

**INTERPRETATIONS FOR CIRCULAR NO. 07 OF 2019 ON
CONCESSIONS GRANTED TO TOURISM INDUSTRY**

The following interpretations are issued in relation the Circular No. 07 of 2019 dated 08 May 2019 on Concessions Granted to Tourism Industry.

1. Individuals

Individuals include persons providing services to tourism sector and permanent employees of entities who provide services to tourism sector.

2. Registration

- (i) Persons and entities providing services to tourism sector shall be registered with any of the following Institutions, as at 18.04.2019.
 - (a) Sri Lanka Tourism Development Authority
 - (b) Agencies under Sri Lanka Tourism Development Authority
 - i) Sri Lanka Tourism Promotion Bureau
 - ii) Sri Lanka Tourism Convention Bureau
 - iii) Sri Lanka Institute of Tourism and Hotel Management
 - (c) The Hotels Association of Sri Lanka
- (ii) Persons and entities who have not registered with any of the Institutions referred in 2(i) above as at 18.04.2019, shall have at least registered their businesses/ services with the local government authorities such as Pradeshya Sabha, Urban Council or Municipal Council as at 18.04.2019 and in order to avail the moratorium, such persons and entities shall now be required to register with the relevant institution/s referred in 2(i) above.

3. Granting of moratorium

- (i) Individuals or entities who wish to avail the moratorium shall make a request to the relevant licensed bank seeking such moratorium.
- (ii) Licensed banks shall evaluate such request individually, including the requirement stipulated in para 2 above, in order to assess the eligibility.
- (iii) The moratorium shall be granted for any performing credit facilities (both capital and interest) as at 18.04.2019 of such individuals or entities.

- (iv) Licensed banks shall report all individuals or entities who have requested to avail the moratorium, as per the reporting format prescribed in the Circular No. 07 of 2019 on Concessions Granted to Tourism Industry.

4. Accounting Treatment under SLFRS 9

- (i) Licensed banks shall comply with the instructions provided by the Chartered Accountants of Sri Lanka in relation to recognitions of interest income and accounting for financial assets (Annex I).



From the Office of the President

13th May 2019

Mr. H. A. Karunaratne,
Deputy Governor,
Central Bank of Sri Lanka,
30, Janadhipathi Mawatha,
Colombo 01.

Dear Mr. Karunaratne,

Re: Concessions to the Tourism Industry

We thank the Central Bank of Sri Lanka for referring to us the proposed concessions to the tourism industry announced by the government requesting to clarify the accounting treatment as per SLFRS 9 *Financial Instruments*.

Accordingly, with reference to your letter dated 07th May 2019 under the above heading, please find below the clarification you sought as per the recommendation made at the CA Sri Lanka Financial Reporting Standards Implementation & Interpretation Task Force meeting:

Issue 1: Recognition of interest income during the moratorium period*Paragraph 5.4.1 of SLFRS 9:*

Interest revenue shall be calculated by using the effective interest method. This shall be calculated by applying the effective interest rate to the gross carrying amount of a financial asset except for:

- (a) *purchased or originated credit-impaired financial assets*. For those financial assets, the entity shall apply the *credit-adjusted effective interest rate* to the *amortised cost* of the financial asset from initial recognition.
- (b) financial assets that are not purchased or originated credit-impaired financial assets but subsequently have become *credit-impaired financial assets*. For those financial assets, the entity shall apply the effective interest rate to the amortised cost of the financial asset in subsequent reporting periods.

Paragraph 5.4.2 of SLFRS 9:

An entity that, in a reporting period, calculates interest revenue by applying the effective interest method to the amortised cost of a financial asset in accordance with paragraph 5.4.1(b), shall, in subsequent reporting periods, calculate the interest revenue by applying the effective interest rate to the gross carrying amount if the credit risk on the financial instrument improves so that the financial asset is no longer credit-impaired and the improvement can be related objectively to an event occurring after the requirements in paragraph 5.4.1(b) were applied (such as an improvement in the borrower's credit rating).

Accordingly, interest income can be recognised by the banks by using the Effective Interest Rate (EIR) applied to the gross carrying amount or the net carrying amount considering the stage into which that loan belongs to at the time of the modification.

Issue 2: Consideration of the rescheduled loans (terms loans) under the same category for classification and provisioning purposes

Based on the given information, "banks are requested to convert the capital and interest falling due during the moratorium period into a loan". Accordingly, there would be a modification of the financial assets where the banks would be required to re-estimate the cash flows attached to the financial assets.

