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Better Information on Intangibles Cover Note

Objective

- 1 The purpose of this session is to approve the Recommendations and Feedback Statement in response to EFRAG's [Discussion Paper: Better Information on Intangibles – Which is the best way to go?](#) (the 'DP').

Background

- 2 In August 2021 EFRAG issued the DP including different approaches to get better information on intangibles. The deadline for comments was 30 June 2022.
- 3 The comment letters received are available from [EFRAG's website](#).
- 4 The input has previously been considered by:
 - (a) The EFRAG Advisory Panel ('EFRAG API') at its 27 October 2022 meeting;
 - (b) EFRAG FR TEG at its 9 November 2022 meeting; and
 - (c) EFRAG SR TEG and EFRAG FR TEG at their joint 17 January 2023 meeting.
- 5 A comprehensive summary of the input received is available [here](#).
- 6 A presentation of the main messages in the input received is available [here](#) (this presentation was used for a previous EFRAG FR TEG session – the questions included in the presentation are therefore not relevant for this meeting).
- 7 At its 9 November 2022 meeting, EFRAG FR TEG considered that it was possible to make some recommendations to the IASB based on the input received in response to the DP.
- 8 At its 18 – 19 January 2023 meeting, EFRAG FR TEG considered an outlined Recommendations and Feedback Statement (the 'RFS'). EFRAG FR TEG agreed on changes to the RFS. It decided to vote on whether it could recommend an amended version of the RFS to the EFRAG FRB by written procedure.
- 9 The voting period ended on 2 February at 16:00 CET.

EFRAG FR TEG vote on the RFS

- 10 13 EFRAG FR TEG members approved the version of the RFS circulated for the vote by written procedure. One EFRAG FR TEG member did not approve. Some of the EFRAG FR TEG members approving the RFS provided some comments they asked to be reflected in the RFS.
- 11 As EFRAG FR TEG approved to recommend the RFS to the EFRAG FRB for approval, the EFRAG Secretariat has made the approved version of the RFS available for this session (Agenda Paper 08-02). In the Appendix to this Cover Note, the EFRAG Secretariat, however, lists the main comments provided by both EFRAG

TEG members who approved the RFS, and the member who did not approve, the RFS. In the Appendix, the EFRAG Secretariat also provides suggestions on how some of the comments made can be addressed without changing the intended content of the RFS. These suggestions have also been reflected in Agenda Paper 08-03 for this session.

Questions for EFRAG FR TEG and EFRAG FRB

- 12 Does EFRAG FR TEG have any comments to the suggestions made by the EFRAG Secretariat on how to deal with the comments made by EFRAG FR TEG members as part of the written procedure to recommend the RFS to the EFRAG FRB (see the Appendix to this Cover Note)?
- 13 Does EFRAG FRB have any comments to the RFS with the amendments suggested by the EFRAG Secretariat in the Appendix to this Cover Note?
- 14 Does EFRAG FRB approve the RFS (with the changes suggested)?

Next steps

- 15 The publication of the RFS is the last step involving EFRAG FR TEG and EFRAG FRB in relation to EFRAG's project on better information on intangibles. The RFS will then be presented at a few events.

Agenda Papers

- 16 In addition to this Cover Note, the following papers have been prepared for the session:
 - (a) Agenda paper 08-02 – the Recommendations and Feedback Statement (as approved by EFRAG FR TEG).
 - (b) Agenda paper 08-03 – the Recommendations and Feedback Statement (with changes suggested by the EFRAG Secretariat following the comments made by EFRAG FR TEG members as part of the written approval)

Appendix: Comments from EFRAG FR TEG members to the RFS

Introduction

- 1 This Appendix describes the comments made by EFRAG FR TEG members when approving to recommend the RFS to the EFRAG FRB and suggestions of the EFRAG Secretariat on how to deal with these comments.

