



cutting through complexity™

Accounting for bonds

Bond Training Workshop for Accountants and Insurance Companies

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Learning objectives

At the end of this course,
you will:

- 1) Understand the accounting requirements under SAS
- 2) Understand the accounting requirement under IFRS.

Agenda

Definitions

Accounting treatment under SAS

Classification and measurement under IFRS

Definitions – Bonds

Debt instrument issued for a period of more than one year with the purpose of raising capital by borrowing.

Usually issued by the government (federal, state or local government), corporations, and other institutions.



They are tradable instruments and can be held until redemption.

Can be classified as long term or short term depending on the intention of the holder of the instrument.

Agenda

Definitions

Accounting treatment under SAS

Classification and measurement under IFRS

Classification

Bonds



Classification under SAS (13)

Long term
investments

Tenure > 12 months
and held to maturity

Short term
investments

if held for trading or
Tenure < 12 months

Investment
properties

Measurement

Long term investment should be stated at cost or revalued amounts

SAS 13 40

Short term investments should be stated at lower of costs and net realisable value

SAS 13 37

Discount or premium amortised over the period to maturity. Amortised premium or discount is credited or charged to profit and loss.

SAS 13 24

Agenda

Definitions

Accounting treatment under SAS

Classification and measurement under IFRS

Definitions – Financial Instruments- IAS 39

A financial instrument is a contract that gives rise to:

- a financial asset of one entity and
- a financial liability or equity instrument of another entity

Financial asset	Financial liability	Equity instrument
<ul style="list-style-type: none"> ◆ Cash ◆ Equity instrument of another entity ◆ Contractual right to receive cash or another financial asset (for example, loans and receivables) or to exchange financial assets or liabilities under potentially favourable conditions ◆ Certain contracts settled in the entity's own equity 	<ul style="list-style-type: none"> ◆ Contractual obligation to deliver cash (for example, accounts payable) or another financial asset or to exchange financial asset or liabilities under potentially unfavourable conditions ◆ Certain contracts settled in the entity's own equity ◆ Except for certain puttable financial instruments and obligations arising only upon an entity's liquidation 	<ul style="list-style-type: none"> ◆ Contract evidencing a residual interest in the assets of an entity after deducting all of its liabilities

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.

Amortised cost is initial recognition - repayments of principal - impairment or uncollectibility +/- cumulative amortisation of the difference between the initial amount and the maturity amount.

Effective Interest rate is the rate that exactly discounts the cash flows associated with an instrument to the net carrying amount at initial recognition.

