

INTANGIBLE ASSETS DISCLOSURE PRACTICES- A LITERATURE REVIEW

Dr. MANDEEP KAUR*
Ms. KRITIKA**

ABSTRACT

Intangible assets are the key driver to achieve the sustainable competitive advantage in the twenty first century. Now- a-days, Most of the businesses have much dependence on the Intangible assets rather than tangible assets in order to create wealth for the long period. The purpose of the paper is to review the literature relating to Intangible assets in relation to identify the gaps and to determine the extent of Intangible assets disclosure. Researcher observed that the overall disclosure level is of low level and unsystematic. Researcher suggested that there is need to establish a general accounting framework for managing, measuring and reporting the Intangible assets.

INTRODUCTION

Intangible assets are the hidden and invisible assets that are used for achieving the sustainable competitive advantage. According to Indian Accounting Standard 38 (Ind AS 38), Intangible asset is an “identifiable non-monetary asset without physical substance”. Hall (1992) states that Intangible assets are value drivers that transform productive resources into value –added assets. The twenty first century's economy is knowledge based economy where Intangible assets play an important role to create wealth for the economy. In this economy, the investment of the Intangible assets (patents, copyrights, brands, information technology, worldwide customer base and many more) are much more important than the Tangible assets (land, labour and machinery). But the traditional model of accounting based on double entry accounting system is incapable to manage, measure and report these hidden assets. There is an immediate need to establish a common accounting framework to managing, measuring and reporting the unrecognized Intangible assets.

OBJECTIVE OF THE STUDY

Based on the above rationale, this study is conducted to review the prior literature on the Intangible assets with an objective to identify the gap and to determine the extent of Intangible assets reporting practices. Specifically it deals with to review the studies related to Intangible assets reporting particular of a) Indian companies b) Foreign companies c) Comparative studies.

REVIEW OF LITERATURE

There existed vast corpus of literature on the Intangible assets. The terms Intangible assets, Knowledge based assets and Intellectual capital have been used interchangeably

*Assistant Professor, Punjab Technical University, Kapurthala

**Research Scholar, Punjab Technical University, Kapurthala

assert that they differentiate with their nature of stream like Intangible assets in accounting literature, Knowledge based assets by economists and Intellectual capital in management practices (Lev 2001, Rodgers 2003). For the purpose of the review, this study is divided into three sections. Section-I deals with the Intangible assets study relating to Indian companies. Section-II deals with the Intangible assets study relating to Foreign companies. Section-III focus on the comparative analysis with an aim to highlight the difference in Intangible assets disclosure practices of the companies operating in different economies.

(a) Intangible assets study relating to Indian companies

Pablos (2005) examined the main similarities and differences between the Indian Intellectual capital report and European Intellectual capital report and also made an attempt to know the idiosyncratic features that define the Indian Intellectual capital report. He found that Indian Intellectual capital report does not focus on the business model, values, mission and vision and/or Knowledge management issues like European intellectual capital reports. Indian companies present a narrative style reporting that describes a firm's intellectual capital and analyzed the components without focus on the specific indicators. Researcher concluded that Indian reports do not combine the narrative and quantitative style and also much larger than the European intellectual reports.

Kamath (2008) studied the relationship between the Intellectual capital components like human capital, structural capital and physical capital with the traditional measures of performance of the company such as profitability, productivity and market valuation by selecting 25 leading Indian Pharmaceutical companies from the year 1996 to 2006. The research indicated that domestic firms were seen to be performed well and efficiently utilizing their IC as per the VAIC ranking. The researcher found that Human capital has the major impact on the profitability and productivity of the firm over the period of study. Study revealed no significant relationship between the dependent variable (ROA, MB and ATO) and the Independent variable (VAIC). Researcher concluded the study by recommending that there is an immediate need to start up the voluntary disclosures of IC so that the negative perception among the stakeholders regarding value creation in the firm may get even more transparent.

