CHAPTER III

ACCOUNTING STANDARDS ON SEGMENT REPORTING: GLOBAL SCENARIO
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3.1 INTRODUCTION

With the paradigm shift in the economic environment, the accounting landscape has also been changed through the emergence of accounting standards. Accounting standards are a kind of codified accounting grammar that offers guideline as to how the transactions and events should be recognized, measured and reported in the financial statement. These are formulated for harmonizing different accounting policies and practices and for reducing the accounting alternatives in preparation of financial statements within bounds of rationality. It ensures reliability and comparability of information which are reported in the financial statement with a view to provide relevant information to the stakeholders who take various economic decisions. In almost all jurisdictions of the world, accounting standards become an essential component of the Generally Accepted Accounting Principles (GAAP). Thus, accounting standard plays a major role in regulating the quality and content of the financial statements. This standardization of financial reporting should also affirm the reflection of the underlying economic realities of transactions. As a result, financial reporting becomes quality-full which is of paramount important particularly for effective and efficient functioning of the market economy. For achieving this desired result, accounting standard itself need to be high quality as they are intended to improve the quality of the financial reporting and also it is very urgent to proper implementation.

The main thrust of this chapter is to explore the prevailing relevant accounting standards on segment reporting along with their role particularly in reporting
practices. To address this prime objective this chapter has been classified into ten parts. First part deals with the introduction in which this particular objective of this chapter has been established. The second part has digging out the origin of accounting standard. Third and fourth parts of this chapter have made a theoretical discussion regarding concepts of accounting standards and its types respectively. Fifth and sixth parts subsequently highlighted necessity of the accounting standard in general along with the needs of disclosure standards more particularly standard on segment reporting. Part seven of this chapter has explored the prevailing relevant accounting standards on segment reporting and made a closer comparison among them to highlight the diversity in their requirements. Next part of this chapter has thrown a light on the emergence of convergence process and the converged accounting standard (i.e. IFRS 8) on segment reporting along with its critical evaluation. Part nine has evaluated the role of prevailing accounting standards including IFRS 8 to resolve the practical problems of segment reporting. A logistic conclusion has also been offered in the last part of this chapter.

3.2 ORIGIN OF ACCOUNTING STANDARD

Accounting standard setting has become a flourishing industry; almost all economically significant countries have arrangement for establishing and implementing accounting standards. Some of them allow the private body to do this remarkable function whereas others rely upon the government initiative for establishment and implementation of the accounting standard. To highlight the origin of accounting standards, a brief history of the accounting standard is explained hereunder for only some economically significant countries including India.
USA

After the wake of great stock market crash in 1929, the idea of having accounting standards comes into the reality. In the year 1934, with the collaboration of New York Stock Exchange, a committee of the American Institute of Accountants (AIA) produced a seminal document entitled ‘Audits of Corporate Accounts’ which set out the general principles to be followed in the preparation of financial statements. In the same year, the US Congress constituted a statutory authority, Securities and Exchange Commission (SEC) to prescribe the accounting policy for publicly traded companies. Although SEC had not preferred to be directly involved in the process of preparation of accounting standard but it acted as a leader in establishing and improving the accounting standards. In 1938, AIA formed a Committee on Accounting Procedures (CAP) for issuing pronouncements on the financial reporting. Subsequently, within 1959, CAP had issued 51 accounting research bulletins which particularly explored the verity of accounting problems. In the year 1940, American Accounting Association published a monograph entitled ‘An Introduction to Corporate Accounting Standard’ which popularized the matching principle and also provided the theoretical basis for financial reporting (Flower, 2002). Although it had no official status but it was widely distributed among the practicing accountants. In the year 1959, the successive body of AIA, American Institute of Certified Public Accountants (AICPA) had replaced the CAP by the Accounting Principle Board (APB) with a view to narrowing the areas of differences in accounting treatment and to resolving some unsettled controversies. By 1973, it had issued 31 opinions on a wide range of fundamental issues. Subsequently, according to the recommendations of Wheat Committee a new independent standard setting body, Financial Accounting Standard Board (FASB) was constituted. The Wheat Committee was also claimed the
term accounting standard would be more appropriate for accounting pronouncements than the term accounting principles. FASB had accepted this term for its accounting pronouncements and other accounting standard setter also adopted it.

**UK**

In the year 1942, the council of the Institute of Chartered Accountants in England and Wales (ICAEW) launched a scheme of issuing Recommendation on Accounting Principles (RoAPs) for providing practical guidelines on financial reporting. In response to the various criticisms those were generated from number of reporting scandals, the Accounting Standard Steering Committee (ASSC) was setup in 1970. Subsequently name of the committee had been changed to Accounting Standards Committee (ASC) and issued pronouncements in the form of statements of Standard Accounting Practices (SSAP). In the line of the recommendation of the Dearing committee, the Accounting Standard Board (ASB) was set up in place of ASC in 1990 and from 1992 it began issuance of accounting standards, Financial Reporting Standards (FRSs). At present ASB provides the efforts for eliminating the differences with the standards of IASB and also try to align its own standards with IASB’s standards.

**Australia**

In 1946, in the line of recommendations made by the Institute of Chartered Accountants in England and Wales (ICAEW), Institute of Chartered Accountants in Australia (ICAA) issued several recommendations on accounting principles. In response to the series of striking corporate collapses in the early 1960s, the Australian Accounting Research Foundation (AARF) was formed in 1966 for producing appropriate accounting standards to guide the profession. To reduce the dominance of the accounting profession, a statutory authoritative body, Australian Accounting
Standard Board (AASB) was developed in 1991. Now the body tries to implement the strategic plan for adoption of the international standards since 2002.

**India**

In 1977, the Institute of Chartered Accountants of India (ICAI) constituted the Accounting Standard Board (ASB) for developing the accounting standards. This board formulates the accounting standards in the line of international standard in force. For formulating various standards it also developed a conceptual framework which is more or less similar to the conceptual framework of IASB. It also gives due considerations to laws, customs, usages and business and economic environment prevailing in India. It issued its first standard in the year 1979 as ‘Accounting Standards’ (AS). It has issued 32 AS in total so far. Initially these standards were recommendatory but after realizing the utility, steps were taken to make them mandatory (Banerjee, 2002). Although these standards have developed in the line of corresponding international standards but still there are some differences. In the line of the other countries, India is also going to converge with the IFRSs. Accordingly, the Ministry of Corporate Affairs has recently notified 39 converged Indian Accounting Standards (Ind AS).

