

STAFF PAPER

July 2016

IASB Meeting

IFRS® Interpretations Committee meeting
May 2016

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| Project | Narrow-scope amendment—IAS 40 <i>Investment Property</i> — Transfers of Investment Property | | |
| Paper topic | Comment letter analysis | | |
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Introduction

1. In November 2015 the Board published the Exposure Draft *Transfers of Investment Property* (proposed amendments to IAS 40 *Investment Property*) (the ED). The ED proposed clarifications to the requirements for transfers of property to, or from, investment property. The comment period ended on 18 March 2016.
2. At its May 2016 meeting, the IFRS Interpretations Committee (the Interpretations Committee) was presented with a summary and an analysis of the 57 comment letters received on the ED¹. The Interpretations Committee discussed the comments and staff recommendations. The [IFRIC Update for the Interpretations Committee meeting in May 2016](#) summarises the decisions made at that meeting.
3. For a detailed description of the comments received and the comment letter analysis discussed by the Interpretations Committee, refer to IFRIC [Agenda Paper 5](#) presented at the May 2016 meeting.

¹ These comment letters can be accessed via the following link: <http://www.ifrs.org/Current-Projects/IASB-Projects/Investment-Property-under-construct-inventory-investment-change-in-use/Exposure-Draft-November-2015/Pages/Exposure-Draft-and-Comment-letters.aspx>

Purpose of this paper

4. The purpose of this paper is to:
 - (a) present the Interpretations Committee's recommendations on the amendments to IAS 40;
 - (b) address a few specific concerns raised by Interpretations Committee members; and
 - (c) ask the Board whether it agrees to finalise the amendments.
5. Appendix A sets out the wording of the amendments to IAS 40 recommended in this paper to provide context for the discussion. However, we are not asking the Board to approve that wording or to provide specific comments on the wording, unless those comments relate to the Interpretations Committee's recommendations. The Board will review the drafting during the balloting process.

Summary of comments and recommendations from the Interpretations Committee

6. The ED proposed to clarify the principle for transfers of investment property by amending paragraph 57 of IAS 40 to:
 - (a) state that an entity transfers a property to or from investment property when, and only when, there is evidence of a change in use. A change in use occurs when the property meets, or ceases to meet, the definition of investment property; and
 - (b) re-characterise the list of circumstances set out in paragraph 57(a)–(d) as a non-exhaustive list of examples of evidence of a change in use.
7. The Board proposed that an entity should apply the amendments to IAS 40 retrospectively.
8. Most respondents agree with the proposed amendments to paragraph 57 of IAS 40. They say that the amendments provide a clear explanation of when a change in use occurs as well as the circumstances that trigger a transfer of property to, or from, investment property. However, some request further clarification in some respects.

9. Some respondents disagree with the Board’s proposal to require retrospective application of the amendments, saying that it might not be possible to apply the amendments retrospectively without the use of hindsight. Some others think that retrospective application could be burdensome in some situations.
10. The Interpretations Committee recommends finalising the amendments to IAS 40, subject to some clarifications and revisions to the wording.

Question 1 in the ED—Proposal to clarify the principle for transfers

11. The Interpretations Committee recommends that the Board:
 - (a) clarify that a change in management’s intentions, in isolation, does not provide evidence of a change in use;
 - (b) amend two examples in paragraph 57 of IAS 40 so they could relate to property under construction or development as well as completed property; and
 - (c) in the Basis of Conclusions, emphasise the use of judgement in assessing whether a property meets, or has ceased to meet, the definition of investment property.
12. In the following paragraphs we provide a brief description of the comments received and the recommendations of the Interpretations Committee.

Clarify that a change in management’s intentions, in isolation, does not provide evidence of a change in use

13. Some respondents request that the Board clarify whether management’s ‘intended’ use of a property provides evidence that is sufficient to support a change in use of a property under construction or development.
14. The Interpretations Committee recommends that, as part of the amendments to paragraph 57 of IAS 40, the Board clarify that a change in management’s intentions alone does not provide evidence that is sufficient to support a change in use. To provide evidence of a change in use, such intentions would need to be supported by observable actions.

15. To clarify this point, the Interpretations Committee recommends moving the explanation in paragraph BC3 of the ED to paragraph 57 of IAS 40 before the sentence that begins ‘Examples of ...’—the suggested change is outlined in Appendix A to this paper.

