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Foreword

This is the fourth Grant Thornton survey of accounting practices in the media sector. Our latest survey looks at the effects of the introduction of IFRS across those UK media companies quoted on the London Stock Exchange Full List and AIM.

Our previous three surveys focused on the areas of revenue recognition, rights recognition and rights amortisation in the UK film and television sectors.

When we published our first survey in 2001, we wanted to create a debate in the area of UK film and television accounting that would lead to better disclosure, and greater consistency and transparency in financial reporting of revenue and rights recognition. We also wanted to improve the understanding between the sources of funding in the City and the creative businesses in the West End.

Although financial reporting in the sector has moved on since 2001, a number of factors have caused us to take up the debate once more, this time right across the quoted media sector:

- the introduction of IFRS, and with it the development of segmental reporting and the requirements of accounting for business combinations
- convergence across the media sector
- the development of the digital economy.

The sector has come a long way from the days when the revenue policy of many media companies read: ‘turnover

comprises the value of goods and services invoiced to customers net of credit notes and value added tax’. It still has a long way to go though. Accounting policies are too often lazily drafted, without enough thought being given to the reader of the financial statements. We would ask all companies and their advisers to think more about the reader of financial statements and how to get across to those readers the inherent differences between the media sector and other sectors.

Where does the media sector go next? There is much to be done in the area of business combinations. The gap in understanding between the City and the West End still exists, and it is up to all of us in the frontline of financial reporting to work to close that gap.



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Introduction and key findings

After over a decade of discussion, anticipation and false starts, convergence in the media sector is finally happening. As audio, televisual, publishing and advertising businesses fight for space on the internet (well – not so much space; more like brand awareness in the ever-growing community that makes up the web), their business models twist and turn as they repackage and reinvent their offerings to grab the attention of the consumer within the marketing battleground that the internet has become.

The media sector is still characterised by its diversity, both in terms of company size and business activity. Even with the advance of digital media, traditional activities still dominate the revenues and profits of most businesses in the sector and despite the advent of convergence, these are still significantly different from each other so as to deserve segmentation.

It is questionable whether such segmentation will still be relevant in five years' time, but for now we have split the quoted UK media sector into three principal business areas in an attempt to improve comparability: audio & televisual, publishing & events and advertising & marketing services.

Audio & televisual – these are businesses that derive their revenues from the origination, development and exploitation of films, music, television and radio programming.

Publishing & events – these are businesses that derive their revenues from the origination, development and exploitation of both online and traditional print media such as newspapers, magazines and books, together with the closely related activities of conference, exhibition and event organisation and promotion.

Advertising & marketing services – these businesses derive their revenues by attracting public attention to the products or businesses of their clients, through paid announcements in the print, broadcast, or online media and/or provide many other ancillary services such as market research, public relations advice, direct mailing or sponsorship.

Other – certain media businesses do not fall in the first three sectors. Companies in this group include the toys and games company The Character Group, artist representation group First Artist Corporation and emerging digital companies, such as ASG Media Group. We have not analysed this group as it is small and diverse, so comparison would not be particularly useful in our survey.

Many companies have areas of overlap between the sub-sectors. Our analysis is based on a subjective view of the best fit of the companies' activities based upon the information contained in their published annual reports.

Table 1. Analysis of companies in survey

	Total sector market cap at 18.1.10	Number of companies on AIM	Number of companies on full list	Number of companies delisted or no longer trading at 18.1.10	Total number of companies included in survey
Sub-sector	(£'000)				
Audio & televisual	12,971	28	6	3	37
Publishing & events	22,321	5	19	2	26
Advertising & marketing services	9,933	27	7	10	44
Other	158	12	0	4	16
Total	45,383	72	32	19	123

Findings

Market size

As at January 2010, the market capitalisation of quoted companies in the media sector totalled c.£45bn across 104 businesses. Nine companies (8.7%) had a market capitalisation of over £1bn each, and accounted for over 85% of the value. At the other end of the spectrum, 42 companies (40.4%) had a market capitalisation of less than £10m each and accounted for 0.3% of the total market value. This puts the giants in the sector on average over a thousand times larger than the minnows. Excluded from this survey are other companies such as the state-controlled BBC and overseas-controlled Channel Five, together with a good deal of the national daily newspapers as they are either privately or overseas owned.

Research

To capture a representative sample of UK companies reporting under IFRS we extracted our population from the Hemscott database and the Financial Times 'media' companies categories. Several companies were excluded on the grounds that they more resembled leisure, hard technology, or printing companies. All qualitative and quantitative information was taken from the latest financial statements or annual reports publicly available at 1 August 2009. Information with respect to acquisitions was taken from up to the last three years' publicly available financial statements or annual reports (dependent on the level and significance of M&A activity).

In January 2010 we revisited the accounting policies disclosed in these companies' most recent annual reports to ensure any change of policy was captured.

Definitions

It is important to clarify some definitions at this stage to avoid ambiguity when references to Business combinations, Intellectual property, Intangible assets and Non-current assets are used.

Non-current assets (or fixed assets as they are commonly referred to) are those items an enterprise either creates or purchases that are intended for use on a continuing basis in the company's activities. Non-current assets normally comprise investments (interests purchased in other businesses), property plant & equipment and intangible assets. **Intangible assets** are assets without physical substance, such as intellectual property rights ('IP rights').

Table 2. Stratification by market capitalisation at 18 January 2010

Market cap £	Number of companies	% of companies	Total market cap £m	% of Market cap
> 1bn	9	7.3%	39,453	87.0%
> 100m	13	10.6%	4,278	9.4%
> 50m	10	8.1%	735	1.6%
> 10m	30	24.4%	777	1.7%
< 10m	42	34.1%	140	0.3%
Delisted/No longer trading	19			
Total	123	84.5%	45,383	100%

The World Intellectual Property Organisation defines Intellectual Property ('IP') as follows:

IP refers to creations of the mind: inventions, literary and artistic works, and symbols, names, images, and designs used in commerce.

IP is divided into two categories:

- Industrial property, which includes inventions (patents), trademarks, industrial designs, and geographic indications of source; and
- Copyright, which includes literary and artistic works such as novels, poems and plays, films, musical works, artistic works such as drawings, paintings, photographs and sculptures, and architectural designs

Rights related to copyright include those of performing artists in their performances, producers of phonograms in their recordings, and those of broadcasters in their radio and television programmes. (source: <http://www.wipo.int/about-ip/en/>).

IP rights can be obtained in three ways – through internal generation, by purchase from third parties, or through business combinations. IP rights arise through business combinations in many sectors, not just media – so what makes the media sector different?

In the media sector companies are built on the investment in, the creation and exploitation of, and the buying

and selling of IP rights. Media companies have to deal with accounting for IP rights every day – it is core to their business. Our chapter on IP rights deals with rights either internally generated or acquired outside of business combinations.

Our chapter on business combinations deals with IP rights recognised at the point of a business combination (as part of the intangible asset measurement criteria).

IFRS 3 'Business combinations' definitions:

Business – An integrated set of activities and assets conducted and managed for the purpose of providing:

- a. a return to investors; or
- b. lower costs or other economic benefits directly and proportionately to policyholders or participants.

A business generally consists of inputs, processes applied to those inputs, and resulting outputs that are, or will be, used to generate revenues. If goodwill is present in a transferred set of activities and assets, the transferred set shall be presumed to be a business.

Business combination – the bringing together of separate entities or businesses into one reporting entity.

Goodwill – future economic benefits arising from assets that are not capable of being individually identified and separately recognised.

Intangible asset – intangible asset has the meaning given to it in IAS 38 Intangible Assets, ie an identifiable non-monetary asset without physical substance.

Areas of focus

Chapter 1 Business combinations

When we started this survey it became apparent that the area of business combinations covered by IFRS 3 was throwing up some interesting interpretations and issues in respect of the valuation of intangible assets. Consequently we have included a section reviewing the allocation of purchase consideration in business combinations.

Chapter 2 IP rights

Our previous surveys found some inconsistencies between the tangible, intangible or inventory classifications of IP rights. Innovative policies for the recognition and amortisation of IP rights are being developed as companies continue to strive to more accurately report how their media-related assets are being created and ‘consumed’; the increased disclosure of companies reporting under IFRS provides a sound base on which to investigate this.

Chapter 3 Revenue recognition and segmentation

The transition to IFRS did not significantly alter revenue recognition practices, but it still warrants an update in terms of what companies are disclosing under IFRS and further debate in terms of the disparities between what appear to be similar companies. There is a greater emphasis placed on segmental information under IFRS and by the Financial Reporting Review Panel. Consequently, we have also performed an analysis of the multitude of segmental analyses companies are reporting. This is an interesting area, given the disparities between what appear to be like-for-like businesses.



Key findings

Business combinations

The area of business combinations needs the most urgent attention from companies and their advisers and, failing this, from the regulators.

The market capitalisation of the quoted UK media sector is £40bn-£50bn (depending upon when you look). This survey looks at 132 deals in the sector across a 2-3 year period. The value of the intangible assets (including goodwill) of these deals was £11.3bn. This is a significant sum and underlines the importance of having robust measurement procedures in place

to deal with intangible asset valuations when business combinations occur.

In January 2010, the Financial Reporting Council published a study of accounting for acquisitions, where they looked at 20 acquisitions across all industry sectors that had been completed in 2008. Among their conclusions, they said: 'Overall, the results were disappointing. In some cases it was difficult to identify the required accounts disclosures and in other cases the information provided in the business review and the audited accounts was either insufficient or inconsistent.'

The media industry is more likely than most to have intangible assets forming a significant proportion of purchase consideration, due to its reliance on

people and content. This survey shows that in these relatively early days of IFRS there is a great deal of inconsistency across the sector in the approach to fair valuing intangible assets at the point of acquisition.

Further guidance is being developed:

- IFRS 3 has been revised and will come into force for June 2010 year ends
- The IASB issued an exposure draft on fair value measurement in May 2009 which is due to be finalised in 2010
- The International Valuation Standards Council has issued an exposure draft addressing the determination of the fair value of intangible assets for IFRS reporting purposes which is expected to be finalised in 2010

Finally, companies' fair value calculations will face a more robust objective challenge from their auditors following the introduction of new International Auditing Standards in 2010.

Advertising & marketing services companies have by far the lowest proportion of intangible assets identified under the requirements of IFRS 3. This comes as no surprise as this sub-sector is not as rich in cash-producing content as either the audio & television or publishing & events sub-sectors.

However, it is surprising that of the 73 deals we looked at in this sub-sector, 50 deals had little or no intangible assets separately identified at the point of acquisition. Statistics like this highlight the need for further guidance, and further action.



For the sake of the future credibility of the sector, this matter should be addressed sooner rather than later. Is it time perhaps for finance directors within the sector to organise a research group to look at intangible valuation and develop a unified approach for media companies? The disparities across what seem like similar acquisitions are just too great.

Rights

The treatment of the recognition of intellectual property rights relating to content on the balance sheets in each sub-sector could hardly be more different. Structurally, advertising & marketing services businesses do not develop much in the way of content, but do have brand value, people value and process value. Under IFRS, there is little to capitalise on a day-to-day basis, and fair value is only recognised on balance sheet at the point of business combination.

What of publishing & events? Much of the value of newspapers, magazines and online publications relates to titles rather than the content therein. Although the content of the publication is crucial to the ongoing success of the title, the value resides within the title rather than the content. IFRS does not permit capitalisation of costs relating to brands or titles, so once again there is very little value on balance sheet for

these items except at business combination time.

In contrast, it is relatively easy for audio & televisual producers to capitalise their internally generated content as intangible assets since the introduction of IFRS, although this is something that will not be replicated in IFRS for SMEs. The difference in capitalisation of intangibles across the sector makes it difficult to compare balance sheets across the sub-sectors and calls into question the value to the user of the balance sheet as a primary financial statement. Far better perhaps to focus on the income and cashflow statements.

Revenue

Segmental analysis draws the most comment from us. The new standard IFRS 8 presents a great opportunity for all companies to improve cross – referencing between the business review at the front of financial statements, the segmental analysis in the body of the financial statements and the accounting policy on revenue recognition.

There are no significant issues in the sector regarding the timing of revenue recognition, although this may become an issue in the future as content is exploited in increasingly diverse methods through digital distribution. Only time will tell.



Chapter 1

Business combinations



The background

One of the characteristics of the media sector is that it comprises ‘people’ businesses which tend to own a lot of IP – from films and programmes to magazine titles and brands. When one media business acquires another, a greater part of the price paid for the acquisition tends to relate to intangible assets and goodwill rather than tangible assets.

In the UK, IFRS extended the concept of analysing purchase consideration beyond the traditional fair valuation of assets and liabilities covered by UK standards.

IFRS 3 ‘Business combinations’ and IAS 38 ‘Intangible assets’ contain provisions mandating the fair valuation of a wide range of identifiable intangible assets in a business combination.

As noted above, this is of particular significance to the media sector and includes the following types of assets:

IFRS 3.BC101

‘...the Board remained of the view that the usefulness of financial statements would be enhanced if intangible assets acquired in a business combination were distinguished from goodwill, particularly given the Board’s decision to regard goodwill as an indefinite-lived asset that is not amortised. The Board also remained concerned that failing the reliability of measurement recognition criterion might be inappropriately used by entities as a basis for not recognising intangible assets separately from goodwill.’

Marketing-related intangible assets

- Trademarks, trade names, service marks, newspaper/magazine mastheads
- Internet domain names
- Non-competition agreements

Customer-related intangible assets

- Customer lists (n)
- Order or production backlog
- Customer contracts and related customer relationships
- Non-contractual customer relationships (n)

Artistic-related intangible assets

- Books, magazines, newspapers and other literary works
- Musical works such as compositions, song lyrics and advertising jingles
- Pictures and photographs
- Video and audiovisual material, including motion pictures or films, music videos and television programmes

Contract-based intangible assets

- Licensing, royalty and standstill agreements
- Advertising, management, service or supply contracts
- Operating and broadcast rights
- Employment contracts

Technology-based intangible assets

- Patented technology
- Computer software
- Unpatented technology (n)
- Databases (n)

Most of these assets arise as a result of contractual benefits – deals that the companies have done to acquire or develop content, rights or orders that can be exploited in the future for the financial benefit of the companies. Valuation of these assets, while not easy, is achievable and is normally based upon the companies’ assessment of the future cashflows to be derived from exploiting the assets.

The assets annotated (n) above are non-contractual. IFRS 3 and IAS 38 require these assets to be separable and capable of measurement in order to be fair valued for acquisition accounting purposes. We have looked at these types of assets in more detail in the section headed ‘Interpretation stretch’ below.

The deals

We looked at all material acquisitions reported by the companies included in our survey in their financial reports over the last 2-3 years – this gave us a total of 132 acquisitions as summarised in Appendix 2.

We looked at the total consideration relating to intangible assets, and noted how this was split between Identified Intangible Assets (IIA) and goodwill, where the goodwill figure is the residue of consideration paid that is not separately identifiable, yet considered by management to have a value. In the UK quoted media sector, purchases of intangible assets across a two-year period totalled £11.3bn, around

20%-25% of the total sector market cap of between £40bn-50bn.

In table 3 below, the amounts for IIAs and goodwill on each deal have been aggregated into three bands – total intangible value up to £25m, £100m and over £100m, and split across the sub-sectors.

There are three extreme acquisitions in this group, however, each of which involved a total intangible value of 3-4 times the value of the next highest deal

in the sample. These were Reed's acquisition of Choicepoint Inc (£2.63bn of intangibles, of which £1.16bn was goodwill and £1.47bn was IIAs), Yell's acquisition of Telefonica Publicidad (£2.46bn of intangibles, of which £1.32bn was goodwill and £1.14bn was IIAs) and WPP's acquisition of TNS (£1.85bn of intangibles, of which £1.32bn was goodwill and £0.53bn was IIAs). These three 'super deals' accounted for £6.9bn of intangibles, 62% of the total.

Table 3. Deal value of intangibles stratified across sub-sectors

Total intangibles	Number of deals	£m Total intangibles	£m Goodwill	£m IIA	IIA%
AUDIO & TELEVISUAL					
£0-£25m	12	120	50	70	58%
£25m-£100m	4	129	79	50	39%
over £100m	1	109	104	5	5%
	17	358	233	125	35%
PUBLISHING & EVENTS					
£0-£25m	20	153	77	76	50%
£25m-£100m	12	534	318	216	40%
over £100m	8	2,344	1,148	1,196	51%
	40	3,031	1,543	1,488	49%
ADVERTISING & MARKETING SERVICES					
£0-£25m	65	452	396	56	12%
£25m-£100m	5	186	149	37	20%
over £100m	2	304	224	80	26%
	72	942	769	173	18%
TOTAL	129	4,331	2,545	1,786	41%
EXCLUDED DEALS					
over £100m	3	6,945	3,611	3,335	48%
	132	11,276	6,156	5,121	45%

The advertising & marketing services sub-sector was the busiest, with 72 deals, but publishing & events carried the highest total intangibles value, at £3bn. We then summarised the IIA as a percentage of total spend on intangibles by sub-sector and deal size.

Table 4. % of total intangible spend relating to identified intangibles

Range £m	Deals	Audio & televisual	Publishing & events	Advertising & marketing services
0-25	97	58%	50%	12%
25-100	21	39%	40%	20%
100+	11	5%	51%	26%
	129	35%	49%	18%

In the publishing & events sub-sector, about half of the intangible spend is separately identified and disclosed. This is reasonably consistent across the deal size range, with the mid-size acquisitions a little lower at 40%.

In the audio & televisual sub-sector the story is similar. On average almost half of intangible consideration is identified for all deals up to £100m. There is one deal in the £100m+ range, BSKyB's acquisition of Amstrad, where identified intangibles were only 5% of the total.

This deal was more about hardware (set top boxes) than content, and is not typical.

The advertising & marketing services sub-sector has an identified intangibles rate of only 18%, between one-third and one-half of the other two sub-sectors. We believe that this is due to a number of factors, principally 'Content v Contacts' and 'Interpretation stretch'.

Of course the whole media industry relies on its people to a great extent, but advertising & marketing services companies do not have the long-tail benefit of exploitable Content sitting on the shelf.

Content v Contacts

IP in media is more prevalent in the audio & televisual and publishing & events sub-sectors than in advertising & marketing services. This is due to the incidence of the various forms of Content such as programmes, films and books. The value in the creation and exploitation of Content underpins the value of entities in these sub-sectors.

In contrast, the advertising & marketing services sub-sector has no Content to exploit. Rather, its IP lies within its

brands and operational strengths. It relies on the quality of its people, particularly at the account management and creative levels, and the strength of their client relationships – their contacts. Of course the whole media industry relies on its people to a great extent, but advertising & marketing services companies do not have the long-tail benefit of exploitable Content sitting on the shelf.

Consequently, we would expect to see a high level of identifiable intangibles in

respect of Content in the televisual, audio and publishing businesses, compared with the advertising & marketing services sector.

In the absence of Content, what other identifiable intangibles do advertising & marketing services businesses have that differentiates one from another in terms of value? We explore this point in more detail in the sample analysed later in the chapter.

Interpretation stretch

In the early days of the implementation of any new accounting standard that differs significantly from its predecessor, there is a period of innovative interpretation when companies deal with the adoption of the standard for the first time.

The approach tends to be (a) understand the thrust of the new standard and evaluate its potential range of effects on the results of the business; (b) look to see how others have interpreted the standard; and (c) interpret the standard in the most beneficial way for the company in the light of (a) and (b). Whether this will capture the spirit of the particular standard, and lead to companies taking a common approach as to its interpretation depends upon how well the standard has been written. When loosely worded, standards can be capable of a wide degree of interpretation across different companies.

As a rule of thumb, the degree of Interpretation stretch will correspond to the degree of ambiguity within the wording of the standard.

Within IFRS 3 there is a wide area of interpretation as to what can be considered a separately identifiable intangible asset. This is particularly true in the relatively newly identified area of non-contractual relationships.

IFRIC (the International Financial Reporting Interpretations Committee) have been debating the topic, and in particular the subtleties of the difference between contractual and non-contractual

customer relationships. The topic has been batted about in the UK and across the Atlantic with our American cousins, all in the cause of international accounting convergence. As at August 2009, the problem of interpretation of recognition, first looked at as a commercial issue seeking a pragmatic solution, appears to have been shunted into a sub-committee siding.

Notes from IFRIC staff meetings include the following helpful comments:

'Valuation practitioners and companies have often asserted that customer relationships are difficult to measure reliably separately from goodwill and hence, they may not have been separated under the previous version of IFRS 3, which included an exception for reliable measurement.

The staff discussed with several valuation practitioners in the US and UK their experiences with non-contractual customer relationships. Though informal, some of the experiences shared with the staff include the following:

- a. intangibles of significant values typically include trade names and contractual customer relationships (income valuation approach);
- b. customer lists are of little value (cost replacement valuation approach), and non-contractual customer relationships (residual income valuation approach) are uncommon and not significantly valued;
- c. a customer loyalty program was cited as an example of non-contractual customer relationship but mixed views on the value;
- d. 'depositor' relationships and related deposit liabilities are not sold as a single asset group outside of business combinations;
- e. 'pay-as-you-go' mobile customers are non-contractual but is that a relationship if mobile providers typically do not know the identity or contact details of the customers;

- f. when non-contractual customer relationships are identified, often the entity has insufficient information for valuation to recognise them separately from goodwill.

