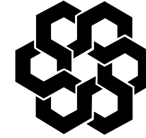

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International Accounting Standards Board

This observer note is provided as a convenience to observers at IFRIC meetings, to assist them in following the IFRIC's discussion. Views expressed in this document are identified by the staff as a basis for the discussion at the IFRIC meeting. This document does not represent an official position of the IFRIC. Decisions of the IFRIC are determined only after extensive deliberation and due process. IFRIC positions are set out in Interpretations.

Note: The observer note is based on the staff paper prepared for the IFRIC. Paragraph numbers correspond to paragraph numbers used in the IFRIC paper. However, because the observer note is less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

IFRIC meeting: **3 November 2006, London**

Project: **Advertising and Promotional costs (Agenda Paper 11)**

INTRODUCTION

1. At its September meeting, the IFRIC agreed to take on a project to consider under what circumstances an entity may carry forward advertising costs in its balance sheet.

2. The project was derived from a request asking for guidance on how catalogue costs should be accounted for in the situation where costs are incurred before the year end but the catalogues are not distributed to customers until after the year end.

3. The IFRIC considered that divergence did exist in this area with some entities accounting for the catalogues as inventory, some as prepayments, and some expensing the costs immediately. Further divergence exists in the way that costs carried forward are recognised as an expense with some recognised at the point at which catalogues are distributed and others recognised over the life of the catalogues.

4. This paper sets out the staff's considerations on the accounting for advertising and promotional costs. Once the IFRIC has concluded on the accounting treatment which it wishes to pursue, the staff will develop a draft Interpretation on the issue.

5. This paper is split into two sections. The first considers which accounting model should be used for advertising and promotional expenditure in the situation where costs have been incurred but the advertising has not been distributed. The second considers how costs should be accounted for using the different accounting models identified.

I CHOOSING AN ACCOUNTING MODEL

6. Differing views exist as to the accounting model which should be used to account for advertising and promotional costs. Some believe that such costs may be accounted for as inventory under IAS 2. Others believe that the accounting model for prepayments set out in IAS 38.70 could be used to justify the carrying forward of costs. Supporters of the view that the costs should be expensed immediately rely on the accounting model for expenditure on intangible items which must be recognised as an expense as incurred in IAS 38.68-69.

7. This section considers when each of these models may be applied to advertising and promotional expenditure.

IAS 2 Inventory model

8. Some preparers believe that catalogues (and other types of advertising and promotional spend) should be accounted for as inventory in accordance with IAS 2.

9. IAS 2.6 defines inventories as "assets :

   (a) held for sale in the ordinary course of business;
   (b) in the process of production for such sale; or
   (c) in the form of materials or supplies to be consumed in the production process or in the rendering of services."

Is a catalogue or other form of advertising which has not been distributed an asset?

10. The Framework defines an asset *as "a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity."*

11. The staff considers that, in the case of advertising which has been developed by an entity but has not yet been distributed to a customer, an entity will have a resource. This may be a physical resource, for example a leaflet or catalogue, an intellectual property type resource associated with the advertising, or another type of intangible, for example a right to have the entity's advertisements displayed in a publication or on television.

12. Since the resource has not been distributed to the customer, the resource remains under the control of the entity. The resource clearly arises from past events (the entity paying for the resource) and future benefits are expected to flow to the entity as a result (the advertising is expected to benefit the entity).

13. The staff therefore considers that, in most cases, where expenditure has been incurred on advertising but the advertising has not been delivered to the customer, an entity will have an asset in respect of that advertising.

14. This may not be the case in certain instances, for example if the advertising campaign is aborted before distribution to customers. The staff have not considered this option further on the basis that, if the asset ceases to exist or be controlled by the entity (for example if the advertising campaign is cancelled), then it is clear that any amounts carried forward in the balance sheet should be written off to the income statement immediately. This would be true regardless of the accounting model used.

Does an advertising asset meet the definition of inventory?

15. The staff next considered whether an advertising asset may meet the other parts of the definition of inventory included in sections a-c of IAS 2.6.

