

# GAAP Technical and Regulatory Update

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# Introduction



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# Disclaimer

## **Keep in mind**

This presentation does not provide official Deloitte & Touche LLP interpretive accounting guidance.

The views expressed are solely those of the presenter and are not formal Deloitte & Touche LLP positions.

Check with a qualified advisor before taking any action.

# Agenda

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Real Estate Accounting Today

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FASB Update

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SEC Rulemaking Update

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Environmental, Social, and Governance (ESG) Outlook

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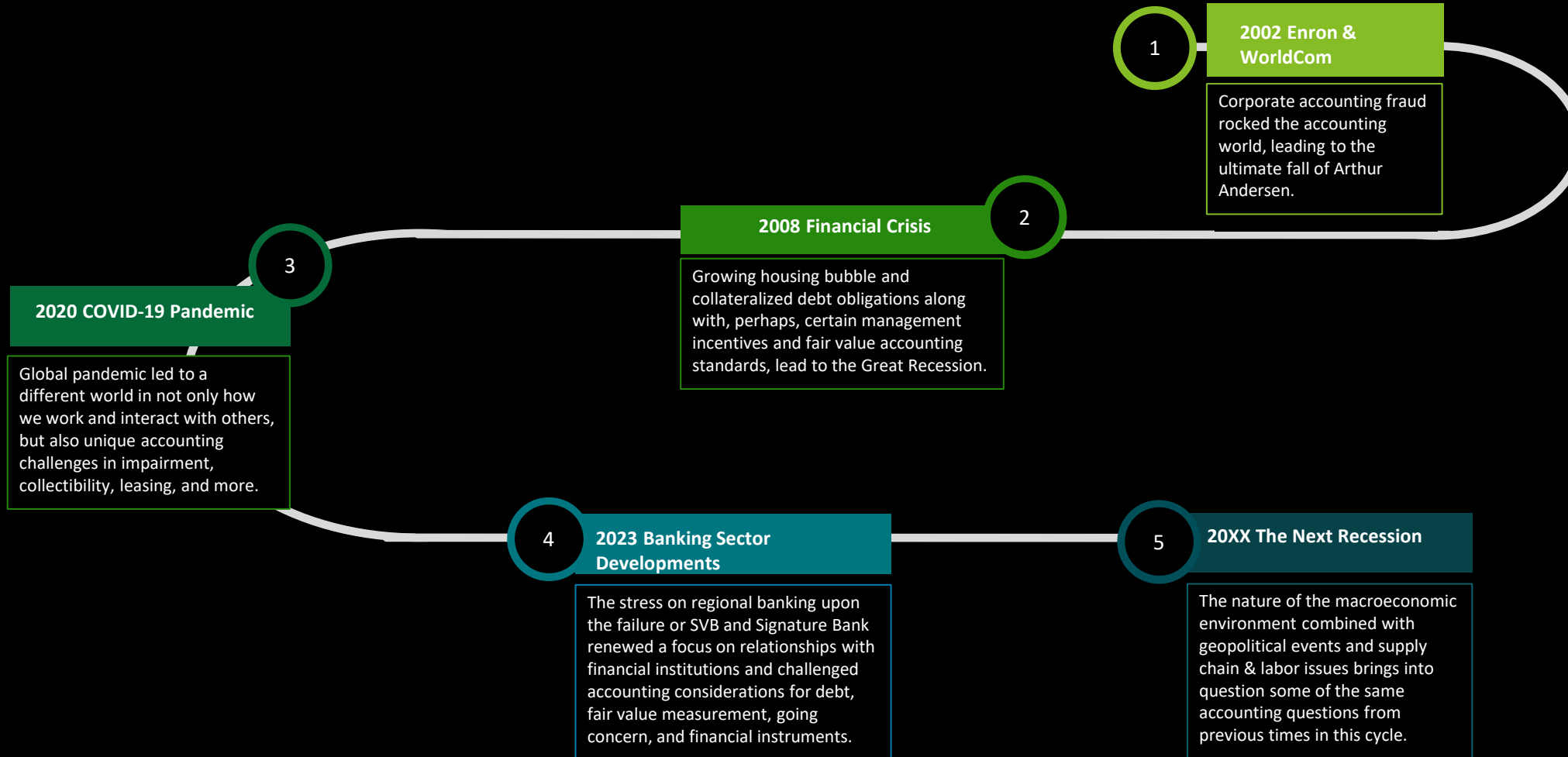
Accounting Hot Topics

# Real Estate Accounting Today

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# How Did We Get Here?

