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Mr. Timothy S. Lucas
Director of Research
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116

Dear Mr. Lucas:

Re: Proposed Agenda Project on Disclosure of Information About Intangible Assets Not Recognized in Financial Statements

We are writing to support the FASB proposal for a new agenda project regarding intangible assets not currently recognized in financial statements. The growing significance of intangibles is apparent, not only in recent criticism of financial statements, but also in the increased attention they have received from management. Our experience in helping firms structure internal reporting and measurement systems for their intangible assets suggests that addressing these issues is both important and feasible.

1. *Is there a need for the FASB or others to comprehensively address the reporting of information about intangibles of a business enterprise?*

Businesses have always used intangibles in their operations, but the growing number of industries in which the primary resources of firms are intangible has created a well-identified demand for reconsideration of how firms measure and report their investments in these critical resources.¹ The need for standards in asset definition, expense classification, capitalization guidelines, financial measures and disclosure requirements for these items makes this topic an altogether appropriate focus for the FASB.

¹ The April 2001 Special Report, *Business and Financial Reporting, Challenges from the New Economy*, by Wayne S. Upton, Jr., clearly documents the demand for more information and recent criticism of the decreased relevance of financial statements.

2. *Is the proposed scope of such a project as described in this Proposal insufficient, appropriate, or too ambitious?*

The proposed FASB project would “address the format and content of disclosure of unrecognized intangible assets.”²

Although the format and content of disclosures could be significantly improved, the fundamental issue of recognition of these off-balance-sheet assets should be included in the Project scope. There is considerable evidence, cited in the New Economy Report, that users of financial statements are undertaking their own *ad hoc* recognition of research and development assets, as well as other intangibles. Acknowledging the importance of these assets, many companies are designing internal measurement and reporting systems to evaluate them. The FASB should establish guidelines for external recognition of these assets that improve the relevance and comparability of financial statements and that inform the design of the format and content of related disclosures.

3. *Should specific issues identified above be excluded from the scope of the proposed project on reporting information about intangibles?*

No.

4. *Should specific issues not identified above be addressed as part of the proposed project on reporting information about intangibles?*

Most of the debate surrounding intangibles has centered on (1) recognition, and (2) measurement, and these issues are related in that an inability to measure the asset will stand in the way of its recognition. It is possible, however, to narrow the scope of the discussion of measurement by adhering to the concept of cost as the most objective and accurate measure of investment. Concerns that it is difficult, if not impossible, to measure the “value” of intangibles reliably could be generalized to most assets, except for marketable securities, currently recognized on the balance sheet. Inventory is not generally measured at its selling price, just as land is not measured at its market value. The balance sheet does not report market values; it reports investment in a set of resources. We can see their value to the firm only when we look at the performance of the entire firm.

Some measurement issues remain, regarding which costs should be capitalized, but those issues go to the heart of the dilemma over recognition, a dilemma which the FASB could help to resolve. Without first dealing with fundamental issues of asset recognition, how can the appropriate disclosure format and content be determined?

² FASB, *Proposal for a New Agenda Project: Disclosure of Information About Intangible Assets Not Recognized in Financial Statements*, p. 3.

In conclusion, we feel that any progress in the area of reporting intangibles is a positive step. However, our experience in developing a complete intangible asset accounting system would indicate that formulating a comprehensive system for defining the assets, classifying expenses, and designing useful financial measures may not be as difficult as some think. Proper taxonomies, classification criteria, economic algorithms, and computer systems go a long way to simplify the issue and produce both relevant and reliable information with less "bolt-ons and exceptions" than a more *ad hoc* approach. It does require a fundamental understanding of how assets (both tangible and intangible) are used in organizations and how they work in combination to create value; once the right strategic paradigm is employed, the accounting is not as challenging as it would seem. The problems caused by the inability to handle intangible assets are pervasive and becoming more acute in each passing year. Our economy could really use the substantial boost in productivity that could be facilitated by better information, as managers are not apt to invest in what they cannot "see" and investors are not able to value properly what is not disclosed.

Sincerely,

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