INDIAN GAAP AND ITS CONVERGENCE TO IFRS: PRAGMATIC EVIDENCE FROM INDIA

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Abstract

There is a growing international consensus on the International Financial Reporting Standards as acceptable standards for assessment of the financial health of a company across the globe. For entities that are globally active, the differences in financial reporting requirements create extra complications in terms of preparing, consolidating, auditing and interpreting financial statements. Against this backdrop, the prime objective of the present work is to study the rationale behind introducing IFRS, comparative analysis of Indian Accounting Standards and IFRS, challenges involved in IFRS while adopting it in India, impact and consequences on financial statement due to IFRS adoption of Noida Toll Bridge Company Ltd. It has been found from our study that there is not much deviations and fluctuations in the net income position as disclosed by financial statement of Noida Toll Bridge Company Ltd in IFRS reporting and Indian GAAP. But, deviation is rather prominent when observing the total liability and equity position which is mainly because of reclassification between equity and total liability. In true generalized sense, the return on equity, return on asset, total asset turnover and net profit ratios are not significantly affected by converging to IFRS but the leverage ratio shows significant change on converging with IFRS.

Keywords: *GAAP, IFRS, convergence, IAS, India, Noida Toll Bridge Company Ltd.*

Introduction

International Financial Reporting Standards (IFRS) are designed as 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. 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.

Globalization of financial markets has meant an increased focus on international standards in accounting and has intensified efforts towards a single set of high quality, globally acceptable set of accounting standards. Financial statements prepared in different countries according to different set of rules, mean numerous national sets of standards, each with its own set of interpretation about a similar transaction, making it difficult to compare, analyze and interpret financial statements across nations.

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. Needless to mention, internationally accepted accounting standards play a major role in this entire process.

Review of Literature

Jones and Higgins (2006) established that larger firms tended to have greater knowledge of IFRS including their expected financial reporting impacts, and were generally more advanced in the implementation process than smaller firms. The costs of converting to IFRS are likely to be significant for most firms in Australian reporting entities; the perceived benefits of these standards were far less clear.

Ali et al. (2006) suggested that low harmonization levels are both due to the degree of flexibility available in selecting benchmark treatments in some IAS and also to non-compliance by companies with IAS mandated requirements and relatively higher degree of harmonization exists in the practice of accounting treatment of gains or losses on disposal of property, plant and equipment, recognition of past service costs/experience adjustment of pension and retirement benefits, method of foreign currency translation of assets and liabilities, method of foreign currency translation of revenue and expenses, treatment of translation differences, business combination, treatment of goodwill, disposal of long-term investments and treatment of gains or losses on disposal of current investments.

Pavera and Jamil (2008) said that for many banks, convergence with IFRS is expected to have a significant impact on their financial position and financial performance, directly affecting key parameters such as capital adequacy ratios and the outcomes of valuation metrics that analysts use to measure and evaluate performance.

Manju (2011) elaborated that the transition from GAAP to IFRS is not only inevitable, but a positive development that would help making capital markets more competitive. Transitioning to IFRS would allow companies to compete for capital in other countries, while reducing cost and complexity for companies operating internationally and embracing a single set of global accounting standards would contribute to a higher degree of investor understanding and confidence.

Sarbapriya (2012) tried that several organizations recognized the need to harmonize financial reporting, and the European Union was one of the first to publish directives to reduce differences in the reporting of similar transactions. Convergence in India would be facilitated by the fact that historically Indian accounting standards have been based on principles as against rules. The conflicting legal and regulatory requirements related to financial statements, the technical preparedness of industry and accounting professionals and the economic environment prevailing in the country will pose challenges to this convergence.

Ugur and Elif (2013) reported that the IFRS provide a more reliable form of financial reporting for companies operating all over the world and makes it possible for companies to lower the costs of preparing different financial statements for each different country. SMEs have positive perception on IFRS, the companies don’t have enough information about IFRS and conversion process of financial reporting system is complicated. This complexity is perceived as a difficulty in front of the companies to implement this financial reporting system.

Muniraju and Ganesh (2014) concluded that IFRS implementation with a fair valuation of financial statements and its comfortableness in using unique standard. The companies will find comfort in using accounting standards converged with IFRS if their accountants, auditors, shareholders and other stake holders along with the rating agencies and investment analysts are conversant with such new standards. It is true that during the transition period some problems may have to be faced by any of the aforesaid persons due to lack of adequate knowledge and experience. But such problems can be mitigated if the professional institutes and industry groups take initiative for imparting intensive training to the accounting and auditing professionals on the practical implications and applications.