The more things change, the more they stay the same



# Real Estate Macroenvironment



Increased Costs of Capital



Changes in the Lending Environment



Evolving Real Estate Demands and Preferences

# Real Estate Accounting Considerations

- Impairment of Real Estate Assets & Held-for-Sale Accounting
- Fair Value Measurement
- Equity Method Investments & Joint Ventures
- Lease Accounting: Reduction in Lease Term and Partial Terminations
- CECL
- Going Concern

# Accounting Talent Challenges

- Number of accounting graduate and CPA candidates declining, accounting majors down 4% in 2021
- Heightened interest in other programs, including data science and analytics
- Greater focus on balancing workplace wellness programs & remote work
- *2023 State of Accounting Firms Trends Report*
  - More than 90% of accountants find it challenging or extremely challenging to hire skilled talent
  - 35% of accountants cite findings the right talent among their three biggest issues over the past year

# Technology in Accounting

- Accounting firms leveraging technology to:
  - Recruit & engage top talent
  - Effectively collaborate with client
  - Promote audit quality through machine learning, AI, and the future of work
- How we audit and use technology effectively in a world of digital assets, Blockchain, AI, and more will drive success
- *2023 State of Accounting Firms Trends Report*
  - 74% of accounting firms plan to adopt new cloud technologies over the next two years
  - 80% of accounting firms use client collaboration tools, but 52% said their client engagement process is only somewhat efficient

# FASB Update



# FASB Update

## Disaggregation – Income Statement Expenses



- Breakout expenses on the I/S based on certain expense captions:
  - Costs Expenses as Incurred
  - Costs Capitalized to Inventory
- Move additional disaggregated information to the footnotes to the financial statements

Exposure draft expected Q2 2023

## Joint venture formations



- Addresses diversity in practice in accounting for contributions made to JVs within separate joint venture financial statements
- Contributions (including identifiable assets acquired and liabilities assumed) from venturers required to be recognized at fair value

