

## EFRAG DISCUSSION PAPER

### BETTER INFORMATION ON INTANGIBLES WHICH IS THE BEST WAY TO GO?

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**Subject:** Efrag Discussion Paper “Better Information On Intangibles Which Is The Best Way To Go”

Dear Mr. Gauzès,

The Portuguese Accounting Standard Setter (Comissão de Normalização Contabilística - CNC) appreciates the opportunity to comment on the EFRAG Discussion Paper “Better Information On Intangibles Which Is The Best Way To Go”.

#### QUESTION 1 - ISSUES WITH THE CURRENT INFORMATION

Chapter 2 summarises issues put forward with the current information on intangibles. Do you think the issues listed are relevant and valid? Are there additional issues with the current information on intangibles that are not listed? If so, what are these issues?

CNC agrees that the issues are relevant and valid and do not identify any further relevant issues.

#### QUESTION 2 - WHICH WAY TO GO?

Chapters 3, 4 and 5 present possible different approaches to provide better information on intangibles (namely recognition and measurement; disclosure of information on specific intangibles; information on future-oriented expenses and risk/opportunity factors) and, within each approach, different alternatives to provide better information on intangibles.

These different approaches represent different trade-offs between benefits and costs when considering the different needs of users of financial reports for better information on intangibles.

Do you think there is room for improvement regarding information on intangibles in financial reporting? If so:

- a) Do you think the different approaches described could be combined in a manner that could meet (most of) the needs of users and for which the benefits would exceed the costs? If so, please describe such a combination.
- b) If you do not think the different approaches described in the Discussion Paper could be combined in a manner that would meet (most of) the needs of users, which (if any) of the described approaches do you think could be worth investigating further with the objective of getting better information on Intangibles:
  - Amending existing recognition and measurement requirements for intangibles (see Chapter 3);

CNC considers that a revision of IAS 38, considering both recognition and disclosures, will satisfy the most relevant needs of the users of the financial statements, without causing too much disruption with the current approach. The way to go should be simple, objective, and easy to understand, apply and verify.

- Providing disclosures on specific intangibles (see Chapter 4);
- Providing disclosures on future-oriented expenses and risk/opportunity factors that may affect future performance (see Chapter 5); or
- An approach other than those described in the Discussion Paper (please explain this approach)?

### QUESTION 3 - RECOGNITION

Chapter 3 considers whether and how internally generated intangibles could be recognised and measured in the financial statements and the benefits and limitations of the proposed approaches. In doing so, consideration is being given to the asset recognition in the statement of financial position but also to the effects in the statement of financial performance.

Do you consider that IAS 38 Intangible Assets should be amended to permit the recognition of certain internally generated intangible assets (in addition to development costs)? (Please explain your answer).

CNC considers that certain internally generated intangible assets should be capitalized to reduce inconsistency between acquired and internally generated intangibles.

If your answer to this question is 'yes', please also answer sub-questions 1 to 3 below.

1. Paragraph 3.26 of this Discussion Paper explains that IAS 38 currently includes an explicit prohibition to recognise some types of internally generated intangible assets such as internally developed brands, mastheads, publishing titles, customer lists and similar items, staff training and marketing. Do you consider that the explicit prohibition to recognise some types of intangible assets that exists in IAS 38 should be removed? (Please explain your answer).

CNC is of the opinion that explicit prohibition to recognize some types of internally generated intangible assets should be removed as the annual impairment test will prevent the capitalization of unsuccessful assets. As said, current inconsistency between acquired and internally generated intangibles assets should be avoidable. The explicit prohibition should be replaced by explicit conditions for recognition.

