

**IS THERE AN AUDIENCE FOR PUBLIC SECTOR ANNUAL REPORTS: AUSTRALIAN
EVIDENCE?**

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Structured Abstract

Purpose - The purpose of this research is to investigate the role and importance of the annual report as a source of information about public sector entities.

Methodology/Approach - This research uses a survey methodology to access users of public sector annual reports and is innovative because it has directly studied actual users across the entire public sector.

Findings - The findings of this research indicate that the annual report is an important source of information about public sector entities but it is not the most important source of information. This study also found that the annual report is not regarded as equally important across all public sector entity types. Differences in the importance attached to the annual report by different stakeholder groups were also noted.

Research Implications - These findings have important implications for policy makers with respect to the information content of public sector annual reports. In particular the blanket approach to legislative requirements for annual reporting may need to be reviewed in view of the findings of this research that there are differing levels of importance attached to the annual report as an information source by users from different public sector entity types.

Originality – The research in this paper is original in that it has, systematically and directly accessed users of public sector annual reports to determine their information sources.

Paper Type – Research Paper

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ABSTRACT

Internationally, the increased emphasis on performance and accountability in the public sector in the last quarter of a century has led to a greater awareness of mechanisms that are available to discharge accountability. In this respect, policy makers have placed increased reliance on the annual report. Some argue the annual report is an integral part of citizen engagement that enables government agencies to discharge their accountability obligations to a diverse group of stakeholders. Others discount the importance of annual reporting arguing that in spite of the considerable resources consumed to produce these reports there is no public interest in them. In terms of adding to this debate, there is little empirical evidence on stakeholders' use of the annual report, the importance of annual reports as an information source to stakeholders and the importance of other forms of information. This study uses a survey method to obtain the views of recipients of annual reports across three different Australian public sector entity types – government departments, local government authorities and government owned corporations to determine whether stakeholders in the public sector consider the annual report to be an important information source relative to other information sources. The study finds that the annual report is considered an important source of information, and further, that this perception varies for the different public sector entity types and across different stakeholder categories. This research has important implications for policy makers in their consideration of accountability mechanisms to stakeholders.

KEY WORD: Public Sector Annual Reports

INTRODUCTION

The public sector reforms which have been embraced in western countries since the 1980s have placed the spotlight on the governance of public sector organisations. Accountability is an important element of good governance. Access to information in a form that allows users to gauge whether the objectives of the organisation are being discharged and to assess its performance is an essential pillar of accountability. In both the private and public sectors, one of the main vehicles used to discharge accountability is the annual report (Cameron 2004).

The concept of the private sector annual report has a long and unchallenged history. It is widely regarded as the main accountability mechanism, reporting on the governance and performance of an organisation. This concept and format of the annual report has been translated, unchallenged, into the public sector. This translation has three main implications for the public sector, all of which lack empirical substantiation. First, the relative importance of the annual report in both sectors has been assumed to be equal. However, it is widely argued that in the public sector, in the absence of a market, and definable performance measures, accountability through the regulated disclosure of information is even more important (Hooks, 2002; Coy et al., 2001; Guthrie et al., 2003). Second, the format and content of the public sector annual report has been adopted from the private sector with little regard for the differences in operating structure and objectives of the organisations in the two sectors. An annual report commonly comprises both descriptive information about the entity and its activities usually at the beginning of

the report and the statutory information - the audited financial statements which comprise the audited general purpose financial report at the end of the report (Stanton and Stanton, 2002). The third implication in prescribing requirements for annual reports, is that public sector regulators in some western democracies have treated the public sector as consisting of an homogenous group of organisations (as indeed the listed companies in the private sector are) and has failed to differentiate requirements between the different public sector organisations. Consequently, in Australia, all public sector organisations (local governments, departments of state and corporatised bodies) have similar annual reporting requirements despite the differences in terms of complexity and diversity of the accountability relationships and the different operating, financial and legal structures of these organisations.

