



**UNIVERSITY OF GOTHENBURG**  
**SCHOOL OF BUSINESS, ECONOMICS AND LAW**

Master Degree Project in Accounting

## **How and why are Accounting Choices Being Made?**

A case study concerning accounting choices of component depreciations in  
Swedish real estate companies

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# Abstract

**Title:** How and why are accounting choices being made?

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## Background and problem discussion

A large accounting choice is which depreciation method to use since it has a large impact on the financial statements. In K3 there is a new area, namely component depreciation, which has to be implemented on current assets if they have more than one substantial component. Especially for real estate companies, this will have a large impact. Since the area is new, there is a lack of guidance for how to implement component depreciation and there is almost no praxis available.

## Purpose

Because of the problematic discussions around the new accounting choice of component depreciations, the purpose of this thesis has been to investigate how and why they have made these choices of for example which component to use and their depreciation period.

## Method

Qualitative interviews have been performed with seven real estate companies in order to understand how they have implemented this new area in practice. We have had interview questions of which components they have chosen and why they have chosen those components. Moreover, internal documents consisting of examples and calculations regarding component depreciation have been received from the companies.

## Analysis and conclusion

Component depreciation is a part of K3 to increase the true and fair view in accounting. Most companies have chosen rather similar components and they have had similar drivers behind their choices. Also, the managers have been affected by almost the same external forces as there was a lack of guidance there were no praxis of how to implement it.

## Keywords

Accounting choice, component depreciation, institutional forces.

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# 1. Introduction

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*The introduction is the beginning of this story and the background gives an insight of the remaining part of this study. The problem discussion will enrich the reader of the problem we want to raise which will be presented as the research question in the end of this chapter.*

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## 1.1 Background

Accounting aims to present relevant information to a company's stakeholders which they can use in order to make appropriate decisions (Smith, 2006). Financial statements are supposed to show a true and fair view of a company's financial position (Marton et. al, 2013). As a reader one expect to be able to rely on the presented financial statements but there exist choices within accounting regulations which could affect the result. The concept of accounting choice refers to how a company will choose to do their accounting (Marton, 2013). The definition of an accounting choice is: *"Any decision that whose primary purpose is to influence, either in form or substance, the output of the accounting system"* (Francis, 2001). Accounting choices are problematic within accounting since it is not possible to find rules for all imaginable circumstances. Therefore, it is impossible to eliminate that accounting choices have to be made; they will always exist in some way (Fields, Lys and Vincent, 2001).

Accounting can be regulated on an international level, such as International Financial Reporting Standards, namely IFRS, for large listed companies and it can also be regulated on a local level, for example the new Swedish framework K3, aimed for large non-listed companies in Sweden. Frameworks can be either principle-based or rule-based, where rule-based frameworks consist of more concrete guidelines for how to account in specific situations. The frameworks mentioned above are both principle-based which means each user has to interpret and make own judgments according to true and fair view (Marton et al., 2013). Therefore, companies have some freedom of act to adjust and interpret the frameworks in order for them to benefit their business (Marton, 2013).

When managers have to make a decision, an accounting choice, they encounter a problem. The managers choose a set of accounting choices that in practice determine the profit and depending on these choices the managers have both a possibility and the flexibility to affect the profit in a desirable direction. Therefore, there exists flexibility for managers to choose a set of accounting methods that accomplish different accounting objectives (Dechow, Ge and Schrand, 2010).

Managers tend to wanting to shape their accounting by doing certain accounting choices in order to achieve their particular objectives (Hagerman and Zmijewski, 1979). Managers are presumed to act in self-interest and an opportunistic manner when making accounting choices. A company makes certain choices depending on a number of drivers influencing them. Therefore, depending on different drivers, the companies will implement certain accounting

methods in their business (Hagerman and Zmijewski, 1979). The external environment influences the companies and the managers within in them and therefore also the choices they make. Accounting choices will influence the financial statements and the managers have a possibility to affect these. One question of interest is how to depreciate current assets, since that is an accounting choice which could have a large impact on the financial statements.

### **1.1.2 Depreciation**

An accounting choice which can have a large impact on the financial statements is the decision regarding how to depreciate the companies' current assets. Current assets are assets which are supposed to be used for at least one year in the company. Depreciation is when a company allocates the value of a current asset over its economic life. That is called the depreciation period and will depend on the kind of asset and for how long the asset will be used in the company (Marton, 2013). The chosen depreciation method will have effect on the financial statements. A short depreciation period of an asset will lead to higher costs in the earlier years which will decrease the profit for these years while it will increase the profit later on, as the costs are decreasing. One can choose if the depreciation should have large or minor effect on the financial statements, as well as if it should increase or decrease the profit. Though, over time the depreciation amount will be the same (Marton, 2013). The companies are expected to choose a depreciation method that reflect the consumption of the current assets future economic benefits (BFNAR 2012:1, 17.20).

### **1.1.3 Swedish context**

For larger, non-listed companies in Sweden there is a new local framework called K3 that had to be implemented from financial years started after the 31th December 2013. When a new framework is implemented, there arise new accounting choices which have to be made. These new choices may create an uncertainty regarding which choices are most accurate. One example is the new area in K3 about component depreciation on current assets. The accounting choices for component depreciation are mainly which components to select and which depreciation periods to use. For example, a real estate consists of many substantial parts and will have to be divided into components which will be depreciated separately (Drefeldt and Törning, 2013). Real estates are a large part of total assets in a company and consequently the depreciation will have a large impact on the financial statements. Therefore this new regulation will have a large effect, especially for companies operating in the real estate industry.

Furthermore, there existed an uncertainty and lack of confidence among companies regarding the implementation of the new area of component depreciations. There were a lot of choices companies faced as an effect of the new framework, K3. Companies had to decide upon which components to divide their real estates into as well as which depreciation periods to use on the components. Therefore, companies faced a lot of choices and had to make the decisions according to true and fair view. For this reason uncertainty appeared as there was no praxis to receive guidance from.

## **1.2 Problem discussion**

Even though accounting is regulated, there still exist choices of which accounting method to use. One example is the depreciation for current assets and how it should be estimated. Depending on how the depreciated amount will be calculated, it will have consequences on the profit and affect the financial statements which then in turn will impact the investment decisions. It has been shown that choices made for external financial reporting purposes influences managers in their decisions of capital investments. For example companies using accelerated depreciation make significantly larger capital investments than companies using a straight-line depreciation method (Jackson, Liu and Cecchini, 2009). If a company within the transfer to K3 choose a more aggressive depreciation method than earlier the influences on the profit would be larger since the costs are higher in the earlier years. Thus, over time this will not have any effect but it can affect the profit for a particular year. Of course one can also choose to do the opposite in order to have a smaller impact on the profit in earlier years of the current asset's economic life.

These accounting choices could be driven by a number of drivers and by analyzing the accounting choices made, one can try to understand why a manager act the way they do in a specific situation. As mentioned above, depreciation is an important accounting choice because it could have a large impact on the financial statements. Regarding component depreciation, which was a new area in Swedish accounting, several choices existed. For example, how many components should a real estate be divided into and how should the depreciation period of these components be estimated. To make these choices in practice required a lot of own judgment in order to implement a suitable accounting method for the focal company. Different managers had different drivers to conduct the choices they made, for example as assumed in Positive accounting theory managers are opportunistic and act in self-interest when making accounting choices. When a new framework is implemented a flexibility to change the depreciation method within the company exist in order to gain a larger or smaller effect on the financial statements in the earlier years. On the contrary the Institutional theory assumes that managers make the choices they do because they are influenced by the external environment to behave in a certain way which therefore affect their accounting choices. These different drivers can create differences between similar companies but also similarities between different companies. Having these theoretical explanations of accounting choice in mind, this study aims to bring a particular context of Swedish real estate companies into discussion and to illustrate how accounting choices regarding component depreciation on real estates have been made in practice.

## **1.3 Research purpose**

The purpose of this thesis is to investigate how and why companies have made their accounting choices regarding component depreciation on real estates. The study will be



conducted in a Swedish context exploring how and why Swedish real estate companies have done these accounting choices regarding component depreciation on real estates when initially implementing the new framework K3 in their financial statements.

## **1.4 Research question**

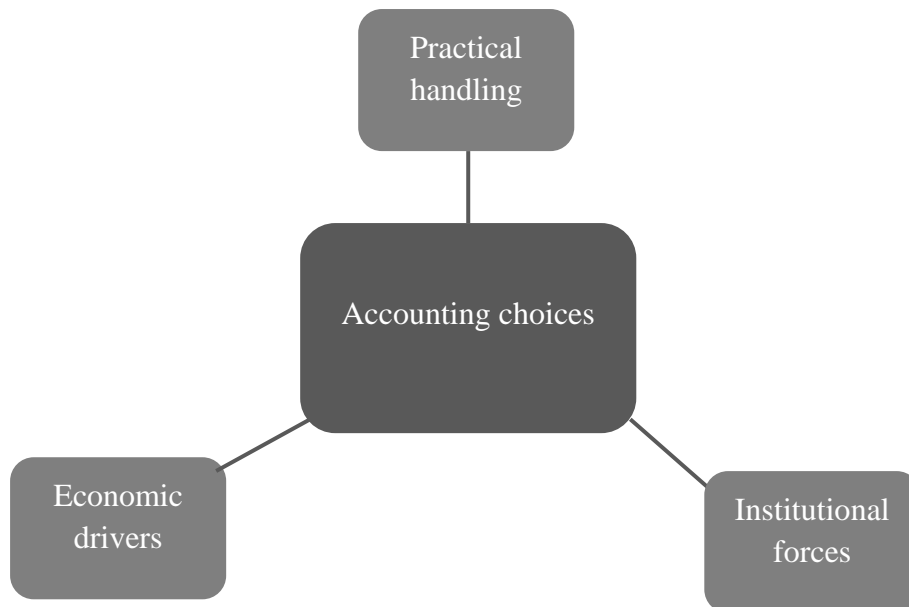
Our background and problem discussion have made us formulating our research question as following:

*“How do Swedish companies using K3 make their accounting choices regarding component depreciation and why are these choices being made?”*

## **1.5 Research design**

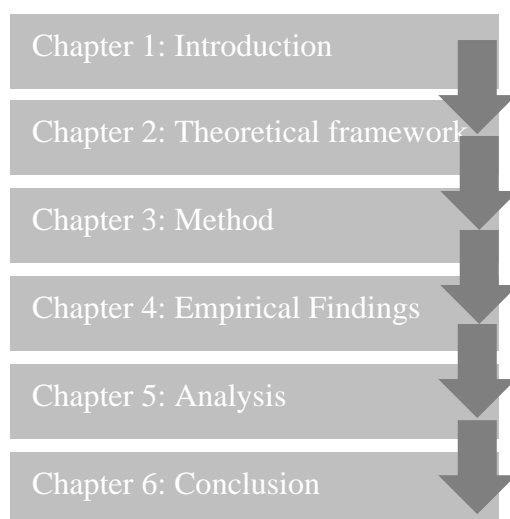
To be able to answer our research question and fulfill the purpose of this thesis we have performed qualitative interviews with Swedish real estate companies. The companies included in this study are of different size and owns different kinds of real estates. The focus lain within the understanding of both how and why the companies had made the accounting choices they had done, especially choices regarding component depreciations. To be able to answer the how question we have asked them about the processes developing the practical handling used. We have also looked at their internal documents in order to get a greater understanding of how the choices of component depreciation have been made. To be able to answer the why question we have asked our respondents of the processes and who have been involved in the accounting choices of component depreciation. By understanding the processes behind the choices made, we are able to understand the drivers behind the choices, in other words, why these choices had been made.

