ISSN 2278 – 0211 (Online)

A Study on IFRS in India

Meenu Sambaru
III B.Com (Hons), St. Ann's College for Women, Hyderabad, India
Dr. N. V. Kavitha
HOD, Commerce, St. Ann's College for Women, Hyderabad, India

Abstract:
Economic development of any country requires a sound financial reporting system sustained by good governance, clearly defined quality standards and established regulatory framework. As the accounting standards formulating body in our country, the Institute of Chartered Accountants of India (ICAI), has always formulated accounting standards that have withstood the test of time. As we globalize, the significance of convergence increases with International Financial Reporting Standards (IFRS). In today's scenario of global business village India cannot afford to insulate itself from the developments and modifications taking place worldwide. IFRS can be explained in a narrow as well as a broad sense. In the narrow sense IFRS is the new numbered series of pronouncements that IASB has issued. In the broad sense IFRS includes standards and interpretations approved by the IASB, IASC & SIC. These new set of accounting standards is more principles based as compared to the earlier standards that were basically a principle based.
The objective of the present paper is to-

- *To examine the significance of IFRS in Indian business environment.*
- *To analyze the similarities and distinction between IFRS and AS.*

Irrespective of the varying opinions convergence of IFRS with local standards is now not just a forum of discussion but a reality. There are significant differences between the accounting treatments laid down in the existing Accounting Standards as against the treatments envisaged in the converged Indian Accounting Standards. These differences necessarily will have an impact on the depiction of profit and financial position of an enterprise. As the regulators and various stakeholders use the financial statements to achieve numerous objectives, they cannot afford to ignore the impact of implementation of the converged Indian accounting standards or Ind AS. Regulators would need to be aware of their impact on regulatory accounts, the return earned on assets and profit position under various regulated services.

Keywords*: IFRS, Convergence, IASB, Regulatory Board and Business environment*

1. Introduction

Accounting fraternity of 10 countries formed International Accounting Standards Committee (IASC) in 1973 and it issued International Accounting Standards. In 2001, the responsibility got transferred to IASB whereby standards were restructured and are now known as IFRS.
International Accounting Reporting Standards is a provider of information aiding n economic decisions, giving importance to preference and changes in the financial position of an entity.
Accounting Standards, when in conflict with court's decision are respected. India needs major improvements in Accounting Standards. More than 100 countries now require changing and many are in the way of replacing and accepting it.
It is mainly based on two concepts and are principle based on-

- Accrual
- Going concern.

Its framework is qualitative and characteristics are

- Understandability
- Relevance
- Reliability
- Comparability.

Indian Accounting Standards (abbreviated as India AS) are a set of accounting standards notified by the Ministry of Corporate Affairs, which are converged with International Financial Reporting Standards (IFRS). These accounting standards are formulated by the Accounting Standards Board of Institute of Chartered Accountants of India. Now India will have two sets of accounting standards viz. existing accounting standards under Companies (Accounting Standard) Rules, 2006 and IFRS converged Indian Accounting Standards (Indian AS). The Indian AS are named and numbered in the same way as the corresponding IFRS. NACAS recommend these standards to the Ministry of Corporate Affairs. The Ministry of Corporate Affairs has to spell out the accounting standards applicable for companies in India. As on date the Ministry of Corporate Affairs notified 35 Indian Accounting Standards (Indian AS). But it has not notified the date of implementation of the same.

2. Need for Convergence towards Global Standards

The last decade has witnessed a sea change in the global economic scenario. The emergence of transnational corporations in search of money, not only for fuelling growth, but to sustain ongoing activities has necessitated raising of capital from all parts of the world, cutting across frontiers.

Each country has its own set of rules and regulations for accounting and financial reporting, Therefore, when an enterprise decides to raise capital from the markets other than the country in which it is located, the rules and regulations of that other country will apply and this in turn will require that the enterprise is in a position to understand the differences between the rules governing financial reporting in the foreign country as compared to its own country of origin.

International analysts and investors would like to compare financial statements based on similar accounting standards, and this has led to the growing support for an internationally accepted set of accounting standards for cross border filings. The harmonization of financial reporting around the world will help to raise confidence of investors generally in the information they are using to make their decision and assess their risks.

A strong need was felt by legislation to bring about uniformity, rationalization, comparability, transparency and adaptability in financial statements. The better way for getting rid of problems faced by different methods of standards is to have a single set of global standards, of the highest quality, set in the interest of public.

