



**Indonesian Accounting Standards Board**  
**Indonesian Institute of Accountants**

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# **Accounting for Telecommunication Tower in Indonesia**

Issue Paper



## EXECUTIVE SUMMARY

The Indonesian Accounting Standards Board (hereafter the Board) is confronted with issue regarding accounting treatment for telecommunication tower (hereafter tower). Entities in the telecommunication tower leasing industry (hereafter the industry) have different interpretations on how tower should be defined and thus recognised and accounted for (property, plant or equipment under IAS 16 *Property, Plant and Equipment*, or investment property under IAS 40 *Investment Property*). One potential significant effect of this is different profit and loss figure when the transaction is measured under the revaluation model (IAS 16) and fair value model (IAS 40). This gives significant impact on the comparability among entities in the industry, and more importantly different accounting treatments of transactions that in substance are the same and have similar economic consequences.

Tower could be in the form of either a physical structure permanently constructed in a specific location or a mobile facility that serve similar function with an advantage in mobility. The scope of this Issue Paper is specifically on the tower permanently constructed in a specific location, belongs to entities which engage primarily in telecommunication tower leasing, and with no association to entities who are telecommunication operators.

The first issue is whether tower falls under the definition and criteria of a building and thus considered to be a property, which both IAS 16 and IAS 40 do not clearly define. Because of this entities in Indonesia made reference to the definition of building in various laws and regulations issued by regulators in Indonesia. This however has caused an issue on whether tower can be classified as a building (property). Another point raised was that tower is a physical construction permanently constructed in a specific location. The focus is on whether there is any intention from the entities to relocate the tower, taking into consideration the technical, economical, and practical aspects of the relocation.

The second issue centred on the ancillary service element of the tower. The issue is on how to classify the element of service provided by the tower owners, taking into consideration some of the arrangements with the tenants. Other than this, another point raised is on the ability of tower to generate lease revenue independently from the entities' other assets.

In order to resolve this issue a clear definition of or guidance on what qualifies as a building is required. Perception on what a building is might not be the same in different jurisdictions, thus, it is important to clarify whether entities could make reference to general definition of a building as defined by regulators or as defined in the standards, to avoid different interpretations.

## **I. INTRODUCTION**

1. In September 2011, the Indonesian Accounting Standards Board (hereafter the Board) received a request to clarify the appropriate accounting treatment for telecommunication tower (hereafter tower), whether it should be accounted for as a property, plant and equipment under IAS 16 or investment property under IAS 40. The request came from the Indonesian Capital Market and Financial Institution Supervisory Agency as one of the regulators in Indonesia, who received inquiries from some entities in the telecommunication tower leasing industry (hereafter the industry).
2. The Board conducted discussions with representatives from regulators, accounting firms, and most importantly relevant entities to obtain more information on the issue.
3. This Issue Paper presents the different point of views on the accounting treatment for tower raised by some entities in the industry and some concerns from the Board with regard to this multi-interpretation issue.
4. The scope of this Issue Paper is specifically on the tower permanently constructed in a specific location, belongs to entities which engage primarily in telecommunication tower leasing, and with no association to entities who are telecommunication operators.
5. This Issue Paper is organised as follows:
  - a) Introduction to the Issue Paper;
  - b) Reasons for raising this issue;
  - c) Analysis
    - i. Definition of property / investment property in IAS 16 and IAS 40;
    - ii. Contrasting views raised by the industry; and
    - iii. Current development in the IASB – FASB project.
  - d) Concerns raised by the Board.

