

Corporate Risk Disclosure in the UK: Current Practices and Trends

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Abstract: There has been considerable debate on risk disclosure adequacy and usefulness to the users. Recently, a number of proposals and documents were released and new accounting standards were issued to encourage companies' directors to report on risk in a greater depth. Using content analysis of 156 annual reports prepared by 52 UK listed companies over the period of 1998-2004, this study examines and explores risk disclosure practice with the aim of establishing trends. The study also relates the extent of risk disclosure to firm-specific characteristics. Overall, the results show an upward trend in the level of information disclosed during the six-year period. The study discusses and comments on the form and nature of information disclosed. We found industry type and US dual listing variables to be related to the level of risk information disclosed by the sample companies, with industrial and US-London-dual-listed companies having higher disclosure levels. However, the empirical evidence shows total risk disclosure is not related to size and leverage.

Keywords: Risk Disclosure, Firm Characteristics, UK Companies

1 Introduction

The last 15 years have seen dramatic changes in the business environment driven by fundamental developments in technology, society and world politics. The evolution of new technology especially has facilitated the expansion of businesses as well as the globalisation of capital markets. While such changes were necessary for businesses' growth and expansion, they have, however, created many challenges and concerns. Business transactions and structures have become more complex. Trading conditions have also become (and remain) very tough and competitive with new businesses emerging all the time. The rise in stock return volatility worldwide together with an increase in economic, political and regulatory uncertainty around the globe was also a concern. At the same time, the business scandals of the late 20th and early 21st century (e.g., Enron, Maxwell, WorldCom) have shaken the confidence of investors and regulators. The survey of UK investors conducted by Cavendish Asset Management (2002) found that two thirds of UK investors no longer feel confident investing in the stock market as a result of fraud and accounting problems at Enron and WorldCom.

With these changes in the business environment in mind, there has been a rise in the attention and interest of regulators, accounting standard setters, stock markets, and accounting bodies worldwide in the quality of financial reporting. Regulators around the world have been actively considering how to promote better disclosure by listed companies in order to increase transparency of financial reporting hence restore investors' confidence, especially by encouraging disclosures which will give investors and others a clearer idea of the risks faced by corporations. It might be anticipated that companies which raise capital through stock-market listings would increase their risk disclosures in order to reduce their cost of capital. This paper represents an effort to examine changes in the level of risk disclosure in corporate annual reports.

The remainder of this paper is structured as follows: section 2 reviews corporate reporting and risk disclosure literature, covering its requirements and recommendations, and its motivations and benefits. Research Hypotheses are developed in section 3. Section 4 describes the selection of the sample and research method. Sections 5 and 6 present the results and hypothesis testing respectively. Section 7 discusses the results and Section 8 presents our conclusions and makes suggestions for future research.

2 Literature Review

2.1 Corporate Reporting: The Disclosure Gap and Motivation for Change

The rapid pace of change in business environment forced companies to use new types of information to manage their businesses. Many companies have adopted new performance measures for internal reporting purposes, such as those developed in the framework of the Balanced Scorecard (Kaplan and Norton 1996). With regard to risk, various risk management methods have evolved over time. Companies have learnt to use sophisticated techniques to quantify and monitor risk effectively, thus reducing the quality gap in internal risk management systems. However, companies' external reporting at the turn of the century was perceived as lacking in adequate disclosure on risk and uncertainties (Cabedo and Tirado, 2004). The American Institute of Certified Public Accountants (AICPA, 1987) stated that financial statements users are increasingly demanding more information to help them assess risk and uncertainties. Schrand and Elliott (1998) summarised and documented the debate held in the 1997 AAA/FASB conference on risk reporting by companies to their stakeholders. They suggest that US companies were not providing sufficient information, related to risk, in their annual reports. In addition, there was recognition that financial reporting standards developed by bodies such as the International Accounting Standards Board (IASB) and the UK's Accounting Standards Board (ASB) or developed from civil law codes in continental Europe fell short of meeting all the information needs of all users. Previous disclosure research (e.g. Rankin, 1996) suggested that users, mainly investors, are demanding more information than they are getting. Further evidence (e.g. Beattie and Pratt, 2002, Solomon et al., 2000; ICAEW 1997, 1999; Schrand and Elliott, 1998) noted investors demand for more information to help them assess a company risk profile and make informed decisions. This has created a reporting gap or information problem. This information problem, actually a form of information asymmetry, occurs when management holds information and withholds it from investors for certain reasons, including commercial sensitivity and uncertainty about measurements. It is a key issue in corporate disclosure that may disturb the functioning of the capital markets leading to their partial or complete breakdown (Akerlof, 1970).

