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InCaS

Intellectual Capital Statement – Made in Europe

Instrument: Collective Research

Thematic Priority: Horizontal Research Activities involving SMEs

Final Publishable Activity Report

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Introduction

To obtain competitive advantage in Europe, it is crucial for small and medium sized enterprises (SMEs) to utilise knowledge efficiently and to enhance their innovation potential. Furthermore, reporting those intangible assets systematically to customers, partners and investors as well as creditors has become a critical success factor.

The relevance of Intellectual Capital

Thus, managing their specific "Intellectual Capital" (IC) becomes increasingly important for future-oriented organisations. Current balance sheets and controlling instruments are not sufficient any more, because intangible assets are not taken into consideration by conventional methods.

Intellectual Capital can prove particularly useful in the development, production and selling of a company's products and services. It covers a diversified knowledge area, ranging, for instance, from staff qualification and motivation, leadership and management structures, to organisational capacities or relations to the market. Overall, IC is a crucial resource in gaining an advantage over competition, and in ensuring the future success of a business. However, such a powerful resource naturally requires an appropriate operating instrument.

The Intellectual Capital Statement (ICS) makes it possible:

- ✓ to assess, report and develop an organisation's Intellectual Capital,
- ✓ to monitor critical success factors systematically, and
- ✓ to support strategic core competencies.

It can thus help to decrease operational and strategic risks, serving as a suitable basis for strategic decisions and organisational development.

Aims and actors of the InCaS project

The collective research project "Intellectual Capital Statement – Made in Europe (InCaS)" aimed at implementing ICS in 25 European SMEs, based on an EU-wide consolidated ICS methodology and at raising the awareness for ICS in over 1.000 SMEs across Europe. To achieve these objectives, a thoroug analysis of researchers and developers (RTD) on existing, but scattered ICS approaches was required in order to identify common grounds, cultural differences and national requirements. "InCaS" places the emphasis on a practical approach, suitable for SMEs, combined with maximum benefit regarding the improvement of exploitation of existing IC and revealing unused innovation potentials.

Focusing on an SME core group in five core branches, the project aimed at minimising complexity and implementation efforts. A systematic dissemination of the developed European ICS Guideline was carried out by a consortium of multipliers in five core countries. The tested ICS methodology set pre-normative standards for assessing and reporting Intellectual Capital in European SMEs.

The InCaS consortium was composed of SMEs and IAGs from 5 European countries willing to develop and implement an ICS method able to meet the specific requirements

of European SMEs. The 5 national SME associations were composed of Association Française des Dirigeants d'Entreprise en Europe (France), Bundesverband mittelständische Wirtschaft - Unternehmerverband Deutschland e. V. (Germany), Polska Konfederacja Pracodawcow Prywatnych Lewiatan (Poland), Foment del Treball (Spain) and Gospodarska Zbornica Slovenije (Slovenia).

The RTD consortium consisted of three main RTD partners: Fraunhofer Institut für Produktionsanlagen und Konstruktionstechnik (Germany), London School of Economics and Political Science (United Kingdom) and Universitat Politècnica de Catalunya (Spain). They were supported by an Expert Group consisting of the following members: ARC Systems Research GmbH (Austria), Intangible Asset Consulting (Austria), UNIC Universal Networking Intellectual Capital AB (Sweden), Univerza v Mariboru (Slovenia) and Wissenskapital Entwicklungsunternehmen GmbH (Germany). The responsibility for the development of technical tools was taken over by Technische Universität Berlin (Germany).

Major achievements during the project

During a project lifetime of 2,5 years, the InCaS consortium has been working on its objectives within three phases:

Phase I: Preparation

With regard to the international state-of-the-art of Intellectual Capital Statements, the activities in phase I focussed on the scientific consolidation of international experiences in the field of Intellectual Capital Management and Reporting. One of the first RTD activities of InCaS in phase I was to summarise the current state-of-the-art on a scientific and on a practical level (requirements of SMEs). Based on the German methodology, a simplified version of the ICS implementation process had been developed and pilot-tested with the 25 core SMEs. As a practical implementation support, trainer guidelines were developed and disseminated within the project consortium, operationalising each of the five implementation steps of the procedural model described in the ICS framework. After the pilot-implementations the results and the experiences of SMEs were evaluated and served as the starting point for the subsequent enhancement of the method in the second phase of the project.

