This paper explores some of the key considerations under IFRS for content development and cost capitalisation by media companies.

Making sense of a complex world
Content development and cost capitalisation by media companies
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Introduction to MIAG

Our Media Industry Accounting Group (MIAG) brings together our specialist media knowledge from across our worldwide network. Our aim is to help our clients by addressing and resolving emerging accounting issues which affect the entertainment & media sector.

With more than 3,575 industry-dedicated professionals, PwC’s global entertainment & media practice has depth and breadth of experience across key industry sectors including: television, film, advertising, publishing, music, internet, video games, radio, sports, business information, amusement parks, casino gaming and more. And just as significantly, we have aligned our media practice around the issues and challenges that are of utmost importance to our clients in these sectors. One such challenge is the increasing complexity of accounting for transactions and financial reporting of results – complexity which is driven not just by rapidly changing business models but also by imminent changes to the world of IFRS accounting.

Through MIAG, PwC aims to work together with the entertainment & media industry to address and resolve emerging accounting issues affecting this dynamic sector, through publications such as this one, as well as conferences and events to facilitate discussions with your peers. I would encourage you to contact us with your thoughts and suggestions about future topics of debate for the MIAG forum, and very much look forward to our ongoing conversations.

With best regards

Marcel Fenez
PwC Hong Kong
Global Leader,
PwC Entertainment & Media

1 PwC refers to the PwC network and/or one or more of its member firms, each of which is a separate legal entity.
Content development and cost capitalisation

In many media sectors intellectual property – “content” – is developed internally rather than being acquired externally. Our fifth MIAG paper explores some of the key considerations under IFRS for content development and cost capitalisation by media companies.

PwC’s 16th Annual Global CEO Survey highlighted that 38% of CEOs in the Entertainment & Media (E&M) sector said they see new product/service/content development as the key way to grow their business over the coming year. This is 13% above the global average for all industry CEOs surveyed.

The accounting for spend on internal development presents challenges such as which IFRS standard to apply; when to start and stop capitalising costs; which costs to capitalise; and how to amortise them. Companies that are adept at navigating the intricate accounting and reporting practices can tell their story in a clear and compelling manner, building public trust in their performance with stakeholders such as investors, analysts, employees, suppliers, advertisers and viewers.

This paper explores the critical considerations relating to the classification, capitalisation and amortisation of content development spend under the applicable IFRS standards IAS 2 Inventories and IAS 38 Intangible Assets, focusing on the television production, educational publishing and video game sectors.

We hope that you find this paper useful and welcome your feedback.

Best wishes

Sam Tomlinson
PwC UK
Chairman, PwC Media Industry Accounting Group

Sam Tomlinson
At its heart, media is a content industry – that is, many media companies use content to capture an audience that can be monetised either by charging the audience directly or by charging advertisers for access to that audience. This content is the key driver of a huge market that continues to grow despite the weak global economy: PwC’s *Global entertainment and media outlook 2012-2016* predicts the global media market will increase from $1.6 trillion in 2011 to $2.1 trillion in 2016, a cumulative annual growth rate of 5.7%.

Accounting for the development of the critical content that drives this growth is therefore a significant issue for many media companies. Specifically, should the costs of content development be capitalised or expensed? And if capitalised, how should the resulting asset be classified on the balance sheet and subsequently recognised in the income statement?

**Content development vs content licensing**

Content can be developed in-house or externally using third parties. When using third parties, either a fixed payment can be made for the content provided, or a usage-based royalty can be made to the third party (“licensor”) for the right to use the content.

Typically, in the case of fixed payments or ownership of the intellectual property transfers to the new owner; whereas in royalty arrangements the intellectual property remains with the licensor, or at least returns to the licensor after a period of time. Distinguishing between a genuine fixed payment and an advance payment against future royalties can sometimes be a matter of judgement and is always dependent on the specific terms of the contract. Royalties were the subject of the separate paper MIAG Issue 4 *Accounting for royalty arrangements – issues for media companies* so are not covered in this paper. Similarly, the accounting for the acquisition of finished content directly from third parties is also the subject of other MIAG papers (eg *Broadcast television: acquired programming rights*) so is not covered here.

This paper therefore focuses on the accounting for content development costs, incurred either internally or externally, where the developer owns the associated intellectual property rights.

