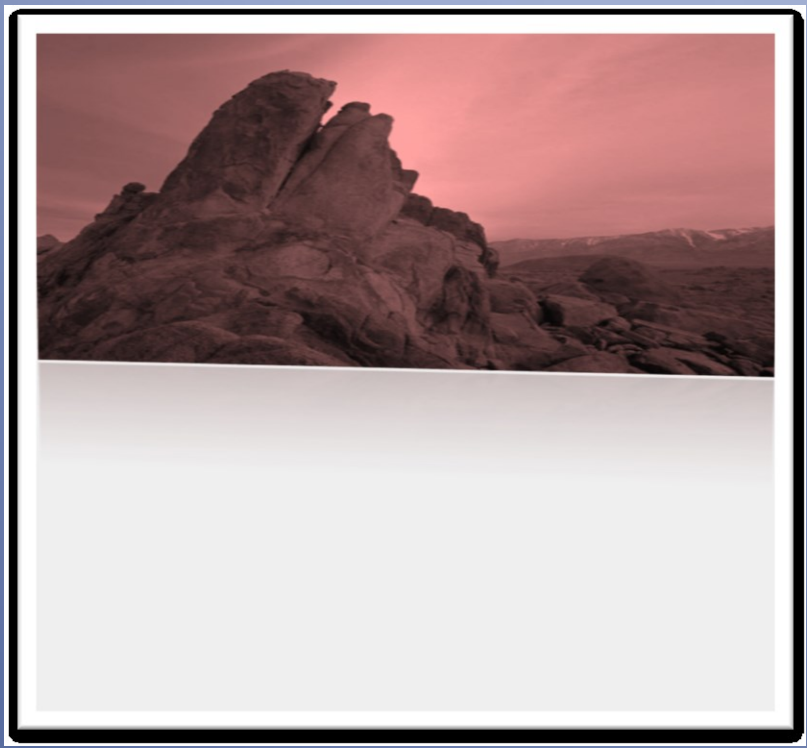

Financial Instruments

AS 30 Recognition & Measurements

As 31 Presentation

As 32 Disclosures

For CA Final

Compiled by Ankit Shah

As-30 Recognition & Measurement
As-31 Presentation
As-32 Disclosures

Meaning of Financial Instrument (FI):

FI is any contract that gives rises to a Financial Asset to one entity and Financial Liability or equity instrument of another entity.

Meaning of Financial Assets (FAs):

FAs are

	ITEMS	EXAMPLES
1.	Cash	• Cash in hand • Cash at Bank • Cash Equivalent in form of Short Term Securities. **Notes: Gold is a cash equivalent but is no a FAs since gold is a commodity.**
2.	Equity Instrument of another entity	Investment in Equity share of another entity.
3.	Contractual Right of receiving Cash (Non-Derivative)	• Debtors • Bills Receivables • Loans & Advances • Investments in Bonds & Debentures • Investments in Preference shares
4.	Contractual Right of Receiving FAs other Cash	• Repurchase Agreement • Securitisation Contract
5.	Contract of exchanging FAs with FL	Exchanging or raising a loan by giving away by old loan
6.	Contract that shall be settled in equity shares of another but is not a derivative contract.	• Issuing Debentures against Equity share issued by another entity. • Selling Fixed Assets or Inventory and receiving payment in form of equity shares of another entity.
7. (a)	Derivative Contract settled in cash	F & O which are cash settled including F & O on commodities which are cash settled.
7. (b)	Derivative Contract settled by delivery in FAs.	F & O to be Settled by Delivery of equity shares or any other FAs. **Notes: F&O on commodities to be settled by delivery of commodity is not a FAs**

Meaning of Financial Liabilities (FLs):