**3.3 CONCEPT OF ACCOUNTING STANDARD**

Accounting is a business language used to communicate the financial performance and position of the reporting entity. Like every language, it has a grammar which is popularly known as accounting standard. It ensures transparency, consistency, comparability, adequacy and reliability of the financial reporting through harmonizing the diverse accounting policies, practices and credibility. According to the Kohler’s dictionary “Accounting standard is 1) a code of conduct imposed on accountants by custom law or professional body; and 2) accounting principle”.
According to Littleton (1953) “A Standard is an agreed upon criteria of what is proper practice in a given situation; a basis of comparison and judgment; a point of departure when the variation is justifiable by the circumstances and reported as such. Standards are not designed to confine practice within rigid limits but rather to serve as guideposts to truth, honesty and fair dealing”. Bromwich (1985) defines accounting standards are “uniform rules for financial reporting applicable either to all or to a certain class of entity promulgated by what is perceived of as predominantly an element of the accounting community specially created for this purpose”. In this regard it is important to note the observation made by the advisory group on International Accounting and Auditing constituted by RBI standing committee on International Financial Standards and Codes – “Accounting standard can be described as a vehicle where by the wisdom and experience of the profession emerges as a consensus in a complex and changing economic and business situation in preference to the views of individual compilers of financial statements”. Accounting standard may be defined as a written policy document, issued by the authoritative bodies to prescribe guidance and direction for recognition, measurement, treatment, presentation and disclosure of business events and transactions in the financial statement.

3.4 TYPES OF ACCOUNTING STANDARD

Basically there are four types of accounting standards - layout and presentation standards, recognition and measurement standards, disclosures standards and mixed standards those are explained one after another.

Layout and presentation standards — to ensure the comparability these standards deal with the structure for presentation of financial information; that is how information should be displayed in the financial statement. Financial statement should
reflect the financial information in a cohesive and complete portrays manner so that it become useful to a wide range of users particularly in their decision making process.

**Recognition and measurement standards** — it is more important to determine what is to be presented in financial statement compared to the form of presentation. Recognition requires identification of financial events and transactions which are to be reported and measurement process translated the business events and transactions into monetary term at which it should be reported in financial statement. These standards are of very crucial in nature as they direct the way in which periodic performance is computed and balance sheet figures are determined.

**Disclosures Standards** — these standards deal with the requirements of supplementary information that is to be disclosed to make financial statement full and fair. They protect the stakeholders’ interest from unfair treatment and enhance the usefulness of financial report through informative disclosures.

**Mixed Standards** — these standards are admixture of any two types of standards that is either measurement and disclosure or disclosure and presentation; that means they have at least two categories requirements. There are many accounting standards of this type.

### 3.5 NEED FOR ACCOUNTING STANDARD

Primarily accounting standard helps to minimize the diversity in reporting style, that means standardize the accounting practices. It promotes the comparability through uniformity in accounting procedures for the similar types of accounting events and transactions. It also ensures relevancy and reliability of the financial statement. In fact financial statements will generate high quality information which would lead to informed decision making by stakeholders. Accounting standards also appreciate the recent motive of stakeholders through changing the central focus of
statements. Recently financial statements use to reflect the useful economic information which are very relevant to stakeholders in contrary to the stewardship information (i.e. information regarding the utilization of the resources and financial earnings). This motive has been reflected in the SFAC 1 of the FASB that financial reporting “should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit and other decisions” (FASB, 1978). This improved decision making process leads to the efficient allocation of the scare recourses and confess speedy growth of the economy. It acts as an essential foundation of efficient and liquid capital market. In the word of former chairman of SEC, Arthur Levitt “good standards, like good cameras, produced sharper, more accurate pictures”.

3.6 NEED FOR THE ACCOUNTING STANDARD ON SEGMENT REPORTING

There has always been a conflict between transparency and secrecy - reservation about complete financial information disclosures for maintaining the business secrecy. But in this robust diversified and globalized business environment, aggregated financial report alone is insufficient to reflect rate of profitability, opportunities for growth, future prospects and risks which a diversified entity faces. The increasing complexity of business structure and transaction has also made it necessary for accounting standard setters to place greater emphasis on disclosures. Naturally a consistent pressure has forced the accountant and professional bodies to shape the financial report in such a manner that it can meet the needs and expectations of the users. Accordingly segment reporting become popularized as a crucial part of financial statement particularly to reflect the risks and opportunities which have been faced by various operating segments of the reporting entity. Keeping in view of the
needs of users of financial statement, major accounting bodies have come out with specific accounting standards on segment reporting for ensuring the segmental disclosures practices more meaningful and relevant.

These standards guide and direct as to how the reportable segment should be identified and what disclosures should be made to make up the segment report. The accounting standards are setup mainly to harmonize the diverse accounting policies and practices which will assist the stakeholders for making efficient economic decisions. So accounting standards reduces the possibility of varying assessment for the same operating result by ensuring accounting information on a more comparable and consistent manner. The introduction of accounting standard on segment reporting should also ensure the transparency of reporting through the reflection of useful information to stakeholders what they rightly deserve. The segment report should enable the users to evaluate nature and financial effect of various business activities of the reporting entity as well as the economic environment in which it operates. Due to this mandatory requirement of segment reporting managers become bound to disclose all require relevant segmental information along with the aggregated information. As a result, competitors will await results of each other although they try to not disclose more than what competitors reveal. Segment report is projected to be of great benefit in enhancing the ability of stakeholders to better understand the underlying economic reality of a diversified entity. This disclosure-driven accounting standard is also expected to help them to make more informed judgement about the entity as a whole and to assist them in achieving an enhanced degree of comparability with other entities.
3.7 IMPORTANT ACCOUNTING STANDARDS ON SEGMENT REPORTING AND THEIR COMPARISON

The concept of segment reporting in a finalized form is almost 40 years old. It was in 1976 that the Financial Accounting Standard Board (FASB) of USA issued SFAS 14 Financial reporting for segment of a business enterprise with strong encouragement from financial analyst community. This is the beginning point of segment reporting. In June 1997, FASB was issued SFAS 131 which is revised format of the SFAS 14. In 1981 international accounting standard setters, International Accounting Standard Committee (IASC) issued International Accounting Standard 14 (IAS 14) Reporting Financial Information by Segment. This was revised by IASC in 1997. In India the Accounting Standard Board of the Institute of Chartered Accountants of India (ICAI) issued Accounting standard 17 (AS 17): Segment Reporting. SFAS 131 is effective from the financial year beginning after December 15, 1997. Earlier application was encouraged. SFAS 131 need not be applied to interim financial statements. IAS 14 become effective from the period beginnings on or after July1, 1998. It does not require segment disclosure for interim report. AS 17 comes into effect from the accounting period commencing on or after 01-04-2001 and is mandatory in nature. In this regard one thing can be notable, SFAS had made voluntary disclosure about segment reporting for interim periods for the listed companies for the quarter ended 30-09-2001 but it had made compulsory for all the listed companies announcing their results for the quarter ended 31st December 2001.

