Corporate Risk Reporting Practices in Annual Reports of Japanese Companies

Ali Md. Mohobbot
Graduate School of Humanities & Social Sciences
Okayama University, Japan

Abstract

This paper attempts to find out the corporate risk disclosure practices of Japanese companies. 90 non-financial companies have been selected randomly from companies enlisted with Tokyo Stock Exchange as the study sample. Their published annual reports have been used for content analysis. The findings show that in absence of any regulatory guidance Japanese companies are voluntarily reporting risk information in the annual reports. Study findings evidence that the company size and the number of risk disclosure are significantly positively correlated i.e., larger companies are disclosing more risk information than smaller companies which is consistent with the findings of previous studies. On the other hand, no significant relation exists between number of risk disclosure and level of risk, relative profitability, and ownership distribution pattern. The study also reveals that companies are used to disclose more past information and reluctant to disclose future risk information which is treated as more useful for the stakeholders for their economic decisions. In addition to that, most of the companies are disclosing descriptive risk information and are reluctant to quantify the risk either because of unavailability of reliable measurement tools or to avoid potential legal complicacies. Although companies are reporting risk information they do not disclose risk identification and measurement system they used. Furthermore, most of the companies do not disclose any information regarding risk prioritization.

1. Introduction

Corporate risk reporting is relatively a new issue and gaining popularity gradually. It is being talked during last few years. For better corporate governance, risk disclosure is very important both for the management and stakeholders of the company. Accordingly, to comply with the better corporate governance disclosure, companies are reporting about risk information voluntarily in annual reports. But, to some extent, these voluntary risk disclosures can not fulfill the demands of the users and therefore, stakeholders are not fully satisfied with the disclosed risk information. More often than not, companies do not provide clear and complete risk profile as there is nothing mandatory to do so. Even the mandatory risk reporting regulations always can not ensure full disclosure and enhanced quality (Woods and Reber, 2003). However, to minimize the level of information asymmetry proper risk disclosure is very important. Therefore risk reporting issue attracts attention to the concerned parties. It is a matter of general interest to know how companies are reporting the risk, how these risks are being identified and measured. To what extent risk information should be disclosed is also an issue of debate. As a result, different professional and regulatory bodies in different countries are concerned about this issue and issued various pronouncements to give clear guidelines. Such as, the Institute of Chartered Accountants of England and Wales (ICAEW, 1997, 1999, 2002), Canadian Institute of Chartered Accountants (CICA, 2002), American Accounting Association / Financial Accounting Standard Board (AAA/ FASB, 1997), and German Accounting Standard Board (GASB, 2001) are concerned in this regard. On the other hand, there are few academicians (for example, Linsley & Shrives, Hookana, Woods, Dowd, and Humphrey, Woods and Reber, Homolle, Dobler, Verrecchia) have also conducted research on this particular issue.

Gordon (1999) says that the world does not trust financial reporting by Japanese companies. How far this comment is trustworthy and evident that is different issue. But, a huge financial scandals and bankruptcies in the 1990s have undoubtedly influenced to come to this comment. Bad loan recovery is a much talked and badly needed issue in the Japanese economy. In response to various financial system weaknesses and pressures from outside community, the government eventually recognized the need for greater transparency in corporate financial reporting and for accounting practices closer to international standards. Consequently, the government announced details of an "Accounting Big Bang" between 1997 and 1999 that require massive reformation of financial reporting and accounting regulations. But traditionally Japanese companies have strong resistance towards

disclosure and inherently secretive and are unwilling to supply accounts to non-shareholders (Cooke, 1991, 1992). Jiang and Kim (2004) find that there is some sort of information asymmetry between firm (manager) and market (outside investors) and show that foreign (institutional) investors are attracted to Japanese firms with low information asymmetry. However, we do not have much study findings particularly about Japanese corporate risk disclosures. Although, The Financial Service Agency (FSA) is set to force listed firms to significantly expand the scope of information they disclose including potential risk factor in their securities reports starting from 2003 (Zaman, 2003). Till to date, no massive initiative has been taken in Japan for risk reporting in annual reports. On the other hand, some countries such as, the UK, Canada, and Germany are well advanced in this regard and have issued various pronouncements aiming at better reporting of risk[1]. But, it is assumed that Japanese companies are disclosing risk information in annual reports as they are to operate their business both in home and abroad. The study aims at finding out their risk reporting status. To be more specific, this study will try to find out the extent of company risk disclosure. It also attempts to find the pattern of risk disclosure e.g. what is the relationship (if any) between number of risk disclosure and corporate characteristics. Corporate characteristics include size, profitability, and level of risk of the company and so on. The study will also reveal the relation between monetary risk disclosure and non-monetary risk disclosure, past and future risk disclosure and the relationship between/among good, bad and neutral risk disclosures. Other objectives include (i) how the Japanese companies identify risk, (ii) how they classify them, (iii) how they prioritize them, (iv) whether they measure risk or not and so on.

This study proceeds as follows. Section 2 presents existing literature, section 3 presents hypotheses of the study followed by methodology in section 4. Section 5 and 6 present the results and discussions and conclusions respectively.

