

The Trouble of Accounting Standards

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Abstract: *We know that Generally Accepted Accounting Principles (GAAP) aims at bringing uniformity and comparability in the financial statements. It can be seen that at many places, GAAP permits a variety of alternative accounting treatments for the same item. For example, different methods for valuation of stock give different results in financial statements. Such practices sometimes can misguide intended users in taking decision relating to their field. Keeping in view the problems faced by many users of accounting, a need for the development of common accounting standards was aroused*

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I. INTRODUCTION

CONCEPT OF ACCOUNTING STANDARDS

We know that Generally Accepted Accounting Principles (GAAP) aims at bringing uniformity and comparability in the financial statements. It can be seen that at many places, GAAP permits a variety of alternative accounting treatments for the same item. For example, different methods for valuation of stock give different results in financial statements. Such practices sometimes can misguide intended users in taking decision relating to their field. Keeping in view the problems faced by many users of accounting, a need for the development of common accounting standards was aroused.



MEANING OF ACCOUNTING STANDARDS:

Accounting standards are the written statements consisting of rules and guidelines, issued by the accounting institutions, for the preparation of uniform and consistent financial statements and also for other disclosures affecting the different users of accounting information.

Accounting standards lay down the terms and conditions of accounting policies and practices by way of codes, guidelines and adjustments for making the interpretation of the items appearing in the financial statements easy and even their treatment in the books of account.

INDIAN ACCOUNTING STANDARD:

Indian Accounting Standard (abbreviated as Ind_AS) is the accounting standard adopted by companies in India and issued under the supervision of Accounting Standards Board (ASB) which was constituted as a body in the year 1977. ASB is a committee under Institute of Chartered Accountants of India (ICAI) which consists of representatives from government department, academicians, other professional bodies viz. ICAI, representatives from ASSOCHAM, CII, FICCI, etc. ICAI is an independent body formed under an act of parliament.

The Ind AS are named and numbered in the same way as the International Financial Reporting Standards (IFRS). National Financial Reporting Authority (NFRA) recommend these standards to the Ministry of Corporate Affairs (MCA). MCA has to spell out the accounting standards applicable[1] for companies in India. As on date MCA has notified 40 Ind AS (Ind AS 11 is omitted by companies).

S. This shall be applied to the companies of financial year 2015-16 voluntarily and from 2016-17 on a mandatory basis.

Based on the international consensus, the regulators will separately notify the date of implementation of Ind-AS for the banks, insurance companies etc. Standards for the computation of Tax has been notified as ICDS in February 2015



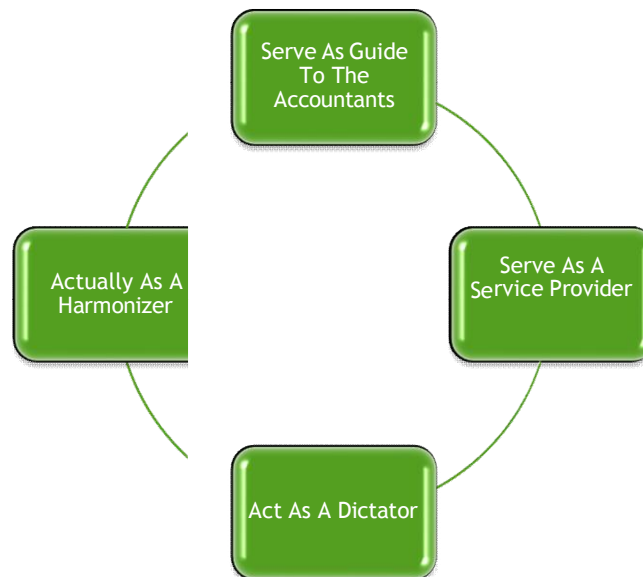
NATURE OF ACCOUNTING STANDARDS:

Serve as a guide to the accountants:

Accounting standards serve the accountants as a guide in the accounting process. They provide basis on which accounts are prepared. For example, they provide the method of valuation of inventories.

Serve as a service provider:

Accounting standards comprise the scope of accounting by defining certain terms, presenting the accounting issues, specifying standards, explaining numerous disclosures and implementation date. Thus, accounting standards are descriptive in nature and serve as a service provider.



