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THE UNDERSTANDING AND USE OF INTERIM FINANCIAL REPORTS BY INDIVIDUAL SHAREHOLDERS OF SOUTH AFRICAN LISTED RETAIL COMPANIES FOR INVESTMENT DECISIONS

by

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ABSTRACT

Since 2007, several studies have been conducted by international and national role players to establish whether the recent efforts to improve financial reporting have been successful. The respondents to the surveys used as part of these studies have indicated that more concise and less complex financial reports would be more understandable to users of financial reports.

In view of the call for shorter and simpler financial reports, the fact that the understandability of financial reports appears to be a problem, as well as the fact that a limited amount of research on the understandability of interim financial reports has been done thus far, it was decided to investigate whether individual shareholders understand the context and content of interim financial reports which, *per se,* are supposed to be more concise and less complex financial reports presented by companies.

The study entailed using a postal questionnaire in a survey of a sample of individual shareholders of three large South African listed retail companies to determine whether individual shareholders understand the context and content of interim financial reports, and whether they use these reports, among other sources, to make investment decisions. The study is based loosely on the high profile studies of Lee and Tweedie in respect of individual shareholders performed in the late 1970s.

The primary research objective of the current study was to determine whether individual shareholders of South African listed retail companies understand the context and content of interim financial reports. It was found that understanding of these reports was generally limited. However, there is evidence that experience and training in the field of financial accounting improve shareholders' understanding of the content of interim financial reports.

Apart from questions on the demographics and investment objectives of individual shareholders, a number of other questions were also included in the questionnaire to address several secondary research objectives. The questions relating to the secondary research objectives were designed to gather information, *inter alia*, on how individual shareholders make investment decisions, sources of information used by individual shareholders when making investment decisions, additional information that should be included in interim financial reports, as well as the medium of communication through which individual shareholders would prefer to receive interim financial reports. The study has shown, amongst other things, that the majority of respondents to

this study initiated their own investment decisions, that articles in the financial press are the most popular source of information when making investment decisions, and that individual shareholders still prefer to receive interim reports by post.

OPSOMMING

Sedert 2007 is verskeie studies deur internasionale en nasionale rolspelers onderneem om vas te stel of die onlangse pogings om finansiële verslagdoening te verbeter wel suksesvol was. Die respondente in die opnames wat deel van hierdie studies gevorm het, het aangedui dat meer bondige en minder komplekse finansiële verslae vir gebruikers van finansiële verslae meer verstaanbaar sal wees.

In die lig van die versoek vir korter en eenvoudiger finansiële verslae, die feit dat die verstaanbaarheid van finansiële verslae ‘n probleem blyk te wees, asook die feit dat beperkte navorsing oor die verstaanbaarheid van interim finansiële verslae tot op hede gedoen is, is daar besluit om vas te stel of individuele aandheelhouers die konteks en inhoud van interim finansiële verslae verstaan, wat, *per se,* die meer bondige en minder komplekse finansiële verslae is wat deur maatskappye aangebied word.

Die studie behels ‘n opname by wyse van ‘n posvraelys onder ‘n steekproef van individuele aandeelhouers van drie groot Suid-Afrikaanse genoteerde kleinhandelsmaatskappye, ten einde vas te stel of individuele aandeelhouers die konteks en inhoud van interim finansiële verslae verstaan en onder andere sodanige verslae gebruik om beleggingsbesluite te neem. Die studie is breedweg gegrond op die hoëprofiel-studies van Lee en Tweedie wat in die laat sewentiger jare uitgevoer is ten opsigte van individuele aandeelhouers.

Die primêre navorsingsdoelwit was om te bepaal of individuele aandeelhouers van Suid-Afrikaanse genoteerde kleinhandelsmaatskappye die konteks en inhoud van interim finansiële verslae verstaan. Daar is bevind dat die begrip van hierdie verslae by individuele aandeelhouers oor die algemeen beperk is. Daar is egter bewyse dat ondervinding en opleiding in die veld van finansiële rekeningkunde begrip van die inhoud van interim finansiële verslae verbeter.

Buiten vrae oor die demografie en beleggingsdoelwitte van individuele aandeelhouers is ‘n aantal ander vrae ook by die vraelys ingesluit ten einde verskeie sekondêre navorsingsdoelwitte aan te spreek. Onder andere is die vrae rondom die sekondêre navorsingsdoelwitte ontwerp om inligting in te samel oor hoe individuele aandeelhouers beleggingsbesluite neem, watter inligtingsbronne deur individuele aandeelhouers gebruik word wanneer hulle beleggingsbesluite neem, watter bykomende inligting by interim finansiële verslae ingesluit behoort te word, asook die kommunikasiemedium waarin individuele aandeelhouers sou verkies om interim finansiële

verslae te ontvang. Die studie het onder andere getoon dat die meeste respondente in hierdie studie hulle eie beleggingsbesluite inisieer, dat artikels in die finansiële pers die mees gewilde inligtingsbron is wanneer beleggingsbesluite geneem word, en dat individuele aandeelhouers steeds verkies om interim finansiële verslae per pos te ontvang.

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LIST OF ACRONYMS AND ABBREVIATIONS

AAA	American Accounting Association
AICPA	American Institute of Certified Public Accountants
ANOVA	Analysis of variance
APB	Accounting Principles Board
AR(s)	Annual Report(s)
ASB	Accounting Standards Board
ASC	Accounting Standards Codification
CICA	Canadian Institute of Chartered Accountants
CPA	Certified Public Accountants
DAA	Data Analysis Australia
DF	Degrees of freedom
DTR	Disclosure and Transparency Rules
EU	European Union
FASB	Financial Accounting Standards Board
FRC	Financial Reporting Council
FRS	Financial Reporting Standard
FSA	Financial Services Authority
G4 + 1	Australia, Canada, New Zealand, United Kingdom, United States
GAAP	generally accepted accounting principles
GPFR(s)	general purpose financial report(s)
IAS	International Accounting Standard
IASB	International Accounting Standards Board
IASC	International Accounting Standards Committee
ICAEW	Institute of Chartered Accountants in England and Wales
ICAS & NZICA	Institute of Chartered Accountants of Scotland & New Zealand Institute of Chartered Accountants
IFAC	International Federation of Accountants
IFRIC	International Financial Reporting Interpretations Committee
IFRS(s)	International Financial Reporting Standard(s)
IR(s)	interim (financial) report(s)

JSE	Johannesburg Stock Exchange (until June 2005)
JSE Limited	JSE Limited (from July 2005) – for reference and other purposes, JSE is used for material up to June 2005, thereafter JSE Limited is used for reference purposes only
MBA	Master of Business Administration
NYSE	New York Stock Exchange
PAT	Positive Accounting Theory
SAICA	South African Institute of Chartered Accountants
SAIPA	South African Institute of Professional Accountants
SEC	Securities and Exchange Commission
SFAC(s)	Statement of Financial Accounting Concept(s)
SFAS(s)	Statement of Financial Accounting Standard(s)
UK	United Kingdom
US	United States

LIST OF DEFINITIONS OF TERMS AND CONCEPTS

For the purposes of this study, the following definitions apply to the terms and concepts listed in alphabetical order below.

Term/Concept	Definition
Content of the IR:	The **content** of IRs in this study refers to the financially-related information (content) presented in IRs in terms of IAS 34 and the JSE Listings Requirements. In this study, it would include the condensed statements of financial position (the condensed balance sheet), the condensed statement of comprehensive income (the condensed income statement), the condensed statement of cash flows, the condensed statement of changes in equity and selected notes to the financial statements, but not management commentary, which is a non-standardized, open-ended component of the IR that could not be assessed effectively by means of the postal questionnaire used in this study.
Context of the IR:	The **context** of the IRs refers to the environment in which these statements/reports are presented. In this study, it specifically refers to with whom the legal responsibility for issuing IRs resides, whether IRs are audited or not, and what the objective of issuing IRs is.
Individual shareholders:	These are all shareholders **excluding** those with shares held by partnerships, joint shareholders, investment clubs, deceased estates, trusts, insurance companies, nominees, investment managers, medical aids, pension, provident and other retirement funds for each company, and individual shareholders that reside outside the borders of South Africa and Namibia, because of practical and cost considerations.

Term/Concept	Definition
Interim financial report (IR):	The meaning of this term is defined in IAS 34, paragraph 4, as a financial report which contains either a complete set of financial statements (as described in IAS 1) or a set of condensed financial statements (as described in IAS 34) for an interim period. In the literature, reference may also be made to quarterly reports and half-yearly reports, and these terms are used interchangeably in referring to IRs. (Also see the definition of an interim period, below, for more clarity.)
Interim period:	This period is defined in IAS 34, paragraph 4, as a financial reporting period shorter than a full financial year. An interim period would include both three-month and six-month periods, depending on the jurisdiction in which the entity providing the IR is listed. In South Africa, the UK and Europe, interim periods of six months would apply, while in the US, an interim period would represent a quarter (a three-month period). Although this situation does not apply to the three companies used in this study, South African companies with a dual listing in a jurisdiction where quarterly interim reports are required would have to issue quarterly interim reports.
Institutional investors:	These are insurance companies, pension, provident and other retirement funds and collective investment schemes, such as unit trusts. (They are not the focus of this study.)
Perceived understanding:	The perceived understanding of the users of IRs refers to how well individual shareholders **believe** they understand IRs.
Total percentage score:	This represents marks achieved for correct answers by respondents when answering questions contained in the research instrument (questionnaire) that were designed to assess their understanding, expressed as a percentage of the total number of possible marks that could have been achieved if a respondent answered all the questions assessing understanding of IRs in the

Term/Concept	Definition
	instrument correctly. This term is used when assessing both the context and the content of IRs, as well as when assessing content only.
Understanding:	Understanding implies that the users of general purpose financial statements/reports should comprehend the information presented in the IRs. In this study, the level of understanding of the content of the IRs is measured with reference to the total percentage scores achieved by individual shareholders when answering the section of the questionnaire designed to assess their understanding.

CHAPTER 1: INTRODUCTION

1.1 INTRODUCTION

The first chapter provides background to the study. It also gives an indication of the reading preceding and related to the study, defines the problem to be investigated and considers the research objectives, the broad research design and the relevance of the study. Furthermore, details are provided on the limitations and structure of the study.

1.2 BACKGROUND

In the business world, annual reports (hereafter ARs) form part of the process whereby business entities (hereafter companies) report to stakeholders on their financial position, financial performance, changes in their financial position, cash flow and other matters. The financial statements of a company, a major component of ARs, generally consist of statements of the company's financial position (formerly called balance sheets), statements of profit and loss and other comprehensive income (formerly called statements of comprehensive income or income statements), statements of changes in equity, statements of cash flows and accompanying notes (IASB, 2011c:§10). ARs therefore include financial statements, as well as other relevant information, and are meant to assist users of ARs in deciding whether these users should provide resources to a company – by investing in the company by buying shares, lending money to the company or selling items to the company on credit (IASB, 2010:§OB2). ARs are therefore used to report financial and other relevant information to stakeholders.

Financial reporting can also be described as a tool that accountants and the management of companies use to communicate financial information to companies' stakeholders to enable these stakeholders to make decisions on whether they would like to buy, sell or hold their investments in companies (AAA, 1966:1; Bartlett & Chandler, 1997:246). It is therefore important that company stakeholders who study ARs find the information provided in these reports **useful**, otherwise such reports will not be able to assist stakeholders in making decisions.

The International Accounting Standards Committee (hereafter IASC), the International Accounting Standards Board (hereafter IASB) and the Financial Accounting Standards Board (hereafter FASB) have concluded that, in order to be useful, financial information needs to meet a number of criteria – these criteria are referred to as the qualitative characteristics of financial statements. The earlier version of the conceptual framework of the IASB (hereafter the 1989 IASB Framework)[1] identified only four qualitative characteristics that contribute to the usefulness of financial information, namely relevance, reliability, comparability and understandability (IASC, 1989:§24). Two more qualitative characteristics are added in the conceptual framework issued jointly by the IASB and FASB (hereafter the 2010 IASB/FASB Framework), and the six criteria are still collectively known as the qualitative characteristics of useful financial information (IASB, 2010:§QC4). According to the 2010 IASB/FASB Framework, financial information must be relevant, reliable (represent what it purports to present faithfully), comparable, verifiable, timely and understandable (IASB, 2010:§QC4). These characteristics are examined in more detail in Chapter 2.

In 1995, South Africa decided to adopt the accounting pronouncements of the IASB, and to apply them *mutatis mutandis* in the South African accounting environment (Techtalk, 1995:4). By implication, South Africa therefore adopted subsequent amendments and new pronouncements from that point forward; hence, the qualitative characteristics required in both the 1989 and 2010 frameworks are relevant to this study.

Company stakeholders include a wide range of users of ARs, such as lenders, creditors, shareholders, employees, the general public and others. In many instances, these stakeholders are unable to demand specific information from a company in which they have an interest; therefore, they have to rely on the information contained in the ARs that the companies provide. This situation led the IASB and FASB to describe the ARs made available to this wide range of users for decision-making purposes as general purpose financial reports (hereafter GPFRs) (IASB, 2010:§OB5). From the definition of GPFRs, it is evident that there

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[1] Although the original document was published by the IASC and appears as such in the in-text reference and the reference list, this framework is referred to as the 1989 IASB Framework throughout the study. This decision was made because the IASB adopted all pronouncements of the IASC when the IASB came into being (IASB, 2011b:§5).

are at least two types of financial report that could be described as GPFRs. These are annual financial statements (which form a part of ARs) and interim financial reports (hereafter IRs). The format and contents of both these types of GPFR are prescribed by the IASB in two International Accounting Standards (hereafter IAS): IAS 1 relates to the presentation of financial statements (comprehensive financial statements which are usually issued annually), and IAS 34 relates to the presentation of IRs (including condensed financial statements, which are issued at intervals shorter than a year). In summary, it can thus be said that the objective of GPFRs (including ARs and IRs) is to provide stakeholders with information about the financial position, the financial performance, changes in equity and cash flows, as well as financial and other related information of an entity, in a way that is useful to stakeholders in making decisions (IASB, 2010:§OB2, 2011b:§7; IASC, 1989:§12).

Shareholders are generally entitled to a GPFR at least once a year. The financial information contained in GPFRs can be used, amongst other things, to enable shareholders to make economic decisions pertaining to a particular company, such as whether to buy, sell or hold their shares in that company (IASB, 2010:§OB2; IASC, 1989:§12). However, logically, shareholders cannot limit themselves to making economic decisions only once a year (Benade, 1970:442), so a need arose for financial information to be communicated to shareholders more frequently than only once a year. To meet this need, IRs were developed – IRs are reports issued at intervals shorter than 12 months (IASB, 2008:§4).

Similar to the ARs mentioned earlier, IRs provide shareholders with information on the financial position, performance, changes in equity, cash flows and other financially-related information of an entity, but, in this instance, the information is provided to stakeholders at the end of an **interim period**, and not only at the end of a financial year (IASB, 2008:§5,§8). In contrast to ARs, which are issued on an annual basis, IRs are issued at least after the first six months of a financial year (the interim period), and can follow a much briefer format than that required for ARs (IASB, 2011a:§1,§6). In most countries, listed companies issue IRs six-monthly (Alves & Dos Santos, 2005:2; JSE Ltd, 2012:§3.15), but in the United States (hereafter US) such reports are issued on a quarterly basis, and are referred to as quarterly reports (Hussey & Woolfe, 1994:6; SEC, 2008b:3).

If shareholders do indeed **use** ARs and IRs when they make investment decisions, it is important that they **understand** the financial information presented in such reports, because otherwise, they would find it difficult to base their investment decisions to buy, sell or hold shares on the information contained in such reports. The usefulness of ARs and IRs in general are not in doubt,[2] but it appears that there may be problems with understanding some of the financial information contained in ARs and IRs. Some of the problems encountered in understanding the financial information presented in such reports are investigated in the rest of this section.

Over the last few years, the IASC and its successor, the IASB, as well as other accounting bodies such as the FASB in the US and the Financial Reporting Council (hereafter FRC) in the United Kingdom (hereafter UK), have made a concerted effort to improve the standard of financial reporting both in their own jurisdictions and globally, as appropriate (IFAC, 2008:5).

Despite their declared intention to improve financial reporting, it appears that the proliferation of financial reporting standards have made financial reports more complex than before, and this may compromise the understanding of the content of financial reports (ICAS & NZICA, 2011:2; IFAC, 2008:28). To address the problem, a number of leading accounting bodies in the world (aside from the IASB) have commissioned investigations into this matter (Hassan, 2009:69; Pounder, 2011:21). These accounting bodies, the reports produced, the information and findings in these reports relevant to this study include the following:

- The International Federation of Accountants (hereafter IFAC) produced three reports, namely *Financial reporting supply chain: current perspectives and directions* (IFAC, 2008), *Developments in the financial reporting supply chain – results from a global study among IFAC members* (IFAC, 2009), and *Integrating the business reporting supply chain* (IFAC, 2011). These reports (the earliest of which was published in 2008) suggest that the usefulness of ARs is constrained by their complexity and disclosure overload, and that stakeholders are finding it increasingly difficult to understand such financial reports (IFAC 2008:32). The respondents who participated in the surveys and in-depth interviews across the financial reporting supply chain included preparers, external auditors, users, regulators, standard setters and academics (IFAC, 2008:8, 2011:3). The respondents indicated that they preferred shorter and simplified reports (IFAC, 2008:35, 2011:20), and that they felt that the relevance and reliability of financial reports had improved (IFAC, 2008:30,50, 2011:8,19).

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[2] See Section 2.6.3.1.

- The Securities and Exchange Commission (hereafter SEC) in the US commissioned the *Final report of the Advisory Committee on Improvements to Financial Reporting to the Securities and Exchange Commission* (SEC, 2008b). This report was based on evidence provided by witnesses called before the Committee and on comment letters received from various constituents (SEC, 2008b:22,F-1). The report states that many individuals may find the annual and quarterly reports (IRs in the US are issued quarterly) of a company too complex and detailed, and it calls for a short executive summary to be included at the beginning of a company's annual report, to be submitted on Form 10-K.[3] In respect of IRs, the Committee recommended that a short executive summary be provided as part of Form 10-Q.[4] This executive summary should contain material updates to the executive summaries presented in previous annual or quarterly reports, as the case may be (SEC, 2008b:3,16). The Committee also recommended that the FASB and SEC update and remove outdated and duplicated disclosure requirements that arose over time as a result of the fact that individual accounting pronouncements were developed on a piecemeal basis (SEC, 2008b:34).
- The FRC in the UK produced two reports, *Louder than words: principles and actions for making corporate reports less complex and more relevant* (FRC, 2009) and *Cutting clutter: combatting clutter in annual reports* (FRC, 2011). Of the two, the latter report is more relevant to this study. The first report used input from a number of interviewees and the second one drew on that input (FRC, 2011:41). These reports identified clutter (providing every required disclosure, irrespective of its materiality, and providing the same explanatory information year-by-year) as the main problem obscuring important information, reducing the usefulness of corporate (annual) reports (ARs) and inhibiting a clear understanding of a business and the challenges it faces (FRC, 2011:2). In addition, the 2011 report states that "reports should be: open and honest, clear and understandable, and interesting and engaging" (FRC, 2011:31). Although the 2011 FRC report relates specifically to ARs, it emphasizes that (all) reports should be understandable.
- The IASB commissioned a report from the Institute of Chartered Accountants of Scotland and the New Zealand Institute of Chartered Accountants (hereafter ICAS & NZICA). The report was published as *Losing the excess baggage – reducing disclosures in financial statements to what is important* (ICAS & NZICA, 2011). This report was prepared by a

[3] Data filed at the SEC in respect of ARs are submitted on Form 10-K.
[4] Data filed at the SEC in respect of IRs are submitted on Form 10-Q.

committee comprised of auditors, company directors, an investment analyst and technical staff from ICAS and NZICA (ICAS & NZICA, 2011:133). Although IRs were excluded from the scope of the study, the principles identified in the report (and these are particularly relevant to the current study) are that disclosures should only be made if they are capable of making a difference to investors' decisions, and that removing countless detailed disclosures makes financial statements more concise, clearer, and consequently more understandable (ICAS & NZICA, 2011:3,4).

The reports considered in this section[5] do not dispute that ARs and IRs are useful to stakeholders who need to make investment decisions, but all conclude that the understandability of financial reports to users has not improved, and has even deteriorated over the years. This problem appears to be a result of increased disclosure requirements (and, in several instances, of a duplication of disclosure requirements) arising from the piecemeal development of accounting standards. Thus, over time, the complexity of the business environment itself and the complexity and increase in the number of standards have led to financial reports' becoming longer (ICAS & NZICA, 2011:2). The respondents surveyed in the preparation of at least five of the reports considered above were convinced that more conciseness and less complexity would make for clearer and more understandable financial reports (FRC, 2011:5,6; ICAS & NZICA, 2011:12; IFAC, 2008:35, 2011:19; SEC, 2008b:3).

The above reports reached a number of conclusions in respect of the understanding of the content of financial statements on the basis of data gathered by means of qualitative surveys and interviews with respondents. However, it appears that no empirical work to establish whether users of financial statements actually understood financial statements was done while compiling these qualitative reports.

The information reflected in the reports suggests that of the two GPFRs identified earlier, IRs should be more understandable to users than ARs, because IRs are shorter, and they generally include financial statements presented in a condensed format. This prompted the decision in the current study to focus on IRs, and to review the literature to establish to what extent the qualitative characteristics that inform the usefulness of IRs (the shorter of the two kinds of GPFR) have been considered and studied in the prior literature.

[5] Other bodies, such as the Global Accounting Alliance, concur with these views.

1.3 REVIEW OF PRIOR LITERATURE ON QUALITATIVE CHARACTERISTICS OF FINANCIAL REPORTS AND IRS

A brief review of the academic literature available on the qualitative characteristics that inform the usefulness of IRs was conducted in the previous section and is elaborated on below.

There is sufficient evidence in the academic literature to show that the usefulness of IRs is not in doubt.[6] A literature review indicates that the relevant accounting pronouncement on IRs, namely IAS 34 *Interim financial reporting*, and the Johannesburg Stock Exchange (hereafter JSE) Listings Requirements have been available and have been applied in South Africa since 1999. IAS 34 prescribes the minimum content and the principles for the recognition, measurement and the format of IRs in South Africa (IASB, 2011a) and the JSE Listings Requirements indicate other disclosure requirements for listed companies. However, none of the peer-reviewed research on qualitative characteristics mentioned below originates in South Africa, which is a developing country with a wide range of users from different cultural and educational backgrounds.

The detailed literature review below on the qualitative characteristics associated with IRs indicates that two of the four characteristics contained in the 1989 IASB Framework have been the subject of extensive research, namely relevance and reliability. The main points of this research are discussed briefly.[7]

A debate arose on the qualitative characteristic of relevance, considering whether IRs should be issued on a quarterly basis or a half-yearly basis (Alves & Dos Santos, 2005:2; Bagshaw, 2000b:40; Baron, 2002:1; Butler, Kraft & Weiss, 2007:26; Gajewski & Quèrè, 2001:701; Jackson, 2008:28; Wilde, 2005:40; Yee, 2004:189). Issuing IRs more frequently would logically increase the relevance of the information, but could lead to a reduction in reliability. The urgency of this matter receded when the European Union (hereafter EU) decided to require six-monthly interim reports (EU, 2004:11). The decreased relevance of the topic can be deduced from the lower number of articles published on this topic after 2005.

[6] See Section 2.6.3.1.
[7] The details are discussed more fully in Chapter 2.

Another issue that has been frequently debated in the literature is whether IRs should be subject to a statutory audit or audit review, and what impact such an audit or review might have on IRs (Bagshaw, 2000a:57; Carroll, 2000:15; Guan, He & Yang, 2006:570; Han, 2010:2; Ketz & Miller, 1999:16). These studies on reliability conclude that having either an audit or an audit review would definitely contribute to the reliability of IRs, but would probably have a negative impact on the timeliness (and thus relevance) of these reports.

Two of the qualitative characteristics of useful financial information, namely relevance and reliability, thus appear to have been researched in respect of IRs. Admittedly, the fact that the 2010 IASB/FASB Framework was only issued in late 2010 may have contributed to the current dearth of research on the two new qualitative characteristics (verifiability and timeliness) identified in this revised conceptual framework. However, the remaining two qualitative characteristics which were identified in the 1989 IASB Framework and which are still present in the 2010 IASB/FASB Framework, namely understandability and comparability, appear not to have been dealt with in research related to IRs to the same extent as relevance and reliability, if at all. The lack of research on the two qualitative characteristics of the understandability and comparability of IRs could imply that the attributes of understandability and comparability in IRs are not perceived to be in doubt, since IRs are considered to be useful, but, at the same time, the paucity of research to enhance understanding of IRs creates an opportunity to investigate questions such as

- whether users of IRs do understand the content of the IR (understandability); and
- whether the ability to compare financial information contained in IRs contributes to the usefulness of IRs (comparability).

The studies of the IFAC (2007) and the SEC (2008) related to understandability have been considered carefully. In view of the fact that these studies mention that users appear to prefer shorter reports (IFAC, 2008:35), the above review of prior literature, and the absence of empirical work to assess whether IRs are understood, it was decided that this study would, amongst other things, endeavour to establish empirically whether users understand the context and content of IRs (see the List of definitions of terms and concepts that precedes Chapter 1) and use IRs to make investment decisions.

Another crucial factor that supported the decision to investigate the qualitative characteristic of understandability was the fact that from 2010 the JSE Listing Requirements, in compliance with the King Report and Code on Corporate Governance (hereafter King III), require listed companies to issue an integrated report (integrating financial and sustainability information in one report) (JSE Ltd, 2012:§8.63; SAICA, 2012). In preparing such integrated reports, it is recommended that the traditional financial component of a report be presented in the format of IRs, as described in IAS 34 (Ernst & Young, 2012a). The effectiveness of integrated reporting in South Africa therefore hinges largely on users' understanding of the financial information contained in IRs. Consequently, the future importance of IRs in line with this listings requirement was an additional impetus for the current study to investigate whether individual shareholders in South Africa understand the content of IRs.

The qualitative characteristic of understandability in the context of IRs is thus the primary focus of this study, while the use of IRs for investment decisions is a secondary focus.

1.4 THE PROBLEM STATEMENT

As indicated in Section 1.2, above, several studies have shown that the understanding of financial information by users is limited and that respondents would prefer more concise ARs. As explained in Section 1.3, above, a review of the available literature reveals that no recent peer-reviewed research has been published in South Africa to indicate to what extent local stakeholders understand the context and content of IRs of South African listed retail companies, and whether or not they use IRs to assist them in making investment decisions. The absence of research on whether IRs are understood by users may be attributed to the fact that users may consider IRs as less important than ARs. However, the advent of integrated reporting and the proposed use of the IAS 34 format for financial statements in such reporting for companies listed on the JSE have increased the importance of IRs, as well as the issue of how well IRs are understood by the users of such reports. This study therefore proposes to investigate the following empirically in respect of individual shareholders (who constitute one group of users of GPFRs and thus of IRs):

- whether or not they understand the general purpose of IRs issued by retail companies listed on the JSE, who is legally responsible for compiling them, and their nature (hereafter collectively defined as the "context" as included in the List of definitions of terms and concepts);
- whether or not they understand the financially related content (hereafter defined as the "content" in the List of definitions of terms and concepts) of the IRs of retail companies listed on the JSE;

- how they make investment decisions (on their own initiative or with the assistance of financial advisors), whether or not they use IRs to make investment decisions, and whether or not they require additional information in IRs to do so;
- to what extent they read IRs; and
- sundry other aspects related to IRs.

The justification for including the components contained in the above problem statement to be investigated is discussed in more detail below.

1.4.1 Limiting stakeholders studied to individual shareholders

Since it would be impracticable to gain access to all the kinds of stakeholders listed in the 1989 IASB Framework and 2010 IASB/FASB Framework for all South African companies, it was decided to limit the stakeholders to be investigated in this study to individual and institutional investors (shareholders).[8] The original intention was to include both individual and institutional shareholders in the study, but the scope was subsequently restricted to individual shareholders – institutional investors as a stakeholder group had to be abandoned due to a response rate of only 1.22% (this represents a total of five responses out of the more than 400 institutional investors surveyed during the initial and follow-up mailing events).

1.4.2 Assessing the understanding of the context and content of IRs and the use of IRs in investment decision-making

Presenting interim financial information to shareholders (investors) is pointless if they do not understand the information contained in IRs. Furthermore, shareholders are not able to make informed decisions about holding, buying or selling shares and providing of resources (based on their use of IRs) unless the context and content of IRs are understood.

The fact that both IAS 34 and the JSE Listings Requirements relevant to IRs have been entrenched in South African financial reporting for a number of years has reduced the uncertainty normally associated with newly introduced reporting standards and listings requirements. This should make a positive contribution to the understanding of the context and content of IRs in South Africa.

[8] See Section 2.6.2 for more detail.

The background information set out in Section 1.2 indicates that over time the accounting standards (the IASs and International Financial Reporting Standards (hereafter IFRS) in particular) have become more complex and comprehensive as the IASB, its predecessor (the IASC) and other accounting bodies, have attempted to provide users of financial statements with more and better information (Bush, 2005:4; IFAC, 2008:32). Usefulness appears to have been compromised by an increase in the complexity of financial reports. Furthermore, the advent of integrated reporting in terms of the JSE Listings Requirements has placed a renewed emphasis on IRs as a vehicle to present useful information to stakeholders in South Africa.[9] In view of the above development, as well as the limited amount of prior questionnaire-based survey research in respect of the understanding of the context and content of IRs worldwide and in South Africa in particular,[10] it was decided that a questionnaire-based study to determine whether or not individual shareholders understand the context and content of IRs of listed retail companies in South Africa and use IRs for investment decisions would provide valuable insight on whether IRs provide individual shareholders with information (both context and content) that they understand and use.

The results of the current study cannot be compared to the results of earlier South African studies, because the qualitative characteristic dealing with understanding (understandability) appears not to have been subjected to academic research previously published in South Africa. Note that this study did not focus on the readability of the narrative sections of IRs (the readability of the narrative sections in ARs has already been researched extensively).

1.4.3 Selecting retail companies on the JSE

The published IRs of three well-known companies listed respectively in the Food & Drugs and the General Retail Sectors of the JSE (collectively known as the Retail Sector of the JSE) were used in this study, because these companies operate in business sectors that should be familiar to most users of financial statements. To answer the questions in the questionnaire probing the understanding of individual shareholders of the context and content of IRs, investors would thus not require specialist knowledge of the industry in which the company

[9] See Section 1.3, above.
[10] See Section 2.7.

concerned operates, as might be the case, for instance, for companies operating in the fields of mining, financial services or information technology.[11]

1.5 RESEARCH OBJECTIVES AND IMPORTANCE OF THE STUDY

The problem statement introduced in Section 1.4 is broken down further in this section by defining the primary and secondary research objectives of this study.

1.5.1 Primary research objective

The primary research objective of the study was to determine whether individual shareholders of South African listed retail companies understand the context and content of IRs. This objective relates to the qualitative characteristic of understandability, which enhances the usefulness of financial information.

1.5.2 Secondary research objectives

The secondary research objectives were related to individual shareholders' investment decisions and use of IRs. The secondary objectives addressed in this study can be divided into the two categories indicated below.

Category 1 deals with investment decisions and the use of IRs for investment decisions by individual shareholders, to establish

- how individual shareholders currently make investment decisions (on their own initiative or via financial advisors);
- what sources of information individual shareholders are using when making investment decisions;
- whether individual shareholders deem IRs important for making investment decisions; and
- what other crucial information is currently not provided, but that individual shareholders would prefer to see in IRs to facilitate investment decisions.

[11] For more detail, see Section 4.4.1.

Category 2 deals with other matters that are related to IRs, to establish

- in what sequence individual shareholders would prefer the components of the IR to be presented;
- whether the IR is read by individual shareholders and to what extent; and
- in what medium of communication individual shareholders would prefer to receive IRs.

1.6 IMPORTANCE OF THE STUDY

The contribution of this study is that it is a comprehensive survey determining primarily whether individual shareholders understand the context and content of IRs that are issued by South African listed retail companies and that are prepared in accordance with the requirements of IAS 34 and the JSE Listings Requirements.

As mentioned earlier, the relevance of IRs in South Africa has increased because the JSE Listings Requirements in the case of listed companies with financial years commencing on or after 1 March 2010 now require such companies to publish integrated reports (SAICA, 2012). In these reports of listed companies, the financial and non-financial information should be integrated, and the most material matters in respect of the business should be addressed as concisely as possible. It has been suggested that traditional financial information presented in such reports should include condensed financial statements prepared according to IAS 34, since these condensed statements are short and concise (Ernst & Young, 2012a). The results of this study could make a valuable contribution to the development of a standard governing integrated reporting in South Africa and could also inform the standard setting process internationally.

Although the literature review in Chapter 2 indicates that the usefulness of IRs is not in doubt, a study focusing on the understanding of IRs has not thus far been conducted in South Africa. Therefore, such a study could provide valuable insight on whether individual shareholders understand the context and content of IRs. This is particularly important at this juncture, because integrated reports may adopt the format of IRs when presenting financial information.

Addressing the secondary objectives listed in Section 1.5.2, above, provides additional information to the South African public at large, to company management, to researchers and to standard setters, on how individual shareholders make investment decisions, what sources of information they use for investment decision purposes, whether IRs are used for making investment decisions, and what additional information individual shareholders require in IRs to facilitate investment decisions. In addition, the findings show in what sequence individual shareholders prefer the individual components of IRs to be presented, whether and to what extent IRs are read, and in what communication medium individual shareholders would prefer to receive IRs.

1.7 LIMITATIONS OF THE STUDY

The study is subject to a number of limitations:

- This study considers the understanding and use of IRs by individual shareholders resident in South Africa and Namibia. Namibian share investors are included because there are a small number of companies listed on the Namibian Stock Exchange, which provides limited local investment opportunities to Namibian nationals. In addition, Namibia had very close historical ties with South Africa prior to independence in 1990.
- This study focuses on the concept of understanding, as defined in the List of definitions of terms and concepts, and does not consider the functions of the cognitive domain as depicted in the taxonomies of either Bloom or Anderson and Krathwohl (Huitt, 2011).
- The IRs of three well-known retail companies listed in the Food & Drug and General Retail Sectors (the Retail Sector) of the JSE are used in the survey. Hence, conclusions drawn from the survey questionnaires administered to the individual shareholders of these companies would therefore only be generalizable to retail companies in the greater retail sector, and not to companies listed in other sectors of the JSE. For reasons of confidentiality, the names of the three participating companies are not revealed, but it can be stated that they represented more than 30% of the combined market capitalization at the end of 2008 and 2009 of the two sectors mentioned respectively. Further details on the companies and sectors are given in Section 4.4.1.
- In view of the fact that the survey was performed by means of a postal questionnaire, the various limitations associated with questionnaire-based postal surveys apply. These include a low response rate (usually below 15%) with the possibility of non-response bias, limitations on the length of postal questionnaires and the resulting reduction in data that can be gathered in this way. To address the anticipated low response rate, a follow-up was mailed, which improved the effective response rate to 17.48%. Tests were performed

to assess the potential presence of non-response bias, but no evidence of non-response bias was found.[12]

- Due to the limitations on the possible length of a postal questionnaire and the reduced number of questions included in the questionnaire resulting from those limitations, the understanding of the context and content of the IRs can only be assessed in total, and not per individual component of the IR.
- The narrative component of IRs (this refers to comment/commentary by management and not the selected explanatory notes) did not form part of questions in the questionnaire and therefore no conclusion could be drawn on whether individual shareholders understand that aspect of IRs.
- Since this type of research has not been done on IRs in South Africa before, it was not possible to compare the research results with the results of similar South African studies on IRs.

1.8 ASSUMPTION MADE IN THE STUDY

No benchmark for an acceptable level of understanding of financial statements (including IRs) when using questionnaires to assess understanding could be identified in the literature. Therefore, it is assumed in this study that 50% indicates an acceptable level of understanding of the content of the financial information contained in an IR. This is in line with the pass mark used by universities in South Africa to award credits for modules students enrol in during their tertiary studies.

1.9 OUTLINE OF THE STUDY

The study consists of six chapters, which are organized as follows:

- **Chapter 1: Introduction**
  In this chapter, the introduction and background to the study, problem statement, research objectives and importance of the study, limitations and outline of the study are addressed.
- **Chapter 2: Underlying theories and literature review**
  The accounting theory on which the study is based and a related literature review are addressed in this chapter. The discussion includes the decision-usefulness theory, the

[12] See Section 4.6.2.2.

relevant conceptual frameworks, qualitative characteristics that improve the usefulness of financial information, understandability and understanding, and some techniques to assess understanding.

- **Chapter 3: The development of interim financial reporting in the US, the UK and South Africa**
  The historical development of IRs in the US, the UK and South Africa is considered in detail to provide insight into the origins, sources of guidance on the presentation of IRs (listings requirements, legal requirements and accounting pronouncements) and development of IRs over time.
- **Chapter 4: Research design and method**
  The details of the research design and method used in the empirical part of the study (a survey by means of a questionnaire) are provided in this chapter. In addition, the chapter discusses the development of the questionnaire that was used in the study, the selection of the population and samples of individual shareholders, the distribution of the questionnaires, the response rate achieved, testing for non-response bias, as well as the statistical techniques employed in the study.
- **Chapter 5: Results of the empirical study**
  This chapter presents the details of the research results that emerged from the analysis of the data using appropriate statistical techniques. The understanding by respondents of the content of IRs is compared to their perception of their understanding of the content. The chapter explores whether various demographic variables provide further insight on what affects respondents' level of understanding. The survey results in respect of the secondary objectives are also elaborated on. Two summaries of the findings are provided: one relating to the primary research objective and the other relating to the secondary research objectives.
- **Chapter 6: Overview, conclusions and recommendations**
  In this concluding chapter, a brief overview of the study, conclusions on the empirical investigation and recommendations on how to improve the understanding of the context and content of IRs are presented. The results of the empirical investigation relating to the secondary research objectives are discussed and recommendations are made where appropriate. The study closes with suggestions for future research.

CHAPTER 2:
UNDERLYING THEORIES AND LITERATURE REVIEW

2.1 INTRODUCTION

The problem to be addressed in this study has been set out in Chapter 1. Flowing from the problem statement, there were the research objectives. These could be summarised as an assessment of whether individual shareholders understand the context and content of the IRs of listed retail companies in South Africa and use IRs in making investment decisions. Since this study endeavours mainly to establish whether individual shareholders (users) **understand** the context and content of IRs and **use IRs for making investment decisions**, it is important to investigate the accounting theory relating to these two matters in particular.

2.2 THEORY, ACCOUNTING AND ACCOUNTING THEORY

Before the specific accounting theories associated with the primary and secondary research objectives of this study are addressed, it is necessary to ensure a broad understanding of the concept of a **theory**, and of what is meant by the terms **accounting** and **accounting theory**.

Hendriksen (1970:1) explains a theory as a "coherent set of hypothetical, conceptual and pragmatic principles forming the general frame of reference for a field of enquiry". The FASB, the first accounting body to develop a conceptual framework for accounting, defines a theory as a "coherent system of interrelated objectives and fundamentals that could lead to consistent standards" (FASB, 1976:2). The *Oxford Dictionary online* (2012) defines a theory as

> A supposition or a system of ideas intended to explain something, especially one based on general principles independent of the thing to be explained, which includes amongst others:
> - An idea used to account for a situation or justify a course of action.

It can be deduced from the three definitions above that a **theory** is a system of principles, interrelated objectives, and fundamentals or ideas that account for a situation or justify a course of action. From the range of different definitions above, it is clear that the definition of a theory is not cast in stone.

The definition of **accounting**, like the definition of a theory, has changed over time. This evolution is illustrated by the following sequential, but not exhaustive, range of definitions:

> The central purpose of accounting is to make possible the periodic matching of costs (efforts) and revenue (accomplishments) in the calculation of the result. This concept is the nucleus of accounting theory, and a benchmark that affords a fixed point of reference for accounting discussions. (Littlejohn, 1953:30)

The above definition provides a somewhat restricted and now dated view of accounting and alludes to what has been called the "income statement approach" to accounting.

Slightly more than a decade later, in 1966, the American Accounting Association (hereafter AAA) in *A Statement of Basic Accounting Theory* (AAA, 1966:1) provided a broader perspective of accounting, by stating that accounting is defined as "the process of identifying, measuring and communicating economic information to permit informed judgements and decisions by users of the information".

This definition is in line with the current view of accounting, because it describes accounting as a process of classifying, measuring and recording information to be communicated to users for the purpose of making decisions. The communication of information to users would generally take the form of ARs. Although it does not indicate whether the information provided should be **useful** to users in making decisions, it does mention that the information should lead to informed decisions, which implies usefulness.

In 1999, the Accounting Standards Board (hereafter ASB) in the UK described financial statements as "information about the reporting entity's financial performance and financial position that is useful to a wide range of users for assessing the stewardship of management and for making economic decisions" (ASB, 1999:19).

This definition by the ASB is in line with the latest international thinking that financial statements should provide information that is useful to users in making economic decisions, although the definition also includes a reference to stewardship. It appears that stewardship has been side-lined in favour of decision-usefulness since 1999, as is evidenced by the wording of the objective of general purpose financial reporting used in the 1989 IASB and

2010 IASB/FASB Frameworks (IASB, 2010:§OB2; IASC, 1989:§12; Sutton, 2009:106). Stewardship is now regarded as being embodied in decision-usefulness, although this view has been subject to much debate (Gray, 1994:35; O'Connell, 2007:224; Oldroyd and Millar, 2011:7; Wagenhofer, 2009:74).

Considering the above-mentioned evolving definitions, the definition of **accounting theory** as proposed by Hendriksen (1992, cited *verbatim* in Glautier, Underdown & Morris, 2011:41) provides an appropriate description of accounting theory for the purposes of this study:

> Accounting theory may be defined as logical reasoning in the form of a set of broad principles that (1) provide a general frame of reference by which accounting practice can be evaluated, and (2) guide the development of new practices and procedures. Accounting theory may also be used to explain existing practices to obtain a better understanding of them. But the most important goal of accounting theory should be to provide a coherent set of logical principles that form the general frame of reference for the evaluation and development of sound accounting practices.

A more concise and more recent definition of accounting theory than that of Hendriksen is that of Wolk, Dodd and Tearney (2004:2):

> The basic assumptions, definitions, principles and concepts – and how we derive them – that underlie accounting rule making by a legislative body – and the reporting of accounting and financial information.

The above two definitions of accounting theory allude to an accounting framework (conceptual framework) against which accounting practices can be evaluated to ensure internal consistency of the concepts that underlie the reporting of accounting, the financial information on a company and the rule-making of a legislative body. Note that the above two definitions of accounting theory relate to financial accounting only, and not to management accounting. Drury (2008:7) and Glautier *et al*. (2011:51) distinguish between financial accounting and management accounting (although both arise from the recording of transactions). Their views can be summarised as indicating that the divergent needs of external and internal users of accounting information have led to the development of two sub-disciplines in the accounting field, namely financial accounting (generating external reporting) and management accounting (generating internal reporting). Since IRs, as addressed in this study, are focused on the needs of external users, IRs fall into the domain of financial accounting and external reporting, rather than that of management accounting.

Wolk *et al.* (2004:3) explain that financial accounting refers to "accounting information that is used by investors, creditors and other outside parties for analysing management performance and decision-making purposes". This definition indicates that financial accounting information (financial reporting) is used by parties outside the entity, and this is also confirmed by the IASB (2010:§OB2), the IASC (1989:§9) and Glautier *et al.* (2011:52).

Belkaoui (2004:83), like Wolk *et al.* (2004:3), concludes that, as yet, no comprehensive (general) theory of accounting has been formulated. This view is confirmed by Glautier *et al.* (2011:46) and Deegan (2010:7), who claim that there are many theories of financial accounting, but not yet a universally accepted theory thereof. Given the absence of a comprehensive/universally acceptable theory of accounting and the wide range of financial accounting theories available, it is imperative to establish theoretical points of departure that are in line with the research objectives of this study.

2.3 POSITIVE AND NORMATIVE ACCOUNTING THEORIES

Deegan (2010:10) suggests that accounting research appears to have evolved into two broad research approaches or classifications, namely positive research and normative research. Similarly, Glautier *et al.* (2011:42) list corresponding research approaches, namely descriptive (positive) research and decision-usefulness research (both normative and empirical). Glautier *et al.* (2011:44) also identify a welfare research approach, which they argue is an extension of the decision-making approach, focusing on the effects of decision-making on social welfare only.

Positive research represents research that seeks to predict and explain specific accounting phenomena and is often based on empirical observation. Theories aligned with this type of research would be classified as **positive theories** of accounting. Specific examples of positive theories of accounting include Legitimacy Theory, Institutional Theory, Stakeholder Theory (managerial perspective), Positive Accounting Theory (PAT) and Agency Theory (Deegan, 2010:256,257). Positive theories are based on the premise that all individuals are driven by self-interest, and leans strongly on this central assumption, which is grounded in Economics. For instance, one such positive theory, PAT, endeavours "to predict and explain why managers (and/or accountants) elect to adopt particular accounting methods in preference to others" (Watts & Zimmerman, 1986:7). However this theory, does not give an indication of whether the firm should have used the method or not (Watts & Zimmerman, 1986:7). Positive theories do not place a value judgement on the findings produced as part of the research process.

By contrast, **normative research** prescribes what should occur in particular instances and is therefore prescriptive. Normative theories are based on the values or beliefs held by researchers subscribing to these theories. These theories may or may not be based on observation, and should not be evaluated with reference to actual accounting practice, as these theories set norms to be adhered to and do not describe existing accounting practices. Some examples of normative theories are Stakeholder Theory (which provides a moral or ethical perspective), decision-usefulness theories, Continuously Contemporary Accounting and Conceptual Frameworks (Deegan, 2010:257).

Even though the study displays positivist characteristics as an attempt is made to explain certain phenomena observed during the analysis of the survey, its primary objective focuses on one specific qualitative characteristic of financial information, namely understandability, which enhances the usefulness of such information. Consequently the study also uses normative accounting theory especially related to decision-usefulness. In particular, the focus is on decision-usefulness theories and conceptual frameworks, as described by Deegan (2010:12) and Glautier *et al.* (2011:44). The conceptual frameworks are based on decision-usefulness theories.

2.4 DECISION-USEFULNESS THEORIES OF ACCOUNTING

According to Wolk *et al.* (2004:179), the large body of decision-usefulness research in the accounting arena focuses on the decisions, information needs, the identity and information processing ability of users of financial reports. Staubus (1999:163), a proponent of the decision-usefulness theory of accounting, is of the opinion that the components of the decision-usefulness theory are the following: "…the decision-usefulness objective, the identification of users and uses, the focus on investors' cash flow-oriented decisions, and the value of accounting information that is relevant to those decisions".

In line with Staubus's (1999) and Wolk *et al.*'s view, this study investigates, amongst other questions, whether individual shareholders (investors) understand the context and content of IRs, and use IRs for investment decisions.

According to Staubus (1999:159), the first prominent publication addressing decision-usefulness was the AAA's *A Statement of Basic Accounting Theory,* dating from 1966. Although *A Statement of Basic Accounting Theory* identifies the importance of decision-usefulness in accounting information, the report does not explicitly identify the users of accounting data (Young, 2006:587) and cautions that users may not be able to assess what information would be most useful to them (Buys, 2011:112). Sutton (2009:104,105) is of the opinion that decision-usefulness as such was specifically articulated for the first time in the work of the renowned accounting pioneer and 20th century Accounting thinker Raymond J. Chambers, in his work on Continuously Contemporary Accounting.

The concept won ground between 1966 and 1973 (Buys, 2011:112; Staubus, 1999:159), particularly when APB[13] Statement No 4, *Basic Concepts and Accounting Principles Underlying Financial Statements of Business Enterprises* (AICPA, 1970) affirmed that accounting should provide information that is useful in making economic decisions. An earlier article by Sterling (1972:198) also proposes this approach, arguing that, while many other properties of accounting information may be desirable, the usefulness of accounting information is indispensable.

Staubus (1999) states that the theory was first labelled the "decision-usefulness theory" by the AAA in 1977 in the publication *A Statement of Accounting Theory and Theory Acceptance*, written by the Committee on Concepts and Standards for External Financial Reports of the AAA. Glautier *et al.* (2011:43) share Staubus's view on the timing of the advent of decision-usefulness theories by stating that these theories of accounting originated in the 1970s when behavioural research expanded into the accounting arena. The view that accounting is linked to human behaviour is also alluded to in the following statement by the AAA (1971:247):[14]

> To state the matter concisely, the principle purpose of accounting reports is to influence action, that is, behavior. Additionally, it can be hypothesized that the very process of accumulating information, as well as the behavior of those who do the accumulating, will affect the behavior of others. In short, by its very nature, accounting is a behavioral process.

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[13] The acronym APB in this context refers to the American Accounting Principles Board and should be distinguished from the acronym used in South Africa for the Accounting Practices Board.
[14] Cited *verbatim* therefore original spelling is retained.

Gray (1994:10) is of the opinion that the term decision-usefulness is not well-defined, but that several studies have concluded the following:

- investors do use financial accounting data;
- most investors do not understand accounting data;
- the prices of shares mostly react significantly on messages presented by the accounting numbers and price movements generally track the underlying sentiment borne out by the accounting numbers;
- the information that investors really want (and that would, according to them, be most useful) is not presented in the current accounting data.

Decision-usefulness theories endeavour to establish what information certain classes of users of financial information need for making economic decisions such as whether to buy, hold or sell shares and other investments. This issue is addressed as part of the secondary research objectives of this study.

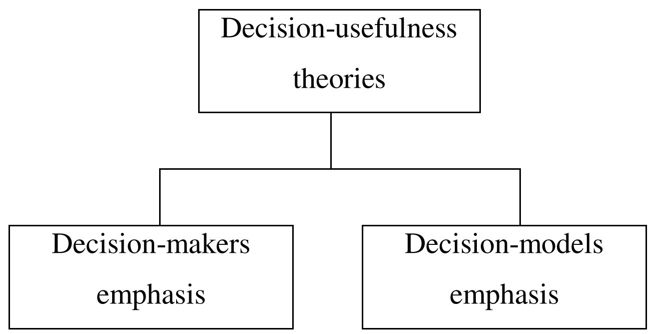
The FASB's Statement of Financial Accounting Concepts No 1, *Objectives of Financial Reporting by Business Enterprises* (FASB, 1978:9) assert that financial reporting should provide information that is useful in making economic decisions. Brewer (2009:95) points out that at the time of his 2009 study, decision-usefulness had become deeply entrenched in the authoritative literature on accounting and had replaced stewardship as an objective of financial reports. Brewer (2009:100) also concludes in his study that the majority of practitioners and academics have accepted decision-usefulness as the dominant objective of financial reporting. As mentioned before, decision-usefulness theories are not necessarily based on observations, but could be, as indicated by Glautier *et al.* (2011:44).

Over time, many criticisms have been levelled at the decision-usefulness theory of accounting. For instance, Buys (2011:118) states that providing decision-useful information for individuals is a difficult task, because the decisions of individual users are based on their specific needs, and these needs would be impossible to predict. In a paper delivered at the 9th Interdisciplinary Perspectives in Accounting Conference, Williams and Ravenscroft (2009:47) concluded that it is difficult to illustrate decision-usefulness in the case of individual decision-makers. McCarthy (2004:73) points out that users' needs are not really addressed in financial reporting, since users are not asked what they want to be presented in financial reports. Puxty and Laughlin (1983:550) have also indicated that decision-usefulness as a criterion for providing information may not be appropriate in complex real-world environments.

Notwithstanding such criticisms (excluding Buys's work, since he published subsequent to the release of the revised IASB/FASB Framework), in the IASB/FASB Framework issued in September 2010, the IASB and FASB once again confirmed their view that the main objective of GPFRs is to "provide information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity" (IASB, 2010:§OB2,). This represents a clear statement of support for the decision-usefulness theory of accounting by two of the largest accounting bodies in the world. In line with this, this study adopts the decision-usefulness theory of accounting as a starting point.

