1975

# Accounting practices in the broadcasting industry : recommendation to Financial Accounting Standards Board; Statement of position 75-5;

American Institute of Certified Public Accountants. Accounting Standards Division

# Statement of Position on

75-5

# Accounting Practices in the Broadcasting Industry

December 29, 1975

Recommendation to Financial Accounting Standards Board

Issued by
Accounting Standards Division

American Institute of
Certified Public Accountants

AICPA

## Notes

Statements of Position of the Accounting Standards Division are issued for the general information of those interested in the subject. They present the conclusions of at least a majority of the Accounting Standards Executive Committee, which is the senior technical body of the Institute authorized to speak for the Institute in the areas of financial accounting and reporting and cost accounting.

The objective of Statements of Position is to influence the development of accounting and reporting standards in directions the Division believes are in the public interest. It is intended that they should be considered, as deemed appropriate, by bodies having authority to issue pronouncements on the subject. However, Statements of Position do not establish standards enforceable under the Institute's Code of Professional Ethics.

AICPA

American Institute of Certified Public Accountants
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December 29, 1975

Marshall S. Armstrong, CPA
Chairman
Financial Accounting Standards Board
High Ridge Park
Stamford, Connecticut 06905

Dear Mr. Armstrong:

The accompanying Statement of Position presents recommendations of the Accounting Standards Division on Accounting Practices in the Broadcasting Industry. It was prepared on behalf of the Division by the Accounting Standards Task Force on Entertainment Companies for consideration by the Financial Accounting Standards Board and for such action as the Board deems appropriate. The Division suggests that the recommendations contained herein be required to be applied in financial statements for fiscal years beginning on or after January 1, 1976 (or beginning in late December, 1975, for enterprises having fiscal years of 52 or 53 weeks).

The Statement discusses three areas of interest to broadcasters: television film license agreements, barter transactions and intangible assets.

The Statement concludes that assets and liabilities should be recorded for television film license agreements with respect to films available for telecasting. Guidelines are provided for the classification of these assets and liabilities. The film rights recorded as an asset should, it holds, be amortized using an accelerated method over the number of future showings estimated by management when the first showing, as is usually the case, is more valuable to a station than reruns. The Statement also takes the position that the provisions of APB Opinion No. 21 are applicable to television film license agreements.

Barter transactions involve the exchange of unsold advertising time for products or services. The Statement concludes that all barter transactions should be recorded by estimating the fair value of the product or service received, in accordance with the provisions of APB Opinion No. 29.

Finally, the Statement provides guidance with respect to the application of APB Opinion No. 17 to intangibles in the broadcasting industry, pending reconsideration by the FASB of the broad area of business combinations and purchased intangibles.

The Division would appreciate being advised as to the Board's proposed action on the recommendations set forth in this Statement of Position.

Sincerely yours,

Seymour M. Bohrer

SEYMOUR M. BOHRER
Chairman
Accounting Standards Task Force
on Entertainment Companies

cc: Securities and Exchange Commission

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## GENERAL BACKGROUND

The Federal Communications Commission (FCC) is responsible for the general regulation of television and radio broadcasters. Under current regulations, stations are licensed for three year periods to use assigned frequencies in specific locations. These frequencies are limited and are part of the public domain. The FCC has the authority to consider quality of programming, financial ability of station ownership, amounts of advertising, attention to community service and other factors in determining whether a license should be granted or renewed. The FCC does not, however, regulate rates. The National Association of Broadcasters has set forth guidelines with respect to the amount of advertising time which may be sold.

Broadcasters derive revenue from national, regional and local advertisers. In addition, if a station is affiliated with a network it receives compensation for the network programming that it carries, based on a formula designed to compensate the station for commercial time sold on a network basis and included in network programming. Rates charged by stations vary considerably from market to market and within markets. The prices charged for advertising time are generally based upon the size and demographics of the estimated audience reached, which in turn depends on the size of the market and on the audience's acceptance of the station's programming. Station audiences are measured during rating periods to determine the size and demographic composition of the audiences reached. A station's selling prices (rate cards) are set by program or time periods, to reflect current audience ratings. Rate cards are revised periodically to reflect subsequent audience ratings and/or changes in economic conditions. While there is not always a direct relationship between revenues and expenses for a specific program, a station must maintain audience acceptance of its programming over a period of time or suffer a reduction in its rate schedule as compared to other stations in the market.