## **II. REASONS FOR RAISING THIS ISSUE**

1. As explained in the Agenda Consultation 2011 of the IASB, one of the five strategic areas driving the work of IASB is to improve consistency and quality of the application of IFRSs. This implementation issue is one key factor in ensuring the success of IFRSs convergence in different jurisdictions, each with its own sets of characteristics, local regulations, common practices, and problems.
2. Indonesia as the only G-20 member from the South East Asia region is well aware of the importance in adopting or converging to IFRSs, as the recognised global sets of financial reporting standards. As of 1 January 2012, Indonesia has converged its local standards to IFRSs.
3. During the convergence process, the Board is confronted with an issue regarding accounting treatment for tower. Entities in the industry have different interpretations on how tower should be defined and thus recognised and accounted for, whether it should

be treated as a property, plant or equipment under IAS 16 *Property, Plant and Equipment*, or whether it should be viewed as an investment property under IAS 40 *Investment Property*. One potential significant effect of this is different profit and loss figure when the transaction is measured under the revaluation model (IAS 16) and fair value model (IAS 40). This gives significant impact on the comparability among entities in the industry, and more importantly different accounting treatments of transactions that in substance are the same and have similar economic consequences.

4. Domestic law concerning the construction and utilization of tower governs that due to the efficient and effective use of space, the utilisation of tower should be shared. The law rules that tower should be used not only by one telecommunication operator. The owner of tower should lease the tower to telecommunication operators based on its capacity. To monopolise the use of tower is prohibited by the law.
5. The common business practice used by entities in the industry in Indonesia is as follows:

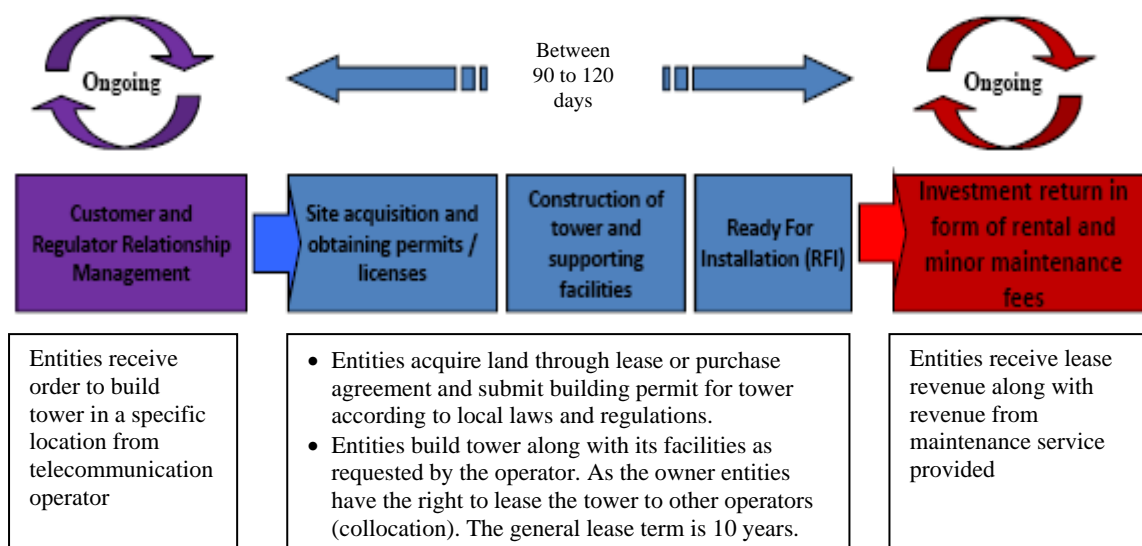


Illustration 1 – Common business practice of the industry in Indonesia

6. Other than the depiction above entities are also allowed by law to build towers without order from the operators as long as permission from relevant Government institutions are obtained.

### III. ANALYSIS

#### **Definition of Property / Investment Property in IAS 16 and IAS 40**

1. In defining what can be classified as a property the two main references introduced in IFRSs are those stated in IAS 16 *Property, Plant and Equipment* and IAS 40 *Investment Property*.

