GDV
DIE DEUTSCHEN VERSICHERER

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Better Information on Intangibles - Which is the best way to go?
EFRAG's Discussion Paper (August 2021)

Dear Mr Gauzès

On behalf of the German Insurance Association (GDV) we welcome the opportunity to comment on the EFRAG's Discussion Paper "Better Information on Intangibles - Which is the best way to go?" (the "DP"), published by EFRAG on 27 August 2021 for comments.

We continue to be fully supportive of the proactive research activities of EFRAG to influence the development of the global IFRS Accounting Standards. We specifically acknowledge that one of the aims which underpins EFRAG's proactive work is to promote solutions that improve the quality of information, are **practical**, and enhance transparency and accountability.

While we do not provide detailed comments on the specific questions raised in the DP, we would like to convey our general assessment and emphasise which aspects are important to the German insurers when proceeding further with this project. Overall, we greatly welcome the thorough analysis of the status quo and of the different alternatives on the possible ways forward provided in the DP. In particular, we appreciate the explicit consideration of advantages and disadvantages of the respective approaches. Nevertheless, we also believe that it should be acknowledged even more explicitly that it is not the objective of the financial reporting to explain or to bridge the gap between the market capitalisation of an entity and its book value. Also, the objective to remove any differences between entities growing organically and those growing via acquisitions should not lead to favouring accounting approaches and outcomes which might be conceptual very appealing but difficult to be operationalised and audited in day-to-day practice. In this context we reinforce our strong view regarding the need for the reintroduction of **goodwill amortisation** as a pragmatic approach for this issue.

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Regarding the different specific approaches portrayed and analysed in the DP, we would like to generally reinforce our strong support for the principle that deficiencies in recognition and measurement should not be addressed via extensive disclosure requirements for the notes and/or the management commentary. Also, in the context of the CSRD proposal, the possibility of an **information overload** due to more and more narrative disclosure requirements should be considered with regard to the IFRS principles of relevance and clarity. Consequently, we are generally sceptical whether the approach discussed in Chapter 4: *Information relating to specific intangibles* or the one analysed in the Chapter 5: *Information on future-oriented expenses and (…)* can be seen as equivalent alternatives to the approaches presented in Chapter 3: *Recognition and Measurement*. Regarding the latter we have the general view that some **targeted improvements** to the current recognition requirements in IAS 38/IFRS 3 could be indeed envisaged. It is however indispensable that any such changes need to be assessed from the **cost-benefit perspective**, explicitly considering the operational perspective of reporting entities in different sectors, including the insurance industry. Such consideration needs to also address the question of the subsequent measurement. We are specifically afraid that the fair value measurement for self-generated intangible assets might be a difficult and costly exercise, resulting in an unreliable outcome and hence being challenging to audit. In this regard we welcome the analysis provided in the DP (paragraphs 3.94 - 3.100).

In the following we would like to note some additional specific aspects which might be worth to be considered in the context of the discussion on how to approach the recognition of self-generated intangible assets/items, based on the analyses conducted in the DP.

- Our assessment of the alternative approaches portrayed in the DP provides the proof that the current requirements in **IAS 38** might benefit from some targeted adjustments, but overall, they seem to reflect an acceptable **balance** between the needs of investors and other users of financial statements with the operational/cost implications for reporting entities and the need to ensure robust accounting outcomes. Hence, we don't believe that there is an urgent need for fundamental changes to the standard. In this regard we would support **neither** the recognition of all internally generated intangibles (paragraphs 3.15 - 3.35) **nor** the general expensing of internally generated intangibles (paragraphs 3.60 - 3.67).

  Moreover, we believe that discussion about recognition and measurement of intangible assets also needs to consider the accounting requirements for goodwill. From the operational/cost perspective it might be more cost-effective to allow not to recognise separately all the assets purchased in a business combination (**IFRS 3**) if the goodwill would be amortised and the useful life of those assets could be assessed to be mostly like the one assumed for the goodwill amortisation. We would not support essential changes to the current requirements in this area if the impairment only approach is going to be retained as is.