Comments of the EFRAG FR TEG member who did not approve the RFS

- 2 The EFRAG FR TEG member who did not approve the RFS considered that:
 - (a) It is unclear whether the '**summary of recommendations**' on page 5 of the RFS represented EFRAG's recommendations to the IASB or a summary of the feedback received. The member thought that if the former was the case, EFRAG FR TEG should consider the summary at a separate session.
 - (b) The section on '**Information on expenses**' reflected a too positive position of EFRAG on the approach and that the section did not explain that it could be challenging to provide guidance on which expenses would be future oriented, should the approach under which the management would have to make the distinction be introduced.
 - (c) That the EFRAG recommendations (in the section '**Interlinkage with sustainability reporting**' on page 8 of the RFS) on the disclosure on risks and opportunities contradicted the statement that efforts in the standard-setting of both financial reporting and sustainability reporting should be coordinated to ensure the information required under the two regimes would be complementary and not overlapping.

Comments of EFRAG TEG members approving the RFS

- 3 The main comments of the EFRAG FR TEG members who approved the RFS related to:
 - (a) Reference to **materiality threshold** in the description on pages 6-7 of the RFS of recognition and measurement and the information on expenses. A member noted that this reference is not needed as the concept of materiality is already a pervasive principle.
 - (b) Reference to '**key to an entity's business model**' on, e.g., page 7 of the RFS. A member thought it should just be explained that it would be a higher threshold than material.
 - (c) The term '**future-oriented expenses**' (used, for example, on page 7 of the RFS). A member thought the term needed to be defined, or at least the meaning needed to be illustrated. Another member thought it could be defined as expenses that "could be *considered* to relate to benefits that will be recorded in future periods". Another member suggested to define it as "expenses that are not recognised as intangible assets".
 - (d) A member thought that the section on '**Information on expenses**' reflected a too positive position of EFRAG on the approach.
 - (e) **Placement of the information on specific intangibles** (page 7 of the RFS). A member disagreed with this information being placed in the notes to the financial statements. The member thought that the question on the placement of this information should be left open.
 - (f) The section '**Interlinkage with sustainability reporting**' on page 8 of the RFS). A member thought that the section should just state that information should not be duplicated in sustainability reporting and financial reporting.

- (g) The sentence on page 9 of the RFS from which it follows that the IASB should consider whether the rationale for including some explicit prohibitions in IAS 38 to recognise **expenditure on training staff, selling and administration**. A member did not support providing this recommendation as it seemed unlikely that it would be possible to provide a working principle that could replace this seemed very unlikely. Another member agreed.
- (h) The statement on page 10 that another alternative to recognising additional intangibles would be to change the requirements in **IFRS 3 Business Combinations**. Two members did not support changing the requirements of IFRS 3 to include some intangibles currently recognised separately in goodwill. Another member thought that the wording used in the RFS could be read as if EFRAG recommended the IASB to reconsider the requirements in IFRS 3. This member suggested to simply recommend the IASB to consider the overall matter in the context of its forthcoming project. Three other members agreed with this.
- (i) **Placement of the information on future-oriented expenses** (page 12 of the RFS). A member disagreed with stating that this information could be placed into the notes to the financial statements).
- (j) The section '**Commercial sensitivity**' on page 12 of the RFS. A member considered that the statement "ensure that entities will not be required to provide information that is (very) commercially sensitive" should be amended to a softer wording such as: "consider providing an exemption to the disclosures requirements in specific circumstances and proposing a principle defining when to apply this exemption". Another member agreed with this but thought it could be necessary to provide application guidance on commercial sensitivity.

