Accounting Standard (AS) 32
Financial Instruments: Disclosures

Issued by

The Institute of Chartered Accountants of India

New Delhi

Accounting Standard (AS) 32

Financial Instruments: Disclosures

Contents

Accounting Standard (AS) 32
Financial Instruments: Disclosures

*(This Accounting Standard includes paragraphs set in **bold italic** type and plain type, which have equal authority. Paragraphs in bold italic type indicate the main principles. This Accounting Standard should be read in the context of its objective and the Preface to the Statements of Accounting Standards[1].)*

Accounting Standard (AS) 32, *Financial Instruments: Disclosures*, issued by the Council of the Institute of Chartered Accountants of India, comes into effect in respect of accounting periods commencing on or after 1-4-2009 and will be recommendatory in nature for an initial period of two years. This Accounting Standard will become mandatory[2] 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, 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) which is not a bank (including a co-operative bank), financial institution or any entity carrying on insurance business;

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

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

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

For the above purpose an entity would qualify as a Small and Medium-sized Entity, if the conditions mentioned therein are satisfied as at the end of the relevant accounting period.

---

[1] Attention is specifically drawn to paragraph 4.3 of the Preface, according to which Accounting Standards are intended to apply only to items which are material.

[2] This implies that, while discharging their attest function, it will be the duty of the members of the Institute to examine whether this Accounting Standard is complied with in the presentation of financial statements covered by their audit. In the event of any deviation from this Accounting Standard, it will be their duty to make adequate disclosures in their audit reports so that the users of financial statements may be aware of such deviations.

Where in respect of an entity there is a statutory requirement for disclosing any financial instrument in a particular manner as asset, liability or equity and/or for disclosing income, expenses, gains or losses relating to a financial instrument in a particular manner as income/expense or as distribution of profits, the entity should disclose that instrument and/or income, expenses, gains or losses relating to the instrument in accordance with the requirements of the statute governing the entity. Until the relevant statute is amended, the entity disclosing that instrument and/ or income, expenses, gains or losses relating to the instrument in accordance with the requirements thereof will be considered to be complying with this Accounting Standard, in view of paragraph 4.1 of the *Preface to the Statements of Accounting Standards* which recognises that where a requirement of an Accounting Standard is different from the applicable law, the law prevails.

The following is the text of the Accounting Standard.

Objective

1. The objective of this Standard is to require entities to provide disclosures in their financial statements that enable users to evaluate:

(a) the significance of financial instruments for the entity's financial position and performance; and

(b) 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.

2. The principles in this Accounting Standard complement the principles for recognising, measuring and presenting financial assets and financial liabilities in Accounting Standard (AS) 30, *Financial Instruments: Recognition and Measurement* and Accounting Standard (AS) 31, *Financial Instruments: Presentation*.

Scope

3. This Accounting Standard should be applied by all entities to all types of financial instruments, except:

(a) those interests in subsidiaries, associates and joint ventures that are accounted for in accordance with AS 21, *Consolidated Financial Statements and Accounting for Investment in Subsidiaries in Separate Financial Statements*, AS 23, *Accounting for Investments in Associates*[3], or AS 27*, Financial*

[3] The titles of AS 21 and AS 23 have been changed by making Limited Revisions thereto pursuant to the issuance of AS 30, *Financial Instruments: Recognition and Measurement.*

Reporting of Interests in Joint Ventures. However, in some cases, AS 21, AS 23 or AS 27 permits or requires an entity to account for an interest in a subsidiary, associate or joint venture using Accounting Standard (AS) 30, *Financial Instruments: Recognition and Measurement*; in those cases, entities should apply the disclosure requirements in AS 21, AS 23 or AS 27 in addition to those in this Accounting Standard. Entities should also apply this Accounting Standard to all derivatives linked to interests in subsidiaries, associates or joint ventures unless the derivative meets the definition of an equity instrument in AS 31.

(b) employers' rights and obligations arising from employee benefit plans, to which AS 15, *Employee Benefits,* applies.

(c) contracts for contingent consideration in a business combination[4]. This exemption applies only to the acquirer.

(d) insurance contracts as defined in Accounting Standard on Insurance Contracts[5]. However, this Accounting Standard applies to derivatives that are embedded in insurance contracts if Accounting Standard (AS) 30, *Financial Instruments: Recognition and Measurement,* requires the entity to account for them separately. Moreover, an issuer should apply this Accounting Standard to *financial guarantee contracts* if the issuer applies AS 30 in recognising and measuring the contracts, but should apply the Accounting Standard on *Insurance Contracts* if the issuer elects, in accordance with the Accounting Standard on *Insurance Contracts*, to apply that Accounting Standard in recognising and measuring them.

(e) financial instruments, contracts and obligations under share-based payment transactions[6] except that this Accounting Standard applies to contracts within the scope of paragraphs 4 to 6 of AS 30.

4. This Accounting Standard applies to recognised and unrecognised financial instruments. Recognised financial instruments include financial assets and financial liabilities that are within the scope of AS 30. Unrecognised financial instruments include some financial instruments that, although outside the scope of AS 30, are within the scope of this Accounting Standard (such as some loan commitments).

---

[4] 'Business combination' is the bringing together of separate entities or businesses into one reporting entity. At present, Accounting Standard (AS) 14, *Accounting for Amalgamations*, deals with accounting for contingent consideration in an amalgamation, which is a form of business combination.

[5] A separate Accounting Standard on *Insurance Contracts*, which is being formulated, will specify the requirements relating to insurance contracts.

[6] Employee share based payment, which is one of the share-based payment transactions, is accounted for as per the Guidance Note on Accounting for Employee Share-based Payments, issued by the ICAI. Further, some other pronouncements of the ICAI deal with other share-based payments, e.g., AS 10, *Accounting for Fixed Assets*.

5. This Accounting Standard applies to contracts to buy or sell a non-financial item that are within the scope of AS 30 (see paragraphs 4-6 of AS 30).

Classes of financial instruments and level of disclosure

6. When this Accounting Standard requires disclosures by class of financial instrument, an entity should group financial instruments into classes that are appropriate to the nature of the information disclosed and that take into account the characteristics of those financial instruments. An entity should provide sufficient information to permit reconciliation to the line items presented in the balance sheet.

Significance of financial instruments for financial position and performance

7. An entity should disclose information that enables users of its financial statements to evaluate the significance of financial instruments for its financial position and performance.

Balance sheet

Categories of financial assets and financial liabilities

8. The carrying amounts of each of the following categories, as defined in AS 30, should be disclosed either on the face of the balance sheet or in the notes:

(a) financial assets at fair value through profit or loss, showing separately (i) those designated as such upon initial recognition and (ii) those classified as held for trading in accordance with AS 30;

(b) held-to-maturity investments;

(c) loans and receivables;

(d) available-for-sale financial assets;

(e) financial liabilities at fair value through profit or loss, showing separately (i) those designated as such upon initial recognition and (ii) those classified as held for trading in accordance with AS 30; and

(f) financial liabilities measured at amortised cost.

Financial assets or financial liabilities at fair value through profit or loss

9. If the entity has designated a loan or receivable (or group of loans or receivables) as at fair value through profit or loss, it should disclose:

(a) the maximum exposure to *credit risk* (see paragraph 36(a)) of the loan or receivable (or group of loans or receivables) at the reporting date.

(b) the amount by which any related credit derivatives or similar instruments mitigate that maximum exposure to credit risk.

(c) the amount of change, during the period and cumulatively, in the fair value of the loan or receivable (or group of loans or receivables) that is attributable to changes in the credit risk of the financial asset determined either:

   (i) as the amount of change in its fair value that is not attributable to changes in market conditions that give rise to *market risk*; or

   (ii) using an alternative method the entity believes more faithfully represents the amount of change in its fair value that is attributable to changes in the credit risk of the asset.

