

**Trends in integrated reporting by
JSE listed companies: an analysis of
the integration of financial
performance with corporate
governance disclosures and
economic, social and environmental
sustainability reporting**

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ABSTRACT

With changes in international governance trends leaning towards integrated reporting, and the inclusion of good governance practices in the Companies Act No. 71 of 2008, it has become imperative for companies to embrace integrated reporting in order to be, and also be seen to be, responsible with regard to social, environmental and economic issues. The purpose of this report is to investigate the trends in the extent of integrated reporting by companies listed on the Johannesburg Stock Exchange (JSE). The report sought to investigate compliance with the recommendations of the King Report and Code of Governance Principles for South Africa 2009 (King III) by companies listed on the JSE. The report assesses the extent of reporting and disclosures made by companies in relation to the specific recommendations contained in the various chapters of King III since the inclusion of King III in the JSE listing requirements for financial years beginning on or after 1 March 2010. The report also assesses the extent of economic, social and environmental sustainability reporting as required by the Global Reporting Initiative (GRI) guidelines. The annual integrated reports of fifty-two companies listed under the various sectors of the JSE were examined to determine whether there had been significant changes in the specific disclosures provided by these companies, as recommended by King III, from 2010 to 2012. The key findings of the study show that although there has been an increase in the level of disclosure by companies, this change was not significant over the three-year period. The results also show that much improvement is needed in disclosures relating specifically to the new King III sections of risk management, compliance management and IT governance.

Key words: corporate governance, disclosure, financial performance, integrated reporting, non-financial information, sustainability

DECLARATION

I, Nkabaneng Tebogo Mashile, declare that this research report is my own work except as indicated in the references and acknowledgements. It is submitted in partial fulfilment of the requirements for the degree of Master of Commerce in the University of the Witwatersrand, Johannesburg. It has not been submitted before for any degree or examination in this or any other university.

Nkabaneng Tebogo Mashile

Signed at Johannesburg

On the 2nd day of July, 2015

DEDICATION

THIS IS FOR KATLEGO PHENYO MASHILE AND LETHABO POTEGO MASHILE, MY BIGGEST CHEERLEADERS THROUGHOUT THIS PROCESS.

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I would like to thank my supervisors, Yaeesh Yasseen and Professor Nirupa Padia, for their guidance and support. Thank you for remaining positive even when I couldn't see the light at the end of the tunnel.

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CHAPTER 1: INTRODUCTION

1.1 Purpose of the study

The purpose of this research was to investigate the trends in the extent of integrated reporting by companies listed on the Johannesburg Stock Exchange (JSE). The report sought to investigate compliance with the recommendations of the King Report and Code of Governance Principles for South Africa 2009 (King III) by companies listed on the JSE.

The effect of the King III has been examined by a number of studies. One of the studies was Makiwane and Padia (2013) who conducted a study to evaluate the way in which the transition from King II to King III affected companies' reporting, using 2009 as the base year for their study and 2010/2011 as the current year. The focus of their study was to evaluate the differences in reporting on governance issues under King II as opposed to King III. Makiwane and Padia (2013) accordingly found that, if the purpose of integrated reporting is to be achieved, improvement would be required in the way that companies reported.

This study builds on Makiwane and Padia's (2013) recommendation for further studies to be conducted on the extent to which integrated reporting by JSE listed companies has improved. While Makiwane and Padia's (2013) study focuses on changes in reporting caused by the introduction of King III, this report evaluates the way in which the integration of financial reporting, corporate governance reporting and economic, social and environmental sustainability reporting has evolved since the introduction of King III. With the launching of the EY (EY, 2012) and Nkonki (Nkonki, 2011) integrated reporting awards, focusing on the top 100 JSE listed companies, this study sought to assess how companies of various sizes listed in the various sectors of the JSE have applied the recommendations of King III in their reporting. This was achieved by evaluating the trends in the extent of integrated reporting by companies listed on the JSE since the inclusion of King III in the JSE listing requirements for the financial years beginning on or after 1 March 2010. The report examines the extent of the reporting and the

disclosures made by companies in relation to the recommendations contained in the various chapters of King III, in order to determine whether there have been significant changes in the disclosures provided by these companies from 2010 to 2012. The report also assesses the extent of economic, social and environmental sustainability reporting as required by the Global Reporting Initiative (GRI) guidelines.

1.2 Context of the study

South Africa's transition to democracy "involved an economic transition from a closed, racially integrated economy to a gradually globalising, more open economy" (Seo, 2008, p. 8). In 2003, the country also saw the harmonisation of its Statements of Generally Accepted Accounting Practices (GAAP) with the International Financial Reporting Standards (IFRS). Since then, during 2012, the SA GAAP has been withdrawn further, highlighting South Africa's commitment to world class reporting (The Accountant Editorial, 2012). Rensburg and Botha (2014) note that South Africa has, furthermore, taken the lead in adopting integrated reporting and is thus at the forefront in terms of financial reporting and corporate governance. In line with this position, PwC (2012) asserts that South Africa is seen as the leader in integrated reporting.

With changes in international governance trends leaning towards integrated reporting, and the inclusion of good governance practices in the new Companies Act no. 71 of 2008, it has become imperative for companies to embrace integrated reporting in order to be, and also to be seen to be, responsible with regard to social, environmental and economic issues (IOD, 2009).

In South Africa, the first King Report on Governance (King I) was published in 1994. The recommendations of King I included, among others, standards of conduct for directors and boards of directors and also encouraged practices of good corporate governance (IOD, 1994). King II was issued in 2002 as a revision to King I and included new sections on sustainability, the role of the board and risk management (IOD, 2002). King III was issued in 2009 and contains

guidelines and recommendations regarding integrated reporting and disclosure, among other requirements (IOD, 2009). King III focuses on the importance of companies to report annually on how their operations have both positively and negatively influenced the lives of the communities in which they operate and further recommends that companies should also disclose how they intend to improve the positive characteristics and do away with the negative features in coming years. The key recommendation of King III is for companies to issue an integrated report that explains the relationship between the company's financial and non-financial performance, rather than a separate annual report and sustainability report (IOD, 2009).

1.3 Problem statement

King III is not legislation (IOD, 2009); the Code provides recommendations that work on an apply-or-explain basis. As such, this report seeks to investigate how companies have interpreted and reported on the recommendations of King III.

The purpose of this report is to investigate the trends in the extent of integrated reporting by companies listed on the JSE. The report seeks to investigate compliance with the recommendations of the King Report and Code of Governance Principles for South Africa 2009 (King III) by companies listed on the JSE. The report also assesses the extent of reporting and the disclosures made by companies in relation to the recommendations contained in the nine chapters of King III, including ethical leadership and corporate citizenship, boards and directors, the audit committee, the governance of risk, the governance of information technology, compliance with laws, rules, codes and standards, internal audit, governing stakeholder relationships, integrated reporting and disclosure. This report also assesses the extent of economic, social and environmental sustainability reporting demonstrated in company reports, as required by GRI guidelines.

1.4 Significance of the study

In the introduction and background to King III, Mervyn King (chairman of the King Committee) notes that surveys have shown that although the stakeholders of companies value the quality of companies' products and services, they also have as a priority the need to trust and have confidence in the company (IOD, 2009). King posits that by providing forward-looking integrated information, companies increase stakeholders' trust and confidence (IOD, 2009).

The objective of King III is not to replace financial activities; nevertheless, Mervyn King (in the introduction and background to King III) stresses that financial results merely represent a "photograph of a moment in time" of a company's position; he asserts that it is important for companies to embrace sustainability and integrated reporting in order to provide information on value matters that are not accounted for, such as future earnings, brand, goodwill, the quality of its board and management, reputation, strategy and other sustainability aspects in order to enable investors to make an assessment of the economic value of a company (IOD, 2009).

Rensburg and Botha (2014) and PwC (2012) note how South Africa has taken the lead in adopting integrated reporting. The country is thus at the forefront of global financial reporting and corporate governance and is also seen as a leader with regard to integrated reporting. Furthermore, EY (2012) posits that although integrated reports prepared during 2012 were not prepared according to a framework, they still resulted in companies presenting a link between their financial and non-financial performance.

By assessing the extent of reporting by companies, this study seeks to establish whether the principles of good governance and the recommendations for integrated reporting (as contained in King III) have been embraced and therefore have influenced the way in which companies report information to their stakeholders. The study further seeks to ascertain whether there have been any significant changes in the specific disclosures made from 2010 to 2012. Finally, this study aims to establish whether, through integrated reporting, companies

have successfully made the link between their financial and non-financial performance.

1.5 Delimitations of the study

Owing to the fact that it is a JSE listing requirement for companies to comply with the recommendations of King III and produce integrated reports, the scope of this research will be limited to the South African context, with a specific focus on companies listed on the JSE. In addition, the study looks at the level of reporting by these companies over the three-year period from 2010 to 2012.

CHAPTER 2: LITERATURE REVIEW

2.1. Introduction

Solomon and Solomon (2004), Steyn and De Beer (2011) and Deloitte (2012) assert that the collapse of companies like Enron together with the 2008 global financial crisis have raised questions about the efficiency of the financial reporting system. In order to assess the mechanisms that are in place to ensure that managers fulfil their fiduciary duties responsibly, a brief look at the role of agency theory in corporate governance is necessary.

In explaining agency theory, Jensen and Meckling (1976) state that an agency relationship involves an agent and principal(s); in this relationship the principal(s) entrust the agent with decision-making powers relating to the affairs of the principal(s). Jensen and Meckling (1976) further explain that inherent in such relationships is the risk that the agent may not always act in the best interests of the principal(s). Therefore there is a need to put systems in place that will align the agent's and principal's interests and encourage the agent to act in the principal's best interests (Fontrodona & Sison, 2006). One may thus conclude that corporate governance in South Africa is aligned with agency theory, as the emphasis is placed on management's duty to maximise value responsibly for shareholders, while taking other stakeholder's interests into account.

Since the inefficiencies in the financial reporting system were cited as contributors to the collapse of companies like Enron and the 2008 global financial crisis, before discussing the requirements of King III in detail this chapter will look briefly at traditional financial reporting, the weaknesses that have been identified in the financial reporting system, the need for and usefulness of reporting on non-financial information and, finally, the requirements and objectives of King III.

2.2. Traditional financial reporting

In companies, a traditional or conventional set of financial statements is prepared and presented in terms of the International Financial Reporting Standards (IFRS). Indeed, the International Accounting Standard 1: Presentation of Financial Statements (IAS 1) states that entities shall apply this standard in preparing and presenting a set of financial statements (IASB, 2013a). The IASB (2013a) also refers to other IFRS with regard to the recognition, measurement and disclosure requirements for specific transactions. Additionally, the Framework for the Preparation and Presentation of Financial Statements (Conceptual Framework) provides guidance on the concepts that underlie the preparation and presentation of financial statements (IASB, 2013e). The Conceptual Framework addresses, among other issues, the objective of financial statements and the qualitative characteristics that enhance the usefulness of information contained in financial statements (IASB, 2013e).

Objectives and components of financial statements

In both the Conceptual Framework and IAS 1, the IASB (2013e) states that the objective of financial statements is to provide information that will be useful to users when making economic decisions about the financial position, financial performance, changes in the financial position and cash flows of the entity. The IASB (2013e) further states that capital providers use financial information to make decisions about the nature of their relationship with entities.

Watts and Zimmerman (1986) concur with this notion, stating that investors in entities use the financial data contained in a company's financial statements and other regulatory filings to determine their investment decisions. These authors continue by observing that while most bankruptcy prediction models use accounting data, accounting ratios are also used in lending agreements in order to restrict management's actions and provide lenders with a reasonable level of assurance of repayment. Moreover, credit-rating agencies use accounting data to measure the risks associated with entities. To support this use of accounting data, Watts and Zimmerman (1986) refer to evidence that includes the following:

(i) the majority of explanations given for changes in credit ratings are accounting-based reasons; (ii) the timing of the change in ratings is usually just after the annual reports have been made available; and (iii) the rating models typically use data from published accounting reports.

