NAREIT Financial Standards Update

National Association of Real Estate Investment Trusts®
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Financial Standards Update

Highlights

- NAREIT Comments on FASB and IASB Proposed Discontinued Operations Definition - P.1
- NAREIT Surveys Members on SEC's Proposal Toward Adopting IFRS - P.3
- FASB Reaches Preliminary Decisions on FIN 46(R) Project - P.5

NAREIT Comments on FASB and IASB Proposed Discontinued Operations Definition

In 2008, the Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB) issued a proposal to amend standards that set forth the reporting for discontinued operations. The FASB and IASB's converged definition proposes that a discontinued operation is a component of an entity that is: 1) an *operating segment* (as defined in FASB Statement No. 131, *Disclosures about Segments of an Enterprise and Related Information*) and either has been disposed of or is classified as held for sale; or, 2) a *business* (as defined in FASB Statement No. 141(R), *Business Combinations*) that meets the criteria to be classified as held for sale *on acquisition*. The proposed amendments would be effective for fiscal years beginning after Dec. 15, 2009 and interim periods within those fiscal years, with early application permitted. The modified reporting would be applied retrospectively. To learn more about the proposed amendments, click HERE.

On Jan. 23, 2009, NAREIT and its global partners of the Real Estate Equity Securitization Alliance (REESA) responded to the FASB and IASB's proposed amendments on reporting discontinued operations in two separate letters – comments to the FASB (click HERE) and comments to the IASB (click HERE). In the letters, REESA strongly recommended that "a strategic shift in the entity's operations" should be the underlying factor in considering when a disposition is to be reported as a discontinued operation. REESA further explained that the converged definition of a discontinued operation should refer to a portion of a company's operations that represents either 1) a reportable segment; or, 2) a *significant* operating segment. A *significant* operating segment would be an operating segment that a) management believes represents a significant shift in operations if disposed of; or, b) constitutes revenues or assets greater than minimum thresholds as a percentage of the entity's consolidated revenues or assets.

SEC Mandates the Adoption of XBRL

On Jan. 30, 2009, the Securities and Exchange Commission (SEC) released *Interactive Data to Improve Financial Reporting*, the final rule that requires public companies preparing their financial statements under U.S. Generally Accepted Accounting Principles (GAAP) to provide a new exhibit of their financial statements and applicable financial statement schedules to the SEC in interactive data format using eXtensible Business Reporting Language (XBRL). Click HERE to access the final rule.

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Under the new rule, filers are required to tag (a function of XBRL) the complete financial statements and any required financial statement schedules for all periods presented. Footnotes must be tagged using four different levels of detail, which include (1) each complete footnote tagged as a single block of text; (2) each policy within the significant accounting policies footnote tagged as a single block of text; (3) each table within each footnote tagged as a separate block of text; and (4) each amount (i.e., monetary value, percentage and number) separately tagged within each footnote.

In a company's first year of XBRL reporting, only level one will be required. Beginning one year from the company's initial required XBRL submission, all four levels will be required with a one-time 30-day grace period. Subsequent XBRL reports with all four tagging levels will be required to be filed simultaneously with the related report or registration statement. XBRL financial statements must also be provided on a company's website for at least 12 months.

Large accelerated filers with a worldwide public common equity float above $5 billion, as of the end of the second fiscal quarter of their most recently completed fiscal year, will begin XBRL financial reporting with the first quarterly report on Form 10-Q containing financial statements for a fiscal period ending on or after June 15, 2009. This implementation date is consistent with NAREIT's recommendation to the SEC in its Aug. 1, 2008 letter to begin XBRL implementation during an interim period. The SEC originally proposed XBRL financial reports for fiscal periods ending on or after Dec. 15, 2008. Click HERE to access NAREIT's letter to the SEC on its proposed rule, *Interactive Data to Improve Financial Reporting*.

All other large accelerated filers will be subject to the same interactive data reporting requirements for a fiscal period ending on or after June 15, 2010. And finally, all remaining filers will be subject to the same interactive data reporting requirements for a fiscal period ending on or after June 15, 2011. All first-time filers of XBRL information are allowed a one-time 30-day grace period.