Pankaj Kumar and Jha (2016) established that adoption of IFRSs by Indian companies is going to affect a number of items of their financial statements including their profitability and financial strength, financial position indicators of a company. The financial information delivered by the statements prepared under IFRSs is considered to be of the highest quality therefore it is also going to have a favorable impact on the confidence level of the users of the financial statements whether they are investors, auditors, students, stake holders, institutions, accountants, legal firms or any academicians; all accept the reliability of the financial statements prepared under IFRSs.

Objectives

The prime objective of the present work is to study impact and consequences on financial statement due to IFRS adoption with the help of case study of Noida Toll Bridge Company Limited.

More specifically, this article has the following objectives:
To observe the effects of voluntary convergence of IFRS on financial statement of Noida Toll Bridge Company Limited.

Methodology of the Study

Study Area

This study has been conducted by incorporating the provisions of IFRS adopted / to be adopted by the Noida Toll Bridge Company Limited running business in India.

Research Design

This study is analytical as well as descriptive in nature. The study gives the comparative details about the IFRS and Indian GAAP for the purpose of better understanding and analysis. We have not taken any hypotheses in the study because adoptions of IFRSs are in progress and it takes time to come in full and fledged manner.

Data Collection

The study is based on secondary data on selected variables sourced from the published annual reports of Noida Toll Bridge Company Limited for the year ended 31st March 2015. Noida Toll Bridge Company Limited had voluntarily prepared its annual report on the basis of Indian GAAP and IFRS for the year ended 31st March 2015, wherein reconciliation of equity based on Indian GAAP and IFRS is presented for the Reconciliation of Equity as at March 31, 2015 and Reconciliation of Income statement as at March 31, 2015.The main sources of secondary data are company ‘s manual, annual general reports, journals, newspapers and concerned websites.

Data Analysis

Comparative study and chart has been prepared for bird ‘s eye view. Since the data has been analyzed and provided by the company itself, we have elaborated the reasons behind the differences and suggested tentative solutions towards better convergence of IFRS.

Analytical Results

Impact of Convergence to IFRS on Financial Statements-study on Noida Toll Bridge Company Limited (NTBCL)
Companies have started the process of preparing IFRS compliant financial statements and are gearing up to adapt to the change in a timely manner to avoid last

moment rush, as ICAI and Ministry of Corporate Affairs is committed to the deadline of IFRS adoption, which is April, 2011. Few companies such as Wipro, Infosys Technologies, NIIT, Mahindra & Mahindra, Tata Motors, Bombay Dyeing and Dr Reddy‘s Laboratories have begun to align their accounting standards to IFRS, three years ahead of the mandatory time for the switchover.

The Company Overview

Noida Toll Bridge Company Limited (NTBCL) is a public limited company incorporated and domiciled in India on 8th April 1996 with its registered office at Toll Plaza, Delhi Noida Direct Flyway, Noida - 201301, Uttar Pradesh, India. The equity shares of NTBCL are publicly traded in India on the National Stock Exchange and Bombay Stock Exchange. The Global Depository Receipts (GDRs) represented by equity shares of NTBCL are traded on Alternate Investment Market (AIM) of the London Stock Exchange. The financial statements of NTBCL are the responsibility of the management of the company.

The Noida Toll Bridge Company Limited (NTBCL) was promoted by Infrastructure Leasing & Financial Services Ltd. (IL&FS) as a special purpose vehicle for the implementation of the Delhi Noida bridge project on a Build, Own, Operate and Transfer (BOOT) basis. The Concession Agreement (Concession) executed between the Company, Promoter and New Okhla Industrial Development Authority (NOIDA) in November 1997, gives the Company the right to levy a User Fee. The Governments of Uttar Pradesh and National Capital Territory of Delhi have, in January 1998, executed a Support Agreement in favour of the Project/ Concessionaire.

NTBCL has been set up to develop, establish, construct, operate and maintain a project relating to the construction of the Delhi Noida Toll Bridge under the "Build-Own-Operate-Transfer" (BOOT) basis. The Delhi Noida Toll Bridge comprises the Delhi Noida Toll Bridge, adjoining roads and other related facilities, Mayur Vihar Link Road and the Ashram flyover which has been constructed at the landfall of the Delhi Noida Toll Bridge and it operates under a Single business and geographical segment.

Pursuant to listing on the Alternate Investment Market (AIM) segment of the London Stock Exchange (AIM), the Company is required to prepare and submit annual and semi-annual financial statements prepared in accordance with IFRS, to AIM.

A reconciliation of Equity and Income statements of Noida Toll Bridge Company Limited under Indian GAAP and IFRS as on March 31, 2015 and related notes as follows. These reconciliations have been prepared on the basis of audited consolidated financial statements of NTBCL prepared in accordance with Indian GAAP and IFRS.

