Exposure Draft of Amendments to Ind AS 109 and Ind AS 107

Suggestions by: Bhopal Branch (CIRC)

Submitted on 30th September 2024

1. Ind AS 109: Financial Instruments – Derecognition and Classification of Financial Assets

Key Amendment: The document proposes amendments to the recognition, derecognition, and classification of financial instruments.

Response: *Agree*
Rationale:

- The new guidance around **electronic payment systems** (paragraph B3.3.8) is practical, allowing entities to derecognize a financial liability even if the payment hasn't been fully settled as long as it is practically impossible to reverse the payment. This is a reasonable approach that reflects the real-world function of electronic payment systems.
- The emphasis on **contractual cash flows** (B4.1.8A and related sections) reinforces the principle that a financial asset must be aligned with basic lending arrangements to qualify as solely payments of principal and interest (SPPI). This amendment helps ensure that financial assets are consistently classified based on their nature, preventing any misclassification that could distort financial reporting.

Alternative Approach: While the amendments are sound, to further improve clarity, the ICAI could provide more **sector-specific examples** of financial instruments, particularly in markets where non-standard lending arrangements are common (e.g., fintech or peer-to-peer lending), to ensure entities properly classify instruments under these rules.

2. Ind AS 109: Financial Instruments – Application of Non-Recourse Features

Key Amendment: Changes to the handling of non-recourse features in financial instruments.

Response: *Agree*
Rationale:
The guidance ensures that financial instruments with non-recourse features are evaluated appropriately by requiring entities to "look through" to the underlying assets or cash flows. This ensures that entities do not misclassify assets with complex risk profiles. The rules provide a robust framework for determining when a financial asset qualifies as solely payments of principal and interest (SPPI), improving classification accuracy and transparency.

Alternative Approach:
A **quantitative materiality threshold** could be added to help entities determine when the non-recourse features or structured nature of an instrument have a material effect on cash flows,

making the classification as SPPI inappropriate. This would provide entities with clearer guidelines for borderline cases.

3. Ind AS 107: Financial Instruments – Disclosures Related to Cash Flow Contingencies

Key Amendment: Requirements for entities to disclose information about contractual cash flow changes tied to contingent events not related to basic lending risks, such as carbon emissions targets (paragraphs 20C and 20D).

Response: *Agree*
Rationale:
These amendments enhance transparency by requiring disclosure of contingent events that affect cash flows but are unrelated to traditional lending risks like credit or interest rate risks. This is especially important in cases where companies link financial instrument performance to ESG targets, like reductions in carbon emissions. The new disclosures allow users to understand how such contingent events could impact financial positions, providing better insights for risk management.

Alternative Approach:
To avoid excessive disclosure requirements, a **materiality filter** could be introduced. Entities could disclose contingent events only when they are expected to cause a **material change** to the financial instrument's cash flows, simplifying reporting for companies with immaterial contingencies.

4. Ind AS 109: Financial Instruments – Transition Requirements

Key Amendment: The amendments must be applied retrospectively, but entities are not required to restate prior periods unless it can be done without the use of hindsight.

Response: *Agree*
Rationale:
This approach strikes a balance between consistency and practicality. By not requiring restatement of prior periods, it reduces the administrative burden on entities, while still ensuring that adjustments are made from the date of initial application. The stipulation that restatement is permitted only if hindsight is not required protects the integrity of the financial reporting process.

Alternative Approach:

We can consider offering a **modified retrospective approach** where companies only apply the new standards to the current period, while providing a disclosure of what the impact would have been in prior periods. This would further reduce the operational burden, especially for smaller entities or those in developing economies with limited resources for retrospective calculations.

5. Ind AS 109: Financial Instruments – Climate-related Financial Instruments

Key Amendment: Addressing contingent features related to environmental factors (e.g., changes in carbon emissions) that adjust financial cash flows (B4.1.10A).

Response: *Agree*
Rationale:
This amendment is forward-looking, recognizing the increasing importance of ESG factors in financial arrangements. By clarifying how to treat features tied to environmental outcomes, it provides companies and investors with clear guidance on handling these emerging instruments. It allows for better risk assessment and classification of instruments tied to climate-related contingencies.

Alternative Approach:
We can consider adding **specific sector guidance** for industries most likely to engage in climate-related financing (e.g., energy, utilities), ensuring that the rules are tailored to the specific financial instruments commonly used in these sectors.

These detailed comments aim to provide insights into how the proposed amendments to Ind AS 109 and Ind AS 107 will improve financial reporting, while also suggesting alternative approaches to further enhance clarity and practicality in implementation.