Such content development costs are incurred, deferred and capitalised across many media sectors eg production of television series; non-fiction publishing; and video gaming. This paper provides examples of industry practice from each of these sectors. The accounting for film production costs is the subject of a future MIAG paper so is deliberately excluded here.

**What is the relevant IFRS guidance?**

IFRS addresses accounting for capitalisation of product development costs, including guidance on the nature of costs, timing of cost capitalisation and method of cost recognition in the income statement as amortisation. However, IFRS does not include specific industry guidance so in practice application of the relevant standards requires careful consideration of the specific facts and circumstances.

Fundamental to the concept of capitalising costs is that they must meet the definition of an asset ie a resource (a) controlled by an entity as a result of past events; and (b) from which future economic benefits are expected to flow to the entity.

The two key standards that provide guidance for cost capitalisation are IAS 38 and IAS 2:

i) **IAS 38 Intangible Assets**, defined as non-physical resources controlled by an entity for which they will generate future economic benefit. Under IAS 38, costs incurred in the “research phase” are expensed as incurred, while costs incurred in the “development phase” are capitalised once the recognition criteria are met. “Development” is the application of research or other knowledge to a plan or design for the production content before the start of commercial sale.

The threshold for capitalising content development costs is reached when a company can demonstrate that all of the following criteria are met:

(a) The technical feasibility of completing the intangible asset so that it will be available for sale.

(b) The intention to complete the asset and use or sell it.
(c) The ability to use or sell the asset.
(d) The way in which the intangible asset will generate probable future economic benefits i.e. the existence of a market for the asset.
(e) The availability of adequate technical, financial and other resources to complete the development and to sell the asset.
(f) The ability to measure reliably the expenditure attributable to the asset during its development.

Once these criteria are met IFRS requires capitalisation of development costs; there is no option to expense such costs.

ii) IAS 2 Inventories, defined as assets held for sale or in the process of production or to be consumed in that process. Inventory costs are capitalised once the general asset criteria are fulfilled:
(a) The entity has control of the inventory.
(b) The inventory will generate probable future economic benefits.
(c) The ability to measure reliably the expenditure attributable to the asset during its development.

It is clear that the capitalisation criteria under IAS 38 and IAS 2 are similar but not identical. These similarities and differences are explored in the next section. Judgement is required when determining which standard to apply, whether to capitalise development costs and if so when and which ones. These judgements can have a significant impact on statutory operating profit and adjusted measures such as earnings before interest, tax, depreciation and amortisation (EBITDA).

This paper first focuses on determining the relevant standard to apply to internal and third party costs associated with content development. It then goes on to consider cost capitalisation scenarios in the television production, educational publishing and video gaming sectors.

Is there any other applicable guidance?
In addition to IAS 38 and IAS 2, development costs can also fall under the scope of IAS 11 Construction Contracts, which applies when an asset, or group of assets, is being developed for sale to a single customer. Under IAS 11, costs are recognised in the income statement as incurred and revenues are usually recognised based on the percentage of completion.
Accounting guidance for capitalising costs varies under each standard
**Classification**
**IAS 38, IAS 2, IAS 11?**

The first question in accounting for product/content development costs (without physical substance) in the E&M industry is which standard to apply. Do the costs qualify as an intangible asset under IAS 38, inventory under IAS 2 or are they treated as contract accounting under IAS 11? A guide to the relevant standard to apply is shown opposite in Figure 1 followed by application examples.

Our theoretical view when considering IAS 38 and IAS 2, as set out in the examples on the next page, is that content development generally falls more naturally under the remit of IAS 38 (eg example 1), except in circumstances where a media company is producing content that could be sold to anyone and for which the producer expects to retain no intellectual property rights (eg example 2). However, the diversity in practice among media companies when classifying content development costs as either intangible assets under IAS 38 or inventories under IAS 2 is driven less by this theoretical distinction than by other factors, notably the treatment under local GAAP prior to transition to IFRS. We believe that the theoretical classification as either intangible assets or inventory is generally of less concern that the more critical practical judgements on when to start and stop capitalising costs and which costs to include.

For example, there is debate among broadcasters on whether to classify acquired programming rights as intangible assets under IAS 38 or inventory under IAS 2; but in practice this makes little difference beyond balance sheet classification since initial recognition, subsequent amortisation and impairment review practices are generally applied consistently regardless of whether programming rights are classified as inventories or intangible assets (see MIAG 2: Broadcast television: acquired programming rights).