The convergence of financial reporting and accounting standards is a valuable process that contributes to the free flow of global investment and achieves substantial benefits for all capital market stakeholders. It improves the ability of investors to compare investments on a global basis and thus lowers their risk of errors of judgment. It facilitates accounting and reporting for companies with global operations and eliminates some costly requirements say reinstatement of financial statements. It has the potential to create a new standard of accountability and greater transparency, which are values of great significance to all market participants including regulators. It reduces operational challenges for accounting firms and focuses their value and expertise standard setters and other stakeholders to improve the reporting model.

3. International Accounting Standards Board

With the view of making the financial statements more reliable and transparent , the London based group namely the International Accounting Standards Committee(IASC), responsible for developing International Accounting Standards , was established in June, 1973. Between1973-2001, the International Accounting Standards Committee (IASC) released International Accounting Standards. Between 1997 and 1999, the IASC restructured their organization, which resulted in formation of International Accounting Standards Board (IASB). These changes came into effect from 1st, April, 2001. IASB publishes its standards in a series of pronouncements called International Financial Reporting Standards.

4. International Financial Reporting Standards as Global Standards

The term IFRS comprises IFRS issued by IASB; IAS issued by International Accounting Standard Committee (IASC); and Interpretations issued by the standard Interpretations Committee (SIC) and the International Financial Reporting Interpretations Committee (IFRIC) of the IASB. International Financial Reporting Standards (IFRSs) are considered a "principles-based" set of standards. In fact, they establish broad rules rather than dictating specific treatments. Every major nation is moving toward adopting them to some extent .Large number of authorities require public companies to use IFRS for stock exchange listing companies to use IFRS for stock-exchange listing purposes, and in addition, banks, insurance companies and stock exchanges may use them for their statutory required reports. So over the next few years, thousands of companies will adopt the international standards. This requirement will affect about 7,000 enterprises, including their subsidiaries, equity investors and joint venture partners. The increased use of IFRS is not limited to public-company listing requirements or statutory reporting. Many lenders and regulatory and government bodies are looking to IFRS to fulfill local financial reporting obligations related to financing or licensing.

5. Comparison between IFRS and GAAP principles

Sl. no	Particulars	International Financial Reporting Standards	Indian Generally Accepted Accounting Principles
1.	Financial statements	Two years consolidated financial statements with exceptions in limited circumstances for entities which may present single entity parent company financial statements with CFS.	Single entity parent company-stand alone to present 2 years CFS and publish listed companies to prepare CFS with standalone financial statements.
2.	Position statements	No particular format unless liquidity presentation provides reliable information.	No particular format according to AS but prescribed by companies act and other industry regulations.
3.	Income statements	Expenditure is presented in one of the two formats- functions or nature otherwise no formats.	Disclosed in accordance with companies act and accounting standards. Industry specific formats are also available.
4.	Cash flow statement and format and methods	To use direct and indirect method with standard heading with limited guidance on items.	Same as International Financial Reporting Standards. Listed companies require indirect method And insurance companies require direct method.
5.	Cash and cash equivalents definition	Cash and equivalents with maturity of 3 months or less and includes bank overdraft	Same as IFRS but excludes bank overdraft
6.	Acquired intangible assets	If recognized-capitalist and to be amortized over useful life. If useful life is not certain to be reviewed for impairment for rare items revaluations are granted.	Same as IFRS but useful life not to exceed 10 years no revaluation to be done. More than 10-year test of impairment is necessary.
7.	Internal tangible assets	Research expenses are incurred cost. Capitalized and moralized. Development cost when specific areas is met.	Same
8.	Financial Assets	Held for maturity –carried at amortized cost.	Long term investments= cost less impairment, any reduction credited to income statements. Industries specified-banking, insurance.
9.	Liabilities-provision and general	Recorded if outflow can be correctly estimated and provable. Provision discounted to present value when time value is effected.	Same but discounting is not permitted.
10.	EPS(earning per share)	Share options and warrants attract treasury share method and for diluted earning per share weighted average potential dilutive shares are denominators.	Same. Only where advance shares application money if received is dilutive potential equity shares.
11.	Revenue recognition	Several criteria are applied with special reference to cases where risk and rewards have been transferred.	Conceptually difference arises.

Table 1

6. Adoption of IFRS in India

Increasingly, Indian accountants and businessmen feel the need for convergence with IFRS. Capital markets provide an important explanation for this change. Some Indian companies are already listed on overseas stock exchanges and many more will list in the future. Internationally acceptable accounting standards are becoming the language of communication for Indian companies.

To bring the Indian Standards at par with IAS/IFRS, some of the earlier Accounting Standards and Guidance Notes have been revised or are under the process of revision. However, at present, the Accounting Standard Board in consultation with the core group, constituted by the Ministry of Corporate Affairs (MICA) for convergence of Indian Accounting Standards (IFRS), has decided that there will be two separate sets of Accounting Standards.

