AS-30,31,32-Financial Instruments

AS-30	AS-31	AS-32
Recognition & Measurement	Presentation	Disclosure

Introduction

Recommendatory in nature for an initial period of two years. This Accounting Standard will become mandatory in respect of accounting periods commencing on or **after 1-4-2011** for all commercial, industrial and business entities *except to a Small and Medium-sized Entity (SME), as defined below*:

(i) Whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India;

(ii) Is not a bank (including co-operative bank), financial institution or any entity carrying on insurance business;

Hyundai Motors India Ltd. **Samsung Electronics India Ltd.**

(iii) Its turnover (excluding other income) does not exceed rupees 50 crore in the immediately preceding accounting year;

(iv) It does not have borrowings (including public deposits) in *excess of rupees ten crore* at any time during the immediately preceding accounting year; and

(v) Is not a holding or subsidiary entity of an entity which is *not a small and medium-sized entity*.

Objective

AS-30

- To establish the principles for recognising and measuring
- Financial assets,
- Financial liabilities and
- Some contracts to buy or sell non-financial items.

AS-31

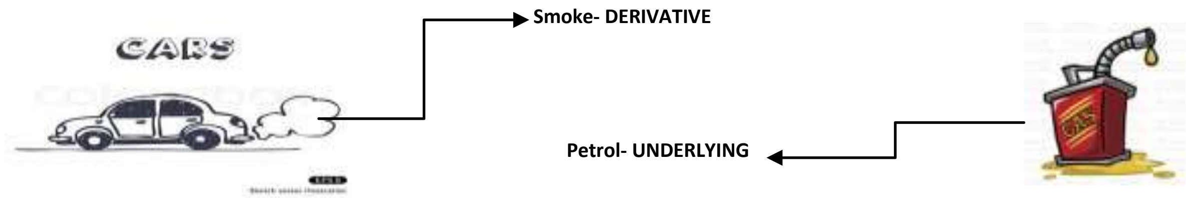
- to establish principles for presenting financial instruments as liabilities or equity and for offsetting financial assets and financial liabilities. It applies to the classification of financial instruments, from the prespective of issuer, into financial assets, liabilities and equity instruments; the classification of related interest, dividends, losses and gains; and the circumstances in which financial assets and financial liabilities should be offset.

AS-32

- to require entities to provide disclosures in their financial statements that enable users to evaluate:
- The significance of financial instruments for the entity's financial position and performance; and
- The nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the reporting date, and how the entity manages those risks.

Definitions

Derivatives



A concept usually used in Chemistry and Maths which changes its function due to change in inputs

Financial instrument or other contract within the scope of this Standard with all three of the following characteristics

- Its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract (sometimes called the 'underlying');
- It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors
- It is settled at a future date

Underlying

An underlying is a variable that, along with *either a notional amount or a payment provision,* determines the settlement amount of a derivative.

Examples of underlyings include:

A security price or security price index**;**

A commodity price or commodity price index;

An interest rate or interest rate index;

A credit rating or credit index;

A foreign exchange rate or foreign exchange rate index;

An insurance index or catastrophe loss index;

A climatic or geological condition (eg temperature, earthquake severity, or rainfall), another physical variable, or a related index; or

Another variable (eg volume of sales).

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

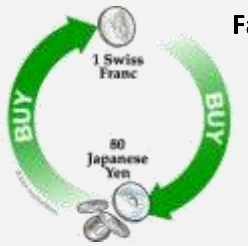
Definitions relating to Recognition and Measurement

Pankaj udas song lyrics "Hui Mehngi bahut hi sharab ke thodi thodi piya kro. Piyo lekin rakho hisab ke thodi thodi piya kro"

The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at *initial recognition minus principal repayments*, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, and minus any reduction (directly or through the use of an allowance account) for impairment or uncollectibility.
The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that *exactly discounts* estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.

De-recognition is the removal of a previously recognised financial asset or financial liability from an entity's balance sheet.

