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This is an **author produced version** of a paper published in:

ICFAI Journal of Accounting Research 8.2 (2009): 17-29

DOI:

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MERITUM and Danish Guidelines for Reporting on Intangibles: A Comparative Study

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This paper presents and compares two of the most renowned guidelines—the Danish and the MERITUM—on reporting of intangibles which have been developed in Europe in recent years. Both works propose a set of recommendations on how to complement traditional financial statements with the publication of an intellectual capital report disclosing additional information on a firm’s intangible resources and activities. The study observes some differences between these two guidelines in their methodology and scope, the terminology they use, and the way they classify actions and indicators. The study, based on personal interviews, has important policy implications and recommendations for practitioners.

Introduction

The purpose of this study is to present and compare two of the most renowned guidelines for reporting on intangibles¹ which have been developed in Europe in recent years: the “Guidelines for the Management and Disclosure of Information on Intangibles”, developed by MERITUM, a EU-funded research network; and “A Guideline for Intellectual Capital Statements”, authored by a task-force financed by the Danish government (Figure 1). Both guidelines consist of a set of recommendations, useful for practitioners, on how to manage and report on Intellectual Capital (IC). Among the existing guidelines, they probably have the broadest institutional and corporate support, and they have been applied by hundreds of firms and research centers across the globe (Nordika, 2002; and Bukh and Johanson, 2003).

The comparison is based on an analysis of the two final reports which were published and on personal interviews with the authors of the guidelines.² The interviewees included the Research Director of the Danish guidelines, Jan Mouritsen and the Research Director of the MERITUM project, Paloma Sánchez, as well as other researchers involved in the development of those guidelines.

Two different arguments justify the relevance of this comparative study. On the one hand, it may be useful for a practitioner interested in exploring the relative strengths of each of the

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¹ The terms ‘intangibles’ and ‘Intellectual Capital (IC)’ have been used interchangeably in the literature. We adopt the view that IC can be defined as the combination of all the intangible resources and activities of an organization.

² The quotes without a reference throughout the study refer to these interviews.

guidelines, which may be more appropriate for his/her organization, and the ways in which they could eventually complement each other. On the other hand, it sends a clear message to the academic and policymakers involved in the development of this kind of guidelines: the need for a consensus on basic issues, like terminology, in order to improve the homogeneity and comparability of information provided by companies using alternative guidelines for reporting on IC.

Figure 1: Key Features of the MERITUM and Danish Guidelines	
MERITUM Guidelines	Danish Guidelines
Funded by the Targeted Socio-Economic Research (TSER) Program of the European Union Commission.	Financed by the Danish government.
Developed by the MERITUM Project (“Measuring Intangibles to Understand and Improve Innovation Management”), a consortium comprising researchers from six European countries (Denmark, France, Finland, Norway, Spain and Sweden) plus a steering committee and a wide group of supporting institutions.	Developed by a task-force comprising researchers from the Copenhagen Business School and the Aarhus School of Business (Denmark), the Danish Agency for Trade and Industry and consultants from Arthur Andersen Denmark.
Directed by Professor Paloma Sánchez from the Autonomous University of Madrid.	Directed by Professor Jan Mouritsen from the Copenhagen Business School.
First published in 2001. Further developed thereafter through different EU-funded projects such as E*KNOW-NET, RICARDIS and PRIME.	First published in 2000. A second, improved version was published in 2003 after further testing in 100 Danish companies. The second version includes a separate guideline on how to interpret IC reports, addressed to financial analysts.

Guidelines for Reporting on Intangibles

The increasing impact of intangibles on corporate performance may result in increased uncertainty and capital market inefficiencies, since only a small proportion of the firm’s IC is reflected in the financial statements (Lev and Zarowin, 1999). In other words, the information provided by the traditional financial statements, without disclosing full information on intellectual capital, does not reflect the real value of the firm. The lack of adequate information on IC may result in an inefficient allocation of limited financial resources, ultimately curtailing economic growth. It is also seen as one of the major reasons behind the increased volatility and information asymmetry in capital markets. In order to fill this gap, there is a growing need for reporting on intangibles by means of IC reports, which complement traditional financial statements with further information on the critical intangibles that drive innovation and future business performance. Enhanced transparency through IC reporting is not only demanded by capital markets, but also by other firm stakeholders, such as its employees, customers, suppliers and, in general, the society.