   Changes in market conditions that give rise to market risk include changes in an observed (benchmark) interest rate, commodity price, foreign exchange rate or index of prices or rates.

(d) the amount of the change in the fair value of any related credit derivatives or similar instruments that has occurred during the period and cumulatively since the loan or receivable was designated.

10. If the entity has designated a financial liability as at fair value through profit or loss in accordance with paragraph 8.2 of AS 30, it should disclose:

(a) the amount of change, during the period and cumulatively, in the fair value of the financial liability that is attributable to changes in the credit risk of that liability determined either:

   (i) as the amount of change in its fair value that is not attributable to changes in market conditions that give rise to market risk (See Appendix B, paragraph B4); or

   (ii) using an alternative method the entity believes more faithfully represents the amount of change in its fair value that is attributable to changes in the credit risk of the liability.

   Changes in market conditions that give rise to market risk include changes in a benchmark interest rate, the price of another entity's financial instrument, a commodity price, a foreign exchange rate or an index of prices or rates. For contracts that include a unit-linking feature, changes in market conditions include changes in the performance of the related internal or external investment fund.

(b) the difference between the financial liability's carrying amount and the amount the entity would be contractually required to pay at maturity to the holder of the obligation.

11. The entity should disclose:

(a) the methods used to comply with the requirements in paragraphs 9(c) and 10(a).

(b) if the entity believes that the disclosure it has given to comply with the requirements in paragraph 9(c) or 10(a) does not faithfully represent the change in the fair value of the financial asset or financial liability attributable to changes in its credit risk, the reasons for reaching this conclusion and the factors it believes are relevant.

Reclassification

12. If the entity has reclassified a financial asset as one measured:

(a) at cost or amortised cost, rather than at fair value; or

(b) at fair value, rather than at cost or amortised cost,

it should disclose the amount reclassified into and out of each category and the reason for that reclassification (see paragraphs 57-60 of AS 30).

Derecognition

13. An entity may have transferred financial assets in such a way that part or all of the financial assets do not qualify for derecognition (see paragraphs 15-37 of AS 30). The entity should disclose for each class of such financial assets:

(a) the nature of the assets;

(b) the nature of the risks and rewards of ownership to which the entity remains exposed;

(c) when the entity continues to recognise all of the assets, the carrying amounts of the assets and of the associated liabilities; and

(d) when the entity continues to recognise the assets to the extent of its continuing involvement, the total carrying amount of the original assets, the amount of the assets that the entity continues to recognise, and the carrying amount of the associated liabilities.

Collateral

14. An entity should disclose:

(a) the carrying amount of financial assets it has pledged as collateral for liabilities or contingent liabilities, including amounts that have been reclassified in accordance with paragraphs 37(a) of AS 30; and

(b) the terms and conditions relating to its pledge.

15. When an entity holds collateral (of financial or non-financial assets) and is permitted to sell or repledge the collateral in the absence of default by the owner of the collateral, it should disclose:

(a) the fair value of the collateral held;

(b) the fair value of any such collateral sold or repledged, and whether the entity has an obligation to return it; and

(c) the terms and conditions associated with its use of the collateral.

Allowance account for credit losses

16. When financial assets are impaired by credit losses and the entity records the impairment in a separate account (eg an allowance account used to record individual impairments or a similar account used to record a collective impairment of assets) rather than directly reducing the carrying amount of the asset, it should disclose a reconciliation of changes in that account during the period for each class of financial assets.

Compound financial instruments with multiple embedded derivatives

17. If an entity has issued an instrument that contains both a liability and an equity component (see paragraph 58 of AS 31) and the instrument has multiple embedded derivatives whose values are interdependent (such as a callable convertible debt instrument), it should disclose the existence of those features.

Defaults and breaches

18. For *loans payable* recognised at the reporting date, an entity should disclose:

(a) details of any defaults during the period of principal, interest, sinking fund, or redemption terms of those loans payable;

(b) the carrying amount of the loans payable in default at the reporting date; and

(c) whether the default was remedied, or the terms of the loans payable were renegotiated, before the financial statements were authorised for issue.

19. If, during the period, there were breaches of loan agreement terms other than those described in paragraph 18, an entity should disclose the same information as required by paragraph 18 if those breaches permitted the lender to demand accelerated repayment (unless the breaches were remedied, or the terms of the loan were renegotiated, on or before the reporting date).

Statement of profit and loss and equity

Items of income, expense, gains or losses

20. An entity should disclose the following items of income, expense, gains or losses either on the face of the financial statements or in the notes:

(a) net gains or net losses on:

(i) financial assets or financial liabilities at fair value through profit or loss, showing separately those on financial assets or financial liabilities designated as such upon initial recognition, and those on financial assets or financial liabilities that are classified as held for trading in accordance with AS 30;

(ii) available-for-sale financial assets, showing separately the amount of gain or loss recognised directly in equity during the period and the amount removed from equity and recognised in the statement of profit and loss for the period;

(iii) held-to-maturity investments;

(iv) loans and receivables; and

(v) financial liabilities measured at amortised cost.

(b) total interest income and total interest expense (calculated using the effective interest method) for financial assets or financial liabilities that are not at fair value through profit or loss;

(c) fee income and expense (other than amounts included in determining the effective interest rate) arising from:

   (i) financial assets or financial liabilities that are not at fair value through profit or loss; and

   (ii) trust and other fiduciary activities that result in the holding or investing of assets on behalf of individuals, trusts, retirement benefit plans, and other institutions;

(d) interest income on impaired financial assets accrued in accordance with paragraph A113 of AS 30; and

(e) the amount of any impairment loss for each class of financial asset.

Other disclosures

Accounting policies

21. In accordance with AS 1, *Presentation of Financial Statements*[7], an entity discloses, in the summary of significant accounting policies, the measurement basis (or bases) used in preparing the financial statements and the other accounting policies used that are relevant to an understanding of the financial statements.

Hedge accounting

22. An entity should disclose the following separately for each type of hedge described in AS 30 (i.e. fair value hedges, cash flow hedges, and hedges of net investments in foreign operations):

(a) a description of each type of hedge;

(b) a description of the financial instruments designated as hedging instruments and their fair values at the reporting date; and

(c) the nature of the risks being hedged.

23. For cash flow hedges, an entity should disclose:

(a) the periods when the cash flows are expected to occur and when they are expected to affect profit or loss;

[7] Revised AS 1 is under preparation.

(b) a description of any forecast transaction for which hedge accounting had previously been used, but which is no longer expected to occur;

(c) the amount that was recognised in the appropriate equity account (Hedging Reserve Account) during the period;

(d) the amount that was removed from the appropriate equity account (Hedging Reserve Account) and included in the statement of profit and loss for the period, showing the amount included in each line item in the statement; and

(e) the amount that was removed from appropriate equity account (Hedging Reserve Account) during the period and included in the initial cost or other carrying amount of a non-financial asset or non-financial liability whose acquisition or incurrence was a hedged highly probable forecast transaction.

24. An entity should disclose separately:

(a) in fair value hedges, gains or losses:

(i) on the hedging instrument; and

(ii) on the hedged item attributable to the hedged risk.

(b) the ineffectiveness recognised in the statement of profit and loss that arises from cash flow hedges; and

(c) the ineffectiveness recognised in the statement of profit and loss that arises from hedges of net investments in foreign operations.

Fair value

25. Except as set out in paragraph 29, for each class of financial assets and financial liabilities (see paragraph 6), an entity should disclose the fair value of that class of assets and liabilities in a way that permits it to be compared with its carrying amount.