Classification under IFRS

Bonds



Classification of financial instruments under IFRS

At fair value
through
profit or loss

Held to
maturity

Loans and
receivables

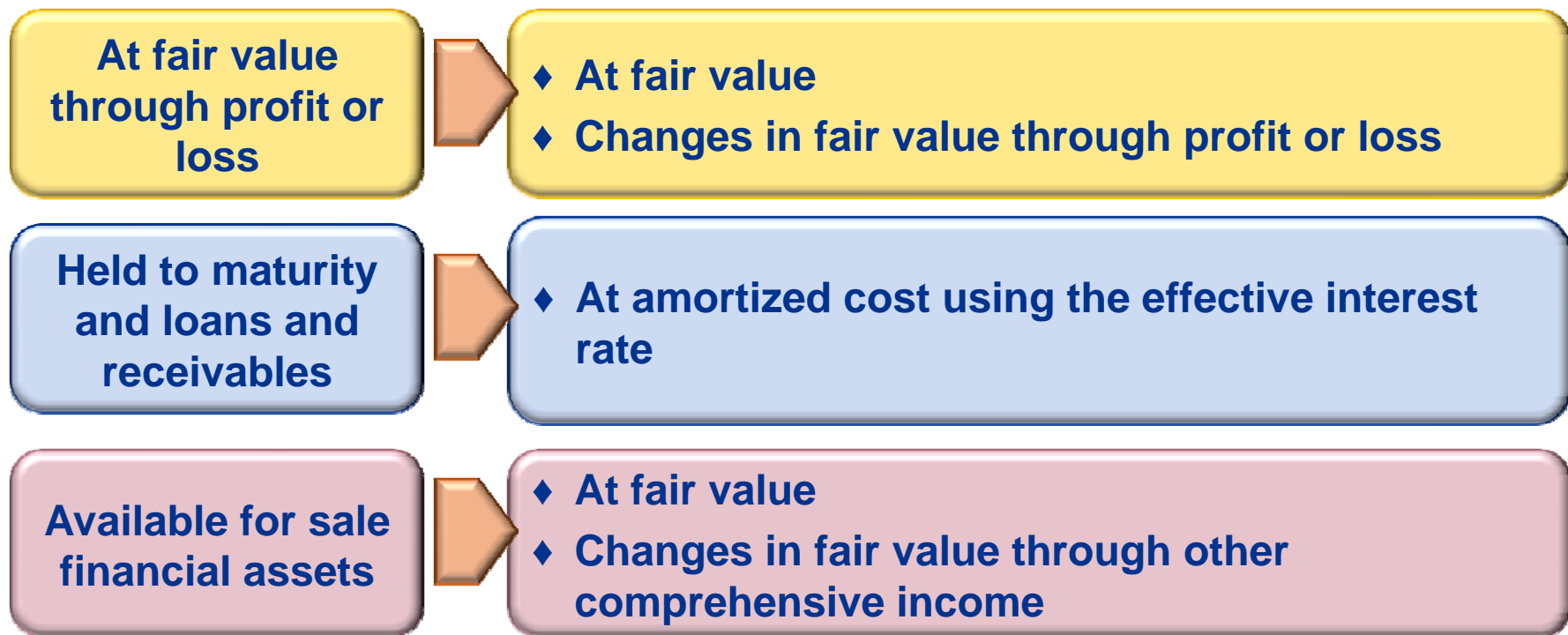
Available for
sale
financial
assets

Categories of financial assets

Category	Definition
Financial assets at fair value through profit or loss	<ul style="list-style-type: none">• Financial assets held for trading• Derivatives, unless accounted for as a hedging instrument
Loans and receivables	Non-derivative financial assets with fixed or determinable payments that are not quoted in an active market
Held-to-maturity investments	Non-derivative financial assets with fixed or determinable payments and fixed maturity that the entity has the positive intent and ability to hold to maturity.
Available-for-sale financial assets	<ul style="list-style-type: none">• All financial assets that are not classified in another category are classified as available-for-sale• Any financial asset designated to this category on initial recognition

Initial recognition and subsequent measurement

Measured at fair value on initial recognition.
Transaction costs are included in the determination of fair value.



Amortised costs measurement



Measurement Amortised costs – EIR and a Discount

Government bond at coupon rate of 19% over 2 years

Tenure	2	years
Present Value	(1,450,000)	
Discount	50,000	
Interest Payments	285,000	(19% on face value)
Future value	1,500,000	
Effective interest rate	21.21%	

Date	Opening balance	Accounting interest at effective interest rate (21.21%)	Cash flow at contractual interest rate (19%)	Closing balance
31-Dec-05	(1,450,000)	307,603	285,000	(1,472,603)
31-Dec-06	(1,472,603)	312,397	285,000	(1,500,000)
31-Dec-06	(1,500,000)		1,500,000	-

Measurement Amortised costs – EIR and Premium

Government bond at coupon rate of 19% over 2 years

Tenure	2(2 years)
Present Value	(1,600,000)
Discount	(100,000)
Interest Payments	285,000 (19% on face value)
Future value	1,500,000

Effective interest rate 14.90%

Date	Opening balance	Accounting interest at effective interest rate (14.90%)	Cash flow at contractual interest rate (19%)	Closing balance
31-Dec-05	(1,600,000)	238,468	285,000	(1,553,468)
31-Dec-06	(1,553,468)	231,532	285,000	(1,500,000)
31-Dec-06	(1,500,000)		1,500,000	-

Impairment

A financial asset or a group of financial assets is impaired if, and only if:

- **there is objective evidence of impairment as a result of one or more events that occurred after initial recognition; and**
- **the loss event has an impact on estimated future cash flows**

An impairment loss is measured as the difference between:

- **the asset's carrying amount and the present value of estimated future cash flows - for loans and receivables or held-to-maturity investments; and**
- **the net carrying value (acquisition cost net of any principal repayment and amortisation) and current fair value-For Available for sale investments.**

Impairment

Indicators of impairment for debt securities (financial assets recognised at amortised cost)

- Significant financial difficulty of the issuer
- Bankruptcy or financial reorganisation of the issuer
- Disappearance of an active market for the bonds concerned
- Measurable decrease in the estimated future cash flows

Impairment

Classification	Impairment	Reversal of impairment
Trading	Adjusted through fair value changes	Adjusted through fair value changes
Available for sale, Held to maturity instruments and loans and receivables.	Recognised in income statements	Can be reversed through income statements if the increase can be objectively related to an event occurring after the loss was recognised

