

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 08-07: EITF 07-6: Accounting for the Sale of Real Estate Subject to the Requirements of FASB Statement No. 66 When the Agreement Includes a Buy-Sell Clause

ISSUE NULLIFIED BY SSAP NO. 40

INT 08-07 Dates Discussed

May 31, 2008; September 22, 2008

INT 08-07 References

SSAP No. 40—Real Estate Investments (SSAP No. 40)

SSAP No. 77—Real Estate Sales, An Amendment to SSAP No. 40, Real Estate Investments

INT 08-07 Issue

1. *EITF 07-6: Accounting for the Sale of Real Estate Subject to the Requirements of FASB Statement No. 66 When the Agreement Includes a Buy-Sell Clause* (EITF 07-6), issued in December 2007, clarifies whether a buy-sell clause is a prohibited form of continuing involvement that would preclude partial sales treatment under *FASB Statement No. 66: Accounting for Sales of Real Estate* (FAS 66).

2. Pursuant to EITF 07-6, a buy-sell clause is a contractual term in an investor agreement of a jointly-owned entity that gives both of the investors of the jointly owned entity the ability to offer to buy the other investor's interest. When an offer is made pursuant to the buy-sell clause, the recipient of the offer can elect to sell its interest for the offered amount or buy the offeror's interest at the offered amount. Generally, once an offer is made, the offeror is contractually required to buy the other investor's interest or sell its interest at the offered amount depending on the other investor's election.

3. As noted within EITF 07-6:

3. Statement 66 includes guidance on the accounting for sales of real estate and criteria that must be met to recognize profit by the full accrual method. One of those criteria is that the seller has transferred to the buyer the usual risks and rewards of ownership in a transaction that is in substance a sale and does not have a substantial continuing involvement with the property. For the purpose of this Issue, the seller is the investor who sold the real estate to the jointly owned entity. The buyer is the other investor in the jointly owned entity. If the seller has complied with all the provisions of Statement 66 to use the full accrual method but retains an equity interest in the real estate or has an equity interest in the buyer, Statement 66 requires the seller to account for the sale as a partial sale.

4. Paragraph 26 of Statement 66 indicates that if the seller has an obligation to repurchase the real estate or if the terms of the transaction allow the buyer to compel the seller or give an option to the seller to repurchase the real estate, the seller is considered to have a prohibited form of continuing involvement that would preclude profit recognition. Some have questioned whether a buy-sell clause would be considered a prohibited form of continuing involvement under paragraph 26 of Statement 66 and therefore preclude partial sale and profit recognition.

4. Per EITF 07-6, the issue is whether a buy-sell clause would be considered a prohibited form of continuing involvement under paragraph 26 of FAS 66 and therefore preclude partial sale and profit recognition.

INT 08-07 Discussion

5. EITF 07-6 provides guidance that a buy-sell clause, in and of itself, does not constitute a prohibited form of continuing involvement that would require partial sales treatment under FAS 66. However, EITF 07-6 provides guidance promoting judgment and consideration of all facts and circumstances at the time the real estate is sold. As noted in EITF 07-6, if the buy-sell clause provides the buyer an in-substance option to put their interest in the jointly owned entity back to the seller, or gives the seller an in-substance option to acquire the buyer's interest in the jointly owned entity (thereby reacquiring the real estate), the buy-sell agreement may be considered to reflect a substantive continuing involvement with the property after the sale by the seller and thus prevent profit from being recognized under the full accrual method.

6. As the EITF consensus requires evaluation of all relevant facts and circumstances pertaining to a buy-sell clause as part of determining whether continuing involvement exists and this evaluation complies with the statutory accounting principle concept of recognition, the Working Group issued a consensus to adopt the consensus reached in EITF 07-6. Thus, a buy-sell clause should be evaluated for substance of the options in assessing continuing involvement with property after a sale pursuant to paragraph 18 of SSAP No. 40. As illustrated in SSAP No. 40, profit for real estate property sold in which a substantial continuing involvement exists shall not be recognized by the full accrual method.

INT 08-07 Status

7. No further discussion planned.