It is the lack of the empirical verification of this translation of the annual report into the public sector that has raised a number of unresolved dilemmas for public sector researchers. Internationally, there have been numerous attempts to determine the use made of the annual report by public sector stakeholders (see for example Butterworth et al., 1989; Lapsley, 1992; Hodges et al., 2002 in the UK, Alijarde, 1997 in Spain, Steccolinni, 2004 in Italy, Skaerbaek, 2005 in Norway, Coy et al., 1997 in New Zealand and Clark, 2001 in Australia). Concurrently several researchers have investigated the approaches taken by public sector entities in reporting to their external stakeholders. Lee (2004) argues that there are two approaches which public sector entities can take in reporting to their stakeholders. He refers to the traditional institutional approach which involves an indirect

reporting relationship with the public through intermediaries such as the media or oversight bodies and a direct approach where the entity communicates directly with its stakeholders. Lee (2004) argues, in an American context, that organizations have found the traditional indirect approach to reporting to external stakeholders through intermediaries unsatisfactory, and have sought a direct involvement with the public through the development of the public report. Similarly in an Australian context Parker and Gould (1996) and Guthrie (1998) have argued that there has been a shift from traditional reporting mechanisms to a reporting regime which is more market and customer oriented.

It is the indepth investigation of this direct reporting to stakeholders which is the focus of this paper. Skaerbaek (2005) acknowledges that it has been a “recurrent ambition” of researchers to analyse who uses annual reports. However, in the main, studies have relied on proxies for actual users. Carlin (2005) acknowledges that the justification for the use of proxies is the difficulty in obtaining “hard evidence” on actual users. This is the contribution this paper makes to the extant literature; it is a survey of actual users of annual reports, across the different types of public sector entities.

The issue of the use of the annual report, and its resolution, has important public policy implications. Not only are considerable resources expended by public sector agencies in the preparation of these reports (Jones and Pendlebury, 2004; Skaerbaek, 2005) but some governments have made a strategic decision to step up their direct

reporting to the public as part of a focus on citizen engagement (Lee, 2004). If reports are not being accessed by stakeholders, then policy makers will need to review the ways in which they discharge their accountability obligations. What is the composition of the stakeholder profile of those that use the annual report? How useful do they find the annual report relative to other sources of information about an organization? These are empirical questions that have not been effectively addressed to date.

The paper proceeds as follows. The next section examines the prior literature pertaining to the production of annual reports in the public sector. The section following then outlines the research methodology, the results and the policy implications that flow from the research are then reported and the final section details the limitations of the study and suggests avenues for further research.

APPROACHES TAKEN IN PRIOR STUDIES

There are a number of prior studies which aim to identify the stakeholders of annual reports. For the purposes of this current study, it is useful to classify them according to their methodological approach.

Most studies that have been conducted have used normative arguments to identify stakeholder groups or classifications. The seminal work in the area is that by Anthony (1978). He aimed to have a brief list and normatively identified five categories of stakeholders; governing bodies, investors and creditors, resource

providers, oversight bodies, and constituents. Other researchers have also used a normative approach, and have identified similar categories to Anthony (see for example Davidson, 1977; Holder 1980; US and Canadian Auditors General, 1985; Jones et al., 1985; Drebin et al., 1981; Hay and Antonio, 1990; Daniels and Daniels, 1991; Priest et al., 1999). Some researchers have used these normatively identified classifications of stakeholders as a starting point and have attempted to empirically identify stakeholder groups. Atamian and Ganguli (1991) found that other municipalities were common recipients of the financial reports of municipalities in the US. While the focus of the prior work was external stakeholders, internal management was identified as a stakeholder of financial information by both a US study (Van Daniker and Kwiatowski, 1986) and a Spanish study (Alijarde, 1997).

A second and smaller group of studies have sought to empirically determine the actual stakeholder profiles by accessing actual users of reports. Butterworth et al., (1989), attempted to identify if the general public actually read annual reports. The method employed to identify users was to leave a questionnaire in copies of a local government's annual report. The copies of the annual report were available in public libraries and the librarians ensured that a questionnaire was always in the report. Because of the low response rate, the study was inconclusive with regard to identifying users. This study also examined the readability of the annual report. The study concluded that as a means of widespread communication, the annual reports were not effective.

