


International Conference on  
Intellectual Capital Management  
IICM2009



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## Intangible assets valuation standards

**Dr. Ali Saghafi and Arash Tahriri**

arashtahriri@ut.ac.ir

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## Accounting for intellectual capital: a brief review

- AIC is a key constitute of broader intellectual capital field.
- Like accounting, It involve two complementary aspects: *measurement & reporting*.
  - Measurement and reporting of the success of IC management.
- Measuring this success provide a means of accomplishing accountability within the organization.

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## Definition of intellectual assets and intellectual liabilities

- In balance sheet terms, intellectual assets are those knowledge-based items, which the company owns which will produce a future stream of benefits for the company”
- the definition on intellectual assets can be widely interpreted for reporting purposes.
- intellectual liabilities
  - existing within the organization
    - weak
    - strategic planning processes, dangerous work conditions, potential environmental, clean up, potential product tampering and poor corporate reputation
  - existing outside
    - poor government policies and political
    - environment of a country

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## Measurement indicators of intellectual capital

- several models are proposed to measure intellectual asset and intellectual liability terms
  - price to book value
  - Tobin's 'q'
  - Calculated Intangible Value (CIV)
  - ...

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## The theoretical underpinning of accounting

1. The objectives of financial statements
2. The postulates of accounting
3. The theoretical concepts of accounting
4. The principles of accounting

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## 12 Objectives of Financial Accounting

1. Basic objective of financial statements is to provide information useful for making economic decisions
2. An objective of financial statements is to serve primarily users...who rely on financial statements as their principal source of information...
3. An objective of financial statements is to provide information useful to investors and creditors for predicting, comparing, and evaluating potential cash flows to them in terms of amount, timing, and related uncertainty.

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## 12 Objectives of Financial Accounting

4. An objective of financial statements is to provide users with information for predicting, comparing, and evaluating enterprise earning power.
5. An objective of financial statements is to supply information useful in judging management's ability to utilize enterprise resources effectively in achieving the primary enterprise goal.
6. An objective of financial statements is to provide factual and interpretive information about transactions and other events which is useful for...

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## 12 Objectives of Financial Accounting

7. An objective is to provide a statement of financial position, useful for...
8. An objective is to provide a statement of periodic earnings useful for...
9. Another objective is to provide a statement of financial activities useful for...
10. An objective of financial statements is to provide information useful for the predictive process. Financial forecasts should be provided when they will enhance the reliability of users' predictions.

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## 12 Objectives of Financial Accounting

11. An objective of financial statements for governmental and not-for-profit organizations is to provide information useful for evaluating the effectiveness of the management of the resources in achieving the organization's goals. Performance measures should be quantified in terms of identified goals.
12. An objective of financial statements is to report on those activities of the enterprise that affect society...

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## Accounting postulates

- They provide a set of rules informing accounting practice:
  - Entity
  - Going concern
  - Unit of measure
  - Periodicity

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## Accounting concepts

- Self evident statements or axioms that portray the nature of accounting entities operating in a free economy characterized by private ownership of property:
  - Property theory
  - Entity theory
  - Fund theory

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## Accounting principle

- They are most closely related to practice and thus more concrete in nature.
  - Accruals or matching concept
  - Consistency concept
  - Prudence concept
  - Cost principle
  - Objectivity principle

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## Accounting standards for Intangible Assets

- US (FASB)
- UK (ASB)
- International standards (AISB)
- Scandinavia
- Iran (Audit Organization)

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## US (APBs, SFASs, ...)

- APB 16 Business Combinations, APB 17 Intangible Assets,
- SFAS 2 Accounting for Research and Development, SFAS 44 Accounting for Intangible Assets of Motor Carriers, SFAS 61 Accounting for Title Plant, SFAS 63 Financial Reporting by Broadcasters, SFAS 68 Research and Development Agreements, SFAS 72 Accounting for Certain Acquisition of Banking or Thrift Institutions, SFAS 86 Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed (see also SOP 98-1 Accounting for the Costs of Computer Software Developed or Obtained for Internal Use, issued by AICPA), and SFAS 121 Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of.
- Some of the FASB Interpretations and Technical Bulletins are also related to intangible assets (e.g., Interpretations Nos. 4, 6, and 9, and Bulletins 84-1 and 85-5).

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## UK (FRSs, SSAPs, ..)

- FRS 2 Accounting for Subsidiary Undertakings, FRS 3 Reporting Financial Performance, FRS 10 Goodwill and Intangible Assets (which supersedes SSAP 22), FRS 11 Accounting for Intangible Assets in Scandinavia, the UK, the US, and by the IASC 247 Impairment of Fixed Assets and Goodwill,
- SSAP 2 Disclosure of Accounting Policies, SSAP 12 accounting for Depreciation, and SSAP 13 Accounting for Research and Development (see also the Companies Act of 1985).

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## International (IFRSs, IASs,...)

- IFRS 3 business combinations
- IAS 4 Depreciation, IAS 5 Information to Be Disclosed in Financial Statements, IAS 22 Business Combinations (revised), IAS 36 Impairment of Assets, and IAS 38 Intangible Assets (superseding IAS 9);
- the Exposure Drafts E60 Intangible Assets, its predecessor E50, and E61 Business Combinations.

