



Ind AS carve outs and challenges with International Financial Reporting Standards (IFRS)

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Abstract

This paper is an attempt to describe the initiatives taken by India for convergence to International financial reporting standards (IFRS) and its deviation from IFRS. It also explain the need of convergence, from AS to Ind AS. Though all the ingredients of IFRS have not been taken in the Ind AS, but still it is a step forward towards IFRS. Difference between IFRS and Ind AS has been discussed for Carve out from IFRS in the relevant Ind AS's and other major changes as notified by Ministry of corporate affairs (MCA). IFRS significance and objectives has also been explained along with Challenges in IFRS beyond Accounting and Financial Reporting in Indian perspective i.e. Human resources, Information System, Internal Control, Amendment of Laws and Auditability of fair value measurements. A brief discussion of challenges to be faced by banks in implementing Ind AS especially Ind AS 9 is given.

Keywords: International Financial Reporting Standards (IFRS), carves out, challenges for banks

1. Introduction

The final Ind AS include several 'carve outs' (deviations) from IFRS as issued by the International Accounting Standards Board (IASB). The Indian standard setters have examined individual IFRS and modified the requirements, where necessary, to suit Indian conditions. Carve outs are generally perceived as non-desirable, since they dilute the key purpose of converging with IFRS (i.e., to have a common set of accounting standards across countries, provide seamless access to international capital^[1]. Hoogervorst the IASB chairman addressed the reason for optimism that India would fully converge in coming years is that there are only seven carve-outs, basically deviations between Indian accounting standards and IFRS. From April 1 2016, India has implemented a new framework of accounting standards (Ind AS) that seeks to converge with IFRS and not fully adopt them. For banks, Ind AS implementation will begin from April 1, 2018.

As discussed above leasing, revenue recognition, foreign currency convertible bonds, current vs noncurrent liabilities, bargain purchases are among the areas where India has deviated from IFRS.

It is crystal clear, where are the differences between IFRS and Ind AS. Thus, it is helpful in removing the deviations^[2].

2. Objectives

The general objective of the study is done to know the level of compliance of International Financial Reporting Standards. The specified objectives include the following:

1. To explain International Financial Reporting Standards.
2. To know need of the convergence of International Financial Reporting Standards.
3. To examine the benefits and challenges of International Financial Reporting Standards to India.

4. To evaluate the challenges to be faced by banks in implementing Ind AS
5. To study the carve out of Ind AS with IFRS

3. IFRS overview

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. They are a consequence of growing international shareholding and trade and are particularly important for companies that have dealings in several countries. They are progressively replacing the many different national accounting standards. They are the rules to be followed by accountants to maintain books of accounts which are comparable, understandable, reliable and relevant as per the users internal or external.

3.1 Need for IFRS convergence

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.

Indian Accounting Standards Converged with IFRS (Ind AS) results in common set of accounting standards, which help in better Comparability of financial statements prepared in different countries as common set of standards is followed. The users of accounts will be benefited by this because same accounting standards will help them to understand the fundamentals of the organization which will generate better transparency. Many companies having subsidiary or Holding

company in different countries, they are required to follow different set of accounting standards (local and global standards). The transition will be helpful in saving time & cost on the finance department. It would also attract foreign investment more in the country as they can more understand, compare the accounting statement and make investment decisions.

3.2 Benefits of adopting IFRS

Economy

In today's scenario of global business village, India cannot afford to protect itself from the developments and modifications taking place worldwide. Adoption or convergence of IFRS help economy by increasing the global business. Financial statement made under IFRS are accepted by stock exchange all over the world.

This help in developing industries and market in economy as it attract more foreign capital at lower cost. It also improves the risk rating of India among the international investors.

Investors

Convergence with IFRS developed better understanding of financial statement globally. It make accounting information more reliable, relevant, timely and comparable. Investors are now more confident while investing as there is more transparency and accuracy in financial statement published by companies.

Corporate world

Convergence with IFRS would build the reputation and long lasting relationship of the Indian corporate world with the international financial entities. Moreover, the corporate entities back in India would be benefited because of several reasons. The higher level of consistency will be maintained between external and internal reporting, two, because of better access to global financial markets, three, it will improve the risk rating and makes the corporate world more and more competitive globally as their comparability with the global competitors will increase

Accounting professionals

However, there would be initially many problems; convergence with IFRS would surely benefit the accounting professionals and it will be helpful them to sell their talent and expertise across the globe.

