Rhetorics in Financial Reporting: An Interpretive Case Study

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ABSTRACT

This study is a case study conducted in an Indonesian insurance company. The aim of the study is to understand the dynamics of financial reporting in the company. Ontologically, this study is built on a belief that financial reporting practice is a socially constructed reality. As a socially constructed reality, such a practice involves an interaction among social actors, and between organisational actors and the institutional and cultural environment in which the company operates. The main research question of this study is why and how the company constructs its financial reporting to deliver messages to its audience. This study reveals that the company is committed to quality financial reporting because such reporting can be used to gain legitimacy and to maintain social harmony. Consequently, financial reporting is constructed as a rhetorical story about its performance, management ability and insight into the future.

Keywords: Rhetorics, financial reporting, legitimacy, narrative, qualitative.

INTRODUCTION

This study claims that ontologically, financial reporting is a socially constructed reality that can shape, and be shaped by powerful actors and institutional environments. As a socially constructed reality, organisational actors can construct financial reporting so as to gain legitimacy and show that their organisation operates in accordance with socially acceptable beliefs, values and norms. Hurst (1970) argues that one of the functions of accounting, including corporate financial reports, is to legitimate the existence of the corporation. The role of corporate financial reporting is to inform a society that an organisation's actions are accountable, and that they conform to social values and norms.

If today's financial reports are compared with those of previous decades, it can be seen that contemporary reports are more professionally made, provide more information (narrative texts) and their presentation is more interesting, with colourful graphs and diagrams. This might be intended to attract stakeholders for the purpose of gaining legitimacy. Indeed, financial reporting represents what is probably the most important document in terms of a company's construction of its own social image (Hines 1988; Neimark 1992; Coy and Pratt 1998). Narrative texts included in annual reports are an example of how a company builds its image for gaining legitimacy from its constituents. As financial reports play an important role in describing organisational reality, companies are careful and serious in preparing financial statements. Consequently, it is reasonable to posit that manipulation of annual reports is an important part of the legitimation process (Dowling and Pfeffer 1975; Lindblom 1994) and that disclosure of information by companies can be viewed as a company's method in reply to the changing perceptions of the public (Patten 1992). This strategy refers to symbolic management (Ashforth and Gibbs 1990). For instance, researchers have found evidence of "self-serving attributions" in annual reports (Aerts 1994; 2005; Bettman and Weitz 1983; Salancik and Meindl 1984; Staw et al 1983). According to Aerts (1994; 2005) "self-serving attributions" refers to a robust tendency to attribute positive outcomes to the company's own actions (company strategies, decisions, human resources, and so on) and negative outcomes to external events (business climate, government regulations, political condition, and so on).

However, it is difficult to find an accounting study concerning rethorics in financial reporting. This study aims to seek an answer to the following specific question: "why and how does a company construct its financial reporting?"

This study is based on the understanding that reality exists as a social product and as a result of human interaction, symbolic discourse and creativity (Burrel and Morgan 1979; Denzin 1983; Hopper and Powell 1985; Morgan 1980; 1988; Tomkin and Groves 1983). Furthermore, it assumes that humans are incapable of total objectivity because they are situated in a reality constructed by subjective experience (Berger and Luckmann 1984). Meanings and the search for the truth is possible only through social interactions

(Streubert and Carpenter 1999). The inability quantitatively to measure some phenomena has led to intense interest in using other approaches to particularly human phenomena (Nahapiet 1988).

RESEARCH METHOD

This study was designed with an interpretive method of inquiry and was conducted in an organisational setting, as also suggested by Nahapiet (1988). This study used *PT. ABTBK*—a national insurance company listed on the Jakarta Stock Exchange since 1989—as a research setting. The reason for using the company is that insurance business in Indonesia is highly regulated—not only by accounting standards, but also other regulations released by the Jakarta Stock Exchange, the Indonesian Capital Market Supervisory Agency (*Bapepam*) and the Ministry of Finance-Republic of Indonesia. Furthermore, *PT. ABTBK* can be seen as successful in implementing a corporate governance mechanism especially in the transparency aspect. Annual report awards received by the company since the 1980s are evidence that the company is an example of one who practises good financial reporting practice in Indonesia, especially in the insurance industry.

This study used interviews and documents to collect data. A combination of such methods enabled the researcher to describe, interpret and analyse the financial reporting practice of *PT. ABTBK*. In qualitative research, there is no single approach to analysing data. The choice of methods is largely dependent on research questions (Baxter and Chua 1998); and research strategies (Glaser and Strauss 1967). Considering the research questions, data were manually analysed using a method suggested by Marshall and Rossman (1999) and Seidel (1998). They proposed six general phases of data analysis referring to data reduction and interpretation. In line with data reduction, the steps of analysis include organising data, generating categories, themes and patterns, and coding data. In addition, interpretation is undertaken through the following steps of analysis: searching for alternative explanations, and writing research findings as explained in the following section.

FINANCIAL REPORTING: LEGITIMACY AS A REASON

A company has legitimacy as a reason for publishing corporate annual reports. However, organisational legitimacy does not occur through merely making a profit and complying with legal requirements. Instead, reference to the existing norms, beliefs and values of society is crucial in ensuring that an organisation has achieved legitimacy. As a device to deliver messages of organisational reality, financial reporting is consequently used to earn legitimacy in the society in which company activities take place (Oliver 1991; Parsons 1956). Hence, in the context of organisational interaction with society, Deegan (2001) claims that:

> …organisations continually seek to ensure that they operate within the bounds and norms of their respective societies, that is, they attempt to ensure that their activities are perceived by outside parties as being legitimate.

A company might create an image that is perceived to be in accordance with socially imposed values. The company actively seeks images that have positive values, and avoids negatively valued images (Gardner and Martinko 1988). In doing so, "impression management" might be employed in creating annual reports. Impression management is a social concept, which is defined as "the conscious or unconscious attempt to control images that are real or imagined in social interaction" (Schlenker 1980).

Different impression management strategies can be adopted for different stakeholders (Marcus and Goodman 1991). It is easier for a company to adopt such strategies because there is power asymmetry affecting how much attention different stakeholders receive (Allen and Caillouet 1994). Consequently, actions made visible by powerful stakeholders will be reframed by accounts in annual reports; actions made visible by less powerful stakeholders will be ignored (Neu et al. 1998).

