

## ACCOUNTING STANDARD – 24 DISCONTINUING OPERATION

SUCCESS IS THE SUM OF SMALL EFFORTS,  
REPEATED DAY IN AND DAY OUT.

### 1. INTRODUCTION

**Para 3:** AS 24 is applicable to all discontinuing operations.

#### **DISCONTINUING OPERATION:**

A discontinuing operation is a **component** of an enterprise:

- a. That the enterprise, pursuant to a single plan, is:
  - (i) **Disposing of substantially** in its entirety, such as by selling the component in a single transaction or **by demerger or spin-off** of ownership of the component to the enterprise's shareholders or
  - (ii) **Disposing of piecemeal**, such as by selling off the component's assets and settling its liabilities individually or
  - (iii) Terminating through **abandonment** (giving up completely) and
- b. That **represents a separate major line** of business or geographical area of operations. (for example Business Segments or geographical Segments as defined in AS 17)
- c. That can be distinguished operationally and for financial reporting purposes.

## 2. DISCONTINUED OPERATION DOES NOT INCLUDE DISCONTINUATION OF A SINGLE PRODUCT ONLY OR DISCONTINUING A BUSINESS IN A PARTICULAR AREA.

To qualify as a discontinuing operation, the disposal must be pursuant to a **single coordinated plan**. However, changing the scope of an operation or the manner in which it is conducted is not abandonment because that operation, although changed, is continuing.

### Examples of Not a Discontinuing Operations:

- a. Gradual or evolutionary phasing out of a product line or class of service.
- b. Discontinuing, even if relatively abruptly, several products within an ongoing line of business.
- c. Shifting of some production or marketing activities for a particular line of business from one location to another and
- d. Closing of a facility to achieve productivity improvements or other cost savings.

### (V.V.IMP)

A component can be distinguished operationally and for financial reporting purposes - criterion (c) of the definition of a discontinuing operation - if all the following conditions are met:

- a. The operating assets and liabilities of the component can be directly attributed to it.
- b. Its revenue can be directly attributed to it.
- c. At least a majority of its operating expenses can be directly attributed to it.

**(Assets, liabilities, Revenues and Expenses can be directly attributable)**

The fact that a disposal of a component of an enterprise is classified as a discontinuing operation under AS 24 does not, in itself, bring into question the enterprise's ability to continue as a going concern.

### (V.V.IMP)

#### Initial Disclosure event

With respect to a discontinuing operation, the initial disclosure event is the occurrence of one of the following, whichever occurs earlier:

- a. The enterprise has entered into a **binding sale agreement** for substantially all of the assets attributable to the discontinuing operation or
- b. The enterprise's **board of directors** or similar governing body has both
  - (i) approved a detailed, **formal plan** for the discontinuance and
  - (ii) Made an **announcement** of the plan.

**Note:**

A detailed, formal plan for the discontinuance normally includes:

- **Identification** of the major assets to be disposed of;
- The expected **method of disposal**; (i.e. how we are going to dispose the business or assets)
- The **period expected** to be required for completion of the disposal;
- The principal **locations affected**;
- Approximate number of **employees who will be compensated** for terminating their services; and
- The **estimated proceeds or salvage** to be realised by disposal.

An enterprise's board of directors or similar governing body is considered to have made the announcement of a detailed, formal plan for discontinuance, **if it has announced the main features of the plan to those affected by it**, such as, lenders, stock exchanges, trade payables, trade unions, etc. in a sufficiently specific manner so as to make the enterprise demonstrably committed to the discontinuance.

