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M Susruth
Assistant Professor
Department of Business Management Bharathi Institute of Business Management Warangal, Telangana, India

Financial statement effect of adopting IFRS: A study on glenmark pharmaceuticals Ltd

M Susruth

Abstract
India, one of the fastest growing global economies is on the verge of converging with International Financial Reporting Standards (IFRS). As on date 123 countries across the globe have converged with IFRS, India is soon to join the bandwagon. The Ministry of Corporate Affairs (MCA) notified 35 Indian Accounting Standards converged with International Financial Reporting Standards (henceforth called Draft IND AS). The Ministry of Corporate Affairs laid out a roadmap for IFRS convergence, to be conducted in phases, for first-time adoption in India. In the first phase, it will be implemented at companies that have a net worth of over Rs.1, 000 crores from April 1, 2015. The second phase will begin from April 1, 2016 and involve both listed and unlisted companies with a net worth of over Rs.500 crores but less than Rs.1, 000 crores. Consequently, the companies will need to convert their accounts from Indian GAAP to IFRS. This paper discusses the influence of international financial reporting standards on financial statements and ratios, and Concluded that IFRS would increase the comparability between financial statements. Balance Sheet and Profit and Loss Account of various companies and to analyze some important ratios across the nation.

Keywords: IFRS, convergence, liquidity, profitability, GAAP

Introduction
International Financial Reporting Standards (IFRS) are designed as a common global language for business affairs so that company accounts are understandable and comparable across international boundaries. They are a consequence of growing international shareholding and trade and are particularly important for companies that have dealings in several countries. To make well-informed decisions regarding their internationally diversified portfolios, investors need to compare the financial performance of companies in different countries. IFRS is a set of international accounting standards stating how particular types of transactions and other events should be reported in the financial statements. The basic purpose of such thing is to bring about uniformity in the language of business that is reporting. This will help in listing of companies across borders. The term IFRS in itself comprises of IFRSs as issued by the IASB, IAS issued by IASC, the interpretations issued by the Standing Interpretations Committee (SIC) and the International Financial Reporting Interpretations Committee (IFRIC) of the IASB. Globalization of business environment made companies to list on stock exchange and in turn intensified the need for consistent worldwide reporting standards. IFRS fulfills this need by creating comparable, reliable, and transparent financial statements to facilitate greater cross-border capital raising, trade and better corporate governance practices. Thus, acceptance of IFRS is gaining momentum across the globe.
IFRS are developed and approved by an independent, not-for-profit Organization called the International Accounting Standards Board (IASB). Sometimes, IFRS also called International Accounting Standards (IAS) but they are not similar to each other. International Accounting Standards were issued between 1973 and 2001 by International Accounting Standards Committee (IASC) and IFRS standards were published from 2001 onwards by IASB (which succeeded the IASC). At present, thirteen IFRS have been developed and issued.

Correspondence
M Susruth
Assistant Professor
Department of Business Management Bharathi Institute of Business Management Warangal, Telangana, India

Objectives of IFRS
Harmonization is the necessity of modern globalized era because various factors like cross border investments, interdependence on trade, increase of Business complexities, global financial crisis, global slowdown and mobility of capital and people across the globe, are significantly influencing the world economy. Therefore, the main objective of IFRS development is harmonization in financial statements reporting. Some additional objectives are:
1. To create the global financial reporting infrastructure.
2. To generate sound business sense among the beneficiaries.
3. To generate the dimensions of fair presentation of financial statement
4. To maintain higher transparency of financial statement and mobility of capital

