AN ANALYSIS OF THE DEVELOPMENT OF ACCOUNTING IN INDIA

THESIS

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CHAPTER I

INTRODUCTION

Problems Identified

Inadequate and antiquated accounting systems as well as the absence of effective financial management in developing countries, appear to be major obstacles to their optimum utilization of resources and may be retarding their economic growth and development. In addition, fiduciary responsibility, or accountability, is a basic requirement of management in both the public and private sectors. Each enterprise owes an accounting to those who provide it with money, or who oversee its activities, or who are affected by what it does. Its managers are obligated to demonstrate that they exercise stewardship over the resources entrusted to them. In addition, clear and credible standards of accountability, whether in public administration or private business, are of basic importance in demonstrating the security of savings and attracting investments.

Financial aid alone will not ensure development of an underdeveloped economy. Pouring financial aid into an underdeveloped country will not improve economic development if that country does not have the capacity to effectively manage, utilize and account for the resources provided. There is an urgent need for a clear understanding that financial performance is a necessary condition of sustained economic growth.

Since demands for resources in developing countries far exceed supplies, the efficiency with which those resources are utilized is (or should be) an important consideration in the way they are allocated. Decisions, therefore, must be made as to the allocation of resources to ensure that optimum utilization is obtained. Without essential information on which to base those decisions, management cannot effectively allocate or utilize available resources. Accounting provides the information essential to the measurement of what resources are available and to the control of their use.

A lesser developed country seeking to increase economic development tends to rely on centralized national planning for resource allocation.[1] Effective planning of that allocation can be accomplished only if adequate financial management information is available to the central planning group. If there is inadequate information then the proper decisions may not be made. In addition, evaluation of the effectiveness (ineffectiveness) of the planning process cannot be accomplished without adequate financial reporting.

This paper attempts to identify possible solutions to the problem of inadequate accounting and financial management in developing countries through an analysis and evaluation of the development of accounting in India. India was selected as the subject of this evaluation because it is presently one of the more advanced developing countries of the world and the common

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[1]Linowes, David F., "The Role of Accounting in Emerging Nations," The Journal of Accountancy 133 (January 1969): 18.

characteristic that it shares with many other developing countries, having once been part of the British empire.

Methodology of Analysis

A significant part of the research for this paper was conducted by personal observation and interviews with various Indian business, education, and political leaders. The interviews were conducted in India during January and February 1981. The remainder of the analysis was accomplished by a search of published data relevant to the accounting and management practices in India.

Questions to be addressed as part of the evaluation of the development of accounting in India are: What is the current status of the accounting profession in India? Has India's development been hindered by inadequate accounting and financial management systems? Can India's experience in developing accounting and financial management systems be utilized by other developing countries? Can a uniform approach to developing adequate accounting systems be established that could be utilized as a guide in other developing countries?

Overview of Study

The lack of adequate accounting and financial management systems in developing countries may be severely restricting their economic growth and development. Possible solutions to these problems are developed in this paper.

Accounting needs of developing countries generally involve developing relevant accounting and auditing standards, providing effective training of accountants and recognizing the accounting function as a tool for economic development. To properly address these needs, it is important to understand that accounting systems and processes are influenced by socio-economic, professional, institutional, statutory, legal, and various other considerations.

Chapter II of the paper describes the foundation of current accounting practices in India. In this segment the British influence on Indian accounting and accounting legislation is examined as it relates to the development of accounting in both the public and private sectors.

The current status of accounting systems in India is the subject of the next chapter. The three major systems addressed are: the enterprise (commercial) accounting system, the government accounting system, and the governmental budgetary accounting system. The analysis reveals that these systems are in need of significant improvements even though they may be very advanced in comparison to many other developing countries. This development can be attributed primarily to the British influence in India.

Accounting research, education and training are discussed in Chapter IV since these are necessary if the accounting profession is to meet the needs of an everchanging business and government environment in India. Research and education are two of the most important factors in developing a strong accounting profession; therefore, significant committments must be made to these areas.

Chapter V summarizes the accounting and financial management deficiencies identified by the analysis. The deficiencies identified are organized in relationship to enterprise accounting, government accounting, and education and training.

In Chapter VI specific programs for improvements are presented. An action plan to provide needed improvements in accounting and financial management has been developed for India. Based on the results of the analysis of the development of accounting in India, a proposed plan for developing and improving accounting and financial management in other developing countries has also been prepared. The plan is predicated on the lessons learned from this analysis of India's development of accounting and financial management systems.

In the final chapter the findings and conclusions, developed from the analysis and evaluation of the development of accounting in India, are summarized. Although the findings and conclusions reached in this paper are generally relevant to all developing countries, any recommended program for improvement would need to be tailored to meet the specific requirements of each developing nation after taking into consideration that countries unique social, political and economic characteristics.

CHAPTER II

FOUNDATION OF CURRENT ACCOUNTING PRACTICES

Accounting in India has a long history dating back many centuries; however, since the most significant factor affecting the structure of accounting in India today was the influence of the British rule from 1773 to 1947 this analysis begins with that period.

British Rule

The English East India Company was the first major British influence in India. The company was incorporated in the year 1600 for the purpose of trade in the Far East[1] and by the middle of the eighteenth century had established its unrivalled control over India. Through this control the East India Company firmly established the English accounting system as the accepted commercial accounting system of India. An uprising among Indian soldiers of the Bengal Army[2] ended the East India Company's power in India and in 1858 the British government assumed direct responsibility for the government of India.

The rule of India as a colony of England for some eighty-nine years firmly established the same basic government accounting system as

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[1] Ramkrishna Mukherjee, The Rise and Fall of the East India Company (New York: Monthly Review Press, 1974), p.65.

[2] Sepoy Mutiny (1857-1859).

that utilized by the British government. British rule in India ended 15 August 1947 with the passage of the India Independence Act.[1] There was thus a full-fledged British administration in India for two crucial centuries, leaving an indelible mark on every aspect of Indian life and culture. Since power was transferred as a result of negotiations and mutual agreement, India inherited the British systems of government, accounting, and administration in their original forms.

Chartered Accountants Act of 1949

The effect of British rule is still very much in evidence today. The British influence on the public accounting profession in India is very pronounced both in the form of regulation of the profession and in the design of the professional institute.

The Chartered Accountant (CA) in India is basically the equivalent of a Certified Public Accountant (CPA) in the United States. Regulation and registration of all CA's in India is governed by the Chartered Accountants Act of 1949. The Act which provides for the registration of all accountants who have passed the three required examinations and have completed the apprenticeship period is modeled after the British Chartered Accountants Act. The three required examinations are: (1) the entrance, (2) the intermediate, and (3) the

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[1] Sir Percival Griffiths, The British Impact on India (London: Archor Books, 1965), p.460.

final.[1] The apprenticeship period consists of either three years as an articled clerk or four years as an audit clerk or a combination of the two.