The above analysis confirms that information contained in the financial statements is used by investors to make investment decisions and can also be used by creditors and other stakeholders to forecast cash flows and predict bankruptcy. It has been determined that information contained in financial statements is used by users in making decisions about entities. The IOD (2009) posits that although it is important for companies to embrace sustainability and integrated reporting, the objective of King III is not to replace financial activities. Accordingly, this literature review seeks to explore the way in which the financial information contained in financial statements can be enhanced by integrating it with non-financial and sustainability disclosures.

The IASB (2013a) states that a complete set of financial statements shall consist of a statement of financial position; a statement of profit or loss and other comprehensive income; a statement of changes in equity; a statement of cash flows; and notes, which should include a summary of important accounting policies and other explanatory information.

The IASB (2013a) further provides a guide as to what information needs to be presented in the different components of the financial statements. Only those guidelines that are deemed to have an effect on this research paper are considered below.

Firstly, the *statement of financial position* presents information about an entity's asset, liability and equity balances as at the end of the financial period. This information is used to measure an entity's financial position at this time (IASB, 2013a). Secondly, the *statement of profit or loss and other comprehensive income* presents items of income earned during the period, expenses incurred and movements in other comprehensive income during the period. This information is used to measure the financial performance of the entity over that specific period (IASB, 2013a). Thirdly, the *statement of changes in equity*

presents a reconciliation between the opening and closing balances for the various components of equity (IASB, 2013a). Fourthly, the *statement of cash flows* provides information on the way in which the entity generates cash and how that cash is used; this statement is prepared and presented in terms of International Accounting Standard 7: Statement of Cash Flows, (IASB, 2013c). Finally, the *notes to the financial statements* present information about the basis of preparation of the financial statements and important accounting policies and provide information that has not been presented elsewhere in the financial statements but which is nevertheless relevant to users' decision-making process (IASB, 2013a).

The above review would seem to show that users of financial statements are expected to make their economic decisions based on financial information only. Accordingly, after discussing the objectives and components of financial statements, it now becomes necessary to consider the limitations that are inherent in conventional financial reporting, and how these can be improved by integrating the disclosures relating to financial and non-financial performance.

2.3. Limitations of the traditional set of financial statements

The limitations inherent in the financial reporting process, as described in section 2.2 above, are described below. This report also determines the impact of these limitations on the usefulness of the financial statements.

Reporting only on financial information

The IASB (2013e) acknowledges that financial statements do not provide all the information that users require when making economic decisions because they report mainly on the financial effects of past transactions and provide limited non-financial information. The IASB (2013a) further states that financial statements can also be used to assess management's stewardship and accountability towards the resources that have been delegated to them.

Verge (1985) and Bray (2011) note that if reporting in the financial statements is limited to financial information only, the information provided for decision-making purposes will be restricted and management's stewardship function in terms of environmental and human resources will be diminished. Steele (1991) supports this view by noting that stewardship not only encompasses accountability for the resources controlled by an entity, but also includes social and environmental responsibility.

Thus, reporting on financial information only does not provide users with the total effects of management's decisions; it does not provide users with a clear picture of the effects an entity's operations have on society and the environment. In addition, users are unable to assess how entity strategy has taken these effects into account.

Steele (1991) consequently notes that information on any social responsibility liabilities would be relevant to investors; therefore non-disclosure of such information would affect the completeness and reliability of the financial statements.

Reporting on historical information

The IASB (2013e) acknowledges that conventional financial reporting does not provide all the information users require when making economic decisions because, in the main, financial statements report only on the financial effects of past transactions. This can be substantiated by the requirement to identify a "past event" before transactions can be recognised in the financial statements (IASB, 2013e).

Steele (1991) notes that, because reporting is done on historical information, income becomes merely a measure of the performance of resources rather than also including the performance of management. Steele (1991) further notes that there is an inevitable delay between management's decisions and the impact they have on resources; hence, reporting on historical information does not give

users an opportunity to assess the future impact of the decisions management makes today.

According to Verge (1985), this historical perspective of financial statements results in limited information being provided to users for decision-making purposes, as historical information can only be used to a certain extent to direct the future. Verge (1985) recognises that including the results of management's decisions up to the reporting date only, and excluding any outstanding results of other current decisions, would only be useful in a relatively stable economy where the near future was not significantly different from the present.

According to Beaver (1991), although past and present information is the only basis for assessing future events, there is a need for a statement that clearly documents the treatment of future events.

Failure to provide adequate information about entities' risk

King III asserts that entities should disclose information on their risk management processes as this enables users to obtain a clear understanding of the risks faced by the entity and the processes (and the effectiveness thereof) put in place to mitigate these risks (IOD, 2009). The risk disclosure categories as identified from King III will now be discussed; the report will also consider whether these are covered in a set of financial statements prepared using the IASB (2013a) principles.

Going concern and financial risk

The IASB (2013e) describes "going concern" as the assumption that an entity would be able to continue operating for the foreseeable future; this concept assumes that an entity is liquid and solvent.

Liquidity risk can be assessed by inspecting the statement of cash flows and the statement of financial position and by comparing the cash and cash equivalents available at the end of the financial period with the value of the entity's current

liabilities. Similarly, solvency can be tested by inspecting the entity's net asset value (total assets less total liabilities) as reported in an entity's statement of financial position as at the end of its financial period.

It is thus evident that financial statements prepared in line with the principles provided by the IASB (2013a) can be used to assess the going-concern risk. The IASB (2013a) further requires that an entity disclose whether its financial statements have been prepared under the going-concern assumption or not.

Linsley and Shrives (2005) categorise financial risk as the risk related to, among other things, the effects of interest rate and exchange rate fluctuations. Accordingly, the King Code of Governance for South Africa 2009 (King III) requires that an entity disclose information that describes the credit and market risks the company is exposed to, as well as how these are managed.

The IASB's (2013d) International Financial Reporting Standard 7 Financial Instruments: Disclosures (IFRS 7) requires entities to disclose their exposure to any type of risk arising from any financial instruments that the entity holds. In addition, the IASB (2013d) requires that the objectives, policies and processes for managing the risks be disclosed, as well as the methods used to measure the risk.

It can therefore be assumed that a set of financial statements prepared in accordance with IASB (2013d) principles will disclose information about an entity's financial risk.

Operational risks

King III recommends that an entity disclose a description of its physical and operational risks and the measures undertaken to manage them in its integrated report (IOD, 2009).

Linsley and Shrives (2005) define operations risks as the risk relating to factors that affect the effective operation of an entity. These factors include

... customer satisfaction, product development, efficiency and performance, stock obsolescence and shrinkage, product and service failure, environmental, health and safety, and brand name erosion (Linsley & Shrives, 2005).

A review of the IASB (2013b) International Accounting Standard 2 Inventories (IAS 2) reveals that entities are required to measure their stock at the lower of the cost of the stock and its net realisable value; thus entities are required to write-down their stock to its net realisable value. IASB (2013b) further requires that an entity disclose the amount of the write-down recognised as an expense.

From the above analysis, it is evident that financial statements disclose information about stock obsolescence and shrinkage; however, this will be limited to financial information, as IAS 2 does not require the disclosure of how stock obsolescence and shrinkage is managed. Traditional financial statements, alone, do not provide information regarding factors such as the management of customer satisfaction or health and safety. It can therefore be concluded that financial statements, by themselves, do not provide users with sufficient information on the complete operations risks faced by an entity.

Empowerment risk

King III requires entities to disclose information about human resource risks and the risks relating to the entity's business continuity and disaster recovery plan (IOD, 2009).

In this regard, Linsley and Shrives (2005) identify empowerment risk as the risks relating to "leadership and management, outsourcing, performance incentives, change readiness, and communications".

As already alluded to above, the IASB (2013e) recognises that financial statements mainly contain financial information, and thus information about an entity's empowerment risks, human resource risks and business continuity and disaster recovery plans would not be disclosed in a set of financial statements.

Information processing and technology risk

King III recommends that entities disclose their technology risks. King III states that the board of directors of an entity should take responsibility for information technology (IT) governance, which should be aligned with the entity's performance and sustainability objectives (IOD, 2009). King III further requires that IT form part of the entity's risk management and for the board to be assisted by a risk and audit committee in managing and evaluating significant IT investments and expenditure (IOD, 2009). The disclosure requirements in terms of King III include how the entity's IT is aligned with its long-term business strategy; whether the board of directors is satisfied that IT will facilitate the achievement of the entity's long-term strategic business plan; and whether the entity's IT enhances the company's performance and sustainability (IOD, 2009).

Linsley and Shrives (2005) identify the risk attached the integrity, accessibility and availability of information, and further state that a lack of proper infrastructure could also pose a risk to an entity. Sumner (2000) maintains in this regard that one of the risk factors when implementing an information system is that the system might not fit an entity's operations or the entity might not have the correct hardware and other functionalities to support the successful implementation of the system.

The preparation and presentation of financial statements in accordance with the principles of the IASB (2013a) does not encompass such disclosure.

Ethics/integrity risk

King III identifies ethics risk as risk relating to factors such as theft, corruption and sabotage (IOD, 2009). According to Linsley and Shrives (2005), integrity risk includes risks relating to the entity's risk management policy, fraud initiated by either management or employees, involvement in illegal actions, and other reputational risk. As discussed above, the requirements of IASB (2013d) IFRS 7 provide for the disclosure of financial risk management only and do not make provision for the disclosure of an entity's non-financial risk management.

Strategic risk

King III advocates that a suitably qualified and experienced chief risk officer be appointed to monitor strategic risk matters and discuss these regularly with the board or relevant board committee (IOD, 2009). It is recommended that companies constantly monitor their operations for any changes in their strategic risk profile (IOD, 2009). Linsley and Shrives (2005) maintain that strategic risk includes risks relating to the industry in which an entity operates, its business portfolio, the entity's market standing and who its competitors are, the effects of pricing on the entity's operations, and performance measurement. The disclosure requirements for a set of financial statements, prepared in accordance with IASB (2013d) principles, do not include the disclosure of information relating to such risks.

The above analysis illustrates that although the objective of financial statements is to provide users with decision-useful information, the conventional set of financial statements fails to provide users with sufficient information about the risks that an entity is exposed to. Furthermore, insufficient information is provided on how such risks are being managed by the entity.

The next section discusses the way in which reporting on non-financial information and corporate governance measures can enhance the usefulness of the information presented in a traditional set of financial statements and, thus, enable users to assess an entity's performance and its risks.

2.4. Usefulness of reporting on non-financial and corporate governance information and the objective of integrated reporting

The purpose of this section is to identify the role played by the reporting of non-financial information and sustainability reporting in assessing an entity's performance and identifying the types of risk that an entity is exposed to.

In order to identify this role, the five elements to be included in a management commentary, as identified in the IFRS Foundation's (2010) Practice Statement, will be discussed. Each element will be evaluated to confirm the role it plays in assisting users to make decisions about the entity.

The nature of the business

The IFRS Foundation (2010) proposes that a management commentary should contain information that will assist users in obtaining an understanding of the entity and the environment in which it operates. It further explains that this information should include, among other things, the industry in which the entity operates, its main markets and its competitive position within those markets, and significant regulatory terms that affect the operations of the entity. According to the IFRS Foundation (2010), this information will help investors interpret and assess the financial statements of the entity in the context of the environment in which the entity operates. This is in line with the GRI (2011) requirement that, in reporting on their economic sustainability, companies should report on the impact of their operations on the economy of the countries in which they operate. All this information will help stakeholders to assess the risks that companies face as a result of the markets that they operate in.