Phase II: Implementation

As a first step of phase II, the harmonisation workshop of all RTD partners outlined the main issues to be focused on in the further development. The feedback from the pilot SMEs revealed one of the most crucial challenges in the field of IC management and reporting, i.e. the two conflicting objectives of “standardisation vs. individualisation”: On the one hand, some SMEs asked for preset components and a standardised structure of the ICS, whereas on the other hand others preferred a more flexible, individualised procedure to tackle their specific questions and problems. In the past, both directions had been followed by different research approaches, providing management instruments with either one *or* the other focus. An instrument combining both views and suitable for an application in SMEs had not yet been developed. During the second phase, InCaS focused on research activities in both areas. Responding to

the individual needs and requirements from SME practitioners, the ICS methodology was enhanced and upgraded in several respects:

Additional ICS modules have been developed in order to complement the basic steps of the ICS process. They are designed especially for those ICS users, who are less acquainted with management methods and are therefore less experienced with the issues addressed by an ICS. Depending on the maturity and demand of the SME, modules can de added at various steps of the implementation process to facilitate the use of the ICS, thus keeping the implementation procedure flexible and individual to a certain degree.

As a second major methodological enhancement with respect to flexibility and user-friendliness, the ICS procedure was modified and now offers two possibilities for analysing the impact of a company's IC. Depending on the size and maturity of a company, either a simple (impact scoring) or a full version (cross impact matrix) can be applied to assess and analyse the Intellectual Capital and its interrelations. Based on experiences with pilot enterprises during the InCaS project, the following issues have to be taken into account when choosing the appropriate approach for a company:

- The Impact analysis is a simple way of assessing the IC factors' impact on a company's business success. It is appropriate for companies going through the ICS implementation for the first time or less experienced companies as it provides fast results within a short time, maximising the cost-benefit relation. Applying the impact scoring reduces the ICS implementation process to two workshop days with the ICS project team. The simple version can sensitise inexperienced companies for the ICS methodology by limiting the complexity of interrelating IC factors to core information. Start-up companies and micro-organisations may also prefer the Impact Scoring, as their organisational complexity is usually lower and might therefore not require an extensive analysis.
- On the other hand, larger or more experienced companies with a higher level of complexity are advised to go through the full version of the impact analysis (cross impact matrix). As the pilot implementations during the InCaS project have revealed, users already familiar with the ICS (ICS reimplementation) or management instruments in general will appreciate the additional information provided by the cross impact matrix. It offers deeper insights into the complex interrelations between their intangible resources and the linkages to business success and strategy. The full version requires one more workshop day, i.e. altogether three workshops with the ICS project team (for details see „European ICS Guideline“, available at www.incas-europe.org).

Following the need for common ICS standards, the RTD partners have focussed on diverse aspects of standardisation within the field of IC management and reporting in phase III. Possibilities of standardisation of the ICS procedure were discussed with standardisation bodies and experts in different countries. As a main result from these investigations, three levels of harmonisation were identified:

Common ICS Ontology

The “ICS Structural Model” outlines the main elements of the ICS. It provides a “common language” in terms of the definition of Intellectual Capital. Basic elements such as Human, Structural and Relational Capital and their relation to strategy,

business processes and business success are defined. The model is helpful for scientists as well as practitioners as it facilitates and structures the discussion by providing a basic taxonomy.

