes 5–7 are deleted.

f. Paragraph 23 is amended as follows:

(1) The references to *segment of a business* are replaced by *component of an entity.*

(2) The last sentence is replaced by the following:

> Disposals of a component of an entity shall be accounted for and presented in the income statement in accordance with Statement 144 even though the circumstances of the disposal meet the criteria specified in paragraph 20.

g. Paragraph 25 is amended as follows:

(1) In the first sentence, *disposals of a segment of a business and* is deleted.

(2) In the second sentence, *of a loss on disposal of a business segment or* is deleted.

C6. AICPA Accounting Interpretation 1, "Illustration of the Application of APB Opinion No. 30," is amended as follows:

a. The first question and its interpretation are amended as follows:

(1) The interpretation and first discussion are deleted.

(2) The following interpretation is inserted before the second discussion:

Interpretation—The criteria for extraordinary items classification should be considered. That is:

Does the event or transaction meet both criteria of *unusual nature* and *infrequency of occurrence?*

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b. The second question and its interpretation are superseded.

C7. In FASB Statement No. 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies,* paragraph 44(a) is replaced by the following:

> a. A transfer of assets used in oil and gas producing activities related to unproved properties in exchange for other assets also used in oil and gas producing activities.*
>
> *If assets used in oil and gas producing activities related to proved properties are transferred in exchange for other assets also used in oil and gas producing activities, a loss, if any, shall be recognized in accordance with paragraph 29 of FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets.*

C8. In FASB Statement No. 43, *Accounting for Compensated Absences,* the last sentence of paragraph 2, as added by FASB Statement No. 112, *Employers' Accounting for Postemployment Benefits,* is deleted.

C9. In FASB Statement No. 66, *Accounting for Sales of Real Estate,* the following is added to the end of the second sentence of paragraph 65:

> unless the property has been classified as held for sale in accordance with paragraph 30 of FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets.*

C10. In FASB Statement No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects,* the first and second sentences of paragraph 24 are replaced by the following:

> The provisions in Statement 144 for long-lived assets to be disposed of by sale shall apply to a real estate project, or parts thereof, that is substantially completed and that is to be sold. The provisions in that Statement for long-lived assets to be held and used shall apply to real estate held for development, including property to be developed in the future as well as that currently under development, and to a real estate project, or parts thereof, that is substantially completed and that is to be held and used (for example, for rental). Determining whether the carrying amounts of real estate projects require recognition of an impairment loss shall be based on an evaluation of individual projects.

C11. FASB Statement No. 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits,* is amended as follows:

a. In paragraph 6(a), *segment of a business* is replaced by *component of an entity.*

b. Paragraphs 8 and 16 and the heading preceding paragraph 16 are deleted.

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c. Paragraph 57 is amended as follows:

(1) In the title of Example 3A, *segment* is replaced by *component.*

(2) In Example 3A, the reference to *segment of its business* is replaced by *component of the entity.*

(3) Footnote d to Example 3A is deleted.

C12. FASB Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions,* is amended as follows:

a. In paragraph 96(a), *segment of a business* is replaced by *component of an entity.*

b. Paragraph 103 and the heading preceding it are deleted.

C13. In paragraph 8(c) of FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* the reference to *segment* is replaced by *component of an entity.*

C14. In the last sentence of paragraph 164 of FASB Statement No. 117, *Financial Statements of Not-for-Profit Organizations,* the reference to *a discontinued operating segment* is replaced by *reporting discontinued operations.*

C15. Paragraph 9 of FASB Statement No. 123, *Accounting for Stock-Based Compensation,* is amended as follows:

a. In the first sentence, *with the same meaning as in FASB Statement No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of.* is replaced by *to refer to.*

b. In the second sentence, *Statement 121 says that the fair value of an asset is . . .* is deleted.

c. The reference to *[paragraph 7]* at the end of the quotation is deleted.

C16. Footnote 18 to paragraph 44 of FASB Statement No. 141, *Business Combinations,* is deleted.

C17. FASB Statement No. 142, *Goodwill and Other Intangible Assets,* is amended as follows:

a. Paragraph 7 is deleted.

b. Paragraph 15 is amended as follows:

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(1) In the first sentence, *Statement 121* is replaced by *FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets,* and *paragraphs 4–11* are replaced by *paragraphs 7–24*.

(2) In the second sentence, *Statement 121* is replaced by *Statement 144*.

c. The second (parenthetical) sentence of paragraph 17 is replaced by *(Paragraph 8 of Statement 144 includes examples of impairment indicators.)*.

d. In paragraph 28(f), *Statement 121* is replaced by *Statement 144*.

e. In the second sentence of paragraph 29, *Statement 121* is replaced by *Statement 144*.

f. Footnote 22 to paragraph 39 is deleted.

g. Appendix A is amended as follows:

(1) In the last sentence of Example 1, *FASB Statement No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of* is replaced by *FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets*.

(2) In Examples 2, 3, 5, and 9, all references to *Statement 121* are replaced by *Statement 144*.

C18. FASB Statement No. 143, *Accounting for Asset Retirement Obligations,* is amended as follows:

a. The fourth sentence of paragraph 2 is replaced by:

This Statement does not apply to obligations that arise solely from a plan to sell or otherwise dispose of a long-lived asset covered by FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*.

b. Paragraph 12 is amended as follows:

(1) In the first sentence, *Statement 121* is replaced by *Statement 144*.

(2) Footnote 11 is deleted.

C19. FASB Interpretation No. 18, *Accounting for Income Taxes in Interim Periods,* is amended as follows:

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a. Footnote 1 to paragraph 5 is replaced by the following:

> The terms used in this definition are described in APB Opinion No. 20, *Accounting Changes,* in APB Opinion No. 30, *Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions,* and in FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets.* See paragraph 10 of Opinion 30 for *extraordinary items* and paragraph 26 for *unusual items* and *infrequently occurring items.* See paragraph 20 of Opinion 20 for *cumulative effects of changes in accounting principles.* See paragraphs 41–44 of Statement 144 for *discontinued operations.*

b. Paragraph 19 is amended as follows:

(1) All references to *measurement date* are replaced by *date on which the criteria in paragraph 30 of Statement 144 are met.*

(2) In the first sentence, *both (a)* and *and (b) the gain (or loss) on disposal of discontinued operations (including any provision for operating loss subsequent to the measurement date)* are deleted.

