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"OPERATING COSTS UPDATE"

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Operating Costs Update

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Are capital expenditures properly recoverable as Operating Costs? On the premise that sometimes they are, the purpose of this paper is to explore:

- the nature of capital expenditures as operating costs;
- the differences between depreciation and amortization - if any; and
- the relevance of "Generally Accepted Accounting Principles" (GAAP) as they will soon be modified by "International Financial Reporting Standards" (IFRS).

Part I – <u>Capital Expenditures/Amortization and Depreciation</u>

The definition of "Operating Costs" in most commercial leases specifically includes capital costs, although tenants generally take exception to this. Tenants maintain that they should not be responsible for capital costs, on the theory that their base rent represents the landlord's return on capital investment. If the landlord must invest more capital to preserve or enhance the value of the building, that investment must be funded through existing base rentals, not as an 'operating expense'. Landlords, of course, maintain that the problem lies in the characterization of expenses as 'capital outlays'. When landlords replace exterior cladding, resurface a parking lot, or retrofit the building's climate control equipment, they regard these expenses as ongoing operational expenses, no different than preventive maintenance or reactive repairs.

The meaning of the phrase "capital costs" and/or "costs/expenditures of a capital nature" is virtually impossible to discern from the case law. Most of the case law deals with income tax issues where the question has to do with whether certain costs (e.g. legal fees) incurred in connection with an asset are or are not part of the capital cost of the asset, but not whether the cost of the asset itself qualifies as a capital cost.

It is somewhat helpful to note that the cases all tend to rely on one ruling (*Montreal Light, Heat & Power Consolidated v. Minister of National Revenue, [1942] S.C.R. 89*) in which the usual test of whether an expenditure is one made on account of capital is expressed to be, "was the expenditure made with a view of bringing into existence an advantage for the enduring benefit of the business".

Another quandary arises from the frequent use, in many lease definitions of "Operating Costs" of the phrase "capital costs in accordance with GAAP". These add-on words suggest that some guidance is to be found in accounting materials that might spell out generally accepted accounting principles, but even the CICA Handbook does not use the term "capital costs", preferring the concept of "betterment". As to generally accepted accounting principles, these are widely recognized as not centrally documented and not very rigid, but generally requiring consistency of treatment of any given type of expense, from one year to the next. We will look into the topic of GAAP in greater detail later on in this paper.

However, the CICA Handbook does define "capital assets" as identifiable property, plant, equipment and intangible properties that:

(a) are held for use in the production or supply of goods and services, for rental to others, for administrative purposes or for the development, construction, maintenance or repair of other capital assets;
(b) have been acquired, constructed or developed with the intention of being used on a continuing basis; and
(c) are not intended for sale in the ordinary course of business.

All of the foregoing criteria must be met for the asset to be considered capital. As a corollary, we can conclude that an expenditure incurred to create, acquire or improve a capital asset would amount to a capital cost. But, an expenditure incurred to *repair* a capital asset would not qualify as a capital cost. And clearly, a cost incurred (e.g. advertising) to generate revenue or operate the business (e.g. employee wages, rent) would not constitute a capital cost. Examples of capital expenditures in the context of a commercial lease include: the installation of a new heating

system[1], the cost of replacing the majority of a roof[2], and the costs of paving, lighting and striping a parking lot that had been previously unpaved and unlit.[3]

There is often considerable debate concerning which capital costs will be included in Operating Costs under a net commercial lease and how those costs are to be passed on. The debate relates to whether capital costs will be fully charged in the year in which the cost was incurred, whether the expenditure will be amortized, whether interest will be charged on the unamortized portion, and what method of amortization will be used.

The Canadian Institute of Chartered Accountants defines amortization as "the writing off, in a rational and systematic manner over an appropriate number of accounting periods, of a balance in an account".[4] The CICA Handbook no longer uses the term "depreciation" (although it does acknowledge that amortization may also be termed, "depletion" or "depreciation") but the *Income Tax Act*[5] still does. The elimination of "depreciation", as a defined term, from the CICA Handbook is not particularly meaningful, but its absence may tend to confuse commercial lease administrators. Although pursuant to the *Income Tax Act*, expenditures on account of capital are to be "depreciated" according to schedules set out in regulations to the *Income Tax Act*, with only the "depreciated" component of the cost (plus interest on the un-depreciated capital cost) being capable of being charged against income, tax treatment is usually irrelevant to the recovery of so-called "Operating Costs" under net leases. "Operating Costs" are usually defined in commercial net leases to permit some degree of amortization (and/or "depreciation" – with the intent possibly being the same). The recoverability of such charges is entirely a function of what the lease says.

Curiously, some leases allow the recovery through Operating Costs of "amortization, but not depreciation". It appears that the intention might be to allow certain costs, incurred to replace and/or improve an asset, to be spread out and recovered over a period longer than a year, but to disallow recovery of the original cost of the initial acquisition on a 'sinking fund' basis. So for

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[1] *Tom Jones and Sons Ltd. v. Obodynski*, 1993 O.J. No. 1135 (Ont. Ct. J., Gen Div.)
[2] *Alderman Holdings Inc. v. McCutcheon Business Forms Ltd.*, [1997] O.J. No. 4386 (Ont. Ct. J., Gen Div.)
[3] *789247 Ontario Inc. v. 215 Piccadilly Properties Inc.*, [1992] O.J. No 1214 (C.A.)
[4] *Terminology for Accountants,* 4th Ed., The Canadian Institute of Chartered Accountants, 1993, p. 11.

example, we might conclude that the intention of the parties was that the initial cost of cladding an office building, or of paving a plaza parking lot, could not be "depreciated" through Operating Costs with a view to having reserve funds available (i.e., as a pre-payment) for the inevitable replacement cost that will be incurred several years later. However, where a re-cladding or re-paving becomes necessary several years after the initial capital outlay, the cost of the replacement can be "amortized" over a period. Thus, what seems to some as a distinction without a difference is an important distinction that seems to be rooted, not in accounting terminology or common law but perhaps, in a general business understanding of 'industry standards'.

The effect of amortizing or depreciating capital costs is to spread out the cost over time. The most common method of amortizing a capital expenditure is by "straight line" method to zero over the useful life of the expenditure. For purposes of leases, some landlords like to use an alternative approach to the straight-line method – they will use a "variable" or "accelerated" method. For example, if snow removal or other variable costs are low in one year, some landlords will take the opportunity to accelerate amortization so that the Operating Costs rate does not decline with the reduction in variable costs. This can lead to higher amortization charges one year than the next, but the overall Operating Costs rate remaining constant or increasing at a modest annual rate. The intent of most landlords using this method is to 'smooth'. Tenants dislike this approach as it smacks of manipulation. Moreover, if the lease stipulates that amortization is recoverable "in accordance with GAAP", it is unlikely that "smoothing" would qualify (as GAAP calls for consistency from one fiscal period to the next).

A sub-issue related to amortization arises where a tenant under a new lease pays amortization relating to an expenditure incurred prior to the lease commencement date. Some tenants maintain that such historical costs should not be payable by the tenant any more than the first tenant entering a new building would pay for the cost of constructing the building. In effect, tenants postulate that their basic rent constitute the "price of admission" for leasing the property as-is, such that its obligation under a net lease is to pay for ongoing costs of maintenance, repairs and operations incurred after the lease commencement date, but not past repairs, replacements or

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[5] R.S.C. 1985, c. 1 (5th Supp.), Section 13.

upgrades. Even a renewing tenant can argue that its renewal rent reflects the new value of the property, despite having willingly paid such amortization as a recoverable operating cost under its lease in the years/months leading up to the renewal. The main point to take from this analysis is that if the landlord wishes to recover historical amortization costs from a new tenant, the lease must expressly provide for it, as there does not seem to be any generally prevailing industry-wide view that the amortization of past expenditures is within the ordinary realm of "Operating Costs", nor is there any case law that deals with or supports this approach.

Another issue related to amortization has to do with interest. Landlords theorize that since the cost of *replacing* (or performing major repairs to) certain capital assets (e.g. roof membrane, paving) is incurred to operate the property (as distinct from costs incurred to add value to the property), this cost could be recovered as a direct charge for the full amount in the year the cost is incurred. It takes very little for landlords to conclude that, having agreed to defer the cost by recovering it through Operating Costs on an amortized basis, they should be entitled to recover an interest cost (at the prime rate from time to time, or at prime plus *x*) on the unamortized portion. It must be noted that in the absence of lease provisions expressly permitting recovery of amortization or interest on unamortized amounts, no such charges may be passed through. However, depending on how the lease is written, the full cost of a replacement may be fully recoverable in the year incurred.

Tenants take the position that basic rent should comprise their consideration paid for the use of a fully complete, properly constructed building and that any ongoing modifications to that asset should be to the account of the landlord. However, the life expectancy of certain functional components of a building is much shorter than that of the structure. For that reason, negotiations of Operating Cost provisions with strong tenants tend to centre around the inclusion or exclusion of the following capital repair or replacement items: (i) substantial re-cladding (including re-glazing), (ii) replacement or substantial rebuilding of the central chillers and boilers, elevator motors or elevator control systems, (iii) replacement of a substantial portion of the roof membrane; (iv) improvements to or upgrades of life safety, fire prevention or security systems; and (v) renovations; whereas the following items are generally not considered to be contentious: (vi) ordinary repairs and maintenance of the cladding (including glazing), (vii) periodic

replacement of insubstantial portions of exterior windows, (viii) relamping, (ix) resurfacing insubstantial portions of the parking facilities or insubstantial portions of the roof, (x) replacement of motors or compressors having a short useful life, and (xi) costs incurred for the purpose of reducing Operating Costs or for pursuing 'green initiatives'. (e.g. energy-saving equipment or conversion to achieve LEED or other 'green' designation/status[6]).