2. Literature review

2.1 Institutional Literature

In fact, a very few empirical studies have been done by academic researchers on this particular issue. Most of the literatures come from various regulatory / professional bodies e.g. ICAEW (1997, 19999, 2002), CICA (2002), AAA/FASB (1997), GASB (2001) and so on. Other than GASB all the above bodies suggest to disclose risk information voluntarily. GASB issued a standard making risk disclosure mandatory. In fact, risk disclosure debate has been brought into spotlight by ICAEW through a discussion paper "Financial Reporting of Risk ? Proposals for a Statement of Business Risk" in 1997. Although, ICAEW has published

several subsequent papers on this issue the first proposal has the exceptional importance as it brings risk reporting idea in the light for the first time. According to this proposal, companies with publicly traded shares should lead the introduction of enhanced risk reporting in annual reports. Enhanced information about what companies do to assess and manage key business risks of all types will provide practical forward-looking information ; reduce the cost of capital ; encourage better risk management ; help to ensure the equal treatment of all investors ; and improve accountability for stewardship, investor protection and the usefulness of financial reporting. Accordance with GAS 5, a risk which threatens the existence of the group should be clearly described and individual risks should be classified in a suitable manner into risk categories. The information provided on risk should be self-contained which means that the risk and the consequences should be disclosed. It also includes that risk should be quantified where this can be done with reliable and recognized methods, where it is economically justifiable and where quantification could affect the decisions of the users of the group management report. In this case, the models and assumptions used should be described. As a general rule, disclosures about risk should be made after taking account of risk reduction techniques to mitigate the effects of risks. If these techniques cannot compensate for the effects of risk with certainty, the disclosures should be made before taking account of such techniques. It also requires that an appropriate description of the risk management system is provided, including a description of the policies, procedures and organization of the risk management system. CICA also mentions that a company should disclose its principal risks and describe related risk management systems to enable readers to understand and evaluate the company's risks and its decisions regarding the management of such risks. Such disclosure should include : the principal risks and uncertaintieSFACing the company and its core businesses and segments, as appropriate ; the strategies and processes employed for managing these risks ; and the potential specific impact of these risks on results and capabilities, including capital resources and liability (CICA, 2002). Therefore, literature from different regulatory bodies implies that in principle, there is no basic difference among the guidelines. All of them advise to disclose principal / material risk information along with consequences of the risk and the methods of risk measurement and identification.

2.2 Literature from Academic Researchers

Academic researchers also have conducted research studies in this arena e.g., Linsley et al. (2000, 2002-04), Hookana (2003), Homolle (2003) and so on. Linsley et al. find that big firms disclose more

risk information than small firms and there is no relation between the level of risk and the number of disclosure. They also find that there is no relationship between the average profitability and the number of risk disclosure. They show that directors are reluctant to quantify the risk ; rather they are more willing to disclose non-monetary risk information. Hookana (2003) sees the nature and influence of institutional environment on the formation of the current practices and problems relating to risk identification and measurement. Woods et al. (2004) criticize the risk measurement system particularly VaR. They mention that institutions will typically be reluctant to reveal more than their peers, as risk information is commercially sensitive by its definition and which lead to make the risk reporting as 'boiler plate'. Ali and Konishi (2005) mention that the existing disclosure requirements are not sufficient for proper risk disclosure and it has been felt that there should have some other guidelines for reporting company risk information. Dobler (2005) advises caution not to overestimate the information content of risk reports. He mentions uncertainty of managerial information availability and verifiability is a problem of risk reporting. Even with regulatory action this problem can not be removed fully. Homolle (2003) also says that risk report does not generally lead to a decrease in bank's risk exposure. In stead it induces higher insolvency risk under certain conditions.

It is noteworthy to mention that most of the studies were conducted on the UK, Germany and Canadian companies possibly as because they are well advanced in this regard. There are some researchers notably, Cooke (1991, 1992) and Choi et al (1999), Singleton and Globerman (2005) who have carried out some researches focusing on financial disclosure of Japan. But no research study has been undertaken specifically on risk disclosure issue about Japanese companies. This dearth in this area motivates the author to reveal the situation in Japanese companies.

3. Hypotheses of the Study[2] :

3.1 Risk disclosure and size of the company

Various general disclosures related studies reveal that there is a positive relation with company size and number of disclosure (e.g. Adams et al., 1998, Marston & Shrives, 1991). These studies do not focus on the risk disclosure issue ; rather these are on general disclosure. Linsley and Shrives (2003) show particularly that there is a positive association between company size and the total number of risk disclosure. They also find the existence of positive association between company size and number of financial risk and non-financial risk disclosure. Their study is particularly on the UK

companies after issuance of risk reporting guidelines by the ICAEW. On the other hand, Japanese companies may have different patterns of disclosure as they have to operate in a separate environment so called secretive environment (Cooke 1991, 1992) and do not have any regulatory guidelines in this regard. In addition to that, most of the sample companies having international business should have more or less same risk disclosure pattern irrespective of their origin. Therefore this study also will test the same set of hypothesis whether results confirm the earlier results.

Hypothesis 1(*a*) : There will be a positive association between company size and the total number of risk disclosures.

Hypothesis 1(*b*) : There will be a positive association between company size and the total number of financial risk disclosures.

Hypothesis 1(*c*) : There will be a positive association between company size and the total number of non-financial risk disclosures.