26. In disclosing fair values, an entity should group financial assets and financial liabilities into classes, but should offset them only to the extent that their carrying amounts are offset in the balance sheet.

27. An entity should disclose:

(a) the methods and, when a valuation technique is used, the assumptions applied in determining fair values of each class of financial assets or financial liabilities. For example, if applicable, an entity discloses information about the assumptions relating to prepayment rates, rates of estimated credit losses, and interest rates or discount rates.

(b) whether fair values are determined, in whole or in part, directly by reference to published price quotations in an active market or are estimated using a valuation technique (see paragraphs A90 –A99 of AS 30).

(c) whether the fair values recognised or disclosed in the financial statements are determined in whole or in part using a valuation technique based on assumptions that are not supported by prices from observable current market transactions in the same instrument (i.e. without modification or repackaging) and not based on available observable market data. For fair values that are recognised in the financial statements, if changing one or more of those assumptions to reasonably possible alternative assumptions would change fair value significantly, the entity should state this fact and disclose the effect of those changes. For this purpose, significance should be judged with respect to profit or loss, and total assets or total liabilities, or, when changes in fair value are recognised in equity, total equity.

(d) if (c) applies, the total amount of the change in fair value estimated using such a valuation technique that was recognised in the statement of profit and loss during the period.

28. If the market for a financial instrument is not active, an entity establishes its fair value using a valuation technique (see paragraphs A93-A99 of AS 30). Nevertheless, the best evidence of fair value at initial recognition is the transaction price (i.e. the fair value of the consideration given or received), unless conditions described in paragraph A95 of AS 30 are met. It follows that there could be a difference between the fair value at initial recognition and the amount that would be determined at that date using the valuation technique. If such a difference exists, an entity should disclose, by class of financial instrument:

(a) its accounting policy for recognising that difference in the statement of profit and loss to reflect a change in factors (including time) that market participants would consider in setting a price (see paragraph A96 of AS 30); and

(b) the aggregate difference yet to be recognised in the statement of profit and loss at the beginning and end of the period and a reconciliation of changes in the balance of this difference.

29. Disclosures of fair value are not required:

(a) when the carrying amount is a reasonable approximation of fair value, for example, for financial instruments such as short-term trade receivables and payables;

(b) for an investment in equity instruments that do not have a quoted market price in an active market, or derivatives linked to such equity instruments, that is measured at cost in accordance with AS 30 because its fair value cannot be measured reliably; or

(c) for a contract containing a discretionary participation feature (as described in the Accounting Standard on *Insurance Contracts*[8]) if the fair value of that feature cannot be measured reliably.

30. In the cases described in paragraph 29(b) and (c), an entity should disclose information to help users of the financial statements make their own judgments about the extent of possible differences between the carrying amount of those financial assets or financial liabilities and their fair value, including:

(a) the fact that fair value information has not been disclosed for these instruments because their fair value cannot be measured reliably;

(b) a description of the financial instruments, their carrying amount, and an explanation of why fair value cannot be measured reliably;

(c) information about the market for the instruments;

(d) information about whether and how the entity intends to dispose of the financial instruments; and

(e) if financial instruments whose fair value previously could not be reliably measured are derecognised, that fact, their carrying amount at the time of derecognition, and the amount of gain or loss recognised.

Nature and extent of risks arising from financial instruments

31. An entity should disclose information that enables users of its financial statements to evaluate the nature and extent of risks arising from financial instruments to which the entity is exposed at the reporting date.

32. The disclosures required by paragraphs 33–42 focus on the risks that arise from financial instruments and how they have been managed. These risks typically include, but are not limited to, credit risk, *liquidity risk* and market risk.

Qualitative disclosures

33. For each type of risk arising from financial instruments, an entity should disclose:

(a) the exposures to risk and how they arise;

[8] See footnote 5.

(b) its objectives, policies and processes for managing the risk and the methods used to measure the risk; and

(c) any changes in (a) or (b) from the previous period.

Quantitative disclosures

34. For each type of risk arising from financial instruments, an entity should disclose:

(a) summary quantitative data about its exposure to that risk at the reporting date. This disclosure should be based on the information provided internally to key management personnel of the entity (as defined in AS 18 *Related Party Disclosures*), for example the entity's board of directors or chief executive officer.

(b) the disclosures required by paragraphs 36–42, to the extent not provided in (a), unless the risk is not material (see AS 1 (Revised)[9] for a discussion of materiality).

(c) Concentrations of risk if not apparent from (a) and (b).

35. If the quantitative data disclosed as at the reporting date are unrepresentative of an entity's exposure to risk during the period, an entity should provide further information that is representative.

Credit risk

36. An entity should disclose by class of financial instrument:

(a) the amount that best represents its maximum exposure to credit risk at the reporting date without taking account of any collateral held or other credit enhancements (eg netting agreements that do not qualify for offset in accordance with AS 31);

(b) in respect of the amount disclosed in (a), a description of collateral held as security and other credit enhancement;

(c) information about the credit quality of financial assets that are neither *past due* nor impaired; and

(d) the carrying amount of financial assets that would otherwise be past due or impaired whose terms have been renegotiated.

[9] See footnote 7.

Financial assets that are either past due or impaired

37. An entity should disclose by class of financial asset:

(a) an analysis of the age of financial assets that are past due as at the reporting date but not impaired;

(b) an analysis of financial assets that are individually determined to be impaired as at the reporting date, including the factors the entity considered in determining that they are impaired; and

(c) for the amounts disclosed in (a) and (b), a description of collateral held by the entity as security and other credit enhancements and, unless impracticable, an estimate of their fair value.

Collateral and other credit enhancements obtained

38. When an entity obtains financial or non-financial assets during the period by taking possession of collateral it holds as security or calling on other credit enhancements (eg guarantees), and such assets meet the recognition criteria in other Standards, an entity should disclose:

(a) the nature and carrying amount of the assets obtained; and

(b) when the assets are not readily convertible into cash, its policies for disposing of such assets or for using them in its operations.

Liquidity risk

39. An entity should disclose:

(a) a maturity analysis for financial liabilities that shows the remaining contractual maturities; and

(b) a description of how it manages the liquidity risk inherent in (a).

Market risk

Sensitivity analysis

40. Unless an entity complies with paragraph 41, it should disclose:

(a) a sensitivity analysis for each type of market risk to which the entity is exposed at the reporting date, showing how profit or loss and equity would have been affected by changes in the relevant risk variable that were reasonably possible at that date;

(b) the methods and assumptions used in preparing the sensitivity analysis; and

(c) changes from the previous period in the methods and assumptions used, and the reasons for such changes.

41. If an entity prepares a sensitivity analysis, such as value-at-risk, that reflects interdependencies between risk variables (eg interest rates and exchange rates) and uses it to manage financial risks, it may use that sensitivity analysis in place of the analysis specified in paragraph 40. The entity should also disclose:

(a) an explanation of the method used in preparing such a sensitivity analysis, and of the main parameters and assumptions underlying the data provided; and

(b) an explanation of the objective of the method used and of limitations that may result in the information not fully reflecting the fair value of the assets and liabilities involved.

Other market risk disclosures

42. When the sensitivity analyses disclosed in accordance with paragraph 40 or 41 are unrepresentative of a risk inherent in a financial instrument (for example because the year-end exposure does not reflect the exposure during the year), the entity should disclose that fact and the reason it believes the sensitivity analyses are unrepresentative.

Appendix A

Defined terms

This appendix is an integral part of AS 32, Financial Instruments: Disclosures.

credit risk

The risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

currency risk

The risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

interest rate risk

The risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

liquidity risk
The risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities.

loans payable

Loans payable are financial liabilities, other than short-term trade payables on normal credit terms.

market risk

The risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: **currency risk**, **interest rate risk** and **other price risk**.

other price risk

The risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from **interest rate risk** or **currency risk**), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

past due

A financial asset is past due when a counterparty has failed to make a payment when contractually due.