Review of Literature
Dr. K. V. Achalapathi and Dr. P. Bhanu Sireesha (2015) the study examines the effects of IFRS adoption on the financial ratios in Indian companies. To analyze the samples, financial ratios were used under the categories: stability, liquidity, profitability and investment valuation.
Dr. Vidhi Bhargava and Divya Shikha (2013) [1] the study emphasizes that IFRS is a fair vale principles based accounting which will improve quality of disclosures and enhance international comparability and understanding of financial statements.
Shibu das (2013) [2] the study concluded that IFRS is the new concept of financial reporting and communicating to the existing and prospective investors. It is a new concept and it is not fully familiar the Indian corporate entities.
S.P. Srivastava and Sanjay Kumar Patel (2009) [3] this paper conclude that adoption of IFRS in india has significantly changed the contents of financial statements as more refined measurements of performance and state of affairs, and enhanced disclosures leading to greater transparency.
Daske *et al* (2008) [4] found that firms adopting IFRS in the year of mandatory adoption experience large increases in market liquidity but mixed results for the cost of capital.
Kannan (2003) [16] regarding international standards with respect to banking operations and importance of corporate financial reporting in corporate governance and documentation of the changes occurred in corporate reporting practices and they provided justifiable suggestions for their gradual introduction in the Indian banking sector.
Dangwal and Singh (2005) [12] made certain valuable observations concerning quality of financial reporting which enables the banks to capitalize their underlying strengths, disclosure practices and social viability after undertaking a study of certain interesting issues with regard to the financial reporting of banking companies in India.
Siqi Li (2010) carried out a study of 1084 European Union firms during the period of (1995-2006), concluded that on average, the IFRS mandate significantly reduces the cost of equity for mandatory adopters. And also the reduction is present only in countries with strong legal enforcement and that increased disclosures and enhanced information comparability are two mechanisms behind the cost of equity reduction.
Cai& Wong (2010) [11] 2undertook a study of global capital markets and summarized that the capital markets of the countries that have adopted IFRS have higher degree of integration among them after their IFRS adoption as compared to the period before the adoption.
Lantto & Sahlstrom (2009) [9] also undertook a study of key financial ratios of companies of Finland and later found that the adoption of IFRS changes the magnitude of the key accounting ratios and also showed that the adoption of Fair Value Accounting rules and stricter requirements on certain Accounting issues are the reasons for the changes observed in Accounting Figures and financial ratios.
Barth (2008) [5] undertook a study of financial data consisting of 21 countries examined whether application of IAS/IFRS is associated with higher accounting quality and the findings of the study confirmed that firms applying IAS/IFRS evidence less earnings management, more timely loss recognition and more relevance of accounting numbers. The study also found out that the Firms applying IAS/IFRS experienced an improvement in accounting quality between the pre-adoption and post adoption period.

Objectives of the Study
- ❖ To review the present scenario of IFRS in India
- ❖ To highlight the impact of IFRS on Pharmaceuticals Companies.
- ❖ To explores the impact of IFRS on financial performance and compare the consolidated financial statement of Glenmark Pharmaceuticals as per Indian GAAP and IFRS.

Methodology
The study is based on secondary data, collected from published annual reports for a period of 2015-16. The consolidated financial statements as per GAAP are compared with the consolidated financial statements under IFRS. Some selected ratios have been analyzed to indicate the Differences between two sets of statements. This paper also tries to explain the updated information about the adoption of IFRS in India.

Present scenario of IFRS in India
In India, the Institute of Chartered Accountants of India (ICAI), as the accounting standards formulating body in our country, has always formulated accounting standards that have withstood the test of time. In Feb, 2011, IFRS converged Indian Accounting Standards (Ind AS) came into existence. The implementation was postponed until April 2012 due to the practical challenges faced by Indian Regulators as well as corporates. Thirty five Indian accounting standards converged with international financial reporting standards (henceforth called Ind AS) was notified by the company affairs of India. The transition to IFRS may cause short term hindrances, but in the long run, the benefits of investments and consistency will definitely outweigh the costs and other challenges. The beneficiaries of IFRS implementation comprise of the economy, investors, industry, accounting professionals and all the stake holders at large. Large numbers of Indian entities are expanding their functioning in the global arena.
On 16 February 2015, the Ministry of Corporate Affairs (MCA) notified the Companies (Indian Accounting Standards) Rules, 2015 (the ‘Rules’) (pending publication in the Gazette of India). The Rules specify the Indian Accounting Standards (Ind AS) applicable to certain class of companies and set out the dates of applicability.

Voluntary adoption

Companies may voluntarily adopt Ind AS for financial statements for accounting periods beginning on or after 1 April 2015, with the comparatives for the periods ending 31 March 2015 or thereafter. Once a company opts to follow the Ind AS, it will be required to follow the same for all the subsequent financial statements.

