

**Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A**

Issue: ASU 2023-01, Leases (Topic 842), Common Control Arrangements

Check (applicable entity):

| | P/C | Life | Health |
|-------------------------------|-------------------------------------|-------------------------------------|-------------------------------------|
| Modification of Existing SSAP | <input checked="" type="checkbox"/> | <input checked="" type="checkbox"/> | <input checked="" type="checkbox"/> |
| New Issue or SSAP | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| Interpretation | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

Description of Issue: In March 2023, the Financial Accounting Standards Board (FASB) issued *Accounting Standard Update (ASU) 2023-01, Leases (Topic 842), Common Control Arrangements*. This ASU was issued as part of FASB’s post-implementation review to address issues that have been found during the implementation of the new lease guidance from *ASU 2016-02, Leases (Topic 842)*. As a reminder, ASU 2016-02 was rejected for statutory accounting and the operating lease treatment was retained.

ASU 2023-01 focuses on two issues that are both related to private company stakeholders’ concerns about applying Topic 842 to related party arrangements between entities under common control. The first issue provides a practical expedient for private companies and not-for-profit entities that are not conduit bond obligors to use the written terms and conditions of a common control arrangement to determine 1) whether a lease exists and, if so, 2) the classification of and accounting for that lease. The practical expedient may be applied on an arrangement-by-arrangement basis. If no written terms and conditions exist (including in situations in which an entity does not document existing unwritten terms and conditions in writing upon transition to the practical expedient), an entity is prohibited from applying the practical expedient and must evaluate the enforceable terms and conditions to apply Topic 842. The new U.S. GAAP guidance for this issue is only applicable to non-public entities.

The second issue involves the accounting for leasehold improvements associated with a lease between entities under common control. U.S. GAAP guidance for life of leasehold improvements prior to this update generally agrees to statutory accounting. It was noted in the ASU that private company stakeholders were concerned that amortizing leasehold improvements associated with arrangements between entities under common control determined to be leases (hereinafter referred to as common control leases) over a period shorter than the expected useful life of the leasehold improvements might result in financial reporting that do not faithfully represent the economics of those leasehold improvements, particularly in common control leases with short lease terms. While this issue originally came from private company stakeholder comments, the guidance for this issue is applicable for all lessees that are party to a lease between entities under common control in which there are leasehold improvements.

Existing Authoritative Literature:

The ASUs related to Topic 842 have previously been rejected in *SSAP No. 22R—Leases*. Guidance for leasehold improvements is included in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements* and *SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities*, and guidance for related parties is included in *SSAP No. 25—Affiliates and Other Related Parties*.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): ASC Topic 842 was the result of a joint project between FASB and the International Accounting Standards Board.

Staff Recommendation:

NAIC staff recommends the Working Group move this item to the active listing of the maintenance agenda categorized as a SAP clarification and expose revisions to adopt, with modification, ASU 2023-01 in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements* and *SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities*, as illustrated in the Form A. The proposed revisions reject the practical expedient for private companies and not-for-profit entities but recommend adoption of the leasehold improvement guidance from the ASU, with modification to the language to align with existing guidance in *SSAP No. 19* and *SSAP No. 73*.

SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements

5. Leasehold improvements that increase the value and enhance the usefulness of the leased asset meet the definition of assets established in *SSAP No. 4*. Within that definition, such items also meet the criteria defining nonadmitted assets. Accordingly, such assets shall be reported as nonadmitted assets and charged against surplus. These nonadmitted assets shall be amortized against net income over the shorter of their estimated useful life or the remaining lease term as defined in *SSAP No. 22R*. [Leasehold improvements associated with a lease between entities under common control shall be amortized over the useful life of those improvements to the holding company group as long as the lessee controls the use of the underlying asset through a lease. If the lessor obtained the right to control the use of the underlying asset through a lease with another entity not within the same holding company group, the amortization period shall not exceed the amortization period of the holding company group.](#) Leasehold improvements that do not meet the definition of assets shall be charged to expense when acquired. The amortization of leasehold improvements (including property improvements and integral equipment) shall cease, with any remaining amount immediately expensed, in any event in which the lease is terminated in advance of the lease term. This includes situations in which leased real estate is acquired by the reporting entity lessee. Such improvements related to the functionality of health care delivery assets shall follow the accounting, reporting and impairment guidance in *SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities*, and an exception to the application of this guidance to leasehold improvements necessary for the functionality of health care delivery assets is included in *SSAP No. 73*. If leased real estate is acquired, recognition of the real estate shall follow the provisions in *SSAP No. 40R—Real Estate Investments*.

