Unit 5 – Accounting Standards in India and IFRS

Topic – International Financial Reporting Standards (IFRS)

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What is IFRS?

- IFRS is short for International Financial Reporting Standards.
- It is the international accounting framework within which financial information is properly organized and reported.
- It is derived from the pronouncements of the London-based International Accounting Standards Board (IASB).
- It is currently the required accounting framework in more than 120 countries.
- IFRS requires businesses to report their financial results and financial position using the same rules; this means that there is uniformity in reporting financial results, which makes it easier to compare and contrast.

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- IFRS is used primarily by businesses reporting their financial results anywhere in the world *except the United States.*
- Generally Accepted Accounting Principles, or GAAP, is the accounting framework used in the United States.
- GAAP is much more rule-based than IFRS. IFRS focuses more on general principles than GAAP, which makes the IFRS much easier to understand.

- Some of the areas covered under IFRS include, but are not limited to:
    - Presentation of financial statements
    - Revenue recognition
    - Employee benefits
    - Borrowing costs
    - Income taxes
    - Investment in associates
    - Inventories
    - Fixed assets
    - Intangible assets
    - Leases
    - Retirement benefit plans
    - Business combinations
    - Foreign exchange rates
    - Operating segments
    - Subsequent events
    - Industry-specific accounting, such as mineral resources and agriculture

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Different IFRS (IFRS 1 – 8)

IFRS 1	First Time Adoption of IFRS
IFRS 2	Share Based Payment
IFRS 3	Business Combination
IFRS 4	Insurance Contracts
IFRS 5	Non-current Assets held for Sale and Discontinued Operations
IFRS 6	Exploration for and Evaluation of Mineral Assets
IFRS 7	Financial Instruments
IFRS 8	Operating Segment

IFRS 1 – First Time Adoption

IFRS 1 requires an entity that is adopting IFRS Standards for the first time to prepare a complete set of financial statements covering its first IFRS reporting period and the preceding year. The entity uses the same accounting policies throughout all periods presented in its first IFRS financial statements. Those accounting policies must comply with each Standard effective at the end of its first IFRS reporting period.

IFRS 1 also prohibits retrospective application of IFRS Standards in some areas, particularly when retrospective application would require judgments by management about past conditions after the outcome of a particular transaction is already known.

IFRS 1 requires disclosures that explain how the transition from previous GAAP to IFRS Standards affected the entity's reported financial position, financial performance and cash flows.

IFRS 2 – Share Based Payment

- IFRS 2 specifies the financial reporting by an entity when it undertakes a share-based payment transaction, including issue of share options.
- It requires an entity to recognize share-based payment transactions in its financial statements, including transactions with employees or other parties to be settled in cash, other assets or equity instruments of the entity.
- It requires an entity to reflect in its reported profit or loss and financial position, the effects of share-based payment transactions, including expenses associated with transactions in which share options are granted to employees.

IFRS 3 – Business Combination

IFRS 3 establishes principles and requirements for how an acquirer in a business combination: recognizes and measures in its financial statements the assets and liabilities acquired, and any interest in the acquiree held by other parties;

recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase; and

determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination.

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- The core principles in IFRS 3 are that an acquirer measures the cost of the acquisition at the fair value of the consideration paid; allocates that cost to the acquired identifiable assets and liabilities on the basis of their fair values; allocates the rest of the cost to goodwill; and recognises any excess of acquired assets and liabilities over the consideration paid (a ‘bargain purchase’) in profit or loss immediately.
- The acquirer discloses information that enables users to evaluate the nature and financial effects of the acquisition.

IFRS 4 – Insurance Contracts

An insurance contract is a contract under which one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.

IFRS 4 applies to all insurance contracts (including reinsurance contracts) that an entity issues and to reinsurance contracts that it holds, except for specified contracts covered by other Standards. It does not apply to other assets and liabilities of an insurer, such as financial assets and financial liabilities within the scope of IFRS 9. Furthermore, it does not address accounting by policyholders.

IFRS 4 exempts an insurer temporarily (i.e. until it adopts IFRS 17) from some requirements of other Standards, including the requirement to consider the Conceptual Framework in selecting accounting policies for insurance contracts.

