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The Use of a Formal Representation of Indian Accounting Standards

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Abstract:

"Accounting is as old as money itself". *Chanakya in his Arthashastra emphasized on the existence and the need of proper accounting and auditing. The purpose of this paper is to introduce the model we built to represent financial information in an efficient way. This kind of information shows an unquestionable delay on the field of knowledge management, and this issue is more important as the requirements on financial reporting increase. We will describe the particular nature of accounting standards. This paper explains the frequent issuance of many Accounting standards in recent years and recommends complementary institutional mechanisms needed to strengthen the quality of financial reporting and corporate governance in India. This paper ends with a description of the applications we build to explain the possibilities of such a model for various financial information users, especially financial auditors.*

Keywords: *Globalisation & Indian Accounting standard, Knowledge representation*

1. Introduction

A financial reporting system supported by strong governance, high quality standards, and firm regulatory framework is the key to economic development. Indeed, sound financial reporting standards underline the trust that investors place in financial reporting information and thus play an important role in contributing to the economic development of a country. The Institute of Chartered Accountants of India (ICAI) as the accounting standards-formulating body in the country, has always made efforts to formulate high quality Accounting Standards and has been successful in doing so. Indian Accounting Standards have withstood the test of time the environment in which financial information is produced and analyzed is changing widely. All over the world, we can see a general trend which consists in more frequent, more extensive and more documented reporting. These changes are the result of several phenomenons, mainly the constantly growing volume of data to manipulate and the recent financial scandals (Enron, Worldcom, etc.). A set of international standards called IFRS (International Financial Reporting Standards) emerged during the last years. They are already used by public companies in the European Union, and their use should become widespread in the future. Thus, we can see that the reporting requirements have considerably increased, both on a qualitative and on a quantitative way.

2. Accounting Standards-Setting in India

The Institute of Chartered Accountants of India (ICAI) being a member body of the IASC, constituted the Accounting Standards Board (ASB) on 21st April, 1977, with a view to harmonise the diverse accounting policies and practices in use in India. After the avowed adoption of liberalisation and globalisation as the corner stone's of Indian economic policies in early '90s, and the growing concern about the need of effective corporate governance of late, the Accounting Standards have increasingly assumed importance. While formulating accounting standards, the ASB takes into consideration the applicable laws, customs, usages and business environment prevailing in the country. The ASB also gives due consideration to International Financial Reporting Standards (IFRSs)/ International Accounting Standards (IASs) issued by IASB and tries to integrate them, to the extent possible, in the light of conditions and practices prevailing in India.

3. New Indian Accounting Standards

Globalisation throws new challenges to enterprises by exposing them to the best. One of them is that management not only needs to be honest, but also open and transparent to shareholders, government and other stakeholders. The Institute of Chartered Accountants of India In the first two decades since the formation of its Accounting Standards Board had come out with about 15 accounting standards. To keep pace with the new challenges it has issued about 13 new Standards in the last two years and some more are in the offing. The furious pace at which these standards were issued and mandated is unprecedented and has shaken the otherwise inert accounting profession to agility. The new Standards are likely to pose not only insurmountable accounting problems and questions but will also have severe business consequences. Corporate results will be significantly impacted by the Standard on deferred taxation and financial statements will provide users with useful but sensitive information relating to transactions with related parties and performance of various business divisions of an enterprise.

The pace, at which these standards have been introduced, provided very little time to the ICAI and the profession in general to understand and resolve areas of disputes and inconsistencies. As a result there is confusion and it is possible in a number of situations that two accountants may reach different conclusions on a particular issue. In this regard it is recommended that ICAI immediately set up a special task force to address the apprehensions of the profession, various implementation issues and more importantly amicably resolve areas of dispute and inconsistencies. SEBI too should play an important role in ensuring compliance with Accounting Standards in respect of listed enterprises, similar to the role played by SEC in the US. If all this does not happen, Accounting Standards, like so many other legislations in India will remain at best an exercise in academics. Since the introduction of the new accounting standards ICAI has issued several Accounting Standards interpretations and provided General Clarifications.

The introduction of the new standards is laudable though due to poor track record application of the accounting standards in its true spirit will not be achieved unless strongly monitored. Indian industry continues to use good old ways to manage bottom line.

