Intangible Assets in Polish Accountancy and Tax Law – Similarities, Differences and their Consequences

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Abstract

The turn of the 20th and 21st centuries is the time period, which is also called 'the new economy' due to significant changes which took place in companies carrying out a variety of business activities and competing against each other on the market. The appearance of the new economy's type was primarily observed on the verge of nineteen seventies and nineteen eighties. This new kind of economy was based on the knowledge, and was named by A. Tofler who presented the wave theory [2]*. The characteristic feature of the present period of civilisation's development are: knowledge, information, the intangible assets and this period's attribute is a computer. The changes which have already occurred caused that the importance of fixed assets, as the source of building competitive advantage, decreased significantly in favour of the intangible assets.*

This growth of importance of the intangible assets caused however, that the expectations towards both accountancy and the tax law have also increased for this particular element of company's wealth was properly expressed and settled in company's financial statements. One of more important elements of proper assessing and accounting the intangible assets, is the definition of the intangible assets, simply because everything begins with its definition, or in other words qualifying particular assets' element to a certain group of the company's assets.

The most important aim of this elaboration is to carry out the analysis of both accounting and tax definitions of the intangible and legal assets' components and also to point out the similarities, the differences and their possible consequences. The secondary aim is to point out the desirable direction of changes in accountancy and tax laws in terms of the intangible and legal assets' definitions.

Because of the fact that the rules of Polish accountancy are based on the International Accounting Standards the conclusions drawn from the analysis presented herein may be useful for other countries whose accountancy systems are also based on the International Accounting Standards.

While creating this article, the following methods of scientific research were used: the method of literature analysis and legal acts in order to present current definition of the intangible and legal assets in both accountancy and the tax laws in Poland, also the method of source documents' analysis to describe the rules of identification and the intangible and legal assets' recognition in KFJ Investments – limited liability company.

Key words: *intangible assets, tax law, intellectual capital, international accounting standard, true and fair view.*

Introduction

The assets of the company can be divided into two basic groups: the fixed assets and the intangible ones. The fixed assets are those which exist physically. This means that they can be seen, measured, counted, touched and sold off. They mostly consist of properties, machinery and equipment, products, commodities, materials, cash, money in bank accounts etc. The intangible assets, unlike the fixed ones, do not appear physically. This means that it is impossible to see them, touch, count or measure. They mostly consist of standards, values, knowledge and employees' competences, company's reputation, clients' database, trademarks, brand names and legal values.

Intangible assets play significant and very often key role in companies' business activities. The company's brand, its products' trademarks, know-how, the costs of completed researches, developmental works and other intangible assets are becoming more and more important for both firms and their clients. Those factors, despite direct influence on current business activity and achieved by the company targets, have also impact on its image presented in financial statement. Thanks to this they are recognised as the most important contemporary value sources of business establishment.

Misidentification, underestimating their initial value, inadequate balance valuation or even omitting some elements of the intangible and legal assets in balance sheets, result in the fact that the company's image in its financial report becomes falsified. All the reasons mentioned result in the need of analysis and modifications of the existing accountancy regulations which concern identification, valuation and the presentation of the intangible and legal assets. From practical point of view the changes in the tax law are also recommended, because despite the tax law being completely separate field of knowledge to accountancy, in reality, especially in the reality of small and medium sized companies, compliance or very close similarity of both tax law and accountancy rules play huge role and eliminate many misunderstandings.

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[2] Toffler A.: Trzecia fala, Państwowy Instytut Wydawniczy, Warszawa 1985.

The intangible and legal assets are one of the most problematic fields of accountancy and the tax law. This situation is mainly the result of the difficulties with their proper defining and measuring their values. At first the analysis of the definition of the intangible and legal assets' element of should be accomplished and we should focus on their possible amendment to adjust to today's contemporary economic realities. The second important problematic field is their valuation, which is not the point of this elaboration.

1. The Importance of the Intangible Assets in Companies' Activities

In not too distant past the companies used to base their competitive advantage only on its capital and fixed assets. Such approach was begun by the Industrial Revolution in the 18th century, when the greatest importance for creating certain situation on the market and achieving economic advantages of the companies running business activities were their financial capital and fixed assets amongst which first and foremost were properties, machines and production equipment.