Revenues are recognized when the station broadcasts the advertising the sponsor has contracted for. The networks report certain revenue information to their affiliates weekly and distribute that revenue monthly.

Broadcasters may barter unsold advertising time for products or services. Such transactions permit the station to obtain something of value for time which might otherwise remain unsold. The station benefits, if bartering does not interfere with its cash sales, by exchanging otherwise unsold time for programs, fixed assets, merchandise, other media advertising privileges, travel and hotel arrangements, entertainment, and other services and products received from advertisers or agencies acting on their behalf.

A major expense of a television station is its programming costs. These costs are substantially higher for an independent station than for a network affiliate because the affiliate does not incur programming costs for network showings and records only its network advertising revenue. The network recovers its programming costs through the sale of national advertising. Television stations include, however, many hours of non-network programming in their schedules. These programs, other than local news and interview shows and the like, are usually on video tape or film. They are generally contracted for under television license agreements and represent the largest element of programming expense for both network affiliated and independent stations.

A broadcaster's principal intangible assets are its network affiliation agreement(s) and FCC license. Without an FCC license, it is impossible to earn revenue no matter how large the investment in equipment, people and programs. A network affiliated station is generally more valuable than an independent station in the same market because of network supplied programming and revenues. Network programming generally improves the audience levels during network and non-network programming periods. The improvement in audience levels tends to increase the rates and resultant revenue that a station receives from its national and local sales to advertisers.

The Division has noted that there are variations in practice with respect to accounting by broadcasters, including networks, for certain transactions. This Statement of Position has been issued to narrow the range of acceptable alternative practices in the following areas:

- Accounting for television film rights and related license fees.
- Accounting for barter transactions.
- Accounting for network affiliation agreements and FCC licenses.

## TELEVISION FILM LICENSE AGREEMENTS

### Industry Practice

Broadcast rights for feature length motion pictures, series produced for television, cartoons and other films are generally sold by producers or distributors to broadcasters for television exhibition under a contract which typically includes several films (a package) and permits one or more exhibitions of each film during specified license periods. (Certain licenses, however, permit unlimited showings during a specified period of time.) Fees stipulated in the agreement are usually payable in installments over a period of time which is generally shorter than the period of the licensing contract. The license expires after the last allowed telecast or at the end of the specified period even if the licensee telecasts a film less than the allowed number of times.

Accounting practices with respect to film rights and related fees vary. The most common alternatives are summarized below:

1. The unpaid fees stipulated in the agreement are considered to be commitments, not liabilities, and neither the film rights nor the related fees are recorded in the balance sheet. Disclosure practices of companies following this alternative are not consistent.

2. Assets and liabilities are recorded for all television film license agreements. The liabilities are classified as current or noncurrent on the basis of the payment terms specified in the agreement but the assets are classified in different ways:

    (a) All film rights reported as current assets.

(b) All film rights reported as noncurrent assets.

(c) Film rights segregated between current and noncurrent based on—

  (i) Availability for telecasting, or

  (ii) Estimated usage within one year.

3. Assets and liabilities are recorded only with respect to those films which are currently available for telecasting. These assets and liabilities are classified in the balance sheet under one of the alternatives described in (2) above.

Those broadcasters who record film rights as assets amortize those assets using one—or a combination—of the following methods:

1. Straight-line based on the period of the agreement.

2. Straight-line based on the number of showings specified in the agreement.

3. Straight-line based on the number of showings estimated by management.

4. Accelerated by assigning higher values to earlier showings, either based on the number of showings specified in the agreement or based on the number of showings estimated by management.

5. Accelerated by using the sum-of-the-years' digits, declining-balance, or variations of those methods.

6. Higher of (a) straight-line based on either the specified or estimated number of showings, or (b) straight-line over the contract period commencing with date of first showing.

The provisions of APB Opinion No. 21, Interest on Receivables and Payables, are also not applied consistently to the receivables and payables arising from television film license agreements.

