

Statutory Issue Paper No. 121

Accounting for the Impairment or Disposal of Real Estate Investments

STATUS

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Original SSAP and Current Authoritative Guidance: SSAP No. 90

Type of Issue:

Common Area

SUMMARY OF ISSUE

1. Current statutory accounting guidance for the impairment or disposal of real estate investments is provided in *SSAP No. 40—Real Estate Investments* (SSAP No. 40). Guidance for accounting for discontinued operations is found in *SSAP No. 24—Discontinued Operations and Extraordinary Items* (SSAP No. 24). Further, *SSAP No. 68—Business Combinations and Goodwill* (SSAP No. 68) contains guidance for impairment of goodwill arising from a business combination.
2. Generally Accepted Accounting Principles (GAAP) guidance for these issues was previously found in *Financial Accounting Standards Board (FASB) Statement No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of* (FAS 121) and *Accounting Principles Board (APB) Opinion No. 30, Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions* (APB 30). FAS 121 was superseded by *FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets* (FAS 144). APB 30 was superseded in part by FAS 144.
3. This issue paper establishes statutory accounting principles for the impairment or disposal of real estate investments and the treatment of long-lived assets associated with discontinued operations including nonadmitted intangible assets other than goodwill, such as trade names (referred to collectively as long-lived assets). This statement is not intended to conflict with guidance concerning operating results associated with discontinued operations, which is contained in SSAP No. 24.
4. This issue paper supersedes SSAP No. 40, paragraphs 9, 10 and 19.
5. This issue paper does not apply to (a) goodwill, (b) servicing assets, (c) financial instruments, including investments in equity securities accounted for under the cost or equity method, (d) deferred policy acquisition costs, and (e) deferred tax assets. This issue paper also does not apply to long-lived assets for which the accounting is prescribed by FASB Statement No. 86, *Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed* as adopted with modification to preclude the capitalization of software development costs in SSAP No. 17—*Preoperating and Research and Development Costs*. For a discussion on software development costs, see the guidance in SSAP No. 82—*Accounting for the Costs of Computer Software Developed or Obtained for Internal Use and Web Site Development Costs*. Statutory guidance on goodwill is in SSAP No. 68.

RECOMMENDED CONCLUSION

Recognition and Measurement of an Impairment Loss

6. For purposes of this Statement, impairment is the condition that exists when the carrying amount of a long-lived asset exceeds its fair value. An impairment loss shall be recognized only if the carrying amount of a long-lived asset is not recoverable and exceeds its fair value. The carrying amount of a long-

lived asset is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset. That assessment shall be based on the carrying amount of the asset at the date it is tested for recoverability, whether in use or under development. An impairment loss shall be measured as the amount by which the carrying amount of a long-lived asset exceeds its fair value.

When to Test a Long-Lived Asset for Recoverability

7. A long-lived asset shall be tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. The following are examples of such events or changes in circumstances:

- a. A significant decrease in the market price of a long-lived asset
- b. A significant adverse change in the extent or manner in which a long-lived asset is being used or in its physical condition
- c. A significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset, including an adverse action or assessment by a regulator
- d. An accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of a long-lived asset
- e. A current-period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset
- f. A current expectation that, more likely than not, a long-lived asset will be sold or otherwise disposed of significantly before the end of its previously estimated useful life.

8. When a long-lived asset is tested for recoverability, it also may be necessary to review depreciation estimates and methods as required by *SSAP No. 3—Accounting Changes and Corrections of Errors* (SSAP No. 3). Any revision to the remaining useful life of a long-lived asset resulting from that review also shall be considered in developing estimates of future cash flows used to test the asset for recoverability. However, any change in the accounting method for the asset resulting from that review shall be made only after applying this Statement.

Grouping Long-Lived Assets to Be Held and Used

9. For purposes of recognition and measurement of an impairment loss, a long-lived asset or assets shall not be grouped with other assets and liabilities at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities for properties occupied by the company.

10. In limited circumstances, a long-lived asset (for example, a corporate headquarters facility) may not have identifiable cash flows that are largely independent of the cash flows of other assets and liabilities and of other asset groups that consist of properties occupied by the company. In those circumstances, the asset group for that asset shall include all assets and liabilities of the entity.

New Cost Basis

11. If an impairment loss is recognized, the adjusted carrying amount of a long-lived asset shall be its new cost basis. For a depreciable long-lived asset, the new cost basis shall be depreciated (amortized) over the remaining useful life of that asset. Restoration of a previously recognized impairment loss is prohibited.

Estimates of Future Cash Flows Used to Test a Long-Lived Asset for Recoverability

12. Estimates of future cash flows used to test the recoverability of a long-lived asset shall include only the future cash flows (cash inflows less associated cash outflows) that are directly associated with, and that are expected to arise as a direct result of, the use and eventual disposition of the asset. Those estimates shall exclude interest charges that will be recognized as an expense when incurred.

13. Estimates of future cash flows used to test the recoverability of a long-lived asset shall incorporate the entity's own assumptions about its use of the asset and shall consider all available evidence. The assumptions used in developing those estimates shall be reasonable in relation to the assumptions used in developing other information used by the entity for comparable periods, such as internal budgets and projections, accruals related to incentive compensation plans, or information communicated to others. However, if alternative courses of action to recover the carrying amount of a long-lived asset are under consideration or if a range is estimated for the amount of possible future cash flows associated with the likely course of action, reporting entities shall use their best estimate in testing the recoverability of a long-lived asset.

14. Estimates of future cash flows used to test the recoverability of a long-lived asset shall be made for the remaining useful life of the asset to the entity.

15. Estimates of future cash flows used to test the recoverability of a long-lived asset that is in use, including a long-lived asset for which development is substantially complete, shall be based on the existing service potential of the asset at the date it is tested. The service potential of a long-lived asset encompasses its remaining useful life, cash-flow-generating capacity, and for tangible assets, physical output capacity. Those estimates shall include cash flows associated with future expenditures necessary to maintain the existing service potential of a long-lived asset, including those that replace the service potential of component parts of a long-lived asset (for example, the roof of a building) and component assets other than the primary asset of an asset group. Those estimates shall exclude cash flows associated with future capital expenditures that would increase the service potential of a long-lived asset.

16. Estimates of future cash flows used to test the recoverability of a long-lived asset that is under development shall be based on the expected service potential of the asset when development is substantially complete. Those estimates shall include cash flows associated with all future expenditures necessary to develop a long-lived asset, including interest payments that will be capitalized as part of the cost of the asset.

17. If a long-lived asset that is under development is part of an asset group that is in use, estimates of future cash flows used to test the recoverability of that group shall include the cash flows associated with future expenditures necessary to maintain the existing service potential of the group as well as the cash flows associated with all future expenditures necessary to substantially complete the asset that is under development.

Fair Value

18. A discussion of fair value is contained in the Glossary to the Statements of Statutory Accounting Principles. This issue paper requires properties occupied by the company, that are determined to be subject to recoverability testing as discussed in paragraphs 7 and 8, to follow the guidance in SSAP No. 40, paragraph 11.