Sometimes landlords and tenants make an attempt to eliminate complexity by stipulating in the lease that any item costing in excess of a stated amount will be 'deemed capital' and require either exclusion or amortization, with the corollary that an item costing less than the stated amount will be 'deemed non-capital' and recoverable. Alas, in lease negotiations, this purportedly elegant solution is readily discredited by debating whether an expenditure is to be valued for inclusion or exclusion 'as a whole', including all project costs, or on a piecemeal basis.

We cannot leave this topic without noting that landlords also seek to recover an administrative or management fee on both the amortized component of a recoverable cost and interest on the unamortized portion. Tenants theorize that this is a gravy train, since no particular effort deserving of an administrative or management fee is required to amortize a cost or track the interest on it. While this argument may have some validity in relation to the interest component, it must be observed that the portion of the cost that is charged through, in the fiscal period, would have attracted the administrative/management fee had it been charged fully in the fiscal period incurred. Mercifully, since this paper is limited to the topic of capital expenditures as operating costs, we need not decide here whether any administrative/management fee can ever be justified.

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[6] LEED – "Leadership in Energy and Environmental Design (LEED) Green Building Rating System". For more information, please visit the website of the Canadian Green Building Council: http://www.cagbc.org/leed/what/index.php. The U.S. Green Building Council Website is: http://www.usgbc.org/. In Alberta and British Columbia, BuiltGreen Canada is available: http://www.builtgreencanada.ca/. Also refer to BOMA BEST (Building Environmental Standards) at http://www.bomabest.com/index.html.

PART II - UPCOMING IFRS CHANGES TO GAAP

To this point, we have considered capital expenditures within the context of the current business environment, which includes accounting guidelines, taxation requirements and concepts generally referred to in the Canadian commercial leasing industry. These are the main elements of the framework supporting every lease negotiation. A frustrating aspect of commercial leasing is the fact that most industry players toss jargon around as if it were a universally understood language. Unfortunately, it is usually the case that no two leasing people (nor the lawyers representing them) mean the same thing when they refer to 'depreciation' or 'amortization' or 'capital expenditures'. Further compounding the problem is that no two lease administrators who carry out the function of identifying operating costs for recovery from tenants will likely interpret the lease terms, 'depreciation', 'amortization' and 'capital expenditures' in the same way. Moreover, the vast majority of all commercial leases are hastily put together with heavy reliance on standard form wording that may be tweaked but seldom wholly re-written. The result is that the intention of the parties is seldom captured by the document nor is the document likely to be administered entirely in accordance with its wording.

Against this backdrop, we have (1) a general assumption, amongst accounting and other business personnel, that GAAP mandates a certain accounting treatment of various types of expenditures, and (2) a new development on the horizon - Canadian Generally Accepted Accounting Principles (GAAP) will be replaced with International Financial Reporting Standards (IFRS) in 2011.

To the extent that commercial leases provide for the recovery of capital expenditures in a manner that may be prescribed by GAAP, this leads to two questions:

1) What is the definition of "GAAP" and in those leases, is it static (*i.e.*, reflecting only GAAP as it exists/existed as at the date of the lease) is it fluid (*i.e.*, reflecting GAAP as amended from time to time)?

2) What will change between how GAAP records a transaction in 2010 and how that same transaction will be treated in 2011?

A lease that either defines GAAP as it exists at the time the lease is executed or is entered into prior to the adoption of IFRS will follow GAAP as outlined in the CICA Handbook. However, a new lease or an existing lease that regards GAAP as fluid will be caught by the new accounting requirements.

The application of the IFRS requirements will depend on the organization's type. In summary, there are four types of organizations:

(1) Publicly Accountable Enterprises (PAEs) are required to follow IFRS for fiscal years beginning on or after January 1, 2011.[7]

(2) Private Enterprises (PEs) have the option of adopting IFRS or the new private enterprise standards.[8]

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[7] According to the Second Omnibus Exposure Draft Issued (March 12, 2009) on the adoption of IFRSs by the Accounting Standards Board (AcSB), a PAE is an entity, other than a not-for-profit organization, or a government or other entity in the public sector that:

i) has issued, or is in the process of issuing, debt or equity instruments that are, or will be, outstanding and traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or

ii) holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses.

Banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks typically meet the second of these criteria. Other entities may also hold assets in a fiduciary capacity for a broad group of outsiders because they hold and manage financial resources entrusted to them by clients, customers or members not involved in the management of the entity. However, if an entity does so for reasons incidental to one of its primary businesses (as, for example, may be the case for some travel or real estate agents, or cooperative enterprises requiring a nominal membership deposit), it is not considered to be publicly accountable.

[8] According to the Accounting Standards Board's Exposure Draft, "*Generally Accepted Accounting Principles for Private Enterprises"* (April 2009), a PE is defined as a profit-oriented enterprise that:

i) has not issued, and is not in the process of issuing, debt or equity instruments that are, or will be, outstanding and traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); and

ii) does not hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses.

As a result of the second criteria, banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks typically are not private enterprises. Other entities may also hold assets in a fiduciary capacity for a broad group of outsiders because they hold and manage financial resources entrusted to them by clients, customers or members not involved in the management of the entity. However, if they do so for reasons incidental to

(3) Not-for-Profit Organizations will continue to apply existing accounting standards for the not-for-profit sector in the CICA Handbook until proposed new standards are finalized.

(4) Federal, Provincial, Territorial and Local Governments will follow the Public Sector Accounting Handbook; not IFRS.

Focussing on the Canadian GAAP that will be followed by PAEs and PEs that elect to adopt IFRS, the following are some of the significant differences between IFRS and the existing CICA Handbook that may impact landlords:

1) Recognition and initial measurement

Under IAS 40[9], an investment property is to be recognized as an asset if and only if probable future economic benefits will flow to the entity and the cost of the item can be measured reliably. IAS 40 is applicable in this context, because leased properties (like shopping centres and office buildings) produce investment income; they are not property used by the business (like a manufacturer uses its lands and buildings to house its factory).

An investment property shall be measured initially at its cost. Transaction costs shall be included in the initial measurement. The cost of a purchased investment property comprises its purchase price and any directly attributable expenditure. Directly attributable expenditure includes, for example, professional fees for legal services, property transfer taxes and other transaction costs. This is similar to the CICA Handbook (Section 3061[10]).

2) Measurement subsequent to initial recognition

IAS 40 permits entities to choose either:

(a) a fair value model, under which an investment property is measured, after initial measurement, at fair value with changes in fair value recognised in profit or loss; or

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their primary businesses (as, for example, may be the case for some travel or real estate agents, or cooperative enterprises requiring a nominal membership deposit), they are not considered to be publicly accountable.

[9] See attached Exhibit A

[10] See attached Exhibit B

(b) a cost model. The cost model requires an investment property to be measured, after initial measurement, at depreciated cost (less any accumulated impairment losses).[11]

By contrast, the CICA Handbook (Section 3061) requires an entity, even one that owns investment property, to carry property, plan and equipment on the cost basis subsequent to their initial recognition. Revaluation is prohibited.

3) Capital costs and repairs and maintenance

In determining the carrying amount of investment property under the fair value model, an entity does not double-count assets or liabilities that are recognised as separate assets or liabilities. For example:

(a) equipment such as elevators or air-conditioning is often an integral part of a building and is generally included in the fair value of the investment property, rather than recognized separately as property, plant and equipment.

(b) if an office is leased on a furnished basis, the fair value of the office generally includes the fair value of the furniture, because the rental income relates to the furnished office. When furniture is included in the fair value of investment property, an entity does not recognize that furniture as a separate asset.

An entity that chooses the cost model, after initial recognition, must measure all of its investment properties in accordance with the cost model (which, in general, provides that each class of property, plant and equipment be carried at cost less accumulated depreciation) and depreciate that cost over the remaining useful life.

Notably, under the fair value model, if a building's roof is replaced, the carrying amount of the building will not necessarily increase unless the new roof increases the fair value of the building. However, under the cost value model, the replacement of that same building's roof would likely increase the carrying value of the building. From a cost recovery perspective, a new lease or an existing lease that regards GAAP as fluid may be impacted by the new accounting requirements.

[11] Depreciated cost is the original cost less accumulated depreciation.

Example: after adopting the new IAS standard, a shopping centre resurfaces its parking lot at a cost of $100,000. The resurfacing has an estimated useful life of five (5) years. The shopping centre is subject to leases that provide that cost of resurfacing the parking lot, charged in accordance with GAAP, are recoverable.

