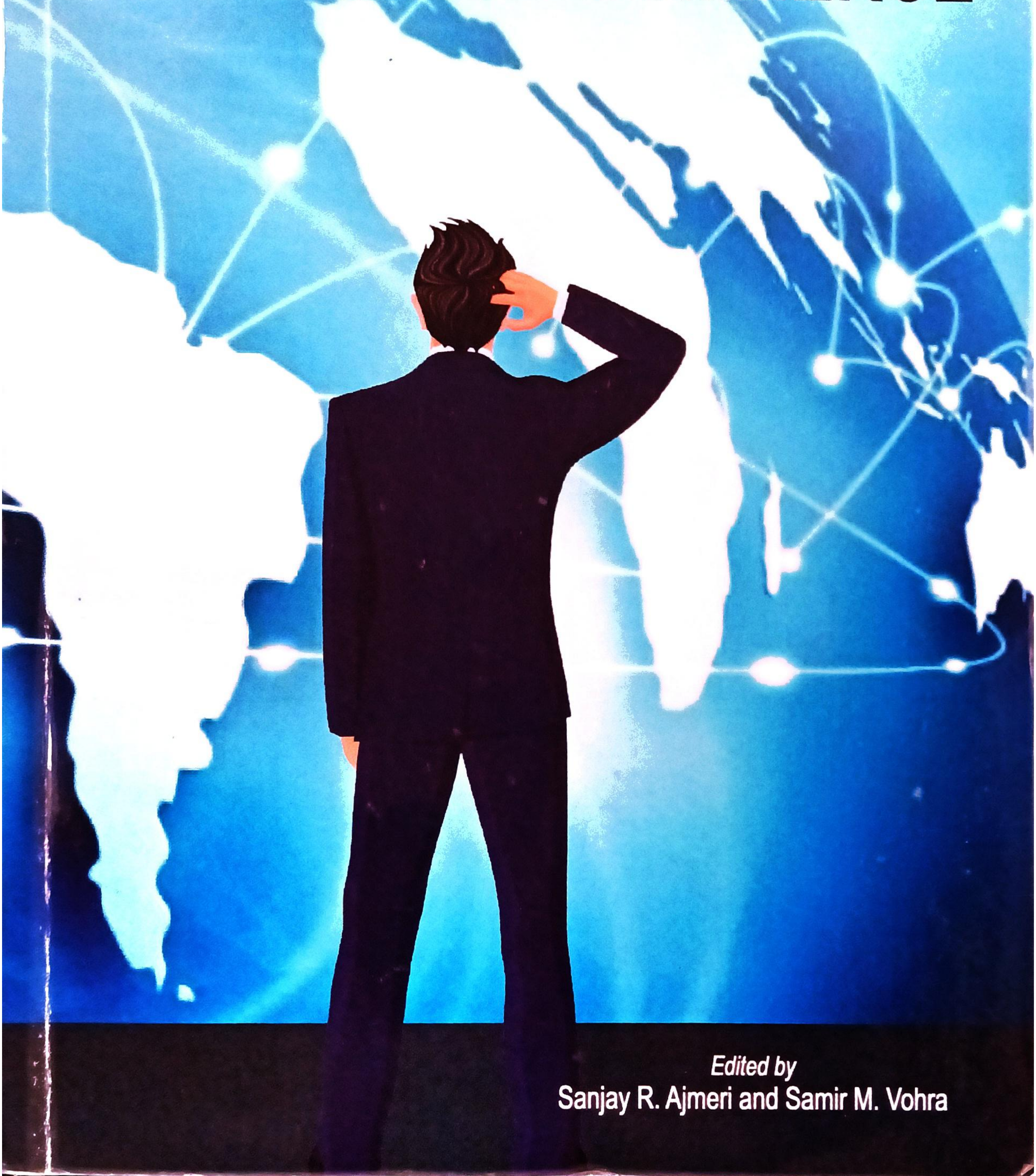
EMERGING TRENDS IN INTERNATIONAL BUSINESS AND COMMERCE



Edited by
Sanjay R. Ajmeri and Samir M. Vohra

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Contents

A Study on IFRS in India: Issues, Challenges and Suggestions

Vaibhav B. Barodiya[1]