The subjects covered in the entrance examination include English, bookkeeping, elementary economics, modern administration, commercial arithmetic and commercial geography. The intermediate examination includes accounting, statistics, cost accounting, auditing, mercantile and company law and general commercial knowledge. The final examination is divided into two parts consisting of papers on advanced accounting, auditing, taxation, cost accounting, management accounting, law and economics. A passing grade of 40% is required on each paper with an average of 50% for all papers combined. The two parts of the final examination may be passed one at a time.[2]

An individual must be at least sixteen years of age and must hold a degree in science, arts, or commerce or hold the National Diploma of Commerce or have passed the entrance examination of the Institute of Chartered Accountants of India in order to be eligible to be an articled clerk or an audit clerk.[3]

Auditing in India took on a distinctively Indian approach with the establishment of the Indian Institute of Chartered Accountants in

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[1]American Institute of Certified Public Accountants: International Practice Executive Committee, Professional Accounting in 30 Countries (New York: American Institute of Certified Public Accountants, 1975), p. 261.

[2]Ibid., p. 263

[3]Ibid.

1949.[1] The Institute, although thoroughly Indian, is modeled after the Institute of Chartered Accountants of England and Wales, and is governed by a council elected by the members.

The Institute is a very stewardship oriented organization primarily because of the Companies Act which sets forth extensive legal requirements involving detailed audit procedures to which the Chartered Accountant must adhere. Approximately 30 to 35 percent of the Chartered Accountants in India, are in public accounting; a majority of the rest are in industry with a few in government.[2] The relatively small number of Chartered Accountants employed in the government can be attributed primarily to the low wages paid by most government positions. The Chartered Accountant in public practice is one of the best paid individuals in India. A senior partner in a Chartered Accounting firm will earn about Rs. (Rupees) 100,000 ($12,500) annually; a junior will earn between Rs. 30,000 - 40,000 ($3,750 - $5,000) annually.[3]

The Companies Act of 1956 greatly enhanced the stature of the Chartered Accountant by requiring that CA's will be the only ones authorized to audit public companies. At the same time the Act has imposed extensive detail audit procedures to which the CA must adhere.

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[1]Mihir Bose, "Growth of Accountancy in India," Accountancy 88, no. 1095 (May 1977): 36.

[2]Adolf J. H. Enthoven, Accounting Systems in Third World Economies (New York: North-Holland Publishing Co., 1977), p. 260.

[3]Ibid.

Companies Act of 1956

Attempts have been made to establish that Indian auditing is as old as the Egyptian accounting system; however, the profession as it stands today first emerged in the 19th century to meet the needs of the British merchants in India.[1] The basis of auditing in India is the Companies Act of 1956,[2] which replaced the British-legislated Companies Act of 1913. The 1956 Act contains some six hundred sections with approximately one-half of the sections based on the "true and fair"[3] concept. Extensive amendments to the 1956 Act have significantly expanded the disclosure requirements and added considerably to the responsibility of the auditor.[4] The Act prescribes the accounting and financial reporting practices for business organizations in India. Company legislation is fundamentally based on British law and is comprehensive even to the point of prescribing the form and contents of the balance sheet and the profit and loss account (income statement). The extensive disclosures in the financial statements, as required by the Act, applies to all companies except insurance, banks, and electric utilities which are governed by special acts.

The central government may exempt any company from compliance

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[1]Bose, "Growth of Accountancy in India," p. 36.

[2]India Ministry of Law, The Companies Act, 1956 (New Delhi: Government of India Press, 1967), p.ix.

[3]The "true and fair" concept is the British equivalent of the U.S. accounting terms "presents fairly."

[4]Mihir Bose, "Auditing in India - A Legacy of Problems," Accountancy 88, no. 1007 (July 1977): 11-12.

with any of the requirements of the act if the exemption is necessary in the "public interest:" however, very few companies have been exempted. Noncompliance with the requirements of the Companies Act[1] concerning the disclosure items in the annual financial statements is punishable with imprisonment of up to six months or a fine of up to one thousand rupees ($125) or both.

The Act requires that a company maintain proper books of account that reflect:[2]

- All sums of money received and expended by the company and the manner in which the receipt and expenditure occurred.
- All sales and purchases of goods by the company.
- The assets and liabilities of the company.

The form in which the books are to be kept is not specified by the Act; however, all books and vouchers relevant to any entry in the books must be retained for a period of at least eight years after the end of the financial year.[3]

A company is required to keep registers of shareholders, directors and their shareholdings and minute books in addition to the books of account mentioned above; however, the shareholders of a company do not have a right to inspect the books except in the case of liquidation of the company.

The Companies Act requires that every company must annually

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[1]A synopsis of the accounting and disclosure requirements of the Act are set forth in Appendix A.

[2]India Ministry of Law, pp.78-81.

[3]Ibid., p.87.

appoint an auditor and that only Chartered Accountants licensed under the Chartered Accountants Act of 1949 can qualify for such appointment. If the company fails to appoint an auditor, the central government may appoint an auditor for the company. The auditor is required to make a report on every balance sheet and profit and loss account (income statement) of the company which is to be presented in a general meeting of the company.

At every annual general meeting financial statements must be presented by the board of directors to the shareholders. These financial statements must also be accompanied by the auditors' report and the report of the board of directors of the company. Consolidated financial statements are generally not prepared since they are not required by the Act. Neither are the financial statements of a company required to be published in any official newspaper.[1]

Any major changes in accounting and financial reporting practices in India will probably require amendment of the Companies Act before they can be implemented. Further improvements in the system, that are dependent upon amendment of the Act, will probably involve a significant period of time in which to implement because of the inherent slowness of the bureaucratic process.

Cost and Works Accountants Act of 1959

A group of industrial accountants were the first to organize cost accountants in India. In 1944 the group formed the Institute of

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[1] Ibid., p.91.

Cost and Works Accountants as a company for the purpose of providing cost accounting training and services.[1] The company was subsequently replaced by the Institute of Cost and Works Accountants (ICWA) under authority of the Cost and Works Accountants Act of 1959.[2] The institute, as it exists today, is the only statutorially recognized professional examining and licensing body in India specializing exclusively in cost and management accounting. One of the main objectives of the institute is to develop cost and management accounting into an important tool for management control in all areas of economic activity.[3] In pursuit of this objective the institute has developed training programs (including such areas as cost accounting and management information systems) for cost accountants in both industry and government.

The requirements for certification as a Cost and Works Accountant are not as demanding as are those for a Chartered Accountant. Students are allowed to take either oral or correspondence courses in preparation for the ICWA examinations. Neither formal university training nor apprenticeship training is required by the institute, in order to become a cost and works accountant.[4]

The cost accounting profession gained significant support in

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[1]American Institute of Certified Public Accountants: International Practice Executive Committee, p.266.

[2]Ibid.

[3]Enthoven, p.266.

[4]Ibid., p.261.

1974 with the amendment of the Companies Act of 1956. Section 33(b) of the Act specifies that cost audits are to be performed by cost accountants licensed under the Cost and Works Accountants Act of 1959 or by Chartered Accountants who possess the prescribed qualifications.[1] If the government considers it necessary, an audit of the cost accounts of a company may be required in order to obtain an insight into the cost structure of the company.

