CHAPTER II
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INTRODUCTION

Historically, accounting and reporting grew up independently and often very differently in different countries. Practice, regulation and especially the mode of regulation differed often very greatly in these countries. Accounting, especially appropriate and relevant accounting, is a critical tool and an information source in any country's efforts towards economic growth and development [Kapaya: 2000]. The end product of accounting is financial reporting. Initially, financial reporting was mainly confined to internal reporting. It provided company owners with a vehicle to manage the company. Later on, in the early 1800s, private capital alone was insufficient to finance business activities. Capital was gathered from sources outside the company and the owners delegated the managing function to directors and provided them with the necessary authority to run the business activity. This resulted in the extension of accounting from internal reporting system to external reporting system. Nowadays, the external financial reporting provides a means of reporting the results and accounts to the owners.

THE NOMENCLATURE DEBATE

Regarding the nomenclature issue, focus may be made on four terms viz., 'bookkeeping' 'accounting' 'standards' and 'financial reporting.' In fact, these terms have historical rooting. The earliest term to be used in unfolding a firm's financial performance was 'bookkeeping'. Since the term connoted the recording process only and not reporting, it was discarded long back and the accounting professionals and academicians embraced the term, 'accounting'. The impetus for this change was initiated by AICPA [1953:*para.9*] when it defined accounting in these words: "Accounting is the art of recording, classifying, and summarizing, in a significant manner and in terms of money, transactions and events which are, in part at least, of a financial character, and interpreting the results thereof." The key word in this definition was 'summarizing,' which, in essence, refer to principles underlying the preparation of financial statements. As a result, the accounting profession was in search of principles. One of the major attempts in this direction was made by Grady

[1965], who took an inventory of GAAP. This 'inventory' attempted to pull together the objectives, concepts and principles contained in the then current professional announcements. Focusing on the needs of the users of financial statements, The American Accounting Association [AAA] [1966:*1*] initiated a paradigm shift in the role of accounting by defining it as "…the process of identifying, measuring and communicating economic information to permit informed judgments and decisions by the users of information." However, the usage of the term 'GAAP' was continued without interruption.

Meanwhile, the impetus to use 'standards' emanated from the seminal work of Paton and Littleton under the title "An Introduction to Corporate Accounting standards" in 1940 itself. The rationale to use this term has been tacitly explained by them in these words [p: *4*]: 'The term "standards" is used advisedly. "Principles" would generally suggest a universality and degree of permanence which cannot exist in a human service institution such as accounting. In this monograph, accordingly, the term "principles" is used sparingly and the idea of useful standards is emphasized.' Supporting the observation of Paton and Littleton, we may quote APB [1970]:"Generally Accepted Accounting Principles are conventional – that is, they became generally accepted by agreement (often tacit agreement) rather than by formal derivation from a set of postulates or basic concepts. The principles have developed on the basis of experience, reason, custom, usage, and to a significant extent practical necessity. The serious objection to GAAP has come from Dyckman et. al., [2001:*9*] in these words: "Over the years, the accounting profession has developed a structure of accounting practice standards to address comparability and reporting abuse. The chief body of practice standards is a set of generally accepted accounting principles [GAAP] intended both to guide and to govern the preparation of financial statements with the public's needs and interest foremost in mind. The description *generally accepted* means that each principle either was established by a designated rule-making body, such as the Financial Accounting Standards Board, or has achieved general acceptance though practice."

It is also important to note that GAAP represent *Generally* (not specifically searched) *Accepted* (not deduced and tested) *Accounting principles* (in fact practices). Hence the usage of the term, 'GAAP,' was discontinued and the term 'accounting standards' emerged. The beginning was made in this direction by promulgating standards through IASC now called IASB, and this term was in circulation till 2000.

Led by IASB, the standard setting bodies pondered over the issue of nomenclature further. The standard setters observed that accounting diversity was no doubt reduced to some extent, but the influence of GAAP still continued resulting in a low level of harmonization. It is also important to note the observations made by Gowda [1993:*68*] on the theoretical validity of accounting standards: "… what is true in accounting standards is not new and what is new, if it is there in accounting standards is not at all true." However, the accounting show has been continued without heeding to this advice with an ad hoc policy of minimizing the number of alternative accounting policy choices.

As a sequel to this development, the IASC was changed as IASB thus increasing the status of authority to a higher level and the Board accepted that IAS be changed IFRS. In tune with change in the name from IASC to IASB, the IASC Foundation changed the nomenclature of standards from IASs to IFRSs. In other words, 'Financial Reporting' was substituted for 'Accounting.' This shift from 'Accounting' to 'Financial Reporting' is not to be construed as a routine event, but it involves the perception of standard setters in understanding the dynamics of accounting as such in the sense that 'Financial Reporting' encompasses a dynamic vision of capturing financial information content in decision making through reporting as against accounting merely pertaining the character of recording. In this regard, we may quote the dictionary meaning of 'report' as a verb documented in Webster's New World College Dictionary under the editorship of Agnes [2005:*1216*] from three angles: "**1** to give an account of, often at regular intervals; give information about (something seen, done etc.)… **6** to present or written (something referred for study, action, etc.) with the conclusions reached or recommendations made… **4a** a formal or official presentation of facts or of the record of some proceedings, an investigation etc…" To put simply, accounting seems to be a static concept but financial reporting is characterized with dynamic understanding and presentation of information for decision making by the users based on the facts backed up by a thorough investigation of the rightness of the reporting process.

ACCOUNTING STANDARDS

Thorell and Whittington [1994] describe accounting as an important language of commerce. Like all languages, its effectiveness as a means of communication is aided by precise definition of words and rules as to its structure. Moreover, users' costs may be reduced, and the value of the data for comparative purposes enhanced, if all companies use the same definitions and rules in their financial reports.

Efforts to achieve this on a national level, by means of company law or the regulatory activities of professional and other bodies are often referred to as standardization, the rules being referred to as accounting standards. Littleton [1953] defines "A standard is an agreed upon criteria of what is proper practice in a given situation; a basis for comparison and judgment; a point of departure when 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. They are not accidental but intentional in origin; they are expected to be expressive of the deliberately chosen policies of the highest types of businessmen and the most experienced accountants; they direct a high but attainable level of performance, without precluding justifiable departures and variations in the procedures employed." Bromwich [1985] observes, "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. Standard setters can be seen as seeking to prescribe a preferred accounting treatment from the available set of methods for treating one or more accounting problems. Other policy statements by the profession will be referred to as recommendations." In the similar line, Harvey and Keer [1981:*9*] explain that a standard in accounting is "a method or an approach to preparing accounts which has been chosen and established by the bodies overseeing the profession." Thus, a standard can be viewed as some form of rule. They further state that "…the word standard is preferred to principle because a standard is pragmatic and it can only do good because it will remove any inhibition about its replacement with a better standard, if this becomes appropriate."

The Canadian Institute of Chartered Accountants has given a broad definition of accounting standards. According to it, "Accounting Standards are solid principles for financial accounting and reporting developed through a structured standard setting body (an Accounting Standard Board). Accounting standards spell out how transactions and other events are to be recognized, measured, presented and disclosed in financial statements. The purpose of such standards is to meet the needs of users of financial statements by providing the information considered necessary to make informed decisions." Van der Tas [1988:*157*] define standards as any financial reporting rule published by either the government or a private standard setting body. These rules can refer either to the degree of disclosure or to the accounting method to be applied.

Accounting standards can be described as a vehicle whereby 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 as a “language of business” communicates the financial results and health of an enterprise to various interested parties by means of periodical financial statements. Like any other language, accounting should have its grammar (set of rules) and this grammar is said to be encoded in accounting standards.

In an effort to generate comparable and reliable accounting information to help investors, creditors and others, each country has developed its own national financial accounting standards. These standards reflect the culture, history, and the characteristics of accounting problems facing that country. In some countries, the professional bodies formulate the financial accounting standards, while in many others, governments and regulators establish these standards. Nobes [1987: *78*] observes professional accounting standards are also endowed with varying degrees of authority in different countries. A standard can range from one that is legally enforced (e.g., Canada), to one that is usually obeyed and is binding on auditors (e.g. U.K.), to one that is persuasive (e.g. the Netherlands), to one that is unimportant (e.g. domestic pronouncement of the accountancy body in West Germany), to one that is largely unknown to companies or auditors.

Accounting standards are formulated with a view to harmonize different accounting polices and practices in use in a country. The objective of accounting standards is, therefore, to reduce the accounting alternatives in the preparation of financial statements within the bounds of rationality, thereby ensuring comparability of financial statements of different enterprises with a view to provide meaningful information to various users of financial statements to enable them to make informed economic decisions.

INTERNATIONAL ACCOUNTING STANDARDS

The concept of establishing international standards of accounting germinated around the turn of the century when, in 1904, the first International Congress of

Accountants was held in St. Louis. However, the history of international accounting standards really began in 1966, with the proposal to establish an International Study Group comprising the Institute of Chartered Accountants of England & Wales (ICAEW), American Institute of Certified Public Accountants (AICPA) and Canadian Institute of Chartered Accountants (CICA). In February 1967, this resulted in the foundation of the Accountants International Study Group (AISG), which began to publish papers on important topics every few months and created an appetite for change. Many of these papers led the way for the standards that followed. In the meantime, international accounting diversity was one of the topics discussed in the tenth International Congress of Accountants in 1972. Accounting bodies of some countries attending the meeting were concerned in reducing the degree of variation in international accounting practices. As a result, in 1973, the International Accounting Standards Committee (IASC) was formed. The founders of this Committee included ten accounting bodies from Australia, Canada, France, Japan, Mexico, Netherlands, West Germany, the United States, United Kingdom and Ireland.

The objectives of the IASC are: (1) to formulate and publish in the public interest accounting standards to be observed in the presentation of financial statements and to promote their worldwide acceptance and observance; and (2) to work generally for the improvement and harmonization of regulations, accounting standards and procedures relating to the presentation of financial statements. Between 1973 and 2001, the IASC promulgated 41 standards. With the renaming of IASC as IASB, the objectives of the latter also changed. At present, the IASB [2005:*12*]: is charged with the following objectives: (a) to develop, in the public interest, a single set of high quality, understandable and enforceable global accounting standards that require high quality, transparent and comparable information in financial statements and other financial reporting to help participants in the world's capital markets and other users make economic decisions; (b) to promote the use and rigorous application of those standards; and (c) to bring about convergence of national accounting standards and International Accounting Standards and International Financial Reporting Standards to high quality solutions.

To support the effective functioning of the former IASC, the SIC was also constituted in 1997 to assist the former on tackling the contentious accounting issues that needed authoritative guidance to stop widespread variations in accounting practices. In tune with a change in nomenclature from IASC to IASB, the SIC was renamed as International Financial Reporting Interpretations Committee [IFRIC]. In addition, the Standards Advisory Council [SAC] was also established. The present status of international accounting standards are presented under (i) Institutional Structure; and (ii) Progress of IAS/IFRS.

(i) Institutional Structure:

The salient features of institutional structure of establishing Financial Reporting Standards are presented under (a) IASC Foundation; (b) Standard Advisory Council; (c) IFRIC; (d) IASB Due Process; (e) IFRIC Due Process; (f) The Framework: (g) Accounting Standards; (h) New Presentation; and (i) Benchmark and Allowed Alternative Treatments.

(a) IASC Foundation:

The name of the organization to monitor the promulgation and implementation of IFRS is the International Accounting Standards Committee Foundation.

(b) Standard Advisory Council:

The Standards Advisory Council (SAC) provides a formal vehicle for further groups and individuals having diverse geographical and functional backgrounds to give advice to the IASB and, at times, to advise the Trustees. The Trustees attach particular importance to the perspective that the SAC can bring to IASB's role and mandate. At present the SAC comprises about fifty members. It has the objective of (a) giving advice to the IASB on priorities in the IASB's work; (b) informing the IASB of the implications of proposed standards for users and preparers of financial statements; and (c) giving other advice to the IASB or the Trustees. The SAC normally meets at least three times a year. It is to be consulted by the IASB on all major projects and its meetings are open to the public.

(c) IFRIC:

The International Financial Reporting Interpretations Committee (IFRIC) is appointed by the IASC Foundation Trustees to assist the IASB in establishing and improving standards of financial accounting and reporting for the benefit of users, preparers and auditors of financial statements. The Trustees established the IFRIC in March 2002, when it replaced the previous interpretations committee of the Standing Interpretations Committee (SIC). The role of the IFRIC is to provide timely guidance on newly identified financial reporting issues not specifically addressed in the IASB's standards (IFRSs) or issues where unsatisfactory or conflicting interpretations have developed, or seem likely to develop. It thus promotes the rigorous and uniform application of IFRSs. The IFRIC assists the IASB in achieving international convergence of accounting standards by working with similar groups sponsored by national standard-setters to reach similar conclusions on issues where underlying standards are substantially similar.

(d) IASB Due Process:

The IASB has the sole responsibility for setting accounting standards. The selection of IASB members is based on technical expertise and the Trustees of the IASC Foundation exercise their best judgment to ensure that the IASB is not dominated by any particular constituency or regional interest. It consists of fourteen members. Headquartered in London, the IASB is committed to developing, in the public interest, a single set of high quality, global accounting standards that require transparent and comparable information in general purpose financial statements.

The IASB due process is summarized below: (a) the staff are asked to identify and review all the issues associated with the topic and to consider the application of the IASB Framework to the issues; (b) study of national accounting requirements and practice and an exchange of views about the issues with national standard-setters;(c) consulting the SAC about the advisability of adding the topic to the IASBs agenda;(d) formation of an advisory group to give advice go the IASB on the project;(e) publishing for public comment a discussion document;(f) publishing for public comment an exposure draft approved by at least eight members of the IASB, including any dissenting opinions held by IASB members;(g) publishing within an exposure draft a basis for conclusions;(h) consideration of all comments received within the comment period on discussion documents and exposure drafts;(i) consideration of the desirability of holding a public hearing and of the desirability of conducting field tests and, if considered desirable, holding such hearings and conducting such tests;(j) approval of a standard by at least eight members of the IASB and inclusion in the published standard of any dissenting opinions; and (k) publishing within a standard a basis for conclusions, explaining, among other things, the steps in the IASB's due process and how the IASB dealt with public comments on the exposure draft.