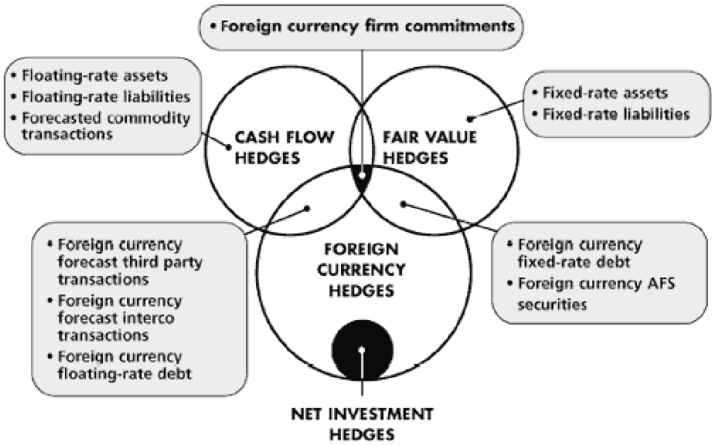


Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Definitions Relating to Hedge Accounting

A hedging instrument is

(a) a designated derivative or



(b) for a hedge of the risk of changes in foreign currency exchange rates only, a designated non-derivative financial asset or non-derivative financial liability whose fair value or cash flows are expected to offset changes in the fair value or cash flows of a designated hedged item

A hedged item is an asset, liability, firm commitment, highly probable forecast transaction or net investment in a foreign operation that

exposes the entity to risk of changes in fair value or future cash flows

is designated as being hedged

Hedge effectiveness of the hedged item

is the degree to which

changes in the fair value or cash flows

that are attributable to a hedged risk

are offset by

changes in the fair value or cash flows

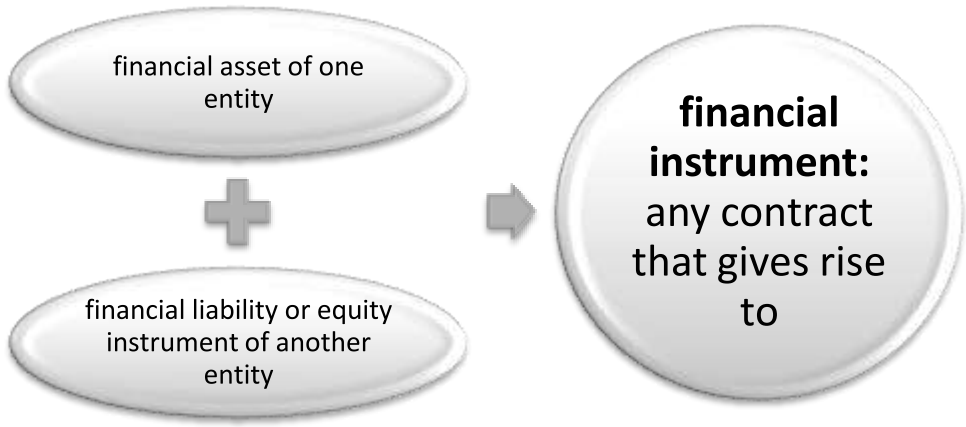
of the hedging instrument

A firm commitment is a binding agreement for the exchange of a specified quantity of resources at a specified price on a specified future date or dates.

A forecast transaction is an uncommitted but anticipated future transaction.

Functional currency is the currency of the primary economic environment in which the entity operates.

Definitions under AS31



Financial Assets are:

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.**
Equity Instrument of another entity	• Investment in Equity share of another entity
Contractual Right of receiving Cash (Non-Derivative)	• Debtors • Bills Receivables • Loans & Advances • Investments in Bonds & Debentures • Investments in Preference shares
Contractual Right of Receiving FAs other Cash	• Repurchase Agreement • Securitisation Contract
Contract of exchanging FAs with FL	• Exchanging or raising a loan by giving away by old loan
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.
Derivative Contract settled in cash	• F & O which are cash settled including F & O on commodities which are cash settled.
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

A financial liability is any liability that is:

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.
Contractual Obligation to deliver FA other Cash	•Repurchased Agreement •Securitisation Contracts •Advance Received for issuing Bonds or debentures
Contractual Obligation of Exchanging FAs against FLs	•Raising a new loan and repay an existing Loan
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".**
Obligation under derivate contract to be settled by delivery of cash	•F & O which are cash settled including F & O on commodities which are cash settled.
Obligation under derivate contract to be settled by delivery of FAs other than cash	•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**

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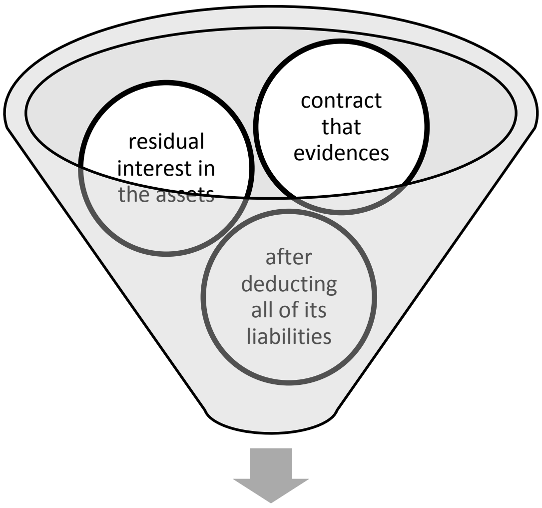
Followings are not FAS or FLs:

- Gold (Since it is a commodity)
- Non-Monetary or Physical Assets. (Fixed Assets, Intangible Assets, Commodities and Inventories)
- Insurance Contracts
- Derivate Contract to be settled by delivery of Commodity.
- Prepaid Expenditure (The Benefit shall be enjoyed inform of service and not FA)
- Deferred Tax Assets, Deferred Tax Liabilities and provision for taxation. (Since there is no contract with Government)
- 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:

- Leases (AS 19)
- Investments in Subsidiaries (AS 21)
- Investments in Associates (AS 23)
- Investments in joint Ventures (AS 27)



equity instrument

Categories of Financial Instruments

The four categories are:

Financial Assets at fair value through profit or loss

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

Held to maturity

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

Note: FA's classified as FVTPL at the time of inception are irrevocable

Loans & Recievable

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

Available for sale

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

Held for trading

- acquired or incurred principally for the purpose of selling or repurchasing it in the near term
- of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking part
- a derivative (except for a derivative that is a financial guarantee contract or a designated and effective hedging instrument).

Examples of held for trading financial assets are:

- Equity securities bought and sold by defined benefit pension plan and investment companies that are actively traded by the entity;
- A portfolio of debt and/or equity securities managed by a trading desk;
- Reverse repurchase agreements that form part of a trading book; or
- Derivative financial instruments that are not effective hedging instruments.

Measurement of FA's

FVTPL- Initial Measurement

- 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

Subsequent Measurement

- Change in fair value between two reporting date, whether gain or loss, shall be recognized in P & L A/c

Treatment of Income Earned

- Recognized in P & L A/c

Treatment of Gain or loss on sale/ De-recognition

- Recognized in P & L A/c

HTM- Initial Measurement

- Initially recorded at fair value on Acquisition Date
- Initially fair value is acquisition price + Directly attributable transaction cost

Subsequent Measurement

- Accounted over its maturity by adopting amortized cost method applying Effective Interest Rate (i.e. IRR/YTM)

Treatment of Income Earned

- Recognized in P & L A/c

Treatment of Gain or loss on sale/ De-recognition

- If any then Recognized in P & L A/c

LR for a period not more than 1yr

Initial Measurement

- Initially recorded at invoice value

Subsequent Measurement

- Continue to be reported at its invoice value

Treatment of Income Earned

- Recognized in P & L A/c

Treatment of Gain or loss on sale/ De-recognition

- Recognized in P & L A/c

LR for a period not more than 1yr

Initial Measurement

- Initially recorded at fair value on Acquisition Date
- Initially fair value is acquisition price + Directly attributable transaction cost