In contrast, the distinction between IAS 38/IAS 2 and IAS 11 is highly important since whereas intangible asset and inventory costs are capitalised on to the balance sheet, costs developing content under a construction contract are recognised in the income statement as incurred with the corresponding revenue booked at the same time.
Example 1: Production where certain rights are retained (TV production)
Producer A is creating and producing a drama series that is intended to be shown around the world. Producer A hopes to sell the national rights in its own country to a national broadcaster for a period of three years, but intends to retain the international format, distribution and ancillary rights to the drama series produced. These international rights will generate the major part of total revenues.

How should the content development costs be classified?
In this case, the costs meet the definition of an asset and the revenues generated from the sale of the national rights are less significant than the international sales rights that are retained. The most appropriate treatment in our view would be to recognise an intangible asset under IAS 38 (although in practice some media companies might classify this asset as inventory under IAS 2).

Example 2: Production for sale and no rights retained (TV production)
Producer B produces a documentary with the primary intention to sell it to a broadcaster. At the time of development there is no sales arrangement in place but Producer B has a successful track record of producing and selling documentaries. Producer B does not expect to retain any rights to the documentary following the sale.

How should the content development costs be classified?
The documentary is an identifiable non-monetary asset without physical substance that is produced for sale in the ordinary course of business. Given that there is no specific arrangement in place with a third party (ie not an IAS 11 construction contract), Producer B would probably account for the production costs as inventory in accordance with IAS 2.

Example 3: Production for hire (TV production)
Producer C is commissioned by a broadcaster to produce a gameshow and earns a fixed fee for the service. Producer C retains no rights to the show.

How should the content development costs be classified?
The programme rights of the documentary are identifiable non-monetary assets without physical substance that are produced for sale in the ordinary course of business, but they are also specific to one contract. Assuming that the outcome can be estimated reliably, costs are recognised as incurred and revenues are recognised based on the percentage of completion under IAS 11. Projects within the scope of IAS 11 are considered in our separate publication MIAG 2: Revenue recognition for media companies.

Example 4: Pre-publication costs (educational publishing)
Publisher D incurs pre-publication costs to develop content that forms the basis for educational textbooks. The publisher controls the legal rights over the content for distribution as both print and eBooks.

How should the content development costs be classified?
Since the publisher has the rights to the benefits from the content, the pre-publication costs qualify as intellectual property. The asset itself – the legal rights to the content – is not sold in the ordinary course of business; rather, it is the print and eBook that are sold in the ordinary course of business. Based on this an intangible asset for pre-publication costs would probably be recognised under IAS 38.

In summary, where the costs relate to the development of a product that will be sold in full, the expenditure is theoretically likely to be classified as inventory under IAS 2; and where the developer retains the rights to the content and will be able to exploit these rights over a period of time, the expenditure is theoretically likely to be an intangible asset under IAS 38. In practice, there is diversity in balance sheet classification but the more critical judgements are scope and timing of cost recognition and amortisation, as set out in the rest of this paper.

“There is diversity in practice among media companies.”
Having determined the appropriate standard to follow, at what point should costs start to be capitalised and which costs should be capitalised? (This section considers projects within scope of IAS 38 and IAS 2 only. “Construction” and “service” projects under IAS 11 are considered in our separate publication MIAG 2: Revenue recognition for media companies.)

When should costs be capitalised? (And when should capitalisation cease?)

As described earlier, IAS 38 and IAS 2 set out similar criteria that must be met in order to capitalise content development costs. The fundamental premise under both standards is that a company must be confident that the asset capitalised will bring future economic benefit exceeding the value of the asset itself. Determining the point at which the asset recognition criteria are met will usually require significant judgement and be dependent on past experience.

Selling, promotion and marketing costs are always expensed. Although such expenditure is intended to generate future economic benefits, these benefits are not separable from the development of the overall business and do not meet the definition of an asset.

The following examples illustrate the application of the criteria to the television production, educational publishing and video gaming sectors.

Example 1: Television production
Producer A creates and produces a drama series that is intended to be shown internationally. Producer A will retain the intellectual property rights ie the international format, distribution and ancillary rights.

Figure 2 sets out the development stages of a new television series:

The start point of capitalising costs occurs when there is evidence that all the recognition criteria set out on pages 6-7 are met.

The ability to confidently assess that a project will be completed and will generate profits is likely to come at some point between the start and the end of the pilot phase, but before the company moves into developing the series.

