

The communication of accounting information in summary annual reports

Michael Bradbury, Tom Scott and Pei-Chi (Kelly) Hsiao

The Problem:

- Annual Reports are too long and complicated
- BHPs 2017 annual report is 296 pages
- Not understandable by 'mum and dad' investors
- 36% of Australians are not financially literate (S&P Global Survey)
 - This was better than NZ



It's not just me saying that:

- *There have also been concerns that financial statements have become longer and more complex (ASB, 2000).*
- *In recent years, the financial reporting community has become concerned about the increasing size of financial reports and the danger of readers being so blinded by so much data that the main messages are lost (NZICA, 2011).*
- *Inadequate communication can also compound transaction complexity and is avoidable (survey of 58 analysts, CFA 2015).*
- *...we need to focus on the information needs of shareholders and provide a report that satisfies their needs, while we address the growing concerns about information overload in financial reporting. We think the summary annual statement is that report (CEO, major accounting firm, 1996).*

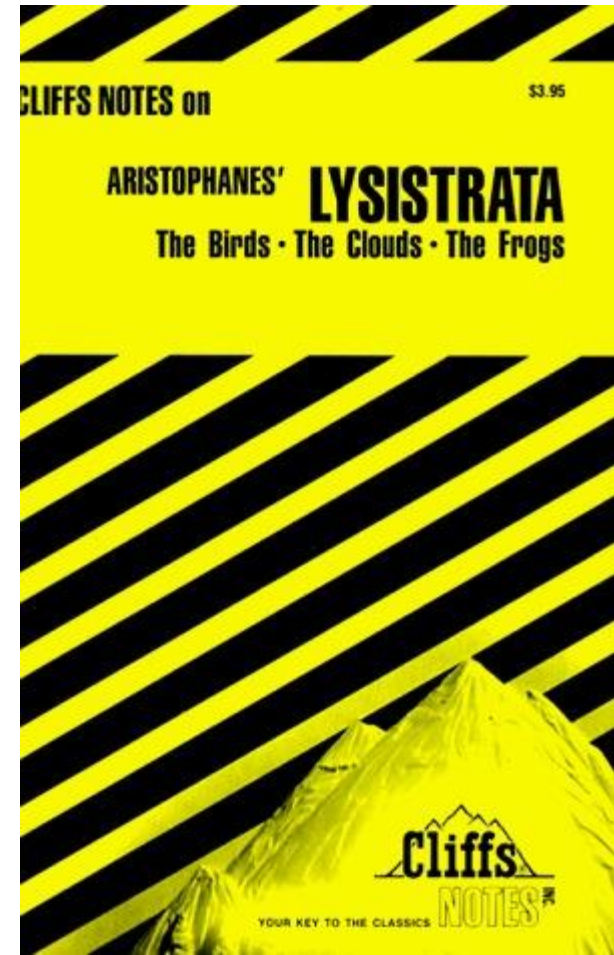


Solutions:

- Review and amend individual accounting standards
- Reduce disclosures – Reduced Disclosure Regime for SMEs
- Disclosure or Materiality Principles
- Summary Annual Reports

Are SARs the Cliffs Notes version?

- SARs aim to be easily understood reports on the most important issues
- Governed by AASB 1039 Concise Reports or FRS 43 Summary Financial Statements
- Not explicit on requirements or format – user specific
- Not a cut-down annual report





Research Questions

- Are SARs effective in their aim?
- Do they reduce information overload (length)?
- Do they improve understandability (readability)?
- What information do they contain?