Mandatory adoption

For the accounting periods beginning on or after 1 April 2016	For the accounting periods beginning on or after 1 April 2017
• The following companies will have to adopt Ind AS for Financial statements from the above mentioned date: - Companies whose equity and/or debt securities are listed or are in the process of listing on any stock exchange in India or outside India (listed companies) and having net worth of Rs. 500 crores or more. - Unlisted companies having a net worth of Rs. 500 crores or more. - Holding, subsidiary, joint venture or associate companies of the listed and unlisted companies covered above. • Comparative for these Financial statements will be periods ending 31 March 2016 or thereafter.	• The following companies will have to adopt Ind AS for Financial statements from the above mentioned date: - Listed companies having net worth of less than Rs. 500 crore. - Unlisted companies having net worth of Rs. 250 crore or more but less than Rs. 500 crore. - Holding, subsidiary, joint venture or associate companies of the listed and unlisted companies covered above. • Comparative for these Financial statements will be periods ending 31 March 2017 or thereafter.

Source: Deloitte: Indian GAAP, IFRS and Ind AS A Comparison

The IFRS convergence to Ind AS will not be applicable to:

- Companies whose securities are listed or in the process of listing on SME exchanges.
- Companies not covered by the roadmap in the "Mandatory adoption" categories above.
- Insurance companies, banking companies and non-banking Finance companies.

Impact of IFRS on Pharmaceuticals Companies

Collaborative Arrangement

Pharma companies entities often enter into R&D arrangement that include multiple elements like intellectual property licenses, R&D services, manufacturing services etc. Product and services delivered under these arrangement is unique.

In Indian GAAP, there is no specific guidance on applying revenue recognition criteria on each component Under IFRS, it is necessary to apply revenue recognition criteria to the separately identifiable components of a single transaction in order to reflect the substance of the transaction.

Acquisition

Acquiring new business for new brands is a common practice in the industry.

In Indian GAAP, it is not mandatory to follow fair value accounting i.e. purchase method, hence the true worth of intangible assets acquired may not be captured Under IFRS 3–R, only purchase method is allowed, hence identifiable assets, liabilities and contingent liabilities acquired to be accounted at fair value

Intangible Asset

In India GAAP, Amortised over estimated useful lives and need persuasive evidence to justify useful life above 10 years Under IFRS, need to determine whether intangible asset has finite or indefinite useful life. In case of finite life, need to Amortised over estimated life. In case of indefinite life, intangible asset is not Amortised but tested annually for impairment

Impact of IFRS on Financial Statements

This paper tends to discuss the impact of IFRS on financial performance and some significant ratios with the help of study on Glenmark pharmaceutical Ltd. Glenmark Pharmaceuticals Limited is a global pharmaceutical company. The Company is engaged in the development of new chemical entities (NCEs) and new biological entities (NBEs). Its segments are India, United States, Latin America, Europe and Rest of the World. It has approximately seven molecules, over two NCEs and approximately five NBEs in various stages of pre-clinical and clinical development. It is focused on developing and marketing branded and generic formulations. It focuses on manufacturing products across therapeutic areas of dermatology, respiratory and oncology. Its active pharmaceuticals ingredients (API) business spans over 80 countries, including regulated markets of the United States, Europe, Japan and Canada The consolidated financial statements as per GAAP are compared with the consolidated financial statements under IFRS. Some selected ratios have been analysed to indicate the differences between two sets of statements. The figures in the Balance Sheet and the Profit and Loss statements have been completely drawn from the annual report of the company. All figures are related to the period ending 31st march 2016.

Liquidity

The sum of current assets and current liabilities in the two sets is quite diverse. The amounts of short term loans and advances and that of other current assets diverge. This is probably due to the variations in recognition of certain items of loans and trade receivables. Under IFRS loans as well as trade receivables are treated quite in a different way. (IAS 18) The total of the current assets are -0.102% less in case of IFRS which shows that negative effect on financial performance. The rationale probably is, under IFRS the fair value measurement difference in recognition of certain current assets. The total of current liability varies by 23.68% which is quite significant. The reason being that cost of leases and interest expenses are treated on fair values in IFRS (IFRS3) which is not the case in AS. The inclusions of items along with their values are treated in a different way under IFRS. Similarly short term provisions too differ by 68.68%. Under IFRS the total current liabilities are quite less as compared to AS. These are the various reasons why the current ratio is 1.90% higher in case of IFRS. So the liquidity of the firm is well depicting in IFRS statements.