16. The staff noted that, in some cases, advertising materials are routinely sold by entities. Examples of this may include catalogue companies who sell catalogues to customers, brochures for luxury items (for example expensive sports cars) which are sold to customers and collectors, and items of merchandise which advertise a product (for example a football shirt, which advertises a club and its sponsors, but primarily exists as a product for sale).

17. Where this is the case, such items may be considered as being "held for sale in the ordinary course of business" and therefore should be accounted for as inventory.

18. In other cases, free samples may be given as a form of advertising. In these cases, the items are likely to meet the definition of inventory until such point as they are no longer for sale in the ordinary course of business. For example, if the items are packaged in such a way that they can only realistically be used as a free sample (maybe in very small quantities with "Free Sample" printed

on them) then the staff considers that they will no longer meet the definition of inventory.

19. In most other cases, advertising spend creates or develops assets which are not held for sale in the ordinary course of business. In these cases, the staff considers that the spend and assets will not meet the definition of inventory as the assets are not held for sale, in the process of production for such sale, or held to be used in that production process.

20. The staff therefore concludes that, unless the advertising costs are incurred acquiring or producing items that are either:

    - routinely sold by the entity (for example catalogues which are sold to customers); or
    - usually sold but sometimes given free (and are not in a condition that precludes them from being sold in the future);

    then they do not meet the definition of inventory and so should not be accounted for in accordance with IAS 2.

IAS 38 Intangible Assets model

21. IAS 38 defines an intangible asset as "an identifiable non-monetary asset without physical substance." IAS 38.4 states that "Some intangible assets may be contained in or on a physical substance such as a compact disc (in the case of computer software), legal documentation (in the case of a licence or patent) or film. In determining whether an asset that incorporates both intangible and tangible elements should be accounted for under IAS16 *Property, Plant and Equipment* or as an intangible asset under this Standard, an entity uses judgement to assess which element is more significant."

22. The staff considers that in many cases, advertising spend will generate assets which are clearly intangible. Examples may include photographs taken for an advertising campaign, consultancy on how best to develop the brand, and the development of a 'slogan' to define the brand.

23. In other cases, the advertising may be captured in a physical asset. For example, advertisements on leaflets, catalogues, and billboards all have

physical form. In these situations, it may not always be clear whether the intangible asset embodied in the advertising is more significant than the physical asset which holds the advertising medium.

24. The staff notes IAS 38.5 which states that "This Standard [IAS 38] applies to, among other things, expenditure on advertising…" Additionally, IAS38.68 – IAS38.70 specifically refers to the accounting for advertising and promotional activities.

25. The staff considers that whilst it may not always be clear whether the physical or intangible asset is more significant, IAS 38.5 is clear in requiring that advertising spend is accounted for under that standard.

26. Furthermore, IAS 38.69 specifically discusses how such spend should be accounted for.

27. The staff therefore concludes that all advertising and promotional expenditure which does not meet the definition of inventory should be accounted for under IAS 38.

28. For the remainder of this paper, the staff has focussed on how costs should be accounted for under IAS 2 *Inventory* and under IAS 38 *Intangible Assets*.

II. APPLICATION OF THE ACCOUNTING MODELS TO ADVERTISING AND PROMOTIONAL SPEND

29. Having concluded on the accounting model to apply to an item of advertising and promotional spend, an entity must then decide on how that model should be applied. The staff considers that further divergence exists in this area. In particular, the staff notes that, in situations where advertising is accounted for as inventory, some entities appear to take into account the anticipated future benefits of the advertising when they are computing its net realisable value. Others rely solely on the proceeds which will be received from distributing the advertising to compute its net realisable value (which may be nil). Similarly, IAS 38 is interpreted as allowing the recognition of costs as an expense when the advertising is distributed to a customer, the recognition of costs as an expense in the periods in which the advertisement is expected to generate revenue, or the recognition of costs as an expense immediately.

30. This section therefore considers how the models discussed in section I above should be applied to items of advertising and promotional spend.

Application of the inventory model

31. Where advertising and promotional material is treated as inventory, it must be accounted for in compliance with IAS 2. IAS 2.9 states that "inventories shall be measured at the lower of cost and net realisable value".