The new XBRL exhibit will be required for the filer's financial statements contained in periodic reports on Forms 10-Q and 10-K and Forms 8-K and 6-K that contain revised or updated financial statements. The rule does not require that filers provide interactive data for their MD&A, executive compensation or other financial, statistical or narrative disclosure. Registration statements filed under the Securities Act, such as Forms S-1, S-3, S-4 and S-11, will also include interactive data when financial statements are included directly in the registration statement, rather than being incorporated by reference. Interactive data must be submitted with a first filing of a Securities Act registration statement and then only after a price or price range has been determined and any later time when the financial statements are changed, rather than requiring interactive data submissions with each filing. Interactive data is not required for the financial statements contained in registration statements under the Exchange Act on Form 10.

NAREIT and several of its members actively participated in the comment process for the XBRL U.S. GAAP real estate taxonomy that resulted in a statement of income exclusive to REITs. XBRL US will continue to release the taxonomy for public review in the future; therefore, industry participants will continue to have the opportunity to enhance the taxonomy for the real estate industry. Click HERE to learn more about XBRL US.

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NAREIT Surveys Members on SEC's Proposal Toward Adopting IFRS

In 2008, the SEC released its proposed roadmap that would require all U.S. issuers to prepare their financial statements under International Financial Reporting Standards (IFRS) as issued by the IASB beginning in 2014. The proposal outlines certain milestones that must be reached before the adoption of IFRS in the U.S., as well as a timeline toward the adoption. To access the SEC's proposal, click HERE.

The SEC extended the comment deadline on its proposed rules for IFRS adoption to Apr. 20, 2009 to allow companies more time to further analyze the impacts of the proposal. In preparation of NAREIT's comment letter on this SEC proposal, NAREIT developed a survey to gather members' views on the proposal. Since the SEC has extended the comment period on the proposal, the survey will continue to be available until Apr. 3, 2009. The survey includes eight questions that will help NAREIT gain its members' views on the adoption of IFRS. To complete the survey, click HERE. If you would like to provide additional feedback on the proposal outside of the survey, please contact Sally Glenn at sglenn@nareit.com.

NAREIT Develops Response to FASB and IASB on Financial Statement Presentation

NAREIT and its REESA global partners are in the process of preparing a comment letter in response to the Preliminary Views Document (PVD) on the *Financial Statement Presentation* Project issued by the FASB and IASB. The objectives of this project are to portray a cohesive financial picture of an entity's activities, disaggregate information so that it is useful in predicting an entity's future cash flows and help users assess an entity's liquidity and financial flexibility. For more information on the PVD, click HERE.

As previously reported, REESA developed a real estate financial statement model to use as a basis for commenting on the PVD. On Mar. 10, 2009, NAREIT's Best Financial Practices Council met to discuss members' views on the PVD and on the global financial statement model, as well as views on an illustrative set of financial statements prepared under the PVD by Taubman Centers. The council concluded that the Boards consider a cost-benefit analysis to determine the usefulness of a proposed schedule that reconciles cash flows to comprehensive income on a line by line basis. Participants also suggested that the timing of the implementation for the new financial statement format should be extended to allow for the many implications of the proposal to a company's financial management.

In preparation of its comment letter to the FASB and IASB, NAREIT staff also sought input from members of NAREIT's Real Estate Investment Advisory Council to obtain the perspective of investors and analysts on certain major issues raised in the PVD.

NAREIT staff shared the Council's and industry users' views with REESA members at a meeting held in London on Mar. 12-13. The REESA group agreed that the proposals in the PVD would generally enhance the usefulness of financial statements but that certain modifications to the proposal are required in order for the revised financial statement model to respond effectively to the needs of our industry's preparers and users. These modifications generally are required to a) enable the industry to report Net Operating Income and Funds From Operations on the face of the income statement and b) to eliminate a great deal of very detailed information.

Comments on the PVDs are due by Apr. 14, 2009. If you have comments concerning this PVD, please contact George Yungmann at gyungmann@nareit.com.