3.2 Risk disclosure and the level of company risk

It could be postulated that companies with higher levels of risk will disclose greater amounts of risk information as the directors need to explain the cause of this risk. On the other hand, companies could have strong incentive to disclose in details to the stakeholders how they are actively managing the risk and this would also result in higher levels of disclosure. Therefore there should be a positive association between risk disclosure and level of risk. In contrast, there could be another argument that companies with higher levels of risk may also feel that they do not want to draw attention to their 'riskiness' and therefore they may show a reluctance to disclose significant amounts of risk information voluntarily. On the other hand, companies with lower level of risk may wish to publicly declare that this is so, possibly directors wanting to signal that this has arisen from their better risk management abilities.

A circular relationship between risk levels and risk disclosure may also exist. The ICAEW, amongst others, argue that companies that disclose more risk information will find an image in the market place that they are less risky than before. Therefore, increased risk disclosure could impact upon the company risk level, although to what extent is unknown.

Because the nature of the relationship between the volume of risk disclosures and risk levels is indeterminate the author therefore presents the hypotheses in a null form :

Hypothesis 2(*a*) : There is no association between the level of

risk within a company and the total number of risk disclosures.

Hypothesis 2(*b*) : There is no association between the level of risk within a company and the total number of financial risk disclosures.

Hypothesis 2(*c*) : There is no association between the level of risk within a company and the total number of non-financial risk disclosures.

3.3 Risk disclosure and profitability

It is being argued that those companies that are better at risk management will have higher levels of relative profitability and they will then want to signal their superior risk management abilities to the market place via disclosures in the annual report (Linsley et al., 2003). Disclosing more risk information, management not only to show their risk management efficiency but also to show their transparent attitude to the stakeholders using this opportunity. Although it is very difficult to know the actual attitude of the management at a comfortable profit position of the company. Whatever may be the actual intention of disclosing risk information, it seems that there is a relation between the profitability and number of risk disclosures. Therefore the hypothesis is :

Hypothesis 3 : There will be a positive relationship between the relative profitability of the company and the total quantity of risk disclosure.

3.4 Risk disclosure and ownership distribution pattern

It is thought that if majority or a large number of shares of a company is owned and controlled by a few persons, risk disclosure pattern would be different than a firm having evenly distributed ownership. If a very few people control the majority shares then most of the risk information will be disclosed at the board room meeting or with analysts as the most interest lies with them. General stakeholders, who are not holding a substantial amount of share, somehow will not get material risk information through annual reports. From the arguments, we can postulate that there is a negative relationship exists between the level of shareholdings of top few shareholders and the level of risk disclosure. On the contrary, if the number of individual shareholders and foreign shareholders is high the pressure mounts to the directors to disclose more risk information. Institutional isomorphism particularly, coercive isomorphism theory may work in this regard. And therefore the relationship between level of individual and foreign shareholdings and risk disclosure will be positive.

Therefore the hypotheses will be :

Hypothesis 4(*a*) : There will be a negative relationship between the level of shareholdings of top few shareholders and level of risk disclosure.

Hypothesis 4(*b*) : There will be a positive relationship between the level of shareholdings by individuals and level of risk disclosure through annual reports.

Hypothesis 4(*c*) : There will be a positive relationship between the level of shareholdings by foreign shareholders and level of risk disclosure through annual reports.[3)]

3.5 Monetary and non-monetary risk disclosure

The ICAEW (1999) advises to quantify the size of a risk whenever possible to improve the quality of risk reporting. Placing of a monetary value upon a risk enables reader to better assess the potential consequences of risk to the company and therefore the consequences to the reader are easier to assess. There are, however, two difficulties associated with the quantification of risk. First, not all risks are susceptible to measurement. There are well-tried techniques for measuring for example, market risks using value at risk methodologies, but these techniques can only be used in certain circumstances. That a large number of risks are difficult to measure leads on to the second problem. A company may do its best to estimate the size of a future risk but the eventual outcome may be quite different to this original estimate. Therefore directors will be very reluctant to attempt to quantify the size of risks as this can leave them open to severe criticism, and potential legal actions from investors who can claim that they have suffered financially, in the future once the actual impact becomes known. Consequently one would expect risk disclosures to be described and discussed, but with infrequent disclosure of risk information that has a monetary value attached. Therefore the hypothesis is :

Hypothesis 5 : The number of non-monetary risk disclosures will be significantly greater than the number of monetary risk disclosures.

3.6 Past and future risk disclosure

The fundamental problem associated with the disclosure of future risk information being that it is inherently uncertain information. Thus, whilst future information is more useful than past information, it is likely that directors will be as reluctant to disclose future risk information as they would monetarily-quantified risk information. The directors will not

want to be held responsible for the decisions stakeholders take based upon the disclosures. Therefore the hypothesis is :

Hypothesis 6 : The number of past risk disclosures will be significantly greater than the number of future risk disclosures.

3.7 Good, bad and neutral risk disclosure

This hypothesis tests whether there are differences in the numbers of risk disclosures in terms of the nature of the 'news' they disclose. That is, is good news or bad news being disclosed or is the information 'neutral' ? Although, prima facie, it could be argued that companies may prefer not to disclose bad news, this will not always translate into their withholding that bad news. The bad news may need to be disclosed if the financial results are such that had the directors omitted an explanation for the results this would merely arouse suspicions and potentially damage their reputations to a greater extent than if the information had been disclosed. The directors may also wish to disclose the bad news if they can attribute this to external factors and therefore deflect blame away from their own management actions and abilities. Attribution theory would support this suggestion that managers wish to attribute bad news to factors that are outside their control or influence. Directors could also be prepared to release bad news into the public domain via annual report if they want to pre-warn of possible difficulties in the future. Therefore there are a number of reasons why bad news will be disclosed.

