Abstract

This paper investigates the use of intangible asset accounting and the selection of accounting policies in the football industry, an environment where discretionary choices were available concerning accounting for transfer fees. Additionally, companies in this dynamic and socially influential industry are unique in recognising investments in human resources on the balance sheet. Proxies representing the level of tax costs, equity depletion, underwriter pressure and auditors used are found to have significant associations with policy selection. This contributes to the debate over the role of discretionary choices, particularly regarding the accounting treatment available for intangible assets, in financial reporting.¹

1. Introduction

Interest in reporting human resource accounting measures for external financial reporting peaked and foundered in the 1970’s (Flamholtz, 1985; Scarpello & Theeke, 1989; Johanson, 1999). Its movement from conceptually attractive proposition to application faltered on issues of asset recognition, as a controlled future economic benefit, and the lack of reliable measurement bases. The debate then widened in attempting to recognise intangible assets, particularly brands, and to dissect goodwill. This came as a response to widening book to market values and a decrease in the net worth of companies from goodwill write-offs prior to the introduction of FRS

¹ I am grateful for the helpful and constructive comments of anonymous BAR referees.
FRS 10 was the first UK standard to specifically address intangible assets, after an earlier attempt, ED 52, was withdrawn after criticism from the business community. FRS 10, released in 1997, recognises intangibles whose fair value can be measured reliably. By linking recognition criteria to measurement, only purchased intangibles with an identifiable transaction cost, generally appear on the balance sheet. Internally generated intangibles are only recognised if they have a readily ascertainable market value.

Although expensing purchased intangibles, a choice available in this study, is no longer available since the introduction of FRS 10, the issue of accounting for intangible assets is still the subject of debate. Several commentators (see for example, Lev & Zarowin, 1999; Eustace, 2000; Vance 2001) have highlighted the inconsistencies between the treatment of purchased and internally generated intangibles. At present, companies must capitalise the former and expense the latter, leading to incomparable results that may be indifferent in terms of their future economic benefit generating potential. The IASB have identified this problem in IAS 38, expressing concern that the guidance is ‘not sufficiently robust’ (IASB, 2001).

The issue of accounting for human resources remains relevant as the industrial shift from a manufacturing-based economy to a knowledge-based economy continues. Entities in more technologically intensive economies increasingly derive more value from intangible rather than tangible factors. Intellectual capital, brands, human resources, utilisation of information and communication technologies and business process improvements affect company performance and position. The identification and utilisation of intangible assets, and the communication of their value is viewed as a key competitive driver (Eustace, 2000). Expenditures on investments in intangibles have been shown to generate future economic benefits (Amir & Livne, 2001; Lev,
However, many intangibles are not recognised in financial reporting leading to a potential decline in the relevance of the financial statements. Increasing book to market values in the last 20 years are argued to be partially attributable to an increasing proportion of unrecorded intangible assets (Lev, 2001; Edvinsson, 2000).

The football industry is the only UK sector where human resource accounting has been applied in financial reporting, in accounting for transfer fees (Morrow, 1999). A high media profile and public interest in football have generated interest in the activities of the companies that organise professional teams. Increasing demand for football and a period of rapid growth and commercialisation have led to a stronger public focus on these companies.

In this industry, a wide variety of policies was employed in accounting for transfer fees until FRS 10. This provides an environment in which to examine what motivates the selection of accounting policies where the reporting effects are highly material and choices are freely discretionary. Several established theories, notably concerning contracting cost, signalling and legitimacy, have been seen to provide a rationale for the discretionary choice of accounting policies in general. The aim of this paper is to explore whether discretionary choices in accounting for intangible assets in the football industry are influenced by such motives.

This paper is organised as follows: section 2 introduces the football industry before detailing transfer fee accounting in section 3; section 4 discusses the motivations in selecting accounting policy; research design and results are described in sections 5 and 6, and some conclusions are drawn in section 7.

2. The Football Industry

The football industry is defined as those companies specifying their core activity as operating a professional football club. Hence, the income and expenditure of all industry members
derives from this activity. The central item of revenue expenditure is staff wages whereas capital expenditure is concentrated on the purchase of player registrations and stadium development. Central income streams comprise gate receipts from attendance at matches, payments to acquire rights to broadcast matches, sponsorship/advertising and merchandising branded products or services.

Matches, by definition, are ‘produced’ jointly by competing organisations. This leads to unique structures in the industry such as income redistribution through the sharing of broadcasting fees and labour market restrictions on transferring players, that help maintain a competitive balance, essential to the success of all industry participants (Commission On Industrial Relations, 1974; Quirk & Fort, 1992).

The main asset base for all companies is the exclusive ownership of football player registrations and in the majority of cases, the ownership of a football stadium. Training grounds, shops and ‘staff houses’ are common whereas hotels and car parks are more atypical assets. Clubs can be distinguished by their size and consequently, the funding of their activities. Traditionally, bank loans, guaranteed on the personal assets of directors or shareholders, have formed the main source of capital. This also tended to prevent the concentration of control by a major shareholder being diluted by share issues. In the 1990’s, clubs increasingly sought equity to fund expansion, from a stock market initially encouraged by greater industry demand and higher expected returns.

The size of the industry is relatively small: 25 listed clubs in the UK had a market capitalisation at 27 June 2001 of £1,119 M. The number of investor stakeholders having a potential interest in the financial reports of football clubs has increased as the individual and institutional shareholder base has widened after share issues. As a result, supporter stakeholders and shareholders have demanded greater accountability from the clubs (see Hamil, Michie & Oughton, 1999; Hamil, Michie, Oughton & Warby, 2000) and have become increasingly
organised in establishing group trust shareholdings that in some cases have majority ownership (Frampton, Michie & Walsh, 2001). Media coverage of and public interest in football naturally extends to the football club companies, including how they are financed and their accountability to all their stakeholders. The cultural status of football in the UK defines the social significance of the industry.

