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ABSTRACT

An Investigation of Intellectual Capital Disclosure in Annual Reports of UK Firms: Practices and Determinants

Jing Li

This study examines the intellectual capital (IC) disclosure practices in the annual reports of 100 listed UK firms selected from sectors considered to be IC-intensive. It also investigates the possible determinants of such disclosure practices from the three perspectives of corporate governance structure, company characteristics and market factors.

IC disclosures were captured using content analysis, and were measured by a disclosure index, supported by word count and percentage of word count metrics to assess the variety, volume and focus of IC disclosure respectively, at both overall and subcategory levels. The presentational formats and locations of IC disclosures were also recorded.

The results indicate that the UK firms sampled provide considerable IC information in their annual reports, mainly in text form, with popular use of numerical information, while the use of graphs and pictures for many IC elements remains low. The distribution of IC disclosures, captured in three categories, varies by the three measures of disclosure applied. IC information was found in virtually all sections of the annual report and was most concentrated in the Operating and Financial Review section. IC terms typically used in the academic literature do not feature in the sampled annual reports.

The results of the statistical analyses based on the three measures of IC disclosure indicate significant associations with a number of corporate governance factors (i.e. board composition, share concentration, audit committee size and frequency of meeting, board directors' shareholding, audit committee directors' shareholding, and board directors with cross-directorships), company characteristics (i.e. firm size, profitability, and listing age), and market factors (i.e. 'hidden value', share price volatility, share turnover, and multiple listing). These findings offer support for a number of theories, such as information asymmetry, agency and signalling theory. The influence of these explanatory factors on human, structural and relational capital disclosures, based on all three disclosure measure metrics, as well as on the format of IC disclosure, was also explored. The study also finds that its IC framework is more effective than a less detailed framework used in prior studies for the purpose of examining IC disclosure practice and its determinants.

The study contributes to the further advancement of the state of knowledge in relation to IC disclosure both empirically and methodologically. It provides information users, preparers, regulatory bodies and academics with a state-of-the-art understanding of IC disclosure practices in the annual report. The transparent content analysis process enables future replication and comparison of results. The rigorous measurements of IC disclosure, the greater specificity of disclosure about the location and presentational format, and the more detailed IC research framework can be usefully applied by other studies. By examining the relationship between explanatory factors and IC disclosure, it helps shareholders and other groups of information users as well as the regulatory bodies to identify factors that may encourage IC disclosure in the annual report.

Keywords:

Intellectual Capital Disclosure, Annual Report, Content Analysis, Determinants, Corporate Governance, Company Characteristics, Market Factors, UK