The empirical findings from the interviews will then be analyzed based on the theoretical framework. In order to do conduct this analysis we developed an analysis model where our research question, *“How do Swedish companies using K3 make their accounting choices regarding component depreciation and why are these choices being made?”* are the center of attention. This question has been analyzed from different perspectives namely practical handling, economic drivers and institutional forces. The practical perspective has primarily been used to answer the how question while the other perspectives have been used to analyze why the companies included in this study had made these choices. The economic drivers are closely linked to the Positive accounting theory while the institutional forces are connected to the Institutional theory.



## 1.6 Disposition

The introduction chapter first introduces the problem investigated in this thesis, which is substantiated under the headlines named background and problem discussion. In the theoretical framework relevant theories and previous research are presented to later on be applied on the empirical findings. The method chapter describes how this thesis has been conducted and its approach to answer the research question. The empirical findings consist of interviews with CFOs of seven Swedish real estate companies with interview questions based on the research question in this study. In the analysis chapter the theories are applied on the empirical findings to provide an understanding of how and why the accounting choices regarding component depreciation have been made. Finally the findings from this study are highlighted in the conclusion together with our suggestions for further research.



## 2. Theoretical framework

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*The theoretical framework chapter is starting out explaining accounting choices and supposedly the choice of component depreciation. To explain why managers make their choices, Positive accounting theory and Institutional theory will be included as well as other previous research which will explain which external forces will affect the managers choices.*

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### 2.1 Literature review

The approach of this study is to investigate how real estate companies in Sweden make their accounting choices with focus on component depreciation on real estates. Previous research regarding accounting choices have been included in the literature search as well as articles concerning depreciation and component depreciation to develop a better understanding of how companies make their choices. The theories used in this study are Positive accounting theory and Institutional theory. As well as the articles about accounting choices, depreciation and component depreciation the articles regarding Positive accounting theory and Institutional theory gives us a better understanding of how real estate companies think about their choices of which components to divide their real estates into and how to decide the depreciation period. The theories are relevant in this context since they are the basis for how companies are influenced and why the companies make the choices they do. Together with the collected empirical findings, the theories have helped us with a deeper understanding for the accounting choices made in the studied companies, why they have made the accounting choices they have done regarding component depreciation. The theories will be helpful in order for us to be able to answer our research question.

### 2.2 Positive accounting theory

Positive accounting theory aims to explain and predict the accounting choices made by the managers in companies. The theory is explaining why managers make certain choices and intend to create an understanding of why managers act the way they do (Watts and Zimmerman, 1978). Watts and Zimmerman developed the Positive accounting theory by hypothesizing economic drivers for managers in selecting accounting methods (Zmijewski and Hagerman, 1981).

Positive accounting theory is based on the Principal agent theory, where managers' self-interest and opportunistic decisions are being explained (Ryan, Scapens and Theobald, 2002). An important relationship within a company is the relationships between the principals and the agents, where the principals are the shareholders of the company and the agents are the managers. Since the agents' work for the principals', conflicts are inevitable as the agents have additional information regarding the company and consequently information asymmetry arises (Grönlund, Tagesson and Öhman, 2010). The agents are deciding regarding the accounting choices for the companies and are therefore able to make decisions best suited for

themselves, which represents the opportunistic behavior (Ryan, Scapens and Theobald, 2002). Managers usually prefer accounting methods which will maximize their self-interests, which are the core of Positive accounting theory (Gordon, 1964).

Positive accounting theory can give an understanding of accounting phenomena's. The largest question within Positive accounting is why managers make the choices they do. It could be explained by the mental processes or beliefs of the managers. However, not every human being will make the same choices even if they face a similar situation. It is also possible for two different persons to make the same choice in different situations (Kabir, 2010).

Managers' actions are based on their desires, needs, preferences as well as their self-interests and their choices are influenced by their view of the world. They do not decide randomly which accounting methods to use; all choices are based on facts (Dhaliwal, Salamon and Smith, 1982). Positive accounting theory can help decision-makers to understand how different drivers interact within the world. Relevant drivers are determined from the decision model used by the managers (Ryan, Scapens and Theobald, 2002). Watts and Zimmerman (1978) implies that the accounting methods used in a company some way is related to the special characteristics of the company or the industry the company operates in (Dhaliwal, Salamon and Smith, 1982).

### **2.3 Accounting choices**

There exist a lot of drivers which all have influences on managers' choice of deciding which accounting methods to use in their company. According to Hagerman and Zmijewski (1979), Watts and Zimmerman (1978), are explaining accounting choices as managers wanting to adjust their accounting methods. Therefore, managers make different accounting choices to achieve their self-interest (Hagerman and Zmijewski, 1979).

According to Watts and Zimmerman (1978) the five drivers influencing managers' accounting choices are *taxes*, *regulation*, *political costs*, *information production costs* and *management compensation plans*. The first one, *taxes*, is connected to accounting, for example by inventory valuation. The driver *regulation* handles the effect of changes in regulation and *political costs* relates to the power which political forces have on various groups and companies. *Information production costs*, such as bookkeeping costs, could influence when there is a change in accounting praxis and the companies are required to change their accounting methods. *Management compensation plans* are a large driver when companies have bonus plans. Then, managers tend to choose to implement accounting methods which will increase the profit.

Furthermore, Hagerman and Zmijewski (1979) discuss another five drivers which have an impact on managers' accounting choices. Those are *size*, *risk*, *capital intensity*, *competition* and *incentive plans*. The first one, *size* is related to large companies which will have drivers to choose accounting methods that reduces profit. *Risk*, may affect the choice of accounting methods. *Capital intensity* refers to that a capital intensive company will report a higher profit than a labor intensive company. Therefore, capital intensive companies will have drivers to

select accounting methods which will decrease profit. *Competition* impact as managers want to reduce competition in interest for them. Higher profit increases the competition which creates drivers for managers to reduce the profit. The last driver is *incentive plans*, if a company has bonus plans it may affect the manager's choice of accounting methods (Hagerman and Zmijewski, 1979).

Another driver added in the discussion of accounting choices are the relationship between ownership structure and adopted accounting method. Dhaliwal, Salamon and Smith (1982) have compared depreciation methods used of management-controlled and owner-controlled companies. They conclude that there is a significant difference in depreciation method for a management-controlled company compared to an owner-controlled company for financial reporting purposes. Management-controlled companies are generally larger than owner-controlled companies and Watts and Zimmerman (1978) argues that depending on the size of the company, the managers' tend to choose different accounting methods depending on what they want to achieve as well as differences in their self-interests. Usually, managers' chose either accounting methods which will increase or decrease the profit in order to complete their self-interests.

### **2.3.1 Depreciation**

Accounting choices are a problematic area within accounting. One frequent accounting choice which managers always are trying to manage is how to depreciate the company's current assets. The definition of depreciation is to allocate the cost of the assets over the estimated economic life. Accounting depreciation exists to correspond with the actual wear and tear of the asset (Stárová and Cermáková, 2010). Moreover, no depreciation method is appropriate for all assets. However, there is one depreciation method that is proper for each individual assets (Reynolds, 1961). Depreciation is affecting the cost structure and therefore also the profit, which makes it one of the most important accounting choices (Filatov, Rudykh and Kiryukhin, 2014). Furthermore, the choices regarding depreciation method could depend on whether the managers want to increase or decrease the profit depending on their self-interest as mentioned in previous sections (Hagerman and Zmijewski, 1979).

### **2.3.2 Component depreciation**

Component depreciation is a depreciation method that refers to if there are components with different economic lives within an asset, that asset has to be divided into components which have to be depreciated separately. Though, these components needs to be significant for the specific asset (BFNAR 2012:1, 17.4; 17.11). According to Tidwell (1977) there are no arguments to believe that different components within a building should have the same expected economic life. Component depreciation is therefore implemented to increase the true and fair view for both the recognition of an asset, but also the accounting in a company (Stárová and Cermáková, 2010; Hellman, Nordlund and Pramhäll, 2011). Especially buildings and real estate's consists of several components and naturally, not all of those components have the same physical and functional economic life (Davis and Wyndelts, 1979). For example, a building could be divided into: elevator, foundation, bathroom, kitchen, front,

windows and metal roof. These components are substantial for a building to function properly and should therefore be depreciated separately (Drefeldt and Törning, 2013).

One can group the components together into logical groups, if they have the same purpose, economic life and functions. Hereafter, one can depreciate the assets in the group in an identical way (Saliers, 1937). However, a component is only a component of the building as long as it contributes to the building producing profit. Therefore, the choice regarding economic life is related to how long the component will continue to contribute to the building (Gilliland, 1989). When replacing a component of an asset the valuation should not be a problem since each component can be purchased separately (Stárová and Cermáková, 2010). When using an asset for a long time, components will be replaced and therefore the components should be depreciated separately (Müllerová and Paseková, 2014). Moreover, when a company is using component depreciation the depreciation will reflect the actual wear and tear of an asset in a more preferable way (Stárová and Cermáková, 2010).

Whether repairs and maintenance should be capitalized or expensed have always been a difficult choice to make (Reynolds, 1961). Nowadays, many components which have been replaced have been expensed and not capitalized which would be better in order to increase the true and fair view (Hellman, Nordlund and Pramhäll, 2011; ÅRL, 2.2; Engström, 2009; Grönlund, Tagesson and Öhman, 2010). The aim with this kind of depreciation is to provide the user of the financial statements with more information regarding depreciation of current assets, especially for users without any specific knowledge in accounting (Drefeldt, 2014).

## **2.4 Swedish context**

K3 (BFNAR 2012:1) is the new main accounting framework in Sweden for financial years started after 31th of December 2013 (Nordlund, Pramhäll and Drefeldt, 2013). It is a principle-based framework like IFRS, where each user has to interpret and make own judgments according to true and fair view (Marton et al., 2013). Before the K-project, there were a large number of different frameworks in Swedish accounting and it could be hard to interpret and seek guidance. Therefore, Bokföringsnämnden, BFN, decided to consolidate those different regulations into a new, joined framework. The new framework was supposed to be an aggregated framework of the earlier ones, which should be easier to use (Smith, 2006). They decided to imitate IFRS for Small and Medium-sized Entities, SMEs, a simpler framework of IFRS which is the framework for all listed companies in the EU (Grönlund, Tagesson and Öhman, 2010).

The K-project is divided into four categories where each category represents a company category. The smallest companies, who have a turnover of maximum 3 MSEK, use K1. Small companies who do not fulfill the requirements to be a large company are allowed to use K2, the simpler variant of the main framework K3. The last category is sometimes called K4 and relates to listed companies which need to apply IFRS. The definition of a large company is when more than one of the requirements below is fulfilled during one of the last two financial year (Backlund et al., 2012):

1. The average number of employees has been more than 50.
2. Total assets have been more than 40 MSEK.
3. Turnover has been more than 80 MSEK.

