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Evaluation of Corporate Integrated Reporting in South Africa Post King III Release

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A research report submitted in partial

fulfilment of the requirements for the

degree of

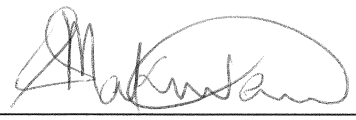
Master of Commerce

University of the Witwatersrand

Ethics Clearance No. CACCN/1004

Declaration

I declare that this dissertation is my own work. It is submitted in fulfilment of the requirements for the degree of Masters in Commerce in the University of the Witwatersrand, Johannesburg. It has not been submitted before for any degree or examination in any other university.



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Evaluation of Corporate Integrated Reporting in South Africa Post King III Release

Abstract

Following the release of the King III report on Corporate Governance for South Africa in March 2010, South African companies are expected to embrace the concept of integrated reporting in which they are required to report on their strategies, corporate governance, risk management processes, financial performance and sustainability. More importantly, companies need to show how these components of integrated reporting are linked to one another, so that stakeholders can make informed decisions about their current performance as well as their ability to create and sustain value in the future. The purpose of this report by is to determine whether the level of reporting by South African listed companies has improved subsequent to the release of the King III report. The findings of this study reveal improvements in this regard. However, there is still a need for further improvement in the level of reporting by South African listed companies in order to achieve the objective of integrated reporting.

Keywords: Integrated reporting, strategies, corporate governance, risk management, sustainability and financial performance.

TABLE OF CONTENTS

		Page No.
Chapter 1	**Introduction**	**1**
1.1	Background to the problem statement	**1**
1.2	Problem statement	**3**
1.3	Research question	**3**
1.4	Relevance of the study	**3**
1.5	Limitations of the study	**3**
1.6	Organisation of the report	**4**
Chapter 2	**Literature Review**	**5**
2.1	Integrated reporting	5
2.2	Financial performance	7
2.3	Corporate governance	9
2.3.1	Background to corporate governance	9
2.3.2	King III report on corporate governance	12
2.3.3	Boards and directors	13
2.3.4	Board committees	17
2.3.5	Audit committees	19
2.3.6	Risk management	21
2.3.7	Remuneration policy	22
2.3.8	Internal audit function	23
2.3.9	Information technology	24
2.3.10	Compliance function	26
2.3.11	Stakeholder relationships	26
2.3.12	Comparison between King III and the regulations	28
2.3.13	Key changes from King II to King III	30
2.4	Sustainability Considerations	35
2.4.1	Background to sustainability	35
2.4.2	The Rio Declaration	37
2.4.3	Millennium Development Goals	38
2.4.4	Global Reporting Initiative	40
2.4.5	Economic sustainability	41
2.4.6	Social sustainability	42
2.4.7	Environmental sustainability	44
2.4.8	Sustainability accounting	47
2.4.9	Audit assurance of sustainability impacts	47

2.5 Corporate failures 48

Chapter 3 Research Methodology 50

3.1 Research design 50
3.1.1 Nature of the study 50
3.1.2 Pilot study 50

3.2 Research approach 51

3.3 Population size and sample 52
3.3.1 Population and sample 52
3.3.2 Sample selection 52

3.4 Research instruments 53

3.5 Data analysis and interpretation 54
3.5.1 Score allocation 54
3.5.2 Harmonisation of information 54
3.5.3 Statistical methods used in the study 55

Chapter 4 Research Results 57

4.1 Comparison between the mean scores of the current year and the base year per individual main categories 57

4.2 Comparison between the integrated annual reports and the annual reports 58

4.3 Indicators showing significant improvement in the level of reporting 59

4.4 Level of reporting by individual sectors 61

4.5 Level of reporting by existing indicators as per the King II report 62

4.6 Level of reporting by new indicators as per the King III report 63

4.7 Harmonisation between components of integrated reporting 64

Chapter 5 Conclusion and Recommendations 66

References 68

Appendices
Appendix A – Research Indicators **77**
Appendix B – Mean Differences per Individual Categories **82**

Chapter 1 Introduction

1.1 Background to the problem

The collapse of companies in the recent past coupled with the global financial crisis has led many stakeholders to question the ability of the existing financial reporting system to provide relevant information for decision making (SAIRC Discussion Paper, 2011; Steyn and de Beer, 2011). The vacuum caused by the inefficiencies of the corporate financial reporting system, which mainly focuses on historical information, has prompted the world to look for a new system that would provide information about the future prospects of companies (SAIRC Discussion Paper, 2011). Although in its infancy in terms of development (Eccles and Armbrester, 2011), integrated reporting promises to be an ideal system to provide answers for decision making.

Integrated reporting is a new concept not only in South Africa but all over the world. It is defined in the King Report on Governance for South Africa 2009 (King III) as a "holistic and integrated representation of the company's performance in terms of both its finance and its sustainability" (IOD, 2009). In terms of this definition, companies are encouraged to assess their performance holistically in that they have to consider various aspects that are essential to the success of their businesses. These aspects include (1) the adoption of good and effective strategies; (2) implementation of good corporate governance practices; (3) application of effective risk management processes; (4) assessment of the company's financial performance; and (5) promotion of sustainability which includes addressing economic, social and environmental issues (IOD, 2009; SAIRC Discussion Paper, 2011).

In South Africa, integrated reporting was first conceptualised by King III (IOD, 2009) which dedicated a separate chapter to this topic. Given the importance of this concept, the South African Integrated Reporting Committee (SAIRC) was formed in May 2010 (Accountancy SA, December 2011) to specifically look at the integrated reporting issues at length, which culminated in the publication of the Discussion Paper on Integrated Reporting in January 2011 (SAIRC Discussion Paper, 2011). On the international front, the International Integrated Reporting Committee (IIRC) was formed. This committee engaged in an extensive consultative process with different organisations and individuals around the world such as the United Nations, the Global Reporting Initiative (GRI), accountants, lawyers, and environmentalists (IIRC Discussion Paper, 2011). The *Accountancy SA* journal (December 2011) believes that the IIRC used some of the recommendations of the South African

Discussion Paper (2011) in the preparation of its own Discussion Paper issued in September 2011.

According to the IIRC Discussion Paper (2011:6), integrated reporting is intended to "bring together the material information about the company's strategy, governance, performance and prospects in a way that reflects the commercial, social and environmental context within which it operates. It provides a clear and concise representation of how the company creates value, now and in the future. It combines the most material elements of information currently reported in separate reporting strands such as financial, management commentary, governance, remuneration and sustainability in a coherent manner".

While integrated reporting is a new concept globally, South Africa has taken the lead by urging its companies to embrace the concept in their reporting (South Africa.Info, January 2011). South African listed companies are required, in terms of the Johannesburg Stock Exchange listing requirements (JSE, 2011), to comply with the King III (IOD, 2009) guidelines with effect from 1 March 2010. In the event that they fail to comply with the guidelines, companies need to provide reasons for failing to do so (JSE, 2011). In contrast, there are no mandatory requirements in many other countries other than that companies operating in other countries can follow the guidelines provided in the IIRC Discussion Paper (2011). These guidelines are at the development stage and the IIRC hopes to issue an Exposure Draft in 2012 after it has solicited the views from various organisations and the public (IIRC Discussion Paper, 2011).

Given that South African listed companies are required in terms of the JSE listing requirements (JSE, 2011) to adopt integrated reporting, the purpose of this report is to evaluate the extent to which the level of reporting by South African listed companies has improved since the introduction of integrated reporting in King III (IOD, 2009), effective from 1 March 2010. This report draws its strength from the concepts of integrated reporting, which include strategies, risk management, corporate governance, financial performance and sustainability and which will be further explored in the literature review. Since the concepts are discussed in detail in King III (IOD, 2009) and the Global Reporting Initiative (GRI, 2011), this report uses the research indicators drawn from these articles to answer the research question in section 1.3.

1.2 Problem statement

South African listed companies should embrace the concept of integrated reporting whereby they are expected to report on their current and future strategies, corporate governance issues, risk management processes, financial performance as well as sustainability matters (IOD, 2009; SAIRC Discussion Paper, 2011). More importantly, companies need to show interdependencies between these components to enable the stakeholders to make informed decisions about their current performance as well as their future prospects (IOD, 2009; SAIRC Discussion Paper, 2011).

1.3 Research question

To what extent has the level of reporting by South African listed companies improved in the current year (2010/2011) relative to the base year (2009) since the introduction of King III which became effective on 1 March 2010?

1.4 Relevance of the study

As a new concept in South Africa and globally, integrated reporting will be a subject of debate for many years to come. It is therefore hoped that the findings of this study will stimulate interest among researchers to conduct more research in this area. Such future research will help to establish whether companies will be able to cope with the new trends and developments in integrated reporting, especially after the interest shown by the International Integrated Reporting Committee (IIRC).

1.5 Limitations of the study

The first limitation of this study is that it is based only on South African listed companies and the fact that the research was limited to the analysis of the annual reports of these companies retrieved from the McGregor database.

The second limitation relates to the fact that, although financial performance is one of the important concepts of integrated reporting, no attempt was made to include the financial performance indicators in the same way as in the other concepts of integrated reporting. This decision was based on the fact that companies use different financial indicators where

the selection of financial indicators from one group of companies may not necessarily address the financial performance of the other group of companies.

The third limitation is that the score allocation, discussed in the research methodology, is based on the researcher's judgement and did not attempt to determine the quality of the information presented in the annual reports as to do so would involve an element of subjectivity.

1.6 Organisation of the report

The remainder of the report is organised as follows. Chapter 2 reviews the literature relevant to strategy, risk, corporate governance, financial performance, sustainability and integrated reporting. Chapter 3 deals with the research methodology adopted in this study. Chapter 4 provides the research results. Chapter 5 concludes the discussion and makes recommendations for future research.

Appendix A provides a list of research indicators used in this report. Appendix B illustrates by means of graphs improvement in the level of reporting per main individual categories. The term "company" is used in this report to refer primarily to listed companies but can also be used to refer to any other organisation or entity, depending on the wording of the sentence or paragraph. In other instances, the term "organisation" is used to refer to a company.

Chapter 2 Literature Review

2.1 Integrated reporting

Integrated reporting provides a platform for companies to report on their financial and non-financial performance in a single report (Eccles and Armbrester, 2011) in terms of providing an overview of their operations, as well as showing the connection between the various concepts of integrated reporting, namely, strategies, corporate governance, risks, financial performance and sustainability (IOD, 2009; SAIRC Discussion Paper, 2011; IIRC Discussion Paper, 2011). Such analysis will enable stakeholders to assess the companies' performance holistically in terms of their ability to create and sustain value in the short, medium and long term (SAIRC Discussion Paper, 2011; South Africa.Info, January 2011).

Mervyn King, Chairman of the South African Integrated Reporting Committee, regards integrated reporting as a fundamental shift and a significant evolution in corporate reporting practice (SAIRC Discussion Paper, 2011). This shift has been necessitated by the inability of companies to present coordinated information in their reports. In the past, companies tended to produce sustainability reports the contents of which differed vastly from the economic reality of their business and prepared in a manner that would make it difficult to ascertain any business value (SAIRC Discussion Paper, 2011; Carte, 2011). Because they were prepared in a disjointed manner, they could not be connected with the information presented in the other parts of the report such as that on financial performance (SAIRC Discussion Paper, 2011).

Transparency, accountability and leadership are at the heart of integrated reporting, the important pillars of corporate governance (SAIRC Discussion Paper, 2011). Driven by these values, companies will be able to select material and relevant information that would be of interest to the stakeholders. To achieve transparency and accountability in their reporting, King III (IOD, 2009) recommends that companies should strike a balance in terms of reporting both positive and negative information rather than providing a one-sided view. Reporting in this manner would make it easier for management and stakeholders to identify those risks that are a threat to the company and the risks that can be turned into the opportunities (IOD, 2009). In the selection process, companies should be guided by the principle of substance over form to ensure that information is selected on the basis of its economic merits rather than its legal form (IOD, 2009).

In essence, integrated reporting builds on the guidelines of the Management Commentary, a Practice Statement issued by the International Accounting Standards Board in December 2010 (IASB, 2010). The Management Commentary (IASB, 2010) provides guidelines on the issues that management of the company should consider when presenting its commentary in support of the financial information. Management is required to explain the key trends and factors that are likely to affect the company's future performance and also needs to discuss the risks facing the company, the strategies designed to manage such risks and to provide assurance on the effectiveness of those strategies. This information is intended to supplement and complement information provided in the financial statements (IASB, 2010).

Building on the Management Commentary (IASB, 2010), integrated reporting emphasises the need to improve communication between companies and the capital markets (Matthews, 2011). According to Matthews (2011), better communication will allow companies to sell their future strategies effectively and inform the markets about the major risks facing their business, as well as the measures intended to address those risks. The benefits of doing so is that the buy-in by the markets will enable companies to obtain capital at a reasonable cost as well as enhancing their reputation, an important element giving them a licence to operate (Matthews, 2011). In this regard, Eccles and Armbrester (2011) give an example of the Danish health-care company, Novo Nordisk, whose share price has increased significantly over the past years as a result of its ability to provide information of interest to the stakeholders.

Once implemented, integrated reporting will, according to Bray (2011), bring a number of benefits to companies including: (1) efficient allocation of capital; (2) streamlined reporting processes; (3) reduced reporting costs owing to the reduction in volume of information; and (4) enhanced organisational clarity in terms of business strategy and business models. In addition, the IIRC Discussion Paper (2011) believes that integrated reporting can help (1) to align the interests of companies with those of stakeholders, thus contributing to long-lasting relationships; (2) improve relations between companies and their employees which, in the long term, can help with the attraction and retention of skilful and talented employees; and (3) companies to learn to use scarce resources for the benefit of the environment which, in turn, helps companies to save costs, thereby improving their profitability.

Bray (2011) further notes the benefits that companies embracing integrated reporting can derive by automating their information. For example, companies can make use of their websites effectively to store relevant information that can be visited by stakeholders on a regular basis. Eccles and Armbrester (2011) point out that some companies use their

websites also as a means to gain competitive advantage. For example, the Danish company, Novo Nordisk, provides the names and contact details of relevant officials within the company. Doing so helps stakeholders seeking clarity on various issues to contact the relevant person. Novo Nordisk also requests stakeholders to provide it with feedback on the use of its website. This feedback has helped the company to improve its service (Eccles and Armbrester, 2011).

No company can profess to meet all the requirements of integrated reporting at this stage since it is still a new concept to be developed further in the coming years. At the time of conducting this study, the IIRC has solicited the views from various organisations and the public on its Discussion Paper with a view to publishing an Exposure Draft in 2012 (IIRC Discussion Paper, 2011). The IIRC is mindful of the fact that integrated reporting is not an end in itself but a journey that has just started, the objectives of which will be met in the future (Heaps, 2010; Wandrag and Hanks, 2010).

2.2 Financial performance

While the concept of integrated reporting is important for the 21st century company, it should be noted that the primary objective of conducting business by any company is to make sustainable profit in the triple context of finance, society and the environment (IOD, 2009) for the wellbeing of its shareholders, employees and other stakeholders. Without this objective, there is no incentive to do business. Hence, companies from time to time use different means of determining whether their objective of making sustainable profit is still on course for the purposes of taking appropriate action if necessary.

As a means to achieve this objective, a company would have to ensure that a system of internal controls is in place to safeguard its assets (IOD, 2009). Effective controls will ensure, among other things, that (1) the system is able to capture all the transactions that have taken place during the period; (2) budgets are prepared on an annual basis and that forecasts are prepared between the periods to update those budgets; and (3) measures have been implemented whereby the budgets and the forecasts are compared to the actual results and corrective action is taken where major deviations have been identified.

Many companies also make use of management accounts to summarise all the activities which took place during a particular period. These management accounts are usually presented in the form of summarised or detailed balance sheets, income statements and cash flow statements. This information is also supplemented by detailed schedules such as

the revenue analyses by division and other ratio analyses. Given the importance of ratios in facilitating the analysis of the company's performance, many companies tend to split them into profitability, liquidity and solvency ratios. If the ratios are also presented for external reporting purposes, stakeholders select those ratios which will meet their needs. For example, shareholders and analysts might be interested in the profitability ratios, whereas money lenders might be concerned with the liquidity and solvency of the company.

Although companies can use different approaches in presenting financial information for internal reporting purposes, the accounting standards prescribe the manner in which such information should be presented for external reporting purposes. This is done to ensure, among other things, comparability of information between companies, as well as consistency from one period to another in line with the requirements of the Conceptual Framework for Reporting issued by the International Accounting Standards Board (IASB, 2010). To avoid using different approaches for internal and external purposes, many companies have adopted the accounting standards even in the preparation of their management accounts for internal reporting purposes. Such a process makes it easier for companies to present the same information, with minor changes, for external reporting purposes. However, to ensure the credibility of the financial information, external auditors need to verify such information.

Since companies cater for a wide range of stakeholders with different interests, the presentation of the company's financial performance alone is not enough (IIRC Discussion Paper, 2011; IOD, 2009). Bray (2011) provides a number of reasons why financial performance alone is not adequate. First, the key features of financial performance are often buried in voluminous financial statements, which makes it difficult for analysts and stakeholders to analyse the information. Second, the commentary by the company's executives sometimes lacks the necessary detail to facilitate comparison of information among its operations or with other companies. Third, information on financial performance is backward looking which does not help stakeholders with information for decision making.

This, therefore, calls for the financial performance to be supplemented with other information to enable the stakeholders to obtain a holistic view of the company's performance in order to assess its ability to create and sustain value. This would entail considering the company's strategies and assessing their effectiveness when viewed in conjunction with risk management practices, corporate governance and sustainability. Corporate governance is discussed in the next section.

2.3 Corporate governance

2.3.1 Background to corporate governance

Many problems facing companies today stem from weak relations that exist between the stakeholders and those in charge of running the companies, often resulting from a lack of adequate information to help stakeholders to make informed decisions (SAIRC Discussion Paper, 2011). As noted in the preceding section, these problems are exacerbated by tendency of managers to cover mainly the companies' financial performance in their reports at the expense of other information of interest to stakeholders. This situation clearly points to the gap that exists between the managers and the stakeholders in terms of what managers believe is in the interests of stakeholders versus what stakeholders (including shareholders) actually need to influence their decision making (Jensen and Meckling, 1976).

The concept of corporate governance is deeply rooted in agency theory, that is, the separation of ownership from control of the company (Jensen and Meckling, 1976). In terms of agency theory, the owners (principals) of the company do not have the power to control the company as such control has been shifted to the managers (agents). The problem that could arise out of this situation is that managers can abuse their powers in that they can decide to release or withhold information at their own discretion (Rossouw et al., 2002; Jensen and Meckling, 1976). Therefore, corporate governance is an essential tool for bridging that gap, thereby ensuring that managers provide relevant information to the owners and other stakeholders (Rossouw et al., 2002).

Corporate governance is based on the values of transparency, accountability, responsibility and fairness (Shkolnikov and Wilson, 2009; IOD, 2009; GRI, 2011; Gray, 2001). These values require managers to provide material and relevant information of interest to the company's stakeholders (IOD, 2009; GRI, 2011). Once the company decides to adopt the values, it should ensure that they are entrenched across all its operations (IOD, 2009). Transparency requires companies to provide relevant information in a clear and concise manner to enable stakeholders to make an informed analysis of the companies' performance (IOD, 2009; Gray, 2001). Accountability requires managers to justify their decisions and actions to the stakeholders (IOD, 2009). With regard to responsibility, managers are required to assume responsibility for the assets and actions of the company (IOD, 2009). In the case of fairness, companies are expected to treat all stakeholders equally, including the minority shareholders (Shkolnikov and Wilson, 2009).

Strong leadership is required to ensure the implementation of corporate governance values across the company. Hence, King III (IOD, 2009) entrusts this responsibility to the board of directors. As a focal point of leadership, directors are required to ensure that the values of transparency, accountability, responsibility and fairness, together with the ethical code of conduct, are respected by everyone within the organisation (IOD, 2009). Otherwise, appropriate action should be taken against those who fail to comply with the values and ethics (Belikov, 2009).

