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In a New Brand World

- Why is an asset not an asset?

Master Thesis

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Abstract

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Subject: In a New Brand World – *Why is an asset not an asset?*

Key words: IAS 38, brand accounting, brand assets, internally generated brands, brand valuation

Background and problem: The treatment of internally generated brands has for long been under discussion. The different opinions represented by accountants and marketers show the gap between those who believe that internally generated brands should be recognized on the balance sheet and those who believe they should not.

Purpose: The purpose of the study is to gain further insight within the field of brand assets and draw conclusions that might provide guidance in further development of the legal and norm setting environment. Further, the purpose is to point out aspects on international brand recognition to be able to recognize internally generated brands. The thesis will provide answers to the question why an asset, often a company's most important asset, is not an asset.

Delimitations: This thesis takes on the international discussion on brands as assets and brand recognition. Therefore, the research is not limited geographically and there is no intention to scrutinize any legislation on any local or national level. This limits the discussion to concern and approach to the international norm-setting and legal environment. The research focuses on the perceptions on internally generated brands as assets and on global brand valuation method.

Methodology: This research is conducted in a qualitative way, using both an exploratory and a descriptive approach. The gathered material consists mainly of interviews, with further input from articles, journals and publications. Interview persons were chosen mainly for their participation in relevant business articles on the subject.

Results and conclusions: The research shows that the general opinion is that internally generated brands should be recognized, as well as acquired brands, but that there are difficulties related to this process. There must be possibility to measure such assets with reasonable certainty. Many argue that there should be a shift towards a harmonization regarding international brand valuation. This is argued to ease the comparability of internally generated brands.

Suggestions for further research: It would be interesting to bring forward further research on what it would mean to companies to include internally generated brands on their balance sheet. This could be done by looking deeper into the comment letters on IAS 38, as these letters vary in critique and come from different countries.

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1 Introduction

The first chapter of this study starts by presenting an introduction and a background to the subject. Further, the problem discussion is provided, leading to the problem statement and the purpose on which this thesis is founded. Moreover, a general outline of the thesis is provided.

“The range of what we think and do is limited by what we fail to notice”

- R. D. Laing

1.1 Background

In 2000, the European Commission announced its intention to require International Accounting Standards (IAS) for use in all companies listed on the stock exchanges existing within the European Union (EU) from January 2005 onwards at the latest. This regulation was formally approved in 2003 and consists of not only full members of the EU but also members of the European Economic Area. The IAS had at this time already been adopted by several large internationally listed companies in countries such as Germany and Switzerland and also by countries in the Eastern Europe region (Whittington, 2005).

The adoption to IAS by the EU was one further step in the process of developing international standards in the world of accounting. As a result, IAS is now fully accepted for overseas registrants by most of the world's stock exchanges. The only notable exception is that of the USA where the Securities and Exchange Commission allows overseas registrants to present international standard accounts but requires that the results are reconciled to US generally accepted accounting principles (Whittington, 2005).

The IAS is divided into several different sections (IAS 1-41) covering all the different aspects on international accounting. The International Accounting Standard 38 (IAS 38) holds information about how intangible assets such as goodwill, licenses, patents and brands should be dealt with (Epstein & Mirza, 2005). Intangible assets on the balance sheets have caused several questions in different countries whether such assets really are assets. For example, in Germany, the basic assumptions have been that tangible assets such as property, plants and equipment are the key value drivers and performance generators of a company (von Colbe et al, 2005). Thus, the intangibles have not been considered to the same extent. On the other hand, in the UK, the accounting profession has advocated not to oppose the recognition of intangibles on the balance sheet, provided that certain criteria are fulfilled and a reliable measurement method can be utilized (Tollington, 1998).

Historically, taking on different perspectives, there has been great difference in the opinions of accountants and marketers concerning brand valuation (Oldroyd, 1994). Marketers have seen brands as a critical asset for the future value of the company, whereas accountants have believed that brand investment was merely a cost to be kept as low as possible (Oldroyd, 1994). Further, there is little guidance and less understanding over accounting treatment of brand valuation. The debate over valuating brands and including them on the balance sheet has become a great controversy (Seetharaman et al, 2001).

In Tollington (2002), the Brand Finance CEO David Haigh explains how the accounting profession is driven by the need to produce reliable information, using transaction-based values, which tends to restrict the independent valuations arising outside this context, as with most brand valuations. In support of business reality, there is need for more relevant information than need for reliable information. Hence, the profession should embrace the use of independent valuations at the initial recognition stage of an asset. Valuations are subjective but the lack of valuations on the balance sheet is making nonsense of it. This argument points out the widening gap between accounting book values and market values (Tollington, 2002).

In the middle of the 1980s, Interbrand company, a consultancy agency, conducted the first ever brand valuation service for Rank Howis McDougall (RHM) company. Interbrand succeeded in presenting the worth of a company's brand as an asset on the balance sheet. Brand valuation was brought to the light in the wave of brand acquisitions at this time. The amount being paid by many companies for these acquisitions, especially for the strongly branded name, was increasingly higher than the value of the company's net tangible assets. This resulted in goodwill on acquisitions. This goodwill, however, contained a mix of intangible assets, such as brands, copyrights, patents, knowledge and customer loyalty (Seetharaman et al, 2001).

Economic benefits associated with brands are relevant to both marketing and accounting. Brands, however, are ambiguous entities in both marketing and accounting literature, and the future economic benefits which they bring to businesses are not as clear as one might suppose. It has been stated that the long-term success of a brand lies in the number of consumers who become repeat purchasers. This is partly attributed to brand loyalty, and encourages the view that brands exist as assets for the continuing benefit of a business (Oldroyd, 1994). The valuation of a brand puts pressure on the systems and tools used to provide such analysis. Today, there are several different ways of valuing a brand, from different points of views, with different methods. This creates a situation which is not only confusing but also unfair to the extent that some brands can be recognized on the balance sheet and some can not.

There is a difference between acquired brands and internally generated brands (Epstein & Mirza, 2005). Although there is no business discrepancy between different types of brands, the IAS 38 and IFRS 3 state that acquired brands can be recognized as assets and that internally generated brands must not be recognized on the balance sheet. As internally generated brands can not be recognized whereas acquired brands can, the question arises; is the lack of internally generated brands on the balance sheets misleading when it comes to valuating a brand asset and, in the end, a company?

So, why is this important? The primary capital of many businesses is their brands (Motameni & Shahrokhi, 1998). A company's most important asset is therefore in many cases not recognized as an asset. As the world changes, the importance of intangible assets is increasing (Günther & Kriegbaum-Kling, 2001). With this shift towards more intangible assets and intellectual capital, this view upon brand asset recognition is not sustainable and must bring different perspectives together. Recognizing brands on the balance sheet as an intangible asset is a relatively recent development in financial reporting and as a result, accounting for intangible assets is one of the least developed areas of accounting theory and regulation (Powell, 2003).

1.2 Problem discussion

Market capitalizations of listed companies often exceed the value of shareholder equity. This discrepancy could be viewed upon as intangible values of a company (Fincham & Roslender, 2003). The treatment over intangible assets has for long been under discussion (von Colbe et al, 2005). The fact that some intangibles, such as internally generated brands, are not reflected in balance sheets represents a big gap between a conservative view of accounting vis-à-vis the “market value” view of brand valuation companies and analysts (Tollington, 2002).

The fact that a brand asset in some perspectives is not an asset and in other perspectives is an asset brings different questions. IAS 38 stipulates that companies must not recognize internally generated brands on the balance sheet (Epstein & Mirza, 2005). However, this deviates from the accounting principle of true and fair value. As the world is changing towards more intangible-intensive companies, with financial statements no longer reflecting true economic values of the companies, leaving out intangibles such as brands, this discrepancy must be handled with (Tollington, 2001). Further, a great challenge facing the accounting profession is to understand the large difference between its balance and market valuation, which is also supported by Seetharaman et al (2002). Lev (2001) states that intangible assets are fast replacing tangible assets, but that the accounting measurement and treatment has stagnated for intangible assets. Accounting does not only fail to capture some intangible assets, but also do not treat assets as assets.

Seetharaman et al (2002) state that the future demands accounting for knowledge and intangibles. It is becoming more and more of a new knowledge economy. The old economy, where production and industrialization dominate, is much more made up of physical, tangible asset. Moreover, Ballou et al (2004) express how intangible assets are said to be drivers of value but ignored by accounting. The current accounting system gives intangibles an incomplete treatment, counting some and ignoring others. This brings a risk of mismanaging many of their company’s most important assets, such as a brand.

The perspectives on these matters are numerous (Artsberg, 2003). Accounting professionals differ in their opinions, marketers hold their view upon the brand as the company’s biggest asset, and some brand finance perspectives gives expression to the importance of brand recognition (Haigh & Rocha, 2004). A marketer must find it strange to separate between brands and brands. However, the accounting profession advocates not recognizing an internally generated brand (Epstein & Mirza, 2005). Although, the profession is more inclined towards the recognition of the same asset, but with the slight difference that it is acquired.

Moreover, the perspectives differ, but it is not solely between the different marketing and accounting bodies, but the opinions differ even within accounting (Artsberg, 2003). Accounting professionals are mainly not willing to recognize these brand assets on the balance sheet, but exceptions has happened, thus some accountants stand in favour of recognizing these assets. There are also perspectives from marketers and brand finance professionals, expressing for long the need for recognizing brands and the importance of monitoring the health of the brand (Ratnatunga & Ewing, 2005). Their view of this brand asset is often seen as the major asset for a company.

Acquiring a brand requires market valuation of some sort, thus the acquisitions will show up on the balance sheet in line with IFRS 3 (Epstein & Mirza, 2005). However, as internally

generated brands are not allowed to be recognized on the balance sheet, such brands still carry the same market value as externally generated brands and this brings a discrepancy of reality as these assets are not considered assets. The perception of brands as intangible assets and as investments needs to take both an accounting and a marketing perspective on brand recognition to be able to describe the reality. It is time to bring the different perspectives together. Regarding internally generated brands, there is a gap between the prudence principle and the accounting demand for true and fair value. Since such brands can not be recognized, the value of the brand asset is not reflecting the reality. The brand asset is not an asset.

1.3 Problem statement

Tollington and Liu (1998) argue that internally generated brand should be recognized as assets. There is no doubt that brand assets exist. However, the evidence required by the accounting profession for the recognition of internally generated brand assets appears to be insufficient for their inclusion on the balance sheet (Tollington, 1998). With research from Tollington (1998) in mind, in combination with the above problem discussion brings forward the following problem statement:

Why is an asset not an asset?

In order to answer this question, the main problem statement has been broken down into two sub-questions. These questions are formulated sequentially:

- Should internally generated brands be recognized on the balance sheet?
- Should there be a harmonization towards one global brand valuation method?

1.4 Purpose

The purpose of the study is to gain further insight within the field of brand assets and draw conclusions that might provide guidance in further development of the legal and norm setting environment. Further, the purpose is to point out aspects on international brand recognition to be able to recognize internally generated brands. The thesis strives to bring further benefits and added value to the discussion on how internally generated brands should be treated on the balance sheet and if there should be a harmonization towards one global method for brand valuation. Moreover, it will provide answers to the question why an asset, often a company's most important asset, is not an asset.

1.5 Scope and delimitations

This thesis takes on the international discussion on brands as assets and brand recognition. Therefore, the research is not limited geographically and there is no intention to scrutinize any legislation on any local or national level. This limits the discussion to concern and approach to the international norm-setting and legal environment. Different perspectives are discussed in the research focusing on the perceptions on internally generated brands on the balance sheets. There are no attempts to try to evaluate brand valuation methods but the intention is to see whether a global brand valuation method should be recognized.

1.6 General outline

This thesis consists of seven chapters. In order to make the research as easy as possible to follow, the chapters one to seven is outlined sequentially:

1 Introduction and background

The first chapter of this study starts by presenting an introduction and a background to the subject. Further, the problem discussion is provided, leading to the problem statement and the purpose on which this thesis is founded. Moreover, a general outline of the thesis is provided.

2 Methodology

In this chapter, the research approach and the method used is provided to gain further insight in how this study was conducted. The focus lies on how the research was made and not on methodology theories. Further, the validity and reliability of the research is presented.