Since K3, as mentioned above, is a principle-based framework it may be better suited for larger entities with more complex accounting choices. Larger companies are often demanding a more flexible framework, while smaller companies often demand more guidance in order to achieve true and fair view. Moreover, a principle-based framework demands more competence from its users (Carmona and Trombetta, 2010).

Component depreciation implicate as mentioned above, that significant components with different economic lives within an asset should be depreciated separately. This depreciation method has not been used in local Swedish frameworks before the publication of K3. Earlier, replaces of components were expensed instead of capitalized as assets in the balance sheet. This is a large change from previous regulations. According to BFNAR 2012:1, 17.5 components which are being replaced should be capitalized. Therefore, maintenance of components should be capitalized while smaller services or repairs should be expensed according to BFNAR 2012:1, 17.5.

Industry organizations issued guidelines for how to implement K3 and component depreciation on real estates correctly. One example is SABO, Sveriges Allmännyttiga Bostadsföretag, which guideline many companies in Sweden have used. It was published in May 2013 for all members in the organization SABO and is issued to be a guideline for how to implement component depreciation on real estates in practice (SABO, 2013). SABO is a well-known industry organization for real estates companies since they interpret new frameworks and publish assistance to implement them among other things. Also Fastighetsägarna and FAR, Föreningen Auktoriserade Revisorer, have released guidelines for how to implement component depreciations. Nevertheless, SABO is more addressed to companies owning residential properties while FAR is more general for all real estates.

## **2.5 Institutional forces**

Institutional theory aims to explain why companies are becoming more homogeneous by changing their behavior to pressures around them in the external environment (DiMaggio and Powell, 1983; Greenwood and Hinings, 1996; Phillips, Lawrence and Hardy, 2004). When a group of companies emerge within an industry, external stakeholders will try to make them become more alike. However in the long run, companies within an industry change (DiMaggio and Powell, 1983). A company sometimes adopts specific organizational structures to gain legitimacy. This theory views companies as working within a social framework of norms, values and taken-for-granted assumptions about what is appropriate economic behavior. Companies conform to pressure from the social context because it helps

them to gain legitimacy and other resources which help the company to survive (Deegan and Unerman, 2011).

Institutions are defined as governmental agencies, laws, courts, professions and interest groups (Oliver, 1991; Hatch and Cunliffe, 2006). Companies adopt technical, economic, social and political demands in order to gain efficiency and legitimacy. When a company gets organized after demands from the external context through different kinds of pressures, the company is being institutionalized (Hatch and Cunliffe, 2006). The pressure comes from external stakeholders such as peers, customers, regulatory agencies, the state, the professions, general social expectations and leading organizations (DiMaggio and Powell, 1983; Greenwood and Hinings, 1996). The praxis adopted by different companies tends to be similar to what the society or specific powerful organizations prefer (Deegan and Unerman, 2011).

### **2.5.1 Institutional pressure**

Institutional pressure emerges from important stakeholders and choices are influenced by internal and external norms, values and traditions. These different kinds of pressures make the companies pressured to take action and therefore institutional forces play a key role for companies to adopt new items (Tate, Ellram and Dooley, 2014). For companies to survive the hard business climate they have to adapt to the institutional pressures (Greenwood and Hinings, 1996).

Simpson (2012) argues that institutional pressure, which could be both legal and social, is the most efficient way to lead a company into changing their behavior. The resources a company has will often develop in line with the external pressure, for example after the market, the praxis in the industry the company operates in or according to peer practitioners. Regulatory pressure often clear states an acceptable behavior and has the power to penalize the companies if the praxis is not adopted correctly. The pressure from those stakeholders could lead to performance changes which may not always be that advantageous to the companies (Simpson, 2012).

One has to understand the institutional factors behind the accounting choices conducted by the companies (Tate, Ellram and Dooley, 2014). The institutional pressure is influencing the managers and companies choice of for example accounting methods (Cui and Jiang, 2012). Trombley (1989) finds out that an adoption choice of whether to adopt a new regulation in an early stage are related to company size and auditor preferences. When managers have problems to agree about a specific accounting choice they listen to other participants in the process of creating financial statements, for example the auditor.

### **2.5.2 Legitimacy**

Institutionalization is a process when something gets widely accepted and becomes both appropriate and necessary and thereafter it becomes something that is needed for companies



to gain legitimacy (Tolbert and Zucker, 1983). Legitimacy is defined as; “*A generalized perception or assumption that the actions of an entity are desirable, proper or appropriate within some socially constructed system of norms, values, beliefs and definitions*” (Scott, 2008). Meyer and Rowan (1977) argue that gaining legitimacy is important for a company. To keep the gained legitimacy, it is important that companies act proper and are suitable for the industry they operate in. Managers tend to imitate other companies’ behavior in their industry. They need a motivation why they take certain choices and they need to both establish and maintain the legitimacy to their external stakeholders (Salge, Kohli and Barret, 2015). Imitation is more common in uncertain environments since it is not possible to predict the outcome of an action (Lieberman and Asaba, 2006).

A lot of organizational structure occurs as reflections of rationalized institutional rules. In order to gain legitimacy, resources, stability and enhanced survival prospects companies implement institutional rules as myths. A formal organizational structure contributes with legitimacy by reflecting the myths in the institutionalized external environment. It is of importance to adjust a company to the institutionalized environment because there is a difference between formal structure in a company and how it is organized in practice (Meyer and Rowan, 1977). Formal structure could be as institutionalized as they work as myths, for example myths of professions, programs or methods. An accounting method does not always have to be effective, it just needs to gain the company legitimacy (Eriksson-Zetterquist, 2009). The companies develops homogenous formal structures since they aim to fulfill the same myth. It is important that all information used outward the company are institutionalized, for example an auditor’s report since it creates legitimacy to the external stakeholders (Eriksson-Zetterquist, 2009). Companies which implement organizational myths create legitimacy and are more likely to survive and be successful (Meyer and Rowan, 1977).

### **2.5.3 Isomorphism**

Isomorphism is according to DiMaggio and Powell (1983) the concept that best capture the process of homogenization. Isomorphism can be defined by; “*A constraining process that forces one unit in a population to resemble other units that face the same set of environmental conditions*” (DiMaggio and Powell, 1983). Isomorphism could be a kind of adoption of an institutional practice in a company (Deegan and Unerman, 2011). Institutional isomorphic change occurs through three mechanisms (DiMaggio and Powell, 1983).

*Coercive isomorphism* originates from political influences and legitimacy problems. It comes from both formal and informal pressure from other companies or organizations but also from cultural expectations from the society (DiMaggio and Powell, 1983). Pressures from regulations can make companies practice certain behaviors (Tate, Ellram and Dooley, 2014). The more dependent the company is of the stakeholder or their resources the more similar it will be to that stakeholder. The stakeholders are big influences when a company adopts a specific practice (Deegan and Unerman, 2011). *Mimetic isomorphism* arises from how praxis responses to uncertainty, as uncertainty forces imitation. One response to uncertainty is modeling where a company “borrows” some ideas from another company or organization that

are perceived as more successful (DiMaggio and Powell, 1983). A company seeks to imitate the institutional practices of other companies that have some kind of competitive advantage (Deegan and Unerman, 2011). *Normative isomorphism* is related to professionalism. Professions are affected of the same process as companies. Universities play an important role since they develop organizational norms among professionals. Students learn the same norms and then distribute them into a wide range of organization when they get employed (DiMaggio and Powell, 1983). Within the group, between the members, there will emerge informal rules when the group members put pressure on each other and also others outside of the group (Tate, Ellram and Dooley, 2014).

## **2.6 Summary of the theoretical framework**

To be able to answer our research question our analysis model will contribute with the three perspectives on accounting choices; practical handling, economic drivers and institutional forces. The economic drivers will be analyzed in accordance to Positive accounting theory and previous research regarding accounting choice. The core within this perspective is how manager's beliefs, desires, needs, preferences and self-interest will affect accounting choices. Furthermore, special characteristics of the company and the industry the company operates in could also affect accounting choices. Previous studies includes the following five drivers as drivers affecting accounting choices; *taxes, regulation, political costs, information production costs* and *management compensation plans*. Moreover, the driver regarding ownership structure could also have a large influence on accounting choice.

The practical handling of our analysis model includes how to depreciate current assets. Naturally, depreciation is an important accounting choice since it has a large impact on the financial statements. To increase the true and fair view of accounting on current assets, the new framework K3 requires component depreciations where significant components with different economic lives within an asset have to be depreciated separately. Finally, the third perspective concerning institutional forces consists of different external factors which will explain why companies make different choices. In order to gain legitimacy, companies tend to adjust to pressure in the external environment and therefore they might do similar choices and become more alike.

## 3. Method

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*The method chapter is designed to describe the research process of this study. The chapter will include how we have performed this study, from the beginning of deciding the subject until the end where we wrote the conclusion. Finally, the quality of our sources has been discussed.*

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### 3.1 Research process

The working process of this thesis started with choosing an area, financial accounting, and later on we decided to write about accounting choices within a Swedish context. One accounting choice is the one of component depreciations on current assets. This is also a new and important area, which had generated a large debate in Sweden as the new framework K3 is currently implemented. Therefore, accounting choices with focus on component depreciation became our field of investigation.

The information search started out with searching for academics articles and previous research related to accounting choices, depreciation and component depreciation. This search was made primarily in the databases Business Source Premier and Emerald Insight among others and we mainly used the key words accounting choice, depreciation, component depreciation, Positive accounting, Institutional theory and institutional forces. Thereafter, we found some articles written in the branch magazines Balans and Resultat as a supplement to conduct the Swedish context. Now the research design started to take form and the two theories were selected as they handled the accounting choice discussion as well as the external forces which could affect the companies into making certain choices. Then, articles were read about those theories as we wrote the second chapter about the theoretical framework. During this entire process of this thesis, the third chapter about the method was gradually written.

The empirical findings have been collected through interviews with companies in the real estate industry. The companies interviewed were founded through a database, namely Retriever Business, where one is able to find company facts as well as annual reports. On all interviews we have also received examples and documents of how they have done the component depreciations which also is included in the empirical findings. After the interviews, selected parts of the respondents' answers have been transcribed and the collected empirical findings have been analyzed and related to the theories in the theoretical chapter together with our analysis model. To accomplish this master thesis, the method part had to be completed almost last in the process.

### 3.2 Research approach

The research approach in this study has been performed under an interpretivist paradigm since the study aims to understand a social phenomenon in a specific context (Collis and Hussey, 2014). In this case, the study seeks to describe and understand how companies had made their

accounting choices and especially the choice regarding component depreciation on real estates. We chose to only focus on one specific current asset, explicitly real estates. This is one of the most affected assets of the new frameworks area of component depreciation, therefore it was very interesting to look deeper into. As we decided to only looking into real estates we also decided to only study real estate companies. We intended to focus only on real estates companies as they, more often than others, owns a lot of real estates. Therefore, we believed they had large drivers behind implementing component depreciation more extended than smaller companies only owning one real estate. Thus, we got more out of this study with larger real estates companies owning a lot of buildings than if we had interviewed smaller companies with only a few buildings.

