Accounting Standards – Introduction, History, Structure and Current Projects

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Introduction

Intention of preparation and presentation of Financial Statements:

Financial accounting and reporting are crucial in communication to:

- Shareholders
- Potential Investors
- Bankers
- Creditors
- Regulators

Background

What is the need for standardized language of financial performance?

- Communicate high quality information on Financial Statements.
- Consistency
- Comparability
- Reliability
- Transparency
- Best practices
- Benchmarking

Basic Objective

Basic objective of accounting standards – to ensure standardization in the presentation of accounts.

Accounting Standards are a set of **principles** that entities follow in **Financial Statement preparation**.

Standardized disclosure of entity's financial position and performance.

Compliance with applicable legal and regulatory framework.

History of Audit and Accounting Standards in India

History of Accounting and Auditing in India

- **Accounting has a long history in India.**
- **Kautilya's Arthashastra deals with concepts, rules and regulations pertaining to business, accounting, auditing and risk management.**
- **Evolution of present-day Indian accounting system can be traced back to as early as 16th century, when India had trade links to Europe and Central Asia through the "Silk Route".**
- **Changes in scale and complexities in economy have brought about changes to financial reporting and accounting standards have a crucial role to play in this scenario.**

History of Accounting and Auditing in India

Year	
1857	Joint-stock companies Act of 1857 – incorporation and regulation of joint-stock companies and other associations, with or without limited liability for members.
1866	The Indian Companies Act 1866 – Mandated companies to maintain accurate records and have their accounts audited.
1913	The Indian Companies Act, 1913 – Regulate trading companies and associations in India. Laid foundation for modern corporate governance in India.

History of Accounting and Auditing in India

Year	
1918 – 1920	Government Diploma in Accounting (GDA) was launched in Mumbai. On completion of 3-year articleship under an approved accountant and passing of qualifying examination, the candidate would become eligible for the grant of an "Unrestricted Certificate". Certificate from the local government to act as an auditor, as the basic qualification. The Unrestricted Certificate holder person had the freedom to act as an auditor throughout the country, but a Restricted Certificate bearer could only act within the allotted province or language specified in the certificate. Issue of Restricted certificates was discontinued in 1920.
1930	Register of Accountants to be maintained by the Government of India to exercise control over the members in practice. Those whose names found entry here were called Registered Accountants (RA). Auditors were allowed to practice throughout India.

History of Accounting and Auditing in India

Year	
1932	First Accountancy Board was formed. The Board was to advise the Governor General in Council on matters relating to accountancy and to assist him in maintaining standards of qualification and conduct required of Auditors.
1933 1943	First examination held by the Indian Accountancy Board. GDA was abolished.
1949	The Chartered Accountants Act, 1949 passed on 1st May, effective from 1st July and the Institute of Chartered Accountants of India was born on 1st July 1949.
1956	The Companies Act, 1956 – provided the legal framework for companies to operate in India, empowering the government to regulate them and ensuring a structured business environment.
1977	**The ICAI constituted the "Accounting Standards Board" on April 21, 1977.** **To formulate "Accounting Standards" to establish sound and robust**

The Accounting Standards Board (ASB)

- ASB includes representatives from ICAI, representatives from Government including Revenue, RBI, IRDA, MCA.
- Takes into consideration "Accounting Standards" at International level and sets National Standards based on the same, ensuring that the Accounting Standards are broadly aligned to Global Accounting principles.
- ICAI notified 11 accounting standards between 1977 and 1988, made in a consultative manner by ASB, but these standards lacked statutory recognition.
- Statutory recognition and legal force was established through sub-sections (3A), (3B) and (3C) to Section 211 of Companies Act 1956, every Balance Sheet and Profit and Loss account of the Company complied with Accounting Standards, prescribed by the Central Government in consultation with NACAS (National Advisory Committee on Accounting Standards).
- Accrual method of accounting evolved with growth of the "Company" form of organization .
- Accrual method was made mandatory for Companies under Section 209(3) of Companies Act 1956.

