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Human resources information in the Management Report of the top Spanish companies

Ainhoa Saitua-Iribar^a*, Lorea Andicoechea-Arondo^b, Eneka Albizu-Gallastegi^c

^aUniversity of the Basque Country (UPV/EHU), E.U. Relaciones Laborales; Sarriena s/n, 48940 Leioa, Spain

^bUniversity of the Basque Country (UPV/EHU), F. CCEEyEE Lehendakari; Agirre 83, 48015 Bilbao, Spain

^cUniversity of the Basque Country (UPV/EHU), E.U. Relaciones Laborales; Sarriena s/n, 48940 Leioa, Spain

Abstract

Since 2005 in Spain it has been mandatory to include information about human resources in the Management Reports, provided it is relevant to understanding business evolution. We study the human resources (HR) disclosure practices of the companies listed on the IBEX-35 for the period 2005-2009, using a structured content analysis which takes as a reference the *International Accounting Standards Board* (IASB) harmonization project. The overall result of this analysis is the poor quality of the information disclosed by the firms, in terms of relevance and comparability. In order to improve disclosure practices, both the Spanish authorities and those of other countries should recommend, if not require, the implementation of the *Practice Statement – Management Commentary* issued by the IASB in 2010, as well as the establishment of appropriate enforcement mechanisms.

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1. Introduction

The building of trust in financial markets is essential for any listed company in an increasingly globalised world. A key pillar of this confidence resides in the disclosure of adequate information to users and stakeholders. Consequently, the reliability of firms and their information transparency are taking on a growing importance. Specifically, the current context of crisis has sharpened the debate about the adequacy of the information disclosed by companies. Among other aspects, there is a questioning of the communication vehicles to be employed by companies when disclosing information, of the non-mandatory nature of the latter, and of the quantity and quality of the information disclosed. Among the possible means available, management reports are of vital importance for enabling investors and other users to form a substantiated opinion regarding company performance and business evolution (García, 2012).

Meanwhile, human resources constitute one of the main assets a company possesses and, as research into Strategic Management has shown, a source of competitive advantage for organizations (Hendry and Pettigrew, 1986; Wright and McMahan, 1992; Grant, 1995; Pfeffer, 1998). This is why firms include some information on the

* Corresponding Author: Ainhoa Saitua-Iribar. Tel.: +00-34-94-601-5859
E-mail address: ainhoa.saitua@ehu.es

situation and evolution of human capital in their annual reports, alongside financial information. The question this work attempts to address is whether companies are making an effort to improve the quality of the information they disclose on human resources in the Management Reports accompanying the financial statements.

This study aims to analyze the disclosure behavior of a sample of firms, which can be identified as leaders due to their greater visibility in the Spanish capital markets, using the requirements of national and international regulators as a benchmark. We use a structured content analysis of the Management Report, taking as a reference the IASB *Management Commentary* harmonization project. We focus on the quantity of references, the use of descriptive or quantified data, and the use of indicators.

This research is particularly timely, given that the International Integrated Reporting Council has issued its framework proposal for financial and non-financial information (IIRC, 2012), which includes social aspects, and for which the main Spanish association for accounting standards has proposed that this integrated report could form part of the Management Report within the current legislation context (AECA, 2012).

2. Background

2.1. Limits on the disclosure of narrative information

Despite the great importance of explaining the numbers in the financial statements published by companies (McCreevy, 2006), the disclosure of financial and non-financial narrative information presents several limitations. Some are associated with the excessive length of annual reports and their ever-increasing complexity, which may reduce comprehensibility (FRC, 2006), but most are connected with the kind of disclosure offered. On the one hand, there is a predominance of descriptive information, transmitting the impression that there is a lack of analytical discussion and forward-looking disclosure, as well as of non-financial indicators (Beattie, McInnes and Fearnley, 2002). On the other, there is an appreciable absence of balance/neutrality (Aerts, 1994). That is to say, there is a certain bias, because the annual reports are written so as to avoid criticism of current results, or to give an impression of gentle growth and steer clear of criticism over the following years (Metcalf, 2002). Furthermore, the managers try to obviate criticism of their performance and the actions of the business organization in general, in an attempt to preserve their legitimacy (Guthrie and Parker, 1989; Wilmshurst and Frost, 2000). The sum effect of all these limitations is that they contribute to reducing the usefulness of the information for users when they have to make their economic decisions.