An annual report that focused predominantly upon bad news would be poor publicity for the directors and therefore they would, presumably, seek to introduce good news also. The type of good risk news that may be disclosed could be discussions of opportunities that the company can exploit or explanations of how a risk has been actively and successfully managed. The amounts of good, bad or neutral news that will be disclosed will presumably be variable however, as it will be dependent upon how much of each category of news exists at the time of preparing the annual report and how much is withheld from the annual report, for example for commercial reasons. As because it is not possible to pre-determine the disclosure patterns of good, bad and neutral news the last hypothesis is :

Hypothesis 7 : The number of good, bad and neutral risk disclosures will not be significantly different from one another.

4. Methodology of the study

4.1 Sample selection

The sample has been selected randomly from the listed companies enlisted with

Tokyo Stock Exchange. About400 companies have been contacted and requested for their annual reports. After receiving the response, 90 non-financial companies were found suitable for the study. Financial companies were not being considered as they are to report some information according to their special nature. The annual reports were selected to form the basis for content analysis with a year-end date nearest to 31st March 2003. Table 1 shows the list of the sample companies.

4.2 Content analysis

Content analyses of the annual reports have been performed to find out the concerned issues. Linsley and Shrives have also used the same technique for various studies. The author himself did the coding job and analyzed based on the decision rule applied by the Linsley and Shrives (appendix A). The researcher has also used the sentences as unit of the analysis as it was supported by the Milne and Adler (1999) saying that they are "far more reliable than any other unit of analysis." The sentence coding was performed according to the grid used by Linsley and Shrive (appendix B) with a little modification about the categories of risk. There are five categories of risk disclosure (appendix C) were used for this study. This risk category has been taken from the Turnbull's report suggested by ICAEW with a minor modification.

4.3 Measurement of variables

Total turnover and total asset have been selected as the proxy variables for size of the firm. For measuring the level of risk, it can be done in various ways like, gearing ratio, beta factor, book to market value and so on. But, it is very tough to justify favoring one method than another to use (Linsley and Shrives, 2002). However, for this study we have decided to use market to book ratio (MBR) and gearing ratio as the risk proxy variables. Fama and French (1992) study advocates the use of book to market value ratio as the appropriate proxy of risk. The year end figure has been considered for calculation of gearing ratio and book to market value ratio. On the other hand, Return on asset (ROA) and Return on equity (ROE) have been selected as the proxy variables for relative profitability of the sample companies. For analyzing the relationship between ownership distribution and risk disclosure, shares held by top 10 shareholders and holdings of individuals and foreign shareholders have been taken as proxies which have been collected from the annual reports on the year end date.

Pearson's correlation co-efficient have also been calculated using SPSS for testing first four sets of hypotheses. To test rest of the hypotheses Wilcoxon Rank-Sum Test (same as Mann-Whitney test) has been performed. By drawing histogram of the data it is found that sample data is not normally distributed and therefore Wilcoxon Sign Rank test could

not be performed.

5. Results and discussion

5.1 Descriptive statistics

The results of the descriptive statistics

Table 2: Descriptive Statistics

	Minimum	Maximum	Mean	Std. Deviation
Nat log of assets	23.7426	29.9514	26.8703	1.4215
Nat log turnover	23.8128	29.9787	26.7701	1.4515
ROA	-8.6	13.19	1.469	3.4608
ROE	-152.91	72.8	2.162	20.2453
Market to book value ratio	0.0019	18.999	2.0404	2.205
Gearing ratio	2.0795	1916.469	133.9689	253.8043
Top 10 shareholder's holdings	19.8	74.49	42.9361	11.3972
Holdings of Individuals and Foreigners	15.2	63.45	39.171	9.7639
Total number of risk disclosure	5	143	51.6	27.311
Total number of financial risk disclosure	0	41	8.03	6.602
Total number of non-financial risk disclosure	4	121	43.57	22.791
Total number of monetary risk disclosure	4	81	19.97	13.012
Total number of non-monetary risk disclosure	0	102	31.63	18.565
Total number of past disclosure	5	125	38.53	21.784
Total number of future disclosure	0	82	13.07	11.742
Total number of good news disclosure	0	95	22.29	15.865
Total number of bad news disclosure	0	61	14.28	9.831
Total number of neutral news disclosure	0	70	15.03	10.485

Table 3: Pearson Correlation Co-efficient for variables

VARIABLES	TOTAL NUMBER OF RISK DISCLOSURES		TOTAL NUMBER OF FINANCIAL RISK DISCLOSURES		TOTAL NUMBER OF NON-FINANCIALRISK DISCLOSURES	
	Pearson correlation	Sig. (2 tailed) for Pearson	Pearson correlation	Sig. (2 tailed) for Pearson	Pearson correlation	Sig. (2 tailed) for Pearson
Nat log of assets	0.261*	0.013	0.275*	0.009	0.233*	0.027
Nat log of turnover	0.290**	0.006	0.308**	0.003	0.258*	0.014

* Correlation is significant at the 0.05 level (2-tailed).

