Chapter 1

Corporate Disclosure: An Overview

Modern economic development to a considerable extent depends on the availability of capital. In developing countries where the goal is to have rapid economic growth, capital is very essential to increase the output and the supply of economic goods for the benefit of members of society. The economic information should be available in such a form that these interested parties having diverse economic interests are capable of supporting their actions in a logical and rational manner. The most important aspect is the reporting of economic success or failure of the economic units that control and use the substantial portion of the scarce capital resources of the country. Therefore, if an economic society is to function effectively, it is essential that this reporting should be an adequate measure of economic performance. A company, which is an economic unit having impact on the individual and institutional investors and the national economy as a whole, should report to the various interested groups reflecting its efficiency in utilising the resources.

The accepted form of financial reporting is the annual report by the companies. This form is viewed as the best way in which the business activities for a specific period are exhibited. The most important components of the annual reports are the balance sheet, which depicts the financial position of the business at a specific point of time and the income statement which measures the performance of the organisation over a specific period of time. Balance sheet and income statement should fully, fairly and adequately meet the informational needs of the parties concerned.

1.1 Importance of Corporate Disclosure

Accounting operates in a socio economic environment as a 'service function'. When there is a drastic change in the political or economic system of the country, it is bound to change the objectives of accounting and
corporate disclosure. In developing countries, the movement toward a market oriented economy has necessitated a revision of financial reporting system. The emergence of joint stock companies together with the divorce of management and ownership has led to the increasing significance of corporate disclosure.

The wider recognition of social responsibility of business for the last few decades has important implications for corporate disclosure practices. This has emphasised the efficient allocation of society's resources and wealth. The concept of social responsibility has now become broader and includes employment generation, pollution control, civic amenities etc. Now, groups other than shareholders such as employees, local communities, social groups and the general public have interest in the accounting information. They are having vital influences on accounting and reporting.

Corporate Disclosure system provides reliable and relevant information to the interested parties for their decision making. Through disclosure requirements, a proper recording and classification of economic transactions of the business concern can be achieved. Thus, a fair picture of the business and the true results of its operations over a period of time are made available. The business future trends can be estimated with greater accuracy, if the financial reports are prepared in accordance with the rules and regulations of disclosure. Thus financial reports should include all the material information relevant for various interested groups for decision making.

1.2 Nature of Corporate Disclosure

The origin of contemporary financial accounting and reporting lies in the 15th century and the development of double entry record keeping by merchants to keep track of their business activities. The system was designed to provide information about economic resources, owners' investments, and obligations to creditors, as well as to measure the results of business transactions. Believing that a common measuring unit would greatly facilitate
the recording and communication process, the merchants selected the monetary unit as the most appropriate choice, because they thought about their investments and the results of their business operations in terms of cash. The system of measuring economic resources, obligations and activities in financial terms was the beginning of financial accounting and reporting.

Financial reporting aims to provide financial information about a business enterprise to various interested groups for decision making. In early times accounting was merely concerned with ascertainment of results of business. However with the divorce of ownership and management, the emphasis has shifted to show the effectiveness as well as the accountability of management team to manage the resources of the enterprise. Corporate disclosure is a vast, relative and indefinite process of providing fair and accurate information about the enterprise to the stakeholders. It covers all areas of financial reporting. Corporate disclosure is based on suitable accounting concepts, techniques and principles which lead to the presentation of clear and meaningful financial information. Thus it requires proper application of Generally Accepted Accounting Principles (GAAP) and accounting standards recommended by professional accounting bodies. Corporate disclosure is interrelated to law in the sense that it can not fulfil the demands of the interested groups if any rule or regulation of Companies Act is ignored.

Corporate disclosure practices are constantly evolving and are influenced by changes in the social, legal and economic environment. It influences capital formation and flow of funds and perform a vital role in the successful functioning of the economy.
1.3 Review of Literature

As the overall objective of the study is to analyse the disclosure practices of Indian companies, a review of concepts, findings and conclusions of the past studies relating to corporate disclosure or financial reporting is essential. A realistic presentation of the studies and research work carried out in the area of corporate disclosure is made to bring in the various points of view of the researchers. Review of literature also helps in identifying the methodology adopted by earlier researchers.

A large number of studies have been conducted in India and abroad covering different aspects of corporate disclosure through annual reports. These include descriptive, qualitative and empirical studies dealing with disclosure in annual report as a whole or covering specific aspects of disclosure, such as, disclosure of accounting policies, price level accounting, segment reporting, social reporting etc. This review has been divided into two parts. Part I deals with the review of the studies undertaken abroad and Part II deals with the analysis of studies conducted in India.

