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A REGULATORY COMPETITION?
A CRITICAL COMPARISON OF THE EXTANT GUIDELINES AND RECOMMENDATIONS ON IC STATEMENTS AND INTANGIBLES REPORTS

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Abstract

In parallel to the growing importance of the intangible economy in the last few years an increasing number of guidelines, recommendations and similar documents dealing with intangibles reports, IC statements and alike have been published. These documents are the result of various collaborations between researchers, companies, industrial organisations, consultants and government officials. The institutions and research initiatives include the Danish Agency for Trade and Industry (DATI), the Meritum Project, the International Federation of Accountants (IFAC) and the Society of Management Accountants of Canada (SMAC).

Even though these guidelines on intangibles reporting are not intended to provide ultimate answers, they aim to support organisations in the process of definition of: 1) what is their vision; 2) what resources they actually have and which ones they should increase; 3) a minimum set of indicators to measure intangible resources and activities; and 4) the information that could be useful in practice for the preparation of an Intellectual Capital Report.

In the light of the lack of a common international framework on the topic of intangibles reporting as yet, the paper aims to compare and contrast the above documents in order to identify common points and idiosyncrasies in the recommendations regarding the reporting of intangibles. This deconstructionist and comparative exercise revolves around five fundamental categories which connote IC reports: a) objectives and intended users; b) formal and procedural aspects; c) structure; d) contents and indicators; and e) foundational concepts.

As a result of the above comparative investigation, the paper will attempt to verify whether it is possible to derive a unitary model for reporting on intangibles which could be able to respond to the different information needs of the various constituencies.

A tentative conceptual mapping of the documents will also be proposed in order to provide a sort of logical compass for the competition between the current guidelines dealing with the reporting on intangibles and intellectual capital.

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1. Introduction

Globalisation, technological change, increasing competition are only some examples of the numerous factors that from the nineties are pushing companies to innovate and restructure their business models. In this context, new value drivers have emerged which are more and more closely associated with the multifaceted concept of Intellectual Capital.

It is also appearing progressively clear that the traditional accounting, based on the notions of transaction and historical cost, is becoming inadequate to measure the new set of critical resources, the so called Intangibles, which are deeply involved in the innovative value creation processes. In the effort to find measures able to "capture" the more authentic value of the enterprise, many academics and practitioners have begun developing models and metrics to quantify and visualise Intangibles, turning their attention in particular to a new form of reporting labelled Intellectual Capital report (also defined as Intellectual Capital Statement). This tool is considered necessary by a growing number of companies because of its capacity not only to monitor and underline intangible resources (for internal uses), but also to show stakeholders the "hidden" portion of company worth by portraying its most important value drivers.

This is the reason why, in parallel to the growing importance of the intangible economy, in the last few years an increasing number of guidelines, recommendations and similar documents dealing with intangibles reports, intellectual capital (IC) statements and alike have been published, which are to some extent in competition between them. These documents are the result of various forms o collaborations between researchers, companies, industrial organisations, consultants and government officials. The institutions and research initiatives include the Danish Agency for Trade and Industry (DATI), the Meritum Project, the International Federation of Accountants (IFAC), the Nordika Project, and the Society of Management Accountants of Canada (SMAC).

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The investigation of the stated *objectives and intended users* will allow us to better frame the different ways to conceive IC reports, which inform the various documents considered.

The analysis of the *implementation procedures and practical issues* related to the preparation of an IC report includes issues like the implementation practices, sources of data, the transitional period, the date of implementation, the identification of target companies and so on.

The section devoted to the *structural aspects* of IC statements relate to the "building blocks" which are suggested by the different guidelines vis-à-vis this type of reports.

As to the *contents*, the analysis aims to compare the different indicators put forward by the documents to measure company Intellectual Capital.

Finally, there will be carried out a comparison between the *foundational concepts* emerging from the documents analysed, such as the very definitions of intangibles and intellectual capital, the view of knowledge (e.g., distributed vs. concentrated), the vision of the firm (e.g., entity vs. proprietary oriented), the assumed management style (e.g., collaborative vs. centralised), and possibly the underlying firm strategy (e.g., focussed vs. differentiated) which may support the adoption of IC statements. It seems important to note that the conceptual aspects are not always explicitly mentioned in the documents analysed, but sometimes they result from a systematic and comprehensive interpretation of the texts.

As a result of the above comparative investigation, the paper will attempt to verify whether it is possible to derive a unitary model for reporting on intangibles which could be able to respond to the different information needs of the various constituencies.

Three sections will follow this introduction. The first section offers a presentation of the documents examined. It is important to underline that the documents here considered are only those whose aim is explicitly to present guidelines supporting managers in the preparation of an Intellectual Capital report. These documents are the Meritum Guidelines, the Dati Guideline, the IFAC/SMAC Study, and the Nordika Project report.

The second section presents a comparison between the above documents using different perspectives (the mentioned five categories). Since now it seems useful to clarify that the aim of this work is not to make a comparison of the guidelines per se (their purpose, target audience, marketing strategy, and so on), but to compare the different model of IC report they suggest. In this sense, we would defer to another paper the meta-analysis of the text.

Spreading from this analysis some concluding remarks will be presented and a general mapping of these documents will also be proposed in order to provide a sort of logical compass in the potential "jungle" of the current guidelines dealing with the reporting on intangibles and intellectual capital.