In a New Zealand study, Coy et al., (1997) attempted to directly identify the users of tertiary education institutions' annual reports and sought their views on the qualities and disclosures of the annual reports that they received. They used a similar data collection method to that of the UK study, but refined the method by obtaining the co-operation of tertiary education institutions in placing cards in all reports distributed and then surveying those recipients who returned the cards. The study revealed that of the recipients who identified themselves by returning the cards, 60% had a role in the management, operation or governance of the institutions, 10% were involved in other educational institutions' management, 25% were managers of businesses or employee organisations and the remainder were journalists, librarians, Members of Parliament and members of the general public. This study provided further evidence of the widespread use of the annual report by internal stakeholders.

The most comprehensive study of recipients and users of public sector annual reports is Clark's (2001) Australian study of eight Victorian government departments. He used the actual mailing lists of these departments to examine the distribution patterns of annual reports and then followed up this interrogation with a survey of recipients. The importance of this study is that the data source used (the mailing lists) allowed for a more reliable and comprehensive identification of users of annual reports than previous studies. The users identified by Clark represent a broader range of stakeholders than prior studies and the study found that library and information services and other government agencies were significant user categories.

While the prior research on stakeholder identification has been sustained and international in focus, it has been piecemeal to the extent that there has been no systematic interrogation of **actual users** of annual reports across all the **different public sector entity types**.

RESEARCH METHOD

Research Approach and Scope

The view adopted in this study was that the most reliable and effective way to determine the role of annual reports and their importance relative to other information sources was to access the recipients of public sector annual reports directly and obtain their views.

Recipients of annual reports of three different entity types in Queensland¹ were included in the study: government departments; local government authorities and government owned corporations. Each of these entity types operates in a different environment and this could be expected to impact on the perceptions of stakeholders on the role of the annual report. Local government authorities operate in a localised environment where the same broad group of stakeholders both receive services and contribute revenues. In central budget agencies (government departments) however there is not necessarily a direct relationship between the receipt of services from an agency and the contribution of revenue. Government owned corporations are largely self funding as a result of charging a fee for service and are profit oriented.

The actual annual report mailing lists used to mail the 1999 annual report of the entities selected for inclusion in the study were obtained. At this time the internet was not used widely as a dissemination medium, and thus there was a 'window of opportunity' in which to gather information about users of annual reports. Once annual reports are freely and widely available on line, the question of determining and accessing annual report users becomes more complex if not impossible due to privacy legislation.

Data Collection

Government Departments

In Australia, government departments have been classified as either central agencies or line departments (Nichols, 1991; Funnell and Cooper, 1998; Fitzgerald et al., 1996). Central agencies are generally described as those departments that have the responsibility to provide advice and support to the executive government on such issues as whole of government co-ordination and future directions. Line departments are also referred to as service departments reflecting their service delivery role. It is likely that the information needs of stakeholders for both of these types of entity will differ and hence their reliance on specific sources of information will vary. Five departments were chosen for inclusion in the study. Queensland Treasury, the largest central agency is the most influential financial policy-making body within the Queensland government.² The Department of Health is the largest spending line agency and a 'traditional' service department. The Public Works Department was included because it operates Commercial Business Units through which it has significant private sector involvement.³ It may be that the identification of the

information sources of its stakeholders will cover a broader spectrum of users in comparison to a line department that has no commercial activities. The Department of Corrective Services and Department of Aboriginal and Torres Strait Islander Policy were chosen because of the sensitive nature of their undertakings and the degree of media scrutiny they receive.

Local Government Authorities

At the time of the study there were 125 local government authorities in Queensland classified into 22 categories in accordance with the Australian Classification of Local Governments Classification system. All of the local government authorities in Queensland were approached to participate in the study. Ninety-seven organisations (78% of local government authorities) agreed to participate in the study.

Government Owned Corporations

There are two types of Government owned corporations - Public Financial Enterprises and Public Trading Enterprises (Fitzgerald, 1996). The three largest government owned corporations were selected - Queensland Investment Corporation (a Public Financial Enterprise) and Queensland Rail and Energex (Public Trading Enterprises).

In summary, the choice of entities in each category was made to maximize the exposure to as many stakeholders and their information sources as possible.

