October 17, 2016

VIA EMAIL

Ms. Susan Cosper
Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-05116

Re: FASB Invitation to Comment – Agenda Consultation
File Reference 2016-290

Dear Ms. Cosper:

We appreciate the opportunity to respond to the Invitation to Comment (ITC) regarding potential financial accounting and reporting topics that the FASB should consider adding to its agenda. As indicated in our previous letters to the FAF and IASB\(^1\), we believe that accounting for intangible assets, including research and development, is an important financial reporting issue that the FASB should add to its agenda and intangible assets accounting should be given the highest priority for improving the existing accounting model.

**Accounting for internally developed intangible assets should be added to the agenda**

Intellectual Ventures is a global leader in the business of invention. Our managed funds have collectively invested hundreds of millions of dollars on the creation and development of new, internally developed invention rights leading to the filing and granting of thousands of patents and patent applications. We meet frequently with our investors to communicate our financial condition and results of operations as presented in our financial statements. However, when we do so, it is clear that current U.S. accounting standards do not adequately reflect the value or, in some cases, the extent of our invention portfolio to our investors.

Today, US GAAP recognizes and reports intangibles when they are purchased, including in-process research and development. In contrast, when we develop our own technologies and patents, these costs are *not* recognized as assets on our balance sheet. In both cases, however, the costs expended meet the definition of an asset: probable future economic benefits obtained or

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\(^1\) See our letter to the IASB dated November 30, 2011 and our letter to the Financial Accounting Foundation dated May 30, 2013
controlled by an entity as a result of past transactions or events. Accordingly, we agree with the conclusion of the Australian Accounting Standards Board (AASB) that the manner by which an intangible asset is derived is irrelevant to the determination of whether or not it can be recognized as an asset;\(^2\) and we see this as a major flaw in the existing U.S. accounting literature that needs to be rectified.

The practical consequence of the appropriate application of current US GAAP is that users have no way to compare the value of intellectual property (IP) within and across companies. Intangible assets are measured on a completely different basis depending on whether they were developed or acquired. There is an extensive body of literature that demonstrates the relevance of intangibles for equity valuation. Thus, investor analysis is severely hindered by the lack of publicly available information regarding the value, and often the existence, of a company’s internally developed intangible assets. Financial statements are, at best, inadequate and, at worst, misleading, because they are missing vital information about intangible assets. This deficiency can be a major contributor to the significant difference between the book value and fair value of the equity of many entities.

As our economy increasingly converts to an information economy, this problem will continue to grow over time. Intangible assets are an increasingly significant class of assets for a wide range of entities across many jurisdictions. For example, one economic study found that total business investment in intangibles was approximately one trillion dollars in 1999, an amount that is roughly the same as investment in tangible capital at that time.\(^3\) Focusing solely on the growth of IP—which is a key driver in the fast-growing high-tech industry—a report by the Organization for Economic Cooperation and Development shows that the number of patent applications filed in Europe, Japan, and the United States grew by more than 40% between 1992 and 2002. This trend continues, reflecting the rapid pace and acceleration of investment in IP on a worldwide basis. Thus, today’s accounting clearly gives rise to problems that are frequent and material and will persist if not resolved. In short, we can see the value of IP everywhere today except in financial statements.

We believe that this inconsistency in accounting for purchased versus internally generated intangibles clearly meets the FASB’s agenda criteria of being both a pressing as well as pervasive problem in light of the increasing importance of intangible assets to the world economy. In the absence of an improvement in this area, investors will find it increasingly difficult to make optimal decisions regarding the allocation of capital.

Moreover, we believe that most of the conceptual and intellectual analysis of this issue has already been performed, such that the issue is technically feasible. Furthermore, resolution of the issue

\(^2\) See the AASB’s 2008 Discussion Paper, *Initial Accounting for Internally Generated Intangible Assets*.

does not depend on the completion of other FASB projects; it is entirely feasible to develop and implement a viable solution without awaiting completion of other projects.

Accordingly, we believe that the issue meets all of the FASB’s criteria for addition to its technical agenda.

Discussion of possible alternatives

As an overall matter, we believe that it is somewhat premature to determine which alternative to pursue, in advance of the FASB deciding to add the project to its agenda. We believe that the merits of the various alternatives can be more fully deliberated once the project is added to the agenda. In short, we believe there is a real need to improve the accounting in this area, and any of the alternatives set forth in the ITC would be an improvement to US GAAP.