6.1. Indian Accounting Standards converged with the IFRS(known as Ind AS)

The MCA has hosted 35 converged Indian Accounting Standards (Ind 'AS') without announcing the applicability date. These are the standards which are being converged by eliminating the differences of the Indian Accounting Standards vis-à-vis.

6.2. Existing Accounting Standards

The entities not falling within the threshold limits prescribed for IFRS compliance in the respective phases shall continue to use these standards in the preparation and presentation of financial statements.

7. Recent Trends of IFRS in India

After the enactment of the Companies Act, 2013, the ministry of corporate affairs has now shifted its focus on rolling out international reporting standards for Indian companies which were to be implemented beginning April 1, 2011.

According to the draft plan, the ministry wants to implement the international financial reporting standards (IFRS) beginning with companies that have a net worth of over Rs 1,000 crore from April 1, 2015, an official told The Indian Express.

In the second phase, both listed and unlisted companies with a net worth of over Rs 500 crore but less than Rs 1,000 crore will have to converge with the international accounting standards from the financial year beginning April 1, 2016.

IFRS had been put on the back burner by the government given issues raised by corporates, and unresolved taxation issues. Industry bodies had sought postponement arguing the industry needed more time to prepare.

The IFRS-converged accounting standards deal with mark-to-market projections and valuation of financial assets among other things.

The implementation is expected to cause some upheaval in companies' finances in the initial stage as the standards call for projecting assets' real value. Various sectors, including banking and real estate would be hit, experts have argued.

"The Institute of Chartered Accountants of India (ICAI) has been asked to conduct a sector-wise study, elaborating on the impact the implementation will have on the sectors," the official said.

As such, all Indian companies listed overseas or doing business on foreign land currently prepare financial statements as per the international standards.

However, banking companies would be exempt from complying with the IFRS. In the third and fourth phase, beginning April 1, 2017, smaller companies would need to prepare their accounts as per the international standards.

The main sectors which are likely to be impacted include oil and gas, finance, telecom and infrastructure companies. Over 100 countries have accepted IFRS while India has converged its accounting standards with the international reporting standards. Currently, the US, Japan and India are the three main economies that have not adopted IFRS while Canada, Brazil and Russia switched to IFRS last year.

8. Benefits and Challenges

The move to IFRS it not just a technical accounting exercise. It is an exercise in change management and offers opportunities for improvement. IFRS conversion offers companies an opportunity to improve their business in several ways.

The company can:

- Reshape its management reporting systems to better manage both its financial accounting and its financial statement generation and provide company leadership with essential information
- Improve disclosure — to analysts, investors, regulators and other stakeholders — of your company's financial results and position and other performance indicators
- Improve the metrics used to evaluate both company and executive performance
- Benchmark itself against its global peers
- Ensure all finance team members have the training, knowledge and skills needed to perform their roles
- Make accounting policy choices that are aligned with global industry practice

9. IFRS: The Impact on Indian Corporate

The use of international financial reporting standards (IFRS) as a universal financial reporting language is gaining momentum across the globe. Over a 100 countries in the European Union, Africa, West Asia and Asia-Pacific regions either require or permit the use of IFRS. The Institute of Chartered Accountants of India (ICAI) has recently released a concept paper on Convergence with IFRS in India, detailing the strategy for adoption of IFRS in India with effect from April 1, 2011. This has been strengthened by a recent announcement from the ministry of corporate affairs (MCA) confirming the agenda for convergence with IFRS in India by 2011. Even in the US there is an ongoing debate regarding the adoption of IFRS replacing US GAAP.

Adopting IFRS by Indian corporates is going to be very challenging but at the same time could also be rewarding. Indian corporate is likely to reap significant benefits from adopting IFRS. The European Union's experience highlights many perceived benefits as a result of adopting IFRS. Overall, most investors, financial statement preparers and auditors were in agreement that IFRS improved the quality of financial statements and that IFRS implementation was a positive development for EU financial reporting (2007 ICAEW Report on 'EU Implementation of IFRS and the Fair Value Directive'.

There are likely to be several benefits to corporates in the Indian context as well. These are:

- Improvement in comparability of financial information and financial performance with global peers and industry standards. This will result in more transparent financial reporting of a company's activities which will benefit investors, customers and other key stakeholders in India and overseas;
- The adoption of IFRS is expected to result in better quality of financial reporting due to consistent application of accounting principles and improvement in reliability of financial statements. This, in turn, will lead to increased trust and reliance placed by investors, analysts and other stakeholders in a company's financial statements; and
- Better access to and reduction in the cost of capital raised from global capital markets since IFRS are now accepted as a financial reporting framework for companies seeking to raise funds from most capital markets across the globe. A recent decision by the US Securities and Exchange Commission (SEC) permits foreign companies listed in the US to present financial statements in accordance with IFRS. This means that such companies will not be required to prepare separate

financial statements under Generally Accepted Accounting Principles in the US (US GAAP). Therefore, Indian companies listed in the US would benefit from having to prepare only a single set of IFRS compliant financial statements, and the consequent saving in financial and compliance costs.

