# ACCOUNTING FOR BRANDS:
# CONTEMPORARY ISSUES AND ALTERNATIVE OPTIONS

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**Abstract:** *Contemporary issues and alternative options on accounting for brands are the main thrusts of this paper. Thus, issues associated with accounting for brands and their effects on the financial statements or alternative financial treatments and valuations of brands on the balance sheets of corporate organizations are examined and evaluated. Accordingly, the definition and recognition of brands as assets in the balance sheet are considered. The paper also dwells on areas related to brand accounting: the need for accountants in the valuation and management of brands, reliability of cost measurement of brands, accounting treatment for brands, revaluation of intangible assets and disclosure requirements. Other areas that are equally discussed are the issues of brands regulation in Nigeria and the way forward. The paper concludes that the financial world arrives at a brand valuation by estimating the operating profit attributable to the brand and comparing it to an unbranded product. Also, brand valuation appears to be the most promising technique capable of illustrating the importance of brands to managers while bridging the different orientations between accountants and marketing managers. The paper recommends that the choice treatments of goodwill should be replaced by one standard treatment of purchased goodwill, amortization, while internally generated goodwill should not be recorded on the balance sheet; and the interaction between management accountants and selling and distribution managers' needs should further be strengthened and improved upon to allow for sound managerial decisions.*

**Key words:** Amortization, Capitalization, Intangible Assets

**Introduction:** Corporate intangibles have recently become more and more important in the economic life and for the success of corporate activities. For most of the companies, intangibles are essential factors for their progress, and a considerable part of their corporate value. Corporate intangibles are assets that are not perceptible to touch, insubstantial or eluding the grasp of the mind; and one type of the very broad spectrum of corporate intangibles is brands.

A brand is any word, tone, design or symbol to identify and distinguish one product or a group of products from other products (Plasseraud & Dehaut, 1994). In other words, a brand is a commercial term which can be name, logo, distinctive packaging or a combination of both, which serves to identify the origin of a product or a group of products and it enables the consumer to distinguish the branded product from other products. Brands also promote the customer's loyalty for the product.

Brands have, over time, been hardly recognized in the balance sheets of most corporate organizations; this is because there was no accounting standard to back up their valuations and disclosures in the balance sheets. However, there was an exposure draft published by accounting standards committee (ASC) in 1990. In 1994, the accounting standards board (ASB) published a discussion paper entitled "Goodwill and Intangible Assets" (ASB, 1994).

**Recognition of Brand as an Asset**

The characterization of intangibles as assets is a necessary and preliminary step leading to the examination of whether or not brands can be recognized in the balance sheet.

Brands are intangible assets which can only be recognized if they comply with asset definition. According to IAS 38 an intangible asset is an "identifiable, non-monetary asset without physical substance held for use in the production or supply of goods or services, for rental to others, or for administrative purposes". An asset, therefore, is a "resource:

- controlled by an enterprise as a result of past events, and
- from which future economic benefits are expected to flow to the enterprise".

The Standard indicates that "enterprises frequently expend resources, or incur liabilities, on acquisition, development, maintenance or enhancement of intangibles resources such as (β) trade marks (including brand names and publishing titles". Not all intangible items meet the characteristics of intangible assets (i.e. identifiability, control over the resource and existence of future economic benefits. IAS 38 requires, in this regard, that an intangible asset is identifiable to distinguish it clearly from others – *Separability*. Separability is achieved if the specific future economic benefits arising from the asset can be used by renting, selling, exchanging or distributing them without disposing of future economic benefits of other assets that are used in the same revenue generating activity. But it may also be possible to prove the identifiability of an asset in some other way (IAS 38, paragraphs 11 & 12). The Standard also defines "control over a resource" as the power to dispose of the future economic benefits that may result from the sale of products or services as well as from cost-saving or other benefits resulting from the use of the asset by the enterprise (IAS 38, paragraph 17).

**The Need for Accountants in the Valuation and Management of Brands**

Much of the information required for brand management is quantitative; the management accountant is, therefore, needed to perform the task of transforming and analyzing the accounting transactions data, which has been collected by the financial accountant, into meaningful results that would assist management in its decision-making process. Thus, management accounting focuses on internal reporting, while financial accounting concentrates on external reporting.

One of the most effective ways for the accountants to provide useful information for management is by conducting periodic brand valuations. Brand valuation assigns a financial value to the equity created by the selling and administration department expenses to the name or image of a brand offering a comprehensive measure of that equity for that Company.