Considerations for the start point of capitalisation may include:

- Ability to complete the project: eg commitment of key talent and script writers.
- Existence of a market: eg prior evidence of successful productions.
- Generate profits: eg history of accurate forecasts of future local and international and DVD sales.

Once the recognition criteria are fulfilled, directly attributable internal and external costs related to the development phase of the drama series must be capitalised.

Capitalisation of eligible costs should cease when the asset is capable of operating in the manner intended. Costs of using or redeploying the asset to other locations or uses are not capitalised. In practice this means that capitalisation of eligible costs would usually cease once the series can be broadcast or sold.
**Example 2: Educational publishing**
Publisher B develops and publishes educational textbooks and websites. Figure 3 sets out the development stages of a new educational textbook:

**Figure 3: Development stages of an educational textbook**

The start point of capitalisation is as usual assessed against the capitalisation criteria. Again, the key judgements in practice are likely to be the existence of the market and the ability to sell the textbook to generate profits. Development costs will probably start to be capitalised when there is:

- Ability to complete the project: eg commitment of authors and editorial support.
- Existence of a market: eg prior evidence of successful book launches in same or similar genre.
- Generate profits: eg history of accurate forecasts of book sales and inventory costs.

The start point for capitalisation is likely to be at some point between the planning stage and editorial stages. Much of the planning stage is likely to be “research” since the plans and market research do not in themselves represent an asset and moreover are unlikely to be sufficiently complete to forecast future revenues. At the editorial stage, costs begin to be incurred directly on the intellectual property. The end point for capitalisation is likely to occur within the “printing” phase of the development cycle illustrated above, once final sign-off of the text has been obtained and activity moves to the physical production of actual textbooks.

A practical challenge when developing multiple products or titles is tracking the relevant costs, particularly internal costs. For example, it can be difficult to accurately allocate editorial time between specific books; publishers therefore need an accurate and reliable time tracking process. This difficulty in tracking internal costs may lead a company to a policy of capitalising only external costs, while all internal costs are expensed. But if internal development costs are material, publishers should not wilfully ignore the requirements of IAS 38/IAS 2. Instead, they should look to develop processes and systems to track these costs: this is good commercial practice for assessing product profitability as well as generating the data required for appropriate cost capitalisation.

**Content development or brand investment?**

IAS 38 states that internally generated brands and publishing titles shall not be recognised as intangible assets. The consensus view among publishers is that this does not apply to book pre-publication costs as the costs incurred are in respect of developing the content that will be exploited over many months or years rather than in developing the brand. In contrast, magazine development costs typically are expensed as incurred because the content is so short-lived and therefore any long-term benefit must reside in the non-capitalisable brand.

Marketing costs are effectively brand investment so must be expensed under IFRS. Sometimes it may be unclear whether costs are development or marketing. For example, most education publishers supply free “samples” of university textbooks to university professors. If this is an early draft, and the purpose is to receive editorial review comments, which will then be reflected and acknowledged in the final publication, it might be legitimate to classify these as development costs. But more often the text is a late (or final) draft being shared to encourage professors to read the publication and add it to reading lists. In this case, the cost is marketing in nature and should be expensed as incurred. Industry practice in the past decade has moved away from capitalising in favour of acknowledging these costs are marketing and expensing them.
**Example 3: Video gaming**

Video game producer C designs and produces video games. The company faces intensive research and development costs in the process of the video game production. Figure 4 sets typical stages in the video game development and production lifecycle:

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**Figure 4: Development stages of a video game**

### Expense costs
- **Research**
  - Game user research
  - Game and content design
  - Talent search
  - Budget
  - Milestone & production plan
- **Development**
  - Game programming
  - Level design
  - Game art
  - Music and sound design
  - Background story
- **Working model**
  - Alpha release
  - Prototypes of gameplay
  - Technical design document
  - Game design document
- **Testing**
  - Beta testing
  - Load testing
  - Multiplayer testing
  - Compatibility testing
  - Regression testing
- **Production**
  - Online
  - Produce copies

### Capitalise costs
- Selling: promotion and marketing

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In this case, the key judgements for when to start capitalisation are likely to be:

- Ability to complete the project: eg technical feasibility and funding availability.
- Existence of a market: eg prior evidence of successful video game launches in same or similar genre.
- Generate profits: eg history of accurate forecasts of video game sales and costs.