In the age of convergence, IASB has issued a number of new International Financial Reporting Standards (IFRS) to replace some International Accounting Standards as part of its convergence project. In this project IASB and FASB try to reduce difference between IFRS and US Generally Accepted Accounting Principle
(US GAAP), resulting into IFRS 8 replaces IAS 14 and aligns segment reporting with the requirements of SFAS 131. A snapshot of important accounting standards on segment reporting is given in the following table:

**Table 3.1: Important Accounting Standards on Segment Reporting**

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Jurisdiction</th>
<th>Issuing Authority</th>
<th>Standard</th>
<th>Title</th>
<th>Issued Date</th>
<th>Effective Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>3</td>
<td>USA</td>
<td>FASB</td>
<td>SFAS 131</td>
<td>Disclosure about Segment of an Enterprise and Related Information</td>
<td>June, 1997</td>
<td>December, 1997</td>
</tr>
<tr>
<td>5</td>
<td>India</td>
<td>ICAI</td>
<td>AS 17</td>
<td>Segment Reporting</td>
<td>October, 2000</td>
<td>April, 2001</td>
</tr>
<tr>
<td>6</td>
<td>International</td>
<td>IASB</td>
<td>IFRS 8</td>
<td>Operating Segments</td>
<td>November, 2006</td>
<td>January, 2009</td>
</tr>
<tr>
<td>7</td>
<td>India</td>
<td>ICAI</td>
<td>Ind AS 108</td>
<td>Operating Segments</td>
<td>February, 2011</td>
<td>April, 2016</td>
</tr>
</tbody>
</table>
To facilitate the close comparison among relevant accounting standards on segment reporting, first of all, some sort of summary of that prevailing accounting standards are given below:

3.7.1 SFAS 131: Disclosures about Segment of an Enterprise and Related Information

FASB issued the new SFAS 131, ‘Disclosures about Segment of an Enterprise and Related Information’ on the place of old accounting standard on the segment reporting SFAS 14. This standard is effective for financial statements for periods beginning on or after December 15, 1997.

SFAS 131 changes the framework for reporting operating segments information and identification process of operating segments to a system based on company’s management approach. Operating segments is a component of an enterprise, the management established for the purpose of decision making about the enterprise’s operating matters. The enterprise may combine two or more segments: 1) if they have similar long-term financial performance and same features in product or services, production process, technology, type or class of customers, distribution method of product or services. 2) if they operate under the same regulatory environment.

The quantitative thresholds also have to be taken into consideration to identify the reportable segment. The quantitative threshold are i) 10% revenue criteria ii) 10% absolute amount of profit of loss iii) 10% assets criteria and iv) 75% consolidated revenue criteria which are similar to IAS 14.

Disclosures

It does not require that an enterprise reports segment cash flow statement. However, an enterprise reports certain items that may provide an indication of the
The disclosures requirements of SFAS 131 are given below:

A. General information

- Factors used to identify reportable segments.
- Types of products or services those are reportable segments provide.

B. Information about profit or loss and assets

- Revenue from external customers.
- Revenue from inter segment transaction.
- Interest-revenue and expenses.
- Depreciation, depletion and amortization expenses.
- Equity in net income of investees accounted for under the equity method.
- Income tax expenses or benefits.
- Extraordinary items.
- Other significant non-cash items.

C. Basis of measurement

- Basis of accounting for inter segment transaction.
- Nature of difference between the measurement of profit or loss of reportable segments and enterprise as a whole.
- The nature of any difference between the measurement of segment assets and consolidated assets.
- The nature of the changes from prior periods in the measurement methods used to determine reported segment profit or loss and effect thereof.
• The nature and effect of asymmetrical allocation to segments.

D. Reconciliation

• Segment revenue with consolidated revenue.

• Segment income before tax, extra-ordinary item with that of the consolidated amount.

• Segment assets with consolidated assets.

• Other significant item of the reported segment with that of the enterprise as a whole.

E. Interim period information

• Revenue from external customers.

• Inter segment revenue.

• A measure of segment profit or loss.

• Total assets for which there has been a material change from the amount disclosed in the last annual report.

• Description of difference from the last annual report in the basis of segmentation or measurement of segment profit or loss.

• A reconciliation of the total reportable segment income to the consolidated income.

Enterprise must disclose the following additional information if it is included in determining segment assets.

• Investments in equity method investees.

• Addition to long-lived assets other than financial instruments.
SFAS 131 also provides the following additional information as “enterprise-wide disclosure” to help the users of financial statements better understanding about the risks of the company:

A. If the reportable segment are identified on the basis of something other than products and services then the enterprises should have to report the revenue earned from external customers for each product or services, if possible.

B. Each operating segments that has not been identified on the basis of geographic location, the enterprise shall disclose the following information for each geographic segment if possible:
   - Revenue from external customers.
   - Information about long-lived assets and expenditure during the period.

C. If 10% or more of the revenues of an enterprise is earned from a single customer, then the enterprise shall disclose the total amount of revenue from each such customer and the identity of the operating segment or segments that earn such revenues.

3.7.2 IAS 14R: Segment Reporting

The international standard on the segment reporting is IAS 14 Reporting Financial Information by Segment published by the IASC in August 1981. Subsequently this standard was revised and this revised standard comes into effect on 1st July 1998. It provides new approach to determine reportable segment. Those approaches are:

1) Risk-Return Approach

In this approach, the segments are defined on the basis of dominant source of risks faced by and the return flowing to the enterprise.
2) Management Approach

Under this approach, segments are defined on the basis of the enterprise’s organizational structure and internal financial reporting system.

To implement the new approach revised IAS 14R distinguish between

1. Industry and geographical segments.
2. Reportable segments.
3. Primary and secondary segments.

As per IAS 14R geographical segment to be based on either

a. Location of its production or services facilities and other assets, or,
b. The destination of its goods or services that means location of its customers and markets.

Management approach should have to be considered to determine whether its geographical segment should be based on location of production or the destination of sales. After identification of businesses and geographical segments the management has to decide whether these segments are reportable segment or not. A reportable segment is that segment which fulfills the following tests:

a. Revenue test

Segment revenue is at least 10% of the total revenue (external and internal of all segments).

b. Profit or loss test

The absolute amount of segments operating profit or loss is at least 10% of the greater in absolute amount of

i. Total profit of all segments reporting profit.
ii. Total losses of all segments reporting losses.

c. Assets test

Segment assets are at least 10% of the total assets of all segments.

d. 75% test

The total external revenues of all reportable segments must be at least 75% of the total external revenue of all segments. If this 75% criteria is not fulfilled then another segment has to be considered as a reportable segment on the basis of management decision although those do not fulfill the 10% criteria.

The primary and secondary segments are determined on the basis of dominant source and nature of an enterprise’s risk and return.