1.3.1 Studies Undertaken Abroad

The pioneer study on measuring corporate disclosure through index of disclosure has been conducted by Cerf (1961). He analysed the annual reports of 527 companies by applying an index of disclosure consisting of 31 items. Using a questionnaire, he asked the financial analysts to rate each item in the index as essential, desirable or of little consequence, to which he assigned weights ranging from 1 to 4. He computed the weighted disclosure score of the annual reports of all the 527 companies. Thereafter, he examined the association between extent of disclosure and the selected company characteristics - (i) asset size as measured by total assets; (ii) extent of ownership as measured by number of stock-holders; (iii) profitability as

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measured by the rate of return; and (iv) method of trading shares, i.e., whether the shares were traded on the New York Stock Exchange or in the Over the Counter (OTC) market. He concluded from his study that a positive relationship existed between the disclosure scores and asset size, number of stockholders and rate of return. A least square regression analysis was carried out by him to ascertain the combined effect of all independent variables on corporate disclosure. The regression results revealed that very little variation in disclosure scores could be explained by the four independent variables. The study also made some suggestions for improving disclosure of certain items like sales breakdown, capital expenditure (current and planned), research and development expenditure (current and planned), information on management, information on future outlook, and disclosure of accounting policies.

The study conducted by Cerf, being the first of its kind, is very significant in the literature on corporate disclosure. However, it has some limitations. Cerf did not include some important items such as changes in accounting policies, earning forecast, etc., in his index of disclosure. Moreover, his index of disclosure included some items of information, which may not be applicable to all companies of his study, but no explicit adjustment for this fact was made in his study.

Singhvi (1967)\(^2\) compared corporate disclosure through annual reports in India with that of United States, for the period 1964-1965 by using an index of disclosure consisting of 34 items. The sample consists of 155 US companies - 100 listed and 55 unlisted - and 45 listed Indian companies. The study noted that corporate management in general is less inclined to take the initiative in disclosing adequate information in the annual reports to stockholders, if disclosure is left to its discretion. He concluded that the disclosure of information in annual reports by the listed companies in India

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is less adequate and less investor-oriented as compared to listed companies in the U.S.A. The study remarked that most of the Indian companies disclose in their annual reports the information, which is required by the law, and the information, which is required by law falls short of what is desired by investors.

Copeland and Fredericks (1968)\(^3\) analysed the relationship between materiality of items and extent of disclosure. Their study consisted of selection of a variable, a measurement of its materiality and its disclosure, and a comparison of the two measures. The variable selected was 'changes in common stock outstanding' and the information was obtained from the listing applications. The study was based on a random sample of 200 New York Stock Exchange (NYSE) listing applications for 1964. After scanning the annual reports, they observed various reasons for listing subsequent issues of common stock, which were classified by them into eight categories. Certain items of information were specified for each category and the annual reports of the companies included in the listing application were scanned by them to know as to whether these items of information were disclosed there. They concluded that there was a positive relation between materiality and disclosure, i.e., more material factors are disclosed more fully. However, Copeland and Fredericks have admitted in their study that the 'conclusion drawn can at best, be tentative. Replication of the study and application of other techniques are needed to provide new evidence to support or negate our findings' (Copeland and Fredericks, p.113).

Singhvi and Desai (1971)\(^4\) studied the association between disclosure of certain informational items and the company characteristics, such as, asset size, number of stockholders, listing status, CPA firms, rate of return and earnings margin taking a sample of 100 listed and 55 unlisted US

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companies for the year 1965-66. They adopted the ‘index of disclosure’ used by Cerf (1961) in his study with minor modifications and their index contained 34 items. They classified the items of the index into four categories and accordingly assigned different weights ranging from 1 to 4, considering their relative importance as indicated by the various sub-committees of the ‘Committee on Corporate Information’ and the security analysts, who were interviewed. They applied ‘multivariate regression analysis, to find out the association between the selected company characteristics and disclosure. They concluded from their study that extent of disclosure was lower for unlisted companies and the disclosure was positively associated with total assets, number of shareholders, CPA firm, and earnings margin.

