

Invitation to Comment

The International Accounting Standards Board invites comments on the changes to IAS 40 *Investment Property* proposed in this Exposure Draft. It would particularly welcome answers to the question set out below. Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, contain a clear rationale and, when applicable, provide a suggestion for alternative wording.

The Board is not requesting comments on matters in IAS 40 not addressed in the Exposure Draft.

Question

The Exposure Draft proposes to include property under construction or development for future use as an investment property within the scope of IAS 40. Do you agree with the proposal? If not, why?

Summary of changes

The main change proposed in this Exposure Draft is to remove an inconsistency within IAS 40 *Investment Property*. At present, if an existing investment property is redeveloped, the property is accounted for using IAS 40. However, if a property is purchased for the purpose of constructing or developing a future investment property, the property is within the scope of IAS 16 *Property, Plant and Equipment* until it is complete.

The Exposure Draft proposes to remove from the scope of IAS 16, property under construction or development for future use as an investment property and include it within the scope of IAS 40. As part of these amendments, such property will be within the definition of investment property. As a result, where an entity uses the fair value model in IAS 40, changes in the fair value of such property will be included in the income statement.

A further change is proposed to paragraph 31 of IAS 40 to ensure consistency with the text of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

Proposed amendments to IAS 40 *Investment Property*

In the Standard, paragraphs 8, 9, 31, 48, 53 and 57 are amended (new text is underlined; deleted text is struck through). Paragraph 22 is deleted.

Definitions

- 8 The following are examples of investment property:
- (a) ...
 - (e) property that is being constructed or developed for future use as investment property.
- 9 The following are examples of items that are not investment property and are therefore outside the scope of this Standard:
- (a) ...
 - (d) ~~property that is being constructed or developed for future use as investment property. IAS 16 applies to such property until construction or development is complete, at which time the property becomes investment property and this Standard applies. However, this Standard applies to existing investment property that is being redeveloped for continued future use as investment property (see paragraph 58).~~
 - (e) ...

Measurement at recognition

- 22 ~~The cost of a self-constructed investment property is its cost at the date when the construction or development is complete. Until that date, an entity applies IAS 16. At that date, the property becomes investment property and this Standard applies (see paragraphs 57(e) and 65).~~

Measurement after recognition

Accounting policy

- 31 IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* states that a voluntary change in accounting policy shall be made only if the change results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows~~will result in a more appropriate presentation of transactions, other events or conditions in the entity's financial statements.~~ It is highly unlikely that a change from the fair value model to the cost model will result in a more ~~appropriate~~ relevant presentation.

Fair value model

- 48 In exceptional cases, there is clear evidence when an entity first acquires an investment property (or when an existing property first becomes investment property ~~following the completion of construction or development, or~~ after a change in use) that the variability in the range of reasonable fair value estimates will be so great, and the probabilities of the various outcomes so difficult to assess, that the usefulness of a single estimate of fair value is negated. This may indicate that the fair value of the property will not be reliably determinable on a continuing basis (see paragraph 53).

Inability to determine fair value reliably

- 53 **There is a rebuttable presumption that an entity can reliably determine the fair value of an investment property on a continuing basis. However, in exceptional cases, there is clear evidence when an entity first acquires an investment property (or when an existing property first becomes investment property ~~following the completion of construction or development, or~~ after a change in use) that the fair value of the investment property is not reliably determinable on a continuing basis. This arises when, and only when, comparable market transactions are infrequent and alternative reliable estimates of fair value (for example, based on discounted cash flow projections) are not available. In such cases, an entity shall measure that investment property using the cost model in IAS 16. The residual value of the investment property shall be assumed to be zero. The entity shall apply IAS 16 until disposal of the investment property.**

Transfers

- 57 **Transfers to, or from, investment property shall be made when, and only when, there is a change in use, evidenced by:**
- (a) ...
 - (c) **end of owner-occupation, for a transfer from owner-occupied property to investment property; or**
 - (d) **commencement of an operating lease to another party, for a transfer from inventories to investment property; ~~or~~**
 - ~~(e) **end of construction or development, for a transfer from property in the course of construction or development (covered by IAS 16) to investment property.**~~

In the Basis for Conclusions on IAS 40 (2000) *Investment Property*, the introductory paragraph, paragraphs B18, B20 and B67 are amended (new text is underlined; deleted text is struck through).

