Guidelines for Disclosure of Intellectual Assets Based Management

Ministry of Economy, Trade and Industry
October 2005

Contents

Introduction

This guideline, compiled by METI, aims to help corporations (managers) that prepare intellectual assets based management report and those who assess it. Based on the examination of Subcommittee on Management & Intellectual Assets, New Growth Policy Committee, Industrial Structure Council, it provides a guide for information disclosure concerning intellectual assets based management.

Intellectual assets based management is a management itself rather than an aspect of management. It is a management method to enhance corporate value with an eye to many stakeholders. Based on the pursuit of interest, this method intends to make sustainable profits and growth through making the best use of the corporation's own ability. In that context, this guideline would also be a great help in preparing and appreciating reports on CSR and sustainability reports.

Note: Please refer to the Interim Report on intellectual assets based management published by the Subcommittee in August.

http://www.meti.go.jp/policy/intellectual_assets/english.htm

Chapter 1 Background

1. Significance of IA based management

In the age of knowledge economy, differentiation is vital for corporations to make sustainable growth. In order to different from others, it is increasingly important to conduct management utilizing intangible intellectual assets such as human resource, technology, organizational skills, network with customers, brands, etc., which no one can imitate easily.

Each corporation has its peculiar intellectual assets. Combination and utilization of them brings about value. Therefore, intellectual assets based management is hard to be imitated by other companies. Top managers should bear in mind this fact more than ever. They are required to reassess current management, recognize its strengths, its own value creation method, and peculiar intellectual assets that are the source of them, and then implement management taking full advantage of them (intellectual assets based management).

Regarding intellectual assets and value creation, analysis should be performed in consideration of the past experiences and performance. Based on this analysis, management policy should be clarified to enhance corporate value, namely, the creation of future value and profits. In deciding future policy, future uncertainty needs to be made clear.

Intellectual assets based management is nothing less than reconfirmation and utilization of the corporation's potential. It optimizes the allocation of management resources fro the whole economy, enhances corporate value, and then brings about a positive impact on global economy as well as domestic economy.

2. Virtuous cycle of IA based management and assessment

Intellectual assets based management is important for either individual corporations or the whole corporate management. In order to make it root more popular and widely-spread, it is necessary for stakeholders to recognize its importance and evaluate it adequately. Efforts by the corporation are also necessary. It is important to gain broad understanding from stakeholders of intellectual assets and the management based on them,, and of future profits and corporate value realized through this management, which are not clearly mentioned in financial statements.

If appropriate appreciation is received from stakeholders through these efforts, corporate value in the market would be enhanced (increase of market value, etc.), and financing would be easier. In addition, efforts and investment for the creation and utilization of intellectual assets, a source of appreciation, would also be increased. This would enhance corporate value and intellectual assets based management furthermore, which would lead to the next cycle, and thus a virtuous cycle is created.

3. Role of disclosure of information on IA based management

In order to deepen understanding, it is prerequisite for a corporation to implement intellectual assets based management. On this premise, what kind of profits the corporation will make in the future is discussed, taking into consideration the past performance. This is the highest interest for both corporations and stakeholders. Today, corporations disclose various information, however, information on corporate value or future profits is not satisfactory for either corporations nor stakeholders. Therefore, in order to match the needs of both parties, it is desirable to set a guidepost for disclosure, giving know-how of explanation on future profits and what kind of management will enable them. Appropriate information disclosure would lead to deepen recognition and understanding of both parties, evolve intellectual assets based management further, and enhance corporate value. This guideline intends to play a role as such a guidepost. We hope that corporations prepare intellectual assets based management report using this guideline and that the report is adequately appreciated.

Please bear in mind that disclosure is a means to make intellectual assets based management more meaningful. What is important is IA based management is actually put into practice. Voluntary efforts of corporations are especially important. Additionally, disclosure of information itself is less important than the actual practice of IA based management by corporations, which is reflected to the disclosure.

Chapter 2 Outline of IA Based Management Report

1. Objectives

Reflecting the idea shown in Chapter 1, fundamental objectives of intellectual assets based management report are:

(1) Top managers inform business activities to produce sustainable profits and enhance corporate value to stakeholders in a story easy to understand, and

(2) Share a sense of value with stakeholders.

2. Basic principles

Intellectual assets based management report is to appeal corporate activities to stakeholders. Its format and contents vary because each corporation can choose its own way to inform what it wants to inform. However, it is desirable to meet the following common principles to achieve objectives (Chapter 2-1) and the idea shown in Chapter 1.

(1) Showing the overall picture of corporate management from top manager’s eye in a story

(2) Focusing on the future value creation that affects corporate value

(3) As a prerequisite for the future value creation, evaluating future uncertainty (risks/chances) fairly and explaining how to deal with them

(4) Making a report easy to understand for important stakeholders (stockholders, employees, clients, creditors, communities, etc.)

(5) Supplementing and complementing financial information

(6) Adding supporting key performance indicators (KPI) to the points of the story to enhance credibility. Explanation on status of internal control is also desirable.

(7) Providing historical comparability (e.g. KPI for the past two years)

(8) Giving explanations reflecting the current business activities in a consolidated based accounting.

3. Factors described in IA based management report

Intellectual assets based management report is desirable to have following factors so that it satisfies basic principles (Chapter 2-2) and enables sharing a sense of value with stakeholders.

(1) Business characteristics and the direction of management

(2) Performance including predicted one in the future

(3) Intellectual assets and value creation method through the combination of them, that are the base of the past and the future performance,

(4) Identification of future uncertainty and how to deal with it

(5) Intellectual assets indicators as KPI to support the above

Other indicators can be attached as reference.

4. Typical style of IA based management report

Considering the idea of Chapter 1 and 1 to 3 of Chapter 2, following contents are desirable for typical intellectual assets based management report.

This format is not a template; it can be customized by each corporation.

[Main body]

(General) Basic management philosophy
Outline of business characteristics

(From Past to Present)

- A: Management policy in the past
- B: Investment (based on A) (performance figures included)
- C: Unique intellectual assets accumulated in the company, strengths based on them, and value creation method (based on A and B) (supporting intellectual assets indicators included)
- D: Actual performance in the past, such as profits (as a result of value creation C) (figures included)

(From Present to Future)

- E: (Based on C and the assessment of the past to the present)Intellectual assets that rooted in the company and will be effective in the future, and future value creation method based on them (supporting intellectual assets indicators included)
- F: Identification of future uncertainty/risks, how to deal with them, and the future management policy including those elements
- G: New/Additional investment for maintenance and development of intellectual assets needed (in line with the management policy F) (figures included)
- H: Expected future profits, etc. (based on E to G) (numerical targets included)

[Attachment]

Other intellectual assets indicators (optional)

5. Other reminders

(1) Disclosure is on the voluntarily basis.

(2) Any corporation, whether public or closed, can make a disclosure using this guideline.

(3) Instead of preparing a new report, it may be possible to be a part of the existing disclosed documents, such as annual report or sustainability report. (It may also be described as a general statement overlapping other reports.)

(4) Regarding future performance, it should be noted that the estimation is based on the current recognition.

(5) Continual disclosure is desirable, though it does not have to go with the “fiscal year”.

Chapter 3 Specific descriptions and reminders

Followings are specific forms and descriptions of “intellectual assets based management report” for disclosure.

1. Overall picture

“Main body of IA based management report”

Intellectual assets, corporate value creation using them, the future profits and their sustainability are explained in a form of a story. Some supporting intellectual assets indicators (quantitative information) are included in the story.

“Attachment to IA based management report”

What is generally considered relevant to intellectual assets is described, referring to the example of typical intellectual assets indicators as shown in Annex 1. (optional)

2. Description of the main body (story)

(1) General

1) Basic management philosophy

Basic policy and targets that top manager always speaks of both within or to outside of the company are described in a way easy to understand. Top manager appeals to stakeholders in his/her own words to ask for their understanding. This part aims to augment supporters of the corporation.

The spirit shown in the corporation motto is embodied to some extent in the context of business activities. This is the philosophy of management, in other words, the raison d’etre of the corporation. It is the basis in making big business judgment, and enhances predictability of corporate activities for stakeholders’.

2) Outline of business

Regarding the main business, the status of supply chain including products and services provided, customers, trading partners, and distribution is explained briefly. (As for customers, it is preferable to show the ratio of the deal B-to-B and B-to-C.)
Status of the market of main products/ services, competition with other companies and related institutional frameworks are also briefly mentioned, as a surrounding business environment.

(2) From Past to Present

A “Management policy/visions of the past”

Management policy/visions of the past that had been partly disclosed are shown. It should not be made retroactively. Specific reference such as description in the past annual report is preferable.

B “Past investment performance”

The strategy and contents of the past investment (selection and concentration), and the consistency with the whole management policy (A) are described.

C "Asset and value chain that accumulated in the corporation"

Corporation's strengths, unique value creation method (value chain), and intellectual and tangible assets that are the origin of the strengths or value chain are described. Supporting figures make them more compelling.

Regarding the above A to C, if the corporation recognizes that efforts have been unsatisfactory or that something is needed in value chain and/or intellectual assets, such a recognition of the corporation should be made explicit. (Clear analysis and description on this point lead to the description of the future value creation.)

D Actual performance, such as corporate profits

Actual performance, such as corporate profits, extracted from financial data is explained, paying attention to segments especially relevant to the value chain mentioned in C. If the corporation recognizes that there are some misarrangements in the past management and that actual performance including profits is unsatisfactory can be, explanation should be made on the recognition. Countermeasures described in the next part (3).

(3) From Present to Future

E "Intellectual assets and value creation method rooted in the corporation"

Reflecting the content of C, what is expected as future source of corporate profit is explained here.

If the corporation recognizes that past efforts do not make considerable achievements, based on the description of A through C, value creation method appropriate for the corporation is described. Specific measures to correct the method are also explained.

F "Future management policy based on identification of risks"

Identification of uncertain factors (both positive and negative) for future profits, and how to manage and deal with them (method and system of risk management) are shown. And then the future value chain which will create future profit in accordance with E, and intellectual assets used for this purpose are described, even in the case those assets are the same as the present ones.

G "Investment to maintain and enhance intellectual assets"

How to maintain and enhance intellectual assets that remain effective, how to make up for scarce or unusable intellectual assets that are to be used in the future corporate management, and what kind of investment will be conducted for these purposes are described, in accordance with F.

It is preferable to show target value on intellectual assets indicators, target control method, and the content and size of specific measures planned.

H “Future profits and cash flow”

Expected or future target profits and cash flow are shown, in accordance with A through G. Considering the interest of stakeholders, it would be better to give explanation on the time horizon, such as short-term, mid-term, or long-term.