Through brand valuation, organizations are able to create a consistent, quantifiable value that is comparable across product lines, countries and company units. Furthermore, current brand expenditures expected to generate future benefits, such as promotions and advertising, can be reflected in the current value of the brand. Choices among alternatives can be compared according to their effect on the brand value calculation. Brand valuation is not solely a historical, cost-based measure, but also allows a means to incorporate future results.

The process of valuing an intangible asset such as brand requires a certain degree of estimation and subjectivity. Nonetheless, the process can be consistently applied over time to all brands managed by an organization. Because of such standardized application, brand valuation can be an essential element of a brand management strategy. With standardization, the technique will gain greater respect from management and can be applied more confidently over time to evaluate evolving trends in brand values.

Effective brand management requires coordination among many areas in the organization. A focus on brand is essential from all areas, since marketing is not the only function concerned with increasing brand value. However, conveying the importance to employees of creating and maintaining brand values across the entire organization is often difficult. Accounting for brand value alerts employees to the strategic importance of the brand. An example might be posting the number of days without an accident in manufacturing department. Employee can infer the importance of the goal of safety by the recording and prominent display of the statistics of accident-free days.

The technique of brand valuation allows an organization to deliver a consistent brand image. If the entire organization understands how brand value is computed, it will be easier to prevent actions that negate each other or interfere with the overall brand strategy. Furthermore, a promotional campaign that dilutes the image of the brand by confusing the key consumer segment’s perception of the brand’s major identity can be avoided. If the overall impact of the campaign is evaluated in terms of the comprehensive value of the brand, the negative effect on the key consumer segment can be determined. Similar analyses are, however, possible without brand valuation, but valuations help to quantify the long-term effects.

Brand valuation allows managers to appraise the efficacy of brand expenditures in terms of enhanced or diminished value of the brand itself. Accountants render assistance to marketing managers in terms of performance measurements of strongly branded companies. Thus, accountants and marketers can work together in order to transform financial transactions data into meaningful and powerful information for supporting brand management decisions. Again, management accounting department should be separated from other accounting departments because of its unique role of providing accounting information for internal managerial decision-making to promote collaboration among managers and accountants.

Brand valuation is another accounting technique that may be even more useful to selling and distribution managers in that it extends beyond a cost focus. It is more comprehensive because it relates to outcomes or results and it incorporates projections of future income and cash flows. Such predictive information is very vital in assisting a firm with strategic brand management decisions. Furthermore, the valuation of brands provides management with a measure that allows an appraisal of the brand relative to other assets of the firm.

Brand valuation also aid managers involved in budget allocation decision making. Selling and distribution expenses could be allocated according to the relative value of the brand in the portfolio. The process of determining the strength of the brand used in the valuation could also yield valuable information for this spending allocation. For instance, the appraisal of brand strength might reveal particular areas of vulnerability for the brand that might warrant a focused marketing campaign and thus create additional implications for the allocation of the budget.

**Reliability of Cost Measurement of Brands**

In practice, the accounting policy in respect of brand recognition and cost measurement depends mostly on the way in which brands have been acquired by the enterprise. Separate acquisition (including acquisition without charge or by exchange), acquisition as part of a business combination (merger as well as acquisition of subsidiaries), and internally generated brands.

**Separate Acquisition**

According to IAS 38 (paragraph 23), if an intangible asset is acquired separately, the cost of the intangible asset can usually be measured reliably. This is particularly so when the purchase consideration is in form of cash or other monetary assets. In the case when the brand is acquired by an exchange (or part of exchange) with another (tangible or intangible) asset, it has to be measured at its fair value, which is supposed to be equivalent to the fair value of the asset given up and adjusted by the amount of any cash equivalents transferred (IAS 38, paragraph 34).

