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State of play on convergence between International Financial Reporting Standards (IFRS) and national Generally Accepted Accounting Principles (GAAP) of India

1. INTRODUCTION AND LEGAL BASES

Since 1 January 2005, companies listed on an EU regulated market¹ have to use International Financial Reporting Standards (IFRS) as adopted by the EU for preparing their consolidated financial statements.² The Prospectus Regulation³ and the Transparency Directive⁴ extend the requirement to produce financial reports either on the basis of IFRS or on the basis of certain third countries national accounting standards equivalent to IFRS, to third country issuers making a public offer of securities in the EU and those whose securities are traded on an EU regulated market.

A mechanism⁵ to determine the equivalence of the Generally Accepted Accounting Principles (GAAP) from third countries was established in 2007. Accordingly, in 2008, the Commission identified as equivalent to IFRS the US GAAP and the Japanese GAAP on a permanent basis, and accepted financial statements using the GAAP of China, Canada, India, and South Korea within the EU on a temporary basis, until 31 December 2011. At the end of 2011, the Commission assessed the efforts made by the four countries that were found equivalent on a temporary basis. The temporary equivalence of the GAAPs of China, Canada, and South Korea was transformed into a permanent equivalence while the temporary equivalence of Indian GAAP was renewed for another 3-year period⁶, due to expire on 31 December 2014. In view of the upcoming expiry of this temporary equivalence, the Commission asked in February 2014 the European Securities and Markets Authority (ESMA) to provide an update on the state of play of the level of convergence of Indian GAAP towards IFRS. ESMA published its report in October 2014. The report highlights delays in the implementation of the convergence program, lists a number of differences from IFRS which could be significant in practice and raises some concerns related to the enforcement.

The present staff paper provides an update on the progress of India towards convergence with IFRS. It takes due account of the technical assessment provided by ESMA in October 2014 on the state of play of the converged Indian GAAP with the International Financial Reporting Standards.

¹ As defined in Article 4(1), point 14, of Directive 2004/39/EC.

² Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 (the "IAS Regulation").

³ Commission Regulation (EC) No 809/2004 of 29 April 2004 (the "Prospectus Regulation"). This Regulation implements Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 (the "Prospectus Directive").

⁴ Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 (the "Transparency Directive").

⁵ Commission Regulation (EC) No 1569/2007 of 21 December 2007 establishing a mechanism for the determination of equivalence of accounting standards applied by third country issuers of securities pursuant to Directives 2003/71/EC and 2004/109/EC of the European Parliament and of the Council (the "Equivalence Mechanism Regulation").

⁶ Commission Implementing Decision 2012/194/EU of 11 April 2012 amending Decision 2008/961/EC on the use by third countries' issuers of securities of certain third country's national accounting standards and International Financial Reporting Standards to prepare their consolidated financial statements OJ L 103, 13.4.2012, p. 49–50. and Commission Implementing Decision 2012/194/EU of 11 April 2012 amending Decision 2008/961/EC on the use by third countries' issuers of securities of certain third country's national accounting standards and International Financial Reporting Standards to prepare their consolidated financial statements OJ L 103, 13.4.2012, p. 49–50.

2. PROGRESS ON THE EQUIVALENCE OF INDIAN ACCOUNTING STANDARD

In January 2010, the Institute of Chartered Accountants in India (ICAI) and the Indian Government had made public commitments on a roadmap regarding the implementation of the Ind-AS (Indian standards converged with IFRS). The strategy followed by the Indian authorities regarding the convergence process has been to adopt IFRS as issued by the IASB and modify them for the specific Indian legal and economic context. However the transition to Indian Accounting Standards converged with IFRS (Ind-AS) was postponed in 2011. Following this postponement, the ICAI performed an impact analysis of Ind-AS in 2013 and subsequently published in March 2014 a new roadmap for the implementation of Ind-AS converged with IFRS. The new roadmap proposes that listed and large entities mandatorily use Ind-AS for the preparation of consolidated financial statements from 1 April 2016.