Regarding the information on the future performance, the possibility that the presumed situations might change due to changes in the business environment should be shown as prerequisite, as it is warned in “Issues regarding the future” section of financial reports.[1]

3. Supporting indicators stated in the main body

Indicators that support the story above are stated in the main body. These indicators need to have credibility through internal control. Considering conducting substantial and effective internal management, approximately 5 to 10 indicators are adequate for a story. However, it is possible to use more indicators. It is also possible to support a story with various figures, even if those are not considered to be important indicators internally. Items that should be kept secret or kept as internal management indicators can be unseen even if they are important to support the story. In such a case, giving abstract explanation, without showing indicators, is enough for ensuring persuasiveness.

Annex 1 shows typical example of intellectual assets indicators. Each corporation can select important ones among them, or use its original ones. In order to ensure credibility to support the story, it is preferable to show historical change in a given indicator and the average value of other corporations in the same industry, in addition to the ways of calculation or sources of quotation.

4. Description of attachment

If a corporation still wants to show some items not stated in the main body, it can show them voluntarily in an attachment, referring to the typical example of intellectual assets indicators (Annex 1). If some indicators need to be kept secret are out of eyes, or cost much for calculation though they can be shown, it is enough to describe only the reason for exclusion as reference information.

The attachment can serve not only as corporate PR but also as a reference tool for other corporations in the same industry, while enhancing comparability. Therefore, if voluntary disclosure increases, it could reduce explanation cost of a story.

Evaluation of the actual figure of each indicator depends on a story. Therefore, those who disclose information and who assess it should deeply bear in mind that “competition for marks”, concerning the level (high or low) of the figure, is meaningless.

Efforts to “show excellent” for indicators remotely relevant to the story on value creation could be a proof corporate that management by selection and concentration does not work well. Assessors should understand this point and refrain from ranking simply by comparing the figure of indicators disclosed.

5. General reminders

- Importance of ensuring credibility

[1] Financial reports “must state that items regarding the future are judged as of the date which those reports are submitted”.

It is necessary to clarify the way to create value and profits unique to a corporation (value chain), which is the basis for future profits, and put emphasis on enhancing credibility of the existence, sustainability, and development of the value chain. Explanation should be brief and easy to understand (targeting roughly in several pages).

Regarding internal control and audit, explanation on their methods enhances credibility of the information disclosed. (Beautiful story without supporting data cannot be appreciated.)

Each corporation has its own story on value creation. It is impossible to decide which story is excellent and which is not. There is no absolute measuring standard. A good way to be appreciated is to enhance credibility of its story and make it resonated with assessors.

- Sincerity

Stakeholders have a lot of interest in a story on value creation and profits and the credibility of the story. A story lacking credibility could lose confidence and downgrade (probably underestimate) even if the story itself is an ideal one. Therefore, it is important for a corporation to show its actual performance and ideas for the future with sincerity.

- Relationship with other reports

Corporations that have already conducted various information disclosures can enhance the credibility of "intellectual assets based management report" by making it related with other reports so that it shows basic guidelines for the whole management. This clarifies the relationship between disclosed reports and leads to enhance their credibility as well.

If more detail explanation is needed for the points on which a corporation emphasizes, other reports such as environment report and intellectual property report can be of help. Details are stated in these reports, with reference for them and their positioning are clearly stated in a story described in the IA based management report.

- Continuous disclosure

Comparing historical changes of the content disclosed is significant for supporting a story. Continuous disclosure enables to enhance its credibility (it doesn't have to be based on a fiscal year).

- Relationship with hostile M&A

Intellectual assets based management eyes many stakeholders as well as stockholders. Manifestation of management policy means the intention to create a corporation as a group of stakeholders who agree with the policy. In this sense, intellectual assets based management could be a greater countermeasure against hostile M&A than technical defensive measures. Also, appropriate appreciation for the whole management would reduce acquisition risk caused by underestimation in the market.

6. Example of descriptions (virtual sample)

Please see Annex 2.

Chapter 4 Reminders for analysts/stakeholders

Regarding the content of disclosure on intellectual assets based management, it is necessary for those who receive the information and assess it should handle it in a way quite different from the conventional one. The following is an example of clues for such assessment.

1. General

- Understanding of the idea

"Intellectual assets based management report" explains how the corporation recognizes its own intellectual assets, how it uses them for differentiation and value creation, and to what extent future sustainable profits brought by its value creation is reliable. The report pays special attention to stakeholders whom the corporation put much on.

Therefore, it is necessary to put emphasis on mid-term corporate value and the possibility of sustainable profits, not on near-term items directly linked to profits.

- Difficulty of simple comparison

Each corporation has its own intellectual assets. Manners of utilization of them, a value chain that creates value and the story also differ from those of other corporations. (This difference enables to ensure excess profits through differentiation.) Consequently, it is not possible to measure the absolute value of a corporation using a single indicator or formula, nor determine a relative ranking of corporate value among all corporations through the disclosure of "intellectual assets based management report", which explains uniqueness of a corporation.

In other words, although some of the disclosed indicators have a limited comparability, as a whole, nothing is easily compared by anyone, for example, with simple figures.

Intellectual assets based management report enables those who can analyze the disclosed information intellectually to make comparison from a certain point of view, which calls for higher capability of assessors than ever before.

- Diversity of assessment

Since each assessor has his/her own point of view, it is no wonder that different assessment results on a corporation can exist. If a corporation and an assessor have much in common with a sense of value, the assessor will appreciate the corporation. If not, the assessor whose sense of value is very different from that of the corporation will not think highly of it.

- Assessment points

Main points of general assessment are as follows.

- Is the story on value creation consistent with general management policy and management philosophy? Is the content persuasive even in relation to other disclosed information and reports?
- Are the unique intellectual assets and their combination (value chain) stated clearly?
- To what extent do supporting indicators and explanations give credibility to the story on value creation?
- Do the indicators have substantive meanings through internal control?

- Assessment capability and the content disclosed

It is desirable for assessors to exchange information like a “play catch” with the corporation by indicating ambiguous points and any improvement to be made. This would promote “awareness” of the corporation, which will lead to the improvement of management and the appropriateness of disclosed information, and also the improvement in the quality of analysis by assessors.

Appropriate assessment and response from assessors (including exchanges mentioned above) will make the content of disclosure more sophisticated and more informative.

2. Main body

(1) General

Basic principle of the whole story on value creation lies in basic management philosophy, whose credibility is judged here. This is the central part of assessment.

Credibility is judged from the consistency with 1) everyday remarks of top manager, 2) the corporate policy and ideas shown in various media, 3) points in the following (2) and after. Whether policy and ideas of the corporation are implemented is also a source of judgment.

Outline of business characteristics should be examined by comparing with information from objective data, and be used for a criterion for understanding the explanation of (2) and after.

(2) From Past Present

A “Management policy/visions in the past”

This is the recognition of value creation method in the past from management side. In many cases, it can be confirmed by data already disclosed. The consistency with the philosophy mentioned in (1) is important. If continual disclosure is conducted, the consistency with the past statement is confirmed. If something changed, the background and the reason for the change are checked as well as the explanation of the content.

B “Past investment performance”

The content (including figures) can be checked by disclosure. Comparing this part with intellectual and tangible assets currently accumulated in the corporation enables to assess the efficiency of investment as well.

C “Assets, etc. accumulated in a corporation”

Contents of value chain or strength, intellectual assets that are a source of them, and relationship of them with the investment (B) are checked. If necessary, the status of other corporations in the same industry is referred to. The status of internal control is also confirmed.

D “Actual performance, such as profits”

This part is examined by financial data, focusing on the relationship between a value chain which was especially emphasized in the explanation mentioned above and actual profits. If past efforts or performance are recognized unsatisfactory and the reason is stated, it should be examined carefully.

(3) From Present to Future

E "Value creation rooted in the corporation"

The consistency with the explanation on a value chain mentioned in (2), and the sustainability are examined. If amendments are made based on the lessons from the past failure, their appropriateness is to be judged.

F "Future management policy based on the identification of uncertainty"

Following points are to be checked: 1) Is the whole identification of future uncertainty appropriate? 2) Is the appropriate risk-weighting made in consideration of the idea of value creation of the corporation? 3) Is internal risk management well-organized? Are measures adopted against the emerging risks? In accordance with these recognitions, management policy is examined together with the amendments needed in (E).

G "Investment to maintain and enforce intellectual assets"

Following points are to be checked: 1) Can the investment be a preventive/toward looking measure in accordance with the identified uncertainty? 2) Do the content and utilization of intellectual assets that are newly created or amended follow the management policy? 3) Are there any numerical supports for sustainable intellectual assets which do not need new investment?

H "Future profits and cash flow"

Persuasiveness, especially in accordance with the explanations of E through G, is examined. As this part deals with the future performance, principles including safe harbor rule in the disclosure of uncertainty are also to be paid attention. If assurance or audit on disclosed information is conducted, it should be confirmed who conducted and how. (In case of listed American companies, check with the data subject to audit by SEC.)

3. Supporting indicators for main body

Credibility of main body is judged from the following points: 1) Are indicators that explain well the story used? 2) What is the basis for calculation and quotation? 3) Does the basis give satisfactory explanation? 4) What is the relationship with the relevant indicators disclosed by other corporations in the same industry (in main body or in attachment)? Regarding these important indicators, if indicators for internal control are kept secret and only abstract explanation is given, persuasiveness of the explanation is examined. (If something is lacking, it is possible to point it out.)

Each indicator can have a different meaning in relation to the story on value creation of the corporations. Therefore, only numerical comparison with other corporations could lose the point: what kind of capability the corporation has for the future value and profits creation.

4. Indicators attached

Even if figures are the same, their evaluation differs in relation to a story. For example, a R&D driven corporation that writes a story emphasizing the registration of their own technology will show the number of international patents registered during the current fiscal year. On the other hand, some corporations trying to maintain technological lead by keeping their technology secret, using the form of trade secrets or black box, may state the number of international patents only in the attachment, and the significance of the figure will be small. Therefore, it is meaningless to judge whether an indicator is “excellent” apart from each corporation’s story on value creation.

Disregarding this fact, converting disclosed indicators into numerical terms simply and analyzing attached common indicators as deducting marks, like finding out a straight-A corporation, can impede the corporation’s efforts to focus on their own strength by selection and concentration. Assessors should refrain from such activity. If they don’t, their own ability should be questioned.

Attached indicator is used to check the consistency between the story of another corporation and the indicator which the corporation stated important in the story. No comparison should be made with other indicators.