Modern literature on the UK football industry covers several disciplines. Szymanski & Kuypers (1999) identify successful business strategies based upon a historical analysis of the industry. Morrow (1999) and Sutherland & Haworth (1986) document the changing environment by studying industry economics, regulatory structures and finance. Other literature explores the effects of commercialisation (for example, Hamil et al, 2000, 1999; Conn, 1998; Dempsey & Reilly, 1998). The accounting treatment of transfer fees is discussed in Michie & Verma (1999), Morrow (1996, 1995, 1992), Brummans & Langendijk (1995) and Biagioni & Ogan (1977). However, few empirical studies have examined the whole UK football industry. Dobson & Gerrard (2000) and Carmichael & Thomas (1993) test the economic determinants of transfer fees whereas Deloitte & Touche (1996-2001) publish biannual financial reporting information for the English leagues. Amir & Livne (2001) address the issue of whether player registrations are assets by examining their potential to generate future economic benefits. Based on a sample of 58 UK clubs, they find that investing in player registrations does lead to probable future economic benefits over a short economic life and they offer some observations on the accounting policy choices selected. This paper aims to further examine and empirically test the choices motivating the selection of transfer fee accounting policies.
3. Accounting for Transfer Fees

The accounting policies examined are those relating to transfer fees. Transfer fees are payments made to acquire the player registration of a football player, and provide exclusive access to the professional footballing activities of the individual. The accounting treatment depends upon whether payments for player registrations are recognised as expenses or assets, and whether the contract provides sufficient control over the revenue generating abilities of the players in playing competitive professional football (Morrow, 1999). Although disparities were found in policies used for capital grants, stadia depreciation and signing-on fees, accounting for transfer fees represents the most controversial area in football industry reporting.

The conventional and traditional treatment of transfer fees was to account for them as an expense in the profit and loss account. The transaction was recognised as an operating or ‘exceptional’ item in the period in which a contract was signed. No value for player registrations was carried on the balance sheet. Known as an ‘expense’ policy, its rationale derives from unreliability of future benefits due to injury and form, and the limitation of control to footballing services, allowing a player to exit the club to any non-footballing employment.

This policy increases expenses and thus reduces reported income in the year the contract is signed. Less retained earnings are transferred to the balance sheet. Ceteris paribus, this policy decreases income and/or net assets.

An alternative, ‘recognition’ method adopts a human resource accounting type approach with the costs of purchasing and also generating player registrations recognised as assets. Two general variations have been used.

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2 This has to some extent been alleviated by FRS 10 which stipulates the ‘capitalisation’ policy.
3 See Rowbottom (1999).
4 One club also disclosed the amount written off on transfer fees as a ‘dangling debit’ in its reserves.
A ‘capitalisation’ policy recognises purchased player registrations (transfer fees paid) as intangible assets. They are amortised over the length of the respective player’s contract to an estimated residual value. Provisions are made for any permanent diminution in value below the amortised value, such as through injury or retirement. No asset value is attributed to non-purchased (internally generated) player registrations held by the club. Although based on a cost approach to human resource accounting, no identifiable training costs are allocated, due to difficulties in the separable measurement of generating a valuable player registration.

An alternative valuation approach attributes asset values to all player registrations. All registrations are valued, by the manager and/or directors, and recognised as assets on the balance sheet. Transfer fees paid are capitalised and added to the player registration account. Changes in the carrying value of both internally generated and purchased player registrations are taken to a revaluation reserve. Further variants were identified; two clubs recognised all player registrations held as investments in the current assets of the balance sheet, and one club wrote off transfer fees to expenses when paid whilst recognising all player registrations in the balance sheet.

All ‘recognition’ policies increase fixed assets in the balance sheet. They generally increase net profit overall, as no transfer fee is charged to expenses in the year of purchase and subsequent amortisation charges are often omitted. Where amortisation was charged, clubs generally made a profit on the sale of registrations due to high inflation in the transfer market. Ceteris paribus, this policy increases income and/or net assets.

Accounting policies for transfer fees and player registrations from the sample set of 102 clubs (defined later in the paper) are displayed in Table 1. The policies are classified on the criteria listed above as ‘expense’ or ‘recognition’. The following section examines the rationales for choosing different policies suggested in prior research.
Table 1: Classification of Transfer Fee Accounting Policies by Sample Set Companies in 1995

<table>
<thead>
<tr>
<th>Recognition Policies</th>
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<tr>
<td>Capitalisation &amp; Amortisation of Fees Paid</td>
<td>8</td>
</tr>
<tr>
<td>Recognition of all Player Registrations as Fixed Assets</td>
<td>5</td>
</tr>
<tr>
<td>Recognition of all Player Registrations as Current Assets</td>
<td>2</td>
</tr>
<tr>
<td>Recognition of all Player Registrations as Fixed Assets with write off of transfer fees paid</td>
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</table>

<table>
<thead>
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<th>Expense Policies</th>
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</thead>
<tbody>
<tr>
<td>Write off as operating expenses</td>
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</tr>
<tr>
<td>Write off as exceptional expenses</td>
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<tr>
<td>Write off with dangling debit</td>
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</tr>
<tr>
<td>Total</td>
<td>86</td>
</tr>
</tbody>
</table>

4. Motivations in Choosing Accounting Policy

The most widely researched area on the selection of accounting policies has been based on differing contracting and information costs associated with different policies (see for example, Zmijewski & Hagerman, 1981; Healy, 1985; Watts & Zimmerman, 1986; Duke & Hunt, 1990; Mohrman, 1993; Muller, 1999; Lin & Peasnell, 2000). The impact of contracting costs and thus organisational cash flows in motivating management behaviour may be real or perceived.

