A Study on International Financial Reporting Standards (IFRS) Implementation Challenges and Opportunities – A Theoretical Review

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Abstract: *One of the foremost requirements to operate a Business successfully is to have a good financial reporting system in place. Keeping this in mind, Accounting Professionals and Accounting Bodies across the globe, during last decade, had tried to put a financial reporting system in place which is harmonized, robust and have extensive applicability. IASB (formerly IASC) came out with IFRS which were adopted formally by members of European Union in 2005. In subsequent years, many other countries either adopted IFRS or converged to IFRS. An upcoming economy on world economic map, India, too, decided to converge to IFRS. This study tries to analyze the information available on IFRS adoption process in India. It also discusses the IFRS adoption procedure in India and the utility for India in adopting IFRS. The paper discuss the problems faced by the stakeholders (Regulators, Accountants, Firms etc) in the process of adoption of IFRS in India. An upcoming economy on world economic map, India, too, decided to converge with IFRS by developing a standard called Ind AS. The purpose of the present paper is to know the awareness of stakeholders towards the implementation of IFRS in India and to know the impact of IFRS Convergence on Different Sectors. The researcher found that the different ways of understanding about IFRS and the results shows that there is a high requirement of knowledge as well as training towards IFRS and also results shows that a Lot of positive response from the different sectors towards the implementation process.*

Keywords: IFRS, Standard Setting, Uniform Accounting Standards, Financial Reporting , Accounting, International Financial Reporting Standards (IFRS)

I. INTRODUCTION

IFRS in INDIA: Convergence with IFRS: IFRSs issued by the IASB are not country specific. They are meant to be applied across the globe. However, each country has its own peculiarities and hence, convergence of IFRSs as they are, with certain modification, may be practicable and departures may have to be made primarily on account of the legal, regulatory and economic environment prevailing in the country. Convergence can be considered "to design and maintain national accounting standards in a way that financial statements prepared in accordance with national accounting standards draw unreserved statement of compliance with IFRSs". In this context, attention is drawn to paragraph 14 of International Accounting Standard (IAS) 1, Presentation of Financial Statements, which states that financial statements shall not be described as complying with IFRSs unless they comply with all the requirements of IFRSs. „Convergence with IFRSs‟ means adoption of IFRSs with the aforesaid exceptions, where necessary. In 2007 the Concept Paper was released which proposed Convergence of Accounting Standards in India with IFRS from April 2011. After going through various legal procedures and consultation, the Ministry of Corporate Affairs which regulates companies in India has issued a Roadmap for Convergence with IFRS in India in January 2010 and has notified 35 accounting standards called as IND AS in February 2011 for the convergence process. New road map for the process of convergence. On 16th February2015, Ministry of Corporate Affairs has announced a new road map for the implementation of New Indian Accounting Standards (Ind AS) with effect from 1st April 2015 as voluntarily basis and from 1st April 2016 as mandatorily. ICAI has issued 39 accounting standards converged with IFRS (Annexure 1). The insurance companies, banking companies and non-banking finance companies shall not be required to apply Indian Accounting Standards (Ind AS) for preparation of their financial statements either voluntarily or mandatorily as per MCA notification.

II. REVIEW OF LITERATURE

The adoption of a common body of international standards is helps in lower cost of financial information processing and auditing to capital market participants. Comparability and uniformity of financial statements among companies and countries making the work of investment analysts easy, attraction of foreign investors in addition to general capital market liberalization. Ball (2006) stated that many developing countries where the quality of local governance institutions is low, the decision to adopt IFRS will be beneficial. Findings showed (Kenneth Enoch Okpala 2012) that IFRS has been adopted in Nigeria perceived that IFRS implementation will promote FDI inflows and economic growth and it was recommended that all stakeholders should endeavor to have full implementation to reap benefits of the global GAAP and principle - based standards. Increasing volume of cross border capital flows and the growing number of foreign direct investments via mergers and acquisitions in the globalization era, the need for the harmonization of different practices in accounting and the acceptance of worldwide standards has arisen (Akinyemi Olumide Akindele, 2012).The observation of the balance sheet revealed differences in respect of Intangible Assets, Available for Sale financial assets, Interest Bearing Loans, Provisions, Deferred Tax Liability, Provisions under Current liabilities, and General Reserve.(Dr. M. Jayasree, 2012). The results confirm that the application of fair-value for derivative instruments and new rules for accounting for goodwill.(Jordi Perramon). The result obtained that increase in Profitability ratios, liquidity ratio noted less significant, but still quite substantial increase, and however, one market-based ratio (P/E ratio) noted slight decrease after the conversion to IFRS. The obtained results indicate that the increase in profitability ratios and decrease in P/E ratio are due to very high income statement profits under IFRS.(Pawel Punda 2011). The valuation and depreciation of property, plant and equipment is also a big cause of difference (Dr Vidhi Bhargava, 2013). The results (Rahul Kamath, 2014) reveals that the financial indicators, investment activities