A good IC report allows its reader to measure the extent to which the firm is advancing towards the achievement of its strategic objectives through the development of its critical intangibles.

IC reports contribute to unveiling enhanced information on the firm's strategy, on its relationship with clients and suppliers, its human capital, its innovative capacity, and other critical intangibles of the firm. This kind of information is increasingly being weighed in financial analysts' decisions (Richardson and Welker, 2001; and Low and Kalafut, 2002). As argued by Cañibano and Sánchez (2004), in order to improve financial analysts' response to knowledge-based ventures, they need a coherent, agreed, homogeneous, reliable and verifiable set of principles and indicators for analyzing intellectual capital, and this is precisely what IC reports strive for. In addition, IC report is, not only a highly efficient communication device, but also a very powerful management tool (Mouritsen, 2003). Given the popular premise that only what can be measured can be managed, IC reports enable a more efficient management and control of the intangible resources and activities that drive innovation and value-creation.

For all these reasons, IC reports are widely being promoted as the preferred means to overcome the limitations of financial performance measures from different platforms, including the European Commission, the OECD, governments, academics and business associations. Indeed, the importance attached by corporate managers and policymakers alike to the IC reports has grown dramatically in recent years. The success of the pioneering experience of Skandia, a Swedish insurance company, in the mid-1990s, has encouraged many other firms worldwide to implement IC management and reporting systems (Ordoñez de Pablos, 2001). In addition, IC reporting has also attracted the attention of organizations other than business firms: an increasing number of non-profit organizations, research centers, universities and governments of regions or nations are now publishing IC reports and using them as a managerial tool (Sánchez and Elena, 2006).

The origin of IC reports dates back to the early 1990s, when a variety of models for IC management were developed and disseminated worldwide. The most popular among these pioneering tools are probably: the Balanced Scorecard (Kaplan and Norton, 1996), the Intangible Asset Monitor (Sveiby, 1997), the Skandia Navigator (Edvinsson and Malone, 1997) and the Technology Broker (Brooking, 1996). More recently, in Europe, some publicly funded initiatives led by academics have aimed, as recommended by OECD (1999), at developing widely accepted guidelines to help companies in the process of developing IC reports, while contributing to a stronger standardization of reporting practices in the longer term. The MERITUM and the Danish guidelines are two of the most prominent examples of this trend.

The MERITUM Guidelines

The MERITUM guidelines are based on best practices observed among 80 European firms and were validated through a Delphi study. Its first chapter develops the conceptual framework, containing precise definitions of the terminology used. Thereafter, the report is divided into two main parts—a model for IC management and a set of recommendations on how to prepare IC reports. The model for IC management proposed by the MERITUM guidelines comprises the following three phases:

- **Identification:** After clearly articulating the 'vision of the firm', this phase consists of identifying the 'critical intangibles' required to attain the firm's strategic objectives.
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Next, a set of 'intangible resources' and 'intangible activities' are attached to each critical intangible, by means of which the latter will be attained and the process will be monitored. As a result, a 'network of intangibles' emerges, providing the firm with a clear picture of current intangible resources, which have to be developed in the future and of the activities which need to be undertaken in order to attain the strategic objectives.

- **Measurement:** This phase involves defining specific indicators to be used as a proxy measure of the different intangibles which were identified in phase 1. The guidelines explain the desirable characteristics that these indicators should hold and provide examples of good practice.
- **Action:** This phase entails the consolidation of the intangibles management system and its integration within the firm's management routines. It is a learning process that involves monitoring and evaluating the effect that the different activities have on the firm's intangible resources, critical intangibles and strategic objectives.