From this literature, several motivations are extracted as being of relevance in explaining the choice of transfer fee accounting policy in the football industry. These motivations are discussed below.
a) Tax costs

Tax computations may allow the use of the same policies used in financial reports in non-standard areas where tax treatments have yet to be formalised, such as transfer fees. Cloyd, Pratt & Stock (1996) and Riley (1999) suggest that where financial reporting and tax treatments are ambiguous, selecting the same method for tax and accounting purposes reduces the probability of a challenge from the tax authorities. The case of Herbert Smith v. Honour (1999) supported the use of GAAP in determining tax relief where no specific tax rules were applicable (Rayney, 1999, p.99). Section 63 of the 1999 Finance Act accepted that determination of tax liabilities would follow the accounting treatments used for transfer fees existing both before and after the introduction of FRS 10 (Riley, 1999, p.96). Thus, managers could alter the timing of tax payments in their selection of policy before FRS 10, ‘Goodwill and Intangible Assets’. This strategy may not be considered unusual in sport in general (see Quirk & Fort, 1992) or in the football industry in particular. An investigation into fiscal fraud by top Italian football clubs highlighted the use of transfer fee accounting policy to minimise tax liabilities. Clubs were alleged to have organised fake transfer deals in order to write off transfer fees payable against taxable profits (The Guardian, 1998).

This paper proposes that a club extensively purchasing player registrations could select an expense policy to minimise their tax liability, whilst those clubs capitalising players would have greater difficulty in claiming tax relief on transfer fees paid. Therefore, it might be anticipated that highly profitable clubs (before transfer fees) with high potential tax liabilities would seek to employ an ‘expense’ policy. Alternatively, less profitable clubs with low tax potential tax liabilities might also have an incentive to employ a ‘recognition’ policy.
b) Political costs

Watts & Zimmerman (1986) propose that the political sensitivity of a company may affect potential contracting costs. They suggest that politicians may use reported corporate financial performance as a justification for proposing wealth transfers. Hence, they hypothesise that where organisations are subject to potential wealth transfers as a result of the political process, managers adopt accounting policies that reduce the probability of transfer.

The football industry is more influential, both socially and politically, than most other industries of a comparable size as can be seen from the significant public interest in the finances of football club companies in addition to the matches themselves. Thus, it is possible that football club companies are susceptible to incurring political costs, which, in this context, include negative publicity, greater financial scrutiny and regulation. Negative publicity is created by significant media attention and can affect income. High operating profits and bad publicity regarding finances may lead to tighter constraints and more comprehensive financial scrutiny, particularly in a context of increasing commercialisation.

Although publicity, both positive and negative, is a permanent feature of a socially influential industry, several extraordinary regulatory initiatives were begun in the 1990's as a response to its commercial growth. The risk of such initiatives generating political costs is considered real following intervention in 1995 by the European court concerning regulations governing the transferral of player registrations, greatly reducing the period of control provided by player registration payments (European Commission, 2000). It restricted the period of control over the player registration to the length of the players contract, thereby reducing previously valuable player registrations to a net realisable value of zero at the end of a players contract. A ‘Football Task Force’ was set up by the government in July 1997 to investigate all aspects of contemporary football. Its final report, Commercial Issues, recommended the appointment of a
Football Audit Commission with wide ranging powers, including restraints on ticket prices, merchandising and the transfer of club ownership plus greater accountability to stakeholders with audited performance indicators (Football Task Force, 1999). The OFT investigated the legality of collectively selling FA Premier League television rights in 1999 (RPC, 1999), and the government upheld the MMC’s recommendation to block the acquisition of Manchester United by British Sky Broadcasting in 1999 (OFT, 1999). Thus, in addition to its high profile and general interest among the electorate, the football industry is argued to be susceptible to political costs.

c) Equity depletion & underwriter pressure

It has been argued that a motivation in selecting intangible asset accounting policy may be the desire to avoid equity depletion (Moorhouse, 1990, p.33). Football club companies had traditionally low accounting net worth because of their low equity funding and lack of profitability.

In the period examined, the impact of equity depletion was potentially greater in an environment where several clubs were seeking finance on the capital markets to fund stadia development and increasing commercialism. The decision making process of management is restricted by a desire to conform to the expectations and/or constraints of the capital markets. Securities underwriters have been claimed to be resistant to underwriting an issue on the market with low or negative book value (Malmquist, 1990, p.176). If demand for the issue is low or the company subsequently becomes insolvent, underwriters will incur negative publicity and can be sued by clients. The probability of insolvency or poor price performance will be affected by cash flows and not accounting policy. However, Malmquist (1990, p.176) suggests that if an organisation does become insolvent, the underwriter is in a better position if an accounting policy
gives higher net assets and/or more stable income. Thus, it is argued that underwriters will protect themselves by pressuring organisations to employ net asset increasing policies.