IFRS 3 Business Combinations (as revised in 2008) requires an acquirer to recognise the identifiable intangible assets of the acquiree separately from goodwill. An intangible asset is identifiable if it meets either the contractual-legal criterion or the separable criterion in IAS 38 Intangible Assets.

Customer-related intangible assets may be either contractual or non-contractual. Contractual customer relationships are always recognised separately from goodwill as they meet the contractual-legal criterion. However, non-contractual customer relationships are recognised separately from goodwill only if they meet the separable criterion. Consequently, determining whether a relationship is contractual is critical to identifying and measuring both separately recognised customer relationship intangible assets and goodwill, and different conclusions could result in substantially different accounting outcomes.

The IFRIC concluded that how the relationship is established helps to identify whether a customer relationship exists but should not be the primary basis for determining whether the acquirer recognises an intangible asset. The IFRIC noted that the criteria in paragraph IE 28 might be more relevant. The existence of contractual relationships and information about a customer's prior purchases would be important inputs in valuing a customer relationship intangible asset but should not determine whether it is recognised.

In the light of the explicit guidance in IFRS 3, the IFRIC decided that developing an Interpretation reflecting its conclusion is not possible. Noting widespread confusion in practice on this issue, the IFRIC decided that it could be best resolved by referring it to the IASB and the FASB with a recommendation to review and amend IFRS 3 by:

- removing the distinction between ‘contractual’ and ‘non-contractual’ customer-related intangible assets recognised in a business combination; and
- reviewing the indicators that identify the existence of a customer relationship in paragraph IE 28 of IFRS 3 and including them in the standard.’

The Interpretation stretch resulting from the lack of clarity ranges from some advertising & marketing services entities carrying out a comprehensive review in the spirit of the standard and identifying a number of intangible assets other than goodwill, to others that have come to the conclusion that nothing can be separately identified from goodwill.

One fear that companies might have is that identifying an intangible asset relating to, say, contractual customer relationships might lead to that asset being amortised over a relatively short period compared with leaving the same amount in goodwill and carrying it forward indefinitely (subject to impairment).

Thus, separate identification of an IIA would lead to a weaker annual result due to the effect of the amortisation change. Part of the argument supporting the assertion of indefinite-life goodwill as opposed to systematic amortisation concerns the replacement effect of subsequent spend. When the IASB revisited IAS 38, they asked ‘why amortise goodwill when you will regularly incur P&L spend to maintain/replace it post acquisition?’. After all, this would lead to a double whammy of the income statement charge of goodwill amortisation together with its cost of maintenance. They concluded, that goodwill should be deemed to have an indefinite-life (ie no foreseeable limit to the period the CGU generates cash inflows) and should be checked for impairment each year.

Should this logic not also be applied to all other intangible assets? Is it inconsistent to treat the intangible asset ‘goodwill’ differently to other intangible assets such as customer relationships? The annual spend on maintaining relationships is written off to P&L annually; why not then simply subject the originally purchased asset to an annual impairment test, as with goodwill?

Alternatively, should the logic of allowing the existence of indefinite-life assets, such as goodwill, be critically examined once more? On balance we would favour this latter course. Under IAS 38.88-96, where there is ‘no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the entity’ then it can be treated as an indefinite-life intangible, which similarly to goodwill is not amortised and is annually tested for impairment. The only limiting factor here is that the useful life of intangibles that arise from contractual rights should be restricted to the term of the contractual life (IAS 38.94). However, non-contractual relationships could quite possibly have longer lives than contractual ones, on the basis that contracts will normally be finite. Non-contractual relationships can exist for decades.

Alternatively, should the logic of allowing the existence of indefinite-life assets, such as goodwill, be critically examined once more?

Residual goodwill and 'synergies'

The basis of conclusions section in IFRS 3 gives some view on what goodwill actually represents and refers several times to 'synergies'.

'Synergies' is a term widely used in practice to describe expected benefits from combining an acquired group of assets or a business with an existing business. These are deemed to include (for example):

- additional revenues from marketing the acquirer's products and services to the acquiree's customers (cross-selling)
- cost savings and economies of scale from integration of operating facilities
- defensive synergies, such as preventing a competitor from gaining a dominant market share.

It seems like it should be easy... acquire a company, combine its revenues with ours and not only rationalise overhead, but also realise additional potential synergies between people, processes, and systems, and the sum will be greater than the two parts. Before the acquisition, buyers carry out detailed due diligence, making estimates of those synergies which influence the price the buyer is ultimately willing to pay. The reality, however, is that the savings tend not to be as great as expected.

There is still a case to be answered as to whether:

- i. synergies materialise in practice and are therefore justifiable as a basis on which to support goodwill?
- ii. synergy assumptions are sufficiently defined and properly tested during goodwill impairment appraisals

'What is goodwill? IFRS 3.BC130/131/135

...the Board observed that when goodwill is measured as a residual, it could comprise the following components:

- a. the fair value of the 'going concern' element of the acquiree... that value stems from the synergies of the net assets of the acquiree, as well as from other benefits such as factors related to market imperfections, including the ability to earn monopoly profits and barriers to market entry
- b. the fair value of the expected synergies and other benefits from combining the acquiree's net assets with those of the acquirer. Those synergies and other benefits are unique to each business combination, and different combinations produce different synergies and, hence, different values
- c. overpayments by the acquirer
- d. errors in measuring and recognising the fair value of either the cost of the business combination or the acquiree's identifiable assets, liabilities or contingent liabilities, or a requirement in an accounting standard to measure those identifiable items at an amount that is not fair value.

The Board observed that the third and fourth components conceptually are not part of goodwill and not assets, whereas the first and second components conceptually are part of goodwill. The Board described those first and second components as 'core goodwill', and focused its analysis first on whether core goodwill should be recognised as an asset.

The Board concluded that goodwill acquired in a business combination and measured as a residual is likely to consist primarily of core goodwill at the acquisition date, and that recognising it as an asset is more representationally faithful than recognising it as an expense.'

- (required at each reporting date)? and consequently;
- iii. it is right to carry an asset on the balance sheet (goodwill) at all on the basis that it represents 'synergies'?

IAS 38 dictates that intangible asset valuations should already be taking account of synergies to the extent that they increase the amount that a knowledgeable, willing buyer would pay for an asset if acquired separately. This applies even if the actual acquirer does not expect to receive those benefits. So the availability of synergies (cross-sell potential for example) might affect the fair value of an asset. In summary, if those synergies are

- (i) intrinsic to the asset and (ii) available to more than one buyer, they should form part of the intangible asset valuation, not goodwill.

In contrast, synergies or other factors that are unique to the specific acquirer or transaction should not be taken in to account during intangible asset valuations and should form goodwill.

IFRS 3.66 does not help, with only light disclosure requirements in this area: 'a description of each intangible that was not recognised separately from goodwill and an explanation of why the fair value could not be measured reliably'. In this respect, we believe companies

should be disclosing exactly what ‘specific, unique synergies’ goodwill represents, and making it clear to the reader the sources of value underlying goodwill. This should be happening behind the scenes in any case – the value of the various identified components of goodwill should be determined in terms of future cashflows, discounted at an appropriate weighted cost of capital and then form the basis of allocation of goodwill to CGUs.

At business combination time, it seems that the standards make it too easy for companies to assert that the IAS 38 criteria for intangible asset recognition is failed (normally on the separability criterion), recognise the entire difference between purchase consideration and the fair value of net assets as goodwill (carrying an indefinite-life), and declare that goodwill simply represents ‘synergies’ – is that really the best we can do? Are shareholders really being given

the full story? The process of evaluating goodwill compels management to identify and quantify the sources of cashflows that go on to support the value of goodwill. If this is a struggle and the assumptions about cashflows are unrealistic or indefinable, not only does it suggest an overpayment but it might also erode value as a lack of measurability leads to a lack of attention by management in the areas previously identified as representing ‘synergies’.

Given the above requirements of IAS 38 and IFRS 3, in each case where ‘synergies’ is disclosed as the description of what goodwill represents, it must mean that they are completely unique to that specific acquirer and/or they are not separately identifiable. Given the lack of detail in IAS 38 with respect to disclosing the nature of what goodwill represents, we did not expect to see meaningful disclosure in this area. We’ll let the analysis do the talking...

“

The process of evaluating goodwill compels management to identify and quantify the sources of cashflows that go on to support the value of goodwill.

”

Analysis of business combinations

Audio & televisual companies analysis

There was significant acquisition activity in this sector during 2007 and 2008, and on the whole the major audio & televisual companies made a sound attempt to value the intangibles acquired with these businesses.

Shed Media acquired Outright, Twenty Twenty and Wall to Wall in 2007 – the difference between the combined purchase price and the combined tangible net assets was £47.3m. Shed allocated £13.7m (29%) of this to intangible assets – £5.1m of trademarks to be amortised over five years, £6.1m of customer relationships amortised over ten years and £1.3m and £1.2m respectively for backlog and recommissions amortised over two years. This left £33.6m of goodwill recognised across the three acquisitions, which was described as being attributable to operational synergies and future earnings potential.

RDF Media acquired Presentable, The Foundation and Comedy Unit in 2007, allocating £13.6m (64.2%) of the £21.2m difference between the combined purchase price and the combined tangible net assets to intangible fixed assets. They too are amortising customer relationships over ten years but are also amortising trade names over ten years. The purchase price (£0.7m) of their acquisition in 2008 – History Rights Limited – was allocated 100% to IP rights. RDF also note goodwill being attributable to operational synergies.

Also in 2007, **DCD Media** acquired September Films, Prospect Pictures and West Park Pictures. They valued the combined trademarks at £9.8m (43.6%) with the balance (£12.6m) recognised as goodwill. DCD did not appear to capitalise customer relationships, IP rights, or contracts. DCD instead noted that goodwill represented the future benefit the group expects from the expertise of the company and the industry contracts that will provide synergies with other group companies.

It is amortising the capitalised trademarks over ten years also. The other big acquisition in the television production world in 2007 was that of 12 Yard by **ITV**. Perhaps because ITV is a broadcaster it did not recognise any value with respect to 12 Yard's relationships with other broadcasters – we might expect these to be of significantly less value to the business subsequent to the acquisition. An order backlog of £4m was recognised with the remaining £31m recognised as goodwill attributed to, rather generically (a recurring theme here), the synergies the acquisition would bring to the group.

Other activity in this sector included **UTV Media's** acquisition of Tibus, the web and content management business, and of FM104, the Dublin based radio station. UTV did not separately value any intangible assets when acquiring Tibus, but disclosed that within the £3.8m of goodwill recognised:

'there are certain intangible assets that cannot be individually separated and reliably measured from the acquiree due to their nature. These primarily relate to the expected value of synergies arising from the integration of Tibus with the Group's existing new media business and the wider strategic benefits of the acquisition to the Group.'

Table 5. The super-indies acquisitions

	Shed Media £m		DCD Media £m		RDF Media £m	
Backlog/Order book	1.3	9%	–	0%	1.7	13%
Recommissions/IP rights	1.2	9%	–	0%	1.0	7%
Customer relationships	6.1	45%	–	0%	7.7	57%
Trademarks	5.1	37%	9.8	100%	2.2	16%
Other	–	0%	–	0%	1.0	7%
	13.7		9.8		13.6	
Goodwill	33.6		12.7		7.6	
Total intangibles acquired	47.3		22.5		21.2	
Identified intangible assets %	28.9%		43.6%		64.2%	

When acquiring FM104, UTV separately valued a radio licence at £37.2m. It also stated that included in the £12.9m of goodwill recognised were certain intangible assets that could not be individually separated and reliably measured. Disclosure noted that:

'these primarily relate to the expected value of synergies arising from the integration of FM104 with the Group's existing radio business in Ireland enabling the Group to offer an enhanced urban access package to advertisers.'

We would have expected separately identifiable brand names and trade marks to have had some value.

None of these companies capitalised non-compete agreements that may have been acquired with the businesses.

Boomerang and **Galleon Holdings** both capitalised non-compete agreements in 2008 (the former amortising over two years).

Furthermore, Boomerang split the customer relationships they acquired into 'contractual' and 'non-contractual' – adopting an indefinite useful life policy on their non-contractual customer relationships identifying them as:

'key to the long term of the business.'

This is an interesting point given that the commissioning process and the way in which televisual content is delivered (through traditional broadcasters) is likely to change substantially over the next ten years. Given these uncertainties, we question whether relationships with existing broadcasters can indeed have an indefinite-life.

Other points of note include **Eros International's** recognition of the 'Eros' trade name (\$14m) when the group came together (via business combination) in 2006 – they considered it to have an indefinite economic life because of the:

'institutional nature of the corporate brand name, its proven ability to maintain market leadership and the Group's commitment to develop and enhance its value.'

BSkyB's purchase of Amstrad in 2008 for £127m created £5m of intangibles and £104m of goodwill, but there was no comment in the accounts as to what the intangibles or goodwill related to at all.

There are several aspects of the acquisition by **HandMade** of HandMade Holdings Limited in June 2006 that are of interest, as this is a transaction that was originally dealt with under UK

GAAP in the 2006 financial statements and then restated in 2007 in accordance with IFRS. The disclosure made surrounding the acquisition and the change in the 2007 financial statements is comprehensive.

The opening part of the Acquisitions note in 2007 reads:

'There were no acquisitions during the year. Below are details of the two acquisitions which took place during 2006. On 9 June 2006 Equator Group plc acquired 100% of the voting equity shares of HandMade Holdings Limited. Following the acquisition Equator Group plc changed its name to HandMade plc. Equator paid consideration fair valued at £24,759,000 via cash, the issue of new shares and a convertible loan note (see below).

The fair value of the assets and liabilities acquired from HandMade Holdings Limited, and adjustments from book value which were necessary when accounting under IFRS are set out in the following table:

Table 6. HandMade – extract from 2007 financial statements – fair value of assets and liabilities acquired

Fair value	Book value £'000	Adjustment £'000	Fair value £'000
Intangible assets – (see note 10)	7,727	24,209	31,936
Debtors	773	–	773
Cash	1	–	1
Loan	(6,483)	–	(6,483)
Creditors	(1,468)	–	(1,468)
Deferred tax liability – (see note 18)	–	(9,581)	(9,581)
Net assets	550	14,628	15,178
Fair value of consideration paid	£'000		
Shares issued on acquisition	16,000		
Convertible loan note	1,790		
Deferred consideration	6,405		
Costs of acquisition	564		
Total consideration	24,759		

The above fair values generated goodwill on acquisition of £9,581,000.

This shows that a deferred tax liability of almost £10m was recognised on this acquisition. The following extract from the Business Review of the Directors' Report helps explain this:

'...Deferred tax has been provided using the balance sheet liability method, recognising all temporary differences. The impact of this has been to recognise a deferred tax liability in respect of intangible assets. The liability is released to the income statement over the period over which the assets are amortised. Where the creation of this liability relates to an intangible asset acquired as part of a business combination (see below), an equal and opposite adjustment is posted to increase goodwill arising on the business in question. This adjustment to goodwill is not amortised, but is subject to an annual impairment review... Goodwill of £11.75m (2006 – £12.16m) is held as an asset in the Balance Sheet at the year end. £10.32m of this balance arose to reflect the deferred tax liability that was recognised in respect of the intangible assets acquired with HandMade and Sequence in 2006, as explained in the opening section of this review which discusses the impact of IFRS on the financial statements... Under IFRS, goodwill is not amortised, but is subject to an annual impairment test. Following analysis of the goodwill balance, no impairment was required.'

The deferred tax liability arose through the use of the balance sheet liability method on the business combination, and will unwind over the asset amortisation period. When the liability is set up, an 'equal and opposite adjustment was posted to goodwill', that is to say, an asset of £10.3m was created to offset the creation of the tax liability. Note 9 in respect of goodwill says:

'...As discussed previously in the financial review in the Directors' report, £10,320,000 of the above goodwill is created when a deferred tax liability is recognised in relation to the intangible assets acquired with HandMade Holdings Limited and Sequence Film Limited in 2006.'

In other words, it had to create £10.3m of goodwill because it had to create £10.3m of deferred tax liability, as a result of increasing the fair value of intangibles by £34.4m (note 10, intangible assets) on acquisition. But having created the goodwill out of nothing, it then has to look at its value. It justifies this in note 9 as follows:

'As a result, £9,327,000 of the above goodwill is 'sheltered' by the deferred tax liability disclosed in note 18. Impairment reviews of the intangible assets in respect of which the deferred tax liability is recognised (see note 10) provide comfort over the £993,000 unsheltered goodwill arising due to the deferred tax liability...'

By 'sheltered' it means that it is offset to the tune of £9.3m by the liability that it was set up to cover, leaving the goodwill asset in excess of the deferred tax liability by some £993k. How did this come about? The deferred tax note reads:

'The following are the deferred tax liabilities recognised by the Group and movements thereon during the current and prior periods.'

Fair value gains	£'000
At 1 January 2006	1,170
Arising on business combinations (see note 13)	10,320
Credit to income (note 7)	(425)
Balance at 31 December 2006	11,065
Credit to income (note 7)	(1,738)
Balance at 31 December 2007	9,327

In plain English, the tax liability that was set up as a result of the combination is being unwound by being credited through the income statement, but the asset that was set up as an 'equal and opposite adjustment' is not being written off accordingly.

Instead, the growing difference between asset and liability is being aggregated with the value of the intangibles that led to the creation of the tax liability in the first place. It is then pronounced not in need of impairment!

The intangibles largely come about as a result of the fair value exercise carried out on the HandMade combination. The total value arising from this was £31.9m, of which £11.4m related to the 'Eloise' franchise and the balance to film library. The carrying value of the film library was £23.7m, prior to an amortisation charge of £1.4m, leaving a carrying value of £22.3m at 31 December 2007.

The basis of amortisation of film library intangibles is straight line, 20 years (accounting policies) so the charge looks reasonable. The impairment review in respect of the film library was described as follows (note 10):

Film library

'The relevant recoverable amount for this asset was determined from value in use calculations based on a six year forecast to 31 December 2013 prepared by the management of HandMade plc. The forecast considered the income that management expect to be generated from the Group's film library (comprising over 100 feature films) and also from four feature films which will be produced in the future and which exploit the re-make and sequel rights inherent in the value of the library.

The key assumptions for the value in use calculation are those regarding the discount rate, the value of un-contracted income streams and the timing of the receipt of all income streams. Management estimates discount rates using post-tax rates that reflect current market assessments of the time value of money and the risks specific to each type of income stream. The rates used to discount the forecast were in the range 10% to 50%.

The assumptions relating to income streams and the timing thereof are based on historical data (in the case of the film library only) and on management's estimates and knowledge of the film industry gained from many years of experience.'

Bear in mind that the library is an established library of existing films (with their re-make rights). In considering the future forecast for the six years to 31 December 2013, management no doubt looked at the past performance of the library for each of the two years ended 31 December 2006 and 2007. Quoting from the business segmental information:

For the year ended 31 December 2007 information about these business segments is as follows:

Library	2007 £'000	2006 £'000
Revenue		
– External	827	292
– Internal	(230)	
Total	597	292
Loss before tax	(868)	(862)
Income tax	843	367
Loss for the year	(25)	(495)
NB – after charging amortisation	1,329	900

It is always difficult to forecast the revenues from the sales of new films. Large established libraries, however, tend to have historic sales patterns across many titles, making forecasting somewhat more predictable. Unless previous exploitation had been particularly weak, or a large number of licences were about to expire, readers of the financial statements might have thought that it would be difficult to drive a value of £22.3m out of the library given the historic sales performance disclosed above.

This example illustrates how the increased disclosure requirements of IFRS can highlight areas worthy of further discussion among stakeholders.

Mama Group point out that fair values of intangibles are provisional and explain that the valuations adopted at the point of acquisition will be reviewed and revised in the 12 months following acquisition. In respect of their acquisition of the Angel Music Group, they disclosed that:

'The Group acquired various rights and trademarks relating to certain brands held by companies within the Angel Music Group of companies. These brands included Global Gathering, Polysexual and Godskitchen. These brands are used by this group in festivals and venues, as well as within worldwide sponsorship agreements.

As part of the fair value adjustment to the net book valued acquired, the Group undertook an exercise to value these brand names based on projections produced by the Directors of Angel Music Group. Based on these forecasts the Directors consider that a value of £2.16m to be attributable to the future marketability of these brands. The directors consider that these brands have a useful economic life of 20 years. A fair value has also been attributed to a customer relationship held by the Angel Group of companies which has been calculated at £350,000.'

They are amortising customer relationships over two years.

Advertising & marketing services companies analysis

The advertising & marketing services sector also had considerable M&A activity through 2007 and 2008. The treatment of intangible assets in this sector was markedly different to that of the TV, film and broadcasting sector. A large number of acquisitions had a low value attributed to specific intangibles and a much higher value remained as residual goodwill. A number of companies made a real attempt to recognise intangibles acquired.

