

## IMPLEMENTING A FRAMEWORK FOR IC REPORTING IN ROMANIA

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**Abstract:** *The paper presents briefly an exploratory research used for debating the issue of intellectual capital (IC) in Romania. Our research is at a starting point for possible future theoretical and empirical investigations. This paper seeks to develop in Romania a framework of IC reporting by starting to learn and adapt some best practices identified abroad.*

**Key words:** *IC, knowledge economy, intangibles, best practice, balance scorecard*

### 1. INTRODUCTION

The main objective of this paper is to develop an evaluation model of IC for Romanian organizations and creating a level of awareness and involvement on the importance of intangible assets and their reporting in Romania, where we consider that the interest in knowledge assets is still low. Based on the literature review we noticed that in Romania there is not a quite clear conceptual complex and holistic framework of measurements carried out on qualitative performance factors. The measurement is fundamental to support management decision in allocation investment and the investor's decision regarding the value in comparison with the price. We underline that companies in Romania have to know that the reward for investing in IC and intangible assets is similar to the return on investment in knowledge capital, research and development.

### 2. STATE OF KNOWLEDGE ON IC REPOTING

Reasons why organizations measure their IC are: to formulate strategies to influence people's behavior and to validate external performance, which includes reporting and benchmarking (Marr et al., 2003 a, b). In the field of performance measurement there is a strong focus on creating frameworks, indicators and guidelines to support the management of IC (Roos et al., 1997; Bontis et al., 1999, Levinsky, 2001, Neely et al. 2003). Neely illustrates the evolution of the measuring approaches from the static measurements such as the Balanced Scorecard or Skandia Navigator (Edvinsson and Malone, 1997) to the most dynamic and open which present how value is created in a company (Kaplan and Norton, 2000).

There are a wide range of measurement methods in which both components of the trial balance and intangible assets are evaluated:

- **Direct IC methods (DIC):** estimating the monetary value of intangible assets by identifying its many components. Once identified, these components can be measured directly, either individually or as an aggregate. (Christina Suci, 2008)

**Strong points:** allow separate assessment of components of IC; allows combinations of monetary and non-monetary assessments; provide a broad view on a company's wealth.

**Weak points:** are specific to a particular company and can be difficult to compare and create a benchmark. Taking into account that it has many financial and non-financial data, it involves a lot of effort and costs in their analysis.

- **Market capitalization methods (MCM):** where the

difference between market capitalization and stockholders equity is calculated.

**Strong points:** best for illustrating the financial value of IC; good for comparison between firms in a given industry.

**Weak points:** not contain information about the components that contribute to IC; an exclusively monetary vision provides only a partial perspective; not suitable for overall view on the socio-economic and human development.

- **Return on assets methods (ROA):** intangible assets and financial growth figures are compared to the industry average. Which exceeds the average income is then used to estimate the value of intangible assets.

**Strong points:** Models are useful in assessing the financial value of IC; are optimal for comparison within an industry; built on traditional accounting and thus are easily accepted.

**Weak points:** not contain information about elements that contribute to IC; focus on value expressed in monetary units; not suitable for a comprehensive approach to social development - economic and human knowledge-based society.

- **Scorecard methods (SC):** the various components of IC are identified and reflected in terms of scorecards or graphs.

**Strong points:** can provide a more complex analysis on knowledge assets and performance than other models based on financial measures; a closer measure to the current inputs, processes and reporting results; are optimal for the task to detect and correct errors in inputs and processes to align with the outputs and outcome; the indicators can provide a useful file for carrying out the policies.

**Weak points:** contextual influences that facilitate the achievement of policies make comparisons in several contexts difficult; high level data revealed significant observations from the complex analysis may not be sufficient in terms of a rapid analysis and achieving a single standard.

- **Knowledge assets map:** knowledge assets are identified as the sum of organizational resources: stakeholder and structural. This framework can be used to help identify knowledge assets, which can then be the basis for visualization of how these assets are interrelated and transformed to satisfy stakeholder needs. Such visualization is called a value creation map and it shows the pathways of how value is created in organizations.