Brands, acquired for consideration, are intangible fixed asset and as such accounted for in the balance sheet. Any asset which is acquired by way of an exchange or free of charge should be recognized at its market value, which is the price that would have been paid under normal market condition (i.e. at arm's length relationship). Hence, a brand, like every other intangible asset, must be recognized at the acquisition cost if it has been acquired for consideration (Keitz, 1997; Coenenberg, 1996). Furthermore, brands which are acquired by way of exchange can be initially measured either at the fair value of the asset given up or at its carrying amount (Knop and Kitting, 1995). If an intangible asset is acquired free of charge, it must not be recognized because of the uncertainty of the value of the asset (Adler, During and Schmaltz, 1995)

**Part of Business Combination Acquisition (Merger or Consolidated Financial Statements)**

The fourth and seventh directives do not include any explicit advice of how to treat intangible assets which are acquired through a merger or an acquisition of a subsidiary. However, it can be implicitly concluded that those assets, if identified, should be recognized and measured separately. IAS 38 covers the treatment of acquired intangible as part of a business combination in the consolidated financial statements as well as part of a merger. Paragraph 27 of IAS 38 stipulates that an intangible asset should be recognized in the consolidated financial statement at its fair value at the date of acquisition if the intangible asset was part of an acquisition of an enterprise.

**Accounting Treatment for Brands**

In 1990, the ASC (Accounting Standards Committee) published new draft rules for the treatment of goodwill ED 47 (Exposure Draft No. 47) "Accounting for Goodwill". ED 47 proved to be controversial and its proposals have not been put into practice in a new standard. The main proposals in ED 47 were as follows:

(i) Purchased goodwill should be carried in the balance sheet and amortized. Immediate write off would no longer be allowed.

(ii) Amortization should be on the straight line basis. A more conservative basis would be allowed if that gave a more realistic allocation.

(iii) The period of amortization should not normally exceed twenty years, but, exceptionally, a longer period might be allowed.

(iv) Goodwill in the balance sheet should be subject to an annual review (to ensure there has been no diminution in value).

(v) Negative goodwill should be credited systematically P&L (profit and loss) account over a suitable period.

The ASC proposed that brands should be treated in the same way as goodwill, especially the amortization period of up to twenty years. Many companies were opposed to this proposal because of the effect on future profits. Also, a number of commentators were unhappy about the proposals contained in ED 47. Coopers and Lybrand, for example, agreed that goodwill should be capitalized, but disagreed that it should be systematically amortized in the P&L account.

Sequel to these controversies and disagreements, the ASC came out with another exposure draft – ED 52 "Accounting for Intangible Assets" published in 1990. This draft recognized a case for reporting 'purchased' brands as an asset but not internally generated or 'home-grown' brands. And in 1992, Arnold et al published a report on "Goodwill and Other Intangibles: Theoretical Considerations and Policy Issues" which contained the following proposals:

(i) Purchased goodwill and internally generated goodwill should be capitalized.

(ii) Goodwill should be written off against profit over its useful life (never against reserves).

(iii) Similar accounting treatment would apply to brands (a typical example of internally generated goodwill).

(iv) Companies would be able choose whether to include internally generated goodwill in their financial statements.

In 1994, the ASB (Accounting Standards Board) discussion paper on "Goodwill and Intangible Assets" considered four of accounting for goodwill:

(i) Capitalization and predetermined life amortization. (ii) Capitalization and annual review.

(iii) Immediate write off. (iv) Separate write off reserve.

Two approaches were supported by the members of the ASB:

(i) A combination of 'Capitalization and predetermined life amortization' and Capitalization and annual review.

(ii) Separate write off reserve.

Capitalization and annual review was regarded as appropriate for brands with a long expected life (say, over twenty years). This approach would be appealing to companies which have been incorporating brand values into their balance sheets.

The features of accounting for brands are similar to issues related to goodwill valuation. Indeed, these two are inextricably intertwined; and to adequately comprehend the current debate on brand valuation a fair knowledge of the current accounting practice for goodwill is required. The relevant Standard for goodwill is SSAP 22 – Accounting for Goodwill. This Standard was published in 1984 and later revised in 1989 by the ASB.

Under the SSAP 22, Companies may treat goodwill in the following ways:

- ❖ Write-off goodwill against reserves; or
- ❖ Write-off part of goodwill against reserves, and capitalize the remainder, then amortize; or
- ❖ Capitalize the whole goodwill then amortize.

Quite often, it is assumed that shareholders are interested in the annual profit figures than in the total for the group reserves. Capitalization or amortization, therefore, is not a popular accounting policy in the managerial sphere or perspective. To write-off goodwill against reserves at the date of acquisition is a treatment which is most preferred by majority of Companies (Skerratt and Tonkin, 1994). Barwise et al (1994) argued that brand accounting was inevitably subjective and recommended that brands (purchased or internally generated) should not be included in the balance sheet of the organization. But this argument greatly contrasts with the views of the discussion document "Making Corporate Reports Valuable" (McMonnies, 1988, Pp 61) which strongly advocates the use of net realizable values as a basis for financial reporting.

