Indian accounting system and international financial reporting standards accounti...

1. History: The roots of accounting system in India had been evolved in early sixteenth century when India had built trade links with Europe and central Asia. Later, with entry of east India company had made a huge impact on trade and commerce of India. The British raj (rule) states that the accounting and financial practice between India and England was almost similar. Moreover at the time of independence India in 1947, there were some changes in accounting practices to match up to the Indian economy. The accounting practice varies from different small unorganized rural areas and small scale urban industrial sector. In India, large number of businesses is having a conservative outlook and don't want to disclose any financial information regarding their company due to having fear competitors and maintain privacy (Perumpral, S. E. et al. 2009).

1. 1 Significant changes in economy: Indian economy policy has seen an important change in the year 1991, when the government had liberalized the economy for foreign collaborations and investments. Some segments of the public sector which were previously with government were privatized. With this significant change India emerged as a major country in export of industrial and consumer goods, etc. With this first stage of globalization also gave the opportunity to interact with major international organizations like United Nations, the world bank and many more. Still the public sector has an important place in Indian economy as all industries that are manufacturing to serve national defence is with Indian government (Perumpral, S. E. et al. 2009).

2. Current Accounting practice in India: All the accounting practices done by the public and the organized private sector companies are based on the

rules of The Companies Act, 1956, and in many criteria they are similar to International Accounting Standards. The important amendments in this act which are modified are in the years 1965 and 1969, which introduced the rules and regulations of preparing cost accounts and the cost audit requirements. There have always been research efforts from some organizations to match the changing need of accounting system with rapidly changing economic environment. These organizations include ‘ Indian accounting association’, ‘ Indian council of social science research’ and ‘ Institute of Chartered Accountants of India’ (ICAI). Besides all these organizations there is always been a cultural and political influence on Indian accounting practices (Perumpral, S. E. et al. 2009).

2. 1 Role of ICAI: Institute of Chartered Accountants of India (ICAI) is a legal body came into existence under chartered accountants act of 1949 (more specifically Act no. XXXVIII of 1949), with the purpose for regulating the chartered accountants profession in India. As being a long existence in Indian economy ICAI has made it’s recognition as a leading accounting body because of it’s contribution in maintaining high accounting, auditing, providing education and setting up of ethical standards. Until now ICAI has issued 32 different standards (ICAI, 2010).

ICAI has again brought a significant change by introducing The Accounting Standard Board (ASB) in 1977, to harmonize diverse accounting practices of India and to bring them together to a common platform with the global practices (Shankaraiah, K. and Rao, D. N., 2004).

3. Harmonization of standards: Accounting standards deals with measuring system and contains rules for preparing and presenting financial statements. Under the global business environment there is need to develop a common accounting language that can be spoken and understood by all companies throughout the world. The financial reporting system should be of a global standard to attract foreign companies and also to access to more home investors; these all can be possible by harmonization of accounting standard. The goal behind setting standard is that they help in bringing uniformity in financial reporting and also makes it more comparable and consistent (Bharathan, V., 2005).

3. 1 Issues with divergent accounting practices: Accounting differences causes problem in valuation and thus in the decision making process. It also puts additional costs of financial reporting and leads to difficulties for multinational companies in interpreting transactions. For example, By the end of the financial period in 1994, British telecom according to UK GAAP accounted a net profit of £1767, but under the rules of US GAAP it reduced to £1476. These qualitative differences can only be eliminated using internationally accepted single set of standards (Bharathan, V., 2005).

4. Criticisms to current Indian accounting standard: There are some criticisms to Indian accounting standards as, that they are very broadly based and general that gives chance to use similar accounting methods for similar events. For example, the accounting for expenses which are incurred under a scheme called voluntary retirement scheme, in which one can use the different methods ranging from present value amortization of future pension to pay as you go method. Another reason for divergent accounting

practices in India is lack of coordination between companies act 1956 of India, income tax act 1961 provisions and accounting standard. Though in India at present, ICAI sets the accounting standard but in the process of preparing standards one could easily see the lack of interest by company legislation in the planning of accounting rules. This resulted in several gaps in requirement of company law concerning financial statements like earning per share, mergers, future cash flow information etc. (Bharathan, V., 2005).

Before the period of 1990's, Indian companies were not concerned towards corporate governance. In that period the companies, investors suffered from weak system with poor disclosure practices, lack of transparency but, that condition had started improving after the process of liberalization. The conditions further improved with the establishment of a committee on corporate governance by " Securities and exchange board of India" (SEBI) to raise the standard of governance of all the companies (Rajagopalan, R., 2003).