Insert Table 1

Explanatory Notes to the reconciliation:

1. Under IGAAP, depreciation on building has been recognized considering useful life as 60 years, however in IFRS depreciation on building has been recognized considering useful life as 30 years.
2. Under Indian GAAP, Intangible asset has been amortised using unit of usage method till FY 2011-12 and in the proportion of the revenue earned for the period to the total estimated toll revenue thereafter (in accordance with notification issued by Ministry of Corporate Affairs in April 2012), while in IFRS, Intangible asset has been amortised using Straight line method till FY 2008-09 and using unit of usage method thereafter. Further in IFRS useful life of the Intangible Asset has been revised to 30 years in current financial year though in IGAAP, the

same has been revised from April 01, 2015.

3. Under Indian GAAP, Minimum Alternative Tax (MAT) Credit has been classified under loan & advances while in IFRS, the same has been re-classified as deferred tax asset in accordance with IAS-12 “Income Taxes”.
4. In accordance with the Scheme of amalgamation with Delhi Noida Direct Flyways Limited, the Company has made certain adjustment in financial statement prepared under Indian GAAP, the adjustments which are not in conformity with the International Accounting Standard have not been considered in preparation of these financial statements in accordance with IFRS.
5. Under Indian GAAP, deferred tax liability has been recognized on timing difference while in IFRS, deferred tax liability has been recognized on temporary differences. Further consequent to change in useful life of bridge in IFRS, certain portion of timing difference in respect of depreciation and construction margin will reverse during the tax holiday period, anticipated tax benefits of such reversal has been recognized.
6. Under Indian GAAP, dividend recommended by Board of Director’s after reporting period has been recognized as liability which has not been recognized under IFRS in accordance with IAS-10 “Events after Reporting Period”.
7. Stock Option expense has been recognised with a corresponding entry to equity over the vesting period of the Option under IFRS 2, Share-based Payments. Stock Option Account relating to options exercised has been transferred to Securities Premium Account. Stock Option Account relating to options lapsed has been transferred to General Reserve.
8. Under Indian GAAP, losses attributable to non-controlling interest (to the extent it exceeds minority interest in equity of subsidiary) are adjusted against majority interest while in IFRS, such losses are attributed to non-controlling interest.

Insert table 2

Explanatory notes to reconciliation:

1. Under Indian GAAP, provision for overlay has been accumulated on straight line basis while in IFRS the same is being built up in accordance with the provisions of IAS 37, Provisions, Contingent Liabilities and Contingent Assets.
2. Under IGAAP, depreciation on building has been recognized considering useful life as 60 years, however in IFRS depreciation on building has been recognized considering useful life as 30 years.
3. In IFRS useful life of the Intangible Asset has been revised to 30 years in current financial year though in IGAAP, the same has been revised from April 01, 2015. Under Indian GAAP, Intangible asset is being amortised in the proportion of the revenue earned for the period to the total estimated toll revenue i.e. revenue expected to be collected over the concession period in accordance with notification issued by Ministry of Corporate Affairs in April 2012, while in IFRS, the same is being amortised using unit of usage method.
4. Finance charges pertain to accretion of interest on loans and borrowings using the effective interest rate method in accordance with IAS 39, Financial Instruments- Recognition and Measurement.
5. Under Indian GAAP MAT Credit has been classified under current tax in IFRS, the same has been reclassified as deferred tax asset in accordance with IAS-12 “Income Taxes”.
6. Under Indian GAAP, deferred tax liability has been recognized on timing difference

while in IFRS, deferred tax liability has been recognized on temporary differences. Further consequent to change in useful life of bridge in IFRS, certain portion of timing difference in respect of depreciation and construction margin will reverse during the tax holiday period, anticipated tax benefits of such reversal has been recognized.

Conclusion

The study investigates empirically the effect of voluntary adoption and convergence of IGAAP with IFRS. It has been found from our study that there is not much deviations and fluctuations in the net income position as disclosed by financial statement of Wipro Ltd in IFRS reporting and Indian GAAP. But deviation is rather prominent when observing the total liability and equity position which is mainly because of reclassification between equity and total liability. The provision under IFRS is reduced mainly because dividend provision is not recognized in IFRS. Fair value measurement of Available for sale investment and the share compensation expense recognized in IFRS is higher, as in IFRS reporting accelerated amortization of stock compensation expense in the initial years following the grant of options, whereas in Indian GAAP reporting recognizes the stock compensation expenses in graded manner on a straight-line basis over the requisite vesting period for the entire award which resulted in increase in share based payment reserve. In true generalized sense, the return on equity, return on asset, total asset turnover and net profit ration are not significantly affected by converging to IFRS but the leverage ratio shows significant change on converging with IFRS. There are also significant changes in the total equity and total liability position on convergence to IFRS but not prominent changes in the total asset position.