Corporate governance is an important pillar not only for companies but also for government institutions given the role that governments play in creating job opportunities and in paving the way for economic growth (Shkolnikov and Wilson, 2009). However, prior research shows that governments, especially in the emerging markets, tend to lag behind the developed countries in terms of good corporate governance principles (Shkolnikov and Wilson, 2009). According to Armstrong (2009), corporate governance remains a challenge in emerging markets owing to the following: (1) the state-owned companies tend to dominate the economy and that alone makes it difficult for a country to attract local and foreign investment; (2) enforcement of corporate governance principles is not consistent and often depends on the political will; and (3) the judicial system is usually not equipped to deal effectively with commercial crimes. This is in contrast to developed countries with well-developed capital markets and judicial systems that are able to handle crime and other related matters (Armstrong, 2009).

To compound the problem in emerging markets, these markets are often plagued by corruption, bribery, political patronage and officials who want to advance their own interests at the expense of social development (Shkolnikov and Wilson, 2009). Corruption and other bad governance practices by governments and companies have negative consequences for the economy, and often give rise to poverty in their countries as the money earmarked for projects, job creation and development ends up in the hands of corrupt individuals (Shkolnikov and Wilson, 2009). The actions of these corrupt individuals eventually lead to situations where people resort to informal businesses mainly for survival purposes rather than helping to stimulate economic growth (Shkolnikov and Wilson, 2009).

Bad practices tend to stifle economic growth as investors are not prepared to invest their capital in governments and companies where there is a lack of transparency and where corruption is rife (Shkolnikov and Wilson, 2009). For Pierce (2009), corruption is the enemy of efficiency as it creates problems beyond the legal repercussions and ethical issues by

constantly increasing the cost of doing business. In the process of creating sound systems of corporate culture, corruption will become unacceptable behaviour (Pierce, 2009).

Based on the Russian experience, Belikov (2009) observes that additional problems in emerging markets such as Russia stem from ownership which is concentrated in the hands of the founders of companies who retain large control over their companies, irrespective of whether these companies are listed or not. The board of directors of these companies seem to play only an advisory role rather than being involved in decision making, while the controlling shareholders and company founders are the only ones to decide on strategic issues (Belikov, 2009). When this happens, Belikov (2009) is of the view that the board plays the role of merely rubber stamping a silent agreement that exists between itself and the controlling shareholders to maintain the status quo.

Despite weak institutions in emerging markets, Armstrong (2009) believes that corporate governance can still be practised as long as an atmosphere conducive to attracting investment can be created. The behaviour of societies and companies can help to attract the required investment as there are investors who are willing to invest their capital in risky countries as long as the atmosphere is conducive to doing so (Armstrong, 2009). He gives the example of South Africa, which managed to turn things around in terms of attracting investment as a result of a strong culture of corporate governance exhibited by both private and state-owned companies. The South African government, regulatory agencies, the accountancy profession and the Johannesburg Stock Exchange (JSE) all played an important role in this regard, motivated largely by the desire to apply international standards in South Africa (Malherbe and Segal, 2001).

In emerging markets, corporate governance can be a useful tool for fighting corruption (Belikov, 2009; Bernal, 2009). According to Belikov (2009), independent internal audit functions can play an important role in this regard, thus ensuring the transparency of information within organisations. Those who transgress the governance rules should be brought to book and appropriate action taken against them (Belikov, 2009). If corporate governance practices are implemented carefully, they can help expand confidence in the private sector while promoting local and foreign investment (Armstrong, 2009). Coupled with strong law enforcement capability, corporate governance can also help to create job opportunities and stimulate economic growth (Shkolnikov and Wilson, 2009; Armstrong, 2009). Bernal (2009) believes that corporate governance is the first thing to be considered by every organisation before deciding to do business (Bernal, 2009). While this section lays

the foundation for corporate governance, the next section on King III (IOD, 2009) covers the components of corporate governance in detail.

2.3.2 King III report on corporate governance

South Africa made its first real attempt to tackle corporate governance problems with the formation of the King Committee, chaired by Mervyn King, by the Institute of Directors of Southern Africa in 1992 (IOD, 1994). This committee followed in the footsteps of the Cadbury Committee set up in the United Kingdom to look into similar corporate governance issues. However, the mandate of the King Committee was broader than that of the Cadbury Committee in that it also dealt with a wide range of issues peculiar to South Africa such as the transformation and affirmative action necessitated by changes in the South African political system.

After an extensive consultative process with various organisations and individuals, the King Committee released its first report on corporate governance for South Africa in November 1994 (King I). Following changes in the labour laws, accounting standards and other business dimensions subsequent to King I, a second set of guidelines was issued by the King Committee in March 2002 (King II). Later, a third set was published in September 2009 but became effective in March 2010 (King III). King III (IOD, 2009) came into being following amendments to the Companies Act of 2008 relating to audit committees but, more importantly, to address new issues such as integrated reporting and to provide more guidance on issues relating to information technology, compliance and stakeholder relationships.

King III (IOD, 2009) deals extensively with the following components of corporate governance: (1) Ethical Leadership and Corporate Citizenship; (2) Boards and Directors; (3) Audit Committees; (4) the Governance of Risk; (5) the Governance of Information Technology; (6) Compliance with Laws, Rules, Codes and Standards; (7) Internal Audit; (8) Governing Stakeholder Relationships; and (9) Integrated Reporting and Disclosure. This report covers each of these components in the following sections. Comparisons between King III (IOD, 2009) and other regulatory disciplines, as well as key changes from King II (IOD, 2002) to King III (IOD, 2009), are addressed towards the end of this section. The discussion of the components of corporate governance is important given that corporate governance is one of the integrated reporting concepts, and also to give perspective to the research indicators on corporate governance used in this report

King III (IOD, 2009) encourages companies to conduct their business in a manner that would guarantee their sustainability in the future by addressing the economic, social and environmental impacts dealt with extensively in the Global Reporting Initiative (GRI, 2011). In one of his presentations, Mervyn King, gave the following example to illustrate the importance of sustainability:

> *"Financial statements are not fit for purpose if they only represent the financial aspects of the company. For example, a company that has much waste that is polluting a nearby lake and reflects large profits will not continue in business compared to a company that does not manufacture and dump waste into a lake."*

2.3.3 Boards and directors

The board of directors is a focal point of leadership and is entrusted with the responsibility for formulating the company's strategies (IOD, 2009). In addition, the board has to ensure that everyone in the organisation abides by the code of ethical conduct (IOD, 2009). This section looks at the role of leadership, ethics and strategies in ensuring the success of the company.

(a) Leadership

According to King III (IOD, 2009), the prerequisite for integrated reporting is good corporate governance, which is characterised by the board of directors being the focal point for effective and responsible leadership. For example, responsible directors will take care of the needs of all the stakeholders affected by and affecting the company before making an informed decision. They are accountable to the company and through the company to its shareholders and other stakeholders to ensure that the company's resources are utilised in the best interests of the company (Deloitte, 2009).

However, leadership is more like a calling and certain qualities are required in an individual in order for him/her to be able to lead the organisation. Leadership is defined in the *Oxford dictionary* (2000) as (1) "the state or position of being a leader"; (2) "the ability to be a leader or the qualities a good leader should have". While there are many other definitions of leadership, Clarke (2011:1) has an interesting one where he defines leadership as "a process by which a person influences others to accomplish an objective and directs the organisation in a way that makes it more cohesive and coherent". A similar definition is used by Jago (1982).

Influence is a key word since a leader needs to be influential before others can take him/her seriously (Maxwell, 2011). He/she also needs to be trustworthy and to be a man or woman of integrity to enable him/her to exert influence upon those who follow him/her (Reh, 2011; The Teal Trust, 2011). In addition, a leader should possess certain traits such as (1) being positive all the time in order to motivate his/her subordinates; (2) communicating effectively to enable his/her subordinates to carry out the instructions; (3) understanding the differences that make his/her subordinates unique; and (4) utilising the unique skills possessed by his/her subordinates for the benefit of the company (Reh, 2011).

Contrary to popular belief that leaders are born, researchers such as Keuzes and Posner (1995) believe that leadership can be taught and learnt by anyone who is interested in becoming a leader. As long as the individual believes and is passionate about becoming a leader, they argue it is possible. As a good leader with a passion, drive and commitment, he/she will overcome any obstacle standing in his/her way (Keuzes and Posner, 1995). When facing obstacles, he/she takes the lead instead of bossing his/her subordinates around.

A leader also needs to adapt to different situations. If one method is not working, he/she should use another one (Clarke, 2011). For example, he/she may have to use a different approach to supervise a new and inexperienced employee to that he/she normally uses to supervise a long-serving and experienced employee. Such approaches are required so as to motivate all the employees under his/her supervision to reach their potential as well as enabling them to achieve the desired goals (Clarke (2011).

King III (IOD, 2009) emphasises the importance of good and responsible leadership in companies to enable them to achieve their strategic goals. Hence, the directors and those in senior positions within companies are called upon to examine themselves to see whether they possess the necessary leadership skills. If they do, their companies will prosper, but if they do not, their companies are bound to fail.

The following words by Reh (2011:1) are encouraging and most appropriate for those who aspire to become leaders of tomorrow irrespective of their area of specialisation:

> *"Leaders dream dreams. They refuse to let anyone or anything get in the way of achieving those dreams. They are realistic, but unrelenting. They are polite, but insistent.*

They constantly and consistently drive forward towards their goal. You can be a leader. You will be - when it matters enough to you."

(b) Ethical considerations

Responsible leadership goes hand in hand with ethics which are an important element of corporate governance (IOD, 2009). According to King III (IOD, 2009), ethics are the reason why companies exist in the first place. They incorporate the concept of trust which is recognised as the foundation of value creation in companies (DiPiazza and Eccles, 2002). Coupled with trust and honesty, ethics also enhance the company's reputation which is viewed by Bebbington et al. (2008) as an important intangible asset.

The collapse of big companies such as Enron (Ivaschenko, 2004) resulted in a loss of confidence in capital markets by the public. It was unthinkable that a company of its size in terms of market capitalisation should declare bankruptcy. Investigations showed that its collapse was due to a lack of the important values that guarantee the very existence of companies, namely, transparency, accountability and integrity (DiPiazza and Eccles, 2002; Gray, 2001). Directors of Enron entered into structured financial transactions which resulted in legal and accounting conclusions to keep the financing off balance sheet. This led to a distorted picture for equity holders as to the total economic value of the company.

After the collapse of Enron, faith in companies as the creators of value decreased significantly, yet faith is important for the proper functioning of the capital markets (DiPiazza and Eccles, 2002). DiPiazza and Eccles (2002) point out that trust can only be restored by entrenching a culture of transparency, accountability and integrity in the company. These values have been discussed in section 2.3.1 but it is worth mentioning that they are supported by the principle of materiality which ensures that only issues of significance and interest to stakeholders are addressed by companies (GRI, 2011).

(c) Strategies

A strategy is defined in the *Oxford dictionary* (2000) as a plan that is intended to achieve a particular purpose. To be able to achieve a purpose requires a company to know where it is going in terms of its short-, medium- and long-term plans (Hay and Williamson, 1997). Hay and Williamson (1997) liken a strategy to a tower with many levels. In a tower, all one can see is an elegant building showing coherence in terms of different levels and boundaries from the bottom to the top. Hay and Williamson (1997) state that a strategy should show a

similar coherence to a building; they believe that a strategy should be an integral part of the company's day-to-day activities.

Companies use different strategies to achieve various objectives such as strategies intended to introduce new products in the market and those intended to grow their businesses. Irrespective of the strategy being pursued, the bottom line is that it should be a strategy that is of benefit to the business. Solving Management Consultants (1988), which specialise in mergers and acquisitions, give an account of companies which diversify their businesses for survival purposes rather than to pursue genuine strategies for the benefit of their businesses. According to Porter (1996), many companies which resort to mergers and acquisitions are often desperate for strategies to give them a competitive advantage in the market.

To ensure the effectiveness of strategies, employees must also be involved in the process through the proper channels of communication, as they are expected to implement them (Hay and Williamson, 1997). In a survey conducted by Higgins and Diffenbach (1989), the researchers found that even the security analysts appreciate a well-communicated corporate strategy. They also found that companies are willing to communicate their corporate strategy for different reasons. For example, firms intending to turn their businesses around or planning major diversification of their operations benefit the most from selling their strategies to the markets.

A strategy should not be confused with operational effectiveness (Porter, 1996). While both are essential to achieve the company's objectives, Porter (1996) points out that they work in different ways. Operational effectiveness refers to the ability of a company to perform similar activities better than its rivals. For example, in the case of an airline company, it can strive to obtain a competitive edge in the market by purchasing an aircraft that runs faster than those of its rivals. On the other hand, a strategy refers to the ability of a company to position itself in the market by performing similar activities in a different way, such as targeting particular customers in the market compared to the mass customers targeted by its rivals (Porter, 1996).

While companies use different strategies to compete with one another, it is important for them to adapt to different situations and to formulate strategies that would sustain them in the market (Porter, 1996). Porter (1996) calls them "fit strategies", which basically involve a number of activities that complement one another in a chain. These therefore make it difficult for the rivals to imitate them (Porter, 1996). The successful implementation of the fit

strategies makes it possible for the company to have a sustainable business to meet its long-term objectives (Porter, 1996).

The strategies finally adopted by the company are usually a product of a consultative process between internal and/or external parties. At the board or top management level, companies allocate time in a year for strategic sessions. Before adopting a strategy, companies normally use different approaches such as scenarios (Hadfield, 1991). Scenarios have proven to be useful at Shell to the extent that Hadfields (1991) recommends them for use by other companies. The benefits of using scenarios, according to Hadfield (1991), are that (1) they facilitate the generation of ideas; (2) they provide a framework for developing strategies at different levels of the organisation; and (3) in a decentralised organisation, they equip managers with tools for dealing with a crisis situation. If applied correctly, scenarios can be used by individual operations to come up with business strategies that would enable them to compete effectively within the industries in which they operate (Harrington, 1985).

Strategies do not operate in a vacuum but require strong and effective leadership (IOD, 2009). Companies benefit in terms of direction and success from strong leaders who are not afraid of making choices (Porter, 1996). It is a pity though that, in other companies, leadership has degenerated into performing activities which, in essence, promote only operational effectiveness (referred to above) rather than formulating effective strategies (Porter, 1996).

2.3.4 Board committees

The board committees, consisting of audit, remuneration and nomination committees, play an important role in the corporate governance structures of companies (IOD, 2009; Pass, 2002; Kesner, 1988). In South Africa, the risk committee has also joined the ranks of influential committees after the recommendation of King III (IOD, 2009), given the significance of the risk management processes in companies which demands a dedicated committee rather than the delegation of risk management to other committees which already have other commitments.

The role of the nomination committee is to assist the board in appointing suitable candidates to serve on the board (IOD, 2009). While shareholders are ultimately responsible for approving the appointment of directors, the nomination committee plays a significant role in determining and verifying the quality of individuals to be appointed to the board (Vafeas, 1999). In terms of King III (IOD, 2009), this would include the verification of the candidate's

qualifications, skills and experience. The nomination committee may engage the services of the external agencies in screening, interviewing and selecting potential candidates for board positions. Companies with nomination committees benefit from having to appoint suitable individuals without the interference of a dominant CEO (Vafea, 1999). Ultimately, it is the board, and not the nomination committee, which makes the final decision about the appointment of suitable candidates (IOD, 2009; Vafea, 1999).

The remuneration committee plays a critical role in determining the remuneration of executive directors (IOD, 2009). In the United Kingdom, the Greenbury report (1995) makes recommendations about how the remuneration of executive directors should be determined. This followed public and shareholders' concerns about high salaries and other incentives paid to executive directors which often lacked transparency and proper disclosure in the financial reports. The Greenbury report (1995) recommends the delegation of the responsibility for determining executive remuneration to the remuneration committee. This committee should prepare its annual report to be tabled before the shareholders, disclosing details of executive remuneration (IOD, 2009; Greenbury report, 1995).

With regard to the risk committee, King III (IOD, 2009) recommends the appointment of a risk committee consisting of both executive and non executive directors. Once a risk committee has been formed, it should be responsible for setting up a risk management policy, which will detail the risk management objectives, the risk approach and philosophy (IOD, 2009). The risk management policy should be distributed to the entire organisation for implementation by its operations (IOD, 2009).

With regard to audit committees, their duties are not only prescribed by King III (IOD, 2009) but are also mandated by the South African Companies Act (Companies Act, 2008). In terms of the Act (Companies Act, 2008), the audit committee is responsible for (1) appointing the external auditor of the company, determining their independence and determining the non-audit services to be allocated to the external auditor; (2) performing an oversight function in terms of the internal and financial controls of the company; and (3) preparing a report to the board and shareholders detailing how it carried out their functions, whether it is satisfied with the auditor's independence and whether it is satisfied with the internal financial controls.

The balance and composition of the board and its committees is vital for the board's effectiveness, which makes the role of the nomination committee more important in terms of selecting suitable candidates for board positions (Ruigrok et al., 2006). Other than the suitability of individuals, the question that arises is what other attributes the board or its

committees should possess to ensure their effectiveness. One of the attributes is the ability of the company to strike a balance between the executive and non executive directors. Some jurisdictions require the board to be comprised of a majority of the non executive directors such as in the United States (Kesner, 1988). In South Africa, King III (IOD, 2009) recommends that, in addition to the majority being non executive, the directors should also be independent. In fact, King III goes to the extent of recommending that the chairmen of these committees should be independent.

King III (IOD, 2009) makes it clear that the board committees are important for the effectiveness of the board, but at the same time the board is not exonerated from its responsibilities of taking the final decisions on any matter presented before it by its committees. The significance of audit committees, risk management practices and remuneration policy makes it imperative for these structures to be discussed separately in the following sections.

2.3.5 Audit committees

Companies in many countries around world have formed audit committees to bridge the gap that exists between external auditors and management, especially when it comes to crucial decisions that may affect the business. Qualified or adverse audit opinions tend to have a negative effect on the perceptions that investors and other stakeholders might have about the company (Choi and Jeter, 1992). Research shows that an adverse opinion has a negative impact on the company's share price (Choi and Jeter, 1992), which is one of the reasons why management would persuade the auditor not to issue such an opinion in the first place. Unfortunately, the auditor faces a litigation and reputation risk, especially when the other stakeholders incur financial losses which could have been avoided had the auditor issued an appropriate audit opinion (Lys and Watts, 1994; Krishnan and Krishnan, 1997).

The recent financial crisis and collapse of big companies (Ivaschenko, 2004) have given rise to a call for the middleman to help take crucial decisions in the best interests of all stakeholders. While companies are not compelled to form audit committees especially in developing countries, other jurisdictions have made it mandatory for companies to do so. For example, Bronson et al. (2009) report that, in the United States, the Sarbanes-Oxley Act of 2002 (SOX, 2002) requires all listed companies to have independent audit committees. South Africa has a similar requirement in the form of a law enacted in 2008 (Companies, 2008) where the shareholders of listed companies are required to appoint audit committees.

While the duties of audit committees vary from one country to another, the South African Companies Act (Companies Act, 2008) details the functions of the audit committees. These functions are also in line with the King III guidelines (IOD, 2009) and with the Johannesburg Stock Exchange (JSE, 2011) listing requirements. Some of the key functions include (1) oversight over the preparation of the integrated reports; (2) oversight over the internal audit functions; (3) assessment of the expertise of the finance function as well as that of the financial director; (4) assessment of the independence of the external auditor; (5) approval of additional services to be allocated to the external auditor; and (6) reporting to the board and to the shareholders on how the audit committee has conducted its duties during the year.

While the formation of audit committees is plausible, the question that often arises is how effective these committees are given that, in some countries, the requirement to institute such committees has been in existence for quite some time. In research conducted by Bronson et al. (2009) to determine the level of effectiveness by audit committees that are completely independent, their finding confirms the benefit of having 100% independent audit committees. They believe their finding will provide support for the SOX (2002) requirement of the completely independent audit committees. A number of other studies have also confirmed the connection between completely independent audit committees and the high level of effectiveness of such committees (Carcello and Neal, 2003; Abbott et al., 2003, Beddard et al., 2004 and Lee et al., 2004). However, DeFond and Francis (2006) find very little connection in this regard.