However, the perceived benefits from IFRS adoption are based on the experience of IFRS compliant countries in a period of mild economic conditions. The current decline in market confidence in India and overseas coupled with tougher economic conditions may present significant challenges to Indian companies.

IFRS requires application of fair value principles in certain situations and this would result in significant differences from financial information currently presented, especially relating to financial instruments and business combinations. Given the current economic scenario, this could result in significant volatility in reported earnings and key performance measures like EPS and P/E ratios. Indian companies will have to build awareness amongst investors and analysts to explain the reasons for this volatility in order to improve understanding, and increase transparency and reliability of their financial statements.

This situation is worsened by the lack of availability of professionals with adequate valuation skills, to assist Indian corporates in arriving at reliable fair value estimates. This is a significant resource constraint that could impact comparability of financial statements and render some of the benefits of IFRS adoption ineffective.

Although IFRS are principles-based standards, they offer certain accounting policy choices to preparers of financial statements. For example, the use of a cost-based model or a revaluation model in accounting for investment properties. This could reduce consistency and comparability of financial information to a certain extent and therefore reduce some of the benefits from IFRS adoption. IFRS are formulated by the International Accounting Standards Board (IASB) which is an international standard-setting body.

However, the responsibility for enforcement and providing guidance on implementation vests with local government and accounting regulatory bodies, such as the ICAI in India. Consequently, there may be differences in interpretation or practical application of IFRS provisions, which could further reduce consistency in financial reporting and comparability with global peers. The ICAI will have to make adequate investments and build infrastructure to ensure compliance with IFRS.

10. In Addition to the Above, there are Several Impediments and Practical Challenges to Adoption of and Full Compliance with IFRS in India. These are

- The need for a change in several laws and regulations governing financial accounting and reporting in India. In addition to accounting standards, there are legal and regulatory requirements that determine the manner in which financial information is reported or presented in financial statements. For example, the Companies Act, 1956 determines the classification and accounting treatment for redeemable preference shares as equity instruments of a company, whereas these may be considered to be a financial liability under IFRS. The Companies Act (Schedule VI) also prescribes the format for presentation of financial statements for Indian companies, whereas the presentation requirements are significantly different under IFRS. Similarly, the Reserve Bank of India regulates the financial reporting for banks and other financial institutions, including the presentation format and accounting treatment for certain types of transactions.
- The recent announcement by the MCA is encouraging as it indicates government support for the timetable for convergence with IFRS in India. However, the announcement stops short of endorsing the roadmap for convergence and the full adoption of IFRS that is discussed in ICAI's concept paper. In the absence of adequate clarity and assurance that Indian laws and regulations will be amended to conform to IFRS, the conversion process may not gain momentum
- There is a lack of adequate professionals with practical IFRS conversion experience and therefore many companies will have to rely on external advisers and their auditors. This is magnified by a lack of preparedness amongst Indian corporates as this project may be viewed simply as a project management or an accounting issue which can be left to the finance function and auditors. However, it should be noted that IFRS conversion will involve a fundamental change to an entity's financial reporting systems and processes. It will require a detailed knowledge of the standards and the ability to consider their impact on business transactions and performance measures. Further, the conversion process will need to disseminate and embed IFRS knowledge throughout the organization to ensure its application on an ongoing basis.
- Another potential pitfall is viewing IFRS accounting rules as "similar" to Generally Accepted Accounting Principles in India (Indian GAAP), since Indian accounting standards have been formulated on the basis of principles in IFRS. However, this view disregards significant differences between Indian GAAP and IFRS as well as differences in practical implementation and interpretation of similar standards. Further, certain Indian standards offer accounting policy choices which are not available under IFRS, for example, use of pooling of interests method in accounting for business combinations.

There is an urgent need to address these challenges and work towards full adoption of IFRS in India. The most significant need is to build adequate IFRS skills and an expansive knowledge base amongst Indian accounting professionals to manage the conversion projects for Indian corporates. This can be done by leveraging the knowledge and experience gained from IFRS conversion in other countries and incorporating IFRS into the curriculum for professional accounting courses. Ultimately, it is imperative for Indian corporates to improve their preparedness for IFRS adoption and get the conversion process right. Given the current market conditions, any restatement of results due to errors in the conversion process would be detrimental to the company involved and would severely damage investor confidence in the financial system.

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