



GLOBAL SERVICE/ INDUSTRY

Corporate Governance in India - Trends in Financial Reporting and Auditing Practices

AUDIT / TAX / ADVISORY / LINE OF BUSINESS

Developments in Financial Reporting – last decade

◆ Accounting Standards given statutory recognition

- ICAI has been issuing accounting standards for companies in India. These Accounting Standards are prepared and finalised by Accounting Standards Board at ICAI.
- Recently, the Central Government has issued the Companies (Accounting Standards) Rules, 2006 in consultation with National Advisory Committee on Accounting Standards (NACAS). These Rules came into force on 7 December 2006. These rules prescribe accounting standards that have been developed by the ICAI but with some structural and other modifications e.g.,
 - Classification of companies have been changed from Level I, II, III to two categories – Small and medium sized company and other companies (large companies)
 - Accounting standard Interpretations issued by the ICAI have been incorporated in the standards as ‘Explanation’ under the relevant paragraphs.

◆ Directors’ Responsibility

- Directors to specifically state in Board Report that accounting standards have been complied with
- Also that accounting policies, accounting judgements and estimates are reasonable and prudent.

Developments in Financial Reporting – last decade (Contd.)

◆ SEBI introduced and gradually improved quarterly financial reporting by listed companies

- Timely reporting of quarterly results made such results a significant benchmark for decisions by users including investors
- Accounting systems of companies saw noticeable improvements
- Decision making by Boards of companies became oriented towards more current financial results
- Practice of consolidated financial statements was given an impetus. Users also started analysing the same.

Present system of financial reporting – still deficient

◆ Limitations of Schedule VI

- No major conceptual revision since 1956
- Current – non current distinction blurred (e.g., long term loans given get shown as part of net current assets)
- Somewhat rigid – unable to properly reflect new financial instruments/knowledge based industries/changes in business environment

◆ **When laws and decisions of the courts are in conflict with accounting standards then law/court decisions prevail – while compliance with accounting standards should be a precondition e.g. merger accounting**

◆ **Indian accounting standards need major improvements**

Financial Reporting Standards - Next Decade

◆ Adoption of International Financial Reporting Standards by 2011 – ICAI Initiative

Why adoption of IFRSs is important – they are being recognised as global standards and more than 100 countries now require or allow the use of IFRS, and many other countries are replacing their national standards with IFRSs.

IFRS Convergence

- ◆ **Areas which will be impacted the most**
 - Business combinations
 - Consolidation
 - Financial Instruments
 - Redeemable Preference Shares
 - Convertible debentures
 - Fair valuation of long term loans
 - Valuation of investments
 - Treatment of prior period items and accounting policy changes
 - Format of disclosure: Complete overhaul of Schedule VI in line with IFRS or disclosures linked with IFRS with no prescriptive, rigid format in law.

IFRS Convergence: Key Challenges

- ◆ **Amendment in Companies Act**
- ◆ **Amendment in requirements of regulators**
- ◆ **Amendment in taxation laws**
- ◆ **Courts/tribunals not to approve proposals which do not comply with accounting standards**
- ◆ **Conceptual development of techniques of fair valuation**
- ◆ **Creation of IFRS resources**

Auditing – the next decade

- ◆ **With more complex business model and ERP being implemented by most organizations, technology will play a greater role in audit.**
- ◆ **As India would be adopting IFRS, which is about fair value accounting, there will be greater use of judgment and estimates for which valuation skills will be required.**
- ◆ **Growing importance of audit committees.**
- ◆ **More effective quality review procedures.**
- ◆ **Growth in the size/resources/specialised knowledge bases of audit firms.**
- ◆ **Development of autonomous self regulatory overseeing institutional mechanisms**