The benefits of having an effective audit committee include better financial reporting and reduction in the cases of fraud (Rupley et al., 2011). Where the audit committees have oversight over financial reporting, the effectiveness of such committees is enhanced (Kalbers and Fogarty, 1993). An interesting study by Archambeault and DeZoort (2001) finds that cases of fraud are likely in companies where audit committees hold fewer meetings than is required. Audit committees are likely to support the external auditors to issue a qualified/adverse opinion if it is necessary to do so. Companies with audit committees are likely to have strong internal control systems (Hoitash et. al., 2009) and are not likely to experience the abnormal accruals (Klein, 2002) often associated with earnings management.

The benefits of having effective audit committees come at a price as companies would have to pay more in audit fees than they would if they had no such committees. Abbott et al. (2003) examine the association between audit fees and audit committee independence, their financial expertise and frequency of audit committee meetings. They find that there is indeed

such an association. Their study confirms the notion that qualified and experienced members of audit committees usually demand higher levels of dedication and commitment from auditors to contribute to a successful audit.

2.3.6 Risk management

Risk management is an essential component of corporate governance (Bhimani, 2009; Sarens et al., 2009) to help companies to identify threats in their business for the purposes of taking appropriate action before the damage is caused. However, there has been a tendency for companies to view risk management from one perspective: as a tool to eliminate the threats facing their businesses (IOD, 2009).

Risk is defined as the “taking of risk for a reward” (IOD, 2009), which is a reminder to companies to understand that the act of conducting business implies that risks cannot be entirely eliminated but companies should constantly make efforts to identify those risks which can be turned into opportunities (Olsson, 2007). This can be achieved by the application of integrated risk management processes which facilitate the identification of both risks and opportunities at the same time (van Wyk, et al., 2008).

Risk management entails the identification, analysis, mitigation, monitoring and reporting of risks (Van Wyk et al., 2008). It also entails risk evaluation and quantification where this is practicable (IOD, 2009). Risk management cannot be done haphazardly but requires coordinated efforts and plans by various operations within the organisation. The risk management policy should set the tone for risk management and also indicate how risk management supports the company’s strategy (IOD, 2009).

Risk management entails taking calculated risks and setting levels of risk tolerance (IOD, 2009). The limits set for risk tolerance should be reviewed on a regular basis, especially during periods of uncertainty and unfavourable changes in the business environment (IOD, 2009). While taking calculated risk is desirable, O'Connor et al. (2008) warn against too much focus on risks which could prevent companies from deriving benefits from major breakthroughs in their businesses.

Monitoring and evaluation of the risk management processes on a regular basis is an important aspect in determining whether or not the company is on course to achieve its objectives (IOD, 2009; McCarty and Power, 2000). While risk management is the responsibility of the board, King III (IOD, 2009) recommends the delegation of this function to

the risk committee comprised of both executive and non executive directors. Involvement of executive directors is important given their intimate knowledge of the business.

2.3.7 Remuneration policy

The remuneration of executive directors of listed companies has attracted a wide range of stakeholders and the public (Bender, 2003). The interest stems from the dissatisfaction with the high salaries and other incentives paid to executive directors and other senior executives of companies, according to the Greenbury report (1995). In addition, there is a lack of transparency about how companies arrive at high levels of remuneration for executives, which is even paid by companies that are not performing well in terms of share prices (Jensen et al., 2004).

Prior research has over the years monitored salaries and incentives paid to senior executives even before formal remuneration policies were set up by companies. Much of this research comes from the United States which, among other things, monitors the effect of salaries and incentives on earnings and share prices. For example, Healy (1985) studies the effect of bonus schemes for executives on companies' earnings. He finds that managers manipulate accounting procedures to maximise their bonus rewards. Many other studies conducted subsequent to Healy's (1985) confirm his findings overall (Holthausen et al., 1995; Guidry et al., 1999).

Other studies have been conducted to determine what motivates some companies to pay higher salaries than others. For example, in the research conducted to determine the level of salaries in growth companies compared to those in non-growth companies, Gaver and Gaver (1995) find that companies with abundant investment opportunities pay higher salaries than non-growth companies. They believe that companies with growth opportunities pay higher salaries to keep their managers motivated so that they can continue doing well. They also find that growth companies pay variable salaries and incentives compared to non-growth companies which tend to pay fixed salaries.

Plantenga and Remery (2006) report the levels of compensations that differ by gender based on their study conducted among 30 European countries. Their study follows a call on European member countries by the European Commission in 2003 to formulate a strategy aimed at reducing the gap that existed in salaries between men and women in their countries. Plantenga and Remery (2006) find that the gender pay gap is higher for married employees and significantly lower for singles. Further, the gender pay gap is lower for public

sector employees than those in the private sector. Plantenga and Remery (2006) argue that differences in the gender pay gap are a function of individuals' age, qualifications and experience.

The above research serves to demonstrate that there is no one solution to the remuneration problem because of different approaches followed by companies. However, the guidelines such as those contained in King III (IOD, 2009) and the Greenbury report (1995) serve to guide companies about the best practice to be followed in order to restore the faith of the public in companies. Both King III and the Greenbury report emphasise the need for transparency and proper disclosure of information on remuneration in the companies' annual reports. Similar disclosure is favoured by Ferrarini (2008) in his summary of executive remuneration in some European countries. Over and above directors' remuneration, King III recommends the disclosure of remuneration of companies' top three executives other than the executive directors.

2.3.8 Internal audit function

Many companies are beginning to realise the importance of the internal audit function as a service that adds value to their business (Sarens et al., 2009). Its primary function is to monitor controls instituted by management to safeguard the companies' assets (Sen and Wallace, 1991). Sen and Wallace (1991) state that internal auditors, while monitoring controls, need to pay special attention to any deviations from the prescribed controls, and can be assisted in this regard by working in collaboration with the external auditors.

Internal auditors are seen as an important component to strengthen the corporate governance structures within the company (Sarens et al., 2009; Abdolmohammadi and Boss, 2010). The complexity of today's information technology has also contributed to the role that internal audit has to play within the organisation (Abdolmohammadi and Boss, 2010). Its functions are varied depending on the nature, size and complexity of the business which, in terms of King III (IOD, 2009), include (1) assessing the effectiveness of the system of internal control; (2) providing assurance on the effectiveness of risk management; (3) adopting a risk-based approach in the planning stage as well as in carrying out its audit functions; and (4) attending audit committee meetings for the purposes of giving feedback to this committee about its findings.

Research has been conducted in the area of internal audit function to determine its effectiveness (Sarens et al., 2009). Using a Belgian case study, Sarens et al. (2009) find that

the internal audit function is still relevant as a first point of reference by the audit committee in establishing whether or not the internal control system is effective. They point out that the internal control system is regarded by the audit committee as the most important pillar of the business which deserves priority. Therefore, its effectiveness gives the audit committee comfort about other areas of the business such as risk management. According to Sarens et al. (2009), internal auditors play a very important role in this regard owing to their familiarity with the company's operations as well as their closeness to the people in charge of those operations.

In terms of King III (IOD, 2009), internal auditors should report directly to the audit committee to enhance the independence of their function. However, a study conducted by Norman et al. (2010) finds that internal auditors generally prefer to report to management rather than the audit committee, as they find the audit committee somewhat intimidating especially when dealing with issues involving high levels of risk in the company. Norman et al. (2010) attribute the internal auditors' fear to the tougher stance that the audit committee is likely to take in addressing risk issues than when they are addressed by management. Norman et al. (2010) are surprised with their finding given that the public and the investor protection agencies would prefer the audit committee to be the direct line of reporting by the internal auditors.

The question that arises is how best the internal audit function should be carried out, in view of companies having it either in-house or outsourced. In South Africa, many large companies have in-house internal audit functions and a few have outsourced it. However, the opposite is true for small-to-medium size companies where outsourcing is believed to be a viable option. There is no straight answer to this question, which leads Rittenberg and Covaleski (2001) to recommend more research to be conducted in this area to determine the benefits of in-house service versus outsourcing.

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2.3.9 Information technology

As in the rest of the world, companies in South Africa have embraced information technology in their businesses. The question that arises is to what extent companies have used information technology to achieve their strategic objectives. Bakos and Treacy (1986) find that, in general, information technology is underutilised by corporate managers, which then undermines its ability to help companies to gain competitive advantage in the markets in which they operate. Part of this underutilisation stems from the fact that some senior managers within organisations are ignorant of the potential use of information technology

and in other cases managers are resistant to change (Bakos and Treacy, 1986). Reich and Benbasat (1996) also find that managers tend to struggle to link information technology goals with company strategies. As a result, these managers fail to see the pay-offs that can be derived from investment in information technology (Tallon et al., 2000).

As noted by Tallon et al. (2000), by virtue of its seniority within the organisation, the board is an ideal place to take decisions around information technology, including whether or not to increase its capacity. However, ignorance by some members of the board about the capabilities of information technology prevents companies from taking advantage of the opportunities they could have used to give them an upper hand over their rivals.

Nevertheless, there are a number of benefits that can be derived from the effective use of information technology. First, Borghoff and Pareschi (1997) explain the role that knowledge management can play in empowering the company with knowledge in the short and in the long term. Information technology can be used to store knowledge that can be retrieved for present and future use. The second benefit gained from the use of information technology is in the area of process innovation, where the company's processes can be reengineered for the purpose of gaining a competitive edge in the market (Davenport, 1993).

It is for this reason that King III (IOD, 2009) places the responsibility for making important decisions around information technology with the board. Although King II (IOD, 2002) considered information technology, it did not provide details as to how companies could use it to their benefit. On the other hand, King III (IOD, 2009) devotes a new chapter to this topic to highlight its importance in the 21st century and its ability to help companies gain a competitive advantage over their rivals.

King III (IOD, 2009) is mindful of the fact that companies, in the past, neglected information technology because it would not even feature on the board's agenda. This situation created an imbalance between what companies originally planned for information technology and the actual results derived from its implementation. Many companies would realise at a later stage that the information technology implemented in their businesses did not complement their strategic goals. By that time, it would be too late as they would have to incur additional costs to supplement the existing systems.

By placing the responsibility for managing information technology strategies with the board, King III (IOD, 2009) intends to protect companies from, among other things, incurring unnecessary costs. It follows that major decisions about significant changes to information

technology should not take place unless approved by the board. To help the board in its duties, King III recommends the appointment of a chief information officer (CIO) who should be suitably qualified and have the necessary experience to carry out his/her duties. King III also urges companies to make information technology an integral part of their businesses so that it can play a role in supporting, growing and sustaining their business.

2.3.10 Compliance function

Compliance is basically an extension of the corporate governance values where companies undertake to comply with the laws of the country and any other codes, rules or standards without being forced to do so (IOD, 2009). When complying with the laws, King III (IOD, 2009) urges companies to do so not only for the obligations that they create but also for the rights and protection that they provide. It is submitted that when companies comply with the law, they should be aware of the business opportunities that such compliance could bring. For example, submitting tax returns on time could afford a company an opportunity to obtain a tax clearance certificate which can be used during the tender process.

King III (IOD, 2009) requires companies to manage compliance risk, which is described as the risk of damage resulting from non-compliance with the law. Edwards and Wolfe (2004:216) provides a similar description of compliance risk where, in relation to banks, it is described as “any action or activity within a bank which impacts negatively upon its integrity or reputation due to non compliance with laws, codes of conduct, standards of good practice or regulation”. Kingbury (1998), on the other hand, relates the concept of compliance to the principles of law in that compliance is seen as conformity to the legal rules.

King III (IOD, 2009) places the responsibility to ensure that all compliance issues are adhered to by everyone within the company with the board. King III further recommends a compliance function to be set up to assist the board in its functions. It may be headed up by a compliance officer who reports functionally to the chief executive.

2.3.11 Stakeholder relationships

A company has a nexus of stakeholders that affect or are affected by its operations, including employees, shareholders, suppliers, customers, unions and the government (IOD, 2009; GRI, 2011). Therefore, it is important for the company to create and maintain strong relationships with its stakeholders to enable it to continue in business (Smudde and Courtright, 2011). The company begins by identifying and understanding what the

stakeholders' interests are and ensuring that such interests are adequately addressed (IOD, 2009; GRI, 2011).

The process of identifying the stakeholders' interest may involve an integrated and a collective approach (Wilson et al., 2010), also referred to as a stakeholder-inclusivity approach (GRI, 2011; IOD, 2009). Different engagement processes can be used (GRI, 2011) such as (1) conducting road shows where directors and senior management meet different stakeholders; (2) encouraging stakeholders to post their views on the company's website; (3) using internal brochures to communicate with its employees; (4) using various forums to communicate with customers and suppliers; and (5) using general meetings and annual general meetings to communicate with shareholders and analysts.

The GRI (2011) recommends the documentation of the stakeholder engagement process. Such a process should be based on systematic and generally accepted principles. The overall approach should be sufficiently effective to ensure that the information needs of the stakeholders are understood. The company should also document the approach it followed (1) to define the stakeholders it engaged with; (2) to state how and when it engaged with those stakeholders; and (3) to report on how its engagement with the stakeholders has influenced the contents of its report.

The above processes are important for the company in order to meet the reasonable expectations and interests of its stakeholders (GRI, 2011). The results of the company's engagement act as a reference point in taking decisions on how the report should be prepared, taking into account the scope, boundaries, materiality, completeness, accuracy and reliability of the information (GRI, 2011). In doing so, the company should bear in mind that not all the stakeholders' needs will be covered (GRI, 2011); nevertheless, the company is required to balance their expectations. Hence, the principle of materiality comes into play in deciding on the issues to be reported on.

The concept of stakeholder relationships is topical in South Africa and is addressed extensively in King III (IOD, 2009). Among other things, King III requires companies to strive to achieve a balance between its various stakeholder groupings in the best interests of the company. King III recommends that differences between the parties should be resolved through a mediation process to avoid the delays and costs that occur if the matter is taken to court. Therefore companies are urged to give due consideration to stakeholder relationships (IOD, 2009). Experience shows that failure to adequately address stakeholder needs can

have unintended consequences similar to the high-profile corporate failures (Boesso and Kumar, 2009) witnessed in the United States and the United Kingdom.

2.3.12 Comparison between King III and the regulations

Comparisons have been made between King III (IOD, 2009) and the Companies Act No.71 of 2008 (Companies Act, 2008), as well as between King III and the Johannesburg Stock Exchange (JSE, 2011) listing requirements. The rationale behind the comparisons has been the fact that, despite the specific sections of the Companies Act and the JSE listing requirements having been inspired by the King III guidelines, there are similarities and differences in the corporate governance issues covered by these documents.

The important section in the Companies Act for the purposes of this research is section 94 dealing with the appointment of the audit committees of public companies and state-owned companies. Section 94 came into being largely because of the recommendations of King II (IOD, 2002), requiring companies to appoint audit committees to be instrumental in the implementation of good corporate governance practices. After the Companies Act had incorporated the recommendations of King II, it became imperative for the King Committee to align its recommendations with those of the Companies Act because of some recommendations being made mandatory by the Act; hence, the publication of King III which became effective in March 2010.

Section 94 (Companies Act, 2008) requires the company to appoint members of the audit committee at its annual general meeting. The committee must be comprised of at least three members who have the necessary qualifications and experience to undertake duties expected of the audit committee. The Act makes it clear that such members must be non executive directors who are not full-time employees or involved in the day-to-day management of the company's business as the executive directors do. In addition, they must not be material suppliers or customers of the company which, in the eyes of a reasonable third party, may be viewed as having compromised their objectivity. The difference between the Companies Act and King III is that the Companies Act requires the members to be non executive directors, whereas King III takes it a step further by recommending that they should also be independent.

Both the Companies Act and King III deal with the duties of the audit committee, but the Companies Act specifically requires them, among other things, (1) to appoint a registered auditor, determine their fees, determine and approve the non-audit services to be provided

by such auditor and satisfy themselves that the auditor is independent; (2) to prepare a report to be included in the annual financial statements stating how they carried out their functions as the audit committee and whether they are satisfied with the auditor's independence; and (3) to make submissions to the board on any matter concerning the company's policies, financial controls, records and any other reports.

With regard to the JSE (JSE, 2011) listing requirements, it should be noted that the JSE has always been at the forefront of corporate governance by encouraging companies listed on its stock exchange to incorporate the recommendations of the King reports, namely, King I (IOD, 1994), King II (IOD, 2002) and King III (IOD, 2009). The recent amendments to the JSE (JSE, 2011) listing requirements require listed companies to comply with the recommendations or to explain their reasons for not complying. Of the recent listing requirements issued in April 2011 (JSE, 2011), paragraphs 3.84 and 8.63(a) are important, dealing with corporate governance issues. Although the entire paragraphs will not be discussed in this report, it is nevertheless worthwhile to briefly highlight some of their important parts.

Paragraph 3.84 (JSE, 2011) requires companies to have a policy in place concerning the appointment of directors to the board. The appointment process must be formal and transparent and be a matter for the board as a whole with the assistance, where possible, of a nomination committee. At board level, no one director should have the power to dictate to the board. The positions of the chief executive and the chairman must be separate with the chairman being an independent non executive director. If not independent, the board must appoint a lead independent non executive director. It is submitted that these requirements are similar to King III (IOD, 2009).

Paragraph 3.84 (JSE, 2011), similar to King III and the Companies Act, also requires companies to appoint an audit committee and a remuneration committee. While recommended, the appointment of risk and nomination committees is not compulsory. A brief curriculum vitae (CV) of each director standing for election or re-election should accompany the notice of the general meeting or annual general meeting. Each director must be categorised as executive, non executive or independent using the King III guidelines. Lastly, the company is required to appoint a full-time financial director or to provide motivation on why he/she is part time. The audit committee must issue a report as to whether or not it is satisfied with the financial director's expertise.

On the other hand, paragraph 8.63(a) (JSE, 2011) requires a company to give a narrative statement of how it has applied the principles set out in King III. In this statement, the company must provide adequate explanation that would enable the users to make informed decisions. In addition, the company is required to state the extent of its compliance with King III, specifying whether or not it has complied with the recommendations during the reporting period. If not having complied, the company should provide the reasons for not doing so.

As expected, the JSE (JSE, 2011) listing requirements, as far as corporate governance issues are concerned, are in line with the Companies Act (Companies Act, 2008) and the King III (IOD, 2009) guidelines. The difference between the JSE requirements and the King III guidelines is that some of the JSE requirements are compulsory whereas, in the case of King III, they are not. King III follows a softer approach given that its guidelines cover a wide range of entities compared to the JSE which only covers the listed companies.

2.3.13 Key changes from King II to King III

This section discusses the key changes from King II (IOD, 2002) to King III (IOD, 2009). The discussion is important given the use of the King III research indicators, together with the GRI (2011) research indicators, in this report in determining whether the level of reporting by South African listed companies has improved since the release of King III in March 2010. The articles from Deloitte (2009), Ernst & Young (2009), KPMG (2009) and PricewaterhouseCoopers (2009) have been instrumental in highlighting the differences. As a result, they have been used, in conjunction with King II and King III, in compiling the following key changes.

(a) Ethical leadership and corporate citizenship

King II deals with ethical considerations as an important foundation for good corporate governance, but King III extends its coverage in a separate chapter. King III highlights the importance of effective leadership in ensuring that ethics are entrenched across every sphere of a company's business and that they are adhered to by everyone within the organisation from senior management down to its lower grades.

(b) Appointment of the board of directors

One of the cornerstones of good corporate governance is the appointment of directors to lead the organisation. In most companies, the board is comprised of executive and non

executive directors. Though all directors are equal in terms of their mandate as directors, their functions tend vary as only the executive directors are responsible for the day-to-day management of the company.

Both King II and King III require the board to be comprised of executive and non executive directors. While King II recommends that the majority should be non executive, King III improves on this requirement by recommending that they should also be independent. In addition, King III recommends that, if an independent non executive director has served on the board for more than nine years, the board should assess whether his/her independence has been impaired and report thereon. According to King III, non executive directors should not be entitled to a company's share options.