The determination of when technological feasibility is reached requires judgement, expertise, and coordination between developers, marketers, finance and accounting personnel. Technological feasibility is generally established when the company has completed the planning, designing, coding and testing necessary to determine that the video game will meet its game design specifications. The practice of defining technological feasibility may differ between development studios based on their internal practices and procedures for game development. Within a studio, the practice of defining technological feasibility may also differ depending on the type of game or product. Factors such as whether proven technology exists must be considered.

Determining whether sales of the game will exceed costs depends on the marketability of the game. Assumptions for future demand will need to reflect future market uncertainties as well as market research and historical performance. For example, consumer preferences for games may shift rapidly, and there may be threats due to new games or hardware from competitors.

The point of starting to capitalise costs may vary considerably between different video game developers. For some, the internal approval process may mean that an idea is never progressed unless there is high degree of certainty of success, which means that capitalisation of costs may start relatively early in the process. For others, there may be multiple smaller projects where there is no certainty of success until the end of the development process and hence costs may never qualify for capitalisation for the first run of a title. As in all industries, the company’s track record and experience developing similar products will impact its ability to judge with confidence when the capitalisation criteria are met.

**Sequel title for existing video game**

When a sequel is developed, a company can look to historical experience with the technical feasibility and sales success of the previous title, plus the general experience of successful sequels. Therefore, capitalisation of internal costs for sequels may start earlier in the process.

**Which costs can be capitalised?**

Examples of “directly attributable” costs that could typically be capitalised include:

- External costs: director, actors, studio rent, copyright registration.
- Internal costs: salaries of script and code writers, producers and other employees working on the project.

The cost of advertising and promotional activities – even if these costs might be significant in establishing the market for a new game – are again expensed as incurred.

Capitalised costs for cancelled projects are recognised as an immediate expense in the period of cancellation. If costs are being written off frequently, the company should revisit its policy to check if costs are being capitalised too early.
Application in practice: policies and procedures
In all examples, judgement is required in determining when to start (and stop) capitalising costs and which costs to include. Factors that can help in practice include:

- Establish a clear policy regarding the threshold, start point and nature of cost capitalisation.
- Communicate this policy.
- Where appropriate, include a list of factors to consider to help staff apply this guidance.
- Set up the systems, month end and year end processes to reflect the policy in the accounts.
- Once the policy is set, follow it consistently.

The policy should be periodically revisited to check it remains appropriate as the business evolves.

Application in practice: identifying costs to capitalise
Companies often have an authorisation processes at each stage of product development. These “gates” can help set a suitable start point for cost capitalisation. However, gathering all the cost data to quantify capitalisation can be a challenge, for example because:

- Contributing costs can come from a number of different general ledger codes, or be a part of a general ledger code. This is frequently the case with payroll cost where individuals may be working on a number of different projects at different stages, some capitalisable and others not.
- The relevant approval to commence capitalisation is unlikely to fall neatly on a reporting period end date, hence requiring additional processes or system modifications to ensure all relevant data is captured appropriately.

The company should also consider the applicability of IAS 23 Borrowing costs in determining whether interest should be capitalised.

Application in practice: treatment in the cash flow statement
Costs qualifying for capitalisation as inventory under IAS 2 are invariably classified as an operating item in the cash flow. But the treatment of costs qualifying for capitalisation as an intangible asset under IAS 38 is less clear. Cash flows to develop (or acquire) intangible assets are often presented as investing activities, but there is some diversity in practice. If the company defines its operating cycle as multi-year, with this content development and exploitation as its principal revenue-generating activity, then the expenditure would be classified as an operating item.

“Gathering all the data for capitalisation can be a challenge”
Cost capitalisation
Amortisation

If the developed content is sold in full with no rights retained, then the capitalised costs are immediately recognised in the income statements when the sale is completed. But if the developed content delivers value over time, then a company must determine an appropriate amortisation life and profile.

Does cost classification impact amortisation?
In practice, regardless of whether media companies classify their product development costs as intangible assets under IAS 38 or inventories under IAS 2, they select the amortisation method that most appropriately reflects underlying economic reality, subject to pragmatic constraints such as simplicity of application and the availability of reliable data. In that sense, the classification as inventories or intangible assets is irrelevant. Various amortisation methods are considered further below.