(e) IFRIC Due Process:

Interpretations of IFRSs are developed through a formal due process that involves accountants, financial analysts and other users of financial statements, the business community, stock exchanges, regulatory and legal authorities, academics and other interested individuals and organizations from around the world. The IFRIC discusses technical matters in meetings that are open to public observation. The due process for each project normally, but not necessarily, involves the following steps: (a) the staff are asked to identify and review all the issues associated with the topic and to consider the application of the IASB Framework to the issues; (b) study of national accounting requirements and practice and an exchange of views about the issues with national standard-setters, including national committees that have responsibility for interpretations of national standards; (c) publication of a draft Interpretation for public comment if not more than three IFRIC members have voted against the proposal; (d) consideration of all comments received within the comment period on a draft interpretation; (e) approval by the IFRIC of an Interpretation if not more than three IFRIC members have voted against the interpretation after considering public comments on the draft Interpretation, and (f) approval of the Interpretation by at least eight members of the IASB.

(f) The *Framework*:

The IASB has a Framework for the Preparation and Presentation of Financial Statements. The *Framework* assists the IASB: (a) in the development of future IFRSs and it its review of existing IFRSs; and (b) in promoting the harmonization of regulations, accounting standards and procedures relating to the presentation of financial statements by providing a basis for reducing the number of alternative accounting treatments permitted by IFRSs.

In addition, the *Framework* may assist: (a) preparers of financial statements in applying IFRSs and in dealing with topics that have yet to form the subject of a Standard or an Interpretation; (b) auditors in forming an opinion on whether financial statements conform with IFRSs; (c) users of financial statements in interpreting the information contained in financial statements prepared in conformity with IFRSs; and (d) those who are interested in the work of IASB, providing them with information about its approach to the formulation of accounting standards.

The *Framework* is not a part of IFRS. However, when developing an accounting policy in the absence of a standard or an Interpretation that specifically applies to an item, an entity's management is required to refer to, and consider the applicability of, the concepts in the *Framework*. In a limited number of cases there may be a conflict between the *Framework* and a requirement within a standard or an Interpretation. In those cases where there is a conflict, the requirements of the standard or Interpretation prevail over those of the *Framework*.

(g) Accounting Standards:

The IASB publishes its standards in a series of pronouncements called International Financial Reporting Standards (IFRSs). Upon its inception the IASB adopted the body of International Accounting Standards (IASs) issued by its predecessor, the Board of the International Accounting Standards Committee. The term 'International Financial Reporting Standards' includes IFRSs, IFRIC Interpretations, IASs and SIC Interpretations.

(h) New Presentation:

Until now, documents that were originated by IASC have been reprinted in their original typeface, and those developed by the Board have been printed in a different typeface. There were other presentational differences, of which perhaps the most obvious was the use by IASC of bold italic type to denote mandatory requirements, whereas the Board uses **bold roman** type to denote the main principles.

(i) Benchmark and Allowed Alternative Treatments:

In some cases, IASs permit different treatments for given transactions and events. In limited cases, one treatment is identified as the 'benchmark treatment' and the other as the 'allowed alternative treatment.' The financial statements of an entity may appropriately be described as being prepared in accordance with IFRSs whether they use the benchmark treatment or the allowed alternative treatment.

The IASB's objective is to require like transactions and events to be accounted for and reported in like way and unlike transactions and events to be accounted for and reported differently, both within an entity over time and among entities. Consequently, the IASB intends not to permit choices in accounting treatment. Also, the IASB has reconsidered, and will continue to reconsider, those transactions and events for which IASs permit a choice of accounting treatment, with the objective of reducing the number of those choices.

(ii) Progress of IAS/IFRS

The IASC promulgated 41 IAS till its termination in 2001. Meanwhile, the IASB began a program of reviewing major standards with a view to improve the quality of international standards particularly by removing as many options as possible, by improving disclosure, and by providing more implementation guidance so that IASs constituted a rigorous set of standards [Pricewaterhousecoopers: 1998].

International Accounting Standards initially tended to be too broad, allowing many alternative accounting treatments to accommodate country differences. This was a serious weakness in achieving the objective of comparability. To gain acceptability of its standards, the IASC undertook a project (called the Comparability Project) aimed at enhancing comparability of financial statements by reducing the alternative treatments in 1989. An important part of this effort was its work plan to produce a comprehensive core set of high-quality standards (Core Standards project).

The IASC also persuaded the stock exchange institutions, particularly IOSCO and its member the Securities and Exchange Commission (SEC), to accept financial statements prepared in accordance with IASs for multinational registration. This effort became successful in 1993 when IOSCO announced that it would recognize IAS 7 and in the following years' announcement, as it would accept 14 IASB standards as they were. Finally, IOSCO recommended acceptance of the use of IAS by its members in May 2000. In June 2000, the European Commission proposed that all listed companies in the EU should be required to prepare their consolidated financial statements using IAS.

Taking into consideration the efforts of IASC and acceptance of 41 IAS by the IASB, it may be construed that the latter has so far issued 47 Exposure Drafts and has come out with 41 IASs. Further, the IASB has issued 7 IFRSs and also guidelines titled "Framework for the Preparation and Presentation of Financial Statements". Sometimes a standard is withdrawn and new standard on the same topic is issued if it becomes necessary. The list of IASs issued by IASB including those of IASC is shown in Table 2.1. At present, the IASB has recognized 41 IAS as its own standards with the old nomenclature being International Accounting Standards [IAS] and they are to be considered as IFRS *per se* and further it has recognized 11 Standing Interpretations [SIC] of IASC as its own interpretations. Since 2001, IASB has promulgated 7 IFRS and accepted 5 IFRIC.

TABLE 2.1
CURRENT INTERNATIONAL FINANCIAL REPORTING STANDARDS (IAS/IFRS) AND INTERPRETATIONS (SIC/IFRIC)

IAS	TITLE
IAS 1	Presentation of Financial Statement (R)
IAS 2	Inventories
IAS 7	Cash Flow Statements
IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors
IAS 10	Events After the Balance Sheet Date
IAS 11	Construction Contracts
IAS 12	Accounting for Taxes on Income
IAS 14	Reporting Financial Information by Segment
IAS 16	Property, Plant, and Equipment
IAS 17	Accounting for Leases
IAS 18	Revenue
IAS 19	Employee Benefits (R)
IAS 20	Accounting for Government Grants and Disclosure of Government Assistance
IAS 21	The Effects of Changes in Foreign Exchange Rates
IAS 23	Borrowing Costs
IAS 24	Related-Party Disclosures
IAS 26	Accounting and Reporting by Retirement Benefit Plans
IAS 27	Consolidated and Separate Financial Statements (R)
IAS 28	Accounting for Investments in Association
IAS 29	Financial Reporting in Hyperinflationary Economies
IAS 30	Disclosures in the Financial Statement so Banks and Similar Financial Institutions (Superseded by IFRS 7 beginning in 2007)
IAS 31	Financial Reporting of Interests in Joint Ventures
IAS 32	Financial Instruments: Disclosures and Presentation (R)
IAS 33	Earnings Per Share
IAS 34	Interim Financial Reporting
IAS 36	Impairment of Asset (R)
IAS 37	Provisions, Contingent Liabilities, and Contingent Assets
IAS 38	Intangible Assets (R)
IAS 39	Financial Instruments: Recognition and Measurement (R)
IAS 40	Investment Property (R)
IAS 41	Agriculture
IFRS 1	First-time Adoption of IFRS (R)

Contd.,

IFRS 2	Share-Based Payment (R)
IFRS 3	Business Combinations (R)
IFRS 4	Insurance Contracts (R)
IFRS 5	Non-current Assets Held for Sale and Discontinued Operations (R)
IFRS 6	Exploration for and Evaluation of Mineral Resources (R)
IFRS 7	Financial Instruments: Disclosures (R)
SIC 7	Introduction of the Euro (IAS 21)
SIC 10	Government Assistance–No Specific Relation to Operating Activities (IAS 20)
SIC 12	Consolidation–Special-Purpose Entities (IAS 27) (R)
SIC 13	Jointly Controlled Entities–No monetary Contributions by Ventures (IAS 31)
SIC 15	Operating Leases–Incentives (IAS 17)
SIC 21	Income Taxes–Recovery of Revalued No depreciable Assets (IAS 12)
SIC 25	Income Taxes–Changes in the Tax Status of an Enterprise or Its Shareholders (IAS 12)
SIC 27	Evaluating the Substance of Transactions Involving the Legal Form of a Lease (IAS 1, IAS 17, and IAS 18)
SIC 29	Disclosure–Service Concession Arrangement (IAS 1)
SIC 31	Revenue–Barter Transactions Involving Advertising Services (IAS 18)
SIC 32	Intangible Assets–Web Site Costs (IAS 38)
IFRIC 1	Changes in Existing Decommissioning, Restoration and Similar Liabilities (IAS 1, IAS 8, IAS 16, IAS 23, IAS 36, IAS 37)
IFRIC 2	Members' Shares in Cooperative Entities and Similar Instruments (IAS 32, IAS 39) (R)
IFRIC 4	Determining Whether an Arrangement Contains a Lease (IAS 8, IAS 16, IAS 17, IAS 38) (R)
IFRIC 5	Rights to Interests Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds (IAS 8, IAS 27, IAS 28, IAS 31, IAS 37, IAS 39, SIC 12) (R)
IFRIC 6	Liabilities Arising from Participating in a Specific Market–Waste Electrical and Electronic Equipment

(R) = Standard is revised or newly issued in 2004 or 2005

Source: Epstein & Mirza [2006].

ACCOUNTING STANDARDS IN INDIA

In India, the setting of accounting standards is entrusted to the Institute of Chartered Accountants of India (ICAI), which is a statutory body established under the Chartered Accountants Act, 1949 it is also the premier institution for the regulation of the profession of chartered accountancy in India. It has achieved recognition of premier accounting body in the country for its contribution in the fields of education, professional development, maintenance of high accounting, auditing and ethical standards. It is also a founder member of various International professional bodies such as the IFAC, CAPA, and SAFA besides a member of International Accounting Standards Board (IASB). Being a premier accounting body in the country, the ICAI took upon itself the leadership role in standards setting process. The developments in India have been presented under (i) Financial Reporting Regulation in India; and (ii) Accounting Standards in India.

(i) Financial Reporting Regulation in India:

In tune with the world development in financial reporting, Indian financial reporting has also undergone an evolutionary process and the British Companies Acts have basically influenced this process because of historicity. The financial reporting regulation in India has been presented under (a) Its Evolution; and (b) Present Status.

(a) Its Evolution:

The first Indian statutory Act of legal recognition to financial reporting was passed in 1886, known as the Indian companies Act, 1886. Section 74 of this Act contained specific provisions about the balance sheet only under regulations 78 to 94 of the Table A. This provision required maintenance of true and correct accounts of the stock in trade of the company and the sums received and expended by it along with credits and liabilities of the company. Regarding the balance sheet, it required the summary of the property and liabilities of the company, arranged in the form annexed to the Table A or as near they were to as circumstances permitted. Highlighting the deficiencies of the balance sheet under this Act, the Bhabha Committee [1952:*126*] observed that the form of the balance sheet included very few items and the information to be disclosed was also limited.

The Indian Companies Act 1913 required more detailed provisions regarding annual reports. Sections 139 to 132 dealt with these provisions. Articles 107 and 108 of Table A presented guidelines for preparation of profit and loss account and balance sheet. Further, a compulsory form of balance sheet under Form - F of schedule III was provided. Article 107 prescribed that the profit and loss account should reveal components of gross income and expenditures under convenient heads with the amounts recognizable and chargeable. The balance sheet was required to be made out every year and laid before the general meeting of the company, accompanied by a report of directors as to state of affairs of the company, dividend proposed and the amount proposed to be carried to reserve fund.

The landmark achievements of the Companies (Amendment) Act, 1936 were related to amending section 130 requiring books to be kept by a company and penalty for not keeping books of accounts and making profit and loss account having equal status with balance sheet. Section 131 was newly introduced making directors' report on accounts compulsory. Section 132 (3) required compulsory disclosure of remuneration to agents, directors, and managers.

After independence, the Companies Act incorporated major financial reporting requirements by bringing the consolidation of the previous companies acts to the present Act, which was passed in 1956. Provisions in Table A were incorporated in the main provisions of the Act. The hallmark of this Act was that many important areas of management and company accounting practices that were entirely left to the judgment of the board of directors were brought as provisions having surveillance by shareholders.

The Companies (Amendment) Act, 1961 removed several vague accounting items like liability fund and any other fund created out of net profits and classification of items as reserves were changed as provisions. The classification of several assets into current assets and fixed assets was implemented. The content of profit and loss account was enlarged to provide a higher level of disclosure, especially with regards to different types of opening and closing stocks.

The Companies (Amendment) Act, 1973 enlarged the scope and magnitude of disclosure focusing on: (i) Specified details in respect of investments and profit earned or loss incurred in partnership firms in which the company is a partner; (ii) Quantities and amounts in respect of the turnover of each class of goods; (iii) Break-up in quantity and value in respect of each class of raw materials consumed or purchased; (iv) Class-wise break up of quantity and value in profit and loss account in respect of opening and closing stock of goods manufactured or purchased; (v) Break-up of expenditure on salary, wages and bonus in respect of employees drawing a remuneration of Rs.3,000 or more; and (vi) Suitable quantitative details regarding licensed capacity, installed capacity and actual production in respect of each class of goods manufactured.

(b) Present Status:

Most of the sections of the Companies Act, 1956 cited above relate to disclosure practices to a substantial level. It is important to note that the financial reporting measurement process is also regulated directly at the minimum level and indirectly at the maximum level. From the viewpoint of indirect regulation, Section 205 states that no dividend shall be declared or paid by a company except out of profits and the profit measurement for this purpose is subject to the provision for depreciation in accordance with sub-section 211 (2). Directly, Section 209 states that every company shall keep proper books of accounts with respect to (a) all sum of money received and expended by the company and the matters in respect of which the receipt and expenditure take place; (b) all sales and purchases of goods by the company; (c) the assets and liabilities of the company and (d) in the case of a company pertaining to any class of companies engaged in production, processing, manufacturing or mining activities, such particulars relating to utilization of materials or labor or to other items of cost as may be prescribed, if such class of companies is required by the Central Government to include such particulars in the books of account. The other aspects of the present status of financial reporting regulation in India under different sections of the Companies Act, 1956 have briefly analyzed below.

