



2002 SEP -4 AM 10: 5

31 August 2002

Deputy Director, Accounting
Hong Kong Society of Accountants
4th Floor Tower Two, Lippo Centre
89 Queensway
Hong Kong

Dear Sirs,

**Comment on Exposure Draft: Proposed Improvements to
International Accounting Standards**

We refer to your notice of 5 June 2002 inviting comments on the Proposed Improvements to International Accounting Standard (IAS).

The Valuation Standard and Practice Committee of Hong Kong Institute of Surveyors has studied the Paper and has the following comments on the relevant part of the Proposed Improvements to IAS:

1. IAS 40 – Investment Property

“Question 1 Do you agree that the definition of investment property should be changed to permit the inclusion of a property interest held under an operating lease providing that:

- (a) the rest of the definition of investment property is met; and*
- (b) the lessee uses the fair value model set out in IAS40, paragraphs 27 – 49?”*



We agree with the proposed amendments as both Hong Kong and the People's Republic of China operate leasehold land systems. We believe the proposed changes to the definition of investment property could better reflect the asset position of the companies.

“Question 2: Do you agree that a lessee that classifies a property interest held under an operating lease as investment property should account for the lease as if it were a finance lease?”

We agree. In addition, we would suggest that where property interest held under an operating lease has been classified as investment property as if it were a finance lease, the property should be marked to fair value to truly reflect the value of the asset at the date of valuation.

“Question 3: Do you agree that the Board should not eliminate the choice between the cost model and the fair value model in the Improvements project, but should keep the matter under review with a view to reconsidering the option to use the cost model in due course?”

The two models are based on two very different rationales and may generate very different figures. We consider that the use of the two models will create confusion and difficulties to less sophisticated users of financial statements.

Industrial comparison would be made more difficult. Time would be needed even for professional financial analyst to adjust the financial statements for comparison, which is undesirable in terms of conveying market information efficiently.

We agree that it takes time for companies and financial statements users to adapt to using fair value model but we believe that the sooner to use the fair value model, the earlier the market value of the assets held by the company could truly be reflected in the accounts.



In addition, we would propose that the fair value should be assessed annually by an external valuer to ensure the independence and fairness of the value of the assets.

IAS 17 - Leases

“Question 1 : Do you agree that when classifying a lease of land and buildings, the lease should be split into two elements – a lease of land and a lease of buildings? The land element is generally classified as an operating lease under paragraph 11 of IAS 17, Leases, and the buildings element is classified as an operating or finance lease by applying the conditions in paragraphs 3-10 of IAS 17.”

Under the current asset ownership system, land and building are physically inseparable. Split between land and buildings can only be done on a hypothetical situation. However, we would draw your attention to the situation in Hong Kong for your Society to consider whether the hypothetical split is needed. In Hong Kong, it is now not uncommon to find that the value of industrial premises is less than the value of the land. Under such circumstance, if we have to split the value of land and building from the value of the premises, the situation will be that there will be a negative value of building element.

“Question 2: Do you agree that when a lessor incurs initial direct costs in negotiating a lease, those costs should be capitalized and allocated over the lease term? Do you agree that only incremental costs that are directly attributable to the lease transaction should be capitalized in this way and that they should include those internal costs that are incremental and directly attributable?”

We are not sure whether under the fair value model, these direct or incremental costs are still relevant. We consider that maintaining these costs as expenses is not inappropriate.



We would be happy to further elaborate our comments and suggestions should this be considered at all of assistance. Should you need any further information please feel free to contact our Mr. K.K.Chiu at 2507 0602.

Yours faithfully,

K.K.Chiu
Convenor of Valuation Standards and Practice Committee
Hong Kong Institute of Surveyors