Most film licensors impute interest on the receivable arising from the agreement. As a general rule, licensees do not impute interest on the payable. The Opinion is applicable to "receivables and payables which represent contractual rights to receive money or contractual obligations to pay money on fixed or determinable dates, whether or not there is any stated provision for interest...." The Opinion is not intended to apply to certain exempted transactions, but none of these exemptions is applicable to television film license agreements unless the receivables and payables arising from those agreements are "due in customary trade terms not exceeding approximately one year." In addition, those few broadcaster-licensees who do impute interest follow different methods:

1. Interest is imputed and expensed on all license agreements.

2. Interest is imputed and expensed only on those license agreements for films which are currently available for telecasting.

3. Interest is imputed on all license agreements but capitalized as additional costs of film rights.

The practices which exist with respect to the recording of assets and liabilities under television film license agreements, the classification of any recorded assets and liabilities, the amortization of film license costs, and the application of APB Opinion No. 21, provide a broadcaster with the ability to select from a large number of combinations of alternative methods. The Division's conclusions with respect to these alternatives are summarized in the next section.

## The Division's Conclusions

The AICPA Industry Accounting Guide, Accounting for Motion Picture Films, specifies that a licensor should record a receivable and recognize income with respect to film license agreements at the commencement of the license period if all of the following conditions have been met:

1. The sales price for each film is known.
2. The cost of each film is known or reasonably determinable.
3. Collectibility of the full license fee is reasonably assured.
4. The film has been accepted by the licensee in accordance with the conditions of the license agreement.
5. The film is available; i.e., the right is deliverable by the licensor and exercisable by the licensee.

The Division concludes that broadcasters' accounting should parallel the accounting by the licensor (although condition (3) above would not, of course, apply) and, accordingly, assets and liabilities should now be recorded in the accounts for the rights acquired and the obligations incurred under license agreements for those films available for telecasting.

The assets should be segregated between current and noncurrent based on estimated usage within one year, and the liability should be segregated between current and noncurrent based on the payment terms specified in the license agreement. This is in accordance with generally accepted accounting principles as set forth in Accounting Research Bulletin No. 43, Chapter 3, Section A, and is also the predominant practice in the industry. The commitment for license agreements executed but not recorded because they are not currently available for telecasting should be disclosed in the notes to the financial statements.

The Division believes that film rights should now be amortized based on the number of future showings estimated by management. This applies equally to licenses providing for limited showings and those with unlimited showings. Feature films should be amortized on an individual film basis. Film series and other syndicated products should be amortized on a series basis. Amortization of feature films on a film package basis may be appropriate if it approximates the amortization that would have been provided on a film-by-film basis. Licenses providing for unlimited showings of cartoons and films with similar characteristics may be amortized over the period of the agreement since this type of film may, in practice, actually be shown on an almost unlimited basis. Costs should be allocated to individual films within a film package on the basis of the relative value of each to the broadcaster.

The Division has concluded that an accelerated method of amortization which takes into consideration the station's programming pattern is now required when the first showing, as is usually the case, is more valuable to a station than reruns. Accordingly, the straight-line method of amortization is only acceptable in those instances where each telecast is expected to generate similar revenues.

Film costs should be carried in the balance sheet at the lower of unamortized cost or estimated net realizable value on a film-by-film, series, or package basis, as appropriate. Unamortized cost would normally not exceed estimated net realizable value; however, in those situations when management's expectations of the programming usefulness of a film, series or package are revised downward, it may be necessary to charge expense to reduce unamortized cost to estimated net realizable value. A write-down from unamortized cost to a lower estimated net realizable value establishes a new cost basis. Similar losses expected to arise from unrecorded television film license agreements should also be provided for by a charge to expense.

Finally, the Division has also concluded that the provisions of APB Opinion No. 21 are applicable to television film license agreements and, accordingly, interest should now be imputed on the recorded liabilities and amortized as interest expense in conformity with paragraph 15 of the Opinion.

## BARTER TRANSACTIONS

### Industry Practice

Present practices for recording barter revenue vary considerably, as indicated below:

1. Revenue and expense are not recognized for financial reporting purposes. (Memorandum records are usually maintained for FCC reporting purposes.)
2. Revenue is recorded when commercials are broadcast.
3. Revenue is recorded when merchandise or services are received.

There is also a lack of uniformity in the methods of valuing the two sides of the transaction:

1. Fair value of merchandise or services received.
2. Retail value of merchandise or services received.
3. Value of commercial spots at standard ("rate card") rates.
4. Value of commercial spots at a discounted rate.