In relation to how management seeks legitimacy, it can be argued that *PT. ABTBK* has been able to show that substantive management—as discussed by Ashforth and Gibbs (1990) is more important than symbolic management as a strategy in gaining legitimacy. The annual report awards and other awards indicated how *PT. ABTBK* has used corporate annual reports as a medium to gain legitimacy and to increase public confidence in *PT. ABTBK*. Gaining public confidence plays significant roles in increasing the public image on which *PT. ABTBK* runs socially acceptable activities. This is consistent with a statement by an employee (Mr F) of *PT. ABTBK* on 21 September 2004 who said:

> …an annual report award is important for *PT. ABTBK* because the award can increase public confidence. This is related to the implementtation of good corporate governance principles. (My translation)

Similarly, one of the branch office heads on 5 October 2004 claimed that:

> …an annual report award is very important for us. When people raise questions about *PT. ABTBK*, the award is the answer. The award tells them that *PT. ABTBK* has conducted ethical and transparent business. (My translation)

A statement by an assistant manager in the Accounting Division (Mr A) on 3 September 2004 also supported such a claim. He noted that:

> ... the annual report award is useful for this company for example to enhance the company image. Thus, the society might say, "look, *PT. ABTBK* is transparent in providing information of its activities to the public". (My translation)

In line with the reason why *PT. ABTBK* chooses a substantive strategy, it might be useful to consider self-presentation theory. According to self-presentation theory, as Aerts (1994) notes, people (including management) give an explanation for their behaviour that is designed (consciously or not) to defend their claims to positive social identities or images. How people determine coping strategies in their justification is influenced by the nature of what has to be explained and the conditions in which the causal claim are created (Tetlock 1985). Thus, through these behaviours, individuals (including company management) seek to be perceived as successful, competent, trusted, responsible and rational. In the case of *PT. ABTBK*, the Director of Administration Services on 8 September 2004 argued that:

> …an annual report award instils pride in us. Internally by winning the annual report award, the directors can use the award as a medium to institutionalise the spirit of fairness and honesty. Externally, the award can be used as marketing media, because the insurance business is a business of trust. The annual report award tells society that *PT. ABTBK* is credible and can be trusted. (My translation)

The statement shows that trust is an essential part of the search for legitimacy. Shockley-Zalabak, et al. (2003) concluded that trust is a result of communication behaviour, such as delivering accurate and reliable information of company activities, exposing sincere and appropriate openness and giving justification for any decisions. The manner in which a company delivers messages in a corporate annual report is an important point in a corporate communication strategy, whereby trust can be constructed by convincing others that the company is pursuing a socially acceptable strategy (Kohut and Segars 1992).

One such strategy that enables a company to seek legitimacy is by including narrative texts in annual reports. The use of narrative texts enables a company to tell the reality of an organisation to a society. Aerts (1994) argues that:

> narrative accounting reports are one of the means by which corporate management can legitimise the company's activities and outcomes. Verbal behaviour and more specifically, the way in which facts, events and actions are explained, is important, certainly in external relations, because it defines the essential elements of the corporate performance environment and portrays the normative and empirical bases on which to judge the appropriateness of the company actions.

In this regard, what *PT. ABTBK* has conducted is consistent with this view. Indeed, narrative texts have been used by *PT. ABTBK* to make a true portrait of its historical performance, show insights of its future, and define management capability for the purpose of legitimating its activities. On average, *PT. ABTBK* takes up 50 pages of every annual report to write narrative texts on the report.

How and why a company publishes a corporate annual report is influenced by socially acceptable values. If the company management perceives that their legitimacy is under attack by public concerns, management will react to this by improving the quality of financial reporting, for example, by increasing the level of company disclosure (Brown and Deegan 1998). For the purpose of showing that *PT. ABTBK* operates in accordance with the social values, its annual reports always deliver messages related to its contributions to the social environment, for example:

> To maintain social and environmental equilibrium, the company adopts an ongoing effort as a participator in the development of social and community environments (2002 annual report, p. 47).
>
> As part of the realisation of the measures reflected by its business ethics, the company at all times makes every possible positive contribution to the environment where it operates... For the purpose of maintaining social and environmental balance, the company makes a continued effort to participate in the construction of a social environment (2003 annual report).

How PT. ABTBK has practised financial reporting shows that quality financial reporting is published in order to gain legitimacy, rather than simply to provide useful information. Financial reporting has been used as a medium to communicate an organisational reality of PT. ABTBK to the Indonesian society that PT. ABTBK does not break social harmony. As Coy and Pratt (1998) note, an annual report plays an important role in communicating and shaping the reality of the organisation in the public's mind. How this reality is perceived depends in part on the extent and quality of information provided in the annual report.

PT. ABTBK is committed to such financial reporting practice because it can be used to build "an image of the corporation that ingratiates it with its stakeholders" (Stanton et al 2004), so as to obtain approval by conveying compliance with the normative rules of the institutional environment (Dowling and Pfeffer 1975). Moreover, as Allen and Caillouet (1994) posit, by self-promotion, acclaiming the corporation's roles, including that of being socially responsible, a company asserts its appreciation for institutional norms and values. What *PT. ABTBK* has done in its annual report is to declare its support and compliance to institutional norms. As such, financial reporting is designed as a rhetorical story to attract those interested in company activities.

FINANCIAL REPORTING AS A RHETORICAL STORY

The term "rhetoric" is appropriate in any case where the medium of an organisation to communicate its activities is a language. As financial reporting is a part of accounting activities and seen as a business language, it is reasonable to claim that an annual report is a rhetorical story—a story about company activities intended to persuade outside parties to support the company's existence. The importance of a language is also supported by Arrington and Schweiker (1992) who argue that:

> …accounting, like other social practice, is rich in meaning: complex, multifaceted, historically fluid, and variant with the particularities of individuals, values, interests, institutions, histories, modes of practices, and consequences in which accounting acts are situated.

In addition, accounting language is rhetorical because it argues and persuades like any other discourse (Thompson 1991).

Before discussing annual reports as rhetoric, it would be useful to discuss what rhetoric constitutes. Such a discussion is important because rhetoric can be interpreted differently, from bombastic and misleading language devices to argumentative language devices.

What is Rhetoric?