This emphasised the importance of narrative disclosure where additional information on company's performance, prospects, and risk and uncertainties are prepared. The regulator and accounting setters in the UK have long recognised the importance of the topic. The Companies Act 1985 requires companies for a 'description' of the principal risks and uncertainties that they face in a 'business review' section identified as part of the Directors' Report (Companies Act 1985, S.234). There has been long constructive discussion and debate over the Operating and Financial Review (OFR) which was first launched by ASB in 1993 (ASB 1993), with a revised statement being issued in 2003 (ASB 2003), recommending UK listed companies to discuss principal risks and uncertainties. The issuance of the statement was an important shift emphasising the importance of narrative disclosure. The government concluded that it was not practical to regulate the OFR by law, partly because of the question of whether Directors could be sued over poor judgments in risk analysis published in the OFR (the question of safe harbour protection), and in 2006 it was left to the ASB to issue a Reporting Statement (replacing Reporting Standard RS 1) recommending that "the OFR should include a description of the principal risks and uncertainties facing the entity together with a commentary on the directors' approach to them" (ASB, 2006, para 52). The requirements for a business review remain. Risk disclosure is also influenced by the standard setters' requirements through the issuance of accounting standards (e.g. FRS13, IAS 32, and IAS39) underpinning the reporting of risk.

The growing literature on corporate governance (CG) provides further evidence that the information needs of users have been recognised by regulators and accounting professions. The CG debate began with the publication in 1992 of Cadbury report which recognised the needs of users for some explanation of the factors likely to influence a company future progress. Cadbury report was followed by the publication of a series of statements and guidelines (e.g. combined code and Turnbull report). Under the combined code (1998) companies' directors should state whether they complied with the code by conducting annual review

of all controls and risk management system. The Turnbull Report issued in 1999 underlined the importance of internal control and risk management and explicitly encouraged companies' directors to provide annual report users with high quality and meaningful information related to key risks.

The information needs of users include those related to risk and uncertainties were also long noted and debated by accounting bodies worldwide. For example, in the UK, the Institute of Chartered Accountants in England and Wales (ICAEW) showed an early interest in the subject and issued several documents in order to help companies' directors to identify, manage and measure risk and further enhance their public disclosure by providing more relevant risk-related information on all types of risk that have a potential bearing upon corporate performance. The best examples are *Financial Reporting of Risk: Proposals for a Statement of Business Risk*; issued in 1997; and *No surprises: the case for better risk reporting* issued in 1999.

2.2 Motivations and Benefits for Disclosure

In research on corporate disclosure, the issue of understanding the motivations for disclosure has attracted considerable attention. Researchers on disclosure have been applying a number of theoretical frameworks to explain what motivates managers to disclose more information than it is necessitated by regulation. However, there is no single theory available to explain disclosure phenomenon sufficiently, and researchers to date tend to select whichever theory articulates best with their hypothesis (Linsley and Shrives, 2000). Examples of theories include agency theory, signaling theory, stakeholders' theory, capital need and benefit cost theory. Linsley and Shrives (2000) suggest that some of these theories could be relevant for discussion of the motivation of risk disclosure. Companies may disclose information in order to meet investors demand for information, thus reduce their interference by publishing additional information. Information asymmetries can be a serious problem that if occurs it may disturb the functioning of the capital market leading even to their partial or complete breakdown (Akerlof, 1970). The evidence (e.g. Lang and Lundholm, 1996; Botosan, 1997, Hail, 2002, and so forth) suggests that additional disclosure benefits companies as it increases transparency and reduces information asymmetries, thus reducing cost of capital. A reduction in information asymmetries makes investors more confident to trade at a fair price, leading to higher stock liquidity (Diamond and Verrecchia, 1991; Walker, 1995). Companies may benefit from making additional disclosure so as to send signals to the market that there is no need for new requirements (signaling theory) and/or reduce the chance of more detailed and perhaps more costly requirements being introduced by accounting regulators (political cost theory).