The following terms are defined in paragraph 8 of AS 30, *Financial Instruments: Recognition and Measurement,* or paragraph 7 of AS 31, *Financial Instruments: Presentation,* and are used in this Standard with the meaning specified in AS 30 and AS 31.

- amortised cost of a financial asset or financial liability
- available-for-sale financial assets
- derecognition
- derivative
- effective interest method
- equity instrument
- fair value
- financial asset
- financial instrument
- financial liability
- financial asset or financial liability at fair value through profit or loss
- financial guarantee contract
- financial asset or financial liability held for trading
- forecast transaction
- hedging instrument
- held-to-maturity investments
- loans and receivables
- regular way purchase or sale

Appendix B

Application guidance

This appendix is an integral part of AS 32, Financial Instruments: Disclosures

Classes of financial instruments and level of disclosure (paragraph 6)

B1 Paragraph 6 requires an entity to group financial instruments into classes that are appropriate to the nature of the information disclosed and that take into account the characteristics of those financial instruments. The classes described in paragraph 6 are determined by the entity and are, thus, distinct from the categories of financial instruments specified in AS 30 (which determine how financial instruments are measured and where changes in fair value are recognised).

B2 In determining classes of financial instrument, an entity should, at a minimum:

(a) distinguish instruments measured at amortised cost from those measured at fair value.

(b) treat as a separate class or classes those financial instruments outside the scope of this AS.

B3 An entity decides, in the light of its circumstances, how much detail it provides to satisfy the requirements of this AS, how much emphasis it places on different aspects of the requirements and how it aggregates information to display the overall picture without combining information with different characteristics. It is necessary to strike a balance between overburdening financial statements with excessive detail that may not assist users of financial statements and obscuring important information as a result of too much aggregation. For example, an entity should not obscure important information by including it among a large amount of insignificant detail. Similarly, an entity should not disclose information that is so aggregated that it obscures important differences between individual transactions or associated risks.

Significance of financial instruments for financial position and performance

Financial liabilities at fair value through profit or loss (paragraphs 10 and 11)

B4 If an entity designates a financial liability as at fair value through profit or loss, paragraph 10(a) requires it to disclose the amount of change in the fair value of the financial liability that is attributable to changes in the liability's credit risk. Paragraph 10(a)(i) permits an entity to determine this amount as the amount of change in the liability's fair value that is not attributable to changes in market conditions that give rise to market risk. If the only relevant changes in market conditions for a liability are changes in an observed (benchmark) interest rate, this amount can be estimated as follows:

(a) First, the entity computes the liability's internal rate of return at the start of the period using the observed market price of the liability and the liability's contractual cash flows at the start of the period. It deducts from this rate of return the observed (benchmark) interest rate at the start of the period, to arrive at an instrument-specific component of the internal rate of return.

(b) Next, the entity calculates the present value of the cash flows associated with the liability using the liability's contractual cash flows at the end of the period and a discount rate equal to the sum of (i) the observed (benchmark) interest rate at the end of the period and (ii) the instrument-specific component of the internal rate of return as determined in (a).

(c) The difference between the observed market price of the liability at the end of the period and the amount determined in (b) is the change in fair value that is not attributable to changes in the observed (benchmark) interest rate. This is the amount to be disclosed.

This example assumes that changes in fair value arising from factors other than changes in the instrument's credit risk or changes in interest rates are not significant. If the instrument in the example contains an embedded derivative, the change in fair value of the embedded derivative is excluded in determining the amount to be disclosed in accordance with paragraph 10(a).

Other disclosure – accounting policies (paragraph 21)

B5 Paragraph 21 requires disclosure of the measurement basis (or bases) used in preparing the financial statements and the other accounting policies used that are relevant to an understanding of the financial statements. For financial instruments, such disclosure may include:

(a) for financial assets or financial liabilities designated as at fair value through profit or loss:

(i) the nature of the financial assets or financial liabilities the entity has designated as at fair value through profit or loss;

(ii) the criteria for so designating such financial assets or financial liabilities on initial recognition; and

(iii) how the entity has satisfied the conditions in paragraphs 8, 11 or 12 of AS 30 for such designation. For instruments designated in accordance with paragraph 8.2 (b)(i) of the definition of a financial asset or financial liability at fair value through profit or loss in AS 30, that disclosure includes a narrative description of the circumstances underlying the measurement or recognition inconsistency that would otherwise arise. For instruments designated in accordance with paragraph 8.2 (b)(ii) of the definition of a financial asset or financial liability at fair value through profit or loss in AS 30, that disclosure includes a narrative description of how designation at fair value through profit or loss is consistent with the entity's documented risk management or investment strategy.

(b) the criteria for designating financial assets as available for sale.

(c) whether regular way purchases and sales of financial assets are accounted for at trade date or at settlement date (see paragraph 38 of AS 30).

(d) when an allowance account is used to reduce the carrying amount of financial assets impaired by credit losses:

(i) the criteria for determining when the carrying amount of impaired financial assets is reduced directly (or, in the case of a reversal of a write-down, increased directly) and when the allowance account is used; and

(ii) the criteria for writing off amounts charged to the allowance account against the carrying amount of impaired financial assets (see paragraph 16).

(e) how net gains or net losses on each category of financial instrument are determined (see paragraph 20(a)), for example, whether the net gains or net losses on items at fair value through profit or loss include interest or dividend income.

(f) the criteria the entity uses to determine that there is objective evidence that an impairment loss has occurred (see paragraph 20(e)).

(g) when the terms of financial assets that would otherwise be past due or impaired have been renegotiated, the accounting policy for financial assets that are the subject of renegotiated terms (see paragraph 36(d)).

AS 1 (Revised)[10], also requires entities to disclose, in the summary of significant accounting policies or other notes, the judgments, apart from those involving estimations,

[10] See footnote 7.

that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

Nature and extent of risks arising from financial instruments (paragraphs 31–42)

B6 The disclosures required by paragraphs 31–42 should be either given in the financial statements or incorporated by cross-reference from the financial statements to some other statement, such as a management commentary or risk report, that is available to users of the financial statements on the same terms as the financial statements and at the same time. Without the information incorporated by cross-reference, the financial statements are incomplete.

Quantitative disclosures (paragraph 34)

B7 Paragraph 34(a) requires disclosures of summary quantitative data about an entity's exposure to risks based on the information provided internally to key management personnel of the entity. When an entity uses several methods to manage a risk exposure, the entity should disclose information using the method or methods that provide the most relevant and reliable information. AS 5, *Accounting Policies, Changes in Accounting Estimates and Errors,*[11] discusses relevance and reliability.

B8 Paragraph 34(c) requires disclosures about concentrations of risk. Concentrations of risk arise from financial instruments that have similar characteristics and are affected similarly by changes in economic or other conditions. The identification of concentrations of risk requires judgement taking into account the circumstances of the entity. Disclosure of concentrations of risk should include:

(a) a description of how management determines concentrations;

(b) a description of the shared characteristic that identifies each concentration (eg counterparty, geographical area, currency or market); and

(c) the amount of the risk exposure associated with all financial instruments sharing that characteristic.

Maximum credit risk exposure (paragraph 36(a))

B9 Paragraph 36(a) requires disclosure of the amount that best represents the entity's maximum exposure to credit risk. For a financial asset, this is typically the gross carrying amount, net of:

(a) any amounts offset in accordance with AS 31; and

[11] The revised Standard is under preparation.