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IFRS 5 – Non-Current Assets Held for Sale and Discontinued Business

- IFRS 5 requires a non-current asset or disposal group to be classified as held for sale if its carrying amount will be recovered principally through a sale transaction instead of through continuing use;
- assets held for sale to be measured at the lower of the carrying amount and fair value less costs to sell;
- depreciation of an asset to cease when it is held for sale;
- separate presentation in the statement of financial position of an asset classified as held for sale and of
- the assets and liabilities included within a disposal group classified as held for sale; and
- separate presentation in the statement of comprehensive income of the results of discontinued operations.

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IFRS 6 – Exploration for and Evaluation of Mineral Assets

IFRS 6 specifies some aspects of the financial reporting for costs incurred for exploration for and evaluation of mineral resources (for example, minerals, oil, natural gas and similar non-regenerative resources),

as well as the costs of determination of the technical feasibility and commercial viability of extracting the mineral resources.

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IFRS 7 – Financial Instruments

IFRS 7 requires entities to provide disclosures in their financial statements that enable users to evaluate: the significance of financial instruments for the entity's financial position and performance.

the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the end of the reporting period, and how the entity manages those risks.

The qualitative disclosures describe management's objectives, policies and processes for managing those risks.

The quantitative disclosures provide information about the extent to which the entity is exposed to risk, based on information provided internally to the entity's key management personnel.

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- IFRS 7 applies to all entities, including entities that have few financial instruments (for example, a manufacturer whose only financial instruments are cash, accounts receivable and accounts payable) and those that have many financial instruments (for example, a financial institution most of whose assets and liabilities are financial instruments).

IFRS - Operating Segment

IFRS 8 requires an entity whose debt or equity securities are publicly traded, to disclose information to enable users of its financial statements to evaluate the nature and financial effects of the different business activities in which it engages and the different economic environments in which it operates.

It specifies how an entity should report information about its operating segments in annual financial statements and in interim financial reports.

It also sets out requirements for related disclosures about products and services, geographical areas and major customers.

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Differences between IFRS and GAAP

S.No.	Basis of Difference	IFRS	GAAP
1	Usage	IFRS is a globally accepted standard for accounting, and is used in more than 120 countries.	GAAP is exclusively used within the United States and has a different set of rules for accounting than most of the world.
2	Methodology	IFRS looks at the overall patterns and is based on principle. With a principle- based accounting method, there is potential for different interpretations of the same tax-related situations.	GAAP focuses on research and is rule-based. With GAAP accounting, there's little room for exceptions or interpretation, as all transactions must abide by a specific set of rules.
3	Inventory Methods	Under IFRS, the LIFO method for inventory is not allowed. LIFO does not reflect an accurate flow of inventory in most cases, thus resulting in unusually low income levels	Under GAAP, a company is allowed to use the Last In, First Out (LIFO) method for inventory estimates.

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S.No.	Basis of Difference	IFRS	GAAP
4	Inventory Reversal	Under IFRS, the amount of the write- down can be reversed.	GAAP specifies that if the market value of the asset increases, the amount of the write-down cannot be reversed.
5	Development Costs	A company's development costs can be capitalized under IFRS, as long as certain criteria are met.	With GAAP, development costs must be expensed the year they occur and are not allowed to be capitalized.
6	Intangible Assets	When it comes to intangible assets, such as research and development or advertising costs, IFRS accounting takes into account whether an asset will have a future economic benefit as a way of assessing the value.	Intangible assets measured under GAAP are recognized at the fair market value only.
7	Income Statements	Under IFRS, extraordinary or unusual items are included in the income statement and not segregated.	Under GAAP, they are separated and shown below the net income portion of the income statement.
8	Classification of Liabilities	With IFRS, there is no differentiation made between the classifications of liabilities, as all debts are considered noncurrent on the balance sheet.	The classification of debts under GAAP is split between current liabilities, where a company expects to settle a debt within 12 months, and noncurrent liabilities, which are debts that will not be repaid within 12 months

Next Topic…

- For the next week, the topic will be Accounting Standards in India

Thank You