**Revaluation of Intangible Assets**

Revaluation of Intangible Assets at the end of a financial year, IAS 38 stipulates a benchmark treatment and an allowed alternative treatment (paragraphs 63 -64). The benchmark is presented under the heading "Amortization" and it means initial measurement minus periodic amortization. According to the allowed alternative treatment, an intangible asset should be carried at a revalued amount, which is "its fair value at the date of the revaluation less any subsequent accumulated amortization and any subsequent accumulated impairment losses". Fair values should be estimated by reference to an "active market". But IAS 38 paragraph 67 specifies that an active market cannot exist for brands like other intangible assets such as newspapers, mastheads, publishing rights, etc. This is because brand transactions are relatively infrequent and individual. Therefore, the prices for recent transactions do not provide a sufficient evidence for the values of other brands. Due to this lack of a reliable measurement basis IAS 38 seems not to allow for the revaluation of brands.

The situation is absolutely clear in Germany and France. In accordance with the Fourth European Directive (Article 33, paragraph 1), the revaluation of intangible assets is generally not allowed in Germany; because – due to the strong principle of prudence – revaluation is not accepted for any asset, and in France, because the general revaluation option are limited to tangible and financial assets (see Article 33 paragraph 1). Therefore, the position taken by IAS 38, the French and German laws lead to the same result of not allowing for revaluation of brands.

**Disclosure Requirements**

Like other IAS and in conformity with the importance of the information aspect of the accounting conception of the IASC, IAS 38 generally contains a lot of disclosure rules which go far beyond the required disclosures for intangible assets in Germany and France. According to Germany and French laws, a company must show the development of the balance sheet item "intangible assets" regarding acquisitions, disposals and amortizations in the fixed assets schedule. Additionally, the methods of amortization period, write-downs and possibly write-ups have to be mentioned and explained in the notes. But, with reference to brands, IAS 38 only requires, in special circumstances, additional disclosures (e.g. if the brand is amortized over more than twenty years). In other cases, the disclosures for brands according to IAS 38 are similar to those in France and Germany.

**Contemporary Issues of Accounting for Brands**

The issue of accounting for brands dates back to the late 1980s when it became very controversial in the financial reporting spheres. A number of some reputable and prominent companies took the lead and decided to include a *value* for their brands in their balance sheets. Thus, brand accounting is a recent development in the field of accounting.

Consistent treatment between 'purchased' and 'home-grown' brands is one of the issues that arise because most of the companies do not value their brands. For example, Marks and Spencer plc do not attach a value to the well-known St. Michael brand, and Guinness plc is the only brewer that give brands a valuation on the balance sheet (Elliott and Elliott, 1993).

It is unlikely that these issues will be satisfactorily resolved until there is a clear consensus about what the balance is supposed to represent. At the moment, balance sheets represent a mixture of historic costs, not yet allocated expenses and market values. Thus, it is difficult to see what a balance total represents, other than an accounting figure which represents the sum of these different values. One way forward would be to report market values (or exit prices) in the balance sheet (which is probably what the lay users of financial statements think these figures represent anyway). By so doing, it would be clearer to account for 'purchased' and 'home-grown' brands on a consistent basis.

The use of brand values also supports a better way to hold managers accountable for their actions. Meeting a budgetary target in terms of conventional accounting measures of performance (revenues and expenses) can be arbitrarily manipulated. Using a long-term perspective, mangers can concentrate on actions that benefit the entire organization and these are reflected in the brand's value.

Another serious issue is the time frame of management focus. A long-term focus on brand value helps marketing professionals at all levels can be more involved in both of these processes. Brand value is a more meaningful metric measurement that provides accountants and marketers with a common means of choosing among alternatives and setting priorities. It also keeps the central focus of the entire organization of paramount importance. Maximizing brand value can become a fundamental operational goal of the planning process, consistent with the corporate objective of maximizing shareholder's value.

A short-term management focus on brand value can be particularly problematic, given the high turnover in many marketing positions due to promotions and lateral assignments. Unlike conventional accounting measures, in which an annual time frame is dominant, brand valuation is a technique that outlives personnel. It has immediate transferability across geographical boundaries. The consistent focus on brand value allows even the new employees to understand their role and how their reward system matches the organization's objectives.