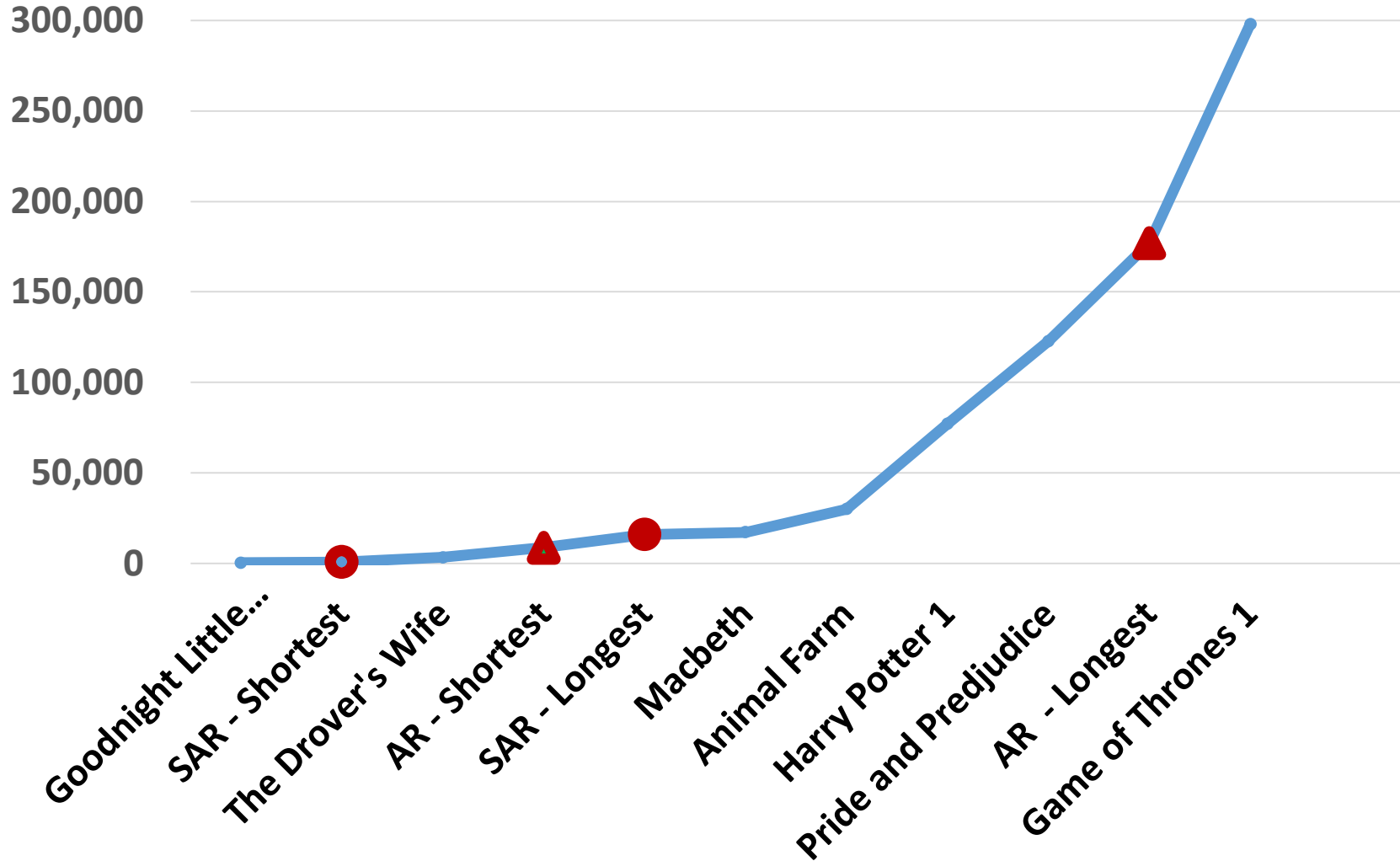


Prior Research and Sample

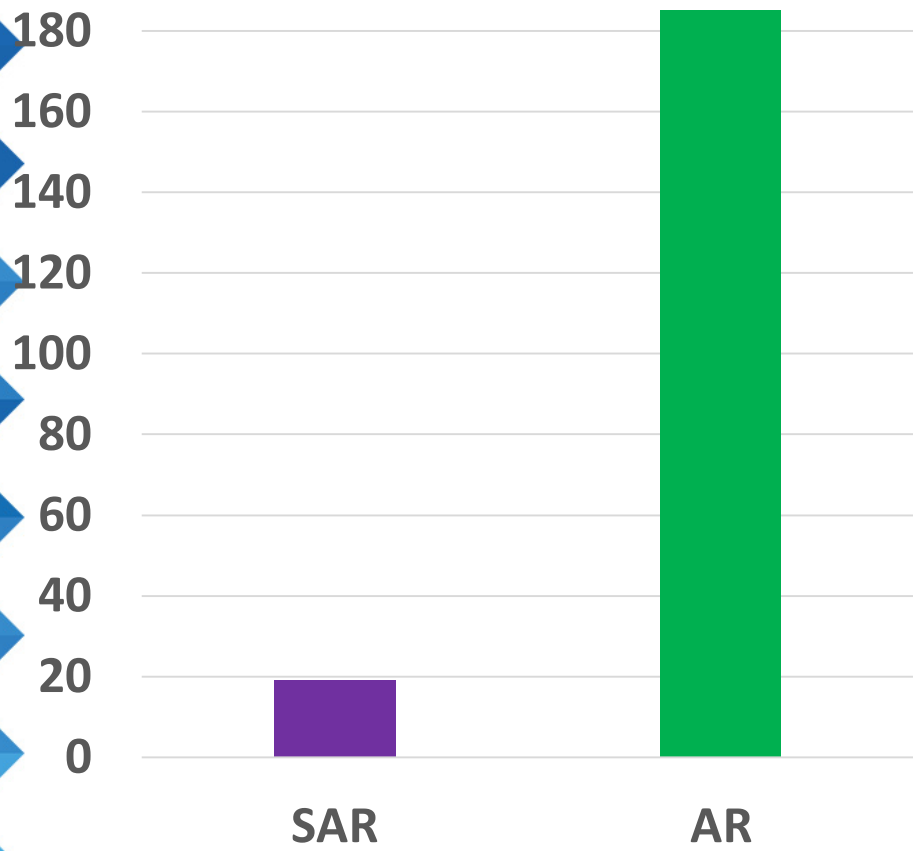
- Uncommon for companies as they are not required
- Makes research hard!
- Summary: typically a reduction in length, but no improvement in readability

- NZ local governments must produce a summary
- 66 NZ Councils in 2015
- Note: must include service performance