For the board to function effectively, it must appoint a chairman. While both King II and King III require the chairman to be an independent non executive director, King III recommends that, in the event where the chairman is not independent, a lead independent non executive director should be appointed. Among other things, the chairman is required (1) to inspire and give direction to the board; (2) to set the board agenda with the assistance of the company secretary; and (3) to evaluate the performance of the board and the chief executive.

(c) Board committees

Given that directors, especially non executive directors, are not involved in the day-to-day running of the company, both King II and King III recommend the delegation of the board's functions to the board committees. Depending on the size, operations and requirements of each company, various committees can be formed. Both King II and King III recommend the appointment of an audit committee, a remuneration committee and a nomination committee. Unlike King II, King III further recommends the appointment of a risk committee to deal with the risk management processes of the company.

While both King II and King III recommend that the committees should be chaired by the non executive directors, King III adds that such directors should also be independent. Both King II and King III encourage companies to have the chairmen of each board committee present at the annual general meeting to answer questions raised by the shareholders.

(d) Independent non executive directors

An independent director is defined in King II and King III as a non executive director who (1) is not a representative of a shareholder who has the ability to control management; (2) has not been employed by the company or the group of which it currently forms part; (3) is not a member of the immediate family of an individual who is employed by the company or the group in an executive capacity; (4) is not a professional advisor to the company or the group other than in a director capacity; (5) is not a significant supplier to or customer of the company or group; (6) has no significant contractual relationship with the company or group; and (7) is free from any business or relationship which could be seen to materially affect his/her independence.

In addition to the above, King III states that a non executive director is considered independent if he/she also (1) does not have a material direct or indirect interest in the company or group which is either greater than 5% of the group's total number of shares in issue or, even though less than 5%, is material to his/her personal wealth; (3) has not been employed by the group as designated auditor in the previous three financial years; (4) is not related to someone who has been employed by the group in an executive capacity in the previous three financial years; and (5) does not receive remuneration based on the company's performance.

(e) Remuneration of directors

King II and King III recommend the disclosure of the remuneration paid to the company's directors. The board is normally assisted by the remuneration committee in setting the remuneration of the directors. In other companies, the remuneration committee also assists in setting up the remuneration policy for the entire company and is not just limited to the directors and the executive management.

Both King II and King III require the full disclosure of remuneration paid to directors showing the breakdown of the package for each director. However, King III also requires the disclosure of the remuneration of the three most highly paid employees. In addition, King III recommends that the company's remuneration policy for executives be put to shareholders at the annual general meeting for a non-binding vote of approval.

(f) Audit committees

King II and King III require the audit committee to have a majority of independent non executive directors who are financially literate. They further recommend that the board chairman should not be a member of the audit committee but can attend its meetings by invitation.

Unlike King II, where the audit committee is appointed by the board, King III emphasises the requirement of the Companies Act (Companies Act, 2008) that the appointment be made by the shareholders. In a separate section within the integrated annual report, the audit committee is required in terms of King III to, among other things, (1) report on how it carried out its functions; (2) report on whether it is satisfied with the independence of the company's auditors and the expertise of the financial director; and (3) comment on the financial statements, accounting practices, internal financial control and any report forming part of the integrated annual report. These requirements are also in line with the provisions of the Companies Act of 2008.

(g) Risk management

King II and King III require the board of directors to identify the key risk areas and key performance indicators of the company's business. Such risks and performance indicators should be monitored on a regular basis. The board is responsible for the total risk management but is entitled to delegate the design, implementation and monitoring of the risk management process to management.

Rather than treating risk management in isolation, King III emphasises the need for the board and management to understand that risk management forms part of its strategic goals together with its policies, plans and processes.

(h) Internal audit function

The role of the internal audit function is important within the organisation to promote good corporate governance. In addition to their function of evaluating the effectiveness of the system of internal control, King III expects the internal auditors to provide a written report on the effectiveness of the company's risk management processes.

King III also recommends that internal auditors should follow a risk-based approach in their audit rather than the compliance-based approach recommended in King II. In addition to the assessment of the internal control system, King III requires internal auditors to specifically assess the internal financial controls to be reported on by the audit committee.

The head of internal audit function is expected to attend audit committee meetings. Whereas King II requires the head of internal audit to report administratively to the company's chief executive officer, King III requires him/her to report directly to the chairman of the audit committee.

(i) Compliance with laws, codes, rules and standards

In King III, compliance with the laws, standards, codes and rules by companies is imperative. Since many companies tend to take a casual approach on this issue, King III recommends the formation of a dedicated compliance section within the company to look after these matters. The compliance function should form part of the company's risk management processes. It is also recommended that the company should appoint a compliance officer to report to the board on the compliance matters.

(j) Information technology

In King III a new chapter has been dedicated to information technology (IT) which requires companies to adopt IT as part of the company's governance structures. Unlike King II, King III places the responsibility for IT governance with the board. Among its functions, the board is responsible for (1) ensuring that the company's IT strategy is integrated with its overall business strategy and processes; and (2) monitoring and evaluating significant IT investments and expenditure. For implementation purposes, the board should delegate its IT strategies to management.

(k) Stakeholder relationships

The governance of stakeholder relationships is dealt with in King II but is expanded further in a separate chapter in King III. This chapter has been devoted to stakeholder relationships given the importance of stakeholders and their role in ensuring that the company addresses the sustainability considerations. As part of managing stakeholder relationships, King III has introduced a new concept of alternative dispute resolution (ADR). With ADR, parties involved

in a dispute are encouraged to resolve their dispute in an amicable way such as appointing a mediator rather than taking the matter to court which can be costly and time consuming.

(l) Integrated reporting

King II recommends that a company should report at least annually on the sustainability issues consisting of economic, social and environmental considerations. The company should also consider reporting on its progress regarding transformation and ethics. While King II allows companies to report on sustainability issues together with their financial performance, many companies preferred reporting on sustainability in a separate report. King III now encourages companies to integrate reporting on financial performance together with their strategies, corporate governance, risks and sustainability in a manner that would show interdependencies between these concepts. Reporting this way will help stakeholders to get a better view and understanding of the company's performance and its ability to create and sustain value.

2.4 Sustainability considerations

2.4.1 Background to sustainability

Sustainability reporting is not a new concept but has its background in the 1970s (Kolk, 2005). In those days, reporting was limited as companies tended to focus on the social issues instead of also addressing economic and environmental issues (Kolk, 2005). This is supported by surveys showing that, by the late 1970s, 90% of Fortune 500 companies reported on social issues in their annual reports (Kolk, 2005). Although social issues received attention, reporting on these issues was very little, as their coverage was often less than a page (Kolk, 2005).

Social reporting lost momentum in the early 1980s following global recession and high rates of unemployment (Kolk, 2005; Gray, 2001). This led to a shift of focus from social reporting to economic issues. It was not until the late 1980s and early 1990s that companies began to report on social issues again (Gray, 2001), this time including environmental issues. According to Kolk (2005), this second wave of reporting was largely due to pressure from non-governmental organisations which required companies to cover both social and environmental issues in their reports.

Following the Rio Declaration (UN Agenda 21, 1992) adopted by many governments at the United Nations summit held in Brazil in 1992, the international community showed its commitment to addressing sustainability issues in different ways. For example, the Global Reporting Initiative (GRI, 2011) issued guidelines on sustainability in 1997 (Nazari, 2009; Labuschagne et al. 2004), which was followed later by the release of the UN Global Compact in 2001. These two documents complement each another. The GRI (2011), in particular, deals extensively with guidelines on sustainability issues based on the three themes, namely, economic, environmental and economic issues. The GRI (2011) gained popularity and was widely quoted by most European and American companies in their reporting.

Although the GRI (2011) and the UN Global Impact provide guidelines on sustainability issues, a large number of non-governmental organisations and the investor community prefer these issues to be regulated as, in their view, companies often pick and choose issues that suit them instead of addressing issues of interest to stakeholders (Ligteringen and Zadek, 2002). This view is supported by Doane (2002) and Adams and Zutshi (2004), who believe that mandatory reporting will allow the market to operate more effectively by ensuring that relevant and transparent information is provided to all stakeholders.

Sustainability reporting has also gained momentum in South Africa following the release of the corporate governance guidelines by the King Committee, that is, King II in 2002 and King III in 2010 (IOD, 2002; IOD, 2009). King III (IOD, 2009), in particular, extended the concept of sustainability reporting to incorporate integrated reporting which, in essence, requires companies to report on sustainability issues, namely, economic, social and environmental and, at the same time, to show their connection to the company's strategy, corporate governance, risks and financial performance. This is in contrast to King II (IOD, 2002) which, although it required companies to report on sustainability issues, did not emphasise the need for integrated reporting. Although it was never the intention of King II (IOD, 2002), companies following its guidelines tended to report on sustainability matters separately from their financial performance. It is submitted that such reporting did not give stakeholders a holistic view of the company's business and its future prospects.

Having given some background on sustainability, it is worthwhile to look at the sustainability concepts, the Rio Declaration (UN Agenda 21, 1992) and the Millennium Development Goals (UN MDG, 2000) in detail in the following sections to provide more clarity and understanding of what sustainability entails. The sustainability concepts, namely, economic, social and environmental, are important given the primary objective of integrated reporting in

encouraging companies to draw the link between strategy, governance, risk, financial performance and sustainability to afford the stakeholders the opportunity of assessing the company holistically in terms of how it will be able to create and sustain value.

2.4.2 The Rio Declaration

Sustainability impacts were considered by the United Nations at their summit held in Rio de Janeiro in Brazil in 1992 (UN Agenda 21, 1992). At that summit, governments concluded that the success of any company in the 21st century, irrespective of the industry or sector in which it operates, is dependent on its consideration of the three pillars of sustainability, namely, economic, social and environmental alongside good corporate governance practices.

Sustainability can be defined as “meeting the needs of the present without compromising the ability of future generations to meet their needs” (Hutchins and Sutherland, 2008:1688; GRI, 2011). In broad terms, this definition reminds companies that, while the primary objective is geared toward financial performance, sustainability must be integrated with their objectives to ensure their future success. Hence, the summit summarised these important sustainability considerations in the Rio Declaration on Environment and Development, known as Agenda 21 (UN Agenda 21, 1992). This is regarded as a comprehensive plan of action to be undertaken by governments to ensure the plan’s success and impact on the environment.

Agenda 21 (UN Agenda 21, 1992) came into being after the United Nations had considered the challenges facing the world, such as poverty, ill health, illiteracy and disparities in income between the developed and the developing nations. It is submitted that the poorest people are found mostly in the developing nations and their condition seems to be worsening by the day. There is also compelling evidence that the ecosystem is deteriorating, including the depletion of the ozone layer, pollution of water and emission of high levels of carbon dioxide contributing to climate change and irregular weather patterns (UN Agenda 21, 1992). The United Nations was therefore forced to take appropriate action to address this situation.

The United Nations (UN Agenda 21, 1992) is, however, aware that the implementation of the environmental and development objectives of Agenda 21 will remain a challenge as they require a significant injection of financial resources especially in the developing countries. Financial resources will help cover the costs of the programmes undertaken by the developing countries to deal effectively with the global environmental problems. Financial

resources will also be required to strengthen the capacity of international institutions to implement such programmes.

While there are financial challenges, governments are nevertheless encouraged to introduce these programmes in their communities (UN Agenda 21, 1992). Such programmes can even be introduced at schools and tertiary institutions. However, governments are encouraged to work in partnership with non-governmental organisations, environmentalists and businesses to fast track the implementation of these programmes. Governments should also consider enacting laws to assist in the effective enforcement of these programmes

While Agenda 21 (UN Agenda 21, 1992) considers the social and economic impacts of sustainability, its primary focus is on the environment, which requires immediate global attention. However, the United Nations (UN Agenda 21, 1992) has realised that governments would first have to tackle the economic and social impacts before dealing effectively with the complex environmental issues.

2.4.3 Millennium Development Goals

After Agenda 21 (UN Agenda 21, 1992), the United Nations supplemented it with a number of other initiatives including the Millennium Development Goals (UN MDG, 2000), which the United Nations developed to assist governments to tackle various challenges around poverty, disease, education, and economic and other related issues, and also to improve the standard of living of the human race. According to the Millennium Development Goals (UN MDG, 2000), consideration of these issues will help the United Nations to meet its long-term objectives which should be a joint effort between all the nations to address challenges facing the environment.

The UN Millennium Declaration was adopted by 189 countries at the United Nations summit held in 2000 at which governments committed themselves to the eight Millennium Development Goals (Travis et al., 2004) to address the challenges mentioned above. While the United Nations plans to tackle all the issues embodied in the eight UN Millennium Goals, its emphasis is on development and poverty eradication with the aim of halving poverty by 2015 (Kabeer, 2003).

Sachs and McArthur (2005) report that the United Nations committed itself to reviewing progress on its goals in 2005. They observe that very little improvement has been made by 2005, as most countries, most notably those in sub-Saharan Africa, are still not on track to

achieving the goals. Travis et al. (2004) concur with this observation and add that it is the low-income countries that look unlikely to achieve the goals by 2015. However, Sachs and McArthur (2005) believe that the goals are still achievable but would require serious effort and commitment from the member countries if substantial progress is to be made.

One of the key challenges hindering the implementation of the UN Millennium Development Goals is a lack of financial resources, which makes it difficult to channel the necessary aid to the poorest countries (Sachs and McArthur, 2005). In addition, Sachs and McArthur (2005) note that empty promises by some countries are hampering the required efforts in this regard. Hence, in March 2002, governments recommitted themselves at the UN Monterrey in a new partnership of both rich and poor countries to meet the UN Millennium Goals (Sachs and McArthur, 2005). This renewed commitment was also intended to address expanded trade, aid and debt relief to help finance the infrastructure needed to attract investments.

While progress has generally been slow in meeting the UN Millennium Development Goals, Khanal (2011) reports some progress in Nepal in this regard. For example, he reports that the UN goals were incorporated into the government's strategic framework with the emphasis on poverty reduction. Accordingly, poverty rates decreased significantly by 11% from 42% to 31% between 1996 and 2004. Although these results are promising, Nepal still needs to improve in other areas such as closing the gap between rural and urban areas (Khanal, 2011).

Alongside poverty reduction, another UN Millennium Goal is intended to address gender inequality (UN MDG, 2000). Kabeer (2003) notes the challenges that women face on a daily basis in comparison to men, despite the major role played by women in their families. According to Kabeer (2003), gender inequality is worse than any other form of inequality and therefore governments need to address it as a matter of urgency.

It is submitted that the Millennium Development Goals (UN MDG, 2000) and Agenda 21 (UN Agenda 21, 1992) are complementary to one another although their focus is different. The Millennium Development Goals' main focus is on socioeconomic aspects, whereas Agenda 21 focuses on the environment. While distinct from one another, the sustainability elements are interdependent, as observed by Hutchins and Sutherlands (2008). An example to illustrate their interdependencies is a situation where a company takes care of its employees' economic situation by paying them salaries and wages. At the same time, it would have to address social considerations by protecting employees from potential hazards to ensure their safety. From an environmental perspective, the company needs to take appropriate

measures to ensure that its operations do not emit excessive amounts of carbon dioxide so as to avoid a negative impact on the climate.

2.4.4 Global Reporting Initiative

The Global Reporting Initiative (GRI) is an independent organisation "established in 1997 by a number of companies and organisations belonging to the Coalition for Environmentally Responsible Economies (CERES), with the mission of developing globally applicable guidelines for reporting on economic, environmental and social performance, initially for corporations and eventually for any business or governmental or non-governmental organisation" (Hedberg and von Malmborg, 2003:155). The GRI partners with United Nations organs such as the United Nations Environment Program (UNEP) in promoting sustainability initiatives (Hedberg and von Malmborg, 2003)

The primary reason behind the formation of the GRI stemmed from a lack of guidelines regarding the corporate sustainability issues that companies were expected to cover in their reports, thus resulting in information that was not comparable between the companies (Hedberg and von Malmborg, 2003). Therefore, the aim of the GRI is to develop a reporting framework to be used by companies on a voluntary basis and that will elevate sustainability reporting to the same level as financial reporting in terms of rigour and comparability (Willis, 2003).

The GRI (2011) regards sustainability reporting as a living process which does not begin or end with the printed or online reports. It encourages companies to entrench its guidelines across all lines of their operations. The guidelines should be implemented in such a way that they support the companies' plans, policies and, more importantly, their strategic goals. Once implemented, sustainability reporting will help the companies to effectively assess their performance in terms of economic, social and environmental impacts (GRI, 2011).

The GRI (2011) gives companies an option of implementing either a full set of its guidelines or introducing them in phases. The GRI splits the guidelines into three categories, namely, Category A, Category B and Category C. Category A is intended for those companies which want to implement a full set of the GRI guidelines, whereas Category C is intended for the beginners. Category B is somewhere in between Categories A and C. Once implemented, companies are encouraged to inform the GRI about their selection so that further support can be provided by the GRI if necessary.

The GRI (2011) also provides guidance on how companies should go about gathering, compiling and analysing data. There are various principles which companies need to follow to ensure that they cover a wide range of issues of interest to various stakeholders without compromising the quality of the report. The principles include (1) materiality; (2) completeness; (3) comparability; (4) accuracy; (5) timeliness; (6) clarity; (7) reliability; (8) balance of information; (9) issues put in context; and (10) stakeholder inclusivity approach. These principles are similar to those of the Conceptual Framework for Financial Reporting (IASB, 2010).

While the spirit of the GRI guidelines is intended to promote consistency and adequate coverage of the sustainability issues by companies, Hedberg and von Malmborg (2003) report instances of deviations from these guidelines based on their study of reporting by the Swedish companies. They find that, where the companies report on sustainability, the objective is more to promote their businesses instead of reporting on sustainability in the manner envisaged by the GRI. To cover the sustainability issues in terms of the GRI guidelines, companies should provide a balanced view in terms of reporting both positive and negative issues.

Based on the sustainability themes covered in the GRI (2011), it is submitted that the GRI guidelines, although more extensive in coverage, are in line with the objectives formulated in the UN Agenda 21 of the Rio Declaration (UN Agenda 21, 1992) as well as the UN Millennium Development Goals (UN MDG, 2000). In South Africa, King III (IOD, 2009) encourages companies to report on the sustainability considerations consisting of economic, social and environmental impacts covered in the GRI (2011).

The next sections will consider each of the sustainability impacts in detail. Their discussion is important given that the sustainability research indicators have been used in this study alongside other integrated reporting research indicators to answer the research question whether the level of reporting by the South African listed companies has improved post the King III (IOD, 2009) release in March 2010.

2.4.5 Economic sustainability

According to the GRI (2011), the economic dimension of sustainability is concerned with the company's impact on the economic condition of its stakeholders and on the economic system of the country in which it operates. Most of the economic information is contained in the company's financial statements in various forms such as tables and graphs highlighting

its financial performance (based on the researcher's analysis of some of the companies' annual financial statements [AFS]). Such information is usually presented in the format dictated by the accounting standards. It is therefore up to the stakeholders to analyse such information in the manner that would to suit their needs.

Though stakeholders can choose to analyse data using their own tools, most companies nowadays present economic information in a manner that would be easily understood by the users (based on the researcher's analysis of AFS). For example, in South Africa, it is common for the chairman and the chief executive to include their commentary on the economic outlook at the beginning of the report (based on the researcher's analysis of AFS). They could comment on the impact of interest rates, exchange rates and inflation on the company's financial performance as well as on the future economic prospect.

In general, economic data is available throughout the entire report. Besides the chairman's and the chief executive's reports, it is common for divisional heads to comment on the performance of their operations (based on the researcher's analysis of AFS). Obviously, such information should be in line with the presentation of the overall company's or group's performance as recommended by King III (IOD, 2009). Nowadays, companies make use of the value added statements to summarise their economic data (based on the researcher's analysis of AFS). Supplemented by graphical presentation, the value added statement shows how the funds were generated and distributed. The primary recipients of funds are employees in the form of wages and salaries, suppliers in the form of monthly invoice payments and the government in the form of taxes.