An enterprise’s primary segments are business segments when their risks and returns are affected by the products and services. In the contrary, the enterprise’s primary segments are geographical segments if its risk and return are affected predominantly by its geographical area in which it operates. When the exact predominant source and nature of an enterprise’s risk and return cannot be determined, then it should use business segments as primary segments and geographical segments as secondary segments. The IAS 14R encourages segmental cash flow disclosure although it is not mandatory. Detail segment disclosures are required for the primary segments and less detail disclosures are required for secondary segments. The disclosures requirements of IAS 14R are given below:

A. Disclosures for each primary segments:

- Sales or other operating revenues.
- Sales to external customers.
- Revenues from transaction with other segments.
The Accounting Standard Board of ICAI has issued AS 17 for Segment reporting. This standard comes into effect in respect of accounting period which commences on or after 1st April, 2001 and it is mandatory in nature in the following cases:

- Enterprises whose equity or debt securities are listed on a recognized stock exchange in India.
- Enterprises those are in process of issuing equity or debt securities that will be listed on a recognized stock exchange in India as evidenced by the board of the director’s resolutions in this regard.
• All other commercial, industrial and business reporting enterprises whose turnover for the accounting period exceeds ₹ 50 crores.

• Banks including co-operative banks.

• Financial institutions.

• Enterprises carrying on insurance business.

Definitions

Segment reporting refers to the disaggregation of accounting information on the basis of products or services of an enterprise and on the basis of geographical area in which the enterprises operates. In other words while consolidated financial statement provide an economic summary, segment report reflects the disintegrated financial information for each economically viable segments to permit a better understanding of the firm’s sources of profitability and growth. The terms which have been defined in this standard briefly mentioned below:

Business segment

It is a distinguished component of an enterprise which is engaged in producing individual product or services. It is subject to risk and return that are different from those of other business segments. The following factors should be considered in determining whether products or services are related:

a) The nature of the product or services.

b) Nature of the production process.

c) The kind or class of customers of the product or services.

d) Modes used in distributing products or in providing the services.
e) Nature of any regulatory environment like banking, insurances, or public utilities.

**Geographical segment**

A geographical segment is a distinguishable component of an undertaking which is engaged in providing products or services within a certain economic environment and which is subject to risks and returns which are separate from those units operating in other economic environment. It may be identified by considering the following factors:

a) Similarity of political and economic conditions.

b) Relationship among operations in various geographical parts.

c) Proximity of operation.

d) Risks specially concerned with operations in a particular area.

e) Exchange control rules and regulation.

f) The associated currency risks involved.

**Enterprise Revenue**

It refers to the sales revenue earned from the external customers as reported in the profit or loss account or income statement.

**Segment Revenue**

It is the aggregate of i) revenue resulting from the operating activities of a segment ii) relevant portion of enterprise’s revenue that can be allocated on a reasonable basis to the segment and iii) revenue relating to transactions with other segment of the same enterprise.
**Segment Expenses**

It is the aggregate of i) expenses for the operating activities of a segment ii) relevant portion of enterprise’s expenses that can be allocated on a reasonable basis to the segment and iii) expenses relating to transactions with other segment of the same enterprise.

Segment expenses do not include any extraordinary items, interest, loss on sales of investment, income tax or any general administration expenses at enterprise level and related to the enterprise as a whole not for any specific segment. However, expenses incurred at the enterprise level on behalf of a segment should be include in the segment expenses, if such expenses relates to the operating activities of the segment.

**Segment Result**

It refers to the difference between segment revenues and segment expenses.

**Segment Assets**

Those are operating assets used by the segment in its operating activities and those are directly attributable to the segment or allocated to the segment on a reasonable basis. It does not include income tax assets or any assets used for the head office purpose.

**Segment Liabilities**

Those are operating liabilities that result from the operating activities of a segment and those are directly attributable to the segment or allocated to the segment on a reasonable basis. It does not include income tax liability or any liability that has been incurred for financing.
Segment Accounting Policies

The accounting policies adopted for preparing the financial statements of the entity as well as those accounting policy which relates specifically to segment reporting. Assets or liabilities that related jointly to more segments should be allocated to segments if their revenues and expenses are allocated to those segments.

Reconciliation Statement

An enterprise should prepare and present a reconciliation statement in which segment revenue should be reconciled to enterprise income, segment assets should be reconciled to enterprise assets and segment liabilities should be reconcile to enterprise liabilities.

Reportable Segment

A business segment or geographical segment should be identified as a reportable segment if:

- Its revenue is 10% or more of the total revenue of all segments.
- Its result is 10% or more of the greater in an absolute amount of:
  a) The combined profits of all segments.
  b) The combined losses of all segments.
- Its assets are 10% or more of the total assets of all segments.

If total external revenue attributable to reportable segment constitutes less than 75% of the total enterprise’s revenue, additional segment should identified as a reportable segment even if the above condition is not meet until at least 75% of the total enterprise’s revenue.

Disclosures

According to this standard, reportable segments are classified as primary and secondary on the basis of dominant source and nature of risk and return of the
enterprise. The extent of disclosures is being lowered for secondary segments than that for the primary segment. Disclosures requirement for primary segment and secondary segment are given bellow:

**i) Disclosures requirement for each primary segment**

- Segment revenue with a break-up of sales to external customers and from transaction with other segment.
- Segment result.
- Total carrying amount of segment assets.
- Total amount of non-cash expenses such as provision and unrealized foreign exchange gains and losses that were included in segment expenses and therefore deducted in measuring segment result.
- Total amount of segment liabilities.
- The total amount of depreciation and amortization in respect of segment assets for the period should be disclosed.
- Total cost incurred during the period to acquire segment fixed assets (tangible and intangible).
- An enterprise should present a reconciliation statement between the information disclosed for reportable segment and the aggregated information in the enterprises financial statement.
- Inter segment transfer should be measured on the same basis that the enterprise actually used to price those transfers. The basis of inter segment transfer pricing and change therein should be disclosed in the financial statements.
• Change in accounting policies adopted for segment reporting those have a material effect on segment information should be disclosed.

• An enterprise should indicate the type of products and services included in each reported business segment and indicate the composition of each reported geographical segment, both primary and secondary.

ii) Disclosures required for each secondary segment

If an enterprise’s primary segment is business segment, it should also report the following information:

• Segment revenue from external customers by geographical area based on the geographical location of its customers whose revenue from sales is 10% or more of enterprise revenue.

• Total carrying amount of segment assets for each geographical segment (which are 10% or more of the total assets to all geographical segments).

• The total cost incurred during the period to acquire segment assets for each geographical segment whose segment assets are 10% or more of the total assets of all geographical segments.

If an enterprise’s primary segment is geographical segment, it should also disclose the following information:

• Segment revenue from sales to the external customers by business segments.

• The total carrying amount of segment assets of business segments.
• Total cost incurred during the period to acquirer any fixed assets (both tangible and intangible) by business segments.

3.7.4 Comparison between SFAS 131 and IAS 14R

An analysis of these two major standards on segment reporting reveals that they are similar in many respects. Both SFAS 131 and IAS 14R are applicable only to listed enterprises. Both are allowed operating segments to be combined for reporting purpose even though they may individually be material, if certain aggregation criteria are fulfilled. Under both standards reportable segments are identified on the basis of company’s organization structure and internal reporting system. Both are required to provide more disclosure about primary segment than that of secondary segment. In addition, the information required for the primary and secondary segments are basically the same.

