Position Paper on "SDGs and Intangibles"

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In 2015, the United Nations adopted the Sustainable Development Goals or SDGs. The volume of the business related to SDGs in 2030 is estimated to be 12 trillion US dollars. They are now widely shared goals internationally.

The most notable difference between the previous Millennium Development Goals (MDGs) and the SDGs is that the former goals were expected to be attained through donations from developed countries to developing countries alone, while the latter ones focus on collaboration (Goal 17), particularly between governments and businesses all over the world. Attainment of the SDGs has necessitated various initiatives such as the development of sustainable finance products which will enable new business models that focus on long-term value creation.

The SDGs cover a wide range of economic, social, environmental, human and governance issues represented by the 17 goals, many of which are inter-related. One of the features of the SDGs is that each company can realize one or more goals by utilizing its own particular way of carrying out economic activity or running business models to create value related to SDGs. The factors that generate and allow such a unique way or model in creating value are not just financial assets, but various types of intangibles, including human beings' skills and competences, innovation, technology, know-how, designing capacity for new businesses, reputation and long-term trust among companies or stakeholders. In this way, intangibles play a key role in attaining the SDGs.

Unlike assets recognized in the balance sheet (such as financial assets), intangibles can grow as a result of the accumulation of human activities for a certain period and be utilized in the business activities. More importantly, the combination of intangibles deployable in one company will be totally different from that in another. Therefore, it is not easily imitated, and even if some standardized technology solutions can be purchased, techniques, know-how or organizational designs and procedures to manage cannot be easily copied. Another characteristic of intangibles is that they may last longer than tangibles as long as they are well tailored to the business needs and features. There is also constant investment in them over time, for example R&D, people learning and development and market-led innovations.

The various intangibles can be categorized in human capital, organizational capital and relational capital that are critical for the organization's capability to create value. These three are aggregately called 'Intellectual Capital' in the traditional academia. Organizational capital includes corporate philosophy, history, technology, know-how, teamwork capability, organizational design and procedures, R&D capacity etc. This specific form of intangible capital is named 'intellectual capital' in the International Integrated Reporting Framework. Relational capital covers relationships with customers or clients, cooperation with the region where the company operates, trust with business partners and so on. This is encompassed in the IIRC's Framework as 'Social and Relationship capital.'

Needless to say, business activities require some financial and/or manufactured capitals, but intangibles can unlock those tangibles and create real value. Moreover, if a company lacks some expertise to handle its own intangibles, it may be quite difficult to create value from other capitals or capture it within the firm.

In general, intangibles can last longer than tangibles, but they cannot survive without proper maintenance activities. If a company leaves them in the situation where another company can easily utilize or imitate them, the core part of the company's value creation mechanism may be diluted or even dispersed.

Since attaining the SDGs involves activity to create new sources of value in many fields, intangibles and their combination which are the main source of creating values are key factors for promoting SDGs. Drawing on the innovative capacity of human endeavour will be vital in this respect.

In the specific scenario where a company contributes to addressing an SDG directly, it would need to use its own intangibles and a combination of resources from the viewpoint of long-term value creation.

According to an analysis done by Edmond de Rothschild AM, some of the issues picked up in the 169 targets under the 17 SDGs have clear links with intangibles. For example, the majority of the issues included in the targets related to 'good health and well-being,' 'quality education,' 'gender equality' and 'decent work and economic growth' has close and evident relationships with organizational and human capitals.

However, even if a specific connection is not apparent in a certain category amongst the 17 SDGs areas, intangibles can still play an essential role to attain the goals and targets of SDGs. For example, the target 'end hunger and ensure access by all people' in the category 'zero hunger' seems to show little connection with intangibles. Yet, imagine a company which collects spare foods from restaurants or a food processing company that gets information on food shortage in a certain country or region, matches those needs and seeds, transfers the food to where it is requested, and raises funds for doing so by utilizing micro-funding, virtual currency or an advertising model. In this case, a business network or business partnership is created, which falls under the category of relationship capital, to collect information about excesses of food, shortage of foods, as well as supporters for raising funds are needed for the success of the business. Some key persons, or human capital, who have passion, intention and vitality, are indispensable. Needless to say, knowledge and/or IT technology is needed for realizing the matching system and handling a large amount of data.

