6.1 INTRODUCTION

Accounting information helps the decision makers in making rational decisions. Accounting is measurement and communication of financial information about economic activities to interested persons. The users of accounting information can be internal users, viz. management or external users, viz. shareholders, debenture holders, financial institutions, security analysts, government, creditors, suppliers, and general public. The users primarily need information on the financial position of an enterprise, its performance from the ongoing and other activities and the changes in its financial position to assess the stability, profitability, liquidity, risk, and return, and the continuance of the enterprise. Thus the essence of accounting is in communication which is termed as disclosure or reporting.

Disclosure means reporting of quantitative and qualitative information of financial and non-financial nature regarding the reporting entity to outsiders for the purpose of their decision making. Disclosures help in empowering the investors with relevant information and are the heart of a securities market’s efficiency. Corporate disclosure as the total system of communication between the company and its interested constituents not only reports the progress and performance of a business enterprise but also demonstrates the credibility, accountability, and reliability of its working. The quality of disclosures made by corporate enterprise influences to a great extent the quality of investment decisions taken by investors, since availability of reliable and timely information helps them to assess the risk better and enables them to make rational investment decisions. Inadequate, incomplete, and unreliable information on the other hand fosters uncertainty, uncertainty creates risks which include investors as well as creditors to demand a higher rate or return and this in turn results in higher cost of capital and lower stock prices. On the other hand, good quality business reporting helps channelize capital to more
productive uses as well as results in better allocation of resources, thereby strengthening the market and economy as a whole.

The need for corporate information is universally felt. The divorce between ownership and management of corporate enterprise, the increasing complexity and size of organizations, the growing awareness of public and their keen interest in the affairs of companies, the changing socio-economic and political environment in the country, and greater emphasis on rational decision making contributed towards enhancing the need for and significance of information disclosed by the companies. Thus disclosure of information has a great significance in achieving accounting objectives and for this disclosure needs to be adequate. Adequate disclosure means full and fair disclosure so that it helps in rational decision making. Thus adequate disclosure relates particularly to objectives of relevancy, neutrality, completeness and understandability.

Information about the affairs of the company can be communicated through different media viz. prospectus, financial press releases, annual report, interim reports and personal contacts with company officials. In addition, newspapers, business and industry magazines, investment advisory services and government statistics also provide information about a company. Despite the existence of different sources of information, the annual report is regarded as the most important of information about a company’s affairs. Corporate annual reports represent the most easily accessible and extremely important source of basic information concerning an enterprise.

The banks are enjoying a dominant position in the Indian financial sector and they are not merely the economic entities, but are engines of economic growth and social transformation. The failure of a bank not only affects its own stakeholders, but also has a systematic impact on the stability of banking system as a whole. The rapid changes brought in by economic reforms and in innovation in financial products combined with technological advances, have an effect on increased risk on banking sector. Thus financial reporting of banking companies is important for several reasons. First, the rapid changes
brought out by economic reforms have exposed the Indian financial sectors in general and the banking sector in particular to the challenges of global banking business. Second, banking companies in India are also moving towards public participation and are coming up with their Initial public offerings and also raising funds through Global Depository Receipts and American Depository Receipts from abroad. Last, unlike other companies most of the funds used by banks to conduct the business belong to creditors, particularly to depositors. Thus, financial reporting norms for banks, assume pertinent importance in the present context. Banks must provide full, reliable, and high quality disclosures of their operations and risks in a timely fashion and must use prudent accounting policies.

The financial reporting and disclosure of banking companies in India are regulated by the Banking Regulation Act 1949, the Companies Act 1956, the rules of the Securities and Exchange Board of India, the guidelines of the Reserve Bank of India, the recommendations of the Institute of Chartered Accountants of India (ICAI) and the recommendations of the Basel Committee on Banking Supervision.