FLs are

	ITEMS	EXAMPLES
1.	Contractual obligation to deliver cash or cash equivalent to another entity	• Creditors • Bills payable • Loan raised • Issue of Bond & Debentures • Issue of Preference shares not classified equity under AS -31.
2.	Contractual Obligation to deliver FA other Cash	• Repurchased Agreement • Securitisation Contracts • Advance Received for issuing Bonds or debentures
3.	Contractual Obligation of Exchanging FAs against FLs	Raising a new loan and repay an existing Loan
4.	Contract that shall be settled in equity shares against delivery of FAs other than Cash	Issuing Equity Shares to settled consideration for Debentures issued by other entity. **Note: Equity Shares issued for Fixed Assets or Inventory purchased is not FLs. Since, this is contract settled by delivery of inventory or Fixed Assets which is not a FAs. Equity Shares are Classified as "Equity Instruments".**
5. (a)	Obligation under derivate contract to be settled by delivery of cash	Same as 7. (a) of FAs.
5. (b)	Obligation under derivate contract to be settled by delivery of FAs other than cash	Same as 7. (b) of FAs.

Followings are not FAS or FLs:

1. Gold (Since it is a commodity)
2. Non-Monetary or Physical Assets. (Fixed Assets, Intangible Assets, Commodities and Inventories)
3. Insurance Contracts.
4. Derivate Contract to be settled by delivery of Commodity.
5. Prepaid Expenditure (The Benefit shall be enjoyed inform of service and not FA)
6. Deferred Tax Assets, Deferred Tax Liabilities and provision for taxation. (Since there is no contract with Government)
7. Provision for expected warranty cost or payment of damages as per court direction.

Followings are FAS or FLs but not covered by AS 30, 31, 32 as covered by another AS:

1. Leases (AS 19)
2. Investments in Subsidiaries (AS 21)
3. Investments in Associates (AS 23)
4. Investments in joint Ventures (AS 27)

However, any disclosure provided in AS 32 which is in addition to the above mention Accounting Standards that additional disclosure demanded by AS 32 should be provided.

AS 21, 23 & 27 provided certain exceptions where AS 21, 23 & 27 shall not be applicable, in such situation AS 30, 31 & 32 shall be become applicable.

Classification of FAs:

Classification of FAs should be carried out as on the date of acquisition or origination. FAs shall be classified in to any one of the following categories:

1. Fair Value Through Profit & Loss (FVTPL)
2. Held To Maturity (HTM)
3. Loans & Receivable (LR)
4. Available For Sales (AFS)

1. FVTPL:

1) These are FAs **held for Trading** or are **designated** as FVTPL at the **inception of classification**.
2) These are FAs acquired with a motive of selling them in near future.
3) These are FAs frequently purchased and sold and there is evidence of short term profit taking.
4) All derivate contracts (other than for hedging) are classified under this category.

2. HTM:

1) These are non-derivate FAs with Fixed or determinable maturity.
2) The enterprise should have an intention and ability to hold these FAs upto their maturity.
3) This category excluded the followings:
   a) Loan given by enterprise
   b) Investments in equity shares
   c) Investments in irredeemable bonds and irredeemable preference shares
   d) Investments in callable and putable redeemable bonds unless derivate can be separate out.
   e) Investment in security where maturity is fixed but the amount to be received is not determinable.

3. LR:

1) These are non-derivate FAs with Fixed or determinable maturity and not quoted in any active market.
2) They typically arise when entity provides money, goods or services directly to a debtor with no intention of trading in receivable.

4. AFS

1) This category comparies of those FAs which could not be classified in to any one of the above 3 category.
2) This category specifically included followings:
   a) Investment in Equity Shares other than trading
   b) Investment in irredeemable bonds or irredeemable preference shares other than trading.
   c) Investment in unquoted securities.
   d) Investments in redeemable securities intended to be sold before maturity.

Reclassification of FAs:

Original Classification	New Classification			
	FVTPL	HTM	LR	AFS
FVTPL	N.A.	Disallowed	Disallowed	Disallowed
HTM	Disallowed	N.A.	Disallowed	Allowed[1]
LR	Allowed	Disallowed	N.A.	Disallowed
AFS	Allowed	Allowed	Disallowed	N.A.

