

THE IMPLICATION OF IFRS ON INDIAN BUSINESS

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ABSTRACT

Business is thinking and acting globally with global customer base, international quality standards and adoption of internationally accepted business practices. In India, we have an accounting system designed by ICAI (The Institute of Chartered Accountants of India). Once an Indian corporate is aiming at raising capital from a foreign market, then that corporate is forced to prepare its statements in a language accepted by foreign market. Currently GAAP (Generally Accepted Accounting Principles) and IFRS (International Financial Reporting Standards) are two domains widely accepted. This article tries to throw some light on the basics of IFRS, the challenges in implementing IFRS in India and the benefits it can offer to corporate world.

KEYWORDS: IFRS, FII, Indian Business Scenario

INTRODUCTION

Accounting is the language of business and business use accounting to communicate to its stakeholders like investors, customers, employees, bankers, creditors, income tax authorities etc. Globalization of capital market has changed the tradition pattern of investment and financing decision. Now corporate are taking an investment decision in the basis of the potential customers in an international perspective and not confined inside the domestic boundaries. Targeting a foreign market need a product which meets international standards. Producing a product meeting global standards needs huge investment which may be available from the domestic stock exchange. This promoted the corporate to target foreign capital markets and issue ADR (American Depository Receipt) and GDR (Global Depository Receipt) and raise capital from USA and Europe. Any corporate issuing ADR and GDR have to prepare an additional financial statements accepted by US and Europe market based on GAAP or IFRS. In other words, those corporate are forced to maintain two set of books, one based on ICAI guidelines and other based on IFRS guidelines. The increase in diversity of the customers for accounting information demands the implementation of a n accounting practice acceptable worldwide.

IFRS

The International Financial Reporting Standards, usually called the IFRS Standards, are standards issued by the IFRS Foundation and the International Accounting Standards Board (IASB) to provide a common global language for business affairs so that company accounts are understandable and comparable across international boundaries. IFRS are a set of international accounting standards stating how particular types of transactions and other events should be reported in financial statements. IFRS are issued by the International Accounting Standards Board, and they specify exactly how accountants must maintain and report their accounts. IFRS were established in order to have a common accounting language, so business and accounts can be understood from company to company and country to country.

The point of IFRS is to maintain stability and transparency throughout the financial world. This allows businesses and individual investors to make educated financial decisions, as they are able to see exactly what has been happening with a company in which they wish to invest. IFRS are standard in many parts of the world, including the European Union and many countries in Asia and South America, but not in the United States. The Securities and Exchange Commission (SEC) is in the process of deciding whether or not to adopt the standards in America. Countries that benefit the most from the standards are those that do a lot of international business and investing. Advocates suggest that a global adoption of IFRS would save money on alternative comparison costs and individual investigations, while also allowing information to flow more freely. In the countries that have adopted IFRS, both companies and investors benefit from using the system, since investors are more likely to put money into a company if the company's business practices are transparent. Also, the cost of investments is usually lower. Companies that do a lot of international business benefit the most from IFRS.

Why we need IFRS?

IFRS is needed because of the following reasons:

- Companies going global
- Global market for raising finance
- Global investors
- Need standardized accounting practice

IFRS Foundation

IFRS Foundation is the supreme body in charge of IFRS. The IFRS Foundation has a three-tier governance structure, based on an independent standard-setting Board of experts (International Accounting Standards Board), governed and overseen by Trustees from around the world (IFRS Foundation Trustees) who in turn are accountable to a monitoring board of public authorities (IFRS Foundation Monitoring Board). The IFRS Advisory Council provides advice and counsel to the Trustees and the Board, whilst the Board also consults extensively with a range of other standing advisory bodies and consultative groups.

IFRS Foundation Monitoring Board

The Monitoring Board was created in January 2009 with the aim of “providing a formal link between the Trustees and public authorities” in order to enhance the public accountability of the IFRS Foundation.

The Monitoring Board's main responsibilities are to ensure that the Trustees continue to discharge their duties as defined by the IFRS Foundation Constitution, as well as approving the appointment or reappointment of Trustees. The Monitoring Board meets the Trustees at least once a year, or more often if appropriate

The Monitoring Board consists of capital markets authorities responsible for setting the form and content of financial reporting. Through the Monitoring Board, securities regulators that allow or require the use of IFRS in their jurisdictions will be able to more effectively carry out their mandates regarding investor protection, market integrity, and capital formation.