Bebbington, Gray and Laughlin (2001:418, cited in Deegan, 2010:12), Belkaoui (2004:343-345), and Wolk *et al.* (2004:179) suggest that decision-usefulness theories of accounting can be classified into two branches. The division is illustrated in the schematic presentation in Figure 2.1, below.

Figure 2.1: Branches of decision-usefulness theories of accounting



Source: Own schematic presentation

If the emphasis is placed on **decision-makers**, one possibility illustrated in Figure 2.1, research is undertaken in which users of financial information are asked what information they would want to be presented in financial reports. Once the information required by the users has been ascertained, the information that users want is then prescribed and provided to users of financial statements. Most of this type of research would be questionnaire-based (Deegan, 2010:13). Another version of this type of prescriptive research, which Belkaoui

(2004:343) calls the "decision-usefulness/decision-maker/aggregate-market-behavior (sic) paradigm" is security price research, where it is assumed that if the market reacts to any information provided, the information must be useful. Gonedes and Dopuch (1974) are considered to be the pioneers of this type of research (Belkaoui, 2004:343; Deegan, 2010:13), which is based on the Efficient Markets Hypothesis (Deegan, 2010:13). In the case of IRs, security price research is often used to illustrate the usefulness of interim financial information via market reaction linked to specific disclosures.[15] The majority of the **secondary research objectives** of this study[16] were met by applying the decision-makers' emphasis in decision-usefulness theory, using a questionnaire which is also typical of positive research. The current study, amongst other things, therefore aims to determine whether individual shareholders use IRs for investment decision purposes.

By contrast, in studies where the emphasis is placed on **decision models** (the other possibility in Figure 2.1), researchers such as Beaver, Kennelly and Voss (1968:678), Chambers (1955:25) and Sterling (1972:200) have developed models based on the researchers' perceptions of what is necessary to facilitate effective decision-making. The theoretical frameworks pursued in *A Statement of Basic Accounting Theory* and the Trueblood Report (see Section 2.5.1.1) subscribe to the decision-models emphasis (Wolk *et al.*, 2004:179). Two assumptions underpin this branch of decision-usefulness theories, namely that all classes of stakeholders have identical needs, and that decision-makers may need to be taught how to use the information provided to them, if they are not familiar with how to do so (Belkaoui, 2004:342; Deegan, 2010:13). Glautier *et al.* (2011:44) and Staubus (1999:159) show that a decision-models approach in decision-usefulness theories is used in developing conceptual frameworks. Deegan (2010:12) and Wolk *et al.* (2004:41) believe that these frameworks are normative accounting theories. The normative nature of conceptual frameworks arises from the fact that these frameworks are prescriptive in nature, as they prescribe when, for instance, financial information would be considered useful. The **primary research objective** of this study was investigated using this emphasis in decision-usefulness theory, since it focuses on one specific prescribed qualitative characteristic of useful financial information in IRs.

In view of the fact that this study deals with whether individual shareholders understand the context and content of IRs, and since understandability is one of the prescribed qualitative

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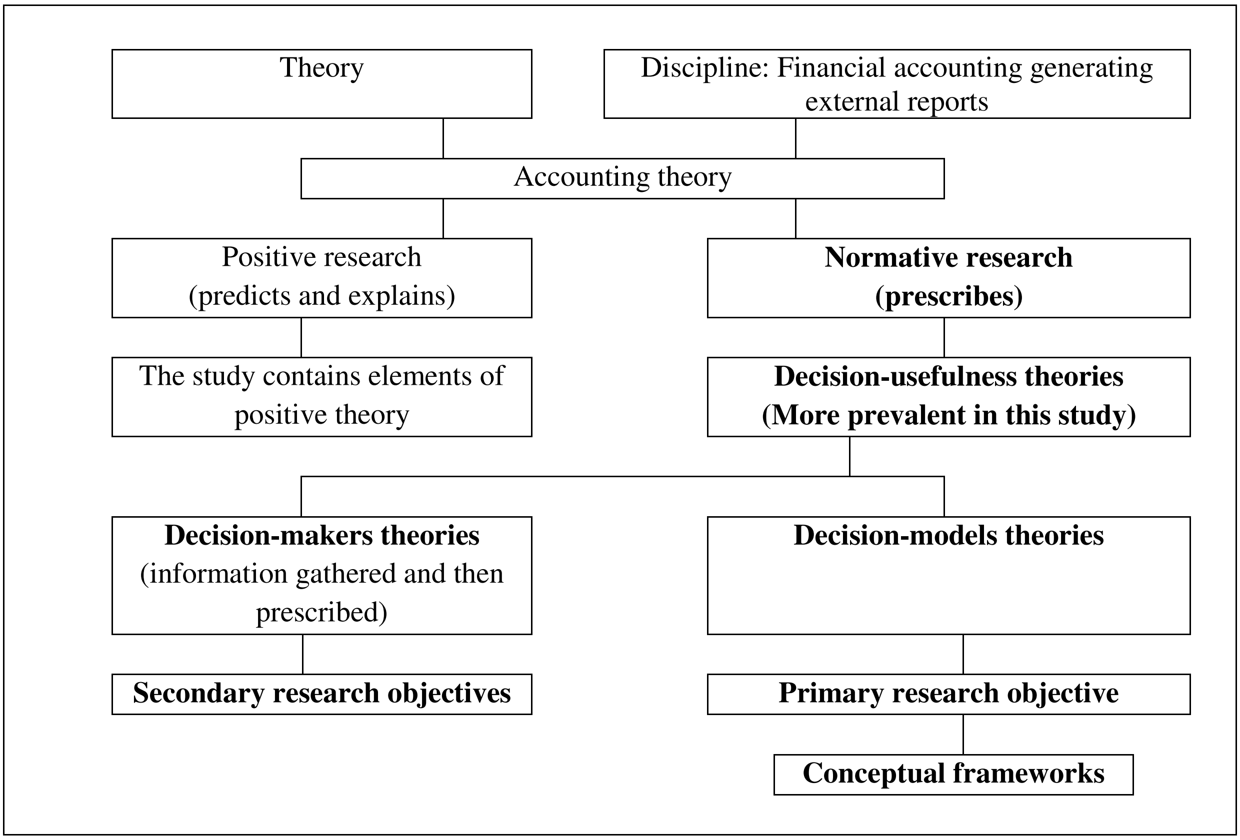
[15] See Section 2.6.3.1 below.
[16] See Section 1.5.2.

characteristics that improve the usefulness of financial reports, conceptual frameworks are considered as one form of normative decision-usefulness theory in the next section. However, if one aligns the research objectives in this study with the two branches of decision-usefulness theory in Figure 2.1, above, without focusing on conceptual frameworks at this stage, it would appear that both are used to address the primary and secondary research objectives listed in Section 1.5. The assessment of understanding is grounded in the 1989 IASB and 2010 IASB/FABS Frameworks, and consequently the decision-models emphasis and conceptual frameworks are used mainly in relation to the primary research objective that respect, while most of the secondary objectives of the study would focus on the decision-makers emphasis, where users are asked what they need in financial information to enable them to make economic decisions. The theories used in the study are summarised in Figure 2.2, below.

Figure 2.2: Overview of theories



Source: Own observation

2.5 CONCEPTUAL FRAMEWORKS

2.5.1 Towards conceptual frameworks

According to Deegan (2010:211), the first conceptual framework of accounting was developed by the FASB; it was defined as "a coherent system of interrelated objectives and fundamentals that is expected to lead to consistent standards" (Deegan, 2010:211). This definition of a conceptual framework is very closely aligned to Hendriksen's (1970) definition of accounting theory, and thus confirms the earlier argument (see Section 2.3) that a conceptual framework represents a normative theory of accounting. According to Macve (2010:305), since the conceptual framework of the FASB was a document that played a key role in directing the development of other conceptual frameworks, its development and other projects that may have had an impact on it are now elaborated on.

As part of the early search for a conceptual framework by the Accounting Principles Board (hereafter APB) which was later replaced by the FASB, two well-known American studies were released by Moonitz in 1961 and Sprouse and Moonitz in 1962 of the Accounting Research Division of the American Institute of Certified Public Accountants (hereafter AICPA) (Deegan, 2010:215; Storey & Storey, 1998:34). Unfortunately, their normative proposals were rejected by the Certified Public Accountants (hereafter CPA) profession as being too different from the generally accepted practices at the time. In response, the AICPA commissioned Grady to develop a theory of accounting. Grady's work was released in 1965. He developed an accounting theory based on a description of existing practice, and his work was not controversial; therefore it was acceptable to the CPA profession. This eventually resulted in the publication by the APB in 1970 of the highly influential Statement No. 4, *Basic Concepts and Accounting Principles Underlying the Financial Statements of Business Enterprises* (Deegan, 2010:215; Storey & Storey, 1998:40). The acceptance of this uncontroversial accounting pronouncement indicated that any frame of reference to be developed should be based on established concepts and principles that are accepted by the accounting profession and other interest groups. This view was reiterated by Belkaoui (1992:178, 2004:163) more than two decades later.

According to Belkaoui (2004:163), a statement of objectives of financial statements had for some time been seen as essential to creating an acceptable platform for establishing concepts and principles that would guide the debate over alternative standards and reporting techniques. As early as in 1960, Devine (1960:399) argued that

> …the first order of business in constructing a theoretical system for a service function is to establish the purpose and the objectives of the function. The objectives and purposes may shift through time, but for any period, they must be specified or specifiable.

The awareness of the importance of clear objectives in formulating a coherent accounting theory system prompted the US, the UK and Canada to launch a number of studies to identify at least what the objectives of financial statements should be, with a view to eventually establishing their own conceptual frameworks. Examples of some of the more important pioneering studies focusing on the objectives of financial statements and other matters related to conceptual frameworks are the Trueblood Report in the US, the Corporate Report in the UK, as well as *Corporate reporting: its future evolution* in Canada. Belkaoui (2004:197) suggests that the reports listed here form part of a sequential process that would eventually culminate in the formulation of conceptual frameworks to guide accounting techniques and standards in these three countries. Several findings of these reports, particularly regarding the objectives, the users, the qualitative characteristics and the understandability (linked to understanding) of financial reports, are relevant to this study and are therefore briefly focused on below in respect of each individual report.

2.5.1.1 The Trueblood Report, produced in the US (AICPA, 1973)

The Study Group on Objectives of Financial Statements was commissioned by the AICPA in 1971 after the AICPA had been criticized for the "lack of any real theoretical framework" (Deegan, 2010:216). The report, released in 1973, became known as the Trueblood Report, after its chairman, Robert M. Trueblood, and is referred to as such hereafter.

In line with the main objective of the study group, namely to identify the objectives of financial statements, Chapter 11 of the Trueblood Report summarises the 12 objectives of financial statements identified by the committee (AICPA, 1973:61-66).

- **Objectives**

  The Trueblood committee re-emphasizes that the basic objective of financial statements is providing information that is useful for making economic decisions (AICPA, 1973:13) and uses the word "useful" in no less than nine of the 12 objectives (AICPA, 1973:61-66).

In Chapter 2 of the Trueblood Report, it is stated that the objectives of financial statements to be formulated in terms of this report focus on the needs of users who rely mainly on financial statements as a source of information for decision-making, but that they should also meet the needs of other users. Although the development of electronic and other media has proliferated since 1973, and users today would thus have access to much more information than only financial statements, the Trueblood Report specifically defines the objectives of financial statements in the context of the circumstances that prevailed at the time of writing (AICPA, 1973:17).

- **Users**

The Trueblood Report identifies two user groups of financial statements, namely potential and current investors and creditors (viewed broadly) (AICPA, 1973:18). Hence, in this study, apart from the understanding of IRs, individual shareholders (current investors) and their use of IRs for investment decisions are investigated.

- **Qualitative characteristics and understandability**

In Chapter 10 (AICPA, 1973:57-60), **seven** qualitative characteristics that financial statements should possess to satisfy the needs of users are proposed. Decision-usefulness is reiterated as a main objective of financial statements, and the report addresses GPFRs as discussed earlier; in addition, the seven qualitative characteristics identified in the Trueblood Report are important. These qualitative characteristics are relevance and materiality, form and substance, reliability, freedom from bias, comparability, consistency and **understandability**. Given the topic of the study, understandability as addressed in this report is elaborated on below.

In addressing **understandability**, the Trueblood Report states that accounting information should be presented in such a manner that it can be understood by **both** reasonably well-informed and sophisticated users. This supports the notion in this study that assessing whether individual shareholders **understand** IRs should provide insight into the understandability of IRs as GPFRs. The report also indicates that merely simplifying financial information may not be sufficient to increase its understandability, and that the nature and circumstances of what is being communicated dictates the level to which the information can be simplified. It also proposed that the simplification of financial information to facilitate understanding should not lead to the omission of information that could be relevant to sophisticated users, merely because unsophisticated users may be less able to understand such items (AICPA, 1973:60).

- **The Trueblood Report's contribution to the US's (FASB's) Conceptual Framework**

The Trueblood Report constitutes the point of departure for the drafting of the ground-breaking conceptual framework developed by the FASB (Sutton, 2009:49). According to Deegan (2010:217), the FASB issued its first Statement of Financial Accounting Concepts (hereafter SFAC) in 1978 as SFAC No. 1: *Objectives of Financial Reporting by Business Enterprises*. This was followed by the release of another six SFACs. The last such SFAC, addressing cash flow information and present value in accounting measurements, was issued in 2000.

2.5.1.2 The Corporate Report produced in the UK (ICAEW, 1975)

- **Objectives**

The Corporate Report's objective was to "re-examine the scope and aims [objectives] of financial reports in the light of modern needs and conditions" (ICAEW, 1975:1). Similar to the Trueblood Report, the Corporate Report concludes that corporate reports should communicate information that is useful to those parties that have a reasonable right to such information (ICAEW, 1975:17). However, the Corporate Report is concerned with general purpose **reports**, "designed for general purpose use" (ICAEW, 1975:16), whereas the Trueblood Report refers to financial statements in particular. GPFRs would, as a wider concept, therefore include general purpose financial statements (in line with the Trueblood Report) as well as other narrative and descriptive statements (ICAEW, 1975:9).

- **Users**

The Corporate Report identifies seven groups that use corporate reports, namely equity investors, loan creditors, employees, analysts/advisors, business contacts, the government and the public (ICAEW, 1975:17). This differs from the broadly defined two user groups of financial statements identified in the Trueblood Report. However, the users listed do overlap, specifically regarding investors and creditors. Individual shareholders (from the equity investor user group) and their use of IRs for investment decisions are investigated in the current study.

- **Qualitative characteristics and understandability**

The Corporate Report states that to be useful and meet their fundamental objective, corporate reports should possess a number of desirable characteristics: reports should be relevant, **understandable**, reliable, complete, objective, timely and comparable (ICAEW, 1975:28). Although the qualitative characteristics mentioned in the Trueblood Report are not identical to the characteristics listed in the Corporate Report, similarities between the items are evident. As in the Trueblood Report and in line with the topic of the study, **understandability** or "being understandable" is explored in more detail, based on the content of the report.

The Corporate Report indicates that understandability and simplicity are not synonyms, as complex economic activities may not allow a discussion in elementary terms. Nevertheless, judgement should be exercised to ensure that all material matters are addressed, but, at the same time, users should not be confused with too much detail.

Ironically, this precise point about too much detail is again raised more than three decades later in the document *Integrating the business reporting supply chain* ,[17] which states that one of the significant unresolved issues in the business reporting supply chain is that the usefulness of business reports is reduced by "complexity and disclosure overload" (IFAC, 2011:8) and that "it is crucial that financial reporting becomes more relevant and understandable to various users" (IFAC, 2011:2).

According to the Corporate Report, understandability or being understandable means that all the information that a reasonably informed user could make use of should be provided in a form that would facilitate clarity as far as possible, while at the same time also presenting the main features to be used by a less sophisticated user. This means that judgement should be exercised when considering whether users will understand the financial information that is presented (ICAEW, 1975:28,29).

[17] See Section 1.2.

- **The Corporate Report's contribution to the UK's (ASB's) Conceptual Framework**

The Corporate Report provided a starting point for research on a conceptual framework in the UK (Deegan, 2010:218), and it was followed by other reports such as *Making corporate reports valuable*, which was issued by The Institute of Chartered Accountants of Scotland in 1988. The conceptual framework of the UK was eventually published by the ASB in December 1999 as the *Statement of Principles for Financial Reporting* (ASB, 1999).

2.5.1.3 The Stamp Report, produced in Canada (CICA, 1980)

- **Objectives**

The study *Corporate reporting: its future evolution* was commissioned by the Research Department of the Canadian Institute of Chartered Accountants (hereafter CICA) in 1980. It later became known as the Stamp Report after the chairman (Professor Edward Stamp) of the committee that prepared the report. The author of the Stamp Report was also part of the team who wrote the Corporate Report, and this could explain some of the similarities between the two reports. The committee preparing the Stamp Report was tasked to address the following matters, amongst others (CICA, 1980:Foreword):

- identify the user groups who may lay claim to corporate information; and
- examine the objectives of corporate reports published in the private sector.

In view of the above, the terms of reference of this committee were broadly in line with those of the Trueblood and the Corporate Reports, although this report was published much later (in 1980) than the other two reports (published in 1973 and 1975 respectively). As in the other two reports, it was concluded that corporate financial reporting should provide information that is useful to those making investment decisions (CICA, 1980:32). Furthermore, the Stamp Report concludes that, since various user groups use financial statements, it is necessary that "the general purpose financial statements achieve the right balance between the often conflicting interests of the various groups of users" (CICA, 1980:24).

- **Users**

In contrast with the modest numbers of users of financial statements specified in the Trueblood and Corporate Reports, the Stamp Report identified fifteen user groups: shareholders, long-term creditors, short-term creditors, analysts and advisors, employees, non-executive directors, customers, suppliers, industry groups, labour unions, government departments and ministers, the public, regulatory agencies, other companies, standard setters and academic researchers. Although this report identified a more comprehensive list of users, there is once again overlap between the identified users; as in the Trueblood and Corporate Reports, shareholders (current and potential) are included among the users identified, as do creditors and employees (CICA, 1980:43,44). Individual shareholders, the users focused on in this study, are again among the users identified in the Stamp Report.

- **Qualitative characteristics and understandability (clarity)**

In respect of qualitative characteristics, it is difficult to compare the Trueblood, Corporate and Stamp Reports directly, since the Stamp Report provides a list of characteristics that are not wholly in line with those mentioned in the two earlier reports. The main characteristics listed are relevance, comparability, timeliness, clarity, completeness, objectivity, verifiability and precision (CICA, 1980:55). The term "**understandability**" does not feature in the Stamp Report, although the matter is addressed in the report, and the characteristic of "clarity" may be regarded as overlapping with the characteristic of understandability. The report states that financial statements are not meant for laymen, because even accountants and financial experts sometimes have difficulty in understanding them, and that users should either receive training in how to understand statements or should consult with analysts or advisors. However, this does not detract from the argument that clarity is a crucial characteristic of financial statements (CICA, 1980:37).

- **The Stamp Report's contribution to the Canadian Conceptual Framework**

The Stamp Report laid some of the groundwork for a conceptual framework for Canada, and the concepts contained in the report were incorporated into the Canadian conceptual framework, *Financial Statement Concepts*, issued in 1991 (Deegan, 2010:219).

2.5.2 Common ground between and criticism of the conceptual frameworks of prominent Anglophone countries

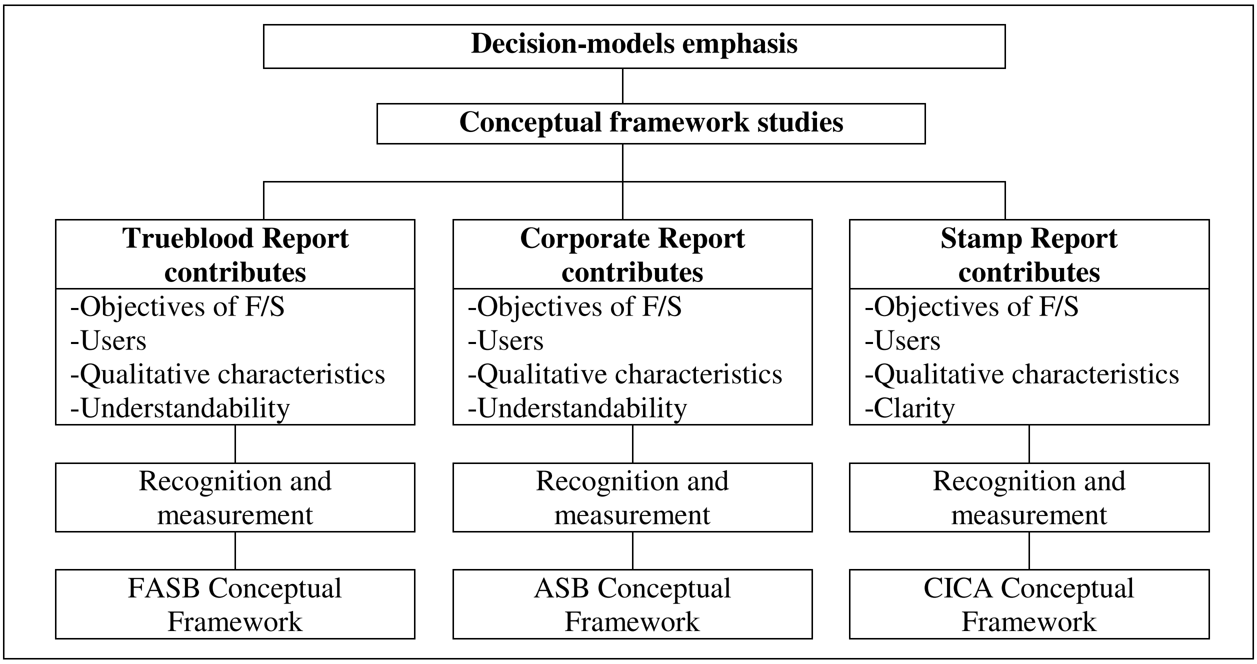
In addition to the US, Canada and the UK, as already mentioned above, which published their conceptual frameworks earlier (the US was the first to do so, followed by Canada and then the UK), a number of other countries also published conceptual frameworks/concept statements. In particular, Australia and New Zealand published their conceptual frameworks in more or less the same period (Scott, 2002:164). Page (2005:566) comments that it appears that the "urge to search for a conceptual framework proved irresistible to standard setters in the English-speaking world". The five countries listed here were known as the G4 + 1 working group (Scott, 2002:164), and they lobbied and laboured toward a set of international accounting standards for a long time.

Page (2005:566), Scott (2002:164) and Solomon and Solomon (2005:23) claim that all conceptual frameworks/concept statements, including the 1989 IASB Framework, appear to be similar and address more or less the same matters (common ground), namely:

- the objectives of financial reporting (decision-usefulness as one objective in all cases);
- the identification of user groups (investors and creditors appear to be common users);
- the qualitative characteristics of accounting information (these are more or less similar);
- the elements of financial statements (these are similar); and
- recognition (these are more or less similar) and measurement rules (these are unsatisfactory).

The development of the conceptual frameworks in the US, the UK and Canada is summarised in Figure 2.3, overleaf.

Figure 2.3: Overview of content and development of conceptual frameworks in US, UK and Canada



Source: Own observation

Despite the similarities of the conceptual frameworks/concept statements prepared by the major English-speaking countries in the world, which may well point to general agreement on fundamental principles, all the conceptual frameworks produced, including the 1989 IASB Framework and in all probability also the 2010 IASB/FASB Framework in future, have elicited some criticism by a number of authors, such as Benston, Carmichael, Demski, Dharan, Jamal, Laux, Rajgopal, and Vrana (2007:238), Joyce, Libby and Sunder (1982:670), Peasnell (1982:255) and Solomons (1986:124), to name but a few. An article by Hines (1989:89) appears to summarize a main point of critique, stating that it would seem that "the major rationale for undertaking CFs (conceptual framework projects) was not functional or technical, but was a **strategic manoeuvre** for providing legitimacy to standard-setting-boards and the accounting profession during periods of competition or threatened government intervention".

2.5.3 The development of the 1989 IASB and 2010 IASB/FASB Conceptual Frameworks

South Africa, unlike the US, the UK and Canada as mentioned in Section 2.5.1, above, did not develop its own conceptual framework. Instead, in 1995, South Africa decided to adopt the accounting standards issued by the IASC (later renamed as the IASB), as well as the *Framework for the Preparation and Presentation of Financial Statements* (the 1989 IASB Framework) (Techtalk, 1995:4). This situation has not changed, except that the revised 2010 IASB/FASB Framework is now in force in South Africa, rather than the 1989 IASB Framework that was in force initially, when the decision was taken (IASB, 2010:Foreword). Since both the 1989 IASB and 2010 IABS/FASB Frameworks have been relevant to the South African standard setting environment over time, and the current study covers the period of transition from one to the other, the development of these two frameworks is examined briefly below.

According to Whittington (2008:498), the IASC drew heavily on the FASB Framework (see Section 2.5.1, above, where the FASB Framework is identified as the first conceptual framework) in developing the original 1989 IASB Framework, but the end result is a much briefer document. The FASB Framework consists of a number of chapters (SFACs), while the 1989 IASB Framework is a single concise document. Camfferman and Zeff (2007:752, cited in Le Manh & Ramon, 2010:10) point out that it is generally admitted that the IASB Framework was derived from the FASB's Conceptual Framework. Indeed, Macve (2010:305) even goes as far as to refer to the ASB and 1989 IASB Frameworks as "subsequent imitations" of the FASB Framework.

By the time that the 1989 IASB Framework was issued, the FASB had already issued six of the seven SFACs that would eventually comprise the entire framework project of the FASB. Since the G4 + 1 were key supporters of the objective to create a single set of international accounting standards at the time when the IASB Framework was developed (see Section 2.5.2), it stands to reason that their contributions to the final IASB Framework document were affected by their involvement in the development of their own conceptual frameworks. Consequently, the comments by Macve (2010), Whittington (2008), Camfferman and Zeff (2007) (cited in Le Mahn and Ramon, 2010) cited above appear to be justified.

As mentioned earlier in this section, the 1989 IASB Framework is currently in the process of being reviewed by the IASB and the FASB in a joint project that originated from the agreement to converge the standards of the IASB and the FASB that Sir David Tweedie (chairman of the IASB at that time) and Robert Herz (chairman of the FASB at that time) reached at Norwalk in 2002 (Burkholder, 2011:658; Cheney, 2005:12). The final version of the revision will probably contain elements of both the 1989 IASB Framework and the 1970

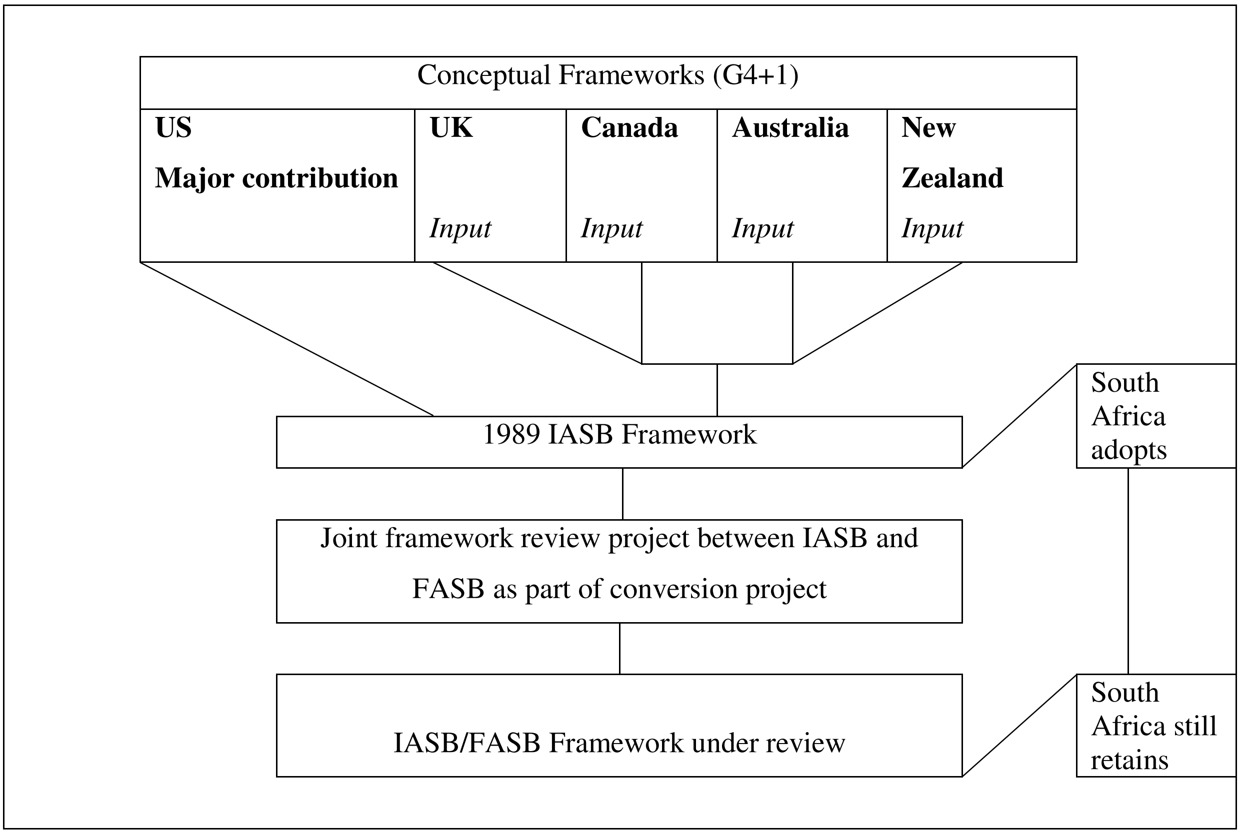
FASB Framework as the two major standard-setting bodies in the world work towards issuing a single complete conceptual framework at some date in the future. Heathcote and Human (2008:24) also confirm that this revision was part of a joint project of the IASB and the FASB to update and harmonize some of the existing standards. This project is dealt with in phases (chapters) and once each additional chapter is completed, the paragraphs in the 1989 IASB Framework, dealing with the corresponding issue, are replaced by the new chapter.

At this stage, only Chapters 1 and 3 of the 2010 IASB/FASB Framework have been completed. These chapters deal with "The objective of general purpose financial statements" and "Qualitative characteristics of useful financial information" respectively. The content of the "Introduction, purpose and status" and the scope paragraph of the Framework have merely been updated, but have not been revised substantially as yet. It therefore still appears at the beginning of the 2010 IASB/FASB Framework, while the rest of the 1989 IASB Framework remains in force until the relevant phases are completed, and the rest is thus currently still included in the 2010 IABS/FASB Framework as Chapter 4 (IASB, 2010:Foreword).

Since the 1989 IASB Framework was and the 2010 IASB/FASB Framework is in use in South Africa, the concepts and principles that are contained in these frameworks and that are relevant to this study are addressed in more detail below. Included in the discussion are the objectives of GPFRs, the users of these reports and the qualitative characteristics that enhance the usefulness of financial reports. Due to its centrality to the study, understandability is addressed in a separate section.

To summarize, the chronological development of the 1989 IASB and 2010 IASB/FASB frameworks are set out in Figure 2.4, overleaf.

Figure 2.4: Chronological development of the 1989 IASB and 2010 IASB/FASB Frameworks



Source: Own observation

2.6 THE 1989 IASB AND 2010 IASB/FASB FRAMEWORKS

2.6.1 Objectives of GPFRs

The following two quotations from the two conceptual frameworks in force in South Africa during the compilation of this study set out the objectives of GPFRs, as defined in these frameworks and considered in Section 1.2:

> The objective of [general purpose] financial statements is to provide information about the financial position, performance and cash flows of an entity that is useful to those users in making economic decisions. (IASC, 1989:§12)
>
> The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity. These decisions involve buying, selling or holding equity and debt instruments and providing or settling loans and other forms of credit. (IASB, 2010:§OB2)

From the two quotations above, it is clear that financial information provided in GPFRs should be useful to users when they are making economic decisions. For the purposes of this study, these two quotations are relevant to the study's secondary objectives (related to whether IRs are used for investment decisions).

2.6.2 Users of general purpose financial reports

In the 1989 IASB Framework, the IASC provided a list of several users of financial statements (IASC, 1989:§9), but concluded that GPFRs (including IRs) that meet the needs of investors (shareholders in the case of a company) would also meet the needs of the majority of other users of financial statements (IASC, 1989:§10). The same point of departure was used when the current study was initially planned, and it was decided to focus on individual shareholders in executing the study.

However, subsequent to the initial design of the study, the section of the 1989 IASB Framework that focused on the scope, on providing in the financial information needs of users, users and the objective of financial statements, was replaced by Chapter 1 of the 2010 IASB/FASB Framework. A comparison of the relevant sections of the two frameworks indicates that during the revision, the IASB moved away from providing an extensive list of users, as well as the assumption that meeting the financial information needs of investors would also satisfy the needs of the other users listed in the 1989 IASB Framework. Instead, a primary user group of GPFRs was identified – this group includes investors, lenders and other creditors (existing and future) (IASB, 2010:§OB2,§BC1.10). The new thinking introduced in the 2010 IASB/FASB Framework thus increases the range of users for whom understanding and investment decision applicability can be investigated from investors only to investors, lenders and creditors. This necessitated a reconsideration of the user group to be targeted in this study.

After due consideration, it was concluded that, since the identities of lenders and creditors of companies are not available in the public domain, it would be impracticable to use them as a user group in a questionnaire-based study. Hence, individual shareholders as the investor target (user) group were retained for this questionnaire-based study (see Section 1.4.1).

2.6.3 Qualitative characteristics that enhance the usefulness of financial information

In Section 1.2, it was pointed out that shareholders (the investor user group) in particular are assumed to use ARs and IRs for making economic decisions. This raises a number of questions as to which attributes or characteristics of financial statements would make these two types of GPFRs useful to shareholders, whether shareholders would find the ARs and IRs useful, and whether they would use them for decision-making purposes.

2.6.3.1 Research on whether financial information is useful for decision-making

Several international studies using surveys have been conducted to confirm that the information presented in ARs (corporate or annual reports) is indeed used, or is useful. Examples of relatively recent international studies in this regard include

- Lee and Tweedie's (1977) study on usefulness for individual (private) shareholders in the UK;
- Chang and Most's (1985) research on usefulness for individual and institutional investors, as well as financial analysts, in the US;
- Epstein and Pava's (1993) work relevant to individual shareholders in the US;
- Anderson and Epstein's (1996) study relating to individual shareholders in Australia, New Zealand and the US;
- Bartlett and Chandler's (1997) work relating to individual shareholders in the UK; and
- Naser, Nuseibeh and Hussaini's (2003) research on eight user groups including individual and institutional investors in Kuwait.

In South Africa, only two studies (both focusing on institutional investors) addressing the usefulness of ARs (to some extent) have been published thus far:

- a study by Flynn (1987) on the perceptions regarding the sources of information of South African institutional investors was conducted before the release of the 1989 IASB Framework or the 2010 IASB/FASB Framework in South Africa and deals with the sources of information used by institutional investors; and
- a study by Stainbank and Peebles (2006) was conducted subsequent to the issuing of the 1989 IASB Framework, but before issuance of the revised 2010 IASB/FASB Framework; it addressed the perception of usefulness of ARs according to preparers and institutional investors in South Africa and briefly touched on qualitative characteristics in terms of the 1989 IASB Framework.

The above international and South African studies all conclude, to a varying extent, that ARs are useful, and by implication, that shareholders would therefore use them.

In respect of IRs, it also appears as if their usefulness is not in doubt, as illustrated by a number of international studies, the more recent of which those by Alves and Dos Santos (2005:27), Butler *et al*. (2007:26), Cornell and Landsman (1989:69), Han (2010:107), Gajewski and Quèrè (2001:701), Hiesh, Jerris and Kross (1999:331), Jones and Bublitz (1990:564), Landsman and Maydew (2002:807), Lunt (1997:35), Mangena (2004:17), and Opong (1995:278). In these studies, the usefulness of IRs can be deduced from the fact that financial markets react to the publication of IRs, that stock (share) prices are sensitive to the financial data contained in IRs, and that investment analysts and fund managers use IRs for the evaluation of a company's shares.

It can thus be concluded that a large body of research in countries other than South Africa has shown that users find both ARs and IRs useful and may use them for making decisions to buy, sell or hold equity and debt instruments, or providing or settling loans and other forms of credit and the like. In South Africa, however, only a limited body of research on the usefulness of ARs to preparers and institutional investors is available, and it appears as if nothing is available in respect of the usefulness of ARs to individual shareholders, or the usefulness of IRs to any type of user, individual, institutional or otherwise. From the literature review conducted in respect of the use or usefulness of IRs, it became evident that, to date, no peer-reviewed questionnaire-based study in respect of the use or usefulness of IRs has been conducted in South Africa.

The lack of research on the use and usefulness of IRs in South Africa posed the question of whether South African users of IRs use them for making investment decisions and by implication thus find them useful. This informed the decision to focus in this study on the use of IRs in South Africa, rather than the usefulness of ARs in South Africa, which has been addressed, albeit to a limited extent. The term "usefulness" in the accounting field, as well as what contributes to financial information being more useful, is investigated further with reference to the 1989 IASB Framework and the 2010 IASB/FASB Framework.

2.6.3.2 Attributes contributing to the usefulness of financial statements/reports

As is clear from the discussion in Section 2.5, above, each of the major accounting bodies in the Anglophone world has attempted in the last fifty years to identify the characteristics of financial statements that contribute towards making financial information useful, when making either economic decisions or decisions on the allocation of resources to an entity. Examples of high profile professional accounting bodies involved in accounting framework projects during the period mentioned include the FASB, the ASB, the CICA and the IASC and its successor, the IASB, in co-operation with the FASB.

Since both the 1989 IASB Framework and the 2010 IASB/FASB Framework were in force in South Africa during the course of the study, the attributes contributing to the usefulness of financial statements are addressed from the perspective of both these frameworks, which were adopted *verbatim* in South Africa.

Both the 1989 IASB Framework and 2010 IASB/FASB Framework indicate that the usefulness of financial information is enhanced when it has certain attributes or characteristics. These characteristics are collectively referred to as qualitative characteristics in both these frameworks, and both frameworks include a reference to understandability or the fact that financial information should be understandable.

Amongst other aspects, the 1989 IASB Framework (IASC, 1989:§5) deals with those qualitative characteristics "that determine the usefulness of information in [general purpose] financial statements". The qualitative characteristics are those "attributes that make the information provided in financial statements useful to users" (IASC, 1989:§24). The four principal qualitative characteristics of financial statements identified in the IASB Framework are understandability, relevance, reliability and comparability (IASC, 1989:§24) and these are presented schematically in Figure 2.5, overleaf.

Figure 2.5: 1989 IASB Framework qualitative characteristics and related research

	Qualitative characteristics			
	All four at the same level			
	Understandability	**Relevance**	**Reliability**	**Comparability**
Level 1	*Very little research,* ***but will be addressed in this study***	*Well-researched*	*Well-researched*	*Very little research, and will* ***not*** *be addressed in this study*

Source: Own observation

In the 2010 IASB/FASB Framework, financial information is considered useful if such information is relevant, as well as faithfully represents what it purports to present (this is similar to being reliable) (IASB, 2010:§QC4) – relevance and faithful representation are thus identified as **fundamental** qualitative characteristics of financial information. In addition to the fundamental qualitative characteristics, the 2010 IASB/FASB Framework states that financial information becomes more useful (its usefulness is enhanced) if it is also comparable, verifiable, timely and understandable – these traits are now identified as **enhancing** qualitative characteristics. See Figure 2.6, overleaf, for a schematic presentation of the qualitative characteristics contained in the 2010 IASB/FASB Framework.

Figure 2.6: Qualitative characteristics included in the 2010 IASB/FASB Framework

Qualitative characteristics

Level 1

Fundamental qualitative characteristics	
Relevance *Well-researched*	Faithful representation *Well-researched*

Level 2

Enhancing qualitative characteristics			
Comparable *Very little research, and* ***not to be addressed in this study***	Verifiable #	Timely #	**Understandable** ***To be addressed in this study***

\# Introduced in IASB/FASB Framework

Source: Own observation and interpretation of the 2010 IASB/FASB Framework

A comparison between the qualitative characteristics addressed in both the 1989 IASB Framework and the 2010 IASB/FASB Framework shows that the two-level view of the hierarchy of qualitative characteristics in the 2010 IASB/FASB Framework represents a departure from the position in the 1989 IASB Framework, where a total of only four qualitative characteristics are identified and ranked at the same level of importance (see Figure 2.5). As can be seen in Figure 2.6, two additional qualitative characteristics (apart from the characteristics of relevance, reliability/faithful representation, understandability and comparability, which all remained in force) have crystalized, namely "verifiability" and "timeliness". "Verifiability" refers to information that can be used with confidence. This appears to be a new characteristic, but that is not the case, as it was formerly covered by the phrase "can be depended upon by users" under the former qualitative characteristic of "reliability" in the 1989 IASB Framework. The same applies to the characteristic "timeliness", which appeared in the 1989 IASB Framework as a constraint that could have a negative impact on "relevance". It appears that both these "additional" characteristics were in fact addressed in the 1989 IASB Framework, but that they are now separated from two of the former qualitative characteristics, which have been reclassified as fundamental qualitative characteristics.

Therefore, irrespective of whether the 1989 IASB Framework or the 2010 IASB/FASB Framework is used as a point of departure when considering usefulness, the usefulness of information provided in ARs and IRs (both GPFRs), is affected by the two fundamental qualitative characteristics (relevance and faithful representation) and the four enhancing qualitative characteristics, which are comparability, verifiability, timeliness and understandability (IASB, 2010:QC4). Although the fundamental qualitative characteristics have to be met to ensure that financial information is useful, there is no prescribed order which must be followed in considering the qualitative characteristics (Level 2) that enhance usefulness, because these characteristics tend to interact with each other when they are applied to different sets of financial statements.

2.6.3.3 Research on qualitative characteristics in respect of IRs

In view of the decision to focus on IRs in this study, the existing literature on the qualitative characteristics mentioned in Section 2.6.3.2 was reviewed. Since the 2010 IASB/FASB Framework was released by the IASB only in September 2010, it is logical that only a limited amount of research focusing specifically on the two newly formulated qualitative characteristics (verifiability and timeliness) related to IRs has been published thus far. Most of the existing research therefore focuses on the four qualitative characteristics identified in the 1989 IASB Framework. In this context, then, the literature review on qualitative characteristics associated with IRs revealed two **main** areas of research on qualitative characteristics.

A debate arose as to whether IRs should be issued on a quarterly basis or not (Bagshaw, 2000b:40; Baron, 2002:1; Butler *et al,* 2007:26; Gajewski & Quèrè, 2001:701; Jackson, 2008:28; Wilde, 2005:40; Yee, 2004:189). The urgency of this matter receded with the issuance of Directive 2004/109/EC on 15 December 2004, stating that the EU has decided not to require listed companies to disclose financial information in the first and third quarters of a financial year (Alves & Dos Santos, 2005). This decline in urgency is obvious from the decrease in the number of articles published on this topic after 2005. Nevertheless, bearing in mind the publication dates of research on this topic, this area of research focuses on the qualitative characteristic of "**relevance**" in the 1989 IASB Framework, and is also concerned with the timely publication of financial information. In terms of the 2010 IASB/FASB Framework, this thus appears to link to the enhancing qualitative characteristic of "timeliness".

Another matter commonly addressed in the literature is whether IRs should be subject to a statutory audit or audit review, and what impact such an audit or review may have on IR (Bagshaw, 2000a:57; Carroll, 2000:15; Guan *et al.,* 2006:570; Han, 2010:2; Ketz & Miller, 1999:16). The existing research concludes that having either an audit or an audit review definitely contributes to the reliability of IRs, but is likely to influence the timeliness of these reports negatively. The main focus in this area of research is therefore the qualitative characteristic of **reliability**, which, based on a perusal of the 2010 IASB/FASB Framework, can be linked to the fundamental qualitative characteristic of "faithful representation".

The above indicates that at least two of the qualitative characteristics (relevance and reliability) of useful financial information contained in IRs have been researched extensively over time in the international arena, resulting in the conclusion that these qualitative characteristics are present in IRs and contribute to the usefulness of IRs.

In addition, the issuance of IAS 34 in 1998, nearly a decade after the issuance of the IASB Framework in 1989, is assumed to have enhanced the usefulness of IRs in line with one of the stated objectives of a conceptual framework, namely assisting standard-setters in developing a standard (Christiansen, 2010:287; Dopuch & Sunder, 1980:5; Vorster, 2007:33).

In summary, it appears as if the majority of research on IRs focuses on two of the four qualitative characteristics identified in the 1989 IASB Framework as contributing to the usefulness of financial statement information, namely relevance and reliability.[18]

The other two qualitative characteristics identified in the 1989 IASB Framework, namely understandability (being understandable) and comparability, appear not to have been dealt with in research on IRs to the same extent. Since this study focuses on understandability, comparability is not pursued further.

[18] See Figures 2.5 and 2.6 above.

This lack of research on the understandability of IRs, the studies commissioned by the IFAC and the SEC (see Section 1.2) that highlighted problems with the understandability of financial reports as early as 2007 and 2008, and the advent of integrated reporting in South Africa with the proposal that financial information in these reports should be presented in the condensed format of financial statements prescribed for IRs in IAS 34, underpins the decision to focus on whether individual shareholders understand the context and content of IRs.

In this study, the qualitative characteristic of understandability was addressed by way of an assessment of whether individual shareholders understand the context and content of IRs. Subsequent to the three studies by IFAC (2008 to 2011) and the SEC (2008), two further studies (see Section 1.2) were published, both probing, amongst other matters, the understandability of financial information. This provided further impetus for the current study to focus on understandability; hence, the meaning of this term is investigated in the next section.

2.7 UNDERSTANDABILITY

Understandability as a term does not appear to have been well-defined in the conceptual framework documents of the IASB. Instead, rather broad descriptions of what it would entail are provided.

For instance, the 1989 IASB Framework states that an "essential quality of the information provided in financial statements is that it is readily understandable by users" (IASC 1989:§25). The more recent 2010 IASB/FASB Framework (IASB, 2010:§QC30), as part of its discussion of enhancing qualitative characteristics, states that "[c]lassifying, characterising and presenting information clearly and concisely make it *understandable*" (emphasis in the original). Since these two definitions relate to the understanding of financial information (GPFRs), the meaning of the word "understand" was investigated further.

According to the *Reader's Digest Great Illustrated Dictionary* (1984:1794), to "understand" means, amongst other things to "perceive and comprehend the nature and significance of", and to "grasp the meaning intended or expressed by another". If the term "understand" is related to the accounting environment and specifically the primary objective of this study, it would mean that users of IRs (individual shareholders) should perceive and comprehend the nature and significance of information contained in IRs, and also grasp the meaning intended or expressed by the preparers of the IRs – specifically the context and content of IRs in this study as described in the List of definitions of terms and concepts. Individual shareholders should thus **understand** the context and content of IRs. The interpretation in this study in relating the dictionary definition of understanding to accounting information is in line with a analysis by Eccles and Holt (2005:383) of the interpretation of understandability offered by the ASB of the UK. They indicate that understandability "requires that users are able to perceive the significance of information provided".

In conducting a review on the meaning of understandability in the academic literature available in the accounting field, it would also appear that interpretations of understandability are linked to the qualitative characteristic of understandability as defined by the various frameworks published by standard-setting bodies mentioned earlier, as well as the studies contributing to the publication of the conceptual frameworks.

As indicated in Section 2.5.3, South Africa adopted the accounting pronouncements of the IASB in 1995. Consequently, the views of the 1989 IASB Framework and the more recent 2010 IASB/FASB Framework are used as point of departure in this South African study when considering the qualitative characteristic of understandability.

In the second paragraph of this section, the explanations surrounding understandability of both the 1989 IASB Framework and the 2010 IASB/FASB Framework are provided. Both these frameworks indicate that the information must be understandable to users – users should thus be able to understand the information. However, both these conceptual frameworks introduce a *caveat* in respect of the level of knowledge of the assumed users.

The 1989 IASB Framework indicates that for the purpose of understandability, users are assumed "to have a reasonable knowledge of business and economics and accounting and a willingness to study the information with reasonable diligence" (IASC, 1989:§25). In the 2010 IASB/FASB Framework, the *caveat* in respect of who the users of GPFRs are is introduced once again by stating that the reports "are prepared for users who have a reasonable knowledge of business and economic activities and who review and analyse the information diligently" (IASB, 2010:§QC32).

Note that the original 1989 IASB Framework assumes that users are willing to study the information diligently, while the 2010 IASB/FASB Framework goes one step further and actually expects users to study it. One would like to believe that the original intention was always that users would actually study the financial reports, rather than merely being willing to do so – merely being willing and not actually studying the financial report before making a decision does seem to defeat the object.

In the context of this study, it can therefore be deduced that understandability implies that information contained in GPFRs must be understandable to individual shareholders or, to put it differently, that individual shareholders must be able to understand such information. This is the qualitative characteristic that ensures that individual shareholders comprehend the information and that it is therefore useful for making decisions (IASB, 2010:§BC3.40). Assessing whether users **understand** the context and content of IRs, as is done in this study, therefore provides an indication of whether the financial information presented in IRs are understandable.

It is also interesting to note that in SFAC No 2 of the FASB Framework, understandability was regarded as a "user-specific quality". However, Wolk *et al.* (2004:199) indicate that understandability is influenced by both the users and the preparers of financial reports. It appears from the 2010 IASB/FASB Framework that the FASB has now accepted that understandability is not merely a "user-specific quality", as it is no longer described as such in the joint 2010 IASB/FASB Framework.

Stevens, Stevens and Stevens (1992:372,373) state that communication between the reader and the preparer can only occur when there are pre-existing knowledge structures and a common language. They are of the opinion that when a topic is known to a reader, the reader's comprehension increases substantially.

When the above is considered in the context of this study and linked to the *caveats* introduced in both the 1989 IASB Framework and the 2010 IASB/FASB Framework, it follows that the level of prior knowledge of accounting (be that by way of a qualification held by the investor or by way of experience) of investors using IRs for investment decisions should translate into a higher level of understanding of the information (context and content) contained in IRs. This is considered in the analysis of the understanding of the context and content of IRs in Chapter 5 and is again commented on in Chapter 6.

In the next section, two other techniques frequently used by researchers to assess the understandability (readability and understandability) of information in ARs are considered.

2.7.1 Understandability versus readability: readability formulas and the Cloze procedure

It appears from the literature that for a number of years, it has been widely assumed that readability is equal to understandability, and that the readability of financial communication can thus be used to determine the comprehension levels required to understand such information (Iu & Clowes, 2004:5; Subramanian, Insley & Blackwell, 1993:51).

As a result, perusing the literature on readability and understandability (syntactical complexity) indicates that there are two techniques which are commonly used to assess readability and understandability, namely readability formulas and the Cloze procedure (Clatworthy & Jones, 2001:312; Noor, 1997:5). While readability formulas use word and sentence length to assess the ease with which a narrative text can be read (Courtis, 2004:297; Smith & Taffler, 1992:86), the Cloze procedure measures the level of interaction between readers of material and the material itself, and in doing so measures the difficulty of reading, as well as the level of comprehension of a narrative piece for a specific audience (Clatworthy & Jones, 2001:312; Stevens *et al*., 1992:373).

Although many assume that readability formulas and the Cloze procedure provide evidence of the difficulty of reading and comprehension of narrative pieces, Smith and Taffler (1992:91) are adamant that readability formulas should not be used to assess the understanding of narrative text in financial reports, as their research has shown that readability and understandability are different concepts. In considering the possibility of using these techniques to assess IRs in this study, it is crucial to remember that these techniques can only be applied to the **narrative information** contained in financial reports, and one is thus not able to subject the condensed financial statements as they mostly appear in the IRs to these tests.

A perusal of prior research on readability or understandability confirms that studies using these techniques focused on the narrative sections of annual and other reports, and in the vast majority of cases, the research on understandability was not conducted by means of questionnaires, but by means of techniques associated with the assessment of readability and understandability (David, 2001:201; Smith and Taffler, 1992:84-88). Only a small proportion of research has thus focused on the financial information contained in financial reports (specifically annual reports), as is done in this study. This type of research (understanding of financial information) is generally conducted via questionnaires or interviews containing multiple choice, true or false questions and open-ended questions. The most renowned study of this nature is that by Lee and Tweedie published in 1977.

