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PERCEPTIVE OBSERVATIONS ON THE BENEFITS AND CHALLENGES OF INTERNATIONAL FINANCIAL REPORTING STANDARDS IN THE INDIAN BANKING SECTOR

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Abstract

Although a large number of countries of the world adopted the IFRS for their accounting purposes, when it comes to India despite the strong intention to implement the same in the banking sector, only a partial implementation has been attempted so far. The Reserve Bank of India itself argues for its implementation in its reports. Yet it remains only in intentions and not in implementation. Therefore, the benefits and challenges due to the implementation of IFRS can only be perceived and observations can be made only based on such perceptions. Currently, a large number of studies are available on the benefits and challenges of IFRS. Most of such studies have relied on the arguments after analysing the secondary data. There is a strong need to study the people, business and environment and prepare the ground for the effective implementation of the accounting standards as available in the IFRS. The Reserve Bank of India has also advised the banking and non-banking financial institutions of India as early as 2016. In this paper an attempt has been made to discuss the benefits and challenges of IFRS in the banking sector of India through perceptive observations.

Keywords

IFRS, Benefits and Challenges, Banking organizations.

Introduction

IFRS has been in operation the world over ever since its adoption. With the intention of making business affairs and accounts accessible across the continent, IFRS originated in the European Union. However, t h e idea quickly took over the world. A common accounting language allowed greater communication worldwide. Although In spite of the fact that all countries of the world have not fully adopted IFRS, the countries participating are spread all over the world, rather than being confined to one geographic region. Similarly, the standards are used in all corporate entities including the banking and non-banking financial institutions. According to Carson, E., and Dowling, C. (2010), financial information prepared and audited according to a specific national accounting standards , nuances of which are known only nationally, may not be useful to users due to the high level of globalisation of businesses and financial markets. Contrary to this, an international accounting language in the form of IFRS provides greater facilitation and more benefits for the stakeholders. However, it is not argued that IFRS is an unmixed blessings. There needs a perceptive observation of the benefits and challenges of IFRS.

Objectives

This paper is purported to achieve the following objectives:

i. To discuss the benefits and challenges of IFSR in general globally and in India particularly.

ii. To highlight the implications of the adoption of IFSR in the Banking and non-banking sector.

Methodology

This research paper uses a content analysis of some of the secondary sources perused as also a descriptive narration of the issues in question. The paper relies on the secondary data as available in the research papers and other reports of agencies.

Brief Review of Literature

Sporadic efforts to recognize the challenges of implementation of IFRS with respect to communication, translation and interpretation of standards from the IASB, and to comprehend the challenges tackled by users and practitioners, with respect to education, staffing, cost, training and IT infrastructure were observed during the past decade. (Jermakowicz and Gornik-Tomaszewski, 2006, Jones and Higgins, 2006, Weaver and Woods, 2015 and Ocheni 2015). In Bangladesh, it is expected to reduce information asymmetry and make information more comparable(Islam and Bhattacharjee,2009). A coordinated regulatory review and enforcement system to provide for the stable application is an essentiality(Larson & Street, 2004). The complexity related to certain international financial reporting standards and tax orientation of most countries have been recognized as the two major significant impediments to convergence(Jermakowicz, 2004). There are challenges on the lack of guidance during the application of

IFRS for Belgian publicly traded companies posing the risk of multiples interpretations during the initial IFRS reporting(Jermakowicz, 2004).