Suggestions of the EFRAG Secretariat

- 4 In response to the comments above, the EFRAG Secretariat suggests (the references to the RFS are to the version presented in Agenda Paper 08-02):
- (a) In response to the comment on the '**summary of recommendations**' (see paragraph 2(a) above), the EFRAG Secretariat notes that the purpose of the summary is to summarise the recommendations included on pages 6 – 12 of the RFS. The summary should therefore not include any information that does not appear from pages 6 – 12. The EFRAG Secretariat invites EFRAG FR TEG and EFRAG FRB members to provide drafting suggestions to the summary (taking into account that the summary should only highlight the most important recommendations).
 - (b) In response to the comment on the **materiality threshold** (see paragraph 3(a) above), the EFRAG Secretariat suggests that the reference to the materiality threshold is removed from the description of 'Recognition and measurement' on page 6 of the RFS and the description of 'Information on expenses' on page 7 of the RFS. Instead, the description of 'Information on specific intangibles' on page 7 would be amended as follows:

“...The threshold 'key to an entity's business model' is higher than the materiality threshold (used for recognition and measurement and information on expenses) described in paragraph 2.11 of the Conceptual Framework.
 - (c) In response to the comment on '**key to an entity's business model**' (see paragraph 3(b) above), the EFRAG Secretariat suggests deleting footnote 1 on page 7 of the RFS:

~~“⁴The EU directive on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings defines key intangible resources as resources without physical~~

~~substance on which the business model of the undertaking fundamentally depends and which are a source of value creation for the undertaking.”~~

- (d) In response to the comments on the term **‘future-oriented expenses’** (see paragraph 3(c) above), the EFRAG Secretariat suggests the following amendment to the section ‘Information on expenses’ on page 7:

Information on expenses: For internally generated intangibles that are not recognised, information on future-oriented expenses, ~~{that is, expenses that could be considered to relate to benefits that will be recorded in future periods (e.g., in some cases this could be marketing expenses related to increasing an entity’s market share) as defined below}~~ could provide information to support users’ understanding of the value of the entity’s unrecognised internally generated intangibles.

- (e) In response to the comment on **‘Information on expenses’** (see paragraphs 2(b) and 3(d) above), the EFRAG Secretariat suggests the following amendments to the paragraph on page 7 of the RFS to reflect a less positive position and highlight the operational issues:

“...The information can, however, provide information on e.g., the entity’s business model when the information is provided on a disaggregated level (see below). EFRAG acknowledges that there would be operational complexities and costs with the approach. For example, it could be challenging to provide guidance on – or for an entity to operationalise – which expenses would be future-oriented, should the approach under which the management would have to provide its assessment be introduced. Similarly, EFRAG acknowledges that, like other examples of disaggregated disclosures about current expenses, this information may trigger operational costs to be implemented, nevertheless the interaction with users during the research project shows that they consider this to be valuable information. However, as it appears from the summary of the feedback EFRAG received on Question 6 of the DP, the majority of the respondents providing a view on the matter, considered the information to be useful.”

- (f) In response to the comment on the **placement of the information on specific intangibles** (see paragraph 3(e) above), the EFRAG Secretariat suggests clarifying that EFRAG does not provide a view on whether the information should be placed in the notes to the financial statements or in the management commentary by adding to the first paragraph on page 8:

“...Conceptual Framework). The information can be quantitative (including KPI’s), qualitative or both. Accordingly, if quantitative information cannot be provided, qualitative information should be provided.

Based on the input received in response to the DP, EFRAG is currently not providing a view on whether information on specific intangibles should be placed in the notes to the financial statements or in the management commentary (see ‘Placement of disclosures’ below).”

- (g) In response to the comment on **‘Interlinkage with sustainability reporting’** (see paragraphs 2(c) and 3(f) above), the EFRAG Secretariat suggests the following changes to the section on page 8 of the RFS:

~~“The DP proposed that information on risk/opportunity factors affecting intangibles should be provided. Following EFRAG’s consultation on the DP, EFRAG recommends that information should be provided on the risk and opportunity factors related to the intangibles that are key to an entity’s business model. In the DP it was noted that these~~The intangibles may or may not be recognised and/or it may, or it may not, be possible to specify which intangible(s) the information is related to. The disclosure would require the