Joshi and Ubha (2009) conducted a study on the Intellectual capital reporting practices of 15 leading Indian Information Technology companies. The researchers found that only 14 items out of 39 items were disclosed in annual reports by the companies. The term Intellectual Property had the maximum disclosed item and Infosys technologies limited was the company who had disclosed maximum number of items (13) from the total list of 39 items. They found negligible disclosures in the annual reports. Thus, Indian companies are also lagging behind in the field of measurement, reporting and disclosure of intellectual capital.

Chandra and Mehra (2011) assessed the extent of Intangible assets disclosure of the Indian companies for the year 2003-04 and 2007-08. Study found that number of employees, market share and research activities were most disclosed attribute in the case of Human capital, External capital and Internal capital respectively. Infosys Technologies

Limited was top company for disclosing the intangible assets for the both of the years. Study found significant difference in the Intangible assets reporting practices of the companies in the year 2003-04 and 2007-08. Researcher concluded the study by saying that there is a need to develop an index of intangible assets disclosure to incorporate both quantitative as well as qualitative description of intangible assets. The overall reporting of intangible assets was unorganized and unsystematic.

Singh and Kansal (2011) explored and examined the voluntary IC disclosures and variation in top 20 listed pharmaceutical companies in India by using the content analysis of the annual reports for the year 2009. Study showed significant variations in the IC disclosure by top 20 pharmaceutical companies. External capital was the most disclosed category. These findings were consistent with the previous research in China. The computed figures of the IC revealed that the huge value of IC remains unreported in the Balance Sheet. The overall IC disclosure was drastically low.

Bhasin (2012) analyzed the IC related information of 16 top IT sector companies of India, for the year 2007-08 and 2008-09 by using content analysis of annual reports. Study found that Intellectual property rights (IPR) was the most disclosed item of IC and Infosys Technology Limited was widely disclosing company of IC related items. However, it was interesting to note that this company did not make any mention of term 'IC' in its annual reports for the year 2007 to 2009. Study revealed significant variation in Item wise disclosure in the annual reports of the companies. Researcher concluded the study by recommended that companies must create a culture that emphasizes the importance of IC in achieving the business advantage. From the above studies, the researcher observed that there is enough awareness among the Indian companies relating to the theme of Intangible assets. But the overall disclosure level is low because of the reason of the lack of established and generally accepted Intangible assets reporting framework.

(b) Intangible assets study relating to Foreign companies

Guthrie and Petty (2000) examined the annual reports of 20 Australian companies to measure the extent of Intellectual capital reporting practices for the year 1998. In an Irish study, **Brennan (2001)** examined the voluntary Intellectual capital reporting practices of the 11 knowledge based Irish listed companies for the year 1999. **Bontis (2003)** conducted a study on the Intellectual capital disclosure practices of 10000 Canadian Corporations by employing content analysis. **April, Bosma and Deglon (2003)** examined the measurement, reporting and management practices in the 20 South African mining industry. **Goh and Lim (2004)** examined the extent of intellectual capital disclosure of 20 profit- making public listed Malaysian companies for the year 2001. They found that the incidence of IC disclosure information in the annual reports was highly qualitative instead of quantitatively in the financial statements. **Oliveras, Gowthorpe, Kasperskaya and Perramon (2008)** conducted a study on the intellectual capital reporting practices of 12 Spanish companies over the period from 2000 to 2002. **Xiao (2008) analyzed the annual reports to determine the extent of IC disclosure in China for the year 2007. A common finding of all above studies has been the inadequacy of IC disclosure irrespective of what model was used to study such disclosures. These studies found that Intangible assets disclosures are highly qualitative rather than**

quantitative.

Pablos (2002) explored the dynamics of measuring and reporting IC in pioneer forms in Asia, Europe and the Middle East. Study showed that there is an increasing interest in the measuring and reporting of their valuable intangible resources. Study found that in initial stage, firms try to experiment with the elaboration of IC accounts, after the publication of first ICR, the following year publish a new intellectual capital report too. Study suggested that successful firms are those which routinely maximize the value from their Intellectual capital.