Objectives and strategies

Secondly, the management commentary should contain information about the entity's objectives and strategies. This would include the time frames for achieving the objectives, how they relate to the creation or preservation of value

over the longer term, and how management plans to measure success in meeting these objectives (IFRS Foundation, 2010). Furthermore, effective communication regarding the objectives and strategies of an entity would enable the users of financial statements to understand what management's priorities are and how resources are being managed in order to achieve the desired outcomes. The IFRS Foundation (2010) confirms that disclosing information on an entity's objectives and strategies would assist investors in assessing the alignment of the strategies to the related objectives and the likelihood of those strategies being successful. This is in line with the King III recommendation that companies should clearly outline their strategies and vision in their integrated reports (IOD, 2009). King III further advocates for a clear explanation of how company strategy is linked to a company's performance and sustainability (IOD, 2009).

Key resources, risks and relationships

In addition to information about the nature of the business and an entity's objectives and strategies, the IFRS Foundation (2010) advises that information relating to the key resources, risks and relationships of the entity, their effects on the entity's pursuit of its objectives, and the way the resources, risks and relationships are managed should be clearly disclosed in the management commentary. This would provide users with useful information on any uncertainties facing the entity.

As already discussed above, both King III and Linsley and Shrives (2005) affirm that communicating on the various types of risk faced by an entity enables users to make a more informed assessment of the entity's performance.

Results and prospects

The fourth element to be included in a management commentary is "a clear description of the entity's financial and non-financial performance, the extent to which that performance may be indicative of future performance and management's assessment of the entity's prospects" (IFRS Foundation, 2010, para 34). According to the IFRS Foundation (2010), this information would include an assessment of the main trends and factors that affect the development

and performance of the entity and their relation to the entity's objectives and strategies.

Owen and Harte (1984) note that the information reported should include the most significant aspects of the social performance of an entity over the past year; the principal objectives of the entity; and a review of the organisation's prospects for the coming year. The IFRS Foundation (2010) concurs in this respect, stating that effective disclosure of this information would provide users with a clear understanding of the entity's performance. The IFRS Foundation (2010) further confirms that disclosing a clear description of the results and prospects would help users to make their own assessment of any assumptions and judgements used by management in measuring the elements of the financial statements.

Performance measures and indicators

Lastly, the IFRS Foundation (2010) states that a management commentary should disclose both the financial and the non-financial performance measures (normally referred to as key performance indicators in South Africa) that are used to assess progress towards achieving the set objectives and strategies. The IFRS Foundation (2010) posits in this regard that this information would also provide users with the evidence needed to assess how well resources, risks and relationships are managed and confirm that this information would help the users in assessing the success of the entity's goals and objectives. Gray and Perks (1982) note that including non-financial performance measures would enable users to assess the entity's performance in social terms, rather than just in terms of profitability.

The above discussion is supported by the GRI guidelines, which in addition to reporting on economic, environmental and social sustainability, also provide for entities to report on their strategy, organisational profile and governance (GRI, 2011).

2.5 King III recommendations and integrated reporting

The above review demonstrates that there are inherent limitations in reporting that uses only a set of financial statements and that the disclosure of non-financial information would enhance the usefulness of financial reports. Thus, companies have moved towards reporting on non-financial information. However, until the introduction of integrated reporting, companies had been presenting their financial statements (financial information) and sustainability reports (non-financial information) as separate reports. One of the objectives of integrated reporting is to communicate the link between the financial and non-financial information in one report; that is, for companies to disclose how they operate and what risks they are exposed to as a result of their operations (IOD, 2009). It is further recommended that companies communicate the way their risks and their risk management policies relate to their financial performance as well as their strategy.

In South Africa, the principles of integrated reporting are highlighted in King III. King III is divided into the following nine chapters, which will be briefly discussed below: 1. Ethical leadership and corporate citizenship, 2. Boards and directors, 3. Audit committee, 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, 9. Integrated reporting and disclosure.

The following section discusses each of these principles in turn and forms the basis for the research instrument discussed in section 3.4 of the next chapter.

Ethical leadership and corporate citizenship

King III states that “good corporate governance is essentially about effective responsible leadership” and highlights the fact that the board has a responsibility to ensure that the company “is and is seen as a responsible corporate citizen” (IOD, 2009). Responsibility, accountability, fairness and transparency are stated

as the key values of responsible leadership that is based on an ethical foundation (IOD, 2009). Brown and Trevino (2006) concur that ethical leaders are fair, honest and principled. Furthermore, Brown and Trevino (2006) state that ethical leadership is about displaying appropriate conduct and also encouraging such conduct among those being led by the board. This can be achieved through effective communication and role modelling. Sims and Brinkmann (2003) also highlight the importance of management's responsibility to model ethical behaviour for subordinates; and how if this is not done effectively it can have dire consequences. Enron is an example of how a breach of ethical boundaries by management led to the collapse and bankruptcy of a company that was once deemed to be highly successful (Sims & Brinkmann, 2003). To ensure that good moral values are instilled in managers very early on in their careers, Pies, Beckmann, and Heilscher (2009) advocate that higher learning institutions should incorporate business ethics in the skills that they train students in. By doing this, future managers would not only learn how to create value but also how to create value while being responsible corporate citizens (Pies et al., 2009).

On the other hand, Schwartz (2005) emphasises the importance of documenting acceptable moral values in a code of conduct; this in line with the recommendation by King III that ethical standards be articulated in a code of conduct (IOD, 2009).

The IFRS Foundation (2010) proposes that disclosure should be made on information that will assist users in obtaining an understanding of the entity and the environment in which it operates. In addition, this information should include, among other things, the industry in which the entity operates, its main markets and competitive position within those markets, and significant regulatory terms that affect the operations of the entity. According to the IFRS Foundation (2010), this information will help investors interpret and assess the financial statements of the entity within the context of the environment in which the entity operates.

In this chapter, chapter 1, King III further recommends that the company's strategies and vision should be clearly outlined in the integrated report (IOD, 2009). The IFRS Foundation (2010) supports the notion that management

commentary should contain information on the entity's objectives and strategies. This would include the time frames for achieving the objectives, how they relate to the creation or preservation of value over the longer term, and how management plans to measure the success of meeting these objectives (IFRS Foundation, 2010). Furthermore, effective communication on the objectives and strategies of an entity would enable the users of financial statements to understand what management's priorities are and how resources are being managed in order to achieve the desired outcomes. The IFRS Foundation (2010) confirms that disclosing information on an entity's objectives and strategies would assist investors in assessing the alignment of the strategies to the related objectives and the likelihood of those strategies being successful.

Boards and directors

In the second chapter, King III highlights the need for a board to be established in order to act as a custodian for corporate governance (IOD, 2009). The board is accordingly responsible for linking the company's strategy, risk, performance and sustainability by identifying key performance and risk areas and setting strategies that will assist in the company running a sustainable business (IOD, 2009). It is therefore recommended that a company appoint a board that comprises a mix of executive and non-executive directors (IOD, 2009). It is further recommended that the majority of the board members should be non-executive, of whom the majority in turn should be independent, and that the board should meet at least four times a year (IOD, 2009). In this regard, Adams, Hermalin, and Weisbach (2008) posit that pressure from various stakeholders has resulted in companies needing to have a majority of non-executive directors.

Another recommendation contained in the second chapter is that the board should elect independent non-executive directors as the chairman and the chief executive officer (CEO) – the two should be different people (IOD, 2009). King III continues by recommending that, should the chairman of an entity not be an

independent director, justification to be included in the integrated report (IOD, 2009).

Furthermore, King III recommends that the board should establish a remuneration committee (which should comprise a majority of independent non-executive directors), disclose the remuneration of each individual director and certain senior executives, and include a remuneration report in the integrated report (IOD, 2009). This recommendation to disclose executives' remuneration is in line with the U.S. Securities and Exchange Commission's requirements for companies to explain executives' remuneration and to disclose the total remuneration per executive (Friday & Crum, 2008).

Another of the Code's recommendations is that the board should ensure that the solvency and liquidity of the company is continually monitored; this is because the board becomes liable should anything go wrong in the company (IOD, 2009). Adams et al. (2008) recall how the directors of Enron and Worldcom were held responsible and had to personally settle fines for fraud that had taken place in their respective companies.

Audit committee

King III recommends that an independent audit committee be established, consisting of at least three skilled and experienced non-executive directors, the chairman of which should be an independent non-executive director (IOD, 2009). Rupley, Almer, and Philbrick (2011) indicate that the financial experience and independence of audit committee members are factors that affect the committee's effectiveness. Audit committees that are independent and knowledgeable have been found to be more effective in overseeing the financial reporting function and more also effective in overseeing both the external and internal audit functions (Rupley et al., 2011).

It is recommended that the audit committee meet at least twice a year, that it meet with the internal and external auditors at least once a year without management being present, and that the chairman of the audit committee should not be the chairman of the board (IOD, 2009). Barua, Rama, and Sharma (2010)

report that frequent meetings by the audit committee allows the committee to be more effective and also results in better communication between the audit committee and both external and internal auditors. Abbott and Parker (2000) agree that audit committees that meet at least twice a year are more effective in carrying out their duties. King III further recommends that the composition and terms of reference of the audit committee be disclosed in the integrated report (IOD, 2009). This chapter of King III has been aligned with the requirements of section 94 of the new Companies Act, which relates to audit committees (Companies Act, 2008).

Zhang, Zhou, and Zhou (2007) posit that the financial expertise and independence of an audit committee allows for the effective monitoring of internal controls. This is in line with the King III recommendation that the audit committee should evaluate the independence, credentials and performance of the external auditor. Furthermore, the audit committee should oversee the internal audit function and assess the performance, expertise and skills of the financial function (IOD, 2009). Abbott and Parker (2000) posit that independent and active audit committees tend to demand good quality from external auditors.

The governance of risk

The principle discussed in the fourth chapter of King III relates to the responsibility of the board in terms of the governance of risk (IOD, 2009). King III recommends that the board set risk tolerance levels and comment, in the integrated report, on the effectiveness of the system and the process of risk management (IOD, 2009). It is further recommended that a risk committee be appointed with a minimum of three members and that it convene at least twice a year (IOD, 2009).

King III specifically suggests that the risk management disclosure should include information on the process of identifying, evaluating or managing significant risks; the internal controls put in place to mitigate significant risks to acceptable levels; and whether the internal control system is a detective or preventative one (IOD, 2009). Such risk assessment process disclosure should cover physical and operational risks, technology risks, human resource risks, business continuity

and disaster recovery, credit and market risks, compliance risks and sustainability risks (IOD, 2009).

Halachmi (2003) advocates that in a spirit of accountability and transparency companies should provide information about their risk management procedures. Drennan (2004) deduces that effective risk management is vital for the survival of any entity as the early identification of any control weaknesses will prevent entities incurring losses. Meanwhile, Drew, Kelley, and Kendrick (2006) concur that the benefits of effective risk management are not limited to compliance with regulations; effective risk management provides the board with an understanding of the varying nature of the risks faced by entities and the effective development of strategies for managing these risks.

The IFRS Foundation (2010) supports this recommendation and proposes that financial statements should be accompanied by a management commentary that contains information relating to an entity's key resources, as well as the risks and relationships and their effects on the entity's pursuit of its objectives. The IFRS Foundation (2010) further states that such a management commentary should disclose a clear description of how these resources, risks and relationships are managed by the entity. This would provide useful information to the users relating to any uncertainties facing the entity.

Linsley and Shrives (2005) suggest that communicating forward-looking information pertaining to the various types of risk faced by an entity enables users to make a more informed assessment of the entity's performance.

The governance of information technology (IT)

In line with the recommendation in chapter 5 of King III, De Haes and Van Grembergen (2006) note that IT governance entails the board taking responsibility for fusing business and IT. King III proposes that the board take responsibility for IT governance and subsequently ensure that IT is aligned with the company's performance and sustainability objectives – thus viewing IT as a pervasive part of business rather than a business enabler (IOD, 2009). Peterson,

O'Callaghan, and Ribbers (2000) agree that IT has moved from being merely an “administrative tool” to forming an integral part of the business.