(3) All references to *discontinued segment* are replaced by *discontinued component.*

(4) Footnote 20 is replaced by the following:

> The term *discontinued component* refers to the disposal of a component of an entity as described in paragraph 41 of Statement 144.

c. In paragraph 35, the references to *segment of a business* are replaced by *component of an entity.*

d. In paragraph 71, under Discontinued operations, *Division* is replaced by *Component* and *Income (loss) on disposal of Division X, including provision of $XXXX for operating losses during phase-out period (less applicable income taxes of $XXXX)* is deleted.

C20. Paragraph 3 of FASB Interpretation No. 27, *Accounting for a Loss on a Sublease,* is deleted.

C21. In paragraph 7 of FASB Interpretation No. 39, *Offsetting of Amounts Related to Certain Contracts,* the reference to *APB Opinion No. 30, Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions (reporting of discontinued operations)* is deleted.

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AMENDMENTS MADE BY STATEMENT 121 CARRIED FORWARD IN THIS STATEMENT WITH MINOR CHANGES

C22. In the first sentence of paragraph 19(h) of APB Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock,* the phrase *the same as a loss in value of other long-term assets* is deleted.

C23. The last question and its interpretation of AICPA Accounting Interpretation 1, "Illustration of the Application of APB Opinion No. 30," are superseded.

C24. FASB Statement No. 15, *Accounting by Debtors and Creditors for Troubled Debt Restructurings,* is amended as follows:

a. The following sentence is added after the first sentence of paragraph 28:

> A creditor that receives long-lived assets that will be sold from a debtor in full satisfaction of a receivable shall account for those assets at their fair value less cost to sell, as that term is used in paragraph 34 of FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*.

b. The last sentence of paragraph 28 is replaced by the following:

> The excess of (i) the recorded investment in the receivable[17] satisfied over (ii) the fair value of assets received (less cost to sell, if required above) is a loss to be recognized. For purposes of this paragraph, losses, to the extent they are not offset against allowances for uncollectible amounts or other valuation accounts, shall be included in measuring net income for the period.

c. In the second sentence of paragraph 33, *at their fair values* is deleted and *less cost to sell* is inserted after *reduced by the fair value*.

C25. The following new heading and paragraph are added after paragraph 62 of FASB Statement No. 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies:*

> **Impairment Test for Proved Properties and Capitalized Exploration and Development Cost**
>
> The provisions of FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets,* are applicable to the costs of an enterprise's wells and related equipment and facilities and the costs of the related proved properties. The impairment provisions relating to unproved properties referred to in paragraphs 12, 27–29, 31(b), 33,

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40, 47(g), and 47(h) of this Statement remain applicable to unproved properties.

C26. The following sentence is added to the end of paragraph 19 of FASB Statement No. 34, *Capitalization of Interest Cost:*

> The provisions of FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets,* apply in recognizing impairment of long-lived assets held for use.

C27. The first two sentences of paragraph 14 of FASB Statement No. 51, *Financial Reporting by Cable Television Companies,* are replaced by the following: **[Note: This amendment does not affect the amendment made by paragraph D5(2) of Statement 142 to refer to other intangible assets subject to the provisions of that Statement.]**

> Capitalized plant and certain intangible assets are subject to the provisions of FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets.*

C28. Paragraph 48 of FASB Statement No. 60, *Accounting and Reporting by Insurance Enterprises,* is amended as follows:

a. In the first sentence, *and an allowance for any impairment in value* is deleted.

b. In the last sentence, *Changes in the allowance for any impairment in value relating to real estate investments* is replaced by *Reductions in the carrying amount of real estate investments resulting from the application of FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets,*.

C29. FASB Statement No. 61, *Accounting for Title Plant,* is amended as follows:

a. In the first and second sentences of paragraph 6, *value* is replaced by *carrying amount.*

b. The last sentence of paragraph 6 is replaced by the following:

> Those events or changes in circumstances, in addition to the examples in paragraph 8 of FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets,* indicate that the carrying amount of the capitalized costs may not be recoverable. Accordingly, the provisions of Statement 144 apply.

C30. Footnote 5 to paragraph 21 of FASB Statement No. 66, *Accounting for Sales of Real Estate,* is replaced by the following:

> Paragraph 24 of FASB Statement No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects,* as amended by FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets,* specifies the accounting for

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property that is substantially completed and that is to be sold.

C31. FASB Statement No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects,* is amended as follows:

a. In paragraph 3, *costs in excess of estimated* ***net realizable value*** is replaced by *reductions in the carrying amounts of real estate assets prescribed by FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets.*

b. Paragraph 16 is deleted.

c. Paragraph 25 is replaced by the following:

   Paragraph 8 of Statement 144 provides examples of events or changes in circumstances that indicate that the recoverability of the carrying amount of a long-lived asset should be assessed. Insufficient rental demand for a rental project currently under construction is an additional example that indicates that the recoverability of the real estate project should be assessed in accordance with the provisions of Statement 144.

d. In paragraph 28, the term *net realizable value* and its definition are deleted.

C32. FASB Statement No. 71, *Accounting for the Effects of Certain Types of Regulation,* is amended as follows:

a. The following sentence is added to the end of paragraph 9:

   If at any time the incurred cost no longer meets the above criteria, that cost shall be charged to earnings.

b. Paragraph 10 is amended as follows:

   (1) The second and third sentences are replaced by:

   If a regulator excludes all or part of a cost from allowable costs, the carrying amount of any asset recognized pursuant to paragraph 9 of this Statement shall be reduced to the extent of the excluded cost.