The study suffers with some limitations also. The content discussed in the article is drawn, by and large, from secondary sources, i.e., journal articles, magazines, newspapers, annual report etc. The study is qualitative as well as quantitative in nature but there is less possibility of judging or analyzing the data on basis of our own best judgment because readymade comparative analysis of financial statement of Wipro Ltd under IFRS and IGAAP has been considered in the study due to difficulty in examining the issues through quantitative tools at the very budding stage of this adoption process.

In summary, it be said that differences in accounting methods create information costs for the preparers, auditors, and users of financial statements. Several organizations recognized the need to harmonize financial reporting, and the European Union was one of the first to publish directives to reduce differences in the reporting of similar transactions. Convergence in India would be facilitated by the fact that historically Indian accounting standards have been based on principles as against rules. However, given the nature of accounting and peculiarities of the Indian economic environment, the process of convergence has its own set of challenges. The conflicting legal and regulatory requirements related to financial statements, the technical preparedness of industry and accounting professionals and the economic environment prevailing in the country will pose challenges to this convergence. Given the task and challenges, all the entities should ensure that their convergence plan are designed in such a way as to achieve the objective of doing it once, but doing it right.

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Table 1: Reconciliation of Equity as at March 31, 2015

Particulars	Notes	Indian GAAP US $	Effect of transition to IFRS US $	IFRS US $
Property, plant and equipment	1	828,491	(25,650)	802,841
Capital work in progress	2	44,683	-	44,683
Intangible asset	2	90,614,418	(13,368,558)	78,245,860
Loans and advances	3	11,137,689	(10,885,949)	251,740
Total non-current assets		102,625,281	(23,280,157)	79,345,124
Inventories		60,162	-	60,162
Trade receivables		219,395	-	219,395
Loans and advances		1,017,906	-	1,017,906
Prepayments		55,635	-	55,635
Cash and cash equivalents		12,108,686	-	12,108,686
Total current assets		2,461,784	-	2,461,784
Total assets		105,087,065	(23,280,157)	81,806,908
Provisions	4	1,417,908	(617,934)	799,974
Trade and other payables		527,949	-	527,949
Deferred tax liability	3 & 5	12, 046,143	(12,503,005)	(456,863)
Total non-current liabilities		13,992,000	(13,120,939)	871,060
Interest bearing loans and borrowings		3,413,422	-	3,413,422
Trade and other payables		2,816,073	-	2,816,073
Provisions	6	4,908,507	(3,580,454)	1,328,053
Provisions for taxes		2,677	-	2,677
Total current liabilities		11,140,678	(3,580,454)	7,560,225
Total liabilities		25,132,678	(16,701,393)	8,431,285
Total assets less total liabilities		79,954,387	(6,578,764)	73,375,623
Issued capital		42,419,007	-	42,419,007
Securities premium	7	23,107,215	99,106	23,206,321
Debenture redemption reserve		863,956	-	863,956
Net unrealized gains reserve	2	-	-	-
General reserves	7	874,799	8,036	882,835
Effect of currency translation		(12,670,643)	(5,176,593)	(17,847,236)
Retained earnings (profit & loss A/C)		25,360,053	(1,338,911)	24,021,142
Total		79,954,387	(64,08,362)	735,46,025
Non-controlling interest	8	-	(170,402)	(170,402)
Total equity		**799,54,387**	**(65,78,764)**	**733,75,623**

Table 2: Reconciliation of Income Statement as at March 31, 2015

Particulars	Notes	Indian GAAP US $	Effect of transition to IFRS US $	IFRS US $
Total revenue		16,918,536	-	16,918,536
License fee		3,249,945	-	3,249,945
Miscellaneous income		9,72,751	-	9,72,751
Total income		1,141,232	-	1,141,232
Operating and administrative expenses				
Operating expenses	1	2,411,911	(162,093)	2,249,818
Administrative expenses		3,563,593	-	3,563,593
Depreciation	2	101,031	26,254	127,285
Amortization	3	268,907	5,488,778	11,698,220
Total operating and administrative expenses		6,345,442	5,352,778	11,698,220
Operating profit from continuing operations		14,795,790	(5,352,778)	9,443,012
Finance income				
Profit on sale of investments		265,643	-	265,643
Finance charges	4	(1,337,066)	874,315	(462,751)
Total		(1,071,423)	874,315	(197,108)
Profit from continuing operations before tax		13,724,367	(4,478,463)	9,245,904
Income taxes:				
Current tax	5	-	(2,913,164)	(2,913,164)
Deferred tax	6	(681,532)	10,661,575	9,980,043
Profit after tax		130,42,835	32,69,948	163,12,783
Attributable to :				
Equity share holders		13,042,835	33,55,200	163,98,035
Minority interest		-	(85,252)	(85,252)