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Dear Mr Keys

Discussion Paper: Initial Accounting for Internally Generated Intangible Assets

Grant Thornton New Zealand Limited (Grant Thornton) is pleased to submit its comments on the National Standards Setters Discussion Paper *Initial Accounting for Internally Generated Intangible Assets* (the DP).

Grant Thornton's response reflects our position as auditors and business advisers both to New Zealand listed companies and privately held companies and businesses, and this submission has been prepared in collaboration with Grant Thornton Australia Limited, has benefited with input from our clients, and discussions with key constituents in New Zealand, and globally.

Having read the DP our view is that this document falls more into the category of a research paper, rather than a discussion paper because it did not ask for comment on specific issues but just the topic generally. Going forward, our recommendation is that if a document is to be labelled a discussion paper, then a series of specific questions should be included because they will signal to respondents where input is most needed by the standard setter(s).

Below are our comments on issues that we believe are most relevant to this debate.

Active monitoring

While accounting for internally generated intangibles is not as yet on the work program of the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB), we support on-going research along the lines of this DP because for many "new" industries internally generated intangibles not only have the potential to be, but already are, a significant component of their financial statements.

Our suggestion is that the excellent research and background contained in this DP is now actively kept up to date by the Australian Accounting Standards Board (AASB) on behalf of the National Standard Setters to keep it in-step with not only the IASB's *Framework*, but also other significant joint IASB and FASB projects such as the on-going work currently being undertaken on *Revenue Recognition*. In this regard, our view is that debate as to the appropriate accounting for internally generated intangibles must always be considered a sub-set of accounting for all intangible assets and great care should be taken not to view this topic as the reason for another "carve-out" because of the recognition and measurement challenges that surround it.

Cost-benefit analysis

We note the acknowledgement in the DP that a more detailed cost-benefit analysis needs to be conducted and as part of this analysis, Grant Thornton believes that it would be useful, and would actively support, comprehensive field tests to validate the various proposals raised in the DP. We see this testing as particularly important given that internally generated intangibles will very rarely have the benefit of a market transaction "to anchor" its carrying value (c.f. a business combination).

The sections of the DP that deal with Recognition (Chapter 3) and Measurement (Chapter 4) provide an alternative between a valuation model and a cost model. We believe that it is too early in the research process to offer a definitive opinion as to the better model to follow. However, we do observe a real tension between them. We note that many current IASB and FASB projects trending towards the use of fair value on the basis that both Boards believe this basis of accounting provides more decision useful information. However, we see this objective is now being challenged by an increasing number of preparers of financial statements because they want accounting policies that will keep their compliance costs to a minimum and the benefits of obtaining fair values has yet to be demonstrated. Given this they support the cost model simply because it ultimately deals with amounts that can be reliably measured, and readily audited.

Disclosure

In the absence of robust and comprehensive field test results, it is our view that right now, the best way to progress an improvement in the accounting treatment for internally generated intangibles is via the disclosure route. This could be implemented in a relatively short period of time, and would enable entities to provide appropriate basic disclosures where the existence of such items is significant. If this approach were taken we believe it would be very helpful to know if the amounts disclosed were sourced from either internal valuations, external valuations, or a combination of both, and why the entity believed it was important to provide this information. Even though paragraph 128 of IAS 38 *Intangible Assets* encourages disclosure of all internally generated intangible assets, there is a decided lack of guidance on how to go about doing this, probably because there is a perception it may be seen by some as undermining the current requirements of the existing standard. This is unfortunate and illustrates why we believe National Standard Setters should continue to actively support this initiative.

Closing remarks

We concur with the conclusion noted in the foreword of the DP prepared by the Chairman of the National Standard Setters that "... the paper makes a significant contribution to the literature on accounting for intangible assets" because it has identified a diverse range of views, each with their own strengths and weaknesses.

We also agree with the DP's final conclusion (paragraph 258) that "consistent with the recognition and disclosure principles in the Framework and the IASB's standards, [that] disclosure is not an adequate substitute for recognition". Notwithstanding this, we encourage the AASB and other National Standard Setters around the world to more actively promote disclosure of internally generated intangible assets as a pragmatic interim step because as noted above, for some entities, restricting the recognition of internally generated intangible assets is a source of frustration with current IFRS.

If you have any questions concerning our comments or require any further information, please contact Mark Hucklesby in our Auckland Office on +64 (09) 308 2534.

Yours sincerely
Grant Thornton New Zealand Limited

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