This case illustrates the necessity of understanding the connection between intangibles and attaining the SDGs. Therefore, more focus is needed to highlight the role of intangibles in realizing the vision of the global goals.

In spite of the importance of sustaining value creation by utilizing own intangibles company specific business or value creation models rooted in the combination of different interconnected resources (or capitals) has not been the traditional method of disclosing information about a company due mainly to inherent short termism in the system, resulting in a focus on quarterly reporting or annual financial results and its prospects in the immediate short-term.

Although the majority of the value of businesses today lies in intangibles, regulators and accountants have been slow to recognize its true importance, while businesses and investors have also not factored them into their decision-making in a meaningful way. Since 2007, the WICI (World Intellectual Capital/Assets Initiative) has been pointing out and advocating the relevance of intangibles for value creation and the associated necessity for their measurement and reporting, while the advent of integrated reporting confirmed this need for a change as to the consideration and representation of intangible capitals.

If the vital role intangibles play in the company's value creation process and their contribution to meeting the SDGs is not recognized, the company could become exposed to risks that harm its value creation potential.

The current situation where intangibles are overlooked is a reflection of the basic attitude of the financial system focusing only on the value created from a short-term perspective. In order to change this situation and promote the SDGs, we need to highlight the long-term value creation capability of a company, which is closely related to the outcomes generated and therefore the contribution of the company to achieving the SDGs. One of the most straightforward ways to do so is to adopt a model of corporate reporting on the company's long-term value creation, focusing on the utilization of its own intangibles, as well as the other resources used by the company to create value.

The corporate reporting model which most fits this purpose is integrated reporting, and the International Integrated Reporting Framework was released in December 2013. The Framework introduces six capitals as elements of company value creation, within which intangibles are included. It also focuses on value creation over the short, medium and long-term.

The WICI Global Network has contributed to the development of integrated reporting from the beginning. Moreover, in 2016 WICI has produced the WICI Intangibles Reporting Framework that can be utilized as a guide to the implementation of the International Integrated Reporting Framework focusing on intangibles. When integrated reporting by companies becomes widely adopted, as is already the case in contexts such as Japan, The Netherlands, South Africa and France, it will be easier to understand which companies have the capability or intention to contribute to the delivery of the SDGs and to what extent, through the leveraging on their own intangibles.

This emerging form of corporate reporting is also important for investors, because it enables them to predict which companies can succeed in SDGs-related businesses which are expected to be more than 12 trillion dollars per year globally. Moreover, for investors, sustainable growth is the most important issue for companies to survive and to respond to the principles of PRI. Thus, integrated reporting is essential also to advance investors' own interests, as well as their beneficiaries.

In this situation, it is appropriate that companies communicate with stakeholders through integrated reports about their own long-term value creation strategy based on a full range of resources, including intangibles. In turn, this will result in a company expressing its capabilities and intentions towards contributing to the SDGs. This approach should be supported by governments as the most efficient and effective way of achieving the 2030 agenda.

WICI and the IIRC will continue their efforts to encourage more companies to focus on long-term value creation in their communications with stakeholders, based on utilizing their own assessment of the resources used, including intangibles. This paper is a contribution to the public policy debate and we encourage its endorsement by all those with an interest in advancing long-term value creation and the achievement of the ambitious sustainable development agenda.

This paper has been developed by WICI (World Intellectual Capital/Assets Initiative) Global Network in association with the International Integrated Reporting Council (IIRC) for the purpose of articulating the importance of intangibles in helping to achieve the UN Sustainable Development Goals (SDGs).
We are pleased to submit the ideas in this paper for consideration by the B20 during Japan's Presidency of the G20 in 2019.

Further resources:

International Integrated Reporting Framework:
http://integratedreporting.org/wp-content/uploads/2013/12/13-12-08-THE-INTERNATIONAL-IR-FRAMEWORK-2-1.pdf

The Sustainable Development Goals, integrated thinking and the integrated report:
http://integratedreporting.org/wp-content/uploads/2017/09/SDGs-and-the-integrated-report_full17.pdf

WICI Intangibles Reporting Framework,:
http://www.wici-global.com/framework

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