

Annual Reports : Medium of Disclosure

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"This tells you what we have done with your business, if you can evaluate from these condensed, technical, financial documents".

— Thomas S. Sanders on Annual Reports

The published corporate annual report is the most vital and favoured channel of information disclosure in the corporate world and investment market. A corporate report is a comprehensive and authentic package of various kinds of information which most completely and suitably describes the economic operations of a company. It provides detailed financial information about a corporation in a more or less standardized way. It is the end product of the accounting information process and set of accounting measurement rules. It reflects a combination of recorded facts, accounting conventions and personal judgments of the preparer which naturally affect the preparation of Annual report. (Lal, 1985 : p. 14). However, the soundness of judgments necessarily depends on the competence and integrity of those who make them and their adherence to generally accepted accounting principles (Varghese, Sreeranganadhan, 2010 : p. 59).

The modern corporate report is the product of financial accounting's gradual evolution into financial reporting. The former was concerned almost exclusively with the financial statement and related notes, while the latter refers to an expanded package containing a great deal of narrative, graphical and photographic material. Despite the existence of different sources of information i.e. prospectus, press release, newspapers, periodicals, house magazines, advertising, press conferences, exhibitions, shareholders' annual general meetings, publications of professional and accounting bodies, interviews with company officials, interim reports, audio-visual and digital media etc. the published annual

reports are the most significant source of information about the company's affairs in the investment market. Thus, from an informational perspective, financial reports provide value-relevant information incremental to the total mix of information (in other words, all other sources of publically available information) (Beaver, 1998 : p.76).

CONTENT OF ANNUAL REPORTS

The annual reports are the most exhaustive resource of information about corporates. A financial report has different sections dealing with different aspects of companies' affairs and performance. Various factors such as social, political, economic, legal etc. influence the level of accounting and reporting in the annual reports. The information disclosed in the annual reports should basically meet the information requirements of the users. All that information, which meets the needs of users in serving all the objectives, should be disclosed (Porwal, 1996 : p.283). Basically, corporate annual reports contain two types of reporting: statutory and non statutory.

MANDATORY REPORTING

Mandatory disclosure includes information and other matters which are statutorily required to be disclosed in accordance with the regulatory environment. The following information is required to be disclosed.

- (a) Balance sheet
- (b) Profit and Loss Account
- (c) Auditors' Report
- (d) A Report by the Board of Directors of the company
- (e) Accounting Policies
- (f) Cash flow statement
- (g) Corporate Governance Report
- (h) Account of Subsidiaries

NON-STATUTORY REPORTING

The annual report of a company also includes certain non-statutory, voluntary information. This information is disclosed to supplement or to elucidate the information contained in the statutory part. Both the management and the investors influence the practice of voluntary disclosure. The consideration of the users' informational needs is of paramount significance in this regard. (Chander, 1992:p.35) Management has a responsibility to act in the interest of the investors.

Managements, competing among one another for investors' funds (Beaver, 1998, p.153) have incentives to voluntarily reveal information (Healy and Palepu, 1993).

Such information may relate to the following :

- (i) Inflation Accounting
- (ii) Human Resource Accounting
- (iii) Social Accounting
- (iv) Statement of Value Added
- (v) Statement of Changes in the Financial Position
- (vi) Financial History and Ratios
- (vii) Statistical Presentation-Charts, Graphs etc.
- (viii) Chairman's Report
- (ix) Corporate Objectives and Profile
- (x) Pollution Control Efforts

Disclosing information voluntarily has become a norm for companies. In fact, a large proportion of corporate disclosures made through annual reporting concern an agenda of visualising the company's core values, mission statement, business concept, and social responsibility. Through voluntary disclosure, corporate managements are able to justify their decisions and moves and they have the freedom and flexibility to report what has been achieved and what can be achieved, given the available assets and existing obligations.

SIGNIFICANCE OF ANNUAL REPORTS

The significance of the annual reports has been widely acknowledged in the accounting literature. According to Duff and Phelps (1976), the annual report is the most direct, least expensive, most timely and fairest method of reaching all the shareholders, and other potential investors. It is the primary medium for projecting a company at its audience and is the most effective voice in corporate communication (Haggie, 1984). For public sector companies, Narian (1968) has called annual reports as an important aspect of public relations.

Annual reports are a highly useful source of data because managers of companies commonly signal what is important through the reporting mechanism. (Guthrie and Richard, 2000) The Board of Directors, the highest management level of decision makers in the company, endorse the annual reports. On the importance of annual reports and responsibility of directors for the contents included therein, Financial Report Council (FRC), the U.K, has stated'.....prime responsibility for published accounts lay with the directors, the directors should aim at providing a clear informative and unambiguous set of account, which supply basis for narrative within the annual report which adequately highlights all matters of significance

good or bad, affecting a company's performance position....' Thus, annual report is the primary means by which effective communication with shareholders and other stakeholders is established by the corporate management. Some of the reasons that have contributed to making annual report the most sought after medium of dissemination of information are as follows :

1. It is a comprehensive, accessible and widely distributed sources of business data.
2. It provides an instrument of control. It is through the annual report that the management of an enterprise gives an account of itself to varied participants. The report highlights the achievements during the year and explains non-achievements too. Future plans and programmes also form an integral part of a good annual report.
3. External users repose greater confidence in information reported in annual reports, because the financial statements (An important section of annual report including schedules and notes to accounts) are independently audited by the statutory auditors, only authenticated information is conveyed through them.
4. It also contains a variety of non-statutory required information in a single document, which may not ordinarily be available through other sources of information.
5. Annual report, representing the most commonly available source of information on past and present performance, and statements therein are used by both amateur and professional investors to predict company's future performance, thereby providing a base for estimating future share prices and the related cash flows to the investors.