Data Analysis

The annual report mailing lists of the 105 entities (5 departments, 97 local governments and 3 government owned corporations) chosen were obtained and formed a database for distribution of a mailed survey. This illustrates one of the methodological strengths of the research that it surveys **actual** recipients. Recipients received a research instrument specific to the entity for which they received an annual report. Two points are worth of note. First, this study asked respondents to self assess the nature of their relationship with the entity. A methodological strength of this paper comes with this direct identification of stakeholders. Prior studies have assigned stakeholders to categories. Stakeholders were given the choice of the 7 categories which were commonly agreed in the public sector accounting literature, ratepayers/taxpayers, other resource providers, elected officials, other recipients of services, oversight bodies, internal management and other like entities (see for example Anthony, 1978; Coy et al., 1997; Clark, 2001). This direct identification of stakeholder groups allows an accurate assessment of the absolute and comparative importance of the annual report from an individual stakeholder perspective. Second, the research instrument asked respondents to indicate the importance, on a five point Likert scale, of a number of sources of information about public sector entities.

Five information sources were presented to the recipients for consideration. As already noted, in recent times public sector entities have been moving to communicate more directly with their stakeholders and not rely on the more traditional indirect methods of using intermediaries (Lee, 2004). This research

considered both of these communication techniques. Three of the information sources represented attempts by the public sector entities to communicate directly with stakeholders. These were annual reports, budget papers and personal contact. Two information sources, the newspaper and TV/Radio represented the more traditional communication through intermediaries. This allowed for both absolute and comparative assessments to be made of the importance of the annual report of an entity to its recipients from an individual entity-type perspective. Recipients were also given the opportunity to indicate whether they had any other information sources available to them.

RESULTS AND DISCUSSION

In total 4,595 research instruments were sent to recipients of annual reports produced by public sector entities in Queensland – there was 999 useable responses. Overall a response rate of 21.7 % was achieved – 24.6% for departments, 23.7% for local governments and 16.5% for government owned corporations. This response rate compares favourably with response rates achieved by other surveys of this type (Jones et al., 1985 – 10%; Priest et al., 1999 – 19%, Dixon et al., 1994 – 56%).⁴

The importance of the annual report relative to other sources of information

Table I reports the mean score for each information source for the entire group of public sector respondents.⁵

TAKE IN TABLE I

Taking the responses in total, personal contact with the entity is rated as the most important source of information by public sector entity stakeholders and is the only information source to be rated as ‘very important’. Annual reports are ranked as the second most important source of information and are rated in the ‘important’ range. Although not ranked as highly as annual reports, budget papers, newspapers and the TV and radio were all ranked important sources of information. Overall the direct methods of communicating with stakeholders rank more highly than the traditional intermediary communication (indirect) techniques. While, to our knowledge, there has been no study in the private sector that taps the relative importance of information sources, this result, that there are many sources of information about the performance of public sector entities, provides valuable insights to public sector regulators. Currently, there is no one consolidated bank of information available on the performance of public sector entities – piecemeal information is obtained from a variety of sources.

This aggregated data endorses the importance of the annual report to stakeholders and provides preliminary evidence that the reports are used by stakeholders. The next two sub-sections seek to capitalize on the methodology strengths of the paper, by elaborating on this overall public sector picture. First, the responses are broken down by the three different public sector entity types, and then the different stakeholder groups within entity types are interrogated to provide a more detailed picture.

The importance of the annual report relative to other sources of information by entity type

Table II seeks to obtain a finer picture than that provided in Table 1, by analyzing the results for each of the three different types of public sector entity – departments of state; local government authorities and government owned corporations.

TAKE IN TABLE II

The breakdown of the overall results to reflect the views of the stakeholders of particular public sector entities reinforces the preference for stakeholders for direct communication with public sector entities. Personal contact and the annual report are the two most important information sources for stakeholders from all three public sector entity types. However, some differences between entity types are also apparent. Government owned corporation stakeholders and local government authority stakeholders both rate the annual report as a very important information source in contrast to government department stakeholders who rate the annual report as an important information source. Further, while for local government authorities and government departments personal contact is still the most important source of information, for government owned corporation stakeholders the annual report is the most important information source. The most likely explanation for this is that the operating and financial structures of government owned corporations are of the

private sector type where the annual report has a long history of being the primary accountability document.