Agenda

Definitions

Accounting treatment under SAS

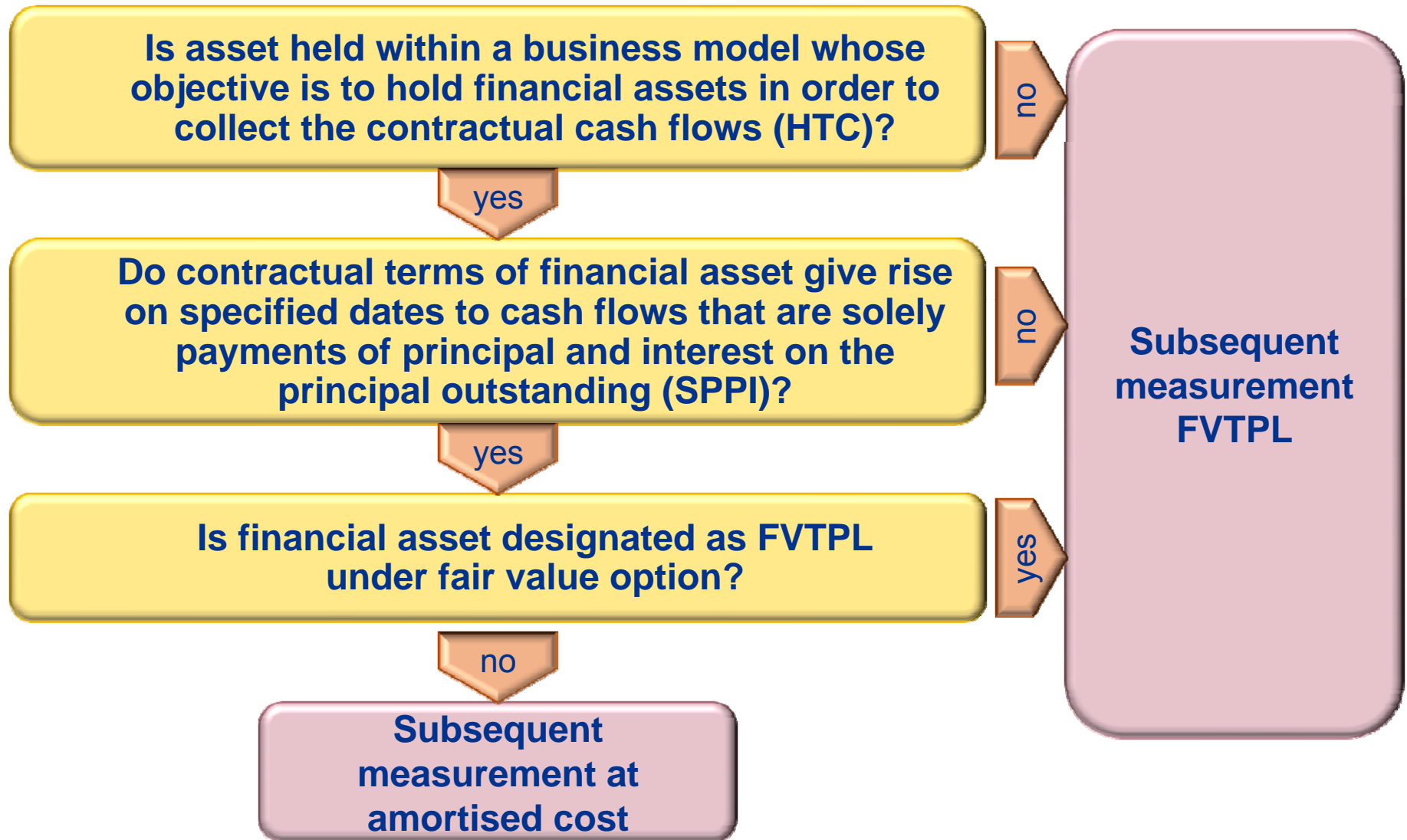
Classification and measurement under IFRS

Accounting under IFRS 9

Initially measured at fair value and;

subsequently valued at amortised cost or at fair value through profit or loss depending on the business model and characteristics of the contractual cash flows

Accounting under IFRS 9



Fair value option: Financial assets

Does designation as FVTPL eliminate or significantly reduce a measurement or recognition inconsistency (accounting mismatch)?

yes

FV option may be applied at initial recognition and is irrevocable

No

FV option prohibited

FVTOCI option: Investments in equity instruments

No option to value bonds at fair value through other comprehensive income anymore



- 1) Under SAS, bonds may be classified as either short term investments or long term investments
- 2) Under IFRS, bonds may be classified into any of the 4 categories of financial assets
- 3) Under IFRS 9, bonds are classified as measured at amortised cost except when they are designated as measured at FVTPL
- 4) Subsequent measurement of bonds will depend on the initial classification.

Thank you

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