Exposure draft released  
October 2022

## Improvements to Income Tax Disclosures



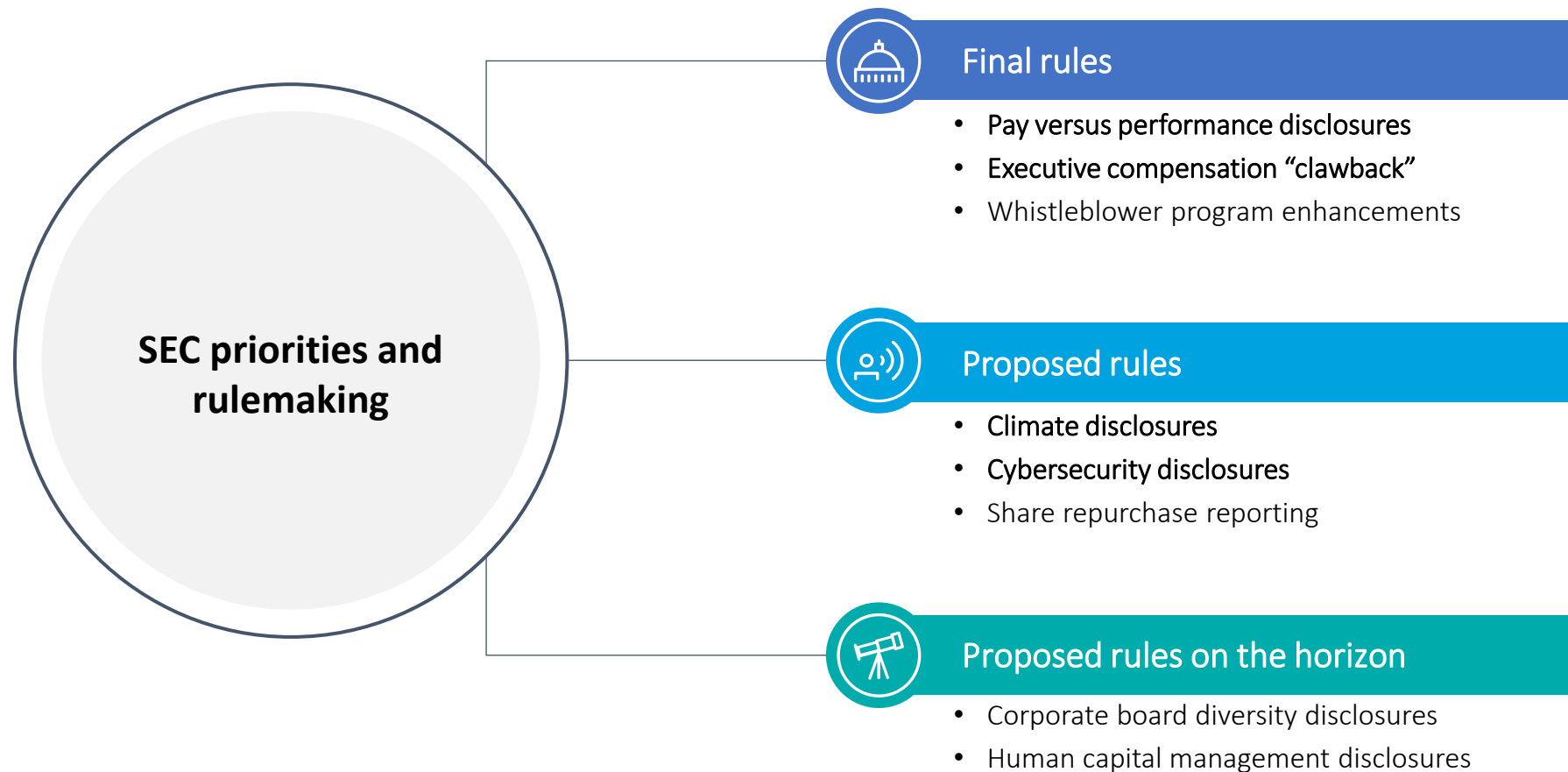
- Disclose income taxes paid disaggregated by individual jurisdiction based on a 5% quantitative threshold
- Separately disclose reconciling items within the Rate Reconciliation by nature (and jurisdiction for foreign tax effects) based on same threshold

Exposure draft released  
March 2023

# SEC Rulemaking Update



# SEC Rulemaking Update



# SEC Rulemaking Update

## Pay versus performance disclosures

<b>Description</b>	Requires certain registrants to provide disclosures about the relationship between executive pay and company performance
<b>Effective Date</b>	Fiscal years ending on or after December 16, 2022
<b>Disclosure Impact</b>	Disclosure within proxy statement of (i) certain tabular disclosures of CEO and NEO compensation, (ii) descriptions of certain compensation relationships, and (iii) list of most important measures linking executive compensation and company performance.

## Relevant Deloitte Thoughtware

[Heads Up: SEC Issues Final Rule Related to Pay Versus Performance](#)

[Heads Up: SEC Adopts Final Rule on "Clawback" Policies](#)

## Executive compensation clawback

<b>Description</b>	Requires issuers to determine and implement a policy to “claw back” excess compensation for the three fiscal years before the determination of a restatement
<b>Effective Date</b>	Company adoption no more than 60 days after the effective date of the new listing rules (policy likely in place by end of 2023 or early 2024)
<b>Disclosure Impact</b>	Disclosure of recovery policy in exhibit to its annual report  Additional disclosures required in proxy statement or annual report when a clawback occurs

# SEC Rulemaking Update



## Cybersecurity

*Fast facts*

Comment period  
closed May 9, 2022

Enhanced disclosures on cybersecurity incidents and cybersecurity risk, management, strategy, and governance







## Climate

*Fast facts*

Comment period  
closed June 17, 2022

Enhanced and standardized climate disclosures related to climate governance, risk and strategy; targets and metrics; Scopes 1, 2 and 3 GHG emissions

### For both proposals:

-  Potential impact to quarterly 10-Qs (*cybersecurity*) and annual 10-K (*cybersecurity & climate*)
-  Comment period [reopened](#) on October 7, 2022, due to a technological error, which may impact rulemaking finalization timeline
-  Disclosures will be both qualitative and quantitative
-  Impacts all types of periodic SEC filers, including domestic registrants, foreign private issuers, smaller reporting companies, and emerging growth companies