The Banking Regulation Act 1949 provides a frame work for regulation and supervision of commercial banking activity. Section 29(1) of the Banking Regulation Act 1949 states that at the expiration of each calendar year every banking company shall prepare a balance sheet and profit and loss account in the forms set out in the Third schedule Form A and Form B of the act respectively. Section 30(1) states that the balance sheet and profit and loss account should be prepared in accordance with Section 29 and audited by a person duly qualified under law. Section 31(1) also states that the accounts and balance sheet, together with the auditors report, shall be published in the prescribed manner and three copies thereof shall be furnished as returns to the RBI within three months from the end of the period. Section 32 requires that three copies of the accounts and balance sheet, together with the auditors report, should be sent to the registrar of Company Affairs. Section 217 of Indian Companies Act requires the preparation of report by the Board
of Directors of the company to be attached with the balance sheet. The section also specifies the particulars to be included in the boards report.

Section 35A of the Banking Regulation Act 1949, empowered the Reserve Bank of India to give directions to the Banking Companies whenever it deems fit and the banking companies shall be bound to comply with such directions. Thus the RBI provides a detailed guidance to banks in the matter of disclosures in the ‘Notes to Accounts’ to the Financial Statements. The notable contribution of SEBI in promoting healthy corporate disclosure in the country has been the introduction of clause 32 and 49 in the listing requirement of a stock exchange. As per clause 32 all the listed companies are required to give the cash flow statement in their annual reports. Clause 49 requires detailed information on the structure and the functioning of the board of directors and its various committees. Such information helps the investors in evaluating the quality of management of different banks.

ICAI is playing a very constructive role in regulating the corporate disclosure practices in India. Till date 32 accounting standards have been issued and banks are also required to comply with these standards. Finally, Basel Committee on Banking Supervision gave its recommendations as to how the banks and the supervisors are to evaluate properly the various risks that the banks can face. It based its study on three important pillars – minimum capital requirement, supervisory review process and market discipline. Thus as a consequence of several reforms brought about by various regulatory authorities over the years not only changed the information content of annual reports but also their presentation. The present study makes an attempt to evaluate the disclosure practices in annual reports of commercial banks in India and capture the changes that have occurred therein over the specified period.

6.2 NEED OF THE STUDY
The motivation for the research study came from several sources. A review of existing literature on the subject revealed that while numerous studies in India and abroad have been undertaken to evaluate the disclosure practices of
companies in their annual reports, yet no study of similar kind has been conducted specially for banks.

Financial disclosure is an effective communication of accounting information to its users for decision making. Fair reporting brings with its motivation, increased competitiveness, comparability and credence. Banks subsists on confidence and disclosure of prudent banking practices is the only way to build confidence. Banks have to foster the well being of shareholders and general public at large. Further the need of study was also felt because of growing importance of corporate governance in banks. The core of governance rests on the quality of transparency and disclosure. Another area which focuses on the need for present study is Basel II. Managing risk is increasingly becoming an important issue for the regulators and financial institutions. Basel II provides a list of desirable best practices for banking safety and efficiency. Thus there seems to be a little question concerning the need for serious research in the area of reporting practices of commercial banks.

6.3 OBJECTIVES

The objectives of the study were:
1. to examine the disclosure practices of commercial banks in India over the period of study;
2. to examine whether or not the growth of banking disclosures over the period of study is statistically significant;
3. to compare the disclosure practices of selected private sector banks and public sector banks;
4. to find out highly disclosed and least disclosed elements of banking disclosures;
5. to study the impact of selected corporate attributes, viz. size, age, ownership, quality of management, profitability of banks and capital adequacy ratio on the disclosure levels of the Indian commercial banks and;
6. to make suggestions for improving the quality of disclosure.
6.4 RESEARCH DESIGN

The sample of the study included all the 27 public sector banks and top 15 private sector banks working in India on the basis of market capitalization. The annual reports were collected for three financial years with a gap of five years in between, i.e., 1996-97, 2001-02 and 2006-07.

To evaluate the disclosure practices of banks in their annual reports, a benchmark in the form of ‘disclosure index’ was prepared for this study. The index was framed after giving due consideration to similar indexes used in previous studies, relevant provisions of the regulatory framework in India, as well as the opinion and advice of experts in the field. The final disclosure index constituted 226 items of information. These included 139 mandatory disclosure elements and 87 voluntary disclosure elements. This was an unweighted index.