(b) any impairment losses recognised in accordance with AS 30.

B10 Activities that give rise to credit risk and the associated maximum exposure to credit risk include, but are not limited to:

(a) granting loans and receivables to customers and placing deposits with other entities. In these cases, the maximum exposure to credit risk is the carrying amount of the related financial assets.

(b) entering into derivative contracts, eg foreign exchange contracts, interest rate swaps and credit derivatives. When the resulting asset is measured at fair value, the maximum exposure to credit risk at the reporting date will equal the carrying amount.

(c) granting financial guarantees. In this case, the maximum exposure to credit risk is the maximum amount the entity could have to pay if the guarantee is called on, which may be significantly greater than the amount recognised as a liability.

(d) making a loan commitment that is irrevocable over the life of the facility or is revocable only in response to a material adverse change. If the issuer cannot settle the loan commitment net in cash or another financial instrument, the maximum credit exposure is the full amount of the commitment. This is because it is uncertain whether the amount of any undrawn portion may be drawn upon in the future. This may be significantly greater than the amount recognised as a liability.

Contractual maturity analysis (paragraph 39(a))

B11 In preparing the contractual maturity analysis for financial liabilities required by paragraph 39(a), an entity uses its judgement to determine an appropriate number of time bands. For example, an entity might determine that the following time bands are appropriate:

(a) not later than one month;

(b) later than one month and not later than three months;

(c) later than three months and not later than one year; and

(d) later than one year and not later than five years.

B12 When a counterparty has a choice of when an amount is paid, the liability is included on the basis of the earliest date on which the entity can be required to pay. For example, financial liabilities that an entity can be required to repay on demand (eg demand deposits) are included in the earliest time band.

B13 When an entity is committed to make amounts available in instalments, each instalment is allocated to the earliest period in which the entity can be required to pay. For example, an undrawn loan commitment is included in the time band containing the earliest date it can be drawn down.

B14 The amounts disclosed in the maturity analysis are the contractual undiscounted cash flows, for example:

(a) gross finance lease obligations (before deducting finance charges);

(b) prices specified in forward agreements to purchase financial assets for cash;

(c) net amounts for pay-floating/receive-fixed interest rate swaps for which net cash flows are exchanged;

(d) contractual amounts to be exchanged in a derivative financial instrument (eg a currency swap) for which gross cash flows are exchanged; and

(e) gross loan commitments.

Such undiscounted cash flows differ from the amount included in the balance sheet because the balance sheet amount is based on discounted cash flows.

B15 If appropriate, an entity should disclose the analysis of derivative financial instruments separately from that of non-derivative financial instruments in the contractual maturity analysis for financial liabilities required by paragraph 39(a). For example, it would be appropriate to distinguish cash flows from derivative financial instruments and non-derivative financial instruments if the cash flows arising from the derivative financial instruments are settled gross. This is because the gross cash outflow may be accompanied by a related inflow.

B16 When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the reporting date. For example, when the amount payable varies with changes in an index, the amount disclosed may be based on the level of the index at the reporting date.

Market risk – sensitivity analysis (paragraphs 40 and 41)

B17 Paragraph 40(a) requires a sensitivity analysis for each type of market risk to which the entity is exposed. In accordance with paragraph B3, an entity decides how it aggregates information to display the overall picture without combining information with different characteristics about exposures to risks from significantly different economic environments. For example:

(a) an entity that trades financial instruments might disclose this information separately for financial instruments held for trading and those not held for trading.

(b) an entity would not aggregate its exposure to market risks from areas of hyperinflation with its exposure to the same market risks from areas of very low inflation.

If an entity has exposure to only one type of market risk in only one economic environment, it would not show disaggregated information.

B18 Paragraph 40(a) requires the sensitivity analysis to show the effect on profit or loss and equity of reasonably possible changes in the relevant risk variable (eg prevailing market interest rates, currency rates, equity prices or commodity prices). For this purpose:

(a) entities are not required to determine what the profit or loss for the period would have been if relevant risk variables had been different. Instead, entities disclose the effect on profit or loss and equity at the balance sheet date assuming that a reasonably possible change in the relevant risk variable had occurred at the balance sheet date and had been applied to the risk exposures in existence at that date. For example, if an entity has a floating rate liability at the end of the year, the entity would disclose the effect on profit or loss (i.e. interest expense) for the current year if interest rates had varied by reasonably possible amounts.

(b) entities are not required to disclose the effect on profit or loss and equity for each change within a range of reasonably possible changes of the relevant risk variable. Disclosure of the effects of the changes at the limits of the reasonably possible range would be sufficient.

B19 In determining what a reasonably possible change in the relevant risk variable is, an entity should consider:

(a) the economic environments in which it operates. A reasonably possible change should not include remote or 'worst case' scenarios or 'stress tests'. Moreover, if the rate of change in the underlying risk variable is stable, the entity need not alter the chosen reasonably possible change in the risk variable. For example, assume that interest rates are 5 per cent and an entity determines that a fluctuation in interest rates of ±50 basis points is reasonably possible. It would disclose the effect on profit or loss and equity if interest rates were to change to 4.5 per cent or 5.5 per cent. In the next period, interest rates have increased to 5.5 per cent. The entity continues to believe that interest rates may fluctuate by ±50 basis points (i.e. that the rate of change in interest rates is stable). The entity would disclose the effect on profit or loss and equity if interest rates were to change to 5 per cent or 6 per cent. The entity would not be required to revise its assessment that interest rates might reasonably fluctuate by ±50 basis points, unless there is evidence that interest rates have become significantly more volatile.

(b) the time frame over which it is making the assessment. The sensitivity analysis should show the effects of changes that are considered to be reasonably possible over the period until the entity will next present these disclosures, which is usually its next annual reporting period.

B20 Paragraph 41 permits an entity to use a sensitivity analysis that reflects interdependencies between risk variables, such as a value-at-risk methodology, if it uses this analysis to manage its exposure to financial risks. This applies even if such a methodology measures only the potential for loss and does not measure the potential for gain. Such an entity might comply with paragraph 41(a) by disclosing the type of value-at-risk model used (eg whether the model relies on Monte Carlo simulations), an explanation about how the model works and the main assumptions (eg the holding period and confidence level). Entities might also disclose the historical observation period and weightings applied to observations within that period, an explanation of how options are dealt with in the calculations, and which volatilities and correlations (or, alternatively, Monte Carlo probability distribution simulations) are used.

B21 An entity should provide sensitivity analyses for the whole of its business, but may provide different types of sensitivity analysis for different classes of financial instruments.

Interest rate risk

B22 *Interest rate risk* arises on interest-bearing financial instruments recognised in the balance sheet (eg loans and receivables and debt instruments issued) and on some financial instruments not recognised in the balance sheet (eg some loan commitments).

Currency risk

B23 *Currency risk* (or foreign exchange risk) arises on financial instruments that are denominated in a foreign currency, i.e. in a currency other than the functional currency[12] in which they are measured. For the purpose of this Standard, currency risk does not arise from financial instruments that are non-monetary items or from financial instruments denominated in the functional currency.

B24 A sensitivity analysis is disclosed for each currency to which an entity has significant exposure.

[12] See paragraph 8.16 of AS 30 for definition of 'Functional Currency'.

Other price risk

B25 *Other price risk* arises on financial instruments because of changes in, for example, commodity prices or equity prices. To comply with paragraph 40, an entity might disclose the effect of a decrease in a specified stock market index, commodity price, or other risk variable. For example, if an entity gives residual value guarantees that are financial instruments, the entity discloses an increase or decrease in the value of the assets to which the guarantee applies.