32. IAS 2.6 states that "Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale."

33. The staff considered the example of a company that produces a catalogue which it sells to customers for CU5. The catalogues are typically posted to customers at a cost of CU2. As discussed in section I above, the staff considers that catalogues of this nature may be accounted for as inventory under IAS 2. However, if this is the case, the inventory must be valued at the lower of cost and net realisable value as defined by IAS 2.9. In this example, the net realisable value in accordance with IAS 2.6 is CU3 and so the catalogues may not be valued at more than CU3 in the balance sheet.

34. The staff also considered the example of goods which are distributed to customers as a sample. For example, product A costs CU1,000 per 100kg to produce. The sales price is CU2,000 per 100kg with a distribution cost of CU100 per 100kg. Sales are typically made in 100kg batches. In this case, the cost of 100kg is CU1,000 and the NRV is CU1,900. The inventory is therefore valued at CU1,000.

35. If the entity commits to give 10kg of product A as a free sample to a customer (who will bear the distribution cost), then the staff consider that the estimated selling price of that 10kg will reduce to nil. The NRV of the 10kg will therefore be reduced to nil and the cost of CU100 be written off to the profit and loss account.

36. Similarly, if the entity were to package 100kg in 10kg batches marked as "Sample, not for resale" and the entity could not economically repack them, the staff believes that these should be written down to a NRV of nil in the balance sheet.

Application of IAS 38.68 – IAS 38.70

Relevant guidance

37. IAS 38.69 – IAS 38.70 states :

> **68 Expenditure on an intangible item shall be recognised as an expense when it is incurred unless:**
>
> **(a) it forms part of the cost of an intangible asset that meets the recognition criteria (see paragraphs 18–67); or**
>
> **(b) the item is acquired in a business combination and cannot be recognised as an intangible asset. If this is the case, this expenditure (included in the cost of the business combination) shall form part of the amount attributed to goodwill at the acquisition date (see IFRS 3 *Business Combinations*).**
>
> 69 In some cases, expenditure is incurred to provide future economic benefits to an entity, but no intangible asset or other asset is acquired or created that can be recognised. In these cases, the expenditure is recognised as an expense when it is incurred. For example, except when it forms part of the cost of a business combination, expenditure on research is recognised as an expense when it is incurred (see paragraph 54). Other examples of expenditure that is recognised as an expense when it is incurred include:
>
> (a) expenditure on start-up activities (ie start-up costs), unless this expenditure is included in the cost of an item of property, plant and equipment in accordance with IAS 16 *Property, Plant and Equipment*. Start-up costs may consist of establishment costs such as legal and secretarial costs incurred in establishing a legal entity, expenditure to open a new facility or business (ie pre-opening costs) or expenditures for starting new operations or launching new products or processes (ie pre-operating costs).
>
> (b) expenditure on training activities.

(c) expenditure on advertising and promotional activities.

(d) expenditure on relocating or reorganising part or all of an entity.

70 Paragraph 68 does not preclude recognising a prepayment as an asset when payment for the delivery of goods or services has been made in advance of the delivery of goods or the rendering of services.

38. SIC 32.9(c) states that, in the case of websites:

> "to the extent that content is developed to advertise and promote an entity's own products and services (eg digital photographs of products), [expenditure] shall be recognised as an expense when incurred in accordance with IAS 38.69(c). For example, when accounting for expenditure on professional services for taking digital photographs of an entity's own products and for enhancing their display, expenditure shall be recognised as an expense as the professional services are received during the process, not when the digital photographs are displayed on the web site."

39. The staff considers that there are two key questions which need to be addressed in considering how to apply IAS 38.69-IAS 38.70 :

- At what point is expenditure on advertising and promotional activities "incurred" in accordance with IAS 38.69?
- At what point does the delivery of goods or rendering of services occur, meaning that no further prepayment may be recognised in accordance with IAS 38.70?