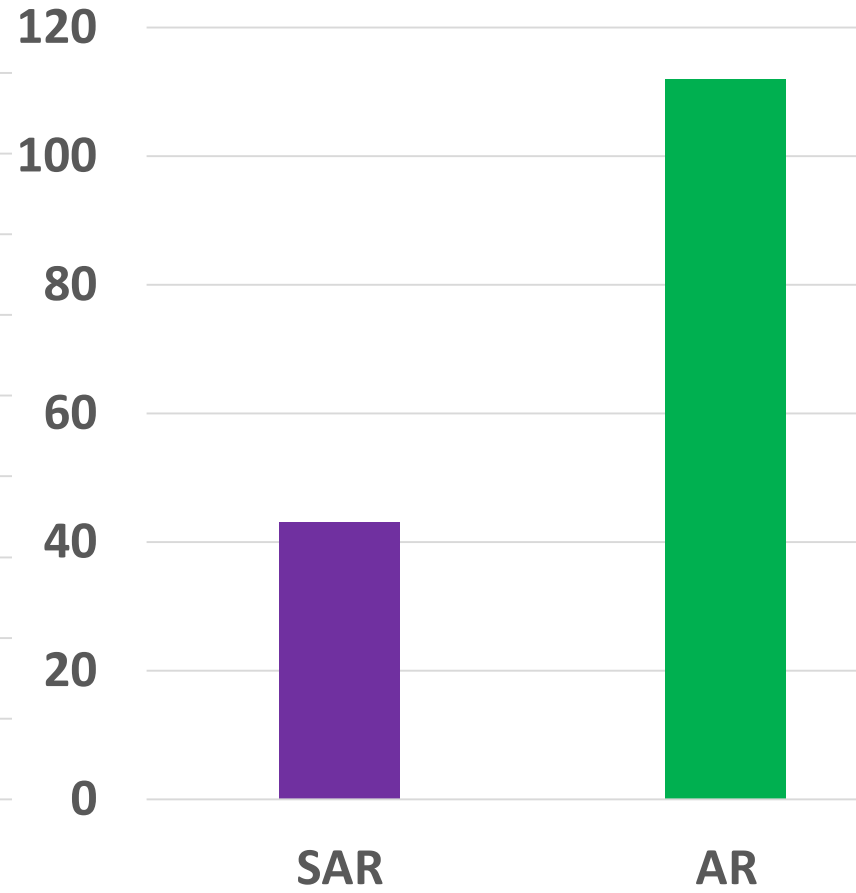
Comparative word count



Page Count



F/S Lines



Financial Statements Example

STATEMENT OF FINANCIAL POSITION

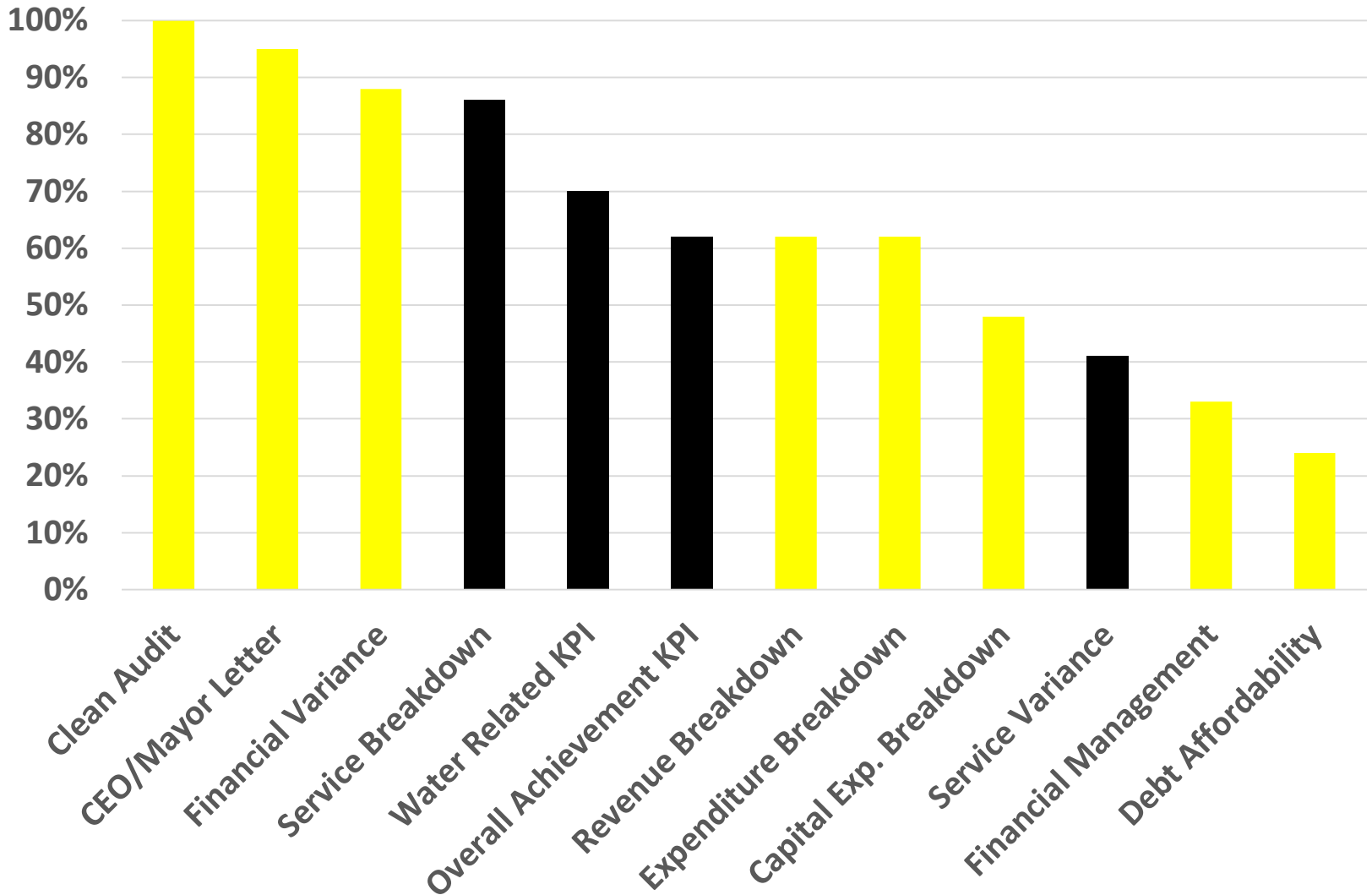
\$'000	\$'000			\$'000	\$'000	\$'000
16,879	17,421	Current assets		9,989	28,933	29,279
1,687,958	1,691,049	Non - current assets		1,791,067	1,825,077	1,830,721
1,704,837	1,708,470	Total assets		1,801,056	1,854,010	1,860,000
15,449	15,653	Current liabilities	(i)	24,894	28,985	29,018
59,116	59,116	Non - current liabilities	(i)	73,416	56,997	56,997
74,565	74,769	Total liabilities		98,310	85,982	86,015
1,630,272	1,633,701	Net assets (assets minus liabilities)		1,702,746	1,768,028	1,773,985
1,630,272	1,633,701	Equity		1,702,746	1,768,028	1,773,985
1,630,272	1,633,701	Total equity		1,702,746	1,768,028	1,773,985



