AMERICAN INTERNATIONAL GROUP, INC.



February 28, 2012

Technical Director Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, CT 06856-5116

Re: File Reference No. 2011-210 – Exposure Draft, Real Estate – Investment Property Entities (Topic 973)

AIG appreciates the opportunity to comment on the Exposure Draft, *Real Estate – Investment Property Entities* ("Exposure Draft"). We support the Financial Accounting Standard Board's ("FASB" or the "Board") initiative to align the scope of entities that would apply the proposed lessor accounting model under U.S. generally accepted accounting principles ("GAAP") to that of International Financial Reporting Standards ("IFRS") and to address the diversity in practice regarding the accounting by real estate investment entities. However, we have certain key concerns with the Exposure Draft as summarized below and discussed in detail in our responses to the FASB's specific questions in the Appendix.

Affordable Housing Partnerships

We are concerned that entities whose primary business objective is to invest in real estate for reasons other than generating returns primarily from capital appreciation, such as providing affordable housing and generating tax credits for investors, may fall within the scope of the proposed investment property entity guidance because the total return of such entities could include a relatively small amount of capital appreciation. There appears to be diversity in the industry's interpretation of the Exposure Draft as it pertains to affordable housing partnerships and whether these partnerships would meet the definition of an investment property entity.

Affordable housing partnerships are formed for the primary purpose of providing affordable housing (usually apartment complexes) and generating tax credits for investors from real estate properties that qualify for low-income housing tax credits under Section 42 of the Internal Revenue Code. A typical affordable housing partnership structure involves two or three ownership tiers. A lower tier partnership is formed by a general partner, which typically is a real estate developer responsible for the operations of property, and upper tier partnerships that generally are limited partners. It is not unusual that additional tiers also exist above the limited partner tier.

At the inception of the affordable housing partnership structures, minimal, if any, consideration is given by the partnership or its investors to the property's potential sales value, which commonly can be nominal, upon expiration of the tax compliance period. Capital appreciation,

which is the residual cash flow available to partners after satisfaction of more senior claims (such as loan repayments and fees), is usually insignificant compared with the total cash flows (including consideration of tax credits to investors) of the partnerships.

Under the Exposure Draft, an entity that meets the express business purpose – that is, an entity that invests in real estate properties for total return including an objective to realize capital appreciation – would qualify as an investment property entity (provided it meets all other criteria). Some industry participants believe an affordable housing partnership would be considered an investment property entity because the partnership *may* realize a comparatively small amount of capital appreciation upon disposition of its real estate properties. These participants disregard the fact that affordable housing partnerships' primary business purpose is to provide affordable housing and generate tax credits for investors and not to generate capital appreciation.

Investments in real estate properties by affordable housing partnerships are long-term investments because the investments are not sold during the tax compliance period, which generally extends to 15 years or more. This long investment-holding period is attributable to the prohibitive consequences of premature sale, such as tax credit claw-backs, loss of fees and other penalties for not maintaining the low-income housing status of the properties during the tax compliance period. Further, the primary use of the partnerships' financial statements is for tax credit delivery and related activities. As such, we believe carrying affordable housing partnership investments in real estate properties at fair value would not benefit or provide meaningful information to the investors (partners) of the affordable housing partnerships.

To appropriately consider the nature and business purpose of affordable housing partnerships and to eliminate the potential for diverse interpretation of the Exposure Draft in the industry as is currently evident, we suggest the Board consider the following:

- If the Board proceeds with issuance of a stand-alone investment property entity standard or amends Accounting Standards Codification ("ASC") Topic 946, *Financial Services Investment Companies*, ("ASC 946") we suggest the Board consider either explicitly excluding affordable housing partnerships from the scope of the standard(s) or redefining the express business purpose to clarify that the Board's intent was, in fact, to *include* entities whose primary business objective is investing in real estate properties for total return other than capital appreciation, such as tax credits.
- If the Board adopts the guidance under International Accounting Standard ("IAS") 40, *Investment Properties*, ("IAS 40") we suggest the Board retain the option (rather than a requirement) to carry investments in investment properties at fair value or cost. This would allow entities, such as affordable housing partnerships, to better align their accounting models with their business objectives and produce more meaningful and beneficial financial information for their investors.