Nowadays the situation has changed and other elements decide about the economic advantages. Labour, especially physical labour, became cheap and its supply significantly exceeds the demand. Good financial company's condition used to be and still is vital reason when struggling against the competitiveness on the market. Unfortunately not always, as it used to be in the past, has it its result in assuring achieving economic advantage. It is no longer difficult for the companies to access the financial reserves. This is a direct result of common access to credits or loans. Thanks funds like venture capital even new firms may get large amounts of money to finance their investments. Thanks to high risk funds it is possible to obtain huge financial capital on risky and insecure activities which however are characterised as those with potentially high profit margin. Technology, based on the knowledge and the newest IT achievements reduced the money demand when producing the same thing, so we can gain bigger advantages from the same funds.

As for the tangible assets, that means machinery, equipment used in production etc., the situation has significantly changed in favour of intangible assets. So far an access to the tangible assets guaranteed achieving competitive advantage. In the era of evenness in accessibility to production factors the sources of competitive advantage should be searched in the intangible assets and in the quality features. The escalation of competitiveness on the market resulted in the growth of strategic meaning of the intangible assets. If a company struggles against other competing firms. How can you fight with this competitiveness? The things, which can be very supportive for certain companies and which may try to search for their competitive advantage are those assets and competences which are very difficult to be copied like:

a) recognised company's trademark and products' brands,
b) the ability to fast adaptations to market changes,
c) company's ability to introducing new products and new services on the market and which will allow outdistancing the rivals,
d) appropriately developed computer systems related with customer's service, handling production processes also trade and storage processes etc., which allow to minimise the costs of these processes.

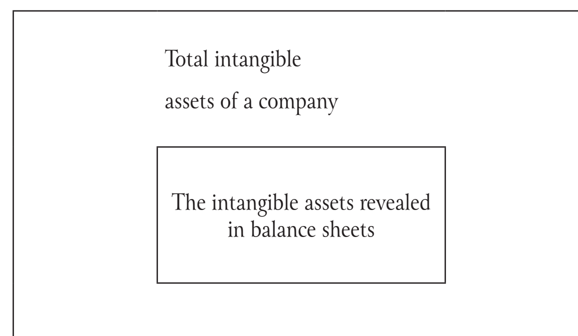
So, the former sources of competitive advantage have significantly devaluated and the intangible assets (new technologies, know-how, computers' software, patents, copyright laws, licences etc.), fast access to them, exploitation, the protection of sources and most of all the ability of identifying, valuation and presentation are in the centre of attention now.

The intangible assets play yet another important role. They make some basic element which makes the value of a company, which then makes basis to evaluate the company's development, management's effectiveness and the main determinant of taking economic decisions related with it. For a long time company's value used to be set on the basis of the fixed assets and it is them that were the main generator of company's worth. Nowadays, it is emphasised, that intangible assets function in two ways: they are a tool used in rivalry and are the main generator of company's worth which is clearly presented in financial statements' analysis, as a result of weakening the correlation between firms' market's value and the traditional indicators calculated on the basis of balance sheets and profit – loss calculations. Nowadays, the correlation between stock market value and intangible values is more and more accurately appointed.

The economy of the 21st century can therefore be called the economy of the intangible assets. According to the data mentioned by Low and Kalafut [3], 35% of the decisions of those people who manage investment portfolios are based on the intangible values. The research conducted by Ocean Tomo bank showed that over 80% of companies' values, which appear on S&P 500 Index are based on the intangible assets.

The intangible assets, as opposed to classic company's assets, are not easily identified, cannot be subjected to accountant's evidence and price valuation, which results in the fact that some of these assets are of the nature of the intangible recognised assets, priced and expressed in particular company's balance sheet. Some of them, however do not exist in balance sheet despite the fact that they have specific and very often significant market value. The relations between all company's intangible assets and their part revealed in balance sheets are presented in a diagram 1.

Diagram 1 – The Intangible Assets Contrasted with Company's Intangible Assets Revealed in Balance Sheets



The source: self study

[3] Low J., Kalafut P.C.: Niematerialna wartość firmy, Oficyna Ekonomiczna, Kraków 2004, p. 14.

The second group of the intangible assets – not revealed today in company's financial reports is often called in literature as an intellectual capital and it is claimed that it is the difference between the net value of the assets presented in balance sheets and the market value of the whole company.

