

## Analysis on Voluntary Disclosure of Accounting Information for Listed Companies in China

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### Abstract

As the capital market develops, listed companies own a broader share in the market, but at the same time they are also faced with fiercer competition, which forces listed companies to disclose more reliable information to attract investors for more capitals. Meanwhile, the increase in the number of investors and the improvement of the quality of the capital market have led to a larger demand for the information from listed companies, as well as higher requirements made by all sectors of the community for information disclosure of listed companies; Mandatory accounting information disclosure alone can no longer satisfy the diverse needs of investors. As the opposite of mandatory disclosure, voluntary disclosure of information can improve the quality of corporate information disclosure, thus attracting more and more attention.

This article is divided into three parts. Firstly, it expounds the concept of voluntary disclosure of information and relating ideas; secondly, on the basis of the first part, it analyses the current situation of voluntary disclosure in the Chinese market as well as the existing problems, such as, unwillingness of voluntary disclosure, inadequate disclosed content and unregulated disclosure. Finally, corresponding countermeasures to improve voluntary information disclosure are put forward, namely, to strengthen supervision and to complete the corporate governance structure. The countermeasures are designed to improve the quality of voluntary disclosure and facilitate scientific decision-making for investors and other stakeholders, so as to promote the capital market to be healthier and more sustainable.

**Key words:** Listed company; Voluntary disclosure of accounting information; Countermeasure

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### INTRODUCTION

Information disclosure of listed companies refers to reporting to security regulators and revealing to the public the company's financial situation, operating results and other related information, in accordance with the relevant laws and regulations. The information disclosure institution serves as an effective guarantee for regulated operation of the capital market. The history of disclosure of accounting information has witnessed the transformation from voluntary to mandatory, and then to a combination of both. Voluntary information disclosure is still a new subject for the Chinese market, but its importance is graduating grabbing more attention. Due to the fact that Chinese accounting principles and systems were not adequately revealed during the making, only a small number of stakeholders were able to participate in the making of the principles, and thus it was difficult to satisfy the demand of market development. Voluntary disclosure of accounting information is not restricted by the national guidelines. Companies can work out the content for voluntary disclosure with their own advanced technologies, so as to meet the demands of the investors. Therefore, in order to accelerate the process of voluntary disclosure of accounting information of listed companies in China, it is extraordinarily important to conduct an in-depth study in its current situation, existing problems and their causes.

## 1. CONNOTATION OF VOLUNTARY INFORMATION DISCLOSURE OF LISTED COMPANIES

### 1.1 Concept of Voluntary Disclosure of Accounting Information of Listed Companies

*Improving Business Reporting: Insights into Enhancing Voluntary Disclosures* issued by Financial Accounting Standards Board (FASB) in 2001 has given a clear definition of voluntary disclosure — the provision of information by a company's management beyond requirements such as generally accepted accounting principles and Securities and Exchange Commission rules. In recent years, corporate voluntary information disclosure has been gradually attracting more attention from Chinese accounting circles, especially in the *Guidelines of the Shenzhen Stock Exchange for the Investor Relations Management by Listed Companies* issued in October 2003 by Shenzhen Stock Exchange the concept of voluntary disclosure was first introduced — listed companies can voluntarily disclose information beyond the requirements made by current laws and regulations through a wide variety of activities including investor relations management.

### 1.2 Differences and Relations Between Voluntary and Mandatory Accounting Information Disclosure

#### 1.2.1 Differences Between Voluntary and Mandatory Accounting Information Disclosure

Information disclosure of listed companies is of great significance for the healthy development of the capital market. From the perspective of being controlled or not, information disclosure can be classified into mandatory and voluntary accounting information disclosure. There are big differences between these two types of disclosure in terms of concept, motive and content. Mandatory accounting information disclosure refers to the content that is required to be disclosed in financial reports by generally accepted accounting principles and other laws and regulations. Voluntary accounting information disclosure means the information disclosed proactively, timely and accurately that is beyond the requirements made by security regulators and the information in which the company owns partial autonomous right. Mandatory accounting information disclosure is likely to cause market failure due to the fact that the company is the exclusive provider of its information; voluntary accounting information disclosure stems from economic globalization and it will lead to global expansion of the capital market. Due to the pressure of competing for capital, enterprises own the motive of reporting voluntarily their corporate information, so as to attract capital and improve their reputation and competitiveness.

#### 1.2.2 Relations Between Voluntary and Mandatory Accounting Information Disclosure

(1) Consistence of purpose. The model of accounting information disclosure of listed companies is the result of

strategic games between all stakeholders, and mandatory and voluntary accounting information disclosure are required to be consistent in terms of disclosure target and requirements. Both models follows the basic purpose of improving the quality of accounting information, and the information meet requirements including timeliness, accuracy, correlation, reliability and clarity; both models are the performance models of corporate governance, of which the entire process needs information, both financial and non-financial, and meanwhile the governance results will be reflected in the company's financial results and development performance, and further more in the accounting information that is disclosed.