Convergence with IFRS

While we recognize the challenges the Board faces in its effort to align GAAP with IFRS, we also recognize that some fundamental differences would remain between the two sets of standards if the investment property entity guidance is issued as proposed in the Exposure Draft. That is, under the Exposure Draft, only the investments that are held by investment property entities would be carried at fair value while all real estate properties that meet the definition of an

investment property under IAS 40, may, at the option of the preparer, be carried at fair value and, further, be excluded from the scope of the proposed lease accounting standard. As a result, we believe the differences between the two sets of standards, including the prospective convergence on accounting for leases, will not be bridged but will result in more inconsistencies.

Uniformity among Real Estate Entities

Further, we do not believe the scope of the proposed guidance appropriately distinguishes entities that should qualify as investment property entities from those that should not qualify as investment property entities and, therefore, we believe the guidance, as proposed in the Exposure Draft, falls short of achieving consistency of accounting among similar entities.

For example, under the Exposure Draft, an entity that holds interests in investment properties through controlling financial interests of other investment property entities would account for its investments using a substantially different accounting model than an entity that holds significant but non-controlling interests in the same investment-property-entity investees. We believe that if two entities have same business objective (that is, primarily investing in real estate properties for capital appreciation) they should account for their investments in a similar manner regardless of what means the entities use to invest in the real estate properties. Similarly, as explained through examples in our response to question 3 in the Appendix, we believe the "substantially all" criterion would create inconsistencies in accounting between similar real estate entities and, therefore, would contribute to greater divergence in the industry than currently exists.

Summary

In summary, we believe a separate standard for investment property entities is not beneficial because, as proposed, it would not create consistency among similar real estate entities and does not closely align GAAP with IFRS. We believe the Board's objectives can be achieved through either of two alternative ways:

- Expand the scope of ASC 946 to include the entities that invest in investment properties; or,
- Provide a model that permits all investment properties to be carried at fair value or cost, similar to IAS 40.

However, if the Board issues a stand-alone investment property entity standard, we suggest the Board consider an entity's business objective and its primary business purpose when determining the criteria that an entity must meet to be an investment property entity. We believe including the criteria "substantially all" and "exit strategy" as currently interpreted in practice, may lead to greater diversity and unintentionally include (or exclude) entities that should be excluded (or included) in the scope of the standard as further explained in our responses to questions in the Appendix to this letter.

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Our responses to questions raised by the FASB of importance to AIG are included in the Appendix to this letter. Thank you for the opportunity to present our views. Please do not hesitate to contact me at (212) 770-8997 if you have any questions or need clarification with respect to any matters addressed in this letter.

Very truly yours,

/s/Tom Jones Director and Global Head of Accounting Policy American International Group, Inc.

APPENDIX

Definition and Scope

Question 1: The proposed amendments would require an entity that meets the criteria to be an investment property entity to measure its investment property or properties at fair value rather than require all entities to measure their investment properties at fair value. Should all entities measure their investment properties at fair value or should only an investment property entity measure its investment properties at fair value? Why? Is fair value measurement of investment properties operational? Please describe any operational concerns.

We do not believe a separate standard for investment property entities will provide greater comparability among similar entities nor will it promote convergence with IAS 40. We believe the Board should adopt the principles contained in IAS 40, including the option (rather than a requirement) to carry investments in investment properties at fair value or cost. This would allow entities to better align their accounting models with their business objectives and produce more meaningful and beneficial financial information for their investors.

However, if the Board believes real estate investment entities should carry their investment properties at fair value, we believe these entities should be included in the scope of ASC 946, provided the Board clarifies that affordable housing partnerships do not meet the criteria to be an investment property entity.

The primary purposes of affordable housing partnerships are to provide affordable housing and to generate tax credits for investors with minimal, if any, importance given to the fair value of the underlying real estate properties at the expiration of the tax compliance period. If these properties are required to be measured at fair value each reporting period, we believe the costs and operational burdens imposed on affordable housing partnerships would outweigh any related benefits.

Generally, however, the fair value measurement of investment properties does not cause significant operational concerns.

Question 2: The proposed amendments would require an investment property entity to measure its investment property or properties at fair value rather than provide an option to measure its investment property or properties at fair value or cost. Should fair value measurement of investment properties be required or permitted? Please explain.

If the Board adopts the guidance under IAS 40, we believe both fair value and cost measurement methods should be permitted choices, based on the related investment objective. This would promote convergence of GAAP with IFRS, ensure that the measurement of investment properties is aligned with the entity's primary business objective, and provide more meaningful financial information to the users of the financial statements.