** Correlation is significant at the 0.01 level (2-tailed).

are shown in the table 2. For the purpose of smooth statistical calculation two variables named total turnover and total assets have been converted into their natural logarithm. Table shows that total number of risk disclosures varies ranging from 5 to 138 with an average 51.60. The average number of financial and non-financial risk disclosures is 8.03 and 43.57 respectively. From the table, we also can see that some companies do not disclose some risk categories at all such as financial risk, future risk information, good risk information and so on having zero as their minimum number.

5.2 Testing the hypotheses

Table 3 shows that both proxy variables for the size of the company, natural log of the assets and natural log of the turnover, are significantly correlated with the number of total risk disclosures, number of financial risk disclosures, and the number of non-financial risk disclosures. The results confirm that there is a positive relation between company size and level of risk disclosure. More specifically, it shows a positive relation between company size and total number of risk disclosures (at the 5% level of significance for total assets and at the 1% level of significance for turnover) ; a positive association between company size and total number financial risk disclosures (at the 5% level of significance for total assets and at the 1% level of significance for turnover) ; and a positive correlation between company size and total number of non-financial risk disclosure (at the 5% level of significance for both total assets and turnover).

Table 4 shows that there is no significant relation exists between the level of risk and number of total risk disclosures. For both the risk proxies, there is no significant relation between level of

Table 4 : Pearson Correlation Co-efficient for variables

VARIABLES	TOTAL NUMBER OF RISK DISCLOSURES		TOTAL NUMBER OF FINANCIAL RISK DISCLOSURES		TOTAL NUMBER OF NON-FINANCIALRISK DISCLOSURES	
	Pearson correlation	Sig. (2 tailed) for Pearson	Pearson correlation	Sig. (2 tailed) for Pearson	Pearson correlation	Sig. (2 tailed) for Pearson
MBR	-0.109	0.305	-0.114	0.283	-0.098	0.359
Gearing ratio	0.046	0.665	0.027	0.802	0.048	0.656

Table 5 : Pearson Correlation Co-efficient for variables

VARIABLE	TOTAL NUMBER OF RISK DISCLOSURES	
	Pearson correlation	Sig. (2 tailed) for Pearson
ROA	0.062	0.563
ROE	0.101	0.345

Table 6 : Pearson Correlation Co-efficient for variables

VARIABLE	TOTAL NUMBER OF RISK DISCLOSURES	
	Pearson correlation	Sig. (2 tailed) for Pearson
Top 10 shareholder's holding	-0.122	0.563
Shareholding by Individuals	-0.122	0.761
Shareholding by Foreign shareholders	0.073	0.495

risk and the level of risk disclosures irrespective of financial and non-financial or total risk.

The above table 5 shows that the correlation between relative profitability and total number of risk disclosures is not significant for both the variables of ROA and ROE.

According to the table 6, the Pearson's correlation coefficient for top 10 shareholders and risk disclosure is -0.122 and correlation coefficient for individual shareholdings and foreign shareholdings are -0.032 and 0.073 respectively. These correlations indicate that distribution pattern of shareholdings and number of risk disclosure is not significantly correlated.

The Wilcoxon sum rank test results are stated in table 7. According to the result, it is evident that number of non-monetary risk disclosures is significantly higher than monetary risk disclosures. Test statistics also supports the significant difference between monetary and non-monetary as the Z score -5.511 and P (Sig 2 tailed) value is 0.000.

Table-7 also supports the hypothesis 6 that the number of past risk information is significantly higher than future risk disclosure. The significance value of 0.000 having Z score of -9.586 clearly evidences that past risk disclosures are higher than future risk disclosures. In addition to that researcher has excluded the risk category F which is being regarded as less useful disclosure for testing the relationship between past and future risk disclosures. The result shows that most of the companies are disclosing past risk information than future risk information.

Test results regarding the relationship of good, bad, and neutral disclosures shows that the number of good disclosures is significantly higher than that of bad and neutral disclosures at a 0.000 level of significance. The result also shows that there is no significant difference between the number of bad and neutral disclosures as P value shows 0.670 having Z score -0.425.

5.3 Discussion of the results

The results of the study reveal that

Table-7 : Wilcoxon Rank Sum test (Mann-Whitney Test)

Ranks

		N	Mean Rank	Sum of Ranks
Monetary-Non-monetary	1	90	69.11	6219.50
	2	90	118.89	10070.50
	Total	180		
Past - Future	3	90	127.69	11492.00
	4	90	53.31	4798.00
	Total	180		
Past-Future excluding F	3	90	133.99	12059.00
	5	90	47.01	4231.00
	Total	180		
Good-Bad	6	90	107.58	9682.50
	7	90	73.42	6607.50
	Total	180		
Good-Neutral	6	90	106.58	9592.50
	8	90	74.42	6697.50
	Total	180		
Bad-Neutral	7	90	88.85	7996.50
	8	90	92.15	8293.50
	Total	180		

Test Statistics

	Monetary-Non-monetary	Past-Future	Past-Future excluding F	Good-Bad	Good-Neutral	Bad-Neutral
Mann-Whitney U	2124.500	703.000	136.000	2512.500	2602.500	3901.500
Wilcoxon W	6219.500	4798.000	4231.000	6607.500	6697.500	7996.500
Z	-5.511	-9.586	-11.243	-4.402	-4.145	-.425
Asymp. Sig. (2-tailed)	.000	.000	.000	.000	.000	.670

Japanese companies are voluntarily disclosing risk information. The statistical mean numbers of various kinds of risks disclosures may relatively be lower if they are compared with other countries having some kind of risk disclosure guidelines.

