A COMPARATIVE STUDY ON REPORTING OF INVESTMENT ACTIVITIES UNDER INDIAN GAAP AND IND AS

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ABSTRACT
The Ministry of Corporate Affairs, Govt. of India has notified 39 Ind-AS converged with IFRS which are applicable in a phased manner starting from the financial year 2016-17. Ind AS is entirely a new concept for Indian companies and so also its consequences of implementation. There are a large number of differences in existing GAAP and the new Ind AS which will impact companies’ performance indicators significantly. Several studies conducted by research firms like KPMG, PWC, Ernst and Young etc. showed that the reported net profit and net worth of the companies were largely impacted on account of adoption of Ind AS. Moreover, the main areas having the maximum impact on the above mentioned performance indicators include investment accounting among others. The present study is an attempt to bring out the major areas of differences in reporting practices with reference to investment activities under IGAAP and Ind AS.

Keywords: converged, IFRS, net profit, net worth

INTRODUCTION
The need to speak a uniform accounting language over the world has resulted in the development of a new concept in accounting known as IFRS. International Financial Reporting Standards (IFRS) are set of high quality, transparent and enforceable global accounting standards which have attracted attention of the accountants all over the world in the recent time. This is due to its growing popularity and application as a result of globalization of business and internationalization of accounting practices which compelled the countries to adopt the same as a means to harmonize the whole concept of accounting. Earlier to the evolution of this concept, every country used to follow their local GAAPs and accounting standards while preparing and presenting their financial statements. As business started spreading beyond the national boundary of countries, it forced the accounting world to develop a uniform accounting language which is understood by all the stakeholders across borders and as a consequence IFRS evolved. These are designed as a common global language for business affairs so that company accounts are comparable and understandable across international borders. The term IFRS has both a narrow and a broader meaning. Narrowly, IFRS refers to the new numbered series of pronouncements that the International Accounting Standards Board (IASB) has been issuing, as distinct from the International Accounting Standards (IASs) issued by its predecessor. More broadly, IFRS refers to the entire body of IFRS pronouncements including standards and interpretations.
approved by IASB and IASs and SIC interpretations approved by the predecessor International Accounting Standards Committee (IASC). Thus IFRS comprises-

1. International Financial Reporting Standards (IFRSs) issued by IASB
2. International Accounting Standards (IASs) issued by IASC
3. Interpretations developed by the IFRS Interpretations Committee (IFRICs) and
4. Former IASC Standing Interpretations Committee (SICs)

In the recent years, IFRS has been a widely debated issue all over the world. The major breakthrough came in the year 2002 when the European Union passed legislation for adoption of the same. The legislation came into effect in 2005 which resulted in mandatory adoption of IFRS by more than 8000 firms in 30 countries belonging to EU including France, Germany, United Kingdom, Italy, Spain and so on. Thereafter, the world is moving rapidly towards the adoption of IFRS in preparation and presentation of financial statements. At present, almost 123 countries have joined the process; some fully adopting the original IFRS and others converging their local GAAPs to IFRS.

OBJECTIVES OF THE STUDY

The main objectives of the present study may be summarized as follows:

1. To discuss the present status of implementation of Ind AS in India.
2. To make a comparative study of reporting of investing activities under IGAAP and IND AS.

REVIEW OF LITERATURE

Swamynathan and Sindhu (2011) conducted a study on the effects of convergence to IFRS and found that the net income position in IFRS reporting and Indian GAAP is not much varied. But there are differences in the total liability and equity position which is mainly because of re-classification between equity and total liability.

Rani and Gupta (2014) conducted a study on IFRS convergence and applicability in India and found that lack of awareness about international accounting practices, proper training to the accounting professionals, amendments to the existing taxation laws etc. are the major challenges faced by India for convergence with IFRS.

Kamath and Desai (2014), made an empirical analysis on eight companies in India already adopting IFRS and found that there is an improvement in investing and operating activities due to IFRS adoption.

Barth et al. (2008) confirmed that firms following IFRS evidence less earnings management, more timely loss recognition and more relevance of accounting numbers. The study also found out that the firms following IFRS experienced an improvement in accounting quality between the pre adoption and post adoption period.