Real Estate Investment Categories

19. SSAP No. 40 states that real estate investments shall be reported in the balance sheet categories of properties occupied by the company, properties held for the production of income, and properties held

for sale. However, the accounting guidance in FAS 144 distinguishes between long-lived assets to be held and used and long-lived assets to be disposed of. For statutory accounting purposes, long-lived assets to be held and used encompass properties occupied by the company and properties held for the production of income. Further, FAS 144 bifurcates the category of long-lived assets to be disposed of into long-lived assets to be disposed of other than by sale and long-lived assets to be disposed of by sale. Long-lived assets to be disposed of other than by sale shall be classified either as properties occupied by the company or as properties held for the production of income. Long-lived assets to be disposed of by sale shall be classified as properties held for sale.

Long-Lived Assets to Be Disposed Of Other Than by Sale

20. A long-lived asset to be disposed of other than by sale (for example, by abandonment, in an exchange for a similar productive long-lived asset, or in a distribution to owners in a spinoff) shall continue to be classified as held and used until disposal. Paragraphs 6-19 shall apply while the asset is classified as held and used. If a long-lived asset is to be abandoned or distributed to owners in a spinoff together with other assets (and liabilities) as a group and that disposal group is a segment, paragraph 33 shall apply to the disposal group at the date of disposal.

Long-Lived Asset to Be Abandoned

21. For purposes of this Statement, a long-lived asset to be abandoned is disposed of when it ceases to be used. If an entity commits to a plan to abandon a long-lived asset before the end of its previously estimated useful life, depreciation estimates shall be revised in accordance with SSAP No. 3 to reflect the use of the asset over its shortened useful life. A long-lived asset that has been temporarily idled shall not be accounted for as if abandoned.

Long-Lived Asset to Be Exchanged for a Similarly Productive Long-Lived Asset or to Be Distributed to Owners in a Spinoff

22. For purposes of this Statement, a long-lived asset to be exchanged for a similarly productive long-lived asset or to be distributed to owners in a spinoff is disposed of when it is exchanged or distributed. If the asset is tested for recoverability while it is classified as held and used, the estimates of future cash flows used in that test shall be based on the use of the asset for its remaining useful life, assuming that the disposal transaction will not occur. In addition to any impairment losses required to be recognized while the asset is classified as held and used, an impairment loss, if any, shall be recognized when the asset is disposed of if the carrying amount of the asset exceeds its fair value.

Long-Lived Assets to Be Disposed Of by Sale

Recognition

23. A long-lived asset to be sold shall be classified as held for sale in the period in which all of the following criteria are met:

- a. Management, having the authority to approve the action, commits to a plan to sell the asset;
- b. The asset is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets;
- c. An active program to locate a buyer and other actions required to complete the plan to sell the asset have been initiated;

- d. The sale of the asset is probable, and transfer of the asset is expected to qualify for recognition as a completed sale, within one year, except as permitted by paragraph 24;
- e. The asset is being actively marketed for sale at a price that is reasonable in relation to its current fair value;
- f. Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

If at any time the criteria in this paragraph are no longer met (except as permitted by paragraph 24), a long-lived asset classified as held for sale shall be reclassified as held and used in accordance with paragraphs 31 and 32.

24. Events or circumstances beyond an entity's control may extend the period required to complete the sale of a long-lived asset beyond one year. An exception to the one-year requirement in paragraph 23.d. shall apply in the following situations in which such events or circumstances arise:

- a. If at the date an entity commits to a plan to sell a long-lived asset the entity reasonably expects that others (not a buyer) will impose conditions on the transfer of the asset that will extend the period required to complete the sale and (1) actions necessary to respond to those conditions cannot be initiated until after a firm purchase commitment is obtained and (2) a firm purchase commitment is probable within one year.
- b. If an entity obtains a firm purchase commitment and, as a result, a buyer or others unexpectedly impose conditions on the transfer of a long-lived asset previously classified as held for sale that will extend the period required to complete the sale and (1) actions necessary to respond to the conditions have been or will be initiated in a timely manner and (2) a favorable resolution of the delaying factors is expected.
- c. If during the initial one-year period, circumstances arise that previously were considered unlikely and, as a result, a long-lived asset previously classified as held for sale is not sold by the end of that period and (1) during the initial one-year period the entity initiated actions necessary to respond to the change in circumstances, (2) the asset is being actively marketed at a price that is reasonable given the change in circumstances, and (3) the criteria in paragraph 23 are met.

25. A long-lived asset that is newly acquired and that will be sold rather than held and used shall be classified as held for sale at the acquisition date only if the one-year requirement in paragraph 23.d. is met (except as permitted by paragraph 24) and any other criteria in paragraph 23 that are not met at that date are probable of being met within a short period following the acquisition (usually within three months).

26. If the criteria in paragraph 23 are met after the balance sheet date but before issuance of the financial statements, a long-lived asset shall continue to be classified as held and used in those financial statements when issued. The information required by paragraph 39 shall be disclosed in the notes to the financial statements. If the asset is tested for recoverability (on a held-and-used basis) as of the balance sheet date, the estimates of future cash flows used in that test shall consider the likelihood of possible outcomes that existed at the balance sheet date, including the assessment of the likelihood of the future sale of the asset. That assessment made as of the balance sheet date shall not be revised for a decision to sell the asset after the balance sheet date. An impairment loss, if any, to be recognized shall be measured as the amount by which the carrying amount of the asset exceeds its fair value at the balance sheet date.

Measurement

27. A long-lived asset classified as held for sale shall be measured at the lower of its carrying amount or fair value less cost to sell. If the asset is newly acquired, the carrying amount of the asset shall be established based on its fair value less cost to sell at the acquisition date. A long-lived asset shall not be depreciated (amortized) while it is classified as held for sale. Interest and other expenses attributable to the liabilities of a disposal classified as held for sale shall continue to be accrued.

28. Costs to sell are the incremental direct costs to transact a sale, that is, the costs that result directly from and are essential to a sale transaction and that would not have been incurred by the entity had the decision to sell not been made. Those costs include broker commissions, legal and title transfer fees, and closing costs that must be incurred before legal title can be transferred. Those costs exclude expected future losses associated with the operations of a long-lived asset while it is classified as held for sale.

29. The carrying amounts of any assets that are not covered by this Statement that are included in a disposal classified as held for sale shall be adjusted in accordance with other applicable statements of statutory accounting principles prior to measurement.

30. A realized loss shall be recognized in the summary of operations for any initial or subsequent write-down to fair value less cost to sell. A gain shall not be recognized for any subsequent increase in fair value less cost to sell until the asset is sold. The loss shall adjust only the carrying amount of a long-lived asset, whether classified as held for sale individually or as part of a disposal group. A gain or loss not previously recognized that results from the sale of a long-lived asset shall be recognized at the date of sale.

Changes to a Plan of Sale

31. If circumstances arise that previously were considered unlikely and, as a result, an entity decides not to sell a long-lived asset previously classified as held for sale, the asset shall be reclassified as held and used. A long-lived asset that is reclassified shall be measured individually at the lower of its (a) carrying amount before the asset was classified as held for sale, adjusted for any depreciation (amortization) expense that would have been recognized had the asset been continuously classified as held and used, or (b) fair value at the date of the subsequent decision not to sell.