However, although the timing and magnitude of the related expense is unaffected, its disclosure can vary. The cost associated with an intangible asset is invariably described as “amortisation” whereas those media companies that classify capitalised content development as inventories sometimes do refer to them as being amortised but sometimes use other terms (eg “content costs”) and sometimes do not separately disclose the related expense at all. Comparing EBITDA between media companies can be a complex and challenging task, with some media companies reversing such amortisation out of EBITDA while others leave it in.

(Throughout this paper, we use “amortisation” to refer generically to the expensing of capitalised cost development in the income statement, even where these rights are classified on the balance sheet as inventories.)

How should the product / content development intangible asset be amortised?
After initial recognition, intangible assets are carried at cost less accumulated amortisation and accumulated impairment losses, if any. This paper covers only “normal” amortisation not impairment reviews, which will be the subject of a separate future MIAG paper.

Under IAS 38 amortisation is defined as the systematic allocation of the depreciable amount of an intangible asset over its useful economic life. The allocation method should reflect the pattern in which the asset’s future economic benefits are consumed by the entity. If that pattern cannot be measured reliably the straight-line method must be used. Under IAS 2 costs are recognised in the income statement as revenue is earned. These approaches are theoretically different but often generate the same result in practice provided the method of amortisation reflects underlying economic reality.

Different types of content development have different underlying economics, resulting in various amortisation methods. For example, the publication of a video game would typically generate more revenue in the weeks immediately after release, whereas the publication of an educational textbook would generate fairly consistent revenues over a number of years. Textbooks sometimes have the added complication that a proportion of the content is expected to be rolled-over into a subsequent edition and hence retains some legacy value that may need to be taken into account when determining the amortisation profile.

The unique nature of each type of content means that companies must consider several factors when selecting the most appropriate amortisation method, including:

- Pattern of consumption of the economic benefit from the developed content.
- Expected useful economic life and pattern of revenues/profits and the related ability to reliably estimate them.
- Likelihood that future editions of publications would generate different revenues/profits.
- Likelihood that future publications would use content within the existing publication meaning that this content retains some legacy value that should not be amortised.

After careful consideration the content developer determines an appropriate amortisation method. Amortisation can occur in full on first airing/publication/release; or can be spread over the estimated expected life cycle of a title (either straight-line or reducing balance); or can follow the pattern of expected revenues (“flow-of-revenue”) particularly if the initial period of release of a publication/video game is considered more valuable.
Figure 5: Amortisation methods by industry

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<th>Type of content</th>
<th>Plausible amortisation method</th>
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<td><strong>TV production (where significant rights are retained)</strong></td>
<td>Amortisation based on the “flow-of-revenue” ie total costs of production are amortised across the combined forecast contributions from the initial licence fee and future exploitation.</td>
</tr>
<tr>
<td><strong>Educational publisher</strong></td>
<td>Amortisation of the depreciable amount (excluding any retained legacy value) over the expected life cycle of the title on a straight-line or reducing balance basis, depending on expected pattern of economic benefits.</td>
</tr>
<tr>
<td><strong>Video game publisher</strong></td>
<td>Expensed in full on first release (unless clear evidence of extended sales cycle).</td>
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The selection of the most appropriate method will vary depending on specific facts and circumstances. A rational amortisation method supported by the underlying economics of the transactions, consistently applied across similar types of content and between reporting periods, is usually effective in determining an appropriate amortisation method.

**What is the life of a product or publication where the content rolls over?**

What should the life of the capitalised content be where the content rolls from one product to the next, such as a school textbook that uses the same base content, but with some updates in each new edition?

Options are to use the expected life of the first edition of the textbook or alternatively, where there is appropriate history, over the expected life of multiple editions, by taking into account what proportion of the content is expected to be re-used and using this retained legacy value in calculating the amortisation of each edition. Since there is no specific accounting guidance both approaches are seen in practice.

**How might the accounting guidance for amortisation change in the future?**

ED/2012/5 published by the IASB in December 2012 states:

“This amendment proposes to clarify that when applying the guidance in paragraph 62 of IAS 16 and paragraph 98 of IAS 38, a revenue-based method should not be used to calculate the charge for depreciation and/or amortisation, because that method reflects a pattern of economic benefits being generated from the asset, rather than the expected pattern of consumption of the future economic benefits embodied in the asset.”