   (2) In the fourth sentence, *the asset has* is replaced by *other assets have* and *and FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, shall apply* is added to the end of that sentence after the footnote added by FASB Statement No. 90, *Regulated Enterprises—Accounting for Abandonments and Disallowances of Plant Costs.*

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c. The following new paragraph is added after paragraph 10:

> If a regulator allows recovery through rates of costs previously excluded from allowable costs, that action shall result in recognition of a new asset. The classification of that asset shall be consistent with the classification that would have resulted had those costs been initially included in allowable costs.

C33. The following phrase is added to the end of the third sentence of paragraph 6 of FASB Statement No. 101, *Regulated Enterprises—Accounting for the Discontinuation of Application of FASB Statement No. 71:*

> , and FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets,* shall apply, except for the provisions for income statement reporting in paragraphs 25 and 26 of that Statement.

Appendix D: REFERENCES TO PRONOUNCEMENTS

D1. There are many references in the existing authoritative literature to impairment of assets. Appendix C indicates the amendments to pronouncements existing at the date of this Statement. The following table lists FASB and APB pronouncements that refer to impairment of long-lived assets and indicates which of those pronouncements will apply the applicable requirements of this Statement and which will continue to apply some other applicable existing requirement.

Existing Pronouncement	Title	Apply Requirement in This Statement	Apply Existing Requirement	Existing Requirement Paragraph Number
APB Opinion No. 18	*The Equity Method of Accounting for Investments in Common Stock*		X	19(h) (as amended by this Statement)
FASB Statement No. 7	*Accounting and Reporting by Development Stage Enterprises*	X		
FASB Statement No. 13	*Accounting for Leases*			
	• Capital leases of lessees	X		
	• Assets of lessors subject to operating leases	X		

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	• Sales-type, direct financing, and leveraged leases of lessors		X	17
FASB Statement No. 19	*Financial Accounting and Reporting by Oil and Gas Producing Companies*			
	• Unproved properties		X	12, 27–29, 31(b), 33, 40, 47(g), 47(h)
	• Proved properties, wells, and related equipment and facilities accounted for using the successful-efforts method of accounting	X		
FASB Statement No. 28	*Accounting for Sales with Leasebacks*		X	3(c)
FASB Statement No. 34	*Capitalization of Interest Cost*	X		
FASB Statement No. 44	*Accounting for Intangible Assets of Motor Carriers*		X	3–7
FASB Statement No. 50	*Financial Reporting in the Record and Music Industry*		X	11, 15
FASB Statement No. 51	*Financial Reporting by Cable Television Companies*			
	• Assets that are being depreciated (amortized)	X		
	• Other intangible assets		X	14
FASB Statement No. 60	*Accounting and Reporting by Insurance Enterprises*			
	• Real estate investments	X		
	• Deferred policy acquisition costs		X	32–37
FASB Statement No. 61	*Accounting for Title Plant*	X		

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FASB Statement No. 63	*Financial Reporting by Broadcasters*		X	7
FASB Statement No. 65	*Accounting for Certain Mortgage Banking Activities*		X	7
FASB Statement No. 67	*Accounting for Costs and Initial Rental Operations of Real Estate Projects*	X		
FASB Statement No. 71	*Accounting for the Effects of Certain Types of Regulation*			
	• Rate-regulated assets		X	9, 10 (as amended by this Statement)
	• Other assets	X		
FASB Statement No. 72	*Accounting for Certain Acquisitions of Banking or Thrift Institutions*		X	4
FASB Statement No. 86	*Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed*		X	10
FASB Statement No. 90	*Regulated Enterprises—Accounting for Abandonments and Disallowances of Plant Costs*		X	7
FASB Statement No. 97	*Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments*		X	25, 27
FASB Statement No. 101	*Regulated Enterprises—Accounting for the Discontinuation of Application of FASB Statement No. 71*	X		
FASB Statement No. 109	*Accounting for Income Taxes*		X	20–26
FASB Statement No. 114	*Accounting by Creditors for Impairment of a Loan*		X	8–16

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FASB Statement No. 115	*Accounting for Certain Investments in Debt and Equity Securities*		X	16
FASB Statement No. 140	*Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*		X	13, 63(g)
FASB Statement No. 142	*Goodwill and Other Intangible Assets*			
	• Goodwill and intangible assets not being amortized		X	17, 19–22
	• Intangible assets being amortized	X		

Appendix E: EXCERPTS FROM CONCEPTS STATEMENT 7

[Best understood in context of full Concepts Statement]

E1. Paragraph 23 of this Statement states that “a present value technique is often the best available valuation technique with which to estimate the fair value of a long-lived asset (asset group).” Paragraphs 39–54 and 75–88 of FASB Concepts Statement No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements,* discuss the use of present value techniques in measuring the fair value of an asset or a liability. Those paragraphs of Concepts Statement 7 follow.

The Components of a Present Value Measurement

39. Paragraph 23 describes the following elements that together capture the economic differences between various assets and liabilities:[7]

a. An estimate of the future cash flow, or in more complex cases, series of future cash flows at different times
b. Expectations about possible variations in the amount or timing of those cash flows
c. The time value of money, represented by the risk-free rate of interest
d. The price for bearing the uncertainty inherent in the asset or liability
e. Other, sometimes unidentifiable, factors including illiquidity and market

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imperfections.

40. This Statement contrasts two approaches to computing present value, either of which may be used to estimate the fair value of an asset or a liability, depending on the circumstances. In the expected cash flow approach discussed in this Statement, only the third factor listed in paragraph 39 (the time value of money, represented by the risk-free rate of interest) is included in the discount rate; the other factors cause adjustments in arriving at risk-adjusted expected cash flows. In a traditional approach to present value, adjustments for factors (b)–(e) described in paragraph 39 are embedded in the discount rate.