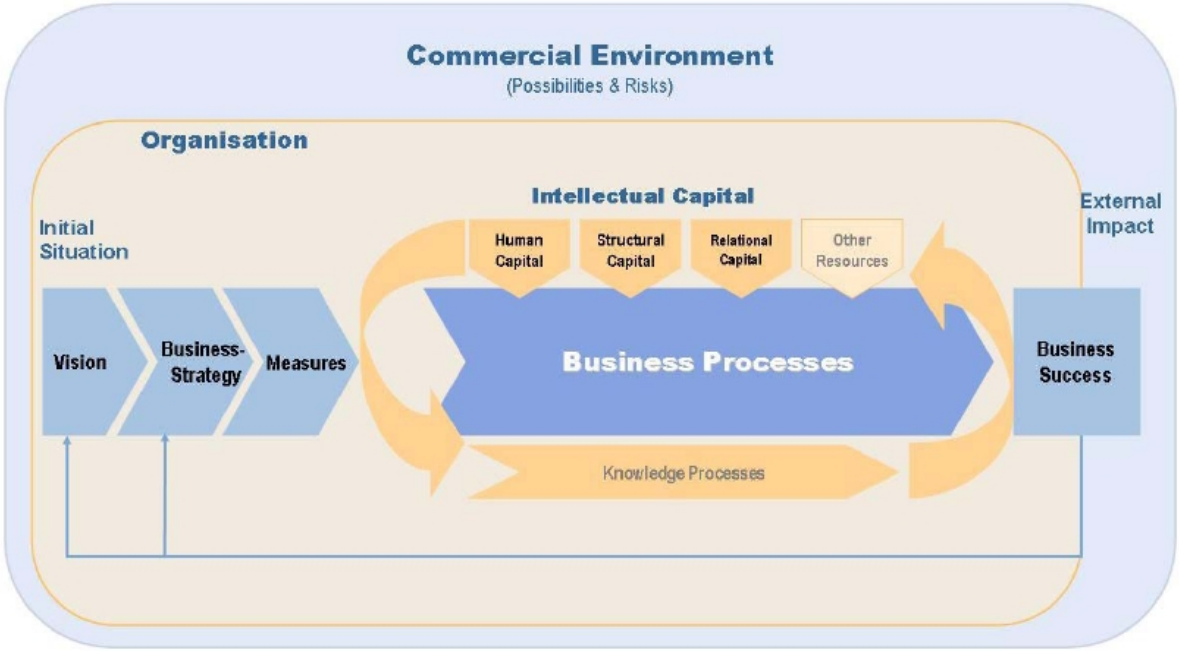

Figure 1: InCaS Structural Model. Source: European ICS Guideline.

Standard ICS Procedure

Furthermore, a standard process for the collection of IC information within the companies was defined (ICS Procedural Model). Especially for practitioners, a clear procedure and a common set of tools is the basis for practicability. Moreover, the ICS procedure leads to ICS documents with a standard structure. The standard ICS procedure as well as a standard structure of the ICS document will assure comparability between different ICS at a basic level.

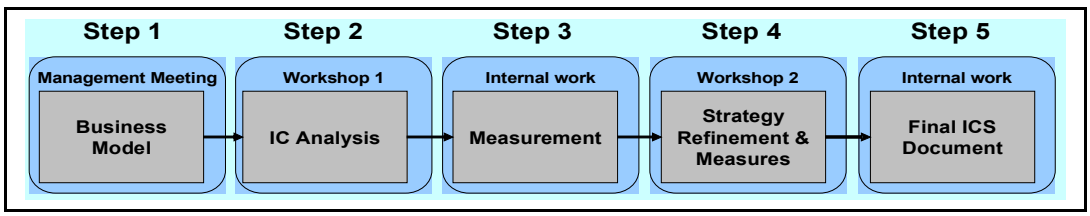

Figure 2: The Incas Procedural Model (European ICS Guideline 2008)

Content Harmonisation

Apart from the taxonomy and process, InCaS started with the harmonisation of the ICS content based on the empirical results collected in 50 pilot implementations: A first set

of common IC factors could be identified by analysing the frequency of the use and the definition of IC factors. The results from practice proved that approximately 80-90% of individual IC factors may be harmonised on an aggregated level, while the remaining 10-20% are completely individual (Mertins, Will 2008). Consequently, the company-specific assessment of those IC factors becomes basically comparable.

These efforts led to the development of basic quality requirements which are to be respected when implementing an ICS according to the European ICS Guideline (See additional module "M7 ICS Quality Requirements", available at www.incas-europe.org). The quality requirements contain all harmonised ICS elements (ICS taxonomy, process, standard IC factors). Altogether, these aspects are the most important part of the ICS quality assurance concept which will allow comparability of ICS documents based on a standard structure and a basic standard ICS procedure.