However, companies' directors are sometimes reluctant to disclose additional disclosure because competitors may make strategic use of information disclosed to their advantage (Edwards and Smith, 1996; Linsley and Shrives, 2005; Tsakumis et al., 2006). This may lead to the imposition of a proprietary cost, hence putting a company at a competitive disadvantage and affecting the company negatively. Thus, a firm has to trade off the positive and negative affects of voluntary disclosure.

2.3 Previous Studies

Recently there has been substantial growth in the research attention being devoted to risk disclosure in companies' annual reports. Although corporate financial and environmental disclosures have been developing for a number of decades, recent evidence (e.g., Stanton and Stanton, 2002; and Beattie, 2005) found little research related to annual report risk disclosure. This increase in attention for risk disclosure can be demonstrated by the increased focus being applied by government and regulators, professional accounting bodies, stock markets, signifying its importance. The studies examining risk disclosure started to evolve (e.g., Abraham and Cox, 2007; Linsley and Shrives, 2006; Woods and Reber, 2003). These studies investigate different issues, covered different data sets; and applied different studies samples.

For example, Beretta and Bozolan (2004) proposed a framework of risk communication and applied it on a sample of non-financial companies listed in the ordinary market on the Italian Stock Exchange. Woods and Reber (2003) carried a pilot study on twelve companies to compare disclosure between UK and Germany.

The present study is a longitudinal study, and distinguishes itself from previous studies as it seeks to determine whether companies' annual report disclosure has enhanced over the years under study in response to recent changes, development in financial reporting, and other regulatory pressure.

3 Hypotheses Development

Given the debate on risk disclosure, the main impetus of this research study was to determine whether risk disclosure in annual reports of UK firms has improved over the period under study in response to development and regulatory changes that occurred lately. Any increase in risk disclosure would be seen as evidence confirm the effectiveness of recent efforts at corporate governance reforms "(Solomon et al., 2000) and recommendations made by professional bodies in increasing disclosure and reducing information asymmetry. Patten (1992) and Deegan et al. (2000) provide examples of studies where the volume of environmental disclosure was shown to respond to the increase exposure to criticisms experienced after a particular event. Thus we would expect risk disclosure to have increased over the years, and operationalized this expectation in the following first research Hypothesis:

H₁: The level of risk disclosure has significantly increased over time in response to recent corporate reporting development and regulatory change.

Prior research suggests that several factors (e.g., financial factors, non-financial factors, and social responsibility factors) may determine firm's disclosure policy. In this research we investigated the effect of size, leverage, industry, and listing.

Prior evidence (e.g., Hossain et al., 1994, Meek et al., 1995; Raffournier, 1995; Depoers, 2000) suggests there may be a positive relation between disclosure and size. The proportion of outside capital tends to be higher for larger companies and agency theory suggests agency costs (monitoring costs) increase with the amount of outside capital. Thus larger firms may have greater incentives to disclose more information in order to reduce agency cost, hence reduce information asymmetries between managers and shareholders. The demand for information by analysts could be greater on larger firms (Hossain et al., 1994). These argument leads to the second hypothesis:

H₂: The extent of disclosure is positively related to firm size.

Industry can also be an important factor in explaining corporate disclosure (Beretta and Bozzolan, 2004). This variable, type of industry, may have the potential to influence the amount and nature of information disclosed by companies. The influence of industry has been proposed by political cost and signalling theory (Inchausti, 1997). Beretta and Bozzolan (2004) suggest that company risk profile is deeply influenced by the technological and market constraints exerted by the competitive industrial environment on the business models. Cooke (1992) found that Japanese manufacturing companies disclose more information than non-manufacturing firms. This leads us to the second hypothesis:

H₃: The extent of disclosure is positively related to industry.