2.4.6 Social sustainability

Gone are the days when companies regarded themselves as separate from the societies in which they operated, thanks to the laws enacted by many countries around the world which treat companies as citizens in the same way as natural persons. As citizens, companies are entitled to certain rights such as the right to existence and freedom. In South Africa, companies' rights are guaranteed by the Bill of Rights enshrined in the Constitution (IOD, 2009).

Although companies are entitled to certain rights in the same way as natural persons, they are expected to play a bigger role in society than any other organisations (Hahn and Scheermesser, 2006). According to Hahn and Scheermesser (2006), they are likely to have a more positive impact on society than the government because of their financial capacity to

drive the resources of the economy. As a result, they are expected to embark upon initiatives that would have a long-lasting impact on society such as (1) creating awareness among the communities about HIV/AIDS; (2) providing bursaries to needy students; (3) donating funds to charitable organisations; and (4) setting up business programmes to uplift the upcoming entrepreneurs.

Given the size of their operations across many countries, multinational companies are expected to act responsibly and be accountable for any impact their operations have on the societies in which they operate (Adams and Zutshi, 2004). A survey conducted in the United Kingdom confirms these expectations and adds that companies are expected to meet not only the health and safety requirements of their employees but to respect their human rights as well (Smith, 2002:42 quoted in Adams and Zutshi, 2004). In another survey conducted in the United Kingdom, the results reveal that 89% of the respondents indicated that they were more likely to be influenced by companies reporting on social issues (Adams and Zutshi, 2004).

The question that arises is how far the companies have gone in terms of heeding the call. Unfortunately, the picture painted by research and surveys shows that companies have not done enough. According to Doane (2002), companies are still lagging behind in terms of participating in and reporting on social issues. For example, in the United Kingdom, Doane (2002) reports that only 35 out of 350 FTSE companies produced social reports by the end of 2000. What is disappointing though is that even those companies which report on social issues do little in terms of disclosing the quantitative data (Doane, 2002). Such information is invaluable in terms of highlighting the extent to which companies are involved in social matters.

Companies reluctant to report on social issues have advanced lame excuses for doing so. According to Doane (2002), they argue that they do not see the benefit of social reporting as there are no proper standards that can be followed similar to those adopted by the accounting profession. It is submitted that these are lame excuses as companies stand to benefit from their involvement in social initiatives in terms of creating a good reputation which is essential in enhancing their brand (IOD, 2009). Moreover, despite some of the shortcomings of the GRI (2011) guidelines, including failure to cover some of the social aspects in detail (McElroy et al., 2008), they are still useful in guiding companies on the social considerations to be reported on.

The disappointing participation of companies in social matters has prompted many stakeholders including non-governmental organisations to push for the legislation that would compel these companies to comply (Doane, 2002). They believe that governments have a responsibility to provide an adequate framework to ensure that, not only are the citizens' rights protected, but that their basic needs are met (Doane, 2002). They believe that expecting companies to drive social change without forcing them to do so gives false expectations.

Companies not engaging in social matters are shooting themselves in the foot as there are more benefits that can be derived than isolating themselves (Adams and Zutshi, 2004). Research shows that reporting on social issues is essential for their long-term survival. Adams and Zutshi (2004) list the benefits that can be derived including that companies can (1) attract and retain most talented employees; (2) develop better internal control systems and cost savings resulting in improved earnings; (3) minimise risks of consumer boycotts which will enhance the company's reputation; and (4) increase the company's economic value in the long term.

Turning to South Africa, this research has found that many listed companies have started to report on social issues. However, in line with what is happening globally, the quality of corporate social reporting remains poor. Companies tend to do well in terms of reporting the initiatives they embark upon but often fail to report on the cost benefit of their efforts. In other words, they still lag behind in terms of providing quantitative data. While this study has focused mainly on listed companies, the situation is likely to be worse in the case of unlisted companies. While signs of social reporting are encouraging, much still needs to be done to improve reporting and take social reporting in South Africa to the next level.

2.4.7 Environmental sustainability

With regard to the environmental dimension, the focus has become a global one following issues around climate change, air pollution and hazardous substances that are dangerous to human beings and the ecosystem (GRI, 2011, UN Agenda 21, 1992). The seriousness of this issue has prompted the United Nations to issue a series of articles such as the UN Global Compact (2000) to encourage governments to incorporate environmental issues in their strategic goals. The latest issue is three of the Ten Principles of the UN Global Compact (2000, which are regarded as the cornerstone of environmental activities and are briefly discussed as follows:

Principle 7 arose from the observation that companies often undertake projects that are harmful to the environment. More often than not, they start doing something to remedy the situation after the damage has been caused, instead of taking precautionary measures right from the beginning of the project to avoid the damage or to ensure that very little damage is caused. ***Principle 8*** encourages companies to be good neighbours to the communities in which they operate. In the same way as communities expect companies to meet their social needs, they expect companies to engage in environmentally sustainable practices. ***Principle 9*** encourages businesses to use environmentally sound technologies (1) that reduce pollution; (2) that recycle more of their waste products; and (3) that use lesser resources in a more sustainable manner.

The above principles are an extension of the environmental principles adopted by governments in terms of the Rio Declaration at the UN summit held in Brazil in 1992 (UN Agenda 21, 1992). The UN admitted that no single country or organisation can tackle the environmental problems alone but that they require joint efforts by all the governments and organisations (UN Agenda 21, 1992). According to Sahay (2004), such efforts are necessary as the damage to the environment, such as air pollution, affects everyone and not only those who caused the damage in the first place. Therefore, organisations need to realise that their joint efforts towards improving environmental impacts can go a long way to making the world a better place. Their efforts can help reduce carbon substances that have a negative impact on the climate change (Sahay, 2004). They can also help reduce the use of chemical substances that could pollute water and be dangerous to human beings, animals and the ecosystem.

Subsequent to the Rio Declaration (UN Agenda 21, 1992), efforts have been made by governments and organisations to tackle the environmental problems. Extensive efforts in reporting on environmental issues have been observed mostly in developed countries such as the United States, Germany, the United Kingdom, Japan and France (Sahay, 2004). According to a survey undertaken by KPMG in 2002, companies operating in industries producing environmentally sensitive products such as chemicals, oil and gas are among the highest in terms of reporting on environmental issues (Sahay, 2004); thanks to countries that have issued environmental laws to govern the operations of these companies. Besides, there are international standards such as ISO 14001 which guide companies on the environmental impacts.

To improve reporting on environmental impacts, the GRI (2011) has issued guidelines to assist companies in this regard. They are complementary to those of the UN Global Impact

(2000) but add a number of environmental indicators to guide companies in their reporting. The GRI (2011) guidelines are voluntary in nature but have gained popularity among many companies and organisations. They have also gained the support of professionals, environmentalists and other stakeholders interested in environmental issues.

Although companies are making an effort to report on environmental issues, there are concerns in terms of the quality and the extent of reporting (Sahay, 2004). In common with social impacts, companies that report on environmental impacts tend to leave out important information such as quantitative data which would have been useful to the environmentalists and other users. Since the GRI (2011) does not give guidance on the specific guidelines to be used, companies tend to pick those indicators that would suit them for publicity purposes rather than disclosing environmental facts (Sahay, 2004).

It shows that companies are not mindful of the fact that poor reporting can damage their public image and prevent them from achieving their strategic goals (Sahay, 2004). This statement implies that the 21st century company is expected to pay the same attention and bring the same rigor to environmental activities as it does in the other sections of its operations to achieve financial performance. It is important since there is now a growing awareness among communities of environmental issues and their impact on the safety and quality of life of the people (Dias-Sardinha and Reijnders, 2001).

It is interesting to note that South Africa is among the countries at the forefront of the initiatives aimed at protecting the environment. Recently, in December 2011, it hosted the global climate change summit. This summit and others previously organised by the United Nations have emphasised the need for companies to start doing something to protect the environment and also to cover these issues in their reports. This would help to avoid shifting unnecessary responsibility to future generations.

In South Africa, the Johannesburg Stock Exchange (JSE) in 2004 launched a Socially Responsible Investment (SRI) Index aimed at encouraging listed companies to incorporate sustainability practices in their business operations (JSE, 2004). Being the first of its kind in the developing countries, the JSE SRI Index (JSE, 2004) has a number of requirements which companies need to comply with before being included in the Index. The Index (JSE, 2004) is modelled on international best practices, including those of the FTSE in the United Kingdom.

2.4.8 Sustainability accounting

Sustainability is a concept that 21st century companies need to remember and incorporate into their businesses to ensure their future success. However, research reveals that companies which report on sustainability developments often fail to quantify the costs incurred in compiling data and reporting on this issue. Hence, Jasch and Stasiskiene (2005) propose the incorporation of sustainability accounting into corporate reporting, which would entail gathering and analysing data in the same way as companies would do for financial accounting purposes. That way, companies will be able to determine the costs as well as the benefits of sustainability reporting.

Given that one of the primary objectives of any business is to derive financial benefit, it would not be in the best interests of the company to continue with sustainability reporting if the costs of doing so outweigh the benefits. Obviously, it would not be a simple matter to discontinue sustainability reporting given its importance, but at least the company would understand the cost implications. In the process, the company might consider other ways of reducing the costs before reaching a final decision.

In a slightly different context, Perrini and Tencati (2006) present a system called sustainability evaluation and reporting system (SERS), which is aimed at monitoring and tracking the company's overall performance measured in terms of its financial performance and its sustainability performance from both a qualitative and a quantitative perspective. According to Perrini and Tencati (2006:300), the goal of SERS is, among others "(1) to build an efficient and effective methodology for an overall assessment of the corporate sustainability in order to foster and support new accounting and reporting efforts in companies; and (2) to improve the quality of decision-making processes". Clearly, SERS supports Jasch and Stasiskiene's (2005) idea discussed above of encouraging companies to implement the sustainability reporting system to help manage sustainability costs.

2.4.9 Audit assurance of sustainability impacts

In addition to the proposed systems aimed at monitoring and keeping track of sustainability costs, Gray (2001) calls for an independent assurance of the social reports in the same way as the auditors provide assurance of the financial reports. It is submitted that assurance should not be limited to social reports but should cover environmental reports as well. Economic issues are normally covered when the auditors provide assurance on the financial statements. Hence, the focus of assurance is on the social and environmental impacts. It is

further submitted that such assurance will provide the stakeholders with some comfort about the relevance, completeness, fairness and honesty of such reports.

There are already international standards such as ISO 14001 aimed at providing assurance on environmental issues. These standards are intended for companies operating in different industries. For example, companies in the chemical industry are required to provide assurance about the measures they have taken (1) to ensure the safety of their employees; and (2) to ensure that their chemicals will not add to the pollution of water. In addition to the international standards, governments are at liberty to issue their own standards to foster compliance by companies.

2.5 Corporate failures

Failure to address strategy, corporate governance, risk, financial performance and sustainability issues could result in corporate failures in the long term such as those witnessed by the collapse of Enron, WorldCom and Parmalat (Grant and Visconti, 2006). Research shows that companies facing financial difficulties tend to focus on the short-term benefits at the expense of their long-term sustainability (Healy and Palepu, 2001). As pointed out in the corporate governance section, there are a number of reasons why companies resort to short-term benefits, including the fact that they want to disclose improved earnings from one period to another to avoid negative share price movement and negative publicity (Collingwood, 2001). By so doing, management are hoping to gain in terms of bonuses and securing their positions.

In the study of corporate failures, Argenti (1983) observes that such failures do not start overnight but often start a few years before the companies eventually collapse. These companies are often characterised by (1) poor management; (2) a few dominant or autocratic individuals; and (3) lack of long-term strategic goals. All of these factors point to the lack of corporate governance practices within such companies. As a result, management of these companies tend to downplay any financial problems that would have a negative consequence on their businesses. And they often disclose very little information in their reports to avoid questions from investors and other stakeholders (Boo and Simnett, 2002).

To discourage companies from taking a short-term view, characterised by the withholding of relevant information, some jurisdictions such as the United States, Denmark, the United Kingdom and Germany have come up with enforceable legislation. In particular, the United States has promulgated the Sarbanes-Oxley Act (SOX, 2002), forcing compliance by all

companies listed on the New York Stock Exchange. SOX (2002) requires companies to, among other things, provide information on corporate governance, risk management and assurance on the system of internal controls.

The lessons learnt from corporate failures are that 21st century companies need to know that addressing their financial performance in conjunction with the corporate governance and sustainability issues in the integrated reporting enhances their economic value. In particular, sustainability considerations are important as investors and other stakeholders put more and more emphasis on them. Another lesson relates to the importance of treating all company stakeholders equally instead of only addressing the needs of a few, as this may have a negative impact on the company's sustainability in the future (Perrini and Tencati, 2006). It would entail listening to their legitimate needs, interests and expectations as well as taking them into account in the decision-making process in the best interest of the company.

Chapter 3 Research Methodology

3.1 Research design

3.1.1 Nature of the study

This study is regarded as the comparative study as it compares the level of reporting by South African listed companies in the current year (2010/2011) to that of the base (2009) to determine if the level of reporting has improved since King III became effective in March 2010 (IOD, 2009).

The source of data for the purposes of this research is the annual reports published by the listed companies for the current year as well as the base year. These annual reports have been extracted from the McGregor database, a reputable database used by a wide range of individuals and organisations.

3.1.2 Pilot study

Before the actual study was conducted, it was decided in August 2011 to conduct a pilot study on a few companies to determine whether the proposed research indicators (provided in Appendix A) and the method of allocating the scores (referred to in section 3.5.1) were suitable for this research. The pilot study used a six-year period from 2006 to 2011 to determine the pattern in the level of reporting by these companies.

The results of the pilot study revealed the following: (1) from 2006 to 2009, reporting by all the companies was generally in compliance with the King II recommendations (IOD, 2002); (2) in 2010, some companies complied with the King II recommendations (IOD, 2002) whereas others complied with the King III recommendations (IOD, 2009); (3) some companies whose financial year ended on or after June had not yet released their 2011 results whereas others had; (4) those companies which had released their 2011 results had their reports titled “integrated annual report”; and (5) companies had either covered sustainability issues in the annual reports or in the separate reports available on their website.

3.2 Research approach

After the pilot study had been conducted, the results highlighted some important aspects which deserved to be taken into account in the actual study. Firstly, there were no significant differences in terms of reporting by companies during the period 2006 to 2009. These results were in line with the researcher's expectations, confirming compliance by companies only with the King II guidelines (IOD, 2009) during these periods. Since similar patterns of reporting were expected for the periods during which King II was in force, this study has decided to use 2009 as a representative period for all the periods from 2002 to 2009. As a result, 2009 is regarded as the base year.

On the other hand, King III (IOD, 2009) was effective from March 2010 and guidance had been provided as to how its guidelines should be implemented given the different financial year ends of companies. In the case of a company with a February year end, the King III guidelines would be applicable to that company from 1 March 2010 to February 2011. Effectively, this company would start reporting on the King III recommendations when it published its February 2011 annual report. A similar analogy can be used in the case of a company with a December financial year end where its cycle starts in January 2011 and runs to December 2011.

Although King III became effective in March 2010, it was first released in September 2009, thus making it possible for companies to start implementing its guidelines as early as 2010. Some companies were proactive in this regard in the sense that, even though they were not obliged to comply with the King III guidelines because of their financial year cycles discussed above, they nevertheless started incorporating the King III recommendations in their annual reports for 2010. Part of the reason for early compliance was attributed to the fact that it would be in the best interests of their businesses to do so.

It is for this reason that this study took the view that, despite the varying financial cycles of companies discussed above, companies were nevertheless expected to comply with the King III recommendations from the beginning of 2010. While this approach might be unfair to other companies, it was however considered an ideal approach in this study for both consistency and comparability purposes.

Another aspect considered in this study was the fact that companies may have issued either 2010 or 2011 annual reports by the cut-off date of 31 December 2011, chosen for the purposes of this study. Depending on the date on which the annual reports were released,

preference was given to the 2011 annual reports, as these were expected to have incorporated more King III recommendations than the 2010 annual reports. Otherwise, the 2010 annual reports were used. In both cases, 2010/2011 is regarded as the current year to be compared to 2009 (the base year) in terms of the level of reporting.

3.3 Population size and sample

3.3.1 Population and sample

In September 2011 the McGregor database consisted of 401 listed companies which made up the population retrieved for the purposes of this study. In every study, a decision needs to be made as to whether to conduct the tests on the entire population or to conduct them on a sample. If the decision is to conduct the tests on a sample, the researcher needs to ensure that scientific methods are followed in terms of determining the sample size and the sample selection. Secondly, the selected sample must be representative of the entire population to avoid bias in the analysis of results.

Where the population is less than 100, it is recommended to select the entire population (Leedy and Ormrod, 2001). However, where the population is more than 100, varying sample sizes can be determined. In some specialised fields such as auditing, the sample size is usually a function of risk and tolerable error that the auditor is prepared to accept and the degree of assurance that the auditor is willing to achieve (Puttick and van Esch, 1987). Puttick and van Esch add that the population has little effect on the sample size unless it is very small. Hence, a minimum sample size of 30 is usually recommended for research purposes irrespective of the population size. For the purposes of this study, a sample size of 92 companies has been determined which takes into account the fact that the analysis has been extended not only to the entire population but also to the individual sectors.

3.3.2 Sample selection

Having determined a sample size of 92 companies, the next step was to select companies from the population. Various statistical methods could be used in this regard. Given that the population was stratified in terms of industries, care was taken to ensure that the selection of at least five companies was made per industry, and that such companies were representative of the entire industry. The selection can be done manually or by means of computer techniques. After careful consideration, it was decided to use a manual selection technique.

The second step was to get 401 small tags representing the population. The name of a company was written on each tag and then the tags were grouped in terms of individual industries before putting them into a pot. The pot was shaken to ensure that each tag stood an equal chance of being selected. Without looking at the tags inside the pot and, in no particular order, the tags were picked out one by one until a total of five were selected. The same process was repeated for each subsequent industry until all 92 companies had been selected.

The fourth step was to write the names of all the selected companies by industry on the computer spreadsheet. The fifth step was to check the McGregor database to ascertain whether the selected companies all had the required annual reports, that is, 2009 and 2010/2011 reports. If either 2009 or 2010/2011 report was missing, such company was excluded from the study as comparison of the level of reporting between 2009 and 2010/2011 would no longer be possible. In that situation, such a company would be replaced by another one in the same industry. In this second round of selection, only those companies which had not been selected before would be part of the process. Interestingly, very few companies had to be replaced.

3.4 Research instruments

A total of 111 research indicators were selected mainly from King III (IOD, 2009) and the GRI (2011). However, there were a few research indicators that were selected based on the researcher's judgement. Given the varying strengths of King III (IOD, 2009) and the GRI (2011), the key research indicators on corporate governance, risk management and strategy were selected from the King III report, whereas those for sustainability, consisting of economic, social and environmental elements, were selected from the GRI (2011). A list of the indicators is provided in Appendix A.

With regard to financial performance, no attempt was made to include the financial performance indicators in the same way as indicators for the other concepts of integrated reporting. This decision was based on the fact that companies use different financial indicators where the selection of indicators from one group of companies may not necessarily address the financial performance of the other group of companies.

3.5 Data analysis and interpretation

3.5.1 Score allocation

Each “indicator” used under appropriate headings (refer to Appendix A) was allocated a score of “1” to “5” with the following meanings:

- “1” meaning “non compliance” – the equivalent of 0%.
- “2” meaning “little detail provided” – ranging between 0% and 25% (poor/average).
- “3” meaning “some detail provided” – ranging between 25% and 50% (satisfactory).
- “4” meaning “more detail provided” – ranging between 50% and 75% (good).
- “5” meaning “much detail provided” – ranging between 75% and 100% (very good / excellent).

The allocation of scores was first conducted on the companies which were part of the pilot study discussed in section 3.1.2 to determine their effectiveness. The pilot study was instrumental in refining these scores. While subjectivity cannot be entirely eliminated, this research can nevertheless take comfort in the fact that consistency was followed in allocating the scores to achieve the desired results.

3.5.2 Harmonisation of information

Integrated reporting requires the company to present information about its strategies, corporate governance, risk assessment, financial performance and sustainability in a manner that would allow stakeholders to draw a link between these concepts of integrated reporting (IOD, 2009; SAIRC Discussion Paper, 2011). In other words, this information should be harmonised from the beginning of the report right through to the end of that report.

