

STAFF PAPER

July 2014

IASB Meeting

Project	Matters arising from the IFRS Interpretations Committee		
Paper topic	Accounting for a structure that appears to lack the physical characteristics of a building		
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Background on the issue

1. In September 2012, January 2013 and July 2013, the IFRS Interpretations Committee (the Interpretations Committee) discussed a request to clarify whether telecommunication towers should be accounted for as property, plant and equipment (PP&E), in accordance with IAS 16 *Property, Plant and Equipment*, or as an investment property, in accordance with IAS 40 *Investment Property*. The request describes a circumstance in which an entity owns telecommunication towers and leases spaces in the towers to telecommunication operators, to which the operators attach their own devices. The entity provides some basic services to the telecommunication operators such as maintenance services. The submitter asserts that the leasing of spaces in such towers is an emerging business model.
2. In the request, the submitter was specifically seeking a clarification on:
 - (a) whether a telecommunication tower should be viewed as a ‘building’ and thus as ‘property’, as described in paragraph 5 of IAS 40 (ie “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 [...]”.
 - (b) if the telecommunication tower is classified as ‘property’, how the service element in the leasing agreement and business model of the entity should

be taken into consideration when analysing this issue (ie whether ancillary services are so significant as to lead to the conclusion that the property is ‘owner-occupied’)—Paragraph 12 of IAS 40 states that if ancillary services provided are significant to the arrangement as a whole, the property would be considered to be owner-occupied property, which is accounted for under IAS 16.

3. The purpose of this paper is to report back to the IASB the views and concerns expressed on this issue in the September 2012, January 2013 and July 2013 Interpretations Committee meeting and to ask for the IASB’s guidance on how to proceed with this issue.
4. This paper is organised as follows:
 - (a) Background on the issue;
 - (b) Summary of the Interpretations Committee’s concerns;
 - (c) Interaction between the IASB and Interpretations Committee on this issue;
 - (d) Staff recommendation.

Summary of the Interpretations Committee’s concerns

5. In the discussions in September 2012, January 2013 and July 2013, the Interpretations Committee noted that the telecommunication tower in the submission has some of the characteristics of investment property, in that spaces in the tower are let to tenants to earn rentals. However, the Interpretations Committee expressed concern as follows:
 - (a) it is questionable whether the tower qualifies as a ‘building’ because it lacks the features usually associated with a building, such as walls, floors and a roof; and
 - (b) the same question could arise about other structures, such as gas storage tanks and advertising billboards.
6. The Interpretations Committee observed that there is merit in exploring approaches to amending IAS 40 to help the IASB to decide whether the scope of

IAS 40 should be expanded to also include a structure that lacks the physical characteristics associated with a building.

Interaction between the IASB and Interpretations Committee on this issue

Summary of the Interpretations Committee's discussions

7. In the January 2013 Interpretations Committee meeting, the Interpretations Committee noted that under the then-proposed lease accounting model, the guidance for deciding (a) how a lessor accounts for a lease; and (b) how a lessee recognises lease-related expenses in profit or loss depends, to a large extent, on whether the lease is a lease of property. In this regard, the Interpretations Committee was concerned about whether the meaning of the term 'property' should be consistent with its meaning under the then-proposed lease accounting model.
8. Consequently, the Interpretations Committee directed the staff to inform the IASB of the views expressed in the meetings of the Interpretations Committee, and to seek the IASB's views as to what extent the IASB thinks the definition of the term 'property' in IAS 40 should be aligned with its definition in the then-proposed lease accounting model.
9. The issue was brought to the IASB's attention at its January 2013 meeting when it discussed this topic within the context of identifying lease components and classifying leases.
10. In July 2013, the staff provided the Interpretations Committee with updates on the interaction between this issue and the proposed lease accounting model in the Leases Exposure Draft published in May 2013 (the 2013 ED'). The staff noted that the IASB had decided to use the same definition of 'property' in the 2013 ED as that in the existing definition of 'investment property' in IAS 40.
11. In the discussions, the Interpretations Committee expressed general support for broadening the scope of IAS 40 to also include a structure such as a telecommunication tower, and to do so by focusing on the way in which the asset

is used rather than by focusing on the physical characteristics of the structure or on whether it is fixed to land.

12. However, because of the linkage between IAS 40 and the then-proposed lease accounting model, the Interpretations Committee observed that it is difficult for the Interpretations Committee to recommend an approach to amending the definition of ‘investment property’ in IAS 40 only within the context of IAS 40. The Interpretations Committee noted that this issue should be analysed within the context of both IAS 40 and the leases project.
13. Accordingly, the Interpretations Committee decided to report back to the IASB the views and concerns expressed in the July 2013 Interpretations Committee meeting so that the IASB can consider this issue when finalising the leases Standard, and to ask for the IASB’s guidance on whether the Interpretations Committee should do any further work on this topic.