In the second part, the MERITUM guidelines describe how to prepare an IC report, comprising three sections (Figure 2). First, the 'vision of the firm', i.e., a narrative of the firm's strategic objectives and critical intangibles. Second, a 'summary of intangible resources and activities', which represents a disclosure of the activities to be developed in order to attain the strategic objectives. And third, the 'system of indicators', which allow the reader to assess how well the company is doing in attaining its objectives. The guidelines recommend classification of different intangible resources and activities, as well as their corresponding indicators, under the following three categories, which jointly conform the IC of the firm:

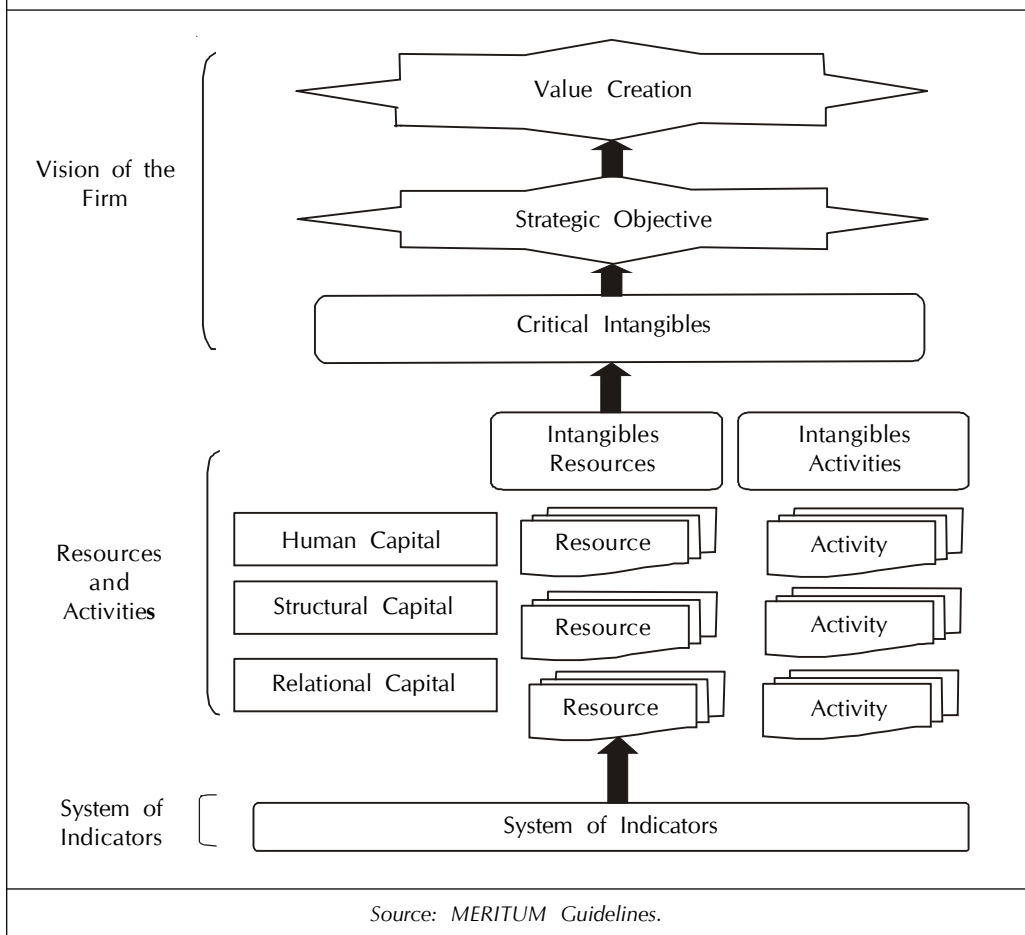
- **Human Capital:** The knowledge that employees take with them when they leave the firm. It includes the knowledge, skills, experiences and abilities of people.
- **Structural Capital:** The knowledge that stays within the firm at the end of the working day. It comprises organizational routines, procedures, systems, cultures and databases.
- **Relational Capital:** All resources linked to the external relationships of the firm. It comprises human and structural capitals involved with the company's relations with stakeholders (investors, creditors, customers, suppliers, etc.) plus the perceptions they hold about the company.