Listing factors have been proposed by many studies in accounting disclosure as an important factor in explaining disclosure practices. Listing in foreign stock exchanges gives firms an opportunity to raise capital (perhaps at a lower cost) in the foreign capital markets. Firms may want to increase their disclosure, perhaps in order to create or maintain strong demand for their securities. Another reason that has been put forward for additional disclosure is that the foreign stock markets may require extra disclosure. This lead to the fourth hypothesis:

H₄: The extent of disclosure is positively related to listing.

It has been proposed that capital structure of a firm is related to agency cost (Jensen and Meckling, 1976). Agency costs are higher in highly leveraged firms (i.e., more debt in the capital structures) because a large

proportion of debt allows greater potential wealth transfers from debtholders to shareholders (Jensen and Meckling, 1976). Thus agency theory predicts that corporate disclosure is expected to increase with leverage. However, the empirical evidence on this hypothesis is contradictory. For example, Hossain et al., (1994); Meek et al. (1995), and Raffournier (1995) found no significant relation with disclosure whilst others (e.g., Malone et al., 1993) found a positive association. These arguments lead to the following fifth hypothesis.

H₅: The extent of disclosure is positively related to leverage.

4 Sample Selection and Research Methods

The analysis is based on companies' annual report excluding financial statements and notes. 156 annual reports prepared by 52 companies over the study period, 1998-2004 were analysed. The 52 companies were classified into eight industry categories, based on LSE classification: namely, resources (RE), basic industries (BI), general industries (GI), non-cyclical consumer goods (NCCG), cyclical services (CS), non cyclical services (NCS), utilities (UT), and information technology (IT). To make comparison easier, Information technology is consolidated with CS because it has only one constituent company, Sage. Thus, this reduced industry categories to seven categories. Table 1 presents the sample companies.

Content analysis (e.g., Neu et al., 1998; Milne and Adler, 1999; Campbell, 2004; Linsley and Shrivess, 2006) is used to determine the themes of risk disclosure. Content analysis can be used to note either the presence or the absence of a theme in written broadcast or other verbal material. It is useful method as it allows for disclosure to be systematically classified and compared and also useful in comparing trends (Milne and Adler, 1999). In content analysis, different counting measures can be used which include 'word', 'sentence', 'page' and 'number of lines'. In this study, 'sentence' was used as it is more likely to provide data which are complete, reliable and meaningful (Milne and Adler, 1999).

Content analysis requires the researcher to design and implement a coding scheme involving a number of stages and steps (e.g., Weber, 1985; Wolfe, 1991). The implementation of these stages requires the researcher to determine the followings: the research question (e.g., measuring disclosure); the codable document (annual report); the coding unit (e.g., sentence), disclosure categories (environmental, operational; strategic risk disclosure); the coding mode. In addition, the researcher needs to assess reliability of coding, and finally, the coded information is interpreted.

Following previous studies (e.g., Linsley and Shrivess, 2006; Wood and Reber, 2003), an analysis instrument (checklist) was designed and utilised so disclosure can be classified according to the time frame (i.e., past, non-time, and future-related); type of news (i.e., bad (negative), good (positive), and neutral news); and form of disclosure (i.e., quantitative .v. qualitative). Table 3 shows an example of the analysis of disclosures.

5 Results

Recently, there has been an increase in demand on risk disclosure information. Companies were put under pressure to enhance their risk disclosure. This is the background against which the result of this study

