ACCOUNTING AND REPORTING OF INTANGIBLE ASSETS IN INDIA

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ABSTRACT

Accounting and reporting of Intangible assets is a complex and important subject in today’s information and knowledge-based economy. For companies, these assets are becoming basic drivers for achieving competitive success. They constitute a fundamental part of balance sheet of a company. Accounting and reporting of Intangible assets is also vital for their effective management as there is a famous saying „What gets measured gets managed” (Ayuso, 2003a). With a view to report these assets in the financial statements, various regulatory bodies have issued accounting standards on intangible assets.

KEYWORDS:

The advent of knowledge economy has changed the value creating mechanism of companies. Traditionally companies used to compete with each other on basis of the strength of their physical assets like raw material, plant & machinery etc. However, in the present business scenario corporates endeavour to create an edge over its competitors is reflected through their investment in intangible assets. Intangible assets vis intellectual capital, knowledge relationships, trademarks, brands, patents, know how, corporate cultures, R&D expenditures, worldwide networks, global customer base, satisfied customers, internet and e-commerce, organisation structures, skilled employees etc are becoming basic drivers for achieving competitive strength (Ayuso, 2003a; Tseng & Goo, 2005). Intangible assets have become fundamental resource for wealth creation and progress.

Intangible resources have moved from the periphery to the core of our modern economy (Marr 2007). They essentially represent the secrets of business enterprise, the key resources and factors that enable it to compete effectively in market place (Osterland, 2001). The strategic management of intangible assets plays a very decisive role in modern business initiatives. “The computation of the true value of a company requires a comprehensive assessment of both tangible and intangible assets” (Satyam Computers, Annual report 2007-08). Prof. Lev (2003) found that both cost cutting initiatives and large strategic investments like mergers and acquisitions require more transparency concerning the intangible assets of business enterprise. The significance of intangible assets in organisations can also be explained with the help of Resource based view (RBV) as suggested by Grant (1991) and VRIO (Valuable, Rare, Inimitable and Organisational support) Framework of Barney (1997) to identify the sources of competitive advantage. Resource based theory argues that a company is a combination of resources and capabilities. The resources and capabilities of a firm are the basis of a firm’s competitive advantage and are thus the central consideration in formulating strategy. The VRIO framework of competitive advantage has emerged from this perspective as a useful way of characterizing strategic assets. In this framework resources and capabilities should be Valuable (economically important, that is, they create value for the company), Rare (unique, i.e. only few companies have these resources), Inimitable (hard to copy, i.e. it can be costly to duplicate them and difficult to figure out what other companies are doing to have such strategic assets), and they have Organizational Support (strong management support and processes and systems to support the assets).

MEANING AND CATEGORIES OF INTANGIBLE ASSETS

Intangible assets of a company can be classified into four main categories-Human resources, External assets, Internal assets and Intellectual property assets. (Meritum, 2000; Guthrie et al, 2001; Vergauwen and Alem, 2005)

Human resources

Human resources represents the expertise, education, vocational qualifications, work-related knowledge, innovation, leadership, entrepreneurship and managerial skills in the employees of an organization which they bring and take home with them when they join or leave the firm.

Simply, human capital represents the individual

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knowledge stock of an organisation as represented by its employees (Bontis et al, 2002). It is the „thinking and doing” capital which captures the knowledge, professional skills and experience and creativity of employees (Li et al, 2008) It is the accumulated value of investments in employee training, competence and future (Ordonezde Pablos, 2003). This category also highlights the employee-based value drivers for a company. Cooperation and coordination among human resources of a company is the means by which exchange of knowledge and creation of new knowledge is made possible. It is the single most important and powerful factor that differentiates one organisation from another. It consists of specific individuals who cannot be owned by the company, nor can it be copied by any of its competitors. When a company invests in human capital, it increases its own value, gaining a sustainable long-run competitive advantage.

External assets

This intangible assets category represents relationship of a company with its customers, suppliers, business partners, industry associates, market channels, investors, society etc. External assets are the market related intangibles that enhance the fitness of an organization for succeeding in the marketplace. Examples are customer loyalty (reflected by the repeat business of the company) distribution channels, company names, business collaborations, favourable contracts and brand value.