Document Readability

- Both SARs and ARs have a reading grade level of a university graduate – there is no change
- Although Summaries may be an effective solution to the problem of overlong annual reports, they do not solve the problem of too complex or non-understandable annual reports
- There is replication across AR and SAR – for example discussion and analysis (Letter from Mayor)

Information content of SARs



Who are the Users of SARs?

- Shorter or more reduced SARs have less information
- What is the point of SARs? (who is the user)
- For NZ councils, aimed to be understood by lay readers
- What information would they want in it? (basis for summarisation)
- NZ survey evidence for SMEs suggests advisors and lenders use summaries for high level analysis and then go to details
- Is it individuals or groups (Grey Power or journalists) using the summary?
- Considering users is also important for reduced disclosure regimes and principles of disclosure

Comparison to Australian Councils

- Queensland Councils produce community reports
 - Typically less accounting information, no financial statements
 - Focus on financial sustainability in a way that is understandable to the community
 - 2% of AR length (relative to 10% in NZ)
 - No change in readability (university graduate)
- Victoria requires councils to supply performance information (KPIs and financial)
 - Accessible online and can compare to similar councils
 - Less ability to emphasis relevant measures or strategic directions (can explain variances)
 - Reflects rethink of reporting rather than replicating paper based reports across new technologies?

Comparison to ASX Companies

- O'Sullivan and Percy (2004) find 24% use of concise reports by largest ASX companies – but some are longer than the AR!
- Decrease in use since as:
- Preliminary reports, continuous disclosure, press releases, analyst briefings and investor packs
- Similar Annual Review or Highlights – but issues with being pro forma or non-GAAP?

How did we go at summarising?

- We have a paper for journal submission and did a summary for today
- Feedback on first draft – not good!
- Did not consider who the users would be
- 33 to 2 pages – 6% of the length
- No change in readability (university graduate)
- Removed all tables/figures



Summary of Policy Implications

- SARs are good at reducing length
- SARs are not good at improving readability
- If regulators want something in SARs, it may need to be mandated (applicable to principles of disclosure?)
- Preparers need to consider who the user is, and not just cut down the AR
- We suggest SARs for general accountability for non-financial experts, with the annual report available for those who need further information