20. [This statement adopts, with modification, ASU 2023-01, Leases \(Topic 842\), Common Control Arrangements. The practical expedient for private companies and not-for-profit entities that are not conduit bond obligors to use the written terms and conditions of a common control arrangement is rejected for statutory accounting. The guidance for lessees that are a party to a lease between entities under common control in which there are leasehold improvements is adopted, with modification to align with existing statutory guidance.](#)

SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities

9. Furniture, medical equipment and fixtures, and leasehold improvements shall be depreciated over their estimated useful lives but for a period not to exceed three years, except for a leasehold improvement which shall be amortized against net income over the shorter of its estimated useful life or the remaining lease term, using methods detailed in *SSAP No. 19*. [Leasehold improvements associated with a lease between entities under common control shall be amortized over the useful life of those improvements to the holding company group as long as the lessee controls the use of the underlying asset through a lease. If the lessor obtained the right to control the use of the underlying asset through a lease with another entity not within the same holding company group, the amortization period shall not exceed the amortization period of the holding company group.](#) The amortization of leasehold improvements (including property improvements and integral equipment) shall cease, with any remaining amount immediately expensed, in any event in which the lease is terminated in advance of the lease term. This includes situations in which leased real estate is acquired by the reporting entity lessee but excludes situations where the real estate lease agreement has a purchase option that contains language that allows leasehold improvements necessary for the functionality of specific health care delivery assets to be excluded from the purchase cost of the real estate. Upon acquisition, such leasehold improvements necessary for the functionality of healthcare delivery assets shall follow the guidance for health care delivery assets in this statement. If

leased real estate is acquired, recognition of the real estate shall follow the provisions in SSAP No. 40R—*Real Estate Investments*.

13. This statement adopts, with modification, ASU 2023-01, Leases (Topic 842), Common Control Arrangements. The practical expedient for private companies and not-for-profit entities that are not conduit bond obligors to use the written terms and conditions of a common control arrangement is rejected for statutory accounting. The guidance for lessees that are a party to a lease between entities under common control in which there are leasehold improvements is adopted, with modification to align with existing statutory guidance.

Staff Review Completed by: Jake Stultz, NAIC Staff – February 2024

Status:

On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to adopt, with modification, *ASU 2023-01, Leases (Topic 842), Common Control Arrangements* in SSAP No. 19—*Furniture, Fixtures, Equipment and Leasehold Improvements* and SSAP No. 73—*Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities*, as illustrated above. The proposed revisions reject the practical expedient for private companies and not-for-profit entities but recommend adoption of the leasehold improvement guidance from the ASU, with modification to the language to align with existing guidance in SSAP No. 19 and SSAP No. 73.

On August 13, 2024, the Statutory Accounting Principles (E) Working Group adopted the exposed revisions which adopt with modification, as final, *ASU 2023-01, Leases (Topic 842), Common Control Arrangements* in SSAP No. 19—*Furniture, Fixtures, Equipment and Leasehold Improvements* and SSAP No. 73—*Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities*.

[https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/NationalMeetings/A.NationalMeetingMaterials/2024/08-13-24 Summer National Meeting/Adoptions/24-02 - ASU 2023-01 Leases.docx](https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/NationalMeetings/A.NationalMeetingMaterials/2024/08-13-24SummerNationalMeeting/Adoptions/24-02-ASU2023-01Leases.docx)