32. Any required adjustment to the carrying amount of a long-lived asset that is reclassified as held and used shall be included in income from operations in the period of the subsequent decision not to sell. That adjustment shall be reported in the same income statement caption used to report a loss, if any, recognized in accordance with paragraph 34.

Reporting Long-Lived Assets and Disposal Groups to Be Disposed Of

Reporting Discontinued Operations

33. For purposes of reporting income and losses related to discontinued operations; any reference to the phrase “component of an entity” is replaced with “segment” as defined in SSAP No. 24.

Reporting Disposal Gains or Losses in Operations

34. Any disposal gain or loss recognized for long-lived assets shall be included as a net realized gain or loss in the summary of operations.

Reporting a Long-Lived Asset or Disposal Group Classified as Held for Sale

35. A long-lived asset classified as held for sale shall be presented separately in the balance sheet. The assets and liabilities of a disposal classified as held for sale shall be presented separately in the asset and liability sections, respectively, of the balance sheet. Those assets and liabilities shall not be offset and presented as a single amount. The major classes of assets and liabilities classified as held for sale shall be separately disclosed either on the face of the balance sheet or in the notes to financial statements (paragraph 39).

Reporting Impairment

36. Any impairment loss recognized on long-lived assets shall be recorded in the summary of operations as a realized loss.

Disclosures

37. The following information shall be disclosed in the notes to the financial statements that include the period in which an impairment loss is recognized:

- a. A description of the impaired assets and the facts and circumstances leading to the impairment;
- b. The amount of the impairment loss and how fair value was determined; and

38. The caption in the summary of operations, which includes the impairment loss.

39. The following information shall be disclosed in the notes to the financial statements that cover the period in which a long-lived asset either has been sold or is classified as held for sale:

- a. A description of the facts and circumstances leading to the expected disposal, the expected manner and timing of that disposal.
- b. If applicable, the gain or loss recognized and if not separately presented on the face of the summary of operations, the caption in the summary of operations that includes that gain or loss.

40. If paragraphs 31 and 32 apply, a description of the facts and circumstances leading to the decision to change the plan to sell the asset; and its effect on the results of operations for the period and any prior periods presented shall be disclosed in the notes to financial statements that include the period of that decision.

Effective Date and Transition

41. Upon adoption of this issue paper, the NAIC will release a SSAP for comment. The SSAP will contain the adopted Summary Conclusion of this issue paper. Users of the Accounting Practices and Procedures Manual should note that issue papers are not represented in the Statutory Hierarchy (see Section IV of the Preamble) and therefore the conclusions reached in this issue paper should not be applied until the corresponding SSAP has been adopted by the Plenary of the NAIC. It is expected that the SSAP will contain an effective date of years beginning on or after January 1, 2004.

DISCUSSION

42. FAS 144 supersedes FAS 121 and in part APB 30. FAS 144 retains the requirements of FAS 121 to (a) recognize an impairment loss only if the carrying amount of a long-lived asset is not recoverable from its undiscounted cash flows and (b) measure an impairment loss as the difference between the carrying amount and fair value of the asset. FAS 144 requires that a long-lived asset to be abandoned, exchanged for a similar productive asset, or distributed to owners in a spinoff be considered held and used until it is disposed of. FAS 144 also sets forth that the accounting model for long-lived assets to be disposed of by sale is used for all long-lived assets, whether previously held and used or newly acquired. FAS 144 also resolves implementation issues that came about in the application of existing guidance.

43. SSAP No. 40 states that real estate investments shall be reported in the balance sheet categories of properties occupied by the company, properties held for the production of income, and properties held for sale. However, the accounting guidance in FAS 144 distinguishes between long-lived assets to be held and used and long-lived assets to be disposed of. For statutory accounting purposes, long-lived assets to be held and used encompass properties occupied by the company and properties held for the production of income and will be referred to as such in this issue paper. Further, FAS 144 bifurcates the category of long-lived assets to be disposed of into long-lived assets to be disposed of other than by sale and long-lived assets to be disposed of by sale. In this issue paper, long-lived assets to be disposed of other than by sale shall be classified either as properties occupied by the company or as properties held for the production of income, as set forth in paragraph 27 of FAS 144 which is adopted in this issue paper. Long-lived assets to be disposed of by sale shall be classified as properties held for sale.

44. FAS 144 contains substantial guidance concerning the concept of grouping of assets for the purposes of measurement of an impairment loss. Grouping would seem to allow for the offsetting of gains on certain assets with losses on other assets in the same grouping, possibly resulting in no impairment loss being recognized. This is contrary to the concept of conservatism in the Statement of Concepts. As such, grouping of assets for the purpose of determining whether an impairment loss has occurred will not be allowed for statutory accounting purposes.

45. During the drafting process of this issue paper, an initial determination was made that SSAP Nos. 24, 40, 68 would be amended as a result of adopting FAS 144. Ultimately, only SSAP No. 40 was amended relative to adoption of FAS 144 as discussed below.

46. This issue paper adopts FAS 144 with modification to paragraphs 9, 17, 18, 19, 21, 25, 28, 35, 36, 37, 41, 42, 44, 45 and 47. Further, this issue paper rejects paragraphs 10-14, paragraphs 22-24, 26.d., and 43 of FAS 144. Refer to paragraph 47 of this issue paper for additional information with regard to these paragraphs.

47. The following modifications to FAS 144 were made in order to maintain consistency with current statutory accounting principles and the Statement of Concepts:

- a. Paragraph 9 is amended to require that changes in depreciation estimates and methods and amortization periods found as a result of a test for recoverability should be accounted for in accordance with SSAP No. 3;
- b. Paragraphs 10-14, which address the grouping of assets, are rejected, as reporting entities should apply the guidance in this statement to each of its assets on an individual basis;
- c. Paragraphs 17, 18, 19 and 21 discuss estimates of future cash flows used to test the recoverability of a long-lived asset, and states that a probability-weighted approach may be useful in considering the likelihood of those possible outcomes. For statutory accounting purposes, reporting entities shall use their best estimate in testing the recoverability of a long-lived asset;

