



REIS

REAL ESTATE INFORMATION STANDARDS

January 5, 2012

International Accounting Standards Board
30 Cannon Street
London, EC4M 6XH
United Kingdom

(VIA E-MAIL: IFRS.ORG)

Re: Proposed Accounting Standard, *Investment Entities*, issued August, 2011

Dear Board Members:

This letter represents the Real estate Information Standards ("REIS") Board's comments on behalf of the members of the National Council of Real Estate Investment Fiduciaries ("NCREIF") and the Pension Real Estate Association ("PREA") to the International Accounting Standards Board (the "IASB") regarding the exposure draft, *Investment Entities*... In our opinion, it is imperative that the IASB and FASB Boards align their thinking on what constitutes Investment Entities and/or Investment Companies and how they should be reported on a consistent basis globally. We urge the development of principles which result in comparable and consistent net asset value calculated on a fair value basis (FVNAV). Secondly, we propose the development of principles which allow for some flexibility in presentation within the primary financial statements in order to provide information to investors which are most useful to them. Further we request that the issuance and effective dates of the proposed standards be aligned.

We appreciate the opportunity provided by the IASB to comment on the exposure draft. We elected to do so in a format that includes a summarization of our thoughts and concerns, as well as our individual responses to the questions provide in the exposure draft.

The Responding Organization

The REIS initiative is sponsored by NCREIF and PREA to develop, refine and integrate each of the standards within the Foundational Standards¹ and provides guidance concerning their application in the institutional real estate investment industry. NCREIF is an association of institutional real estate professionals which includes investment managers, plan sponsors, academicians, consultants, and other service providers who share a common interest in the industry of private institutional real estate investment. NCREIF serves the institutional real estate community as an unbiased collector and disseminator of real estate performance information, most notably the NCREIF Property Index (NPI). PREA is a nonprofit organization whose members are engaged in the investment of tax-exempt pension and endowment funds into real estate assets. PREA's mission is to serve its members

¹ Within REIS, Foundational Standards include U.S. Generally Accepted Accounting Principles, the Global Investment Performance Standards and the Uniform Standards of Professional Appraisal Practice.

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engaged in institutional real estate investments through the sponsorship of objective forums for education, research initiatives, membership interaction, and information exchange. Collectively the organizations represent the institutional real estate community consisting of over 9,000 investment properties with a fair value of approximately \$350 billion.

The REIS Board's Opinion on the Proposed Investment Entities Standard

We support efforts by the IASB to issue guidance for determining whether an entity meets the criteria to qualify as an investment entity. The REIS Board recognizes and appreciates the overall objective of the Board which includes the improvement of financial statement reporting to end users and the alignment of Investment Entity accounting with the FASB's Investment Companies accounting (Topic 946). The exposure draft effectively adopts many of the same principles currently embedded in FASB Topic 946.

The FASB issued exposure draft, *proposed amendments to Financial Services-Investment Companies (Topic 946)* proposes changes to existing Topic 946 principles. It appears that some of these changes proposed by the FASB were not included in the IAS *Investment Entities* exposure draft. Rather, the IAS *Investment Entities* appears to align closely with existing Topic 946 principles. For example, under the proposed guidance entities that meet the criteria of an investment entity, as defined in the exposure draft, would no longer consolidate controlled entities and instead measure them at fair value through profit and loss. In addition, the exposure draft also proposes to amend the relevant paragraphs of IAS 28, *Investment in Associates and Joint Ventures* to also require an investment entity to measure its investments in associates and joint ventures at fair value through profit and loss. These principles are very similar to the existing FASB's Topic 946 which states that consolidation or the use of the equity method of accounting for entities that qualify as Investment Companies is not appropriate. We believe that under this new guidance many of the real estate funds now following the guidance under International Accounting Standards (IAS 40), *Investment Property*, would meet the criteria as outlined in the exposure draft for an investment entity and change their external reporting presentation. As our industry includes investors and managers who invest globally, we urge the IASB and the FASB develop a consensus treatment. In order to meet the institutional investor's needs and requirements, our industry has applied a fair value reporting model for investment properties similar to IAS 40 for over 30 years. We are in support of a global converged effort to promote conformity in guidance.

Our responses to the specific questions that are included in the proposed exposure draft are presented below.