Table 7. Companies recognising over 5% of total intangibles as separately identified intangible assets

Company	Acquisition	£m Total intangibles	£m Goodwill	£m IIA	IIA%
Aegis	[14 acquisitions totalled]	151.3	92.2	59.1	39.1%
Centaur	Period Living	1.5	0.1	1.4	93.3%
Centaur	Recruiter	4.0	0.6	3.4	85.0%
Centaur	Pro Talk	5.9	3.2	2.7	45.8%
Digital Marketing Group	Hyperlaunch	3.2	2.0	1.2	37.5%
Digital Marketing Group	Graphico	9.4	6.0	3.4	36.2%
Digital Marketing Group	Scope Creative (Dig for Fire)	8.2	5.6	2.6	31.7%
Digital Marketing Group	Alphanumeric (Jaywing)	14.7	10.3	4.4	29.9%
Digital Marketing Group	HSM Telemarketing	8.0	5.9	2.1	26.3%
Digital Marketing Group	Cheeze	10.3	8.9	1.4	13.6%
Huntsworth	Dorland Corporation	13.0	9.0	4.0	30.8%
Huntsworth	Axis Healthcare	20.5	16.0	4.5	22.0%
Interactive Prospect Targeting Holdings	NP6	6.3	5.0	1.3	20.6%
Interactive Prospect Targeting Holdings	Direct Excellence	0.6	0.5	0.1	16.7%
Interactive Prospect Targeting Holdings	Directinet/J2P2N	21.9	19.6	2.3	10.5%
M&C Saatchi	Clear Ideas/Walker Media	45.7	39.9	5.8	12.7%
Thomson Reuters	[4 acquisitions totalled]	56.0	26.0	30.0	53.6%
Toluna	Speedfacts	4.7	3.2	1.5	31.9%
WPP	Taylor Nelson Sofres	1,858.4	1,132.7	725.7	39.0%
WPP	Others	152.8	132.4	20.4	13.4%
YouGov	Polimetrix	12.6	7.0	5.6	44.4%
YouGov	Psychonomics	20.8	13.3	7.5	36.1%
YouGov	Zapera	12.0	8.5	3.5	29.2%
		2,442	1,548	894	36.6%

Intangible allocations vary widely from 93.3% for **Centaur**'s acquisition of Period Living, to 53.6% with respect to the combined **Thomson Reuters** acquisitions, to an average of 12.8% for the combined **Interactive Prospect Targeting Holdings** acquisitions.

Centaur purchased Period Living, Recruiter and ProTalk in 2006, attributing a high percent to customer relationships and brand names. It chose to amortise brand names over 20 years and customer relationships over ten years. **Aegis** also valued customer relationships in its 2008 acquisitions with an amortisation policy of five years.

Digital Marketing Group appeared to allocate a consistent amount to intangibles for most of its acquisitions and adopts a policy of amortising customer relationships over 8-12 years.

M&C Saatchi amortise its capitalised customer relationships over 1-5 years and brand names over anything from seven years to an indefinite period.

Interactive Prospective Targeting made three acquisitions – none of which had particularly highly valued customer relationships, contracts or brand names – recognising IIAs of 13% combined. Its amortisation policies included customer relationships and trade names over 7-16 years, forward orders between 1-4 years, software over 15 years, website and data costs over three years and licences over 1-5 years. It noted that the goodwill recognised on these acquisitions related to:

'the expansion of current products to the online market and anticipated future synergies.'

Huntsworth valued brands and customer relationships on both its major acquisitions (Dorland Corporation and Axis Healthcare), amortising these over 3-20 years.

Of the research-based companies, **Toluna** separately valued its customer lists (amortised over four years) as well as panel costs (amortised over 1-2 years). It also noted that:

'a significant amount of the value (of the acquisition) is attributable to its workforce and sales knowhow.'

and furthermore, that it was:

'expecting significant synergies from integration into the rest of the group.'

In comparison, **YouGov** amortise customer contracts and customer lists over 10-11 years and consumer panel costs over five years. They too attributed goodwill to:

'anticipated synergies and the value of the workforce acquired.'

WPP's acquisition of research consultants Taylor Nelson Sofres is clearly of interest given its size (£1bn compared to WPP's market cap of £5-6bn), but disclosure was relatively light with respect to intangible allocation. Intangible assets recognised as fair value adjustments included customer relationships, proprietary tools and brands. It states that brands are amortised over anything from 10-20 years or are deemed to have an indefinite-life and that customer related intangibles are amortised over 3-10 years.

Many companies struggled to find few, if any, IIAs

Table 8. Companies recognising under 5% of total intangibles as separately identified intangible assets

Company	Acquisition	£m Total intangibles	£m Goodwill	£m IIA	IIA%
Cello	Market research international	2.2	2.1	0.1	4.5%
Cello	Hill Murray group	3.8	3.7	0.1	2.6%
Cello	2CV	7.9	7.7	0.2	2.5%
Cello	MSI	7.5	7.4	0.1	1.3%
Cello	SMT consulting	8.3	8.3	0	0.0%
Cello	Magnetic advertising	2.4	2.4	0	0.0%
Cello	Farm communications	1.2	1.2	0	0.0%
Cello	Rosenblatt/Digital online people	1.0	1.0	0	0.0%
Cello	Bankbrae	0.9	0.9	0	0.0%
Cello	OMP services	0.3	0.3	0	0.0%
Chime	Fast Track Sales	27.9	27.0	0.9	3.2%
Chime	VCCP and Stuart Francis Whitson	22.8	22.8	0	0.0%
Chime	The Corporate Citizenship company	3.0	3.0	0	0.0%
Chime	De Facto Communications	1.8	1.8	0	0.0%
Chime	Stuart Higgins communications	1.5	1.5	0	0.0%
Chime	Facts International	0.6	0.6	0	0.0%
Creston plc	ICM Research	18.5	17.6	0.9	4.9%
Creston plc	Red Door	7.7	7.5	0.2	2.6%
Creston plc	PAN Advertising	12.5	12.2	0.3	2.4%
Creston plc	Tullo Marshall Warren	27.4	26.9	0.5	1.8%
Ekay	WFCA Integrated	8.5	8.5	0	0.0%
Hasgrove	Pavillion Communications	7.3	7.3	0	0.0%
Hasgrove	Odyssey Interactive	3.3	3.3	0	0.0%
Hasgrove	Politics International	2.5	2.5	0	0.0%
Hasgrove	Amaze	2.4	2.4	0	0.0%
Hasgrove	Cabinet Stewart	1.4	1.4	0	0.0%
Hasgrove	Hailstone Creative	1.0	1.0	0	0.0%
Huntsworth	Grayling International	1.3	1.3	0	0.0%
International Marketing & Sales Group	V+O Communication	14.8	14.8	0	0.0%
International Marketing & Sales Group	Shared Value	10.6	10.6	0	0.0%
International Marketing & Sales Group	Zap	8.1	8.1	0	0.0%
International Marketing & Sales Group	Pragma	6.4	6.4	0	0.0%
International Marketing & Sales Group	Friends	3.5	3.5	0	0.0%
International Marketing & Sales Group	BIP	3.0	3.0	0	0.0%
International Marketing & Sales Group	Tarantula	1.0	1.0	0	0.0%
International Marketing & Sales Group	MAPP & Promer	1.0	1.0	0	0.0%
MKM Group	Leisure World/Leapfrog	5.1	5.0	0.1	2.0%
Optimisa	eq group plc	12.7	12.1	0.6	4.7%
Research Now	Samplenet e-Research Solutions Inc	16.6	16.2	0.4	2.4%
The Mission Marketing Group	Bray Leino	28.8	28.8	0	0.0%
The Mission Marketing Group	RLA	15.0	15.0	0	0.0%
The Mission Marketing Group	April-Six	12.1	12.1	0	0.0%
The Mission Marketing Group	Story UK	10.0	10.0	0	0.0%
The Mission Marketing Group	Bastin Day Westley	9.0	9.0	0	0.0%
The Mission Marketing Group	Big/Fuse	8.4	8.4	0	0.0%
The Mission Marketing Group	Broadskill	1.7	1.7	0	0.0%
The Mission Marketing Group	TMMHL	1.1	1.1	0	0.0%
The Mission Marketing Group	PCM	0.5	0.5	0	0.0%
The Mission Marketing Group	Rhythmm Communications Group	0.4	0.4	0	0.0%
Twenty	Ominor	1.6	1.6	0	0.0%
		358	354	4	1.2%

Cello Group made ten acquisitions over 2006 and 2007, recognising a small value (1%) for customer contracts but no allocation in respect of brand names or non-contractual customer relationships. This resulted in residual goodwill of £35.5m using the ‘synergies’ contention to support each balance. Every acquisition carried identical disclosure:

‘The goodwill arising on acquisition is attributable to the anticipated profitability of the company and future operating synergies from the combination.’

Chime Communications have made six acquisitions since 2005 resulting in £57.6m of goodwill. It recognised a small value for customer relationships on the acquisition of Fast Track Sales. In 2005 Chime disclosed that with respect to its acquisition of VCCP, management carried out a review of intangibles and concluded no value could be ascribed to intangibles on the basis that:

‘the company was only formed in 2002 and [because of] the nature of the contracts.’

It is not clear what is meant by the ‘nature of the contracts’ – further disclosure would have been useful.

Creston chose to adopt an indefinite-life with respect to acquired brands because of their:

‘proven market position and the group’s commitment to develop and enhance their value.’

However, in 2007 Creston paid £24m for ICM Research, £32.1m for Tullo Marshall Warren, and £13.2m for PAN Advertising, but capitalised just £450k as brand names and £1.2m as customer contracts, both of which seem particularly low even taking into account the nature of Creston’s activities. There was no

reference to non-contractual customer relationships in the acquisition note.

Hasgrove made several acquisitions in the period under review recognising £17.9m of goodwill, again with no intangible allocation. Its accounts noted that:

‘the Directors consider that customer relationships are not separable or intangible assets.’

International Marketing & Sales Group

acquired eight businesses in 2007, recognising £48.4m of goodwill and no intangible assets. **Ekay** acquired WFA Integrated in 2008, recognising £8.5m of goodwill and allocating none of the purchase price to intangibles. Neither of these companies made reference to intangible assets at all in their accounts.

In its acquisition of eq group, **Optimisa** capitalised customer contracts and relationships worth just 4.7% of the total intangibles allocation. It states that it amortises contracts over 1-18 months and relationships over:

‘an estimation of the tenure of the relationship at acquisition.’

MKM Group did not mention any intangible allocation in its acquisition of Leisure World, recognising nearly all as goodwill and attributing it to synergies and the benefits of entering into new markets.

In acquiring Samplenet e-Research, **Research Now**, on the other hand, recognised no customer relationships, customer contracts, or brand names, with panel costs of £0.4m being the only intangible asset recognised on acquisition worth £16.9m. Research Now amortise these panel costs over 12 months being the group’s

‘estimated average life of a panellist.’

As a result £16.1m of goodwill was recognised and the group disclosed that:

‘included in goodwill are certain intangibles that cannot be individually separated and reliably measured from the acquiree due to their nature. These included high calibre staff, a reputation for great quality, and the fact the acquisition was a ready made platform for North America.’

In this instance we ask the question that if there is a valuable reputation, then is there not a valuable brand name? And if there is a platform for growth, is there not some value in contractual or non-contractual customer relationships?

The Mission Marketing Group, the integrated communications agency, has made ten acquisitions over the last three years with the difference between the combined purchase price and combined tangible net assets being £87m. This has been recognised in full as goodwill with the only disclosure regarding intangibles allocation being that:

‘management carried out a review to assess whether any intangible assets relating to brand names, customer relationships and contractual arrangements were acquired as part of the transaction. Management concluded that no value could be ascribed to these intangible assets on the basis that other intangibles and goodwill cannot be separately valued reliably, due to the nature of the intangible assets in question.’

Stakeholders might question why other companies in the sector are able to carry out such valuations, whereas their board cannot.

Twenty acquired Ominor in 2007 for £1.3m with £1.6m recognised as residual goodwill and no intangible assets allocated at all. There was no reference in the accounts to intangible assets but it did disclose that:

‘the goodwill is attributable to reputation, customer base and future profitability.’

If the acquired company has a valuable reputation and customer base then it begs the question as to why these weren’t separately valued.

Publishing & events companies analysis

The acquisitions in the publishing and events sector generated a significant, and more consistent, level of intangible allocation – likely to be because of the more tangible nature of the product and service offerings of the companies involved, and (as discussed in the next chapter – IP rights) the lack of previous capitalisation with respect to internally generated IP rights, publishing titles and customer lists.

Table 9. Average identified intangible fixed assets in the publishing & events sub-sector

Company	Average IIAs
Bloomsbury Publishing	58%
Haynes Publishing	63%
Informa	67%
ITE Group	68%
Johnston Press	77%
Moneysupermarket.com	62%
Motivcom	13%
Pearson	47%
Reed Elsevier	57%
Trinity Mirror	35%
United Business Media	26%
Wilmington	49%
YELL	33%

Trinity Mirror made six acquisitions generating £81.1m of goodwill and £56.7m of intangible assets – an average intangible asset allocation of some 35%. The acquisition of Smart Media Services and Financial Jobs Online had intangibles allocated of nearly 50% from the difference between the combined purchase price and the fair value of the tangible net assets. Trinity groups its intangibles into ‘publishing rights and titles’ and ‘customer relationships and brand names’. Its customer relationships and domain name assets are amortised between five and ten years but the following disclosure was made regarding the publishing rights and titles:

‘the directors consider that publishing rights and titles have an indefinite-life due to the historical longevity of the brands and the ability to evolve the brands in the ever changing media landscape. It is not practicable to review individual publishing rights and titles due to the interdependencies of the inflows within the CGUs.’

United Business Media averaged a 26% intangible allocation across all of its 2007 and 2008 acquisitions. They recognised various intangibles including subscription lists (amortised 2-5 years), trade marks (amortised ten years), databases (amortised 2-10 years), customer contracts and relationships (1-10 years), software (amortised 5-6 years), brands (amortised ten years) and website (amortised three years).

Haynes Publishing were the only company to capitalise ‘know-how’ as an intangible on which they adopted an indeterminate life policy. Trademarks were also capitalised and classified as having an indefinite-life.

Informa categorise their intangibles under booklists (amortised 20 years), journal titles (20- 40 years), database content and IP (amortised 4-10 years) and large scale events and exhibitions (8-10 years).

Motivcom recognised a relatively low value of intangible assets for their acquisition of Zibrant, but full disclosure explained that:

‘the goodwill arising on the acquisition of Zibrant is attributable to the anticipated profitability arising from cross-selling opportunities within the enlarged Group from both selling acquired services to the pre-existing client base and selling pre-existing services and products into the acquired non-contractual client base, anticipated future operating synergies from the combination, the account direction and production ability and skills of key personnel of Zibrant and the premium paid to facilitate a large combination. In the context of the latter point, it should be noted that the Group could have established its own business similar to that of Zibrant. However, it would have taken time to build and



develop such a business and an acquisition, although expensive at the outset, is more cost-effective in the long run and gives more certain and immediate results than building a business from scratch. Under IFRS no value can be attributed to such intangibles and this has contributed to the amount recognised as goodwill.'

There are still questions here over whether the cross-sell synergies (with the non-contractual client base) are unique or, instead, available to other buyers, and therefore should have been separately identified (and valued).

This is positive disclosure setting out the basis on which the goodwill has been recognised – something sorely missing in the advertising & marketing services disclosures.

Reed Elsevier's two main acquisitions were Choicepoint Inc. and BuyerZone Inc. with substantial intangibles allocated on each (55.9% and 66.7% respectively). Reed groups its intangibles into 'market and customer related' (which includes trademarks, imprints, brands, subscription bases, lists and relationships) amortised over 3-40 years, and 'content, software and other' (which includes content, delivery systems, publishing rights, exhibition rights and supply contracts) amortised over 3-20 years. With respect to the residual goodwill, Reed states that it:

'represents benefits which do not qualify for recognition as intangibles, including the ability of a business to generate higher returns than individual assets, skilled workforces, acquisition synergies that are specific to Reed and high barrier to market entry.'

Moneysupermarket.com used an external valuer to value the intangibles in respect of their 2007 acquisition. They are now amortising market-related intangibles over ten years, customer relationships over seven years, customer lists over three years and technology over three years. They define market-related intangibles as those that are primarily used in the marketing or promotion of products and services, for example trademarks, trade names and internet domain names. Customer-related intangibles consist of customer lists, customer contracts and relationships, and non-contractual customer relationships. They go on to say:

'relationships with high-profile customers provide the group with prominence in the marketplace, create volume and traffic on the website, and enhance the reputation of the brand. Customer lists allow the group to undertake targeted marketing activities.'

Pearson and **Quarto** were the only companies in the survey that capitalised current intangibles assets (on the basis they met the IFRS 'current' definition with respect to the operating cycle of the business) – this seems logical as these were pre-publication costs. Quarto's policy explains that these:

'represent direct costs incurred in the development of book titles prior to their publication. These costs are carried forward in current intangible assets where the book title will generate future economic benefits and costs can be measured reliably. These costs are amortised upon publication of the book title over estimated economic lives of three years or less, being an estimate of the expected operating cycle of a book title.'

Overall comments and conclusions

Content v Contacts

We expected the differential between the percentage of identified intangibles within audio & televisual, publishing & events and the advertising & marketing services sub-sector to be primarily due to 'Content' ownership within audio & televisual and publishing & events entities. Advertising & marketing services companies focus on 'Contacts' intangibles not 'Content' intangibles, and hence attribute proportionately lower values to intangible assets. Although our survey showed that this was the case in some of the deals looked at, much of the identified intangible value in the audio, televisual and publishing deals actually related to 'non-content' assets such as customer relationships and trade marks. Both of which you would also expect to find in the advertising & marketing services sector.

Advertising & marketing services sector appears out of range

Notwithstanding this differential, there is a worryingly large range of interpretation within the advertising & marketing services sector itself when it comes to valuing intangible assets.

More guidance and insight required

As this is a new area, companies will benefit from more guidance. Another factor could be that companies have not researched the marketplace with enough depth before determining the application of their accounting policies. As time goes on, so practices and norms will develop, but we believe that companies should be more rigorous in their analysis and valuation of what they acquire as part of a business combination. Perhaps a more thorough examination of some of the

factors affecting the price of the acquired business – negotiation and due diligence for example – might give a clearer indication of what companies thought they were paying for. A robust challenge from their auditors on both the policies used and the degree of disclosure surrounding their choice of policy should also be an expectation.

Inconsistency between the amortisation of separately identified intangible assets and goodwill

Prior to IFRS, when a company made an acquisition, goodwill was the excess consideration to be capitalised after the fair value of net assets acquired was deducted from the consideration paid. Under FRS 10, goodwill was believed to have a finite life and its consumption was recognised each year. It was typically amortised over 20 years, due to a feature of FRS 10 which allowed companies to ignore impairment reviews on intangible assets (including goodwill) with a life of less than 21 years. Under IFRS the presumption is that goodwill has an indefinite-life through constant expenditure on replenishment, but must be tested for impairment annually (or more frequently if events or changes in circumstances indicate that it might be impaired) in accordance with IAS 36 'Impairment of Assets'. Why is the treatment of goodwill inconsistent with the treatment of other intangibles whose value is not presumed to be sustained through continued replenishment?

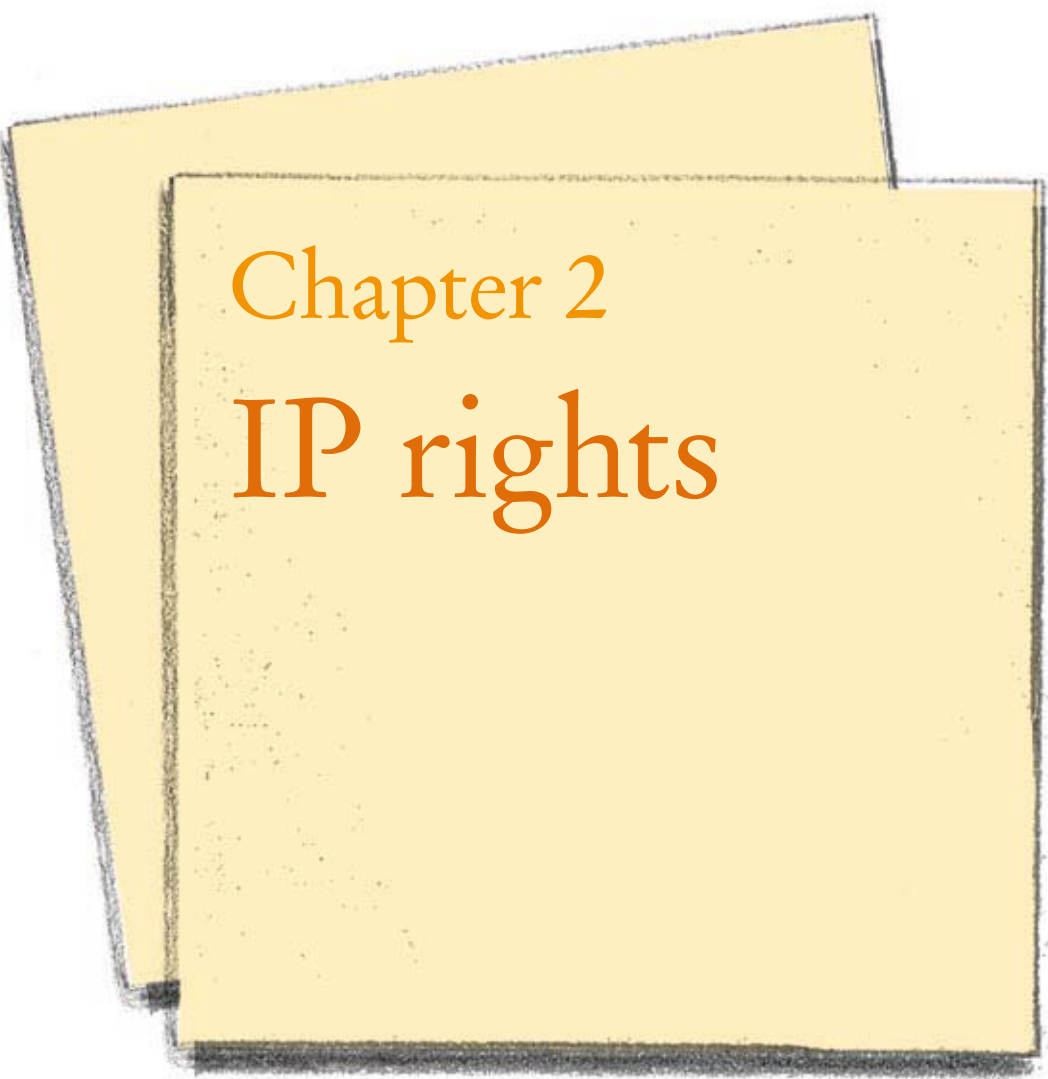
Increased information is available

The improvement in reporting on intangibles and segmental reporting means that it is easier than in the past to spot inconsistencies in reporting, and potentially for analysts and shareholders to question management more closely about the carrying value of intangible assets recognised at the point of business combinations.