B26 Two examples of financial instruments that give rise to equity price risk are a holding of equities in another entity, and an investment in a trust, which in turn holds investments in equity instruments. Other examples include forward contracts and options to buy or sell specified quantities of an equity instrument and swaps that are indexed to equity prices. The fair values of such financial instruments are affected by changes in the market price of the underlying equity instruments.

B27 In accordance with paragraph 40(a), the sensitivity of profit or loss (that arises, for example, from instruments classified as at fair value through profit or loss and impairments of available-for-sale financial assets) is disclosed separately from the sensitivity of equity (that arises, for example, from instruments classified as available for sale).

B28 Financial instruments that an entity classifies as equity instruments are not remeasured. Neither profit or loss nor equity will be affected by the equity price risk of those instruments. Accordingly, no sensitivity analysis is required.

Appendix C

Comparison with IFRS 7, *Financial Instruments: Disclosures*

Note: This Appendix is not a part of the Accounting Standard (AS) 32. The purpose of this appendix is only to bring out the differences between Accounting Standard (AS) 32 and the corresponding International Financial Reporting Standard (IFRS) 7.

Comparison with IFRS 7, *Financial Instruments: Disclosures*

This Accounting Standard is based on International Financial Reporting Standard (IFRS) 7, *Financial Instruments: Disclosures* issued by the International Accounting Standards Board (IASB). There is no material difference between AS 32 and IFRS 7.

Appendix D

GUIDANCE ON IMPLEMENTING AS 32, *FINANCIAL INSTRUMENTS: DISCLOSURES*

Guidance on implementing
AS 32, *Financial Instruments: Disclosures*

This Appendix is not part of AS 32.

Introduction

IG1 This guidance suggests possible ways to apply some of the disclosure requirements in AS 32. The guidance does not create additional requirements.

IG2 For convenience, each disclosure requirement in the AS is discussed separately. In practice, disclosures would normally be presented as an integrated package and individual disclosures might satisfy more than one requirement. For example, information about concentrations of risk might also convey information about exposure to credit or other risk.

Materiality

IG3 Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.

IG4 Assessing whether an omission or misstatement could influence economic decisions of users, and so be material, requires consideration of the characteristics of those users. The *Framework for the Preparation and Presentation of Financial Statements* states in paragraph 26 that 'It is assumed that users have a reasonable knowledge of business and economic activities and accounting and study the information with reasonable diligence.' Therefore, the assessment needs to take into account how users with such attributes could reasonably be expected to be influenced in making economic decisions.

Classes of financial instruments and level of disclosure (paragraphs 6 and B1–B3)

IG5 Paragraph B3 states that 'an entity decides in the light of its circumstances how much detail it provides to satisfy the requirements of AS 32, how much emphasis it places on different aspects of the requirements and how it aggregates information to display the overall picture without combining information with different characteristics.' To satisfy the requirements, an entity may not need to disclose all the information suggested in this guidance.

IG6 AS 1 (Revised)[13] requires an entity to 'provide additional disclosures when compliance with the specific requirements in ASs is insufficient to enable users to

[13] See footnote 7.

understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.'

Significance of financial instruments for financial position and performance (paragraphs 7–30, B4 and B5)

Financial liabilities at fair value through profit or loss (paragraphs 10(a)(i) and B4)

IG7 The following example illustrates the calculation that an entity might perform in accordance with paragraph B4 of Appendix B of this AS.

IG8 On 1 January 20X1, an entity issues a 10-year bond with a par value of Rs. 150,000 and an annual fixed coupon rate of 8 per cent, which is consistent with market rates for bonds with similar characteristics.

IG9 The entity uses MIBOR as its observable (benchmark) interest rate. At the date of inception of the bond, MIBOR is 5 per cent. At the end of the first year:

(a) MIBOR has decreased to 4.75 per cent.

(b) the fair value for the bond is Rs. 153,811, consistent with an interest rate of 7.6 per cent.[14]

IG10 The entity assumes a flat yield curve, all changes in interest rates result from a parallel shift in the yield curve, and the changes in MIBOR are the only relevant changes in market conditions.

IG11 The entity estimates the amount of change in the fair value of the bond that is not attributable to changes in market conditions that give rise to market risk as follows:

[paragraph B4(a)] First, the entity computes the liability's internal rate of return at the start of the period using the observed market price of the liability and the liability's contractual cash flows at the start of the period. It deducts from this rate of return the observed (benchmark) interest rate at the start of the period, to arrive at an instrument-specific component of the internal rate of return.	At the start of the period of a 10-year bond with a coupon of 8 per cent, the bond's internal rate of return is 8 per cent. Because the observed (benchmark) interest rate (MIBOR) is 5 per cent, the instrument-specific component of the internal rate of return is 3 per cent.

[14] This reflects a shift in MIBOR from 5 per cent to 4.75 per cent and a movement of 0.15 per cent which, in the absence of other relevant changes in market conditions, is assumed to reflect changes in credit risk of the instrument.

[paragraph B4(b)] Next, the entity calculates the present value of the cash flows associated with the liability using the liability's contractual cash flows at the end of the period and a discount rate equal to the sum of (i) the observed (benchmark) interest rate at the end of the period and (ii) the instrument-specific component of the internal rate of return as determined in accordance with paragraph B4(a).	The contractual cash flows of the instrument at the end of the period are: • interest: Rs. 12,000[(a)] per year for each of years 2–10. • principal: Rs. 150,000 in year 10. The discount rate to be used to calculate the present value of the bond is thus 7.75 per cent, which is 4.75 per cent end of period MIBOR rate, plus the 3 per cent instrument-specific component. This gives a present value of Rs. 152,367[(b)].
[paragraph B4(c)] The difference between the observed market price of the liability at the end of the period and the amount determined in accordance with paragraph B4(b) is the change in fair value that is not attributable to changes in the observed (benchmark) interest rate. This is the amount to be disclosed.	 The market price of the liability at the end of the period is Rs. 153,811.[(c)] Thus, the entity discloses Rs. 1,444, which is Rs. 153,811 – Rs. 152,367 as the increase in fair value of the bond that is not attributable to changes in market conditions that give rise to market risk.
(a) Rs. 150,000 × 8% = Rs. 12,000 (b) PV = [Rs. 12,000 × (1 – (1 + 0.0775) $^{-9}$)/0.0775] + Rs. 150,000 × (1 + 0.0775)$^{-9}$ (c) market price = [Rs. 12,000 × (1 – (1 + 0.076) $^{-9}$)/0.076] + Rs. 150,000 × (1 + 0.076) $^{-9}$	

Defaults and breaches (paragraphs 18 and 19)

IG12 Paragraphs 18 and 19 require disclosures when there are any defaults or breaches of loans payable. Any defaults or breaches may affect the classification of the liability as current or non-current in accordance with AS 1 (Revised)[15].

[15] See footnote 7.

Total interest expense (paragraph 20(b))

IG13 The total interest expense disclosed in accordance with paragraph 20(b) is a component of the finance costs, which AS 1 (Revised)[16] requires to be presented separately on the face of the statement of profit and loss. The line item for finance costs may also include amounts associated with non-financial liabilities.

Fair value (paragraph 28)

IG14 The fair value at initial recognition of financial instruments that are not traded in active markets is determined in accordance with paragraph A95 of AS 30. However, when, after initial recognition, an entity will use a valuation technique that incorporates data not obtained from observable markets, there may be a difference between the transaction price at initial recognition and the amount determined at initial recognition using that valuation technique. In these circumstances, the difference will be recognised in the statement of profit and loss in subsequent periods in accordance with AS 30 and the entity's accounting policy. Such recognition reflects changes in factors (including time) that market participants would consider in setting a price (see paragraph A96 of AS 30). Paragraph 28 requires disclosures in these circumstances. An entity might disclose the following to comply with paragraph 28:

Background

On 1 January 20X1 an entity purchases for Rs. 15 crore financial assets that are not traded in an active market. The entity has only one class of such financial assets.