This motivation can be described as legitimacy theory, whereby managers seek to legitimise the club finances (Wilmhurst & Frost, 2000). Management must meet the demands of the investment community that clubs are credible, well-run businesses suitable for profitable investment rather than appealing only to fans. Employing a ‘recognition’ policy in accounting for transfer fees would not directly affect contracting costs or cash flows, but by resisting the expectations of the capital markets, clubs may face higher future underwriting costs and, possibly, higher costs of capital.

Several cases provide support for testing this proposition. For example, the 1995 reports of Preston North End (Holdings) Ltd were authorised on 7 August. In those accounts, the transfer fee accounting policy was changed from an expense approach to an asset recognition policy. The effects of selecting the asset/income increasing policy, disclosed as a prior year adjustment, were that net liabilities for the period ending 1994 were restated at £(18,164) from £(411,419) and the retained profit for the year rose to £24,208 from a loss of £(165,772). The company subsequently moved to a positive net assets balance of £937,437 for the period ending 1995. The rationale given for the change was to provide a fairer presentation of trading performance and financial position. The company was re-registered and re-named as Preston North End plc on 5 September 1995. On 11 September, a share prospectus was issued including a copy of the 1995 audited accounts as part of the Accountants’ Report, but omitted a note on prior year adjustments concerning the accounting policy change that had been in the published accounts, the only change between the audited accounts as returned to the Registrar of Companies and those contained in the prospectus. Thus, no mention was made of the recent

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5 Audited accounts in a prospectus do not constitute statutory accounts within meaning of section 240 of the Companies Act 1985.
policy change in accounting policy and its impact on the past and future reported results of the company. Finally, shares of the company were admitted to the Alternative Investment Market (AIM) on 14 September 1995.

The 1994 annual reports of The Celtic Football and Athletic Company Ltd showed several accounting policy changes. Their cumulative effect was to increase the profit and loss account reserves by £6,824,003. Of this figure, £5,929,056 was a reclassification of reserves; the other £894,947 was the result of accounting policy changes. The company was re-named and re-registered as Celtic plc on 15 December 1994, in anticipation of flotation on the stock exchange. The 1995 annual reports showed that the accounting policy for transfer fees had changed from an ‘expense’ policy to a ‘capitalisation’ policy. This compounded the loss for the period ending 1994 by £1,286,000 but increased net assets by £3,883,000. Shares of Celtic plc were admitted to the AIM on 29 September 1995.

The 1994 annual reports of Sunderland Association Football Club Ltd included a change to transfer fee policy from ‘expense’ to ‘recognition’. The effect was to increase the net assets of the company by £4,307,051. By 9 December 1996, a holding company, Sunderland plc, had acquired all the share capital of the Sunderland Association Football Club Ltd. On 10 December 1996, a share prospectus for Sunderland plc was published. It included audited accounts for periods ending 1994-1996, but these did not disclose the transfer fee policy change. The shares were admitted to the London Stock Exchange on 24 December 1996.

These examples illustrate specific cases where transfer fee policies had been changed before flotation and had a material impact on the net assets and/or income of the company. This study will test the assertion, that underwriter pressure may affect accounting policy choice, on the whole sample data set.
It may also be that other parties such as auditors exert pressure on accounting policy selection. They have an incentive not to support a company's financial position that proves misleading upon flotation (Beattie, Brown, Ewers, John, Manson, Thomas & Turner, 1994). A study by Menon & Williams (1991) supported the claim that underwriters were reluctant to bring issues to the market unless those organisations had ‘credible’ auditors. Those who may be liable for the reliability of the information published in the financial statements have an incentive to influence the preparation of those financial statements; an incentive exists to minimise the probability of liability.

Other motivations have been tested in the policy choice literature. Companies may signal future performance whereby a positive signal may suggest improved expectations of future performance (Aboody, Barth & Kasznik, 1999). Clubs changing transfer fee accounting policy stated that it gave a better representation of the financial position and performance, or that the policy change was necessary to provide ‘a true and fair view’ (for example, Celtic plc). This can be interpreted under a signalling perspective as reflecting future expectations and thus future market performance (O’Hanlon & Pope, 1999). However, information asymmetries in the football industry are diminished due to media speculation over and public disclosure of material inflows and outflows of football clubs. For example, media speculation over transfer fees (market values of player registrations) reduces the power of any signal as users are informed on fluctuations in the carrying value of player registrations. Further details on wages and contract details are also regularly disclosed. Details of other material transactions are also disseminated in the public domain, due to the demand for information about the football industry. For example, records of match receipts, broadcasting revenues, attendances, sponsorship revenues, grants and policing costs were all provided by the Football Trust over the sample period (see Football Trust, 1996).
Thus, the opportunity for companies to signal changes in future expectations are limited in this environment as sources other than the financial reports provide information relevant in estimating future performance. Brown & Hartzell (2001) describe the process of how non-accounting information about an US professional basketball club is impounded by the market in revising expectations of company performance, thereby reducing the impact of traditional financial reporting disclosures. Therefore, it is argued that any financial reporting signal would not yield any significant information that had not been disseminated through alternative informational channels. For this reason, a signalling motivation is not considered in this context.

The debt contracting cost hypothesis was also considered irrelevant due to industry characteristics. More specifically, debt covenants were extremely rare and company debts are normally guaranteed independently by a shareholder or director. Thus, policy choice did not affect debt contracting costs. The bonus plan hypothesis was also thought irrelevant due to the irregularity of financial performance related pay. A discussion of how the motivations, outlined above, will be tested is provided below.