When used for such purpose, the accuracy of the information is checked in accordance with the status of internal control, relationship with other disclosed information, etc.

Indicators which do not appear in a story and little importance is placed on by the corporation might be useful for assessors. They may pay attention to an item in a common indicator in the attachment and judge that the corporation can make better use of intellectual assets shown in the indicator, or that the corporation does not fully utilize its management resources. Such assessment can lead to play catch between assessors and a corporation, which can give “awareness” to the corporation.

Chapter 5 Simplified method

Regarding future value creation, degree of difficulty in writing a story supported by indicators varies greatly among corporations. A corporation which has not built sufficient internal control system or which has no experience in preparing reports on factors other than financial information would have difficulties in finding a clue to the preparation of intellectual assets based management report.

In such a case, the first step of preliminary work in creating the story on value creation is “SWOT analysis”, that is a method to analyze the strengths and weaknesses identified in the business process from the past to present, and the areas of future business opportunities with high degree of profit earning expectation and associated threats.

Since these items are mutually related to each other, it is useful to make a matrix in which all items can be viewed simultaniously, such as the one presented below. Putting them together and adding supporting indicators makes a basis for intellectual assets based management report.

Strength	**Weakness**
Opportunities that are highly likely to produce future profits	**Threats which are highly likely to adversely affect future profits**

Annex 3 shows an example of analysis based on this method.

Chapter 6 Future Prospects

This guideline state specific ways for disclosure on intellectual assets based management. However, the most important thing does not lie in disclosure itself. Rather, it is to reconfirm strengths and characteristics of a corporation, through the process of preparing for disclosure, and to review and reform management so that they are fully utilized.

In other words, disclosure is a clue for leading to a virtuous cycle concerning intellectual assets based management. If it works well, promotion of managerial efficiency, enhancement of competitive strength, sustainable growth, and development of the whole economy are expected.

It is expected that disclosure of intellectual assets based management is conducted based on this guideline and that intellectual assets based management is implemented in many corporations and that this guideline wold be a basis for international discussion on disclosure of corporate management information in the future.

Additionally, this guideline itself will be further developed as required, considering international trend on disclosure of non-financial information, actual disclosed content on intellectual assets based management in venture companies and small to medium-sized companies as well as in big companies, and reactions from stakeholders who assess disclosed content.

Annex 1

Example of typical intellectual assets indicators (list)

- Intellectual assets indicators are stated in the main body so that they support the story describing overall picture of management. Indicators not included in the main body can be stated voluntarily in the attachment.
- Followings are typical intellectual assets indicators. It is possible to select some of them which a company considers important for it. Other original indicators are also possible to use.
- The meaning of actual figures of each indicator (high or low) varies depending on the relationship of it with a story. It is meaningless to make simple comparison of indicators with other corporations which have different stories. Whether the indicator provides sufficient explanation should be assessed in accordance with the corporation's story.

(1) Management stance/ Leadership

Degree of sharing and penetration of management stance and target

- (Indicator 1-1) Degree of internal penetration of management principles
- (Indicator 1-2) External transmission of information by top manager (external PR activities)
- (Indicator 1-3) Development of future leaders (average age of subsidiary presidents)

(2) Selection and concentration

Status of selection and concentration in products and services (2-1 to 2-3), technologies (2-4), customers and markets (2-5), etc. Characteristics of selection and concentration depend on the type of business. Therefore, it is desirable to make explanation on classification of business (including basic structure of business model and sales structure per B-to-B, B-to-C) as a prerequisite.

- (Indicator 2-1) Competitiveness of major business (sales, profit, profit rate)
  (Indicator 2-1-1) Proportion of major business to the entire sales (sales)
  (Indicator 2-1-2) Proportion of major business to the operating profit
  (Indicator 2-1-3) Operating profit margin of major business
- (Indicator 2-2) Weighted average of the numbers of companies providing the same products/services
- (Indicator 2-3) Review performance of unprofitable department
- (Indicator 2-4) Degree of R&D concentration
- (Indicator 2-5) Differentiation of market
- (Indicator 2-6) Employee assessment

(3) External negotiation power/ relationships

Degree of negotiation power and connections over and with external parties--clients, customers (3-1 to 3-5), suppliers (3-6), funding sources (3-7)—such as upstream and downstream parties

- (Indicator 3-1) Weighted average of market share of main products/services in the main business
- (Indicator 3-2) Degree of customer satisfaction
- (Indicator 3-3) Changes in customer unit price
- (Indicator 3-4) New customer sales ratio (in B to B business) or growth rate of new customers or members (in B to C business), compared to those in the previous year
- (Indicator 3-5) Price elasticity value of product sales as compared to changes in the cost of goods purchased (price pass-through capability)
- (Indicator 3-6) Price elasticity value of the goods purchased as compared to changes in material market conditions (negotiation power)
- (Indicator 3-7) Financing capacity

(4) Knowledge creation/ innovation/ speed

Capacity and efficiency of new value creation, speed of business management

- (Indicator 4-1) R&D expenditure (or ability development costs) vs. sales
- (Indicator 4-2) Outsourced R&D cost ratio
- (Indicator 4-3) Number of intellectual property owned economically meaningful term
- (Indicator 4-4) Employees' average age and increase/decrease from the previous year
- (Indicator 4-5) New products rate

(5) Teamwork/ organizational knowledge

Organizational power (collective strength) and solidarity as a unity of individual capacities

- (Indicator 5-1) In-house improvement proposal for quality control system, number of proposals and improvements achieved
- (Indicator 5-2) Number of lateral projects
- (Indicator 5-3) Degree of employees' satisfaction
- (Indicator 5-4) Incentive system (including yearly contract system)
- (Indicator 5-5) Job leaving ratio

(6) Risk management/ governance

Identification, assessment and response, management, public announcement and governance of risks

- (Indicator 6-1) Compliance system
- (Indicator 6-2) Number of public announcements regarding risk information and speed of public announcement of problems
- (Indicator 6-3) Diversification of risks
- (Indicator 6-4) Risk of being an acquisition target
- (Indicator 6-5) Compensation claims in pending lawsuits
- (Indicator 6-6) Risk of information leakage (number of trade secrets and ratio of core employees who deals with them)

(7) Coexistence in society

Status of contribution to the community and society, etc

- (Indicator 7-1) Amount of environment-related investment
- (Indicator 7-2) Number of SRI funds which adopted the corporation
- (Indicator 7-3) Corporate image survey and ranking results

1. Management stance/ leadership

- Degree of sharing and penetration of management stance and target

- (Indicator 1-1) Degree of internal penetration of management principles

[Implication]

Even if top management has clear management principles, the integrity of the whole business activities differs depending on the degree of its internal penetration. This difference can affect business performance of a corporation. If internal recognitions differ on principles, targets, or strategies, cross-sectoral business operations may be hindered and performance of the whole organization may be impaired.

In other words, when management philosophy and targets are understood by and shared with many employees, it is highly possible that management utilizing intellectual assets and strengths penetrates through out a company, and that on-site performance is carried out in line with top manager's intention.

Therefore, an indicator that shows how far employees understand management philosophy, etc. can have a certain meaning.

There are various methods to have management philosophy penetrated. For example, when top manager makes efforts to send messages by himself/herself and, as a result, degree of penetration is rising, it is possible to show additionally figures reflecting such efforts (e.g. frequency of internal transmission of information). (In such a case, degree of penetration can ever rise by future efforts.) If degree of penetration is high but frequency of transmission is small, it is possible to interpret that the influence of one transmission, i.e. leadership is strong.

* However, in a case that only a few managers fully control the strategic part and employees only follow instructions, employees may be purposefully kept ignorance of management principles, targets, and strategies. In such a corporation, low degree of internal penetration goes with management policy.

[How to calculate]

A corporation utilizes the results of surveys on how far management philosophy and targets, etc. are recognized by employees. These surveys are conducted by the corporation itself (survey method and subjects should be clarified) or by external institutions (sources should be clarified).
(Annual frequency of internal transmission of information may be added as supplement.)

- (Indicator 1-2) Frequency of external transmission of information by top manager (external PR activities)

[Implication]

Management philosophy, targets, and strategies of a corporation are important for stakeholders to judge whether they can basically support its management method. If management philosophy, etc. are clearly shown to and shared with many stakeholders, management base is reinforced. For example, if the corporation is threatened by hostile M&A, many stakeholders will approve current top managers. Having such a common base can make a difference in efficiency in daily business activities, in recruiting new employees, and in marketing activities.

It is important for top managers to transmit externally such philosophy, targets, and strategies in their own words. It is the act of showing their commitment to the realization of them, which entails responsibility. Top managers' transmitting information with the understanding of its importance appeals their enthusiasm on sharing sense of value with stakeholders. Also, their attitude to take risks personally when failed to fulfill the commitment is one of the proofs of leadership.

If their enthusiasm and the actual degree of penetration are compared, as 1-1, it is possible to judge whether top managers' efforts bear fruits. However, compared with the survey on the degree of internal penetration, the survey on the degree of external penetration into stakeholders is not always easier. Regarding this matter, some degree of penetration can be estimated with the frequency and degree of clarity of transmission. Even if frequency is small, an indicator which shows that many people recognize messages would be a proof of leadership. Such an indicator is desirable to be shown, if possible.

[How to calculate]

Number of times and hours spent by top management (CEO) for external PR activities during the previous year are stated following the classifications below.

i) To investors
ii) To clients
iii) To customers
iv) To others

- (Indicator 1-3) Development of future leaders (average age of subsidiary presidents)

[Implication]

Ability for leadership does not basically depend on age nor the number of years of employment. However, it is unlikely that an employee with no experience can lead organization members.

From this point of view, it may be a way to select competent leaders continually that a corporation evaluates relatively young employees through experiences as supervisors of certain organizations (without having a boss).

To embody the above mentioned, a parent company, for example, can make president’s post of subsidiaries as a setting for training young leader candidates, not as an award for seniors who has acquired certain amount of experiences. In such a case, the average age of subsidiary presidents is rather young, which may produce leaders who have both on-site sense and management sense. In short, “the average age of subsidiary presidents” can be an effective indicator to show the efforts to develop new leaders.

However, top management may not grasp the situation if a corporation has too many subsidiaries. In such a case, it is possible to restrict only to main subsidiaries.

Development of next leader candidates using president’s post of subsidiaries is surely an example of cultivating leadership capability. Even if there is no subsidiary or even if the average age of subsidiary presidents is high, corporations can take other measures to develop excellent managers and leaders.

[How to calculate (example)]

Average age of presidents of consolidated subsidiaries (If other method is adopted, explain it.)