Differing Views

40. The staff has identified four existing interpretations as to when the costs of advertising are incurred and should be recognised as an expense in the profit and loss account:

- At the point at which an entity has an unavoidable obligation to pay for the advertising or promotional goods or activities.
- At the point at which the entity receives the advertising or promotional goods or activities.
- At the point at which the entity's prospective customers receive the benefit of the advertising or promotional goods or activities.
- Over the period during which the entity expects to receive the benefits of the advertising or promotional goods or activities.

41. The staff has set out below a brief summary of these views and, how they are justified by their supporters. Later in this paper the staff considers the relative merits of these different arguments and whether they comply with IAS 38.

View A – recognition of an expense when a liability is incurred

42. Supporters of View A may illustrate this view using the following example. Suppose that an entity contracts with a TV company such that the TV company will screen an advert on its channel on a specific date. The terms of the contract specify that if the entity terminates the contract (for reasons other than breach of contract by the TV company) up to a month before the screening then there will be no cost. If it cancels later than that but up to two weeks before the screening, then it will be forced to pay 50% of its fee as a cancellation charge. If it cancels less than two weeks before the screening, the entire charge for the screening will become payable.

43. Supporters of View A argue that 50% of the charge is incurred a month before screening with the remaining 50% incurred two weeks before screening.

44. Supporters of View A look to IAS 37 which states that a liability is a present obligation arising from past events which is expected to result in an outflow from the entity of resources embodying economic benefits.

45. Since the obligation to pay meets the definition of a liability and the advertising will not result in an asset which can be recognised under IAS 38, supporters of this view argue that costs are incurred at the point at which a liability is incurred.

View B – recognition of an expense when the goods or services are received

46. Supporters of view B believe that the expense is incurred at the point at which the goods or services are received by the entity. They note IAS38.70, which states that "paragraph 68 does not preclude recognising a prepayment as an asset when payment for the delivery of goods or services has been made in advance of the delivery of goods or the rendering of services."

47. Supporters of this view argue that, if a prepayment may be recognised until the entity has received the "delivery of goods or the rendering of services" then the expense should be recognised at the point at which the entity takes

delivery of the goods or services. Since paragraph 69 requires that the expense be recognised as incurred, the point at which the entity takes delivery of the goods or services must be the point at which the expense is incurred.

48. Supporters of this view believe that, even where there are cancellation penalties which become payable if the entity does not continue with its advertising contract, the expense is still incurred when the service is received (or on the day that the contract is terminated if sooner).

49. The merits or otherwise of this view are discussed further in paragraphs 69-72 below.

View C – recognition of an expense when the advertising is delivered to the customer

50. Supporters of View C believe that the cost is incurred at the point at which the entity ceases to have control of the advertising media and it is sent to the customer.

51. Supporters of this view may draw an analogy with IAS 2 under which, inventory is recognised as an expense at the point at which it is distributed to the customer. They note that IAS 38.70 states that a prepayment may be recognised as "an asset when payment for the delivery of goods or services has been made in advance of the delivery of goods or the rendering of services".

52. Supporters of View C believe that the delivery of goods or services only occurs when these are delivered to the potential customers targeted by the advertising. Up to that point, an entity may recognise costs as a prepayment in the balance sheet.

53. Whether this view can be supported under the current wording of IAS 38 is discussed further in paragraphs 73-77 below.

View D – recognition as an expense over the period during which the entity expects to receive the benefits of the advertising or promotional goods or activities

54. Supporters of View D believe that the advertising cost is incurred over the period when the benefit of the advertising is received by the entity.

55. Supporters of this view believe that the cost should be recognised in a way that matches it with the recognition of revenue. They look to paragraph 95 of the

Framework which states that matching "involves the simultaneous or combined recognition of revenues and expenses that result directly and jointly from the same transactions or other events" and argue that the matching principle dictates that the cost be recognised in the periods in which the entity receives the benefit of the advertising.

56. Whether this view can be supported in IFRS is discussed further in paragraphs 78-81 below.

Staff analysis

57. The staff have considered the lifecycle of an item of advertising spend, starting at the point at which an entity makes an order to acquire advertising or promotional supplies from a supplier, continuing through the points at which the entity receives these goods or services from the supplier and delivers them in the form of an advertisement to a customer, and ending when the entity receives the benefit of the advertising activity in the form of increased sales.

