Proposed FSP FAS 144-d
Amending the Criteria for Reporting a Discontinued Operation
Comment Letter Summary

(As of April 3, 2009)

INTRODUCTION

1. The comment period on the Exposure Draft for the proposed FSP 144-d ended on January 23, 2009. This memorandum summarizes the significant comments and issues raised by respondents in their comment letters.

2. Twenty-two comment letters were received on the proposed FSP. The majority of respondents generally supported the principles of the proposed FSP. Most respondents provided significant comments on the proposed changes to FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets.

3. A breakdown of the types of respondents is noted below:

<table>
<thead>
<tr>
<th>Respondent type</th>
<th>Number of respondents</th>
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<tbody>
<tr>
<td>Auditor</td>
<td>6</td>
</tr>
<tr>
<td>Other</td>
<td>7</td>
</tr>
<tr>
<td>Preparer</td>
<td>6</td>
</tr>
<tr>
<td>Standard-setter</td>
<td>1</td>
</tr>
<tr>
<td>User</td>
<td>2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>22</strong></td>
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4. The respondents categorized as other were National Association of Real Estate Investment Trusts, American Accounting Association, Private Companies Practice Section of AICPA, Private Company Financial Reporting Committee, Institute of Management Accountants, one CPA state society, and an individual.
5. The respondents commented on the following issues:

1) Definition of a Discontinued Operation

2) Applicability to Entities Not Required to Apply FASB Statement No. 131, *Disclosures about Segments of an Enterprise and Related Information*

3) Disclosure Requirements

4) Effective Date and Transition

5) Other Comments.

**ISSUE 1: DEFINITION OF A DISCONTINUED OPERATION**

**Proposal**

6. The Exposure Draft proposed changing the definition of a discontinued operations so that it is a component of an entity that is:

   a. An *operating segment* (as that term is defined in FASB Statement No. 131, *Disclosures about Segments of an Enterprise and Related Information*) and either has been disposed of or is classified as held for sale, or

   b. A *business* (as that term is defined in FASB Statement No. 141 [revised 2007], *Business Combinations*) or a nonprofit activity that meets the criteria to be classified as held for sale on acquisition.

**Operating Segment**

7. Twenty one respondents commented on the definition of discontinued operations. Seven of these respondents were supportive of the proposed definition referring to *operating segments* (as defined in Statement 131). These respondents observed that the current definition of discontinued operations, as defined in FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, results in the reporting of too many disposals as discontinued operations, which reduces the usefulness of the financial statements. KPMG (CL #8) noted that an operating segment as defined by Statement 131 “is a well-understood concept and can provide a
basis for evaluating whether a component that either has been disposed of or qualifies as held-for-sale is a discontinued operation, without the need to define a new term in U.S. GAAP.” E&Y (CL #11) stated that “the link to an entity’s internal management approach and related reporting under Statement 131 will reduce the lack of consistency involved in determining what is or is not a component.”

8. Fourteen respondents disagreed with the reference to operating segments in the proposed definition of discontinued operations. These respondents expressed the following views:

(a) Five respondents expressed a view that the level of an operating segment was too high and four of these respondents suggested the definition of a discontinued operation should refer to a reporting unit, as defined in FASB Statement No. 142, *Goodwill and Other Intangible Assets*, instead. These respondents suggested the disposal of a component at which goodwill is tested for impairment should be an indicator of a strategic shift in operations and observed that it appears inconsistent that a reporting unit is significant enough to have a goodwill impairment, but the disposal of such a reporting unit would not be considered to represent a strategic shift in operations. PwC (CL #3) observed that “the level at which goodwill is tested for impairment reflects the way in which an entity manages its operations” and “because disposals at the level at which goodwill is tested for impairment in only an indicator, companies will still be able to apply judgment in determining whether there has been a strategic shift in operations, even if there is no recorded goodwill.” PwC (CL #3) also noted that determining the level at which goodwill is tested for impairment is generally well understood by preparers in the U.S. and internationally.

(b) Four respondents expressed a view that the level of an operating segment was too low for reporting discontinued operations. NYSSCPA (CL #1) suggested the proposed FSP include quantitative thresholds found in paragraphs 18-24 of Statement 131. The rest of these respondents observed that in the real estate
industry, each operating property often is an operating segment; however, disposal of a single property does not necessarily indicate a strategic shift in operations. NAREIT (CL #7) and ForestCity (CL #9) recommended the proposed definition of a discontinued operation refer to reportable segment or a significant operating segment (an operating segment the assets or revenues of which exceed minimum thresholds, which could be similar to those provided in paragraph 13 of IFRS 8, *Operating Segments*), and KPMG (CL #8) urged the Board “to reach out to businesses that may have this type of operating structure to consider whether such reporting is consistent with the objective that a discontinued operation should represent a strategic shift for the entity.”