2. Selection and concentration

- Status of selection and concentration of products and services, technologies, customers and markets, etc. Characteristics of selection and concentration depend on the type of business. Therefore, it is desirable to make explanation on classification of business (including basic structure of business model and sales structure per B-to-B, B-to-C) as a prerequisite.

- (Indicator 2-1) Competitiveness of major business (sales, profits, profit rate)

[Implication]

Major business is what corporations consider as their “major” business, which varies from one corporation to another.

* For example, for complex corporations or general corporations undertaking multiple projects, major business may be sectors that make more than 20% of the whole sales.

Major business is considered to be business the corporation selects (and concentrates). If a corporation expands into so many fields, both the proportion of major business to the entire sales (2-1-1) and the proportion of major business to the operating profit (2-1-2) should be small.

On the other hand, if a corporation expanding into many fields has a single technology and know-how that underlie its activities, (and if that is explained), the degree of selection and concentration are not always interpreted as small.

If the degree of concentration for major business compared in profits is smaller or tends to decline than that compared in sales, it is effective to take countermeasures such as making efforts to raise profit rate of major business, shifting management resources to the current non-major business to upgrade to major business.

* However, this gap can be temporal for corporations whose strategy is to concentrate their business based on sales and then undergo a restructuring to raise profit rate as well. In such a case, giving explanation on the situation and on targets is effective to avoid misunderstandings.

On the contrary, if the degree of concentration for major business compared in sales is smaller or tends to decline than that compared in profits, review of non-major business can raise profit rate of the whole corporation.

Profit rate of major business is expected to be higher, maybe with some minor fluctuations, than that of the whole business including non-major business in the med-term. Even if this rate is not higher, it is desirable that targets are set to make it rise in the future. Level and changes of profit rate in major business can be important clues to estimate the future profitability of the corporation as well as prospects for future change.

(Indicator 2-1-1) Proportion of major business to the entire sales (sales)
[How to calculate]: Sales of major business ÷ total sales
(Indicator 2-1-2) Proportion of major business to the operating profit
[How to calculate]: Operating profit of major business ÷ total operating profit
(Indicator 2-1-3) Operating profit margin of major business
[How to calculate]: Operating profit of major business ÷ sales of major business

- (Indicator 2-2) Weighted average of the numbers of companies providing the same products/services

[Implication]

If many corporations in the same industry compete for their main products or services, it is highly possible that a corporation may be caught up in intense price competition and may not ensure sufficient profits. For example, in relationship between providers and sellers of final products, if sellers take control over product providers, like a case of mass retailer, following situation is likely to happen. If low quality products appear in the market of products of the same type, they may become the price leader through efforts of their providers to maintain sales regardless of prices, which impede other providers of better products to make profits. The case of mass retailer is a kind of exception. However, providing similar products with other competing companies of the same industry can cause severe price competition, which is likely to make it difficult to realize excess profits.

Consequently, if a product which many competing companies provide the similar type plays a great role in major business of a corporation, it has to say that the possibility to enlarge feasible profit margin is generally rather small, even if the corporation gets competitiveness through technological development. The corporation has alternatives, such as withdrawal from producing products which many competing companies in the same industry produce, or concentration to those with few competing companies in the same industry.

At the same time, other aspects such as how this indicator changes, whether the change is the result of the corporation's choice, and whether the change was brought about by external factors can also serve as one of the criteria for the prospect of future profit margin. If a company itself brings about the change (especially if it conducts management to reduce the figure of this indicator), it could be considered to have intentions to change the situation to raise profit margin by its own choice.

* However, a corporation can ensure sufficient excess profit through brands and technical superiority even if it has many competing companies in the same industry. In such a case, explanation on sustainability of the source of excess profit would enhance credibility of prospect of future profits.

[How to calculate]

The number of other corporations in the same industry is calculated by weighted average of all products in major business (e.g. 10 products: A to J) against the total sales.
(Number of other corporations in the same industry providing product A) × (sales for product A ÷ total sales of major business) + (number of other corporations in the same industry providing product B) × (sales for product B ÷ total sales of major business) + ・・・+ (number of other corporations in the same industry providing product J) × (sales for product J ÷ total sales of major business)

- (Indicator 2-3) Review performance of unprofitable department

[Implication]

One of the most difficult decisions for a corporation in selecting and concentrating is how to deal with unprofitable department. Each business department has many staff and various relationships with trading partners. Therefore, making a plan to give up some business or specific products/services is possible, however, carrying it out is not so easy. If the plan is smoothly carried out, it can make a huge contribution to the improvement of profit rate of the whole corporation in that the costs required for unprofitable business are cut down and that management resources for the department can be turned to fields with higher profit margin.

It should be kept in mind that too early withdrawal from a department whose profit rate decreased by temporal stagnation of the whole industries could result in losing a big business opportunity after economic recovery. It's not as if withdrawal always a good idea for corporations. If there is some internal criteria for withdrawal, it is effective to show its actual performance together with explanations on the criteria (amount of sales, profitability, added value, the number of years, etc.).

[How to calculate]

The number of business departments closed or sold off in the past 5 years. The number and size of major products/services discontinued development, sales, or provision. Total profit and loss with them.

- (Indicator 2-4) Degree of R&D concentration

[Implication]

The significance of R&D investment differs greatly whether or not it has a clear target supported by management strategies. Status of concentration of R&D costs for core (technology) field and its relating fields is a clue to infer strategic characteristics of R&D of a corporation. Degree of concentration is measured by focusing on R&D costs, the number of resulting patent applications, and the number of patents obtained. Regarding units of concentration, international patent classification (IPC) is effective if seen from relationship with patents, while R&D costs is effective if seen from degree of concentration on major products or major business.

If R&D and the resulting patents are fully concentrated on a specific field and no investment is conducted on strategically relevant fields, no breakthrough through technical fusion in the company is likely to be expected. Therefore, it could be effective for a corporation to show that it has certain ranges of R&D. The ranges include possible field of strategic relevance as well as major fields on which the corporation focuses. Reference indicator is, for example, "ratio of field of patent application out of [number of fields] strategically relevant fields".

R&D includes depreciation cost of capital investment for research and development, personnel cost, and other costs. Definition of R&D cost is the same as that used in calculating experimental and research expenses in the tax incentive system to promote research and development.

This indicator is meaningless for corporations unrelated to R&D or patent.

[How to calculate]
(Example)

i) (Degree of patent concentration) Out of the subclass of IPC classification(four-digit), the number of patent applications in the top ten classifications of the corporation's applications ÷ total number of applications of the corporation (annual)
It is possible to use the number of registered patents instead of the number of patent applications.

ii) (Degree of R&D concentration by field) Out of four-digit IPC classification, R&D investment in the top ten classifications of the corporation's R&D investment (annual) ÷ total R&D investment of the corporation (annual)

iii) (Degree of R&D concentration in major business) R&D investment in major business (annual) ÷ total R&D investment (annual)

iv) (Degree of R&D concentration by product) R&D investment on major ten products (annual) ÷ total R&D investment (annual)

In case of showing portfolio as well:
(Status of diversification of applications) For example, it is possible to calculate like this: the number of applied classifications where the corporation applied out of strategically relevant fields ÷ the number of . the strategically relevant four-digit IPC classification.

- (Indicator 2-5) Differentiation of market

[Implication]

Specialization for users market that has specific characteristics means selection and concentration, making a decision of giving up other users. For example, a corporation that selected providing environment-oriented products/services excludes low-price oriented consumers if its products/services are rather expensive compared to similar products/services of other corporations. Regarding excluded users, they may have a lot of positive impact on corporation, as it can cut down costs of marketing, etc. in return for getting no returns, if the selection of the corporation is successful.

If a corporation doesn't take any decision to differentiate concerning market, explanation may be given to the reason and the fact that it conducts differentiation from another point of view.

[How to calculate]

Sales of products/services targeted for specific users and markets (annual) ÷ total sales (annual)
(It is desirable to add brief explanation on targeted market.)

- (Indicator2-6) Employee assessment

[Implication]

If a corporation has clear recognition on businesses with high and low substitution possibility, staff placement and personnel policy based on the recognition are possible.

The way to evaluate personnel and his/her achievement differs from one corporation to another and what specific measures to take according to the evaluation also differs. Some corporations prepare career path for only specific personnel as core employees, some give stock options to specific personnel, recognizing that it gives a great influence on the corporation's performance, and some utilize external personnel for business with high substitution possibility.

Whether such distinction is made or not, and the degree of distinction suggest the corporation's attitude toward selection and concentration in human resources allocation.

* However, using external personnel is not always good, for example. It is necessary to confirm, in accordance with other indicators, if such distinction yields actual results.

[How to calculate]
(Example)
i) The number of employees given stock option ÷ total employees
ii) The number of permanent employees ÷ total employees
iii) The number of core employees ÷ total employees

3. External negotiation power/ relationships

- Degree of negotiation power and connections over and with external parties [clients, customers (3-1 to 3-5), suppliers (3-6), funding sources (3-7)] such as upstream and downstream parties

- (Indicator 3-1) Weighted average of market share of main products/services in the main business

[Implication]

Some corporations occupy a high share of the world or domestic market, based on their own technologies and know-how for specific products. Having products/services with a large market share means that the corporation can have a great ability to control its products' prices because it has such a strong customer base for the products/services. The ability to control products' prices enables the realization of excess profits. If competitiveness origination such a high share is sustainable, the corporation may continue to earn excess profits. In order to see such potential as potential of the whole major business, share of products in major business weight-averaged by sales is useful.

Although market share shows potentiality of the ability to control prices, whether it relates actually to profits should be judged comparing to other indicators (e.g. 2-1-3).

In such a case, if the ability to earn excess profits is not fully used despite high market share, that is also a message to show corporate management conditions. It can be said that the corporation misses opportunities to earn excess profits, or that it passes along to consumers, or that it has a chance to realize excess profits through the change of future management policy.

[How to calculate]

Each market share of all the products in major business (e.g. three products, A to C) is weighted averaged by total sales ratio of major business.

(Example)
(Market share of product A) × (sales of A ÷ total sales of major business) + (market share of product B) × (sales of B ÷ total sales of major business) + (market share of product C) × (sales of C ÷ total sales of major business)

- (Indicator 3-2) Degree of customer satisfaction

[Implication]

Degree of customer satisfaction is the result of various factors such as the quality of products/services provided, their prices, image of the corporation, etc. High degree suggests that the corporation has a base to maintain stable business relationships in the future and bargaining ability rooted in it. If the degree is high but is declining, it is interpreted that the corporation is losing persuasive power on which future profits depend. In forecasting future changes of degree of customer satisfaction, clear statements on how much degree of customer satisfaction decreased and on how long it needed to recover when big accidents happened in the past can be a great criterion for assessment.

