IFRS convergence & alignment of Indian Accounting Standards: An Insight on Ind AS Carve-outs

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ABSTRACT
In the present scenario, most of the Indian Multinational companies are emphasizing on establishing their businesses in emerging economies to get exposure to global markets, with an intention to fulfil their capital needs by getting their securities listed on the foreign stock exchanges. Hence a need arises to have uniform accounting standards for global business.

Also, foreign companies establishing a presence in India will encounter a host of considerations that do not exist in their home country. Thus, it can be a difficult challenge for understanding & interpreting India’s distinctive accounting system.

Until recently, India, like many countries in Asia, employed a very old set of generally accepted accounting principles (GAAP) that often proved difficult for foreign firms to adhere to.

Hence, the Institute of Chartered Accountants in India (ICAI) set out to introduce a new system, called Indian Accounting Standards (IND AS) an “Indian Juggad” which are converge more closely with the global standard, International Financial Reporting Standard (IFRS).

This has given harmonized financial reporting standards which are intended to provide a common basis of financial reporting, wider investment choice, more efficient capital market, lower cost of capital & enhanced business development.

This research paper is an attempt to study and explain the significant differences between IFRS (International Financial Reporting Standards) and IND AS and to provide a brief insight on Ind-AS Carve-Outs.

Keywords: Accounting Standards, IFRS, IND AS, Carve-outs, MCA, NACAS, ICAI
INTRODUCTION

“Accounting is the Language of Business” - Warren Buffett

Language is meant for men to express their feelings in written or verbal form. Similarly, the business entities convey the various information of the business through accounting statements. A business communicates its financial position to the concerned persons like owners, investors, employees etc. through its financial statements.

Since now, the Indian companies are emerging and doing business with the companies in the other countries, also a lot of foreign direct investments are happening. The need arises to have a common global language of accounting, with an aim to make companies' accounts understandable and comparable across international boundaries.

In order to make it happen, India has converged with IFRS and came up with its very own Indian version-IND AS which is a new set of global accounting standards in a phase wise manner. This has given harmonized financial reporting standards which are intended to provide a common basis of financial reporting, wider investment choice, more efficient capital market, lower cost of capital & enhanced business development.

The idea of converging Indian Accounting Standards with IFRS is to facilitate

1. Capital inflows in India
2. Obtaining global recognition for our balance sheet
3. International acquisitions
4. Systematic consolidation of financial statements of multinational companies operating in India and Indian companies operating abroad.
5. Movement of learned accounting professionals from India across the world.

IND AS Convergence in India-The Roadmap:(Minister et al., 2017)

On 16 February 2015, the Ministry of Corporate Affairs (MCA) finally notified the much awaited Indian Accounting Standards (Ind AS) which are converged with International Financial Reporting Standards (IFRS).

IND AS to be adopted in a phased manner for the financial year beginning on or after 1st April 2016 with comparatives for the year ending 31st March 2016 for certain class of companies.

On 30th March 2016, MCA notified the companies (Indian Accounting Standards) Amendment Rules, 2016, which include Ind AS implementation roadmap by banks & NBFCs. (Mca & As, 2016)

On 5th April 2018, RBI has deferred Ind AS implementation by one year for scheduled commercial banks.

RBI issued circular providing directions to all scheduled commercial banks (excluding regional rural banks) to submit their pro-forma Ind AS financial statements for the half year ended 30th September 2016, latest by 30th November 2016.
## IND AS Convergence in India - Phase-wise adoption (Trust, 2019)