Nolan and McFarlan (2005) warn that lack of board oversight on IT poses significant risks to the wellbeing of a company. In line with this view, King III further advocates for IT to form part of the company's risk management and for the board to be assisted by the risk and audit committee in managing and evaluating significant IT investments and expenditure. Nolan and McFarlan (2005, p. 5) concur that boards are responsible for providing assurance on “the completeness, quality, security, reliability and maintenance of existing IT investments that support day-to-day business processes”.

King III recommends that the integrated report disclose information regarding the alignment of IT and the company's long-term business strategy, stating whether the board is satisfied that IT will facilitate the achievement of the company's long-term strategic business plan and whether the company's IT enhances the company's performance and sustainability (IOD, 2009). Nolan and McFarlan (2005) posit that a company's IT strategy needs to be aligned with the company's objectives.

Compliance with laws, rules, codes and standards

Chapter 6 of King III maintains that the board of directors has the responsibility of ensuring the company's compliance with applicable laws. The Code accordingly recommends the consideration of adherence to non-binding rules, codes and standards. The IFRS Foundation's (2010) management commentary is an example of a non-binding statement that could be considered by companies looking to enhance their integrated reporting because it provides guidelines for the preparation of a management commentary. However, it does not specify which companies are required to apply these principles nor does it specify the frequency with which a management commentary should be issued.

Internal audit

In the seventh chapter of the report, King III addresses the establishment of a dedicated and objective internal audit function by companies (IOD, 2009). King III recommends that the audit committee take responsibility for reviewing the company's control systems, overseeing the internal audit function and approving internal audit's plans (IOD, 2009). Goodwin-Stewart and Kent (2006) assert that the formation of an internal audit function by a company reflects positively on the company's commitment to risk management.

King III proposes the appointment of a chief audit executive and that internal audit plans should follow a risk-based approach; that is, internal audit plans should be informed by the company's strategy (IOD, 2009). According to King III, the chief audit executive's responsibilities include reporting to the audit committee on issues regarding the adequacy of the skills and resources available to implement the internal audit function's risk-based plan (IOD, 2009). The Code further recommends that internal audit, and not the audit committee, should provide written assessments of the effectiveness of the system of internal controls and risk management to the board (IOD, 2009). Arena and Azzone (2009) assert that internal audit departments are more effective when led by a suitably qualified chief audit executive and when the audit committee participates in the internal audit activities. Abbott, Parker, and Peters (2010) maintain that when the audit committee has oversight over the internal audit function, this steers internal audit towards a risk-based approach in their plan.

Sarens, De Beelde, and Everaert (2009) found that the audit committee places reliance on the risk assessments performed by the internal audit function, as well as the work internal audit performs on the evaluation of the control environment. This is due to the fact that internal audit's knowledge and experience of risk management and the control environment provide the internal audit function with the competence to make such assurances (Sarens et al, 2009).

Governing stakeholder relationships

King III notes the importance of acknowledging the effects of stakeholders' perceptions on a company's reputation (IOD, 2009). Vinten (2001) defines stakeholder theory simply as "the theory that a firm should be run in the interests of all its stakeholders rather than just its shareholders" (p. 37). Damak-Ayadi and Pesqueux (2005) recall that the term "stakeholder" came about as a result of resistance to the idea of companies focusing only on financial value and thus only being concerned about shareholders' needs. Freeman, Wicks, and Parmar (2004) maintain that looking after all stakeholders' concerns will automatically result in shareholders' interests being addressed; thus shareholders do not have to be anxious that applying stakeholder theory would minimise management's focus on their interests as primary stakeholders.

The Code, thus, requires the board to delegate management in order to deal proactively with stakeholder relationships while striving to achieve an appropriate balance between the various stakeholder groupings and ensure equitable treatment of stakeholders (IOD, 2009). It is further noted that transparent and effective communication with stakeholders increases stakeholders' trust and confidence in the company (IOD, 2009). Hutton (2004, p. 16) concurs that "confident well informed investors are necessary for achieving and maintaining accurate valuation of a company's stock". Hutton (2004) further states that the objective of integrated reporting is to provide supplementary disclosure, in addition to financial statements, that will assist in eradicating the gaps between investors' expectations and management's plans. Foster and Jonker (2005) concur that effective communication with stakeholders is vital in managing stakeholder relationships.

Integrated reporting and disclosure

In the last chapter of the report, King III recommends that an integrated report be prepared annually and that it should convey adequate information regarding the company's financial and sustainability performances (IOD, 2009). Integrated reporting is defined as "a holistic and integrated representation of the company's performance in terms of both its finance and its sustainability" (IOD, 2009, p. 54).

The Code further recommends that the board should include commentary on the company's financial results, disclose whether the company is a going concern, describe how the company made its money, and communicate both the positive and the negative effects of the company's operations (on society, the environment, human rights, manufactured capital and technology) and plans to improve the positive effects and eradicate the negative (IOD, 2009). Derwent (1989) supports the disclosure of both the positive and negative effects of an entity's operations on the environment by asserting that entities generally prefer to report only on the positive impacts of their operations and this results in some entities erroneously elevating themselves. Linsley and Shrives (2005) affirm that obliging entities to openly disclose the negative impacts of their operations will result in most entities genuinely working towards improving their records. In an interview with Kiron (2012) published in the *MIT Sloan Management Review*, Robert Eccles also notes that integrated reporting is about disclosing both the positive and the negative outputs of a company's operations.

As discussed earlier, this view is supported by the IFRS Foundation (2010) which states that a management commentary should contain information that will assist users in obtaining an understanding of the entity and the environment in which it operates; and further explains that this information would include, among other factors, the industry in which the entity operates, significant regulatory terms that affect the operations of the entity, its main markets and its competitive position within those markets. The IFRS Foundation (2010) further states that effective disclosure of information relating to an entity's results and prospects will provide users with a clear understanding of the entity's performance and further confirms that disclosing a clear description of the results and prospects would help users make their own assessment of any assumptions and judgements used by management in measuring the elements of the financial statements. Owen and Harte (1984) are in full support of this view, noting that an entity's annual report should provide users with information on the most significant aspects of the social performance of the entity over the past year, the principal objectives of the entity and a review of the entity's prospects for the coming year. The International Corporate Governance Network (ICGN, 2008) asserts that including non-financial

performance measures would enable users to assess the entity's performance holistically, rather than just in terms of profitability.

In his study titled "Trends in sustainability reporting by the Fortune Global 250", Kolk (2003) examined the environmental, social, sustainability and annual reports of these companies as well as their websites and found that there had been an increase in the level of disclosure of non-financial information. Makiwane and Padia (2013) also found that there had been an increase in the level of reporting; however, they nevertheless found that much improvement was still needed in order to achieve the objective of integrated reporting. PwC (2012) conducted an assessment of the application of King III by the top 100 JSE listed companies in their integrated reports; the assessment found that, amongst other factors, most companies provided adequate disclosures in accordance with King II requirements; however, newer areas of governance introduced in King III (such as IT governance) had not been addressed adequately.

The International Integrated Reporting Committee noted that companies were increasingly producing sustainability reports; however, there were concerns about the relevance and quality of these reports (IRC, 2011). In January 2011, the Integrated Reporting Committee of South Africa issued a discussion paper which aims at formulating a standard for measuring integrated reporting disclosures (IRC, 2011).

The IFRS Foundation (2010) states that a management commentary should include the disclosure of both the financial and non-financial performance measures (normally referred to as key performance indicators in South Africa) that are used to assess progress in achieving the set objectives and strategies. The IFRS Foundation (2010) posits that this information would also provide users with the evidence needed to assess how well resources, risks and relationships are managed, and confirms that this information would help the users in assessing the success of the entity's goals and objectives. Gray and Perks (1982) note that including non-financial performance measures would enable users to assess the entity's performance in social terms, rather than just in terms of profitability.

With the mounting interest in integrated reporting; it is expected that the recommendations of King III will have an effect on the way companies disclose information on corporate governance and issues of sustainability.

The extent of the disclosure in companies' integrated reports is expected to have improved, as PwC (2012) asserts that South Africa is seen as the leader in integrated reporting. In 2013, the IIRC issued a consultation draft framework that gives guidelines on the process of integrated reporting and the elements that should be present in an integrated report (IIRC, 2013). Following the consultation process, in December 2013 the IIRC released a framework for integrated reporting. Although the content recommended by the IIRC's 2013 framework for inclusion in an integrated report is closely linked to the recommendations of King III, these have not been specifically included in the research instrument used in this study, as the cut-off for this research is reports issued for the year ended 2012.

It is interesting to note opposing views with regard to integrated reporting. Kolk (2003, p. 289) for instance cautions that sustainability reporting could be regarded as "mere window-dressing". This view is echoed by Steyn and De Beer (2011), who maintain that integrated reporting can be used for public relations purposes, while Owen, Swift, Humphrey, and Bowerman (2000) caution that the integration of social, environmental and financial issues tends to result in the weakening of sustainability reporting. These views will be interrogated further in the analysis of the results in chapter 4 of this report.

The above disclosure is supported by the GRI guidelines; in addition to reporting on economic, environmental and social sustainability, these guidelines provide for entities to also report on their strategy, organisational profile and governance.

2.5. Conclusion

As demonstrated in this chapter, there are limitations in traditional financial reporting, as financial statements report mainly on financial information and historical information and do not provide users with an understanding of the entity's risk and the impact of its operations on the environment and society. Reporting on non-financial information has thus become important as this provides users with information on the nature of an entity's business, the entity's objectives and strategies, its key risks, its non-financial performance and its key performance indicators. A study conducted by Palenberg, Reinicke, and Witte (2006), which evaluated the trends in non-financial reporting, confirmed that there has been an increase in non-financial reporting by entities. Furthermore, EY (2012) posits that although the integrated reports prepared during 2012 were not prepared according to a framework, these still resulted in companies presenting a link between their financial and non-financial performance. Finally, the literature shows that integrated reporting promotes the integration of an entity's financial and non-financial reports into one report. The single report should communicate how the entity's strategy links to its risks, prospects and performance, taking into account financial, social and environmental factors. This report should also disclose both the positive and negative effects of the entity's operations on the environment and society.

This study seeks to evaluate the extent of integrated reporting by companies listed on the JSE since the introduction of King III as part of the JSE listing requirements. It concentrates on an evaluation of companies' disclosures relating to the various principles contained in the different chapters of King III; in addition, it seeks to assess the trends in integrated reporting by examining whether companies have been able to harmonise the disclosures relating to their financial and non-financial information.

CHAPTER 3: RESEARCH METHODOLOGY

3.1 Research methodology /paradigm

A mixed research methodology was used to assess the extent of integrated reporting, as this is a descriptive study. Leedy and Ormrod (2010) confirm that descriptive research simply seeks to explore an existing situation as opposed to altering the status quo. A descriptive research approach is, therefore, appropriate for this study as the study only sought to investigate the trends in the extent of integrated reporting by companies listed on the JSE. Accordingly, the study involved a content analysis of the reports. Leedy and Ormrod (2010) state that a content analysis involves the analysis of the contents of specific reports in order to identify key ideas. This method is appropriate for this study as it included the inspection of the annual integrated reports for key trends relating to the various disclosures. A sample of annual integrated reports of fifty-two JSE-listed companies was examined for specific disclosures relating to the principles listed in section 3.2 below. The results discussed in the next chapter (chapter 4) include a discussion of the trends noted in the various annual integrated reports.

3.2 Research design

The study was conducted by means of an analysis of the annual integrated reports of companies listed on the JSE. These reports were analysed for disclosure pertaining to the following principles which emerged from chapters 1 to 9 of King III: A. Ethical leadership and corporate citizenship, B. Boards and directors, C. Audit committee responsibilities, D. Risk management, E. Remuneration committee responsibilities, F. Nomination committee responsibilities, G. Internal audit function, H. Information technology governance, I. Compliance management, J. Governing of stakeholder relationships, K. Integrated reporting. The reports were also inspected for the following GRI sustainability indicators: L. Economic sustainability, M. Social sustainability and N. Environmental sustainability.