Table 1 Sample selection

Categories	Number of observant
Resources (RE)	4
Basic Industries (BI)	5
General Industries (GI)	2
Non-cyclical consumer goods (NCCG)	9
Cyclical services and information technology (CS&IT)	22
Non-cyclical service (NCS)	4
Utilities (UT)	6
Total	52

should be interpreted. This study sets out to examine how companies have responded to this growing pressure and demand. Table 2 presents the results of content analysis. The table shows that all companies in the sample make some risk disclosures. The average number of sentences of risk disclosure has steadily increased across the period under study, rising from 50.23 in 1998 to 64.94 in 2001 and then to 93.5 in 2004. The table also shows that average disclosure attributed to each theme/category (i.e., environmental risk, operational risk and strategic risk) has also increased. This provides evidence that there is an upward trend in the average amount of risk disclosure being published by the sample of companies over the period from 1998-2004. Average disclosure, regardless of form (quantitative or qualitative), time-scale and type of news (good, bad or neutral) all increased overall. However, quantitative disclosure decreased slightly between 1998 and 2001 and bad news disclosure slightly decreased between 2001 and 2004. The results show that operational risks disclosure dominates, reflecting its growing importance. Items under this theme/category such as risk management policies and internal control, liquidity and cash flow risk, environment and health and safety risk and others; received higher ranks than items covered under other categories.

Table 3 provides an in-depth and detailed analysis of risk disclosure sentence characteristics. The table exhibits a clear analysis of the form, time and type of the information disclosed.

The results show that companies reveal both qualitative and quantitative disclosure. However, qualitative disclosures dominate. The companies also publish 'past', 'non-time', and 'future' disclosure with non-time disclosure found to be dominating. In terms of news type, it was noted that companies disclose little 'bad news' information in comparison 'good' and 'neutral' disclosure.

Table 2 The overall trend in risk reporting (figures are related to the most recent year, year 2004)

		N	Year 1998	Year 2001	Year 2004
Disclosure characteristics	Code		Average disclosure	Average disclosure	Average disclosure
1. Quantity	Total average risk disclosure	52	50.23	64.94	93.5
2. Content	Environment risk disclosure	52	7.64	12.43	19.28
	Operational risk disclosure	52	34.12	41.5	60.64
	Strategic risk disclosure	52	8.47	11.01	13.58
3. Form of disclosure	Qualitative disclosure	52	43.40	58.36	84.10
	Quantitative disclosure	52	6.83	6.58	9.40
4. Time-scale	Past news	52	7.11	8.42	10.96
	Non-time	52	26.43	38.25	52.21
	Future	52	16.70	18.25	30.32
5. Type of news	Good news	52	20.97	29.84	43.98
	Bad news	52	2.63	3.39	3.37
	Neutral news	52	26.63	31.71	46.15

Table 3 Results of Risk disclosure

Mean Disclosure	Qualitative			Qualitative			Qualitative			Qualitative			Qualitative			Qualitative			Total
	Past			Past			Non-time			Non-time			Future			Future			
	Qualitative			Qualitative			Qualitative			Qualitative			Qualitative			Qualitative			
	Past			Past			Non-time			Non-time			Future			Future			
	Good	Bad	Neu	Good	Bad	Neu	Good	Bad	Neu	Good	Bad	Neu	Good	Bad	Neu	Good	Bad	Neu	
Year 1998	2.1	1.29	0.98	0.59	0.58	1.58	14.48	0.1	10.78	0.28	0	0.79	3.33	0.63	9.727	0.2	0.04	2.78	50.23
Year 2001	2.14	1.68	0.86	0.75	0.52	2.47	24.89	0.06	12.03	0.13	0	1.16	1.77	1.06	13.88	0.15	0.08	1.32	64.94
Year 2004	3.01	1.31	1.28	1.51	0.71	3.14	36.39	0.1	14.07	0.35	0.04	1.527	2.57	1.02	24.35	0.15	0.19	2.04	93.5

6 Hypotheses Testing

To test hypothesis 1, A Wilcoxon signed rank test was conducted to test the significant differences in average disclosure between the years. The results indicate that there are significant differences between years 1998-2001; 1998-2004, and 2001-2004. The $z = -4.538$; -6.071 ; and -5.711 respectively ($p = 0.000$). A t-test, was also conducted for the same paired samples. Again, the results show significant differences between the years confirming the Wilcoxon test results; t statistics (-5.404 ; -7.941 ; and -6.088) respectively ($p = 0.000$).

Table 4 gives the descriptive statistics for dependent (disclosure score) and independent continuous variables (e.g., size, leverage) included in the study. Figures are related to the most recent year, year 2004. To examine the correlations between disclosure scores and continuous variables, Pearson product moment correlations were computed.