2. Paragraph 6 of IAS 16 defines property, plant and equipment as follow:  
*“Property, plant and equipment are **tangible items** that:  
a) are **held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and**  
b) are expected to be used during **more than one period**”*
3. The main characteristics that must be satisfied in order for a tower to be classified as a PPE under IAS 16 are:
  - a. The tower must be a tangible assets;
  - b. The tower is occupied by the entity; and
  - c. The tower is expected to last more than one year.
4. Paragraph 5 of IAS 40 defines investment property as follow:  
*“Investment property is property (**land or a building—or part of a building—or both**) **held** (by the owner or by the lessee under a finance lease) to **earn rentals or for capital appreciation or both, rather than for:**  
a) *use in the production or supply of goods or services or for administrative purposes;*  
*or*  
b) *sale in the ordinary course of business.*”*
5. The main characteristics that must be satisfied in order for a tower to be classified as a PPE under IAS 40 are:
  - a. The tower must be a property (land or a building—or part of a building—or both);
  - b. The tower is not owner-occupied; and
  - c. The tower is held by the entities to earn rental and / or capital appreciation.
6. Under IAS 40, property consists of either building or land, part of building, or both. IAS 16 and IAS 40 do not provide a clear definition and / or set of characteristics of what can be classified as a building. This lack of clarity led to entities in the industry to make references to the definition of building in various laws and regulations issued by different regulators.
7. The question is on how certain physical structures could be classified as building, and thus property, under either IAS 16 or IAS 40.



Illustration 2 – Is it similar to building?

**Contrasting Views Raised by the Industry**

CRITERIA	TELECOMMUNICATION TOWER	
	AS PROPERTY, PLANT AND EQUIPMENT	AS INVESTMENT PROPERTY
Definition of Property	Tower is a tangible asset used by the entities in their ordinary activities, in line with their business model, which is to generate revenue from leasing arrangement with telecommunication operators as their tenants. It is generally expected to be used during more than one period.	Tower is a property held by the entities to generate revenue from the leasing arrangement with telecommunication operators as their tenants, and not used by the entities in their ordinary activities. Entities also expect value appreciation through appreciation in the value of the land where the tower is constructed.
	Based on Indonesian tax regulation, income earned from lease of land and/or building is levied by a deemed (final) tax. The regulation states the scope of building that is levied by the deemed tax system, but based on the regulation tower is outside the scope of the regulation.	Based on the definition of tower as stated by the Ministry of Communication and Information  <i>Tower is a special building designed and constructed specifically for telecommunication service purpose, functioned as supporting structure to attach telecommunication equipments.</i>  <i>Permit to construct tower is permit to construct building under required laws and regulations.</i>
	Based on the company classification as defined by the Indonesian Stock Exchange (ISE), entities with the main business of tower leasing are classified under the Infrastructure, Utilities & Transportation Companies	Based on the definition of tower as stated in a joint law as issued by the Ministry of Communication and Information, Ministry of Home Affairs, and Ministry of Public Works

	<p>and not under the Property, Real Estate and Building Construction Companies.</p>	<p><i>Tower is a structure constructed for public purposes on a land, or a building constructed for public purposes with typically steel structure, where the function, design, and structure are meant as supporting structure to attach telecommunication equipments.</i></p> <p><i>Permit to construct tower is permit to construct building issued by local Government to the telecommunication tower owners to either construct new towers or modify towers based on required administrative and technical requirements.</i></p>
<p>Physical Characteristics</p>	<p>Tower even if permanently constructed is similar to equipment in a sense that should required it could be relocated to other locations. Some of the considerations raised for this are:</p> <ol style="list-style-type: none"> <li>1. Should it be required and considered to be beneficial, technically speaking, entities could dismantle, relocate and reconstruct the tower in other locations. This process is considerably easier compared to relocating other assets or structures that are generally considered to be a building.</li> <li>2. From the economic perspective, entities could always consider whether the benefit is significantly higher compared to the potential costs of relocating the tower.</li> </ol>	<p>Tower is characteristically similar to a building in a sense that it is permanently established / constructed in a specific location. Some of the considerations raised are:</p> <ol style="list-style-type: none"> <li>1. From the perspective of practicality, generally there is no intention to relocate unless required by certain laws or regulations issued by the Governments.</li> <li>2. From the economic perspective, the costs incurred to dismantle, relocate, and reconstruct the tower is considerably significant (approximately 70% of the total costs of the tower).</li> <li>3. From the technical perspective, the decision to construct a tower in a particular area is based on the quality of networks available as part of the network of towers available in that particular area. Relocating</li> </ol>