~~entity to describe its business model. Disclosure on risk and opportunity factors could cover information about value creation linked to intangible resources, for which it is not possible to identify a specific intangible, as they contribute to value creation in conjunction with other resources of the entity. The description should be limited to the risks/opportunities that are specific to the entity. The disclosure should include a description of the risk/opportunity, relevant measures reflecting the risk/opportunity and how the risk is managed and mitigated. An assessment should be provided on the materiality of the risk/opportunity based on the probability of its occurrence and the expected magnitude of the impact. A majority of the respondents providing a view on the issue, supported these disclosures.~~

~~The DP noted that there could be risks and opportunities related to sustainability that could also become useful for the primary users of the financial reports. EFRAG considers that the information on risk and opportunity factors would be best placed in the management commentary. It could therefore be considered as part of the IASB's project on the management commentary, on which EFRAG is looking forward to working with the IASB.~~

In this regard, EFRAG notes that information on intangibles will not only be found in the financial statements but also in relation to sustainability information, for intangibles that are linked to sustainability matters. Much is currently taking place in this area at the moment. To improve information on intangibles in a broader corporate reporting perspective, the efforts in the standard-setting of both financial reporting and sustainability reporting should be coordinated to ensure the information required under the two regimes would be complementary and not overlapping.

To consider the interlinkage between financial reporting and sustainability reporting, EFRAG has initiated a project on the interconnectivity between these regimes. The findings, suggestions and recommendations of this project will be relevant for the IASB.

EFRAG considers that the information on risk and opportunity factors could be relevant in relation to the IASB's project on the management commentary. ~~would be best placed in the management commentary. It could therefore be considered as part of the IASB's project on the management commentary, on which~~ EFRAG is looking forward to working with the IASB on this project."

- (h) In response to the comment on '**expenditure on training staff, selling and administration**' (see paragraph 3(g) above) the following amendment to page 9 of the RFS is suggested by the EFRAG Secretariat:

"...The prohibitions that should be re-considered are:

- a) the prohibition in paragraph 63 of IAS 38 to recognise internally developed intangibles such as brands, mastheads, publishing titles, customer lists and items similar; and
- b) the prohibition to recognise expenditure on training staff, selling and administration (paragraph 69 of IAS 38).

The IASB's reconsideration of these prohibitions does not mean that they would be removed.

It was noted that the recognition of items in a) ..."

- (i) In response to the comment on the reference to **IFRS 3 Business Combinations** (see paragraph 3(h) above), the EFRAG Secretariat suggests the following amendment to the related paragraph on page 10 of the RFS:

“When it comes to recognising the same assets regardless of whether these have been acquired as part of a business combination or developed internally, EFRAG recommends the IASB to consider this matter as part of its project on intangibles, notes that another alternative, which it has not further explored, is to significantly change the requirements in IFRS 3 Business Combinations.”

- (j) In response to the comment on the **placement of the information on future-oriented expenses** (see paragraph 3(i) above), the EFRAG Secretariat suggests removing the comment on the placement:

A few respondents have suggested that the different level of audit requirements may be a differential factor, as well as the forward-looking nature of some of the disclosures and their interlinkage with the information about strategy and business model, which is normally placed in the management commentary. ~~Disclosure about specific intangibles does not have a direct link to amounts that are recognised on the statement of financial position. Disclosure of future-oriented expenses is seen by some as better located in the notes to the financial statements, as it pertains to amounts (expenses) that are recognised, nevertheless due to the forward-looking and judgemental nature of their disaggregation, others consider that the management commentary is more suitable. Some users were less interested to the location, to the extent that the information is available~~”

- (k) In response to the comment on the section ‘**Commercial sensitivity**’ (see paragraph 3(c) above), the EFRAG Secretariat suggests the following amendment to the last paragraph on page 12 of the RFS:

“When considering whether the benefits of new requirements would exceed the costs, the IASB should consider the potential commercial sensitivity of the information. It should thus be considered providing an exemption to the disclosures requirements in specific circumstances and proposing a principle defining when to apply this exemption. Application guidance on the issue (see the section on application guidance above) could be considered on this issue, ensured that entities will not be required to provide information that is (very) commercially sensitive.”

- 5 Consequential amendments to other parts of the RFS might follow from the changes suggested above.