On 2 January 2015, The Ministry of Corporate Affairs (MCA) announced a revised roadmap for the implementation of Ind-AS that would be converged with IFRS. This roadmap entails a phase adoption: voluntary adoption of Ind-AS allowed for accounting periods beginning on or after 1 April 2015, mandatory adoption for all listed companies and companies having a net worth of INR 500 or more on or after 1 April 2016, mandatory adoption of companies having a net worth of INR 250 or more but less than INR 500 on or after 1 April 2017. This roadmap, will have to be translated into law before these Ind-AS become applicable. Moreover, the level of convergence of Ind-AS with IFRS will have to be re-assessed (see below).

In addition to the delays in the implementation of the convergence program, the ESMA report lists a number of differences between Indian converged standards and IFRS which could be significant in practice and raises some concerns related to the enforcement.

With respect to the level of convergence, the ICAI has since 2011 continued the process of developing the Ind-AS based on IFRS as initiated in the past. However the ICAI has in some cases adjusted these Ind-AS for the specific Indian legal and economic context. Consequently, some Ind-AS may constitute significant departures from IFRS⁷. Moreover, for some IFRS standards there may not be equivalent under Ind-AS⁸.

With respect to enforcement, the expertise in India regarding IFRS application and enforcement remains limited. Even though the ICAI has made a significant effort to prepare auditors and preparers for the implementation of Ind-AS, more practical experience will be necessary.

⁷ Examples of such departures from IFRS: Accounting for the excess value of net assets acquired over purchase consideration (converged Indian standard required recognition of the excess in equity directly or through other comprehensive income depending on evidence of bargain purchase and not in profit or loss as required under IFRS 3); Obligation to prepare consolidated financial statements (The draft *Ind-AS 110 – Consolidated financial Statements* removed some exemptions granted to parent companies under *IFRS 10 – Consolidated Financial Statements* when presenting consolidated financial statements).

⁸ Examples of IFRS standards with no equivalent: Accounting for agreements for the construction of real estate (no converged Indian standard has been issued and the method for revenue recognition follows the percentage of completion method and not the method required under IFRIC 15 – *Agreements for the Construction of Real Estate*); Accounting for biological assets (the converged Indian standard corresponding to IFRS 41 – Agriculture has not been released).

3. CONCLUSIONS

The Commission staff notes the further steps that have been undertaken by the authorities of India towards convergence of Indian accounting standards with IFRS. However, the Commission staff also observed that there have been multiple delays in the convergence of Indian accounting standards towards IFRS and in certain areas the progress remains limited. Indian accounting standards deemed to be converged with IFRS appear to have a number of differences from IFRS which could be significant in practice. The Commission staff welcomes the revised roadmap for implementation of Indian Accounting Standards converged with IFRS (Ind-AS) published by the Ministry of Corporate Affairs on 2 January 2015. However, uncertainties remain about the timetable for the adoption of legislative acts implementing Ind-AS and about the level of convergence between Ind-AS and IFRS. For these reasons and given the past multiple delays in this process, the Commission has decided to shorten the period during which Indian GAAP would be considered as equivalent. The period will expire on 31 March 2016 instead of 31 December 2017. This date has been chosen because the accounting period in India runs from 1 April of year X to 31 March of year X+1. Moreover, it corresponds to the date set in the Indian Government roadmap. Indeed, the roadmap requires that all listed companies use Indian GAAP converged with IFRS for the accounting periods beginning on or after 1 April 2016. This additional period should be sufficient to allow Indian authorities to implement the revised roadmap published by the Ministry of Corporate Affairs and should be considered as the last opportunity to implement it.

The Commission staff will continue to monitor the situation, assess the ongoing efforts by third countries converging to IFRS or intending to adopt IFRS, with the technical assistance of ESMA.