The disclosure score for each bank was computed by evaluating its disclosure practices against the above mentioned index. Also, the percentage of total sample banks disclosing each item of information included in the index was determined. A comparison of the mean percentage of banks furnishing information under a specific disclosure head for the three years facilitated in identifying those disclosures which witnessed significant improvement in terms of an increase in the number of banks disclosing them.

To compare the disclosure levels of banks over the study period, a comparative analysis of the selected measures of central tendency and variation was conducted. To study the empirical relationship between selected corporate attributes, correlation analysis was carried out using the technique of zero-order correlation matrix. In order to study the impact of selected corporate attributes as independent factors on the disclosure score of bank as the dependent factor, multiple linear regression analysis technique was invoked, the results of which were interpreted by using the statistical tools of coefficient of determination, t-value, f-value and standard error of estimate etc.
6.5 FINDINGS OF THE STUDY

The disclosure practices of banks were studied under three broad heads:

- Bank-Wise Disclosure Practices
- Element-Wise Analysis of Banking Disclosures
- Impact of Bank Attributes on the Disclosure Practices

Following is the summary of results and findings of the empirical analysis as contained in the chapters of the present study:

6.5.1 Bank-Wise Disclosure Practices

Bank-wise overall and voluntary disclosure levels of 42 sample banks have been calculated using the index of banking disclosures. An effort has also been made to examine the difference, if, any in the disclosure levels of public and private sector banks. Growth in disclosure levels of all banks has also been found out. The results of the same are as follows:

6.5.1.1 Bank Wise Overall Disclosure Performance: This section deals with the bank-wise disclosure scores in 1996-97, 2001-02 and 2006-07. Results show that in 1996-97 out of 226 items of index of banking disclosure, only 81 items have been shown at maximum. In this year top banks on the basis of disclosure performance included Corporation Bank, Bank of India and Bank of Baroda. On the other side i.e. on bottom, Centurion Bank of Punjab, South Indian Bank and ICICI Bank have included the least number of items in their disclosure.

In 2001-02, the disclosure performance of almost all the banks found to be improved. Maximum disclosure score increased from 81 to 145. In this year, ICICI Bank, Corporation Bank and Oriental Bank of Commerce disclosed the maximum number of information elements in their annual reports. Bottom list included Development Credit Bank, United Commercial Bank and United Bank of India.

Finally in 2006-07, the disclosure performance of all the banks improved further. Maximum disclosed items reached to 173. Corporation Bank, Andhra
Bank and Allahabad Bank emerged as maximum disclosure level banks in this year. On the contrary, Punjab and Sind Bank, United Bank of India and State Bank of Patiala were on the bottom of the list.

A look on the disclosure scores of all the banks in all the three years can make it clear that Corporation Bank has remained among the top disclosing banks throughout this study. Some other banks like ICICI Bank and HDFC Bank showed a tremendous growth in disclosure levels after being on the bottom in the first year. However, some banks like Centurion Bank of Punjab, United Commercial Bank, Development Credit Bank and United Bank of India remained in the bottom list.

Paired sample z-test was applied to examine if the growth in disclosure performance of banks was significant or not in the three years of study. Results showed that z-value remained significant during all the three years of study. It may be interpreted that the level of disclosures of Indian banking industry has grown significantly during the period of study.

6.5.1.2 Bank Wise Voluntary Disclosure Performance: this section includes a brief discussion on the voluntary disclosures made by Indian banks in 1996-97, 2001-02 and 2006-07. In total 87 items were put in the voluntary disclosures in the index. Results show that in 1996-97, maximum number of voluntary disclosures made by any bank was 34 out of 87. Hence, the level of voluntary disclosure was very low in this period. Corporation Bank, IndusInd Bank and Bank of India disclosed maximum level of voluntary information in their disclosures. On the other hand, HDFC Bank, ICICI Bank and Bank of Rajasthan were on the bottom of the list.

In 2001-02 again the number of voluntary disclosures at maximum was 37 against a maximum of 34 in 1996-97. Hence, the growth of voluntary disclosures was not impressive during this period. ICICI Bank, Corporation Bank and State Bank of Bikaner and Jaipur were the banks disclosing maximum voluntary information in their annual reports. Towards the bottom of the list were Karnataka Bank, Development Credit Bank, Federal Bank and Indian Overseas Bank.
Finally in 2006-07 a tremendous growth in voluntary disclosures was witnessed. In this year, the maximum level of voluntary disclosures reached on all time high of 46. Corporation Bank, Andhra Bank and Kotak Mahindra Bank were the leaders of this growth. Bottom list in this period included Punjab and Sind Bank, Karur Vysya Bank and United Bank of India.