Table 1: Comparative Consolidated Balance sheet of Glenmark Pharmaceuticals under GAAP and IFRS in the year ending 31st March 2016 (Rs. in Crore)

Particulars	As AS	As IFRS	Diff in%
Liabilities			
Shareholders' funds			
Share capital	282.16	282.16	0.00
Reserve and surplus	30,282.25	42,420.30	40.08
Total Shareholders' funds	30,564.41	42,702.46	39.71
Minority interest	(3.01)	(3.01)	0.00
Non-current liabilities			
Long-term borrowings	24,872.97	24,872.97	0.00
Deferred tax liabilities	1,576.98	2,666.42	69.08
Other long-term liabilities	769.90	722.95	-6.09
Total Noncurrent liabilities	27,219.85	28262.34	3.82
Current liabilities			
Short-term borrowings	7,874.18	7,874.18	0.00
Trade payables	19,407.86	20,065.79	3.39
Other current liabilities	11,370.14	2,465.75	-78.31
Short-term provisions	2,020.25	632.64	-68.68
Total current liabilities	40,672.43	31,038.36	-23.68
Total Equity And Liabilities	98,453.68	1,02,000.15	3.60
ASSETS			
Non-current assets			
Fixed assets			
Tangible assets	16,437.35	24,622.85	49.79
Intangible assets	8,726.46	14,452.42	65.61
Goodwill on consolidation	574.80	574.80	0.00
Non-current investments	171.95	0	-100
Deferred tax assets	1,830.62	11,739.66	541.29
Long-term loans and advances	6,174.02	349.75	-94.33
Total fixed assets	39,343.15	51,739.48	31.50
Current assets			
Inventories	15,677.60	15,677.60	0.00
Trade receivables	24,926.46	24,926.46	0.00
Cash and bank balances	8,692.44	8,571.21	-1.39
Short-term loans and advances	8,669.88	312.11	-96.40
Other current assets	1,144.15	9,562.49	735.77
Total current assets	59,110.53	59,049.87	-0.102
Total assets	98453.68	1,10,789.35	12.52

Source: Annual reports of Glenmark Pharmaceuticals Limited

Table 2: Comparative Consolidated Income statement of Glenmark Pharmaceuticals under GAAP and IFRS

Particulars	As AS	As IFRS	% Diff
Revenues			
Operating Revenue	76,495.83	76339.61	-0.20
Other Income	200.00	280.42	40.21
Total Revenues	76 695.83	76620.03	-0.098
Expenses			
Materials Consumed	19,270.75	19,875.15	3.13
Changes In Inventories of Finished Goods And Work-In-Process	(1,401.60)	(1,401.60)	0.00
Purchase Of Products For Sale	5,139.97	5,139.97	0.00
Employee Costs	13,772.34	13,781.95	0.069
Other Expenses	24,479.95	24,772.64	1.19
Depreciation, Amortisation And Impairment	2,517.63	2,691.42	6.90
Total Expenses	65,567.89	64,859.53	-1.08
Operating Profit	11,127.94	11,760.50	5.68
Finance Income	0	75.80	0.00
Finance Costs	1,788.85	1,788.85	0.00
Profit Before Tax	10,232.10	10,047.45	-1.80
Taxes			
Current Tax Expenses	5,114.41	5,145.96	0.61
Deferred Tax Benefit	(650.41)	(2,117.56)	225.57
Total Tax Expenses	4464.00	3,028.40	-32.15
Profit For The Year	7,201.02	7,019.05	-2.52

Source: Annual reports of Glenmark Pharmaceuticals Limited

Table 3: Comparison of ratios as per values under AS and IFRS as on 31st March, 2016