The word rhetoric has been widely cited in discussing politics and communication. In general, rhetoric is seen as a term dealing with the use of both written and verbal language to persuade an audience. In the *Oxford English Dictionary* (1992), rhetoric is defined as:

> The art of using language so as to persuade or influence others; speech or writing expressed in terms calculated to persuade or impress (often in a deprecatory sense); language characterised by artificial or ostentatious expression.

In this definition, rhetoric refers to a language that is intended to persuade someone to feel, think or do something for an ostensible reason when the actual reason is different.

Similarly, Hopper and Pratt (1995) describe rhetoric as a form of persuasive or effective speech or writing that is intended to control a reality, and is used to obscure real meaning—even to "promote ambiguity". Hence, rhetoric is used to signify a language that might be intended to mask a reality in order to seduce compliance and consent.

However, it should be noted, as Carter and Jackson (2004) claim, that "rhetoric is not just an unfortunate epiphenomenona of language use, but a total system of persuasion, reinforcement and reassurance". Even though rhetoric has been described as an art, it can be seen as a process of argumentation and persuasion (Carter and Jackson 2004).

Rhetoric as a Process

Rhetoric, as a process, has a certain characteristic. Perelman (1982) proposed two key characteristics of rhetoric: style and context. The first characteristic of rhetoric is "style", which involves a choice that a rhetorician makes in the way that an argument is presented. As style concerns presentation, rhetoric will be greatly influenced by the ability of the arguer in presenting arguments (Carter and Jackson 2004).

The second characteristic of rhetoric is "context", referring to consideration of a particular situation in which the argument is made. Thompson (1991, p. 598) argues that "what is said, how it is said, and why it is said...need to be placed in its contingent institutional context". Hence, a context in rhetoric deals with a particular situation in which an argument is made. In other words, arguments are addressed to an audience. Indeed, an audience is the context of stylistic techniques that is extremely important to the rhetoric (Carter and Jackson 2004).

To whom persuasion will be directed is a matter of a speaker's construction. It is claimed that a universal audience is the most difficult one to address. Thus, rhetoric is mostly directed to a particular audience. The rhetorician must adapt to the particular audience and can only argue in accordance with the ideas and concepts already accepted by the audience (Carter and Jackson, 2004). According to Perelman (1982), the point of arguments is to secure or to reaffirm adherence—not to convince an audience of a truth which must be accepted notwithstanding previous beliefs. In other words, the process of rhetoric is not to challenge beliefs, but to reinforce them.

DESCRIPTION OF FINANCIAL REPORTING OF *PT. ABTBK*

Corporate annual reports might be divided into two sections: the first containing graphs, pictures and narrative texts, and the second describing financial figures and fewer narrative texts. To analyse annual reports of *PT. ABTBK*, this study uses three annual reports that were entered in the annual report award competition: the 2001, 2002 and 2003 annual reports. Beside the fact that such reports were the most currently available at the time field research was being conducted, the 2001 annual report won the annual report award competition, whereas the 2002 and 2003 annual reports were ranked fourth and sixth respectively.

The First Section of the Annual Report: Building Company Image

The first section of the annual financial report of *PT. ABTBK* consists of a colourful cover, and graphics, pictures and narrative texts describing a profile of the company, with messages, management discussion and analysis.

The Cover: Discerning the Corporate Message

The cover of annual reports is often designed to describe an image of a company. The covers of the annual reports of *PT. ABTBK* uses different pictures, designs and captions to covers the current condition of the company. According to Preston et al. (1996) such images and captions show that annual reports are "a visual medium through which corporations, one of the principal political, social, and economic institutions of the twentieth century, attempt to represent and... constitute themselves".

The 2001 annual report cover is characterised by a picture of an eagle carrying a flower and flying above layers of bricks. The caption reads: "Start with a Piece of Commitment and Integrity to Build Trust". This report was intended as a testimony to *PT. ABTBK*'s commitment and integrity, so the picture and caption are visual representations of the way that *PT. ABTBK* has a commitment and integrity to build trust with customers and to protect them. In the 2001 annual report, *PT. ABTBK* claimed:

> The layers of bricks describe the activity of building something...[to represent] the verb 'to build'...The process of brick laying into a building demands prudence. It can be further interpreted that the building will give shelter to anybody inside it.
>
> A flying eagle carrying a flower in its claws symbolises the service quality of *PT Asuransi PT. ABTBK*. An eagle symbolises something robust and invulnerable. The flower has a philosophical meaning of providing the best services at all times.

The pictures and captions on the cover of the 2001 annual report are different from those of the 2002 and 2003 annual reports. The cover of 2002 annual report has a picture of a warrior and a star with a caption reading: "...to Serve and Protect". *PT. ABTBK* claimed that a warrior in an upright position reflects "the strong determination and commitment of *PT. ABTBK* to serve and to protect its clients from the risks of financial losses by providing quality [insurance] products and services". The warrior who is wearing an armoured-war uniform is intended to represent the readiness and consistency of *PT. ABTBK* in coping with increasing competition in the insurance business. The image of a star represents an element that strengthens the company identity.

A different picture and caption can also be seen in the 2003 annual report, where the condition of *PT. ABTBK* is visualised by a historical, monumental building, which was supported by large pillars and with a caption reading: "Stronger for Your Protection". This picture symbolises the firm foundation of *PT. ABTBK* to show the abilities of the company in coping with a competitive insurance business. The strong pillars represent the commitment of management to maintaining the credibility of *PT. ABTBK* in delivering the best services to customers.

The use of such pictures and captions aims to tell the audience about *PT. ABTBK*. Of course, how the audience perceives *PT. ABTBK* depends on their interpretation of the pictures and captions. Barthes (1964) believes that "in advertising, images are presented with a view to the best reading; its meaning is intended to be clear or at least empathic" (quoted by Preston, et al. 1996). In the annual reports of *PT. ABTBK*, there are definite attempts to communicate an empathic message and relate the image to a particular corporate attribute. Photographs or pictures within annual reports do not reflect how people behave, but how one thinks they behave (Anderson and Imperia 1992). In addition, photographs or pictures are used to lend credibility to the report (Graves et al 1996) and are intended to persuade readers (Simpson 1999).