(c) Grant Thornton (CL #16) observed that a chief operating decision-maker (CODM) “may choose to review [information] at an extremely detailed level, which could result in the identification of numerous operating segments. This in turn could result in the disposal of an operating segment being identified as a discontinued operation despite the fact that the disposal does not constitute a strategic shift in the entity’s operations.”

(d) German Accounting Standards Board (CL #22) suggested that a major component of an entity (*component* as defined in IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*, and Statement 144) would be a better basis for defining discontinued operations. This respondent further suggested that quantitative and qualitative factors should be considered in determining whether a component of an entity is major, such as dissimilarity of the disposed component in comparison to the remaining components.

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1 IFRS 8, paragraph 13 states “An entity shall report separately information about an operating segment that meets any of the following quantitative thresholds:
   a. Its reported revenue, including both sales to external customers and intersegment sales or transfers, is 10 per cent or more of the combined revenue, internal and external, of all operating segments
   b. The absolute amount of its reported profit or loss is 10 per cent or more of the greater, in absolute amount, of (i) the combined reported profit of all operating segments that did not report a loss and (ii) the combined reported loss of all operating segments that reported a loss
   c. Its assets are 10 per cent or more of the combined assets of all operating segments”
(e) KPMG (CL #8) and PwC (CL #3) expressed a view that the definition of a discontinued operation currently contained in IFRS 5 is consistent with the objective of reporting a strategic shift in operations and should be retained, with some improvements, such as clarifying whether the current definition includes only major geographic areas or all geographic areas.

(f) Deloitte & Touche (CL #12) observed that the proposed definition of a discontinued operation may fail to capture certain disposals by an entity that follows a matrix form of organization. If the CODM regularly reviews the operating results by product or service line, disposal of the geographical component would not be reported as a discontinued operation; even if this disposal represented a strategic shift in the entity’s operations.

9. KPMG (CL #8) suggested the Boards clarify the following issues that might arise in practice:

1) “Whether the disposal that includes more than one operating segment, for example a disposition of an entire operating segment along with operating assets of a second operating segment, would be reported as a discontinued operation; and if so, would it include only the operating segment disposed of in its entirety or would the discontinued operation include the entire disposition?”

2) “Whether a change in investment structure without elimination of an operating segment is intended to be reported as a discontinued operation. For example, if an entity ceases to have a controlling interest in a subsidiary while retaining a non-controlling interest that continues to be an operating segment, would discontinued operations be reported?”

10. Pfizer (CL #21) mentioned it is unclear as to whether the disposal that includes substantially all of one operating segment and various assets and liabilities of two other operating segments would meet the definition of a discontinued operation under this proposed FSP and how would it be reported. For example, what would be included in discontinued operations and what would be included in continuing operations.
11. NAREIT (CL #7) observed that significant diversity exists in application of Statement 131. Consequently, defining a discontinued operation as an operating segment would result in diversity in reporting discontinued operations and reduce comparability of financial statements. “The Board could, as part of this project, help to alleviate the diversity in interpretation of the definition of an operating segment by clarifying that the fact that the CODM could review financial information about a component on an exception basis does not result in that component being deemed an operating segment.”

12. AAA (CL #14) observed that only 40 percent of publicly-traded firms in the U.S. disclose more than one reportable segment, and that, “assuming that many of these firms also have only one operating segment, separate reporting of discontinued operations would not occur for these firms.”

13. PCFRC (CL #4) and PCPS of AICPA (CL #15) recommended the proposed definition of discontinued operation include a description of an operating segment, rather than reference to Statement 131, as private and not-for-profit entities are not familiar with that Standard.

14. KPMG (CL #8) asked the Board to clarify that the review of a component’s operating information by the entity’s CODM in order to make decisions about the disposal of that component does not cause the component to become an operating segment, if the component otherwise was not an operating segment.

**Strategic Shift in Operations**

15. Nine respondents supported the view expressed in paragraph A2 of Appendix A to the Exposure Draft, Background Information and Basis for Conclusions, that “a disposal activity should be presented as a discontinued operation only when an entity has made a strategic shift in its operations”. These respondents also stated that management should be allowed flexibility in determining whether a particular disposal represents a strategic shift in an entity’s operations. KPMG (CL #8) observed that “using a management approach to determine discontinued operations is
appropriate since it is management that establishes the strategic objectives of the entity.”