1. INTRODUCTION

Accounting fraternity of 10 countries formed International Accounting Standards Committee (IASC) in 1973 and it issued International Accounting Standards. The objective of setting IASC was to formulate and publish in the public interest standards to be observed in preparation of audited financial statements and to promote their world wide acceptance and observance. 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 in economic decisions, giving importance to préférence 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 it 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 and Comparability. IFRS Standards deals with this confront by providing a set of Accounting standard of High quality as well as internationally acceptable which will also bring Transparence, Accountability and Efficiency to Financial markets of world. **Transparency** by intensifying the comparability and quality of Financial information which will enable international investors and other market participants to make well-versed economic decisions, **Accountability** by plummeting the information gap between the capital providers and capital users and **Efficiency** by helping the investors to find out favorable openings and risks related to it which will improve capital allocation.

IFRS—International Financial Reporting Standards (IFRS) are a set of Accounting standards developed by the IASB that is becoming the global standard for the preparation and disclosure of public company financial

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statements. IFRS being a single set of worldwide standards, simplified Accounting procedures by allowing a company to use one Reporting language that will be recognized globally.

International Accounting Standards Board (IASB)—With the view of making the financial statements more transparent, efficient and steadfast, the London based group—International Accounting Standards Committee (IASC), developed International Accounting Standards which was established in June, 1973. Between 1997 and 1999, the IASC rationalized their organization and formed the IASB. These changes came into effect from 1st, April, 2001, IASB publishes its standards in a series of announcement and label it as International Financial Reporting Standards (IFRS).

IndAS—IFRS are now becoming universally accepted Reporting language of Accounting standards. In the swing of global trend the Government of India declared the convergence of the Indian Accounting Standards with IFRS by 1st April, 2011. The formal notification of Indian Accounting Standards (IndAS) was issued by the Ministry of Corporate Affairs (MCA) on 20 February 2015. Approximately 39 new Accounting standards have been notified to converge with the globally recognized and accepted IFRS.

The objectives of the study are (a) to comprehend the applicability, implication and prospects of IFRS; (b) to encompass the present scenario and the adoption phases of IFRS in India; (c) to embrace the challenges faced by corporate firms in adopting IFRS and IndAS, (d) To explore the current status of IFRS convergence in India, and (e) to examine the benefits and challenges of convergence of IFRS.

2. FINDINGS

IFRS Position in India

A company having presence in different countries has to prepare financial reports as per Generally Accepted Accounting Principles (GAAP) of the country of operation which is then required to reconcile for the purpose of consolidation as per the Accounting Standards of the country to which the parent company belongs. This has raised the issue of harmonization of accounting policies, presentation, disclosure etc. Harmonization of accounting standards has become a highly demanded issue of discussion and debate among accounting professionals around the globe. The use of International Financial Reporting Standards (IFRS) as a universal financial reporting language is gaining thrust across the globe. Adopting IFRS by Indian corporate 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.

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 financial reporting. There are likely to be several benefits to corporate in the Indian context. 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.

It is imperative for companies which have already performed a diagnostic study for IFRS to revisit their diagnostic study, as IFRS itself is a moving target and gets regularly updated. Companies also need to consider that some IFRS may not be applicable when the diagnostic study is in process, but their applicability in future may result in material changes to the financials. Understanding IFRS and its implications is a business imperative for Indian companies.

In March 2014, the Institute of Chartered Accountants of India (ICAI) submitted to Ministry of Corporate Affairs (MCA) a proposed new IFRS roadmap and convergence plan for India. In the proposed roadmap, the ICAI recommended implementation of Ind AS by select companies only in preparation of their consolidated financial statements. In July 2014, the Finance Minister in his Budget speech proposed the adoption of the new Indian Accounting Standards (Ind AS—the converged IFRS standards) by Indian Companies Voluntarily from FY 2015–16 and mandatory from FY 2016–17.

Prospects of Adoption of IFRS Converge 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. The convergence of IFRS into IndAS is a very important process that contributes to the free flow of international investment and attains significant benefits for all capital market stakeholders. It improves the aptitude of investors to compare investments on a global base and also decreases their risk of errors of judgment. The benefits of IFRS convergence to IndAS are:

- The adoption of IFRS is anticipated to provide better outcome in respect of quality of financial reporting as there is continuous application of accounting principles. It will lead to increased trust, reliability and confidence among investors, analysts and other stakeholders in a company's financial statements.
- Transparency, easy accessibility with reduced cost of capital increases the global capital markets as IFRS are now accepted as a financial reporting framework for companies.
- The accounting professionals are able to work in different parts of the globe which will increase the scope of accounting professionals in industry as well as in practice.
- With adoption of IFRS Stock exchanges have possibility of heavy profit as more companies will be eligible for listing.
- Internationally acceptable accounting standards become the language of communication for Indian companies which increases listed Indian companies in overseas stock exchanges.

