Comments on the Tentative Agenda Decision Classification of Income and Expenses from Cash and Cash Equivalents (IFRS 18)

The Accounting Standards Board of the Institute of Chartered Accountants of India appreciates the opportunity to submit its comments on the IFRS Interpretations Committee's Tentative Agenda Decision on **"Classification of Income and Expenses from Cash and Cash Equivalents (IFRS 18)"**.

The issue considered by the Committee concerns the classification of income and expenses from cash and cash equivalents in the consolidated statement of profit or loss where an entity has, alongside other business activities, a main business activity of investing in financial assets within the scope of paragraph 53(c) of IFRS 18 and a main business activity of providing financing to customers.

We appreciate the Committee's analysis and agree that the assessment of specified main business activities is an important element in applying the presentation requirements of IFRS 18. However, we believe that the fact pattern considered in the Tentative Agenda Decision raises certain application issues that may benefit from further clarification.

1. Overall view

We agree with the Committee that paragraph 56(a) of IFRS 18 specifically addresses the classification of income and expenses from cash and cash equivalents for an entity that invests in financial assets within the scope of paragraph 53(c) as a main business activity.

However, we believe that the interaction between paragraph 56(a) and the requirements applicable when an entity also has a main business activity of providing financing to customers warrants further consideration.

In particular, where an entity has two specified main business activities—namely, investing in financial assets and providing financing to customers—the classification of income and expenses arising from cash and cash equivalents may not necessarily reflect the nature of the activity to which the relevant cash and cash equivalents are principally connected if paragraph 56(a) is applied uniformly to all cash and cash equivalents.

Accordingly, we recommend that the Committee provide additional clarification regarding the application of paragraph 56(a) in such circumstances.

2. Relevance of the purpose and use of cash and cash equivalents

The Tentative Agenda Decision indicates that the request specifically questioned whether paragraph 56(a) applies to income and expenses from **all cash and cash equivalents**, even where income and expenses from some cash and cash equivalents relate to providing financing to customers and others relate to another business activity, such as manufacturing products.

In our view, the purpose and use of cash and cash equivalents may provide relevant information about the economic nature of the related income and expenses.

An entity may maintain cash and cash equivalents for different purposes, including:

- supporting its ordinary operating activities;
- meeting short-term liquidity requirements;

- supporting its financing activities; and
- managing liquidity arising from its specified main business activities.

Where an entity can reasonably identify that particular cash and cash equivalents are maintained in connection with a financing activity, consideration could be given to whether the related income and expenses should be classified consistently with the nature of that financing activity.

We acknowledge that cash and cash equivalents are generally highly liquid and may be fungible. Nevertheless, where the entity's treasury arrangements, internal management processes or other evidence demonstrate a clear relationship between particular cash balances and a specified main business activity, we believe that the Standard should provide sufficient clarity as to how such information should be considered.

3. Interaction between the two specified main business activities

The fact pattern considered by the Committee involves an entity that has both:

(a) a main business activity of investing in financial assets within the scope of paragraph 53(c) of IFRS 18; and

(b) a main business activity of providing financing to customers.

We believe that this fact pattern is particularly important because IFRS 18 permits an entity to have more than one main business activity. Consequently, an entity may conduct both investment and financing activities as integral parts of its business model.

In such circumstances, a blanket requirement that income and expenses from all cash and cash equivalents be classified in the operating category could result in similar economic activities being presented differently depending on whether an entity has a specified main business activity of investing in financial assets.

We therefore recommend that the Committee clarify whether paragraph 56(a) is intended to operate as an overriding requirement whenever an entity has the specified main business activity described in paragraph 53(c), irrespective of whether the relevant cash and cash equivalents are held or utilised principally in connection with another specified main business activity.

4. Need for clarity regarding cash and cash equivalents associated with financing customers

The issue becomes particularly relevant for entities whose business model includes providing financing to customers.

Where financing to customers is a main business activity, income and expenses arising from the financing activity would ordinarily be expected to be closely connected with the entity's financing operations.

The Tentative Agenda Decision states that, although the entity described in the fact pattern has a main business activity of providing financing to customers, the accounting policy choice in paragraph 56(b)(ii) is not available and paragraph 57 is not applicable. At the same time, the accounting policy choice in paragraph 65(a)(ii), relating to liabilities arising from transactions that involve only the raising of finance, remains available.

In our view, this interaction may not be immediately apparent to preparers and users of financial statements.

We therefore recommend that the final Agenda Decision explain more clearly why the existence of a main business activity of providing financing to customers does not affect the classification of income and expenses from cash and cash equivalents under paragraph 56(a).
Such clarification would assist in ensuring consistent application of IFRS 18.

5. Consideration of the nature of cash equivalents
The existing accounting framework distinguishes cash equivalents from investments held for investment purposes. Cash equivalents are generally held for meeting short-term cash commitments and are subject to requirements relating to their ready convertibility and insignificant risk of changes in value.