The study was performed as a qualitative study, inspired by Bryman and Bell (2007), since the focus was how companies had made their accounting choices and how they had handled component depreciation for their real estates (Bryman and Bell, 2007). The methodology is a case study since the objective was to explore the phenomenon of component depreciation in order to gain in-depth knowledge of why these accounting choices had been made (Collis and Hussey, 2014; Yin, 2009). Our research question involves both how and why, as the aim of the thesis was to explain how and why a social phenomenon works and therefore the methodology is a case study (Yin, 2009). The purpose of our study was to perform a case study with a Swedish context of a few real estate companies using component depreciation. The aim was to provide a strong case of our certain phenomena in order to increase the understanding of the phenomena. Our case was how Swedish real estate companies had applied the framework K3 and how they had made the accounting choices concerning component depreciation. By closely looking at this case, the knowledge could potentially be generalized on other similar real estate companies choices. Case study was therefore an appropriate method for our study, since one is able to perform a generalization if the case is a well-formulated example of a larger phenomenon (Yin, 2009).

Our respondent companies were different; they could not be interchangeable with each other. The ownership structure is different, both private as well as municipal companies have been included in the study. Also the size differs between the included companies; both smaller and larger companies were chosen as well as companies owning different kind of real estates. We decided to have this mix of companies as well as different kinds of real estates in order to be able to capture a wider perspective of how companies had made their accounting choices. The case study has been conducted in the context of Swedish real estate companies applying the framework K3 and performing component depreciation on real estates. We have chosen to perform this study in Sweden because it was interesting as Sweden had a new framework, namely K3. The framework has a new area which has not been present in Swedish accounting before, called component depreciation. This was implemented on current assets with more than one substantial component. We decided to perform this thesis as a case study, since a case study offers a possibility to understand accounting in practice (Ryan, Scapens and Theobald, 2002).

### **3.3 Data collection**

As this is a qualitative study, we have performed qualitative interviews with seven real estate companies in the Gothenburg area. Interviews are one of the most important methods to collect qualitative data (Qu and Dumay, 2011). Therefore, interviews were our method for collecting our data to be able to write the empirical part of this thesis.

The data was primarily collected through interviews with respondents at real estates companies. Furthermore, we have received internal documents provided by the companies. The documents of examples of component depreciations we received from the respondents have helped us to verify the empirical data and have therefore been used as a complementary part in the data collection.

#### **3.3.1 Selection of companies**

To gather the data needed for this study, Swedish companies have been interviewed regarding their accounting choices and how they have handled the new area of component depreciation. The companies were selected from a number of criteria in order to include suitable companies. It was important that the companies were able to be a relevant case for the purpose of our study. Companies have been selected if they are:

- Swedish companies.
- Located in the area of Gothenburg.
- Non-listed companies.
- Companies which applies the K3 framework.
- Real estate companies, which owns real estates.

These criteria have been selected in order to get a Swedish context on the accounting choices. We decided to choose companies in the area of Gothenburg as this is the second largest city in Sweden where we were able to find sufficiently large companies which will use K3. The criterion regarding non-listed companies was self-explained as listed companies have to use another framework than K3, namely IFRS. Only real estate companies were included in this study as we needed companies which own a lot of real estates to get better responses. As mentioned above, we believed they had larger drivers to implement the component depreciation part more extended than smaller companies. We decided to have the criteria to narrow down the number of companies which might be of interest for us. When searching for suitable companies, which were matching the above mentioned criteria, we found 39 companies. After a thorough selection, seven companies with different ownership structures and different kinds of real estates were included in the case.

#### **3.3.2 Selection of respondents**

When choosing the respondents, it was of high importance that all the respondents in this study should be participating in the daily work within the accounting in the companies. The

respondents are mainly CFOs, but also one accountant and one controller which have been involved in the accounting choices process, have been interviewed. Therefore when we contacted the chosen companies we mainly contacted CFOs on all companies as they were the ones we primarily wanted to perform the interviews with. However in one case, we interviewed an accountant instead since she was the one most involved in the process of implementing component depreciations and in one case a controller together with the CFO was interviewed. For our study, we have not chosen to interview CEOs since they are typically not a part of the accounting part in the company and not all CEOs have a financial background.

### **3.3.3 Description of respondents**

A short description of the seven respondent companies, which were selected from the above criteria, and have been interviewed, is presented below. The interviewed companies are *AB Alebyggen*, *Bostads AB Poseidon*, *Familjebostäder i Göteborg AB*, *Higab AB*, *HSB Göteborg*, *Svenska Hus AB* and *Öckerö Bostads AB*.

*AB Alebyggen* is a municipal company, fully-owned by Ale Kommun. They have about 2200 apartments, a lot of independence houses as well as some industrial premises. We made our interview with the CFO of the company, Sven-Arne Rasmussen. We will further call this company *Alebyggen*.

*Bostads AB Poseidon* is a municipal company and a subsidiary company of Förvaltnings AB Framtiden, which is owned by Göteborgs Stad. *Bostads AB Poseidon* owns 26 603 apartments in the Gothenburg area and is therefore one of the largest real estate companies in Gothenburg. We interviewed Jessica Kruse, the CFO of *Bostads AB Poseidon*. We will further call this company *Poseidon*.

*Familjebostäder i Göteborg AB* is a municipal company and a subsidiary company of Förvaltnings AB Framtiden, which is owned by Göteborgs Stad. They own 430 real estates which contains 18 257 apartments, around the area of Gothenburg. We interviewed Charlott Bengtsson, an accountant responsible for their real estates and the practical implementation of component depreciation at *Familjebostäder i Göteborg AB*. We will further call this company *Familjebostäder*.

*Higab AB* is also a municipal company owned by Göteborgs Stad. They own real estates containing for example heritage buildings, football stadiums, industrial premises and theatres. We interviewed Fredrik Setterberg and he is the CFO of *Higab AB*. We will further call this company *Higab*.

*HSB Göteborg* is a cooperation and is therefore owned by its members and all profit is reinvested in the company. They own real estates which include apartments which contains residences. We interviewed Anders Westman, CFO and Rebecca X, the controller in the company *HSB Göteborg*. We will further call this company *HSB*.

*Svenska Hus AB* is a privately owned company and a subsidiary company of Gullringsbo-koncernen. They own both real estates containing apartments, around 40 %, as well as commercial real estates, around 60 % of all real estates. We made our interview with Måns Johannesson, he is the CFO of the company Svenska Hus AB. We will further call this company *Svenska Hus*.

*Öckerö Bostäder AB* is a municipal real estate company owned by Öckerö Kommun, in the archipelago of Gothenburg. They have apartments for renting, for example on Öckerö, Björkö and Hälsö as well as municipal real estates containing for example schools and pre-schools. We performed our interview with the CFO of the company, Hans Andreasson. We will further call this company *ÖBO*.

### **3.4 Interviews**

To be able to answer the research question of the study, we have been performing interviews. The interviews have been made with real estate companies which own real estates and have implemented component depreciations on those. We wanted to try to make an illustration of the phenomena and thereafter analyze with the theoretical chapter as a basis.

The preparations of the interviews started out with finding a time and place when the interviews could be held. About one hour per interview was planned, however some interviews lasted longer and some shorter. All interviews have been held in Swedish, as we believe the respondents are more confident with their native language. However, even though all interviews were held in Swedish and thereafter translated into English, we have not lost any substance when translating the interviews. We have also recorded all our interviews to be able to listen to them many times when transcribing and writing the empirical findings chapter. The reasons why we had performed interviews were to collect our empirical findings and qualitative interviews are one of the most important methods to collect qualitative data (Qu and Dumay, 2011). It was very important the interview questions were connected to our theories from the theoretical framework. The interview questions were, as mentioned above, based on the theories and previous research presented in the theoretical chapter, namely Positive accounting theory and Institutional theory. The interview questions are attached in Appendix 1. Questions 1 and 2 were general questions regarding the respondent and the interviewed company. Thereafter, question 3-11 were concerning the how part of our research question. Those questions will therefore help us answer the part of how the companies had made the accounting choices of component depreciations on their real estates. To be able to answer the why part of the research question, the theories Positive accounting theory and Institutional theory have been selected. As a result, the interview questions 12-17 were related to Positive accounting theory and questions 18-19 were related to Institutional theory. Beyond that, all interview questions had to be in line with the aim of the thesis and the research question. By connecting the theoretical framework to our empirical findings we were able to answer our research question later on. Also, qualitative interviews required an accurate plan and also preparation to be able to ask questions which were useful for our study. Therefore, as

we had written both the introduction chapter as well as the theoretical chapter we had knowledge within the subject and were thereafter able to ask appropriate and relevant interview questions (Qu and Dumay, 2011).

As mentioned above, preparation was important to get the most out of the interviews, however one cannot prepare the whole interviews. If structured interviews were used, one cannot get to know everything the respondent know or if using non-structured interviews, one could miss something important to ask (Patel and Davidson, 2011). Therefore, in this study semi-structure interviews have been performed as it also is the most common method to gather qualitative data. When using semi-structured interviews one will be able to identify hidden patterns of organizational behavior and the method is very flexible (Qu and Dumay, 2011). Therefore, as suggested by Widerberg (2002) we have used the interview guide as a facilitator during the interviews but we have not followed it literally. The interviews were held in a qualitative manner, as this is a qualitative study. Therefore, semi-structured interviews fit our research design well and we could ask questions not included in the interview guide in order to receive better information from the respondent (Patel and Davidson, 2011). Also, by performing qualitative interviews one were focused on the respondents answers, not ours, which is the focus in a qualitative study. More valuable information could be received by using this flexible interview structure (Bryman and Bell, 2007). Furthermore during the interviews, we have asked the questions as neutral as possible to avoid misunderstandings. We have performed face-to-face interviews as they increased the trustworthiness of our study. Face-to-face interviews were also to prefer as we were able to read the respondents facial expressions and thereafter make assumptions regarding the information the respondent told us (Collis and Hussey, 2014).

### **3.4.1 Interview guide**

The interview questions have been designed as easy to understand and the intention was not to mislead the respondent to answer the wrong thing. The same interview guide with questions was used on all interviews, but as we performed semi-structured interviews, some follow-up questions became different according to the respondents' answers to the permanent questions (Bryman and Bell, 2007). We were able to use the same interview questions on all respondents as they had similar positions in the companies. The interview questions are attached in Appendix 1.

We sent out the questions that we were going to ask to the respondents in advance. Then, the respondents could be able to prepare themselves and we could receive more appropriate answers. However, when the questions were sent out in advance one could miss out on the reaction of the respondent, but the answers were supposedly more appropriate when the respondent have been able to prepare themselves and collect all information they need to be able to answer our questions (Bryman and Bell, 2007). Moreover, we used both open and closed questions. To have a mix of these kind of questions, one could receive more information as open questions are freer for the respondent to talk by themselves and more unchained (Collis and Hussey, 2014). After we had had the seven interviews we felt it was



enough, these seven interviews gave us a satisfaction and no more interviews would have given us more information.

### **3.4.2 Companies internal documents**

Together with the interviews we have also received internal documents and examples from the companies included in this study. The documents have contained calculations as well as examples regarding how and which components they had chosen to divide their real estates into. Furthermore, depreciation periods of the components have been stated in the documents. We have therefore used these documents as a complement to the interview data, as a complementing source, in order to capture how the companies actually had handled the implementation of component depreciation in practice. These documents have increased our understanding of the practical implementation of component depreciation and drivers behind these choices.