Summary of the IASB’s discussions

14. In the ongoing leases project, the staff referred to the telecommunication tower issue discussed in this paper in the Leases Working Group meeting¹ in January 2012. The discussion at the Leases Working Group meeting was intended to seek input on the issue of whether the current definition of investment property in IAS 40 should be used to determine the accounting for a lease from a lessor’s perspective. On the basis of the discussions in the Leases Working Group meeting, the staff prepared the Agenda Paper² for the February 2012 IASB meeting discussing this issue. This Agenda Paper also contained a reference to the telecommunication tower issue discussed in this paper. However, the Agenda Paper was not discussed by the IASB because the IASB tentatively decided to pursue a different approach that was no longer based solely on the definition of investment property. The new approach was largely based on the nature of the underlying asset (see paragraph 7).

¹ <http://www.ifrs.org/Meetings/Pages/leases-WG-24-Jan-2012.aspx>

² Agenda Paper 2E (<http://www.ifrs.org/Meetings/Pages/IASB-February-2012.aspx>)

15. In the January 2013 IASB meeting, the IASB discussed the telecommunication tower issue within the context of identifying lease components and classifying leases. In particular, the IASB discussed how to determine whether a lease (that includes both property and non-property elements) is a property lease or a lease of assets other than property. The IASB tentatively decided that an entity would make that determination based on the nature of the primary asset within the lease component. The primary asset was described as the predominant asset for which the lessee has contracted for the right to use. In the January 2013 Agenda Paper, the staff acknowledged that the disadvantage of such an approach would be that there may be some leases (eg leases of telecommunications towers) that are priced similarly to more traditional property leases, which would be classified on a basis different from those more traditional property leases. This is because, under this approach, the primary asset in a lease of a telecommunications tower would be the tower itself and, thus, an asset other than property.
16. In May 2013, the IASB published the 2013 ED. In November 2013 the IASB discussed a summary of feedback received on the 2013 ED and started its redeliberations in January 2014.
17. In March 2014, the IASB revisited its lessee and lessor accounting models and tentatively decided the following:
 - (a) not to retain the distinction between leases of property and all other leases as proposed in the 2013 ED, but, instead:
 - (i) to adopt a single approach for lessee accounting; and
 - (ii) to retain lease classification guidance similar to that in IAS 17 for lessors;
18. According to the IASB's most recent tentative decisions reached in March 2014, a lessor would classify and account for telecommunication towers based on whether a lease is effectively a financing/sale, rather than an operating lease (that is, the concept underlying existing IFRS lessor accounting). A lessor would make that determination by assessing whether the lessor transfers substantially all the risks and rewards incidental to ownership of the underlying asset (ie the telecommunication tower).

19. Because of the decisions reached in March 2014 (ie the lease accounting models no longer depend, to a large extent, on whether the lease is a lease of property), the IASB has not discussed whether to amend the definition of ‘property’ within the context of the leases project.

Staff recommendation

20. We observe that the issue has not been resolved in the leases project. In this meeting we would therefore like to ask the IASB how to proceed with this issue. In our view, there are three alternatives:
- (a) The IASB could take the issue onto its agenda.
 - (b) The Interpretations Committee could do further work on this topic on behalf of the IASB.
 - (c) The IASB could wait and consider the issue within the context of the agenda consultation in 2015.
21. We generally agree with the Interpretations Committee’s conclusion that there is merit in exploring approaches to decide whether the scope of IAS 40 should be expanded. This would be to accommodate business models that are similar to those of traditional investment property lessors, but that lack the physical characteristics of a building.
22. We also highlight the history and importance of this issue in particular jurisdictions. Since the issue was discussed in the July 2013 Interpretations Committee meeting, we have received further correspondence on this issue. The correspondence highlights the ongoing concern with this issue and the need for guidance.
23. Nonetheless, broadening the scope of IAS 40 (to also include a structure that lacks the physical characteristics associated with a building, such as leasing of spaces in telecommunication towers) is likely to include other structures such as gas storage tanks and advertising billboards. We are concerned about the broad implications of such an amendment. Because of those implications, the issue could be seen as being broader than could be dealt with by a narrow-scope amendment.

24. Consequently, we think further analysis would be needed to understand any consequences of such an amendment to IAS 40. We think that additional research on the scope of this issue should be undertaken as the next step. We therefore recommend that the IASB should wait and consider this issue within the context of the agenda consultation that is expected to commence in 2015.

Question

1. Does the IASB agree with the staff recommendation set out in paragraph 24 of this paper?