Basis for Conclusions on IAS 40 (2000) *Investment Property*

This Basis for Conclusions accompanies, but is not part of, IAS 40. It was issued by the Board of the former International Accounting Standards Committee (IASC) in 2000. Apart from the deletion of paragraphs B10–B15, B18, B20, B25, ~~and B26 and B67(b)(iv)~~, this Basis has not been revised by the IASB. Those paragraphs are no longer relevant and have been deleted to avoid the risk that they might be read out of context. In addition, the text has been annotated where references to material in other standards are no longer valid, following the revision of those standards. Reference should be made to the IASB’s Basis for Conclusions on the amendments made in 2003 and 200X.

Investment Property under Construction

- B18 ~~The Board was persuaded by this argument and concluded that investment property under construction should be excluded from the scope of this Standard and should be covered by IAS 16.~~
- B20 ~~When an entity completes the construction or development of a self-constructed investment property that will be carried at fair value, there is likely to be a difference between the fair value of the property at that date and its previous carrying amount. The Board considered two approaches to accounting for such differences under the fair value model.~~
- ~~(a) Under the first approach, the difference would be transferred to revaluation surplus. This approach would be consistent with the Standard’s approach to transfers from owner-occupied property to investment property.~~
- ~~(b) Under the second approach, the difference would be recognised in profit or loss for the period. The Board concluded that this second approach gives a more meaningful picture of performance (see paragraph 59).~~

Summary of Changes to E64

- B67(b) In relation to the scope of the Standard and the definition of investment property:
- (i) ...
- (iv) ~~property that is being constructed or developed for future use as investment property is now covered by IAS 16 and measured at cost, less impairment losses, if any (paragraph 7(d)). E64 proposed that investment property under construction should be measured at fair value; and~~
- (v) ...

Basis for Conclusions on Proposed Amendments to IAS 40 *Investment Property*

This Basis for Conclusions accompanies, but is not part of, the draft amendments.

Property being constructed or developed for future use as an investment property

- BC1 The Board noted that IASC had originally proposed to include property being constructed or developed for future use as an investment property in the scope of IAS 40 *Investment Property*. However, as a result of comments received on its Exposure Draft, IASC decided to include it within the scope of IAS 16 *Property, Plant and Equipment*. This was because of concerns about the difficulties of reliably estimating fair values of such property. However, since IAS 40 was issued, these concerns have lessened significantly as the use of fair values has become more widespread and valuation techniques have become more robust.
- BC2 In addition, the Board was concerned about the inconsistency of the accounting for the redevelopment of an existing investment property and the construction or development of a future investment property. For these reasons, the Board proposes to include both properties in the scope of IAS 40.

Appendix

Amendment to IAS 16 *Property, Plant and Equipment*

The amendment in this appendix shall be applied for annual periods beginning on or after [date to be determined]. If an entity applies the proposed amendments to IAS 40 for an earlier annual period, this amendment shall be applied for that earlier period.

A1 IAS 16 *Property, Plant and Equipment* paragraph 5 is amended as follows (deleted text is struck through):

- 5 ~~An entity shall apply this Standard to property that is being constructed or developed for future use as investment property but does not yet satisfy the definition of ‘investment property’ in IAS 40 *Investment Property*. Once the construction or development is complete, the property becomes investment property and the entity is required to apply IAS 40. IAS 40 also applies to investment property that is being redeveloped for continued future use as investment property. An entity using the cost model for investment property in accordance with IAS 40 shall use the cost model in this Standard.~~