2. The Intangible and Legal Assets in Polish Accountancy

One of more important rules of accountancy is the idea of a true and fair view of a company (TFV), which belongs to the superior accountancy rules. Primarily, this idea appeared in Great Britain and then it was accepted by other countries. Nowadays it appears in accountancy law regulations in many more countries. TFV states that a company running business activity ought to present in a true and fair way its financial situation together with accurate results of its business activity. The true view is described and understood as the depiction of wealth and financial situation of a particular company in as fair way as possible and in accordance with the truth. TFV excludes free shaping company's image depending on the situation, simply because it assumes depicting the reality in accordance with truth and facts without any embellishments or falsifying the situation.

In Polish legislation the rule of the true and fair view is not directly mentioned, however, the Accountancy Act[4] obligates companies to present wealth and financial situation in an honest and clear manner together with accurate financial reports. This Act states that actions, including economic operations, must be both included in the accountant books and shown in balance sheets in accordance with their economic content.[5]

The view on the conception of TFV can also be found in EEC Directive IV about the annual accounts' closures[6], where an entry is seen: „The annual financial report should present the true and fair view of company's assets and liabilities of the partnership, its financial situation and its profits or losses." In exceptional circumstances, if applying any regulation or directive was contradictory to the duty of presenting the true and fair view of the company, it is recommended to refrain from such regulation. The reasons for such refrain must be explained in the form of additional information included in the financial statement. Also the impact on the assets of such refrain, liabilities, financial situation and its profits or losses must be specified.

In the International Accounting Standards the true and fair view is achieved by applying appropriate accounting standards, also by the realisation quality features while issuing financial statements. Furthermore, IAS 1 – the Presentation of Financial Statements specifies that companies' financial statements should fairly depict their financial situation, financial results and the cash flow.[7] For the presentation to be true and fair, it is required that all the effects of transactions, other occurrences and conditions were ideally depicted. Such depiction must comply with the definitions and conditions which are set for assets, commitments, income and costs, which were presented in „conceptual guidelines for issuing financial statements". Applying appropriate standards causes, that the financial statement will meet reliable presentation's requirement, though in justified cases additional information will have to be provided.

Important reason for applying the TFV concept in reality is an accurate classification of owned intangible assets, which must ensure true, reliable and harmonious with the actual state presentation of company's intangible and legal assets[8]. Intangible assets are such elements which cannot be touched because they do not appear physically[9]. That is why they make one of the most difficult problematic fields of accountancy.

In Polish accountancy the element of the intangible and legal assets was defined by section 3 paragraph 1 item 14 of the Accountancy Act and in accordance with this law the intangible and legal assets are those which were acquired by a company, counted as the fixed assets, property rights – suitable for economic usage in predicted time of economic usage longer than a year, intended to be used for company's purposes. In particular they are:

a) copyright property law, licensees, concessions
b) inventors' rights to their inventions, patents, trademarks, etc.,
c) know-how.

Analysing the literal meaning of the definition it is not difficult to see that, in accordance with Polish accountancy law, to the intangible and legal assets can be counted only those elements which were purchased by a company. This means those ones which were paid for, given in the forms of reports, issued for free, including donations – the possibility of producing such element by the company itself has not been foreseen.

Furthermore, each element of the intangible and legal assets must fulfil three conditions stated below:

1. the expected period of company's economic usage must last longer than a year,
2. it must be suitable for economic usage and
3. it must be intended for company's economic needs

Both acquired legal rights and long-term periodical financial settlements of particular sort of costs, which are intangible assets, are ranked as the intangible and legal assets – from the sort's of element point of view. The Accountancy Act counts copyright property laws, licensees, concessions, inventors' rights to their inventions, patents etc., to especially distinctive

[4] Accountancy Act 29 September 1994 r. (Law Paper 2009 No: 152, item 1223).
[5] Article 4 of the Accountancy Act.
[6] Directive IV of the Council 78/660/EEC dated 25 July 1978 r. about annual accounts' closures of some sorts of partnerships (Law paper. UE, 1978 No 222, entry 11).
[7] §15 International Accounting Standard No 1 – The presentation of financial statements.
[8] The second very important element is true valuation of priced intangible and legal assets, but the issues of this valuation are not the subject of this dissertation and that is why they were omitted in further discussion, which focuses on the definition itself and on the identification of the intangible and legal assets.
[9] Hendriksen H.A., van Brenda M.F.: Teoria rachunkowości, Wydawnictwo Naukowe PWN, Warszawa 2002, p. 628.

property rights. Property laws are generally understood as the rights on basis which entitled subject has certain property benefits (such as the right to receive payment, the right to receive interests, etc).