The results in the table-3 show that size of the company and number of risk disclosure is significantly correlated which is consistent with the findings of Linsley and Shrives (2002) in the UK. Their study was conducted after issuance of the ICAEW's risk reporting proposals to disclose more risk information. This result also helps to come to a conclusion that the relationship between number of risk disclosures and company size is not much influenced by the introduction of risk reporting guidelines. Non-risk disclosure study also shows the existence of this kind

of relation between size of the company and volume of disclosures (Adam et al., 1998 in Linsley and Shrives, 2002). So, irrespective of the financial and non-financial risk information, large companies are reporting more risk information than that of smaller one.

Table-4 shows that the correlation between level of risk and number of risk disclosures is insignificant. These findings also support the previous findings of Linsley and Shrives (2002).

The results also show that there is no significant relation exists between number of risk disclosure and level of relative profitability of the sample companies (Table-5). The results are also consistent with the findings of Linsley and Shrives (2003). It does not support the argument that a firm having better risk management capability earns relatively higher profit and wants to signal to the concerned party about their superiority. In addition to that management would prefer to show their sincerity regarding stewardship function to the stakeholders. But, it might be the reason that because of proprietary cost and other sensitive internal reasons company is not disclosing full risk picture.

There is no significant relation between the ownership distribution pattern and the number of risk disclosures is found by the study (table-6). Although, this issue may have some credence as because, release of any risk information can not be done without the involvement of the board or the management. If the board members hold the majority shares / or a significant portion of total shares, they may have some influence on the disclosures of risk information.

Table-7 shows that number of monetary risk disclosure is significantly lower than that of non-monetary risk disclosure which shows that most of the sample companies are not interested to quantify the risk. These results also confirm the findings of Linsley and Shrives (2003). Always all kinds of risk can not be measured accurately with the existing techniques and the possible risk of legal actions from investors may possibly be the reasons behind of it. Another result in the table-7 shows that good news is significantly higher than bad and neutral news. It implies that management is pretty interested to signal about their capabilities and efficiency of managing the company. On the other hand, it is very positive aspect of reporting that they are not merely for boiler plate reporting as the number of neutral disclosure is lower than that of good disclosure. This finding has partial disagreement with the findings of Linsley and Shrives (2002).

Table-7 sows that future risk information is significantly lower than past risk information. This finding conflicts the result of Linsley and Shrives (2003). The findings help to support the argument that managements are very reluctant to disclose future risk information as this can not be done objectively. The descrip-

Table 8 : Medium of reporting risk information

	Number	Percentage
OFR	43	48 %
MD&A	35	39 %
President's Message	9	10 %
Informal and others	3	3 %
Total	90	100 %

tive statistics also supports the test result as the mean number of past disclosures 38.53 is significantly higher than that of future risk disclosures 13.07.

In addition to the test results, author has some observations regarding risk related practice of the sample companies. Companies are lacking of standard risk identification and measuring system, risk management policy and so on. Author find that there are some companies which are disclosing very negligible risk information not even keeping in mind to do so ; rather they are disclosing those risk information as part of their regular financial disclosure. Since they do not have any policy to report about risk state, they are not doing so in a sophisticated way. But one of the interesting findings of the study is most of the companies are reporting through either Operating and Financial Review (OFR) or Management Discussion and Analysis (MD&A) which have been recommended as the medium of reporting risk information in UK and Canada respectively.

Table 8 evidences that 48% sample companies are reporting through OFR and 39% disclose their information through MD&A. Some companies are disclosing risk information through the president's message and other informal ways. Only 3% of the companies are using separate risk related section for disclosing risk information.

But the frustrating observation is that all most all the companies do not disclose any information about the nature of the risk whether it is material or immaterial. They do not disclose any information regarding the identification and measurement system if any they use. They do not mention about specific effects of any risk to the company other than some financial risk information. As per the observation, only 3 companies out of 90 sample companies are using separate section for risk related issue. It indicates that companies which are using MD&A as the medium are not well aware of proper use of MD&A.

6. Conclusions

Undoubtedly risk reporting is an emerging issue. It is assumed that risk reporting will provide users with more fair and true view of the business. Scandal like Enron

put more emphasis on the disclosure of risk information. So, it is getting growing interest all over the world. Results help to conclude that the company size and the number of risk disclosure are correlated.

On the other hand results show that no association was found between level of risk and the number of risk disclosure, profitability and level of disclosure, and ownership distribution pattern and number of risk disclosure. It also shows that companies are reluctant to quantify the risk as the non-monetary information is significantly higher than monetary information. The study reveals about the medium used by Japanese companies for risk disclosure in the annual reports. 48% companies are using OFR and 39% using MD&A as reporting place in the annual reports. Only 3 companies disclosed risk information in a separate section for risk in the annual reports. But one thing is important to mention that without any regulatory framework companies are reporting risk information voluntarily. Although the future risk information which is also treated as more useful information is significantly lower than the past information, but authors believe that regulatory framework could do help in this regard. Although regulatory framework can not guarantee the quality of the reporting it can help the reporting to be consistent and comparable. Since the human beings are involved within the risk reporting process, motivation is also important with the regulation. To have more details about the risk reporting pattern it needs more intensive research. Particularly it will be interesting to study whether there is any cultural influence on risk reporting in Japanese companies. It also needs attention to study the relation if any between Japanese management style and risk reporting.