Carpenter, Francia and Strawser (1971)\(^5\) examined the perceptions of preparers, attesters and users on the current problem areas in financial reporting by selecting a random sample of 300 members each from the membership directories of the Institute of Chartered Financial Analysts, the American Institute of Certified Public Accountants, and the American Accounting Association. In order to obtain the views of management, Controllers of 500 largest industrial companies in the United States were selected. They developed a questionnaire consisting of four parts, i.e., (i) general considerations in financial reporting, (ii) current problems in financial reporting, (iii) proposals for improving financial reporting, and (iv) other considerations. They asked respondents to provide three ratings for: (a) How much information do you feel is now available to the users of financial statements with regard to an item? (What is the ‘current state of the art’?) (b) How much information do you feel should be available to the users of financial statements with regard to an item? (What should be the ‘current state of the art’?) (c) How important is this item?. The respondents

were asked to encircle a number from 1 to 7 on a rating scale, for each of the item included in the questionnaire. The amount of perceived deficiency for each of the item was calculated by subtracting the rating for part ‘a’ of an item (what is the current state of the art?) from part ‘b’ of an item (what should be the current state of the art?). They concluded that among the items listed in first part (general considerations in financial reporting) of the questionnaire, the ‘generally accepted accounting principles’ were the least deficient and the ‘timing of revenue recognition’ was the most deficient. In the case of ‘current problems in financial reporting’, ‘pension plans’ were the most deficient. The ‘proposals for improving financial reporting’, which consisted of eight items, were considered to be the most deficient of the four categories used in the study. ‘Effects of price-level changes’ from this category was ranked as the most deficient item. The ‘miscellaneous considerations’, which constituted the fourth category in the questionnaire, was considered as the least deficient of all categories.

Though this study highlighted certain important deficient areas of financial reporting, it suffers from the major limitation that the authors did not carry out the cross-sectional analysis of the responses of CPA’s, CFA’s, members of AAA and the Controllers, who represented the management. Obviously, if this had been done, the differences in perceptions of ‘different interested groups’ would have been known.

Chandra (1974) examined whether those who attest the corporate reports and those who use such reports, i.e., the public accountants and the security analysts respectively, have any consensus about the value of information included in the published corporate annual reports. Using a questionnaire containing 58 items of information, responses were obtained from the public accountants and security analysts on a five-point scale in order of its importance to them. The overall result of this study was that

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there was a lack of consensus between the accountants and the security analysts regarding the value of information disclosed in an annual report. The security analysts attached greater significance to the items of information than the accountants. The accountants generally do not value information for equity investment decisions the same way as security analysts do, although they tend to have equivalent value preferences in their dual role as preparers and users of information.

Buzby (1974) measured the disclosure of 39 selected informational items in the annual reports of 88 small and medium sized companies. He constructed a questionnaire containing 39 items of information and mailed it to 500 financial analysts to determine the relative importance of each item. He asked them to score each item on a five-point scale (4 to 0) i.e., 4 represented that the item was of great significance and 0 (zero) represented that the item was not at all significant. Mean scores were calculated for each item, these scores were used to study the extent of disclosure in the annual reports. It was found that the correlation between the relative importance of the items and their extent of disclosure was small. The author, on the basis of this study, concluded that the companies should give due consideration to information needs of the users of financial statements while deciding on the items to be included in the annual reports. The study observed that there existed a case for expansion in the extent of disclosure in the annual reports of small and medium sized companies.

In an extension of his study, Buzby (1975) examined the association between the extent of disclosure in annual reports and two company characteristics – asset size and listing status. He used the scores assigned by the security analysts to 39 items of information for calculating the relative disclosure for each of the 88 companies of the sample. The results showed

that the extent of disclosure was not affected by the listing status of the companies. This study has some limitations, which have been admitted by Buzby also in his work. Firstly, to determine the relative importance of items, the financial analysts were asked to rate each item in order of their significance. It may be pointed out that financial analysts alone may not give the true value of the items of information, as the annual reports are also used by individual shareholders, who may not use the services of financial analysts. Secondly, the statistical tests used depended in part upon the assumption that sampling was random. In the opinion of Buzby himself the annual report was not strictly random.

Barret (1976)\(^9\) analysed the extent of overall disclosure and the degree of comprehensiveness of firms' financial statements as reflected in the annual reports of 103 large companies in seven different countries selected on the basis of market capitalisation in 1973. The data for the study were collected for the years 1963 to 1972 for fifteen companies each from six countries - United States, Japan, United Kingdom, France, Germany and Sweden- and thirteen companies from the Netherlands. The overall extent and quality of financial disclosure was measured with reference to 17 categories using a weighted index scoring system. The study concluded that while the overall level of corporate financial disclosure steadily improved throughout 1963 to 1972, there was still a wide variance between the overall level of disclosure of American and British companies on one hand and the companies from other five countries. The American and the British firm's financial statements were considerably more comprehensive in terms of including the results of related companies and of taking a broad view of income related items than were those of the firms located in other five countries. The French companies, on the other hand, were found having both less disclosure and less comprehensive financial statements than the firms in

other six countries. Although this study may be considered as a significant contribution in studying inter-country financial reporting, it suffers from certain limitations. The index of disclosure used in the study was not very comprehensive. Also, the mode of assigning weights to various items has not been very scientific because investors in different countries may not assign equal weights to the different items of information.