4. 1 Why global accounting standard?: According to IIM professor Mr. R. Narayanaswamy, in such developing stage where, Indian businesses are becoming global in their operations there is an important need to adopt global accounting standard and to overcome existing financial criticisms. The reason for adoption of such global standards as because of their quality, transparency and acceptability make them internationally recognized. By these global standards Indian companies can communicate more cost efficiently with other countries. Mr. Narayanaswamy also concerns about being ineffective monitoring of reporting entities. According to him, SEBI lacks in recruiting the kind technical staff they require. Another issue is that

there is no standard which serves to business combinations, the one AS 14 which is there- only deals with amalgamation, but many businesses come in contact by inter-company investments. The standards relating to revenue recognition, presentation of financial statements and many more are outdated and there is need to be reworked on them (Narayanaswamy, R., 2007).

5. IFRS: Is the accounting framework which are being set by standard setting private sector body, international accounting standard boards(IASB), which replaced IASC foundation in 2001 (IASB, 2010).

5. 1 Adoption of IFRS: Indian government and ICAI has decided to fully converge with international financial reporting standards (IFRS) and will be functional from April 1, 2011. The president of ICAI Ved Jain said, that the decision of following a common accounting standard is to help the investors who are seeking an opportunity to invest in different geographical areas as well. Currently more than 110 countries including china which have adopted IFRS practice. Also there many more countries like Japan, Canada which will start follow it soon (Financial Express, 2008). Budgets are being passed every year without meaningful discussions on important issues because of different views of different members. Only small amount of voices come up on that issues and yet they are being forced down (ICAI, 2009).

5. 2 Benefits of adopting IFRS: Adoption of IFRS will enable the Indian companies to have more easily access to international capital markets because many stock exchanges require or permit IFRS certified accounts. Currently, to list the securities abroad Indian companies have to prepare

another set of financial statements that are acceptable in the following country. IFRS will remove this requirement of preparing dual financial statements and thus reduces the cost of raising capital which was earlier costly form foreign markets. Preparation of financial statements according to IFRS will increase comparability and also enable foreign companies to develop more thorough understanding of financial statements of Indian companies. Besides the companies, the accountants of India will also gain more knowledge and experience in working with IFRS and now they would be globally acceptable. There are benefits for ICAI also as now it can focus more on empirical and theoretical research which can be beneficial for Indian accounting profession (Mercer, 2009) (appendix-1).

5. 3 Some further Amendments in applying IFRS in India: There are some standards of accounting for items like investment property, share based payments, minerals exploration, insurance contracts which requires amendment. The convergence process from Indian GAAP to IFRS will be achieved by several modifications in the current Indian accounting standards. For example, current Indian accounting standard (AS-14) which deals with amalgamations will be modified in accordance to IFRS 3 which is on business combinations and acquisitions. The new standards will be issued in those areas which the current Indian accounting standard does not cover. For example, a new standard has to be issue on share based payments to be according with IFRS 2. Indian standard setters will require to release somewhat, similar first time adoption standard that will be in conformity with IFRS 1. If any accounting standard can’t be converged to conformity of IFRS

because of not being according to Indian law or court order, then the provisions of the said law will exist (Khatri, J. 2009) (Appendix-2, 3).

All those listed public and private companies along with all those who are in process of being listed having revenues in excess of Rs. 100crore or whose borrowings exceeding Rs. 25crore needs to adopt IFRS. Also all of those private companies, which in the public market have issued debt instruments. Lastly all those private companies like banks, insurance companies holding assets in fiduciary capacity (Gajra, R., 2008).

5. 4 Complications in applying IFRS in India: The basic principle of IFRS is being based on “ fair value” accounting, whereas, Indian GAAP works on the basis of historical cost accounting. Further, to diminish any possible negative impact like renegotiating debt covenants there is a need to reconsider the management plans. The company management should take a right, practical and proactive approach in preparing their plans for the company from such a transition (Wadhwani, V., 2009).

According to Mr. Sai Venkateshwaran, the transition process from to IFRS will be complicated because, in India there will large number of companies which will be adopting IFRS. ICAI has taken the first step by issuing whitepaper which states the broad outline for this changeover. Besides these several more legislative changes like amendments to the companies act, rules and regulations of SEBI, the income tax act etc. have to be made. To add up to these the current accounting and the style of presentation guidance will be modified according to IFRS. Before applying IFRS all the different accounting bodies like ICAI, companies act, SEBI, income tax authorities and regulators like RBI(Reserve Bank Of India) should work together to prepare a regulatory landscape for this transition in 2011. Another challenge is to train large pool of resources like accountants from both industry and profession to obtain the objective of this transition (Giriprakash, K. And Varadarajan, V. K., 2008).

6. Conclusion: Indian financial system has seen many changes from starting, but with the outlook of within the nation, but now this historical change to adopt IFRS in India will enable it to use the same standards which the other counties in the world are using. To taste the full benefits of IFRS there should be more serious training of people who will be get affected by this transition and also proper implication of several amendments are required. India is already moving very rapidly in the growth in all the aspects whether it's in manufacturing, investing, exporting. Implications of IFRS will result in more increase in the rate of growth of India.

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