Section 211 of the Companies Act, 1956 governs the form and contents of balance sheet and profit and loss account. This provision does not apply to an insurance company, a banking company or a company engaged in generation and supply of electricity or to any other company for which a form of balance sheet and profit and low account has been specified under the Indian Electricity Act, 1948 governing such companies.

Section 211(1) provides that every balance sheet of a company shall give a true and fair view of the state of affairs of the company as at the end of the financial year and shall, subject of the provision of this section, be in the form set out in Part 1 of Schedule VI or as near thereto as circumstances admit or in such other form as may be approved by the Central Government either generally or in particular case; and in preparing the balance sheet due regard shall be had, as far as may be, to the general instructions for preparation of balance sheet under the heading "Notes" at the end of the Part.

Section 211(2) provides that every profit and loss account of a company shall give a true and fair view of the profit or loss of the company for the financial year and shall, subject as aforesaid comply with the requirements of Part II of Schedule VI, as far as they are applicable thereto.

Section 211(3) provides that the Central Government, by notification in the official Gazette, exempt any class of companies from compliance with any of the requirements in Schedule VI, if, in its opinion, it is necessary to grant the exemption in the public interest. The exemption may be granted unconditionally or subject to such conditions as may be specified in the notifications.

Section 211(4) provides that the Central Government may, on the application, or with the consent of the Board of Directors of the company, by order, modify in relation to the company any of the requirements of this Act as to the matters to be stated in the company's balance sheet or profit and loss account for the purpose of adapting them to the circumstances of the company.

Thus, in order that the statements of a company exhibit a true and fair view of the state of affairs of a company, it is necessary that the information required by law (as specified in Schedule VI to the Act and Section 212 as regards subsidiary companies) should be disclosed and that the same should be displayed in the manner required. Insurance companies, banking companies and companies engaged in generation or supply of electricity should comply with respective Acts in preparation and presentation of financial statements.

Section 211 (3A) – [Sub-sections 3A, 3B and 3C] were inserted by the Companies (Amendment) Act, 1999 with effect from 31.10.1998 and it states: "Every profit and loss account and balance sheet of the company shall comply with the accounting standards."

Section 211(3B) – "When the profit and loss accountant and the balance sheet of the company do not comply with the accounting standards, such companies shall disclose in its profit and loss account and balance sheet, the following, namely, (a) deviation from the accounting standard; (b) the reasons for such deviation; and (c) financial effect, if any, arising due to such deviation."

Section 211 (3C) states: "For the purpose of this section, the expression accounting standards/means the standards of accounting recommended by the Institute of Chartered Accountants of India constituted under the chartered Accountants Act, 1949, as may be prescribed by the Central Government in consultation with the National Advisory Committee on Accounting Standards established under sub-section (i) and Section 210 (A). Provided that standards of accounting specified by the Institute of Chartered Accountants of India shall be deemed to be the Accounting Standards until the Accounting Standards are prescribed by the Central Government under this sub-section".

Section 217 (2AA) inserted by the Companies (Amendment) Act, 2000 states that the board's report shall also include a Director's Responsibility Statement, indicating therein (i) that in the preparation of the annual accounts, the applicable accounting standards had been followed along with proper explanation relating to material departures; (ii) that the directors had selected such accounting policies and applied them consistently and made judgment and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company at the end of the financial year and of the profit or loss of the company for that period; (iii) that the directors had taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of this Act for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities; and (iv) that the directors had prepared the annual accounts on a going concern basis.

Section 219 (1) requires that a copy of every balance sheet (including the profit and loss account, the auditor's report and every other documents required by law to be annexed or attached, as the case may be, to the balance sheet), which is to be laid before a company in general meeting shall, not less than twenty-one days before the date of the meeting be sent to every member of the company and to the entitled persons. However, in the case of listed company, copies of the documents can be made available for inspection at its registered office for a period of twenty-one days before the date of meeting and the balance sheet and profit and loss account prepared in prescribed (Abridged) form can be sent for use of the members and others who do not need full statements. Such abridged accounts are to be prepared as per Form 23 AB of companies (Central Government's) General Rules and Forms 1956. The statement shall be approved by the Board of Directors and signed on behalf of them.

Section 227A (I) (b) (iv) states that in the case of a listed company, copies of the documents can be made available for inspection at its registered office for a period of 21 days before the date of meeting and the balance sheet and profit and loss account prepared in prescribed (abridged) form and they can be sent for use of the members and other entitled person.

Section 227(3) (d) requires that auditors' report shall also state whether, in his opinion, the profit and loss account and balance sheet comply with the accounting standards referred to in sub-section (3C) of Section 211.

Section 227 (4A) requires auditor's report to comply with the Companies (Auditor's Report) Order (CAR) 2003.

Section 292 A (1) has been introduced which states: "Every Company having paid-up capital of not less than five crore rupees shall constitute a Committee of the Board known as 'Audit Committee' which shall consist of not less than three directors and such number of other directors as the Board may determine of which two-thirds of the total number of members shall be directors, other than managing or whole-time directors."

(ii) Accounting Standards in India:

The setting of accounting standards in India has been taken up in the private sector led by the Institute of Chartered Accountants of India. The developments in standard setting process in India have been presented below under (a) Evolution; (b) Institutional Framework; and (c) Progress of Accounting Standards Board.

(a) Evolution:

The Institute of Chartered Accountants of India (ICAI) was established in 1949 under the Chartered Accountants Act of 1949 to serve the needs of accounting profession and improve the quality of financial reporting and regulation. It is the sole accounting institution that enjoys the right to audit the financial statements of companies. In the initial years, it paid less attention to the development of accounting principles. The Institute constituted a research committee in 1955 to give a new direction to accounting practices. Since then, it has brought out a number of research publications and guidance notes dealing with different issues in accounting and auditing. Until 1970, there were no significant developments. The setting up of ASC in 1970 in UK, replacement of APB by the FASB in 1973 in the USA and the setting up of IASC in 1973 had significant influence on the Indian accountancy profession. As a result, the ICAI became an associate member of the IASC in 1974. By becoming a member of the IASC, the Institute undertook the obligation to support the objectives of the IASC. In the background of the possible misusing of flexible accounting policy alternatives, and to improve corporate reporting practices, the Institute held a joint workshop with Associated Chambers of Commerce and Industry (ASSOCHAM) on July 21, 1976. The workshop decided to set up a joint working group to review existing requirements relating to annual corporate reports and suggest modifications thereto. The outcome of the workshop was that the adoption of IASs in Indian financial reporting was not the right approach because the profession was unfamiliar with standards and financial reporting regulation in India clashed with IASs [Bhoopatkar: 1977]. Finally, it was decided not to go in for the adoption of international standards as such and develop national standards considering the existing laws, customs, usages etc., in the country and integrating the international standards to the extent possible.

Consequent to these decisions, the Accounting Standard Board (ASB), originally called Accounting Standards Committee (ASC) was established on 21st

April 1977 as a non-standing committee of the Institute. The main function of the ASB is to formulate accounting standards in the light of national laws, customs, usages etc., and integrate to the extent possible with the international standards. Apart from the main function of formulating accounting standards, the ASB was expected to devote special attention to the following [Bhoopatkar, 1977: *253-254*]: (i) Defining the purpose and limitations of published financial statements and of the attest functions of the auditor; (ii) Enumerating and describing the basic concepts to which the practices and procedures should conform; (iii) Stating accounting principles to which the practices and procedures should conform; (iv) Defining the phrases commonly used in the audit reports and imposing he terminology in these wherever found necessary; and (v) Moving towards the reduction in number of alternative practices in accounting.

Regarding the compliance with accounting standards, the Accounting Standards Board [2004: *5*] observes: “The Accounting Standards will be mandatory from the respective date(s) mentioned in the Accounting Standard(s). The mandatory status of an accounting standard implies that while discharging their attest functions, it will be the duty of the members of the Institute to examine whether the Accounting Standards is complied with in the presentation of financial statements covered by their audit. In the event of any deviation from the Accounting Standard, it will be their duty to make adequate disclosures in their audit reports so that the users of such financial statements may be aware of such deviations.”

(b) Institutional Framework:

The institutional framework for standard setting in India basically consists of the ICAI, which is the standard setting body. However, the Securities and Exchange Board of India (SEBI) acts as the monitoring body of the Indian stock market. It also acts as the supporting body and the suggestive body for the standards set by the ICAI.

The SEBI was set up on 30th January 1992 to protect the interests of investors in securities and to promote the development of and to regulate the securities market. Initially, SEBI restricted its role in financial disclosure to improving disclosure in prospectus and other offer documents. But after stock market scams, it is getting more active in the financial reporting arena. In 1995, it directed stock exchanges to amend the listing agreement and send their shareholders full annual reports, rather than the abridged ones currently permitted by the Companies Act.

As part of capital market reform, SEBI has further tightened listing norms. It has asked all regulators to make it mandatory for companies to come up with consolidated accounts, deferred tax payments and earnings per share (EPS) in accordance with international standards of accounting. It has warned Institute of Chartered Accountants of India to draft new norms in line with IASs [The New Indian Express, 16th February, 2001]. The failure to come up with these standards by March 31st, 2001 would force regulator to make it mandatory through listing requirements.

Recently, the SEBI has amended the clauses 41 and 32 of the listing agreement and a new clause has been added to it as clause 50 making it mandatory for companies to comply with all the accounting standards. As per amendments, all the listed companies will be required to furnish segment wise revenues, results and capital employed along with quarterly un-audited results [The Financial Express, 7th September, 2001].

In India, the ICAI should also use corporate governance in its standard setting task. Hence the Kumara Mangalam Committee code on good corporate governance has now been made mandatory for all listed public companies through instrumentality of listing agreement. It has made obligatory on the audit committee to review any related party transaction, which is aimed at increasing transparency in disclosure of financial statements [The Financial Express, 10th July, 2000].

The Amended Clause in 49 of the Companies Act, 1956 provides for corporate governance. The corporate governance provides for setting up of audit committee. The SEBI's perception of audit committee role includes the following functions. (I) Of the company's reporting process and disclosure of its financial information to ensure that the financial statement is correct sufficient and credible; (ii) Reviewing with management the annual financial statements before submission to the board focusing primarily on:(a) Any changes in accounting polices and practices; (b) Major accounting entries based on exercise of judgment by management; (c) Qualification in draft report; (d) Significant adjustments arising out of audit; (e) The going concern assumption; and (f) Compliance with accounting standards. (iii) Compliance with stock exchange and legal requirements concerning financial statements; and (iv) Examination of any related party transaction.

Section 211 (3c) of the Companies (Amendment) 1999 states that the expression 'accounting standards' means standards of accounting recommended by the Institute of Chartered Accountants of India (ICAI) constituted under the Chartered Accountants Act, 1949m as may be prescribed by the Central Government in consultation with the National Advisory Committee on Accounting Standards (NACAS) established under sub-section (i) and Section 210 (A). Provided that standards of accounting specified by the Institute of Chartered Accountants of India shall be deemed to be the Accounting Standards until the Accounting Standards are prescribed by the Central Government under this sub-section." Accordingly, the NACAS was established on 15th June 2001. The basic function of the NACAS is to advise the central government on the formulation and on laying down of accounting policies and accounting standards for adoption by companies or class of companies. The Committee consists of 12 members under the chairmanship of Yezdi H. Malegam with ICAI president as member secretary. Besides, it consists of a representative from ICSI, ICWAI, joint secretary of companies affairs, a nominee of RBI, a member from IA and AS, representative from university, a member from CBDT, nominee of SEBI, a representative from industry (CII nominee), and FICCI nominee. It is important to note that the advisory committee is only a recommendatory body to the central government. In nutshell, it may be observed that the establishment of ASs is still the prerogative of the ICAI and NACAS is a link between the ICAI and the central government, which gives official sanctity to the standards. It is still not clear at this stage regarding the strategic role played by the NACAS.

(c) Progress of Accounting Standards Board:

The Institute of Chartered Accountants of India (ICAI) constituted the Accounting Standards Board (ASB) on 21st April 1977 with the main objective of harmonizing the diverse accounting policies and practices in India.

The various dimensions of accounting standards promulgated by ASB have been presented under (1) Objectives of the ASB; (2) Scope of Accounting Standards; (3) Presentation of a Standard; (4) Compliances of ASs; (5) Applicability of ASs; (6) Exemptions/Relaxations for SMEs; (7) Universal Applicability; and (8) Progress of Accounting Standards.

(1) Objectives of the ASB:

The following are the objectives of the Accounting Standards Board: (a) To conceive of and suggest areas in which Accounting Standards need to be developed; (b) To formulate Accounting Standards with a view to assisting the Council of the ICAI in evolving and establishing Accounting Standards in India; (c) To examine how far the relevant International Accounting Standards/International Financial Reporting Standards can be adapted while formulating the Accounting Standards and to adapt the same; (d) To review, at regular intervals, the Accounting Standards from the point of view of acceptance or changed conditions, and, if necessary, revise the same; (e) To provide, from time to time, interpretations and guidance on Accounting Standards; and (f) To carry out such other functions relating to Accounting Standards.

(2) Scope of Accounting Standards:

Efforts are made to issue Accounting Standards, which are in conformity with the provisions of the applicable laws, customs, usages and business environment in India. However, if a particular Accounting Standard is found to be not in conformity with law, the provisions of the said law will prevail and the financial statements should be prepared in conformity with such law.

The Accounting Standards by their very nature cannot and do not override the local regulations, which govern the preparation and presentation of financial statements in the country. However, the ICAI will determine the extent of disclosure to be made in financial statements and the auditor's report thereon.

Such disclosure may be by way of appropriate notes explaining the treatment of particular items. Such explanatory notes will be only in the nature of clarification and therefore need not be treated as adverse comments on the related financial statements.