General Principles

41. The techniques used to estimate future cash flows and interest rates will vary from one situation to another depending on the circumstances surrounding the asset or liability in question. However, certain general principles govern any application of present value techniques in measuring assets or liabilities:

a. To the extent possible, estimated cash flows and interest rates should reflect assumptions about the future events and uncertainties that would be considered in deciding whether to acquire an asset or group of assets in an arm's-length transaction for cash.
b. Interest rates used to discount cash flows should reflect assumptions that are consistent with those inherent in the estimated cash flows. Otherwise, the effect of some assumptions will be double counted or ignored. For example, an interest rate of 12 percent might be applied to contractual cash flows of a loan. That rate reflects expectations about future defaults from loans with particular characteristics. That same 12 percent rate should not be used to discount expected cash flows because those cash flows already reflect assumptions about future defaults.
c. Estimated cash flows and interest rates should be free from both bias and factors unrelated to the asset, liability, or group of assets or liabilities in question. For example, deliberately understating estimated net cash flows to enhance the apparent future profitability of an asset introduces a bias into the measurement.
d. Estimated cash flows or interest rates should reflect the range of possible outcomes rather than a single most-likely, minimum, or maximum possible amount.

Traditional and Expected Cash Flow Approaches to Present Value

42. A present value measurement begins with a set of future cash flows, but existing accounting standards employ a variety of different approaches in

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specifying cash flow sets. Some applications of present value use contractual cash flows. When contractual cash flows are not available, some applications use an estimate of the single most-likely amount or **best estimate.**

43. Accounting applications of present value have traditionally used a single set of estimated cash flows and a single interest rate, often described as “the rate commensurate with the risk.” In effect, although not always by conscious design, the traditional approach assumes that a single interest rate convention can reflect all the expectations about the future cash flows and the appropriate risk premium. The Board expects that accountants will continue to use the traditional approach for some measurements. In some circumstances, a traditional approach is relatively easy to apply. For assets and liabilities with contractual cash flows, it is consistent with the manner in which marketplace participants describe assets and liabilities, as in “a 12 percent bond.”

44. The traditional approach is useful for many measurements, especially those in which comparable assets and liabilities can be observed in the marketplace. However, the Board found that the traditional approach does not provide the tools needed to address some complex measurement problems, including the measurement of nonfinancial assets and liabilities for which no market for the item or a comparable item exists. The traditional approach places most of the emphasis on selection of an interest rate. A proper search for “the rate commensurate with the risk” requires analysis of at least two items—one asset or liability that exists in the marketplace and has an observed interest rate and the asset or liability being measured. The appropriate rate of interest for the cash flows being measured must be inferred from the observable rate of interest in some other asset or liability and, to draw that inference, the characteristics of the cash flows must be similar to those of the asset being measured. Consequently, the measurer must do the following:

a. Identify the set of cash flows that will be discounted.
b. Identify another asset or liability in the marketplace that appears to have similar cash flow characteristics.
c. Compare the cash flow sets from the two items to ensure that they are similar. (For example, are both sets contractual cash flows, or is one contractual and the other an estimated cash flow?)
d. Evaluate whether there is an element in one item that is not present in the other. (For example, is one less liquid than the other?)
e. Evaluate whether both sets of cash flows are likely to behave (vary) in a similar fashion under changing economic conditions.

45. The Board found the expected cash flow approach to be a more effective measurement tool than the traditional approach in many situations. In developing

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a measurement, the expected cash flow approach uses all expectations about possible cash flows instead of the single most-likely cash flow. For example, a cash flow might be $100, $200, or $300 with probabilities of 10 percent, 60 percent, and 30 percent, respectively. The expected cash flow is $220.[8] The expected cash flow approach thus differs from the traditional approach by focusing on direct analysis of the cash flows in question and on more explicit statements of the assumptions used in the measurement.

46. The expected cash flow approach also allows use of present value techniques when the timing of cash flows is uncertain. For example, a cash flow of $1,000 may be received in 1 year, 2 years, or 3 years with probabilities of 10 percent, 60 percent, and 30 percent, respectively. The example below shows the computation of **expected present value** in that situation. Again, the expected present value of $892.36 differs from the traditional notion of a best estimate of $902.73 (the 60 percent probability) in this example.[9]

Present value of $1,000 in 1 year at 5%	$ 952.38	
Probability	10.00%	$ 95.24
Present value of $1,000 in 2 years at 5.25%	$ 902.73	
Probability	60.00%	541.64
Present value of $1,000 in 3 years at 5.50%	$ 851.61	
Probability	30.00%	255.48
Expected present value		$ 892.36

47. In the past, accounting standard setters have been reluctant to permit use of present value techniques beyond the narrow case of "contractual rights to receive money or contractual obligations to pay money on fixed or determinable dates." That phrase, which first appeared in accounting standards in paragraph 2 of Opinion 21, reflects the computational limitations of the traditional approach—a single set of cash flows that can be assigned to specific future dates. The Accounting Principles Board recognized that the amount of cash flows is almost always uncertain and incorporated that uncertainty in the interest rate. However, an interest rate in a traditional present value computation cannot reflect uncertainties in timing. A traditional present value computation, applied to the example above, would require a decision about which of the possible timings of cash flows to use and, accordingly, would not reflect the probabilities of other

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timings.

48. While many accountants do not routinely use the expected cash flow approach, expected cash flows are inherent in the techniques used in some accounting measurements, like pensions, other postretirement benefits, and some insurance obligations. They are currently allowed, but not required, when measuring the impairment of long-lived assets and estimating the fair value of financial instruments. The use of probabilities is an essential element of the expected cash flow approach, and one that may trouble some accountants. They may question whether assigning probabilities to highly subjective estimates suggests greater precision than, in fact, exists. However, the proper application of the traditional approach (as described in paragraph 44) requires the same estimates and subjectivity without providing the computational transparency of the expected cash flow approach.