### 3. CREATING A GUIDE OF BEST PRACTICES

A guide to best practices in the field of IC will allow organizations to identify key processes and to look for solution that can be applied. Companies can extract existing knowledge and use it for strategic planning, process analyze, organizational development. Understanding what has been the cause of their success and what are the mechanisms used is the key to develop a method for evaluating intangibles and how it could also be implemented in Romanian companies. *The Croatian Program of Increasing Efficiency of National IC*, made in cooperation with the Ministry of Economy and the Chamber of Economy where more than 50 companies from different sectors participated in a series of steps to create awareness of knowledge economy and IC reporting.

In Germany, the accounting standards require companies to report IC management in the accounting, although this is not a requirement. Denmark requires companies to provide information on their human capital only if it is relevant to their economic activity, while in Austria reporting of human capital is now mandatory for all universities by the *Universities Act/2002*. The guide for IC declarations developed by the *Danish Ministry of Science Technology and Innovation* is the result of the long-term cooperation between researchers, companies, government organizations and consultants. The *IC declaration* is an integral part of the knowledge management in a company. It identifies knowledge management strategy that involves identifying objectives, initiatives and results in composition, application and development of knowledge-based resources of the company. It is formed by 4 dimensions: knowledge perspectives, managerial challenges, initiatives and indicators. The *Meritum project* is based on best practices observed in over 80 European companies and comprises definitions, a general model for IC management and a set of recommendations for how IC reports are made. Ericsson, the Swedish telecommunications company, has developed a commercial product called the *Cockpit Communicator*, based on the balanced scorecard. Celemi monitors three overall categories: customers; people; and organisation. Under each of these interdependent categories, the three key areas of growth/renewal, efficiency and stability are tracked, each with its own performance indicators. Measuring IC in the company *Gorenje* is closely connected with the establishment of the *Innovation Centre of Gorenje Group* in 2004. *Infineon* is another good example with their IC Report. It emphasizes the outstanding importance of knowledge and provides the stakeholders and the general public with information regarding corporate strategy.

#### 4. A METHODOLOGY FOR MEASURING KNOWLEDGE ASSETS

We adapted this methodology to fit the problems and needs of organizations in Romania and to focus on the holistic development for competitiveness and human development. We should first mention that creating an *IC National Center* should be the first stage in order for it to supervise all policies or projects related to IC. The process consists of 5 main phases and is developed based on lessons learned and best practices:

- *Developing a vision for the knowledge organization*- the establishment of a IC team in the company is the main step.
- *Awareness and education*: During the project a minimum level regarding knowledge should be offered by a range of courses and trainings. A manual on IC in companies will be distributed free, also the last report on "*IC Efficiency at National, Regional and Company Level*" containing information about efficiency and value creation.
- *Adapting the Balance Scorecard* for measurement: develops a model of the Balanced Scorecard for measuring and managing knowledge assets for organizations. The method helps to observe links between practice and performance results. The four perspectives of the Balance Scorecard that we established have at the heart the vision and strategy: learning and growth; organizational processes; stakeholder's satisfaction and value creation. These perspectives are made through the following strategic management activities: knowledge management, organizational process improvement, relational management and budget management and cost. The measurement must be performed at various levels: company level but also offices, processes, projects or product lines. A Balanced Score software program is required to be installed in the company and all team members to learn how to use it.
- *Visualizing and evaluating IC*: the situation can be scanned using a set of questions related to IC as part of a software. The

focus categories are: human capital; structural capital; relational capital; location capital.

- *Transformation to a value oriented organization*: in this last step IC consultants, working with the management teams will provide new perspectives and opportunities in dealing with reality. Depending on the results of Balanced Score method and software analysis they will need to continue improving performance for the company.

#### 5. CONCLUSIONS AND RECOMMENDATIONS

In the knowledge-based economy, IC provide a competitive advantage and is fundamental to support the measure making management decisions in the allocation of investments and investors' decision on the value comparative to price. National policies should be implemented to begin to measure IC and create a supplement to the annual financial records to report IC. Organizations in Romania should be encouraged to make reports containing views of the vision and business goals, challenges and actions of management. We propose for further research the development of operational parameters in Romania and of empirical methodological studies based on dialogue and dissemination of knowledge. We are interested what is the perception and awareness of intellectual capital in our country and in particular the importance of intellectual capital reporting as part of the annual statement. This part will be achieved through a case study, completed questionnaires on the perception of intellectual capital in organizations in Romania.

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