- d. Paragraphs 22-24, which discuss fair value, are rejected. The definition of fair value is in the glossary to the Statement of Statutory Accounting Principles. In addition, this statement allows a modification to use for determining the fair value of properties occupied by company.
- e. Paragraph 25 is amended to require that an impairment loss on properties occupied by the company and properties held for the production of income shall be recorded in the summary of operations as a realized loss;
- f. Paragraph 28 is amended to require that changes in depreciation estimates shall be accounted for in accordance with SSAP No. 3;
- g. If the sale is expected to occur beyond one year, paragraph 35 allows the cost to sell to be discounted. For statutory accounting purposes, the cost to sell shall not be discounted;
- h. Paragraph 36 is amended to remove the reference to goodwill, as FAS 144 does not include goodwill within its scope unless such goodwill is included in an asset group that is or includes a reporting unit; paragraph 18 of this issue paper does not recognize a reporting unit. Paragraph 36 is further amended to require reporting entities to adjust all assets in accordance with other applicable statements of statutory accounting principles prior to measurement;
- i. Paragraph 37 is amended to clarify that losses recognized as a result of adjustments to fair value less cost to sell shall be recorded in the summary of operations as a realized gain/loss. Paragraph 37 is also modified to disallow the recognition of any gain for subsequent increases in fair value less cost to sell until the asset is sold. This is consistent with the concept of conservatism found in the Statement of Concepts;
- j. Within paragraphs 41, 42 and 44 of FAS 144 addressing discontinued operations, any reference to the phrase “component of an entity” is replaced with “segment” as defined in SSAP No. 24;
- k. Paragraph 42 is amended to state that the results of operations of a discontinued operation shall be reported consistently with the entity’s reporting of continuing operations. This is consistent with the guidance found in paragraph 5 of SSAP No. 24;
- l. Paragraph 44 is amended to state that adjustments to amounts previously reported related to continuing operations shall be reported consistently with the entity’s reporting of continuing operations. This is consistent with the guidance found in paragraph 5 of SSAP No. 24. In addition, subparagraphs a. through c. of paragraph 44 are adopted into paragraph 5 of SSAP No. 24;
- m. Paragraph 45 is amended to state that a gain or loss on an asset classified as held for sale that has been disposed of shall be included in the summary of operations as a realized gain or loss;
- n. The disclosures in paragraphs 47.a. and 47.b. are adopted with respect to properties held for sale, except for the disclosures related to major classes of assets, as grouping has been rejected in this issue paper. Subparagraphs 47.c. and 47.d. are rejected as such paragraphs relate to discontinued operations and segment reporting. The disclosures included in paragraphs 6 and 7 of SSAP No. 24 are more appropriate given the differences between statutory and GAAP reporting of discontinued operations;

- o. Paragraph 26.d. requires the disclosure of the segment in which an impaired asset is reported. This paragraph is rejected, as statutory accounting requires accounting and reporting at the legal entity level. Further, any additional references to segments, reporting units, or disposal groups found in FAS 144 are also rejected, except with regard to a segment within the context of discontinued operations; and
- p. Paragraph 43 is rejected and the guidance related to the recognition of losses/income expected between the measurement date and the expected disposal date included in paragraph 4 of SSAP No. 24 is retained, as such guidance is consistent with the concept of conservatism in the Statement of Concepts.

48. Paragraphs 12-14 of FAS 121 address the impairment of goodwill, and paragraphs 12, 14.a. and 14.b. of FAS 121 were adopted in SSAP No. 68. However, paragraph 12 of FAS 121 was superseded by FASB Statement No. 142, Goodwill and Other Intangible Assets (FAS 142), which was rejected in SSAP No. 68. Given the applicability of the guidance found in paragraph 12 of FAS 121 to statutory accounting principles, the impairment guidance found in FAS 121, paragraph 12 is retained. Paragraph 12 of FAS 121 has been excerpted in *Issue Paper No. 68—Business Combinations and Goodwill*, paragraph 31.

RELEVANT STATUTORY ACCOUNTING AND GAAP GUIDANCE

Statutory Accounting

49. SSAP No. 40 paragraphs 4, 8, 9, 10, 11, and 19:

4. Real estate investments shall be reported net of encumbrances in the following balance sheet categories, with parenthetical disclosure of the amount of related encumbrances:

- a. Properties occupied by the company;
- b. Properties held for the production of income; and
- c. Properties held for sale.

8. The cost of property included in real estate investments, other than land, shall be depreciated over the estimated useful life, not to exceed fifty years. Depreciation expense shall be included in investment expenses.

9. Properties occupied by the company and properties held for the production of income shall be carried at depreciated cost less encumbrances unless events or circumstances indicate the carrying amount of the asset (amount prior to reduction for encumbrances) may not be recoverable. Paragraph 5 of *FASB Statement No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of* (FAS 121), provides examples of events or changes in circumstances which indicate that the recoverability of the carrying amount of properties occupied by the company or properties held for the production of income should be assessed. If the events or changes in circumstances set forth in paragraph 5 of FAS 121 are present or if other events or changes in circumstances indicate that the carrying amount of properties occupied by the company or properties held for the production of income may not be recoverable, the entity shall determine whether an impairment loss must be recognized in accordance with paragraph 6 of FAS 121. Property occupied by the company shall be evaluated using the asset grouping approach of paragraph 8 of FAS 121. An impairment loss is measured as the amount by which the individual carrying amounts exceed the fair value of properties occupied by the company or properties held for the production of income. Fair value is determined in accordance with paragraph 11 of this statement. If the fair value of the asset is less than the carrying value, the asset shall be written down to the fair value thereby establishing a new cost basis. The new cost basis shall not be changed for subsequent recoveries in fair value. The adjustment shall be recorded in the statement of operations as a realized loss.

10. Properties that the reporting entity has the intent to sell or is required to sell shall be classified as properties held for sale and carried at the lower of depreciated cost or fair value less encumbrances and estimated costs to sell the property consistent with paragraph 16 of FAS 121. The intent to sell a property exists when management, having the authority to approve the action, has committed to a plan to dispose of the asset, either by sale or abandonment. Fair value of the asset shall be determined in accordance with paragraph 11 of this statement. Subsequent revisions to the fair value of the asset shall be accounted for in accordance with paragraph 17 of FAS 121.
11. The current fair value of real estate shall be determined on a property by property basis (i.e., increases in the fair value of one property shall not be used to offset declines in fair value of another) and shall be defined as the price that a property would bring in a competitive and open market under all conditions requisite to a fair sale (i.e., the buyer and seller acting prudently and knowledgeably with the price not affected by any undue stimulus). If market quotes are unavailable, estimates of fair value shall be determined by an appraisal (internal or third party), which is based upon an evaluation of all relevant data about the market, considering the following:
- a. A physical inspection of the premises;
 - b. The present value of future cash flows generated by the property (Discounted Cash Flows), or capitalization of stabilized net operating income (Direct Capitalization);
 - c. Current sales prices of similar properties with adjustments for differences in the properties (Sales Comparison Approach);
 - d. Costs to sell the property if the reporting entity does not have the intent or ability to hold the real estate as an investment; and
 - e. Replacement costs of the improvements, less depreciation, plus the value of the land (Cost Approach).
19. An entity that recognizes an impairment loss shall disclose all of the following in financial statements that include the period of the impairment write-down:
- a. A description of the impaired assets and the facts and circumstances leading to the impairment;
 - b. The amount of the impairment loss and how fair value was determined; and
 - c. The caption in the statement of operations in which the impairment loss is aggregated.
50. SSAP No. 24 paragraphs 4, 6 and 7:
4. The determination of whether a gain or loss results from the disposal shall be made at the measurement date based on estimates at that date of the net realizable value of the segment after giving consideration to any estimated costs and expenses directly associated with the disposal and, if a plan of disposal is to be carried out over a period of time and contemplates continuing operations during that period, to any estimated income or losses from operations. If it is expected that net losses from operations will be incurred between the measurement date and the expected disposal date, the computation of the gain or loss on disposal shall also include an estimate of such amounts. If it is expected that net income will be generated from operations during that period the computation shall include the estimated net income, limited however to the amount of any loss otherwise recognizable for the disposal, with any remainder accounted for when realized. Any changes in the original estimate shall be accounted for in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

6. Additionally, the financial statements for the period encompassing the measurement date and the year subsequent shall contain the following:

- a. The identity of the segment of business that has been or will be discontinued;
- b. The expected disposal date, if known (see definition in paragraph 2 above);
- c. The expected manner of disposal;
- d. A description of the remaining assets and liabilities of the segment at the balance sheet date; and
- e. The amounts related to the discontinued operations and the effect on the financial statements, including the balance sheet and income statement line items which have been affected.