However, there are some prime differences. The important dissimilarities between SFAS 131 and IAS 14R are given bellow:

Table 3.2: Dissimilarities between SFAS 131 and IAS 14R

<table>
<thead>
<tr>
<th>SFAS 131</th>
<th>IAS 14R</th>
</tr>
</thead>
<tbody>
<tr>
<td>It allows mixed segmentation.</td>
<td>An enterprise should use either business segment or geographical segment as its primary segment.</td>
</tr>
<tr>
<td>It allows departure from GAAP when management receives and analyses segment information in a way that is not consistent with GAAP.</td>
<td>Segment report should be prepared using the same accounting policies as the consolidated accounts.</td>
</tr>
<tr>
<td>Under this standard reportable segments are determined by employing the management approach.</td>
<td>Under this standard reportable segments are identified on the basis of the dominant source and nature of the enterprise’s risk and return.</td>
</tr>
<tr>
<td>It allows flexibility.</td>
<td>It requires a standardized measure of segment result.</td>
</tr>
<tr>
<td>-----------------------</td>
<td>------------------------------------------------------</td>
</tr>
<tr>
<td>Disclosure of segment liabilities is not required.</td>
<td>Disclosure of segment liabilities is required.</td>
</tr>
<tr>
<td>If the number of reportable segment increases above 10, the enterprise should consider whether a practical limit has been reached for making disclosures.</td>
<td>It does not contain any such provisions.</td>
</tr>
<tr>
<td>It does not encourage disclosure of segment cash flow, but requires disclosure of significant non-cash expenses.</td>
<td>It encourages disclosure of segment cash flow, although it has not made such disclosure mandatory.</td>
</tr>
</tbody>
</table>

3.7.5 Comparison between IAS 14R and AS 17

An analysis of the two major standards on segment reporting the IAS 14R and AS 17 reveals that they are similar in many respects. Under both the standard a segment is a distinguishable component that is subject to risks and return that are different from those of other segments. Under IAS 14R and AS 17, segment information should be prepared in conformity with the accounting policies adopted for preparing and presenting financial statements of the enterprise as a whole. Thus, AS 17 is in line with IAS 14R in respect of identification of segments, determination of reportable segments and presentation of segment information in the financial statement. In addition, the information which is required for the ‘primary segment’ and ‘secondary segment’ is basically the same.

However, there are some important differences between IAS 14R and AS 17. The prime dissimilarities between IAS 14R and AS 17 are given below.
**Table 3.3: Dissimilarities between IAS 14R and AS 17**

<table>
<thead>
<tr>
<th>IAS 14R</th>
<th>AS 17</th>
</tr>
</thead>
<tbody>
<tr>
<td>It applies only to listed enterprises.</td>
<td>It applies to listed enterprises as well as unlisted enterprises with an annual turnover exceeding ₹ 50 crores.</td>
</tr>
<tr>
<td>Under this standard segments are allowed to combine for reporting purpose even though they may individually be material, if certain aggregation criteria are fulfilled.</td>
<td>According to this standard, aggregation of reportable segments is not permitted.</td>
</tr>
<tr>
<td>It prescribes treatment of revenues, expenses, profit or loss, assets and liabilities in relation to associates and joint ventures in consolidated financial statements.</td>
<td>It is silent on the aspect of such treatment in consolidated financial statements.</td>
</tr>
<tr>
<td>It encourages reporting of vertically integrated activities as separate segments but does not mandatory.</td>
<td>It does not make any distinction between vertically segment and other segments.</td>
</tr>
<tr>
<td>It provides that a business segment can be treated as reportable segment only if, majority of its revenue is earned from external customers.</td>
<td>It does not contain any such stipulation.</td>
</tr>
<tr>
<td>Under this standard, if a reportable segment ceases to meet threshold requirements, then also it remains reportable for one year if the management judges the segments to be of continuing significance.</td>
<td>Under this standard, this is mandatory irrespective of the judgment of management.</td>
</tr>
<tr>
<td>In case of change in identification of segments, IAS 14 requires restatement of prior period segment information. Thus, it requires disclosure of data for both the old and new bases of segmentation.</td>
<td>It requires only disclosure of the nature of the change and the financial effect of the change, if it is reasonably determined.</td>
</tr>
</tbody>
</table>
3.8 CONVERGENCE OF ACCOUNTING STANDARDS ON SEGMENT REPORTING

The rapid globalization of capital market, explosive growth of cross border transactions, cross-border security listing and the growth of large multi-national companies have threatened the users of accounts particularly for assessing the financial performance and position of the reporting entity. Because, almost all countries have their own distinct set of accounting standards for the financial reporting with different requirements which leads to diversity in reporting. This diversity in reporting requirements mainly generate from the distinct socio-economic environment of the country. In this sphere of diversity, one recent past development is the global convergence in accounting standards for developing a single set of quality full worldwide recognized accounting standards.

In this age of convergence, the International Accounting Standard Board (IASB) has issued a number of new International Financial Reporting Standards (IFRSs) to replace some International Accounting Standards (IASs) as part of its ‘Convergence Project’. To achieve the objectives of convergence of accounting standards throughout the world, the IASB has undertaken a joint short-term convergence project with the United States’ Financial Accounting Standard Board (FASB). One aspect of this project involves adopting high quality financial reporting solutions by considering two boards’ (i.e. IASB and FASB) recent standards. The comparisons of standards (i.e. IAS 14R and SFAS 131) set out requirements for the disclosure of information about an entity’s operating segments, resulted in the issuance of IFRS 8 ‘Operating Segments’ by IASB on 30th November, 2006. IFRS 8 replaces IAS 14R and aligns segment reporting with the requirements of SFAS 131. The IFRS 8 ‘Operating Segments’ states the enterprise prepare its segment report on
the basis of operating segment which is determined by the managerial approach (i.e. key decision maker); by which enterprise can minimize the cost of segment reporting as it has produced previously for decision making purpose. The prime change from the current standards is the introduction of management approach. With this new approach IASB claimed that, information through the eye of management will allow users to better assess an entity’s operations. In this regard users of segment information are sharply divided into two field of opinion. Some believe that the new standard will lead to low quality segment reporting; on the other side others think that it is the only way to improve the segment information. In this backdrop, the present part of this chapter makes an endeavor to make a critical evaluation of this converged accounting standard IFRS 8.

3.8.1 IFRS 8: Operating Segments

IFRS 8 ‘Operating Segments’ applies only to listed companies. It replaces IAS 14R and is effective from periods beginning on or after 1st January, 2009. Operating segments are identified on the basis of internal reports. Internal report is a report which is used by the entity’s chief operating decision maker to allocate resources to the segment and assess its performance. This is because IFRS 8 requires the information which is used by the management to make decision about operating matters. The IASB believes that this management approach will help to improve financial reporting by allowing users of financial statements to review the operation through the eye of management. There is little cost of preparation as the information is already used internally by management and the information is available on a timely basis.
Core principle

An entity should disclose information in such a way that should enable the users of financial statements to evaluate the nature and financial effects of the types of operation in which it engages and the surrounding economic environment. This principle is consistent with the objective of financial reporting discussed in the IASB’s Framework for the preparation and presentation of financial statements.