In summary, despite their prevalence when assessing understanding, neither readability formulas nor the Cloze procedure could be used to assess the understanding of IRs in this study, because the context and content IRs as defined for this study included condensed financial statements, and excluded management commentary (narrative), since it is not standardised from one company to the next. For these reasons, the respondents' understanding of the context and content of IRs had to be assessed in another way, which is considered in Section 2.7.2, below.

2.7.2 Studies focusing on IRs and the understandability of the financial information contained in annual reports

A number of studies related to IRs were undertaken in the UK and the US from 1970 to 1999 to establish the purpose, uses, users, frequency, timeliness, level of auditor involvement, accounting issues, content, best practice and compliance with regulations. However, these studies on IRs did not focus on the understandability of IRs (Bagshaw, 1999; Edwards, Dominiak & Hedges, 1972; Hussey & Woolfe, 1994; Schiff, 1978). However, historical information emanating from these studies is referred to in Chapter 3, where the development of IRs is addressed.

Although there is a dearth of survey research on understandability of context and content in respect of IRs by means of questionnaires, a number of questionnaire-based surveys have been completed over the years dealing with three, or in some instances at least two, of the following matters: the understanding, perception of understanding and usefulness of information presented in ARs.

These studies include those by Lee and Tweedie in 1975 ("Accounting information: an investigation of private shareholder understanding"), in 1976 ("The private shareholder: his sources of financial information and his understanding of reporting practices") and in 1977

(*The private shareholder and the corporate report*), and by Naser, Nuseibeh and Hussaini in 2003 ("Users' perceptions of various aspects of Kuwaiti corporate reporting").

The above surveys were all based on the decision usefulness/decision-model theory or paradigm, departing from the premise that financial statements provide useful information and assist active investors in their buy/sell/hold decisions or have an impact on the markets. These studies also showed, as this one, some positivist characteristics. However, only the above-mentioned questionnaire-based studies addressed the understandability or perception of understandability of annual reports, while several other major studies addressed the usefulness of annual reports for making investment decisions by means of surveys in developed countries, such as the studies by Anderson and Epstein (1996), Bartlett and Chandler (1997), and Chang and Most (1985) and Epstein and Pava (1993). The absence of questionnaire-based research in respect of the understandability of the context and content of IRs and their use for investment decision-making in South Africa as well as the use of the format of IRs in the integrated reports of South African listed companies subsequent to 2010, provided an opportunity in this study to investigate this aspect further.

2.8 SUMMARY AND CONCLUSION

In this chapter, the theoretical grounding of the study has been considered. It was concluded that the accounting theory used in this study, namely the decision-usefulness theories of accounting, contains elements of both normative and positive theory. The use of a questionnaire to gather information to arrive at a description of what was observed in respect of the secondary research objectives also introduces positivist elements into the thesis, in conjunction with the decision-makers' emphasis on the decision-usefulness theories presented in Table 2.1.

Conceptual frameworks as a normative theory were used in addressing the primary objective of this study, which is to establish whether individual shareholders understand the context and content of IRs. In this regard, the qualitative characteristic of understandability as identified the 1989 IASB Framework and the 2010 IASB/FASB Framework is the focus of the study.

The standard techniques used to assess understanding and understandability of narrative information could not be used in this study for the reasons explained in Section 2.7.1. In view of this, the limited alternative methods available to assess understanding were considered in Section 2.7.2. It was concluded that the understanding of IRs could best be assessed using survey questionnaires, as also used in the studies by Lee and Tweedie and by Bartlett and Chandler to determine whether individual shareholders understand the context and content of ARs.

In the case of the secondary objectives (the investigation dealing with individual shareholders' use of IRs for investment decisions), the decision-makers emphasis of decision-usefulness theories which introduced certain positivist elements into the study were deemed more appropriate.

In Chapter 3, the development of interim financial reporting over time and its regulatory environment are considered, with specific reference to listings requirements, legal requirements and accounting pronouncements. This chapter thus provides a bridge between the accounting theories addressed here and the development of accounting pronouncements to embed the relevant accounting theory in practice.

CHAPTER 3: THE DEVELOPMENT OF INTERIM FINANCIAL REPORTING IN THE US, THE UK AND SOUTH AFRICA

3.1 INTRODUCTION

According to the IASC (1996:13), interim financial information represents financial information of an entity for less than a full financial year (a quarter or six months), or for a 12-month period ending on a date other than the financial year-end of the entity. This definition was eventually pared down in IAS 34 to financial information for a reporting period less than a full financial year (IASB, 2008:§4). The term is also explained in the List of definitions of terms and concepts provided with this study. The terms “quarterly reports”, “half-yearly reports” and “interim reports” are often used interchangeably for IRs.

As is indicated in Section 2.6.3.1, numerous prior studies indicate that interim financial reporting is useful to investors and creditors, and that financial markets react to the publication of interim financial information.[19] For example, Bagshaw (2000a:56) has concluded that interim information is price-sensitive.

The literature review (Hussey & Woolfe, 1994:27; IASC, 1996:19; Ottermann, 1991:47; Schiff, 1978:4) indicates that, globally, there are two distinct schools of thought on the accounting for interim financial reporting. Some believe that an IR should be prepared with the focus clearly on the fact that an interim period is an integral part of a financial year, rather than a reporting period in its own right – the integral approach. Others believe that an IR should be prepared by viewing any interim period as a “stand-alone” reporting period – the discrete approach. The two approaches are briefly compared and contrasted below.

3.1.1 The integral approach

According to the IASC (1996:18), Lunt (1982:25), Ottermann (1991:49) and Koen, Botha and Nieuwoudt (1999:4), the integral approach evolved from the view that IRs are meant to

[19] See Section 2.6.3.1.

supply users with information on what to expect for the current full financial year. IRs should therefore assist in **forecasting** what an entity's financial position and liquidity will be at the end of the current financial year.

When an integral approach is adopted, the accounting definitions and principles used for preparing information for reporting periods of a 12-month financial year have to be modified to accommodate the view that interim periods are part of a financial year and not stand-alone periods (Ottermann, 1991:48). This implies that the definitions of elements of financial statements as contained in the 1989 IASB Framework (IASC, 1989:§53-§80) and the 2010 IASB/FASB Framework (IASB, 2010: §4.8-§4.35) have to be reformulated to accommodate the preparation of IRs using this approach.

3.1.2 The discrete approach

The IASC (1996:19), Lunt (1982:33) and Ottermann (1991:55) explain that the discrete approach evolved from the view that each financial reporting period, irrespective of its length, represents a separate (discrete) or stand-alone financial period. This means that a reporting period shorter than a full financial year (12 months) does not require any modification of the accounting definitions and principles generally used when preparing financial statements for a full financial year (Koen *et al.*, 1999:4; Ottermann, 1991:48). IRs prepared using the discrete approach are intended to supply users with information to understand the earnings-generating and cash-generating capacity of an entity for a period better, irrespective of whether or not the period is shorter than a full financial year.

Under the discrete approach, the definitions of elements of financial statements as defined in the 1989 IASB Framework (IASC, 1989:§53-§80) and the 2010 IASB/FASB Framework (IASB, 2010:§4.8-§4.35) also apply to IRs when these are prepared. A further advantage of the discrete approach is that IRs prepared in terms of this approach can help users to identify turning points in an entity's earnings and liquidity on a timely basis, while the integral approach tends to smooth away the turning points by viewing the financial year as the main period and the interim period as a subset of that financial year.

The above discussion on the two possible approaches to interim financial reporting provides an essential framework for the subsequent overview of the development of IRs. Preparers of

IRs generally follow one of these two approaches, and different jurisdictions use different approaches.

3.2 HISTORICAL OVERVIEW OF THE DEVELOPMENT OF IRS

In this chapter, the historical development of IRs from the beginning of the 20th century is considered. Developments in the US, in particular relating to the New York Stock Exchange (hereafter NYSE), the UK and South Africa, with specific reference to listed companies, are summarised.

Developments in the US and the UK are also addressed in this study for the following reasons:

- These countries have committed themselves to either adopting International Accounting Standards (IASs) or International Financial Reporting Standards (IFRSs), in the case of the UK and South Africa, or, to converge (harmonize) with IASs and IFRSs, in the case of the US (Schipper, 2005:101; SEC, 2007:1).
- Several large companies in South Africa have dual listings on the JSE Limited (JSE) and on the London Stock Exchange or the NYSE.
- The accounting bodies of the US, the UK and South Africa are all members of the International Accounting Standards Board (IASB).

The practices and principles applied in the presentation of IRs by the three countries are dealt with and are used to compare the interim reporting practices for listed companies in South Africa, which have adopted IFRSs outright, to the UK, which implemented IFRSs for listed companies from 1 January 2005, and the US, which is endeavouring to converge US GAAP with the IFRSs over time, and to identify differences and similarities in respect of interim financial reporting.

3.3 INTERIM FINANCIAL REPORTING IN THE US

The developments for each of the three countries identified are dealt with under the headings of listings requirements, legal requirements and accounting pronouncements, since these appear to be the main drivers of the development and eventual regulation of IRs (Koen *et al.,* 1999:1).

3.3.1 Listings requirements

Edwards *et al*. (1972:55) and Schiff (1978:15) argue that the first IR in the US was probably the report published by the United States Steel Corporation in 1901. These authors also conclude that this IR, as well as other such reports, resulted from voluntary efforts by corporate managements to provide their shareholders with information in respect of a company's financial performance on a more frequent basis than the customary annual reports. Being voluntary, the contents of these reports were not standardised.

Hussey and Woolfe (1994:5) note that, in addition to voluntary disclosures made by companies, the first NYSE listing agreement (an agreement between the stock exchange and the listed companies) to stipulate disclosure of quarterly (interim) income statements was signed in October 1910. By 1939, the NYSE listing agreement required quarterly earnings to be published, unless proof could be supplied that the publication thereof would be impractical or misleading (Hussey & Woolfe, 1994:6). It was contended that the desire of listed companies to comply with requests from the NYSE contributed to the phenomenon that, by 1960, irrespective of the fact that listings requirements for such companies did not specifically require IRs, more than 99% of companies listed on the NYSE already provided some form of interim data (Edwards *et al.,* 1972:55).

According to Bagshaw (1999:61), specific listings requirements in respect of IRs at the NYSE never progressed beyond the quarterly earnings statements that were first required in 1939. The reason for this is probably that the SEC took over the role of issuing disclosure requirements[20] for listed companies in 1934, and listings requirements were therefore largely replaced by the disclosure requirements of the SEC. The situation has not changed since then.

3.3.2 Legal requirements in the US

3.3.2.1 The Securities Exchange Act, Form 10-Q and its earlier equivalents, and the Sarbanes-Oxley Act

The implementation of the Securities Exchange Act of 1934 in the US transferred the power to require annual reporting, as well as IRs, to the SEC. Currently, quarterly reports are still required in terms of Sections 13(a) and 15(d) of the Securities Exchange Act of 1934.

[20] See Section 3.3.2, below.

However, it appears that the only SEC disclosure requirements related to interim reporting in particular were the reporting of significant events in respect of the company during a specific year on the prescribed form, Form 8-K (Edwards *et al.,* 1972:57; Hussey & Woolfe, 1994:6). In 1946, the SEC increased the amount of information to be supplied in respect of interim periods by requiring companies to file quarterly reports of sales and gross revenues (Hussey & Woolfe, 1994:6; Schiff, 1978:15). By 1949, Form 9-K had been adopted to provide interim financial information.

According to Edwards *et al.* (1972:58) and Hussey and Woolfe (1994:6), the filing of quarterly reports on Form 9-K continued until 1953. However, at this point, the Form 9-K requirement was rescinded, when an unpopular proposal in 1952 to expand quarterly reporting to include a complete income statement and a statement of retained earnings was rejected. Edwards *et al.* (1972:58) state that from 1953, after the use of Form 9-K (containing sales and gross revenue) had been discontinued, until 1955, the only IRs required by the SEC were the earlier 8-K reports on significant events – the situation therefore returned to what it was prior to 1946.

During 1955, the SEC adopted a new requirement in respect of IRs – this time, they required a semi-annual report, and reinstituted the earlier Form 9-K (Bagshaw, 1999:61; Deitrick & Alderman, 1979:324; Hussey & Woolfe, 1994:6). According to Hussey and Woolfe (1994:6), this step met with strong resistance from corporate management, but the SEC refused to retract the revised requirement. The semi-annual IR (Form 9-K) required the following information (Edwards *et al.*, 1972:57):[21]

- sales, less discounts, returns and allowances;
- operating revenues;
- extraordinary items;
- net income or loss before taxes on income;
- provision for taxes on income;
- net income or loss;
- special items; and
- earned surplus items.

[21] Cited *verbatim*, but broken up into bullets and with minor changes to the punctuation.

The interim reporting requirements of the SEC remained largely unchanged until 1971, when Form 9-K was withdrawn by Release No 9004, in which the implementation of Form 10-Q for quarterly reports, instead of the earlier semi-annual reports, was specified (Bagshaw, 1999:61; Deitrick & Alderman, 1979:324; Hussey & Woolfe, 1994:6). Since then, Form 10-Q has had to be submitted for the first three quarters of the financial year, but is not required for the fourth quarter, since the annual report is normally published shortly after the end of the fourth quarter (year-end).

The income statement information required by Form 10-Q, as issued in 1971, comprised the following (Edwards *et al.*, 1972:59):[22]

- gross sales, less discounts, returns and allowances;
- operating revenues;
- costs and expenses (interest charges had to be shown separately, but all other costs and expenses could be combined);
- income before taxes on income and extraordinary items;
- provision for taxes on income (amounts related to deferred taxes had to be disclosed separately);
- minority interests;
- income before extraordinary items;
- extraordinary items, net of income tax effect (the amount of the applicable income tax had to be disclosed);
- net income;
- earnings per share; and
- dividends per share.

Several changes are evident when the requirements for the income statement information in Form 10-Q are compared to those of the earlier Form 9-K. In broad terms, the 1971 version of Form 10-Q required several items in addition to the information initially required in Form 9-K, as well as comparative information for the corresponding period of the previous year. The 1971 version of Form 10-Q also introduced new requirements in respect of capitalisation and stockholders' equity, whereas Form K-9 contained no such requirements.

[22] Cited *verbatim*, but broken up into bullets and with minor changes to the punctuation and tenses.

The following additional items were required specifically in the 1971 version of Form 10-Q (Edwards *et al.*, 1972:60):[23]

- short-term loans and notes;
- long-term debt (the current portion had to be reported separately and convertible and subordinated debt had to be separately disclosed);
- minority interests;
- "deferred credits";
- preferred stock shares and amounts (convertible and nonconvertible issues had to be disclosed separately);
- common stock shares and amounts;
- capital in excess of par;
- analysis of retained earnings since the beginning of the current fiscal year, with appropriate disclosure of
    - prior period adjustments;
    - net income;
    - dividends;
    - other credits or charges;
- Treasury shares and amounts, by class of security; and
- number of shares of each class of securities reserved for conversion, warrants, options and other rights.

Over time, several other changes to Form 10-Q were made. Most notably, IRs now comprise condensed financial statements with the normal form and the usual content of financial statements (with a few exceptions), rather than the detailed per item requirements of the earlier versions of Form 10-Q. Furthermore, the IR information in Form 10-Q now also includes a statement of cash flows, which was not required in the original Form 10-Q. This became a requirement shortly after APB 19, which requires a statement of changes in financial position (an early version of the statement of cash flows), was issued in 1971 (APB, 1971). The preparation of a statement of cash flows in terms of Statement of Financial Accounting Standard (hereafter SFAS) 95 only became a requirement after the issuance of the standard in 1987 (FASB, 1987).

[23] Cited *verbatim*, but broken up into bullets and with minor changes to the punctuation and tenses.

The interim financial information required in Form 10-Q is contained in Section 210.10-01 of the Electronic Code of Federal Regulations issued on 8 May 2008 (SEC, 2008a) and 10 July 2012 (SEC, 2012), which states that condensed financial statements should be prepared following the general form and content of presentation prescribed by the federal regulations, except for the following:

- Only consolidated IRs, which need not be audited, need to be prepared.
- Interim balance sheets need only include major headings (captions) as prescribed by the federal regulation, except for inventories, in respect of which more detail is required. If any major balance sheet heading represents less than 10% of total assets, and the amount of the heading has not fluctuated by more than 25% from the end of the preceding financial year, such a heading may be combined with another heading.
- Interim income statements (statements of income) must also include major headings prescribed by the federal regulation, but if any such a major heading is equal to less than 15% of the average net income in the most recent three financial years and the amount has not fluctuated by more than 20% compared to the IR of the immediately preceding financial year, it may be combined with other headings. If the amounts so calculated are immaterial, they need not be shown separately.
- The interim statement of cash flows (statement of changes in financial position) can be abbreviated by starting with a single figure for net cash flows from operating activities and should show changes in the net cash flows from investing and financing activities separately only when they exceed 10% of the average net cash flows from operating activities for the most recent three years. If these amounts are immaterial, they need not be shown separately.
- Disclosures of sufficient interim financial information so as to not make IRs misleading must be provided on the face of the financial statements or in accompanying footnotes. To this end, it may be assumed that users have read or have access to the audited financial statements of the preceding financial year. In the case of material contingencies, these matters must be disclosed irrespective of whether a significant change has occurred since the year-end or not.
- Several other detailed disclosures (such as business combinations, disposals of entities, earnings and dividends per common share and so forth) are required, but are not listed here (Paragraph 210.10-01(b)).

- The comparative information in respect of the current interim period (quarter) to be presented in the IRs as set out in Paragraph 201.10-01 (c), are the following:
    - On the interim balance sheet, the balance sheet at the end of the immediately preceding quarter and at the end of the preceding financial year must be provided. The balance sheet at the end of the immediately preceding financial year should be condensed to the same level as the current interim balance sheet. The comparative interim balance sheet is not required, unless it is crucial to the understanding of the effect of seasonal fluctuations on the financial position of the relevant entity.
    - In the case of the interim income statement, such statements shall be provided for the most recent quarter to be reported on, cumulatively from the end of the previous financial year and cumulatively from the end of the immediately preceding quarter and for the corresponding periods in the preceding year.[24]
    - In the case of interim statements of cash flows, such statements must be provided cumulatively between the end of the previous financial year and cumulatively from the end of the immediately preceding quarter and for the corresponding periods in the preceding year.
    - In the case of interim income statements and cash flow statements of entities engaged in seasonal production or single-crop agricultural activities, certain exceptions are made.
- Detail on interim reviews by an independent accountant is addressed in Paragraph 210.1-01(d) and guidance in respect of other financial information to be provided under certain circumstances are contained in Paragraph 201.10-1(e) (these two requirements were added in 2009 and 2011 respectively).

Since 1971, all listed companies had to submit Form 10-Q to the SEC within 45 days from the end of the quarter to which the information relates. However, in 2002, Release 33-8128 was issued, and this document scheduled a reduction of the deadline for the submission of Form 10-Q from 45 days to 35 days over a four-year phase-in period (SEC, 2002) for companies with a market capitalisation of $75 million and above – the “accelerated filers”. In 2005, the SEC issued revised rules in Release 33-8644, whereby the reduction of the period between the interim date and the submission date of the Form 10-Q was set at 40 days, rather

[24] This may also be provided for the cumulative 12-month period ended during the most recent interim period and for the corresponding preceding period, and these could be issued in lieu of the year-to-date statements required in respect of the income statement and statement of cash flows.

than being reduced to the 35 days proposed by the earlier Release 33-8128 (SEC, 2005). All other issuers of interim reports should still file within 45 days after the end of the fiscal quarter up to this date.

The promulgation of the Sarbanes-Oxley Act of 2002, and specifically Section 906 of the Act, requires the chief executive officer, as well as the chief financial officer of a company to certify that the IR "fully complies" with sections 13(a) and 15(d) of the Securities Exchange Act, and that "information contained in the periodic report fairly presents, in all material respects, the financial condition and results of operations of the issuer". Non-compliance with this legal requirement can lead to large fines and imprisonment of the officials (Ernst & Young, 2012b:2.4).

3.3.3 Accounting pronouncements

3.3.3.1 APB Opinion 28 on interim financial reporting, now renamed as ASC 270

In May 1973, the American Accounting profession's first pronouncement directed specifically at interim financial reporting was promulgated, namely APB Opinion No. 28, *Interim Financial Reporting* (APB, 1973). This document represents the Accounting Principles Board's consensus on the accounting principles and reporting practices surrounding interim financial reporting, as well as minimum disclosure requirements for interim financial reporting by publicly traded companies. Note that this accounting pronouncement, and by implication all amendments from 1973 up to January 2008, has been absorbed into the FASB Accounting Standards Codification (hereafter ASC) as ASC 270 *Interim Reporting* (also referred to as Topic 270), and is effective for all interim and annual periods ending after 15 September 2009 (FASB, 2009:§A11).[25]

The requirements of the SEC in respect of the filing of Form 10-Q are not the same as those of APB Opinion No. 28 or its more recent version, ASC 270. Form 10-Q pertains to the regulatory requirements of the SEC, while ASC 270 applies to the form and content of IRs of publicly traded companies that are issued to shareholders, irrespective of whether some of the information in these quarterly reports are also included in Form 10-Q, and whether such a company is also required to file a Form 10-Q at the SEC. However, the principles used for

[25] See Section 3.3.3.6, below, for a brief explanation of this change.

measuring quarterly accounting information as set out in ASC 270 should be used when completing Form 10-Q (Ernst & Young, 2012b:3.1).

The broad accounting principles associated with issuing IRs to the shareholders of publicly traded companies identified in this accounting pronouncement, are the following:

- Each interim period should be viewed as an integral part of an annual period. This means that the integral approach is applied.
- IRs should generally be prepared in accordance with the generally accepted accounting principles (GAAP) and practice used during the preparation of the latest annual financial statements of the entity, unless a change in accounting policy has been adopted in the current year.
- Some generally accepted accounting principles and practice should be modified so that the results of the interim period relate better to those of the annual period. This confirms that the integral approach is adopted.

The following disclosures are required in terms of APB Opinion No. 28 (APB, 1973:Part II; Bagshaw 1999:64) – subsequent changes to APB Opinion No. 28 in its ASC 270 guise are indicated in brackets where applicable:

- sales or gross revenues, provisions for income taxes, extraordinary items, the effects of changes in accounting policies and net income – “other comprehensive income” is added in ASC 270 (FASB, 2009);
- primary – the term “basic” is used in ASC 270 (FASB, 2009) – and fully diluted earnings per share for each period presented;
- material seasonal variations in respect of revenues, costs and expenses;
- significant changes in estimates or provisions for income taxes;
- disposals of business segments (the phrase “component of an entity” is used in ASC 270 (FASB, 2009)) and extraordinary, unusual or infrequently occurring items;
- contingent items;
- changes in accounting principles or accounting estimates; and
- significant changes in the financial position of the entity.[26]

[26] Although balance sheets and statements of cash flows are not required, companies are **encouraged** to provide these statements or at least disclose changes related to these since the last reporting period.

No maximum period between period-end and submission date is recommended in the above-mentioned documents.

The disclosure requirements of comparative amounts required by APB Opinion No. 28 and ASC 270 are comprehensive, and include the amounts for the previous period and year-to-date figures for the previous year – this results in four columns (two for the current year and two for the previous (comparative) year presented in any specific quarter.

According to McEwen and Schwartz (1992:78) and the APB (1973:§12), this document requires revenues and costs directly associated with revenues (cost of sales) to be accounted for on the same basis as for annual reporting periods. In respect of other costs, the following broad principles apply:

- costs other than product costs related to revenue should be recognized in income in the period incurred, or be allocated among interim periods on some acceptable basis;
- if a specific cost or expense relates to more than one interim period, the item may be allocated to those interim periods on a basis consistent with that used when reporting results in the annual financial reports;
- in the case of costs and expenses that relate to a specific interim period, these should be charged in that specific period and disclosure should be made of the nature and amount of such costs, unless these items are also reported in the previous reporting period;
- an arbitrary assignment of the amount of the above costs to an interim period should not be made;
- where gains and losses arise in any interim period and these are similar to items that would not be deferred at year-end, these items should not be deferred to a later interim period within the financial year; and
- in the case of taxation, APB Opinion No. 28 states that a provision for taxation for an interim period should be raised at the best estimate of the effective tax rate expected to apply to the complete financial year.

3.3.3.2 Changes to APB Opinion No. 28 in respect of changes in accounting policy

In December 1974, the FASB issued the SFAS (*SFAS* No. 3, *Reporting Accounting Changes in Interim Financial Statements*: *An amendment to APB Opinion No. 28* (FASB, 1974:§9-§13) to elaborate on how to report changes in the applicable accounting method in the interim periods.

The original version of APB Opinion No. 28 stated that changes in interim or annual reporting practice made during a specific interim period should be reported in the period in which the change is made, in terms of the provisions of APB Opinion No. 20, *Accounting Changes*. This pronouncement required the cumulative effect of a change in accounting practice or principle to be accounted for as part of net income in the period when the change is effected. That meant that if a change in accounting principle or practice took place in the second interim period, the IR reflected cumulative changes until the beginning of the current financial year, as well as to the beginning of the second interim period, as part of the net income of the second interim period. The first quarter interim statement was not restated.

In SFAS No. 3 of the FASB this requirement was changed so that for a change in accounting principle or practice that took place in a period other than the first quarter, no cumulative effect of the change was included in the net income of the period of change. Instead, the cumulative effect of the change as at the beginning of the financial year was accounted for as a part of net income in the first interim period of the financial year in which the change was made. At the same time, the financial information of other pre-change interim periods should be restated in terms of the new policy, and the interim information in the period of change should be presented on the new basis. Certain related disclosures to clarify the above treatment were required in the IRs (FASB, 1974:§10).

In 2005, SFAS No. 154 was issued by the FASB as part of the broader effort to improve the comparability of financial reporting across international borders in collaboration with the International Accounting Standards Board (IASB). In doing so, the accounting for changes in accounting principles or practice in IRs contained in SFAS No. 3 was aligned with the latest international developments. According to these amendments, changes in an interim or annual accounting principle effected in an interim period should be reported and disclosed in the period in which the change is made, in terms of the provisions of SFAS No.154, *Accounting Changes and Error Corrections*. This standard requires a change in accounting principles to be reported with retrospective application as far as it is practicable. However, the impracticability exception may not be applied to interim periods in the current financial year before the one in which the change took place. If it is impracticable to effect changes in the interim periods before the change, the change in the applicable accounting principle may only be effected at the beginning of the next financial year (FASB, 2005:§15).

3.3.3.3 Changes to APB Opinion No. 28 related to the tax charge in interim financial statements

As has already been mentioned in Section 3.3.1, APB Opinion No. 28 originally required an estimated annual effective tax rate to be determined, which must then be used to determine the interim period taxation. However, the application of this rather broad guideline led to differences in the accounting treatment that different companies used for similar situations. To counter this situation, in 1977, the FASB issued SFAS Interpretation No. 18 *Accounting for Income Taxes in Interim periods: An interpretation of APB Opinion No. 28* (FASB, 1977). Paragraph 9 of this interpretation prescribes the following calculation for the interim period tax: the estimated annual effective tax rate, the calculation of which is prescribed in APB Opinion No. 28, is applied to the year-to-date ordinary income at the end of a specific interim period to determine the year-to-date tax charge at the end of the specific interim period. This cumulative amount is then reduced by the total tax charge reported at the end of the previous interim period to isolate the interim period tax for that specific interim period.

SFAS No. 96, *Accounting for income taxes*, issued in 1987, required the method of providing for deferred tax to change from the deferred method to the liability method. This pronouncement superseded APB Opinion No.11, *Accounting for income taxes*, under which deferred tax was calculated using the deferred method. Although this change did not result in changes to the allocation method of income taxes to interim periods, as described in APB Opinion No. 28 or SFAS Interpretation No. 18, it did result in the fact that the calculation of the estimated annual effective interest rates became much more complex (FASB, 1987).

In 1992, SFAS No. 109, *Accounting for income taxes*, superseded SFAS No. 96. According to the basis for conclusions set out in SFAS No. 109, this pronouncement was issued in order to reduce the restrictive requirements for the recognition of deferred tax assets contained in SFAS No. 96, as well as reduce the complexity of scheduling anticipated future reversals of temporary differences and the impact of tax-planning strategies. Although the application of APB Opinion No. 28 was not directly affected by these changes, it did have an impact on the treatment of deferred tax assets and, consequently, the tax charge reflected in the IRs (FASB, 1992).

3.3.3.4 Other developments in accounting pronouncements on interim financial reporting

Hussey and Woolfe (1994:6) noted that the FASB issued a discussion memorandum on interim financial reporting in 1978, but this memorandum was never developed into an exposure draft or an accounting standard, and was removed from the FASB's agenda in 1981. Consequently, the accounting for interim reporting, until the recent Codification project, was still governed by APB Opinion No. 28, with related amendments and clarifications as explained earlier.

The approach adopted under interim financial reporting as specified in APB Opinion No. 28 is clearly the integral approach.[27] However, it is interesting to see that the text of the opinion, and now the ASC, includes several examples that illustrate applications of the discrete approach. Note that, despite these examples, several of the APB's members dissented in respect of the adoption of the opinion, specifically because they did not concur with the integral approach's being used for interim financial reporting (APB, 1973:Dissenting opinions).

3.3.3.5 Changes to APB Opinion No 28 (name changed to ASC 270 from 2009) after 2005

As part of the process to convert APB Opinion No. 28 to ASC 270,[28], the terminology of the opinion was also updated, for instance, by changing references to "companies" to the now generally accepted term "entities".

In addition, the following disclosure requirements were added in ASC 270 to align it with the latest accounting developments:

- disclosures about reportable segments (see ASC 280);
- disclosures about defined benefit plans and other defined benefit postretirement benefit plans (see ASC 715);
- information about the use of fair value to measure assets and liabilities in line with Section 820;
- information about derivative instruments as required in certain sub-sections of Section 815;

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[27] See Section 3.1.1 above.
[28] See Section 3.3.3.6, below, for details on the process.

- information about the fair value of financial instruments as required in certain sub-sections of Section 825;
- information about debt and equity securities as required in certain sub-sections of Sections 320 and 942;
- information about impairments that are not temporary as required in certain sub-sections of Sections 320, 325 and 958;
- information about the credit quality of financing receivables and the allowance for credit losses as mentioned in ASC 310; and
- gross and net information as required by certain subparagraphs of paragraph 210.

3.3.3.6 FASB Accounting Standards Codification and ASC 270

As mentioned earlier, APB Opinion No. 28 (as amended) was renamed ASC 270, *Interim Reporting* when the FASB ASC project came to fruition in 2009, via the FASB SFAS No. 168. The ASC project was initiated when the SEC issued a report in 2003 entitled *The study pursuant to Section 108(d) of the Sarbanes-Oxley Act of 2002 on the adoption by the United States financial reporting system of a principles-based accounting system* (FASB, 2009:§A3).

In response to the recommendations of this study, the FASB took a number of steps to improve the quality of standards and the standard-setting process. These initiatives included improving the conceptual framework, codifying existing accounting pronouncements, moving to a single standard-setter system and pursuing the convergence of FASB and IASB standards (FASB, 2009:§A3).

The ASC project aims to organise and simplify authoritative GAAP literature, and not to create new accounting and reporting guidance. This aim was met by reorganizing GAAP literature into approximately 90 accounting topics within a consistent structure and format (FASB, 2009:§A8). The conversion of APB Opinion No. 28, *Interim Financial Reporting* to ASC 270, *Interim Reporting* formed part of this process. With the exception of a number of changes subsequent to the conversion (see Section 3.3.3.5, above) that arose from developments in the accounting arena, the guidance as amended up to 2008 and as contained in APB Opinion No. 28 (as amended up to that point in time) was absorbed into ASC 270.

3.4 INTERIM FINANCIAL REPORTING IN THE UK

3.4.1 Listings requirements (rules) and related requirements

Compared to the US, interim reporting in the UK has a short history. According to Hussey and Woolfe (1994:7) and Lunt (1982:5), the first company to produce an IR in the UK was ICI in 1955. The chairman of the London Stock Exchange first recommended the preparation of IRs by listed companies in August 1964, and this finally became a rule in the *Admission of Securities to Listing* in 1973.

Hussey and Woolfe (1994:8) also report that a revision of the earlier version of the *Admission of Securities to Listing* was issued late in 1984, and that this new version remained unchanged until 30 November 1993. These longstanding listings rules (issued in 1984 and revised slightly in 1993) closely followed the requirements of Statutory Instrument 1984 No 716 (considered in Section 3.4.2). According to the latter document, an IR had to provide the disclosures below in tabular format, with an explanatory report on the activities of the group, as well as the profit or loss during the period (these are minimum requirements). Hussey and Woolfe (1994:10) confirm that the following items were required in IRs according to the listings requirements in the approximately nine-year period between 1984 and 1993:[29]

- net turnover;
- profit or loss before taxation and extraordinary items;
- taxation on profits (UK taxation and, if material, overseas and share of associated companies to be shown separately);
- minority interests;
- profit or loss attributable to shareholders, before extraordinary items;
- extraordinary items, (net of taxation);
- profit or loss attributable to shareholders;
- rates of dividend(s) paid and proposed as well as the amount absorbed thereby;
- earnings per share expressed in pence per share (computed on the figures shown for profits after taxation as defined by SSAP 3); and
- comparative figures in respect of (a) to (j) inclusive for the corresponding previous period.

[29] Cited *verbatim*, but the numbering from (a) to (j) has been replaced by bullets and there are minor changes to the punctuation.

The explanatory report on activities had to address all the significant information necessary to enable users of an IR to assess the trend of the group's activities and profit or loss, including any special factors that had an effect during the interim period on either the activities or profit or loss. The IR also had to provide sufficient information to enable users to make a comparison with the corresponding interim period in the previous year, and as far as possible a reference to the group's prospects in the current year. No balance sheet and cash flow statement disclosures were required (Bagshaw, 1999:16; Hussey & Woolfe, 1994:11).

The next step in the development of interim financial reporting in the UK was the establishment of the Cadbury Committee in May 1991 by the FRC, the London Stock Exchange and the accounting profession to investigate corporate governance in the UK (Cadbury, 1992:3,61; Hussey & Woolfe, 1994:8). This investigation led to the following recommendations on interim reporting (excluding comments on auditing of IRs) in the Cadbury Report (Cadbury, 1992:34):

- Balance sheet information should be included in the IR.
- The IRs should be issued half-yearly, although the committee could see the advantages of quarterly reporting. However, from a cost-benefit perspective, it was perceived as not feasible, and in addition there was no pressure from other shareholder bodies for quarterly reports.
- The ASB and the London Stock Exchange should clarify the accounting rules that companies should follow in the preparation of IRs.
- The publication of cash flow information as part of IRs should be considered again two years hence (that is, in 1994). However, in 1992, the Institute of Chartered Accountants in England and Wales (hereafter ICAEW) issued a technical release recommending the immediate inclusion of cash flow information in the IRs (Hussey & Woolfe, 1994:9).

Despite the above recommendations, disclosure requirements on IRs in the listings rules remained the same until late in 1999, when these rules were amended in response to the eventual clarification of the accounting principles, as proposed by the Cadbury Report. The clarification was contained in a long-awaited accounting pronouncement on IRs issued by the ASB in the UK in 1997.[30] This accounting pronouncement finally addressed the problems on interim reporting identified by the Cadbury Committee (Deloitte Assurance and Advisory,

[30] See Section 3.4.3, below.

2005:15). The additional disclosure requirements in the profit or loss account required by the revised listings rules were the following (Deloitte Assurance and Advisory, 2005:15):

- operating profit or loss;
- interest payable less interest receivable (net); and
- profit or loss on ordinary activities after tax.

The word "basic" was added to the requirement that "earnings per share" should be disclosed.

Apart from the above, the Standard on Interim Reporting also prompted the listings rules to require both a balance sheet and cash flow statement as part of the IR from that point onwards. The change also required comparative amounts for the corresponding interim period in the previous financial year for both the balance sheet and income statement (Deloitte Assurance and Advisory, 2005:12).

Up to 1999, the listings rules (listings requirements) of the London Stock Exchange required IRs to be issued no more than four months after the end of the relevant interim period. From January 2000, however, the time limit on the publication of IRs was reduced from 120 days (four months) to 90 days (Bagshaw, 2000a:56).

On 1 May 2000, the function of providing listings rules via the UK Listing Authority of the London Stock Exchange was transferred from the London Stock Exchange to the independent Financial Services Authority (hereafter FSA) (Sants, Cox, Evans, Ferguson, Hunter, Main, Mathews & Papanichola, 2007:1).

After the transfer of the UK Listing Authority to the FSA, the next extensive revision of the listings rules was prompted by the issuance of three documents by the EU as part of the EU's Financial Services Action Plan, namely the *EU Prospectus Directive*, the *EU Market Abuse Directive* and the *EU Transparency Directive*. These documents had a major impact on the review of the listings rules of the FSA and resulted in a re-writing and splitting of the existing listings rules into three new rule books (Sants *et al.*, 2007:6). The three new rule books are

- the Listing Rules dealing with requirements to be eligible for listing, listing application procedures and the ongoing obligations of listed companies;
- the Prospectus Rules (mainly driven by the *Prospectus Directive* mentioned above); and
- the Disclosure and Transparency Rules (hereafter DTR) (mainly driven by the *Market Abuse Directive* and the *Transparency Directive* and dealing with Periodic Financial Reporting).

A comparison between the revised DTR and *Directive 2004/109/EC i*ndicate that in the case of interim financial reporting (also known as half-yearly reporting in the EU documentation and now in the revised listings rules), the changes to the DTR (the section on disclosure and transparency) could in its entirety be attributed to this EU *Transparency Directive* issued by the EU Parliament on 15 December 2004. In terms of this directive, EU Member States were to comply with this directive from 20 January 2007 (EU, 2004:56).

The new requirements in respect of half-yearly financial reports (IRs) as contained in Chapter 4.2 of the DTR are the following (FSA, 2008):

- Listed companies must issue half-yearly financial reports (IRs) covering the first six months of the financial year.
- An issuer of such report must ensure that the report is available to the public for perusal for at least five years.
- Half-yearly reports (IRs) must include
  - a condensed set of financial statements;
  - an interim management report; and
  - responsibility statements by the persons in the company responsible for half-yearly reports.
- If an issuer is required to prepare consolidated accounts, the condensed set of financial statements must be prepared in terms of IAS 34.[31]
- If an issuer is not required to prepare consolidated accounts, a condensed set of half-yearly financial statements must be still be prepared and although governed by the UK accounting pronouncement, these requirements are very similar to those in IAS 34. These requirements are contained in the Accounting Standards Board's statement *Half-yearly Financial Reports*.[32]
- For issuers not required to prepare consolidated accounts, certain transitional requirements apply.
- The accounting policies and presentation applied to half-yearly figures must be consistent with those applied in the latest published annual financial statements, except where
  - the accounting policies and presentation are to be changed in the annual financial statements to be presented immediately following the half-yearly report (IR), in which

[31] See Section 3.4.3.2, below.
[32] See Section 3.4.3.3, below.

case, the changes in accounting policy and presentation should be disclosed in the half-yearly report (IR); or
    - the FSA agrees otherwise.
- An interim management report must include at least the following:
    - a discussion of the important events that took place during the first six months of the financial year and their impact on the condensed financial statements;
    - a description of the main uncertainties and risks anticipated for the remaining six months of the year. Additional guidance on this is provided in the UK Listing Authority Technical Note: Disclosure and Transparency Rules; and
    - going concern disclosures in terms of the UK Corporate Governance Code of 2010, C1.3 could be included in the IMR or elsewhere in the IR (FRC, 2012:17).
- In respect of related party transactions, a listed company must disclose, as a minimum, the following:
    - related party transactions that took place in the first six months of the financial year and that materially affected the financial position or performance of the entity during that period; and
    - any changes in related party transactions that were addressed in the last annual financial report that could have a material impact on the financial position and performance of the entity in the first six months of the current financial year.
    - As stipulated in DTR 4.2.8R(2), different related party disclosures apply if an entity is not required to prepare consolidated financial statements.
- If the half-yearly report (IR) has been audited or reviewed by auditors in terms of the guidance of the Auditing Practices Board in their *Review of Interim Financial Information*, the report on the audit or the review note must be reproduced in full.
- If the half-yearly report (IR) has not been audited or reviewed by auditors in terms of the guidance of the Auditing Practices Board in their *Review of Interim Financial Information*, this fact must be stated in the report.
- Statements of responsibility must be made by the persons responsible for the IRs (usually it would be the board of directors) in the IRs.
- The name and function of each person who makes such a responsibility statement must be clearly indicated in the responsibility statement.
- Each person providing a responsibility statement must confirm a number of prescribed matters.

In addition to the normal requirements in respect of half-yearly financial reports (IRs), in Chapter 4.3 of the DTR (FSA, 2012), there is also a requirement in respect of an interim management statement. Note that this statement is not the same as the interim management report mentioned earlier in this chapter. This new statement is required for listed companies issuing half-yearly financial statements (IRs) whose shares are admitted to trading, whose home state is the UK and who do not report quarterly. It could therefore be described as a disclosure requirement in lieu of the publication of quarterly reports. The requirements in respect of the interim management statement are set out below:

- An interim management statement should be made public during the first six months of the financial year and also during the second six months of the financial year.
- The statement must be made in the interval between ten weeks after the beginning of the relevant six month period and six weeks before its end.
- The statement must contain information covering the period between the beginning of the six-month period and the date of its publication.
- The interim management statement must provide the following:
    - an explanation of the material events and transactions that have taken place during the relevant period and their impact on the financial position of the issuer and its subsidiaries; and
    - a general discussion of the financial position and performance of the issuer of the IRs and its subsidiaries during the period under review.

In contrast with the earlier requirement of publication of an IR within 90 days from the end of the interim period to which it relates, half-yearly reports (IRs) must, in terms of the DTR, be made public as soon as possible, but not later than two months after the end of the period to which the report relates.

3.4.2 Legal requirements

According to Lunt (1982:101), until 1980, legislation was not directly concerned with interim reporting. However, contained in the UK's then new Companies Act of 1980 was section 43, which refers to IRs in respect of the distribution of dividends. This reference to IRs was part of the justification of the payment of dividends, and the IR as such was not the main focus of the section. The above requirement in the UK's Companies Act of 1980 was repeated in the

UK's Companies Act of 1985, but at that point the requirement was moved to section 270(4) (Davies, Patterson & Wilson, 1994:1474).

By contrast, the first relatively extensive statutory requirements in respect of IRs were contained in Statutory Instrument 1984 No 716 (Hussey & Woolfe, 1994:9). This document was based on the European Commission Interim Reports Directive (82/121/EEC) and was enacted in UK law in 1984 with 1 January 1985 as its implementation date. The main requirements were the following (Hussey & Woolfe, 1994:9):[33]

- listed companies should publish half-yearly reports (IRs) on their activities and profits and losses during the first six months of each financial year;
- the half-yearly report (IRs) should be published within 4 months from the end of the relevant six month period;
- the minimum figures required to be presented in table form were:
  - the net turnover, and
  - the profit or loss before or after deduction of tax.
- where a company had paid or proposed to pay an interim dividend, the figures should indicate the profit or loss after tax for the six-month period and the interim dividend paid or proposed;
- against each figure should be shown the figure for the corresponding period in the preceding financial year;
- an explanatory statement should be given, including any significant information enabling investors to make an informed assessment of the trend of a company's activities and profits or losses, together with an indication of any special factor which has influenced those activities and those profits or losses during the period in question. As far as possible reference should also be made to likely future developments in the current financial year; and
- where the accounting information had been audited, the auditor's report and any qualifications thereof should be reproduced in full.

Bagshaw (1999:13) confirms that up to the end of 1998, no further requirements on IRs were added to the UK Companies Act (as amended). In 1998, the Secretary of State for Trade and Industry decided that a comprehensive review of company law should be conducted by a

[33] Cited *verbatim*, but the numbering from (a) to (g) has been replaced by bullets and there are minor changes to the punctuation.

Steering Group of experts from law, commerce, accountancy and academia, supported by a broadly based consultative group (House of Commons: Trade and Industry Committee, 2003).

The above review culminated in a final report published in July 2001. The UK government responded to proposals in this report in July 2002 in a White Paper called "Modernising Company Law" (House of Commons: Trade and Industry Committee, 2003). No mention is made of IRs in the government White Paper, and the first action resulting from the review was the issuance of the UK's Companies Act of 2004. In Section 14 of this Act, the Financial Reporting Review Panel is granted permission to review periodic (annual and half-yearly) accounts and reports of listed companies and to inform the FSA of its findings on these reports. By implication then, periodic accounts and reports would also include IRs, although these reports are not mentioned specifically (UK, 2004).

The UK's Companies Act of 2006 received Royal Assent on 8 November 2006, and repealed the vast majority of sections contained in earlier Companies Acts. Although the UK's Companies Act of 2006 contains requirements on the form and content of accounts and reports in Part 15, a perusal of the Act indicated that no specific mention of IRs is made in this Act. The new Act also no longer addresses the length of time that may elapse between the interim date and the date of publication of the IR. However, since this new Act does not repeal section 14 of the UK's Companies Act of 2004, IRs are still subject to review by the Financial Reporting Review Panel (UK, 2006). Section 435 of the Companies Act of 2006 requires that if extracts from statutory financial statements (such as annual financial statements) are used in non-statutory reports such as IRs (the full-year comparative amounts, for instance), a statement to this effect must be made in the IR. This statement should, amongst others, point out that the statements containing the extract of the statutory accounts are not statutory accounts, and whether the statutory accounts that formed the basis of the extract have been subject to audit, whether the audit report was qualified or unqualified or contained a statement as contemplated in Section 498(2) or (3) (UK, 2006).

3.4.3 Accounting pronouncements

The report of the Cadbury Committee indicates that no formal accounting pronouncements by the ASB in respect of interim financial reporting existed in the UK by December 1992 (Cadbury, 1992:34). The regulation of interim reporting for listed companies was restricted to the listing rules of the London Stock Exchange[34] and the UK's Companies Acts.[35] The Cadbury Report[36] recommended that the ASB in conjunction with the London Stock Exchange should clarify the accounting principles associated with IRs.

3.4.3.1 The ASB Statement on interim reports

In 1997 the ASB issued a statement, *Interim reports,* which indicated that the objectives of interim financial statements are similar to those of annual financial statements and encouraged listed companies to issue IRs within 60 days after the end of the six-month interim period. The statement also required the discrete approach[37] to be followed in preparing IRs, with the exception of the calculation of the tax charge in the IR, which should be based on a projection of the total projected tax payable for the year and must be aligned with the entity's interim profit before tax. This statement (replaced after being updated in 2007 as discussed in Section 3.4.3.3, below) contained non-mandatory recommendations of best practice for listed and unlisted companies, and broadly speaking required (ASB, 1997:§34-§56):

- commentary by management;
- a summarised income statement;
- a statement of total recognised gains and losses;
- a summarised balance sheet; and
- a summarised cash flow statement.

- **Summarised income statement (ASB, 1997:§40-§48)**

  In terms of this statement, the summarised income statement contained in the IRs had to include the following (ASB, 1997:§40):[38]

  - turnover;
  - operating profit or loss;
  - interest payable less interest receivable (net);
  - profit or loss on ordinary activities before tax;
  - tax on profit or loss on ordinary activities;
  - profit or loss on ordinary activities after tax;

[34] See Section 3.4.1, above.
[35] See Section 3.4.2, above.
[36] See Section 3.4.1, above.
[37] See Section 3.1.2, above.
[38] Cited *verbatim*, with minor changes to the punctuation.

- minority interests;
- profit or loss for the period; and
- dividends paid and proposed.

In addition to the above, the turnover (sales) and operating profit of acquisitions and discontinued operations had to be presented on the face of the income statement in terms of Financial Reporting Standard (hereafter FRS) 3. The comparative information in respect of the IR would, in the case of the summarised income statement, be that on the full previous period and the corresponding interim period.

- **Statement of total recognised gains and losses and reconciliation of movement in shareholders' funds (ASB, 1997:§49-§51)**
  The statement of total recognised gains and losses was required only where the amounts involved were material. In addition, a reconciliation of the movements in shareholders' funds had to be presented where movements in shareholders' funds (which were not included in the statement of total recognised gains and losses) warrant disclosure. The same comparative information as for an interim income statement had to be presented.

- **Summarised balance sheet (ASB, 1997:§52)**
  The summarised balance sheet contained in the IR had to use similar classifications to those used in the annual financial statements (APB, 1997). These classifications had to be (ASB, 1997:§52):[39]
  - fixed assets;
  - current assets;
    - stock;
    - debtors;
    - cash at bank and in hand;
    - other current assets;
  - creditors: amounts falling due within one year;
  - net current assets (liabilities);
  - total assets less current liabilities;
  - creditors: amounts falling due after more than one year;
  - provisions for liabilities and charges;

[39] Cited *verbatim*, with minor changes to the punctuation.

- capital and reserves; and
- minority interests.

For the summarised balance sheet the comparative amounts at the end of the previous annual period were required. However, where there were seasonal variations, comparative amounts for the corresponding interim period could also be useful.

- **Summarised cash flow statement (ASB, 1997:§53)**

In the case of the summarised cash flow statement, only the total amounts for categories of cash flows required by FRS 1, had to be presented in the IR (ASB, 1997). The totals recommended by FRS 1 were the following (cited *verbatim*):[40]

  - net cash inflow/outflow from operating activities;
  - returns on investments and servicing of finance;
  - taxation;
  - capital expenditure and financial investment;
  - acquisitions and disposals;
  - equity dividends paid;
  - management of liquid resources;
  - financing; and
  - increase/decrease in cash.

A reconciliation of operating profit to operating cash flows should be provided in sufficient detail for users to be able to appreciate its chief components.

For the summarised cash flow statement, the comparative disclosures were the same as for the income statement and statement of total recognised gains and losses.

The management commentary accompanying the IR was not as detailed as the operating and financial review required for annual financial statements, but had to include the issues normally included in the operating and financial review. A balanced narration, dealing with significant changes since the last set of annual financial statements, reasons for the changes, the main factors influencing performance and an explanation of seasonal trends had to be presented (ASB, 1997:§34).

[40] Cited *verbatim*, with minor changes to the punctuation.

3.4.3.2 IAS 34 on Interim Financial Reporting

In terms of Regulation (EC) No 1606/2002, companies listed on regulated markets such as the London Stock Exchange had to comply with International Financial Reporting Standards (IFRS) from 1 January 2005 when preparing their consolidated financial statements (EU, 2002). This implies that all consolidated IRs of companies listed on the London Stock Exchange had to comply with IAS 34 when presenting condensed (summarised) financial statements, but that entities that did not prepare consolidated financial statements did not have to prepare IRs in terms of IAS 34 (FSA, 2008). The latter rule on consolidated IRs was confirmed in the DTR addressed in Section 3.4.1 of this study. (The requirements of IAS 34 are discussed in detail in Section 3.5.3, where IAS 34, the applicable accounting pronouncement which is also in force in South Africa, is addressed at length.)

3.4.3.3 ASB Statement on Half-yearly Financial Reports

The original 1997 *Statement on Interim Reports* was updated and revised in 2007 in response to the issuance and implementation of Directive 2004/109/EC in the UK (ASB, 2007:§1 of Introduction) and issued as the ASB Statement *Half-yearly Financial Reports*. The revised statement modernized the former statement with regard to the terminology and subsequent developments on financial statements, and in addition requires a number of new disclosures such as disclosures on principal risks and uncertainties and major related party transactions.

In the case of companies that do not prepare consolidated financial statements, the DTR determines that the requirements of IAS 34 need not be complied with, but that the IRs of such companies should be prepared in terms of the ASB Statement *Half-yearly Financial Reports* as issued in 2007 (ASB, 2007:§2).

According to paragraph B1 of Appendix B of the new statement, this statement and IAS 34 are consistent in all material respects, except for the fact that this statement was drafted in the context of half-yearly reports, whereas IAS 34 also accommodates the scenario of quarterly reports. The only significant difference between the two standards arises from the fact that the guidance of the International Financial Reporting Interpretations Committee in interpretation IFRIC 10 *Interim financial reporting and impairment* (IFRIC, 2011) does not allow the write-back of impairment losses on goodwill and equity investments recognised in an interim period, whereas paragraph 27 of the ASB Statement *Half-yearly Financial Reports* allows such write-backs under the circumstances set out in FRS 10 in paragraph 44 (ASB, 2007).