Ratios	As AS	As IFRS	% Diff
Liquidity Ratios			
Current Ratio	1.45	1.90	31.04%
Acid Test Ratio	1.06	1.39	31.13%
Profitability Ratios			
Return on Capital Employed	0.177	0.125	-29.38%
Return on Shareholders Equity	0.235	0.164	-30.21%
Earnings per share Basic	25.65	25.01	-2.50%
Earnings per share Diluted	25.65	25.00	-2.53%

Source: Annual reports of Glenmark Pharmaceuticals Limited

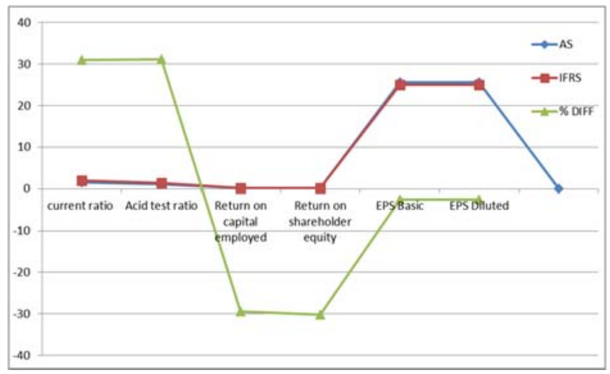

Table 3: percentage difference in ratios

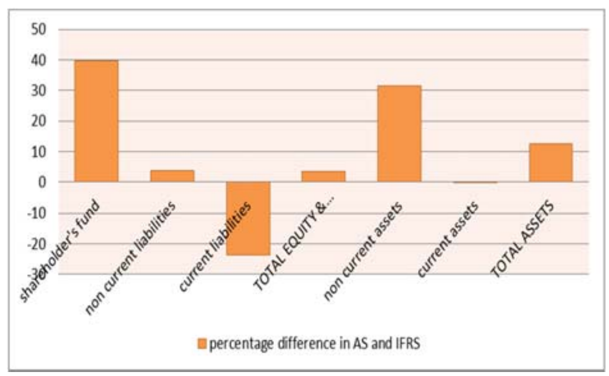

Table 4: percentage difference in AS & IFRS

Profitability

The Return on Capital Employed, Return on Shareholders Fund and Earning per Share are best measures to know profitability of a firm. The return on capital employed and return on shareholders fund depends upon the share capital. Return on capital employed ratio is according to AS it is 0.17 and as per IFRS it is 0.12. This ratio is a prime test of the efficiency of business. It measures not only the overall efficiency of business but also helps in evaluating the performance of various departments. The differences are due to consideration of Reserves are a part of shareholder funds in AS but not under IFRS (IAS19, IAS39, IAS 32). In AS the surplus from P&L is a part of reserves and surplus which is not included under IFRS (IAS 19). IFRS permits its measurement of share identifiable net assets at fair value. This explains the variation of 29.38% and 30.21% in the Return on Capital Employed and Return on Shareholders' Equity. The EPS basic varies by 2.50% and diluted by 2.53%. The outstanding share are considered for the purpose of calculation under AS and IFRS are different and used fair value method under IFRS whereas AS permits their valuation on intrinsic value method.

Conclusion
The study examines the effects of IFRS adoption on the financial ratios in glenmark pharmaceutical Ltd to analyze effects of IFRS adoption on the financial ratios were used are liquidity and profitability. This paper concludes that IFRS would increase the comparability between financial statements viz. Balance Sheet and Profit and Loss Account of various companies and to analyze some important ratios across the nation. The paper discusses the impact of transition on various item of the financial statements and their impact on some powerful ratios. The variation in total assets and liabilities is because of the reclassification among equity and liability and also because of the difference in the concept of revenue recognition. Revenue recognition will get impacted for Collaborative Arrangement. Intangibles will be recognized at fair value on acquisition will result in reduction in goodwill component. Intangibles will get amortized over its actual life and will get tested for impairment All the above observations emphasis the fact that IFRS is a fair value principles based accounting which will improve quality of disclosures and enhance international comparability and understanding of financial statements. Indian corporate sector has to migrate to International Financial Reporting Standards (IFRS) from the home-grown Indian Accounting Standards by 2016-17 financial year. The new system will be mandatory from that year and it was necessitated by the need to be compliant with global practices.

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