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## UNITED STATES ENVIRONMENTAL PROTECTION AGENCY WASHINGTON, D.C. 20460

OFFICE OF ENFORCEMENT AND COMPLIANCE ASSURANCE

October 4, 2001

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

Dear Mr. Lucas:

I am writing on behalf of the Office of Planning, Policy Analysis, and Communications in the Environmental Protection Agency's Office of Enforcement and Compliance Assurance to express my office's strong support for the Financial Accounting Standards Board's (FASB) proposed project on the Disclosure of Information About Intangible Assets Not Recognized in Financial Statements. As the FASB proposal states, investors are increasingly interested in using information about assets which have not been generally recognized and disclosed in their decision making processes. These intangible assets, and the information they provide about issues such as a company's environmental policies and performance, are material to many actual and potential shareholders. The proposed project has significant potential to improve the availability and utility of this information, while also ensuring that companies currently generating intangible assets are not deterred from doing so because the market and disclosure systems do not explicitly attribute value to those types of assets.

The Environmental Protection Agency (EPA) is exploring ways in which market forces can take environmental matters into consideration and be utilized to positively influence environmental performance. FASB's proposal presents an opportunity to complement several of these efforts. In 1992, EPA initiated its Environmental Accounting Project in order to better evaluate and demonstrate the economic benefits of pollution prevention to those making business decisions. It has subsequently produced numerous guides for the regulated community with special emphasis on calculating the economic outcomes of pollution prevention activities, and allocating the costs of pollution within a business organization. Explicit guidance and support from the financial accounting community to encourage the disclosure of intangible assets, especially those related to environmental assets, will help to ensure that market values accurately reflect both the costs and benefits which accrue pursuant to responsible and forward-looking environmental management practices.

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More recently, EPA's Office of Enforcement and Compliance Assurance, in consultation with the Securities and Exchange Commission (SEC), has implemented a program to notify parties to some environmental enforcement actions of their potential duty to publicly disclose the legal proceeding by filing with the SEC pursuant to Regulation S-K, Item 103. EPA's assessment of disclosure among parties to EPA enforcement actions indicated that many companies are not satisfactorily meeting their obligation to make information regarding their environmental compliance available to the public.

EPA has also initiated several projects to make environmental information it collects available to the public. One example is the Sector Facility Indexing Project (SFIP), which brings together information from several EPA data systems to produce facility-level profiles for five industry sectors and a subset of major federal facilities. SFIP information relates to compliance and inspection history, chemical releases and spills, demographics of the surrounding population and production. EPA hopes that through a combination of these activities, market forces will be able to positively influence environmental performance. In order for market forces to operate optimally, however, they must be capable of accurately capturing all relevant information on tangible and intangible assets held by companies whose operations have environmental impact.

Despite the progress that has been made by EPA to facilitate the public dissemination of environmental performance information, FASB's project has the potential to significantly improve the public's ability to become informed of matters related to the full range of intangible environmental assets that currently are not uniformly disclosed. Most of the information which EPA collects relates to activities at individual facilities, not broader corporate environmental initiatives or programs. The companies themselves are in the best position to fully assess and disclose information on internally generated intangible assets that presents an accurate and holistic view of the company's assets, financial condition, and management policies and priorities.

Scope of the Project – FASB has proposed that the scope of this project be "intangible assets that are not recognized, but would have been recognized had they been acquired from others, as well as inprocess research and development assets written off after acquisition." My office encourages FASB to develop standards for the disclosure of intangible assets that will ensure consistent disclosure of those assets which reflect sound implementation of environmental policies and projects that result in improved environmental performance.

Information which should be disclosed about intangible assets – FASB suggests that possible quantitative and qualitative disclosures might include: major classes of intangible assets and their characteristics, expenditures to develop and maintain them, values of those assets, and significant events that change the anticipated future benefits arising from intangible assets. My office supports the inclusion of these factors, especially the last. A recent report by the World Resources Institute, Pure Profit: The Financial Implications of Environmental Performance, found that, contrary to the representations made in many disclosures by the pulp and paper sector, upcoming regulatory standards will not uniformly impact the sector financially due to differing geographical concerns and the varied ages and types of technology used at the facilities. It is important that the final FASB

guidance include an element which would specifically require parties to consider and disclose the impact of reasonably expected regulatory changes to the value of their intangible assets.

Voluntary or mandatory disclosure — One of the stated goals of FASB's proposed project is to facilitate comparisons of entities with respect to intangible assets. A voluntary disclosure requirement will enable those companies that have generated intangible assets to demonstrate to the public the benefits that these assets create for their company and the public, as compared to those that have not. However, a comparison of companies will be more difficult in the absence of an affirmative duty to disclose this information. The public may be discouraged from relying upon voluntarily disclosed information because of the difficulties involved in determining if a disclosure is false or misleading. The U.S. Supreme Court remarked in Basic v. Levinson¹ that a company's silence on an issue cannot support a claim that its disclosure was misleading under Rule 10(b)-5 in the absence of an affirmative duty to disclose the information. In determining if the disclosure of intangible assets should be voluntary or mandatory, my office asks FASB to consider these issues to ensure that companies are not put at a competitive disadvantage by voluntarily disclosing information. If FASB's final standard cannot assure the public of the completeness of disclosure statements, a comparison of companies on this basis will be hindered.

Frequency of disclosure – In order for information on intangible assets to be of value to investors and shareholders, it must be provided in a timely manner. The public should be able to simultaneously consider information on intangible assets in conjunction with other relevant information, such as the information included in 10-Q fillings. Required quarterly disclosure of intangible asset information will ensure that all relevant information can be considered together, and enable market forces to influence the generation and maintenance of intangible assets. Because some companies may not currently have the expertise or processes in place to immediately accommodate quarterly disclosure, my office suggests that quarterly disclosure could be gradually phased in, if necessary.

Accounting standards which generally recognize intangible assets when they are acquired from others but not if they are developed internally serve as a disincentive to firms to implement programs and policies that produce these assets. This subsequently creates a disincentive for firms to have a strong environmental policy, to pursue pollution prevention, to vigilantly prevent noncompliance, and consistently improve environmental performance. My office commends FASB for considering this proposed project, and for taking steps to ensure that financial accounting practices address the information needs which investors and new market forces are increasingly demanding.

Sincerely,

Shirin Venus Attorney Advisor Office of Planning, Policy Analysis & Communications

<sup>&</sup>lt;sup>1</sup>Basic Inc. v. Levinson, 485 U.S. 224, 239 n.17 (1988).