3 Theoretical framework

The theoretical framework consists of theories from different sources and perspectives to fully support the empirical research. The chapter is presented in five parts; brand accounting, the accounting treatment of intangible assets, a discussion on intangibles and IAS 38, the brand asset and brand valuation perspectives.

4 Empirical data

In this chapter the empirical findings from the research is presented. The material is linked to the theory and the interview questions provided earlier. The empirical data is presented consequently along the interview question areas to make it easier to follow the discussion. The empirical material in this thesis is fully based on interviews. The material as presented as it was said, without any further analysis in this chapter.

5 Analysis

In this chapter the empirical data is analyzed with inputs from the theoretical framework to investigate whether the data correlate. The empirical data is analyzed in a qualitative way by comparing the respondents' opinions with previous research within the area of brands in accounting.

6 Conclusions

In this chapter the conclusions from the empirical and theoretical analysis are drawn. In this part, the thesis is linked back to the purpose and the research questions presented in the problem statement are answered. Further, some own reflections on the subject are provided.

7 Further research

In the last chapter, the suggestions for further research within the subject are provided. There are many interesting areas that can be investigated taking on a different perspective and making other choices than presented in this thesis.

2 Methodology

In this chapter, the research approach and the method used is provided to gain further insight in how this study was conducted. The focus lies on how the research was made and not on methodology theories. Further, the validity and reliability of the research is presented.

2.1 Research approach

Method depends on methodology, and inadequacy of either will lead to deficient research (Ryan, Scapens & Theobald, 2002). To make the research adequate, the instructions provided in the methodology literature have been followed and the theories have been applied on this specific research.

The thesis will primarily take on an explorative approach since it hopefully will bring new knowledge concerning the different perspectives and point of views of the accountants and marketers within this subject. In line with the conception of Halvorsen (1992), an explorative approach is useful when the intentions are to get a broad insight and a comprehensive overview of the research subject.

A descriptive approach is also necessary as there is a need for explaining the theories and framework for brands, valuation, legalities and more. In order to comprehend the results and findings in its context, there is a need for descriptive outlook on existing knowledge and research. This approach is applicable when the researchers want to describe a certain state or actual fact (Halvorsen, 1992).

The thesis is conducted, interpreted and analyzed in a qualitative way. It relies almost entirely on qualitative information collected through interviews together with input from articles, journals and literature. This approach is chosen for its advantages for this type of research along with the theories of Lekvall and Wahlbin (2001). The distinction between a qualitative approach and a quantitative approach is basically about how the data is presented and how it is being analyzed. The qualitative method is more suitable when the researcher aims at creating a deeper understanding of a subject that can not be measured with quantitative method. As a critique to this method, Lekvall and Wahlbin (2001) discuss the problem with scientific inaccuracy, generated by uncertain or arbitrary answers found in some qualitative research. However, this can be avoided by distinguishing the reliability and the validity of the research. The reliability of a qualitative research is in many cases limited. On the contrary, the validity is often much higher than if a quantitative method is used.

2.2 Research design

To generate an effective empirical research, the researcher must know how and where to locate data that already exist, generate data that do not already exist and to determine the reliability and applicability of the data to the research problem (Ethridge, 2004).

This thesis is a cross-over research with inputs from both accounting and marketing practices. The subject was chosen after brain storming within these areas and is result of personal influences and interests. Among the criteria for the subject were that is up-to-date and interesting from an international perspective.

Initially, to get better knowledge of the chosen subject, an introductory search for articles, journals and business report in several different international data bases accessed through the Economic Library, was conducted. The information there is provided through several databases accessed through the library; GUNDA, Business Source Premier and Emerald Insight. The key words used in the initial exploratory research were, individually or in combination;

Accounting, Accounting treatment intangibles, Brand accounting, Brand asset, Brand equity, Brand valuation, IAS 38, IFRS 3, Intangible assets, Marketing

This research resulted in a large number of articles, journals and business reports that held valuable information for the future work. By reading these articles, a foundation of basic knowledge was created and gave the opportunity to outline the main research problem, the research questions and the purpose with this study. This initial step also set out the guidelines for how the future research were to be conducted to the best meet the purpose and answer the research questions.

2.3 Data collection

In order to conduct a study there are two main groups of data that can be collected; primary and secondary. The information that is labelled primary data is collected and treated uniquely for this specific study. A common mode of procedure when obtaining primary data is through survey questionnaires compiled by the researchers (Ethridge, 2004). The advantage with this method is that the researcher can develop and form data accordingly with the specific study, thus not only relying on secondary data, often created for another purpose (Lekvall & Wahlbin, 2001).

This thesis' primary data consists of a number of interviews conducted with persons who were believed to hold relevant information and knowledge within the boundaries of the chosen subject. This is advantageous for qualitative research (Lekvall & Wahlbin, 2001). Appointments for personal interviews with some of the recipients were made and telephone interviews and mail interviews with other respondents were conducted. The primary data was collected only for this particular research purpose and used for the first time in this study. The information collected from the interviews was in the form of in-depth interviews using an interview guide with open-ended questions.

In order to get full benefit of the primary data, several sources of secondary data has been brought in, gathered from various available database sources combined with sources suggested by the thesis tutor. The necessity of a wide collection of literature and information arises when conducting research of this sort (Halvorsen, 1992). In this thesis, the secondary data consists of relevant articles, journals, reports, economic and business literature and Internet sources collected through data bases, in renowned business reviews and journals through the library and on the Internet. The information is provided through several databases described earlier. In order to treat the secondary data in an accurate way, the study have to rely on relevant and explanatory theories (Halvorsen, 1992). Therefore, the secondary data constitutes the base of the theoretical framework of this study.

2.4 Interviews

To make a successful research interview there are several different techniques that can be used. According to Lekvall and Wahlbin (2001) there are several different interview methods that can be used to conduct a research. Which method to use in a research study is due to the specific circumstances following the research problem. The methods differ widely and the most adequate method to be used in each case must be determined by the researcher. The methods most suitable for this specific research are personal interviews, telephone interviews and email interviews. Lekvall and Wahlbin (2001) define these different interview techniques sequentially:

Personal interviews: The questions are asked by a researcher and answered by the respondent at a personal meeting. The greatest advantage with this method is that it is easier to ask follow-up questions and to easier interpret the answers than with any other method. Among the disadvantages are that the method is costly and time inefficient. Personal interviews were the number one choice with the respondents and were conducted with persons located in Gothenburg at the time for the research.

Telephone interviews: The questions are asked by a researcher and the questions are answered orally by a respondent during a telephone call. The telephone interview holds many of the advantages found in personal interviews and is also cheaper and often more time efficient. However, the lack of personal interaction increases the risk for misinterpretation and lack of interest. Telephone interviews were made with persons who were located far from Gothenburg or did not have time to meet us personally, to keep the thesis within the boundaries of cost and time. These interviews were conducted from home using conference call equipment.

Email interviews can be view upon as a certain type of written interviews as there is no researcher as a direct link to the respondent. It is an easy and cheap way to get in contact with respondents all around the world. A disadvantage may be that the respondent is not focused on the questions. Email interviews were used to get information from persons who were very busy and did not want to book an appointment for a telephone interview but had time to answer some questions when they felt they had time. This way the answers could be collected even if the respondents were busy.

2.4.1 Sample and access

The interview persons were chosen for their expected knowledge and contribution to the study. These persons were found by recommendation from the tutor and by their participation in relevant business articles and lectures. For the research to be relevant and to increase the validity, respondents who were believed to represent different perspectives on the subject were chosen. As a result, both persons from marketing and accounting perspective were asked to state their views on internally generated brands. In line with the research purpose there is an aim to investigate different professional perspectives on the subject. Further, there is also a distinction between the theoretical perspective and the practical perspective, the former represented by Professors and a renowned researcher and the latter by a professional working in the industry.

An undisclosed member of the International Accounting Standards Board¹, was contacted via mail at an early stage. The person's position in the IASB and accounting expertise was

¹ Any opinions expressed in this thesis by this person are personal, rather than official views of the Board

believed to bring significant validity to the thesis. Anthony Tollington, Doctorate in Goodwill and Intangibles and writer of several articles on the subject, was chosen for his proven expertise and knowledge concerning intangible assets and brands. Mr Tollington, based in London, was interviewed via mail as this was the only way to get in contact with him. Further, Jan-Erik Gröjer, Professor of Accounting and Finance at Uppsala University, was contacted to get more information as these issues are within his area of expertise and previous research. In this case, a telephone interview was the most suitable method. To get a marketing perspective on brands as assets, Professor of Marketing at the University of Exeter, Jonathan, E. Schroder was interviewed. Professor Schroeder is Guest Professor during April 2006 at the School of Business, Economics and Law, Gothenburg University, and therefore a personal interview was conducted in the premises of the school. Moreover, Chartered Accountant at KPMG Company and Board member of Swedish body IREV, Kajsa Drefeldt, was interviewed to investigate the practical aspect on brand accounting. This personal interview was conducted at the KPMG Head Office in Gothenburg, Sweden. A complete presentation of the interview persons are provided in the reference list.

Lekvall and Wahlbin (2001) address the access problem. This has to do with the problems related to establish contact with the recipients. One of the thought-of respondents at an Accounting firm in Gothenburg was afraid to state anything that would be opposite or even threatening to the general company policy. As a result, it was impossible to make an interview with this person. Further, several internationally renowned writers of relevant articles on this subject was contacted via mail. However, the access to these persons is limited. As a result, some replies were not received within the time limit of this thesis, some did not reply at all. However, the sample of five interview respondents is believed to be enough in this case because of the positions of the interview persons and the quality of their answers.

2.4.2 Interview procedure

When the respondents were chosen, an interview questionnaire was compiled. Open-ended and wide questions were used in the beginning of the interviews to ease the conversation and to make the respondents comfortable and more willing to answer the questions. The questions were asked in a certain predicted order but the opportunity was given to the respondents to mix the questions and add or exclude any information during the interviews, no matter the interview technique. The questionnaire was sent to the respondents in advance to introduce the subject and to prepare them in order to receive adequate and better thought out answers. This because some of the questions were rather complicated and needed preparation.

To make the interviews accessible to analysis, Kvale (1996) argues that the oral interviews must be taped and the tapes must be transcribed into written text. At the interview occasions, the answers were written down as well as recorded in order to secure the information and be able to listen to the information several times to make sure that everything was clear and to avoid mistakes or any case of misinterpretation, along with the theories of Kvale (1996). The respondents were kindly asked if a recording device could be used and this was approved by all respondents. By using this kind of equipment, the researchers can concentrate on the topic and the dynamics of the interview. After the interviews, the material was transcribed into text. Transcribing involves translating from an oral language to a written language with another set of language rules. Kvale (1996) points out the importance of not looking at the transcriptions as copies of the reality, but as interpretative constructions of the reality which serve different purposes. Along with the transcriptions, there might be issues regarding the reliability and the validity of the research. To further raise the reliability and validity of this research, both authors have listened to the tapes and the answers have been discussed to make the most

useful transcription to the study. As Kvale (1996) states; the correct transcription can not be made since there is no true, objective transformation from the oral to the written mode.

Both thesis authors were present at all of the interview occasions and telephone interviews. The personal interviews took place at different locations in the Gothenburg area, at the offices of the interviewed companies or in premises at the Gothenburg School of Business, Economics and Law.

2.4.3 Interview questions

The interview questions are relevantly linked to the theoretical framework. The theories make the foundation from which the interview questions are derived. After scrutinizing the articles reflecting the current development within the research subject, a number of interview questions were written in order to provide the answers necessary to answer the main problem statement. Along with the theories of Kvale (1996), the interview questions should be brief and simple to get better answers. Therefore, the questionnaire has been constructed with questions as brief as possible to meet this criteria. The questions were introduced to and discussed with the tutor before the interviews were conducted.

To get the best possible answers from the respondents, in line with the research purpose to get the different perspectives, an interview questionnaire was formulated. Some questions were of general nature and relevant to both professions and were therefore included in all interviews. Each interview was formed based on the same idea and the same set of questions, although some parts of the interviews were individually prepared in order to fit the respondent's position and area of expertise. In the interview questionnaire below, it is stated which questions were asked to whom of the respondents, using the first letter of their surnames right after the question to indicate this. The questions were also adjusted and corrected during the interviews. The respondents were encouraged to speak freely and openly on the subject. As a result, it was possible to discover and receive information not explicitly asked for.

