

Making financial disclosures more readable

Firms should incorporate the use of plain English when drafting such documents so that the reader can understand.
 BY CLARENCE GOH, SEOW POH SUN AND GARY PAN

FINANCIAL disclosure documents are notoriously difficult to make sense of, even for seasoned investors. Warren Buffett, the guru of investing, spoke for many of us when he said: "For more than forty years, I've studied the documents that public companies file. Too often, I've been unable to decipher just what is being said or, worse yet, had to conclude that nothing was being said."

While financial concepts can themselves be complex, they are frequently made more difficult to understand by the manner in which they are presented to readers. Financial disclosure documents are often wordy and repetitive, and can contain unnecessary details. It is not uncommon for material information that is relevant to readers to be concealed by the use of jargon, or for companies to use convoluted explanations or descriptions in their disclosures.

To make financial disclosures more easily readable and understandable, companies should incorporate the use of plain English when drafting such documents. A plain English document uses words economically

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and at a level that the reader can understand. Its tone should also be welcoming and direct, and its design visually appealing. At its best, a document written in plain English should be understood by a reader the first time he or she reads it.

There are many benefits to having disclosures written in plain English. Investors would be more likely to understand the disclosures and to make informed judgments.

Investment analysts would also be able to make more timely and accurate recommendations to their clients if they can understand such disclosures more quickly and easily. In communicating with their investors in plain English, companies would also surely be more likely to successfully communicate their messages to investors and to build up stronger relationships with them.

Regulators around the world have been actively encouraging the use of plain English. In the US, the Securities and Exchange Commission (SEC) published a plain English handbook in 1998. The handbook was published with the objective of providing preparers of financial disclosures with a guide to using well-established techniques to create clearer and more informative disclosure documents. In his introduction to the plain English handbook, then SEC chairman Ar-



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thur Levitt acknowledged that "many investors are neither lawyers, accountants, nor investment bankers" and that companies need to "start writing disclosure documents in a language investors can understand".

He further expressed the hope that companies would use plain English to "speak to investors in words they can understand" and to "tell them plainly what they need to know to make intelligent investment decisions".

In Singapore, the Monetary Authority of Singapore (MAS) has also issued a set of guidelines on good drafting practices for prospectuses. Issued in 2015, these guidelines aim to provide guidance to issuers of financial products on good drafting practices for prospectuses.

THREE KEY RECOMMENDATIONS

The document makes three key recommendations. First, companies should strive to present information using plain English so that prospectuses are easy to understand. Second, to enhance the effectiveness of plain English, companies should also present information in a clear, concise, and logical manner. Third, companies should try to keep the length of their prospectuses as short as possible without compromising

on the accuracy or completeness of information that is required.

There are obvious benefits to preparing readable financial disclosure documents. But how can preparers of financial disclosures ensure that the documents they produce are readable? In addition to closely following the best practices prescribed in the guides produced by the SEC and MAS, one simple way for preparers to gauge how difficult their disclosure documents are to read would be to use readability formulas.

Readability formulas measure specific characteristics of a text that influence its readability and, based on these measurements, assign a corresponding readability score to that text.

One popular readability formula that has been used by practitioners and academics alike is the **Bog Index**. The Index is expressed as such:

$$\text{Bog Index} = \text{Sentence Bog} + \text{Word Bog}$$

- **Pep**
 A document which records a higher Bog Index score is less readable than one that records a lower Bog Index score.

Sentence Bog deals with readability issues related to sentence length. Longer sentences are often more convoluted and more difficult to read than shorter sentences. Consequently, documents with longer average

sentence lengths would record higher Sentence Bog scores than those with shorter average sentence lengths.

Word Bog addresses readability issues related to word difficulty, the use of abbreviations and acronyms, the wordiness of a text, the use of passive verbs, and other related style issues. Documents containing a greater number of these traits are more difficult to read, and would record higher Word Bog scores.

Finally, **Pep** measures the features in a document that are hallmarks of good writing. **Pep** reduces the overall Bog Index score because it makes reading a document easier and more enjoyable. Features that contribute to **Pep** include the use of interesting words, personal pronouns, contractions, and variations in sentence length.

GAINING INSIGHTS

To gain some insights into the readability of financial disclosures in Singapore, we used the Bog Index to measure the readability of Chairman's Statements published in the 2016 annual reports of constituent companies of the STI index. (see table)

While none of the 30 companies that we examined earned a "good" rating on the Bog Index (corresponding to a Bog Index score of 40 or below), 22 companies had an "aver-

age" rating (score of 41-70) and eight companies had a "poor" rating (score of 71-100). Also, no company was rated as "bad" (score of 101-130) or "dreadful" (score of 131 and above). Overall, this simple analysis suggests that while most of the companies on the STI index fare reasonably well in crafting readable disclosure documents, more can be done to enhance the readability of these disclosures to ensure that they are easily understandable to investors.

With the growing complexity of financial reporting, it is particularly important for companies to ensure that information that is communicated to investors is easily understood. In this respect, improving the readability of information that is disseminated is something that companies can focus on to enhance their communication with investors.

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An engaging good read?

COMPANY NAME	BOG INDEX*
Ascendas Real Estate Investment Trust	60
CapitalLand Commercial Trust	88
CapitalLand Ltd	69
CapitalLand Mall Trust	84
City Developments Ltd	66
ComfortDelGro Corporation Ltd	53
DBS Group Holdings Ltd	73
Genting S'pore PLC	52
Global Logistic Properties Ltd	86
Golden Agri-Resources Ltd	79
Hongkong Land Holdings Ltd	69
Hutchison Port Holdings Trust	76
Jardine Cycle & Carriage Ltd	54
Jardine Matheson Holdings Ltd	47
Jardine Strategic Holdings Ltd	49
Keppel Corporation Ltd	68
OCBC Ltd	78
SATS Ltd	53
Sembcorp Industries Ltd	65
Singapore Airlines Ltd	56
Singapore Exchange Ltd	69
Singapore Press Holdings Ltd	61
Singapore Technologies Engineering Ltd	76
Singapore Telecommunications Ltd	60
Starhub Ltd	54
Thai Beverage Public Co Ltd	43
UOB Ltd	51
UOL Group Ltd	64
Wilmar International Ltd	53
Yangzijiang Shipbuilding (Holdings) Ltd	54

* Based on the readability of the Chairman's Statement published in the company's 2016 annual report