

This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG FR TEG. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG FR Board or EFRAG FR TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG FR Board, are published as comment letters, discussion, or position papers, or in any other form considered appropriate in the circumstances.

## Better Information on Intangibles Cover Note

### Objective of the session

- 1 The objective of this session is to consider practical issues on intangibles reporting not addressed in [the Discussion Paper Better Information on Intangibles – Which is the Best Way Forward](#) (the DP).
- 2 The EFRAG Secretariat has conducted several interviews with the Big Audit firms. In this paper, in order to facilitate the discussion, the EFRAG Secretariat provided the summary of comments received during these interviews.

### Background and history of the project

#### *Objective and the scope of the project*

- 3 In August 2018, following the input received from constituents in response to the EFRAG Research Agenda Consultation, the EFRAG Board decided to add a research project on better information on intangibles to EFRAG's research agenda. The aims of the project are:
  - (a) to understand how entities report on creating, maintaining and/or improving their value;
  - (b) to understand how users consume information on creating, maintaining and/or improving value, and the extent to which current reporting addresses their needs; and
  - (c) to provide suggestions on how information on creating, maintaining and/or improving value can be provided in financial reports in a manner that is useful for decisions on providing resources to the entity.
- 4 The project focuses on information to be provided in the financial statements, including the notes, and in the management report, and considers information on intangible sources of possible economic benefits other than financial assets. This also includes intangibles used in the entity's operation. The project's scope is therefore broader than intangible assets and covers sources of possible economic benefits that would not be controlled by an entity.

#### *Discussion paper*

- 5 On 27 August 2021, EFRAG published the DP. The DP consults on the possible approaches to provide better information on intangibles, including whether/how they should be combined. The DP identifies three approaches:
  - (a) Recognition and measurement of intangibles in the primary financial statements, in Chapter 3;
  - (b) Providing information on specific intangibles in the notes to the financial statements or in the management report, in Chapter 4; and

- (c) Providing information on future-oriented expenses and risk/opportunity factors that may affect future performance in the notes to the financial statements or in the management report, in Chapter 5.

6 The DP comment period ends on **30 June 2022**.

*Future steps*

7 In Q4 2022, EFRAG FR TEG and EFRAG FRB will consider the comments received and will decide whether on that basis EFRAG will include recommendations in its resulting feedback statement.

**The issues for today's discussion**

8 In Chapter 2, the DP provides a list of reported issues with the existing information requirements related to intangibles. This list was established based on the discussions with the EFRAG Advisory Panel on Intangibles. However, some of these issues have not been discussed in more detail in the DP as the issues were considered to be too specific for the DP. The topics that were not considered included::

- (a) When something would be considered a prepayment for a right or service instead of an intangible asset;
- (b) When an agreement would be an executory contract or an intangible asset that should be recognised;
- (c) How to consider the unit of account when reporting on intangible assets.

9 The complete list of the issues is provided in **Appendix 1** of this paper.

10 At its October 2021 meeting, EFRAG FR TEG agreed that it would consider the additional issues identified by the EFRAG Advisory Panel on Intangibles that were not addressed in the DP.

11 In order to consider what EFRAG could do on the topics, including the potential outcome of discussion the issues, the EFRAG Secretariat has consulted major audit firms to learn about the identified issues and possible solutions. One of the purposes of this outreach was to receive information on the scope of the issues and number of possible solutions that could be considered. It was thus considered that EFRAG could relatively easily prepare, for example, bulletins on the issues if the scope would be relatively narrow and there would only be a few possible solutions to consider.

*Feedback received from interviews*

12 The EFRAG Secretariat consulted several Big Audit representatives during private interviews. The questionnaire prepared for these interviews is provided in **Appendix 1** of this paper.

13 During the interviews, the Big Audit representatives provided the comments on the consulted issues. The detailed comments are listed in **Appendix 2** to this paper.

*EFRAG Secretariat recommendation*

14 The EFRAG Secretariat has considered the reported issues and the explanation/comments received from Big Audit representatives.

15 The discussion showed that accounting for intangibles proves to be challenging. Many practices have emerged and there are different approaches to accounting for various specific intangibles. These solutions are not necessarily inconsistent and provide a robust and working solutions. However, they do not always fit the Conceptual Framework.

16 Consequently, we think that a scope of the discussion that would address the issues, that were not yet discussed in the DP, would be too large and reaching

conclusions would not be possible in a reasonable time frame . Therefore we do not propose to extend the scope of the project and to continue the discussion on the issues with accounting for intangibles.

- 17 Consequently, we think that EFRAG should prepare and publish the feedback statement on the DP and pass it to the IASB for their consideration during their discussions in the projects on intangibles.
- 18 Moreover, following EFRAG's publication of the feedback statement, EFRAG Secretariat should monitor the progress of the IASB project on intangibles and provide timely updates to the EFRAG FR Board and EFRAG FR TEG.

**Questions for EFRAG FR TEG**

- 19 Do you have comments on the feedback received by EFRAG Secretariat?
- 20 Do you agree with the recommendation of the EFRAG Secretariat?
- 21 What other activities would you propose for the EFRAG's Research Project *Better Information on Intangibles*?