Under the cost model, when the $100,000 is spent, the expenditure would be capitalized; ie. the $100,000 expenditure would be amortized over five (5) years at $20,000 per year (leaving aside any consideration of interest accruing). So, at the end of the first year, $20,000 would be amortized (including in Operating Costs) and recovered from the tenants.

Under the fair value model, there would be no amortization. Instead, the carrying value of the shopping centre at the end of the year would be compared to the fair value at the end of the prior year and any changes in fair value recognized in profit or loss. In this scenario, the $100,000 cost would likely be expensed in its entirety in the first year.

If the expenditure occurred in the year before the new IAS standard was adopted, and the Landlord used GAAP to recover $20,000 from its tenants in year 1, but then chose the fair value model upon adopting the new standard, the remaining unamortized $80,000 of resurfacing costs would likely never be recoverable.

This simplified scenario assumes that the reference in the leases to GAAP will be construed as incorporating "new GAAP" (or IFRS), whereas, it is possible that the leases might have been written to specify "GAAP as of the date hereof", and it is also possible that a court might interpret a reference to GAAP in a lease pre-dating "new GAAP" (or IFRS) as limited to GAAP as it existed as of the date of the lease.

Due to the complexity of GAAP as it will soon be modified by IFRS, not to mention the uncertainty of how GAAP might change over the term of a commercial lease, it is suggested that there are too many pitfalls associated with tying costs recoverability under commercial leases to GAAP. The determination of how and which costs should be considered as capital costs and

potentially amortized over a lease term as operating costs, should not be left to “GAAP”. It should be spelled out in clear lease terms.

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EXHIBIT A

IAS 40
Investment Property

Publisher's Note: In November 2009, the IASB issued IFRS 9 *Financial Instruments.* Entities shall apply this IFRS for annual periods beginning on or after 1 January 2013. Earlier application is permitted. If an entity applies this IFRS in its financial statements for a period beginning before 1 January 2013, it shall disclose that fact and at the same time apply the amendments in Appendix C.

Amendments made by IFRS 9 have not yet been incorporated into the Standard below. To view IFRS 9 and related amendments in PDF format, please click on the following:

- IFRS 9 Financial Instruments
- Basis for Conclusions (Appendix Amendments to the Basis for Conclusions on other IFRSs)
- Amendments to other IFRSs and guidance.

This version includes amendments resulting from IFRSs issued up to 31 December 2008.

IAS 40 *Investment Property* was issued by the International Accounting Standards Committee in April 2000.

In April 2001 the International Accounting Standards Board (IASB) resolved that all Standards and Interpretations issued under previous Constitutions continued to be applicable unless and until they were amended or withdrawn.

In December 2003 the IASB issued a revised IAS 40. Since then, IAS 40 and its accompanying documents have been amended by the following IFRSs:

- IFRS 2 *Share-based Payment* (issued February 2004)
- IFRS 4 *Insurance Contracts* (issued March 2004)
- IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* (issued March 2004)
- IAS 1 *Presentation of Financial Statements* (as revised in September 2007)1
- *Improvements to IFRSs* (issued May 2008).2

The following Interpretation refers to IAS 40 (as revised in 2003):

- SIC-21 *Income Taxes—Recovery of Revalued Non-Depreciable Assets* (issued July 2000 and subsequently amended).

International Accounting Standard 40 *Investment Property* (IAS 40) is set out in paragraphs 1–86. All the paragraphs have equal authority but retain the IASC format of the Standard when it was adopted by the IASB. IAS 40 should be read in the context of its objective and the IASB's Basis for Conclusions, the *Preface to International Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*. IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Introduction

IN1 International Accounting Standard 40 *Investment Property* (IAS 40) replaces IAS 40 *Investment Property* (issued in 2000), and should be applied for annual periods beginning on or after 1 January 2005. Earlier application is encouraged.

Reasons for revising IAS 40

IN2 The International Accounting Standards Board developed this revised IAS 40 as part of its project on Improvements to International Accounting Standards. The project was undertaken in the light of queries and criticisms raised in relation to the Standards by securities regulators, professional accountants and other interested parties. The objectives of the project were to reduce or eliminate alternatives, redundancies and conflicts within the Standards, to deal with some convergence issues and to make other improvements.

IN3 For IAS 40 the Board's main objective was a limited revision to permit a property interest held by a lessee under an operating lease to qualify as investment property under specified conditions. Those conditions include requirements that the property must otherwise meet the definition of an investment property, and that the lessee must account for the lease as if it were a finance lease and measure the resulting lease asset using the fair value model. The Board did not reconsider the fundamental approach to the accounting for investment property contained in IAS 40.

The main changes

IN4 The main changes from the previous version of IAS 40 are described below.

IN5 A property interest that is held by a lessee under an operating lease may be classified and accounted for as investment property provided that:

(a) the rest of the definition of investment property is met;

(b) the operating lease is accounted for as if it were a finance lease in accordance with IAS 17 *Leases*; and

(c) the lessee uses the fair value model set out in this Standard for the asset recognised.

IN6 The classification alternative described in paragraph IN5 is available on a property-by-property basis. However, because it is a general requirement of the Standard that all investment property should be consistently accounted for using the fair value or cost model, once this alternative is selected for one such property, all property classified as investment property is to be accounted for consistently on a fair value basis.

IN7 The Standard requires an entity to disclose:

(a) whether it applies the fair value model or the cost model; and

(b) if it applies the fair value model, whether, and in what circumstances, property interests held under operating leases are classified and accounted for as investment property.

IN8 When a valuation obtained for investment property is adjusted significantly for the purpose of the financial statements, a reconciliation is required between the valuation obtained and the valuation included in the financial statements.

IN9 The Standard clarifies that if a property interest held under a lease is classified as investment property, the item accounted for at fair value is that interest and not the underlying property.

IN10 Comparative information is required for all disclosures.

IN11 Some significant changes have been incorporated into the Standard as a result of amendments that the Board made to IAS 16 *Property, Plant and Equipment* as part of the Improvements project:

(a) to specify what costs are included in the cost of investment property and when replaced items should be derecognised;

(b) to specify when exchange transactions (ie transactions in which investment property is acquired in exchange for non-monetary assets, in whole or in part) have commercial substance and how such transactions, with or without commercial substance, are accounted for; and

(c) to specify the accounting for compensation from third parties for investment property that was impaired, lost or given up.

Summary of the approach required by the Standard

IN12 The Standard permits entities to choose either:

(a) a fair value model, under which an investment property is measured, after initial measurement, at fair value with changes in fair value recognised in profit or loss; or

(b) a cost model. The cost model is specified in IAS 16 and requires an investment property to be measured after initial measurement at depreciated cost (less any accumulated impairment losses). An entity that chooses the cost model discloses the fair value of its investment property.

IN13 The choice between the cost and fair value models is not available to a lessee accounting for a property interest held under an operating lease that it has elected to classify and account for as investment property. The Standard requires such investment property to be measured using the fair value model.

IN14 The fair value model differs from the revaluation model that is permitted for some non-financial assets. Under the revaluation model, increases in carrying amount above a cost-based measure are recognised as revaluation surplus. However, under the fair value model, all changes in fair value are recognised in profit or loss.

IN15 The Standard requires an entity to apply its chosen model to all of its investment property. However, this does not mean that all eligible operating leases must be classified as investment properties.

IN16 In exceptional cases, when an entity has adopted the fair value model, there may be 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 its fair value will not be reliably determinable on a continuing basis. In such cases, the Standard requires the entity to measure that investment property using the cost model in IAS 16 until disposal of the investment property. The residual value of the investment property is assumed to be zero.

IN17 A change from one model to the other is made only if the change results in a more relevant presentation. The Standard states that this is highly unlikely to be the case for a change from the fair value model to the cost model.

IN18 IAS 40 depends upon IAS 17 for requirements for the classification of leases, the accounting for finance and operating leases and for some of the disclosures relevant to leased investment properties. When a property interest held under an operating lease is classified and accounted for as an investment property, IAS 40 overrides IAS 17 by requiring that the lease is accounted for as if it were a finance lease. Paragraphs 14–18 of IAS 17 apply to the classification of leases of land and buildings. In particular, paragraph 18 specifies when it is not necessary to measure separately the land and building elements of such a lease.

International Accounting Standard 40
Investment Property

Objective

1 The objective of this Standard is to prescribe the accounting treatment for investment property and related disclosure requirements.

Scope

2 This Standard shall be applied in the recognition, measurement and disclosure of investment property.

3 Among other things, this Standard applies to the measurement in a lessee's financial statements of investment property interests held under a lease accounted for as a finance lease and to the measurement in a lessor's financial statements of investment property provided to a lessee under an operating lease. This Standard does not deal with matters covered in IAS 17 *Leases*, including:

(a) classification of leases as finance leases or operating leases;

(b) recognition of lease income from investment property (see also IAS 18 *Revenue*);

(c) measurement in a lessee's financial statements of property interests held under a lease accounted for as an operating lease;

(d) measurement in a lessor's financial statements of its net investment in a finance lease;

(e) accounting for sale and leaseback transactions; and

(f) disclosure about finance leases and operating leases.

4 This Standard does not apply to:

(a) biological assets related to agricultural activity (see IAS 41 *Agriculture*); and

(b) mineral rights and mineral reserves such as oil, natural gas and similar non-regenerative resources.