Amend two of the examples in paragraph 57 of IAS 40 to clarify that the requirements also apply to property under construction or development

16. Some respondents comment that the list of examples described in paragraph 57(a)–(d) provides evidence of a change in use only for completed properties. These respondents suggest that the Board expand this list by including additional examples of what constitutes evidence of a change in use for properties under construction or development.
17. The Interpretations Committee observed that the focus of the amendments should be to clarify the principle for transfers to, or from, investment property, and thus it did not propose to add more examples. However, to address the concerns raised, the Interpretations Committee recommends that the Board amend two of the examples in paragraph 57 of IAS 40 so that these examples could relate to property under construction or development, as well as to completed property. The recommendations are:
- (a) amend paragraph 57(a) to include ‘commencement of development with a view to owner-occupation’ as an example of a transfer from investment property to owner-occupied property; and
 - (b) amend paragraph 57(d) to refer to ‘inception’ of an operating lease, instead of ‘commencement’ of an operating lease².
18. One Interpretations Committee member was unsure about whether the additional example proposed in paragraph 57(a) (ie ‘commencement of development with a view to owner-occupation’) provides sufficient evidence of a change in use of a property that is under construction or development. This member questioned whether some might interpret the phrase ‘with a view to’ to be similar to management intent.

² The ‘inception date’ of a lease is defined in IFRS 16 *Leases* as the ‘earlier of the date of a lease agreement and the date of commitment by the parties to the principal terms and conditions of a lease’. IAS 17 *Leases* includes an almost identical definition of the inception of a lease.

19. In response to that concern, we considered changing the proposed example in paragraph 57(a). However, paragraph 57(b) has for some time included the example ‘commencement of development with a view to sale, for a transfer from investment property to inventories’. We did not receive any comments to suggest that that same phrase ‘with a view to’ is misinterpreted in paragraph 57(b). The evidence of a change in use in each of these examples is the ‘commencement of development’, which we think is understandable. We also think it is helpful to draft each of the examples in paragraph 57 in a similar way, and thus recommend retaining the additional example proposed in paragraph 57(a) of IAS 40 (as outlined in Appendix A to this paper).

Emphasise the use of judgement in assessing whether a property meets, or has ceased to meet, the definition of investment property

20. Some respondents request that the Board explain what provides substantive evidence of a change in use to avoid subjectivity in deciding whether a change in use has occurred.
21. The Interpretations Committee was of the view that the Board should not define what provides substantive evidence of a change in use. It observed that, in identifying a change in use applying paragraph 57 of IAS 40, an entity assesses all relevant facts and circumstances (and uses judgement, where relevant), as it does when initially classifying property. Consequently, the Interpretations Committee recommends that, in the Basis for Conclusions, the Board emphasise that judgement may be required to assess whether a property meets, or has ceased to meet, the definition of investment property.

Other issues raised by respondents for which the Interpretations Committee did not consider that further clarification was needed

22. The Interpretations Committee agreed not to recommend amending IAS 40 further to clarify whether:
- (a) the example in paragraph 57(b) (ie ‘commencement of development with a view to sale, for a transfer from investment property to inventories’) is the

only circumstance in which an entity could transfer property from investment property to inventories; and

- (b) the requirements in paragraph 57 of IAS 40 apply to temporary transfers of property.

23. The Interpretations Committee observed that the list of examples in paragraphs 57(a)–(d) is not exhaustive. In the circumstances described above, an entity would apply the principle and requirements in paragraph 57 of IAS 40, and where necessary apply judgement in determining whether there is a change in use of property.