It is common for companies to address the concepts of integrated reporting in the chairman’s, chief executive’s, financial director’s or other executives’ reports. Irrespective of how the information is presented, the company should ensure that the commentary by directors is complementary to information presented in the other parts of the report. Harmonisation of information is a critical aspect of integrated reporting which is the essence of this study. It is for this reason that two research indicators, referred to as numbers 93 and 94 of Appendix A, were selected to deal specifically with the tone and harmonisation of information in the companies’ annual reports.

3.5.3 Statistical methods used in the study

This research did not use parametric statistics owing to the basic categorical nature of the data and the non-normality of data when treating it as numeric scale data to calculate mean score values. Instead, descriptive statistics and non-parametric methods were used to analyse the data. This study used the non-parametric Spearman's rho to determine whether there is any correlation between the scores for the current year (2010/2011) and the scores for the base year (2009) for each indicator. High correlation between the years is an indication of little improvement in reporting in the current year when compared to the base year. On the other hand, low correlation is an indication of some improvement in the current year.

Correlation between the current year and the base year is measured in terms of the correlation coefficient on a scale of between -1 and 1. It has been decided in this study to use three decimal places before and after zero for any correlation coefficient to enable the interpretation of data. Generally, correlation coefficients above 0.5 are leaning towards high correlation and those below 0.5 are leaning towards low correlation.

Though the correlation coefficient is interpreted differently by various authors, Cohen (1988) suggests the following guidelines with r representing the relevant correlation coefficient:

r = 0.10 to 0.29 or r = -0.10 to -0.29 low correlation
r = 0.30 to 0.49 or r = -0.30 to -0.49 medium correlation
r = 0.50 to 1.00 or r = -0.50 to -1.00 high correlation

The view taken in this study follows the thinking of Cohen (1988) but with a slight change in terms of the interpretation in order to suit the objectives of this study. Therefore, in this study, the correlation coefficients falling between 0 and 0.4 OR 0 and -0.4 indicate much improved performance, whereas those falling between 0.4 and 0.5 OR -0.4 and -0.5 indicate normal or slight improvement. However, the correlation coefficients between 0.5 and 1.00 OR -0.5 and -1.00 indicate no improvement.

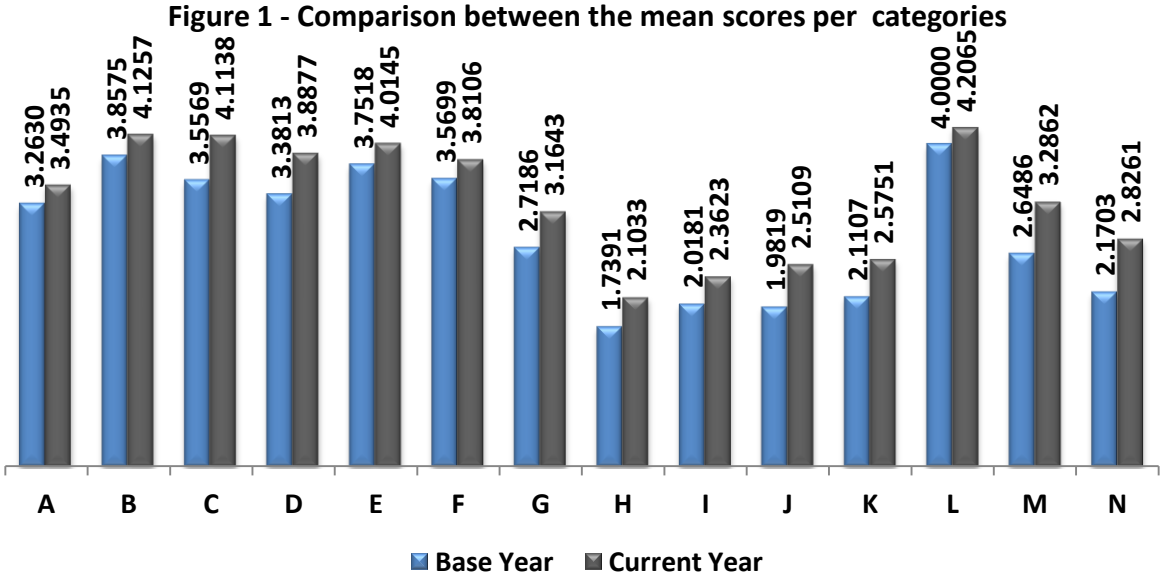
Besides the Spearman's rho correlation, this study also makes use of the mean scores and the mean score differences to determine whether, on average, the companies demonstrated any improvement in the level of reporting. Unlike Spearman's rho correlation, the mean scores and the mean score differences are used to determine whether a change in the pattern of reporting is due to improvement or not. A higher mean score in the current year

than that of the base year indicates, on average, an improvement in the level of reporting by the companies in the current year. The opposite is true for a lower mean score in the current year when compared to the base year. The magnitude of the mean score differences are used to quantify the improvement or deterioration. Equal means in both the base year and the current year is an indication that, on average, the companies did not demonstrate any change in their level of reporting.

While the means and the mean differences have been used in this study, it was decided to ignore standard deviations, variances and standard errors due to (1) the non-normality of data used in this study; and (2) the fact that for some indicators only small variances have been observed. It was therefore concluded that standard deviations, variances and standard errors would not lend themselves to any meaningful interpretation. As a result, they have been excluded from the study, and reliance is now placed on the analysis of the mean scores and the mean score differences as they relate to the scoring scale.

Chapter 4 Research Results

4.1 Comparison between the mean scores of the current year and the base year per individual main categories



Legend
A – Ethical leadership and corporate citizenship; **B** – Boards and directors; **C** – Audit committee; **D** – Risk management committee; **E** – Remuneration committee; **F** – Nomination committee; **G** – Internal audit function; **H** – Governance of information technology; **I** – Compliance with laws, rules, codes and standards; **J** – Governing stakeholder relationships; **K** – Integrated reporting; **L** – Economic sustainability; **M** – Social sustainability; **N** – Environmental sustainability

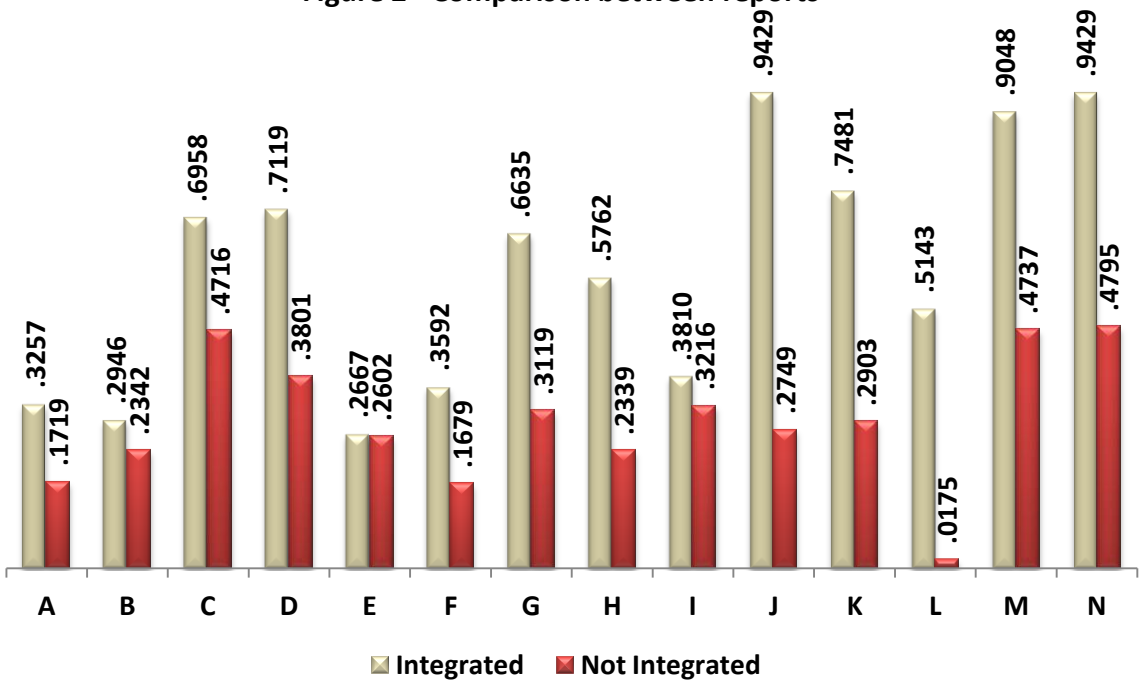
This section makes use of the graph to compare, for each category of indicators, the mean scores of the current year (2010/2011) and those of the base year (2009) in order to investigate whether any improvement in the level of reporting has been achieved in the current year. Given the large number of indicators under each main category, presenting individual indicators could make the interpretation difficult especially if they are all presented graphically. Instead, it was decided to show the mean scores of the main categories which were created by calculating the mean scores for the set of indicators that fall under each of the categories.

In the graph in Figure 1, the mean scores of the current year are shown in black and those of the base year shown in blue. Overall, the mean scores for all categories show improvement by companies in terms of the level of their reporting in the current year compared to the base year. The results of the performance of individual indicators under each main category are provided in Appendix B. While a few indicators show some deterioration in the level of reporting (see Appendix B), for the majority of indicators an improvement in the level of reporting is evident in the current year.

4.2 Comparison between the integrated annual reports and the annual reports

Out of 92 companies, only 35 companies (representing 38%) issued annual reports titled "integrated annual reports" in the current year (2010/2011). On the other hand, the remaining 57 companies issued annual reports titled "annual reports". This study expected companies with "integrated annual reports" to perform better in terms of the level of their reporting in the current year than those with the "annual reports". The graph in Figure 2 shows the mean score differences illustrating how they have performed.

Figure 2 - Comparison between reports



Legend
A – Ethical leadership and corporate citizenship; **B** – Boards and directors; **C** – Audit committee; **D** – Risk management committee; **E** – Remuneration committee; **F** – Nomination committee; **G** – Internal audit function; **H** – Governance of information technology; **I** – Compliance with laws, rules, codes and standards; **J** – Governing stakeholder relationships; **K** – Integrated reporting; **L** – Economic sustainability; **M** – Social sustainability; **N** – Environmental sustainability

The graph in Figure 2 shows companies with the "integrated annual reports" in light brown colour and those with the "annual reports" in red. Overall, companies with the integrated annual reports performed better than those with annual reports in all main categories. The graph further illustrates that 10 out of 14 categories show significant improvement in the level of reporting by companies which have issued integrated annual reports. Using the mean score differences, such significant improvements have been noted in the case of (1) Ethical Leadership and Corporate Citizenship; (2) Risk Management; (3) Nomination Committee; (4) Internal Audit Function; (5) Governance of Information Technology; (6)

Governing Stakeholder Relationships; (7) Integrated Reporting; (8) Economic Sustainability; (9) Social Sustainability; and (10) Environmental Sustainability.

These results show that companies which have published integrated annual reports have taken steps in the right direction to comply with the King III guidelines (IOD, 2009) and the JSE listing requirements (JSE, 2011). The results also confirm that those companies not having released integrated reports are already lagging behind those which have published these reports, and stand to lose out in terms of the benefits associated with integrated reporting such as (1) the ability to attract investors to their businesses; and (2) restoring public confidence which would guarantee them success in the future.

4.3 Indicators showing significant improvement in the level of reporting

	Table 1 – Indicators showing significant improvement		
#	**Indicator**	**Spearman***	**Mean ^**
A	**Boards and Directors**		
1	CFO is a board member	0.318	0.348
2	Remuneration of the three most highly-paid employees is disclosed	0.370	0.648
B	**Audit Committee**		
3	Meets at least twice a year	0.304	0.109
4	Oversees the preparation of the integrated report	0.199	1.033
5	Applies a combined assurance model on risk, internal audit and others	0.345	1.196
6	Reports to the board how it carried out its responsibilities	0.251	1.315
C	**Governance of Information Technology**		
7	Board monitors and evaluates significant IT investments and expenditure	0.315	0.207
8	Board ensures that IT complies with IT laws, rules, codes and standards	0.307	0.283
9	Risk committee/other structure oversees overall risk implications of IT	0.313	0.435
10	Audit committee/other structure oversees financial risk implications of IT	0.364	0.533

Legend
** - Spearman correlation coefficient
^ - Mean difference

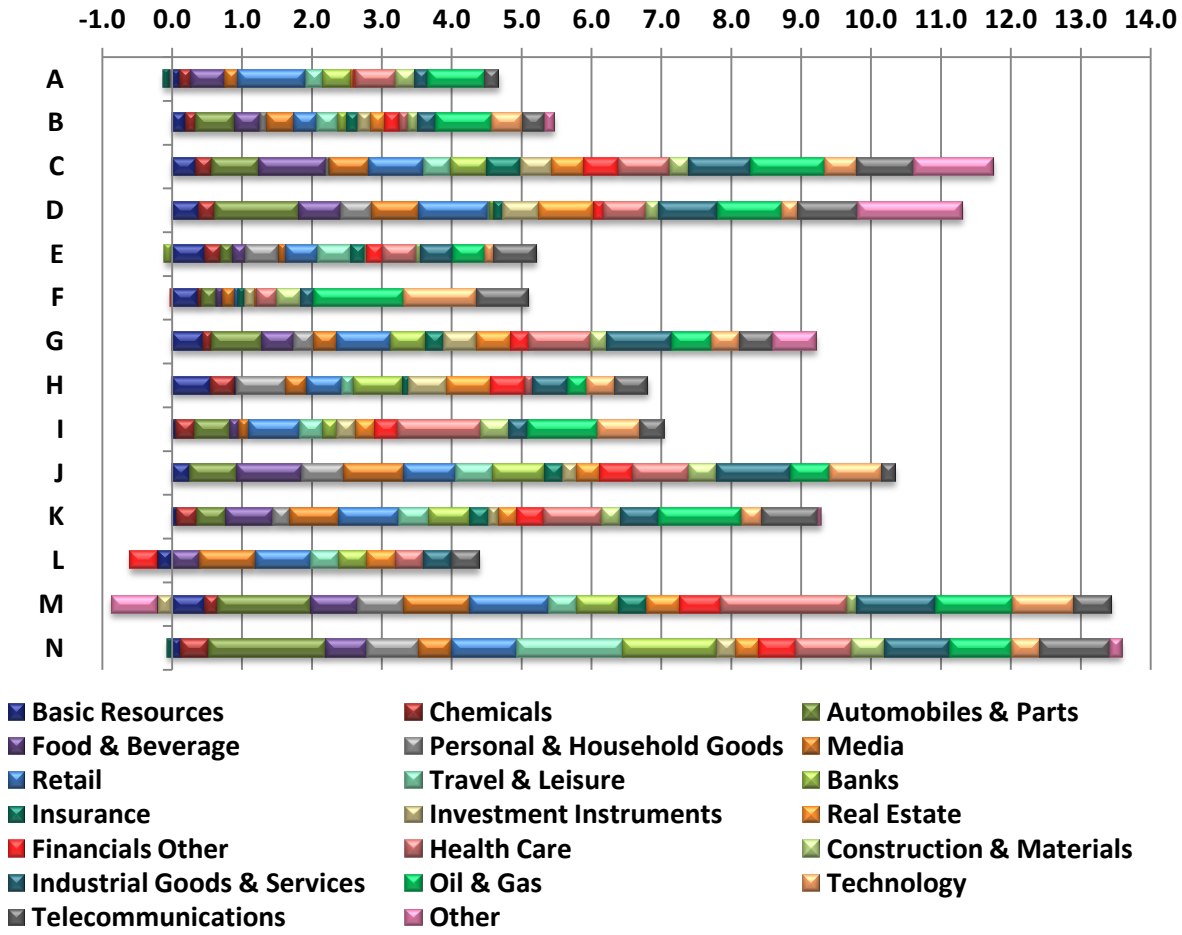
Table 1 illustrates those individual indicators for which the coefficients of correlation between the current year (2010/2011) and the base year score (2009) show significant improvement in the reporting patterns. All the mean differences are positive, implying much improved performance by companies in terms of the level of reporting against each indicator in the current year compared to the base year. It should be noted that such significant improvement in the level of reporting has been demonstrated for a very few indicators (shown in Table 1) under the three main categories, namely, Boards and Directors, Audit Committee and Governance of Information Technology (IT).

Of the 10 indicators shown in Table 1, eight are new indicators in King III (IOD, 2009), namely, (1) discloses the remuneration of the three most highly-paid employees; (2) oversees the preparation of the integrated report; (3) applies a combined assurance model on risk, internal audit and others; (4) reports to the board how it carried out its responsibilities; (5) board monitors and evaluates significant IT investments and expenditure; (6) board ensures that IT complies with IT laws, rules, codes and standards; (7) risk committee/other structure oversees overall risk implications of IT; and (8) audit committee/other structure oversees financial risk implications of IT. The remaining two indicators, that is, (1) CFO is a board member; and (2) audit committee meets at least twice a year, have been part of the King II guidelines (IOD, 2002).

The eight new indicators indicate the level of commitment by companies to start complying with the new King III recommendations (IOD, 2009). In particular, this commitment has been demonstrated by companies in terms of Information Technology, which is an important tool for companies to remain competitive. Though the other indicators did not show any significant improvement, it is nevertheless interesting to note that the South African listed companies have taken steps in terms of improving the level of their reporting.

4.4 Level of reporting by individual sectors

Figure 3 - Level of reporting by sectors



Legend
A – Ethical leadership and corporate citizenship; **B** – Boards and directors; **C** – Audit committee; **D** – Risk management committee; **E** – Remuneration committee; **F** – Nomination committee; **G** – Internal audit function; **H** – Governance of information technology; **I** – Compliance with laws, rules, codes and standards; **J** – Governing stakeholder relationships; **K** – Integrated reporting; **L** – Economic sustainability; **M** – Social sustainability; **N** – Environmental sustainability

The graph in Figure 3 shows the performance in terms of the level of reporting by individual sectors such as Basic Resources, Chemicals and Automobiles & Parts. These sectors are represented by individual colours on the graph shown against each of the main categories such as Ethical Leadership and Corporate Citizenship. Each colour represents the performance derived from the mean score differences between the current year (2010/2011) and the base year (2009). Colours lying on the right-hand side of the graph from zero depict positive (or good) performance whereas those lying on the left-hand side of the graph from zero depict negative (or bad) performance by a particular sector against each main category.

As noted on the graph, some sectors performed better than others in terms of having higher mean score differences. The Oil & Gas sector tops the chart by showing higher levels of

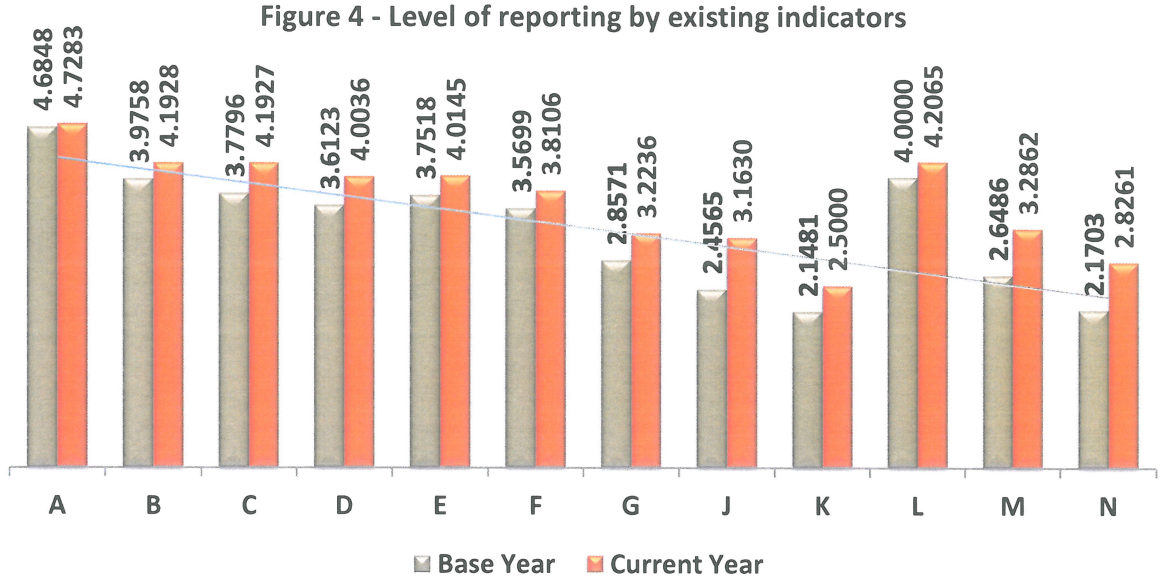
improvement in eight main categories than any other sector. Improvements for this sector have been noted in (1) Ethical Leadership; (2) Boards and Directors; (3) Audit Committees; (4) Risk Management; (5) Compliance with Laws, Rules, Codes and Standards; (6) Integrated Reporting; (7) Social Sustainability; and (8) Environmental Sustainability. It is not surprising to see this sector doing well in the majority of the main categories given the nature of products produced by companies operating in this sector. There are stringent laws governing this sector with strict requirements over and above those recommended by King III (IOD, 2009) and the JSE listing requirements (JSE, 2011).