3.3 Challenges in adopting IFRS

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 routed. It would be a challenge to bring about awareness of IFRS and its impact among the users of financial statements.

Training and Education

Lack of training facilities and academic courses on IFRS will also pose challenge in India. There is a need to impart education and training on IFRS and its application.

Legal Consideration

Currently, the reporting requirements are governed by various regulators in India and their provisions override other laws. IFRS does not recognize such overriding laws. The regulatory and legal requirements in India will pose a challenge unless the same is been addressed by respective regulatory.

Taxation effect

IFRS convergence would affect most of the items in the financial statements and consequently the tax liabilities would also undergo a change. Thus the taxation laws should address the treatment of tax liabilities arising on convergence from Indian GAAP to IFRS.

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 used [3].

3.4 Challenges to be faced by banks

Banks and NBFCs will start implementing Ind AS from April 1, 2018 (barely three months from now). Adoption of Ind AS is expected to significantly enhance comparability of the financial statements of Indian banks with their global peers and hence it is indeed a welcome move for the Indian financial system. In order to be in readiness for its implementation, the Reserve Bank of India (RBI) had asked banks to submit pro forma Ind AS financials for the six months ended September 30, 2016, and also the three months ended June 30, 2017 [4]. The biggest impact of Ind AS comes from Ind AS 109 (equivalent of IFRS 9), an accounting standard on Financial Instruments, which impacts almost all line-items of banks' balance sheets. IFRS 9 introduces a new classification and measurement category, Fair Value through Other Comprehensive Income (FVOCI), while eliminating the categories available for sale, held to maturity, loans and receivables. It also mandates a three-stage impairment model for computing expected credit losses on loans, something that IAS 39 did not require. And IFRS 9 has new guidance on hedge accounting that requires enhanced disclosure of the organization's risk management activity. The challenge is that IFRS 9 is principles-based and does not provide any standard model for computing expected credit losses. Banks must therefore create their own ECL model, one that would be compliant with IFRS 9 yet at the same time would not unduly affect the bank's financial performance [5].

3.5 Carves out from IFRS

Ind AS refers to converged standards notified by NACAS. In all 35 standards has been notified till date, Ind AS in a mathematical equation is Ind AS = IFRS as issued by IASB less carve outs Add IFRS pronouncement being adopted in Ind AS. Following are the carves out from IFRS in relevant Ind AS as shown in table-1 below: [6]