58. Appendix 1 to this document sets out a timeline for these activities showing the points at which Views A-D above would require the recognition of an expense in the profit and loss account.

59. The goods or services which an entity may acquire include TV slots, catalogues, leaflets, promotional photography, brand design services, or a range of other goods and services.

60. The staff have considered below the key events occurring through this lifecycle and whether these events trigger the recognition of an expense in the profit and loss account.

Development of the goods or services by the supplier

61. At this stage in the lifecycle, the entity has placed an order for advertising or promotional goods or services with its supplier but has not yet received these goods or services. During this stage, the entity's supplier commences work producing or developing the goods or services.

62. Supporters of View A believe that a liability may arise between the point at which the entity places its order with its supplier and the point at which the supplier delivers its goods or services to the entity. Supporters of this view

consider that the cost of the related goods or services should be recognised as an expense in the profit and loss account when that liability arises.

63. The staff considers that a liability may arise during this period for one of two reasons. Firstly, there may be penalty clauses which become payable over the period. Secondly, there may be a liability which arises from partial performance of the supplier's contractual obligations during the period.

64. The staff have considered the following examples to illustrate these two fact patterns :

   i. An entity contracts to pay CU1,000 to a TV company to air an advertisement on a specific date. The content has previously been developed by the entity which it passes to the TV company to air. The TV company levies a late cancellation penalty such that, if the entity cancels within 30 days of the expected airing of the advertisement, it is liable to pay CU500.

   ii. An entity contracts to pay CU1,000 to a TV company to produce and air an advertisement on a specific date. The content is developed by the TV company over the month before airing. In the event that the entity cancels the contract during production, it will be liable (under local contract law) to re-imburse the TV company for the work it has completed on the advertisement up to the date of cancellation at cost plus a reasonable margin.

65. In example (i), the entity may have incurred a liability 30 days before the advertisement is aired. However, in this case, the entity has not received the related services. The staff therefore considers that, whilst the entity may recognise a liability at this point, under IASS 38.70 the entity should also record a prepayment in respect of the services which it is yet to receive.

66. The staff therefore concludes that, in this situation, the entity should not recognise an expense at the point at which the liability arises.

67. In example (ii), the entity may incur a liability over the course of the month before the commercial is aired. In this case, however, the TV company has commenced the development of the advertisement and has performed some of its duties under its contract with the entity. Since the entity could take

advantage of the development or partial development of the advertisement, it could be argued that, whilst it has not taken physical delivery of them, the entity has received the benefit of the goods or services in the period. ***If the IFRIC considers that this is the case (even though the entity has not taken physical receipt of the output) then the staff considers that the entity should recognise the advertising expenditure as an expense at this point.***

68. If, on the other hand, the IFRIC considers that the entity has not received the goods or services as it has not taken physical possession of them, then the staff considers that under IAS 38.70, the entity should record a prepayment in respect of the services which it has not yet received. If this is the case then the entity will recognise nil net expense at this point.

Receipt of goods or services by the entity

69. Supporters of View B believe that the expense is incurred at the point at which the goods or services are received by the entity and, since the entity has received the goods and services at that point, it is not able to recognise a prepayment beyond that time under IAS 38.70.

70. ***If the IFRIC agrees that the delivery of goods or the rendering of services has occurred at the point at which the goods or services are delivered, then the entity may not recognise a prepayment under IAS 38.70 beyond this point. It must therefore recognise the expense in the profit and loss account upon receipt of the goods or services.***

71. The staff notes that if the IFRIC concludes that this is the case, the expenditure will be recognised in the profit and loss account at the point at which goods or services are received rather than the point at which the buying entity incurs an unavoidable obligation because of the selling entity completing (or partially completing) its contractual obligations. If this is the case, then preparers may report different results depending upon the timing of the delivery of goods or services.

72. The staff also notes that this may have implications for the recognition of expenditure other than advertising or promotional expenditure.