Table 1.1 Interview questionnaire

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| <ul style="list-style-type: none">• Please give a brief presentation of yourself, your education and career and your main assignments today. (D, G, S, T)• What is your opinion on the formulation of the IAS 38 regarding its treatment of brands? (D, G, T)• Is there, according to your opinion, a problem that there is a difference between acquired brands and internally generated brands? Why/why not? (D, G, S, T, W)• Should internally generated brands be recognized on the balance sheet? Why/why not? (D, G, S, T, W)• Regarding brand valuation; should there be a general international valuation method to be used by all companies in all countries? (D, G, S, T, W)• Do you think that the treatment of internally generated brands stands in contrast to the accounting demand for a <i>true and fair view</i>? (D, G, T, W)• Is there a comparison conflict between different companies if different systems for brand recognition are used in different countries? (D, G, S, T)• If acquired brands can be valued and recognized on the balance sheet as assets, why can not internally generated brands face the same procedure, i.e. why is there a difference between assets and assets? (D, G, T, W)• What do you think will happen in the future within the area of internally generated brands? (D, G, T, W, S)• Is the IAS 38 good enough today or is there a need to revise it to include internally generated brands on the balance sheets? (D, G, T, W) |
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- What is your definition of brand equity (asset) and brand value (financial metric)? Is there a difference between these terms? (S)
- According to you, should brands be measured as assets? How? (S)
- Do you think brand value can be measured with reasonable certainty? (D, G, S, T)
- What do you think will happen in the future within the area of brands? (D, G, S, T, W)
- Is there a certain difficulty related to the specific values that can be derived from the brand? (S)

2.4.5 Empirical presentation and analysis

As a result of this thesis' choice of method, the empirical data is presented along with the interview questions to ease the navigation and understanding of the research. In this way, the answers are naturally linked to the questions, and therefore to the theories, and it is easy to follow the collected empirical material under each topic. The empirical material is gathered under a number of head lines which together cover all interview question areas. The empirical findings are presented and analyzed using a qualitative method.

According to Lekvall and Wahlbin (2001) the interpretation and analysis of a qualitative research is mainly of subjective character. In this thesis, the empirical data has been compared to previous research and opinions within this area to form the analysis of the material.

2.5 Validity

Validity is concerned with the quality of the knowledge that is being developed (Arbnor and Bjerke, 1997). It is important that the study investigates what is intended to be investigated from the beginning. Further, it is important to procure a true picture of what is being studied and that the findings represent what is actually happening.

The personal implications on interviews can be misleading in some cases (Kvale, 1996). The interview questions have been discussed with the tutor and have been sent to the respondents in advance to ensure higher validity and receive well thought-out answers. The respondents were free to add or exclude questions during the interviews. Some of the persons interviewed had problems answering some of the questions since they were not applicable to the situation in which they worked. Therefore, it is likely to believe that some of the respondents have guessed and assumed certain things. However, it is not believed that these factors are negative to the validity in this case.

In one case, regarding one of the respondents, there were obstacles to make an interview. However, the validity was not affected negatively by this lack of information since another interview was conducted with an equal respondent. The number of respondents can be viewed upon as a limit to the validity.

There is always a challenge to collect and analyze relevant material. There is question whether the right questions to best answer the purpose have been asked and if relevant data for the stated problem was collected.

Two of the respondents have requested to read this thesis when finished, for further research purposes, which is proof of the up-to-date-ness of the study. It is not possible to measure empirically how good the validity by definition is, but all in all the study displays high validity.

2.6 Reliability

An interesting aspect about the credibility of the findings brings us reliability and the question if these results are possible to obtain again if conducted by another researcher (Ejvegård, 2003). Thus, if the research study is repeated, another can test the reliability of the results, and argue how dependable and trustworthy the results are. The findings of this study can be seen upon as subjective, thus uncertain whether another researcher with different interview subjects would receive the same results. Halvorsen (1992) defines reliability as how dependable and trustworthy the results are. High reliability indicates that independent measurements will provide fairly identical results.

The interviews have been conducted both with Swedish speaking and English speaking respondents. To be able to get the best results, all of the respondents were interviewed in their native language. This way, the respondents feel safer and give more accurate answers to the questions. As a result, there was a need to translate the Swedish interviews into English. This problem is also applicable to the Swedish literature used in this research. There could be a translation problem in these cases but as accurate translations as possible have been made, using all possible knowledge and dictionaries in the process. As a result, the translation process has not affected the reliability of the interviews and literature collection in a negative way.

To further increase the reliability of the research, the intention has been to carefully follow the instructions found in the methodology literature regarding issues affecting the reliability. As a result, the research has been conducted as good as possible given the external prerequisites. Further, each respondent's expertise within a specific area can also be considered a contributor to a high reliability in the research.

Reliability pertains to the consistency of the research findings (Kvale, 1996). The study is characterized by subjectivity from each respondent. Such subjectivity is however necessary to get the different perspectives on the research problem that is stated in the research purpose. This qualitative study is almost impossible to perform in exactly the same way once again because of the changing circumstances and the changing interview respondents. The thesis authors have tried to make professional interviews with small influence of personalities even though such influences are unavoidable. The interview findings are not generalizable because there are too few subjects; along with the theories of Kvale (1996). The secondary data collected have high reliability because of its consistency.

3 Theoretical framework

The theoretical framework consists of theories from different sources and perspectives to fully support the empirical research. The chapter is presented in five parts; brand accounting, the accounting treatment of intangible assets, a discussion on intangibles and IAS 38, the brand asset and brand valuation perspectives.

3.1 Brand Accounting

There have been numerous talks and discussions about the difficulty of reaching international harmonization regarding accounting for brands (Stolowy & Haller, 1996; Stolowy & Jeny-Cazavan, 2001). The debate on brand accounting has caused controversy and raised voices in many countries, particularly the United Kingdom and Australia. Influences by the Anglo-American approach have given a touch of more relevance than reliability in forming the current international accounting standards by the IASB. Stolowy et al (2000) state that brand accounting is the focus point of the conflicting relationship between the major characteristics of accounting data; relevance and reliability. It is not perfectly clear which of the two characteristics that is considered most important, but there is an emphasis towards more relevance. Moreover, the area where this challenging relationship between relevance and reliability becomes highly obvious is in accounting for intangibles. Intangibles, especially brands, have become increasingly important elements in the companies' balance sheets. The accounting consequence of intangible assets is always of interest and with practical relevance because of the relative significance which these assets, and often brand names, may have on the presentation of the balance sheet of certain companies (Stolowy & Haller, 1996).

Stolowy and Haller (1996) presented a study on the differences in brand asset recognition between France and Germany, pointing out some differences both in the definition of intangible assets and the recognition of internally generated brands. Tollington and Liu (1998) wrote about some of the weaknesses of the definition of an asset. Arguments were presented to include internally created intangible assets such as brands under the definition of an asset, as brands at the time fell outside the scope of the definition. Further, these researchers state that these valuable assets often are not reported on the balance sheet, due to the fact that such assets are not derived from a transaction or an event.

Still, at present times, internally generated intangible assets such as brands are not allowed to be recognized on the balance sheet. It means that many assets, which can produce future economic benefits, such as internally generated brands, are not included. Tollington (2002) argues that there is a need to bring these intangibles to the balance sheets. For example, a successful advertising campaign, which is the result of a transaction, may achieve extra sales, profits and market share over a number of years. Under such circumstances it can be said to contribute towards future economic benefits and therefore can be regarded as an asset. The definition makes advertising expenses seen as not possible to separate from the other goods or services in the company. Further, a situation where the core of a company's financial strengths and future economic benefit are excluded from the balance sheet is indefensible (Tollington & Liu, 1998). The result from this lack of intangibles on the balance sheet represents much of the gap between market and book values (Tollington, 2001).

Further, it is stated by von Colbe et al (2005) that there is a lack of adequate accounting rules concerning the treatment of intangible values, thus the need for further discussion is crucial. It

is also stated that the intangibles and its representation on balance sheets have long been under discussion. There is definitely potential for a broader reporting of these assets and there have also been talks of some sort of additional voluntary disclosure of these assets instead. This is supported by Kumar (2005), who states that there are several intangible assets of a company that are either not valued or not properly valued in its financial statements. Given the increasing importance of intangibles, accountants entered new fields by requiring their financial disclosure. However, the present financial disclosure norms on valuation of intangibles are not satisfactory. Accountants should value all those factors that contribute significantly to the market valuation of a firm. Historically, accountants have avoided valuing any asset that is not either sold or purchased or exchanged since they prefer to have market value as fair value to meet accounting criteria for valuing an asset.

As companies increasingly begin to recognize the value of intangible assets, it is interesting to know to which extent marketing should be viewed as an investment as opposed to an expense (Ratnatunga & Ewing, 2005). Companies spend significant amounts of money on marketing activities to optimize sales, profitability and brand equity. The question whether these companies spend the right amount of money on these activities therefore arises (Ratnatunga & Ewing, 2005). Extensive research shown by Barskey and Marchant (2000), Litman (2000), among others, presents intangible assets as the most sustainable source of competitive advantage. Therefore, as brand equity also often accounts for a major portion of shareholder value, the importance of brands and other intangibles becomes self-explanatory.

Intangible assets are known to generate most of corporate growth and shareholder value (Lev, 2004). Part of these intangibles is brands. Research by Lev (2004) shows that investors in capital markets systematically misprice the shares of intangibles-intensive companies. It is uttered that there is a need for more information from these companies, as the result is misallocation of resources when investors are kept unaware of the real intangible values. There are indications that companies should provide more information about their investments in intangibles and the benefits that come from these intangibles. If this information is not disclosed, substantial value is overlooked by investors and companies.

According to Nurton (2001), analysts in the UK demanded more information about brands from companies. A little more than half of the questioned analysts preferred to see internally generated brands separately identified. The importance for companies to monitor and manage brand value not only internally, but also the need for these companies to communicate these values externally to shareholders, is stressed. A more inclined environment towards brand values on the balance sheet would significantly boost the balance sheets.

3.2 The Accounting Treatment of Intangible Assets – IAS 38

In early 2004, the International Accounting Standards Board issued IFRS 3 “Business Combinations”, complementing the issuance with revised versions of IAS 36 “Impairment of Assets” and IAS 38 “Intangible Assets” (Haigh & Rocha, 2004). IFRS 3 gives a framework on how to conduct and deal with business combinations (Epstein & Mirza, 2005). Its objective refers entities to apply the purchase method and mainly stipulates that recognition of asset, liabilities and contingent liabilities will be recorded at their fair values and it also recognizes goodwill, which is not longer subject for amortization, rather tested for impairment (Epstein & Mirza, 2005). Concerning intangible assets, it stipulates that an acquired entity’s intangible assets should only be recognized if the criteria for an intangible asset in accordance with IAS 38 is fulfilled and its fair value can be estimated reliably (Epstein & Mirza, 2005).

The IAS 38 framework provides the guidance required for estimating whether the fair value of the intangible assets acquired in a business combination can be measured reliably (Epstein & Mirza, 2005). Public listed companies within the EU are required to apply and practice IFRS 3 and IAS 38.

3.2.1 Recognition criteria

IAS 38 is a comprehensive standard that establishes the recognition criteria, measurement bases and disclosure requirements for intangible assets (Epstein & Mirza, 2005). It also stipulates that impairment testing for intangible assets must be made on a regular basis so that only assets having recoverable values are capitalized and carried forward to future periods. Companies often expend resources on various activities, whereas the enhancement of intangible resources such as knowledge, intellectual property, brand names and licenses are among common activities (Epstein & Mirza, 2005). However, not all the items described as activities meet the definition of an intangible asset. An intangible asset is defined as a non-monetary asset, which is identifiable, without physical substance (Epstein & Mirza, 2005). The criteria of identification, control over the resource and existence of future economic benefits are not always met (Epstein & Mirza, 2005). Intangible assets are to be recognized when the following criteria are fulfilled:

- Separate identity from other aspects of the company;
- Controlled use by the company as a result of its past actions and events;
- Reliable cost measurement
- Expectation of future economic benefits

If an item within the scope of IAS 38 does not meet the definition of an intangible asset, it must be recognized as an expense. However, on the contrary, if the item is acquired as part of a business combination, it will constitute a part of the recognized goodwill (Epstein & Mirza, 2005).