# SEC Rulemaking Update

## Non-GAAP Measures

- Misleading and tailored accounting adjustments
  - Add-back of normal recurring cash operating costs or of material operating costs
  - Adjusted revenue
  - Adjusted gross profit/gross margin/contribution margin
- Prominence and balanced presentation
- Labeling, purpose, and use
- Use of multiple segment measures

# ESG Outlook



# ESG Outlook

## 1 Climate risk management & governance

Processes for identifying, assessing, and managing climate-related risks, including:

- ✓ Whether there is system integration
- ✓ Likelihood of material impact on the business and consolidated financial statements
- ✓ Effects on strategy, business model, and outlook

Oversight and governance of climate-related risks and strategy by board of directors and management, including:

- ✓ Significant climate-related events
- ✓ Scenario analysis/modifications
- ✓ Climate risks and transition plans

## 2 Climate targets & goals

Disclosure of company climate targets and goals, including:

- ✓ **Timelines**
- ✓ **Plans** to achieve targets or goals
- ✓ **Progress** towards meeting goals
- ✓ **Internal carbon pricing** & associated disclosures
- ✓ **Carbon offset and renewable energy credit** considerations

## 3 GHG Emissions

### Scope 1 and Scope 2:

- Related to a registrant's owned or controlled operations (direct and indirect emissions)
- Disclosures must include assumptions, data sourced, and calculation methodologies

⚠ **Subject to attestation** over a **phase-in period** of 1-3 years depending on the issuer filing status.

### Scope 3

- Related to a company's indirect upstream and downstream value chains
- Disclosures required when:
  - Considered material, or
  - If Scope 3 emissions are included in GHG reduction targets

⚠ **No requirement for attestation**, and companies will have a **safe harbor** for liability. Smaller companies are exempt.

## 4 Climate-related risks & opportunities

Disclose how any climate-related risks identified have had or are likely to:

- Have a material impact on business and consolidated financials, which may manifest over the short-, medium-, or long-term
- Affect strategy, business model, and outlook

Risks include **Physical** risks & **Transition** risks.

If using an **internal carbon price**, disclose inputs, anticipated price changes, rationale for how price is determined, and how price is used to assess and manage climate-related risks.

If using a **scenario analysis**, include detail around the parameters, assumptions, analytical choices, and projected principal financial impacts.

## 5 Climate-related financial statement metrics & disclosures

Disclose the financial statement impacts of:

- Climate-related events, including severe weather events and other natural conditions
- Transition activities, including efforts to reduce GHG emissions or otherwise mitigate exposure to transition risks

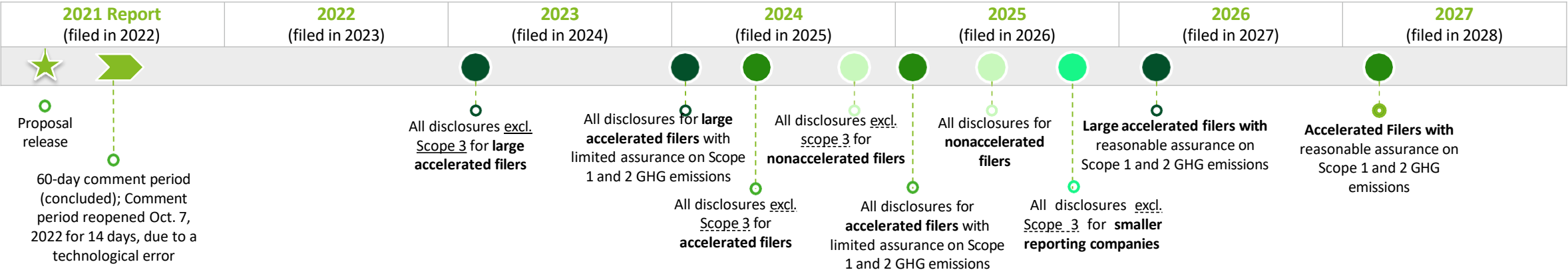
For both climate-related events and transition activities, the disclosures would include **financial impact metrics**, **expenditure metrics**, and a discussion of the impact on **financial estimates and assumptions**.