2. The basic features of the documents

In this section the origin of the four documents offering some guidelines for the preparation of an IC report will be briefly presented. These documents are the following: the Danish Guidelines ("A Guideline for Intellectual Capital Statements"), the MERITUM Guidelines ("Guidelines for Managing and Reporting on Intangibles"), the IFAC Study no. 7 (strictly related to another document produced by the SMAC in 1998), and the Nordika Guidelines ("Intellectual Capital – Managing and Reporting").

THE MEASUREMENT AND MANAGEMENT OF INTELLECTUAL CAPITAL – An introduction, by IFAC, 1998

This study was commissioned by the Financial and Management Accounting Committee (FMAC) of the International Federation of Accountants (IFAC) to discuss some of the major issues surrounding the measurement and management of intellectual capital and the accountant's role in this process. It is intended to provide an introduction to the accounting challenges and opportunities associated with intellectual capital management by discussing its underlying concepts and describing merging practices. The Study no. 7 is therefore designed to support professionals in the difficult task to develop an IC report and to build public awareness, understanding and demand for this type of service. In substance, the choice of this document is justified by the will to consider the practitioners' point of view.

A GUIDELINE FOR INTELLECTUAL CAPITAL STATEMENTS – A key to knowledge management, by the Danish Agency for Trade and Industry (DATI), 2000

The guideline is the result of a unique collaboration of researchers, companies, industrial organisations, consultants and government officials. It is based on practical experience as well on solid research into this field lead by Professor Jan Mouritsen (Copenhagen Business School) and BDO Professor Per Nikolaj Bukh (Aarhus School of Business) from Denmark.

The Guideline for intellectual capital statements signifies a major R&D achievement of a project co-ordinated by the Danish Agency for Trade and Industry (which is part of the Ministry of Trade and Industry) and started in 1998. Seventeen Danish companies[1] have contributed to the project by preparing two sets of intellectual capital statements each. As the seventeen companies are not representative of the Danish corporate sector, the Guideline is expected to develop as more companies compile IC reports according to the Danish Guidelines; for this reason the document shows some examples of companies that have prepared IC statement (in particular Coloplast, Nelleman Konsulenterne, Biggeplandata). Arthur Andersen has consulted on the project and the Copenhagen Business School and the Aarhus Business School have been co-responsible for the research elements of this project[2].

With the publication of this Guideline the first stage of the project is accomplished. At the moment, the project is completing the second phase where over 100 companies are preparing intellectual capital statements based on the Guidelines. The purpose is to test the Guideline on a wide variety of organisations and, on the basis of this experience, to present an adjusted Guideline at the end of 2002.

With this initiative Denmark has taken the international lead in being the first country to develop a guideline at a national level for preparing intellectual capital statements.

INTELLECTUAL CAPITAL – Managing and Reporting, by the Nordika Project, 2001

This report is the main product of Nordika[3] – a project on intellectual capital initiated by the Nordic Industrial Fund – in collaboration with a Task Force of government representatives and a Round Table drawn from business and professional associations in the Nordic countries.

The Task force and the Round Table have contributed to and commented on the report. Authors of, and responsible for, the report are Henrik Jensen, Project Manager, Consultant to the Nordic Industrial Fund and Professor Hanno Roberts, Norwegian School of Management.

The document gives companies an overview of the vast number of possibilities and mainstream approaches for using, managing and reporting on IC. It intends to help decide the right approach to follow in this respect. The document also provides some examples of Nordic companies that have worked with implementing IC management and reporting, and presents a number of cases, illustrating how companies have produced their IC reports (e.g., Cowi, Celemi, WM data).

[1] The companies involved in this first phase of the Project are: A/S Danish Shell, ATP, Byggecentrum, Byggeplandata, Carl Bro Group, Coloplast A/S, Cowi, Dansk System Industri A/S, Dator A/S, The Danish Insurance Institute Rungstedgaard A/S, Hofman-Bang A/S, Hotel Impala A/S, Kommunedata A/S, Nellemann Konsulenterne A/S, Meku A/S, Systematic software Engineering A/S, Tele & Data.

[2] Additional information on the project is available on www.efs.dk/icaccounts.

[3] Additional information on the project is available on www.nordika.net.

GUIDELINES FOR MANAGING AND REPORTING ON INTANGIBLES – Intellectual Capital Report, by the MERITUM Project, 2002

The Meritum Guidelines are an outcome of the MERITUM Project (Measuring Intangibles to Understand and Improve Innovation Management), which has been funded by the European Union within the framework of TSER (Targeted Socio-Economic Research) Programme. In this Project researchers from two European countries (Spain and France) and Four Nordic countries (Denmark, Finland, Norway and Sweden) collaborated. The following institutions have been involved: IADE-Autonomous University of Madrid and the University of Seville (Spain – Coordinator), Groupe HEC (France), Copenhagen Business School (Denmark), the Research Institute of Finnish Economy and the Swedish School of Economics and Business Administration (Finland), Norwegian School of Management (Norway), and Stockholm University (Sweden).

The basic research has been carried out between November 1998 and May 2001. Another research process has followed, starting with a thorough analysis of the economic nature of intangibles and a discussion on their definition and classification, and ending with a *Delphi* analysis thanks to which this document gathers the consensus of a group of experts with renown reputation in the field of Economics and Business Administration.

3. A critical comparison

In order to facilitate a comparison, each document will be "deconstructed" as follows:

- *Objective and intended users* (internal/external) of the report;
- *Implementation procedures* and *practical issues* related to the preparation of the report;
- *Structural aspects* (elements of IC report);
- *Contents* (indicators suggested, characteristics, categories, and so on);
- *Foundational concepts*.