It is argued that before introducing IFRS in the accounting curriculum, the teachers must acquire the necessary knowledge, beginning with the basic background knowledge till the trends towards global accounting standards (Patro and Gupta, 2012). In some countries like Libya, the challenges to adoption and implementation of IFRS are lack of technical skills and inadequate knowledge of the Libyan professional accountants, inconsistency of existing laws and regulatory frameworks of accounting in Libya with the recent development of accounting profession and the weakness of the professional accounting body(Laga (2013). Adoption of IFRS refers to adopting a complete set of different reporting standards(Hossain, Hasan and Safiuddin,2015). Professionals report that the awareness of these reporting standards is still not there among the stakeholders like Banks, Financial institutions, Stock Exchanges, etc in Bangladesh. Awareness generation of these standards is a complicated issue. Another hitch is inadequacy of training material on IFRS or its total absence. In the case of countries like India, there is a critical need to deal with the challenges of IFRS and work towards its adoption by implementing the roadmap by creating necessary preparedness. The required IFRS skills and *adequate* knowledge among the accounting professionals who can supervise the conversion process have to be generated. A very commonly documented challenge for IFRS implementation is `the complicated nature of some IFRS.(Street,2004 and UNCTAD, 2008). IFRS has a voluminous nature and enormous requirements such as standards on financial instruments. In this context, an empirical study conducted by Arpitha and Preeti (2021) is relevant and worth quoting verbatim: "Since IFRS has been enforced by more than 110 nations and others are planning to shift to this high quality principle based standards, India too is not an exception. India is the most recent participant in the IFRS convergence process where the adoption of the Indian Accounting Standards (Ind-AS) will initiate from the financial year 2016-2017. This research is motivated to explore the issues and challenges faced by the accounting bodies and members of the accounting profession in India in implementing the IFRS-based accounting standards."

Benefits of IFRS

A good number of studies carried out in different countries have highlighted the benefits of having single set of financial reporting standards across the globe. Studies conducted on the adoption of IFRS at country level indicated that countries that adopted IFRS experienced huge increases in Direct Foreign Investment (DFI) flows across countries(Irvine & Lucas, 2006).

In some European countries like Great Britain, Italy and Germany, the implementation of IFRS has improved the quality of accounting information(Iatridis (2010); Paglietti (2009); Pannanen and Lin, 2009). The adoption of IFRS will foster common benchmark in financial information across international borders with the aim of generating greater momentum for economic development(Kunle, Omoruyi & Hamed, 2011). IFRS is capable of financial transformation because it comes with it accountability and transparency in fair value measurement and investment efficiency (Ng, Tsang and Yang, 2013). IFRS standards are yardsticks that enables organizations to provide stakeholders with relevant, reliable and timely information and that such information contributes towards the achievement of orderly capital markets around the world(Imhoff (2003). The benefits from adaptation of IFRS over the world include better financial information for shareholders and regulators, enhanced comparability, improved transparency of results, increased ability to secure cross-border listing, better management of global operations and decreased cost of capital(Gordon, 2008).

IFRS directly contribute to high-quality, transparent, and comparable financial information. The International organizations, because of the benefits to investors, creditors, financial analysts, and other users of financial statements thoroughly assess the performance of their investment.(Carson and Dowling, 2010; Latifah, I., Asfadillah, C. & Sukmana, R., 2012).

Several of the studies have been able to document the benefits of IFRS as given below:

i) The level of comparability between the financial statements and the improvement of the transparency level increases significantly.

When similar standards are used to prepare financial statements, they enlarge the transparency and expand the accuracy to compare with each other for the businesses adopting these. Therefore, helpful for comparison of businesses globally using the same standards while they might have otherwise found it difficult to compare if they had used different standards. The expanded and easier comparability benefitted investors and other market participants to arrive at informed economic decisions.

ii) The accountability is made stronger by reducing the information gap between the providers of capital and the people to whom they have entrusted their money because of the IFRS. They are also powerful tool for the global regulators.

IFRS create increased flexibility. IFRS are based principles and not rules and therefore, reasonable valuation with various ways to accomplish tasks can be arrived at. Corporate the freedom to adopt IFRS to their specific situations that result in financial statements which can be more easily read and are more useful.

iii) Capital from foreign markets at lower cost can be raised if the industries can create more confidence in the minds of foreign investors that their financial statements in tune with globally accepted accountingstandards.

iv) Investors can have more opportunities with lower risks across the world, thus improving capital allocation. Corporate that use a single, trusted accounting language lowers the cost of capital and reduces international reporting costs. Thus IFRS Standards contribute to economic efficiency.