The transaction price of Rs. 15 crore is the fair value at initial recognition.

After initial recognition, the entity will apply a valuation technique to establish the financial assets' fair value. This valuation technique includes variables other than data from observable markets.

At initial recognition, the same valuation technique would have resulted in an amount of Rs. 14 crore, which differs from fair value by Rs. 1 crore.

The entity has existing differences of Rs. 5 crore at 1 January 20X1.

Application of requirements

The entity's 20X2 disclosure would include the following:

Accounting policies

The entity uses the following valuation technique to determine the fair value of financial instruments that are not traded in an active market: [description of technique, not

[16] ibid

included in this example]. Differences may arise between the fair value at initial recognition (which, in accordance with AS 30, is generally the transaction price) and the amount determined at initial recognition using the valuation technique. Any such differences are [description of the entity's accounting policy].

In the notes to the financial statements

As discussed in note X, the entity uses [name of valuation technique] to measure the fair value of the following financial instruments that are not traded in an active market. However, in accordance with AS 30, the fair value of an instrument at inception is generally the transaction price. If the transaction price differs from the amount determined at inception using the valuation technique, that difference is [description of the entity's accounting policy].

The differences yet to be recognised in the statement of profit and loss are as follows:

	31 Dec X2 Rs. crore	**31 Dec X1** Rs. crore
Balance at beginning of year	5.3	5.0
New transactions	–	1.0
Amounts recognised in the statement of profit and loss during the year	(0.7)	(0.8)
Other increases	–	0.2
Other decreases	(0.1)	(0.1)
Balance at end of year	4.5	5.3

Nature and extent of risks arising from financial instruments (paragraphs 31–42 and B6–B28)

Qualitative disclosures (paragraph 33)

IG15 The type of qualitative information an entity might disclose to meet the requirements in paragraph 33 includes, but is not limited to, a narrative description of:

(a) the entity's exposures to risk and how they arose. Information about risk exposures might describe exposures both gross and net of risk transfer and other risk-mitigating transactions.

(b) the entity's policies and processes for accepting, measuring, monitoring and controlling risk, which might include:

(i) the structure and organisation of the entity's risk management function(s), including a discussion of independence and accountability;

(ii) the scope and nature of the entity's risk reporting or measurement systems;

(iii) the entity's policies for hedging or mitigating risk, including its policies and procedures for taking collateral; and

(iv) the entity's processes for monitoring the continuing effectiveness of such hedges or mitigating devices.

(c) the entity's policies and procedures for avoiding excessive concentrations of risk.

IG16 Information about the nature and extent of risks arising from financial instruments is more useful if it highlights any relationship between financial instruments that can affect the amount, timing or uncertainty of an entity's future cash flows. The extent to which a risk exposure is altered by such relationships might be apparent to users from the disclosures required by this Standard, but in some cases further disclosures might be useful.

IG17 In accordance with paragraph 33(c), entities disclose any change in the qualitative information from the previous period and explain the reasons for the change. Such changes may result from changes in exposure to risk or from changes in the way those exposures are managed.

Quantitative disclosures (paragraphs 34–42 and B7–B28)

IG18 Paragraph 34 requires disclosure of quantitative data about concentrations of risk. For example, concentrations of credit risk may arise from:

(a) industry sectors. Thus, if an entity's counterparties are concentrated in one or more industry sectors (such as retail or wholesale), it would disclose separately exposure to risks arising from each concentration of counterparties.

(b) credit rating or other measure of credit quality. Thus, if an entity's counterparties are concentrated in one or more credit qualities (such as secured loans or unsecured loans) or in one or more credit ratings (such as investment grade or speculative grade), it would disclose separately exposure to risks arising from each concentration of counterparties.

(c) geographical distribution. Thus, if an entity's counterparties are concentrated in one or more geographical markets (such as Asia or Europe), it would disclose separately exposure to risks arising from each concentration of counterparties.

(d) a limited number of individual counterparties or groups of closely related counterparties.

Similar principles apply to identifying concentrations of other risks, including liquidity risk and market risk. For example, concentrations of liquidity risk may arise from the repayment terms of financial liabilities, sources of borrowing facilities or reliance on a particular market in which to realise liquid assets. Concentrations of foreign exchange risk may arise if an entity has a significant net open position in a single foreign currency, or aggregate net open positions in several currencies that tend to move together.

IG19 In accordance with paragraph B8, disclosure of concentrations of risk includes a description of the shared characteristic that identifies each concentration. For example, the shared characteristic may refer to geographical distribution of counterparties by groups of countries, individual countries or regions within countries.

IG20 When quantitative information at the reporting date is unrepresentative of the entity's exposure to risk during the period, paragraph 35 requires further disclosure. To meet this requirement, an entity might disclose the highest, lowest and average amount of risk to which it was exposed during the period. For example, if an entity typically has a large exposure to a particular currency, but at year-end unwinds the position, the entity might disclose a graph that shows the exposure at various times during the period, or disclose the highest, lowest and average exposures.

Credit risk (paragraphs 36–38, B9 and B10)

IG21 Paragraph 36 requires an entity to disclose information about its exposure to credit risk by class of financial instrument. Financial instruments in the same class share economic characteristics with respect to the risk being disclosed (in this case, credit risk). For example, an entity might determine that residential mortgages, unsecured consumer loans, and commercial loans each have different economic characteristics.

Collateral and other credit enhancements pledged (paragraph 36(b))

IG22 Paragraph 36(b) requires an entity to describe collateral available as security for assets it holds and other credit enhancements obtained. An entity might meet this requirement by disclosing:

(a) the policies and processes for valuing and managing collateral and other credit enhancements obtained;

(b) a description of the main types of collateral and other credit enhancements (examples of the latter being guarantees, credit derivatives, and netting agreements that do not qualify for offset in accordance with AS 31);

(c) the main types of counterparties to collateral and other credit enhancements and their creditworthiness; and

(d) information about risk concentrations within the collateral or other credit enhancements.

Credit quality (paragraph 36(c))

IG23 Paragraph 36(c) requires an entity to disclose information about the credit quality of financial assets with credit risk that are neither past due nor impaired. In doing so, an entity might disclose the following information:

(a) an analysis of credit exposures using an external or internal credit grading system;

(b) the nature of the counterparty;

(c) historical information about counterparty default rates; and

(d) any other information used to assess credit quality.

IG24 When the entity considers external ratings when managing and monitoring credit quality, the entity might disclose information about:

(a) the amounts of credit exposures for each external credit grade;

(b) the rating agencies used;

(c) the amount of an entity's rated and unrated credit exposures; and

(d) the relationship between internal and external ratings.

IG25 When the entity considers internal credit ratings when managing and monitoring credit quality, the entity might disclose information about:

(a) the internal credit ratings process;

(b) the amounts of credit exposures for each internal credit grade; and

(c) the relationship between internal and external ratings.

Financial assets that are either past due or impaired (paragraph 37)

IG26 A financial asset is past due when the counterparty has failed to make a payment when contractually due. As an example, an entity enters into a lending agreement that requires interest to be paid every month. On the first day of the next month, if interest has not been paid, the loan is past due. Past due does not mean that a counterparty will never pay, but it can trigger various actions such as renegotiation, enforcement of covenants, or legal proceedings.

IG27 When the terms and conditions of financial assets that have been classified as past due are renegotiated, the terms and conditions of the new contractual arrangement apply in determining whether the financial asset remains past due.