5. Research Design

a) Data Collection

The sample for this study comprises of all football club companies in the English Premier League, English Football League and the Scottish Premier League. Other football club companies outside these leagues are omitted because they are not generally full-time professional football clubs. The sample size is 102, and represents nearly all UK professional football companies. Data was collected from the financial reports for the period ending 1995 for all clubs in the sample.6
b) Variables

The response variable, TRAN, represents the transfer fee accounting policy used in 1995. This dummy measure equals 1 for companies using a ‘recognition’ policy and 0 for those using an ‘expense’ policy.7

To test whether the selection of policy could be affected by tax costs, several proxies are used. One variable measures the availability of tax losses to carry forward from the previous year. Those clubs with taxable losses would have less incentive to expense transfer fees in order to reduce their tax bill. A dummy, TAXLCF, is used, as the absolute size of tax losses was not universally disclosed. The second measure was net transfer fees receivable, NTF, which attempts to identify those clubs gaining more from ‘recognising’ player registrations. Clubs with high transfer fees receivable would have potentially higher taxable profits. A third proxy, taxable profit, (PBTTF) is measured by the profit on ordinary activities before tax and player trading for the period. Both net transfer receivable and taxable profits are scaled by turnover (excluding transfer fees receivable) to control for size effects. A substitute proxy for TAXLCF, the effective tax rate (ETR), is reported in an alternative specification, model 2. This is defined as the negative tax charge in the 1994 profit & loss account divided by the profit on ordinary activities before tax and player trading.8

Many studies have analysed the relationship between political sensitivity and asset/income decreasing policies suggested by the political cost hypothesis (see for example, Daley & Vigeland, 1983; Lin & Peasnell, 2000). Although empirical tests have been generally supportive of the hypothesis, size variables are often used to proxy for political sensitivity in

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6 A questionnaire sent to all sample clubs (33 usable responses) and a questionnaire sent to 70 bankers of football clubs (23 usable responses), as part of a wider research project aimed at assessing the usefulness of football club accounts, helped corroborate the data extracted from the football club financial reports.

7 See Table 1
testing (Zmijewski & Hagerman, 1981; Malmquist, 1990). It is suggested by Watts & Zimmerman (1990) that politicians and regulatory bodies are only attracted to potential ‘irregularities’ where their scale is large enough to arouse public attention. However, they state that a formal relationship between the probability of incurring political costs and size has not been established and may be subject to interacting effects. This has led to doubts over whether political sensitivity, size, or unknown effects captured by size are associated with accounting policy choice. This study will attempt to measure political sensitivity through its level of public exposure in the electorate, measured by the league in which it competes (DIV), rather than financial size. Clubs competing in the higher leagues are subject to greater public exposure, and generate greater public interest in and scrutiny of their operations, performance and position. Indicators of financial size based on the balance sheet are not considered relevant as they are subject to equity depletion, resulting from the selection of transfer fee accounting policy. Due to the difficulties in capturing political sensitivity, two measures of financial size not subject to the equity depletion problem are substituted for DIV in testing. The log of turnover (LTURN) and log of average attendance 1993-1995 (LAVEAT) are included as alternative specifications in models 3 and 4 respectively.

The effects of equity depletion in influencing accounting policy choice are measured by the percentage change in net tangible assets over the year (PCHEQDEP).[^9] This seeks to capture the relative effect of equity depletion given the level of net assets available. A dummy variable, DNTL, highlights those clubs with net tangible liabilities in 1994. This investigates whether a club with a low, absolute level of equity reserves is motivated to select a ‘recognition’ policy. A substitute proxy for DNTL, DQUAL, is also reported as an alternate measure in model 5. DQUAL, a dummy variable, represents those clubs whose auditors have noted a fundamental

[^9]: The tax charge is given a negative sign to distinguish it from tax refunds in the data set. As suggested by Gupta & Newberry (1997), tax refunds are recorded as 0% (ETR = 0) and paying tax upon negative income is recorded as 100% (ETR = -1.0).
uncertainty or qualified their opinion with respect to the application of the going concern principle. This seeks to investigate whether those clubs whose funding adequacy has been highlighted by the auditors have an incentive to adopt an asset/income increasing recognition policy. Although auditor judgements are highly unlikely to be affected by a cosmetic accounting policy change, an incentive, however irrational, may still exist to ‘strengthen’ the balance sheet where funding weaknesses have been exposed.

The presence of underwriter pressure (UNDP) is measured by those clubs listed or considering a capital market listing when selecting transfer fee accounting policy. It captures those companies listed on the full list of London Stock Exchange or AIM, or announcing plans to list at the date upon which the directors approved the financial statements.\textsuperscript{10}

To test whether there was any association between the accounting policy selected and having a ‘credible’ auditor, a dummy variable (AUDP) was used representing whether the club employed a ‘big six (five)’ auditor. A summary of the proxies and their predicted signs in the selection of transfer fee policy is provided later, within Table 3 which reports the regression results.

c) Statistical Test

Descriptive statistics, shown in Table 2, indicate the distributional characteristics of the response and explanatory variables. The distribution of the response variable, TRAN, is skewed to the left and has a mean of 0.16, representing 16% of clubs used a ‘recognition’ transfer fee accounting policy.