2. Paragraphs 3.10 to 3.71 of this Discussion Paper explore four possible approaches regarding the recognition of internally generated intangibles. Which of the following approaches would you support?
  - a. Recognise (as an asset) all defined intangibles; with no specified conditions or thresholds (see paragraphs 3.15 - 3.35 of this Discussion Paper);
  - b. Threshold for recognition of an asset (see paragraphs 3.36 - 3.48 of this Discussion Paper);
  - c. Conditional recognition of an asset (see paragraphs 3.49 - 3.59 of this Discussion Paper); if you prefer this approach, would you prefer an approach under which:
    - i) Costs are expensed in profit and loss until the condition is met;
    - ii) Costs are capitalised and fully impaired until the condition is met, at which point in time the impairment
    - iii) losses are reversed;
    - iv) Costs are expensed in other comprehensive income until the condition is met, at which point in time
    - v) the expenses are 'recycled' and capitalised.
  - d. No recognition (that is, expensing all internally generated intangibles) (see paragraphs 3.60 - 3.67 of this Discussion Paper); and
  - e. None of the above or other suggestions (please explain).

CNC agrees that only intangibles that meet the definition of an asset in the Conceptual Framework should be recognize. Concerning the four possible approaches, CNC supports option b), that is to amend the current recognition thresholds on IAS 38. CNC supports a revision of IAS 38 in order the define a less restrictive version of the current identifiability criterion combined with other clear and explicit recognition conditions as those presented in paragraph 3.45. CNC supports the cost model to recognize intangibles. Additionally, CNC is of the opinion that only intangible that could be monitored for impairment could (or should) be capitalized and an impairment test should be done annually until a useful life for the intangible is assessable. CNC is aware that the approach could lead to an implicit "option" for recognizing intangibles and supports that a clarified statement should be made in the revised standard concerning a mandatory or, alternatively, an optional view to recognize internally generated intangibles.

3. If you support 'Conditional recognition of an asset' or 'Threshold for recognition of an asset' in the previous sub-question, which criteria would you consider for recognition:

- a. Criteria based on the level of (un)certainty about the outcome of the intangibles (that is, the probability of expected benefit and the pattern of consumption of these future benefits);
- b. Criteria based on the identifiability of the expenditure related to the intangibles;
- c. Criteria based on the technical or commercial feasibility of the intangibles considered at inception of the development;
- d. Criteria based on separability of the assets, that is, the existence of a legal right and/or the ability to sell, transfer, licence or pledge the asset;
- e. All or a combination of the above depending on the nature of the intangibles (please explain);
- f. Other suggestions (please specify).

CNC supports option b) as it is consistent with the cost model.

#### QUESTION 4 - POSSIBLE MEASUREMENT BASES

Paragraphs 3.72 to 3.100 of this Discussion Paper consider possible measurement bases for internally generated intangibles without suggesting a preferred approach. If you think that IAS 38 should be amended to permit the recognition of certain internally generated intangible assets (in addition to development costs), which of the following suggested measurement approaches would you support:

- a. Initial and subsequent measurement at amortised cost with impairment ('Cost model');
- b. Initial measurement at cost and subsequent measurement at fair value ('Revaluation model');
- c. Initial and subsequent measurement at fair value ('Fair value model');
- d. Initial measurement at fair value (as deemed cost) and subsequent measurement at amortised cost with impairment ('IFRS 3 model')?

CNC supports the cost model. Assessing the fair value of an intangible is too subjective, volatile, based on level 3 inputs and difficult to validate.

#### QUESTION 5 - INFORMATION RELATING TO SPECIFIC INTANGIBLES

Chapter 4 discusses an approach under which information on specific intangibles, that are key to an entity's business model, is provided to help users assess the contribution of the intangible to the value of the entity.

1. To the extent that information relating to specific intangibles should be provided, do you agree that the information should be limited to the intangibles that are key to an entity's business model? If not, why?
2. Preliminary feedback received from some users of financial reports indicates that an entity's fair value estimate of a specific intangible would generally not be particularly relevant information. Do you agree that disclosing the fair value of an intangible is less helpful for users than disclosure of quantitative and qualitative information that could

assist them in forming their own views on the value for an entity of the specific intangible?

3. Do you agree with the advantages and disadvantages of information relating to specific intangibles as identified in Chapter 4 compared to recognition and measurement (see Chapter 3) and information on future-oriented expenses (see Chapter 5)? If not, which aspects do you disagree with and/or which additional advantages and disadvantages have you identified?