Both the historical and the legislative foundation of current accounting practices in India are strongly British oriented. During the early British rule basic enterprise and government accounting systems were firmly established. The British influence remained even after India's independence as is evidenced by the form of subsequent accounting related legislation. Both the Chartered Accountants Act of 1949 and the Companies Act of 1956 were closely modeled after existing British legislation, while the Cost and Works Accountants Act of 1959 was one of the first pieces of truly Indian accounting legislation. The establishment of professional accounting institutes did not ensure that a unified effort would be made to improve accounting in India. In fact there appears to be a general lack of cooperation and coordination among the various institutes of the accounting profession. India was able, however, to make dramatic progress, in a relatively short period of time, in establishing accounting systems and an accounting profession. This was accomplished by simply adopting established systems and institutions which had been developed by the British.

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[1]American Institute of Certified Public Accountants: International Practice Executive Committee, p.768.

CHAPTER III

CURRENT STATUS OF ACCOUNTING SYSTEMS

The British impact on India was significant; therefore, it is not surprising to find that the accounting practices in India today are largely based on the practices in the United Kingdom (U.K.). As a result, the structure of government accounting and budgeting in India has been developed through a strong nationally-controlled system. This system evolved primarily from the adoption and "Indianization" of the British accounting and financial management systems in place at the time of independence. Traditionally, government accounting was linked to taxation and revenue control and to the recording of and accountability for receipts and expenditures. The twentieth century development of budgeting and budgets gave a much larger scope to the area of government accounting.

There are three distinct branches of financial accounting - enterprise, government, and national. National accounting deals primarily with national income measurement and the macro economic determination of the gross national product. The enterprise and government accounting branches are more micro oriented and as such are somewhat unrelated to the national accounting process; therefore, for the purposes of this paper only the enterprise and government accounting branches will be addressed, along with a discussion of government budgetary accounting.

Enterprise Accounting Systems

Private sector financial accounting and auditing in India essentially follows the U.K. pattern of enterprise accounting. Even though there has been very little research done on accounting concepts and principles, a gradual Indianization of the system has been occurring over the past few years. The enterprise form of accounting reflects a strong stewardship orientation, due primarily to the fact that the Companies Act of 1956 sets forth, in great detail, specific legal requirements that must be adhered to by both the accountant and auditor, even to the point of specifying the precise format for the financial statements.

Many of the larger public and private enterprises in India have excellent accounting systems, procedures, and personnel. However, the accounting procedures of the smaller establishments tend to be somewhat inadequate because management may not recognize the need for good accounting, or even want it, or may have difficulty in attracting good personnel.[1]

A unique aspect of auditing required by the government of India is the "Cost Audit." This is an examination and verification of the correctness of cost accounts and adherence to cost accounting plans and procedures. The purpose of the cost audit is to identify errors of ommission and commission, if any, in the basic financial records supporting the balance sheet and profit and loss statement. The cost audit is in addition to the normal statutory audit and must

[1] Interview with S. U. Gupta, former president of the Indian Institute of Chartered Accountants, New Delhi, India, 18 February 1981.

be performed by someone other than the statutory auditor. The cost audit report must be submitted to the Company Law Board of the central government.[1] The government presently requires that cost audits be performed for only fourteen specific types of industries.[2] These fourteen industries, however, account for approximately eighty percent of all enterprise operations in India. The government plays a significant role in the development and implementation of accounting systems in India as will be discussed further in the next section.

In an attempt to improve accounting information received from their clients, the nationalized banks in India have set up "Technical Cells," which provide accounting and management assistance to the business community.[3] To this extent the banks have been instrumental in attempting to improve the financial systems of their existing and potential clients.

The Industrial Development Bank of India has established the Management Development Institute of New Delhi to train executives. One of the Institute's main purposes is to improve existing accounting systems not only for the bank's clients but also for the bank itself since bank accounting systems generally tend to be outdated and in need of improvement.[4]

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[1]American Institute of Certified Public Accountants: International Practice Executive Committee, p.769.

[2]Enthoven, p. 261.

[3]Interview with Maurice Mould, Chief Financial Analysist for the World Bank, Washington, D.C., 8 January 1981.

[4]Ibid.

Although there is a need for significant improvements in the accounting and financial management systems of most private sector enterprises, it should be noted that the enterprise branch of accounting in India appears to be more advanced and well developed than in many other developing countries.

Government Accounting Systems

It is important to understand that the accounting and financial reporting practices at both the state and local levels are highly influenced by the actions of the national government. Accounting systems and charts of accounts for all levels of government are dictated by the central government.[1] As a result, significant uniformity in government accounting has been achieved, which is somewhat unique to India when compared to other developing countries. Uniformity, however, does not ensure that the information produced will be relevant, accurate or timely.

Present government accounting and auditing systems in India can be traced back to the early 1860's during the period of British rule.[2] The post of the Comptroller and Auditor General, as it exists today, can also be traced back for more than a hundred years. It is apparent, therefore, that the present government accounting and financial management systems had their beginnings during the period of British influence and were significantly affected by that influence.

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[1]Appendix B provides a flowchart of the Municipal finance structure currently in place in India.

[2]Bose, "Growth of Accountancy in India," p.36.

The role of the central government in the area of accounting and financial management is generally confined to establishing broad principles and providing necessary advice. Two agencies responsible for advising the government on certain matters are the Bureau of Costs and Prices and the Bureau of Public Enterprises.

The Bureau of Costs and Prices is a government agency whose responsibility it is to render advice to the government on various issues pertaining to cost reduction and improvement of efficiency.[1] In this capacity, the Bureau undertakes cost studies of various industries as to cost of inputs, proper utilization of capital and materials, and scope and methods for achieving cost reduction together with an assessment of the implications thereof. In addition to specific industries on which the advice of the Bureau is sought by the government, it may, on its own, undertake cost studies of other industries where it feels such investigation is desirable.

Although public enterprises have been established primarily by the government a small number have been created through nationalization.[2] The Bureau of Public Enterprises was established by Parliament in 1964 and assigned the responsibility of coordinating the various policies and administrative activities of over one hundred public enterprises in India.[3] These enterprises originate either as:

(1) corporations authorized under Acts of the government, or

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[1]Enthoven, p.262.

[2]Ibid.

[3]Ibid., p.263.

(2) companies established under the Companies Act.

There is little if any distinction between these entities.

The specific duties of the bureau include:[1]

(1) advising the government regarding investment decisions,

(2) evaluating accounting and management functions of the public enterprises and

(3) providing advice regarding national policies.

The Bureau operates in an advisory capacity only; however, in fact they do exert significant influence.

A unique aspect of the government accounting system in India is its uniformity of accounting structure for the transactions of the central and state governments.[2] The evolution of a highly centralized form of government appears to have facilitated the implementation of this uniform system, which is somewhat unique to India when compared to other developing countries. While the system has, over the years, acquired some commendable features such as simplicity and uniformity, it has also displayed a weakness in responding to the ever changing needs and objectives of government activities.[3] One of the more significant weaknesses in the system appears to be its inability to

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[1]Ibid., p.268.

[2]Interview with G. S. Ahuja, Chief Financial Officer of the Housing and Urban Development Corporation of India, New Delhi, India, 10 February 1981.

[3]Interview with H. U. Bijlani, Chairman of the Housing and Urban Development Corporation of India, New Delhi, India, 4 February 1981.

produce "timely" financial information. In many instances the information produced is so outdated that it is of little or no value.

