

A STUDY ON IND-AS AND ITS HARMONIZATION WITH INDIAN ACCOUNTING PRACTICES

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ABSTRACT

The Ministry of Corporate Affairs (MCA) notified 41 Indian Accounting Standards (IND-AS) through Companies (Indian Accounting Standards) Rules, 2015 (16 February 2015) and Companies (Indian Accounting Standards) (Amendment) Rules, 2016 (30 March 2016) in pursuance of the provisions of Section 133 read with Section 469 of the Companies Act, 2013. As Indian companies now have a wider global reach than before, the need to integrate reporting standards with international standards was felt, which led to IFRS. IND AS 1 prescribes the basis for presentation of general purpose financial statements to ensure comparability both with the entity's financial statements of previous periods and with the financial statements of other entities. It sets the minimum requirements of guidelines for the presentation of financial statements, their structure and their contents. The requirements for the presentation of financial statements are set out in Schedule III of the Companies Act, 2013, Banking Regulation Act, 1949 (for banks), the regulations issued by the Insurance Regulatory and Development Authority (for insurance companies) and the SEBI Guidelines for mutual funds together with the Accounting Standards notified under the companies (Accounting Standard) Rules, 2006. This paper is an attempt to find out whether the accounting quality has improved of selected Indian companies listed on the Bombay Stock Exchange, before and after the adoption of IND AS, in preparing their financial statements in terms of cash flow prediction and cash flow persistence.

KEYWORDS: Indian Accounting Standards (IND-AS), Schedule III.

Introduction

Accountants around the world decided to speak the same accounting language and present the same accounting format resulting in the Uniform Accounting Standard - International Financial Reporting Standard (IFRS) worldwide. More than 100 countries around the world had already implemented IFRS instead of their national standard. In 2015, the Ministry of Corporate Affairs (MCA) notified the Companies (Indian Accounting Standards (IND AS)) Rules 2015, which laid down the adoption and applicability of IND AS in a phased manner starting from the accounting period 2016-17. The MCA has since issued three amendment rules, two in the year 2016, 2017 and one in 2018 to amend the 2015 rules.

Phase of Adoption

The MCA has notified, a phase-wise convergence, to IND AS from current accounting standards. IND AS will be adopted by specific classes of companies based on their Net worth and listing status. These are given in detail below:

- **Phase I**
Mandatory applicability of IND AS, to all companies from 1 April 2016:
 - It is a listed or unlisted company
 - Its net worth is more than or equal to Rs. 500 Crore *

* Net worth will be checked for the last three financial years (2013-14, 2014-2015 and 2015-16).

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- **Phase II**

Mandatory applicability of IND AS, to all companies with effect from 1 April 2017:

- It is a listed company or is in the process of being listed (as on 31.03.2016)
- Its net worth is more than or equal to Rs. 250 crores but less than Rs. 500 crores (for any of the periods mentioned below).

Net worth will be checked for the last four financial years (2013-14, 2014-2015, 2015-16 and 2016-17).

- **Phase III**

Compulsory applicability of IND AS, to all banks, NBFCs and insurance companies from 1 April 2018, whose:

Net worth is greater than or equal to INR 500 crore as on 1 April 2018.

IRDA (Insurance Regulatory and Development Authority) of India will notify a separate set of IND AS for banks and insurance companies from 1 April 2018. NBFCs (Non-Banking Financial Company) include core investment companies, stock brokers, venture capitalists, etc. Net worth, will be checked in Last 3 financial years (2015-16, 2016-17 and 2017-18).

- **Phase IV**

For all NBFCs whose Net worth is more than or equal to INR 250 crore but less than INR 500 crore, IND AS will come into force to them from 1 April 2019. This paper is an attempt to find out whether the accounting quality has improved of selected Indian companies listed on the Bombay Stock Exchange, before and after the adoption of **IND AS**, in preparing their financial statements in terms of cash flow prediction and cash flow persistence. Section 129 of Companies Act, 2013, provides for preparation of financial statements. The **Schedule III** to the **Companies Act, 2013** became applicable to all **companies** for the preparation of financial statements for financial years beginning on or from 1st April, 2014. Cash flow information provides the basis for assessing an entity's ability to generate cash and cash equivalents to users of the financial statement, and requires the entity to use those cash flows. **IND AS 7** sets out requirements for the presentation and disclosure of cash flow information.

Literature under Review

This paper presents a study on existing papers, articles, journals and reports provided by various authors, groups and committees from time to time. The following are some important literature:

Gupta, Pallavi, Akhter, Javaid and Chaklader, Barnali (2017): Its research topic was 'The Impact of IFRS Adoption on Key Financial Ratios - An Analysis of Wipro'. The objective was to assess the impact of IFRS adoption on the key financial ratios of the Indian company i.e. Wipro Limited. The empirical results of their study indicate that there are significant differences between the ratios calculated as per Indian GAAP and IFRS.