4. Procedure for Issuing Accounting Standards

- Accounting Standard Board (ASB) determines the broad areas in which Accounting Standards need to be formulated. In the preparation of AS, ASB is assisted by Study Groups.
- ASB also holds discussions with representative of Government, Public Sector Undertakings, Industry and other organizations (ICSI/ICWAI) for ascertaining their views.
- An exposure draft of the proposed standard is prepared and issued for comments by members of ICAI and the public at large.
- After taking into consideration the comments received, the draft of the proposed standard will be finalized by ASB and submitted to the council of the Institute.
- The council of the Institute will consider the final draft of the proposed Standard and If found necessary, modify the same in consultation with ASB. The AS on the relevant subject will then be issued under the authority of the council.

5. Rationale of Accounting Standards

Accounting Standards are formulated with a view to harmonise different accounting policies and practices in use in a country. The objective of Accounting Standards is, therefore, to reduce the accounting alternatives in the preparation of financial statements within the bounds of rationality, thereby ensuring comparability of financial statements of different enterprises with a view to provide meaningful information to various users of financial statements to enable them to make informed economic decisions. The Companies Act, 1956, as well as many other statutes in India requires that the financial statements of an enterprise should give a true and fair view of its financial position and working results. This requirement is implicit even in the absence of a specific statutory provision to this effect. The Accounting Standards are issued with a view to describe the accounting principles and the methods of applying these principles in the preparation and presentation of financial statements so that they give a true and fair view. The Accounting Standards not only prescribe appropriate accounting treatment of complex business transactions but also foster greater transparency and market discipline. Accounting Standards also helps the regulatory agencies in bench.

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7. India and IFRS

In India, there will be two set of Accounting Standards –

1. The existing Indian Accounting Standards (IAS) – will be applicable to all companies which are not required to adopt IFRS converged standards.
2. Indian Accounting Standards, as converged with IFRS (Ind-AS) – will be applicable to companies operating in India in phased manner beginning from April 1, 2011. In the first phase companies forming part of stock exchange index and those with net worth of above approx 250 million USD will be required to present their financial statements as per Ind-AS. There are conceptual differences between IAS and IFRS. Keeping in view the extent of gap between IAS, Ind-AS and the corresponding IFRSs – conversion process would need careful handling. By introducing a new company law, the Indian Government has initiated the process to amend the legal and regulatory framework. The conversion would involve, Impact Assessment, Revisiting Accounting Policies and thereafter changing the Accounting & Operational Systems (including ERP) in order to be fully compliant with Ind AS or IFRS.

8. Composition of the Accounting Standards Board

The composition of the ASB is broad-based with a view to ensuring participation of all interest groups in the standard-setting process. These interest-groups include industry, representatives of various departments of government and regulatory authorities, financial institutions and academic and professional bodies. Industry is represented on the ASB by their apex level associations, viz., Associated Chambers of Commerce & Industry (ASSOCHAM), Confederation of Indian Industries (CII) and Federation of Indian Chambers of Commerce and Industry (FICCI). As regards government departments and regulatory authorities, Reserve Bank of India, Ministry of Company Affairs, Comptroller & Auditor General of India, Controller General of Accounts and Central Board of Excise and Customs are represented on the ASB. Besides these interest-groups, representatives of academic and professional institutions such as Universities, Indian Institutes of Management, Institute of Cost and Works Accountants of India and Institute of Company Secretaries of India are also represented on the ASB. Apart from these interest groups, certain elected members of the Central Council of ICAI are also on the ASB.

9. Globalisation and Indian Accounting Standards

9.1 Japan

(Indian accounting regulation has evolved in two major phases so far. Since accounting regulation is affected by the development of economic and political institutions and policies in a country, these phases largely mirror the economic development model that was followed. The first phase was from the 1950s the early 1990s and the second phase was from the mid-1990s onwards. During the first phase (1950 to1991), India's economy remained isolated from events in the rest of the world. The state assumed a major role in determining the economic life of the country and even involved itself in firm-level decisions on plant location, products, prices, raising capital and pricing capital issues. Its serious balance of payments crisis in 1991 forced India to radically reform its economic policies. Besides structural reforms in foreign trade, taxation and industrial policy, many of the controls on firm-level economic decision making were dismantled. Free floatation of the Indian rupee within limits, permission to Indian companies to raise capital abroad, liberalisation of the rules for foreign direct investment, and permission for portfolio investment by foreign financial institutions are particularly significant in the context of reforms in accounting standards.