RESEARCH METHODOLOGY

The study is basically qualitative in nature and does not use any quantitative tool to analyze data. It has been conducted mainly on the basis of literature survey and secondary information. Various journals, newspapers, magazines and books have been referred to in writing this paper. Moreover, information published in the various websites including the official websites of ministry of corporate affairs and the ICAI relating to various accounting and reporting issues in India have been used extensively for the study.
ANALYSIS AND DISCUSSION

Present status of implementation of Ind As

Accounting standards in India are issued by the Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India (ICAI) and these are largely based on IFRS. However, because of its sensitive local conditions including conflicting legal and economic environment, India has not been able to keep pace with the developments and amendments made in IFRS. In the year 2006, the ICAI started to set accounting standards in parity with IFRS. As a result the existing accounting standards announced and issued after AS-14 (Accounting for Amalgamation) are almost in line with IFRS.

In 2009, India made a commitment towards the convergence of Indian accounting standards with International Financial Reporting Standards (Called Ind-AS) at the G-20 summit held at Pittsburgh, USA. Following this, the Ministry of Corporate Affairs came out with a road map for the implementation of Indian Accounting Standards (Ind-AS) converged with IFRS starting April 2011. This was for all Indian companies other than banking, insurance and non-banking finance companies. Because of some integration issues and political compulsions we could not kick start the Ind-AS at that time. In his first budget speech in July 2014, our present Finance Minister proposed that Ind-AS would be a reality soon.

Following the proposal made by the finance minister, the Ministry of Corporate Affairs, Government of India started notifying Ind-AS (approved by NACAS) to be implemented in a phased manner. Till now, the MCA has notified 39 Ind-AS which are applicable in India in the following manner-

. Entities could voluntarily adopt Ind-AS from the accounting year 2015-16.
. Mandatory adoption of Ind-AS is to be exercised in a phased manner as shown below
  1. All listed and unlisted companies having net worth of ₹ 500 crores or more will follow Ind-AS from the accounting year 2016-17
  2. All listed companies along with unlisted companies having net worth of more than ₹ 250 crores will follow Ind-AS from the accounting year 2017-18
  3. Unlisted companies having net worth of less than ₹ 250 crores will follow Ind-AS from the accounting year 2018-19 onwards.

Whenever a company gets covered under the roadmap, Ind AS becomes mandatory, its holding, subsidiary, associate and joint venture companies will also have to adopt Ind AS (irrespective of their net worth). For the purpose of computing the net worth, reference should be made to the definition under the Companies Act, 2013. In accordance with section 2 (57) of the Companies Act, 2013, net worth is computed as “Net worth means the aggregate value of the paid-up share capital and all reserves created out of the profits and securities premium account, after deducting the aggregate value of the accumulated losses, deferred expenditure and miscellaneous expenditure not written off, as per the audited balance sheet, but does not include reserves created out of revaluation of assets, writing-back of depreciation and amalgamation.”

Banking companies, insurance companies, NBFCs and SMEs are exempted from mandatory adoption of Ind-AS for the time being. However, this is evident from the recent announcements made by the RBI and IRDA that banking and insurance companies are also going to join the bandwagon very soon.

REPORTING OF INVESTING ACTIVITIES UNDER IGAAP AND Ind AS

Meaning of investment activities

An investment is an asset or item that is purchased with the hope that it will generate income or will appreciate in the future. In an economic sense, an investment is the purchase of goods that are not consumed today but are used in the future to create wealth. In finance, an investment is a monetary asset purchased with the idea that the asset will provide income in the future or will be sold at a higher
price for a profit. For accounting purpose, investment can be classified as investment in physical assets like land and buildings, gold etc and investment in financial assets like shares, debentures, bonds and similar other financial instruments issued by various companies. The scope of the present study is limited to the extent of reporting of those investment activities which are covered by AS13 under IGAAP and Ind AS 109 and Ind AS 40 under Ind AS regime.

Accounting Standard 13 (AS 13) deals with accounting for investments in the financial statements of enterprises and related disclosure requirements. The standard comes in to effect for financial statements covering periods commencing on or after April1, 1995. AS 13 covers accounting for investment in physical assets like land and buildings, gold etc. as well as financial assets like shares, debentures, bonds and similar other financial instruments issued by corporate houses.

Under Ind AS regime, accounting for investment activities are split in to standards. Accounting for investment in physical assets are covered by Ind AS 40 on Investment Property leaving investment in financial assets to the better care of Ind AS 109 on Financial Instruments. Moreover, Ind AS 109 is concerned with recognition and measurement of financial instruments while presentation and disclosures are covered by Ind AS 32 and Ind AS 107 respectively.

