BUSINESSEUROPE

Andrew Lennard
Financial Reporting Council8th Floor
125 London Wall
London EC2Y 5A
United Kingdom

Email: intangibles@frc.org.uk

22 May 2019

Dear Mr Lennard,

Re: Discussion Paper on Intangible Assets

BusinessEurope welcomes the opportunity to comment on the FRC's Discussion Paper on Intangible Assets. We acknowledge that intangible assets are a significant driver of entities' values and that investors do have a vast interest in information about the potential effects of intangible values on the companies' profitability.

We agree with the FRC's DP that there are extensive uncertainties to be regarded when measuring intangible assets. This is why – in our view – the application of prudence does have merit when placing intangible values on the face of the balance sheet. Further we note and agree, that it not always possible to identify the portion of intangible values that have been consumed in a reporting period without the use if hindsight.

In consequence, we agree with the FRC not to pursue a change in the accounting requirements for intangible assets.

As for the proposals regarding potential extensions to the disclosure regime, we think that there is an interesting debate on what information may be useful and can be presented reliably. We want to raise again the concern that – also in the field of disclosure – management judgement would have to be applied to a great extent. Further, we think that a careful assessment is needed in the level of detail of any proposal as the information on intangible values is likely to be very sensitive in its content.

Please find our detailed answers to the questions laid out in the DP below. If you require any further information on our comments, please do not hesitate to contact us.

Yours sincerely,

Erik Berggren
Senior Adviser
Legal Affairs Department

APPENDIX

Question 1
Do you agree that it is important to improve the business reporting of intangibles?

We note that accounting for intangible assets, whether internally generated or purchased, is a very difficult area. We fully agree with the FRC's statement that "Intangible factors that are important to an entity in its creation of value, whether or not they are secured by legal means and whether or not they meet the current definition of 'assets'" (DP 1.7). We also acknowledge that it is often difficult to estimate the value of an intangible as in most cases there are many uncertainties about the benefits of an intangible asset. That is either because it is difficult to estimate returns that may be generated in the future or because the internal synergies and efficiency gains that can be reached are not determinable and depend on the implementation of an intangible asset. We therefor agree with the FRC's statement on the use of fair value measurement on intangible assets (see DP 8(ii)).

With the current guidance of IAS 38, we think the IFRS lay down a rather prudent accounting framework for intangibles that takes into account the uncertainties that are inseparable from many intangible assets.

We also note that IFRS reporting does not intend to provide for the fair value of the reporting entity and agree with respective notion in the DP. We think that the application of prudence fits well into the high levels of uncertainty that comes with intangible assets.

Question 2
Do you agree that an intangible should be recognised at cost under the two conditions set out above in (i)?

As a first remark, we do not understand the difference between the estimated costs when the project is undertaken (assuming this period of time starts and ends with the development phase) and the actual cost incurred within the development phase.

Further we question whether the approach presented in DP.8(i) would not be too broad since there are no criteria asking whether or not the internally generated intangible asset can be completed and can be used.
As for the economic benefits, it seems contradicting the first criterion refers to the "difficulty of establishing the future economic benefits" and the second one requires the specification of the economic benefits in order for an intangible asset to be recognized at cost.

In our view, the set of criteria presented in IAS 38.57 are well understood and applied in practice, although we acknowledge that there might be diversity in practice. We think it is appropriate to capitalize only those costs that are directly attributable to an intangible asset. Hence, by referring to the example of a customer list as laid out in DP 2.9, if there are no costs that are directly attributable to such an intangible asset, the intangible asset does not result in the recognition of an asset.

Question 3
Do you agree with the assumptions the paper makes regarding measurement uncertainty of intangibles?

With regard for the costs of an intangible asset, we think that most significant intangible assets stem from definable projects with more or less clear boundaries. For those, the costs of intangible assets can be determined rather easily. However, we agree that for "by-product" intangible assets it is difficult or impossible to define costs that are directly attributable.

We do also agree that the fair value of an intangible asset is – in many cases – very difficult to estimate. Fair value measurement requires judgement in the estimation of future return. We note however, that there are measurement models in place that deal with intangible assets, such as the "relief from royalties"-method. However, the uncertainties remain.

Uncertainties increase when it comes to the definition of the economic benefits of an intangible asset. Judgement is needed to estimate not only future returns but also cost savings and the realization of synergies.

Question 4
Do you agree that existing accounting standards should be revisited with the aim of improving the accounting for intangibles?

As noted in Question 1, we think that accounting for intangible assets is a difficult area. We do see a standard that is well established and understood. By taking into account that IFRS reporting is not meant to provide the fair value of the reporting entity itself, we do not think that the current standard needs a general review.

Question 5
Do you agree with the above proposals relating to expenditure on intangibles?

With regard to DP 3.1 we'd like to mention that expenses resulting from staff training or brand building are likely to be ongoing and recurring. As such, we do agree with the point made there conceptually but note that this problem might not exist to the extent implied in practice.

As for the proposals set out in DP 3.9 and following, we are confused about the definition of the 'future-oriented expenditures'. We assume that all expenses are incurred with the expectation to generate future benefits. Further, we think it might be very difficult, if not impossible to determine past and current expenditures that are written off in the current period because the benefits have been consumed. This would result in the use of judgement to a great extent (e.g. to define when the economic benefits of a past or present expenditure have been consumed) and may therefor diminish reliable disclosure. In addition, we think that – depending on the granularity of the information required – companies will be very careful as information about the intangible assets (whether recognized or not) is often very sensitive.

Question 6
Do you agree with the proposals aimed at improving the quality of information on recognised and unrecognised intangibles in narrative reporting?

First of all, we would like to note that many entities report on research and development already within their management commentary. Expenditure on R&D activities is sometimes even one of the most significant KPIs (see Daimler's Management Commentary). At least in Germany, comparative figures must be provided alongside any quantitative disclosure. Further, we refer to Question 5 and the use of management judgement that is inherent in the proposals made.

Question 7
What are your views about how the various participants involved in business reporting could or should contribute to the implementation of the proposals made in the paper?

In our view, all stakeholders should participate in forming these proposals. Investors should express a detailed view on how the proposed disclosures enhance their understanding of the company and issuers must make sure that potential disclosures remain relevant and reliable.

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