\textsuperscript{9} PCHEQDEP is calculated with a positive denominator to ensure that companies with improving net tangible liability positions receive positive values. PCHEQDEP = \frac{\text{Net Assets}_t - \text{Net Assets}_{t-1}}{|\text{Net Assets}_{t-1}|}

\textsuperscript{10} The statements used in the sample were approved between 26 June 1995 and 21 November 1996. Those clubs traded on the unregulated trading facility OFEX, are not thought to be susceptible to underwriter pressure. Shares are thinly traded and are rarely offered en masse. This facility also requires little financial disclosure to users.
TAXLCF equals 1 if the company has tax losses to carry forward and 0 if there are no available tax losses. The mean of 0.44 signifies 44% of the sample companies had corporation tax losses to carry forward against future tax charges. The mean of the effective tax rate (ETR) is -0.12 (or 12%) with only 20 sample clubs paying corporation tax during the period. NTF, the net transfer fees receivable divided by turnover has a mean of 0.040, representing that a small surplus was gained by the average club from player trading. PBTTF, the profit on ordinary activities before tax and player trading scaled by turnover, returns a mean of -0.18, indicating that the pre-tax loss margin at the average club was 18%.

DIV equals 4 for clubs in the highest division and 1 for those in the lowest division. The distribution of LTURN, the natural log of turnover, has a mean of 14.85, equating to an average turnover of approximately £2.8M. Similarly, the log of average attendance (LAVEAT) has a similar distribution and represents attendances between 1,738 and 43,993.

PCHEQDEP, the relative change in net tangible assets, ranges from -4.93, representing a 493% fall in equity reserves, to 6.23, representing a 623% increase in reserves. The mean change was a 9% increase in net tangible assets over the year. DNTL equals 1 where a company had net tangible liabilities in 1994 and 0 for those companies with net tangible assets. The mean, 0.43, indicates that 43% of the sample (44 clubs) had net tangible liabilities. DQUAL equals 1 where the club received an audit qualification or fundamental uncertainty relating to the applicability of the going concern concept and applied to 27% of the sample clubs. UNDP equals 1 for listed companies or those planning to list upon the date the financial statements are approved, and 0 otherwise. A mean of 0.12 indicates that 12% of the sample were listed or had announced a listing during the period of investigation. The dummy variable AUDP equals 1 where the company appoints a big six auditor, represented by 24% of the sample.
Table 2: Descriptive Statistics of the Response and Explanatory Variables of Sample Set Companies in 1995

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<th>Variables</th>
<th>Mean</th>
<th>Median</th>
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<th>Maximum</th>
<th>Std. Dev.</th>
<th>Skewness</th>
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<td>NTF</td>
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<tr>
<td>DIV</td>
<td>2.65</td>
<td>3</td>
<td>1</td>
<td>4</td>
<td>1.14</td>
<td>-0.17</td>
</tr>
<tr>
<td>LTURN</td>
<td>14.85</td>
<td>14.71</td>
<td>12.84</td>
<td>17.92</td>
<td>1.08</td>
<td>0.40</td>
</tr>
<tr>
<td>LAVEAT</td>
<td>9.01</td>
<td>8.96</td>
<td>7.46</td>
<td>10.69</td>
<td>0.82</td>
<td>0.20</td>
</tr>
<tr>
<td>PCHEQDEP</td>
<td>0.089</td>
<td>0.022</td>
<td>-4.93</td>
<td>6.23</td>
<td>1.56</td>
<td>0.048</td>
</tr>
<tr>
<td>DNTL</td>
<td>0.43</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>DQUAL</td>
<td>0.27</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>UNDP</td>
<td>0.12</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>AUDP</td>
<td>0.24</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

TRAN = Transfer Fee Accounting Policy
TAXLCF = Availability of Tax Losses Carried Forward
ETR = Effective Tax Rate
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DNTL = Net Tangible Liabilities
DQUAL = Going Concern Fundamental Uncertainty or Audit Qualification
UNDP = Listing Status
AUDP = Auditor
An empirical test is proposed that estimates the transfer fee accounting policy selected (TRAN) using a discrete choice model. This test can accommodate the discrete nature of the dummy response variable, TRAN, and the skewness inherent in many of the explanatory variables. Discrete choice models are common in policy choice studies (for example see Noreen, 1988; Stone & Rasp, 1991; Lin & Peasnell, 2000). As such, a probit regression procedure will provide a model of the probability of selecting a particular accounting policy given a set of attributes for the explanatory variables.\(^\text{11}\)

The model will take the form: \(P(y_i=k) = \Phi(a_{ki} + b_jx_{ji} + e_i).\)

d) Sensitivity Analysis

The effect of multicollinearity between some of the explanatory variables was assessed due to the various aspects of company or club size that are measured. High pairwise correlations, interpreted as greater than 0.4, were not found.\(^\text{12}\) Variance inflation factors, determined from auxiliary regressions of each explanatory variable on the remaining explanatory variables for each model were calculated between 1.02 and 1.74. All are significantly below 10, suggested by Gujarati (1995) as indicating that collinearity may be present. Analysis of residuals and leverage from initial regressions reveal 5 influential observations. All estimations are rerun using bounded influence regressions (see Maddala, 2001; Belsley, Kuh & Welsch, 1980).

A sample size over 100 reduces the chances of severe miscalibration of discrete choice test statistics (Stone & Rasp, 1991, p.179). The error term of the model is assumed to have a

\(^{11}\) The probit function, \(g(p)=\Phi^{-1}(p)\), represents the inverse of the cumulative standard normal distribution function. It was chosen due to its general applicability where frequency distributions approximate to it even if individual observations behave differently. It enables responses from 0 to 1, and the explanatory variables can range from \(-\infty\) to \(+\infty\), with non-constant and correlated error terms. Nevertheless, the results showed no material differences to those obtained using a logit link function model.
normal distribution and a mean of zero. Should this assumption not hold, the model might be invalid. The error term will account for parameters omitted from the model but can be considered valid as long as omitted terms are independent from existing terms.