Question 2 in the ED—Transition

24. Some respondents disagree with the Board’s proposal to require retrospective application of the amendments to IAS 40. This is because they say that:
- (a) it might be impossible to apply the amendments retrospectively without the use of hindsight; and
 - (b) retrospective application could become complex and burdensome in some situations—eg in determining the exact point in time in prior periods at which there was evidence of a change in use, or in obtaining fair values at new or revised transfer dates.
25. Those respondents suggest that the Board require either prospective application or retrospective application but with some practical expedients (ie allow a limited form of retrospective application).
26. The Interpretations Committee assessed the possible transition approaches and observed that:
- (a) many entities would already apply the requirements in paragraph 57 of IAS 40 in line with the proposed amendments to that paragraph. Consequently, for those entities, there would be no difference between applying prospective or retrospective application;
 - (b) for some previous transfers, the amounts recognised would be unaffected by the transition approach (for example, transfers to investment property that are measured at fair value); and

- (c) for some previous transfers, applying the amendments retrospectively could be complex because it might involve a change in the classification and measurement of a property some considerable time ago (for example, transfers from investment property to owner-occupied property that occurred several years ago). Some members also observed that it may be impossible to apply the amendments retrospectively without the use of hindsight.
27. To address the concerns raised, the Interpretations Committee recommends that the Board allow entities to choose either:
- (a) a full retrospective approach applying IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; or
 - (b) an approach for which the entity would:
 - (i) reassess the classification of property at the date of initial application of the amendments to IAS 40 to reflect its use at that date; and
 - (ii) apply the amendments to changes in use that occur after the date of initial application of the amendments to IAS 40.
28. The Interpretations Committee also recommends that the Board does not permit first-time adopters a choice of transition approach (ie first-time adopters would be required to apply the amendments to IAS 40 retrospectively). This is consistent with IFRS 1 *First-time Adoption of International Financial Reporting Standards*, which does not include an exception to, or exemption from, the requirements in IAS 40.

Summary of the recommendations of the Interpretations Committee

29. The Interpretations Committee recommends that the Board finalise the amendments to IAS 40, subject to some clarifications and revisions to the wording outlined in Appendix A to this paper. The Interpretations Committee recommends that the Board:
- (a) clarify that a change in management's intentions, in isolation, does not provide evidence of a change in use;

- (b) amend two examples in paragraph 57 of IAS 40 so they could relate to property under construction or development as well as completed property; and
 - (c) in the Basis of Conclusions, emphasise the use of judgement in assessing whether a property meets, or has ceased to meet, the definition of investment property.
30. The Interpretations Committee also recommends that an entity be permitted to apply either of the following transition approaches:
- (a) a full retrospective approach applying IAS 8; or
 - (b) an approach for which the entity:
 - (i) reassesses the classification of property at the date of initial application of the amendments to IAS 40 to reflect its use at that date; and
 - (ii) applies the amendments to changes in use that occur after the date of initial application of the amendments to IAS 40.
31. The Interpretations Committee also recommends that the Board does not permit first-time adopters a choice of transition approach.

Questions for the Board

Questions for the Board

1. Does the Board agree with the Interpretations Committee's recommendation to finalise the amendments to IAS 40?
2. Does the Board agree with the recommended revisions to the proposed amendments to IAS 40 as described in paragraphs 29–30 of this paper?

Appendix A—Draft amendments

This Appendix includes the Interpretations Committee's recommendations regarding the wording of the amendments to IAS 40—this drafting is subject to change. Changes to the proposals in the ED are shown in red and *italics*.

[Draft] Amendment to IAS 40 *Investment Property*

Paragraphs 57–58 ~~is~~ are amended and paragraph 85G is added. Deleted text is struck through and new text is underlined.

Transfers

- 57 **Transfers** An entity shall transfer a property to, or from, investment property shall be made when, and only when, there is ~~evidence of~~ a change in use, evidenced by. A change in use occurs when the property meets or ceases to meet the definition of investment property *and there is evidence of the change in use. A change in management's intentions for the use of a property, in isolation, does not provide evidence of a change in use.* Examples of evidence that *may* support a change in use that would lead to a transfer to, or from, investment property include, among others:
- (a) commencement of owner-occupation, *or of development with a view to 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~~ and
 - (d) ~~commencement~~ *inception* 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~~ *such as on* 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.

...

Effective date

...

85G ~~Draft~~ *Transfers of Investment Property* (Amendments to IAS 40), issued in [date], amended paragraphs 57–58. An entity shall apply these amendments *either*:

- (a) retrospectively to each prior period presented in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; or
- (b) following an approach for which the entity shall:
 - i. reassess the classification of property at the date of initial application of the amendments to reflect its use at that date; and
 - ii. apply the amendments to changes in use of property that occur on or after the date of initial application of the amendments.