Some corporations may enhance the degree of customer satisfaction regardless of profits such as simple low-price strategy. Therefore, it is necessary to assess this indicator together with other indicators including financial data. Here, suppliers are not included in "customers", and corporations under partnership are excluded.

[How to calculate]
Any survey (survey method should clarified), results of researches or surveys by external resources (sources should be clarified) are used to explain status of degree of customer satisfaction.

- (Indicator 3-3) Changes in customer unit price

[Implication]

In case of continual dealings with the same customers/clients, if the degree of customer satisfaction is high, unit prices for the next purchase can increase. If this degree is low, they can decrease because customers are likely to purchase at cheaper prices. If customers/ clients change accordingly, it is not likely that unit prices for new customers/ clients are higher, so in this case, too, unit prices will decrease. Therefore, increase in purchase unit price (customer unit price) per a purchase suggests that persuasive power over continuous customers is increasing or that the corporation has found new customers/clients who place very high confidence on it.

However, if a corporation reduced the sales price due to external factors such as collapses in the price of raw materials or import prices, certain corrections should be made in addition to showing a simple indicator of changes in customer unit price.

[How to calculate]

i) Year-to-year of annual average of purchased value per client per purchase
ii) Year-to-year of sales value per sale (sales value ÷ the number of sales)

- (Indicator 3-4) New customer sales ratio in B to B business or growth rate of new customers or members to, in B to C business, compared to those in the previous year

[Implication]

From the viewpoint of expansion and development of business and profits, paying attention to the ability to attract new customers or its actual performance of grasping new customers may have significance. Especially when market environment changes greatly, it is important to get excess profits as an antecessor by finding new customers one after another or to expand the whole market. This indicator sheds light on this aspect.

If changes in market environment are predicted in the future, past performance shown in this indicator enhances predictability in terms of future profits. If market that had been changing continuously is not maturing, however, past performance does not always predict future success automatically. Changes of this ratio and changes in market environment should be examined together.

For industries where stability of customer base is especially important, this ratio is not always highly appreciated; it might be interpreted as a destabilizing factor for future profit base.

Additionally, in some cases, this indicator should be assessed together with 3-2 as assessment from total customers.

[How to calculate]

i) Sales for new corporate customers ÷ sales (in case of B-to-B)
ii) Number of new individual customers (annual) ÷ number of customers (previous year) (in case of B-to-C)
(If the number of new individual customers cannot be grasped, increase/decrease of number of customers from the previous year is calculated.)

- (Indicator 3-5) Price elasticity value of product sales as compared to changes in the cost of goods purchased (price pass-through capability)

[Implication]

This indicator shows, contrary to 3-6, how far a corporation can pass swelling costs that corporations confront on to customers. The higher elasticity value than one is, the stronger bargaining power and persuasive power will be.

Following four points are in common with 3-6: 1) Explanation on sales price is persuasive. 2) Changes in the past elasticity value make future profits more predictable. 3) Indicator 3-5 and 3-6 should be assessed together. 4) The content can be highly confidential. If costs are not passed on sufficiently even though the situation is favorable, it is possible that the corporation has some strategies expecting future return or that it only misses opportunities for profits.

[How to calculate]
Rate of change in shipment unit price of major products (e.g. major 10 products)(year-to-year) ÷ rate of change in prime cost (year-to-year)

- (Indicator 3-6) Price elasticity value of the goods purchased in response to changes in material market conditions (negotiation power)

[Implication]

Regarding relationships with suppliers, how changes in suppliers' costs (e.g. raw materials costs) are reflected in purchasing price is considered to show negotiation power in relation to suppliers. For example, in case of no or small increase in purchasing prices in spite of the increase in supplier's costs, negotiation power of the corporation is strong. On the other hand, in case of no or small decrease in purchasing prices in spite of the decrease in supplier's costs, negotiation power is weak. However, there are various types of costs. If market trend is visible, like that of specific raw materials, it is easy to understand. Without such objective indicators, it is difficult to calculate.

Showing strong negotiation power is not always sufficient. If the power seems weaker in view of the corporation's size, it can be said that the corporation currently gives advantages to clients and expects return from them in tight supply situation in the future.

If there are downward/upward rigidities in prices pecuriar to the industry-specific prices, statement on that point enables more precise understanding. Changes in past elasticity value serve criteria in estimating future profits.

However, it is necessary to keep in mind that these figures, though effective for internal control, are highly possible to be strictly-confidential trade secrets. Also, they should be assessed together with 3-5. For example, if elasticity value in relation to customers (3-5) is higher, profits can be increased, in inflationary situation.

[How to calculate]

Rate of change in purchasing price from main clients (suppliers) (e.g. top ten corporations) (year-to-year) ÷ rate of change in prime cost in the ten corporations (year-to year)
(Note) It is also possible to focus on specific raw materials and use rate of change in market trend price of raw materials as denominator.

- (Indicator 3-7) Financing capacity

[Implication]

Deviation between contracted interest rate on borrowing from financial institutions (indirect financial market) and issuance interest rate on bond issue (direct financial market) shows directly the level of confidence the corporation receives in financial market and its negotiation power there. In addition, its historical change shows the change of evaluation of the corporation viewed from financial market, and can suggest capital cost that has much effect on future profits.

[How to calculate]

For example, debt with interest is classified to loan from financial institutions, corporate bond (including 0-coupon CB) and others, and "(annual weighted average of borrowed contracted interest rate or bond issue interest rate) — (annual average value of prime rate) is calculated for each of them. (Rounding off to the nearest tenth.)

<Answers>

	Average maturity (year)	Rate of annual weighted average interest	Deviation from prime rate of 1. (annual average)
Loan			
Straight bond			
Others			
Total			

4. Knowledge creation/ innovation/ speed

- Capacity and efficiency of new value creation, speed of business management

- (Indicator 4-1) R&D expenditures (or ability development expenditures) vs. sales

[Implication]

Innovation is one way to enable differentiation from other corporations. Especially in manufacturing business, enthusiasm for R&D suggests the possibility of differentiation. In corporations based on human resources, however, enthusiasm is expressed in ability development of personnel, not in R&D.

This indicator shows how much a corporation focuses its energy on prior investment or knowledge creation for innovation. It has great significance in assessing the possibility of future competitiveness and profits. On the other hand, these expenditures are costs and have to be checked, using with other indicators and explanation, whether they generate concrete achievements, and whether they relate to clear management strategy.

These expenditures may vary wildly in relation to corporate profits. If they are judged together with other financial figures, it is possible to estimate willingness for prior investment, strategic nature, and relationship with management policy.

In this regard, this indicator is more meaningful if explanation is given to corporate target such as time lag between prior investments and achievements.

[How to calculate]

Annual R&D expenditure ÷ annual sales and their year-to-year
Range of R&D expenditure should be the same as the one disclosed in financial reports, and be stated specifically. If cost calculation in name of "R&D expenditure" is difficult, for service businesses, etc., the value is calculated as: ability development expenditure ÷ annual sales. (Source for calculation should be showed for ability development expenditure.)

- (Indicator 4-2) Outsourced R&D cost ratio

[Implication]

R&D in cooperation with external sources (universities, research institutes, relevant corporations, R&D based venture corporation, etc.) which conduct many different researches can be a source for innovation which has a great influence on the corporation's profits. In addition, since this type of R&D is not a fully independent one, it suggests that researches are conducted not only for immediate product development but also for establishing a basis for medium-term competitiveness including basic research. Some of these research are substituted by other methods (purchase, M&A, etc.), however, some are not in view of cost performance and the necessity for employees to learn know-how by participating in a research from the very beginning.

While this type of research can create the positive effect of technical fusion through collaboration, it might cause the risk of leaking important internal information. Additionally, even if some positive results were achieved, they do not necessarily pay for the corporation, depending on the conditions stated in the contract. Therefore, it is necessary to judge this point together with the status of management of trade secret and contract.

[How to calculate]

Outsourced R&D costs of the previous year ÷ total R&D expenditure of the year
(Information on the outline of main outsourced cases of each corporation should be included.)

- (Indicator 4-3) Number of intellectual property owned and economically meaningful term

[Implication]

If the result of knowledge creation is registered in a form of patent, etc., this enables differentiation from other corporations through exclusive implementation. If it is an especially important one, it attracts attention from various quarters, and it will be cited in increasing number of documents. The number of citation means not only the number but also the quality. This suggests the true innovation ability, and its technical superiority can be a source for future profits. However, in some cases, intellectual property is not registered intentionally for strategic reasons and is black boxed as know-how or handled as trade secret. Therefore, it is desirable that strategy on the whole technology including the number of such cases is also explained.

Showing the number of products/services that appeared first in the market makes it possible to show the efficiency of patents owned, trade secrets and designs. The status of disclosure of intellectual property report can also be used in the explanation. Regarding trade secrets, an explanation on the effectiveness of management method is desirable since too many trade secrets can not be adequately managed internally.

Regarding patents and know-how that relate especially to products and have a direct effect on future profits, economically meaningful term of the intellectual property should be showed, because various situations can happen such as 1) obsolescence of patents may occur within the remaining term of rights, 2) know-how impedes other corporations to follow even if the term of rights is expired, 3) the remaining term of the patent is the very term in which they can enjoy profits exclusively.

[How to calculate]

i) Number of “patent”, “utility model right”, “industrial design right”, “trademark right”, “registration of plants (Seeds and Seedlings Law) owned. Number of trade secrets managed in the corporation.
ii) Number of annual citation in documents on the results of R&D of the previous year (per right)
iii) Expiration date or economically meaningful term of especially important patent, etc.

- (Indicator 4-4) Employees’ average age and increase/decrease from the previous year

[Implication]

Metabolism of employees, etc. can trigger innovation or change in corporate system. This indicator can have important implications, depending on business characteristics. For example, if a corporation develops a strategy targeting the young market, relatively young average age of employees may be significant. If the average age is one year older compared to that of the previous year, this means no young force has been introduced.

Some corporations require youth, fresh ideas, speed, etc. Some require capability and experience for each employee. In any cases, whether average age of employees and metabolic rate are matched with characteristics of each business is to be assessed. However, the significance of this indicator varies widely between, for example, tasks in which technology with years of experience is needed and tasks which anyone can do. Therefore, in some cases, explanation on this indicator focusing on specific tasks is significant.