Act as a dictator:

Accounting standards act as a dictator in the field of accounting. Like a dictator, in some areas accountants have no choice of their own but to opt for practices other than those stated in the accounting standards. For example, Cash Flow Statement should be prepared in the format prescribed by accounting standard.

Act as a harmonizer:

Accounting standards are not biased and bring uniformity in accounting methods. They remove the effect of diverse accounting practices and policies. On many occasions, accounting standards develop and provide solutions to specific accounting issues. It is thus clear that whenever there is any conflict on accounting issues, accounting standards act as harmonizer and facilitate solutions for accountants.

NEED FOR ACCOUNTING STANDARDS

Accounting is an information system and its main aim is to provide financial information to a number of parties such as investors, management, creditors, government etc. Such information is provided through a set of financial statements such as profit and loss account, balance sheet, and cash flow statement etc.

The set of financial statements of a company should depict a true and fair view of its operating results and financial position. There is need to harmonise and standardise the different accounting policies so that financial statements become consistent and comparable.

Certain standard must be followed for preparing the financial statements, so that there is minimum ambiguity and uncertainty about the figures contained in financial statement.

BENEFITS OF ACCOUNTING STANDARDS

There are many benefits of accounting standards. Let us discuss the main benefits of Accounting Standards one by one.

Standardized Accounting:

Perhaps the most important advantage of the FASB standard setting for businesses is the uniform set of accounting principles it promotes. The FASB clearly states the generally-accepted accounting principles that businesses must follow to avoid confusion. For example, the FASB prevents businesses from using one method for calculating inventory at the beginning of a fiscal year and finishing the year with another method. Without the accounting standards set forth by the FASB, businesses could use accounting methods that portray financial data inaccurately to investors.

Problem Identification:

The FASB standard setting provides a framework upon which potential accounting problems are identified and corrected. Because all businesses in the US use the same accounting principles, any problems or inadequacies in the accounting process are quickly identified and reported to the FASB. The FASB then investigates the problem and, if needed, modifies or writes a new accounting rule for the accounting process. For example, if businesses find that reporting a certain type of liability on their income statement unfairly lowers their net income, they can appeal to the FASB so that it can identify problems with the standard setting.



Private Regulation:

The FASB is a private entity with no affiliation to the US government. Despite this, the Securities and Exchange Commission relies on the FASB to set the accounting rules that all companies in the US must follow. The SEC can technically create an accounting oversight board or government agency to set accounting rules. However, using the FASB eases the burden on the US government and lets the private sector dictate accounting rules.

International Accounting Standard:

The FASB is advantageous because it actively promotes an internationally recognized set of accounting rules. Globalization has deeply connected foreign financial markets; a standard set of accounting rules would make financial reporting more accurate and fairer between countries. One of the goals of the FASB is to make financial reporting more uniform globally with the cooperation of the International Accounting Standards Board (IASB).

Guider:

Accounting Standards serve as a guide for the whole accounting system. Accounting standards govern the manner in which financial statements are prepared and presented.

Mandatory to follow:

All companies must have to follow the accounting standards; these guidelines are not optional in nature.

Brings uniformity:

It sets the same guidelines and standards for every business for accounting treatments. Companies are required to prepare & present financial statements as per the same accounting standards.

For example, each company has to prepare its balance sheet according to format given in schedule III of companies act.

Flexible:

In many cases, companies are free to adopt any method from the option of different accounting practices. As in case of accounting for depreciation companies can adopt any depreciation method (straight line or written down method) according to their will.

Avoids frauds and data manipulation:

It aims at reducing the errors & chances of manipulation of data by management. Companies are strictly bound to follow the guidelines of accounting standards.

Comparability:

All companies follow the same guidelines for the same accounting treatments. This makes the comparison between financial statements possible and easy.

Assist auditors:

These standards help auditors in verifying the correctness of company accounts. Accounting standards provides all accounting rules and regulations to be followed in a written format that enables auditors to follow uniform practices

LIMITATIONS OF ACCOUNTING STANDARDS

There are a few limitations of Accounting Standards as well. The regulatory bodies keep updating the standards to restrict these limitations.