Chand & White (2007) in their paper on convergence of Domestic Accounting Standards and IFRS, demonstrated that the influence of Multinational Enterprises and large international accounting firms can lead to transfer of economic resources in their favour, wherein the public interests are usually ignored. The study carried out by Callao et al (2007) on financial data of Spanish firms revealed that local comparability is adversely affected if both IFRS and local Accounting Standards are applied in the same country at the same time. The study, therefore calls for an urgent convergence of local Accounting Standards with that of IFRS. Barth et al (2008) in their study of financial data of firms from 21 countries examined whether application of IAS/IFRS is associated with higher accounting quality. The findings of the study confirmed that firms applying IAS/IFRS evidence less earnings management, more timely loss recognition and more relevance of accounting numbers. The study also found out that the Firms applying IAS/IFRS experienced an improvement in accounting quality between the pre-adoption and post adoption period. Referring to a study carried out by Audit Integrity, Steffee (2009) in his article concluded that there are considerable differences in the approaches taken to implementing IFRS by individual Western European countries and companies. He viewed that corporations in Luxembourg, Austria and Switzerland demonstrate the most transparent accounting practices and best corporate governance, while European Banks with large capitalizations display very aggressive Accounting and Poor

The study is primarily qualitative in nature and do not use any quantitative tool to analyze the data. It has been conducted mainly on the basis of literature survey and secondary Information. Various journals, newspaper and magazines articles have been referred to in writing this paper.

III. The objectives of this study can be listed down as below:

- To discuss the IFRS adoption procedure in India;
- To discuss the utility for India in adopting IFRS;
- To discuss the problems faced by the stakeholders in the process of adoption of IFRS in India; and

- To discuss the ways through which these problems can be addressed.

IV. THEORETICAL ANALYSIS AND DISCUSSION

IFRS Adoption Procedure in India

In 1949, Indian government to streamline accounting practices in the country established Institute of Chartered Accountants of India by passing ICAI Act, 1949. Accounting Standard Board was constituted by ICAI in 1977 with a view to harmonize the diverse accounting policies and practices in India. The other objectives of the Board are: (i) conceive of and suggest new areas in which Accounting Standards are needed, formulation of Accounting Standards, (iii) examine how far IAS and IFRS can be adapted while formulating the accounting standards and to adapt the same [vii], and (iv) review the existing Accounting Standards and revise them regularly as and when necessary, among others. In 2006, a task force was set up by ICAI. The objective of the task force was to lay down a road map for convergence of IFRS in India.

Step 1 – IFRS Impact Assessment

In this step, the firm will begin with the assessment of the impact of IFRS adoption on Accounting and Reporting Issues, on systems and processes, and on Business of the firm. The firm will then identify the key conversion dates and accordingly a IFRS training plan will be laid down. Once the training plan is in place, the firm will have to identify the key Financial Reporting Standards that will apply to the firm and also the differences among current financial reporting standards being followed by the firm and IFRS. The firm will also identify the loopholes in the existing systems and processes.

Step 2 – Preparations for IFRS Implementation

This step will carry out the activities required for IFRS implementation process. It will begin with documentation of IFRS Accounting Manual. The firm will than revamp the internal reporting systems and processes. IFRS 1 which deals with the first time adoption of IFRS will be followed to guide through the first time IFRS adoption procedure. To make the convergence process smooth, some exemptions are available under IFRS 1.These exemptions are identified and applied. To ensure that the IFRS are applied correctly and consistently, control systems are designed and put in place.

Step 3 – Implementation

This step involves actual implementation of IFRS. The first activity carried out in this phase is to prepare an opening Balance Sheet at the date of transition to IFRS.A proper understanding of the impact of the transition from Indian Accounting Standards to IFRS is to be developed. This will follow the complete application of IFRS as and when required. First time implementation of IFRS requires lot of training and some difficulties may also be experienced. To ensure a smooth transition from Indian Accounting Standards to IFRS, Continuous training to staff and addressing all the difficulties that would be experienced while carrying out the implementation is also required.