- Furthermore, we believe that any recommendations finally suggested to the IASB should respect the principle that generally only intangible items are eligible for recognition that meet the **asset definition** in the Conceptual Framework, incl. the control concept (paragraph 3.2).
- Considering the different methods described in the DP in paragraph 3.12 we would favour the **conditional recognition approach**, as the threshold approach (paragraphs 3.36 - 3.48) does not consider the dynamic nature of the developments (e.g., agile software developments projects).
- We would tentatively support the combination of the conditional recognition approach with the **prospective method**, i.e., only future expenditures would be capitalised, occurring after the recognition criteria are met (paragraph 3.49 a)), mostly for pragmatic/cost reasons. We would not prefer to use the OCI presentation as suggested in the paragraph 3.49 c). The OCI presentation shouldn't be a 'waiting room' to avoid the need to debit costs occurred in the current period if the recognition condition is not met yet. We are sceptical whether it would be in line with the objectives stated in the Conceptual Framework to use the OCI presentation in such a way (paragraphs 3.57 - 3.59).
- Regarding information on intangibles to be disclosed in the **notes**, we believe that any new requirements should be thoroughly assessed against the objectives they should contribute to. Specifically for reporting entities it is essential that a robust **cost-benefit assessment** is conducted in this regard. To increase the acceptance of any new obligatory disclosures it would be useful to make it even more transparent **how** investors and other users of financial statements would use them.

Overall, our primary preference would be not to re-open IAS 38 fully for a fundamental rebuilding of the Standard. We would rather suggest focussing the activities on some targeted improvements to **better account for** modern/current developing methods, like for example agile software development. Overall, in any case a very careful consideration will be necessary to avoid artificial requirements which are conceptually very appealing, but which would be appreciated neither by reporting entities nor by investors or other users of financial statements. Any efforts should be undertaken to ensure that any potential changes to the Standard provide a true added value to investors and other users of financial statements, but also to reporting entities. And as a matter of fact, IAS 38 is a **principle-based** Standard and should remain as such as rule-based requirements would never be capable of covering all the different facts and circumstances occurring in practice.

In this context, the German insurers believe that the **asymmetric treatment** of intangible assets between IFRS framework and the prudential framework (e.g., Solvency II) should be part of a more comprehensive consideration. The current misalignment of the approaches might be seen as being justified in terms of the different objectives of IFRS framework and prudential frameworks. Nevertheless, in the current situation, the capitalization of self-generated intangible assets leads to additional operational costs while providing no relief regarding capital requirements for insurers. Additionally, in Germany there are also no direct implications of IFRS financial statements regarding distributable profits. Moreover, some of our listed members experienced that rating agencies treat intangibles very conservative/reluctant. In this regard there is a view emerging that **no real benefits** can be achieved by the costly reporting of self-generated intangibles in IFRS financial statements. Consequently, a robust holistic approach needs to be followed when any significant changes to IAS 38 should be approached. The aim should be to increase the robustness of the information provided in the primary financial statements, hence, to create a valid basis on which the prudential regulators accept the intangibles recognised in IFRS balance sheet to the extent possible.

Finally, we understand that the DP does not provide any assessment on the **connectivity** between financial and sustainability information within the management report (e.g., CSRD proposal, IFRS Sustainability Disclosure Standards to be developed by the ISSB), while considering that it is going to be essential element of the future considerations (paragraph ES3). In this regard we welcome the EFRAG's recent decision to prioritise this important topic in a new proactive research project of EFRAG.

We would appreciate if the views of the German insurers would be considered when finalising the EFRAG's research activities on the issues in focus of the DP. From the perspective of the German insurance industry, it is essential that any outcome of the current analysis and future consultations conducted by EFRAG is finally shared with the IASB. We note that in the April 2022 Board meeting the IASB decided to add to its research pipeline a project on intangible assets. Hence, EFRAG activities are going to be finalised just-in-time to support and influence the IASB's activities.

If you would like to discuss our comments further, please do not hesitate to contact us.

Yours sincerely,

German Insurance Association (GDV)