49. Many estimates developed in current practice already incorporate the elements of expected cash flows informally. In addition, accountants often face the need to measure an asset or liability using limited information about the probabilities of possible cash flows. For example, an accountant might be confronted with the following situations:

a. The estimated amount falls somewhere between $50 and $250, but no amount in the range is more likely than any other amount. Based on that limited information, the estimated expected cash flow is $150 [(50 + 250)/2].
b. The estimated amount falls somewhere between $50 and $250, and the most likely amount is $100. However, the probabilities attached to each amount are unknown. Based on that limited information, the estimated expected cash flow is $133.33 [(50 + 100 + 250)/3].
c. The estimated amount will be $50 (10 percent probability), $250 (30 percent probability), or $100 (60 percent probability). Based on that limited information, the estimated expected cash flow is $140 [(50 × .10) + (250 × .30) + (100 × .60)].

50. Those familiar with statistical analysis may recognize the cases above as simple descriptions of (a) *uniform,* (b) *triangular,* and (c) *discrete* distributions.[10] In each case, the estimated expected cash flow is likely to provide a better estimate of fair value than the minimum, most likely, or maximum amount taken alone.

51. Like any accounting measurement, the application of an expected cash flow approach is subject to a cost-benefit constraint. In some cases, an entity may have access to considerable data and may be able to develop many cash flow scenarios. In other cases, an entity may not be able to develop more than general statements

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about the variability of cash flows without incurring considerable cost. The accounting problem is to balance the cost of obtaining additional information against the additional reliability that information will bring to the measurement. The Board recognizes that judgments about relative costs and benefits vary from one situation to the next and involve financial statement preparers, their auditors, and the needs of financial statement users.

52. Some maintain that expected cash flow techniques are inappropriate for measuring a single item or an item with a limited number of possible outcomes. They offer an example of an asset or liability with two possible outcomes: a 90 percent probability that the cash flow will be $10 and a 10 percent probability that the cash flow will be $1,000. They observe that the expected cash flow in that example is $109[11] and criticize that result as not representing either of the amounts that may ultimately be paid.

53. Assertions like the one just outlined reflect underlying disagreement with the measurement objective. If the objective is accumulation of costs to be incurred, expected cash flows may not produce a representationally faithful estimate of the expected cost. However, this Statement adopts fair value as the measurement objective. The fair value of the asset or liability in this example is not likely to be $10, even though that is the most likely cash flow. Instead, one would expect the fair value to be closer to $109 than to either $10 or $1,000. While this example is a difficult measurement situation, a measurement of $10 does not incorporate the uncertainty of the cash flow in the measurement of the asset or liability. Instead, the uncertain cash flow is presented as if it were a certain cash flow. No rational marketplace participant would sell an asset (or assume a liability) with these characteristics for $10.

54. In recent years, financial institutions and others have developed and implemented a variety of pricing tools designed to estimate the fair value of assets and liabilities. It is not possible here to describe all of the many (often proprietary) pricing models currently in use. However, those tools often build on concepts similar to those outlined in this Statement as well as other developments in modern finance, including option pricing and similar models. For example, the well-known Black-Scholes option pricing model uses the elements of a fair value measurement described in paragraph 23 as appropriate in estimating the fair value of an option. To the extent that a pricing model includes each of the elements of fair value, its use is consistent with this Statement.

Present Value in the Measurement of Liabilities

75. The concepts outlined in this Statement apply to liabilities as well as to assets. However, the measurement of liabilities sometimes involves problems different

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from those encountered in the measurement of assets and may require different techniques in arriving at fair value. When using present value techniques to estimate the fair value of a liability, the objective is to estimate the value of the assets required currently to (a) settle the liability with the holder or (b) transfer the liability to an entity of comparable credit standing.

76. To estimate the fair value of an entity's notes or bonds payable, accountants attempt to estimate the price at which other entities are willing to hold the entity's liabilities as assets. That process involves the same techniques and computational problems encountered in measuring assets. For example, the proceeds from a loan are the price that a lender paid to hold the borrower's promise of future cash flows as an asset. Similarly, the fair value of a bond payable is the price at which that security trades, as an asset, in the marketplace. As outlined in paragraphs 78–81, this estimate of fair value is consistent with the objective of liability measurement described in the preceding paragraph.

77. On the other hand, some liabilities are owed to a class of individuals who do not usually sell their rights as they might sell other assets. For example, entities often sell products with an accompanying warranty. Buyers of those products rarely have the ability or inclination to sell the warranty separately from the covered asset, but they own a warranty asset nonetheless. Some of an entity's liabilities, like an obligation for environmental cleanup, are not the assets of identifiable individuals. However, such liabilities are sometimes settled through assumption by a third party. In estimating the fair value of such liabilities accountants attempt to estimate the price that the entity would have to pay a third party to assume the liability.

Credit Standing and Liability Measurement

78. The most relevant measure of a liability always reflects the credit standing of the entity obligated to pay. Those who hold the entity's obligations as assets incorporate the entity's credit standing in determining the prices they are willing to pay. When an entity incurs a liability in exchange for cash, the role of its credit standing is easy to observe. An entity with a strong credit standing will receive more cash, relative to a fixed promise to pay, than an entity with a weak credit standing. For example, if 2 entities both promise to pay $500 in 5 years, the entity with a strong credit standing may receive about $374 in exchange for its promise (a 6 percent interest rate). The entity with a weak credit standing may receive about $284 in exchange for its promise (a 12 percent interest rate). Each entity initially records its respective liability at fair value, which is the amount of proceeds received—an amount that incorporates that entity's credit standing.

79. The effect of an entity's credit standing on the fair value of particular

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liabilities depends on the ability of the entity to pay and on liability provisions that protect holders. Liabilities that are guaranteed by governmental bodies (for example, many bank deposit liabilities in the United States) may pose little risk of default to the holder. Other liabilities may include sinking-fund requirements or significant collateral. All of those aspects must be considered in estimating the extent to which the entity's credit standing affects the fair value of its liabilities.