Procedure for the issue of Accounting Standards:

- ASB study group to formulate preliminary draft.
- Issues exposure draft (ED) for public comments and comments from specified bodies (industry associations, regulators, Stock Exchanges) after consideration of preliminary draft.
- Finalizes the draft Accounting Standard for consideration of Council.
- Draft approved by Council is recommended to NACAS.
- NACAS recommends the Standard to the Government of India (MCA) after its review and modifications, if any, in consultation with ICAI.
- Government of India (MCA) notifies the Accounting Standard.

Important milestones in Accounting Standards in India:

1979 – Preface to Statement of AS and AS 1 issued.

1987 – Mandatory status of AS 4 and AS 5.

1991 – Mandatory status of AS 1, AS 7, AS 8, AS 9, AS 10 and AS 11 for Corporate Entities.

1999 – Legal recognition to ASs issued by ICAI under Companies Act 1956.

2000 – 2003 – 12 AS were issued based on IASs towards convergence with IAS.

2002 – Insurance Regulatory and Development Authority (IRDA) to comply with Accounting Standards

Important milestones in Accounting Standards in India:

2003 – RBI issued guidelines to Banks on compliance with Accounting Standards to ensure strict compliance with AS issued by the ICAI.

2006 – MCA notified separate AS under Companies AS Rules, 2006 (ASB of ICAI and NACAS)

2006 – ASB to constitute a task force for convergence with IFRS.

2007 – ASB and Council accepted recommendations of Task force for IFRS convergence.

2010 – 11 – Ind AS prepared by ICAI, approved by NACAS and notified by MCA.

2016 – MCA notified revised AS 2, AS 4, AS 10, AS 13, AS 14, AS 21 and AS 29.

Accounting Standards – Applicability criteria

Accounting Standards

- The Central Government after consultation with National Financial Reporting Authority (NFRA) notified **The Companies (Accounting Standards) Rules, 2021**, on 23rd June 2021 through MCA (Ministry of Corporate Affairs) and published in the Gazette of India.

- Accounting Standards are applicable to companies other than those that follow IND–AS (Indian Accounting Standards in accordance with The Companies (Indian Accounting Standards) Rules, 2015)

Accounting Standards

Companies (Accounting Standards) Rules, 2021
• **Applicability criteria:** Accounting Standards are applicable to those companies, whose: • Equity / debt securities are **not** listed or not in the process of getting listed (inside/ outside India). • Unlisted company having **net-worth less than Rs. 250 crores.** • Company who is **not** a subsidiary/ associate/ JV of a company to whom Ind AS is applicable.

Accounting Standards

- Following entities should get their financial statements prepared in compliance with Accounting Standards:
  - Banks
  - Companies whose securities are listed or are in the process of being listed on SME exchange as referred to in Chapter XB of SEBI (Issue of capital and Disclosure Requirements) Regulations, 2009) – (voluntary adoption of Ind AS allowed).
  - Companies whose securities are listed or are in the process of being listed on the Institutional Trading Platform without IPO (Chapter XC of SEBI (Issue of capital and Disclosure Requirements) Regulations, 2009) – (voluntary adoption of Ind AS allowed).

Accounting Standards – Structure

List of Accounting Standards

AS 1	Disclosure of Accounting Policies
AS 2	Valuation of Inventories (revised 2016)
AS 3	Cash Flow Statements
AS 4	Contingencies and Events occurring after Balance Sheet Date
AS 5	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
AS 7	Construction Contracts
AS 9	Revenue Recognition

AS 10	Property, Plant and Equipment
AS 11	Effects of Changes in Foreign Exchange Rates (revised 2003)
AS 12	Accounting for Government Grants
AS 13	Accounting for Investments (revised 2016)
AS 14	Accounting for Amalgamations (rev 2016)
AS 15	Employee Benefits
AS 16	Borrowing Costs
AS 17	Segment Reporting
AS 18	Related Party Disclosures