3.2.2 Identifiability

The asset will meet the criteria of identification for an intangible asset firstly if it is separable, that is, capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged. Secondly, it will meet the criteria if it arises from contractual or legal rights, not considering whether the rights are transferable or separable from the entity (Epstein & Mirza, 2005). Identifiability does not require separability although if separability of an asset can be demonstrated, it can assist a company in identifying an intangible asset.

3.2.3 Control

Control is another important instrument subject for judgment. The company is considered to control the asset if it has the power to obtain and can determine that future economic benefits will flow to the company. It must also restrict the access from others from obtaining those benefits (Epstein & Mirza, 2005). Control implies the power to obtain future economic benefits from the asset and restrict others from having access to such benefits.

3.2.4 Future economic benefits

These benefits relating to the intangible asset can be from revenues, cost savings or from other benefits related to the asset (Epstein & Mirza, 2005). The criterion for future economic benefits follows the criteria for the recognition of assets that the probability of future

economic benefits will flow to the enterprise and the cost of the asset can be measured reliably.

3.2.5 Measurement

The standard expresses how the nature of the intangible assets tends to be difficult to determine. Most expenditure is not likely to meet the definition of an intangible asset and the recognition criteria in IAS 38. It is particularly difficult to attribute expenditures directly to a particular intangible asset rather than to the business as a whole. Further, it is stated that an intangible asset shall be recognized if it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity and if the cost of the asset can be measured reliably (Epstein & Mirza, 2005).

3.2.6 Internally generated intangible assets

Epstein and Mirza (2005) state the problems associated with recognition of an internally generated intangible asset, and whether it can fulfil the criteria to be activated on the balance sheet. The problems attributes to identifying whether and when there is an identifiable asset that will generate expected future economic benefits. Further, a reliable determination of the cost of the asset is also brought up. IAS 38 clearly stipulates that internally generated brands are not allowed to recognize as intangible assets on the balance sheet. Moreover, not even expenditure for such brands is recognized; expressing that expenditure cannot be distinguished from the cost of developing the business as a whole (Epstein & Mirza, 2005).

3.3 Discussions and controversies on intangible assets and IAS 38

Numerous articles have been presented to discuss advantages and disadvantages with the current IAS 38. It is of significant interest to bring forward the discussions and opinions on the current accounting treatment of intangible assets. These discussions contain different aspect and views on several subjects. Stolowy & Jeny-Cazavan (2001); Seetharaman et al (2002), among others, point out problems with the IAS 38 and stress the fact that it has been considered highly controversial among different parties.

Artsberg (2003) discusses the possibility to capitalize intangible assets. Regarding the treatment of intangible assets, there would fundamentally not be any differences in the way an intangible resource is treated and recognized compared to a tangible resource, i.e. that the resource meets the asset definition and recognition criteria. Ardent advocates of capitalizing these intangible assets, Tollington & Liu (1998); Tollington (2002), among others, express that there are sufficient and reliable methods, which can calculate and determine the relationship between investments and future economic benefits on such assets. On the contrary, critics of this line of conduct state that these calculations are subjective, much due to the fact that responsibilities are laid upon management to make decisions, resulting in insufficient or inadequate comparability between companies. Moreover, critics also express that tangible assets have alternative fields of application (Artsberg, 2003). It is possible to derive a sale price, while intangible assets are closely dependent and allied with the specific company and contribute to revenue only in combination with other assets, specifically the tangible assets. However, this argument could be viewed upon the other way around meaning that the tangible assets are bound to the intangible (Artsberg, 2003).

Seetharaman et al (2002) argue some of the problems recognized in IAS 38. Their study investigates mainly intellectual capital and intangibles, but their highlights of the problems with IAS 38 are also applicable to internally generated assets, such as brands. Firstly it

requires, for capitalization purposes, an item must meet the definition of intangible assets when it is currently known there is no comprehensive definition of intangible assets. Secondly, it requires that intangibles must be separately identifiable and distinguishable from other assets. This is also impossible to meet, as many intangibles already are interrelated and interwoven with each other. Thirdly, the company must demonstrate a clear control over the asset. Seetharaman et al (2002) explain how The Canadian Institute of Chartered Accountants has highlighted this difficulty in 1998 stating that organizations do not own or control all forms of intangibles. This means that the issue of having a clear control over an intangible asset is difficult to demonstrate. Fourthly, a company must be able to show that there is a probable chance of returns from the asset. Borneman et al (1999) believe that this shall not be made a criterion for capitalization as nobody knows with certainty on future returns for tangible assets or intangible assets. Financial accounting standards on future returns from physical assets do not rely on fact rather they rely purely on accounting conventions. Their future returns are as uncertain as that of intangibles. Furthermore, it is difficult to associate and link returns to a particular intangible asset. Finally, the cost must be able to be measured reliably. As a result, Seetharaman et al (2002) argue that IAS 38 is not a good solution to measure all intangible assets.

There exists an active market for many of the intangible assets. The presence of an active market makes it easier for the norm-setting environment to accept a capitalization of the assets (Artsberg, 2003). However, it is stated that an active market can not exist for brands due to the uniqueness of that specific asset (Epstein & Mirza, 2005). Much because of this, there is considered no possibility to provide a correct and sufficient value for a fair value of another similar asset. According to Artsberg (2003), financial analysts should be more reluctant towards recognition, whilst instead advocating detailed and open information in notes. This stands in contrast with earlier mentioned article by Nurton (2001), dealing with a sample of 238 financial analysts, where over 50 percent of these respondents in the UK preferred to see internally generated brands on the balance sheet.

Artsberg (2003) explains that the starting point for IASB, when developing the standards for accounting for intangible assets, was that intangible assets were to be handled with in the same way as tangible assets. However, the result is not in compliance with that intention. IAS 38 gives further range of possibility to capitalization than earlier standards, but does not allow as much as the advocates of recognition preferred. IAS 38 demands tough criteria in order to be able to recognize an intangible asset (Artsberg, 2003). Internally generated intangible assets are not assessed in the same way as tangible assets. The reason for this lies much in tradition. It had always been seen as a sign of weakness to capitalize intangible assets, historically several low performing companies have capitalized these assets. Another explanation is that these assets are more subject for judgement and estimations. Furthermore, the development of the norms and standards moves towards individual judgement in the specific company instead of general judgements and criteria. This results in higher demands on those who shall make the decisions. The fact that many intangibles are not recognizable can be explained by the norm-setting environment's fear to put too much of the decisions on an optimistic management. In order to be able to activate the intangible asset, there is, other than certain criteria in the asset definition, also the demand for identification. It is mainly this recognition criterion that makes it difficult to recognize the internally generated intangible assets. The demand for identification can also be seen upon as a demand for separability, i.e. that it is possible to reliably measure the expenditure for the asset (Artsberg, 2003).

Stolowy and Jeny-Cazavan (2001) present a study describing the international accounting disharmony concerning the case of intangibles and explain a need of moving towards accounting harmonization. Their research shows that there is no conceptual framework commonly accepted and that there is a lack of consistency both inter-country and intra-country. As mentioned earlier, these researchers state that IAS 38 has been controversial with the exceptional issue of two exposure drafts that challenges the principle of acceptability of all international accounting standards by companies that wish to or are required to apply these standards in general. Epstein and Mirza (2005) also express the exceptionality of two exposure drafts. Moreover, Stolowy and Jeny-Cazavan (2001) argue that there is nothing fundamentally different about tangible and intangible assets and that there is no theoretical conceptual framework behind the approaches to intangible assets. The explanation that there would be no differences has been widely debated. Lev and Zarowin (1999) claim that an intangible asset should be treated like any other tangible asset. This is supported by Henriksen and van Breda (1992), who argue that intangible assets are just as much assets and should follow the same recognition rules, even though they lack substance. Furthermore concerning the debate on recognition, it has been assumed that the recognition of intangible assets was determined by the trade-off between relevance and reliability, conservatism vs. prudence, and the way they affect the information value of accounts (Hoegh-Krohn & Knivflå, 2000). If the existing asset recognition boundary is too restrictive then this is likely to result in an incomplete view of the balance sheet (Tollington, 1998b).

Discussing the example of brands, there are some main arguments against a definite useful life, and therefore against amortization of brands (Stolowy & Jeny-Cazavan, 2001). In many countries the legal protection of brands is unlimited or at least renewable indefinitely. Some brands are very old, e.g. 150 years for the French Champagne brand Moët & Chandon, and are expected to continue their useful life for an unforeseeable future (Stolowy & Jeny-Cazavan, 2001). Some authors argue that the value of a brand is maintained or even increased by significant advertising expenses, which are recognized as expenses and do not therefore give reason for amortization or a limitation of the useful life (Perrier, 1997). On the contrary, those in favor of amortization and a limited useful life for brands put forward responses to these arguments. For the purpose of financial reporting, an economic approach is more relevant than a legal point of view. The expenses incurred to maintain a brand, e.g. advertising costs, are not arguments in favor of an indefinite life as it could mean that the purchased brand is eventually replaced by an internally generated brand, which should not be recognized as an asset. Just as there seem to be examples of brands always keeping their value, there are also brands which have vanished (Stolowy & Jeny-Cazavan, 2001). In the end, the debate over brand amortization can be broadened to include intangible assets. It is a question of what is desired to obtain through the amortization process. If the purpose of amortization is to reflect current value, there seem to be more objections than reasons for its application. On the other hand, if the purpose of amortization is to spread the recognized amount over a limited time, there are more arguments in favor of regular amortization (Stolowy & Jeny-Cazavan, 2001).

Artsberg (2003) discusses some of the reactions from the norm-setters in different countries concerning intangible assets. It has been a long and tough process for IASB, bringing forth a standard on intangible assets. During the creation of IAS 38, there was significant critique brought forward from the practitioners, especially concerning issues about amortization and useful life. From the beginning it was meant that twenty years was the maximum number of years that an intangible asset could be amortized. However, the IAS 38 stated that it is possible to apply a longer useful life period longer than twenty years, if it can be proven. IAS

38 also applies an alternative rule to amortization that it is possible to regularly do an impairment test. Another critique concerned the fact that it is not possible to capitalize internally generated brands. This critique was not taken into consideration. A list of 96 comment letters on Exposure Draft 50, which was one of the first drafts on IAS 38, displayed several different opinions, both positive and negative, on the IASB discussion concerning valuation and recognition criteria.

According to Artsberg (2003), the opinions in these comment letters differ significantly. The problem is that different countries bring criticism on different issues with the critique taking various forms. Thus, the critique of one country stands in contrast to that of another country. Australia, France and Switzerland are found especially critic to restrictive attitude towards the possibility to activate certain intangibles as assets. The critique from larger countries is mostly due to own traditions and a developed norm-setting environment, which can be difficult to change. Another French company, the luxury conglomerate Christian Dior, expressed frustration over having to amortize its brands over twenty years, when having useful life periods over 200 years, and also not being able to recognize internally generated brands. IASB changed its view concerning amortization time but not concerning the recognition of internally generated brands. This restrictive standpoint was, needless to say, not in line with the view of the accounting association of Australia, which thought that Exposure Draft 50 did not reflect economic reality in relation to the recognition and measurement of those assets and failed to recognize the importance of intangible assets in the new modern economy. On the other hand, the German view was that the recommendation could be even more restrictive. The German norm-setters are famous for being conservative in their accounting (Artsberg, 2003). However, concerning the French and Swiss environment, the Swiss accounting professionals are being in favor of IAS 38, but not the French, although both countries are famous for prudent accounting. The companies in both these countries would like to see less restrictive rules. Needless to say, the opinions differ, and it is difficult to find a pattern in the way they differ. The companies are in favor of less restrictive rules and the accounting professionals are not (Artsberg, 2003). Moreover, Stolowy et al (2001) presented a study where accounting for brands in France and Germany was compared with IAS 38. These two countries have adopted very different solutions in relation to each other and to IAS 38. This highlights the difficulty of international accounting harmonization. It also shows that the often made association between relevance and reliability, derived from the concern for qualitative characteristics of accounting, may not be able to apply on accounting for brands. The authors argue for a disclosure of additional information to solve this international accounting disharmony.

