WORLD INTELLECTUAL PROPERTY ORGANIZATION

INTERNATIONAL NETWORK FOR SMALL AND MEDIUM-SIZED ENTERPRISES

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Intangibles & IC: Accounting, Regulation & Reporting

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“The substantial foundation of the industrial corporation is its immaterial assets”

“There may be peculiar difficulties in the way of reducing this goodwill to the form of a fund, expressing it in terms of a standard unit”

Thorstein Veblen, 1904

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AGENDA

1) Intangibles, Intellectual Capital and the new economic environment
2) The traditional accounting approach to intangibles (“the problem”)
3) A new approach to the management and reporting of Intellectual Capital
4) International initiatives
5) The Crowded world of non-financial information and the role of WICI
6) The way forward and concluding remarks

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1. INTANGIBLES, INTELLECTUAL CAPITAL AND THE NEW ECONOMIC ENVIRONMENT

The New Value Creation Process and Its Implications

- Change in company production processes
- Strategic aspects are research and innovation, marketing and know-how, customer relationship, entrepreneurial and managerial skills and not so much manufacturing à
- All phases and activities where intangibles are key à Patents & IPR are crucial intangibles
- Today, intangibles are considered the main drivers of sustainable value creation over time

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Towards the "Conceptual Company"

(Greenspan/Lev)

- Negligible physical assets (low PP&E, inventories)
- Intangibles-intensive: R&D, brands, alliances, human resources, organization capital
- Strong patent/trademark protection
- Extensive outsourcing of manufacturing, distribution and other low-knowledge functions
- Extensive trade in intellectual property (IP): patent sale and licensing, know-how sale
- Flexible business model

Intangibles and Risks

- However, investment in intangibles is associated with high levels of uncertainty in terms of outcomes and timing

- Hence, intangibles have also a negative side **à** recent history has shown that intangibles may "evaporate" very fastly, giving rise to large losses **à** intangibles are also a potential liability

- Fundamental lack of methodologies for measuring and assessing intangibles-related risks

Definitions of Intangibles

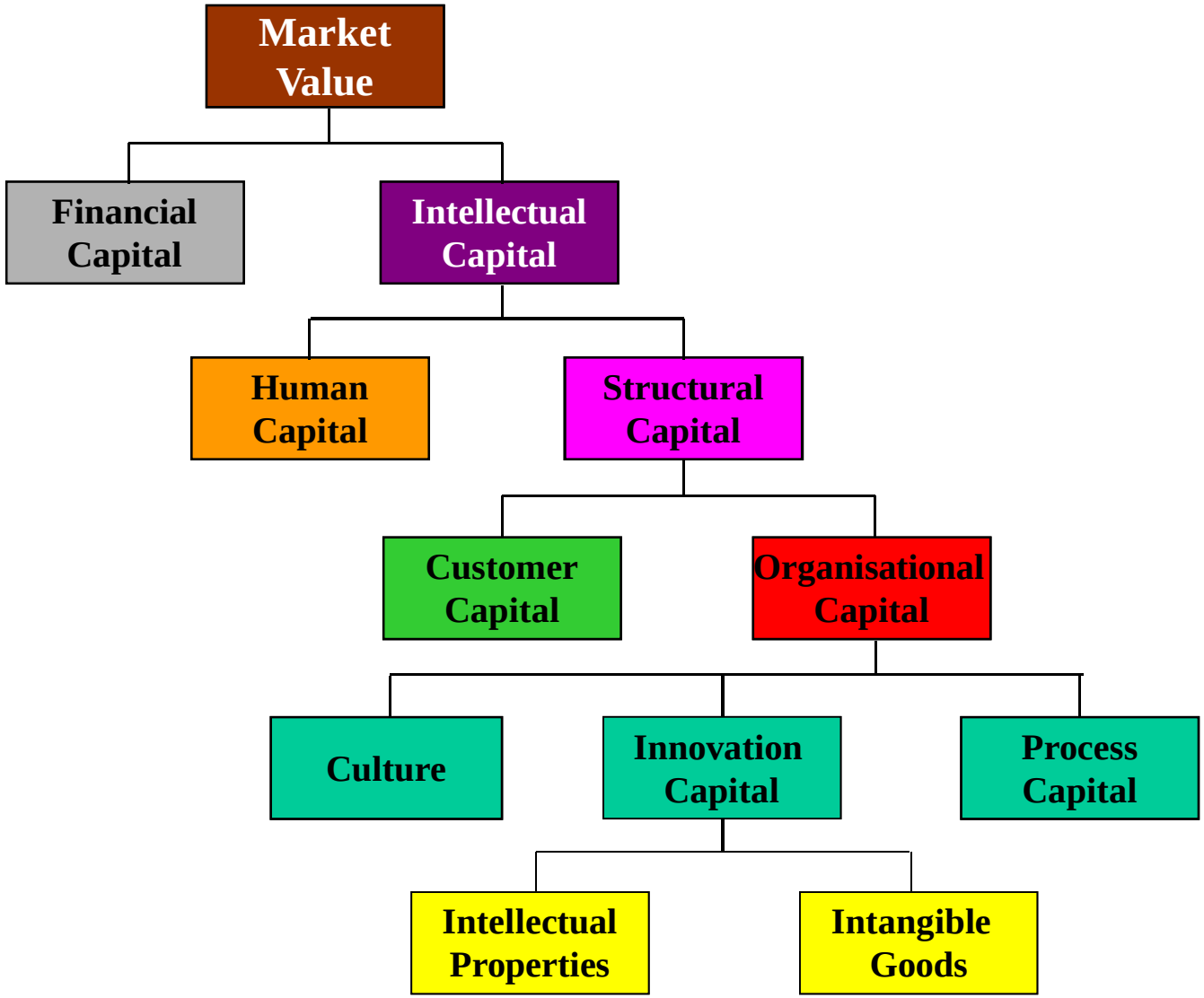
Intangible assets can be defined as a source of future benefits that is without a physical embodiment:

- Intellectual property is an intangible asset with legal rights
- Includes innovation-related intangibles (*R&D*, *patents*), but also market-related (*brands*), human resource (*competencies & skills*, *training*), and organizational intangibles (*internal structures*, *systems*, *procedures*, *routines*, *and processes*)
- "Hard" intangibles (tradable) vs. "Soft" intangibles

Intellectual Capital

Intellectual Capital – IC – is the internal (*competencies, skills, leadership, procedures, know-how, etc.*) and external (*image, brands, alliances, customer satisfaction, etc.*) stock of intangibles "available" to an organisation, which allows the latter to transform a set of tangible, financial and human resources into a system capable of creating stakeholder value through the pursuit of sustainable competitive advantages (Zambon, 2000)

Intangibles become IC only when they are durably and effectively internalised or appropriated by an organisation



Source: Intellectual Capital Report, Skandia, 1998

Intellectual Capital as Disaggregation of the Market Value

Re-focussing Managerial Attention on Intellectual Capital

- Need for regaining control by managers on the performance and knowledge generation processes à understanding long-term value creation drivers

- According to Mr. Sam J. Palmisano, Chief Executive Officer (CEO) of IBM (April 2006):

  "The economy is re-aggregating itself around the Intellectual Capital, the capacity of making technology and information live together as innovation"

2. THE TRADITIONAL ACCOUNTING APPROACH TO INTANGIBLES (“THE PROBLEM”)

THE BASIC PROBLEM

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Companies need to manage their intangibles in order to manage in a conscious way value creation processes

↓

Information is necessary to manage

↓

There is a lack of structured, systematic, reliable, and comparable information on company intangibles

Traditional Accounting for Intangibles

(e.g. International Accounting Standard no. 38)

- General suspicion of accountants towards intangibles
- Stress on reliability and not on relevance **à** no reliability = no accounting recognition
- No recognition possible for internally generated intangibles (e.g. R&D, Brands, Training)
- Conservative measurement criteria **à** general principle: immediately expensed as a cost
- Goodwill is a too synthetic representation of intangibles
- In general, rather poor information on long term growth drivers (key performance indicators – KPIs)
- Backward-looking information

Economic Consequences

This situation of lack of information on intangibles induces many adverse economic consequences:

- It easily produces short-termism, behavioral myopia, ill-informed allocation decisions, market volatility, information asymmetry, insider information, credit crunch for companies, etc.

- Risk is seen only in monetary/financial terms

“Information Cascade” Effect

- In this situation of information and valuation deficit on Intangibles, there is a serious risk that an information cascade phenomenon could take place (Zambon, 2003)
- In behavioural finance, this effect occurs when one agent looks at the behaviour of other agents for making a decision **à** spreading of partial ignorances
- “The blind that leads the blind” effect **à** increase in price volatility in the financial markets and in company cost of capital

Costs of Mismeasurement

- Firm level: risk of wrong strategies
- Industry level: misallocation of resources within and between industries; skill bias
- Capital market level: under- or over-valuation of companies; misallocation of resources; volatility
- Country and Supra-National level: policy making based on imperfect set of indicators may result in inappropriate policies

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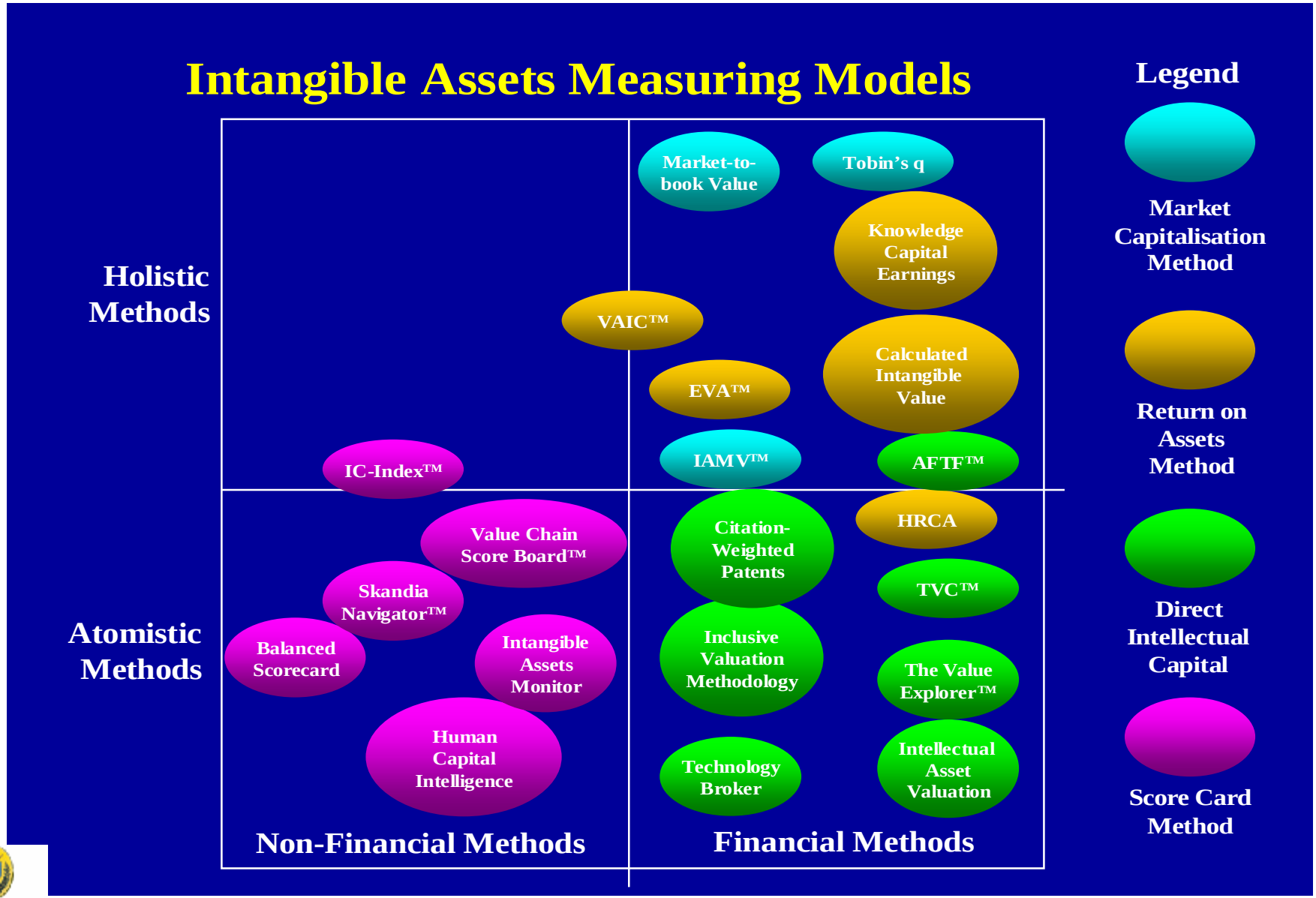
3. A NEW APPROACH TO THE MANAGEMENT AND REPORTING OF INTELLECTUAL CAPITAL