Notes

1) For risk reporting about America, please see Kazuyuki Suda et al. (2004) "Disclosure Strategy and its Effect". pp. 151-168. Moriyama.
2) Author gratefully acknowledges the adoption of hypotheses from Linsley and Shrives tested on UK and Canada.
3) I acknowledge the advice of Prof Kazuyuki Suda for separating Individual shareholdings from shareholdings of Foreigners.

References :

Adams, C. A., Hill, W. and Roberts, C. B. (1998). Corporate Social Reporting Practices in Western Europe : Legitimating Corporate Behavior ? British Accounting Review 30, 1-21.

Ali, M. M. and Konishi, N. (2005). The UK Guidelines for Company Risk Reporting ? An Evaluation. Okayama Economic Review, Vol. 37, No. 1, 1-18.

ASB, Accounting Standard Board. (1993). New Operating and Financial Review. ASB, UK

Choi, F. D. S., Frost, C. and Meek, G. (1999). International Accounting 3rd ed. Englewood Cliffs. Prentice Hall.

CICA, Canadian Institute of Chartered Accountants (2002). Management's Discussion and Analysis ? Guidance on Preparation and Disclosure. Ontario, Canada.

Cooke, T. E. (1991). An Assessment of Voluntary Disclosure in the Annual Reports of Japanese Corporations. International Journal of

Accounting. Vol. 26, No. 3, 174-189.
Cooke, T. E. (1992). The Impact of Size, Stock Market Listing and Industry Type on Disclosure in the Annual Reports of Japanese Listed Corporations. Accounting and Business Research. Vol. 22, No. 87, 229-237.
Dobler, Michale (2005). How informative is Risk Reporting? A Review of Disclosure Models. Working paper.
Fama, E. F. and French, K. R. (1992). The Cross-Section of Expected Stock Returns. The Journal of Finance. Vol. 47. No. 2. 427-465.
GASB, German Accounting Standard Board (2001). Risk reporting, GAS 5, Berlin, Germany.
Gordon, W. D. (1999). A Critical Evaluation of Japanese Accounting Changes since 1997. An MA dissertation. University of Sheffield, UK.
Homolle, Susanne (2003). Risk Reporting and Bank Runs. Working paper.
Hookana, Heli (2003). The Revelation of Financial Risk Disclosure: To Whom? By Whom? How? Why? Working paper. Turku School of Business and Administration, Finland.
ICAEW, The Institute of Chartered Accountants in England and Wales (1997). Financial Reporting of Risk: Proposals for a Statement of Business Risk, ICAEW, London.
ICAEW, The Institute of Chartered Accountants in England and Wales (1999a). Implementing Turnbull: A Boardroom Briefing. ICAEW, London, UK.
ICAEW, The Institute of Chartered Accountants in England and Wales (1999b). No Surprises: The Case for Better Risk Reporting, ICAEW, London.
ICAEW, The Institute of Chartered Accountants in England and Wales (2002). No Surprises: Working for better risk reporting. ICAEW, London.
ICAS (1997). Institute of Chartered Accountants of Scotland. Corporate Communication with Institutional Shareholders: Private Disclosures and Financial Reporting. Scotland.
Linsley, P. M. and Shrives, P. J. (2002). Risk Disclosure in the Corporate Annual Reports of UK Companies. Working paper.
Linsley, P. M. and Shrives, P. J. (2004). Risk Reporting: Finding a way forward through the boilerplate towards better risk reporting. Working paper.
Linsley, P. M., Shrives, P. J., and Crumpton, Mandy. (2003). Risk Disclosure Practices: A Study of UK and Canadian banks. Working paper.
Marston, C. L. and Shrives, P. J. (1991). The Use of Disclosure Indices in Accounting Research: A review Article, British Accounting Review. Vol. 25, 195-210.
Milne, M. J. and Adler, R. W. (1999). Exploring the reliability of social and environmental disclosures content analysis. Accounting, Auditing and Accountability Journal. Vol. 12. No. 2. 237-256.
Shrives, P. J. and Linsley, P. M (2003). Risk Reporting by UK and German Companies: Towards Meaningful Disclosure? Working paper.
Singleton, W. R. and Globerman, S. (2005). The Changing Nature of Financial Disclosure in Japan. Working Paper. Western Washington University, Bettingham, WA.
Verrecchia, R. E. (2004). Policy Implications from the Theory-Based Literature on Disclosure. The Economics and Politics of Accounting, 149-163 (Oxford et al.: Oxford University Press).
Woods, M and Reber, B. (2003). A comparison of UK and German Reporting Practice in respect of Risk Disclosure post GAS 5. Working paper.
Woods, M., Dowd, Kevi., and Humphrey, C. G. (2004). Credibility at Risk? The Accounting Profession, Risk Reporting and The Rise of VaR. CRIS Discussion Paper Series? 2004. III.
Zaman, Arif. (2003). Made in Japan? Converging Trend in Corporate Responsibility and Corporate Governance. Research Report of Royal Institute of International Affairs, UK, 2003.