Finally, the guidelines conclude with a set of recommendations on how to collect information, who should prepare the information in the company and the frequency of reporting.

The Danish Guidelines

The Danish guidelines describe how to prepare an 'intellectual capital statement' in practice. They draw on the experience of 17 Danish companies which participated in the project by means of preparing two sets of IC statements under the supervision and assistance of the Danish guidelines' task force. Thus, they include in-depth examples from the IC statements prepared by these firms. The guidelines emphasize that the IC statement is an integral part of knowledge management within a company, but does not specifically describe a model for knowledge management.

Figure 2: A Schema for the Presentation of Intellectual Capital Reports



The Danish guidelines propose a process for preparing IC statements comprising the following four phases (Figure 3):

- **Knowledge Narrative:** This first phase involves defining the mission of the firm, the ‘use value’ (i.e., the value for the final customer) of the product or service offered by the firm and the conditions of production, with special emphasis on the system of knowledge and competencies.
- **Management Challenges:** This second phase consists of identification of a set of ‘management challenges’ which are to be addressed in order to develop and realize the ambition defined in the first phase. In other words, it involves translating the company’s knowledge narrative into specific management challenges. More importantly, it involves a selection of an action plan among the different strategic alternatives available to implement the knowledge narrative.
- **Actions and Indicators:** The objective of the third phase is to develop detailed actions attached to each management challenge, as well as specific indicators to measure the

impact of each of those actions. With respect to the classification of these actions and indicators, the Danish guidelines are very flexible, proposing some examples, but not a unique classification method.

- **Reporting:** This final phase involves the preparation of the IC statement, which is composed of text, figures and illustrations. The text serves to communicate the company's knowledge narrative, its management challenges and actions, as well as to provide a general description of the company. The figures present a detailed picture of the different management challenges, the actions attached to them and the specific indicators used to measure the impact of those actions. The illustrations are specially meant to communicate the style and cultural identity of the company.

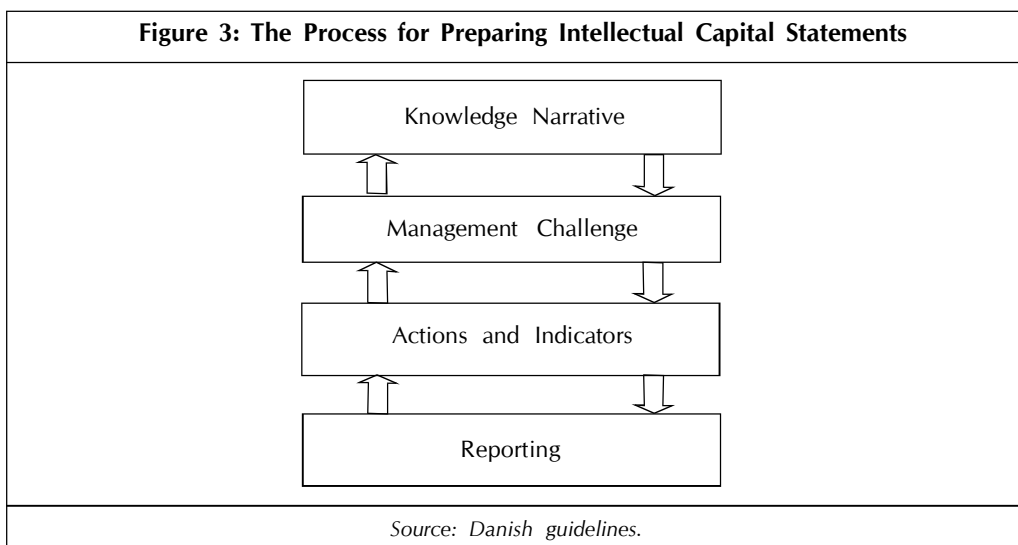
According to the Danish guidelines, it is a good practice to report on the accounting policies used and to include a statement of an auditor in the IC statement. Finally, in its appendixes, it provides some detailed examples, a survey of indicators that could be used in an IC statement, a summary of the differences between IC statements and social statements, and a glossary of terminology.