[1] Tainting implications

Measurement of FAs:

Category	Initial Measurement	Subsequent Measurement	Treatment of	
			Income Earned	Gain or loss on sale/ De-recognition
FVTPL	• Initially recorded at Fair value on acquisition date • Initially fair is the acquisition price • Directly attributable transaction cost shall be debited to P & L A/c	Change in fair value between two reporting date, whether gain or loss, shall be recognized in P & L A/c	Recognized in P & L A/c	Recognized in P & L A/c
HTM	• Initially recorded at fair value on Acquisition Date • Initially fair value is acquisition price + Directly attributable transaction cost	Accounted over its maturity by adopting amortized cost method applying Effective Interest Rate (i.e. IRR/YTM)	Recognized in P & L A/c	If any then Recognized in P & L A/c
LR For a period				
not more than 1 year	Initially recorded at invoice value	Continue to be reported at its invoice value	Recognized in P & L A/c	Recognized in P & L A/c
More than 1 year	Same as HTM	Same as HTM	Same as HTM	Same as HTM
AFS	• Initially recorded at fair value on acquisition date. • Initial fair value is acquisition attributable transaction cost	Change in Fair value between reporting date, whether gain or loss, shall be transferred to investment revaluation reserve* or fair value reserve	Recognized in P & L A/c	Recognized in P & L A/c Cumulative gain or loss recognized in IRR* should be transferred to P&L A/c take a proportionated transferred if sold partially
FAs who fair value cannot be determined (e.g. Invt. In unquoted securities)	Same as AFS	Continued to be reported at initial recorded cost	Recognized in P & L A/c	Recognized in P & L A/c

Impairment of FAs:

Following are the indicators for impairment.

1. Significant Financial Difficulties of their issuer.
2. Default on interest or principal
3. Loss of active market.
4. High probability of bankruptcy of issuer or debtors.
5. Granting of concession to a borrowed which would not be offer under business conditions.

It should be noted that dis-listed or reduction in credit rating are not indication of impairment.

Category	Formula to compute Impair Loss	Treatment of IL	Treatment of Reversal IL
FVTPL	Impairment loss provision is not required	N.A.	N.A.
HTM & Long term LR	Amortized cost on date of Impairment Less: PV of* future expected benefits * Discounted rate issued is effective interest rate (IRR) used for amortized cost schedule	Debited to P &L A/c	Credited to P &L A/c
Short Term LR	Carrying Amount – Undiscounted future Excepted Cash flow	Debited to P &L A/c	Credited to P &L A/c
FAs carried at cost	Carrying Amount – PV* of future Excepted Benefit * Discounted Rate to be used is current market Interest Rate	Debited to P &L A/c	Not permitted
AFS	FV on Preceding Reporting date Less: FV on date of Impairment	Debited to P &L A/c	• **Debt Instrument** Credited to P & L A/c • **Other Instruments** Credited to Investment Revaluation Reserve

Disclosure for FAs (AS 32)

1. Cateria uses for classification of FAs in to different Categories.
2. Carrying amount of each category of FAs.
3. Income earned from different FAs.
4. Gain or Loss on sale or de-recognition of FAs.
5. Any Directly attributable transaction cost recognized in P & L A/c
6. Cumulative gain or loss recognized in Profit & Loss from investment revaluation reserve or fair value reserve.
7. Whether any reclassification has been carried out during the period and if yes then disclosure the amount reclassification, original classification, new classification and reason for reclassification.
8. Impairment Loss provided or reserved.

Classification for FLs

AS 30 Classified FLs in to following two categories

1. Fair Value Though Profit & Loss
2. Other FLs.

1. FVTPL

1) These are FLs arising out of Trading or are classified as FVTPL from inception.
2) These FLs are created due to short selling with motive of purchasing in near future.
3) These are FLs frequently short sold and purchased and there is evidence of short term profit taking.
4) This category specifically included FLs under derivate contact except for hedging.