The Accountant General is the central government official who is in charge of all government accounting policies.[1] He is responsible for the the general accounting system of the government which consists primarily of a decentralized system of payments and receipts through a number of widely distributed treasuries.

The higher level accounting positions within the government are generally occupied by Indian Audit and Accounts Services officers (IAAS). The accounting training that the IAAS officer receives has an intense stewardship orientation and is about the only organized training program available to government accountants. This training is based on the strong administrative concept of India's civil service program and generally bears little relationship to the training provided by the other two professional accounting institutes.

Accumulation and compilation of the expenditures incurred by the various ministries and agencies is the duty of the Comptroller and Auditor General.[2] It is his responsibility to accumulate all expenditures according to the major heads (classification) of accounts and any sub-division thereof. This information is then used to compile another set of accounts known as appropriation accounts which show the total amount of expenditures incurred against each grant. This report then enables the audit department to monitor the progress of expenditures. Any over expenditure of a grant requires approval

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[1] Enthoven, p.266.

[2] Interview with S.U. Gupta.

through a supplementary demand which must be passed by Parliament along with an appropriation act to fund the demand.

The audit department tends to emphasize precontrol approval of disbursement requests, or post-control voucher audits of governmental financial transactions. These voucher audits are primarily concerned with the legality of transactions with little or no emphasis on internal controls, economy, or efficiency.

The quality of accounting systems at the municipal level is generally poor. These are usually single entry cash basis systems which are inaccurate, not up-to-date and lack appropriate control features.[1] As a result of these deficiencies, they are generally unable to produce meaningful financial data on a timely basis.

The government accounting and financial management systems of India are in need of significant improvements; however, these needs appear to have generally been neglected. This neglect may be the result of a lack of understanding of the importance of having adequate management information systems.

Government Budgeting Systems

The present government budgeting systems and procedures of India have remained virtually unaltered for nearly a century.[2] The budget approach has been predominately a revenue and expenditure

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[1]Enthoven, p.270.

[2]These conclusions are based on personal observation and analysis of the accounting systems of some ten cities in India as well as extensive disussions with numerous government officials at the national, state, and local level.

approach with little emphasis on economy and efficiency. There is very little, if any, relationship between budget information and past and present accounting data, so that past performance is not used to project future requirements; therefore, no real comparisons of planned and actual financial performance can be made. As a result of the inadequacies in the accounting systems, the budgeting process generally does not reflect economic or financial viability; nor does it enable the government to determine the actual demand for its services or the true cost of providing those services.

Article 112(1) of the Constitution of India requires that annual financial statements, setting forth the estimated receipts and expenditures of the government for the succeeding fiscal year, be presented to both houses of Parliament. The expenditure estimates included in the annual financial statement are aggregated into a number of "demands for grants." The demands for grants are then segregated by each ministry. The demands for grants together with the annual financial statement consititute the budget. In order to fund the expenditures that have been budgeted Parliament must pass a finance act.

The importance of adequate accounting and financial management systems must be conveyed to management. It appears that this lack of understanding may have contributed to the apparent neglect of the need for improvements in these systems. Although the enterprise and government accounting and budgeting systems of India are in need of significant improvements and modernization when compared to the systems of the United States or the United Kingdom, they have been shown to be very advanced in comparison to many other developing countries. Here again the advanced stage of their development may be attributed primarily to the British influence and the adoption of existing British accounting systems.

CHAPTER IV

ACCOUNTING RESEARCH AND EDUCATION

Research, education and training are necessary if the accounting profession is going to keep pace with the every changing business and government environment in India. Responsibility for the education and training of accounting and auditing professionals in India is currently vested in the Indian Institute of Chartered Accountants, the Institute of Cost and Works Accountants and the Indian Audit and Accounts Services organization. Therefore, it would seem logical that the responsibility for accounting research should also vest in those same institutions.

Accounting Research

Research work in the field of accounting in India has almost been nonexistent, although there is a significant need for such research. Accounting research could assist in developing appropriate financial models and their underlying legal requirements or to accurately identify a country's particular accounting needs. The Institute of Chartered Accountants, the Institute of Costs and Works Accountants and the Indian Accounting Association[1] have done some research in accounting; however, their efforts have been very

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[1]The Indian Accounting Association is a small body composed of academicians.

limited.[1] Without adequate research the accounting profession will be unable to meet the needs of a dynamic business and government environment.

Before meaningful research can be undertaken it will be necessary to first establish a proper base upon which that research can be developed. Various studies should be undertaken in order to establish this base. These should include:

- a study of the development of accounting principles in India as they relate to both enterprise and government accounting.

- a study of the role of the Companies Act and current tax laws in dictating accounting principles and practices.

- a study to collect all accounting principles that are currently in use and evaluate the need to retain, revise or standardize those principles.

- identification of statutory and other legal changes that may be required in order to implement needed changes in existing accounting systems.

- a study of current Indian accounting systems and terminology to determine if there is a need for Indianization.

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[1]Interview with N. K. Bose, former president of the Institute of Cost and Works Accountants of India, New Delhi, India, 3 February 1981.

- development of a glossary of accounting terms in Hindi.[1]

For the accounting profession in India to just keep pace with the dynamic business and government environment, much less to upgrade the quality of its services, significant commitments to accounting research must be made.

Accounting Education

Three levels of training and education for accountants in India can be distinguished: academic, institutional, and vocational.

Academic training for accountants, at the bachelor's or even master's degree level, is generally carried out within the department of economics or commerce. As such, accountancy at the academic level appears to be strongly biased toward financial enterprise accounting. At the present time there are no separate schools of accountancy in India. Almost all accounting and business education is provided by the various universities through the Bachelor or Master of Commerce degree programs. Some professional institutions such as the Institute of Costs and Works Accountants do not even require university training.

Institutional training under the guidance of existing accounting institutes concerns primarily financial accounting and auditing, and management or cost accounting, and in some cases, may be either oral or by correspondence. The Indian government has established its own training program for government accountants through

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[1]Adoption of Hindi as the official language of India is presently under consideration by the Indian Parliament.

the Indian Audit and Accounts Service; however, government interest in providing training in accounting and auditing appears to be generally quite low.

Two major obstacles to expanding accounting education in India are (1) an insufficient supply of qualified, dedicated, full-time teachers, and (2) a shortage of current textbooks and teaching materials. The quality of teaching is often below desired standards because of low pay and the pressure for good accountants elsewhere. An American Accounting Association study identified shortages of teaching staffs, materials, and physical facilities as the "greatest weakness in accountancy training in Third World Countries."[1] The study also stated that government-oriented, financial institutes, such as the IAAS, which train the majority of government accountants tend to emphasize existing practices and methods and neglect newer and more relevant government accounting and budgetary techniques.

Assistance from international donor agencies will be needed to help strengthen existing training institutions and universities. It will also be necessary to make changes in existing salary structures in order to attract and retain qualified teachers so as to achieve an adequate supply of trained accountants and financial managers in the future.

Research and education are two of the most important factors in developing a strong accounting profession. A significant commitment

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[1] American Accounting Association: Committee on International Accounting Operations and Education, Accounting Education and The Third World (New York: American Accounting Association, 1978), p. 20.

to both research and education is needed; otherwise, the profession will be unable to keep pace with the everchanging needs of both business and government.