Firth (1979a)\textsuperscript{10} studied the impact of size, stock market listing and auditors' firm size on voluntary disclosure in corporate annual reports. He included 48 items of information in his index, none of them were required by the law to be disclosed in the annual report. He mailed the index to 120 financial analysts working for stockbrokers and investment institutions, asking them to rate each item of information on a five-point scale in order of its relative importance. The weighted index was applied to the annual reports of three samples of companies and a disclosure index was calculated for each company. These samples consisted of 40 companies with no stock exchange listing, 40 stock exchange listed companies paired with the unlisted companies on the basis of size and industry, and 100 stock exchange listed companies. The association between size of the company and extent of disclosure was measured by Kendall's rank correlation co-efficient for each of the three groups of companies. For measuring the association of share listing and auditors' firm size with the extent of disclosure, standard t-test was applied. He concluded that both the size of the company (measured by sales turnover and capital employed) and stock market listing were related to the extent of disclosure, but auditors' firm size had no impact on disclosure.

Firth (1979b)\textsuperscript{11} explored the association between the actual and desired voluntary disclosures in the annual reports of 100 British listed companies. Actual disclosure on 48 informational items was measured in terms of mean reporting on each in the annual reports and the desired


\textsuperscript{11} M. Firth. (1979b). The disclosure of information by the companies. \textit{Omega}, 7(2), 273-280.
reporting was computed in terms of the mean importance weights assigned by 120 financial analysts and representatives of investment institutions on a five point scale. The study concluded that there is little association between the relative importance of the informational items and their actual disclosure. Also, there is a growing demand for increasing the amount of disclosures through the corporate annual reports. However, British companies were disclosing more information than statutorily required under the legislations.

Ingram and Frazier (1980)\textsuperscript{12} examined the relationship between measures of firm's environmental performance and the environmental disclosures contained in the firm's annual reports. The environmental performance was measured using indices of firm's performance devised by the Council on Economic Priorities (CEP) [1977]. Content analysis was used to measure the content of each firm's environmental disclosures. The study was conducted by using annual reports of 40 firms containing environmental disclosures. Product moment correlation was applied to ascertain the relationship between firm's environmental performance (CEP index scores) and the content of the firm's environmental disclosure (content analysis scores). The study revealed a weak positive correlation (between content and performance) for all categories except litigation, which is negative and also weak. It was also revealed that, on average, the poorer performers made slightly more disclosures than the better performers in all categories except litigation.

McNally, Eng and Hasseldine (1982)\textsuperscript{13} focused on three aspects of the discretionary disclosure of financial and non-financial information in the annual reports of 103 manufacturing companies listed on the New Zealand stock exchange. These were: (a) the importance of items to be disclosed in


annual reports, as perceived by the financial editors and the stock exchange members; (b) the disclosure practices of manufacturing companies vis-a-vis perceptions of external decision-makers; and (c) examining the possible association between the disclosure practices and selected company characteristics such as size, rate of return, growth and auditors. Using a questionnaire consisting of 41 informational items, the authors of this study asked the financial editors and members of the stock exchange to assign weights ranging from 1 to 5 to each item in order of its relative importance to them. Applying mean responses as weights, weighted disclosure scores were computed for the 103 companies. The study revealed that the level of actual disclosure by companies was lower than what the professional external users perceived to be desirable and there was a considerable variation across the 41 items in the degree of non-disclosure. They concluded that a positive relationship existed between size and both the number of items disclosed and the average score for each company. Neither of the other three characteristics, viz., rate of return, growth and auditors were significantly related to the measure of actual company disclosure. This study is very significant as it considers the influence of ‘growth of the company’ on the disclosure score, which has not been considered in other studies.

Marston (1986)\textsuperscript{14} compared the financial reporting practices of Indian and British companies. He analysed the annual reports of 30 large Indian companies applying the ‘Index of Disclosure’ developed by Barret (1976) consisting of 17 items. The disclosure in the United Kingdom and India was compared on an item-by-item basis using the result of the surveys of the Institute of Chartered Accountants in England and Wales (ICAEW). On the basis of this study, Marston concluded that, while relatively higher disclosure of an item by the Indian companies was attributed to the more stringent legal environment, better disclosure of an item by British

\textsuperscript{14} C. Marston. (1986). \textit{Financial reporting in India}. London: Croom Helm.
companies was mainly due to the existence of an accounting standard in excess of legal requirements. Moreover, the overall disclosures in the United Kingdom was greater than in India. This study, however, suffers from certain limitations. First, the index of disclosure used in this study was not only a decade old but was also non-comprehensive. Second, the author has compared his own survey of the annual reports of the 30 Indian Companies with the survey conducted by the ICAEW, Britain. All the 17 items considered by Marston might not have been covered by the ICAEW survey.