FASB and IASB Include Lessor Accounting Discussion in Lease Accounting Proposal

In 2008, the FASB and IASB agreed to defer the development of specific standards for lessor accounting and focus on a new lessee accounting model under the FASB and IASB joint *Lease Accounting* Project. The most significant preliminary conclusion of the Boards is that lease accounting should be based on a "right of use" model as opposed to the lessee recording a property asset. This model would require the lessee to recognize the asset representing its right to use the leased asset and a corresponding liability for its obligation to pay rent. Additionally, under this model, accounting for operating leases would no longer exist and lessees would account for all leases similar to the current accounting treatment of capital leases.

On Jan. 22, 2009, the Boards decided to include a high-level discussion of lessor accounting issues, rather than preliminary views on specific standards, in their Preliminary Views Document (PVD), which was issued Mar. 19, 2009. To access the PVD click HERE. You are invited to join a task force that will evaluate the PVD and develop NAREIT's comments on this PVD. If you are interested in participating in the task force, please contact Ali Clark at aclark@nareit.com.

FASB and IASB Release Preliminary Views on Revenue Recognition

On Dec. 19, 2008, the FASB and IASB issued a Preliminary Views Document (PVD) on *Revenue Recognition in Contracts with Customers*. The objective of the joint project is to clarify the principles for recognizing revenue and to create a converged revenue recognition standard for U.S. GAAP and IFRS that companies can apply consistently across all industries and transactions. The overarching principle proposed in the PVD is to recognize revenue when the seller satisfies a "performance obligation" by transferring goods or services to a customer as contractually agreed. For our industry, NAREIT believes the goods or services would be represented by "rights to use space." When a company enters into a contract with a customer, the company obtains rights to payments from the customer and assumes obligations to provide goods or services to the customer. These obligations are referred to as "performance obligations" in the PVD. The combination of those rights and obligations produces a net contract position that can be an asset, a liability or net zero position for the company. Revenue arises from positive increases in that net contract position over the life of the contract. Therefore, satisfying a performance obligation increases a company's net contract position.

In the PVD, the Boards propose that revenue under the contract would be the amount of payment or consideration received from the customer in exchange for transferring goods and services to the customer. The amount of revenue recognized would be based on an allocation of the customer's consideration. If a bundle of goods and services are transferred to a customer all at the same time, a company would recognize revenue in the contracted amount at the time of the transfer. On the other hand, if the company transfers goods and services at different times, it needs to determine how much of the total consideration to allocate to each performance obligation. The PVD proposes that consideration would be allocated to each performance obligation in proportion to the company's stand-alone selling price for the promised good or service.

The accounting for a landlord's right to receive payments for the use of space may be resolved in the FASB and IASB *Lease Accounting* Project discussed above. However, lessor accounting will probably be influenced by the conclusions reached in this project.

To access the PVD, click HERE. The PVD is open for public comment until June 19, 2009. The Boards expect to release the related Exposure Draft before the end of 2010. If you are interested in joining a task force to assist in developing NAREIT's comment letter, please contact Sally Glenn at sglenn@nareit.com. NAREIT will submit a letter, along with its REESA partners, similar to the process noted above for the Financial Statement Presentation PVD.

FASB Reaches Preliminary Decisions on FIN 46(R) Project

During 2008, the FASB issued a proposal, *Amendments to FASB Interpretation No. 46(R)*, that would modify the accounting and reporting for a variable interest entity (VIE) and eliminate the exceptions that consider the consolidation of special purpose entities. The exposure draft is available by clicking HERE.

In its Nov. 14, 2008 letter, NAREIT conveyed several negative impacts that the proposed statement would have on the accounting for jointly owned entities. These impacts include:

- inconsistent consolidation or deconsolidation conclusions for similar entities due to conflicting treatment of substantive kick-out rights and differing interpretations of the term "power to direct" in the determination of a primary beneficiary;

- the impracticality, as well as increased effort and costs, in performing ongoing assessments of VIEs and primary beneficiaries; and,

- the unintended consequence of deconsolidating real estate joint ownership arrangements.

Click HERE to access NAREIT's comment letter.

