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AN OBSERVATION OF DISCLOSURE PRACTICE REGARDING PROPERTY, PLANT AND EQUIPMENT ON TEN LISTED INDIAN COMPANIES

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ABSTRACT

Financial Reporting provides useful information for decision making purpose by external users, which depends on the nature and extent of information disclosed by corporate entities. Accounting Standards plays an important role in enhancing usefulness of information contained in corporate financial reports by providing different types of accounting principles and policies. The rapid growth of international trade and trans-nationalization of the corporations necessitated global convergence of diverse accounting practices. On 16th February 2015, in exercise of the powers conferred by Section 133 read with section 469 of the Companies Act, 2013 the Central Government, has introduced the Companies (Indian Accounting Standards) Rules, 2015 (Companies Act, 2015). One of the important Indian Accounting Standard, Ind AS 16, Property, Plant and Equipment deals with recognition, measurement and disclosure of Property, Plant & Equipment (PP&E) and related depreciation on such assets. The objectives of the study are to assess the disclosure level in relation to property, plant and equipment made in the annual reports of top manufacturing companies in India and to compare the disclosure level relating to property, plant and equipment before and after implementation of Ind AS 16. For this purpose, the annual financial statements were studied for the year 2015-16 and 2016-17 of top 10 Indian manufacturing companies and to show the difference, if any, relating to disclosure practice on Property, Plant and Equipment.

Keywords: Financial Report, Accounting Standard, Disclosure Practice, Property, Plant and Equipment

INTRODUCTION

Corporate financial reporting is the communication of financial information of a corporate enterprise to the external world. Till the first quarter of the twentieth century, financial reporting was confined to the stewardship reporting, i.e., reporting of the wealth and income earned by the owners (Banerjee, 2002). Thereafter, the central focus of financial reporting has been shifted from stewardship reporting to decision-oriented financial report. The basic objective of corporate financial reporting is to provide useful information for decision making by external users, which depends on the nature and extent of information disclosed by corporate entities. Accounting Standards play an important role in enhancing usefulness of information contained in corporate financial reports by providing different types of accounting principles and policies of how particular type of economic transaction should be measured, recognized, presented and disclosed in the financial statements.

LITERATURE REVIEW

Global Convergence of Indian Accounting Standard

Accounting policies adopted by different countries differed widely due to differences in social, economic and legal environments. The rapid growth of international trade and trans-nationalization of the corporations necessitated global convergence of diverse accounting practices. To enjoy the benefits of international harmonization of accounting standards, India has initiated the process of harmonizing its accounting standards with global accounting standards. During 2010 the ICAI drafted 35 Indian Accounting Standards (Ind ASs) which are substantially converged with International Accounting Standard (IASs)/ International Financial Reporting Standard (IFRSs). In 2015, 41 accounting standards were issued under the Companies (Indian Accounting Standards) Rules, 2015 (Companies Act, 2015) which are converged with IASs/ IFRSs (India) (Ministry of Corporate Affairs, 2013). These converged accounting standards are known

'Indian Accounting Standards' (Ind ASs). Indian Accounting Standards are applicable for specified companies in a phased manner starting from the accounting year beginning on or after 1st April 2016. At present, 39 Indian Accounting Standards (Ind ASs) issued under the Companies (Indian Accounting Standards) Rules, 2015 (Companies Act, 2015).

Ind AS 16: Property, Plant & Equipment

Out of 41 Indian Accounting Standards, Ind AS 16 on *Property, Plant and Equipment* is one of the important accounting standards. Ind AS 16 deals with recognition, measurement and disclosure of property, plant & equipment (PP&E) and related depreciation on such assets. Previously two separate Accounting Standards, i.e., AS 10 for accounting for Fixed Assets and AS 6 (Accounting Standard (AS) 6; Accounting Standard (AS) 10) for accounting for Depreciation are used.

Ind AS 16 define Property, Plant and Equipment (PP&E) are those tangible assets which are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes and are expected to be used during more than one accounting period. These assets constitute a significant proportion of total assets of an enterprise, particularly, in case of manufacturing companies.

That is why users of the financial statements are very much interested in information about an entity's investment in its property, plant and equipment and the changes in such investment. Unless these assets are properly accounted for and reported in financial statements, the financial position and performance of an enterprise could not be properly appreciated. If property, plant & equipment (PP&E), related depreciation and impairment loss are not recognized, measured and reported as per the Indian Accounting Standards (Ind AS) 16, financial statements of Indian companies will not be comparable at the international level and hence, Indian companies will lose the benefits of international harmonization of accounting standards.

The objectives of the study are as follows:

(i) To *assess the disclosure level* in relation to property, plant and equipment made in the annual reports of top manufacturing companies in India.

(ii) To *compare the disclosure level* relating to property, plant and equipment before and after implementation of Ind AS 16.