Chow and Wong-Boren (1987)\textsuperscript{15} made an attempt to know the voluntary financial disclosure practices of 52 listed Mexican Corporations and whether the extent of disclosure was related to firm's size, financial leverage and the proportion of the assets in place. Using a questionnaire consisting of 24 informational items, he asked 106 loan officers of 16 Mexican Banks to indicate on a seven point scale, the importance they placed to each item in evaluating an average loan application. In the study, both the weighted and unweighted disclosure scores were measured and it was shown that the correlation between the two scores was statistically significant. The study concluded that the extent of disclosure was significantly associated only with the size variable. This study differs from the other studies that it has considered both the weighted and the unweighted scores in analysing the disclosure practices of companies in a non-Anglo-American country. However, it has some limitations. First, the authors asked the bank officers to give weights to various items of information. They have not considered the prime users of the annual reports, i.e., the shareholders, for this purpose. There may be difference in the importance of the items of information as perceived by shareholders and the bank officers. Second, their index of disclosure was not very comprehensive; the authors have not considered even the price level adjusted statements, human resource

accounting, social accounting, etc. which are much discussed issues in corporate reporting.

Cooke (1992)\textsuperscript{16} examined the association between the level of disclosure and three corporate attributes – size, listing status and nature of industry- for 35 Japanese companies. He constructed an index of disclosure consisting of 165 items, which consisted of both statutory and voluntary items of information. He analysed the disclosure levels of Japanese companies using the annual reports of companies for the year 1988. This study was a unique one in the sense that the size of the company was measured in terms of a composite variable i.e., a linear combination of eight alternate indicators of size – capital stock, turnover, number of shareholders, total assets, current assets, fixed assets, shareholders funds and bank borrowings. He concluded that the extent of disclosure was positively and significantly associated with all the three explanatory variables – size, listing status and nature of industry.

Hackston and Milne (1996)\textsuperscript{17} analysed social and environmental disclosure practices of the 47 'top' listed New Zealand companies for the year 1992. Besides identifying certain determinants of the extent of disclosure, they examined the disclosure practices in an international context. In this study, the method accepted for measuring disclosure was content analysis in terms of page amount and the number of sentences. The study concluded that both measures of the amount of disclosure were highly correlated. Also size, market capitalisation and total assets and industry were significantly associated with the amount of social and environmental disclosures. But both current and lagged profitability-return on assets and return on equity - were not significantly associated with disclosures. The


\textsuperscript{17} D. Hackston., & M. J. Milne. (1996). Some determinants of social and environmental disclosures in New Zealand companies. \textit{Accounting, Auditing & Accountability Journal}, 9(1), 77-108.
study provided some evidence that New Zealand companies with dual (overseas) stock exchange listings were reporting more information on their social and environmental performance.

**Ahmed and Courtis (1999)** performed a meta-analysis on the 29 studies that had analysed associations between the corporate attributes and disclosures through the annual reports since the year 1961. The main objective of this study was to identify the underlying factors that could have moderated the apparent variation in the results reported in the past studies. The study observed that the findings in the past studies had consistently shown that size and listing status are significantly associated with the extent of disclosure, and that results had been inconsistent for leverage, profitability and size of the audit firm. The analysis confirmed significant and positive relationships between disclosure levels and corporate size, listing status and leverage. However, no significant association was found between the aggregated disclosure levels and corporate profitability, or audit firm size. The study attributed the reasons for differences in research findings to sampling error, differences in the construction of index of disclosure and variations in the definitions of the explanatory variables.

**Barako, Hancock and Izan (2006)** conducted a study on the factors influencing the voluntary corporate disclosures by 43 companies in Kenya for the period 1992 to 2001. They performed a longitudinal analysis on the voluntary disclosure practices in the annual reports of sample companies listed in Nairobi stock exchange. The study investigated the extent to which corporate governance attributes, ownership structure, and company characteristics influence the voluntary disclosure practices. The study found out that there was an increase in the extent to voluntary disclosure.

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disclosures over the sample period of ten years. Results of the study also showed the existence of a relationship between the level of voluntary disclosures and corporate governance attributes, ownership structure, and company characteristics. It was also found that large companies and companies with high debt, were disclosing more voluntary information. However, board leadership structure, liquidity, profitability and type of external audit firm were not found having a significant influence on the level of voluntary disclosure in corporate annual reports of Kenya.