Disclosure around what 'goodwill' represents is lacking

Many companies disclose simply that goodwill represents 'synergies'. We do not believe this is sufficient disclosure and question whether the requirements of IAS 38 should be strengthened in this area.

The process of evaluating goodwill compels management to identify and quantify the sources of cashflows that go on to support the value of goodwill. If this is a struggle and the assumptions about cashflows are unrealistic or indefinable, not only does it suggest an overpayment but it might also erode value as a lack of measurability leads to a lack of attention by management in the areas previously identified as representing 'synergies'.



Chapter 2

IP rights



IP is integral to how media businesses operate, but many continue to grapple with how the value of IP created by their businesses can be recognised in their financial statements. So how do media companies deal with internally generated or acquired IP? What do they capitalise and how do they amortise it?

The background

Under UK accounting standards, the treatment of intangible fixed assets is dealt with within two different standards. FRS 10 deals with goodwill and intangible assets, SSAP 13 deals with Research and Development costs.

Much of the development work on FRS 10 was carried out during the late 1980s and early 1990s, in a period of recession in the UK. At that time there was a backlash against some of the accounting practices of the 1980s that had led to the capitalisation of brands, and hence FRS 10 contained provisions to ban the capitalisation of brands and other internally-generated intangible fixed assets.

The standard was not particularly helpful for the media sector. Companies that developed valuable content in-house for exploitation potentially could not recognise its value on the balance sheet.

Some businesses considered their content as a tangible fixed asset rather than intangible. This was on the basis that the value in, say, a television programme, lay as much in the physical master tape of the programme, which was tangible, as in the copyright ownership of the programme. It was therefore dealt with under FRS 15, tangible fixed assets, rather than FRS 10.

Another method was to consider the creation of each piece of content as a piece of research and development. Under SSAP 13, certain costs of development work carried out internally could be capitalised provided that a number of criteria were met.

Internationally, FRS 10 and SSAP 13 were pushed together into IAS 38 'Intangible Assets', which broadly speaking allowed the capitalisation of internally generated intangibles using the SSAP 13 criteria, although capitalisation of brands and mastheads was still not permitted.

IFRS for SMEs

It was proposed by the ASB that IAS 38 (in the form of FRED 37) would replace the UK standard FRS 10. However, this move was shelved awaiting convergence. Since then, we have had the publication of the proposed IFRS for SMEs.

IFRS for SMEs prohibits the capitalisation of internally generated IP rights. This potentially creates a problem for smaller media companies, while banks and other lenders get used to the idea of these companies not recognising the cost of their content on their balance sheets.

The effect on the balance sheet of this essential difference between IFRS and IFRS for SMEs could give rise to early adoption of full IFRS by smaller media companies (see Appendix 3) in order to increase the asset value shown on their balance sheets in line with their pre-IFRS levels.

The IAS guidance

IAS 38 is the international standard guiding the treatment of internally generated or acquired IP rights. The standard defines an intangible asset as ‘an identifiable non-monetary asset without physical substance’ and goes on to explain that entities ‘frequently expend resources, or incur liabilities, on the acquisition, development, maintenance or enhancement of intangible resources such as... intellectual property.’

Acquired IP rights

For acquired IP to be recognised as an intangible, the asset must meet the identifiability (1), control (2), and future economic benefit (3) criteria:

1. ‘An asset meets the **identifiability** criterion in the definition of an intangible asset (IAS 38.12) when it:
 - a. is separable, ie is capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, asset or liability; or
 - b. arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.’
2. ‘An entity **controls** an asset if (IAS38.13) the entity has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits’
3. ‘The **future economic benefits** flowing from an intangible asset may include (IAS 38.17) revenue from the sale of products or services, cost savings, or other benefits resulting from the use of the asset by the entity.’

Internally generated IP rights

IAS 38.57 allows costs arising from ‘development’ (or from the development phase of an internal project) to be capitalised as an intangible asset if, and only if, an entity can demonstrate all of the following:

- a. ‘the technical feasibility of completing the intangible asset so that it will be available for use or sale
- b. its intention to complete the intangible asset and use or sell it
- c. its ability to use or sell the intangible asset
- d. how the intangible asset will generate probable future economic benefits. Among other things, the entity can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset
- e. the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset
- f. its ability to measure reliably the expenditure attributable to the intangible asset during its development.’

Expenditure on internally generated brands, mastheads, publishing titles, customer lists and items similar in substance cannot be distinguished from the cost of developing the business as a whole. Therefore, such items are not recognised as intangible assets.

Amortisation of IP rights

IAS 38 is relatively light on amortisation guidance, with the overriding aim being around allocating the depreciable amount on a ‘systematic basis’ (IAS 38.97) over the asset’s useful life. It states:

‘The depreciable amount of an intangible asset with a finite useful life shall be allocated on a systematic basis over its useful life. Amortisation shall begin when the asset is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. The amortisation method used shall reflect the pattern in which the asset’s future economic benefits are expected to be consumed by the entity. If that pattern cannot be determined reliably, the straight-line method shall be used.’

Audio & televisual companies analysis

The Super Indies

These companies, by virtue of the fact they have in-house distribution businesses as well as production units, tend to have both categories of IP rights – internally generated and acquired.

Shed Media's programming assets were reclassified on transition to IFRS from tangible assets to intangible assets on the basis they met the IAS 38.57 capitalisation criteria. RDF Media applied a similar policy to their programming catalogue that was already on the balance sheet. Clearly, IP rights do not fit in the IFRS 'Property, plant and equipment' classification.

Shed Media and **DCD Media** adopt a slightly different policy to RDF Media in respect of on going programming. Shed Media and DCD Media both capitalise **all programme costs** as they are incurred up to completion of the programme as internally generated intangible assets – presumably on the basis that the entire period of production qualifies as 'development' expenditure under IAS 38.

Where programmes in development are not considered to be proceeding, the related costs are written off. For those programmes that are proceeding or are commissioned, the costs are amortised in the ratio that actual revenue recognised in that period bears to estimated ultimate revenue, after making provision for anticipated losses or overspends.

This method places a significant emphasis on forecasting techniques; interestingly neither company disclose the forecasting

techniques used in assessing ultimate revenues and how they mitigate the risks inherent in those forecasts. We find this surprising given the significant impact those forecasts must be having on the results reported.

In contrast **RDF Media** continues to expense all production costs, capitalising only where a production is deficit financed, and then amortising them 40%/40%/20% over three years – presumably mirroring their expected revenue profile. This policy essentially assumes that only the deficit financed part of the production cost qualifies as 'development' expenditure. It may present a cleaner, and more transparent position in respect of the income statement, but is the inherent value of the IP that has been created really captured on the balance sheet?

Interestingly, in 2007 RDF adopted an 'ultimate revenue' policy to amortise certain programme costs. This applied when significant contribution is anticipated to come not solely from the initial broadcast licence over the production period, but also from subsequent worldwide distribution and exploitation over several years. The accounting policy states that total costs of production are amortised across the contribution derived from the initial licence fee and that from future anticipated exploitation. Further disclosure elaborated on this policy:

'Production and licence revenues are recognised on a straight line basis over the length of the production as are the costs associated with them. Revenues from exploitation are recognised in line with the Group's existing policy with the balance of production costs amortised in line with revenues recognised versus total anticipated

forecasted revenues. The forecasted future exploitation revenues are reviewed regularly to ensure the forecasted gross contribution exceeds the balance of capitalised cost. Where future forecasted revenues reduce permanently versus original estimates, the rate of amortisation increases. Where future forecasted revenues increase, the rate of amortisation will remain as originally estimated. The rationale for the adoption of the new approach, where applicable, is that the Group is entering into diverse production models in terms of revenue structures, time being invested to produce the content and the ultimate value of the content to the Group. The advantage with this policy is that it more closely matches the costs incurred to produce the asset with the revenues it ultimately will generate.'

RDF also added useful disclosure in respect of their forecasting techniques, which are clearly instrumental in how the above policy affects the financial results. This policy reads:

'In applying the Group's accounting policies with respect to revenue and asset recognition, the group has adopted varying forecasting methods that involve significant judgments and estimates. In the case of revenue recognition, ultimate revenues and ultimate contributions (together 'ultimate estimates') from certain production and programme rights have been forecasted as a basis on which to recognise revenue and contribution across the life of a programme (see revenue recognition accounting policy for more detail). In the case of asset recognition, ultimate estimates from certain production and programme rights have been forecasted as a basis to support the capitalisation of investment in programmes (see production investments accounting policy for more detail).

Significant judgments and estimates have been adopted in determining these forecasts and ultimately, the amounts recognised. The Group has drawn upon the experience of its senior operating executives in determining the ultimate

estimates from the exploitation, exhibition, and sale of secondary and tertiary rights in all markets and territories over the useful economic life of the associated rights.

The following constraints have been applied to these estimates:

- for a completed episodic television series, ultimate estimates have been forecasted over a period not exceeding ten years from delivery of the first episode
- for an episodic television series still in production, ultimate estimates have been forecasted over a period not exceeding five years from delivery of the most recent episode (if later than delivery of the first episode)
- estimates of all secondary market revenue have been included only where the Group is satisfied that it will be able to successfully license those episodes already produced and where there is a commitment to produce the remainder
- revenue and associated contribution has been included in ultimate estimates where:
 - persuasive evidence exists that revenue can be generated from secondary markets or territories (estimates from newly developing territories have only been used if an existing arrangement provides convincing evidence that the entity will realise such amounts)
 - persuasive evidence exists that revenue can be generated from third party licensing arrangements to market programme-related products
 - persuasive evidence exists that wholesale or retail revenue can be generated from the sale of peripheral items (such items as toys and merchandising) attributable to the exploitation of the programme
- estimates of wholesale promotion or advertising reimbursement from third parties have not been included in ultimate estimates, but rather have been offset against exploitation costs
- ultimate estimates have not been discounted to their present value. In addition, ultimate estimates have not included projections for future inflation

- all foreign currency estimates of future revenues and contribution have been based on current spot rates.'

In terms of acquired IP rights, all three of the groups capitalise advances paid in respect of distribution rights from third party producers as intangible assets where they are 'supportable by future revenues' – these assets presumably meet the identifiability, control and future economic benefits criteria of IAS 38 to support capitalisation.

Talent Group – a smaller producer – carries costs relating to in-progress productions in current assets and writes them off if they do not proceed within two years of inception – this infers they are carrying development costs on-balance sheet within current assets. Their acquired IP rights are classified as intangibles and are written off over ten years.

The Broadcasters

ITV and BSkyB are captured by this survey but we considered that a wider comparison among all of the main UK broadcasters – including the BBC, Channel 4 and Channel 5 which all report under IFRS – would give greater context and completeness to the analysis.

In terms of capturing, capitalising and amortising their IP rights, the broadcasters are in a fundamentally different position to the independent producers since the shake up of the Communications Act in 2003. They no longer retain or own the IP created by independent producers and as such are

not capitalising, and amortising, programme cost in the same way. Most do have in-house production units, and thus originate and own IP rights, as well as retaining their back catalogues. But the IP rights from commissioned programmes are no longer owned by the broadcasters. What we are seeing now is a reduction in broadcaster IP capitalisation and an increase in programme cost coming through the current asset position in their balance sheets as they fund the production of the content they have commissioned.

This indeed is the case with all of the main broadcasters showing investments in programming in the 'inventories' part of the balance sheet. What is interesting from the analysis, however, is how the broadcasters are amortising or writing off those programme costs or 'inventories'. There is no clear theme here with each broadcaster disclosing policies that are subtly different from each other, but yet could result in considerably different financial statement positions.

STV group carry the costs of film and programming as inventory and write them off 70%/30% on first and second transmission respectively.

BSkyB also carries programme costs as inventory and adopts different write off policies for each genre:

'Programme inventories are stated at the lower of cost and net realisable value ("NRV"), including, where applicable, estimated subscriber escalation payments, and net of the accumulated expense charged to the income statement to date. Programming rights are included as inventories when the legally enforceable licence period commences and all of the following

conditions have been met: (a) the cost of each programme is known or reasonably determinable; (b) the programme material has been accepted by the Group in accordance with the conditions of the rights, and (c) the programme is available for its first showing. Prior to being included in inventories, the programming rights are classified as television programme rights not yet available for transmission and not recorded on the Group's balance sheet and are instead disclosed as contractual commitments (see note 27).

Payments made upon receipt of commissioned and acquired programming, but in advance of the legal right to broadcast the programmes, are treated as prepayments.

The cost of television programme inventories is recognised in the operating expense line of the income statement, primarily as described below:

Sports – 100% of the cost is recognised in the income statement on the first broadcast or, where the rights are for multiple seasons or competitions, such rights are principally recognised on a straight-line basis across the seasons or competitions.

News – 100% of the cost is recognised in the income statement on first broadcast.

General entertainment – the cost is recognised in the income statement based on the expected value of each planned broadcast.

Movies – the cost is recognised in the income statement on a straight-line basis over the period of broadcast rights.

Where programme rights are surplus to the Group's requirements, and no gain is anticipated through a disposal of the rights, or where the programming will not be broadcast for any other reason, a write-down to the income statement is made.'

BSkyB also added commentary in its significant estimates and judgments section stating:

'The key area of accounting for programming inventory requiring judgement is the assessment of the appropriate profile over which to recognise amortisation in the income statement. This assessment requires the Group to form an expectation of the number of times a programme

will be broadcast and the value associated with each broadcast. For general entertainment programming, in order to perform this assessment of amortisation profile, we consider the expected number of viewers a programme is likely to achieve on repeat broadcast, the alternative programming available to the programming scheduler, the potential marketing benefits relating to the scheduling of certain programmes and the Group's assessment of its competitors' scheduling intentions when determining the amount of programme expense to recognise for each broadcast. Acquired movie rights are amortised on a straight-line basis over the period of the transmission rights. Where contracts for sports rights provide for multiple seasons or competitions, they are amortised on a straight-line basis across the season or competition as our estimate of the benefits received from these rights is determined to be most appropriately aligned with a straight-line amortisation profile.'

Channel 5 discloses that all programme rights are stated at the lower of cost and net realisable value and are

'consumed based on the expected number of transmissions.'

This would appear to suggest it could forecast that a series will air three times and it would carry the cost over the dates of transmission of the three airings – this doesn't seem unreasonable if that is how it expects to consume the asset it has purchased – and clearly this is spreading the level of expense recognised in the income statement.

In contrast, **Channel 4** writes off programme rights in full on first transmission. This is significantly different to Channel 5. Certain feature films are written off over more than one transmission in line with total expected revenue (similar to the super-indies ultimate-income forecast model).

ITV is similar to Channel 4 in that it writes off in full on first transmission and certain features are written off in line with total expected revenue. It does say though that consideration is made of the number of transmissions available in the schedule over the licence period when assessing net realisable value of those rights still carried on the balance sheet. ITV's policy on programme rights is as follows:

'Where programming, sports rights and film rights are acquired for the primary purpose of broadcasting, these are recognised within current assets. Assets are recognised when the Group controls, in substance, the respective assets and the risks and rewards associated with them. Acquired programme rights assets are recognised as payments are made and are recognised in full when the acquired programming is available for transmission. Programming produced internally, either for the purpose of broadcasting or to be sold in the normal course of the Group's operating cycle, is recognised within current assets at production cost.

Programme costs and rights, including those acquired under sale and leaseback arrangements, are written off to operating costs in full on first transmission except certain film rights and programming for digital channels which are written off over a number of transmissions.

Programme costs and rights not yet written off are included in the balance sheet [current assets] at the lower of cost and net realisable value. In assessing net realisable value consideration is given to the contracted sales price and estimated costs to complete for programmes in production, and the estimated airtime value of programme stock, sports rights and film rights. In assessing the airtime value of programme stock and film rights consideration is given to whether the number of transmissions purchased can be efficiently played out over the licence period.

Any reversals of write downs for programme costs and rights are recognised as a reduction in operating costs.'

ITV writes off acquired film libraries over 20 years using a sum of digits method.

UTV Media states that:

'Intangible assets created within the business are not capitalised and are expensed.'

presumably because they don't meet the IFRS capitalisation criteria. Its radio and television licences are carried as intangible assets, with an indefinite useful life however. This is allowed under IAS 38.94:

'The useful life of an intangible asset that arises from contractual or other legal rights shall not exceed the period of the contractual or other legal rights, but may be shorter depending on the period over which the entity expects to use the asset. If the contractual or other legal rights are conveyed for a limited term that can be renewed, the useful life of the intangible asset shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost.'

UTV's programming is carried in current assets and written off on first transmission.

The **BBC** writes off programme rights on first transmission except when further showings are scheduled – in which case they are written off over their transmission profile. Programmes commissioned from indies are written off on first transmission except for costs relating to prepaid repeats.

The Distribution Companies

Considering what these companies do (invest in programme rights) you would expect significant policy disclosure with respect to the capitalisation and amortisation of rights. These rights fall into the intangible assets category in all cases.

ContentFilm separates its rights purchases into six distinct categories – each carrying its own amortisation basis:

'Television library rights – ultimate revenue amortisation model (normally ten years)

Film library rights – ultimate revenue amortisation model (normally ten years)

DVD library rights – ultimate revenue amortisation model (normally ten years)

Investments in Film/TV rights – amortisation as recouped (normally 12-36 months after completion)

Investments in DVD rights – ultimate revenue model (normally ten years)

Investments in 'first look' rights – ultimate revenue model where attributable to a title and over the period of the first look rights where it is a general first look right.'

Eros International presents its content rights in three categories – productions, film and content rights, and content advances. It does not explicitly say how it amortises these rights, simply that a charge is calculated and expensed over the estimated useful life of the asset. It does state that the average life of assets is five years. Its policy reads:

'Investments in films and associated rights, including acquired rights and distribution advances in respect of completed films, are stated at amortised cost less provision for impairment. A charge is made to write down the

cost of completed rights over the estimated useful lives except where the asset is not yet available for exploitation. The average life of assets is five years and the amortisation charge is recognised in the income statement within cost of sales.'

Indian Film Company amortises film costs using the individual-film-forecast method. It states that:

'Under the individual-film-forecast method, such costs are amortised for each film in the ratio that current period revenue for such films bears to management's estimate of remaining unrecognised ultimate revenue as at the beginning of the current fiscal year. Management regularly reviews and revises, where necessary, its total estimates on a film-by-film basis, which may result in a change in the rate of amortisation and/or a write down of the intangible asset to fair value. The amortisation charge is included under cost of sales in the Consolidated Income Statement.

The assets are assessed for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. If any such indication of impairment exists, the Group makes an estimate of its recoverable amount.'

Metrodome writes off costs in line with actual income flows against future income and states that:

'Expenditure on the Group's film distribution library is carried forward and recognised as an asset when it is estimated that sufficient future income will be earned to cover recoupment of the costs. These costs are written off in line with actual income flows calculated in accordance with licensor agreements. Pre-production expenditure is recognised when the costs may be recouped through reduced commission payments.

The estimate of future income depends on management judgement and assumptions based on the pattern of historical revenue streams and the remaining life of each film contract.'

Metrodome also adds useful commentary in its significant estimates and judgments section on both its film library policy and its inventories policy:

Film distribution library asset

'Expenditure on the Group's film distribution library is carried forward and recognised as an asset when it is estimated that sufficient future income will be earned to cover recoupment of the costs. To calculate the provision for impairment for each film, the carrying value of the asset is compared to the expected revenue streams. Estimates of future income are made, film title by title, based on the following:

- total revenue to date on each title
- revenue for the current year on each title
- historic revenue patterns by film category
- contract expiry dates
- quarterly forecast
- commercial knowledge and experience
- future revenues are discounted to present values at a rate of 10%.

Where expected revenue is lower than the carrying value of the asset, the value of the asset is impaired to reflect the expected revenue.

Inventories

Expenditure on the Group's film distribution library is normally held as a non-current asset, including expenditure on replication of DVDs and packaging costs. If a film has been successful with total revenues exceeding total costs, its value will be nil. However, if future revenues are expected on these fully recouped titles, it is appropriate to recognise a value for the inventories held at the balance sheet date. In this instance, these inventories are stated in the balance sheet as a current asset at the lower of cost and NRV in accordance with IAS 2 Inventories.'