3.5 INTERIM FINANCIAL REPORTING IN SOUTH AFRICA

3.5.1 Listings requirements

According to Levenberg (1977:11), the JSE, which was called the Johannesburg Stock Exchange up to the middle of 2005 and the JSE Limited from 1 July 2005 (JSE, 2013), Listings Requirements for IRs in South Africa came into effect for the first time on 1 July 1972. These requirements stated that all relevant disclosures required by the Companies Act applicable at the time should be provided in IRs. In addition, the JSE also called for estimated unaudited profits or losses before **and** after tax, whereas the South African Companies Act required only net profit or loss after tax to be disclosed.

In 1986, the JSE issued extensive formal listings requirements (JSE, 1986) in respect of interim financial reporting for the first time – the requirements were contained in Paragraphs 2.32 to 2.36 of these listings requirements, and included disclosures in respect of both interim balance sheets and income statements. However, according to Vermaas (1995:176), during the period from 1972 to 1995, the application of the content of these listings requirements relied to a large extent on practice notes, as well as on the JSE, for interpretation. For this reason, these requirements are not considered in detail. The Research Sub-committee on the Future Structure of the Johannesburg Stock Exchange (JSE, 1994:372) also stated that the listings requirements in use until April 1994 had to be revised, as they were partially out of date, to some extent confusing, and open to misuse in their format at that time. The comment by Vermaas (1995:177) thus supports the call for a major revision of the listings requirements, and which took place in 1995.

The 1995 revision of the JSE Listings Requirements resulted in the following requirements in respect of interim financial reporting (JSE, 1995:§8.44 to §8.50):

- In addition to the disclosure requirements contained in Schedule 4 of the Companies Act of 1973 (as amended) then applicable in South Africa, an entity had to, at least, where applicable, include the following information in respect of the interim income statement (JSE, 1995:§8.45):[41]

- income before crediting dividends received and deducting depreciation, interest paid, taxation and extraordinary items;
- dividends received (including dividends from associated companies and non-consolidated subsidiaries);
- depreciation;
- interest paid;
- net income before taxation and extraordinary items;
- net income;
- net income of the group;
- extraordinary items; and
- outside shareholders' interest.

- Furthermore, in addition to the disclosure requirements contained in Schedule 4 of the South African Companies Act (as amended) then in force, an entity had to, at least, where applicable, include the following information in respect of the interim balance sheet (JSE, 1995:§8.46):[42]
  - fixed assets;
  - investments: listed, unlisted, market value of listed investments and directors' valuation of unlisted investments;
  - other non-current assets;
  - current assets;
  - ordinary shareholders' funds;
  - preference shareholders' funds;
  - outside shareholders' interest;
  - deferred taxation;
  - current liabilities; and
  - intangible assets.

[41] Cited *verbatim*, with minor changes in the punctuation.
[42] Cited *verbatim*, with minor changes in the punctuation.

Apart from the above information related specifically to the interim income statement and balance sheet, the following supplementary information was also required (JSE, 1995:§8.47):[43]

- capital expenditure for the period;
- capital expenditure committed or authorised;
- finance and operating lease commitments;
- contingent liabilities;
- interest capitalised;
- full disclosure of all borrowings and off-balance sheet borrowings;
- any exceptional increase in borrowings during the period under review and where possible the effect of such increased borrowings on earnings per share – if it is not possible to quantify the effect on earnings per share, the reasons must be stated; and
- details of any Category 4 transactions not previously disclosed to shareholders.

- If a change in the financial year (year end) was proposed, the Listings Division of the JSE must be notified in writing and consulted as to the period or periods covered by the IR (JSE, 1995:§8.48).
- Where the figures in the IR had been audited, the report of the auditors, including any qualifications, must be provided in full (JSE, 1995:§8.49).
- IRs should be presented on a consolidated basis (JSE, 1995:§8.50).
- No guidance in respect of the maximum period subsequent to the end of the interim period before publication of the IR was provided.

In 1998, the JSE Listings Requirements were revised once again, but a comparison of the 1998 version with the 1995 version shows that no changes were effected in respect of interim reporting, although several other changes were evident (JSE, 1995, 1998:§8.44-§8.55).

The 1998 JSE Listings Requirements were again revised and were re-issued in full in September 2000. They became effective from 2 October 2000. Interim reporting disclosures were now contained in Paragraphs 8.55 to 8.59 (JSE, 2000) and the volume of disclosures was severely reduced, due to the fact that the new listings requirements stated that all IRs had to be prepared in accordance with the South African accounting standard AC 127, *Interim*

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[43] Cited *verbatim*, with minor changes in the punctuation.

financial reporting, as issued by the South African Institute of Chartered Accountants (hereafter SAICA) in December 1998 (SAICA, 1998). AC 127 was issued by SAICA to govern IRs and is considered in detail in Section 3.5.3, below. The disclosure requirements of AC 127 were much more comprehensive than the 1998 version of the listings requirements; consequently, the majority of detailed disclosures required by the listings requirements previously now disappeared, as the disclosure requirements were contained in AC 127.

However, despite the requirement to comply with AC 127, some of the supplementary information required by the 1995 and 1998 versions of the JSE Listings Requirements was retained, as well as details on changes of the financial year-end, audited interim reports and the basis of presentation of IRs (JSE, 1995, 1998:§8.48-§8.50).

The disclosures contained in the 1998 version of the listings requirements that were retained after the 2000 revision are the following (JSE, 2000:§8.56(a) and (c):

- any exceptional increase in borrowings during the period under review, and, where possible, the effect of such increased borrowings on earnings per share – if it was not possible to quantify the effect on earnings per share, the reasons had to be stated; and
- details of any Category 4 transactions not previously disclosed to shareholders.[44]

In the 2000 revision, the disclosure of headline earnings was added: in terms of each IR of the periods under review and the immediately preceding comparable period, headline earnings per share had to be disclosed, as well as an itemised reconciliation between headline earnings and the earnings figure used to calculate earnings per share. The headline earnings per share figure had to be calculated in terms of the Accounting Issues Task Force Opinion – Headline Earnings as issued by SAICA (JSE, 2000:§8.56(b)).

The following disclosures were modified (JSE, 2000:§8.58):

- Although disclosures in respect of audited IRs were still required, the matters to be disclosed changed. Where the audit report previously had to be reproduced in the IR (if applicable), the name of the auditor now had to be disclosed. Although the report of the auditor need no longer be disclosed in the published IR, where the audit report was modified, the nature of the modification had to be presented.

[44] A Category 4 transaction is a transaction where any of the percentage ratios defined in Paragraph 9.6 of the JSE Listings Requirements exceed 5%, but are less than 10%.

- If the audit report was not included in the published IR, the fact that the report was available for inspection at the company's registered office had to be disclosed.
- If the report had not been audited, a statement to that effect had to appear in the published report.

Another revision of the listings requirements took place in 2002 and this also amended certain requirements in respect of IRs (JSE, 2002). In this revision, the following two changes in respect of IRs were effected:

- Any reference to Category 4 transactions in paragraph 8.56(d) were dropped.
- The requirement in paragraph 8.56(b) that headline earnings needed to be determined in terms of the Accounting Issues Task Force Opinion – Headline Earnings, was replaced by the requirement stating that headline earnings should be calculated in terms of Circular 7/2002, Headline Earnings of SAICA.

A review of the JSE Listings Requirements from late 2002 to 2007 shows that a large number of other changes took place, but that the impact on interim financial reporting was fairly limited. The changes related to interim financial reporting are the following:

- In 2005, the rule that IRs should be prepared in accordance with and containing the information required by the Statement of Generally Accepted Accounting Practice on Interim Financial Reporting was replaced by a requirement to comply with IFRS (IAS 34) and AC 500 standards on Interim Financial Reporting, as issued by the Accounting Practices Board or its successor. This requirement also applies to the supplementary information to be disclosed in terms of Paragraph 8.58 (Paragraph 8.56 in the 2002 version) of the Listings Requirements (JSE Ltd, 2005).
- In 2005, an additional requirement was inserted, stating that Mineral Companies should make available summary information disclosing material changes in mineral resources and reserves or stating that there have been not any material changes in this regard (JSE Ltd, 2005:§8.58(c)).
- In 2006, the JSE inserted a further requirement, stating that where a material change occurred to the initial estimate of a contingent consideration payable or a receivable payable in terms of an acquisition or disposal as used in *pro forma* financial effect calculations, this should be disclosed (JSE Ltd, 2006:§8.58(d)).
- In 2007, the JSE effected an amendment to Paragraph 8.58(b), whereby the reference to Circular 7/2002 in respect of headline earnings as issued by SAICA was replaced by a

requirement that headline earnings and diluted headline earnings be disclosed, in addition to earnings per share figures calculated in terms of IFRS (JSE Ltd, 2007:§8.58(b)).

In 2008, revised listings requirements were issued, but a review of these requirements revealed no changes in respect of interim financial reporting (JSE Ltd, 2008).

Subsequent to 2008, the following changes in respect of listings requirements for IRs were identified:

- In 2010, the general reference to complying with IFRS was replaced by a specific reference that IRs should be prepared in terms of the requirements of IAS 34: *Interim Financial Reporting* (JSE Ltd, 2010:§8.57(a)).
- Also in 2010, Paragraph 8.58(a) was repealed and the existing Paragraphs 8.58 (b), (c) and (d), were renumbered as 8.58 (a), (b) and (c), but with no change to their content. In addition, Paragraph 8.59 was amended and now requires that the JSE be notified "by the applicant issuer", although there is no indication of who should have notified the JSE in the past (JSE Ltd, 2010:§8.58,§8.59).
- In 2011, the reference to Schedule 4 of the South African Companies Act of 1973 was removed and replaced by a reference to Chapter 2 of the new Companies Act of 2008 (JSE Ltd, 2011:§8.58).
- Updated guidance in respect of the review or audit of IRs is provided. IRs need not be audited or reviewed unless the auditor of an issuing company in the last annual financial reports of the company publishing the IR gave a disclaimer, issued a qualified report or an adverse opinion. Amongst others, the name of the auditor and the fact that the IRs were audited or reviewed should be stated in the published IR. If the IR was not audited or reviewed, this fact should also be stated clearly in the IR. Detailed guidance on this matter appears in Paragraphs 3.18 and 8.60 of the listings requirements (JSE Ltd, 2010).

In summary, the latest JSE Listings Requirements dictate that IRs should be prepared in terms of IAS 34 and AC 500 standards issued by the relevant accounting body. The JSE requires very few disclosure and other requirements in respect of IRs over and above those required in IAS 34. The following is a summary of those requirements relevant to retail companies in South Africa:

- Earnings per share, headline earnings (as well as diluted numbers) and a reconciliation between the two numbers should appear in IRs.

- A statement that IRs have been prepared in terms of IAS 34 must appear in a published IR.
- A material change in the initial estimates of contingent considerations payable or receivable in respect of an acquisition or disposal must be disclosed.
- Details of the auditors and audit report must be given if IRs have been reviewed or audited, or a statement should be included where it has not been done.

3.5.2 Legal requirements

According to Van Wyk de Vries, Janse van Rensburg, Hofmeyr, Suzman, Linn and Glen (1970:12), South African company legislation first came into being with the publication of the 1909 Transvaal Act, which was followed by Act No. 46 of 1926, the Companies Act of 1926. After several commissions of enquiry and extensive amendments to the Companies Act of 1926, the State President appointed a final commission of enquiry into the Companies Act on 14 October 1963. This commission prepared the main report with recommendations on which Act No. 61 of 1973 (the Companies Act of 1973) was based (Van Wyk de Vries *et al*, 1970).

It is clear from the report of this commission that there was nothing on interim financial reporting in either the Transvaal Act of 1909 or in the South African Companies Act of 1926 (as amended) (Van Wyk de Vries *et al*, 1970). Due to the fact that shareholders and prospective investors would have to wait until the end of a company's financial year and in most cases even many months thereafter to receive any information on a company's financial results for the past year, the commission felt that these parties seldom had current information to work with. These parties were therefore at a distinct disadvantage, compared to the directors and officers of the company who, at all times, have current information on the company at their disposal.

This fact, coupled with a local and international trend to disclose interim financial information[45] caused the Van Wyk de Vries Commission to conclude that interim reporting is essential in the modern business world. To this end, the commission made several recommendations on interim financial reporting, which culminated in sections 303, 305, 306, 307 to 309 of Companies Act No. 61 of 1973 (as amended), as well as several paragraphs on

[45] See Sections 3.3 and 3.4, above.

minimum disclosure requirements in Schedule 4 of the Companies Act of 1973 ("the Act" hereafter) (South Africa, 1973). Apart from a few minor amendments to the Companies Act of 1973 in sections 303, 307 and 309, as promulgated in the Companies Amendment Act, No. 76 of 1974 (South Africa, 1974), the sections in respect of interim financial reporting remained intact from 1974 to late 2007. The sections in force before the change in late 2007, stipulated the following:

- Section 303 of the South African Companies Act of 1973 required each public company with share capital, with the exception of a wholly-owned subsidiary, to issue an IR no later than three months after the end of the first six month period of its financial year. If a company changed the end of its financial year, an IR should be prepared from the beginning of the changed book year to the date of the "old" book year. An IR had to be issued to each member and holder of a debenture of the company and was to present the business and affairs of the company fairly or, if it was a holding company, the business and affairs of the group.
- Section 305 stated that the IRs should contain the matters prescribed by Schedule 4, as well as other requirements of the Act. It further stated that IRs need not be audited and each IR of a company should be approved by its directors and signed on their behalf by two directors.
- In terms of Section 306, copies of these IRs had to be lodged with the Registrar of Companies within seven days of the date of issue, accompanied by the prescribed CM 34 Form.
- The Registrar of Companies could, in terms of Section 307, exempt a company from preparing IRs under certain circumstances and could also grant a discretionary extension for submission.
- In terms of Section 309, any member of or holder of a debenture of a company was entitled to be provided on demand with a copy of the most recent IR, without any cost to him or her.

Section 305 originally mentioned that IRs should contain other requirements of the South African Company Act of 1973, as well as the matters described by Schedule 4. The other requirements of the Act were explained earlier, while the content of Schedule 4 mentioned here, is discussed further below. It is important to note that Schedule 4 was amended only twice since 1973 (once in 1992 and once in late 2007), before being retracted when South Africa's new Companies Act of 2008 was promulgated. Although some amendments in respect of IRs occurred in 1992, no further such amendments were promulgated in 2007. Thus the requirements of Schedule 4 as per paragraphs 73 to 79 after the 1992 amendment (before the amendment in 1992, these requirements were contained in paragraphs 66 to 68) could be summarised as follows (South Africa, 1992:§73-79§):

- The fact that information in an IR was not audited had to be mentioned (before the 1992 amendments, the fact that IRs were not audited was not stated).
- If a required amount in respect of an IR was not available from the accounting records, such an amount could be estimated, provided that the fact that it was an estimate was clearly stated (this was not changed in 1992).
- An IR had to, under appropriate headings and in narrative form, deal with all descriptive matters and had to provide amounts and statistics, as far as possible, in tabular format (this was not changed in 1992).
- Any matter not specifically prescribed by Schedule 4, but that was necessary to understand the financial position and results of operations of an entity during the interim period, also had to be dealt with in an IR under appropriate headings. In particular, any material changes in net realisable value and the replacement value of any assets compared to their carrying amount that the directors are aware of, had to be disclosed (no change was made in 1992).
- Where amounts were provided, comparative amounts (if appropriate) had to be provided in respect of the immediately preceding interim period, as well as the corresponding previous audited amounts in respect of the most recently completed financial period (before the 1992 amendments, only the corresponding interim amounts were required and no annual comparatives).
- The minimum prescribed content of an interim income statement after the 1992 amendments would be the following:[46]
    - turnover;*[47]
    - net income before interest paid and taxation (before the 1992 amendments only profit or loss after tax had to be disclosed);
    - net interest paid;*
    - taxation;*
    - retained equity income of associates and non-consolidated subsidiaries;*

[46] Cited *verbatim*, with minor changes in the punctuation.
[47] * Not required before 1992.

- net income attributable to ordinary shareholders;*
- dividend per share;*and
- any other information material to understanding the business of the company*.

- The minimum prescribed content of a summarised interim balance sheet would be the following (no balance sheet was required before 1992):[48]
  - total assets;
  - shareholders' funds;
  - non-interest bearing debt;
  - interest bearing debt;
  - net asset value per share;
  - number of issued ordinary shares; and
  - any other information material to understanding the business of the company.
- The IR must include sufficient information on the cash position of the company (nothing was required before 1992).
- Any comments on facts or circumstances related to the financial position of the company, and, where appropriate, the group, that are necessary to understand better the information given must be stated. This includes information in respect of contingent liabilities, capital commitments, acquisitions and disposals of subsidiaries and changes in interest in respect of subsidiaries (no change was made in 1992).
- The extent, if any, to which a change in accounting policy applied in previous IRs has materially affected the IR when compared to previous reports, must be stated (no change was made in 1992).

With the promulgation of the Corporate Laws Amendment Act, No. 24 of 2006 on 14 December 2007, the items set out below were the only changes effected in respect of IRs (South Africa, 2007):

- In Section 303, the terminology referring to a "public company" was changed to refer to a "widely held company", but apart from that, the meaning of the section remained unchanged.
- In Section 305, the reference to compliance with requirements of Schedule 4, which took up the whole of subsection 1, was removed and replaced by paragraph 4A(b) of the revised Schedule 4. Paragraph 4A(b) stated that public interest companies (presumably

[48] Cited *verbatim*, with minor changes in the punctuation.

this referred to "widely held companies", as there was an inconsistency in the use of this term throughout the Act) still had to comply with paragraph 73 on IRs, as contained in Schedule 4, unless there was a conflicting requirement in financial reporting standards. In subsection 3, a provision was added to indicate that IRs should be signed by a single director when the company only has one director.

The requirements of the Corporate Laws Amendment Act mentioned above were in use only for a short time, until the new Companies Act, Act No. 71 of 2008 (South Africa, 2009) was promulgated on 8 April 2009. Unlike the Companies Act of 1973 and the Corporate Laws Amendment Act of 2006, the Companies Act of 2008 no longer makes specific reference to IRs, except as part of the definition of a financial statement where IRs are included as part of the list of reports qualifying as such.

Section 29(1) and (2) of the Companies Act of 2008 states that if financial statements (in this study specifically IRs) are provided by a company, they must satisfy IFRS (IAS 34 in the case of IRs) as to form and content, state the affairs and business of the company fairly, and explain the financial position and transactions of the business, show the assets, liabilities, equity, income and expenses and any other information prescribed, and set out the date on which they were produced and the applicable accounting period. The section continues by stating that on the first page of the IRs, a prominent notice should be provided on whether the IRs have been independently reviewed or not independently reviewed, as well as the name and professional designation (if applicable) of the individual who prepared or supervised the preparation of the IRs. In Section 29(2), it is stated specifically that any financial statements (including IRs) should not be false, misleading or incomplete in any material respect.

3.5.3 Accounting pronouncements

No accounting standard in respect of interim financial reporting was issued by the IASC internationally, or by the Accounting Practices Board in South Africa, prior to IAS 34 and AC 127, which were issued in 1997 and 1998, respectively. Since the Accounting Practices Board took a decision to adopt the international accounting standards issued by the IASC in South Africa with only minor adjustments (Techtalk, 1995:4), AC 127 was virtually identical to IAS 34. A comparison of the two standards indicates that, at the time, there was only one material difference in principle between AC 127 and IAS 34. This difference arose from the fact that the South African standard did not allow the IAS 8 alternative treatment, which stipulated that an adjustment resulting from a change in accounting policy should be included in profit or loss for the current interim period, and that only the financial statements of the prior interim periods in the current year should be restated, while no restatement of comparative information in prior years was allowed. AC 127 allowed changes in accounting policy to be adjusted only in terms of the normal rules on changes in accounting policy as contained in AC 103 (SAICA, 1998). In 2004, the alternative treatment in respect of changes in accounting policy previously contained in IAS 8 was removed from this international standard and, consequently, this allowed alternative was also removed from IAS 34 (IASB, 2004) – IAS 34 and AC 127 became identical. In 2004, the notation reference of all South African statements/standards was also changed to include the international standard numbers; consequently, AC 127 became IAS 34(AC 127) (SAICA, 2005:§09). This notation format is not used in this study, since the double-barrel notation format has been dropped since and is no longer in use.

During September 2007, a revised IAS 1 on the presentation of financial statements was issued. This document resulted in a number of minor editorial and limited consequential amendments to IAS 34, without changing any of the principles contained in the pronouncement (IASB, 2008). The new terminology introduced is used in the analysis below, with the previously used terminology presented in brackets.

The main principles on interim financial reporting as contained in IAS 34 are the following:

- The discrete approach (see Section 3.1.2) should be followed, except in the case of the income tax charge in the statement of comprehensive income (income statement), where the integral approach is followed.
- The IR should as a minimum contain the following components:
    - condensed statement of financial position (formerly condensed balance sheet);
    - condensed statement or statements of profit or loss or other comprehensive income and statement of comprehensive income (formerly condensed income statement);
    - condensed statement of changes in equity;
    - condensed statement of cash flows (formerly condensed cash flow statement); and
    - selected explanatory notes.

- Alternatively the IRs of an entity may also comprise a complete set of financial statements as prepared in terms of the statement on the presentation of financial statements (IAS 1).
- Basic and diluted earnings per share must be presented on the face of the interim period statement (statement of comprehensive income) containing the components of profit or loss.
- The selected explanatory notes mentioned earlier must contain the following, provided the amounts are material and are not disclosed elsewhere in the IR:
  - a statement that the same accounting policies and methods of computation were used in the interim financial statements as in the most recent prior annual financial statements;
  - a description of the nature and effect of the change if the accounting policies or methods have changed;
  - explanatory comments of the cyclical or seasonal nature of interim operations;
  - the nature and amount of unusual items affecting any of the elements of the financial statements;
  - provided they have a material effect in the current interim period, the nature and amount of changes in accounting estimates of amounts reported in prior interim periods of the current year or changes in estimates of amounts reported in prior financial years;
  - movements in debt and equity securities;
  - dividends paid, distinguishing between ordinary and other shares;
  - certain disclosures in respect of operation segments in terms of IFRS 8;
  - "[e]vents after the interim period that have not been reflected in the financial statements for the interim period" (IASB, 2011a:§16A(h));
  - "the effect of changes in the composition of the entity during the interim period" (IASB, 2011a:§16A(i)); and
  - changes in contingent assets and liabilities since the last annual balance sheet date.
- Changes in accounting policy are addressed in terms of the principles contained in IAS 8.
- IRs should contain the following in respect of corresponding periods:
  - the statement of financial position (balance sheet) at the end of the interim period and the comparative statement of financial position (balance sheet) as at the end of the immediately preceding financial year;

- the statement of comprehensive income (income statement) for the interim period and cumulatively for the current year-to-date, as well as the comparative statement of comprehensive income (income statement) for the comparable interim period in the immediately preceding financial year;
- the statement of changes in equity cumulatively for the current year to the interim date, as well as the comparative amounts for the comparable year-to-date period in the immediately preceding financial year; and
- statements of cash flows (cash flow statements) cumulatively for the current year to date, as well as the comparative amounts for the comparable year-to-date period in the immediately preceding financial year.

- Materiality in the case of IRs is determined in relation to the financial data of the interim period, keeping in mind that, in the case of interim measurements, estimates may be more frequently used.

IFRIC 10 *Interim financial reporting and impairment* interprets paragraph 28 of IAS 34 as stating that an impairment loss on goodwill, once recognised in a specific interim period, cannot be reversed in a subsequent period (IFRIC, 2011:§8).

In 2010/11, a number of changes to the disclosure examples contained in IAS 34.§15B were inserted (IASB, 2011a:§15B). These related specifically to financial instruments. The following must now be disclosed:

- changes in the business or economic environment that have an impact on the fair value of financial items in the statement of the financial position;
- transfers of financial instruments between the different levels of disclosure; and
- changes in the classification of financial assets due to changes in their purpose or use.

In addition, some changes resulting from the 2011 revision of IAS 1 had a consequent impact on IAS 34. These are related to the statements of profit or loss and other comprehensive income and are presented in IAS 34.§11, §11A and §20(b). Paragraphs 11 and 11A refer to where basic and diluted earnings per share should be disclosed, depending on whether the statement of comprehensive income is presented as a single unit, or as both a statement of profit or loss and other comprehensive income.

One other disclosure requirement on financial instruments and their fair values was inserted under the note disclosures required in IAS 34, namely the disclosures prescribed in

Paragraphs 91 – 93(h), 94 - 96, 98 and 99 of IFRS 13 as well as Paragraphs 25, 26 and 28 to 30 of IFRS 7.

None of the changes to IAS 34 subsequent to 2008/9 required a change in the questionnaire used for the empirical work presented in Chapter 5, since the questions asked to assess understanding relate to basic accounting principles, rather than detailed disclosure requirements.

3.6 DIFFERENCES AND SIMILARITIES IN THE DEVELOPMENT OF IRS IN THE US, THE UK AND SOUTH AFRICA

The discussion of the historical developments in respect of interim financial reporting in the earlier part of this chapter can be divided into three main categories, namely, developments in listings requirements, legal requirements and accounting pronouncements. The differences and similarities between these categories are summarised below by comparing developments in the three countries under consideration.

3.6.1 Listings requirements

In respect of listings requirements with regard to IRs, the US (in particular the NYSE) was, in 1910, the first of the three countries dealt with to enter into some form of listings agreement. However, at that stage, the disclosures in IRs were still voluntary. IR disclosures only became a formal listings requirement for the NYSE in 1939.

The UK initially also commenced with voluntary disclosures on interim financial reporting in the form of a recommendation to provide these by the chairman of the London Stock Exchange in 1964. Formal inclusion in the listings requirements followed in 1973.

In South Africa, the first formal listings requirements on interim financial reporting were issued in 1972, although it appears from the Van Wyk De Vries Report (1970:14) that by 1970, listed companies were in fact already issuing interim information on a voluntary basis to such an extent that the Commission felt that their disclosure should be controlled by the Companies Act of 1973.

Subsequent to the initial issuance of listings requirements in respect of IRs, several developments took place in the listings requirements of both the UK and South Africa. The development of listings requirements for the NYSE in the US appear to have been halted with the formation of the SEC, which took over the formulation of disclosure requirements for listed companies, despite the fact that it was the NYSE that first introduced listings requirements in respect of interim financial reporting, more than 50 years before the UK and approximately 60 years before South Africa.

3.6.2 Legal requirements

The legal requirements in respect of interim reporting in the US are contained mainly in pronouncements by the SEC in the Securities Exchange Act of 1934 (as amended). By contrast, the UK direct legal requirements in respect of IRs are no longer contained in the UK's Companies Act of 2006 (as amended). In South Africa, the legal requirements in respect of interim financial reporting were contained in the South African Companies Act of 1973 (as amended) read in conjunction with Schedule 4, as well as the Corporate Laws Amendment Act of 2006. However, direct references to IRs are no longer made in the revised South African Companies Act of 2008, although indirect reference is made to them in section 29 of the Act.

Interestingly, in both the UK and South Africa, interim financial reporting was addressed in their earlier Companies Acts respectively, and the South African Companies Act addressed the matter first. In the case of the US, however, requirements in respect of IRs are still contained in the Securities Exchange Act, but not in the corporate law of the US.

The UK and South Africa now both require half-yearly reports (IRs) to be issued in terms of their listings requirements, but not in terms of their respective Companies Acts, while the US requires quarterly reports (IRs) for all listed companies in terms of Sections 13(a) and 15(d) of the Securities Exchange Act of 1934 (as amended).

In the case of the US, the Securities Exchange Act prescribes the maximum period that may elapse between the interim period-end and the date on which the IRs must be issued or filed – this is 40 days. In the UK, this requirement is contained in the DTR, and not in the Companies Act, and the period is limited to two months (approximately 60 days). In South Africa, the latest Companies Act (South Africa, 2008) also does not address this aspect, but the JSE Listings Requirements state that the IRs must be published within three months from the interim date (JSE Ltd, 2012:§3.15).

The shorter time allowed before interim reports must be filed in the US appears reasonable, as the SEC requires quarterly reporting, as opposed to half-yearly reporting, as is the case in the UK and in South Africa.

3.6.3 Accounting pronouncements

In the UK and in South Africa, to comply with IFRSs in the case of listed companies, the accounting pronouncements issued by the two countries' standard setting bodies require interim financial information to be prepared using the discrete approach, except in the case of income taxes, where an exception is made, and the integral approach is followed. By contrast, the US uses the integral approach when preparing interim financial information.

The accounting pronouncements of the UK and South Africa both require condensed financial statements to be issued when reporting interim information. These should include a condensed statement of profit or loss and other comprehensive income (income statement), a statement of financial position (balance sheet), a statement of changes in equity or equivalent and a statement of cash flows (cash flow statement) and selected explanatory notes. In the case of South Africa (complying with IFRS), and the UK (complying with IFRS for consolidated financial statements), an additional alternative is allowed in terms of IAS 34, whereby a full set of financial statements can be issued at each interim reporting date. However, the DTR in the UK prohibits the use of this latter alternative.

Even though the alternative to provide a full set of financial statements as an IR is still allowed in South Africa, it appears unlikely that companies will follow this route, given the cost and time associated with issuing IRs in this format. In the case of the UK statement on half-yearly reports currently in force, the full set of financial statements is not offered as an alternative to the condensed financial statements.

The US APB Opinion No 28 (as amended), now called ASC 270 (FASB, 2009), does not require companies to present balance sheets and statements of cash flows, but it does encourage the presentation of these statements. However, it would appear that the requirements of Form 10-Q of the SEC ensure that most of the information that one would expect in a balance sheet is presented. In addition, Form 10-Q now also requires that a statement of cash flows be presented. It can therefore be stated that this omission of the balance sheet and cash flow information in the accounting pronouncement of the US on IRs is corrected by the relevant legal requirements.

The accounting pronouncements in the US and South Africa on IRs are not prescriptive in respect of the length of the interim period, but the UK's local statement (ASB Statement: *Half-yearly Financial Reports*) prescribes half-yearly reports (ASB, 2007:§1). In contrast with its local standard, IAS 34, which is applicable to consolidated IRs in the UK, is not prescriptive regarding the length of the interim period.

3.7 SUMMARY OF AND CONCLUSION ON THE DEVELOPMENT OF IRS IN THE US, THE UK AND SOUTH AFRICA

In the case of all three countries considered in this chapter, it would appear that the first formal guidance on what to disclose in respect of interim periods was initially contained in the listings requirements of their securities exchanges. Follow-up guidance in respect of interim reporting was then formalized in the Securities Exchange Act in the US in 1934, the South African Companies Act in 1973, and the UK Companies Act in 1980, only to be removed from the Companies Acts of both South Africa and the UK in the most recent revisions of these Acts. However, the guidance on interim reporting has remained firmly entrenched in US corporate law in the Securities Exchange Act.

Unlike listings requirements and corporate laws governing interim financial reporting early in the 20th century, the first accounting pronouncement on IRs was issued in the US only in 1973. This pronouncement (opinion) has been amended only to a limited extent since then, although its name has been changed to AC 270 in 2009, for reasons elucidated in Section 3.3.3.6 above. In the case of the UK and South Africa, despite listings and corporate law guidance appearing in the 1970s, their respective first accounting standards on IRs were issued only in 1997 and 1998. South Africa later adopted IFRS as the only set of accounting standards applicable to listed companies in South Africa (apart from the AC 500 series in South Africa); consequently, for IRs, IAS 34 became the only accounting standard pertaining to listed companies in South Africa.

The listings requirements of both the UK (now called the DTR) and South Africa therefore prescribe that IRs must be prepared in accordance with IAS 34 (which applies to all South African listed companies and UK companies preparing consolidated accounts). However, in the case of listed UK companies that do not prepare consolidated accounts, IRs should be prepared according to the ASB Statement: *Half-yearly Financial Reports* (ASB, 2007:§2). Although a number of additional disclosures are required by the listings requirements of both the UK and South Africa, the vast majority of the disclosure content and the format of financial information in IRs of the UK and South Africa is now provided in terms of the guidance in their accounting pronouncements.

In South Africa, in particular, the additional disclosures required by the JSE Listings Requirements beyond the ones stipulated in IAS 34 are minimal. These additions relate only to headline earnings, mineral resources and reserves (not applicable for this study, because only retail companies were used in this study for the sample of shareholders), and material changes to estimates of contingent consideration payable or receivable in terms of an acquisition or disposal (JSE, 2011:8.58).

In conclusion, the questionnaire used in the current study was designed to assess the understanding of IRs and their use for investment decisions by individual shareholders of listed South African retail companies. The IRs used in this study, like all other IRs issued in South Africa were prepared in terms of IAS 34, with limited additional information required by the JSE Listings Requirements and are embedded in the South African corporate law environment. This implies a less complex situation than in the past, where guidance on required disclosures contained in IRs originated from several sources (the earlier versions of the South African Companies Acts and listings requirements).

The research design and method used in the study to assess the understanding of the content of IRs by individual shareholders as well as their use of IRs to make investment decisions are addressed in Chapter 4.

CHAPTER 4:
RESEARCH DESIGN AND METHOD

4.1 INTRODUCTION

The primary objective of the study was to determine whether individual shareholders of South African listed retail companies understand the context[49] and content[50] of IRs.

The study's secondary aims, which are closely associated with the primary objective, related to individual shareholders' investing in shares and using IRs, and were divided into two categories: Category 1 dealt with investment decisions and the use of IRs for investment decisions, while Category 2 dealt with various other matters related directly to IRs. The first secondary objective under Category 1 was to establish how individual shareholders made investment decisions (on their own initiative or via financial advisors); the second endeavoured to establish what sources of information individual shareholders use when taking investment decisions; the third aimed to conclude whether individual shareholders deem IRs to be important for making investment decisions; the fourth aimed to determine what other crucial information individual shareholders would prefer to have in IRs that is not provided currently, in order to facilitate investment decisions. The first of the secondary objectives in Category 2 investigated in what sequence individual shareholders would prefer the individual components of the IR to be presented; the next aimed to establish whether individual shareholders read the components of the IR and to what extent. The seventh and last secondary aim was to determine in what medium of communication individual shareholders would prefer to receive the IR.

To address the problem that individual shareholders of South African listed retail companies did not receive financial and other information at intervals shorter than a year, IRs were

[49] The **context** of the IRs refers to the environment in which these statements/reports are presented. In this study it specifically refers to with whom the legal responsibility for issuing IRs resides, whether IRs are audited or not, and what the objective of issuing an IR is.
[50] The **content** of IRs in this study refers to the financially related information (content) presented in IRs in terms of IAS 34 and the JSE Listings Requirements. In this study it would include, the condensed statement of financial position (balance sheet), the condensed statement of comprehensive income (income statement), the condensed statement of cash flows, the condensed statement of changes in equity and selected notes to the financial statements, but not management commentary, which is a non-standardized, open-ended component of the IR that could not be assessed effectively by way of the postal questionnaire used in this study.

introduced by standard setting bodies throughout the world and in South Africa. This intervention to solve a real-life problem has been in operation for a number of years and in this study related to South African listed retail companies, it is endeavoured to do scientific research to establish whether individual shareholders understand the context and content of IRs and, amongst others, use IRs in investment decisions. The effectiveness of the intervention (IRs) is thus subjected to scientific investigation to establish whether the report achieved its objectives and if it can be improved upon, given the responses of individual shareholders. This implies a positive research paradigm, even though understandability is a qualitative characteristic contained in the conceptual framework of the IASB.

To collect the information necessary to meet both the primary and secondary aims set out above, an anonymous postal survey was conducted using a questionnaire distributed to the individual shareholders of three retail companies[51] listed on the South African stock exchange, the JSE.

Given the risk of a low response rate in the case of a postal survey (Malhotra, 2010:225), a number of steps were taken to improve the response rate in this study. These are considered in Section 4.5.1, below.

In this chapter the following are addressed:

- an overview of the development of the questionnaire sent to individual shareholders;
- the process used to test, refine and improve the questionnaire before distributing it to the individual shareholders selected for the study and assessing their understanding of IRs;
- the identification of the population of individual shareholders and the selection of the samples;
- the initial distribution of the questionnaires, as well as the follow-up mailing event;
- the response rates achieved for the postal questionnaire survey and testing for non-response bias;
- the coding, processing and preparation of the data; and
- the statistical techniques used in analysing the data.

[51] See Section 4.4, below.

4.2 DEVELOPMENT OF THE QUESTIONNAIRE

4.2.1 The contributions of earlier studies

The questionnaire used in this study was based on the questionnaires used by Lee and Tweedie (1975, 1976, 1977) in their surveys dealing mainly with the understanding of annual financial reports. Their main study on individual shareholders was interview-based, but this South African study on IRs was conducted by postal questionnaire, given the distances that would have to be travelled to conduct interviews in a country where the main cities are situated far apart and to accommodate a larger sample. A postal questionnaire survey was thus used for data collection, in line with a similar study on annual financial reports conducted by Bartlett and Chandler in the UK in 1994/1995 (Bartlett & Chandler, 1997:249).

Although the questions contained in the questionnaire on IRs were based on those of Lee and Tweedie (1975, 1976, 1977), some of the questions in their studies were adapted, some were removed and others were added to take into account a number of aspects. The following factors, amongst others, necessitated amendments to the original questionnaires:

- the research questions now relate to IRs, rather than to annual financial reports;
- this study was conducted by means of a postal questionnaire;
- international harmonization of financial reporting standards has been in effect for a number of years and this has had an impact on terminology used today;
- the formats of financial statements (and IRs) have changed substantially since 1975 (the date of the last company financial statements used in Lee and Tweedie's study);
- some information required to answer questions on annual financial statements used in Lee and Tweedie's studies would not appear in the condensed financial statements contained in IRs, and therefore questions related to such information had to be removed. For example, questions on financial ratios that appeared in Lee and Tweedie's (1975) original study had to be excluded, because the relevant information was not necessarily available from the condensed financial statements in IRs (see Figure 4.1, below).

Similar to the approach followed in this study, as described above, Bartlett and Chandler (1997) in their UK postal questionnaire survey on annual financial reports also used the questions of Lee and Tweedie in respect of annual financial reports as a point of departure and adapted those questions for developments in financial accounting from 1975 to 1995

(Bartlett & Chandler, 1997:249). Furthermore, later studies on the usefulness of different aspects of annual reports to various user groups, such as the study by Naser *et al*., (2003) in Kuwait, were also examined to gather information on pertinent additional questions that were contained in those studies (Naser *et al*., 2003).

In summary, the questions used in assessing understanding in Lee and Tweedie's (1977) main study on the understanding of individual shareholders of annual financial reports were divided into five main areas. These were the financial reporting environment, the main valuation bases used in accounting with regard to particular assets, the content of specific financial statements, commonly used accounting terminology, and financial ratios (Lee & Tweedie, 1977:28,29).

Although four of the five areas identified by Lee and Tweedie (1977) were retained for the current South African study on IRs, the five areas used to assess understanding were reclassified into two main categories (context and content) for this study on IRs, as is elucidated in Figure 4.1, below.

Figure 4.1: Comparison of main categories of questions on understanding

Original Lee & Tweedie (1977) categories in respect of annual reports	Revised main categories in this study on IRs	Composition of revised areas for this study on IRs
• The financial reporting environment	Context of IRs	• Reporting objective • Legal responsibility • Accuracy of information (level of assurance)
• Main valuation bases for particular assets	Content of IRs	• Main valuation bases for particular assets
• Content of specific financial statements		• Content of specific condensed financial statements
• Commonly used accounting terminology		• Commonly used accounting terminology
• Financial ratios		• Eliminated in the study on IRs, since relevant information not available in all instances

Source: Adapted from Lee and Tweedie (1977:28,29)

4.2.2 Main sections of the questionnaire (see Appendix A for the complete questionnaire)

The questionnaire was distributed to individual shareholders. The questions in the questionnaire were divided into two main sections, namely Sections A and B.

Section A dealt with background information, focusing on demographic and related information[52] about the respondents (gender, age, level of education, accounting knowledge, occupation/experience, employment status, number of shares held, Rand value of shares held, number of companies in the investor's portfolio, information on investment objectives and decisions). In addition to the demographic and related information, data were collected on the sources of information that respondents used for investment decisions, as well as the importance and level of use of IRs for investment decisions.

Table 4.1, below, contains a list of the questions in Section A in condensed format with a justification for their inclusion.

Table 4.1: Questions in Section A of the questionnaire and rationale for their inclusion in the questionnaire

Questions 1 to 9:

1. What is your **gender**?

2. How **old** are you? (Please indicate **completed years**)

3. What is your **highest academic level** of education?

4. Was **Accounting** one of your **major** (*final year*) degree / diploma / certificate subjects?

5. What **professional qualification** do you have (if any)?

6. How many **shares** of the company, identified in the accompanying *Interim Financial Report*, are **in your portfolio** (collection of shares)?

7. How many **companies** on the **JSE** do you **currently have shares** of in your portfolio?

8. How would you **describe** your **current employment status**?

9. What **field** are you (or were you) working in?

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[52] See Section 5.2.

Rationale: Questions 1 to 9 were designed to collect the demographic information on respondents, namely individual shareholders.
Question 10: **10.** What is your **single** most important **objective** (goal) when investing in shares?
Rationale: Question 10 was designed to determine the investment objectives of the respondents.
Question 11: **11.** How do you **currently** make investment **decisions** to *buy*, *sell* or *hold* shares in **any** company?
Rationale: Question 11 was designed to determine how the respondents made investment decisions.
Question 12: **12.** In **general**, how **often** do you **consult** the following sources of **information** when making an investment decision to *buy*, *sell* or *hold* shares in **any** company?
Rationale: Question 12 was designed to determine which sources of information respondents used when making investment decisions.
Question 13: **13.** In **general**, how **important to you** are the following components of the *Interim Financial Report* when making a decision to *buy*, *sell* or *hold* shares in **any** company?
Rationale: Question 13 was designed to assess the perception of respondents as to the importance of the individual components of the interim financial report when making investment decisions.
Question 14: **14.** During the **last 8+ years** (since 2000), approximately **how many times** have you **made use** of the *Interim Financial Report* in **taking** investment **decisions** to *buy*, *sell* or *hold* shares in respect of any of your **shareholdings**?
Rationale: Question 14 was designed to determine how often respondents used IRs when making investment decisions. Note that since the questionnaire was administered during 2009 for the first time, a period of eight years was used as point of departure.

Section B addressed the assessment of the context of IRs, but mainly focused on the assessment of understanding of financially-related information (content) contained in the IR.[53] In this section, information about the perceived relevance of interim information to decision-making, the understanding of the context and content of the IR (see List of definitions of terms and concepts), the extent to which respondents read IRs and what would dissuade them from reading IRs, their perceived understanding (see List of definitions of terms and concepts) of IRs as well as recommendations in respect of improvements to IRs and related matters, were assessed.

Table 4.2 contains a schematic presentation of the questions in Section B (dealing with context and content) in condensed format and reasons for including the questions in the questionnaire.

Table 4.2: Questions in Section B of the questionnaire and rationale for their inclusion in the questionnaire

Question 15: **15.** Please indicate the **extent in general** of the **relevance** of the **information** contained in the *Interim Financial Report* in respect of your **making** investment **decisions** to *buy*, *sell* or *hold* shares.
Rationale: Question 15 was designed to assess whether respondents considered information in the interim financial report relevant to making investment decisions.
Questions 16 to 18: **16.** Who do you believe is **legally responsible** for the *Interim Financial Report* of a Company? **17.** Is the *Interim Financial Report* **accompanying** this questionnaire **audited** or not? **18.** In your view, what is the **single most important** objective of providing an *Interim Financial Report*?
Rationale: Questions 16 to 18 were designed to test whether respondents understood the context in which IRs were issued.
Questions 19 to 20: **19.** To what **extent** do you **read** the following **components** of the *Interim Financial Report*? **20.** Which of the following **factors** would **dissuade** you from reading the *Interim Financial Report* **thoroughly**?
Rationale: Questions 19 to 20 were designed to assess the extent of reading and aspects that would dissuade respondents from reading the interim financial report.

[53] See Section 4.2.4, below.

Question 21:

21. How **well** do you **understand** the following **components** of the *Interim Financial Report*?

Rationale: Question 21 was designed to determine the perceived understanding of the individual components of the interim financial report by respondents.

Questions 22 to 26:

22. What **basis of valuation** is used to determine the **carrying amounts** (book values) of the following items included in the *Condensed Balance Sheet / Statement of Financial Position*?

Basis of valuation	**Original cost price**	**Original cost less accumulated depreciation**	**Replacement cost**	**Lower of cost and net realisable value**	**I really do not know**
Property, plant and equipment (fixed assets)	**1**	**2**	**3**	**4**	**5**
Inventory (stock)	**1**	**2**	**3**	**4**	**5**

23. To what does the **operating lease accrual/liability/obligation** (the line-item) in the *Condensed Balance Sheet / Statement of Financial Position* **refer**?

The amount payable in respect of an operating lease in the 12 months subsequent to the balance sheet / statement of financial position date	**1**
The accrual of operating lease payments in order to recognise these payments in the income statement on a straight-line basis over the lease term	**2**
The correction of the erroneous application of the lease standard in the past	**3**
I really do not know	**4**

24. Consider **each** of the **statements** below and provide an **answer** to **each**. (**Circle** a **single number** between "**1**" and "**3**" for ***each*** "**Statement**" below)

Statement	**Yes**	**No**	**I really do not know**
The profit before tax line-item on the *Condensed Income Statement / Statement of Comprehensive Income* represents the difference between income/revenue received and/or earned and expenses paid and/or incurred during the six months under review	**1**	**2**	**3**
The line-item for tax in the *Condensed Income Statement / Statement of Comprehensive Income* includes merely the taxation payable to SARS	**1**	**2**	**3**
The *Condensed Statement of Changes in Equity* reflects all movements in equity (share capital and reserves) that occurred during the six month period under review	**1**	**2**	**3**

The final balances on the *Condensed Statement of Changes in Equity* can be linked to condensed balance sheet items at the end of the six month period	**1**	**2**	**3**
Net cash flows from operating activities on the *Condensed Cash Flow Statement / Statement of Cash Flows* include interest payable and dividends payable	**1**	**2**	**3**
The purchase of property, plant and equipment (fixed assets) on credit, would represent a cash outflow under investing activities on the *Condensed Cash Flow Statement / Statement of Cash Flows*	**1**	**2**	**3**

25. What do you **understand** by the term "**Accounting policy**"? (**Circle** a **single number** between "**1**" and "**4**" below)?

It is the policy used when assessing the creditworthiness of the customers buying on credit from the company	**1**
It is the policy used to determine the amounts used when preparing the financial statements	**2**
It is the policy the company follows with regard to the exchange and/or return of goods sold to customers on credit	**3**
I really do not know	**4**

26. Are the **accounting policies** used in the *Interim Financial Report* the **same** as those used in the Annual Financial Statements of the company? (**Circle** a **single number** between "**1**" and "**3**" below)

Yes	**1**
No	**2**
I really do not know	**3**

Rationale: Questions 22 to 26 were designed to assess the understanding of respondents of the content of IRs as a whole.

Question 27:

27. Which **one statement** of the following corresponds **most closely** to your view of *Interim Financial Reports?*

Rationale: Question 27 was designed to assess the perception of respondents as to the understanding and relevance of the information contained in the interim financial report as a whole (content).

Question 28:

28. Would you consider the information contained in the *Interim Financial Reports* as **adequate** for you as a shareholder to make investment decisions?

Rationale: Question 28 was designed to ascertain the perceptions of respondents on whether enough information was presented in IRs to make investment decisions.

Question 29:

29. List **one crucial item** of **additional information** that is not presented in the *Interim Financial Report* at this stage that you **would require** to make investment decisions.

Rationale: Question 29 was designed to determine what crucial additional information

respondents would like to see in the interim financial report with a view to improving the content of the interim financial report and thereby facilitate making investment decisions.
Question 30: **30.** Please indicate the **sequence** in which you would prefer the **components** of the *Interim Financial Report* to be **presented**.
Rationale: Question 30 was designed to establish whether the sequence of information as it appeared in the interim financial report was acceptable to respondents.
Question 31: **31.** How would you **prefer** to **receive** the *Interim Financial Report*?
Rationale: Question 31 was designed to establish how respondents would prefer to receive the interim financial report (what medium of communication).

As pointed out earlier in this section, the questions contained in Section B included several questions to assess the understanding of the context as well as content of the IR (see Figure 4.1, as well as the List of definitions of terms and concepts for more clarity on the meaning of context and content). In total, seven questions (some with multiple subsections) were included to test the understanding of individual shareholders of the information contained in the IR.

No questions were asked in respect of commentary on the interim period under review provided by the directors for each different company, because such commentary would not be standardized and would differ according to the specific circumstances of each company. The understanding of the context and content of IRs was thus tested on a broad base.

The questions on the **context** of IRs dealt with the following:

- Who is legally responsible for the IR (Q16, Variable V36)?
- Was the IR audited or not (Q17, Variable V37)?
- What is the most important of objective of providing an IR (Q18, Variable V38)?

The questions/subsections of questions on **content** (financially related information) were the following:

- those dealing with the statement of financial position addressed assets as well as the valuation bases of assets (Q22, Variables V57 and V58) and liabilities (Q23, Variable V59);
- those dealing with revenue and expenditure and the tax expense contained in the statement of financial performance (Q24, Variables V60 and V61 respectively);

- those dealing with the statement of changes in equity, especially changes in equity (Q24, Variable V62) and its relationship with the statement of financial position (Q24, Variable V63);
- those dealing with the cash flow statement, addressing operating activities (Q24, Variable 64) and investing activities (Q24, Variable 65); and
- two questions (Q25, Variable V66, and Q26, Variable V67), dealing with notes to the financial information; specifically accounting policy, which has an overarching effect on all financial information presented in financial statements.

Unfortunately, in the case of Q23 (Variable V59) dealing with liabilities, the time that had elapsed between the issuance of the previous IRs and the IRs accompanying the questionnaires resulted in the presence of the specific type of liability tested only in the case of the first company sampled, and not in the case of the two companies sampled subsequently. To ensure that the understanding of IRs by individual shareholders of the three companies would be comparable, this question had to be discarded from the final assessment of understanding. On further investigation of the results during the testing of the questionnaires,[54] it was also evident that very few of the members of the pilot groups were able to answer this question. Consequently, the impact of the exclusion of this data on the total percentage scores achieved by respondents would have been negligible, and it therefore does not negate the validity of the outcome of the assessment of understanding.

4.2.3 Mark allocation for individual questions assessing understanding

To enable the assessment of the level of understanding of each respondent, marks were allocated to each correct answer of the associated questions contained in the questionnaires. The mark allocation was kept as simple as possible to ensure consistency and the following principles were applied in allocating marks:

- one mark was awarded where the answer to a question was evident from information in the IR or from the various options provided as part of the question;
- two marks were awarded to questions where the answer to the question was not evident from the IR and required a broader knowledge of accounting matters;
- three marks were awarded in one instance, where individual shareholders needed detailed accounting knowledge to answer the question.

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[54] See Section 4.3, below.

Once the initial design and mark allocation of the questionnaire had been finalized, the questionnaire was subjected to testing to ensure that the required information would be collected and the stated objectives achieved once the questionnaires were distributed to respondents, and filled out and returned by them.

4.2.4 Assessment of understanding of the context and content of IRs

In the 1977 study by Lee and Tweedie, face-to-face interviews were conducted with respondents, and open-ended questions were asked in many instances (Lee & Tweedie, 1977:24,36). In view of the range of responses, those researchers categorized the understanding of respondents into levels of understanding, namely "reasonable understanding", a "vague understanding" and "no understanding" to facilitate sensible analysis. However, these classifications varied, depending on the specific item in the annual report being assessed for comprehension, and were therefore not standardized (Lee & Tweedie, 1977:35-41).