Subsequent Measurement

- Accounted over its maturity by adopting amortized cost method applying Effective Interest Rate (i.e. IRR/YTM)

Treatment of Income Earned

- Recognized in P & L A/c

Treatment of Gain or loss on sale/ De-recognition

- If any then Recognized in P & L A/c

AFS -Initial Measurement

- Initially recorded at fair value on acquisition date.
- Initial fair value is acquisition attributable transaction cost

Subsequent Measurement

- Change in Fair value between reporting date, whether gain or loss, shall be transferred to investment revaluation reserve* or fair value reserve

Treatment of Income Earned

- Recognized in P & L A/c

Treatment of Gain or loss on sale/ De-recognition

- 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)

Initial Measurement

- Initially recorded at fair value on acquisition date.
- Initial fair value is acquisition attributable transaction cost

Subsequent Measurement

- Continued to be reported at initial recorded cost

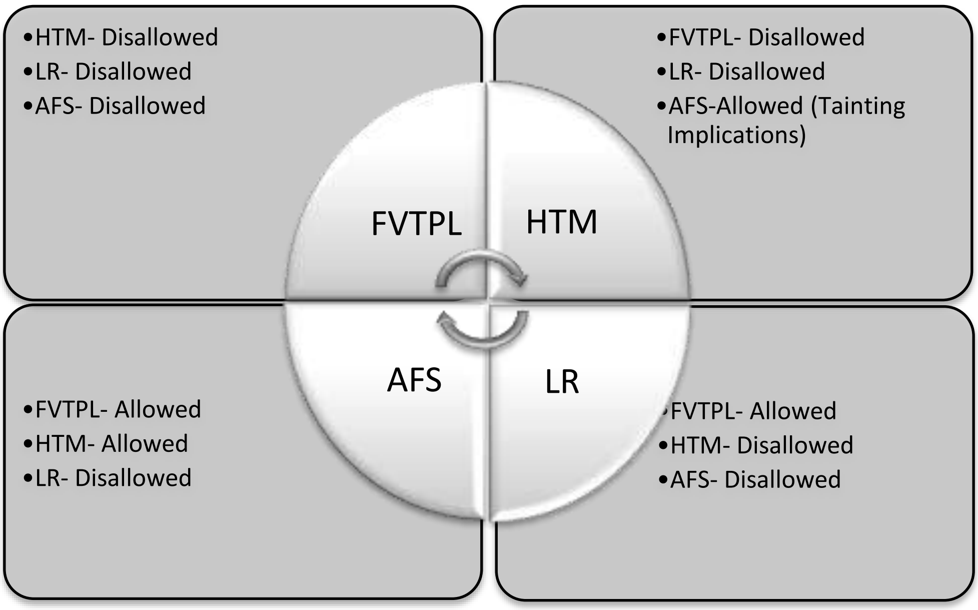
Treatment of Income Earned

- Recognized in P & L A/c

Treatment of Gain or loss on sale/ De-recognition

- Recognized in P & L A/c

Reclassification of FA's



Embedded Derivatives

An Embedded Derivative is a component of hybrid instrument, which also include a non-derivative host contract.

<u>Note:</u> A derivative that is attached to a financial instrument but is contractually transferable independently of that instrument, or has a different counterparty from that instrument, is not an embedded derivative, but a separate financial instrument.

An embedded derivative should be separated from the host contract and accounted for as a derivative under this Standard if, and only if:

Host Contract is not classified as FVTPL. → Contract gives rise to free standing derivative (i.e. derivative has an identity its own) → Economic Characteristic and risk of derivative are not closely related to (i.e. significant different) economic characteristic & risk of the host contract.

This Standard does not address whether an embedded derivative should be presented separately on the face of the financial statements.

