CAIRNGORMS NATIONAL PARK AUTHORITY
AUDIT COMMITTEE

FOR DECISION

Title: **INTANGIBLE ASSETS POLICY**

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Purpose of Paper

This paper presents a follow up to points made by Audit Scotland in their audit of the 2011/12 accounts for consideration by the Committee prior to moving forward with the audit of the accounts for 2012/13.

Recommendations

The Committee is asked to:

a) Agree the adoption of an additional accounting policy covering the separate disclosure of non-current assets – intangible assets which will result in separate disclosure of software values from other assets.
b) Agree the continuation of the current practice of not recognising a value in the Authority's balance sheet in respect of the Cairngorms National Park brand.

Executive Summary

The external audit of the Authority's 2011/12 accounts gave rise to an action to review current accounting policies and associated disclosure on non-current assets – intangible assets. This potential accounting policy impacts primarily on the Authority's disclosure of values of software purchased and in use as an intangible asset, and also on the treatment and potential valuation of the Cairngorms National Park brand.

The paper considers each of these two issues and makes appropriate recommendations for their treatment in the 2012/13 and subsequent years' accounts.

INTANGIBLE ASSETS POLICY – FOR DECISION

Background

1. In the Annual Audit Plan 2012/13 for the Park Authority, Audit Scotland identified a number of audit risks, one of which was on intangible assets.

2. The issue was identified as follows:
    a) The CNPA did not disclose any intangible assets in the 2011/12 financial statements. Whilst this is accordance with the current Park Authority's policy, management have agreed to review the policy for 2012/13.

3. The specific risk identified was:
    a) There is a risk that intangible assets are not correctly identified and valued which may impact on financial statement disclosures.

4. Audit Scotland's source of assurance was that CNPA management agreed to review the intangible asset policy during 2012/13.

5. To consider this audit risk, and prepare a considered response, the risk has to be looked at on two very different types of intangible assets, and a possible reclassification of an asset currently disclosed as a tangible asset :
    a) Non-current intangible assets – software licenses
    b) Non-current intangible assets – the Cairngorms National Park brand

Non-current Intangible Assets – Software Licenses

6. The issue identified by Audit Scotland means that the Non-current Assets note in the financial statements does not disclose <u>separately</u>, as a distinct class of non-current assets, the most obvious intangible assets (IT systems and copyright) as does, for instance, the Loch Lomond and Trossachs National Park Authority's financial statements.

7. Purchases of information technology equipment and services are reviewed in line with the Park Authority's stated policy on the minimum quantum for an asset to be capitalised rather than expensed. Purchases of software licences, in aggregate more than £500 are capitalised as "Information Technology" (IT).

8. No additional analysis has historically been included in the financial statements splitting IT between what is effectively "hardware" and "software": "tangible" v "intangible".

9. However, the accounting records maintained by the Park Authority are in sufficient detail to allow this split (see below) to be calculated.

10. The specific risk identified by Audit Scotland was:
    a) There is a risk that intangible assets are not correctly identified and valued which may impact on financial statement disclosures.

11. On examination, and having confirmed that the accounting records are in sufficient detail to allow separate identification of software and hardware values, our review indicates that the issue is one of disclosure only. If a software license is above £500 it will be capitalised as IT and identified in the asset register for what it is (i.e. the software package). Where the operating system is part of the cost of a computer base unit no attempt is made to split out the cost of the hardware and software elements.

12. The value of the licence is the purchase price and the depreciation rate will be that appropriate to the remaining useful economic life of that license. It is rarely appropriate to revalue upwards the cost of software licenses as all that the Park Authority has bought is the right to use the software for a specific period: it rarely owns the underlying source code.