Amogh, Nisha and Gowda, S. Mari (2016): Their research title was 'Impact of IFRS Adoption on Financial Performance of Corporates. A Study on Sify Technologies Ltd.'. The study results suggest that the impact of adopting IFRS varies depending on the nature of the industry. Assets and liabilities and its realization have a large impact on ratios and depreciation and the company's financial performance ratio has fallen significantly.

Desai, Hiral (2016): Its research topic was 'IND AS converged with IFRS'. Main objective of the study was to understand the applicability of IFRS, its adoption phases in India and the challenges faced by firms and various stakeholders. The researcher concludes that IND.-AS has converged with IFRS, which has assumed a great importance, despite many issues and challenges in the way of harmonization of accounting standards.

V, Ramesha (2016): The research topic was 'Convergence of Indian Accounting Standards with IFRS – Prospects & Challenges'. The main objective of the research was to study the Indian scenario of IFRS adoption, advantages of IFRS adoption and suggestions about it. The researcher concludes that IFRS is a major challenge, but it is also an opportunity for audit firms to review their programs, processes and practices to make them more effective and efficient.

Babu, R., Narendra, J. Muni and Venkateswarlu, M. (2016): The research topic was 'International Financial Reporting Standards (IFRS) in India: Problems and Challenges'. The aim of the research was to study the process of IFRS adoption in India and the utility for India in adopting IFRS, the problems and challenges faced by stakeholders and its impact on India. This study has found that

converting from Indian GAAP to IFRS will face many difficulties, but at the same time convergence with IFRS is strongly recommended as facilitating convergence of IFRS by ICAI and other regulatory bodies the measures taken are reliable and give positive views. India is ready for convergence.

Gap in Research

From the above literature review it was found that no studies have been conducted for the year ended 2017 and 2018 for the harmonization of IND-AS with Indian Accounting Practices before and after the adoption of IND AS, in preparing their financial statements in terms of cash flow prediction and cash flow persistence. Hence the current scenario of adoption of IND AS was not reflected by the above researcher. So it is useful to research on this topic.

Objectives of the Study

The main objective of this paper is to find out whether the accounting quality has improved of selected Indian companies listed on the Bombay Stock Exchange, before and after the adoption of IND AS, in preparing their financial statements in terms of cash flow prediction and cash flow persistence.

Scope of Study

This study is concentrate on cash flow forecasting and cash flow persistence to measure accounting quality. The study is limited to Indian companies listed on the BSE Sensex of Bombay Stock Exchange for the period 2016-2017 and 2017-2018. BSE SENSEX is considered for the study as BSE SENSEX covers large, liquid and representative companies. BSE SENSEX is widely believed by Indian investors and is regarded as pulse of Indian stock market.

Methodology

Period of Study

From 2016-2017 to 2017-2018.

Collection of Data

The main source for conducting the study is taken from the annual report submitted by the company from the company's web site. Other documents such as journal papers, working papers are also considered for the study. Convenience sampling techniques have been used for selection of samples. Fourteen Indian companies included in the BSE SENSEX for the study.

Hypothesis

The Hypothesis framed is as follows:

H₁ Firms performing Schedule III exhibit higher cash flows than forecasting operations prior to reporting under Schedule III.

Tools and Technique

Statistical tools used in the study are mean, standard deviation, regression, and correlation. The quality of accounting is tested in terms of cash flow prediction and cash flow persistence. Good accounting quality as a high cash flow predictive capability, more cash flow persistence shows higher quality of accounting.

Analysis, Interpretation and Findings

The cash flow from the operation (current year) is the dependent variable for the purpose of the study. The independent variables are cash flow from operations (previous year) and accruals (previous year) Cash flow operation (current year, firm j) = + cash flow operation (previous year, firm j) + Accruals (previous year, firm j) +

The estimated coefficient measure the persistence of cash flows and the standard deviation of residuals from the equation is interpreted as the prediction of cash flows. Smaller values of residuals indicate greater predictability and therefore higher accounting quality. Coefficient values near 1 indicate greater persistence and higher accounting quality, and values closer to 0 indicate highly transitory cash flows from operations.

Regression and correlation analysis for the fiscal year ended 2016-2017 In this part, cash flow prediction and cash flow persistence are studied for the year before the start of IND AS (2016-2017). Cash flow from operation (2017) is the dependent variable and is treated as cash flow from operation (2016) and accruals (2016). From the following Table 1 it is concluded that the regression equation is significant because significance is 0.01. Cash flow from operations for the year 2017 is the dependent

variable and the independent variable is the cash flow from operations for the year 2016 and accruals for the year 2016. The R square is 0.584 and the adjusted R square is 0.529. The table shows that cash flow from operations for the year 2017 is a significant dependence on cash flow from operations for the year 2016 and accruals for the year 2016.