Scope

IFRS 8 applies to the separate or individual financial statements of an entity and the consolidated financial statements of a group with a parent whose debt or equity instruments are traded in a public market or is in the process of filing, its consolidated financial statements with a regular organization for the purpose of issuing class of instruments in a public market.

However, when both separate and consolidated financial statements of the parent are presented in a single report, segment information need be presented only on the basis of the consolidated financial statements.

Operating segments

An operating segment is a component of an entity that engages in business activities from which it may earn revenues and incur expenses; whose operating results are reviewed regularly by the entity’s chief operating decision maker to make decision about its resource to be allocated to the segment and assess its performance and for which discrete financial information is available.

All operations of an entity will not necessarily be treated as operating segment. Some functional department may not earn or may earn revenues that are only incidental to the activities of the entity. These would not be operating segments. An entity’s post-retirement benefit plans is not the part of operating segments.
**Quantitative thresholds and aggregation**

Segment information is required to be disclosed about any operating segment which meets any of the following thresholds:

- Its revenue, from both external customers and inter-segment transfers is 10% or more of the combined revenue, internal and external of all operating segments.
- The absolute amount of its profit or loss is 10% or more of the greater, in absolute amount of
  a) The combined reported profit of all operating segments.
  b) The combined reported loss of all operating segments.
- Its assets are 10% or more of the combined assets of all operating segments.

If the total external revenue reported by operating segments constitutes less than 75% of the entity’s revenue, additional operating segments must be identified as a reportable segment even if they do not meet the quantitative thresholds.

**Disclosures**

An entity should disclose information about its operating segments to enable users of financial report to evaluate the nature and financial effects of the business activities and the economic environment in which it operates. The disclosure requirement of IFRS 8 are given below:

**A. General information**

- Factor used to identify reportable segments.
- Types of products and services those are reportable segment provide.

**B. Information about profit or loss and assets**

- Revenue from external customers.
Revenue from inter segment transfer.

Interest revenue and expenses.

Depreciation, depletion and amortization expenses.

Income tax expenses and benefit.

Material items of income and expenses.

The entities interest in the profit or loss of associates and joint ventures accounted for by the equity method.

Other significant non-cash items.

C. Basis of measurement

The amount of each item shall be measured on the same basis which is used for reporting to the chief operating decision maker.

Adjustment, elimination and allocation shall be made if they are included in the chief operating decision maker report.

Assets also are reported on the same basis which is followed to prepare the chief operating decision maker report.

If the chief operating decision maker uses more than one method to determine the segment profit or loss and assets then reported method should be consistent with the corresponding amounts in the entity’s financial statements.

However, entity shall also disclose the following general measurement basis

Basis of accounting for inter segment transaction.

Nature of difference between the measurement of profit or loss of reportable segments and enterprise as a whole.
• The nature of any difference between the measurement of segment assets and consolidated assets.

• The nature of the change from prior periods in the measurement methods used to determine reported segment profit or loss and effect thereof.

• The nature and effect of asymmetrical allocation of segments.

D. Reconciliation

• Segmental revenue with consolidated revenue.

• Segmental income before tax, extraordinary items with that of the consolidated amount.

• Segment assets with consolidated assets.

• Other material items of the reported segment with that of the enterprise as a whole.

In addition, there are some prescribed entity wise disclosures that are required even when an entity has only one reportable segment. Analysis of revenue and certain non-current assets by geographical area are required if material, irrespective of the identification of operating segments. If the information necessary for this analysis is not available and the cost for development would be excessive, that fact must be disclosed. To disclose the information about transaction with major customers, need not disclose the identity of a major customer, nor the amount of revenues that each segment reports from that customer.
3.8.2 Comparison between SFAS 131 and IFRS 8

Except for some terminology and some minor differences SFAS 131 and IFRS 8 are similar in many respects but there are some minor differences which are given below:

Table 3.4: Dissimilarities between SFAS 131 and IFRS 8

<table>
<thead>
<tr>
<th>SFAS 131</th>
<th>IFRS 8</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under this standard, ‘long-lived’ assets refer to hard assets that cannot be readily removed, which does not include intangible assets. So there is no explicit requirement to disclose intangible assets.</td>
<td>Under this standard, non-current assets include intangible assets; therefore they are require to be disclosed if regularly considered by the chief operating decision maker.</td>
</tr>
<tr>
<td>No requirement to disclose the segment liabilities.</td>
<td>Segment liabilities should be disclosed if only chief operating decision maker use it for their reporting purpose.</td>
</tr>
<tr>
<td>Segments are determined on the basis of products and services.</td>
<td>The operating segments are determined based on the core principle of IFRS 8</td>
</tr>
<tr>
<td>Extraordinary items are required to be disclosed, if it regularly consider by the chief operating decision maker for their decision making purpose.</td>
<td>The concept of extraordinary items was eliminated from IFRSs in 2003.</td>
</tr>
</tbody>
</table>

3.8.3 Comparison between AS 17 and IFRS 8

Upon adoption of IFRS 8, the identification of an entity segments may or may not change depending on how the entity has applied AS 17 in the past. If under the AS 17 an entity identified its primary segment on the basis of the report provided to the person whom IFRS 8 regards as the chief operating decision makers, those might become the operating segment for the purpose of IFRS 8. Segment liabilities under AS 17 are disclosed mandatorily but it should be disclosed under IFRS 8 if it is
considered by chief operating decision maker in their internal report. So generally both the standards require disclosure about the segmental liabilities. Although, there are some important differences between AS 17 and IFRS 8 which are given below:

**Table 3.5: Dissimilarities between AS 17 and IFRS 8**

<table>
<thead>
<tr>
<th>AS 17</th>
<th>IFRS 8</th>
</tr>
</thead>
<tbody>
<tr>
<td>This standard comes into effect in respect of the accounting period commencing on or after 1st April, 2001.</td>
<td>This standard comes into effect in respect of accounting period commencing on or after 1st January, 2009.</td>
</tr>
<tr>
<td>It applies to listed enterprises as well as unlisted enterprises with an annual turnover exceeding ₹50 crore.</td>
<td>It applies only to listed enterprise or to the enterprise which is going to be listed.</td>
</tr>
<tr>
<td>Under this standard an enterprise identify two sets of segments using a risk and rewards approach with the enterprise’s system of internal financial reporting to key management personnel.</td>
<td>Operating segments are identified based on the financial information that is evaluated regularly by the chief operating decision maker in deciding to allocate resources and in assessing performance.</td>
</tr>
<tr>
<td>Segment information is prepared in conformity with the accounting policies adopted for preparing and presenting the financial statements for the enterprises as a whole.</td>
<td>Segment profit or loss is reported on the same measurement basis as that used by the chief operating decision maker.</td>
</tr>
<tr>
<td>Under this standard segment revenue, segment expenses, segment result, segment assets and segment liabilities have been defined.</td>
<td>Under this standard segment revenues, segment expenses, segment result, segment assets and segment liabilities have not been defined.</td>
</tr>
<tr>
<td>Reconciliation is required between the information disclosed for reportable segment and for the aggregated information in the enterprise’s financial statements.</td>
<td>This standard requires reconciliation of segment performance measures and segment assets and liabilities with the corresponding amounts reported in the financial statements.</td>
</tr>
</tbody>
</table>
Disclosures are required based on the classification of segments as primary or secondary. Disclosure requirement for secondary reporting format are less detailed than those required for the primary reporting format.