Even if it is not always possible to find the above listed information in all the examined documents, we think that to fix a common scheme of comparison is useful to the help the "deconstructive" process.

3.1. Objective and intended users of the report

According to the IFAC Study no. 7 the users are both managers and stakeholders and the objective of the report is not explicitly mentioned.

On the contrary the Danish Guideline gives special attention to the explanation of the role of IC report within and outside the company. The Guideline in fact states that IC statement is part of the process of knowledge management in the company. The IC report shows what a company does to enhance its knowledge resources. It reports on the company efforts to obtain, develop, share and anchor the knowledge resources required to ensure future results.

In this sense the IC can contribute to creating value for the company by improving the company's strategy for what it must excel in order to deliver satisfactory products or services to its customers.

However, in the Danish perspective IC statement is not only a strategic tool for adding value to the company (helping managers to organise knowledge resources), but it is also a communication tool for inducing employees, customers and others to engage this process. In this sense it should be publicly available

It seems now clear that the IC statement is not primarily intended to account (in financial terms) for the current portfolio of knowledge resources at any particular time. This is the reason why it cannot be used to explain the difference between book value and market value.

Starting from these premises, the target of the report is represented by the potential customers, the employees and the other stakeholders (crucial to the company's competitive power). In fact it can be internal and/or external[4].

This Nordika vision is very similar to the Danish one, because both underline that the accounting purpose of the report is secondary as regards understanding the contribution of IC to the value creation process. Indeed, from the Nordika point of view the report should not only estimate the financial value of IC but should explain the role of IC (and of knowledge in particular) in creating value for the company: how it is built, retained and so on. The report should cover the range of knowledge resources at the disposal of the company, how they interact, and what the company is doing to develop them for the exploitation of business opportunities. It is a tool for managing knowledge and other intangibles.

The intended users are both internal and external but, according to the Nordika Guidelines, companies that choose to work with IC reporting are in general motivated by internal rather than external demand.

Like all the other documents, the MERITUM Guidelines assert that the report identifies IC as critical intangible resources and activities, linked to the company strategic objectives. The model they suggest points at the connectivity of these critical resources and activities and focuses on how to create value for the company's users ad other stakeholders organising properly the three elements of IC (see section 3.5).

The target is both internal (managers) and external (stakeholder) because "the differences between the internal and external use of the information on intangibles tends to blur since outsider's perception of how value is created increasingly take account of internal management systems" (Vickery, 2000).

From the comparison of the IC report purpose it can be concluded that according to the various documents IC reports (or IC statements) do not estimate only the value of IC as such, but also, and especially, what IC means in terms of value creation. It can also be added that all the documents recognise both an internal and an external use of this type of reports.

3.2. Implementation procedures and practical issues

It seems clear from the IFAC Study no. 7 that in the process of creating an IC report is involved first of all the management accounting whose task is identifying, valuing, reporting, and participating in the management of the intellectual capital of the firm. In particular, accountants in applying their skills to creating and integrating knowledge within their organisations have a triple role:

- classify knowledge-based assets;
- identify how they form intellectual capital and therefore, how they are linked to the overall strategic goals of the organisation;
- evaluate how they contribute to the intellectual capital of the firm and compare to the intellectual capital of other organisations.

The time necessary for the implementation process is not specified: "it is a long way to go for general accepted and endorsed practices to evolve".

[4] It should be noticed that the Guideline *per se* is an internal tool, however the reporting section concentrates on the way to prepare external report.

The Danish perspective appears much more comprehensive than the IFAC one because, after specifying that managers are the first subjects involved in the development of IC statement, it concentrates its attention more on the concrete preparation process of IC statement.

This process is divided in four phases:

a) ***Knowledge narrative***: describes how the company ensure that its products or services accommodate the customer requirements and specifies how the company has organised its resources to achieve this. The leitmotiv in the knowledge narrative is the explanation of the chosen knowledge management strategy behind structuring, applying and developing the company's knowledge resources It should therefore establish the connection between the user and the company's know-how.

Formulating a knowledge narrative is a creative process (it is different from presenting more conventional strategic objectives) and include issues like:

- the company mission with special regard to the users
- what use value (of a product or a service) the company offers to its customers
    - The user's situation and his need for company's product and services)
    - The special features of the product/service with regard to how this will benefit the user
- what particular condition of production and how do they interact with special demand for knowledge resources to be structured trough knowledge management. The types of knowledge resources required for the particular companies are very different.

b) ***Management challenges***: set of challenges derived from the knowledge narrative (that represents the ambitions).

Identifying management challenges means to defining critical relationships (between the use value and the knowledge resources). There is more than one way to translate knowledge narrative into management challenges.

Knowledge narrative and management challenges have to take the form of a coherent tale: "the knowledge management strategy".

c) The management challenges are further translated into ***actions*** (implementation of the ambitions). These actions are related to knowledge resources in connection with customers, employees, processes and technologies or frequently a combination of these. Each action is tied to one or more ***indicators*** measuring how far these actions have been implemented.

d) ***Reporting***: when the knowledge narrative and the management challenges are defined, they are put together in a report. The statement communicates the knowledge narrative and the management challenges, and it documents the actions that have been implemented; in keeping with best practices it also sets out the applied accounting policies and reflects on the credibility of the IC statement. There are two types of reports: internal and external (it might be more detailed). The external reports on the company strategy for knowledge management in text, figures and illustrations.