We believe this distinction is relevant to the issue considered by the Committee.
Where cash equivalents are primarily maintained for liquidity management and short-term commitments, their classification may appropriately follow the specific requirements of IFRS 18. However, where an entity has a specified main business activity of providing financing to customers and maintains significant cash balances as an integral component of that financing activity, further explanation may be necessary to determine how the related income and expenses should be presented.

We therefore suggest that the Committee consider whether an illustrative example could demonstrate the application of paragraph 56(a) to cash and cash equivalents maintained by an entity having more than one specified main business activity.

6. Potential diversity in practice
We believe that the issue may result in diversity in practice if entities reach different conclusions regarding whether the purpose for which cash and cash equivalents are held is relevant to the application of paragraph 56(a).

For example, an entity may have:
- a specified main business activity of investing in financial assets;
- a specified main business activity of providing financing to customers; and
- other operating activities.

The entity may hold cash and cash equivalents in connection with each of these activities.
In such circumstances, it would be useful to clarify whether:
(a) all income and expenses from cash and cash equivalents are required to be classified in the operating category solely because the entity has the specified main business activity described in paragraph 53(c);
(b) the purpose for which particular cash and cash equivalents are held may be considered; or
(c) the entity is required to apply paragraph 56(a) without regard to the purpose or use of individual cash balances.
A clear statement on this point would significantly enhance consistent application of IFRS 18.

7. Management judgement and supporting evidence
The assessment of an entity's main business activities is inherently based on facts and circumstances.

Accordingly, where an entity has multiple specified main business activities, we believe that the information used by management in managing liquidity and evaluating the performance of those activities may provide useful evidence.

For example, relevant evidence could include the manner in which cash balances are managed, the entity's treasury arrangements and the relationship between liquidity maintained and the entity's financing activities.

We therefore suggest that the final Agenda Decision clarify whether such evidence is relevant in determining the classification of income and expenses from cash and cash equivalents.

8. Interaction with paragraph 65(a)(ii)
The Tentative Agenda Decision notes that the accounting policy choice in paragraph 65(a)(ii), relating to liabilities arising from transactions that involve only the raising of finance, remains available even though the accounting policy choice in paragraph 56(b)(ii) is not available and paragraph 57 is not applicable.

We believe that this interaction may create practical questions concerning the presentation of financing-related income and expenses.

Accordingly, we recommend that the final Agenda Decision include a more explicit explanation of the relationship between paragraphs 56, 57 and 65 in circumstances in which the entity has both investing and financing as specified main business activities.

This would assist preparers in understanding the intended presentation outcome and reduce the risk of inconsistent application.

9. Whether additional illustrative guidance would be useful
We acknowledge the Committee's conclusion that the principles and requirements in IFRS 18 provide an adequate basis for determining the classification of income and expenses from cash and cash equivalents.

Nevertheless, considering the interaction between several requirements and the possibility of entities having multiple specified main business activities, we believe that an illustrative example would be useful.

Such an example could demonstrate:
1. an entity having investing in financial assets as a main business activity;
2. the same entity also having providing financing to customers as a main business activity;
3. cash and cash equivalents being maintained for different purposes;
4. the application of paragraph 56(a) to the resulting income and expenses; and
5. the interaction with paragraphs 56(b)(ii), 57 and 65(a)(ii).

This would provide greater implementation clarity without necessarily requiring a standard-setting project.

10. Conclusion and recommendation
We appreciate the Committee's consideration of this matter and agree that the principles and requirements of IFRS 18 provide an important framework for determining the classification of income and expenses.

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However, in view of the practical implications of paragraph 56(a) for entities having more than one specified main business activity, we believe that additional clarification would be beneficial.

Accordingly, we recommend that the Committee consider revising or supplementing the final Agenda Decision to clarify that:

(a) paragraph 56(a) requires income and expenses from cash and cash equivalents to be classified in the operating category where the specified conditions in that paragraph are met;
(b) where an entity has more than one specified main business activity, the interaction between paragraph 56(a) and the requirements applicable to providing financing to customers should be explicitly explained;
(c) the final guidance should clarify whether, and to what extent, the purpose for which cash and cash equivalents are held is relevant to the classification assessment;
(d) the availability or non-availability of the accounting policy choices in paragraphs 56(b)(ii), 57 and 65(a)(ii) should be explained together to provide a comprehensive understanding of the resulting presentation; and
(e) an illustrative example should be considered to demonstrate the application of the requirements where an entity has both investing and financing as specified main business activities and holds cash and cash equivalents in connection with those activities.

In view of the above, while we do not necessarily believe that a separate standard-setting project is required, we believe that **additional application guidance or an illustrative example would significantly enhance clarity and promote consistent application of IFRS 18 in practice**.

We thank the Committee for providing stakeholders with an opportunity to comment on this important matter.