Inspection of the results reported in Table II also indicates that with the exception of annual reports local government stakeholders find all of the information sources, more useful than stakeholders from government departments and government owned corporations. One explanation for these results could be the broader, more direct and immediate relationship that stakeholders in local government authorities have to the entity when compared to that which stakeholders of government departments and government owned corporations have with those entities.

The results add to the prior literature. With respect to Australian local governments, they reinforce the importance of personal contact as an information source (Kloot and Martin 2001). However, they contradict the results of Butterworth et al., (1989) in the UK, where he found there was 'no interest in annual reports' for local government authorities. On a broader level, the diversity of sources of information highlights the importance of the debate about the understandability of the information contained in annual reports, particularly how accessible the information contained in local government reports is (see for example Jones et al., 1985; Collins et al., 1991; Priest et al., 1999; Mack, 2004).

These results provide empirical evidence that annual reports are an important information source for most public sector entity types, and reinforce the emphasis

that policy makers have placed on annual reports. As this research surveyed actual users and also asked them to classify themselves into stakeholder types, rather than using proxies for users as the majority of prior research has done (see for example Alijarde, 1997; Priest et al., 1999; Hay, 1994; Mignot and Dolley, 2000) the pattern of usage of the annual report by each stakeholder category can be explored in order to obtain precise information to assist regulators and preparers.

The importance of the annual report as an information source by stakeholder category

Following the lead of prior research (see for example Collins et al., 1991; Taylor and Rosair, 2000 and Cheng 1994) the responses were classified into internal or external stakeholders based on the stakeholder group to which respondents had self-selected. External stakeholders are those to whom an accountability obligation is owed, and they rely on the organization to provide information. Internal stakeholders are those stakeholders who have a defined role within the organization and thus have access to information sources themselves, they are not dependent on the organization to provide information. Consistent with prior research (Collins et al., 1991; Taylor and Rosair, 2000 and Cheng, 1994) internal management and elected officials were classified as internal stakeholders. The remaining stakeholder groups were classified as external stakeholders.

TAKE IN TABLE III

The results of this table indicate that while overall external stakeholders, the primary target of annual reports, account for 54% of respondents, this result is not consistent across entity types. Government owned corporations have a large proportion of external respondents (92%) while for local government authorities external respondents only account for 37% of respondents. This large difference has the capacity to confound an assessment of the role of the annual report to stakeholders in so far as the primary audience for annual reports is external stakeholders and the primary purpose for producing annual reports is to directly communicate with external stakeholders. As a consequence Table IV analyses the results for external stakeholders for each of the three different types of public sector entity.

TAKE IN TABLE IV HERE

Several issues worthy of consideration emerge from the results reported in this table. First, at this level of analysis (external stakeholders) only respondents from government owned corporations find the annual report as a 'very important' source of information. This result can be explained by the emulation of the governance and reporting processes of private sector companies by government owned corporations. Second, once again with the exception of annual reports, respondents from local government authorities find all source of information more important than respondents from either departments or government owned corporations. This greater interest in information about local affairs is consistent with the patterns of community engagement highlighted by such researchers as (Passey, 2004 and Putnam, 2000) .Third, for external stakeholders of local government authorities the

annual report was the third ranked information source behind personal contact and the newspaper. This result would seem to indicate that although external stakeholders of local government authorities have embraced the notion of direct reporting by the authorities they have not done so at the expense of the more traditional reporting through intermediaries. One reason for this could be that regional and local newspapers contain relevant and timely information about local government authorities that is of interest to local government authority stakeholders. These results are consistent with Kloot and Martin (2001) who argue that local government stakeholders need accessible and understandable information on many facets other than accountability information, and this is not provided in the annual report.