On Jan. 28, 2009, the Board reconsidered several issues related to its proposed statement, *Amendments to FASB Interpretation No. 46(R)*. Based on the comments received, the Board agreed to:

- retain the current FIN 46(R) requirement for VIE reassessments that are based on the occurrence of certain triggering events and add criterion for reassessing an entity's status upon an event that causes the holders of the entity to lose the direct or indirect ability through voting rights to make decisions that have a significant effect on the entity;

- provide explicit guidance on accounting for the derecognition of VIEs and require a deconsolidation event to be accounted for similar to a loss of control of a subsidiary in FAS 160, *Noncontrolling Interests in Consolidated Financial Statements*;

- remove the significance exception in the determination of a VIE and in the proposed disclosures in the FIN 46(R) ED; and,

- eliminate the quantitative analysis, which explicitly factors in expected losses and expected residual returns, in the determination of the primary beneficiary.

The Board will further discuss several additional issues, such as the impact of substantive kick-out rights and the "power to direct" in the determination of a VIE's primary beneficiary. The Board also concluded that it would not reassess the following issues as part of this project: a) the reconsideration of primary beneficiary status, b) one consolidation model for both voting entities and VIEs and c) a converged standard with the IASB. It is important to note that Board decisions are final after they have been subject to FASB's due process.

SEC Provides Feedback on Elective Stock Dividends

In December 2008, the IRS issued a revenue procedure that allows a listed REIT to offer a mixture of stock and cash (with at least 10 percent of the total distribution being cash) to satisfy its distribution requirement. The elective stock/cash dividend arrangement has raised a financial reporting issue relating to the impact of the new shares issued on reported per share amounts. Two possible accounting treatments have been put forth. One treatment would restate per share amounts of prior periods presented to reflect the shares issued under the dividend arrangement. An alternative treatment would account for the stock portion of the dividend as if it was a stock issuance rather than a stock dividend. Under this accounting, the new shares issued would only affect per share amounts reported prospectively. The SEC concluded that the FASB/EITF should examine this issue. To access the NAREIT Financial Standards Alert issued on this topic, click HERE.

In connection with this revenue procedure, a REIT with an operating partnership (OP) (or UPREIT structure) may accordingly provide an option to its unitholders to elect to receive a distribution in a combination of cash, additional OP units or REIT stock. The SEC advised NAREIT of the registration implications of such OP distributions and concluded that any REIT stock that is offered by the OP to unitholders must either be registered or another exemption must be available under SEC rules. In addition, the SEC conveyed that it viewed the transaction as a primary offering by the REIT of its shares through the OP. Thus, the SEC staff advised that another alternative is for the REIT to use its shelf registration statement to register the stock that an OP offers to its unitholders. The SEC staff said that the SEC views the OP as acting as an underwriter in this instance. For more details, click HERE.

Additionally, to learn more about the tax implications of the elective stock dividends, click HERE for a Q&A series offered by NAREIT.

2009 NAREIT Financial Standards Events

REITWise 2009: NAREIT's Law, Accounting and Finance Conference

REITWise 2009: NAREIT's Law, Accounting and Finance Conference will be held at La Quinta Resort & Club in La Quinta, CA on Mar. 25-27, 2009. The Conference provides business and technical educational sessions regarding legal, accounting, finance and tax topics for REITs and real estate companies. The Conference also offers members opportunities to network with colleagues and exchange information about the latest trends and changes occurring in our industry. To register, click HERE.

Internal Audit Forum

The 2009 Internal Audit Forum will be held on Aug. 18 and 19 in San Francisco, CA. The event will be hosted by BRE Properties, Inc. The Internal Audit Forum is designed exclusively for internal audit directors or other senior level financial professionals responsible for a company's internal audit function. This annual event has proven to be successful in providing useful information in improving the internal audit function. Program and registration information will be available in the coming weeks. For more information on this event, please contact Sally Glenn at sglenn@nareit.com or (202) 739-9442.

Retail Sector Operations Accounting Forum

Arrangements for the 2009 Retail Sector Operations Accounting Forum are underway. The program will offer best practice guidelines for controlling and accounting for operations of retail space. Prior year programs have been very successful in providing useful industry-specific information to our members. Each year one or two of NAREIT's retail sector companies host(s) this event. If you are interested in hosting this event in 2009, please contact Sally Glenn at sglenn@nareit.com or (202) 739-9442.

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