If a contract contains one or more embedded derivatives, designate the entire hybrid (combined) contract as a financial asset or financial liability at FVTPL *unless*:

- the embedded derivative(s) does not significantly modify the cash flows that otherwise would be required by the contract
- it is clear with little or no analysis when a similar hybrid (combined) instrument is first considered that separation of the embedded derivative(s) is prohibited, such as a prepayment option embedded in a loan that permits the holder to prepay the loan for approximately its amortised cost

If embedded derivative and host contract cannot be seperated

Record hybrid contract at FVTPL

If fair value of embedded derivative cannot be determined, then

fair value of the embedded derivative is the difference between the **fair value of the hybrid** (combined) instrument and the **fair value of the host contract**

Example: A lease contract contains a provision that rentals increase each year by 10%. Is there an embedded derivative in this contract?
Answer: No. There is no embedded derivative since lease rental does not depend on any underling basis.

Example: X Co. entered with Y Co. to sell coal over a period of two year. The coal price will be determined as per the increase in electricity prices. Is there an embedded derivative?
Answer: Yes, there is embedded derivative because cash flow of the contract or settlement price is dependent on underlying electricity price.

De-recognition of a Financial Asset

An entity should derecognise a financial asset when, and only when

- the contractual rights to the cash flows from the financial asset expire
- it transfers the financial asset and the transfer qualifies for derecognition

An entity transfers a financial asset if, and only if it

transfers the contractual rights to receive the cash flows of the financial asset

assumes a contractual obligation to pay the cash flows to one or more recipients in an arrangement that meets the conditions

When an entity assumes a contractual obligation to pay those cash flows to one or more entities, the entity treats the transaction as a transfer of a financial asset if, and only if

The entity has no obligation to pay amounts to the eventual recipients unless it collects equivalent amounts from the original asset. Short-term advances by the entity to the eventual recipients with the right of full recovery of the amount lent plus accrued interest at market rates do not violate this condition, &

The entity is prohibited by the terms of the transfer contract from selling or pledging the original asset other than as security to the eventual recipients for the obligation to pay them cash flows

The entity has an obligation to remit any cash flows it collects on behalf of the eventual recipients without material delay. In addition, the entity is not entitled to reinvest such cash flows, except for investments in cash or cash equivalents

When an entity transfers a financial asset (see paragraph B), it should evaluate the extent to which it retains the risks and rewards of ownership of the financial asset

all risk & rewards transferred- Derecognise

Retains Substantially all rights- continue to recognise

Regular Way Purchase or Sale of a Financial Asset

Trade Date Accounting	the recognition of an asset to be received and the liability to pay for it on the trade date	derecognition of an asset that is sold, recognition of any gain or loss on disposal and the recognition of a receivable from the buyer for payment on the trade date
Settlement Date Accounting	the recognition of an asset on the day it is received by the entity	derecognition of an asset and recognition of any gain or loss on disposal on the day that it is delivered by the entity

Hedging relationships are of three types:

Fair Value Hedge

- hedge of the exposure to changes in fair value of asset or liability or an unrecognised firm commitment, attributable to a particular risk and could affect profit or loss
- from existing assets or liabilities, including firm commitments
- Non-financial assets have a fair value exposure to changes in their market price, eg a commodity price
- Eg. Fixed rate liabilities like loans; Fixed rate assets like investments in bonds; Investments in equity securities; and Firm commitments to by/sell non-financial items at fixed price.

Firm Commitments

binding agreement for the exchange of a specified quantity or resources at a specified price on a specified future date

CASH FLOW HEDGE
hedge of the exposure to variability in cash flows that

attributable to a particular risk associated with a recognised asset or liabilityor a highly probable forecast transaction &

could affect profit or loss

Eg. Variable rate liabilities like loans; Variable rate assets like investments in bonds; Highly probable future issuance of fixed rate debt; Forecast reinvestment of interest and principal received on fixed rate assets; and Highly probable forecast sales and purchases

An example of a cash flow hedge is a hedge of variable rate debt with a floating to fixed interest rate swap. The cash flow hedge reduces future variability of interest cash flows on the debt. A hedging instrument that swaps one variable rate for another, eg LIBOR for MIBOR, would not qualify in a cash flow hedge relationship as it does not reduce cash flow variability; it merely swaps the existing cash flow variability of the debt for cash flow variability determined on a different basis.