

# Statutory Issue Paper No. 67

## Depreciation of Property and Amortization of Leasehold Improvements

### STATUS

Finalized March 16, 1998

Original SSAP and Current Authoritative Guidance: SSAP No. 19

### Type of Issue:

Common Area

### SUMMARY OF ISSUE

1. Current statutory guidance for accounting for the depreciation of property and the amortization of leasehold improvements is provided in Chapters 4 and 9 of the Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies (P&C Accounting Practices and Procedures Manual) and Chapter 4 of the Accounting Practices and Procedures Manual for Life, Accident, and Health Insurance Companies (Life/A&H Accounting Practices and Procedures Manual). This guidance requires:

- a. The cost of directly owned property (except land), occupied by the company or held for investment, to be allocated to expense (depreciated) over the property's estimated useful life in a systematic and rational manner.
- b. The cost of nonadmitted furniture and equipment (including EDP equipment) to either be fully expensed when purchased or depreciated over the property's estimated useful life.
- c. The cost of leasehold improvements to be allocated to expense (amortized) over the term of the lease.

2. GAAP guidance for accounting for depreciation is provided in *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins* (ARB 43), Chapter 9, *Depreciation*, and *Accounting Principles Board Opinion No. 12, Omnibus Opinion - 1967* (APB 12). This guidance requires that the cost of depreciable assets, less salvage value (if any) be expensed over the estimated useful lives of the assets. GAAP guidance requires a leasehold improvement to be amortized over the remaining term of the lease or its estimated useful life, whichever is shorter.

3. The purpose of this issue paper is to establish statutory accounting principles for accounting for the depreciation of property and the amortization of leasehold improvements that are consistent with the Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy (Statement of Concepts).

4. *Issue Paper No. 16—Electronic Data Processing Equipment and Software* (Issue Paper No. 16), *Issue Paper No. 19—Furniture, Fixtures and Equipment* (Issue Paper No. 19), *Issue Paper No. 31—Leasehold Improvements Paid by the Reporting Entity as Lessee* (Issue Paper No. 31), and *Issue Paper No. 40—Real Estate Investments* (Issue Paper No. 40) each require the depreciation of these assets against net income as their estimated economic benefit expires.

### SUMMARY CONCLUSION

5. The acquisition cost of all depreciable assets, net of salvage, shall be allocated to expense over the estimated useful lives of the



- c. Paragraph 10 requires disclosures with respect to depreciable assets and depreciation and, leasehold improvements and amortization in the notes to the financial statements.
13. The statutory principles outlined in the conclusion above are consistent with the following issue papers:
- a. Issue Paper No. 4 which requires that assets be depreciated or amortized against income as the economic benefit expires.
  - b. Issue Paper No. 16 which requires that the cost of electronic data processing equipment and software be depreciated against net income as the estimated economic benefit expires.
  - c. Issue Paper No. 19 which requires that the cost of furniture, fixtures and equipment be depreciated against net income as the estimated economic benefit expires.
  - d. Issue Paper No. 31 which requires that the cost of leasehold improvements be depreciated against net income as the estimated economic benefit expires.
  - e. Issue Paper No. 40 which requires that the cost of property included in real estate investment, other than land, be depreciated over the estimated useful life.
14. This issue paper rejects Chapter 9 of ARB 43 however, it is considered appropriate to use the concepts of depreciating assets discussed in the GAAP guidance, which requires that the acquisition cost less salvage value be recorded as an expense over the estimated useful life of the asset, as the basis for the statutory guidance codified in this issue paper. Additionally, this issue paper rejects APB 12 although the disclosures required by this issue paper are consistent with the disclosures required therein.

## RELEVANT STATUTORY AND GAAP GUIDANCE

### Statutory Accounting

15. The P&C Accounting Practices and Procedures Manual, Chapter 4, Real Estate, provides the following guidance:

#### Depreciation and Amortization

The cost of property, other than land, should be depreciated over its estimated useful life. Useful lives for buildings and improvements can best be obtained from contractors, appraisers, engineers, and manufacturers. Estimates published by the Internal Revenue Service can be helpful in the selection of useful lives for specific assets. Depreciable life may at times be fixed by contract, such as in a leasehold investment.

A variety of depreciation methods is available, and a company should select the method that is most appropriate provided, however, that the method is both systematic and rational. Depreciation methods in use include the straight-line method and accelerated methods, such as sum-of-years' digits and various declining balance methods.

Because real estate leasehold improvements revert to the lessor at the end of the lease, and the lessee receives benefits from the improvements only during the life of the lease, a leasehold improvement is subject to amortization over the lease life.

The Accounting Practices and Procedures Manual for Life, Accident, and Health Insurance Companies provides identical guidance.

16. The Life/A&H Accounting Practices and Procedures Manual, Chapter 9, Nonadmitted Assets, provides the following guidance:



**RELEVANT LITERATURE****Statutory Accounting**

- Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy
- Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies, Chapters 4 and 9
- Accounting Practices and Procedures Manual for Life, Accident and Health Insurance Companies, Chapter 4
- *Issue Paper No. 3—Accounting Changes*
- *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets*
- *Issue Paper No. 16—Electronic Data Processing Equipment and Software*
- *Issue Paper No. 19—Furniture, Fixtures and Equipment*
- *Issue Paper No. 31—Leasehold Improvements Paid by the Reporting Entity as Lessee*
- *Issue Paper No. 40—Real Estate Investments*
- Emerging Accounting Issues Working Group of the Accounting Practices and Procedures (EX4) Task Force minutes 89-1
- Emerging Accounting Issues Working Group of the Accounting Practices and Procedures (EX4) Task Force minutes 89-2
- Emerging Accounting Issues Working Group of the Accounting Practices and Procedures (EX4) Task Force minutes 89-3
- Emerging Accounting Issues Working Group of the Accounting Practices and Procedures (EX4) Task Force minutes 89-4
- Emerging Accounting Issues Working Group of the Accounting Practices and Procedures (EX4) Task Force minutes 90-1
- Emerging Accounting Issues Working Group of the Accounting Practices and Procedures (EX4) Task Force minutes 90-2
- Emerging Accounting Issues Working Group of the Accounting Practices and Procedures (EX4) Task Force minutes 90-3
- Emerging Accounting Issues Working Group of the Accounting Practices and Procedures (EX4) Task Force minutes 90-4

**Generally Accepted Accounting Principles**

- *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins, Chapter 9, Depreciation*
- *Accounting Principles Board Opinion No. 12, Omnibus Opinion - 1967*

**State Regulations**

- No additional guidance obtained from state statutes or regulations.

**This page intentionally left blank.**