Delivery of the advertising to the entity's customers

73. Supporters of View C believe that an entity incurs advertising and promotional expenditure at the point at which the entity delivers the advertising to its customer.

74. The staff notes IAS 38.70, which states that an entity may recognise a prepayment when payment has been made "in advance of the delivery of goods or the rendering of services."

75. ***To recognise the expense at the point at which the entity delivers the advertising to its customers, the staff believes that the IFRIC must conclude that the delivery of goods or rendering of services occurs at that point.***

76. The staff considers that recognising an expense when the advertising is delivered to the customer would most closely match the recognition of the expense in the books of the advertiser to the point at which the advertisement occurs. However, to recognise an expense at this point under IAS 38.70 would require an Interpretation that states that "the delivery of goods or rendering of services" refers to onward delivery from the reporting entity. This kind of Interpretation may have implications for a wide range of other situations.

77. For example, if a similar logic were applied to start-up costs (which are also discussed in IAS 38.69) then entities might attempt to use this as justification for capitalising start-up costs and expensing them on the day of the start-up.

Over the period when the entity receives the benefit of the advertising

78. Supporters of View D believe that the cost of advertising should be matched with the recognition of increased revenue as a result of that advertising.

79. The staff considers that when the advertising has been delivered to the customer, the advertising cost has clearly been incurred. Furthermore, the fact that the advertising has been delivered to the customer implies that the delivery of goods or services has taken place, and so that the recognition of a prepayment under IAS 38.70 is no longer appropriate.

80. The only justification for deferring the costs of the advertising to a point after the delivery of the advertising would therefore be to apply the matching principle.

81. The staff does not consider that the matching principle should take precedence over the wording of a specific standard, and so does not consider that this accounting treatment is appropriate.

Concluding on the appropriate point to recognise the expense

82. In the light of the above discussion, the staff considers that the question of when the cost should be recognised as an expense in the profit and loss account can be summarised as follows.

    - The IFRIC may consider that an entity has received goods or services at the point at which its supplier has performed (or partially performed) it obligations under the contract to supply those goods or services and the entity has an unavoidable obligation to pay for the supplier's performance to date. If so, the IFRIC should conclude that the cost is incurred, and should be recognised as an expense in the profit and loss account as the goods or services are completed.

    - If the IFRIC concludes that the delivery of goods or rendering of services occurs at the point at which the goods or services are physically delivered to the entity, the IFRIC should conclude that the expense is incurred at the point at which the entity takes delivery of the goods or services (View B).

    - If, on the other hand, the IFRIC concludes that the delivery of goods or the rendering of services occurs when the advertising is delivered to the entity's customer, the IFRIC should conclude that the expense is incurred at the point at which the advertising is distributed to the entity's customers (View C).

83. The staff notes that SIC32.9(c) states that (in the case of websites), "to the extent that content is developed to advertise and promote an entity's own products and services… expenditure shall be recognised as an expense as the professional services are received during the process, not when the [content is] displayed on the web site."

84. The staff notes that supporting View C (recognising the expense when the advertising is distributed to the entity's customers) would be inconsistent with

the conclusions which the IFRIC reached in issuing SIC 32. This would be particularly troublesome in the case of an entity which sells both through a website and through a catalogue. For example, if the IFRIC were to support View C then promotional photographs, which are used both on websites and in catalogues would be expensed at different points depending on whether the costs relate to the website or the catalogue.

85. Furthermore, the staff do not believe that the usual usage of the phrase "as incurred" in IAS 38.69 would support the deferral of costs until the advertisement is delivered to a customer. Similarly, the staff does not believe that references to the "delivery of goods or the rendering of services" (IAS 38.70) are intended to refer to the onward delivery of goods or services.

86. Whilst the staff considers that View C has some conceptual merit, the staff does not consider that the deferral of advertising and promotional expenditure in an entity's balance sheet until that advertising is delivered to the entity's customers can be considered to be in accordance with IAS 38 or to be consistent with SIC 32.