Concerning disclosure about intangibles, CNC agrees that it is important to investors and other stakeholders to understand how the business model depend on some key intangible resources. However, we are also concerned about market sensitive information. CNC is of the opinion that a compulsory disclosure about how the business model depends on intangible resources may lead firms to provide excessive information about their own business, so we defend flexibility in the process of disclosing information about intangibles. To assure relevance and reduce subjectivity, we are of the opinion that disclosures items regarding non capitalized intangibles should be limited to information about the reasons why these intangibles are not being recognized in the balance sheet and information about the relevance of each intangible that contributes to the business model. Concerning capitalized intangibles, CNC agrees with the list of information about specific key intangibles presented in the first picture of paragraph 4.19.

#### QUESTION 6 - INFORMATION ON FUTURE-ORIENTED EXPENSES

Chapter 5 proposes various elements of information on expenses recognised in a period that could be considered to relate to benefits that will be recorded in future periods ('future-oriented expenses').

1. Do you consider that requiring such information could be useful? If so:
  - a) Should the information mainly complement information on specific intangibles (see Chapter 4) or should requirements on future-oriented expenses be introduced instead of requirements on information on specific intangibles?
  - b) Should the information mainly:

(i) Reflect the views of the entity's management by disclosing the recognised expenses the management considers relate to the benefits of future periods)? Or

(ii) Help users perform their own assessments on the recognised expenses that relate to benefits of future periods, by providing further specifications and breakdown of the expenses of a period?

CNC believes that information on future-oriented expenses should mainly complement information on specific intangibles on an option basis.

2. Do you agree with the advantages and disadvantages of information on future-oriented expenses identified in Chapter 5? If not, which aspects do you disagree with and/or which additional advantages and disadvantages have you identified?

CNC agrees with the list of advantages and disadvantages identified in chapter 5.

#### QUESTION 7 - INFORMATION ON RISK/OPPORTUNITY FACTORS AFFECTING INTANGIBLES

Chapter 5 proposes that information included in the financial reports on factors affecting intangibles should be limited to disclosing risk/opportunity factors linked to the key intangibles (whether or not specified) according to the entity's business model. The disclosure should include a description of the risk/opportunity, relevant measures reflecting the risk/opportunity, if relevant (for example, KPI's used to measure it), and how the risk is managed and mitigated. It should include an assessment of the materiality of the risk/opportunity factors based on the probability of their occurrence and the expected magnitude of their impact.

Do you agree with this proposal? If not, what information on risk/opportunity factors affecting intangibles should be provided?

CNC agreed with the proposal.

#### QUESTION 8 - ISSUES TO BE CONSIDERED

Chapter 6 discusses challenges and issues to be considered when finding a manner to provide better information on intangibles. It mentions that it could be beneficial to introduce a common terminology on intangibles and that preparers of financial statements should not be required to disclose information on intangibles that would be (very) commercially sensitive.

1. Do you consider that it would be useful to introduce a common terminology on intangibles?  
Yes.
2. Do you agree that preparers of financial statements should not be required to disclose information on intangibles that would be (very) commercially sensitive?  
Yes.
3. Are there additional issues than those listed in Chapter 6 you think should be taken into account when considering how to provide better information on intangibles?

#### QUESTION 9 - PLACEMENT OF THE INFORMATION

Chapter 6 presents an approach under which information discussed in Chapter 4 and Chapter 5 would be placed in the notes to the financial statements if the information is related to an item that meets the definition of an asset or to an item recognised in the statement of financial performance. In other cases, the information would be placed in the management report.

However, it is noted that such an approach would result in information about intangibles to be spread between the notes to the financial statements and the management report.

Where do you think the different types of information that would follow from the approaches discussed in Chapter 4 and Chapter 5 should be placed? Should they be placed all in the same section or in different sections of the financial report and why?

CNC supports the disclosure on a specific section with cross reference to other sections of the financial report because is easy to access-