Table 1: Regression Test for the financial year ended 2017

| Variables | Definitions/Values |
|----------------------|--|
| Dependent variable | Cash flow from operation (2017) |
| Independent Variable | Cash flow from operation (2016), Accruals (2016) |
| R square | 0.584 |
| Adjusted R square | 0.529 |
| F value | 12.3 |
| Sig | 0.01 |

Table 2: Coefficients for the Financial Year Ended 2017

| Variables | Cash flow from operation 2017 | |
|----------------------------|-------------------------------|--------------|
| | t value | Significance |
| Cash flow operation (2016) | -0.051 | 0.769 |
| Accruals (2016) | 4.397 | 0.01 |

From the Table 2 it can be concluded that the cash flow from operation (2017) the dependent variable is function of the independent variable, accruals for the year ended 2016 as the significance is 0.01.

Table 3: Pearson's Correlation for the Financial Year Ended 2017

| Variables | | Cash flow Operation (2017) | Cash flow operation (2016) | Accruals (2016) |
|----------------------------|-----------------------|----------------------------|----------------------------|-----------------|
| Cash flow operation (2017) | Pearson's Correlation | 1 | 0.08 | 0.721 |
| | Sig (2tailed) | | 0.674 | 0.01 |
| Cash flow operation (2016) | Pearson's Correlation | 0.080 | 1 | 0.156 |
| | Sig (2tailed) | 0.674 | | 0.572 |
| Accruals (2016) | Pearson's Correlation | 0.721 | 0.156 | 1 |
| | Sig (2tailed) | 0.01 | 0.572 | |

Furthermore upon Pearson's correlation (Table 3) noted above it can be clearly seen that cash flow from 2017 operations is significantly positively correlated with charges at the .01 level (2 tailed).

Table 4: Spearman Correlation for the Financial Year Ended 2017

| Variables | | Cash flow Operation (2017) | Cash flow operation (2016) | Accruals (2016) |
|----------------------------|----------------------|----------------------------|----------------------------|-----------------|
| Cash flow operation (2017) | Spearman Correlation | 1 | 0.521 | 0.620 |
| | Sig (2tailed) | | 0.013 | 0.003 |
| Cash flow operation (2016) | Spearman Correlation | 0.520 | 1 | 0.486 |
| | Sig (2tailed) | 0.013 | | 0.077 |
| Accruals (2016) | Spearman Correlation | 0.621 | 0.374 | 1 |
| | Sig (2tailed) | 0.003 | 0.077 | |

Looking at the Table 4 Spearman correlation it proves that cash flow from operations till the end of 2017 is the significant flow of Indian companies taken for the study, which is significant with cash flow for operations since 2016 and with accruals at the .01 level (2 tailed tests). Regression and correlation analysis for the fiscal year ending 2017-2018, during the first start of Schedule III, cash flow prediction and cash flow persistence are studied. Cash flow from operation (2018) is the dependent variable and cash flows from operation (2017) and accruals (2017) are treated as independent variables.

Table 5: Regression Test for the Financial Year Ended 2018

| Variables | Definitions/Values |
|----------------------|--|
| Dependent variable | Cash flow from operation (2018) |
| Independent Variable | Cash flow from operation (2017), Accruals (2017) |
| R square | 0.764 |
| Adjusted R square | 0.726 |
| F value | 27.5 |
| Sig | 0.01 |

The regression equation from Table 5, cash flow from operation during the year ended 2017 is dependent on cash flow from operations during the year ended 2018 and accruals for year ended 2017 is significant. The R square 0.764 and the adjusted R square is 0.726.

From Table 6 it can be seen that the independent variable cash flow from operation of 2018, has significance relation with the dependent variable cash flow from operation 2017.

Table 6: Coefficients for the Financial Year Ended 2017

| Variables | Cash flow from operation 2018 | |
|----------------------------|-------------------------------|--------------|
| | t value | Significance |
| Cash flow operation (2017) | .887 | 0.01 |
| Accruals (2017) | -.577 | .576 |

Further the Pearson's correlation (Table 7) proves that there is a significant positive correlation between the dependent variable (cash flow from operation, 2018) and independent variable (cash flow from operation, 2017) and the value is 0.810 which is significant at 0.01 levels (2 tailed).