Abeyesekera and Guthrie (2005) examined the annual reports of top 30 Sri Lankan listed companies to measure the trends of Intellectual capital from the year 1998/1999 and 1999/2000. The results of study indicated that firms in Sri Lanka reported an overall increase in all categories of IC. The most reported category was external capital over 2 years. The study revealed that firms in Sri Lanka emphasized intellectual capital and has covered a wide range of intellectual capital items. The overall increase in intellectual capital indicates that reporting was proactive rather than reactive, and can be explained by the political economy of accounting theory.

Meca (2005) conducted a study in the year 2000 and 2001 to analyze the information concerning intellectual capital disclosed in presentations to analysts held by Spanish firms is relevant for financial analysts when they take their investment decisions. The findings showed that the items like strategy, customers and processes are highly relevant in the meetings as well as in the valuation tasks by the financial analysts while taking decision-making. Innovation and R & D was least disclosed because companies might have some risk of future litigation due to releasing information which could be beneficial to competitor.

Liang and Lin (2008) examined the value relevant information provided by Intellectual capital (IC) beyond the financial performance under different life-cycle stages from the year 1998 to 2003. Empirical results indicated that overall IC provided the most value relevant information in the stagnant stage and the lowest value relevant information into the growth stage. Study revealed that the evaluation of the company should not be limited to financial performance; instead, there should be a thorough review of IC.

Bruggen, Vergauwen and Dao (2009) examined the determinants that influence the decision to disclose Intellectual capital in annual reports. The researcher found that Structural capital was the most frequently disclosed category and Intellectual Property was the most frequently disclosed element. Study revealed that health care Industry and firms of Information Technology industry discloses significantly more on IC compared to other firms. Further results suggested that size of a firm has an influence on the level of IC disclosure. Results found that the level of IC disclosure is not related to the level of Information asymmetry.

Anam (2011) examined the effects of IC information disclosed in the annual reports of 91 listed companies on Bursa Malaysia on their market capitalization. Results showed that extent of IC disclosure in the annual reports for the year 2006 was slightly higher compared to the year 2002 which indicates that overall financial performance of Malaysian listed companies in 2006 was better than 2002. MCAP, NP, BV, SIZE was higher in 2006

compared to 2002, but leverage had decreased in 2006. The results revealed that the extent of IC disclosure can be considered as a predictor of MCAP.

Nurunnabi, Hossain and Hossain (2011) assessed the extent of ICR in annual reports of 90 listed companies in Bangladesh from 13 industry groups in the year 2008-09 by conducting the content analysis. The results of the study indicated that there is lack of ICD practices by the firms (54% of the sample companies disclose within the range from 5.8 % to 10.6%). Overall, the study also revealed that firms with greater size (total sales) provide more ICD in their annual reports than other corporate attributes. The pharmaceuticals industry disclosed the most IC information among 13 industries covered by the sample.

Fadur, Ciotina and Mironiuc (2011) examined the extent of Intangible assets related information in Romanian companies quoted in Bucharest Stock Exchange and also revealed the difference existing between the market value of the company and its net accounting value as a result of the existence of Intangible asset. The findings indicated that a low degree of dissemination of the information on Intangible assets in Romanian companies and the differences between the market value and the accounting value was explained in accounting relating to the investor's confidence but not based on the Intangible asset.

Ferreira, Branco, Moreira (2012) analyzed the various factors that influence the intellectual capital disclosure using the cost/benefits framework in the year 2006. The research found that External capital was the most disclosed category and Management processes was the most disclosed element. Study revealed that there was significant relationship between the size and type of auditor whilst no significant relationship between Leverage, Profitability, Ownership Concentration and Intellectual capital in explaining Intellectual capital disclosure.

Omoye (2013) investigated the various factors that can influence Nigerian companies to disclose the Intangible assets in their annual reports of 65 Nigerian companies from the year 2006 to 2010. The researcher found that the disclosure of Intangible assets were weakly associated with the companies in service oriented industry, company without foreign activities, less profitable firms, firms that uses big-audit firms, older firms but highly significant to firms with debt stakeholders in Nigeria.