1.3.2 Studies Conducted in India

Shankar (1972)\textsuperscript{20} conducted a study to examine the adequacy of corporate reporting in the Indian annual reports, as compared to the annual reports of foreign countries, such as, USA, Germany, UK and Japan. He selected 50 Indian and 25 foreign companies for the purpose of this study. He identified seven 'interested groups', viz., shareholders (institutional and individual), investors (prospective), public, creditors, government, employees and the consumers as the main users of the annual reports and developed an index of disclosure consisting of 24 relevant items of information for these groups. On the basis of this study, he concluded that, 'the Indian balance sheet is the least innovative and informative and is prepared largely within the legal framework'. The foreign annual reports are much informative and illustrative. The Indian annual reports were lagging behind their foreign counterparts with respect to the disclosure of items such as corporate objectives and policies, corporate-governance relations, information about employees and marketing operations. The study termed the Indian annual reports, as 'artificial and discontinuous' and stressed the role that shareholders and accounting profession could play in improving them.

Shankar’s study can be considered to be of great significance in the Indian context, as it has suggested the measures of improving the disclosure in the Indian annual reports. However, it suffers from the following limitations. The list of the items considered in the study is not very comprehensive. Some important items of information such as accounting policies, statistical information for the past, strengths and weaknesses of the companies during the year, amount incurred on human resources and price level accounting, etc. have been ignored. Moreover, certain items included in the list, such as ‘information about employees’ and ‘investment details’, etc, were too general and not very specific.

Dasgupta (1977)\(^\text{21}\) has critically analysed the financial reporting practices prevalent in India. The author has also reviewed the financial reporting requirements in foreign countries, such as, USA, Australia, UK, France, Japan, etc. He has suggested that the ‘statement of highlights’, ‘summarised balance sheet and profit and loss account’, ‘narrative statements’, ‘statement of sources and application of funds’, ‘statistical records’, ‘diagrams and charts’, and ‘inflation adjusted statements’ should be included in the annual reports so as to make these reports more informative and to serve the increasing needs of their users. Unlike other studies conducted on disclosure in foreign countries, the author has not analysed the annual reports using an ‘index of disclosure’, instead, he has laid greater emphasis on the review of the legal framework on disclosure in India and other countries, exposure drafts and statements issued by the professional accounting bodies in UK and USA and the accounting standards issued by the ‘International Accounting Standards Committee’ (IASC).

Singh and Gupta (1977)\(^\text{22}\) explored the relationship between the quality of disclosure and seven organisational correlates. The organisational correlates considered by them were age of the company, earnings margin, rate


of return, size of the company as measured by total assets and net sales, number of shareholders, size of the auditing firm and the ownership pattern of the companies. The authors prepared an index of disclosure consisting of 32 important items, which were assigned weights ranging from 1 to 3 in order of their importance as perceived by the investigators. The weighted index of disclosure was applied to annual reports of 22 companies in the private sector and six companies in the public sector to know the quality of disclosure in the annual reports of these companies. On the basis of the findings of their study, Singh and Gupta concluded that the public sector companies were disclosing more information than the private sector companies. Also, the level of disclosure was significantly associated with the number of shareholders, age and ownership pattern of companies.

**Singh and Bhargava (1978)**\(^{23}\) examined the disclosure of financial and non-financial information in annual reports of 40 public sector enterprises on the basis of index of disclosure consisting 35 items. They also analysed the relationship between the quality of disclosure and organisational pattern and nature of industry. The findings of the study indicated that there were significant cross sectional differences in the disclosure of information by sample companies. Based on the analysis, the study inferred that the organisational pattern did not have any impact on the quality of disclosure of information, whereas the nature of industry did influence it.

**Seshan and Gujrathi (1980)**\(^{24}\) carried out a survey of the financial reporting practices followed by 200 public limited companies in India. They laid emphasis on studying the form and contents of the balance sheet, profit and loss account, auditors' report and directors' report of the sample companies, and disclosure of information such as accounting policies, supplementary financial statements including the statement of changes in

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financial position, inflation adjusted statements, consolidated financial statements, historical summaries of the financial information, disposition of gross earnings and highlights of year’s operations. Based on the analysis, the authors concluded that many companies were not disclosing the accounting policies and the supplementary financial statements in their annual reports and laid emphasis on the inclusion of these statements in the annual reports.

Lal (1985)\textsuperscript{25} examined the disclosure practices of 180 manufacturing companies in the private sector for the years 1965 and 1975. The study also made an attempt to examine the impact of four company characteristics, viz., asset size, earnings margin, nature of industry and the association with a large industrial house, on the quality of disclosure. Using an index of disclosure consisting of 50 items of information (104 items in all, with all possible sub-items) were constructed for measuring the extent of disclosure in the annual reports of selected companies. The study concluded that the extent of disclosure in the annual reports of companies had improved in 1975 over 1965. The regression results revealed positive associations between the extent of disclosure and size of the company (as measured by assets), earnings margin, nature of industry and the association with a large industrial house. However, the ‘size of the company’ possessed a better association with the extent of disclosure than the other three variables.