2. Other FLs

- Any FL not classified as FVTPL is put under this category.
- This category is further sub-divided in to:
  1) Long term FLs such as Loan Raised, Issued Bonds, Debentures or preference shares not classified as equity instruments.
  2) Short term FLs such as Creditors, Bills payable, Bank Overdraft, etc.

Measurement of FLs:

Category	Initial Measurement	Subsequent Measurement	Treatment of Expenses	Treatment of Gain or loss on De-recognition
FVTPL	• Initially recorded at Fair value on acquisition date • Initially fair is the acquisition price or issue price • Directly attributable transaction cost shall be debited to P & L A/c	Change in fair value between two reporting date, whether gain or loss, shall be recognized in P & L A/c	Recognized in P & L A/c	Recognized in P & L A/c
Other FLs				
Long Term	Initially recorded at Fair value which is the acquisition or issue price net off direct attributable transaction cost	Account over its maturity cost. Method applying Effect Interest Rate (IRR)	Recognized in P & L A/c	If any then Recognized in P & L A/c
Short term	Recorded at its invoice value	Continue to be reported at invoice value	Recognized in P & L A/c	If any then Recognized in P & L A/c

Disclosure for FLs (AS 32)

1. Cateria uses for classification of FLs in to different Categories.
2. Carrying amount of each category of FLs.
3. Changes in Fair value recognized in Profit & Loss
4. Net Gain or Loss for each category of FLs on de-recognition..
5. Interest Expenses/ Dividend Expenses recognized in P & L A/c
6. Changes in market conditions affecting of risk of FLs.
7. If there is any default then the Carrying Amount of FLs in default should be disclosure. If there is any reconstruction / renegotiation then new terms should be disclosures.

Debt-Equity Classification & Presentation as per AS 31

- An Equity Instrument is any contract that gives to its holder a residual interest in the entity after deducting all liabilities from the assets.
- The primary factor distinguishing debt & Equity instrument is the existing of contractual obligation of the issuer to make payment of interest/Dividend/principal amount.
- Any Instrument that does not give rises to any contractual obligation to the issuer is an equity instrument.

1. Classification of Preference Shares

(A) Preference Shares that provide for redemption on a specific day or redemption at option of the holder is the Financial Liability.

(B) Preference shares that provide for payment of dividend, whether redeemable or irredeemable are classified as Financial Liability.

(C) Preference Shares that pays dividend and provides for redemption at the option of issuer is an Equity Instrument.

Notes:
(a)
- If Preference Share are classified as FLs, then preference dividend should be treated an expenses and not as item of appropriation.
- Redeemable preference shares shall be accounted over its maturity following amortized cost method applying effective interest rate. (IRR)

- Irredeemable preference shares shall be listed on Stock Exchange and hence shall be accounted as FVTPL FLs.

(b)

- Preference Dividend on Preference share classified as equity and Equity Dividend on Equity Shares paid/ Declared by the entity should be reported in B/S (along with its tax implication) as the deduction from Reserves & Surplus.
- Provision for proposed dividend should not be recognized since there is no contractual obligation.
- Directly attributable transaction cost related to equity instrument should be reported in B/S as a deduction from paid up share capital or security premium or any other similar reserve.

2. Classification of Shares warrants and options:

(A) Shares Warrants or options to be settled by payment of cash or the option of the holders are classified as FLs.

(B) Shares warrants or options to be settled at the options of the issuer by the issuing a Fixed No. of equity shares is an Equity Instruments.

3. Classification to be contract settled by equity shares or cash on the basis of outcome of future uncertain event not wholly within control of entity:

This Contract represents contingent Liability to be disclosure in notes to account as per As 29

4. Classification of Compound Financial Instrument:

- Not all Financial Instrument are either debt or equity.
- A compound Financial Instrument is the one that has certain elements of debts and certain elements of equity in a single contract.
- For e.g. Convertible bond.
- A compound Financial Instrument should be split in to its debt & equity component and both the component should be accounted for separately.