		<p>the tower would affect the quality of the network coverage (network interruption), which would affect tenants' decision in leasing a particular space on a particular tower in a particular area.</p>
	<p>Tower is a mechanical structure consisting of steel structure and other supporting components used to serve a specific purpose in a telecommunication process. This can be considered similar in characteristics to advertising board / tower (space), which in practice is accounted as equipment (PPE).</p>	<p>There are no physical limitations in dimension or shape on what constitutes a building. An example for this would be a house constructed on a knock-down basis, which is still considered a building. A tower could be seen to be similar to a knock-down house in this sense.</p>
<p>Telecommunication Tower as an Integral Part of a Building / Land</p>	<p>Tower is closer in characteristics to those of equipment since it is mobile as it is not permanently attached to a particular building or land. Also, what is considered to be an integral part could be seen from a perspective where a particular land or building would generally still serve its functions regardless of whether a tower is attached to it.</p>	<p>Based on the definition as stated by the Ministry of Communication and Information, Ministry of Home Affairs, and Ministry of Public Works</p> <p><i>Telecommunication tower is a structure that is constructively attached to a building, thus it can be considered to be an integral part of a building or land on where it is constructed.</i></p>

		<p>The value of the lease arrangement consists of components representing the value of the land or building where the tower is constructed, the value of the networks available in that particular location, and the value of the tower. This illustrates how tower is integrated with the building or land where it is constructed.</p>
<p>Ancillary Service Element</p>	<p><u>Paragraph 12 of IAS 40</u>  <i>“In other cases, <b>the services provided are significant.</b> For example, if an entity owns and manages a hotel, services provided to guests are significant to the arrangement as a whole. Therefore, an owner-managed hotel is owner-occupied property, rather than investment property.”</i></p> <p>The service provided in the arrangement between the entities and the customer / tenant is considered to be significant. Taking the example of the owner-managed hotel, the entities acts as both the owner of the tower leased by the tenant and the manager providing the service bought by the customer in the form of access to the network available in the area where the tower is constructed. The service is considered to be the main element bought by the tenant, where the physical tower</p>	<p><u>Paragraph 11 of IAS 40</u>  <i>“In some cases, an entity <b>provides ancillary services</b> to the occupants of a property it holds. An entity treats such a property as investment property <b>if the services are insignificant to the arrangement as a whole.</b> An example is when the owner of an office building provides security and maintenance services to the lessees who occupy the building.”</i></p> <p>Typical lease arrangement would include a portion of “service” where the entities would be responsible for the routine maintenance, security, and other things as specified in the arrangement. Although entities provide these services they are considered to be insignificant to the arrangement as a whole (generally ranges between 5 and 10% of the overall value of the arrangement).</p> <p>Other example similar to this type of arrangement is</p>

	<p>only acts as the media just as a hotel room in the owner-managed hotel example.</p> <p>In addition, the owner is the party that operate and manage the tower. Tenants have no power to manage/operate the tower and have no physical access to the tower. Tenants only place their transmitter-receiver device and responsible only for the device, not to the tower. This condition is similar to an owner-managed hotel example.</p>	<p>maintenance and security service provided by building management in an office lease arrangement.</p>
<p>Business Model</p>	<p>The entities' business is to provide network access to the tenants through leasing arrangements where tenants could lease a particular space to attach their telecommunication devices in order to gain access to the network available in the area. The entities are using the tower as a mean to deliver this network access to the tenants. This is generally similar to an owner-managed hotel situation.</p> <p>Tower is only of value when the tenancy ratio is high, thus affecting the overall quality of the network coverage available. This is different to assets generally considered as building where it will generally increase in value over time.</p>	<p>Business model of the entities is to lease the tower to the telecommunication operator. The main objective is to increase the tenancy ratio per tower. The increase in the tenancy ratio would increase the earnings and cash flows of the entities which in the end will increase the value of the tower. This is generally similar to an office lease arrangement.</p> <p>The selling price of a tower does not depend on the historical value of the tower, but on the lease value of the tower and the tenancy ratio. Consequently, entities believe that tower should be measured using the fair value model so that the carrying value of the tower at the statement of financial position will reflect the increase in the value of the entities' tower.</p>

