International Convergence of Accounting Standards: A long road ahead

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The increasing trend of cross-border investments and rapid growth of international business and trade in recent times have necessitated the need for a common accounting and financial reporting language. The financial reporting by using this accounting language should be such which investors, lenders, vendors and other stakeholders in one country can understand in the same way as the stakeholders in other countries and informed economic decisions can be taken.

With the above objective, International Accounting Standards Committee (IASC) (the predecessor body of International Accounting Standards Board (IASB)), was formed long back in 1973. Over more than four decades of its existence, IASC/ IASB has made tremendous efforts towards adoption of one common accounting language, named as International Financial Reporting Standards (IFRSs). This initiative gained momentum with the restructuring of IASC in late nineties and adoption of IFRS by European countries (through endorsement mechanism) beginning 2005. Around that time, Financial Accounting Standards Board (FASB) of United State of America (US) had also started with a joint convergence project with IASB. Other countries such as Canada, India, Japan also demonstrated their commitments to adopt/ adapt IFRSs.

The benefits were many, including better investors' confidence, low cost of compliances by multinational companies, easy flow of capital across geographies among countries, etc. With various countries having adopted IFRS or taking initiatives towards convergence with IFRS, it seemed that the age-old barriers of local business environment, customs, practices have become secondary in the light of benefits of convergence. However, against the backdrop of financial crisis in years 2008-2009, fair value measurements propagated under IFRS came under debate. Further, the IFRS-US joint convergence project also did not proceed as was expected. The concerns about complexities and unreliability of fair value measurements and different economic environment also dissuaded some of the countries to have a full convergence with IFRS.

The current status of IFRS adoption *(source: IASB website)*

It may be noted that analysis of IFRS jurisdictions by GDP shows that capital market investors and lenders in jurisdictions with 56% of the world's GDP receive IFRS financial statements. IFRS are also used in some of the remaining economies, for example, by nearly 500 foreign companies whose securities trade in the United States.

To assess progress towards the IFRS adoption, the IFRS Foundation is developing profiles of application of IFRS in individual jurisdictions. Currently, profiles are completed for 130 jurisdictions:

Sl. No.	Convergence status	Number of jurisdictions
1	IFRS required for all or most domestic publicly accountable entities (listed companies and financial institutions) in capital markets	105 jurisdictions (including 3 countries, viz, Brunei, Bhutan, and Colombia, which will begin using IFRS in 2014, 2021 and 2015 respectively)
2	IFRS permitted rather than required	14 jurisdictions (including Japan, Singapore, Switzerland, India). In India, Securities and Exchange Board of India (SEBI) has given the option to listed entities to prepare and file consolidated financial statements in conformity with IFRSs issued by IASB.
3	IFRS required only for financial institutions	3 jurisdictions (Saudi Arabia, Uzbekistan and Yemen)
4	Jurisdictions in process of adopting IFRS in full	2 jurisdictions (Indonesia and Thailand)
5	National or regional standards used	7 jurisdictions (including United States, China, Egypt)

The 105 jurisdictions classified as requiring IFRS for all or most domestic publicly accountable entities include the EU Member States to which the IAS 39 'carve-out' applies. The carve-out affects fewer than two dozen banks out of the 8,000 IFRS companies whose securities trade on a regulated market in Europe. The 105 also include four jurisdictions that have adopted recent, but not the latest IFRSs. These jurisdictions are working to update their adoption to the current version. Further, 8 jurisdictions out of 105 jurisdictions do not require IFRS for financial institutions.

The 130 jurisdictions made very few modifications to IFRS, and the few that were made are generally regarded as temporary steps in the jurisdiction's plans to adopt IFRS. The IASB currently has projects on its agenda to address most of the other modifications. A few jurisdictions have deferred the effective dates of some Standards, particularly IFRSs 10, 11 and 12 and IFRIC 15.

*Auditor's report***:** In 76 jurisdictions, the auditor's report (and/or basis of presentation note) refers to conformity with IFRS. In another 33 jurisdictions the auditor's report refers to conformity with IFRS as adopted by the EU. In the 21 remaining jurisdictions the auditor's report refers to conformity with national standards.

The status of convergence of some of the significant jurisdictions is as below:

Status in United States of America (US)

Considering the overall contribution of US to the world economy, no convergence can be completed without US being a part of it. IASB and the US FASB have been working together since 2002 to achieve convergence of IFRSs and US generally accepted accounting principles (GAAP).

In September 2002, the IASB and the FASB agreed to work together, in consultation with other national and regional bodies, to remove the differences between international standards and US GAAP. This decision was embodied in a Memorandum of Understanding (MoU) between the boards. The boards' commitment was further strengthened in 2006 when the IASB and FASB set specific milestones to be reached by 2008.