### **3.4.3 Data processing**

Once the interviews were completed, the information was processed. We have transcribed most parts of the interviews which were considered to be most relevant for our research question. The transcription part were the first stage before the analyzing process and it was in this stage the data was processed, selected, simplified, summarized and reorganized (Collis and Hussey, 2014). It was through that process, the data became information and transformed to empirical findings as we interpreted the information (Holme and Solvang, 1997).

As the interviews have been held in Swedish, we have performed the transcription in Swedish as well. However, when the transcription part was done we started to translate those parts we wanted to include in our empirical chapter to English. When transcribing, we listened to the recordings over and over to capture even small details. Thereafter, when all transcriptions of all interviews had been done, we started to put everything together under headings for the empirical findings chapter. We also sent out a summary of the transcriptions for the respondents to comment upon and confirm that we had perceived the answers correctly.

We wrote the empirical part with the interview questions as well as our research question in mind, to be able to capture what was important from the interviews. We divided the text after content and not after each company by themselves as we believed it would be easier to see the entirety of the substance in the chapter then. On all interviews we also had received internal documents, examples and calculations of how the companies had done their component depreciations. We transferred this data into tables to include in the empirical chapter and in the appendix. The table was included in order to illustrate for the reader how the companies had handled the implementation in practice.

### **3.4.4 Data analyzing**

Once the empirical findings had been written, we started to write the analysis chapter. In the analysis we started to connect the empirical findings to the theories, Positive accounting theory and Institutional theory as well as additional previous research from the theoretical

framework. In order to accomplish a well-written analysis, our analysis model came well in handed. Together with the first perspective, practical handling, we were able to draw conclusions about how those seven companies we have interviewed had implemented component depreciations. We also related what was said in the interviews to what was done in the companies' internal document, examples and calculations which we had received from the respondents. As a result, the first part of our research questions about how the companies had done, have been presented. The second and third perspective regarding economic drivers and institutional forces were analyzed in the analysis chapter together with the previous research and the empirical data. To be able to answer the why part of our research question those perspectives were appropriate to use. Particularly we looked deeper into what drivers which have been affecting managers' choice. We discussed that special characteristics of the company and the industry the company operates in could also affect accounting choice. When analyzing the institutional forces we recognized SABO as well as auditors' preferences to be large forces when companies became institutionalized. Furthermore we analyzed institutional forces and in order to gain legitimacy, companies tend to adjust to pressure in the external environment and therefore they might make similar choices and become more alike.

The analysis part has been made based on our research question to make it easier to answer the research question. Moreover, almost the same headings have been used in the empirical part and the analysis part to make it easier to answer the research question. When analyzing we started in the interview questions to find a pattern between the companies in how they had implemented component depreciation on their real estates and what drivers had affected them into making those choices.

### **3.5 Quality of the sources**

The data was collected through interviews with respondents at seven companies and internal documents were provided by the companies. The quality of academic research is often evaluated by using two dimensions, namely reliability and validity (Patel and Davidson, 2011).

#### **3.5.1 Reliability**

Reliability means that a study later can be repeated and the result will be the same. To record the interviews, as well as performing follow-up interviews will increase the reliability. However, reliability is not as valuable within a qualitative study as this is, as it is in a quantitative study (Bryman and Bell, 2007). Experiences and knowledge of both the interviewers and the respondents could affect the result of the study and had to be taken into consideration even if new experiences may not mean lower reliability (Collis and Hussey, 2014; Patel and Davidson, 2011). The internal documents which have been provided from the companies have also assisted into increasing the reliability of the study.

When performing a qualitative study, the right case will contribute to increased reliability. To increase reliability, the constellation of companies and respondents was important to have. In

our study, those companies included as well as the respondents in those companies were the right case for us and for our study in order to be able to answer our research question in a reliable way. The right case is when the choice of companies and respondents has been made carefully in order to increase reliability of the study (Collis and Hussey, 2014). Also how we approach to our respondents in the interviews will contribute to increase reliability, as we did not wanted them to talk generally, we wanted them to talk about how they did in their own company and what choices they had done. Therefore, the right case in our case is the case study of component depreciation in Swedish real estate companies.

### **3.5.2 Validity**

The notion validity means that the study should measure and include what it ought to measure and include. The focus in this study lies on the accounting choices in companies with a focus on component depreciations, to measure what is ought to be measured. Therefore, the interview questions have been based on the research question to be in line with the aim of the thesis (Bryman and Bell, 2007). Often, one will receive high validity if qualitative data is collected. In order to get the most out of the interviews, semi-structured interviews with both open and closed questions have been used (Collis and Hussey, 2014).

To perform a study with high validity, it is important to perform a believable interpretation of the respondents' answers as well as the internal documents we received. To do this, the transcription part was important to perform accurate to not lose the meaning of the answers. It was also important for high validity to not involve our own thoughts in the empirical part. One could, to increase validity, also send out a summary of the transcriptions for the respondent to comment upon which will increase the validity as they will confirm that we have perceived the answers correctly. Therefore, this was performed in our case (Patel and Davidson, 2011).

## 4. Empirical findings

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*The chapter containing empirical findings will include the result of what we have collected from our qualitative interviews with seven Swedish real estate companies. The answers have been divided into categories in line with the main interview questions. Therefore, the companies' answers will be easier to compare. This chapter is supposed to be a basis for our analysis chapter.*

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### 4.1 Practical handling

First out in this chapter is the practical handling of component depreciation in the seven companies included in this study. Thereafter, members in the companies which had been included in the implementation process were being evaluated as well as which components the companies had chosen to divide their real estates into. That part is in line with the research question and will help us answer it. In this chapter the impact on the financial statements as well as capitalization of maintenance is also included to demonstrate what impact the accounting choice of component depreciations had on the companies' financial situations. After that part containing more of the practical handling, the chapter is moving on to the next part in the research question which is why the companies had made the accounting choices they had made and also what influenced them into doing those choices.

As mentioned in earlier chapters, component depreciation had to be implemented in the financial statements from the annual report 2014-12-31, and forward. However, the work with the actual implementation in the real estate companies started earlier. In some companies already during the year 2012, but most companies started in 2013. The practical handling in the companies we have studied had been slightly different.

*Alebyggen* started with a theoretical reasoning and together with a consultant firm they tried to figure out a way to handle this new regulation. Early in the process the administrators were involved together with the administrative manager since the technical process was a large part of the component method. The technical perspective needed to be in line with the financial perspective in order to optimize the implementation of component depreciation. The optimal case would have been to physically examine all the buildings and make individual judgments for each building, but that were not possible. Therefore, in practice they started to look at some neighborhoods which they broke down into individual buildings. Thereafter they calculated a weighted depreciation for each real estate. *Alebyggen* also owns a shopping mall, where they hired an external appraiser to do the implementation of component depreciation since the mall involved more specific components.

Both *Familjebostäder* and *Poseidon* are subsidiaries of the parent company Förvaltnings AB Framtiden and they had together considered and discussed how to implement component depreciation on their real estates. *Poseidon* started to look at new production since it was

easier when you knew exactly what each component was worth. Then they developed templates that also were used on the older real estates. For example, if a building was recently produced, each component represented a percentage of the buildings total value. These percentages were then used to calculate backwards in order to get the values of the components for older real estates. Each district have been involved in the process to complement with which improvements and replacements that had been made on their real estates earlier. The depreciation periods of the components had been decided together with the administrators. All the work regarding the implementation had been conducted within the company, as they had appropriate experience and knowledge. The collaboration between the financial department and the administrators have been extended during this work. In order to get a smooth transition to component depreciation and to create comparative numbers for 2013, *Poseidon* had a “shadow-bookkeeping”, also explained as parallel-books, during this year to simplify the closing of the annual report. *Familjebostäder* had a similar procedure when they examined their real estates. The consideration between the financial department and the project managers were important to include different perspectives. *Familjebostäder* argued that the project managers were the one most suitable for deciding the depreciation periods since they knew when a component usually are replaced and they also have a great knowledge of their real estates. Thereafter the financial perspective had to be considered as well. It was also appropriate to include how these projects had been accounted for historically which in *Familjebostäder* resulted in that a large part were capitalized into foundation.

In *Higab*, the controller together with the maintenance-planner made the initial classification of components in their real estates. Also the CFO was involved in that process. It was hard to find a template that could be used, since *Higab* owns such different types of buildings. For example they owns; heritage buildings, football stadiums, industrial premises and theatres. Instead, all the real estates had to be examined individually, even on a building-level. The department of maintenance was involved in this process in order to include another aspect of when a specific component needed to be replaced. *Higab* needed this aspect to be able to determine suitable depreciation periods for each component. The project managers added information about which components that had been replaced, which material that had been used and then the depreciation periods were decided. These aspects were needed for the components to correspond to the maintenance-plans of their real estates.

In practice, *Svenska Hus* initially started to form a group consisting of the CFO and a few administrators in order to discuss and deliberate around which components that were essential in their real estates. Also the CEO was involved since these specific accounting choices had a large impact on the financial statements. Thereafter, they connected them to the existing maintenance-plans which reached over three to five years. Every building had been inspected by an administrator who allocated the book value to the existing components. As a help they had a list of investments made the last ten years in each building. The aim was that each component should get the value it should have had if the investment were made today. Thereafter, estimations of the remaining economic lives of the components were made and the residual value was allocated to the foundation. After the administrators had made their process, the financial department analyzed it to make sure it was reasonable. Thus, the

administrators and the administrative manager had been involved to include another view than the pure financial aspect.

*HSBs* controller Rebecca X, started the work with the implementation of component depreciation together with the manager of their investment properties. Already from the start the administrators were involved as well. They also contacted *HSB* in both Stockholm and Malmö, in order to implement a similar approach to component depreciation. In practice, all buildings have been inspected individually in order to find out, for example, if the windows had to be replaced within the following 30 years. In the discussion with *HSB* in both Stockholm and Malmö, both those companies were arguing that it should be enough to collect information five years back and five years forward in the maintenance-plans. However, *HSB* Göteborg decided to go as far back as possible in their business system. This work had foremost been conducted by the administrators and the manager of investment properties in-house.

*ÖBO* owns three kinds of real estates; residential properties, municipal real estates and industrial premises. Therefore they started the implementation process with hiring a consultant to perform an appraisalment of one real estate for each group of real estates. These templates were then used when examining each real estate individually. Afterwards the CFO, the project manager, the administrative manager and a HVAC-engineer made an evaluation of how much each real estate differed from these different types of real estates.

These seven companies included in this study had made the initial implementation of component depreciation in their financial statements. However, to implement the new way of thinking in the rest of the company still exists. A few companies had started to educate their personnel in how to, for example, make replacements of components. *Poseidon* has had lectures for their administrators in order to create an understanding for how they should work with component depreciation according to their internal guidelines. In general for all companies included in this study the financial departments had to introduce the new approach into the rest of the company and especially the administrators' needs to be well-informed to simplify the work for the accountants the following years.

All companies have had a rather similar implementation process of component depreciation on their real estates. They have all started looking into the theoretical reasoning and thereafter they have had discussions in order to select suitable components and to be able to establish depreciation periods depending on the material used on the components.