Definitions

5 **The following terms are used in this Standard with the meanings specified:**

Carrying amount **is the amount at which an asset is recognised in the statement of financial position.**

Cost **is the amount of cash or cash equivalents paid or the fair value of other consideration given to acquire an asset at the time of its acquisition or construction or, where applicable, the amount attributed to that asset when initially recognised in accordance with the specific requirements of other IFRSs, eg IFRS 2** ***Share-based Payment*****.**

Fair value **is the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.**

Investment property **is property (land or a building—or part of a building—or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both, rather than for:**

(a) use in the production or supply of goods or services or for administrative purposes; or

(b) sale in the ordinary course of business.

Owner-occupied property **is property held (by the owner or by the lessee under a finance lease) for use in the production or supply of goods or services or for administrative purposes.**

6 **A property interest that is held by a lessee under an operating lease may be classified and accounted for as investment property if, and only if, the property would otherwise meet the definition of an investment property and the lessee uses the fair value model set out in paragraphs 33–55 for the asset recognised. This classification alternative is available on a property-by-property basis. However, once this classification alternative is selected for one such property interest held under an operating lease, all property classified as investment property shall be accounted for using the fair value model. When**

this classification alternative is selected, any interest so classified is included in the disclosures required by paragraphs 74–78.

7 Investment property is held to earn rentals or for capital appreciation or both. Therefore, an investment property generates cash flows largely independently of the other assets held by an entity. This distinguishes investment property from owner-occupied property. The production or supply of goods or services (or the use of property for administrative purposes) generates cash flows that are attributable not only to property, but also to other assets used in the production or supply process. IAS 16 *Property, Plant and Equipment* applies to owner-occupied property.

8 The following are examples of investment property:

(a) land held for long-term capital appreciation rather than for short-term sale in the ordinary course of business.

(b) land held for a currently undetermined future use. (If an entity has not determined that it will use the land as owner-occupied property or for short-term sale in the ordinary course of business, the land is regarded as held for capital appreciation.)

(c) a building owned by the entity (or held by the entity under a finance lease) and leased out under one or more operating leases.

(d) a building that is vacant but is held to be leased out under one or more operating leases.

(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) property intended for sale in the ordinary course of business or in the process of construction or development for such sale (see IAS 2 *Inventories*), for example, property acquired exclusively with a view to subsequent disposal in the near future or for development and resale.

(b) property being constructed or developed on behalf of third parties (see IAS 11 *Construction Contracts*).

(c) owner-occupied property (see IAS 16), including (among other things) property held for future use as owner-occupied property, property held for future development and subsequent use as owner-occupied property, property occupied by employees (whether or not the employees pay rent at market rates) and owner-occupied property awaiting disposal.

(d) [deleted]

(e) property that is leased to another entity under a finance lease.

10 Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held for use in the production or supply of goods or services or for administrative purposes. If these portions could be sold separately (or leased out separately under a finance lease), an entity accounts for the portions separately. If the

portions could not be sold separately, the property is investment property only if an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes.

11 In some cases, an entity provides ancillary services to the occupants of a property it holds. An entity treats such a property as investment property if the services are insignificant to the arrangement as a whole. An example is when the owner of an office building provides security and maintenance services to the lessees who occupy the building.

12 In other cases, the services provided are significant. For example, if an entity owns and manages a hotel, services provided to guests are significant to the arrangement as a whole. Therefore, an owner-managed hotel is owner-occupied property, rather than investment property.

13 It may be difficult to determine whether ancillary services are so significant that a property does not qualify as investment property. For example, the owner of a hotel sometimes transfers some responsibilities to third parties under a management contract. The terms of such contracts vary widely. At one end of the spectrum, the owner's position may, in substance, be that of a passive investor. At the other end of the spectrum, the owner may simply have outsourced day-to-day functions while retaining significant exposure to variation in the cash flows generated by the operations of the hotel.

14 Judgement is needed to determine whether a property qualifies as investment property. An entity develops criteria so that it can exercise that judgement consistently in accordance with the definition of investment property and with the related guidance in paragraphs 7–13. Paragraph 75(c) requires an entity to disclose these criteria when classification is difficult.

15 In some cases, an entity owns property that is leased to, and occupied by, its parent or another subsidiary. The property does not qualify as investment property in the consolidated financial statements, because the property is owner-occupied from the perspective of the group. However, from the perspective of the entity that owns it, the property is investment property if it meets the definition in paragraph 5. Therefore, the lessor treats the property as investment property in its individual financial statements.

Recognition

16 Investment property shall be recognised as an asset when, and only when:

- **(a) it is probable that the future economic benefits that are associated with the investment property will flow to the entity; and**

- **(b) the cost of the investment property can be measured reliably.**

17 An entity evaluates under this recognition principle all its investment property costs at the time they are incurred. These costs include costs incurred initially to acquire an investment property and costs incurred subsequently to add to, replace part of, or service a property.

18 Under the recognition principle in paragraph 16, an entity does not recognise in the carrying amount of an investment property the costs of the day-to-day servicing of such a property. Rather, these costs are recognised in profit or loss as incurred. Costs of day-to-day servicing are primarily the cost of labour and consumables, and may include the cost of minor parts. The purpose of these expenditures is often described as for the 'repairs and maintenance' of the property.

19 Parts of investment properties may have been acquired through replacement. For example, the interior walls may be replacements of original walls. Under the recognition principle, an entity recognises in the carrying amount of an investment property the cost of replacing part of an existing investment property at the time that cost is incurred if the

recognition criteria are met. The carrying amount of those parts that are replaced is derecognised in accordance with the derecognition provisions of this Standard.

Measurement at recognition

20 An investment property shall be measured initially at its cost. Transaction costs shall be included in the initial measurement.

21 The cost of a purchased investment property comprises its purchase price and any directly attributable expenditure. Directly attributable expenditure includes, for example, professional fees for legal services, property transfer taxes and other transaction costs.

22 [Deleted]

23 The cost of an investment property is not increased by:

(a) start-up costs (unless they are necessary to bring the property to the condition necessary for it to be capable of operating in the manner intended by management),

(b) operating losses incurred before the investment property achieves the planned level of occupancy, or

(c) abnormal amounts of wasted material, labour or other resources incurred in constructing or developing the property.

24 If payment for an investment property is deferred, its cost is the cash price equivalent. The difference between this amount and the total payments is recognised as interest expense over the period of credit.

25 The initial cost of a property interest held under a lease and classified as an investment property shall be as prescribed for a finance lease by paragraph 20 of IAS 17, ie the asset shall be recognised at the lower of the fair value of the property and the present value of the minimum lease payments. An equivalent amount shall be recognised as a liability in accordance with that same paragraph.

26 Any premium paid for a lease is treated as part of the minimum lease payments for this purpose, and is therefore included in the cost of the asset, but is excluded from the liability. If a property interest held under a lease is classified as investment property, the item accounted for at fair value is that interest and not the underlying property. Guidance on determining the fair value of a property interest is set out for the fair value model in paragraphs 33–52. That guidance is also relevant to the determination of fair value when that value is used as cost for initial recognition purposes.

27 One or more investment properties may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. The following discussion refers to an exchange of one non-monetary asset for another, but it also applies to all exchanges described in the preceding sentence. The cost of such an investment property is measured at fair value unless (a) the exchange transaction lacks commercial substance or (b) the fair value of neither the asset received nor the asset given up is reliably measurable. The acquired asset is measured in this way even if an entity cannot immediately derecognise the asset given up. If the acquired asset is not measured at fair value, its cost is measured at the carrying amount of the asset given up.

28 An entity determines whether an exchange transaction has commercial substance by considering the extent to which its future cash flows are expected to change as a result of the transaction. An exchange transaction has commercial substance if:

(a) the configuration (risk, timing and amount) of the cash flows of the asset received differs from the configuration of the cash flows of the asset transferred, or

(b) the entity-specific value of the portion of the entity's operations affected by the transaction changes as a result of the exchange, and

(c) the difference in (a) or (b) is significant relative to the fair value of the assets exchanged.

For the purpose of determining whether an exchange transaction has commercial substance, the entity-specific value of the portion of the entity's operations affected by the transaction shall reflect post-tax cash flows. The result of these analyses may be clear without an entity having to perform detailed calculations.

29 The fair value of an asset for which comparable market transactions do not exist is reliably measurable if (a) the variability in the range of reasonable fair value estimates is not significant for that asset or (b) the probabilities of the various estimates within the range can be reasonably assessed and used in estimating fair value. If the entity is able to determine reliably the fair value of either the asset received or the asset given up, then the fair value of the asset given up is used to measure cost unless the fair value of the asset received is more clearly evident.

Measurement after recognition

Accounting policy

30 With the exceptions noted in paragraphs 32A and 34, an entity shall choose as its accounting policy either the fair value model in paragraphs 33–55 or the cost model in paragraph 56 and shall apply that policy to all of its investment property.

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. It is highly unlikely that a change from the fair value model to the cost model will result in a more relevant presentation.

32 This Standard requires all entities to determine the fair value of investment property, for the purpose of either measurement (if the entity uses the fair value model) or disclosure (if it uses the cost model). An entity is encouraged, but not required, to determine the fair value of investment property on the basis of a valuation by an independent valuer who holds a recognised and relevant professional qualification and has recent experience in the location and category of the investment property being valued.