6. Results

a) Model Fit

Five models are tested: the specified model (model 1) and four alternative specifications using substitute proxies that help assess the robustness of the estimators. Coefficients and goodness of fit statistics for all models are shown in Table 3. The model chi-square statistic tests the null hypothesis that all parameter estimates in the specified model are equal to zero. It is rejected at the 1% level for all models except model 4, where it is rejected at the 5% level. Wald statistics, testing the null hypothesis that the associated parameter estimates are zero, are also indicated in Table 3 with their significance with respect to a chi-squared distribution. To estimate the response probability of this model, \( P(TRAN) = \Phi(a + b_jx_{ji}) \).
Table 3: Coefficients of Specified Models for Probit Regressions on Transfer Fee Accounting Policy Choice by Sample Set Companies in 1995 (Wald test statistics in parentheses)

<table>
<thead>
<tr>
<th>Explanatory Variables</th>
<th>Expected Sign</th>
<th>Model 1</th>
<th>Model 2: Substituting LTURN for DIV</th>
<th>Model 3: Substituting LAVEAT for DIV</th>
<th>Model 4: Substituting ETR for TAXLCEF</th>
<th>Model 5: Substituting DQUAL for DNTL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>?</td>
<td>3.402 (7.791)&lt;sup&gt;c&lt;/sup&gt;</td>
<td>4.242 (0.750)</td>
<td>7.166 (2.895)&lt;sup&gt;a&lt;/sup&gt;</td>
<td>2.310 (8.211)&lt;sup&gt;c&lt;/sup&gt;</td>
<td>1.841 (7.169)&lt;sup&gt;c&lt;/sup&gt;</td>
</tr>
<tr>
<td>TAXLCEF</td>
<td>+</td>
<td>1.579 (6.920)&lt;sup&gt;c&lt;/sup&gt;</td>
<td>1.573 (6.978)&lt;sup&gt;c&lt;/sup&gt;</td>
<td>1.653 (7.025)&lt;sup&gt;c&lt;/sup&gt;</td>
<td>1.407 (7.450)&lt;sup&gt;c&lt;/sup&gt;</td>
<td></td>
</tr>
<tr>
<td>ETR</td>
<td>+</td>
<td></td>
<td>0.075 (0.010)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>NTF</td>
<td>+</td>
<td>1.195 (2.056)</td>
<td>1.215 (2.145)</td>
<td>1.224 (2.216)</td>
<td>0.439 (0.398)</td>
<td>0.720 (1.073)</td>
</tr>
<tr>
<td>PBTTF</td>
<td>-</td>
<td>-0.458 (0.371)</td>
<td>-0.457 (0.302)</td>
<td>-0.744 (0.795)</td>
<td>0.620 (0.795)</td>
<td>-0.639 (0.839)</td>
</tr>
<tr>
<td>DIV</td>
<td>-</td>
<td>0.161 (0.350)</td>
<td></td>
<td>0.129 (0.334)</td>
<td>-0.127 (0.366)</td>
<td></td>
</tr>
<tr>
<td>LTURN</td>
<td>-</td>
<td></td>
<td>0.089 (0.081)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>LAVEAT</td>
<td>-</td>
<td></td>
<td>0.454 (1.149)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>PCHEQDEP</td>
<td>-</td>
<td>-0.217 (1.935)</td>
<td>-0.212 (1.824)</td>
<td>-0.206 (1.774)</td>
<td>-0.259 (3.042)&lt;sup&gt;a&lt;/sup&gt;</td>
<td>-0.056 (0.174)</td>
</tr>
<tr>
<td>DNTL</td>
<td>+</td>
<td>1.507 (4.393)&lt;sup&gt;b&lt;/sup&gt;</td>
<td>1.374 (4.560)&lt;sup&gt;b&lt;/sup&gt;</td>
<td>1.540 (5.290)&lt;sup&gt;b&lt;/sup&gt;</td>
<td>1.187 (4.036)&lt;sup&gt;b&lt;/sup&gt;</td>
<td></td>
</tr>
<tr>
<td>DQUAL</td>
<td>+</td>
<td></td>
<td></td>
<td></td>
<td>-0.081 (0.025)</td>
<td></td>
</tr>
<tr>
<td>UNDP</td>
<td>+</td>
<td>1.507 (7.515)&lt;sup&gt;c&lt;/sup&gt;</td>
<td>1.490 (5.816)&lt;sup&gt;b&lt;/sup&gt;</td>
<td>1.283 (4.669)&lt;sup&gt;b&lt;/sup&gt;</td>
<td>1.734 (10.753)&lt;sup&gt;c&lt;/sup&gt;</td>
<td>1.263 (5.803)&lt;sup&gt;b&lt;/sup&gt;</td>
</tr>
<tr>
<td>AUDP</td>
<td>?</td>
<td>-1.729 (5.055)&lt;sup&gt;b&lt;/sup&gt;</td>
<td>-1.606 (5.018)&lt;sup&gt;b&lt;/sup&gt;</td>
<td>-1.832 (5.919)&lt;sup&gt;b&lt;/sup&gt;</td>
<td>-1.115 (2.885)&lt;sup&gt;a&lt;/sup&gt;</td>
<td>-0.869 (2.718)&lt;sup&gt;a&lt;/sup&gt;</td>
</tr>
<tr>
<td>Model χ² statistic</td>
<td></td>
<td>28.315&lt;sup&gt;c&lt;/sup&gt;</td>
<td>28.039&lt;sup&gt;c&lt;/sup&gt;</td>
<td>29.212&lt;sup&gt;c&lt;/sup&gt;</td>
<td>18.893&lt;sup&gt;b&lt;/sup&gt;</td>
<td>22.244&lt;sup&gt;c&lt;/sup&gt;</td>
</tr>
</tbody>
</table>