In regard to different pictures and captions on the covers of annual reports, the Directors of Financial Services who is responsible for producing annual reports, on 24 August 2004, explained as follows:

> Each year our annual reports have different symbols, mottos [captions], and styles of presentations...We have reasons for doing this. First of all, we want to express the experience of *PT. ABTBK* in the annual report. Because *PT. ABTBK* has experienced different challenges in doing business we put different pictures and mottos [captions] on the reports. Second, it relates to a style of design. For example, we believed that in 2004 *PT. ABTBK* would make good progress in the insurance business. Thus, we put a picture of strong pillars on the cover of the 2003 annual report and wrote a motto: "Stronger for Your Protection" on it (My translation).

This explanation shows that financial reporting uses rhetoric intended to persuade the audience. However, it can be argued that the literary devices used by *PT. ABTBK* are not intended to manipulate the real facts. Instead, *PT. ABTBK* has tried to portray the "true picture" of its activities.

Narrative Texts: Looking Beneath the Surface

Besides pictures and captions on covers, the first section of a corporate annual report also comprises narrative texts, graphs and pictures. The 2001 annual report of *PT. ABTBK,* for example, contains fifty pages of narrative texts, tables and graphs imparting messages from the Board of Commissioners and the Board of Directors, the history of the company, business risks, opportunities and threats, description of powerful staff members, ownership structures, and an analysis and discussion of company performance.

It is important to note that narrative texts significantly dominate the first sections of the annual reports. Most of these discuss management views in regard to company performance, insights into the future and management capabilities to run the company. For example, the 2001 annual report states that:

> The company achieved targeted premium income whereas the net profit after tax decreased and was lower than that of the previous year but only 4% below projected profit. The negative growth of premium income in 2000 resulted in a significant increase in the unearned premium reserve in 2001. Another factor that decreased the 2001 profit was an increase in incurred claims. Both factors are the main causes of a decrease in the company's underwriting result.

These statements are mainly intended to justify the reasons for a decrease in company performance. In addition, when describing the 2002 company plans, the Board of Directors wrote an analysis in the 2001 annual report as follows:

> The undue recovery of the nation's economic situation [that] is worsened by the tragedy on WTC New York on 11 September 2001...has brought along additional burdens to the national insurance companies, which are endeavouring to prepare themselves for the forthcoming AFTA where the level of competition will be tougher.
>
> Notwithstanding the above situation, we can be proud that the company is able to renew all treaty programs for 2002 without any shortage in reinsurance protection... Amazingly, the company is able to have reinsurance protection for sabotage and terrorism risks which have disappeared from the Indonesian market (and from the market in certain countries). This enables the company to provide clients with a whole range of protection...

To support what has been done by the Board of Directors, the Chairman of the Board of Commissioners in his message to shareholders in the 2001 Annual Report of *PT. ABTBK*, said:

> ...what the management of *Asuransi PT. ABTBK* has done in 2000 in giving first priority to the enhancement of "Credibility" and "Service Quality" within the framework of Good Corporate Governance is a forward looking policy. As a consequence of this policy, we observe, the increase in operating expenses resulting in the decrease in the profitability by 31% in 2001 compared to 2000 is reasonable as this situation has been mainly caused by the significant increases in the claim cost and unearned premium reserve.

These texts are intended to provide an argument and explain the logic of the causes of success and failure of *PT. ABTBK* in managing resources entrusted by stakeholders to its management. In this regard, on 7 September 2004 a manager (Mr C) in the Accounting Division who previously worked at one of the "big five" accounting firms in Indonesia claimed that:

> *PT. ABTBK* also discloses information voluntarily. For example if we gain tax returns, we will make a note on the related accounts. Or... we can provide additional narrative texts to tell certain important information. These will allow users to gather more information than they need, so it is not necessary for them to raise questions to *PT. ABTBK*. (My translation)

Similarly, the head of the Internal Audit Unit, on 9 September 2004 believed that:

> We always attach voluntary explanations of any items that we consider important for users to know. This is part of our commitment to transparency. We always try to disclose any information as transparently as possible. (My translation)

These statements are supported by the Director of Financial Services, on 24 August 2004, who pointed out that:

> A voluntary disclosure is an automatic process. I mean if we think that such a disclosure is important and makes financial reporting more useful we will do that. By so doing, we wish that users or readers will be encouraged to know more about our company. (My translation)

The above statements demonstrate that *PT. ABTBK* has used narrative texts to describe the company's efforts and accomplishment below the surface in the insurance industry.

The Second Section: the Statutory Form of a Rhetorical Story

The second section of the 2001 annual report consists of 57 pages of statutory materials. This section includes six reports/statements: an audit report, a balance sheet, a statement of income, a statement of changes in stockholders' equity, a statement of cash flow and notes to the financial statements. There are no graphs or pictures on this section but narrative texts are still included, especially in the notes to the financial statements, to help users understand accounting policies used by *PT. ABTBK*.

In the audit reports, *PT. ABTBK* always requests that external auditors put the name of the international audit firm with which the local auditors are affiliated on the heading of the report. As a result, all audit reports concerning *PT. ABTBK* financial statements are always written by the external auditors, including the name of the international audit firm. This request can be seen from a discussion in the Audit Committee meeting on 25 September 2002. The Chairman of the Audit Committee asked the external auditor to include the name of the international auditor in any papers used in correspondence:

> In an engagement letter, the audit committee saw an unclear statement that needs further clarification from the external auditor. It should be clearly stated that any matters related to correspondence and reports must be written on the paper with the logo of "Ernst & Young International Ltd", not just the "*Prasetyo Utomo*" Audit Firm. (My translation)

Furthermore, on 10 October 2002 the Audit Committee and the Board of Directors had another meeting with the external auditor to finalise the engagement letter. In this meeting, the Audit Committee asked the auditor about a change in the international partner from Arthur Anderson to Ernst & Young. In reply to the question, the external auditor explained that a change in the international audit firm is mainly due to the fact that the credibility of Arthur Andersen had been questioned after the firm was involved in the Enron scandal. A change in the affiliated partner is considered important by *PT. ABTBK* because such a change can deliver a certain message to its audiences and can be differently interpreted by the audiences.

Other financial statements, such as balance sheets and income statements are not different from those of other companies. Part of the *PT. ABTBK* financial statements that provides narrative text is in a note to financial statements. This section clearly tells a story how *PT. ABTBK* uses accounting policies and complies with regulations. For example, in the Summary of Significant Accounting Policies in the 2001 financial statements, note 2a: Basis of Financial Statement, it is stated that:

> The financial statements have been prepared on the historical costs basis of accounting, except for investment in marketable securities... in conformity with *generally accepted accounting principles in Indonesia*. The financial statements are presented in accrual basis, except for statements of cash flows [emphasis added].
> The statements of cash flows present the receipts and payment of cash on hand and in banks classified into operating, investing and

> financing activities. Effective on 1 January 2000, cash flows from operating activities *are presented based on Decision Letter of BAPEPAM No. Kep-06/PM/2000 dated 13 March 2000 on the amendment of Rules No. VIII.G.7 "Guidelines in the Presentation of Financial Statement* [emphasis added].