The published annual (integrated) reports for the 2010, 2011 and 2012 financial years were inspected with the aim of identifying any significant changes that had occurred in the way companies disclosed on the above information and whether the different factors had been harmonised in any way.

It is important to note that although King III was issued in response to the inclusion of governance issues in the new Companies Act, the Code itself is not legislation (IOD, 2009). That is, the King Code works on an apply-or-explain basis. As such, companies' annual integrated reports were examined not only for the application of the King III principles but also for an explanation for non-application.

One advantage of using published annual (integrated) reports is that these normally contain the audited financial statements and auditors are required to read through the information contained in these reports in order to identify inconsistencies with the audited financial statements (IAASB, 2013). The information contained in these reports is therefore regarded as valid and reliable.

3.3 Population and sample

3.3.1 Population

The population for this study is companies listed under the various sectors, on the JSE.

3.3.2 Sample and sampling method

As the JSE listing requirements necessitate the application of King III by all listed companies, only JSE-listed companies were considered for the purpose of this study. Accordingly, fifty-two companies were used for the sample for this study. This sample cut across the different sectors and industries on the JSE and included companies listed in the following sectors: automobiles and parts, food and beverage, media, retail, travel and leisure, real estate, health care, construction and materials, industrial goods and services, oil and gas,

technology, telecommunications and the basic materials and financials. The sample represents an average of four companies per sector from a range of sectors that holds a sizable percentage of the market share of the JSE, and is therefore regarded as a representative sample of companies listed on the JSE.

3.4 The research instrument

The research instrument was in the form of a scorecard approach, where the recommendations of King III and three GRI indicators were recorded and scored against the disclosure contained in the various company reports. It is acknowledged that using a scorecard may not be entirely in the spirit of integrated reporting as it promotes a “tick-box” mentality; however, it was used to help attain consistency in the testing as all companies were rated on the basis of the same indicators.

The King III indicators in the research instrument include information on elements such as risk management, internal audit, IT governance, managing stakeholder perceptions, compliance management and integrating financial and non-financial information.

The information disclosed under each indicator was analysed for the level of disclosure over a period of three years. The rating scale used was adapted from Makiwane and Padia (2013); this rating scale is similar to the one used by Duab (2007) in assessing the quality of sustainability reporting by Swiss companies.

1	The report provides no information (nor an explanation of the non-disclosure) on the indicator
2	The report provides little detail on the indicator
3	The report provides satisfactory details on the indicator

4	The report provides more details on the indicator
5	The report provides a large amount of detail on the indicator

The indicators in the research instrument were derived from the different chapters of King III. Three GRI sustainability reporting indicators were also included on the research instrument (see Appendix A for the research instrument). The indicators listed under each heading were scored using the above rating scale.

It should be noted that the mark for non-compliance (1) was given in two instances: (i) where companies did not have any information on an indicator and (ii) where companies disclosed practice that was contrary to the recommendations of King III without providing an explanation for doing so.

3.5 Procedure for data collection

The companies' annual (integrated) reports for the years ended 2010, 2011 and 2012 were downloaded from the McGregor BFA, an electronic database of financial data. These reports were then inspected and examined by the researcher to evaluate the extent of disclosure for each of the research indicators listed in Appendix A, using the rating scale discussed above.

It should be noted that while the evaluation of the extent of reporting may involve a small level of subjectivity, the researcher's consistency was relied upon for dependable results.

3.6 Data analysis and interpretation

The rating scale discussed in section 3.4 above was used to rate the level of disclosure by each company. These results were then analysed to determine the overall trend in the level of disclosure and the integrated reporting as follows:

- by all the companies in the sample
- by all companies for each subsection of the research indicators
- per sector/industry
- per sector/industry for each subsection of the research indicators
- indicators displaying the most significant trends

In addition to descriptive statistics using frequencies and multiple bar graphs, a non-parametric test was used to test any significant differences in the extent of disclosure from 2010 to 2012. According to Hanke and Reitsch (1994), non-parametric tests do not assume anything about the population data and are useful when qualitative data needs to be converted into useful information that can be used for decision-making purposes.

The paired sample *t*-test is the standard test one would be expected to use for this analysis as scores were derived for each company per measure per year. The scores were then averaged to obtain aggregate scores and sub-scores. The final test was a comparison of the 2010 and 2011 scores, and then the 2011 and 2012 scores.

The *t*-test was not used, however, as it assumes that the scores are normally distributed, an assumption that may not be correct as the data may be skewed and the scores were bound between 1 and 5, while the normal distribution is unbound with values between negative infinity and positive infinity. Hence, the Wilcoxon signed-rank test; a test that does not require the normal distribution assumption was used.

Scores were allocated for the disclosure and extent of integrated reporting, while the Wilcoxon signed-rank test was used to test for any significance in the changes in the disclosure and extent of integrated reporting. This test can be used where there are repeated observations of the same issue and does not assume that the data is normally distributed. McDonald (2009) confirms that the Wilcoxon signed-rank test can be used “when there are two nominal variables and one measurement variable. One of the nominal variables has only two values such as ‘before’ and ‘after’ and the other nominal variable often

represents individuals". Thus, in the case of this research the extent of disclosure in the preceding years (2010 and 2011) and in the current year (2012) was examined for each of the fifty-two companies against the various King III and GRI recommendations.

In using the Wilcoxon signed-rank test the following hypotheses have to be considered:

- A null hypothesis that assumes that the extent of disclosure is the same in 2011 as it is in 2010, and the same in 2012 as it is in 2011.
- The alternative hypothesis is that the extent of disclosure in 2010 is not the same as in 2011, and disclosure in 2011 is not the same as in 2012.

Demšar (2006) posits that where the results of the test show a p -value of less than 0.05, the null hypothesis can be rejected. This means that there exists a significant difference at a greater than 95% probability level. Alternatively, where the p -value is more than 0.05, the results fail to reject the null hypothesis.

For the purposes of this study, the movement in the average scores per year will show whether there has been a change in the level of disclosure; and the p -values derived from the Wilcoxon signed-rank test will explain whether these changes have been significant or not.

3.7 Limitations of the study

Bray (2011) maintains that company websites can be used to keep useful data. Since the annual (integrated) reports were retrieved from McGregor BFA, there is the risk that some companies may have included certain information on their websites without making reference to this in the actual annual (integrated) reports. In such circumstances the company would be awarded a 1 (no information provided) for such an indicator; that is, information contained on company websites was only considered for those companies that explicitly referred to their websites in their integrated reports.

CHAPTER 4: RESEARCH RESULTS

This chapter will first discuss a number of key findings noted from the examination of the various companies' annual integrated reports. The chapter will then proceed to present the trends in the level of reporting under the different subsections of the research indicators, highlighting the best versus the worst performing sectors. The chapter will end with an overview of the overall trends.

4.1 Key findings

Although King III advocates for companies to issue a single report that harmonises their financial and non-financial performance, there were a number of companies that still issued separate reports: all sampled companies issued a single report for 2010, one issued multiple reports in 2011 and six companies issued multiple reports in 2012. The main report issued by these companies was still called an "integrated report" while the other report was found to contain either the corporate governance or sustainability disclosures.

Both King III and the IIRC framework state that an integrated report is a "concise communication" of the link between a company's financial and non-financial performance. Atkins and Maroun (2014) found that institutional investors desired shorter integrated reports, which were less complex and avoided repetition and confusion.

The average number of pages contained in the sampled companies' reports increased from 136 in 2010 to 140 in 2011 and 151 in 2012. Although this average increase in volume was only four pages between 2010 and 2011 and 11 pages between 2011 and 2012, it will be interesting to see whether the reports get significantly larger in future periods.

The inspection of the annual integrated reports also revealed that companies with a bigger market capitalisation had better disclosures than smaller companies.

It is evident that the application of King III has enhanced management's ability to carry out their stewardship function more efficiently. As Jensen and Meckling (1976) explain, inherent in the agent–principal relationship is the risk that the

agent may not always act in the best interests of the principal. King III encourages companies to be good corporate citizens and to also disclose the effects of their operations on society, the environment and the economy (IOD, 2009). The inspection of the sampled integrated/annual reports did show evidence of companies explaining how they would eradicate the negative effects of their operations, and the way in which this and improving the positive effects of their operations would contribute to the sustainability and the value-creation of the companies. In line with Fontrodona and Sison (2006)'s observation, putting governance systems in place has contributed to the alignment of agents' and principals' interests and has encouraged the agents (board of directors) to act in the best interests of the principals.

Table 4.1 and Figure 4.1 illustrates that the application of King III does not necessarily imply that companies will give the reports they issue the name "integrated report"; there were still companies that termed their reports "annual reports" even under King III. For example, in 2011, although forty-nine companies reported that their reports had been prepared in line with King III only thirty-six companies called their reports integrated reports. Similarly, in 2012, forty-nine companies reported that their reports had been prepared in line with King III but only forty-five companies called this report an integrated reported.

Table 4.1: Number of reports that clearly indicate whether King II/III guidelines have been followed			
	2010	2011	2012
Number of companies who declared reporting under King III	22	49	49
Number of companies who declared reporting under King II	26	1	0
Number of companies who did not make a declaration of applying either King Code	3	1	3
Number of companies who declared the non-application of the King Code due to their small size	1	1	0
Total	52	52	52

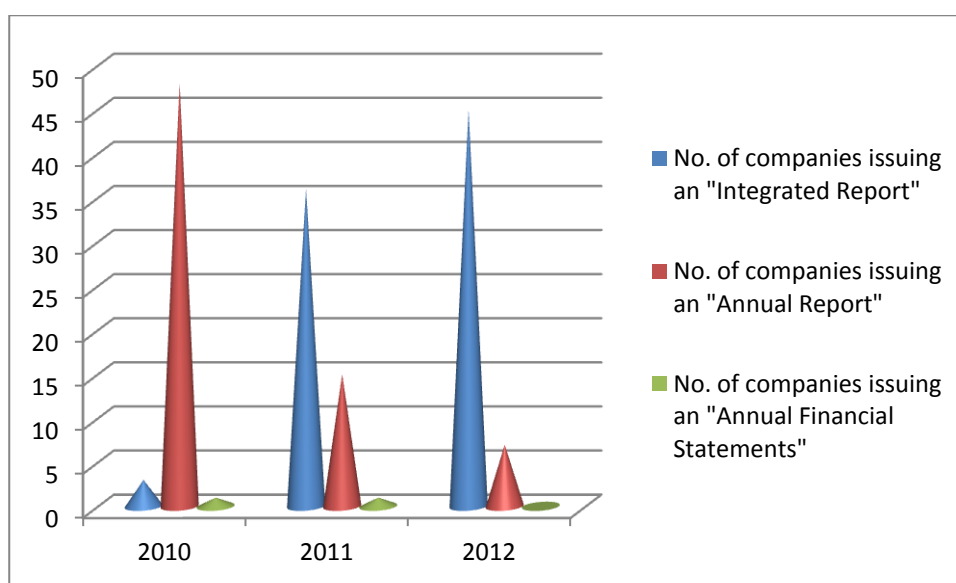


Figure 4.1: Number of companies issuing an integrated report vs an annual report

Table 4.2: Average scores per indicator over the three-year period

Indicator	2010	2011	2012
Ethical leadership and corporate citizenship	3.09	3.32	3.44
Boards and directors	3.82	4.05	4.12
Audit committees	3.88	4.12	4.24
Risk management committees	3.64	3.88	3.96
Remuneration committees	3.86	3.92	4.10
Nomination committees	3.27	3.39	3.52
Internal audit function	2.74	2.94	3.08
The governance of IT	1.38	1.72	1.87
Compliance with laws, rules, codes and standards	2.13	2.34	2.51
Governing stakeholder relationships	2.13	2.65	2.76
Integrated reporting	2.65	3.02	3.08
Economic, social and environmental sustainability	2.93	3.15	3.22

The scores recorded in Table 4.2 and Figure 4.2 indicate that the annual/integrated reports of the sampled companies provided very little or no information or detail with regard to information relating to the governance of IT. That is, the average score for the level of disclosure relating to IT governance increased over the three-year period but was still below two. Other areas on which the annual/integrated reports did not provide satisfactory details by 2012 included disclosures on compliance with laws, rules, codes and standards – with the average score only going up to 2.51 by the end of 2012– and disclosures relating to the governance of stakeholder relations – with the average score reaching 2.76 by the end of 2012.