Framework of analysis



Some measuring methods

<u>Four financial and holistic methods</u>

1) *Market-to-book value*

2) *Tobin's Q*

3) *Economic Value Added* (EVA™)

4) *Knowledge Capital Earnings* by B. Lev

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Some measuring methods (cont'd)

<u>Four non-financial and atomistic methods</u>

a) *Skandia Navigator* by Edvinsson & Malone

b) *Intangible Assets Monitor* by Sveiby

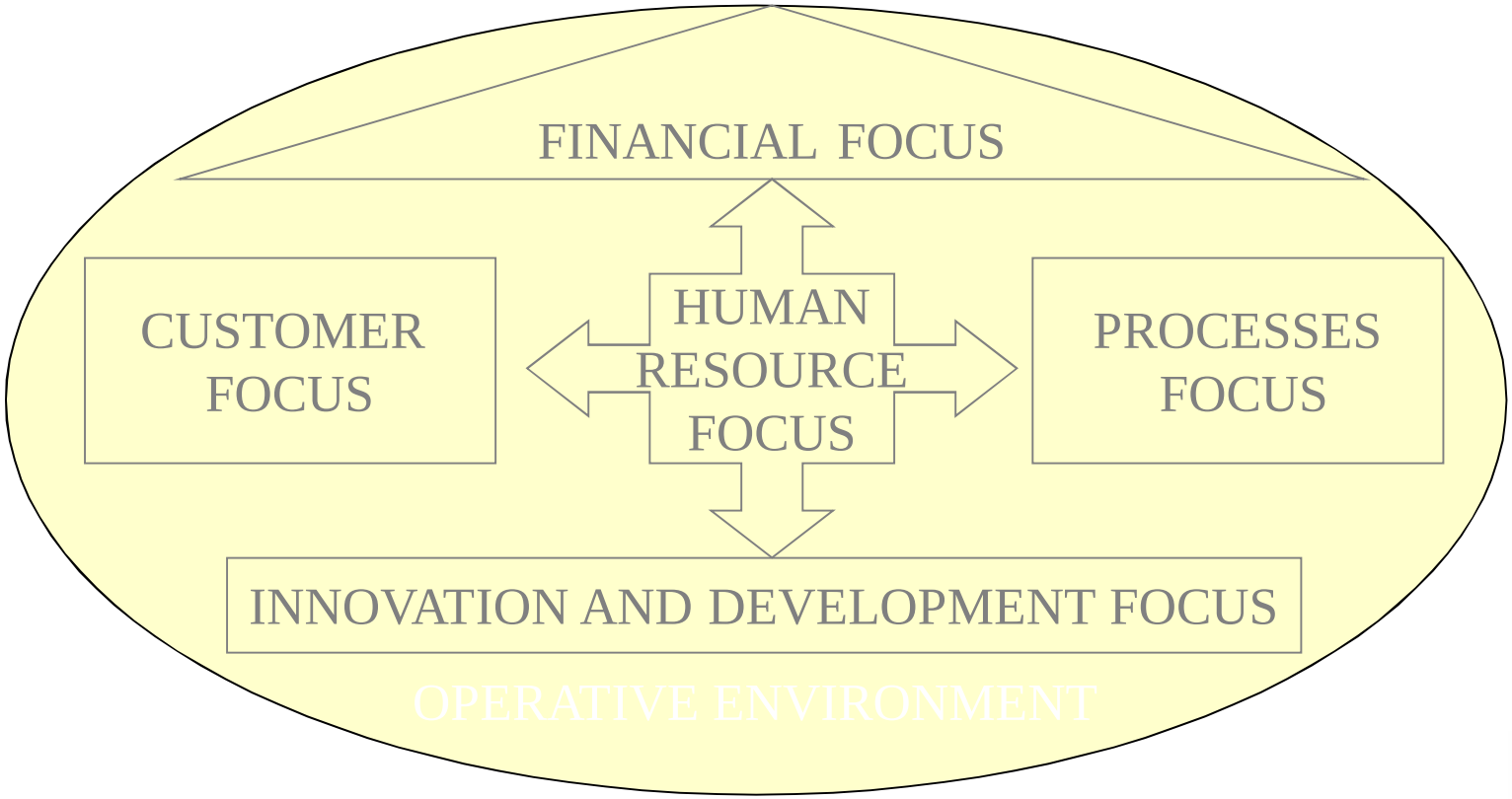
c) *Balanced Scorecard* by Norton & Kaplan

d) *Value Chain Scoreboard* by Lev

Some measuring methods (cont'd)

Four non-financial and atomistic methods

a) *Skandia Navigator*, Edvinsson & Malone, 1998



Some measuring methods (cont'd)

Four non-financial and atomistic methods

b) *Intangible Assets Monitor*, Sveiby, 1997

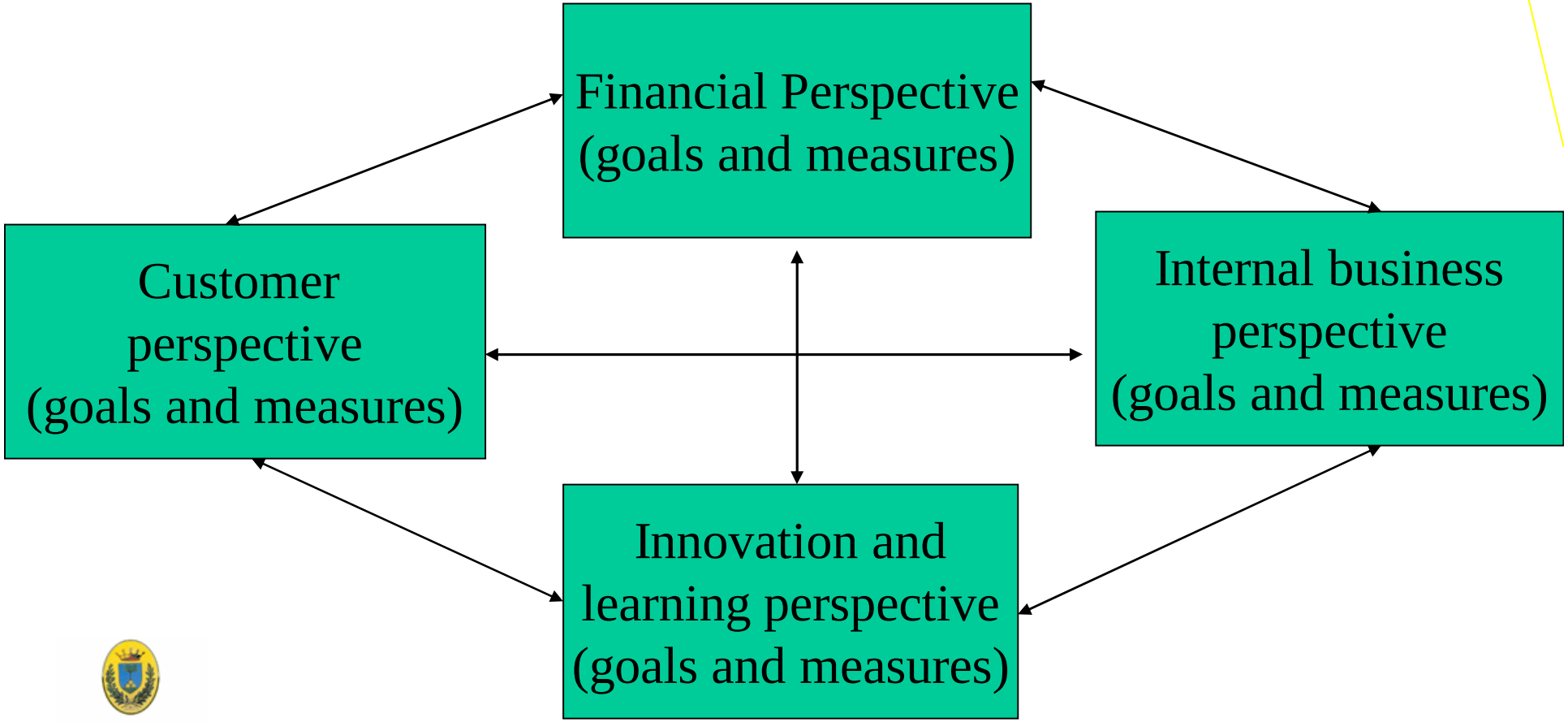
INTANGIBLE ASSETS

External Structure	Internal structure	Personnel Competence
Growth/Renewal	Growth/Renewal	Growth/Renewal
- Growth of personnel - Growth of market share - Customer satisfaction or quality	- Investment in IT - Time for R&D - Personnel behaviour towards managers, culture, customers	- Competence-enhancing customers - Growth of average professional competence (years) - Turnover of competence
Efficiency	Efficiency	Efficiency
- Revenues per customer - Sales per agent	- % of administrative staff - Sales per staff	- Value added per employee - - Changes in the proportion of highest competence employees
Stability	Stability	Stability
- Repeat orders - Age of structure	- Age of organisation - Rookie ratio	- Employees turnover

Some measuring methods (cont'd)

Four non-financial and atomistic methods

c) *Balanced Scorecard*, Norton & Kaplan, 1992



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Some measuring methods (cont'd)

Non-monetary and atomistic methods

Value Chain Scoreboard, Lev 2001

Disc. and learning

1. Internal renewal

- Research and development
- Work force training and development
- Organizational capital, Processes

2. Acquired capabilities

- Technology purchase
- Spillover utilization
- Capital expenditure

3. Networking

- R&D alliances and joint Ventures
- Supplier and customer Integration
- Communities of practice

Implementation

4. Intellectual property

- Patents, trademarks and copyrights
- Licensing agreements
- Coded know-how

5. Technological feasibility

- Clinical tests, Food and Drug Administration approvals
- Beta tests, working pilots
- First mover

6. Internet

- Threshold traffic
- Online purchases and sales
- Major internet

Commercialisation

7. Customers

- Marketing alliances
- Brand values
- Customer churn

8. Performance

- Revenues, earnings, and market share
- Innovation revenues
- Patent and know-how royalties
- Knowledge earnings and capital

9. Growth prospects

- Product pipeline and launch dates
- Expected efficiencies and savings
- Planned initiatives
- Expected breakeven and