CHAPTER V

ACCOUNTING AND FINANCIAL MANAGEMENT DEFICIENCIES

Numerous deficiencies in the accounting and financial management systems of India have been identified in this paper. These deficiencies have contributed to the ineffective utilization of resources, thus, retarding economic growth and development. The deficiencies identified here are not unique to India but, to a greater or lesser degree, are common to most developing countries.[1] The deficiencies have been organized by their relationships to enterprise accounting, to government accounting or to accounting education and training.

Enterprise Accounting

Enterprise accounting in India is more advanced than in most developing countries; however, there is still a need for significant improvements in existing systems. Some of the more significant deficiencies relating to enterprise accounting include:

- lack of cooperation within the accounting profession
- inadequate accounting research
- lack of financial measurement and reporting

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[1]"Comptroller General of the United States, _Report to the Congress of the United States: Training and Related Efforts Needed to Improve Financial Management in the Third World_ (Washington, D.C.: United States General Accounting Office, 1979), passim.

- detail rather than system oriented auditing procedures

- Lack of Cooperation Within the Accounting Profession

Inadequate cooperation and coordination exists among the various institutes of the accounting profession.[1] Progress toward standardization of accounting and financial reporting principles and practices as well as educational and training requirements cannot be achieved without the unified support of all of the professional accounting institutes. In India, these include the Institute of Chartered Accountants, the Institute of Cost and Works Accountants and the Indian Audit and Accounts Service.

- Inadequate Accounting Research

Sufficient accounting and financial management research is not being conducted in India. Without adequate research the accounting profession will be unable to meet the needs of a dynamic business environment, much less to upgrade the quality of its current services. If the accounting profession in India is to continue to improve its services; significant commitments to accounting research must be made.

- Lack of Financial Measurement and Reporting

Enterprise accounting tends to be primarily stewardship oriented with an emphasis on meeting the requirements of the Companies Act. This causes financial reporting to be more procedural and technical oriented rather than being directed toward economic-financial measurement. The Companies Act is so detailed that it forces accountants to spend a large portion of their time simply keeping

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[1] Enthoven, p.272.

basic records.

- Detail Rather Than System Oriented Auditing Procedures

The Companies Act requires the auditor to perform extensive detailed checking of data while insufficient attention is given to reviewing the accounting system. Auditors generally spend a relatively small part of their time reviewing systems, procedures and other planning and internal control aspects. This tends to indicate that not enough emphasis is being given to constructing effective accounting systems and procedures that could substantially reduce the amount of financial data verification needed. Frequently, however, a proper accounting system does not exist and specific evidence must be checked. Also, most enterprise accounting systems tend to neglect operational accounting procedures and effective cost-benefit measurements. Although deficient in these areas, enterprise accounting is considerably more advanced in its development than is government accounting.

Government Accounting

Government accounting in India, as in almost all other countries, appears to be significantly less developed than private sector accounting. Some of the more significant deficiencies are:

- lack of integrated financial information
- incomplete or unreliable financial data
- inadequate budgeting process
- archaic accounting systems
- inadequate budgeting process
- outdated auditing practices

- minimal cost accounting
- shortage of trained accountants and financial managers

- Lack of Integrated Financial Information

The major weakness in government accounting in India appears to be a lack of adequate integrated financial data that can be used by management in the resource allocation process. Much of the data that is provided to management has not been prepared on a timely basis and is, therefore, of limited value in the current decision-making process. It is reported that there is very little communication between government ministries;[1] therefore, generating the cooperation needed to institute integrated financial systems would be difficult.

- Incomplete or Unreliable Financial Data

Government financial data, especially at the state and local levels, are often incomplete, inaccurate and, therefore, of limited usefulness. As a result, economic planning, capital budgeting, and other financial management functions, of a planning and control nature, are frequently carried out with deficient and outdated accounting data. Such plans are, therefore, no more than rough estimates rather than reliable projections. Similarly, economic and fiscal policies cannot be well founded if they are based on information that is unreliable or out of date; nor can their implications and results be properly assessed. A United Nations report[2] points out that this fundamental

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[1] Interview with Maurice Mould.

[2] United Nations, Report of the Fourth Meeting of Experts on the United Nations Programme in Public Administration and Finance, (ST/TAO/M/52), May 1977, p.7.

weakness in reported financial data is common among many of the developing countries of the world.

• Archaic Accounting Systems

Many of the deficiencies in reported financial data can be attributed to inadequate accounting systems. Government accounting is still viewed by many government officials as primarily a means by which to account for receipts and expenditures of public funds. Most government accounting systems are nothing more than cash basis bookkeeping systems and bear little or no relationship to the budgeting process.

• Inadequate Budgeting Process

Government budgets are often based on inaccurate and outdated accounting data or, in many instances, bear little or no relationship at all to prior accounting data. Since accounting data that indicates past performance is usually not used to predict future needs, no real comparison of planned and actual financial performance can be made.

• Outdated Auditing Practices

Government auditing practices tend to concentrate almost entirely on verifying the legality of transactions or preaudit of vouchers, with little or no emphasis on internal controls or system evaluation. Many government entities fail to submit timely auditing financial statements. As an example, the Madhya Pradesh Housing Board has not submitted audited financial data to the central government in over three years.[1] While timely audited annual financial statements

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[1]This deficiency was noted during an analysis of the Madhya Pradesh Housing Board conducted in February 1981.

are no guarantee of an effective system of management information, their absence leads to a strong indication that the information available to management may be similarly out of date and unreliable.

• Minimal Cost Accounting

Financial information about costs and prices is the basic determinant of economic designs on such matters as investment, labor utilization and mechanization, and pricing and marketing policies. It is also critical for controlling and evaluating the impact of such decisions. Apparently very little cost accounting is being performed in the public sector in India. An example of this is the government enterprise operations at Bhilai where doors and windows for government housing projects are produced. The enterprise is unable to determine the unit cost of any of its products because it lacks a cost accounting system. Also, there is an absence of a real understanding of cost-benefit relationships. A recent American Accounting Association study concluded that in developing countries throughout the world,

> "... a great need exists for cost accounting and the presentation of analyses and various statements for planning purposes and decision-making. The economic development process is in need also of effective cost - benefit measurements for project and program evaluations, and of information for operating measurement, internal organization pricing, and other management and economic policies."[1]

A possible explanation for the lack of cost accounting could be that very few government accountants have been adequately trained in the use of cost accounting.

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[1] American Accounting Association: Committee on International Accounting Operations and Education, p. 42.

• Shortage of Trained Accountants and Financial Managers

There is a critical shortage of trained accountants and financial managers in the public sector in India as well as most other Third World countries.[1] Because of this lack of well-trained government accountants and financial managers, the most efficient allocation and utilization of resources is probably not always attained. The shortage can be attributed primarily to the fact that relatively few trained financial managers elect to work for the government. Low salary levels compared to the private sector are primarily responsible for this lack of interest. This has caused great difficulty for many government agencies in hiring and retaining trained people. This problem was cited by several India government officials as the most significant obstacle to improving the quality of governmental accounting and financial management. Government organizations that are unable to retain enough trained accountants and financial managers have little hope for improving resource management, installation of integrated financial management systems or implementation of other critically needed accounting reforms.

