AS 30, 31 & 32 review – Financial Liabilities

Contents:

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Particulars

Financial Liability: (Para 7 AS 31)

- a contractual obligation
- to deliver cash or another financial asset to another entity; or
- to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the entity; or

Eg 1: Company has purchased raw material from Techno & Co. Payment due on 25th Feb 2011. On reporting date 31st Dec 2010, 'Techno & Co. a/c' is a FL – obligation to deliver cash

Eg 2: Company A writes a put option of ` 150 for 2 months. A is obliged to purchase shares at ` 150 even if the market prices are lower on the settlement date if the counter party exercises the option – exchange of FL with potential unfavourable conditions.

a. a contract that will or may be settled in the entity's own equity instruments and is
   - a non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or
   - a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include instruments that are themselves contracts for.

Eg 3: Company sold goods worth ` 2 lacs and agreed to issue equivalent value own equity shares based on the rates prevailing on the settlement date – non derivative

Eg 4: Company issues an option to sell 1 lac own equity shares. Share price will be determined as follows:

Share Price = ` 0 to 10 → 10 shares at ` 1 each
Share Price = ` 11 to 20 → 10 shares at ` 1.5 each

Classification of Financial Liabilities

a. Held at fair value through P&L

   Includes FL held for trading and those FL which the company designates under this category.

   Held for trading includes:

   - Derivatives other than Hedge derivatives
   - Liabilities incurred with an intention to repurchase in a short span of time
   - FL from a portfolio which shows recent trend of short term profit making due to price fluctuations

   Note 1: One should note that the above list is a not exhaustive. FL which is incurred for short span with an intention to trade falls under this category.

   Apart from 'Held for Trading' all those FL held at fair value includes those which the company classifies under this category. However, the standard further states that a company can voluntarily classify liabilities under this category only when:

   - Such classification results in a more relevant way of presenting information. Refer para A15 from AS 30

   Note 2: Only in certain limited cases a company can voluntarily designate a FL under held at fair value category. The conditions mentioned in para A15-A18 should be satisfied.

   Disclosure: Description as to how this classification is consistent with company's investment strategy.

b. Other financial liabilities held at amortized cost

   These are liabilities which do not fall under HAFV. Any change in their fair value is not recognised.

   Amortised cost is calculated as under:

Initially recognised amount	xx
Less: principal repayment	(xx)
Add/less: difference between initial amount recognised and maturity amount using effective interest method	xx / (xx)
Less: uncollectibility	(xx)
Amortised cost	xx

Loan commitments which are under the scope of AS 30:

a. Loans which the company designates as held at fair value. In this case the company has a past trend of selling the asset resulting from loan. Such loans are grouped under HAFV to avoid mismatch between accounting for loan and related asset.
b. Those which can be settled net in cash (regarded as derivatives) except for repayment in installment based on progress payment received.
c. Loan commitments at below market rate

   Loans which are not under this standard should be accounted as per AS 29. However, even in case of such loans derecognition rules of AS 30 will be applied.

Measurement:

a. Initially
   - Should be measured at fair value through P&L.
   - Short term payables for which discounting is immaterial need not be discounted. It will be held at amount payable.
   - Guarantees should be measured as per AS 29 i.e. best estimate and without discounting.
b. Subsequently
   - Liabilities HAFV should be valued at fair value and the changes should be taken to P&L.
   - Short term payables which are not discounted are held at initially recognised value.
   - Financial guarantee and loan below market interest rate should be held at higher of:
     - Value as per AS 29
     - Amortised cost. (refer Appendix A12)
   - Other financial liabilities should be held at amortised cost.

De-recognition:

- Financial Liability: A financial liability is de-recognised when it is extinguished. Extinguished means discharged, expired, cancelled or modification of same debt (whether in part or whole) for new terms and conditions.
  Eg: cash paid to creditors, shares issued against liability, part settlement by court, loan re-schedulement, etc.
- If part of the debt is modified or paid off then only that portion of the debt should be extinguished. Difference between carrying amount and consideration paid in cash or kind should be recognised in Profit & Loss statement.
- When only part of the liability is repurchased, carrying amount of both parts i.e. portion which is repurchased and which is de-recognised is bifurcated based on the fair value of each part. Difference between carrying amount of extinguished part and consideration received (whether in cash or in kind) is taken to profit & loss statement.
  Eg 5:

Financial Liability (repay after 5 yrs)	1500
Initially booked at fair value (10% discount rate)	931
Repaid in 1st year	300
Fair value of repayment	186
Deduct 186 from 931 and not 300	

- When terms and conditions of loan are modified,
  1. Present value of the cash flows under new terms including additional fees paid or received (using original effective interest rate)
  2. Present value of remaining cash flows of original liability
  3. If difference between (1) & (2) is 10% or more then, original liability should be de-recognised and liability with modified terms should be recognised as a new FL.

Following items do not fall under financial liability category since they do not give rise to an obligation to pay cash or financial asset:

Sr. No.	Particulars
1.	Advance tax paid
2.	TDS certificates booked
3.	Deposit with octroi authorities
4.	Balance in PLA
5.	Deposit / advance with sales tax authorities
6.	Other Liabilities which are not contractual
7.	Deferred revenue expenditure
8.	Advance from customers (contractual but in the course of regular business. Will be settled by supply of units and not in cash)

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