Accounting of Derivatives (other than for Hedging)

(A) Accounting for Futures

1. Fair value of forward/future contract shall be nil on the date of entering in to contract. This is on account of fact that a futures contracts concerned a right as well as an obligation on the day on which such contract enter in value in the right (FAs) and value of obligation (FLs) are equal. Hence no accounting entry is required.
2. Initial margin paid is in nature of deposit

   Initial Margin A/c Dr.

   To Bank A/c
3. If MTM Margin are payable

   MTM Margin A/c Dr.

   To Bank/ Initial Margin A/c

   If MTM margins are receivable, then

   Bank/ Initial Margin A/c Dr.

   To MTM Margin A/c
4. Futures give rise to FAs / FLs which are compulsorily classified as FVTPL. Change in fair value between two reporting days, whether gain or loss, should be recognised in profit & Loss.

   If there is fair value gain then

   Forward/futures A/c Dr.

   To Profit & Loss A/c

   If there is fair value Loss then

   Profit & Loss A/c Dr.

   To Forward/futures A/c
5. Accounting on Settlement

If Net is settled in cash

Cash / Bank A/c Dr.

To Forward/futures A/c

Or

Forward/futures A/c Dr.

To Cash / Bank A/c

If Net is settled by delivery

Equity Share A/c Dr.

To Forward/futures Contract A/c

Or

Forward/futures Contract A/c Dr.

To Equity Share A/c

(B) Accounting for Options

1.

- Options premium paid for buying options gives rises to rights, which is FAs. This is accounted as:

  Options A/c Dr.

  To Bank A/c

- Options Premium received for selling an options gives rises to an obligation which is a FLs. This is accounted as:

  Bank A/c Dr.

  To Options A/c

2.

- FAs/FLs of options is compulsory classified as FVTPL change in Fair value between two reporting date, whether gain or loss, should be recognized in Profit & Loss A/c.
- Fair value gain or loss on settlement date shall be computed comparing options premium rate if options is square up or by comparing sport price and strike price if option is exercise.

  If there is fair value gain then

  Option A/c Dr.

  To Profit & Loss A/c

  If there is fair value Loss then

  Profit & Loss A/c Dr.

  To Option A/c

3. Accounting on Settlement date:

   If Net is settled in cash

   Cash / Bank A/c Dr.

   To Option A/c

   Or

   Option A/c Dr.

   To Cash / Bank A/c

   If Net is settled by delivery

   Equity Share A/c Dr.

   To Option A/c

   Or

   Option A/c Dr.

   To Equity Share A/c

Embedded Derivatives

- An Embedded Derivative is a component of hybrid instrument, which also include a non-derivative host contract.
- An Embedded Derivative should be separated form host contract if all of the following 3 conditions are fulfilled:
  1. Host Contract is not classified as FVTPL.
  2. Contract gives rise to free standing derivative (i.e. derivative has an identity its own)

AND

3. Economic Characteristic and risk of derivative are not closely related to (i.e. significant different) economic characteristic & risk of the host contract.

- Derivative once separate out is compulsory is classified as FVTPL.
- After Separation Hot contract shall be classified as HTM/ LR / AFS on the basis of its indepently features.

Hedge Accounting

Hedge is the risk management tool aiming to reduce the impact of future potential loss or cost.

Composition of hedge Accounting:

1. Hedge document should be prepared showing the following details:
   (a) Hedge objective
   (b) Risk being hedged
   (c) Hedging instrument used
   (d) Hedge item
2. Fair value changes between two reporting date for the hedge instrument should be recognized in hedge reserve account.
3. Once the hedge objective has been met, subsequent fair value change should be recognized in Profit & Loss A/c.