The accounting and financial management systems of the public sector in India appear quite deficient. These deficiencies, however, cannot be overcome without the total support of the government and that support will probably not be forthcoming unless there is a clear understanding of the importance of these functions.

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[1]Comptroller General of the United States, pp. 11-14.

Accounting Education and Training

India, as well as many other developing countries, has not identified long-range manpower requirements which detail the levels of accountants and financial managers that will be needed in the future. In addition to the absence of adequate long-range planning, several deficiencies exist in current educational and training programs. These deficiencies include:

- inadequate number of teachers
- poor quality of training
- lack of government support

• Inadequate Number of Teachers

Shortages of dedicated qualified teachers is apparently the greatest weakness in accountancy education and training in India. The shortage of teachers coupled with a shortage of current text books and teaching materials has had a detrimental effect on the supply of trained accountants and financial managers. Low pay and the pressure for good accountants elsewhere has probably contributed to the shortage as well as affected the quality of teaching.

• Poor Quality of Training

Training provided by the professional institutions may often be inadequate and of poor quality. In some instances the poor quality of the courses may be attributed to inadequately trained instructors. Many of the courses do not adequately prepare the student for a career in accounting or auditing. The training provided by the universities, however, is generally considered to be of a much higher quality than that provided by the public institutions.[1]

• Lack of Government Support

Accounting and financial management training generally has been given a low priority by the government in relation to other development programs.[2] This attitude by the government stems from the fact that apparently very few government officials really understand the contribution that effective accounting and financial management can make to continued economic development. Effective accounting education and training is essential to the development and maintenance of adequate accounting and financial management systems, since the best system available is virtually useless without properly trained people to operate it.

The analysis of the development of accounting in India identified a number of accounting and financial management deficiencies. Those deficiencies are summarized as follows:

Enterprise accounting:

- lack of cooperation within the accounting profession
- inadequate accounting research
- lack of financial measurement reporting
- detail rather than system-oriented auditing procedures

Government accounting:

- lack of integrated financial information
- incomplete or unreliable financial data

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[1] Enthoven, p. 264.

[2] Interview with Maurice Mould.

- archaic accounting systems
- inadequate budgeting process
- outdated auditing practices
- minimal cost accounting
- shortages of trained accountants and financial managers

Accounting education and training:

- inadequate number of teachers
- poor quality of training
- lack of government support

A plan to correct these deficiencies is presented in the next chapter.

CHAPTER VI

PROGRAMS FOR IMPROVEMENT

Research for this paper indicated that the accounting needs of developing countries generally involve three main elements: (1) relevant accounting and auditing standards, (2) effective training of accountants and (3) recognition of the accounting function as a tool for economic development. To properly address these needs it is necessary to understand that accounting systems and processes are influenced by socio-economic, professional, institutional, statutory, legal and various other considerations. Any program for assistance in the development of accounting systems must take into consideration these factors as well as the countries' particular paths of development. For example, the influence of British rule in India has contributed significantly to the form of its present accounting systems.

Recommendations for India

A recommended program for meeting the accounting and financial management needs of India and for correcting the deficiencies identified in the preceding chapter is as follows:

- develop relevant professional standards
- provide effective training
- recognize importance of accounting

• Develop Relevant Professional Standards

The establishment and maintenance of relevant accounting and auditing standards is one key to improving accounting and financial management in India. To provide the appropriate framework within which to develop these standards, consideration should be given to the consolidation of the various professional accounting institutes into a single body that would represent all areas of the profession. This would provide the vehicle through which uniform accounting and auditing standards could be developed. Effective accounting (including cost accounting), auditing and internal control procedures could also be formulated under the guidance of this body or under the guidance of a national research body.

Consideration should be given to establishing a national research body whose responsibility would be to conduct indepth accounting related research. The first duty of this body would be to establish an appropriate base upon which future accounting and financial management research could be built.

In the government sector an integrated financial management system should be developed that utilizes an appropriate basis of accounting in order to improve the usefulness of government financial data. The government should also require that all budget information be related to either past or present accounting data. Current government financial reports should include a comparison of budget to actual amounts. By including actual accounting data with budget data, a comparison of planned and actual financial performance can be made.

In addition to the development of accounting standards, the quality of financial information can be greatly improved by providing better training to accounting personnel.

• Provide Effective Training

A national training plan must be developed if the current inadequacies in the training of accounting personnel are to be corrected. The plan should be developed based on an inventory of currently available training programs, existing human resources and projected future needs. The process of developing this national training plan should be under the direction of a centralized body that would have access to all areas of the profession. The single professional organization that was suggested previously would be ideal to coordinate the development of such a plan.

Before any national training plan can be properly implemented, however, it will be necessary to increase the quantity as well as the quality of teachers in the various educational and professional institutes. This will require both technical and financial assistance from international donor organizations as well as a general increase in teacher salary levels in order to attract and retain qualified teaching personnel.

• Recognize Importance of Accounting

The benefits to be derived from proper accountability for resources must be conveyed to management. To accomplish this a program should be developed to inform and educate government officials as to the contribution that effective accounting and financial management can make to sustained economic development.

Implementation of these proposed recommendations will require several years to accomplish, however, they should go a long way toward eliminating inadequate accounting and financial management practices in India and improve economic development through the optimum utilization of available resources.

Program for Developing Countries

The maintenance and improvement of accountability in developing countries is a continuing task under difficult circumstances. Unless urgent steps are taken to reverse their current low output of trained personnel, developing countries may be increasingly incapable of meeting the demands for accountants and auditors. It must be emphasized, however, that assistance in the development of accounting and auditing capabilities could have a time horizon of up to twenty-five years. The reasons for this lengthy time period can be attributed to the inherent slowness with which government operates and to the start-up time required before the program begins producing trained personnel.

Because of inadequate financial and technical resources developing countries will be unable to achieve effective national accounting systems without assistance from the international community in designing and developing the financial management infrastructure.

The objectives of international assistance should include:

- design of legislation for accounting, financial reporting and auditing standards,
- design and development of national and regional plans for accounting and auditing development and training;

- identification and organization of training institutions, systems and projects;

- preparation of textbooks and training courses;

- assistance to national professional organizations and

- development of an awareness of the importance of financial management among senior officials of the governments.

A developing country may be willing to follow a sequence of changes from one accounting system to another because it has observed that some other country has successfully followed such a program to what it believes is a more appropriate accounting system. Since India is perceived to be one of the more advanced Third World countries, it is only natural that its experience in developing accounting and financial management systems should be used as a model for such programs.

A program outline for improving financial management infrastructure should be developed for each country. This should include a review of current accounting and auditing standards, development of a national accounting profession and should also cover the financial aspects of public administration. International donor organizations such as the World Bank and the Agency for International Development have a unique opportunity to assist with, as well as to ensure implementation of recommended programs. Possible ways of accomplishing these objectives could be as follows:

- audits should be required of all lending agency programs,

- noncompliance with lending agreement audit convenants should result in suspension of payments,

- agencies should actively assist countries in improving their accounting and auditing standards and financial management systems at the national level through financial and technical assistance and

- where local auditing capabilities are weak, the possibility of strengthening them through sub-contracting or joint venture audits with expatriate firms should be considered.

