Minutes of the 13th Meeting of National Financial Reporting Authority

The 13th Meeting of the National Financial Reporting Authority was held on 20 February 2024 at NFRA office. The meeting was chaired by Dr. Ajay Bhushan Prasad Pandey, Chairperson, NFRA. The meeting was attended by the following Members/officials:

Full Time Members:

a) Dr. Praveen Kumar Tiwari
b) Ms. Smita Jhingran

Part Time Members:

a) Shri IDS Dhariwal, Joint Secretary, Ministry of Corporate Affairs
b) Shri S V Muralidhar Rao, Executive Director, Securities and Exchange Board of India.
c) Ms. Sudha Balakrishnan, Chief Financial Officer, Reserve Bank of India (online)
d) CA. Ranjeet Kumar Agarwal, President ICAI
e) CA. Pramod Jain, Chairman, Accounting Standard Board, ICAI
f) CA. (Dr.) Sanjeev Kumar Singhal, Chairman, Auditing and Assurance Standard Board, ICAI
g) Professor Sanjay Kallapur, Professor of Accounting at Indian School of Business, Hyderabad
h) Professor R. Narayanaswamy, Ex-Faculty of the Finance & Accounting, IIM Bangalore

Officials

a) Ms Vidhu Sood, Secretary, NFRA
b) CA Vidhyadhar Kulkarni, Sr. Consultant, NFRA

2. The quorum for the meeting of the Authority was met in accordance with para 3(9) of the National Financial Reporting Authority (Meeting for Transaction of Business) Rules, 2019. Ms. Kavita Prasad, Director General, O/o CAG of India, was granted leave of absence.

3. Chairperson welcomed the participants and apprised the members about the agenda item for the meeting comprising (i) status of carve-out in para 74 of Ind AS 1, Presentation of Financial Statements, regarding classification of long-term loan in the event of material breach of loan covenant(s) where the lender has waived this breach before the approval of the financial statements and, (ii) MCA's reference to NFRA regarding suggesting valuation methodology of AT-1 bonds. Chairperson also welcomed newly elected President of the ICAI, CA Ranjeet Kumar Agarwal, to the Authority.

4. A presentation was made on the following agenda issues which were deliberated in the meeting.

4.1 **Agenda Item No.1 - Consideration of the recommendations of the Institute of Chartered Accountants of India (ICAI) regarding *Classification of Liabilities as Current or Non-current* and *Non-current Liabilities with Covenants:* Amendments to Indian Accounting Standard (Ind AS) 1, *Presentation of Financial Statements***

a. The Authority discussed the amendments to Indian Accounting Standard (Ind AS) 1, *Presentation of Financial Statements,* proposed by ICAI, which were approved for recommendation to the Ministry of Corporate Affairs.

b. The matter relating to ICAI's initial proposal (at the time of issue of Exposure Draft) regarding removal of the existing carve-out in para 74 of Ind AS 1 and its subsequent recommendation on its continued retention based on feedback received, was discussed. ICAI had recommended in its proposal to NFRA to continue with the carve-out primarily due to concerns raised by Indian Banks' Association (IBA). In this regard, the Members deliberated and noted the following.

i. The carve-out has been in place since the implementation of Ind AS Framework from 2015-16 and sufficient transition time has elapsed since then.
ii. NFRA had consulted the Banking Sector Prudential Regulator viz. Reserve Bank of India (RBI) who had stated that domestic financial reporting standards should be aligned with global best practices and any decision to remove the carve-out may factor in the time required for smooth transition to new regime, and a period of one or two years may be provided for transition.
iii. Covenants in the bank loans or credit facilities are expected to increase in view of the new type of credit facilities to emerging business and operating environment such as Green Financing.
iv. The Authority also noted that there is a consequential existing carve-out in para 3 of another standard viz. Ind AS 10, *Events after the Reporting Period.* The text of that carve-out is reproduced below.

- "Notwithstanding anything contained above, where there is a breach of a material provision of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand on the reporting date, the agreement by lender before the approval of the financial statements for issue, to not demand payment as a consequence of the breach, shall be considered as an adjusting event."

c. Members felt that the suggestion of RBI to give transition time of one or two years can be considered but the same may be recommended to be suitably incorporated in the Ind AS Rules 2015 to be notified by the Central Government. This will be helpful to the stakeholders and enable them to take necessary steps for the transition to the new regime.

4.2 Accordingly, it was agreed to recommend to the Ministry of Corporate Affairs as follows.

i) Paragraph 139U of Ind AS 1, Presentation of Financial Statements may be replaced as given below.