Unlike the above documents (mentioning only the managers between the subject whose task is the implementation of an IC report), the Nordika Guidelines make an effort to represent different groups of subjects involved in this process. The most relevant role is duty of all CEOs, and projects managers from financial department, IT department, HR department or other departments.

In second position there are board members, executives, middle managers and accountants. But Nordika also specifies that implementation, as a learning process, should involve the major part of the company and stimulate a constructive debate.

A second important point underlined by the Nordika is the necessity of a relevant (logical and consistent with the facts) and reliable information, even if sometimes the information reported can be very difficult to check. The reliability of information has much to do with the quality of the internal information system (e.g. practical approach to the collection of data). A company can also use external experts to device or adapt its IC approach. Using such collaborators makes it clear that the data have been gathered and interpreted by experts using professionally recognised methods and standards. In the long-term this can also boost the confidence of the broader community in the company and in IC reporting generally. Some practical suggestions to establish reliability are:

- opening a dialogue between the company and those to whom the reporting is addressed;
- being open about motives, shortcomings, important excluded information, and IC downsides;
- ensuring that the presentation looks accurate and credible;
- assuring the quality of the information system, data collecting methods and reporting principles;
- stimulating a public debate.

Besides these issues the Nordika Guidelines set also the following four focal points for the implementation process:

1) *identification of the idea* of the project
   A) overall purpose of the project and link to the company strategy
   B) changes required
   C) priority and importance of each aspect of the project

2) *organisational preparation*: there is no one-size-fits-all solution, it depends on situation, culture, atmosphere
   A) tradition (if any) the company has in terms of tools for reporting
   B) kind of support and enthusiasm can the project expect from the middle managers/other employees/other groups
   C) internal/external culture for communicating information is open/closed

3) *previous experiences* with IC
   A) experience the company already has on IC
   B) existing resources relevant to IC measuring and reporting
   C) how well IC is integrated in your company business model, explicitly or implicitly

4) *cost* of measuring and reporting IC (not only financial but also in terms of manpower, time and so on). The more diversified the company's product and market portfolio, the more energy should be devoted to the work of describing and measuring, and the more demanding such tasks are likely to be. To calculate the cost the company should answer the following questions:
   A) is the company's product/market portfolio diversified or simple?
   B) how knowledge-intensive is the company?
   C) how much time and manpower should be dedicated directly to the project?

Another practical suggestion of the Nordika document relates the frequency of the IC report: it should cover the same period of the annual financial report.

Like the above analysed documents also the MERITUM Guidelines present the managers as the most important subjects involved in the preparation of the information inside the company. But in this document there is a clearer intention to make a separate analysis of the different tasks:

a) development and design of measurement system, under the responsibility of:
   - top/senior management;
   - external/internal consultant;
   - human resource mangers;
   - accounting and financial mangers (CFOs);

b) development of indicators (concrete preparation of the intellectual capital report):
   - top management.

Managers can obtain information by company databases, internal documents and review, surveys, interviews, accounting system and external sources.

In the MERITUM perspective the level of disclosure is up to the firm and the frequency depends on the specific needs of management[5], nevertheless it is specified that it has to be similar to the periodic accounting disclosures (minimum the fiscal year)

But maybe the most important aspect in the MERITUM approach is that the implementation of the IC report is seen as the result of the "Management of Intellectual Capital". This consists of three phases: first the *identification of intangibles* (resources and activities), second the *measurement* (indicators), and third the *action* (evaluation of results). From the action there is then a feed-back towards the identification of relevant intangibles because the implementation is a learning process. It seems important here to underline that the described phases are susceptible of criticisms. For example in the first phase it could be very difficult find the right intangible activity to develop or improve each intangible resource because you can't base on the past experience. In order to do that you should have a very good learning process, and even if you have it the context always changes.

Beyond the single specificity of the four compared documents, a common rule of implementation can be derived. In fact for all the documents to launch and implement an IC project is always necessary to identify at least two issues:

- definition of knowledge and its practical consequences;
- data, information and indicators required.

Another important convergence relates the fact that the managers are always the most important subjects involved in the implementation process.

Last but not least the implementation process is almost always explicitly defined as a learning process.

Therefore, it seems important to notice a relevant difference in the identification of the phases (or different steps) to implement IC report.

3.3. Structural aspects

The IFAC Study no. 7 does not proposes a particular structure of the IC report, it rather points its attention on the concrete way to measure intellectual capital and intangible resources. The analysis of this topic will be object of the section 3.4.

Contrary to the IFAC Study, the Danish Guideline proposes a clear design of the IC statement structure. This is represented in Fig. 1.

The general layout it is a table of contents showing the structure and the interrelationship between the individual elements of the IC statement and the director's knowledge report on the objectives. It also shows the content of the company's IC statement, with a presentation of the knowledge narrative and of the management challenges, preferably carrying their signatures. Another important element of the layout is the presentation of the company (size, products, organisation).