The Wilcoxon p -values derived from analysing the annual/integrated reports of the sampled companies for each of the indicators are summarised in Table 4.3. In line with Demšar's (2006) position, where the results of the test show a p -value of less than 0.05, the null hypothesis (being that the extent of disclosure is the same in 2011 as it is in 2010, and the same in 2012 as it is in 2011) can be rejected. This means that there exists significant difference at a greater than 95% probability level. Thus, where the p -value is more than 0.05, the results fail to reject the null hypothesis.

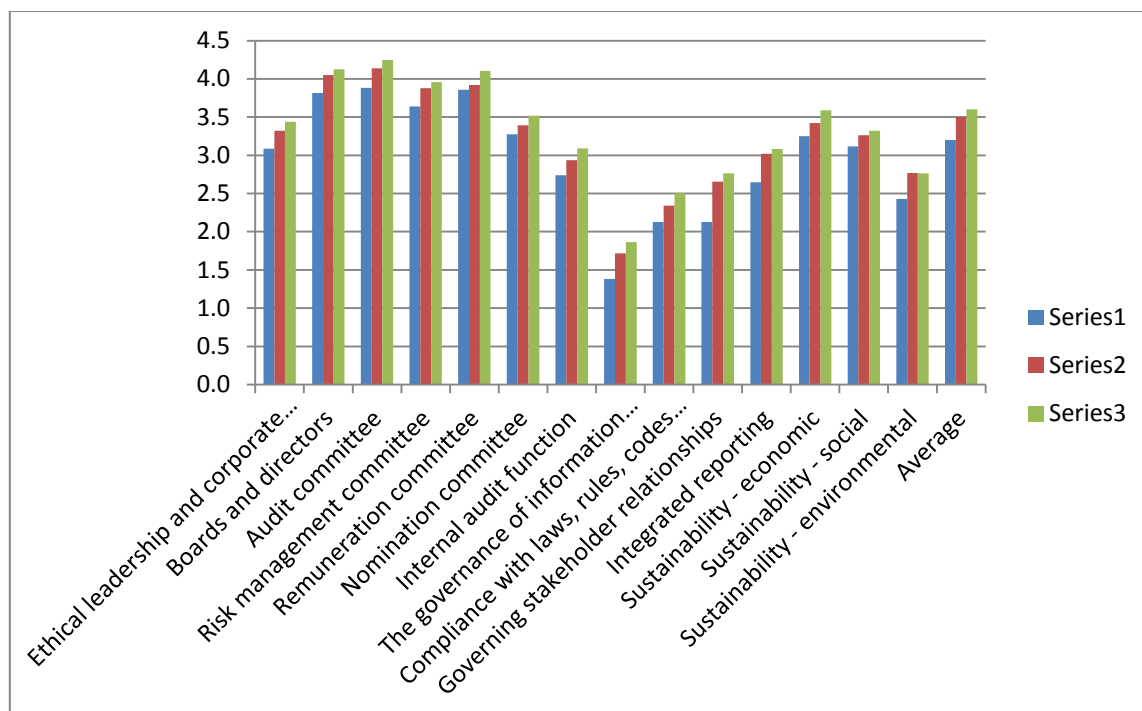


Figure 4.2: Average scores per indicator (presented in graph format)

Table 4.3 Wilcoxon *p*-values per indicator, showing the level of change in disclosure over the three-year period

Indicator	2010–2011	2011–2012
Ethical leadership and corporate citizenship	0.2481	0.4059
Boards and directors	0.0592	0.3241
Audit committees	0.0064	0.2870
Risk management committees	0.1086	0.4461
Remuneration committees	0.6617	0.2488
Nomination committees	0.6182	0.5080
Internal audit function	0.2657	0.4482
The governance of IT	0.0006	0.4082
Compliance with laws, rules, codes and standards	0.1873	0.2869
Governing stakeholder relationships	0.0030	0.4341
Integrated reporting	0.0224	0.6747

Economic sustainability,	0.6747	0.5004
Social sustainability	0.5910	0.7932
Environmental sustainability	0.1603	0.9660

The above *p*-values show that a significant change in the level of disclosures was only observed between 2010 and 2011 for disclosures relating to audit committees, the governance of IT, the governance of stakeholder relationships and integrated reporting. While the significant improvement in disclosures relating to audit committees between 2010 and 2011 can be attributed to the inclusion of this subject in the Companies Act of 2008, the significant improvement in disclosures relating to the governance of IT, stakeholder relationships and integrated reporting can be attributed to the fact that these are some of the updated requirements of King III; that is, the disclosure requirements pertaining to these indicators were not included in King II.

4.2 Ethical leadership and corporate citizenship

There was little improvement in the disclosure relating to ethical leadership and corporate citizenship. The disclosure under this subsection remained satisfactory with companies' reports displaying an attempt to link their strategies and values to their economic, social and environmental performance. In line with the King III recommendations and the IFRS Foundation (2010), companies disclosed information about the strategies and objectives and also included disclosure on how these related to the companies' creation and preservation of value. Only nine (17%) of the fifty-two sampled companies did not provide such information over the three-year period.

An increased number of companies are also moving towards documenting their commitment to ethical values in formalised codes of conduct. This trend supports

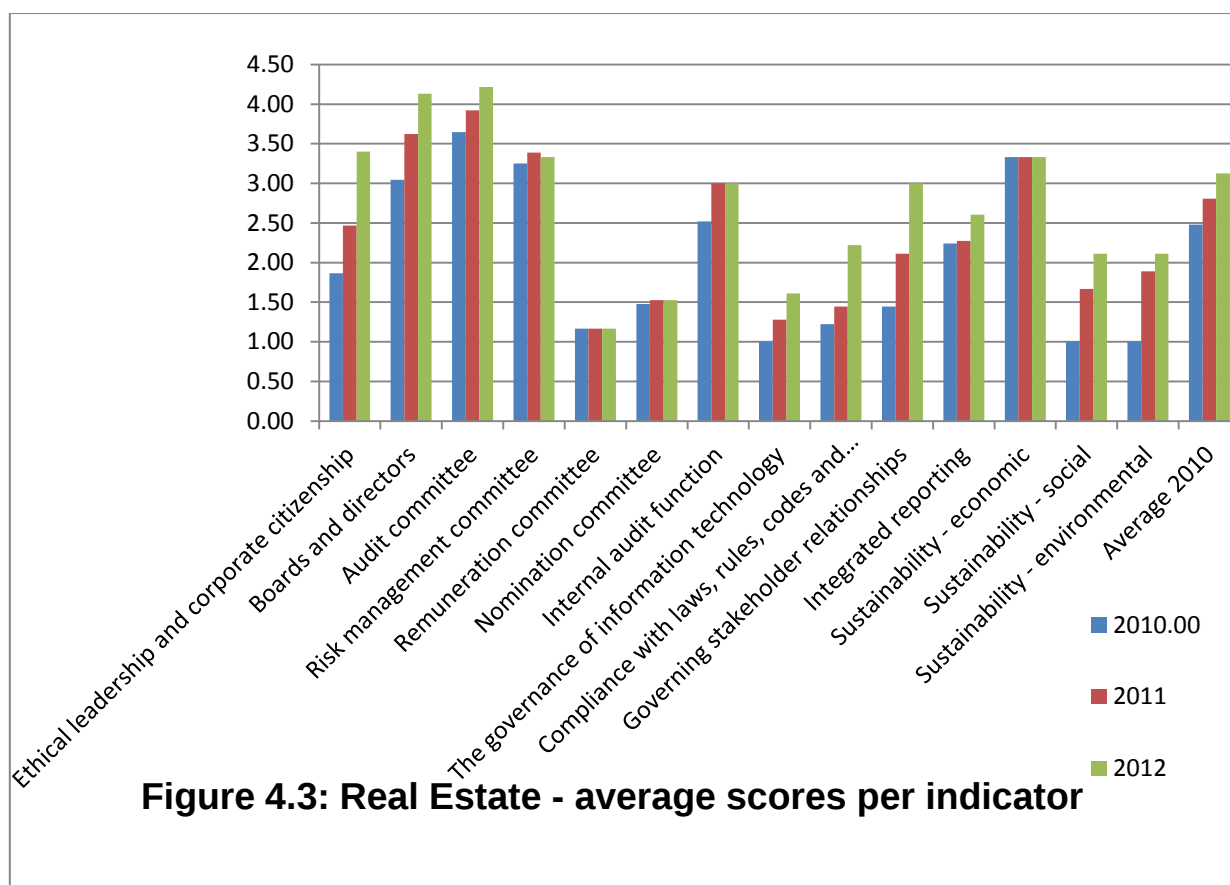
Schwartz's (2005) position, in line with King III, that it is important for the acceptable moral values of a company to be documented in a code of conduct.

Although King III advocates for the assurance of such information in order to improve its reliability, forty-eight of the sampled companies did not obtain such independent assurance on their ethics disclosures nor disclose information relating to obtaining such assurance – only 8% of the companies obtained such assurance.

The average scores depicted in Table 4.2 confirm that there has been satisfactory disclosure by companies in terms of this subsection over the three-year period.

The Wilcoxon p -values in Table 4.3 show that there were no significant changes in the way companies disclosed their information in relation to ethical leadership and corporate citizenship over the three-year period. This is in line with the average scores reported in Table 4.2, which show that reporting on this subsection has remained satisfactory over the three years.

Of all the sectors reviewed, the real estate sector showed the most improvement with regard to the level of disclosure on this subsection. The average scores moved from close to non-compliance in 2010 (with an average score of 1.87), to little detail provided during 2011 (with an average score of 2.5) and satisfactory detail provided during 2012 (with an average score of 3.4).



4.3 Boards and directors

There has been some improvement in this category of indicators. Companies heeded the call for more independent non-executive directors to sit on boards. Although boards made an effort to appoint more independent non-executive directors, not as many companies appointed independent non-executive chairmen of the board; hence, there was an increase in the number of companies that appointed independent directors as required by King III. As Adams et al. (2008) posit, pressure from various stakeholders has resulted in companies needing to have a majority of non-executive directors.

Although there was generally little disclosure regarding the evaluation of directors' performance, the examination of the 2012 reports showed that companies are starting to provide some details on the way in which they conduct such evaluations.

Individual indicators that would seem to be in serious need of improvement under this subsection were the existence of induction programmes for new directors and the provision of ongoing training for directors. There was generally very little disclosure provided on these specific recommendations.

The scores relating to this section depicted in Table 4.2 indicate that, overall, companies moved from providing satisfactory disclosures during 2010 to providing more details during 2011 and 2012 on their boards and directors.

The Wilcoxon p -values recorded in Table 4.3 show that although there was some improvement in the disclosure relating to boards and directors from 2010 to 2011 and 2012, improvement over the three-year period was not significant.