Requires disclosures of i) external revenues from each product or services ii) revenues from customers in the country of domicile and from foreign country iii) geographical information on non-current assets located in the country of domicile and foreign countries.

### 3.8.4 Critical Evaluation of IFRS 8

This standard requires to report financial and descriptive information about its reportable segments. It extends the scope of segment reporting by including entities whose equities or debt securities are publicly traded and entities that are in process of issuing the securities in public securities markets. It requires the information about components of the entity that management used to make decisions about operating matters and assesses its performance. The reconciliation of total reportable segment revenue, total profit or loss, total assets and other amounts disclosed for reportable segments to corresponding amounts in the entities’ financial statements have to be disclosed. An explanation of how segment profit or loss and segment assets are measure is to be mentioned in the financial statements for each reportable segment. The entity have to report information about its major customers and about the countries in which it earns revenue and holds assets, regardless of whether that information is used by management in operating decision making. Finally, it also requires the descriptive information about the way by which operating segments are determined.

Adoption of IFRS 8 may or may not change the identification of an entity’s segments. IFRS 8 requires operating segments to be identified on the basis of internal
reports that are regularly reviewed by the chief operating decision maker. IAS 14R required an entity to identify two sets of segments using a risks and rewards approach with the entity’s system of internal financial reporting to key management personnel. One set of segments was regarded as primary and other as secondary. If under IAS 14R an entity identified its primary segments on the basis of reports provided to the person whom IFRS 8 regards as the chief operating decision maker (CODM), those might become the operating segments for the purpose of IFRS 8.

Under IFRS 8, for the purpose of identifying reportable segments, no distinction is made between revenues and expenses relating to transactions with third party and revenue and expenses relating to transaction with other segments of the entity. This indicates that vertically integrated operations may be composed of several segments for the purpose of IFRS 8. But under IAS 14R, a business segment or geographical segment treated as a reportable segment only if a majority of revenue is earned from sales to the external customers. This important difference leads to increase the number of reportable segments under IFRS 8.

IFRS 8 requires the amounts reported to the chief operating decision maker for the purpose of allocating resources and assessing its performance are to be disclosed for each reportable segments, even if this transaction is not prepared in accordance with the IFRS accounting policies. This may result in difference between the amount reported in segment report and those reported in the entity’s primary financial statement. But in contrast, IAS 14R requires segment information to be prepared in conformity with the accounting policies adopted for the preparation and presentation of the consolidated financial statements.

Unlike IAS 14R, IFRS 8 does not define terms such as “segments revenue”, “segment profit or loss”, “segment assets” and “segment liabilities”. As a result,
entities will have more discretion in determining what is included in segment profit or loss under IFRS 8, limited only by their internal reporting practices. This also leads to diversify in reporting practices among the various entities.

Under IFRS 8, an entity must disclose an explanation of how it determines its reportable operating segments and the basis on which the disclosed amounts has been measured. But under IAS 14R these disclosures are not required to be disclosed.

Disclosures are required when an entity receives more than 10% of its revenue from a single customer. In this regard, the entity must disclose total amount of revenues earned from each of such customer and name of the operating segments that reports the revenue. This is not required by IAS 14R.

Even if an entity has only one reportable segment, IFRS 8 requires to disclose about the entity’s products and services, geographical areas and major customers. IAS 14R does not include this requirement.

Changes may took place in the reporting for replacing the IAS 14R by IFRS 8:

- Extends the scope of segment reporting.
- Requires identification of operating segments based on internal report.
- Includes a segment of an entity that sales primarily to other operating segments of the entity in the definition of operating segment if the entity is managed that way.
- Requires an explanation of how segment profit or loss and segment assets are measured.
- Requires the information about the production or services and the countries in which it earns revenue and holds assets.
• Requires the information about the major customers, regardless of whether that information is used by management in their operating decision making report.

• Requires an entity to give descriptive information about the way that operating segments are determined and difference between the measurements used in reporting segment information and those used in the entity’s consolidated financial statements.

Several arguments against the management approach have been put forward. An endeavor is now being made to examine such major criticisms. IFRS 8 introduces the management approach to segment reporting for disclosures of the measures used to manage the business entity. This approach is unfamiliar to many companies and managers will have to think carefully about the implication of the existing management structure. Due to this management discretion the comparability of information across entities will be lost. But comparability is one of the principal quality of the financial statement that is very rightly set out in the FASB’s Framework. It does not define measurement of segment revenue, expenses, result, assets and liabilities. That’s why the management can measure the various segment disclosures in his/her own way which may not be consistent enough. There is less direct focus on products; geographic factors which are most useful segment information for investors, unless they are used for internal reporting. Finally, this is the great cause of diversity in reporting.

The information available internally in companies is often more informative than the information reported in financial reports. So if segment reporting is based on the internal reporting practice then it leads to high competitive disadvantages. It will be harder to justify the needs of segmented disclosures particularly for the entities
those are claimed to operate in one segment. When entities use their own measures in their segment report, that might be hard to understand and it leads to deprive overall quality of the information.

A risk under the management approach is that, companies may continue to misuse the aggregation criteria to give less detailed segment information. But optimum amount of information is urgent to analysis and to take a decision over the financial performance or position. If so many items are required to reach the optimum quantum of information, entity will aggregate segments in order to disclose less valuable information. This holds particularly for the profitable segment of the companies.

An endeavor will now be made to examine the validity of major criticisms against the management approach. The IFRS 8’s disclosures focuses on the information that management believe is important and should therefore provide more meaningful segment reporting. The standard has not specified any defined measure of profit and loss but allowed the use of non-IFRS compliant data, if this is used in internal reports; this would lead to less comparative disadvantages. It supports the global harmonization so that entities do not have to prepare more than one set of accounts for different regulations. The analytical value of segment information is greater if it is consistent with actual management of the entity. Segment disclosure following the management approach in annual reports does not result in significant extra efforts, time and cost as it is already used in the interim reports. The observation of segment information through the eye of management will be useful to investors, creditors and other users of financial statements, as it will highlight the risk and opportunity measures in timely basis. The management approach provides an additional insight about the company to the financial statements users. However, it

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hampers the comparability criteria of financial statements among the entities but insists the unique and creative reporting, that’s why this might be given less significance.