Question 1

Do you agree that there is a class of entities, commonly thought of as an investment entity in nature that should not consolidate controlled entities and instead measure them at fair value through profit and loss?

Response:

Yes. We agree that there is a class of entities, commonly thought of as an investment entity in nature that should not consolidate controlled entities and instead measure them at fair value through profit and loss. When considering the criteria for determining when an entity is an investment entity, paragraphs 2 and B1-B17 of the exposure draft, we think that many real estate funds have been organized for that explicit purpose and would meet the criteria as expressed in the exposure draft. Many US real estate funds already follow the accounting guidance provided by ASC Topic 946 because they meet the definition of an investment company and as such apply that accounting which is similar to what is being proposed by the exposure draft.

Question 2

Do you agree that the criteria in this exposure draft are appropriate to identify entities that should be required to measure their investments in controlled entities at fair value through profit and loss? If not, what alternative criteria would you propose and why are those criteria more appropriate?

Response:

Yes. We agree that the criteria in the exposure draft, paragraphs 29a and B1-B6, are appropriate to identify entities that should be required to measure their investments in controlled entities at fair value through profit and loss.

Question 3

Should an entity still be eligible to qualify as an investment entity if it provides (or holds an investment in an entity that provides) service that relate to:

(a) Its own investment activities?

Response:

Yes. We agree that an entity should still be able to qualify as an investment entity if it provides (or holds an investment in an entity that provides) services that relate to its own investment activities. By allowing an entity to perform activities that support its investing activities, it would allow a real estate fund or REIT to qualify as an investment company if the fund (directly or indirectly through an agent) advises or manages only properties that it owns. This seems appropriate as investors typically view these types of funds as another investment vehicle in the same fashion as their typical investment entities such as a mutual funds, fund of funds, or securities fund. The underlying principle of investing in multiple investments for capital appreciation, investment income, or both continue to hold true in this situation. This is also consistent with the guidance within the FASB's recently released exposure draft on the proposed changes to *Financial Services – Investment Companies* (Topic 946). We think the guidance in these two documents should be consistent.

(b) The investment activities of entities other than the reporting entity?

Response:

No. We do not agree that an entity should still be able to qualify as an investment entity if it provides (or holds an investment in an entity that provides) services that relate to investment activities of entities other than the reporting entity. An entity that does so does not meet the requirement of investing in multiple investments for capital appreciation, investment income, or both. When the services are for an entity's own investment activities the principle of this requirement is still met. However once an entity is providing such a service for other entities, and most likely generating a fee, the underlying principle of the requirement is no longer met.

Question 4

- (a) Should an entity with a single investor unrelated to the fund manager be eligible to qualify as an investment entity?**

Response:

Yes

- (b) If yes, please describe any structures/examples that in your view should meet this criterion and how you would propose to address the concerns raised by the Board in paragraph BC16.**

Response:

A subsidiary entity whose parent entity accounts for its investments at fair value should be permitted to report the information in the stand alone financial statements at fair value. An example of this in US GAAP is a pension plan that represents multiple unrelated investors and is required under the Employee Retirement Income Security Act of 1974 (ERISA) or other similar legislation to report on a fair value basis. We believe that the IASB should adopt a similar position in this exposure draft

Question 5

Do you agree that investment entities that hold investment properties should be required to apply the fair value model in IAS 40 and do you agree that the measurement guidance otherwise proposed in the exposure draft need apply only to financial assets, as defined in IFRS 9 and IAS 39 Financial Instruments: Recognition and Measurement?

Response:

We believe that entities that hold investment properties should be required to apply the fair value model in IAS 40. There should be no optionality. We further feel that an entity that qualifies as an investment entity under this guidance should measure all assets and liabilities at fair value with the measurement recognized through profit and loss. We believe that this is a more consistent presentation and necessary for investors to understand the net asset value of the entity especially when compared with other potential investments of a similar class.

Question 6

Do you agree that the parent of an investment entity that is not itself an investment entity should be required to consolidate all of its controlled entities including those it holds through subsidiaries that are investment entities?

Response:

No, we do not agree that the parent of an investment entity that is not itself an investment entity should be required to consolidate all of its controlled entities including those it holds through subsidiaries that are investment entities.