Although IAS 38 is now capturing all intangible assets, it is not particularly prescriptive with respect to amortisation methodologies.

DQ Entertainment has a comprehensive policy covering advances, projects under development, subsequent expenditure and amortisation:

'Distribution rights that are acquired by the Group are stated at cost less accumulated amortisation and impairment losses.

Advances paid for distribution rights

Advances paid for distribution rights include amounts paid to the producers for acquisition of the distribution rights. These advances are transferred to distribution rights on completion of the entire production activities and when the asset is ready for exploitation. No amortisation is charged on these advances until they are transferred to the distribution rights. Up to that point, they are assessed annually for impairment.

Projects under development

Direct or indirect expenses incurred on the Development of Projects in order to create Intellectual Property or Content, which are exploited on any form of media are capitalized as an intangible asset under development in accordance with IAS 38 (intangible assets). In the event, the project is not scheduled for production within three years, or project is abandoned, the carrying value of the Development Rights would be expensed in the year in which such project is discontinued or abandoned.

Subsequent expenditure

Subsequent expenditure on capitalised intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets. Intangible assets are amortised from the date they are available for use. The estimated useful lives are the term of the licensing agreement or 10 years which ever is less. Useful lives for individual assets are determined based on the nature of the asset, its expected use, the length of the legal agreement or patent and the period over which the asset is expected to generate economic benefits for the Group ('Economic life').'

All companies have stated the different classes of IP rights they are capitalising and the respective amortisation method adopted, thus giving clear and comprehensive disclosure.

The most interesting area, however, in respect of the audio & televisual distributors' IP rights, is the adoption of the 'income-forecast' amortisation methodology. This is a methodology that has been around for some time and has been widely adopted by the US film studios as it is mandated under specific US accounting guidance. Their equivalents in the UK were left to their own devices in the past, resulting in a multitude of policies ranging from IP being recognised in current assets with no amortisation policy being disclosed, to IP being capitalised as a tangible or intangible asset and amortised on a straight line or income-forecast basis. As explained in the opening paragraphs of this chapter, although IAS 38 is now

capturing all intangible assets, it is not prescriptive with respect to amortisation methodologies. DQ Entertainment and Eros International were the only distributors in the sample not using the 'income forecast' method; both used systematic methodologies – which, as IAS 38 .97 explains, should be used if the pattern in which the asset's future economic benefits are expected to be consumed cannot be determined reliably. Presumably the uncertainties in the income forecasts or 'future economic benefits' for these assets prevented the directors from being able to rely upon those forecasts as a basis for amortisation.

Those companies that do use the income forecasting method would be expected to disclose this as a key source of estimation uncertainty in accordance with IAS 1.116.

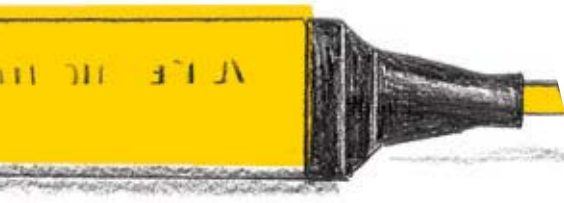
Advertising & marketing services companies analysis

Marketing & advertising services companies have significantly less internally generated IP rights that can be capitalised under IAS 38 compared with the other two sub-sectors:

This is to be expected as their businesses are predominantly based on the provision of professional services in their chosen areas, and the development of brands and processes to complement those services. Although these processes create value in the businesses, they are not able to be capitalised under IAS 38. It is only at the point of business combination that the true value of the brand names, customer relationships and customer lists of these companies make their way onto the balance sheet, as discussed in Chapter 1.

The market research companies do stand out, however, in that they capitalise internally generated software and panel costs – which are particular to their businesses. **YouGov**, **Research Now** and **Toluna** all capitalised consumer panel costs, amortising them over five years, one year, and 1-2 years respectively. YouGov also stated that they had adopted an indefinite-life policy with respect to patents and trademarks.

In summary, the lack of internally generated IP on the balance sheets across the advertising & marketing services sub-sector comes as no surprise and highlights an essential difference between this and the other two sub-sectors of media.



“

It is only at the point of business combination that the true value of the brand names, customer relationships and customer lists of these companies make their way onto the balance sheet.

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Publishing & events companies analysis

As noted above, IAS 38.64 specifically excludes expenditure on internally generated brands, mastheads, publishing titles and customer lists for recognition as intangible assets, so we would not expect a significant level of capitalisation in this area. This was indeed the case. Unfortunately, these happen to be four of the most valuable assets that publishing and events companies create.

Publishing companies have had to live with this situation for many years now. This can make comparisons between businesses difficult at times. Companies that have grown organically and developed titles internally will tend to have a lower level of assets in their balance sheets compared with companies that have grown by acquisition (where the fair value of assets acquired is disclosed). Although the ‘organics’ balance sheets might seem weaker than the ‘acquirers’, their return on capital ratios will be stronger, given that the ‘organics’ have reduced their capital employed by writing off title development costs. Also, the ‘organics’ do not have to suffer any ongoing amortisation or impairment costs in respect of these intangible assets, having written off the costs to develop as incurred.

It will be interesting to see the changes in the intangible capitalisation policies of companies in this sector as the publishing model migrates from a traditional one to a cross platform, cross media form of delivery where

‘development’ expenditure that ought to be capitalised could be significant.

Pearson’s policy with respect to its recognition of ‘newspaper development costs’ highlights this point perfectly. It states that:

‘Investment in the development of newspaper titles consists of measures to increase the volume and geographical spread of circulation. The measures include additional and enhanced editorial content extended distribution and remote printing. These costs are expensed as incurred as they do not meet the criteria under IAS 38 to be capitalised as intangible assets.’

Going forward, we could see an argument being presented for capitalising newspaper development costs relating to new models or formats of distribution.

A further point of note in this sector was **Pearson’s** and **Quarto’s** recognition of ‘pre-publication costs’ as current intangible assets as opposed to inventories or non-current intangible assets in the way the companies in the television sector do. Quarto states:

‘Pre-publication costs represent direct costs incurred in the development of book titles prior to their publication. These costs are carried forward in current intangible assets where the book title will generate future economic benefits and costs can be measured reliably. These costs are amortized upon publication of the book title over estimated economic lives of three years or less, being an estimate of the expected operating cycle of a book title. The investment in prepublication has been disclosed as part of the investing activities in the cash flow statement.’

Pearson’s policy was similar in this area:

‘Pre-publication costs represent direct costs incurred in the development of educational programmes and titles prior to their publication. These costs are recognised as current intangible assets where the title will generate probable future economic benefits and costs can be measured reliably. Pre-publication assets are amortised upon publication of the title over estimated economic lives of five years or less, being an estimate of the expected operating life cycle of the title, with a higher proportion of the amortisation taken in the earlier years. The investment in pre-publication assets has been disclosed as part of cash generated from operations in the cash flow statement. The assessment of the recoverability of pre-publication assets and the determination of the amortisation profile involve a significant degree of judgement based on historical trends and management estimation of future potential sales. An incorrect amortisation profile could result in excess amounts being carried forward as intangible assets that would otherwise have been written off to the income statement in an earlier period.’

Going forward, we could see an argument being presented for capitalising newspaper development costs relating to new models or formats of distribution.

Overall comments and conclusions

How has IFRS impacted?

A key difference between UK GAAP previously adopted and IFRS in respect of the capitalisation of intangible assets, has meant that audio & televisual businesses no longer need to take the approach of considering their film, television programme or music libraries as tangible fixed assets, showing them as internally generated intangible assets instead.

How will IFRS for SMEs impact?

Although full IFRS clarifies and improves the reporting position for those listed companies in the audio & televisual sector, under the proposals published in mid 2009, any unquoted companies would be prohibited from capitalising such assets under the IFRS for SME standards. This will not aid cross-sector comparison, particularly between mid-cap listed companies and large privately-held companies.

Is the balance sheet capturing all intangibles?

Although IAS 38 permits the capitalisation of certain internally generated intangible assets, it prohibits the capitalisation of others, specifically brands, mastheads, publishing titles and customer lists. This adversely affects the balance sheet net asset totals of companies in the publishing & events sub-sector as these are four of the more valuable intangible assets that are generated by these businesses.

To a degree, this prohibition also adversely affects the balance sheets of companies in the advertising & marketing services sub-sector as well. The effect would be more keenly felt in both sub-sectors by those businesses that expand primarily by organic growth and not by acquisition. Companies that grow by acquisition and carry out fair value exercises identify and value intangibles acquired on their balance sheet.

Where are key judgements made by management?

A theme running throughout this section was the lack of disclosure in respect of judgments and key sources of estimation which is required under IAS 1. This is a particularly useful disclosure in understanding how management have developed, and are monitoring their amortisation policies.

“[The treatment of intangible assets under IFRS for SMEs] will not aid cross-sector comparison, particularly between mid-cap listed companies and large privately-held companies.”

Chapter 3

Revenue recognition and segmentation



Sector-wide segmentation analysis

Our survey captured segmental reporting under both IAS 14 ‘Segment reporting’ and IFRS 8 ‘Operating segments’ as both standards were in force during the accounting periods under review. IFRS 8 requirements applied for accounting periods beginning on or after 1 January 2009; early adoption was permitted but during the period covered most companies were still reporting under the IAS 14 criteria.

IAS 14 v IFRS 8 – key changes

Identification of segments – IFRS 8 requires amounts to be disclosed based on the components of the entity that management uses to make decisions about operating matters. It requires identification of operating segments on the basis of internal reports that are regularly reviewed by the entity’s chief operating decision maker in order to allocate resources to the segment and assess its performance. IAS 14 required identification of two sets of segments – one based on related products and services, and the other on geographical areas. IAS 14 regarded one set as primary segments and the other as secondary segments.

Measurement of segment information – IFRS 8 requires the amount reported for each operating segment item to be the measure reported to the chief operating decision maker for the purposes of allocating resources to the segment and assessing its performance. IAS 14 required segment information to be prepared in conformity with the accounting policies adopted for preparing and presenting the financial statements of the consolidated group or entity. IAS 14 defined segment revenue, segment expense, segment result, segment assets and segment liabilities. IFRS 8 does not define these terms, but requires an explanation of how segment profit or loss, segment assets and segment liabilities are measured for each reportable segment.

Disclosure – Among other things, IFRS 8 requires an entity to disclose the following information:

- a. factors used to identify the entity’s operating segments, including the basis of organisation (for example, whether management organises the entity around differences in products and services, geographical areas, regulatory environments, or a combination of factors and whether segments have been aggregated), and
- b. types of products and services from which each reportable segment derives its revenues.

IAS 14 required the entity to disclose specified items of information about its primary segments. IFRS 8 requires an entity to disclose specified amounts about each reportable segment, if the specified amounts are included in the measure of segment profit or loss and are reviewed by or otherwise regularly provided to the chief operating decision maker.

IFRS 8 requires an entity, including an entity with a single reportable segment, to disclose information for the entity as a whole about its products and services, geographical areas, and major customers. This requirement applies, regardless of the entity’s organisation, if the information is not included as part of the disclosures about segments. IAS 14 required the disclosure of secondary segment information for either industry or geographical segments, to supplement the information given for the primary segments.

IFRS 8 seems instinctively to be a more pragmatic standard than IAS 14. Its reporting requirements spring from the in-place operating procedures of the business rather than being a matter of choice for management. Two points occur to us – how much will disclosure be opposed by management on the basis of commercial confidentiality and how quickly will reconfigured segmental information flow through into accounting policies structured and expressed around those policies?

‘Implementing IFRS 8

January 2010 saw the Financial Reporting Review Panel highlight the challenge of implementing the new segmental reporting requirements under IFRS 8 ‘Operating segments’; the Panel encouraged companies to test their initial conclusions about their segmental reporting by considering the following questions:

1. What are the key operating decisions made in running the business?
2. Who makes these key operating decisions?
3. Who are the segment managers (as defined in the standard) and who do they report to?
4. How are the group's activities reported in the information used by management to review performance and make resource allocation decisions between segments?
5. Is any proposed aggregation of operating segments into one reportable segment supported by the aggregation criteria in the standard, including consistency with the core principle?
6. Is the information about reportable segments based on IFRS measures or on an alternative basis?
7. Have the reported segment amounts been reconciled to the IFRS aggregate amounts?
8. Do the accounts describe the factors used to identify the reportable segments including the basis on which the company is organised?

IAS 14 required companies to identify their primary segment reporting format as either a business segment or a geographical segment based on the dominant source and nature of the company's risks and returns. The table below sets out the segmentation by sub-sector.

Table 10. Segmentation by sub-sector

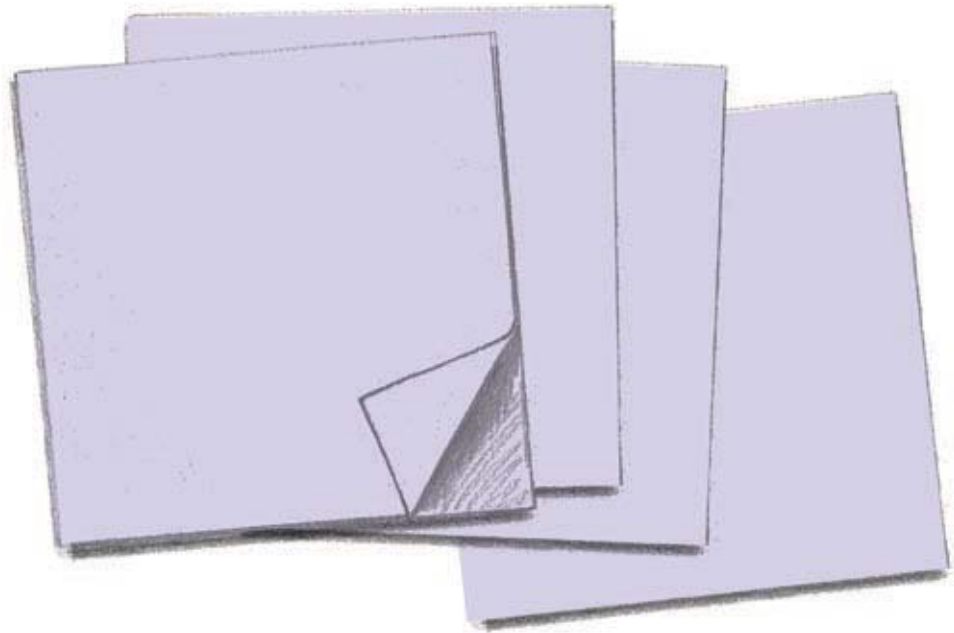
	Audio & televisual	Advertising & marketing services	Publishing & events	Other	Total
Geographical as primary	9	17	8	7	41
Business as primary	7	14	13	1	35
TOTAL	16	31	21	8	76
Not reporting segmentation	(single market/country/chose not to)				47
					123

Even in what are relatively small sub-sectors there was a broad range of business segments disclosed by companies. We have grouped these below for information.

Table 11. Analysis of business segmentation by reported activity

Audio & televisual	No. of companies	Publishing & events	No. of companies	Advertising & marketing services	No. of companies
TV/Film production/Content creation	13	Segmentation by specific market sector	9	Consultancy/Business/Design services	11
Exploitation/Distribution (sales)	7	Newspapers and information services	6	Segmentation by specific market sector	8
Licensing/Merchandising/		Publishing	5	Online marketing and media	7
Consumer products/DVD	5	Digital/Online/Interactive	5	PR/IR	6
Broadcasting/Outdoor	4	Events	4	Branding, media/response	
Unallocated	3	Book publishing	2	communications	5
Corporate	3	Contract/Co-publishing	2	Technology & Data	4
Wholesale subscription	2	Intermediary	2	Advertising & Media buying	4
Gaming/Betting	2	Exhibitions/Conferences	2	Market research	4
Music	2	Advertising/Sales promotions	2	Direct marketing	4
Retail subscription	1	Corporate/Central	1	Central	3
Advertising	1	Unallocated	1	Publishing & events	3
Installation, hardware and service	1			Unallocated	2
Theatrical	1			B2B	2
Digital/Online	1			B2C	2
Executive producer fees	1			Loyalty & Partnership/CRM	2
Sales commissions	1			Broadcast	1
Recoverable project cost	1			Tactical sales promotion	1
				Promotional marketing	1
				Multi-channel marketing	1

We have looked at the reporting of revenue recognition policies under IAS 18 to see if these have differed widely from those in use prior to the adoption of International Accounting Standards. We have also looked at the interaction between segmental analyses and revenue recognition policies – does the terminology from one flow through to the other so that the reader can understand (a) the areas in which the business operates, and (b) how it measures its revenues in each of those areas? Or are these disjointed, giving the reader no real clue as to how the business comes together?



Audio & televisual companies revenue analysis

Of the 37 companies in this sub-sector, six are on the main market with the balance on AIM, although two (RDF and The Local Radio Company) have been taken private in the last year and one (Entertainment Rights) is no longer trading.

We selected ten companies to examine revenue recognition policies in greater depth. These are:

Company	AIM/FTSE
BSkyB	FTSE
ITV plc	FTSE
RDF Media Group Limited	AIM
Entertainment Rights plc*	FTSE
Shed Media plc	AIM
Eros International plc	AIM
DCD Media plc	AIM
ContentFilm plc	AIM
Boomerang Plus plc	AIM
DQ Entertainment plc	AIM

*now in administration

Of the ten companies, eight give a primary segmental analysis of revenues by business type. Of the remainder, **Boomerang**'s principal activity is television production; no analysis is given. Presumably the other activities referred to in its business review of facilities and talent management are not material. As all activity is UK based, Boomerang has no need to give any geographical analysis. **Entertainment Rights** also claimed a single activity, but provided a geographical analysis.

The opening of the introduction to the business, objectives and strategy of **British Sky Broadcasting Group (BSkyB)** reads:

'British Sky Broadcasting Group plc and its subsidiaries (the "Group") operate the leading pay television broadcast service in the UK and Ireland as well as broadband and telephony services. We acquire and commission programming to broadcast on our own channels and supply certain of those channels to cable operators for retransmission by the cable operators to their subscribers in the UK and Ireland. We retail channels (both our own and third parties') to DTH subscribers and certain of our own channels to a limited number of DSL subscribers (reference in this Annual Report to the number of "DTH subscribers" includes the number of DSL subscribers to whom Sky retails its content directly).'

The revenue recognition note in BSkyB's accounting policies reads:

Revenue recognition

'Revenue, which excludes value added tax and transactions between Group companies, represents the gross inflow of economic benefit from Sky's operating activities. The Group's main sources of revenue are recognised as follows:

- Retail subscription revenue, including subscriptions for Sky TV, Sky Broadband and Sky Talk services, is recognised as the goods or services are provided, net of any discount given. Pay-per-view revenue is recognised when the event or movie is viewed
- Wholesale revenue is recognised as the services are provided to the cable retailers and is based on the number of subscribers taking the Sky channels, as reported to the Group by the cable retailers, and the applicable rate card or contract
- Advertising sales revenue is recognised when the advertising is broadcast. Revenue generated from airtime sales, where Sky acts as an agent on behalf of third parties, is recognised on a net commission basis
- Sky Bet revenue is recognised in accordance with IAS 39. Sky Bet revenue represents income in the period for betting and gaming activities, defined as amounts staked by customers less winnings paid out
- Installation, hardware and service revenue is recognised in the income statement when the goods and services are delivered

Although ITV's revenue policy is clear and simple, it does not directly tie back to the segmental analysis.

- Other revenue principally includes income from Sky Active, Sky Card, Sky Mobile TV, technical platform services, Easynet Enterprise and Amstrad. Other revenue is recognised, net of any discount given, when the relevant goods or service are provided. Revenue is measured at the fair value of the consideration received or receivable

When the Group sells a set-top box, installation or service and a subscription in one bundled transaction, the Group allocates the total arrangement consideration to the different individual elements based on their relative fair values. Management determines the fair value of individual elements based on vendor specific or third party evidence. The amount of revenue the Group recognises for delivered elements is limited to the cash received.'

The policy ties back perfectly to the segmental analysis. There are no surprises in the policies although the referencing of 'Sky Bet revenues' back to IAS 39 is not a particularly helpful short-cut as it gives no disclosure of the requirements of that standard.

The other broadcaster in our sample is **ITV**. ITV's recognition policy reads as follows:

'Revenue is stated exclusive of VAT and consists of sales of goods and services to third parties. Revenue from the sale of goods is recognised when the Group has transferred the significant risks and rewards of ownership and control of the goods sold and the amount of revenue can be measured reliably. Key classes of revenue are recognised on the following bases:

- Advertising and sponsorship on transmission
- Programme production on delivery
- Programme rights when contracted and available for exploitation
- Participation revenues as the service is provided
- Revenue on barter transactions is recognised only when the goods or services being exchanged are of a dissimilar nature'

While the Group's segmental analysis reads as follows:

'The Management Committee considers the business primarily from a product perspective. The reportable segments are therefore Broadcasting, Global Content, Online and Other. All of the segments reported meet the quantitative thresholds required by IFRS 8, which the Group first adopted in 2007. Management has determined the reportable segments based on the reports reviewed by the Management Committee. The Management Committee comprises the executive directors.

Broadcasting is responsible for commissioning and scheduling programmes on the ITV channels, marketing and programme publicity. It derives its revenue primarily from the sale of advertising airtime and sponsorship. Other sources of revenue are from premium rate services and the digital terrestrial multiplex SDN. The Broadcasting segment also includes the investment in STV group plc (formerly SMG plc).