However, if the Board issues a stand-alone investment property entity standard or amends ASC 946, we believe the entities in the scope of those standards should be required to measure their investment properties at fair value rather than have an option to measure their investment properties at fair value or cost, provided the Board clarifies that affordable housing partnerships do not meet the criteria to be an investment property entity. We believe only then can the Board

achieve its objective of reducing diversity in practice regarding the accounting by investment property entities.

Question 3: Do the criteria in the proposed amendments appropriately identify those entities that should be required to measure their investment property or properties at fair value, and, therefore, should be excluded from the scope of the lessor accounting model in the proposed Update on leases? If not, what changes or additional criteria would you suggest, and why are those criteria more appropriate?

We do not believe the criteria in the proposed guidance appropriately identify those entities that should be required to measure their investment properties at fair value. For example, an entity that holds "substantially all" of its investments in real estate properties indirectly through controlling financial interests in entities that meet the nature-of-the-business-activities and express-business-purpose criteria would qualify as an investment property entity. However, if the same entity holds 85% of its investments in controlled investment property entities and 15% of its investments in investment property entities in which the entity does not hold controlling financial interests, the entity would not qualify as an investment property entity. The same would apply when the entity has one significant equity method investment even if the entity's business objective and purpose has not changed. As such, the proposed investment-property-entity guidance would not identify those entities that should be required to measure their investment properties at fair value, and, consequently, would not exclude some investment properties that should be measured at fair value from the scope of the lessor accounting model in the proposed accounting updated on leases.

We suggest the Board modify the proposed nature of the business activities guidance to address the primary investment objective rather than the means through which that objective has been achieved (i.e., investments in real estate whether it be directly in real estate properties, indirectly through subsidiaries, or through investments in other investment property entities).

Questions 4: The proposed amendments would require an entity to reassess whether it is an investment property entity if there is a change in the purpose and design of the entity. Is this proposed requirement appropriate and operational? If not, why?

We agree that an entity must reassess whether it is an investment property entity if there is a change in the purpose and design of the entity.

Question 5: An entity that would be an investment property entity under the proposed amendments would be required to follow the accounting requirements in the proposed amendments even if that entity also would be an investment company under Topic 946. Is it appropriate for an entity that would meet the criteria to be both an investment property entity and an investment company under Topic 946 to be subject to the amendments in this proposed Update? If not, what alternative approach would you recommend if an entity would meet the criteria to be both an investment property entity and an investment company? Should the form of the entity (real estate fund versus real estate investment trust) dictate whether an entity should be an investment company or an investment property entity for accounting purposes? If yes, please describe the difference between the business activities of a real estate fund and a real estate investment trust to support your view.

If the Board issues a stand-alone standard for investment property entities, we believe the appropriate accounting determination should be based on the initial investment objective of the entity and this accounting should be consistently applied among similar entities; thus, we believe investment property entities should first be subject to the investment property entities guidance (if issued).

Nature of the Business Activities

Question 6: To be an investment property entity, the proposed amendments would require substantially all of an entity's business activities to be investing in a real estate property or properties. Should an entity's business activities be limited to investing in a real estate property or properties rather than investing in real estate assets in general (such as real-estate-related debt securities and mortgage receivables) to be an investment property entity? If not, why? Is this requirement operational? Please describe any operational concerns.

We do not believe an investment property entity should be limited to investing only in real estate properties because it may lead to a reduction in comparability among similar entities. For example, entity A may not qualify as an investment property entity because its investment portfolio consists of 15% investments in real-estate-related debt securities and 85% investments in real estate properties. However, a similar entity, entity B, may qualify as an investment property entity because its investment portfolio consists of 8% investments in real-estate-related debt securities and 92% investments in real estate properties. Therefore, if the Board issues a stand-alone standard, we believe the business activities should not be limited only to investing in real estate properties but also should include investments in real estate assets in general.

Question 7: The implementation guidance in this proposed Update specifies that when evaluating whether substantially all of the parent entity's business activities are investing in a real estate property or properties, the parent entity would not consider real estate properties held indirectly through investments in which the parent entity does not have a controlling financial interest. Should the evaluation of an entity's business activities consider properties held through noncontrolling financial interests (for example, investments in which the entity can exercise significant influence)? Why or why not?

If the Board issues a stand-alone investment property entity standard, we believe the evaluation of an entity's business activities should consider properties held through noncontrolling financial interests. As discussed in our response to Question 3, two entities with the same business activities and express business purposes would be accounted for under two different methods if one entity holds interests in real estate properties through controlling financial interests and the other does not. As such, the investment property guidance as proposed would not achieve consistency or reduce diversity in the industry.