87. The staff does not therefore consider that View C can be supported under the existing guidance.

88. The staff considered a situation in which an entity contracts with an advertising agency to develop advertising materials for the entity (for example to develop and print catalogues). In this situation, the material may be developed and printed over the course of a number of months. The entity may choose either :

- to take delivery of the materials at the point at which they are complete and then to store them before distributing to its customers; or
- to request that the materials not be delivered to the entity until immediately before they are distributed to customers.

89. The staff notes that, if the costs are recognised as an expense when they are delivered to the entity, then the above situations will lead to the recognition of expenses in the profit and loss account at different points in time, despite the fact that the commercial effect of the two arrangements may be identical.

90. An approach consistent with view B may therefore give rise to the potential for manipulation with entities managing the timing of the delivery of goods or services in order to manage the timing of the recognition of expenses.

91. To a certain extent, these issues will not arise if view A is adopted, since the expense will be recognised at the point at which the entity's supplier completes (or partially completes) its obligations under its contract to supply goods or services and the entity becomes unavoidably obliged to pay for the goods or services (or a portion thereof). This treatment will result in the recognition of the expense at the same point regardless of the timing of the physical delivery.

92. The staff notes that, in the example above, measuring the entity's liability during the period over which the advertising agency produces the advertising materials may be difficult. However, the staff considers that this is unlikely to be more difficult than accruals for other items, for example legal costs.

93. The staff therefore considers that View A is the most appropriate Interpretation of how IAS38 should be applied to advertising and promotional spend.

Conclusion

94. The staff considers that recording an expense over the period during which an entity expects to receive the benefits of its advertising can not be justified under IAS 38.

95. The staff also considers that recording an expense when an entity delivers its advertising to its customers can not be supported under the normal reading of IAS 38. Furthermore, such a treatment is inconsistent with SIC32, and adopting such a treatment may have implications for a range of other costs which are normally recognised as an expense when incurred.

96. The staff considers that recording an expense at the point at which an entity receives goods and services may lead to entities reporting expenses in differing periods dependent on delivery schedules.

97. The staff therefore concludes that an entity should record a liability for costs relating to advertising and promotional activities at the point at which it has an

unavoidable obligation to pay for those goods or services as a result of its supplier completing (or partially completing) its obligations under the supply contract. A prepayment may be recognised only to the extent to which the activities have not yet been completed by the supplying entity.

98. An advertising or promotional expense should therefore be recognised at the point at which an entity has an unavoidable obligation to pay for a good or service, and the supplier has performed or partially performed its obligations under the contract to supply that good or service To the extent that the obligation to provide the good or service has only been partially completed, an expense should be recognised only to the extent that the good or service is completed and the entity has a current obligation to pay for that stage of completion.

III Other considerations

99. The staff considers that the above approach is consistent with the guidance in IAS 38 and IAS 2.

100. The result of this guidance is that advertising and promotional expenditure is likely to be recognised as an expense before it is delivered to customers in most cases. In some cases this may result in the recognition of an expense significantly earlier than the delivery of the advertisement. For example the staff is aware that the advertising material for motor-homes, boats, and the like is often developed in the spring or early summer but not delivered to the customer until the following new year. In this example, using the above approach would result in the expenditure being recognised as an expense in the profit and loss account approximately 9 months before the advert is delivered to the customer.

101. The staff recognises that this solution may not be seen as applying the matching principle and may therefore not be considered as an ideal solution by all constituents.

102. The staff considers that, if the IFRIC wishes, it may be able to address this concern by asking the Board to amend the guidance in IAS 38 and developing new guidance for a new type of short-term intangible asset. This could allow the recognition of an asset in the situation where an entity has incurred expenditure on developing an asset but that asset has not been put to its final use.

103. The staff notes that, if such guidance were developed, it would have implications for a wide range of other situations, including for the assets in IAS 38.69. For example, such guidance would result in start-up costs being capitalised and expensed on the day of the start-up, and relocation and re-organisation costs being recognised as an expense on the day that the relocation or reorganisation takes place.

104. If the IFRIC would like to pursue this route, the staff can develop a full paper considering the implications of developing such guidance for the next IFRIC meeting.

APPENDIX 1

Lifecycle of advertising and promotional spend