Lee and Tweedie (1977:45-48) then proceeded to define more precisely the levels of understanding of respondents by constructing an index of understanding using the assessment of the reasonableness of answers provided by the interviewees. In the case of this study, which deals with individual shareholders' understanding of IRs, however, the fact that a postal questionnaire was administered when collecting data, the smaller number of questions, as well as the fact that the questions used were, of necessity, not open-ended, precluded the construction of a similar index. A decision was thus taken to assess the understanding of IRs in a more fundamental manner.

This was done by determining the total possible marks that could be achieved when considering all the questions used to assess the understanding of the context and/or content of the IRs and expressing the actual marks achieved by each respondent for the questions related to the understanding of the IRs as a percentage, called the **total percentage score** (this term is used extensively in Chapter 5 of the current study and is defined in the List of definitions). A detailed explanation on exactly how individual marks were allocated is provided in Sections 4.2.2 and 4.2.3, above, where the questionnaire questions and marks awarded for each question are considered.

The actual marks allocated per individual question associated with assessing understanding, are set out in Table B1 in Appendix B. The maximum number of marks associated with questions on context was 4 out of 4, while the maximum marks associated with content was 18 out of 18. The total number of marks that could be obtained when questions on context and content were combined was 22 out of 22.

The individual total percentage scores of respondents to the survey were calculated, as well as the mean of total percentage scores for all respondents to the survey. These total percentage scores were compared to a total of 50%, which is deemed to be the acceptable benchmark of understanding when assessing the knowledge levels of university students in South Africa. The assumption is that students with more than 50% are considered to have mastered the prescribed study material adequately, while students with less than 50% are considered not to have mastered the prescribed study material. Using the mode or median of the total percentage scores of respondents to the questionnaire was also considered for purposes of assessment, but the comparability of the mean with a standardised measure of assessment of understanding led to its being chosen as the benchmark in this study.

4.3 TESTS TO IMPROVE THE QUALITY OF THE QUESTIONNAIRE

A number of procedures were followed to ensure that the questions were unambiguous and would not discourage respondents from completing the questionnaire, and that the questionnaires would collect the information required to complete the study successfully. These procedures are addressed below.

In the initial phase of testing, the first version of the questionnaire was distributed to three experienced researchers in the accounting field, as well as a statistical consultant (a specialist in questionnaire design) for commentary on the format, clarity and quality of the questionnaire. Any comments received were considered, and the questionnaire was adjusted accordingly. Thereafter, the revised questionnaire had been evaluated by a second experienced statistical consultant to finalize the layout of the questionnaire to ensure that the recording of the coded data contained in the completed questionnaire could be captured as effectively and efficiently as possible. The latter step was considered crucial, given the volume of data anticipated from the survey.

The second (revised) version of the questionnaire was sent to two academic trainees at the Department of Accounting at the University of Pretoria (Pilot Group 1, see Appendix B, Table B1). The questionnaire was accompanied by a copy of the IRs of the first company selected for the survey (Company A), dated 31 December 2007. The first questionnaire of the study was distributed in February 2009, together with the 31 December 2008 IR. Academic trainees are former students (ranked in the top 20% of their year group) who completed their BCom (Hons) in Accounting Sciences at the end of the previous academic year and who wrote and passed the technical component of their professional examinations to become South African chartered accountants. They are seconded from their training offices to the university to spend the first year of their training contract in an academic environment. Due to their perceived level of technical competency, the academic trainees were identified as members of the pilot group with a high level of understanding of the content of IRs.

To facilitate the completion of all the questions in the questionnaire, simulated information was provided on the number of shares and number of companies on the JSE that the members of the pilot group were asked to imagine that they held shares in, as well as on the number of times they had used the IRs of the company over the period since 2000. The IR for the previous period (ended 31 December 2007) was used for the pilot, since the IR for 31 December 2008 had not been prepared at that time.

This pilot was done to determine whether any technical errors or ambiguities in the questionnaire were evident and to assess the approximate time needed to complete the questionnaire, before distributing it to a larger pilot group. One technical error was detected and corrected, creating a third version of the questionnaire. The two pilot testers indicated that it took them each approximately 13 minutes to complete the questionnaire. At this point, the total percentage scores obtained by respondents in answering the seven questions (see Sections 4.2.3 and 4.2.4, above) in respect of the assessment of understanding of both context and content* (see scores marked with * directly below) included in the questionnaire, were determined for the first time – the members of Pilot Group 1 obtained 86%* and 91%* respectively, and errors made by the two members of the pilot group were due to carelessness, rather than a lack of knowledge.[55] This confirmed the researcher's contention that the questions were not excessively difficult.

[55] See Appendix B, Table B1.

This third version of the questionnaire was distributed to Pilot Group 2. Once again, as in the case of Pilot Group 1, simulated information on the number of shares, the number of companies on the JSE they supposedly held shares in and the number of times they used the IR over an eight-year period was provided to facilitate the completion of the entire questionnaire. Five of the eight members in Pilot Group 2 were selected based on the premise that they had little or no accounting background, while three individuals selected were considered to have a good level of accounting knowledge, based on their professional qualifications and field of work. Once again, their comments and insights (limited in scope and excluding the correctness of the technical accounting content of the questionnaire) were considered and processed to produce the final version of the questionnaire. At this stage, it was concluded that respondents would, on average, take approximately 15 minutes to complete the questionnaire.

In total, Pilot Groups 1 and 2 consisted of five individuals with a sound level of accounting knowledge, and five with limited or no accounting knowledge. The total percentage scores obtained by individual respondents for the five questions in respect of the assessment of understanding included in the questionnaire (see Appendix B, Table B1) indicated that the set of questions successfully distinguished between users with a sound accounting background and those without it.

4.4 SELECTION OF THE POPULATION AND SAMPLES

4.4.1 Selection of the companies used in the survey

In view of the fact that the information presented in IRs may be considered complex by individuals without a sound accounting background, it was decided to send the questionnaires to individual shareholders of retail companies only, as the activities of the majority of these companies are well-known to the public at large, and their operations and accounting are easier to understand. This contrasts with information on, for example industrial, mining, construction and financial services companies, where specialized accounting may be used in presenting financial and other information. This selection was an attempt to level the playing field between individual shareholders with different levels of knowledge and accounting experience, and thereby to increase the response rate and quality of the data collected in the survey.

Two sectors on the JSE contain retail companies, namely the Food & Drugs and General Retail Sectors. These two sectors are collectively known as the Retail Sector in the JSEs market reports. As indicated earlier, the intention was that individual shareholders should not require specialist accounting knowledge related to the industry in which the company operates in order to answer the questionnaire.

To improve the validity of the information collected in the survey, it was decided to select three well-known retail companies instead of only one, as was done in the studies by Bartlett and Chandler (1997:250) and Lee and Tweedie (1975:4, 1976:304, 1977:12). A number of the largest companies listed in the Retail Sector were approached, and three companies granted permission to use their IRs as part of the study and to assist with the study. To ensure their anonymity, the three companies were identified as follows:

- Company A, with an interim date of 31 December 2008;
- Company B, with an interim date of 28 February 2009; and
- Company C, with an interim date of 31 December 2009.

The interim dates of the three companies were not the same. Although the day and month components of the interim dates of Companies A and C were the same, the actual dates were separated by a full year. This is a result of the fact that these companies were approached sequentially, as the search for companies that were prepared to assist with the research project proved to be challenging. To improve the response rate of the survey and facilitate the answering of the questionnaire, it was decided to include the questionnaire in the same envelope as the original IRs sent out by the respective companies and also to include a black and white copy of the IRs with the questionnaire in the follow-up (second) mailing event.

It might be possible to identify the three companies used in the survey if their individual market capitalizations in Rands on the respective interim dates are provided, so these are not provided here. Also note that in the case of Company B, the interim date of 28 February 2009 and the closest trading date on the JSE (27 February 2009), did not coincide. Nevertheless, the combined market capitalizations of the individual companies were expressed as a percentage of the total market capitalization of the Retail Sector of the JSE. This provided an indication of the magnitude of the market capitalizations of the companies involved, whilst still protecting the identities of the three companies involved in the research. The relevant market capitalization percentages on the reporting dates of the three IRs used in the study are set out in Table 4.3, overleaf.

Table 4.3: Market capitalization summary on the relevant interim dates

Date of IR	Total market capitalization of the Retail Sector Rand Million	Combined market capitalization of the three companies presented as a % of the Retail Sector market capitalization
31 December 2008	148 685	30%
28 February 2009	132 505	31%
31 December 2009	183 960	32%

Companies A and B were consistently among the six largest companies in the General Retail sector of the JSE, based on market capitalization during the period of selection, while Company C was one of the larger companies based on market capitalization in the Food & Drug Sector.

It is clear from the above table that the three companies selected represented a substantial portion (approximately 30+ %) of the total market capitalization of companies in the Retail Sector of the JSE on the respective dates.

Note that although the data was gathered in early 2009 and 2010, it is believed that the time that has lapsed to completion of the study, would not impact on the validity of the data, since the questions included in the questionnaire tested basic accounting knowledge that would not be influenced by changes in accounting standards.

4.4.2 Selection of shareholder samples

Two identical print runs of the lists of address labels with names and addresses of all the shareholders of each of the three companies involved in the survey were obtained from the transfer secretary company that dealt with the three companies on the respective dates listed in Table 4.3. These lists were those that the transfer secretaries provide to the company secretaries for purposes of mailing IRs, and it was argued that those lists would contain the most up-to-date contact details for shareholders. Two print runs were required, since two mailing events were planned – the first by each company involved, together with the initial release of the IR, to ensure that the questionnaire and the IR were received simultaneously; the second in the follow-up mailing event executed by the researcher (this time including a copy of the relevant IR with the questionnaire in case a shareholder had misplaced the original IR).

Since the three companies used the same transfer secretary company, it simplified the process. The above-mentioned lists were obtained after securing written permission from the management of each of the three companies involved in the survey, prior to the commencement of each stage of the survey. The lists of address labels obtained were based on the share registers of the selected companies.

The transfer secretary company was requested to divide the shareholders of each of the three companies into individual and institutional shareholders according to their in-house parameters regarding these two categories. The study adopted a definition similar to that used by Lee and Tweedie (1975:4, 1976:4) for individual shareholders, and adapted it slightly for South African circumstances. Individual shareholders were thus defined as follows for the purposes of the current study:

> All shareholders excluding partnerships, joint shareholders, investment clubs, deceased estates, trusts, insurance companies, nominees, investment managers, medical aid funds, pension, provident and other retirement funds for each company as well as shareholders that reside outside the borders of South Africa and Namibia.

To ensure that all individual shareholders were identified, the researcher perused the individual and institutional shareholder lists as provided by the transfer secretary company. During this process, individual shareholders were identified and marked one by one after ensuring that they complied with the definition above.

The above procedures did not take place simultaneously for Companies A, B and C, as their interim dates were spread over a period of one year, ranging from 31 December 2008, 28 February 2009 and 31 December 2009. This presented the problem that sampling could not be done in a single session for all three companies, as the individual shareholders of the companies could change from one interim financial reporting date to the next, whenever they bought and sold shares.

The problem was solved by using the systematic random sampling technique to select individual shareholders. This ensured that the selection remained random from a statistical perspective, even though sampling occurred on the different reporting dates of each of the three companies. In view of the fact that the participation of Companies A to C was not confirmed at the start of the project and that it was therefore not possible to determine the size of the total population of individual shareholders, it was decided to select every second individual shareholder (that is, 50% of all individual shareholders) for the survey. This was done in an attempt to ensure that a sufficiently large number of shareholders was selected and would respond to the questionnaire sent out in the survey.

To maintain randomness, the starting point for the systematic samples in the case of each company at the respective dates when the samples were drawn was determined by tossing a coin. Heads indicated starting with the first individual shareholder on the list of individual shareholders, and tails starting with the second one.

Once the above procedure had been performed, it was determined that the three companies involved in the survey had a total of 12 976 individual shareholders, as identified in terms of the definition explained earlier in this section and elucidated in Tables 4.4 and 4.5.

Table 4.4: Total number of individual shareholders per company at the interim reporting dates

Company	Number of individual shareholders identified
Company A	3 814
Company B	898
Company C	8 264
Total population	12 976

Applying the 50% systematic selection rate to the population of individual shareholders mentioned in Table 4.4, resulted in a sample of 6 488 individual shareholders who were eventually surveyed.

Table 4.5: Total number of individual shareholders per company at the interim reporting dates included in the sample for the survey

Company	Sample size: individual shareholders
Company A	1 907
Company B	449
Company C	4 132
	6 488

The individual shareholders selected on the original lists of address labels were transferred to the second set of address label list to be used during the planned follow-up (second) mailing events mentioned in Section 4.4.1, above, and Section 4.5.4, below.

4.5 DISTRIBUTION OF THE QUESTIONNAIRES FOR THE SURVEY

4.5.1 Background

Companies A, B and C routinely distribute their IRs to their shareholders based on address label lists provided by the transfer secretary company, as mentioned in Section 4.4.2, above.

To improve the response rate of the postal survey, a number of steps were taken:

- In view of the fact that the survey assessed understanding of IRs by individual shareholders, and that this could be a sensitive issue, the survey was kept anonymous. Aaker, Kumar, Day and Leone (2011:225) indicate that using mail surveys may counter fear of a lack of confidentiality as a potential cause of low response rates.
- A follow-up mailing was done six weeks after the initial mailing event, as is indicated in Section 4.5.4, below. Aaker *et al.* (2011:227) indicate that follow-ups or reminders may increase response rates.
- The questionnaire, in both the first and second mailing event, was accompanied by a prepaid reply envelope, as well as a persuasive letter of introduction, and the length of the questionnaire was limited to eight pages. According to Aaker *et al.* (2011:225,227), these precautions could improve the response rate of a survey conducted by mail.
- To improve the response rate further, each individual shareholder received the research questionnaire simultaneously with the IR to which it related, during both the first mailing event (the original IR) and the second mailing event (a copy of the IR) for each of the three companies. In order to ensure that respondents received the questionnaires, together with the related IRs, during the first mailing event, it was necessary to obtain permission from the companies involved to include the letter of introduction in respect of the research project, a prepaid reply envelope and questionnaire of eight pages (printed back-to-back on four sheets) in the same envelope as the IR when the IRs were mailed to the shareholders. During the second mailing event, the same set of documents, together with a copy of the IR of the company concerned, was mailed to the same shareholders by the researcher and his team.

In the case of Companies A and C, the initial (first) mailing event was not handled by the transfer secretary company, although it still provided the lists of address labels. In the case of Company A, the researcher and his team loaded the envelopes with the survey documentation, but the loading of the IRs and the actual mailing was handled by a distribution company nominated by Company A. In the case of Company C, the appointed distribution company loaded both the survey documentation and IRs, and then mailed the envelopes. However, in the case of Company B, the researcher and his team loaded the survey documentation in the envelopes and the transfer secretaries handled the loading of the IRs and mailing of the envelopes on behalf of the company. The problems created by the different approaches were addressed as explained below.

4.5.2 First mailing event – Companies A and B

- Step 1: Based on the number of individual shareholders in the sample identified in respect of each of the companies from the lists of address labels, the researcher was supplied with the correct number of envelopes to be used for mailing of the IRs and other correspondence.
- Step 2: The researcher and his team loaded each of these envelopes with the following survey documents: a letter of introduction in respect of the research, a prepaid reply envelope and the research questionnaire.
- Step 3: The researcher performed an audit on the unsealed but loaded envelopes by systematically checking each tenth envelope to ensure that the three documents listed in Step 2 above were present in each envelope. Corrective action was taken in two cases.
- Step 4: The unsealed but loaded envelopes were then labelled by attaching the address labels of all individual shareholders identified in the sample to these envelopes.
- Step 5: To ensure the completeness of the sample, the researcher performed an audit on the used address label lists and confirmed that only the labels of those individual shareholders selected had been affixed to the loaded envelopes.
- Step 6: The loaded envelopes were returned to the transfer secretary company, together with the lists of address labels used by the researcher and his team (that is the lists minus the labels for the shareholders sampled). This meant that the transfer secretary company received the lists of address labels containing only the address labels of those shareholders who did not form part of the sample for the survey, as

well as the labelled envelopes loaded with the content related to the survey. In the case of Company A, the loaded (but unsealed) envelopes were couriered to a distribution company as per instruction of the relevant company secretary to insert the original IRs and mail the sealed envelopes. In the case of Company B, the insertion of the original IRs in the loaded envelopes, the sealing and mailing of the envelopes were all executed by the transfer secretary company.

- Step 7: For the individual shareholders who did not form part of the sample, the distribution company in the case of Company A and the transfer secretary company in the case of Company B labelled the non-sampled envelopes, loaded and sealed all envelopes with the original IRs and mailed them on behalf of the companies.

4.5.3 First mailing event – Company C

The procedure in the case of Company C was similar to Steps 1 to 7 above, except that this company preferred the entire loading process and the labelling of the envelopes to be done at the premises of their distribution company. To limit the administrative load of the distribution company, the researcher and his team prepared a survey information packet (a letter of introduction, a prepaid reply envelope and a questionnaire) for each envelope. The researcher audited the packets of research documentation and, once he was satisfied with the completeness thereof, couriered these packets to the distribution company.

The researcher consequently arranged to be at the premises of the distribution company during the mailing event, and with the assistance of the personnel of the distribution company loaded each envelope with the research documentation. The loaded envelopes were then audited, and these envelopes were labelled with the addresses of individual shareholders forming part of the sample. Once again the used address label lists were audited to ensure that none of the individual shareholders who were to be part of the sample had been accidentally omitted.

The distribution company lastly loaded all envelopes (sampled and non-sampled) with the original IRs, labelled the envelopes to shareholders not sampled, and sealed and mailed all the envelopes.

4.5.4 Second mailing event – Companies A, B and C

A total of 6 488 individual shareholders were identified as the sample size during the first mailing.[56] The fact that the survey was anonymous[57] created a situation where it was impossible to determine which of the shareholders had responded to the first mailing event and which had not. This necessitated the follow-up (second) mailing event to be done for all shareholders in the sample. In the case of each of the three companies in the survey, a second mailing event was undertaken six weeks after the first. Recipients had been pre-warned of the fact that a second mailing event could occur in the letter of introduction in respect of the research mailed to each respondent during the first mailing event.

In the end, a total of 12 976 questionnaires were distributed to individual shareholders in two mailing events – 6 488 individual shareholders received the research questionnaire twice within a six-week period. The procedure followed during the second mailing event was exactly the same for each of the three companies, as it was not necessary to adhere to specific instructions by the individual companies during the second mailing event. As mentioned before, a black and white copy of the IRs of the respective companies, instead of the original IR, was included in the envelopes during the respective second mailing events to facilitate ease of completing the research questionnaire. The procedure was the following:

- Step 1: Based on the number of individual shareholders in the sample identified for each company, envelopes to be used for mailing the IRs and the research correspondence were supplied by the researcher.
- Step 2: The researcher and his team loaded each of these envelopes with the following documents: a letter of introduction in respect of the research (a stamp requesting respondents "please/asseblief" to respond was added during the second mailing), a prepaid reply envelope, a copy of the IR of the company concerned and the research questionnaire.
- Step 3: Once that had been done, the researcher performed an audit on the open but loaded envelopes by systematically checking each tenth envelope to ensure that the content mentioned in Step 2 above, was present in the envelope. No corrective action was necessary.

[56] See Section 4.4.2 above, and Table 4.5.
[57] See Section 4.5.1, above.

- Step 4: The loaded envelopes were then labelled by attaching the address labels of all the individual shareholders identified in the sample to these envelopes.
- Step 5: To ensure completeness of the sample, the researcher performed an audit on the address label lists and confirmed that only the labels of those shareholders who had been selected were affixed to loaded envelopes.
- Step 6: The loaded envelopes were then sealed and mailed.

4.6 RESPONSE RATE

4.6.1 Responses and responses excluded from the response rate

As noted in Section 4.5.1, above, a questionnaire was sent out twice to individual shareholders of each of the three companies. Although every effort was made to ensure that the names and addresses of individual shareholders in the sample were correct and up to date, 182 envelopes were "returned to sender" indicating that the addresses of the individual shareholders were unknown, outdated or wrong. Of the 182, 64 came from Company A, 11 from Company B and 107 from Company C. Thus, between 2.45% and 3.41% of the respondents sampled, depending on the company under consideration, could not be reached. In line with guidance from Data Analysis Australia (DAA, 2012), such respondents to a mail survey of this nature should be classified as "out of scope" and should be removed when calculating the response rate. This represented about 2.8% of the total sample size for individual shareholders.

Among the individual shareholders that responded, 12 individual shareholders returned their questionnaires without attempting to complete them. These shareholders were not included among the respondents used in the statistical calculations. The reasons given for non-completion varied: one respondent objected to the fact that the questionnaire was in English only, rather than in English and Afrikaans (others also commented on this, but still completed the questionnaire); one indicated that the person did not trade in shares, as the person had inherited the shares; two were physically incapacitated to the extent that they could not complete the questionnaire; four did not complete the questionnaire and provided no indication as to why; one indicated that the person had two accounts and had completed the questionnaire for the other account; two indicated that the shareholders surveyed had passed away in the interim. Lastly, one respondent felt that it was arrogant to assume that the research project was unique, and therefore declined to complete the questionnaire.

One respondent responded to both mailing events, but indicated that his/her affairs were managed by a *curator bonus*, as the respondent was a psychiatric patient. It was decided to ignore this questionnaire, because this respondent was not legally accountable.

All questionnaires received up to 5 July 2010, except for those indicated above, were included in the total number of respondents used in the statistical analysis. Since their impact was negligible, given the sample size, the 12 respondents mentioned above were not removed for the calculation of the net sample size (see Table 4.6, below). Six questionnaires were received after 5 July, and these were excluded from the total number of respondents. These six questionnaires were analysed, as, given the size of the two age group classifications in the statistical analysis to which these respondents belonged, it was deemed highly unlikely that their contribution could in any way distort the statistical results already calculated.

4.6.2 Response rates and non-response bias

4.6.2.1 Response rate

The individual response rates per company and the overall response rate in respect of the survey are provided in Table 4.6, below.

Table 4.6: Response rate of individual shareholders surveyed

Company	Contribution to population	Sample mailed to	Net (1) sample	Respondents (n)	Resp / Mail %
Company A	3814	1907	1843	354	19.21%
Company B	898	449	438	70	15.98%
Company C	8264	4132	4025	678	16.85%
Overall	12976	6488	6306	1102	17.48%

(1) The net sample size was calculated by removing "out of scope" respondents, whose questionnaires, for mail-out surveys such as the one used in this thesis, are returned as "not at this address" or "return to sender".

As is evident from Table 4.6, above, the survey response rate per company ranged between 15.98% and 19.21%.

According to Lohr (2010:256), the best method of reducing non-response is to prevent it. To this end, several steps were taken, as is evident from Section 4.5.1, above. Despite the preventative steps, the final response rate was still low, and this raised the question of the impact of non-response bias on the external validity of the data. It is argued that the size of the sample, the fact that the shareholders of three companies were surveyed, as well as the number of respondents (1 102), may have mitigated the impact of non-response bias, but this potential limitation was nevertheless assessed, as is explained in the next section.

4.6.2.2 Non-response bias

Several techniques have been developed and reported on in the literature to detect the existence of and magnitude of non-response bias. In this study, the most commonly applied technique employed to assess non-response bias, namely extrapolation (early versus late respondents and wave analysis) (Armstrong and Overton, 1977:397; Wagner and Kemmerling, 2010:368), was used. It was not feasible to use some of the other available techniques to assess non-response bias, because the survey was anonymous and the shareholders' registers from which individual shareholders for the survey were selected were not set up to facilitate the extraction of reliable demographic information.

The primary objective of the study was to determine whether individual shareholders of South African listed retail companies understand the context and content of IRs; this is evidenced by calculating a mean of the total percentage scores achieved by individual shareholders in respect of their understanding of context and content, and content only.[58] Since these statistics are crucial to the study and include all responses to answers provided by respondents to the survey, it was concluded that if non-response bias was not present when applying extrapolation to these total percentage scores, it could be assumed that non-response bias was not present for respondents to the survey, and that the respondents were representative of the sample.

The process followed in executing the extrapolation technique was the following:

- Respondents from the first mailing event (early respondents – Wave 1) and respondents from the second mailing event (late respondents – Wave 2) were identified separately, based on the date of receipt of the completed questionnaire.

[58] See Tables 5.14 and 5.15.

- The calculation of two means (context and content, and content only) was done separately for Wave 1 and Wave 2.
- The means calculated for Wave 1 (early) and Wave 2 (late) respondents were subjected to t-tests to establish whether they differed significantly from each other from a statistical perspective. The results are reported in Table 4.7, overleaf.

Table 4.7: Results of t-tests between early and late respondents (n = 1 102)

Percentage score achieved by respondents	**Wave 1, n = 588 (early respondents)**		**Wave 2, n = 514 (late respondents)**	
	Mean	**Std Deviation**	**Mean**	**Std Deviation**
Context and content	43.6766	25.7991	41.6166	25.2272
T = 1.34, p = 0.1818				
Content only	39.4463	27.7381	37.7756	27.4349
T = 1.00, p = 0.3163				

The t-test statistics for context and content, as well as for content only, indicated that there was no statistically significant difference between the means for Wave 1 and Wave 2. This is the case as the null hypothesis could not be rejected at the 5% level in either of the two instances (p = 0.1818 / 0.3163).

Since neither assessment provided any evidence of non-response bias, concerns about non-response bias were minimal, and it appears that the respondents are representative of the sample as a whole.

4.7 CODING OF DATA, DATA PROCESSING AND PREPARATION

The data collected from the returned questionnaires were checked on receipt. Simultaneously, all the variables in the completed questionnaires received were coded. The data contained in the coded questionnaires were captured in an electronic data base by a single data typist at Statomet at the University of Pretoria. Once the data capture had been completed, a printout of the results was obtained, and the data units reflected on the printout from the electronic data base were compared with the original coded questionnaires, to ensure that all items had been captured correctly. Any errors detected were corrected on the printout, thereafter processed on the electronic data base, and finally checked back to the data base.

To verify the correctness of the data, logical tests were performed on the data to ensure that any logical errors were identified and corrected. Lastly, the codes associated with open-ended questions were reconsidered, and these codes were "collapsed" into smaller numbers of associated variables per question on the questionnaire. The electronic data base was then ready for statistical analysis.

4.8 STATISTICAL TECHNIQUES USED IN ANALYSING THE DATA

Statistical tests were performed using the SAS® Version 9.3 (SAS Institute Inc., SAS Campus Drive, Cary NC 27513) with Microsoft Windows XP (SP3) on a desk-top computer to analyse the data collected and captured on the data base. Each of the tests performed is discussed briefly below. The level of significance in respect of appropriate tests was specified as 5% or 0.05.

The statistical techniques associated with descriptive statistics used in this study, are explained below.

4.8.1 Frequency tables and descriptive statistics

In the case of a number of variables reported in Chapter 5, frequency distribution tables were constructed to facilitate a descriptive analysis of the data by providing absolute or relative data on how often different values of a variable were encountered in a sample from a population – in this study, the individual shareholders of three South African listed retail companies.

Where such frequency distribution tables were used, the number of responses or respondents in the case of each demographic or other variable was used as a point of departure to calculate the relative value or percentage of responses in that specific instance. The results provided by the frequency tables were described, and possible explanations for fluctuations in responses were proposed.

Where the results of a frequency table arose from using a Likert scale indicating, for instance, the perception of importance, the means of the variables were calculated as a "centre of gravity" of the scale to enable responses to be ranked. This specific technique was used as reported in Chapter 5, specifically in Tables 5.54 and 5.58.

4.8.2 Chi-square tests

As part of the statistical analysis, two-way tables were constructed and Chi-Square tests were performed to determine whether there was a statistically significant association between pairs of variables, for example the interaction between graduate status and perception of understanding. Chi-square tests are used to test for significant differences between the observed distribution of data between categories and the expected distribution using the null hypothesis as a base. The null hypothesis assumes that the variables are independent. Depending on the Chi-square values and the associated p-values generated by the tests, as well as the critical test values determined, the null hypothesis of independence could either be rejected, or not, when comparing the two variables involved. In instances where too many cells had expected frequencies lower than 5, Fisher's exact test was performed.

4.8.3 T-tests for two independent groups

A t-test compares the means for the same variable between two independent groups. This test enables a researcher to assess the magnitude of the difference between the means calculated for these groups, relative to the spread or variability of their scores, for example comparing the average total percentage score of graduates with that of non-graduates. T-tests are performed under two assumptions, namely that the observations come from a normal distribution and that the variances within the two groups are equal (homoscedasticity). In this study, the size of the sample ensured that the normality assumption was not violated, as the Central Limit Theorem states that the means calculated for the sample can be approximated by a normal distribution, regardless of the underlying distribution of the observations.

The equality of variances was assessed using Levene's test and, depending on whether the equality of variances assumption was violated or not, the test statistic was calculated using the pooled-variances (where the assumption was not violated) or Satterthwaite-variance method (where the assumption was violated).

4.8.4 ANOVA tests

In cases where statistical differences for more than two groups were assessed, an analysis of variance (ANOVA) was performed to determine whether the means were the same or not. An example of this would be comparing the average total percentage scores of respondents across degrees with different focal areas. ANOVAs are performed under two assumptions, namely the normality and equality of variances (homoscedasticity). Levene's test for equality of variances was performed in each case to establish whether the null hypothesis of equality of variances could be rejected or not. In cases where the null hypothesis could be rejected ($p < 0.05$) in terms of Levene's test, Welch's F-statistic was used instead of the ANOVA F-statistic.

4.8.5 Effect size in the case of t-tests and ANOVAs

For t-tests and ANOVAs, it was decided to assess the practical importance of an effect. It is a well-known fact that statistical significance is directly related to sample size; it is much more likely to find statistical significance with a large sample like this one. The mere fact that a test statistic was significant does not mean that it is necessarily meaningful or important, so, to assess importance or meaningfulness of an effect, a standardized measure called an effect size was developed. This enables researchers to compare effect sizes across different studies.

In this study, it was decided to use Pearson's correlation coefficient r as the measure of effect size. The following are widely accepted guidelines of effect size: $r = 0.10$ is regarded as a small effect, $r = 0.30$ is regarded as a medium effect, and $r = 0.50$ is a large effect (Field, 2005:32).

4.9 SUMMARY

In this chapter, the research method and the statistical techniques used to analyse the information collected via the research questionnaires are explained. In Chapter 5, the results of the empirical study that was conducted to meet the primary and secondary objectives of this study are analysed.

CHAPTER 5: RESULTS OF THE EMPIRICAL STUDY

5.1 INTRODUCTION

As indicated in Sections 1.5 and 4.1, the primary objective of the study was to determine whether individual shareholders (respondents) understand the context and content of the IRs of South African listed retail companies. Level of understanding is measured using the total percentage score achieved by individual shareholders. As part of this investigation, the individual shareholders' perceptions of their understanding of the IRs were also considered.

The secondary research objectives can be divided into two categories, namely those that investigate investment decisions and the use of IRs for investment decisions in general (Category 1) and those that investigate other matters directly associated with IRs (Category 2). The Category 1 secondary research objectives related to investment decisions explored how users (individual shareholders) make investment decisions (on their own initiative or via financial advisors) and what sources of information individual shareholders use when making investment decisions, whether individual shareholders deem IRs important for making investment decisions and what other crucial information individual shareholders may require to make investment decisions but that is not currently provided in IRs. The objectives related to IRs in particular (Category 2) aim to establish in what sequence individual shareholders would prefer the individual components of the IR to be presented, whether the components of the IR are read by respondents and to what extent and, lastly, in what medium of communication users would prefer to receive an IR.

The results of the empirical study for individual shareholders are evaluated by addressing the following aspects:

- Section 5.2: Profiling of the survey respondents;
- Sections 5.3 and 5.4: Assessing the understanding of respondents of the context and content of the IR, as well as their perceptions of their understanding of these items;
- Section 5.5: Summary of findings of the survey on the primary research objective.
- Section 5.6: How investment decisions are made by individual shareholders (Category 1);

- Section 5.7: Sources of information used by individual shareholders when making investment decisions (Category 1);
- Section 5.8: Importance of IRs for making investment decisions (Category 1);
- Section 5.9: Crucial additional information required in IRs (Category 1);
- Section 5.10: Sequence of presentation of individual components of the IR (Category 2);
- Section 5.11: Reading of IRs by respondents (Category 2);
- Section 5.12: Preferred medium of communication in the case of IRs (Category 2); and
- Section 5.13: Summary of findings of the survey on the secondary objectives.

5.1.1 Response rate and number of respondents answering individual questions

A total of 1 102 respondents (individual shareholders) completed the research questionnaire, but not all respondents answered every question in the questionnaire. Consequently, the number of respondents listed in tables presented in this chapter may vary. The number (n) of respondents is provided for each table.

5.2 PROFILING THE SURVEY RESPONDENTS

To provide a framework for analysing the results of empirical work in this study, the demographic and related factors in respect of the respondents to this study on IRs are considered individually, using frequency tables. Obtaining demographic information on individual shareholders was not the sole objective of collecting this data from shareholders in this study on IRs. Nevertheless, a broad profile of the 1 102 individual respondents[59] to the survey was compiled by collecting the following information: gender, age, level of education (possessing a degree or not, and level of post-graduate qualifications), focal area of degrees, whether accounting was a major in the respondent's tertiary studies (an indication of some knowledge of accounting), professional qualifications, fields of work experience, employment status, number of shares held in companies in the sample, the Rand value of such shares held, the number of companies in share portfolios, investment objectives and how investment decisions are made.

[59] See Table 4.6 for a breakdown of the response rate and number of respondents.

5.2.1 Gender and age of respondents

The gender of respondents was requested to obtain an impression of the gender participation of individuals into the shareholding in retail companies on the JSE. The analysis of gender distribution of respondents shows that 75.41% of the respondents were male and 24.59% of the respondents were female. This matter will not be pursued further in the detailed analysis of the impact of demographic variables on the perception of understanding and understanding of the content of the IRs.

Age distribution was requested to obtain an impression of the spread of investors over the spectrum of age brackets although this will not be pursued further when considering the impact of the different demographic factors on the perception of understanding and understanding of respondents (the primary objective). Age distribution, as presented in Table 5.1 below, does however still feature under the investigation surrounding the secondary objectives.

Table 5.1: Age of respondents

Age bracket (n = 955)	Frequency	Cumulative Frequency	Percentage	Cumulative percentage
18 <= 29 years	34	34	3.56	3.56
>29 <= 40 years	89	123	9.32	12.88
>40 <= 65 years	477	600	49.95	62.83
>65 <= 80 years	299	899	31.31	94.14
>80 <= 95 years	56	955	5.86	100.00

According to the above table, a total of 81.26% of the respondents fell into the age bracket of 40 to 80 years. Of these, 49.95% of the total fell into the bracket between 40 and 65 years and 31.31% into the age bracket between 65 and 80 years. This result is expected, as the 40- to 65-year age bracket logically coincides with the life phase during which the majority of share investors in South Africa should be saving for retirement at around 65 years of age, while the majority of the respondents over the age of 65 years would have retired (Department of Labour, 2004) and could be retaining shares as part of their retirement provision (also see the discussion in Section 5.2.2.7, below).

5.2.2 Education, occupation and employment status of respondents

As it is believed that investment decisions and understanding of financial information is affected by a person's level of education, the occupation and employment status of respondents, these factors were included in the demographic section of the questionnaire.

5.2.2.1 Respondents hold or do not hold a degree

Table 5.2: Respondents hold or do not hold a degree

Degree or no degree (n = 1102)	Frequency	Percentage
Degree	632	57.44
No degree	470	42.56
	1102	100.00

Of the sample of 1 102 respondents, 470 did not hold a degree, while 632 were in possession of at least a first degree. A more detailed analysis of the 632 respondents holding a first degree is provided in Table 5.3, below.

5.2.2.2 General focal area of first degrees held by respondents

Table 5.3: First degrees held by respondents

Focal area of degree (n = 632)	Frequency	Percentage
Science, but not medicine	69	10.92
BCom, but not Accounting	91	14.40
BCom (Accounting) or equivalent	147	23.26
Engineering-related degree	82	12.98
Human medicine and related degree	59	9.34
All other degrees (including 20 law degrees)	184	29.10
	632	100.00

As indicated in Table 5.3, above, 632 respondents to the survey held a first degree, while 470 did not. The 470 respondents could also include individuals with tertiary qualifications other than degrees. Of the respondents with a first degree as analysed in Table 5.3, above, 23.26% indicated that they had a degree with an accounting focus, suggesting that financially literate respondents may be more inclined to invest in shares.

5.2.2.3 Majored in accounting during tertiary qualification

Table 5.4: Major in tertiary qualification

Major (n = 1100)	Frequency	Percentage
Accounting	287	26.09
Not Accounting	813	73.91
	1100	100.00

Of the respondents, 26.09% indicated that they had majored in Accounting during their tertiary studies, although they may not necessarily have obtained a BCom (Accounting) or equivalent degree. Note that tertiary education in this instance was not limited to graduate studies, and would also include tertiary diplomas or certificates. The respondents who did not major in accounting included respondents who did not embark on tertiary studies at all as the questionnaire did not specifically exclude such respondents. This, in conjunction with the detail on BCom (Accounting) degrees or their equivalents in Table 5.3, appear to confirm that a substantial proportion of respondents who held shares had some knowledge of accounting.

5.2.2.4 Highest level of post-graduate qualification

Table 5.5: Highest post-graduate qualification

Level of higher degree obtained (n = 338)	Frequency	Percentage
No post-graduate degree	764	69.33
Honours or equivalent	189	17.15
Master's degree and/or PhD	149	13.52
	1102	100.00

Of the total number of respondents, 764 did not have post-graduate degrees, and 338 had post-graduate degrees. Of the 338 respondents with post-graduate degrees, 189 had obtained an Honours degree or equivalent, such as a Post-graduate Diploma as their highest post-graduate qualification, while 120 had obtained a master's degree (19 obtained a master's degree in Business Administration, hereafter MBA), without a degree prior to enrolling for the MBA, and would thus not hold a first or an Honours degree) and 29 held a PhD as their highest level of post-graduate qualification. In summary, 189 respondents obtained an Honours degree and 149 a Master's degree and/or a PhD.

5.2.2.5 Professional qualification held

Table 5.6: Professional qualification held

Professional qualification held (n = 520)	Frequency	Percentage
Teaching	77	14.81
Engineering and related	118	22.69
Medical	86	16.54
Financial	190	36.54
Other (including 17 legal)	49	9.42
	520	100.00

Of the respondents, 520 indicated that they held a professional qualification, and of these, 36.54% (190) were professionals in the financial field. As indicated in Table 5.6, read in conjunction with Table 5.7, below, it appears that the largest percentage of professionals that invest in shares came from the financial field.

5.2.2.6 Fields in which respondents work or have worked (work experience)

Table 5.7: Work experience

Fields of work (n = 1 085)	Number of respondents	% of respondents
Accounting/Investment/Banking/Finance	324	29.86
Medical/Legal	122	11.25
Engineering/Construction and related	190	17.51
Other	449	41.38
	1085	100.00

Of the respondents who held shares in the three companies covered in the survey, 29.86% worked in the accounting/investment/banking and finance fields. This high incidence may be attributed to either a greater interest in investing in shares or the fact that share incentive schemes may be more prevalent as part of remuneration packages in these particular fields, with the result that people working in these fields hold more shares.

5.2.2.7 Employment status

Table 5.8: Employment status and age of respondents (n = 1 098)

Age / Employment status	No age given	Age 18-25	Age 26-40	Age 41-65	Age 66-80	Age 81-95	No of resp	% of resp
Employed full-time	60	10	96	282	31	2	481	43.81
Employed part-time	15	1	5	66	16	2	105	9.56
Retired	70	0	4	104	244	51	473	43.08
Unemployed / Housewife / Student	1	4	2	24	7	1	39	3.55
Total	146	15	107	476	298	56	1098	100.0

A total of 586 (53.37%) of the respondents indicated that they were employed either full-time or part-time. Of the 511 respondents who provided their age in the employed group (those employed full-time or part-time), only 51 were older than 65 years, while 460 (90%) were 65 or younger. This alignment appears to confirm the general assumption that the majority of individuals in this survey (90%) in the age bracket from 18 to 65 years were employed at some level. At the same time, 473 (43.08%) of the respondents indicated that they were retired, and 70 did not provide their age. Of the 403 retirees who did provide their age, 295 (73%) were older than 65 years, and 104 were in the age bracket between 41 and 65 years. This finding also appears to confirm the assumption that the majority of retirees are above the age of 65 years, which is the common upper range of the retirement age in South Africa (Department of Labour, 2004).

5.2.3 Number of shares held (invested), Rand value of such shares in specific companies, and number of companies in the investment portfolios of respondents.

The magnitude of investment risk exposure may be closely linked to investment size, which can influence investment objectives, the way investment decisions are made, as well as the diligence with which IRs are perused. For these reasons, the number of shares held, the Rand value of shares held and the portfolio size were included in the demographic section of the questionnaire.

5.2.3.1 Number of shares held

Table 5.9: Number of shares held

Number of shares – interval (n = 972)	Number of respondents	Cumulative number of respondents	% of respondents	Cumulative % of respondents
0	30	30	3.09	3.09
1 – 100	134	164	13.79	16.87
101 – 250	110	274	11.32	28.19
251 – 500	160	434	16.46	44.65
501 – 1 000	173	607	17.80	62.45
1 001 – 2 500	169	776	17.39	79.84
2 501 – 5 000	78	854	8.02	87.86
5 001 – 10 000	54	908	5.56	93.42
10 001 – 15 000	21	929	2.16	95.58
15 001 – 30 000	24	953	2.46	98.04
30 001 plus	19	972	1.96	100.00

A total of 30 respondents indicated that they held no shares in the three companies involved in the survey and that they had disposed of the shares between the date of the interim report and the date on which they completed the questionnaire. Of the total number of respondents, 972 supplied the number of shares held in one or more of the companies involved in the survey, while 130 respondents of the 1 102 omitted to provide detail in this regard, or indicated that they could not remember how many shares they held.

Nearly 80% of respondents to this question in the survey held 2 500 or fewer shares, while 87.86% of respondents held 5 000 or fewer shares. The remaining 12.14% of respondents held more than 5 000 shares, which confirms that individual shareholders represent a large proportion of shareholders holding small blocks of shares in the companies under consideration. Individual shareholders who hold larger blocks of shares may thus hold more of the share capital of companies, but represent fewer of the individual shareholders receiving IRs.

5.2.3.2 Rand value of shares held by individual respondents

The actual number of shares held by individual shareholders gave some indication of the magnitude of investment risk exposure, but did not provide a clear picture of the monetary value of the shares held, because the market prices of the individual shares of the three companies at their respective interim dates varied substantially. For instance, the Rand value per share of Companies A to C ranged between approximately R12 to more than R65 in the interval between 31 December 2008 and 31 December 2009. The above share prices indicate that the value of five shares in one company approximated the value of one share of another company, while in the other instance slightly more than two shares of one company equalled the value of one share in another company. When only the number of shares is used as a point of departure, as in Table 5.9, above, it clearly reduces comparability, because the monetary values of the shares differed substantially.

To align the magnitude of investment risk exposure between the respondents more closely, the estimated monetary Rand value of all shares held by a respondent was calculated by applying the price per share at the respective interim dates to the number of shares held by each respondent. This converted the individual shareholdings to an approximate Rand value, providing a better basis for comparing relative investment risk exposure. These data are reflected in Table 5.10, below.

Table 5.10: Rand value of shares held

Rand value of shares – interval (n = 972)	Number of respondents	Cumulative number of respondents	% of respondents	Cumulative % of respondents
0	30	30	3.09	3.09
>0 – 2500	72	102	7.41	10.50
>2500 – 5000	72	174	7.40	17.90
>5000 – 10000	100	274	10.29	28.19
>10000 – 20000	152	426	15.64	43.83
>20000 – 50000	199	625	20.47	64.30
>50000 – 100000	119	744	12.24	76.54
>100000 – 200000	127	871	13.07	89.61
>200000 – 500000	46	917	4.73	94.34
>500000 plus	55	972	5.66	100.00

From the above table it appears that the majority of respondents held share blocks with monetary values of between (just above) R5 000 and R200 000. Nearly 72% of shareholders fell within this bracket, while 17.9% of shareholders held share blocks with values of R5 000 and less, and 10.39% had share blocks with values in excess of R200 000. Of the 1 102 respondents, 130 omitted details in this regard, or indicated that they could not remember how many shares they held.

5.3.2.3 Number of companies comprising share portfolios

Table 5.11: Number of companies in share portfolios

Number of companies – intervals (n = 1055)	Number of respondents	Cumulative number of respondents	% of respondents	Cumulative % of respondents
0 – 20 (incl. 6 with 0)	758	758	71.85	71.85
21– 40	244	1002	23.13	94.98
41 – 60	40	1042	3.79	98.77
61 plus	13	1055	1.23	100.00

The six respondents who indicated that they did not have any companies in their share portfolios probably sold their entire portfolios between the date on which the share registers were used to identify shareholders and the date when they completed the research questionnaires. Due to the anonymous nature of the questionnaire, it was not possible to determine the real reason for their not having any companies in their portfolios. It was found that 71.85% of the portfolios of respondents to this question of the survey consisted of 20 or fewer companies, while 94.98% of respondents had 40 or fewer companies in their portfolios.

5.2.4 Investment objectives and decisions of respondents

5.2.4.1 Investment objectives of respondents

Table 5.12: Respondents' investment objectives

Investment objective (n = 1095)	Number of respondents	% of respondents
Speculative gains/Other	26	2.37
Long-term capital growth	367	33.52
Dividends/income	78	7.12
Combination of dividend income and capital growth	624	56.99
	1095	100.00

Of the total of 1 102 respondents, seven were discarded because their investment objectives were unrelated to any of the objectives listed, or to each other, and they could therefore not be allocated to a category of a reasonable size for statistical purposes. It is clear from the above table that more than 90% of the shareholders held their investments either to achieve long-term capital growth or a combination of dividend income and capital growth. More specifically, 33.52% of respondents listed their objective as long-term capital growth and 56.99% listed a combination of dividend income and capital growth.

5.2.4.2 How respondents make investment decisions

Table 5.13: Initiative when making investment decisions

Making investment decisions (n = 1071)	Number of respondents	% of respondents
Own decision	659	61.53
Own decision, but financial advisor directly involved (consulted)	242	22.60
Sub-total respondents taking own decisions	*901*	***84.13***
Financial advisor takes decision after consulting with shareholder	75	7.00
Financial advisor makes decisions	95	8.87
Sub-total respondents with financial advisor involvement	***170***	***15.87***
Grand total	1071	100.00

Of the respondents, 61.53% indicated that they make investment decisions entirely on their own initiative, while another 22.6% of respondents make investment decisions on their own initiative, but would consult with a financial advisor – a total of 84.13% therefore initiated their own investments. The remaining 15.87% of respondents (7% and 8.87% respectively) would depend entirely on their financial advisor to make investment decisions or would expect the financial advisor to take the initiative and clear it with them before making the final decision. Of the 1 087 respondents who answered this question initially, 16 from the category "other" on the questionnaire gave a diverse range of answers, and these could not be grouped together or logically allocated to the remaining categories. Consequently, it was decided to discard those responses and use only the 1 071 respondents from the four remaining categories. For the purposes of the further analysis of respondents' perception of understanding and understanding of content, the above-mentioned four categories were collapsed into two larger groups – the first larger category (owner initiative) is a combination of the first two categories that appeared in the above table, while the second larger category (financial advisor initiative) is a combination of the third and fourth categories.

5.3 ASSESSING PERCEPTION OF UNDERSTANDING AND UNDERSTANDING OF THE CONTEXT AND CONTENT, AND CONTENT ONLY, OF IRS

To address the primary research objective of the study, namely to ascertain whether individual shareholders understand the context and content of IRs, the postal questionnaire discussed in Chapter 4 contained a number of questions designed specifically to assess the understanding of the context and content of the IR by respondents to the questionnaire. Details in respect of these questions and the marks awarded to the answer to each question were presented in Sections 4.2.2 and 4.2.3.

Although this study focused on the understanding by respondents of the context and content of IRs, it was also interesting to see whether respondents' understanding of the IRs was in line with their perceptions of their understanding of the IRs.

5.3.1 Assessment of understanding of individual shareholders of the context and content of IRs

In assessing whether respondents understand specifically the context of the IR, the total percentage scores achieved by respondents for questions dealing with context and content (**combined**) were compared to the total percentage scores achieved by respondents for the questions related to content **only**. This approach was followed for the sake of brevity, since it simultaneously provides the reader with an overview of whether individual shareholders understand the context and content, the content only, as well as the context only, of an IR. Perception of understanding could not be considered in respect of the context of IRs only, since the questionnaire did not facilitate this.

The total percentage score per respondent for context and content (combined) was calculated by expressing marks achieved by a respondent out of 22, as a percentage. By contrast, the total percentage score per respondent for content only was calculated by expressing marks achieved by a respondent out of 18 as a percentage.[60]

A frequency table containing the total percentage scores achieved by respondents for context and content combined (marks out of 22) is provided in Table 5.14, overleaf. In Table 5.15, a frequency table containing the total percentage scores achieved for content only (marks out of 18) is provided. The contents of the frequency tables are discussed immediately below each of the two tables.

Once the comparison between the average total percentage scores of context and content, and content only, as referred to earlier in this section has been done and the understanding of context of the IR has been assessed, the three questions focusing exclusively on context are addressed individually in the frequency tables presented in Section 5.3.3.

To facilitate deliberations as to "understanding" in this part of the study, an assumption was made (see Section 1.8) that a total percentage score of 50% was an acceptable level of understanding. This assumption is based on the widely accepted principle in tertiary education that 50% represents sufficient knowledge to pass a module.

[60] See Appendix B, Table B1.

Table 5.14: Frequency table and mean of total percentage score achieved by respondents in the assessment of their understanding of both the context and content of the IRs

Total percentage score achieved by respondents (Score out of 22 in brackets and n = 1102)	Frequency	Percentage	Cumulative frequency	Cumulative percentage
0.00 (0)	30	2.72	30	2.72
4.55 (1)	57	5.17	87	7.89
9.09 (2)	75	6.81	162	14.70
13.64 (3)	52	4.72	214	19.42
18.18 (4)	77	6.99	291	26.41
22.73 (5)	29	2.63	320	29.04
27.27 (6)	57	5.17	377	34.21
31.82 (7)	45	4.08	422	38.29
36.36 (8)	78	7.07	500	45.36
40.91 (9)	63	5.72	563	51.08
45.45 (10)	63	5.72	626	56.80
50.00 (11)	51	4.63	677	61.43
54.55 (12)	94	8.53	771	69.96
59.09 (13)	37	3.36	808	73.32
63.64 (14)	58	5.26	866	78.58
68.18 (15)	55	4.99	921	83.58
72.73 (16)	27	2.45	948	86.03
77.27 (17)	64	5.81	1012	91.83
81.82 (18)	18	1.63	1030	93.47
86.36 (19)	48	4.36	1078	97.82
90.91 (20)	7	0.64	1085	98.46
95.45 (21)	15	1.36	1100	99.82
100.00 (22)	2	0.18	1102	100.00
Mean of total percentage score in respect of **context and content** as contained in this table = 42.72%.				

From Table 5.14, above, which shows the total percentage scores of context and content of IRs, it is clear that 38.57% of the respondents achieved a total percentage score of above 50%, while 56.80% achieved 50% and below. Just more than 51% of respondents achieved about 41% and below, suggesting that the majority of respondents to the survey display a limited understanding of context and content (combined) of IRs. As explained before, perception of understanding was not considered here.

