



The World Conference on Intellectual Capital for Communities

IC Reporting and Standards Relevance

The OECD Agenda for IC Reporting

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The views expressed do not necessarily reflect the official views of the OECD or of its member countries

Overview of OECD project on IAVC

- 2004: Horizontal project at OECD level (DSTI, DAF and EDU)
- 2006 MCM: OECD ministers noted the growing importance of intellectual assets and proposed follow-up studies in this area
 - **Macro-level:** impact of IA in national accounts and economic growth
 - **Regional level:** importance of IA for clusters and for the geography of innovation activities in OECD regions
 - **Micro-level:** management and reporting of IA at firm-level

Overview of OECD project on IAVC

- 2006: Intellectual Assets and Value Creation: Implications for Corporate Reporting
- 2007: Intellectual assets and corporate reporting: the situation of small caps
- 2008 MCM: Intellectual Assets and Value Creation: Synthesis report

Key issues on corporate reporting

- Steep increase in the importance of non-financial and non-GAAP information
- « Reporting explosion »: CSR reports, ICR, CG reports...
- Discrepancies in companies reporting: there is a big tail of poor companies
- Many national and institutional initiatives but no international reporting framework
- Proposed frameworks do not meet investors' expectations as they are often too general and lack industry-specific indicators
- IA taxonomies provided not used by investors

Benefits of enhanced corporate reporting

- Improved capital market efficiency
 - ❖ Lower cost of capital
 - ❖ Lower bid/ask spread
 - ❖ Reduced stock price volatility
- Impact on cost of capital higher for small listed IA intensive companies suffering from low analyst coverage
- Improved internal control and enhanced risk management
 - ❖ Improved information systems that make IA and their value drivers more visible to executives and directors
 - ❖ More efficient resource allocation and improved investment strategies

Four conclusions of OECD work on corporate reporting

1. Necessity to provide taxonomies value-relevant for investors and managers
2. Necessity to develop global business reporting frameworks that are sector-specific, supported by KPIs and related XBRL taxonomies
3. Necessity to improve incentives for financial analysts to follow small IA-based companies
4. Necessity to consider the risks of managing IA & to systematically and specifically disclose risk issues (no more boilerplate disclosures)

Necessity to provide taxonomies value-relevant for investors and managers

- Evolving scope
 - R&D, patents, trademarks
 - Human resources and capabilities, organisational competencies and « relational » capital
 - Dynamic business attributes: knowledge-creating capability, right of access to technology, ability to use information
- Confusion between the assets and their value drivers
- IA are included in SRI issues
- Taxonomies provided not used by investors although more investors take them into account in their research

Towards global business reporting frameworks?

- Two types of guidelines with different scope, target companies, users and purposes
 - Narrative reporting : listed companies, mandatory, shareholder-oriented, reporting tool
 - Specific reporting on IA: all organizations, voluntary, not only shareholder-oriented, management tool. Recent development in some countries
- Main challenges for non-financial reporting frameworks
 - Disclose timely, relevant and comparable reports
 - No overlap with existing voluntary reporting & provide consistency with all existing reports
 - Ensure materiality of information released
 - No increase in preparation costs for companies listed in multiple jurisdictions

Growing number of initiatives address disclosure of intellectual assets

Selected Frameworks and Guidelines of reporting on IAs

| Institution/Country | Scope | Year | Reference |
|---|---------------------|------|--|
| Narrative/non-financial reporting | | | |
| European Union | All companies | 2003 | Modernisation Directive (4 th and 7 th Directives) |
| | Listed companies | 2004 | Transparency Directive |
| Australia | Listed companies | 2003 | ASX Listing Rule, Australian Stock Exchange |
| Canada | Listed companies | 2003 | Continuous Disclosure Obligations, Sec. Admin. |
| Germany | All companies | 2004 | GAS 15 Management Reporting, DRSC |
| United Kingdom | Quoted companies | 2005 | Operating and Financial Review, DTI |
| United States | Listed companies | 2003 | Management Discussion and Analysis, SEC |
| Specific reporting about intellectual assets | | | |
| European Union | All companies | 2002 | Guidelines on Intangibles, MERITUM Project |
| Australia | All companies | 2002 | Guiding Principles on Extended Performance Management |
| Austria | Public universities | 2002 | Austrian Universities Act |
| Denmark | All companies | 2003 | Intellectual Capital Statements, MSTI |
| Germany | SME | 2004 | Intellectual Capital Statement, BMWA |
| Japan | All companies | 2005 | Guidelines for Disclosure of IA-based Management, METI |

Driving forces to enhanced corporate reporting

- Institutional investors such as EAI and Financial Analysts such as EFFAS CIC are stimulating research on how to incorporate extra-financial and forward-looking information into their analysis for LT investments.
- Improving the visibility and liquidity of small caps has become a key concern for stock exchanges
- Development of XBRL (eXtensible Business Reporting Language) as a driving force for an harmonisation of taxonomies on non-financial information and KPI

What is XBRL about?

- XBRL is a technology that tags information of all kinds (financial and non-financial) and makes it machine readable
 - ❖ Narrative sections of AR can be tagged and compared
 - ❖ Tagging can be focused on performance metrics for carrying out the strategy of a specific company and can be organised into a variety of standard formats for KPI organised by industry
- XBRL is a dictionary: XBRL taxonomies for financial reporting relate to the definitions and classifications that enable contextual tags to be applied to every item in a company's financial statement. There is a taxonomy for every industry group
- With US SEC's support, XBRL has gained visibility and several projects are underway
- XBRL developments in Japan: case of FSA (EDINET)
 - ❖ All companies have to prepare financial reports « *Yuka Shoken Houkokusho* » (like 10K) and will have to provide FSA financial statements under XBRL format
 - ❖ Targets are B/S, P/L and cash flow statements
 - ❖ Pilot test has already been successfully done
 - ❖ Target date is April 2008

Policy Implications

- Additional public disclosure for listed companies would enhance market efficiency
- Principles-based & voluntary approach to improved disclosure on IA: too complex for prescriptive standard
- Governments need to encourage diffusion of best practices already pioneered by advanced firms. The top companies are not the problem
- Reporting frameworks could be further developed to incorporate internal control and risk management issues
- Private initiatives such as WICI network aiming at developing business reporting frameworks with industry-specific KPI and related XBRL taxonomies should be supported
- Governments need to support investors initiatives that encourage the financial analysts' coverage of small caps, especially IA-intensive ones (EAI, EFFAS CIC).

Future OECD activities on corporate reporting

WICI network: cooperation between key players in the field of management and reporting of IA: EBRC, METI, OECD, EFFAS, University of Waseda and University of Ferrara

WICI activities

1. To develop business management and reporting frameworks for key industries
2. To support the development of XBRL taxonomies
3. To disseminate information and best practices concerning the management and reporting of IA through, among others, conferences, workshops and dedicated webpages
4. To encourage the conclusion of international agreements designed to promote IA management and reporting
5. To establish working relations and cooperate with other international organisations



Thanks!

The ***IAVC report*** can be downloaded on our
website at:

www.oecd.org/daf/corporate-affairs