# SEC Proposal: Enhancement and Standardization of Climate-related Disclosures

## Proposed disclosure location and timeline

	Financial Statements	Outside the Financial Statements
<b>Disclosure Required</b>	For climate-related events and transition activities: (1) financial impact metrics (2) expenditure metrics (3) discussion of the impact on financial estimates and assumptions	<ul style="list-style-type: none"> <li>GHG emission disclosures for Scopes 1, 2 and 3</li> <li>Climate governance</li> <li>Climate-related risks and opportunities</li> <li>Climate risk management</li> <li>Climate targets and goals</li> </ul>
<b>Controls and procedures</b>	Subject to internal control over financial reporting	Subject to disclosure controls and procedures
<b>Attestation</b>	Part of financial statement & ICFR audit	Phase-in to reasonable assurance over Scope 1 & 2 GHG emission disclosures for large accelerated and accelerated filers

### Timeline for Proposed Climate Rule\* (Illustrative timeline for calendar year end filers)



\*Given the [reopening of the comment period](#), the implementation timeline will likely be impacted. These dates are subject to change when the SEC issues the [final rule, currently set for April 2023](#).

# Climate disclosure regulations — Mapping SEC, ISSB, and ESRS

Overview and guiding requirements from the ISSB exposure draft standards and SEC proposed climate change disclosure rule

		Regulation <i>(proposed)</i>	Standards <i>(exposure drafts)</i>
		SEC	ISSB
Guiding Requirements	Type		
	Scope		
	Materiality		
	Assurance		
Climate-Related Disclosures	Governance	<ul style="list-style-type: none"> <li>• <b>Authoritative regulatory</b> disclosure requirements</li> </ul>	<ul style="list-style-type: none"> <li>• Standards that <b>can be jurisdictionally mandated</b> through regulation</li> </ul>
	Strategy <i>Climate Risks, Opportunities</i>	<ul style="list-style-type: none"> <li>• <b>Climate-related disclosures</b> (industry-agnostic)</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Sustainability (S1) and Climate (S2) disclosures</b> (industry-specific)</li> </ul>
	Risk Management	<ul style="list-style-type: none"> <li>• <b>Investor-focused:</b> Consistent with Supreme Court's definition</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Investor-focused</b></li> </ul>
		<ul style="list-style-type: none"> <li>• <b>Limited assurance, followed by reasonable</b> (Scope 1 and 2 GHG)</li> <li>• <b>Financial statement audit/ICFR</b> (Financial Impact Metrics)</li> </ul>	<ul style="list-style-type: none"> <li>• <b>N/A, subject to jurisdictional</b> implementation requirements</li> </ul>
Climate-Related Metrics	Financial		
	GHG Emissions		
	Targets & Other Metrics		

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Climate-Related Disclosures	Governance	<ul style="list-style-type: none"> <li>• <b>Board oversight</b> of and expertise in climate-related risks</li> <li>• Process by which management informed about and monitor climate-related risks</li> </ul>	<ul style="list-style-type: none"> <li>• Reflection of risks and opportunities within the <b>board mandates and policies</b></li> <li>• Climate-related <b>remuneration policies</b></li> </ul>
	Strategy <i>Climate Risks, Opportunities</i>	<ul style="list-style-type: none"> <li>• How climate-related risks had or are likely to have material impact <b>on business or financials</b></li> <li>• Affect of risks on strategy, business model, and outlook</li> <li>• <b>Scenario analysis</b> details, if performed</li> </ul>	<ul style="list-style-type: none"> <li>• Direct and indirect <b>responses to climate risk</b></li> <li>• Changes to <b>financial position</b> and resourcing impacts</li> <li>• <b>Assets aligned with risks and opportunities</b></li> <li>• <b>Resiliency of strategy</b>, informed by scenario analysis</li> </ul>
	Risk Management	<ul style="list-style-type: none"> <li>• Processes to <b>identify, assess, and manage</b> climate risks</li> <li>• Significance and materiality of <b>climate-related risks</b></li> <li>• Consider actual or potential <b>regulations for transition risks</b></li> </ul>	<ul style="list-style-type: none"> <li>• Processes to <b>identify, assess, and manage</b> climate risks</li> <li>• Extent of <b>integration</b> into overall risk management processes</li> </ul>
Climate-Related Metrics	Financial		
	GHG Emissions		
	Targets & Other Metrics		