The Future: A New Management and Reporting Tool

Intellectual Capital (IC) Statements or Report on Intangibles à based on indicators à most of them of a non-financial nature

The partitioning of IC into three interrelated sections is today quite widely accepted: Human Capital, Organizational Capital (including Innovation Capital), Relational Capital are visualised/measured through indicators and parameters, and accompanied by a Narrative that links these parameters with company Strategy

IC Report Composition

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Relational Capital

- Clients
- Suppliers
- Business Partners
- Image/Reputation on the market
- Communication

Organisational Capital

- <u>Know-How / IPR</u>
- Innovation
- Organisation
- Management Control Systems
- R&D

Human Capital

- Skills & Competencies
- Staff Turnover
- Education level
- Management Leadership
- Employee Satisfaction / Engagement

Benefits and Features of IC Visualisation

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Internally

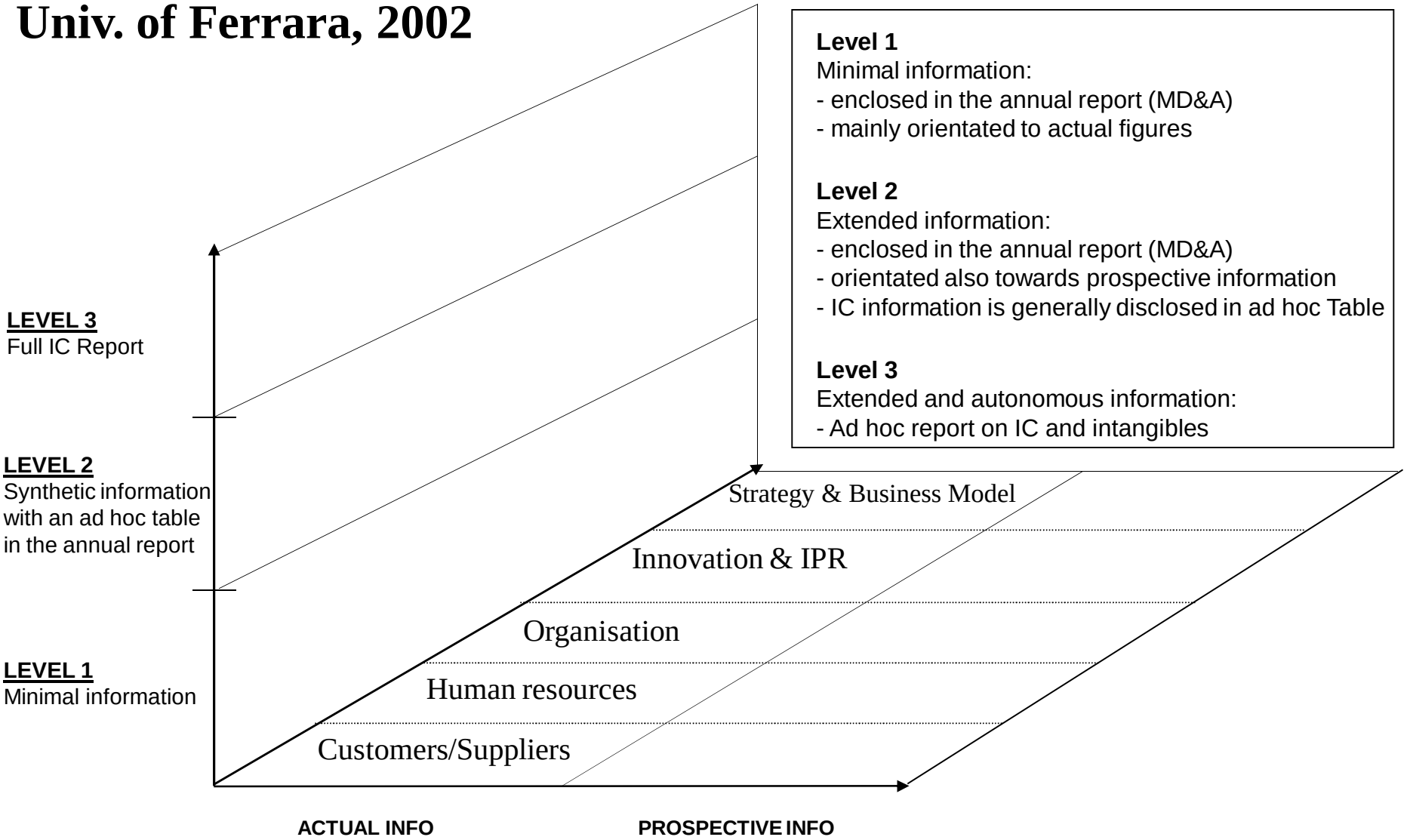
- Creation of a measurement and codification culture
- Knowledge management and sharing within org'on
- Identification of intangibles-linked value drivers & risks
- Support to the investment/divestment decisions
- Definition of new executive compensation and incentive systems
- Improvement of the internal corporate image
- Aid to the recruiting of the best talents
- Help to get R&D/IPR Depart out of a sort of "ghetto"

Benefits and Features of IC Visualisation (2)

Externally

- Better visualisation of company value creation processes for investors & financial analysts
- Easier – and possibly cheaper – access to funding sources from banks (Basel 2 ratings)
- Increased transparency on financial markets
- Support to merger and acquisition operations and stock exchange listings (initial public offering – IPO)
- Positive impact on external co. image & reputation
- More solid and documented disclosure on sustainable competitive advantages

THE MODEL FOR RANKING IC & INTANGIBLES DISCLOSURE by Italian Association of Financial Analysts & Univ. of Ferrara, 2002

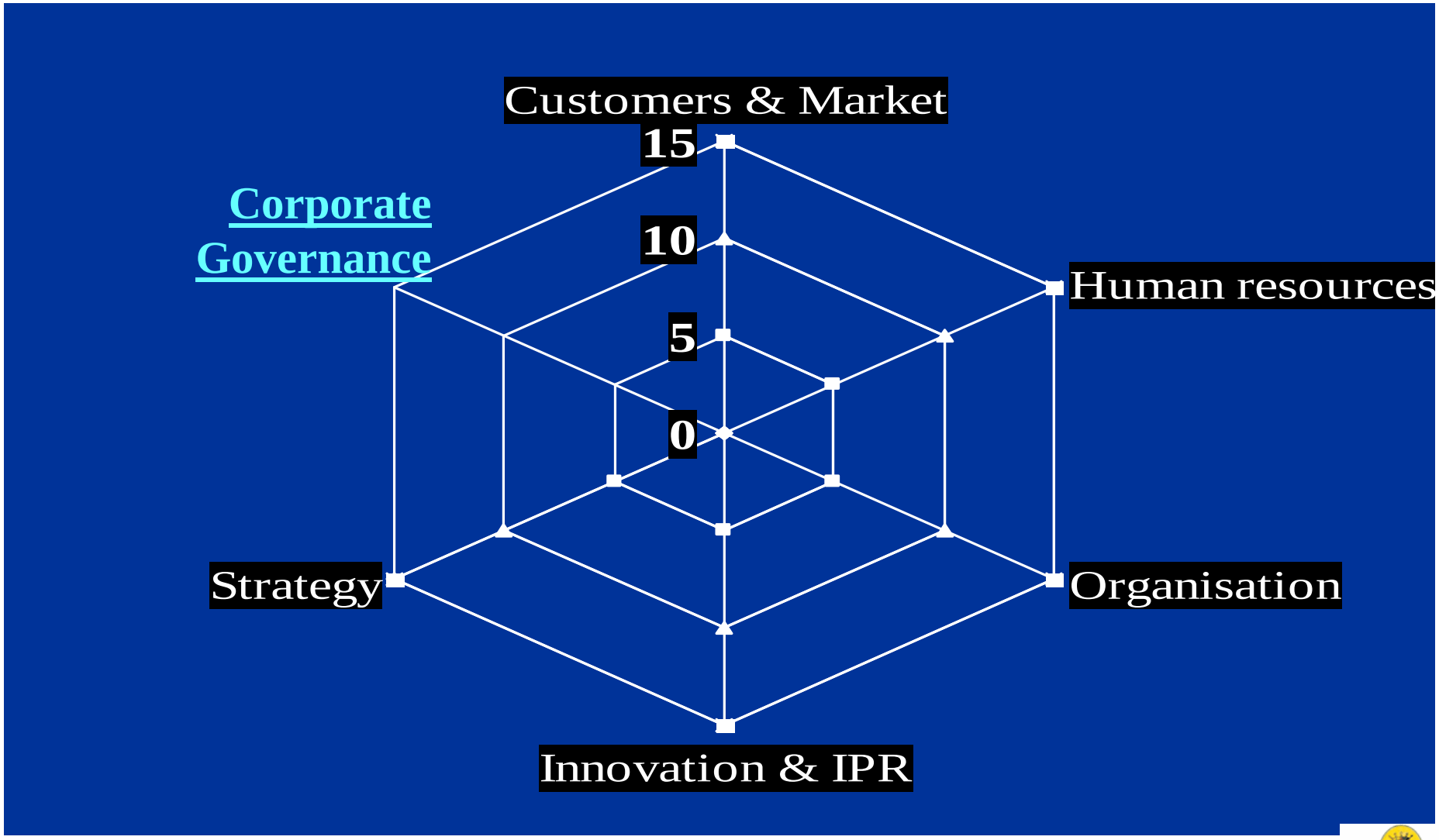


Level 1
Minimal information:
- enclosed in the annual report (MD&A)
- mainly orientated to actual figures

Level 2
Extended information:
- enclosed in the annual report (MD&A)
- orientated also towards prospective information
- IC information is generally disclosed in ad hoc Table

Level 3
Extended and autonomous information:
- Ad hoc report on IC and intangibles

Development of the Radar Diagram for evaluating the level of disclosure on Intangibles (B & Z, 2003)



0-5 = Insufficient ; 5-10 = Sufficient ; 10-15 = Excellent

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Sample and data collection: an example

- Sample: French, German, Italian and UK companies composing the main indices of each national Stock Market (CAC40, DAX30, MIB30 +Midex, FTSE100)

- Exclusions: Companies from financial and insurance sectors as well as non-national companies have been excluded