## **Appendix 1: Questionnaire on remaining issues for future discussions**

### **Prepayment for a right or service versus intangible asset**

- 1 Have you encountered situations where it was debatable whether 'something' was a prepayment (e.g., for a right or a service) or an intangible asset? If so, what was the situation? What factors do you think should be considered when assessing whether something is an intangible asset or a prepayment?
- 2 Consider the following example: An entity may pay an amount to be able to broadcast a given future event (potentially together with other broadcasting companies). Do you consider that the entity has made a prepayment or acquired an intangible asset? Would it be a different situation if the entity had paid an amount for the master broadcasting rights for a given event (that is the entity can determine whether other entities should have any rights to broadcast an event)? If so, why is the latter situation different?

### **An executory contract or an intangible asset that should be recognised**

- 3 Have you encountered situations where it was debatable whether something was an executory contract or an intangible asset that should be recognised (e.g. an acquired right or a right achieved after incurring costs)? If so, please provide an example of such a situation. What factors do you think should be considered whether a contract would be an intangible asset?

### **The unit of account to consider when reporting on intangible assets**

- 4 Often the item referred to as an intangible asset consists of various rights. In principle, each of these rights is an asset. However, for recognition, measurement, and disclosure purposes these rights are accounted for a single asset. For many purposes, whether the various rights are accounted for separately or as a bundle does not have any impact on the information provided in the financial statements. However, the decision could impact, for example, the disclosures provided (whether they should be provided on each right or for a combination of these rights). It could also affect the accounting when not all rights related to the bundle of rights presented as a single asset, would be controlled by the same party.
- 5 When providing information on intangible assets, have you encountered situations where it was debatable what the unit of account should be when providing information on the intangible asset? If so, please provide examples of such situations and describe the factors you would consider when assessing the unit of account on which you think the information should be provided.

### **The issues mentioned but not addresses by the Discussion Paper**

- 6 The above topics were discussed during the interviews with the Big Audit firms representatives. However, the full list of issues for further consideration is listed as follows in the DP:  
For intangibles that would meet the definition of an asset
  - (a) How to assess 'control' in relation to certain intangibles. For example, should control be assessed in relation to the right to be able to broadcast a given event (together with other broadcasting companies) or to holding the master broadcasting rights for a given event?
  - (b) It is not always straightforward whether an asset should be accounted for under IAS 2 Inventories or IAS 38.

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- (c) It is not always clear whether an asset is a pre-payment or an intangible asset. For example, whether an upfront payment to be able to broadcast a given event would be a pre-payment for a service or the purchase of an intangible right.
- (d) It is not always straightforward whether/when a contract could be considered an intangible asset.
- (e) Difficulties with allocating the total transaction price for intangible assets acquired in a bundle (outside a business combination).

For the broader category of intangibles which would not necessarily meet the definition of an asset

- (f) Information on intangibles is difficult to compare and use as the boundaries between different intangibles are not (well) defined and are interpreted differently. Even for those that meet the definition of intangible assets there are different interpretations on what development costs are.
- (g) It is unclear what the unit of account is. This also applies for acquired intangible assets. For example, a movie picture includes many distinct types of rights such as author rights, music rights and graphical rights. It is unclear whether these rights are different intangible assets or the intangible asset on which information should be provided is the movie picture.
- (h) The information to be provided may be commercially sensitive.

## Appendix 2 – Comments received for Big Audit firms

- 1 The EFRAG Secretariat organised five interviews with the members of Big Audit. They provided the following comments grouped by topic as follows:

### *Prepayment vs intangible*

- (a) The issue identified on whether something is a prepayment or an intangible asset, in addition to existing on broadcasting rights, also exists in relation to cloud software. On cloud software, the issue is amplified because of the implementation costs. If there is not an asset, these implementation costs cannot be capitalised. The issue on the implementation cost also reflect on the unit of account issue – i.e. it is not clear whether the software to be used, and the hosting platform is one unit, or they represent two units of account. In this respect, the IFRS Interpretation Committee has pointed in the direction that this would normally constitute just one service – that would mean that implementation costs cannot be capitalised.
- (b) It is also commented that IAS 38 and the definition of intangibles in IAS 38 was developed long time ago and does not reflect the currently existing types of intangibles.
- (c) When deciding whether an event is a purchase of intangible asset or a prepayment, it should be considered whether there is an intangible asset if there is a payment in arrears instead of in advance.
- (d) Actually the difference does not matter. The question is whether there is an asset and then what type of asset it is. Depending on that, the expense would be presented differently.
- (e) The idea that prepayment may be an intangible on its own seems self contradictory.
- (f) Another issue is with a talent show, when a tv station makes a significant prepayment, which funds the production. It is not clear whether the prepayment is an instalment for intangible or something separate.
- (g) In pharma industry, should a prepayment to a bio-tech company be considered as research and development, or a prepayment for the service and carried as prepayment asset in the balance sheet. Furthermore, there is significant difference between the accounting for a research contract and the same research done “in-house”, however, operationally, the two alternatives seems similar.
- (h) Accounting for prepayments is a bit of an art rather than science, therefore, it is hard to propose something for enhancing the guidance on intangibles in this respect. In many cases there are solutions that work and are robust but do not really fit the framework.