Concerning the present accounting framework, Lev (2001), Seetharaman et al (2002), and many others, including accountants themselves, agree that the current accounting system has serious deficiencies. The current accounting and financial reporting practices have also been criticized by many business leaders, especially in the high-tech industries and by financial analysts, as not keeping pace with the vast changes in the business world (Seetharaman et al, 2002). According to Seetharaman et al (2002), it is stated that intangibles are difficult to isolate and value, which bring challenges to the accounting and reporting process. If these intangibles are said to be the driving force for future innovation and profits growth, this means more money would be invested on intangible asset development. The accounting profession has a negative view on money spent on intangible assets. Rather than seeing it as a productive investment for future innovations and growth, they see it as a loss and the more a company spends for its intangible asset development, the greater the loss would be. According to Lev (2001), not only does accounting fail to capture some intangible assets, but

also accountants do not treat assets as assets. This is also agreed by Brennan (2001), who argues that the current accounting framework, which is transactional and realization based, only recognizes the existence of an item when transactions with third parties take place. It assumes that when there is no transaction, then no value is created. According to Leadbeater (1999), traditional accounting approaches based on transactions to measure assets are not suitable for intangibles, as these assets are not actively traded unlike tangible assets.

According to Seetharaman et al (2002), problems with intangibles are that values are very subjective, and unlike tangible assets, intangible value could disappear overnight and thus, create uncertainty among investors and managers rather than helping them. Seetharaman et al (2002) describe how numerous attempts to measure or value intangible assets over periods have run into the difficult problem of pricing such assets. It is said that there seems to be more problems in capitalizing intangible assets in the financial statement than expected. If they are capitalized at cost, problems that would be encountered include uncertainty surrounding the possibilities to realize such assets and it would not be a good indication of such assets economic value. However, if intangible assets are capitalized based on economic value, discounted cash flows, then another set of problems would emerge. There is a subjectiveness of the cash flow projection, which is strongly dependent on changes in interest rates, inflation or future outlook. There is also a difficulty to break down total value into individual intangible value.

According to Ballow et al (2004), accounting practice has not kept up with developments in modern economies. Decades ago, businesses generated value through tangible assets, such as buildings and equipment. In our more knowledge-based economy, businesses are likely to generate much of their value through differentiating themselves by using intangible assets such as proprietary processes, brands etc. However, these are the assets current accounting practices are most likely to overlook. Seetharaman et al (2002) talks about brand capitalization, admitting that brand valuation is filled with difficulties and attempts in the UK to put brands on the balance sheet have been highly controversial. It is concluded that more needs to be done before brand value estimation could be included on the balance sheet. Brennan (2001) also believes that there is still a long way from knowing what the best practices for intangible measurement and reporting are.

3.4 Brand definitions, Brand assets and Brand equity

There are several different definitions of what a brand really is. According to Kotler et al (2001) a brand is; a name, term, sign, symbol or design, or combination of them which is intended to identify the goods or services of one seller to differentiate them from those of competitors. Further, a brand can also be defined as an asset that does not have physical existence and the value of which can not be determined exactly unless it becomes the subject of a specific business transaction of sale and acquisition (Seetharaman et al, 2001). According to Motameni and Shahrokhi (1998), it is stated that the competitive advantage of a successful brand name is a valuable asset for the firm owning the brand. The value of this advantage is indicated by the money paid by firms that have acquired consumer package goods with strong brand names. Moreover, Murphy (1990) stresses that a brand is a complex phenomenon. It is not only an actual product; it also bears uniqueness for a specific company and has been developed over time, including both tangible and intangible values, which differentiate products. Whatever definition, brands are proved to be valuable assets for many companies. A brand consists of many different aspects, all influencing the value of the brand.

The recognition of brands as assets can occur in three different ways (Tollington, 2002). Firstly, as the result of a transaction when purchasing or licensing a brand, secondly, as an extraction from the transaction for the purchase of goodwill and thirdly, as the result of a managerial decision to include internally generated brands on the balance sheet. However, the third way is not in compliance with the current IFRS 3 (Epstein & Mirza, 2005). Tollington (2002) defines a brand asset as; a name and/or symbol, design, trademark, logo used to uniquely identify the goods or services of a seller from those of its competitors, with a view to obtaining wealth in excess of that obtainable without a brand. A brand asset's unique identity is secured through legal recognition which firstly protects the seller from competitors who may attempt to provide similar goods and services, and secondly enables it to exist as an entity in its own right and therefore to be capable of being transferred independently of the goods and services to which it was originally linked (Tollington, 2002).

According to Aaker and Joachimstaler (2002), the objective of many marketing managers is to create a strong brand. However, the definition of a strong brand is hard to determine. The brand asset consists of several things that might provide a value to the company. Aaker and Joachimstaler (2002) define brand equity as the brands assets (or liabilities) linked to a brand's name and symbol that add to (or subtract from) a product or service. These assets can thereafter be divided into four dimensions; brand awareness, perceived quality, brand associations and brand loyalty. Further, these dimensions guide brand development, management and measurement. Firstly, brand awareness has been shown to affect consumer perceptions and taste. However, brand awareness is an often undervalued asset. People like the familiar. Secondly, perceived quality has been shown to affect profitability, as measured by both return on investment (ROI) and stock return. It is a special type of association as it influences brand association in many contexts. Thirdly, brand associations could be anything that links the customer to a certain brand. It can include brand personality, symbols and product attributes. Finally, brand loyalty is an important part of any brand's value. The aim is to strengthen the size and intensity of each loyalty segment. A brand with a small but loyal customer base can have significant equity (Aaker & Joachimstaler, 2002).

According to Ratnatunga and Ewing (2005), the notion of brand equity has attracted considerable attention. These authors stress the importance of defining and contrasting brand equity components. They define brand equity as the asset, that is, what one has, for example a Ferrari F1 racing car (tangible asset) or Michael Schumacher's driving skills (intangible asset). Brand capability is what can be achieved or what one can do when these asset categories are combined in a contextual situation, which is, winning the F1 World Championship. Moreover, Rao et al (2004) provide evidence of a great variety of research concerning the importance of brand equity. It is stated that a powerful brand is necessary to achieve growth. Research by Aaker and Jacobson (1994) shows that brands have been accepted to attribute to a financial value, because of their ability to generate future cash flows. Further, researchers have found that financial markets take brands into consideration in stock valuation (Barth et al, 1998; Simon & Sullivan, 1993). This is also supported by Lamons (2004), where brand equity is defined as the percentage of a company's total market capitalization which is directly attributable to its corporate brand. However, it comes with problems as it is difficult to put a specific number on or measure exact brand equity (Lamons, 2004). Finally, there have been several articles on the estimation of brands' financial value and measurements techniques (Haigh, 2000; Keller & Aaker, 1992). According to Lev (2001), there are no doubts that brands are intangible assets of a firm.

3.5 Brand valuation

The problem with brands on the companies' balance sheets has among other things to do with the different methods for brand valuation. These methods provide different solutions to how brands should be valued. Every method has its limitations. Brand recognition depends on how well the brand value can be measured. There are several methods of determining the value of a brand. These methods can generally be classified into four types based on existing uses (Seetharaman et al, 2001).

1. *The cost-based approach* is based on the costs involved in developing a brand, meaning the actual costs for acquiring, building or maintaining the brand. This method is conservative as it complies with standard accounting practice for valuing assets. Therefore, accountants see this method as the most suitable way to value a brand. On the other hand, marketers disagree because of the method's disability to capture the value added by strategic brand management and because the method tend to look to the past rather than the future. All previously expended brand-related costs must be included. Tollington (1999) states that the problem with this method is to identify the costs which were not attributable to the brand but were expended in support of it.
2. *The market-based approach* focuses on the external brand management approach and is based on the amount at which the brand can be sold. To determine the market value, the future benefits associated in owning the brand are included. The problem, however, is to determine the market value (Tollington, 1999). The estimation of the brand value can be difficult due to the absence of an actual market for most brands. Financial markets can make this estimation by separating the tangible assets and the intangible assets. Most firms, however, consider market-based approaches impracticable because of the amount of research they involve.
3. *The income-based approach* focuses on the future potential of the brand. This method avoids the problems related to the costs. To determine the net revenue of a brand there are several different approaches to be used. One is to compare the brand's generic product to an unbranded equivalent. Another method is to estimate the annual royalties associated with the brand as it is in a licensing agreement. A third method is to consider supply and demand to estimate brand strength.
4. *The formulary approach* involves various criteria to determine brand value. This method is suitable for internal-management purposes and for external financial reporting. Brand profitability is computed, taking into account the factors directly related to the brand identity. A multiplier is then attached to the valuation. To determine a multiplier there are seven factors to take into consideration; leadership, stability, market, support, protection, international image and trend of the brand. Formulary approaches generally have fewer disadvantages than the other methods of assessing brand value (Seetharaman et al, 2001).

The different methods for brand valuation create a situation where different aspects are taken into account in different valuations. This can lead to that brands are valued differently in different countries. Motameni and Shahrokhi (1998) describe how and when to value brand assets. They argue the importance of a global perspective on brand valuation in order to make brands more comparable. This is argued to make it easier for brands to be recognized as assets and make their way to the balance sheets. Further, Seetharaman et al (2001) argue the importance of global standardization principles regarding brand valuation. It is stressed that

there must be a commonly accepted brand valuation technique, to be used by all companies. Moreover, Tollington (1999) brings forward critique to the existing brand valuation methods. It is clear that the main brand valuation methods lack consistency, that is, a lack of general agreement on methodology, and subjectivity at every stage of the valuation process, no matter the valuation technique. Tollington (1999) states that the brand valuation technique becomes the basis for both recognition and measurement of the brand asset. As Tollington (1999) does not see problems with the recognition of internally generated brands, the valuation methods themselves are considered problematic. The professional bodies have been uncertain how to solve the brand valuation problem. There is a lack of understanding and guidance over the accounting treatment of brands. The uncertainty associated with brands and the confusion about the distinction between brands and other assets leads to problems when deciding how to measure and report such assets (Seetharaman et al, 2001).

3.6 Summary of theories

Theories consist of a discussion on brand accounting followed by a description of the current accounting treatment of intangible assets in international accounting standard 38. It is important to give a view on the different perspectives about brands and their accounting treatment, both what is allowed to act and also what has been done anyway.

This section is followed by a deep, thorough discussion about several discussions and controversies, views and opinions over the years on intangibles and the IAS 38. The formation of this standard is characterized by controversy and there is critique on a plethora of different issues. The discussions described range from recognition issues and the question if an intangible asset is an asset to amortization and useful life problems.

Furthermore, the brand as an asset is discussed given several researchers' points of views. Brand equity has a received attraction in the last couple of years and therefore is also included and described. Finally, the methods and discussions about brand valuation are necessary to fully support the problems concerned with the recognition of intangibles.

4 Empirical data

In this chapter the empirical findings from the research is presented. The material is linked to the theory and the interview questions provided earlier. The empirical data is presented consequently along the interview question areas to make it easier to follow the discussion. The empirical material in this thesis is fully based on interviews. The material as presented as it was said, without any further analysis in this chapter.

4.1 Perceptions of the accounting treatment of brands in IAS 38

In general the IAS 38 is restrictive, according to Gröjer (2006). However, the interesting part is that when doing an acquisition, in accordance with the IFRS 3, you are allowed to be less restrictive. Therefore, we end up with two different systems, one relating to the development of brands and the other when another company is acquired and expenses can be activated. Gröjer (2006) finds this a bit awkward.

Drefeldt (2006), states that nothing is permanent concerning the formation of IAS 38 and that it is constantly developed. In doing this, there should be a certain amount of conservatism because it is hard to value brands. The acquired brands are always recognizable but it is harder with the internally generated brands. The problem is how such brands should be measured. The reason for such brands not to be recognized on the balance sheet is that the costs and expenses can not be separated with reasonable certainty. The question of contra accounting is also important.

According to Tollington (2006), the distinction between an internally generated brand and a purchased brand is artificial, based on rules imposed by accountants.

There is overlap between accounting and marketing in terms of trying to measure things, in trying to quantify brands and brands values but much of the drive of marketing is to create associations and to create strategic brands which then can be leveraged and extended to different product categories and industries, where that is not accounting school at all. The accounting school is more trying to handle how this brand works, but you can see an interesting fusion of accounting trying to predict or control the kind of leveraging activity a brand might undergo (Schroeder, 2006).

4.2 The difference between assets and assets

According to Schroeder (2006), brands should be measured as assets because so much of the organization's strategic focus nowadays is on building a brand, and the brand allows the corporations to do a whole lot of different things, you can leverage a brand as an asset.

