

Results of the AEG e-discussion on Purchased Goodwill and Marketing Assets in the SNA

Introduction

1. The 1993 SNA only records purchased goodwill and it treats purchased goodwill for corporations and unincorporated enterprises differently. Should goodwill continue to be recognized only when purchased or should internally generated goodwill also be recognized? Should the purchased goodwill be treated the same way for corporate and unincorporated enterprises? Should the SNA recognize assets such as brand names, trademarks, franchises, etc.?

2. The Canberra II Group has considered these issues in detail at three separate meetings and made the following recommendations to the AEG for its consideration:

- (a) the nature of purchased goodwill be clarified in 1993 SNA;
- (b) Although marketing assets are normally identifiable as separate assets from goodwill, these be included in the same asset category as purchased goodwill. In the main, the value of marketing assets would only be available when a business is sold, and even then they could be bundled with goodwill. When a separate transaction does occur, it should be recorded;
- (c) The purchased goodwill and marketing assets should be calculated as the excess of the purchase (or takeover) value of a business over the net value of the other assets and liabilities otherwise identified in the SNA system for that business. The same calculation should apply for both unincorporated businesses (including quasi corporations) and all incorporated businesses;
- (d) internally generated goodwill and marketing assets should be excluded except where they are evidenced by a sale. It also reaffirmed that in any one accounting period there is no reason for the sum of all recorded and unrecorded assets less liabilities of corporations to be exactly equal to the value of shares and other equity held by the owners (and recorded as a liability in the corporation sectors' balance sheet). However, given rational markets it could be expected to show reasonable correspondence over the medium term. This should be made explicit in SNA;
- (e) purchased goodwill and marketing assets continue to be treated as 'non-produced' assets in SNA. However, further consideration will be given to whether a terminology can be found that better reflects the nature of these assets; and
- (f) the 1993 SNA discussion of the amortisation of purchased goodwill and marketing assets be changed to reflect the impairment approach adopted in the international accounting standards.

Response received

3. The recommendations of the Canberra II Group were referred (document no. SNA/M1.05/24.1) to the AEG members soliciting their opinions through a questionnaire. The questions asked of AEG members and responses received through e-discussions have been summarized in the following table:

Table: Questions asked of the AEG members and response received

No.	Question(s)	Response received		
		Yes	No	No Opinion
1	Do you agree that an asset class 'Purchased goodwill and marketing assets' should replace the existing 'purchased goodwill'?	15	0	-
2	Do you agree that the economic nature of purchased goodwill and marketing assets should be clarified along the lines presented in this paper?	15	0	-
3	Do you agree that the valuation principles for purchased goodwill and marketing assets should be applied consistently, irrespective of whether the entity is a listed or unlisted corporation, a quasi corporation or is unincorporated. They should be calculated as the excess of the purchase (or takeover) value of a business over the value of the other assets and liabilities otherwise identified in the SNA system for that business?	15	0	-
4	Do you agree that internally generated goodwill and marketing assets should continue to be excluded, except when their value is evidenced by a sale. In the case of internally generated goodwill, this occurs only with the sale of a business. In the case of marketing assets it can also occur with their independent sale?	12	2	1
5	Do you agree that the assets should continue to be classified as non-produced assets, even though their value is often driven by a productive activity. However, further consideration will be given by the Canberra II Group to whether a term can be found that better reflects the nature of these assets. This will be addressed in the issues paper concerning Classification and terminology of assets (Issue 27)?	15	0	-
6	Do you agree that the assets should not be amortised at a predetermined rate but made subject to an impairment test consistent with the international accounting standards for these assets?	14	0	1

Conclusions

The consultation showed that all AEG members participating in the e-discussions supported the proposals in paragraph 2 above overwhelmingly.

A summary of comments is annexed.

Summary of Comments Made by Members in the Questionnaire

The original response and full comments are available on the UN website¹. The objective of this annex is only to give limited extracts to entice readers to read the full comments of the AEG members.

Question 1

One member prefers the term “Revealed goodwill and marketing assets” for “Purchased goodwill and marketing assets”. In his view this term also leaves open the possibility to include e.g. marketing assets which are not purchased but nevertheless recognised and included on the balance sheets of an enterprise.

One member observes that delineation of marketing assets is consistent with work on company accounting practices and is important given the magnitude of brand equity as an economic phenomenon

Question 2

Agreeing with the proposal one member has observed that the paper usefully outlines an economic basis for ‘purchased goodwill and marketing assets’ (G&MA). However, it defines G&MA as “internally generated.” Yet changes in G&MA (assumed positive or negative here) can arise for a business from actions outside of the production boundary (function) of the business. For example, by actions by national and international rivals which improve/damage their brand equity to the cost/gain of the business, imposition of government restrictions, and random events (such as the poisoning of a supermarket shelf item). In this sense, the term ‘internally generated’ may be unhelpful. Is the term needed and, if so, could it be clarified in SNA this respect? The economic nature of marketing assets is considered in paragraph 23 only in terms of providing capital services to production. However, it may also be considered in terms of shifting the demand curve and impacting on profitability in this way. Asset values would be generated from the effect on profits and their forecasts. It does not enter the production function directly, though there may be a simultaneity. A feature of the process that underlies the generation of brand equity is the sometimes immense gains/losses, which are far less predictable than a technological production function. Mueller and Supina (2002) (Small Business Economics, 19, 223-53) cite examples of increases in G&MA of an almost windfall nature.

Question 4

Two members *disagree* with the proposal and argue that one should not exclude the possibility of a recognition of marketing assets not purchased. The resulting series of purchased G&MA in a period would include the asset value of businesses for sale in that period, and that carried over (with some amortization) from sales in previous periods. It will (i) increase, as more businesses are sold, and reflect changes in the rate of sales of businesses, (ii) may be subject to a selection bias. The selection bias is first, because businesses sold may have unusually high brand asset values (for brand leverage; the well-documented purchase of a brand for extension to diversified products) and second, may have unusually low brand equity, the sale being because of loss of brand equity. Mueller and Supina (2002) found for the US roughly half of their estimates of

¹ <http://unstats.un.org/unsd/sna1993/viewquestions.asp?tID=22&stID=0&sstID=0>

residual goodwill to be negative. This all detracts from the series' value as an analytical series. The SNA might include caveats on the limitations of the series and hold out the possibility of a series for 'non-purchased goodwill and marketing assets.'

Question 5

It is agreed that its description "non-produced" is certainly inappropriate. Only a minimal activity may be needed to generate them. Yet, this is akin to the normal practice in SNA of using the market to value outputs where possible.

Question 6

In practice, statisticians will not be able to make such an impairment test by themselves. They have to rely on the accounting standards as applied by the enterprises themselves.

It is also possible to take a more radical approach to these issues. This would be based on two considerations: (i) analytically, it is not useful that the accounts forever record an item "purchased goodwill" exclusively because some time in the past a payment for acquiring such goodwill has been made, and (ii) many users of the national accounts have serious problems in interpreting the current convention of recording a negative net worth for those corporations that are expected to do well in the future and thus have high share prices. The solution would be that the 1993 SNA Rev 1 sets the net worth of corporations by definition at zero. The difference between the value of outstanding shares and the aggregate of the other assets and liabilities would then be recorded as "goodwill." All changes in this goodwill between the opening and closing balance sheets would originate in other changes in assets, except for outright purchases/sales of goodwill that would be recorded as transactions.

It would be difficult for statisticians to make impairment test for an asset which is recognized only when the entity goes on sale. It may not be feasible to implement such a recommendation unless some guidance is included in the SNA Rev. 1 to help countries perform this test