RESEARCH METHODOLOGY

The proposed study is intended to focus on examination of disclosure practices relating to property, plant & equipment and measurement of the level of such disclosure in annual reports of the companies listed in Indian Stock Exchanges. For measuring the extent of disclosure in relation to property, plant and equipment, information disclosed in the annual reports of 10 manufacturing companies in India for the accounting years 2015-16 and 2016-17 (i.e., before and after mandatory implementation of Ind AS 16) will be studied. Sample companies were selected from the list of top 500 companies (ranked based on Revenue Earned) listed in different stock exchanges in India. The list of 500 companies was found in ET 500 Companies, 2017 (ET Markets).

Legal Framework

The accounting practices of the country are governed by the legal provisions of the land. In India, the main source of accounting regulations is the Companies Act, Accounting Standards and SEBI Acts. Neither the Companies Act, 1956, nor the Companies Act, 2013 makes any direct provision in relation to accounting for or disclosure of property, plant and equipment (Ministry of Corporate Affairs, 2013; Ministry of Corporate Affairs, 1956).

However, both the Acts legally recognizes accounting standards which deals with different accounting issues including recognition, measurement and disclosure of property, plant and equipment and depreciation thereon.

The Companies Act, 2013 requires that the financial statements should comply with the accounting standards notified under section 133 (Section 129) (Ministry of Corporate Affairs, 2013). On 16th February 2015, in exercise of the powers conferred by Section 133 read with section 469 of the Companies Act, 2013 and section 210A (1) of the Companies Act, 1956, the Central Government, in consultation with the National Advisory Committee on Accounting Standards, the Companies (Indian Accounting Standards) Rules, 2015 (Companies Act, 2015) has been introduced (Ministry of Corporate Affairs, 1956).

According to rule 4 of the said rule, certain specified companies are required to comply with the Indian Accounting Standards (Ind AS) and are to be implemented in a phased manner. The first phase of implementation of the Indian Accounting Standards (Ind AS) including Ind AS 16 on Property, Plant and Equipment will commence from the accounting periods beginning on or after 1st April 2016.

Construction of Disclosure Checklist & Methods for Measuring the Disclosure Checklist

1. Disclosure checklist for fixed assets and related depreciation under Accounting Standard 10 & 6 respectively has been prepared based on disclosure requirement specified in the AS 10 (Companies Rules, 2006) & AS 6 for the year 2015-16 and disclosure checklist for the year 2016-17 relating to property, plant and equipment under Indian Accounting Standard (Ind AS 16) has been prepared on the basis of disclosure requirement specified in the Ind AS 16. For checking disclosure score 15 disclosure items have been prepared among these 7 disclosure items as per AS10 and 8 disclosure items as per AS6 (Accounting Standard (AS) 6; Accounting Standard (AS) 10). Out of these 15 items, 8 items of disclosures are applicable to all companies and 7 items are required whenever it is applicable.

2. Disclosure score for the year 2016-17 has been prepared based on Ind AS 16 which contains 22 items of disclosures among these 7 are generally applicable items and other 15 items are necessitated as per applicability.

The extent of disclosure in annual reports of sample ten companies was measured by using Disclosure Index Method. Previous researchers have used two different Disclosure Index Methods, namely, (a) Weighted Disclosure Index Method and (b) Unweighted Disclosure Index Method (Abdullah *et al.*, 2013).

The most important limitation of a weighted disclosure index is that it involves an element of subjectivity in assigning weights to different information items. To avoid this limitation, Unweighted Disclosure Index method has been used in the present study.

Under unweighted disclosure index method, equal weight i.e., 'one' is assigned to each information item and disclosure score is measured by using any one of the following two approaches:

1st Approach: Normal Disclosure Approach (Based on Maximum Achievable Score)

$$\text{Unweighted Disclosure Index (\%)} = \frac{\text{Total Score Obtained by the Company}}{\text{Maximum Achievable Score}} \times 100$$

2nd Approach: Modified Disclosure Approach (Based on Applicable Score)

$$\text{Unweighted Disclosure Index (\%)} = \frac{\text{Total Score Obtained by the Company}}{\text{Total Applicable Score}} \times 100$$

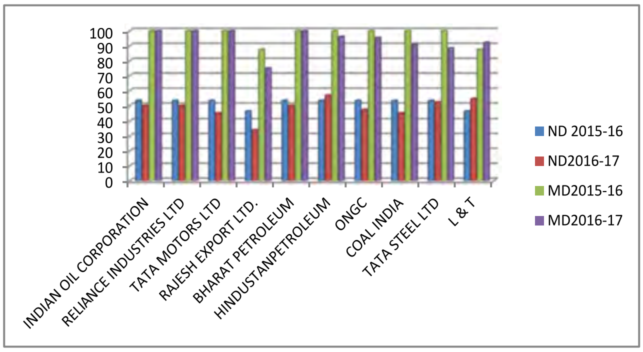
List of Sample Companies (In descending order of rank as found in ET 500 Companies, 2018)