Utility for India in Adopting IFRS

Economies across the globe have benefitted by adopting IFRS for financial reporting purposes. Previous Studies have suggested various benefits of adopting IFRS, notably, Better financial information for shareholders, Better financial information for regulators, Enhanced comparability, Improved transparency of results, Increased ability to secure cross-border listing, Better Management of global operations and Decreased cost of capital. This study will try to connect some of these and few other benefits with respect to the firms in India and also India as a country.

Challenges in the Process of Adoption of IFRS in India

Institute of Chartered Accountants of India set up a task force in 2006 to study and suggest a path for adoption of IFRS in India. On the basis of the recommendation of task force, a 3 phased programme (already discussed somewhere in this paper) has been initiated to adapt to IFRS in India. Accounting Professionals in India and across the world have listed various benefits of adopting IFRS. In spite of these benefits, adoption of IFRS in India is difficult task and faces many challenges.

Awareness of International Financial Reporting Practices

Adoption of IFRS means a complete set of different reporting standards have to bring in. The awareness of these reporting standards is still not there among the stakeholders like Firms, Banks, Stock Exchanges, Commodity Exchanges etc.. To bring a complete awareness of these standards among these parties is a difficult task.

Training

Professional Accountants are looked upon to ensure successful implementation of IFRS. Along with these Accountants, Government officials, Chief Executive Officers, Chief Information officers are also responsible for a smooth adoption process. India lack training facilities to train such a large group. As the implementation date draws closer (2011), It has been observed that India does not have enough number of fully trained professionals to carry out this task of adoption of IFRS in India.

Amendments to the Existing Laws

In India, Accounting Practices are governed mainly by Companies Act 1956 and Indian Generally Accepted Accounting Principles (GAAP). Existing laws such as Securities Exchange Board of India regulations, Indian Banking Laws & Regulations, Foreign Exchange Management Act also provide some guidelines on preparation of Financial Statements in India. IFRS does not recognize the presence of these laws and the Accountants will have to follow the IFRS fully with no overriding provisions from these laws. Indian Lawmakers will have to make necessary amendments to ensure a smooth transition to IFRS.

Taxation

IFRS adoption will affect most of the items in the Financial Statements and consequently, the tax liabilities would also undergo a change. Currently, Indian Tax Laws do not recognize the Accounting Standards. A complete overhaul of Tax laws is the major challenge faced by the Indian Law Makers immediately. Enough changes are to be made in Tax laws to ensure that tax authorities recognize IFRS-Compliant financial statements otherwise it will duplicate the administrative work for the Firms.

Use of Fair Value as Measurement Base

IFRS uses fair value to measure majority items in financial statements. The use of Fair Value Accounting can bring a lot of volatility and subjectivity to the financial statements. Adjustments to fair value result in gains or losses which are reflected in the Income Statements and valuation is reflected in Balance Sheet. Indian Corporate World which has been preparing its Financial Statements on Historical Cost Basis will have tough time while shifting to Fair Value Accounting.

Financial Reporting System

IFRS provide complete set of reporting system for companies to make their Financial Statements. In India, various laws and acts provide the financial reporting system but not as comprehensive as provided by the IFRS. Indian Firms will have to ensure that existing business reporting model is amended to suit the requirements of IFRS. The amended reporting system will take care of various new requirements of IFRS. Enough control systems have to be put in place to ensure the minimum business disruption at the time of transition. All the challenges mentioned here can be worked out by bringing a proper Internal Control & Reporting system in place. Firms, Regulators and Stock Exchanges in India should take some guidelines from the countries which have adopted the IFRS and have similar economic, political and social conditions.

V. Conclusion

Ensuring a high quality corporate financial reporting environment depends on effective Control & Enforcement Mechanism. Merely adopting International Financial Reporting Standards is not enough. Each interested party, namely Top Management and Directors of the Firms, Independent Auditors and Accountants and Regulators and Law Makers will have to come together and work as a team for a smooth IFRS adoption procedure. Top Management should ensure that the Financial Statements are prepared in compliance with the IFRS. Auditors and Accountants should prepare and audit Financial Statements in compliance with IFRS. Regulators and Law Makers must implement efficient monitoring system of regulatory compliance of IFRS. Along with this the Regulators should ensure that proper changes are to be made in existing laws for IFRS adoption process.

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