Trustees of the IFRS Foundation (Trustees)

The Trustees are responsible for the governance and oversight of the International Accounting Standards Board (Board). The Trustees are not involved in any technical matters relating to IFRS Standards. This responsibility rests solely with the Board. The Trustees are accountable to the Monitoring Board, a body of publicly accountable market authorities. Trustees are appointed for a renewable term of three years.

Each Trustee is expected to have an understanding of, and be sensitive to, international issues relevant to the success of an international organisation responsible for the development of high quality global accounting standards for use in the world's capital markets and by other users. Michel Prada was appointed Chairman of the IFRS Foundation Trustees, effective 1 January 2012, and his second term runs until 31 December 2017.

International Accounting Standards Board

The Board is an independent group of experts with an appropriate mix of recent practical experience in setting accounting standards, in preparing, auditing, or using financial reports, and in accounting education. Broad geographical diversity is also required. Board members are responsible for the development and publication of IFRS Standards, including the *IFRS for SMEs* Standard. The Board is also responsible for approving Interpretations of IFRS Standards as developed by the IFRS Interpretations Committee (formerly IFRIC). Members are appointed by the Trustees through an open and rigorous process that includes advertising vacancies and consulting relevant organisations.

IFRS Interpretations Committee

The IFRS Interpretations Committee (Interpretations Committee) is the interpretative body of the International Accounting Standards Board (Board). The Interpretations Committee works with the Board in supporting the application of IFRS Standards. The Interpretations Committee responds to questions about the application of the Standards and does other work at the request of the Board.

The Interpretations Committee comprises 14 voting members, appointed by the Trustees of the IFRS Foundation. The members provide the best available technical expertise and diversity of international business and market experience relating to the application of IFRS Standards. Click here to read the criteria for Interpretations Committee members.

IFRS Standards

International Accounting Standards Board (IASB) is in charge of developing and publishing IFRS Standards. As of now 15 standards are developed of IASB and the same is mentioned below:

- IFRS 1 – First time Adoption of IFRS
- IFRS 2 – Share Based Payment
- IFRS 3 – Business Combination
- IFRS 4 – Insurance Contracts
- IFRS 5 – Noncurrent assets held for sale and Discontinued Operations
- IFRS 6 – Exploration for and evaluation of Mineral Resources

- IFRS 7 – Financial Instruments; Disclosures
- IFRS 8 – Operating Segments
- IFRS 9 – Financial Instruments
- IFRS 10 – Consolidated Financial Statements
- IFRS 11 – Joint Arrangement
- IFRS 12 – Disclosure of Interest in other Entities
- IFRS 13 – Fair Value Measurement
- IFRS 14 – Regulatory Deferral Accounts
- IFRS 15 – Revenue from contracts with customers

IFRS AND ITS BUSINESS IMPLICATIONS

Initial Beneficiaries

If IFRS is implemented in India then blue chip companies will be the initial beneficiaries. Many of the blue chip companies are already using IFRS and raising money from the global market. Currently they are forced to follow two accounting standards which incur additional cost. Now they may get the comfort of following IFRS alone.

Software sector is a competing sector in India. The big names of Indian software industries like TCS, Infosys, Wipro, CTS, Mahindra Satyam etc. having reputed customer base in USA and West and have already started raising foreign capital. The 2nd level payers will also get an opportunity to issue ADR and GDR and raise foreign capital. The software sector is already a hot pic of FIIs (Foreign Institutional Investors).

Companies in the business of oil and natural gas are one among the most profitable companies worldwide. Of the top 10 profit making companies globally in 2013, 6 companies were in petroleum sector. This sector is considered to be one the most profitable sectors in the world. India has many giants in this sector both in public and well as private sector. They will be able to reap initial benefit with the implementation of IFRS.