32A An entity may:

(a) choose either the fair value model or the cost model for all investment property backing liabilities that pay a return linked directly to the fair value of, or returns from, specified assets including that investment property; and

(b) choose either the fair value model or the cost model for all other investment property, regardless of the choice made in (a).

32B Some insurers and other entities operate an internal property fund that issues notional units, with some units held by investors in linked contracts and others held by the entity. Paragraph 32A does not permit an entity to measure the property held by the fund partly at cost and partly at fair value.

32C If an entity chooses different models for the two categories described in paragraph 32A, sales of investment property between pools of assets measured using different models shall be recognised at fair value and the cumulative change in fair value shall be recognised in profit or loss. Accordingly, if an investment property is sold from a pool in which the fair value model is used into a pool in which the cost model is used, the property's fair value at the date of the sale becomes its deemed cost.

Fair value model

33 After initial recognition, an entity that chooses the fair value model shall measure all of its investment property at fair value, except in the cases described in paragraph 53.

34 When a property interest held by a lessee under an operating lease is classified as an investment property under paragraph 6, paragraph 30 is not elective; the fair value model shall be applied.

35 A gain or loss arising from a change in the fair value of investment property shall be recognised in profit or loss for the period in which it arises.

36 The fair value of investment property is the price at which the property could be exchanged between knowledgeable, willing parties in an arm's length transaction (see paragraph 5). Fair value specifically excludes an estimated price inflated or deflated by special terms or circumstances such as atypical financing, sale and leaseback arrangements, special considerations or concessions granted by anyone associated with the sale.

37 An entity determines fair value without any deduction for transaction costs it may incur on sale or other disposal.

38 The fair value of investment property shall reflect market conditions at the end of the reporting period.

39 Fair value is time-specific as of a given date. Because market conditions may change, the amount reported as fair value may be incorrect or inappropriate if estimated as of another time. The definition of fair value also assumes simultaneous exchange and completion of the contract for sale without any variation in price that might be made in an arm's length transaction between knowledgeable, willing parties if exchange and completion are not simultaneous.

40 The fair value of investment property reflects, among other things, rental income from current leases and reasonable and supportable assumptions that represent what knowledgeable, willing parties would assume about rental income from future leases in the light of current conditions. It also reflects, on a similar basis, any cash outflows (including rental payments and other outflows) that could be expected in respect of the property. Some of those outflows are reflected in the liability whereas others relate to outflows that are not recognised in the financial statements until a later date (eg periodic payments such as contingent rents).

41 Paragraph 25 specifies the basis for initial recognition of the cost of an interest in a leased property. Paragraph 33 requires the interest in the leased property to be remeasured, if necessary, to fair value. In a lease negotiated at market rates, the fair value of an interest in a leased property at acquisition, net of all expected lease payments (including those relating to recognised liabilities), should be zero. This fair value does not change regardless of whether, for accounting purposes, a leased asset and liability are recognised at fair value or at the present value of minimum lease payments, in accordance with paragraph 20 of IAS 17. Thus, remeasuring a leased asset from cost in

accordance with paragraph 25 to fair value in accordance with paragraph 33 should not give rise to any initial gain or loss, unless fair value is measured at different times. This could occur when an election to apply the fair value model is made after initial recognition.

42 The definition of fair value refers to 'knowledgeable, willing parties'. In this context, 'knowledgeable' means that both the willing buyer and the willing seller are reasonably informed about the nature and characteristics of the investment property, its actual and potential uses, and market conditions at the end of the reporting period. A willing buyer is motivated, but not compelled, to buy. This buyer is neither over-eager nor determined to buy at any price. The assumed buyer would not pay a higher price than a market comprising knowledgeable, willing buyers and sellers would require.

43 A willing seller is neither an over-eager nor a forced seller, prepared to sell at any price, nor one prepared to hold out for a price not considered reasonable in current market conditions. The willing seller is motivated to sell the investment property at market terms for the best price obtainable. The factual circumstances of the actual investment property owner are not a part of this consideration because the willing seller is a hypothetical owner (eg a willing seller would not take into account the particular tax circumstances of the actual investment property owner).

44 The definition of fair value refers to an arm's length transaction. An arm's length transaction is one between parties that do not have a particular or special relationship that makes prices of transactions uncharacteristic of market conditions. The transaction is presumed to be between unrelated parties, each acting independently.

45 The best evidence of fair value is given by current prices in an active market for similar property in the same location and condition and subject to similar lease and other contracts. An entity takes care to identify any differences in the nature, location or condition of the property, or in the contractual terms of the leases and other contracts relating to the property.

46 In the absence of current prices in an active market of the kind described in paragraph 45, an entity considers information from a variety of sources, including:

(a) current prices in an active market for properties of different nature, condition or location (or subject to different lease or other contracts), adjusted to reflect those differences;

(b) recent prices of similar properties on less active markets, with adjustments to reflect any changes in economic conditions since the date of the transactions that occurred at those prices; and

(c) discounted cash flow projections based on reliable estimates of future cash flows, supported by the terms of any existing lease and other contracts and (when possible) by external evidence such as current market rents for similar properties in the same location and condition, and using discount rates that reflect current market assessments of the uncertainty in the amount and timing of the cash flows.

47 In some cases, the various sources listed in the previous paragraph may suggest different conclusions about the fair value of an investment property. An entity considers the reasons for those differences, in order to arrive at the most reliable estimate of fair value within a range of reasonable fair value estimates.

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 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).

49 Fair value differs from value in use, as defined in IAS 36 *Impairment of Assets*. Fair value reflects the knowledge and estimates of knowledgeable, willing buyers and sellers. In contrast, value in use reflects the entity's estimates, including the effects of factors that may be specific to the entity and not applicable to entities in general. For example, fair value does not reflect any of the following factors to the extent that they would not be generally available to knowledgeable, willing buyers and sellers:

(a) additional value derived from the creation of a portfolio of properties in different locations;

(b) synergies between investment property and other assets;

(c) legal rights or legal restrictions that are specific only to the current owner; and

(d) tax benefits or tax burdens that are specific to the current owner.

50 In determining the carrying amount of investment property under the fair value model, an entity does not double-count assets or liabilities that are recognised as separate assets or liabilities. For example:

(a) equipment such as lifts or air-conditioning is often an integral part of a building and is generally included in the fair value of the investment property, rather than recognised separately as property, plant and equipment.

(b) if an office is leased on a furnished basis, the fair value of the office generally includes the fair value of the furniture, because the rental income relates to the furnished office. When furniture is included in the fair value of investment property, an entity does not recognise that furniture as a separate asset.

(c) the fair value of investment property excludes prepaid or accrued operating lease income, because the entity recognises it as a separate liability or asset.

(d) the fair value of investment property held under a lease reflects expected cash flows (including contingent rent that is expected to become payable). Accordingly, if a valuation obtained for a property is net of all payments expected to be made, it will be necessary to add back any recognised lease liability, to arrive at the carrying amount of the investment property using the fair value model.

51 The fair value of investment property does not reflect future capital expenditure that will improve or enhance the property and does not reflect the related future benefits from this future expenditure.

52 In some cases, an entity expects that the present value of its payments relating to an investment property (other than payments relating to recognised liabilities) will exceed the present value of the related cash receipts. An entity applies IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* to determine whether to recognise a liability and, if so, how to measure it.

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 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. If an entity determines that the fair value of an investment property under construction is not reliably determinable but expects the fair value of the property to be reliably determinable when construction is complete, it shall measure that investment property under construction at cost until either its fair value becomes reliably determinable or construction is completed (whichever is earlier). If an entity determines that the fair value of an investment property (other than an investment property under construction) is not reliably determinable on a continuing basis, the 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.

53A Once an entity becomes able to measure reliably the fair value of an investment property under construction that has previously been measured at cost, it shall measure that property at its fair value. Once construction of that property is complete, it is presumed that fair value can be measured reliably. If this is not the case, in accordance with paragraph 53, the property shall be accounted for using the cost model in accordance with IAS 16.

53B The presumption that the fair value of investment property under construction can be measured reliably can be rebutted only on initial recognition. An entity that has measured an item of investment property under construction at fair value may not conclude that the fair value of the completed investment property cannot be determined reliably.

54 In the exceptional cases when an entity is compelled, for the reason given in paragraph 53, to measure an investment property using the cost model in accordance with IAS 16, it measures at fair value all its other investment property, including investment property under construction. In these cases, although an entity may use the cost model for one investment property, the entity shall continue to account for each of the remaining properties using the fair value model.

55 If an entity has previously measured an investment property at fair value, it shall continue to measure the property at fair value until disposal (or until the property becomes owner-occupied property or the entity begins to develop the property for subsequent sale in the ordinary course of business) even if comparable market transactions become less frequent or market prices become less readily available.

Cost model

56 After initial recognition, an entity that chooses the cost model shall measure all of its investment properties in accordance with IAS 16's requirements for that model, other than those that meet the criteria to be classified as held for sale (or are included in a disposal group that is classified as held for sale) in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. Investment properties that meet the criteria to be classified as held for sale (or are included in a disposal group that is classified as held for sale) shall be measured in accordance with IFRS 5.