However, of the various alternatives outlined in the ITC, we believe that Alternative B, Recognize Research and Development Costs, is the best approach to pursue at this time. While a project that addresses the accounting for all internally generated intangible assets might be theoretically superior, it could be difficult to reach a broad consensus on a change in accounting for many different types of intangible assets. Accordingly, we believe that a narrower scope project that focuses on capitalizing development costs would be more feasible, and would also ensure that changes could be made to the accounting by the FASB in a reasonable time frame, as opposed to a full-scope project that tackled all intangible assets.

We believe that research and development costs is a good starting point for the FASB because the costs of developing intangible assets constitute one of the most important assets not currently recognized on the balance sheet. (We do not support capitalizing research costs, as we do not believe they meet the definition of an asset.) If successful, the project could then be the basis for a second-phase, longer-term project that addressed the recognition of all (or most) other intangible assets.

We do not, however, support limiting the project solely to software intangible assets, as some stakeholders have suggested. We believe that this would be too narrow a scope for the project, as it would focus too much of the FASB’s time and effort on an area of accounting for which practice is largely settled, without exploring the issues that would arise in applying a capitalization model to other classes of intangible assets, such as patents or other types of IP.

Regarding the FASB’s choice of an appropriate measurement basis for internally developed intangible assets, we believe that the cost approach might be more feasible than a fair value approach. The fair value of new and emerging technologies can often be difficult to estimate. Tracking cost information, on the other hand, is feasible, cost-effective, and reliable; in fact, many companies routinely track research and development costs for tax credit and other management purposes. This approach is also consistent with the accounting for internally developed software, which has proved to be workable in practice. Moreover, we believe that cost information has relevance to investors. Specifically, the capitalization of certain intangible assets will provide our investors with greater visibility into amounts spent creating our patent portfolio and a basis on
which they may value their investment, which serves as the basis for substantially all of our monetization efforts. The use of a cost-based approach would provide transparency regarding an entity’s investment in intangible assets while avoiding the additional expense of having to rely on external valuation specialists to produce the information. Consideration could be given to whether and how the asset would be periodically tested for impairment, for instance by using a valuation methodology based on current or replacement cost, to alleviate any concerns regarding potential over-capitalization of costs.

If, on the other hand, the FASB instead decides to pursue Alternative D, Adopt IAS 38, we recommend that FASB take a fresh look at the recognition criteria of that standard. Based on the feedback reported in the ITC, it appears that under IAS 38, the threshold for recognition of development costs is so high that only minimal amounts are capitalized, and are done so relatively late in the development process. Accordingly, we believe that a reconsideration of the recognition criteria of IAS 38 is warranted if the FASB’s project is meant to result in meaningful improvement to the existing accounting model. Although convergence with IFRS is a laudable goal, it should not be pursued at the cost of adopting accounting standards in the US that will not result in a significant step forward.

While we believe that Alternative B may be the most feasible at this time, we agree wholeheartedly with the conclusion of the AASB that acquiring an intangible asset by purchase in a business combination does not necessarily make it more valuable to an entity than one that has been internally generated. Therefore, we believe a project that would recognize the internal development of intangible assets using either a cost-based approach or a fair value-based approach would be a significant improvement to the current accounting model.

If a recognition approach is deemed not possible, we would support a disclosure-based approach (Alternative C). While it is not our first recommendation, we believe it is better than not addressing the issue at all. Expanded disclosures about internally generated intangible items would provide users with additional information to assist in analyzing similar companies in industries in which intangible items are significant to future prospects.

Conclusion
Our view is that addressing the inconsistencies in accounting for intangible assets will improve information quality, transparency and usefulness of financial statements to investors. Accordingly, we believe that a project that addresses the accounting for the internal development of intangible assets should be added to the agenda and should be a high priority for the FASB at this time.

We believe that investors would be strong advocates of this approach. Investors who consider investing in industries in which the primary source of economic value is the creation and management of intangible assets have a real need for more, and more comparable, information regarding the value of development costs. Accordingly, we believe that undertaking a project to remedy this deficiency would advance the FASB’s mission to serve investors in their economic and resource-allocation decisions.
We hope you find our comments constructive, and we would be happy to participate in a Roundtable Meeting or otherwise meet with the FASB on this issue. Please do not hesitate to contact us should you have any questions.

Best regards,

[Signature]

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