RE: Request for Information Post-implementation Review of IFRS 9, Financial Instruments: Classification and Measurement issued by the IASB for comments.

INDAS <indas@pnb.co.in>

Fri 10-12-2021 17:20

To: Comments ASB - ICAI <commentsasb@icai.in>

Cc: hr@scopeonline.in <hr@scopeonline.in>; MD PS <mdps@pnb.co.in>; INDAS <indas@pnb.co.in>; Anuj Kansal <anujkansal@pnb.co.in>; P. K.Varshney <pkv@pnb.co.in>; Ram Kishore Khichi <rkkhichi@pnb.co.in>; Mahesh Dhawan <mahesh.dhawan@pnb.co.in>; Dilip K. Jain <jaindk@pnb.co.in>

PUNJAB NATIONAL BANK
FINANCE DIVISION
GROUND FLOOR, WEST WING, PLOT NO.4, SECTOR- 10,
DWARKA, NEW DELHI- 110075
Email: indas@pnb.co.in

Date: 09/12/2021

Dear Sir,

This is with reference to the trailing email dt.12.10.2021 vide which our views/ comments were sought on **Request for Information: "Post-implementation Review of IFRS 9—Classification and Measurement issued by the IASB".**

In this regard, our view/comments on **Business model for managing financial assets and Amortised cost and the effective interest method** are as under:-

Business model for managing financial assets

(a) Is the business model assessment working as the Board intended? Why or why not?
(b) Can the business model assessment be applied consistently? Why or why not?
(c) Are there any unexpected effects arising from the business model assessment? How significant are these effects?

Comments:
(a):- An entity's business model refers to how an entity manages its financial assets so at to generate/realise cash flows. In other words, business model is concerned with whether an entity will collect contractual cash flows by holding them to maturity or sell those financial assets or both. An entity may have one of the following models for its debt instruments:-

(i) Hold to collect contractual cash flows
(ii) Hold to collect contractual cash flows and selling financial assets
(iii) Other business models

An entity's business model for managing the financial assets is a matter of fact and not merely an assertion. It is observable through particular activities that an entity undertakes to achieve the objectives of the business model. An entity will need to use judgment to determine the business model for managing financial assets. It depends on facts and circumstances as well as the intentions of an entity as it relates to particular instruments.
In our view, business model assessment working will help to achieve the board's objective.
(b):- In our view business model assessment may be applied consistently. Discussion on the same is as under:-
An entity's business model is determined at a level which reflects how groups of financial assets are managed together to achieve a particular business objective. An entity will be able to split its financial assets in two portfolios/sub-portfolios, only if the assets belonging to each sub-portfolio are defined and separately identifiable. If this is not the case, a sub-portfolio approach will not be appropriate. It is clear that judgment is required when determining the level of aggregation to which the business model assessment is made.
An entity determines that the objective for its portfolio of financial assets is to hold till maturity for collecting contractual cash flow. However, there are few past sales related to the portfolio. : Although the entity's business model is to hold financial assets for collecting contractual cash flows, it does not require all the instruments to be held until maturity. Hence, an entity may have business model for holding financial assets to collect contractual cash flows despite the fact that sales of financial assets occur or are likely to occur in the future. Ind AS 109 requires an entity to consider the following to evaluate the impact on sales on the hold to collect business model:-

- Frequency, value and timing of sales in prior periods
- Reasons for the sales, and
- Expectations about future sales activity

The following scenarios may be consistent with the hold-to-collect business model:-

(a) The fact that an entity's sells financial assets due to increase in the assets credit risk does not vitiate the entity's business model of holding assets to collect contractual cash flows.
(b) Sales that occur for other reasons, e.g. Sales made to manage credit concentration risk (without an increase in the assets credit risk), may also be consistent with the hold-to-collect business model.
(c) Sales may be consistent with the objective of holding financial assets to collect contractual cash flows, if the sales are made close to maturity of the financial assets and proceeds from the sales approximate the collection of the remaining contractual cash flows.

(c):- Cost benefit analysis of business model assessment is yet to be done.

Amortised cost and the effective interest method

(a) Is the effective interest method working as the Board intended? Why or why not?
(b) Can the effective interest method be applied consistently? Why or why not?