Besides Oil & Gas, other sectors that did well in terms of the higher levels of reporting in either one or more than one category include (1) Automobiles & Parts; (2) Retail; (3) Travel & Leisure; (4) Banks; (5) Health Care; (6) Telecommunications; and (7) companies classified as Other. On the downside, the "Financials Other" and "Other" sectors performed badly in terms of Economic Sustainability and Social Sustainability respectively in the current year relative to the base year.

However, overall, the majority of the sectors performed much better against each main category in the current year when compared to the base year. These results are in line with the findings discussed in the other parts of this chapter, confirming the overall improvement in the level of reporting by the South African listed companies since King III (IOD, 2009) was released.

4.5 Level of reporting by existing indicators as per the King II report

Figure 4 - Level of reporting by existing indicators



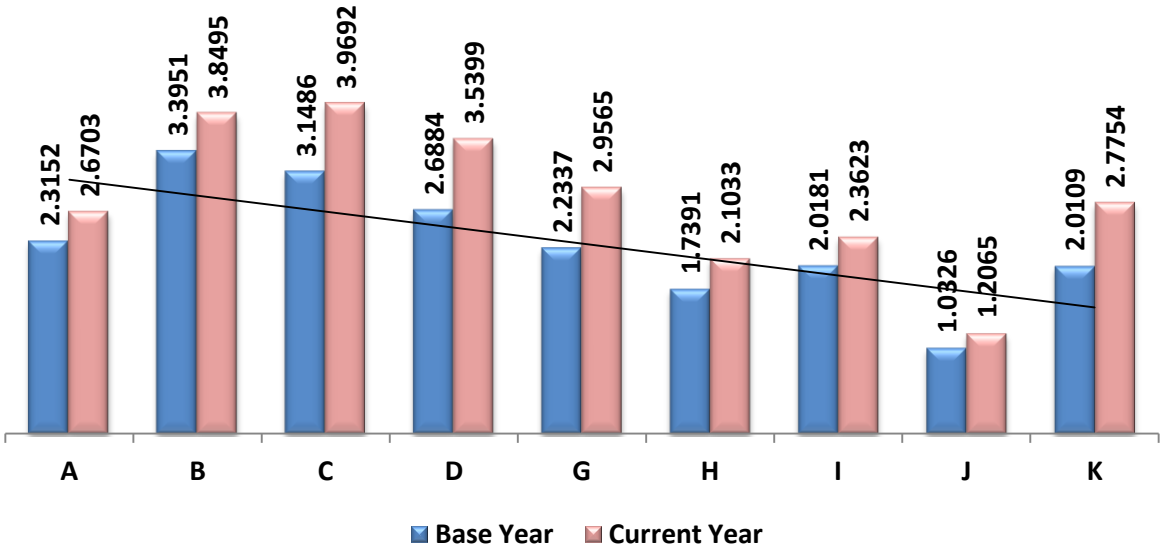
Legend
A – Ethical leadership and corporate citizenship; **B** – Boards and directors; **C** – Audit committee; **D** – Risk management committee; **E** – Remuneration committee; **F** – Nomination committee; **G** – Internal audit function; **H** – Governance of information technology; **I** – Compliance with laws, rules, codes and standards; **J** – Governing stakeholder relationships; **K** – Integrated reporting; **L** – Economic sustainability; **M** – Social sustainability; **N** – Environmental sustainability

The objective of the analysis in this section was to determine if the level of reporting by companies had improved in the current year (2010/2011) relative to the base year (2009) despite the fact that the indicators had been in existence since the publication of King II report in 2002 (IOD, 2002). Under normal circumstances, there should not be much difference in the level of reporting in the current year relative to the base year given the same set of indicators in both years.

Surprisingly, the results in Figure 4 show an improvement in the level of reporting in the current year compared to the previous year. This is an important finding which confirms the change of attitude by companies subsequent to the publication of King III (IOD, 2009). This change of attitude is also attributable to changes made to the Companies Act (Companies Act, 2008) dealing with the roles of the audit committees. In addition, the JSE listing requirements (JSE, 2011) require companies to comply with the King III guidelines or to provide reasons for failing to do so.

4.6 Level of reporting by new indicators as per the King III report

Figure 5 - Level of reporting by new indicators



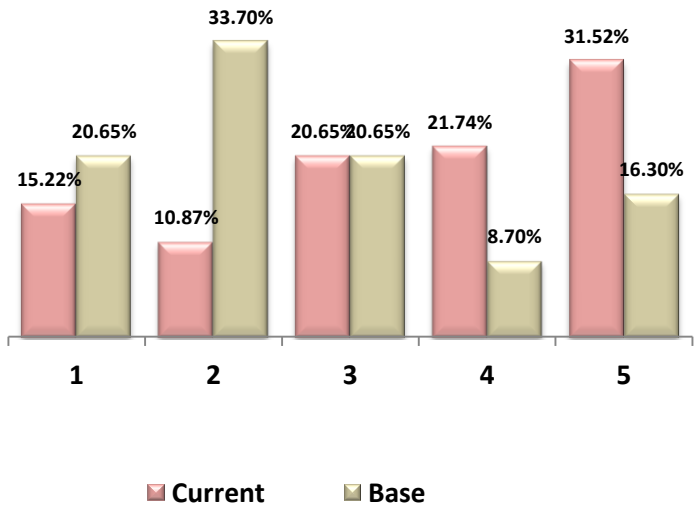
Legend
A – Ethical leadership and corporate citizenship; **B** – Boards and directors; **C** – Audit committee; **D** – Risk management committee; **E** – Remuneration committee; **F** – Nomination committee; **G** – Internal audit function; **H** – Governance of information technology; **I** – Compliance with laws, rules, codes and standards; **J** – Governing stakeholder relationships; **K** – Integrated reporting; **L** – Economic sustainability; **M** – Social sustainability; **N** – Environmental sustainability

The results In Figure 5 show improvement in the level of reporting in the current year (2010/2011) compared to the base year (2009), using the new indicators from King III (IOD, 2009). In the absence of any other information, these results could be confusing given that one would have expected non compliance by companies in the base year.

However, the results indicate that the King Committee might have been involved in an extensive consultative process with companies to determine the trends in reporting subsequent to King II (IOD, 2002). This process might have resulted in some of the good practices by companies being incorporated into the King III guidelines (IOD, 2009). Therefore, in some companies, the King III guidelines are a new phenomenon whereas in other companies such guidelines are an extension of the existing practices in their operations. It therefore explains why the new guidelines appear to have existed in the base year.

4.7 Harmonisation between components of integrated reporting

Figure 6 (a) Tone on integrated reporting components in introduction, chairman's and CEO's commmentary

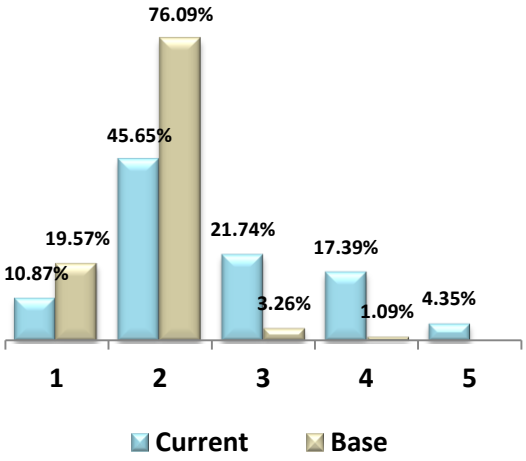


Legend
1 – None compliance; **2** – Little detail provided, **3** – Some detail provided; **4** – More detail provided; **5** – Much detail provided

Figure 6(a) illustrates how companies have performed in terms of reporting on the components of integrated reporting based on the commentaries by the chairmen, chief executives and other executives within companies. The graph shows that, on the scale of "1" to "5" where "1" means "non compliance" and "5" means "much compliance", companies

improved significantly in covering integrating reporting issues in the current year (2010/2011) relative to the base year (2009) in the form of commentaries by top executives.

Figure 6 (b) Harmonisation of integrated reporting components



Legend
1 – None compliance; **2** – Little detail provided, **3** – Some detail provided; **4** – More detail provided; **5** – Much detail provided

Figure 6(b) was intended to illustrate how companies managed to show connections between the integrated reporting components, namely, strategy, risk, corporate governance, financial performance and sustainability. Figure 6(b) shows much improvement in terms of harmonisation in the components of integrated reporting in the current year relative to the base year.

Chapter 5 Conclusion and Recommendations

The purpose of this research was to determine whether the level of reporting by South African listed companies has improved since the issue of King III in March 2010 (IOD, 2009). King III encourages companies to embrace the concept of integrated reporting in which they are expected to report on their strategies, corporate governance, risk assessment, financial performance and sustainability dimensions, and to show how these components are connected to one another to enable stakeholders to assess their performance holistically in terms of their ability to create and sustain value (IOD, 2009, SAIRC Discussion Paper, 2011).

As the cornerstone of good corporate governance practices, this study appreciates the importance of adopting the values of transparency, accountability, responsibility and fairness in all spheres of business operations and across all the government institutions to restore faith in the capital markets (IOD, 2009). Once adopted, these values help to encourage managers to provide relevant information of interest to the stakeholders. In addition, companies are required to address economic, social and environmental impacts to ensure their future success (IOD, 2009; GRI, 2011). According to the United Nations, companies failing to address these sustainability considerations have no future in the 21st century, as they are likely to lose reputation among the societies in which they operate (GRI, 2011; UN Global Compact, 2000). This will eventually force them out of the business.

The study made use of 111 key research indicators, grouped under the main categories, chosen mainly from King III (IOD, 2009) and the GRI (2011). However, a few research indicators were based on the researcher's judgement. Grouping them this way facilitated comparison in reporting between the current year (2010/2011) and the base year (2009). The research indicators were carefully chosen to address the main components of integrated reporting encompassing strategies, risk, corporate governance and sustainability. Some of the indicators were specifically chosen to determine the harmonisation of information in the annual reports, which is the essence of this study to demonstrate the link between the components of integrated reporting.

Overall, the results confirmed improvement in the level of reporting by South African listed companies in the current year relative to the base year. In some instances, this improvement was significant especially when comparisons were made between companies having issued integrated annual reports and those without. The results showed that companies with

integrated annual reports made more effort in terms of improving the level of their reporting than those without integrated annual reports. The results further confirmed that companies without integrated annual reports were already lagging behind those with such reports and might lose out in terms of competitiveness.

Significant improvement was also noted in the case of eight individual indicators grouped under Audit Committees, Information Technology and Internal Audit. With regard to Audit Committees, these results were expected to confirm compliance by companies with the King III recommendations (IOD, 2009) as well as the Companies Act (Companies Act, 2008). In the case of IT, the results signified the importance of companies implementing appropriate strategies for information systems in order to enable them to gain competitive advantage over their rivals.

In line with the International Integrated Committee's (IIRC) thinking (IIRC Discussion Paper, 2011), this study acknowledges that integrated reporting is a new concept not only in South Africa but internationally. It will therefore take a considerable time before the intended objectives of integrated reporting are fully met by companies. While South African listed companies are no exception in this regard, it is interesting to notice improvement in the level of their reporting. Part of this improvement is attributed to the King III guidelines (IOD, 2009) and the South African Discussion Paper on Integrated Reporting (SAIRC Discussion Paper, 2011) in encouraging companies to make integrated reporting part of their businesses. In addition, the JSE listing requirements (JSE, 2011) urge listed companies to comply with King III or to provide reasons for failing to do so.

As a new concept, integrated reporting has opened the doors for future research. In its Discussion Paper (IIRC Discussion Paper, 2011), the IIRC has voiced its intentions to publish an Exposure Draft on integrated reporting in 2012 once it has received comments from various organisations and the public. It is therefore suggested that future research can take different forms including exploring the extent to which the level of reporting by South African or international companies will have improved after the Exposure Draft has been published. Researchers can decide to replicate the same research indicators as those used in this study or to use different research indicators.

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Appendix A Research Indicators

Notes on how to find the source of research indicators

1. The research indicators were extracted from the three sources, namely, (1) King III report; (2) Global Reporting Initiative (2011); and (3) Researcher's own research indicators.
2. The source of each research indicator is provided next to that research indicator..
3. Most of the paragraphs, for example, Par. 7 or Principle 2.23, refer to the paragraph or principle quoted in a chapter from the King III report. Otherwise, a different source such as Global Reporting Initiative or Researcher's own research indicators will be provided.
4. Whenever a paragraph or principle referring to the King III report is provided, it is also important to note the chapter from which the paragraph or principle was extracted. Each chapter is provided next to the main category.

A. Ethical leadership and corporate citizenship [King III – Chapter 1]

1. Effective leadership based on ethical values such as integrity, honesty, independence, accountability and trust can be ascertained from the integrated report. **[Par. 1]**
2. Company strategies and vision are clearly outlined. **[Par. 7, 9, 35]**
3. Mission statement and company values are provided. **[Par. 9, 10]**
4. Ethical standards are articulated in the code of conduct. **[Par. 12-15]**
5. Independent assurance of ethics by internal audit or external assurance providers. **[Par. 52]**

B. Boards and directors [King III – Chapter 2]

6. Company is governed by a unitary board of directors. **[Par. 62]**
7. Directors are appointed through a formal process. **[Principle 2.19, Par. 80-82]**
8. Board is comprised of the majority of non executive directors. **[Par. 64]**
9. Of the non executive directors, the majority are independent. **[Par. 64]**
10. Board is chaired by a non executive independent director. **[Par. 38]**
11. Board has appointed a lead independent director, if the chairman is not independent. **[Par. 38]**
12. The CEO is a board member. **[Par. 47, 73]**
13. The financial director (or CFO) is a board member. **[Par. 47, 73]**
14. Qualifications and experience of directors are disclosed. **[Par. 88]**
15. Board is assisted by a competent, suitably qualified and experienced company secretary. **[Principle 2.21]**
16. Board is regulated by a formal charter which sets out the role of the board and each director. **[Par. 1]**
17. Appointment of well-structured committees to deal with key functions of the board, which include separate audit, risk, remuneration and nomination committees as a minimum. **[Principle 2.23, par. 130]**
18. Committees are regulated by formal charters which set out the role of individual committees. **[Par. 125-126]**
19. Board meets at least 4 times a year. **[Par. 1]**
20. Satisfactory attendance of board meetings as per the attendance register. **[Researcher's own indicator]**
21. Induction programme for new directors is in place. **[Par. 89-90]**
22. Ongoing training for all directors is in place. **[Par. 92]**
23. Performance of the board, individual directors and committees is evaluated on a regular basis. **[Par. 109-114]**
24. Share option scheme is not available to non executive directors. **[Par. 154]**
25. Policy is in place for appointment and retirement of directors. **[Par. 74-75, 80-82]**
26. Remuneration of directors and senior executives is disclosed. **[Par. 180]**

27. Remuneration of the three most highly-paid employees (other than directors) is disclosed. **[Par. 180]**
28. Remuneration policy regarding directors is approved by the shareholders. **[Par. 186]**

C. Audit Committees [King III – Chapter 3]

29. Audit committee is appointed by the board (through the nomination committee) and is approved by the shareholders. **[Par. 3]**
30. Formal charter and processes are in place outlining the functions of the audit committee. **[Par. 6 of Audit Committees, Par. 125,126,129&134 of Boards & Directors]**
31. Suitably skilled and experienced independent non executive directors. **[Principle 3.2, Par. 12-15]**
32. Comprised of at least three non executive, independent directors. **[Par. 10]**
33. Chairman of the Board is not a member of the audit committee. **[Par. 11]**
34. Chaired by a non executive, independent director, other than the chairman of the Board. **[Principle 3.3]**
35. Meets at least 2 times a year. **[Par. 7]**
36. Satisfactory attendance of audit committee as per attendance register. **[Par. 7]**
37. Oversees internal and financial controls. **[Par. 30, 64, 66-70]**
38. Oversees internal audit function. **[Par. 66-70, Principle 7.4 of Internal Audit Function]**
39. Oversees financial risk management (and other risks if necessary). **[Par. 64, 65]**
40. Assesses the performance, expertise and skills of the financial function including financial director. **[Par. 51, 52]**
41. Oversees the preparation of the integrated report (including sustainability issues). **[Principle 3.4, Par. 24-29]**
42. Audit committee (or company as a whole) applies a combined assurance model in providing assurance on activities such as risk, compliance, internal audit and governance. **[Principle 3.5, Par. 46-48]**
43. Evaluates independence and credentials of the external auditor. **[Par. 77]**
44. Evaluates performance of the external auditor. **[Par. 77]**
45. Reports to the board and shareholders how it carried out its responsibilities. **[Principle 3.10, Par. 83-85]**

D. Risk management committee [King III – Chapter 4; Researcher's own indicator]

46. Board appoints risk and/or audit committee to oversee risk management. **[Par. 16]**
47. Risk (or audit) committee consists of at least 3 directors (both executive and non executive). **[Par. 20, 21]**
48. It is chaired by an independent non executive director, other than chairman of the board or the executive director (not required by King III but considered necessary for the purposes of this research). **[Researcher's own indicator]**
49. Formal charter and processes are in place outlining the functions of the risk/audit committee. **[Par. 5]**
50. Risk (or audit) committee meets at least 2 times a year. **[Par. 22]**
51. Satisfactory attendance of risk (or audit) committee as per attendance register. **[Researcher's own indicator]**
52. Risk committee (or audit/board) identifies key financial risks and quantify them, if possible. **[Par. 31-34, 40, 41-43]**
53. Risk committee (or audit/board) identifies key non financial risks and quantify them, if possible. **[Par. 31-34, 41-43]**
54. Risk committee (or audit/board) explains how the identified financial risks will be addressed. **[Par. 31-34, 40, 41-43]**
55. Risk committee (or audit/board) explains how the identified non financial risks will be addressed. **[Par. 31-34, 41-43]**
56. Risk committee (or audit/board) sets levels of risk tolerance. **[Principle 4.2, Par. 11-15]**
57. Risk committee (or audit/board) expresses its views on the effectiveness of the company's risk management processes. **[Par. 4]**

E. Remuneration committee [King III – Chapter 2]

58. Remuneration committee comprises at least 2 non executive and independent directors. **[Researcher's own indicator]**
59. It is chaired by an independent non executive director, other than the chairman of the Board or executive director. **[Par. 131 of Boards & Directors]**
60. Formal charter and processes are in place outlining the functions of the remuneration committee. **[Par. 125,126&134 of Boards & Directors]**
61. Remuneration committee meets at least 2 times a year (not required by King III but considered necessary for the purposes of this research). **[Researcher's own indicator]**
62. Satisfactory attendance of remuneration committee as per attendance register. **[Researcher's own indicator]**
63. Remuneration committee or other structure determines remuneration of executive and non executive directors. **[Par. 150 of Boards & Directors]**