Global Content derives its revenue primarily from ITV Studios in the UK (a commercial production company), international production centres in America, Germany, Sweden and Australia and the businesses in ITV Global Entertainment ('IGEL'). A proportion of revenue is generated internally via programme sales to the Broadcasting segment. IGEL sells programming and exploits

merchandising and licensing worldwide, and is a distributor of DVD entertainment in the UK.

Online derives its revenue from two main areas: broadband and mobile. Broadband includes itvlocal.com, itv.com and Friends Reunited. Mobile manages ITV's mobile portal and arranges distribution of ITV's channels and content on mobile networks.

Other comprises the Group's 100% interest in Carlton Screen Advertising ('CSA'), which sells cinema screen advertising in the UK, and its 50% interest in Screenvision, which operates cinema screen advertising businesses in continental Europe and the United States.'

Although ITV's revenue policy is clear and simple, it does not directly tie back to the segmental analysis. Advertising and Sponsorship relate to the Broadcasting activity and Programme Production and Programme Rights tie back to Global Content, but ITV does not explain what segments are affected by Participation Revenues and Barter Transactions. Also, it is not clear what part of the policy covers the activities of online.

RDF Media's accounting policy in respect of revenue recognition is as follows:

'Revenue

Revenue is measured by reference to the fair value of consideration received or receivable from customers.

Production

Production revenue comprises broadcaster licence fees and other pre-sales receivable for work carried out in producing television programmes. Production revenue is recognised over the period of the production. Gross profit on production activity is recognised over the period of the production and in accordance with the underlying contract. Overspends on productions are recognised as they arise and underspends are recognised on completion of the productions.

Distribution

Revenue arises from the distribution or other exploitation by the Group of programmes produced by third parties or by the Group, or from the distribution by third parties of programmes produced by the Group. Revenue is recognised when receivable. For completed programmes distributed by the Group, the directors consider revenue to be receivable when the following conditions have been met:

- contractual terms have been agreed
- the contracted sum has been invoiced
- the programme is complete and delivered or available for delivery.

For programmes distributed by third parties, the directors consider that revenue is receivable when the Group has been notified of sums due to it.'

The RDF policy also deals with the contemporary issues around television programme funding.

Other

'Where costs are incurred to produce certain programmes or series where significant contribution is anticipated to come not solely from the initial broadcast licence over the production period, but also from worldwide distribution and exploitation over several years, the Group has adopted an accounting policy whereby the total costs of production are amortised between the contribution derived from the initial licence fee and from future anticipated exploitation.

Production and licence revenues are recognised on a straight line basis over the length of the production as are the costs associated with them. Revenues from exploitation are recognised in line with the Group's existing policy with the balance of production costs amortised in line with revenues recognised versus total anticipated forecasted revenues. The forecasted future exploitation revenues are reviewed regularly to ensure the forecasted gross contribution exceeds the balance of capitalized cost. Where future forecasted revenues reduce permanently versus original estimates, the rate of amortisation increases. Where future forecasted revenues increase, the rate of amortisation will remain as originally estimated.

The rationale for the adoption of the new approach, where applicable, is that the Group is entering into diverse production models in terms of revenue structures, time being invested to produce the content and the ultimate value of the content to the Group. The advantage with this policy is that it more closely matches the costs incurred to produce the asset with the revenues it ultimately will generate.'

This policy demonstrates the traditional fundamental difference between the production and distribution models. Production revenue is recognised over the production period, acknowledging that the activity of creating a commissioned work gives rise to revenue arising across that period. On the other hand, distribution income is recognised at a single point in time when a number of contractual conditions have all been met.

The RDF policy also deals with the contemporary issues of television programme funding. This has been brought about by the reduction in television audiences leading to a reduction of advertising spend and a consequent squeeze by UK broadcasters on spend-per-hour on programming. This has led to producers having to fund an increasing proportion of their programme budgets from elsewhere – often from distribution advances.

RDF's position as producer and distributor enables it to partly self-fund programmes on the basis of future expected distribution revenues. It recognises pre-contracted (eg commissioning broadcaster) revenue on such programmes during the production process, and the balance as it arises on future sales during the distribution cycle. As a matter of interest, where there is significant income forecasted from worldwide exploitation, it apportions the programme cost across the total expected income and amortises it accordingly.

RDF recognises 'production' and 'exploitation of programme rights' as its principal business segments, and these fit in with the revenue recognition policies of production and distribution.

Entertainment Rights defined a single business segment:

'The Group's activities are in one business segment, namely the commercialisation of children's characters and brands. There are no other significant classes of business, either singularly or in aggregate.'

Although having a single business segment, Entertainment Rights went on to define two types of revenue to be recognised, firstly television distribution and production and secondly consumer products: licensing and video, as follows:

Television distribution and production

'Income recognised represents the value of licence fees including withholding tax but excluding VAT. The Group's policy is to recognise the income and associated royalty payable when all of the following criteria are met:

- a licence agreement has been signed by both parties;
- the licensee is able to freely exploit its rights;
- the licensor has no remaining performance obligations;
- the arrangement is fixed and determinable;
- collection of the arrangement fee is reasonably assured; and
- delivery to the broadcaster has occurred.

Any licence fees received in advance which do not meet all of the above criteria are included in deferred income until the above criteria are met.

Consumer products: licensing and video

Revenue from licence and video sales is recognised on the date that the licence revenue is contracted or royalties declared by licensees. Up-front fixed fees are recognised as revenue on contract signature if the following additional criteria are met:

- The contract is non-cancellable;
- The licensee is able to exploit its rights freely; and
- The Company has no significant remaining obligations to perform under the contract'

Of the two types of revenue shown (in the single business segment of Entertainment Rights), the first, television distribution and production, is recognised as two separate business segments by four of the other companies sampled. So within a single segment Entertainment Rights had what most other companies would probably have described as three different segments. Was Entertainment Rights being too coy with its lack of analysis? Its subsequent descent into insolvency means that we shall never find out.

Shed Media recognises three business segments; Broadcasting UK, Broadcasting US (both involving programme production) and Sales of IP rights (income from secondary distribution). Although a mix of type of business and geography, this is explained as follows:

'Management has determined the operating segments based on the reports reviewed by the Board that are used to make strategic decisions. The Board considers the business by type of revenue and geographic location. The Group primarily operates through its offices in London and Brighton UK and in Los Angeles, USA but sells the rights to its programmes worldwide. The Group differentiates between newly

commissioned production revenue both in the UK and the US and revenue arising from the sale of the rights of the Group's library (Intellectual Property (IP) Revenue). Central costs segment represents the cost of the head office function. This operates as an independent function to the trading businesses.

The Board assesses the performance of the operating segments based on a measure of adjusted EBITDA.'

The combination of business type and geography into a single segmental analysis is a logical way of presenting the results of Shed. Its policy on revenue recognition closely mirrors the business segmentation. There are no surprises within its revenue policy, which is as follows:

'Revenue represents amounts receivable for work carried out in producing television programmes and is recognised on the basis of the value of costs related to production activity. Revenue also includes sums receivable from the exploitation of programmes in which the Group owns rights. Gross profit on production activity is recognised based upon the stage of completion of the production and in accordance with the underlying contract.'

'For distribution income the amount recognised in the profit and loss account represents the value of the licence fees including withholding tax but excluding Value Added Tax.'

Distribution income is recognised when:

- an agreement is contracted
 - the arrangement is fixed and determinable.
- And for finished programme sales when the programme is delivered.'

Eros International recognises three business segments:

- theatrical
- home entertainment
- television syndication.

These represent the exploitation of filmed content through (currently) the three most lucrative media.

Its accounting policy on revenue recognition is as follows:

'Revenue recognised represents the value of the licence fee and includes withholding tax but excludes sales taxes. It is recognised once the following criteria are met:

- there is persuasive evidence of a sale or licensing arrangement agreement
- the film is complete and available for delivery
- collection of the revenue is reasonably assured
- the fee is fixed and determinable.

The following additional criteria apply in respect of these revenue streams:

Theatrical – Revenue is stated at the minimum guarantee due, where applicable, plus the declared Group's share of box office receipts in excess of the minimum guarantee.

Digital and Home entertainment – DVD, CD and Video revenue is recognised on the date the licence revenue is contracted or declared. Provision is made for returns where applicable. New media revenues are recognised at the earlier of when the content is accessed or declared.'

These are clearly set out policies, once again linked into the segmental analysis. Much of the language used is from the US standard SOP-002, so phrases such as ‘persuasive evidence’ may not immediately resonate with UK users, but the intention is clear.

DCD Media segments its activities into programme production, programme distribution and DVD sales (there are two further segments of Internet/TV broadcasting and Educational music courses, but revenues were insignificant).

Revenue Recognition

‘Production revenue represents amounts receivable from producing programme content and is recognised over the period of the production in accordance with the underlying signed contract. The revenue is recognised through the different stages of production, including pre-production, filming, post-production and delivery to the commissioning broadcaster. The assessment of the stage of completion is made by reference to production costs incurred and after consultation with production staff. Attributable profit is calculated by recognising all appropriate costs up to the stage of production completion, and amortising production costs in the proportion that the revenue recognised in the period bears to estimated total revenue from the programme. The carrying value of programme costs in the balance sheet is subject to an annual impairment review.

Where productions are in progress at the period end and where billing exceeds the value of work done, the excess is classified as deferred income and is shown within trade payables. Distribution revenue arises from the licencing of programme rights which have been obtained under distribution agreements with either external parties or Group companies. Distribution revenue is recognised in the income statement on signature of the licence agreement, and represents amounts receivable on such contracts.’

‘Revenue from sales of DVDs and other sales is the amounts receivable from invoiced sales during the year.’

Once again, the policy ties in with the segmental analysis. DCD’s distribution policy lacks real depth of explanation compared with some other companies surveyed.

The principal business segments of **ContentFilm** are International Sales, US Home Entertainment Distribution and Film Production. It also recognises UK Distribution and Licensing and merchandising as segments, but these contribute insignificant levels of revenues.

Its policy of revenue recognition is:

‘Revenue is measured by reference to the fair value of consideration received or receivable by the group for goods supplied and services provided, excluding value added tax and trade discounts. Revenue is recognised upon the performance of services or transfer of risk to the customer.

Income from the exploitation of film and television rights is recognised based upon the contractual terms of each agreement. Income is recognised on a receivable basis where there is reasonable contractual certainty that the revenue is receivable and will be received. In circumstances where the income is dependent on the fulfilment of further contractual obligations, income is recognised when the Group has performed the obligations necessary under the contract to fulfil those contractual obligations.

In respect of the supply of DVD, video and audio inventory, income is recognised at the point at which goods are despatched and recorded net of sales returns.’

The first paragraph of the policy is generic wording straight from the standard. The second paragraph covers the International Sales aspect of the business and the third paragraph relates to DVD sales, the activity of the US Home Entertainment business.

Boomerang’s segmental analysis is limited to the following statement:

‘A business segment is a group of assets and operations engaged in providing services that are subject to risks and returns that are different from those of other business segments. The principal activity of the group is that of independent television production. The customer base and distribution channels for each group company are the same so that for the purposes of IAS 14 Segment Reporting, the consolidated entity operates in one business segment. As the group only operates in one business segment, no additional business segmental analysis has been shown.

All business activities are located within the UK and therefore the group operates in a single geographical segment.’

In its business review, Boomerang describes its activities as being in six genres of television production, as well as being active in Post-Production, Radio, Talent Management and Digital Media. The segmental analysis and business review would appear to be out of step.

Boomerang's revenue recognition policy is fairly simple and specific to programme production. It reads as follows:

'Revenue (which excludes VAT) represents amounts receivable for work carried out in the production and post-production of television and radio programmes and is recognised over the period of the related activity. Gross profit on production activity is recognised over the period of the production and in accordance with the underlying contract. Cost overspends on productions are recognised as they arise and cost savings are recognised on completion of the productions in line with the underlying contractual agreement. Where productions are in progress and where sales invoiced exceed the cost of work done, the excess is shown as deferred income. Where the value of work done exceeds the invoiced amount, the excess is shown as accrued income. When it is probable that total production costs will exceed contract revenue, the expected loss is recognised as an expense immediately.'

Elsewhere in the financial statements, reference is made to how the business amortises programme catalogues. However, no reference is made to dealing with any revenues arising from these catalogues in the revenue recognition policy.

DQ Entertainment segments its business into Animation, Gaming and Distribution. Its revenue recognition policy is as follows:

i. Production service fee and licensing revenue

'Revenue represents amounts receivable for production services rendered and is recognised in the income statement in proportion to the stage of completion of the transaction at the balance sheet date. The stage of completion can be measured reliably and is assessed by reference to work completed as on the balance sheet date. The Group uses the services performed to date as a percentage of total services to be performed as the method for determining the stage of completion.

Where services are in progress and where the amounts invoiced exceed the revenue recognised, the excess is shown as deferred income. Where the revenue recognised exceeds the invoiced amount, the amounts are classified as unbilled revenue.

The stage of completion for each project is estimated by the management at the onset of the project by breaking each project into specific activities and estimating the efforts required for the completion of each activity. Revenue is then allocated to each activity based on the proportion of efforts required to complete the activity in relation to the overall estimated efforts. The management's estimates of the efforts required in relation to the stage of completion, determined at the onset of the project, are revisited at the balance sheet date and any material deviations from the initial estimate are recognised in the income statement.

The Group's services are performed by a determinable number of acts over the duration of the project and hence revenue is not recognised on a straight-line basis. Contract costs that are not probable of

being recovered are recognised as an expense immediately.

Revenue from the licensing of distribution rights (including withholding tax) is recognised on a straight-line basis over the term of the licensing agreement and in the case of the license fee from co-production rights on the date declared by the licensee.

No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due.

ii. Government grants

Government grants are not recognised until there is reasonable assurance that the Group will comply with the conditions attaching to them and the grants will be received. Grants that compensate the Group for the cost of an asset are recognised on receipt by way of deduction from the carrying cost of the asset. The grant is recognised as income over the life of the depreciable asset by way of a reduced depreciation charge. Grants that compensate the Group for expenses incurred are recognised as reduction from relevant head of expense in the income statement on a systematic basis in the same periods in which the expenses are incurred.'

Here the focus appears to be on the production service activity, with a short reference to distribution revenues. Information on how the group estimates the stage of completion is useful in understanding the application of the policy.

There is a reference in the policy to government grants. A number of governments try to attract animation companies to their country in an effort to create or sustain an indigenous animation industry, principally through the operation of tax incentive or grant schemes, and this part of the policy deals with that (often significant) stream of cashflow.

Publishing & events companies revenue analysis

Of the 26 companies in this sub-sector, 19 are on the main market with the balance on AIM, although one (SPG Group) has delisted and one (Expomedia) is no longer trading.

We selected six companies to examine revenue recognition policies in greater depth. These are:

Company	AIM/FTSE
News Corporation	FTSE
Reed Elsevier plc	FTSE
Pearson plc	FTSE
Yell Group plc	FTSE
Future plc	FTSE
Bloomsbury Publishing plc	FTSE

NewsCorp's activities span the content-exploiting media sector. Its segmented business activities comprise Filmed Entertainment, Television, Cable Network Programming, Direct Broadcast Satellite Television on the television and film side and Magazines and Inserts, Newspapers and Information Services and Book Publishing on the publishing side.

For the purpose of this section on publishing, we shall focus on the revenue recognition policy relating to the latter three activities. Its policy reads:

'Newspaper and Information Services, Magazine and Inserts and Book Publishing – Advertising revenue from newspapers, inserts and magazines is recognised when the advertisements are published. Subscription revenues from the Company's print and online publications and electronic information services

is recognised as earned, pro rata on a per-issue basis, over the subscription period. Revenues earned from book publishing are recognised upon passing of control to the buyer.'

A very simple, clear and neat policy compared with some we have seen in the audio & television sector.

Reed Elsevier splits its business into four segments, being two publishing streams (Elsevier and LexisNexis) and two events streams (Reed Exhibitions and Reed Business).

Its revenue recognition policy starts with a general point:

'Revenue represents the invoiced value of sales less anticipated returns on transactions completed by performance, excluding customer sales taxes and sales between the combined businesses.'

It goes on to say:

'Revenues are recognised for the various categories of turnover as follows:

- subscriptions – on periodic despatch of subscribed product or rateably over the period of the subscription where performance is not measurable by despatch;
- circulation – on despatch;
- advertising – on publication or over the period of online display; and
- exhibitions – on occurrence of the exhibition.

Where sales consist of two or more independent components whose value can be reliably measured, revenue is recognised on each component as it is completed by performance, based on attribution of relative value.'

Again, simple and clear compared with audio & televisual, although perhaps more detail could be given about subscription income not measurable by despatch – presumably this would relate to online subscriptions.

The business segmentation of **Pearson** reflects the market sectors in which it operates rather than the type of goods or service it offers. Its 2008 financial statements included early adoption of IFRS 8 and the financial overview at the front end of these statements tied in to the segmental analysis in the body of the financial statements. The segments are: Education-US, Education-International, Professional, FT Publishing, Interactive Data and Penguin. Its revenue policy is as follows:

'Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services net of value-added tax and other sales taxes, rebates and discounts, and after eliminating sales within the Group. Revenue from the sale of books is recognised when title passes. A provision for anticipated returns is made based primarily on historical return rates. If these estimates do not reflect actual returns in future periods then revenues could be understated or overstated for a particular period.'

Circulation and advertising revenue is recognised when the newspaper or other publication is published. Subscription revenue is recognised on a straight-line basis over the life of the subscription. Where a contractual arrangement consists of two or more separate elements that can be provided to customers either on a stand-alone basis or as an optional extra, such as the provision of supplementary materials with textbooks, revenue is recognised for each element as if it were an individual contractual arrangement.

Revenue from multi-year contractual arrangements, such as contracts to process qualifying tests for individual professions and government departments, is recognised as performance occurs. The assumptions, risks, and uncertainties inherent in long-term contract accounting can affect the amounts and timing of revenue and related expenses reported. Certain of these arrangements, either as a result of a single service spanning more than one reporting period or where the contract requires the provision of a number of services that together constitute a single project, are treated as long-term contracts with revenue recognised on a percentage of completion basis. Losses on contracts are recognised in the period in which the loss first becomes foreseeable. Contract losses are determined to be the amount by which estimated total costs of the contract exceed the estimated total revenues that will be generated by the contract.

On certain contracts, where the Group acts as agent, only commissions and fees receivable for services rendered are recognised as revenue. Any third-party costs incurred on behalf of the principal that are rechargeable under the contractual arrangement are not included in revenue.

Income from recharges of freight and other activities which are incidental to the normal revenue generating activities is included in other income.'

The increasing importance of digital publishing, together with other forms of online delivery and consumption, should add something to the mix.

Pearson goes into more detail than Newscorp or Reed, detailing its returns policy for example. The detail in the policy is very useful for the user, although the policy did not explain which parts related to which segment(s).

Yell carries out the business of publishing classified directories. It segments its business geographically, between the three principal territories in which it trades; the US, UK and Spain. With effectively a single-stream revenue model across a number of territorial markets, we would expect a simple revenue recognition policy, and the company does not disappoint. The policy is:

'Group revenue, after deduction of sales allowances, value added tax and other sales taxes, comprises the value of products provided by Group undertakings. Revenue from classified directories and other directories, mainly comprising advertising revenue, is recognised in the income statement upon completion of delivery to the users of the directories. Other revenue, principally from internet and voice products, is recognised from the point at which service is first provided over the life of the contract.'

Once again, clear and simple. Only when advertisers can derive benefit (upon delivery of directories) does Yell recognise the revenues derived from them.

Future is a specialist magazine publisher. In 2008, it reported under IAS 14. Its primary segmental analysis is geographical, splitting operations between UK and US. It has a secondary segmental analysis by type of magazine publication, between Games (32%), Music & Movies (21%), Technology (27%) and Active (20%). There is a tertiary split by type of service/product which is disclosed in the business review, as Circulation 60%, Advertising 31%, Customer publishing 5%, Licensing Events and Other 4%.

All information in the business review ties through to the same headings in the body of the financial statements. Future's revenue recognition policy starts out in generic fashion, but then homes in on the service/product types as follows:

'Revenue from the sale of goods is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer. Revenue from services rendered is recognised in the income statement once the service has been completed. Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Group's activities. Revenue is shown net of value added tax, estimated returns, rebates and discounts and after eliminating sales within the Group.

