# AFA 300: Held for Sale Assets

**TRAIN TO LEARN EFFECTIVELY: TIP SHEETS**

## What are Held for Sale Assets?

Sometimes a company decides to make significant changes in the way it operates. When a company plans asset disposals to improve its operations, there are generally 2 options: abandonment and held for sale assets. There are many reasons for making changes; for example, to cut costs and restore profitability, to make the company's production more efficient, or to meet competitive threats. For accounting purposes, we can identify two different scenarios for asset disposals:

(1) Disposing of individual noncurrent assets; or
(2) Disposing of several assets as a group.

Under IFRS, assets put up for sale are reclassified from *noncurrent* to *current* on the Statement of Financial Position. They are classified as current assets because the intent is to sell them rather than hold them for productive use.

A company may decide to put an individual asset, or series of individual assets, on the market for sale. Often, a company will put one or more individual noncurrent assets, such as a warehouse building, up for sale. For the purposes of this tip sheet, we will be looking at **Scenario #1**, putting **ONE** individual asset on the market for sale. The asset has been classified as a capital asset, but once it is removed from productive use and put on the market, it is subjected to an impairment test and written down to a recoverable amount, if that amount is lower than carrying value. The asset may be classified as a **held for sale asset,** if it meets the necessary conditions. A held for sale asset is shown on the Statement of Financial Position as a current asset. When the asset is reclassified, depreciation or amortization ceases because it is no longer being held as a productive asset with future benefit beyond its recoverable amount.

## Conditions of *Held for Sale* classification for a noncurrent asset

Before an asset can be classified as "held for sale", **BOTH** of the following conditions must be satisfied:

(1) The asset is available for immediate sale in its present condition. This does not mean that the business must stop the use of the asset, but rather if a customer comes up and says that they would like the asset, the business would want to sell it immediately;

**and**

(2) The asset's sale is highly probable, which means **ALL 5** requirements and criteria are met:

(a) The price being asked is reasonable, relative to the asset's current condition and fair value. This means the price is equal to its fair market value or lower;
(b) An active program to find, seek and search for a buyer must have been started;
(c) Management must be committed to selling the asset;
(d) It is unlikely that the offer to sell will be withdrawn or that the terms of the offer will be changed significantly, such as the price; **and**
(e) The sale is expected to take place within one year of the asset's being reclassified as "held for sale".

## Steps to classify asset as Held for Sale

Here are the steps to record a noncurrent asset as held for sale.

1. A noncurrent asset intended for sale must first be "remeasured" to the lower of its carrying value and its fair value less cost to sell.
2. After remeasurement, the asset can be declared "held for sale" and classified as a current asset, provided the five conditions listed above are satisfied.
3. Depreciation stops

In general, when any noncurrent asset is written down, the loss is reported as part of that period's net income. If the recoverable amount of the written down asset increases later, the increase in value is reported in profit or loss as a gain. When a company writes up the asset, the writeup is limited to the extent of any prior writedowns, including any impairments recorded prior to the asset's classification as a held for sale. It is important to note that assets are only written down when classified as held for sale, they are not written up to fair value if that is higher than the carrying amount.

## Declassification as Held for Sale Asset

Declassification as held for sale occurs when a noncurrent asset no longer satisfies the held for sale criteria. The company may have changed its mind about selling the asset; or market conditions may have changed so that the sale is no longer "highly probable". If that happens, here are the steps for the declassification:

(1) Must restore asset to its original noncurrent classification; **and**
(2) Revised amount is *lower* of:
 (i) Its net recoverable amount at the date of decision not to sell; or
 (ii) What its carrying amount would have been if the reclassification had not taken place and depreciation had continued

## Example 1:

Suppose that in early September 2014, near the end of the company's third quarter, Finagle Ltd. (a public company) completes installation of new package handling equipment in its distribution centre in downtown Montreal. The old equipment is still serviceable but is not as efficient as Finagle's new equipment.