4.4 Audit committees

Disclosure regarding audit committees was best; one is left to speculate whether this is due to the fact that the King III recommendations have been aligned to the requirements of the Companies Act. That is, do companies respond more positively to legislation (requirements) than non-mandatory regulation (recommendations)? The entire sample showed improvement in alignment with and disclosure of the King III requirements relating to the composition, expertise, meeting and meeting attendance requirements for these committees. There was evidence of at least four meetings being held by audit committees and certain meetings being conducted with external and internal auditors without management being present. Barua et al. (2010) report that frequent meetings by the audit committee allow the committee to be more effective and also result in better communication between the audit committee and both the external and internal auditors. Abbott and Parker (2000) agree that audit committees that meet at least twice a year are more effective in carrying out their duties.

Furthermore, there was more detailed, clear disclosure on the audit committee responsibilities with regard to internal financial controls, the internal audit function, risk management and the performance of the financial director. Rupley,

et al. (2011) and Zhang et al. (2007) are in agreement that the financial expertise and independence of an audit committee are some of the factors that influence the committee's effectiveness and allow for the effective monitoring of internal controls. It would seem that most companies provided more detail in their audit committee disclosures because this is a statutory requirement.

Although there was improvement in the level of disclosure relating to audit committees, by 2012 only twenty-nine of the sampled companies overall disclosed information relating specifically to the application of a combined assurance model by the audit committee in providing assurance on activities such as risk management, compliance management, internal audit and governance.

As can be observed, according to the average scores recorded in Table 4.2, disclosures relating to audit committees were satisfactory during 2010 and more details were provided during 2011 and 2012. The improvement in the disclosures relating to audit committees was significant from 2010 to 2011 but not significant from 2011 to 2012; this can be validated by the Wilcoxon *p*-values documented in Table 4.3 above.

4.5 Risk management committees

Another area that saw little improvement in reporting was risk management oversight by the risk management committee; most companies appointed an audit committee that acted as both the audit and the risk committee. Most of these companies gave more detail on the disclosures relating to the composition of the committees and meeting attendance, and little to sufficient information on the actual supervision of risk management by these committees. While Drew et al. (2006) posit that effective risk management provides the board with an understanding of the varying nature of the risks faced by entities and assists the board in effectively developing strategies to manage these risks, the level of disclosure for specific indicators that require improvement include the clear identification and management of non-financial risks. Some companies also gave

ambiguous disclosure on whether risk tolerance levels had been set by the committees or boards; there was also vague disclosure of the audit and risk committees' or boards' views on the effectiveness of the risk management processes.

The average scores under risk management committees, depicted in Table 4.2, indicate that there has been little improvement under this section as companies continued to provide merely satisfactory information during the three-year period being tested.

As can be seen from Table 4.3, disclosures relating to risk management committees remained satisfactory over the three-year period and the improvement in disclosures over the period was not significant.

4.6 Remuneration committees

Disclosures relating to remuneration committees were satisfactory during 2010 and 2011, and then saw an improvement during 2012 as companies started to provide more details on their remuneration committees' responsibilities with regard to the determination of the remuneration of executive and non-executive directors. This is supported by the scores reported in Table 4.2. Fourteen of the sampled companies, however, provided little to no information on whether their remuneration committees were operating under formalised charters or board-approved terms of reference as required by King III.

The Wilcoxon p -values in Table 4.3 show that although the improvement in the disclosures relating to remuneration committees was not significant over the three-year period, there was more improvement from 2011 to 2012 compared to 2010 to 2011 – this is supported by a lower p -value for the period 2011 to 2012.

4.7 Nomination committees

Some improvement is still to be made regarding nomination committees. Although the disclosure relating to nomination committees was satisfactory over the three-year period, as can be observed by the scores reported in Table 4.2, twelve of the sampled companies had not yet appointed nomination committees by 2012.

Similar to disclosures relating to risk management committees, the Wilcoxon p -values in Table 4.3 show that disclosures on nomination committees remained satisfactory over the three-year period, thus showing no significant improvement.

4.8 Internal audit function

The disclosures relating to the internal audit function still need improvement. The average scores depicted in Table 4.2 show that companies moved from disclosing little detail regarding their internal audit function, during 2010 and 2011, to disclosing satisfactory detail during 2012. While companies assert that they have set up internal audit functions (either in-house or outsourced), very little information was provided about the functions performed by these departments. The reports also failed to provide sufficient information on whether internal audit reviewed and provided assurance on the effectiveness of the companies' internal control environment, risk management policy and governance. Furthermore, the reports did not provide sufficient information on whether the internal audit functions followed risk-based plans and if the divisions were subjected to independent quality reviews. The score depicting satisfactory disclosure during 2012 was mainly due to adequate disclosure relating to oversight of the internal audit functions by audit committees.

Table 4.3 shows the Wilcoxon p -values relating to internal audit function disclosures over the three-year period; these confirm that there has been no significant improvement in the information reported relating to companies' internal auditing functions.

4.9 The governance of information technology (IT)

This was the most poorly reported-on section. There was little disclosure on how the use of IT was aligned to and enhanced the companies' strategy. Very few companies explained the monitoring of IT spending by the board or other governance body. There was also no disclosure regarding ensuring compliance with IT-related laws and regulations, and oversight over IT risk. Consequently, no independent assurance was obtained on the effectiveness of the IT function.

The average scores detailed in Table 4.2 confirm that there was generally non-compliance, over the three-year period, relating to IT governance disclosures.

Amazingly, although there was general non-compliance regarding the IT governance disclosure required by King III over the three-year period, the Wilcoxon *p*-values recorded in Table 4.3 show that significant improvement in the disclosure was achieved between 2010 and 2011. This significant improvement is attributed to the fact that 2011 was the first year that companies attempted to provide any information on IT governance – 35% of the sampled companies moved from providing no information on IT governance during 2010 to starting to provide details on IT governance during 2011.

4.10 Compliance with laws, rules, codes and standards

Another poorly reported-on area was the area of compliance management; little disclosure was made under this section. Only nineteen companies provided at least satisfactory details on their compliance function over the three-year period. By 2012, twenty of the sampled companies still provided little to no information regarding the setting up of dedicated compliance functions; thus little disclosure was made concerning oversight of compliance with laws and regulations. There was also little disclosure regarding companies' adherence to non-binding rules, codes and standards. The scores reported in Table 4.2 confirm that few details

were consistently provided on the supervision of compliance with laws, rules, codes and regulations over the three-year period.

The Wilcoxon p -values recorded in Table 4.3 show that there was no significant improvement in disclosures relating to compliance management over the three-year period.

4.11 Governing stakeholder relationships

There was a slight increase in the disclosures relating to the identification of different stakeholders and their interests and how the stakeholders' concerns and interests were addressed by the companies. The reports also showed a slight improvement in disclosures, thus showing that companies are engaging more with various stakeholders and considering the needs of the different stakeholders rather than only focusing on creating value for shareholders. As noted by Freeman et al. (2004), engaging with all stakeholders and taking all stakeholders' concerns into account has not prevented companies from addressing the interests of shareholders as the primary stakeholders.

This subsection included one GRI indicator that was weakly reported on – that is, the explanation of the process of rating stakeholder engagement topics in order of their priority. Table 4.2 shows that little detail was provided over the three-year period based on the average scores.

Although little detail was provided on the governance of stakeholder relationships over the three-year period, Table 4.3 shows that there were significant differences in the information provided under this section from 2010 to 2011; no significant improvement was seen between 2011 and 2012, however. The significant difference between 2010 and 2011 may be attributed to the fact that 2011 was the first year that most companies reported on stakeholder engagement processes.

4.12 Integrated reporting

Eccles and Krzus (2010) emphasise that integrated reporting is about communicating the relationship between financial and non-financial performance measures and how the two affect each other. This is another subject that requires improvement. Although the integrated reporting improved, as evidenced by the average scores recorded in Table 4.2 in that on average the inspected reports moved from disclosing little information during 2010 to disclosing satisfactory information during 2011 and 2012, the reports did not provide much information explaining the link between financial and non-financial information disclosed in the reports and there was little independent assurance provided on sustainability issues. Moreover, while companies included a “King III compliance checklist” in their reports, most of the conclusions documented in the compliance checklist did not agree with the actual disclosures made in the reports. For example, the checklist would state that committee meetings were conducted during the year; however, details of these meetings were not included anywhere in the report. Another example is of companies that state on their checklist that their committees were led by independent non-executive directors, while the report contains disclosures which confirm the participation of these same directors in share incentive schemes.

It would therefore seem that most of the non-compliance was due to non-reporting/poor communication in the reports rather than not having followed the recommendations of King III.

Table 4.3 shows Wilcoxon p -values which demonstrate that there was significant improvement in integrated reporting disclosures between 2010 and 2011; the slight improvement from 2011 to 2012 was, however, not significant.

4.13 Sustainability – economic, social and environmental

Most companies reported satisfactorily on their economic, social and environmental sustainability issues even though, as discussed above, they failed to display a clear link between their financial and non-financial performance. The

average scores reported in Table 4.2 show that the sustainability disclosure improved, with little information being provided in 2010 and satisfactory information being provided in 2011 and 2012. Solomon and Maroun (2012) found that the introduction of integrated reporting had resulted in increased levels of disclosure relating to social, environmental and ethical information.

The analysis also showed that it was simpler for companies whose operations had a direct (rather than indirect) effect on the environment or communities around which they operate, such as mining companies, to harmonise their economic/financial, social and environmental efforts. This finding can be supported by the fact that in their study of the impact of integrated reporting on social, environmental and ethical disclosures, Solomon and Maroun (2012) only sampled companies from “high social or environmental impact sectors”.

Table 4.4 confirms this by comparing the average scores of the basic resources sector with the technology sector; these scores validate the fact that sustainability disclosures were better and improving for the basic resources sector, whereas little detail with no improvement were being provided by companies in the technology sector.

Table 4.4: Average scores under economic, social and environmental sustainability			
Sector	2010	2011	2012
Basic Resources	3.78	4.4	4.5
Technology	2.83	2.8	2.8

The Wilcoxon p -values in Table 4.3 illustrate that there was no significant improvement in the disclosures relating to economic, social and environmental sustainability over the three-year period.

4.14 Overall comments

Overall, the results show that companies are still on a journey towards eventually providing an integrated report that clearly displays an integration of financial and non-financial performance. King III requires the board of directors to apply its collective mind to determining the contents of an integrated report. In line with this, the integrated reporting framework allows the preparers of the report to use their own judgement when determining the disclosures to be made in their report (IIRC, 2013). What constitutes integrated reporting remains a subject of international debate; hence it has been challenging to identify any comparability among the various integrated reports. Although comparability was not evident in the different companies' reports, the individual company reports were comparable in that the table of contents over the three-year period remained very similar. Certain disclosures were reported on in exactly the same way as the previous year with the exception of updating figures to relate to the relevant year. This could be a contributing factor to the problem identified by Kolk (2003, p. 289), who cautions that sustainability reporting may sometimes be regarded as "mere window-dressing", and why Steyn and De Beer (2011) posit that integrated reporting could be used for public relations purposes.

As the discussions above show, the following, among others, are some of the areas identified for development: a lack of induction programmes and ongoing training for directors, no information on board and committee evaluations, non-disclosure/little disclosure on IT governance, compliance management, harmonising the financial and non-financial information, limited disclosure on internal audit, and obtaining assurance on the non-financial information. PwC (2012) also conclude that much improvement is required in relation to the way that companies report on the new elements of King III.

As can be seen from the above analysis, although some improvement has been made with regard to certain subsections of the research indicators, the p -values reported in Table 4.5 below show that, overall, the improvement for all companies and per sector has not been significant.

The p -values reported in Table 4.5 show that although there has been some improvement overall in the disclosures made by companies under King III, this improvement was not significant from 2010 to 2011 to 2012. This is evidenced by all of the p -values being greater than 0.05. It is further noted that the p -values relating to the real estate sector and the technology sector remained constant from 2010 to 2011 and 2011 to 2012, thus demonstrating that the improvement in the level of disclosure from 2010 to 2011 was the same as from 2011 to 2012. This can be corroborated by the overall average scores observed for these sectors: real estate (average score of 2.5 in 2010, 2.8 in 2011 and 3.1 in 2012) and technology (average score 3 in 2010, 3.1 in 2011 and 3.2 in 2012).