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Guiding Requirements	Type		
	Scope		
	Materiality		
	Assurance		
Climate-Related Disclosures	Governance		
	Strategy <i>Climate Risks, Opportunities</i>	<ul style="list-style-type: none"> <li>Financial impact and <b>expenditure metrics</b> for climate-related events and transition activities</li> <li>Impact on financial estimates and assumptions</li> </ul>	<ul style="list-style-type: none"> <li>Impact of climate-related risks and opportunities on <b>financial position</b>, performance, and cash flows for reporting period, and anticipated impacts over short, medium, and long-term</li> </ul>
	Risk Management	<ul style="list-style-type: none"> <li><b>Scope 1 and 2 GHG emissions</b></li> <li><b>Scope 3 GHG emissions, if material or Scope 3 target</b></li> <li>Gross emissions disaggregated by each GHG</li> <li>GHG emissions intensity</li> </ul>	<ul style="list-style-type: none"> <li><b>Scope 1, 2, and 3 GHG emissions required</b></li> </ul>
	Financial	<ul style="list-style-type: none"> <li>Climate-related <b>targets</b> or goals, interim targets, and supporting qualitative disclosures</li> <li>Carbon offsets or renewable energy credits (RECs)</li> </ul>	<ul style="list-style-type: none"> <li>Metrics used to assess climate risks and opportunities</li> <li>Targets, performance, and approach to target setting</li> <li><b>Industry-based metrics</b></li> </ul>
Climate-Related Metrics	GHG Emissions		
	Targets & Other Metrics		

# Preparing for the Emerging Climate Disclosure Regulations and Standards



# Accounting Hot Topics



# Demolition Cost Capitalization

ASC 970 applies to the planned demolition and redevelopment of real estate as this guidance is applicable for **project costs** or **changes in use**



## Common questions from the field

- Is it acceptable to capitalize demolition costs associated with a real estate project?
  - Yes - although there is **diversity in practice**, we believe **it is acceptable** to conclude that out-of-pocket demolition costs are a necessary cost of an **active real estate project** and thus capitalizable
- Is it acceptable to capitalize tenant buyout costs associated with an active real estate project?
  - Yes – if the tenant buy-out is deemed a **necessary cost** of the active real estate project



## Other considerations

- Not all costs incurred as part of the real estate project / demolition are capitalizable (i.e. acceleration of depreciation expense on existing real estate)

# Tax Credits

The CHIPS Act and the Inflation Reduction Act introduced clean energy tax incentives, which include direct-pay options, transferability provisions, or both

## Direct-pay option

- Allow entity to elect to treat the tax credit as a direct payment against income tax liability and claim a refund for any resulting overpayment

## Transferability provision

- Allow eligible taxpayers to elect to transfer the tax credit to unrelated entity
- Could achieve better economic benefit if insufficient taxable income or long use horizon for credit holder

# Accounting for Tenant Improvements & Lease Incentives

What is the difference between a tenant improvement and a lease incentive – and how are each of these items accounted for?

- Judgment will have to be applied to determine whether the lessee is constructing leasehold improvements or leasing built-out space
- Factors to consider:
  - Who legally owns the improvements?
  - What happens at the end of the lease? (Are the improvements removed or retained by the landlord)
  - Which party is supervising construction and bears the risk of cost overruns?

Why does it matter?