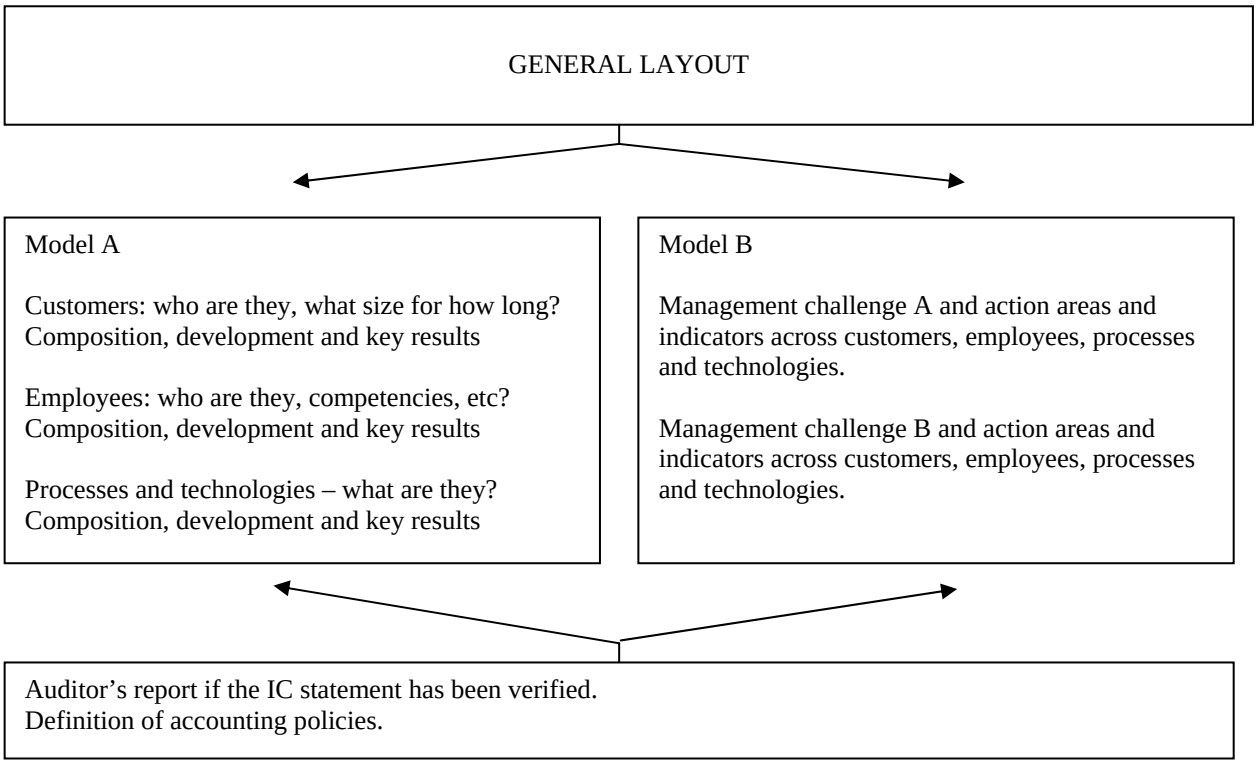
The general layout is followed by a description of the three fundamental resources of the company (customers, employees, processes and technologies) and the related management challenges (see section 3.2.).

[5] To establish the frequency is advised a cost-benefit analysis.

But the most innovative element in the Danish structure is the role of auditor. The auditor report is useful[6] because to be effective an IC statement must qualifying as being credible. The basic quality assessment criteria suggested in the document are the following:

- relevance (for the decision-making process);
- reliability (they must allow for verification);
- clarity;
- materiality (figures an measurement must be included);
- completeness (view of the company's situation);
- substance (real issue not formality);
- gross measurement (all measurement must be reported separately);
- neutrality (of the impact on the overall view);
- comparability (trough different years).

Fig. 1. The structure of the IC statement in the Danish Guideline.



Source: DATI Guideline.

A possible criticism could be the fact that these quality criteria can be conflicting on certain points, therefore the overall criterion to adopt is whether the IC statement is able to strike a balance between relevance and reliability.

In its last part the IC statement has to specify its accounting policies (the adopted measuring methods). The accounting quality requirements and the basis for their reported weighting should also be included. The time period for IC statement can be specified as part of the accounting

[6] At the moment there are no statutory requirements for the verification or auditing of intellectual capital statements. It is therefore up to the company to decide whether such procedures will lead to improve and more credible intellectual capital statements – considering the resources required.

policies. These are important details because allow the reader to understand and interpret the IC statement content correctly.

Similarly to the IFAC Study, the Nordika Guidelines do not suggest a particular structure of IC report but they anyway present a list[7] of the points an IC report should always touch:

1) the overall functioning of knowledge (relation between company and markets, products and customers; interaction between knowledge and other resources; influence of knowledge in the realisation of value);
2) opportunities (markets), goals and challenges;
3) resources;
4) actions (company's activities associated with using and developing its IC);
5) relationships;
6) non-financial focus = not concerned with physical and financial assets (though the measures can be both financial and non-financial);
7) indicators (more than just numbers: they should explain and visualise the effects of the actions by illustrations and graphs.

But between the analysed structures probably the most clear is the one designed by the MERITUM Guidelines. It is composed by three parts:

a) *a vision of the firm* comprising a statement of the management team on the corporate strategic goals and their related critical intangibles;
b) a summary of *intangible resources and activities* (referring to three categories of Intellectual capital; activities should be divided into improvement activities and monitoring activities)
c) a system of *indicators* (see section 3.4.) to measure resources owned and activities executed (internal use) and to allow external parties to estimate correctly the firm's future expected earnings and risk.

The structures described are connected by a *file rouge*: the constant presence of the identification of the relevant intangible resources and their related activities, and the presence of some sort of indicators (most of times not stricly fixed) to measure the results.