7. If material revisions are made to the estimates of the cost to dispose of a segment in years subsequent to the disclosure required in paragraph 6 above, the nature and the effect of the revisions to the estimates shall be disclosed for the period in which the revision was made including the effect on income or loss from operations and the effect on the carrying amount of the remaining assets and liabilities of the segment at the balance sheet date.

51. SSAP No. 3 paragraphs 3-6:

Change in Accounting Principle

3. A change in accounting principle results from the adoption of an accepted accounting principle, or method of applying the principle, which differs from the principles or methods previously used for reporting purposes. A change in the method of applying an accounting principle shall be considered a change in accounting principle.

4. A characteristic of a change in accounting principle is that it concerns a choice from among two or more statutory accounting principles. However, a change in accounting principle is neither (a) the initial adoption of an accounting principle in recognition of events or transactions occurring for the first time or previously immaterial in their effect, nor (b) the adoption or modification of an accounting principle necessitated by transactions or events that are clearly different in substance from those previously occurring.

5. The cumulative effect of changes in accounting principles shall be reported as adjustments to unassigned funds (surplus) in the period of the change in accounting principle. The cumulative effect is the difference between the amount of capital and surplus at the beginning of the year and the amount of capital and surplus that would have been reported at that date if the new accounting principle had been applied retroactively for all prior periods.

Change in Accounting Estimate

6. Changes in estimates used in accounting are necessary consequences of periodic presentations of financial statements which require estimating the effects of future events. Examples of items for which estimates are necessary include service lives of depreciable assets and changes in loss reserve estimates for property and casualty companies. Accounting estimates change as new events occur, as more experience is acquired, or as additional information is obtained.

Generally Accepted Accounting Principles

52. FAS 144 provides the following:

Long-Lived Assets to Be Held and Used

Recognition and Measurement of an Impairment Loss

7. For purposes of this Statement, impairment is the condition that exists when the carrying amount of a long-lived asset (asset group) exceeds its fair value. An impairment loss shall be recognized only if the carrying amount of a long-lived asset (asset group) is not recoverable and exceeds its fair value. The carrying amount of a long-lived asset (asset group) is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset (asset group). That assessment shall be based on the carrying amount of the asset (asset group) at the date it is tested for recoverability, whether in use (paragraph 19) or under development (paragraph 20). An impairment loss shall be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.

When to Test a Long-Lived Asset for Recoverability

8. A long-lived asset (asset group) shall be tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. The following are examples of such events or changes in circumstances:

- a. A significant decrease in the market price of a long-lived asset (asset group)
- b. A significant adverse change in the extent or manner in which a long-lived asset (asset group) is being used or in its physical condition
- c. A significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset (asset group), including an adverse action or assessment by a regulator
- d. An accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of a long-lived asset (asset group)
- e. A current-period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset (asset group)
- f. A current expectation that, more likely than not, a long-lived asset (asset group) will be sold or otherwise disposed of significantly before the end of its previously estimated useful life.

9. When a long-lived asset (asset group) is tested for recoverability, it also may be necessary to review depreciation estimates and method as required by APB Opinion No. 20, Accounting Changes, or the amortization period as required by *FASB Statement No. 142, Goodwill and Other Intangible Assets*. Any revision to the remaining useful life of a long-lived asset resulting from that review also shall be considered in developing estimates of future cash flows used to test the asset (asset group) for recoverability (paragraph 18). However, any change in the accounting method for the asset resulting from that review shall be made only after applying this Statement.

Grouping Long-Lived Assets to Be Held and Used

10. For purposes of recognition and measurement of an impairment loss, a long-lived asset or assets shall be grouped with other assets and liabilities at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities. However, an impairment loss, if any, that results from applying this Statement shall reduce only the carrying amount of a long-lived asset or assets of the group in accordance with paragraph 14.

11. In limited circumstances, a long-lived asset (for example, a corporate headquarters facility) may not have identifiable cash flows that are largely independent of the cash flows of other assets and liabilities and of other asset groups. In those circumstances, the asset group for that long-lived asset shall include all assets and liabilities of the entity.

12. Goodwill shall be included in an asset group to be tested for impairment under this Statement only if the asset group is or includes a reporting unit. Goodwill shall not be included in

a lower-level asset group that includes only part of a reporting unit. Estimates of future cash flows used to test that lower-level asset group for recoverability shall not be adjusted for the effect of excluding goodwill from the group.

13. Other than goodwill, the carrying amounts of any assets (such as accounts receivable and inventory) and liabilities (such as accounts payable, long-term debt, and asset retirement obligations) not covered by this Statement that are included in an asset group shall be adjusted in accordance with other applicable generally accepted accounting principles prior to testing the asset group for recoverability.

14. An impairment loss for an asset group shall reduce only the carrying amounts of a long-lived asset or assets of the group. The loss shall be allocated to the long-lived assets of the group on a pro rata basis using the relative carrying amounts of those assets, except that the loss allocated to an individual long-lived asset of the group shall not reduce the carrying amount of that asset below its fair value whenever that fair value is determinable without undue cost and effort. (Example 1 of Appendix A illustrates the allocation of an impairment loss for an asset group.)

New Cost Basis

15. If an impairment loss is recognized, the adjusted carrying amount of a long-lived asset shall be its new cost basis. For a depreciable long-lived asset, the new cost basis shall be depreciated (amortized) over the remaining useful life of that asset. Restoration of a previously recognized impairment loss is prohibited.

Estimates of Future Cash Flows Used to Test a Long-Lived Asset for Recoverability

16. Estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) shall include only the future cash flows (cash inflows less associated cash outflows) that are directly associated with and that are expected to arise as a direct result of the use and eventual disposition of the asset (asset group). Those estimates shall exclude interest charges that will be recognized as an expense when incurred.

17. Estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) shall incorporate the entity's own assumptions about its use of the asset (asset group) and shall consider all available evidence. The assumptions used in developing those estimates shall be reasonable in relation to the assumptions used in developing other information used by the entity for comparable periods, such as internal budgets and projections, accruals related to incentive compensation plans, or information communicated to others. However, if alternative courses of action to recover the carrying amount of a long-lived asset (asset group) are under consideration or if a range is estimated for the amount of possible future cash flows associated with the likely course of action, the likelihood of those possible outcomes shall be considered. A probability-weighted approach may be useful in considering the likelihood of those possible outcomes. (Example 2 of Appendix A illustrates the use of that approach when alternative courses of action are under consideration.)

18. Estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) shall be made for the remaining useful life of the asset (asset group) to the entity. The remaining useful life of an asset group shall be based on the remaining useful life of the primary asset of the group. For purposes of this Statement, the primary asset is the principal long-lived tangible asset being depreciated or intangible asset being amortized that is the most significant component asset from which the asset group derives its cash-flow-generating capacity. Factors that an entity generally should consider in determining whether a long-lived asset is the primary asset of an asset group include the following: (a) whether other assets of the group would have been acquired by the entity without the asset, (b) the level of investment that would be required to replace the asset, and (c) the remaining useful life of the asset relative to other assets of the group. If the primary asset is not the asset of the group with the longest remaining useful life, estimates of future cash flows for the group should assume the sale of the group at the end of the remaining useful life of the primary asset.

19. Estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) that is in use, including a long-lived asset (asset group) for which development is substantially complete, shall be based on the existing service potential of the asset (asset group) at the date it is tested. The service potential of a long-lived asset (asset group) encompasses its remaining useful life, cash-flow-generating capacity, and for tangible assets, physical output capacity. Those estimates shall include cash flows associated with future expenditures necessary to maintain the existing service potential of a long-lived asset (asset group), including those that replace the service potential of component parts of a long-lived asset (for example, the roof of a building) and component assets other than the primary asset of an asset group. Those estimates shall exclude cash flows associated with future capital expenditures that would increase the service potential of a long-lived asset (asset group).

20. Estimates of future cash flows used to test the recoverability of a long-lived asset (asset group) that is under development shall be based on the expected service potential of the asset (group) when development is substantially complete. Those estimates shall include cash flows associated with all future expenditures necessary to develop a long-lived asset (asset group), including interest payments that will be capitalized as part of the cost of the asset (asset group).

21. If a long-lived asset that is under development is part of an asset group that is in use, estimates of future cash flows used to test the recoverability of that group shall include the cash flows associated with future expenditures necessary to maintain the existing service potential of the group (paragraph 19) as well as the cash flows associated with all future expenditures necessary to substantially complete the asset that is under development (paragraph 20). (Example 3 of Appendix A illustrates that situation.)

Fair Value

22. The fair value of an asset (liability) is the amount at which that asset (liability) could be bought (incurred) or sold (settled) in a current transaction between willing parties, that is, other than in a forced or liquidation sale. Quoted market prices in active markets are the best evidence of fair value and shall be used as the basis for the measurement, if available. However, in many instances, quoted market prices in active markets will not be available for the long-lived assets (asset groups) covered by this Statement. In those instances, the estimate of fair value shall be based on the best information available, including prices for similar assets (groups) and the results of using other valuation techniques.

23. A present value technique is often the best available valuation technique with which to estimate the fair value of a long-lived asset (asset group). Paragraphs 39-54 of *FASB Concepts Statement No. 7, Using Cash Flow Information and Present Value in Accounting Measurements*, discuss the use of two present value techniques to measure the fair value of an asset (liability). The first is expected present value, in which multiple cash flow scenarios that reflect the range of possible outcomes and a risk-free rate are used to estimate fair value. The second is traditional present value, in which a single set of estimated cash flows and a single interest rate (a rate commensurate with the risk) are used to estimate fair value. Either present value technique can be used for a fair value measurement. However, for long-lived assets (asset groups) that have uncertainties both in timing and amount, an expected present value technique will often be the appropriate technique. (Example 4 of Appendix A illustrates the use of that technique.)

24. If a present value technique is used, estimates of future cash flows shall be consistent with the objective of measuring fair value. Assumptions that marketplace participants would use in their estimates of fair value shall be incorporated whenever that information is available without undue cost and effort. Otherwise, the entity may use its own assumptions.

Reporting and Disclosure

25. An impairment loss recognized for a long-lived asset (asset group) to be held and used shall be included in income from continuing operations before income taxes in the income statement of a business enterprise and in income from continuing operations in the statement of

activities of a not-for-profit organization. If a subtotal such as “income from operations” is presented, it shall include the amount of that loss.

26. The following information shall be disclosed in the notes to the financial statements that include the period in which an impairment loss is recognized:

- a. A description of the impaired long-lived asset (asset group) and the facts and circumstances leading to the impairment
- b. If not separately presented on the face of the statement, the amount of the impairment loss and the caption in the income statement or the statement of activities that includes that loss
- c. The method or methods for determining fair value (whether based on a quoted market price, prices for similar assets, or another valuation technique)
- d. If applicable, the segment in which the impaired long-lived asset (asset group) is reported under FASB Statement No. 131, Disclosures about Segments of an Enterprise and Related Information.

Long-Lived Assets to Be Disposed Of Other than by Sale

27. A long-lived asset to be disposed of other than by sale (for example, by abandonment, in an exchange for a similar productive long-lived asset, or in a distribution to owners in a spinoff) shall continue to be classified as held and used until it is disposed of. Paragraphs 7-26 shall apply while the asset is classified as held and used. If a long-lived asset is to be abandoned or distributed to owners in a spinoff together with other assets (and liabilities) as a group and that disposal group is a component of an entity, paragraphs 41-44 shall apply to the disposal group at the date it is disposed of.

Long-Lived Asset to Be Abandoned

28. For purposes of this Statement, a long-lived asset to be abandoned is disposed of when it ceases to be used. If an entity commits to a plan to abandon a long-lived asset before the end of its previously estimated useful life, depreciation estimates shall be revised in accordance with Opinion 20 to reflect the use of the asset over its shortened useful life (refer to paragraph 9). A long-lived asset that has been temporarily idled shall not be accounted for as if abandoned.

Long-Lived Asset to Be Exchanged for a Similar Productive Long-Lived Asset or to Be Distributed to Owners in a Spinoff

29. For purposes of this Statement, a long-lived asset to be exchanged for a similar productive long-lived asset or to be distributed to owners in a spinoff is disposed of when it is exchanged or distributed. If the asset (asset group) is tested for recoverability while it is classified as held and used, the estimates of future cash flows used in that test shall be based on the use of the asset for its remaining useful life, assuming that the disposal transaction will not occur. In addition to any impairment losses required to be recognized while the asset is classified as held and used, an impairment loss, if any, shall be recognized when the asset is disposed of if the carrying amount of the asset (disposal group) exceeds its fair value.

Long-Lived Assets to Be Disposed Of by Sale

Recognition

30. A long-lived asset (disposal group) to be sold shall be classified as held for sale in the period in which all of the following criteria are met:

- a. Management, having the authority to approve the action, commits to a plan to sell the asset (disposal group).

- b. The asset (disposal group) is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (disposal groups). (Examples 5–7 of Appendix A illustrate when that criterion would be met.)
- c. An active program to locate a buyer and other actions required to complete the plan to sell the asset (disposal group) have been initiated.
- d. The sale of the asset (disposal group) is probable, and transfer of the asset (disposal group) is expected to qualify for recognition as a completed sale, within one year, except as permitted by paragraph 31. (Example 8 of Appendix A illustrates when that criterion would be met.)
- e. The asset (disposal group) is being actively marketed for sale at a price that is reasonable in relation to its current fair value.
- f. Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

If at any time the criteria in this paragraph are no longer met (except as permitted by paragraph 31), a long-lived asset (disposal group) classified as held for sale shall be reclassified as held and used in accordance with paragraph 38.

