



## Chapter XI

# I-Accounting: An Adaptive Approach (Method + Practices) to Account for Intangibles

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### Abstract

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*This chapter introduces the core aspects of an approach facilitating the valuation of intangible assets created by virtual organisations. The approach we present relies on established simple unified procedures which can drastically reduce problems caused by handling each situation individually, especially if there is no previous experience of similar cases. At the same time, the volume, value, and visibility of transactions between the various stakeholders and involved parties is increased. We conclude with an example case analysis related to the reality faced in collaborative research projects; these are carried out by diverse partners operating as a virtual organisation whose different intellectual assets (IAs) and the value thereof need to be recognised in order to prepare the ground for successful project completion.*

## Introduction

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At the heart of our thinking is a growing body of evidence revealing that reliance on financial measures alone will critically undermine the strategies that leading-edge companies must pursue to survive and thrive long term. As Baruch Lev, professor of Accounting and Finance at New York University's Stern School of Business, argues: "To claim that tangible assets should be measured and valued, while intangibles should not—or could not—is like stating that *things* are valuable, while *ideas* are not" (Ernst & Young, 1996, p. 27).

The comments and finding above and also from others, for example, Sveiby and Lloyd (1988), Sveiby (1997), and Edvinsson and Malone (1997), indicate that there is a linkage between intellectual capital performance and business performance. The International Federation of Accountants define an intellectual capital framework, based on the work of Edvinsson, St. Onge, Armstrong, and Petrash that comprises of human, customer, and organisational components (IFAC, 1998).

Work carried out by Ernst and Young has two major connotations, namely: "... non-financial indicators can be used as leading indicators of future financial performance" and that "... all non-financial criteria are fed by performance, and in turn, feed the perception of performance" (Ernst & Young, 1996, p. 35). Thus, traditional ways of "measuring" a company do not necessarily prove future performance; the non-financial (or intangible) indicators provide more reliable information into the future health of the organisation.

Furthermore, the changing economy, in particular, the impact of the Internet and acceleration of timescales, has led to the need for correspondingly enhanced and more reliable financial reporting approaches. Companies are now evolving ever faster as they become enmeshed in an ever more complex network of alliances, virtual networks, joint ventures, partnerships, and other related entities. Furthermore, they increasingly extract their value and growth primarily from intangible assets such as innovative organisational forms, brands, know-how, patents, and so forth, in a way that was previously only vaguely understood. This holds for small and medium sized enterprises as well as for big players, though especially in the latter case, the inefficiencies that they face grow in proportion to their size, thus limiting their growth.

The terms intangibles, intangible assets, knowledge assets, and intellectual capital are all used by different groups of professionals to describe basically the same thing, that is, the knowledge and corporate relationships that are so important for success, indeed more important today in many cases than physical assets. However, the elementary linkage between intangibles and the focus on knowledge is still often overlooked, as is the role of the learning process in value creation. In fact, a surprising number of experts within the accounting discipline ignore the elementary linkage between intangibles and the focus on knowledge, missing also the importance of the basic operation that helps value creation, namely the learning process.

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