- Total sample: 27 companies in France, 19 in Germany, 28 in Italy, 65 in UK

- Document considered: 2001 annual report

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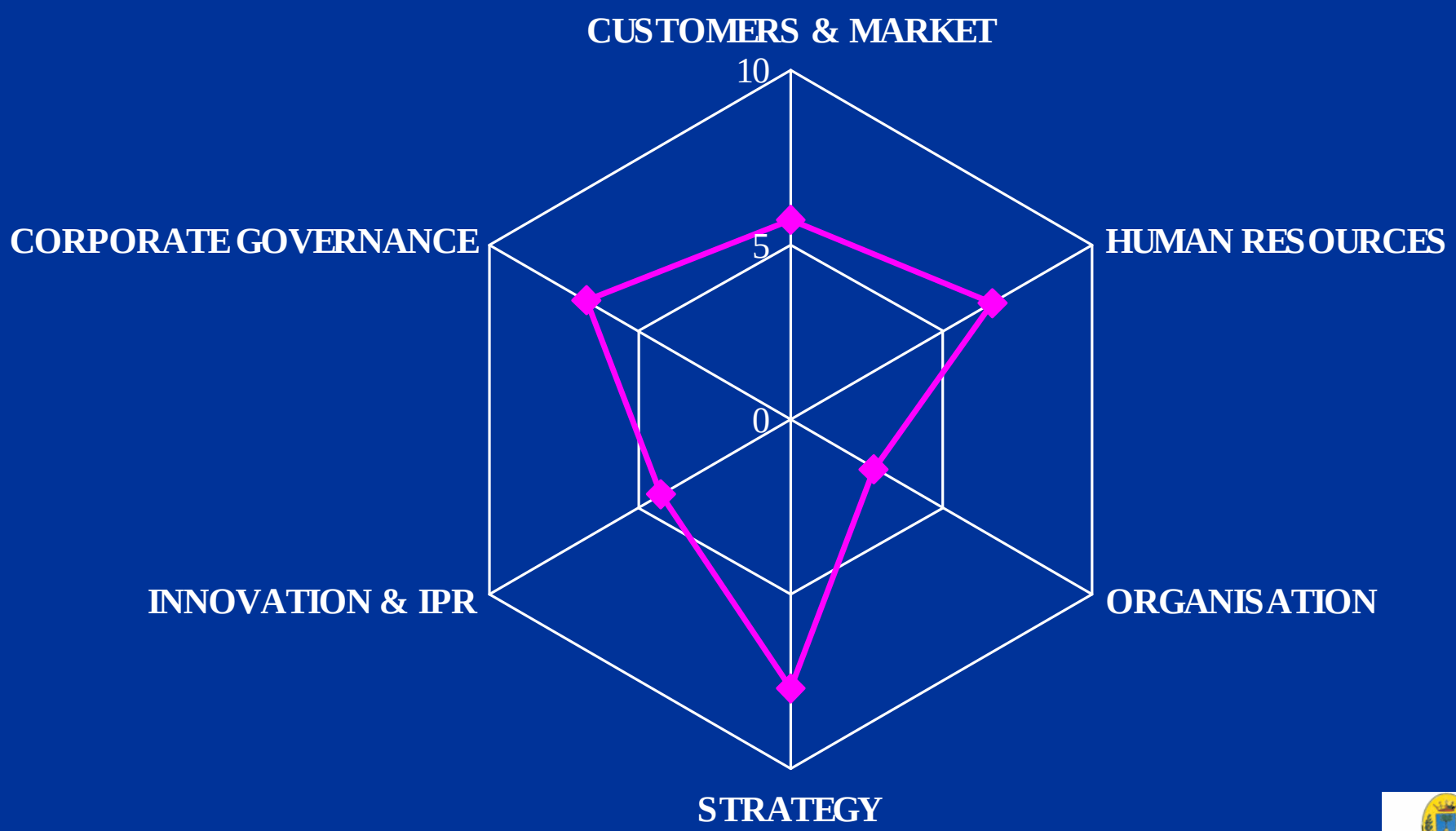
Results - France



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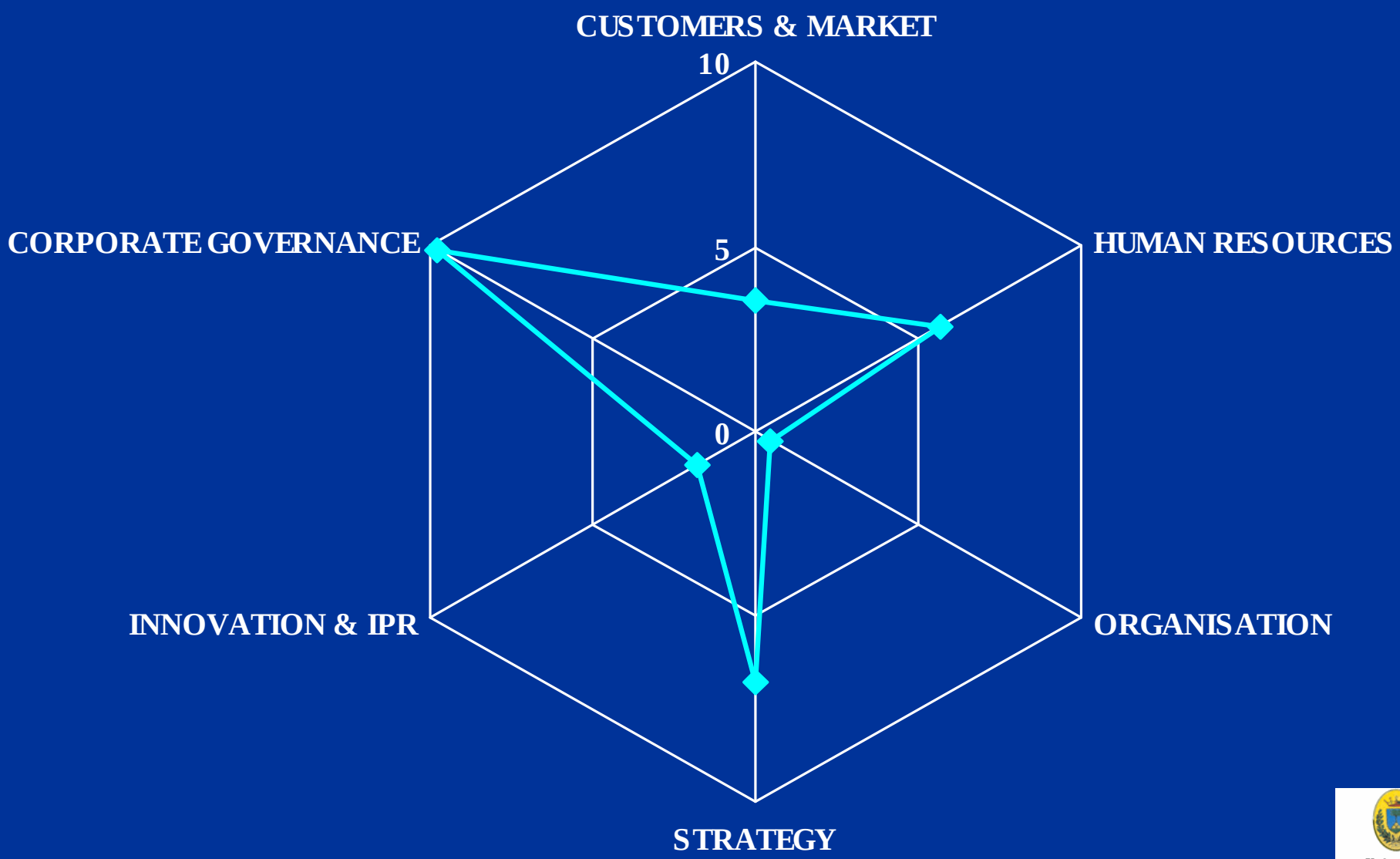
Results - Germany



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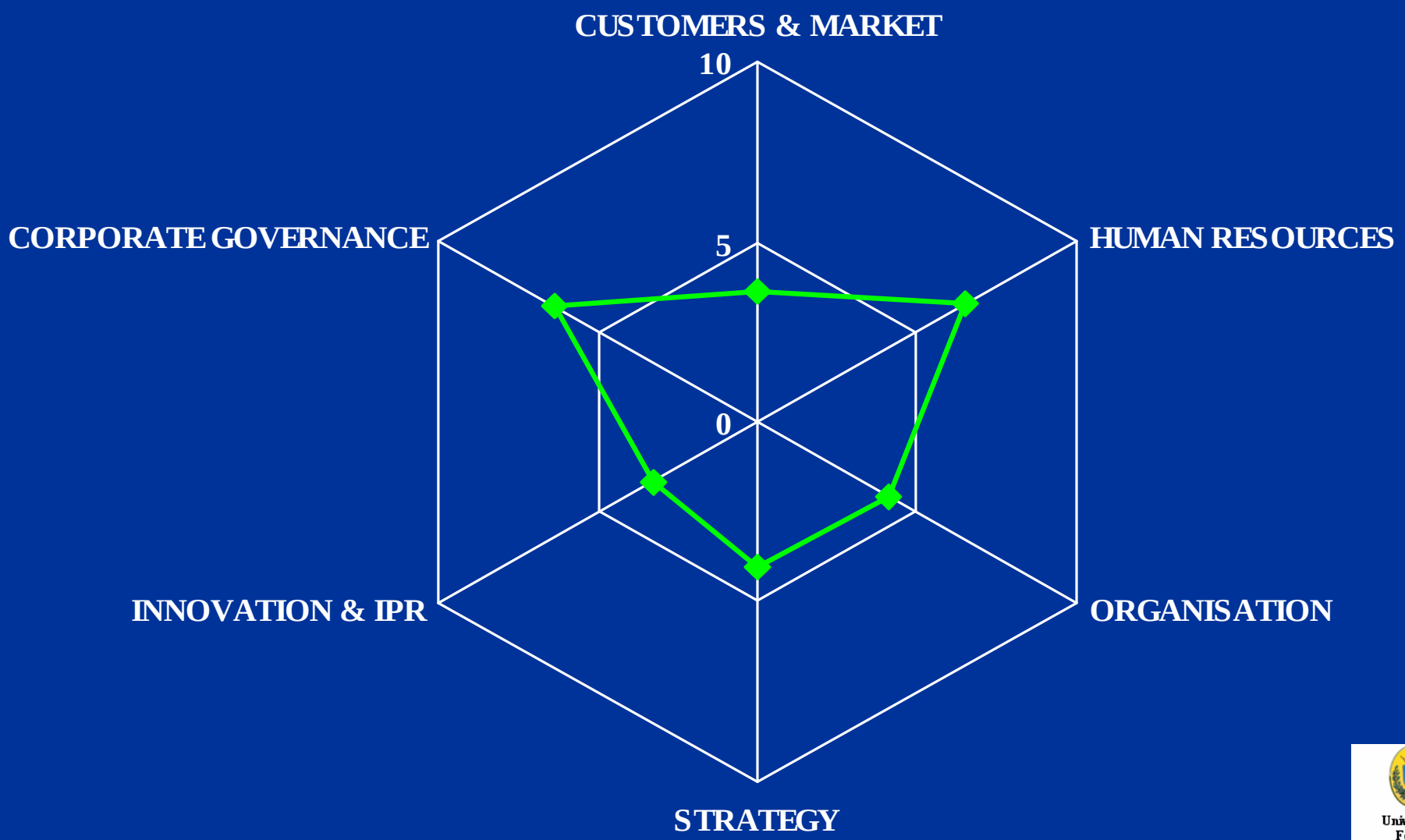
Results - Italy