The Results indicate that there is no strong evidence that risk disclosure score is related to either size or leverage, contrary to the predictions of agency theory. Deloitte (2006) found that the quality of disclosure on markets and external environment did not vary by size of company. Previous evidence (Malone et al., 1993; Meek et al. 1995) tested the association between disclosure and leverage variable is contradictory.

In an attempt to examine the relationship between the type of industry and risk disclosure level the sample companies were initially categorized into seven industrial groups as explained above and shown in table 1. Based on this classification, a One-way ANOVA test was carried out on most recent year results, year 2004. Table 5 presents the results, which show significant differences between industries.

Following this categorisation, the companies were also further divided into dichotomous groups based on whether they are industrial or non-industrial companies. The dichotomous approach was also used to classify companies in the sample according to whether or not companies have a US listing in addition to their UK listing. Having developed this classification, two statistical tests were performed, a Student's t test and a Mann-Whitney U test. The results of the Student's t test presented in table 6 (panel A) suggest that there is a significant difference in risk disclosure score ($p < 0.000$) between the two groups of industries. As hypothesized, firms belonging to industrial sectors are disclosing more information than those whose belong to non-industrial sectors. The Mann – Whitey U test yields a Z statistic -4.27 ($p < 0.000$), which supports the results of the Student's t test.

With regard to the US dual listing variable, the Student's t test results (panel B) show that there is a statistically significant difference ($p < 0.000$) in disclosure scores between the two groups. It appears that firms with US dual listing have a greater propensity to disclose information than other companies. The Mann-Whitney U test yields a Z statistic of $-0.3.89$ ($p < 0.000$), which supports the results of Student's t test.

Table 4 Descriptive statistics and univariate analysis between disclosure and the independent variables

	Min	Max	Mean	SD	Pearson Correlation
Total risk disclosure score	28.00	275.00	93.50	54.12	N/A
Size	6.57	11.98	8.46	1.23	0.084
Leverage	1.50	527.18	131.15	106.99	0.066

Total disclosure is the firm's total disclosure on three categories: namely, strategic, operational and environmental risk disclosures. Size is log of turnover. Leverage is total debt to total assets.

Table 5 Risk disclosure by industry type and ANOVA test results

Industry	RE	BI	NCCG	CS&IT	NCS	UT	GI	ANOVA	
	Mean	Mean	Mean	Mean	Mean	Mean	Mean	F	Signif.
Total risk disclosure score (2004)	121.75	177.6	111.77	60.27	92.25	97.16	101.5	5.94	0.000

Table 6 Univariate analysis between disclosure score and industry variable

Panel (A)	Industrial (26)	Non-industrial (26)	Student's t test	2 – tailed probability
Mean disclosure score	121.80	65.19	-4.398	0.000
Std. Deviation	58.97	28.82		
Mann-Whitney Z= -4.027; 2 – tailed probability 0.000				
Panel (B)	US dual listing (28)	Non US dual list- ing (24)	Student's t test	2 – tailed probability
Mean disclosure	124.08	67.28	-4.193	0.000
Std. Deviation	60.41	29.65		
Mann-Whitney Z= -3.89; 2 – tailed probability 0.000				