80. The role of the entity's credit standing in a settlement transaction is less direct but equally important. A settlement transaction involves three parties—the entity, the parties to whom it is obligated, and a third party. The price of the transaction will reflect the competing interests of each party. For example, suppose Entity A has an obligation to pay $500 to Entity B 3 years hence. Entity A has a poor credit rating and therefore borrows at a 12 percent interest rate.

a. In a settlement transaction, Entity B would never consent to replace Entity A with an entity of lower credit standing. All other things being equal, Entity B might consent to replace Entity A with a borrower of similar credit standing and would probably consent to replace Entity A with a more creditworthy entity.
b. Entity C has a good credit rating and therefore borrows at a 6 percent interest rate. It might willingly assume Entity A's obligation for $420 (the present value at 6 percent). Entity C has no incentive to assume the obligation for less (a higher interest rate) if it can borrow at 6 percent because it can receive $420 for an identical promise to pay $500.
c. However, if Entity A were to borrow the money to pay Entity C, it would have to promise $590 ($420 due in 3 years with accumulated interest at 12 percent).

81. Based on the admittedly simple case outlined above, the fair value of Entity A's liability should be approximately $356 (the present value of $500 in 3 years at 12 percent). The $420 price demanded by Entity C includes the fair value of Entity A's liability ($356) plus the price of an upgrade in the credit quality of the liability. There may be situations in which an entity might pay an additional amount to induce others to enter into a settlement transaction. Those cases are analogous to the purchase of a credit guarantee and, like the purchase of a guarantee, the additional amount represents a separate transaction rather than an element in the fair value of the entity's original liability.

82. The effect of an entity's credit standing on the measurement of its liabilities is usually captured in an adjustment to the interest rate, as illustrated above. This is similar to the traditional approach to incorporating risk and uncertainty in the measurement of assets and is well suited to liabilities with contractual cash flows. An expected cash flow approach may be more effective when measuring the

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effect of credit standing on other liabilities. For example, a liability may present the entity with a range of possible outflows, ranging from very low to very high amounts. There may be little chance of default if the amount is low, but a high chance of default if the amount is high. In situations like this, the effect of credit standing may be more effectively incorporated in the computation of expected cash flows.

83. The role of an entity's credit standing in the accounting measurement of its liabilities has been a controversial question among accountants. The entity's credit standing clearly affects the interest rate at which it borrows in the marketplace. The initial proceeds of a loan, therefore, always reflect the entity's credit standing at that time. Similarly, the price at which others buy and sell the entity's loan includes their assessment of the entity's ability to repay. The example in paragraph 80 demonstrates how the entity's credit standing would affect the price it would be required to pay to have another entity assume its liability. However, some have questioned whether an entity's financial statements should reflect the effect of its credit standing (or changes in credit standing).

84. Some suggest that the measurement objective for liabilities is fundamentally different from the measurement objective for assets. In their view, financial statement users are better served by liability measurements that focus on the entity's obligation. They suggest a measurement approach in which financial statements would portray the present value of an obligation such that two entities with the same obligation but different credit standing would report the same carrying amount. Some existing accounting pronouncements take this approach, most notably FASB Statements No. 87, *Employers' Accounting for Pensions,* and No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions.*

85. However, there is no convincing rationale for why the initial measurement of some liabilities would necessarily include the effect of credit standing (as in a loan for cash) while others might not (as in a warranty liability or similar item). Similarly, there is no rationale for why, in initial or fresh-start measurement, the recorded amount of a liability should reflect something other than the price that would exist in the marketplace. Consistent with its conclusions on fair value (refer to paragraph 30), the Board found no rationale for taking a different view in subsequent fresh-start measurements of an existing asset or liability than would pertain to measurements at initial recognition.

86. Some argue that changes in an entity's credit standing are not relevant to users of financial statements. In their view, a fresh-start measurement that reflects changes in credit standing produces accounting results that are confusing. If the

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measurement includes changes in credit standing, and an entity's credit standing declines, the fresh-start measurement of its liabilities declines. That decline in liabilities is accompanied by an increase in owners' equity, a result that they find counterintuitive. How, they ask, can a bad thing (declining credit standing) produce a good thing (increased owners' equity)?

87. Like all measurements at fair value, fresh-start measurement of liabilities can produce unfamiliar results when compared with reporting the liabilities on an amortized basis. A change in credit standing represents a change in the relative positions of the two classes of claimants (shareholders and creditors) to an entity's assets. If the credit standing diminishes, the fair value of creditors' claims diminishes. The amount of shareholders' residual claim to the entity's assets may appear to increase, but that increase probably is offset by losses that may have occasioned the decline in credit standing. Because shareholders usually cannot be called on to pay a corporation's liabilities, the amount of their residual claims approaches, and is limited by, zero. Thus, a change in the position of borrowers necessarily alters the position of shareholders, and vice versa.

88. The failure to include changes in credit standing in the measurement of a liability ignores economic differences between liabilities. Consider the case of an entity that has two classes of borrowing. Class One was transacted when the entity had a strong credit standing and a correspondingly low interest rate. Class Two is new and was transacted under the entity's current lower credit standing. Both classes trade in the marketplace based on the entity's current credit standing. If the two liabilities are subject to fresh-start measurement, failing to include changes in the entity's credit standing makes the classes of borrowings seem different—even though the marketplace evaluates the quality of their respective cash flows as similar to one another.

E2. Paragraph 24 of this Statement requires that estimates of future cash flows used in a present value technique be consistent with the objective of measuring fair value. Paragraph 23 of Concepts Statement 7 discusses the essential elements of a present value measurement. That paragraph of Concepts Statement 7 follows.

23. A present value measurement that fully captures the economic differences between the five assets described in paragraph 20 would necessarily include the following elements:

a. An estimate of the future cash flow, or in more complex cases, series of future cash flows at different times [2]
b. Expectations about possible variations in the amount or timing of those cash flows
c. The time value of money, represented by the risk-free rate of interest

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d. The price for bearing the uncertainty inherent in the asset or liability

e. Other, sometimes unidentifiable, factors including illiquidity and market imperfections.

