KATHOLIEKE UNIVERSITEIT
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Economie en Bedrijfswetenschappen

The Impact of Disclosure and Audit Effort on the Reliability of Fair Value Estimates in the Real Estate Industry

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IAS40: Firms need to report *investment property* at historical cost or *fair value* in the *balance sheet*

Investment property:

Land or building to earn rental income

Fair value:

price/m^2

comparable asset or transaction

$$\sum_{i=1}^{i=n} \frac{FCF_i}{(1+r)^i}$$

DCF or rent capitalization

Use of market inputs

Use of model inputs

Balance sheet:

	Fair value	Historical cost
Market inputs		
Model inputs	X	

Value of investment property can be adjusted to manage income (FVBM firms)

Discretion present

Changes in fair value reported through the income statement

Research question 1

Can more disclosure and more audit effort increase the reliability of fair value estimates?

Disclosure:

Revelation of information in the financial statements
=> provides insight into accounting figures for external users

Investors do not value additional disclosure
-Overall disclosure low
-More disclosure when estimates are uncertain

Audit effort:

Evaluation of the financial statements by an auditor
=> ascertain the reliability

Investors value additional effort by the auditor for FVBM firms

Research question 2

Do firms improve their disclosure quality over time?
What determines the improvement in disclosures after IFRS adoption?

Local GAAP:

Local GAAP can include a standard for investment properties
=> this standard can allow fair value or prohibit it

The more similar both standards are the higher disclosure quality is

-effect can disappear over time : convergence
-effect can remain

Time:

- Firms will improve disclosure quality over time
- Firms will make adjustments in disclosure according to portfolio performance

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