The big problem is that internally generated brands can not be measured because there is no initial expense. As a result, such brands can not be measured with reasonable certainty along with the IAS 38 p. 45. For an asset to be recognized on the balance sheet, there are several criteria that must be fulfilled. One is that the asset can be valued with certainty, in Sweden according to RR 15 p.45. The big problem with internally generated brand is that they can not be measured with this certainty (Drefeldt, 2006).

You can put it this way, states Gröjer (2006); if a brand is acquired externally there is always a market-based price or a market quotation. This, however, is based on the perception that company leaders normally make clever decisions and that they do not pay too much or too little for the brand. This reference, i.e. the market price, does not exist for the internally generated brand and this is the difference. However, the different expenses that build a brand are of course transaction. It is the combination effects of these external transactions that are unclear if it has a market value.

Tollington, (2006) argues that the difference between brand assets relates to the issue of reliability of measurement.

Member of the IASB (2006) states that it is a question of reliability of evidence: acquired brands involve an arms-length transaction between independent parties.

Schroeder (2006) states that it partly depends on how brands are measured. Further, about equity as among other things, there are two main issues, how well known your brand is, and how positive or negative people or the market, feels about it. Some sense from the marketing perspective is that the evaluation often comes from consumers or consumer groups. From a financial perspective, the evaluation comes from the investment people. They can tell you for example how Volvo is doing as a company. So it's just a little bit about what community or what group is providing the information on how you value it. Therefore, there is a little bit difference in terms of what is the value of a company on the stock market compared to what the is the value of a brand in the market. They are certainly correlated but it is just a little bit different what you are thinking about (Schroeder, 2006).

Schroeder (2006) points out the example Hasselblad, a company which has an incredible high equity in terms of it is considered a high quality brand. The company has received critique for not capitalizing on their brand asset, for not leveraging it. According to Schroeder (2006), more and more people within companies will be held accountable for not leveraging and using the strong brand to the extent that they should. Brands should be measured as assets but Schroeder (2006) also points out the importance of leveraging the brand and the brand extension. Companies not coping with these issues will be seen as old fashioned. There is so much strategic activity in building a brand.

4.3 Acquired brands and internally generated brands

Member of the IASB (2006) states that the difference between an acquired brand and an internally generated brand is the evidence of a transaction to support recognition and measurement of an acquired brand.

As earlier mentioned, the distinction between an internally generated brand and a purchased brand is artificial based on rules imposed by accountants (Tollington, 2006). Thus, no difference exists.

Further, Tollington (2006) argues that if brand recognition is supported by a trademark then prima facie it is transactable, preferably using the word "transferable". The fact that it may be non-transaction based (i.e. internally generated) is irrelevant for the purposes of recognition on another, and equally valid, legal basis: trademarking. The prohibition of internally generated brands from IAS38 is therefore nothing to do with the issue of asset recognition; rather, it is an issue of asset measurement and the reliability thereof. The real question is

whether a brand should be excluded from the balance sheet because of its measurement “unreliability”. This is a much broader issue concerning accounting as a whole, notably, between a stewardship view of accounting (favouring transactions) and an economic decision making view (favouring fair values), the latter being the trend over the past 20 years.

Drefeldt (2006) does not see any problem with the difference between acquired brands and internally generated brands today.

Gröjer (2006), on the other hand, argues that there is a problem as long as only internally generated brands are allowed to consist of activated factual expenses. However, there is a dilemma when the brands are to be revaluated but this is also a problem regarding acquired brands. All in all, it is strange that there is this difference between different brands.

In a marketing perspective there is not really a difference between acquired brands and internally generated brands. In terms of brand management, it would not make that much different. Technically it would be different but it is hard to quite see the difference between the brand itself and how you think about it. It might just depend on the corporation (Schroeder, 2006).

As a result of the debate over internally generated brand and acquired brands, a direct question was addressed to the respondents; *should internally brands be recognized on the balance sheet?* The respondents answered sequentially:

“Yes” (Tollington, 2006).

“Yes, if there is sufficient supporting evidence” (Member of the IASB, 2006).

Internally generated brands should not be recognized on the balance sheet. Acquired brands can always be capitalized but it is harder with the internally generated brands. The costs can not be separated or measured with the certainty needed (Drefeldt, 2006).

Brands should be recognized on the balance sheet if the costs are activated. When activating these costs, the judgement must also be that there is a future value. There are practical difficulties with separating current costs from new investments (Gröjer, 2006).

Maybe that is a market issue whether a distinction between acquired brands and internally generated brands should be made. If companies are willing to buy a brand from within a portfolio, e.g. from Procter & Gamble, they will sell this brand, and not sell the rest, then why shouldn't they be recognized? It seems like they are separate. And that is really the way that brands have gone in the last couple of decades, they are seen as assets and they could be sold off without selling off the entire company (Schroeder, 2006).

4.4 Internally generated brands and true and fair view

Gröjer (2006) finds himself amongst those who believe that a true and fair view can not be created if it is not known exactly what a true and fair view really is. In order to have a true and fair view there must be some sort of key. Further, Gröjer (2006) looks upon accounting as a construction of a reality rather than a representation of reality. This makes terms like true and fair view a bit complicated, if accounting is a representation of a construction. The

problem is the term true and fair view. It is never clear which is the absolute correct way to do something.

Tollington (2006) agrees, referring to Arden (1993, para14): "...true and fair view is a dynamic concept. Thus what is required to show a true and fair view is subject to continual rebirth." Further, Tollington (2006) stresses that "truth and fairness" are compromised through the absence of internally generated intangibles from the balance sheet, but as Arden (1993) indicates, there is no absolute version of the truth. As Pontius Pilate once commented "What is truth?" (Tollington, 2006).

Member of the IASB (2006) does not think the treatment of internally generated brands stands in contrast to the demand for true and fair view.

It would be wrong to recognize internally generated brands on the balance sheet and it would certainly stand in contrast to the true and fair view as it would present the value on the balance sheet date. The company cash flow is still the most important (Drefeldt, 2006).

4.5 Comparability between companies – a comparison conflict?

From a recognition view there is a comparison conflict where some companies are disclosing brands and others do not. From a measurement view many would argue that, as the brand value is extracted from purchased goodwill (also disclosed on the balance sheet), it is irrelevant as to whether one labels the disclosure as a brand or goodwill. (Tollington, 2006)

At first, this is a philosophical problem. The question is whether the comparability is increasing or decreasing if the prerequisites are totally different. A very central criteria of accounting is comparability, everybody within accounting knows the importance of comparability. However, the question is how to obtain comparability if the prerequisites are widely different. Should the rules be applied in the exact same way? This is difficult. Comparability is important! There is always the possibility to do exactly the same thing, no matter the context. But if some experience is acquired, knowing for example that a service company is not exactly the same as a manufacturing company, the differences are already here big enough to question whether there should be a general appliance or if there should be an adoption to the business in which the company exists (Gröjer, 2006).

According to Drefeldt (2006), there is no conflict because of the harmonization with the IFRS where all national diversities disappear. This way the national differences play no significant roll in international accounting.

4.6 Brand valuation

Brand valuation is an interesting matter. It would make sense to have a general international valuation method if brands are a big part of the accounting standards. It is still difficult because that some brands are part of national industries and some brands are part of protected markets. It will probably be a while until such brand valuation methods are formulated. It is up to the market to decide; after all it is a powerful mechanism (Schroeder, 2006). The problem is that the creativity and the promises can not be quantified. It is still all about strategy, and we can not really quantify that for while. It takes creativity and it takes execution and you can not make it scientific (Schroeder, 2006).

The important thing is the transparency; that the companies show how the valuation was made. The method itself is not that important but in theory one should always use the discounted cash flow (Drefeldt, 2006).

Brand valuation is a difficult question, according to Gröjer (2006). The problem is that if the value is to be revised there is need for an accounting prerequisite (accounting necessary conditions). The value itself can not be the prerequisite; it must be the process that has lead to a certain value. If you compare with Research & Development, there is a sharp line between R&D and product development. The same problem is found regarding brand valuation. However, it is the other way around. When it comes to R&D it is the short term costs (product development costs) that are activated and the long term costs are expensed right away. Regarding brands, on the other hand, it is the short term cost that are expensed right away and the long term costs that are activated. Some sort of general idea of which costs that should be a part of an activated brand is necessary (Gröjer, 2006).

Brand valuation is dependent on how much is meant to be measured. The stock market is a measure of brand value. Economists argue that the system is not perfect but if looking at the thousands of millions of investors making decisions one might assume that the expressed value is decent value of the brand. However, some listings on the stock exchange are not exactly what the brand is. In my opinion, people are more and more thinking about corporate brands because such brands are very synonymous with the brand itself. Corporate brands are really most of the best known brands. In that case you would say that the corporate brands is listed on the stock market and as are a pretty good proxy for the brand value but it is of course much more complicated than that (Schroeder, 2006).

In principle, there should be a global valuation standard for all companies. In practice, it is uncertain, because it may depend on the availability of information (Tollington, 2006). Member of the IASB (2006) states that there should be a general international brand valuation method to be used by all companies in all countries.

4.7 The future of brands and the IAS 38

Schroeder (2006) states that in the future, we will probably see more virtual brands, brands that exist almost independently from distribution channels and factories. It will be just the brand or this entity which could be bought and sold. The brand will become more like money, as an exchangeable object. The future will also see brands that are placed into different industries, to follow the examples of Virgin or Ferrari. There will also be brands built on history and legacy, brands which refer back to the history and use that as a competitive advantage

Drefeldt (2006) does not think that internally generated brands will be allowed on the balance sheets within the next three years. It is to a complex question to be dealt with. However, there are difficulties within the IAS 38 that need to be taken care of.

Gröjer (2006) sees two different future developments. One is that the accounting practice is separated from what analysts want i.e. the analysts must gather own information to a larger extent than today. The value relevance in accounting is therefore decreasing. On the other hand, there are institutional prerequisites. For example, the annual report must not contain any traces of “price relevant information”, according to the registration contract. This is the basic idea even though there might be some new information in the annual report and many people

tend to miss this. For some people, the quarterly report is the most interesting. The question however, is how much information the quarterly report will contain in the future. We might see a future where neither the annual report nor the quarterly report is interesting. The companies can be connected to other companies' terminals to look closer at the sales figures in real time.

Drefeldt (2006) thinks that the regulation for internally generated brands is enough and does not see any further development on this issue. However, there is a need to look deeper into the development of the IAS 38 in general as it contains several areas that need to be developed to meet the real world. One example is the matching principle, for example is not a marketing campaign allowed to be matched over periods. It is simply considered a cost. This has been neglected by the IASB, it is only referred to as "bad accounting". Within this area there must be a change to meet the reality.

The IAS 38 is a product of an extreme compromise (Gröjer, 2006). After ten years of investigating, there must be compromise to produce anything at all. The result after this time must be as conventional as possible; there were no space for more controversial thinking. Therefore, Gröjer (2006) believes that there is already a project running today to revise the IAS 38.

The value of market capitalizations in the world will continue to grow with the ongoing shift from product-based companies to service-based industries. This leads to more intangibles on the balance sheets and definition problems along with the IFRS 3 on intangibles. Some assets can be questioned why they can be recognized but also how companies choose to portion over valued acquisitions. The problem is that there is no control over some intangible assets over a certain period of time, for example customer relations (Drefeldt 2006).

Nothing will probably happen in the future within internally generated brands because the attachment to a transactions basis to accounting is so profound and longstanding that one cannot see a development of valuations-based accounting independently of it. The IAS 38 is not good enough but the issues are much broader than intangibles, that is, concerning the nature of accounting itself (Tollington, 2006).

Member of the IASB (2006) states that brands are likely to be recognised more often in accounts, as confidence develops in measurement techniques, but that there will be limits to this. It is unlikely that all brands will meet the recognition and measurement criteria. Further, the IAS 38 should be reconsidered eventually, but there are other priorities.

5 Analysis

In this chapter the empirical data is analyzed with inputs from the theoretical framework to investigate whether the data correlate. The empirical data is analyzed in a qualitative way by comparing the respondents' opinions with previous research within the area of brands in accounting.

