EITF ABSTRACTS

Issue No. 07-6

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

Dates Discussed: September 11, 2007; November 29, 2007

Reference: FASB Statement No. 66, Accounting for Sales of Real Estate

Objective

1. The objective of this Issue is to clarify whether a buy-sell clause is a prohibited form of continuing involvement that would preclude partial sales treatment under Statement 66.

All paragraphs in this Issue have equal authority.

Paragraphs in bold set out the main principles.

Background

2. When investors enter into an arrangement to create a jointly owned entity and one investor sells real estate to that entity, a buy-sell clause often is included in the agreement between the investors. The buy-sell clause is a contractual term that gives both of the investors of the jointly owned entity the ability to offer to buy the other investor's interest. In some cases, the buy-sell clause may be executed at any time or in other cases only at some specified future date. 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

Superseded by the FASB Accounting Standards Codification on July 1, 2009
offered amount depending on the other investor's election. A buy-sell clause can specify that the offer be at fair value, at a contractually specified amount, or at an amount determined by the offeror, which is the most common type.

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.
Scope

5. **This Issue applies to a real estate sale transaction subject to the requirements of Statement 66 when the transaction includes a buy-sell clause.**

6. The scope of this Issue includes sales of real estate to an entity that is partially owned by the seller and the arrangement between the seller and the other investor of the jointly owned entity includes a buy-sell clause. Except for the potential effect of the buy-sell clause, the seller of the real estate as contemplated in this Issue has met the criteria in Statement 66 to recognize a partial sale. This Issue does not apply to transactions that are outside the scope of Statement 66.

Recognition

7. **Determining whether the terms of the buy-sell clause indicate that the seller has transferred the usual risks and rewards of ownership and does not have substantial continuing involvement pursuant to paragraph 26 of Statement 66 is a matter of judgment and requires consideration of all relevant facts and circumstances of the transaction at the time the real estate is sold.**

8. A buy-sell clause, in and of itself, does not constitute a prohibited form of continuing involvement that would preclude partial sales treatment under Statement 66. However, a buy-sell clause should be evaluated, in consideration of all the relevant facts and circumstances, to determine whether the buy-sell clause gives the buyer an in-substance option to put its 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).
Transition

9. This Issue shall be effective for new arrangements entered into and assessments performed in fiscal years beginning after December 15, 2007, and interim periods within those fiscal years. Earlier application is not permitted.

10. For purposes of the transition guidance, assessments are any assessment performed pursuant to Statement 66 after the effective date of this Issue for arrangements accounted for under the deposit, profit-sharing, leasing, or financing methods for reasons other than the existence of a buy-sell clause.

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

Board Ratification

11. At its December 12, 2007 meeting, the Board ratified the consensus reached by the Task Force in this Issue.

Status

12. No further EITF discussion is planned.
Suggested Index Entries for Issue No. 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”

REAL ESTATE

Sale of Real Estate Subject to the Requirements of Statement 66 When the Agreement Includes a Buy-Sell Clause 07-6

REAL ESTATE: SALES

Sale of Real Estate Subject to the Requirements of Statement 66 When the Agreement Includes a Buy-Sell Clause 07-6