5.3.2 The understanding of respondents of the content only of IRs

Table 5.15: Frequency table and mean of total percentage score achieved by respondents in the assessment of their understanding of the content only of IRs

Total percentage score achieved by respondents (Score out of 18 in brackets and n = 1102)	Frequency	Percentage	Cumulative frequency	Cumulative percentage
0.00 (0)	181	16.42	181	16.42
5.56 (1)	17	1.54	198	17.97
11.11 (2)	97	8.80	295	26.77
16.67 (3)	35	3.18	330	29.95
22.22 (4)	61	5.54	391	35.48
27.78 (5)	54	4.90	445	40.38
33.33 (6)	85	7.71	530	48.09
38.89 (7)	47	4.27	577	52.36
44.44 (8)	91	8.26	668	60.62
50.00 (9)	42	3.81	710	64.43
55.56 (10)	101	9.17	811	73.60
61.11 (11)	57	5.17	868	78.77
66.67 (12)	44	3.99	912	82.76
72.22 (13)	78	7.08	990	89.84
77.78 (14)	18	1.63	1008	91.47
83.33 (15)	63	5.72	1071	97.19

Total percentage score achieved by respondents (Score out of 18 in brackets and n = 1102)	**Frequency**	**Percentage**	**Cumulative frequency**	**Cumulative percentage**
88.89 (16)	10	0.91	1081	98.09
94.44 (17)	19	1.72	1100	99.82
100.0 (18)	2	0.18	1102	100.00
Mean of total percentage score in respect of **content only** as contained in this table = 38.67%.				

From Table 5.15, which contains the total percentage scores in respect of content only of the IRs, it is clear that 35.57% (see also Table 5.14 on context and content = 38.57%) of respondents achieved a total percentage score of above 50%, while 60.62% (see Table 5.14 on context and content = 56.80%) achieved a score below 50%. Using the same line of argument, just more than 52.36% (see Table 5.14 = 51.08%) of respondents achieved about 39% (see Table 5.14 = 41%) and below, once more leaving the impression that the majority of respondents display a limited understanding of the content only of IRs.

When one considers the percentages mentioned in the preceding paragraph, it is evident that respondents have a better grasp of the context of the IR than its content. This conclusion on the understanding of context is also corroborated by the fact that the mean of the total percentage score achieved by respondents for questions dealing with both context and content of the IR is 42.72% (see the bottom part of Table 5.14), while the mean dealing with content only is 38.67% (see the bottom part of Table 5.15). The higher mean for context and content combined can only be attributed to the fact that the questions relating to context are included when calculating the mean of 42.72% for context and content (combined) and excluded when calculating the mean of 38.67% for content only. Perceptions of understanding and understanding are considered in the table overleaf.

Table 5.16: T-test between respondents' perceptions of understanding and their understanding of the content of IRs (n = 1 048)

Understand (n = 675)		Don't understand (n = 373)	
Mean (Average total percentage score)	**Standard Deviation**	**Mean (Average total percentage score)**	**Standard Deviation**
50.5267	24.6174	20.1072	20.0928
T = 21.62, p < 0.0001			

A t-test for two independent variables was performed to assess whether the average total percentage scores (means) of respondents who perceived themselves to understand the content of the IR differed from those of respondents who believed they did not understand it. In this instance, the assumption of equal variances was also violated, and consequently the Satterthwaite method was used (T = 21.62, DF = 902.4). This test statistic indicated that the null hypothesis should be rejected at a 5% level ($p< 0.0001$). This relates to a large effect size ($r = 0.58$). The outcome of this test showed that the understanding of the content only of the IR of the two groups differed significantly. The average total percentage score of respondents who believed that they understood the content only of the IR (mean = 50.53) was statistically higher than that of respondents who believed that they did not understand the content only of the IR (mean = 20.11).

- *Conclusion*

The higher average total percentage score (mean = 50.53) of respondents who believed they understand the content only of the IR is in line with their perception that they understood the content only of the IR. The low average total percentage score (mean = 20.11) of the group of respondents who believed they did not understand the content only of the IR was also in line with their perceived understanding.

5.3.3 Understanding of individual questions related to context of IRs

There is only one correct answer to each of the three questions assessing context, as explained below. The rationale used to award marks to the correct answer in each instance has already been addressed in Section 4.2.3 and is applied consistently in the deliberations in Sections 5.3 and 5.4. The questions and the responses are addressed individually.

Question 16

Who do you believe is legally responsible for the interim financial report of a company?

The answer to this question was considered to be fairly difficult, since it was not evident from the IR itself. Consequently, a mark of 2 was awarded for the correct answer as explained in Section 4.2.3. Only 41.6% of the total number of respondents answered it correctly. The wide distribution of responses across the available answers indicates that respondents were not well informed on this matter.

Table 5.17: Frequencies in respect of legal responsibility and field of work (n = 1 007)

Answer / Field of work	Chair-man	CEO	*Board of Directors (Correct answer)*	CFO	Auditors	Total
Accounting and related	15 (4.9%)	44 (14.5%)	192 (63.1%)	37 (12.2%)	16 (5.3%)	304 (100%)
Medicine and law	15 (13.5%)	24 (21.6%)	35 (31.5%)	20 (18%)	17 (15.4%)	111 (100%)
Engineering, construction and related	25 (14.3%)	51 (29.2%)	62 (35.4%)	20 (11.4%)	17 (9.7%)	175 (100%)
Other	43 (10.3%)	95 (22.8%)	157 (37.7%)	61 (14.6)	61 (14.7)	417 (100%)
Total	98 (9.7%)	214 (21.3%)	446 (44.3%)	138 (13.7%)	111 (11%)	1007

Table 5.17 addresses the relationship between "field of work" and the "people being legally responsible for the IR". It indicates that 63.1% of the respondents working in the accounting/investment/finance and banking field chose the correct answer. This finding was expected, as these respondents are expected to have a good knowledge of financial and related matters. As is confirmed later in Section 5.4.1.6, where the average total percentage scores are assessed, the respondents from the medical and legal professions gave the lowest number of correct responses.

Question 17

Is the Interim Financial Report accompanying this questionnaire audited or not?

Table 5.18: Frequencies in respect of the audit status of IRs

Options provided (n = 1050)	Frequency	Percentage
Not audited (Correct answer and counts 1 mark – see 4.2.3)	908	86.48
Audited	142	13.52
	1050	100.00

The fact that the vast majority of responses are correct is not surprising, as the audit status of the IRs is clearly stated on the front pages of two of the three IRs used in the survey (Companies A and C). In the case of the third IR used (Company B), the front page indicates that the results have been reviewed and the fact that a review is not an audit is explained lower down on the first page of the IR.

To analyse the results in Table 5.18 further, these responses were split per company. The salient frequencies from the cross-tabulation are presented in Table 5.19, below.

Table 5.19: Frequencies per company on audit status of IRs

Audited/Not Audited (n = 1050))	Total	Company A (not audited)	Company B (reviewed)	Company C (not audited)
Not audited	908	(88%) 287	(81%) 54	(86%) 567
Audited	142	38	13	91
Total	1050	325	67	658

The percentage of responses indicating that the IRs were not audited was 86%, and was higher for the two companies where the fact that the IRs were not audited was displayed prominently on the front page. In the case of Company B, where the IR indicates that it was reviewed, the percentage was lower. This difference in percentage (6% or higher) may indicate that respondents were confused when it was not stated explicitly that the IR was not audited, as they may not have been familiar with the meaning of the term “reviewed”.

Question 18

In your view, what is the most important single objective of providing an interim financial report?

Table 5.20: Frequencies in respect of objective of issuing an IR and accounting major (n = 1 067)

Accounting major or not / Objective of issuing an IR	Accounting major (%)	Not accounting major (%)	Total (%)
To make directors of the company accountable to shareholders	18 (16.8)	89 (83.2)	107 (100)
To provide information to the South African Revenue Service in respect of the first six months of the year	1 (5.9)	16 (94.1)	17 (100)
To provide shareholders with a progress report on the financial performance and position of the company after the first six months of the financial year (Correct answer and counts 1 mark – see Section 4.2.3)	257 (29.3)	620 (70.7)	877 (100)
To provide shareholders with information for investment decisions in respect of the company	7 (10.6)	59 (89.4)	66 (100)
Total	283	784	1067

The details contained in the options in respect of the objectives of the IR that are provided in Table 5.20, above, gives some guidance on what the answer to this question should be. It was therefore not surprising that 82% of the 1067 respondents provided the correct answer. Further analysis of the responses in respect of the variables “Accounting a major/Accounting not a major at tertiary level” and “Objective of IR” indicated that 257 (91%) of the 283 respondents from the group who took Accounting as a major at a tertiary level answered this question correctly, as opposed to 620 (79%) of the 784 who did not take Accounting as a major at a tertiary level. This result is not surprising, as an understanding of accounting would facilitate interpretation of the options provided in the question.

5.4 PERCEPTION OF UNDERSTANDING AND UNDERSTANDING OF THE CONTENT OF IRS

In Section 5.3.3, the understanding of the context of the IR was explored in isolation. To elucidate the understanding of **content only** by respondents further, the investigation now focuses on respondents' perceptions of their own understanding, as well as their understanding of the content (excluding the context) of the IR.

Question 27 (which deals with perceptions of understanding of the IR) focuses only on information contained in the IR (questions related to context also include matters not contained in the IR), and therefore the understanding of the content of the IR (excluding context) as reflected in Table 5.15 can be compared to perception of understanding of the content of IRs (opinion of respondents) to ensure alignment. The following approach was followed:

- The **perception of understanding** of the content of the IR by the respective demographic groups listed in Section 5.2 (except gender and age) was considered by dividing the responses of these groups to Question 27 of the questionnaire into two categories – those respondents who were of the opinion that they understood the information contained in the IR, and those who were of the opinion that they did not understand the information contained in the IR. To test for association, Chi-square tests were performed.
- The total percentage score achieved for Q22 to Q26 collectively (calculated using the scoring mechanism explained in Section 4.2.4) was used to assess **understanding** of the content only, and these scores were also divided into subsections according to the demographic variables considered in Section 5.2. T-tests or ANOVAs were performed to assess whether the different categories of demographic variables differed with regard to the understanding of the content of the IR concerned, as indicated by the means (the average total percentage scores).

The results of the statistical procedures are summarized and considered below in tables per demographic variable. The tables in Sections 5.4.1 to 5.4.4 deal with **perceptions** of understanding, and **understanding** of the content of the IR via the average total percentage scores (means). The focus (perception or understanding) is underlined in headings and table headings to assist the reader.

5.4.1 Education, occupation and employment status

In this section, the association between education (degree/no degree, focal area of degree, having Accounting as a major and holding a post-graduate degree/not), occupation (professional qualification and field of work experience) and employment status and the perception of understanding and understanding of the content of IRs are considered (see Tables 5.21 to 5.34).

5.4.1.1 Degree or no degree

- *Discussion: Holding a degree or not and perception of understanding of the content of IRs*

Table 5.21: Degree or no degree and perception of understanding the content of IRs (n = 1 048)

	Understand	Don't understand	Total
No degree			
Frequency	256	185	441
Expected frequency	284	157	
Cell Chi-Square	2.7683	5.0096	
Row percentage	58.05	41.95	100.0
Degree			
Frequency	419	188	607
Expected frequency	391	216	
Cell Chi-Square	2.0112	3.6396	
Row percentage	69.03	30.97	100.0
Total	675 64.41	373 35.59	1048 100.00
Chi-square test statistic = 13.4286, $p < 0.0002$			

The above two-way table was constructed using degree status (respondent held a degree or did not hold a degree) and respondents' perceptions of whether they did or did not understand the content of the IR. The Chi-square test statistic of 13.4286 (DF = 1, p = 0.0002) provides convincing evidence that the null hypothesis of no association should be rejected. There is therefore statistical evidence that whether respondents hold a degree or not, interacts with their perceptions of understanding the interim financial report.

From the cross-tabulation in Table 5.21, above, it is evident that significantly more respondents without a degree held the perception that they did not understand the content of the IR than was expected (cell Chi-square = 5.0096).

- *Discussion: Holding a degree or not and understanding of the content of the IR as indicated by average total percentage score*

Table 5.22: T-test between respondents with a degree or no degree and understanding of the content of IRs (n = 1 102)

Degree (n = 632)		No degree (n = 470)	
Mean (Average total percentage score)	**Standard Deviation**	**Mean (Average total percentage score)**	**Standard Deviation**
44.7609	28.9039	30.4728	23.7878
T = -9.06, p < 0.0001			

A t-test for two independent samples was performed to assess whether the means of the total percentage score of respondents with a degree and those of respondents without a degree differ. For this test, the assumption of equal variances was violated, and consequently the Satterthwaite method was used (T= -9.06, DF = 1092.3). This test statistic indicates that the null hypothesis should be rejected at the 5% level (p <0.0001). This relates to a medium effect size (r = 0.26). The outcome of this test was that the mean in respect of understanding of the content of the IR indicated that the understanding of respondents holding a degree (mean = 44.76) and of those respondents not holding a degree (mean = 30.47) differs significantly.

- *Conclusion*

Although the means of total percentage score of understanding of the content of the IR for both respondents with a degree and those without a degree were once again disappointingly low, the perceptions of respondents with a degree and those of respondents without a degree corresponded with the means achieved by the two groups. Note that the nature of the degrees held by respondents would have an impact on the percentage scores indicating understanding, as is further elucidated in Section 5.4.1.2, overleaf.

5.4.1.2 Focal area of degree

- *Discussion: Focal area of degree and perception of understanding of the content of IRs*

Table 5.23: Focal area of degree and perception of understanding of the content of IRs (n = 607)

	Understand	Don't understand	Total
BSc/Veterinary and non-medical			
Frequency	33	31	64
Expected frequency	44	20	
Cell Chi-Square	2.8282	6.3034	
Row percentage	51.6	48.4	100
BCom, but not BCom (Accounting)			
Frequency	69	17	86
Expected frequency	59	27	
Cell Chi-Square	1.5641	3.4859	
Row percentage	80.2	19.8	100
BCom (Accounting)			
Frequency	141	5	146
Expected frequency	101	45	
Cell Chi-Square	16.05	35.772	
Row percentage	96.6	3.4	100
BEngineering and related			
Frequency	53	26	79
Expected frequency	55	24	
Cell Chi-Square	0.043	0.0959	
Row percentage	67.1	32.9	100
Medicine and related			
Frequency	26	30	56
Expected frequency	39	17	
Cell Chi-Square	4.1434	9.2345	
Row percentage	46.4	53.6	100
BA/Theology/Law etc.			
Frequency	97	79	176
Expected frequency	121	55	
Cell Chi-Square	4.9364	11.002	
Row percentage	55.1	44.9	100
Total	419 69.03	188 30.97	607 100.00
Chi-square test statistic = 95.4594, $p < 0.0001$			

The above two-way table was constructed using the focal area of undergraduate degree and the perception of respondents as to whether they understood the content of the IR concerned or not as the variables. As elsewhere in the study, a Chi-square test was performed to determine whether there is a statistically significant association between the two variables involved. The test statistic of 95.4594 (DF = 5, p <0.0001) provides evidence of an association between the focal area of respondents' undergraduate degrees and their perceptions of understanding. Statistically significant associations between the perceptions held by the different degree focal area groups are evident, so it can be concluded that the perception of understanding of the IR of respondents interacts with the specific degree focal area groups identified in this cross-tabulation.

From the cross-tabulation in Table 5.23, above, it is clear that significantly fewer BCom (Accounting) (or equivalent) graduates held the perception that they did not understand the content of the IR than was expected (cell Chi-square = 35.772).

The opposite is also evident in that significantly more respondents in the BA/Theology/Law, etc. degree group hold the perception that they did not understand the content of the IR than was expected (cell Chi-square = 11.002).

- *Discussion: Focal area of degree and understanding of the content of IRs*

Table 5.24: ANOVA with focal area of degree as independent variable and average total percentage score on content as dependent variable (n = 632)

Test result	Breakdown of demographic group	Means (Average total percentage score)	Standard deviation
F = 99.09,	-BSc non-medical (n = 69)	29.7907^{ad}	21.2186
DF1 = 5,	-BCom, not Accounting (n = 91)	47.9243^{b}	24.2818
DF2 = 229.5,	-BCom Accounting (n = 147)	74.1119^{c}	17.0367
p < 0.0001	-Engineering + related (n = 82)	42.8184^{bc}	23.7713
(Welch)	-Medicine + related (n = 59)	27.5895^{a}	24.6294
	-BA/Theology/law etc (n = 184)	31.7331^{d}	26.4680
Means identified by different superscript differ significantly at the 5% level.			

An ANOVA was performed to determine whether the understanding of the content of the IR was the same for respondents grouped by focal area of undergraduate degree.

According to Levene's test, the assumption of equal variance was violated ($p < 0.0001$) and thus Welch's test statistic had to be used. The null hypothesis that there are no differences between the means of total percentage scores of different degree focal area groups should be rejected ($F = 99.09$, $DF1 = 5$, $DF\ 2 = 229.5$, $p < 0.0001$). This relates to a strong effect size ($r = 0.60$). It can therefore be concluded that there are statistically significant differences between the average total percentage scores (means) of respondents with degrees with differing focal areas. This is confirmed by the means or average total percentage scores (see Table 5.24), which show BCom (Accounting) graduates (mean = 74.11) and other BCom graduates (mean = 47.92) to have the highest means. Respondents with degrees in medicine and related focal areas appear to have the lowest mean (27.59).

Post hoc tests confirmed that the mean of respondents holding BSc/Veterinary/Non-medical degrees (mean = 29.79) differs significantly from the means of the three groups of respondents respectively who held non-accounting BCom degrees (mean = 47.92), BCom (Accounting) degrees (74.11) and Engineering-related degrees (mean = 42.82), but does not differ significantly from that of respondents who held degrees in medical fields (mean = 27.59) and sundry other degrees (mean = 31.73). This may be explained by the fact that respondents who held pure science, medicine and sundry other degrees may have little exposure to accounting, investment and business, while engineering graduates may be more readily exposed to mathematical problems and business. It is surprising that the mean of the group of respondents holding non-Accounting BCom degrees differs significantly from that of respondents holding BCom (Accounting) degrees or degrees in the medical field and the group holding a range of degrees, but not from respondents holding engineering degrees. The mean of respondents holding engineering degrees differ significantly from respondents holding degrees in medicine and the group holding a wide range of degrees.

- *Conclusion*

The perception of understanding of the IR was the highest amongst BCom (Accounting) graduates and the means of their total percentage scores are also the highest – there is thus evidence of alignment between perception of understanding and understanding of the content of IRs. This result was anticipated, because such graduates are deemed to be financially well-informed and should consequently be able to assess their own level of knowledge accurately. Interestingly, the graduates in the medical field performed the worst in the total average percentage scores (mean = 27.59) and, according to the Chi-square results, significantly more of these respondents than expected held the perception that they did not understand IRs.

5.4.1.3 Majored in Accounting during tertiary education

- *Discussion: Majored in accounting and perception of understanding of the content of IRs*

Table 5.25: Accounting major in tertiary education and perception of understanding of the content of IRs (n = 1 046)

	Understand	Don't understand	Total
Accounting major in Tertiary studies			
Frequency	259	24	283
Expected frequency	182	101	
Cell Chi-Square	32.216	58.369	
Row percentage	91.5	8.5	100.0
No accounting major in tertiary studies			
Frequency	415	348	763
Expected frequency	492	271	
Cell Chi-Square	11.949	21.649	
Row percentage	54.4	45.6	100.0
Total	674	372	1046
	64.44	35.56	100.00
Chi-square test statistic = 124.1833, p < 0.0001			

The above two-way table was constructed by dividing respondents who majored in accounting during their tertiary education (degrees as well as other tertiary qualifications) from those that did not, and their perceptions as to whether or not these respondents understand the content of the IR. A Chi-square test performed to determine whether there is a statistically significant association between the two variables involved rendered a test statistic of 124.1833 (DF = 1, p <0.0001), providing convincing evidence that the null hypothesis of no association should be rejected. Statistically significant associations between the perceptions held by the two groups are evident. It can be concluded that the perception of understanding of the content of the IRs of respondents interacts with whether respondents majored in accounting during tertiary education or not.

More respondents who majored in accounting than was expected held the perception that they did understand the content of the IR (cell Chi-square = 32.216). The opposite is true for those respondents who did not major in accounting, where far more than expected indicated that they did not understand the content of the IR (cell Chi-square = 21.649).

- *Discussion: Majored in Accounting and understanding of the content of IRs as indicated by average total percentage score*

Table 5.26: T-test between respondents who majored in Accounting in tertiary education and understanding of the content of IRs (n = 1 100)

Accounting major (n = 287)		Not an accounting major (n = 813))	
Mean (Average total percentage score)	**Standard Deviation**	**Mean (Average total percentage score)**	**Standard Deviation**
61.6725	23.8978	30.5726	24.0138
$T = 18.89$, $p < 0.0001$ (pooled method)			

A t-test for two independent variables was performed to assess whether the average total percentage scores (means) of respondents with a tertiary accounting major and those without a tertiary major in accounting differ. In this instance, the assumption of equal variances was not violated, and consequently the pooled method was used ($T = 18.89$, $DF = 1098$). This test statistic indicated that the null hypothesis should be rejected at the 5% level ($p< 0.0001$). This relates to a large effect size ($r = 0.50$). The outcome of this test showed that the two groups' understanding of the content of the IR differed significantly. The average total percentage score of respondents who majored in accounting at a tertiary level (mean = 61.67) is statistically larger than that of respondents who did not major in accounting (mean = 30.57).

- *Conclusion*

The perception of respondents who majored in Accounting in their tertiary education was that they understood the content of IRs. This finding was anticipated, as these respondents can be expected to have a better understanding of accounting due to their academic background. It would also explain why their average percentage score (mean) is relatively high, at approximately 62%. The mean of the group of respondents who did not major in Accounting is only 31% and their perceived level of understanding is also much lower than that of the respondents who did major in Accounting. One can thus conclude that respondents who major in Accounting have a better understanding of the content of IRs. The level of understanding of the content of IRs of respondents who majored in Accounting was lower than that of respondents holding a BCom (Accounting) degree or an equivalent degree, but was higher than that of respondents holding other BCom degrees.[61] One explanation for this phenomenon could be that Accounting is not necessarily a major in all BCom degrees.

5.4.1.4 Post-graduate degrees

- *Discussion: Post-graduate degrees and perception of understanding of the content of IRs*

Table 5.27: Post-graduate degrees and perception of understanding of the content of IRs (n = 1 048)

	Understand	Don't understand	Total
No post-graduate qualification			
Frequency	432	289	721
Expected frequency	464	257	
Cell Chi-Square	2.2584	4.0869	
Row percentage	59.9	40.1	100.0
Honours or equivalent[62]			
Frequency	146	38	184
Expected frequency	119	65	
Cell Chi-Square	6.3759	11.538	
Row percentage	79.3	20.7	100.0
Master's and PhD			
Frequency	97	46	143
Expected frequency	92	51	
Cell Chi-Square	0.2603	0.471	
Row percentage	67.8	32.2	100.0
Total	675	373	1048
	64.41	35.59	100.00
Chi-square test statistic = 24.9906, p <0 .0001			

The above two-way table was constructed using post-graduate degrees held by respondents (including a category of respondents who did not hold a post-graduate degree) and the

[61] See Table 5.24, above.
[62] 103 respondents held Honours degrees or Post-graduate diplomas in Accounting, the rest held Honours degrees in other disciplines.

perception of respondents as to whether they understood the content of the IR or not. A Chi-square test was performed to determine whether there is a statistically significant association between the variables involved. The test statistic of 24.9906 (DF = 2, p < 0.0001) provides convincing evidence that the null hypothesis of no association should be rejected. Statistically significant associations between the perceptions held by the respondent groups who held and that did not hold higher degrees are evident and it can be concluded that the perception of understanding of the IR of respondents interacts with the level of the higher degree held.

From Table 5.27, above, it is clear that more respondents who did not hold a higher degree believed that they did not understand the IR than was expected (cell Chi-square = 4.0869).

In the case of Honours graduates or equivalent, more respondents than was expected held the perception that they understood the content of the IR (cell Chi-square = 6.3759). Since 103 out of 184 respondents holding Honours degrees or equivalents held BCom (Honours) degrees or Post-graduate diplomas in Accounting, this result was to be expected.

- *Discussion: Post-graduate degrees and understanding of the content of IRs*

Table 5.28: ANOVA with post-graduate degree status as independent variable and average total percentage score on content as dependent variable (n = 1 102)

Test result	Breakdown of demographic group	Means (Average total percentage score)	Standard deviation
F = 60.28, DF1 = 2, DF2 = 284.1, p < 0.0001 (Welch)	-No PG qualification (n = 764) -Honours or equivalent (n = 189) -Master's & PhD (n = 149)	33.0061[a] 57.4662[b] 43.8479[c]	24.7051 29.2703 28.0552
Means identified by different superscript differ significantly at the 5 % level.			

An ANOVA was performed to determine whether the understanding of the IR was the same, irrespective of whether respondents held post-graduate degrees or the level of their post-graduate degrees.

According to Levene's test, the assumption of equal variance was violated (p <0.0001) and thus Welch's test statistic had to be used. The null hypothesis that there are no differences between the average total percentage scores of respondents holding no or different levels of post-graduate degrees should be rejected ($F = 60.28$, $DF1 = 2$, $DF2 = 284.1$, $p < 0.0001$). This relates to a medium effect size ($r = 0.34$). It can thus be concluded that there are statistically significant differences between the average total percentage scores (means) of respondents holding no or different levels of post-graduate degrees. This is confirmed by the fact that the average total percentage scores (see Table 5.28, above) of graduates holding Honours degrees or equivalents (mean = 57.47) were higher than those of both respondents who do not hold a higher degree (mean = 33.01) and those holding Master's degrees and PhDs (mean = 43.85). *Post hoc* tests confirm that the means associated with respondents from all three groups differ significantly from each other.

- *Conclusion*

The perception of respondents who do not hold a post-graduate degree is that they do not understand the content of the IR, and their perception is borne out by the average total percentage score they achieved (mean = 33.01). Respondents holding an Honours degree or an equivalent as their highest post-graduate degree have the perception that they understand the content of IRs. This can probably be attributed to the fact that 103 (56%) of these respondents specialized in Accounting Sciences in their Honours degree or Post-graduate diploma. The latter finding would also explain why the mean of the group holding Honours degrees or equivalents was relatively high, at approximately 58%. By contrast, the mean of the group of respondents holding Master's degrees and PhDs from a diverse range of fields was approximately 44%, and their perceived level of understanding was also much lower than that of the respondents who held Honours degrees or equivalents. The apparent anomaly that respondents with Honours degrees or equivalents have a better understanding of IRs than respondents with Master's and PhD degrees may be linked to the fact that respondents who have an Honours degree or Post-graduate diploma in Accounting Sciences as their highest qualification have probably also qualified as chartered accountants eventually, as this is the minimum requirement for this sought-after professional qualification. Chartered accountants in South Africa, who mostly hold Honours degrees or Post-graduate diplomas, are considered to be highly skilled in accounting and financial matters.

5.4.1.5 Professional qualification

- *Discussion: Professional qualification held and perception of understanding of the content of IRs*

Table 5.29: Professional qualification held and perception of understanding of the content of IRs (n = 497)

	Understand	Don't understand	Total
Teaching			
Frequency	25	45	70
Expected frequency	47	23	
Cell Chi-Square	10.127	20.376	
Row percentage	35.7	64.3	100
Engineering and related			
Frequency	72	41	113
Expected frequency	75	38	
Cell Chi-Square	0.1609	0.3237	
Row percentage	63.7	36.3	100
Medical			
Frequency	38	43	81
Expected frequency	54	27	
Cell Chi-Square	4.7957	9.6495	
Row percentage	46.9	53.1	100
Financial			
Frequency	180	9	189
Expected frequency	126	63	
Cell Chi-Square	22.88	46.037	
Row percentage	95.2	4.8	100
Legal and other			
Frequency	17	27	44
Expected frequency	29	15	
Cell Chi-Square	5.2248	10.513	
Row percentage	38.6	61.4	100
Total	332	165	497
	69.03	30.97	100.00
Chi-square test statistic = 130.0874, $p < 0.0001$			

The above two-way table was constructed using the professional qualifications held by respondents and their perception as to whether they understood the content of the IR or not. The Chi-square test statistic of 130.0874 (DF = 4, $p < 0.0001$) provides convincing evidence that the null hypothesis of no association should be rejected. Statistically significant associations between the perceptions held by the two groups are evident, and it can be concluded that the perception of understanding of the IRs of respondents interacts with professional qualifications held by the respondents.

Table 5.29 clearly indicates that fewer respondents who had financially related professional qualifications hold a perception that they do not understand the content of the IR than was expected (cell Chi-square = 46.037). The opposite was true for those respondents who had a professional teaching qualification, where far more indicated that they did not understand the content of the IR than was expected (cell Chi-square = 20.376).

- *Discussion: Professional qualification held and understanding of the content of the IR as indicated by percentage score*

Table 5.30: ANOVA with professional qualification held as independent variable and average total percentage score on content as dependent variable (n = 520)

Test result	Breakdown of demographic group	Means (Average total percentage score)	Standard deviation
F = 95.44, DF1 = 4, DF2 = 515 and $p < 0.0001$	-Teaching (n = 77)	21.6450[a]	22.1597
	-Engineering & related (n = 118)	38.4181[b]	24.5092
	-Medical field (n = 86)	25.7752[a]	23.2899
	-Financial (n = 190)	67.6316[c]	21.2734
	-Legal & other (n = 49)	24.3764[a]	22.5045
Means identified by different superscript differ significantly at the 5% level.			

An ANOVA was performed to determine whether the understanding of the content of the IR is the same for respondents split into groups based on professional qualification.

According to Levene's test, the assumption of equal variances was not violated (p = 0.3978). The null hypothesis that there is no difference amongst the means of total percentage score of different professional qualification groups should be rejected (F = 95.44, DF1 = 4, DF2 = 515, $p < 0.0001$). This relates to a large effect size (r = 0.65). It can therefore be concluded that there are statistically significant differences between the average total percentage scores based on professional qualification of respondents. This was confirmed by the means (see Table 5.30), which show that respondents with a financially related professional qualification (mean = 67.63) outperformed those holding professional qualifications in the teaching, medical, legal and other fields (means range between 21.65 and 25.78). *Post hoc* tests confirmed that the mean of the average total percentage score of the respondents from the teaching profession (mean = 21.65) differs significantly from that of all professional groupings, except respondents from the medical profession (mean = 25.78) and legal and other professions (mean = 24.38). The mean of the respondents from the medical profession differs significantly from that of respondents from the financial professions, but not from that of respondents from the legal and other professions.

- *Conclusion*

It would appear as if the perception of understanding and understanding of respondents holding financially related professional qualifications are aligned with each other, and similarly, perception of understanding and the understanding of respondents holding the other professional qualifications are also aligned. The mean of total percentage score of the financially related professions is more than double that of the teaching, medical and legal and other professions. This is not unexpected, since financially related professionals generally have more exposure to accounting, finance and investments.

5.4.1.6 Field of work experience

- *Discussion: Field of work experience and perception of understanding of the content of IRs*

Table 5.31: Field of work experience and perception of understanding of the content of IRs (n = 1 036)

	Understand	Don't understand	Total
Accounting/investment/ banking and finance			
Frequency	273	43	316
Expected frequency	204	112	
Cell Chi-Square	23.052	42.2	
Row percentage	86.4	13.6	100
Medical and legal			
Frequency	50	62	112
Expected frequency	72	40	
Cell Chi-Square	6.9474	12.718	
Row percentage	44.7	55.3	100

	Understand	Don't understand	Total
Engineering, construction and related			
Frequency	116	69	185
Expected frequency	120	65	
Cell Chi-Square	0.1109	0.203	
Row percentage	62.7	37.3	100
Other			
Frequency	231	192	423
Expected frequency	274	149	
Cell Chi-Square	6.6219	12.122	
Row percentage	54.6	45.4	100
Total	670	366	1036
	64.67	35.33	100.00
Chi-square test statistic = 103.9752, p < 0.0001			

The above two-way table was constructed using the field of work experience and respondents' perceptions as to whether they understand the content of the IR or not. A Chi-square test with a test statistic of 103.9752 (DF = 3, $p < 0.0001$) provides convincing evidence that the null hypothesis of no association should be rejected. Statistically significant associations between the perceptions held by the two groups are evident, so it can be concluded that the respondents' perceptions of their understanding of the content of the IR interacts with their field of work experience.

From the cross-tabulation in Table 5.31, above, it is clear that more respondents who work in the accounting, investment, banking and finance field held the perception that they understood the content of the IR, than was expected (cell Chi-square = 23.052, with a row percentage of 86.4%).

The opposite is true for those respondents who work in the other fields where far more than expected indicated that they did not understand the content of the IR (cell Chi-square = 12.112, with a row percentage of 45.4%).

- *Discussion: Field of work experience and understanding of the content of IRs*

Table 5.32: ANOVA with field of work experience as independent variable and average total percentage score on content as dependent variable (n = 1 085)

Test statistic	Breakdown of demographic groups	Means (Average total percentage score)	Standard deviation
F = 83.37, DF1 = 3, DF2 = 1081, p < 0.0001	-Acc/Invest/Bank/Fin (n = 324) -Medical/Legal (n = 122) -Engineering, related (n = 190) -Other (n = 449)	56.6015[a] 26.2750[b] 37.0458[c] 30.3514[b]	26.0460 24.6808 23.9145 24.3914
Means identified by different superscript differ significantly at the 5 % level.			

An ANOVA was performed to determine whether the understanding of the content of the IR was the same for all groups of respondents irrespective of work experience.

According to Levene's test, the assumption of equal variances was not violated ($p = 0.28$). The null hypothesis that there is no difference between the average total percentage scores of different groups based on field of work experience should be rejected ($F = 83.37$, $DF1 = 3$, $DF2 = 1081$, $p < 0.0001$). This relates to a large effect size ($r = 0.43$). It can therefore be concluded that there is convincing evidence of statistically significant differences between the means based on the fields of work experience of respondents. This is confirmed by the means that show that respondents with experience in accounting, investing, banking and finance (mean = 56.60) performed much better than those who have work experience in other fields (mean = 30.35). *Post hoc* tests indicate that the mean of the total percentage score of respondents having experience in the accounting, banking, financial and investment field differs significantly from the means of the total percentage scores of the medical/legal fields (mean = 26.28), engineering/construction and related fields (mean = 37.05), as well as other fields of work experience. The mean of the medical/legal field does not differ significantly from that of respondents from "other" fields of experience. The lower mean for the accounting/investing/banking and finance group (56.60%) compared to respondents holding an Accounting major (61.67%, see Section 5.4.1.3) and Accounting as the focal area of their undergraduate degrees (74.11%, see Section 5.4.1.2) can be attributed to the fact that "field of work experience" is not focused on accounting exclusively (it includes a diverse group of qualifications such as engineering and MBAs), whereas in the other two instances Accounting is the field of specialization.

- *Conclusion*

The perception of understanding and average total percentage score of the respondents with experience in the work field of accounting, investing, banking and finance appear to be aligned with each other, and this finding also applies to respondents with working experience in other fields. This phenomenon is also evident when accounting majors in tertiary studies (see the tables in Section 5.4.1.3) and focal areas of undergraduate degrees (see the tables in Section 5.4.1.2) are considered. In both these instances, respondents with an accounting background have a higher mean of total percentage score and more of them are of the opinion that they understand the content of the IR.

5.4.1.7 Employment status

- *Discussion: Employment status and perception of understanding of the content of IRs*

Table 5.33: Employment status of respondents and perception of understanding of the content of IRs (n = 1 044)

	Understand	Don't understand	Total
Full-time employment			
Frequency	316	148	464
Expected frequency	299	165	
Cell Chi-Square	0.9536	1.7299	
Row percentage	68.1	31.9	100
Part-time employment			
Frequency	61	42	103
Expected frequency	66	37	
Cell Chi-Square	0.4388	0.7959	
Row percentage	59.2	40.8	100
Retired			
Frequency	274	69	440
Expected frequency	284	65	
Cell Chi-Square	0.3276	0.203	
Row percentage	62.7	37.3	100
Unemployed, housewife, student			
Frequency	22	15	37
Expected frequency	24	13	
Cell Chi-Square	0.1437	0.2607	
Row percentage	59.5	40.5	100
Total	670	366	1044
	64.67	35.33	100.00
Chi-square test statistic = 5.2446, p = 0.1547			

The above two-way table was constructed using the employment status and perception of respondents as to whether or not they understand the content of the IR. The Chi-square test statistic of 5.2446 (with DF =3, p = 0.1547) provides no evidence of any association between employment status and perception of understanding. Therefore, no statistically significant association between the perceptions held by the different groups is evident, and it could be concluded that the perception of understanding of the IR of respondents is independent of the employment status of respondents.

- *Discussion: Employment status and understanding of the content of IRs*

Table 5.34: ANOVA with employment status as independent variable and average total percentage score on content as dependent variable (n = 1 098)

Test result	Breakdown of demographic group	Means (Average total percentage score)	Standard deviation
F = 19.14, DF1 = 3, DF2 = 152.0, p < 0.0001 (Welch)	-Full-time employment (n = 481) -Part-time employment (n = 105) -Retired (n = 473) -Unemployed/housewife/student (n = 39)	45.4147^{a} 38.4656^{b} 32.1118^{c} 34.9003^{bc}	28.4087 25.6873 25.9260 22.6189
Means identified by different superscript differ significantly at the 5% level.			

An ANOVA was performed to determine whether the understanding of the content of the IR was the same for respondents, irrespective of employment status.

According to Levene's test, the assumption of equal variances was violated (p = 0.0032) and thus Welch's test statistic was used. The null hypothesis that there is no difference between the mean of different categories of employment status should be rejected. It can therefore be concluded that there are statistically significant differences between at least two of the average total percentage scores based on the respondents' employment status (F = 19.14, DF1 = 3, DF2 = 152.0, p < 0.0001). This relates to a medium effect size (r = 0.23). *Post hoc* tests confirmed that the mean of total percentage score of respondents employed on a full-time basis differs significantly from the means of all three the other categories of employment (part-time, retired, unemployed/housewives/students). In the case of the mean of total percentage score of respondents employed on a part-time basis, it differs significantly from the mean of retired respondents, but there is no significant difference between the mean of respondents that are employed on a part-tune basis and the mean of respondents who are unemployed/housewives/students. There is no significant difference between the means of retired respondents and respondents who are unemployed/housewives/students.

- *Conclusion*

It would appear as if respondents who are employed understand the content of IRs marginally better than those that are not employed, although employment status does not show a significant association with perception of understanding. Employment status appears to be a poor predictor of level of understanding of IRs.

5.4.2 Number of shares held in the specific company for which an IR was received, Rand value of shareholding and overall portfolio size of respondents

In this section of the chapter, the association between the number of shares held by an individual shareholder (respondent), the Rand value of shares held and the overall portfolio size (number of companies in portfolios) of respondents and the perception of understanding and the understanding the content of IRs are considered.

5.4.2.1 Number of shares held in a specific company

- *Discussion: Number of shares held by respondents in a specific company and perception of understanding of the content of IRs*

Table 5.35: Number of shares held in a specific company and perception of understanding of the content of IRs (n = 939)

	Understand	Don't understand	Total
Number of shares held = 0			
Frequency	19	10	29
Expected frequency	19	10	
Cell Chi-Square	0.0001	0.0001	
Row percentage	65.5	34.5	100
Number of shares held >0- 100			
Frequency	83	46	129
Expected frequency	84	45	
Cell Chi-Square	0.0217	0.0409	
Row percentage	64.3	35.7	100

	Understand	Don't understand	Total
Number of shares held >100 – 250			
Frequency	72	36	108
Expected frequency	71	37	
Cell Chi-Square	0.027	0.051	
Row percentage	66.7	33.3	100
Number of shares held >250 – 500			
Frequency	98	57	155
Expected frequency	101	54	
Cell Chi-Square	0.1109	0.2095	
Row percentage	63.2	36.8	100
Number of shares held >500 – 1000			
Frequency	105	59	164
Expected frequency	107	57	
Cell Chi-Square	0.0467	0.0882	
Row percentage	64.0	36.0	100
Number of shares held >1000 – 2500			
Frequency	100	65	165
Expected frequency	108	57	
Cell Chi-Square	0.5772	1.0904	
Row percentage	60.6	39.4	100
Number of shares held >2500 – 5000			
Frequency	49	26	75
Expected frequency	49	26	
Cell Chi-Square	0.0000	0.0001	
Row percentage	65.3	34.7	100
Number of shares held >5000 – 10000			
Frequency	36	17	53
Expected frequency	35	18	
Cell Chi-Square	0.0521	0.0985	
Row percentage	67.9	32.1	100
Number of shares held >10000 – 15000			
Frequency	14	6	20
Expected frequency	13	7	
Cell Chi-Square	0.065	0.1229	
Row percentage	70.0	30.0	100

	Understand	Don't understand	Total
Number of shares held >15000 – 30000			
Frequency	21	1	22
Expected frequency	14	8	
Cell Chi-Square	3.0414	5.7458	
Row percentage	95.4	4.6	100
Number of shares held >30000 – 340000			
Frequency	17	2	19
Expected frequency	12	7	
Cell Chi-Square	1.6856	3.1844	
Row percentage	89.5	10.5	100
Total	614	325	939
	65.4	34.6	100.00
Chi-square test statistic = 16.2593, p = 0.0924			

A Chi-square test was used to test for a relationship between the number of shares held and the perceptions of respondents as to whether or not they understood the content of the IR. The Chi-square test statistic of 16.2593 (DF = 10, p = 0.0924) provides no evidence of association between the number of shares held and perception of understanding. No statistically significant association between the perceptions held by the different groups is evident, so it can be concluded that the perception of understanding of the IR of respondents is independent of the number of shares held by respondents.

- *Discussion: Number of company shares held by respondents and understanding of the content of IRs*

Table 5.36: ANOVA with number of company shares held by shareholders as independent variable and average total percentage score on content as dependent variable (n = 972)

Test statistic	Breakdown of demographic group	Means (Average total percentage score)	Standard deviation
F = 1.53, DF1 = 10, DF2 = 961, p = 0.1247	-SH = 0 (n = 30)	42.4074	28.0820
	-SH 0 to 100 (n = 134)	38.6401	27.0529
	-SH 101 to 250 (n = 110)	40.9091	27.4314
	-SH 251 to 500 (n = 160)	38.9583	28.1491
	-SH 501 to 1000 (n = 173)	36.6089	26.5080
	-SH 1001 to 2500 (n = 169)	39.2176	26.3433
	-SH 2501 to 5000 (n = 78)	35.4701	27.3375
	-SH 5001 to 10000 (n = 54)	49.2798	28.5541
	-SH 10001 to 15000 (n = 21)	43.9153	27.4371
	-SH 15001 to 30000 (n = 24)	46.0648	30.5382
	-SH 30001 plus (n = 19)	47.9532	21.5333

An ANOVA was performed to determine whether the understanding of the IR is the same for respondents irrespective of the number of shares held by them.

According to Levene's test, the assumption of equal variances was not violated ($p = 0.7294$). The null hypothesis that there is no difference between the average total percentage scores of the groups comprising different numbers of shares held ($F = 1.53$, $DF1 = 10$, $DF2 = 961$, $p = 0.1247$) should not be rejected. This relates to a small effect size ($r = 0.13$). It can therefore be concluded that there is no evidence of statistically significant differences between the means based on the number of shares held by respondents.

- *Conclusion*

There is no statistically significant association between the perception of understanding of the content of the IR and the average total percentage scores achieved by the groups based on the number of shares held.

5.4.2.2 Rand value of shares held in specific company for which IR was received

- *Discussion: Rand value of shares in company held by respondents and <u>perception</u> of understanding of the content of IRs*

Table 5.37: Rand value of shares held in a specific company and <u>perception</u> of understanding of the content of IRs (n = 939)

	Understand	Don't understand	Total
Rand value of shares held			
= 0			
Frequency	19	10	29
Expected frequency	19	10	
Cell Chi-Square	0.0001	0.0001	
Row percentage	65.5	34.5	100
Rand value of shares held			
>0 – 2500			
Frequency	46	25	71
Expected frequency	46	25	
Cell Chi-Square	0.0039	0.0074	
Row percentage	64.8	35.2	100
Rand value of shares held			
>2500 – 5000			
Frequency	54	16	70
Expected frequency	46	24	
Cell Chi-Square	1.479	2.7942	
Row percentage	77.1	22.9	100
Rand value of shares held	65	30	95
>5000 – 10000	62	33	
Frequency	0.1336	0.2524	
Expected frequency	68.4	31.6	100
Cell Chi-Square			
Row percentage			
Rand value of shares held			
>10000 – 20000			
Frequency	98	49	147
Expected frequency	96	51	
Cell Chi-Square	0.0367	0.0694	
Row percentage	66.7	33.3	100
Rand value of shares held			
>20000 – 50000			
Frequency	107	84	191
Expected frequency	125	66	
Cell Chi-Square	2.5633	4.8427	
Row percentage	56.0	44.0	100

	Understand	Don't understand	Total
Rand value of shares held			
>50000 – 100000	67	47	114
Frequency	75	39	
Expected frequency	0.7633	1.4421	
Cell Chi-Square	58.8	41.2	100
Row percentage			
Rand value of shares held			
> 100000 – 200000			
Frequency	78	45	123
Expected frequency	80	43	
Cell Chi-Square	0.0733	0.1385	
Row percentage	63.4	36.6	100
Rand value of shares held			
>200000 – 500000			
Frequency	36	9	45
Expected frequency	29	16	
Cell Chi-Square	1.4692	2.7757	
Row percentage	80.0	20.0	100
Rand value of shares held			
>500000			
Frequency	44	10	54
Expected frequency	35	19	
Cell Chi-Square	2.1387	4.0405	
Row percentage	81.5	18.5	100
Total	614	325	939
	65.39	34.61	100.00
Chi-square test statistic = 25.0241, p = 0.0029			

The above two-way table was constructed using the Rand value of shares held and the perceptions of respondents as to whether or not they understand the content of the IR. The Chi-square test statistic of 25.0241 (DF = 9, p = 0.0029) provides evidence that the null hypothesis of no association should be rejected. Statistically significant associations between the perceptions held by the different groups are evident and it can be concluded that the perception of understanding of the content of the IR of respondents interacts with the Rand value of shares held by the respondents.

From the cross-tabulation in Table 5.37, it is clear that cell Chi-square statistics are mostly low, with the exception of the respondents holding shares with a Rand value greater than R20 000 and up to R50 000 (cell Chi-square = 4.8427). In this instance, more respondents than expected indicated that they did not understand the content of the IR. In most other instances, the difference in perception could be attributed to chance.

- *Discussion: Rand value of shares in company held by respondents and understanding of the content of IRs*

Table 5.38: ANOVA with Rand value of shares held as independent variable and average total percentage score on content as dependent variable (n = 972)

Test result	**Breakdown of demographic group (RV = Rand value of shares held)**	**Means (Average total percentage score)**	**Standard deviation**
F = 1.94, DF1 = 9, DF2 = 962, p = 0.0438	-RV of shares held = 0 (n = 30)	42.4074[ab]	28.0820
	-RV >0 to 2500 (n = 72)	39.1204 [ab]	25.5089
	-RV >2500 to 5000 (n = 72)	46.3735[a]	28.0218
	-RV >5000 to 10000 (n = 100)	40.2222[ab]	28.4719
	-RV >10000 to 20000 (n = 152)	39.5468[ab]	26.3382
	-RV >20000 to 50000 (n = 199)	35.3992[b]	27.8016
	-RV >50000 to 100000 (n = 119)	35.9477[b]	26.3357
	-RV >100000 to 200000 (n = 127)	40.2450 [ab]	27.0334
	-RV >200000 to 500000 (n = 46)	43.7198 [ab]	28.0752
	-RV >500000 plus (n = 55)	47.3737[a]	26.3383
Means identified by different superscript differ significantly at the 5 % level.			

An ANOVA was performed to determine whether the understanding of the IR is the same for respondents irrespective of the Rand value of shares held by these respondents.

According to Levene's test, the assumption of equal variances was not violated (p = 0.8966). The null hypothesis that there is no differences amongst the average total percentage scores of the groups of respondents based on Rand value should be rejected (F = 1.94, DF1 = 9, DF2 = 962, p = 0.0438). This relates to a small effect size (r = 0.13). It can therefore be concluded that there is evidence of statistically significant differences between at least two of the means of total percentage score based on the Rand value of shares held by respondents. This was also confirmed by *post hoc* tests. The mean of the Rand value interval ranging between just more than R2 500 and up to R5 000 (mean = 46.37) differs significantly from the two Rand value intervals starting just above R20 000 and up to R50 000 (mean = 35.40) and above R50 000 up to R100 000 (mean = 35.95). The means of the latter two Rand value intervals also differ significantly from the Rand value interval starting above R500 000 (mean = 47.37). Nevertheless all means of the Rand value intervals are below 48%.

- *Conclusion*

It can be concluded that in the case of the Rand value of share portfolios held by individual shareholders, there is a limited association between the perception of understanding of the content of the IR and the average total percentage scores achieved by the corresponding groups. Although a few differences in average total percentage score (means) of the Rand value intervals are statistically significant, it would appear as if respondents holding more than R500 000 worth of shares achieved slightly higher means than those in most other Rand value intervals.

5.4.2.3 Number of companies in a respondent's portfolio

- *Discussion: Number of companies in share portfolio and perception of understanding of the content of IRs*

Table 5.39: Number of companies in portfolio and perception of understanding of the content of IRs (n = 1 010)

	Understand	**Don't understand**	**Total**
Number of companies 0 <= 20			
Frequency	470	258	728
Expected frequency	473	255	
Cell Chi-Square	0.0171	0.0316	
Row percentage	64.6	35.4	100
Number of companies >20 <= 40			
Frequency	148	83	231
Expected frequency	150	81	
Cell Chi-Square	0.0276	0.0512	
Row percentage	64.1	35.9	100
Number of companies >40 <= 60			
Frequency	28	10	38
Expected frequency	25	13	
Cell Chi-Square	0.4463	0.827	
Row percentage	73.7	26.3	100
Number of companies >60 <= 195			
Frequency	10	3	13
Expected frequency	8	5	

	Understand	Don't understand	Total
Cell Chi-Square *Row percentage*	0.2869 76.9	0.5317 23.1	 100
Total	656 64.9	354 35.1	1010 100.00
Chi-square test statistic = 2.2193, p = 0.5282			

A two-way table was constructed using the number of companies in the share portfolios of respondents and the perceptions of respondents as to whether they understood the content of the IR or not. The Chi-square test statistic of 2.2193 (DF = 3, p = 0.5282) provided convincing evidence that the null hypothesis of no association should not be rejected. There thus appears to be no statistically significant association between the perceptions held by the different groups based on number of companies in the share portfolio. The conclusion is that the perception of understanding of the IR of respondents does not interact with the number of companies in respondents' share portfolios.

- *Discussion: Number of companies in share portfolios and understanding of the content of IRs*

Table 5.40: ANOVA with number of companies in share portfolio as independent variable and average total percentage score on content as dependent variable (n = 1 055)

Test result	Breakdown of demographic group	Means (Average total percentage score)	Standard deviation
F = 0.97, DF1 = 3, DF2 = 1051, p = 0.4039	-NC 0 to 20 (n = 758) -NC 21 to 40 (n = 244) -NC 41 to 60 (n = 40) -NC 61 to 195(n = 13)	38.6837 40.1639 45.8333 38.0342	27.2502 28.1506 26.4722 25.9437

An ANOVA was performed to determine whether the understanding of the IR is the same for respondents, irrespective of the number of companies in their share portfolios.

According to Levene's test, the assumption of equal variances was not violated (p = 0.6647). The null hypothesis that there are no differences amongst the average total percentage scores of the different groups based on number of companies in share portfolios should not be rejected (F = 0.97, DF1 = 3, DF2 = 1051, p = 0.4039). This relates to a small effect size (r = 0.05). The conclusion is thus that there is no convincing evidence of statistically significant differences between the average total percentage scores based on the number of companies in respondents' share portfolios. This is confirmed by the means of all groups – the means are concentrated in a tight band of between approximately 38% and 46%.

- *Conclusion*

The number of companies in the share portfolio of an individual shareholder is a poor indicator of understanding of the content of IRs.

5.4.3 Investment objectives and decisions

In Tables 5.41 to 5.44 in this section of the chapter, the association between investment objectives and the way investment decisions are taken and the perception of understanding and the understanding of IRs are considered.