5.1 Perceptions of the accounting treatment of brands

The accounting treatment of an internally generated asset, such as a brand, is described in IAS 38 (Epstein & Mirza, 2005). Companies are not allowed to recognize such assets on the balance sheets. As described in earlier research and discussions, there are numerous opinions and views on these matters (Artsberg, 2003). First of all, Tollington (2006) finds the way of handling internally generated brands unacceptable, stating that the distinction between an internally generated brand and a purchased brand is artificial, based on rules imposed by accountants. Henriksen and van Breda (1992) also argue that intangible assets are just as much assets and should follow the same recognition rules even though they lack substance. From a marketing view, Schroeder (2006) finds no difference between acquired brands and internally generated brands, and finds no reason for different treatment. Gröjer (2006) finds the IAS 38 restrictive and a bit awkward, pointing out that it really means two different systems, one relating to less restrictiveness regarding acquisitions in IFRS 3 and the possibility to activate expenses, and the other relating to the more restrictive view on the development of brands. If the existing asset recognition boundary is too restrictive then this is likely to result in an incomplete view of the balance sheet (Tollington, 1998b). Finally, Drefeldt (2006) takes on a whole different viewpoint, arguing the impossibility to activate an internally generated brand and points to the problem of how such brands should be measured. This is supported by von Colbe et al (2005) who argue that there can be obstacles concerned with the insecurity of measuring intangibles. Also, the opinions of Drefeldt (2006) that costs and expenses can not be separated with reasonable certainty are in line with the current formation of IAS 38 (Epstein & Mirza, 2005). A view in line with this statement is provided by Seetharaman et al (2002) who state that intangibles are difficult to isolate and value, meaning a real challenge to the accounting profession.

Some accounting professors, including Gröjer (2006), believe the two different systems for brand accounting used today is not preferable. This is supported by Ballou et al (2004) stating that accounting practice has not kept up with the modern economy development. These two systems make the international accounting term true and fair view inadequate. However, the accounting term true and fair view seems to have lost its meaning to some extent. As stated by Gröjer (2006) and Tollington (2006) a true picture of reality can not be made. Further, Tollington (2006) argues that the true and fair view is compromised with the absence of recognized internally generated brands. Moreover, Drefeldt (2006) stresses the point that the difference between acquired brands and internally generated brands is necessary, because of the lack of an initial transaction. This correlates to the view of Member of the IASB (2006) who feels that it is a question of reliability of evidence; that acquired brands involves a transaction between independent parties.

5.2 Controversy in accounting for intangibles

As mentioned earlier, there have been numerous talks and discussions about the difficulty of reaching international harmonization regarding accounting for brands and intangibles (Stolowy & Haller, 1996; Stolowy & Jeny-Cazavan, 2001; Artsberg, 2003; Seetharaman et al, 2002). Barskey and Marchant (2000); Litman (2000), among others, present intangible assets as the most sustainable source of competitive advantage. Therefore, intangibles, especially brands, have become increasingly important elements in the companies' balance sheets as argued by Stolowy and Haller (1996). It is stated by von Colbe et al (2005) that there is a lack of adequate accounting rules concerning the treatment of intangible values. The need for further discussion within this area is considered to be crucial. In the new brand world, where the world changes towards more and more intangibles and brand assets, the demand for more adequate recognition criteria for these assets arises.

Artsberg (2003) explains that when developing the standards for accounting for intangible assets, the starting point for IASB was that intangible assets were to be handled with in the same way as tangible assets. However, the result was not in compliance with that intention. IAS 38 gives further range of possibility to capitalization than earlier standards, but does not allow as much as the advocates of recognition preferred. Tollington (2002), for example, expresses several arguments in favour of recognition. Agreeing with Artsberg (2003), Gröjer (2006) stresses that the IAS 38 is a product of an extreme compromise. After ten years of investigating, there must be compromise to produce anything at all. The result after this time must be as conventional as possible; there were no space for more controversial thinking. Another explanation for this, argued by Artsberg (2003), lies in tradition and that these intangible assets are too much subject for judgement and estimation in order for them to be recognized.

The recognition of brands on the balance sheet requires specific criteria stated in the IAS 38. According to Drefeldt (2006) and Epstein and Mirza (2005), the recognition of internally generated brands is impossible. Drefeldt (2006) argues in favour of this accounting perspective that there is no initial expense and no market value to measure from. Furthermore, it is stated that it is not measurable with enough certainty. Gröjer (2006) points to the favour of the accounting standard that if a brand is acquired externally there is always a market-based price or a market quotation and that this reference does not exist for an internally generated brand. However, according to Gröjer (2006), the expenses for building up the brand are derived from transactions. On another note, criticism towards not recognizing internally generated brands has been brought forward. Seetharaman et al (2001) argue that there are some major problems with the IAS 38 that prevent brand assets from being recognized. Tollington and Liu (1998) and Tollington (2002) argue that there is something wrong when a firm's major asset can not be recognized as an asset. This is supported by Tollington (2006), who talks in favour of recognizing internally generated brands on the balance sheets.

Drefeldt (2006) does not see any problem with the difference between acquired brands and internally generated brands. Gröjer (2006), on the other hand, argues that there is a problem as long as only internally generated brands are allowed to consist of activated factual expenses. However, there is a dilemma when the brands are to be revaluated but this is also a problem regarding acquired brands. All in all, it is strange that there is this difference between different brands. This view is also supported by Schroeder (2006), saying that in a marketing perspective there is not really a difference between acquired brands and internally generated brands.

Further, Tollington (2006) argues that if brand recognition is supported by a trademark then it is transactable, preferably using the word “transferable”. It is argued that the fact that it may be non-transaction based, internally generated, is irrelevant for the purposes of recognition on another, and equally valid, legal basis: trademarking. This is supported by Lev and Zarowin (1999); Tollington and Liu (1998). Further, Tollington (2006) argues that the prohibition of internally generated brands from IAS38 is an issue of asset measurement and the reliability thereof. This is in line with the perceptions of Tollington (1999) who states that the brand valuation technique becomes the basis for both recognition and measurement of the brand asset. As a result, Tollington (2006) means that the real question is whether a brand should be excluded from the balance sheet because of its measurement unreliability. This discussion is the same as brought forward by Seetharaman et al (2002), who described intangibles as difficult to value and very subjective, and also by Seetharaman et al (2002), who described numerous attempts to value intangibles over periods, resulting in problems. Hence, Tollington (2006) explains that this is a much broader issue concerning accounting as a whole, notably, between a stewardship view of accounting (favouring transactions) and an economic decision making view (favouring fair values), the latter being the trend over the past 20 years.

The debate on brand accounting has caused controversy and raised voices in many countries. Influences by the Anglo-American approach have given a touch of more relevance than reliability in forming the current standards by the IASB (Stolowy & Haller, 1996). Moreover, the area where this challenging relationship between relevance and reliability becomes highly obvious is in accounting for intangibles. Stolowy and Haller (1996) argue that intangibles, especially brands, have become increasingly important elements in the companies’ balance sheets. Therefore, the accounting demand for true and fair view becomes interesting to discuss. The different opinions on true and fair view are clearly shown. For example, Gröjer (2006) finds himself amongst those who believe that a true and fair view can not be created if it is not known exactly what a true and fair view really is. Further, Gröjer (2006) looks upon accounting as a construction of a reality rather than a representation of reality. This makes terms like true and fair view a bit complicated, if accounting is a representation of a construction. The problem is the term true and fair view. It is never clear which is the absolute correct way to do something. Moreover, Tollington (2006) agrees, stressing that truth and fairness are compromised through the absence of internally generated intangibles from the balance sheet, and that there is no absolute version of the truth. Finally, standing in contrast, Member of the IASB (2006) does not think the treatment of internally generated brands stands in contrast to the demand for true and fair view. Moreover, Drefeldt (2006) states that brand recognition of internally generated brand would stand in contrast to the true and fair view. Further, Drefeldt (2006) argues that it would be wrong to recognize internally generated brands on the balance sheet and it would certainly stand in contrast to the true and fair view as it would present the value on the balance sheet date. The company cash flow is still the most important (Drefeldt, 2006).

Concerning different national accounting views, Stolowy and Haller (1996) presented a study on the differences in brand asset recognition between France and Germany, pointing out some differences both in the definition of intangible assets and the recognition of internally generated brands. According to Artsberg (2003) there were several different opinions and critique in forms of comment letters in the formation process of IAS 38. This critique was, needless to say, in various forms from various countries. This brings a discussion of a comparison conflict. Tollington (2006) argues, from a recognition view, that there is a comparison conflict where some companies are disclosing brands and others do not. From a

measurement view many would argue that, as the brand value is extracted from purchased goodwill it is irrelevant as to whether one labels the disclosure as a brand or goodwill. Furthermore, Gröjer (2006) states that comparability is important. The question is whether the comparability is increasing or decreasing if the prerequisites are totally different. A very central criteria of accounting is comparability, everybody within accounting knows the importance of comparability. However, the question is how to obtain comparability if the prerequisites are widely different. Should the rules be applied in the exact same way? This is difficult. There is always the possibility to do exactly the same thing, no matter the context. But if some experience is acquired, knowing for example that a service company is not exactly the same as a manufacturing company, the differences are already here big enough to question whether there should be a general appliance or if there should be an adoption to the business in which the company exists (Gröjer, 2006). Another aspect on comparability is shown by Motameni and Shahrokhi (1998), stating that a global perspective on brand valuation would make brands more comparable.

5.3 Brand asset recognition

The introduction of the IAS 38 in all European countries is a step forward towards harmonized brand recognition. However, there are still different opinions on what is important regarding future brand recognition. According to Artsberg (2003) the main recognition criterion, that makes it difficult to recognize the internally generated intangible asset, is referring to the demand for identification or the demand for separability.

Tollington (2002) describes how the recognition of brands as assets can occur in three different ways and that the problem with brand recognition is clearly linked to the problems concerned with valuating brands. Tollington (2006) argues that there probably will not be any development regarding internally generated brands on the balance sheets as long as the attachment to transaction-based accounting is so profound. This also agreed by Brennan (2001) who argues that the current accounting framework is highly transactional and realisation based. However, Tollington (2006) argues, it has to do with more than just brands or even intangibles; it is a question of accounting itself.

The recognition of brands requires specific criteria stated in the IAS 38 (Epstein & Mirza, 2005). Seetharaman et al (2001) argue that there are some major problems with the IAS 38 that prevent brand assets from being recognized. As a result of the debate over the recognition of internally generated brand and acquired brands, the opinions on these matters vary significantly. Tollington (2006) argues that internally generated brands should be recognized on the balance sheets, as well as tangible assets. Member of the IASB (2006) supports this view, if the recognition of these assets can be supported with sufficient evidence. On the contrary, Drefeldt (2006) argues that internally generated brands should not be recognized on the balance sheet, which is in line with IAS 38 (Epstein & Mirza, 2005). The argument for this view is depending on the difference between internally generated brands and internally generated brands. Acquired brands can always be capitalized but it is more difficult with the internally generated brands. The costs can not be separated or measured with the certainty needed (Drefeldt, 2006). Gröjer (2006) stresses that brands should be recognized on the balance sheet if the costs are activated. When activating these costs, the judgement must also be that there is a future value. There are practical difficulties with separating current costs from new investments (Gröjer, 2006). This difficulty is also stressed by Seetharaman et al (2002), arguing valuation and isolation problems. Moreover, Gröjer (2006) realizes the difficulties with internally generated brands on the balance sheet, but, once again, the two

different systems used today are not preferable. There should be a general brand policy for all types of brands.

Tollington and Liu (1998); Tollington (2002); Henriksen and van Breda (1992); Lev and Zarowin (1999), among others argue that there is no difference between assets. Tollington, 2006 even states that, as earlier mentioned, the distinction between an internally generated brand and a purchased brand is artificial based on rules imposed by accountants. Thus, no difference exists. Further, Tollington, (2006) argues that the difference between brand assets relates to the issue of reliability of measurement. Member of the IASB (2006) means that the difference between an acquired brand and an internally generated brand is the evidence of a transaction to support recognition and measurement of an acquired brand. Maybe that is a market issue whether a distinction between acquired brands and internally generated brands should be made. If companies are willing to buy a brand from within a portfolio, e.g. from Procter & Gamble, they will sell this brand, and not sell the rest, then why shouldn't they be recognized? It seems like they are separate. And that is really the way that brands have gone in the last couple of decades, they are seen as assets and they could be sold off without selling off the entire company (Schroeder, 2006). Moreover, Member of the IASB (2006) states that it is a question of reliability of evidence: acquired brands involve an arms-length transaction between independent parties.