A look on the voluntary performance reveals that Corporation Bank has consistently disclosed high number of pieces of information in its annual reports while Karnataka Bank, United Commercial Bank and United Bank of India have remained among bottom banks.

Paired sample z- test revealed that the growth in voluntary disclosures of Indian banks has been significant in the analysis. From 1996-97 to 2001-02 and also from 2001-02 to 2006-07 the z-value showing growth in voluntary disclosure performance has been significant. So it may be interpreted that the voluntary disclosure performance of Indian banking industry is improving significantly.

### 6.5.1.3 Disclosure Performance of Public and Private Sector Banks:

Disclosure performance of public and private sector banks has been compared with the help of analysis of variance (ANOVA). Results show that the overall disclosure score of public sector banks was significantly higher than private sector banks in 1996-97. However, in 2001-02 and 2006-07 there was no significant difference in overall disclosures of public and private sector banks. Thus, it may be said that the overall disclosure performance of private sector banks in 1996-97 was not relatively impressive. But it improved a lot in 2001-02 and 2006-07.

When it comes to voluntary disclosures the results are different. In all the years of the study i.e. 1996-97, 2001-02 and 2006-07, the voluntary disclosure scores of public sector banks have been significantly higher than the private sector banks. Thus it may be concluded that disclosure performance of private banks improved but only for mandatory information.
For voluntary information, public sector banks are disclosing more significantly.

6.5.2 Element-Wise Disclosure Practices of Banks

This section covered the element wise disclosure analysis of Indian banks during the study. Results show that in mandatory disclosures the contents of balance sheet and profit and loss account were disclosed by all the banks. Hence the disclosure level was 100% in these categories. RBI guidelines and management discussion and analysis are also highly disclosed categories. However, growth has been rapid in case of RBI guidelines. Board’s report and mandatory corporate governance reports are somewhat low disclosed categories. Hence, board’s report and corporate governance report are the target areas where the disclosure can be increased.

In voluntary disclosure areas, minimum disclosure level was found in the categories like credit risk exposure, market risk exposure and interest rate risk exposure. Thus Indian banking industry is not very good in disclosures related to risks. A bank’s efficiency of investment planning is normally judged in terms of the risk involved in its investing decisions. As per prudential norms, banks should disclose maximum information on such topics. Thus, Indian banks should try to make more disclosures in these areas. However, banks are increasing disclosing information related to their employees, financials and general risk management which is really encouraging. Average level of disclosure has been found in the categories of key non financial statistics, corporate social disclosure, general corporate information and corporate governance. Thus disclosure can be improved by targeting at these areas.

6.5.3 Impact of Bank Attributes on the Disclosure Practices

Towards the end of analysis an exercise has been carried out to examine if certain bank attributes have any impact on disclosures. These attributes included age of the bank, ownership structure, size of the bank, profitability of the bank, capital adequacy ratio and quality of management. Dependent variables were overall disclosure score and voluntary disclosure score. Step-wise regression analysis was used to calculate the impact.
Results show that due to low correlation among attributes the regression models did not suffer from the problem of multicollinearity. Further, in 1996-97, three regression models were found under analysis. Quality of management was the most significant predictor of overall disclosure score followed by ownership and capital adequacy ratio respectively.

In case of voluntary disclosures in 1996-97 age came out to be the most significant predictor followed by quality of management and ownership. In 2001-02 two regression models were found for overall disclosures. Most significant predictor of overall disclosure was quality of management, followed by ownership. Results for voluntary disclosures in this year were significantly different when the most significant predictor was found to be ownership followed by quality of management.

Finally in 2006-07, again two regression models were available for overall disclosures. This time again, quality of management was the major predictor of overall disclosure followed by ownership. Results were same for voluntary disclosure in this year.

In brief, it may be stated that quality of management, ownership of banks and age of banks were by and large, the most significant predictors of both overall and voluntary disclosures.