The above examples show how *PT. ABTBK* is committed to quality financial reporting practice by complying with regulations. The numbers and narrative texts are used as a story to tell the truth about a company's condition. These messages are mainly intended to persuade those who are interested in the financial reporting of *PT. ABTBK.* In line with narrative texts written on annual reports, it is important to note that financial reporting is characterised by serious texts, which use understandable and formal language. Indeed, it is difficult to find any unnecessary words, phrases and sentences.

In annual reports, as Preston et al (1996) argue, certain phrases typify the rhetoric of designers. Such phrases are intended to send the right messages to mirror the bankable value of a company (Pettit 1980), to overcome conflict among external perceptions of the company (Howard 1991), or to frame the way various members of the public know or feel about the company (Hood 1963). The right messages might be directed to enhance the story of a company's performance contained in the financial statements.

RHETORIC AND TRUTH IN ANNUAL REPORTS

Understanding the definition of rhetoric will lead questioning about whether annual reports are used as a rhetorical story to mask the reality of the company. The current belief about rhetoric is that language is used to persuade an audience by masking a reality with literary devices and wordy flourishes for the purpose of hiding a reality. Thus, in everyday speech, as Thompson (1991) notes:

> …'rhetoric' has connotations of bombastic demagoguery. It is the device of the less than honest politician in his or her attempt to manipulate the political arena. It is associated with a disreputable practice of propaganda and cajolery, involving flowery diction and empty figures of speech.

However, it can be argued that rhetoric does not always connote such views. Indeed, rhetoric can be seen from a positive side. In this study rhetoric has a different meaning and application from those of current commentators. This is because the rhetoric of financial reporting can be used to gain legitimacy by employing a substantive strategy rather than a symbolic strategy.

The Positive Side of Rhetoric in Financial Reporting

It is claimed that to gain legitimacy a company can choose two approaches: substantive management and symbolic management (Ashforth and Gibbs 1990). If a company chooses the first approach, the company will use a language device to convince an audience about the truth of the company's activities. Young (2003) rejected a view that rhetoric is a mere addition, a flourish, and a deliberate attempt to trick the simple or weak-minded. He views rhetoric the opposite way from the current commentators. Young (2003) argues that rhetoric is:

> …a pervasive element within our lives as we argue with and attempt to persuade others and ourselves of the viability, credibility, and plausibility of our positions, beliefs, problems, solution and perspectives. Through persuasion, significances and meaning are established in our lives as well as in the more specialised arenas of politics and policy making... mathematics... and economics.

Within this context, rhetoric can be argumentative language describing a reality and used to persuade an audience. Rhetorical techniques are resources that are drawn on in efforts to persuade others about the "correctness" of a particular view of reality (Young 2003). This implies that rhetoric tends to be argumentative.

Young's arguments show that the central point of rhetoric is more concerned with the way arguments and conversations are conducted in an attempt to persuade, rather than to manipulate facts or information. Rhetoric sees argumentation as a social activity and focuses its functional design of language on managing a controversy and disagreement (Young 2003). Consequently, rhetoric locates rationality of argumentation in the process of overcoming doubts and answering objections. This involves aspects of morality and emotions in those who are arguing. In this regard, Thompson (1991) argues that:

> Three distinct but not separable forms of argument have been traditionally deployed here, it is suggested: ethical appeals (*ethos*) involving one's own values and one's own character, emotional appeals (*pathos*) involving an appeal to the feelings of the audience; and rational appeals (*logos*). The preparation of, and reflection on these kinds of appeals is known as the invention of the arguments [original emphasis].

Considering such views and arguments, it is believed that corporate financial reporting can be used as a rhetorical story to persuade ethically stakeholders to support company strategies and goals. This argument is consistent with arguments by other scholars who see accounting practice as rhetoric. Covaleski et al (1995), for example, believe that "...accounting is not only an instrument for representing economic reality...but also a rhetorical device for setting forth...". Moreover, Nahapiet (1988) concludes that accounting is a language for discourses, a set of rules for negotiating an understanding or an organisational reality and a mechanism for establishing and maintaining the legitimacy of social actions.

An example of the use of rhetoric can be seen from a message by the Board of Commissioners in the 2003 annual report of *PT. ABTBK* as follows:

> The year 2003 was the year of changes and rearrangement, marked with two events of Board of Directors change, followed by changes in their subordinate's functions, responsibility and duty, as it is reflected in the new organizational structure...It is understandable at this early stage that the changes affected the company's performance...

This statement shows that the decrease in performance is not a major problem for *PT. ABTBK* because the decrease is caused by important changes in the organisational structure.

The reason why financial reporting can be used as a rhetorical device of communicating a reality is that financial reporting, as a part of accounting activities, can be interpreted in different ways by using argumentative language. In the case of *PT. ABTBK*, the Director of Financial Services on 24 August 2004 agreed with the importance of language in annual reports. He claims that:

> I see quality of an annual report from its completeness and the way the annual report is presented including wording used in it...When I read the annual report of *PT. Aneka Tambang, Tbk*, the presentation of the report is excellent. Even though I am not an employee of *Aneka Tambang* and do not understand the mining industry, I enjoyed reading the report and found it easy to understand ...For me the use of language in annual reports is important because it motivates readers to know about a company. (My translation)

This statement implies that all narrative texts, including those stated in corporate financial reporting, are the result of conscious deliberation by knowledgeable individuals. Hence, it is necessary to understand why texts are written and at whom they are directed.

Texts motivate certain beliefs and behaviour (Young 2003). Any arguments, justifications and values contained within them are intended to tell the audience about what the writers believe, and should persuade the audience to accept a particular viewpoint or undertake particular actions. In fact, as Young (2003) argues, "facts are marshalled and arguments are presented, considered, and disposed". They are intended "to make a point or argument, to present a concern or to serve as a reason to accept a position or to act" (Young 2003). Thus, rhetoric in this study is telling the truth about an organisational reality by providing argumentation and logic.