Transfers

57 Transfers to, or from, investment property shall be made when, and only when, there is a change in use, evidenced by:

(a) commencement of owner-occupation, for a transfer from investment property to owner-occupied property;

(b) commencement of development with a view to sale, for a transfer from investment property to inventories;

(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.**

(e) [deleted]

58 Paragraph 57(b) requires an entity to transfer a property from investment property to inventories when, and only when, there is a change in use, evidenced by commencement of development with a view to sale. When an entity decides to dispose of an investment property without development, it continues to treat the property as an investment property until it is derecognised (eliminated from the statement of financial position) and does not treat it as inventory. Similarly, if an entity begins to redevelop an existing investment property for continued future use as investment property, the property remains an investment property and is not reclassified as owner-occupied property during the redevelopment.

59 Paragraphs 60–65 apply to recognition and measurement issues that arise when an entity uses the fair value model for investment property. When an entity uses the cost model, transfers between investment property, owner-occupied property and inventories do not change the carrying amount of the property transferred and they do not change the cost of that property for measurement or disclosure purposes.

60 For a transfer from investment property carried at fair value to owner-occupied property or inventories, the property's deemed cost for subsequent accounting in accordance with IAS 16 or IAS 2 shall be its fair value at the date of change in use.

61 If an owner-occupied property becomes an investment property that will be carried at fair value, an entity shall apply IAS 16 up to the date of change in use. The entity shall treat any difference at that date between the carrying amount of the property in accordance with IAS 16 and its fair value in the same way as a revaluation in accordance with IAS 16.

62 Up to the date when an owner-occupied property becomes an investment property carried at fair value, an entity depreciates the property and recognises any impairment losses that have occurred. The entity treats any difference at that date between the carrying amount of the property in accordance with IAS 16 and its fair value in the same way as a revaluation in accordance with IAS 16. In other words:

(a) any resulting decrease in the carrying amount of the property is recognised in profit or loss. However, to the extent that an amount is included in revaluation surplus for that property, the decrease is recognised in other comprehensive income and reduces the revaluation surplus within equity.

(b) any resulting increase in the carrying amount is treated as follows:

(i) to the extent that the increase reverses a previous impairment loss for that property, the increase is recognised in profit or loss. The amount recognised in profit or loss does not exceed the amount needed to restore the carrying amount to the carrying amount that would have been determined (net of depreciation) had no impairment loss been recognised.

(ii) any remaining part of the increase is recognised in other comprehensive income and increases the revaluation surplus within equity. On subsequent disposal of the investment property, the revaluation surplus included in equity may be transferred to retained earnings. The transfer from revaluation surplus to retained earnings is not made through profit or loss.

63 For a transfer from inventories to investment property that will be carried at fair value, any difference between the fair value of the property at that date and its previous carrying amount shall be recognised in profit or loss.

64 The treatment of transfers from inventories to investment property that will be carried at fair value is consistent with the treatment of sales of inventories.

65 When an entity completes the construction or development of a self-constructed investment property that will be carried at fair value, any difference between the fair value of the property at that date and its previous carrying amount shall be recognised in profit or loss.

Disposals

66 An investment property shall be derecognised (eliminated from the statement of financial position) on disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from its disposal.

67 The disposal of an investment property may be achieved by sale or by entering into a finance lease. In determining the date of disposal for investment property, an entity applies the criteria in IAS 18 for recognising revenue from the sale of goods and considers the related guidance in the Appendix to IAS 18. IAS 17 applies to a disposal effected by entering into a finance lease and to a sale and leaseback.

68 If, in accordance with the recognition principle in paragraph 16, an entity recognises in the carrying amount of an asset the cost of a replacement for part of an investment property, it derecognises the carrying amount of the replaced part. For investment property accounted for using the cost model, a replaced part may not be a part that was depreciated separately. If it is not practicable for an entity to determine the carrying amount of the replaced part, it may use the cost of the replacement as an indication of what the cost of the replaced part was at the time it was acquired or constructed. Under the fair value model, the fair value of the investment property may already reflect that the part to be replaced has lost its value. In other cases it may be difficult to discern how much fair value should be reduced for the part being replaced. An alternative to reducing fair value for the replaced part, when it is not practical to do so, is to include the cost of the replacement in the carrying amount of the asset and then to reassess the fair value, as would be required for additions not involving replacement.

69 Gains or losses arising from the retirement or disposal of investment property shall be determined as the difference between the net disposal proceeds and the carrying amount of the asset and shall be recognised in profit or loss (unless IAS 17 requires otherwise on a sale and leaseback) in the period of the retirement or disposal.

70 The consideration receivable on disposal of an investment property is recognised initially at fair value. In particular, if payment for an investment property is deferred, the consideration received is recognised initially at the cash price equivalent. The difference between the nominal amount of the consideration and the cash price equivalent is recognised as interest revenue in accordance with IAS 18 using the effective interest method.

71 An entity applies IAS 37 or other Standards, as appropriate, to any liabilities that it retains after disposal of an investment property.

72 Compensation from third parties for investment property that was impaired, lost or given up shall be recognised in profit or loss when the compensation becomes receivable.

73 Impairments or losses of investment property, related claims for or payments of compensation from third parties and any subsequent purchase or construction of replacement assets are separate economic events and are accounted for separately as follows:

(a) impairments of investment property are recognised in accordance with IAS 36;

(b) retirements or disposals of investment property are recognised in accordance with paragraphs 66–71 of this Standard;

(c) compensation from third parties for investment property that was impaired, lost or given up is recognised in profit or loss when it becomes receivable; and

(d) the cost of assets restored, purchased or constructed as replacements is determined in accordance with paragraphs 20–29 of this Standard.

Disclosure

Fair value model and cost model

74 The disclosures below apply in addition to those in IAS 17. In accordance with IAS 17, the owner of an investment property provides lessors' disclosures about leases into which it has entered. An entity that holds an investment property under a finance or operating lease provides lessees' disclosures for finance leases and lessors' disclosures for any operating leases into which it has entered.

75 An entity shall disclose:

(a) whether it applies the fair value model or the cost model.

(b) if it applies the fair value model, whether, and in what circumstances, property interests held under operating leases are classified and accounted for as investment property.

(c) when classification is difficult (see paragraph 14), the criteria it uses to distinguish investment property from owner-occupied property and from property held for sale in the ordinary course of business.

(d) the methods and significant assumptions applied in determining the fair value of investment property, including a statement whether the determination of fair value was supported by market evidence or was more heavily based on other factors (which the entity shall disclose) because of the nature of the property and lack of comparable market data.

(e) the extent to which the fair value of investment property (as measured or disclosed in the financial statements) is based on a valuation by an independent valuer who holds a recognised and relevant professional qualification and has recent experience in the location and category of the investment property being valued. If there has been no such valuation, that fact shall be disclosed.

(f) the amounts recognised in profit or loss for:

(i) rental income from investment property;

(ii) direct operating expenses (including repairs and maintenance) arising from investment property that generated rental income during the period; and

(iii) **direct operating expenses (including repairs and maintenance) arising from investment property that did not generate rental income during the period.**

(iv) **the cumulative change in fair value recognised in profit or loss on a sale of investment property from a pool of assets in which the cost model is used into a pool in which the fair value model is used (see paragraph 32C).**

(g) **the existence and amounts of restrictions on the realisability of investment property or the remittance of income and proceeds of disposal.**

(h) **contractual obligations to purchase, construct or develop investment property or for repairs, maintenance or enhancements.**

Fair value model

76 **In addition to the disclosures required by paragraph 75, an entity that applies the fair value model in paragraphs 33–55 shall disclose a reconciliation between the carrying amounts of investment property at the beginning and end of the period, showing the following:**

(a) **additions, disclosing separately those additions resulting from acquisitions and those resulting from subsequent expenditure recognised in the carrying amount of an asset;**

(b) **additions resulting from acquisitions through business combinations;**

(c) **assets classified as held for sale or included in a disposal group classified as held for sale in accordance with IFRS 5 and other disposals;**

(d) **net gains or losses from fair value adjustments;**

(e) **the net exchange differences arising on the translation of the financial statements into a different presentation currency, and on translation of a foreign operation into the presentation currency of the reporting entity;**

(f) **transfers to and from inventories and owner-occupied property; and**

(g) **other changes.**

77 **When a valuation obtained for investment property is adjusted significantly for the purpose of the financial statements, for example to avoid double-counting of assets or liabilities that are recognised as separate assets and liabilities as described in paragraph 50, the entity shall disclose a reconciliation between the valuation obtained and the adjusted valuation included in the financial statements, showing separately the aggregate amount of any recognised lease obligations that have been added back, and any other significant adjustments.**

78 **In the exceptional cases referred to in paragraph 53, when an entity measures investment property using the cost model in IAS 16, the reconciliation required by paragraph 76 shall disclose amounts relating to that investment property separately from amounts relating to other investment property. In addition, an entity shall disclose:**

(a) a description of the investment property;

(b) an explanation of why fair value cannot be determined reliably;

(c) if possible, the range of estimates within which fair value is highly likely to lie; and

(d) on disposal of investment property not carried at fair value:

(i) the fact that the entity has disposed of investment property not carried at fair value;

(ii) the carrying amount of that investment property at the time of sale; and

(iii) the amount of gain or loss recognised.