Finagle contacts a major industrial resale firm and requests that the firm put the old equipment on the market for sale. The resale firm believes that it can get a quick sale, because many start-up companies in the Montreal area can use serviceable low-cost package handling equipment. Finagle therefore wishes to reclassify the equipment as held for sale.

The original cost of the equipment was $500,000; accumulated depreciation to the date of disuse (September 2014) was $240,000, leaving a carrying value of $260,000. The resale firm estimates that the old equipment is worth about $250,000 on the resale market; the firm will charge 20% commission on the sale spruce. The commission is the "cost to sell". Therefore, the recoverable amount (fair value less cost to sell) is $200,000 ($250,000 x 80%). The process is as follows:

1. The accumulated depreciation to the date of abandonment will be offset against the original cost of $500,000, leaving a net book value of $260,000 in the equipment account

| | | | |
|---|---|---|---|
| DR | Accumulated depreciation | 240,000 | |
| | CR Equipment | | 240,000 |

2. Finagle will "remeasure" the old equipment by writing it down to $200,000, reporting the $60,000 loss in profit or loss

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|---|---|---|---|
| DR | Loss on equipment held for sale | 60,000 | |
| | CR Equipment | | 60,000 |

3. Finagle then reclassifies the equipment from a noncurrent asset to current asset

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|---|---|---|---|
| DR | Equipment held for sale (current asset) | 200,000 | |
| | CR Equipment (noncurrent asset) | | 200,000 |

This series of entries will (1) reclassify the equipment as a current asset at its net recoverable amount and (2) record the $60,000 writedown as a loss to be included in net income. These entries can be combined into a single compound entry.

| | | | |
|---|---|---|---|
| DR | Equipment held for sale (current asset) | 200,000 | |
| DR | Accumulated depreciation | 240,000 | |
| DR | Loss on equipment held for sale | 60,000 | |
| | CR Equipment (noncurrent asset) | | 500,000 |

In December 2014, a sudden economic crisis has the effect of freezing the capital market; few new companies are able to get going. The resale firm advises Finagle that the equipment can now be sold for no more than $180,000. Consequently, Finagle writes down the equipment to the new lower estimated recoverable amount: $180,000 x 80% = $144,000. The loss of $56,000 ($200,000 - $144,000) is reported in Finagle's income statement with the following entry:

| | | | |
|---|---|---|---|
| DR | Loss on equipment held for sale | 56,000 | |
| | CR Equipment held for sale | | 56,000 |

In March 2015, the Canadian financial market begins to recover as the nation finds that the banking and financial system is still sound. The resale firm now begins aggressively marketing the equipment, asking a selling price of $260,000. For Finagle's first quarter financial reports, under IFRS the company remeasures the equipment and writes it up to $208,000, disclosing the gain as a component of profit or loss.

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|---|---|---|
| DR Equipment held for sale | 64,000 | |
| CR Gain (recovery) on equipment held for sale | | 64,000 |

In July 2015, the beginning of Finagle's third quarter, the asset is sold for $270,000. The resale firm collects its 20% commission and remits the remaining $216,000 to Finagle. Since the carrying value at the end of the second quarter was $208,000, the company recognizes a gain of $8,000.

| | | |
|---|---|---|
| DR Cash | 216,000 | |
| CR Equipment held for sale | | 208,000 |
| CR Gain on sale of equipment | | 8,000 |

In this example, Finagle met all five conditions of reclassifying the asset as held for sale:

- The asking price is realistic, according to expert opinion (the resale firm);
- An active program of sale was started;
- Management is committed to selling the asset;
- It is unlikely that management will withdraw or significantly change the terms of the offer to sell; and
- There is a reasonable expectation of selling it within a year.

Even though it took longer than a year to sell the equipment, the cause of delay (a general economic financial crisis) was beyond the control of management.