Comments
(a):- In our view the effective interest method working fine and useful for determining amortised cost and for allocation of interest income/expense. Discussed in details as under:-
The amortized cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, and for financial assets, adjusted for any loss allowance.
The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability (or a group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.
The effective interest rate (EIR) is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the gross carrying amount of a financial asset or to the amortised cost of a financial liability. For financial assets, the gross carrying amount is generally the point of reference for applying the effective interest method as it does not take into account the loss allowance for the financial asset.
The rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset or to the amortised cost of a financial liability. When calculating the effective interest rate, an entity shall estimate the expected cash flows by considering all the contractual terms of the financial instrument (for example, prepayment, extension, call and similar options) but shall not consider the expected credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts.
In applying the effective interest method, an entity identifies fees that are an integral part of the effective interest rate of a financial instrument. The description of fees for financial services may not be indicative of the nature and substance of the services provided. Fees that are an integral part of the effective interest rate of a financial instrument are treated as an adjustment to the effective interest rate, unless the financial instrument is measured at fair value, with the change in fair value being recognised in profit or loss. In those cases, the fees are recognised as revenue or expense when the instrument is initially recognised.
(b):- In our view effective interest method may be applied consistently. Discussion on the same is as under:-
Treatment of processing fees belonging to undisbursed term loan:- When calculating the effective interest rate, an entity shall estimate the expected cash flows by considering all the contractual terms of the financial instrument (for example, prepayment, extention, call and similar options) but shall not consider the expected credit losses. It may be noted that to the extent there is evidence that it is probable that the undisbursed term loan will be drawn down in the future the processing fee is accounted for as a transaction cost under Ind AS 109 i.e. the fee is deferred and deducted from carrying value of the financial liabilities when the draw down occurs and considered in the effective interest rate calculations. However it is not probable that the undisbursed term loan will be draw down in the future then the fees is recognised as an expense on a straight line basis over the term of the disbursed loan. Assuming that the undisbursed loan amount will be disbursed in future, the entire processing fee, i.e. processing fee pertaining to the disbursed as well as to the undisbursed loan amount will be included, while calculating the effective interest rate of the loan and is recognised as an expense over the term of the loan.
Amortisation period of transaction costs:- Fees, Points paid or received, transaction costs and other premiums or discounts that are integral to the effective interest rate shall be amortised over the instrument's expected life.

Yours Faithfully,

Sd/-
General Manager (Finance)
Punjab National Bank

From: SCOPE HR <hr@scopeonline.in>
Sent: 12 October 2021 05:20 PM
To: cmd@bhel.in; nalinshinghal@bhel.in; GAIL <cmd@gail.co.in>; GAIL <manojjain@gail.co.in>; Chairman IOCL <chairman@indianoil.in>; CMD NTPC <cmd@ntpc.co.in>; cmd@ongc.co.in; cmd@powergrid.in; Chairmansail <chairman.sail@sail.in>; CMD Bharat Petroleum <cmd@bharatpetroleum.in>; padmakar पद्माकर के <padmakark@bharatpetroleum.in>; CMD HPCL <cmd@hpcl.in>; Coal India <chairman.cil@coalindia.in>; CMD CONCOR <cmd@concorindia.com>; CMD EIL <cmd@eil.co.in>; CMD MTNL <cmd@bol.net.in>; cmd-nbcc@nic.in; cmdsectt-nbcc@nic.in; dpsectt-nbcc@nic.in; Oil India Limited CMD <cmd@oilindia.in>; rsdhillon@pfcindia.com; CMD REC <cmd@recl.in>; Shipping Corp. <cmd@sci.co.in>; Cmd <cmd@nalcoindia.co.in>; Cmd <cmd@bel.co.in>; chairman@hal-india.co.in; cmd@nmdc.co.in; NLC <cmd@nlcindia.in>; CMD RINL <cmd@vizagsteel.com>; cmd@airindia.in; aniidco@gmail.com; cmd@andrewyule.com; cmd@antrix.co.in; cmdalimco@alimco.in; adika.rs@balmerlawrie.com; MD & CEO BoB <md.ceo@bankofbaroda.com>; mdceo@mahabank.co.in; cmd@beml.co.in; abhijit.pati@vedanta.co.in; cmd.bccl.cil@coalindia.in; cmdbdl@bdl-india.in; md.bibcol@nic.in; bpclindia@sancharnet.in; cmd@bharatpumps.co.in;