[How to calculate]

Employees’ average age and increase/decrease from the previous year

- (Indicator 4-5) New products rate

[Implication]

If a corporation continues providing the same products/services, increase in profits cannot be expected other than through cost reduction or new market exploration, because there is little possibility of increasing the price. If the provided content is the same, offered price generally tends to decline and profits are likely to decrease.

Although developing and providing new products/services have risks, this may hasten replacement of goods, especially durable ones. Introduction of new model or additional function may maintain or increase unit price. These may maintain customers in accordance with the change in tastes of the market and may attract new customers, which expands opportunities to increase future profits.

Responding appropriately to these changes in the market and utilizing them to develop new products/services infers managerial speed of the corporation.

The important thing is that the willingness of introducing new products/ services is recognized specifically by customers, that is to say, it leads to sales. This indicator suggests willingness to develop new products/services and to realize them.

Additionally, if the introduction of new products/services relates to increase in profits, this means that the corporation is competent in responding appropriately to changes in the market and that it may increase profits in such a way in the future. Therefore, it is appropriate to judge this indicator together with the status of profits expressed in financial report.

[How to calculate]

Sales of products/services within three years from the start of provision ÷ total sales
(“New products” may include remodeling and minor changes. This judgment depends on each corporation.)

5. Teamwork/ organizational knowledge

- Organizational power (collective strength) and solidarity as a unity of individual capacities.

- (Indicator 5-1) In house improvement proposal for quality control system, number of proposals and improvements achieved

[Implication]

Internal improvement proposal is widely spread in Japan, and its on-site implementation often enhances business efficiency. These proposals are highly effective since they are based on reality, and can lead directly to improvement in corporate profits.

This is related to the ability of "adjustment to resolve issues([※1])", quality of employees, and their motivations to contribute to improve the corporate activities. This ability derives from the mentality of Japanese workers of finding joy in their works instead of considering them drudgery. Also, in some cases, the implementation of these proposals makes individual employees feel that they are contributing to the corporation with satisfaction.

The important thing may not be only the number of proposals. If such proposals are actually implemented, the high quality of their contents, corporate culture that they willingly utilize proposals from employees, and employees' satisfaction are also suggested.

(*1) "Adjustment to resolve issues": Operations or business processes to manufacture products of high quality through adjustment and combination between factories and sites for R&D. This term, first used by Prof. Takahiro Fujimoto, Tokyo University, is said to express one of Japan's strengths.

[How to calculate]

i) Number of internal improvement proposals
ii) Number of internal improvement proposals adopted/implemented

- (Indicator 5-2) Number of lateral projects

[Implication]

The bigger an organization becomes, the more sectionalism increases, which makes it difficult to cooperate laterally and yields trend in which workers tend to think first of the section rather than the whole organization. This can cause duplicated investment between sectors, increase in impediments in collecting and analyzing information, delay in taking action to new changes by the penetration of fixed concept, and business ideas with narrow scopes, and can hamper effectiveness of the whole management and possibility of profits.

One way to salvage such situation is to carry out lateral organizational activities or projects, formal or informal, which go beyond individual sector framework. Through this, effective and pioneering activities with an eye to the whole organization can increase.

In those activities, heads of lateral teams are more likely to be chosen on their own merit regardless of their age than those of vertically-structured organizations. Additionally, knowledge, idea, and know-how limited in individuals or sectors are fused in the whole organization, which can lead to innovative knowledge creation.

However, these efforts should be appreciated only if they are made by the corporation with clear intention and recognition.

[How to calculate]

Number of ongoing or accomplished lateral projects
(Any size will do. Projects may range from formal ones by official personnel arrangement to informal ones conducted voluntarily. Project teams newly set up with personnel from different sectors due to personnel changes may also be included, depending on the judgement of each corporation. Brief explanation is desirable.)

- (Indicator 5-3) Degree of employees' satisfaction

[Implication]

In Japan, basic level of each employee is said to be high. Especially when individuals feel rewarding and exercise their abilities, performance and creation activities in the whole organization can be enhanced and bring profits. Confidence in organization can develop certain loyalty and activities with more emphasis on teamwork. Additionally, employees who have loyalty and few complaints are less likely to engage in outflow of technology against the corporation's intention.

On the other hand, however high their abilities are, organizational performance may not be improved if individuals are quite dissatisfied with the organization.

* However, even if the degree of employees' satisfaction is high, the effects above mentioned may not be expected in such cases that only economic measures for satisfaction including wages and benefits are focused. This indicator should be examined referring to the status of labor distribution rate and personnel cost.

[How to calculate]

Existing rankings and surveys on the degree of employees' satisfaction conducted by business journals can be used. (Sources should be indicated.) Results of internal surveys or questionnaires conducted voluntarily by each corporation are also possible. (In this case, survey/questionnaire method should be clarified.)

- (Indicator 5-4) Incentive system (including yearly contract system)

[Implication]

Reasonable remuneration system may be effective to bring out employees' abilities. If many of employees want such a performance-based system, high proportion of performance-based fee in wages is a strong incentive to exercise their abilities in the corporation. On the other hand, if many of them think that equal treatment brings solidarity, such wage system is not an incentive.

Therefore, what kind of incentive system a corporation formulates in relation to characteristics of employees is considered to play an important part in business performance. The effectiveness of the system can be confirmed by a relationship between the change of this indicator and that of corporate profits, or between this indicator and 5-3.

However, remuneration system is not the only source of incentive for employees. For example, promotion can substitute for remuneration. It is effective for a corporation which lays special emphasis on that aspect to explain such efforts.

[How to calculate]

i) Performance-based fee ÷ total wages (annual), or
ii) Number of employees who receive annual compensation ÷ total employees (end of the fiscal year)

- (Indicator 5-5) Job-leaving ratio

[Implication]

Job-leaving (emigration) ratio of employees shows the relationship between employees and the organization.

For corporations which utilize teamwork and organizational power for value creation, or which consider it important for skilled workers to accumulate know-how through experiences, higher stability of the work force and lower emigration ratio predict future profits. In fact, some corporations maintain motivation of employees and prevent the outflow of know-how through keeping emigration ratio low and eventually get through difficulties and maintain growth in the medium term.

On the other hand, for some corporations, higher emigration ratio suggests higher possibility of pursuit of new profits through drastic change in management policy. One of such cases can be seen in information industry where fresh and flexible ideas are especially needed and the creation of new value and energy through metabolism is focused on in order to meet rapidly changing needs.

Therefore, this indicator, in particular, should not be assessed by seeing the level of figures but in the context of the story of each corporation, taking into consideration of how human resource is utilized to create value.

However, this indicator has important significance in either case above mentioned. This proves that human factors play a great role in management.

[How to calculate]

Number of employees leaving the company ÷ total employees
It is possible to calculate respectively according to nature of tasks or employment status (permanent employees/contract employees).

6. Risk management/governance

- Identification, assessment and response, management, public announcement and governance of risks

- (Indicator 6-1) Compliance system

[Implication]

It is necessary for top management and each employee to recognize risks the corporation might take and the necessity of compliance and to share these recognitions. This factor is necessary for the risk management of the whole organization. Precise risk management enhances the predictability for future profits, since the system is more likely to continue in the future.

In order to realize adequate compliance, it is effective to allocate appropriate number of persons in charge of organizational compliance according to the size of organization (※1), and to provide each employee education on how to handle emerged risks and compliance. Such allocation and education should be incorporated in the system. Recruiting outside personnel or a lawyer for person in charge of compliance can enhance the quality of compliance.

In such a case, explanations on how operation and supervision are divided and on the status of internal control make the story more persuasive.

(*1) It should be noted that the number of persons in charge does not always respond to the degree of enhancement of compliance system.

[How to calculate]

i) Total hours of education on risk management and compliance (annual) ÷ total employees
ii) Number of outside directors in corporations which introduce outside director system ÷ number of directors
iii) Presence or absence of external personnel recruited to compliance department, and the number of external personnel
iv) Number of persons in charge of compliance in the previous year (Note) ÷ total employees

(Note) "Persons in charge of compliance" includes employees who hold additional tasks in operating departments as well as employees who engage in compliance exclusively. Number of each type should be specified.

- (Indicator 6-2) Number of public announcements regarding risk information and speed of public announcement of problems

[Implication]

In risk management, taking prompt response and taking measures for recurrence prevention in case of risk elicitation are as important as prior restraint of risk elicitation. For assessors, vague information on risks is the biggest risk. Timely announcement of information on its own risks is interpreted that the corporation recognizes its risks accurately and it will not hold back risk information. Additionally, prompt public announcement in case of trouble is considered that it has high-quality internal system on recognition, assessment, and response on risks and that it is very capable to respond to risks. These everyday efforts are more likely to be basis for the appreciation that the corporation has smaller risks of sudden deterioration in the future performance.

Regarding public announcement of risk information, number of announcement should be assessed in relation to the size and range of business.

[How to calculate]

i) Number of public announcements on risk information (annual total)
ii) Amount of time between the outbreak of trouble and public announcement (annual average)
(Means of announcement are press conference, internet website, press release, description in annual security report, etc.)

- (Indicator 6-3) Diversification of risks

[Implication]

A corporation faces any kind of risk factor, external or internal, such as objects and processes of R&D, trading partners (upstream/downstream), geographical conditions, etc. While selection and concentration enhance the degree of dependence on specific business or business partners, corporations with multiple pillars of R&Ds, various clients (upstream/downstream), or various operating bases are considered to have effective resistance to risks. In this sense, such corporations are more likely to have smaller risks of sudden eterioration in the future performance. These portfolios are sometimes a part of business continuity planning (BCP). (Theoretically, each corporation has its own portfolio suitable for it, since each one faces its own risks.)

Portfolio in the field on which the corporation focuses is especially important. For example, portfolio on R&D is important for corporations which emphasize superiority in high technology fields through R&D; portfolio on suppliers of parts (e.g. status of geografical diffusion of their factories) is important for those which keep their competitive superiority tanks to specific parts at the core. If sales of the few products represent the total business of a corporation, well-balanced weight of major products are important.

[How to calculate]

(Example)

i) Number of fields to which the corporation pay R&D costs in important fields (IPC classification, 4-digit) which may relate to its core products ÷ total number of important fields
ii) Number of main suppliers of raw materials or parts
iii) Number (and diffusion) of main factories of suppliers of specific core parts
iv) Herfindahl-Hirschman Index which shows the degree of decentration on the share of major products (Sk) in the total sales of the corporation = $\sum_{k=1}^{n}(sk)^2$

- (Indicator 6-4) Risk of being an acquisition target

[Implication]

A corporation with better business performance can have a risk of being acquired, depending on its market value. Especially when its share price does not reflect the potential of the corporation, it is a “bargain” for buyers and is likely to be targeted for acquisition. In such a case, it is important to get its share price upward to fair price by informing the market properly its management method utilizing its own intellectual assets.