31. Events or circumstances beyond an entity's control may extend the period required to complete the sale of a long-lived asset (disposal group) beyond one year. An exception to the one-year requirement in paragraph 30.d. shall apply in the following situations in which such events or circumstances arise:

- a. If at the date an entity commits to a plan to sell a long-lived asset (disposal group) the entity reasonably expects that others (not a buyer) will impose conditions on the transfer of the asset (group) that will extend the period required to complete the sale and (1) actions necessary to respond to those conditions cannot be initiated until after a firm purchase commitment is obtained and (2) a firm purchase commitment is probable within one year. (Example 9 of Appendix A illustrates that situation.)
- b. If an entity obtains a firm purchase commitment and, as a result, a buyer or others unexpectedly impose conditions on the transfer of a long-lived asset (disposal group) previously classified as held for sale that will extend the period required to complete the sale and (1) actions necessary to respond to the conditions have been or will be timely initiated and (2) a favorable resolution of the delaying factors is expected. (Example 10 of Appendix A illustrates that situation.)
- c. If during the initial one-year period, circumstances arise that previously were considered unlikely and, as a result, a long-lived asset (disposal group) previously classified as held for sale is not sold by the end of that period and (1) during the initial one-year period the entity initiated actions necessary to respond to the change in circumstances, (2) the asset (group) is being actively marketed at a price that is reasonable given the change in circumstances, and (3) the criteria in paragraph 30 are met. (Example 11 of Appendix A illustrates that situation.)

32. A long-lived asset (disposal group) that is newly acquired and that will be sold rather than held and used shall be classified as held for sale at the acquisition date only if the one-year requirement in paragraph 30.d. is met (except as permitted by paragraph 31) and any other criteria in paragraph 30 that are not met at that date are probable of being met within a short period following the acquisition (usually within three months).

33. If the criteria in paragraph 30 are met after the balance sheet date but before issuance of the financial statements, a long-lived asset shall continue to be classified as held and used in those financial statements when issued. The information required by paragraph 47.a. shall be disclosed in the notes to the financial statements. If the asset (asset group) is tested for recoverability (on a held-and-used basis) as of the balance sheet date, the estimates of future

cash flows used in that test shall consider the likelihood of possible outcomes that existed at the balance sheet date, including the assessment of the likelihood of the future sale of the asset. That assessment made as of the balance sheet date shall not be revised for a decision to sell the asset after the balance sheet date. An impairment loss, if any, to be recognized shall be measured as the amount by which the carrying amount of the asset (asset group) exceeds its fair value at the balance sheet date.

Measurement

34. A long-lived asset (disposal group) classified as held for sale shall be measured at the lower of its carrying amount or fair value less cost to sell. If the asset (disposal group) is newly acquired, the carrying amount of the asset (disposal group) shall be established based on its fair value less cost to sell at the acquisition date. A long-lived asset shall not be depreciated (amortized) while it is classified as held for sale. Interest and other expenses attributable to the liabilities of a disposal group classified as held for sale shall continue to be accrued.

35. Costs to sell are the incremental direct costs to transact a sale, that is, the costs that result directly from and are essential to a sale transaction and that would not have been incurred by the entity had the decision to sell not been made. Those costs include broker commissions, legal and title transfer fees, and closing costs that must be incurred before legal title can be transferred. Those costs exclude expected future losses associated with the operations of a long-lived asset (disposal group) while it is classified as held for sale. If the sale is expected to occur beyond one year as permitted in limited situations by paragraph 31, the cost to sell shall be discounted.

36. The carrying amounts of any assets that are not covered by this Statement, including goodwill, that are included in a disposal group classified as held for sale shall be adjusted in accordance with other applicable generally accepted accounting principles prior to measuring the fair value less cost to sell of the disposal group.

37. A loss shall be recognized for any initial or subsequent write-down to fair value less cost to sell. A gain shall be recognized for any subsequent increase in fair value less cost to sell, but not in excess of the cumulative loss previously recognized (for a write-down to fair value less cost to sell). The loss or gain shall adjust only the carrying amount of a long-lived asset, whether classified as held for sale individually or as part of a disposal group. A gain or loss not previously recognized that results from the sale of a long-lived asset (disposal group) shall be recognized at the date of sale.

Changes to a Plan of Sale

38. If circumstances arise that previously were considered unlikely and, as a result, an entity decides not to sell a long-lived asset (disposal group) previously classified as held for sale, the asset (disposal group) shall be reclassified as held and used. A long-lived asset that is reclassified shall be measured individually at the lower of its (a) carrying amount before the asset (disposal group) was classified as held for sale, adjusted for any depreciation (amortization) expense that would have been recognized had the asset (disposal group) been continuously classified as held and used, or (b) fair value at the date of the subsequent decision not to sell.

39. Any required adjustment to the carrying amount of a long-lived asset that is reclassified as held and used shall be included in income from continuing operations in the period of the subsequent decision not to sell. That adjustment shall be reported in the same income statement caption used to report a loss, if any, recognized in accordance with paragraph 45. If a component of an entity is reclassified as held and used, the results of operations of the component previously reported in discontinued operations in accordance with paragraph 43 shall be reclassified and included in income from continuing operations for all periods presented.

40. If an entity removes an individual asset or liability from a disposal group previously classified as held for sale, the remaining assets and liabilities of the disposal group to be sold shall continue to be measured as a group only if the criteria in paragraph 30 are met. Otherwise, the remaining long-lived assets of the group shall be measured individually at the lower of their

carrying amounts or fair values less cost to sell at that date. Any long-lived assets that will not be sold shall be reclassified as held and used in accordance with paragraph 38.

Reporting Long-Lived Assets and Disposal Groups to Be Disposed Of

Reporting Discontinued Operations

41. For purposes of this Statement, a component of an entity comprises operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity. A component of an entity may be a reportable segment or an operating segment (as those terms are defined in paragraph 10 of Statement 131), a reporting unit (as that term is defined in Statement 142), a subsidiary, or an asset group (as that term is defined in paragraph 4).

42. The results of operations of a component of an entity that either has been disposed of or is classified as held for sale shall be reported in discontinued operations in accordance with paragraph 43 if both of the following conditions are met: (a) the operations and cash flows of the component have been (or will be) eliminated from the ongoing operations of the entity as a result of the disposal transaction and (b) the entity will not have any significant continuing involvement in the operations of the component after the disposal transaction. (Examples 12-15 of Appendix A illustrate disposal activities that do or do not qualify for reporting as discontinued operations.)

43. In a period in which a component of an entity either has been disposed of or is classified as held for sale, the income statement of a business enterprise (or statement of activities of a not-for-profit organization) for current and prior periods shall report the results of operations of the component, including any gain or loss recognized in accordance with paragraph 37, in discontinued operations. The results of operations of a component classified as held for sale shall be reported in discontinued operations in the period(s) in which they occur. The results of discontinued operations, less applicable income taxes (benefit), shall be reported as a separate component of income before extraordinary items and the cumulative effect of accounting changes (if applicable). For example, the results of discontinued operations may be reported in the income statement of a business enterprise as follows:

Income from continuing operations before income taxes	\$XXXX
Income taxes	<u>XXX</u>
Income from continuing operations 24	\$XXXX
Discontinued operations (Note X)	
Loss from operations of discontinued Component X (including loss on disposal of \$XXX)	XXXX
Income tax benefit	<u>XXXX</u>
Loss on discontinued operations	<u>XXXX</u>
Net income	<u>\$XXXX</u>

A gain or loss recognized on the disposal shall be disclosed either on the face of the income statement or in the notes to the financial statements (paragraph 47.b.).