The Accounting Standards are intended to apply only to items, which are material. Any limitations with regard to the applicability of a specific Accounting Standard will be made clear by the ICAI from time to time. The date from which a particular Standard will come into effect, as well as the class of enterprises to which it will apply, will also be specified by the ICAI. However, no standard will have retrospective application, unless otherwise stated.

The institute will use its best endeavors to persuade the Government, appropriate authorities, industrial and business community to adopt the Accounting Standards in order to achieve uniformity in preparation and presentation of financial statements. In formulation of Accounting Standards, the emphasis would be on laying down accounting principles and not detailed rules for application and implementation thereof.

(3) Presentation of a Standard:

The standards formulated by the ASB include paragraphs in bold italic type and plain type, which have equal authority. Paragraphs in bold italic type indicate the main principles. An individual standard should be read in the context of the objective stated in that standard and the Preface to the Statements of Accounting Standards.

The ASB may consider any issue requiring interpretation on any accounting standard. Interpretations will be issued under the authority of the Council. The authority of interpretation is the same as that of Accounting Standard to which it relates.

(4) Compliance with ASs:

The Accounting Standards are mandatory from the respective date(s) mentioned in the Accounting Standard(s). The mandatory status of an Accounting Standard implies that while discharging their attest functions, it will be the duty of the members of the Institute to examine whether the Accounting Standard is complied with in the presentation of financial statements covered by their audit. In the event of any deviation from the Accounting Standard, it will be their duty to make adequate disclosures in their audit reports so that the users of financial statements may be aware of such deviation.

Ensuring compliance with the Accounting Standards while preparing the financial statements is the responsibility of the management of the enterprise. Statutes governing certain enterprises require of the enterprises that the financial statements should be prepared in compliance with the Accounting Standards. Financial statements cannot be described as complying with the Accounting Standards unless they comply with all the requirements of each applicable standard.

(5) Applicability of ASs:

The Council, at its 236th meeting, held on September 16-18, 2003, considered the matter relating to applicability of Accounting Standards to Small and Medium Sized Enterprises [SMEs]. This scheme comes into effect in respect of accounting periods commencing on or after 1-4-2004. The Council decided the following scheme for applicability of accounting standards to SMEs and the scheme is presented in Figure 2.1.

FIGURE 2.1
APPLICABILITY OF ASs

(1) For the purpose of applicability of Accounting Standards, enterprises are classified into three categories, viz., Level I, Level II and Level III. Level II and Level III enterprises are considered as SMEs;

(2) Level I enterprises are required to comply fully with all the accounting standards; and

(3) It has been decided that no relaxation should be given to Level II and Level III enterprises in respect of recognition and measurement principles. Relaxations are provided with regard to disclosure requirements. Accordingly, Level II and Level III enterprises are fully exempted from certain accounting standards, which primarily lay down disclosure requirements. In respect of certain other accounting standards, which lay down recognition, measurement and disclosure requirements, relaxation from certain disclosure requirements are given. The exemptions/relaxations are decided to be provided by modifying the applicability portion of the relevant accounting standards.

Source: ICAI [2005]. *Compendium of Accounting Standards,* New Delhi: ICAI.

The criteria for classification of enterprises into Level I, Level II and Level III are given in Figure 2.2

FIGURE 2.2
CRITERIA FOR CLASSIFICATION OF ENTERPRISES

Level I Enterprises

Enterprises which fall in any one or more of the following categories, at any time during the accounting period, are classified as Level I enterprises:

(i) Enterprises whose equity or debt securities are listed whether in India or outside India.

(ii) Enterprises, which are in the process of listing their equity or debt securities as evidenced by the board of directors' resolution in this regard.

(iii) Banks including co-operative banks.

(iv) Financial institutions.

(v) Enterprises carrying on insurance business.

(vi) All commercial, industrial and business reporting enterprise, whose turnover for the immediately preceding accounting period on the basis of audited financial statements exceeds Rs.50 crore. Turnover does not include 'other income.'

(vii) All commercial, industrial and business reporting enterprises having borrowings, including public deposits, in excess of Rs.10 crore at any time during the accounting period.

(viii) Holding and subsidiary enterprises of any one of the above at any time during the accounting period.

Level II Enterprises:

Enterprises which are not Level I enterprises but fall in any one or more of the following categories are classified as level II enterprises:

(i) All commercial, industrial and business reporting enterprises, whose turnover for the immediately preceding accounting period on the basis of audited financial statements exceeds Rs.40 lakh but does not exceed Rs.50 crore. Turnover does not include 'other income.'

(ii) All commercial, industrial and business reporting enterprises having borrowings, including public deposits, in excess of Rs.1 crore but not in excess of Rs. 10 crore at any time during the accounting period.

(iii) Holding and subsidiary enterprises of any one of the above at any time during the accounting period.

Level III Enterprises:

Enterprises, which are not covered under Level I and Level II are considered as Level III enterprises.

Source: ICAI [2005]. *Compendium of Accounting Standards*, New Delhi: ICAI.

(6) Exemptions/Relaxations for SMEs:

The details of exemptions/relaxations of SMEs are presented under Figure 2.3.

FIGURE 2.3
EXEMPTIONS/RELAXATIONS FOR SMEs

(A) Accounting Standards not applicable to Level II and Level III enterprises in their entirety:

- (i) AS 3, Cash Flow Statements;
- (ii) AS 17, Segment Reporting;
- (iii) AS 18, Related Party Disclosures; and
- (iv) AS 24, Discontinuing Operations.

(B) Accounting Standards not applicable to Level II and Level III enterprises since the relevant Regulators require compliance with them only by certain Level I enterprises.*

- (i) AS 21, Consolidated Financial Statements;
- (ii) As 23, Accounting for Investments in Associated in Consolidated Financial Statements; and
- (iii) AS 27, Financial Reporting of Interests in Joint Ventures [to the extent of requirements relating to consolidated financial statements].

*AS 21, AS 23 and AS 27 [relating to consolidated financial statements] are required to be complied with by an enterprise if the enterprise, pursuant to the requirements of a statute/regulator or voluntarily, prepares and presents consolidated financial statements.

(C) Accounting Standards in respect of which relaxations from certain disclosure requirements have been given to Level II and Level III enterprises.

(i) AS 19, Leases

Paragraphs 22[c], [e] and [f]; 25[a], [b] and [e]; 37[a], [f] and [g]; and 46[b]; [d] and [e], of AS 19 are not applicable to Level II and Level III enterprises.

(ii) AS 20, Earnings Per Share
As regards As 20, diluted earnings per share and information required by paragraph 48 of AS 20 are not required to be disclosed by Level II and Level III enterprises if this standard is applicable to these enterprises because they disclose earnings per share. So far as companies are concerned, since all the companies are required to apply AS 20 by virtue of the provisions of Part IV of Schedule VI to the Companies Act, 1956, requiring disclosure of earnings per share, the position is that the companies which do not fall in Level I, would not be required to disclose diluted earnings per share and information required by paragraph 48 of AS 20.

(iii) AS 29, Provisions, Contingent Liabilities and Contingent Assets

- Paragraph 67 is not applicable to Level II enterprises.
- Paragraphs 66 and 67 are not applicable to Level II and Level III enterprises.

The above relaxations are incorporated in AS 29 itself.

(D) Accounting Standard applicability of which is deferred for Level II and Level III enterprises:

AS 28, Impairment of Assets

- For Level I Enterprises applicable from 1-4-2004.
- For Level II Enterprises applicable form 1-4-2006.
- For Level III Enterprises applicable from 1-4-2008.

(E) AS 25, Interim Financial Reporting does not require any enterprise to present interim financial report. It is applicable only if an enterprise is required or elects to prepare and present an interim financial report. However, the recognition and measurement requirements contained in this Standard are applicable to interim financial results, e.g. quarterly financial results required by the SEBI.

Source: ICAI [2005]. *Compendium of Accounting Standards,* New Delhi: ICAI.

(7) Universal Applicability:

Accounting Standards applicable to all enterprises in their entirety [Level I, II, and III] are presented in Figure 2.4

FIGURE 2.4
UNIVERSAL APPLICABILITY

(i)	AS 1, Disclosure of Accounting Policies
(ii)	AS 2, Valuation of Inventories
(iii)	AS 4, Contingencies and Events Occurring After the Balance Sheet Date
(iv)	AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
(v)	As 6, Depreciation Accounting
(vi)	AS 7, [revised 2002], Construction Contracts[1]
i.	AS 7, [issued 1983], Accounting for Construction Contracts
(vii)	AS 8, Accounting for Research and Development[2]
(viii)	AS 9, Revenue Recognition
(ix)	AS 10, Accounting for Fixed Assets
(x)	AS 11 [revised 2003], The Effects of Changes in Foreign Exchange

	Rates[3]
	AS 11, [issued 1994], Accounting for the Effects of Changes in Foreign Exchange Rates
(xi)	AS 12, Accounting for Government Grants
(xii)	AS 13, Accounting for Investments
(xiii)	AS 14, Accounting for Amalgamations
(xiv)	AS 15, Accounting for Retirement Benefits in the Financial Statements of Employers
(xv)	AS 16, Borrowing Costs
(xvi)	AS 22, Accounting for Taxes on Income
(xvii)	As 26, Intangible Assets

[1]The revised Standard [2002] comes into effect in respect of all contracts entered into during accounting periods commencing on or after 1-4-2003 and is mandatory in nature from that date. Accordingly, the pre-revised AS 7 [issued 1983] is not applicable in respect of such contracts.

[2] AS 8 is withdrawn form the date AS 26, Intangible Assets, becoming mandatory for the concerned enterprises, As 26 is mandatory in respect of expenditure incurred on intangible items during accounting periods commencing on or after 1-4-2003 for the following:

i. Enterprises whose equity or debt securities are listed on a recognized stock exchange in India, and enterprises that are in the process of issuing equity or debt securities that will be listed on a recognized stock exchange in India as evidenced by the board of directors' resolution in this regard.
ii. All other commercial, industrial and business reporting enterprises, whose turnover for the accounting period exceeds Rs.50 crore.

In respect of all other enterprises, AS 26 is mandatory in respect of expenditure incurred on intangible items during accounting periods commencing on or after 1-4-2004.

[3] The revised AS 11 [2003] would come into effect in respect of accounting periods commencing on or after 1-4-2004 and would be mandatory in nature from that date. The revised Standard [2003] would supersede As 11 [1994], except that in respect of accounting for transactions in foreign currencies entered into by the reporting enterprise itself or through its branches before the date the revised AS 11 [2003] comes into effect, As 11 [1994] will continue to be applicable.

Source: ICAI [2005]. *Compendium of Accounting Standards,* New Delhi: ICAI.

(8) Progress of ASs:

Since its inception, the ASB has promulgated 30 accounting standards and there are 29 standards at present with the AS-8 on 'Accounting For Research and Development' being withdrawn and included under AS-26 on 'Intangible Assets'

FIGURE 2.5
ACCOUNTING STANDARDS AS ON JULY 1, 2005

Sl. No.	Accounting Standard [AS] No.	Title of the Accounting Standard	Date from which mandatory [accounting periods commencing on or after]	Mandatory
(1)	AS 1	Disclosure of Accounting Policies	1-4-1991 – for companies governed by the Companies Act, 1956, as well as for enterprises other than those specified in Note 1. 1-4-1993 – for all enterprises, including those specified in Note 1.	For all enterprises
(2)	AS 2 [Revised]	Valuation of Inventories	1-4-1999	For all enterprises
(3)	AS 3[Revised]	Cash Flow Statements	1-4-2001	See Note 2
(4)	AS 4 [Revised]	Contingencies and Events Occurring After the Balance Sheet date	1-4-1995	For all enterprises
(5)	AS 5[Revised]	Net Profit or Loss for the Period, Prior Period Items and Changes I Accounting Policies	1-4-1996	For all enterprises
(6)	AS 6 [Revised]	Depreciation Accounting	1-4-1995	For all enterprises
(7)	AS 7	Accounting for Construction Contracts	As in case of AS 1 above [see also Note 3.]	For all enterprises
(8)	AS 8*	Accounting for Research and Development	As in case of AS 1 above	For all enterprises
(9)	AS 9	Revenue Recognition	As in case of AS 1 above	For all enterprises
(10)	AS 10	Accounting for Fixed Assets	As in case of AS 1 above	For all enterprises
(11)	AS 11[Revised]	Accounting for the Effects of Changes in Foreign Exchange Rates	1-4-1995	For all enterprises [see also Announce-ment IX above]
(12)	AS 12	Accounting for Government Grants	1-4-1994	For all enterprises
(13)	AS 13	Accounting for Investments	1-4-1995	For all enterprises
(14)	AS 14	Accounting for Amalgamations	1-4-1995	For all enterprises
(15)	AS 15	Accounting for Retirement Benefits in the Financial Statements of Employers	1-4-1995	For all enterprises
(16)	AS 16	Borrowing Costs	1-4-2000	For all enterprises
(17)	AS 17	Segment Reporting	1-4-2001	See Note 2
(18)	AS 18	Related Party Disclosures	1-4-2001	See Note 2
(19)	AS 19	Leases	In respect of all assets leased during accounting periods commencing on or after 1-4-2001	For all enterprises
(20)	AS 20	Earnings Per Share	1-4-2001 [see also Note 4]	See Note 4
(21)	AS 21	Consolidated Financial Statements	1-4-2001 [see also Note 5]	See Note 5
(22)	AS 22	Accounting for Taxes on Income	See Note 6	See Note 6

(23)	AS 23	Accounting for Investments in Associates in Consolidated Financial Statements	1-4-2002 [see also Note 7]	See Note 7
(24)	AS 24	Discontinuing Operations	2004-05	See Note 8
(25)	AS 25	Interim Financial Reporting	1-4-2002 [see also Note 9]	See Note 9
(26)	AS 26	Intangible Assets	2003-04	See Note 10
(27)	AS 27	Financial Reporting of Interests in Joint Ventures	1-4-2002 [see also Note 11]	See Note 11
(28)	AS 28	Impairment of Assets	2004-05	See Note 12
(29)	AS 29	Provisions, Contingent Liabilities and Contingent Assets	2004	

*AS 8 would stand withdrawn with effect from the date AS 26, 'Intangible assets,' becomes mandatory [see Note 10 of this Table].