Sl.No.	Name of the Company	Sl. No	Name of the Company
1.	INDIAN OIL CORPORATION (IOC)	6.	HINDUSTAN PETROLEUM (HP)
2.	RELIANCE INDUSTRIES LTD (RIL)	7.	ONGC
3.	TATA MOTORS LTD (TM)	8.	COAL INDIA (CI)
4.	RAJESH EXPORT LTD. (REL)	9.	TATA STEEL LTD (TSL)
5.	BHARAT PETROLEUM (BP)	10.	L & T

Table 1: Disclosure Score of Samples 10 Companies for the Years 2015-16 & 2016-17

		NORMAL DISCLOSURE		MODIFIED DISCLOSURE	
		2015-16	2016-17	2015-16	2016-17
1	INDIAN OIL CORPORATION	53.33	50	100	100
2	RELIENCE INDUSTRIES LTD	53.33	50	100	100
3	TATA MOTORS LTD	53.33	45.45	100	100
5	BHARAT PETROLEUM	53.33	50	100	100
6	HINDUSTAN PETROLEUM	53.33	56.82	100	96.15
7	ONGC	53.33	47.73	100	95.45
8	COAL INDIA	53.33	45.45	100	90.91
9	TATA STEEL LTD	53.33	52.27	100	88.46
4	RAJESH EXPORT LTD.	46.66	34.09	87.5	75
10	L & T	46.66	54.54	87.5	92.31

Result generated on study of Annual Financial Statement of 10 companies



On analyzing the above table 1 following observations or findings are made in respect of the extent of disclosure in annual reports of our 10 sample companies:

First: It is evident that normal disclosure score is very low as compared to modified disclosure score because it is calculated only based on total items of disclosure, but modified disclosure score is based on applicable items only. Out of these 10 sample companies Indian Oil Corporation is in the highest and L&T is the lowest scorer in both approaches for the year 2015-16.

Second: It is evident that in Normal Disclosure approach L&T is the top scorer and Indian Oil Corporation is highest scorer under modified disclosure approach, but Tata Motors is the lowest scorer under both the approaches year for the year 2016-17.

Table 2: Summary of the Descriptive Statistics relating to Extent of Disclosure

		NORMAL DISCLOSURE		MODIFIED DISCLOSURE	
		2015-16	2016-17	2015-16	2016-17
1	Maximum	53.33	56.82	100	100
2	Minimum	46.67	34.09	87.5	75
3	Average	52	48.64	97.5	93.83
4	Standard Deviation	2.81	6.26	5.27	7.85
5	Range	6.66	22.73	12.5	25

Source: Computed from Information Provided in table 1

Findings from the analysis of table 2

First, the maximum disclosure score is 53.33% in the year 2015-16 and 56.82 in the year 2016-17 under normal disclosure approach, which implies that none of the sample companies has disclosed all the information relating to fixed assets or property, plant and equipment as stated in the disclosure requirement of AS 10 and AS 6 for the year 2015-16 and Ind AS 16 for the year 2016-17 respectively. But under modified disclosure approach, the maximum disclosure score for both the year is 100%, which implies that at least one of the sample companies has disclosed all the information items which are applicable to it. From table 2 it is evident that the number of companies disclosing all the applicable information item for the year is eight and four for the year 2016-17.

Second, the minimum disclosure score for the year 2015-16 is 46.67% and 34.09% for the year 2016-17 under normal disclosure approach, both of which are considered as extremely poor.

However, the minimum extent of disclosure is 87.5% and 75% for the year 2015-16 and 2016-17 respectively measured under modified disclosure approach which are better than minimum disclosure under normal disclosure approach. Here the result of 2016-17 is lowered than 2015-16, it implies that disclosure practice in relation to property, plant and equipment as per Ind AS 16 is not satisfactory.

Third, average level of disclosure score under normal disclosure approach for the year 2015-16 is 52% and 47.64% for the year 2016-17 which may be considered as very poor. However, under modified disclosure approach where we consider only applicable information items, mean disclosure score is found to be 97.5% and 93.83% for the year 2015-16 and 2016-17 which can be considered as very satisfactory.

Fourth, the variability in the extent of disclosure is low under both the approaches of measuring disclosure score. This is evident from the range (6.66% and 12.50%) and the standard deviation (2.81% and 5.27%) of disclosure score under normal disclosure approach and under modified disclosure approach for the year 2015-16.

However, the variability in the extent of disclosure for the year 2016-17 is wide as compare to the year 2016-17 because this is evident from the range (22.73% and 25%) and the standard deviation (6.26% and 7.85%) of disclosure score under normal disclosure approach and under modified disclosure approach.