The figures included in Appendix B can be referred to for an analysis of the performance of each sector in the different subsections.

Table 4.5: Overall <i>p</i> -values for all companies by sector		
Details	2010 vs. 2011	2011 vs. 2012
All companies (all sectors)	0.0692	0.3837
Basic Resources	0.4647	0.6015
Construction & Materials	0.1913	0.5637
Financial Services	0.6015	0.4647
Food & Beverage	0.2506	0.754
Health Care	0.6631	0.7728
Industrial Goods & Services	0.1488	0.7483
Oil & Gas	0.5127	0.2752
Real Estate	0.2752	0.2752
Retail	0.2506	0.6015
Technology	0.4386	0.4386
Telecommunications	0.2482	0.5637

CHAPTER 5: CONCLUSION AND RECOMMENDATIONS

The purpose of this study was to assess the trends in integrated reporting by JSE listed companies over a three-year period since the inclusion of the King III recommendations in the JSE listing requirements. The assessment was conducted by inspecting the annual integrated reports of fifty-two JSE listed companies issued for the financial years ended 2010, 2011 and 2012, for specific disclosures that have been recommended by King III and some GRI indicators relating to sustainability reporting. The fifty-two companies included companies from the various sectors listed on the JSE had varying market capitalisation.

The level of disclosure relating to each research indicator was scored on the basis of the rating scale discussed under section 3.4. Average scores were then determined for each subsection of the research indicators to ascertain whether there had been improvement in the level of disclosure from 2010 to 2011, and from 2011 to 2012. Furthermore, *p*-values were calculated to assess whether the change in the level of disclosure was significant or not.

The results have rejected the Wilcoxon signed-rank test's null hypothesis, which assumes that the extent of disclosure is the same in 2011 as it is in 2010, and the same in 2012 as it is in 2011. The alternative hypothesis that the extent of disclosure in 2010 is not the same as in 2011 and disclosure in 2011 is not the same as in 2012 has not been rejected as the results show that companies moved from reporting satisfactory details to providing more details in disclosures relating to boards and directors, audit committees and remuneration committees. Satisfactory details were consistently provided for disclosures relating to ethical leadership and corporate citizenship, risk management committees and nomination committees. However, the results show that little detail was consistently provided for disclosures relating to compliance management (compliance with laws, rules, codes, and standards), and governing stakeholder relationships. The disclosures relating to the internal audit function, integrated reporting and economic, social and environmental sustainability saw an improvement from little detail to satisfactory detail being provided by companies.

Overall, companies displayed the worst disclosure under IT governance; there was generally non-compliance with the King III requirements for IT governance over the three-year period.

The results show that there was some improvement in the level of disclosure; this was evidenced by increasing average scores over the three-year period from 2010 to 2012. Although significant improvement in disclosure was observed from 2010 to 2011 with regard to disclosures relating to audit committees, the governance of IT, governance of stakeholder relationships and integrated reporting, only these indicators showed significant improvement from 2010 to 2011. Moreover, overall improvement taking all the indicators into account was not significant, as the overall *p*-values (Table 4.3) over the three-year period are greater than 0.05.

Other noteworthy details that were observed during the analysis of the annual integrated reports include the following: Some companies still issued separate reports containing different information rather than one integrated report (all sampled companies issued a single report for 2010, one issued multiple reports in 2011 and six companies issued multiple reports in 2012). There was a slight increase in the average number of pages per report issued over the three-year period (from 136 in 2010 to 140 in 2011 and 151 in 2012). In addition, the reports of companies with a larger market capitalisation contained more disclosures compared to smaller companies. It was also observed that the issuing or preparation of reports under King III did not necessarily translate to the reports being called integrated reports; certain companies still issued an “annual report”.

Integrated reporting is a journey and companies have acknowledged in their reports that further improvements should be expected in the future as they find their way in producing integrated reports that explain concisely the relationship between their non-financial performance (including governance) and their financial performance.

Future research should focus exclusively on disclosures relating to the new sections of King III to test whether any significant progress is being made by companies in providing more detailed information.

It was observed that smaller companies had poorer disclosure compared to larger companies. Another observation was that it was simpler for companies whose operations had a direct impact on the environment or society to harmonise their financial and non-financial performance. It would, thus, be valuable for future research to conduct a cost-benefit analysis of the application of King III in order to understand whether this could be a contributor to smaller companies displaying poorer disclosure than bigger companies and how the cost of providing the disclosures influences what or how much various companies decide to disclose.

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APPENDIX A: Research Instrument (Indicators)

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.
2. Company strategies and vision are clearly outlined.
3. Mission statement and company values are provided.
4. Ethical standards are articulated in the code of conduct.
5. Independent assurance of ethics by internal audit or external assurance providers.

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

6. Company is governed by a unitary board of directors.
7. Directors are appointed through a formal process.
8. Board is comprised of a majority of non-executive directors.
9. Of the non-executive directors, the majority is independent.
10. Board is chaired by a non-executive independent director.
11. Board has appointed a lead independent director if the chairman is not independent.
12. The CEO is a board member.
13. The financial director (or CFO) is a board member.
14. Qualifications and experience of directors are disclosed.
15. Board is assisted by a competent, suitably qualified and experienced company secretary.
16. Board is regulated by a formal charter which sets out the role of the board and each director.
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.
18. Committees are regulated by formal charters which set out the role of individual committees.

19. Board meets at least four times a year.
20. Satisfactory attendance of board meetings as per the attendance register.
21. Induction programme for new directors is in place.
22. Ongoing training for all directors is in place.
23. Performance of the board, individual directors and committees is evaluated on a regular basis.
24. Share option scheme is not available to non-executive directors.
25. Policy is in place for appointment and retirement of directors.
26. Remuneration of directors and senior executives is disclosed.
27. Remuneration of the three most highly-paid employees (other than directors) is disclosed.
28. Remuneration policy regarding directors is approved by the shareholders.

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.
30. Formal charter and processes are in place outlining the functions of the audit committee.
31. Suitably skilled and experienced independent non-executive directors.
32. Comprised of at least three non-executive, independent directors.
33. Chairman of the Board is not a member of the audit committee.
34. Chaired by a non-executive, independent director, other than the chairman of the Board.
35. Meets at least 2 times a year.
36. Satisfactory attendance of audit committee as per attendance register.
37. Oversees internal and financial controls.
38. Oversees internal audit function.
39. Oversees financial risk management (and other risks if necessary).
40. Assesses the performance, expertise and skills of the financial function including financial director.
41. Oversees the preparation of the integrated report (including sustainability issues).

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.
43. Evaluates independence and credentials of the external auditor.
44. Evaluates performance of the external auditor.
45. Reports to the board and shareholders on how it carried out its responsibilities.

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

46. Board appoints risk and/or audit committee to oversee risk management.
47. Risk (or audit) committee consists of at least 3 directors (both executive and non-executive).
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).
49. Formal charter and processes are in place outlining the functions of the risk/audit committee.
50. Risk (or audit) committee meets at least 2 times a year.
51. Satisfactory attendance of risk (or audit) committee as per attendance register.
52. Risk committee (or audit/board) identifies key financial risks and quantify them, if possible.
53. Risk committee (or audit/board) identifies key non financial risks and quantify them, if possible.
54. Risk committee (or audit/board) explains how the identified financial risks will be addressed.
55. Risk committee (or audit/board) explains how the identified non financial risks will be addressed.
56. Risk committee (or audit/board) sets levels of risk tolerance.
57. Risk committee (or audit/board) expresses its views on the effectiveness of the company's risk management processes.

E. Remuneration committee [King III – Chapter 2]

- 58. Remuneration committee comprises at least two non-executive and independent directors.
- 59. It is chaired by an independent non-executive director, other than the chairman of the Board or executive director.
- 60. Formal charter and processes are in place outlining the functions of the remuneration committee.
- 61. Remuneration committee meets at least 2 times a year (not required by King III but considered necessary for the purposes of this research).
- 62. Satisfactory attendance of remuneration committee as per attendance register.
- 63. Remuneration committee or other structure determines remuneration of executive and non-executive directors.

F. Nomination committee [King III – Chapter 2]

- 64. Nomination committee comprises at least two non-executive and independent directors.
- 65. It is chaired by an independent non-executive director, who can also be the chairman of the Board, other than the executive director.
- 66. Formal charter and processes are in place outlining the functions of the nomination committee.
- 67. Nomination committee meets at least twice a year (not required by King III but considered necessary for the purposes of this research).
- 68. Satisfactory attendance of nomination committee as per attendance register.
- 69. Nomination committee or other structure recommends the appointment and dismissal of executive and non-executive directors.
- 70. Directors nominated by the committee or other structure are presented for approval by the shareholders.

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

- 71. Internal audit function has been set up (within the company or externally).
- 72. Internal audit function reports to the audit committee.
- 73. Internal audit is headed by the chief audit executive (CAE) or external company.
- 74. Internal audit (or its CAE)/external company attends audit committee meetings, board meetings by invitation.
- 75. Internal audit/other structure provides assurance on the effectiveness of internal control environment.
- 76. Internal audit/other structure provides assurance on the effectiveness of risk management.
- 77. Internal audit/other structure provides assurance on the effectiveness of governance (including ethics).
- 78. Internal audit is subjected to an independent quality review.
- 79. Internal audit follows a risk-based approach to its plan.

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

- 80. Board or other structure monitors and evaluates significant IT investments and expenditure.
- 81. A suitably qualified and experienced chief information officer (CIO) is appointed to manage IT.
- 82. Board or other structure ensures that IT complies with IT related laws, rules, codes and standards.
- 83. Risk committee or other structure oversees overall risk implications of IT.
- 84. Audit committee or other structure oversees financial risk implications of IT.
- 85. Board receives an independent assurance on the effectiveness of IT through internal audit function and/or external assurance providers.

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

- 86. Compliance function has been set up by the company.
- 87. Compliance function/other structure oversees compliance with laws, rules, codes and standards.

88. Company discloses non binding rules, codes and standards to which it adheres.

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

89. Board identifies key stakeholders and their interests on a regular basis.
90. Interests of key stakeholders are taken into account in the integrated report.
91. Explanation of the process used for rating topics in the order of priority.

K. Integrated reporting [King III – Chapter 9; Global Reporting Initiative, 2011]

92. Financial and sustainability issues on economic, social and environmental impacts all covered in one or more documents of integrated report.
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.
94. Information on integrated reporting components is harmonised and a link drawn to show interdependencies between these components in the integrated report.
95. Sustainability issues and disclosures are independently assured (under the auspices of the audit committee or other structure).
96. Report clearly indicates whether King II/III guidelines have been followed.
97. Report clearly states areas of improvement on King II/III guidelines.
98. Report clearly indicates whether Global Reporting Initiative (GRI) guidelines have been followed.
99. Report clearly states areas of improvement on GRI guidelines.
100. Index is provided as per GRI guidelines.
101. Glossary of Terms provided as per GRI guidelines or other guidelines.
102. Report provides proper referencing with page numbers for each major issue covered.

L. Economic Sustainability [Global Reporting Initiative, 2011]

- 103. Value-add statement and other economic/value-add information are provided.
- 104. Quantification of economic efforts.
- 105. Report is easy to read.

M. Social Sustainability [Global Reporting Initiative, 2011]

- 106. Involvement in CSI programmes for employees and communities such as training, education, sports, HIV/AIDS, donations, bursaries.
- 107. Quantification of costs as well as the number of social projects/programmes.
- 108. Report is easy to read.

N. Environmental Sustainability [Global Reporting Initiative, 2011]

- 109. Implementation of sound environmental programmes.
- 110. Quantification of costs incurred and efforts to curb environmental damages.
- 111. Report is easy to read.

APPENDIX B: Disclosures per sector over the three-year period