44. Adjustments to amounts previously reported in discontinued operations that are directly related to the disposal of a component of an entity in a prior period shall be classified separately in the current period in discontinued operations. The nature and amount of such adjustments shall be disclosed. Examples of circumstances in which those types of adjustments may arise include the following:

- a. The resolution of contingencies that arise pursuant to the terms of the disposal transaction, such as the resolution of purchase price adjustments and indemnification issues with the purchaser

- b. The resolution of contingencies that arise from and that are directly related to the operations of the component prior to its disposal, such as environmental and product warranty obligations retained by the seller
- c. The settlement of employee benefit plan obligations (pension, postemployment benefits other than pensions, and other postemployment benefits), provided that the settlement is directly related to the disposal transaction.

Reporting Disposal Gains or Losses in Continuing Operations

45. A gain or loss recognized for a long-lived asset (disposal group) classified as held for sale that is not a component of an entity shall be included in income from continuing operations before income taxes in the income statement of a business enterprise and in income from continuing operations in the statement of activities of a not-for-profit organization. If a subtotal such as "income from operations" is presented, it shall include the amounts of those gains or losses.

Reporting a Long-Lived Asset or Disposal Group Classified as Held for Sale

46. A long-lived asset classified as held for sale shall be presented separately in the statement of financial position. The assets and liabilities of a disposal group classified as held for sale shall be presented separately in the asset and liability sections, respectively, of the statement of financial position. Those assets and liabilities shall not be offset and presented as a single amount. The major classes of assets and liabilities classified as held for sale shall be separately disclosed either on the face of the statement of financial position or in the notes to financial statements (paragraph 47.a.).

Disclosure

47. The following information shall be disclosed in the notes to the financial statements that cover the period in which a long-lived asset (disposal group) either has been sold or is classified as held for sale:

- a. A description of the facts and circumstances leading to the expected disposal, the expected manner and timing of that disposal, and, if not separately presented on the face of the statement, the carrying amount(s) of the major classes of assets and liabilities included as part of a disposal group
- b. The gain or loss recognized in accordance with paragraph 37 and if not separately presented on the face of the income statement, the caption in the income statement or the statement of activities that includes that gain or loss
- c. If applicable, amounts of revenue and pretax profit or loss reported in discontinued operations
- d. If applicable, the segment in which the long-lived asset (disposal group) is reported under Statement 131.

48. If either paragraph 38 or paragraph 40 applies, a description of the facts and circumstances leading to the decision to change the plan to sell the long-lived asset (disposal group) and its effect on the results of operations for the period and any prior periods presented shall be disclosed in the notes to financial statements that include the period of that decision.

RELEVANT LITERATURE

Statutory Accounting

- Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy
- *SSAP No. 3—Accounting Changes and Corrections of Errors*
- *SSAP No. 24—Discontinued Operations and Extraordinary Items*

- *SSAP No. 40—Real Estate Investments*

Generally Accepted Accounting Principles

- *FASB Statement No. 121, Accounting for the Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of*
- *FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets*

EXHIBIT A: Illustration of Marked Changes to Amended SSAPs

The following depicts the amendments made by this issue paper as “marked changes” (new text underlined and deleted text struck-through). These amendments may ultimately be revised in the final statement of statutory accounting principle.

SSAP No. 40 paragraph 9:

Properties occupied by the company and properties held for the production of income shall be carried at depreciated cost less encumbrances unless events or circumstances indicate the carrying amount of the asset (amount prior to reduction for encumbrances) may not be recoverable. Paragraph 85 of FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (FAS 144)~~FASB Statement No. 121, Accounting for the Impairment of Long-Lived Assets to be Disposed Of (FAS 121)~~, provides examples of events or changes in circumstances which indicate that the recoverability of the carrying amount of properties occupied by the company or properties held for the production of income should be assessed. If the events or changes in circumstances set forth in paragraph 85 of FAS ~~144~~144 are present or if other events or changes in circumstances indicate that the carrying amount of properties occupied by the company or properties held for the production of income may not be recoverable, the entity shall determine whether an impairment loss must be recognized in accordance with paragraph 76 of FAS ~~144~~144. In evaluating the recoverability of properties ~~occupied by the company or properties held~~ for the production of income, the reporting entity should utilize the methods of estimating future cash flows in accordance with paragraphs 16-21 of FAS 144. Property occupied by the company shall be evaluated using the asset grouping approach of ~~paragraph 8 of FAS 121~~ paragraphs 10 and 11 of FAS 144. An impairment loss is measured as the amount by which the individual carrying amounts exceed the fair value of properties occupied by the company or properties held for the production of income. Fair value is determined in accordance with paragraph 11 of SSAP No. 40~~this statement~~. If the fair value of the asset is less than the carrying value, the asset shall be written down to the fair value thereby establishing a new cost basis. The new cost basis shall not be changed for subsequent recoveries in fair value. The adjustment shall be recorded in the statement of operations as a realized loss.

SSAP No. 40 paragraph 10:

Properties that the reporting entity has the intent to sell or is required to sell shall be classified as properties held for sale and carried at the lower of depreciated cost or fair value less encumbrances and estimated costs to sell the property consistent with paragraph ~~34~~16 of FAS ~~144~~144. The intent to sell a property exists when the criteria set forth in paragraph 30 of FAS 144 are met~~management, having the authority to approve the action, has committed to a plan to dispose of the asset, either by sale or abandonment~~. Fair value of the asset shall be determined in accordance with paragraph 11 of SSAP No. 40~~this statement~~. Subsequent revisions to the fair value of the asset shall be accounted for in accordance with paragraph ~~37~~17 of FAS 144, as modified by this issue paper ~~121~~.

SSAP No. 40 paragraph 19:

~~An entity that recognizes an impairment loss shall disclose all of the following in financial statements that include the period of the impairment write-down:~~

- a. ~~A description of the impaired assets and the facts and circumstances leading to the impairment;~~
- b. ~~The amount of the impairment loss and how fair value was determined; and~~

e. ~~The caption in the statement of operations in which the impairment loss is aggregated.~~

An entity that recognizes an impairment loss shall disclose all of the following in financial statements that include the period of the impairment write-down:

- a. A description of the impaired assets and the facts and circumstances leading to the impairment;
- b. The amount of the impairment loss and how fair value was determined; and
- c. The caption in the statement of operations in which the impairment loss is aggregated.

In the period in which a property classified as held for sale has either been sold or is classified as held for sale, the reporting entity shall disclose the following:

- a. A description of the facts and circumstances leading to the expected disposal, the expected manner and timing of that disposal; and
- b. If applicable, the gain or loss recognized and if not separately presented on the face of the statement of operations, the caption in the statement of operations that includes that gain or loss.

If the reporting entity makes changes to a plan of sale in accordance with paragraphs 38 and 40 of FAS 144, in the period of that decision the reporting entity shall disclose a description of the facts and circumstances leading to the decision to change the plan to sell the asset and its effect on the results of operations for the period and any prior periods presented.

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