#### **4.1.1 Employees involved in the process**

As mentioned above, not only the financial departments, containing of CFOs and accountants among others, have been involved in the process to implement component depreciation on the companies' real estates. To involve more than the financial department in the implementation process, the companies were able to include more than the financial perspective on component depreciation. Therefore, the administrators have also been involved during the

whole process as they are more familiar with the companies' real estates. Since they work with the real estates in practice, they could present a more technical perspective on how one could implement component depreciation in practice. Naturally, the auditors have also been involved from the beginning in all seven companies. To implement a new accounting choice, from a new framework without any praxis, the companies needed the assistance from their auditors to be able to keep the true and fair view of the accounting. Component depreciation is a large accounting choice and therefore the CEOs have been involved in some cases, for example in *Svenska Hus*.

#### **4.1.2 Accounting choices of component depreciations**

When implementing a new framework with new areas, like component depreciations on current assets, there will emerge new accounting choices the companies had to consider before implementing the new method. The accounting choices regarding component depreciation are primarily; how many components a real estate should be divided into and which depreciation periods the components should have. The choices of the components used in the companies are attached in Appendix 2.

*Alebyggen* had in the initial phase chosen 13 components. Before K3, they used the same depreciation period on one residential area which was considered as one investment. Now every individual building had to be divided into components. Every building has been allocating their part of the book value according to the percentage of square meter in order to receive the initial component values. *Familjebostäder* and *Poseidon* had decided to divide their real estates into 16 components initially exclusive land improvements and permanent equipment in buildings. Shortly, they had used the same components in the whole group in order to create, primarily comparability. These components were only used for residential properties. For industrial premises only five components were used while carparks only have three components. Depending on each specific building one uses the components that were appropriate. The depreciation period of each component was depended on the material used to build each component. The material used was also an aspect for *Alebyggen* to determine the depreciation periods. In *Poseidon* one component could have different depreciation period within an interval which was consistent with their maintenance-plans.

*Svenska Hus* focused a lot on how this new method of component depreciation could benefit them in order to choose their components. They ended up with initially ten components that later on increased to eleven. To select appropriate components was a process where *Svenska Hus* chose to be restrictive in the beginning. Though, over time when parts had to be disposed a larger number of components could lead to an easier implementation. In order to allocate the book value of the real estates into suitable components, they started with the specifics of each building for example the tenant adjustments or if the building contained elevators.

The guidelines from SABO have given the opportunity to gather components with the same depreciation periods together with each other, in order to have as few components as possible. However, as they argued in *Svenska Hus*, in the long run it may be easier to have more

components already from the start. *Svenska Hus* claimed that difficulties could arise when you for example, needed to replace the windows. If these are grouped together with the frontage, it may be hard to decide how much should be disposed. It may also be hard to decide how much already realized depreciation should be referred to the windows. Therefore the number of components could not be too few. It may be easier in the initial phase but in the long run a large number of components might be more appropriate and also give an easier extended handling. This reasoning was not only used in *Svenska Hus*, both *ÖBO* and *Alebyggen* among others shared the same thoughts. The number of components could increase by time, for example in *Svenska Hus*, kitchen and bathroom are for now included in the same component, namely interior surface. However, it may be possible that these could be divided into two new separate components in the future.

In *Higab*, the link between the depreciation periods of the components and their maintenance-plans were of high importance. Eight components were selected but in some cases a few more components may be added such as an elevator or a technical installation if the building contains it. Depending on the material, the depreciation periods for the components were decided. Thus the aim was to be synced with the maintenance-plans. *Higab* is a group consisting of a parent company and three subsidiaries, which also are real estate companies. Therefore, they developed a guideline with a minimum number of components that had to be used for all companies within the group. The planned maintenance was also used when deciding the number of components in *ÖBO* and *HSB*, among others. *ÖBO* have chosen 15 components for their real estates. The ordinary maintenance was used in order to select suitable components which were essential for their real estates. The components chosen were the ones commonly used in projects within the company. Since *ÖBO* mainly owns three different types of real estates; residential properties, municipal real estates and industrial premises they had to manage those three differently. Consequently they needed to use a simplification in order to get a reasonable workload. In order to do that, they made an example for each type of real estate to use as a template when examine all the real estates.

The maintenance-plans were used as a base for calculating and deciding upon the components depreciation periods also in *HSB*. *HSB* decided to use eight components in order to not get too detailed. The different components needed to be essential so that they can create a more true accounting, otherwise it might just lead to heavier administration. A lot of discussion in *HSB*, as well as in other companies, was regarding the question of how many years the foundation could be depreciated for and how much one could allocate to the foundation. The final choice became 120 years in *HSB* but they could also have chosen to have a longer depreciation period. Because, a foundation may in many cases last for hundreds of years and one will not tear it down even though it is fully depreciated.

Finally, all our observed companies had chosen the components they consider as essential to their specific real estates. The numbers of components have been between 8-16, depending on if land and land improvements are considered as components. One need to understand what is included in each component to be able to see the entire picture. *Higab*, *HSB* and *Svenska Hus* have examined all their real estate individually while *Alebyggen*, *ÖBO*, *Poseidon* and



*Familjebostäder* have used templates to a larger extent. This also depended on the kind of real estates they have, for *Higab* and *Svenska Hus*, who does not only own residential properties, it was harder to develop templates since their real estates are more individually adapted to the business contained within these buildings. Moreover, for example *Poseidon* which is a large company, have too many real estates to be able to perform an individual examination of all real estates.

<b>Alebyggen</b>	13
<b>Familjebostäder and Poseidon</b>	16
<b>Higab</b>	8
<b>HSB</b>	8
<b>Svenska Hus</b>	11
<b>ÖBO</b>	15

*Table 1: Number of components*

#### **4.1.3 Impact on financial statements**

All companies had by implementing component depreciation into their financial statements received an effect on their profit. They received larger depreciations on their real estates than before and therefore the profit decreased in the companies in the year 2014, in comparison to 2013. For example in *Alebyggen*, before the implementation of K3 and the component depreciation, they had 2 % in depreciation on their real estate values and now they have 2,06 %. That is a weighted average where some real estates are around 3 % and some are around 1 %. It is not a significant change, it does only represent a smaller amount and therefore the effect on their profit is rather small, according to *Alebyggen*. This could be compared with *HSB* and *Svenska Hus* which got a larger effect on their profits as their depreciations now have increased from 1 % to 2 % of their real estates values.

#### **4.1.4 Capitalization of maintenance**

A purpose with K3 was to capitalize more maintenance costs and therefore the companies will keep receiving larger depreciations as these maintenance costs will be capitalized and later on depreciated. All companies' balance sheets will become larger in the future, since they will keep capitalizing the maintenance costs which previously have been expensed. Therefore, all balance sheets will become expanded over the years. Together with larger balance sheets, the more a company tends to capitalize the more impairments will probably emerge. Once a component should be replaced, one has to dispose the values when investing in the new components. For example, *HSB* does not believe that when a frontage is done depreciated, it will be time to invest in a new one. Therefore, the depreciations may not always match the

actual wear and tear of the components. Then the eliminations will be larger as you have to dispose to be able to invest in a new frontage. All companies interviewed have started to capitalize more than they used to do, however *Svenska Hus* has as mission to invest in real estates containing refining possibilities. Therefore, they have been capitalizing a lot already before the implementation of K3 and it will not affect them as much as the other companies. In difference to *Svenska Hus*, *HSB* was more restrictive to capitalize investments before the implementation of K3. Therefore, the difference became larger for *HSB*.

There are in some cases hard knowing what should be referred to as maintenance costs and what should be repair costs. Therefore, some companies have certain criteria for which investments should be capitalized and which should be expensed. For example, *Higab* have three minimum requirements for which components should be classified as maintenance costs and then capitalized. Those requirements are; at least three years economic life, minimum 25 % of the component has to be replaced and the total cost of the investment has to be at least 250 000 SEK. However in some cases *Higab* will make exceptions and perform individual judgments for some investments. *Higab* does not want residual values and if a component ought to be replaced, they will dispose the residual values. Moreover, *Familjebostäder* and *Poseidon* also have a minimum requirement that at least 25 % of a component has to be replaced to capitalize the investment.

## **4.2 Drivers of accounting choices**

The companies in this study had done their accounting choices depending on certain drivers which have influenced their choices. The choice regarding component depreciation has especially been made in line with the maintenance-plans in the companies. It is of importance to select components which are consistent with the existing maintenance-plans and that these components easily could be disposed when replacing the component. When implementing component depreciation on real estates which is in line with the company's maintenance plans, it will be easier to replace and dispose components in the future. The companies in this study have made their own approach, depending on the characteristics of their real estate and their own specific situation. The choice of component depreciations have been made by the CFOs and the accountants, with the financial perspective, together with the administrators which have more of a technical perspective. Therefore all companies in this study have had the financial department working together with the administrators to try to manage the new area within accounting choices. For example, *HSB* said in the interview that they have frontage and windows as one component instead of two since they always replaces the frontage and windows at the same time. They do not put up a scaffold and only replace the windows, one always replace the frontage at the same time since it is very expensive to put up the scaffolds.

Regarding the accounting choices and the choice of component depreciations, the CFOs were responsible in the end. This was the case for all seven companies included in this study. However, companies which are subsidiaries are sometimes more or less regulated by their

parent company. For example, both *Familjebostäder* and *Poseidon* are regulated by Förvaltnings AB Framtiden and they have to agree concerning larger accounting choices. Likewise, *Svenska Hus* has a parent company called Gullringsbo-koncernen, however *Svenska Hus* are more independent from their parent company than *Familjebostäder* and *Poseidon*. The municipal-owned companies in this study; *Alebyggen*, *Familjebostäder*, *Higab*, *Poseidon* and *ÖBO*, are not at all influenced by the municipality of which they are owned. All these five companies are all independent even though they are owned by three different municipalities.

The auditors have had a large influence in the accounting choice, especially regarding the implementation of component depreciation. However, they have not in any company made any decisions, they have had more of supporting role for the companies. As *Alebyggen* said; they do not want the auditors to criticize how they implemented it later on. Furthermore, as there was no praxis to follow, they needed the opinion of the auditors to be able to implement it correctly from the start. Especially in the case regarding component depreciations, when there currently do not exist praxis in Sweden, the opinion from the auditors is crucial according to the companies in this study. For example, *Higab* mentioned the close collaboration with their auditors. They believed one of the most important drivers regarding which accounting choices to made was to receive an unmodified auditor's report. It is despite of all, the auditors which approve the final financial statements.

Some existing guidelines, recommended to implement only a few components. However, *Alebyggen*, *Svenska Hus* and *ÖBO* among others, thought that was not the right way to go as it may be harder to replace and dispose components later on if one have gathered many components together as one. They believed it would be easier in the future not to have too few components in the initial phase. Therefore, the companies interviewed had selected 8-16 components to start with. However, for example *Svenska Hus* believes they may add even more components after the initial phase, when they start to work with it in practice. To group components together were suitable if they are alike, with the same depreciation period and if you will replace them at the same time. As for example already mentioned above, the example of *HSB* with the windows and frontage. That is a good example of when it is suitable to consolidate two components into one. Furthermore, *HSB* thought it was important not to have too many components as well, as it could create a larger workload. However, they did not want to have too few as it would be hard to replace and dispose later on.