Internal assets

Internal assets are systems, routines, technologies, databases, methodologies, processes and culture that are specific to an organization. It comprises the capabilities of a company, its infrastructure and organisational processes to manufacture products and render services to the market. It is the pool of knowledge that remains with the firm at the end of work, after employees have left (Stewart, 1997). Intangible assets of this category are idiosyncratic to a company and they constantly need to adapt to changing business scenarios. These assets give the organization a unique advantage over its competitors as these assets are not licensed to outsiders and are under company”s control.

Intellectual property assets

Intellectual property assets include know-how, copyrights, patents, products and tools that are owned by a corporation. These assets are valued based on their commercial potential. A corporation can derive its revenues from licensing these assets to outside users.

SIGNIFICANCE OF REPORTING INTANGIBLE ASSETS

The importance of intangible assets has augmented with the advent of information age and the virtual economy. Corporate financial reporting needs to evolve to include elements which create value for businesses such as customer satisfaction, brand valuation, business collaborations, corporate culture, etc. The disclosure of such intangible assets is presently restricted in the financial statements under the prevailing reporting practices. The Financial Accounting Standards Board (FASB) requires that "financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit and similar decisions."

ACCOUNTING OF INTANGIBLE ASSETS

Accounting of Intangible assets is a complex and important subject in today”s information and knowledge based economy. For companies, these assets are becoming basic drivers for achieving competitive success. They constitute a fundamental part of balance sheet of a company. Accounting of Intangible assets is also vital for their effective management as there is a famous saying „What gets measured gets managed” (Ayuso, 2003a). With a view to report these assets in the financial statements, various regulatory bodies have issued accounting standards on intangible assets.

International Financial Reporting Standard (IFRS)

Under IFRS, International Accounting Standard-38 (IAS-38) on intangible assets was issued by the International Accounting Standards Committee (IASC) in September, 1998. The objective of the standard was to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another standard. The standard requires an entity to recognise an intangible asset if, and only if, specified criteria are met. The Standard also specifies how to measure the carrying amount of intangible assets and requires specified disclosures about these assets. Accounting treatment for amortisation, impairment, retirements and disposals have also been explained. Further IASC has also issued International Accounting Standard 36-Impairment of
Assets which discusses the impairment provisions for goodwill and intangible assets with indefinite life.

OBJECTIVES OF THE STUDY

This study has been undertaken with the main objective of examining the accounting and reporting of intangible assets by the selected companies in India and the UK. Following are the specific objectives of this study:

- To analyse and compare International, Indian and other standards on intangible assets worldwide.
- To study the extent of disclosure of intangible assets by companies in India.
- To evaluate the impact of different corporate attributes on the extent of intangible assets disclosure by the companies in India.
- To compare the extent of intangible assets disclosures in Indian and UK based companies.

RESEARCH METHODOLOGY

The design of this research which has been formed in article is descriptive research design. The information is collected for this research based on secondary data. Therefore the relevant and needed information are collected from secondary recourses such as text books, national and international articles, journals and annual reports.

LIMITATIONS OF THE STUDY

The present study suffers from the following limitations.

1. The study focuses only on annual reports.
2. Content analysis technique has been used for gathering intangible assets information. Subjective judgement involved in identifying and classifying the nature of reported intangible assets information cannot be ruled out.

CONCLUSION

The transition of Indian economy from production to knowledge podium and the growing software & IT, financial services, business outsourcing, media, healthcare, pharmaceutical industries etc. have lead to increasing investments in intangible assets. In present competitive business world only commodities do not ensure the success of a firm. To gain success, a firm must have some competitive advantages (Ali et al, 2008). Intangible assets like skilled employees, knowledge relationships, R&D expenditures, worldwide networks, global customer base, satisfied clients, internet and e-commerce, trademarks, brands, markets, patents, corporate cultures etc create competitive advantages for a firm. Resource based value (RBV) theory and VRIO (Valuable, Rare, Inimitable and Organisational Support) framework also emphasise on the role of intangible resources in creating competitive advantages for a firm.

According to the Indian Accounting Standard (AS-28) an intangible assets is an “identifiable non-monetary asset without physical substance held for use in production or supply of goods and services for rental to others, or for administrative purposes.” These assets have been regarded as "Soft" assets and "Weightless Wealth" (Guthrie & Petty, 2000; Grojer and Johanson, 1999).

REFERENCES