Castro and Benetti (2013) examined the impact of Intangible assets on the market value of the firm. They proposed a model for computing the Intangible assets that are not shown in balance sheet. The 30 companies were selected for the study listed on the Sao Paulo Stock Exchange. The model revealed that the possible existence of relevant Intangible assets was not recorded in the companies. Study suggested that higher the recording of Intangible assets, smaller will be the difference between the book value and market value of the firm. Researcher expected that in the future the recording will be allowed or at least, the disclosure of the fair value of internally generated Intangible assets will be mandatory.

From the above studies, Researcher observed that there is high level of unrecognized Intangible assets. There is an immediate need to generate Intangible assets reporting practices so that the negative perception among the stakeholders may be reduced and they can get more transparent information.

(c) Comparative studies

Pablos (2003) analyzed the intellectual capital reporting practices in Spain and compared the study with Dutch and Swedish counterparts. Study found that Spanish companies do not compare favorably with their Dutch and Swedish counterparts in building Intellectual capital reports. In Spain, the banking sector was significantly ahead in measuring and reporting the Intellectual capital.

Vergauwen and Alem (2005) investigated the current IC disclosure practices in three European countries namely France, the Netherlands and Germany. The research indicated significantly higher average disclosure number in French annual reports as compared to Dutch counterparts. The German is in between but is not significantly different from both countries. There was much larger disclosure number compared to the results of Bontis, who used exactly the same research in Canada, but this phenomenon has some bias when comparing the result of Bontis (2002) research. The researchers found not only that voluntary IC disclosure significantly differs from these countries, but also that this difference might be explained by country- specific regulation and auditor conservatism.

Guthrie, Petty and Ricceri (2006) made investigation on the voluntary reporting of intellectual capital (IC) by listed companies in Australia and Hong Kong and also evaluated size, industry and time effects on IC disclosure levels. The researchers found that the level of voluntary IC disclosures was low and in qualitative rather than quantitative form in both locations. Study revealed that disclosure level was positively related to company size, this finding was consistent with the previous literature on voluntary reporting that was held in Australia for the year 1998.

Joshi, Ubha and Sidhu (2012) compared and analyzed the IC disclosures made by top 20 Indian and Australian information technology companies for the year 2008. Indian IT companies disclosed 21 items whereas in comparison Australian IT companies report only 14 items. Intellectual property was the most disclosed item in the both of the countries. Study found that Australian companies are making lesser disclosures than Indian companies. Despite these differences IC disclosures by companies in both countries remain relatively low.

Sonnier (2008) compared the extent of Intellectual capital disclosure of firms in the high technology and traditional sectors of the economy. The results showed that HTCs had a significantly higher level of ICD than TSCs for each category of the RBV IC model with the exception of supplier capital in both 2000 and 2004 years. Regarding the level of supplier capital disclosure, the data were inconclusive. HTC may be motivated to provide disclosures of their IC in the narrative portion of their annual reports due to the failure of the financial accounting model to account for the same in the financial statements.

An observation from the literature studied that comparative analysis of Intangible assets disclosure practices by companies from different economies also did not report much variation in the level of disclosures between developed and developing countries.

CONCLUSION

The aim of the study to review the literature in relation to Intangible assets disclosure used to identify the gaps and also to determine the extent of Intellectual capital disclosure. Study found that there is enough awareness regarding the theme of the Intangible assets, but still the overall extent of the disclosure practices is low in relation to the Indian as well as Foreign companies. Further study observed that different countries are not report much variation in relation to level of reporting between developed and developing countries. The reason of unsystematic and unrecognized level of disclosure is the lacuna of the general accounting framework relating to the Intangible assets reporting practices. There is a need for the revised general accounting guidelines that is useful for the companies to disclose their hidden assets in their annual reports which is beneficial for achieving the sustainable competitive advantage. Also it is useful for the stakeholders to take the efficient decisions by considering both the tangible as well as intangible assets.

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