Table 7: Pearson's correlation for the financial year ended 2018

| Variables | | Cash flow operation (2018) | Cash flow operation (2017) | Accruals (2017) |
|----------------------------|-----------------------|----------------------------|----------------------------|-----------------|
| Cash flow operation (2018) | Pearson's Correlation | 1 | 0.810 | -0.476 |
| | Sig (2 tailed) | | 0.01 | 0.085 |
| Cash flow operation (2017) | Pearson's Correlation | 0.921 | 1 | -0.453 |
| | Sig (2 tailed) | 0.01 | | 0.104 |
| Accruals (2017) | Pearson's Correlation | -0.476 | -0.453 | 1 |
| | Sig (2 tailed) | 0.085 | 0.104 | |

Table 8 shows Spearman's correlation test, which proves that the dependent variable cash flow from operation 2018 is positively correlated with the independent variable cash flow from 2017, at the 0.01 level (2 tailed) but Not with other independent variable accruals 2017.

Table 8: Spearman Correlation for the Financial Year Ended 2017

| Variables | | Cash flow operation (2018) | Cash flow operation (2017) | Accruals (2017) |
|----------------------------|----------------------|----------------------------|----------------------------|-----------------|
| Cash flow operation (2018) | Spearman Correlation | 1 | 0.912 | -0.358 |
| | Sig (2 tailed) | | 0.01 | 0.208 |
| Cash flow operation (2017) | Spearman Correlation | 0.912 | 1 | -0.464 |
| | Sig (2 tailed) | 0.01 | | 0.095 |
| Accruals (2017) | Spearman Correlation | -0.358 | -0.464 | 1 |
| | Sig (2 tailed) | 0.208 | 0.095 | |

Cash Predictability

In this study it also assumed that the small values of residuals from the regression equation: Cash flow operation (current year, firm J) = + Cash flow operation (previous year, firm J) + Accruals (previous year, firm J) + indicates greater cash forecasting and higher quality of accounting.

Table 9: Standard Deviation of Residuals for the Financial Year Ended 2016-2017

| Variable | N | Minimum | Maximum | Mean | Std. Deviation |
|----------------|---|----------|---------|---------|----------------|
| Residual Valid | 1 | | | | |
| N (list wise) | 4 | -0.11087 | 0.06193 | -0.0245 | 0.04673453 |
| | 1 | | | | |
| | 4 | | | | |

Table 10: Standard Deviation of Residuals for the Financial Year Ended 2017-2018

| Variable | N | Minimum | Maximum | Mean | Std. Deviation |
|----------------|---|----------|---------|--------|----------------|
| Residual Valid | 1 | | | | |
| N (list wise) | 4 | -0.04487 | 0.07442 | 0.0715 | 0.03565598 |
| | 1 | | | | |
| | 4 | | | | |

On verifying from Table 9 it can be seen that the standard deviation of the residuals of the regression equation for the related information before adoption IND AS (Schedule III) to the presentation of the financial statement for the year ended 2017 is 0.0467, and from Table 10 it show that the standard deviation of the residuals of the regression equation for the related information after adoption IND AS (Schedule III) to the presentation of the financial statement for the year ended 2018 is 0.0356. It can be observed that the standard deviation after adoption the IND AS is lesser than before, implementation of IND AS which is a good step to harmonize Indian accounting practices with IND AS. It shows more cash predictability and more accounting quality when compared with presentation of financial statement before adoption the IND AS.

Cash Persistence

This study on cash persistence indicated that the coefficient of cash flow independent variable closer to 1 from the operation indicates more persistence and being closer to 0 indicates less persistence. The independent variable cash flow from Operation (2016) and the dependent variable from Operation (2017) described in Table 2 for the coefficient of cash flow is -0.051. For the independent variable cash flow from Operation (2017) and the coefficient of its dependent variable cash flow from Operation (2018) described in Table 6 is 0.887. In this way, the coefficient 0.887 for the independent variable cash flow from operation 2017, shows more persistence as compared with the coefficient -0.051 for the independent variable cash flow from operation for 2016 (which is close to 0). Therefore it can be proved that accounting data submitted after adoption of IND AS for the sample firms studied for the financial year 2017 and at the end of fiscal year 2018, is a good step towards harmonization of Indian accounting practices with IND AS.

Conclusion

In this study accounting quality is measured in cash flow persistence and cash flow prediction. Prediction of high (low) cash flow and high (low) cash flow persistence are considered to be related to high (low) accounting quality. Finally, it has been concluded from this study that from the sample firms taken to cover the period 2016-2017 and 2017-2018 it can be clarified that the harmonization of Indian accounting practices with Ind.-AS is improved accounting quality. It has been measured in terms of cash flow persistence and cash flow prediction. This study supports harmonizing Indian accounting practices with Ind.-AS and issues related to shareholders, creditors, regulating institutions, other decision-making authorities and other stakeholders at large.

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