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\(^a\) Significant at the 0.10 level
\(^b\) Significant at the 0.05 level
\(^c\) Significant at the 0.01 level

\(b)\) Analysis

It was asserted that the potential to reduce tax costs could motivate the selection of policy. The measure representing the availability of tax losses, TAXLCF, is associated with the selection of a ‘recognition’ transfer fee policy. The coefficient is positive and significant at the 1% level in models 1, 2, 3 and 5. However, the alternative proxy specified in model 4, the effective tax rate (ETR), is not significantly different from zero. The measure of transfer fees receivable (NTF), measuring the potential to reduce tax from ‘expensing’ transfer fees, returned a positive sign but was insignificant. The coefficient for PBTTF, profit on ordinary activities before tax and player trading, is negative in models 1, 2, 3 and 5 and positive in model 4. However, the measure is not significantly different from zero in all models.

The association with tax losses suggests that the incentive to recognise intangible assets in this case was more prevalent if the company would not incur further tax costs in the current
period. This finding was supported by discussions with the financial director of one large UK club. It is argued that clubs recognising player registrations in their financial reports would use this treatment in assessing taxable profits. As a recognition policy generally increases taxable profits, only those clubs with tax losses available to set against would select this policy.

The possibility that more politically sensitive clubs would select ‘expense’ policies in order to avoid the risk of incurring political costs was tested. The coefficient for DIV was not significantly different from zero in models 1,4 and 5. Two alternative proxies, the log of turnover (LTURN) and the log of average attendance (LAVEAT) are tested in models 2 and 3. However, both return positive rather than negative coefficients and are insignificant. As such, proxies for political sensitivity representing public profile or financial performance did not appear to be associated with policy selection. This brings into question whether potential contracting costs are perceived in this environment and raises doubts about how effectively the measures chosen capture political sensitivity.

The coefficient of the proxy for relative equity depletion, PCHEQDEP, was negative and insignificant in models 1,2,3 and 5. However, in model 4, the coefficient is negative and significant at the 10% level. The coefficient of the proxy measuring whether a club had net tangible liabilities (DNTL) returned a positive sign and was significantly different from zero at the 5% level in models 1-4, suggesting equity depletion may have some explanatory power. An alternative proxy representing the existence of a going concern fundamental uncertainty or qualification in the audit report (DQUAL), reported in model 5, returns a negative sign but is insignificant.
These results provide some indication that a desire to avoid equity depletion per se may be an influence in policy selection. This is investigated further by examining the listing status of the clubs (UNDP), the proxy for underwriter pressure.

UNDP is positive and significantly associated with the selection of a ‘recognition’ transfer fee policy in all models. The coefficient is significantly different from zero at the 1% level in model 1 and 4, and the 5% level in models 2, 3 and 5. The hypothesis stated that clubs would be under pressure to select asset/income increasing transfer fee policies in order to ensure demand for the issue was adequate and that the reputation of the underwriters would remain intact regardless of subsequent price performance. It is suggested that underwriter pressure and capital market expectations do influence accounting policy selection. Expectations of capital market agents, such as underwriters, help form perceptions of credibility and legitimacy held by those selecting accounting policies. Those perceptions, in turn, constrain and influence their choice of accounting policy.

Finally, some negative association was found between the use of big six (five) auditors and the selection of a ‘recognition’ transfer fee accounting policy. The coefficient, AUDP, was negative and significant at the 5% level in models 1-3 and at the 10% level in models 4 and 5. The negative relationship indicates that companies employing big six auditors were more likely to adopt an ‘expense’ policy. From the sample data, it suggests that the use of larger, ‘more reputable’ auditors is associated with the use of a more conservative policy in this environment.

7. Conclusions

The intention of this paper has been to examine the selection of policies used in accounting for intangible assets. As investments on intangible assets continue to increase, it is argued that to maintain the relevance of financial reporting, their accounting treatment is likely to
evolve from that prescribed in FRS 10 and IAS 38, particularly the inconsistencies between the treatment of purchased and internally generated intangibles. This paper studies intangible asset policies in an environment where choices are discretionary and the effects upon the financial statements are material.

The setting for this study, the UK football industry, was chosen because of the freedom available in selecting policies in accounting for transfer fee payments, and the material effect of transfer fee policies on the profit & loss account and balance sheet. Data from 102 football club companies was collected to test associations between company characteristics and the transfer fee accounting policy. Statistical tests were carried out using probit discrete choice regressions, appropriate due to the discrete nature of the response variable and the skewness of several explanatory variables.

The test results, displayed in Table 3, show an association between those clubs listing on a capital market and transfer fee accounting policy. The paper argues that policy selection is constrained and influenced by perceptions of capital market expectations, consistent with legitimacy theory. The association found between the use of larger auditors and policy selection lends some support to this assertion. An association is also found between those clubs with corporation tax losses to carry forward and transfer fee accounting policy. The paper argues that those clubs susceptible to paying corporation tax selected an ‘expense’ transfer fee policy due to the probability that the policy selected for financial reporting purposes would be also be accepted for corporation tax computations and would therefore reduce tax costs. The findings of this paper provide insights into the selection of developmental intangible asset accounting policies in the absence of specific standard setting guidance. These insights may be usefully explored in contexts other than intangible asset and human resource accounting, where accounting treatments are developmental and, as a consequence, discretionary.
References