Fundamentally, the annual report is seen as a document which adds value to the stakeholders. The investors are the foremost audience of the annual reports. Hay in his study finds that 99 per cent of a company management's communicates to investors through annual reports. Hence, annual report is the most important and vital corporate document in financial reporting to a broad range of users.

Brand Building

Companies build brands through their annual reports by the use of celebrities, increased focus in employees as the company gained recognition and persistent focus on transparency. Reports not only communicate the business performance, but also communicate the character of the company. They are used as an effective marketing tool. Annual report today is not simply a means of

communication, it is now being used as a vehicle of building and enhancing corporate image. (The Chartered Accountant, Oct. 11).

Annual reports today are produced by a team of graphic designers, communication specialists and investor relation team. In 1955, IBM hired a graphic designer for their annual reports and Litton industries in 1962, published theme-based annual report, setting new standards for others to follow. In the same vein, for the first time Infosys published 'In pursuit of excellence' theme-based annual report in 1996, using celebrities' endorsements (Madhuri Dixit, Anil Kumble, Prof. C. K. Pradhan, JRD Tata etc.) to enhance the appeal of the annual reports to wider audience. Also, the list of management awardees was included which brought the employees to the centerstage. The annual report was used as a vehical for both legs of transparency, i.e communicating setbacks and the governance practices. Over the years, annual reports have graduated from a staid corporate document to an innovative branding product. Also, CAR has traditionally been published by using the print media, but of late, because of the rapid development of information technology, corporations are increasingly distributing digital versions of their annual reports via the internet, and thereby reducing their information costs.

Size Does Matter, But.....

The size of a report depends on the content and matter, it has to communicate to its audience. The difference between reporting and communication widens, as the report size increases. The distinction is best understood by the Aesop's Fable 'The fox and the stork'. In this fable, a sly fox invites a stork for dinner and serves soup in a shallow dish. While the fox relishes the soup, the stork could only just watch it. To reciprocate, when the fox is invited over for a dinner, the stork serves the soup in a long jar with a narrow mouth. This time, the stork enjoys the soup and the fox watches it longingly.

Similarly, in annual reports too, it is not only the quantity or the quality of information provided that reaches the audience, but the way it is served or presented, also matters. If it is not served appropriately, the reader can only watch the dish longingly and the journey of the annual report will be short-from the printers press to the dustbin.

Since the advent of computers and graphic softwares, written communication has come a long way. To attract and retain the target audience, it is important that photographs and graphs are included and woven into the written narrative of the annual reports. Adding color, graphics, style, visual appeal etc. enhances the readability of the annual reports and thus their prospects of investment. Commenting on the quality of writing and the presentation of report, Dr. Mc Queen,

a researcher remarked, 'many were so well written that one left feeling not just a desire, but an obligation to invest'

ICAI'S ROLE IN BRINGING ABOUT BETTER PRESENTED ACCOUNTS

The Institute of Chartered Accountants of India instituted a competition in 1958, for the best presented accounts in India. Their objective was to promote better standards in presentation of reports, an effort in effecting improved disclosure practices. There are seven categories for ICAI Awards for Excellence in Financial Reporting -Manufacturing and trading enterprises, Finance sector, Service sector, Banking, finance and financial institutions, Information technology, communication and entertainment enterprises, Infrastructure and construction sector and others which includes Sec.25 companies, educational institutions, NGO, charitable organizations etc. The reports are judged by the experts and the best annual report is selected. Some of the significant factors considered by the Institute of Chartered Accountants of India for the award of shields and plaques for the best presented accounts are as follows :

1. Compliance with the legal requirements in the preparation and presentation of financial statements as specified by the Companies Act, 1956 and other relevant statutes.
2. Basic quality of accounts as judged from the qualifications in the auditors' reports, notes to the accounts and compliance with generally accepted accounting principles.
3. The nature and quality of information presented in the accounts to make the disclosure of accounting policies, statement of changes in financial position, disclosure of unusual and prior period items, use of charts, graphs, inflation-adjusted accounts, human resource accounting, value-added statements, break-up of operations, product-wise or department-wise, social cost statements, location of factories, branches etc.
4. How informative are the directors' reports?
5. Description of the operations of the organization, information regarding financial operations, capital raised during the year, financial requirements, borrowing etc. and employee relations.
6. The quality of printing and general presentation.

The Way Forward.....

Given the important role that they play in corporate reporting framework, it is essential that annual reports are relevant and present an accurate, coherent and

balanced picture of the business and its prospects. Reports should appear to be more focused with more thought given to the linkage between the components of the report. Now a days it is required that a contemporary report should include disclosure of even those aspects of business performance that have still not be mandated under the statute law.

In addition to reporting financial information, annual reports are gradually reflecting future business potential. They have become the corporate calling cards.(Jaganathan,2009).To interpret the results, management discussion and analysis has been introduced in the reports. The management analyses and draws inferences in narrative form and significant future implications are highlighted. Content was added to address the concerns and issues of diverse users of the report, specifically pertaining to the social and environmental impact of business.

Though annual report provides an important benchmark for measurement of financial progress, that has the benefit of being independently audited, it is inherently less timely. Investors require more current information at periodic intervals -at quarterly and sometimes monthly interim dates, for continuously evaluating the performance of industry, company developments and revising their earning expectations as a basis for investment decisions. Given the dynamics of the frequent changes in the economic forces in the environment, disclosure of adequate information on timely basis, which will be useful to investor, is the need of the hour.

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