16. Grant Thornton (CL #16) suggested the Board provide a description of factors for management to consider in determining whether a disposal constitutes a strategic shift in the entity’s operations. This respondent also suggested the Board indicate that there is a rebuttable presumption that the disposal of an operating segment represents a strategic shift in operations.

17. The German Accounting Standards Board (CL #22) disagreed with limiting the reporting of discontinued operations to strategic shifts in operations. This respondent expressed the view that users may find the information on major disposals useful, even if such disposals do not represent strategic shifts in operations.

**Business Held for Sale on Acquisition**

18. Verizon (CL #6) disagreed with the proposed definition of a discontinued operation referring to a *business* (as defined in Statement 141 (R)). This respondent stated that the definition of a business under Statement 141 (R) is too broad and expressed a concern that using the term in the proposed definition may lead to reporting more discontinued operations. The respondent also stated that the cost of obtaining necessary information would exceed the benefits and recommended the term *business* should be replaced with the term *operating segment* in part (b) of the proposed definition of a discontinued operation.

**Elimination of Criteria Contained in Paragraph 42 of Statement 144**

19. Five respondents commented on the proposed elimination of criteria for determining discontinued operations contained in paragraph 42 of Statement 144, namely that (a) the operations and cash flows of the component has been (or will be) eliminated from the ongoing operations of the entity and (b) the entity will not have any significant continuing involvement in the operations of the component after the disposal transaction. Three respondents supported the elimination of the continuing involvement and cash flows criteria and two respondents objected the proposal.
20. IMA (CL #10) who objected to the proposal stated that “it is inconsistent to report an operating segment as "discontinued" while the enterprise continues to include the operation's direct cash flows in its consolidated financial statements or to report an operating segment as "discontinued" while management is still involved in its day-to-day operations.” E&Y (CL #11) supported eliminating the continuing involvement criteria but objected to the elimination of the continuing operations and cash flow criteria, noting that “the resulting discontinued operations presentation may not provide users with information that is relevant in assessing the ongoing ability of the entity to generate cash flows. For example, in certain situations the periods after a disposal transaction would include significant increases in revenues and cash flows in continuing operations due to the continuing relationship with the disposed operating segment.”

21. McGladrey & Pullen (CL #20) observed that continuing involvement and cash flows are important criteria in determining discontinued operations and requested that the Board provide additional rationale for eliminating these criteria. This respondent further observed that classification of disposals with significant continuing involvement and cash flows as discontinued operations may impair comparability of financial statements and further guidance may be necessary to help preparers determine what amounts need to be reclassified. For example, assume a situation in which an operating segment of an entity sells services solely to other segments of that entity. The operating segment is then disposed and continues to provide those same services to the enterprise. In such a situation, the “costs” of the former segment would be included in continuing operations for the period after disposal, but not before.

22. E&Y (CL #11) stated that at a minimum, the Board should provide guidance on presenting transactions between a disposed component and the selling entity and require disclosure of significant continuing involvement and future cash flows, similar to the requirements currently required by paragraph 17 of Emerging Issues Task Force (EITF) Issue No. 03-13, “Applying the Conditions of Paragraph 42 of
FASB Statement No. 144 in Determining Whether to Report Discontinued Operations.”

**ISSUE 2: APPLICABILITY TO ENTITIES NOT REQUIRED TO APPLY STATEMENT 131**

23. In the proposed FSP, the Board proposed that an entity should determine whether the component of an entity meets the definition of an operating segment regardless of whether it is required to apply Statement 131.

24. The majority of the respondents agreed with the Board’s proposal. The overarching response by these respondents was these entities are currently required to identify their operating segments under Statement 142 as part of the process of allocating goodwill to reporting units.

25. IMA (CL #10) agreed with the Board’s proposal recommended that the Board should make it clear that there is no need for an entity (that is not required to apply Statement 131) to compile any new information prior to the disposal to determine whether a component is an operating segment. Otherwise, an entity may feel compelled to adopt Statement 131 (at least on a pro forma basis) so it can identify its operating segments in case of a disposal.