<table>
<thead>
<tr>
<th>Mandatory Adoption</th>
<th>PHASE I</th>
<th>PHASE II</th>
<th>Voluntary Adoption</th>
</tr>
</thead>
<tbody>
<tr>
<td>Listed companies or companies in the process of listing and having net worth of Rs.500 Crore or more (debt or equity listed in or outside India)</td>
<td>Listed companies or companies in the process of listing and having net worth of less than Rs.500 Crore (debt or equity listed in or outside India)</td>
<td>Companies can voluntarily converge with IND AS from 1st April 2015 with comparatives for 31st March 2015.</td>
<td></td>
</tr>
<tr>
<td>All other unlisted companies having net worth of Rs.500 Crore or more.</td>
<td>Unlisted companies having net worth of Rs.250 Crore or more but less than Rs.500 Crore.</td>
<td>Audited standalone financial statements as on 31st March 2014 to be considered for the calculation of net worth.</td>
<td></td>
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<tr>
<td>Holding, subsidiary, joint venture or associate companies covered above.</td>
<td>Holding, subsidiary, joint venture or associate companies covered above.</td>
<td>Net worth does not include revaluation reserves; write back of depreciation &amp; amalgamation reserve.</td>
<td></td>
</tr>
<tr>
<td><strong>Accounting period beginning from 1st April 2016 with comparatives for 31st March 2016.</strong></td>
<td><strong>Accounting period beginning from 1st April 2017 with comparatives for 31st March 2017.</strong></td>
<td>Once IND AS is followed, it shall be followed for all subsequent years.</td>
<td></td>
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</tbody>
</table>

## IND AS Convergence in India - The Roadmap for NBFCs

<table>
<thead>
<tr>
<th>Covered NBFCs</th>
<th>PHASE I</th>
<th>PHASE II</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Listed NBFCs</td>
<td>All NBFCs with net worth &gt;= INR 500 Cr.</td>
<td>All NBFCs listed or in the process of listing.</td>
</tr>
<tr>
<td>b. Unlisted NBFCs</td>
<td>All NBFCs with net worth &gt;= INR 500 Cr.</td>
<td>All NBFCs with net worth &gt;= INR 250 Cr.</td>
</tr>
<tr>
<td>c. Group companies</td>
<td>Applicable to holding, subsidiary, joint venture or associations of NBFCs covered in (a) and (b) above other than those already covered under roadmap for other companies.</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year of Adoption</th>
<th>Comparative Year</th>
<th>IND AS Transition Date</th>
<th>Covered NBFCs</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018-19</td>
<td>2017-18</td>
<td>1st April 2017</td>
<td>All NBFCs with net worth &gt;= INR 500 Cr.</td>
</tr>
<tr>
<td>2019-20</td>
<td>2018-19</td>
<td>1st April 2018</td>
<td>All NBFCs listed or in the process of listing.</td>
</tr>
</tbody>
</table>

1. Applicability of IND AS for the banks has been deferred by RBI
2. Insurance companies expected to apply IND AS from accounting periods beginning on or after 1st April 2020.
3. Voluntary early adoption is not permitted.
This transition has thrown many accounting challenges for companies which come under the purview of this compliance. Also, Indian GAAP is still valid for the companies which do not fit in the above criteria. In such a case, it becomes so crucial to know the differences or carve-outs to bring the local standards closer to the global arrangements.

As Ind AS are largely converged with IFRS, Indian Accounting Standards setters have worked out & made some modifications, popularly known as ‘Carve-Outs’ to suit Indian economic & business environment.

Even though this transition has brought significant change in the financial reporting landscape in India, the ongoing convergence of Ind AS and IFRS is a worthwhile endeavour for the global comparability & transparency.

II. RATIONALE OF THE RESEARCH:

The convergence of Ind AS and IFRS introduces several new and complex concepts which will definitely have an effect on the financial statement of the companies. Hence, this research exploring Ind AS carve-outs would positively bring new outcomes which will be very helpful not only for the new researchers but mainly for the preparers of financial reports in India.

III. RESEARCH OBJECTIVE

1. To find out the “Carve-outs” of Ind AS from IFRS.
2. To examine the reason behind Ind-AS Carve-Outs.

IV. RESEARCH METHODOLOGY

This research work is descriptive and exploratory in nature where the Ind AS Carve-outs is explored. It also provides researcher’s insight on these “Carve-outs”. The data is collected from the secondary sources through various notifications & guidelines provided by the governing bodies, websites, and journals as well as published books.

V. RESEARCH SCOPE

This research paper covers only the differences or “Carve-outs” of Ind AS with IFRS. It does not discuss the challenges and opportunities that this convergence has brought and its impact on financial statements of the companies.