CFOs make accounting choices depending on what they think is relevant to include in the books. Since the framework K3 is principle-based the companies have more freedom of act than if one were to use a rule-based framework. For example, both *Svenska Hus* and *ÖBO*, adjusted the depreciation periods in order for it to become both more relevant as well as more reasonable. Moreover, *Alebyggen* and *HSB* wanted it to be relevant and both these companies mentioned the example of an old building; no one will tear down a 50 year old building, even though companies have used 50 years as depreciation periods for buildings. Therefore 50 years as a depreciation period is neither relevant nor reliable. Consequently, it will become more reliable now when companies can increase their depreciation periods. For example, *HSB* will now have 120 years on the foundation instead of 50 years.

All companies had decided which accounting choices to implement depending on them wanting to increase the true and fair view in their accounting. To attain this, they followed recommendations and praxis. For example, the companies have mentioned the regulations ABL, Aktieföreläggelsen, and ÅRL, Årsredovisningslagen, as well as other recommendations from BFN, SABO, FAR and Fastighetsägarna. Managers' self-interest in the companies were mostly driven by true and fair view, to make the accounting the best reflection of reality as possible. However, *HSB* did not believe there existed many choices in today's accounting even though the framework is principle-based. There exists too many recommendations companies have to follow and they believe it became the same for the area regarding component depreciation.

### 4.3 The impact of institutional forces

At the time for implementing component depreciation in Sweden, K3 was a new framework and therefore there were no praxis to follow. Consequently, most companies interviewed for this study have collected information from a guideline from SABO, Sveriges Allmännyttiga Bostadsföretag. SABO presented their guideline about component depreciation for their members in May 2013 (SABO, 2013). Especially the companies which own residential properties, such as *Alebyggen*, *HSB* and *ÖBO* have been taking guidance from SABO and have implemented component depreciation consistent with their guidelines. Neither *Higab* nor *Svenska Hus*, which are companies with mostly other real estates than residential properties, did not believe SABO's guidelines were as helpful. *Familjebostäder* and *Poseidon* worked together with Förvaltnings AB Framtiden, their parent company, and also with their other subsidiary Bostadsbolaget. Neither *Familjebostäder* nor *Poseidon*, have been looking that much into the guidelines of SABO, as the other companies we have interviewed. When SABO presented their guideline, the group was already done and therefore they did not use SABO as much as the other companies we have interviewed. However, *Poseidon* thought it was favorable to be an early adopter since they could affect and navigate the implementation process in the industry.

Other than SABO, both *Alebyggen* and *Svenska Hus* also followed the recommendations from FAR, Föreningen Auktoriserade Revisorer. *Svenska Hus* thought FAR had a decent recommendation as it was more aligned with other real estates than residential properties, which was more helpful as they have a lot industrial premises. Also the magazine *Balans* had written some articles concerning component depreciation which was helpful when implementing it for *Alebyggen*. *ÖBO* considered Fastighetsägarnas guidelines, and both *Alebyggen* and *ÖBO* glanced at other companies which was early in their implementation of component depreciation, mostly to be inspired.

All companies have been taking guidance from their auditing firms and all companies have had a close collaboration with their auditors as mentioned above. Most companies have been on lectures the auditing firms have held to learn more about component depreciation and to

see some examples of how to implement it. The auditors' have in all companies had a supporting role when they implemented component depreciation on their real estate. Furthermore, they have consequently been a large institutional force and they have influenced the companies a lot.

	<b>SABO</b>	<b>FAR</b>	<b>Fastighetsägarna</b>
<b>Alebyggen</b>	X	X	
<b>Familjebostäder and Poseidon</b>	X		
<b>Higab</b>	X		
<b>HSB</b>	X		
<b>Svenska Hus</b>	X	X	
<b>ÖBO</b>	X	X	X

*Table 2: Applied guidelines*

## 5. Analysis

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*The analysis chapter includes the analysis of the empirical findings in line with the three perspectives from our analysis model, which are based on theories from the theoretical chapter.*

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### 5.1 Drivers of accounting choices

In theory, there are different economic drivers which influence managers' choice of deciding which accounting methods to use in their company. Those drivers are; *taxes, regulation, political costs, information production costs and management bonus plans* (Watts and Zimmerman, 1978). Other drivers influencing managers' accounting choices are according to Hagerman and Zmijewski (1979); *size, the level of risk, capital intensity, competition and incentive plans*. Another driver is the ownership structure, which was discussed in previous research by Dhaliwal, Salamon and Smith (1982). One of the perspectives from the analysis model, namely economic drivers will be analyzed here.

According to the collected empirical findings, neither of those drivers above were affecting the respondents in that extent in practice. The drivers which were influencing the companies included in this study were mainly; available frameworks, existing guidelines and auditor's preferences. All respondents believed that the guidelines were what influenced them the most to make accounting choices. Nevertheless, one can assume another kind of companies may have been used when the drivers in previous research were selected. The companies included in our study are non-listed and therefore not a subject for political costs in the same extent as listed companies. In the case concerning component depreciation, the maintenance plans in the companies were important to consider as well. The companies consistently believed it would be easier to dispose and replace components later on if they were in line with the maintenance plans in the first place. That is consistent with the debate hold by Stárová and Cermáková (2010). They argued that the depreciation periods of the components needed to correspond to the actual wear and tear of the asset.

All companies included in this study had been working with the implementation of component depreciation for over a year. The seven companies all argue and believed it were important to implement it correctly. Furthermore, depreciation is considered to be one of the most important accounting choices, not only according to the interviewed companies, also according to Filatov, Rudykh and Kiryukhin (2014). Therefore, one can understand why the companies have made this exhaustive work with the implementation of component depreciations on their real estates. Moreover, as the uncertainty regarding the implementation was high, companies had to work with the implementation longer to be able to implement it correctly. All companies included in this study wanted to increase the true and fair view for the accounting concerning their real estates and therefore one can understand why the implementation process was extended.

The guideline from SABO also includes that one is able to group components together if they are alike. For example, *HSB* always replace the windows at the same time as they replace the frontage and therefore they have these components together as one. This is line with the previous research from Saliers (1937), which claims one should group the components together into logical groups. Moreover, both SABO as well as Saliers (1937) believed one should only group components together if they have the same purposes, economic life and functions. One could thereafter depreciate the assets in the group in an identical way according to Saliers (1937). This was exactly what the companies in this study had done. However, *Svenska Hus* among others believed one had to be careful to not gather too many components together as it may be hard to replace and dispose the residual values in the future. This has affected the respondents when choosing their components. All respondents also agreed that some kind of generalization needed to be made in order to get a reasonable workload.

Both in theory as well in practice, it is hard to know if repairs and maintenance should be capitalized or expensed (Reynolds, 1961). This is also a heavily debated question among the respondents. For example *Svenska Hus* capitalized almost the same amount now as they did before the implementation of K3. However, the other six companies capitalized more now than before. To capitalize more will increase the true and fair view and that is in line with Hellman, Nordlund and Pramhäll (2011). According to the seven companies in our study, their main driver for what was influencing them was existing regulations and to increase the true and fair view of their accounting. Also, the companies believed they had increased the true and fair view by capitalizing more investments in collaboration with applying guidelines from SABO among others. Therefore, according to Hagerman and Zmijewski (1979), one could assume managers used different accounting choices to achieve their particular objectives and in our study most of the companies had used component depreciation to increase the true and fair view of their accounting. However, even though the respondents wanted to increase the true and fair view, all companies had to use templates to some extent to get a reasonable workload. It was not possible to include every detail, it had to be reasonable. This view had influenced the choices made in these companies regarding component depreciation since the process needed to be reasonable comparing to the outcome.

### **5.1.1 Differences in accounting choices**

One of the largest question in this study was why managers make the choices they do. All final choices had been made in the financial departments even though the administrators had been involved in the process of choosing components and deciding their depreciation periods. According to Kabir (2010) one could explain it by understanding the mental processes or beliefs of the managers. Not every human being will make the same choices even if they face a similar situation, like the implementation of component depreciations. This is consistent with the companies included in this study. All seven companies faced the same implementation and even though most companies we have interviewed owns residential properties they have not done the accounting choices exactly the same way. However, it is

also possible for two different persons to make the same choice in different situations (Kabir, 2010). For example in *HSB* and in *Svenska Hus*, they had made similar accounting choices of which components to use on their real estates. They had done this even though they do not have the same types of buildings, since *HSB* almost only owns residential properties and *Svenska Hus* mainly owns commercial real estates.

Ryan, Scapens and Theobald (2002) states that managers' actions are based on their desires, needs or preferences and their choices are influenced by their view of the world. Therefore, one can understand why managers in the seven companies had some differences in their accounting choices. Not only because of their differences in preferences, also depending on variances in their self-interests. Since there were different types of companies included in this study, it was obvious that they had made different accounting choices which are consistent with Watts and Zimmerman (1978). Watts and Zimmerman (1978) implied that the accounting methods used in a company some way was related to the special characteristics of the company or the industry the company operates in (Dhaliwal, Salamon and Smith, 1982). One can conclude, since the companies in this study operates in the same industry however owns different types of real estates as well have different ownership structure, their choices were in some ways different. According to Reynolds (1961), no depreciation method is appropriate for all assets and therefore the same component depreciation could not suit all buildings. Therefore, no companies in this study had made exactly the same component depreciations and that is in line with Reynolds (1961).

## **5.2 The impact of institutional forces**

Since K3 is a new framework in Sweden there do not exist any praxis in the industry. Therefore these companies have been influenced by other forces in the external environment to be able to implement component depreciations on their real estates. In this section, the perspective concerning institutional forces will be analyzed. According to the collected empirical data the companies had made similar choices with just small differences depending, foremost on their differences in types of real estates and the number of real estates they owned. Institutional forces affected the companies to become more homogenous by changing their behavior to pressures from the external environment (DiMaggio and Powell, 1983; Greenwood and Hinings, 1996; Phillips, Lawrence and Hardy, 2004). When companies interact and accept the same definition of reality, institutionalization emerges (Phillips, Lawrence and Hardy, 2004). Thus, the companies included in this study had been institutionalized since they had made similar choices in order to capture a comparable implementation of component depreciation.

According to Oliver (1991); Hatch and Cunliffe (2006) institutional influences in the society could be governmental agencies, laws, courts, professions and interest groups. The largest influence has been the guidelines from SABO since it had been used in all companies included in this study. Also the guidelines from FAR and Fastighetsägarna had been used in a few cases but not to the same extent. When analyzing the practical calculations of the studied



companies it was clear that a few of them had used similar components and depreciation periods like the examples presented in SABOs guidelines. As an observer it was clear that the guideline had made a large impact on the practical handling of component depreciation. This could be explained by the large confidence and respect SABO has from its members within the real estate industry. If your company follows SABOs guidelines it will gain legitimacy from external stakeholders.

Another factor that had a large impact was the auditor's point of view. They are a large institutional force since all companies need unmodified auditor's reports to gain legitimacy from external stakeholders. According to Trombley (1989) an adoption choice of whether to adopt a new regulation in an early stage are related to company size and auditor preferences. When managers had problems agreeing about a specific accounting choice they listened to other participants, for example the auditors. The guidelines had been limited since component depreciation has not been used in Swedish accounting earlier. Therefore the auditor's preferences have been of high importance since there have not been anywhere else to seek guidance. It is necessary to receive an unmodified auditor's report to be able to be a going concern and therefore the auditors have had a large impact. The auditors' needed to accept the accounting for the component depreciations. In our empirical findings it is stated that the auditors had not provided any clear guidance but all companies have had a close communication with them in order to get their acceptance. Shortly, an organization such as SABO influences the choices of how to account for component depreciation but the large impact comes from the auditors.