F. Nomination committee [King III – Chapter 2]

64. Nomination committee comprises at least 2 non executive and independent directors. **[Researcher's own indicator]**
65. It is chaired by an independent non executive director, who can also be the chairman of the Board, other than the executive director. **[Par. 131 of Boards & Directors]**
66. Formal charter and processes are in place outlining the functions of the nomination committee. **[Par. 125,126&134 of Boards & Directors]**
67. Nomination committee meets at least 2 times a year (not required by King III but considered necessary for the purposes of this research). **[Researcher's own indicator]**
68. Satisfactory attendance of nomination committee as per attendance register. **[Researcher's own indicator]**
69. Nomination committee or other structure recommends the appointment and dismissal of executive and non executive directors. **[Par. 79 of Boards & Directors]**
70. Directors nominated by the committee or other structure are presented for approval by the shareholders. **[Par. 80 of Boards & Directors]**

G. Internal audit function [King III – Chapter 7]

71. Internal audit function has been set up (within the company or externally). **[Par. 1]**
72. Internal audit function reports to the audit committee. **[Par. 24, 33]**
73. Internal audit is headed by the chief audit executive (CAE) or external company. **[Par. 11]**
74. Internal audit (or its CAE) / external company attends audit committee meetings, board meetings by invitation. **[Par. 28, 29, 34]**
75. Internal audit/other structure provides assurance on the effectiveness of internal control environment. **[Principle 7.3, Par. 2, 12-17]**
76. Internal audit/other structure provides assurance on the effectiveness of risk management. **[Principle 7.3, Par. 2, 12-17]**
77. Internal audit/other structure provides assurance on the effectiveness of governance (including ethics). **[Par. 2]**
78. Internal audit is subjected to an independent quality review. **[Par. 23]**
79. Internal audit follows a risk-based approach to its plan. **[Principle 7.2, Par. 7, 18]**

H. Governance of information technology [King III – Chapter 5]

80. Board or other structure monitors and evaluates significant IT investments and expenditure. **[Principle 5.4]**
81. A suitably qualified and experienced chief information officer (CIO) is appointed to manage IT. **[Par. 20]**
82. Board or other structure ensures that IT complies with IT related laws, rules, codes and standards. **[Par. 33]**

83. Risk committee or other structure oversees overall risk implications of IT. **[Par. 30-34; 43-47]**
84. Audit committee or other structure oversees financial risk implications of IT. **[Par. 47]**
85. Board receives an independent assurance on the effectiveness of IT through internal audit function and/or external assurance providers. **[Par. 28]**

I. Compliance laws, rules, codes and standards [King III – Chapter 6]

86. Compliance function has been set up by the company. **[Par. 16]**
87. Compliance function/other structure oversees compliance with laws, rules, codes and standards. **[Principle 6.1]**
88. Company discloses non binding rules, codes and standards to which it adheres. **[Par. 6]**

J. Governing stakeholder relationships [King III – Chapter 8; Global Reporting Initiative, 2011]

89. Board identifies key stakeholders and their interests on a regular basis. **[Par. 7, 8 of King III]**
90. Interests of key stakeholders are taken into account in the integrated report. **[Par. 7, 9 of King III]**
91. Explanation of the process used for rating topics in the order of priority. **[Global Reporting Initiative, 2011]**

K. Integrated reporting [King III – Chapter 9; Global Reporting Initiative, 2011; Researcher's own indicators]

92. Financial and sustainability issues on economic, social and environmental all covered in one or more documents of integrated report. **[Par. 1]**
93. Tone on integrated reporting components is articulated, hinted or summarised in the introductory section, chairman's report or CEO's report within the integrated report. **[Researcher's own indicator]**
94. Information on integrated reporting components is harmonised and a link drawn to show interdependencies between these components in the integrated report. **[Researcher's own indicator]**
95. Sustainability issues and disclosures are independently assured (under the auspices of the audit committee or other structure). **[Principle 9.3; Par. 17-21]**
96. Report clearly indicates whether King III / II guidelines have been followed. **[Researcher's own indicator]**
97. Report clearly states areas of improvement on King III / II guidelines. **[Researcher's own indicator]**
98. Report clearly indicates whether Global Reporting Initiative (GRI) guidelines have been followed. **[Global Reporting Initiative, 2011]**
99. Report clearly states areas of improvement on Global Reporting Initiatives (GRI) guidelines. **[Researcher's own indicator]**
100. Index is provided as per Global Reporting Initiatives (GRI) guidelines. **[Global Reporting Initiative, 2011]**
101. Glossary of Terms provided as per Global Reporting Initiatives (GRI) guidelines or other guidelines. **[Global Reporting Initiative, 2011]**
102. Report provides proper referencing with page numbers for each major issue covered. **[Global Reporting Initiative, 2011]**

L. Economic Sustainability [Global Reporting Initiative, 2011; Researcher's own indicators]

103. Value-add statement and other economic/value-add information are provided. **[Page 25-26 of Global Reporting Initiative, 2011]**
104. Quantification of economic efforts. **[Researcher's own indicator]**
105. Report is easy to read. **[Researcher's own indicator]**

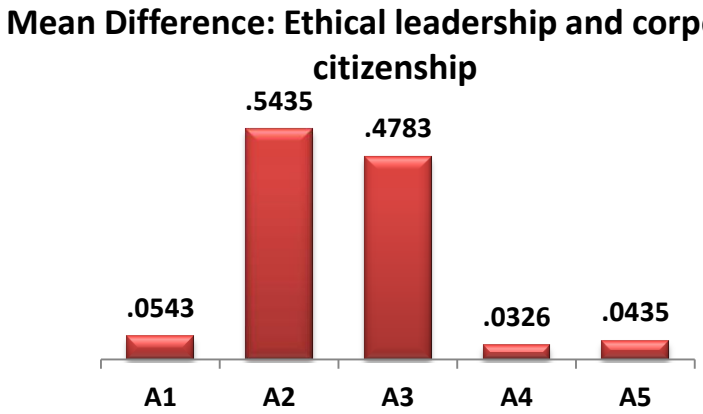
M. Social Sustainability [Global Reporting Initiative, 2011; Researcher's own indicators]

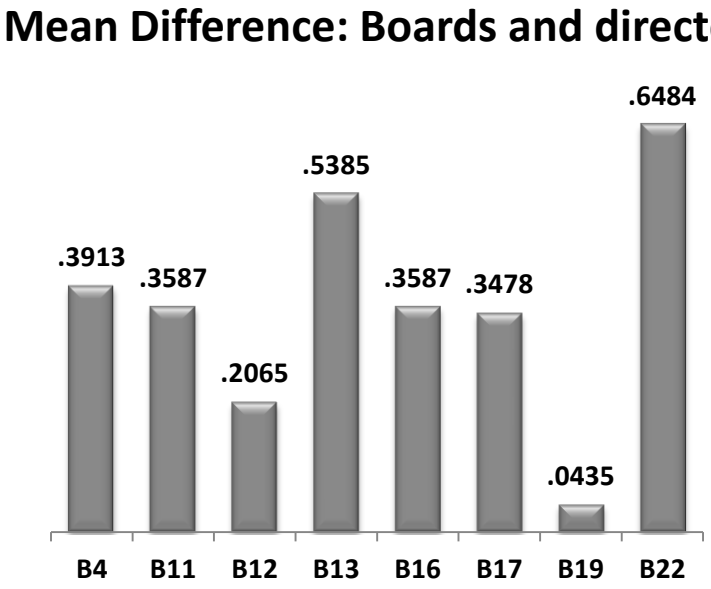
106. Involvement in CSI programmes for employees and communities such as training, education, sports, HIV/AIDS, donations, bursaries. **[Page 29-37 of Global Reporting Initiative, 2011]**
107. Quantification of costs as well as the number of social projects/programmes. **[Researcher's own indicator]**
108. Report is easy to read. **[Researcher's own indicator]**

N. Environmental Sustainability [Global Reporting Initiative, 2011; Researcher's own indicators]

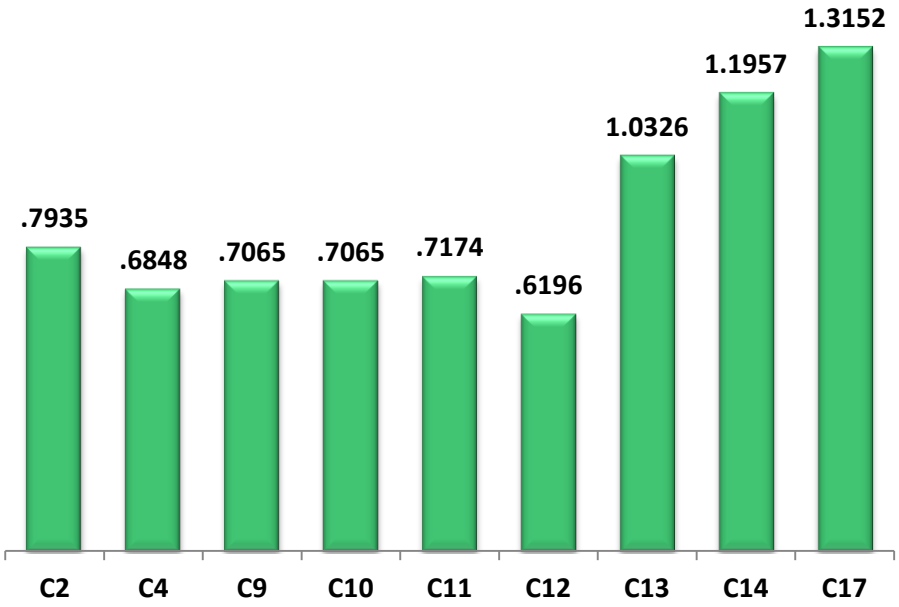
109. Implementation of sound environmental programmes. **[Page 27-29 of Global Reporting Initiative, 2011]**
110. Quantification of costs incurred and efforts to curb environmental damages. **[Researcher's own indicator]**
111. Report is easy to read. **[Researcher's own indicator]**

Appendix B Mean Differences per Individual Categories

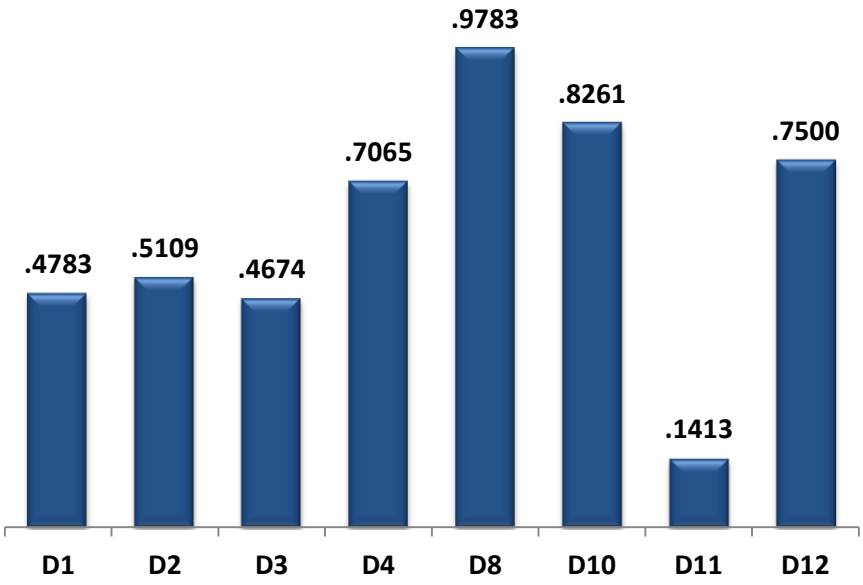




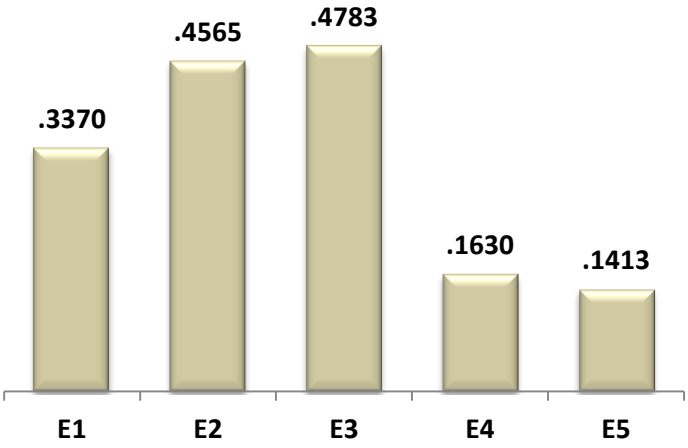
Mean Difference: Audit committee



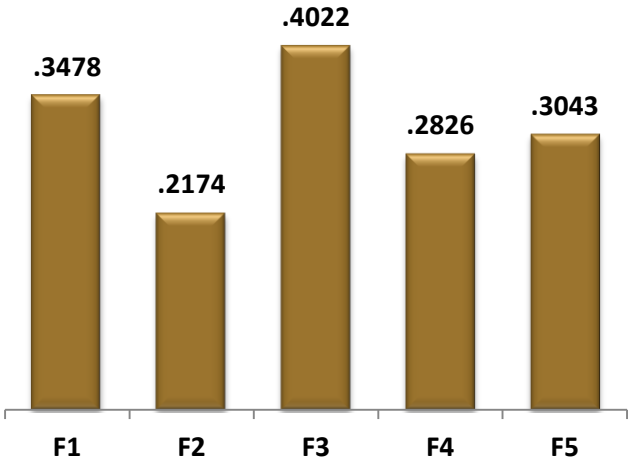
Mean Difference: Risk management committee



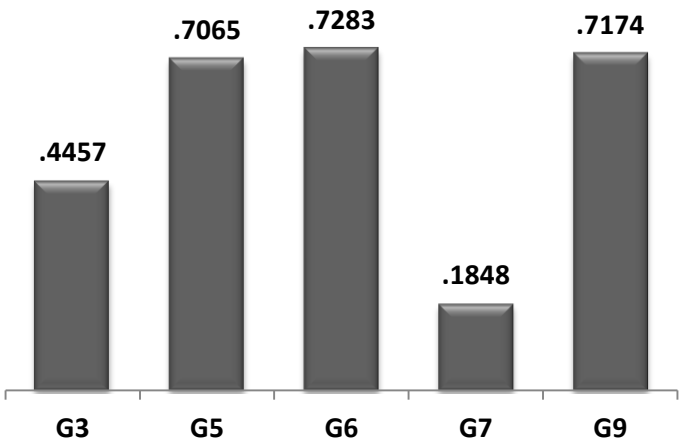
Mean Difference: Remuneration committee



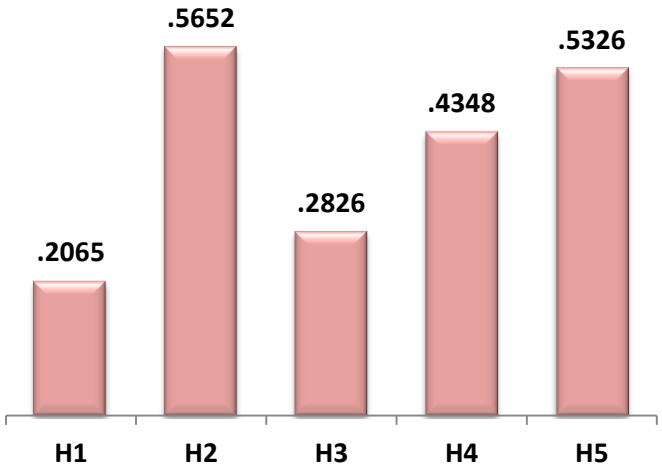
Mean Difference: Nomination committee



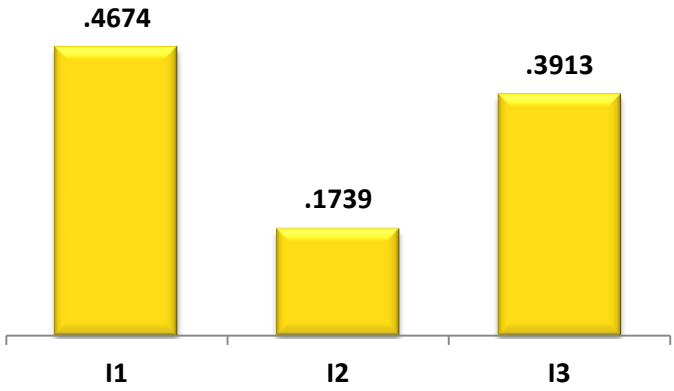
Mean Difference: Internal audit function



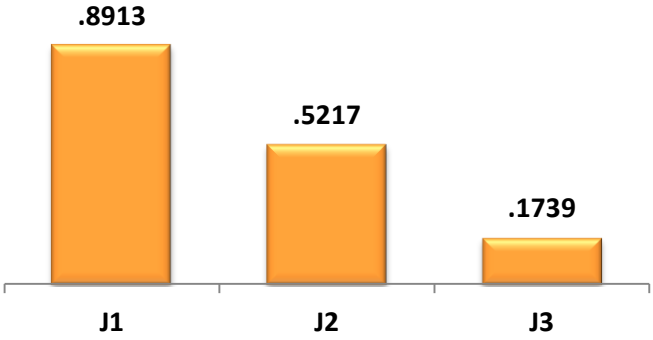
Mean Difference: The governance of information technology



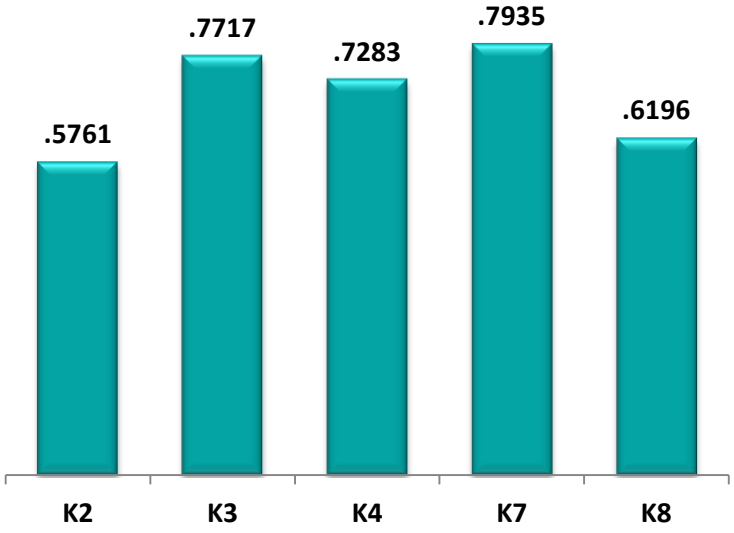
Mean Difference: Compliance with laws, rules, codes and standards



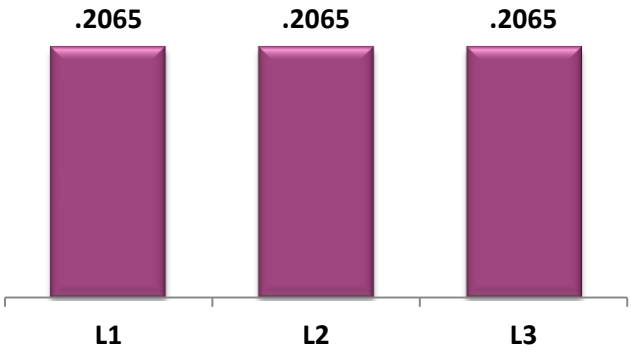
Mean Difference: Governing stakeholder relationships



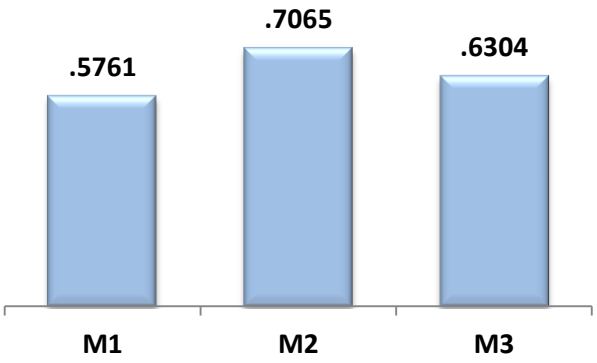
Mean Difference: Integrated reporting



Mean Difference: Sustainability - economic



Mean Difference: Sustainability - social



Mean Difference: Sustainability - environmental