Note 1:
(a) Sole proprietary concerns/individuals
(b) Partnership Firms
(c) Societies registered under the Societies Registration Act
(d) Trusts
(e) Hindu Undivided Families
(f) Associations of persons

Note 2: AS 3, AS 17, and AS 18 have been made mandatory in respect of following enterprises:

(i) Enterprises whose equity or debt securities are listed on a recognized stock exchange in India, and enterprises that are in the process of issuing equity or debt securities that will be listed on a recognized stock exchange in India as evidenced by the board of directors' resolution in this regard.
(ii) All other commercial, industrial and business reporting enterprises, whose turnover for the accounting period exceeds Rs.50 crore.

Note 3: This standard has been revised as Accounting Standard (AS) 7, 'Construction Contracts.' The revised standard would come into effect in respect of all contracts entered into during accounting periods commencing on or after 1-4-2003 and will be mandatory in nature from that date. Accordingly, Accounting Standard (AS) 7, 'Accounting for Construction Contracts,' issued by the Institute in December 1983, will not be applicable in respect of such contracts.

Note 4: AS 20 is mandatory in nature in respect of enterprises whose equity shares or potential equity shares are listed on a recognized stock exchange in India. An enterprise, which has neither equity shares nor potential equity shares which are so listed but which discloses earnings per share, should calculate and disclose earnings per share in accordance with As 20. it has been clarified that every company, which is required to give information under Part IV of the Schedule VI of the Companies Act, 1956, should calculate and disclose earnings per share in accordance with AS 20, whether its equity shares or potential equity shares are listed on a recognized stock exchange in India or not.

Note 5: AS 21 is mandatory if an enterprise presents consolidated financial statements. In other words, the accounting standard does not mandate an enterprise to present consolidated financial statements but, if the enterprise presents consolidated financial statements in accordance with AS 21.

Note 6: As 22 comes into effect in respect of accounting periods commencing on or after 1-4-2001. It is mandatory in nature for:

(a) All the accounting periods commencing on or after 1-4-2001, in respect of the following:
  (i) Enterprises whose equity or debt securities are listed on a recognized stock exchange in India and enterprises that are in the process of issuing equity or debt securities that will be listed on a recognized stock exchange in India as evidenced by the board of directors' resolution in this regard.
  (ii) All the enterprises of a group, if the parent presents consolidated financial statements and the Accounting Standard is mandatory in nature in respect of any of the enterprises of that group in terms of (i) above.

(b) All the accounting periods commencing on or after 1-4-2002, in respect of companies not covered by (a) above.
(c) All the accounting periods commencing on or after 1-4-2002, in respect of all other enterprises.

Note 7: AS 23 comes into effect in respect of accounting periods commencing on or after 1-4-2002. AS 23 is mandatory if an enterprise presents consolidated financial statements. In other words, if an enterprise presents consolidated financial statements, it should account for investments in associates in the consolidated financial statements in accordance with AS 23 from the date of its coming into effect, i.e., 1-4-2002.

Note 8: AS 24 will be mandatory in nature in respect of accounting periods commencing on or after 1-4-2004 for the following:

(i) Enterprises whose equity or debt securities are listed on a recognized stock exchange in India, and enterprises that are in the process of issuing equity or debt securities that will be listed on a recognized stock exchange in India as evidenced by the board of directors' resolution in this regard.

(ii) All other commercial, industrial and business reporting enterprises, whose turnover for the accounting period exceeds Rs.50 crore.

In respect of all other enterprises, the Accounting Standard will be mandatory in nature in respect of accounting periods commencing on or after 1-4-2005.

Note 9: AS 25 comes into effect I respect of accounting periods commencing on or after 1-4-2002. This AS does not mandate which enterprises should present interim financial reports, how frequently, or how soon after the end of an interim period. If an enterprise is required or elects to prepare and present an interim financial report, it should comply with this AS.

Note 10: AS 26 will come into effect in respect of expenditure incurred on intangible items during accounting periods commencing on or after 1-4-2003 and will be mandatory in nature from that date for the following:

(i) Enterprises whose equity or debt securities are listed on a recognized stock exchange in India, and enterprises that are in the process of issuing equity or debt securities that will be listed on a recognized stock exchange in India as evidenced by the board of directors' resolution in this regard.

(ii) All other commercial, industrial and business reporting enterprises, whose turnover for the accounting period exceeds Rs.50 crore.

Note 11: AS 27 comes into effect in respect of accounting periods commencing on or after 1-4-2002. In respect of separate financial statements of an enterprise, this AS is mandatory in nature form that date. In respect of consolidated financial statements of an enterprise, this standard is mandatory in nature where the enterprise prepares and presents the consolidated financial statements in respect of accounting periods commencing on or after 1-4-2002.

Note 12: AS 28 will come into effect in respect of accounting periods commencing on or after 1-4-2004 and will be mandatory in nature from that date for the following:

(i) Enterprises whose equity or debt securities are listed on a recognized stock exchange in India, and enterprises that are in the process of issuing equity or debt securities that will be listed on a recognized stock exchange in India as evidenced by the board of directors' resolution in this regard.

(ii) All other commercial, industrial and business reporting enterprises, whose turnover for the accounting period exceeds Rs.50 crore.

In respect of all other enterprises, the Accounting Standard will come into effect in respect of accounting periods commencing on or after 1-4-2005 and will be mandatory in nature from that date.

Sources: (1) ICAI [2005]. *Compendium of Accounting Standards,* New Delhi: ICAI, Table C, pp.xxvi–xxxiii; and (2) Kumar, M.P. Vijay., [2006]. *First Lessons in* Accounting *Standards,* Sixth Edition, Mumbai: Snow White Publication Pvt. Ltd. Index, pp. xvii - xviii.

IAS Vs. AS IN INDIA

It is very much true that the national accounting standards are to be promulgated by adopting the IAS as far as possible. However, it is observed that these national accounting standards vary from the IAS with a minimum of difference and wide ranging differences. Comparing the accounting standards in India vis-à-vis IAS, Baingani and Agarwal [2005:*1052-1060*] list the major differences between IFRS/IAS and Indian accounting standards. Table2.3 summarizes these differences.

TABLE 2.2
IFRS/IAS Vs. Indian Accounting Standards

AS by ICAI	IFRS/ IAS	Position under IAS/IFRS After considering recent changes	Position as per Indian GAAP
AS-1	IAS-1	**Disclosure of Accounting Policies:** IAS 1, inter alia, deals with overall considerations, including fair presentation, off-setting, comparative information. IAS 1 prescribed minimum structure of financial statements and contains guidance on elated issues viz. current liabilities etc. Under IAS 1, financial statements includes Statement showing changes in equity Under IAS 1, there is a presumption that application of IFRS would lead to fair presentation IAS 1 requires specific disclosure for departures from IFRS IAS 1 requires disclosure of critical judgments made by management in applying accounting policies IAS 1 prohibits any items to be disclosed as extraordinary items.	AS 1 does not deal with these aspects. AS 1 does not prescribe any minimum structure. AS 1 does not prescribe any such statement to be prepared. There is no such presumption under AS 1. There is no such specific provision in AS 1. There is no such specific disclosure requirement in AS 1 AS 5 specifically requires disclosure of certain items as Extra-ordinary items.
AS-2	IAS-2	**Valuation of Inventories:** IAS 2 prescribes same cost formula to be used for all inventories having a similar nature and use to the	AS 2 requires that the formula used in determining the cost of an item

		entity. **There are certain additional requirement in IAS 2 which are not contained in AS 2 which are as under:** 1. Purchase of inventory on deferred settlement terms - excess over normal price is to be accounted as interest over the period of financing. 2. Measurement criteria are not applicable to commodity broker-traders. 3. Exchange differences are not includible in inventory valuation. 4. Inventory pledged as security for liabilities requires separate disclosure.	of inventory needs to be selected with a view to providing the fairest possible approximation to the cost incurred in bringing the item to its present location and condition. However, there is no stipulation for use of same cost formula in AS 2 as compared to IFRS
AS-3	**IAS-3**	**Cash Flow Statements**: Bank overdrafts are to be treated as a component of cash / cash equivalents under IAS 7.	AS 3 has no such stipulation
		IAS 7 allows interest and dividend paid to be classified either under Operating Activities or Financing Activities.	AS 3 mandates disclosure of interest and dividend paid under Financial Activities only.
		IAS 7 requires additional disclosure of cash payments by a lessee relating to finance lease under Financing Activities.	No such disclosures required under AS 3.
		IAS 7 deals with issues relating to disclosure in cash flow statement in consolidated financial statements viz. Undistributed profits of associate & minority interests, Forex cash flows of foreign subsidiary etc.	AS 3 was issued prior to AS 21, hence issues relating to consolidate financial statements are not dealt with.
		IAS 7 prohibits separate disclosure of extraordinary items in Cash Flow Statements.	AS 3 mandates such disclosure.
		In case of acquisition of subsidiary, IAS 7 requires two Additional disclosures on acquisitions viz. Cash/ cash equivalents of acquired subsidiary and all other assets acquired.	No such provision in AS 3
AS 4	**IAS 10**	**Contingencies and Events occurring after the Balance Sheet Date:** IAS 10 provides that proposed dividend should not be shown as liability.	AS 4 specifically requires such disclosure as the same is mandated by statutory requirement.
		IAS 10 requires date of authorization for issue of financial statements to be specifically mentioned in the financial statements itself.	AS 4 has no such stipulation.
		IAS 10 also requires disclosure of contingent liability to be updated in the light of new information received after the balance sheet date.	AS 4 requires adjustments to figures stated in financial statements for events occurring after the balance sheet date, if such events relate to conditions existing at the balance sheet date.

AS 5	IAS 8	**Prior Period Items and Changes in Accounting Policies:** In case of change in accounting policy IAS 8 requires retrospective effect to be given by adjusting opening retained earnings. The **definition of prior period Items is broader** under IAS 8 as compared to AS 5 since IAS 8 covers all the items in the financial statements. IAS 8 requires retrospective restatement of prior period figures by restatement of opening balances of assets, liabilities and equity for the earliest period practicable. IAS 8 requires disclosure of any impending change in accounting policy viz. change mandated by a new accounting standard which is yet to come into effect.	AS 5 requires only prospective change in accounting policy with appropriate disclosures. AS 5 covers only incomes and expenses in the definition of prior period items. AS 5 requires prior period items to be included in the determination of net profit or loss for the current period. AS 5 does not require such disclosure
AS-6	No Corresponding IAS (covered by IAS which discuss about assets)	**Depreciation Accounting (AS 6):** In case of change in method of depreciation, IAS 16 requires effect to be given respectively. Change in method of depreciation is treated as change in accounting estimate under IAS 16. IAS 16 requires estimation of Residual value without considering inflation effects i.e, residual value has to be estimated assuming that the asset were already of the age and in the condition expected at the end of its useful life	AS 6 requires retrospectively re-computation of depreciation and any excess or deficit on such re-computation is required to be adjusted in the period in which such change is effected. AS 6 considers this as change in accounting policy There is no such stipulation in AS 6 although it prescribes use of realizable value of similar assets, which have reached the end of their useful lives and have operated under conditions similar to the asset as one of the basis of estimating residual value.
AS-7 (Revised)	IAS 11	**Construction Contract (AS 7):** Contract Revenue under IAS 11 is measured at the fair value of the consideration received or receivable.	AS 7 does not refer to fair value and states that Contract revenue is measured at the consideration received or receivable
AS-9	IAS-18	**Revenue Recognition (AS 9):** Under IAS 18, revenue from sale of goods cannot be recognized when entity retains continuing managerial ownership or effective control over the goods sold. In case of revenue from rendering of services, IAS 18 allows only percentage of completion method. IAS 18 requires effective interest method prescribed in IAS 39 to be followed for interest income recognition. Under IAS 18, payments received in advance for goods yet to be manufactured or third party sales, cannot be recognized as revenue until such goods are delivered to the buyer.	AS 9 does not contain any such stipulation. AS 9 allows completed service contract method or proportionate completion method. AS 9 requires interest income to be recognized on a time proportion basis. AS 9 permits recognition when the goods are manufactured, identified and ready for delivery in such cases.
AS-10	IAS-16	**Accounting for Fixed Assets**: Under IAS 16, if subsequent costs are incurred for replacement of a part of an item of fixed assets, such costs are required to be capitalized and simultaneously the replaced part has to be de-capitalized.	AS 10 provides that only that expenditure which increases the future benefits from the existing asset beyond its previously assessed standard of performance is included in the gross book value, e.g., an increase in capacity.
AS-11(Revised)	IAS-21	**Effects of changes in Foreign Exchange Rates:** The revised IAS 21 makes no distinction between an integral foreign operation and non-integral foreign operation as done in AS 11. In fact, the factors of	AS 11 provides separate treatment for integral