Managing complex brands which have multiple product categories under the brand umbrella, can be simplified with brand valuation. Strategies among separate product managers can be coordinated by considering the combined effects on brand value for the management of separate product segments. Instead of focusing on short-term cost minimization or revenue maximization, a more holistic view can result from product managers taking a more integrated approach in maintaining or maximizing the value of the brand.

Sometimes, it is difficult to compare the performance of managers of different products or in different geographic segments; brand valuation allows the use of a comparable measure. The measure of brand value is less subjective and more consistent when evaluating among alternative performances.

**Issues of Brand Regulations in Nigeria**

Nigeria's trade mark laws are quite obsolete and need to be updated and revised. The current trade mark law is based on England's Trade Mark Act of 1938, which was repealed by the Trade Marks Act 1994.

A working paper has been produced by the Nigerian Law Reform Commission. This document focuses on the Reform of Industrial Property Law and setting out a proposed Industrial Property Law. The proposed law, when enacted, is expected to allow for the simultaneous prosecution of infringers under both the criminal and civil law, in addition to making other changes. Unfortunately, this proposed law has lingered since 1990, when it was first issued as a draft, without legislative affirmation.

It is also expected that any new legislation on trade marks will include a certain provision allowing for the registration of shapes and certain distinctive aspects of packaging. Such a provision would require precise and limited scope otherwise it swallows up the limited protection now given for design registrations. According to the proposed law, a registered trade mark can be renewed every seven (7) years, in perpetuity, but the design registration gives the owner only five (5) years of protection that can only be renewed two times for consecutive period of five (5) years each.

The Nigerian law also needs to be revised so that the definition of *infringement* is no longer restricted to goods within the same trade mark specification but will extend to cover similar goods and even dissimilar goods in other categories, where the trade mark is famous. Such protection will the advantage of allowing brand owners to use the reputation which their trade marks have acquired should they expand the range of their products, without needing to expand under the new trade marks.

More importantly, the Nigerian law on trade marks needs to be changed so as to protect well-known trade marks even if they are not registered in Nigeria, by prohibiting the registration of identical or similar marks without the consent of the owner.

The Standards Organization of Nigeria (SON) Act 1970 should be amended to give SON the powers and responsibilities of investigating the manufacture, distribution and sale of counterfeit products. The investigators of SON, if properly and well trained, should be able to gather enough evidence to be used in criminal and civil prosecutions. SON should also be empowered to assist the police in enforcing criminal sanctions under the Trade Malpractice's (Miscellaneous Offences) Decree 1992 and the Merchandise Act 1956.

Furthermore, the surveillance arm of the Department of Customs and Excise needs to be strengthened so that skilled custom officials can find and seize imitation and counterfeit products at the point of entry into Nigeria. Such a change must be made if Nigeria is to satisfy her obligations under the agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS). Again, TRIPS requires member states to "adopt the procedures to enable the rightful holder of a trade mark, who has valid grounds for suspecting that the importation of counterfeit trade mark or pirated copyright goods may take place, to lodge an application in writing with competent authorities, administrative or judicial, for the suspension by customs authorities of the release into free circulation of such goods".

**Conclusion**

The financial world arrives at a brand valuation by estimating the operating profit attributable to the brand and comparing it to an unbranded product. The resulting premium associated with the brand is adjusted for taxes, and then multiplied by a seven-item factor (leadership, stability, market, internationality, trend, support and protection) using interbrand's assessment of brand strength.

Also, brand valuation appears to be the most promising technique capable of illustrating the importance of brands to managers while bridging the different orientations between accountants and marketing managers. Since the value of brand can be expressed in monetary terms, all decision makers have a common point of reference. The measure of brand value may include subjective elements, but the lack of such a measure means that the importance of intangible assets may be overlooked.

Furthermore, the use of brand valuation can help foster recognition of a common goal for individuals in pursuing strategic objectives. Each discipline can contribute a substantial amount of expertise to the brand valuation process. This joint contribution can then assist the organization with brand management.

**Recommendations**

ED 47 recommends that the choice treatments of goodwill should be replaced by one standard treatment of purchased goodwill, amortization, while internally generated goodwill should not be recorded on the balance sheet (Jupe et al, 1995); also, the interaction between management accountants and selling and distribution managers' needs should further be strengthened and improved upon to allow for sound managerial decisions.

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