Cost model

79 In addition to the disclosures required by paragraph 75, an entity that applies the cost model in paragraph 56 shall disclose:

(a) the depreciation methods used;

(b) the useful lives or the depreciation rates used;

(c) the gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the period;

(d) a reconciliation of the carrying amount of investment property at the beginning and end of the period, showing the following:

(i) additions, disclosing separately those additions resulting from acquisitions and those resulting from subsequent expenditure recognised as an asset;

(ii) additions resulting from acquisitions through business combinations;

(iii) assets classified as held for sale or included in a disposal group classified as held for sale in accordance with IFRS 5 and other disposals;

(iv) depreciation;

(v) the amount of impairment losses recognised, and the amount of impairment losses reversed, during the period in accordance with IAS 36;

(vi) the net exchange differences arising on the translation of the financial statements into a different presentation currency, and on translation of a foreign operation into the presentation currency of the reporting entity;

(vii) transfers to and from inventories and owner-occupied property; and

(viii) other changes; and

(e) the fair value of investment property. In the exceptional cases described in paragraph 53, when an entity cannot determine the fair value of the investment property reliably, it shall disclose:

(i) a description of the investment property;

(ii) an explanation of why fair value cannot be determined reliably; and

(iii) if possible, the range of estimates within which fair value is highly likely to lie.

Transitional provisions

Fair value model

80 An entity that has previously applied IAS 40 (2000) and elects for the first time to classify and account for some or all eligible property interests held under operating leases as investment property shall recognise the effect of that election as an adjustment to the opening balance of retained earnings for the period in which the election is first made. In addition:

(a) if the entity has previously disclosed publicly (in financial statements or otherwise) the fair value of those property interests in earlier periods (determined on a basis that satisfies the definition of fair value in paragraph 5 and the guidance in paragraphs 36–52), the entity is encouraged, but not required:

(i) to adjust the opening balance of retained earnings for the earliest period presented for which such fair value was disclosed publicly; and

(ii) to restate comparative information for those periods; and

(b) if the entity has not previously disclosed publicly the information described in (a), it shall not restate comparative information and shall disclose that fact.

81 This Standard requires a treatment different from that required by IAS 8. IAS 8 requires comparative information to be restated unless such restatement is impracticable.

82 When an entity first applies this Standard, the adjustment to the opening balance of retained earnings includes the reclassification of any amount held in revaluation surplus for investment property.

Cost model

83 IAS 8 applies to any change in accounting policies that is made when an entity first applies this Standard and chooses to use the cost model. The effect of the change in accounting policies includes the reclassification of any amount held in revaluation surplus for investment property.

84 The requirements of paragraphs 27–29 regarding the initial measurement of an investment property acquired in an exchange of assets transaction shall be applied prospectively only to future transactions.

Effective date

85 An entity shall apply this Standard for annual periods beginning on or after 1 January 2005. Earlier application is encouraged. If an entity applies this Standard for a period beginning before 1 January 2005, it shall disclose that fact.

85A IAS 1 *Presentation of Financial Statements* (as revised in 2007) amended the terminology used throughout IFRSs. In addition it amended paragraph 62. An entity shall apply those amendments for annual periods beginning on or after 1 January 2009. If an entity applies IAS 1 (revised 2007) for an earlier period, the amendments shall be applied for that earlier period.

85B Paragraphs 8, 9, 48, 53, 54 and 57 were amended, paragraph 22 was deleted and paragraphs 53A and 53B were added by *Improvements to IFRSs* issued in May 2008. An entity shall apply those amendments prospectively for annual periods beginning on or after 1 January 2009. An entity is permitted to apply the amendments to investment property under construction from any date before 1 January 2009 provided that the fair values of investment properties under construction were determined at those dates. Earlier application is permitted. If an entity applies the amendments for an earlier period it shall disclose that fact and at the same time apply the amendments to paragraphs 5 and 81E of IAS 16 *Property, Plant and Equipment*.

Withdrawal of IAS 40 (2000)

86 This Standard supersedes IAS 40 *Investment Property* (issued in 2000).

Approval by the Board of IAS 40 issued in December 2003

International Accounting Standard 40 *Investment Property* (as revised in 2003) was approved for issue by the fourteen members of the International Accounting Standards Board.

Sir David Tweedie	Chairman
Thomas E Jones	Vice-Chairman
Mary E Barth	
Hans-Georg Bruns	
Anthony T Cope	
Robert P Garnett	
Gilbert Gélard	
James J Leisenring	
Warren J McGregor	
Patricia L O'Malley	

Harry K Schmid

John T Smith

Geoffrey Whittington

Tatsumi Yamada

Footnotes

1 effective date 1 January 2009

2 effective date 1 January 2009

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Exhibit B

SPECIFIC ITEMS
SECTION 3061
property, plant and equipment

Additional Resources

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PURPOSE AND SCOPE

.01 This Section establishes standards for the recognition, measurement, presentation and disclosure of property, plant and equipment (tangible capital assets) by profit-oriented enterprises. This Section applies to property, plant and equipment recognized under LEASES, Section 3065. Not-for-profit organizations would account for property, plant and equipment in accordance with CAPITAL ASSETS HELD BY NOT-FOR-PROFIT ORGANIZATIONS, Section 4430.

.02 This Section does not deal with goodwill or intangible assets (see GOODWILL AND INTANGIBLE ASSETS, Section 3064), with the impairment of property, plant and equipment (see IMPAIRMENT OF LONG-LIVED ASSETS, Section 3063) or with the disposal of property, plant and equipment (see DISPOSAL OF LONG-LIVED ASSETS AND DISCONTINUED OPERATIONS, Section 3475). This Section also does not deal with special circumstances when it may be appropriate to undertake a comprehensive revaluation of all the assets and liabilities of an enterprise (see COMPREHENSIVE REVALUATION OF ASSETS AND LIABILITIES, Section 1625).

DEFINITIONS

.03 The definitions that follow have been adopted for the purposes of this Section.

.04 **Property, plant and equipment** are identifiable tangible assets that meet all of the following criteria:

(a) are held for use in the production or supply of goods and services, for rental to others, for administrative purposes or for the development, construction, maintenance or repair of other property, plant and equipment;

(b) have been acquired, constructed or developed with the intention of being used on a continuing basis; and

(c) are not intended for sale in the ordinary course of business.

Spare parts and servicing equipment are usually carried as inventory and recognized in net income as consumed. However, major spare parts and standby equipment qualify as property, plant and equipment when an entity expects to use them during more than one period. Similarly, if the spare parts and servicing equipment can be used only in connection with an item of property, plant and equipment, they are accounted for as property, plant and equipment. Property, plant and equipment and intangible assets, as defined in GOODWILL AND INTANGIBLE ASSETS, paragraph 3064.08, are referred to collectively as "capital assets".

.05 **Cost** is the amount of consideration given up to acquire, construct, develop, or better an item of property, plant and equipment and includes all costs directly attributable to the acquisition, construction, development or betterment of the asset including installing it at the location and in the condition necessary for its intended use. Cost includes any asset retirement cost accounted for in accordance with ASSET RETIREMENT OBLIGATIONS, Section 3110.

.06 **Mining properties** are items of property, plant and equipment represented by the capitalized costs of acquired mineral rights and the costs associated with exploration for and development of mineral reserves.

.07 **Net carrying amount** of an item of property, plant and equipment is cost less both accumulated amortization and the amount of any write-downs.

.08 **Net recoverable amount** of an item of property, plant and equipment is its estimated future net cash flow from use together with its residual value.

.09 **Oil and gas properties** are items of property, plant and equipment represented by the capitalized costs of acquired oil and gas rights and the costs associated with exploration for and development of oil, gas and related reserves.

.10 **Rate-regulated property, plant and equipment** are items of property, plant and equipment held for use in operations meeting all of the following criteria:

(a) The rates for regulated services or products provided to customers are established by or are subject to approval by a regulator or a governing body empowered by statute or contract to establish rates to be charged for services or products.

(b) The regulated rates are designed to recover the cost of providing the services or products.

(c) It is reasonable to assume that rates set at levels that will recover the cost can be charged to and collected from customers in view of the demand for the services or products and the level of direct and indirect competition. This criterion requires consideration of expected changes in levels of demand or competition during the recovery period for any capitalized costs.

.11 **Rental real estate** is real estate held primarily to generate income through rental to others (i.e., not held for sale in the ordinary course of business). It includes rental property under development and developed property that is intended to be held for rental. In addition, it includes land designated for development as rental property.

.12 **Residual value** is the estimated net realizable value of an item of property, plant and equipment at the end of its useful life to an enterprise.

.13 **Salvage value** is the estimated net realizable value of an item of property, plant and equipment at the end of its life. Salvage value is normally negligible.

.14 **Service potential** is used to describe the output or service capacity of an item of property, plant and equipment and is normally determined by reference to attributes such as physical output capacity, associated operating costs, useful life and quality of output.

.15 **Useful life** is the period over which an asset, singly or in combination with other assets, is expected to contribute directly or indirectly to the future cash flows of an enterprise.