A handbook on governmental auditing in developing countries has recently been developed by the United Nations.[1] The handbook points out that adequate systems of internal control and internal audit are the most useful complements to external audits for the efficient management and evaluation of government operations.[2] For auditors in developing nations, the handbook has the potential to become an excellent source material for auditor training.

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[1]United Nations, Department of Economic and Social Affairs, Handbook on Governmental Auditing in Developing Countries, (ST/ESA/SER.E/8, New York, 1977.)

[2]Ibid., p.7.

In order for any recommendation for improvement to be of benefit it must be accepted and implemented. To assure implementation of needed improvements in accounting systems in developing countries, international aid organizations such as the World Bank International Development Agency, and the Agency for International Development, should include, as a condition for receiving or continuing their loans or grants, implementation of specific improvements in the accounting systems of the developing countries. This should then be carried one step further by providing funds and technical support to underwrite the cost of developing and implementing the improved systems and training the personnel to operate them. Tying financial aid to improvements in accounting can provide the necessary incentive to the developing country to follow through with their commitment.

Recommended plans to correct the accounting and financial management deficiencies identified by this paper, have been presented in this chapter. India's plan has been designed to specifically meet its needs as identified by the analysis. The suggested program for other developing countries has been modeled after India's approach to developing accounting and financial management systems. For any of these plans to be of benefit, however, they must be accepted and fully implemented.

CHAPTER VII

SUMMARY OF FINDINGS AND CONCLUSIONS

An analysis and evaluation of the development of accounting in India has been presented in this paper and based on that analysis plans for improving accounting and financial management in India and other developing countries have been formulated.

In the identification of the problems facing developing countries, certain questions were raised relating to India's experience in developing accounting and financial management systems. Those questions were:

- What is the current status of the accounting profession in India?
- Has India's development been hindered by inadequate accounting and financial management systems?
- Can India's experience in developing accounting and financial management systems be utilized by other developing countries?
- Can a uniform approach to developing adequate accounting systems be established that could be utilized as a guide in other developing countries?

Questions Answered

The purpose of this paper was to address those questions concerning the development of accounting in India and to determine whether India's experiences could be utilized in developing accounting systems in other Third World countries. Answers to those questions are presented in the following paragraphs.

- What is the current status of the accounting profession in India?

The accounting profession in India appears to be fairly well developed in the private sector while somewhat deficient in the public sector. India has a relatively strong accounting profession that is regulated by the Institute of Chartered Accountants and is directed in its duties and responsibilities by the Companies Act of 1956. The profession's weakest link can be attributed to the accountants in the public sector. Government accountants, auditors and financial managers are generally less competent than their counterparts in the private sector. This is a fact that is generally recognized for all developing countries. It is interesting to note that this statement is also true for the United States, although to a much lesser degree.

- Has India's development been hindered by inadequate accounting and financial management systems?

Without a doubt, India's economic development has been greatly hindered because of inadequate accounting and financial management systems that cannot produce accurate, relevant and timely financial management information. Without adequate financial information, optimum utilization of resources cannot be made.

- Can India's experience in developing accounting and financial management systems be utilized by other developing countries?

The accounting and financial management systems currently in use in India, although antiquated by U.S. standards, are considered to be among the most advanced systems in use by lesser developed countries. India's experience in developing these systems, therefore, can and should be utilized by other developing countries to accelerate the development of adequate financial systems within their own countries. Since India is perceived to be one of the more advanced developing countries, it is only natural that it should be used as a model.

- Can a uniform approach to developing adequate accounting systems be established that could be utilized as a guide in other developing countries?

Using India as the model, a uniform approach can be established to developing adequate accounting systems in other Third World countries. Any program for assistance, however, must take into consideration the various influences on the accounting process as well as the countries particular paths of development.

Concluding Summary

Developing nations must be made aware of the importance of adequate accounting and financial management systems, because without them the cost of economic development can become an elusive and immeasurable variable.

The need to develop adequate accounting and financial management systems in developing countries is greater now than at any time in the recent past. With a worsening of the world economy, aid to developing countries will inevitably be reduced.[1] Even India, the most favored of developing countries, is being subjected to tightening credit.[1] Because of this reduction in financial aid, it is imperative that developing countries improve their accounting and financial management systems so as to more effectively utilize and control what resources are available. The plans developed in the previous chapter of this report can help to accomplish this objective.

The analysis of the development of accounting in India identified a number of accounting and financial management deficiencies. Those deficiencies were then organized into three major areas; enterprise accounting, government accounting and accounting education and training. A plan was then developed to address these deficiencies. The plan has been specifically designed to meet India's needs as identified by the analysis. Table 1 summarizes the deficiencies identified and the solutions proposed for meeting these accounting and financial management needs.

A program for developing or improving accounting and financial management systems in other developing countries has also been formulated. The program, modeled after this analysis of India's experiences, cannot be successfully implemented without substantial support and assistance from the international community.

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[1]"U.S. to Propose Cuts to Agencies Aiding Developing Nations," Wall Street Journal, 19 February 1982, p.18.

[1]"India, Long the World Bank's Favorite, Is Told to Seek More Market-Rate Loans," Wall Street Journal, 28 January 1982, p.24.

Table I

SUMMARY OF DEFICIENCIES IDENTIFIED AND SOLUTIONS PROPOSED FOR MEETING THE ACCOUNTING AND FINANCIAL MANAGEMENT NEEDS OF INDIA

Deficiencies Identified	Solutions Proposed
Enterprise accounting	
Lack of cooperation within the accounting profession.	Consolidate the various professional accounting institutes into a single body.
Inadequate accounting research.	Establish a national research organization.
Lack of financial measurement reporting.	Develop relevant professional standards.
Detail rather than system-oriented.	Develop appropriate auditing procedures.
Government accounting	
Lack of integrated financial information.	Develop integrated financial management system.
Incomplete or unreliable financial data.	Develop government accounting and financial reporting standards.
Archaic accounting. systems.	Develop an integrated financial management system that utilizes an appropriate basis of accounting.
Inadequate budgeting process.	Improve budgetary process by requiring that all budget data be related to supporting accounting data.
Outdated auditing practices	Formulate improved auditing practices.
Minimal cost accounting.	Develop and implement appropriate accounting systems.
Shortages of trained accountants and financial managers	Develop a national training plan to meet current and future needs.
Accounting education and training	
Inadequate number of teachers.	Increase the quantity and quality of teachers through technical and financial assistance from the international community. An increase in teacher salary levels will also be required.
Poor quality of training.	Improve the quality of training by improving teacher quality.
Lack of government support.	Inform and educate management as to the importance of accounting and financial management.

For any recommendation to be of benefit, it must be accepted and implemented. To assure implementation of needed improvements, international aid organizations should tie their financial aid programs to commitments from recipient governments to improve their accounting and financial management systems. This should then be carried one step further by providing funds and technical support to underwrite the cost of developing and implementing the improved systems. Tying financial aid to implementation of improved accounting systems can provide the incentive necessary for the developing country to follow through with its commitment.