The Research Committee of the Institute of Chartered Accountants of India (1985)\textsuperscript{26} surveyed the published accounts of 87 private sector companies and 25 public sector companies to highlight the financial reporting practices being followed by them. This study is similar to study conducted by Seshan and Gujrathi (1980). The study reported that though all companies disclosed the minimum information required by the Companies Act to be disclosed, however, there were noticeable differences in the pattern


\textsuperscript{26} Institute of Chartered Accountants of India (ICAI). (1985). \textit{Trends in published accounts.} New Delhi : ICAI.
of disclosing this information among the different companies. A few companies particularly in the public sector, disclosed information about funds flow, accounting policy, value-added, inflation accounting, human resources accounting and social activities. The study concluded that the companies in the public sector provided much more information than those in the private sector. Also, the study concluded that public sector companies were leading in tackling those problems and questions in accounting that had so far defied definite solutions.

Chander (1992)\textsuperscript{27} had made a comprehensive study of corporate reporting practices of public and private sector companies in India. The extent of disclosure has been measured both in terms of item wise disclosure and company wise disclosure by applying the ‘index of disclosure’ to the annual reports of selected public and private sector giants for the years 1980-81 to 1984-85. He studied top 50 companies from public and private sectors selected on the basis of a survey conducted by the research bureau of ‘The Economic Times.’ Index of disclosure consists of 92 items for public sector and 98 for private sector companies. He studied the association between company attributes and disclosure, the timeliness of financial statements and disclosure of some of the contemporary issues like price level accounting, Human Resource Accounting, Corporate social reporting, Segment reporting, Accounting Standards etc.

The study concluded that the quality of disclosure is significantly better in case of public sector giants as compared to the private sector. Also, there is significant association between size of a company, age, profitability, industry in which a company belongs and the disclosure status. In addition, the public sector companies take comparatively greater time in finalising their annual accounts.

Atieq and Agrawal (1994) studied the extent to which the balance sheet and the profit and loss statements reflect the truth and fairness and whether such statements fulfill the readers’ decision needs. For this purpose, an index of disclosure consisting of 148 items divided into 16 groups was formulated. The study was confined to the 16 companies of the cement industry in India during the period 1989-91. They calculated the item wise disclosure score by dividing the number of companies which actually disclosed the item by the maximum number of companies, which are supposed to disclose the very same item. They concluded that Balance sheet and Income statements included in the annual reports do not truly and fairly present the state of affairs and the performance results of company and user needs are not fulfilled. However the study has some limitations as they themselves quoted in the paper. It used a small sample of companies and the index of disclosure was not a comprehensive one.

Eresi (1996) studied the forms and extent of disclosure of information on environment in the annual reports of companies. He examined whether the companies are environmentally sensitive and environmental awareness of many companies as expressed in different statements is translated into specific action programmes. For this, he studied the annual reports of 68 companies belonging to different industries selected at random for the years 1991-92 and 92-93. The study concluded that only 30% of sample companies have disclosed environmental information (EI) and environmentally sensitive companies shared only positive information. Also, companies disclosed information only with regard to protection of environment, pollution control, conservation of energy and raw-materials. They ignored more serious environmental issues like waste generation, water

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wastage, recycling of wastes, odour, noise nuisance etc. The study has the limitation that it confines itself only to a small number of companies.

Rathinam (1996) has made a comprehensive study about disclosure practices of Indian companies. Using an index of disclosure consisting of 114 items, he measured the disclosure of statutory and voluntary items of information in the annual reports of 160 companies – 146 private sector and 14 public sector companies. He also examined the relationship between various corporate attributes and disclosure, and analysed disclosure practices of companies regarding certain contemporary issues in financial reporting like Social Responsibility Accounting, Human Resource Accounting, Value Added Statement etc. Thereafter, he collected data from three user groups – corporate executives, corporate auditors and investors through 3 sets of questionnaires. The study revealed that companies give more emphasis on the disclosure of statutory information. The voluntary information is not given significant attention by the companies. The special statements like HRA, VAS and SRA are not found to present except in a few cases. Companies, which belong to different age, profitability, asset size, turnover and existence of collaboration, have different disclosure scores.