### 3. PRESENTATION AND DISCLOSURE

#### **1. Initial Disclosure (in the first financial statements subsequent to announcement)**

An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:

- a. A **description** of the discontinuing operation(s)
- b. The **business or geographical segment(s)** in which it is reported as per AS 17
- c. The **date** and nature of the initial disclosure event.
- d. The **date or period in which the discontinuance is expected to be completed** if known or determinable
- e. The **carrying amounts**, as of the balance sheet date, of the **total assets** to be disposed of and the **total liabilities** to be settled
- f. The amounts of **revenue and expenses** in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period
- g. The amount of **pre-tax profit or loss from ordinary activities** attributable to the discontinuing operation during the current financial reporting period, **and the income tax expense** related thereto
- h. The amounts of **net cash flows** attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period

**Where to disclose above items?**

All the disclosures above should be presented in the notes to the financial statements except for amounts pertaining to pre-tax profit/loss of the discontinuing operation and the income tax expense thereon (second last bullet above) which should be shown on the face of the statement of profit and loss.

**2. Further disclosures (in the next financial statements)**

When an enterprise disposes of assets or settles liabilities attributable to a discontinuing operation or enters into binding agreements for the sale of such assets or the settlement of such liabilities, it should include, in its financial statements, the following information

**when the events occur:**

- a. For any gain or loss that is recognised on the disposal of assets or settlement of liabilities attributable to the discontinuing operation,
  - (i) the amount of the pre-tax gain or loss and
  - (ii) income tax expense relating to the gain or loss and
- b. The net selling price or range of prices (which is after deducting expected disposal costs) of those net assets for which the enterprise has entered into one or more binding sale agreements, the expected timing of receipt of those cash flows and the carrying amount of those net assets on the balance sheet date.

**3. Updating the disclosures**

In addition to these disclosures, an enterprise should include, in its financial statements, for periods subsequent to the one in which the initial disclosure event occurs, a description of **any significant changes** in the amount or timing of cash flows relating to the assets to be disposed or liabilities to be settled and the events causing those changes.

## 4. TILL WHICH PERIOD THE DISCLOSURES SHOULD BE GIVEN? (IMPORTANT)

The disclosures should continue in financial statements for periods upto and including the period in which the discontinuance is completed.

Discontinuance is completed when the plan is substantially completed or abandoned, though full payments from the buyer(s) may not yet have been received.

If an enterprise abandons or withdraws from a plan that was previously reported as a discontinuing operation, that fact, reasons therefore and its effect should be disclosed.

## 5. SEPARATE DISCLOSURE FOR EACH DISCONTINUING OPERATION

Any disclosures required by AS 24 should be presented separately for each discontinuing operation.

### V.V.IMP

#### Presentation of the required disclosures

The above disclosures should be presented in the notes to the financial statements except the following which should be shown on the face of the statement of profit and loss:

- a. The amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto and
- b. The amount of the pre-tax gain or loss recognised on the disposal of assets or settlement of liabilities attributable to the discontinuing operation.

## 6. RESTATEMENT OF PRIOR PERIODS

Comparative information for prior periods that is presented in financial statements prepared after the initial disclosure event **should be restated to segregate** assets, liabilities, revenue, expenses, and cash flows of continuing and discontinuing operations in a manner similar to that mentioned above.

## 7. DISCLOSURE IN INTERIM FINANCIAL REPORTS

Disclosures in an interim financial report in respect of a discontinuing operation should be made in accordance with AS 25, 'Interim Financial is reporting', including:

- a) Any significant activities or events since the end of the most recent annual reporting period relating to a discontinuing operation and
- b) Any significant changes in the amount or timing of cash flows relating to the assets to be disposed or liabilities to be settled.

**Note:** Discontinuing One Operations (component) doesn't always necessary that there is doubt of Going concern on other continuing operation.

**Example 1.**

Co XY runs a famous chain of restaurants. It decides to sell its stake in one of the restaurant. This restaurant contributes around 5% of total revenue to the entire business. XY does not sell any other restaurant as part of its strategy.

In the above case, the sale of one restaurant out of the chain does not constitute disposal of business under a single plan, or a portion that represents a major line of business or geographical area of operations. Thus, it cannot be regarded as a discontinuing operation.