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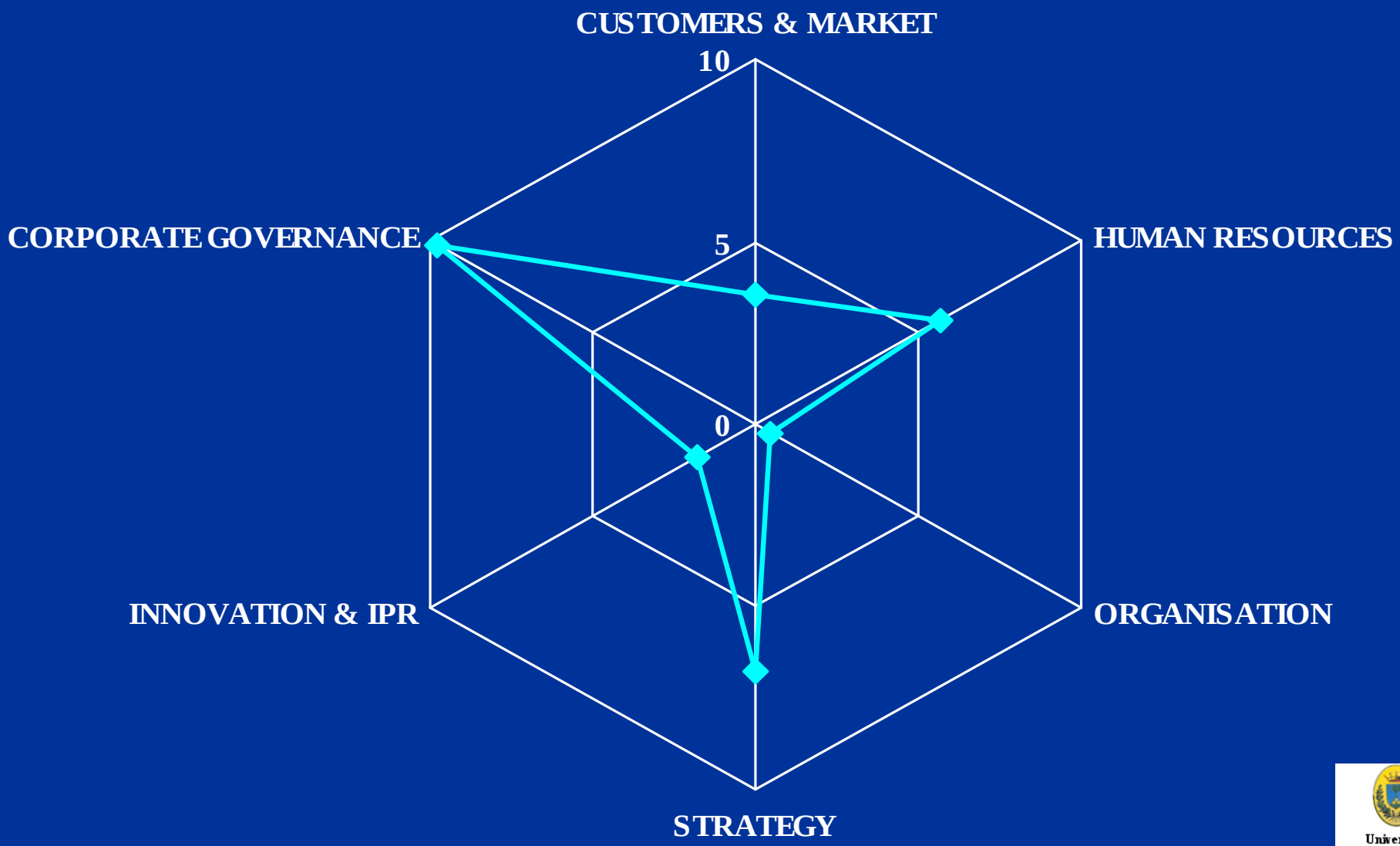
Results – United Kingdom



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Results – Areas of Hexagons

COUNTRY	AREA (Units)
France	77.04
Germany	72.57
Italy	53.93
UK	39.17

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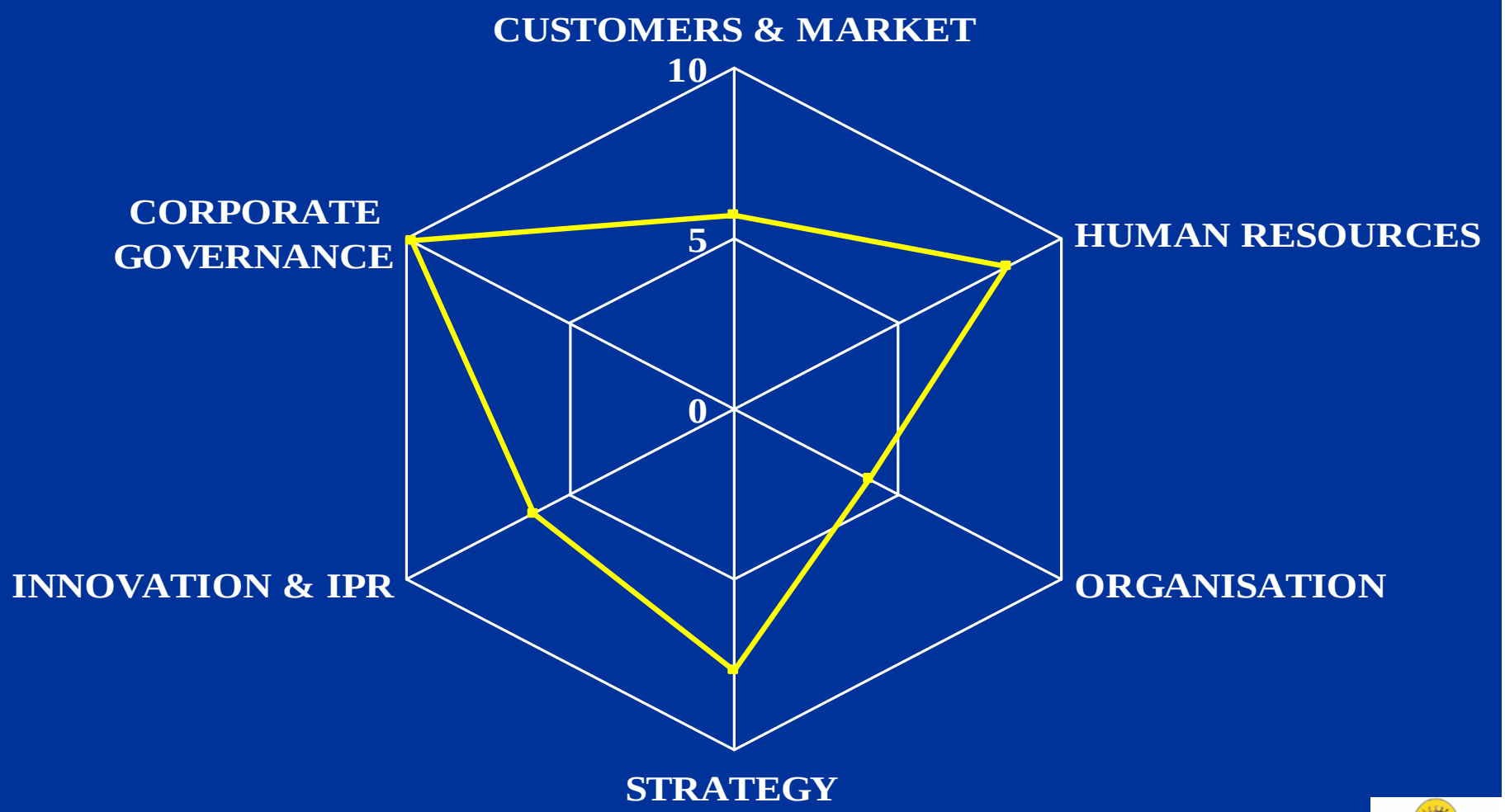
Disclosure on Intangibles: The simulated European best practices



Area of simulated hexagon = 119.48 units

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Some critical issues of these new measures

Despite their value and innovativeness, these measures face some *critical issues* concerning their:

- consistency / comparability à some form of international standard is needed
- reliability (auditability)
- thoroughness / completeness
- meaningfulness:
    a) subjectivity in the choice of the "useful" indicators
    b) indicators do not possess additive properties
    c) high company specificity of indicators

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4. INTERNATIONAL INITIATIVES

A series of European initiatives at an institutional level

- 2002-2003: Official Study for the European Commission (DG Enterprise) on

  "The Measurement of Intangible Assets and Associated Reporting Practices"

  Partners:

  - University of Ferrara (lead partner)

  - New York University (Prof. Baruch Lev)

  - Melbourne University (Prof. Margaret Abernethy)

  http://ec.europa.eu/enterprise/services/business_related_services/policy_papers_brs/intangiblesstudy.pdf

A series of European initiatives at an institutional level (cont'd)

2005-06: European Commission's (DG Research) study on IC reporting to increase R&D in SMEs and help these companies to access bank credit (RICARDIS) **à** published in June 2006

"Reporting Intellectual Capital to Augment Research, Development and Innovation in SMEs (RICARDIS)", (cf. http://ec.europa.eu/invest-in-research/pdf/download_en/2006-2977_web1.pdf)

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Some recent international developments in IC Reporting

The Intellectual Assets-based Management (IAbM) initiative by the Japanese Government and business community is expanding

Interest by World Bank continues (Regional/Cities/ /Communities IC) à Paris Conferences

Research in this area by the Organisation for Economic Cooperation and Development (OECD) is also progressing

Also the World Intellectual Property Organisation (WIPO) is addressing the "IC Readiness" issue

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Some recent international developments in IC Reporting

(cont'd)

1st International OECD Policy Conference in collaboration with the University of Ferrara & WIPO (Ferrara, 20-22 October 2005) **à** cf. www.ferraraonintangibles.net

2nd International OECD Policy Conference in collaboration with the METI of the Japanese Government (Tokyo, 7-8 December 2006)

Some recent international developments in IC Reporting (cont'd)

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Increase in the interest of statistical agencies at national and international level à e.g. U.S. Federal Reserve, UK Statistical Office, Eurostat à "Growth Accounting" approach

The United Nations International Conference in New York, 23-24 June 2008 on "Information Gaps at Micro- and Macro-Level" à session on IC information and reporting

Other relevant initiatives

- "Wissenbilanz phenomenon" in Germany
- Austrian law mandated IC Reports for universities
- The "PIP Project" in Nordic countries
- The "Observatoire sur l'immaterial" in France
- The "Value Reporting" by PwC
- The IC Rating
- Intellectual Assets Centre in Glasgow
- The VALI Project" in Italy for IC Reporting of small-medium enterprises (SMEs)

Principal Guidelines on IC Reporting

- International Federation of Accountants (IFAC) – Study no. 7 (1998)
- Danish Agency for Trade and Industry (DATI) Guidelines (2000; latest edition 2003)
- Nordika Project Guidelines (2001)
- Meritum Project Guidelines (2002)
- German Ministry of Labour (2004)
- Japanese Ministry of Economy (METI) (2005)
- Australian IC Guidelines (2002 e 2005)
- Putting IC into Practice Guidelines (PIP) by Nordic countries (2006)

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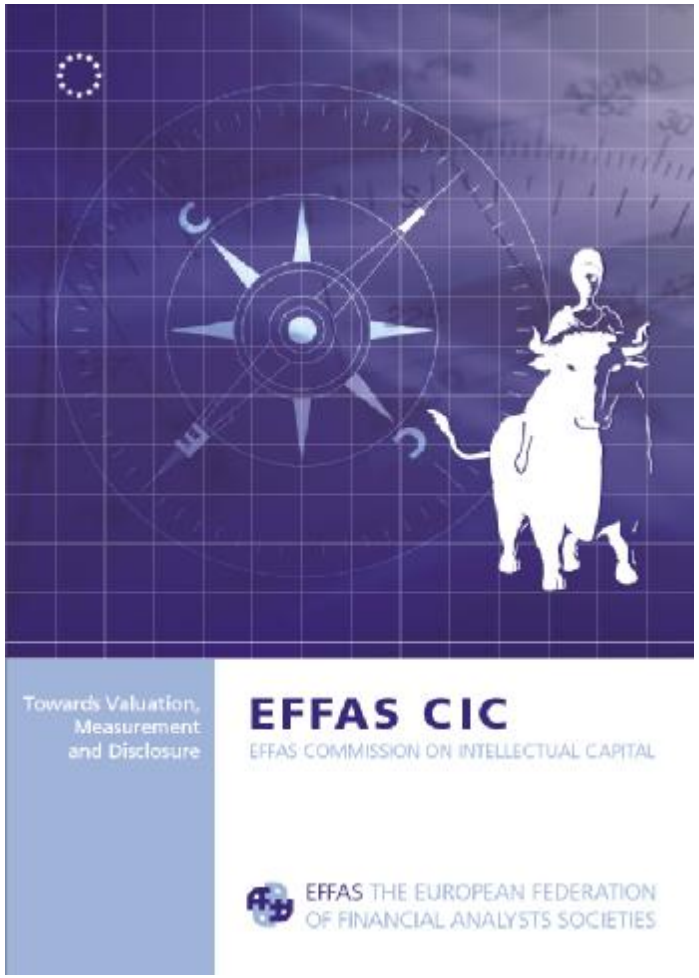
Ten principles for effective communication of IC



Why and how the financial community should tackle intangibles – now

EFFAS/CIC Principles

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1. Clear link to future value creation
2. Transparency of methodology
3. Standardisation
4. Consistency over time
5. Balanced trade-off between disclosure & privacy
6. Alignment of interests between company & investors
7. Prevention of information overflow
8. Reliability and responsibility
9. Risk assessment
10. Effective disclosure placement and timing

Ten principles for effective communication of IC

1. Clear link to future value creation

The indicators should enhance the basis for decisions of both internal and external parties. Only those indicators that are also used for internal management are relevant for investors. To that end, indicators should exhibit a clear link to the company's future value creation.