5.4.3.1 Investment objectives

- *Discussion: Respondents' investment objectives and their perception of their understanding of the content of IRs*

Table 5.41: Investment objectives and perception of understanding of the content of IRs (n = 1 044)

	Understand	Don't understand	Total
Speculative and other			
Frequency	12	14	26
Expected frequency	17	9	
Cell Chi-Square	1.3521	2.4528	
Row percentage	46.2	53.8	100
Long-term capital growth			
Frequency	246	111	357
Expected frequency	230	127	
Cell Chi-Square	1.0937	1.984	
Row percentage	68.9	31.1	100
Dividend return and steady income stream			
Frequency	38	34	72
Expected frequency	46	26	
Cell Chi-Square	1.5252	2.7668	
Row percentage	52.8	47.2	100

	Understand	Don't understand	Total
Combination of dividend return and long-term growth			
Frequency	377	212	589
Expected frequency	380	209	
Cell Chi-Square	0.0191	0.0346	
Row percentage	64.0	36.0	100
Total	673	371	1044
	64.46	35.54	100.00
Chi-square test statistic = 11.2283, p = 0.0106			

The above two-way table was constructed using respondents' investment objectives and their perceptions as to whether or not they understood the content of the IR. The Chi-square test statistic of 11.2283 (DF = 3; p = 0.0106) provided convincing evidence that the null hypothesis of no association should be rejected. Statistically significant associations between the perceptions held by the groups of respondents distinguished by investment objectives are evident, and it can be concluded that respondents' perceptions of understanding of the content of the IR interact with the respondents' investment objectives.

Table 5.41 shows that cell Chi-square statistics are mostly low, with the marginal exception of the respondents who held shares with the objective of earning a dividend return and steady income from it (cell Chi-square = 2.7668) and respondents with speculative intentions (cell Chi-square = 2.4528). In these instances, more respondents than expected indicated that they did not understand the content of the IR.

- *Discussion: Respondents' investment objectives and their <u>understanding</u> of the content of IRs*

Table 5.42: ANOVA with investment objective as independent variable and average total percentage score on content as dependent variable (n = 1095)

Test result	Breakdown of demographic group	Means (Average total percentage score)	Standard deviation
F = 12.62, DF1 = 3, DF2 = 100.9 (Welch), p < 0.0001	-Speculative gains/Other (n = 26) -Long-term capital growth (n = 367) -Dividend income (n = 78) -Combination of dividends and LT capital growth (n = 624)	24.5727[a] 43.5816[b] 27.0655[a] 38.0520[c]	20.8565 28.3489 26.2167 26.8683
Means identified by different superscript differ significantly at the 5 % level.			

An ANOVA was performed to determine whether the understanding of the IR is the same in all groups, irrespective of the investment objectives of respondents.

According to Levene's test, the assumption of equal variances was violated ($p = 0{,}0259$) and thus Welch's test statistic was used. The null hypothesis that there are no differences between the average total percentage scores of different groups based on investment objective should be rejected ($F = 12.62$, $DF1 = 3$, $DF2 = 100.9$, $p < 0.0001$). This relates to a small effect size ($r = 0.17$). It can therefore be concluded that there are statistically significant differences between at least two of the average total percentage scores (means) of the different groups of respondents based on investment objective. *Post hoc* tests confirmed that there are significant differences between the means of the different groups, except between the group that has speculative gains and other unrelated matters as objective (mean = 24.57) and the group that has dividend returns and a steady income as their investment objective (mean = 27.07).

- *Conclusion*

The perception of understanding interacts with the investment objectives. It would appear as if information contained in the IR is understood better by respondents with long-term capital growth (mean = 43.58) and a combination of dividend and capital growth (mean = 38.05) as their investment objectives. However, both these means are still below an acceptable assumed pass mark of 50%. It is, however, surprising that speculative investors did not have a higher level of understanding of IRs, as they actively trade in shares on a frequent basis.

5.4.3.2 Investment made on own initiative or financial advisor initiative

- *Own or financial advisor initiative and perception of understanding of IRs' content*

Table 5.43: Investments made on own or financial advisor initiative and perception of understanding of the content of IRs (n = 1 025)

	Understand	Don't understand	Total
Investments done on own initiative			
Frequency	602	263	865
Expected frequency	565	300	
Cell Chi-Square	2.3673	4.4678	
Row percentage	69.6	30.4	100.0

	Understand	Don't understand	Total
Financial advisor takes the initiative with investments			
Frequency	68	92	160
Expected frequency	105	55	
Cell Chi-Square	12.798	24.154	
Row percentage	42.5	57.5	100.0
Total	670	355	1025
	65.37	34.63	100.00
Chi-square test statistic = 43.7872, p < 0.0001			

The above two-way table was constructed using respondents' investment objectives and their perceptions as to whether they understood the content of the IR or not. The Chi-square test statistic of 43.7872 (DF = 1, p < 0.0001) provides convincing evidence that the null hypothesis of no association should be rejected. There is therefore statistical evidence that whether the initiative for the investment decision was taken by the respondents or the financial advisor interacts with respondents' perceptions of their understanding of the IR.

From Table 5.43 it is clear that significantly more respondents who allow financial advisors to take the investment initiative held the perception that they did not understand the content of the IR than was expected (cell Chi-square = 24.154). The opposite is also evident in that significantly fewer respondents who made investment decisions on their own initiative held the perception that they did not understand the content of the IR (cell Chi-square = 4.4678).

- *Discussion: Own or financial advisor initiative and <u>understanding</u> of the content of IRs*

Table 5.44: T-test between who takes the initiative when making investment decisions and <u>understanding</u> of the content of IRs (n = 1 071)

Own initiative (n = 901)		Broker initiative (n = 170)	
Mean (Average total percentage score)	**Standard Deviation**	**Mean (Average total percentage score)**	**Standard Deviation**
41.3245	27.5931	29.3137	24.8011
T = 5.29, p < 0.0001			

A t-test for two independent samples was performed to assess whether the total percentage score of respondents who used their own initiative when taking investment decisions differed from that of respondents who allowed the financial advisor to take the initiative. In this instance, the assumption of equal variances was not violated ($p = 0.084$) and consequently the pooled method was used ($T = 5.29$, $DF = 1069$, $p < 0.0001$). This relates to a small effect size since $r = 0.16$. The test statistic indicates that the null hypothesis should be rejected at the 5% level. The outcome of the test shows that the average total percentage score of respondents (understanding of the content of the IR) who made investment decisions of their own initiative (mean = 41.33) and those whose financial advisor took the investment initiative (mean = 29.31) differ significantly. Given the level of the means, it is probably appropriate that the latter group of respondents allowed their financial advisors to make investment decisions.

- *Conclusion*

When relating the outcomes of the two tests mentioned above, it is confirmed that respondents who made investments of their own initiative have a perception that they have a better understanding of the content of the IR than those who let financial advisors make the investment decisions. This is not surprising, as one would assume the first-mentioned respondents to have a fair knowledge of financial matters, especially since they are taking investment decisions of their own initiative and *vice versa*. Although the mean of respondents who make investment decisions of their own initiative is higher than that of respondents who depend on their financial advisors to make investment decisions, in both instances their understanding was still rated at below 42%. At most, it can be concluded that respondents who made their own investment decisions have a better understanding of the content of IRs than those respondents who depended on their financial advisors to make investment decisions.

5.4.4 Assessing perception of understanding and understanding of respondents of the individual components comprising the IR

Up to this point, whilst addressing the primary objective of the study, respondents' perceptions of their own understanding and respondents' understanding of the content of IRs have been considered. In this section of the study, the analysis and discussion of the empirical data focus on their perceptions and understanding of the individual components (condensed statements of financial position, comprehensive income, changes in equity etc.) comprising the IR. The objective here was to identify which components are understood well, and which are understood less well. As with the assessment of perception of understanding for the IR as a whole, the perception of understanding for the individual components was split into two categories, namely "Understand" and "Don't understand". Due to the nature of the questions in the questionnaire, the perception of understanding per individual component of IRs could be identified successfully.

Because the understanding of each individual component of the IR in the questionnaire was assessed using only two questions per component, and because of the difference in level of difficulty of individual questions (and the resulting variation in marks awarded per question), it was not feasible to calculate a mean per individual component that could serve as a "centre of gravity" for assessing level of knowledge/importance etc., as was done in other instances later in this chapter. Consequently, it was not possible to derive whether individual shareholders understand each of the individual components of IRs on the basis of the data collected in the questionnaire. Nevertheless, the data per individual component of IRs were analysed and are addressed below to provide some indication of the understanding of the individual questions posed to individual shareholders.

In the case of the questions in the questionnaire assessing the understanding of the individual components of IRs, the marks awarded to respondents per question were provided for each component and the number of respondents who achieved those marks was determined.

5.4.4.1 Perception of understanding of individual components of the IR

The questions in the questionnaire that facilitate this part of the study are the following: for perception of understanding, Question 21 (see Table 5.45), and for understanding of the individual components Questions 22 to 26 (see Table 5.46). The responses to questions on perception of understanding and understanding of individual components are summarized in the two tables below and the content of each table is debated directly below the relevant table.

Question 21

How well do you understand the following components of the interim financial report?

Table 5.45: Frequency table of perception of understanding of individual components of the IR

Individual components of IR	Perception: Understand		Perception: Don't understand	
	Very well	Well	Not well	Not at all
Comment / Commentary of management (n = 1034)	323 (31.2%)	439 (42.5%)	195 (18.9%)	77 (7.4%)
	762 (73.7%)		272 (26.3%)	
Explanatory notes (n = 1031)	249 (24.1%)	440 (42.7%)	249 (24.2%)	93 (9.0%)
	689 (66.8%)		342 (33.2%)	
Condensed Statement of comprehensive income / Income statement (n = 1032)	234 (22.7%)	393 (38.1%)	272 (26.3%)	133 (12.9%)
	627 (60.8%)		405 (39.2%)	
Condensed Statement of financial position / Balance sheet (n = 1048)	211 (20.1%)	384 (36.6%)	316 (30.2%)	137 (13.1%)
	595 (56.8%)		453 (43.2%)	
Condensed Statement of cash flows / Cash flow statement (n = 1026)	185 (18.1%)	376 (36.6%)	314 (30.6%)	151 (14.7%)
	561 (54.7%)		465 (45.3%)	
Condensed Statement of changes in equity (n = 1028)	158 (15.4%)	295 (28.7%)	378 (36.8%)	197 (19.1%)
	453 (44.1%)		575 (55.9%)	

When interpreting the information in this table, it was assumed that respondents who believed that they understood an individual component of the IR "very well" or "well" held the perception that they understood the specific component, while the others had the perception that they did not understand the specific component.

In the case of understanding considered hereafter, as with the IR as a unit, it was not possible to assess understanding of the comment/commentary by management. It is the case since this information is not standardized from any one company to the next, as circumstances and events pertaining to each specific company would be unique to that company. Consequently only the perception of understanding of respondents related to this specific component of the IR could be addressed and not understanding of the specific component.

- *Conclusion on perception of understanding*

Based on the information presented in Table 5.45, above, and applying the assumption explained in the paragraph below the table, it would appear as if the majority of respondents believed they understood the comment/commentary of management (73.7%), while slightly fewer of the respondents believed they understood the explanatory notes (66.8%). The majority of respondents believed that they understood the condensed statement of changes in equity "not well" or "not at all" (55.9%).

5.4.4.2 Understanding of the individual components of the IR

As explained in Section 5.4.4, it was not possible to assess how well respondents understood the individual components. However, Table 5.45, overleaf, contains the questions related to each specific component, as well as an exposition of the related responses. Also included in Table 5.46, below the correct answer, is an analysis of the perception of understanding of the respondents who answered a specific question correctly. The percentage of respondents who had the perception that they understood the component of the IR to which the question related is indicated by PU (perception: understand) and those who did not believe they understood the question is indicated by PDU (perception: don't understand). No conclusion in respect of the understanding of individual components could be drawn from the content of this specific table. This is an opportunity for further research on IRs.

Table 5.46: Understanding of the questions related to individual components of IRs

Individual component of IR and related questions					
Condensed Statement of financial position / Balance sheet (n = 1047)	**Original cost price**	**Cost less depreciation**	**Replacement cost**	**Lower of cost and NRV**	**Don't know**
Question 22 (2 marks): What basis of valuation is used to determine the carrying amounts (book values) of the following items included in the condensed balance sheet / statement of financial position? This question relates to property, plant and equipment (fixed assets).	5.2	52.6 **Correct** **PU** = 68.9 **PDU** = 29.6	6.8	2.9	32.5
Discussion: This question required some accounting knowledge, and the percentage of correct responses (52.6) is thus not surprising. A substantial number of respondents indicated that they did not know the answer.					
Condensed Statement of financial position / Balance sheet (n = 1024)	**Original cost price**	**Cost less depreciation**	**Replacement cost**	**Lower of cost and NRV**	**Don't know**
Question 22 (3 marks): What basis of valuation is used to determine the carrying amounts (book values) of the following items included in the condensed balance sheet/statement of financial position? This question relates to inventory (stock).	23.6	6.4	8.4	27.1 **Correct** **PU** = 42.4 **PDU** = 5.3	34.5
Discussion: This question required detailed knowledge of accounting and thus the low percentage of correct responses (27.1) was expected. Once again a substantial portion (34.5%) of respondents indicated that they did not know the answer.					

Condensed Statement of comprehensive income / Income statement (n = 1037)	**Yes**	**No**	**Don't know**
Question 24 - Statement requiring a "Yes or No" answer (1 mark)**:** The profit before tax line-item on the condensed income statement/statement of comprehensive income represents the difference between income/revenue received and/or earned and expenses paid and/or incurred during the six months under review.	68.8 **Correct** **PU** = 85.3 **PDU** = 29.0	4.2	27.0
Discussion: As can be seen from the mark allocation, the answer of this question was evident from the IR, and thus the high percentage of correct responses (68.8) was anticipated.			
Condensed Statement of comprehensive income / Income statement (n = 1033)	**Yes**	**No**	**Don't know**
Question 24 - Statement requiring a "Yes or No" answer (2 marks)**:** The line-item for tax in the condensed income statement/statement of comprehensive income includes merely the taxation payable to SARS.	42.7	26.2 **Correct** **PU** = 12.3 **PDU** = 34.5	31.1
Discussion: Although a slightly lower percentage of correct responses for this question was expected, the very low percentage of correct responses (26.2) was surprising. A large number of respondents answered this question incorrectly, since the incorrect answer could easily be mistaken for the correct one if one does not have a reasonable accounting knowledge.			
Condensed Statement of changes in equity (n = 1027)	**Yes**	**No**	**Don't know**
Question 24 - Statement requiring a "Yes or No" answer (1 mark)**:** The condensed statement of changes in equity reflects all movements in equity (share capital and reserves) that occurred during the six month period under review.	61.7 **Correct** **PU** = 84.1 **PDU** = 41.0	4.3	34.0

Discussion:

Although it is indicated in Table 5.44 that respondents did not consider the statement of changes in equity important when making investment decisions, a high percentage of responses were correct (61.7) and this is in line with the low level of difficulty of the question. A substantial percentage of respondents indicated that they did not know the answer.

Condensed Statement of changes in equity (n = 1028)	**Yes**	**No**	**Don't know**
Question 24 - Statement requiring a "Yes or No" answer (2 marks)**:** The final balances on the condensed statement of changes in equity can be linked to condensed balance sheet/statement of financial position items at the end of the six month period.	49.2 **Correct** **PU** = 73.5 **PDU** = 28.2	6.0	44.8

Discussion:

The low number of correct responses can in all probability be attributed to the fact that this was a more challenging question. Furthermore, the presentation in the IRs of two of the three companies was not as clear as it could have been, although the final numbers in the respective statements of changes in equity do tie up with the final balances in the statement of financial position. What is interesting in this instance is that nearly 45% of responses were "I really do not know" – this is the highest number of such responses received for any question.

Condensed Statement of cash flows / Cash flow statement (n = 1030)	**Yes**	**No**	**Don't know**
Question 24 - Statement requiring a "Yes or No" answer (2 marks)**:** Net cash flows from operating activities in the condensed cash flow statement/statement of cash flows include interest payable and dividends payable.	41.6	25.0 **Correct** **PU** = 34.0 **PDU** = 12.9	33.40

Discussion:

This was a question requiring some accounting knowledge, so the low percentage of correct responses (24.95) was not entirely surprising, although it was unexpectedly low.

Condensed Statement of cash flows / Cash flow statement (n = 1034)	**Yes**	**No**	**Don't know**
Question 24 - Statement requiring a "Yes or No" answer (2 marks)**:** The purchase of property, plant and equipment (fixed assets) on credit, would represent a cash outflow under	35.4	30.9 **Correct** **PU** = 18.9	33.7

investing activities on the condensed cash flow statement/statement of cash flows.		**PDU** = 39.9	

Discussion:

This question required some knowledge of accounting, but not more than any other question with a mark allocation of 2. Consequently the low percentage of correct responses was not anticipated.

Explanatory notes (n = 1060)	**Creditworthy-ness policy**	**Policy for amounts in F/S**	**Policy on Exchange of goods**	**Don't know**
Question 25 (2 marks)**:** What do you understand under the term "Accounting policy"?	3.7	75.3 **Correct** **PU** = 85.8 **PDU** = 54.1	2.1	18.9

Discussion:

In line with the perception that respondents understood the explanatory notes fairly well (ranked second in Table 5.51), the percentage of correct responses in this instance was very high, at nearly 76%. This high level of understanding was also corroborated by the fact that, in this case, the lowest percentage of responses fell into the "I really don't know" category.

Explanatory notes (n = 1065)	**Yes**	**No**	**Don't know**
Question 26 (1 mark)**:** Are the accounting policies used in the interim financial report the same as those used in the annual financial statements of the company?	64.0	8.0 **Correct** **PU** = 7.5 **PDU** = 7.3	28.0

Discussion:

The extremely low percentage of correct responses in the case of this question (8.0) was disappointing, as it is clearly stated in the explanatory note of each of the IRs that there are a number of differences between the accounting policies applied in the IRs and the annual financial statements. One possible reason for the low percentage of correct responses could be that respondents did not read the explanatory notes thoroughly and assumed that, since the accounting policies of the IRs and annual financial statements would usually be the same, it would also be the case here. However, this was not the case in any one of the three IRs used in the study.

5.5 SUMMARY OF FINDINGS ON THE PRIMARY RESEARCH OBJECTIVE

On the basis of the detailed analysis above in respect of the primary research objective related to the understanding of IRs and the analysis per demographic variable, the main results are presented in Table 5.47, below.

Table 5.47: Summary of findings associated with the primary objective

Primary research objective	
5.3 Assessing perception of understanding and understanding of IRs by individual shareholders, distinguishing between context and content.	
5.3.1 Context and content	
Understanding: Individual shareholders appeared to have a marginally better understanding of the context and content (combined) of IRs, since the mean of total percentage score including questions on both context and content was slightly higher at 42.72% than the 38.67% for content only. However, both these means are below an assumed acceptable total percentage score of 50%.	
5.3.2 Content	
Understanding: Individual shareholders appeared to have a limited understanding of the content of IRs, achieving a mean of total percentage score of 38.67%, as opposed to an assumed acceptable total percentage score of 50%. **Perception of understanding**: Respondents who believed they did not understand the content of IRs achieved a lower mean (20.11%) than those who believed they understood the content of the IRs (50.53%).	
5.3.3 Context	
The difference between the mean of total percentage score for content only (38.67) and the mean of context and content (42.72) is attributed to the fact that individual shareholders scored higher percentages in the questions on context if these are isolated. Of the individual questions on context, the question on who bears legal responsibility for the preparation of IRs was answered the worst.	
Further analysis of the primary research objective (content only) by demographic variable	
5.4 Association between perception of understanding and understanding of the content of IRs and demographic and other variables	
Demographic variable and perception	**Findings on understanding**
5.4.1 Education, occupations and employment status	
5.4.1.1 *Degree or no degree* Perception of understanding aligns broadly with the findings on understanding.	Respondents who had a degree had a better understanding of the content of the IRs than those who did not hold a degree.

5.4.1.2 ***Focal area of degree*** Perception of understanding aligns broadly with the findings on understanding.	Respondents who held a BCom (Accounting) degree or an equivalent degree had a better understanding of the content of the IRs than any of the respondents who held degrees with other focal areas.
5.4.1.3 ***Accounting major during tertiary education*** Perception of understanding aligns broadly with the findings on understanding.	Respondents with an Accounting major in their tertiary studies had a better understanding of the content of the IRs than those without an Accounting major in their tertiary studies.
5.4.1.4 ***Post-graduate degrees*** Perception of understanding aligns broadly with the findings on understanding.	Respondents who held an Honours degree or an equivalent as their highest qualification had a better understanding of the content of the IRs than respondents who held Master's and Doctoral degrees, possibly because the majority of them held an Honours degree or an equivalent in Accounting.
5.4.1.5 ***Professional qualifications*** Perception of understanding aligns broadly with findings on understanding.	Respondents with financially related professional qualifications had a better understanding of the content of the IRs than respondents with professional qualifications unrelated to finance.
5.4.1.6 ***Field of work experience*** Perception of understanding aligns broadly with findings on understanding.	Respondents who had work experience in financially related fields had a better understanding of the content of the IRs than respondents who did not work in financially related fields.
5.4.1.7 ***Employment status*** No association between perception of understanding and understanding.	Respondents who worked full-time had a better understanding of the content of the IRs than respondents who did not work full-time.
5.4.2 Number of shares held, Rand value of shareholding and overall portfolio size	
5.4.2.1 ***Number of shares held*** No association between perception of understanding and understanding.	There was no significant association between the understanding of the content of the IRs and the number of shares held by respondents.
5.4.2.2 ***Rand value of shares held*** Limited association between perception of understanding and understanding.	Respondents with share blocks in a Rand value range between R2 500 and R5 000 and above R500 000 had a better understanding of the content of the IRs than individual shareholders with share blocks in other Rand value ranges.

5.4.2.3 ***Number of companies in portfolio*** No association between perception of understanding and understanding.	There was no significant association between the understanding of the content of the IRs and the number of companies in which respondents held shares.
5.4.3 Investment objectives and decisions	
5.4.3.1 ***Investment objective*** Limited association between perception of understanding and understanding.	Respondents with long-term capital growth as their investment objective had a better understanding of the content of the IRs than respondents with other investment objectives.
5.4.3.2 ***Initiative when making investment decisions*** Perception of understanding aligns broadly with findings on understanding.	Respondents who made investment decisions on their own initiative had a better understanding of the content of the IRs than respondents who made these decisions with the help of financial advisors.
5.4.4 Understanding of individual components of the IR	
Respondents held the perception that they understood the narrative components of the IRs better than the non-narrative components. They perceived themselves to have the weakest understanding of the condensed statement of changes in equity.	Questions posed to respondents were limited in number because the maximum acceptable length of a postal questionnaire had to be observed. Furthermore different marks were awarded per question, as explained in Chapter 4. Consequently, a final conclusion on the understanding of the individual components of IRs per component could not be drawn, although a detailed analysis of responses is provided.

This concludes the investigation of the primary objective of the study. The sections below deal with the secondary objectives of the study on an individual basis.

5.6 HOW INVESTMENT DECISIONS ARE MADE BY INDIVIDUAL SHAREHOLDERS

The first of the secondary objectives (Category 1 – investment decision and use of IRs category) of this study was to establish how individual shareholders, in general, make investment decisions. Although the focus was not specifically limited to IRs, this part of the study provides context around the way investment decisions are made by South African investors at large. Question 11 of the questionnaire for individual shareholders was used to elicit information in this regard.

Question 11

How do you currently make investment decisions to buy, sell or hold shares in any Company?

The responses to the above question are summarized in Table 5.54, overleaf, and are addressed thereafter.

Table 5.48: Responses in respect of who takes the initiative for investment decisions (n = 1 071)

Taking investment decisions (V15)	Number of responses	% of responses
Own decision	659	61.53
Own decision, but financial advisor directly involved (consulted)	242	22.60
Financial advisor makes decision after consulting with shareholder	75	7.00
Financial advisor makes decisions	95	8.87

Of the respondents, 61.53% indicated that they made investment decisions entirely on their own initiative, while another 22.6% made investment decisions on their own initiative, but would consult with a financial advisor. A total of 84.13% of respondents therefore initiated their own investment decisions. By contrast, 7% of respondents allowed their financial advisors to make the final investment decision after consulting with them, while 8.87% allowed their financial advisors to make investment decisions entirely on their behalf – a total of 15.87% of respondents thus depended on their financial advisors to make investment decisions for them.

The perception of understanding of the content of the IR, as well as the understanding of the content of the IR for the two classes of investment decision-makers, have been considered in detail in Section 5.4.3.2, above. Amongst other conclusions in Section 5.4.3.2, it was indicated that investors who made decisions on their own initiative achieved a higher mean

(41.33%), as opposed to those who allowed their financial advisors to make investment decisions on their behalf (mean = 29.31%). Although this finding was not unexpected, the fact that investors who made their own decisions scored below 50% in the assessment of their understanding of IRs is disconcerting, since they appear to make investment decisions while using information that they do not understand fully.

5.7 SOURCES OF INFORMATION USED BY INDIVIDUAL SHAREHOLDERS WHEN MAKING INVESTMENT DECISIONS

The second secondary objective of this study (Category 1 – investment decision and use of IRs category) was to establish what sources of information shareholders consult before making investment decisions. Question 12 of the questionnaire for individual shareholders was used to collect information in this regard, and the discussion distinguishes between sources of information suggested in the questionnaire and new sources of information that respondents proposed in the last part of the question.

5.7.1 Analysis in respect of suggested sources of information

Question 12.
In general, how often do you consult the following sources of information when making an investment decision to buy, sell or hold shares in any company?

The responses to the above question (excluding the "new" or "other" sources of information proposed by respondents, as dealt with in Section 5.7.2) are contained in Table 5.49, below.

Table 5.49: Responses related to specific sources of information

	Level of usage (%)		
Sources provided in the questionnaire	**Always/ Nearly always**	**Sometimes**	**Hardly ever/Never**
Financial press (newspaper & magazine articles) (n = 1027)	506 (49.3%)	380 (37.0%)	141 (13.7%)
Annual financial reports of company (n = 937)	253 (27.0%)	331 (35.3%)	353 (37.7%)

	Level of usage (%)		
Sources provided in the questionnaire	**Always/ Nearly always**	**Sometimes**	**Hardly ever/Never**
Financial investment programs on radio and TV (n = 952)	234 (24.6%)	425 (44.6%)	293 (30.8%)
IRs of company (n = 924)	190 (20.6%)	322 (34.8%)	412 (44.6%)
Officials of company (n = 891)	39 (4.4%)	129 (14.5%)	723 (81.1%)
Advice of friends and acquaintances (n = 903)	44 (4.9%)	311 (34.4%)	548 (60.7%)
Advice of colleagues (n = 885)	22 (2.5%)	245 (27.7%)	618 (69.8%)
The internet (n = 906)	185 (20.4%)	248 (27.4%)	473 (52.2%)
Notices from the JSE (n = 903)	119 (13.2%)	311 (34.4%)	473 (52.4%)
Seminars (n = 889)	33 (3.7%)	185 (20.8%)	671 (75.5%)

The most popular source of information used for investment decisions when considering the use thereof in nearly all instances (always/nearly always) appears to be the financial press (49.3% of respondents for that subsection of the question). The annual financial report was the second most popular source (used by 27% of respondents for that subsection of the question). Of the sources that are "Always/Nearly always" used by investors, the IR was the fourth most popular source of information (used by 20.6% of respondents for that subsection of the question). In the case of the advice of colleagues, very few respondents indicated that they "Always/Nearly always" used this source (it was used by only 2.5% of respondents).

According to the feedback from respondents who indicated that they used the specific source of information "Always/Nearly always" and "Sometimes" when making investment decisions, the financial press was the most popular source of information. Furthermore, the most widely used four sources of information when combining the "Always/Nearly always" and "Sometimes" categories were the same as those found when looking merely at

"Always/Nearly always". However, the use of annual financial statements and financial investment programmes on radio and television traded places when both levels of usage were employed to assess popularity, while the financial press remained the most popular source of information used for investment decisions.

When the sources of information are considered in respect of the individual shareholders that make investment decisions on their own initiative, the popularity of the first four sources of information remained in the same sequence as that given in Table 5.49 above.

5.7.2 Analysis of the last subsection of Question 12 where respondents were invited to supply their own "Other" sources of information

The last subsection (V26) of Question 12 requested respondents to indicate whether they used "Other" sources of information when making investment decisions. In response, 100 respondents indicated that they did. More specifically, these respondents indicated that they "Always/Nearly always" (64 responses) or "Sometimes" (36 responses) used "Other" sources of information, but only 92 of these respondents provided the "Other" source.

Contrary to expectation, the second part of this subsection (V27), which requested respondents to specify what these "Other" sources were, elicited 120 responses. This meant that 20 respondents did not read the question with care and provided "Other" sources of information even though they did not initially indicate that they used "Other" sources of information. To ensure that potentially valuable information was not discarded, both sets of responses were analysed. The findings are considered below.

Table 5.50: "Other" sources of information specified by responses of respondents

"Other" sources of information specified	Frequency (120)	Frequency (92)
Financial advisor, analyst or broker	41	29
Radio and TV	4	4
Publications	8	8
Family advice	7	5
Computer programs	11	7
Own view of investment possibilities	24	19
Reports	21	17
Share price movements	4	3
Total	120	92

Table 5.50 shows that 41 out of 120 and 29 out of 92 respondents respectively indicated that they use financial advisors in the question designed to ascertain what sources of information respondents would generally use over and above those referred to in Question 11. Furthermore, 19 out of 120 and 17 out of 92 respondents respectively indicated that they used radio and television, various publications and family advice as “Other” sources of information. These “Other” sources of information were identical to the specific information source categories listed in the subsections of Question 12, and reallocation was considered, but this was not done for fear of double-counting these items, due to the anonymous nature of the questionnaire. Only one half of the already small group of respondents who supplied “Other” sources of information provided new sources of information over and above those listed in Question 12, and therefore this analysis yielded little informational value. This may present another opportunity for future research.

5.8 IMPORTANCE OF IRS FOR MAKING INVESTMENT DECISIONS

To satisfy the third secondary objective, in which the study aims to determine whether IRs are considered to be important when making investment decisions (Category 1), the responses to Questions 12 (also used earlier under Section 5.7), 14, 15, 28 and 13 were considered and analysed.

Question 12.

In general, how often do you consult the following sources of information when making an investment decision to buy, sell or hold shares in any company?

	Always/Nearly always	**Sometimes**	**Hardly ever/Never**
Interim financial reports of the company involved (n = 924)	190 (20.6%)	322 (34.8%)	412 (44.6%)

For an examination of the results arising from the above question, see Table 5.49 in Section 5.7, above. In summary, the IR appears to be the fourth most popular source of information in making investment decisions, with a total of 55.4% of respondents’ using the IR “Always/Nearly always” (21%) or “Sometimes” (34%) for investment decision purposes. Nearly 45% of respondents never or hardly ever used the IR when making investment decisions.

Question 14

During the last 8+ years (since 2000), approximately how many times have you made use of the Interim Financial report in making investment decisions to buy, sell or hold shares in respect of any of your shareholdings?

Table 5.51: Number of times the IR was used for investment decisions since 2000

Number of times IR was used since 2000 (8 years +) (n = 993)	Frequency	Percentage	Cumulative frequency	Cumulative percentage
Nil – do not use	506	50.96#	506	50.96
Between 1 and 25 times during 8 years	316	31.82	822	82.78
Between 26 and 50 times during 8 years	26	2.62	848	85.40
Between 51 and 100 times during 8 years	7	0.70	855	86.10
Between 101 and 200 times during 8 years	8	0.81	863	86.91
Between 201 and 400 times during 8 years	3	0.30	866	87.21
More than 400 times during 8 years	1	0.10	867	87.31
Many times during 8 years	42	4.23	909	91.54
Always during 8 years	27	2.72	936	94.26
Hardly ever during 8 years	57	5.74 #	993	100.00

The above table gives an indication of how many times over the last eight or more years respondents used the IR to make investment decisions. Note that the information provided in the three rows at the bottom of the table represents respondents who did not give a specific indication of how many times they used the IR – they merely provided a descriptive answer which made it difficult to quantify. Nevertheless, if the number of respondents who never used the IR during the last eight or more years (marked #) were added to those who indicated that they hardly ever used the IR (also marked #), nearly 57% indicated that they virtually never use the IR for making investment decisions.

It is acknowledged that the number of companies in which respondents hold shares could also have had an impact on the number of times the IR was used for investment purposes. For instance, respondents holding shares in fifty different companies would, due to the volume of transactions they may be involved in, tend to use the IR more than a respondent who holds shares in only one company. It was not possible to isolate the impact of the number of companies held by respondents on the responses. Therefore the reported number of times the IR was used was taken at face value. If this study is replicated at a later stage, it is proposed that this question be reworded to take into account the fact that the number of companies in an individual shareholder's portfolio could have an impact on the number of times IRs are used to make investment decisions.

It is not feasible to make a direct comparison between the respondents who indicated that they never, or hardly ever, use the IR for investment decisions based on the frequencies in Question 14 marked with # (56.7%) and those who indicated that they never, or hardly ever, use the IR for investment decisions based on Question 12 (44.6%) as indicated in Section 5.7. However, it is clear that the IR is not a popular source of information when making investment decisions.

Question 15

Please indicate the extent in general of the relevance of the information contained in the interim financial report in respect of your making investment decisions to buy, sell or hold shares.

Table 5.52: Responses related to relevance of IRs for investment decisions

Relevance of IR for investment decisions (n = 1078)	Number of responses	% of responses
I find the information in the interim financial report relevant to making an investment decision to buy, sell or hold shares	450	41.74
I do not find the information in the interim financial report relevant to making an investment decision to buy, sell or hold shares	319	29.59
I actually do not understand the information in the interim financial report and therefore do not find it relevant	309	28.67

The above table gives an indication of whether respondents find the information in the IR relevant to making investment decisions to buy, sell or hold shares. It is interesting, but not surprising, that approximately 29% of respondents did not find the IRs relevant to investment decisions because they did not understand the information in the IR. The 41.74% who did understand the IR and found it relevant to decision-making is fairly close to the percentage of respondents who understood the content of the IR (35.57%), as determined in Section 5.3.2, in Table 5.15. The total percentage of respondents who did not find the IR relevant to making investment decisions is 58.26% and this percentage aligns fairly closely with the 56.7% mentioned just below Table 5.57, which indicated that they had not used the IR for investment decisions in the last eight or more years. This is also fairly closely aligned with the percentage of respondents who achieved a total percentage score of below 50% (see Section 5.3.2) in respect of their understanding of the IR.

Question 28

Would you consider the information contained in the Interim Financial Reports as adequate for you as a shareholder to make investment decisions?

In Table 5.53, below, the frequencies of the responses as to whether information contained in the IR is adequate to make investment decisions are reflected. These responses were analysed further, comparing respondents with an Accounting major at a tertiary level and those without such an Accounting major, because it was believed that this variable may have had an impact on the answers provided by the respondents.

Table 5.53: Frequencies indicating whether the content of the IR is considered adequate to make investment decisions by respondents holding an Accounting major or not

Adequate for making investment decisions or not (n = 1045)	Accounting major	Not accounting major	Total
Yes, adequate	172	394	566
	60.8%	51.7%	54.2%
No, not adequate	111	368	479
	39.2%	48.3%	45.8%

Of the respondents, 54.2% were of the opinion that the information contained in the IR would be adequate to make investment decisions. The balance of respondents (45.8%) were of the opinion that the information contained in the IR was not adequate as a basis for investment decisions. Further analysis was done to distinguish the differences between those respondents who had Accounting as a major in tertiary studies, as opposed to those that did not, to assess whether or not accounting knowledge had an impact on the perception of adequacy of IRs for investment decisions. This analysis indicated that nearly 61% of respondents with an Accounting major were of the opinion that the information was adequate for making investment decisions, while only approximately 52% without an Accounting major felt this to be the case.

Further clarification was sought on to how important respondents considered the individual components of the IR to be when making investment decisions – to this end, the responses to Question 13 were analysed.

Question 13

In general, how important to you are the following components of the Interim Financial Report when making a decision to buy, sell or hold shares in any company?

In order to rank the importance of the individual components of IRs, the respondents rated each individual component of the IR on a Likert scale anchored by 1= "very important", 2 = "fairly important", 3 = "not important" and 4 = "I do not use it". As explained in Section 4.8.1, the means of the variables (individual components of the IR) for the respondents were calculated to provide a "centre of gravity" of this scale to enable the ranking of the responses. Note that, using this ranking method, the lowest mean indicates the most important individual component of the IR, while the highest mean represents the least important individual component of the IR.

Table 5.54: Frequencies and means of the scale of importance of the individual components of the IR

Ranking	Importance of individual components of an Interim Financial Report V28 to V33)	Very important	Fairly important	Not important	I do not use it	Mean #
1	Commentary by management (n = 997)	337	293	113	254	2.28
2	A condensed income statement/ statement of comprehensive income (n = 992)	318	303	88	283	2.34
3	A condensed balance sheet / statement of financial position (n = 1008)	311	294	100	303	2.39
4	A condensed cash flow statement / statement of cash flows (n = 976)	239	278	132	327	2.56
5	Selected explanatory notes (n = 973)	190	333	160	290	2.57
6	A condensed statement of changes in equity (n = 961)	121	253	218	369	2.87

See explanation on "centre of gravity" just above Table 5.54.

Based on the outcome of the "centre of gravity" calculations, the commentary of management was considered to be the most important component of the IR for making investment decisions, the statement of comprehensive income was considered to be the second most important and the statement of changes in equity the least important. Note that the commentary of management was not tested for understanding in this study, due to the non-standardized nature or responses (see Section 5.4.4.1, above).

- ***Conclusion***

It seems clear from the analyses of Tables 5.51 and 5.52 that the majority of individual shareholders did not deem IRs to be important when making investment decisions.

Nevertheless 54.2% of respondents indicated in Table 5.53 that they felt that the information contained in IRs was adequate to make investment decisions, while the feeling was more prevalent among respondents who had Accounting as a major during their tertiary studies.

It appears as if individual shareholders consider the most important **individual** component of the IR when making investment decisions to be the commentary by management, followed by the condensed statement of comprehensive income. However, it appears that individual shareholders do not deem IRs to be of particular importance when they are making investment decisions.

5.9 CRUCIAL ADDITIONAL INFORMATION REQUIRED IN IRS

The next secondary objective of the study in Category 1 was to establish what crucial items are omitted from the IR that should be included to facilitate investment decisions. Question 29 was included in the questionnaire to collect the relevant information from the respondents.

Question 29

List one crucial item of additional information that is not presented in the Interim Financial Report at this stage that you would require to make investment decisions.

Tables 5.55 and 5.56, below, contain a summary of the responses collected.

Table 5.55: Summary of responses of one crucial additional item to be presented in the IR to facilitate making investment decisions

Initial analysis of responses (n = 1102)	Frequency	Percentage
Did not answer / said nothing more is required / sufficient information is provided / don't know what to ask for	674	61.17
Indicated that additional information is required	428	38.83
Total respondents	1102	100.00

According to the initial analysis of the data, 61% of respondents either did not answer the question, indicated that nothing more was required, mentioned that the information in the IR was sufficient to make investment decisions, or did not know what to ask for. For the purposes of this study, these respondents were all deemed to be satisfied with the current information contained in the IR, although their responses could also be attributed to a lack of understanding of the content of the IR. By contrast, 39% indicated that they could identify one crucial item of additional information in the IR that would facilitate their investment decisions – these responses are listed below.

Table 5.56: Summary of responses of one crucial additional item to be presented in the IR to facilitate making investment decisions

Detail list of frequencies of additional information (n = 428)	Frequency	Percentage
More commentary is required	11	2.6
More forward-looking information is required ***(discussed below)***	**115**	**26.9**
Forward looking reports from chairman/CEO, including risk statements	6	1.4
Requests for information to be explained in simpler terms	21	4.9
Item already provided in the IR, so of no consequence	6	1.4
Information on dividends and/or proposed dividends	22	5.1
Information on share price of the company during the interim period ***(discussed below)***	**45**	**10.5**
Sundry (free cash flow, is it a good investment, inflation, liquidity, number of employees, intrinsic share value, stockbrokers' comments, management's ability to run the company, has the company been approached by a BE consortium, info on market share etc.) ***(discussed below)***	**60**	**14.0**
Ratios, trends graphically depicted	13	3.1
Don't use the IR	11	2.6
Segment reports including geographical segmentation	10	2.3
Performance of the company relative to the sector and peers	8	1.9
Audit report/review report	7	1.6
Economic forecast related to specific market and industry	7	1.6
Details on directors' emoluments and share dealings ***(discussed below)***	**42**	**9.8**
Statement of comprehensive income details, such as stock shrinkage, bad debt, movements on provisions, investment income	10	2.3

Detail list of frequencies of additional information (n = 428)	Frequency	Percentage
Price-earnings Ratio of the company	15	3.5
Important line-items for the past 5 years	11	2.6
Detailed use of assets	8	1.9
	428	100

The detailed analysis of the response of the 428 (39%) respondents who indicated that they would require additional information in the IR to facilitate their investment decisions revealed the following:

- 26.9% of these respondents indicated that they required more forward-looking information;
- 10.5% indicated that they required more information on movements of the company's share price;
- 9.8% indicated that they required more information on the emoluments and share dealings of directors of the company during the interim period; and
- 14.0% had sundry other proposals that individually did not exceed two to four similar responses and no specific items could be isolated from this.

Only forward-looking information and details on directors' emoluments and share dealings are difficult to access from sources other than the IR, and it may therefore be worthwhile to provide this information in IRs. However, information on share prices at an interim date, as well as movements in share price represent information that is readily available on the internet, in the daily newspapers, as well as in JSE reports. If these are provided in the IR, it would at best be convenient for shareholders. It is also submitted that such comparisons may be rather dated by the time they reach the shareholders in the mail – which still appears to be the preferred medium of communication, as indicated in Section 5.12, below.

5.10 SEQUENCE OF PRESENTATION OF THE INDIVIDUAL COMPONENTS OF THE IR

Another secondary objective of the study (the fifth secondary objective, and the first in Category 2 on matters directly associated with IRs) was to determine in what sequence users of the IR would prefer the individual components of the IR to be presented.

Given that the study focuses on the use of the IR for making investment decisions, it was considered possible that respondents using IRs to make investment decisions may have a different preferred sequence in respect of the individual components of the IR than that proposed in IAS 34.8. This expectation was supported by the results of the survey in respect of the importance[63] and extent of thoroughness of reading[64] attached to the individual components of the IR. To investigate this matter, Question 30 was used.

Question 30

Please indicate the sequence in which you would prefer the components of the Interim Financial Report to be presented. (Enter a "1" for the component you would prefer to be "First" and a "6" for the component you would prefer to be "Sixth". Do not repeat a number between 1 and 6).

A summary of the responses to Question 30 is presented in Table 5.57, below.

Table 5.57: Frequencies of responses in respect of the sequence of the individual components contained in the IR

Individual components of an Interim Financial Report (V71 - V76)	**Sequence preferred**					
	1st	**2nd**	**3rd**	**4th**	**5th**	**6th**
A. Condensed balance sheet/ statement of financial position (n = 925) (V71)	**282** **1**	272	186	95	47	43
B. Condensed income statement/ statement of comprehensive income (n = 912) (V72)	260	**344** **1**	157	81	60	10
C. Condensed statement of changes in equity (n = 907) (V73)	10	51	**220** **1**	**294** **1**	174	158
D. Condensed cash flow statement/ statement of cash flows (n = 914) (V74)	55	89	**257** **1**	**316** **1**	136	61
E. Selected explanatory notes (n = 923) (V75)	40	124	51	75	**392** **1**	241
F. Commentary by management (n = 936) (V76)	305	40	43	48	98	**402** **1**
Preferred position in sequence of individual component of the IR	A	B	C/D	C/D	E	F

[63] See Section 5.8, in particular Table 5.54, above.
[64] See Section 5.11, Table 5.58, below.

The above frequency table shows the preference of respondents for each of the individual components of the IR in the respective rows – the most popular position in the sequence in a row is marked by "1". In the bottom row of the frequency table, the most popular position per row is indicated and this finally provides the preferred sequence of the individual components of the IR in total, according to responses.

From the above frequency table, it would appear as if the majority of respondents prefer the individual components of the IR to be presented in the exact sequence contained in Paragraph 8 of IAS 34, although there is some ambivalence on the position of the statement of changes in equity and the statement of cash flows. It is conceded that the fact that respondents may be used to the customary sequence in which the individual components of the IR are presented may have influenced their answers.

5.11 RESPONDENTS' READING OF COMPONENTS OF THE IR

The sixth secondary objective of the study (Category 2) aimed to establish how thoroughly the IR is read and what would dissuade respondents from reading the IR thoroughly. Note that readability is not addressed here, but rather how thoroughly respondents choose to read the individual components of IRs. To achieve this objective, Questions 19 and 20 were included in the questionnaire.

5.11.1 Extent of thoroughness of reading of components of the IR

Question 19
To what extent do you read the following components of the Interim Financial Report?

The "centre of gravity" technique used in Section 5.8 and in Table 5.54 was also used here to rank the responses on the thoroughness of reading of the IR, anchored by the 3-point Likert scale of 1 = "thoroughly", 2 = "not thoroughly" and 3 = "I do not read it at all". Note that using this ranking method, the lowest mean indicates the highest extent of thoroughness of reading, while the highest mean indicates the opposite.

Table 5.58: Frequencies and means of the scale of extent of thoroughness of reading of the components of the IR

Ranking	Extent of reading of individual components of an Interim Financial Report (V39 to V44)	Thoroughly	Not thoroughly	I do read it at all	Mean #
1	Commentary by management (n = 1037)	459	344	234	1.78
2	A condensed income statement/ statement of comprehensive income (n = 1022)	359	394	269	1.91
	A condensed balance sheet/ statement of financial position (n = 1035)	276	453	306	2.03
4	Selected explanatory notes (n = 1014)	244	463	307	2.06
5	A condensed cash flow statement/ statement of cash flows (n = 1013)	252	390	371	2.12
6	A condensed statement of changes in equity (n = 1007)	104	419	484	2.38

\# See explanation on "centre of gravity" just above Table 5.58.

In line with the fact that commentary by management is deemed to be the most important component of the IR,[65] commentary by management is also the individual component of the IR that respondents read most thoroughly. The second most thoroughly read component is the condensed statement of comprehensive income, while the statement of changes in equity appears to be the least thoroughly read of the IR components. The ranking determined in this instance is virtually identical to that determined in Section 5.8, where the importance of the individual components of the IR was assessed.

5.11.2 Factors dissuading respondents from reading the IR thoroughly

Question 20
Which of the following "factors" would dissuade you from reading the Interim Financial Report thoroughly?

[65] See Table 5.54, above.

In this instance the objective of the study was to determine which factors would lead to respondents not reading the IR thoroughly. Table 5.59, below, ranks each individual component of the IR in terms of what percentage of respondents would not read the IR thoroughly because of the specific factor mentioned in the questionnaire.

Table 5.59: Frequencies of factors that would dissuade respondents from reading the individual components of the IR thoroughly

Factors that would dissuade you from reading IR thoroughly (V45 to V50)	**I don't understand it**	**I do not have the time**	**I am not interested**	**It is not important**	**Printing is too small**
A condensed balance sheet/ statement of financial position (n = 979) (V45)	239 25%	332 34%	186 19%	72 7%	150 15%
A condensed income statement/ statement of comprehensive income (n = 941) (V46)	221 24%	334 36%	164 17%	57 6%	165 17%
A condensed statement of changes in equity (n = 969) (V47)	228 24%	271 28%	234 24%	125 13%	111 11%
A condensed cash flow statement/ statement of cash flows (n = 944) (V48)	218 23%	304 32%	204 22%	73 8%	145 15%
Selected explanatory notes (n = 925) (V49)	137 15%	319 35%	201 22%	88 9%	180 19%
Commentary by management (n = 921) (V50)	131 14%	342 37%	163 18%	97 11%	188 20%

Respondents who were dissuaded from reading the IR thoroughly because they chose "I don't understand it" ranged between 23% and 25% for the condensed statements of financial position, comprehensive income, changes in equity and cash flow (collectively referred to as "the condensed financial statements"). Interestingly, the percentage of respondents dissuaded from reading the "Selected explanatory notes" and "Commentary by management" thoroughly because they not feel that they understand these components of the IR was in a much lower range, between 14% and 15% than the percentage range associated with formal condensed financial statements. This phenomenon can probably be attributed to the fact that the explanatory notes and commentary by management would be easier to understand, since these are provided in narrative format, and therefore do not require the same amount of technical accounting knowledge and interpretation as the individual components which constitute the condensed financial statements.

Of the five possible factors dissuading respondents to read the IR thoroughly, the highest percentage of respondents indicated that they would not read each one of the individual components of the IR (and consequently the IR as a whole) thoroughly, because they did not have time to do so. Obviously, this matter is beyond the control of both the issuers of IRs and the standard setters, and it is difficult to take steps to mitigate the impact of this factor. Note that the percentages associated with this reason for not reading the individual components of the IR are the highest for "Selected explanatory notes" and "Commentary by management". If related to the level of understanding of these two IR components, it appears that despite the respondents' apparently understanding these components better, these details are probably more time-consuming to read because they are generally not condensed to the same extent as the components comprising the four condensed financial statements contained in the IR.

For five out of six components, 22% or fewer respondents indicated that the factor that would dissuade them from reading the IR was the fact that they were not interested in the individual components of the IR. Interestingly, in the case of the statement of changes in equity, the highest percentage (24%) of respondents was of the opinion that they were not particularly interested and would therefore not read the statement.

For five out of six components, the smallest number of respondents was dissuaded from reading the individual components of the interim report thoroughly because they perceived these components not to be important – put differently, most respondents appeared to consider the components important. The one exception to this phenomenon was the condensed statement of changes in equity, which appeared to be considered less important than the other components. Also see Table 5.54 for confirmation of the fact that the condensed statement of changes in equity is considered to be the least important individual component of an IR.

The largest percentage of respondents felt that they would be dissuaded from reading the selected explanatory notes and commentary by management thoroughly if these were printed in too small a letter type. This can probably be attributed to the fact that those components are presented in narrative format, and excessively small printing would make reading the details difficult.

5.12 PREFERRED MEDIUM OF COMMUNICATION IN THE CASE OF IRS

Given the anecdotal perception that the medium of communication over the last number of years has developed from being paper-based to being largely electronic, it was considered that the study could assist in determining through which mode of communication respondents would prefer to receive their IR. Question 31 was formulated to achieve this objective.

Question 31
How would you prefer to receive the Interim Financial Report?

The summary of responses to Question 31 is set out below.

Table 5.60: Responses to medium of communication in respect of the IR and respondents' age (n = 924)

Age group / Medium of communication	**18 <= 29 years**	**>29 <=40 years**	**>40<=65 years**	**<65>=80 years**	**>80 years**	**Total %**
Post	18	33	229	216	46	542 (58.7)
E-mail	15	53	215	54	2	339 (36.7)
Post + e-mail	0	0	2	2	0	4 (0.4)
Internet + e-mail	0	1	9	0	0	10 (1.1)
Other mediums	0	0	3	2	0	5 (0.5)
IR not required	0	2	11	8	3	24 (2.6)

Age group / Medium of communication	18 <= 29 years	>29 <=40 years	>40<=65 years	<65>=80 years	>80 years	Total %
	33 (3.6)	89 (9.6)	469 (50.8)	282 (30.5)	51 (5.5)	924 (100)

From the above cross-tabulation between age and medium of communication, it is evident that the majority of respondents (58.7%) still prefer to receive the IR by post. By contrast, 36.7% of respondents prefer to receive it solely by e-mail. The remainder or respondents indicated a diverse range of preferences, none of which appeared to be material in context.

It was anticipated that the popularity of receiving the IR by post would wane in the era of electronic communication, so the age of correspondents (see Section 5.2.1 for age brackets) was introduced in the above table. The findings indicate that 54.6% of respondents in the age bracket 18≤29 years (n = 33), 37.1% in the age bracket >29 to 40 years (n = 89), 48.8% of respondents in the age bracket >40 to 65 years (n = 469), 76.6% in the age bracket >65 to 80 years (n = 282) and 90.2% in the age bracket of above 80 years (n = 51) preferred to receive the IR by post.