List of Accounting Standards

AS 19	Leases
AS 20	Earnings per share
AS 21	Consolidated Financial Statements (rev 2016)
AS 22	Accounting for taxes on income
AS 23	Accounting for Investments in Associates in Consolidated financial statements
AS 24	Discontinuing operations

AS 25	Interim Financial Reporting
AS 26	Intangible Assets
AS 27	Financial reporting of interest in Joint Ventures
AS 28	Impairment of Assets
AS 29	Provisions, Contingent Liabilities and Contingent Assets

Exemptions

Entities are bifurcated into Level I, Level II and Level III company and non-company enterprises and certain exemptions/ relaxations have been granted by the Central Government to:

- Small and Medium sized companies
- One-person company
- Small company
- Dormant Company
- Level II and
- Level III enterprises

Structure of Accounting Standards

Accounting Standards

• Built upon established principles.
• Standardization of diverse accounting policies.
• Both Management and Auditors require in-depth knowledge of accounting standards.
  • Management – to record financial data accurately
  • Auditor – to verify if the accounting records are accounting standard compliant

Structure of Accounting Standards

Accounting Standards
• Primary purpose is to systematically record, classify and summarize financial transactions. • On-going (continuous process of) recording and management of Financial data. • Focus is to record transactions in compliance with applicable laws and regulations. • Accounting treatment in Financial Statements

Structure of Accounting Standards

Accounting Standards

• Guidance in preparation of Financial Statements and framework for financial reporting.
 	
• Consistency and Comparability of Financial Statements across years, across sectors, across countries.
 	
• Documentation and record-keeping of:
  • Transactions recorded
  • Evidential matter in complex accounting scenario
  • Financial Statements
  • Notes to the Financial Statements

Reporting requirements

Reporting on compliance with Accounting Standards

By Auditor
• Auditors report on the financial statements' conformity with accounting standards prescribed under Sec 133 of the Companies Act 2013, and • The Companies (Indian Accounting Standards) Rules, 2015 (or) • The Companies (Accounting Standards) Rules, 2021, as applicable.

Current Projects

Current Projects – Accounting Standards

Exposure draft of Accounting Standards for LLPs has been finalized and issued for comments till Feb 28, 2025.

ASB is working on the project of revision of Accounting Standards applicable to whom Ind AS is not applicable.

The entire set of revised Accounting Standards will consist of 32 standards, including a Standard on transition from existing AS to Revised AS.

So far, 28 revised AS have been developed and approved by the Council after due process

Exemptions

Entities are bifurcated into Company and Non- company which in turn are bifurcated into Level I, Level II Level III or Level IV enterprises and certain exemptions/ relaxations have been granted by the Central Government to them depending on the category to which they belong

Interplay of Auditing Standards and Accounting Standards

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Small and Medium Sized Company (SMC)

If the below conditions are satisfied at the end of the accounting period then the company may be classified as an SMC

Small and Medium-Sized Company (SMC) as defined in Clause 2(e) of the Companies (Accounting Standards) Rules, 2021:

"Small and Medium Sized Company" (SMC) means, a company-

(i) whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India;

(ii) which is not a bank, financial institution or an insurance company;

(iii) whose turnover (excluding other income) does not exceed two hundred and fifty crore rupees in the immediately preceding accounting year;

(iv) which does not have borrowings (including public deposits) in excess of fifty crore rupees at any time during the immediately preceding accounting year; and

(v) which is not a holding or subsidiary company of a company which is not a small and medium-sized company.

CRITERIA FOR CLASSIFICATION OF NON-COMPANY ENTITIES AS LAID OUT BY ICAI

Level I Entities

Level I entities are those non-company entities which fall in any one or more of the following categories, at the end of the relevant accounting period:

(1) Entities whose securities are listed or are in the process of listing on any stock exchange, whether in India or outside India.

(2) Banks (including co-operative banks), financial institutions or entities carrying on insurance business.

(3) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds rupees two-fifty crore in the immediately preceding accounting year.