		distinction between an integral operation and a non-integral operation are incorporated as considerations for determining functional currency.	operations and non-integral operations.
		Revised IAS 21 requires an entity to determine functional currency and measure results and financial position in that currency. Functional currency is the currency of the primary economic environment.	There is no concept of functional currency under AS 11.
		Under the revised IAS 21 states that if functional currency of a foreign operation is other than reporting currency, the provisions of translation of such operation are similar to that prescribed for a non-integral foreign operation under AS 11.	Absence of functional currency concept does not enable AS 11 to provide for such a stipulation.
		If financial statements are presented in any other currency other than functional currency, the revised IAS 21 requires Assets /Liabilities to be translated at Closing Rate and Income / Expenses at Average Rate.	AS 11 does not contain any guidance on this issue.
AS-12	**IAS-20**	**Government Grants**:	
		The concept of extra-ordinary item is deleted under all standards of IFRS.	AS 12 requires disclosure of government grants for financial support / compensation for losses as extra-ordinary items in P&L.
		In case of non-monetary assets acquired at nominal / concessional rate, IAS 20 permits accounting either at fair value or at acquisition cost	AS 12 requires accounting at acquisition cost.
		In respect of grant related to a specific fixed asset becoming refundable, IAS 20 requires retrospective re-computation of depreciation and prescribes charging off the deficit in the period in which such grant becomes refundable.	AS 12 requires enterprise to compute depreciation prospectively as a result of which the revised book value is provided over the residual useful life.
		IAS 20 requires separate disclosure of unfulfilled conditions and other contingencies if grant has been recognised.	AS 12 has no such disclosure requirement.
AS-14	**IFRS 3(IFRS 3 supersedes IAS 22)**	**Accounting for Amalgamations:**	
		IFRS 3 allows only purchase method. Option of pooling method given under IAS 22 has been withdrawn.	AS 14 allows both Pooling of Interest Method and Purchase Method.
		IFRS 3 requires valuation of assets & liabilities at Fair Value.	AS 14 requires valuation at carrying value.
		IFRS 3 requires Goodwill to be tested for impairment.	AS 14 requires amortization of Goodwill
		IFRS 3 requires recognition of negative goodwill immediately in P&L A/c.	AS 14 requires it to be credited to Capital Reserve
		IFRS 3: Reverse Acquisition is accounted assuming acquirer is the acquiree.	AS 14 does not deal with reverse acquisition
		IFRS 3 requires valuation of Financial Assets to be dealt with as per IAS 39.	AS 14 contains no such similar provision.
		Under IFRS 3, provisional values can be used provided they are updated retrospectively within 12 months with actual values.	There is no such provision in AS 14.
Exposure Draft issued on AS-15	**IAS 19**	**Employee Benefits:**	
		IAS 19 provides an option to recognise actuarial gains and losses either by following "Corridor Approach" or immediately in P&L A/c.	Exposure draft on revised AS 15 (AS 15 ED) does not admit "Corridor Approach".
		Under IAS 19, the discount rate used to discount post employment benefit obligations should be determined by reference to market yields of high quality corporate bonds or, in case there is no deep market in such bonds, on the basis of market yields of Govt. bonds.	Exposure draft on revised AS 15 allows use of only market yields on Govt. bonds.
		Under IAS 19, the liability for termination benefits	

		has to be recognized on constructive basis for e.g. Announcement of a formal plan.	AS 15 ED requires an entity to follow AS 29 in this regard.
		IAS 19 provides a choice to recognize the incremental liability on first time application either immediately in P&L or over a period of five years on SLM basis.	AS 15 ED requires adjustment against opening balance of revenue reserves.
AS-16	IAS 23	**Borrowing Costs :** IAS 23 prescribes borrowing costs to be recognized as expense as benchmark treatment. It requires capitalization as an allowed alternative.	AS 16 mandates capitalization
		IAS 23 requires disclosure of capitalization rate used to determine the amount of borrowing costs.	AS 16 does not require such disclosure.
AS-17	IAS 14	**Segment Reporting:** IAS 14 prescribes treatment of revenue, expenses, profit/loss, assets and liabilities in relation to Associates & Joint Ventures in consolidated financial statements.	AS 17 is silent on the aspect of treatment in consolidated financial statements.
		IAS 14 encourages reporting of vertically integrated activities as separate segments but does not mandate the disclosure.	AS 17 does not make any distinction between vertically integrated segment and other segments
		IAS 14 provides that a business segment can be treated as reportable segment only if, inter alia, majority of its revenue is earned from sales to external customers.	AS 17 does not contain any such stipulation.
		Under IAS 14, if a reportable segment ceases to meet threshold requirements, than also it remains reportable for one year if the Management judges the segment to be of continuing significance.	Under AS 17, this is mandatory irrespective of the judgment of Management.
		In case of change in identification of segments, IAS 14 requires restatement of prior period segment information. In case it is not practicable, IAS 14 requires disclosure of data for both the old and new bases of segmentation.	AS 17 requires only disclosure of the nature of the change and the financial effect of the change, if reasonably determinable.
AS-18	IAS 24	**Related Party Disdosures:** The definition of related party under IAS 24 includes Post employment benefit plans (e.g. gratuity fund, pension fund) of the enterprise or of any other entity, which is a related party of the enterprise.	AS 18 does not include this relationship.
		The definition of Key management persons (KMPs) under IAS 24 includes any director whether executive or otherwise i.e. Non-executive directors are also related party. Further, under IAS 24, if any person has indirect authority and responsibility for planning, directing and controlling the activities of the enterprise, he will be treated as a key management person (KMP)	AS 18 read with ASI-18 excludes non-executive directors from the definition of key management persons. AS 18 does not specifically cover indirect authority and responsibility.
		The definition of related party under IAS 24 includes close members of the families of KMPs as related party as well as of persons who exercise control or significant influence.	AS 18 covers only relatives of KMPs
		IAS 24 requires compensation to KMPs to be disclosed category-wise including share-based payments.	AS 18 read with ASI 23 requires disclosure of remuneration paid to key management persons but does not mandate category-wise disclosures.
		IAS 24 mandates that no disclosure should be made to the effect that related party transactions were made on arms length basis unless terms of the related party transaction can be substantiated	AS 18 contains no such stipulation.
		No concession is provided under IAS 24 where	AS 18 provides exemption from

		disclosure of information would conflict with the duties of confidentiality in terms of statute or regulating authority.	disclosure in such cases.
		Under IAS 24, the definition of "control" is restrictive as it requires power to govern the financial and operating policies of the management of the enterprise	Under AS 18, the definition is wider as it refers to power to govern the financial and /or operating policies of the management.
		The definition of "control" under IAS 24 is restrictive on the count that it does not include control over composition of Board of Directors	AS 18 includes control over composition of Board of Directors in the definition of "control"
		The disclosure requirement under IAS 24 are applicable when related party relationship exists as on the date of balance sheet	Under AS 18 the standard applies if related party relationship exist at any time during the year.
		IAS 24 requires disclosure of terms and conditions of outstanding items pertaining to related parties.	No such disclosure requirement is contained in AS 18.
		IAS 24 does not define "significant influence" which is to be considered while determining related party relationship.	AS 18 prescribe a rebuttable presumption of significant influence if 20% or more of the voting any party holds power.
AS-19	**IAS -17**	**Leases** Under IAS-17 it has been clarified that land and buildings elements of a lease of land and buildings need to be considered separately. The land element is normally an operating lease unless title passes to the lessee at the end of the lease term. The buildings element is classified as an operating or finance lease by applying the classification criteria.	AS-19 - " Accounting for Leases" at it stands at present does not deal with lease agreements to use lands. Hence, the classification criteria are applicable only to buildings as a separate asset. To be in line with IAS-17, a suitable modification is required in AS-19 to bring lease agreements for use of land within the purview and prescribe separate classification criteria for land as stated in revised IAS-17.
		The definition of residual value is not included in IAS 17. IAS 17 specifically excludes lease accounting for investment property and biological assets.	AS 19 defines residual value. There is no such exclusion under AS 19.
		IAS 17 does not prohibit upward revision in value of un-guaranteed residual value during the term of lease.	AS 19 permits only downward revision
		In case of sale & lease back, IAS 17 requires excess of sale proceeds over the carrying amount to be deferred and amortised over lease term.	AS 19 requires excess or deficiency both to be deferred and amortised over the lease term in proportion to the depreciation of the leased asset.
		IAS 17 does not require any separate disclosure for assets acquired under finance lease segregated from assets owned.	AS 19 mandates such separate disclosure.
		IAS 17 prescribes initial direct costs incurred by lessor to be included in lease receivable amount in case of finance lease and in the carrying amount of the asset in case of operating lease and does not mandate any accounting policy related disclosure.	AS 19 requires initial direct cost incurred by lessor to be either charged off at the time of incurrence or to be amortized over the lease period and requires disclosure for counting policy relating thereto in the financial statements of lessor.
		IAS 17 requires assets given on operating leases to be presented in the Balance Sheet according to the nature of the asset.	AS 19 requires assets given on operating lease to be presented in Balance Sheet under Fixed Assets.
AS-20	**IAS 33**	**Earnings per Share (EPS):** IAS 33 requires separate disclosure of basis and diluted EPS for continuing operations and discontinued operations.	AS 20 does not requires any such separate computation or disclosure. AS 20 does not contain any such

		IAS 33 deals with computation of EPS in case of Share based payment transactions.	provision. AS 20 is silent on this aspect.
		IAS 33 prescribes treatment of written put options and forward purchase contracts in computing EPS.	
		IAS 33 requires changes in accounting policy to be given retrospective effect for computing EPS, which means EPS to be adjusted for prior periods presented.	AS 20 does not prescribe such treatment.
		IAS 23 does not require disclosure of EPS with and without extra-ordinary item	AS 20 requires EPS / DPS with and without extra-ordinary items to be disclosed separately.
		IAS 33 does not deal with the treatment of application money held pending allotment.	Under AS 20, application money held pending allotment should be included in the computation of diluted EPS.
		IAS 33 requires disclosure of anti-dilutive instruments even though they are ignored for the purpose of computing dilutive EPS.	AS 20 does not mandate such disclosure.
		IAS 33 does not require disclosure of normal face value of share	Disclosure of normal face value is required under AS 20.
		Consolidated Financial Statements (CFS):	
		Under IAS 27, it is mandatory to prepare CFS and an entity should prepare separate financial statements in addition to CFS only if local regulations so require.	Under AS 21, it is not mandatory to prepare CFS.
		Under IAS 27, exemption from preparation from CFS if certain conditions are fulfilled.	There is no such exemption under AS 21.
		Under IAS 27, a subsidiary cannot be excluded from consolidation under any circumstances.	Under AS 21, a subsidiary can be excluded from consolidation if (1) the subsidiary is acquired and held with an intention to dispose; or (2) the subsidiary operates under severe long term restrictions impairing its ability to transfer funds to parent.
		Under IAS 27 while determining whether entity has power to govern financial and operating policies of another entity, potential voting rights currently exercisable should be considered.	AS 21 does not provide for such eventuality.
AS-21	**IAS 21**	Under IAS 27, the definition of "control" is restrictive as it requires power to govern the financial and operating policies of the management of the enterprise	Under AS 21, the definition is wider as it refers to power to govern the financial and /or operating policies of the management.
		Use of uniform accounting policies for like transactions while preparing CFS is mandatory under IAS 27.	AS 21 gives exemption from following uniform accounting policies if the same is not practicable
		Under IAS 27, minority interest has to be disclosed within equity but separate from parent shareholders equity.	Under AS 21, minority interest has to be separately disclosed from liability and equity of parent shareholder.
		Under IAS 27, Goodwill / capital reserve on consolidation is computed on fair values of assets / liabilities	Under AS 21, Goodwill / capital reserve on consolidation is computed on the basis of carrying value of assets/ liabilities.
		Under IAS 27, 3 months' time gap is permitted between Balance Sheet dates of financial statements of subsidiary and parent.	Under AS 21, six months time gap is allowed.
		IAS 27 prescribes that deferred tax adjustment as per IAS 12 should be made in respect of timing difference arising out of elimination of unrealised profit.	AS 21 is silent on this aspect.
		IAS 27 requires drawing up of financial statements as on the date of acquisition for computing parent's	Under AS 21, for computing parent's portion of equity in a subsidiary at the date on which

		portion of equity in a subsidiary.	investment is made, the financial statements of immediately preceding period can be used as a basis of consolidation if it is impracticable to draw financial statement of the subsidiary as on the date of investment.
		IAS 27 does not require additional disclosure of list of all subsidiaries including the name, country of incorporation, proportion of ownership interest and if different, proportion of voting power held.	AS 21 requires additional disclosure of list of all subsidiaries including the name, country of incorporation, proportion of ownership interest and if different, proportion of voting power held.
		Accounting for Taxes on Income:	
AS-22	**IAS 12**	IAS 12 is based on Balance Sheet approach and therefore temporary difference (for e.g. Difference on any upward revaluation of assets, leads to creation of deferred tax liability) Under IAS 12, deferred tax liability for differences associated with investments in subsidiaries, associates and Joint Ventures may not be provided, if the parent is able to control the timing of reversal and it is probable that difference will not reverse in foreseeable future.	AS 22 is based on income statement approach and only timing differences leads to creation of deferred tax asset or liability. AS 22 provides no such exception as it does not deal with temporary differences
		Accounting for Associate in Consolidated Financial Statement:	
		Under IAS-28, Potential voting rights currently exercisable to be considered in assessing significant influence.	AS-23 is silent on this.
		As per IAS 28, difference between Balance sheet date of investor and associate can not be more than three month.	Under AS 23, no period is specified. Only consistency is mandated
		In case uniform accounting policies are not followed by investor & Investee, necessary adjustments have to be made while preparing consolidated financial statements of investor.	Under AS 23, if it is not practicable to make such adjustments, exemption is given, provided appropriate disclosures are made.
AS-23	**IAS 28**	While recognizing losses of associates / joint ventures under IAS 28, carrying amount of investment in equity and other long term interests to be considered	Under AS 23, losses are to be recognized to the extent of investment plus incurred obligations plus payments made towards guaranteed obligations.
		For identification of goodwill / capital reserve , IAS-28 envisages net fair value basis on acquisition	AS-23 prescribes historical cost basis on acquisition , for computation of goodwill.
		Under IAS 28 it is necessary to subject the investments in associates / joint ventures to the test of impairment.	If decline in value of investment in an associate is permanent, provision for diminution to be made. Impairment testing is not required under AS23.
		While defining Significant influence under IAS 28 participation in the financial and operating policy decisions is envisaged.	As per AS-23, participation in the financial and / or operating policy decisions is required
		Interim Financial Reporting:	
		Under IAS 34, minimum components of Interim Financial Report includes - Statement showing changes in Equity	No such disclosure is required under AS 25.
AS-25	**IAS 34**	Under IAS 34, in case of any change in accounting policy, figures of prior interim periods of the current financial year and comparable figures of corresponding previous periods to be restated.	AS 25 requires restatement of figures of prior interim periods of the current financial year only
		Under IAS 34, separate guidance is available for	