- Different income statement presentation.
- Lease incentives amortized as a reduction of rental revenue over the life of a respective lease
- Tenant improvements are amortized through depreciation expense

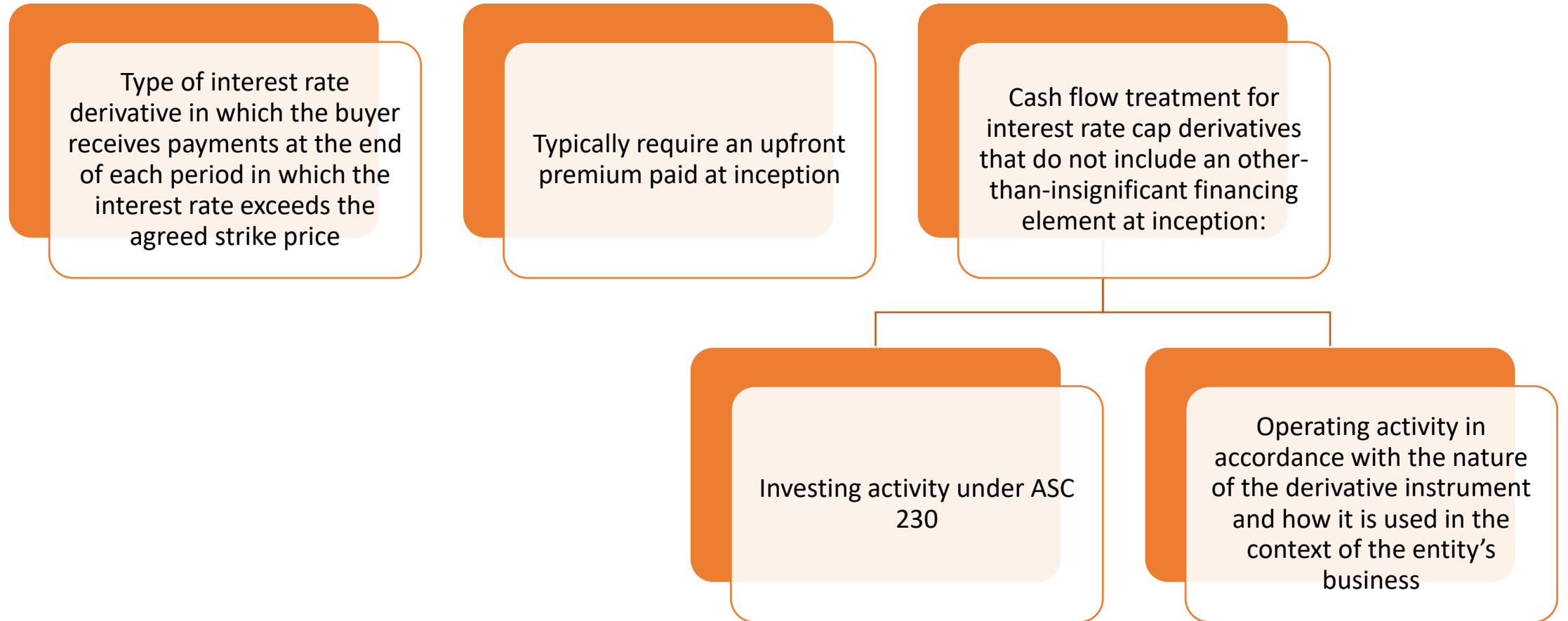
# Principal vs. Agent Accounting

- Determining whether the nature of a promise to transfer goods or services itself (as a principal) or to arrange for goods or services to be provided by another part (as an agent) can significantly impact the amount of revenue recognized under ASC 606
- Principal controls the goods or services before they are transferred to the customer and recognizes price paid by end customer as gross revenue, offset by amounts remitted to other party (as expense)
- Agent does not have control of the good or service before it is transferred to the customer and recognizes as revenue the net amount of consideration retained (after remitting amounts to other party)
- ASC 606-10-55-39 includes indicators that an entity controls a good or service before it is transferred to the customer:
  - Primary responsibility for fulfilling the good or service (including acceptability)
  - Inventory risk
  - Discretion in establishing price for the good or service

# Capitalized Interest

- ASC 835 applies to the capitalization of interest and provides scenarios for which this capitalization is required. There is additional guidance within ASC 970 on the topic that is applicable for real estate project costs
- According to ASC 835-20-15-5, interest shall be capitalized in the following scenarios:
  - Assets that are constructed for a company's own use
  - Assets that are constructed and intended for sale or lease
  - Equity method investments in which the investee is completing activities to prepare the investee for operations
- Capitalization of interest is not permitted for assets that are currently in use
- GAAP requires that companies capitalize interest (as well as insurance and real estate taxes) during periods of development / redevelopment – this is not an optional accounting policy

# Accounting for Interest Rate Caps



# Questions

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