On the other hand, buyers are keen to know the value of reserved cash, in addition to the information whether value of shares is much cheaper than book value of net assets. Because cash-rich corporation is an “easy target”, since they can further reduce the risks which might happen associated with acquisition. Therefore, this indicator can be more useful to examine the risk of being acquired than simple PBR.

Even if the risk of acquisition is high, it would be effective to explain qualitatively the facts, if any, that appropriate defensive measures against acquisition are taken, or that the corporation has a clear plan to invest the existing large amount of net cash to for medium-term profits, etc.

[How to calculate]

(Present corporate value in the stockmarket − net cash) ÷ book value of net assets (end of the fiscal year)
And/Or the status of defensive measures against acquisition adopted by the corporation

- (Indicator 6-5) Compensation claims in pending lawsuits

[Implication]

With the increasing trend of large-scale lawsuits related to business, the amount of claimed compensation in a pending lawsuit shows the maximum amount of unexpected future damage in the lawsuit. Showing the maximum downside risk can significantly reduce the total risks for stakeholders.

Some people think that it is vital for a corporation to keep such information secret, however, compensation claim can be known to the public because of the principle of open justice. If compensation claim is unreasonably excessive, however, this indicator may cause misunderstanding. In such a case, a supplement may be given or this indicator may be calculated excluding the specific case with excessive claim..

In addition, corporate attitude that it files lawsuits against other corporations to defend and enhance its corporate value may reinforce its story on value creation.

[How to calculate]

i) Total value of compensation claims in pending lawsuits (end of year)
ii) Number of pending lawsuits or prosecutions (as plaintiff) (annual)

- (Indicator 6-6) Risk of information leakage (number of trade secrets and ratio of core employees who deal with them)

[Implication]

One way to differentiate products/services from those of other corporations is to utilize patent or trade secrets in a way others cannot imitate. If this method is effective in the future, the corporation's profits are more likely to continue to grow.

Regarding trade secrets, especially, controlling them properly is important. In order to do that, it is necessary to clarify information subject to control and persons who deal with it, to prevent them from moving out from the company and to define the obligation through a contract, etc. to prevent important information to be leaked. The number of persons and information subject to control should be limited to really important ones, in order to make this method effective.

This indicator suggests the effectiveness of controlling trade secrets of the corporation.

Additionally, showing qualitatively that control is conducted in accordance with the "guidelines for trade secret management" compiled by METI is also considered to be efforts on management of trade secrets.

[How to calculate]

i) Presence or absence of internal regulation on trade secret, and its content
ii) Number of employees who are recognized and controlled by the corporation to deal with trade secrets ÷ number of total employees (end of year)
iii) Number of information controlled as trade secrets (end of year)

7. Coexistence in society

- Status of contribution to the community and society, etc.

- (Indicator 7-1) Amount of environment-related investment

[Implication]

For the realization of sustainable economy and society, expectations for business activities compatible with environmental conservation and solution for global environmental problems tend to be rising. This indicator shows how much a corporation puts emphasis on such expectations and how it responds to them. Such corporate attitude can be a source for its sustainable development and profits through being recognized and appreciated by communities.

On the other hand, environment-related expenditures and investments fall in the category of cost reducing profics. Therefore, they will not last long unless some return is obtained. And some return would means that stakeholders sharing a sense of value with the corporation have appeared, which suggests the basis for future profits are being formulated.

In this context, it is desirable to explain not only the amount of expenditures/investments but also returns obtained from them. If so-called environmental accounting is introduced, the figures of loss and profits calculated in it can also be described.

Expenditures/Investments for ex-post elimination of burden on environment and those for new products/services which reduce the burden through technology, etc. can have different impacts on society. It is preferable to separate them and give an explanation independently on each, if possible.

[How to calculate]

Costs for preventing pollution, reducing carbon dioxide emission, decreasing waste, and developing new environment-conscious products (annual)

Note 1: Capital investment is calculated based on annual depreciation cost amount. Capital investment is stated so.
Note 2: Income relating to environment-related expenditure/investment is also stated, if possible, by corporations, such as those with environmental accounting.

- (Indicator 7-2) Number of adoption of Social Responsibility Investment (SRI) funds

[Implication]

In judging business activities from the aspect of coexistence in society, CSR is increasingly focused on. Many corporations have already prepared CSR report to show their activities, however, it is not easy for them to explain by themselves that such activities lead to their own sustainable profits.

Recently, financial institutions and institutional investors that invest with a relatively medium-term not a short-time view from SRI funds, noticing the importance of CSR. This may show that market is appreciating CSR activities which can be tied to medium-term profits of corporations. Therefore, this indicator is considered to reflect assessment of practitioners in the financial markets: whether they recognize the efforts for CSR activities of corporation, and if recognized, whether such efforts can be a source for future profit of the corporation.

This indicator can affect portfolio of future possible SRI funds, meaning that a corporation can benefit from the active disclosure of this indication.

Additionally, showing qualitatively its efforts for CSR in relation to the story on value creation as well as the number of SRI funds can also be beneficial.

[How to calculate]

Number of SRI funds which a corporation recognize by a voluntary survey as ones incorporating the corporation's stocks (at the end of year. Funds matured during the year may be included with the indication of it. It is desirable to show additionally the content of efforts for CSR.)

- (Indicator 7-3) Corporate image survey and ranking results

[Implication]

Corporate image held by its relating community and society shows the status of everyday business activities as a social citizen, goods and services the corporation provides, and how its nonprofit activities are evaluated by society.

Such corporate image cannot be created in a short period of time, and can sustain as brand image of the whole corporation, which can affect future profits.

On the other hand, each corporation has different ideas on who the most important stakeholders are in relation to future profits. For example, if human resource is especially important, it matters how much the corporation appeals to people who may work for it. If product image for customers is important, it may matter whether the corporation can establish trademarks as a well-known brand name. And in some cases, how the corporation as a whole is viewed from the society is the stake.

It takes time to create a positive corporate image. Although it usually sustains, it often degrades by sudden accidents or scandals and takes a long time to recover. Smaller degree of degradation and higher resilience shows that the appreciation for the corporation is deeply rooted, which influences certainty for future profits. Therefore, it would be very useful in judging future profits and risks if a corporation shows additionally the degree of degradation in corporate image and the amount of time to recover in the past.

[How to calculate]

(Example)

i) Existing corporate image surveys or ranking results (sources clarified)

ii) Ranking of corporations by people who seek for permanent jobs (sources clarified)

iii) Awards from national/local governments, NGOs, international institutions, etc. (annual)

iv) Number of trademarks established as famous brand (end of year and increased number from the previous year)

Note: As to i) and ii), the explanation on the degree of image degradation and its recovery in the past can be shown as reference.

Annex 2

Example of Intellectual Assets Based Management Report (Virtual Sample)

Principal parts of intellectual assets based management report (Example)
The story on value creation

* Intellectual assets indicators

Basic Management Philosophy

Since our foundation in [year], under the philosophy of "realizing comfortable fulfilling urban life" we have tried to establish our corporate image through dissemination of the philosophy widely to those concerned (*Frequency of IR) and penetrating the idea to employees as a code of action (*Degree of internal penetration of management principles)… We will continue our business to recognize today's trends or to go a step ahead of the times by promoting technological development based on the technology we had developed in [year] in order for the development of products that meet users' needs.

Characteristics of Business

We put focus on A as major business and offer products mainly to individual customers (B-to-B: B%, B-to-C: C%). Our major products are for consumers, such as D, E, F, and G. Our main trading partners are H, I, J, etc. as for K, and L, M, N, etc. as for O. Our products are distributed through P, Q, etc.

Recently, while sales of D, E, F, and G are growing at around R%, unit prices are declining in the deflationary trend, and competition with a major company, S, has been more intense.

For environmental conservation, establishment of regulation standard of T is expected in this field. We conducted environment-related investment of U yen in [year] (*Amount of environment-related investment). We have already been satisfying the predicted standard.

Past to Present

(1) (Management policy) … With progress of urbanization and heightening demand for living environment in the background, we expect an increasing demand for … which can be used even in a relatively small living space. We have conducted our business aiming at gaining a competitive advantage in the field of products for urban residents which are low-noise and easy to handle.

(2) (Investment performance) … We have invested intensively on development of insulation technology, weight-saving technology, and space-saving design (*Degree of R&D concentration)(A yen, from [year] to [year]) … We also conducted the joint project with university to develop materials for that purpose (the joint project with B University, …yen, in [year]) (*Outsourced R&D costs ratio). …

(3) (Intellectual assets, value chain) We acquired the basic patent of A in the field of B in [year]. We expanded our rights in the related areas (Relevant patent: C cases)(*Number of patents owned) through improvement and invention based on it. We also acquired design rights (Relevant design rights: D cases)(*Number of design rights owned) and have continued development of raw materials (E). In order to incorporate these activities in marketing, we established the "product team" as an inter-divisionary organization in [year] and have realized a new style of development and sales under a young leader that can meet market needs. This team has produced products such as F and G. We have succeeded in commercialization of H that other corporations cannot produce and have strengthened our lineup with various designs to meet our users' needs. As a result, our products account for I% (*Weighted average market share by of main products of the main business), … We have maintained the unit price even in the recent trend of deflation (*Changes in customer unit price), and have been trying to enhance our corporate image by increasing PR activities for consumers since [year](*Corporate image survey).

(4) (Performance) As a result, sales increased from A yen in [year] to B yen in [year], and current profits decreased from C yen in [year] to D yen in [year]. The decrease in current profits in last year was due to …

Present to Future

(1) **(Vision)** With the rise of a Korean competitor, the management environment has become severer. However, based on our past performance, we will continue to remain differentiated from other corporations by enhancing our high credibility to meet the needs of customers. Specifically, we will maintain the current unit price, and promote product development focusing on our main product A, based on basic patent, in order to ensure our share in the domestic market. We will also enhance corporate image and further strengthen profitable structure by launching PR activities of our design capacity towards customers, especially PR activities by the president to show our contribution to society, and by ensuring that employees understand and work according to these ideals. In addition, since appropriate compliance system is vital to maintain and improve corporate image, we will continue to enhance our compliance system (Person in charge of compliance: B persons)(*Compliance system).