VI. LITERATURE REVIEW:

1. (Basu, 2021) positively stated that the convergence of Indian accounting standards with IFRS is a significant step towards becoming the dominant economic force in the world economy and explained the Ind-AS carve-outs from IFRS very precisely. It also highlighted how Indian business models are evolving and competing with world economy with more efficient and intellect human resource which are capable to compete with the professionals in the developed countries.

2. (Ojha, 2021) presented a detailed analysis on IFRS adoption in India and stated that the IFRS convergence leads to better integration and management of global operations than GAAP.

3. (Raval, 2017) pointed out the positive and negative outcomes of convergence of Indian accounting standards with IFRS. It also stated that the implementation of Ind-AS would bring lot of challenges to the entities as they are very much use to with the Indian GAAP, now with this new implication mandate both cost and expertise will be affected.

4. (Lious et al., 2016) adoption of IFRS in India is analysed based on the stock returns and price models of regression to find out the importance or value relevance of the convergence of IFRS in India.
5. (Colleges & Pal, 2015) explained three major potentially irreconcilable differences occur in the topics IND AS 19: Employee Benefits, IND AS 32: Financial Instruments – Presentation and IND AS 103: Business Combinations. The author finally concluded on a positive note that the complete convergence of Indian accounting standards with IFRS can indeed be possible one day.

6. (Ashok Kumar, 2014) Indicated that the transition journey towards Indian GAAP to Ind AS is quiet difficult but at the same time it benefited the users at large. Harmonization and convergence needs efforts from all parties because IFRS is a principle based approach rather than a rule based approach. The challenges with the implementation process of Ind-AS are well explained.

7. (Next et al., 2014) stated that to adopt this big change in the form of Ind AS in Indian accounting system is very exigent and the companies must proactively initiate the processes and systems to get the best fit as per its business needs. It is believed that once companies adopt Ind AS, a large number of transactions which were earlier carried out in the form of an asset acquisition would now become a business combination. The companies would be required to carry out a fair valuation exercise and identify assets and liabilities being taken over, including goodwill or reserves, if any.

VII. FINDINGS & DISCUSSIONS

The Concept:

The ‘Carve-Outs’ means deviation or differences and in this research paper we are discussing the Ind AS Carve-Outs or say deviations from International Financial Reporting Standards (IFRS), as India had decided to have convergence not adoption to have smooth implementation of global standards without disturbing India’s business & economic environment.

In simple terms, convergence of Indian accounting standards with international financial reporting standards (IFRS) means that India would not be applying IFRS as issued by the international bodies but would try to get its own accounting standards in sync with the IFRS & this arrangement is popularly known as Ind-AS.

This is obvious, as the Indian economy is in the developing stage as compared to the other developed countries of the world economies and so the accounting procedures. This is why applying IFRS as it is in India is not possible, also Ind-AS won’t be completely synchronised with the IFRS as of now.

The Main Discussion: Need of Ind-AS Carve-Outs

The core objective of preparing financial statements is to provide useful information to the investors, stakeholders and potential investors. And this objective is met only when there is a uniform accounting policy that results in fair presentation of economic consequences of transactions on the financial position and performance of the entity and complete disclosure of the material information.

It is needless to say that accounting standards control accounting policy. They specify the most appropriate accounting principles, methods and disclosure requirements. These are meant for implementation by companies operating in different regions or territories.

This is why the accounting standards setters take almost everything into consideration like the culture and customs of the territory, competencies of the preparers and auditors of the financial statements and even the skills and abilities of the analyst and the investors while framing the Ind AS.

It is not possible for the global standard like IFRS, to take into account the environment and capabilities available in each country. Therefore the national standard setters modify and customize IFRS, wherever required keeping the deviations as minimal as possible.

We must appreciate ICAI and NACAS for adopting the policy of carving out and carving in IFRS while formulating Ind-AS. The convergence with essential deviations from IFRS is a better option than adopting it as it is.
The Carve-Outs in Ind-AS from IFRS are discussed under:

The Ind-AS has been prepared by NACAS along with ICAI and MCA after considering comments and suggestions from various industry representatives. The final Ind-AS have the following carve-outs from IFRS to bridge the gap in application of accounting policy and economic conditions prevailing in India.