(4) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees fifty crore at any time during the immediately preceding accounting year.

(5) Holding and subsidiary entities of any one of the above.

Level II Entities

Level II entities are those non-company entities which are not Level I entities but fall in any one or more of the following categories are classified as :

(1) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds rupees fifty crore but does not exceed rupees two-fifty crore in the immediately preceding accounting year.

(2) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees ten crore but not in excess of rupees fifty crore at any time during the immediately preceding accounting year.

(3) Holding and subsidiary entities of any one of the above.

Level III Entities

Non-company entities which are not covered under Level I and Level II but fall in any one or more of the following categories are classified as Level III entities:

(1) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds rupees ten crore but does not exceed rupees fifty crore in the immediately preceding accounting year.

(2) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees two crore but does not exceed rupees ten crore at any time during the immediately preceding accounting year.

(3) Holding and subsidiary entities of any one of the above.

Level IV Entities

Non-company entities which are not covered under Level I, Level II and Level III are considered as Level IV entities.

Background

What is the intention of Financial Statements?

To meet the common information needs of a wide range of users, viz:

- Shareholders
- Potential Investors
- Bankers
- Creditors
- Regulators

Background

Why standardized language of financial performance?

- Communicate high quality information on Financial Statements.
- Consistency
- Comparability
- Reliability
- Transparency
- Best practices
- Benchmarking

Interplay of Auditing and Accounting Standards: What it means

- Accounting Standards are a set of **principles** that entities follow in **Financial Statement preparation**.
- **Standardized disclosure** of entity's financial position and performance.
- **Compliance** with applicable legal and regulatory framework.
- Standards on Auditing ensure that these **accounting standards are applied appropriately.**
- Lends **credibility** and wider **acceptability** of Financial Statements
- **Benchmark performance** that can be measured and evaluated at Global level.
- Ensuring right approach in **complex/ emerging areas**, in engagements.

Interplay of Auditing and Accounting Standards:

Accounting Standards	Auditing Standards
• Built upon established principles. • Recording and presentation of Financial data • Both Management and Auditors require in-depth knowledge of accounting standards.	• Built upon established principles. • Provides framework for verification the accuracy of financial data presented. • Auditors report on the financial statements' conformity with accounting standards prescribed.

Interplay of Auditing and Accounting Standards:

Accounting Standards	Auditing Standards
• Primary purpose is to systematically record, classify and summarize financial transactions. • On-going (continuous process of) recording and management of Financial data. • Focus is to record transactions in compliance with applicable laws and regulations.	• Primary purpose is to independently verify the accuracy and fairness of the financial statements. • Reviewing and assessing financial records after recording transactions. • Focus is to identify discrepancies, misstatement due to error or fraud.

Interplay of Auditing and Accounting Standards:

Accounting Standards	Auditing Standards
• Guidance in preparation of Financial Statements and framework for financial reporting. • Consistency and Comparability of Financial Statements across years, across sectors, across countries.	• Verifying the accuracy of the Financial Statements. Guidance to verify adherence to Accounting Standards and other legal and regulatory framework. • Assists in verification of accuracy and reliability of FS.

Interplay of Auditing and Accounting Standards:

Accounting Standards	Auditing Standards

• Documentation and record-keeping of:
  • Transactions recorded
  • Evidential matter in complex accounting scenario
  • Financial Statements
  • Notes to the Financial Statements
	• Documentation and record-keeping of:
	  • Ethics and Independence
	  • Audit planning
	  • Audit execution
	  • Audit findings
	  • Discussion with management
	  • Audit conclusion and reporting

Interplay of Auditing and Accounting Standards:

Accounting Standards	Auditing Standards

• Auditors report on the financial statements' conformity with accounting standards prescribed under Sec 133 of the Companies Act 2013, and
  • The Companies (Indian Accounting Standards) Rules, 2015 (or)
  • The Companies (Accounting Standards) Rules, 2021, as applicable.
	• Auditor should report that the audit was conducted in accordance with Standards on Auditing specified under Sec 143(10) of the Companies Act, 2013.