Difficulty between Choosing Alternatives:

There are alternatives for certain accounting treatments or valuations. Like for example, stocks can be valued by LIFO, FIFO, weighted average method, etc. So, choosing between these alternatives is a tough decision for the management. The AS does not provide guidelines for the appropriate choice.

Restricted Scope:

Accounting Standards cannot override the laws or the statutes. They have to be framed within the confines of the laws prevailing at the time. That can limit their scope to provide the best policies for the situation.

Brings inflexibility and rigidity:

Accounting standards basically establish all principles and rules for accounting treatment. Every company is required to follow the same principles constantly



Time consuming:

Implementation of accounting standards requires many steps to be followed to prepare financial report. It makes the process of preparing financial statements complex & time-consuming.

WHAT ARE ACCOUNTING PROBLEMS?

Accounting problems are issues resulting in material financial statement errors, undetected fraud due to inadequate internal control, misapplication of generally accepted accounting principles (GAAP accounting standards), regulatory noncompliance, and cybersecurity risks. Accounting problems may have unfavourable cash flow impacts and misstate business profitability.

WHAT CAUSES ACCOUNTING PROBLEMS?

Some accounting problems are caused by using outdated software technology for accounting. Intentional fraud due to greed and poor internal control causes other financial issues. Low staffing levels can cause accounting problems. Not training the financial team causes accounting problems related to improperly applying GAAP.

The business must defend itself against cybersecurity attacks and stay up-to-date on changing regulatory compliance issues.

HOW DO BUSINESSES SOLVE ACCOUNTING PROBLEMS?

Financial professionals in businesses should use software with advanced technology capable of handling current accounting standards, including revenue recognition and lease accounting, and regulatory requirements to avoid or solve significant accounting problems.

Requiring CPA employees and accountants to take relevant continuing education courses regularly can also help businesses solve accounting problems. Adequate staffing levels help accountants solve accounting issues.

Top management must communicate an ethical tone, corporate values, employee empowerment, and key expectations

COMMON ACCOUNTING PROBLEMS

Revenue Recognition

Improperly applying GAAP revenue recognition standards, creating fraudulent revenue schemes, including improper accounting for consignments and third-party inventory shipments beyond the level of possible usage, and using unreasonable estimates, are revenue recognition problems.



Lease Accounting

Changes to GAAP lease accounting standards require lessee companies to capitalize their operating leases with tenant right of use (ROU) and a term of over twelve months. Shorter operating leases (including office space leases) can still be recorded monthly as rent expenses. The leases are amortized over time

Payroll Errors

If a small business decides to calculate its own payroll, payroll taxes, and benefits, it’s possible that payment errors and accounting problems will occur. Payroll problems like miscalculating paychecks for salary expenses and hourly wages hurt employee morale and productivity.

Cash Flow Statement

The cash flow statement may include errors in classification by activity type and may not include restricted cash, a newer GAAP requirement. Cash flow statement classification errors may include misclassifying the type of activity for interest and dividends received and paid. Interest received and paid is an operating activity in the cash flow statement. Dividends received are an operating activity, and dividends paid are a financing activity in the cash flow statement.

The CPA firm, RSM, summarizes U.S. GAAP (vs IFRS) classification for certain items in the cash flow statement, including interest and dividends and restricted cash.



Not Enough Financial Analysis

An accounting team without efficient accounting systems is spending too much time closing the books, leaving less time for value-added work. Financial analysis adds value by calculating ratios, spotting and managing business trends, and providing decision support for new opportunities.

Regulatory Non-Compliance

Regulatory compliance covers different areas, including taxation, data privacy and security, sanctions lists like OFAC, and the Foreign Corrupt Practices Act (FCPA).

The Foreign Corrupt Practices Act covers not making bribes in foreign countries. And the FCPA's scope goes far beyond preventing bribes.

Violations of the Foreign Corrupt Practices Act and other regulations could result in:

Massive fines for companies and convicted individuals

Imprisonment

Tarnishing a company's and convicted individual's business reputation and ethics

II. CONCLUSION

Accounting standards are written statements containing rules and guidelines approved by accounting institutions for the preparation of coherent and consistent financial statements, as well as other disclosures affecting the various users of accounting information.