Snapshot

by Capital Markets & Accounting Advisory Services

July 2024

MASB issues targeted improvements to financial instruments standards

What is the issue?

On 15 July 2024, the Malaysian Accounting Standards Board ("MASB") issued targeted amendments to MFRS 9 'Financial Instruments' and MFRS 7 'Financial Instruments: Disclosures' to:

(a) clarify the date of recognition and derecognition of some financial assets and liabilities, with a new exception for some financial liabilities settled through an electronic cash transfer system;

(b) clarify and add further guidance for assessing whether a financial asset meets the solely payments of principal and interest ("SPPI") criterion;

(c) add new disclosures for certain instruments with contractual terms that can change cash flows (such as some instruments with features linked to the achievement of environment, social and governance ("ESG") targets); and

(d) update the disclosures for equity instruments designated at fair value through other comprehensive income ("FVOCI").

The amendments in (b) are most relevant to financial institutions, but the amendments in (a), (c) and (d) are relevant to all entities.

What is the impact and for whom?

(a) Date of recognition and derecognition of financial assets and liabilities

The amendments clarify the date of recognition and derecognition of a financial asset or financial liability, as set out in the table below.

	Financial asset*	Financial liability
Date of recognition	the date the entity becomes party to the contractual provisions of the instrument	the date the entity becomes party to the contractual provisions of the instrument
Date of derecognition	the date the rights to cash flows expire or the asset is transferred	the settlement date (that is, the date the liability is extinguished or otherwise qualifies for derecognition)

** MFRS 9 provides an exception for regular way purchases or sales of financial assets that allows for recognition / derecognition using either trade date or settlement date accounting. That exception continues to apply and is not impacted by these amendments.*

However, the amendments provide an optional exception relating to the derecognition of a financial liability. Applying the exception, an entity is permitted to derecognise a financial liability at an earlier date if the cash transfer takes place through an electronic payment system and specific conditions are met.

The conditions for the exception are that the entity making the payment does not have:
- the practical ability to withdraw, stop or cancel the payment instruction;
- the practical ability to access the cash; or
- significant settlement risk.

This exception does not apply to other payment methods such as cheques, and must be elected on a system-by-system basis.

(b) Assessing whether a financial asset meets the SPPI criterion

The amendments cover three areas that impact the SPPI assessment for financial assets:

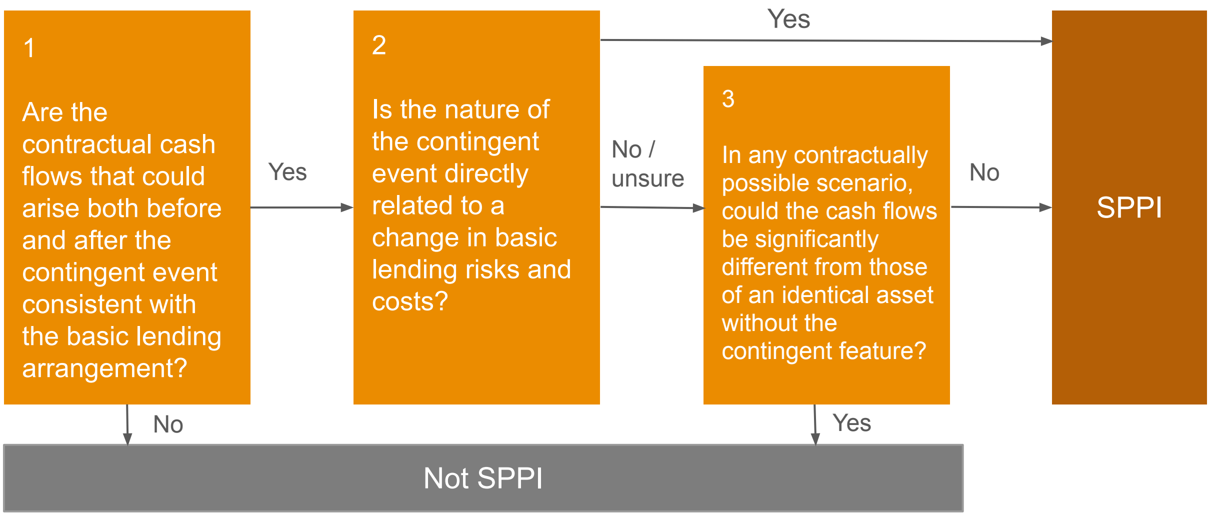
- contractual terms that can change cash flows based on contingent events (for example, interest rates linked to ESG targets);
- non-recourse features; and
- contractually-linked instruments.

What is the impact and for whom? (continued)

(b) assessing whether a financial asset meets the SPPI criterion (continued)

Contractual terms that can change the timing or amount of cash flows based on contingent events

Over the past few years, there has been an increase in lending products with interest rate adjustments that incentivise customers to meet specified ESG targets. The amendments provide additional guidance on the SPPI assessment for financial assets with contractual terms that can change the timing or amount of contractual cash flows (summarised in the flowchart below).



Non-recourse features

When assessing whether a financial asset meets the SPPI criterion, an entity considers the various features of the contract, including any 'non-recourse' features. The amendments clarify that a financial asset has non-recourse features if the holder's right to receive cash flows is contractually limited to the cash flows generated by specified assets. The presence of such non-recourse features does not necessarily preclude the financial asset from meeting the SPPI criterion, but the features do need to be carefully considered.

Contractually-linked instruments ("CLIs")

In some transactions, an issuer might prioritise payments using multiple CLIs that create concentrations of credit risk (known as 'tranches'). Identifying CLIs is important, because MFRS 9 has specific requirements for determining whether their cash flows meet the SPPI criterion.

The amendments clarify that a key element that distinguishes CLIs from other financial assets with non-recourse features is the waterfall payment structure that results in a disproportionate allocation of cash shortfalls between the tranches.

What is the impact and for whom? (continued)

(c) New disclosures for borrowers and lenders about contingent events and their potential impact on contractual cash flows

The amendments introduce new disclosure requirements for instruments with contractual terms that can change cash flows because of events that are not directly related to changes in basic lending risks (such as certain loans subject to ESG targets).

These new requirements are applicable to financial assets measured at FVOCI as well as financial assets and liabilities measured at amortised cost, and include:

- a qualitative description of the nature of the contingent event;
- quantitative information about the possible changes to contractual cash flows — for example, the range of possible changes; and
- the gross carrying amount of financial assets and amortised cost of financial liabilities subject to these contractual terms.

(d) disclosures for FVOCI equity instruments

The amendments also change some of the disclosures for equity instruments designated at FVOCI.

When does it apply?

The amendments to MFRS 9 and MFRS 7 will be effective for annual reporting periods beginning on or after 1 January 2026, with early application permitted. An entity can elect to early apply only the amendments discussed in (b) and (c) above together, without yet applying the amendments discussed in (a) and (d).

When an entity first applies the amendments, it is not required to restate comparative information, and is only permitted to do so if possible without the use of hindsight.

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