Interplay of Auditing and Accounting Standards:

Accounting Standards	Auditing Standards
• Sec 134 (5), Companies Act 2013 mandates Director's Report to include a statement on adherence to accounting standards, confirming that the company has complied with all applicable standards in preparing Financial Statements.	• SA 706 – Emphasis of Matter paragraphs and Other Matter paragraphs in Independent Auditor's Report – It is the auditor's responsibility to read and report on the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements, or the knowledge obtained during the course of audit or otherwise appears to be materially misstated.

The interplay between Auditing and Accounting Standards

- Accounting Standards and Auditing Standards are distinct yet interconnected.
- Accounting standards help in recording and reporting of financial statements while auditing standards help verify these transactions.
- Conversely, audit findings are used to improve financial reporting practices.
- Adherence to "Accounting standards" is paramount for management as it marks the initiating point through which transactions are recorded.
- Auditing Standards are crucial for auditors to verify correctness and accuracy, compliance with accounting standards and regulatory requirements.

Accounting Standards and Auditing Standards on Estimates

AS 2 – Valuation of Inventory	SA 540 – Auditing Accounting Estimates, including Fair Value accounting estimates and related disclosures
Determination of the value at which inventories are carried in FS is a crucial item both from management and audit perspective. This also includes valuation of WIP, Net realisable value of stock, interest and borrowing costs to be added to inventory, provision for obsolescence.	Audit risk involved here is the susceptibility of accounting estimate and related disclosures to a lack of precision in measurement thereby affecting the true and fair view of the financial position and performance. Requires understanding of the Accounting Standard, how management identifies events/ conditions that give rise to these accounting estimates, understanding and evaluating the correctness of the underlying data and assumptions, method used to calculate the estimate, relevant controls.

Risk of material misstatement

AS 9 – Revenue Recognition

In revenue recognition, we are mainly concerned about the

- Timing of revenue recognition
- Amount of revenue recognition
- Uncertainties if any, involved in the points above

When performance consists of more than one act, revenue is recognised proportionately with reference to the performance and percentage of completion of each act.

SA 315 - Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment

In this scenario and as per guiding standard SA 315, the auditor should identify what are all the risks involved (in this case the percentage of completion based on which revenue recognised), what can go wrong at the assertion level, relevant controls that are to be tested, consider likelihood of risk of fraud or misstatement due to internal/ external pressure, identifying control activities surrounding these risks and testing the same.

Related Party Transactions

AS 18 – Related Party Disclosures	SA 550 – Related Parties
This accounting standard stresses on the general presumption that transactions reflected in financial statements are at arm's length between parties which may sometimes not hold good when a related party or related parties are involved. Arm's length is not the pricing alone, terms and conditions of a contract with a third party may be different from the contract with a related party for the provision of the exact same goods or service (credit terms or discount terms, management services etc)	Because related parties are not independent of each other and the inherent risk of material misstatement due to fraud or error exists, the auditor has a responsibility to perform audit procedures to identify, assess and respond to RoMM from entity's failure to appropriately account/ disclose related party transactions / relationships and its correctness, accuracy and genuineness. Related party relationships may present a greater opportunity for collusion, concealment or manipulation by

Using the work of an expert

AS 15– Employee Benefits	SA 620 – Using the work of an Auditor's expert
Accounting for Employee benefits includes: • Short-term employee benefits – salary, bonus • Non- monetary benefits – medical care, housing • Post-employment benefits – Gratuity, pension • Other long-term benefits – Sabbatical leave, deferred compensation. • Termination benefits Each category mentioned above has different characteristics and therefore	Using the work of an expert does not reduce auditor's reporting responsibilities with respect to the audit opinion. The auditor has to evaluate • the necessary competence, capabilities, objectivity for audit purposes. • The correctness of base data (employee data incl salary, age, date of joining and such other information) provided by the company's HR. • Analytical procedures.