3.4. Contents (indicators)

The IFAC Study no. 7 does not suggest own indicators to measure IC because its principal intention is to make a sort of "*collage*" of the knowledge accumulated until then on the issue of IC report. For this reason it cites different measuring models and indicators coming from academic and professional perspective and lets the company free to choose the best indicators according to its needs and activity. For example the Study presents the Skandia model, developed by Edvinsson & Malone in 1997. This model consolidates 164 indicators into five main categories according to the primary focus they take – financial focus, customer focus, process focus, renewal and development focus, and human focus. The Study also describes some indicators proposed by SMAC in 1998 and some comparative indicators like the "Market-to-Book Value", the "Tobin's Q" and the "Calculated Intangible Value".

In the Danish Guideline the company freedom of choosing indicators is limited by the necessity of indicators strictly related to the identification of the actions that translate the management challenges into concrete activities (see section 3.2.). In this sense it cannot be fixed a general

[7] It seems important to clarify that the Nordika Guideline represents already an initial effort to summarise the content of other models regarding the implementation of IC reports. The above list for example is the result of the common points identified through the analysis of the Intangible Asset Monitor, the Danish Guideline and of the MERITUM Guidelines.

scheme of indicators because each specific indicator measures a specific implemented action[8]. In addition to this general rule the document presents four types of actions (one for each category of resources): actions towards employees, customers, processes and technology. As a result, the same four categories of indicators are proposed. Reading the Danish Guideline it can be noticed that there is no perception that there is any direct connection between input and output. The priority of this Guideline is to explain how companies can make their own IC statement: this is the so called "do-it-yourself approach..

Also the Nordika Guidelines confirm the lack of a fixed scheme of indicators, because they depend on the company specificities. From the Nordika point of view[9] what is important is develop indicators having the strategic purpose to make visible IC in order to generate maximum value. More simply, indicators have to establish how to work with the knowledge resources of the company, and to built IC that create value; in this perspective they have very little in common with the traditional indicators used to run the company, because they have the double role (instead of unique) of *measurement* and *visualisation.*

Developing useful indicators is described by Nordika Guidelines as a learning process because individual employees need to understand how the IC works but also need to educate each other on what is important to their work (educational techniques are useful: e.g. cases reading speeches from people). More in general indicators should represent what *everybody* understands as the most important aspects of the company: this implies virtual unanimity at all levels. In order to identify such indicators some technical criteria are hinted:

- precision: small margin of error increase information value and motivation (trust in the system);
- objectivity: preferably no self-evaluation;
- timeliness: short period between available measurement and underlying activities;
- simplicity: understandable terminology helps to create identity.

A further remarkable concept stressed by in this document is the ***dynamic perspective*** (see also section 3.4.). Adopting this perspective on the organisation means not only measuring flows, but also changing the measure themselves (indicators) with some frequency according to the knowledge processes.

To analyse the Meritum Guidelines regarding the indicators it has to be pointed out that they are identified in the second phase of the already described process of "Management of intellectual capital" (see section 3.2.).

Likewise the analysed approaches the Meritum Guidelines do not fix the indicators *a priori*, because they are firm specific, but they confine themselves to settle three categories of intellectual capital to which indicators must refer: human, structural and relational capital. Furthermore for each of these categories the Guidelines suggest to distinguish, whenever possible, between resources and activities. This finds explanation in the declared visualisation role of indicators (besides the measurement role) regarding what the company is doing with its intangibles in order to fulfilling its objectives. This doubleness of role has been already pointed out by the Nordika Guidelines.

In addition to this information the Meritum Guidelines show the three fundamental characteristics indicators should have:

- relevance;
- comparability; and
- reliability.

The document adds that the company is free to choose financial or non-financial indicators, nevertheless there is a little preference towards financial indicators because they make easier to

[8] Nevertheless, the Danish Guideline specifies that sometimes it is possible to find, if not one, at least a limited number of indicators for each action.

[9] The Nordika Guidelines specify that this section has been developed following Professor Hanno Roberts' point of view.

relate financial indicators of intellectual capital to the other financial indicators of performance. This point of view can be criticise because financial indicators are not necessarily the best indicators. In any case what it is important is that indicators provide a clear idea, to the extent possible, about the link between the firm's intangible resources and activities and, the wealth created with them. To satisfying this purpose it is clear that the set of indicators has to be *dynamic* in order to better reflect and visualise changes and learning effects accomplished by the organisation: this characteristic implies a frequent redefinition of indicators and recalls to mind the "dynamic perspective" mentioned in the Nordika Guidelines. A possible problem could be represented by the fact that the dynamic perspective is in conflict with the necessity to have a trend of indicators (comparability).

As already pointed out, all the approaches underline the importance of indicators in the preparation of an IC report not only as tools to measure IC but also as tools to visualise IC.

Concluding we could say that any of the documents fix a general scheme, they only present some categories of indicators (in particular by Danish and Meritum Guidelines) that differ a little bit. Another difference is the process leading to the identification of indicators. As a result of this two differences the reported information a little bit different.

A crucial converge relates the recognised double role of indicators (measurement and visualisation) and the relevance of their dynamism.

3.5. Foundational concepts

Three main foundational concepts have been identified in the four documents analysed. They are:

a) the definition and classification of intangibles and IC;
b) the concept of knowledge, the management style, and the vision of the firm;
c) the value creation process and the company strategy.