10. Financial Reporting in the Context of Economic Reforms and Globalisation

The system of financial reporting is a function of the economic, legal and political institutions in a country. There have been major changes in financial reporting in India since the economic reforms and globalisation began in the early 1990s. Among others, the following forces are important: § Capital, product and labour market pressures, Company law and securities law changes in India and International accounting and securities regulations.

11. Impact of Economic Reforms and Globalisation on Accounting and Governance

A recent study on corporate governance in ten countries in Asia indicates that in conformity to the IASB's standards, India is ranked fourth in the region; Singapore, Hong Kong and Malaysia are ahead of India; South Korea, Taiwan, Thailand, Philippines, China and Indonesia are behind. In enforcement, only Hong King and Singapore are ahead of India. Indian investors are willing to pay a governance premium of 23 per cent, conceivably for lower agency costs. (Barton et al. 2003).

12. Accounting Standard and Indian Companies Act

ICAI not being a regulatory body cannot on its own mandate accounting standards. A mandatory accounting standard if not followed required auditors who are members of ICAI to quality their audit reports. Failing which they will be guilty of professional misconduct. However preparers of financial statements were not obliged to confirm to these mandatory accounting standards. SEBI and the Indian Companies Act recently made the implementation os accounting standards by preparers of financial statement compulsory for listed companies and the entire corporate sector respectively. Both SEBI and companies act requires auditors to quality audit reports that do not confirm to mandatory accounting standards. Section 217(2AA) of the companies act also casts a responsibility on the board of director to comply with mandatory of accounting standards. As per this section , the board's report shall include a director's responsibility statement indicating there in the applicable accounting standards have been followed with proper explanation relating to material departure if any the directions had selected such accounting policies and the applied them consistently and made judgement and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company that the directors had taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of this act for the safeguarding the assets and for the preventing and detecting frauds and other irregulaties, and that the directors had prepared the accounts on a going concern basis.

Under section 211 of the companies Act, Where the financial statements do not comply with accounting standards. Such companies shall disclose, the following

(a) The deviation from the accounting standards
(b) The reason for such deviation
(c) The financial effects,

If any arising out of such deviation. for the purpose of this section , the expression accounting standards means the accounting standards recommended by ICAI as may be prescribed by the central government in consultancy with the National advisory Committee on accounting standards established under section 210 (1). Provided that the standard of accounting specified by ICSAI shall be deemed to be the accounting standard until the accounting standard are prescribed by the central government under the section. The ICAI has issued a list of specified standard that I mandatory for the purposes of the company's act.

By the powers conferred to the central government under section 210(A) of the company's act, the composition of the National Advisory committee on accounting standard had been notified on 15th June, 2001, by the department of company affairs. The committee has been set up to advised the central government on the formulation and lying down of accounting policies and accounting standards for adoption by the corporate sector. With the formation of the national advisory committee, one more accounting body has been added to the long list of accounting bodies.

13. Accounting Standards and Mutual Funds

As per the preface on accounting standards issued by ICAI, Accounting standards apply to general purpose financial statements of enterprises which include trusts. ICAI would make efforts to issue accounting standards which are in conformity with the provisions of the applicable laws, customs, usages and business environment in India .however, if due to subsequent amendments, A particular accounting standards is found to be note in conformity with such laws, the provisions of the said law while prevail and the financial would be prepared in conformity with such laws, in relation to mutual funds accounting treatment and disclosure requirements under SEBI mutual fund regulation should be followed. Where for a particular matter SEBI regulations have not prescribe the accounting treatment, ICAI standards should be followed. Where an accounting standards is in consistent with SEBI's mutual fund regulations and financial statements are appropriately prepare in accordance with SEBI regulations, an auditor's qualification on mandatory standards issued by ICAI is inappropriate, though a clarificatory note should be included in the audit report. AS 13 specifically excludes AMC's & mutual funds, therefore in that regards SEBI mutual funds regulations on accounting disclosure and valuations of investment should be followed.