IFRS Convergence in India

IFRS convergence, in recent years, has gained momentum all over the world. As capital markets become increasingly global in nature, more and more investors see the need for a common set of accounting standards. Approximately 100 countries have adopted and many have converged IFRS with their own standards.

Table 1: IFRS Convergence in Some Countries

Sr. No	*Country*	*Implementation Year*
1.	U K	2005
2.	Canada	2011
3.	USA	2016
4.	Japan	2016
5.	Nepal	2011
6.	Brazil	2010
7.	India	2016

In India, Accounting standards are formulated by Council of Institute of Chartered Accountants of India (ICAI). In July 2007, ICAI set a Target of adopting IFRS for all listed, public Interest and large size entities from April 2011. In 2007 India decided to converge to IFRS. The Accounting standards that are converged with IFRS are known as Indian AS. Thus in India Indian Accounting Standard Board and IASB continue to collaborate together to develop High quality, compatible Accounting standards rather than adopting IFRS by itself. In India Ministry of Corporate Affairs has Announced the Implementation of new standards effective from 1st April 2016 in a phased manner. Existing standards will cease to apply after that dates. The Ministry of Corporate Affairs notified the implementation plan in a phased manner over a period of four years. i.e., From 1st April 2016 to 1st April 2019. This leads to the necessity of learning new standards at the earliest.

Recent Trends and Situation 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 ₹ 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 ₹ 500 crore but less than ₹ 1,000 crore will have to converge with the international Accounting standards from the financial Years 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.

However, banking companies would be exempt from compliance 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.

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 statements 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.
- 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.

Benefits of IFRS

The Economy

When the Market expands globally the need for convergence increases since the convergence benefits the economy by increasing growth of its international business. It facilitates maintenance of orderly and efficient capital markets and also helps to increase the capital formation and thereby economic growth.

The Industry

The other important set of beneficiary as the researchers perceive is the industry which in the event of convergence with IFRS will be benefited because of, one, increased confidence in the minds of the foreign investors, two, decreased burden of financial reporting, three, it would simplify the process of preparing the individual and group financial statements and four, it leads to lower cost of preparing the financial statements using different sets of accounting standards.

Accounting Professionals

Although there would be initial teething problems, convergence with IFRS would definitely benefit the accounting professionals as the latter would then be able to sell their expertise in various parts of the world.

Investors

Financial statements prepared using a common set of accounting standards help investors better understand investment opportunities as opposed to financial statements prepared using a different set of national accounting standards. Investors' confidence is strong when accounting standards used are globally accepted. Convergence with IFRS contributes to investors' understanding and confidence in high quality financial statements.

The Corporate World

Convergence with IFRS would raise the reputation and relationship of the Indian corporate world with the international financial community. Moreover, the corporate houses back in India would be benefited because of one, achievement of higher level of consistency between the internal and external reporting, two, because of better access to international market, and three, convergence with IFRS improves the risk rating and makes the corporate world more competitive globally as their comparability with the international competitors increases.

Improved Consistency and Transparency of Financial Reporting

This factor can also be mentioned as one of the crucial advantages of converting to IFRS as it makes the EU member countries to be consistent not only on macroeconomic aspects, but also on financial reporting which improves relationship between investors and companies among member countries.

Better Access to Foreign Capital Markets and Investments

As thousands of companies in Europe and other joining countries across the world has already created a huge base for IFRS adoption, it also improves the companies, access to financial markets by having the financial statements prepared under one reporting standard. One of the main reasons for converting from previously used GAAP to new IFRS was for improving comparability in international financial markets, thus increasing the focus on investors. And this has been mainly achieved and still going to be achieved as more and more countries around the world have been converting to IFRS from their national reporting standard.

Standardization of Accounting and Financial Reporting

The most mentioned factor about the advantages of IFRS has been the standardization of financial reporting which eventually improves the comparability of financial statements in major financial markets. This also removes the trade barrier, as this was one of the key factors as to why the EU has been trying to adopt single reporting standards.