In the following the ways in which these concepts are addressed by the guidelines considered will be examined.

a) *Definition and Classification of Intangibles and Intellectual Capital*

The definition of intangible/intellectual assets presented by the IFAC Study no. 7 is the same proposed by the Society of Management Accountants of Canada (SMAC) in 1998:

> *"In balance sheet terms, intellectual assets are those knowledge-based items, which the company owns which will produce a future stream of benefits for the company".*

On the other hand intellectual capital can be thought of as the total stock of capital or knowledge-based equity that the company possesses. As such, intellectual capital can be both the end result of a knowledge transformation process or the knowledge itself that is transformed into intellectual property or intellectual assets of the firm. Intellectual capital is more encompassing than the traditional view of intangible assets: it is the ability that the members of the firm have to perceive, analyse, and react to both the changes of opportunity and threats in the environment, as well as the ability to collectively reorganise the allocation of resources to meet the new and ever-changing challenges involved in formulating an original modus operandi (not a reproduction of past patterns) that allows the firm to continue as a successful enterprise. IC is composed by three parts: human, organisational (structural) and customer (relational) capital.

The Study reserves a special attention to the definition of intellectual property, seen as a sub-classification of IC because includes resources legally defined and regularly recognised for accounting purposes.

On the same issue also the Meritum Guidelines express their point of view making a differentiation between the terms "intangibles/intellectual capital" and "intangible assets". The second is more restrictive because identifies the elements susceptible of being recognised as assets in accordance with the current accounting model. The definition of intangibles presented is an accounting definition underlying the lack of physical substance, the economic utility, the separability and the possibility to control it. A further crucial point introduced by the Meritum Guidelines is the difference between intangible resources and intangible activities. The intangible resources[10] represent a static notion because they can be measured at any given time, while the activities[11] imply an allocation and use of resources that are sometimes not expressed in financial terms, and consequently may or may not appear in the corporate financial reports (dynamic notion).

Passing to the concepts of intellectual capital, it is divided into the same three categories proposed by the IFAC Study (human, structural, relational). What is relevant is that IC is more than simply the sum of human, structural and relational resources of the firm, it is about how to let the knowledge of a firm for it and have it create value (Roberts, 1999). This can be achieved by creating the right *connectivity* between those resources through the appropriate intangible activities. Interpreted in this sense this concept is quite similar to the IFAC one.

b) *Concept of Knowledge, the Management Style, and the Vision of the Firm*

According to the IFAC Study no. 7 perspective, knowledge is a primary competitive factor in business today and its accumulation, transformation, and valuation lie at the heart of intellectual capital management. The analysis of this concept is based on Grant (1996) point of view. In his vision knowledge has to be distributed but this process requires certain organisational structure and cultures that facilitate communication, integration, and transformation of knowledge within the firm: the risk is that knowledge can only be exercised by the individuals who posses it[12]. This approach implies a collaborative management style and derives from an entity theory of the firm.

The concept of knowledge presented in the Danish Guideline concerns much more practice because knowledge is seen "in action" and not in a philosophical sense. This is due to the fact that the IC role is showing the ability and potential of the company to trade (see *knowledge narrative*, section 3.2.). Examples of knowledge: user's situation, awareness on competencies and on how interpersonal skills can be developed, practical skills, know-how, motivation, understanding how the need for knowledge is heading, and in general all the intangibles that can make a difference to the company.

Otherwise the Nordika approach points out a dynamic concept of knowledge, and in a larger sense of IC. They are both seen as "flows" and not "stocks" because of their continuous changing. Adopting this dynamic perspective on the organisation means not only measuring flows but also changing the measure themselves (indicators) with some frequency. From the Nordika point of view knowledge has to de shared through seminars, panels aimed at broad mobilisation of ideas and proposal: communication and dialogue are very important parts of the IC project. In this view the management style is based on a culture of openness (middle managers, other employees, external contacts and partners) and on an entity vision of the firm.

[10] Some examples of intangible resources are the worker competencies (human capital), intellectual property rights (structural capital), customer satisfaction or agreements with suppliers (relational capital).

[11] The Meritum Guidelines specify that there are three types of activities:

- develop intangible resources internally or acquire them externally;
- increase the value of existing intangible resources;
- assess the effects of the previous activities.

Some examples of intangible activities are training, R&D, specific marketing activities and surveys to asses employees.

[12] The Author asserts that in this case the shareholder value approach would be challenged.

Finally, it cannot be found in the Meritum Guidelines a definition of knowledge as such, even if it is presented as the intangible which provide the competitive advantage. The documents suggests explicitly to distribute knowledge trough knowledge-sharing activities in order to allow stakeholders to benefit from it. This recalls a collaborative style of management and an entity vision of the firm. The vision is explicitly defined in the document as the starting point for the first phase (identification of intangibles) of the process of "management of intellectual capital" (see section 3.2).

To summarise the above analysis, there is a little consensus on a precise definition of knowledge; on the contrary it is commonly recognised that it is one of the most important element of the intellectual capital, even if it contributes differently from an approach to another to the value creation process. Furthermore it can be noticed that, when specified, knowledge has to be distributed.

c) *Value Creation and Company Strategy*

The IFAC Study no. 7, assuming Edvinsson and Sullivan point of view (1996), states that value derives from a conversion of the knowledge. The document also describes the "Value Platform", a model proposed by Saint-Onge, Armstrong and Petrash and adapted by Edvinsson and Malone (1997). In this model the merging of three types of capital (human, organisational and customer) creates the designed outcome (value).