5.4 Brand valuation

According to Tollington (1999), brand recognition is depending on, and is more of a question of, brand valuation. Tollington (1999) does not see a problem with the recognition of internally generated brands. However, Tollington (1999) brings forward critique to the existing brand valuation methods. These are considered being insufficient. This is also supported by Kumar (2005), who argues that the present valuation framework of intangibles is not satisfactory, that such assets can not be valued with reasonable certainty. A perspective brought forward by Schroeder (2006) is that brand valuation is dependent on how much is meant to be measured. The stock market is a measure of brand value, where investors determine the value. However, some listings on the stock exchange are not exactly what the brand is.

Seetharaman et al (2001) state that the norm-setting bodies have been uncertain how to solve the brand valuation problem. The explained uncertainty associated with brands and the confusion about the distinction between brands and other assets leads to problems when deciding how to measure and report such assets. This uncertainty is also explained by Drefeldt (2006), who states that there are those who believe that intangibles, especially internally generated brands, can not be recognized because the value of such assets can not be measured with reasonable certainty. When there is nothing to measure from, there is no possible recognition. This important aspect of brand recognition, that the brand can be valued with reasonable certainty, is supported by Motameni and Shahrokhi (1998). Today there are different brand valuation methods to use by companies. The different methods for brand valuation lead to brands being valued differently among companies in different countries and this may lead to a comparison conflict. Motameni and Shahrokhi (1998) argue the importance of a global perspective on brand valuation in order to make brands more comparable. Further, Seetharaman et al (2001) also argue the importance of global standardization principles regarding brand valuation. It is stressed that there must be a globally accepted brand valuation method, to be used by all companies.

Regarding a global valuation method, Drefeldt (2006) states that the important thing is the transparency; that the companies show how the valuation was made. The method itself is not that important, but in theory one should always use the discounted cash flow (Drefeldt, 2006). According to Schroeder (2006), it would make sense to have a general international valuation method if brands are a big part of the accounting standards. However, it will probably take some time until such brand valuation methods are formulated. Tollington (2006) argues that there in principle should be an international valuation method but that there is a question of availability of information. Further, Member of the IASB (2006) thinks that an international valuation method would be a good idea to increase the comparability of brand assets. This view is also partly supported by Gröjer (2006) who believes that some idea of which costs that an activated brand should consist of, is necessary. However, Gröjer (2006) feels that this is a difficult question and points out the problem that if the value is to be revised there is need for an accounting prerequisite. The value itself can not be the prerequisite; it must be the process that has resulted in a certain value.

5.5 Towards the future of accounting for brands

Tollington (2006) stress the importance of the recognition of internally generated brands on the balance sheet. If such assets are not recognized, Tollington (2006) questions the accounting profession as a whole. Schroeder (2006) sees a future where there probably will be more virtual brands, brands that exist almost independently from distribution channels and factories. The brand will become more like money, as an exchangeable object. Therefore, it will be just the brand or this entity which could be bought and sold.

Tollington and Liu (1998) argue that the treatment of intangibles, such as brand assets, must be revised to also include internally generated brands on the companies' balance sheets. Therefore, as brand equity also often accounts for a major portion of shareholder value, the importance of brands and other intangibles becomes obvious. Motameni and Shahrokhi (1998) also state that the brand is to be seen as a valuable asset.

Gröjer (2006) sees a future where the accounting practice may be further separated from the analysts. Such development would result in more work for the analysts to gather information to a larger extent. Nurton (2001) describes how analysts in the UK demanded more information about brands and a majority wanted to see internally generated brands on the balance sheets. Member of the IASB (2006) believes that brands will be recognized more often in the future due to the confidence in measurement techniques. However, it is unlikely that all brands will meet the recognition and measurement criteria. Tollington (2006) is more uncertain about future brand recognition, meaning that the accounting profession itself is opposed to the recognition of internally generated brands on the balance sheets. As a result, Tollington (2006) believes that nothing will probably happen in the future within internally generated brands since the attachment to a transaction-based accounting is so profound and longstanding that one can not see a development of valuations-based accounting independently of it. Moreover, Tollington (2006) argues that the valuation of brands seems to be the heart in the question of internally generated brands. Drefeldt (2006) does not think that internally generated brands will be allowed on the balance sheets within the next three years, meaning that it is to a complex question to be dealt with.

The value of market capitalizations in the world will continue to grow with the ongoing shift from product-based companies to service-based industries. This leads to more intangibles on the balance sheets and definition problems along with the IFRS 3 on intangibles. The problem

is that there is no control over some intangible assets over a certain period of time, for example customer relations (Drefeldt, 2006).

Lev (2001) points to the serious deficiencies in the current accounting system. Further, Seetharaman et al (2002) stress the fact that many company leaders have criticized the accounting and financial reporting system. Further, the view from accounting professionals on intangible assets can be looked upon as negative. The costs for many of the intangible assets are not seen as investments. According to Lev (2001), current accounting standards fail to capture some of the intangible assets.

Drefeldt (2006) looks upon the IAS 38 as generally formulated and that it has not been developed fully. However, Drefeldt (2006) thinks that the regulation for internally generated brands is enough and does not see any further development on this issue. However, there is a need to look deeper into the development of the IAS 38 in general as it contains several areas that need to be developed to meet the reality. Gröjer (2006) stresses the point that the IAS 38 is such a compromise and therefore it is too restrictive. Gröjer (2006) believes that there is already a project running today to revise the IAS 38. Member of the IASB (2006) stresses that there are other priorities to be dealt with, prior to the development of the IAS 38, but that the IAS 38 should be reconsidered eventually. Tollington (2006) puts it; the IAS 38 is not good enough but the question is much broader, concerning the accounting itself. Moreover, Drefeldt (2006) gives the opinion that nothing is permanent concerning the formation of IAS 38 and that it is constantly developed. In doing this, there should be a certain amount of conservatism because of the difficulties concerned with valuating brands.

6 Conclusions

In this chapter the conclusions from the empirical and theoretical analysis are drawn. In this part, the thesis is linked back to the purpose and the research questions presented in the problem statement are answered. Further, some own reflections on the subject are provided.

6.1 Why is an asset not an asset?

According to IAS 38, it is not possible to recognize an internally generated asset, such as a brand (Epstein & Mirza, 2005). The arguments are that the asset can not be derived from a transaction or an event. Another problem is the notion of separability or identifiability. Further, Gröjer (2006) there is no market based transaction, as for an acquired brand, to help validate the asset. Moreover, there are serious deficiencies in the measurements and valuation techniques which are in need of further development and harmonization. Further, von Colbe et al (2005) describe the insecurity on the measurability of intangibles, which makes recognition difficult.

The brand is a valuable asset for the firm owning and controlling the brand. It is clearly shown that brands are the primary capital of many businesses. The measurement of internally generated brand assets is the key issue why such assets still are not considered assets in accounting practices. Tollington (2006) states that the most important factor for determining and recognizing brand assets is the reliability of measurement. This, in combination with the lack of a transaction found in acquired brands, explains why the internally generated brand is not considered an asset.

Schroeder (2006); Tollington (2006) argue that internally created brand assets carry the same value as acquired brand assets. However, if there is no initial expense or no transaction, there is no recorded market value. And without a market value, internally generated brands can not be recognized on the balance sheet.

6.2 Should internally generated brands be recognized on the balance sheet?

The lack of internally generated brands on the companies balance sheets have caused debate, showing different perceptions on whether such assets should be recognized in the balance sheets or not. According to Gröjer (2006) the question is complex. However, the distinction between acquired brands and internally generated brands systems regarding brand recognition used today is not preferable. Member of the IASB (2006) argues that internally generated brands should be recognized if there is sufficient supporting evidence. Schroeder (2006), being a marketer, sees no difference between brand assets and therefore should also internally generated brands be recognized. Drefeldt (2006), on the other hand, argues that internally generated brands should not be recognized because such brands can not be measured. Tollington (2006) states that internally generated brands should be recognized since the rules opposing brand recognition are imposed by accountants. Schroeder (2006) agrees, referring to the non-existing difference between acquired brands and internally generated brands from a marketing perspective.

The respondents are clearly in favour of recognition of internally generated brands. This is supported by research on internally generated assets being just as much assets as tangible

assets (Lev, 2001; Lev & Zarowin, 1999; Henriksen & van Breda, 1992). However, the perception that this is a complex question is common. There is a tendency towards that the internally generated brands should be recognized, but the question is how.

6.3 Should there be a harmonization towards one global brand valuation method?

Brand recognition is more than just the debate over internally generated brand and acquired brands. According to Tollington (1999), brand recognition is depending on brand valuation. Tollington (2006) argues that the most important question is whether a brand should be excluded from the balance sheet because of its measurement unreliability. Motameni and Shahrokhi, (1998); Seetharaman et al (2001) argue the importance of global brand valuation principles to make brands more comparable.

Many voices argue that there should be an international brand valuation method (Tollington, 2006; Member of the IASB, 2006; Schroeder, 2006). This is believed to increase the comparability of brand assets on an international level. Internally generated brands can only be recognized on the balance sheet if an international method of brand valuation is recognized. Still, there are different definitions of brand assets and different opinions on how to value brands. When there is harmonization regarding brand valuation then internally generated brands can make their way to the balance sheets.

Drefeldt (2006) argues that the big problem with internally generated brand is that they can not be measured with certainty. However, Drefeldt (2006) does not see a need for a global brand valuation method, arguing that the method itself is not important, it is that the companies show how the valuation was made that counts.

6.4 Own reflections

The accounting profession displays reluctance towards recognizing brands on the balance sheet. It seems irrational not to recognize internally generated brand assets, while recognizing purchased brands. In fact, they bear the same value to the firm and it is of paramount importance to communicate that to users of financial statements and balance sheets.

Clearly there are contrary views about the directions in which accounting and financial reporting will develop. There are increasing criticisms of traditional accounting methods, which are said to look backwards and at tangible assets only. Therefore, most certainly, a need for a more suitable recognition and reporting of intangible assets is obvious. The current accounting system gives intangibles an incomplete treatment, leaving some highly important intangibles out. Thus, a risk of mismanaging these assets arises.

The need for an international brand valuation method seems obvious to ease the comparability and in the end the recognition of internally generated brands. The general opinion seems to be that a global valuation method for brands is necessary to be able to recognize internally generated brands. The most important question is whether brands, including internally generated brands, can be measured with reasonable certainty. It is easier to value acquired brands since such assets have a market value. Today there are several different methods used to value a brand but the certainty can not be guaranteed in none. As long as the internally generated brands can not be measured with the reasonable certainty, and there is a method

used consequently by all international companies, internally generated brands will probably not make their way to the balance sheets.

Accounting for intangible assets remains one of the biggest challenges facing accounting with significant economic consequences. The issue is very complicated and will require input from not just standard setters, but also academics and industry. The future of intangibles, such as brand assets, is not clear. This thesis has aimed to provide information to engage in educated debate on this issue, as it is only through such debate including professionals and norm-setting bodies that a resolution to this issue will be found.

7 Further research

In the last chapter, the suggestions for further research within the subject are provided. There are many interesting areas that can be investigated taking on a different perspective and making other choices than presented in this thesis.

7.1 Suggestions for further research

This thesis has scrutinized the problems with internally generated brands on the balance sheet. It is delimited to the accountants' and the marketers' perceptions on these issues. However, there are of course other interested parties that are interested in the development of brand accounting.

It would be attractive to bring forward a discussion, what it would mean for companies to recognize their brands on the balance sheet. This could be done by further looking into the comments on the accounting standards made by some companies, and by interviewing international firms. It would be highly interesting to conduct some type of research scrutinizing the comment letters on the exposure drafts (E50) on IAS 38. These comment letters vary in critique and they come from different norm-setting environments and countries. Do these companies prefer recognition of internally generated brands and intangible assets? Furthermore, are companies willing to fully accept IAS 38, bearing in mind that if companies do not accept all standards required according to IAS 1, then financial statements should not be described as complying with IAS, unless they comply with all the requirements of each applicable standard? The opinions of the companies are as interesting as the ones of marketers, accountants and analysts. It would be of both common and legal interest to find out what such research could add to the debate.

If investors misprice several companies in the market place, as a result of the lack of some intangible assets on the balance sheet, then it would be interesting to conduct both quantitative and qualitative studies on these issues.

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