IG28 Paragraph 37(a) requires an analysis by class of the age of financial assets that are past due but not impaired. An entity uses its judgement to determine an appropriate number of time bands. For example, an entity might determine that the following time bands are appropriate:

(a) not more than three months;

(b) more than three months and not more than six months;

(c) more than six months and not more than one year; and

(d) more than one year.

IG29 Paragraph 37(b) requires an analysis of impaired financial assets by class. This analysis might include:

(a) the carrying amount, before deducting any impairment loss;

(b) the amount of any related impairment loss; and

(c) the nature and fair value of collateral available and other credit enhancements obtained.

Liquidity risk (paragraphs 39 and B11)

Liquidity management (paragraph 39(b))

IG30 If an entity manages liquidity risk on the basis of expected maturity dates, it might disclose a maturity analysis of the expected maturity dates of both financial liabilities and financial assets. If an entity discloses such an expected maturity analysis, it might clarify that expected dates are based on estimates made by management, and explain how the estimates are determined and the principal reasons for differences from the contractual maturity analysis that is required by paragraph 39(a).

IG31 Paragraph 39(b) requires the entity to describe how it manages the liquidity risk inherent in the maturity analysis of financial liabilities required in paragraph 39(a). The factors that the entity might consider in providing this disclosure include, but are not limited to, whether the entity:

(a) expects some of its liabilities to be paid later than the earliest date on which the entity can be required to pay (as may be the case for customer deposits placed with a bank);

(b) expects some of its undrawn loan commitments not to be drawn;

(c) holds financial assets for which there is a liquid market and that are readily saleable to meet liquidity needs;

(d) has committed borrowing facilities (eg commercial paper facilities) or other lines of credit (eg stand-by credit facilities) that it can access to meet liquidity needs;

(e) holds financial assets for which there is not a liquid market, but which are expected to generate cash inflows (principal or interest) that will be available to meet cash outflows on liabilities;

(f) holds deposits at central banks to meet liquidity needs;

(g) has very diverse funding sources; or

(h) has significant concentrations of liquidity risk in either its assets or its funding sources.

Market risk (paragraphs 40–42 and B17–B28)

IG32 Paragraph 40(a) requires a sensitivity analysis for each type of market risk to which the entity is exposed. There are three types of market risk: interest rate risk, currency risk and other price risk. Other price risk may include risks such as equity price risk, commodity price risk, prepayment risk (ie the risk that one party to a financial asset will incur a financial loss because the other party repays earlier or later than expected), and residual value risk (eg a lessor of motor cars that writes residual value guarantees is exposed to residual value risk). Risk variables that are relevant to disclosing market risk include, but are not limited to:

(a) the yield curve of market interest rates. It may be necessary to consider both parallel and non-parallel shifts in the yield curve.

(b) foreign exchange rates.

(c) prices of equity instruments.

(d) market prices of commodities.

IG33 Paragraph 40(a) requires the sensitivity analysis to show the effect on profit or loss and equity of reasonably possible changes in the relevant risk variable. For example, relevant risk variables might include:

(a) prevailing market interest rates, for interest-sensitive financial instruments such as a variable-rate loan; or

(b) currency rates and interest rates, for foreign currency financial instruments such as foreign currency bonds.

IG34 For interest rate risk, the sensitivity analysis might show separately the effect of a change in market interest rates on:

(a) interest income and expense;

(b) other line items of the statement of profit and loss (such as trading gains and losses); and

(c) when applicable, equity.

An entity might disclose a sensitivity analysis for interest rate risk for each currency in which the entity has material exposures to interest rate risk.

IG35 Because the factors affecting market risk vary depending on the specific circumstances of each entity, the appropriate range to be considered in providing a sensitivity analysis of market risk varies for each entity and for each type of market risk.

IG36 The following example illustrates the application of the disclosure requirement in paragraph 40(a):

Interest rate risk

At 31 December 20X2, if interest rates at that date had been 10 basis points lower with all other variables held constant, post-tax profit for the year would have been Rs. 1.7 crore (20X1—Rs. 2.4 crore) higher, arising mainly as a result of lower interest expense on variable borrowings, and other components of equity would have been Rs. 2.8 crore (20X1—Rs. 3.2 crore) higher, arising mainly as a result of an increase in the fair value of fixed rate financial assets classified as available for sale. If interest rates had been 10 basis points higher, with all other variables held constant, post-tax profit would have been Rs. 1.5 crore (20X1—Rs. 2.1 crore) lower, arising mainly as a result of higher interest expense on variable borrowings, and other components of equity would have been Rs. 3.0 crore (20X1—Rs. 3.4 crore) lower, arising mainly as a result of a decrease in the fair value of fixed rate financial assets classified as available for sale. Profit is more sensitive to interest rate decreases than increases because of borrowings with capped interest rates. The sensitivity is lower in 20X2 than in 20X1 because of a reduction in outstanding borrowings that has occurred as the entity's debt has matured (see note X)[a]

Foreign currency exchange rate risk

At 31 December 20X2, if the Rupee had weakened 10 per cent against the US dollar with all other variables held constant, post-tax profit for the year would have been Rs. 2.8 crore (20X1—Rs. 6.4 crore) lower, and other components of equity would have been Rs. 1.2 crore (20X1—Rs. 1.1 crore) higher. Conversely, if the Rupee had strengthened 10 per cent against the US dollar with all other variables held constant, post-tax profit would have been Rs. 2.8 crore (20X1—Rs. 6.4 crore) higher, and other components of equity would have been Rs. 1.2 crore (20X1—Rs. 1.1 crore) lower. The lower foreign currency exchange rate sensitivity in profit in 20X2 compared with 20X1 is attributable to a reduction in foreign currency denominated debt. Equity is more sensitive in 20X2 than in 20X1 because of the increased use of hedges of foreign currency purchases, offset by the reduction in foreign currency debt.

(a) Paragraph 39(a) requires disclosure of a maturity analysis of liabilities.

Other market risk disclosures (paragraph 42)

IG37 Paragraph 42 requires the disclosure of additional information when the sensitivity analysis disclosed is unrepresentative of a risk inherent in a financial instrument. For example, this can occur when:

(a) a financial instrument contains terms and conditions whose effects are not apparent from the sensitivity analysis, eg options that remain out of (or in) the money for the chosen change in the risk variable;

(b) financial assets are illiquid, eg when there is a low volume of transactions in similar assets and an entity finds it difficult to find a counterparty; or

(c) an entity has a large holding of a financial asset that, if sold in its entirety, would be sold at a discount or premium to the quoted market price for a smaller holding.

IG38 In the situation in paragraph IG37(a), additional disclosure might include:

(a) the terms and conditions of the financial instrument (eg the options);

(b) the effect on profit or loss if the term or condition were met (i.e. if the options were exercised); and

(c) a description of how the risk is hedged.

For example, an entity may acquire a zero-cost interest rate collar that includes an out-of-the-money leveraged written option (eg the entity pays ten times the amount of the difference between a specified interest rate floor and the current market interest rate). The entity may regard the collar as an inexpensive economic hedge against a reasonably possible increase in interest rates. However, an unexpectedly large decrease in interest rates might trigger payments under the written option that, because of the leverage, might be significantly larger than the benefit of lower interest rates. Neither the fair value of the collar nor a sensitivity analysis based on reasonably possible changes in market variables would indicate this exposure. In this case, the entity might provide the additional information described above.

IG39 In the situation described in paragraph IG37(b), additional disclosure might include the reasons for the lack of liquidity and how the entity hedges the risk.

IG40 In the situation described in paragraph IG37(c), additional disclosure might include:

(a) the nature of the security (eg entity name);

(b) the extent of holding (eg 15 per cent of the issued shares);

(c) the effect on profit or loss; and

(d) how the entity hedges the risk.