In order to explain the value creation process, the Study no. 7 gives a particular attention to the concept of value chain analysis. The objective of value chain analysis is to identify the elements of organisational processes and activities and link them to the creation of value by the firm. Processes are structured and measured sets of activities, designed to produce a specific output for a particular customer or market. Identifying the firm's value-creating process - the way in which knowledge is created, integrated, transformed, and utilised - will require a horizontal view of the organisation and the cross-functional relationships that exist within it. A model is first established using process analysis and the activities within each process are subsequently analysed. In this way management can begin to assess the flows of information, flows of knowledge, and characteristics of knowledge transformation between functional departments, within divisions, and throughout the organisation. The end product of the knowledge management process can then be identified and valued as: 1) a patent, consulting process, or trademark; 2) an improvement in organisational efficiency and measured by cost savings, profits, revenue growth, return of investment; or 3) improved innovative capabilities of the firm, measured by a variety of individual and team-based performance indicators.

Also from the analysis of the Danish Guideline IC statement creates value because is a way of advising the stakeholders to exert their motivated interest. This is why it should be publicly available. In other words value creation is related to the *value in use* of services and products for the end-user. Through the knowledge narrative the value in use is spelled out. It can be concluded that IC can contribute to creating value for the company by improving the company's strategy for what it must excel in order to deliver satisfactory products or services.

Nordika Guidelines confirm substantially this vision asserting that value is based on firm's knowledge and competencies.

Slightly different appears the Meritum approach, in which the value creation is linked to the "management of intellectual capital" (see section 3.2) and in particular to its first phase. It is also added that value creation derives from the interaction between the different categories of IC (concept of *connectivity*). Furthermore, this approach treats value creation in terms of the broader stakeholder value because the vision of the company should describe how different stakeholder benefit from the company's knowledge productive activities. The strategic objective are thus about adding value to the customers or users of the company's product and services to the other stakeholders.

Summarising the analysed approaches we could conclude that all attribute a fundamental role to the IC report in the value creation process, but it is very different between the documents the way it contributes to this process.

4. Some concluding remarks

The paper intended to explore four recent and important documents offering guidelines on the preparation of IC statements. These documents have been compared in order to detect the emerging convergences and the nature of the remaining differences.

Regarding the focus of the documents, the comparative analysis pointed to the following features.

- The IFAC Study no. 7 was designed to support professionals in the difficult task to develop an IC report and to build public awareness, understanding and demand for this type of service; for this reason it does not set particular rules to develop an IC report; rather it limits itself to present what has been done until then (1998) on the topic, letting professionals free to choose the most adequate approach to company specificities.
- The focus of the Danish Guideline is on the concept of knowledge management to create "value in use" for users by its total forces, by relying not on a single factor but on multiple, interrelated factors, and on what actions a company takes to meet its challenges.
- The Nordika document sees the implementation process of IC report more as a learning process. Its primary preoccupation is to make IC report look as a visible and easy-to-do tool.
- The Meritum approach focuses on how a company – through the connectivity of critical intangibles linked in a network – pursues its strategic objectives and, though this, on how it creates value for users and stakeholders.

Among the most important convergences emerging from the analysis there is the commonly recognised centrality of the IC report contribution to the value creation process, even though the way it performs this function is deemed to be different. Indeed, all the documents state that the report should not only estimate the financial value of IC, but it should also explain the role of IC in creating company value. The report should cover the range of knowledge resources at the disposal of the company, how they interact, and what the company is doing to develop them for the exploitation of business opportunities. Secondly, it has to be pointed out that all the approaches aim to capture processes which are dynamic and systemic in nature. Initiatives directed to a particular factor often have second and third order effects on other parts of the business (e.g., motivation affects customer satisfaction and then product development). Another area of convergence relates to the long-term perspective assumed by the proposed procedures and techniques. Furthermore, all the documents stress the firm-specificity character of IC and, consequently, of its indicators.

The main differences found between the documents deal with value creation, the concept of knowledge, and the categories used for indicators when disclosing information. In particular, even though all the documents recognise the knowledge as he source of value, rather different are the implementation procedures and phases through which knowledge is converted into sustainable company value. Moreover, the analysis underlines that IC reports can be structured in various ways and use many different vehicles of communication, such as texts, figures, indicators and many other devices, in order to represent intangibles assets and performance.

Summarising the results of this analysis, it could be said that the weight of the emerging convergences appears greater than that of the identified differences, since the analysed documents agree upon the most important issues, which are the results they are looking for through the IC report and its role in the value creation process. What differs between the documents is essentially the choice of the pattern to reach those shared end-results.

In conclusion, the examined guidelines are likely to represent only a starting point, but which seems to be relevant on the way to create a more common framework. In this respect, they appear as a valuable and significant step in the direction of setting some form of weak and voluntary standards on IC statements. However, a lot of work is clearly still needed, and it is fair to wonder whether in the next few years there will be room for an harmonisation of these standards into a coherent and commonly accepted set of guidelines.

An example of an interesting future research pattern could be that of understanding whether and to what extent these guidelines are consistent with the characteristics of the basic accounting elements as they are set in the conceptual frameworks issued by various national standard setting, and in particular in that of the US FASB. Another research challenge could be represented by the search for a solution to two dilemmas, i.e. that between the specificity of the intangibles measurements and the need for the standardisation of information in the IC reports, and that between the permanence of indicators through time (in order to appreciate trends) and the need for an evolution of them along the learning curve of an organisation.

The first pioneers launched the concept of IC reporting in the early nineties. Since then, it seems to have reached a fairly robust level of theoretical and practical acceptance, but it still looks like a concept and a subject area that will continue to witness relevant developments and innovations in the future.

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