This would potentially require those media companies classifying their capitalised content as intangibles to discontinue use of the flow-of-revenue amortisation method. Such media companies would need to amend their amortisation profiles; or reclassify capitalised content as inventories; or demonstrate that their current revenue matching methods (“generation of economic benefit”) approximate to an amortisation method explicitly permitted in IAS 38 such as unit-of-production or diminishing balance (“consumption of economic benefit”).

ED/2012/5 does go on to state within its Basis for Conclusions:

“During its deliberations, the IASB considered the question of whether there could be limited circumstances in which revenue could be used to reflect the pattern in which the future economic benefits of the asset are expected to be consumed. The IASB noted that the limited circumstance when revenue could be used is when the use of a revenue-based method gives the same result as the use of a units of production method.

For example, some types of intellectual property assets (for example, acquired rights to broadcast a film) will initially incur a significant decline in value followed by a diminishing rate of decline (for example, when a film is initially shown and with each subsequent showing the value of the rights typically decrease quickly at first and then at a slower rate). The IASB noted that the use of a time-based straight-line amortisation method may not be appropriate in those cases because these rights have an inherent and fast initial pattern of decline in value.

The IASB observed that in those cases a measure such as the number of viewers attracted could be used as a reasonable basis for the pattern in which the benefits for those rights are expected to be consumed. In rare cases such as this, advertising revenue could serve as an equivalent for viewer numbers to the extent that advertising revenue has a linear relationship with viewer numbers.”

Although this wording is somewhat helpful for those media companies wishing to use flow-of-revenue amortisation profiles, the use of terms such as “limited circumstances” and “rare cases” means they would be unwise to simply assume their current policies would continue to be acceptable. Moreover, the wording in this draft may be omitted from the final version.

For now, we advise media companies to pay close attention to further developments and to formally contact the IASB if they feel strongly on this topic.
In many media sectors intellectual property – “content” – is developed internally rather than being acquired externally. The accounting for spend on internal development presents challenges such as which IFRS standard to apply; when to start and stop capitalising costs; which costs to capitalise; and how to amortise them. Companies that are adept at navigating the intricate accounting and reporting practices can tell their story in a clear and compelling manner, building public trust in their performance with stakeholders such as investors, analysts, employees, suppliers, advertisers and viewers.

Management is often called on to make significant judgements and estimates for capitalising and amortising content development costs, which should be disclosed under IAS 1 Presentation of financial statements if they are material. In particular, the accounting for content development frequently relies on forecasts of revenue and profits to assess whether costs should be capitalised and how they should be amortised.

This paper has explored some of the critical considerations relating to the classification, capitalisation and amortisation of content development spend under the applicable IFRS standards IAS 2 Inventories and IAS 38 Intangible Assets, focusing on the television production, educational publishing and video game sectors. The answer for complicated real life transactions will depend on the specific facts and circumstances in each case. In addition to this existing commercial and accounting complexity, the use of revenue-based amortisation profiles is currently subject to potential amendment by the IASB. As always, planning ahead can prevent painful surprises.

We hope that you find this paper useful and welcome your feedback.

To comment on any of the issues highlighted in this paper please visit our dedicated website www.pwc.com/miag or contact your local PwC entertainment and media specialist.
Further reading

MIAG Issue: 1
Accounting for joint ventures – issues for media companies
This paper explores some of the accounting complexities related to joint ventures which can arise for media companies both under existing IFRS and in the future.

MIAG Issue: 2
Revenue recognition for media companies
This paper explores some of the main implications for media companies of the revenue recognition ED re-exposed in November 2011.

MIAG Issue: 3
Broadcast television: Acquired programming rights
This paper explores the critical considerations under IFRS relating to the recognition, presentation, amortisation and impairment of acquired programming rights.

These publications are available at www.pwc.com/miag
This paper explores some of the key considerations under IFRS in accounting for royalty arrangements by both licensors and licensees.

PwC’s Global entertainment & media outlook contains detailed industry analysis and forecasts trends in the global entertainment & media industry over the next 5 years across 13 industry segments in 48 countries.

This year’s outlook focuses on the emergence of a golden age for empowered consumers, driven by the profound move to digital, which has created a “new normal” for the entertainment & media industry.

15th Annual Global CEO Survey
Entertainment & Media industry summary

This year our findings show that E&M CEOs think their businesses’ future growth depends—crucially—on responding to consumer change through innovation. Collaboration within and across the digital ecosystem will be vital for achieving this. The key element currently lacking is the right skills – a shortcoming they’re determined to address.
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