FINANCIAL REPORTING PRACTICES IN COMMERCIAL BANKS IN INDIA - A COMPARATIVE STUDY

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Abstract - Today banks are not merely financial institutions instead their role has changed considerably with the passage of time. The modern economy is now dependent on banks and their services in order to grow. In India banking sector has undergone series of transformation after independence from being a lending institution to being the fulcrum of our economy. They have the surplus resources from all the sectors and they channelize them into the deficit sectors. Thus there comes a need to disclose their operational information to satisfy the information needs of the users. This research paper will try to highlight the current scenario of disclosure practices in the banking sector and also do a comparative study of the disclosure practices of public and private sector banks.

Keywords - Disclosure, Transparency, Corporate Governance, Stewardship Information, Financial Reporting

I. INTRODUCTION

Every economy is dependent on correct and efficient information system. Banks are the backbone of any economy. So, there's a special significance of disclosure practices of commercial banks in India. The modern accounting is not merely concerned with record keeping but with a range of activities involving planning, control, decision making, problem solving, performance measurement and evolution, directing, coordinating, auditing, tax management and planning, cost and management accounting. The concept of Financial Reporting has gained much importance due to increase in company form of organization, increased competition and increase in the information needs of the users.

Financial Reporting means communication of financial statements and related information by the business enterprise to the concerning parties (internal as well as external users). Financial soundness and profitability of a business enterprise can be examined and analyzed with the financial position as disclosed in its annual accounts. Annual Reports are the most comprehensive means of communication by the business enterprise to its various stakeholders. Investors will prefer to invest in a company that makes full disclosure. In India, the regulation of the financial system is done by the Reserve Bank of India which implements various rules and regulations to regulate the working of banks.

II. IMPORTANCE OF STUDY

Financial disclosure is an effective communication of accounting information to its users for decision making. The users of financial statements should be in a position to evaluate and assess the company's earnings performance and financial position, so that, they are able to make intelligent investment decisions necessary for efficient allocation of scarce resources. The aim of financial disclosure is to portray economic performance of an enterprise. Financial information can be disclosed by using various modes, but annual reports occupy a very significant position among them. Today there is general acceptance of the value of fair reporting in the business community. Fair reporting brings with it motivation, increased competitiveness, comparability and credence.

Banks are also business entities, i.e. they produce and sell financial services instead of products. The distinctive feature about banks is that they are highly leveraged firms. They have to foster the well-being of shareholders and general public at large. The essential part of the banking system is its financial viability. It is not only necessary for its survival but also to discharge its various obligations. Banks subsists on confidence and disclosure of prudent banking practices is the only way to build confidence. Further the need of the study was felt because of growing importance of **corporate governance** in banks. Governance is a reform package to strengthen the banks and corporate with the objective of making them more accountable, open, transparent, democratic and participatory. Governance in banks is considerably a more complex issue than in other sectors because bank activities are less transparent and thus it is more difficult for shareholders and creditors to monitor their activities.

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. Bank regulation is now increasingly getting risk concentric. This process had its origin in Basel I proposals in 1988. The thrust of first accord was adequate capitalization of banks in relation to credit risk, the second accord recognizes that banks face a number of risks in the form of credit, market and operational risk. Basel II is built around three pillars –

minimum capital requirement, supervisory review and market discipline. Pillar three provides a comprehensive menu of public and regulatory disclosures related to capital structure, capital adequacy, risk assessment and risk management process to enhance transparency in banking operations.

Thus, Basel II provides a list of desirable best practices for banking safety and efficiency. Protecting the interest of the depositors becomes a matter of paramount importance to banks. Regulators, the world over, have recognized the vulnerability of depositors to the whims of managerial misadventures in banks and therefore have been regulating the banks more tightly than other corporate. Thus there seems to be a little question concerning the need for serious research in the area of reporting practices of commercial banks.

III. LITERATURE REVIEW

Copeland and Fredericks (1968) examined the relation between materiality and disclosure with aggregate data from 200 companies and found a positive correlation between materiality and disclosure.

Singhvi and Desai (1971) *undertook* an empirical analysis of the quality of corporate financial disclosures in annual reports of 100 listed and 55 unlisted American corporations for the year 1965-66 and concluded the quality of disclosure was one of the variables affecting the price of a security.

Baker and Haslem (1973) examined the information needs of individual investors in common stock. They further concluded that investors made investment decisions on the basis of expectations of future economic outlook of the company and industry, earnings and sales forecast and the quality of management. The study also revealed that individual investors had information needs different from the professional analysts. They considered stock brokers followed by advisory services and newspapers as important source of corporate information, while attaching minor importance to financial statements in annual reports.

IV. OBJECTIVES OF THE STUDY

1. To examine the disclosure practices of commercial banks in India over the period of study.
2. To compare the disclosure practices of selected private sector banks with the public sector banks.
3. To find out highly disclosed and least disclosed elements of banking disclosures.
4. To examine the discriminatory power of total, mandatory and voluntary disclosures in relation to public and private sector banks.
5. To make suggestions for improving the quality of disclosure.

V. HYPOTHESIS

1. Ho (1): There are no significant differences in the disclosure practices of public sector banks and private sector banks.
2. Ho (2): There are no significant differences in the reporting of various elements of banking disclosures.

VI. RESEARCH METHODOLOGY

Sample selection
Sampling Unit in the study has been any scheduled commercial bank registered in India and among top banks on the basis of market capitalization. There were 26 public sector banks operating in India. Out of these Allahabad bank (public sector bank) and HDFC bank (private sector bank) was chosen.

