INTERNATIONAL VALUATION STANDARDS COMMITTEE

IVSC ALERT

FOR IMMEDIATE RELEASE (26 March 2002)

European Parliament endorses use of International Accounting Standards
The European Parliament has overwhelmingly endorsed the proposal from the European Commission that all EU listed companies (including banks and insurance companies) must follow standards issued by the International Accounting Standards Board in their consolidated financial statements starting no later than 2005. The European Council has already indicated its support for the proposed Regulation in December and the Parliament's decision opens the way to 'fast-track' adoption of the Regulation with just a single reading by the Council in May. European Commissioner, Fritz Bolkestein said: "*This crucial vote gives a strong political signal not only that the European Union is serious about achieving an integrated capital market by 2005, but also that it is ready to lead the development and acceptance of International Accounting Standards. EU publicly-traded companies must start preparing for IAS in earnest. I hope the United States will now work with us towards full convergence of our accounting standards. Recent events, especially the Enron affair, mean there has never been a more appropriate time."*

2005 may sound some way off but the date is misleading. In reality, compliance will require comparative figures for 2004. Companies will also want to get the IAS numbers on the table early so that there is plenty of time to work out what message they convey and how best to communicate the new presentation to stakeholders.

The 300 or so EU companies who moved to adopt US Generally Accepted Accounting Principles in the last couple of years will have until 2007 to comply.

The Regulation will also apply to countries within the European Economic Area. The thirteen EU applicant countries will also have to adopt the Regulation as part of the body of EU legislation. For example, a new Czech accounting law came into effect on 1 January 2002. This enable companies to choose between Czech standards and IAS. Most large companies are expected to adopt IAS to ensure that their financial statements are comparable with the rest of Europe.

EU companies are faced with a huge task. They have to adopt an entire accounting regime for the first time not just existing changes in an existing body of standards. The move to IAS also has many implications for the EU valuation profession (and for the real estate industry). It will affect how assets, liabilities and profits are measured. Companies thinking about the change need to integrate the consequences into daily business life – they may be conducting transactions today which would be accounted for differently under IAS. If a company is planning to lease a large new office building for 20 years, for instance, it may need to re-assess that plan in the light of the new standards.

The IVSC will issue regular Alerts to assist the European real estate industry with the adoption of the International Accounting Standards.

First Time Application of IAS

The International Accounting Standards Board, working in partnership with the French accounting standard setter, is to issue a new standard to help with the complexity of the task of adopting IAS. Existing guidance on first-time IAS application represents the pure academic view that any entity preparing IAS accounts for the first time must go back in time and restate each element as if it had always used the standards. The practical implications of this are significant for long-lived assets such as fixed assets. The IASB has been debating how far it might move away from a strict interpretation, to make mass first-time adoption workable without compromising the integrity of the standards and undermining the goal of providing comparable, relevant accounts between companies and across industries. An exposure draft is imminent that it expected to propose that

on first time application of IAS, the measurement of assets is to be based on restatement of the initial cost. However, if the initial cost of an item of property, plant or equipment cannot be determined without undue cost and effort, the item must be remeasured at its fair value (usually market value). This amount would become the deemed cost for the asset or the liability for subsequent measurement purposes.

The IASB will propose an exception. Using their previous primary basis of accounting, some entities have revalued items of property, plant and equipment, by applying, for example, a general or specific price index to a cost that is broadly comparable to cost determined under IAS, or have revalued the items to an amount that is broadly comparable to fair value determined under IAS. The Board agreed that an entity may treat such revalued amounts as deemed cost under IAS. It will be interesting to see whether the IASB issues any guidance as to what is 'broadly acceptable'?

IAS 40, Investment Property

The adoption of IAS 40, Investment Property will also force many changes. Until recently only the UK and Ireland had national accounting standards on investment property. New Danish Accounting Standard, DKA 16, Investment Property, is effective for annual financial statements from 1 January 2002. In The Netherlands, draft guidelines issued for comment introduce a new benchmark treatment for measurement of investments in real estate: fair value without any depreciation is the preferred method. The alternative treatment remains cost less accumulated depreciation. And in Sweden, a new standard on Investment Property was issued for exposure in July 2001.

