Intangible assets: what is the true value of your business?

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Abstract— The true value of a business can only be valued if the intangible assets are understood and well recognized, this is especially due to the huge difference they bring to the business. From an intense research about the huge impact that the intangible assets add to the true value of the business, it therefore forms the fundamental of this paper, which outlines in details the value it brings to the business. The paper clearly differentiates between the intangible assets and the tangible assets, the various methods of evaluating the intangible assets, the intangible assets evaluation that can be done through comparative analysis, elimination method, scenario analysis and converting them to money. The intangible assets are measured using various methods like cost model and the evaluation model. The paper also outlines the performance of the intangible assets within the business. For instance, the artificial intelligence will help in making sure that the business is performing well by being more competitive and so much more; therefore, there is a great opportunity behind the value of intangible assets in determining the true value of your business.

1 Introduction

Intangible capital is not physical in nature but the benefits accrued from it are significantly visible. It is proper to call it a background financier of a company as its provide lots of benefits and potential revenue yet it is rarely recognized. Intangible assets mostly include intellectual property like patents, trademarks and copyrights. Others are goodwill, brand recognition, franchises, computer software and customer satisfaction. Intangible capital can either be created or acquired 1 (Axtle-Ortiz, 2013). When it is acquired, it means that it has been bought from another entity like a franchise or patent. Only the acquired intangible assets are recorded on the company's balance sheet.

2 Intangible capital

Intangible assets can also be of an indefinite or definite lifecycle. Definite intangible assets are amortized to appear as amortization expenses in the books of account while the indefinite is assessed over their infinite lifespan. There is difficulty in assigning value to intangible capital due to the uncertainty of the quantity and value of benefits that it may provide overtime. Internally developed or created intangible assets do not appear on the balance sheet since they are uniquely part of the company's creation and there is no market price that can be used to compare them with 2 (Dumay & Garanina, 2013). Hence most companies make enormous gains with their created intangible assets.

Intangible capital can be much more valuable than tangible capital in most circumstances. There are factors that may decrease or increase the value of an intangible asset. A merger or acquisition will increase the value of the predators' intangible asset and decreases that o the prey. When intangible assets are converted to tangible assets, their value also decreases. In the case of finite intangible assets, their value decreases as their life time approaches expiration. Some intangible assets like patents may be subject to capital gains income depending on their type 3 (Eisfeldt & Papanikolaou, 2014). Licensed patent income does not get capital gains while the sales of patents income provide capital gains.

Intangible capital is difficult to quantify and evaluate due to its immateriality trait. There are different forms of intangible benefits some of which are new and continue to manifest in different ways like the internet domains and services, blue prints and manuscripts. These intangible assets did not exist

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previously when standards for evaluating intangible assets were being made. International accounting standards(IAS) has many guidelines for valuation of intangible assets but these assets keep evolving overtime. There are some intangible assets that go unrecognized and thus not valued yet they create tremendous benefits for the companies.

3 Evaluation

Intangible benefits are of high risk and their value changes frequently. This makes it very difficult to attach a specific value to intangible capital over its lifespan. Their values may take an upward or downward slope during their life time depending on the prevailing circumstances and market changes. Therefore, intangible capital requires constant reevaluation. Mostly preferred is an annual basis of reevaluation. Evaluation of intangible capital helps in the planning and budgetary processes of a company. All the benefits and losses that are expected are accounted for properly 4 (Greco et al., 2013). This means that the numerous variations that between standard and actual costs can be reduced or minimized.

One method used in evaluation of intangible capital is comparative analysis. Comparative analysis is mostly used in the valuation of assets whose fair market price has already been determined. Intangible assets without a predetermined fair value cannot be evaluated using comparative analysis.

Under this method, a company compares its intangible benefits with that of intangible assets that have a fixed price or value. Intangible assets such as goodwill and patents can be evaluated using this method. An example is when a company acquires a patent for the business and needs to know the value or worth of the patent. If the owners are interested in selling the patent, they can use the existing sale prices of patents to gauge the value of their patent. The company may not want to sell the patent but is just interested in knowing the value 5 (Hamilton & Liu, 2014). In this case, the management can take a look at the existing market prices for patents and know its monetary worth.

Elimination process is also a useful method for evaluating intangible capital. Just as the name says elimination takes some form of picking out tangibles cost and benefits in order to remain with the intangibles. Tangible and intangible benefits are miscible and so elimination process simply applies the rules of separating miscible elements. When evaluating the intangible capital, first measure the total gains. After valuation of the total gains or benefits, tangible benefits are subtracted from this value 6 (Peters & Taylor, 2017). The difference between the total benefits and tangible benefits is assumed to be the intangible benefits Elimination simple applies the principle of removing the tangible capital from total capital in order to remain with Intangible capital.