Appendix A

Decision rules for risk disclosures

- All disclosures must be specifically stated, they cannot be implied.
- If a sentence has more than one possible classification, the information will be classified into the category that is most emphasized within the sentence.
- Tables (quantitative and qualitative) that provide risk information should be interpreted as one line equals one sentence and classified accordingly.
- Any disclosure that is repeated shall be recorded as a risk disclosure sentence each time it is discussed.
- If a disclosure is too vague in its reference to risk then it shall not be recorded as a risk disclosure.

Appendix B

Disclosure coding grid

	Category	Financial Risk	Buisiness Risk	Operational and other risk	Compliance risk	Information Processing and Technology Risk
Text Disclosures Sentence Characteristics		1	2	3	4	6
Monetary/good news/future	A					
Monetary/bad news/future	B					
Monetary/neutral/future	C					
Non-monetary/good news/future	D					
Non-monetary/ bad news/future	E					
Non-monetary/neutral/future	F					
Monetary/good news/past	G					
Monetary/bad news/past	H					
Monetary/neutral/past	I					
Non-monetary/good news/past	J					
Non-monetary/ bad news/past	K					
Non-monetary/neutral/past	L					

Appendix C

Risk Disclosure Categories

Financial risk	Interest rate Exchange rate Liquidity brisk Credit risk Market risk Treasury risk Going concern problems Breakdown of accounting system and unreliable records High cost of capital

Business Risk	Wrong business strategy Competitive Pressure on price / market share General economic problem Regional economic problem Political risk Obsolescence of technology Adverse government policy Industry sector in decline Substitute products Take ?over target Inability to obtain further capital Bad acquisition Too slow to innovate
Operational and other risk	Customer satiSFACtion Product / project development Sourcing Efficiency and performance Business processes not aligned to strategic goals Failure of major change initiatives Loss of entrepreneurial spirit Stock-out of raw materials Skills shortage Physical disasters（fire and explosion） Loss of physical assets Failure to create and exploit intangible assets Loss of intangible assets Lack of orders Loss of key people Breach of confidentiality Health and safety Brand name erosion Ineffective and inefficient management process Other business honesty issues Missed business opportunities Lack of employee motivation
Compliance	Breach of Listing Rules Breach of financial regulations Breach of Companies Act requirements Litigation risk Breach of other regulations and laws VAT and Tax problems Health and safety Environmental problems
Information processing and technology risk	Integrity Access Availability Infrastructure Y２K others

Table 1: List of the sample companies

Aichi Steel
Aisin Seiki Co. Ltd
Ajinomoto Co.
Akebono break industries
All Nippon Airways Co. Ltd.
Alpine Electronics Inc.
Alps Electric Co Ltd.
Amano corporation
Anest Iwata Corp
Anritsu Corporation
ARGO 21 Corp
Asahi Breweries Co. Ltd.
Asahi Kasei Corp
Bridgestone Corporation
Casio Computers Ltd.
Chiyoda Corporation
Chugai Pharmaceuticals co. ltd.
Chugai Ro. Co. Ltd.
chugoku electric power co. ltd.
Citizen Watch Co. Ltd.
Cosmo Oil Co.Ltd.
Dai Nippon Printing Co. Ltd.
Daido Steel Co. Ltd.
Daihatsu Motors co. ltd.
Daiichi Jitsugyo Co. Ltd.
Daiichi Pharmaceutical co. ltd
Daimei Telecom Eng Corp
Dainippon Ink and Chemicals Inc.
Dainippon Screen Mfg. Co. Ltd.
Daiwa House Ind. Co. Ltd.
Daiwabo Information System Co.
ESPEC Corporation
Fuji Electric Co Ltd.
Fuji Oil Co. Ltd.
Hitachi Cable Ltd.
Hitachi Ltd.
Hitachi Metals Ltd.
Horiba Ltd.
Inabata & Co. Ltd.
Itochu Corporation
Juki Corporation
Kanamoto Co. Ltd
Kansai Electric Power Co. Inc.
Kao Corporation
Kawasaki Heavy Industries Ltd.
Kirin Brewery Company Ltd.
Kubota Corporation
Kuraray Co. Ltd.
Kurita Water Industries Ltd.
Mabuchi Motor Co. Ltd.
Marubeni Corporation
Meitec Corporation
Mitsubishi Chemical Corporation
NGK Insulators, Ltd.
NichIASCorporation
Nippon Light Metal Co. Ltd
Nippon Shokubai Co. Ltd.
Nippon Yusen Kabushiki Kaisha
Nissan Motor Company
Nisshinbo Industries, Inc.
Nissin Electric Co. Ltd.
Oki Electric Industry Co. Ltd.
Oriental Construction Co. Ltd.
Osaka Gas Co. Ltd
Pioneer Corporation
Sanyo Denki Co. Ltd.
Sharp Corporation
Shikoku Electric Power Co. Inc.
Shin- Etsu Chemical Co. Ltd.
Shiseido Company Ltd.
Sumitomo Chemical Co. Ltd.
Sumitomo Metal Industries Ltd.
Sysmex Corporation
Taisei Corporation
Takeda Chemical Industries Ltd.
Tanabe Seiyaku Co. Ltd.
Tohoku Electric Power Co. Inc.
Tokyo Electron Limited
Tokyo Seimitsu Co. Ltd.
Tomen Corporation
Toray Industries Inc.
Toshiba Corporation
Toyota Industries Corporation
World Co. Ltd.
Yamaha Corporation
Yamaha Motor Co. Ltd.
Yokogawa Electric Corporation
Zeon Corporation