<p>Ability to Independently Generate Cash Flows</p>	<p><u>Paragraph 7 of IAS 40</u>  <i>“Investment property is held to earn leases or for capital appreciation or both. Therefore, an investment property generates cash flows largely independently of the other assets held by an entity. This distinguishes investment property from owner-occupied property. The production or supply of goods or services (or the use of property for administrative purposes) generates cash flows that are attributable not only to property, but also to other assets used in the production or supply process. IAS 16 Property, Plant and Equipment apply to owner occupied property.”</i></p>	
	<p>In generating the lease revenue entities use other assets such as other towers and other supporting assets to provide the benefit of network to the tenants. Thus the cash flows generated is dependent to other assets.</p>	<p>Cash flows generated from a tower is independent to the other towers or assets of the entities. In an arrangement between the entities and the tenants generally a particular space on the tower is leased to a particular tenant / operator. The cash flows from that particular space would be independent to the conditions that might affect other spaces in other towers that might be in the possession of the entities.</p>
	<p>Technically speaking, a network is created through continuous chains of towers communicating signal to generate a network in the area. Communication also exists between networks. A single tower cannot create a network, which is something that is of the concern of the tenants. Without the existence of network a tower would be without economic value and thus bring no economic benefit to the entities.</p>	<p>Entities could still generate cash flows from a tower that they have regardless of the conditions of other towers that they might have (from the point of view of the entities), assuming that they could still access the network created by other towers that might be available in the area (owned by other entities).</p>

### **Current Development in the IASB – FASB Project**

1. On 24 January 2012, IASB issued a staff paper of the IASB working group meeting on leases, Agenda ref 3 – Lessor Accounting: The definition of investment property. The paper discussed the issue about investment property as follows:

*“The FASB’s Investment Property Entities Exposure Draft (IPE ED) defines equipment integral to real estate property as **“any physical structure or equipment attached to the real estate, or other parts thereof that cannot be removed and used separately without incurring significant cost”**. This definition would, therefore, include assets such as **cell-towers as items of investment property** (which are likely to be excluded from the IAS 40 definitions)...”*

2. Based on the FASB’s IPE ED, tower could be classified as an investment property. On the other hand, it could not be classified as a property according to IAS 40. However, there is no detail explanation about why it could not be classified as a property according to IAS 40.
3. The definition of equipment integral to real estate property as introduced by FASB shows that there is a difference on how to view a particular asset, in this case telecommunication tower between the IASB and FASB. The issue here is whether IAS 40 provides sufficient guidance in classifying whether certain assets such as tower would be considered to be an investment property.

### **IV. CONCERNS RAISED BY THE INDONESIAN ACCOUNTING STANDARDS BOARD**

1. The Board acknowledges the arguments raised by the industry, and believes that in order to decide on the accounting treatment for the tower the focus should be on the definition of building (and thus property). The lack of definition on what constitutes as building has become the main issue faced by entities in the telecommunication tower leasing industry in Indonesia. Both IAS 16 and IAS 40 do not provide clear definition of building and the characteristics of assets that could be classified as one. This lack of clarity creates multi-interpretation issue in defining the very nature of telecommunication tower. Due to the absence of clear definition, entities in Indonesia made reference to various laws and regulations, which leads to further discrepancies in how to define and account tower.
2. Taking into consideration similar users needs with regard to fair value information of tower and investment property, the Board would also like to raise concern about how IAS 40 is only limited to property as means of investment. If the intention of IAS 40 is to include assets such as the tower to be a property, the Board believes that the current definition in IAS 40 is not sufficient to capture that intention. On the other hand, if the

tower is not considered to be a property, the needs of users with regard to fair value information might not be satisfied, particularly if entities elect to use cost model.

3. The Board would like the view of other emerging economy countries regarding this particular issue. If this issue is proven to be a common issue between EEG members, Indonesia would like to propose an establishment of an EEG Working Group to further investigate the problem and to come up with a resolution on how to approach and resolve this issue.

\*\*\* End of Issue Paper \*\*\*