(2) Complementarity of content. Both disclosure models are complementary to each other. One type of information cannot replace another, and such statement that one type of information is valuable and another is not does not exist. For investors, the value of information is not demonstrated in the model of disclosure, but in whether the information is related to the content of the investors' decision-making. Overstressing either model is inevitably biased to some extent. In the light of voluntary accounting information disclosure, on the one hand, it is to refine and deepen mandatorily disclosed accounting information, and on the other it supplements and expands the mandatory information disclosure, in order to highlight the company's core competitive force and disclose the information in a more comprehensive and systematic way to show the company's profitability and potential in the future. Both models are in the same system, and the absence of either one will lead to high risks.

(3) The two can convert into each other. Voluntary and mandatory accounting information disclosure can convert into each other. First, because of different cultural and legal background, the same information that should be disclosed mandatorily in certain countries might be disclosed voluntarily by corporates. For instance, information of company employees is mandatorily disclosed information in the UK and Australia; in other countries in the European continent, however, this is the information that can be disclosed on a voluntary basis. Second, the accounting information that can be disclosed voluntarily now may, with the political, social and economic development, become mandatorily disclosed information in the future. For example, in the Chinese security market, the profit forecast of a company was mandatory to disclose before April 2000, but will become voluntary after 6 April 2000 according to new laws and regulations. And vice versa, voluntarily disclosed accounting information can turn into mandatory. Third, the way and time of mandatory information disclosure can be chosen voluntarily, and voluntary information disclosure can be induced by mandatory one or serve as a necessary supplement for mandatory disclosure. For instance, the annual report is the regular report that must be disclosed mandatorily, and the time to disclose the annual report

can be decided by the high-level managers. Information disclosure is the result of the strategic game between all stakeholders. Mandatory and voluntary accounting information disclosures are seemingly contradictory, but in essence these two models of information disclosure are internally related.

## **2. CURRENT SITUATION OF VOLUNTARY INFORMATION DISCLOSURE OF CHINESE LISTED COMPANIES AND THE EXISTING PROBLEMS**

Chinese security market originated from the early 1990s. After decades of development, great achievements have been made in terms of accounting information disclosure—regulations of information disclosure have been gradually improved and the supervision system of information disclosure of listed companies have been more completed. With the development of the capital market, all sectors of the community have made higher requirements for information disclosure of listed companies, and mandatory information disclosure alone cannot meet diverse requirements from the investors. As the opposite of mandatory disclosure, voluntary disclosure of information can improve the quality of corporate information disclosure, thus attracting more and more attention. Although voluntary information disclosure is developing towards a positive trend, due to the deficiencies in the capital market, Chinese listed companies are still faced with a small funding pressure, and thus there are still a number of problems existing in voluntary accounting information disclosure, such as starting late and unregulated disclosure.

### **2.1 Unwillingness of Voluntary Accounting Information Disclosure**

In China, due to the less developed capital market and the limited conditions, there is just a small number of companies that can enter the market for funding. Therefore the investors outnumbered the listed companies, and the excessive supply leads to a smaller pressure for the funding raisers. In addition, companies have only limited cost, and they fear they may face lawsuits due to inaccurate information disclosed on a voluntary basis. Besides, there is a lack of sincerity and transparency in the market. As a result, Chinese listed companies show unwillingness to some extent to disclose their information voluntarily.

### **2.2 Inadequate Content of Voluntary Accounting Information Disclosure**

Voluntarily disclosed information mainly includes: managers' evaluation of the company's long-term strategies and competitive edges, environmental protection and social responsibilities, actual operating information,

forward-looking information, human resources information and operating effects, etc.. As classified by Shenzhen Security Institute, there are mainly the following five types of information, namely, background information, historical information, key non-financial information, forecast information, discussion and analysis from the management level. However, from the currently disclosed information from Chinese companies, the background information is general description, such the steps and actions taken for achieving the goal, schedule for completing the strategies and barriers the company may face. There is hardly information about the impact of these barriers on current and future profit. The current situation about social responsibility information disclosure in China is engendering little optimism. Although the National People's Congress and the State Council have established the committee and issued "Environmental Protection Law" and dozens of laws about environmental protection and resource utilization as well as a series of administrative laws and regulations, the present laws and regulations about social responsibilities still focus on environmental management and the information need of the country. There is a lack of rules, principles and guidelines for social responsibility information disclosure, and thus the companies are short of motives of disclosing information voluntarily, and the little and scattered information they disclose is far from being comprehensive. By March 2007, 14 large state-owned companies and 2 private companies had made the public their social responsibility reports, but Chinese companies are still far behind multinational companies from western countries.