The following benefits can be enumerated because of the use of IFRS.

1. A single set of accounting standards around the world will be created. The use of multiple accounting standards based on the preference of each country can be done away with. International Financial Reporting Standards would enable agencies from different segments of the world to apply the same standards in every transaction. The transparency increases that lead to more accessible cross-border investments. The cost of capital can be reduced and higher liquidity during each transaction can be enjoyed.

2. The time, effort, and expense of preparing multiple reports can be avoided.

If multiple reports are prepared based on multiple accounting standards, the cost will increase, more time will be needed and multiple reports have to be prepared and read, comprehended and compared. When this saving can be enjoyed year after year, the corporate stand to benefit immensely.

3. IFRS has the one-time cost that would impact the economy, the actual expense of transitioning to this global standard is minimal. The different agencies would save significantly, if they adopted International Financial Reporting Standards because it would reduce the amount of work it takes to remove errors, meet multiple regulations, and distribute the information effectively.

4. Subsidiaries from foreign countries can be easily monitored and controlled. In the case of USA, where the IFRS has not been adopted, subsidiaries must create parallel reports using GAAP and IFRS, which means there is an increased risk of error and additional auditing requirements necessary to ensure compliance. With IFRS, the potential for misunderstandings can be reduced. It would help shareholders and firms to simplify their investment decisions.

5. It is beneficial to consider with the adoption of IFRS as many American-based companies doing business overseas are already preparing reports based on this standard. They are producing a simultaneous GAAP report to meet with domestic regulations while complying with the international rules. IFRS will stop duplication and focus on the potential of doing the best possible.

6. Accounting practices will become more flexible if the International Financial Reporting Standards used a principles-based system instead of one that is based on specific rules. The goal of each standard in IFRS will be to reach a reasonable valuation, and there can be several ways to reach this result. This provides ease to the agencies for the production of useful statements that are much easier to comprehend.

7. IFRS will enable all countries to do business in the foreign markets. The digital developments has expedited the process of globalization. Corporate expansion beyond borders of their country of origin helps the consumers as well. The added cost of reporting a financial statement using IFRS and GAAP can be cost-prohibitive. The current start up environment will be adversely affected due to this. A single accounting standard will expand opportunities because there would be fewer regulations on the functioning of the businesses.

8. Adoption of IFRS will lead to the unified accounting standards across the world. This would allow for rulemaking and policy authorities to have a common central authoritative body that could oversee the standards and overall compliance.

9. The various cost reduction efforts due to single unified accounting system will lead to better return on equity. Reconciliation amounts always vary by industry and country, but the advantage remains the same. Although the net income levels for the firms reduces in the differences between the two standards, the overall benefits can better support economic growth. This is because of increases in stock value, dividend payments, and a strong regulatory environment.

10. IFRS can help increase the rates of foreign direct investment around the world. The presence of the International Financial Reporting Standards globally would make it easier for companies

to invest in one another whenever there is a market opportunity. There may also be a lack of familiarity or understanding with the anticipated future cash flows under differing accounting systems.

IFRS, will reduce a home-bias in place for shareholders to prefer domestic firms over international ones. There will be a familiarity and certainty in the financial information that will enhance their decision-making process.

11. IFRS can help newer investors and smaller investments. Investors who are new to their industry to understand the information in the financial statements because the data would be simpler and of better quality. This advantage would allow anyone to become competitive because there is a greater understanding of what is going on with the financial health of an organization.

12. IFRS can also be a binding accounting force that will unify the businesses and also provide a ground for global economic growth.

An empirical study involving the Chartered accountants of India was conducted and the data relating to the same are presented in the table given below (A .Srivatsava and P. Kulshreshtha, 2019).