Phase III: Finalisation

These results served as an input for further discussion and research about standardisation of ICS for different purposes in phase III:

IC Benchmarking

Standardised elements of the ICS could serve as a basis for the comparison of IC between companies and opens up the possibility for an "IC Benchmarking": On the basis of a firms' assessment of IC factors, strengths and weaknesses can either be compared between single companies or between a company and a whole group, e.g. the respective industrial sector. Comparing to a larger group of companies can be useful for a company to derive individual measures in order to catch up with the level of IC within the sector. The aim of a comparison between single companies can be based on the desire to find suitable benchmarking partners in order to initiate best practice transfers or to exchange experiences between companies with similar or the same problems in a certain field of IC management.

External IC Reporting

By defining quality requirements of a standard ICS procedure as well as basic must-have elements in terms of content, the European ICS successfully led to a basic comparability of different ICS documents regarding structure and basic content. This can facilitate the communication towards external stakeholders: field reports and surveys have shown that complementing financial data with information on intangible resources can sharpen the view on SMEs' creditworthiness (Thomas 2003; Will, Alwert, Bornemann, Wuscher 2007). If some requirements about structure, content and length of an IC report are fulfilled (Wuscher, Will, Alwert, Bornemann 2006), it contributes to a more homogeneous rating of SMEs thanthe assessment of anaylists which are based solely on information from annual financial reporting.

Therefore the ICS reduces risks for both banks and SMEs (Alwert, Bornemann, Will 2007). With the analysis and the identification of basic quality requirements on structure and content elements InCaS has also successfully driven the development of the ICS as an external reporting instrument.

ICS Auditing

Experiences from ISO 9001 or the EFQM assessment clearly show the necessity of validation from a third party in order to strengthen the general credibility of an ICS towards external readers. To validate the matching between the ICS method and the factual implementation process, a concept for an ICS quality audit has been drafted and will be enhanced in the future (Mertins, Wang, Will 2007). This will contribute to the development of the ICS as an external reporting instrument and will ensure a long-term quality of the ICS method.

As a major result of InCaS, the consolidated ICS methodology has been summarised in the "European ICS Guideline" (available at www.incas-europe.org). The guideline describes the single steps of the ICS implementation in detail with the aim to provide practical support for ICS moderators and/or companies that want to implement an Intellectual Capital Statement. Templates and checklists supplement the European ICS Guideline, and the ICS Toolbox provides technical support for the collection and analysis of the IC information.

Main Project Results

European ICS Guideline for SMEs

Summarising all research results and practical experiences as well as the reviews of IC experts, the capital market and standardisation bodies, the project published a "European Guideline for Intellectual Capital Statements" serving as an instruction manual for further SME-users as well as defining minimal standards for IC benchmarking activities. It contains the experiences from the pilot implementations as well as practical guidance for ICS moderators and SMEs.

Supporting software "ICS-Toolbox"

To enable SMEs and trainers, a software tool (ICS toolbox) to support and accelerate the ICS process was developed, taking the experiences of the pilot-SMEs into consideration. Consisting of several components for methodical support and data management the final ICS toolbox is a significant part of the ICS methodology as well as the InCaS training programme.

50 Pilot-implementations

Since InCaS refers to a strong empirical research and development approach, one of the basic ideas of InCaS was to choose 25 pilot-SMEs in 5 core countries to implement a first version of their specific ICS, supported by specially qualified trainers and consultants (implementation leaders). The results of these pilot-implementations were used in numerous ways:

- As empirical research results to foster further methodical development,
- As "real" ICS published for proof-of-concept and raising public awareness, and
- As best practice partners to support dissemination and multiplication of the European ICS method across the European SME community.

Customized ICS modules for IC management

The experiences deriving from these pilot-implementations were used to elaborate the ICS methodology and to adapt it to the specific needs of SMEs. As a result, so called additional modules were developed to guide and support each individual SME according to its specific management experiences and maturity.

IC Benchmarking concept

Based on scientific and practical consensus from the pilot implementations, methodical standards reflecting the view of the Capital Market Community and standardisation bodies on minimal reporting requirements were set up. These reporting requirements will increase the comparability of IC on the European level and enable an IC benchmarking between different companies. For instance, a set of common IC indicators, a standard basic ICS procedure and a common IC taxonomy contribute to ICS standardisation and comparability between organisations.

Sustainability and quality assurance concept

As a result of these harmonisation and standardisation efforts, a consistent ICS implementation procedure and minimal IC reporting requirements guarantees a certain level of quality and provides the basis for an ICS quality audit.

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