Express Business Purpose

Question 8: To be an investment property entity, the proposed amendments would require that the express business purpose of an entity is to invest in a real estate property or properties for total return with an objective to realize capital appreciation, for example, through disposal of its real estate property or properties. Real estate properties held by an entity for either of the following purposes would not meet this criterion:

- a. The entity's own use in the production or supply of goods or services or for administrative purposes
- b. Development for sale in the ordinary course of business upon completion (such as land developers and home builders).

Is the express-business-purpose criterion operational? Please describe any operational concerns.

If the Board issues a stand-alone investment property entity standard, we believe the determination of whether an entity is an investment property entity should be based on the entity's investment objective and its primary business purpose. That is, the entity invests in real estate properties for total return with a <u>primary</u> objective to realize capital appreciation. We believe this clarification would eliminate potential diversity in practice because entities such as affordable housing partnerships, whose primary business purposes are to provide affordable housing and generate tax credits for investors, may be viewed by some industry participants as investment property entities, while others would view the same partnerships to be out of the scope of the proposed guidance.

Question 9: To meet the express-business-purpose criterion, the implementation guidance in this proposed Update would require that an investment property entity have an exit strategy to dispose of its real estate property or properties to realize capital appreciation to maximize total return. An entity that invests in a real estate property or properties to collect rental income long term and does not have an exit strategy for its real estate property or properties would not be an investment property entity under the proposed amendments. Should those entities be excluded from the amendments in this proposed Update? If not, why? Is the exit strategy requirement operational? Please describe any operational concerns.

We believe if an entity's primary business objective is to invest in investment properties primarily for total return other than capital appreciation, such as to collect rental income or to provide affordable housing and generate tax credits for investors, the entity should not qualify as an investment property entity. Thus, we suggest the Board consider the intent of the business objective and clarify the consideration of an exit strategy in the context of express business purpose.

Unit Ownership and Pooling of Funds

Question 10: To be an investment property entity, the proposed amendments would require an entity to have investors that are not related to the entity's parent (if there is a parent) and those investors, in aggregate, must hold a significant ownership interest in the entity. Is this criterion appropriate? If not, why?

We agree that an entity should have investors that are not related to the entity's parent.

Question 11: To be an investment property entity, the proposed amendments would provide an exemption from the unit-ownership and pooling-of-funds criteria for a subsidiary entity that (a) has a parent entity that is required to account for its investments at fair value with all changes in fair value recognized in net income in accordance with U.S. GAAP or (b) has a parent entity that is a not-for-profit entity under Topic 958 that measures its investments at fair value. Should this exemption be available only to a

subsidiary entity with a parent entity that is (a) required to account for its investments at fair value in accordance with U.S. GAAP or (b) a not-for-profit entity under Topic 958 that measures its investments at fair value? If not, which entities should be permitted to apply the exemption and why?

We believe an exemption should be provided for a subsidiary entity whose parent is required to account for its investments at fair value with all changes in fair value recognized in net income.

Measurement

Question 12: The proposed amendments would require real estate properties other than investment properties that are held by an investment property entity to be measured in accordance with other U.S. GAAP. Should an investment property entity be required to measure those properties at fair value with all changes in fair value recognized in net income instead of applying other U.S. GAAP? Why or why not?

If the Board issues a stand-alone investment property entity standard, we believe an investment property entity with real estate properties other than investment properties should follow other GAAP which, for example, allows entities to elect the fair value option for financial assets and liabilities when management believes such accounting provides investors with more relevant financial information.

Question 13: The proposed amendments would require a right-of-use asset in which the underlying asset meets the definition of an investment property to be measured at fair value with all changes in fair value recognized in net income. Should those right-of-use assets be measured at fair value with all changes in fair value recognized in net income? If not, why and which measurement attribute would you recommend for those right-of-use assets?

If the Board issues a stand-alone investment property entity standard, we agree that right-of-use assets should be measured at fair value.

Interests in Other Entities

Question 14: The proposed amendments would require an investment property entity to evaluate whether an interest in (a) another investment property entity, (b) an investment company as defined in Topic 946, or (c) an operating entity that provides services to the investment property entity should be consolidated under Topic 810. Should an investment property entity consolidate controlling financial interests in those entities? If not, why? Should an investment property entity consolidate controlling financial interests in other entities? If yes, why?