13. The costs of identified software licenses included in IT are as follows:

	31/03/12	**31/03/13**
Cost	£63,656	£63,656
Net book value	£6,213	£275

Software Licences - Conclusions

14. The net book value of the capitalised software licenses at 31 March 2013 are £275 which is unlikely to be considered material by the auditors. The question to be address by the board and management is not therefore materiality, but whether the inclusion of a specific accounting policy on intangible non-current assets is:
    a) Appropriate
    b) Strengthens the overall accounting control
    c) Complies with reporting guidelines (FReM)
    d) Is cost effective to implement

15. On review, our understanding is that the answer to each of the above questions is yes. The information is available with no additional procedures required to implement. The only changes are the inclusion of an appropriate accounting policy and the disclosure of the intangible assets in the financial statements.

Recommendation

16. **Our recommendation is that the Audit Committee agree the adoption of an additional accounting policy to cover disclosure of non-current assets – intangible assets. The recommended policy is as follows:**
    a) Non-current assets – intangible assets
    b) 1.5 Copyrights and software licenses are disclosed as intangible assets in accordance with Financial Reporting Manual (FReM) guidelines and are amortised on a straight line basis over their expected useful lives.

17. As the NBV at 31 March 2013 is £275 we propose to include a statement in the non-current asset note that IT includes the NBV of intangible assets of £275 (2012:

£6,213) at the relevant year ends. Any future material purchases of software will be separately disclosed.

Non-current Intangible Assets – The Brand

18. Brand accounting is a complex subject, addressed by international accounting standards, and highly technical, esoteric even, often misunderstood and in the context of the National Park at odds with the concept of the value of a consumer brand where the value of the brand can be calculated easily by reference to numerous bases and perceptions:
    a) Bases: sales, profits, market penetration, desirability of product or service or often the cost of gaining control or a product/process or a company;
    b) Perceptions: the value to the economic owner is not necessarily the same as that perceived by an interested third party – and critically is sought after because of its actual or perceived values, which are not necessarily financial. The brand value is also often simply the cost of buying a brand. Value therefore depends on whatever is meant by value.

19. The Cairngorms National Parks "brand" (the brand) has existed since 2004 and clearly has a "value" but recognising the value of brand as a non-current intangible asset is limited by current accounting practice.

20. In accounting terms there are two ways to recognise the value of a brand:
    a) **Buy** a brand (**acquired** goodwill); or
    b) To **capitalise** all costs incurred in internally developing the brand as an asset (**created** goodwill), which means there is a balancing act between deciding what part of the cost incurred is immediately expensed and which is recognised as an asset.

21. The former can be discounted immediately as actual ownership of the Cairngorms is divorced from the brand.

22. The brand has been created by CNPA to be exploited by businesses and organisations within the National Park's boundaries at no charge. The costs of bringing into existence, maintaining and managing are borne by CNPA and are correctly written off. The only costs which <u>could</u> have been capitalised as intangible assets historically are the origination costs – the design costs of the brand – which would then be amortised over a period of time. As the Park Brand section in the CNPA web site points out the brand is not the logo of the CNPA but represents the National Park. The CNPA role is neutral, being only a facilitator. The brand is independent of CNPA so recognising the value of the brand is not appropriate, the more so since it is offered for use for no consideration and what gives the brand its uniqueness is attributable to a natural asset with multiple ownership.

23. In its leadership role in developing and coordinating delivery of the National Park Partnership Plan and through that, integrated management of the National Park, the Authority does have a stewardship role in supporting the management of the brand. Even this stewardship role is, to a degree, delivered at arms-length to the Authority, through the Brand Management Group.

24. Therefore, on balance, our view is that the brand is not sufficiently within the direct control and management of the Authority to warrant capitalising as an intangible asset within the Authority's accounts. Audit reviews have previously reinforced the need to ensure that the Authority, in taking a lead role in supporting brand management processes, continues to review resource levels required to maintain and if necessary enhance brand management processes and protecting its strong, positive brand identity, and this remains the case. However, while the overall management of the brand remains at arms-length and toward the collective benefit of the National Park as a whole, we believe it is not appropriate to bring an intangible asset value for the brand onto the Authority's balance sheet.

Recommendation

25. Our recommendation is therefore that there is no change at this time to the current practice of not recognising an intangible asset value in relation to the National Park brand in the Authority's accounts. This policy will be reviewed to reflect any changes made in brand management arrangements.

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