### SAAS (Software as a service) agreements

- (a) The number of business models that use service packages is increasing. If they provide a right to something that the provider may change, then it could be a service. Also, when you buy the right to something that still needs to be developed, it is not clear what is actually being purchased (e.g. film rights).
- (b) In regard to SAAS agreement, the investment cannot be recognised on the balance sheet. Furthermore, IFRIC tries to clarify that IFRS 15 should be applied to check whether it is a prepayment for a service. However, IFRS 15 was written for the selling side not the purchasing side.

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- (c) Sometimes something perceived as a prepayment for a service could be related to an asset e.g. implementation costs for a service could be part of the software.
- (d) In a SAAS arrangement there is an exclusive right to use a software and at the end of the service period, the software provider would delete the software. However, there are usually significant implementation expenses. So the question is why the implementation expenses should be expensed as they would result in benefits in the future.
- (e) In a SAAS contract there is an issue of control i.e. the client does not control the code. It could be seen that the client controls the code according to the contract but IT people think that a code cannot be controlled by anyone.
- (a) The SAAS contracts seems to be like leasehold improvements. They are not controlled, but they were not expensed.
- (b) In IFRS 16, now, nobody questions that there is an asset. In SAAS it is like renting an asset so the issue should be also considered while revising leases guidance in IFRS 16.

### Broadcasts

- (a) Actually there is no consensus on the examples. It seems similar to the accounting for football players' contracts.
- (b) Regarding the broadcasting rights there are mixed views. It is debatable whether these are prepayments, intangibles, or inventory. If the right is an exclusive right, then most would consider it as an intangible asset. However others would recognise a service.

### *Unit of account*

- (a) There is no clear answer to the question. Multiple elements of IFRS 15 guidance could be considered.
- (b) Regarding the football matches, when considering a contract, you can do summaries of the games you could sell to other entities. So, to determine the units of account, you would need to consider how many rights there would be and allocate the price to these.
- (c) IFRS 15 model gave you a framework on unit of account and on the allocation and that was the only available so far. The IFRS IC has made a reference to IFRS 15 and noted that the customers should also apply IFRS 15. It would be an innovation to use the distinct guidance to determine whether there is a separate asset, but IFRS IC has not come so far.
- (d) There is no specific guidance on intangibles. IFRS 16 could provide some more guidance.
- (e) Unbundling just for the sake of unbundling would involve costs and would impact decision process. For instance, a movie is made up of various component elements. The question is therefore whether an investor would benefit from bigger granularity of the presentation of such intangibles.

### *General comments*

- (a) All topics that touch on intangibles were important questions. However, it may take 10 years before a new IAS 38 is available. Therefore, bringing the issues to the table does make sense. There would be no consensus on what the solutions should be. Moreover, the financial statements of companies were not comparable in regard to intangibles because of the divergence in practice.

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- (b) The issue with intangibles should have been discussed when moving from IAS 17 to IFRS 16. Intangible assets are the value drivers of the future, so it needs to be addressed.
- (c) IAS 28 is a research and development standard and assumes that at the beginning there is some fundamental risky work, and towards the end the product gets ready for market and capitalisation may begin. However, existing intangibles barely fit this pattern. At the same time, IFRS 3 requires aggressive identification of intangibles.
- (d) There are other examples of difficulties when accounting for intangibles. For instance, should the costs spent on verifying the road network for a map provider be capitalised or expensed. Moreover, when a right to only certain uses of the data can be sold / purchased. the buyer would recognise a different asset. However, there is a question whether an asset should be partially derecognised.
- (e) Another issue relates to a situation when a long-lasting legacy software that is expected to cost each time when the operating system is changed. Does it require a recognition of liability? Similarly, ongoing maintenance could be burdensome, but not recognised as an asset.
- (f) It is high time to start recognising the importance of intangibles.
- (g) IAS 37 could be described as a pre-Internet drafted standard and does not address the issues that recently emerged. Consequently, its guidance does not fit such items as cloud computing, other
- (h) Some believed that the interpretations of the various issues by Big Audit seem consistent.
- (i) The reason not to recognise internally generated intangibles is that the valuation of such asset cannot be reasonable assured.
- (j) A potential revision could consider identifying distinct buckets of intangibles and provide guidance separately on each of those buckets. However, on the other hand it may not fit all the new emerging types of intangibles that may result from legislative right, or other social circumstances.
- (k) There is another question regarding whether accounting guidance could be different for government or private organisations.
- (l) The role of global IFRS desk is to agree with the assessment or explain why they cannot support certain recognition, presentation, or approach. So it is more a validation process than standard setting.
- (m) The way forward would to be to identify the areas where IAS 38 lacks guidance. The most common situations would need to be addressed. It is also not possible, even when principle-based standards to address all the existing options and permutations. Furthermore, the name of the standard plays a significant role.