Scenario analysis can also be used in the evaluation of intangible capital. This method takes more of a speculative and predictive form to quantify intangible capital. Scenario analysis deals with the efforts of trying to determine the value of an uncertainty. In this method, managers try to examine the possible outcome of a specific action in terms of the likelihood of bearing intangible benefits. If the curse of action results in certain benefits, all other factors are quantified and any other unplanned for benefits became the intangible reaped from the particular course of action. A good example for scenario analysis is when companies try to evaluate the outcomes of their research and development. If sales increase as result of research and development the company will try and look at all possible causes of increase 7 (Sydler et al., 2014). After an analysis of the possible drivers of sales, if they are still other benefits, all credits will go to research and development. Therefore, through this scenario, the company is able to evaluate the benefits brought about by research and development.

Another possible way for evaluating intangible capital is by converting it to money. This conversion is assigned to experts who have vast knowledge and experience in the valuation of intangible capital. People who can be trusted to attach an estimated material value to intangible capital. This method is not very famous because of the fact that it may be subject to the bias by the expert. There is the possibility of a lesser value being attached to intangible capital du to lack of a precedent price and human error 6 (Peters & Taylor, 2017).

4 MESUREMENT OF INTANGIBLE CAPITAL

Measurement of intangible capital can be done through various ways according to the provisions of the international accounting standards (IAS 38). It can be initially measured at cost using the cost model. Before measurement through the cost model, there has to be recognition of the intangible asset. Identify whether it is an indefinite or finite asset. After initial recognition, IAS 38 requires that the intangible assets be measured at cost minus the accumulated amortization expenses and impairment costs.

Revaluation model of measuring intangible capital is different from the cost model. The differentiating factor is that the revaluation model is based on the fair value of the of the intangible asset whereas the cost model focuses on the initial cost at recognition. This means that this model is mostly used to measure intangible assets whose fair value can be determined from the market. Under this model, measurement is done by subtracting any amortization and impairment costs from the revalued amount. Revaluation increases are recognized as income in the books of account. Meanwhile decreases caused by revaluation are started as losses or expenses in the profit and loss statements.

The two models can be used to measure both acquired and created intangible capital. Intangible capital with an unlimited lifespan re not amortized while those with limited lifetimes are amortized. Instead their useful life is reviewed after every period in order to measure the impacts of any changes in the market to their value. Amortization is done on a straight-line method if a pattern of identifiable benefits can not be achieved. Due to the changes in cost and value, regular review of the measurement of intangible capital should be done 6 (Peters & Taylor, 2017).

Amortization and impairment costs relate to the value of intangible assets that are recorded in a company's balance sheet. Amortization, as stated is only done on finite intangible assets. It is used to show the value of the finite asset decreases as it approaches the conclusion of its lifetime. Impairment costs on the other hand occur is of a lesser value than it has been sated on the balance sheet. Amortization expense is achieved by use of an intangible assets present value and not an estimated future value. The present value is amortized over its lifespan and the annual amortized value is subtracted from its present value to determine the value at the current time 8(Webster et al., 2006). The amount is debited in the amortization account and credited then reported as an expense in the income statement.

Generally Accepting Accounting Principles requires the annual reevaluation of intangible assets so as to avoid the impairment costs. Impairment costs occur when the fair value is realized to be less than the current value of the asset after deducting amortization expense. Impairment cost is an expense is reported as an expense and therefore should be avoided so as to maintain the profits.

4 PERFORMANCE

Intangible capital has a great impact on the performance of an organization. In most cases, intangible capital greatly amplifies the performance of an organization in disguise. For example, customer satisfaction will mean boost of sales and eventually increase in the profit margin and vice versa. When a company acquires a legal patent to be the only producer of a specific good or service, it becomes a monopoly. Monopolistic benefits like supernormal profits and sales are achieved and losses are very minimal. Performance is therefore more tied to intangible capital than tangible capital or even human capital 6 (Peters & Taylor, 2017). Companies like amazon do not have much of human capital but are able to perform very well compared to their chain store peers and supermarkets that are highly dependent on human capital. This clearly shows the immense performance benefits that an organization can get from intangible capital.

5 SUMMARY

Human capital is under threat of a hostile takeover by the robots with almost equal artificial intelligence. Intangible capital has not any foreseeable replacement that can make it extinct in the coming generation. It is therefore prudent that more focus is paid to intangible capital and other types of unrecognized assets under this category should be recognized. Businesses operating as franchises or those with trademarks can sell at insane prices but customers will still buy. They buy because of the logo, trademark or the reputation of the company. All these sales drivers fall under intangible capital.

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