The following recognition also applies:

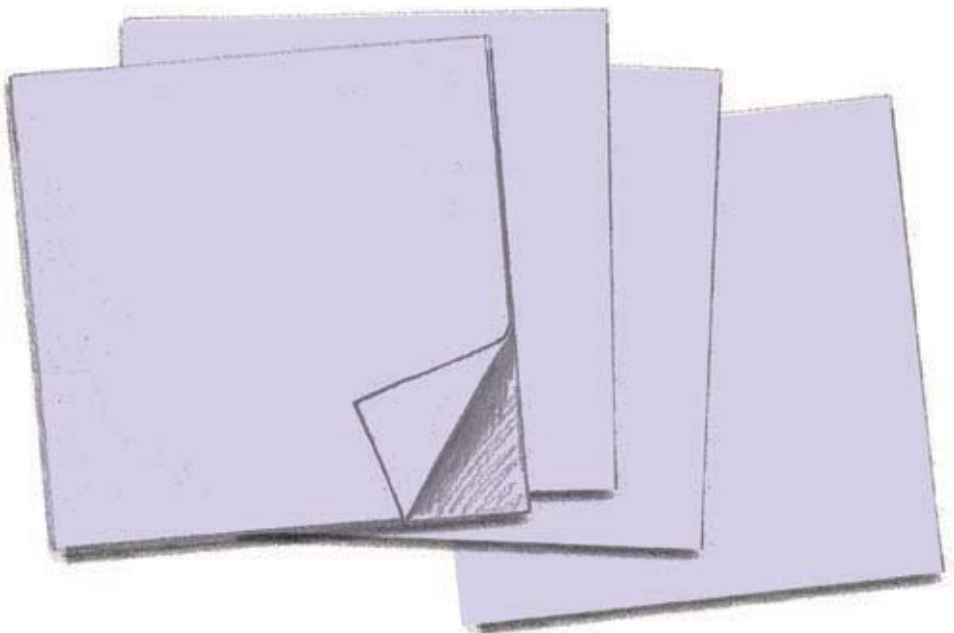
- Magazine newsstand circulation and advertising revenue is recognised according to the date that the related publication goes on sale

- Event income is recognised when the event has taken place
- Licensing revenue is recognised on the supply of the licensed content
- Other revenue is recognised at the time of sale or provision of service'

Bloomsbury's business segmentation is considered secondary to its geographic segmentation. Although its Chief Executive Statement talks of the restructuring of the Group into two overarching divisions; Specialist and Trade, the business segmentation is into the product areas of Adult, Children's (falling under the trade division) and Reference (under the specialist division). It will be interesting to see where it goes next year with its segmental analysis with the introduction of IFRS 8. The increasing importance of digital publishing, together with other forms of online delivery and consumption, should also add something to the mix. Its policy on revenue recognition is:

'Revenue represents the amount derived from the provision of goods, services and rights falling within the Group's ordinary activities, after deduction of trade discounts, value added tax and anticipated returns. Revenue from book publishing is recognised on delivery. Revenue from the sale of publishing and distribution rights, including film, paperback, electronic, overseas publishing rights and sponsorship, is recognised on the delivery of the related content. Revenue from database contracts is recognised in accordance with the stage of completion of contractual services provided.'

The policy for the publishing side of the business is fairly standard, with the greatest judgment probably needed within the area of anticipated returns. Compare **Bloomsbury's** disclosure with **Pearson's** disclosure on returns; the latter goes into the detail of the provision being based upon historical patterns, and warns that deviation from this leads to over or underprovisions.



Advertising & marketing services companies revenue analysis

Of the 44 companies in this sub-sector, eight are on the main market with the balance on AIM, although seven (Interactive Prospective Targeting, MKM, Research Now, Essentially, Cagney, International Marketing & Sales, and Optimisa) have delisted and two (Delling Group and Vision Media Group) are no longer trading.

We selected four companies to examine revenue recognition policies in greater depth. These are:

Company	AIM/FTSE
WPP plc	FTSE
M&C Saatchi plc	AIM
Creston plc	FTSE
Aegis Group plc	FTSE

The principal activities of companies in the advertising & marketing services sub-sector, and the revenues that arise from these activities, are somewhat different from the other sub-sectors we have looked at.

Revenue for audio, televisual and publishing is derived from the creation and exploitation of ‘content’ IP. In the advertising & marketing services arena, however, revenues are generated from the performance of services for clients. These are normally charged on a time, contract rate or commission basis.

The services provided are either internally-generated and labour-based (such as creative advertising, public relations or research) or are externally sourced (such as media buying).

Consequently, the profile of revenue recognition within the advertising & marketing services area is a lot closer to that of, say, professional service firms than television and film companies. This can be seen when looking at the revenue accounting policy adopted in this area. A common yardstick used within the advertising world is ‘Billings’

as opposed to ‘Revenues’. Billings comprise everything an agency invoices to its clients, including all media buying done by the agency for the client. Revenue includes the commissions earned on media buying, but is net of the cost of media. Most companies in this sub-sector report a top-line of ‘Billings’ in their income statements, followed by ‘Revenue’.

The table below summarises the approach adopted by the four companies in our sample.

Table 12. Billings v Revenue disclosure

Company	WPP	M&C Saatchi	Creston	Aegis
Top line description	Billings	Billings	Turnover (billings)	Turnover – amounts billed to clients
Second line	Revenue	Revenue	Revenue	Revenue
Reconciliation between the two	No	No	No	No

WPP provides a definition within its financial glossary:

'Billings comprise the gross amounts billed to clients in respect of commission-based/fee-based income together with the total of other fees earned.'

M&C Saatchi provides a definition within its accounting policy linking billings to revenue:

- 'Billings represents the gross amounts billed to clients in respect of revenue earned and other client recharges, net of discounts and sales taxes
- Revenue comprises commission and fees earned in respect of billings'

Creston defines both turnover and revenue, but does not link the two.

None of the companies include a figure on the face of the income statement for the difference between billings and revenue. They explain the difference in a variety of ways.

Billings are an industry standard measure in advertising and deserve recognition within financial statements, but should they be disclosed on the face of the income statement, as a stand-alone number?

Paragraph 8 of **IAS 18 'Revenue'** explains why gross income from media buying is not included within revenue:

...Similarly, in an agency relationship, the gross inflows of economic benefits include amounts collected on behalf of the principal and which do not result in increases in equity for the entity. The amounts collected on behalf of the principal are not revenue. Instead, revenue is the amount of commission.

There is no further guidance within IAS 18 with respect to disclosure. A helpful point was included in **Paragraph G72 of appendix G to FRS 5:**

Where a seller acts as agent, it is encouraged, where practicable, to disclose the gross value of sales throughput as additional, non-statutory information. Where such disclosure is given, a brief explanation of the relationship of recognised turnover to the gross value of sales throughput should be given.

Given that WPP is a business covering all the bases of the sub-sector, it is a good place to start analysing the specific policies disclosed.

Aegis defines turnover and revenue in consecutive sentences, creating an implied link between the two:

- 'Turnover (amounts invoiced to clients) represents amounts invoiced for media handled by the Group on behalf of clients, together with fees invoiced for media and research services provided, net of discounts, VAT and other sales related taxes
- Revenue is the value of media and research fees and commissions earned by the Group'

WPP provides the following operating segmental rationale:

'The Group is a leading worldwide communications services organisation offering national and multinational clients a comprehensive range of communications services.

For management purposes, the Group is currently organised into four operating segments – Advertising and Media Investment Management; Information, Insight & Consultancy; Public Relations & Public Affairs; and Branding & Identity, Healthcare and Specialist Communications. These disciplines are the basis on which the Group reports its primary information. Operating segments are aggregated where they have similar economic characteristics, provide similar products and services and serve similar clients.'

WPP's revenue recognition policy is closely aligned to the operating segmental analysis, and reads as follows:

'Revenue comprises commission and fees earned in respect of amounts billed. Direct costs include fees paid to external suppliers where they are retained to perform part or all of a specific project for a client and the resulting expenditure is directly attributable to the revenue earned. Revenue is stated exclusive of VAT, sales taxes and trade discounts.

Advertising & Media Investment Management

Revenue is typically derived from commissions on media placements and fees for advertising services. Revenue may consist of various arrangements involving commissions, fees, incentive-based revenue or a combination of the three, as agreed upon with each client. Revenue is recognised when the service is performed, in accordance with the terms of the contractual arrangement. Incentive-based revenue typically comprises both quantitative and

qualitative elements; on the element related to quantitative targets, revenue is recognised when the quantitative targets have been achieved; on the element related to qualitative targets, revenue is recognised when the incentive is received or receivable.

Information, Insight & Consultancy

Revenue recognised in proportion to the level of service performed for market research contracts is based on proportional performance. In assessing contract performance, both input and output criteria are reviewed. Costs incurred are used as an objective input measure of performance. The primary input of all work performed under these arrangements is labour. As a result of the relationship between labour and cost, there is normally a direct relationship between costs incurred and the proportion of the contract performed to date. Costs incurred as a proportion of expected total costs is used as an initial proportional performance measure.

This indicative proportional performance measure is subsequently validated against other more subjective criteria (i.e. relevant output measures) such as the percentage of interviews completed, percentage of reports delivered to a client and the achievement of any project milestones stipulated in the contract. In the event of divergence between the objective and more subjective measures, the more subjective measures take precedence since these are output measures.

While most of the studies provided in connection with the Group's market research contracts are undertaken in response to an individual client's or group of clients' specifications, in certain instances a study may be developed as an off-the-shelf product offering sold to a broad client base. For these transactions, revenue is recognised when the product is delivered. Where the terms of transaction provide for licensing the product on a subscription basis, revenue is recognised over the subscription period on a straight-line basis or, if applicable, based on usage. Substantially all services are provided on a fixed price basis. Pricing may also include a provision for a surcharge where the actual

labour hours incurred in completing a project are significantly above the labour hours quoted in the project proposal. In instances where this occurs, the surcharge will be included in the total revenue base on which to measure proportional performance when the actual threshold is reached provided that collectibility is reasonably assured.

Public Relations & Public Affairs and Branding & Identity, Healthcare and Specialist Communications

Revenue is typically derived from retainer fees and services to be performed subject to specific agreement. Revenue is recognised when the service is performed, in accordance with the terms of the contractual arrangement. Revenue is recognised on long-term contracts, if the final outcome can be assessed with reasonable certainty, by including in the income statement revenue and related costs as contract activity progresses.'

The WPP policy is comprehensive, but the wording is not particularly user-friendly. For example the first part of the policy on Information, Insight and Consultancy regarding market research contracts runs for over 160 words. It could be halved to:

'Revenue from market research contracts is recognised during the contract on a proportional performance basis as the client derives benefits. Typical measures of deriving benefit include the percentage of interviews completed, percentage of reports delivered to a client or the achievement of any project milestones stipulated in the contract. Where measures of output like these are not available, proportional performance is calculated on the basis of the cost of work carried out to date compared with overall expected cost.'

The **M&C Saatchi** primary segmental analysis is geographical. The secondary analysis is by business type, split between advertising and media buying, PR and consulting.

Its revenue recognition policy is as follows:

‘Billings represents the gross amounts billed to clients in respect of revenue earned and other client recharges, net of discounts and sales taxes. Revenue comprises commission and fees earned in respect of billings. Each type of revenue is recognised on the following basis:

- a. Project fees are recognised over the period of the relevant assignments or agreements, in line with incurred costs
- b. Retainer fees are spread over the period of the contract on a straight-line basis
- c. Commission on media spend is recognised when the advertisements appear in the media’

WPP and M&C Saatchi are probably at either end of the disclosure spectrum. The WPP policy is comprehensive, but over complex in places. M&C Saatchi’s policy is clear and simple but, unlike WPP’s policy, its terminology does not tie back to the business segmental analysis. Also, does its simplicity mask a lack of detail which the reader might otherwise find useful?

Creston divides its business into two segments, Insight and Communications. Creston’s revenue recognition policy differentiates between turnover and revenue, and reads as follows:

Turnover

‘Turnover represents amounts received or receivable from clients, for the rendering of services and is stated after deduction of trade discounts and excluding value added tax or similar sales taxes outside of the United Kingdom. Turnover is recognised at fair value as service activity progresses on the following basis:

1. Project fees are recognised over the period of the relevant assignments or agreements
2. Retainer fees are spread over the period of the contract on a straight-line basis
3. Third-party production fees are recognised at the point the client accepts delivery of each component of a project

Turnover includes all charges paid to external suppliers where they are retained to perform part or all of a client assignment.

Revenue

Communications

The revenue derived from commissions on media placements, retainer fees, projects and fees for creative services are recognised on each contract in proportion to the level of services performed. The level of services performed are assessed based on the relevant criteria including proportion of costs incurred, time-based recognition for retainers and milestones. Incentive-based revenue is recognised when the relevant target has been met.

Insight

Revenue is derived from fees on research assignments. These are recognised on each assignment in proportion to the level of completion. The level of completion is assessed using costs incurred (primarily employment costs) as a proportion of total costs. On long-term contracts, revenue is recognised as contract activity progresses.’

Creston’s revenue recognition policy is fairly standard. That part dealing with turnover looks at Creston’s activities from a generic activity perspective. That part dealing with revenue looks at

recognition specifically in each of the two business segments.

Aegis operates in two business segments, media communications and market research. Its revenue recognition policy ties back to each segment as follows:

‘Turnover (amounts invoiced to clients) represents amounts invoiced for media handled by the Group on behalf of clients, together with fees invoiced for media and research services provided, net of discounts, VAT and other sales related taxes.

Revenue is the value of media and research fees and commissions earned by the Group.

Media revenue is recognised when charges are made to clients, principally when advertisements appear in the media. Fees are recognised over the period of the relevant assignments or agreements. Performance related income is recognised when it can be reliably estimated whether, and the extent to which, the performance criteria have been met.

For the market research business, revenue is recognised on the satisfactory completion of a specific phase of a project. Provision is made for losses on a project when identified. Invoices raised during the course of a project are booked as deferred income on the balance sheet until such a time as the related revenue is recognised in the income statement.’

The wording used here is slightly ambiguous, ‘Media revenue is recognised when charges are made to clients’ – does this mean at the point at which invoices are raised? The next phrase: ‘principally when advertisements appear in the media.’ seems to qualify when Aegis makes charges to its clients rather than when it recognises income.

Overall comments & conclusions

Audio & televisual

We have analysed film and television revenue recognition policies in some detail in previous surveys. IFRS does not appear to have altered the overall approach to revenue recognition policies in this sub-sector with any significance.

Publishing & events

Revenue recognition appears to be a lot simpler and clearer in the publishing & events arena than in the audio & televisual. This is probably due to the capital costs of content origination in film and television being a lot higher per project than in publishing. Higher project costs lead to more complex funding arrangements and the creation of sometimes complex IP rights. This in turn requires more complicated accounting to properly reflect the substance of transactions.

Advertising & marketing services

The main issues around revenue recognition policies in advertising & marketing services are covered off in IAS 18, and broadly revolve around the nature of services being provided and the consequent timing of their recognition. The principal points raised by this survey concern the question of how and where gross billings should be disclosed.

Overall

A number of points common across all sub-sectors need to be addressed:

The level of policy disclosure

Do companies look for short, sharp clear disclosures in their policies, or use more descriptive and detailed policies? Our view is: If in doubt, disclose.

Such disclosure should be a considered and relevant summary of how the board have interpreted the various Reporting Standards in relation to their business.

Improved cross-referencing between segmental analysis and revenue recognition policy

Some companies appear to be adopting an absolutely minimum disclosure approach to business segmental analysis, and their lack of effort is probably not welcomed by their stakeholders. The additional disclosure required by the application of IAS 14 (over the previous UK standard) has brought more structure and analysis to financial

statements. Many companies are logically cross-referring their segmental analysis to their revenue recognition policies, and using similar descriptive language in both segmental analysis and revenue recognition accounting policies. This is welcome and its more widespread adoption should be encouraged as it presents a joined-up approach and makes the task of understanding the financial statements much easier for the user.

IFRS 8 presents opportunity to improve cross-referencing between the business review, segmental analysis and revenue recognition

This joined-up approach extends in many cases to the business and divisional reviews at the front end of financial statements. The requirement of the incoming IFRS 8 for segmental analysis to mirror management's own view of the different strands of the business should in theory make it easier to tie in the business review with segmental analyses. This form of effective cross-referencing

should be adopted by all companies for the benefit of their stakeholders. It presents a great opportunity for all companies to improve cross referencing between the business review at the front of financial statements, the segmental analysis in the body of the financial statements and the accounting policy on revenue recognition.

Impact of future revenue still unknown

The development of joined-up, online, new-media based products, with more complex revenue models, is likely to give rise to some interesting revenue recognition policies over the coming years. The greatest challenge is likely to arise from content owners exploiting their product across a number of media on a variety of fixed and variable revenue models under a single contract.

Appendix 1

List of companies surveyed

Audio & televisual

Company	AIM/FTSE
Air Music and Media Group plc (MBL Group plc)	AIM
Apace Media plc	AIM
Boomerang Plus plc	AIM
BSkyB plc	FTSE
Cellcast plc	AIM
Chrysalis plc	FTSE
ContentFilm plc	AIM
Coolabi plc	AIM
DCD Media plc	AIM
Dori Media Group Limited	AIM
DQ Entertainment plc	AIM
Entertainment Rights plc†	FTSE
Eros International plc	AIM
Galleon Holdings plc	AIM
HandMade plc	AIM
Independent Media Distribution plc	AIM
Intandem Films plc	AIM
ITV plc	FTSE
Mama Group plc	AIM
Metrodome Group plc	AIM
Milestone Group plc	AIM
Motive Television plc	AIM
Music Copyright Solutions plc (Conexion Media Group plc)	AIM
Pinewood Shepperton plc	FTSE
Prime Focus London plc	AIM
RDF Media Group Limited*	AIM
Ten Alps plc	AIM
The Works Media Group plc	AIM
The Indian Film Limited	AIM
The Local Radio Company plc*	AIM
Shed Media plc	AIM
STV Group plc	FTSE
Talent Group plc	AIM
UBC Media Group plc	AIM
UTV Media plc	FTSE
X-Phonics plc	AIM
Zest Group plc	AIM

†No longer trading

*Delisted

Publishing & events

Company	AIM/FTSE
Bloomsbury Publishing plc	FTSE
Cheerful Scout plc	AIM
Daily Mail and General Trust plc (DMGT)	FTSE
Euromoney Institutional Investor plc	FTSE
Expomedia Group plc†	AIM
Future plc	FTSE
Haynes Publishing Group plc	FTSE
Huveaux plc	AIM
Informa plc	FTSE
ITE Group plc	FTSE
Johnston Press plc	FTSE
Knowledge Technology Solutions plc (now Arcontech Group plc)	AIM
Mecom Group plc	FTSE
Moneysupermarket.com Group plc	FTSE
Motivcom plc	AIM
Pearson plc	FTSE
Reed Elsevier	FTSE
Rightmove plc	FTSE
SPG Media Group plc*	AIM
Tarsus Group plc	FTSE
The Quarto Group, Inc	FTSE
Trinity Mirror plc	FTSE
United Business Media plc	FTSE
Vitesse Media plc	AIM
Wilmington Group plc	FTSE
Yell Group plc	FTSE

†No longer trading

*Delisted

Advertising & marketing services

Company	AIM/FTSE
4imprint Group plc	FTSE
Aegis Group plc	FTSE
Altitude Group plc	AIM
Avesco Group plc	AIM
BrainJuicer Group plc	AIM
Cagney plc*	AIM
Cello Group plc	AIM
Centaur Media plc	FTSE
Chime Communications plc	FTSE
Creston plc	FTSE
Delling Group plc†	AIM
Digital Marketing Group plc	AIM
Ebiquity plc (Thomson Intermedia)	AIM
Ekay (WFCA plc)	AIM
Electric Word plc	AIM
Essentially Group Ltd*	AIM
Freshwater UK plc	AIM
Hasgrove plc	AIM
Huntsworth plc	FTSE
i-design group plc	AIM
Immedia Group plc	AIM
Infoserve Group plc	AIM
Interactive Prospect Targeting Holdings plc*	AIM
International Marketing & Sales Group Ltd*	AIM
M&C Saatchi plc	AIM
Media Square plc	AIM
MKM Group plc*	AIM
Next Fifteen Communications Group plc	AIM
Optimisa plc*	AIM
Parallel Media Group plc	AIM
Phorm Inc	AIM
Pixel Interactive Media Ltd	AIM
Progressive Digital Media Group plc (TMN Group plc)	AIM
Research Now plc*	AIM
SpaceandPeople plc	AIM
The Mission Marketing Group plc	AIM
Thomson Reuters plc	FTSE
Touch Group plc	AIM
Toluna plc	AIM
Totally plc	AIM
Twenty plc	AIM
Vision Media Group (International) plc†	AIM
WPP plc	FTSE
YouGov plc	AIM
†No longer trading	
*Delisted	

Other

Company	AIM/FTSE
Adventis Group plc	AIM
Adwalker plc*	AIM
Avanti Screenmedia Group plc†	AIM
Catalyst Media Group plc	AIM
CSS Stellar plc	AIM
Deal Group Media plc (now Asia Digital Holdings plc)	AIM
First Artist Corporation plc	AIM
IncaGold plc	AIM
Infoscreen Networks plc	AIM
Landround plc*	AIM
MediaZest plc	AIM
Mirada plc	AIM
NetPlay TV plc	AIM
Printing.com plc	AIM
Retec Digital plc*	AIM
The Character Group plc	AIM
†No longer trading	
*Delisted	