E3. Paragraph 24 of this Statement also requires that estimates of future cash flows used in a present value technique incorporate assumptions that marketplace participants would use in their estimates of fair value whenever that information is available without undue cost and effort. Paragraph 32 of Concepts Statement 7 provides examples of circumstances in which an entity's cash flows (entity assumptions) might differ from the market cash flows (marketplace assumptions). That paragraph of Concepts Statement 7 follows.

> 32. An entity's best estimate of the present value of cash flows will not necessarily equal the fair value of those uncertain cash flows. There are several reasons why an entity might expect to realize or pay cash flows that differ from those expected by others in the marketplace. Those include:
>
> a. The entity's managers might intend different use or settlement than that anticipated by others. For example, they might intend to operate a property as a bowling alley, even though others in the marketplace consider its highest and best use to be a parking lot.
> b. The entity's managers may prefer to accept risk of a liability (like a product warranty) and manage it internally, rather than transferring that liability to another entity.
> c. The entity might hold special preferences, like tax or zoning variances, not available to others.
> d. The entity might hold information, trade secrets, or processes that allow it to realize (or avoid paying) cash flows that differ from others' expectations.
> e. The entity might be able to realize or pay amounts through use of internal resources. For example, an entity that manufactures materials used in particular processes acquires those materials at cost, rather than the market price charged to others. An entity that chooses to satisfy a liability with internal resources may avoid the markup or anticipated profit charged by outside contractors.

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Footnotes

FAS144, Footnote 1—This Statement applies to a business enterprise and a not-for-profit organization, each of which is referred to herein as an *entity*.

FAS144, Footnote 2—Accounting requirements for oil and gas properties that are accounted for using the full-cost method of accounting are prescribed by the Securities and Exchange Commission (Regulation S-X, Rule 4-10, "Financial Accounting and Reporting for Oil and Gas Producing Activities Pursuant to the Federal Securities Laws and the Energy Policy and Conservation Act of 1975").

FAS144, Footnote 3—In this Statement, all references to a *long-lived asset* refer to a long-lived asset covered by this Statement.

FAS144, Footnote 4—Examples of such liabilities include, but are not limited to, legal obligations that transfer with a long-lived asset, such as certain environmental obligations, and obligations that, for business reasons, a potential buyer would prefer to settle when assumed as part of a group, such as warranty obligations that relate to an acquired customer base.

FAS144, Footnote 5—This Statement amends only pronouncements of the FASB, the APB, and the Committee on Accounting Procedure. Conforming changes to other literature, including consensuses of the FASB's Emerging Issue Task Force and pronouncements of the American Institute of Certified Public Accountants, may be made subsequently.

FAS144, Footnote 6—The term *more likely than not* refers to a level of likelihood that is more than 50 percent.

FAS144, Footnote 7—Paragraphs 10 and 31–33 of Opinion 20 address the accounting for changes in estimates; paragraphs 23 and 24 of Opinion 20 address the accounting for changes in the method of depreciation. Paragraph 11 of Statement 142 addresses the determination of the useful life of an intangible asset.

FAS144, Footnote 8—The term *reporting unit* is defined in Statement 142 as the same level as or one level below an operating segment (as that term is defined in paragraph 10 of FASB Statement No. 131, *Disclosures about Segments of an Enterprise and Related Information*). Statement 142 requires that goodwill be tested for impairment at the reporting unit level.

FAS144, Footnote 9—Paragraph 29 of Statement 142 requires that goodwill be tested for impairment only after the carrying amounts of the other assets of the reporting unit, including the long-lived assets covered by this Statement, have been tested for impairment under other applicable accounting pronouncements.

FAS144, Footnote 10—The primary asset of an asset group therefore cannot be land or an

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intangible asset not being amortized.

FAS144, Footnote 11—FASB Statement No. 34, *Capitalization of Interest Cost,* states, “The capitalization period shall end when the asset is substantially complete and ready for its intended use” (paragraph 18).

FAS144, Footnote 12—The fair value of an asset or a disposal group refers to the amount at which the group as a whole could be bought or sold in a current single transaction. Therefore, the fair value of the group would not necessarily equate to the sum of the fair values of the individual assets and liabilities of the group.

FAS144, Footnote 13—Appendix E incorporates those paragraphs of Concepts Statement 7.

FAS144, Footnote 14—Concepts Statement 7 discusses the essential elements of a present value measurement (paragraph 23) and provides reasons why an entity’s estimates of cash flows might differ from those used by marketplace participants (paragraph 32). Appendix E incorporates those paragraphs.

FAS144, Footnote 15—A *component of an entity* is defined in paragraph 41 of this Statement as comprising operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity.

FAS144, Footnote 16—Because the continued use of a long-lived asset demonstrates the presence of service potential, only in unusual situations would the fair value of a long-lived asset to be abandoned be zero while it is being used. When a long-lived asset ceases to be used, the carrying amount of the asset should equal its salvage value, if any. The salvage value of the asset should not be reduced to an amount less than zero.

FAS144, Footnote 17—The provisions of this paragraph apply to those transactions described in paragraphs 21 and 23 of APB Opinion No. 29, *Accounting for Nonmonetary Transactions,* for which the accounting is based on the recorded amount (after reduction, if appropriate, for an indicated impairment of value) of a long-lived asset exchanged or distributed.

FAS144, Footnote 18—The term *probable* is used consistent with the meaning associated with it in paragraph 3(a) of FASB Statement No. 5, *Accounting for Contingencies,* and refers to a future sale that is “likely to occur.”

FAS144, Footnote 19—A *firm purchase commitment* is an agreement with an unrelated party, binding on both parties and usually legally enforceable, that (a) specifies all significant terms, including the price and timing of the transaction, and (b) includes a disincentive for nonperformance that is sufficiently large to make performance probable.