		treatment of Provision for Leave encashment, Interim Period Manufacturing Cost Variances, Foreign Currency Translation Gains and Losses.	AS 25 does not address these issues specifically.
		Intangible Assets:	
		There is no presumption under IAS 38 as regards useful life of an intangible asset	Under AS 26, there is a rebuttable presumption that the useful life of intangible assets will not exceed 10 years.
		IAS 38 does not exclude intangible assets arising in insurance enterprise from contract with policy holder	Intangible assets arising in insurance enterprise from contract with policyholder are excluded from scope of AS-26.
		Under IAS 38, intangible assets having "Indefinite useful life" cannot be amortized. Indefinite useful life means where, based on analysis, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflow for the entity. Indefinite is not equal to Infinite. Such assets should be tested for impairment at each Balance sheet date and separately disclosed	There is no such restriction in AS 26
AS 26	**IAS 38**	IAS 38 does not require any impairment testing if there are no indications of impairment.	AS 26 requires test of impairment to be applied even if there is no indication of that the asset is impaired for following assets: -Intangible asset not yet available for use -Intangible asset amortised over > 10 years.
		Under IAS 38, if Intangible Asset is 'held for sale' then amortization should be stopped.	There is no such stipulation under AS 26.
		Under IAS 38, R&D expenditure that relates to an in process R&D project acquired separately or in a business combination shall be accounted as per normal principles considering the research phase and development phase.	AS 26 is silent on this.
		Under IAS 38, Revaluation Model is allowed for accounting Intangible Asset provided active market exists.	AS 26 does not permit revaluation model.
		Financial Reporting of Interests in Joint Ventures:	
		Under IAS 31, when the investments are made by venture capital organization, mutual funds, unit trusts and similar entities when those investments are classified as held for trading and accounted for as per IAS 39.	There is no such provision under AS 27.
AS- 27	**IAS 31**	IAS 31 not to apply if parent is exempt from preparing CFS under IAS 27. Similar exemption for investor satisfying same conditions as parent.	There is no such specific provision under AS 27.
		IAS 31 permits both proportionate consolidation method and equity method for recognizing interest in a jointly controlled entity in CFS. Equity method prescribed in IAS 31 is similar to that prescribed in AS 23.	AS 27 permits only proportionate consolidation method.
		Impairment of Assets:	
AS-28	**IAS 36**	Under IAS 36, for determining net selling price, cost of disposal to be reduced only in cases where asset is intended to be disposed off.	AS 28: For determining net selling price, cost of disposal to be reduced from fair value of assets in all cases.
		IAS 36 does not permit reversal of impairment losses.	AS 28 permits reversal of impairment losses.
		IAS 36 suggests only bottom-up approach for	AS 28 allows both bottom up and

		allocation of goodwill in case of a cash-generating unit.	top down methods
		Provisions, Contingent Assets and Contingent Liabilities	
		IAS 37 permits discounting of provisions.	AS 29 does not permit any discounting
		IAS 37 requires that provisions for onerous contracts to be recognized	AS 29 does not mandate it.
		IAS 37 requires provisioning on the basis of construction obligation on restructuring.	AS 29 prohibits the same.
AS - 29	**IAS 37**	IAS 37 requires disclosure of Contingent Assets in Financial Statements.	AS 29 allows such disclosure only in approving authority report.
		IAS 37 provides certain basis and statistical methods to be followed for arriving at the best estimate of the expenditure for which provision is recognised.	AS 29 does not contain any such guidance and relies on judgement of management.
		IAS 37 defines only obligation but does not define present obligation and possible obligation.	AS 29 defines present obligation and possible obligation as well.

Baingani, V. and N. Agarwal [2005:*1052-1060*]

EVIDENCES ON CLUSTERS

For a longtime, the accounting researchers treaded their way deducing financial reporting theory. With their failure in attempting to deduce the theory, they adopted the approach of what accountants did in practice and this led to the emergence of GAAP. Meanwhile, they researched the effect of 'environment' on the development of accounting theory and much evidence concluded that environment did play a significant role, especially though the dominance of culture in accounting practices. At the same time, accounting researchers focused their attention on whether accounting practices had a tendency of similarities or uniformity across countries. In this direction, Zeff [1971] first demonstrated that accounting principles development did not come from specific scientific theory but from interactions among theory, practice and various social, economic and political influences. Upholding the proposition of Zeff, Belkaoui [1981:*17*] concludes that "The traditional approach has evolved into an eclectic and political approach." Remarking on these developments, Choi and Mueller [1984:*31*] observe: "Corollary to this major conclusion is Zeff's proposition (based on a substantial amount of research in the five countries concerned – Canada, England, Mexico, Scotland, and the United States) that the formulation of accounting principles cannot be achieved by an accounting profession alone but necessarily depends on the tacit or expressed support of the real "power centers" in an economy- for example, governmental agencies, industry associations, and investor groups and their representatives."

Keeping in view the harmonization as a long term objective, accounting researchers must have felt that financial reporting phenomenon peters down on the basis of "power centers" and these power centers might become a platform for global harmonization. These power centers are identified on the basis of similarity in accounting practices.

The initial work on classifying existing accounting practices is traceable to Mueller [1968]. In a completely subjective and nonhierarchical manner, he asserted that ten different "sets" of accounting practices could be discerned. He related the ten groupings to the respectively different business environments in which they operated. Each set was reportedly different from all others in at least one important respect. He identified the ten groups as given below: (1) United States/Canada/The Netherlands; (2) British Commonwealth (excluding Canada); (3) West Germany/Japan; (4) Continental Europe (excluding West Germany, the Netherlands, and Scandinavia); (5) Scandinavia; (6) Israel/Mexico; (7) South America; (8) Developing nations of the Near and Far East; (9) Africa (excluding South Africa); (10) Communist nations.

The AAA [1977] reported that the accounting patterns of the world may be classified according to "Zones of Influence." They based their conclusion on historical-cultural-socio economic sources that have influenced accounting principles underlying financial measurement and reporting in different countries and regions. The following five distinct zones of influence were distinguished: (1) British; (2) Franco-Spanish-Portuguese; (3) Germanic/Dutch; (4) United States; and (5) Communistic.

Nobes [1980:*16*] suggested a classification system that added hierarchical integrity to earlier efforts. Continuing Nobes's efforts, Nobes and Parker [1981:*212*] captured the essence of classification in these words: "[The classification] contains a hierarchy and tries to show not only that two particular countries are in different categories but how close or distant these categories are. Terminology has been borrowed from biology. As examples, Australian accounting is shown, by the "family" it belongs to, to be closer to U.K. accounting than it is to Netherlands accounting or to Canadian accounting. However, it is closer to any of these than to French accounting, which is in a different "class" entirely. U.K. and Irish accounting are so similar that these individual systems could be said to be twins."

A few important studies on classification of accounting systems may be cited. DaCosta et. al., [1978:*79*] and Frank [1979:*596*] grouped the accounting systems in two groups and four groups respectively. The study by Nair and Frank [1980:*426-50*] classified accounting systems into four groups and into seven groups based on measurement groups and disclosure groups respectively. However, it may be observed that the classifications are not similar in the sense that a researcher's grouping of one country is classified in another grouping leading to inconsistent results in the empirical studies.

Observing the limitations and inconsistencies of these classification studies, d'Arcy [2001] used multidimensional scaling (MDS) to group the selected leading countries based on their accounting practices. The MDS had a range '1' or '0'. The conclusions of this study are directly quoted below:[pp: 345-346].

"The most homogeneous results can be found for the European accounting systems. Essentially, Germany, Australia, France and Belgium can be interpreted as the core of the continental European cluster. So far, the European accounting directives have led to more homogeneity at the regulation level. But there are some

European systems like Sweden or Spain that tend to make a break from European accounting traditions. But even if they adopt accounting methods that better serve the information needs of capital market participants they do not merge with the North American cluster. Rather, they find new combinations of accounting methods.

"Against this background we are immediately aware that it is not at all possible to find an Anglo American cluster. However a relative heterogeneous North-American cluster including the IASC can be identified. The picture of an Anglo-American accounting model that is subsumed specially by opponents of the harmonization process cannot be established. But many systems that normally come under the label "Anglo-American" show the tendency to concentrate on more capital-marked-orientated accounting methods than the European core countries. The conjecture arises that there are no simple typical accounting methods that stand for the capital marked orientation of an accounting system. In fact, another analysis applying the TRANSACC reference matrix as a database shows that according to the degree of determination of accounting methods an Anglo-American cluster can be identified [d'Arcy, 2000]. Consequently, not only specific accounting methods but also the fact that methods are requested or forbidden versus the possibility of accounting method choice seems to be relevant.

"However, the analysis demonstrates that the adoption of IAS or US-GAAP as alternative accounting rules for European countries implies a substantial change for the accounting users. It is notable that particularly the European core countries allow the alternative application of IAS or US-GAAP whereas "Anglo-American" systems like the Australian of British do not accept alternative accounting principles [Knorr, 1998]." The above analysis of accounting practices country groupings is only a glimpse of the controversial debate on international classifications. We may cite other innumerable studies to highlight the confusions in classifications. Table 2.3 shows the classification attempts as reported by d'Arcy [2001].

TABLE 2.3
EMPIRICAL STUDIES ON CLUSTERS

Study	Study Topic	Classification Criterion	Results, Cluster Definition
1	2	3	4
Hatfield [1911] USA	Describing accounting differences between UK/FRA/GER/USA	Financial reporting practices	USA, UK, Continental European (Germany, France)
Seidler [1967] USA	Develop and present coherent patterns of international variation	Spheres on influence based on economic, political and legal factor	British, US, Continental European
Mueller [1967] USA	Find fundamental patterns of accounting development as a framework for analysis	Importance of economic, governmental, business factors in the development of accounting systems	Patterns of development: macro-economic (SWE), microeconomic (NETI-1), independent discipline (UK, US), uniform (GIR)
Mueller [1968] USA	Classification based on national business environments	States of economic development, of business complexity, shades of political persuasion, reliance on some particular system of law	Sets of business environments, e.g. US/CAN/NETH, British Commonwealth (without CAN), GER/JAP
Previts [1975] USA	Classification according to positive, normative and historical factors	Environmental conditions, future influence of standard setters, historical circumstances	Anglo-American, Continental
AAA [1977] USA	Find international zones of influence, propose a morphology	Eight parameters for influencing factors	British, FRA/ES/POR, GER/NETH, communistic
Barrett [1977] USA	Empirically test whether the extent of financial disclosure in foreign annual reports is significantly different from that found in US reports	Disclosure practices (17 items of information drawn from annual reports of 103 firms 1963-1972)	US/UK, JAP/SWE/NETH/GER, FRA (others not classified)
Da Costa et. al., Canada [1978]	Test the posited existence of groupings of accounting models, search for environmental factors	Accounting practices (100 out of 233)	UK (former British empire versus US model)
Frank [1979] USA	Examine the extent to which different patterns of accounting concepts and practices exist and relate differences to economic and environmental factors	Accounting practices (233)	British-Commonwealth, Latin American, Continental European, US-model, indirect support of environmental determinism theory
Nair and Frank [1980] USA	Examine differences in classifications whether measurement or disclosure practices are used the association with underlying environmental variables	Accounting practices differentiated in measurement (mp 147/162)+disclosure practices (dp = 86/102) environmental factors	Mp 1975: British Commonwealth, Latin American South European, Northern and Central European, US model, Chile; support of environmental determinism theory for mp only

Contd.,

Nobes and Matatko [1980] UK	Test the validity of the DBL 1978 classification with varying number of	Accounting practices (233)	Support British model only

	factors		
Nair [1982] USA	Develop empirical guidelines for comparing financial accounting data + replicate earlier study by Nair/Frank for examine the stability of country groupings over time	Accounting practices differentiated in measurement practices (mp) and disclosure practices (dp) (267)	Mp: British-Commonwealth, Central America + Southern Europe, Central Europe + Scandinavia, US, South American, African, African, India
Goodrich [1982] UK	Attempt to delineate factor groupings based on PW-data	Accounting principles and policies (26)	Prototypes: US, Switzerland, UK, Brazil, Jersey
Doupnik [1987] USA	Grouping countries according to their respective degrees of commonality on two points of time in order to measure the harmonization efforts since the establishment of the IASC in 1973	Accounting practices (70)	For 83 analysis: British Commonwealth, South American/South European, JAP/Panama/US, CAN/MEX, Scandinavia, GER; differences have decreased and quality has improved.
Puxty et. al., [1987]	Proposes a general model for different models of accounting regulation	Accounting standard setting	Purely political approach (GER,FRA), private professional approach (Australia, CAN, UK), public/private mixed approach (US), broadly mixed approach (NETH)
Daley and Mueller [1989] USA	Typify the standard setting process according to the role of private and governmental institutions in the development and enforcement of accounting	Accounting standard setting	Purely political approach (GER, FRA), private professional approach (Australia, CAN, UK), public/private mixed approach (US), broadly mixed approach (NETH)
Nobes [1983-1994] UK	Test the validity of proposed hierarchical classification with a self-generated morphology and PW-data	Two explanatory variables + seven measurement practices, accounting practices (267)	Support hypotheses (but few deviations)
Nobes [1992 UK	Find classification of standard setting processes and institutions	Accounting standard setting	2-cluster solution: non-government creation (US, Australia, CAN, UK, NETH, New Zealand), government creation (GFR, JAP, FRA)

Contd.,

AlNjjar [1986] USA	Test the validity of a classification proposed by Nobes + own hypotheses about an international tendency toward more standardization and increasing governmental jurisdiction	Five casual factors, standardization elements	Support hypotheses (but few deviations)

Gray [1988] UK	Explore the extent to which international differences may be explained by differences in cultural factors, link accounting values and culture area classifications	Cultural value dimensions	Adopt Hofstede's culture area classification
Shoental [1989] USA	Determine whether the education factors is an essential element in clustering, test for UK and US only	Accounting competencies (63)	Support hypothesis for UK and US
Cooke and Wallace [1990] UK	Test whether the level of corporate financial disclosure regulation in developed countries is likely to be determined by more internal factors, whereas that of developing countries by more external factors	Disclosure regulation	Support hypotheses, UK/US "leader" in financial disclosure regulation
Salter and Doupnik [1992] USA	Test the relationship between legal system groupings (David/Briefly) and accounting practices	Accounting practices (100)	Support hypothesis, substantial differences in accounting systems can be explained by reference to a country's laws (code versus case law)
Doupnik and Salter [1993]USA	Empirically classify current financial reporting systems + test the validity of a classification proposed by Nobes [1983], Berry [1987]	Accounting practices (100)	Confirm Nobe's classification (few deviations), support existence of a Latin American group suggested by Berry
Doupnick and Salter [1995] USA	Test the relationship between environmental factors and accounting practices based on classifications	Accounting practices (100), socio-economic factors	Does not support hypothesis,
D'Arcy [2001] Germany	Find a hierarchical classification based on accounting rules	Accounting rules	For 4 – cluster solution European, Northern-American, JAP/SWE/ESP, Australia

Source: d'Arcy [2001]. Table 2 (edited) pp. *337-340*.