A Comparison of Two Approaches

As argued by Bukh and Johanson (2003), the process described in the two guidelines is very similar. They are, indeed, very coherent with each other. Nevertheless, some relevant differences between the two guidelines can be found in the terminology they use, in their methodology and scope, and in the way they classify actions and indicators.

Scope and Methodology

In a way, the MERITUM guidelines can be seen as being more ambitious in scope, since besides describing how to prepare an IC report, they also propose a model for managing intangibles. Conversely, the Danish guidelines focus only on how to prepare an IC statement.



In the words of Professor Manuel García-Ayuso, a member of the MERITUM project, “The MERITUM guidelines are more ambitious, because they start with the management process and then proceed with the reporting process. The intellectual capital report is presented as the logical conclusion of the intangibles management process. So they clearly have a deeper scope”.

However, it could be argued that the Danish guidelines are also concerned with the management process since, alongside their recommendations on how to prepare an IC report, they also provide useful suggestions on how to manage it.

The different methodologies employed in the development of the two guidelines have a clear influence on their final results. The Danish guidelines were produced with the involvement of a group comprising government officials from the Danish Agency for Trade and Industry, consultants from Arthur Andersen and researchers from two Danish universities. They concentrated on a group of 17 Danish companies which were guided and supervised as they produced two sets of IC statements. These companies had previous experience in IC management. The involvement of the Danish government and the consulting firm, Arthur Andersen, helps explain the fact that the Danish firms were more easily mobilized than those from other countries which participated in the MERITUM project.

On the other hand, the MERITUM guidelines were developed by a wider range of researchers more disperse geographically, and it was thus harder to build consensus. A broader range of companies were analyzed, but the research team did not work as closely with those companies as the Danish team did. A draft version of the MERITUM guidelines was validated by a group of experts by means of a Delphi analysis. So in a way, it follows that the MERITUM approach is more precise in its grounded theory.

The following quote from an interview with Paloma Sánchez, director of the MERITUM project, serves to illustrate the impact of the different methodologies on the final results:

“For a collective such as the Danish firms, which have been measuring and managing intangibles for a long time, an instrument that they can apply immediately such as the Danish guidelines is very useful, so in this case the approach followed by the Danish team has been very adequate. However, when the goal is to work towards an international framework, towards a set internationally-harmonized guidelines, I believe that the approach we have adopted makes more sense. Our starting point has been to build a strong conceptual framework which is widely accepted and which facilitates the analysis by external agents. The process of developing and implementing internationally accepted guidelines to report on intangibles is a very long process on which many different parties need to agree, and which has to be useful for many different purposes. From this perspective, I believe that the MERITUM approach is more adequate than that of the Danish guidelines.”

On the whole, their different approaches explain why the Danish guidelines are more user-driven and provide a wider range of examples. On the other hand, the MERITUM guidelines are more theoretical, but their big strength is precisely the consensus that was built among the researchers from the different countries involved.

Conceptual Framework and Terminology

While the guidelines are describing the same process, they use a different language which may lead to confusion for the readers. The first difference can be found in the titles of the two guidelines. While the MERITUM guidelines use the term ‘intellectual capital report’, the Danish guidelines refer to it as the ‘intellectual capital statement’. When it comes to reporting on IC, the MERITUM partners believe that the term ‘report’ is preferable because it denotes a voluntary character, whereas the term ‘statement’ is associated with the traditional financial statements, which are compulsory and must conform to a given format. In the methodological appendix of the MERITUM guidelines, there is a clear description of why the term ‘intellectual capital report’ was chosen, validated by a Delphi analysis.

However, Professor Mouritsen, Director of the Danish guidelines, disagrees with this reasoning: “report to me sounds as if it is something that has a fixed format of reporting a certain issue, while a statement is an expression, and therefore has more narrative nodes to it than a report”, he explains. However, in practical terms, this is only a slight difference with no further implications. The differences that will be discussed next are clearly more relevant, in the sense that they are more likely to lead to confusion among users.