## Example 2:

**Example 2:**

On September 13, 2021, Nitish Corp's board of directors moved the company's operations into a newly constructed building and declared its old building available for sale. The original cost of the old building was $20 million, it was 40% depreciated. Other information is as follows:

a) On September 15, a professional appraisal of the old building estimated its value as $10 million
b) On September 24, Nitish engaged a commercial property developer to place the building on the market for $10 million. Despite some softness in the market, the developer expects to be able to sell the building within the next 9 months. The developer charges a commission of 6% on final sale.
c) By December 31, the commercial real estate market had "softened" considerably. Although the developer held the official asking price at $10 million, Nitish and the developer agreed they would consider offers as low as $8.5 million.
d) Despite receiving several "lowball" offers from prospective buyers over the first two months of 2022, Nitish's management did not accept any of the offers.
e) By March 31 2022, the end of the Nitish's first reporting quarter, the market had improved considerably. The developer relisted the property at $11.5 million, its newly appraised value.
f) On April 27, 2022, Nitish's board accepted an offer of $11.7 million.

**Required:** Prepare the appropriate general journal entries to record the information above.

**Step 1.** Does the building classify as held for sale?

1. Asset is available for immediate sale in its current condition - MET
   - old building is empty and available immediately.
   - we have no intention of renovating or making any changes
2. Sale is highly probable if meet the following:
   a. price is reasonable - MET
   - a professional appraiser estimated a value of $10 million and we put it for sale for that price, which is reasonable
   b. active program to find a buyer - MET
   - engaged a commercial property developer and they put it on the market
   c. management is committed to selling - MET
   - this is an old building which management is no longer using, so they are committed to get rid of it
   d. unlikely the offer will be withdrawn or changes - MET
   - offer is with the developer and management wants to get rid of this empty building so unlikely withdraw or change terms
   e. sale is expected to take place in upcoming 12 months - MET
   - developer feels they can sell the building in next 9 months

**YES,** all the criteria are MET and therefore this building is a held for sale asset.

**NOTE:** if not met, then continue to depreciation and report as part of PPE.

**Step 2.** Record the depreciation up to the date that the asset becomes held for sale.

In this case, there is no information so omit and skip this step.

**Step 3.** Eliminate the accumulated depreciation account by closing it to the asset account. 20000000 x 40% = 8000000

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|---|---|---|---|
| 13-Sep-21 | DR Accumulated Depreciation, Building | 8000000 | |
| | CR Building | | 8000000 |

**Step 4.** Remeasure the asset by writing it down to its fair value less cost to sell. Since the commission paid to the developer who sells it is 6%, we have to recognize 94% of the selling price.

Fair value less cost to sell = 10000000*(100%-6%) = 9400000
Loss = 12000000 (net book value) - 9400000 = 2600000

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|---|---|---|---|
| 13-Sep-21 | DR Loss on asset held for sale | 2600000 | |
| | CR Building | | 2600000 |

**Step 5.** At every reporting period, remeasure the fair value less cost to sell. If it is lower, write the asset down (no limit to writedown, up to 0). If it is higher, then write the asset up BUT only by the same amount as it has been written down by. We wrote it down by 2,600,000 so we can write it up to a MAX amount of 2,600,000.

31-Dec-21 Fair value less cost to sell now: 85000000*(100%-6%) = 7990000
Loss = 9400000 - 7990000 = 141000

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|---|---|---|---|
| 31-Dec-21 | DR Loss on asset held for sale | 141000 | |
| | CR Held for Sale Asset | | 141000 |

**Step 6.** Remeasure at every reporting period.

31-Mar-22 We have written it down by a total of 4010000 - 2820000 = 1190000
Fair value less cost to sell now: 11500000*(100%-6%) = 10810000

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|---|---|---|---|
| 31-Mar-22 | DR Held for sale asset | 2820000 | |
| | CR Gain (recovery) on held for sale asset | | 2820000 |

**Step 7.** Record the sale. If selling price is greater than > the carrying amount, record a gain. Otherwise if the selling price is less than < the carrying amount, record a loss.

Amount receivable is equal to fair value less cost to sell = 11700000*(100%-6%) = 10998000

| | | | | |
|---|---|---|---|---|
| 27-Apr-22 | DR Accounts receivable | 10998000 | | |
| | CR Gain on disposal of held for sale asset | | 188000 | Income statement as other revenues and gains |
| | CR Held for sale asset | | 10810000 | |