Thus it can be summarized that there has been a growth of disclosures in all the Indian banks for both the overall and voluntary disclosures. Private sector banks are yet to disclose more information voluntarily whereas public sector banks are doing good and disclosing more. Though financial information is disclosed at good length in Indian banking annual reports, certain areas where more information can be disclosed includes risk related information and corporate governance. Finally, ownership of the bank, quality of management and age of the banks are the significant predictors of overall and voluntary disclosures made by banks.
6.6 SUGGESTIONS

Corporate disclosure practices of companies depend upon the philosophy that the management believe in; the legal and regulatory environment prevailing at the contemporary times; the practice followed by the competitors and the leading companies; the national and international imperatives for raising finance from the capital markets, and most important, mainly for voluntary nature of disclosures, the perceived advantage or disadvantage associated therewith. In the words of Ottoh Chang “while there is a thin line between corporate privacy and financial disclosures, competitive advantage has been used as an excuse for not disclosing the information relevant to investors and creditors. Ironically, information not disclosed in financial statements is available through other business intelligence sources” (Ottoh Chang, 2002). When some disclosure is not made as it is thought to be damaging, and the user gets information from other sources, the damage caused to the interests of the company is enhanced. In case, company itself provides such information with proper explanations, if any, the damage caused will definitely low. Transparency in business affairs pays in the long run, as the old saying goes ‘truth triumphs’.

As the banking companies in India are moving towards public participation and coming up with their IPOs, better quality of financial reporting will act as a catalyst to capitalize on their underlying strengths. Moreover, the economic environment at the global level is changing at a very fast pace and there is a need to change the quality of financial reporting accordingly. Keeping in view the emerging economic environment, the needs of various users of financial reporting of banks, some suggestions are being offered for the improvement of disclosure practices of banks:

1. The results of the study show that the level of disclosure of voluntary items is low and wide variation in disclosure score exits among various banking companies of public and private sector. It is therefore suggested that banking companies should report more of voluntary information in their annual reports like performance highlights, financial ratios, graphical presentation, corporate strategy and employee related
information. Higher disclosure will also help the present and potential investors along with other stakeholders in taking economic decisions.

2. Effective corporate governance is necessary for commercial banks if they have to grow and compete successfully in liberalized environment. Good governance can prove to be a powerful source of competitive advantage. Foundations of corporate governance are independence, disclosures and transparency, accountability and self-regulation. Thus disclosure of information by banking companies can be enhanced by targeting the area of corporate governance. Banks can focus on disclosing the information about the contact of CEO, background of senior managers, information on remuneration committee, information on half-yearly reports sent to shareholders and information on presentations made to institutional investors.

3. The guidelines on financial reporting issued by RBI and the ICAI should be followed in letter and spirit; these guidelines may or may not be mandatory, but these are definitely useful for the better presentation of information in the annual reports of banks. Banks do follow the mandatory guidelines but overlook the non-mandatory ones, which is not a good practice.

4. Managing risk is increasingly becoming an important issue for the regulators and financial institutions. Bank regulation is also now getting risk concentric. The results of the study suggest that banks should try to improve risk-related disclosures in the areas of credit risk, market risk and interest rate risk exposures.

5. The results show that quality of disclosure is affected by the quality of management and ownership structure of banks. Therefore, it is suggested that banks must focus on improving their quality of management which will further enhance the quality of disclosure.
6. The results also indicate significant growth in the disclosure level of banks over the study period and it is suggested that banks should keep up with this momentum in future also.

6.7 RECOMMENDATIONS FOR FUTURE RESEARCH

A research often acts as the fountain head from which ideas for future studies emanate. The following list enumerates some topics that have been identified for further research pertaining to subject matters related to the present study:

1. This study evaluates the disclosure practices of commercial banks in India. Similar study can be undertaken to study and analyze the disclosure practices of intra-country banks.

2. In the current study, unweighted disclosure index has been used. Hence, similar work can be further undertaken using the weighted disclosure indices where weights can be assigned after survey of experts, investors and account holders.

3. With the implementation of Basel II, a separate study keeping in view the Basel Norms can be conducted.