MEASUREMENT

Cost

.16 ♦ *Property, plant and equipment should be recorded at cost.* [DEC. 1990]

.17 The cost of an item of property, plant and equipment includes the purchase price and other acquisition costs such as option costs when an option is exercised, brokers' commissions, installation costs including architectural, design and engineering fees, legal fees, survey costs, site preparation costs, freight charges, transportation insurance costs, duties, testing and preparation charges. In addition, if the cost of the asset acquired other than through a business combination is different from its tax basis on acquisition, the asset's cost would be adjusted to reflect the related future income tax consequences (see INCOME TAXES, Section 3465). It may be appropriate to group together individually insignificant items of property, plant and equipment.

.18 The cost of each item of property, plant and equipment acquired as part of a basket purchase (i.e., when a group of assets is acquired for a single amount), is determined by allocating the price paid for the basket to each item on the basis of its relative fair value at the time of acquisition.

.19 When, at the time of acquisition, a portion of the acquired item of property, plant and equipment meets the criteria in DISPOSAL OF LONG-LIVED ASSETS AND DISCONTINUED OPERATIONS, Section 3475, to be classified as held for sale at the acquisition date, that portion of the item is measured at fair value less cost to sell. The remainder of the acquired item is measured at the cost of acquisition of the entire item less the amount assigned to the portion to be sold. For example, if a portion of land acquired is to be resold, the cost of the land to be retained would be the total cost of the purchase minus the fair value less cost to sell of the portion of land held for sale. When, at the time of acquisition, a portion of the acquired item of property, plant and equipment is not intended for use because it will be abandoned, its cost and any costs of disposal, net of any estimated proceeds, are attributed to that portion of the acquired asset which is intended for use. For example, the cost of acquired land that includes a building which will be demolished, comprises the cost of the acquired property and the cost of demolishing the building.

Acquisition, construction or development over time

.20 The cost of an item of property, plant and equipment includes direct construction or development costs (such as materials and labour), and overhead costs directly attributable to the construction or development activity.

.21 For a mining property, the cost of the asset includes exploration costs if the enterprise considers that such costs have the characteristics of property, plant and equipment. An enterprise applies the method of accounting for exploration costs that it considers to be appropriate to its operations and applies the method consistently to all its properties.

.22 For an oil and gas property, the cost of the asset comprises acquisition costs, development costs and certain exploration costs depending on whether the enterprise accounts for its oil and gas properties using the full cost method or the successful efforts method. An enterprise applies the method of accounting for acquisition, exploration and development costs that it considers to be appropriate to its operations and applies the method consistently to all its properties.

.23 The cost of an item of property, plant and equipment that is acquired, constructed, or developed over time includes carrying costs directly attributable to the acquisition, construction, or development activity such as interest costs when the enterprise's accounting policy is to capitalize interest costs. For an item of rate-regulated property, plant and equipment, the cost includes the directly attributable allowance for funds used during construction allowed by the regulator.

.24 Capitalization of carrying costs ceases when an item of property, plant and equipment is substantially complete and ready for productive use. Determining when an asset, or a portion thereof, is substantially complete and ready for productive use requires consideration of the circumstances and the industry in which it is to be operated. Normally it would be predetermined by management with reference to such factors as productive capacity, occupancy level, or the passage of time.

.25 Net revenue or expense derived from an item of property, plant and equipment prior to substantial completion and readiness for use is included in the cost.

Betterment

.26 The cost incurred to enhance the service potential of an item of property, plant and equipment is a betterment. Service potential may be enhanced when there is an increase in the previously assessed physical output or service capacity, associated operating costs are lowered, the life or useful life is extended, or the quality of output is improved. The cost incurred in the maintenance of the service potential of an item of property, plant and equipment is a repair, not a betterment. If a cost has the attributes of both a repair and a betterment, the portion considered to be a betterment is included in the cost of the asset.

.27 A redevelopment project that adds significant economic value to rental real estate is treated as a betterment. When a building is removed for the purpose of redevelopment of rental real estate, the net carrying amount of the building is included in the cost of the redeveloped property, as long as the net amount considered recoverable from the redevelopment project exceeds its cost.

Amortization

.28 ♦ *Amortization should be recognized in a rational and systematic manner appropriate to the nature of an item of property, plant and equipment with a limited life and its use by the enterprise. The amount of amortization that should be charged to income is the greater of:*

(a) the cost less salvage value over the life of the asset; and

(b) the cost less residual value over the useful life of the asset. [DEC. 1990]

.29 Property, plant and equipment is acquired to earn income or supply a service over its useful life. An item of property, plant and equipment, other than land that normally has an unlimited life, has a limited life. Its useful life is normally the shortest of its physical, technological, commercial and legal life. Amortization is the charge to income that recognizes that life is finite and that the cost less salvage value or residual value of an item of

property, plant and equipment is allocated to the periods of service provided by the asset. Amortization may also be termed depreciation or depletion.

.30 The cost of an item of property, plant and equipment made up of significant separable component parts is allocated to the component parts when practicable and when estimates can be made of the lives of the separate components. For example, initial leasing costs may be identifiable as a separable component of the cost of rental real estate and engines may be a separable component of an aircraft.

.31 Different methods of amortizing an item of property, plant and equipment result in different patterns of charges to income. The objective is to provide a rational and systematic basis for allocating the amortizable amount of an item of property, plant and equipment over its estimated life and useful life. A straight-line method reflects a constant charge for the service as a function of time. A variable charge method reflects service as a function of usage. Other methods may be appropriate in certain situations. For example, an increasing charge method may be used when an enterprise can price its goods or services so as to obtain a constant rate of return on the investment in the asset; a decreasing charge method may be appropriate when the operating efficiency of the asset declines over time.

.32 Factors to be considered in estimating the life and useful life of an item of property, plant and equipment include expected future usage, effects of technological or commercial obsolescence, expected wear and tear from use or the passage of time, the maintenance program, results of studies made regarding the industry, studies of similar items retired, and the condition of existing comparable items. As the estimate of the life of an item of property, plant and equipment is extended into the future, it becomes increasingly difficult to identify a reasonable basis for estimating the life.

Review of amortization

.33 ♦ *The amortization method and estimates of the life and useful life of an item of property, plant and equipment should be reviewed on a regular basis.* [DEC. 1990]

.34 Significant events that may indicate a need to revise the amortization method or estimates of the life and useful life of an item of property, plant and equipment include:

(a) a change in the extent the asset is used;

(b) a change in the manner in which the asset is used;

(c) removal of the asset from service for an extended period of time;

(d) physical damage;

(e) significant technological developments;

(f) a change in the law, environment, or consumer styles and tastes affecting the period of time over which the asset can be used.

Asset retirement obligations

.35 Obligations associated with the retirement of property, plant and equipment are accounted for in accordance with ASSET RETIREMENT OBLIGATIONS, Section 3110.

(paragraphs 3061.36-.37 deleted)

PRESENTATION AND DISCLOSURE

.38 ♦ *For each major category of property, plant and equipment there should be disclosure of:*

(a) *cost;*

(b) *accumulated amortization, including the amount of any write-downs; and*

(c) *the amortization method used, including the amortization period or rate.* [DEC. 1990]

.39 ♦ *The net carrying amount of an item of property, plant and equipment not being amortized, because it is under construction or development, or has been removed from service for an extended period of time, should be disclosed.* [DEC. 1990]

.40 ♦ *The amount of amortization of an item of property, plant and equipment charged to income for the period should be disclosed* (see INCOME STATEMENT, Section 1520). [DEC. 1990]

.41 The presentation and requirements of IMPAIRMENT OF LONG-LIVED ASSETS, Section 3063, and DISPOSAL OF LONG-LIVED ASSETS AND DISCONTINUED OPERATIONS, Section 3475, apply to property, plant and equipment.

.42 Major categories of property, plant and equipment are determined by reference to type (for example, land, buildings, machinery, leasehold improvements), operating segment and/or nature of operations (for example, manufacturing, processing, distribution, rental real estate).

(paragraph 3061.43 deleted)

PROPERTY, PLANT AND EQUIPMENT RECORDED AT APPRAISED VALUES

.44 ♦ *When an enterprise has an item of property, plant and equipment that was recorded at an appraised value prior to the effective date of this Section, the following additional requirements apply:*

(a) *the basis of the valuation and the date of the appraisal should be disclosed;*

(b) *charges against income should be based on the appraised value; and*

(c) *appraisal increase credits should be shown as a separate item in accumulated other comprehensive income. The appraisal increase should be transferred to retained earnings in amounts equal to the realization of appreciation through sale or the amortization provision. The basis of any transfer to retained earnings should be disclosed.* [OCT. 2006]

TRANSITIONAL PROVISIONS

.45 This Section applies to all fiscal periods beginning on or after December 1, 1990. However, earlier adoption is encouraged. The Section may be applied either prospectively or retroactively.

.46 When this Section is applied prospectively, it is applied to all property, plant and equipment existing on the date of adoption of the Section.

.47 When this Section is applied retroactively, any resulting adjustments are treated as a retroactive application of a change in an accounting policy (see ACCOUNTING CHANGES, Section 1506).

.48 The reference to accumulated other comprehensive income in paragraph 3061.44(c) applies when an entity adopts COMPREHENSIVE INCOME, Section 1530.

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