Indian banking is unique for its conservative approach. RBI (Reserve Bank of India) is still following a safe and risky approach in banking business compared to aggressive market oriented approach of foreign banks. This conservative approach helped Indian banks during subprime crisis who adversely affected the biggest bankers in the world like Citi Bank, Bank of America etc. Even though an Indian bank cannot make exorbitant profit like a foreign bank, the Indian banks are compared to a safe haven for investment and many FIIs already consider banking sector as preferred sector to invest. The next best expansion for a sector to global financial market can be Indian banking sector.

MSME (Micro, Small and Medium Enterprises) is a major sector in our industry. They are concentrating in multiple business segments like apparels, automobile parts, pump sets, restaurants etc. Majority are not even having a proper costing system. Based on current scenario majority of them will have to wait for years to get their IPO (Initial Public Offering) listed in BSE(Bombay Stock Exchange) and NSE (National Stock Exchange). In the current scenario it may take some time for MSME sector to reap advantage from IFRS

Challenges in Implementation of IFRS

The challenge for anything is the comparison between the cost and benefit that IFRS offers. The cost (challenge) in implementation is changing the current status quo. We have an accounting system designed by ICAI, followed over the years by corporate and income tax authorities. Shifting to a new standard may require time, cost and expertise. Secondly, adopting something new scrapping the existing system may create lot of chaos and can affect the GDP and revenue at least in short run.

Majority of the small Indian business are not aware of IFRS. It requires proper training and support in the initial years. The cost is another hindrance to the adoption. The companies have to pay for new software and experts. Our legal and tax framework is unique in many aspects and its having a standard practice for years. To alter that also is a cumbersome process which consumes time, long term vision and continuous monitoring.

Keeping this in mind a good number of experts in the area of accounting and business is recommending a convergence between Indian Accounting Standards and IFRS and not the adoption of IFRS. Convergence basically talks of slightly modifying or amending the Indian accounting practice keeping in line with the IFRS standards. These will avoid confusion and helps in easy transition. The corporate can get the benefit of IFRS without much financial burden.

Benefits of IFRS

The benefits that IFRS offers can be viewed in 3 angels:

- Benefits to Corporate
- Benefits to Investor
- Benefits to India

Benefits to Corporate

Corporate are the prime beneficiaries in the implementation of IFRS. The main advantages to a corporate with IFRS implementation is stated below:

- It can be a more competitive player in the financial market.
- The options for a corporate in raising finance will be increase multifold.
- The additional options of raising the finance helps the corporate to choose a mode of finance which carries lowest cost of capital. This in turn helps in the increase in value of the business.
- The visibility in the financial market is more for a corporate which follows an international accounting practice. Visibility helps acceptance also in the stock market which may increase the value of the investors
- In nutshell, the chance of becoming a global player is more with IFRS implementation. This can act as a stimulus in exploring equity markets of foreign countries.

Benefits to Investors

Investor is the prime stakeholder in capital market. Investor fortunes is directly depended on the stock market

performance of the company he owns. His benefits are listed below:

- The financial statements will be more transparent. This will help him in understanding the business in a better way and enable him in taking a rational decision
- The reliability will be more if a corporate is following IFRS. The chance of cheating will get drastically reduced.
- If more and more companies are following IFRS, then FIIs will be more interested in exploring Indian stock market. This will make the market lucrative and help the investor.
- If the Indian stock market becomes lucrative then there is a chance that foreign companies will also try to get listed in NSE and BSE. This will help an Indian investor to invest or buy shares of multi-national corporations.
- All this may result in increasing the net return than an investor can expect from the stock market

Benefits to India

All businesses use the resources of the nation for its operations. So it's logical to analyze the benefit that the nation can get by implementing IFRS.

- Our nation will become an investor friendly nation. This will have a huge impact on our GDP and per capita income.
- The foreign cash inflows to our nation will drastically improve. They will have a direct positive impact on capital and employment generation.
- India can become a hub of international business
- All these result in increase in GDP, per capital income, tax revenues and prosperity.

The Way Ahead

IFRS can be the next revolution of the accounting system. Whether IFRS followed in India or not the blue chip companies will follow it and try to raise money from the foreign markets. For the past few years our stock market is growing fast than the growth of Indian economy, which is expected to continue with the implementation of new accounting practices. IFRS is basically an opportunity and challenge and benefit depends on how well we can overcome the challenges.

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