2.2. Regulation on the Spanish Management Report

The *Informe de Gestión* (the Management Report in Spain) is a document that is presented along with financial statements, and places in context information related to business evolution as seen through management's eyes. It is generally known at an international level, but has not yet been sufficiently harmonized in terms of whether it is or is not mandatory, and of the rules or recommendations that guide its preparation. In Spain, it is compulsory for firms defined as big size to present a Management Report, but its content is not adequately regulated, so company practice does not match the expectations aroused (ICAC, 2002).

The main reference in international scene is the IASB project entitled *Management Commentary*. From it emerged a discussion document (IASB, 2005), a draft (IASB, 2009), and the final voluntary application guide (IASB, 2010). It constitutes a compulsory point of reference in Spain, in that when applying European decisions, listed groups have had to apply the international standards when drawing up their financial statements since the financial year of 2005. In its Conceptual Framework and norms for presenting Financial Statements, the IASB does not oblige directors to present the report, but proposes a guide based on principles for voluntary application, in such a way that the content to be disclosed is a matter for the company's discretion. This is how the international body seeks to improve the quality of the reports, encourage inter-company comparability and, as a final objective, improve its usefulness for users (IASB, 2010). However, it is questionable whether this has been achieved given that the guide is voluntary.

The discussion paper (IASB, 2005) proposed an approach based on the following principles: it would supplement and complement the Financial Statements; offer an analysis of the entity from the managerial viewpoint; and have a focus on the future. And it was specified that the information disclosed in a Management Commentary of quality should meet criteria of comprehensibility, relevance, balance, and comparability. Likewise, a list of recommended contents was put forward to guide what companies were to disclose, offering flexibility so that they might choose the content they deemed most relevant, and also the best manner of presenting it.

Finally, the existence of narratives as a response to an obligation to comply with a model, which are however comprised of boiler-plate phrases that offer no additional information, is a problem that has been highlighted in most researches (SEC, 2005; Aerts and Tarca, 2007; Brown and Tucker, 2011; Roulstone, 2011), regardless of the country under study, which means that it is still a long way to discover how to disclose good quality narrative information.

2.3. Disclosure about Human Resources

Human resources represent a valuable asset for organizations (Sierra and Moreno, 2000; Wyatt and Frick, 2010; Gamerschlag and Moller, 2011), so HR information is useful for users. Nonetheless, this asset is hard to measure and, without measuring it is difficult to manage properly (Martínez and Burgos, 2010). Information on HR is not properly disclosed in financial statements (Sonnier, Carsson and Carsson, 2007), but a generalized agreement has not yet been reached as to what constitutes the most suitable framework for disclosure (Sujan and Abeysekera, 2007; Giuliani and Marasca, 2011). The succession of different theoretical and methodological proposals expressed over recent decades, including Human Resources Accounting or Intellectual Capital (Martínez Ramos, 1998; Moneva, 1993; Sanz, 1994; Suárez, 1996; Camúñez, Sierra and Moreno, 2003), and the results of studies that have been carried out in different countries analyzing social information and employees (Bozzolan, O'Regan and Ricceri, 2006; Cooper, 2011), show that the devising of reports that provide HR information is yet an unresolved work area. Among other problems, the fact that today it is reported scattered throughout different documents (Villacorta, 2006) such as the Notes of the financial statements, the Management Report, or Social Responsibility Report, do not contribute to more useful information on HR.

In Spain, implementation of the modernization Directive 2003/51/EC through the law 62/2003, amended the contents of the Management Report accompanying the annual financial statements. The results was that, since 2005, the Management Report must contain, among other items, information about the company's human resources, providing it is relevant for understanding business evolution.

3. Method

3.1. Propositions development

Previous studies that have analyzed social information in annual reports in Spain (Pons, 1996; Carmona and Carrasco, 1998; Mazarracín, 1998; Archel, 2003; Aranguren and Ochoa, 2008; Aranguren, Ochoa and Ochoa, 2011) have obtained evidence that the information is poor, leading us to assume that HR information in Management Reports will generally be scarce in terms of quantity. And its quality may also be taken to be poor, because the information is essentially qualitative and historical.