Since component depreciation was a new depreciation method for the companies in this study there existed a lot of uncertainty for how to account in accordance to this new regulation. There was no praxis available and according to DiMaggio and Powell (1983), the uncertainty could force companies to imitate other companies or organizations which have been made in our case since all the companies have, to some extent, imitated SABOs guidelines. This concept is in theory usually called mimetic isomorphism and has occurred in our study (DiMaggio and Powell, 1983). Although these companies have made similar implementations there are still differences which could imply that there are affected of other drivers than only the auditor's opinion and guidelines such as SABOs.

### **5.2.1 Institutional pressure**

Hatch and Cunliffe (2006) claims that when a company gets influenced from the external environment such as from the auditors or SABO as mentioned above, a company is being institutionalized. Institutionalization mainly occurs through different kinds of pressures (Hatch and Cunliffe, 2006). Pressure originates from external stakeholders and affects companies to become more alike (DiMaggio and Powell, 1983). The pressure in this study consisted mainly of regulations, guidelines from industry organizations and auditors. Pressure from regulations could make companies practice certain behaviors (Tate, Ellram and Dooley, 2014). This is in line with the coercive isomorphism developed by DiMaggio and Powell (1983). However, the pressure could also be from peer practitioners or industry praxis which

tells the company how to perform (Simpson, 2012). In our cases both *Alebyggen* and *ÖBO* looked at peer practitioners which have been early adopters to find notions. In *Poseidon's* case they were early with the implementation process and they did not have any other companies or industry guidelines to seek guidance from. Instead they could have been used as an institutional force since they, as an early adopter, had the opportunity to control and navigate the practical implementation to some extent.

K3 is a new framework which has an impact on the accounting generated within a company. The companies which applied these new regulations have, as Greenwood and Hinings (1996) wrote, changed their behavior according to the new pressure around them. In our study we can confirm that this had been made since the companies studied had put a lot of work into changing their depreciation methods to component depreciation since it was required in K3. In order to achieve an accounting with a true and fair view each company had to follow K3 to gain legitimacy. Therefore one can conclude that the framework is a large institutional force and according to Tate, Ellram and Dooley (2014), institutional forces play a key role for companies to adopt new items. According to Meyer and Rowan (1977) a formal organizational structure contributes with legitimacy by reflecting the myths in the institutionalized external environment. Sometimes an accounting method does not have to be effective, it just needs to gain the company legitimacy (Eriksson-Zetterquist, 2009). In this study regulation requires companies to implement component depreciation on their real estate and they had to do it to gain legitimacy. According to Eriksson-Zetterquist (2009) it is important that all information used outward the company is institutionalized, for example an auditor's report since it creates legitimacy to the external stakeholders.

## 6. Conclusion

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*The conclusion will answer our research question by using the analysis chapter as a base. Also, suggestions for future research will be presented here.*

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### **6.1 How do Swedish companies using K3 make their accounting choices regarding component depreciation?**

The new local framework was implemented in Sweden in 2014. Therefore, the first financial statements made according to K3 have recently become official. The new area component depreciation started to become implemented in the companies to be ready in time for the financial statements in the end of 2014. Some companies started with their implementation process already 2012 while some began in 2013 with the work. To relate to our research question, our analysis model will be used even in this chapter. First the perspective concerning practical handling will be evaluated.

To conclude, the companies included in this case study had decided to divide their real estates into 8-16 components. All companies have had a rather similar implementation process of the component depreciation on their real estates. They have started looking into the theoretical reasoning and thereafter they have had discussions in order to select suitable components and to be able to establish reasonable depreciation periods, depending on the material used on the components. Most companies had started out with looking into those few guidelines there were at the time of implementation, such as SABO, FAR and Fastighetsägarna. They have also evaluated which components that was in line with their maintenance plans which they consider to be important. The CFOs as well as accountants have been involved in the implementation process. Furthermore the administrators have been involved in the implementation in the companies as they are familiar with all real estates. One can conclude they were included to implement a more technical perspective to not only use the financial one. Therefore, one can conclude the companies in this study have made the implementation rather similar however with smaller differences.

To establish which components were suitable for their real estates, some companies had examined all their real estate while some had used templates. This also depended on the kind of real estates they had, some companies who did not only own residential properties, it was harder to use templates since their real estates were more individually adapted to the business contained within these buildings. The study showed that there was also hard to know what should be classified as maintenance and what should be repair. In the new framework, maintenance should be capitalized and repairs should not. Therefore, one had to divide the investments into those two. One can therefore conclude larger balance sheets will occur in the future as more and more investments have to be capitalized in differences than before when those costs were expensed.

## 6.2 Why are these choices being made?

The second part of our research questions will be answered by the remaining two perspectives of our analysis model, namely economic drivers and institutional forces. The study showed that the main reasons behind the choices of component depreciation had been made in consistence with the surrounding society. Managers had many different economic drivers behind their choices. The drivers which had influenced the companies the most were available frameworks, existing guidelines and auditor preferences. The main driver for what was influencing the companies within the existing regulations was to increase the true and fair view of their accounting. The study showed that all companies also used their existing maintenance plans when deciding which components to include. The maintenance plans played a major part when the companies were implementing component depreciations. The companies believed it would be easier to dispose and replace components later on if they were in line with the maintenance plans in the first place. Another factor influencing companies' choices was if components had the same purposes, economic life and functions. Then, companies tended to group these together as one component. Thereafter, companies believed it was be easier to replace parts of the real estates. However, the benefits to implement component depreciations had to exceed the costs of managing the components in the future.

Since K3 was a new framework and component depreciation was a new area there have been some difficulties to find guidance for how it should be implemented in the financial statements. One can conclude, as there have not existed any praxis the auditor's preferences have had a large impact since they have to accept the implementation in the financial statements. This institutional force had a large impact since all companies needed an unmodified auditor's report to gain legitimacy from external stakeholders. Furthermore, guidelines from industry organizations such as SABO, Fastighetsägarna and FAR have had a large influence as institutional forces in guiding companies in the initial implementation. When conducting this study it was clear that the companies included in this study had used these guidelines to a large extent in the practical handling of component depreciation. Also if a company followed SABOs guidelines it would gain legitimacy from external stakeholders. This leads to that the companies within the real estate industry would have a similar accounting procedure for component depreciation.

In this study the included companies have made similar choices regarding component depreciation to a large extent but all companies have made their choices in line with their business. Since the managers in each company have had different economic drivers for both themselves and their company, their choices became rather different. Not every manager made the same choices even though they faced a similar situation, like the implementation of component depreciations in this case. All seven companies in this study faced the same implementation and even though most companies we have interviewed owns residential properties they had not done the accounting choices precisely in the same way. Even though K3 is a principle-based framework one can conclude that the companies cannot completely make their own accounting choices since they were controlled by the regulations and their desire for an unmodified auditor's report. To conclude, depreciation is considered as one of

the most important accounting choices made in a company. Therefore all companies included in this study believed it was very important to implement it correctly and care about the implementation process.

### **6.3 Suggestions for further research**

The implementation of component depreciation on real estates is brand new and there has only been one annual report published at the time when this study is written. Therefore, to perform a similar study in, for example five years from now would be interesting as a complement for this study. Are companies in the real estate industry using the same components? Are their accounting choices influenced by other external factors than now and what are affecting the managers when doing their accounting choices? The follow-up study would be interesting to perform as one would be able to conclude how praxis will emerge within accounting and how much the companies have been influenced from new guidelines which will have arisen.

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## **Guidelines**

SABO, Sveriges Allmännyttiga Bostadsföretag. (2013). *“Komponentredovisning av Fastigheter: En vägledning”*.

## **Interviews**

AB Alebyggen: Sven-Arne Rasmussen, CFO. 19th March 2015.

Bostads AB Poseidon: Jessica Kruse, CFO. 30th March 2015.

Familjebostäder: Charlott Bengtsson, accountant. 23th March 2015.

Higab AB: Fredrik Setterberg, CFO. 30th March 2015.

HSB Göteborg: Anders Westman, CFO. Rebecca X, controller. 24th March 2015.

Svenska Hus AB: Måns Johannesson, CFO. 27th March 2015.

Öckerö Bostads AB: Hans Andreasson, CFO. 30th March 2015.

## **Regulations**

BFNAR 2012:1 (K3).

Årsredovisningslagen 1995:1554 (ÅRL).

## Appendix 1: Interview questions

1. What is your position in the company?
2. What kind of real estates does your company own? How are they used?
3. Which components did you choose to divide your real estate into? Which components do you consider as essential components for the significance of the asset?
4. How did you select the components in practice?
5. Who in the company has been a part of the implementation of component depreciation? Have other parts of the company apart from the accounting department been involved?
6. Who has the main responsibility for the accounting choices?
7. Do you have any examples of how you have applied component depreciation?
8. Which depreciation time did you choose for the different components? Why did you choose that time?
9. One aim with K3 is that maintenance costs should be capitalized in a larger extent than before. How does that affect you? Do you capitalize or expense costs you previously expensed? Has there been a change?
10. How much disclosure are you leaving in the financial statements?
11. Do you see any difficulties with component depreciation?
12. Why did you choose the components you did?
13. How big difference will component depreciation make on your total depreciable amount? More or less than before?
14. Do you think component depreciation gives a more true and fair view? Compared to earlier?
15. If you are supposed to make an accounting choice, what drives you to take the decision you do?
16. What affects you to do the accounting choices you do?
17. Do the same drivers affect you in choices of component depreciation as in other accounting choices? Or is there a difference?
18. Where did you find guidance for the implementation of component depreciation? Did you consult your auditors or other external part?
19. What has mainly affected you in order to choose the components you did?

## Appendix 2: Table of components

<b>Alebyggen</b>	<b>Familjebostäder and Poseidon</b>	<b>Higab</b>	<b>HSB</b>	<b>Svenska Hus</b>	<b>ÖBO</b>
Foundation	Foundation	Foundation	Foundation	Land	Foundation
Foundation, interior walls	Frontage	Roof	Roof	Land improvements	Roof
HVAC	Roof	Frontage	Frontage and windows	Permanent equipment in building	Frontage
Electricity	Windows	Windows	Technical installations	Foundation	Windows
Interior surface and kitchen appliance	Balconies	Installations	Foundation complementary	Roof	Interior surface
Frontage	VA	Foundation complementary	Land improvements	Windows	Kitchen design and kitchen appliance
Windows	Heating	Land improvements	Interior surface	Frontage	Bathroom
Kitchen and bathroom	Ventilation	Land	Residual values	Interior surface	Installations, electricity
Roof	Electricity			Installations	Installations, pipe
Ventilation	Elevator			Tenant adjustments	Installations, ventilation
Transport and elevators	Thermal installation			Ongoing projects	Installations, elevator
Control and monitoring systems	Ventilation aggregate				Installations, control
Residual values and interior surface	Kitchen and kitchen appliance				Installations, heating
	Bathroom				Garage/car-ports etc.
	Other interior design				Tenant adjustments
	Residual values				