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## Scandinavia

- Denmark
- Norway
- Sweden

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## Some considerations

- When it comes to intangible resources, standard-setters have been reluctant to recognize them as assets, particularly assets generated from activities such as R&D, because
  - recognition would be inconsistent with the asset recognition criteria and
  - give reporting entities larger possibilities to manage earnings by recognizing doubtful or even imaginary assets.
- However, we might trace a greater willingness over time to recognize intangible resources as assets, especially by the IASC and ASB, presumably because of pressure from financial statement users
  - We expect this pressure to increase as the importance of intangibles increases over time.
- Our review of how the FASB, the ASB, and the IASC account for intangible resources reveals little differences among these standard-setting organizations, presumably because
  - they are all dominated by the Anglo-American accounting tradition, focusing on the capital market as the primary users of financial statement information

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## Some considerations

- The reporting of intangible resources in Scandinavia follows the EU Fourth and Seventh Directives in which intangible assets should be capitalized in the balance sheet.
- Our review of accounting practice reveals that the Scandinavian countries have been less reluctant to recognize intangible assets in the balance sheet than standard-setting organizations in the UK, the US, and the IASC.
  - In credit-oriented economies, such as the Central European ones, it is important to signal the value of the collateral to banks as the main sources of finance.
  - ....

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## Iran

- استاندارد شماره ۷ (مخارج تحقیق و توسعه که لغو گردید).
- استاندارد شماره ۱۷ (دارایی های نامشهود، تجدید نظر شده سال ۱۳۸۶).
- استاندارد شماره ۱۸ (صورت های مالی تلفیقی و حسابداری سرمایه گذاری در واحدهای تجاری فرعی، تجدید نظر شده سال ۱۳۸۴).
- استاندارد شماره ۱۹ (ترکیبهای تجاری، تجدید نظر شده سال ۱۳۸۴).
- مبنای اصلی تدوین استانداردهای حسابداری در ایران، استانداردهای منتشر شده بین المللی است سایر استانداردهای موجود نیز مطابق با رویه های بین المللی می باشد.
- به عنوان مثال در استاندارد شماره ۷ که دیگر وجود ندارد مخارج توسعه و نه تحقیق به شرط تحقق شرایط خاصی قابل سرمایه ای

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## A Look into the future: How will intangibles reporting evolve?

- Several studies have proposed different ways of reporting on intangibles so that financial statements will reflect the increasing changes that affect the business environment.
- Together with the intellectual capital reports in the management field, accounting academics have suggested certain changes of the current accounting system so that the reporting model follows the pace of the modern economy.

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## A Look into the future: How will intangibles reporting evolve?

1. Similar to IAS 38 (1998) for development costs, or SFAS No 86 for software development expenditures, Lev and Zarowin (1999) and Høegh-Krohn and Knivslå (2000) support the condition-based cost capitalization approach to account for certain intangible assets, with attributable benefit streams, together with the corresponding amortization or impairment test to revise the asset's value.
2. Abbody and Lev (1996), Barth and Clinch (1998), and Healy et al. (2002) go beyond a simple cost capitalization approach. They propose adding all previous expenditures related to a project to the capitalized amount, thus recognizing the reversal of expenditures from previous years on current year earnings, and recording the corresponding intangible asset in the balance sheet
3. Lev and Zarowin (1999) offer another alternative and suggest accounting for all previous costs of developing intangibles before technical feasibility is achieved.
4. While these alternatives are based on historical-cost measurement of intangibles, other alternatives suggest a fair value recognition approach. Upton (2001) argues that cost based capitalization of intangibles might not be suitable in certain situations.

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## Conclusion

- Although the significance of intellectual assets has gained its importance in the corporate world from a strategic sense, accounting for them in financial statements has not kept pace with it for several reasons. These include the conservative approach of the profession, and leaning towards reliability over relevance
  - In particular, the uncertainty about future economic benefits, the lack of full control, and the absence of markets to measure and value of intangibles reliably, has made accounting regulators reluctant to adopt more liberal measures
- Recently there have been signs of a growing willingness to provide some forward looking information not always financial in nature , within the set of financial statements incorporated within annual report.
- However the best solution may be the combination of two bellow approaches: a) the recognition of intangible assets including internally generated intangibles in the financial statements and b) in addition to financial statements , providing a complementary report.

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## Conclusion

- However, the accounting principles and rules developed over the last century to ensure that information reported is accurate and reliable struggle to include information on many intangibles.
- Finally while the approach to AIC envisaged here will have little use for some of the more technical, transaction-based accounting principles such as accruals/matching, prudence, or materiality, alternative principle may emerge to replace them.
- Accounting regulators are aware of the current reporting deficiencies for intangibles, but regulatory changes will take place slowly. It seems that in the near future the field of accounting for intangibles is going to evolve faster in the management domain, strengthening voluntary disclosure in financial statements and adopting less conservative criteria to record internally generated intangibles in the balance sheet.

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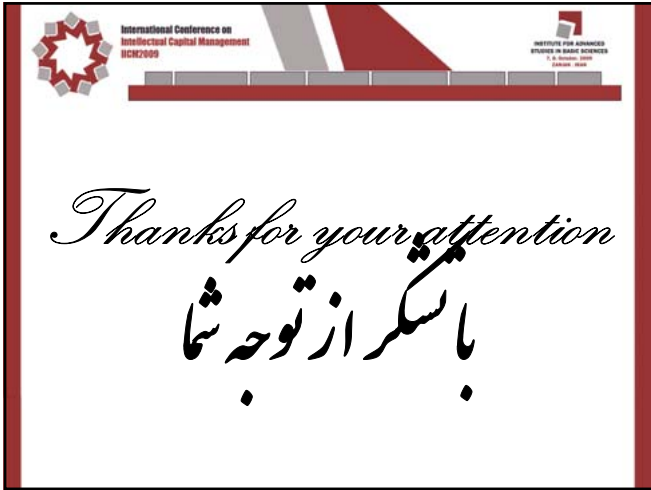
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