The expected evolution due either to the influence of the regulation resulting from the implementation of the Law 62/2003, or to the time factor, due to the advance of the global harmonization process, are firstly that the volume of HR information (the number of observations) has increased, and, secondly, that its quality has improved. In other words, at the end of the period under analysis we expect the information to be more quantitative, in that it will include more quantification and a greater amount of indicators, and also more exploratory, with the incorporation of more forward-looking information, and more risk information.

3.2. The sample and data analyzed

In the present work we study the nature of HR disclosure practices in the Management Reports of the companies that formed part of the IBEX35 Spanish capitalization index over the period of 2005-2009 under study (23 firms). We consider their practices evolution attempting to shed light on their actual disclosure behavior, compared with what the regulators demand. The specific choice of the study period derives from the regulatory change following implementation in 2005 of the Law 62/2003 which request relevant information concerning personnel to be included in Management Reports from 2005 onwards. Moreover, since the Discussion Paper was published (IASB, 2005), we might expect leading companies in Spain to use it as a reference when preparing their Management Reports.

3.3. Methodology for developing the content analysis

Since Beattie et al. (2002) underscored the limitations of narrative analysis methodologies, some proposals, including those by Beretta and Bozzolan (2004), have incorporated specification of the semantic properties of each text unit, such as the economic sign, historical or forward-looking orientation, and type of financial/non-financial measure, etc. In our case, taking Saitua's proposal (2010) as a reference, we applied an information collection method based on the Discussion Paper-Management Commentary (IASB, 2005), which poses questions concerning the relevance and comparability of the information disclosed in each case. Specifically, we focused on the section in the IASB proposal that suggests that information should be provided on contents, such as the company's Key Resources, Risks and Relations. So, considering HR under Resources, we applied the questions that appear in the following table.

Table 1. Characteristics of the information disclosed

Relevance
Does the Management Commentary identify it as a key resource?
Does it discuss the appropriateness of the resource for meeting company objectives?
Does it explain how it is being managed?
Does it contain a management explanation as to how they aim to manage it?
Does it include an analysis of plans to tackle any deficiency or surplus of resources that is identified?
Comparability
Does it reflect changes in the content previously disclosed?
Does it explain the changes in the content previously disclosed?
Does it inform using non-financial or non-IFRS indicators?
Are the corresponding measures from the previous period disclosed?

And we applied a similar list of questions for cases where information is disclosed about human resources deemed to constitute a key risk or a key relation.

3.4. Results

In the period under review, the sample companies disclosed some human resources content in 10% of the report pages, but 13% of the companies do not disclose any data at all. In general, there is little quantification and use of indicators and in the whole sample analyzed we did not find a single observation considering personnel as a key relation. In addition, there is a lack of prospective data, while risk information is also scarce. In general, the amount of HR information is low and, although it increased during the period under review, it lost weight in the content of Management Report. Furthermore, the disclosure quality was shown to be poor, since the content is essentially qualitative and historical.

The propositions concerning the poor quantity and poor quality of HR information in the management reports of the IBEX-35 companies are thereby confirmed. The propositions regarding its evolution are, however, rejected because, in the whole set of companies analyzed, apart from the increase in information about personnel considered as a risk, no evidence is obtained either of an improvement in aspects with more quantification, or of a greater quantity of outlook information. So, we observe that the application of the Law 62/2003 *has* had an effect on company disclosure behavior, as the global quantity of HR information for the companies as a whole has increased and, in addition, the number of companies that disclose nothing has fallen. Nevertheless, our understanding is that the dissemination of the *Discussion Paper – Management Commentary* has not had a sufficient impact on the quality and evolution of the quality of information disclosed during the period analyzed.

4. Conclusion

Implementation of the Law 62/2003 has only resulted in an increase in the quantity of information about human resources in the sample of companies analyzed, but without impacting its quality, evaluated in terms of whether it meets the characteristics of relevance and comparability of the information disclosed. Therefore, in order to improve disclosure practices, particularly in human resources, both the Spanish authorities and those of other countries should recommend, if not require, the implementation of the *Practice Statement - Management Commentary* issued by the IASB in 2010, both for listed and unlisted companies, as well as the establishment of appropriate enforcement mechanisms.

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