### **2.3 Inaccurate and Unregulated Voluntary Information Disclosure**

Due to the consistent technological guidelines for voluntary accounting information disclosure for Chinese listed companies, managers from some companies, worrying about investors' doubt about the company's prospect and the falling stock price, are reluctant to disclose information voluntarily, so their disclosed information are not accurate and regulated enough; some do not disclose timely or even disclose nothing, some disclose financial indexes that are far different from the real one, and some only give general and ambiguous information with no value, fearing they may face lawsuits due to inaccurate information. For example, they disclose hardly forecast accounting information, sales information or market share rate; instead they only give in accurate profit forecast.

### **2.4 Lack of Variety in the Ways of Voluntary Information Disclosure**

Voluntary disclosure of information by listed companies is carried out mainly through the following three channels. Firstly, it is done through regular financial reports (listing announcements, annual reports, financial statements of the

first half of the year and season reports). The information includes the company's governance information, analysis and evaluation from the managers, environmental protection and social responsibilities. Secondly, it is done through communication with brokers, investors from institutions and specialized security analysts. This kind of communication is sort of private; normally after regular reports issued or major investment announced by the company, brokers, investors from institutions and specialized security analysts would ask the listed company to give further explanation about the content of the reports or the investment. Thirdly, listed companies issue information about core competitiveness, environmental protection and social responsibilities. This type of voluntary information disclosure is fast and influential, and can get timely response from the market. At present, there are two types of voluntary information disclosure, namely, regular reports and temporary reports. There are few opportunities of communication with agencies, especially with small and medium agencies as well as disclosure through television, networks and other forms of media.

## **2.5 Cause Analysis of Problems Existing in Voluntary Information Disclosure by Chinese Listed Companies**

In Chinese security market, there are some particular forms of manifestation due to the incomplete market institution and the severe ineffective information balance problems. In brief, problems in this perspective mainly exist in the following aspects.

### **2.5.1 Incomplete Capital Market**

Chinese listed companies are mainly state-owned enterprises, and state-owned shares account for most of the stock. Lack of status for state-owned shares owners and individual shareholders have lower requirements for information disclosure, and thus the listed companies face smaller pressure in this respect. Moreover, compared with investors in developed countries, the number of investors from institutions and individual investors is far behind, and the requirements for information disclosure are not high enough. Therefore, the level of voluntary information disclosure of Chinese listed companies is comparatively lower.

### **2.5.2 Low Cost of Law Violation and Inadequate Regulation and Punishment**

CSRC is featured with weak power and low authority, and the security market is filled with conflicts. The government is used to control the market in administrative ways instead of following the particular rules of the market. Due to the investors' low quality, useful accounting information cannot be conveyed to the investors and others who need the information in a comprehensive and timely manner. Hence, the inadequate supervision is also one of the causes for problems existing in accounting information disclosure.

### **2.5.3 Deficient Listed Companies' Governance Structure and Mechanism**

For listed companies, effective governance structure and institution can not only protect investors' interests, but also enhance the transparency of accounting information disclosure. The problems are also related to the deficiencies in the governance structure and the weakened governance institution. (1) The governance structure of listed companies is not complete. They have set up the board of directors and supervisors and recruited general managers, but the governance structure does not play its role; in other words, it is only a matter of formalization. a) Rights and responsibilities of the board of directors and the management level are not clear. The board of directors is the centre for decision-making and the general manager should be responsible for daily operation of the company. b) The board of directors is ineffective. In actual work, the board of directors cannot give full paly to its function and behave ineffectively in making decisions. c) The board of directors are controlled by big shareholders. The biggest shareholder for most companies in China is the country, so the chairman and board of directors lose their independency. d) The supervision institution of the board of directors is weakened. The company is internally controlled seriously due to lack of effective supervision and balancing mechanism. (2) The external management of listed companies is not complete. The external management institution mainly stems from the balance between managers and the capital market, between managers and the manager market as well as between managers and the product market. It is mainly shown in the following aspects: a) The stock structure of listed companies is not reasonable, so individual shares accounts for a small proportion and are too speculative despite its high liquidity. b) Commercial banks play a limited role in corporate governance, and the function of the investors from institutions is also very weak. c) Operators of limited companies are short of pressure in taking over the market. The state-owned regrouping, merging, "selling shell" and "buying shell" are mainly brokered by listed companies and other related companies or by high-level managers, so they are administrative and to some extent impartial.