The IASB believes that adoption of the management approach will improve financial reporting. First, it allows users of financial statements to review the operation through the eye of management. Secondly, as the information is already used internally by management, there are few costs for preparers and the information is available on a timely basis. This means that the interim reporting of segment information might be extended beyond the current requirements. Finally, according to the chairman of IASB Sir David Tweedie “…. It therefore, gives users of financial statements the opportunity to query how the entity is controlled by its senior decision maker. It does this by enabling entities to provide timely segment information at little extra cost…. ”

Generally accepted principles allow management wide latitude in the choice of accounting policies. Given adopted accounting principles, management faces discretionary accounting decisions, which are heavily oriented to a judgment process of determining amounts, rates and timing. This situation enables management to influence the figures disclosed. Discretion in particular is recognized in the translation of the management accounts (internal report) to the financial accounts (annual reports). In this backdrop and in the age of convergence, the introduction of IFRS 8 has been well accepted by many countries for getting advantages such as cost of capital, saving in cost of preparation of financial statements and increasing opportunities for investors or analyst. Generally in our country the apex standard setting body ICAI tries to converge its existing set of standards with corresponding international standards to the maximum extent possible. Moreover, with a view to
promoting greater convergence, the ICAI has revised many of its early standards with the objectives of bringing them at par with the IASB requirements. Most of the countries throughout the world have realized that converging their domestic standards with IFRS is a necessary step towards development of global capital market.

3.9 EVALUATION OF THE ROLE OF PREVAILING ACCOUNTING STANDARDS IN SEGMENT REPORTING PRACTICES

In this part, researcher has made an endeavor to reflect some practical problems in segment reporting and also to examine the validity of the prevailing accounting standards on segment reporting to resolve the practical problems associated with the segment reporting in term of comparability and consistency.

The main objective of segment reporting is to provide segment-wise financial information like Segment Revenue, Segment expenses, segment result, segment assets, segment liabilities etc. to stakeholders to enable them to take more informed judgment about any segment of the reporting entity or about the reporting enterprise as a whole. Some problems in the reporting of income for different segments of an enterprise, of course, are related to the allocation of joint costs and the treatment of inter segmental transfer pricing. To measure profitability of segments separately, it is necessary that their net assets are reported segment-wise. There are also difficulties in the measurement of assets segment wise. The important problems are discussed below:

**Arbitrary allocation of joint cost**

Even though it is not difficult to identify the significant reportable segments of an entity by business line or economic environment, it is difficult to report segment wise cost as most of the costs incurred by the enterprise are joint costs in nature. Reliability of the segment profit or loss largely depends on the appropriateness of the
basis of joint cost allocation. This joint cost may allocate on several reasonable basis which leads to diversity and inconsistency in reporting practices. In absence of any standardized method for joint cost allocation; it is possible to opt for suitable cost allocation method to arrive at the desired segment result. So there is a chance of window dressing that means users are not getting the reliable information of the various segments from the financial statement.

**Interchangeable assets**

Generally certain assets are utilized for more than one segment. In such case, it is very difficult to earmark assets employed for a particular segment. As a result profitability of a separate segment cannot be accurately measured. Moreover the proportion of unidentifiable assets may be significant and therefore no relevant result of return on segmental assets can be computed for evaluating comparative performance of various segments.

**Influence of transfer pricing**

Transfer price is the price at which one segment transfers its product or services to another segment within a particular enterprise. There are various methods of transfer pricing like cost plus method, negotiated transfer pricing method, market price method etc. That means the transfer price is varied on the basis of the method which is applied. Hence the segment results may be influenced by the transfer pricing formula. The profit of an efficient segment can be distributed among interconnected segments which is not reliable at all. In this ground it is notable that the Bear Stearns equity research has supported the segmental manager’s misinterpretation about their own segment performance by using transfer pricing mechanism because their incentive depends on their performance.
Now it is desirable that the accounting standard should chalk out a standardized method to resolve such problems as the main objective of accounting standards is to standardize the diverse accounting policies and practices with a view to enhancing the comparability and consistency of financial statements. So the next part will explore the various remarkable accounting standards on segment reporting to highlight how they addressed such problems.

**AS 17: Segment Reporting**

Although it is required to disclose such items for both the reportable segments it should not be useful to the stakeholders as they are not measured accurately. It claims to measure the inter segment transfer on the basis that enterprise is actually used to transfer but is silent about any specific method of transfer pricing. So the segment report may mislead the financial statement users.

**IAS 14R: Segment Reporting**

This standard more clearly explains the basis of determination of reportable segment but it also allows the same technique to measure such problematic items. So it is also not free from bias.

**SFAS 131: Disclosures about Segment of an Enterprise and Related Information**

This standard claims to disclose the basis of the determination of reportable segments and the method of transfer pricing but it is silent about any specific method of transfer pricing or any specific method of distribution of joint costs or assets among reportable segments. So it should be able to reflect the effects of transfer pricing mechanism to some extent but totally fails to ascertain segment asset, expenses and revenue accurately.
IFRS 8: Operating Segments

This standard claims to use the same method of transfer pricing and same method for allocation of joint assets or expenses which is followed to prepare the chief operating decision makers’ report. That means it gives the weight to the managements’ discretion but not any specific method. It is also required to disclose the basis of the determination of reportable segments and the method of transfer pricing but it is silent about any specific method of transfer pricing or any specific method of distribution of joint costs or assets among reportable segments. It should be able to capture the effects of transfer pricing mechanism to some extent but totally fails to ascertain segment asset, expenses and revenue uniquely. So it may lead to non-comparable and inconsistent report as sometimes decision makers change their pattern of analysis.

3.10 CONCLUSION

In the age of convergence, almost all accounting standard setting bodies are trying to develop a single set of accounting standards for improving the quality of financial statement but they forget about the basic objective which is to recognize the system of measurement and disclosure rules for preparation and presentation of financial statements. Another main objective of the accounting standard is to standardize the divergent accounting policies and practices. But the prevailing accounting standards on segment reporting do not pave out any specific way of allocation of common cost or assets and are also silent about any specific method of transfer pricing. Almost all the accounting standards are only concerned with the identification of reportable segment and items to be disclosed. Some international standards claim to disclose the method of transfer pricing and some suggest to use the same basis of distribution of joint cost and assets which has been used by internal
decision makers. Very recently developed international accounting standards IFRSs are ‘principle-based’ standards rather than ‘rule-based’ standards which are more reliant upon professional judgment. It allows management wide latitude in the choice of accounting; management faces discretionary accounting decisions which are heavily oriented to a judgment process of determining amounts, rates and timing. This situation enables management to influence the figures to be disclosed. Discretion in particular is recognized in the translation of the management accounts (internal report) to the financial accounts (annual reports). It is unfortunate to note that even after four decades of development of segment reporting, accounting standards failed to standardize the various accounting policies and practices. That means it fails to maintain two basic qualitative characteristics, comparability and consistency of financial statements. Still there is a gap between the expectation of stakeholders from the segment report and content of the segment report which is not desirable to us.