The fact that only 54.5% of the youngest age bracket (a very small group, numerically) wanted to receive the IR by post was unexpected and no conclusion could be drawn from this statistic, but the steady upward trend regarding a preference to receive the IR by post as age increases beyond 40 years of age is not surprising, since one would expect the technological skills of older respondents to be less advanced than those of younger respondents.

5.13 SUMMARY OF FINDINGS ON SECONDARY OBJECTIVES OF THE STUDY

In this section, a summary is presented of the most important findings of the investigation into individual shareholders' understanding of IRs in line with the secondary research objectives identified as part of this study.

Table 5.61: Summary of findings associated with secondary research objectives

Secondary research objectives – Category 1 on investment decisions and use of IRs
5.6 Determine how investment decisions are made by individual shareholders
The majority (61.53%) of respondents made their own investment decisions without the involvement of a financial advisor, while 8.87% of respondents left investment decisions entirely up to their financial advisor.
5.7 Sources of information used by individual shareholders when making investment decisions
The financial press, by a wide margin, appears to be the most popular source of information used by individual shareholders to make investment decisions. Of the individual shareholders 45% hardly ever used information contained in IRs when making investment decisions.
5.8 Importance of IRs when making investment decisions
Over 57% of respondents indicated that over the last eight years, they never used IRs to make investment decisions, while slightly more than 58% of respondents did not find the information relevant to investment decisions. Of the individual components of IRs, respondents perceived the commentary by management to be the most important individual component of IRs in making investment decisions. One could therefore conclude that IRs are not considered to be particularly important when individual shareholders make investment decisions.
5.9 Crucial additional information required in IRs
The majority of respondents (61%) indicated that they required no additional information in IRs to make investment decisions. Nearly 27% of the 39% of respondents who indicated that they did require additional information in IRs requested more forward-looking information. The frequencies of all other requests for additional information were negligible, compared to the total number of respondents.

Secondary research objectives – Category 2 on other matters
5.10 Sequence of presentation of the individual components of IRs
The majority of respondents appeared to prefer the sequence of individual components of IRs proposed in IAS 34.8. There is some ambivalence around the positions of the condensed statement of changes in equity and the condensed cash flow statement.
5.11 Respondents' reading of the components of the IR
Respondents appeared to read the commentary by management most thoroughly of all the IR components. The majority of respondents indicated that they were dissuaded from reading the components of IRs thoroughly by a lack of time to do so.
5.12 Preferred medium of communication in the case of IRs
The most popular medium by which respondents would prefer to receive IRs was still by post (58.7%), although e-mail as medium of communication is the second most popular medium, at 36.7%. The age group of >29 to 40 years is most averse to receiving IRs by post, and the majority of this group would prefer to receive IRs by e-mail.

In Chapter 6, an overview of the study, conclusions and findings based on the empirical work in this chapter and recommendations, are provided.

CHAPTER 6: OVERVIEW, CONCLUSIONS AND RECOMMENDATIONS

6.1 INTRODUCTION

This chapter provides a brief overview of the study. Furthermore, the conclusions drawn in respect of the research objectives addressed in the empirical work in Chapter 5 and recommendations as to how to solve the problems identified are provided. Finally, recommendations for future research are made.

6.2 OVERVIEW OF THE STUDY

Recent studies, as summarised in Chapter 1 (ICAS & NZICA, 2011:4; IFAC, 2008:30,35; FRC, 2011:31; SEC, 2008b:3,16), indicate that the understandability of financial reports may have been compromised over the last number of years due to the proliferation of accounting pronouncements, the increased complexity of disclosure requirements, the larger number of disclosure requirements and the resulting increases in the length of ARs.

The perceived reduction in how well ARs are understood raised the question of whether individual shareholders of South African listed companies understood the information provided to them in published GPFRs, including both ARs and IRs. Since several of the studies mentioned above indicate that users of financial statements would prefer shorter and more concise financial reports, and that these would presumably be more understandable, the study focuses on IRs rather than ARs to answer this question. This decision was strengthened by the fact that integrated reports are now required, in terms of the JSE Listings Requirements for all South African listed companies and that the condensed format of IRs is seen to be the appropriate format in which to present the traditional financial information in integrated reports (Ernst & Young, 2012a). The use of the format of IRs in integrated reports led to a raised profile of IRs in South Africa and consequently also to the question whether stakeholders understand the content of IRs.

International research has confirmed that IRs are useful to individual shareholders. Extensive research has been conducted on the relevance and reliability of IRs,[66] but not on the understandability and comparability of IRs. Consequently, it was decided to investigate in this study, by means of a postal questionnaire (see Chapter 4), whether individual shareholders understood the context and content of IRs published by South African listed retail companies. The fact that IRs in South Africa tend to consist of condensed financial statements due to time and cost constraints, coupled with the other reasons mentioned earlier in this chapter, made these financial statements eminently suitable to assess to what extent shareholders comprehend basic accounting principles contained in such reports. Furthermore, the format of IRs, and the relevant JSE Listings Requirements have been stable for a number of years, and IAS 34 has been in issue for more than a decade.[67] These stabilizing factors negated the possible impact that changes in content and lengthier financial statements would have had on the understanding of individual shareholders of financial statements. A further rationale for this decision was that no investigation as to whether individual shareholders understand the context and content of IRs has been published in South Africa, a developing country, to date, and this was seen as an opportunity to assess this issue.

The secondary objectives of the study were related to how individual shareholders make investment decisions. The study also addresses whether they use IRs for investment decisions, as well as other matters related to IRs.

As indicated in Chapter 2, the two pilot studies and a final study by Lee and Tweedie dating to the late 1970s on whether individual shareholders understand financial information were some of the small number of survey-based studies conducted to establish whether individual shareholders understand financial information. These studies, using postal questionnaires in the pilot studies by Lee and Tweedie (1975:4, 1976:304) and interview questionnaires when conducting personal interviews in a final study on individual shareholders by Lee and Tweedie (1977:12), were used as a basis in the design of this study to assess whether individual shareholders understand the context and content of IRs. As more than 30 years have passed since these prior studies were completed, changes were necessary to align the questionnaire used with developments in the accounting field since then, as well as the fact that this South African study focused on IRs rather than on ARs.

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[66] See Section 1.3.
[67] See Section 1.4.2.

It must be reiterated that although this study on IRs was based on the studies of Lee and Tweedie (1975, 1976, 1977), it focused on IRs rather than ARs, and could therefore not be seen as a replication or partial replication of the Lee and Tweedie's studies, as was the UK study done in 1994/1995 by Bartlett and Chandler (1997:250). It is therefore unlikely that the findings of this study could be compared with those of Lee and Tweedie (1975, 1976, 1977), or Bartlett and Chandler (1997). However, where appropriate, comparisons were made.

The primary and secondary research objectives investigated in the study were the following:

- **Primary research objective**

  As indicated in Section 1.5.1, the **primary research objective** of the study was to determine whether individual shareholders (respondents) understood the context and content of the IRs of South African listed retail companies. As part of this investigation, the perception of understanding of the individual shareholders of the IRs was also considered.

- **Secondary research objectives**

  The **secondary research objectives** of this study that were related to decision-usefulness can be divided into two categories:

  - **Category 1 - Investigating investment decisions and the use of IRs for investment decisions in general to establish**
    - how individual shareholders currently make investment decisions (on their own initiative or via financial advisors);
    - what sources of information individual shareholders are using when making investment decisions;
    - whether individual shareholders deem IRs important for making investment decisions; and
    - what other crucial information, that is not provided currently, individual shareholders would prefer to see in IRs to facilitate investment decisions.

- **Category 2 – Investigating other matters directly related to IRs to establish**
  - in what sequence individual shareholders would prefer the components of the IR to be presented;
  - whether the IR is read by individual shareholders and to what extent; and
  - in what medium of communication individual shareholders would prefer to receive IRs.

The final outcomes of the investigation, after statistical analysis of the empirical data, are presented below.

6.3 CONCLUSIONS ON RESEARCH OBJECTIVES AND RELATED RECOMMENDATIONS

The primary and secondary research objectives of the study and associated findings and recommendations are addressed individually.

6.3.1 Primary research objective: assessing the understanding of individual shareholders in listed retail companies of the context and content of IRs

6.3.1.1 Understanding the context of IRs

6.3.1.1.1 Background and conclusions/findings

It was clear from the results and discussion in Section 5.3.2 that individual shareholders have a better understanding of the context (with whom the legal responsibility of issuing IRs lie, whether IRs are audited and what the objective of issuing IRs is) of IRs than of the content of IRs. An analysis of the individual questions assessing the context of IRs in Section 5.3.3 rendered the following results:

- The majority of respondents did not know that the board of directors of a company is legally responsible for the IRs of a company, as only 44.3% of respondents provided the correct answer and 56.7% provided an incorrect answer (see Table 5.17). As anticipated, respondents with an accounting-related background performed better when answering this question, with 63.1% of them providing the correct answer.
- The vast majority (86.48%) of respondents correctly indicated that IRs are not subject to audit (see Table 5.18), but individual shareholders of the one company that did not

specifically state that its IR was not audited performed slightly worse than those of the other two companies (see Table 5. 19).

- A substantial majority (82%) of respondents indicated correctly what the most important objective of IRs is to provide individual shareholders with a progress report of the financial affairs of a company after the first six months of a financial year (see Table 5.20). As expected, respondents who majored in Accounting at tertiary level had a better grasp of what the most important objective of IRs is, with 90.8% of them answering this question correctly.

6.3.1.1.2 Recommendations arising from the assessment of understanding of the context of IRs

It is recommended that steps be taken to assist in further clarifying the above three important contextual issues in respect of IRs. It is proposed that this should be done either through amendments to IAS 34 or to the Listings Requirements of the JSE, if amendments to IAS 34 are not feasible. The proposals are considered in the sequence of the results listed under 6.3.1.1.1.

- This specific contextual issue (legal responsibility for IRs) appeared problematic, since only around 45% of respondents provided the correct answer. In the section of IRs where delegated members of the board provide their signatures, a clear statement should be made that the board of directors is legally responsible for IRs. This could be achieved by changing the generic statements: "By order of the board" or "For and on behalf of the board" in IRs, to the following:

> "By order of the board which is legally responsible for the interim financial statements of the company… " or "For and on behalf of the board which is legally responsible for the interim financial statements of the company… ".

The JSE Listings Requirements would probably be the most appropriate medium for guidance on this matter, since it deals with matters related to South Africa in particular.

- Although it does not appear to be a major problem, since the majority of respondents provided the correct answer in respect of the audit status of IRs, it seems as if the meaning of the term "reviewed" may not be as clearly understood as the phrase "not audited" or the word "unaudited". This is despite the fact that "reviewed" is a much-used technical term in the financial world and that it was stated in the body of the one reviewed IR that it was reviewed and not audited. Consequently, it is proposed that the heading of IRs containing a reference to the length of the interim period should, if the results for the interim period have been reviewed, also include a reference to the fact that the financial statements are not audited. This could be done by changing the heading to include the words "but not audited" where it is stated that the results presented in an IR are reviewed. An example of a proposed revised heading subsequent to implementing the proposal would be

"Reviewed, **but not audited,** [my emphasis] results for the six months ended…. ".

Again the JSE Listings Requirements appear to be the appropriate place to provide guidance on this matter. Although the impact on the understanding of context would affect only a small percentage of individual shareholders, it is believed that the change required is so minor that it would be worthwhile doing it for the small number of shareholders who would benefit.

- Most respondents appeared to be aware of the objective of IRs, since the majority of respondents appeared to know that the main objective of presenting IRs was to provide a progress report on the financial performance and position of a company at the end of the first interim period. Nevertheless, a statement to this effect would clarify the matter beyond doubt. This statement could be placed in several positions in an IR. It is proposed that such a statement be included at the beginning of the commentary by management, since the empirical results set out in Table 5.54 and Table 5.58 respectively, indicate that respondents consider this component of the IR important and read it diligently. Such a prominent position in this section of the IR would ensure that most shareholders would take note of this statement.

  An amendment to the disclosure requirements contained in IAS 34 may be the appropriate vehicle to address this issue.

6.3.1.2 Understanding the content of IRs

6.3.1.2.1 Background and conclusions/findings

The question of whether respondents (individual shareholders) understand the content of IRs was addressed in Section 5.3.2, in Table 5.15, and elaborated on in Section 5.4, where the different demographic variables and understanding of the content of IRs were provided. While it was possible to assess respondents' general understanding of the content of the IR as a whole, it was not possible to assess the understanding of each individual component of the IR and the non-financial information contained in the IR. This limitation of the study[68] primarily arose from the small number of questions devoted to individual components of IRs in order to limit the length of the postal questionnaire and in so doing, improve the response rate (see Section 5.4.4 for a detailed exposition).

- **Conclusion/Finding 1**

  The mean (see bottom part of Table 5.15) of the total percentage score reflecting understanding in respect of the content of IRs is 38.67%, whilst a total percentage score of 50% is deemed to reflect an adequate understanding of the context and content or content only of IRs for purposes of this study.[69] This low mean of total percentage score in respect of content only, even when considered in isolation, gives a clear indication that shareholders do not have a good understanding of the content of IRs. If this finding is analysed further, it becomes even more evident that the level of comprehension of shareholders is not adequate, as a total of 60.62% of respondents achieved a total percentage score of below 50%, whilst 39.38% achieved 50% and above.

- **Conclusion/Finding 2**

  Other interesting findings on understanding based on the percentage scores for IRs as a whole and linked to demographic variables can be summarized as follows:

  - Respondents who held a degree appeared to have a better understanding (mean = 44.8%) of the content of IRs than respondents who did not hold a degree (see Table 5.22). In particular, holders of commerce degrees specializing in Accounting appeared to have the highest mean (74.1%) (see Table 5.24).
  - Respondents who majored in Accounting appeared to have a relatively good understanding (mean = 61.7%) of the content of IRs (see Table 5.26).
  - Respondents holding an Honours degree or an equivalent as their highest qualification appeared to have a relatively good understanding (mean = 57.5%) of the content of IRs (see Table 5.28). This comment should be judged against a background of 56% of

[68] See Section 1.6.
[69] See Sections 1.8, 4.2.4 and 5.3.1.

individual shareholders holding an Honours degree or an equivalent as their highest qualification, having specialized in Accounting Sciences. The focal area of the degree thus appears to have had an impact on the mean of Honours graduates. Respondents in financially related professions (mean = 67.6%) and with work experience in the accounting/investment/banking and financial fields (mean = 56.6%) appeared to have a better understanding of the content of IRs than respondents in other professions and fields of work experience (see Tables 5.30 and 5.32).

- The number of shares held by respondents as well as the number of companies held by them in their portfolios did not have an impact on levels of understanding of the content of IRs (see Tables 5.36 and 5.40).
- The Rand value of shares (irrespective of number of shares) has some impact on levels of understanding, but levels of understanding still remained low (see Table 5.38).
- The investment objective of respondents and whether investment decisions are made by the respondents themselves or their financial advisors did have an impact on the respondents' level of understanding (see Tables 5.42 and 5.44). Individual shareholders who made their own investment decisions achieved a mean of 41.3%, while those who depended on financial advisors achieved a mean of 29.3%. These means differed significantly from each other.

- **Conclusion/Finding 3**

From the summary of responses under **Conclusion/Finding 2, above**, it can be concluded that respondents did not appear to understand the content of IRs, based on the measurement benchmark used in this study (with the exception of respondents who majored in Accounting during their tertiary studies, respondents whose focal area in their undergraduate degrees was Accounting, respondents holding an Honours degree or equivalent as their highest degree where the degree was a BCom(Hons) (Accounting Sciences) or an equivalent, respondents who had professional qualifications and work experience in accounting/investing/banking). Interestingly all these demographic groups achieved average total percentage scores (means) of above 55%, indicating that they understood the content of IRs if related to the assumed benchmark of understanding.

The above findings lend support to the approach used by the IASB in both its frameworks (as well as in several other conceptual frameworks) when preparing International

Financial Reporting Standards,[70] namely that users of financial statements should have a reasonable knowledge of business and accounting and should be prepared to study (and actually study) financial statements with diligence. It is also in line with the findings of Stevens *et al.* (1992:372,373), who state that readers would understand topics they are familiar with better than unfamiliar topics. Consequently respondents with exposure to accounting and business could be expected to understand the content of IRs better than those with no such exposure. However, it does not solve the problem of individual shareholders who do not have a reasonable knowledge of accounting and business, but still choose to make their own investment decisions.

6.3.1.2.2 Recommendations resulting from the assessment of understanding of the content of IRs

- ***Measures that could improve the overall understanding of the content of IRs***

To facilitate an improvement in the understanding of the content of IRs, the following three proposals are offered:

- IRs should contain a short glossary of terms that explain the meaning of the main line-items in IRs, as well as jargon used in the management commentary in layman's terms. This should improve the understanding of the individual components of the IRs. Although the assessment of understanding of individual components of IRs[71] could not be used to draw conclusions at the level of understanding of the components of IRs in isolation, this analysis could be used to identify an example of knowledge gaps of individual shareholders. For instance, individual shareholders did not understand the term "lower of cost and net realizable value" related to the valuation base of inventories. Other examples include the meanings or definitions of "current assets", "non-current assets' and "headline earnings", to name but a few. Although this proposal would facilitate an improvement in the understanding of IRs, it has the inherent disadvantage that it would increase the length of IRs, whereas this should be balanced with the calls to make GPFRs more concise.[72] This proposal is within control of the preparers of financial statements and regulators – guidance in this regard could come from either IAS 34 or the JSE Listings Requirements.

[70] See Sections 2.5 and 2.7.
[71] See Section 5.4.4.
[72] See Section 1.2.

- The *caveat*[73] on understandability introduced in the 1989 IASB and 2010 IASB/FASB Frameworks indicates that users should have a reasonable knowledge of financial matters and should be prepared to study (and actually study) the financial information with diligence. To assist users in obtaining a reasonable knowledge of financial matters contained in IRs, it is proposed that focused financial literacy training be offered to the public. The training could be offered through the professional accounting bodies in South Africa (SAICA, SAIPA and others) to improve the general level of understanding of shareholders. It should also be borne in mind that the apparent discrepancy between the perception of understanding of IRs and the understanding of IRs by individual shareholders who make their own investment decisions, as elucidated in Section 5.4.3.2, creates a risk for such shareholders that could be mitigated by encouraging them rather to use financial advisors when making investment decisions, or to change to collective investment schemes such as unit trusts or index-related products such as Satrix 40 until their understanding of IRs has improved.
- Although a further simplification of information contained in IRs may be considered, this could be difficult to achieve, given that IAS 34 already allows the option for financial statements in IRs to be presented in a condensed format. Greater simplification of complex financial matters may lead to a loss of informational value, which would be counterproductive. It may, however, be wise to consider removing the option of providing a complete set of financial statements as part of IRs (IASB, 2011a:§9), as this has the potential to further reduce the understanding of IRs by individual shareholders.

6.3.2 Secondary research objectives

In addition to the primary research objective addressed in Section 6.3.1, several secondary research objectives were identified. These were related to the investment decisions based on IRs by individual shareholders in general and broader aspects related to IRs in particular. The secondary objectives were divided into two categories as explained in Section 6.2. The first category focused on investment decisions and the use of IRs for investment decisions in general, while the second category dealt with other matters related to IRs in particular.

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[73] See Section 2.7.

6.3.2.1 Category 1: Investment decisions of individual shareholders (by own initiative or by brokers/financial advisors)

6.3.2.1.1 Background

From the results of the survey as summarized in Section 5.6, 84.13% of individual shareholders made investment decisions[74] on their own initiative. The high percentage of individual shareholders relying on their own initiative when making investment decisions is in line with the results of the research by Lee and Tweedie (1977:20), who found that 77% of respondents made their own investment decisions without help or advice from financial advisors or after consulting with their financial advisors. In the case of Bartlett and Chandler (1997:251), the percentage of respondents who made investment decisions on their own initiative or with some advice from financial advisors was, at 84%, a percentage similar to that of the respondents to this South African survey.

6.3.2.1.2 Conclusion

The basis of this decision-making phenomenon could be attributed to a number of factors, one of which may be that the majority of share investors in the retail sector appeared to be graduates[75] and of these graduates nearly 38% held commerce degrees.[76] Their graduate status and focus during their studies may have given them the confidence to make their own investment decisions, rather than rely on a financial advisor. The high number of individual shareholders making their own investment decisions was corroborated by the higher perception of understanding of the content of IRs of the group who had degrees, as is illustrated in Section 5.4.1.1. Although the understanding of the content of the IRs for respondents who had a degree was disappointingly low compared to the assumed benchmark of an acceptable level of understanding at an average total percentage score of 44.76% (see Table 5.22), this was significantly higher than that of respondents who had no degree, at 30.47%.

The same observation was also evident when considering the respondents' perception of understanding and respondents' understanding of the content of IRs of the individual share shareholders when dividing them between shareholders who made investment decisions on

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[74] See Table 5.13.
[75] See Table 5.2.
[76] See Table 5.3.

their own initiative, as opposed to those who allowed financial advisors to take the initiative when making investment decisions. Those individual shareholders who made their own investment decisions had a higher perception of understanding of the content of the IRs than those who allowed their brokers to make investment decisions. Once again, the understanding of share investors making their own investment decisions was higher, at an average total percentage score of 41.3%, than the mean of 29.3% of the broker-decision group (see Table 5.44).

The perception of understanding of the content of the IRs would be a greater contributing factor to the final decision of individual shareholders as to whether they should make their own investment decisions than their tested understanding, since the level of understanding of individual respondents measured in terms of this study was not known to them. It could be that they tend to overestimate their level of understanding of the content of IRs.

6.3.2.1.3 Recommendations

No specific recommendations emerged, because how respondents choose to make their investment decisions is beyond the control of the companies publishing IRs. However, see Section 6.3.1.2.1, above, proposing financial literacy training for individual shareholders.

6.3.2.2 Category 1: Sources of information used by individual shareholders when making investment decisions

6.3.2.2.1 Background

The survey results presented in Table 5.49 indicate that by far the most popular source of information on which investment decisions were based was the financial press, with nearly half (49.3%) of respondents “Always / Nearly always” using sources such as newspaper and magazine articles as their sources of information when making investment decisions. This view is also strengthened by the fact that 86.3% of respondents used the financial press sources “Always/Nearly always” or “Sometimes”.

The second and third most popular sources used “Always/Nearly always” were the ARs (27.0%) and financial investment programmes on radio and television (24.6%). The difference in use of these two sources is marginal, at 2.6 percentage points.

When considering those respondents who used the ARs and financial investment programmes on radio and television "Always/Nearly always" and "Sometimes", financial investment programmes on radio and television appeared to be more popular, while the popularity of ARs receded slightly.

IRs were the fourth most popular source of information to facilitate investment decisions, considering respondents who used them "Always/Nearly always" (20.6%). However, when considering a source that was used exclusively or nearly to the exclusion of other sources, the difference between IRs in fourth place (20.6%) and the internet in fifth place (20.4%) was negligible.

To ensure that respondents were not focused on only the list of options provided in the questionnaire, respondents were also given an open-ended question, allowing them an opportunity to provide other sources of information they used (see Section 5.7.2). Unfortunately, the majority of "other" resources provided by respondents were already mentioned in the list of resources in the questionnaire and the "new" additional resources provided were sources such as "my own view", "share price movements" and "reports" which were of little assistance.

6.3.2.2.2 Conclusion

Bearing in mind that the majority of respondents made their own investment decisions, the above analysis appears to indicate that by far the most popular source of investment decision information used by respondents was the financial press. This source of investment decision information has several advantages, namely that it is easily accessible, can be retained for future reference, could be deemed reputable since articles in the financial press are generally written by well-known and trusted financially informed individuals, the guidance given in such articles is written in accessible language, and these articles may even be viewed as a replacement of the advice of brokers/financial advisors.

It is also evident that the most popular sources of information used by respondents tend not to require a large financial outlay. For instance, the cost of newspapers and magazines is not prohibitive; ARs are provided by the company in which shares are held at no direct cost to the shareholder; radio and television programmes are virtually free (except for licensing fees and monthly subscriptions, where applicable). IRs are also provided at no cost by the company in which shares are held.

Although IRs are listed as the fourth most popular source of investment information of respondents in this survey, one should be careful about deducing that individual shareholders prefer using the IR as a source of information for investment decisions. Respondents could have been influenced by the fact that the survey as a whole deals with IRs in particular and this could have inflated the importance attached to IRs as a source of information for investment decisions. This view is corroborated by the results presented in Table 5.51, where it is evident that nearly 57% of respondents indicated that they virtually never used IRs for making investment decisions in the last eight years or more. It is acknowledged that this question could have been phrased better and it is recommended that this is done when future research on this matter is conducted. Apart from the conclusion drawn based on the results presented in Table 5.51, other findings in Section 5.8 tend to support the notion that individual shareholders do not deem IRs to be particularly important for their investment decision-making.

6.3.2.3 Category 1: Crucial additional information in IRs required by individual shareholders to facilitate investment decisions

6.3.2.3.1 Background

The survey results in Section 5.9 (see Table 5.55) indicated that 61.17% (674 out of 1 102) of respondents were satisfied with the information provided in IRs. To arrive at this conclusion, it was assumed that if respondents did not answer, indicated that nothing more was required, stated that sufficient information was provided, or did not know what to ask for, they did not believe that additional information in IRs was required. In terms of their responses, 38.83% (428 out of 1 102) of respondents believed that additional information was required and were thus seen as dissatisfied respondents. A more detailed analysis of what dissatisfied respondents required, is set out in Table 5.56 and this is now examined in more detail in Section 6.3.2.3.2.

6.3.2.3.2 Conclusions

The item of additional information most commonly required is more forward-looking information. Of the dissatisfied respondents, 26.9% believed that more such information in the IR was required for investment decision purposes, but the range of types of forward-looking information required by respondents was so diverse that no clear-cut need could be identified.

Apart from forward-looking information, a total of 10.5% of dissatisfied respondents indicated that they believed information on the share price of the company providing the IR during the interim period would be useful. Although presenting this information could be convenient for shareholders, the information would be dated by the time it reached individual shareholders and consequently would add little value. In addition, sufficient information on listed companies in stock exchange reports is available to enable shareholders to find this information themselves.

Of the respondents who were dissatisfied, 9.8% indicated that they would like more information on directors' emoluments and share dealings to be presented in IRs. This type of information could be valuable, and shareholders would have difficulty in obtaining this information from a source other than the IR.

6.3.2.3.3 Recommendation

Of the three most popular items of information that could be added to IRs to facilitate investment decisions as identified in this survey, it would appear that the most popular item would be more future-oriented information. Given the nature of the integral approach[77] to presenting IRs as used in the US, it appears as if changing to this approach could provide information that would assist in forecasting what the entity's financial position and liquidity would be by the end of the year. However, the future-oriented items identified by respondents in their questionnaires were (albeit diverse) very specific and did not include an extrapolation of financial information from six months to a full year. For instance, respondents expected management to provide an overview of future prospects of the company, a forward-looking view and future strategic direction of management. These items were asked for in addition to information currently provided under the discrete approach used for the preparation of IRs in terms of IAS 34.

In view of the effective response rate on the other two items listed by the dissatisfied respondents (share price and information on directors' emoluments and their share dealings),

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[77] See Section 3.1.1.

it appears that the prevalence of these items was very low, compared to the total number of respondents.

6.3.2.4 Category 2: Sequence of components of the IR

6.3.2.4.1 Background

With regard to the sequence in which individual components of IRs should be presented, as addressed in Section 5.10 (see Table 5.57), respondents were mostly satisfied with the current sequence of the individual components of the IRs. However, some respondents displayed ambivalence about whether the statement of cash flows or statement of changes in equity should be displayed third or fourth. The sequence of individual components of IRs as prescribed by IAS 34.8 therefore seems to be acceptable to individual shareholders.

6.3.2.4.2 Conclusion

There is no need to do further research on the sequence in which individual components of the IR should be presented. Respondents appeared to be satisfied with the sequence in which these components are presented at present, and this sequence is also consistent with that used for ARs.

6.3.2.5 Category 2: Reading of IRs by individual shareholders

6.3.2.5.1 Background

It is important to remember that the readability of narrative information in IRs was not assessed in this study, since the focus was on the understanding of the context and content of IRs, as defined in the List of definitions of terms and concepts, and not on management commentary. The results of the survey as included in Section 5.11 therefore pertain to the extent of the thoroughness of respondents' reading and factors that would dissuade individual shareholders (respondents) from reading IRs only. It would appear from Table 5.58 that the commentary by management was the component of IRs that respondents read most thoroughly, because it was associated with the lowest "centre of gravity" mean, while the statement of comprehensive income was the second most thoroughly read component.

The factors that would dissuade respondents from reading IRs are presented in Table 5.59. The fact that respondents claimed that they did not have enough time to read the individual components of IRs appeared to be the most important and most commonly cited reason why any individual component of IRs would not be read. It is not surprising that this factor (lack of time) was more prevalent with regard to commentary by management and the statement of comprehensive income, because respondents considered these components to be the most important individual components[78] of IRs, and respondents would probably only neglect to read these if they did not have time.

In respect of why respondents would not read the commentary by management, print size appeared to be the second most prevalent discouraging factor. This was confirmed by the fact that excessively small printing appears to play a larger role where individual components of IRs contain more narrative information, as in the case of management commentary and, to a lesser extent, explanatory notes.

The third most common reason why respondents do not read the individual components of IRs, excluding explanatory notes and the commentary by management, was that respondents felt that they did not understand these components. This lack of understanding was confirmed by the conclusion on the primary objective of this thesis.

6.3.2.5.2 Conclusions

The fact that individual shareholders indicated that the commentary by management was read most thoroughly was not surprising, because this component of IRs provides narrative explanations of matters presented in the IR. However, as was explained earlier, the non-standardised content of commentary by management was specifically excluded from the assessment of the understanding of the content of IRs as defined in the List of definitions of terms and concepts.

Neither standard setters nor preparers of IRs have influence on the amount of time that individual shareholders (readers) of IRs have at their disposal. However, the size of the fonts used in the printing is a matter that these two stakeholders can control, and they would be able to contribute to ease of reading by addressing this issue.

[78] See Table 5.54.

6.3.2.5.3 Recommendations

Prescribing the minimum font size used in IRs would appear to fall outside the sphere of influence of the standard setters of the IASB, especially since these reporting standards are intended to service the international community. However, a recommendation from the IASB in this regard may carry some weight in individual constituencies.

However, it is proposed that the minimum font size of lettering used in IRs be prescribed by the JSE in its listings requirements for IRs that are distributed in hard copy, as this would be a factor that preparers can control, and such guidelines presented via the regulating authorities would improve the ease of reading of IRs. It is recommended that the font size, especially that used for the commentary by management, explanatory notes and the statement of comprehensive income, be made slightly larger than may currently be usual to facilitate ease of reading, as shareholders appear to consider these components of IRs to be more important than the other components of the IRs.

6.3.2.6 Category 2: Preferred medium of communication for individual shareholders in the case of IRs

6.3.2.6.1 Background

A detailed analysis of the responses on this matter is presented in Table 5.60 . Of the respondents, 58.7% indicated that they would still prefer to receive the IR by post, while 36.7% of the respondents indicated that they would prefer to receive it by e-mail. Only 2% of respondents chose other media of communication or a combination of communication media, and 2.6% would prefer not to receive IRs at all.

An analysis of the preference by age group indicated that just less than 59.6% of respondents between the age group >29 to 40 years preferred e-mail, while just more than 45.8% of the age group >40 to 65 years preferred e-mail. This indicates a steady decline in the preference for e-mail the older respondents were, which was to be expected, as computer literacy among and access to computers by older respondents (as a group) is likely to be less.

It can be concluded that the majority of respondents at this stage would still prefer to receive the IR by post, but there are a substantial number of respondents who would prefer to receive the IR by e-mail. It is expected that the demand for the distribution of IRs by e-mail will grow over time as people in the current >29 to 65 year age brackets become older and retain their access to e-mail and other electronic mediums of communication.

6.3.2.6.3 Recommendations

It is recommended that this trend be monitored over time by means of further longitudinal research to determine when a shift to providing IRs by e-mail only would be feasible, which would be when e-mail is the preferred medium of communication for the majority of shareholders. Once this shift occurs, it will facilitate substantial cost savings to listed companies, which are currently required to provide all shareholders with a hard copy of IRs.

6.4 FUTURE RESEARCH

During the course of this study, the following areas requiring further research were identified:

- Since the number of questions devoted to the individual components of IRs was limited due to the research strategy of postal questionnaires, the understanding of each individual component of IRs could not be assessed in this study. In addition, the variation in the marks allocated to each question complicated this assessment. Further research could be conducted to establish to what extent each of the individual components of IRs is understood by individual shareholders. It is recommended that such research be done by means of interviews rather than by means of a postal questionnaire to be able to expose respondents to a larger number of structured questions, as was done in Lee and Tweedie's (1977:12) study.
- Although this study addressed the sources of information used when making investment decisions, more objective results will be obtained if future research is not linked to a topic of research such as IRs, as is the case in the current study.
- The range of additional information respondents would require to be included in IRs to facilitate investment decisions could not be refined to a usable level in this study, since answers by respondents covered too wide a spectrum of possible items of additional information. Establishing more clearly what this information should entail, would be useful, and thus further research should be conducted to establish clearly what respondents would want in this regard.
- The understanding of the narrative sections of IRs could be assessed using the Cloze procedure during further research. However, due to the brevity of the narrative sections

of IRs, the execution of the Cloze procedure may be challenging. Included in such research could be an investigation on the minimum font size to be used when publishing IRs.

- It is recommended in respect of medium of communication that this trend be monitored over time via future longitudinal research in order to determine when providing IRs by e-mail only would become feasible as the preferred medium of communication for the majority of shareholders.

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APPENDICES

APPENDIX A:
COVERING LETTER AND QUESTIONNAIRE

19 February 2010

Dear respondent

You, as an individual shareholder/institutional shareholder, have been selected to take part in **one of the first studies of its kind** on interim financial reports in the world. The research will be done in the pursuit of a D Com degree in Financial Accounting at the University of Pretoria.

To this end you are kindly requested to assist me in gathering information (complete a questionnaire) **on the usefulness and understandability of interim financial reports** with specific reference to the interim financial report that you have just received.

The objective of the questionnaire is to determine to what extent the content of the interim financial report is understood by the users thereof and also to what extent they use interim financial reports when making their investment decisions.

The results of this research could lead to future interim reports being more understandable and useful for making investment decisions.

Please complete the questionnaire included with this interim report and **return it** to me **in the enclosed pre-addressed envelope**. It will take **approximately 15 minutes** of your time.

Information to consider when completing this questionnaire

Please answer the questions in the questionnaire as honestly as possible, bearing in mind that the questionnaire is **completely anonymous** and that there is no way in which you can be identified. Your responses will be treated in the strictest confidence and will only be utilised in a summarised form (i.e together with the answers of other respondents).

Please complete all the questions in the questionnaire.

Note that since I am unable to identify who has replied, **you could receive up to two reminders** to complete the questionnaire. If, on receiving a reminder, you have already completed the questionnaire, please disregard this follow-up request.

Should you want to receive a summary of the results of this research, please lodge a request at: johan.oberholster@up.ac.za.

Your time and your contribution to this unique research project are much appreciated.

Note that the answers to the questions asked should reflect your view and NOT that of a firm or other institution.

Prof JGI Oberholster
RESEARCHER
Department of Accounting

Prof C Koornhof
SUPERVISOR AND DEAN
Faculty of Economic and Management Sciences

UNIVERSITEIT VAN PRETORIA
UNIVERSITY OF PRETORIA
YUNIBESITHI YA PRETORIA

QUESTIONNAIRE: INTERIM FINANCIAL REPORTS SENT TO INDIVIDUAL SHAREHOLDERS

Respondent V1 1

Please answer each question by circling an appropriate number in a shaded box or by writing your answer in the shaded space provided

Consent to participate. (**Circle** the "**1**" below if you **consent** to participate)

I hereby ***GIVE*** my informed consent to take part in this research project	**1**

SECTION A: Background Information

1. What is your **gender**? (**Circle** either "**1**" or "**2**" below)

Male	**1**	V2 5
Female	**2**	

2. How **old** are you? (Please indicate **completed years**)

	V3 6

3. What is you **highest academic level** of education? (**Circle** a **single number** between "**1**" and "**5**" and fill in an answer next to each "**Specify**", *if appropriate*, below)

High (Secondary) School **not completed**	**1**	V4 8
High (Secondary) School **completed**	**2**	
Diploma or Certificate	**3**	
First Degree – Specify:	**4**	V5 9
Post-graduate degree – Specify:	**5**	V6 11

4. Was **Accountancy** one of your **major** (*final year*) degree / diploma / certificate subjects? (**Circle** a **single number** between "**1**" and "**3**" below)

Yes	**1**	V7 13
No	**2**	
Not applicable	**3**	

5. What **professional qualification** do you have (if any)?

	V8 14

Question 6 *follows on the next page …..*

6. How many **shares** of the Company, identified in the accompanying *Interim Financial Report*, are **in your portfolio** (collection of shares)?

V9 | | | | | 16
V10 | | 20

7. How many **Companies** on the **JSE** do you **currently have shares** in?

V11 | | | | | 21

8. How would you **describe** your **current employment status**? (**Circle** a **single number** between "**1**" and "**4**" or, *if appropriate*, fill in an answer next to "**specify**" below)

I am employed / self-employed full-time	**1**
I am employed / self-employed part-time	**2**
I am retired	**3**
I am unemployed	**4**
Other (specify:)	

V12 | | 25

9. What **field** are you (or were you) working in? (**Circle** a **single number** between "**1**" and "**3**" or, *if appropriate*, fill in an answer next to "**specify**" below)

Accounting, investment, banking or financial management fields	**1**
Medical and legal fields	**2**
Engineering, construction and related fields	**3**
Other (specify:)	

V13 | | 26

10. What is your **single** most important **objective** (goal) when investing in shares? (**Circle** a **single number** between "**1**" and "**5**" or, *if appropriate*, fill in an answer next to "**specify**" below)

Speculative gains (making a quick profit within a year)	**1**
Long-term asset/capital growth (holding shares for at least a year or more)	**2**
Return in the form of dividends, steady income	**3**
A combination of dividend income & capital growth	**4**
To achieve a specific taxation effect/benefit	**5**
Other (specify:)	

V14 | | | 27

<u>Question 11</u> ***follows on the next page .....***

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11. How do you **currently** make investment **decisions** to *buy*, *sell* or *hold* shares in **any** Company? (**Circle** a **single number** between "**1**" and "**4**" or, *if appropriate*, fill in an answer next to "**specify**" below)

I take investment decisions entirely on my own initiative	**1**	V15		29
I take investment decisions on my own initiative with the *direct involvement* of an investment analyst, stockbroker, financial advisor, accountant, fund manager or similar	**2**			
Investment decisions are *taken solely* by an investment analyst, stockbroker, financial advisor, accountant, fund manager or similar *on my behalf*	**3**			
Investment decisions are taken by an investment analyst, stockbroker, financial advisor, accountant, fund manager or similar *after consultation with me*	**4**			
Other (specify:)				

12. In **general**, how **often** do you **consult** the following sources of **information** when making an investment decision to *buy*, *sell* or *hold* shares in **any** Company? (**Circle** a **single number** between "**1**" and "**3**" per "**Information source**" and, *if appropriate*, fill in an answer next to "**specify**" below)

Information source	**Always / Nearly always**	**Sometimes**	**Hardly ever / Never**			
The Financial Press (Newspaper or magazine articles)	**1**	**2**	**3**	V16		30
The Annual financial reports of the Company	**1**	**2**	**3**	V17		31
Financial investment programmes on radio and/or television	**1**	**2**	**3**	V18		32
Interim financial reports of the Company involved	**1**	**2**	**3**	V19		33
The officials of the Company involved	**1**	**2**	**3**	V20		34
Advice of friends/acquaintances	**1**	**2**	**3**	V21		35
Advice of colleagues	**1**	**2**	**3**	V22		36
The Internet	**1**	**2**	**3**	V23		37
Notices from the JSE	**1**	**2**	**3**	V24		38
Seminars	**1**	**2**	**3**	V25		39
Other (specify:)	**1**	**2**	**3**	V26		40
				V27		41

Question 13 ***follows on the next page …..***

13. In **general**, how **important to you** are the following components of the *Interim Financial Report* when making a decision to *buy*, *sell* or *hold* shares in **any** Company? (**Circle** a **single number** between "**1**" and "**4**" per "**Importance of component**" below)

Importance of component of an Interim Financial Report	Very important	Fairly important	Not important	I do not use it		
A condensed balance sheet / statement of financial position	1	2	3	4	V28	43
A condensed income statement / statement of comprehensive income	1	2	3	4	V29	44
A condensed statement of changes in equity	1	2	3	4	V30	45
A condensed cash flow statement / statement of cash flows	1	2	3	4	V31	46
Selected explanatory notes	1	2	3	4	V32	47
Comment/commentary by management	1	2	3	4	V33	48

14. During the **last 8+ years** (since 2000), approximately **how many times** have you **made use** of the *Interim Financial Report* in **taking** investment **decisions** to *buy*, *sell* or *hold* shares in respect of any of your **shareholdings**?

	V34	49

SECTION B: Assessment of understanding

15. Please indicate the **extent in general** of the **relevance** of the **information** contained in the *Interim Financial Report* in respect of you **making** investment **decisions** to *buy*, *sell* or *hold* shares. (**Circle** a **single number** between "**1**" and "**3**" below)

I find the information in the *Interim Financial Report* relevant to making an investment decision to *buy*, *sell* or *hold* shares	1	V35	53
I do not find the information in the *Interim Financial Report* relevant to making an investment decision to *buy*, *sell* or *hold* shares	2		
I actually do not understand the information in the *Interim Financial Report* and therefore I do not find it relevant	3		

16. Who do you believe is **legally responsible** for the *Interim Financial Report* of a Company? (**Circle** a **single number** between "**1**" and "**5**" or, *if appropriate*, fill in an answer next to "**specify**" below)

The Chairman of the Company	1	V36	54
The Chief Executive Officer (CEO)	2		
The Board of Directors	3		
The Financial Director (CFO)	4		
The Auditors of the Company	5		
Other (specify:)			

Question 17 ***follows on the next page .....***

17. Is the *Interim Financial Report* accompanying this questionnaire audited or not? (Circle either "1" or "0" below)

Audited	1	V37		56
Not audited	0			

18. In your view, what is the single most important objective of providing an *Interim Financial Report*? (Circle a single number between "1" and "4" below)

To make Directors of the Company accountable to shareholders	1	V38		57
To provide information to the South African Revenue Service in respect of the first six months of a financial year	**2**			
To provide shareholders with a progress report on the financial performance and position of the Company after the first six months of the financial year	**3**			
To provide shareholders with information for investment decisions in respect of the Company	**4**			

19. To what **extent** do you **read** the following **components** of the *Interim Financial Report*? (**Circle** a **single number between** "**1**" and "**3**" for ***each*** "**Component**" below)

Component	**Thoroughly**	**Not thoroughly**	**I do not read it at all**			
Condensed balance sheet / statement of financial position	**1**	**2**	**3**	V39		58
Condensed income statement / statement of comprehensive income	**1**	**2**	**3**	V40		59
Condensed statement of changes in equity	**1**	**2**	**3**	V41		60
Condensed cash flow statement / statement of cash flows	**1**	**2**	**3**	V42		61
Explanatory notes	**1**	**2**	**3**	V43		62
Comment/commentary by management	**1**	**2**	**3**	V44		63

20. Which of the following "**Factors**" would **dissuade** you from reading the *Interim Financial Report* **thoroughly**? (**Circle** a **single number between** "**1**" and "**5**" for ***each*** "**Component**")

Component	**I do not understand it**	**I do not have the time**	**I am not interested**	**It is not important**	**The printing is too small**			
Condensed balance sheet / statement of financial position	**1**	**2**	**3**	**4**	**5**	V45		64
Condensed income statement / statement of comprehensive income	**1**	**2**	**3**	**4**	**5**	V46		65
Condensed statement of changes in equity	**1**	**2**	**3**	**4**	**5**	V47		66
Condensed cash flow statement / statement of cash flows	**1**	**2**	**3**	**4**	**5**	V48		67
Explanatory notes	**1**	**2**	**3**	**4**	**5**	V49		68
Comment/commentary by management	**1**	**2**	**3**	**4**	**5**	V50		69

Question 21 ***follows on the next page …..***

21. How **well** do you **understand** the following **components** of the *Interim Financial Report*? (**Circle** a **single number** between "**1**" and "**4**" for ***each*** "**Component**" below)

Component	**Very well**	**Well**	**Not well**	**Not at all**			
Condensed balance sheet / statement of financial position	**1**	**2**	**3**	**4**	V51		70
Condensed income statement / statement of comprehensive income	**1**	**2**	**3**	**4**	V52		71
Condensed statement of changes in equity	**1**	**2**	**3**	**4**	V53		72
Condensed cash flow statement / statement of cash flows	**1**	**2**	**3**	**4**	V54		73
Explanatory notes	**1**	**2**	**3**	**4**	V55		74
Comment/commentary by management	**1**	**2**	**3**	**4**	V56		75

22. What **basis of valuation** is used to determine the **carrying amounts** (book values) of the following items included in the *Condensed Balance Sheet / Statement of Financial Position*? (**Circle** a **single number** between "**1**" and "**5**" for ***each*** "**Basis**" below)

Basis of valuation	**Original cost price**	**Original cost less accumulated depreciation**	**Replacement cost**	**Lower of cost and net realisable value**	**I really do not know**			
Property, plant and equipment (fixed assets)	**1**	**2**	**3**	**4**	**5**	V57		76
Inventory (stock)	**1**	**2**	**3**	**4**	**5**	V58		77

23. To what does the **operating lease accrual/liability/obligation** (the line-item) in the *Condensed Balance Sheet / Statement of Financial Position* **refer**? (**Circle** a **single number** between "**1**" and "**4**" below)

The amount payable in respect of an operating lease in the 12 months subsequent to the balance sheet / statement of financial position date	**1**	V59		78
The accrual of operating lease payments in order to recognise these payments in the income statement on a straight-line basis over the lease term	**2**			
The correction of the erroneous application of the lease standard in the past	**3**			
I really do not know	**4**			

Question 24 ***follows on the next page .....***

24. Consider **each** of the **statements** below and provide an **answer** to **each**. (**Circle** a **single number** between "**1**" and "**3**" for ***each*** "**Statement**" below)

Statement	**Yes**	**No**	**I really do not know**			
The profit before tax line-item on the *Condensed Income Statement / Statement of Comprehensive Income* represents the difference between income/revenue received and/or earned and expenses paid and/or incurred during the six months under review	1	2	3	V60		79
The line-item for tax in the *Condensed Income Statement / Statement of Comprehensive Income* includes merely the taxation payable to SARS	1	2	3	V61		80
The *Condensed Statement of Changes in Equity* reflects all movements in equity (share capital and reserves) that occurred during the six month period under review	1	2	3	V62		81
The final balances on the *Condensed Statement of Changes in Equity* can be linked to condensed balance sheet items at the end of the six month period	1	2	3	V63		82
Net cash flows from operating activities on the *Condensed Cash Flow Statement / Statement of Cash Flows* include interest payable and dividends payable	1	2	3	V64		83
The purchase of property, plant and equipment (fixed assets) on credit, would represent a cash outflow under investing activities on the *Condensed Cash Flow Statement / Statement of Cash Flows*	1	2	3	V65		84

25. What do you **understand** by the term "**Accounting policy**"? (**Circle** a **single number** between "**1**" and "**4**" below)

It is the policy used when assessing the creditworthiness of the customers buying on credit from the company	1	V66		85
It is the policy used to determine the amounts used when preparing the financial statements	2			
It is the policy the company follows with regard to the exchange and/or return of goods sold to customers on credit	3			
I really do not know	4			

26. Are the **accounting policies** used in the *Interim Financial Report* the **same** as those used in the Annual Financial Statements of the company? (**Circle** a **single number** between "**1**" and "**3**" below)

Yes	1	V67		86
No	2			
I really do not know	3			

Question 27 ***follows on the next page .....***

27. Which **one statement** of the following corresponds **most closely** to your view of *Interim Financial Reports*? (**Circle** a **single number** between "**1**" and "**3**" or, *if appropriate*, fill in an answer next to "**specify**" below)

I am able to understand the information contained in the *Interim Financial Report* and it is of considerable relevance and use in my investment decisions	**1**	V68		87
I am able to understand the information contained in the *Interim Financial Report* but find it is of little relevance and use in my investment decisions	**2**			
I am unable to understand the information in the *interim Financial Report* sufficiently for it to be of any use to me with regard to investment decisions	**3**			
Other (specify:)				

28. Would you consider the information contained in the *Interim Financial Reports* as **adequate** for you as a shareholder to make investment decisions? (**Circle** either "**1**" or "**0**" below)

Yes	**1**	V69		88
No	**0**			

29. List **one crucial item** of **additional information** that is not presented in the *Interim Financial Report* at this stage that you **would require** to make investment decisions.

	V70			89

30. Please indicate the **sequence** in which you would prefer the **components** of the *Interim Financial Report* to be **presented**. (Enter a "**1**" for the component you prefer to be "**First**", to a "**6**" for the component you prefer to be "**Sixth**". **Do not repeat a number between "1" and "6"**)

A condensed balance sheet / statement of financial position		V71		91
A condensed income statement / statement of comprehensive income		V72		92
A condensed statement of changes in equity		V73		93
A condensed cash flow statement / statement of cash flows		V74		94
Selected explanatory notes		V75		95
Comment/commentary by management		V76		96

31. How would you **prefer** to **receive** the *Interim Financial Report*? (**Circle** either "**1**" or "**2**" or, *if appropriate*, fill in an answer next to "**specify**" below)

In the post	**1**	V77		97
Via e-mail	**2**			
Other (specify:)				

Thank you for your time and co-operation

APPENDIX B:
RESULTS OF PILOT QUESTIONNAIRE

Table B1: Marks awarded for assessment of understanding for Pilot Groups 1 and 2 (Q 16 to Q18 and Q22 to Q 26)

Correct	Pilot Group 1		Pilot Group 2							
Q V# Answer Mark	1A	1B	2A	2B	2C	2D	2E	2F	2G	2H
Context questions										
16 V36..3* (2)	2	2	2	0	2	0	0	2	2	0
17 V37..0* (1)	1	1	0	1	0	1	0	1	1	0
18 V38 3* (1)	0	1	1	1	1	1	1	1	1	1
Content questions										
22 V57 2*^ (2)	2	0	0	$	0	2	2	2	2	2
22 V58 4*^ (3)	3	3	0	$	0	3	0	3	3	0
23 V59 -*^ (!)	(!)	(!)	(!)	(!)	(!)	(!)	(!)	(!)	(!)	(!)
24 V60 1*^ (1)	1	1	1	$	1	1	0	1	1	1
24 V61 2*^ (2)	2	2	0	$	0	2	2	2	2	2
24 V62 1*^ (1)	1	1	1	$	0	0	1	0	1	1
24 V63 1*^ (2)	2	2	2	$	2	2	2	2	2	2
24 V64 2*^ (2)	0	2	2	$	0	2	0	0	2	0
24 V65 2*^ (2)	2	2	0	$	0	0	2	0	2	2
25 V66 2*^ (2)	2	2	2	$	2	2	2	2	2	0
26 V67 2*^ (1)	1	1	1	$	0	1	0	1	1	1
***Total Score / 22**	19	20	12	$	8	17	12	17	22	12
***Total percentage (%) score**	86	91	55	$	36	7	55	7	100	55
^Total Score / 18	16	16	9	$	5	15	11	13	18	11
^Total percentage (%) score	89	89	50	$	28	83	61	72	100	61
	K	K	L	L	L	K	L	K	K	L

Key to abbreviations and symbols used in Table B1:

(!) This question was excluded from the final scoring, as the issue dealt with only surfaced in the case of Company A, and to use it for the other two companies would have compromised the comparability of the scores obtained by respondents from all three companies involved in the survey.

$ This symbol indicates that the member of the pilot group declined to answer the question because the person did not have any idea of the answers and did not want to guess. This comment resulted in the inclusion of an "I really do not know" option in the final questionnaire.

K Member of pilot group is considered to be knowledgeable.

L Member of pilot study is a layperson and/or has dated knowledge.