## **3. STRATEGIES TO IMPROVE VOLUNTARY DISCLOSURE OF ACCOUNTING INFORMATION BY LISTED COMPANIES IN CHINA**

### **3.1 Guidelines for Voluntary Information Disclosure**

#### **3.1.1 The Principle of Authenticity**

The principle of authenticity means that listed companies should be honest in disclosing the true information

beyond the regulations and the information in which the company has the autonomous right. The information will have a direct impact on the decision-making of investors and other stakeholders. First, listed companies should give accurate accounting information voluntarily without overrating or underrating. The information they give should objectively reflect the company's operating and financial status, instead of being made up to affect the stock price or manipulate others. Then the companies should make sure that the disclosed information is consistent so as not to mislead the investors.

### **3.1.2 The Principle of Completeness**

The principle of completeness means that all information affecting investors' decisions should be disclosed, without deliberate concealing or major leaving out. While disclosing certain specific information, one must reveal all aspects of the information in a thorough, comprehensive and complete way; One should disclose not only information favorable to the company's stock price, but also the negative information. Information about potential or actual risks should not be left out. The investors will make decisions according to all the information disclosed by the company, so the companies are required to present the complete image of the company in front of the investors. Complete and voluntary disclosure of accounting information should involve the completeness of content and formats: first the content should be complete, without man-made hiding or leaving out; second the format, method and language of information disclosure should be regulated and understandable, and the information should be disclosed on wide-covering media.

### **3.1.3 The Principle of Timeliness**

The principle of timeliness means that listed companies should disclose their accounting information voluntarily as soon as possible. When the operating and financial situation changes, the company should immediately inform the details to investors and other stakeholders. This principle is a continuous obligation, namely, during the period from issuing securities to running the company, the information disclosed to investors should be updated in real time. Then investors can make rational choices according to the updates. On the security market, the value of information lies in its timeliness. A complete information disclosure system should have true and comprehensive information, as well as an effective and fast pathway for information. Only by enabling all market participants to access relevant information timely, can the fairness and effectiveness be ensured. The principle of timeless requires listed companies to disclose their important information legally and timely. Listed companies should inform the investors of major changes and events of the company, so as to make sure the fair and ordered operation of the market.

We should stick to the above-mentioned principles for voluntary disclosure of accounting information, and

improve the quality of information disclosure, so as to give investors easier access to more accurate information, and thus they can make smarter decisions.

## **3.2 To Enhance Laws and Regulations About Voluntary Accounting Information Disclosure**

Currently, there are no laws and regulations governing the content and format of voluntary accounting information disclosure in China, so managers can, taking into account the company's own interests, choose to disclose or not the information. Voluntary accounting information disclosure is relatively independent, and it can reflect the transparency of accounting information. However, it cannot be operated by the management level of the company; otherwise the transparency will deteriorate further.

In order to decrease this kind of situations and give full play to its function as signal pathways, post facto supervision must be conducted on the reliability of corporates' information disclosure, and punishment should be exerted on entities and individuals abusing voluntary information disclosure, so as to achieve the goal of effectively protecting the interests of investors.

Regulators' supervision on information disclosure includes the supervision not only on the content, but also on the timing, expression, forms and media. Therefore, it can be understood that listed companies can voluntarily disclose their accounting information, but once the information is out, it must meet the specified qualities to avoid misleading the public. These basic qualities involve the quality of the information content and the information disclosure. At present, auditors and national regulators pay more attention to and spend more efforts in the content. But the quality of accounting information disclosure should never be neglected. The management of accounting information disclosure has a significant impact on its transparency. Therefore, more focus should be put on the timeliness, equity accessibility of accounting information disclosure and the relations between accounting information and related information, so that investors can access and interpret the accounting information in an easier way and improve the transparency of accounting information.

## **3.3 To Strengthen Regulation of China Securities Regulatory Commission (CSRC) and Ensure Its Regulation Ability**

To establish the authority of CSRC calls for not only an ordered business allocation between CSRC and other regulators, but also a stronger regulating ability, so as to obtain true recognition from the security market. According to the actual situation in China, first other governmental organization's regulating power should be taken back to CSRC, making CSRC the only and highest security regulator all across the country. Then CSRC should be scaled up. In developed countries with a mature and regulated security market, a large-scale and strong security regulator is still necessary, not to

mention in China, where the security market is not mature enough and law violations are frequent. Strengthening the regulating power does not only refer to increasing the number of regulating staff, but also involve making sure the staff are qualified to do their job. Examinations of all forms should be carried out to recruit high quality and experienced talents in this field.

### **3.4 To Complete the Corporate Governance Structure and Establish Effective Main Body of Supply for Accounting Information**

A complete corporate governance structure is an effective way to prevent man-made unreal information disclosed by listed companies. A reasonable and improved company governance structure can promote the regulated information disclosure, improve the quality of the disclosed information and ensure the authenticity of accounting information to the largest extent. Only with competed property institution can the shareholders pursue maximum capital gains and form a contract relationship with the managers of the company, and then form the main body of demand for the real financial reports.

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