Opinion Issued by the Accounting Standards Board
Income recognition / suspension on Lease & Finance Contracts overdue by 90 days

Brief facts of the enquiry:

ABC Financial Services Pakistan Limited (the Company) is primarily engaged in financing assets through finance leases or loan arrangements. The Company is licensed to carry out Investment Finance Services as a Non-Banking Finance Company (NBFC) under the Non-Banking Finance Companies (Establishment and Regulations) Rules, 2003.

The Company adopted IFRS 9 in 2019 and follows IFRS 9 ECL model for calculation and recording of allowances for potential lease and loan losses.

The applicable accounting framework of the Company comprises of IFRS Accounting Standards as adopted in Pakistan, Fourth Schedule to the Companies Act 2017, and provisions contained in and directives issued under NBFC regulations and rules made thereunder.

The Company has been following the criteria of not recognizing revenue on contracts that were past due by 90 days based on the Company's accounting policy and in accordance with Schedule X of Non-Banking Finance Companies and Notified Entities Regulations 2008 (NBFC Regulations).

IFRS 9 is applicable on NBFCs effective for reporting periods ended or after June 30, 2024 in view of S.R.O. 1827 (I) / 2022 dated September 29, 2022.

The enquiry relates to annual accounting period beginning on or after July 01, 2023.

The Company requested an opinion on income recognition based on time-based criteria i.e. the Company continues to suspend income recognition on overdue contracts (i.e. contracts where installments are overdue by 90 days) and in case of recovery of installments from such overdue contracts, the Company can release/ recognize the income portion on such installments that are actually collected from the customer.

Opinion:

The Board based on the enquired fact pattern, concluded that:

Sub-regulation (1) of Regulation 25 of NBFC regulations states that:

A Lending NBFC shall observe the criteria for classification of its assets and provisioning as provided in Schedule X: Provided that in case of loans of up to Rs. 100,000 that are not secured by any Tangible Security and having a duration of up to six months, provided by lending NBFCs engaged in Investment Finance Services, the classification criteria specified for Micro Finance portfolio in Schedule X shall apply. ***Notwithstanding anything contained in this sub-regulation, after adoption and implementation of IFRS 9, the requirements of IFRS 9 shall be applicable.*** *(Emphasis is ours)*

Schedule X of the NBFC Regulations outlines time-based criteria for provisioning and classifying financial assets, including provisions for income suspension.

As stipulated in clause 25(1) of the NBFC Regulations, the adoption and implementation of IFRS 9 supersede Schedule X. Consequently, the income suspension criteria within Schedule X are no longer applicable after applicability of IFRS 9 from July 1, 2023 in view of S.R.O. 1827 (I) / 2022 dated September 29, 2022.

Hence, on the applicability of IFRS 9 as stipulated in regulation 25(1), all requirements of IFRS 9 should be followed (including those relating to income recognition).

(Issued on January 25, 2024)

Disclaimer

The Board believes that the enquired matter, transaction or arrangement has been or will be made considering the legal, ethical and moral requirements. The comments and opinion are based on the facts and circumstances provided by the enquirer. The comments and opinion may change if the facts and the circumstances change. An opinion may also change due to subsequent change in law, pronouncements made by the Institute and other relevant changes. The Institute, its staff and the Board will have no liability in connection with such opinion and this opinion is not a ‘legal advice’.