FAS144, Footnote 20—Refer to AICPA Statement on Auditing Standards No. 1, *Codification of*

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Auditing Standards and Procedures, Section 560, "Subsequent Events."

FAS144, Footnote 21—Because it is difficult to separate the benefit of hindsight when assessing conditions that existed at a prior date, it is important that judgments about those conditions, the need to test an asset for recoverability, and the application of a recoverability test be made and documented together with supporting evidence on a timely basis.

FAS144, Footnote 22—Expected future operating losses that marketplace participants would not similarly consider in their estimates of the fair value less cost to sell of a long-lived asset (disposal group) classified as held for sale shall not be indirectly recognized as part of an expected loss on the sale by reducing the carrying amount of the asset (disposal group) to an amount less than its current fair value less cost to sell.

FAS144, Footnote 23—Paragraph 39 of Statement 142 provides guidance for allocating goodwill to a lower-level asset group to be disposed of that is part of a reporting unit and that constitutes a business. Goodwill is not included in a lower-level asset group to be disposed of that is part of a reporting unit if it does not constitute a business.

FAS144, Footnote 24—This caption shall be modified appropriately when an entity reports an extraordinary item or the cumulative effect of a change in accounting principle or both in accordance with Opinion 20. If applicable, the presentation of per-share data will need similar modification.

FAS144, Footnote 25—Paragraph 3 of FASB Statement No. 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits,* defines *settlement* as "a transaction that (a) is an irrevocable action, (b) relieves the employer (or the plan) of primary responsibility for a pension benefit obligation, and (c) eliminates significant risks related to the obligation and the assets used to effect the settlement." A settlement is directly related to the disposal transaction if there is a demonstrated direct cause-and-effect relationship and the settlement occurs no later than one year following the disposal transaction, unless it is delayed by events or circumstances beyond an entity's control (refer to paragraph 31).

FAS144, Footnote 26—Paragraph 43 requires that when a component of an entity is reported as a discontinued operation, the income statements of prior periods be reclassified to report the results of operations of the component separately. This transition provision does not affect that requirement.

FAS144, Footnote 27—The alternatives of whether to sell or use an asset are not necessarily independent of each other. In many situations, after estimating the possible future cash flows relating to those potential courses of action, an entity might select the course of action that results in a significantly higher estimate of possible future cash flows. In that situation, the entity generally would use the estimates of possible future cash flows relating only to that course of action in computing future cash flows.

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FAS144, Footnote 28—Present value is the current measure of an estimated future cash inflow, discounted at an interest rate for the number of periods between today and the date of the estimated cash flow. The present value of *$X* in *n* periods in the future and discounted at interest of *i* per period is computed using the formula $X / (1 + i)^n$. Because all of the risks are considered in the estimates of cash flows, the entity discounts the expected cash flows for each year using the risk-free rate of interest. The risk-free rate of interest is the interest rate on monetary assets that are essentially risk free and that have maturity dates that coincide with the expected timing of the cash flow. In the United States, the risk-free rate is the rate for zero-coupon U.S. Treasury instruments. A yield curve for U.S. Treasury instruments may be used to determine the appropriate risk-free rates of interest.

FAS144, Footnote 29—In this example, a reliable estimate of the market risk premium is not available. Paragraph 62 of FASB Concepts Statement No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements,* explains:
An estimate of fair value should include the price that marketplace participants are able to receive for bearing the uncertainties in cash flows—the adjustment for risk—if the amount is identifiable, measurable, and significant. An arbitrary adjustment for risk, or one that cannot be evaluated by comparison to marketplace information, introduces an unjustified bias into the measurement. On the other hand, excluding a risk adjustment (if it is apparent that marketplace participants include one) would not produce a measurement that faithfully represents fair value. There are many techniques for estimating a risk adjustment, including matrix pricing, option-adjusted spread models, and fundamental analysis. However, in many cases a reliable estimate of the market risk premium may not be obtainable or the amount may be small relative to potential measurement error in the estimated cash flows. In such situations, the present value of expected cash flows, discounted at a risk-free rate of interest, may be the best available estimate of fair value in the circumstances.

FAS144, Footnote 30—If at the date of the sale-leaseback the fair value of the property is less than its undepreciated cost, a loss would be recognized immediately up to the amount of the difference between undepreciated cost and fair value in accordance with paragraph 3(c) of FASB Statement No. 28, *Accounting for Sales with Leasebacks*.

FAS144, Footnote 31—Paragraph 15 of Opinion 30 stated that "in the usual circumstance, it would be expected that the plan of disposal would be carried out within a period of one year from the measurement date. . . ."

FAS144, Footnote 32—The prohibition on retroactive application does not extend to the provisions of this Statement for reporting discontinued operations after this Statement is initially applied.

FAS144, Appendix E, Footnote 7—The effect of the entity's credit standing on the measurement

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of its liabilities is discussed in paragraphs 75–88.

FAS144, Appendix E, Footnote 8—($100 × .1) + ($200 × .6) + ($300 × .3) = $220. The traditional notion of a best estimate or most-likely amount in this example is $200.

FAS144, Apppendix E, Footnote 9—Interest rates usually vary with the length of time until settlement, a phenomenon described as the *yield curve*.

FAS144, Appendix E, Footnote 10—The uniform and triangular distributions are *continuous* distributions. For further information about these and other distributions, refer to:

- M. Evans, N. Hastings, and B. Peacock, *Statistical Distributions,* 2d ed. (New York: John Wiley & Sons, Inc., 1993).
- N. Johnson, S. Kotz, and N. Balakrishnan, *Continuous Univariate Distributions,* 2d ed., vol. 2. (New York: John Wiley & Sons, Inc., 1995).

FAS144, Appendix E, Footnote 11—($10 × .9) + ($1,000 × .1) = $109. For purposes of illustration, this example ignores the time value of money.

FAS144, Appendix E, CON7, Footnote 2—In complex measurements, such as measurements of liabilities settled by providing services, cash flow estimates necessarily include elements like overhead and profit margins inherent in the price of goods and services.

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