Apart from property rights, to the intangible and legal assets the Accountancy Act counts also very specific sorts of financial settlements' periodical costs, which include two titles such as:

1. the wealth of a company and
2. the costs of completed researches and development works.

The wealth of a company was defined under the article 33 section 4 of the Accountancy Act, as the difference between the purchasing price of a certain company or its organised part and a smaller than that one fair value of the established net assets. If the purchasing price of a certain company or its organised part is lower than the fair value of the established net assets, then the result is the negative firm's value.

The rules of recognising the costs of completed researches and developmental works were described under the article 33 section 2. According to this rule the costs of completed researches and developmental works are counted as the intangible and legal assets when:

a) the product or the technology of production are strictly established and bound with them costs of the developmental works are reliably described,
b) the technical usefulness of a product or technology was stated and the proper documentation was provided and on their basis the company decided to produce these products or applying the technology,
c) the costs of developmental works will be covered, according to predictions, by the income which either comes from the sales of these products or from applying the technology.

As for the intangible and legal assets, Polish accountancy is based on the International Accounting Standards [10], so many solutions in Polish accountancy are analogous to the ones in the international standards. This is the result of a few factors one of which is the Accountancy Acts' harmonisation within European Union, to which Poland has also been belonging since 2004.

3. The Intangible and Legal Assets in Polish Tax Law

The tax law sets completely different goals to accountancy. In some sort of simplification it can be stated that the main aim of the tax law (all over the world, not only in Poland) is gaining appropriate income to country's budget in order to secure certain country's expenses, killing the risk of lack in regularity of budget collections and making sure that the taxation base will not be reduced. This could put at risk the realisation of the fiscal policy. The consequence of such state is that the tax law does not accept the rules of accountancy, which results in various differences, first and foremost in understanding the result categories [11], and also in classifying balance categories.

As for defining the intangible and legal assets in Polish tax law, according to an entry in law article 16 b section 1 of the company's income tax law act [12], the intangible and legal assets are understood as, acquired and suitable for economic usage, on the day in which the law was permitted to use, elements:

1. eligibility to residential premises,
2. eligibility to business establishment,
3. eligibility for a single-family house within housing cooperative,
4. copyright or acquired property rights,
5. licences,
6. the rights defined in the Act on 30 June 2000 r. – Business Proprietorship, Law paper 2003 No 119, item 1117),
7. value being an equivalent of gathered information related to knowledge in industrial, commercial, scientific, or organisational (know-how) fields;

These elements must additionally fulfil strictly set in the law act regulations such as:

a) expected period of their economic usage must last longer than a year,
b) they must be used by the tax payer for the purposes of a business activity run by him
c) must be handed over by him for usage purposes on the basis of a licence contract (sub-licence), a lease for premises etc.

Similarly to the accountancy, to the intangible and legal assets are also counted:

a) the value of the company, if this value was raised as a result of purchasing a company or its organised part as:
   - in a form of buying,
   - accepting for payable usage. The depreciation allowances in accordance with chapter 4a, are the user's responsibility,
   - investing in the partnership on the basis of commercialization and privatisation laws,
b) the costs of the developmental works positively completed, which can be used for tax-payer's business activity if:
   - the product or technology of manufacturing are strictly established and bound with them the costs of developmental works are lawful and reliably set, and
   - the technical usefulness of a product or technology was properly documented by the tax-payer and on these basis the tax-payer decided to begin the products' production or decided to use the technology, and
   - from the documentation bound with the developmental works appears that the costs of developmental works will be covered either with expected profits from the sales of those products or from using the technology.

Comparing the two definitions: the accountancy definition and the tax definition it is clear to state that they are conver-

[10] International Accounting Standard No 38 – Intangible assets.

[11] What counts here is understanding the costs and income, the rules of their recognition and the rules of setting tax financial result which is the base for calculating taxes.