26. McGladrey & Pullen (CL #20) who disagreed with the Board’s proposal noted certain entities that have not been required to apply Statement 131 may encounter difficulties in applying the proposed definition. The process and information used by management (of nonpublic and not-for-profit entities) to review the operating results

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2 The following information should be disclosed in the notes to the financial statements for each discontinued operation that generates future cash flows: (a) the nature of the activities that give rise to continuing future cash flows, (b) the period of time continuing cash flows are expected to be generated, and (c) the principal factors used to conclude that the expected continuing cash flows are not direct cash flows of the disposed component. Additionally, for each discontinued operation in which the ongoing entity will engage in a “continuation of activities” with the disposed component after its disposal for which the amounts presented in continuing operations after the disposal transaction include a continuation of revenues and expenses that were intercompany transactions (eliminated in consolidated financial statements) before the disposal transaction, intercompany amounts before the disposal transaction, intercompany amounts before the disposal transaction should be disclosed for all periods presented. The types of continuing involvement, if any, that the entity will have after the disposal transaction should be disclosed. That information should be disclosed in the period in which operations are initially classified as discontinued.
and allocate resources are often more informal than in public entities and may not be well documented. Additionally, nonpublic business entities that do not report any goodwill may not be familiar with Statement 142 which requires entities to consider Statement 131 to determine reporting units.

27. KPMG (CL #8) noted that paragraph 118 of Statement 131 indicates that the FASB decided to exclude not-for-profit organizations from the scope of that Statement, in part, because “there are likely to be unique characteristics of some of those entities… which the Board has not studied.” This respondent suggested that the Board examine the potential unique issues involved in identifying operating segments for not-for-profit entities before requiring those entities apply the operating segment concept.

ISSUE 3: DISCLOSURE REQUIREMENTS

Proposal

28. The proposed FSP would require three types of disclosures:

a. Those related to a long-lived asset (disposal group) that has either been sold or is classified as held for sale

b. Those related to a discontinued operation

c. Those related to a component of an entity that has either been disposed of or is classified as held for sale regardless of whether it is reported in the income statement as a discontinued operation or within continuing operations.

Disclosure of Components of an Entity that has been either Disposed of or Classified as Held for Sale

29. Nine respondents stated that the disclosure requirements should relate only to discontinued operations and not for components of an entity that are reported within continuing operations that have been either disposed of or classified as held for sale. These respondents argued that, if the information does not warrant presentation on the face of the financial statements, it should not be required in the notes. PwC (CL #3)
stated the framework for disclosing disposal activities should be consistent with the framework for reporting discontinued operations. The staff believes that users would likely benefit from a level of disclosure for discontinued operations that mirrors the level of reporting in the primary set of financial statements. E&Y (CL #11), who was of the same view, stated it appears contradictory that, on one side, the FASB intends to reduce the number of discontinued operations, but on the other side, proposes additional disclosures in the notes for discontinued activities that are not significant enough to be presented as a discontinued on the face of the income statement.

30. Tyco (CL #13) recommended the proposed disclosures for components of an entity that are reported within continuing operations should be structured similarly to those prescribed in Statement 141(R) paragraphs 68-69. The same respondent also stated that if the Board’s proposed disclosure requirements are adopted, the disclosure of major cash flows for disposals that are reported within continuing operations should be made optional.

31. IMA (CL #10) stated that proposed disclosures for components of an entity that are reported within continuing operations should consider limiting this information to significant disposals using similar measures of significance as contained in Statement 131.

32. McGladrey & Pullen (CL #20) suggested that the disclosure requirements for all components of an entity regardless of whether it is reported in the income statement as discontinued operations or within continuing operations should align with Statement 131 as entities may be required to covert the internal reporting to GAAP and make allocations that were not made previously.

33. NYSSCPA (CL #1) requested that examples should be included because the requirements are relatively difficult to understand without reading paragraphs A5 and A6.
Disclosure Exemptions for Businesses that are Classified as Held for Sale on Acquisition

34. In the proposed FSP, the Board proposed that businesses that meet the criteria to be classified as held for sale on acquisition should be provided disclosure exemptions. All respondents agreed with the Board’s proposal.

Income Tax Expense or Benefit not calculated within Continuing Operations

35. In the proposed FSP, the Board proposed that under the disclosure requirements, income tax expense or benefit does not have to be calculated and disclosed for components of an entity that are reported within continuing operations and that have been disposed of or are classified as held for sale. The majority of the respondents agreed with the Board’s proposal. Two respondents disagreed with the Board’s proposal. Tyco (CL #13) disagreed, stating that if companies are required to disclose major financial statement line item impacts, the related tax impact should be disclosed as well. Deloitte & Touche (CL #12) noted that if it is determined that users of the financial statements want detailed information at the component of an entity level, then information regarding income tax expense or benefit would appear to be useful.

Guidance on Aggregation

36. A few respondents asked the Board to clarify whether disclosures are permitted on an aggregate basis for all disposed components, or whether it is required for all individual components. Of these respondents, E&Y (CL #11) asked the Board to clarify, if aggregation is permitted, whether components classified in discontinued and continuing operations could be aggregated.