CONCLUSIONS

This study has adopted a research methodology that directly surveys stakeholders of the three different public sector entity types to obtain insights into the role of the annual report as a source of information. The results support the notion of direct reporting to stakeholders by public sector entities. Direct reporting mechanisms comprise the top sources of information for departments, local governments and government owned corporation stakeholders. These results empirically support Lee's (2004) argument that agencies are beginning to place more emphasis on annual reporting as a way of directly engaging with their stakeholders.

The results have implications for policy makers internationally, who are charged with the responsibility for determining the content of annual reports. Regulators need to differentiate content prescription depending on entity type. Moreover, they support the various efforts being made internationally to tailor the information provided to stakeholders. Examples of this are seen in the US through the services effort and accomplishment reporting framework established by the Governmental Accounting Standards Board and the attempts to simplify reporting embodied in the move towards “Popular Reporting” in local governments (Carpenter and Sharp, 1992); in Australia through the provision of audited performance, and the moves to simplification with the production of a Community Financial Report (Cunningham, 2001).

A limitation to this research lies in its reliance on the use of a mailed survey as the data collection method. There is no guarantee that the person to whom the research instrument was sent was the person who actually completed the survey. With governments spending increasing resources on annual reporting, future research could aim to capture the views of those who currently do not use the annual report to assess the changes that need to be implemented.

¹ Queensland is one of the 8 jurisdictions in the federation of Australia. This jurisdiction was chosen as the focus of this study initially because of accessibility of data to the researchers but also because similar annual report legislation has been adopted throughout Australia there is no reason to suspect any cross jurisdictional differences. While it could be argued that the external validity of the study has been limited by selecting only one jurisdiction, the internal validity of the study has been strengthened particularly with regard to the between levels of government analysis. As all the public sector entities come from one state any other factors that may influence the use of annual reporting

practices, for example size, culture, economic circumstances or the political environment have been controlled for.

² Queensland Treasury had a budget of \$1,371m in 1998/99 compared to \$176m for the Department of Premier and Cabinet and \$148m for the Department of State Development.

³ The Business Units for the Department of Works are Project Services, QPM Property Management, Qbuild, GoPrint, Qfleet and Sales and Distribution Services.

⁴ In the Dixon (1994) study the response rate reflects that the survey instrument was sent to people who had already indicated their willingness to participate in the research by supplying their contact details to the researchers.

⁵ The mean score means the average score of all of the respondents for each entity type.

Table I

Mean score* for each source of information

Information Source	All Respondents n=999
<i>Direct</i>	
Personal Contact	4.20
Annual Report	3.93
Budget Papers	3.58
<i>Indirect</i>	
Newspaper	3.53
TV/Radio	3.14
Internet	2.84

*1-2 unimportant, 2-3 not very important, 3-4 important, 4-5 very important

Table II

Mean score* for each entity type for each source of information

Information Source	All Respondents n=999	Departments n=289	Local Government Authorities n=540	Government Owned Corporations n=170
<i>Direct</i>				
Personal Contact	4.20	4.03	4.38	3.92
Annual Report	3.93	3.62	4.04	4.13
Budget Papers	3.58	3.13	3.82	n/a
<i>Indirect</i>				
Newspaper	3.53	3.21	3.75	3.35
TV/Radio	3.14	3.10	3.26	2.80

*1-2 unimportant, 2-3 not very important, 3-4 important, 4-5 very important

Table III

Analysis of stakeholders by public sector entity type

	Total	Departments	Local Government Authorities	Government Owned Corporations
External	541 (54%)	189 (65%)	196 (36%)	156 (92%)
Internal	458 (46%)	100 (35%)	344 (64%)	14 (8%)
Total	999 (100%)	289 (100%)	540 (100%)	170 (100%)

Table IV

Mean score* for external stakeholders for each entity type for each information source

Information Source	Departments n=189	Local Government Authorities n=196	Government Owned Corporations n=156
<i>Direct</i>			
Personal Contact	3.92	4.22	3.88
Annual Report	3.62	3.80	4.16
Budget Papers	3.06	3.20	n/a
<i>Indirect</i>			
Newspaper	3.19	3.88	3.37
TV/Radio	3.07	3.35	2.78

*1-2 unimportant, 2-3 not very important, 3-4 important, 4-5 very important

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