It is important to note that the latest classifications by d'Arcy are not essentially the ultimate conclusion on classifications of accounting practices. nevertheless, Jeffrey and Radebaugh [1985] state an understanding of certain groupings can be useful in determining how different one country's system is likely to be from another's and, hence, what degree of causation and further study is advisable when analyzing accounting information generated in another country. There is a direct relationship between research on international accounting harmonization process and classification of accounting practices. d'Arcy [2001:*327*] observed that it is possible to identify two groups who use classification in their argumentation for or against international accounting harmonization. The first group favors the traditional continental European system and the second group prefers Anglo-American accounting system.

THE CONVERGENCE PROCESS

It seems that the accounting world is moving away from cluster studies to convergence process. In this regard, Vikamse [2005] remarks: "As the world is shrinking into a global village and as economic borders are vanishing and investment is freely flowing across countries, it becomes important that accounting standards applied in preparation of financial statements are similar so as to provide uniform information to all users of these statements." He adds that the convergence of Accounting Standards is a foregone conclusion and the issues, which arise in convergence, need to be discussed at length. Convergence refers to the process of integrating the national standards and the regional standards with the IFRS. Kellas [2005], while elaborating on the benefits of convergence with the international standards, observes if common standards are applied across the world, then auditing becomes easier not only for the auditing firms, international investors, international regulators but also for educators and learners.

The move towards convergence has been spearheaded by the FASB and the IASB and this trend is based on what are known as 'power centers' advocated by Zeff in 1971 or 'zones of influence' advocated by the AAA in 1977. In this regard Tweedi [2005] observes "If we are to achieve truly global standards and all the benefits that they will bring, accounting convergence must necessarily involve the United States, which accounts for nearly half of the world's total market capitalization." Accordingly, the IASB and FASB have taken a flexible approach to converge and they are focusing on issuing standards of the highest quality possible, regardless of where the principles underlying them originate. Pactor [2005:*73*] also observes: "National standards in most countries of the world have been based either on IFRSs or US GAAP to a large extent. Despite the tendencies of national standard setters to make small or large changes to those standards, they cannot and do not ignore those two substantial and advanced bodies of literature in developing their own national standards. Therefore, a sensible way to achieve a single set of global accounting standards in a reasonable time span is to work towards convergence of IFRSs and US GAAP-in turn causing a 'trickle down effect' in those countries that continue to maintain their national GAAPs."

"The convergence process between the two accounting standard setters, the FASB and the IASB, was officially initiated in September 2002 when the Memorandum of Understanding, "The Norwalk Agreement", was signed. In the agreement, each Board has acknowledged its commitment to the development of high quality, compatible accounting standards that can be used for both domestic and cross-border financial reporting. The agreement symbolizes a major step towards convergence of US and international accounting standards. In the agreement, both FASB and IASB pledged to use their best efforts: (a) to make their existing financial reporting standards fully compatible as soon as is practicable and (b) to co-ordinate their future work programs to ensure that once achieved, compatibility is maintained.

At their meetings in April and October 2005, the FASB and the IASB reaffirmed their commitment to the convergence of US GAAP and IFRSs. A common set of high quality global standards remains the long-term strategic priority of both the FASB and the IASB. The FASB and the IASB recognize the relevance of the roadmap for the removal of the need for the reconciliation requirement for non-US companies that use IFRSs and are registered in the United States. It has been noted that the removal of this reconciliation requirement would depend on, among other things, the effective implementation of IFRSs in financial statements across companies and jurisdictions, and measurable progress in addressing priority issues on the IASB-FASB convergence program. Therefore, the ability to meet the objective set out by the roadmap depends upon the efforts and actions of many parties-including companies, auditors, investors, standard-setters and regulators.

The FASB and the IASB recognize that their contribution to achieving the objective regarding reconciliation requirements is continued and measurable progress on the FASB-IASB convergence program. Both boards have affirmed their commitment to making such progress. The discussions by the FASB and the IASB regarding their approach to the convergence program indicated agreement on the following guidelines: (a) Convergence of accounting standards can best be achieved through the development of high quality, common standards over time, (b) Trying to eliminate the differences between two standards that are in need of significant improvement is not the best use of the FASB's and IASB's resources-instead, a new common standard should be developed that improves the financial information reported to investors, and (c) Serving the needs of investors means that the boards should seek to converge by replacing weaker standards with stronger standards.

The Sarbanes-Oxley Act of 2002 provided some impetus and support for the Norwalk agreement. Section 108 of the Act permits the SEC to recognize standards established by a private sector accounting standard-setter (i.e., FASB) provided that the standard-setter considers "the extent to which international convergence on high quality accounting standards is necessary or appropriate in the public interest and for the protection of investors". Section 109 of the Act provides US Government funding to the SEC-recognized standard setter [Pactor: 2005, *73*].

The IASB and the FASB have various joint initiatives to accomplish the convergence goal and these initiatives are labeled as comparability project also. The two Boards have agreed on two main projects in order to achieve comparability: (a) Short-term convergence, and (b) Joint projects.

The short-term convergence projects are aimed to eliminate a set of selected differences between US GAAP and IAS/IFRS. The short-term projects are expected to result in standards that will lead to convergence in certain areas. The scope of the short-term convergence project is limited to those differences between US GAAP and IAS/IFRS though which convergence appears to be achievable in the short-term perspective. The Boards are currently working toward eliminating the existing differences and aiming to achieve this convergence by selecting between existing US GAAP and IAS/IFRS. By 2008, the goal is to reach a conclusion about whether major differences in the following few focused areas shown in Table 2.5 should be eliminated through one or more short-term standard-setting projects and, if so complete or substantially complete work in those areas.

TABLE 2.4
TOPICS FOR SHORT-TERM CONVERGENCE

To be examined by the FASB	To be examined by the IASB
Fair value option*	Borrowing costs
Impairment (Jointly with the IASB)	Impairment (jointly with the FASB)
Income tax (jointly with the IASB)	Income tax (jointly with the FASB)
Investment properties**	Government grants
Research and development	Joint ventures
Subsequent events	Segment reporting
FASB Note: *On the active agenda at 1 July 205 ** To be considered by the FASB as part of the fair value option project	*IASB Note*: Topics are part of or to be added to the IASB's short-term convergence project, which is already on the agenda.

Source: http://wwwfasb.org

Apart from the short-term convergence projects, the Boards are working on several joint projects on major accounting topics and are developing a coordinated agenda for continuing the convergence effort. This is to identify areas where accounting has failed to keep pace with new developments in the market place or where assets and liabilities have been kept off the balance sheet. The aims of these projects are to develop common high quality solutions to these accounting problems.

The FASB and IASB have expressed the progress they expect to achieve on their convergence project in the form of a list of 11 areas of focus after consultations with representatives of the European Commission and the SEC staff and based on priorities and resources. These projects will occur in the context of the ongoing joint work of the FASB and the IASB on their respective Conceptual Frameworks. As part of their Conceptual Framework project, the FASB and the IASB will be addressing issues relating to the range of measurement attributes to enable a public discussion on these topics to begin in 2006. The boards have set the following goals for 2008 for convergence topics already on either active agendas or on research programs:

TABLE 2.5
TOPICS FOR CONVERGENCE JOINT PROJECTS

Topics already on an Active Agenda				
Convergence topic		**Current status on the FASB Agenda**	**Current status on the IASB Agenda**	**Progress expected to be achieved by 2008**
1.	Business combinations	On agenda deliberations in process	On agenda deliberations in process	To have issued converged standards (projected for2007), the contents and effective dates of

				which to be determined after taking full account of comments received in response to the Exposure Drafts.
2.	Consolidations	On agenda currently inactive	On agenda -no publication yet	To implement work aimed at the completed development of converged standards as a matter of high priority.
3.	Fair value measurement guidance	Completed standard expected in the first half of 2006	On agenda deliberations in process	To have issued converged guidance aimed at providing consistency in the application of existing fir value requirements.
4.	Liabilities and equity distinctions	On agenda -no publication yet	On agenda (will follow FASB's lead)	To have issued one or more due process documents relating to a proposed standard.
5.	Performance reporting	On agenda- no publication yet	Exposure draft on a first phase	To have issued one or more due process documents on the full range of topics in this project.
6.	Postretirement benefits (including pensions)	On agenda- deliberations underway on the first phase of multi-phase project	Not yet on the agenda	To have issued one or more due process documents relating to a proposed standard.
7.	Revenue recognition	On agenda-no publication yet	On agenda-no publication yet	To have issued one or more due process documents relating to a proposed comprehensive standard.

Topics already being researched, but not yet on an Active Agenda				
Convergence topic		**Current status on the FASB Agenda**	**Current status on the IASB Agenda**	**Progress expected to be achieved by 2008**
1.	De-recognition	Currently in the pre-agenda research phase	On research agenda	To have issued a due process document relating to the results of staff research effort.
2.	Financial instruments (replacement of existing standards)	On research agenda and working group established	On research agenda and working group established	To have issued one or more due process documents relating to the accounting for financial instruments.
3	Intangible assets	Not yet on agenda	On research agenda (led by a national standard-setter)	To have considered the results of the IASB's research project and made a decisions about the scope and timing of a potential agenda project.
4.	Leases	Pre-agenda research underway	On research agenda (led by a national standard-setter)	To have considered and made a decision about the scope and timing of a potential agenda project.

Source: http://www.fasb.org

The objective of the convergence goals set out above is to provide a time frame for convergence efforts in the context of both the objective of removing the need for IFRS reconciliation requirements by 2009 and the existing agendas of the FASB and the IASB. The FASB and the IASB will follow their normal due process when adding items in the agenda.

In setting out the projects for both the short-term convergence topics and the major joint topics, the FASB and the IASB recognize that with respect to its foreign registrants, the SEC staff will undertake an analysis of their 2005 IFRS financial statements across companies and jurisdictions. This analysis may reveal the need for additional standard-setting actions by one of the boards or both.

In the words of Tweedi [2006], "We are at a key juncture in the development of international accounting standards. Nearly, 100 countries are using IFRSs and are working hard to ensure their consistent application. The other major economies of the world, Japan and the United States, and the fastest growing emerging economies, China and India, are converging with IFRSs." This evidences that majority of the countries in the world are in favor of convergence. Table 2.7 shows the countries, which require IFRSs and converging with IFRSs.

TABLE 2.6
COUNTRIES THAT USE IFRS AND ARE CONVERGING

	Europe/Central Asia	Americas	Asia-Pacific	Africa/Middle East
Requires IFRS	Armenia Austria, Bangladesh Belgium, Bulgaria Croatia, Cyprus, Czech, Republic, Denmark, Estonia, Finland, France, Georgia, Germany, Greece, Hungary, Ireland, Italy, Kingston, Latvia, Lithuania, Luxembourg, Macedonia, Malta, Netherlands, Norway, Portugal, Romania, Russia, Slovakia, Slovenia, Spain, Sweden, Switzerland, Tajikistan, Ukraine, United kingdom	Bahamas, Barbados, Costa Rica, Dominican Republic, Ecuador, Guyana, Haiti, Honduras, Jamaica, Panama, Papua New Guinea, Peru, Trinidad, & Tobago	Australia, Brunei, Nepal, Singapore, Taiwan,	Egypt, Jordan, Kenya, Kuwait, Malawi, Mauritius, Oman, Tunisia
Converging With IFRS	Moldova, Uzbekistan	Argentina, Brazil, Canada, Cayman Islands, Chile, Guatemala, Mexico, Uruguay, Venezuela, United States	New Zealand, China/Hong Kong, India, Indonesia, Japan, South Korea, Malaysia, Philippines, Thai land	Iran, Israel, Pakistan, South Africa, Zimbabwe

Source: The Chartered Accountant, February 2005, p. *1049*.

Across the world from Asia to Latin America, national governments, regulators and accountancy professionals are taking active steps to consider how their national accounting rules differ from IFRS, to reduce those differences and also to converge with IFRS. These processes will in many countries lead to a significant improvement in financial reporting transparency, but it will take time. Convergence of accounting standards will not be achieved without substantial co-operation among governments, the business communities and the profession accountancy bodies. Improvements in accounting practice will also require the development of educational, professional and regulatory infrastructures. Adoption of new standards without adequate preparation may be more detrimental than beneficial.

CONCLUSION

Since financial reporting is the means of information dissemination, to be comparable, all information is required to refer to facts of the same kind. The annual report, for example, provides information on the financial position of a company and its results. Although the general purpose is similar in most countries or companies, many differences occur resulting from different environmental and cultural influences in the individual countries and/or companies. This hampers the very purpose of comparability of the results between companies. The solutions identified to resolve this problem is accounting standards. This facilitates to pursue uniform accounting systems by companies. At present, the efforts to bring uniform financial reporting have been made at three levels, international level, regional level and country specific level. The salient feature of these levels is that there are substantial differences in measurement process as well as disclosure process. Historically, the accounting researchers felt that there was some uniformity in financial reporting based on the concept of power centers. This led to many studies conducted to identify the clusters of accounting practices but the researchers failed to identify the clusters with much clarity. Meanwhile, the accounting researchers led by IASB (formerly IASC) harped on the strategy of international accounting standards to be emulated by different countries. Even then, the differences between IAS and national accounting standards have differed in many respects. The new experiment on uniform financial reporting in terms of harmonization has been taken up by making efforts towards converging US GAAP with IFRS and the results are yet to be assessed. To conclude, the accounting research has moved away from GAAP to standards and now it is in the crossroads of convergence.