Table 1

Carve Outs from IFRSs in the relevant IND AS's.	Carve outs
Ind AS 21-The Effects of Changes in Foreign Exchange Rates, it requires recognition of exchange differences arising on translation of monetary items from foreign currency to functional currency directly in profit or loss	Ind AS 21 permits an option to Recognize exchange differences arising on translation of certain long-term monetary items from foreign currency to functional currency directly in equity. In this situation, Ind AS 21 requires the accumulated exchange differences to be amortized to profit or loss in an appropriate manner
Ind AS 28- Investment in Associates 1. Paragraph 25 require that difference between the reporting period of an associate and that of the investor should not be more than three months, in any case	The phrase 'unless it is impracticable' has been added in the relevant requirement i.e., paragraph 25 of Ind AS 28. IAS 28 requires that for the purpose of applying equity method of accounting in the preparation of investor's financial statements, uniform accounting policies should be used. In other words, if the associate's accounting policies are different from those of the investor, the investor should change the financial statements of the associate by using same accounting policies. Carve out The phrase, 'unless impracticable to do so' has been added in the relevant requirements i.e., paragraph 26 of Ind AS 28
Ind AS 32-Financial Instruments: Presentation	An exception has been included to the definition of 'financial liability' in paragraph 11 (b) (ii), Ind AS 32 to consider the equity conversion option embedded in a convertible bond denominated in foreign currency to acquire a fixed number of entity's own equity instruments as an equity instrument if the exercise price is fixed in any currency. This exception is not provided in IAS 32.
Ind AS 39-Financial Instruments: Recognition and Measurement IAS 39 requires all changes in fair values in case of financial liabilities designated at fair value through Profit and Loss at initial recognition shall be recognized in profit or loss. IFRS 9 which will replace IAS 39 requires these to be recognized in 'other comprehensive income.	Whereas a proviso has been added to paragraph 48 of Ind AS 39 that in determining the fair value of the financial liabilities which upon initial recognition are designated at fair value through profit or loss, any change in fair value consequent to changes in the entity's own credit risk shall be ignored
Ind AS 103 -Business Combinations IFRS 3 requires bargain purchase gain arising on business combination to be recognized in profit or loss.	Ind AS 103 requires the same to be recognized in other Comprehensive income and accumulated in equity as capital reserve, unless there is no clear evidence for the underlying reason for classification of the business combination as a bargain purchase, in which case, it shall be recognized directly in equity as capital reserve.
Ind AS 101- First-time Adoption of Indian Accounting Standards (a) Presentation of comparatives in the First-time Adoption of Indian Accounting Standards (Ind AS) 101 (corresponding to IFRS 1) IFRS 1 defines transitional date as beginning of the earliest period for which an entity presents full comparative information under IFRS. It is this date which is the starting point for IFRS and it is on this date the cumulative impact of transition is recorded based on assessment of conditions at that date by applying the standards retrospectively except to the extent specifically provided in this standard as optional exemptions and mandatory exceptions. Accordingly, the comparatives, i.e., the previous year figures are also presented in the first financial statements prepared under IFRS on the basis of IFRS	(a) Ind AS 101 requires an entity to provide comparatives as per the existing notified Accounting Standards. It is provided that, in addition to aforesaid comparatives, an entity may also provide comparatives as per Ind AS on a memorandum basis.
(b) Presentation of reconciliation IFRS 1 requires reconciliations for opening equity, total comprehensive income, cash flow statement and closing equity for the comparative period to explain the transition to IFRS from previous GAAP.... (e) Cost of Property, Plant and Equipment (PPE), Intangible Assets, Investment Property, on the date of transition of First-time Adoption of Indian Accounting Standards. In contrary to IFRS, Ind AS 101 provides an entity has an option to use carrying values of all assets as on the 768 date of transition in accordance with previous GAAP as an acceptable starting point under Ind AS. II. Industry specific deviations taken	(b)Ind AS 101 provides an option to provide a comparative period financial statements on memorandum basis. Where the entities do not exercise this option and, therefore, do not provide comparatives, they need not provide reconciliation for total comprehensive income, cash flow statement and closing equity in the first year of transition but are expected to disclose significant differences pertaining to total comprehensive income. Entities that provide comparatives would have to provide reconciliations which are similar to IFRS
(c) Cost of Non-current Assets Held for Sale and Discontinued Operations on the date of transition on First-time Adoption of Indian Accounting Standards (Ind AS) circumstances to measure such assets or operations at the lower of carrying value and fair value less cost to sell	(c)In contrary to IFRS, Ind AS 101 provides transitional relief that while applying Ind AS 105 - Non-current Assets Held for Sale and Discontinued Operations, an entity may use the transitional date
(d) Foreign currency gains/losses on translation of long term monetary items	(d)In contrary to IFRS, Ind AS 101 provides that on the date of transition, if there are long-term monetary assets or long-term monetary liabilities mentioned in paragraph 29A of Ind AS 21, an entity may exercise the option mentioned in that paragraph regarding spreading over the unrealized Gains/Losses over the life of Assets/Liabilities either retrospectively or prospectively. If this option is exercised prospectively, the accumulated exchange differences in respect of those items are deemed to be zero on the date of transition.
(e) Cost of Property, Plant and Equipment (PPE), Intangible Assets, Investment Property, on the date of transition of First-time Adoption of Indian Accounting Standards	(e) In contrary to IFRS, Ind AS 101 provides an entity has an option to use carrying values of all assets as on the date of transition in accordance with previous GAAP as an acceptable starting point under Ind AS.

4. Conclusion

The challenge of Ind AS conversion projects will usually be very significant, as the differences between Indian GAAP and Ind AS are many. With many stakeholders involved, and given the combination of marketing, financial reporting, human resources, IT, process, controls, tax and risk management issues, change needs to be managed. There are major demands on financial and human resources in companies. An Ind AS conversion project cannot be a distraction from the primary activities of your business. It must be integrated, coordinated, and aligned. Considering the volume of changes due to Ind AS implementation and onerous disclosure requirements, banks will need to reassess and upgrade their policies, processes and IT systems. Capital will also have significant impact.

5. References

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