In the light of the progress achieved by the boards and other factors, the US Securities and Exchange Commission (SEC) removed in 2007 the requirement for non-US companies registered in the United States to reconcile their financial reports with US GAAP if their accounts complied with IFRSs as issued by the IASB. At the same time, the SEC also published a proposed roadmap on adoption of IFRSs for domestic US companies that would have given U.S. companies the option to use IFRS as early as 2014. However, since then, there is no firmed-up decision by SEC on adoption of IFRS by US domestic companies.

It may be noted that recently in June 2014, former SEC Chairman Christopher Cox, as a part of his keynote address on "How America's Participation in International financial Reporting Standards was lost" to a conference, stated that "Full-scale adoption of IFRS in the United States might once have been possible, but it is no longer". Mr. Cox further stated that "U.S. stakeholders have stumbled over the domestic use of IFRS because they are unsure the rules will serve their interests. They also continue to worry about the influence of national and regional governments on the International Accounting Standards Board,"

Status in China

Although China has adopted national accounting standards that are substantially converged with IFRSs, the use of IFRSs is not permitted for domestic companies. According to the Accounting Law in China, all the Chinese companies must comply with the accounting standards issued by the Ministry of Finance in China.

Status in Japan

The IASB and the Accounting Standards Board of Japan (ASBJ) have been working together to achieve convergence of IFRS and Japanese Generally Accepted Accounting Principles since 2005. That work was formalised in 2007 with the Tokyo Agreement. Till date, adoption of IFRS is not required in Japan. Voluntary application of IFRS for consolidated financial statements by companies that meet certain criteria has been permitted since March 2010. As of February 2014, only 34 companies have either started to use IFRS or have publicly announced their intention to use IFRS as a basis for preparing consolidated financial statements as required by the Financial Instruments and Exchange Act (FIEA).

Status in India

The Ministry of Corporate Affairs (MCA), Government of India, in 2011, on a recommendation made by the Institute of Chartered Accountants of India (ICAI) had also decided to converge with IFRS. It was decided not to adopt the IFRS which is the practice in many countries but to converge with IFRS. This means that India would have the right to depart in appropriate cases from the requirements in the IFRS keeping in view its local economic and legal environment. In this direction, in 2011, 35 Indian Accounting Standards (Ind AS) converged with IFRS, formulated by the ICAI and after recommendation thereof by the National Advisory Committee on Accounting Standards were approved by the Ministry of Corporate Affairs (MCA) and placed on its website in February, 2011.

At that time, the MCA had decided to implement these Standards in phased manner from accounting periods commencing on or after 1st April 2011, but the same could not be implemented because of various issues, such as, non-compatible legal and regulatory requirements, tax related issues, etc.

Recognising the need of implementation of IFRS-converged Indian Accounting Standards in India at the earliest, particularly after the enactment of new Companies Act, 2013, which removes various impediments towards implementation of Ind AS converged with IFRS, the MCA recently requested the ICAI to suggest a revised roadmap for implementation of these Ind AS. As the Ind AS could not be implemented earlier due to various tax, dividend and other issues, to overcome these issues, the ICAI in its revised roadmap has suggested to the MCA that Ind AS may be made applicable for preparation of Consolidated Financial

Statements of public-interest entities compared to the earlier announced roadmap where Ind AS were to be made applicable to both the Consolidated Financial Statements as well as Individual Financial Statements. The major benefit of the revised approach in the view of the ICAI would be that there would not be any tax, managerial and other employee compensation implications, dividend policy implications, etc., because Individual Financial Statements would continue to be prepared as per the existing notified Accounting Standards, which would be the basis for all these purposes and these Standards would be upgraded over a period of time. It has been recommended that such first financial statements may be prepared for the accounting periods beginning on or after April 1, 2016, with comparatives for the year ending 31st March 2016.

Subsequent to the submission of the proposed roadmap by the ICAI, the MCA has requested the ICAI to obtain the views on the proposed roadmap from the Securities and Exchange Board of India and Reserve Bank of India. ICAI is in the process of interacting with SEBI and RBI and the views of the aforesaid regulators would be communicated to the MCA in near future.

Challenges in convergence

While the above status of convergence/ adoption is encouraging, it is also evident that large economies such as United States, China, Japan, etc. still do not have full convergence with IFRS. Further, many countries have not mandated the use of IFRS for non-publicly accountable entities, which results in simultaneous application of two sets of GAAPs.

There are many challenges towards convergence with IFRS. Some of the significant ones include, increasing use of fair value measurements, different economic environments, legal requirements, complexities, subjective framework requiring interpretations, etc. The ultimate goal of one set of global accounting standards would not be achieved till these challenges are addressed and also significant jurisdictions achieve full convergence with IFRS.