Table 1. Table showing the Benefits of IFRS Implementation in India

Statements	Mean	SD	5_SA	%	4_A	%	3_N	%	2_D	%	1_SD	%	T
IFRS implementation will provide better information for decision making	4.25	.77	64	42.7	64	42.7	18	12	4	2.7	0	0	150
IFRS implementation will provide for better inter-company comparison of financial statement	4.16	.75	50	33.3	78	52	20	13.3	0	0	2	1.3	150
IFRS implementation will help in timely financial reporting	4.07	.90	54	36	62	41.3	26	17.3	6	4	2	13	150
IFRS implementation will provide for Better access to international capital market	3.92	.91	42	28	64	42.7	38	25.3	2	13	4	2.7	150
IFRS adoption will provide for ease of using one high standard and consistent reporting standard	4.17	.83	58	38.7	66	44	22	14.7	12	1.3	2	1.3	150
IFRS implementation will reduce cost of equity and will improve earning management	3.88	.82	38	25.3	60	40	48	32	4	2.7	0	0	150
IFRS implementation will provide a true and fair view of financial position	4.19	.78	58	38.7	66	44	22	14.7	4	2.7	0	0	150
IFRS implementation will enhance the accuracy and reliability of financial statements	4.17	.72	51	34	77	51.3	19	12.7	3	2	0	0	150
IFRS implementation will provide opportunities to Indian professionals at international level	3.13	.79	1	.7	54	36	58	38.7	37	24.7	0	0	150
Use of IFRS will help in prevention of accounting frauds/manipulation	3.72	.84	22	14.7	76	51	43	28.7	6	4	3	2	150

Source: "The Benefits and Challenges of IFRS Adoption in India:The Dawn of a New Era", International Journal of Accounting and Financial Reporting, ISSN 2162-3082, 2019, Vol.9, No.4.pp334-350,Anubha Srivastava and Preeti Kulshreshtha.

Challenges of Adopting IFRS

IFRS cannot be considered as an unmixed blessing. Various studies have pointed out the challenges of IFRS also which can be seen hereunder:

Few of the studies have given contradictory views questioning the relevance of IFRS adoption in developing and emerging economies.

Cultural context was pointed out prominently. One single set of accounting standards cannot reflect the differences in national business practices arising from differences in institutions and cultures.(Rong-Ruey, D, 2006). Another issue was the quality of governance. If countries have relatively high quality of governance in institutions, IFRS implementation per se will not be attractive as high quality institutions represent high opportunity and switching costs to adopting international accounting standards will be difficult or hazardous.

Thus, cultural, political and business differences may also continue to impose significant obstacles in the progress towards a single global financial communication system because a single set of accounting standards cannot reflect the differences in national business practices arising from differences in institutions and cultures(Sawan, N and Alsagga, I , 2013).

Implementation of IFRSs by developing countries has significant challenges(Michas, 2010, Alp and Ustuntage, 2009 and Zhang et al.,2007). There are complexity of the standards, fair value issues, cost, regulation, lack of technical skills and knowledge in standards, inadequate education and training of accountants (Schachler et al., 2012; Laga, 2012; Masoud, 2014). Further, other issues are cultural issues, mental models, legal impediments, educational needs and political influences (Obazee, 2007).

Inadequate active markets needed for fair value determination may reduce the quality of accounting information presented in financial statements prepared in accordance with the IFRS (Ionaşcu et al (2011). Another challenge identified was that because IFRSs is principle- based, it may create avenue for earning management (Hong 2008; Chand, Patel & Patel 2005; Jeanjean & Stolowy 2008).

The other difficulties confronted are that the timely interpretation of standards, continuous amendment to IFRS, accounting knowledge and expertise possessed by financial statement users, preparers, auditors and regulators, and managerial incentive (Ball, Robin & Wu 2000). Therefore, the gist of the various research studies are that the challenges of IFRS in the emerging economies are the lack of relevant specific knowledge and of practical experience, the need of training and consultancy services, difficulties encountered in using the fair value concept, and the transition costs. An empirical study of the Chartered Accountants in India brought ought the following challenges of the implementation of IFRS in India (A. Srivatsava and P. Kulshreshtha, 2019). The data relating to the same is given in the table 2 below:

Table 2: Table showing the Challenges of IFRS Implementation in India

Statements	Mean	SD	5_SA	%	4_A	%	3_N	%	2_D	%	1_SD	%	T
Inadequate training facilities at huge cost is a road block to IFRS	4.03	.80	40	26.7	82	54.7	22	14.7	4	2.7	2	1.3	150
The fair value measurement is highly obstructive the execution of IFRS	3.91	.91	43	28.7	63	42	31	20.7	13	8.7	0	0	150
IFRS adoption requires major changes in IT infrastructure	4.12	.65	42	28	84	56	24	16	0	0	0	0	150
IFRS adoption requires changes in existing law	4.15	.69	44	29.4	88	58.7	14	9.3	4	2.7	0	0	150
IFRS adoption requires too much disclosure and changes in whole accounting process	3.85	.68	21	14	90	60	35	23.3	4	2.7	0	0	150
IFRS itself is complicated, hence it increases the risk of errors and omissions	3.34	.81	0	0	82	54.6	38	25.3	29	19.3	1	6.7	150
IFRS implementation will increase the burden of Accountants and auditors due to complexity of conversion	3.84	.61	14	9.3	102	68	30	20	4	2.7	0	0	150

Source: "The Benefits and Challenges of IFRS Adoption in India:The Dawn of a New Era", International Journal of Accounting and Financial Reporting, ISSN 2162-3082, 2019, Vol.9, No.4.pp334-350,Anubha Srivastava and Preeti Kulshreshtha.

Thus, it can be further narrated that the challenges of IFRS in different situations are asunder:

a. The cost of implementation of IFRS for small businesses will be higher and not absorbable while large businesses can manage to adjust the cost. The resources position of the Small and Medium Enterprises do not encourage them to train their staff or spend time for documentation adjustments.

b. The flexibility available with IFRS can lead to manipulation of records. It is also debated that the IFRS standards have the possibility of fraudulent manipulations.

c. For deriving the benefit of IFRS, there should be consistency of auditing and enforcement at a global level which will turn out to be a disadvantage in many cases of differences in practices.

d. The work load of accountants will increase significantly sometimes causing to inadvertent mistakes. The domestic accounting practices have to be completely revamped to make it converge with IFRS.

e. The transition period of domestic accounting practices to international practices can create additional problems of delay, discrepancies and depletion of quality.

f. One important requirement of IFRS implementation is the extreme need of reorienting the educational level of the employees, accountants and other practitioners. In many universities, IFRS is not even taught at business school level or at the level of teaching accounting.

g. It is argued by some researchers that there is a home-court bias in accounting and implementation of IFRS will create further complications and confusions. It is not the same through all the demographic area. The investors have a tendency to work with the accounts of the domestic practitioners more than an international system with which they are not exposed.

h. It is not that all the countries would like to fall in just because the big countries adopt IFRS. They have their own concerns and challenges. Corporate choosing to do business overseas might need to continue producing

2+ reports when necessary to comply with those standards. The disadvantages of the International Financial Reporting Standards will always affect adversely the smaller businesses which are the backbone of the economies of many countries.

Conclusion

Though the enforcement of IFRS is recommended by many researchers but the implementation of IFRS in many countries poses challenges too. IFRS convergence mechanism will bring few inherent challenges and issues like lack of required software, lack of human capital training, the huge cost involved in implementation and modification in rules and regulations, etc. However, the adoption of international accounting and auditing standards is not enough. There are three important links which exist in the enforcement sequence:

i. The top management must ensure preparation of financial statements in compliance with established standards,

ii. Auditors must act independently and judiciously to assure the compliance of financial statements with applicable accounting standards and represent a true and fair position of the company.

iii. Regulators must monitor the compliance with accounting standards and take appropriate actions against violators.

iv. As in the case of India, the Ministry of Corporate Affairs has already issued guidelines. For the banking and non-banking financial sectors, the Reserve Bank of India has already issued necessary instructions for the preparation of the ground for the project management, yet the awareness among the stakeholders is pretty much pathetic.

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