**Example 2**

Group MN operates in various industries including Hotels, Airlines and Software through its subsidiaries. It has decided to sell its Airline business to be able to concentrate on other verticals. As a result, it has started to sell its aircrafts and paying off the associated liabilities. During the year, it has sold off 5 aircrafts out of the fleet of 50 aircrafts so far as part of the sale. The Airline business constitutes 25% of total group revenue.

In the above case, Airline business may be considered as **discontinuing operation**. This is due to the fact that the assets are sold off as part of a single plan, and that the business represents a separate major line of business, and can be distinguished both operationally and for financial reporting purposes.

**Example 3**

Entity RT operates in a single state and is trading in 3 products - X, Y and Z. Details with respect to the performance of each of the products are as under:

Particulars	X	Y	Z	Total
Sales	1,00,000	14,00,000	20,00,000	35,00,000
Cost of Goods Sold	(80,000)	(10,80,000)	(14,40,000)	(26,00,000)
Gross Margin	20,000	3,20,000	5,60,000	9,00,000
Operational Expenses	(15,000)	(1,70,000)	(3,60,000)	(5,45,000)
Profit before Tax	5,000	1,50,000	2,00,000	3,55,000

RT has decided to sell the business relating to Product Y to another entity. Since Product Y constitutes a major product, it may be considered as a discontinuing operations.

**Example 4**

GH, a large car manufacturing company, decides to discontinue its manufacturing operations relating to the diesel cars production. It plans to restructure the business by revamping its existing operations, and starting new manufacturing process for manufacture and sale of electric vehicles.

In the above example, it needs to be evaluated whether the restructuring is a result of continuing operations, or termination of existing operations, and accordingly it can be concluded whether it is a case of discontinuing operations or not.

## 8. (MCQ's from ICAI Material)

1. AB decided to dispose of its Clothing division as part of its long-term strategy.
  - (a) Date of Board approval - 1<sup>st</sup> March 20X1;
  - (b) Date of formal announcement made to affected parties - 15<sup>th</sup> March 20X1.
  - (c) Date of Binding Sale agreement - 1<sup>st</sup> July 20X1;
  - (d) Reporting date - 31<sup>st</sup> March 20X1

The date of initial disclosure event would be:

- (a) 1<sup>st</sup> March 20X1
  - (b) 15<sup>th</sup> March 20X1
  - (c) 31<sup>st</sup> March 20X1
  - (d) 31<sup>st</sup> July 20X1
  
2. To qualify as a component that can be distinguished operationally and for financial reporting purposes, the condition(s) to be met is (are):
  - (a) The operating assets and liabilities of the component can be directly attributed to it.
  - (b) Its revenue can be directly attributed to it.
  - (c) At least a majority of its operating expenses can be directly attributed to it.
  - (d) All of the above
  
3. Identify which of the following statements is incorrect?
  - (a) A discontinuing operation is a component of an enterprise that represents a separate major line of business or geographical area of operations.
  - (b) A discontinuing operation is a component of an enterprise that can be distinguished operationally and for financial reporting purposes.
  - (c) A discontinuing operation is a component of an enterprise that may or may not be distinguished operationally and for financial reporting purposes.
  - (d) A discontinuing operation may be disposed of in its entirety or piecemeal, but always pursuant to an overall plan to discontinue the entire component.
  
4. Identify the incorrect statement.
  - (a) Discontinuing operations are infrequent events, but this does not mean that all infrequent events are discontinuing operations.
  - (b) The fact that a disposal of a component of an enterprise is classified as a discontinuing operation under AS 24 would always raise a question regarding the enterprise's ability to continue as a going concern.
  - (c) For recognising and measuring the effect of discontinuing operations, AS 24 does not provide any guidelines, but for the purpose the relevant Accounting Standards should be referred.
  - (d) An enterprise shall include a description of the discontinuing operation, in its financial

statements beginning with the financial statements for the period in which the initial disclosure event occurs.

<b>ANSWERS</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>
	b	d	c	b