[12] The Law Act on 15 February 1992 r. about the company income tax (Law paper 2011 No 74, item. 397).

gent. First and foremost, the tax definition, by analogy to the the accountant one, requires that only purchased elements were counted as the intangible and legal assets. This means that if a company produces an intangible and legal asset on its own, this element will not be mentioned in the balance sheet.

As for the differences between two definitions, they concern only two fields, such as:

1. the tax law includes a certain catalogue of the intangible and legal assets while the accountancy regulations define elements' criteria for the intangible and legal assets and show an 'open' list of the particular intangible and legal assets' elements,
2. the tax law treat differently to the accountancy:
   a) the right to timeless usufruct of land,
   b) eligibility to a residential premises,
   c) eligibility to business establishment,
   d) eligibility for a single-family house within housing cooperative,

Which for tax law purposes are categorised as the intangible and legal assets, while in accountancy they are categorised as fixed assets [13].

Summary

The aim of companies' financial statement preparation is to deliver information about its financial situation and achieved by the company results, which will be useful for wide range of users while taking right and accurate economic decisions. It is necessary to ensure the credibility of information presented, so neither decreasing nor increasing any presented in balance sheets values of wealth elements, sources of funds or even the result of company's financial situation are allowed. It is expected that the economic image of the company, presented in its financial reports, is true and fair. Experience gained in the 21st century shows, that the most important element of company's assets, the element which is responsible for the value of a company and also company's competitive ability are the intangible assets. With reference to many companies and many financial reports it is ok to say that the company's image improvement presented in its financial report depends on completeness, correctness, the point of view and the valuation of the intangible company's assets. Unfortunately the issues related with the intangible assets, their perspectives, their valuation and their revealing constitute big problem and challenge for economic sciences, especially for the science of accountancy.

Although, there are no bigger problems related with defining and identification (also valuation) of the intangible assets purchased by the company, there are many problems and doubts related with a group of the intangible assets created by the company itself. Such elements are not enclosed, valuated or presented in neither Polish accountancy nor in Polish tax law. The problem makes the definition of a particular element of the intangible and legal assets which admits the classification of only purchased elements, not those produced by the company.

The list of chosen differences and similarities of the definition of intangible and legal assets' element in the view of Polish accountancy and Polish tax law are presented in table no 1.

Table no 1 – Basic differences between the definitions of intangible and legal assets' element in the accountancy and the TAX law

	Accountancy	TAX law
Definition		
Analogy	The intangible and legal value is a non-money and purchased element of the assets, without its physical appearance, fulfilling following criteria: a) used in production, delivering goods or providing service by the company, b) remaining under company's supervision, c) from which in the future the company will gain economic profits.	
Divergence	Example titles which are counted to the intangible and legal assets are listed. This is still an 'open' list	The 'closed' list of titles which are counted as the intangible and legal assets is defined.
	Stated below elements are counted as the **fixed assets**:	Stated below elements are counted as the **intangible and legal assets**:
	1. the right to timeless usufruct of land, 2. eligibility to a residential premises, 3. eligibility to business establishment, 4. eligibility for a single-family house within housing cooperative	

Source: self study on the basis of the LAW ACT, 29 September 1994 r. about accountancy and LAW ACT, 15 February 1992 about company income tax

Such approach causes that the expenses spent in order to produce the intangible and legal assets by the company itself are moved to costs, which results in:

1. from the accountancy point of view – in disproportion of company's image in its financial statement,
2. from the tax point of view – lowering taxation base by company's income tax, and consequently lower tax paid annually by the company.

In order to eliminate mentioned above anomalies the definition of the intangible and legal assets' element should be changed both in the field of accountancy and in tax law.

[13] See Government Order on10 December 2010 r. The Classification of Fixed Assets (Law paper 2010 No 242, item. 1622).

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4. Directive IV of the Council 78/660/EEC dated 25 July 1978 r. about annual financial statements of some sorts of partnerships (Law paper. UE, 1978 No 222, entry 11).
5. International Accounting Standard No 1 – The presentation of financial statements.
6. International Accounting Standard No 38 – Intangible assets.
7. Government Order on10 December 2010 r. The Classification of Fixed Assets (Law paper 2010 No 242, item. 1622).
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