"*139U Classification of Liabilities as Current or Non-current and Noncurrent Liabilities with Covenants, amended paragraphs 60, 69, 71, 73, 74 and 75 and added paragraphs 72A, 72B, 75A, 76, 76ZA, 76A and 76B. An entity shall apply those amendments for annual reporting periods beginning on or after 1 April 2024 retrospectively in accordance with Ind AS 8. However, for annual reporting periods beginning on or after 1 April 2026 an entity shall follow following paragraphs 74 retrospectively in accordance with Ind AS 8.*

When an entity breaches a covenant of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand, it classifies the liability as current, even if the lender agreed, after the reporting period and before the approval of the financial statements for issue, not to demand payment as a consequence of the breach. An entity classifies the liability as current because, at the end of the reporting period, it does not have the right to defer its settlement for at least twelve months after that date."

ii) Further because of the above, the following amendments shall be made for *annual reporting periods beginning on or after 1 April 2026:*

1. Following text of Paragraph 76 shall be added as follows:

76. If the following events occur between the end of the reporting period and the date the financial statements are approved for issue, those events are disclosed as non-adjusting events in accordance with Ind AS 10, *Events after the Reporting Period*:

- refinancing on a long-term basis of a liability classified as current (see paragraph 72);
- rectification of a breach of a long-term loan arrangement classified as current (see paragraph 74); and
- the granting by the lender of a period of grace to rectify a breach of a long-term loan arrangement classified as current (see paragraph 75); and
- settlement of a liability classified as non-current (see paragraph 75A).
    - In para 75, the word 'However' may be added in the beginning of that para.
    - Reference of paragraph 76(d) may be added in paragraph 75A
    - Consequential amendments in Appendix 1 may also be made

iii) A footnote may be included in para 3 of Ind AS 10 as given below.

"*Following text in para 3 stands deleted for annual reporting periods beginning on or after 1 April 2026.*

*Notwithstanding anything contained above, where there is a breach of a material covenant of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand on the reporting date, the agreement by lender before the approval of the financial statements for issue, to not demand payment as a consequence of the breach, shall be considered as an adjusting even*t."

Because of the above, the following para may be added.

23CA *Classification of Liabilities as Current or Non-current and Noncurrent Liabilities with Covenants (Amendments to Ind AS 1), amended paragraph 3 for annual accounting periods beginning on or after 1 April 2026.*

Consequential changes to Appendix 1 may also be made.

4.3 **Agenda Item No. 2 - Consideration of the recommendations of the ICAI amendments to Indian Accounting Standard- Ind AS 7 and Ind AS 107**

Amendments to Ind AS 7, *Statement of Cash Flows* and Ind AS 107, *Financial Instruments: Disclosures* as recommended by ICAI were approved for recommendation to the Ministry of Corporate Affairs.

4.4 **Agenda Item No. 3 - Consideration of the recommendations of the ICAI**

Amendments to Indian Accounting Standards (Ind AS)- Editorial Corrections Amendments to Ind AS 101, Ind AS 108, Ind AS 109, Ind AS 115, Ind AS 117, Ind AS 28 and Ind AS 32.

Editorial Corrections to Ind AS 101, Ind AS 108, Ind AS 109, Ind AS 115, Ind AS 117, Ind AS 28 and Ind AS 32 as recommended by ICAI were approved for recommendation to the Ministry of Corporate Affairs.

4.5 Agenda Item No. 4 - MCA referral regarding valuation methodology for AT-1 Bonds

Authority was apprised that Ministry of Corporate Affairs, Government of India (MCA), vide letter dated 12.01.2024, had referred to National Financial Reporting Authority (NFRA), the proposal of Department of Economic Affairs, Ministry of Finance for NFRA's recommendation on the valuation methodology for AT-1 Bonds.

i. It was noted by the Authority that the reference to the Authority had been made in keeping with NFRA's remit under u/s 132(2) of the Companies Act 2013, '*to recommend accounting and auditing policies and standards to be adopted by companies for approval by the Central Government and to monitor and enforce compliance with accounting standards and auditing standards etc.*
ii. RBI permits the issue of AT-1 bonds that are Perpetual Debt Instruments (PDIs) with loss absorption features in conformity with Basel III capital adequacy norms. AT-1 bonds carry a higher coupon rate on account of associated risk and are an important source of quasi-equity capital for Banks globally Investors in such Bonds include Mutual Funds, Corporates and other institutional investors.
iii. The Authority took note of SEBI (Mutual Fund) Regulations 1996, and the two SEBI circulars of March 2021 on prudential investment limits for mutual funds for AT-1 bonds, and valuation of bonds. The Authority was apprised of RBI views, RBI Master Directions/Circulars, FBIL[1] and FIMMDA[2] and IRDAI Guidelines as relevant to the issue on fair value measurement of investments. In the case of Banks, valuation of Investment Portfolios are based on the Master Directions/Circulars issued by the RBI. Chapter 1 of the RBI Master Direction[3] has definitions of various key terms including those relevant for fair value measurement for investments, where prescribed. It was noted that these terms are broadly in line with those in Ind AS 113, *Fair Value Measurement*.
iv. Since various regulators require the valuation of investments based on fair value, the Authority considered it relevant and essential to follow the Principles and Concept of Fair Value Measurement in the Financial Reporting Framework applicable for General Purpose Financial Statements.
v. Valuation of Financial Instruments such as Bonds, Debentures and Equity Instruments is an important and material accounting matter in the broader area of financial reporting frameworks. In the financial reporting frameworks, valuation is generally referred to as 'Measurement Basis' and two categories of measurement bases viz. Historical Cost and Current Value are recognised by the Conceptual Framework.
vi. In the former category, amortised cost is the commonly used measurement approach; and in the latter category, Fair Value, Value-in-Use for Assets, Fulfilment Value for Liabilities, and Current Costs are the common approaches. It is important to note that specific individual accounting standards prescribe specific principles and detailed guidelines as to when and how to apply these different measurement bases to various assets and liabilities. In view of the wider

[1] Financial Benchmarks India Private Ltd.
[2] Fixed Income Money Market and Derivatives Association of India
[3] RBI/DOR/2023-24/104 DOR.MRG.36/21.04.141/2023-24 effective for accounting period commencing on or after April 1,2024

relevance and application of fair value in the financial reporting, there is a specific and comprehensive Indian Accounting Standard viz. Ind AS 113[4], as a single source of Fair Value Measurement Principles and related guidance. Ind AS 113 is based on high-quality globally accepted IFRS Accounting Standards viz IFRS 13.

vii. Certain key features of Fair Value Measurement principles in Ind AS 113 state that Fair Value is a market-based measurement reflecting market participants' perspective in an orderly market transaction. Fair value measurement approaches under Ind AS 113 can be broadly categorised into two types viz., Quoted Price in Active Markets (Level 1 Fair Value Hierarchy) and Valuation Techniques (Level 2 & 3 Fair Value Hierarchies)

viii. As per Ind AS 113, Fair Value is based on the 'assumption' that the asset or liability is exchanged in an orderly transaction between market participants. An entity shall measure the fair value of an asset or a liability using the assumptions that market participants would use when pricing the asset or liability, if market participants act in their economic best interest. Even when the Fair Value is determined using valuation techniques, the methodology to be used has to be based on valuation assumptions or approaches generally used by market participants.

ix. Therefore, the main issue determined by the Authority was to determine a basis for valuation of AT-1 bonds which would be in sync with Ind AS 113 and also mirror the global market practice for valuation for such bonds, as the global market for these bonds appears mature and functioning well.

x. The Authority had obtained the view various experts and expert bodies including RBI, SEBI and IBBI on the practices followed by them in market- based measurement and the assumptions/techniques used by them. The following institutions also briefly presented their views and provided clarifications to the queries from the Authority members.
    - FIMMDA
    - AMFI
    - CRISIL
    - ICRA
    - CARE Ratings
    - ICICI Mutual Funds

xi. The Authority also reviewed the live global market trades of AT-1 bonds as on 20.02.24. This was facilitated by Treasury Officers of the State Bank of India, through a live demonstration on the Bloomberg terminal. It was observed in the live trades that mostly the AT-1 bonds were trading on YTC basis.

xii. The Authority noted that the theme underpinning the fair value measurement in Ind AS 113 is a market-based measurement considering the traded/quoted prices, data and information observed from the markets and the assumptions and practices of market participants.

xiii. Chairman, ASB, ICAI stated that, in his opinion, the instant matter pertaining to valuation of a particular security does not seem to fall within the purview of NFRA. Chairman, ASB, was apprised that the matter pertained to the interpretation of Ind AS (Ind AS 113). Such an examination, therefore, is integral to functions bestowed upon NFRA under s.132 (2) of CA 2013 (monitoring and enforcing compliance with accounting and auditing standards).

[4] Ind AS 113 is corresponding to IFRS 13 *Fair Value Measurement* which is an IFRS Accounting Standard developed by the International Accounting Standards Board (IASB) of IFRS Foundation jointly with U.S. national standard-setter, the Financial Accounting Standards Board (FASB) as common requirements for measuring fair value and for disclosing information about fair value measurements in accordance with IFRSs and U.S. generally accepted accounting principles (GAAP) – Topic 820 (previously SFAS 157)

xiv. Based on the discussions, it was decided to prepare a draft discussion note to be sent for comments and views of the Authority before finalising recommendations on the issue.

The meeting ended with a vote of thanks.

-sd/-
Secretary, NFRA