Appendix 2

Business combinations surveyed

Company	Acquisition	£m Total intangibles	£m Goodwill	£m IIA	IIA%
Audio & television					
BSkyB plc	Amstrad	109.0	104.0	5.0	4.6%
UTV Media plc	FM104	49.0	12	37	75.5%
HandMade plc	HandMade holdings	41.5	9.6	31.9	76.9%
ITV plc	12 Yard	35.0	31.0	4.0	11.4%
Shed Media plc	Outright/Wall to Wall/Twenty Twenty	47.3	33.6	13.7	29.0%
DCD Media	September/Prospect/West Park	22.4	12.6	9.8	43.8%
RDF Media Group Limited	Foundation/Comedy Unit/Presentable	21.2	7.6	13.6	64.2%
Mama Group plc	Angel Music Group	5.4	2.9	2.5	46.3%
HandMade plc	Sequence films	5.3	2.8	2.5	47.2%
Mama Group plc	Mean Fiddler Holdings/GAY	4.6	4.5	0.1	2.2%
UTV Media plc	Tibus	3.8	3.8	0	0.0%
Ten Alps plc	Mongoose	3.6	2.3	1.3	36.1%
Ten Alps plc	DBDA	3.2	1.9	1.3	40.6%
Ten Alps plc	Sovereign	2.9	2.5	0.4	13.8%
VTR plc	Machine Effects	1.7	1.7	0	0.0%
Eros International plc	Ayngaran	1.0	0	1.0	100.0%
RDF Media Group Limited	History Rights	0.7	0	0.7	100.0%
Publishing & events					
Informa plc	Datamonitor plc	617.0	385.0	232.0	37.6%
Moneysupermarket.com Group plc	Moneysupermarket.com Financial Group	332.0	125.0	207.0	62.3%
Pearson plc	Harcourt Assessment	314.0	113.0	201.0	64.0%
Reed Elsevier	Buyerzone Inc	303.0	101.0	202.0	66.7%
Pearson plc	eCollege	283.0	181.0	102.0	36.0%
Reed Elsevier	[others 2008]	225.0	117.0	108.0	48.0%
Pearson plc	Harcourt Education	165.0	68.0	97.0	58.8%
Trinity Mirror plc	Smart media services/Financial jobs online	104.4	57.7	46.7	44.7%
United Business Media plc	[all 2007 acquisitions]	79.6	58.1	21.5	27.0%
Pearson plc	[others 2007]	71.0	55.0	16.0	22.5%
United Business Media plc	[all 2008 acquisitions]	62.8	44.1	18.7	29.8%
Pearson plc	[others 2008]	51.0	15.0	36.0	70.6%
Yell plc	[various US acquisitions 2008]	43.6	32.6	11.0	25.2%
Informa plc	Haworth press	38.0	7.8	30.2	79.5%
Pearson plc	Money Media	35.0	25.0	10.0	28.6%
Informa plc	[others 2007]	33.8	4.8	29.0	85.8%
Yell plc	[various US acquisitions 2007]	31.9	24.1	7.8	24.5%
Yell plc	Publicom SA	30.9	19.8	11.1	35.9%
Informa plc	Investment Scorecard Inc	30.0	11.0	19.0	63.3%
United Business Media plc	Vintage Filings	26.2	21.0	5.2	19.8%
Motivcom plc	Zibrant	14.3	12.4	1.9	13.3%
Trinity Mirror plc	Totallyfinancial.com	14.0	10.8	3.2	22.9%
Johnston Press plc	Archant	13.4	3.1	10.3	76.9%
Wilmington Group plc	The Matchett Group	12.1	8.9	3.2	26.4%

Company	Acquisition	£m Total intangibles	£m Goodwill	£m IIA	IIA%
Informa plc	Multilingual Matters/Keegan Paul/ INMEX/Binet exhibitions and others	11.6	2.1	9.5	81.9%
ITE Group plc	Primeexpo Northwest	11.2	4.0	7.2	64.3%
Informa plc	Online congress	10.5	5.2	5.3	50.5%
Wilmington Group plc	AP/Aspire	9.2	4.8	4.4	47.8%
Wilmington Group plc	Mercia Group	8.8	2.5	6.3	71.6%
ITE Group plc	Siberian Fairs	8.3	2.4	5.9	71.1%
Haynes Publishing plc	Vivid Holding	7.2	2.7	4.5	62.5%
Trinity Mirror plc	Rippleffect Studio	6.3	4.5	1.8	28.6%
Trinity Mirror plc	Globespan media	5.9	3.3	2.6	44.1%
Informa plc	Productivity press	5.0	1.4	3.6	72.0%
Trinity Mirror plc	Email4property	5.0	3.5	1.5	30.0%
Bloomsbury Publishing plc	John Wisden	3.1	1.6	1.5	48.4%
Trinity Mirror plc	The Career Engineer	2.2	1.3	0.9	40.9%
Bloomsbury Publishing plc	Oxford International publishers	2.1	1.2	0.9	42.9%
Bloomsbury Publishing plc	Arden Shakespeare	2.1	0.5	1.6	76.2%
Bloomsbury Publishing plc	Featherstone Education	1.1	0.4	0.7	63.6%
Advertising & marketing services					
WPP plc	Others	152.8	132.4	20.4	13.4%
Aegis Group plc	14 acquisitions aggregated	151.3	92.2	59.1	39.1%
Thomson Reuters plc	Feri Fund Market Information/Clear Market/ Thomas Weisel/Arian	56.0	26.0	30.0	53.6%
M&C Saatchi plc	Clear Ideas/Walker Media	45.7	39.9	5.8	12.7%
The Mission Marketing Group plc	Bray Leino	28.8	28.8	0	0.0%
Chime Communications plc	Fast Track Sales	27.9	27.0	0.9	3.2%
Creston plc	Tullo Marshall Warren	27.4	26.9	0.5	1.8%
Chime Communications plc	VCCP and Stuart Francis Whitson	22.8	22.8	0	0.0%
Interactive Prospect Targeting Holdings plc	Directinet/J2P2N	21.9	19.6	2.3	10.5%
YouGov plc	Psychonomics	20.8	13.3	7.5	36.1%
Huntsworth plc	Axis Healthcare	20.5	16.0	4.5	22.0%
Creston plc	ICM Research	18.5	17.6	0.9	4.9%
Research Now plc	Samplenet e-Research Solutions Inc	16.6	16.2	0.4	2.4%
The Mission Marketing Group plc	RLA	15.0	15.0	0	0.0%
International Marketing & Sales Group Ltd	V+O Communications	14.8	14.8	0	0.0%
Digital Marketing Group plc	Alphanumeric (Jaywing)	14.7	10.3	4.4	29.9%
Huntsworth plc	Dorland Corporation	13.0	9.0	4.0	30.8%
Optimisa plc	eq group plc	12.7	12.1	0.6	4.7%
YouGov plc	Polimetrix	12.6	7.0	5.6	44.4%
Creston plc	PAN Advertising	12.5	12.2	0.3	2.4%
The Mission Marketing Group plc	April-Six	12.1	12.1	0	0.0%
YouGov plc	Zapera	12.0	8.5	3.5	29.2%
International Marketing & Sales Group Ltd	Shared Value	10.6	10.6	0	0.0%
Digital Marketing Group plc	Cheeze	10.3	8.9	1.4	13.6%

Business combinations surveyed

(continued)

Company	Acquisition	£m Total intangibles	£m Goodwill	£m IIA	IIA%
The Mission Marketing Group plc	Story UK	10.0	10.0	0	0.0%
Digital Marketing Group plc	Graphico	9.4	6.0	3.4	36.2%
The Mission Marketing Group plc	Bastin Day Westley	9.0	9.0	0	0.0%
Ekey plc	WFCA Integrated	8.5	8.5	0	0.0%
The Mission Marketing Group plc	Big/Fuse	8.4	8.4	0	0.0%
Cello Group plc	SMT consulting	8.3	8.3	0	0.0%
Digital Marketing Group plc	Scope Creative (Dig for Fire)	8.2	5.6	2.6	31.7%
International Marketing & Sales Group Ltd	Zap	8.1	8.1	0	0.0%
Digital Marketing Group plc	HSM Telemarketing	8.0	5.9	2.1	26.3%
Cello Group plc	2CV	7.9	7.7	0.2	2.5%
Creston plc	Red Door	7.7	7.5	0.2	2.6%
Cello Group plc	MSI	7.5	7.4	0.1	1.3%
Hasgrove plc	Pavillion Communications	7.3	7.3	0	0.0%
International Marketing & Sales Group Ltd	Pragma	6.4	6.4	0	0.0%
Interactive Prospect Targeting Holdings plc	NP6	6.3	5.0	1.3	20.6%
Centaur Media plc	Pro Talk	5.9	3.2	2.7	45.8%
MKM Group plc	Leisure World/Leapfrog	5.1	5.0	0.1	2.0%
Toluna plc	Speedfacts	4.7	3.2	1.5	31.9%
Centaur Media plc	Recruiter	4.0	0.6	3.4	85.0%
Cello Group plc	Hill Murray group	3.8	3.7	0.1	2.6%
International Marketing & Sales Group Ltd	Friends	3.5	3.5	0	0.0%
Hasgrove plc	Odyssey Interactive	3.3	3.3	0	0.0%
Digital Marketing Group plc	Hyperlaunch	3.2	2.0	1.2	37.5%
Chime Communications plc	The Corporate Citizenship company	3.0	3.0	0	0.0%
International Marketing & Sales Group Ltd	BIP	3.0	3.0	0	0.0%
Hasgrove plc	Politics International	2.5	2.5	0	0.0%
Cello Group plc	Magnetic advertising	2.4	2.4	0	0.0%
Hasgrove plc	Amaze	2.4	2.4	0	0.0%
Cello Group plc	Market research international	2.2	2.1	0.1	4.5%
Chime Communications plc	De Facto Communications	1.8	1.8	0	0.0%
The Mission Marketing Group plc	Broadskill	1.7	1.7	0	0.0%
Twenty plc	Ominor	1.6	1.6	0	0.0%
Centaur Media plc	Period Living	1.5	0.1	1.4	93.3%
Chime Communications plc	Stuart Higgins communications	1.5	1.5	0	0.0%
Hasgrove plc	Cabinet Stewart	1.4	1.4	0	0.0%
Huntsworth plc	Grayling International	1.3	1.3	0	0.0%
Cello Group plc	Farm communications	1.2	1.2	0	0.0%
The Mission Marketing Group plc	TMMHL	1.1	1.1	0	0.0%
Cello Group plc	Rosenblatt/Digital online people	1.0	1.0	0	0.0%
Hasgrove plc	Hailstone Creative	1.0	1.0	0	0.0%
International Marketing & Sales Group Ltd	Tarantula	1.0	1.0	0	0.0%
International Marketing & Sales Group Ltd	MAPP & Promer	1.0	1.0	0	0.0%
Cello Group plc	Bankbrae	0.9	0.9	0	0.0%

Company	Acquisition	£m Total intangibles	£m Goodwill	£m IIA	IIA%
Interactive Prospect Targeting Holdings plc	Direct Excellence	0.6	0.5	0.1	16.7%
Chime Communications plc	Facts International	0.6	0.6	0	0.0%
The Mission Marketing Group plc	PCM	0.5	0.5	0	0.0%
The Mission Marketing Group plc	Rhythmm Communications Group	0.4	0.4	0	0.0%
Cello Group plc	OMP services	0.3	0.3	0	0.0%
TOTAL		4,329.9	2,545	1,785	41.2%
WPP plc	Taylor Nelson Sofres	1,858.4	1,132.7	725.7	39.0%
Reed Elsevier	ChoicePoint Inc	2,633.0	1,162.0	1,471.0	55.9%
Yell plc	Telefonica Publicidad	2,454.0	1,316.0	1,138.0	46.4%
TOTAL		11,275.3	6,155.2	5,120.1	45.4%

Appendix 3

IFRS for SMEs – how might this affect the media sector?

The ASB plans to replace **UK Standards** with the **IFRS for SMEs** from 2012. How might this affect the media sector?

What is the IFRS for SMEs?

The International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs) is basically a simplified version of ‘full IFRS’ (International Financial Reporting Standards, other than IFRS for SMEs). It’s much smaller than full IFRS, being just over 200 pages long. There are also about 10% of the disclosure requirements in full IFRS (about 300 compared to 3,000 in full IFRS).

The IFRS for SMEs was designed to produce general purpose financial statements. It is based on the premise that if investors in non-publicly accountable companies require information in addition to that provided in such financial statements, the investors can demand that information separately. Therefore certain requirements which are of benefit to some users, such as users of capital markets, have been omitted, for example segmental reporting.

The simplification has partly been achieved by allowing only one accounting policy option, where full IFRS allows a choice of options in some areas. Because the IFRS for SMEs been several years in the making, full IFRS has moved on in some areas. This has resulted in some unfortunate contradictions between IFRS for SMEs and full IFRS, as we will see.

How will the IFRS for SMEs apply in the UK?

The ASB (Accounting Standards Board) proposes replacing existing UK GAAP with a new, differential reporting regime based on public accountability, and incorporating the IFRS for SMEs. These plans aren’t finalised yet, but a decision is expected in mid-2010.

The change is planned for financial years beginning on or after 1 January 2012 (which would require 2011 comparatives and 2010 closing balances to be restated).

What companies will be affected?

The ASB proposes the following approach:

Tier 1	
Publicly accountable entities	Full IFRS
Tier 2	
Non-publicly accountable entities	IFRS for SMEs
Tier 3	
Small entities	FRSSE

Any entity could elect to use the GAAP of a higher tier, for example a Tier 3 entity could chose to adopt IFRS for SMEs or full IFRS.

- In the near future, current UK GAAP is likely to be replaced with IFRS for SMEs for non-publicly accountable companies other than small ones
- IFRS for SMEs does not allow certain accounting treatments, such as capitalising internally generated intangible assets or capitalising borrowing costs, which are relevant to the media sector
- Companies could choose to adopt full IFRS instead, and this may be a better option for some

What is a ‘publicly accountable entity’?

The ASB proposals contain a definition of ‘publicly accountable’. It will include companies with debt or equity instruments traded in a public market (including non-regulated markets, such as AIM and PLUS) or companies in the process of issuing such instruments. It will also include companies which take deposits and/or hold assets in a fiduciary capacity as one of their primary businesses (such as banks).

What are the GAAP options?

Companies can chose to adopt full IFRS rather than IFRS for SMEs. This could be an advantage where the IFRS for SMEs requires certain accounting treatments which could be seen to have a negative impact on the financial statements.

In particular, if a company's peers and competitors are using full IFRS, either because they are publicly accountable or because they choose to, using IFRS for SMEs may mean that it is more difficult to compare results and balance sheets.

However, adoption of full IFRS does have the well-known disadvantage of more (and ever-increasing) disclosure requirements. Financial instruments is one example, where IFRS 7 requires many disclosures of different aspects, such as categories of financial instruments, maturity analysis, aging analysis of financial assets, explanations and sensitivity analysis for financial risks and analysis of the methods of calculation of any fair values used. IFRS for SMEs does require some disclosures for financial instruments, but these are limited to a fraction of those in full IFRS (a few paragraphs of requirements rather than a 40-plus paragraph long, separate standard).

IFRS for SMEs has been written in a style which is easier to understand than full IFRS. Also making life easier is the plan to change the IFRS for SMEs only once every three years, which would make it a more stable reporting structure than full IFRS.

What are the major issues?

The major differences between UK GAAP, IFRS for SMEs and full IFRS which may affect companies in the media sector particularly are set out in the table overleaf.

Area of difference	UK GAAP	IFRS for SMEs	Full IFRS
Revenue recognition	Requirements of UK standards, IFRS for SMEs and full IFRS do not differ substantially.	Requirements of UK standards, IFRS for SMEs and full IFRS do not differ substantially.	Requirements of UK standards, IFRS for SMEs and full IFRS do not differ substantially.
Segmental information	<p>SSAP 25 'Segmental Reporting' gives the following exemptions which do not appear in IFRS:</p> <ul style="list-style-type: none"> – an entity need not disclose segmental information if it is deemed seriously prejudicial to its interests – an entity need not disclose turnover segmentally if it is not required by statute to disclose turnover – a subsidiary (that is not a plc) need not make disclosure if its parent does so. 	No segmental reporting required.	IAS 14 and IFRS 8 apply – see page 42.
Internally generated intangible assets	Under UK GAAP (FRS 10), internally developed intangible assets can only be capitalised if there is a readily ascertainable market value, which is highly unlikely to be the case. Therefore, these have often been capitalised as development costs under SSAP 13, when the requirements for feasibility, viability, etc are met. SSAP 13 allows, but does not require capitalisation.	IFRS for SMEs is explicit in stating that any expenditure incurred internally on an intangible item is expensed, and cannot be capitalised. This includes any research and development costs.	<p>Under full IFRS, IAS 38 requires capitalisation of development costs as intangible assets, when they meet certain strict criteria. However, it does specifically rule out recognising internally generated brands, mastheads, publishing titles, customer lists and similar items, on the grounds that the expenditure on such items cannot be distinguished from the cost of developing the business as a whole.</p> <p>So, where a company has internally generated intangible assets which meet the criteria for recognition in IAS 38, it may be beneficial to adopt full IFRS to allow them to be included on the balance sheet.</p>

Area of difference	UK GAAP	IFRS for SMEs	Full IFRS
Intangible assets acquired in a business combination	<p>UK GAAP requires intangible assets to be separable, that is to say they are capable of being disposed of or settled separately, without disposing of part of the business.</p> <p>After the acquisition, intangible assets are usually measured at cost. They may be measured at a revalued amount if they have a readily ascertainable market value.</p>	<p>IFRS for SMEs takes the same approach as full IFRS, under IFRS 3. Acquired intangible assets are recognised if they are either separable from the business or if they arise from contractual or legal rights, and when the fair value can be measured reliably.</p> <p>However, once the intangible assets have been recognised under IFRS for SMEs, they must be measured at cost. No revaluations are permitted.</p> <p>The disclosure requirements for business combinations under IFRS for SMEs are much more straightforward, concentrating on the numerical facts, such as the cost of combination, and omitting much of the narrative and explanation required by full IFRS.</p>	<p>Acquired intangible assets are recognised if they are either separable from the business or if they arise from contractual or legal rights, and when the fair value can be measured reliably.</p> <p>After the acquisition, IFRS allows them to be measured either at cost or at a revalued amount.</p>
Amortisation of goodwill and intangible assets	<p>Under UK GAAP, for both intangible assets and goodwill, there is a rebuttable presumption that the useful life will not exceed 20 years. This has meant in practice that if the useful life is long but uncertain, these assets have been amortised over 20 years.</p>	<p>IFRS for SMEs requires amortisation of both intangible assets and goodwill over a finite life. When a reliable estimate cannot be made, the asset should be amortised over 10 years.</p> <p>IFRS for SMEs has the advantage of not requiring annual impairment testing. In addition, no disclosure is required beyond the amount of any impairment, compared to the reams of information about the impairment methodology required by IAS 36.</p>	<p>IFRS allows either a definite or an indefinite useful life for intangible assets, and does not allow amortisation of goodwill or indefinite-life intangible assets. Instead, goodwill and intangible assets with an indefinite-life have to be tested for impairment annually.</p> <p>Full IFRS allows an indefinite-life, therefore allowing certain assets to hold their balance sheet value for longer.</p>

Appendix 4

Sale and leaseback revisited

Our survey published in 2002 commented on the accounting for sale and leaseback transactions under UK accounting standards. We thought it would be useful to revisit this area under IFRS.

ITV recognise their sale and leaseback obligations, which comprise the principal and accrued interest, within borrowings on the balance sheet. The finance element of the agreement is charged to the income statement over the term of the lease on a systematic basis. Sale and leaseback obligations are secured against an equivalent cash balance held within cash and cash equivalents.

RDF Media, Shed Media and DCD Media derecognised their sale and leaseback obligations and associated cash balances. Each used the same basis on which to do so. RDF's policy stated that the Group had entered into:

'certain sale and leaseback transactions of television programme rights. Funds received from these transactions are held in deposit accounts and comprise monies to provide for the full discharge of future leasing liabilities. The banks with which these sums are deposited have given guarantees to the lessors in respect of the lease liabilities. Further:

- a. the Group is not able to control the deposit account in pursuit of its own objectives and any payments under the lease are due out of this restricted account. The Group has neither control over the bank balance nor over any interest earned thereon;
- b. the risk of reimbursing the amount of fee receivable by the Group in respect of tax losses transferred and the risk of paying an amount due under the guarantee in case of collapse of the bank holding the deposit are remote; and
- c. other than the initial cash flows at inception of the arrangement, the only cash flows expected under this arrangement are the lease payments satisfied solely from funds withdrawn from the separate account established for this arrangement.

Given the above, the asset and the liability in respect of the sale and leaseback transactions do not represent an asset and a liability of the Group according to SIC-27 'Evaluating the Substance of Transactions Involving the Legal Form of a Lease', and have not been recognised in these financial statements.'

Adding additional disclosure, the directors added in the significant estimates and judgments section that:

'the Group has determined that, under IAS 39 'Financial Instruments: Recognition & Measurement', each sale and leaseback transaction entered into by the Group has, from inception, failed to meet the definition of an asset and liability and has therefore not been recognised in these financial statements. The Group has applied guidance from SIC-27 'Evaluating the Substance of Transactions Involving the Legal Form of a Lease'.'

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Our media and entertainment team

Our media and entertainment team has specialised in advising clients in the media space for nearly 20 years. Our inherent understanding of content and rights exploitation, combined with people who can provide specialist services, enables us to deliver innovative, efficient, and cost-effective solutions to our clients. Led by eleven partners comprising industry specialists from audit, tax, corporate finance and business advisory, our media sector offers a complete, multi-discipline service. Our audit and financial reporting practice, in particular, acts for large listed and privately owned entities through to entrepreneurial independents – many of which involve multi-location, cross-border assignments.

In an advisory capacity we work alongside key investors, bankers and legal advisers in the media sector and provide advice on selling your business, raising finance, management buy-out/management buy-in, acquisitions and due diligence. We provide a full range of tax services including international tax, employee share schemes and remuneration planning, VAT and film tax relief.

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