1. Business Combinations: Gain on Bargain Purchase

**IFRS 3 Business Combinations:** It requires the excess of fair value of identifiable net assets acquired over the purchase consideration to be recognised in Profit or Loss as **Gain on Bargain Purchase.**

**Ind AS 103 Business Combinations Carve-Out:** It requires that the acquirer should first examine whether there was indeed a bargain purchase i.e. the asset is acquired for less than the fair market value.

The acquirer should find out whether there are any circumstances which indicate that he had made a bargain purchase, for example an unhappy sale in which the seller is acting under compulsion. In such a case, the acquirer recognises the resulting gain in other comprehensive income (OCI) on the date of acquisition and accumulates the same in equity as capital reserves.

However if the business combination is not classified as a bargain purchase the excess is recognised directly in equity as capital reserve.

**Ind AS 103, Business Combinations, mandates the recognition of assets acquired and liabilities assumed at fair value on the acquisition date, this further complicates the accounting. Hence the entities have to appoint or engage valuers to calculate & apply fair value to assets (mainly customer contracts and brand) and liabilities to meet the rigorous requirements of the standard.**

2. Effect of Foreign Exchange Rates: Unrealised Exchange Differences

**IAS 21 Effect of Foreign Exchange Rates:** IFRS requires all foreign exchange differences to be recorded immediately in the statements of profit or loss.

**Ind AS 21 Carve-Out:** It provides an option to recognise unrealised exchange differences arising on the translation of long-term foreign currency monetary assets and liabilities either directly in equity and accumulated in a separate component of equity. *(Ministry of Corporate Affairs, 2019)*

This accumulated amount is then transferred to profit or loss over the period of maturity of such long term monetary items in an appropriate manner.

It was mandatory to bring Ind AS 21 Carve-out on unrealised exchange differences, because over the last few years, many Indian companies have borrowed funds from foreign countries especially in US dollars or Euros or Yen. Converting these foreign currency borrowings into Indian rupees at the end of each period creates huge volatility in the profit or loss account of the current accounting period even though it is repayable after a specific period.

3. Financial Instruments: Recognition & Measurement

Under **IFRS 9,** Financial Assets classified under fair value through Profit or Loss (FVTPL) & fair value through other comprehensive income (FVTOCI) will be measured at fair value to profit or loss and other comprehensive income (OCI) respectively.

Financial Assets & Liabilities classified under amortised cost will be measured at amortised cost using Effective Interest Rate (EIR) method.

Financial liabilities classified under FVTPL will be subsequently measured at fair value with changes in fair value to profit or loss except for changes in fair value due to its own credit risk. Such changes will be transferred to OCI.
Ind-AS 39 Carve-Out: Determining the fair value of the financial liabilities classified as FVTPL upon initial recognition, any change in the fair value due to changes in the entity’s own credit risk will be ignored.

The accounting for Financial Instruments has undergone complete change. It has affected the balance sheet ratios to the great extent due to change in classification of instruments as liability or equity.

Use of effective interest rate method for calculating interest costs and recognition of fair value changes has also impacted the performance measures. Now, companies have to be very cautious while undergoing financial contracts to avoid accounting complications.

4. Investment Property:

Under IAS 40-Investment Property there is an option to apply either cost model or the fair value model. If a fair value model is used, all investment properties including those under construction are measured at fair value & changes in the fair value are recognized in the Profit or Loss for the period in which it arises. Under the fair value model the carrying amount is not required to be depreciated.

Ind-AS 40 Crave-Out: Ind AS does not permit the use of a fair value model. It requires investment property to be measured under cost model only. Also it requires the fair value of the investment property to be disclosed in the notes to financial statements.

The Ind AS 40 Carve-out on investment property was made primarily for the industries where the price includes a cash component, as the fair value assessment of the investment property becomes difficult in such cases.

5. Employee Benefits:

Under IAS 19 market yields at the end of the reporting period on high quality corporate bonds are used as discount rates. In countries where there are no deep markets for such bonds, market yields on Government bonds are used.