International Valuation Standards

IAS are to be introduced to ensure a high level of transparency and comparability of financial reporting from all publicly traded EU companies. To achieve consistency, any allowed or required valuations under IAS logically should be determined in accordance with International Valuation Standards rather than national valuation standards.

“To achieve comparability and transparency, IAS financial statements should comply fully with IAS; should be audited in accordance with International Standards on Auditing (ISA); and any allowed or required valuations should be determined in accordance with International Valuation Standards (IVS). To achieve consistency between IAS, and IVS, the IASB determines the measurement basis and the IVSC determines the valuation standards for achieving that measurement basis.

Asset valuation are an option under IAS 16, *Property, Plant and Equipment*; IAS 40, *Investment Property* (although even if cost model is chosen, the fair value should be disclosed); and IAS 20, *Government Grants*. Asset valuations are required under IAS 22, *Business Combinations*; IAS 19, *Employee Benefits*; and IAS 36, *Impairment of Assets.”*

David Cairns, OBE. *Director*, International Financial Reporting; *Secretary-General, International Accounting Standards Committee* (1985 to 1994) speaking on behalf of IVSC to the Technical Expert Group, European Financial Reporting Advisory Group, January 2002.

European Public Real Estate Association

The European Public Real Estate Association (EPRA) published ‘Best Practices Policy Recommendations’ in October 2001 aimed at making the financial statements of public real estate companies in Europe clearer, more transparent and comparable across Europe to improve the industry’s reception amongst the investment community.

EPRA says, “At present, there is no consistently agreed basis for valuing the assets held by public real estate companies based in Europe”. It recommends that the standard reported valuation of the assets held by public real estate companies should be an open market price assessment of those assets. As EPRA is not a valuation body, it “defers to the work of the International Valuation Standards

Société Foncière Lyonnaise has stated that it sought to follow the EPRA guidelines in its 2001 Results released in early February.

GAAP 2001

GAAP 2001 is the result of a project by the large accountancy firms. It presents an overview of the differences between local written accounting rules and the International Accounting Standards, benchmarked against some 80 accounting measures in force at 31 December 2001 for over 60 countries. Some of the areas where EU/EEA national accounting standards do not accord with IAS 16, *Property, Plant and Equipment*, and IAS 40, *Investment Property* are as follows. The full survey can be accessed at www.ifad.net

Austria, Belgium, Finland, France, Germany, Greece, Italy, Luxembourg, Netherlands, Norway, Portugal, Spain, Sweden have no specific rules requiring disclosures of fair values of investment properties – IAS 40.69
Belgium – Revaluations of fixed assets need not be kept up to date – IAS 16.29
Finland – Absence of specific rules on recognition and measurement of treatment of exchanges of assets – IAS 16.21
France – Revaluation of assets does not have to be kept up to date – IAS 16.29
Greece – Land and buildings revalued periodically (currently every 4 years) based on co-efficients provided by law rather than based on fair values – IAS 16.29

Luxembourg – Investment property revalued every 4 years and depreciated – IAS 40.27
Italy – Fixed assets have been revalued in the past as a result of specific laws but these revaluations are not kept up to date – IAS16.29
The Netherlands – Tangible fixed assets can be held at an out-of-date fair value, and gains and losses on their sale can be calculated by reference to an amount other than carrying value – IAS 16.29/56
Portugal – Most revaluations of property, plant, and equipment (legally based on price indexes) are not generally at fair value and are not kept up to date – IAS 16.29
Spain – Occasional revaluations of fixed assets according to government rules not kept up to date – IAS 16.29
Sweden – Any revaluation of tangible fixed assets does not need to be kept up to date – IAS 16.29

UK – The Convergence Handbook (David Cairns and Christopher Nobes) commissioned by the UK ASB highlighted the following:
Revaluation of property should be at market value under IAS 16.29/30, but UK GAAP used the 'value to the business' model and therefore requires valuation at existing use, replacement cost or open market value, depending on the property.
It is possible that a difference valuation basis may have to be applied to the same asset under UK GAAP and IAS.

FOR FURTHER INFORMATION ON THE IVSC, VISIT THE WEB SITE –www.ivsc.org
OR CONTACT IVSC EXECUTIVE DIRECTOR – mtissier@ivsc.org