Period of study
The time frame of the study is one financial year i.e. 2016-17. Annual reports of the selected banks were collected/ downloaded from their websites for further analysis.

Disclosure Index
The index of disclosure was used in the study to evaluate the annual reports of both the commercial banks. The index of disclosure which was used in the present study is different from the previous indices because of the fact that the disclosure requirements of banking companies are different from non-banking companies. A total of 348 elements were identified. These included 161 mandatory disclosure elements and 187 voluntary disclosure elements. Further, these elements were divided into twenty sub-groups.

Tools of analysis
Both a weighted disclosure index and an unweighted disclosure index are usually used to determine disclosure level. Previous experiences also show that the use of unweighted and weighted scores for the items disclosed in the annual reports and accounts can make little or no difference to the findings (Coombs and Tayib, 1998). Thus, unweighted disclosure index methodology has been adopted. In this case, the key fact is whether or not a bank discloses an item of information in the annual report. If a bank discloses an item of information in its annual report, then ‘1’ is awarded and if the item is not disclosed, then ‘0’ is awarded. Thus, the unweighted disclosure method measures the total disclosure (TD) score of a banking company as additive.

VII. DISCLOSURE PRACTICES OF THE SELECTED BANKS

A COMPARATIVE EVALUATION OF ALLAHABAD BANK AND HDFC BANK REGARDING THE MANDATORY DISCLOSURE ITEMS

	ALLAHABAD BANK		HDFC BANK
PARTICULARS	No. of items	DISCLOSURE SCORE	DISCLOSURE SCORE
DISCLOSURE SCORE ACCORDING TO BALANCE SHEET ITEMS	13	13	13
DISCLOSURE SCORE ACCORDING TO PROFIT & LOSS ACCOUNT ITEMS	6	6	6
DISCLOSURE SCORE ACCORDING TO DIRECTOR'S REPORT	6	5	6
DISCLOSURE SCORE ACCORDING TO MANAGEMENT DISCUSSION AND ANALYSIS REPORT	9	7	9
DISCLOSURE SCORE ACCORDING TO CORPORATE GOVERNANCE	46	44	37
DISCLOSURE SCORE ACCORDING TO RBI GUIDELINES	46	42	42
DISCLOSURE SCORE ACCORDING TO BASEL II (PILLAR3)	35	35	35

A COMPARATIVE EVALUATION OF ALLAHABAD BANK AND HDFC BANK REGARDING THE VOLUNTARY DISCLOSURE ITEMS

		ALLAHABAD BANK	HDFC BANK
PARTICULARS	No. of items	DISCLOSURE SCORE	DISCLOSURE SCORE
DISCLOSURE ACCORDING TO GENERAL CORPORATE INFORMATION	6	4	3
DISCLOSURE ACCORDING TO CORPORATE GOVERNANCE	11	2	3
DISCLOSURE ACCORDING TO FINANCIAL PERFORMANCE	37	19	13
DISCLOSURE SCORE ACCORDING TO INFORMATION RELATING TO KEY PERSONNEL	5	1	3
DISCLOSURE SCORE ACCORDING TO CORPORATE STRATEGY	19	10	6
DISCLOSURE SCORE ACCORDING TO GENERAL RISK MANAGEMENT	5	5	5
DISCLOSURE SCORE ACCORDING TO KEY NON FINANCIAL STATISTICS	13	4	6
DISCLOSURE SCORE ACCORDING TO EMPLOYEE RELATED INFORMATION	4	1	2
DISCLOSURE SCORE ACCORDING TO DISCLOSURE REGARDING COMMITTEES	21	10	5
DISCLOSURE SCORE ACCORDING TO CORPORATE SOCIAL DISCLOSURE	20	11	7
DISCLOSURE SCORE ACCORDING TO INFORMATION REGARDING BORROWERS/DEPOSITORS	8	8	8
DISCLOSURE SCORE OF SELECETED BANKS ACCORDING TO INFORMATION/FORMS FOR SHAREHOLDERS	12	7	6
DISCLOSURE SCORE ACCORDING TO MISCELLANEOUS INFORMATION	26	10	7

CONCLUSION

The central focus of corporate financial reporting has changed with the passage of time. In the past, corporate financial reporting was oriented to providing **stewardship information**, which was essentially backward looking. The essence of stewardship reporting lies in giving an account of what management has done with the money entrusted to it. Today, the preparation and presentation of corporate financial reports is being driven by the consideration of providing information that is useful for making economic decisions, i.e., **decision oriented financial reporting**. Decision oriented financial reporting is basically concerned with providing information that will enable the users of the financial statements to judge the ability of the company to generate cash flows in the future. This shift in emphasis is fully reflected in the objectives of financial statements developed by Financial Accounting Standards Board (FASB).

According to the **True Blood Study Group Report**, "the basic objective of financial statements is to provide information useful for making economic decisions" (Sorter & Gams, 1974).Disclosure of information has a greater significance in achieving accounting objectives and for this disclosure needs to be **adequate**. Adequate disclosure means fair and full disclosure so that it helps the users in making rational decisions. It reflects economic efficiency of the resource use and thereby helps in directing the flow of capital into productive channels. It would also prevent and mitigate fraud and manipulation. The more the information available, the less is the opportunity for fraud and greater the confidence in the company.

Thus adequate disclosure relates particularly to objectives of relevance, neutrality, completeness and understandability. Information should be presented in a way that facilitates understanding and avoids erroneous implications.

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