7 Discussion of Disclosure Results

In the basis of the comparison made over the period from 1998-2004, we observed what was expected that there is a general increase in the level of information disclosed on risk disclosure. Yet still relatively little detailed disclosure is provided. Much of the disclosure appears to be linked to general risk causes where companies report that they are subject to/expose to/face various types of risks which may affect their operations (future/qualitative/neutral disclosure). Much of the disclosure was also on non-time/qualitative/neutral and non-time/qualitative/good disclosure. The disclosures comprise those disclosures linked to internal control systems, risk management policies, corporate social responsibility risk (include health and safety and environment risk) and others. We have seen more reporting on risk factors, general statement of risk management policy, and control system than detailed reporting on what would be the impact of such risk. Some of the disclosure related to internal control is mandated under Turnbull committee, which requires a description the system in place to identify, evaluate and manage risk. A general feature appears to be the desire of companies directors to provide bad news as well as good and neutral news although the level of bad news disclosure remains low. Another feature appears in the willingness of directors to disclose information related to the future. Evidence suggests (e.g., Solomon et al., 2000) that investors demand more information related to the future. Linsley and shrives (2000) suggest that the provision of forward looking information would be especially useful to investors. However, this feature holds as most of the disclosures related to the future are neutral news and qualitative. The results show little information linked to future quantitative disclosure and future bad news disclosure. Evidence suggests (e.g., Skinner, 1994) company directors withhold negative information (especially those related to the future) when they feel this is necessary to avoid excessive legal costs or reputation concerns. Nonetheless, understandably there are difficulties associated with forecasting the future and quantifying risk due for example to data availability and subjectivity in measurement. For example, one company writes “as a result of uncertainties, including the current economic conditions, it is considered difficult to forecast the level of losses for joint ventures and associates in 2002” (Reuters Group plc, annual report, 2001). This is an example of future bad news disclosure, as it deals exclusively with losses but it lacks any quantitative information. Other typical risk disclosure examples are presented in table 7. There are also some circumstances where directors are reluctant to release forward-looking risk information without safe harbour protection and when disclosure are deemed too commercially sensitive (Linsley and Shrides, 2005).

The results show that listing and industry variables are significantly related to the level of risk disclosure. This was expected as there are additional disclosure requirements for companies quoted on US stock markets. For the industry variable, industrial companies were found to disclose more than other companies. This may be due to certain industries being subject to more complex regulations than others or the result of a herd instinct or bandwagon effect where companies increase their level of disclosure in order to avoid the appearance of failing to meet the standards set by other similar companies.

Table 7 Typical examples of risk disclosure

Risk disclosure example	Risk category	Sentence characteristics
Wolseley has its principal operations in North America and Europe and therefore subject to specific risks of conducting business in these regions. (Wolseley 2004/05 annual report)	Strategic risk	Non-time/ qualitative/ neutral
Hedging operation are subject to internal control including review by an internal audit function. (Antogfasta 2004/05 annual report)	Operational risk	Non-time/qualita- tive/good
Our lost time injury frequency improved by 15% in 2004, reducing to 0.6 injuries per million man hours worked. (BG 2004 annual report)	Operational risk	Past/ quantitative/ good
Management does not anticipate that the dispute with certain issues over their declination of coverage of macrotextured product liability claims will be resolved during 2005. Consequently, it is expected that settlements with patients will not reimbursed by insurers and that this will have an adverse impact on cash flow of a proximately £40m during 2005. (Smith and Nephew 2004/05 annual report)	Operational risk	Future/quantitative/ bad

8 Conclusion

This study was carried out to examine how companies responded to recent regulatory developments and other pressures on corporate reporting. The further examined the relationship between risk disclosure in annual report and four company variables include company size, industry type, listing status, and leverage.

Although disclosure level, reflecting the effect of regulation, found to be increased over the years. However the analysis indicates that there are so many bland statements being disclosed by companies. Thus, although investors consider risk disclosure desirable, they may be concerned that risk disclosure may not fully enable them assess company risk profiles. Accordingly, the usefulness of the risk information disclosed by companies remains a question for future research.

The study has a number of limitations. Our sample was extracted from the FTSE 100 companies so the sample choice should be consider when the conclusion are drawn. A further research study could extend the sample to include medium-sized and smaller companies. The second limitation is that our analysis is restricted to annual reports only. Previous evidence suggests that managers' disclosure of good news forecasts information and bad news (e.g., Skinner, 1994) disclosure promptly to avoid litigation costs. It is acknowledged that companies communicate with stakeholders through other channels, such as interim reports, preliminary announcements, and the internet. Future research could examine these other forms of information disclosure.

Finally, in view of the potential role of risk disclosure in reducing information asymmetries and thereby increasing investors' confidence, it would be valuable to conduct further research to establish whether there is any negative correlation between risk disclosure and cost of capital reflecting this improvement in investor sentiment.

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