Telling the True Reality of an Organisation

Financial reporting does not merely discuss accounting numbers. It also contains serious texts, because it uses lengthy sentences and formal language describing what happened in the past and what the company will achieve in the future. Even though annual reports are not the only source of information about the performance of a company, annual reports are considered as significant sources due to wide coverage and availability of annual reports (Hooks et al 2002).

The annual report is a comprehensive communication intended to make company information easily and routinely available in a single document (Hook et al 2002). The annual report is a multi-objectived and multi-audienced communication (Anderson and Imperia 1992). The potential audience of annual financial reporting is "composite" (Myers 1999). Annual financial reporting is not only required by shareholders, but also read by competitors, suppliers, customers, regulators, the press and other parties interested in the annual financial report. Although this mass communication has so many intended recipients, the main audience is frequently considered to be shareholders (Kohut and Segars 1992; NIRI 2004).

Considering the audience of such reporting, annual reports contains basic information about a company expressed both in financial and narrative texts. The narrative texts are intended to supplement financial information. A combination of quantitative information and narrative data enables an annual report to supply information to those who need it. Hence, narrative texts are becoming increasingly important in external financial reporting. This is particularly important because traditionally, these narrative texts have been unaudited. There is, therefore, potential scope for managers to control and manipulate the impression conveyed to users of accounting information (Deegan and Gordon 1996).

However, it can be argued that the use of narrative texts depends on the designer of corporate annual reports. Indeed, narrative texts can be used to explain or to give an argument in regard to company performance or what the company management has done in running the company. To some extent, the behaviour in writing a necessary narrative text in financial reporting is influenced by corporate culture and the ethical conduct of the designer.

Rhetoric of financial reporting is designed to tell a true story of an organisational reality. Thus it is hard to find any unnecessary language just to mask the reality of the company being described in an annual report. This can be seen from the case of *PT. ABTBK* when the Board of Directors made an argument in the 2001 annual report in regard to a decrease in profit. The Board of Directors said that:

> We achieved the targeted premium revenue even though income after tax was lower than last year but it was only 4% lower than the projected income. The negative growth of premium revenue in 2000 led to an increase in premium reserves in 2001. Another factor that caused a decrease in profit in 2001 was the increasing number of claims. Both factors contributed to the decrease in underwriting results

These sentences were used by the Board to explain the causes of a decrease in the income of PT. ABTBK. There are no wordy flourishes used to mislead audiences. Instead, the report used an argumentative style, telling the truth, to persuade the audience that such decreases are reasonable.

In line with financial reporting practice in PT. ABTBK, the Director of Administration Services, who is also one of the minority shareholders, on 8 September 2004 claimed that PT. ABTBK is committed to providing the true information to its audiences. He said:

> ...a good annual report is one that shows accurate information and provides enough narrative explanations of company activities. However, it must tell the truth. *PT. ABTBK* has produced such a report. (My translation)

On 7 September 2004, an ex-external auditor (Mr C) who currently is employed by PT. ABTBK also confirmed the commitment of PT. ABTBK to portraying the true organisational reality and said:

> If we compare the annual report of *PT. ABTBK* to that of other insurance companies, the annual report of *PT. ABTBK* is the best. I mean *PT. ABTBK* has presented transparent and informative figures in the annual report. When we read the report we will understand what the figures or information mean. (My translation)

The case of *PT. ABTBK* also shows that financial reporting has provided a unique access to a company's embeddedness in a civic society. This is because annual reports are "the most publicized and visible documents produced by a publicly owned company" (Henriques and Sadorsky 1999). In addition, annual reports are intended to "communicate implicit beliefs about the organisation and its relationship with the surrounding world" (Fiol 1989). An annual report at least delivers messages of historical performance and an insight into the company's future and management capability (Ind 1997).

Historical Performance

In terms of historical performance, annual reports can be used as a device to diagnose past events and to attribute the praise or blame for the events. Indeed, companies usually claim credit for their success but attribute failures to external factors (see Bettman and Weitz 1983; Salancik and Meindl 1984). Narrative texts, as part of language, can be used as a device to show such attribution. Thus, corporate financial reporting, as business language, might be used to obscure distinctions about the causes of poor performance, presenting the company in a positive light (Jameson 2000). For Thomas (1997), language is used to blur attributions. These attributions can be seen as "hedonic bias" (Aerts 1994), showing a general tendency to attribute anything negative to external environmental causes and to attribute favourable outcomes to internal dispositional factors.

In general, some studies (Aerts 1994; 2005; Bettman and Weitz 1983; Salancik and Meindl 1984) have documented a robust tendency to attribute positive results to the company's own actions (company strategies, decisions, human resources, and so on) and negative outcomes to external events (business climate, government regulations, political condition, and so on). Hence, in describing its performance, a company can explain negative performance in either technical accounting terms (Aerts 1994) or convoluted language (Jones 1996). On the other hand, the company can explain good performance in strict cause-and-effect terminology so that management's responsibility for them is clear (Aerts 1994).

The financial reporting practice of *PT. ABTBK,* to some extent, might show this phenomenon. However, *PT. ABTBK* has conducted such a practice for neither misleading audiences nor hiding true information. Instead, this is part of its honesty and ethical conduct to tell the real story of *PT. ABTBK* performance. For example, when describing the history of *PT. ABTBK* in the 2003 annual report the Board of Directors claimed that:

> One reason why *PT. ABTBK* has been successful during the last four decades in the insurance industry is that *PT. ABTBK* is always consistent in implementing good corporate governance principles. The spirit to implement good corporate governance has been inherited from the founders of *PT. ABTBK* whose idealism was to promote the dignity of Indonesian people through economic and trade activities that were previously dominated by foreign companies. Thus, it is no wonder that *PT. ABTBK* has been awarded the Annual Report Award by BAPEPAM from 1980 to 1983 even though at the period *PT. ABTBK* was still a private company that did not raise capital from the capital market.

This statement shows that the cause of success was an internal factor, the ability to implement good corporate governance principles.

However, the internal aspect is also mentioned as the cause of a decrease in company performance. For example, in the same report it is claimed that:

> 2003 was a rather tough period to go through. Ever since there was awareness about the decrease in our earnings in 2002 which was specifically due to the growing number of claims, the company made several changes in technical policies...[*which*] have had a direct impact on the decrease in the amount of our premiums.
>
> Internal efforts to improve infrastructure and to apply the principles of good corporate governance... caused a fairly strong contraction and decrease in a number of personnel at several key positions.