Throughout the Danish guidelines, the terms ‘intellectual capital’ or ‘intangibles’ are rarely used. Instead, they use the terms ‘knowledge management’ and ‘management challenges’. On the other hand, the MERITUM guidelines prefer to use the terms ‘intangibles management’ and ‘critical intangibles’. Nevertheless, it must be noted that the definition of knowledge employed in the Danish guidelines is a very broad one, so in effect ‘knowledge management’ can be considered to be equivalent to ‘intangibles management’ (Figure 4).

Figure 4: Different Terms for Similar Concepts		
MERITUM Guidelines		Danish Guidelines
Intellectual Capital Report	↔	Intellectual Capital Statement
Intangibles Management	↔	Knowledge Management
Vision of the Firm and Strategic Objectives	↔	Knowledge Narrative
Critical Intangibles	↔	Management Challenges

The authors of the Danish guidelines justify their choice by stating that their wording is clearly more appealing to users. In the words of Professor Bukh, who was involved in the development of both the Danish and the MERITUM guidelines, “intangibles is an accounting word, whereas knowledge management is more closely related to strategy and therefore much more appealing to companies”. Professor Mouritsen argues that another reason why they use the terms ‘knowledge management’ and ‘management challenges’, instead of ‘intangibles management’ and ‘critical intangibles’, is that they do not focus solely on intangibles. “In our guidelines we don’t make that distinction between tangibles and intangibles (...) and I think some of the problems we have in this field today is that we take this distinction too seriously”, he explains.

Another clear difference originates from the stronger emphasis of the Danish guidelines on ‘use value’ (i.e., the value that the company’s products or services provide to its end customer). Indeed, the Danish guidelines support the view that the knowledge narrative and the strategic objectives must clearly determine their link with the end customer. The MERITUM guidelines, on the other hand, attach less importance to this idea, and emphasize that strategic objectives may be formulated in relation to other stakeholders, such as suppliers, employees, investors or the society as a whole. As a result, an IC statement prepared by following the Danish guidelines will tend to have a clearer description of the link between the firm’s goals and its customers. According to the Nordika Report (2002):

“Using the Danish guidelines will put the focus on ‘value in use’ to create value for users by its total forces, relying not on a single factor but on multiple factors and on what actions the company takes to meet its challenges. Using the MERITUM approach will bring into focus how the company—through the connectivity of critical intangibles in a network—pursues its strategic objectives and by this focus on how to create value for users and other stakeholders.”

Since the underlying concepts are in effect very closely related and coherent, it could be argued that the differences in terminology are only a minor issue. However, we believe it was useful to bring some thought into these differences and to clearly identify the analogies between the different terms used to refer to the similar concepts. We can conclude that the language employed by the Danish guidelines is easier to understand and more appealing to users, while that of the MERITUM guidelines is more precise and theoretically consistent, but harder to apply. However, this remains still to be tested, specifically by bringing the practitioners’ opinions into the analysis. As argued by Professor García-Ayuso, “It is not so easy to state which terms are more attractive for the firm; one cannot generalize. We have seen that it depends a lot on the country, on the industry sector and on the specific firm which we’re talking about”.

Actions and Indicators

As stated earlier, the MERITUM guidelines recommend classifying actions and indicators into three categories—human capital, structural capital and relational capital. The Danish guidelines adopt a more flexible approach, suggesting that actions and indicators be classified into employees, customers, processes and technology, but leave the option for the firm to decide. According to Bukh, “The classification is not that important in practice. The important thing is to develop indicators. You can later group them to put things more nicely, but it’s only a communication device and I find it to be counter-productive management-wise.”

Additionally, the MERITUM guidelines classify intangible activities into the following three groups: (1) Activities that develop new intangible resources internally or acquire them externally (for example, attracting new employees with a specific knowledge), (2) Activities that increase the value of existing intangible resources (for example, training existing employees), and (3) Activities that assess the effects of the previous two activities (for example, surveys of employee satisfaction). While this classification is very precise from a conceptual viewpoint,

it might be confusing, when implemented in practice. The Danish guidelines do not propose any such classification.

Regarding indicators, the Danish guidelines include a complete list of the most frequently used indicators. The MERITUM guidelines also present a list of possible indicators, but this list is smaller and does not offer as much information on how to compute and interpret them. This is another example of the more user-driven approach of the Danish guidelines.

