FIDC

Finance Industry Development Council

(A body incorporated as a Self Regulatory Organisation for Registered NBFCs)

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Note on significant changes envisaged in Indian Accounting Standards (Ind AS) and issues that NBFCs may face

The Ind AS to be implemented effective April 2018 requires significant changes to be made by NBFCs in their accounting policies/practices. The significant ones and the concerns are highlighted below:

1. Ind AS mandates recognition of income on loans given on the basis of "effective interest rates", which are determined on the basis of expected pattern of behaviour of the portfolio taking into account prepayment probability, fee income amortisation, delinquency etc. Currently fee income is usually recognised up front, while interest on all non-NPA loans are recognised on accrual basis. Interest on NPAs is recognised on cash basis etc. There is no judgement involved and hence comparability of numbers is higher. Under the Ind AS since there is a judgement involved in determining the effective rate, there may be divergence in the way different entities report numbers.

2. Recognition of NPA and provision therefor is based on expected credit loss (ECL). ECL may vary across entities and types of businesses depending upon the behaviour expected as per the judgement of the NBFC. This may lead to differences in reporting an account as regular or NPA and on the amount of provision being carried in the accounts. What would this mean for a consortium-based lending? Whose judgement will prevail? What are the implications for a Joint Lender Forum mandated to be created in case of SMA2 assets when different lenders may opine differently on the same customer?

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3. There is no clarity on whether Income Tax authorities will consider the new Ind AS as the basis for tax assessments, especially on income recognition and provision for ECL. Absent this clarity, there could be adverse impact on the NBFC's financial position.

4. In respect of purchase of assets (say for own consumption or for leasing out) on credit terms/usance LC basis, the Ind AS states that the difference between the upfront price and the deferred payment price should be recognised as interest expenses and expensed over the credit period. What are the implications of this on GST? Will GST be charged on the total bill (even though a part of the invoice value may be "interest" as per Ind AS)?

5. In respect of Securitisation/Direct assignment, the question of derecognition of the asset being securitised is a critical factor from an NBFC perspective from a CRAR point of view. The Ind AS lays down that derecognition will be dependent upon the selling entity not retaining control and the income/losses will be proportionate to the involvement. It is unclear if continuing to hold 10% of the interest as MRR and retaining servicing rights would be deemed to "retaining control" and therefore will derecognition of the securitised assets would be allowed or not.

6. Whether Other Comprehensive Income (OCI) will form part of NOF for the purposes of CRAR or not?

We request the Reserve Bank to kindly clarify on these concerns.