Apart from quantification of the extent of disclosure, we have tried to make a qualitative assessment of disclosure relating to property, plant & equipment. For grading the quality of disclosure, the following self-constructed criteria as reported in table 3 have been used.

Criteria for Grading the Quality of Disclosure

DISCLOSURE SCORE	DISCLOSURE GRADE
100%	Excellent
90% - less than 100%	Satisfactory
75% - less than 90%	Moderate
60% - less than 75%	Unsatisfactory
less than 60%	Poor

Table 3: Gradation of Sample Companies Based on Disclosure Quality

DISCLOSURE SCORE	DISCLOSURE GRADE	2015-16		2016-17		2015-16		2016-17	
		Normal Disclosure Approach				Modified Disclosure Approach			
		NO. OF COs	(%)	NO. OF COs	(%)	NO. OF COs	(%)	NO. OF COs	(%)
100%	Excellent	0	0	0	0	8	80	4	40
90% - less than 100%	Satisfactory	0	0	0	0	0	-	4	40
75% - less than 90%	Moderate	0	0	0	0	2	20	2	20
60% - less than 75%	Unsatisfactory	0	0	0	0	0	-	0	-
less than 60%	Poor	10	100	10	100	0	-	0	-
TOTAL		10	100	10	100	10	100	10	100

Source: Computed from Information Provided in table 1

Findings from table 3

From table 3, it is found that all the sample companies got below 60% disclosure score for both the year 2015-16 and 2016-17 under normal disclosure approach. This indicates that result of all ten sample companies are 'Poor'.

However, disclosure quality shows much better picture when gradation is based on disclosure score measured under modified disclosure approach. It shows that 80% of sample companies have 'Excellent' extent of disclosure level while only 20% of them have 'Moderate' disclosure level for the year 2015-16. For the year 2016-17 it is found that 40% of the sample companies secure Excellent, another 40% secure Satisfactory disclosure grade and only 20% get Moderate disclosure grade.

RESULTS & DISCUSSION

First: In 2015-16 all companies disclosed information relating to gross and net book value at the beginning and end of the period, reconciliation of book value, and total depreciation of each class of assets, accumulated depreciation, gross amount of depreciable assets and depreciation rates or useful lives.

Out of 10 sample companies, Rajesh Export Limited did not show the cost of construction or acquisition of assets. Eight out of ten companies used Straight Line Method as the method of depreciation and only Reliance Industries Ltd is used Written Down Method as method of depreciation, but L&T did not disclose the method of depreciation at all.

Second: In 2016-17 the information disclosed by all the companies are as follows:

1. All sample companies measured the gross currying amount at Historical Cost.
2. Straight Line Method was used as a method of depreciation eight companies out of ten sample companies and other two companies, Reliance Industry Ltd and ONGC were used Written Down Value Method as a method of depreciation.
3. All ten sample companies were using the useful lives as the basis of depreciation and shown the gross currying amount and accumulated depreciation at the beginning and end of the period.
4. Reconciliation of currying amount at the begging and end of the period was made by all ten sample companies.
5. Existence and amount of restrictions on title of property, plant and equipment and pledged as security were applicable to eight companies except ONGC and Coal India Ltd.
6. Recognition of amount of expenditure in course of construction of property, plant and equipment were applicable to all ten sample companies and nine out of ten sample companies were shown it properly but Tata Steel Ltd was shown it partially.
7. The amount of contractual commitment for purchase of property, plant and equipment is applicable to one company i.e., L&T Ltd and shown it in its annual financial statement.
8. The amount of compensation received from third party for items of property, plant and equipment include in the statement of Profit & Loss was only applicable and shown by two companies, i.e., Bharat Petroleum Ltd and Hindustan Petroleum Ltd.
9. Depreciation was recognized in the Statement of Profit & Loss Statement by all ten sample companies.
10. None of the company did not make the revolution of property, plant and equipment, as a result items of disclosure in relation to revaluation were not applicable.
11. List of impaired property, plant and equipment were applicable to four sample companies but none of them was disclosed in their annual financial statement.
12. Currying amount of any property, plant and equipment retired from their active use (not held for disposal) was applicable for four companies but only two companies, Hindustan Petroleum and ONGC were disclosed these items in their Annual Financial Statement.

CONCLUSION

Based on the empirical results under modified disclosure approach, average disclosure score for the year 2015-16 is 97.5% and for the year 2016-17 is 93.83%, both of which are found to be satisfactory and most of the sample companies have 'Satisfactory' disclosure level (90% or more). However, the minimum disclosure score of sample companies are below satisfactory level before and after implementation of Ind AS. This suggests that there is a need for further monitoring of disclosure practices of manufacturing companies in India to improve disclosure quality which will assist in achieving the objectives of harmonization of Indian accounting standards with global accounting standards.

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