We do not believe that entities other than investment companies and investment property entities should be consolidated by an investment property entity. We believe all other investments including operating entities that provide services to investment property entities should be required to follow other GAAP, which, for example, allows entities to elect the fair value option for financial assets and liabilities when management believes such accounting provides investors with more relevant financial information.

Question 15: The proposed amendments would prohibit an investment property entity from applying the equity method of accounting in Topic 323 unless the investee is an operating entity that provides services to the investment property entity. Is that exception

to the equity method of accounting requirements in Topic 323 appropriate for investment property entities? If not, why?

If the Board issues a stand-alone investment property entity standard, we believe that an investment property entity with investments in which it can exercise significant influence should be required to follow other GAAP, which, for example, allows entities to elect the fair value option for financial assets and liabilities when management believes such accounting provides investors with more relevant financial information.

Question 16: The proposed amendments would require an investment property entity to measure investments in which it does not have a controlling financial interest or cannot exercise significant influence in accordance with U.S. GAAP. For example, that would currently require held-to-maturity debt securities to be measured at amortized cost and would permit certain equity securities to be measured using the cost method, unless the fair value option in Topic 825, Financial Instruments, is elected. Should an investment property entity be required to measure those investments at fair value with all changes in fair value recognized in net income instead of applying other U.S. GAAP? Why or why not?

If the Board issues a stand-alone investment property entity standard, we agree that an investment property entity with investments in which it does not have a controlling financial interest or cannot exercise significant influence should be required to follow other GAAP, which, for example, allows entities to elect the fair value option for financial assets and liabilities when management believes such accounting provides investors with more relevant financial information.

Financial Liabilities

Question 17: The proposed amendments would require an investment property entity to measure its financial liabilities (such as its own debt) in accordance with other U.S. GAAP, which currently requires amortized cost measurement unless the fair value option in Topic 825 is elected. Should an investment property entity be required to measure its financial liabilities at fair value with all changes in fair value (including changes in an entity's own credit) recognized in net income instead of applying other U.S. GAAP? Why or why not?

We do not believe investment property entities should be required to account for financial liabilities at fair value. We believe such entities should be required to follow other GAAP, which, for example, allows entities to elect the fair value option for financial assets and liabilities when management believes such accounting provides investors with more relevant financial information.

Rental Revenue Recognition

Question 18: The proposed amendments would require an investment property entity to recognize rental income on investment properties subject to a lease when lease payments are received or as the lease payments become receivable in accordance with the contractual terms of the related lease rather than on a straight-line or other basis. Is that basis of recognizing rental revenue appropriate for investment properties measured at fair value? If not, why?

We believe the proposed basis of recognizing rental revenue is appropriate for assets that are carried at fair value.

Practical Expedient for Measurement of an Interest in an Investment Property

Question 19: The proposed amendments would permit, as a practical expedient, an entity to estimate the fair value of its investment in an investment property entity using the net asset value per share (or its equivalent) of the investment if the entity would transact at the net asset value per share. Are there investments that currently qualify for the practical expedient that would no longer qualify for the practical expedient because of the proposed amendments? If so, please identify those types of investments.

We do not support the practical expedient provision as proposed in the Exposure Draft. If the Board issues a stand-alone investment property entity standard, we believe the practical expedient guidance for investment property entities should be consistent with the guidance under ASU 2009-12, Fair Value Measurements and Disclosures (Topic 820): Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent).

Disclosure

Question 20: Are the proposed disclosures appropriate for an investment property entity? If not, which disclosures do you disagree with? Should any additional disclosures be required? If so, why?

We believe the disclosures proposed in the Exposure Draft are appropriate.

Effective Date and Transition

Question 21: Should an entity recognize the effect of adopting the requirements in this proposed Update as an adjustment to the beginning balance of retained earnings in the period of adoption? If not, what transition requirements would you recommend and why?

We agree that if an entity is an investment property entity as a result of the proposed amendments it would report the effect of applying the amendments as a cumulative effect adjustment to retained earnings as of the beginning of the period of adoption.

Question 22: How much time would be necessary to implement the proposed amendments?

If the standard is issued as proposed, we estimate 12 months to be adequate time to educate, evaluate and implement the proposed guidance.

Question 23: The proposed amendments would prohibit early adoption. Should early adoption be permitted? If yes, why?

We believe early adoption should be prohibited to promote consistency of application.