(2) **(Investment plan)** Since [year], we have adopted and trained the total of A designers, and will increase the number to B and enhance the contents of the training (Training expenses: at present C yen, 5 years later D yen)(*R&D expenditure per employee). In order to enhance corporate image, our external PR activities will be focused on the points that our products improve the beauty of the environment and that we value human-friendly and eco-friendly aspects in deciding colors and materials of new products (Investment related to environment: E yen)(*Amount of environment-related investment). Development of new raw material following our main product F will be finished in two years (Amount of investment: G yen), and commercialization will be started.

(3) **(Sustainability)** Basic patent is valid for A years, and relevant patents are to be valid until [year] on average. Our products have gained a high evaluation from buyers, and the figures are on an upward trend year by year (*Corporate image, survey)(*Degree of customer satisfaction). In order to give higher incentive to the "product team", we will introduce the new system of B. Since we started to export our products to some big cities in China last year, expansion of the market is expected (Expected average growth rate C%). We expect D% growth in sales and current profit will be E in [year].

Note: Calculation method of each indicator

- Frequency of IR: Number of times and hours spent by the CEO for external PR activities in the previous year
  Previous year: A times, B hours; previous year before: C times, D hours
- Degree of internal penetration of management stance: General administration department carried out a blank questionnaire survey in [month, year].
  All staff was subject.
- Degree of R&D concentration: R&D investment in major business (annual) ÷ total R&D investment (annual)
  Previous year: A%; previous year before: B%
- Weighted average of market share of main products of main business: (share of product A) × (sales of A ÷ total sales of business B) + (share of product C)
  (sales of C ÷ total sales of B) + (share of product D) × (sales of D ÷ total sales of B)
  Previous year: E%; previous year before: F%
- Compliance system: Number of employees in charge of compliance ÷ total stuff
  Previous year: A%; previous year before: B%
  *Number of persons in charge of compliance:
  Previous year: employees who engage in compliance exclusively:
  C persons, employees who hold additional tasks: D persons;
  previous year before: employees who engage in compliance exclusively:
  E persons, employees who hold additional tasks: F persons
- R&D expenditure per employee: R&D cost in prior period ÷ number of researchers (Number of researchers: as of [date] Designers included)
  Previous year: A yen; previous year before: B yen
- Amount of environment-related investment
  i) Environment-related expenditure
  Previous year: A yen; previous year before: B yen
  ii) Change in environment-related expenditure
  1998: A yen, 1999: B yen, 2000: C yen, …
  iii) Capital investment in pollution control equipment: D yen (cost for depreciation under fixed percentage depreciation method was adopted in the first year; useful life F years)
- Corporate image survey
  Based on the result of questionnaire survey conducted by A in [month, year] to about 10,000 subscribers of the magazine issued by A.
- Degree of customer satisfaction
  A% of purchasers of our products replied "very satisfied" or "satisfied". (Based on the questionnaire in a product registration card we received in the prior period.)
  As for image of our products, B% replied "very reliable" or "reliable". (Based on the questionnaire survey through the internet conducted by C in (month, year).
  About D replies were received.)

Example of Intellectual Assets Based Management Report (Virtual Sample)

Annex: Intellectual Assets Indicators

Indicators in Annex 1 are described.
(Certain comparability is provided to assessors.)

- External transmission of information by top manager
  *Number of times and hours the CEO spent for external PR activities in the previous year
  i) To investors: A times, B hours
  ii) To clients: C times, D hours
  iii) To customers: E times, F hours
- Competitiveness of major business
  i) Proportion of major business (A) to the entire sales: B%
  * Sales of A ÷ total sales
  ii) Proportion of major business(A) to the operating profit: C%
  * Operating profit of A ÷ total operating profit
  iii) Operating profit margin of major business(A)
  * Operating profit of A ÷ sales of major business (A)
- Review performance of unprofitable department
  * We perform review of businesses with operation of profit margin of A% or fewer after B years of their start. We closed C department and withdrew development of product D. Total profit and loss with it is E yen.
- Degree of R&D concentration
  i) Degree of patent concentration: A%
  *Number of application in the top ten classifications of our application in the International Patent Classification (B cases) ÷ total number of our application (C cases)
  ii) Degree of R&D concentration in major business: D%
  *R&D investment in major business (annual) ÷ total R&D investment (annual)
- Price elasticity of procurement value vis a vis the change in material price
  *We recognize that we have high price bargaining power, however, this value is not calculated since it is difficult to obtain cost information of suppliers.
- R&D costs vs. sales
  i) Annual R&D costs ÷ annual total sales = A%
  *Annual R&D costs: cost for B is included
  ii) Change in R&D costs vs. sales
  1998: C%, 1999: D%, 2000: E%, …
- Degree of employees' satisfaction
  *Fth place in G listed companies on the Tokyo Stock Exchange First Section (Source: Survey conducted by H on [month, date, year]. Published in I journal.)
- Compliance system
  i) Number of outside directors ÷ total number of directors = A%

Annex 3

Example of SWOT Analysis Kikkoman Co.

<Strength>	<Weakness>
★ Brand power domestically and abroad ★ Fully-developed internal QA system • Maintain image of reliable, safe, high-quality products ★ High capability in brewing technology • Know-how and technology accumulated over a long time • Product development ability related to seasonings ★ Technological alliance with group companies • Japan Del Monte, Manns Wine, …	★ Mature industry (food products industry) • Patent rights expired, many technologies are public domain • Hard to obtain basic patents • Much of the know-how is not protected by patents
<Items that are highly likely to produce future profits>	**<Areas of likely risk of threats from rivals>**
★ Cooperative network with collaborating companies • Joint product development, use of distribution channels, … ★ Establishment of jointly owned company with a famous US nutritional supplement maker company • Joint research and product development on health foods • Manufacture and sale of nutritional supplements and health foods in the USA ★ Obtaining patents in new business areas • Bio-technology, organic foods, …	★ Patents obtained on know-how • Patents on know-how obtained by other companies ★ Imitation products (China, Asia) • Decline in brand image due to counterfeiting and similar products

Reference

Disclosure of Non-Financial Information in EU, England, and Germany

Revision of accounting directive in European Union (EU)

In June 2003 a revision of a EU directive on accounting[1] was made in response to the measures which made the application of International Accounting Standards (IAS) mandatory. In this directive, member countries were enjoined to require that companies above a certain size disclose comprehensive analyses of the balance between business processes, business results and current status in the annual reports for fiscal operating periods that start after January 1, 2005.

Description of annual report is stated in Article 46 of the revised directive above mentioned.

Main content of disclosure

- Non-financial information and indicator (KPI) are disclosed, including "information related to the environment and employees", in addition to the financial statements in the scope needed to understand the business processes, results and current status.
- Possible future growth of corporations is disclosed.

Disclosure standard for non-financial information in England

(1) Background

Upon receiving the revision of the EU accounting directive, in March 2005, the British government established a revision to the accounting statutes[2] that companies above a certain size be required to create and disclose "Operating and Financial Review" (OFR) documents. This obligation is entered into force for accounting periods that start after April 1, 2005.

---

[1] DIRECTIVE 2003/51/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 18 June 2003 amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC on the annual and consolidated accounts of certain types of companies, banks and other financial institutions and insurance undertakings
[2] http://www.dti.gov.uk/companiesbill/whitepaper.htm

The Operating and Financial Review describes the long-range value creation of a company from the view point of top manager. The OFR is somewhat more comprehensive because it also incorporates clarifications of the items related to corporate social responsibility (CSR). In addition, the companies are obligated to disclose the future performance with Key Performance Indicators (KPI).

ASB (Accounting Standards Board) made the "Reporting Standard"[3] based on the law.

(2) Principles of disclosure standard of OFR

1. Views of board of directors should be reflected.
2. It should be future-oriented, clarifying current and future performance, and trends and factors relating to development toward the fulfillment of business purpose in the long run.
3. It should be complementary with financial information, and supplementary for it.
4. It should be comprehensive (though everything is not covered) and understandable.
5. It should be well-balanced and neutral, dealing fairly with both advantages and disadvantages.
6. Historical comparison should be possible.

(3) Framework for disclosure (main factors)

1. Characteristics, targets, and strategies of business
2. Development of actual performance including future one
3. Resources influential for future prospect (reputation, brand, natural resources, R&D, intellectual capital, intellectual property, market position, etc.)
4. Risks and uncertainty (including risk management policy)
5. Relationships with wide range of stakeholders (customers, suppliers, employees, regulatory authorities, financial institutions, etc.)
6. Financial status
7. Important indicators on 1 to 6 (comparability is also improved): Definition, calculation method, objective, data source, and future targets are included. If some indicators are changed, the reason is explained. Information on environment, employees, society, community, suppliers, those who receive profit share, and members of organizations is also included.

(4) Implementation guidance

[3] http://www.frc.org.uk/asb/press/pub0793.html

The implementation guidance attached to the reporting standard includes the following 23 examples of KPIs: Return on Capital Employed (ROCE), economic profit, market share, customer unit price, number of subscribers, sales per square unit, sales ratio of new products, number of products purchased per customer, products on pipeline, cost per unit, alienation of customers, emissions to environment, carbon-dioxide emission, amount of waste, employees' morale, health and safety of employees, social risks in supply chain, number of times of violation of noise regulation, oil reserve, market risks described by Value at Risk, business continuity management, economic capital, and operating profit of cash flow.

Disclosure standard for management report in Germany

(1) Background

In Germany, disclosure of information on risks had been mandatory since the revision of the Commercial Law in 1998. Upon receiving the revision of the EU accounting directive in June 2003, Accounting Law was revised in December 2004. This revision emphasized that development, achievement, or status of business and financial status of a corporation should be explained together with financial and non-financial KPIs, and that annual report should include the statement on possible development in the future including risks and opportunities.

Additionally, the commentary on the revision of Accounting Law above mentioned stipulated the formation of accounting standard by German Accounting Standard Board, which announced German Accounting Standard 15 (GAS15) on February 25, 2005.

(2) Principles of disclosure standard of GAS15

1. Significant risks and opportunities that decide future management are provided.
2. Focusing on sustainable value creation, credibility (consistent with financial information and other statements), clarity and transparency (historical consistency), integrity (all information users require is provided), and information on management horizon by top manager are provided.
3. Main factors that affect changes in future value of a corporation are disclosed and explained.
4. Disclosure of off balance information is required. Disclosure of intangible assets is also recommended.
5. Non-quantitative information is disclosed for at least the next two fiscal years.

(3) Framework of disclosure (main factors)

1. Table of contents is provided at the beginning of the accounting report.
2. Contents are divided at least into the following sections:
   Business environment/ results of business/ financial status/ net worth/ report on risks/ report after the settlement date/ report on future expectations
3. It is desirable to quantify KPI used for internal control.