CLASSIFICATION OF INVESTMENTS

Under AS13, Investments are classified as current investments and long-term investments. Current investments are those which are intended to be sold within one accounting year or which are to be realized within one year. On the other hand, investments other than current investments are called long-term investments. Thus, the investments which are not to be sold within one year are long-term investments as per AS 13. However, Revised schedule VI of the Companies Act, 1956 which came in to effect from 1st April, 2011, requires classification of investments as non-current investment and current investment. Though, the revised schedule VI clarifies that the accounting standard would prevail over itself in case of any inconsistency between the two, it is pertinent to note that AS 13 does not lay down presentation norms, though it requires disclosures to be made for current and long-term investments.

Under Ind AS 109, investments are classified as investment measured at amortized cost, investment measured at fair value through profit and loss (FVTPL) and investments measured at fair value through other comprehensive income (FVTOCI).

Recognition

Under existing GAAP, both current and long term investments are initially recognized at cost price. While calculating the cost price of such investments, transaction costs such as brokerage fees, legal expenses are added to the purchase price of the investment.

Under Ind-AS regime, transaction costs do not form part of the total cost for FVTPL investments and are directly transferred to the profit and loss account.

Measurement

Under AS13, Current investments are measured at cost price or market price whichever is lower either on an individual investment basis or by category of investment but not on overall basis.

Shares, debentures and other securities held for sale in the ordinary course of business are treated as stock in trade and accordingly are measured applying AS 2 (Valuation of Inventory). However, it is pertinent to note that AS 2 also uses the same formula for valuation of inventory, i.e. lower of cost or market price.

Long-term investments are always measured at cost. However, provisions are made for diminution, other than temporary, in the value of such investment.

Investment properties accounted as long-term investments and as such these are measured at cost after maintaining provision for permanent decline in the value of such property.
Under Ind AS 109, an investment in financial asset can be measured at amortized cost if both the Cash Flow Test and Business Model Test are satisfied. The Cash Flow Test says that the asset gives rise to cash flows which are solely the payment of interest and principal. The Business Model Test says that the asset is held in order to collect the contractual cash flows till maturity. It is worth mentioning that only debt instruments can be measured at amortized cost. Equity instruments do not qualify the business model test since they do not have any maturity, these cannot be measured at amortized cost. After initial recognition at fair value plus transaction costs, these investments are subsequently measured at amortized cost using effective interest rate. Effective interest rate is the Internal Rate of Return which is computed by using trial and error method. IRR is the rate at which the present value of all the cash inflows will become equal to initial cash outflow. Amortized cost of the investment is defined as the amount at which the investment is measured at initial recognition minus the principal repayments plus the amount of cumulative amortization ascertained using effective interest rate. Gains and losses arising due to fair value fluctuations are not recognized for the investments measured at amortized cost.

Investments falling in the FVTOCI category are those which generate cash flow of interest and principal and held with an objective of collecting contractual cash flow as well as cash flow on selling the investments. Unlike the investments measured at amortized cost which include debt instruments only, FVTOCI investments can be both equity and debt instruments. At each year end, we will find the fair value (market value) of such investment and the difference between the carrying amount (recorded price) and fair value is transferred to OCI or investment revaluation reserve.

The investments which do not qualify for measurement at Amortized Cost and FVTOCI must be measured at FVTPL. Generally, FVTPL investments are those which are held for trading purposes. All equity investments are measured at FVTPL unless and otherwise the investing entity makes an irrevocable decision to classify such investment as FVTOCI at initial recognition. At each year end, FVTPL investments are recorded at fair value and the difference between carrying amount and fair value is transferred to profit and loss account.

CONCLUSION

Investment activity forms a major component of financial activities which has its impact on reported net profit, cash flows and net worth of a business concern. Every investment activity has three dimensions. Firstly, the interest income recognized and credited to profit and loss account, secondly, the actual cash inflow from interest and cash flows arising from purchase and sale of investment which are shown in the cash flow statement and finally the carrying value of the investment which is shown in the balance sheet. Since Ind AS is a reporting standard and it does not have any impact on business fundamentals, cash flows from investment activities remain intact irrespective of the accounting standards adopted. But, a change in the accounting standard adopted which brings changes in recognition, measurement and disclosure principles regarding a certain accounting event will subsequently impact the entity’s reported net profit and net worth. Thus, it is essential for all the stakeholders having interest in the accounting information provided in the financial statements to understand these changes which may affect their decision making.

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