Ind-AS 19 Carve-Out: It does not permit the use of yield on high quality corporate bonds but requires the use of of yield on Government bonds for Indian entities however provision of of IAS 19 are applicable for foreign subsidiaries associates and joint arrangements

6. Government Grants:

Under IFRS, Government grants related to assets can be presented in the balance sheet either by setting up the grant as deferred income or by detecting the grant in arriving at the carrying amount of the asset.

Ind-AS 20 Carve-out: It requires grants related to assets to be presented in the balance sheet only by setting it up as deferred income. The option for deducting the grant from the carrying amount of the asset is not available under Ind-AS 20. (Assistance, n.d.)
7. Presentation of Financial Statements:

<table>
<thead>
<tr>
<th></th>
<th>IAS 1</th>
<th>Ind AS 1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance Sheet</td>
<td>Statement of Financial Position</td>
<td>Balance Sheet</td>
</tr>
<tr>
<td>Statement of Profit &amp; Loss</td>
<td>Statement of Profit or Loss and other comprehensive Income</td>
<td>Statement of Profit &amp; Loss.</td>
</tr>
<tr>
<td>Presentation of single or separate statement (Profit or Loss and OCI)</td>
<td>Allows presentation of Profit or Loss A/c either as a single statement giving a separate heading of OCI or two different statements</td>
<td>Allows only the single statement approach</td>
</tr>
<tr>
<td>Statement of changes in equity</td>
<td>Required to be present as a separate statement</td>
<td>Schedule III Div. II required Statement of changes of equity to be shown as a part of Balance sheet</td>
</tr>
<tr>
<td>Classification of Expenses</td>
<td>Allowed either by nature or by function. however if expenses are classified on the bases of function then disclosure to be given for classification by nature in notes</td>
<td>Allowed by nature only</td>
</tr>
</tbody>
</table>

8. First Time Adoption of Ind-AS

There are few differences in first time adoption of Ind-AS and the first time adoption of IFRS. Key carve-outs are discussed under:

Under IFRS 1, the first time adopter may elect to measure an item of its PPE at the date of transition to IFRS at its fair value & this fair value is nothing but the deemed cost to be considered on the date of transition.

**Under Ind AS 101**, the adopter can continue with the carrying values of its PPE as on the date of transition to Ind AS, in accordance with previous GAAP i.e.Indian GAAP and use that as its deemed cost.

Under IFRS 1, the entities are required to present comparatives.

Under **Ind AS 101**, entities are not required to present comparative information. They have an option to present memorandum comparative information based on the deemed transition date as of the beginning date of immediately preceding the financial year.

**Other Carve-outs for first time adopters of Ind AS**

1. Previous GAAP is always Indian GAAP.
2. Option to adjust capital reserve /goodwill in case past business combinations are restated.
3. No exemption to apply borrowing cost standard prospectively.
4. A first time adopter may continue the policy adopted for accounting for exchange differences arising from translation of long term foreign currency monetary items recognised in the financial statements for the period ending immediately before the beginning of the first Ind-AS financial reporting period as per the previous GAAP. (As & Facilitation, 2016)
5. Additional exemption to use the transition date facts and circumstances for lease arrangements which includes both land and building elements to assess the classification as on the transition date.
6. Option to use the transitional date circumstances to measure non-current assets held for sale and discontinued operations at the lower of carrying value and fair value less cost to sell.
VIII. CONCLUSION

Convergence of Indian accounting standards with IFRS have been a real challenge not only for the standard setters but also for the preparer of financial statements, analysts & investors.

But, it is equally true that this transition has brought significant change in the financial reporting landscape in India and it is a worthwhile endeavour for obtaining global recognition, comparability & transparency.

The Carve-outs have had a significant impact on the financial statements. These carve-outs are made for a specific reason, and are accordingly customised to implement it smoothly without disturbing the economic and business conditions prevailing in India.

To conclude with, Ind AS is not a “one size fits all” tool and this is why every company will have to cautiously develop an accounting framework of adopting Ind AS according to its business needs. An in-depth understanding of the Ind-AS & IFRS standards and their applicability is a real challenge for all the business leaders, accounting professionals and auditors in India. But it is needless to say that it has brought a lot of learning and growth opportunities for accounting professionals and has opened a new horizon for Indian businesses in the global market.

IX. REFERENCES: