FAQ on Elaboration of terms ‘infrequent number of sales’ or ‘insignificant in value’ used in Ind AS 109

Question

Ind AS 109, *Financial Instruments*, requires an entity to classify financial assets on the basis of the entity’s business model for managing the financial assets. In this regard, under a business model whose objective is to hold assets in order to collect contractual cash flows, the Standard provides that for this purpose, it is necessary to consider the frequency, value and timing of sales in prior periods. Ind AS 109 appears to envisage sale of assets held under the amortised cost category before maturity, the application guidance of Ind AS 109 states that such sales may be consistent with a business model whose objective is to hold financial assets in order to collect contractual cash flows if those sales are infrequent (even if significant in value) or insignificant in value both individually and in aggregate (even if frequent).

In view of the above, the following may be clarified:

a) How should the terms ‘infrequent number of sales’ or ‘insignificant in value’ be interpreted and determined. Can indicative rebuttable thresholds be prescribed for sales that are more than insignificant in value?

b) What is the relation between the terms ‘immaterial’ and ‘insignificant’?

Response

Ind AS 109 does not define the terms ‘infrequent number of sales’ or ‘insignificant in value’. However, these terms have been used in the Standard in the context of determination of business model. Under Ind AS 109, generally, sales which are ‘infrequent in number’ or ‘insignificant in value’ are considered to be consistent with a business model whose objective is to hold financial assets in order to collect contractual cash flows. The Standard does not lay down any thresholds for value or number in this regard.

However, the Standard provides detailed guidance on the hold to collect business model. In 2012, IASB had made limited amendments in IFRS 9 to clarify the objective of the hold to collect business model by providing additional application guidance. Ind AS 109 discusses various situations including credit risk where business model may be to hold assets to collect contractual cash flows even if the entity sells financial assets before maturity. Ind AS 109 provides that frequency and value of sales due to an increase in the assets’ credit risk may not be inconsistent with a business model whose objective is to hold financial assets to collect contractual cash flows. Accordingly, while determining the business model, management may decide the situations in which sales of financial assets occurring before the maturity date may not be considered inconsistent with the entity’s business model whose objective is to hold assets in order to collect contractual cash flows, e.g., an entity may lay down some criteria such as, if an entity sells a security which is initially rated as AAA security and subsequently, it is rated as BB, it will not be inconsistent with the entity’s business model whose objective is to hold assets in order to collect contractual cash flows because the management may want to rebalance its portfolio by selling it rather than waiting till the maturity date. There can be other situations also depending upon the facts and circumstances which need to be judged by the management.

In this regard, apart from the guidance contained in the Standard, the Basis of Conclusions to IFRS 9 contains an additional instance in which sales of financial assets occurring before the maturity date may not be considered inconsistent with the entity's business model whose objective is to hold assets in order to collect contractual cash flows. The instance relates to change in the regulatory treatment of a particular type of financial asset which may cause an entity to undertake a significant rebalancing of its portfolio in a particular period.

In view of the above, following may be concluded:

a) On the reading of Ind AS 109 along with the Basis of Conclusions to IFRS 9, it can be concluded that it is a matter of judgement which should be assesssed keeping in view the facts and circumstances pertaining to each case. Therefore, no rule of thumb in terms of even indicative percentage can be laid down to determine 'infrequent number of sales' or 'insignificant in value', since it may not be applicable in all cases considering the differing quantum, configuration and nature of financial assets in different entities. Hence, no indicative rebuttable thresholds can be prescribed for sales that are more than insignificant in value.

b) With regard to relation between terms 'immaterial' and 'insignificant', it may be noted that guidance on the term 'materiality' is already there in Ind AS which also does not lay down any criteria based on indicative fixed percentages. However, the term 'insignificant' has not been defined and can be interpreted to mean 'less than material' or almost 'negligible'.