Relative Strengths

In the words of Professor Mouritsen, “The strength of the Danish guidelines is that they are more user-driven, more practical, more implementable”, while “the main value of the MERITUM guidelines is the knowledge and consensus that was built among the different countries which were involved”. Professor Sánchez, Director of the MERITUM project, agrees that the strength of the Danish guidelines is that these are easier to implement. On the other hand, she believes the main strength of the MERITUM guidelines lies in its conceptual framework. “One of the main strengths of the MERITUM guidelines is the development of a strong conceptual framework which is widely accepted”, she said.

Professor García-Ayuso, member of the MERITUM project, argues, “the MERITUM guidelines are more abstract, more theoretical, harder to apply, and less didactical”. For Professor Bukh, coauthor of the Danish guidelines, the strength of the MERITUM guidelines is that they have “more arguments, a deeper conceptual framework and a better literature review”, while the strength of the Danish guidelines is that they are “easier to implement because they have more ‘facilitating devices’”. Hence, there seems to be a strong consensus with respect to the relative strengths of the guidelines. Figure 5 provides a comparison of both the guidelines with respect to the main variables analyzed, reflecting the opinions which were gathered through the different interviews.

Figure 5: Benchmarking Guidelines		
	MERITUM Guidelines	Danish Guidelines
Main Strength	Developed with consensus from wide range of researchers coming from six different European countries and from different disciplines.	User-driven, implementable. Better use of examples, facilitating devices and indications on how the firm should proceed.
Scope	Deeper scope, including IC management and reporting.	Limited to IC reporting.
Presentation	Black and white. Insufficient use of examples.	Colorful and appealing. Includes a wide set of examples.
Conceptual Framework	Precise conceptual framework.	Ambiguous terminology but more appealing to users.
Actions and Indicators	Classified into human capital, structural capital, relational capital.	Flexible classification.

Conclusion

It should be emphasized that the two guidelines have more similarities than differences. Therefore, applying one or the other approach should not result *per se* in significantly different IC reporting practices. In addition, given their complementarities, it has been suggested that using both simultaneously could provide an enriched framework. As illustrated by Bukh (2003), “in a way, the Danish guidelines start where the MERITUM guidelines end, because the MERITUM guidelines have more on the conceptual framework and the management process, while the Danish guidelines have more clear advice on how to proceed in practice”. However, the differences among the guidelines—especially language differences—could prove to be a serious obstacle in this endeavor. Hence, those differences should be understood by the user before proceeding to their simultaneous implementation.

Moreover, stronger consensus and coherence may be needed among the research community prescribing guidelines for IC reporting, since the capital market inefficiencies can only be properly addressed if the information on IC provided by different firms is comparable. Indeed, the heterogeneity of reporting practices across firms, and the subsequent lack of comparability, have been identified as the main barriers that limit the current impact of IC reporting in capital markets (Bukh, 2003; García-Ayuso, 2003; Holland and Johanson, 2003; and Guimón, 2005). In addition, by building a stronger consensus among users unnecessary conceptual discussions can be reduced, communication among researchers would be facilitated, and this should set the pace for faster advancements in the field. The identification of best practices among the existing guidelines should be the starting point of such harmonization efforts, hence the relevance of this comparative study.

However, it also needs to be acknowledged that there are forces acting in the opposite direction. Specifically, resistance to change and vested interests among the various parties promoting specific approaches (professional bodies, research groups, entrepreneurial associations, national governments, etc.) are both important obstacles to standardization. More importantly, firms clearly demand freedom of choice and flexibility when it comes to managing and reporting on IC, and oppose further regulations. In particular, cultural differences may demand different kind of guidelines for IC reporting (Chaminade and Johanson, 2002). From the perspective of the academic community, it can also be argued that we are still at an early stage of research where the variety of initiatives and perspectives stimulates new insights. But while full standardization might not be desirable, the aim should be to reach some agreement on a minimal set of indicators, some of which could be industry-specific. ■

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