More specifically, analysts and investors are interested in indicators directly related to a company's operating and/or financial market performance. It might be necessary to further clarify this link in a narrative fashion. In addition, an ideal indicator would be one that could be "modelized", i. e. included in quantitative valuation frameworks

Ten principles for effective communication of IC

2. Transparency of methodology

Companies should explain how they have built the indicators disclosed. “Easy to measure” often means “easy to understand” and thus effective in communication.

The calculation method should be derived from the internal management system. This helps to ensure that the benefit attributable to the use of the indicator exceeds the cost for obtaining the information.

Ten principles for effective communication of IC

3. Standardisation

A transparent methodology facilitates a more fertile discussion with analysts about the company's potential and performance. The resulting deeper understanding in turn enables analysts to compare different indicator approaches. Eventually, market forces would then lead to the emergence of a "market best practice" in the calculation and disclosure of intellectual capital indicators. This is a crucial step: only standardised intangibles indicators can be benchmarked between companies, and only benchmarked indicators are truly useful.

For the time being, we would prefer the market-driven approach to the imposition of mandatory standards on a detailed level, as leeway is still needed for collaborative experimentation including both companies and analysts/investors. Ultimately, we think indicator standardisation should exhibit three levels of specificity. Indicators on the low level should be generally applicable, i.e. they should be relevant for most or all sectors and companies. Indicators on the middle level should be those specific to a certain sector (using a sector taxonomy already broadly used in the financial community). Indicators on the top level should be those specific to the individual company.

Ten principles for effective communication of IC

4. Consistency over time

The second possible dimension of benchmarking is to compare today's indicator values to historical ones for the same company. To enable that, the set of indicators chosen has to be as consistent over time as possible. When a company decides to replace an indicator, a rationale should be given (for instance, to align it to a change in the company's strategy).

As long as standardisation has not progressed far enough, there is a risk of "indicator moral hazard": We should strive to help companies counter the obvious temptation to replace indicators with new ones that currently seem to portray them more favourably.

Ten principles for effective communication of IC

5. Balanced trade-off between disclosure and privacy

Indiscriminate disclosure of information on intellectual capital could in some cases result in competitive disadvantages. It is thus indispensable to search for the right balance between the disclosure of intellectual capital and privacy issues. The publication of such information should always be preceded by a careful internal management decision process.

Ten principles for effective communication of IC

6. Alignment of interests between company and investors

Progresses in the disclosure of intellectual capital may only be achieved by aligning the interests of the company, asked to provide a higher quantity of better quality information to the outside world, and the investor, who will use this information within his or her valuation framework. Where true alignment proves difficult, an adequate compromise should be aimed at.

One important issue to be covered is the disclosure/privacy balance discussed above. Another relates to cost/benefit considerations, on the sides of both the disclosing company and analysts/investors.

Ten principles for effective communication of IC

7. Prevention of information overflow

Analysts and investors are confronted with a substantial stream of information already today. Thus, while there is a clear lack of information on companies' intellectual capital, this information should be focussed on the most crucial indicators.

Only then will analysts and investors be able to work with the additional information on a day-to-day basis and closely integrate it into their valuation frameworks. Corporates should privilege relevance instead of quantity also when publishing a separate Intellectual Capital Report.

Ten principles for effective communication of IC

8. Reliability and responsibility

As any reported company information, information on intellectual capital should of course reflect the true corporate situation. Both the choice of indicators and the calculation of their values should be objective in portraying the company's potential. Moreover, the indicator values should be verifiable: it should be possible to track the sources of information in order to check accuracy (which also implies the need for transparent indicator calculation methods, see principle 2).

On a more practical note, information on a company's intellectual capital should be a true and fair expression of its existing internal measurement system or the result of a custom-made, transparent assessment process. The latter could be conducted either internally or by third parties. In addition to external assurance, the assignment of internal management responsibility (on board or senior management level) for the information disclosed will be necessary.

Ten principles for effective communication of IC

9. Risk assessment

Where feasible, disclosed information on a company's intellectual capital should be accompanied by an assessment of the risks inherent to each indicator. This should include those possible future events and their probability that might endanger a company's operating performance.

For instance, with reference to human capital, this refers to the risk of key employees leaving the firm. Risks are obviously higher when this key personnel carries confidential and/or strategic knowledge. Another important examples are risks to a company's reputation.

Ten principles for effective communication of IC

10. Effective disclosure placement and timing

Finally, information on a company's intellectual capital should be communicated through both efficient and effective channels, and with an adequate frequency. In our view, an appropriate place for broader information on a company's intellectual capital, as discussed in this paper, would be the "Management Commentary" (or "Management Discussion and Analysis") within the annual report. Here, intellectual capital indicators can and should be embedded in narrative where necessary to clarify their meaning and link to the company's future value creation. The publication of a separate Intellectual Capital Report is another possibility, to be deliberated in the context of the company's whole reporting system.

Both ways would suggest a publication frequency synchronised with the annual report. External stakeholders might ask to be provided with information on some particularly important indicators of intellectual capital (or the associated risk assessments) more frequently, though.

We would not rule out the notion of integrating broad information on intellectual capital into either the balance sheet, the profit and loss or the cashflow statements. This being subject to valuation from accounting standard setters and a broader stakeholder community.

The Future:
the IASB's Management Commentary

- In June 2009 IASB has published an Exposure Draft on Management Commentary (MC) due to be a voluntary Guidance and not a Standard
- It sets out principles, qualitative characteristics, and content elements of Management Commentary to provide capital providers with decision-making useful information à a context for understanding management's objectives and related strategies
- Management Commentary should <u>especially</u> provide forward-looking (future-oriented) non-financial information à especially on intangibles

The Future:
the IASB's Management Commentary (2)

- Attention should be given to the commentaries on the nature of the business, management objectives and strategies, main resources-risks-relationships, results of operations and prospects, & critical performance measures and indicators

- Management Commentary includes financial and non-financial information **à** inclusion of key-performance indicators (KPIs) **à** how non-financial factors have influenced and will be able to influence financial performance

The Harmonisation Role of XBRL

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eXtensible Business Reporting Language (XBRL) needs taxonomies in order to operate

Taxonomies are dictionaries of tags/labels logically structured

The tags can regard both quantitative and qualitative company and non-profit organisation information

The Harmonisation Role of XBRL (cont'd)

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The more these dictionaries are internationally accepted and adopted, the more XBRL produces its benefits

In the US à the SEC thrust towards a general XBRL Taxonomy includes the search for establishing also a global taxonomy for non-financial and non-GAAP information à 90% of this information deals with intangibles

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5. THE “CROWDED” WORLD OF NON-FINANCIAL INFORMATION AND THE ROLE OF WICI

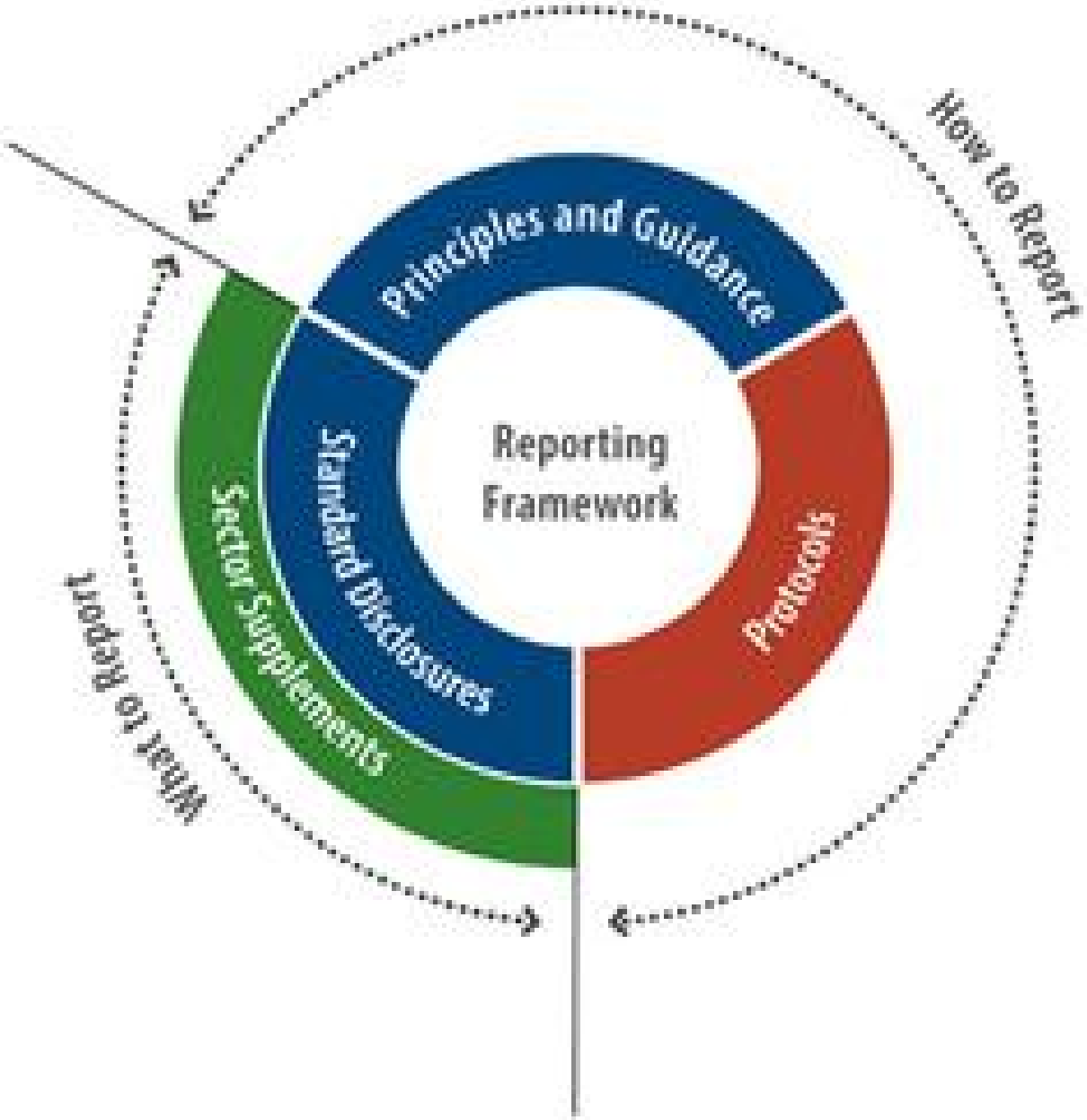
GRI
GLOBAL REPORTING INITIATIVE

Global Reporting Initiative (GRI) is a network-based organization that has pioneered the development of the sustainability reporting framework **à** multi-stakeholder organisation with a quite strong influence of NGOs and developing countries

Outcome of the corporate social reporting & the triple-bottom line reporting logic **à** not linked to value creation

Reporting Guidelines at their third edition (G3) have been quite widely adopted in the past, but most recently there have been some problems

G3 Reporting Framework



INTERNATIONAL INTEGRATED REPORTING COMMITTEE (IIRC)

On 2 August 2010 The Prince's Accounting for Sustainability Project (A4S) and the Global Reporting Initiative (GRI) announced the formation of the International Integrated Reporting Committee (IIRC).