The above statements illustrate that internal changes and management ability contributed to a negative performance.

It might be true that, in annual reports, a positive performance provides a powerful signal of managerial competence, and does not necessarily need further explanation to make them consistent with a desired organisational image (Gibbins et al 1990). But this does not hold for a negative performance, which has to be explained to make intelligible or legitimate (Scott and Lyman 1968). However, *PT. ABTBK* practises a balance in arguments in regard to its historical performance. Indeed, the company has provided explanations to both positive and negative performances. The reason for doing this can be seen from a statement by the President of the Board of Directors on 16 September 2004:

> I think what is meant by a quality annual report is a report that fairly presents what is really going on in the company. We must be honest in reporting information. If our performance is unfavourable we might be able to manipulate data or information to make it look favourable. But we always think...what is the point of doing that? I think it is not necessary for us to manipulate data. If other companies do that, it is their choice. We do not copy such an unethical practice. I always believe that external auditors will find any frauds and irregularities. (My translation)

The statement by the President of the Board is also reinforced by those who are directly involved in recording a company's transactions. For example, on 21 September 2004 Mr E, who has spent more than 15 years in the Accounting Division said:

> I think *PT. ABTBK* never hides any important information. We provide transparent and completed data. What the users need is available on annual reports. (My translation)

This view is similar to that by Mr F, who also works in the Accounting Division. On 21 September 2004, he claimed:

> We never manipulate data and there is no involvement of top management that forces me to manipulate data. I think the quality financial reporting is determined by the honesty of staff involved in it. (My translation)

In addition, management always praises the company workforce as an important part of a company's success and consequently, this is mentioned in annual reports. For example, in the 2001 annual report, the Board of Directors claimed that:

> With all we have been through and trying to achieve in 2001, the management wish to express thanks especially to all staff and employees of the company who have worked hard, sincerely understood the company's demands and have high commitment to maintain the company's existence, which may bring benefit to the shareholders, management, employees and clients.

The Board of Commissioners also supports the importance of employees for *PT. ABTBK*. In the 2003 annual report of *PT. ABTBK*, the Chairman of the Board of Commissioners concluded that:

> The ability [of PT. ABTBK] to recover [from the economic crisis] and become a stronger company is not generated by the capital strength, nor by a sophisticated technology, but by the idealistic spirit of our people who always want to enhance their abilities/skills, to make corrections, to make changes and improvement…

The above statement provides evidence that the annual report is used as a vehicle to exhibit the fact that internal factors and workers' enthusiasm have contributed to the success of *PT. ABTBK*.

On the contrary, it can be seen that the cause of failure is to some extent determined by external forces which *PT. ABTBK* cannot directly control. For example, in the 2003 annual report it was claimed that:

> The decree issued by the Minister of Finance 30 September 2003 requires earlier payment of premiums, from 90 days to 60 days. Failure to comply with this regulation will result in the fact that the premium cannot be recognised as admitted assets and will consequently decrease our solvency.

This statement implies that it is the regulation that influences company abilities in achieving the level of solvency. However, problems of regulations are faced not only by *PT. ABTBK,* but also by other insurance companies. To understand this, it might be important to note what the Director of Administration Services said on 8 September 2004 about the regulation:

> We have very tight regulations in the insurance business, for example, the regulation about risk-based capital (RBC) and admitted assets. This regulation has made the Indonesian insurance business more difficult. When I explained this regulation to a director of a British insurance company, he said to me, "if this regulation is applied in the UK, my company will go bankrupt. The implementation of the regulation is too fast. It is impossible to fulfil the targeted RBC within four or five years". (My translation)

Statements by parties outside *PT. ABTBK* concerning these tight regulations also support such difficulties. For example, Mr Hotbonar Sinaga, the Chairman of *Dewan Asuransi Indonesia*, the Indonesian Insurance Board, insisted that

> The requirement set by the Ministry of Finance [to achieve the level of solvency at 120%] is a major problem for insurance companies. If we count accurately, most insurance companies will collapse because of the regulation. Thus, the regulators should be careful in reviewing annual reports submitted by insurance companies (My translation from Jawa Pos, a daily newspaper).

Apropos to the impact of external factors as the causes of negative performance, it is also interesting to consider a statement by a member of the Board of Commissioners at the 2004 Management Annual Meeting of *PT. ABTBK* conducted in Bogor, Jakarta on 24 February 2004:

> We are facing a serious problem...We have practised honest business, but our company performance was unfavourable. We have made a wrong conclusion on what we have done. We think that our performance was mainly due to bad luck [external factors]...To improve our performance we must be able to separate those with good conduct from those with bad conduct…My translation).

This statement obviously explains that blaming negative performance on external factors such as bad luck is not the culture of *PT. ABTBK*.

To conclude, it is clear that *PT. ABTBK* has used the necessary narrative texts in financial reporting. The texts are designed as argumentative language to tell the true story of historical performance of *PT. ABTBK.* There are no literary flourishes used to mislead audiences. Instead, *PT. ABTBK* has utilised argumentative texts in annual reports to persuade its audience that the company performance is determined by both internal and external forces.

Insight into the Company's Future

Besides telling a story about historical performance, corporate financial reporting is intended to tell a story about insights into the company's future, and how capable management is of coping with future challenges and threats. Consequently, management usually uses narrative texts in corporate financial reporting to deliver messages concerning risks, opportunities and threats faced by the company. In so doing, management considers internal and external forces that might affect the company's future.

The case of *PT. ABTBK* is an example of how management has used narrative texts to deliver messages regarding the company's future. This can be seen from the language it used to describe risks that it might face in conducting insurance business. In the 2003 annual report *PT. ABTBK* states an expression as follows:

> Natural disasters, such as floods and earthquakes, have occurred lately...even though

> sound underwriting policies have been accurately set....The possibility of losses and obligation to pay customer claims...due to such disaster will eventually influence company performance.
>
> Regulations require insurance companies to include a currency mismatch in the calculation of solvency... In the condition in which the value of Indonesian Rupiah tends to decrease such an inclusion can influence foreign exchange losses
>
> Macro-economic conditions and the stability of national security and politics are uncontrollable factors that might influence the performance of company investment.