Ubha (2001) examined the annual reports of 50 selected companies for the period 1989-90 to 1993-94 to find out the general disclosure trends and practices prevalent in the corporate sector in India. He studied the information contents of financial statements and the item wise disclosure was examined by using an index of disclosure. To highlight the relative importance of the various items of information contained in the annual reports, he collected data from 232 investors having different educational qualifications and investment experience. He concluded that all the sample companies disclosed statutory items of information even though there are certain differences in the

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presentation of items. Further there are many items which are considered ‘highly useful’ and ‘useful’ by the investors but are overlooked by the companies. He suggested that if financial reporting is to be really useful for the society, it must provide really useful, relevant, reliable, timely and transparent information about its various events and actions.

Banerjee (2005)\(^{32}\) analysed environmental accounting and reporting practices of 60 companies for the financial year 2002-03. Based on the findings, the study concluded that disclosure of environmental information was not significant with only a few companies showing their awareness to disclose quantitative information voluntarily. Also there is an improvement in the environmental disclosures by the companies over time and there were hardly any disclosures on environmental auditing.

Nangia (2005)\(^{33}\) examined the disclosure practices of MNCs operating in India as against domestic companies by taking a sample of ten MNCs and ten domestic companies for a period of ten years from 1992 to 2001. She studied the association between the extent of disclosure and certain company characteristics like size, profitability and type of industry. She constructed an index of disclosure consisting of 106 items of information. She collected responses from the users of annual reports by adopting the method of questionnaire based personal interview to study the perceived difference about the importance of items between the preparers and users of annual reports. Results indicated that mean disclosure by domestic companies is higher than that of multinational companies. Also, there is a lack of consensus between the perceptions of preparers and users of annual reports. She found that while there is no association between the extent of disclosure and size and profitability of companies in both groups, type of industry has a significant association with the extent of disclosure.

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Vasal (2006)\(^{34}\) examined the quality of corporate financial reporting by drawing a sample from the Central Public Sector Companies (CPSCs) for a period of four years from 1988 to 1991. He analysed the corporate reporting under three major heads – extended corporate reporting, extended financial reporting and extended social reporting. Applying an index of disclosure consisting of 65 non statutory items, he measured the level and variability of disclosure- both weighted and unweighted scores- of 129 CPSCs. To analyse the relevance of informational items in evaluating corporate performance, he collected responses from 69 users and 65 prepares of annual reports on a 5-point scale by using a questionnaire. His major findings were - disclosure on extended financial reporting items is higher than disclosure on extended social reporting items and disclosure had a tendency to rise over the sample period. Further size, age, profitability, review of accounts and industry were found as significant determinants of corporate reporting in all the sample years. It is also found that actual disclosures on the information items were not in harmony with the relative importance of the items to the users of annual reports.

The review of the empirical studies on corporate disclosure brought to light some of the research findings pertinent to the current research. There are enough grounds to believe that no comprehensive study has been conducted in India to examine the disclosure practices of the companies. Moreover, the conclusion drawn by these studies do not remain much relevant now-a-days when the subject of ‘corporate disclosure’ has caught much attention of the corporate sector, professional bodies and the users of the annual reports. The present study is an attempt to analyse the disclosure practices of the selected Indian companies for a period of three years.

1.4 Operational Definitions of the terms used in the study

The title of the study is ‘Corporate disclosure by Indian companies’. The operational definitions of the different terms used in the study are:

**Indian Company:** An Indian company means a company formed and registered under the Indian Companies Act, 1956. Indian Companies Act, 1956 defines a company as “a company formed and registered under the Indian Companies Act or an existing company”. For the purpose of the study, Indian company includes domestic companies and MNC associates operating in India.

**Corporate Disclosure:** Corporate disclosure is defined as reporting of qualitative and quantitative information of financial and non financial nature regarding the reporting entity to outsiders for the purpose of their analysis and decision-making. For the purpose of the study corporate disclosure through published annual reports is examined.

**Mandatory Disclosure:** Disclosures made in accordance with the relevant regulatory framework of a country are termed as mandatory disclosures. In India mandatory disclosures are as required by the Companies Act 1956, the mandatory accounting standards issued by ICAI and the listing agreement with the stock exchanges.

**Voluntary Disclosure:** Disclosures made over and above the mandatory minimum are referred to as voluntary disclosure. They are disclosed purely at the company’s discretion to provide accounting and other information deemed relevant to the decision needs of users of their annual reports.

Corporate disclosure is a broad area consisting of mandatory and voluntary disclosures about a company and its operations. A thorough understanding of the conceptual and regulatory framework of corporate disclosure is essential before going for analysing the disclosure practices of Indian companies. The conceptual framework of corporate disclosure is
intended to be a collection of fundamental concepts on which accounting and reporting standards are based.

The researcher has made an attempt to study the conceptual and regulatory framework of corporate disclosure in the next chapter.
Chapter 2

Conceptual and Regulatory Framework of CorporateDisclosure