The principal objective of the IIRC is to create a globally accepted framework for integrated reporting. Such a framework will seek to bring together financial, environmental, social and governance information in a clear, concise, consistent and comparable format.

A further objective is to help with the development of more comprehensive and comprehensible information about an organization's total performance, prospective as well as retrospective, to meet the needs of the emerging, more sustainable, global economic model

INTERNATIONAL INTEGRATED REPORTING COMMITTEE (IIRC) (2)

Steering Committee

- Sir Michael Peat, Principal Private Secretary to TRH The Prince of Wales and The Duchess of Cornwall (Chairman)
- Professor Mervyn King, Chairman, Global Reporting Initiative (Deputy Chairman)
- Georg Kell, Exec Director, UN Global Compact
- John Elkington, Founding Partner & Executive Chairman, Volans

ACCA, IFAC, UNCTAD, FASB, IASB, Global Accounting Alliance (National professional accountancy bodies), Big Four (auditing), Climate Disclosure Standards Board, Nestle, Tata, HSBC, Tokyo Stock Exchange, World Business Council for Sustainable Development...

Working Group

- Paul Druckman, Executive Board Chairman, The Prince's Accounting for Sustainability Project (Co-Chairman)
- Ian Ball, Chief Executive, International Federation of Accountants (Co-Chairman)

Railpen, Big Four (auditing), AccountAbility, United Nations Principles for Responsible Investment, Novo Nordisk, Aviva, Microsoft, UNCTAD, GRI, IASB….

W I C I

World Intellectual Capital /Assets Initiative

The World's Business Reporting Network

www.wici-global.com

WICI

World Intellectual Capital/Assets Initiative Network

www.wici-global.com

The “World Intellectual Capital/Assets Initiative” (WICI)

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The general aim is to work towards a new and generally accepted framework for business reporting worldwide with particular reference to intangibles/intellectual capital

Promoting & Participating Parties

- Japanese METI (Ministery of Economy, Trade & Industry)
- U.S. Enhanced Business Reporting Consortium (*EBRC*) [AICPA, PricewaterhouseCoopers, Grant Thornton, Microsoft]
- Waseda University of Tokyo
- University of Ferrara
- European Financial Analysts (Commission on Intellectual Capital)
- OECD
- Society for Knowledge Economics in Australia (SKE)
- European Commission (observer)
- Brazilian Development Bank (BNDES) (observer)
- World Intellectual Property Organisation (WIPO/OMPI) (observateur)

The WICI – The World's Business Reporting Network

The WICI Network was officially born on 31 March 2008 with the signature of the Memorandum of Understanding (MoU) in Washington DC at the American Enterprise Institute (AEI) (first meetings from March 2007)

Founding values of WICI are its global reach, its institutional vein, and its non-profit consortium nature

The particular objective is now to provide the new measures and information giving content to the future of company business reporting (KPIs), including intangibles and intellectual assets

WICI Deliverables

(cf. www.wici-global.com)

- Commentaries on relevant international documents (e.g. IASB's Exposure Draft on Management Commentary; European Commission's Workshop Series on Environment, Social, Governance)

- Development of a more comprehensive business reporting framework (combining generalisability & specificity)

- KPI Concept paper

- Development of KPIs per sector/industry:
    - Electronics (WICI Japan) – draft for public discussion
    - Pharmaceutical (WICI Japan) – draft for public discussion
    - Automotive (WICI Japan) – draft for public discussion
    - Telecommunications (WICI Europe+EFFAS CIC) – draft for public discussion
    - Software and IT services (EBRC + Gartner)

- XBRL-ization of KPIs information

WICI Framework versione 1.0

(already tagged in XBRL - *www.wici-global.com*)

0 Corporate profile and business attributes
0-1 Industry overview
0-2 Duration and results per business unit
0-3 Business cycle per business unit
0-4 Competitive analysis

Past → Current → Future

a. Business landscape
A-1 Business landscape

b. Strategy
b-1 Corporate strategy summary
b-2 Vision and mission
b-3 Strengths
b-4 Weaknesses
b-7 Goals and objectives
b-8 Corporate strategy
b-9 Business unit strategies
b-10 Business portfolio

c. Resources & processes
c-1 Resources and processes summary
c-2 Resource forms
c-3 Key processes
c-4 Value drivers

d Performance
d-1 Performance summary
d-2 GAAP-based
d-3 GAAP-derived
d-4 Industry-based
d-5 Company-specific
d-6 Capital market-based

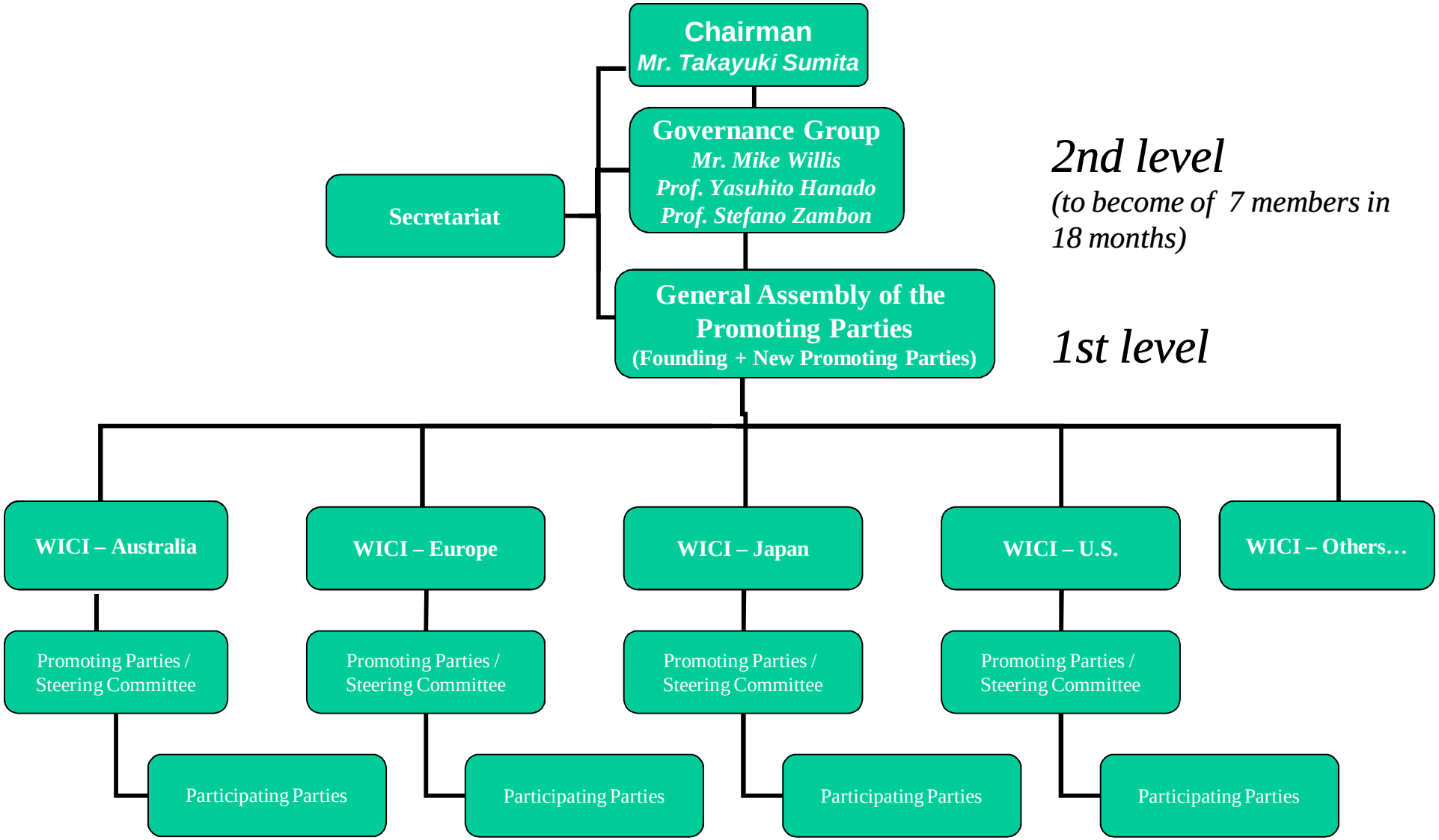
A. Business landscape
A-1 Business landscape summary
A-2 Economic
A-3 Industry analysis
A-4 Technological trends
A-5 Political
A-6 Legal
A-7 Environmental
A-8 Social

C. Resources & processes
C-1 Resources and processes summary

B. Strategy
B-1 Corporate strategy summary
B-2 Vision & mission
B-5 Opportunities
B-6 Threats
B-7 Goals and objectives
B-8 Corporate strategy
B-9 Business unit strategies
B-10 Business portfolio

D. Performance
D-1 Financial prospects summary

WICI Governance Structure



The Establishment of the WICI Europe Network

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On 29 May 2009 in Paris the EFFAS, the University of Ferrara and the Intellectual Assets Center of Glasgow jointly signed the Memorandum of Understanding (MoU) for the establishment of the WICI Europe Network

The seat of WICI Europe is in Frankfurt at EFFAS, and the Chairman of WICI Europe is Prof. Stefano Zambon (University of Ferrara)

W I C I Europe

regional jurisdiction of the

Global WICI Network

the world's business reporting network

www.wici-global.com

Current Steps of WICI Europe

- To promote the establishment of WICI jurisdictions/ associations in Europe under the aegis of WICI Europe

- To gather supra-national European-wide institutions/ associations/companies as direct members of WICI Europe (European Investment Bank, Business Europe, AIM ….)