Simply upgrading accounting systems alone will not ensure continued improvements in the area of accounting and financial management. The developing countries must be encouraged and assisted in formulating comprehensive and up-to-date training programs at both the national and local levels. Improved accounting systems are of no benefit without properly trained personnel to operate them.

Developing countries must also be made aware of the importance of adequate accounting and financial management systems. They are aware of the size of the task that they face in the area of economic development and that the needs are great in comparison to the resources available to meet those needs. Also, with limited resources it is imperative that all developing countries manage their resources as effectively as possible, so as to obtain the maximum benefit from every dollar spent. Only through improved accounting and financial management will they be able to reach their goal of effectively allocating and utilizing their limited resources to improve their standards of living.

APPENDIX A.

Synopsis of Accounting Practices Required by the Companies Act of 1956

The following synopsis of accounting practices required by the Companies Act of 1956 summarizes some of the more significant requirements that must be adhered to by accountants and auditors in India.

Definitions

The difference between a provision and a reserve has special significance under the Companies Act.

1. The expression "provision" means any amount written off or retained by way of providing for depreciation, renewals or diminution in value of assets, or retained by way of providing for any known liability of which the amount cannot be determined with substantial accuracy.

2. The expression "reserve" relates to any appropriation of profit, which is not a specific provision of a known liability.

Balance Sheet

The balance sheet presentation of a company is the usual type followed by British companies showing capital and liabilities on the left side and assets on the right side. Provision has been made in the Companies Act to permit preparation of the balance sheet in any form approved by the government. Several companies have obtained government approval to prepare their balance sheets in vertical form. Footnotes must be included with the balance sheet disclosing claims against the company, unmatured liabilities on shares that have been partially paid, fixed dividends in arrears, estimated amount of unexecuted contracts and other amounts for which the company is contingently liable. The balance sheet and the profit and loss statement must show the comparable figures for the preceding period.

Accounts Receivable

Customers balances (secured, unsecured and doubtful) have to be classified between "those exceeding six months" and "others." The provision for doubtful debts must be deducted and any excess provision shown as reserve on the liabilities side of the balance sheet.

Other amounts receivable should be broken down as to:

(1) advance and loans to subsidiaries, bills of exchange, advances receivable in cash or in kind or for value to be received (i.e., rates, taxes, insurance, etc.) and

(2) the amounts due from directors and other officers of the company, etc., whether for sale of goods or otherwise, should be disclosed together with the maximum amount due from each of them during the year.

Inventories

These must be shown separately as to: stores and spare parts, loose tools, stock in trade and work in progress. The method of valuation of each of these items, except loose tools, should be stated.

Long Term Assets

The following captions must be shown separately:
Goodwill, freehold land, buildings, leasehold land, railway sidings, plant and machinery, furniture and fixtures, development of property, patents, trademarks and designs, livestock and vehicles, etc. The original cost of each item and the additions thereto and the deductions therefrom and the total depreciation written off through the end of the year are to be stated. Where original cost could not be ascertained at the time the Act became effective, the valuation shown by the books less the accumulated depreciation could be used.

Restatement of fixed assets is permitted and the credit is to be recorded in a capital reserve account. Depreciation on the restatement is not allowed for tax purposes. Any restatement of fixed assets must be disclosed in the accounts for the five years succeeding such restatement.

The minimum amount of depreciation to be provided for each depreciable asset before any dividend can be declared by a company can be computed either by applying tax rates to the written-down book value of each such asset or by reference to the number of years for which the depreciation allowance is given for tax purposes before a specified residual value is reached.

Liabilities

Secured and unsecured loans together with interest accrued and due thereon should be shown separately. These should also be broken down as to: amounts payable for debentures, loans and advances from banks, subsidiaries, directors, etc. for secured loans, and fixed deposits, loans and advances from subsidiaries, short-term and other loans and advances from banks, etc., for unsecured loans.

Other actual liabilities for acceptances, sundry creditors, amounts payable to subsidiaries, advance payments and unexpired discounts, unclaimed dividends, etc., are to be disclosed under current liabilities.

Proposed dividends and estimated liabilities for taxes, employees' pensions and other benefit schemes, contingencies, etc., should be shown under "provisions."

Stockholder Equities

The amounts authorized, issued and called for each class of stock should be stated indicating the number of shares allotted as fully paid up pursuant to a contract without payment being received in cash and the number of shares allotted as fully paid up by way of bonus shares.

Reserves and surplus should be shown separately as to capital reserve, share premium account and uncommitted reserves. Current additions and deductions must be shown for each account. A debit balance in the profit and loss account (if any) must be deducted from the uncommitted reserves.

General Income Determination Principle

The act states that the profit and loss account must clearly disclose the operating result of the company for the period covered by the account and shall disclose every material item, including receipts and expenses, for nonrecurring transactions or transactions of an exceptional nature as well as any material effect caused by changes in the basis of accounting. The following information among others must always be disclosed:

1. The turnover, that is, the aggregate amount for which net sales are effected by the company.

2. Commission paid to sole or other selling agents.

3. Brokerage and discounts on sales, other than the usual trade discount.

4. In the case of manufacturing concerns, the purchases of raw materials and the opening and closing inventory balances of goods produced.

5. The gross income derived from different operations.

6. For all businesses having work in progress the beginning and ending finished goods inventories must be shown.

7. The amounts provided for depreciation, renewals or diminution in value of fixed assets.

8. The amount of interest on the company's debentures and other fixed loans, showing separately any interest paid to managing directors and managers.

9. Income tax provision.

10. The amount reserved for repayment of shares and debentures.

11. The aggregate, if material, amounts set aside or proposed to be set aside for reserves but not including provisions made to meet any specific liability, contingency or commitment known at the date of the balance sheet.

12. The aggregate, if material, of any amounts drawn from such reserves.

13. Provisions for specific liabilities, contingencies or commitments and the amounts withdrawn from such provisions when no longer required.

14. Expenses in connection with stores and spare parts, power and fuel, rent, repairs, salaries, wages and bonus, contributions to provident and other funds; workmen and staff welfare expenses, insurance; taxes other than income taxes and miscellaneous expenses.

15. Income from other sources such as trade investments, other investments and interest must be segregated.

16. Detailed information on payments made to various categories of managerial personnel, i.e., directors and managers.

17. Payments to auditors as auditors or in any other capacity must be reported separately.

APPENDIX B

MUNICIPAL FINANCE STRUCTURE

- Income
  - Selfsource
    - Nontax Revenue
    - Tax Revenue
      - Direct
        - . Properties
        - . Business
        - . Profession
        - . Vehicle
        - . Fee on lights
        - . Pilgrims tax
        - . Passenger tax
      - Indirect
        - . Entry tax
        - . Toll tax
        - . Advertisement tax
        - . Show tax
  - External Source
    - . State Govt.
    - . General purpose grant
    - . Other grants
    - . Loans
    - . Central Govt.
    - . Nationalized banks
    - . L.I.C.
    - . HUDCO
    - . International institutions
    - . UNESCO
    - . Asian Banks
    - . World Bank
- Expenditure
  - . General administration
  - . Capital investment
  - . Public health
  - . Education
  - . Public security
  - . Miscellaneous

L.I.C. - Life Insurance Corporation
HUDCO - Housing and Urban Development Corporation

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