## The Division's Conclusions

The Division has concluded that all barter transactions should now be recorded by estimating the fair value of the product or service received, in accordance with the provisions of paragraph 25 of APB Opinion No. 29. Barter revenue should now be recorded when commercials are broadcast, and merchandise or services received should be recorded when received or utilized. If merchandise or services are received prior to the broadcast of the commercial, the deferred revenue should be recorded. Likewise, if the commercial is broadcast first, a receivable should be recorded.

Television film license agreements, game shows and other programming, exclusive of network programming, obtained in exchange for a specified number of commercials should be valued at the fair value of the programming received.

Barter revenue should be disclosed in the financial statements when it is material, in accordance with paragraph 28 of APB Opinion No. 29.

## INTANGIBLE ASSETS

### Industry Practice

A network affiliation agreement and an FCC license are intangible assets frequently transferred to the buyer upon the purchase of a broadcasting station. An additional intangible asset arising upon the acquisition by purchase of a broadcasting station may be an excess of cost over the fair value of net identifiable tangible and intangible assets acquired (goodwill).

Present practices with regard to the balance sheet presentation of these items and their amortization vary. Amounts allocated to network affiliation agreements, FCC licenses and goodwill are frequently presented by some companies as one amount and identified as "Intangibles," "Excess of Cost Over Underlying Net Assets Acquired," or other all-encompassing descriptions which frequently include the word "Goodwill." Other companies, however, segregate their intangible assets into components on the face of the balance sheet or in the notes thereto. Companies amortize these intangible assets in conformity with the requirements of APB Opinion No. 17 and generally use the maximum 40-year period for assets acquired after October 31, 1970, the effective date of APB Opinion No. 17. Intangible assets arising prior thereto are usually not amortized on the basis that there has been no diminution in value.

The Institute of Broadcasting Financial Management, Inc., the financial management association of the broadcasting industry, and the

National Association of Broadcasters have established a joint committee which has submitted a position paper to the Financial Accounting Standards Board on accounting for intangibles in the broadcasting industry.

The joint committee believes that broadcasting intangibles have several characteristics which are shared with few, if any, other types of intangible assets, for the following reasons. First, broadcasting licenses and network affiliation contracts are identifiable assets which are granted under contractual terms having a virtually unlimited duration. Secondly, they have historically retained their original value and generally increased in value over a period of time. Third, the intangibles are marketable assets, inasmuch as they can be and frequently are sold, thus their value when compared to the sales of similar properties can be reasonably estimated.

The joint committee's position paper requests that Accounting Principles Board Opinion No. 17 be modified by the Financial Accounting Standards Board, to provide that (1) the amortization or write-down of broadcasting licenses and network affiliation contracts be required only if their estimated value and future benefits are lower than their carrying value and (2) that the amortization or write-down of these assets below their residual value not be required. The joint committee acknowledges that a diminution in the value of these intangible assets should be recognized either through systematic amortization or write-offs as is warranted by the circumstances.

The Division's Conclusions

The Division believes that the provisions of APB Opinion No. 17 apply to intangibles in the broadcasting industry as well as in other industries and should be followed, absent any action by the Financial Accounting Standards Board.

APB Opinion No. 16, paragraph 68, requires that the cost of an acquisition be allocated to each individual asset acquired on the basis of its fair value. The individual assets are comprised of the tangible and identifiable intangible assets acquired. APB Opinion No 17, paragraph 26, elaborates on this with the statement that "Cost should be assigned to all specifically identifiable assets; costs of identifiable assets should not be included in goodwill." Therefore, separate costs should be assigned to network affiliation agreements and any other identifiable intangible assets.

The Division has concluded that when a network affiliation is terminated and not immediately replaced or under agreement to be replaced, the unamortized balance of the amount originally allocated to the network affiliation should be charged to expense. If a network affiliation is terminated and immediately replaced or under agreement to be replaced, and the fair value of the new network affiliation equals or exceeds the unamortized cost of the terminated affiliation, no gain should be recognized. However, a loss should be recognized to the extent that the unamortized cost of the terminated affiliation exceeds the fair value of the new affiliation.

The amortization policy of the broadcaster should not be changed solely because there has been a change in the network with which the station is affiliated.

*   *   *   *   *   *   *

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