In these circumstances the banks may need to assess whether the financial asset need to be derecognized under SLFRS 3.2.3(a) which states that an entity shall derecognize a financial asset when and only when: (a) the contractual rights to the cash flows from the financial asset expire. On that basis, de-recognition of a financial asset on the revised terms would occur where the moratorium results in substantial modification to the original cash flows which could be seen as an expiry of those cash flows.

As per B5.5.25 of SLFRS 9, in some circumstances, the renegotiation or modification of the contractual cash flows of a financial asset can lead to the derecognition of the existing financial asset in accordance with this Standard. When the modification of a financial asset results in the derecognition of the existing financial asset and the subsequent recognition of the modified financial asset, the modified asset is considered a 'new' financial asset for the purposes of this Standard.

As per B5.5.26 Accordingly, the date of the modification shall be treated as the date of initial recognition of that financial asset when applying the impairment requirements to the modified financial asset. This typically means measuring the loss allowance at an amount equal to 12-month expected credit losses until the requirements for the recognition of lifetime expected credit losses in paragraph 5.5.3 are met. However, in some circumstances following a modification that results in derecognition of the original financial asset, there may be evidence that the modified financial asset is credit-impaired at initial recognition, and thus, the financial asset should be recognised as an originated credit-impaired financial asset. This might occur, for example, in a situation in which there was a substantial modification of a distressed asset that resulted in the derecognition of the original financial asset. In such a case, it may be possible for the modification to result in a new financial asset which is credit-impaired at initial recognition.

Accordingly, the holder of the financial asset should perform a quantitative and qualitative evaluation of whether the modification is substantial.

As per SLFRS 9, para 5.4.3, when the contractual cash flows of a financial asset are renegotiated or otherwise modified and the renegotiation or modification does not result in the derecognition of that financial asset in accordance with this Standard, an entity shall recalculate the gross carrying amount of the financial asset and shall recognise a modification gain or loss in profit or loss. The gross carrying amount of the financial asset shall be recalculated as the present value of the renegotiated or modified contractual cash flows that are discounted at the financial asset's original effective interest rate

Paragraph B5.5.26 of SLFRS 9:

Accordingly the date of the modification shall be treated as the date of initial recognition of that financial asset when applying the impairment requirements to the modified financial asset. This typically means measuring the loss allowance at an amount equal to 12-month expected credit losses until the requirements for the recognition of lifetime expected credit losses in paragraph 5.5.3 are met.

Paragraph B5.5.27 of SLFRS 9:

If the contractual cash flows on a financial asset have been renegotiated or otherwise modified, but the financial asset is not derecognised, that financial asset is not automatically considered to have lower credit risk. **An entity shall assess whether there has been a significant increase in credit risk since initial recognition on the basis of all reasonable and supportable information that is available without undue cost or effort.** This includes historical and forward-looking information and an assessment of the credit risk over the expected life of the financial asset, which includes information about the circumstances that led to the modification. Evidence that the criteria for the recognition of lifetime expected credit losses are no longer met may include a history of up-to-date and timely payment performance against the modified contractual terms. Typically, a customer would need to demonstrate consistently good payment behaviour over a period of time before the credit risk is considered to have decreased.

Accordingly, the modified loan referred to above in order to grant concessions to the tourism sector, should be classified in an appropriate stage considering the bank's assessment on whether there has been a significant increase in credit risk since initial recognition on the basis of all reasonable and supportable information, at the time of modification and in subsequent reporting periods. Otherwise, the modified loan result in the derecognition of the financial asset, guidance given in paragraph B5.5.25 and B.5.5.26 shall be applied.

Issue 3: What should be the disclosure requirements in relation to the above?

General disclosures in terms of SLFRS 7 Financial Instruments: Disclosures need to be followed by the banks in the financial statements. In addition to the general disclosures required, in relation to impairment requirements of financial assets which have had modifications to their contractual cash flows need to provide disclosures required by SLFRS 7 (35F(f)), (35I)(b) and (35J).

This explanation is provided purely based on the limited facts and information provided by you and as such the Institute of Chartered Accountants of Sri Lanka takes no responsibility if the explanation would have been different had more information been available. Further, the application of the Sri Lanka Accounting Standards requires exercise of judgement. Therefore, the ultimate responsibility for the recognition, measurement, presentation and disclosures of any transaction rests with the preparers of the financial statements. In providing this clarification, we have exercised due care and diligence and therefore we believe that the clarification given is appropriate. If you require further clarifications on the issue, we advise you to seek professional advice.

Thank you

Yours sincerely
**THE INSTITUTE OF CHARTERED ACCOUNTANTS
OF SRI LANKA**



Jagath Perera
PRESIDENT