NATIONAL ASSOCIATION OF
REAL ESTATE INVESTMENT TRUSTS®

December 22, 2003

Mr. Lawrence W. Smith
Director-Technical Applications and Implementation Activities and EITF Chair
Financial Accounting Standards Board
407 Merritt 7
Norwalk, Connecticut 06856-5116

Re: AICPA's Proposed SOP, *Accounting for Certain Costs and Activities Related to Property, Plant and Equipment*

Dear Larry:

Once again we want to thank you and the FASB for meeting with NAREIT representatives on November 25, 2003 regarding the Association's concerns with respect to the AICPA's proposed SOP, *Accounting for Certain Costs and Activities Related to Property, Plant and Equipment.* The dialogue was very useful in terms of our understanding the Board's perspective on the proposed SOP as well as the pace of global harmonization of accounting standards. We hope the dialogue provided the Board and staff with a clearer understanding of NAREIT's concerns.

A number of questions were asked regarding NAREIT's position that the proposed SOP moves accounting for investment property in the U.S. further from IAS No. 40, *Investment Property.* This letter is intended to clarify our position.

First, it is important to understand the industry's current practice in accounting for property, plant and equipment. Most companies categorize investment property into less than six accounts. These might include land, land improvements, structure, mechanical and electrical equipment and furniture, fixtures and equipment. Each of these categories of a property's cost is depreciated on a straight-line basis over the weighted average lives of assets in each category. Cost records are generally not maintained for asset components within each category. When a component is replaced, the cost of the new component is added to the appropriate category of costs. The cost of the replaced component is not written-off at that time. This composite method of depreciation assumes that, on average, components are replaced at the end of their useful lives.

Second, the fair value model of accounting for investment property included in IAS 40 treats investment property as an integrated entity and does not require componentization of the property.

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Our position is that requiring the real estate industry to componentize hundreds of billions, even trillions, of dollars of property at this time when there is a high probability of moving to the international integrated-entity fair value model in the foreseeable future, would be a tremendous waste of resources and confusing to investors and other users of our industry's financial statements.

While we understand that the fair value model is but one of two choices for accounting for investment property under IAS 40, we do believe that the alternative approach, historical cost/depreciation, is largely illusory. This is because when the alternative approach is used under IAS 40, the fair value still must be measured and disclosed in a note; while, under the fair value model, fair value is reported in the balance sheet. For practical purposes, both approaches require the measurement of fair value and the inclusion of those values in the financial statements/notes.

Consequently, we would expect that most companies that expend the considerable effort to measure the fair value of investment property would choose to report these values in the financial statements under the fair value model rather than in a note under the historical cost/depreciation model. Therefore, if the Board continues to move U.S. financial standards toward international standards, we believe that eventually most investment property will be reported at fair value under global accounting standards. Given the course that the Board and IASB appear to be on, we urge the Board to exempt investment property from the componentization requirements of the proposed SOP until the accounting for investment property under U.S. GAAP and international standards is conformed.

Finally, we intend to follow-up our discussion of the industry's proposed method of more realistically measuring the depreciation of investment property under current GAAP. As we indicated, this method incorporates a realistic salvage value in the measurement of depreciation of the initial cost of investment property. We expect to deliver this proposal to FASB staff during the first quarter of 2004.

If you have any further questions regarding our position, please contact me at 202-739-9432 or gyungmann@nareit.com.

Sincerely,

George L. Yungmann
Vice President, Financial Standards

CC: Robert H. Herz, Chairman, Financial Accounting Standards Board
Steven A. Wechsler, President and CEO, NAREIT
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