Some Key Challenges to Implementation

As in the case of two sides of a coin, along with utilities it also consists of challenges for the Indian firms. They are following:

1. *Difference in GAAP and IFRS:* Adoption of IFRS means that the entire set of financial statements will be required to undergo a drastic change. The differences are wide and very deep rooted. It would be a

challenge to bring about awareness of IFRS and its impact among the users of financial statements.

2. *Impact on Financial Results:* Financial reports will experience a lot of changes. For example treatment of depreciation differs. Hence, the value of assets as well as the profitability of the organization may swing, which, in turn, may impact the net worth.
3. *User Awareness, Training and Education:* Many people are yet not aware of IFRS, their complexities and impact. A change in the reporting format will require awareness of these new norms and systems, training and education, both for the professional as well as the user. There is a need to impart education and training on IFRS and its application.
4. *Legal and Regulatory Considerations:* Presently, the financial reporting requirements are authorized by various regulatory authorities in India and their provisions override other laws and regulators. IFRS does not recognize such overriding laws. So, such laws and regulation in India will create challenges to IFRS and its application.
5. *Awareness of International Practices:* The entire set of financial reporting practices needs to undergo a drastic change after the adoption of IFRS to overcome the number of differences between the two GAAP's. It would be a challenge to bring about awareness of IFRS and its impact among the users of financial statements.
6. *Fair value Measurement:* IFRS uses fair value as a measurement base for valuing most of the items of financial statements. The use of fair value accounting can bring a lot of instability and prejudice to the financial statements. It also involves a lot of hard work in arriving at the fair value and valuation experts have to be consulted.
7. *Taxation:* Present scenario, Indian Tax laws do not recognize the Accounting Standards. To entertain immediate change in the Indian Tax Law is the major challenge faced by the Indian Law makers.
8. *Financial Reporting System:* In India financial reporting is done according to standards issued by ICAI (Institute of Chartered Accountants of India). We need to amend the same to suit the requirements of IFRS. The information systems should be designed to capture new requirements related to fixed assets, segment disclosures, related party transactions etc.
9. *Renegotiation of Contract:* The contracts would have to be renegotiated which is also a big challenge. This is because the financial results under IFRS are likely to be very different from those under the Indian GAAP.

Suggestions for Successful Implementation of IFRS

- Intensive training, conferences, seminars, workshops from the experts to bridge the gap between Trained Professionals required and trained professionals available. IFRS should be incubated as a compulsory part in the academic curriculum.
- In keeping with international best practices, IFRS under the auspices of IASB should take cognizance of the GAAP of different countries in its subsequent review so that users can benefit globally.
- Tax authorities should reflect on IFRS implications on direct and indirect taxes. IFRS should provide clear/appropriate guidelines from a tax perspective.
- It should be made compulsory for the companies to prepare IFRS compliant statements as well as Indian GAAP compliant statements, which will help in tracing problems likely to be happen in advance and corrected as much as possible.
- IFRS should be included in curriculum at universities, polytechnics and at UG Level so as to build human capacity that will support the preparation of financial statements in an organization.
- IASB should announce standards, take proper feedback from the accounting profession, member countries and corporate management.
- IASB should support member bodies to adopt IFRS and formulate and reformulate their rules as to eradicate upcoming hurdles.
- Local stock exchange and other governing bodies of various accounting profession should cooperate in taking action against companies that fail to comply with the IFRS.

3. CONCLUSION

From the above discussion it is very much clear that transition from Indian GAAP to IFRS will face many difficulties but at the same time looking at the advantages that this adoption will confer, the convergence with IFRS is strongly recommended. We have also seen that this transition is not without difficulties as to the proper implementation process which would require a complete change in formats of accounts, accounting policies and more extensive disclosure requirements. There is a crucial need to deal with the challenges and work towards full adoption of IFRS by implementing the roadmap in India. The most significant need is to build adequate IFRS skills and an extensive knowledge amongst Indian accounting professionals to supervise the conversion projects for the Indian corporate. Convergence to IFRS is expected to improve the relevance, transparency, reliability and comparability of financial reports and benefit global investors. Adoption of IFRS requires commitment and dedication from various stakeholders to promote international convergence of accounting. Thus to implement IFRS successfully and efficiently, a high level of mutual international understanding about corporate targets, financial reporting targets and harmonization targets need to be achieved.

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About the Book

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