The above quotations clearly show how *PT. ABTBK* explains external forces surrounding the insurance business, and how such forces might lead to the company's losses. Considering the language used in the annual reports, it can be seen that the above statements are intended to persuade the audience that *PT. ABTBK* is facing uncontrollable forces. Such statements show how *PT. ABTBK* uses language as a rhetorical device. However, in creating a rhetorical story about the company's future, management also delivers a message about strategies that will be employed to minimise such risks. For example, to minimise technical risks, *PT. ABTBK* has set in place a number of strategies, such as setting a sound reinsurance program and establishing a reinsurance committee. In the 2003 annual report it is claimed that:

> A reinsurance program plays a role in assisting the expansion of the company's risk insurance capacity. Through proper reinsurance programs, customer needs for insurance protection may be met...
>
> For the purpose of assisting management with the determination of reinsurance program, the Reinsurance Committee has been set up and assigned to conduct reviews of the current year's program and to determine the reinsurance programs for the following year.

Moreover, in the 2002 annual report *PT. ABTBK* included the following statements to show how it responds to the external forces.

> In response to these economic conditions...the company plans to:
>
> a. keep providing insurance protection in accordance with market demand, while maintaining prudent underwriting
> b. consolidate the company's operations in order to face global competition
> c. minimise operating expenses
> d. exert efforts to maintain the company's financial health according to the existing regulations.
>
> Recovery of economic conditions depends on the fiscal, monetary and other measures that have been and will be undertaken by the Indonesian Government, actions that are beyond the company's control. It is not possible to determine the future effects of the economic conditions on the company's liquidity and earnings, including the effects from its customers, stockholders, ceding companies and reinsurance companies.

These messages mean that even though *PT. ABTBK* faces a number of business risks, its management is capable of minimising such risks by enacting a proper strategy. In addition, in the 2003 annual report, it is claimed that

> ...for the last 14 years, *PT. Asuransi PT. ABTBK Tbk*, has provided dividends to the shareholders every year. In this turbulent year, we are apparently still able to uphold our commitment to distribute dividends.

Again, this statement shows that management of *PT. ABTBK* is capable of running an insurance business even though the business environment seems not to support the industry. A commitment to the distribution of dividends to its shareholders can be seen as an indication that the management of *PT. ABTBK* can be trusted. Within this context, the use of narrative texts in delivering emphatic messages provides a powerful signal of managerial competence.

The management competence in setting proper strategies will influence the extent to which management is able to build a company identity. As corporate identity refers to the "planned assembly of visual cues by which the audience can recognise the company and discriminate one company from another and which may be used to represent or symbolise the company" (Bernstein 1984), communication to promote a corporate identity is the purpose of corporate messages. Therefore, written communication is an important part of promoting a corporate identity and contributes to a company's reputation (Schmidt 1997).

The case of *PT. ABTBK* shows that the effectiveness of using narrative texts in constructing a rhetorical story for the purpose of communicating a corporate identity depends on the abilities of the key players to provide sound arguments and logical statements in the messages delivered to the company's audience. Finally, it is important to note that corporate culture and ethical conduct will greatly determine and shape the behaviour of management in constructing and delivering emphatic messages, through annual reports, to the audience.

CONCLUSION

The financial reporting practice of *PT. ABTBK* shows that it is intended to seek legitimacy in order to maintain social harmony. Social harmony is seen as the ultimate purpose of corporate financial reporting. In so doing, *PT. ABTBK* has designed corporate financial reporting as a rhetorical story to show fact that *PT. ABTBK*'s activities are in accordance with socially acceptable beliefs, norms, values and rules.

The management of *PT. ABTBK* also designs the covers of the annual reports with interesting pictures to represent the company's condition. This has been done to build an image of *PT. ABTBK* in the eyes of its stakeholders. Moreover, in delivering emphatic messages, *PT. ABTBK* has included narrative texts to provide arguments on either favourable or unfavourable performances. Narrative texts are also used to tell a story about an insight into the company's future and management's capability to cope with that future.

Thus, whatever the purpose of writing narrative texts, the case of *PT. ABTBK* illustrates that effective communication plays an important role in delivering messages to audiences. This is consistent with claims that regardless of the role of annual reports, as legal obligation (Flanagan 1993), a marketing tool (Rogers and Brown 1999) and an information piece (Kwon and Wild 1994), effective communication only occurs if messages intended by senders through annual reports are the same as those actually interpreted by the receivers (Courtis 1987).

Finally, as corporate financial reporting is a social construction involving cultural and institutional aspects; financial reporting practice in a company becomes a routine of constructing and delivering messages. Because routines are concerned with values shared by organisational members, beliefs, norms, values and rules are perceived as parts of financial reporting practice. Hence, how socially imposed norms, values and rules are internalised in a company will determine the behaviour of organisational actors in constructing an organisational reality through corporate financial reporting as a medium for delivering messages. Successful the institutionalisation of such values will greatly influence ethical conduct of actors, and will drive them to be committed to quality financial reporting practice. Consequently, further study should be directed to the relationship between financial reporting practice and organisational culture as well as institutionalisation of values, norms and beliefs in an organisation.

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APPENDIX
LIST OF QUESTIONS FOR INTERVIEWS

1. What do you know about financial reporting practice?
2. We have an annual report award competition for Indonesia companies, what do you think about the competition?
3. Could you tell me what is the importance of winning annual report awards for yourself and for your company?
4. I saw that the covers of annual reports of your company were designed using different pictures. Could you tell me why you put different pictures on the covers?
5. What do the pictures of annual reports mean? What about the caption?
6. We know that certain information is not required by regulations to be disclosed. Why did you voluntarily disclose some information especially narrative texts on the annual reports?
7. How important is the information for users of annual reports?
8. Do you believe that providing more information in annual reports can legitimate your company? Tell me more about this.
9. Why do your company requires your external auditor to put the name of its international accounting firm affiliation on the audit report?
10. In your opinion, could you tell me the importance of language in designing narrative text of annual reports?
11. Based on your experience in designing annual report, what is the criteria of good, transparant and reliable annual report?
12. How do you design your company annual report?
13. We know that some companies tend to manipulate information of their annual reports. What do you think about this issue?
14. The insurance industry is a highly regulated industry. Could you tell me how regulations affect you in designing annual reports when a certain authoritative body issues new accounting regulations?
15. How do you deal with the regulations?