- To advocate for WICI's and WICI Europe's cause before the European Commission as well as other national and supra-national institutions

- To favour the creation, implementation and testing of knowledge in the area of measuring, reporting, and managing intangibles & IC **à** ad hoc working groups **à** academics/practitioners, public/private

Current Steps of WICI Europe (2)

- WICI Italy has just been set up (Network Italiano per il Business Reporting – NIBR)

- First meeting of WICI UK is going to be held in Glasgow on 7 December 2010

- First meeting of WICI Luxembourg on 24 March 2011

-To elaborate and propose the KPIs for agreed sectors **à** so far telecommunication industry. We also commented on the KPIs proposed by WICI Japan on pharmaceutical, electronic component & automobile industries. Now WICI Europe started working on the fashion industry KPIs

Current Steps of WICI Europe (3)

-WICI France has been established having the Observatoire de l'Immatériel as founding member

- WICI Europe is going to participate in the organisation of the Symposium International 2011 of the Ecole Française de l'Immatérial (EFI) (Bercy, Paris, 6-7 October 2011)

Comparability vs. Specificity: The "Inverted Pyramid" approach

- Non-financial indicators could be articulated in three levels: General, Industry, Company Specific. **à** the "inverted pyramid concept"

  Only the first two levels are to be agreed upon in the future

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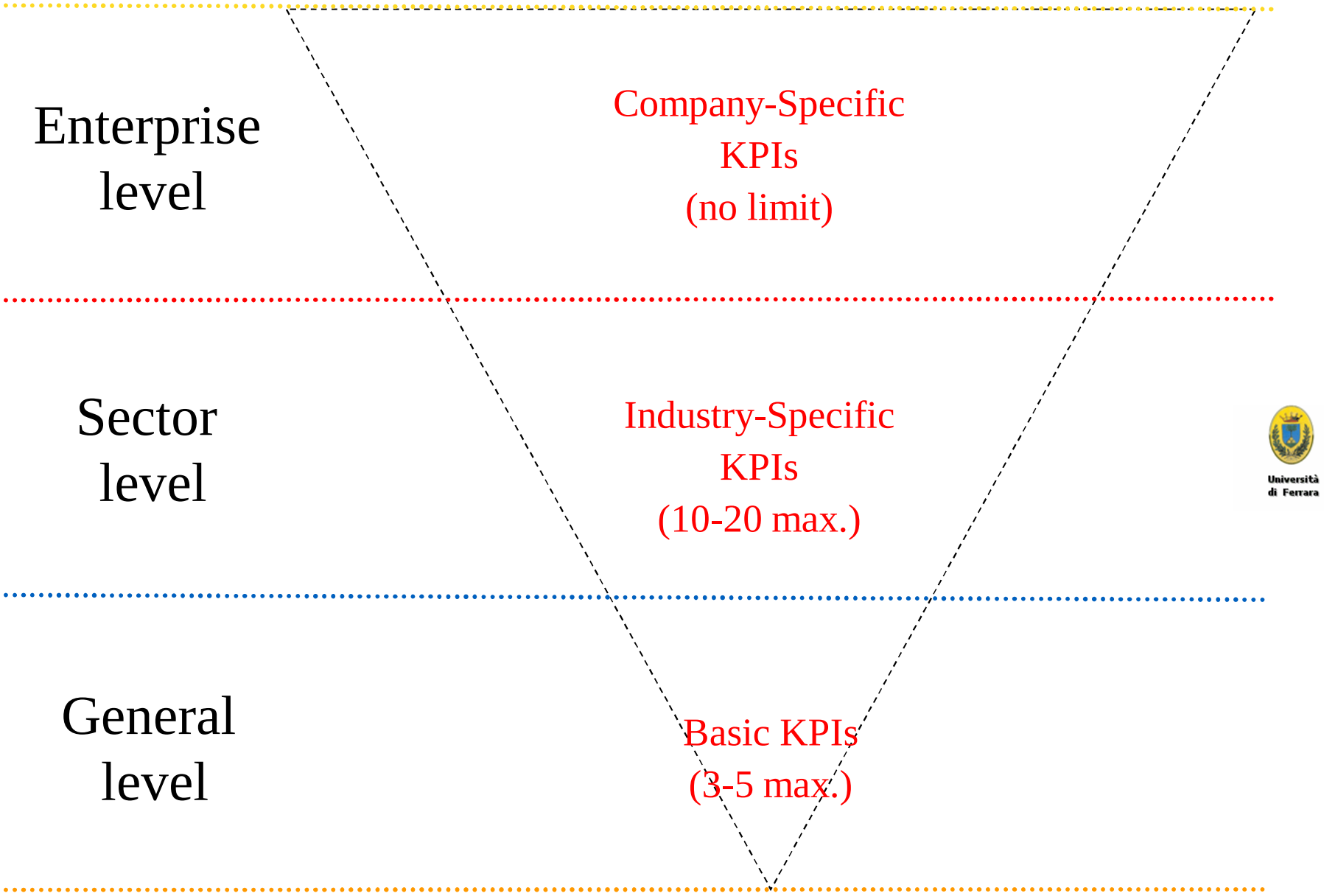

Reporting on Intangibles: combining comparability & specificity

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CONVERGENCE OF IC REPORTING AND SUSTAINABILITY REPORTING

Sustainability Reporting: Main Trends of the Debate

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1. A larger concept of sustainability (environmental vs. business)
2. From CSR to ESG (Environment, Social, Governance)
3. Business vs. civil society indicators
4. Increasing search for systemic vision of company information (interconnected, integrated, combined, comprehensive)
5. Information on risks (e.g. reputation)
6. Convergence of effort **à** e.g. European Combined Reporting Alliance (ECRA) **à** WICI Europe, Eurosif, EFFAS, Railpen, A4S
7. Several attempts to provide standardisation of ESG/non-financial information (WICI, GRI, International Interconnected Reporting Committee, Global Compact, ISO….) **à** EFFAS ESG indicators
8. Regulation-based vs. voluntary adoption
9. Education of/for stakeholders (banks, investors, managers, governments…)

An Intangible Perspective on CSR and Stakeholder Value

A simple idea

Social Capital & Environmental Capital as particular intangibles to be managed by companies for achieving sustainability (exploiting the overlappings between “business intangibles” & “E.S.G. intangibles”)

Intellectual Capital and Corporate Social Responsibility (CSR)

Social and Environmental Issues can be seen as part of the management of Intellectual Capital (image/reputation/risk management)

Therefore, social and environmental capital can be considered as particular intangibles to be managed by companies for achieving long-term sustainability and preserving income generation capacity through reputation à BUSINESS SUSTAINABILITY

Already many common information "ingredients" between IC reports & social/environmental reports (Cordazzo, JIC, 2005)

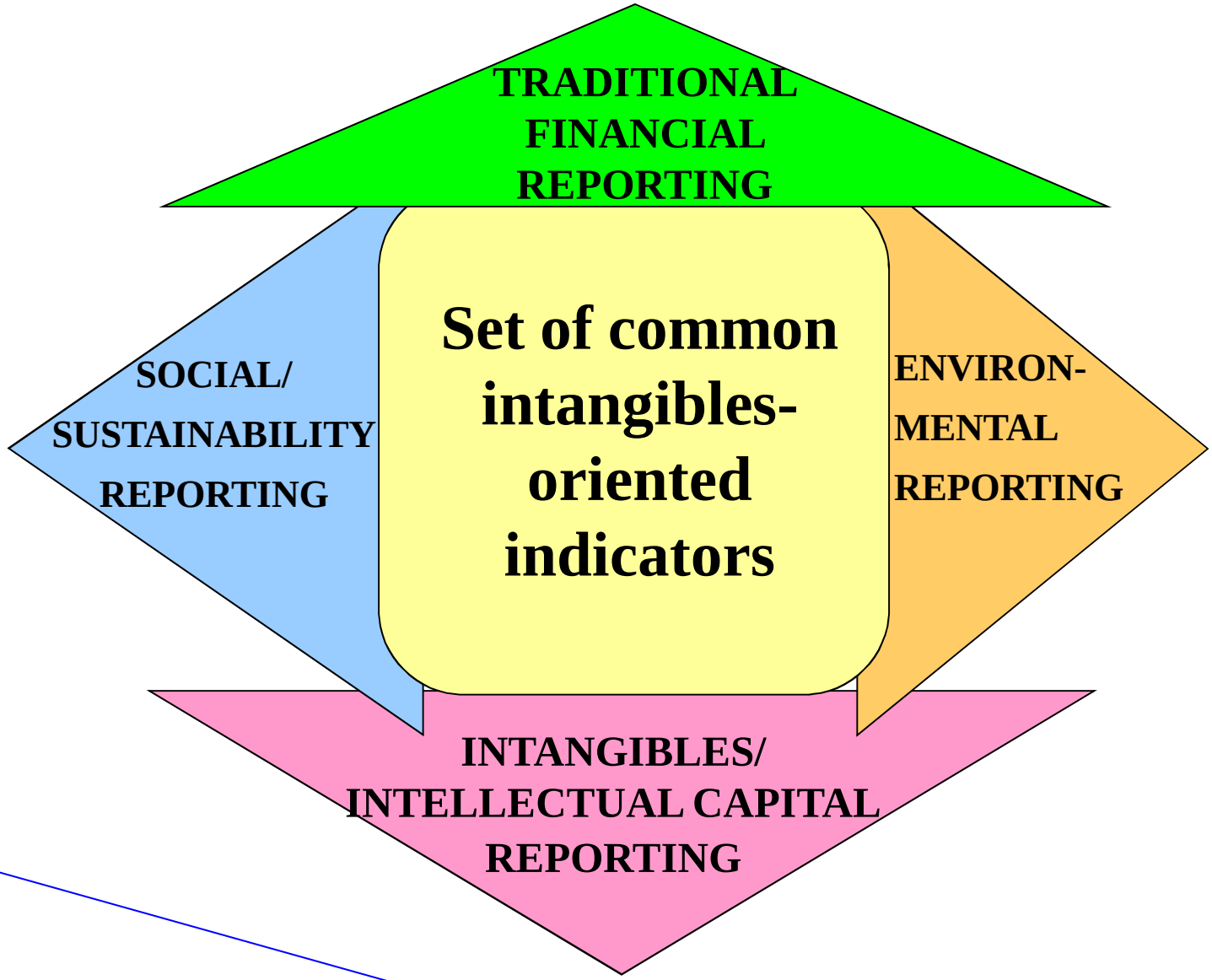
From sustainability reporting to the sustainability of reporting

From sustainable development to reputation to risk management optimisation

"We are committed to the goal of sustainable development. We believe that operating to leading standards of health, safety and environmental management, contributing to the development of sustainable communities, and engaging with our stakeholders in two-way, open dialogue, regardless of our location, enhances our corporate reputation and is a source of competitive advantage. This enables us to gain access to new resources, maintain a license to operate, attract and retain the best people, access diverse and low-cost sources of capital, identify and act upon business opportunities, and optimise our management of risks." (XSTRATA Annual Report, 2008, p. 21)

Towards the Integrated Reporting System

(S. Zambon (ed.), 2003, Study for the European Commission)



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6. THE WAY FORWARD & CONCLUDING REMARKS

Concluding Remarks

- The today's economic environment and the Conceptual Company pose new challenges to managers, investors, policy makers
- It is important to learn how to visualise the link between value creation, management and intangibles/IPR through a new information set and reporting system à to become a market standard
- Intangibles are also associated with risk à risk management overlaps with intangibles management
- Financial Analysis à communication of appropriate information on intangibles is necessary to value and price company processes

Main Policy Indication

- Urgent to improve information on intangibles and IPR at micro level initially in a <u>non-mandatory perspective</u>, because good indicators at micro level will also allow to build better indicators at regional, meso and macro level

Company Reporting: policy indications (cont'd)

- Policy aim: identify in a collaborative way (public & private) at an international level a standardised set of intangibles non-financial indicators serving as minimum common information denominator **à** WICI is open to collaborations & join forces
- Need to develop and promote an innovative, integrated, reliable, and verifiable company reporting system
- Convergence between various forms of reporting and avoidance of proliferation of guidelines and alike

Final consideration

We face a major PARADOX:

- The more the economic system is based on intangible assets, the stronger it is (because they are major drivers of growth & value creation).

- However, at the same time:

  The more the economic system is based on intangibles, the more vulnerable it becomes.

The challenge <u>we all</u> face is <u>to learn</u> how to manage, organise, and report on these "invisible" resources

THANK YOU!

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