First, we believe that the Board is misinformed; in most cases, investment entities do not have noninvestment entity parents. In fact, there are numerous examples in practice where an investment entity has a corporate parent that is a noninvestment entity. Secondly, the investment entity generally keeps its books on a fair value basis and if the parent were required to consolidate the investment entity including its underlying controlled entities, the investment entity would need to develop the information needed to adjust its books to comply with the parent's historical cost basis of accounting which would be cost prohibitive. Thirdly, we note that US GAAP has not historically required the parent of an investment company/entity to consolidate the investment company/entity and this accounting treatment has served the capital markets well because the markets are only interested in the fair value of an investment entity's net investments, not in seeing the consolidated results of any particular investment. Lastly, in our experience, it is rare that a non-investment entity parent issues its equity instruments to an investee of its investment entity subsidiary. If this were to occur it is likely that the investment entity subsidiary would no longer qualify for the measurement exemption.

Question 7

(a) Do you agree it is appropriate to use this disclosure objective for investment entities rather than including additional specific disclosure requirements?

Response:

We agree with the disclosure requirements regarding a change in the entities' status as described in paragraph 10(a) of the Exposure Draft.

We generally agree with the disclosure requirements regarding a change in the entities' status as described in paragraph 10(b) (i), 10(b) (ii), and 10(c) of the Exposure Draft. However, we would ask that the Board clarify whether or not funding to and from investment entity to its controlled investment (e.g., real estate funds), in the ordinary course of business, would require this type of disclosure. It is typical for some investments to periodically distribute cash to investors as well as require a periodic contribution. Providing detail analyses of the cash movement may only serve to confuse users of the financial statements as this is not representative of what is available for distribution to them.

We agree with the disclosure requirements regarding a change in the entities' status as described in paragraph 10(d) of the Exposure Draft

(b) Do you agree with the proposed application guidance on information that could satisfy the disclosure objectives?

Response:

In general, we agree with the proposed application guidance regarding controlled investments in paragraph B18 of the Exposure Draft, but we suggest the Board consider revising the language in B18(c) from “voting rights” to “interests held”.

In general, we agree with the proposed application guidance regarding controlled investments in paragraph B19 of the Exposure Draft, but we suggest the Board consider revising B19 (a) (viii) to also reference certain industry standards with respect to calculations of this number (e.g., INREV NAV) especially where the Board seeks consistency across investment classes.

We agree with the proposed application guidance regarding duplicate disclosures in paragraph B20 of the Exposure Draft.

Question 8

Do you agree with applying the proposals prospectively and the related proposed transition requirements?

Response:

We agree with prospective application only. Any other application methodology would distort otherwise comparable investment products and make the financial statements uninformative and potentially misleading to users. We would also suggest that the Board consider an application effective date that coincides with the FASB’s effective dates for ASC Topic 946 and the proposed ASC Topic 973.

Question 9

(a) Do you agree that IAS 28 should be amended so that the mandatory measurement exemptions would apply only to investment entities as defined in the exposure draft?

Response:

We do not agree that this exemption should apply only to investment entities. It would appear that entities that went through an evaluation to determine if fair value accounting or equity method accounting provided information that was more useful in the decision making process. The focus should be on what provides transparent information about the performance of the underlying investment to the users of the financial statements. A move away from fair value accounting to equity method accounting would not consistently provide such transparency or useful information to investors.


(b) As an alternative, would you agree with an amendment to IAS 28 that would make the measurement exception mandatory for investment entities as defined in the exposure draft and voluntary for other venture capital organizations, mutual funds, unit trusts and similar entities, including investment-linked insurance funds?

Response:

Yes, we agree that the proposal should be mandatory for investment entities as defined, and voluntary for other venture capital organizations, mutual funds, unit trusts and similar entities, including investment-linked insurance funds. It would be challenging to make one decision fit all types of organizations. Since such entities focus on the fair value of their portfolio and report their performance based on fair value accounting, moving to an equity method of accounting would not seem in line with the expectations of their investors. We would envision such organizations having to maintain such fair value information and provide it to investors through disclosure, which defeats the purpose of meeting the expectations of investors to have transparent information about the performance of all aspects of the organization in which they have invested.

We would be pleased to discuss our comments above or the answers to the specific questions with you at your convenience. Should you wish to discuss the contents of this letter with us, please feel free to contact us at the above address or at 978-887-3750.

Very truly yours,

A handwritten signature in blue ink that reads "John J. Baczewski". The signature is written in a cursive, flowing style.

John Baczewski
REIS Board Chair